TAX TALK

Will Canada Pension Plan changes affect your retirement plans?

New Canada Pension Plan (CPP) rules took effect on Jan. 1, kicking off a series of graduated changes over the next five years that may make you think twice about drawing your government pension before you turn 65.

Most people in Canada between the ages of 18 and 70 who earn more than $3,500 a year contribute to CPP (except in Quebec, where the Quebec Pension Plan provides benefits). Like an insurance plan, CPP is designed to provide a monthly retirement or disability benefit or, if you die, a survivor benefit to your spouse and children.

In retirement, the amount you receive depends on how much you've earned, how many contributions you've made, and your age when you stop working. The normal age for receiving a CPP retirement pension is 65. If you start your CPP retirement pension then, you'll get the full pension amount you're eligible to receive. For 2011, the maximum amount is $934.17 per month.

You can, however, start drawing a retirement pension as early as 60 (at a discount) or wait until as late as 70 (and get a premium). Among the recent changes to CPP, two of the biggest involve these discount and premium rates.

Taking CPP early

You can begin to draw your CPP retirement pension at age 60. Starting in 2012, however, your pension amount will decrease by a larger percentage for every month you take it before age 65.

Currently, your CPP retirement pension is reduced by 0.5% for each month before age 65 that you begin receiving it. This means that, if you started receiving your CPP pension at 60, your pension amount is 30% less than it would have been if you had waited to take it at 65.

From 2012 to 2016, the early pension reduction will gradually change from 0.5% to 0.6% per month. So by 2016, if you start receiving your CPP pension at the age of 60, your pension amount will be 36% less than it would have been if you had taken it at 65.

Retiring later

Starting this year, after age 65 your monthly CPP retirement pension amount will increase by a larger percentage for every month you delay taking CPP, from 0.5% per month (6% per year) to 0.7% per month (8.4% per year) by 2013. At that point, if you start receiving your CPP pension at the age of 70, your pension amount will be 42% more than it would have been if you had taken it at 65.

A cash flow hit?

If you're age 65 to 70 and work while drawing your CPP retirement pension, you can choose to make CPP contributions if you want to. If you decide to contribute, your employer will have to as well.

Starting in 2012, if you're under 65 and work while receiving your pension, you and your employer must make CPP contributions.

This will be a big cash flow hit for some. Many people choose to start their CPP at 60 even though they plan to continue working. This way they have an increased income from CPP but also less money going out as they no longer have to contribute.

Say you're in this magic bracket, 60 to 65 years old, collecting your CPP retirement pension, still working as an owner/operator, and making $40,000 with your truck. Starting in 2012, you'll have to pay $3,613.50 a year into CPP that you're not paying now. Ouch!

Welcome change

One new rule makes it easier for Canadians to – what's that phrase Ottawa is using? – "transition to retirement."

Starting in 2012, you can begin receiving your CPP retirement pension before age 65 without any work interruption.

Today, if you want to take your pension early, you have to either stop working or significantly reduce your earnings for at least two months.

CPP isn't intended to supplement your earnings from a regular job. It's a retirement pension. But these days, the rule just encourages people to skirt it.

The age when you start to take your CPP retirement pension depends on your savings, debt, job satisfaction, health, family, the lifestyle you lead, and other factors. Ask your accountant or financial advisor about the new CPP rules and how they'll affect you personally, especially if you're counting on tapping into your government pension before you turn 65.

Visit servicecanada.gc.ca to view or print a copy of your CPP statement. It will show the total amount of your CPP contributions by year and your pensionable earnings on which they are based. It will also estimate what your pension or benefit would be if you were eligible to receive it now. ☐

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