

Making cents of your retirement savings

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It's that time of year again when those four letters are the starring role in almost every bank commercial, they are the topic of discussion with mom and dad at the dinner table and they may be consuming your every thought as the March 3 deadline approaches.

You know the four letters I'm talking about: RRSP. As in Registered Retirement Savings Plan.

Retirement?

Many young readers may be thinking: I'm only 22. Recently graduated. Finally starting to pay my OSAP loan. Earning enough cash to buy a little, something, something! Who wants to think about wrinkles, Botox, grandchildren, everyday being Saturday... But it's far better to start now. With dire predictions about pension plans and the uncertainty of the economy, hedging your bets against the financial storms ahead will not only give young investors some welcome shelter, but also a much rarer commodity: peace of mind.

The following is a list of common RRSP questions a young investor may ask before embarking on their first retirement savings contribution. Chartered Financial Analyst Dave Paterson, president of Paterson and Associates provides the answers.

Q: What exactly is an RRSP?

A: An RRSP is a government-endorsed plan designed to help you to save for your retirement.

With this plan, you can deduct any money you contribute to your RRSP right off the top so you are saving income tax today. As well, the money invested in your RRSP is allowed to grow tax-free until you take it out, when the funds will be treated as regular income.

It is because of this tax deferral that you will be able to save more money faster than you would be able to otherwise.

Q: How does an RRSP work? And what does contributing money to this investment "purchase" the investor? Bonds? Stocks?

A: An RRSP is not a specific type of investment, but more of a designated holding place where the investments of your choice will grow tax-deferred for your retirement savings.

Within this holding place, you have the option to invest in a wide variety of investments including stocks, bonds, mutual funds, GICs and property.

When you contribute to your RRSP, your financial institution will send you a contribution receipt that you can use when doing your income tax. This will benefit you in that you will have less taxable income in the year.

The second benefit comes from the earnings of your investments within the RRSP not being subject to income taxes in future years. In fact, you will pay no taxes on any of the investments in your RRSP until

you take them out of the plan. Any funds taken out of the plan are taxed as normal income.

IDEAL TIME

Q: What age is an ideal time to start investing in RRSPs?

A: The ideal time to start investing in an RRSP is now. It doesn't matter how old or young you are. The sooner you can start putting money away for your retirement, the better.

For example, if at age 20, you start putting \$100 a month into an RRSP which earns 10 per cent a year, by the time you are 65, you should have over \$900,000. Not bad considering that you have only invested a total of \$54,000. However, if you hold off until you are 35 to start investing the same \$100 a month, you should have just under \$208,000 in your RRSP on your \$36,000 of investment contributions.

Q: What if I want to contribute but I don't have a great deal of cash right now; are there options that allow me to invest in an RRSP?

A: If you are short on cash but still want to contribute to your RRSP, there are a couple of options for you.

One is an RRSP loan. With a loan, you borrow money to make a contribution to your RRSP. Most financial institutions offer some sort of a loan program where you can get a favourable interest rate, usually around prime. Many will even offer deferred payments for 90 days or so while you wait for your tax refund to arrive.

Whether or not an RRSP loan is right for you depends on your individual circumstances. In general terms, if you have a higher income, you will benefit more from an RRSP loan than somebody with a lower income. To find out more, check with your financial planner or bank.

Another alternative is to set up a monthly contribution plan. With this option, you are contributing a set amount each month to your RRSP, just like any other regular payment you have. After a while, you don't even know you are doing this, until you get the contribution receipt in February and you notice you are paying less in income tax each year.

"LOCKED IN"

Q: Will my money be "locked in" forever? What if I need some of that cash for later?

A: With an RRSP, your funds are not "locked in". You can withdraw money out of your RRSP at any time, but, any withdrawals are treated as taxable income.

There are, however, a couple of ways you can access some of the funds in your RRSP in a tax-free way.

The first is "the home buyers plan". With is strategy, you can borrow up to \$20,000 out of your RRSP to buy a home. You must repay a portion of these funds back into your RRSP each year over a maximum period of 15 years. If you fail to do this, the annual amount you were supposed to pay back will be treated as income.

The second way to access some of your RRSP funds is "the lifelong learning plan". This plan allows you to borrow up to \$20,000 out of your RRSP to go to school full-time. You will be required to pay a

portion of these funds back over a period of no more than 10 years. Failure to do so will result in the amount owed to be treated as income.