TAX MATTERS

Nine strategies for using a First Home Savings Account

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You may recall that the 2022 federal budget introduced a new type of registered savings plan, called the Tax-Free First Home Savings Account (FHSA). On Aug. 9, the government released draft legislation for FHSAs that expands on the rules in the federal budget. You'll find a great summary of those rules at canada.ca (enter "FHSA" in the search field).

Today, I want to share specific strategies to consider once FHSAs become available in 2023.

The accounts

1. Open an FHSA as soon as possible. If you're eligible for one, you'll receive $8,000 of contribution room each year, up to a lifetime maximum of $40,000, and you can carry forward unused contribution room. But the carry forward room doesn't accumulate until you open an FHSA. If, for example, FHSAs can be opened in 2023 but you wait until 2024, you'll be able to contribute just $8,000 that year. If, however, you open your account in 2023 yet don't contribute until 2024, you'll be able to contribute as much as $16,000 in that first year.

2. Choose the FHSA instead of the HBP. You won't be able to use the FHSA and the Home Buyers' Plan to buy the same home. My preference would be to use the FHSA instead because you can accumulate more for a down payment, and the HBP requires you to repay the amounts to your RRSP. Finally, the FHSA provides a tax deduction and the ability to save over and above your RRSP limits, while the HBP simply uses RRSP assets to help purchase a home.

The contributions

3. Make contributions early. A down payment for a home could amount to a lot of money. So get your FHSA working for you as soon as possible to allow for growth in the plan.

4. Contribute to an FHSA before your RRSP. If you don't have the funds to contribute to both an FHSA and an RRSP, consider using the FHSA first – even if buying a home is merely a possibility and not a sure thing. If you contribute, say, $40,000 to your RRSP

and this grows over time, you may then want to transfer these funds to your FHSA so you can make tax-free withdrawals to buy a home. But you can only transfer $40,000 tax-free, as any amount over that will be taxable if you transfer it. On the other hand, if you contribute $40,000 to your FHSA instead, the original amount plus the growth can all be withdrawn tax-free to buy a home. In addition, if you contribute to your RRSP first and then transfer funds to your FHSA, you won't get your RRSP contribution room back, whereas contributing to an FHSA can be done over and above the RRSP contribution room you have.

5. Contribute even if you're not sure you'll buy. You can contribute to an FHSA, and if you eventually decide to not buy a home, you can transfer those funds to your RRSP or RRIF. This doesn't use up any of your RRSP contribution room, so these funds can be thought of as additional RRSP savings in the long run, even if you choose to keep renting instead.

6. Give your spouse or adult kids funds to contribute. If your spouse or adult children are eligible to contribute to an FHSA but don't have the cash, consider giving them the money for contributions, if you can. The attribution rules won't apply on income earned in the FHSA. This could enable you and your spouse to save as much as $80,000 in FHSAs to help with a home purchase and could help a child buy a first home.

7. Borrowing to contribute might make sense. You might consider borrowing to invest in your FHSA. This will only make sense if the rate of return in your FHSA is higher than the interest rate you pay on the loan. You won't be able to deduct the interest on your loan.

8. Consider a contribution in-kind. If you don't have the cash to contribute, but you have non-registered investments, consider contributing investments in-kind. If the assets you contribute have appreciated in value, you could pay tax on a capital gain, but the deduction from the FHSA contribution will offset that taxable amount.

9. Defer the deduction if it saves more tax. You'll be entitled to a tax deduction for your FHSA contributions, but if you expect your income to be higher in the year or two after your contribution, you can defer your deduction and claim it in a future year. You'll save more tax if you claim the deduction when you're in a higher tax bracket.

I'll finish this conversation next time with more ideas related to withdrawals, investing your FHSA dollars and some nuances around these plans.

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