Tax, Retirement & Estate Planning Services

INVESTMENT INSIGHT

RRSP? TFSA? RESP?

Make the most of your savings options

When it's time to decide which mix of savings vehicles is right for you, your options can start looking like a hearty bowl of alphabet soup. There are Registered Retirement Savings Plans (RRSPs), Tax-Free Savings Accounts (TFSAs) and Registered Education Savings Plans (RESPs). Determining which savings plan, or combination of savings plans is best, depends on your personal situation and your objectives.

REGISTERED SAVINGS OPTIONS

Until 2009, most Canadians held their retirement savings in an RRSP, where they could claim a deduction for their contributions and then defer tax until withdrawals were made which generally occurred at retirement. The introduction of TFSAs has provided another powerful savings vehicle that allows investment growth to accumulate and be withdrawn at any time tax-free. Unlike an RRSP, you cannot claim a tax deduction for the contributions you make to a TFSA. On the plus side, if you need to withdraw money from your TFSA, you have an opportunity to replace that money because all TFSA withdrawals are added back to your unused contribution room but not until the following year.[1]

If you have children or grandchildren, RESPs are another popular option. The subscriber (or contributor) makes contributions on behalf of a beneficiary (the child). The contributions are not deductible or taxable on withdrawal(s). The growth is tax-deferred until withdrawal(s) are made, at which time it can be taxed in the beneficiary's hands if he or she enrolls in a qualifying post-secondary educational program. Contributions to a child's RESP may qualify for the Canada Education Savings Grant (CESG)[2] and, if your family's income is below certain thresholds, you may also qualify for the Canada Learning Bond (CLB).

[1]Overcontributions in a year will be subject to tax consequences assessed by the Canada Revenue Agency.

[2]Contributions to an RESP for a child under the age of 18 qualify for the CESG, which pays 20 per cent of the annual contributions you make, up to a maximum of $500 per year, per beneficiary (or a maximum of $1,000 if there is unused grant room from a previous year), to a lifetime limit of $7,200. You may be entitled to an enhanced CESG if your family's income is below certain thresholds.

THE RETIREMENT DILEMMA

If you are saving for retirement, then you may be torn between an RRSP and a TFSA. Ideally, you would maximize contributions to both, but if that's not an option here are some thoughts to consider.

Whether the best choice is to save in an RRSP or a TFSA depends on your savings needs, as well as your current and expected future financial situation and income level.

PRIMARY PURPOSE OF REGISTERED SAVINGS PLANS

RESP: Saving for post-secondary education. Government grants and incentives may be available to enhance savings.

RRSP: Saving to provide retirement income. Allows for withdrawals at any time and also under the Lifelong Learning Plan and the Home Buyers' Plan.

TFSA: Saving for any short-term or long-term savings needs.

Generally, an RRSP is used for saving for retirement, while a TFSA can be used for both saving for retirement and other shorter-term purchases. Because TFSA withdrawals are added back to your available TFSA contribution room in the following year, there is very little downside to using your TFSA savings for mid-sized to large purchases.

If you are in a low tax bracket, saving in a TFSA may be more advantageous than saving in an RRSP since TFSA withdrawals have no impact on federal income-tested benefits and credits such as child tax benefits and Old Age Security. On the other hand, RRSPs may be a better option if your tax rate at the time you contribute is higher than it will be when you withdraw your savings. You'll benefit from a tax deduction when you make your contribution and withdrawals will be taxed at your lower future rate. If the reverse is true, a TFSA can provide better results.

EDUCATION SAVINGS CHOICES

If you are saving for your child's education, then you are probably weighing the pros and cons of an RESP or a TFSA. For children under age 18, RESPs are the preferred savings vehicle because of the CESG. For children over age 18, the CESG no longer applies so you may want to help them start their own TFSA. If you want to maintain control over the funds, then you could save for their education in your own TFSA instead.

Features of registered savings plans

	RESP	RRSP	TFSA
Is there an annual contribution limit?	No annual limit but a $50,000 lifetime limit per beneficiary	Yes, it is based on previous year's earned income	Yes, an annual limit[3] but there are no earning requirements
Can I carry forward unused contribution room?	Yes	Yes	Yes
Is there a monthly penalty on excess contributions?	Yes, calculated at month-end	Yes, calculated at month-end	Yes, calculated on the highest excess during the month[4]
Are my contributions tax-deductible?	No	Yes	No
Is my investment growth tax-deferred or tax-free?	Tax-deferred	Tax-deferred	Tax-free
Are taxes payable on withdrawals?	Withdrawals are fully taxable except for refund of contributions[5]	Withdrawals are fully taxable	Withdrawals are tax-free – except for growth after death if no successor holder[6]
Are withdrawals added to my contribution room?	No	No	Yes, but not until the following year[7]
Can withdrawals have an impact on income-tested benefits/credits?	Yes, for the taxable portion (No, for refund of contributions)[5]	Yes	No
What is the minimum age to contribute?	None	None	Age 18
What is the maximum age to contribute?	None	At the end of the 71st year or 71st year of spouse in case of spousal plan	None
If I borrow to invest in this account, can I deduct the interest?	No	No	No
Can I use assets in this account as collateral for a loan?	No	No	Yes

[3] The annual contribution limit is currently $5,500 per year. Increases rounded to the nearest $500, will be applied as warranted by the consumer price index. The annual contribution limit was $5,000 for years 2009 to 2012, $5,500 for years 2013 and 2014, and $10,000 for 2015.

[4] Any income attributable to deliberate overcontributions will be taxed at 100 per cent.

[5] Any withdrawals other than the refund of contributions will be fully taxable to either the beneficiary (student), if he or she qualifies to receive the payment, or the subscriber (contributor).

[6] Successor holder means a spouse or common-law partner as these terms are defined in the *Income Tax Act* (Canada). Certain contracts may provide that if a spouse is named as the sole beneficiary, he or she will automatically continue the contract as the successor holder and the applicable successor holder rules would apply. In these situations, the investor's spouse may have the option to be treated as a beneficiary of the contract and, in that case, beneficiary rules would apply.

[7] The withdrawal of amounts in respect of deliberate overcontributions, prohibited investments, non-qualified investments, asset transfer transactions and income related to those amounts do not create additional TFSA contribution room.

For more information, please contact your advisor or visit manulife.ca/investments

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