Tax Free Savings Account (TFSA)

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OVERVIEW

In 2009, the federal government introduced the Tax Free Savings Account (TFSA) to give Canadians another means to save for their financial goals. The TFSA is similar to the Registered Retirement Savings Plan (RRSP) in some ways, but different in others.

The TFSA's investment options are broad and the investments grow tax-free. Contributions to the TFSA are not tax-deductible, but withdrawals are tax-free. Another feature of the TFSA is contribution limits are not determined by "earned income" as any Canadian 18 or older can contribute.

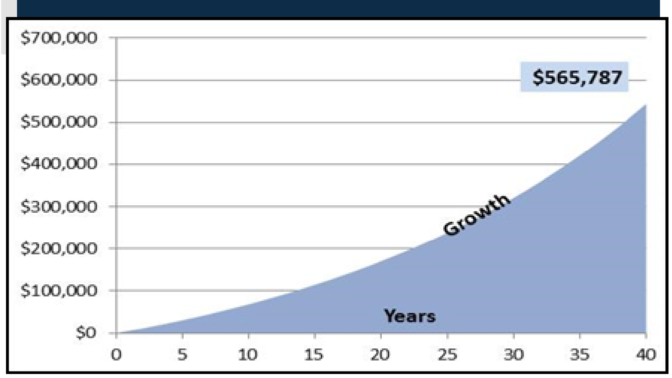
Starting in 2009, the annual contribution limit was $5,000 per person, increasing to $5,500 in 2013. In 2015 the amount increased to $10,000, but was reduced back to $5,500 in 2016. In 2019 the annual contribution limit has been increased to $6,000. Therefore, those yet to contribute to a TFSA have accumulated $63,500 of contribution room as of 2019. For a couple, this represents $127,000 in combined room.

Contributions can be made from cash or non-registered accounts as an "in-kind" contribution, where investments already held are transferred into the TFSA without selling the securities. Like an in-kind transfer to an RRSP, any deemed capital gain is taxable in the year of the transfer, while any capital loss cannot be claimed.

On the death of the owner, the TFSA assets pass tax-free to the estate or beneficiaries. If a beneficiary is named on the account, probate fees can also be avoided.

Quick Facts

- Investments grow and compound on a completely tax-free basis within the TFSA.
- Contributions to the TFSA are not tax-deductible, but withdrawals are tax-free and can be made at any time.
- Withdrawals from the TFSA do not impact Old Age Security (OAS) benefits.
- Unused contribution amounts accrue and can be used in future years.
- The annual contribution limit is $6,000 per person.
- Anyone who has never contributed to a TFSA has accrued a lifetime contribution limit of $57,500.
- Minimal contribution restrictions – any Canadian 18 or older can contribute to a TFSA throughout their lifetime.
- The chart below illustrates the growth of TFSA with an individual maximizing contributions over a 40 year period, at a return of 4%:



PLANNING CONSIDERATIONS

- Consider how the TFSA fits within the overall financial plan – it may be better to maximize RRSPs, RESPs or pay down personal debt first.
- The TFSA can complement other retirement savings and since withdrawals are tax-free, they could help avoid potential OAS claw-back.
- Since contributions can be made at any age over 18, a TFSA can be a powerful estate planning tool in building a sizable tax-free asset for an estate or heirs – a benefit similar to using permanent life insurance. If a specific beneficiary is named in a TFSA, the estate administration tax (probate fees) can be avoided on the value of the plan.
- Consider using existing personal non-registered savings to maximize TFSA contribution limits in order to shelter future investment income from tax.
- Investors owning a corporation may want to consider withdrawing additional dividends to fund a TFSA. Although the additional income from the corporation would be taxable, future investment earnings on those contributions would be tax-free.
- Both capital and growth can be withdrawn on a tax-free basis. The total amount withdrawn can then be re-contributed in the next calendar year, or any time afterwards with no impact on annual contribution limits.

Consult your accountant, financial planner, or investment manager to determine what strategies are best for you.

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