Advisor
Investment

Tax-free savings account (TFSA)

A practical addition to your client's savings portfolio.

The Tax-Free Savings Account (TFSA)

The Tax-Free Savings Account (TFSA) is probably the single most important savings vehicle innovation since the introduction of the Registered Retirement Savings Plan (RRSP). TFSAs combine the flexibility of non-registered investments with some of the tax advantages of registered plans.

Although TFSA rules are fairly straightforward, it may not be readily apparent which is more advantageous and when... an RRSP or a TFSA? This brochure is intended to help you to understand which of your clients could benefit most from integrating a TFSA into their financial investment strategy.

TFSA Key Features

- TFSAs are suitable for both retirement and other types of savings projects. Withdrawals can be made at any time without restriction*.
- All Canadian residents who are at least 18 years old are eligible to contribute to a TFSA, whether they are earning a salary or not. The annual contribution limit is the same for everyone ($6,000 in 2020).
- Unused contribution room from previous years increases the contribution limit, as is the case with RRSPs.
- Amounts withdrawn from a TFSA are added to the contribution limit for the following year.
- Withdrawals are not included in taxable income and capital gains and other investment income earned in a TFSA are tax-free.
- Withdrawals do not affect eligibility for federal income-tested benefits and tax credits.
- Contributions are not deductible from taxable income.

* Subject to redemption fees, where applicable.

The TFSA is suitable for a broad range of investors–and definitely worth considering when providing clients with financial advice!

TFSA or RRSP?

In some ways, the TFSA mirrors the RRSP as both provide investors with tax advantages. Like RRSPs, there is an annual contribution limit for TFSAs, but the contributions are not deductible. Unlike RRSPs, the contributions and income that accumulate in a TFSA are not taxable on withdrawal. A TFSA therefore lets you grow tax-free investment income (i.e., interest, dividends and capital gains) earned on the contributions made using already taxed income.

Both of these financial vehicles offer tax relief, however there are some key differences. A good way to understand these is to compare them. The table below presents the main characteristics of each. The section following the table provides more detailed information about TFSAs.

Features	TFSA	RRSP
Clientele		
Target clientele	For individuals from all income levels, in particular: young adults saving for a special project; individuals having reached RRSP contribution limits who are seeking an alternative tax-sheltered savings vehicle; and retirees who don't need all of the retirement income they are required to withdraw; etc.	The RRSP was designed primarily for clients who want to put savings away for retirement.
Eligibility	Canadian residents who are at least age 18, whether earning a salary or not.	Canadian residents earning a salary.

Features	TFSA	RRSP
Contribution room		
TFSA dollar limit	$6,000 in 2021 (this limit is indexed annually and rounded off to the nearest $500).	Based on earned income (18%), less pension adjustment as applicable (maximum $27,830 in 2021).
Unused contribution room can be carried forward indefinitely	Yes	Yes
Withdrawals can be recontributed	Yes, as of the year after the withdrawals were made.	No
Possible to have more than one plan in different financial institutions provided that the contribution limit is not exceeded	Yes	Yes
Excess contributions	Taxed at 1% per month.	Taxed at 1% per month ($2,000 overcontribution cushion).
Investments		
Investments allowed	GIAs, funds, bonds, stocks, etc.	GIAs, funds, bonds, stocks, etc.
Tax considerations		
Contributions deductible from taxable income	No	Yes
Investment income is taxable	No	No
Withdrawals are taxable	No	Yes
Effect on income-tested government benefits or credits	None	Yes, government benefits are affected by withdrawals.
Spousal plans		
Contributions to spousal plans	An individual may give money to his/her spouse to enable the spouse to contribute to a TFSA.	Contributions made to a spousal plan affect the contribution ceiling of the payer.
Loans		
Plan can be used as collateral for loans	Yes*	No
Interest on loans is deductible	No	No
Death and divorce		
In the event of death	No tax impact if the spouse or common-law partner is designated as the sole beneficiary as he/she becomes the successor holder.	Amounts may be transferred to the surviving spouse's RRSP with no tax impact.
In the event of divorce or separation	Amounts may be transferred to the ex-spouse with no tax impact (no tax payable and no impact on ex-spouse's contribution limit). In this case, the transfer does not reinstate the transferor's contribution room.	Amounts may be transferred to the ex-spouse's RRSP with no tax impact.
Beneficiary may be designated under an annuity contract	Yes	Yes

*Subject to SSQ Insurance approval.

General Information about TFSAs

Target Clientele

Many types of clients will be interested by the advantages offered by TFSAs. A case-by-case analysis should be carried out to determine whether a client would be better off contributing to an RRSP, opening a TFSA or paying off debt.

