3 Huge TFSA Mistakes to Avoid If You Don't Want to Pay Taxes to the CRA

Description

Some Tax-Free Savings Account (TFSA) users might not know that there's a TFSA return. In most TFSA situations, you don't incur tax payables whatsoever. However, the Canada Revenue Agency (CRA) requires users to file a TFSA return by June 30 of every year in certain circumstances.

TFSA contributions are not deductible for income tax purposes. However, your contributions and all interest, capital gains, and investment income earned in the account are generally tax-free. Even withdrawals, regardless of amount, are not subject to tax.

The advice to users is not to commit three mistakes that would lead to one or more taxes with respect to a TFSA. All are costly blunders. Hence, it's always the user's lookout to be free of the CRA.

1. Over-contribution

The CRA set annual TFSA limits, and the rule is crystal clear. Don't over-contribute. If you do, the penalty tax is 1% of the excess contribution per month. The contribution limit for 2021 is $6,000. You can't go beyond it unless you have an unused contribution room from 2020. The sum of both becomes the available contribution room.

2. Foreign investments

Since Canada's Income Tax Act no longer imposes a cap on foreign investments in a TFSA, users can diversify to include international stocks. The CRA allows it as long as your chosen stock trades on major stock exchanges. Unfortunately, it's not the best strategy if tax is your concern.

The complication arises when you collect dividends. There's a corresponding 15% withholding tax on foreign dividends. Furthermore, the money isn't recoverable because it's also not deductible on your tax return. You'll not realize the desired income from a high-yield foreign dividend stock.

3. Day trading

Don't toy with the idea to buy and sell stocks in your TFSA to make quick bucks or derive outsized gains. Frequent trading is what day traders do. But the CRA strictly prohibits users from carrying on a business in their TFSAs. If the tax agency catches you during audits, it will treat your income as business income, and therefore, taxable. The CRA sometimes charges violators in court.

Rich enterprising legacy

The **North West Company** (TSX:NWC) trades only on the TSX, but it packs a mean dividend yield. Its business model is likewise recession-resistant and could endure economic downturns. This $1.71 billion multinational grocery and retail company rule in underserved rural communities and urban neighborhood markets.

It operates a near-monopoly in the hard-to-reach areas in Canada. It also caters to customers in Alaska, the South Pacific, and the Caribbean. Management has yet to report the full-year 2020 results, although the showing in Q3 2020 (quarter ended October 31, 2020) was already stellar.

On record, the North West Company is one of the longest continuing retail enterprises in the world. It has built a rich enterprising legacy that dates back to 1668. Besides adapting its product mix to each market, the company has the logistics expertise to move the products.

You can purchase this consumer-defensive stock today at $35.14 per share. With a dividend offer of 4.16%, you can boost your tax-free income.

Pointless expenses

Penalty taxes are pointless expenses, especially in a TFSA. The CRA won't hound users who avoid the three mistakes. Pick the right dividend stock and let your money grow the tax-free way.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

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

PARTNER-FEEDS

1. Business Insider
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Date
2025/08/24
Date Created
2021/03/19
Author
cliew