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The TFSA: 12 years on and growing strong

The new kid on the savings block isn't so new anymore. 2020 marks the 12th year of the Tax-Free Savings Account (TFSA). **More than 14 million** Canadians now have a TFSA, representing over **\$275 billion** in savings¹.

And there's more to come

The annual contribution limit is \$6,000, and unused contribution room accumulates. Those who've never contributed – and were age 18 or older in 2009 when TFSAs began – now have **\$69,500** in TFSA contribution room available. For many individuals, a tax-free savings opportunity awaits.

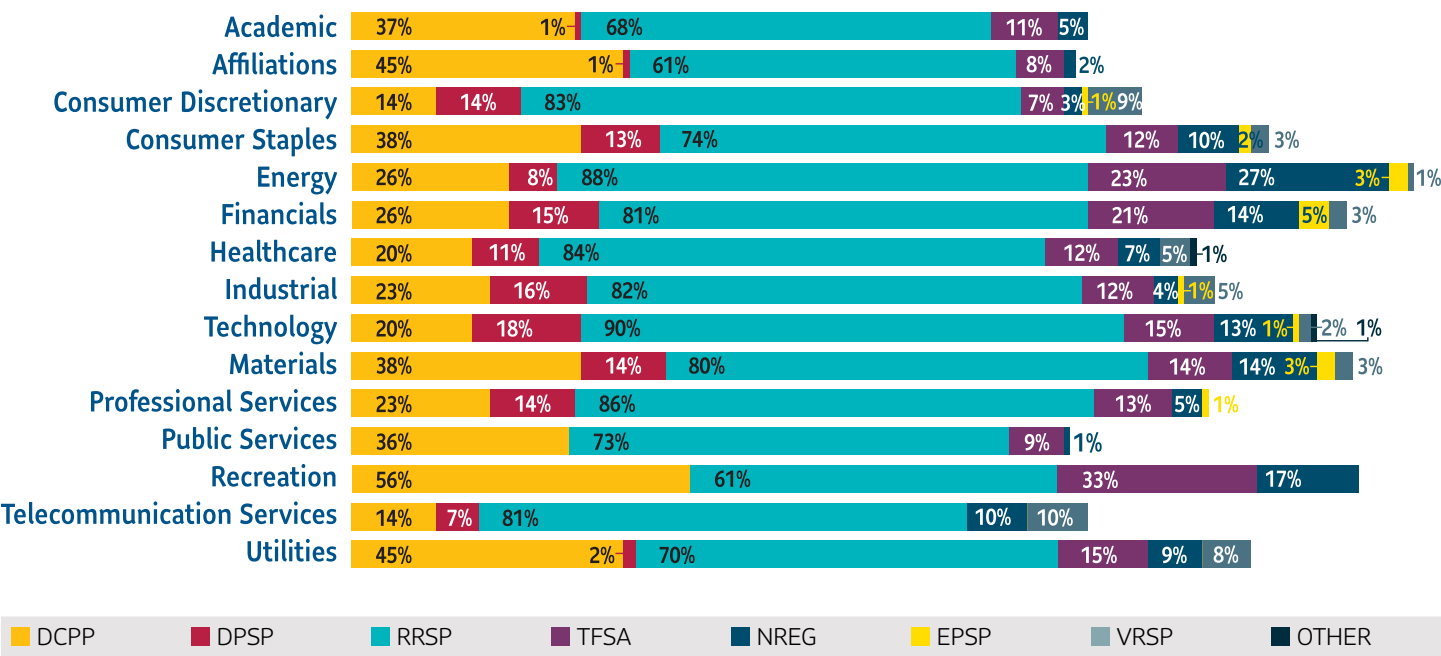
Of the \$275 billion in TFSA savings, **just \$1 billion is saved in employer-sponsored group TFSAs²**. Despite the popularity of TFSAs as a savings vehicle, a majority of employers have not introduced these solutions to their retirement programs. It may be time to reconsider.

There's an opportunity for employers too

Concerns about TFSA contributions cannibalizing long-term savings in group plans have failed to materialize. In fact, group plans that added a TFSA option saw total net contributions increase³. And familiarity with TFSAs is growing rapidly. The Canadian households making TFSA contributions (40.4%) now exceed those making RRSP contributions (35%) by a significant margin⁴.

