

## CPP Issues As You Approach Age Sixty

### **Introduction**

Your sixtieth birthday will mark an important milestone, as it brings some special treatments such as paying seniors' rates offered by businesses to those sixty and over. More importantly, the Canadian Pension Plan (CPP) allows you to start taking your government pension at this age, but with a penalty for taking it before 65. So you'll need to weigh the pros and cons of taking CPP early. Our previous article listed a number of factors that you should consider when making this decision.

This article focuses on the way your CPP benefits are calculated and whether you continue to work after age 60 as factors that affect the level of your benefits in taking CPP early or late. The CPP calculations may seem complicated, but if you need any help or clarification, please give us a call and we'll be glad to answer your questions.

### **More on CPP basics**

The amount of your CPP retirement benefits depends on:

1. how many years you contributed, and
2. how much you contributed between the ages of 18 to 65 (or whenever you start taking CPP).

The government uses a "general dropout" rule to drop 17% of the lowest earning years from this calculation and uses 83% of your highest earning years to determine your CPP benefits. Since there are 47 years between age 18 and 65, the calculation takes 39 (83%) of your highest earning years and drops 8 (17%) of your lowest earning years. Outside of Child Rearing Dropout years and disability years (when you received CPP disability benefits), all years, regardless of whether you worked or not, will be counted in calculating your benefits.

### **Implications**

The Year's Maximum Pensionable Earnings (YMPE) is the level of income at which you make the maximum contribution to CPP. In 1966 it was \$5,000 and it increased progressively to \$54,900 in 2016. In order to receive the maximum CPP retirement benefits, you must have earned at the (YMPE) level or more in 39 of your highest income years between age 18 and 65. The maximum CPP benefit payout was \$1092.50/month or \$13,110/year in 2016.

### **Taking CPP Early or Late**

The earliest you can start collecting CPP is the month following your 60<sup>th</sup> birthday, or you can delay it until a month following your 70<sup>th</sup> birthday as the latest. There is a penalty of 0.6% for each month before your 65<sup>th</sup> birthday, so that 36% will be deducted from your qualified benefits if you start at age 60. Alternatively, you will be rewarded by 0.7% per month for delaying your benefits after age 65, meaning you will receive an extra 42% to your benefits if you wait until age 70.

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## What To Watch For

A key factor in determining to take CPP early or late is your **longevity**, because you need to live long enough to make up for the income you forego by delaying. However, other factors such as your

- 1) level of income
- 2) your CPP contribution history, and
- 3) whether you have dropout provisions, are also important.

### **1) Level of Income**

Delaying CPP will increase the payments, but if you already have a certain level of income, you could be pushed into the next tax bracket and pay a higher marginal tax rate. Additionally, you could start losing your age credit if your income exceeds \$35,927 (2016) and trigger the Old Age Security (OAS) clawback if your income exceeds \$73,756 (2016).

### **2) Your Contribution History**

If you stop work before age 65, delaying CPP will add years of no income in your benefits calculation. Although you are penalized for starting CPP before age 65, if you're not working, the net result of adding zero income years to your benefits calculation may decrease the amount of benefits you qualify for. The analogy here is a bigger slice of a smaller pie.

On the other hand, if you continue to work after accumulating 39 years of maximum YMPE contributions, you gain nothing for the extra years of contribution because you cannot receive more than the maximum retirement benefits. However, if you start CPP and also keep working and contributing, you add Post-Retirement Benefits (PRBs) which will increase your overall CPP payments.

### **Post-Retirement Benefit (PRB)**

Your contributions to CPP after you have started collecting will earn additional benefits call Post-Retirement Benefits (PRBs). Roughly speaking, each year of maximum YMPE earnings will add approximately \$27 dollars to your monthly benefits. Like the regular retirement benefit itself, PRBs are fully indexed and you receive them for the rest of your life.

