# Four steps to maximizing your children's education savings

2021

ATB Wealth™

In 2018, a Maclean's article asked 23,384 Canadian university students six questions about the cost of their education. When it came to how the students pay for school, more than two-thirds indicated their parents or guardians were picking up at least some of the tab. But the really surprising part was that only 41% of students reported having Registered Education Savings Plans (RESPs), which means their parents had missed a key opportunity to help fund their children's education.

Student loans

48.4% with

51.6% without

RESP

41.3% with

58.7% without

Money from parents or guardians

67.2% with

32.8% without

Given the attractiveness of the 20% "bonus" paid directly into a beneficiary's RESP through the Government of Canada's Canada Education Savings Grant (CESG) program, in addition to the tax-deferred compounding that occurs within the account, these accounts present a superior education funding vehicle.

In 2020, only 53.3% of eligible CESG recipients in Alberta received basic grants into an RESP, and the average subscriber contribution was $1,532[1]—well below the threshold needed to earn the full $500 annual CESG.

[1]Source: Employment and Social Development Canada, Canada Education Savings Program — 2020 Annual Statistical Review, retrieved from:

https://www.canada.ca/content/dam/canada/employment-social-development/services/student-financial-aid/education-savings/reports/annual-statistical-review/Annual-Statistical-Review-2020-EN.pdf

# RESP basics

Before we dig into the value of RESPs in saving for post-secondary education, let's start with some program basics.

The following are some highlights of the current features of RESP accounts[2]:

| | |
|---|---|
| **Tax treatment** | • Contributions are not deductible from the subscriber's taxable income.<br>• Contributions can be withdrawn tax-free[3].<br>• If any investment income accrued within the RESP as well as grants are withdrawn while a beneficiary is enrolled in a qualifying educational program, those amounts will be included in the beneficiary's taxable income at time of withdrawal. This is referred to as an education assistance payment (EAP). |
| **Annual contribution limit per beneficiary** | None |
| **Lifetime contribution limit per beneficiary** | $50,000 |
| **Maximum time accounts may remain open** | 36 years[4] |
| **Annual basic CESG limit** | • 20% of annual contributions up to $500 per year and a lifetime maximum of $7,200.<br>• Grant room (unused basic CESG amounts) accumulates until the end of the year in which the child turns 17.<br>• Subscribers can make up for unused CESG one year at a time.<br>• There are eligibility restrictions for children who are 16 or 17 years old. |
| **Additional CESG** | 10% to 20% of the first $500 in annual contributions. Eligibility is based on family income. |
| **Canada Learning Bond** | $500 upon opening and $100 per year for 15 years. Eligibility is based on family income. |

For more information, refer to ATB's RESP reference guide.

[2]Terms and conditions outlined are current as of 2021-11-17, go to https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/rc4092/registered-education-savings-plans-resps.html for the full RESP guide published by CRA.

[3]If the RESP beneficiary is not enrolled in a qualifying program at the time of withdrawal, a withdrawal of contributions may require a repayment of the CESG.

[4]Unless the plan is a specified plan, which is an individual RESP plan for a beneficiary who is entitled to the disability tax credit, specified plans must be closed by the end of the  year of the 40th anniversary of the plan.

# Get started and stay on track

In this article we walk through four steps parents can take to establish and maintain a plan to support their children with post-secondary education expenses, and review how best to maximize RESP savings towards those costs.

# Step 1: Resolve the "what ifs"

When considering an RESP, there are a few common questions people ask. Here we answer key concerns.

### What if my child doesn't attend a post-secondary program right after high school?

No problem! An RESP can stay open for 36 years, so they have lots of time to withdraw funds.

