



## RRSP: 3 Common Myths Debunked

### Description

Canadians have until [March 1 to contribute to their Registered Retirement Savings Plan](#) (RRSP) for the 2020 tax year. Should you contribute to an RRSP or not? Many taxpayers still wonder about the usefulness of the RRSP. Questions jostle in their heads. Shouldn't we prefer the Tax-Free Savings Account (TFSA)? What is an RRSP good for, knowing that when you withdraw your funds, you have to pay tax?

While its usefulness is sometimes disputed, in recent years several myths have spread among the population. Here are three common myths about the RRSP that need to be debunked.

### **Myth 1: There's no need to invest in an RRSP – you pay back all the tax savings when you retire anyway**

Although this is a fairly common myth, it is not correct. The idea behind this myth is that ultimately the RRSP is useless since it certainly allows time to avoid taxes, but this advantage goes up in smoke when it comes time to withdraw your savings.

Even if you pay tax on RRSP withdrawals, remember that you also get a tax deduction when you contribute. If your tax rate is the same in the year of contribution as in the year of withdrawal, an RRSP actually provides a fully tax-free rate of return on your net contribution. And if your tax rate is lower in the year of withdrawal, you'll get an even better after-tax rate of return on your RRSP investment.

### **Myth 2: You can't withdraw from your RRSP before you retire**

That's not true. Money in an RRSP can be withdrawn at any time, but it's essential to know that Ottawa will impose a withholding tax of up to 30%. Plus, the amount you withdraw will be taxed at your marginal tax rate the year of withdrawal.

The government allows exemptions like the Home Buyers' Plan, where the plan holder and its spouse

can each borrow up to \$25,000. Repayment must begin no later than two years later and must be fully repaid within 15 years. The offer is only available to first-time home buyers.

The Lifelong Learning Plan also allows investors to withdraw up to \$20,000 tax-free for full-time training or post-secondary education. The full amount must be repaid within 10 years.

## Myth 3: It's better to invest in a TFSA than an RRSP

Many Canadians believe that it is better to invest in a [TFSA](#) than an RRSP, claiming that TFSAs are better tax-saving vehicles because they are completely tax-free.

In general, an RRSP is usually a better choice than a TFSA if you plan to have a lower tax rate in retirement. This is especially likely if you are a baby boomer in your prime earning years and expect less income when you are no longer working.

A TFSA may indeed be a better choice than an RRSP in some cases, for example, if you expect a higher tax rate at the time of withdrawal or if you face a clawback (refund) of government benefits. Even so, you may not be able to save enough in a single TFSA and may need to supplement your retirement savings with an RRSP.

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