Beat the deadline: How to get more out of RRSP contributions

Many people put cash into an RRSP right before the deadline, but there may be better ways to invest.

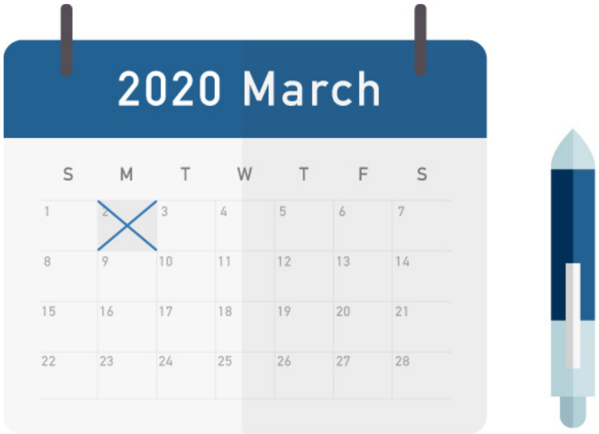
Most of us need a deadline to get things done, and contributing to an RRSP is no exception. Years ago, the government wisely created a contribution date for RRSP contributions to qualify for an income tax deduction on your annual return. That deadline is 60 days into the new year, which this year, is February 29, 2020. But because this year falls on a weekend, you have until Monday, March 2nd to contribute.

While the deadline has helped people invest, many people also, naturally, leave their contribution to the last minute. That's completely acceptable—so long as you meet the deadline, you can reduce your 2019 taxable income by any allowable RRSP contribution amounts you've made—but you also want to be sure your hard-earned savings are delivering the best possible returns.

To that end, here are a few tips to get your RRSP contributions to work as hard as you are.

Don't leave contributions in cash

In the rush to meet to the deadline, many people put their RRSP contribution in cash, thinking they'll invest it at some point in the near future. Unfortunately, too many investors forget to come back to their account and inadvertently leave their money in cash for the entire year.



There are a couple of problems with holding cash: you miss out on a year's worth of potential investment earnings—markets could head higher while you remain uninvested—and, your savings can lose ground to inflation. (Prices for goods and services usually increase every year, so in order to preserve or improve your purchasing power, your savings need to increase by at least that much—and ideally, more.) So, do yourself a favour and invest your contributions into a suitable long-term asset allocation right away. When it comes to long-term savings, cash can be a four-letter word.

Make next year's contribution now

Since you're already taking action to invest this year's contribution, go one step further and increase your lump-sum investment to cover your 2020 tax year contribution as well.

For example, if you max out your contribution before the deadline, then this year—assuming you have the allowable contribution room and cash on hand—you might also want to put something toward your 2020 tax year. If you don't have the cash available to contribute earlier, you could move funds from your taxable account. Moving funds from a taxable account into an RRSP will defer those gains going forward until you withdraw them. However, be aware that if you sell funds in a taxable account, the corresponding capital gains will be triggered.

Ideally, you'd want to max out both 2019 and 2020, and then get into the routine of contributing every January (13 months before the deadline). But even saving a bit at the start of the year can be a benefit.

Why? For one, you won't feel the stress of needing to find cash to contribute at the RRSP deadline, but more importantly, it gives your investments an extra year of potential market earnings, which can then compound and grow for longer. You are also sheltering returns and income, and deferring taxation until you ultimately withdraw from the account.

However, make sure not to overcontribute. You can err on the side of caution and top up the remainder at the end of the year when you know exactly how much you have earned.

Set up monthly contributions

If you can't invest a lump sum at the start of the year (again, 13 months before the deadline), then consider splitting your annual contribution up into monthly payments. You can do this through your bank by setting up automatic monthly payments to go from your chequing or savings account right into your RRSP.

By going this route, you'll never have to think about contributing again—it will just happen—and you might also lower your investment risk by dollar-cost averaging. In a nutshell, dollar-cost averaging means spreading out your investment contributions evenly throughout the year, which can help you avoid buying a stock at a low point. If, for example, you make one lump-sum investment right before a market correction, it could take weeks or months until your money gets back to its baseline and starts earning a profit. However, if you've been investing all year long, you can be sure that at least some of your money will enter the market when prices are lower, therefore avoiding the full force of a decline.

This 'pay yourself first' strategy can be very effective. People who do this are far more likely to meet their retirement goals, whereas those who wait until the end of the month tend to find that life spending got away from them and have no surplus funds left to invest. Set up the withdrawals a day or two after you get paid so it leaves your bank account right away.

It's important to remember that RRSP contributions are about more than the tax deduction. That money needs to grow, too—it funds your retirement, after all. Fortunately, with the right strategies you can lower your tax bill and boost your retirement savings in the process.

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