Canada Revenue Agency: Your TFSA Contribution Limit Will Rise in 2021!

Description

2021 is fast approaching, and you know what that means: new TFSA contribution room!

With a new year comes a new opportunity to contribute to your TFSA. As of 2020, the maximum possible contribution room was $69,500. In 2021, that's set to increase. With a $6,000 increase (the same as last year), you'd be up to $75,500 in total. The question is, how much contribution room are you actually going to get?

How much contribution room will you get?

So far, 2021 TFSA contribution room hasn't been announced. However, it's possible to gauge what it's likely to be. Generally, TFSA space is indexed to inflation. It started at $5,000 and has been inching up since then. The amount of space is rounded to the nearest $500, so you don't get the *exact* inflation indexed amount. This is why there have been some abrupt jumps from $5,000 to $5,500 and from $5,500 to $6,000.

According to the personal finance site *Finiki*, TFSA contribution room is based on inflation and rounding. In each year, there's a basic "un-rounded amount" based on the pure inflation calculation — that is, starting amount times one plus the inflation rate. That's then rounded to the nearest increment of $500 to give us the final amount. In 2020, the unrounded amount was $5,959. Assuming 2% inflation, that gets us to an "unrounded amount" of $6,078. That rounds down to $6,000.

So, the TFSA contribution room is likely to remain at $6,000 for 2021. We'd need an "unrounded amount" over $6,250 to get to $6,500. Inflation has been too low this year for that to happen.

Of course, the federal government has the discretion to give Canadians more space if it wants to. In 2015, the outgoing Harper government offered a whopping $10,000, which was not based on the standard calculations. But the point stands. Unless Trudeau gives us a surprise gift, we're getting $6,000.

What to do with your contribution room

If you plan on adding to your TFSA in 2021, there are several great assets you can consider buying.

Dividend stocks like **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) are always great TFSA investments. Dividends create automatic taxable income that the TFSA spares you, so they take advantage of the account's tax saving features well. The same goes for interest-bearing bonds. With capital gains-only stocks, you can avoid taxes by not selling. With dividend stocks like TD, you have to shelter them to avoid taxation. So, if you're going to hold a stock like TD, it pays to hold it in a TFSA.

Next up we have growth stocks like **Shopify** (TSX:SHOP)(NYSE:SHOP). It pays to hold these in a TFSA instead of an RRSP. If you hold a super-hyped-up growth stock like SHOP, there's a good chance you're trying to profit off quick capital gains. SHOP isn't the type of stock people plan to hold for life, but more of a vehicle for high-risk speculation. The TFSA is the best tax-free account for these types of plays. RRSPs aren't good for "quick gains you plan to cash out," because there's a tax penalty on withdrawal. The TFSA doesn't have that, so it's better for speculating on stocks like SHOP.

Finally, we have index funds like **iShares S&P/TSX Capped Composite Fund.** The lowest risk of the investments I've mentioned here, index funds are perfect for beginner investors. With index funds, you get built-in diversification and a complete portfolio right out of the gate. If you're just starting with TFSA investing, such funds are great to get your feet wet.

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TICKERS GLOBAL

1. NYSE:SHOP (Shopify Inc.)
2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:SHOP (Shopify Inc.)
4. TSX:TD (The Toronto-Dominion Bank)

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