HITTING YOUR STRIDE

HIGH-INCOME EARNERS

When RRSPs aren't enough, TFSAs can help you shelter more income from the taxman

ANTHONY AND JENNIFER DELPERO
TORONTO, ON

The Delperos may want to use some of their TFSA savings to help finance travel with their twins or pay for post-secondary school costs when three-month-old Julia and Anthony are older.

Photograph by Angela Lewis

The highlight of 2015 for Anthony and Jennifer Delpero was the arrival of their twins. But the $4,500 bump in annual TFSA contribution room was a (not very) close second. "I love the TFSA increase," says Anthony, the owner of Hawksdale Landscaping in Toronto. With Jennifer at home looking after the kids, she's not earning income, which means she's not accumulating RRSP room. "So our primary tax savings vehicle is the TFSA," he explains.

GIVE FREELY TO SPOUSES

A key benefit of the TFSA is that it allows single-income couples like the Delperos to avoid the "attribution rules" that normally apply when you give your spouse money. If Anthony were to give Jennifer money to invest in a non-registered account, all of the income and capital gains would be taxable in his name. And while he could contribute to a spousal RRSP for Jennifer, that would eat into his own contribution room. But Anthony can now give $10,000 annually to Jennifer for her TFSA contribution, and none of the investment returns will be taxable now or in the future.

While the Delperos understand that the RRSP is often the best retirement account for high-income earners because of the immediate tax refund, they have other considerations. They may want to use their TFSA money to grow the family business in a few years when the twins are in school. "I won't have to worry about paying taxes if I decide to make withdrawals, like I would with an RRSP. That's huge for me at this stage of my life," says Anthony.

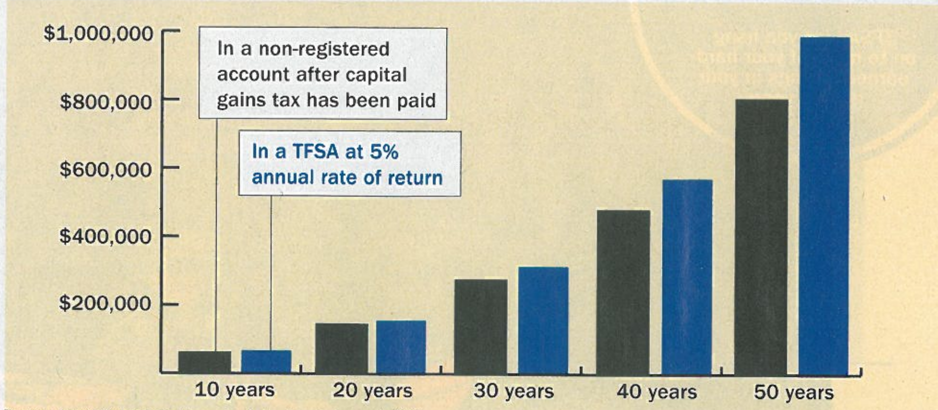
RETIRE RICHER

Brett Robinson is another high-income earner who has embraced the new TFSA rules. With a job that pays him $150,000 annually, the Edmonton engineer's biggest financial problem is how to tax-shelter the $55,000 or so he's able to save each year. Such a plush income has meant he's always been able to max out his RRSP and his TFSA. Last year he even bought a small rental property in Medicine Hat, Alta., and was still left with some cash that would otherwise have gone into a taxable investment account. He got a break when the government raised the TFSA contribution limit. "As soon as the limit was upped from $5,500 to $10,000, I knew I'd be using it," says Brett, who is 26 and single. "I contributed the full amount right after the announcement."

Like most high-income earners, Brett

SUPERIOR LONG-HAUL SAVINGS

So what does $4,500 a year in extra tax-sheltered savings mean for high-income earners? We've run the numbers to show you that the tax savings can be substantial over the long haul. We've assumed 5% equity returns and a combined federal and provincial tax rate of 50%.



Source: Jamie Golombek, tax and estate planning expert, CIBC

tries to avoid investing in non-registered accounts, since he's taxed at the highest rate, which ranges from 39% in Alberta to almost 55% in New Brunswick. By taking full advantage of the TFSA to avoid that massive tax hurdle, Brett figures he'll be able to achieve his dream of retiring at 50, if not sooner. "If I stay single, I could retire pretty damn early," he says. "It's going to change my life."

Jamie Golombek, a tax and estate planning expert at CIBC in Toronto says Brett made the right move. "Putting the extra $4,500 into a TFSA is a no-brainer. I can think of no situation where there's any excuse to have money in a non-registered account if you still have TFSA room—high-income earner or not."

In fact, Golombek has run the numbers and the tax savings—especially for high-income earners—are eye-popping. If Brett puts that extra $4,500 a year into his TFSA for the next 50 years and gets a 5% average annual return, he'll have an additional $989,169 by age 76—all tax-free. Had he invested that money in a taxable account, it would have grown to just $789,127 once capital gains taxes were paid.

The extra $4,500 in annual TFSA contribution room ($9,000 for couples) will especially help Canadians who are able to save more for retirement than the RRSP rules allow. The RRSP contribution ceiling is 18% of earned income to a maximum of $24,930 for the 2015 tax year, and many big earners are able to save more than that: Brett, for example, saves about 35% of his gross salary. The TFSA also helps members of employer-sponsored pension plans who are limited to small RRSP contributions, as well as single-income families like the Delperos, where one spouse has little or no opportunity to contribute to an RRSP.

TFSA 101

If you've maxed out both your RRSP and your TFSA, **keep the highest-growth investments (such as stocks) in the TFSA.** That will maximize your tax savings

SHIFT SAVINGS

If you have already amassed a healthy non-registered portfolio, the new TFSA contribution limit can help you shelter more of that money every year. Rather than making contributions with new cash, you can simply shift $10,000 a year from your taxable accounts to your TFSA. Just keep in mind that while all TFSA investments are sheltered from income tax, some assets are better suited to the account than others. "Any investment offering steady returns is not a bad option—except for U.S. dividend-paying stocks," says Vickie Campbell, a certified financial planner with Ryan Lamontagne in Ottawa. "If you own the same stock in an RRSP and it pays a dividend of $1, you will keep the whole dollar," she says, explaining that the U.S. government's 15% withholding tax on dividends does not apply to RRSPs. "But this exemption doesn't apply to TFSAs." And unlike with non-registered accounts, you can't apply for the foreign tax credit to recover that U.S. withholding tax.

While small-cap and growth stocks held in a TFSA can provide potentially large tax-free capital gains, they are risky. Of course, these investments can suffer big declines in a taxable account, too, but at least you would be able to use any capital losses to offset other gains. Not so with stocks held in a TFSA. That's why low-cost equity mutual funds or ETFs that suit your risk tolerance and time horizon are often a better bet for your TFSA than risky stocks with the potential for a big win. "While there will be periods of losses in the short term for balanced equity funds, they generally have a greater potential to grow over the long term," says Campbell.

"Even holding a simple balanced fund in a TFSA can yield impressive returns over the long-term," says Gordon Pape, author of *Tax-Free Savings Accounts: How TFSAs Can Make You Rich*. "It's the most potent investment tool available to Canadians right now."