CPP –How Do The New Rules Affect You?

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Tax changes are a regular event in Canada. However, changes to the Canada Pension Plan haven't happened for many years: so when we have new proposals, it's important to pay attention. In May some proposed changes were announced, and these will affect the amount of benefits you receive.

First, effective January 2012, you no longer have to prove you've stopped working. The work cessation test currently requires anyone wishing to take their CPP benefit early (as early as age 60) to basically stop working for at least two months. The challenge has always been how to enforce this, as many people have collected CPP early while still working with simply a break in income. This new ruling could also be beneficial to those that want to go part-time, yet apply for CPP without having to stop work completely.

In keeping with this change however, one proposal is workers under 65 who opt to receive the CPP, will still have the CPP premium deducted from their paycheques. This would allow you to enhance your CPP benefits over time if you are not at the maximum. Currently, once you are receiving CPP benefits, your deductions for the CPP premium stop.

You can still collect as early as age 60 & as late as age 70. When applying for CPP earlier or later than the "standard age of 65", there has always been an adjustment of .5%/month. For example, if you apply to receive CPP at age 60, then you will receive 30% less than waiting until age 65 (.5% x 12 mos. x 5 yrs). If you delay, you will receive up to 30% more.

The recommended changes here mean that the adjustment for taking the pension early is .6%/month. Yet, for taking the pension late, you would see an increase of .7%/month. Therefore, if you apply at age 60, you would receive 36% less. If you applied at age 70, you would receive up to 42% more. In a nutshell, this provides a disincentive to apply to early, but certainly encourages people to apply later.

Another change is the number of low-income years you can exclude from your calculation. It is currently up to 15% to a max. of 7 years, but will be increasing on a gradual scale to 16% in 2012, and 17% in 2014. In this case, up to 8 yrs of low-income periods can be excluded from your calculation. This will benefit many people who've had periods of unemployment or low income earning years.

One final note: None of the proposed changes will affect anyone currently receiving CPP retirement benefits, or anyone who applies prior to the proposed changes taking effect.

Why the changes? Revenue Canada is stating they are trying to equate the actuarial benefits to those applying at different times to the actual costs and benefits to the Canada Pension Plan.

They are also trying to tie in more flexibility for the changing demands of retirees. As the mandatory retirement age of 65 is no longer in effect in most provinces, changes to the CPP options seem to be appropriate.

As a financial advisor, my biggest concern for my clients is ensuring they have maximum cashflow when you need it. For somebody, age 60, working and earning $75,000/an, applying for CPP early, will mean you're increasing your tax rate to almost 40%, yet also decreasing the amount you will receive once you truly retire. After-tax income is what really counts.

Often, people will calculate how much cash they will receive over the long run and this is the sole decision for applying early. If you spend the difference and pay 40% or more in taxes at age 60, rather than 20% that you might pay with income splitting and pension benefits, was it really worth taking the CPP early? There are many factors to consider in this equation and I encourage you to work through these for your personal situation.

To learn more about proposed changes to CPP, refer to the government website that outlines the proposal. http://www.fin.gc.ca/n08/data/09-051_1-eng.asp

There are also changes to both old and new Ontario Locked-in RIF's & LIF's, whereby a one-time lump sum withdrawal can be made from the account. If you hold one of these accounts, watch for this notice as it provides increased flexibility and is only offered for a short-time. Your financial institution is required to let you know about these options.

To learn more, go to the government website for more details http://www.fsco.gov.on.ca/english/pensions/li-account-regchanges2009.asp

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