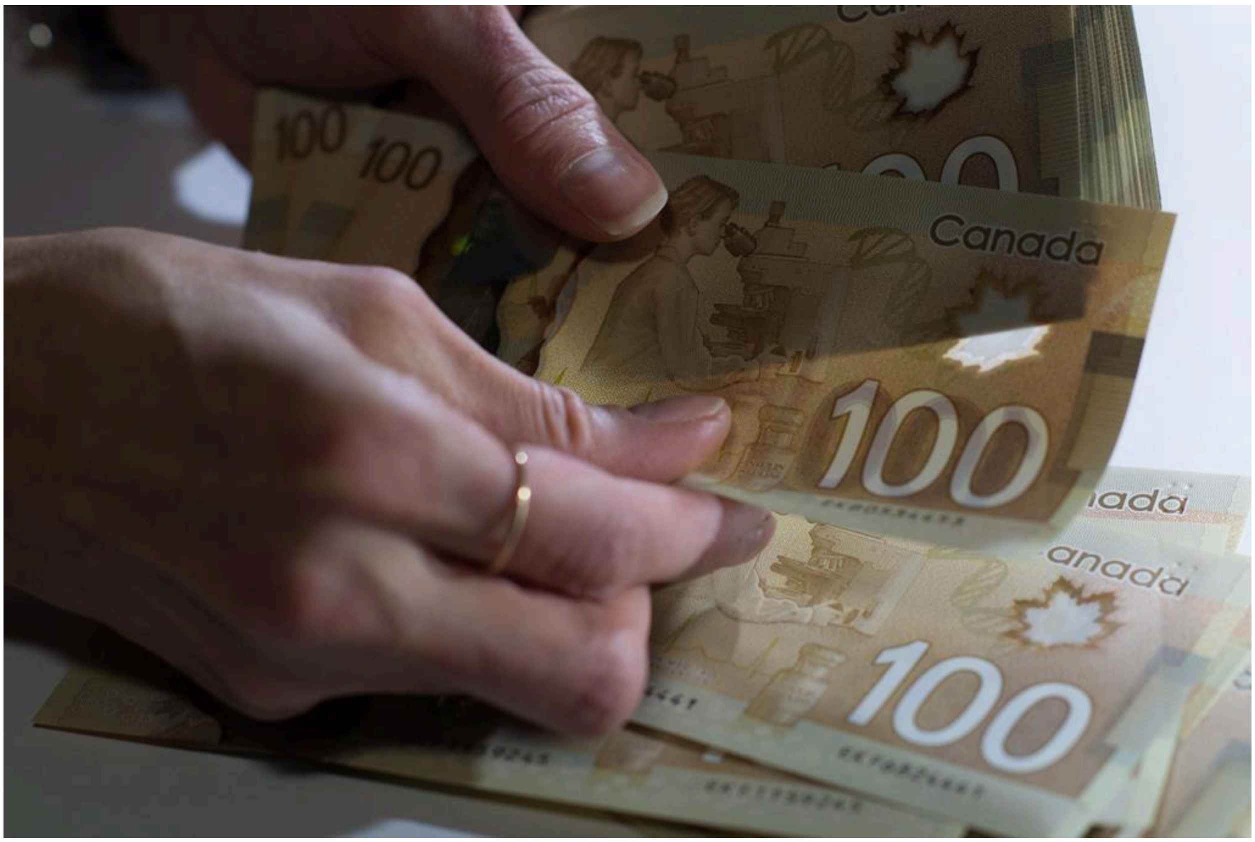
Want to boost your tax refund with an RRSP loan? Experts say there's more to consider



RRSP loans might be a tempting option for Canadians short on cash and looking to top up their retirement savings this year, but financial advisers are urging caution to those thinking about borrowing to invest. Canadian $100 bills are counted in Toronto, Feb. 2, 2016. THE CANADIAN PRESS/Graeme Roy

By Craig Wong, The Canadian Press

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OTTAWA — RRSP loans might be a tempting option for Canadians looking to top up their retirement savings this year, but financial experts urge caution for those thinking about borrowing to invest.

Kimberley Tran, an economist and advisor with McAuley Financial Services, said an RRSP loan should be the “rare exception and not the rule” for Canadians looking to save for retirement.

“An RRSP loan is not for everyone,” she said.

If an investor has the contribution room and is short on cash, the idea of a larger tax refund than they would otherwise receive if they didn’t take out a loan does sound enticing.

But Tran says those considering taking on debt to invest need to look at more than the potential size of a tax refund.

An investor’s tax bracket, cash flow and savings priority should also be considered, she says.

Even investors who have used an RRSP loan successfully in the past will want to consider the higher interest rates charged on loans this year.

Gabriel Lalonde, a certified financial planner, said RRSP loans were more attractive when interest rates were lower. He said the pitch used to be that you could earn more on the investments than you would have to pay in interest on the loan.

“Well, now it’s not really the case. I mean, at eight per cent, you know, on the loan, it’s pretty tough to beat that safely in the market,” said Lalonde, who is president of MDL Financial Group.

And while interest payments on loans taken out for investing purposes can sometimes be tax-deductible, this is not the case for RRSP loans.

There are a few circumstances where a loan might be worth considering.

Lalonde said seasonal workers or commission-based sales people who have uneven income throughout the year may find an RRSP useful if they don’t have the cash right now to make a contribution, but know they will have the money later to repay the debt.

He also said if an investor is in a high tax bracket today, but knows they will be in a lower tax bracket in a few years, it might make sense to use up their RRSP contribution room now when the tax benefit of making a contribution is bigger.

“You definitely have to have an appetite for risk when you’re using somebody else’s money to invest,” Lalonde said.

Janet Gray, an advice-only certified financial planner with Money Coaches Canada, said if an investor is expecting a large tax bill this year, an RRSP loan and large contribution might make sense to help offset the bill.

But, she cautioned, there is risk associated with borrowing to invest.

“There’s no guarantee on your return,” she said.

“You could take a, I don’t know, a $10,000 loan and be paying on it and then that $10,000 investment that you purchased could go down in value to $8,000.”

Gray said like any loan, you shouldn’t borrow more than you can afford to repay even with the help of a larger tax refund. And while a larger tax refund is nice to have, that extra cash should be used to repay the loan that the investor took out to help generate it.

“Don’t let the carrot blind you to the fact that you will have repayments to make,” she said.

Gray said investors also need to remember that an RRSP loan is adding debt and it could impact your credit score and affect other borrowing.

“It’s a loan and you still have to do all the qualifications around it and then all the ramifications of it afterwards.”

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