Canada Revenue Agency: Stop Overcontributing to Your TFSA!

Description

The Tax-Free Savings Account (TFSA) was introduced as a blessing for Canadian families by the government in 2009. The account can let you enjoy tax benefits that can help you accumulate significant wealth without paying the Canada Revenue Agency (CRA) a single penny on your income in the account.

However, the CRA will keep a close eye on your account to catch you if you make any mistakes. The TFSA can let you enjoy tax-free wealth growth. Still, it comes with certain rules and regulations you need to comply with to enjoy the tax-free status. Failing to comply will allow the CRA a chance to come collecting their due, which they will gladly do.

Stop over-contributing

Canadians make the mistake of disregarding the maximum contribution limit in their TFSAs. Since the account was introduced, the government introduced a limit to which you can contribute to your TFSA each year. The government increases the contribution limit annually.

With the 2020 update, the maximum contribution limit for your TFSA is $69,500. It means that if you have never invested in a TFSA since its inception, you can contribute $69,500 in cash or equivalent assets to the account.

Unfortunately, Canadians make the mistake of contributing a lot more to their TFSAs than they should. The CRA charges you a penalty of 1% on the excess amount you hold in your TFSA each month. You can effectively lose the tax-free status of your account by making this mistake.

Don’t trade too much in the account

Another mistake you never want to make with your TFSA is using it as a day-trading account. Yes, you can use the TFSA to hold assets equivalent to $69,500. However, you can’t use the tax-free status of your TFSA to make trades for the short-term. If you plan on using the account for day trading, you can expect the CRA to take action.

The CRA can consider any account frequently trading stocks to have taxable business income.

Long-term investment to consider

There is no definitive limit to how many trades you can make in your TFSA in a year, but you should not act as a day trader with the account. Ideally, you should use the account to buy and hold long-term investments like the **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) stock.

Toronto-Dominion is one of the most ideal long-term bets for Canadian investors. Part of a highly regulated financial sector, TD has been a powerful force in Canada's banking sector for a long time. It enjoys market-leading positions across several banking segments in the domestic market and has substantial international exposure.

The bank stock is trading for $59.75 per share at writing. At its current share price, TD has a very juicy 5.29% dividend yield. A high dividend yield is typically alarming. However, TD's dividend yield is relatively secure due to its wide moat. The pandemic is pressuring the stock and leading to the inflated dividend yield.

Foolish takeaway

TD looks attractive for TFSA investors right now. The stock has a long way to go before it recovers to pre-pandemic prices. Between the potential capital gains and dividend income, Toronto-Dominion can generate significant tax-free wealth in your TFSA.

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