### What if they don't attend a conventional program at a post-secondary institution?

Qualifying educational programs are not limited to conventional undergraduate/graduate studies at Canadian universities. For the purposes of an Educational Assistance Payment (EAP), a post-secondary educational institution can be any of the following:

- University, college or other educational institution in Canada that is designated under the Canada Student Financial Assistance Act. *In Alberta alone there are 245 designated educational institutions;*
- An educational institution in Canada certified by the Minister of Employment and Social Development as an institution that provides courses (other than courses for university credit) that furnish a person with skills for, or improve a person's skills in, an occupation;
- A university outside Canada that has courses at the post-secondary school level at which the beneficiary is enrolled on a full-time basis in a course of not less than three consecutive weeks; and
- A university, college or other educational institution outside Canada that has courses at post-secondary school level at which a beneficiary was enrolled on a full or part-time basis in a course of not less than 13 consecutive weeks.

### What if my child does not pursue post-secondary education?

In the event your child does not attend any qualifying educational programs you still have options for your accumulated RESP funds. The Government of Canada outlines five choices here.

# Step 2: Establish a goal

As parents, your next step is to research potential education costs and then determine how much of the cost you are willing to cover. Many parents want their children to financially contribute to their own education so they have some skin in the game.

Let's put some numbers together. To get started with our research, we reviewed the Average Canadian undergraduate fees by field of study published by Statistics Canada for the 2021/2022 school year. Tuition fees ranged from a low of $4,947 annually for an education degree to a high of $22,731 for dentistry. There are also additional fees to account for, including student fees, books, and accommodation for students living away from home.

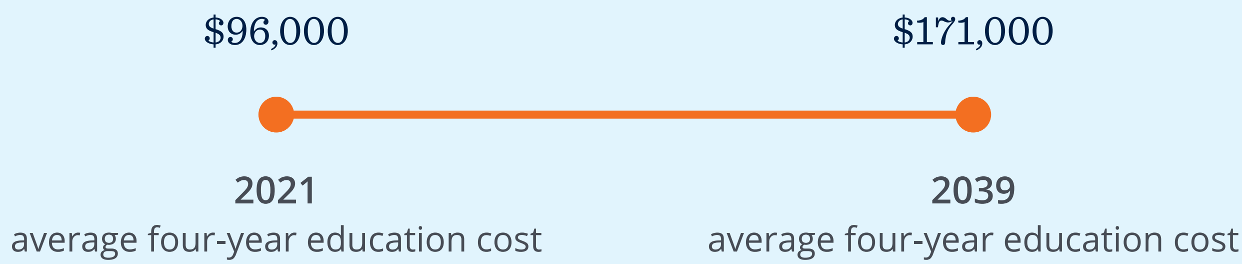
Given the vast range in tuition fees, we focused our research on a four-year undergraduate business/commerce/management program with high levels of student enrolment. We sampled the fall 2021 undergraduate student costs, including residence, published on the websites of eight Canadian universities across Canada. The average first-year cost was $24,000 to attend two full-time semesters per year, assuming the student lived on campus, in a single room, with an eight-month daily meal plan.

Now we must consider what the current cost of $24,000/year will be at the time of enrolment. From 2008/09 to 2018/19, undergraduate tuition fees in Canada increased an average of 3.7% per year against general inflation of 1.6% over the same period[5]. Interestingly, tuition decreased an average of 5.3% across Canada in the 2019/20 period, influenced largely by a tuition decrease in Ontario. This timeframe also included the start of the COVID-19 pandemic, which impacted major post-secondary institutions. Additionally, we must consider that not all costs related to education (such as food, shelter, transportation) may increase at the same rate as tuition and may be more in line with general inflation in Canada.

[5]Source: Statistics Canada. Table 37-10-0003-01 Canadian undergraduate tuition fees by field of study

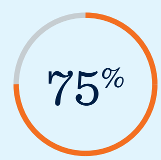
If we assume then that the blended cost of education will increase 3% annually from today, the total cost over four years in a $24,000/year program for a child born in 2021 will be $171,000 (enrolment at age 18, 2039). If parents cover part of the cost, say 75%—or $18,000/year—the total cost is projected to be $128,000, and at 50% coverage—$12,000/year—the amount is $85,500.

