2 Massive TFSA Mistakes to Avoid in 2021

Description

The Registered Retirement Savings Plan (RRSP) has been the staple of Canadians saving for retirement. However, the RRSP is now second only to the Tax-Free Savings Account (TFSA) as the preferred investment vehicle. If people could contribute to only one, the money will likely go into a TFSA.

A TFSA is excellent to save money for short-term financial goals. If you have a long-term horizon, the account is the best there is to build retirement wealth. All capital gains and dividends are tax-free. However, some users don't derive the full tax-free benefits due to massive and costly mistakes.

1. Don't belittle your TFSA

The term *savings* is perhaps why account holders mistake their TFSAs for an ordinary savings account. A **Bank of Montreal** survey reveals that users are underutilizing the account. On average, cash is the primary investment of 38% of the poll respondents. A TFSA can hold cash and other assets such as stocks, bonds, GICs, ETFs, and mutual funds.

The federal government introduced the TFSA in 2009 to encourage and help Canadians save and invest for the future. Hence, the contributions must work for the users. It means, therefore, the assets inside a TFSA should be income producing, not idle cash. Since money growth is tax-free, your balance will accumulate faster.

2. Don't overcontribute

The Canada Revenue Agency (CRA) sets the annual contribution limit every year, so users have ample room to save at the beginning of each year. Since its inception in 2009, the TFSA cumulative contribution is now $75,500 in 2021. Unused contribution rooms carry over to the next year or indefinitely until you can use them or contribute again. However, the CRA is strict with its overcontribution rule.

It would be best if you did not go over the limit or else incur a penalty of 1% of the excess contribution every month. Monitor your available contribution room to avoid the needless penalty tax. Be mindful that if you withdraw after maxing out the limit, you can only recontribute the amount in the next calendar.

Key TFSA partner

High-yield dividend stocks are ideal investments in a TFSA, although sometimes they are risky. Be cautious and understand the nature of the business. **Keyera** (TSX:KEY) in the energy sector pays a lucrative 7.37% dividend. Your $6,000 will generate $442.20 in tax-free income. Assuming you're a new user with $75,500 available room, the windfall is $5,564.35.

Keyera underperformed in 2020, with its -27.3% total return. However, there was no dividend cut. Over the last five years, the dividend-growth rate is 8.9%. The company expects to earn an annual return on capital of 10% to15% in 2022. The $5.76 billion energy infrastructure company is a vital cog in North America's oil and gas midstream industry. It owns and operates raw gas gathering pipelines and processing plants.

While some industry peers disapprove, Keyera welcomes the federal government's plan to hike carbon prices to $170 per tonne by 2030. Management is confident the company will do better with the hike and a clean fuel standard to reduce fuel emissions.

More awesome features

Besides earning and saving taxes simultaneously, TFSA users can withdraw any amount at any time without paying penalties. Furthermore, maximizing your TFSA won't affect income-tested government benefits. TFSA withdrawals don't count as taxable income.

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2. Energy Stocks
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