Analysis – How TFSAs are being used in group plans

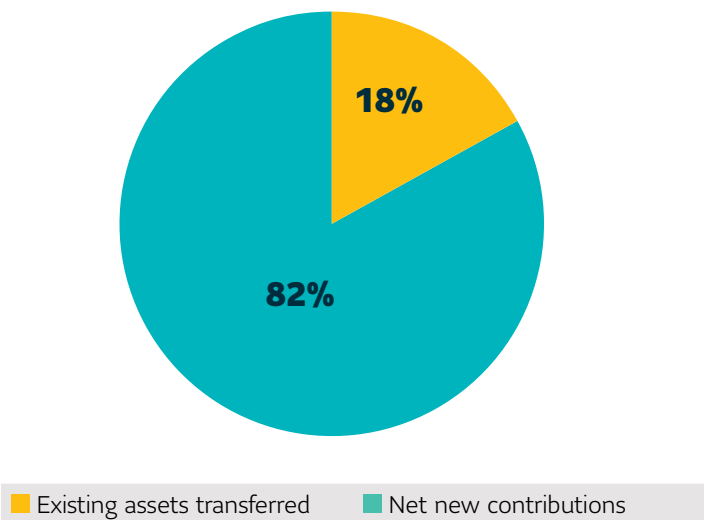
The current adoption of group TFSAs varies by industry, from a low of 7% in the Consumer Discretionary industry to a high of 33% in the Recreation sector.



As the graph shows, many group retirement plans have other long-established savings vehicles in place – namely defined contribution pension plans (DCPPs) and registered retirement savings plans (RRSPs).

For many employers, one of the concerns in introducing a TFSA is the fear that it will reduce savings to these other long-term savings plans. Based on our analysis of Sun Life’s capital accumulation plan database, that has not been the case.

TFSA member contribution sources



One in five plan members are redirecting existing assets from non-registered products to their TFSA, making more tax-efficient use of their savings. But most deposits involve net new contributions, meaning that **plan members with access to a TFSA at work are saving even more.**

And interestingly, despite their attractiveness as a short-term savings vehicle (whereby withdrawals can be made at any time and for any reason), the vast majority of employees saving in a TFSA at work are using it for mid to long-term savings purposes.

TFSA withdrawals by age

Age	% of members who have made withdrawal by age group
Under 20	20%
20 to 29	32%
30 to 39	36%
40 to 49	36%
50 to 54	32%
55 to 59	29%
60 to 64	28%
65 and greater	21%

The case for group TFSAs

Given that plan members with access to a group TFSA are using their plans effectively, the case for introducing a TFSA as part of a broader retirement savings program becomes more compelling.

For plan members, there can be a number of benefits:

Tax advantages

Generally, higher-income employees benefit most from making RRSP contributions. They contribute in their higher tax years (and can benefit from a larger tax deduction) and withdraw in their lower tax years in retirement.



TFSAs are ideally suited for the early-career millennial generation*, and for others with lower levels of earnings. They can make TFSA contributions in their lower tax years and withdraw their TFSA savings tax-free in their higher tax years. With millennials now the largest cohort in the workplace⁶, a TFSA savings option could be a timely addition.

Flexibility

Plan members can withdraw money from a TFSA at any time. And when they make a withdrawal, they can re-contribute this amount in any subsequent year – without reducing their future contribution room.



They also have complete flexibility in using their TFSA savings for any short, medium or long-term goal – from student debt repayment, to building a rainy date fund, to covering unexpected health care costs in retirement.

* According to Statistics Canada, in 2018 millennials earned lower incomes, on average, than older generations (between the ages of 34 and 65) did in the given year⁵.

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Advantages in retirement

One of the advantages of using a TFSA to provide retirement income is that withdrawals are not taxable income. This means they don't affect eligibility for income-linked government benefits like Old Age Security.



The clawback of Old Age Security benefits begins once your annual income reaches about \$79,000. And at an income of approximately \$128,000, it's fully clawed back. To avoid or minimize the impact, retirees could make annual withdrawals from both their taxable registered plans and their TFSA. This could keep their taxable income close to, or below, this threshold – and decrease or eliminate the clawback of Old Age Security benefits.

Retirees can also consider using a TFSA if they're receiving an income they don't need at the time. While RRSP contributions must end by age 71, TFSAs have no cut-off age for contributions. This means that any additional savings during retirement can benefit from tax-free investment growth in the TFSA.



Future decumulation innovations with TFSAs?

The TFSA has the potential to become an even more valuable part of workplace retirement savings programs.

