moneysense.ca, 29/03/12

Advice for first time homebuyers

The RRSP Home Buyers' Plan is a great option for first time homeowners, but it doesn't always make sense to pay it all back.

By Bryan Borzykowski | Online only, 29/03/12

When Krystal Yee opened her RRSP five years ago it wasn't because she wanted to get a head start on her retirement savings. The 29-year-old marketing manager and financial blogger started the account for another reason: she had plans to buy a house.

Yee wanted to take advantage of the RRSP Home Buyers' Plan, a program introduced by the Federal Government in 1992 that allows first time homebuyers to withdraw up to $25,000 from their account tax-free. By last May she had saved up enough to take out the maximum amount to use as a down payment on a house in New Westminster, B.C.

Now comes the tough part—paying the money back. Under the program, homebuyers have to return the funds over a 15-year period, starting the year after the money was withdrawn from an RRSP. That means Yee will have to pay $1,666 before the RRSP deadline next February and another $1,666 every year until 2028.

Initially, she thought about paying it back as quickly as she could, but she changed her thinking after she did the math. "It makes sense to only pay the minimum towards the plan in order free up money for a larger RRSP contribution," she says. It makes sense. Yee wouldn't get a tax refund on the money she pays back into RRSP under the plan, so by designating the minimum repayment she can still get the tax benefit for any RRSP contribution she makes above $1,666.

Most advisors suggest taking Yee's approach, but there are cases where it makes sense to not repay the borrowed funds to your RRSP in a given year, or in some instances at all.

Rona Birenbaum, a Toronto-based CFP, generally advocates returning the money to the RRSP, but if you know you're not going to earn any income in a particular year, or you expect to be in a lower tax bracket than you were when you initially contributed the funds, then it may be smarter to not pay it back. "Supposed you're on maternity leave for a year, you might want to skip that payment since you won't be in a taxable position."

Those who go this route will be taxed on the money they borrowed, but like the re-payments the tax hit would also be spaced out over the next 15 years. For this reason, Birenbaum suggests taking a year-by-year approach. If you're going to be in the highest tax bracket then it's a good idea to pay back the funds to your RRSP to avoid a $766 tax bill. If you're in a lower bracket, the tax implications become less of a burden and repaying the RRSP loan become less important.

Stephanie Holmes-Winton, a Dartmouth-based financial advisor and author of *$pent: How Money Management is the Key to your Financial Freedom*, says that for some people, it may not make sense to pay back the $25,000 at all. For low-income earner, it may make more sense to take the tax hit—which will be small—and invest the money in a tax-free savings account. Many experts say that if you earn less than $40,000 a year, you're better off investing in a TFSA.

Some people may also have a pension, which typically lessens the importance of an RRSP, says Holmes-Winton. While many first time homebuyers are in their 20s and 30s and likely don't have a company pension, Birenbaum says that a number of older Canadians who either wait to buy a house or need the years to save are using the plan, too.

Of course, it all depends on your circumstance. Yee, for instance, has every intention to paying back the money she borrowed from her RRSP. And while she says could pay off the loan faster, she doesn't see the point. "The advantage to putting more money into repaying the plan would be that I owe less money, and my future minimum payments would be smaller," she says. "But since

I make regular contributions into my RRSP, the size of my Home Buyers' Plan minimum payments doesn't make a difference to me."

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