CRA: Build Your Own Tax-Free Pension

Description

Everyone wants a tax-free pension. The Canada Revenue Agency has made that dream a reality. That's right; you can get a permanent income stream without ever paying a cent in taxes.

It's actually quite simple, but don't mistake simple for easy. Taking advantage of this opportunity takes good habits, but, most importantly, it takes time. There is no substitute for the power of compound interest, which only plays out over a period of many years.

Want to have your own tax-free pension? Here's how.

Ditch the taxes

The first step is to ensure you'll never pay taxes again. The CRA makes that possible with a TFSA. Many Canadians know that TFSAs are powerful, but the magic is in the details.

The most obvious advantage is that your capital grows tax free as long as it stays within a TFSA. But the protections continue even upon withdrawal. A $1,000 deposit can grow into $1 million, and you get to keep the entire sum!

Unlike other retirement vehicles, TFSA withdrawals can occur at any time, for any reason. So, when it comes time to receive your tax-free pension money, you can make regular withdrawals for decades at a time without penalty. This really is the best investing move Canadians can make.

Of course, to withdraw money from a TFSA, there needs to be capital there in the first place. There's no getting around the need to save money, but there is one simple trick that can guarantee you hit you investing goals.

Build your empire

Dollar-cost averaging is an incredible tool. It involves buying a fixed dollar amount of a particular investment on a regular schedule.

Let’s assume you invest $100 every week. If a stock is worth $10 per share, you’ll purchase 10 shares. If shares drop to $5, you’ll buy 20 shares. If shares rise to $20, you’ll purchase five shares.

You can easily see what’s happening here. When markets fall — the time you should be buying more stock — dollar-cost averaging *automatically* makes you purchase more. When valuations rise, you buy fewer shares.

Over time, dollar-cost averaging can attain incredible results. For example, assume you save $100 per week and earn a 10% annual return. After one year, you’ll have $5,500. After a decade, you’ll have $100,000. In just three decades, you’ll wind up with a cool $1 million.

If you’d invested through a TFSA, you’ll pay nothing in taxes, meaning you can keep the entire $1 million. At that point, you can stop saving altogether and begin your withdrawals. You should be able to withdraw $100,000 per year for the rest of your life — tax free!

Pick your stocks

There is no magic wand to create your own tax-free pension. You need to diligently save over the long term, harnessing the power of compound interest. Investing through a TFSA means you’ll accrue capital faster, allowing you to cut *years* off your time horizon.

The only thing missing is a portfolio of stocks to invest all this capital in. There are plenty of options, but be sure to only pick companies that can compound your capital for decades to come.

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Date
2025/08/28
Date Created
2020/08/03
Author
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