The C.D. Howe Institute's recent e-brief, **TFSAs: Time for a Tune-Up**⁷, proposes several TFSA innovations that could enhance their effectiveness as a retirement savings vehicle.

A key proposal is to let people buy an annuity within their TFSA, just as they can with RRSPs. The CLHIA has also been a strong advocate of this change⁸.

Annuities purchased with RRSP funds preserve the tax deferral on the income earned within the annuity. However, it's not currently possible to buy life annuities within a TFSA and preserve tax-free investment income.

The federal government has recently shown a willingness to address decumulation issues – with the introduction of two new types of retirement income solutions: the Advanced Life Deferred Annuity (ALDA) and the Variable Payment Life Annuity (VPLA). If it extends this innovative thinking to allow for TFSA annuities, the TFSA could become an even more valuable part of workplace retirement savings programs.



TFSA benefits for plan sponsors

While plan members can benefit from a TFSA in a number of ways, the TFSA option also offers potential benefits to plan sponsors. These include:

Recruitment and retention

TFSA's have become the savings vehicle of choice outside of the workplace. For this reason, a TFSA could be a valued addition to your current retirement and savings plan, providing plan members with convenient access to a simple, tax-effective, highly flexible way to save. With a tight talent pool – and high millennial interest in saving for broader goals – it makes sense to consider a TFSA within the context of your employee value proposition.

Productivity and retirement readiness

Adding a TFSA to your lineup helps employees build healthy savings habits, prepare for the unexpected and improve their overall financial well-being. This in turn leads to a more engaged and productive workforce.

A TFSA can also be used to incent higher levels of retirement savings, such as through matching contributions. For instance, an employer might choose to match TFSA contributions, but have the match directed to the employee's Group RRSP or DCP. The plan member builds both their flexible TFSA savings (for medium or shorter-term goals) and their RRSP or pension savings for retirement.

Given that it has become the savings vehicle of choice outside of the workplace plan*, it makes sense to consider the TFSA within the context of your employee value proposition.

*Since its inception, average annual contribution amounts to the TFSA have consistently exceeded those made to the RRSP for individuals aged 20-29. In recent years, this greater interest in the TFSA has also been seen with those aged 30-44⁹.

Strategic role in compensation

A TFSA can be used strategically by your organization to provide broader compensation options for plan members. For example, a TFSA can be used as a deposit option for bonuses, excess health credits, or expense reimbursements.

Overall plan growth

Our evidence shows that offering a TFSA promotes increased savings and helps grow your plan assets. This helps drive down overall costs and generates opportunities to enhance the value of your workplace savings plan – representing additional benefits for members, beyond those they already reap from lower fees (than those typically available at a retail level).



Adding a TFSA option to your existing group retirement plan can add considerable value, at little or no cost to your organization.

Explore the TFSA fit for your organization

The retirement savings landscape is evolving, and TFSA's are playing an increasingly larger role. They're now the dominant tax-free savings vehicle in Canada – with the fastest growth in adoption among millennials, the largest cohort in the workforce⁹.

Organizations that have introduced TFSA's to their group plans have seen an overall increase in plan member contributions. And while some TFSA assets are used for shorter-term financial goals, a surprising number of plan members are retaining their TFSA assets for retirement or other longer-term goals.

While a TFSA is not a retirement savings solution in itself, it can play a valuable role in providing plan members with a flexible and tax-effective source of retirement income during their decumulation years.

Additionally, the overall impact that offering a TFSA can have on your workforce and broader corporate objectives should not be overlooked. **By including it in your benefits package you're promoting financial and mental health, greater employee resilience and more sustainable outcomes.**



Sources

¹ Statistics Canada, Tax-Free Savings Account statistics (2017 tax year)

² Strategic Insight and Statistics Canada, Sun Life 2019 Designed for Savings

³ Sun Life, 2019 Designed for Savings

⁴ Statistics Canada, 2016 Census, Household contribution rates for selected registered savings accounts

⁵ Statistics Canada, Table 11-10-0239-01, Income of individuals by age group, sex and income source

⁶ Statistics Canada, Table 14-10-0017-01, Labour force characteristics by sex and detailed age group (January 2020)

^{7,9} C.D. Howe Institute E-Brief: TFSA's: Time for a Tune-Up, December 2019

⁸ Canadian Life and Health Insurance Association (CLHIA), 2019 Federal Budget Submission