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TFSA Designations Matter

The method that you use to name a successor, owner or beneficiary of a TFSA makes a big difference to your estate, not only for a TFSA to maintain its tax-exempt status but also to ensure that the assets are distributed to the intended recipients.

You can name your spouse or common-law partner as a successor-holder or anyone else as a beneficiary. The successor-holder and beneficiary designations vary across provinces (for example, Quebec only allows transfers to be done via the deceased's estate). A successor-holder trumps a beneficiary if both are alive at the time of the original plan holder's death. Moreover, a beneficiary trumps the deceased's estate if the successor-holder is also dead. If neither is specified, the assets in the TFSA account become part of the deceased's estate, losing their tax-sheltered status and becoming subject to probate fees.

As you can see from the above scenario, some thought is necessary to be able to approach how you fill out the application for your TFSA. In addition, you may also need to review the elections you have made for an existing TFSA.

Naming a surviving spouse as the successor owner results in the assets held in the TFSA to roll over immediately to your spouse without losing the TFSA's registered tax status. By doing this, the spouse now assumes ownership of the TFSA contract and all of its investments.

By stepping into the ownership shoes of the deceased, the new owner has all the same privileges of any TFSA account owner, such as making tax-free withdrawals from the deceased holder's TFSA. The new owner's TFSA contribution limits are unaffected as it is possible to maintain two separate TFSA accounts or consolidate their own with that of the deceased for better investment management.

On the flip side, naming a spouse or a common-law partner as a beneficiary results in some additional complications. There is additional paperwork for the surviving spouse, as well as decreased tax sheltering. Similar to the successor-holder designation, a beneficiary designation also allows the surviving spouse to retain the tax-sheltered status of the TFSA without affecting his or her contribution room. However, this happens thanks to an exempt contribution of the deceased holder's TFSA assets to the beneficiary's TFSA plan, which cannot exceed the market value of the original owner's TFSA on the date of his or her death.

Moreover, any change in value between the original owner's death and the exempt transfer by the beneficiary cannot be transferred to the surviving spouse's TFSA. As a result, any such excess is no longer tax-sheltered. Interestingly enough, the excess amount would likely be small if the exempt contribution is done shortly after the death of the original owner. However, such matters often get neglected around the time of a spouse's death. The surviving spouse has to notify the CRA within 30 days of the exempt contribution (or the transfer of the original owner's TFSA assets) using Form RC240.

As a result of these complications, the preferred route is naming a spouse (or common-law partner) as a successor-holder in the TFSA contract with the financial institution.

Most provinces allow a TFSA holder to designate both a successor-holder and a beneficiary. If the original holder and the successor-holder die at the same time, the beneficiary can get the money without having to go through probate, depending on where the asset is held. Therefore, most plan holders prefer to designate both a successor-holder and a beneficiary.

It is recommended to confirm that both options are available in the contract of your financial institution of choice since not all of them allow both a successor-holder and a beneficiary designation, even though the law in most provinces allows both.

To summarize, it is important that Canadians co-ordinate their successor-holder and beneficiary designations with the wishes of their Wills to avoid any future complications for your Executor.

Please contact us at [\(289\) 235-9223](tel:2892359223) [1] if you wish to review your current TFSA account designations.

Regards,

Tom

Do you have questions about your investment strategies?

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