Canada Revenue Agency: How Retired Couples Can Earn an Extra $985 Per Month and Protect Against OAS Clawback

Description

The Canada Revenue Agency (CRA) taxes your income when you earn. Even in retirement, it taxes the OAS (Old Age Security) payments under certain conditions. The OAS is Canada's largest pension program and is subject to CRA taxes, which is also known as a clawback.

This means Canadian retirees who receive the OAS payouts might have to see if this clawback can be avoided or reduced.

What is the OAS clawback?

The Canada Revenue Agency levies a clawback on your OAS if your net world income exceeds the $79,054 threshold for the 2020 tax year. The maximum income threshold is $128,149, after which the entire OAS payment will be taxed.

The CRA taxes each dollar earned above the minimum threshold limit at a rate of 15%. So, if Judy is a retiree with a net income of $90,000 in 2020, the OAS clawback will be imposed on $10,946 ($90,000-$79,054), which means total taxes will be $1,641.9 (15% of $10,946).

The clawback amount will increase to $3,141.9 if Judy's net income rises to $100,000, and the clawback will be $7,364.25 for retirees with a net income of $128,149.

If the CRA taxes your OAS, it means you are generating robust income, even in retirement. While it's a good problem to have, Canadians should always look to lower their tax liabilities, even more so during retirement.

Any income that you earn is subject to taxes by the Canada Revenue Agency, which puts retirees in a high marginal tax bracket. It means the amount left over after you account for taxes and expenses will decline significantly.

The Canada Revenue Agency cannot tax income from your TFSA

Any income that you earn under the Tax-Free Savings Account is not subject to taxes from the Canada Revenue Agency. This makes it an ideal account for retirees where they can hold blue-chip dividend-paying stocks.

The TFSA was introduced back in 2009 and the cumulative contribution limit for this registered account is $75,500 at the start of 2021. For retired couples, the maximum TFSA contribution limit doubles to $151,000.

Dividend-paying stocks will help you generate a steady source of recurring income. While interest rates are hovering below 2%, stocks such as **Enbridge** (TSX:ENB)(NYSE:ENB) are extremely attractive to income investors.

Enbridge stock has a forward yield of 7.82%, which means a $151,000 investment will help you generate $11,850 in annual dividends, indicating a monthly payout of $987.

Enbridge is a diversified energy giant with a solid business model. Canada's midstream heavyweight derives over 90% of its EBITDA from long-term or regulated contracts. So, Enbridge generates stable cash flows across business cycles and is relatively immune to volatile commodity prices.

In the last 25 years, Enbridge has increased dividend payments at an enviable rate of 11% annually. So, if you invested $10,000 in Enbridge stock at the start of 1995, you would have returned $192,310 today after accounting for dividend reinvestments. If you did not reinvest dividends, your investment would have ballooned to $104,000.

The Foolish takeaway

Enbridge is just an example of a top Canadian dividend-paying company. While it does not make financial sense to allocate $150,000 in a single stock, you can use this article as a starting point for your research and identify similar dividend stocks for your TFSA.

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