Should Mark invest his tax refund or put it to his mortgage?

He earns $200,000 annually and wants to prioritize his goals

by Janet Gray Dec 13, 2018

Q. I'm confused as to what to do with my tax refund—pay off the mortgage, or contribute to an RRSP or TFSA. I'm 39 years old, and in 2018 I expect to earn about $200,000 in Alberta, so my tax bracket is high. I'll probably earn about $125,000 to $150,000 in 2019. I have a mortgage of about $416,000, at about 3.2% interest with about 25 years left to pay it off. (I plan to accelerate this someday).

In 2017, I made RRSP contributions resulting in a $9,000 tax refund, so I planned to take $8,500 to put towards my mortgage, but I'm having second thoughts. Would it be more advantageous to me to put the money in an RRSP at 6% to 8% returns or higher, reducing my taxable income in 2018? (I am nowhere near my lifetime RRSP ceiling). Or perhaps even a TFSA? Or should I pay down the mortgage, and continue taking lump-sum refunds from tax returns each year to get the debt level down?

— *Mark*

A. Mark, thank you for this question. It's a common dilemma for many. At your high income and tax rate, you are right to be contributing to your RRSP to reduce taxes owing, especially since you are earning 6 to 8% on your RRSP. Best to then take your tax refund and make a lump sum payment on your mortgage which is applied directly to the principal thus reducing total interest paid and the amortization period too.

As well, I suggest you speak to your mortgage lender about the possibility of increasing your regular mortgage payments by an additional amount—even $100 per payment. This will further reduce the principal and the interest paid. Most mortgages allow for pre-payment amounts on your regular payments. Find a comfortable amount for now since you can often increase the amount later.

You don’t mention if you have any balances owing on consumer debt like credit cards? If you do, then that should be the first priority as the interest rates can often be 19% or more.

And finally, while a TFSA will not reduce your taxes owing on current income, if you have additional funds, it’s a great investment vehicle to start building up.

Janet Gray is a Certified Financial Planner (CFP) with Money Coaches Canada in Ottawa