



4 Huge TFSA Mistakes to Avoid When Investing

Description

Tax-free money growth is the biggest benefit Canadians derive from their [Tax-Free Savings Account \(TFSA\)](#). The Canada Revenue Agency (CRA), the duly appointed administrator, allows qualified investments such as bonds, mutual funds, GICs, ETFs, and stocks in a TFSA.

You can place cash in it, although it's the least-preferred option, because the TFSA isn't an ordinary savings account. Most accountholders use it to meet short-term or [long-term savings goals](#). Since interest, profits, or dividends earned within the account are tax exempt, TFSA balances grow faster.

However, some users overlook the governing rules when investing, resulting in huge mistakes, because you must pay taxes to the CRA or sometimes lose the tax-free benefits.

1. Breaking the cardinal rule

The CRA sets the TFSA contribution limit every year, usually in November. If you contribute more than the limit or go beyond the available contribution room, you break the cardinal rule.

Always keep in mind that an overcontribution amount is subject to a 1% penalty tax per month. You'll receive an "excess amount letter" from the CRA as a reminder. Rectify the mistake by withdrawing the excess amount soon to avoid the penalty tax.

2. Returning a withdrawn amount on the same year

Once you've maxed out your TFSA limit for the year and withdraw an amount, don't return the amount in the same year. It constitutes as overcontribution. Wait for the next calendar year, when the new contribution limit takes effect.

3. Holding foreign assets

The CRA is liberal in that it permits foreign investments in a TFSA. This feature, however, is tricky, because dividend income paid by companies from abroad isn't tax exempt and is subject to a withholding tax.

4. Operating a business

TFSA users can buy and sell stocks, but they can't operate a business of trading them. The CRA conduct audits to check if users are abusing the system. You'll end up paying business income tax and lose your TFSA's tax-free status altogether.

Investor-friendly asset

Bank of Montreal ([TSX:BMO](#))([NYSE:BMO](#)) is perhaps the most [investor-friendly asset](#) you can find to hold in your TFSA. Canada's fourth-largest bank is the first company ever to pay dividends. Its track record is eight years short of 200 years. The practice of sharing a portion of profits with shareholders began in 1829.

BMO currently trades at \$123.53 per share and a steady performer on the TSX in 2021 with its 31.31% year-to-date (YTD) gain. The \$79.96 billion bank pays a 3.36% dividend, while maintaining a less than 50% payout ratio. Based on analysts' forecasts, the price could climb between 8.9% and 21.43% in the next 12 months.

Longest dividend-growth streak

If BMO holds the longest dividend track record, **Canadian Utilities** ([TSX:CU](#)) owns the longest dividend-growth streak. The \$9.87 billion diversified utility company has raised its dividends for 49 consecutive calendars. Only industry peer **Fortis** comes close with 47 years.

Utility stocks hardly fluctuate but displays resiliency most of the time. Thus far, in 2021, investors in Canadian Utilities enjoy a 20.67% YTD gain. The stock's total return in the last 38.88 years is 8.857.52% (12.26% CAGR). You can purchase this dividend stock today at \$36.55 per share to partake of the lucrative 4.89% dividend.

Don't lessen overall returns

Besides tax-free compounding, TFSA users can make tax-free withdrawals anytime without affecting government benefits. However, you lessen overall returns when you commit the above four mistakes.

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2. Dividend Stocks
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