Tax-Free Down Payment: Understanding the First-Home Savings Account

Description

The Federal government is stepping in to make home ownership a little more attainable for first-time buyers. The upcoming First-Home Savings Account (FHSA) is a tax shelter that can be used to accumulate a down payment. If you're saving up to buy your first property, here's what you need to know.

FHSA basics

The new FHSA program is expected to launch in 2023. Any Canadian taxpayer over the age of 18 is eligible to open this account. To be eligible, you must also prove that you do not own a home currently and have not bought a property within the past four calendar years.

Once the account is set up, you can contribute up to $8,000 to the account every year. This amount is deducted from your annual taxable income. The total cap for the program is $40,000. Unused contribution room cannot be carried forward. Also, the account must be shut within 15 years.

If you use the funds to place a down payment for a home, the withdrawal is tax free. You can also defer taxes by transferring funds from the FHSA to the Registered Retirement Savings Plans (RRSP). However, if you withdraw the funds directly from the FHSA for any purpose other than buying a home, it will be taxed.

Will this help?

When it comes to savings and investment, every little helps. The FHSA can be thought of as a supercharged Tax-Free Savings Account (TFSA) that is focused on first-time homebuyers. The annual contribution limit of $8,000 is certainly higher than the TFSA, and the program shares the same tax deduction benefits of the RRSP.

However, the account may not be enough to buy a home. The average home price in Canada is $746,146 right now. You would need $150,000 to place a 20% down payment on a typical home. Even if you combine funds with a partner, the maximum you can accumulate in these accounts is $80,000 within five years.

To close the gap, you need to invest your FHSA funds in growth stocks.

Where to invest

While you wait to buy your first home, you can get some exposure to the real estate sector via real estate investment trusts. High-yield, low-risk REITs can boost your FHSA savings by a significant amount.

Slate Grocery REIT (TSX:SGR.U) is an excellent example. The company owns and operates a network of grocery store properties across the United States. Most of these units are anchored by robust retailers like **Wal-Mart** and **Krogers**. These tenants are likely to pay rent regardless of economic conditions, which means the company's earnings are secure.

Over the past five years, Slate's average annual dividend yield has been 9%. Right now, it's closer to 6%. At that rate, you could boost your FHSA to $45,000 within five years. Robust dividend stocks like Slate could get your closer to your goal of homeownership.

Bottom line

Canada's upcoming FHSA program helps first-time homebuyers, but it may not be enough. Savers might need a high-growth or high-yield dividend stock to close the gap. Alternatively, they should hope for home prices to drop off a cliff!

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