Beware! 1 Tricky Way the CRA Will Tax Your $6,000 TFSA

Description

U.S. equities rose to all-time highs on January 7, 2021, following the confirmation of Joe Biden by Congress as the new President. All three major indexes eventually finished the first week of the year at record levels. The **Nasdaq Composite Index** breached 13,000 for the first time after posting four straight weeks of gains.

Tech heavyweights **Apple**, **Alphabet**, and **Microsoft**, were among the top gainers. News that president-elect Biden will introduce more financial aid to Americans help propped the stock market. The December U.S. jobs report, the worst since April 2020, didn't dampen investors in Canada.

Many Tax-Free Saving Account (TFSA) users in Canada might be thinking of using their new $6,000 TFSA contribution limit in 2021 to purchase high-yield U.S. dividend stocks. However, please don't do it unless you know the rules and the tax implications.

Withholding tax on foreign dividends

The CRA allows TSFA contributions in foreign funds, although the tax agency will convert the value first to Canadian dollars. The resulting value will be the basis to compute the TFSA contribution amount. Should the exchange rate calculation exceed the available contribution, the CRA will deem it as over-contribution and levy a 1% penalty tax on the excess amount.

Foreign stocks are eligible investments, too, as long as the chosen stock belongs to the CRA's approved list of designated exchanges. If you insist on investing in dividend stocks outside Canada, you will lose the tax advantage in your TFSA. Dividend income from a foreign country is subject to a 15% withholding tax.

Penalty tax on non-qualifying investments

The CRA also charges a penalty if a TFSA user holds a non-qualifying investment in the account. If your foreign stock is delisted then moves to over-the-counter (OTC), it automatically becomes a nonqualified investment. Publicly-listed Canadian companies can also move to the OTC, although the CRA could still consider them a qualified TFSA investment.

Holding a non-qualifying investment in your TFSA is costly, if not expensive. The CRA will charge you a one-time penalty tax equivalent to 50% of the investment's fair market value at the purchase date.

Best-in-class TFSA investment

The **Toronto Stock Exchan**ge (TSX) has performed pretty well in recovering the mid-March 2020 market crash losses. Likewise, Canada's primary stock market finished at an all-time high of 18,042.10 on January 8, 2021. **Enbridge** (TSX:ENB)(NYSE:ENB) is the hands-down choice if you're looking for a high-yield, dependable dividend stock.

This top-tier energy stock trades in both the Canadian and American stock exchanges. While Enbridge's total return in 2020 was -15%, investors enjoyed a lucrative 7.88% dividend. Your $6,000 TFSA contribution will generate $472.80 in tax-free income. The energy sector suffered a beating from the crisis, but it doesn't mean that Enbridge is a risky investment choice.

The $85.83 billion energy infrastructure company is a Dividend Aristocrat. Enbridge has raised its dividends for 25 consecutive years. Furthermore, it stands above the rest in the sector because it functions more like a utility stock. It generates stable cash flows from fee-based contracts.

Make the wise move

In conclusion, it makes no sense for TFSA users to risk paying taxes because the preference is in foreign stocks. You can purchase Enbridge at 42.38 per share today and never sell again. Your tax-free income could be for life

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