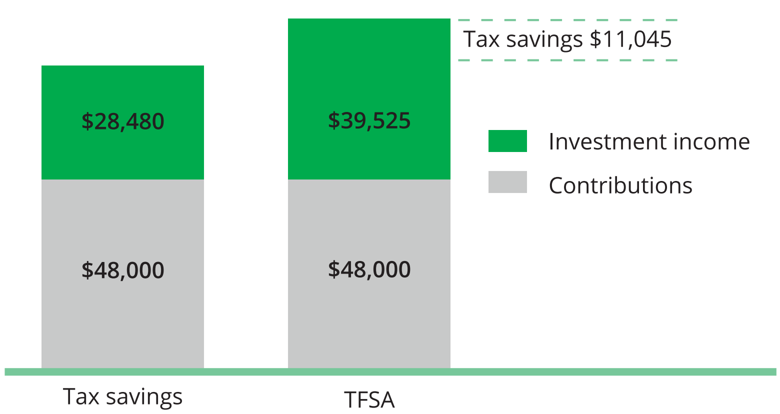
Savings for short- or medium-term projects

Because the TFSA is so flexible in terms of withdrawals and how amounts accumulated in the account can be used, individuals who want to save for a special project (a trip, new car, renovations or down payment on a home) would be wise to opt for a TFSA rather than a traditional non-registered savings plan because the returns are tax-free and available when they need them.

For example, an individual contributing $200 a month to a TFSA for 20 years (assuming an average annual return of 5.5%) will accumulate about $11,045 more in savings than if the investment had been made in a non-registered account.

Investors who have contributed to a non-registered plan in the past could consider transferring these funds to a TFSA. They could begin by transferring relatively high-interest products such as guaranteed interest accounts (GIAs) as the interest income earned on these products is 100% taxable. Please note, however, that there will be a tax impact when funds from a non-registered plan are transferred to a TFSA. Individual client needs must be assessed carefully.

TFSA Versus Unregistered Savings



Notes
Combined federal and provincial tax savings based on a $200 monthly contribution for 20 years and a 5.5% rate of return. For unregistered savings, a 21% average tax rate on investment income is assumed (based on 40% interest. 30% dividends and 30% capital gains, and a middle-income earning account holder).

Retirement savings for low-income earners

A TFSA may be more advantageous than an RRSP if it is anticipated that the income tax rate will be higher upon retirement than at the time the contributions were made. This may apply to some young adults in very low income tax brackets or to low-income earners. Contributions can be transferred to an RRSP at a later date, resulting in a potentially substantial tax refund.

A word of caution, however. Because the TFSA has a very flexible withdrawal provision, clients may be tempted to make withdrawals before they retire. From this point of view, an RRSP may be a better choice for clients who really want to save for their retirement given the stricter withdrawal constraints.

Additional retirement savings for clients with deeper pockets

Investors who have already used up all of their RRSP contribution room can use the TFSA as an alternative retirement savings vehicle – and enjoy the advantage of their investment income being tax-free.

Advantages for retirees

Retirees who are required to make RRIF withdrawals, even when they may not necessarily need this income, can reinvest this money into a TFSA. The same applies if they wish to set aside money which can be transferred to their spouse with no tax impact upon death.

Spouses wishing to share savings

Since attribution rules do not apply to TFSAs, an individual can give money to a spouse, and the spouse can then invest this money in a TFSA, with no impact on the contributing spouse's contribution room limit. In the event of the spouse's death, the same individual can then recover the assets in the TFSA.

Eligibility

Since 2009, all Canadian residents who are at least 18 years old and who have a valid Social Insurance Number (SIN) can open a TFSA, whether or not they have earned an income.

Unlike RRSP contributions, TFSA contributions can be made after age 71.

If an individual becomes a non-resident of Canada, he/she will be allowed to keep the TFSA and will not be taxed on any earnings in the account. However, contributions can no longer be made and no TFSA contribution room will accrue for any year of non-residency. Any withdrawals made during the non-resident period will be added back to the unused contribution room in the following year, however contributions can only be made if residency status is resumed in Canada.

Contribution Limit

The annual TFSA contribution limit does not depend on an individual's income. This limit is set every year by the federal government and applies to all eligible individuals. Starting in 2020, the amount is $6,000. The individual contribution limit is increased by any unused contribution room from the previous year, as is also the case with RRSPs.

