

# RRSP participation – the sooner the better

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To maximize registered retirement savings plan (RRSP) opportunities, “the golden rule is: start saving early” (Gay, 1995). Recently, much attention has focused on the magic of compound interest (Stokes, 1995) and its effects on long-term contributions. In particular, financial institutions’ RRSP marketing campaigns seem to have tapped into concerns about a possible reduction or elimination of public pension programs. Growing numbers of young workers are contributing to RRSPs.

Past analysis has dealt with the RRSP population as a whole (Frenken, 1995; Frenken and Maser, 1993). This article focuses on eligible taxfilers aged 25 to 29. It examines their rate of participation, frequency of contribution and average amounts deposited from 1983 to 1992. It also looks at the incidence of cash withdrawals and analyzes some of the characteristics that increase or decrease the likelihood of RRSP participation.

## Increasing popularity of RRSPs

The overall RRSP participation rate has increased dramatically in recent years. In fact, from 1983 to 1992 the proportion of eligible taxfilers of all ages who contributed to an RRSP grew from 20% to 36%, or from 2.5 million contributors to 4.9 million. Not all participated every year, however. There were 8.6 million different RRSP contributors during this period and they participated, on average, 4.2

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## Data source and definitions

This article uses the Small Area and Administrative Data Division's longitudinal administrative data (LAD) file. The LAD, derived from the T1FF (File on Families based on the T1 income tax form), represents a random sample of 1% of all taxfilers and their dependants who have social insurance numbers. Once individuals are selected for inclusion, they remain in the file. In 1992, the LAD contained information on 202,390 individuals. It is estimated (on the basis of demographic estimates of the population) that in 1992 almost 96% of Canadians were represented in the weighted file. A new LAD file based on a 10% sample is also available.

The focus of this article is younger taxfilers, those aged 25 to 29 in two specific years, 1983 and 1988. Only taxfilers eligible in at least one year of 5 – 1983 to 1987 for the first group or 1988 to 1992 for the second group – were analyzed. Those under 25 were excluded from the analysis, since few contribute to RRSPs at that age (Frenken, 1995).

years out of 10. Over half participated 3 years or less, while only 7% reported contributions in all 10 years.

To determine how actively young people have participated, two cohorts of younger taxfilers were studied (see *Data source and definitions*): those aged 25 to 29 in 1983 (1983 cohort) and in 1988 (1988 cohort). Each cohort was followed for 5 years, the first from 1983 to 1987, and the second from 1988 to 1992.<sup>1</sup>

In 1983, 11% of eligible taxfilers in the 1983 cohort contributed to an RRSP. This proportion rose to 22% in 1987 (Table 1). Of the 2.2 million taxfilers eligible to contribute over that 5-year

Averages of contributions and withdrawals exclude non-participation years. All amounts are in 1990 dollars.

**Cohort:** persons of the same age range grouped together for the purpose of studying specific characteristics over time.

**Eligible taxfiler:** an individual who has income that qualifies for RRSP contribution purposes, which in this study means employment income from both paid work and self-employment for the tax year. The definition of eligible income was changed in 1991, but this change had little effect on younger taxfilers.

**Frequency:** in this study, refers to the number of years the person contributes to or withdraws from an RRSP during the study period. The years need not be consecutive. Some individuals may have filed tax returns annually, but contributed sporadically; others may not have filed each year.

**Low income:** in this study, refers to a range from one dollar to \$19,999.

period, 30% (679,000) did so at least once. Over 60% of contributors participated in only one or 2 years, while 11% did so all 5 years.

On average, members of this cohort participated in RRSPs 2.4 years of the 5. Many of those who participated in only one or 2 years did so at the end of the period of study.

Some 987,000 of the 2.5 million eligible taxfilers in the 1988 cohort contributed at least once over the 5 years, for a participation rate of 40%. For each year the rate was considerably higher than that of the equivalent year in the first cohort. In year one it was 19%, 8 percentage points higher than it had been in the 1983 cohort. In

**Table 1  
Young RRSP contributors**

	Eligible taxfilers	Contributors	
		Number	% of eligible taxfilers
	'000	'000	%
<b>1983 cohort *</b>			
1983	1,845	212	11
1984	1,858	275	15
1985	1,847	328	18
1986	1,889	391	21
1987	1,900	410	22
<b>1988 cohort **</b>			
1988	2,036	393	19
1989	2,059	480	23
1990	2,061	525	25
1991	2,039	602	30
1992	2,033	655	32

Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1983.

\*\* Aged 25 to 29 in 1988.

year 5 it was nearly 11 percentage points higher.

