Canada Revenue Agency: If You Did This 1 Thing Wrong, Your TFSA Will Get Taxed!

Description

The Tax-Free Savings Account (TFSA) is very popular, because it enables Canadians to earn money tax-free. It's also the perfect hedge against inflation and a tool for retirees to avoid the notorious 15% Old Age Security (OAS) clawback. However, the unique features of the investment vehicle can be a temptation at times.

Since TFSA balances accelerate faster without tax implications, some users tend to abuse the utilization. If you think you can be a trader using your TFSA, be extra careful. The Canada Revenue Agency (CRA) will not tolerate wayward behaviours that undermine the purpose of a TFSA. You'd lose your tax-free benefit if you did one thing wrong.

Excessive trading

First and foremost, the TFSA is a savings vehicle for average Canadians. A user must stick to the annual contribution limits and not overcontribute to avoid the 1% penalty tax per month. However, frequent or excessive trading is an unforgivable error.

You risk the ire of the CRA if you insist on carrying a full-time stock trading business to earn profits at every turn. The tax agency prohibits such practice and conducts random audits to identify professional or day traders. Usually, the CRA flags active traders that are buying and selling stocks inside the TFSA.

Severe consequences

The frequency of trading raises alarm bells, and the CRA will flag an account suspected of carrying a business. In a TFSA, higher-frequency trading often indicates business income. You should be earning investment income, not business income, inside your TFSA.

If the CRA discovers that you're using your TFSA to generate business income, the consequences are severe. Your efforts will be for naught as the tax agency will treat your business income as regular income and, therefore, is taxable. Everything will be taxed accordingly.

Generally, a TFSA user holds eligible investments in the account for the long haul. Your TFSA will appear on the CRA's radar when there's a disproportionate amount of trading activity.

Profitable investment option

North West Company (TSX:NWC) is a profitable investment prospect if you plan to maximize your $6,000 TFSA contribution limit in 2021. The $1.58 billion grocer in hard-to-reach regions pays a hefty 4.46% dividend. This consumer-defensive stock rewarded investors with a nearly 25% gain in 2020.

This leading retailer of food and everyday products and services enjoys the lion's share of the markets in rural communities and urban neighborhoods in Canada, Alaska, the South Pacific, and the Caribbean. There's no doubt that the near-monopoly business of North West will see continuous strong sales in the years ahead.

The impressive 44% growth in net earnings in Q3 2020 versus Q3 2019 proves North West's resiliency and stability during economic downturns. Analysts' growth estimate is 13.5% annually in the next five years. They also forecast the stock price to climb by 17.3% to $38 in the next 12 months.

The CRA is watching

A TFSA is a one-of-a-kind investment vehicle. Users must use the account correctly and not stray away from its intended purpose. Furthermore, the CRA is watching and running after speculators wishing to earn quick bucks. Don't attempt to be one or else you'll lose the tax-free and tax-shelter benefits altogether.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:NWC (The North West Company Inc.)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
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