Tax-free savings account

The tax-free savings account (TFSA) is a flexible investment savings vehicle that allows you to earn investment income (including capital gains) tax-free. The account can be used to meet a variety of financial security planning needs, such as:

- Retirement saving
- Saving for vacation
- Major purchases
- Parental leave
- Income splitting

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Compound your savings . . . tax-free

Eligibility

Every resident of Canada who is age 18 or older and files an income tax return is eligible to contribute to a TFSA. There is no maturity date on a TFSA like a registered retirement savings plan (RRSP) and it doesn't need to be wound-up or converted to a different investment vehicle.

Investment options

The types of investments that can be held in a TFSA are generally the same as those permitted for an RRSP. These investments include:

- Mutual funds
- Segregated funds
- Publicly traded shares
- Government and corporate bonds
- Guaranteed investment certificates

Some of the types of investments that cannot be held in a TFSA are:

- Shares or debt of a company in which you have a significant interest
- Futures contracts
- Works of art
- Precious metals
- Real estate

If you hold a non-qualified investment in your TFSA, you would be liable to pay tax equal to 50 per cent of the value of the non-qualified investment. Any income earned on that investment would also be subject to tax.

You can transfer funds from an existing non-registered account to your TFSA, but be aware the redemption may trigger capital gains and tax. If the transfer gives rise to a capital loss, the loss is denied.

Contributions: $5,000 per year for life

Starting in 2009, the annual contribution limit is $5,000, regardless of how much income you earn. This amount will be indexed annually based on increases in the consumer price index in $500 increments. The Canada Revenue Agency (CRA) will notify you of your contribution room for each year. A one per cent per month penalty tax applies for over-contributions.

Unused contribution room can be carried forward like an RRSP, so if you can't contribute the maximum amount in any given year you can wait and contribute larger sums in the future when you have more money available. When withdrawals are made, your contribution room is not lost and the amount of the withdrawal is added back to your contribution room in the following year.

Although contributions aren't tax deductible, you don't pay tax when you take the money out, unlike an RRSP, and you don't pay tax on the investment income you earn while your money grows inside a TFSA. Although you cannot contribute directly to your spouse or common law partner's TFSA, you can gift money to your spouse so he or she can contribute to his or her own TFSA without the investment income being subject to the normal attribution rules as long as the investment stays in the TFSA.

Withdraw any time, for any purpose

The money you accumulate in a TFSA can be withdrawn at any time without tax consequences, and without affecting any federal income-tested benefits or tax credits you may be eligible for such as old age security, guaranteed income supplement, the age credit, the goods and services tax (GST) credit or the Canada child tax benefit. There are no time limits for withdrawing and no restrictions on how you spend your money.

Withdrawals increase your contribution room in the year following the withdrawal, allowing you to save again for another purpose.

Save, withdraw and contribute again

This example shows the flexibility of the TFSA. You don't lose contribution room if you don't use it because you can carry it forward, and you can withdraw your savings any time you need to.

Year 1	Annual contribution room	$5,000
	Contribution	- $2,000
	Amount to carry forward	$3,000
Year 2	Annual contribution room	$5,000
	Carry forward from year 1	+ $3,000
	Amount to carry forward	$8,000
	Withdraws $1,000 later in the year	
Year 3	Annual contribution room	$5,000
	Carry forward from year 2	+ $8,000
	Withdrawal from year 2	+ $1,000
Available contribution room		$14,000

Upon death

To maintain the tax-free status of the TFSA on death, you can name your spouse or common-law partner as the successor account holder. On your death your spouse would become the holder of the ongoing TFSA. Alternatively, subject to meeting certain conditions, he or she could transfer your TFSA assets or the value of the your TFSA to his or her own TFSA without affecting his or her contribution room.

If the plan cannot be continued as a TFSA with your spouse as account holder, or transferred to the TFSA of your spouse, the plan is taxed as a non-registered investment after your death.

Upon death, any unused TFSA room you had is lost.

Talk to your Quadrus investment representative to determine if a TFSA is right for you. He or she can help build the TFSA into your overall financial security plan so you can take advantage of the tax benefits.

The information provided is based on current tax legislation and interpretations for Canadian residents and is accurate to the best of our knowledge as of September 2008. Future changes to tax legislation and interpretations may affect this information. This information is general in nature, and is not intended to be legal or tax advice. For specific situations, you should consult the appropriate legal, accounting or tax advisor.

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46-6698-10/08