Supercharge Your Retirement Savings!

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Tax filing season is upon us. I think that I just heard you groan.

Unfortunately, since the calendar has flipped to 2019, there aren't many things that we can still do to alter our tax situation for the 2018 tax year. However, the primary tool that remains at our disposal relates to Registered Retirement Savings Plans (RRSPs).

RRSP Breakdown

The way RRSPs work is that the contributions that you make to your account are a deduction from your employment income for tax purposes. This means that for every dollar that you contribute to your RRSPs, you do not have to pay any tax on it in the current year. Tax is only paid when you withdraw the funds from your RRSP upon retirement, or sooner if required. The benefit to this is that the money in your RRSP grows tax-deferred for as long as you don't withdraw the funds. This is one of the best retirement savings and wealth building tools in the Canadian personal finance arsenal.

RRSP contributions are broken out into two separate timeframes.

- January to February
- March to December

You should be receiving your March to December of 2018 RRSP contribution slip any day now from your financial institution, so keep an eye out. Even though 2018 has drawn to a close, the government of Canada has given us all a great tool to maximize our RRSP utilization. They allow us to make contributions up until the end of February and have them applied against the previous tax year. So, you can make an RRSP contribution during this two-month period and can apply it to your 2018 tax year.

Why is this so important?

We are in a very advantageous position because of this contribution flexibility. I like to use this window as an opportunity to kick-start RRSP savings.

The Supercharger!

The strategy that I recommend is effectively a "loan to yourself" for the exact amount of your tax refund (give or take). Now, this isn't a technical loan with interest, etc. but rather a cashflow loan to yourself.

If you are filing your taxes on your own, 2018 tax filing software is now available. As you begin to work on your tax filing, you can begin to get a sense of the size of your eventual tax refund. Once you complete your initial entry into the software, you will have a rough estimate of what your return will be.

Related: How to prepare your taxes yourself. **https://novelfinancial.ca/you-can-file-your-own-taxes**

Once you have a reasonable estimate of your tax refund, you now know the amount that you will "loan to yourself". For example, let's say that you are going to expect a $2,000 tax refund. This means that once you file your taxes, you will receive a $2,000 payment from the government.

This is where the supercharger for your RRSP savings comes in. Presuming that you have $2,000 in your non-registered savings account, you can make a $2,000 contribution to your RRSP. Then you can repay the loan to yourself with your tax refund and replace the $2,000 that you had withdrawn in order to make the RRSP contribution.

The benefit of this is that by making the RRSP contribution, you have now increased your tax refund!

Let's assume that you have a 35% marginal tax rate. This means that you have just increased your tax refund by $700.

	No Supercharged	Supercharged
RRSP Contribution	$ -	$ 2,000
Tax Refund	$ 2,000	$ 2,700

Now, for the real supercharger. If you contribute the incremental $700 to your RRSPs for the 2019 tax year, you have now created an additional $245 in extra cash from your 2019 tax refund. By making a simple $2,000 contribution you can create $945 in additional cash flow to yourself in roughly a year. In addition to the cashflow, the new contributions to your RRSP will grow tax deferred until your retirement. The below table shows how this simple manoeuvre compounds over a 30-year period.

Tax Year	Contribution	Marginal Tax Rate	Incremental Tax Refund	Opening RRSP	Income on Savings*	Closing Balance
2018	2,000	35%	700	-	-	2,700
2019		35%	245	2,700	135	3,080
2020		35%	86	3,080	154	3,320
2021		35%	30	3,320	166	3,516
2022		35%	11	3,516	176	3,702
2023		35%	4	3,702	185	3,891
2024		35%	1	3,891	195	4,087
2025		35%	0	4,087	204	4,291
2026		35%	0	4,291	215	4,506
2027		35%	0	4,506	225	4,732
2028		35%	0	4,732	237	4,968
2048		**35%**	**0**	**10,467**	**523.35**	**10,990**

Assumes 5% income per year

A single $2,000 loan to yourself can result in nearly $11,000 in additional retirement savings. This is a strategy that I have used personally with great success in the past. This is also something that can be performed each and every year. Since this is something that can be done every year, let's see what happens if we expected a $2,000 tax refund for the next five years, and used the same approach.

Tax Year	Contribution	Marginal Tax Rate	Incremental Tax Refund	Opening RRSP	Income on Savings*	Closing Balance
2018	2,000	35%	700	-	-	2,700
2019	2,000	35%	945	2,700	135	5,780
2020	2,000	35%	1,031	5,780	289	9,100
2021	2,000	35%	1,061	9,100	455	12,616
2022	2,000	35%	1,071	12,616	631	16,318
2023		35%	375	16,318	816	17,508
2024		35%	131	17,508	875	18,515
2025		35%	46	18,515	926	19,487
2026		35%	16	19,487	974	20,477
2027		35%	6	20,477	1,024	21,507
2028		35%	2	21,507	1,075	22,584
2048		**35%**	**0**	**47,583**	**2,379**	**49,962**

Assumes 5% income per year

This example shows $10,000 of contributions over 5 years using the supercharge technique, which equates to over $15,000 in total contributions once you include the contributions made with the funds from the incremental tax refund. Who wouldn't want to have an extra $50,000 dollars available to them in their retirement?

Tax Refund Estimate

Now you may ask, but what if I don't have all my tax forms? How can I reasonably estimate my tax refund?

Make the best estimates that you can and enter them into the software. Use your final pay slip from your employer instead of your T4, add up the interest earned in your savings account in place of your T5, etc. As long as the estimates that you use are reasonable and complete, you shouldn't have any issues coming up with a reasonable estimate of your tax refund. An added bonus of this approach is that if you are slightly off with your estimate, the increment to your tax refund (the $700 in our example above) acts as a buffer in case you over-estimated your original tax refund.

A critical thing to keep in mind with this approach is that you don't forget to update your tax software with the correct figures once your tax slips come in. The tax man doesn't like estimates like actuaries do.

Does This Make Sense For You?

As with all tax planning, this manoeuvre should only be utilized if it makes sense for your situation. Some critical aspects to consider are

- Whether or not you have the cash available in a non-registered account
- Whether or not you need the cash between now and your tax refund being paid
- Your available RRSP contribution room
- Your marginal tax rate
- Your expected marginal tax rate in retirement
- Workplace pension plan considerations
- Your overall retirement plan

RRSP contributions should generally be made when your current tax rate is greater than your expected tax rate in retirement. If you are unsure whether this technique makes sense for your situation, you should consult with a financial planning professional.

The Brass Tacks

Saving for retirement is a critical objective for all Canadians. The January-February RRSP contribution period can be used as a powerful tool. With this simple approach you can have a significant positive impact on your retirement savings. This could allow you to reach your retirement goals faster or provide extra cushion once you get there.

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