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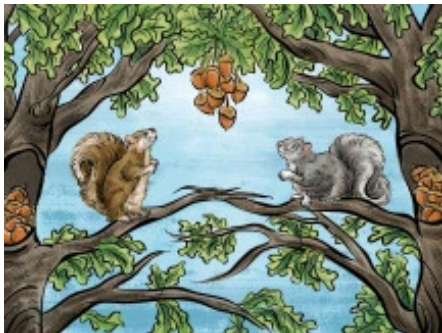
## Why you shouldn't risk over-contributing to your TFSA

By Jamie Golombek

*If you're hoping to make a \$10,000 TFSA contribution this year before the law officially changes, beware: The lower limit will be retroactive to Jan....*

It may be the middle of RRSP season, but Canadians still seem to be confused about TFSA contribution limits, carryforward of prior years' room and how withdrawals affect the amount you can contribute in future years. In some cases, this confusion can lead to penalty tax on over-contributions.

**As the TFSA accumulates more value, are RRSPs even relevant anymore?<sup>1</sup>**



This year's RRSP contribution deadline is Feb. 29, meaning that if you want to claim a deduction on your 2015 tax return, you need to make your contribution by midnight on that date.

But the bigger question is: should you even bother?

*Continue reading.*<sup>2</sup>

For starters, you need to determine your TFSA contribution limit, which is comprised of your unused contribution room from prior years plus the TFSA dollar limit for the current year. Under proposed legislation now before the House of Commons, the annual TFSA dollar limit for 2016 is decreasing from \$10,000 to \$5,500 and will be subject to indexation in future years.

While we've received a number of inquiries from opportunistic taxpayers seeking to take advantage of the higher \$10,000 limit before the law is officially passed, doing so would be a mistake since the reduced TFSA limit of \$5,500 will be retroactively effective as of Jan. 1, 2016. This could put taxpayers in an over-contribution situation and subject them to a penalty tax of one per cent per month on the amount of their over-contribution. If the Canada Revenue Agency takes the view that this over-contribution was deliberate, steeper penalties could be imposed.

Over-contributing to TFSAs has been a problem for years, mainly because of a misunderstanding of how withdrawals affect your contribution room. Withdrawals from a TFSA get added to your available TFSA contribution room the following calendar year. If you simply walk into your financial institution and withdraw all your TFSA funds and walk across the street to a competitor to make a new contribution, unless you have unused TFSA contribution room carried forward, you will be in an over-contribution situation and subject to penalty tax. The right way to do this is via a direct transfer from one institution to the other.

According to an internal CRA memo made public in December under the Access to Information Act, the CRA is considering some changes to the TFSA assessing system for 2016. The memo states that any taxpayers who exceed their TFSA contribution limit for the first time, will be sent a warning letter. If they still fail to remove the excess amount from their TFSA, they will be subject to an automatic assessment of tax on the excess contributions. The memo confirmed that the CRA had the legal authority to assess the penalty tax "without first contacting the taxpayer."

Fortunately, when the TFSA was launched in 2009, the rules contained a special provision allowing the CRA to cancel the over-contribution penalty tax provided the excess TFSA contribution, along with any income earned on that excess contribution, is fully removed from the account.

To request a waiver of the penalty tax, you should forward a detailed written request to the TFSA Processing Unit in Ottawa with all relevant information, including: your name, address, telephone number, social insurance number, the name of your TFSA issuer, the amount of tax for which a waiver is being requested and the years involved. A "complete history of events including what measures were taken, and when they were taken, to resolve the non-compliance, the facts and reasons supporting that the transactions that gave rise to the tax were mainly caused by factors beyond the taxpayer's control or by reasonable error."

In your letter, be sure to explain why your situation should merit relief.

*Illustration by Chloe Cushman/National Post*

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## References

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3. [jamie.golombek@cibc.com](mailto:jamie.golombek@cibc.com)

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