

## RRSP or credit card bills?

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**Question:** Should I maximize my RRSP contribution or pay my credit card bills and invest in RRSPs when the bills are paid?

**Answer:** You should pay off your credit card bills before contributing to your RRSP. The answer to your question boils down to comparing paying off the credit card and investing in your RRSPs as two alternative investments.

Let's assume you have \$1,000 to invest. Let's also assume that the interest rate on your credit card is 15%. If you "invest" this \$1,000 into the credit card debt, your effective rate of return is a guaranteed \$150 over one year. Unlike a normal investment, your return will not be in the form of interest that the bank gives to you, but rather in the saved interest that you didn't have to give to the bank.

What guaranteed return can you expect within your RRSP? Current interest rates on GICs with a one-year term are approximately 2%. Yes, you might be able to get a 15% rate of return inside the RRSP, but not with same guaranteed yield as is promised by paying down your credit card.

While you do get a tax-refund by putting the money into the RRSP, keep in mind that by choosing to pay off the credit card, you are only deferring contributing to the RRSP. You don't lose your RRSP contribution room and will get this tax savings eventually.

Next year, when the credit cards are paid off, you can start using up your RRSP contribution room and will enjoy all the tax-savings associated with that. Meanwhile, for the year in which you paid off the credit cards you will have received a risk-free rate of return on your investments unmatchable in your RRSP. Bottom line, if someone offered me a risk-free investment outside of my RRSP with an after-tax return of 15% on the condition that I would have to defer making an RRSP contribution for a year, I would do it.

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