TFSA Passive Income: How to Earn $385 Per Month Tax Free for Life

Description

Now more than ever could a dependable stream of passive income be of use to investors. Passive income, specifically generated through dividend stocks, could help offset some of the volatility in the market today.

Many investors are understandably feeling the pain of the recent market correction. An additional source of income could certainly help ease that pain.

When it comes to investing in dividend stocks, Canadians have a few options. The two registered accounts that likely come to mind first are the Tax-Free Savings Account (TFSA) and Registered Retirement Savings Plan (RRSP). While both are solid options, I'll explain why a TFSA may be your best bet.

Generating a tax-free passive-income stream within a TFSA

As the name suggests, there are tax benefits to investing through a TFSA. Any income generated within a TFSA, whether from capital gains or dividends, is not taxed. In addition, withdrawals can be made from a TFSA at any point in time — once again, without the need of paying any tax at all.

The catch is that there are certain contribution limits that Canadians need to be aware of. Each calendar year has a maximum TFSA contribution. In 2022, it's $6,000 — the same as it's been since 2019. However, unused contributions can be carried over from year to year, so don't worry if you're behind on your TFSA contributions.

Dating back to 2009, when the TFSA was introduced, the total contribution limit now sits at $81,500. As long as you were 18 years or older in 2009, you're eligible to contribute up to $81,500 in your TFSA right now.

Earning $300 a month in tax-free passive income

Now that we understand the basics of a TFSA, let's look at how we can build a dependable stream of passive income. In terms of generating passive income, dividend stocks are one of your best bets. There are other options, but you won't find many with an annual return above 5%.

Let's assume you're investing in a dividend stock that's currently yielding 5% annually. A maxed-out TFSA of $81,500 invested in a dividend stock yielding 5% would return just over $4,000 a year, or $340 per month.

Keep in mind that most dividend-paying companies will pay out dividends quarterly. However, not all dividend stocks follow that schedule, as some may be paid on a monthly basis.

Two top dividend stocks for TFSA investors

The previous example looked at a return of 5%. But on the TSX today, there are plenty of options for Canadians to earn a dividend higher than that.

Bank of Nova Scotia (TSX:BNS)(NYSE:BNS) and **Manulife** (TSX:MFC)(NYSE:MFC) are two solid choices for passive-income investors. The two companies currently yield 5.2% and 6.15%, respectively.

Assuming that the two companies are invested in evenly, that would equal an annual return of just under 5.7%. At that rate, an investment of $81,500 made today, split evenly between Bank of Nova Scotia and Manulife, would earn $4,625 a year, which comes to $385 per month.

Best of all, you don't need to pay any tax at all on that $385.

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