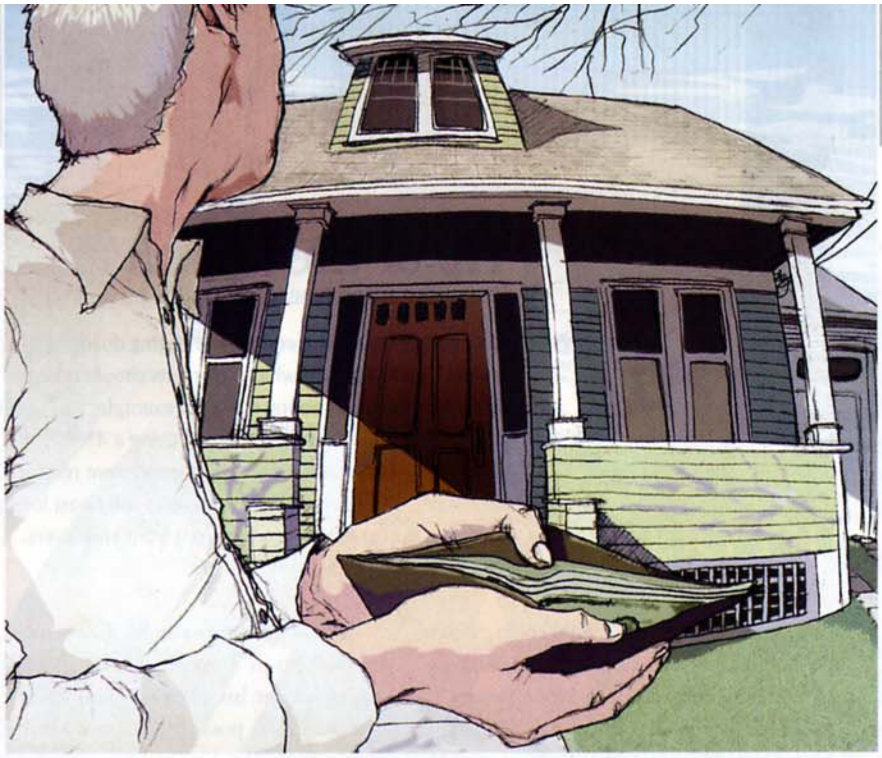

Pay it down or save it up?

Ezra Marshall gave up luxuries like travel and clothes when he became a homeowner. Now he's choosing between extra mortgage payments and his RRSP BY DAVID DIAS

It used to be that Ezra Marshall didn't have to think much about his investments. Until recently, the 46-year-old Toronto architect had kept things simple. He'd been renting an inexpensive apartment in the city's west end and making automatic contributions to his company's group RRSP program with each paycheque — all out of sight and out of mind.

The system worked for a long time, and Ezra accumulated more than $220,000 in his RRSP accounts. But when Toronto housing prices started to boom in the late 1990s, he was caught on the sidelines. While homeowners were building up thousands in equity, he was stuck living in a cramped space with all his investments in a single asset class. One day he looked around and decided he'd had enough. In May 2004, Ezra bought a real home — a 1940s bungalow in a west-end neighbourhood he describes as one of Toronto's last undiscovered gems. He's now within spitting distance of Lake Ontario, and can drive to his office or downtown within 15 minutes.

Home ownership, however, has come with its own complications. Ezra earns a healthy income of $85,000 in salary and bonuses. But the payments on his $266,000 mortgage are much higher than what he paid in rent — $1,500 a month, plus $400 for taxes, insurance and utilities. Increased costs have forced him to become frugal, and he's reluctantly sacrificed certain luxuries. "I don't go on my annual vacations anymore," he says. "I definitely don't buy clothes. I make do with what I have."

Ezra Marshall says he'd be crazy not pay into his employer's generous RRSP-matching scheme. "On the other hand, I wonder if I should focus on paying down my mortgage"

More important is the new choice Ezra faces: Should he pay down his mortgage quickly to get rid of his debt, or should he continue to focus on his RRSP so that he meets his modest retirement income goal of $25,000 a year? The RRSP option is certainly attractive. The group plan at Ezra's company comes with a generous matching program. For every dollar he invests (up to 10% of his salary), his employer adds 33¢. The incentive is so strong that Ezra has given up on his personal RRSP (worth $80,000) and now pays only into his company's plan (worth $146,000). "It's crazy not to participate fully," he says. "But I wonder if I should concentrate on just paying my mortgage."

