A TFSA can be an excellent complement to an RRSP

Tax-Free Savings Accounts (TFSAs) are a unique way for Canadians to save money and pay less tax. Every Canadian resident with a social insurance number and who has reached the age of majority[1] can open a TFSA. The current annual contribution limit is $6,500.

Key features

- Unlike Registered Retirement Savings Plans (RRSPs), contributions are not deductible for tax purposes.
- Investments grow tax-free while inside the TFSA.
- Withdrawals can be made at any time for any purpose and are not subject to tax.
- Unused contribution room can be carried forward indefinitely.
- Withdrawals can be re-contributed, although not in the same year the withdrawal was made.
- TFSAs can hold many of the same investments as an RRSP.

TFSAs and RRSPs are important savings and investing plans available to Canadians and generally one is not better than the other. They each have their own unique tax advantages and can work together to help maximize your savings and investments. TFSAs are flexible enough to help you save for both short-term objectives, such as major purchases, and long-term goals. RRSPs are long-term plans designed for retirement income saving.

A TFSA can be an excellent complement to an RRSP. It can help you maximize retirement income when RRSP contribution limits have been reached.

The TFSA or RRSP decision

Consider the following:

- An RRSP when pre-retirement income is expected to be higher than retirement income. Income during retirement may benefit from a lower tax rate.
- Either a TFSA or an RRSP when pre-retirement income is anticipated to be equal to retirement income. Income tax rates may be equal before and during retirement, so there is no advantage to one over the other.
- A TFSA when pre-retirement income is expected to be lower than retirement income. Income during retirement may be withdrawn tax-free from a TFSA.

1 In some provinces the age of majority is 19 and a plan may not be opened until then. These provinces are British Columbia, Newfoundland and Labrador, Nova Scotia and New Brunswick. However, you will accumulate contribution room from the time you are 18.

A TFSA compared to an RRSP

The major difference between a TFSA and an RRSP is the treatment of contributions and withdrawals for tax purposes. RRSP contributions are tax-deductible, but withdrawals are taxed as income. On the other hand, TFSA contributions are not tax-deductible, but withdrawals and the growth on investments are tax-free.

Furthermore, TFSA withdrawals have no effect on an individual's eligibility for federal income-tested benefits and credits. However, RRSP withdrawals are included as income for the purposes of calculating benefits. This may be particularly important to seniors who receive Old Age Security and/or the Guaranteed Income Supplement.

	TFSA	RRSP
Tax-deductible contributions?	No	Yes
Tax on withdrawals?	No	Yes, taxed as income
Withdrawals increase contribution room?	Yes[2]	No
What are the contribution limits?	$6,500, regardless of income	18% of earned income to a maximum of $30,780 (2023)
Accumulate unused room?	Yes	Yes
Need for conversion?	No	Yes, to a RRIF or life annuity by age 71
Do income attribution rules apply?	No	Generally no, but may apply to withdrawals from a spousal RRSP

2 TFSA withdrawals increase the available contribution room in the year following a withdrawal.

Contribution room formula

TFSA contribution limit

$6,500 per year regardless of income

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Available TFSA contribution room

RRSP contribution limit

18% of prior year's income to the annual maximum contribution limit

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Unused RRSP contribution room

For more information on Tax-Free Savings Accounts, contact your financial advisor.

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