Retired Couples: Earn $7,550 Tax-Free Annually and Avoid the OAS Clawback

Description

Canadian retirees are searching for ways to earn extra income without putting their Old Age Security pension payments at risk of an OAS clawback. Fortunately, pensioners can use their Tax-Free Savings Account (TFSA) to solve the problem.

TFSA advantage

The government created the TFSA in 2009 as an additional tool to help Canadians put some cash aside to hit financial goals. Anyone can benefit from holding investments inside the TFSA, but retirees who receive OAS pensions are the real winners.

The cumulative TFSA contribution room per person is up to $75,500 in 2021. That means a retired couple has as much as $151,000 in total contribution space to hold income-generating investments that produce tax-free earnings. In addition, the CRA does not use the TFSA profits that are earned or removed when it calculates net world income in determining potential OAS pension recovery taxes, otherwise known as the OAS clawback.

Pensioners who have a 2021 net world income that exceeds $79,845 get hit with a 15% OAS pension recovery tax on every dollar above that amount. The OAS clawback continues to the maximum threshold of $129,581, at which point the full OAS pension would be clawed back in the next payment year.

For example, a retiree who has a net world income of $99,845 in the 2021 tax year would see their OAS payments for the period of July 2022 to June 2023 reduced by $3,000. That’s a big hit, especially for someone already facing a tight budget.

Now, you might think that income of around $80,000 is pretty good money in retirement, and that is certainly the case. However, many retirees pay rent or still have mortgages. Food, gasoline, utilities, property taxes, and insurance costs keep rising, and some people have medical and other expenses that can quickly eat up their monthly income.

So, a person with a decent company pension, CPP, and OAS can quickly hit the minimum income threshold for the OAS clawback, even though they might be struggling to cover all their expenses. They would then see part of the OAS pension subjected to the recovery tax if income from investments comes from taxable sources.

Top TFSA income stocks

The best stocks to put in a TFSA income portfolio tend to be ones that pay attractive dividends that grow at a steady pace. Stocks come with risks, so it makes sense to own shares in companies that normally bounce back when the market takes a big hit.

Let's take a look at one top **TSX** dividend stock that might be an interesting pick to start a TFSA income fund today.

TC Energy

TC Energy (TSX:TRP)(NYSE:TRP) owns a vast network of natural gas transmission pipelines and natural gas storage sites in Canada, the United States, and Mexico. Oil pipelines and power generation facilities are also part of the mix.

The company has a steady revenue stream that holds up well during challenging economic times and growth comes from strategic acquisitions and internal development projects. TC Energy's current $21 billion capital program should ensure investors get annual dividend increases of at least 5% in the next few years. The board has raised the payout every year for the past two decades.

The current distribution provided a dividend yield of 5.5%.

The bottom line on avoiding the OAS clawback

The TSX Index is home to many top dividend stocks that pay attractive and growing distributions. Investors can quite easily put together a high-quality TFSA portfolio that would provide an average yield of 5%.

For a retired couple with $151,000 in TFSA contribution room, this would generate $7,550 in annual tax-free dividends that won't put OAS payments at risk of a clawback.

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