Retirees: How to Use the TFSA Limit to Maximize Passive Income

Description

The Tax-Free Savings Account (TFSA) limit for 2023 is $6,500. This brings the total maximum contribution space to $88,000 per person, depending on their age at the time of its inception. A retired couple would therefore have as much as $176,000 in TFSA contribution room to earn tax-free passive income.

Benefits of using the TFSA

Canadian retirees get taxable income from a variety of sources that can include the Canada Pension Plan (CPP), Old Age Security (OAS), Registered Retirement Savings Plan (RRSP) withdrawals, Registered Retirement Income Fund (RRIF) payments, company pensions, rental properties, part-time jobs, and non-registered investments.

All of these sources of income are used by the Canada Revenue Agency (CRA) to determine net world income. The problem for seniors who collect OAS is that the CRA will claw back part of a person's OAS payments if net world income tops a minimum threshold. For the 2023 income year, the level to watch is $86,912.

Each dollar in net world income earned above that amount will trigger a $0.15 OAS pension recovery tax that kicks in for the OAS payments in the following year. As net world income rises, the clawback could eventually wipe out the full OAS payments due in the following year. For the 2023 income year, the threshold upper limit is $141,917 for people aged 65 to 74 and $147,418 for those who are 75 and older.

One way to minimize the impact is to shift investments in taxable accounts to the TFSA. All interest, dividends, and capital gains generated inside the TFSA and removed as income are exempt from the CRA's net world income calculation. For couples with $176,000 in TFSA room, this can make a significant difference on taxes paid on investment earnings and help avoid or minimize the OAS clawback.

Best investments for TFSA passive income

Guaranteed Investment Certificate (GIC) rates have increased considerably in the past year as a result of aggressive interest rate hikes by the Bank of Canada. Investors can now get 4-5% returns on a GIC depending on the term. This is decent compared to recent years, and GICs deserve to be part of the TFSA mix.

Investors who can stomach a bit of risk might want to also consider buying top TSX dividend stocks that have long track records of dividend growth and now trade at discounted prices after the 2022 market correction.

Dividend yields from some stocks are still above GIC rates and the payouts should continue to grow. Investors also get a shot at potential capital gains if the share prices recover.

Enbridge (TSX:ENB) and **Canadian Imperial Bank of Commerce** (TSX:CM) are two examples of top Canadian dividend stocks that trade below their 2022 highs and offer high dividend yields.

Enbridge currently trades for close to $54 compared to more than $59 last summer. The company raised the dividend in each of the past 28 years and has a solid capital program in place to drive ongoing revenue growth. At the time of writing, the stock provides a 6.5% dividend yield.

CIBC trades for close to $58.50 right now compared to more than $80 at this time last year. Ongoing volatility should be expected as the market tries to determine if a recession is on the way and how harmful it will be for the banks. That being said, CIBC stock now appears cheap at just 8.75 times trailing 12-month earnings and offers investors a dividend yield of 5.8%. The board raised the dividend twice in 2022, and management expects adjusted earnings to grow in fiscal 2023.

The bottom line on TFSA passive income

Retirees can use their TFSA limits to hold a diversified portfolio of GICs and top TSX dividend stocks to generate passive income that won't put OAS payments at risk of a clawback. If you have TFSA contribution room available, it is worthwhile to consider shifting funds to the TFSA from taxable investment accounts.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:CM (Canadian Imperial Bank of Commerce)
2. TSX:ENB (Enbridge Inc.)

PARTNER-FEEDS

1. Business Insider
2. Flipboard

3. Koyfin
4. Msn
5. Newscred
6. Quote Media
7. Sharewise
8. Smart News
9. Yahoo CA

PP NOTIFY USER

1. aswalker
2. kduncombe

Category

1. Investing

Date
2025/06/27
Date Created
2023/01/30
Author
aswalker