### Assuming a 3% annual increase in blended cost of education:

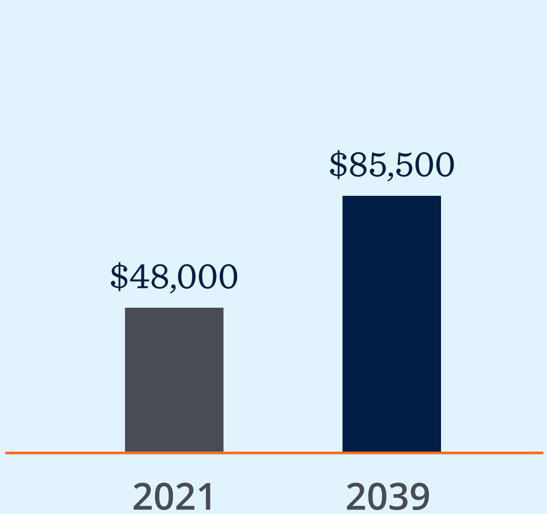



### Partial yearly cost contributed:


When covering 50% of the cost




When covering 75% of the cost



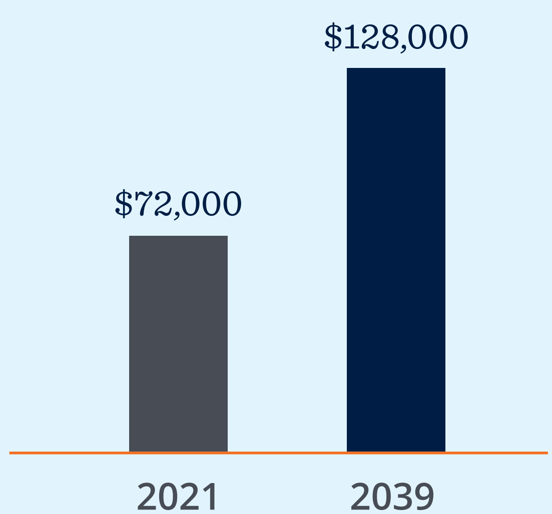



Table 1: The chart below illustrates the anticipated future cost depending on the beneficiary's year of birth and budget based on today's dollars

| Year of birth | Year of admission | Total cost for four years (based on a $24,000/ year budget today and 3% inflation) | Total cost for four years (based on an $18,000/ year budget today and 3% inflation) | Total cost for four years (based on a $12,000/year budget today and 3% inflation) |
|---|---|---|---|---|
| 2009 | 2027 | $119,891 | $89,918 | $59,946 |
| 2010 | 2028 | $123,488 | $92,616 | $61,744 |
| 2011 | 2029 | $127,193 | $95,394 | $63,596 |
| 2012 | 2030 | $131,008 | $98,256 | $65,504 |
| 2013 | 2031 | $134,939 | $101,204 | $67,469 |
| 2014 | 2032 | $138,987 | $104,240 | $69,493 |
| 2015 | 2033 | $143,156 | $107,367 | $71,578 |
| 2016 | 2034 | $147,451 | $110,588 | $73,726 |
| 2017 | 2035 | $151,875 | $113,906 | $75,937 |
| 2018 | 2036 | $156,431 | $117,323 | $78,215 |
| 2019 | 2037 | $161,124 | $120,843 | $80,562 |
| 2020 | 2038 | $165,958 | $124,468 | $82,979 |
| 2021 | 2039 | $170,936 | $128,202 | $85,468 |
| 2022 | 2040 | $176,064 | $132,048 | $88,032 |
| 2023 | 2041 | $181,346 | $136,010 | $90,673 |

# Step 3: Build a plan and start early

Moving from goal setting to planning, parents now need to decide how they'll fund the educational goal they've established. Do you want to open an RESP and build a balance that covers most if not all of the projected educational goal? Or, will you use other sources, such as available cash flow at the time of enrolment, non-registered savings, or even TFSAs? If you're using your funding sources for multiple purposes, carefully consider the impact on other financial goals such as retirement or debt repayment.

