I’m short on cash. Can I dip into my RRSP to help cover my bills?

The pros and mainly cons of using your RRSP to paying down debt.

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If recent interest rate hikes have put you in a financial bind, you might be thinking of dipping into your RRSP to cover everyday expenses. But is it a good idea?

The answer, in most cases, is no.

Both Jason Heath, managing director at Objective Financial Partners, and Steve Bridge, an advice-only financial planner with Money Coaches Canada, say this strategy has several downsides.

For one, Bridge says once you withdraw money from an RRSP, it is taxed as income in the year it's taken out — and the contribution room is lost forever. The only instances when you can withdraw from an RRSP and pay it back are when you use the First-Time Home Buyers Plan to purchase a home or the Lifelong Learning Plan to fund your education.

The higher your income, the more you pay in taxes when you make early withdrawals. "If somebody with a modest to high income wants to take money out of their RRSP to pay off debt, they might lose somewhere between 20 and 50 per cent of that withdrawal to income tax," says Heath.

Amount of tax payable on early RRSP withdrawals

If you withdraw...	...the tax rate is
$0 to $5,000	10%
$5,001 to $15,000	20%
Over $15,000	30%

Rates differ in Quebec.

SOURCE: SUN LIFE TORONTO STAR GRAPHIC

Consider other options before touching your RRSP. "If your income is moderate to high and you are working, I would always consider an RRSP to be the last place you would look to pay debt or any expenses," says Heath. He recommends Canadians look to a Tax-Free Savings Account first, as it allows for tax-free withdrawals.

Bridge cautions that borrowing money to pay down debt without a plan is "no good" and might be a sign that you need to take a hard look at your budget. If you really have to borrow to pay down debt, it should be a short-term solution to cash-flow issues, and Bridge suggests using a line of credit instead of racking up expenses on credit cards.

Lines of credit offer lower interest rates than credit cards. Most credit cards charge an annual interest rate of around 20 per cent. Meanwhile, according to the personal finance comparison website Finder, the current average interest rate for a secured personal line of credit is about four per cent and seven per cent for an unsecured one.

“Sometimes people get into bad financial situations and don’t have another option,” says Heath. “It’s not to say you can’t catch up on replenishing your RRSP later, but I think you really need to consider all options before an RRSP withdrawal.”