Take advantage of the new First Home Savings Account

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Keith: Welcome to the Empowered Investor. My name is Keith Matthews and I'm joined by my co-host Marcelo Taboada. Marcelo, how are you today?

Marcelo: Keith, I'm good. Two podcasts in a row in person. I'm happy we're doing this.

Keith: I expect that every podcast from here on in is done face to face, live in a conference room. So great to be doing it.

Marcelo: It's still taking me time to get used to it.

Keith: What we used to do for three years during the pandemic is do it behind the screens and Zoom calls, either from home or one from the office. So it's really unique to be able to be together face to face.

Marcelo: And the pandemic is officially over.

Keith: I hear that.

Keith: So what's going on in the office in the next month or two, Marcelo?

Marcelo: Oh, it's super exciting. We hired a bunch of people now; the team is looking great. There's a great vibe in the office. Now we're going through renovations, so the office will look more modern. A bunch of guys are doing Spartan races. There's a good vibe going around in the office, which if you plan to be lazy, it's hard because everybody's doing all these crazy workouts and exercises and races.

Keith: And I saw this week that everybody went for a team walk after lunch just to go outside. It was beautiful and got some exercise in. We also are going to have our very first company party. We've been doing these for 20 years in the summer where all of the team come with their spouses, their partners, and their kids. And so this will be the first time we'll be able to pull it off in the last three years in a big fashion. So we're really looking forward to that in a couple of weeks from now.

Marcelo: Well the last one we had was 2019, and after that, we had a few, but it was still during COVID—people wearing masks inside, keeping social distancing. So it's going to feel great.

Keith: Yeah, that's great. So today what we're going to talk about is the First Home Savings Account. We did one together, Marcelo, about six months ago when it was first announced. But when we did it, we knew that there were some gaps of information, at least three or four very important gaps that were just not disclosed at that point. So now, as they're getting ready to be rolled out, we understand all the issues. It's much clearer, and we're going to walk through that account in today's episode. Specifically, we're going to talk about what is a First Home Savings Account and how does it work? We'll discuss why the government created this account, who benefits from the account, and then finally we'll have a bit of a discussion around whether it really solves the affordability problem that's here in Canada right now. Home affordability. Marcelo, what's the underlying issue, what's the underlying challenge that is trying to be addressed by this account?

Marcelo: The government's feeling a lot of pressure because people are complaining, and we have a housing affordability crisis in Canada right now. That was coupled with low supply, low interest rates, and generational change as well. People living in their homes and more young people trying to get into the housing market. So that's created an imbalance in the market where houses are extremely expensive, young people can't afford them, and they're putting pressure on the government. They're making their voices heard when it comes to public opinion. So the government comes out with this account, and they created it to help this problem.

Keith: Okay. That's a good explanation. In addition to that, this week Rob Carrick out of the Globe and Mail had a survey, and it's his own survey that he does with his newsletter where he surveyed young Canadians between the ages of 20 and 40, asking them about how they feel about home ownership and the opportunity to buy. And of course, it's based on the fact that it's not affordable. And the stats were very telling. So 39 percent of those that responded are furious about the housing market. Twenty-nine percent are frustrated about the housing market. Fourteen percent are angry about the housing market. And at the end of the day, only less than 2 percent are actually hopeful about the housing. So these are tough statistics that we're now starting to see based on younger Canadians and how they feel about homeownership. So this account is a small step in terms of trying to help. We'll discuss how it works, and at the end of the day, we'll also discuss the type of impact it might have.

Marcelo: Yeah, there's definitely a general sense of despair in young people in this country right now. And when I say young people, I include my peer group as well. I have friends who are both having great incomes, two household incomes, and they've been trying to buy a house for the last four or five years, and they just can't find something reasonable within what's acceptable for them. And a lot of people will say, "I don't want to drive three hours a day to own a home."

Keith: So Marcelo, your friends live in Montreal.

Marcelo: Yes.

Keith: Montreal is considered an affordable city. Imagine if they were in Toronto or Vancouver.

