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PERSPECTIVES

An Excerpt from Volume 14 | Issue 8 **December 2023**

Financial & Estate Planning

RRSPS: YOU CAN'T START SAVING FOR RETIREMENT TOO EARLY!

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When you're young and in a career, retirement seems far away. But it *will* come eventually – faster than you think. So, you're best to start saving early for your retirement.

A Registered Retirement Savings Plan (RRSP) helps you do that. The two big advantages of an RRSP are:

1. tax-deductible contributions that lower your taxable income, resulting in less tax to pay; and
2. tax-deferred growth, meaning you don't pay tax on any of your gains until you ultimately withdraw them.

These two advantages are a huge help in saving for retirement. The larger the (positive) difference in income tax bracket when you contribute to your RRSP compared to when you eventually withdraw the funds in retirement, the greater the tax deferral benefit.

Contributions can either come from yourself or your spouse. There are limits on how much you can contribute each year. These limits will be the lower of:

- 18% of your earned income in the previous year, or
- the maximum contribution amount for the current tax year, which for 2023 is $30,780.

You can find your contribution limits on your Notice of Assessment, which the CRA provides each year after you submit your tax returns. By following the guidelines in our previous articles, you will have hopefully learned the tools to budget and save for personal investing. You should therefore have the funds to contribute! However, if you don't have the funds this year, it's still okay. You have the option to carry forward your RRSP contribution room and use it in the future.

As noted, you must close your RRSP the year you turn 71. At that time, you will have the option to withdraw from your RRSP, convert it to a Registered Retirement Income Fund (RRIF) or buy an annuity. Regardless which option you choose, you'll need to pay income tax when you withdraw from the plan.

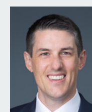
If you have a spouse who earns a lower income, and/or who is younger than you, you could benefit from a spousal RRSP. With this type of RRSP, the contributor can deduct the contributions, while the money grows tax-free under the spouse's name. By building up the spousal RRSP rather than your own, you can delay the withdrawal of your assets until your younger spouse turns 71. If you withdraw from a spousal RRSP, it will be taxed as income to your spouse, who is presumably in a lower tax bracket, and not to you as the original contributor. However, a withdrawal cannot be made within three years of the spousal contribution; otherwise the income will be attributed back to the contributor.

Designating your spouse as a beneficiary for your RRSP is an important part of estate planning. It allows your RRSP to flow to your spouse tax-free and, by ensuring your registered account will not be included in your estate, avoids probate fees.

You'll find plenty of RRSP calculators online that help you get an idea of how much to save to fund your retirement. Just make sure the assumptions are realistic. And remember to factor in inflation! Retirement may be a long way off, but remember that when it does come, it can last a long time, most likely decades. You'll need a healthy amount of savings to fund your retirement.

As we mentioned about TFSAs, you can arrange for funds to automatically be deposited (and invested) into your RRSP every pay period. This is an effective technique and simple to follow.

What if you don't have enough savings for both TFSAs and RRSPs? Which should you do first? The answer is, they are both great options. RRSPs are a bit more attractive if your tax bracket is higher, because the contributions are tax-deductible. TFSAs could be better if you might need to withdraw some of the funds in the next year or two. Withdrawals from TFSAs are tax-free, whereas you need to pay tax on RRSP withdrawals. If you want to increase the benefit from the RRSP contribution further still, then reinvest any tax refund the contribution may provide you with. The key lesson is: Just contribute as much as you can to one or both. Once again, your future self – your retired future self – will thank you for it.



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