

Tax Free Savings Accounts

A new way to save

Starting in 2009, Canadians will have a new way to save with a Tax Free Savings Account – a flexible, registered general-purpose account that will allow Canadians to earn tax-free investment income. The TFSA was introduced in the 2008 federal budget as an incentive for Canadians to save. It is the first account of its kind in Canada, and the government is calling it the single most important personal savings vehicle since the introduction of the Registered Retirement Savings Plan in 1957. It is estimated that, in the first five years, over 75% of the benefits of TFSA savings will go to individuals in the two lowest income tax brackets, with seniors expected to receive one-half of the total benefits provided by the TFSA.

What is a TFSA?

- An account where contributions are made with after-tax dollars and withdrawals are tax-free. This means that money can be earned in the account and withdrawn at any time without being taxed.

Who is eligible to contribute to a TFSA?

- Anyone over the age of 18 – even those without an income, or those over the age of 71, who are ineligible to contribute to an RRSP.

How does it work?

- You can save up to \$5,000 every year in a TFSA. The \$5,000 annual contribution limit will be indexed to the Consumer Price Index and rounded to the nearest \$500. For example, with a 2% rate of inflation, the first increase to \$5,500 would occur in 2012.
- TFSAs can hold the same investments as registered accounts, such as mutual funds, segregated funds, stocks, bonds, and GICs.
- Any amount withdrawn from the account is automatically added back to your contribution room for the following year.
- Unused contribution room can be carried forward indefinitely to future years.

If investment growth is tax free for both TFSAs and RRSPs, what are the differences?

- An RRSP is primarily for your retirement savings, while a TSFA is for other investments and savings.
- Contributions to an RRSP are tax deductible and reduce your taxable income, while contributions to a TFSA are not deductible.
- Withdrawals from an RRSP are added to your income and taxed at your current rate, while TFSA withdrawals are tax-free.
- You must convert your RRSP to a RRIF by age 71 and withdrawals after that time are mandated according to a schedule based on your age. There is no similar requirement for TFSAs.
- For RRSPs, once a contribution is made, that contribution room is “used up”. With TFSAs, the amount of a withdrawal is automatically added back to the contribution room.

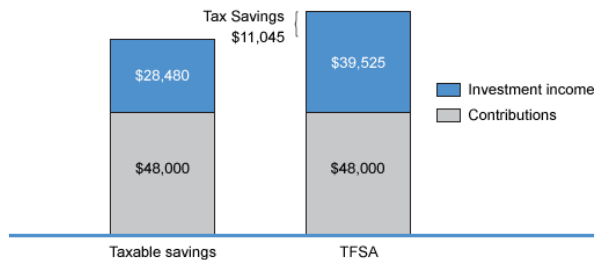
What are the other benefits of a TFSA?

- Income earned in a TFSA and withdrawals do not affect your eligibility for income-tested benefits, such as Old Age Security, Guaranteed Income Supplement and the Canada Child Tax Credit.
- You can provide the funds for your spouse to contribute to their account and the assets in your account are transferred to your spouse upon death without tax implications.
- Income attribution rules don’t apply, so contributions can also be provided to an adult child for their contribution to their account. (In simple terms, income attribution occurs when income earned from money loaned to a spouse or child is attributed back to the lender, who is then taxed on that income.)
- For those who have maximized their RRSP contributions, or those with employer pension plans who may not be allowed to contribute to an RRSP because of a large pension adjustment amount, a TFSA can supplement their savings on a tax-assisted basis.

TFSA versus an unregistered account

Capital gains and other investment income earned in a TFSA are not taxed.

So, if you contributed \$200 a month for 20 years to a TFSA instead of a non-registered account, you would enjoy a total tax savings of \$11,045.



*Assumes a \$200 monthly contribution for 20 years, a 5.5% rate of return and an average tax rate of 21%.
Source: Government of Canada, 2008 budget.*

The TFSA can be a valuable savings tool, with enough flexibility to meet many different needs. If you have any questions, please call me.