As if that's not enough, there's also the matter of home renovation. Ezra would like to modernize his kitchen and finish his basement. That would cost $30,000. And while the

ILLUSTRATION BY MATHEW VINCENT

renos would boost the home's value, Ezra already has $8,400 in loans he took to cover closing costs from buying his house. He fears that taking on more debt will squeeze his cash situation even further.

Overall, Ezra has modest goals, but he needs to find a solid financial footing to achieve them. He'd like to know how much he should be saving for retirement and which of his vehicles he should be investing in — his mortgage, his company RRSP or perhaps even that home reno.

Tip of the Month

Prioritize investment and debt payments

Can't decide between investing and paying down debt? You can get a good sense of which payments should take precedence by simply comparing rates. For example, you should pay down a 7% line of credit before buying a 4% GIC. But keep in mind factors that may affect investment returns. Deferred taxes within an RRSP, for example, will boost long-term results, as will matching contributions from employers.

WHAT THE EXPERTS SAY

Ezra's predicament is what Andrew Rice calls "a classic case of weighing short-term goals against long-term ones." That being said, the planner at Stewart & Kett Financial Advisors in Toronto says Ezra's first choice — between his mortgage and RRSP — is easy to make. "Anytime you can save a dollar in your RRSP and get your boss to give you 33¢ more, you have to ask yourself why you *wouldn't* do it."

Rice says Ezra's return on extra mortgage payments simply doesn't compare to what he'd get from his company's RRSP program. Suppose Ezra set aside $1,000 of his pre-tax income for his mortgage, for instance. He'd first have to pay about $400 of that in taxes, leaving $600 to pay down debt that's only costing 4.4% in interest. Investing in his company's RRSP program, meanwhile, would defer taxes on the $1,000. His employer would also contribute $333 under the matching program. That would leave Ezra with $1,333 invested. "It's a no-brainer," Rice says.

Outside the mortgage question, though, the advice isn't so cut and dried. Ezra would like to free up spending cash, but he'd also like to invest in renovations. Rice, however, says these are mutually exclusive options, and Ezra will have to decide which is more important: "He already feels house rich and cash-flow poor. Taking on $30,000 in debt is just going to make him feel more that way."

Barbara Garbens at BL Garbens Associates, also in Toronto, is a bit more optimistic about his chances. She thinks the renovation is possible, but not until Ezra pays off the $8,400 he already owes and adjusts to a more frugal lifestyle. "It will take about five years for him to adjust, and to start seeing results from paying down his loans." Until then, he should fight the temptation to take on more debt. Otherwise, he may jeopardize his retirement.

Ezra has barely enough saved as it is, Garbens says, adding that he'll need to make extra payments if he wants to be done with his mortgage before he reaches retirement age. Still, Garbens is confident Ezra can pay off the mortgage in time. She can even see him retiring as early as age 63. By then his RRSPs and government benefits should provide $30,000 a year after taxes until age 90, the minimum she thinks he'll need to maintain his current living standard. Rice generally agrees, but says Ezra should choose his retirement age carefully. If he worked until age 65, Rice figures Ezra would be able to spend a more comfortable $36,000 a year.

Even then, the margin for error will be thin. But our advisers say that Ezra is on track for retirement and will remain so as long as he sticks to the blueprint he's drafted. And for an architect like Ezra, Rice says that shouldn't be too difficult: "Planning for retirement is much like designing a building — it always pays to measure twice and cut once." **B**

Financial Snapshot

INCOME	
Salary	74,000
Bonus	11,000
Total Income	**$85,000**
EXPENSES	
Income taxes, CPP/EI	20,800
RRSP contributions	15,000
Mortgage payments	17,500
Home insurance, taxes	3,400
Home improvements	4,000
Heating, hydro	2,000
Phone, cable, Internet	2,200
Life insurance	600
Car (gas, insurance)	3,500
Groceries	2,400
Lunch money, wine	2,100
Newspapers, magazines	300
Clothing	500
Fitness club	400
Gifts, charity	1,100
Loan payments	2,400
Miscellaneous	4,400
Savings	2,400
Total Expenses	**$85,000**
LIABILITIES	
Mortgage	254,000
Loans	8,400
Total Liabilities	**$262,400**
ASSETS	
Home	290,000
Car	15,000
Possessions	3,500
Company RRSP	146,400
Personal RRSP	80,400
Total Assets	**$535,300**
Net Worth	**$272,900**

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