Canada Revenue Agency: 2 TFSA Mistakes That Could Cost You Money

Description

The Tax-Free Savings Account (TFSA) is nothing short of a blessing for Canadian families. The investment vehicle was designed to encourage Canadians to save more money, but it can help you do so much more.

You can use the account type to grow your savings, amass a retirement nest egg, and even use it to generate passive income. The best thing about it is the tax advantages that it offers. Any money or assets you store in the account can grow tax-free. Additionally, you can withdraw money from the account without incurring any charges or tax penalties.

With all its tax advantages, there are aspects of the account that people forget. I will discuss two costly mistakes that Canadians make with the TFSAs that can keep them from fully benefiting from the account.

Overcontributing

There is a contribution limit to the TFSA that the Canada Revenue Agency (CRA) keeps increasing each year. After the latest update, the contribution limit stands at $69,500. It means that if you have not invested in a TFSA since the account type's inception, you can contribute a total of $69,500 to your TFSA.

One third of Canadians make the mistake of not understanding their TFSA contribution limit, which could lead to them contributing too much to their accounts. Exceeding the contribution limit entails tax penalties that the CRA will happily collect. The CRA will tax you for all the excess amount in your TFSA until you reduce it within the contribution limit.

Not investing your cash

Another TFSA mistake Canadians make is that they use the account to hold cash. While you can get returns from interest on the cash you store in your TFSA, it is a waste of the contribution room and tax advantages. You can get better tax-free returns for the contribution limit if you use it to invest in other assets equivalent to the contribution amount.

Investing in a reliable dividend-paying stock like **Fortis Inc.** (TSX:FTS)(NYSE:FTS) could help you make better use of the account. You can buy shares of the company, store them in your TFSA and forget it for years. The result will be substantial growth of your TFSA account balance through its capital gains and dividend payouts.

Fortis owns and operates utility assets across Canada, the U.S., and in the Caribbean. Since Fortis provides its customers with an essential service, the company can continue generating a stable and predictable cash flow. No matter how bad the economy gets, Fortis can continue creating the cash flow to fund its juicy dividends and fuel its growth.

At writing, Fortis is trading for $53.92 per share and has a 3.75% dividend yield. Investing in the stock and storing it in your TFSA can provide you with far better returns than holding cash.

Foolish takeaway

Avoiding TFSA mistakes can help you improve your financial situation. It can provide you with short-term benefits like passive income and long-term benefits, like creating a retirement fund of your own. Stocks like Fortis could become a valuable foundation in your investment portfolio, regardless of how you choose to use your TFSA.

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Author
adamothman