When saving for any goal, take advantage of the power of compounding. With compounding, your investment income grows each year because you continue to earn returns on already accrued income and growth in the account. Continuing with our example of $24,000/year in education expenses, let's look at how we can fund 50% of this cost ($12,000/year in today's dollars) for a child born in 2021. We want the RESP worth around $85,000 by the end of the year when our beneficiary is 17. The two charts on the following pages show the impact of saving money in an RESP sooner versus later.

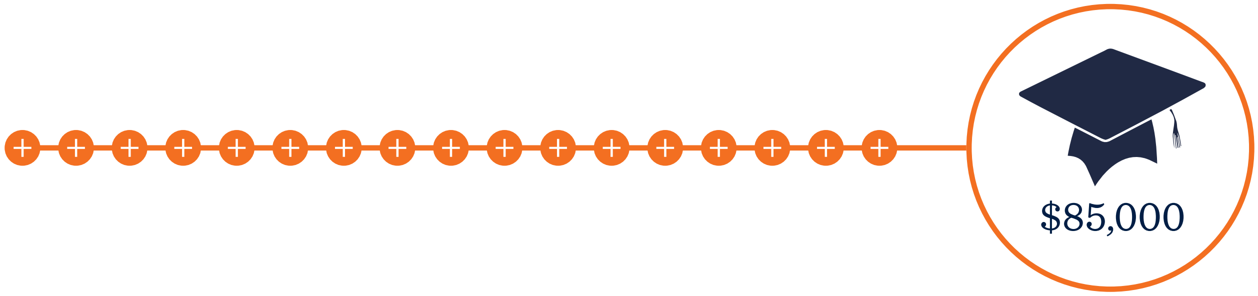


Table 2: Parents start contributing to RESPs the year their child is born

| Year | Age of beneficiary | Contribution | Grant | Rate of return 5%[6] | Year ending balance |
|---|---|---|---|---|---|
| 2021 | 0 | $2,500 | $500 | $150 | $3,150 |
| 2022 | 1 | $2,500 | $500 | $308 | $6,458 |
| 2023 | 2 | $2,500 | $500 | $473 | $9,930 |
| 2024 | 3 | $2,500 | $500 | $647 | $13,577 |
| 2025 | 4 | $2,500 | $500 | $829 | $17,406 |
| 2026 | 5 | $2,500 | $500 | $1,020 | $21,426 |
| 2027 | 6 | $2,500 | $500 | $1,221 | $25,647 |
| 2028 | 7 | $2,500 | $500 | $1,432 | $30,080 |
| 2029 | 8 | $2,500 | $500 | $1,654 | $34,734 |
| 2030 | 9 | $2,500 | $500 | $1,887 | $39,620 |
| 2031 | 10 | $2,500 | $500 | $2,131 | $44,751 |
| 2032 | 11 | $2,500 | $500 | $2,388 | $50,139 |
| 2033 | 12 | $2,500 | $500 | $2,657 | $55,796 |
| 2034 | 13 | $2,500 | $500 | $2,940 | $61,736 |
| 2035 | 14 | $2,500 | $200 | $3,222 | $67,657 |
| 2036 | 15 | $2,500 | $0 | $3,508 | $73,665 |
| 2037 | 16 | $2,500 | $0 | $3,808 | $79,974 |
| 2038 | 17 | $2,500 | $0 | $4,124 | $86,597 |
| **Total** | | **$45,000** | **$7,200** | **$34,397** | **$86,597** |

*For the purposes of this illustration we assume that the RESP subscribers are eligible to receive CESG only, (not Canada Learning Bond or additional CESG amounts). Contributions are made annually to maximize the amount of CESG the beneficiary is entitled to ($7,200). Deposits are assumed to be made at the beginning of each period and returns at the end.*

