How to save for university at any age

Advice for whether your kid's in diapers or entering their teen years

by Julie Cazzin
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Most parents have barely taken their baby on their first stroller ride when they start to wonder how to pay for a university education. There's a lot to figure out. Can they afford it? How much will they need to save? And what's the proper way to invest their money now? With Canadian universities estimating that a single year of post-secondary expenses—including tuition, room and board, food, transportation and books—costs between $18,000 and $25,000, the price tag for four years can easily reach $80,000 or more. Further, recent studies by the Canadian University Survey Consortium show that Canadian post-secondary students leave university with an average debt load of $27,000. But don't feel discouraged by the steep costs. Having a plan will make things feel far more manageable. "Life is so busy," says Annie Kvick, a certified money coach in Vancouver. "It pays to put milestones in your calendar . . . when there may be a little extra money to put toward your child's education savings, like when daycare costs are done, the mortgage is paid off or the stay-at-home spouse goes back to work."

Here's a step-by-step—and stage-by-stage—guide to helping your child pay for school.

Kids aged zero to two
This is an expensive time for families. With daycare bills, a mortgage and new baby gear straining the household budget, there's little cash left to save for a distant post-secondary education. "The best investment you can make at this time is simply paying off your non-deductible debt," says Al Feth, a registered financial planner in Kitchener, Ont. "Especially credit cards with 18 per cent interest rates—those should be the priority at this stage."

But even if you have personal debt, it's still a smart move to open a registered education savings plan (RESP) for your child. It's simple and convenient. Your money might be tight, but family members and close friends might make contributions as birthday and Christmas gifts. It can add up quickly if you make a point of depositing right into the RESP. "It's a good cause as opposed to just buying toys and more clothes for the child," says Kvick. "Grandparents especially love to have this option available to them."

At this stage, it helps if you understand a bit about how RESPs work and how you can use them to maximize their savings potential. An RESP is an investment account introduced by the federal government in 1972, modified in 1998 to include a grant from the government, designed to help you save for a child's post-secondary education. Not only does the money grow tax-free, but the government contributes generous grants. Setting up an account is easy. All you need is a social insurance number for each child. "It's a chaotic time, but as soon as they're born, get them a SIN and open an RESP for them," says financial educator and personal finance columnist Bruce Sellery. "That's what I did for my daughter Abby seven years ago, and she now has $32,000 in that account."

What are your start-up options?
There are three types of RESPs available: individual plans, family plans and group plans. Group RESPs—typically called scholarship trusts—aren't a good choice because they typically have high fees, pre-set contributions and no entitlement to investment income if the plan is cancelled. And while individual RESPs, which are plans that pay for the education of just one beneficiary, are available as self-directed accounts at your local bank, the best idea is to set up the RESP account as a family plan there. With a family plan, more than one child can benefit from the savings—which works well when there are multiple kids. Opening a trust is also an option, but that's not a good choice for most families. "Trusts are really beneficial for people who have $500,000 as a minimum to invest for their child," says certified financial planner and father of two Jason Heath. "I don't think they work for accounts with $10,000 or $20,000 in them like most RESPs."

How much should you save?
Sellery believes parents should be ambitious with their RESP savings goals from the get-go. "Set up a pre-authorized payment of $200 monthly to maximize the government grant," says Sellery. "Do that amount right from the beginning, because I've found that people don't go back to change things."

Government benefits like the Canada Education Savings Grant (CESG) add up quickly, which is one of the main benefits of an RESP. "Nowhere in the world can you get the 20 per cent return on your money like you can with an RESP," notes Sellery. To maximize the basic CESG, you need to put $2,500 into your child's RESP annually.

