

TFSA or RRSP

Two of the most common investment questions asked are: “What is the difference between an RRSP and TFSA?” and “Which one should I choose?” The differences are outlined below and the decision to choose depends on a few factors: your current tax rate, your reason for saving, and your future tax rate.

The difference between an RRSP and TFSA

A registered retirement savings plan (RRSP) is primarily intended for retirement savings.

- > Annual contributions are tax deductible.
- > Your contribution limit is based on earned income.
- > Your contribution room begins at whatever age you begin working and filing a tax return.
- > It is based on 18% of your earned income in a year to a maximum of \$26,010 for the year 2017.
- > If you do not contribute to an RRSP, your contribution room accumulates and you can contribute even larger amounts in the future.

The Tax-Free Savings Account (TFSA) was introduced for the first time by the federal government in 2009, as a way for anyone 18 years of age or older, to set money aside tax-free throughout their lifetime.

Annual contribution limits amounts have varied over the years.

- > In 2009, 2010, 2011 and 2012 the room for each year was \$5,000.
- > In 2013 and 2014 the contribution amount increased to \$5,500 for each year.
- > In 2015 the contribution amount increased again to \$10,000.
- > However; the maximum contribution room for 2016 was reduced to \$5,500.

TFSA contributions are not tax deductible and contribution room accumulates if not used. Anyone who was 18 or older in 2009, and has not yet contributed, will have \$46,500 of contribution room available in 2016.

The chart below shows how different tax rates during your working years and retirement years can affect your decision to invest in an RRSP or a TFSA today, and the after-tax value after 20 years.

	Same tax rate today as in retirement		Higher tax rate today than in retirement		Lower tax rate today than in retirement	
	40% / 40%		40% / 30%		30% / 40%	
Marginal tax rate (contribution/retirement)	RRSP	TFSA	RRSP	TFSA	RRSP	TFSA
Contribution (before tax)	\$1,000	\$1,000	\$1,000	\$1,000	\$1,000	\$1,000
Tax payable	\$0	\$400	\$0	\$400	\$0	\$300
Net contribution	\$1,000	\$600	\$1,000	\$600	\$1,000	\$700
Investment income	\$2,207	\$1,324	\$2,207	\$1,324	\$2,207	\$1,545
Market value*	\$3,207	\$1,924	\$3,207	\$1,924	\$3,207	\$2,245
Tax payable	\$1,283	\$0	\$962	\$0	\$1,283	\$0
Account value (after-tax)	\$1,924	\$1,924	\$2,245	\$1,924	\$1,924	\$2,245

*Assumes annual 6% return over 20 years.