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PORTFOLIO STRATEGY

Use the Canada Child Benefit to invest in your children's education

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It's hard finding money to invest in your child's postsecondary education, so let the federal government help.

Parents receiving the new Canada Child Benefit can use the monthly payments to invest in their children's registered education savings plans. Ottawa offers a matching 20-per-cent grant for RESP contributions of up to $2,500 per year. Already taking full advantage of this money? Then use the CCB to build additional savings for your child's postsecondary education and later life.

The Canada Child Benefit was launched in July and is sent monthly to families with children under the age of 18. It's a non-taxable payment based on the number and age of your kids and adjusted family net income, which means total income minus deductions for things like contributions to registered retirement savings plans, pensions and union dues. It's estimated that 90 per cent of families will receive more money from this program than its predecessors.

A federal government calculator shows that a family with income of $140,000 would get $129 per month for a child under the age of six, or $1,548 per year. That's more than halfway to the amount needed to claim the maximum $500 per year in Canada Education Savings Grant money, which is available to people making RESP contributions (additional grants are available to lower-income families).

A lot of people today are worried about how low interest rates and an erratic stock market will affect their investments. With RESPs, you get an automatic 20-per-cent return on the first $2,500 you contribute to a lifetime limit of $7,200 in grant money.

There's a lifetime $50,000 contribution limit for RESPs, so you're not limited to putting in $2,500 per child on an annual basis. But there's a case to be made for building up additional funds beyond that annual $2,500 outside an RESP using the Canada Child Benefit. RESPs are subject to many rules and restrictions, particularly when someone doesn't end up pursuing a postsecondary education. With a separate investment account built up over the years using the CCB, a young person would have access to funds with virtually no restrictions.

Let's be clear that using CCB money for your children's education is what we might call a luxury strategy. You should only use it if you don't need the CCB to cover household costs, and you don't have any big debts beyond the mortgage. But e-mails I've received from parents over the years show there's a high level of interest in teaching kids about investing.

After spending a week talking to university students on the East Coast about financial literacy earlier this month, I'm all for this as long as it's done in a way that promotes sensible long-term investing rather than stock trading. When young adults talk about investing, the conversation too often turns to picking hot stocks.

RESPs can be used as a teaching tool, but they require a high level of expertise and diligence. For example, you have to carefully manage RESPs through the years to tailor the risk level to the age of the student (more on this in an upcoming column). A separate investment account for your minor child might offer a simpler learning experience.

Toronto-Dominion Bank says that in a majority of provinces and territories, children must typically be 18 or the age of majority to have investment accounts in their own name at a bank or online brokerage (18 is also the minimum age for someone to have a TFSA). This means parents must open in-trust accounts, also called informal trusts, on a minor child's behalf. Opening an in-trust account typically requires that you familiarize yourself with the attribution rules that are meant to prevent people from shifting income to other individuals to reduce taxes.

Interest and dividends earned in an in-trust account are taxed in the hands of the parent who funded the account, while realized capital gains are taxed in the child's hands. One of the big benefits of using the CCB to invest for a child is that these attribution rules don't apply to parents.

"The Canada Child Benefit is specifically carved out of the attribution rules for minor children," said Jamie Golombek, managing director of tax and estate planning at CIBC Private Wealth Management. "If a parent sets that money aside for the child, then it becomes the child's money and the child's income will not be attributed back to the parent."

It's highly unlikely a child would actually have to pay any income tax based on dividend and interest income, but Mr. Golombek still suggests filing a tax return. The reason is that consistent tax filing demonstrates to the Canada Revenue Agency that someone is diligent about reporting all income.

Ideal investments for parents using CCB money have the following attributes:

- Low requirement for initial and subsequent investments: You'll likely be working with fairly small amounts on a month-by-month basis.
- No commissions for buying and selling: These costs can be particularly onerous when you're investing smaller amounts.
- Low fees: Minding your fees is a foundational investing lesson.

Exchange-traded funds are great for this purpose if you use a brokerage that charges no commissions to buy them. Questrade and Virtual Brokers waive commissions on ETF purchases, but charge a fee to sell. Qtrade and Scotia iTRADE have a limited list of commission-free ETFs. National Bank Direct Brokerage offers commission-free ETF trading on orders of 100 Canadian ETFs or more, but you'll almost certainly be buying in much smaller quantities if you're using CCB money.

ETFs are a great teaching tool, as well as an ideal portfolio building block. The classic index-tracking ETF gives you all the stocks in a target stock index, say, the S&P/TSX composite index. You can tell your kids they're investing in all the big companies of Canada if they own a Canadian index ETF. Add a U.S. and international equity ETF and you've covered off the major stock markets of the world. If you're a dividend enthusiast, there are plenty of dividend ETFs to choose from.

A simple alternative to ETFs is the e-series of index funds from Toronto-Dominion Bank, which require a minimum upfront and subsequent investment of just $100, or $25 for subsequent contributions made through a pre-authorized purchase plan. These funds are ideal for building a portfolio for a child using the CCB, and for RESPs as well. One other option is the Tangerine Equity Growth Portfolio, which has no minimum investment.

Tangerine actually offers four different balanced fund products, which mix stocks from Canada and globally with different weightings of bonds. The equity growth option was selected here because it has no bonds in it. If you're investing for a young child and figure on going for at least 10-plus years, you can afford to forgo bonds and focus on higher returning but more volatile stocks.

If you do one investing-related thing with your CCB money, make it an RESP contribution that gets you some federal grant money. "You'd be foolish to pass that up," CIBC's Mr. Golombek said.

What happens when you invest the Canada Child Benefit?

Here's an example of how much money you can generate by investing the Canada Child Benefit on behalf of your own child. We'll assume here that you have already made good use of registered education savings plans.

Family net income	**$140,000**
Child's current age	**2**
Monthly tax-free benefit under age 6	**$129**
Value after four years investing monthly and earning 4% annually	**$6,698**
From age 6 to 17, monthly benefit drops to	**$45**
Estimated final value when the CCB runs out, based on accumulated payments and investment gains	**$19,055**

NOTES

- A 4 per cent after-fee return is used to be conservative
- CCB payments are not indexed for inflation; the federal government has said indexing will start in 2020
- Investment income and capital gains are taxed in the child's hands, which means there would typically be no tax owing

JOHN SOPINSKI/THE GLOBE AND MAIL › SOURCE: GOVERNMENT OF CANADA CCB CALCULATOR; GETSMARTERABOUTMONEY.CA COMPOUND INTEREST CALCULATOR

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