Tax-Free Savings Accounts

Case Study – High income earner and income splitting

The situation:

James, age 51, is a new client. He has earned income of $200,000 and is also enrolled in a generous defined benefit company pension plan, which will provide him with a financially secure retirement at age 65. He has been investing primarily in a non-registered account, where he has accumulated $950,000. James has three grown children, ages 19 to 24, and a spouse. He is considering using a tax-free savings account to shelter more of his income and to split some of his accumulated wealth with his family.

The challenge:

To find a tax-effective way to shelter as much of James's income as possible and split some of his investments with his family.

Annual maximum RRSP contribution room

The allowable RRSP contribution room is the lower of:

- 18% of earned income from the previous year, or
- the maximum annual contribution limit for the taxation year (2016 – $25,370)

Less any pension adjustment from an employer sponsored pension from the previous year.

Tax-free savings account summary

Starting in 2009, every individual resident in Canada over the age of 18 can contribute to a TFSA. Contribution room accumulates each year if a TFSA contribution is not made. The cumulative TFSA contribution room for 2016 is:

TFSA contribution room			
Year	Amount	Year	Amount
2009	$5,000	2013	$5,500
2010	$5,000	2014	$5,500
2011	$5,000	2015	$10,000
2012	$5,000	2016	$5,500
Total $46,500			

Every individual resident in Canada who was at least 18 years of age in 2009 and has not contributed to a TFSA has $46,500 in contribution room available as of 2016.

James needs to keep in mind:

- his annual adjusted allowable RRSP contribution limit given his pension adjustment
- his family's total TFSA contribution limits
- the tax status of his non-registered investments

The strategy:

James should continue to contribute his adjusted RRSP contribution limit.

For 2016, James has $46,500 of individual TFSA contribution room, or $232,500 of combined contribution room for himself, his spouse and three children. James decides to use TFSAs to shelter as much income as possible and to share some of his current investments with his family so they can maximize the growth potential of their investments tax free.

The result:

James cannot invest directly in a family member's TFSA. Instead, he must provide them with the money for their respective contributions. As James wishes to use his non-registered account to fund the TFSA contributions, he may have to crystallize capital gains and pay tax on them, and/or trigger capital losses and must keep in mind the superficial loss rules, particularly for financial accounts held by him and his spouse.

James continues to use this strategy over the next 15 years. He maximizes his RRSP and TFSA contributions, and transfers $22,000 a year to his family for their TFSAs. During this period, he is able to shelter over $645,000 in principal, along with the future growth of the investments, in TFSAs. James realizes that once he gifts the funds to his family, he no longer has control over the funds or the future investments, but he sees this as an opportunity for his children to benefit during his lifetime. Over the years, his children are able to use their TFSAs for a variety of purposes. Every time they withdraw money, that amount is available as TFSA contribution room in future years.

James was able to use TFSAs to shelter as much income as possible for himself and his family.

For more information on Tax-Free Savings Accounts, please contact your Assante Advisor.

1604-0749_E (04/16)