3 Ways Your TFSA Can Be Taxed

Description

Besides *savings*, the phrase *tax-free* in Tax-Free Savings Account (TFSA) can be confusing, especially to new accountholders. While you can hold not only cash but other assets like bonds, GICs, ETFs, mutual funds, and stocks, the TFSA isn't entirely free from the Canada Revenue Agency (CRA).

The tax agency can still impose taxes on this one-of-kind investment vehicle if TFSA users violate three essential rules. Follow them strictly, and all your earnings are completely tax-exempt.

1. Overcontribution

The common blunder of TFSA users is going beyond their annual contribution limit or available contribution room. You risk incurring a penalty tax every month (1% of the excess amount) if you overcontribute. The new annual contribution limit in 2022 is $6,000.

If you have an unused contribution room of $1,000 in 2021, your available contribution room next year is $7,000. Remember, whether the overcontribution was accidental or deliberate, you must withdraw the excess amount to avoid the penalty tax.

2. Foreign investments

The CRA allow TFSA investors to hold foreign assets in their accounts. However, income or dividend earned from U.S. stocks, for example, is subject to a 15% withholding tax. The cross-border move is tax-exempt only if you'll hold the stocks in a Registered Retirement Saving (RRSP) or Registered Retirement Income Fund (RRIF).

3. Overly frequent trading

Overly frequent trading or day trading raises alarm bells. TFSA users must refrain from buying and selling stocks in a TFSA for short-term gains. The CRA will treat all your earnings as business income and, therefore, taxable income.

Top picks for TFSA investors

TFSA investors are better off limiting their holdings to Canadian stocks. The top picks for 2022 are **Restaurant Brands International** (TSX:QSR)(NYSE:QSR) and **National Bank of Canada** (TSX:NA).

RBI, one of the world's largest quick-service restaurant companies, is an excellent recovery play. It owns three iconic brands (Burger King, Tim Hortons, and Popeyes) that operate independently. The $23.84 billion company is almost sure to return to pre-pandemic growth in 2022.

In Q3 2021, total revenue and net income grew 11.8% and 47.1% versus Q3 2020. RBI's CEO José Cil said the quarterly results reflect the value of having a diversified business model (three brands in over 100 countries). In the nine months ended September 30, 2021, net cash flow provided by operating activities reached US$1.25 billion — 106.4% year-over-year growth.

National Bank of Canada has entered the fintech space through an 83% ownership stake in Flinks. The tech startup is a global leader in financial data connectivity and analytics. Canada's sixth-largest bank will capitalize on the opportunities in a high-growth marketplace.

The $32.61 billion bank recently announced a 23% dividend hike, the highest percentage increase by a Big Six bank. In fiscal 2021 (year ended October 31, 2021), National Bank's net income rose 53% to $3.17 billion versus fiscal 2021. Its president and CEO, Laurent Ferreira, said the bank has a strong footing entering fiscal 2022 and should generate solid growth across its business segments.

Maximize your TFSA

Follow the rules and maximize your TFSA in 2022 to create tax-free income. If finances allow, invest in Restaurant Brands (3.47%) or National Bank of Canada (3.61%), which pay decent dividends.

CATEGORY

1. Dividend Stocks
2. Investing

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2. TSX:NA (National Bank of Canada)
3. TSX:QSR (Restaurant Brands International Inc.)

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