Tax Free Savings Accounts
(TFSA) PLAN OVERVIEW

The Tax-Free Savings Account (TFSA) is a flexible, registered account that allows Canadians to watch their investments, including interest income, dividend payments and capital gains, grow tax free. Whereas an RRSP is intended for retirement, the TFSA can be effective for achieving pre-retirement, retirement and estate planning goals.

This overview summarizes the features and benefits of the plan.

ELIGIBILITY
Age 18 or older
Since 2009, all Canadian resident taxpayers at least 18 years old are allowed to open a TFSA. The only other requirement is that the individual must have a Social Insurance Number (SIN) when the account is opened.

CONTRIBUTIONS
Beginning January 1, 2009
Each eligible individual is entitled to TFSA contribution room of $5,000 per calendar year.

Unlimited carryforward
Contribution room is cumulative and will be carried forward indefinitely to future years. For example, if you have only contributed $3,000 since 2009, your remaining TFSA contribution room in 2011 will be $12,000 ($5,000 entitlements for each of 2009, 2010 and 2011, less the $3,000 of contributions).

Product choice
Perhaps poorly named, the Tax Free Savings Account is creating considerable confusion in error, that the investment product used must be a (bank) Savings Account. In addition to savings accounts, a TFSA can be invested in a broad list of investment options including GICs, mutual funds, bonds and stocks. The product choice should be based on your overall investment strategy, reflecting time horizons and desired returns.

Funding sources
If you are not in a position to be accumulating new TFSA savings, but hold existing non-registered investments, it may be prudent (with advice) to convert non-registered monies to TFSA year by year.

TAX STRUCTURE
Unlike an RRSP but similar to the RESP model, contributions to a TFSA are made using after-tax funds, which is to say that these contributions are not tax deductible from income.

Tax-sheltering within the plan
Whether the chosen investment within the TFSA earns interest income, dividend payments or capital gains, there is no tax to be paid on those earnings.

Please see overleaf for more reasons to discuss tax planning with a professional…

Withdrawals are not taxable
Whereas RRSP or RRIF withdrawals are fully taxable, there is no tax paid on TFSA withdrawals. As well, at no time is there a minimum or maximum withdrawal amount, nor are there any requirements or restrictions on what you do with those withdrawals. Additionally, any withdrawals actually taken will cause a dollar-for-dollar recovery of contribution room to be used in the future. *Finally, savings you can use!*

Recovery of contribution room
Unlike the RRSP system, where contribution room is completely exhausted as it is used, any amounts withdrawn from your TFSA in a particular year are automatically added to your TFSA contribution room for the following year (and again may be carried forward indefinitely). Fitting with the flexible, general-purpose nature of the account, this will allow individuals to re-contribute an equivalent amount in a future year.

Excess contributions
Just like with an RRSP, any excess contributions beyond the TFSA contribution limit will be taxed at 1% per month.

Effect on income-tested government benefits
A significant drawback to receiving RRSP-sourced income is that the holder is not only taxed on that income, but those receipts can affect eligibility for income-tested government benefits (such as the Guaranteed Income Supplement or Old Age Security) and tax credits (in particular the Age Credit, Canada Child Tax Benefit and Goods and Services Credit). In stark contrast, TFSA withdrawals are not considered to be income and therefore will not contribute to the loss of those income sources or tax credits.

STRATEGIC USE OF A TFSA

Interest deductibility
Since the income earned inside a TFSA along with TFSA withdrawals are non-taxable, you won't be able to write off any interest expense on funds borrowed for the purpose of investing in a TFSA.

As loan collateral
Unlike an RRSP, which cannot be used as collateral for a loan (unless you want your RRSP deregistered and immediately taxed), TFSA assets can be used as collateral, which may facilitate obtaining secured credit for other purposes at more favourable rates.

No spousal income attribution
Where an individual contributes to a non-registered investment of a spouse or partner, the income attribution rule will attribute taxation back to the contributor. The TFSA rules contain a specific exception to these attribution rules, effectively creating a new avenue for spousal wealth planning.

What happens upon death?
The fair market value of the TFSA on the date of death will be received by the estate on a tax-free basis; any income or gains accruing after the date of death will be taxable. The ability to name a direct beneficiary on a TFSA will depend on future amendments to provincial laws allowing for such designations.

Rollover to spouse
An individual may designate a surviving spouse or partner as a successor account holder to continue the particular TFSA or transfer the value to the survivor's own TFSA. Either way, the account continues to be tax-exempt and there is no effect on the survivor's own existing TFSA contribution room.

What happens upon separation or divorce?
On the breakdown of a marriage or common-law partnership, any TFSA amount may be transferred from the TFSA of one spouse or partner to the TFSA account of the other while maintaining the tax-exempt status. Such transfers do not recover contribution room for the transferor, nor do they affect the existing room of the transferee.

Annual indexing
An indexing formula is applied annually to determine whether the TFSA contribution room will increase. The resulting figure is rounded to the nearest $500. For example, if the calculation for 2012 yields a figure of $5,200, then room for 2012 will remain at $5,000. However, if the formula brings it to $5,400, then the actual room will be $5,500.

TFSA vs RRSP
While the plans are meant to be tax-neutral where a person has the same marginal tax rate at all times, an RRSP will tend to make more sense when the tax rate upon withdrawal is expected to be lower than your tax rate upon original contribution. Conversely, a TFSA will work out better if your tax-rate (including the effect of RRSP withdrawals on reduced income-tested benefits) will be higher upon ultimate withdrawal than it was when you contributed.

THE OSTIC GROUP FINANCIAL

Ostic Financial Group Limited
Ostic Insurance Brokers Limited
175 Provost Lane
PO Box 245
Fergus ON N1M 2W8

t 519 843-2540
800 551-3651
f 519 843-4152
financial@theosticgroup.com

[Charted Wealth Planning] DREAMQUEST®