SUMMER ISSUE 1998

From D'Costa's Files

Nearly Anyone can get rich by saving

Chances are you will disagree with this statement: For most people, becoming rich is a matter of choice.

If it were, you might say, I'd be rich or on my way to becoming so, and my parents and children would be too. You might even become irritated that such a crazy notion should intrude into your comfortable, middle-class repose.

But there is a compelling case for the statement, one that can be demonstrated with facts, examples and anecdotes in a study for the Centre for the Study of American Business, a non-profit think tank at Washington University in St. Louis, Mo.

If a 22 year old man or woman made a one time investment of $ 2,000 and earned 10 percent a year on that money, he or she would have amassed $ 194,000 by age 70.

An investment of $ 2,000 every year at the same annual yield would net $ 2.1 million at age 70.

Ten percent is what the stock market has returned over the last seven decades, so it is conceivable it will be done again. But even if the return were just 6 percent, the result of setting aside $ 2,000 a year would be well over a half million dollars at age 70.

Taxes could be a problem, as they almost always are. Inflation also would be a problem. But even if it cut buying power in half, diligent savers still would end up with a lot more money than non-investors.

Two professors, Richard McKenzie of University of California, and Dwight Lee of the University of Georgia show the way. Their treatise has the nonacademic title, *Rich in America: A Few Easy Rules to Follow.*

They begin with question: How can an ordinary person with a modest annual income become rich? And they answer: "One surefire method is to live modestly," as many self-made wealthy people do. That is, save and enjoy the magic of compounding.

By doing so, they say, you will have an income level that will be the envy "of those who have chosen to fritter away their incomes on compact discs, chips, cigarettes and new cars."

Most people, they say, have the ability to save more than they do. But they end up choosing expensive consumption behaviors, like smoking, which can add up in terms of lost wealth.

For example: A retired person who smoked two packs of cigarettes a day since age 21, paying roughly $ 1.50 a pack in U.S. (a lot more in Canada) could have invested the money each year at 6 percent and been $ 150,000 richer at age 70. Make that 15 percent and he or she would have had $ 3 million-plus.

Most people have a reasonable income base, which used wisely means at least a small amount can be saved. But while meager amounts grow, they may not grow into substantial sums. Therefore, the professors developed "auxiliary rules."

The first of these is to stay in school as long as possible, since incomes grow with the level of schooling.

The others may involve sacrificing what you want for what will make you rich. The professors suggest if wealth is a priority, choose your profession accordingly.

In the U.S. teachers, for instance, earn half as much as engineers over a span of their careers.

And they suggest marrying someone with equal or higher level of education, and staying married. Married couples earn and save more; 95 percent of millionaires are married.

Courtesy of Associated Press, New York - by John Cuniff.

Borrowing from your RRSP to purchase a Home

The federal government introduced a home buyers plan in 1992 that allows individuals to borrow up to $20,000 from their RRSP to purchase a home. The plan was due to expire in 1994, but the 1994 federal budget extended the program indefinitely. The amounts borrows from the RRSP's must be repaid within 15 years. The concept appears straight forward, but like most tax driven programs, the devil is in the detail. Both spouses can withdraw $20,000 and the definition of spouse includes common-law relationships.

Eligible Individuals-

The program is for "first time" home owners, but the definition of a first time owner is an individual that has not owned a home in the past five years. Thus individuals withdrawing money from their RRSP in 1995 may not have owned a home since January 1, 1991. If you sold your home in 1991 and didn't own another in the interim, you could enter the program in 1996. The definition of eligible individual will not allow people to participate in the program if their spouse owned a home during the five year period and the couple lived in the home together.

Written Agreement Requirement-

In order to withdraw up to $20,000 from your RRSP and not have the amounts included in your income, you must enter into a written agreement to purchase a home before funds can be released from your RRSP. If the funds were withdrawn from the RRSP in 1995, you must purchase or build a home prior to October 1, 1996. The rules allow extensions and the purchase of a home other than the one designated in your written agreement, should circumstances impair your original decision.

RRSP Contribution

Readers are advised to get professional financial management advice.
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Restriction-

A contribution to your RRSP may be restricted if you participate in the plan. Any contribution made to your RRSP in the 89 days prior to withdrawing for the purposes of purchasing a home may not be deductible.

