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First Glimpse at First Home Savings Account

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In recent years, home ownership is increasingly becoming an unattainable dream for many Canadians.

Governments at all levels have been using various policies to approach tackling the problem. Recently, the Federal Government has tried to combat the issue by pulling another fiscal policy lever. In her 2022 budget, Finance Minister Chrystia Freeland introduced a new tax-free savings plan aimed at responding to what she referred to as the "intergenerational injustice" for new homebuyers in Canada.

Namely, the budget proposes a First Home Savings Account (FHSA) that would offer certain taxpayers a new way to jump-start their new home nestegg. Although the budget was passed by parliament in June, at the time of this writing the legislation codifying the new FHSA has yet to be introduced to the House of Commons; the program could therefore be subject to change before receiving royal assent.

In the meantime, here is what we know so far.

- Starting in 2023, the FHSA would allow certain taxpayers to contribute up to $8,000 per year to the account—to a lifetime maximum of $40,000.
- An individual would be allowed to carry forward unused portions of their annual contribution limit up to a maximum of $8,000.
- In other words, an individual contributing less than $8,000 in a given year could contribute the unused amount in a subsequent year on top of their annual contribution limit of $8,000 (subject to their lifetime contribution limit).
- For example, an individual contributing $5,000 to an FHSA in 2023 would be allowed to contribute $11,000 in 2024—$8,000 plus the remaining $3,000 from 2023.
- Carry-forward amounts would start accumulating only after an individual opens an FHSA for the first time.
- Therefore, an individual who waits until 2024 to open an FHSA would not be permitted to contribute $16,000 in 2024, whereas an individual who does open an account in 2023 but who waits until 2024 to make a contribution would be permitted to contribute $16,000 in 2024.

The FHSA has key benefits that are characteristic of existing registered savings plans. Specifically, contributions made to the plan would be deductible from taxable income, similar to contributions made to an RRSP; income earned from investments made in the account that is used to make a qualifying home purchase would not be subject to tax, similar to a TFSA.

As is true with RRSP deductions, plan holders would not be required to claim a deduction for the tax year in which a contribution is made; such amounts could be carried forward indefinitely and deducted in a later taxation year. Unlike RRSPs, there would be no provision for deductions made to a spouse's FHSA.

Although unused contributions can be carried forward indefinitely, the FHSA itself has a finite lifespan and must be closed after 15 years, irrespective of whether the funds were utilized to purchase a home.

Unused funds, however, could be transferred to an RRSP or RRIF on a tax-deferred basis, penalty-free—and without impacting the taxpayer's contribution room.

For those who may have utilized all their RRSP contribution room from earned income, but who are not contemplating home ownership, this provides an opportunity to increase their RRSP contribution room without attracting the usual punitive penalties for overcontributing to an RRSP.

To be eligible to open an FHSA,

- you must be a resident of Canada for income tax purposes;
- you must be at least 18 years of age; and
- you must not have lived in a home that you owned at any time in either the year the account was opened or any of the preceding 4 calendar years.

For example, if you previously owned a home that you sold in 2018 and you have since been renting or otherwise living with someone who is not your legal spouse (such as parents or siblings), you would be considered a first-time homebuyer in 2023 for the purposes of the FHSA.

There is, however, an exception to allow individuals to make qualifying withdrawals within 30 days of moving into their home. Of note, ownership is defined broadly for the purpose of the FHSA and includes beneficial ownership, not just legal ownership.

There would be no limit to the number of accounts any one individual can hold; aggregate contributions among all accounts would be subject to the annual and lifetime maximums, however.

Moreover, individuals would be limited to making nontaxable withdrawals from an FHSA for one single property during their lifetime; once a withdrawal is made to purchase a home, the account must be closed within a year from the withdrawal date.

Once a tax-free withdrawal has been made, the individual would not be eligible to open another account, meaning that an individual with multiple accounts who makes a tax-free withdrawal for a purchase, would need to withdraw all funds from all accounts when making the home purchase or otherwise be prepared to make a taxable withdrawal of unused funds or transfer them in kind, as described above.

Taxpayers would generally be responsible for ensuring they do not exceed their contribution limit in a given year, although the Canada Revenue Agency (CRA) would provide basic FHSA information to support taxpayers in determining their available contribution room.

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To illustrate the significant financial benefits of the FHSA, consider the following scenario.

- Assume you were to contribute the annual maximum $8,000 to your FHSA in each of the next 5 years, starting in 2023. All else being equal, fully utilizing the deductibility of the contributions would reduce your taxable income by the same amount. Assuming your combined marginal tax rate is 45.8 per cent, you would save $18,320 in taxes ($40,000 X 45.8%).

If the investments in your FHSA realize an annual rate of return of, say 8 per cent, the total "return" on the $40,000 invested in just those 5 years is $25,252—more than 63 per cent overall, turning your $40,000 into $65,252.

Note: That is a simplified example for the purposes of illustrating the advantages of the FHSA. Numerous factors could influence the outcome; readers are encouraged to seek the advice of an income tax professional to assess their individual financial outcome.

- With the average home price in British Columbia now over $900,000, that would allow you to save for a down payment in 5 years—at least 2 years sooner than investing that same $8,000 annually without the tax advantages of the FHSA, all else being equal.

It is interesting to note that the new FHSA does not replace the existing Home Buyers' Plan (HBP); rather, it provides an additional option for using savings to access the property ladder.

The HBP would continue to be available as under existing rules, but you would not be permitted to make both an FHSA withdrawal and an HBP withdrawal in respect of the same qualifying home purchase; funds currently held in an RRSP, however, can be transferred to an

FHSA (subject to the contribution limits mentioned above).

There are some obvious advantages to the FHSA plan over the HBP program.

For instance,

- the FHSA plan allows for access to a higher maximum-funding amount;
- any funds currently invested in your RRSP will remain in place to continue to generate a return; and
- of course the funds don't need to be repaid.

That is not to say the HBP won't continue to have relevance—if not just in the near term. When weighing the two programs, your time horizon for investing and saving to purchase a home and making the actual purchase transaction is an important consideration.

- For instance, if you're planning to buy a home in 2023, you would be able to contribute only $8,000 to an FHSA. If you have sufficient funds already invested in your RRSP, however, making a withdrawal under the HBP would allow you access to up to $35,000.

Based on the information currently publicly available, there are clear benefits to the new FHSA.

Until final legislation receives royal assent, there is also uncertainty. Readers are cautioned that further review will be necessary once the final rules are announced. ▲

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