If you don't max out your annual CESG, the eligibility room carries forward, but $1,000 is the maximum grant you can receive in any one year. So if you miss a year in contributing to the RESP, don't worry. You can carry that maximum $2,500 per year contribution room to the following year and make both the $2,500 contribution from the missed year as well as the $2,500 contribution for the present year. There is no limit on how much you can contribute each year, although there is a lifetime maximum of $50,000 per child. "You can catch up on the grants later if you double up on your contributions," says Heath. "Theoretically, you can start making RESP contributions at age eight, pay double each year and catch up on all the CESG grant money." But Sellery reiterates that the earlier you start contributing to the RESP, the longer the money has to grow. "Look for surplus savings in the family budget," he says. "Really, $200 monthly often comes down to a couple of dinners out."

But even if you're a very low-income household and can't contribute much, there's still good news for you. Simply opening an RESP for your child will make them eligible for the Canada Learning Bond (CLB)—a government grant to help lower-income families save for their child's post-secondary education. Qualifying for the grant provides your child with access to $500 at birth and an additional $25 to cover the costs of opening an RESP. Based on your income tax return, an additional $100 will be deposited in the RESP until your child turns 15. This can add up to more than $2,000 in grants. "This is free money for your child, and every low-income family should grab it," says certified financial planner Heather Franklin.

Deciding how to invest
Setting up the RESP is often the easy part. Things get hard when deciding how to invest the money. Unlike RRSPs, which will have decades to grow, RESPs really only have—at most—an 18-year horizon. That shorter time frame can make the investing process confusing. Should you be

aggressive in your investing approach and try to grow the money as quickly as you can? Or should you aim to be as conservative as possible? "The 20 per cent CESG grant alone is a great return on your money without having to do anything too aggressive," says Kvick.

The simplest and cheapest way to utilize RESP contributions is using them to buy a GIC or term deposit through your bank. Yes, rates are low, but you're already getting 20 per cent through the CESG.

The key is to keep it simple. If you have a higher tolerance for risk, keep 70 per cent or more of the RESP money invested in equities—the growth potential of equities is much higher than fixed income funds. If you are a DIY investor and like to manage your own money, a good asset allocation in these early years is about 75 per cent equities and 25 per cent fixed income. This provides your RESP with good growth in the early years, even if returns fluctuate because of the higher equity component. "I have 100 per cent of my children's RESPs in equities," says Heath. "But I'm comfortable with higher risk and higher volatility. You don't need to do that to get very good returns. Whatever suits your risk tolerance will work nicely for you."

To replicate this more aggressive investing approach, you can contribute equal amounts to four different mutual funds: so 25 per cent to a Canadian bond mutual fund, 25 per cent to a Canadian equity index mutual fund, 25 per cent to a U.S. equity index fund and 25 per cent to an international equity index mutual fund. If you want something simpler, a good low-fee balanced fund is a great option. Funds such as the Tangerine Balanced Portfolio or the Mawer Balanced Fund Class A are good choices, both with management expense ratios of about 0.8 per cent annually—a fairly low amount.

Another smart yet under-the-radar solution is a target-date mutual fund. RBC and BMO offer target-date education funds for RESPs. And while management expense fees are relatively high at nearly two per cent annually, it is a viable option for parents who want a stress-free option for their RESP investments. You simply choose the year your child is likely to go to college, invest your money then leave it alone. The portfolio is designed to automatically rebalance as your child's college start date nears to reduce risk by adding a larger fixed income component.

Kids aged five to seven
At this age, it's important to think about exactly what you want to achieve. Kvick recommends that parents consider how much of their child's education costs they actually want to cover. "Parents should have a shared goal," says Kvick. "Do you want to pay for your child's tuition? Or do you plan to pay for room and board as well as other expenses? These discussions go a long way toward focusing on the goal and what you really want to achieve." Heath has made some of these decisions in regards to his own two young kids' RESPs. "I think it's a good idea to get them to fund some of their own education, because they value it more," says Heath. Once you've had the talk about goals and have decided how much you want to cover and how much you will need to contribute, you need to monitor your RESP and revisit those goals annually. And if you haven't started already, you should make every attempt to teach your child the basics of good financial habits. "Then, as they get older, talk to them about deferred gratification so they learn the difference between short-term and long-term financial goals," says Heath. "Now's the time to start."

