

Tax Free Savings Accounts

Details and Benefits

As of January 2, 2009 – Canadians who are residents of Canada and who are 18 years and older can save up to \$5,000 per year within a Tax Free Savings Account (TFSA) – *Note however that because the age of majority is 19 in British Columbia, contribution room shall be carried forward until the individual has achieved age of majority*

- Unlike an RRSP, contributions to a TFSA are not tax-deductible (contributions are made with after-tax dollars,) however investment income (including capital gains) earned inside the TFSA will not be taxed, even when withdrawn
- Unused TFSA contribution room may be carried forward and used in future years. **Canada Revenue Agency** (CRA) will track contribution room and report this data annually on a Notice of Assessment
- Withdrawals may be made at any time and proceeds withdrawn can be re-deposited without reducing contribution room
- Neither income earned, nor withdrawals will affect eligibility for federal income-tested benefits and credits. Further, there is no requirement to convert the TFSA to an income payment option (such as Registered Retirement Income Fund (RRIF) or Annuity at any age
- Contributions to a spouse's TFSA will be allowed (spousal income attribution rules do not apply) and TFSA assets can be transferred upon death to a spouse (potentially without probate) – *Note however, that many provinces have yet to pass legislation regarding the naming of a beneficiary (spousal or otherwise) and/or the designation of a successor holder (spouse or common-law partner only.) Until formal legislation is passed and TFSA applications are updated, it may be prudent to name one's beneficiary and/or spouse (as successor holder) in one's Will.*
- The \$5000 annual contribution limit will be indexed to inflation in \$500 increments – Note however that excess contributions must be removed or be subject to a 1% penalty per month for each month that the excess remains
- *In-kind* contributions (of qualified investments) are permitted, however just as in the case of an in-kind RRSP contribution, a “deemed disposition” may result in the realization of a taxable capital gain. Where a deemed disposition results in a capital loss, the capital loss cannot be used to offset past/future (taxable) capital gains
- Qualified investments include all arm's-length Registered Retirement Savings Plan (RRSP) qualified investments
- Borrowing to invest inside a TFSA is permitted, however interest expenses related to sum borrowed are not tax-deductible. The TFSA may however be used as collateral for a loan.

Who should invest?

A TFSA is particularly valuable for retirees and/or pensioners who have limited RRSP contribution room eligibility. Withdrawals from one's RRSP (structured or otherwise) and/or excess incomes from mandatory RRIF payments (in cash or in-kind) or pension incomes (including CPP/OAS) can be further *sheltered* from tax consequences.

A Tax Free Savings Account may also be ideal for new/younger investors; those in the early stages of their careers – proceeds of a TFSA can be called upon to help fund one's RRSP contribution. From a tax savings standpoint it often makes sense to defer one's RRSP contribution to a future year when one's income is expected to be higher, thus maximizing the value of the corresponding tax deduction.

Investors who have (already) maximized RRSP contributions and/or RESP Canada Education Savings Grant eligibility should consider contributing to a TFSA. Likewise, couples with uneven incomes (opportunity for income-splitting) and those individuals/couples with non-registered (joint) savings should also take advantage of the Tax Free Savings Account.

Consider this...

The new Tax Free Savings Account provides for an attractive opportunity for significant tax savings/deferral. The TFSA is designed to **complement** other *registered* and non-registered savings plans including RRSPs, Individual Pension Plans (IPP), Registered Education Savings Plans (RESP) and Registered Disability Savings Plans (RDSP) as well as various other *tax-exempt* investment alternatives (including Universal Life Insurance*.)

Consideration should be given however to the *hierarchy* of tax-savings – for instance it may be beneficial to defer contributions to a TFSA in favor of one's RRSP. Recall how RRSP contributions are fully tax-deductible against *earned* income – a tax benefit of **up to 43.7%** of amounts contributed is possible**. Likewise, RESP and/or RDSP contributions may qualify for the 20% Canada Education Savings Grant or matching Disability Grant.

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