You do not need to apply for PRBs, the government will automatically calculate them if you are contributing to CPP. PRBs earned in one year are added to the benefits paid out in the following year. Contributions to CPP are not mandatory after age 65, but can be continued until you reach 70.

### **3) Dropout Provisions**

Dropout provisions allow you to omit a period of low or no income from your CPP contribution history that would normally decrease the benefits you qualify for. The most common dropout provisions are:

- the **Child Rearing Dropout (CRDO)**, which applies to one parent (the primary care giver) and allows them to drop the number of months from their contribution history during which the child or children were under the age of 7.

- the **disability dropout**, which applies to people who received or receives the CPP disability pension and allows them to drop those years in which they collected this disability pension.

If you are eligible for dropout provisions and are still working, it may be worthwhile to delay taking CPP as long as you are earning at the YMPE level or at a level higher than your lifetime average. This is because a dropout provision will reduce the number of contributory years in your benefits calculation, which will allow each year of higher earnings to have a bigger influence on the calculated benefits.

*(the following examples are taken from "Examples of CPP after age 60 but still working" written by Doug Runchey of [www.drpensions.ca](http://www.drpensions.ca))*

### **Example 1**

John just turned 60 and plans to continue working until age 65, at which point he plans to retire and start his CPP. He started work right out of high school and has earned at the maximum CPP contribution level for 39 years and he will continue to contribute to CPP until he retires at age 65.

In this case, John will receive the maximum benefit level from CPP at age 65 because he has contributed at the maximum level for 39 or more years. But his contributions from age 60 to age 65 would not have gained him any more benefits because you cannot receive more than the maximum benefit. His contributions from age 60 to 65 will have been "wasted".

What could he have done differently? He could have started his CPP early and his contributions after starting CPP would then earn Post Retirement Benefits (PRBs) that would have added annually to his benefits level. Although he is penalized for taking CPP early, collecting benefits earlier and the PRBs he earns will help compensate for that.

### **Example 2**

Peter is also age 60. He came to Canada at age 40 as an engineer and had a good salary every year since his arrival in Canada. Peter's Statement of Contributions (SOC) estimates he could receive a CPP retirement pension of \$595.00/mo at age 65. If Peter continues to work and earn at the maximum contribution level, his CPP at age 65 would actually be approximately \$727.50, much more than the SOC estimate.

The reason is that the extra five years of maximum earnings increases his CPP by about \$132.50 because the SOC estimate assumes earnings from age 60 to 65 based on his average lifetime earnings to that point (approximately \$30,000 annually, compared to the yearly maximum of \$54,900 for 2016). If he didn't work at all after age 60, his actual CPP at age 65 would reduce from the amount shown on the SOC to about \$532.50.

### Example 3

Betty had her first child when she was age 18 and then two more children born about three and six years later. She didn't start working outside of the home until the youngest child turned age 14, when she was age 37.

For the first six years she worked only part-time and earned approximately half of the YMPE each year, but for the last 17 years she has been working full-time and earning above the YMPE.

Betty's SOC indicates that she could receive a retirement pension of \$595.00 at age 65 (the same as Peter's SOC above). But Betty's situation is very different from Peter's because she is eligible for the child-rearing dropout (CRDO) for approximately 13 years, from age 18 to age 31.

As a result of the CRDO, Betty's SOC estimate is virtually meaningless. Her actual CPP retirement pension at age 65 would be about \$708 if she doesn't work after age 60 and it could be as much as \$920 if she continues to work and earn at the YMPE level for those five years. That means that working those five years after age 60 could increase Betty's CPP by about \$212 a month.

### Conclusion

As you can see from the above examples, working after age 60 will affect your age 65 CPP retirement pension calculation depending on:

- Your individual lifetime record of pensionable earnings under the CPP
- Your level of earnings after age 60, relative to the YMPE
- Other "dropout provisions" that you might be eligible for under the CPP

Our recommendation is that you understand these impacts before you decide when to retire and when to start receiving your CPP retirement pension.