Contribution Limit Since TFSA Inception

Years	Annual Contribution Limit	Number of Years	Total
2009 to 2012	$5,000	4	$20,000
2013 to 2014	$5,500	2	$11,000
2015	$10,000	1	$10,000
2016 to 2018	$5,500	3	$16,500
2019 to 2020	$6,000	2	$12,000
Cumulative Contribution Limit			**$69,500**

For example, if you contributed $4,000 to a TFSA in 2013, you are able to contribute up to $65,500 in 2020 (i.e. $6,000 for 2020 plus $59,500 in unused contributions since 2009). These unused amounts can be carried forward indefinitely.

However, if you withdrew $2,500 in 2014, you will be able to contribute up to $68,000 in 2020. This unique provision makes the TFSA highly advantageous as investment returns can be withdrawn and then put back into the TFSA at a later date. For example, if an initial $5,000 investment grows over time to $7,500, the entire amount may be withdrawn and then contributed again at a later date. However, individuals must wait until the following year before they can recontribute the amount withdrawn.

The contribution limit applies to all of the TFSAs an individual may have in different financial institutions. Canadian residents are informed of their annual contribution limit after filing their tax returns. Please note that overcontributions are subject to a monthly penalty of 1% on the excess amount contributed.

Although the annual contribution limit may seem relatively low, the TFSA has the potential to generate significant investment savings within only a few years.

Investments

All of our financial products are eligible for TFSAs: all types of GIAs, all Guaranteed Investment Funds (GIF), etc. The payment of income option is available, as is the simple interest option for GIAs. The redemption fee exemption that applies to RRSPs, LIRAs and NRSPs also applies to TFSAs. In addition, a TFSA may be opened as part of a group plan or as an individual account.

Tax Considerations

One huge advantage for TFSA holders is that they can accumulate investment income tax-free. This means that no tax slips are issued for any type of investment income (capital gains, interest, dividends, etc.) and clients are not required to declare this income on their tax return. This also means that TFSA clients will be able to obtain the maximum benefit from their investment income. However, capital losses are not deductible from taxable income.

Withdrawal amounts are not included as taxable income and therefore in this sense are tax-free. In addition, contributions are not deductible from taxable income.

Another big advantage of TFSAs is that withdrawals will not affect income-tested benefits or tax credits, including the following:

- Age Credit
- Guaranteed Income Supplement
- Old Age Security
- Canada Child Tax Benefit
- Goods and services tax (GST) Credit
- Employment Insurance

Since amounts withdrawn from RRSPs reduce an individual's eligibility for certain government benefits and credits, low-income earners who depend on these benefits should opt for a TFSA since any withdrawals will not affect benefits they may depend on to cover their living expenses.

Spousal Plans

Strictly speaking, TFSA rules do not provide for the creation of a "spousal plan" that specifies the names of the planholder and the contributor. However, a TFSA can still be used to enable a spouse who has little or no income to save money tax-free. Since the attribution rules do not apply to TFSAs, an individual may give money to a spouse, who may then invest this amount in a TFSA–without affecting the contributing spouse's contribution limit.

Loans

As with RRSPs, the interest on loans taken out to invest in a TFSA cannot be deducted from taxable income. For that reason, taking out an investment loan to invest in a TFSA is not really advantageous. However, TFSAs can be used as collateral for a loan taken out for other purposes, subject to the approval of SSQ Insurance.

In the Event of Death

In the event of death, the value of the assets accumulated in the TFSA is payable tax-free to the designated beneficiary or the estate.

The investment income in the TFSA becomes taxable following the death of the TFSA holder, while the income accumulated prior to the planholder's death remains exempt from income tax. Therefore, the estate will be required to declare the investment income, where applicable.

However, if the spouse or common-law partner is the sole designated beneficiary under the contract, he/she would be considered the successor holder and the TFSA remains 100% non-taxable.

In the Event of Divorce or Separation

In the event of divorce or separation, amounts may be transferred directly from an individual's TFSA to the TFSA of the ex-spouse or ex-common-law partner. In this case, the transfer does not reinstate the transferor's contribution room and is not counted against the transferee's contribution room.

The information contained in this guide was valid at the date of publication based on information provided by the Canada Revenue Agency (CRA). However, this document does not constitute a legal opinion.

If you have clients that are interested in investing in a TFSA, please use the FRA1251A form.

Quebec Sales Office
Tel.: 1-888-292-8483

Ontario, Western And Atlantic Canada Sales Office
Tel.: 1-888-429-2543

Client Services
2515 Laurier Boulevard
P.O. Box 10510, Stn. Sainte-Foy
Quebec City QC G1V 0A3

Tel.: 1-800-320-4887
Fax: 1-866-559-6871

service.inv@ssq.ca

ssq.ca

BRA1276A (2020-12)