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In this edition of the Canadian Tax Planners Newsletter, we shall review the following topics:

- Tax Free Savings Accounts
- changes to federally regulated Locked in Life Income Funds
- CRA goes after sellers on Ebay

Tax Free Savings Accounts

In the 2008 federal budget, the government introduced a new tax vehicle that we believe is the most positive tax change in the past decade. Tax Free Savings Accounts (TFSA) will allow individuals to structure their accounts to avoid paying tax on a portion of their investment income. In the Budget Papers, the Department of Finance made the following statement:

“As the TFSA matures over the next 20 years, it is estimated that, in combination with existing retirement plans, it will permit over 90% of Canadians to hold all of their financial assets in tax efficient savings vehicles.”

In this edition of the Canadian Tax Planners Newsletter, we shall review the following issues as they relate to Tax Free Savings Accounts:

- the mechanics of TFSA's
- potential tax planning opportunities utilizing these new vehicles
- advantages and disadvantages of Tax Free Savings Accounts as compared to using Registered Retirement Savings Plans and Registered Educational Savings Plans to save for retirement and a post-secondary school education

Mechanics of Tax Free Savings Accounts

The tax rules related to Tax Free Savings Accounts can be summarized as follows:

- financial institutions will be allowed to offer these plans to the public in January 2009

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- Canadian residents that are eighteen years of age or older will be allowed to open a TFSA
- contributions to a Tax Free Savings Account are not deductible for income tax purposes, but withdrawals are not taxable
- unused contribution room can be carried forward to future years. Thus, a twenty year old college student who does not have the resources to contribute to a TFSA at the current time, could make his first contribution at age thirty and the initial contribution could be \$50,000. This ignores the indexing provisions of contribution limits
- if funds are withdrawn from a Tax Free Savings Account, individuals will receive additional contribution room equal to the amount of the withdrawal. For example, assume an individual has made the maximum contribution every year and on December 31, 2013 he withdraws \$28,500 from the TFSA to be used as a down payment on a home. The \$28,500 represents five years of contributions at \$5,000 per year, plus tax free investment income of \$3,500. In 2014, the maximum allowable contribution would be \$33,500. This amount is calculated as the total of the year's allowable contribution (\$5,000) plus the amount that has been previously withdrawn, i.e. \$28,500
- in addition to contributing to their own TFSA, individuals can contribute to their spouse's Tax Free Savings Account without tax consequences. Spouse includes both married and common-law relationships
- qualified investments that can be maintained in a Tax Free Savings Account are defined as those investments that qualify for inclusion in an arm's length Registered Retirement Savings Plan. Qualified investments include most Canadian and foreign investments, such as stocks, bonds, GIC's, T-Bills and mutual funds. Non-qualified investments include real estate, precious stones, shares of private corporations (unless your family owns less than 10% of the shares,) commodity futures and a class of assets known as "listed personal property." Listed personal property includes art, stamps, coins and jewellery
- withdrawals from a TFSA do not count as income for the various government programs that provide a level of benefits based upon family income. Examples of such programs would include the GST credit, old age security payments, or Guaranteed Income Supplement

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