Marcelo: Not even close.

Keith: So this affordability issue is popping up around the country right now. And it's not a big city issue. It's even a smaller city issue. So this account is an interesting one. It's expected to be opened pretty much in most financial institutions in the fall of 2023. The way it works is now much clearer than six months ago. So we're going to go into some of these details right now. Let's start with what is—I guess technically there's some confusion as to what this account is called. People throw the word tax-free at the beginning of the account or the end of the account, but officially this account is called a First Home Savings Account. What essentially is the gist of the account?

Marcelo: Perfect. It is a vehicle that allows people to save for a first home purchase. The account is tax-sheltered and provides also a tax deduction and contributions. It is a vehicle where people put in money, they get a tax deduction, the money grows tax-free, and then you can use it to buy a house. That's the cream of the account, pretty much.

Keith: Now essentially, we have another type of account that financial institutions will offer its clients. We've had the RRSP for many decades. We've had the tax-free savings account for a decade plus. We have non-registered accounts, we have RESP accounts, we have disability savings accounts, and now we have the First Home Savings Account. Okay, good. So how exactly does it work?

Marcelo: Okay, so let's go through the facts here. You must be a resident of Canada. The age of majority is 18, 19 in some provinces. So you have to be of the age of majority, and you have to be younger than 71. So those are the age ranges.

Keith: Essentially an adult.

Marcelo: Correct. It'll become available again, like you said, in the fall of 2023. We still don't have an exact date, but we know that it's going to be available. To use this account, it requires you to not have owned a home in the previous four years. This is key also. If your spouse owns a home, you can only open an FHSA if you did not live in that home in any of the four previous years. And as for dollar contribution wise, it's $8,000 per year up to a maximum of $40,000.

Keith: Okay. So those are the basics. What about any unused carry forward?

Marcelo: You can use it. So if you don't use the $8,000 in one year, you can catch up the next year but up to a maximum of $8,000.

Keith: So you get one year of unused to catch up, but you never lose your $40,000. You just can't catch up all at once.

Marcelo: Correct.

Keith: That makes sense. So in essence, in summary, what exactly does this account provide?

Marcelo: It provides a vehicle where people can save for a home tax-free and also get the benefit of the RRSP because a lot of people traditionally will be saving in an RRSP. "I can use my home buyer's plan," and then you still get that tax deduction with this account. You're getting the tax deduction. So if I put $8,000 today, let's say I don't own a home. I am going to get those $8,000 of deduction, but the money grows tax-free. And when I take it out, it's not taxed.

Keith: Okay. So that's the crux of it. You get a deduction like an RRSP, your money grows tax-free like an RRSP. And here's the big bonus: now when you take it out, you don't get taxed. It looks like a tax-free savings account a little bit when you take it out, and you take it out when you have a contract, when you have an agreed-upon contract to either buy or build a home. Okay. So what about the old home buyers plan? Six months ago there were questions as to whether you could use both the home buyers plan and this new account. Can you use them together?

Marcelo: Yes. So that was some confusion that we had at the beginning, that we were still fuzzy about the details regarding that. I think initially they had said you can't use both of them, but now the government has said that you can. So for example, let's say a young person is saving for five years, saves $8,000, and then already has $35,000 in their RRSP. You can combine both of them and use $75,000 to buy your first home. Now the home buyer's plan is not changing. It's staying as it is. Just be clear about that. You can combine both and use $75,000. If your spouse is doing the same, you can combine them both to a purchasing power or a down payment of $150,000 using both plans. So that's important to know.

Keith: Okay. And that really favors the higher-income younger individual who's making RRSP contributions and, in addition to that, has the ability to put money aside. But that's a fairly sizable amount that young individuals can build in a matter of hopefully four to eight years.

Marcelo: Yeah. The other thing that we need to mention also is, for example, if you make an RRSP contribution, you can decide not to use that deduction today. So if I'm 25 and I know I'm going to earn more money in the future, it benefits me to put in my RRSP and not take the deduction today because I know I can use it at a higher marginal tax rate later on. The FHSA does the same thing. You can delay the deduction. You can put it in this year, not take the deduction, and use it in a future year.

