Is it a good idea for parents to gift money to children for the Tax-Free First Home Savings Account?

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If the child doesn't buy a home, the money in an FHSA can be transferred to an RRSP within 15 years of the plan being opened or by the time they're age 71, whichever comes first.

EVAN BUHLER/THE CANADIAN PRESS

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The Tax-Free First Home Savings Account (FHSA) is expected to take effect in the coming months and advisors are fielding a flurry of questions from parents about how to take advantage of the plan to get their adult children into the housing market.

The FHSA, announced in last year's federal budget, is a registered plan giving individual home buyers the option to save up to $8,000 a year – to a maximum of $40,000 – tax-free. The program is for first-time home buyers or anyone between ages 18 and 71 who hasn't bought a home in the current or prior four calendar years.

FHSA contributions are tax-deductible like a registered retirement savings plan (RRSP). Also, any investment income generated in the FHSA is non-taxable, similar to the tax-free savings account (TFSA). The major difference with the TFSA is that the FHSA has a 15-year time limit before the funds need to be withdrawn, whereas the TFSA has no time restriction.

The FHSA comes into force on April 1, but experts say it could be summer before the system is up and running at financial institutions.

Late last year, the government amended the legislation to enable homebuyers to use the FHSA and the Home Buyers' Plan (HBP), which has a withdrawal limit of $35,000 from an RRSP, for the same home purchase. The FHSA and HBP funds can also be combined with more than one person such as a couple buying a home together. With a couple, each person can put a minimum of $75,000 ($40,000 from the FHSA and $35,000 from the HBP) – or a combined $150,000 – toward a qualifying new home purchase. The FHSA minimum of $40,000 doesn't include any potential gains made on the original investment.

Jamie Golombek, managing director of tax and estate planning at CIBC Private Wealth in Toronto, has been getting a lot of questions lately from parents looking at ways to help adult kids buy their first homes. While parents can't contribute directly to a child's FHSA, Mr. Golombek says they can gift the kids the money.

"It's another great way to do intergenerational tax-free wealth transfer," Mr. Golombek says, adding that the earlier families start planning, the better the tax-saving and investment benefits will likely be.

For example, he suggests gifting each child $8,000 a year for the FHSA once they turn 18, so they can invest the money and allow it to grow for a future down payment. It's similar to the advice he gave parents and grandparents when the tax-free savings account started in 2009. Now, he recommends starting with the FHSA before the TFSA.

"Mathematically, your best bet is the FHSA. Where do you have a product in which you get the tax deduction on the way in, no tax throughout, and tax-free on the way out?" Mr. Golombek says

"If the money is going to them anyway, at the end of the day, why not take advantage of the kids' contribution room?" he adds.

Another benefit is that the FHSA tax deduction can be carried forward, similar to what's possible with an RRSP, he notes.

Is homeownership a priority?

Zainab Williams, certified financial planner (CFP) at Elleverity Wealth Management in Caledon, Ont., says parents should discuss homeownership goals with their adult children before earmarking funds for the FHSA.

A TFSA might be a better use of the funds if homeownership is not a priority, she says, because it's more flexible for other uses.

"If you want your child to be a first-time home buyer and they want to take advantage of deductions, then definitely give them the funds to invest through their FHSA over the TFSA," she says.

Ms. Williams notes that if the child doesn't buy a home, the money can be transferred to an RRSP within 15 years of the plan being opened or by the time they're age 71, whichever comes first. She also warns that if you transfer funds from your RRSP to fund your FHSA, your RRSP's contribution room is lost forever. It doesn't get replenished as it does with the TFSA.

She also points out that, unlike an RRSP, FHSA contributions made within the first 60 days of the calendar year can't be attributed to the previous tax year.

Rachel Metzger, CFP at Caring for Clients in Kitchener, Ont., says parents need to consider the impact on their own financial and tax situations when gifting money to kids for an FHSA.

"If they're going to sell investments, then they have to look at the tax implications," Ms. Metzger says. "Are there other sources they can use for the funds without triggering a capital gain," such as cash or high-interest savings accounts?

Parents also need to consider the risk of their kids not using the gifted funds for the FHSA or taking it out for other uses.

"When you gift it to your child, it's their money. Their name is on the account," she says.

'Like advancing an inheritance'

Jason Heath, CFP and managing director at Objective Financial Partners Inc. in Markham, Ont., says the FHSA isn't suitable for parents who want more control over funds given to children. An example is they don't want to potentially lose the money to an ex-daughter or son-in-law if their child goes through a divorce.

He says some parents might prefer to loan their kids money instead, especially if they need some or all of it down the road in retirement.

"Funding an adult child's FHSA is really for parents in a good financial position," he says. "It's almost like advancing an inheritance, and they would be willing to do so without any protections."

Parents who gift money to kids for an FHSA should also explain to them how it can and should be invested, potentially with the help of a financial advisor.

"There's a certain degree of responsibility for the parents to try to provide some input," he says, "so the kids aren't day-trading the funds or making risky investment moves."

Mr. Heath notes the FHSA is allowed to hold qualified investments currently allowed to be held in a TFSA including mutual funds, publicly traded securities, government and corporate bonds, and guaranteed investment certificates.

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