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Tax form hints for RRSPs

Tax planning can make RRSP contributions doable

According to a recent Investors Group study, 26% of Canadians do not invest in RRSPs. A whopping 62% of those report budget constraints as their primary reason against investing, stating they don't have enough money after living expenses. However, for some a bit of savvy tax planning can reduce the burden of RRSP contributions.

Investors making regular RRSP contributions through payroll deductions can ask the Canada Revenue Agency to reduce the taxes withheld by their employer, using a form called 'T1213 Request to Reduce Tax Deductions'. This effectively allows the investor to use the future refund to make RRSP contributions now.

Consider an investor who wishes to make monthly contributions to maximize their RRSP. Given the \$22,450 RRSP deduction limit for 2011, monthly contributions would amount to \$1870.83.

Applying the source deduction strategy, a B.C. an investor in the highest personal income tax bracket could have the monthly tax withholdings reduced by \$817.55, lowering the monthly net cash required for the RRSP contribution to \$1,053.28.

To justify a monthly overpayment of taxes, many taxpayers use rationale such as getting pleasure from a refund, or being concerned about paying some amount at year-end. It's false economy. Parking money with

the tax department does not add to wealth, but investing in an RRSP on a monthly basis, instead of a lump sum, is definitely beneficial.

One advantage is dollar-cost averaging, which allows investors to buy more shares when prices are low, and less when they are high. By investing equal dollar amounts over a set period of time, investors generally end up with a lower average cost. Even collecting interest on vehicles like GICs is better than leaving the earnings with the tax department.

The source deduction strategy requires an annual application but the paperwork is not onerous and the CRA can be expected to reply within four to eight weeks. The strategy also works for investors in lower tax brackets, although their reduction of tax withholdings will be a lower percentage.

As with all tax planning, individuals should make sure they understand the tactics thoroughly. There are many different rules, so it is imperative to check with a tax professional prior to pursuing any strategies to make sure they make sense for the particular situation.

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