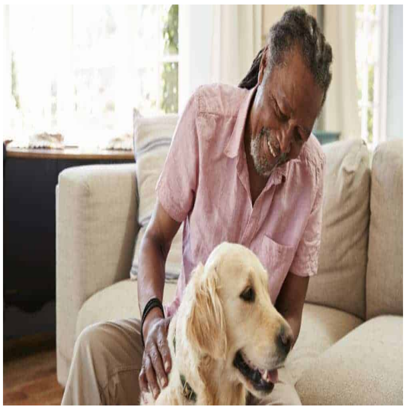

Canada Revenue Agency: Earn an Extra $400 a Month and Avoid the 15% OAS Clawback

Description

Every Canadian is encouraged to save for retirement. The RRSP was created for the sole purpose of giving Canadians a tax-sheltered environment where they could grow the savings for their retirement. And to encourage people to save as much as they can, the government also made the RRSP contributions tax deductible.

But not everyone has the means (or the financial discipline) to put away a significant sum for their retirement every year. Also, not every individual has the same investment opportunities or knowledge to grow their savings at a considerable pace. To create a dependable retirement income stream, the CPP and OAS were created. But the OAS comes with a stipulation.

Don't earn too much

The OAS clawback "rationale" can be summed up quite simply in just four words: "Don't earn too much." If your taxable income for 2021 exceeds $79,845, you'll need to pay a recovery tax (at a rate of 15%) on every dollar that exceeds that amount. Let's say a person's net income is $84,000 in 2021 as a retiree. Their income would be $4,155 over the minimum OAS recovery threshold.

They would pay a little over $623 (15% of the excess amount) to the CRA in an OAS clawback. The reasoning behind it seems to be that the government-funded pension should first go to those most in need (with net income below the thresholds). Thankfully, there are ways to avoid this clawback, and one of them involves the other tax-sheltered account: the TFSA.

Adjust your taxable income with a TFSA

Let's say you are likely to earn a net income of $84,000 for 2021, and you want to avoid the OAS recovery tax. The simplest solution is to reduce your taxable income by relying on your TFSA. If the amount above the OAS threshold comes out of your TFSA, you can have the same net income without paying back a single OAS dollar to the CRA.

One simple way to do it would be to start a dividend-based income stream from your TFSA. If you invest $70,000 from your fully stocked TFSA into two high-yield Aristocrats, **Enbridge** and **Canadian Imperial Bank of Commerce**, with an aggregated yield of 6.85%, you'd earn about $4,795 a year in dividends. That's about $400 a month, which can augment your other retirement income.

Enbridge is an established energy leader, and even though the sector is going through some troubled times, this long-standing Aristocrat might pull through and keep growing its payouts. CIBC is one of the Big Five and enjoys the stability of the Canadian banking sector. A stable payout ratio backs its juicy yield.

Foolish takeaway

It might not be prudent to keep all your TFSA eggs in two baskets, and you may consider diversifying your funds into more assets. You can either add more high-yield assets to grow your tax-free monthly income or choose some growth stocks for capital gains. In any case, a sizeable TFSA income means that you need to rely less on taxable RRIF payouts.

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