5 smart ways to use your tax refund

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Expecting an income tax refund? Before rushing out to spend it, consider how you can put it to work to enhance your financial future.

You just pushed the send button on your income tax return and you can't wait for your refund to be deposited into your account. But before you start thinking about using that money for an exotic vacation or a down payment on a new car, you may want to think instead about how it can enhance your family's financial picture over the long term.

Here are 5 options to consider:

1. Start an emergency fund

At some time in your life, one of the following things may happen: You will lose your job; your car will break down when you need it for work; or you will need to take extended, unpaid time off work to care for a sick or dying family member. By having the money to cover about 3 to 6 months of necessary living expenses in an easily accessible, high-interest emergency savings account or a TFSA (if you have contribution room), you will be better able to financially weather a crisis. Your income tax refund can form the basis for an emergency fund or enhance your current emergency savings.

2. Top up your RRSP

For the 2018 tax year, the Registered Retirement Savings Plan (RRSP) contribution limit is 18% of earned income from the previous year, to a maximum of $26,230 (with adjustments for company-sponsored pension plan contributions). Yet studies consistently show that less than half of Canadians contribute to their RRSP every year. If you haven't been contributing the maximum to your RRSP, you can use your income tax refund to help accumulate a larger nest egg for your retirement. The interest on your money will also compound over a longer period than if you only make contributions at the end of each year.

3. Pay down credit card debt

According to calculations by CreditCards.com, the average adult Canadian carries about 2 credit cards. The Canadian Bankers Association reports that about 56% of Canadians pay off their accounts in full each month – but that means that 44% of us are paying interest rates of 15, 20 or even 30% on our outstanding balances. Paying down or paying off your credit card debt will give you more disposable income to boost your retirement savings.

4. Pay down your mortgage

Given that the average Canadian home sold for $609,700 in February 2018, according to the Canadian Real Estate Association — and the sale price of an average detached home in Toronto topped $1.2 million the following month, per the Toronto Real Estate Board — there's a good chance you took on a large mortgage to purchase your family home. Mortgage interest rates have started to inch up, and your payments may no longer be affordable the next time your mortgage renews. So, depending on your situation, it may make sense to take advantage of early pre-payment privileges to reduce your mortgage debt as quickly as possible. Once your mortgage is paid down or paid off, you can catch up on RRSP contributions.

5. Open an RESP

For the 2017-2018 school year, the average undergraduate tuition fee was $6,571, according to Statistics Canada — and that's only 1 year out of a 4-year program and doesn't count books and living costs. Those expenses can add 10s of thousands of dollars to the bill — and by the time your young children are of university age, the total will likely be a lot higher. If you're not saving for your child in a Registered Educational Savings Plan (RESP) you're leaving free money on the table. That's because when you contribute to an RESP for your child, the Canada Education Savings Grant adds 20 cents to every dollar you contribute, up to a maximum of $500 on an annual contribution of $2,500 until your child is 17. Special rules apply, so it's important that you speak to your financial advisor in order to maximize the grant. Using your tax refund to make annual RESP contributions is a great investment in your child's future.