Canaccord Genuity Wealth Management

Financial Focus

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RRSPs- Are They Worth It?

By Clinton Orr

It is that time of year again. We are rapidly approaching the RRSP deadline. In my opinion enthusiasm surrounding RRSPs has faded in recent years. I stumbled across a poll last week that confirmed that feeling. The poll was done by Angus Reid Forum in January 2018 and found that 39% of adult Canadians believe there is no point investing in RRSPs because the taxes eventually have to be paid when the money is withdrawn.

In 2009 the Tax Free Savings Account was introduced. We are fortunate to have multiple tax advantaged savings tools. I believe the introduction of the TFSA has made contributing to your RRSP less attractive, however the RRSP is not pointless, there are scenarios when contributions are advantageous.

Before we review the scenarios, a few details about the RRSP. The RRSP was created in 1957, at the time contributions were limited to 10% of the previous year's income, to a maximum of $2,500. If you did not contribute in a given year that contribution room was lost. Contribution room did not carry-forward. In the 90s there were significant changes. The contribution limit was increased to 18% of the previous year's income, the maximum contribution was increased, the maximum was indexed to annual wage growth and the carry-forward rule was introduced. Now unused contribution room can carry-forward indefinitely. For the 2018 tax year the dollar limit is $26,230. The last day you can contribute to your RRSP and use the tax deduction against your 2018 income is March 1, 2019.

Part of the attractiveness of the RRSP is the up-front tax deduction. Any dollar you contribute creates a tax deduction that can be used against your income. In terms of immediate tax relief, it is hard to beat the RRSP. If you have a temporary increase in your taxable income a RRSP contribution makes a lot of sense. The sale of a cottage, retirement payouts, severance payments, bonuses from your employer, the sale of rental property are all examples of events that might create a bump your taxable income. In all cases a RRSP contribution can help alleviate the extra tax.

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In addition to the immediate tax deduction, the money in a RRSPs grows tax free. The downside of a RRSP is that when the money is eventually withdrawn it is added to your income and fully taxed. A RRSP contribution makes the most sense if you contribute while you are in a high-income tax bracket and withdraw the funds while in a lower bracket. If you earn a good income and are in one of the higher tax brackets, this scenario will likely apply, and a RRSP contribution would make sense.

If you are in a lower income tax bracket or it is probable that you will be in the same tax bracket today as when you withdraw the money, a RRSP might not be the best fit. A contribution to your TFSA could be better.

The RRSP has lost some luster with the introduction of the TFSA. However, as described above, there are scenarios where a RRSP contribution makes sense. It is best to review your financial plan and see if a contribution is a fit for you.

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