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USING RRSPS FOR YOUR DOWN PAYMENT

Many people are still unclear about the particulars surrounding registered retirement savings plan (RRSP) withdrawals for the purpose of buying a home, so Canadian Real Estate asked Winnie L Go of ScotiaMcLeod in Toronto, Ontario to demystify the process



What are the restrictions on using RRSPs for a down payment on real estate?

You can always use your RRSPs for a down payment on real estate. However, you have to pay taxes on the amount withdrawn, as it will be added to your income in the year of withdrawal.

If you're considering purchasing (or building) your first home, the federal government's Home Buyers' Plan (HBP) is an option you can consider. The plan allows you to withdraw up to \$20,000 from your RRSP. There's no tax withheld on this withdrawal, however the funds must be repaid in annual minimum amounts over a period of 15 years.

Here are some of the rules you should be aware of with the HBP:

- » The home you're buying must become your principal residence
- » Two people can withdraw from their RRSPs for the same home. They need not be spouses, however the home must be intended to be the principal residence of both
- » The home must be located in Canada
- » Before withdrawing from your RRSP you need to have a written agreement to buy or build a home
- » You must acquire your home by 1 October of the year following the year that you withdraw the money from your RRSP
- » If you make a contribution to your RRSP within 90 days prior to your withdrawal, that contribution won't be deductible if the contributed funds were needed for the withdrawal

Am I still eligible for the HBP if I've owned a home previously?

You can't have owned a home or have lived in a home owned by your spouse in any of the past five calendar years beginning at the time of the withdrawal.

What are the advantages of using RRSPs for your down payment?

You have an immediate source of funds to assist in securing a home. If qualified to use the HBP, there's no tax withheld on the withdrawal as long as the funds are repaid accordingly.

What are some of the pitfalls?

By withdrawing funds from your RRSP under this plan, you're foregoing the investment income and the related tax deferred compounding of that income during the time that this money would have been in your RRSP.

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This results in the reduction of your RRSP balance and subsequently the income available to you during your retirement.

As an example, assume a 30-year-old investor takes \$20,000 out of his RRSP under the plan and begins to repay the amount right away (\$1,333/year over 15 years). Had he left the amount untouched until age 69, the \$20,000 would have grown on a tax-deferred basis to approximately \$430,000 (assuming an 8% rate of return).

However, the homebuyer's withdrawal together with the subsequent repayment (1/15th per year) would result in an RRSP balance (at age 69) of approximately \$245,000 – a difference of \$185,000 from the RRSP that was left untouched. While this is a significant amount, it doesn't necessarily mean that a homebuyer's withdrawal is a poor strategy to follow. A homebuyer's withdrawal strategy, however, should be well thought out. This may mean, for instance, that a comparison is required of the amount of interest that is saved due to the smaller mortgage balance that results from the homebuyer's withdrawal.

Also, where other non-registered funds are available, it would be wise to use this money (before you use RRSP funds), since the investment returns earned on it aren't deferred but are instead taxable to you each year.

How does the payback process work?

You must repay this money to your RRSP over the next 15 years starting in the second calendar year after the withdrawal. Your payments are due within 60 days of the end of each year.

If you don't make this payment then the amount is added to your income for the year and as a result will be taxed at your highest marginal tax rate. Each year, the Canada Revenue Agency will provide you with a statement informing you of your minimum repayment requirement.

Can you use your RRSPs for purchasing investment properties?

Yes, you can use RRSPs for investment purposes. Note, though, that taxes will be withheld and the withdrawal amount added to your taxable income. You can't use the HBP for purchasing investment properties. The home you're buying must be your principal residence.