Table 3: Parents start contributing to an RESP when their child is five and "caught up"[7] on unused CESG that carried forward for the first five years of their savings plan

| Year | Age of beneficiary | Contribution | Grant[7] | Rate of return 5%[6] | Year ending balance |
|---|---|---|---|---|---|
| 2021 | 0 | $0 | $0 | $0 | $0 |
| 2022 | 1 | $0 | $0 | $0 | $0 |
| 2023 | 2 | $0 | $0 | $0 | $0 |
| 2024 | 3 | $0 | $0 | $0 | $0 |
| 2025 | 4 | $0 | $0 | $0 | $0 |
| 2026 | 5 | $5,000 | $1,000 | $300 | $6,300 |
| 2027 | 6 | $5,000 | $1,000 | $615 | $12,915 |
| 2028 | 7 | $5,000 | $1,000 | $946 | $19,861 |
| 2029 | 8 | $5,000 | $1,000 | $1,293 | $27,154 |
| 2030 | 9 | $5,000 | $1,000 | $1,658 | $34,811 |
| 2031 | 10 | $2,500 | $500 | $1,891 | $39,702 |
| 2032 | 11 | $2,500 | $500 | $2,135 | $44,837 |
| 2033 | 12 | $2,500 | $500 | $2,392 | $50,229 |
| 2034 | 13 | $2,500 | $500 | $2,661 | $55,890 |
| 2035 | 14 | $2,500 | $200 | $2,930 | $61,520 |
| 2036 | 15 | $2,500 | $0 | $3,201 | $67,221 |
| 2037 | 16 | $2,500 | $0 | $3,486 | $73,207 |
| 2038 | 17 | $2,500 | $0 | $3,785 | $79,492 |
| Total | | $45,000 | $7,200 | $27,292 | $79,492 |

[6]Our 5% return assumption is based upon FP Canada's 2021 projection assumption guidelines for return rates, assuming a typical long-term balanced asset mix within the RESP

[7]You can make up for unused CESG one year at a time

When we compare tables 2 and 3, we note the savings amount under both is equal—$45,000 in subscriber contributions—matched by $7,200 in grants. However, between the delayed start and catching up on unused CESG amounts for five years, the subscriber misses out on more than $7,000. In context, that's almost a full year's commerce tuition fee today.

Before starting any RESP savings plan you should work with your financial advisor to clarify and quantify your goal and then assess the appropriate:

- contribution amounts
- frequency of contributions
- number of years you may need to make contributions
- asset allocation of the investments to be held in your RESP account

# Step 4: Manage your education funding plan

As with planning for any financial goal you need to revisit your education funding plan and accumulated savings regularly to assess if you're staying on track.

Once your child is in high school you can have more focused conversations with them about their post-secondary education—what programs they're interested in, where they're offered and what those costs look like.

Will your child be eligible for scholarships or bursaries? Now is the time to discuss the financial responsibilities your child will need to bear. Teaching your child good saving habits while they're in high school will help them practice lifelong spending and savings patterns where they prioritize paying their future selves first, before any immediate gratification.

You should also assess if the anticipated cost you want your child responsible for is reasonable. Consider the number of hours your child may need to work to contribute funds from their own wages. Will it interfere with their ability to successfully complete their course work? Or will they be burdened with high student loan balances upon graduation?

Finally, once your child is in high school, assess the risk of the investments held in the RESP account. Significant withdrawals may need to occur in the next three years or less. Now is the time to limit downside risk to the investments, should a market correction reduce the RESP balance, and your ability to meet your child's expenses.

# Summary

So when is the right time to start planning for your child's post-secondary education? Right now! Consider that your time horizon to save for your child's education may be 18 years or less compared to planning for your own retirement, which could span 30 years or more. The shorter the planning horizon, the more focused you need to be.

Education expenses such as tuition, fees and books are generally considered a fixed expense and as shown in step two, they have increased dramatically over time in Canada. If you miss out on valuable government matching grants and compounded returns you must rely more on less efficient funding sources to pay for those fixed expenses, such as your or your child's after-tax income during enrolment, or by taking on debt to pay for costs not covered by existing savings.

Even if your child is now a teenager and you're worried you've missed the RESP bus, don't let that stop you from talking to your advisor. ATB Wealth advisors can help you work through a goal-planning exercise and evaluate all your funding options so you can build a plan and take one item off the list of things that keep you awake at night—not the least of which is being a parent to a teenager.