The average frequency of participation in the 1988 cohort was 2.7 years of the 5, an increase of 0.3 over that recorded in the 1983 cohort. Although the 51% of contributors who participated only one or 2 years was down almost 10 percentage points, the percentage who contributed in all 5 years (17%) was much higher than the previous 11% (Chart A). So, not only did the percentage of young eligible taxfilers contributing to RRSPs increase, their frequency of participation was also higher.

**Differences in average contributions**

From 1983 to 1987, the 679,000 contributors in the 1983 cohort deposited \$4.2 billion for an average annual amount of \$2,600 (1990 dollars). Men’s average annual contributions were larger than women’s: \$2,800 versus \$2,300. This can be explained in part by their higher earnings, as RRSP contributions are highly correlated with income level (Frenken, 1995).

During the study period, these men earned on average \$40,200 and women, \$28,000.

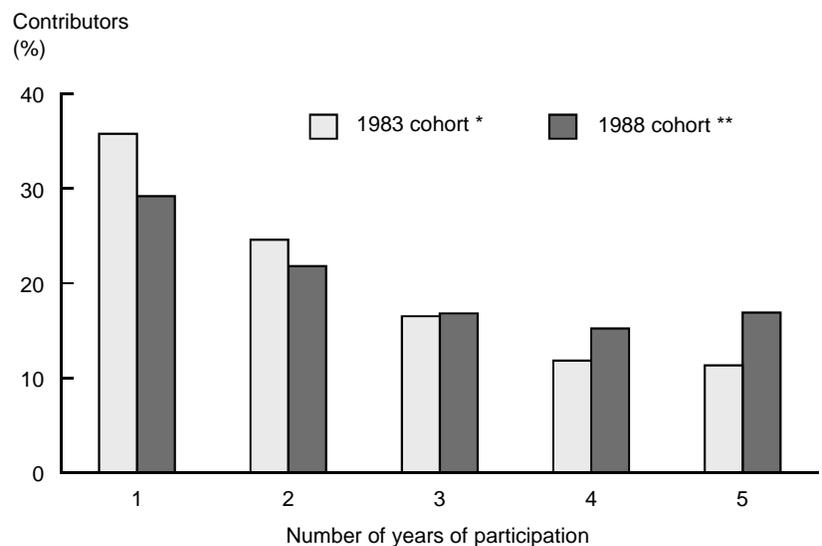
Despite the fact that the 1988 cohort’s total contribution (\$5.8

billion) was considerably higher than the 1983 cohort’s, the average annual deposit for the second period was 15% lower, or \$2,200 (Table 2) and the number and proportion of small contributions higher (Chart B). Both men’s and women’s averages decreased by about \$400. Contributions dropped significantly each year, especially in 1990,<sup>2</sup> when there was a 20% decrease from the same point (1985) in the earlier cohort. The decline can be attributed to lower employment incomes, which averaged only \$37,300 for men and \$27,200 for women. Overall, the proportion of employment income contributed fell from 7.2% (1983 cohort) to 6.6% (1988 cohort).

**More contributors with low earnings**

At the same time, the proportion of eligible taxfilers who contributed rose from 30% to 40%. Much of the growth was attributable to individuals with low earnings. The

**Chart A  
The proportion of frequent RRSP contributors has increased.**



Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1983.

\*\* Aged 25 to 29 in 1988.

Table 2  
RRSP contributions and employment income of young RRSP contributors

	Number of contributors '000	Contributions		Employment income	
		Total \$ millions	Average 1990 \$	Total \$ millions	Average 1990 \$
<b>1983 cohort *</b>					
Overall	1,616 †	4,151	2,600 ††	56,898	35,300 ††
1983	212	496	2,300	6,924	32,800
1984	275	674	2,400	9,248	33,700
1985	328	833	2,500	11,472	35,100
1986	391	1,062	2,700	14,043	36,100
1987	410	1,085	2,600	15,212	37,200
<b>1988 cohort **</b>					
Overall	2,654 †	5,779	2,200 ††	87,333	33,000 ††
1988	393	844	2,100	12,505	31,900
1989	480	980	2,000	15,789	33,000
1990	525	1,075	2,000	17,485	33,300
1991	602	1,319	2,200	19,710	33,000
1992	655	1,561	2,300	21,844	33,600

Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1983.

\*\* Aged 25 to 29 in 1988.

† Contributors were counted once for each year of contribution.