Keith: Okay. That's critical because that's one of the pieces of information we did not have six months ago. And so what you're speaking about here is—and this is often where even a parent or grandparent may gift a younger person money into that account while they're, for example, a university student or while they may have just started and they don't have a larger income—but the younger person does not need to use the deduction. They can defer the deduction a year, two, three, four, five until they have a higher income. That's a pretty major point. Okay. So what would be the last point? Let's say you go through here, you build up a plan, you don't actually buy a house. And I believe you're allowed to have money in the account for 15 years, and you don't buy a house. What are your options for someone who's renting and chooses not to buy a home?

Marcelo: Yeah, you can transfer it into your RRSP. And even if you don't have room in your RRSP—so just to be clear about this—so let's say you have a person who rented their whole life, maxed out their RRSP, and also opened this account hoping that they'll buy a home but never did. Fifteen years go by, they can take that FHSA account and roll it over into the RRSP even if they don't have RRSP room. So that's the key fact about this account that after 15 years, you can put it back into the RRSP without needing the room. So that's important to know because a lot of people will say, just to give you a very basic example, let's say you've maxed out your RRSP contributions. You have zero. The moment the 15-year mark comes, you've put $40,000 into your FHSA. It's grown to $60,000, just for argument's sake. You can now take those $60,000 and roll it over into the RRSP even if you don't have RRSP room.

Keith: Yeah. So essentially, some people have discussed this as odd. This seems like a loophole. It seems like it's not well thought through, but essentially that's the way it is for now. Which means if you don't buy your house, you can roll extra money into your RRSP. As an aside, I think there's a conversation that seems to be starting, and I'm seeing it in newspapers and journalists who are writing that renters need to be given some sort of additional perhaps benefit—a saving benefit—because they're foregoing tax-free capital gains in principal residences. And so there's an equity, a fairness issue here that's being discussed. Maybe this is one area where they're saying, "Let's give something back to those who choose to rent." This is a bit of an aside here, a tangent. The other one I've heard of, which I think makes sense, is if you rent long term, you should be allowed to have a larger tax-free savings account contribution than somebody who owns a home.

Marcelo: That's an interesting concept.

Keith: I read it out of an article in the Globe and Mail. I thought it was a very smart suggestion. But let's get back to this plan here for a sec. So what's the main difference between this plan and the home buyer's plan?

Marcelo: So essentially, the FHSA, you save your $8,000 every year. It grows tax-free. You take it out when you buy a home. So in the RRSP, you can take out—the government allows you to take $35,000. That's the maximum. You can take less, but the maximum is $35,000. You can use it to buy a home. It's tax-free, but you have to repay it in 15 years.

Keith: Ah, that's the difference. So one is you have to repay, which is the home buyer's plan, and the First Home Savings Account you don't need to repay. It's a saving mechanism. Once you take it out, it's done.

Marcelo: Correct. And in the RRSP, it's also important to know because there's one key fact that once you take the money out for the home buyer's plan, it'll be divided by 15, and that's the amount you have to repay every year. Let's say one year you're tied in a tough financial situation, you can't do an RRSP contribution. That home buyer's plan repayment for that year gets added to your taxable income. So that's different from the FHSA, where you don't have these repayments to make. Don't get me wrong; it is a good thing that you have to repay it because at the end of the day, you're borrowing from your future self, and you want that money in your RRSP for retirement. But the FHSA has that flexibility that the home buyer's plan doesn't have.

Keith: Okay. That's great. So let's discuss a little bit about who benefits from this account.

Marcelo: So it's clear that the main people who benefit are young people who want to buy a home. They now have this vehicle available to them. It also benefits people who are in the older stage of their career—retired grandparents who have sizable assets and they want to help their kids or grandkids buy a home. They can start gifting this money, $8,000 a year, so the young person can put it into this account. So I think those are the two groups that get benefit from something like this.