Kids aged eight to 14
Don't worry if you haven't contributed $2,500 a year into your RESP up until now—many new

parents can't. It's not too late to catch up on the grant money. The CESG accumulates every year for a child until December of the year she turns 17.

Remember, there's no limit on what you can put into an RESP each year, but there is a lifetime limit of $50,000. But don't be tempted to catch up too much at once—you have a limited amount of time to take advantage of the CESG. Because you can't collect more than $1,000 in a single year and the grant stops after the child turns 17, you need to open the RESP when your child is no older than 10 if you want to collect the full $7,200 in grants. And if you wait until your child is 16, you'll miss out on the CESG money.

Decrease your RESP's exposure to equities
Losing 20 to 30 per cent of your savings when your child is in Grade 8, 9 or 10 can put a serious dent in your plans. So a few years before they turn 17, you should ratchet down the equity allocation so you are close to 50-50 when your child is 14, perhaps to 80 per cent fixed income when they are 16 and finally to 100 per cent fixed income or cash when they are 17 and entering university. "When they are just about to enter university, you really need to keep things as safe as possible," says Kvick. "You have to ensure the money is there for room, board, tuition and books."

Kids aged 14 to 18
This is a time when many kids start getting a part-time job, whether it's delivering flyers, flipping burgers at McDonald's or cashing out groceries at the local No Frills. "Get them comfortable with receiving a paycheque and the concept that just because you earn $10 doesn't mean you get to keep $10," says Franklin. "Realizing they don't get to keep the entire amount because of various tax and other deductions is a real lesson for them."

If you want your child to pay for part of their post-secondary education—and if you haven't done this earlier—now's the time to talk with them about it. Also talk about scholarships they can apply for and encourage them to fill in the necessary applications. Approaching a high school guidance counsellor about opportunities for free money in Grade 9 is a good way to get the ball rolling. "All of this helps to make them responsible for some of their own education bill," says Sellery.

By the time your kids leave for school, they should have saved some of their own money for expenses. "You can now have a talk about the actual numbers and discuss how much money is there for them," says Kvick. "Then you can work out a budget for four years of university so they can see the annual costs of tuition, room, board, books and other expenses up close."

This is also a good time for parents to start learning about the best way to withdraw money from an RESP so that tax is minimized during the university years. Speak to your financial adviser or tax accountant about this the year before your child leaves for university, or research the topic on your own. A good book to read is *The RESP Book: The Simple Guide to Registered Education Savings Plans for Canadians* by Mike Holman. It will show you the best techniques for making the most of the money you've saved in RESPs, and is very useful no matter what stage of RESP savings your family is at. If you buy only one book on the topic, this is it.

What if you haven't contributed a dime to RESPs?
Even if your child has reached age 17 and you haven't saved any money at all for their university education, you have some good options available to help pay for some of the costs. For instance, if you made paying for your family's residence your main financial goal and you're now mortgage-free, you can simply pay for your child's post-secondary education through cash flow as university

expenses come up during the year. “Any mortgage payments can simply go toward paying for the child’s education as it’s needed,” says Kvick.

Or you may have been saving in a tax-free savings account. Tapping this money for university costs is also a good idea so your child doesn’t have to go deep into debt. “There’s at least $52,000 available in TFSA room that you may have contributed to over the years,” says Feth. “There’s no tax liability on this money if you take it out and you control it, not the kids. And if the kids decide not to go to university, it’s still all yours and you don’t have to do the special rollovers that need to happen with RESP money when you go to make withdrawals.”

Even if you’ve contributed to RESPs but haven’t saved enough, Feth suggests you use TFSA money to top up any shortfalls. “There’s only so much money available for any family at any one time,” says Feth. “Stay the course with your RESP and TFSA savings, and teach your child good budgeting and financial habits along the way.”