†† These figures represent the average amounts deposited and/or earned by contributors per year of participation over the 5-year period.

viduals with lower employment incomes represented 33% of the gain; those with higher earnings, 20%. Thus, women with low earnings accounted for most of the drop in average contributions from the 1983 to the 1988 cohort.

At the family level, most contributors with low earnings belonged to families with low earnings, including those where spouses worked. Some 98% were married, and 63% of these had family earnings less than double their individual level.

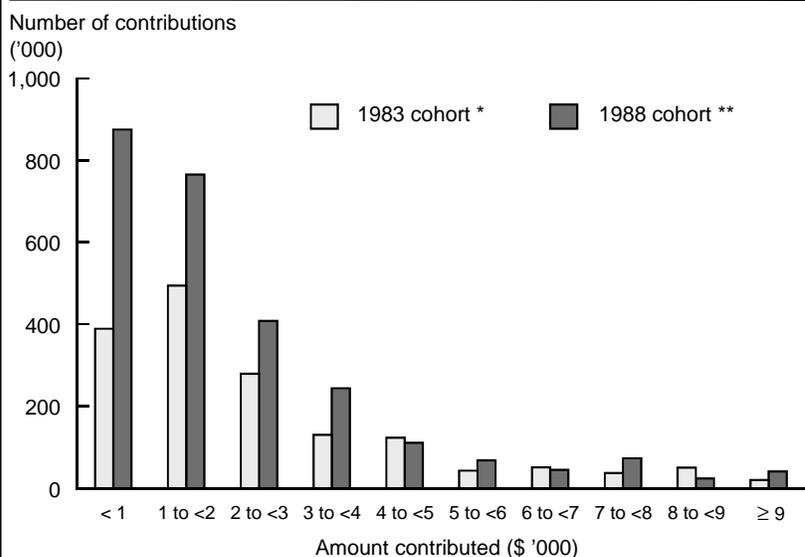
### Lower frequency of contribution

The average contribution of those who participated all 5 years was not significantly different from one cohort to the next (Table 3). Neither did the income dynamics of this group change. These people continued to have relatively high annual earnings and, in most cases, contributed annually to defer taxes. On

number of RRSP participants with low employment income jumped 64% from one cohort to the next, to over 400,000. Because they were responsible for over 43% of the increase in the total number of contributors, they had a dampening effect on both employment income and RRSP contribution averages. Those earning \$40,000 and over were also contributing in greater numbers, but their growth was much lower (20%). They were responsible for just 13% of the increase in contributors.

The differences between men's and women's contribution patterns are considerable. In 1988, women who earned under \$20,000 (but greater than zero) were responsible for 58% of the increase in the number of female contributors, while those who earned \$40,000 and over accounted for less than 3%. Among male taxfilers growth was more evenly distributed. Indi-

Chart B  
The number of small contributions has grown dramatically.



Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1983.

\*\* Aged 25 to 29 in 1988.

**Table 3**  
**Average RRSP contribution by cohort and frequency of contribution**

	Frequency	Contribution
	years	1990 \$
1983 cohort *	1	2,300
	2	2,500
	3	2,500
	4	2,700
	5	2,800
1988 cohort **	1	1,700
	2	1,800
	3	2,000
	4	2,200
	5	2,700

Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1983.

\*\* Aged 25 to 29 in 1988.

the other hand, participants with lower earnings tended to contribute more sporadically. Of those who contributed only one or 2 years, members of the 1988 cohort contributed on average over 25% less than their predecessors. So, although the number of contributors with lower employment incomes grew, the size of contribution diminished and continued to be infrequent.

### Characteristics of RRSP contributors

Characteristics likely to affect participation in an RRSP are similar for both cohorts. Most influential is the younger worker's level of earnings (Table 4). In the 1988 cohort, 21% of individuals earning less than \$10,000 contributed at least once to an RRSP. This proportion increased for each group to 88% for those earning \$50,000 or more. And persons with some investment income (which is highly correlated with levels of employment income) had a participation rate of 58%, 2.5 times higher than those with no in-

vestment income. Also, eligible taxfilers with some self-employment income were significantly more likely to participate than those reporting no such income. This may be because self-employed individuals are not able to participate in employer-sponsored pension plans, and therefore have a greater need to plan for their own retirement. Being married also dramatically increases the odds of contributing, while having children decreases the odds.

### Significant withdrawals

RRSP savings cashed in annually by taxfilers of all ages must be taken into account in a study of RRSP contributions. (For a detailed analysis of RRSP withdrawals in recent years see Frenken, 1996.) Since withdrawals have been iden-

tifiable from tax data only since 1988, this analysis considers those from the second cohort.<sup>3</sup> Of the 2.5 million younger taxfilers eligible to contribute during this time, over 10% or 256,000 withdrew at least once from their RRSPs. The average annual amount withdrawn was \$3,200 for men and \$2,600 for women (Table 5).