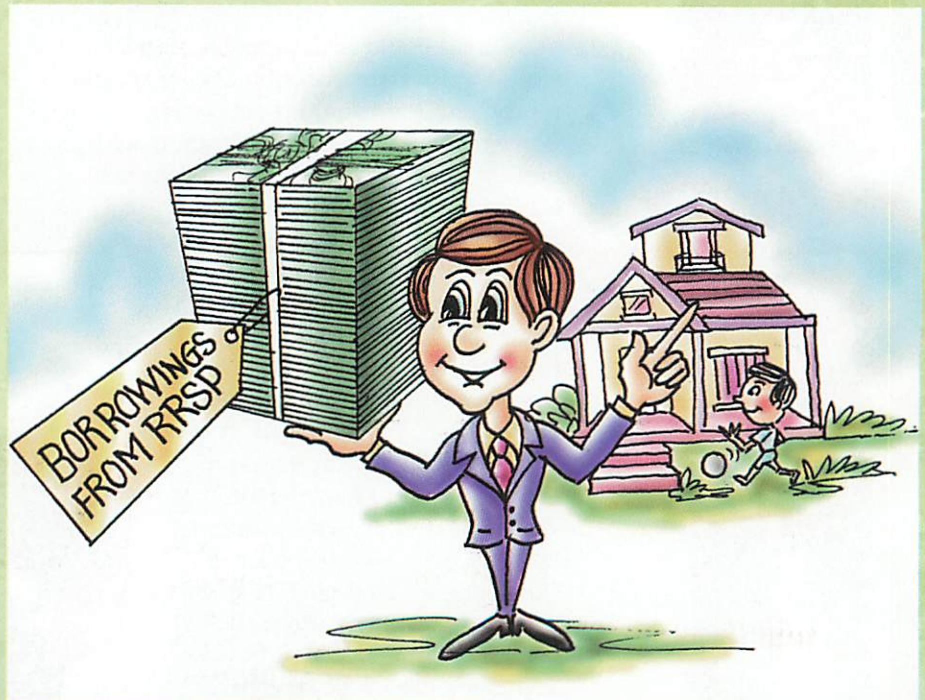
The funds withdrawn from your RRSP must be repaid within 15 years. The minimum repayment is 1/15 of the amount borrowed and if funds were borrowed from the RRSP in 1995, the first repayment is due in 1997 with the final payment due in 2011. Once you enter the plan, Revenue Canada will send an annual statement that outlines the amounts that have been repaid, the outstanding balance and the amount to be paid in the next calendar year. In order to make a repayment, a contribution is made to your RRSP along with Revenue Canada form T1037. This form requires an allocation of the contribution between the current year's RRSP deductible contribution and the non-deductible repayment. There are three potential scenarios related to the repayments:

1) the individual makes the proper amount of the designated repayment;

2) the individual makes a payment that is less than the required amount; and

3) the individual makes payment that is greater than the designated repayment amount.

If the individual making the RRSP repayments should die, become a non-resident or reach the



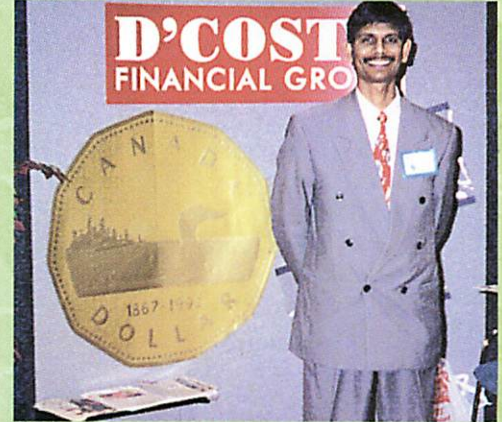
age of 71, there are additional tax consequences. If the individual dies, the unpaid amount has to be in the deceased's income in the year of death. If there is a surviving spouse, the spouse can jointly elect with the deceased's legal representative to not have the income included in the deceased's final tax return. The election allows the unpaid amount to be repaid from the spouse's RRSP. This election is not available if both spouses were participating in the home buyer's plan and at the time of death the repayment periods were identical.

If you become a non-resident while the loan to your RRSP is still outstanding, you must repay the entire loan before the date you file your return for the year, or no later that 60 days after you cease to be a Canadian resident, whichever is earlier. If you do not make the repayment by this deadline, you have to include the unpaid amount in your income in the year that you become a non-resident.

Since you cannot make a RRSP contribution the year after you turn age 69, you will be unable to repay your RRSP loan. In the year you reach age 69, you can choose to repay the unpaid balance or include in your income for each subsequent year as it becomes due, the amount that would have been your annual repayment.

Over 140 guests attended the Luncheon RRSP Seminar. Mr. Scott Edgington and Mr. Sayed Hussain also presented tax planning concepts at the seminar.

Glynis Lobo receiving her prize from Ms. D. Kayser at the DFG's Luncheon Seminar.



D'Costa Financial Group at the Trade Show (CNE) Booth

Mortgage Insurance Breakfast Seminar presented by Francis D'Costa to Homelife Realtors at the Pear Tree Restaurant down town.

BUSINESS OWNERS ALLOWED DEDUCTIONS!

The recent federal budget announced that starting in 1998, unincorporated owner-operators are now allowed to deduct premiums for health and dental premiums against their business income.

(Excert from The Budget in Brief 1998)
Deducting Health and Dental Premiums for Self-Employed Canadians

- To improve equity in the treatment of self-employed Canadians, owner-operators of businesses will now be able to deduct premiums for health and dental insurance against their business income.

Tom Kayser, one of the 3 speakers, at the Luncheon RRSP Seminar, presented by DFG.

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