Keith: You're right. The actual individual that benefits the most is the buyer, the home buyer, the person who's looking to buy their first home by increasing their ability to save. It doesn't necessarily solve the issue in Canada. We'll talk about that from a supply perspective, but it allows them to build the nest egg a little faster. And then the second part you're alluding to is, and we see this in our client base, individuals, parents, or grandparents who we know they have surplus in their accounts, they've saved hard, and they wish to help their kids, their adult kids in the future. This is a great way for them to help. When we have proposed it to some of our clients, the clients sit back and go, "This is an amazing concept. I would like to help my grandkids." And they're basically saying, "Look, let me help set it up." And for the grandkids who might even be in university, the university student will simply defer the deduction.

Marcelo: Absolutely. You do five years of that. You have $40,000 of deductions, and you can use them in your peak earning years when you're 30, 35, 40 if you want.

Keith: Okay. That's amazing. That is really great. What's the criticism? We're starting to see a few criticisms now about the account, not so much in terms of how it works and do people benefit because clearly people do benefit. I think the criticism is more geared around whether it solves the problem.

Marcelo: Yeah, I think the broad criticism has been that it does not help the problem because you're just fueling the demand side even more. So the question is, I could see politically how it's an appealing decision from the government to make because it does create the impression that you're helping the people trying to buy a home. But from the get-go, the housing problem in Canada has never been, "Do we have enough demand, or can people actually put in the money to buy a house?"

Keith: Hang on. There has been a problem with regards to individuals having to save for a down payment. It takes a ridiculous amount of time for a young person to save.

Marcelo: Correct. But it's a result of the supply problem. And because supply has been so limited, the housing prices have gone up significantly, and that makes it so that young people have to pay more to buy a home. So at the end of the day, you're helping the side of the demand. You're not helping the supply side. And if we fix the supply and we have a balanced situation where we have more housing, that'll help the problem even more than just creating an account that gives more purchasing power to people.

Keith: Yeah. Some of the best writers on this subject that I've been following have put together some really interesting comments. And they've said essentially the federal government, with its policies on immigration—and I think that everybody in Canada knows we need to have an open immigration policy where we bring more people. We need individuals to help grow the economy, grow our society. But the federal government controls the levers on immigration. It's controlling levers on these types of homebuyers plans. So it's controlling and fueling demand, but it's not in charge of supply. And supply is controlled by municipal governments across this country, and municipal governments seem to be counter-densification. On the one hand, you've got the federal government pushing the demand button, and then municipalities holding back on the supply button, and that is creating an imbalance. And until things become more balanced, we're going to be struggling a little bit on this. But at the end of the day, we can see a lot of our clients' families benefiting from this account. We can see a lot of Canadians benefiting from this account. And so we're excited about it. We expect to see these accounts opened up with our custodians, either National Bank or Credential. And Canadians will see this across all of their financial institutions in the fall. So, Marcelo, last comments for today's episode.

Marcelo: My takeaway is make sure you get the facts right, inform yourself, and if you have any more questions, don't hesitate to reach out. We have the episode for this reason—to help you make informed decisions. And the account will help a lot of people. Just make sure you know what you're doing because if you're planning on doing RRSP contributions and FHSA, you may want to think about what your strategy will be and use the accounts properly.

Keith: Those are great takeaways. Thank you. I'll also add, I think for younger individuals between the ages of, call it, 22 and 40, there are now more opportunities to move forward. There are now more opportunities to save. It's actually getting trickier because in the old days it was just an RRSP. Now individuals have to choose RRSP, tax-free savings account, and First Home Buyers Account. So lots of different— First Home Savings Account. That's how tricky this one is.

Marcelo: We're getting confused already.

Keith: Yeah. So I think there's opportunities, and I think it's amazing. So thank you, Marcelo, for participating. I'm happy that we're able to do today's show because it does clear up a lot of what's going on with this very important new account.

Marcelo: Thank you for listening.

Keith: Thanks guys, see you next time.

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