

Are You Benefiting from the TFSA?



Recognizing that higher inflation is a concern for many people as the cost climbs for a number of goods and services, the federal government has boosted the 2023 contribution limit for the Tax-Free Savings Account (TFSA) to \$6,500, an increase of \$500 from 2022. It's not a huge increase, but the additional amount coupled with the potential for compounding growth can make a difference over the long run.

How TFSAs work

The TFSA was introduced in 2009 as a tax-effective savings option. Unlike the well-established Registered Retirement Savings Plan (RRSP), where you deduct contributions from taxable income because they're made with "pre-tax dollars," TFSA contributions are not tax deductible since they're made with "after-tax" dollars. However, TFSA investment growth and withdrawals are never taxed, while they are for the RRSP once you withdraw from the plan.

If you choose to withdraw funds from your TFSA, you may recontribute the withdrawn amount to preserve your total allowable contribution. The only stipulation is that you cannot recontribute in the same calendar year in which you made the withdrawal.

Also, since income earned in TFSAs is tax-free, it won't affect eligibility for income-tested benefits like the Canada Child Benefit, Employment Insurance, Old Age Security and credits related to HST/GST.

Who can hold a TFSA?

Canadians aged 18 or older with a valid Social Insurance Number can open a TFSA at a qualifying financial institution and start contributing. The federal government sets the annual contribution limit based on several factors, including the rate of inflation. If you don't contribute the maximum amount in a given year, you may accumulate contribution room for future years.

The TFSA contribution room is currently \$88,000 (i.e., the amount available if no contributions had been made from 2009 to 2023). Depending on your previous contributions and the cash you might have available this year, you can invest a lump sum now and start getting that money working for you, tax-free, right away. For example, if you had contributed \$67,000 to your TFSA over the years, you're eligible to contribute up to \$21,000 (\$88,000 – \$67,000) in 2023.

Take note, however, that over-contributions in a given calendar year will incur a penalty of 1% per month. Let's say you contributed \$9,000 in 2023, which is \$2,500 above the current limit. You would be assessed a penalty of \$25 per month for each month that the over-contribution stays inside your account, so be sure to keep track of your annual contribution amounts and avoid this penalty.

Uses for a TFSA

If possible, allow your contributions to grow in value over time and then take the savings in your account to provide cash flow in retirement. However, some people also use their TFSA for shorter-term purposes. For instance, TFSAs may be a tax-efficient way to save for a big vacation, buy a vehicle, make a down payment on a home or some other financial goal. Whenever you need the funds, simply withdraw them tax-free from your account and you'll still maintain the option to recontribute withdrawn funds in the future.

Ways to invest in a TFSA

How you choose to invest the money invested in your TFSA depends on personal circumstances, such as your specific risk tolerance, time horizon and financial goals. Similar to RRSPs, a broad range of investment securities are permitted in a TFSA, from stocks and bonds to mutual funds, exchange-traded funds (ETFs) and other products. Together with your advisor, you can create a suitable investment strategy for your TFSA that's designed to achieve your short-term and long-term objectives. Given the many benefits of holding a TFSA, it's certainly worth considering adding this versatile investment account to your overall portfolio.

Contact us today to learn how TFSAs can help you meet your unique financial goals.

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