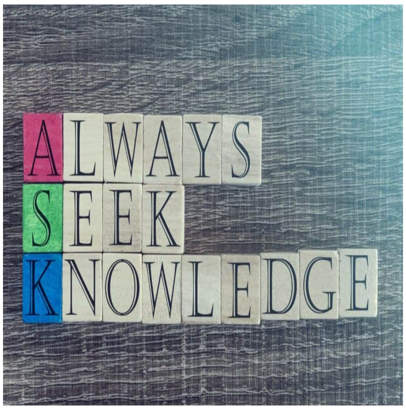

The 1 Thing They Won't Tell You About RRSPs

Description

So, you want to open an RRSP.

Great decision.

Not only do RRSPs let you put away money for retirement, but they also give you a number of tax benefits for doing so. First, you get a tax deduction on contributions below your limit. Second, your capital gains and dividends aren't taxed until you withdraw. Third, your RRSP income is taxed at a lower rate if you withdraw it after you have retired.

So there are a number of great reasons to hold long-term positions in an RRSP. There's just one thing you need to be aware of that you may not have been told: a specific withdrawal rule that could conflict with your investing goals. Although RRSPs are good for your retirement overall, this rule is something you urgently need to know about. The good news is, with the right investing approach, it actually works in your favour.

RRIF minimum withdrawals increase progressively with age

When you reach the age of 71, you need to transfer your RRSP holdings to a RRIF. From that point on, a certain amount of your holdings are withdrawn to a regular bank account. Once you start to withdraw from your RRIF, there's a minimum amount you need to withdraw each year. Initially, the amount is low, but it increases progressively with age. According to **CIBC**, by the time you reach 95, you have to withdraw a full 20% of your holdings annually!

How this affects your RRSP investing strategy

Because RRIFs have mandatory minimum withdrawals, it's in your best interest to hold dividend stocks that pay enough income to cover the withdrawals. That way, your withdrawal won't actually cut in on your holdings. Dividend stocks like **Fortis Inc** (TSX:FTS)(NYSE:FTS) pay close to 4%, enough annual income to cover your withdrawals early on. Eventually, your RRIF withdrawals will increase to far higher than 4%. But the genius of Fortis is that the stock has a 45-year track record of steady dividend increases. Thus, the income has the potential to increase along with your minimum withdrawals.

Three types of RRIFs

If you're planning on investing in an RRSP, it pays to know what type of RRIF you'll ultimately get. Like RRSPs, RRIFs come in three basic types: guaranteed, managed, and self-directed. Guaranteed RRIFs pay you income, but the amount is fairly low, similar to a GIC. Managed RRIFs, including mutual fund RRIFs, may pay high income, but it depends on the specifics of the plan. Self-directed RRIFs give you the ability to pick your own stocks, which makes them ideal for high yield investing.

Bottom line

RRSPs are the perfect vehicles for retirement investors. Offering tax deferments, deductions and sheltering, they deliver a triple whammy of tax benefits that TFSAs can't match. But RRSP investing calls for a particular strategy. While you might be tempted to hold high-growth stocks like **Shopify Inc**, it's best to hold dividend stocks that will pay income that can be withdrawn year after year–especially in the later years of your RRSP, when the transfer to a RRIF is imminent.

CATEGORY

1. Dividend Stocks
2. Investing
3. Tech Stocks

TICKERS GLOBAL

1. NYSE:FTS (Fortis Inc.)
2. TSX:FTS (Fortis Inc.)

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