

TFSA or RRSP?

When RRSP season arrives, many members are likely to see the TFSA as an alternative to an RRSP.

While the feature differences between the two products means that for the most part they should complement rather than compete with each other in an individual's savings program, there are circumstances under which one can be better than the other for long term savings objectives such as retirement. One key is to compare tax rates during the contribution and withdrawal phases.

Because of their tax-advantaged status, funds placed in TFSAs and RRSPs will generate higher after-tax returns than investing in non-registered accounts, particularly for interest bearing investments such as GICs, bonds or savings accounts, which attract the highest marginal tax rates. To help savers determine how the TFSA will benefit their particular circumstances, the federal government has placed a TFSA calculator on its website. It can be found at www.budget.gc.ca/2008/mm/calc_e.html.

While there are situations when a TFSA may yield better long term results than an RRSP for retirement savings, generally the TFSA complements savings under an RRSP. Here are some specific members that a TFSA may appeal to.

HIGH INCOME EARNERS

High income earners who have maximized their RRSP contributions, and are looking for another investment vehicle that shelters income from tax will benefit from the TFSA. Using TFSAs and RRSPs is not necessarily an 'either-or' situation. The TFSA can offer valuable tax savings over and above what's achievable through an RRSP.

RETIREES

Because it has no upper age limit on making contributions, seniors can continue to grow their tax free income under a TFSA. They do not have to collapse their plan, as with an RRSP, and move their funds to a retirement income option such as a RRIF, where the funds are gradually taxed. For those who already have a RRIF, the TFSA can be used to shelter withdrawals which are not needed. And, as mentioned, TFSA withdrawals and earnings do not affect means-tested programs such as OAS.

CONSERVATIVE INCOME INVESTORS

Those who prefer to save using savings accounts, GICs, bonds or other interest-bearing instruments will do substantially better tax-wise under a TFSA than by keeping their funds in a non-registered account.

WORKERS WITH PENSION PLANS

The TFSA can help the individual offset RRSP contribution room lost from pension adjustments.

SHORT TERM, GOAL-ORIENTED SAVERS

While the ability to contribute up to \$5,000 is an obvious benefit under the TFSA, a more valuable feature for many will be the account's liquidity. The ability to shelter funds from tax, withdraw and then replace funds in a subsequent year as needed without affecting contribution room, makes the TFSA a perfect tool to save for a variety of shorter term objectives, such as: **Down payment for a home purchase • Home renovations • Emergency funds • Travel • Vehicle purchase • Educational expenses**

HOMEOWNERS, EMPTY NESTERS

In the future, homeowners looking to downsize will be able to utilize their TFSA to shelter proceeds of a

home sale from future taxation. Although a principal residence can be sold tax-free, the proceeds once reinvested in non-registered accounts would begin to generate tax.

SMALL BUSINESS STARTUPS

Those looking to start a business can use the TFSA to grow their seed capital tax-efficiently, and also use the account as collateral for a business loan. Your deposits are safe and secure with insurance provided by the Deposit Insurance Corporation of Ontario for up to \$100,000 for each RRSP and TFSA contract. Your Credit Union is able to help you sift through the pros and cons of the different investment vehicles to help you determine the right mix for your situation.