Persons who withdrew at least once did so on average 1.3 years out of 5. Their average frequency of contribution was 2.7 years out of 5, which may explain, in part, why the average amount withdrawn was significantly higher than the average amount of contribution. Those cashing in all their RRSP savings in one year may have had more than one years' contribution available to them.

**Table 4**  
**Characteristics of young RRSP contributors (1988 cohort \*)**

	Eligible taxfilers	Contributors	
		Number **	% of eligible taxfilers
	'000	'000	%
<b>Total</b>	<b>2,476</b>	<b>987</b>	<b>40</b>
<b>Employment income</b>			
\$1 to 9,999	1,170	241	21
\$10,000 to 19,999	409	167	41
\$20,000 to 29,999	422	233	55
\$30,000 to 39,999	276	186	67
\$40,000 to 49,999	126	96	76
\$50,000 and over	73	64	88
<b>Investment</b>			
Income declared	1,177	683	58
None declared	1,299	304	23
<b>Self employment</b>			
Income declared	340	152	45
None declared	2,136	835	39
<b>Marital and parental status</b>			
Married			
With children	1,439	593	41
Without children	445	251	56
Single			
With children	340	81	24
Without children	253	62	25

Source: Small Area and Administrative Data Division

\* Aged 25 to 29 in 1988.

\*\* Number eligible to contribute who did so at least once over the 1988-to-1992 period.

Table 5  
Average withdrawal made by  
persons aged 25 to 29 in 1988

Year	Men	Women
	1990 \$	
<b>Overall</b>	<b>3,200 *</b>	<b>2,600 *</b>
1988	3,100	2,400
1989	3,100	2,500
1990	3,500	2,700
1991	3,400	2,700
1992	3,100	2,800

Source: Small Area and Administrative Data Division

\* These averages represent the average withdrawal per year of withdrawal, over the 5-year period.

People dipping into these savings were still fewer than those contributing, and total amounts cashed in were small compared with contributions. For every young person withdrawing over the 5-year period there were almost four contributors, and for every one dollar withdrawn there were six in contributions. In 1992, the most recent year in this study, 655,000 young people contributed \$1.6 billion to RRSPs while just 81,000 withdrew \$241 million.

Contributors and withdrawers were not mutually exclusive in any given year; some people both contributed and withdrew in a single tax year. Of those who withdrew, 44% contributed the same year. Most were not sporadic or first-time contributors, but participated an average 3.2 years of the 5.

This pattern may have been caused in part by the timing of these transactions. While withdrawals are reported on a calendar year basis, allowable contributions can be made up to 60 days after December 31.<sup>4</sup> During the year these young workers may have

needed to draw on their RRSP savings to meet immediate financial obligations. However, they could have made a contribution before the end of the following February for a number of reasons: their financial situation may have improved by year end; they may have taken advantage of arrangements offered by financial institutions;<sup>5</sup> or they may have decided to contribute to their RRSPs to reduce their tax liability.

## Conclusion

More young people than ever before are investing in RRSPs. While middle and high income earners have always used the tax deferral opportunity, much of the recent increase in contribution activity has come from those with lower earnings. This development has caused the average amount of contribution to drop.

Younger workers contribute regularly to RRSPs in order to achieve greater financial independence for future retirement, which should result in less reliance on government transfers. There are indications that their growing RRSP participation will likely persist, particularly because of their concern over future availability of government pensions (Cohen, 1996).

## Acknowledgements

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## Notes

1 The ages in each cohort were evenly distributed, that is, each one represented about 20% of the total in each cohort.

2 During the recession of the early 1990s, fewer young people would have had the discretionary income to invest in RRSPs. For details on the 1990 decline in overall RRSP participation and the contrasting 1991 growth, see Frenken and Maser (1993).

3 Excluded are withdrawals under the Home Buyers' Plan, which are not reported on tax returns (Frenken, 1996).

4 Therefore, the withdrawals shown are those made from January 1 to December 31 of a given year, whereas contributions reported may have been made from January 1 of a given year to the end of February (or beginning of March) of the subsequent year. In fact, in the past up to 80% of annual contributions claimed on each year's tax returns were actually deposited in January and February of the next year.

5 Many institutions offer RRSP contribution loans to their clients, with a postponed repayment schedule effective only after a tax refund.

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