Wealth Management

RBC Wealth Management Services

Proposed enhancements to Canada Pension Plan

What this means for employers, employees and retirees

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The proposed agreement, in brief

On June 20, 2016, Canada's Finance Ministers reached an agreement in principal on proposed enhancements to the Canada Pension Plan (CPP) that are intended to improve the retirement security of Canadians. Approval from the Federal government and at least seven out of ten provinces representing two-thirds of the population of the 10 provinces is required to bring the changes into effect. At present, all provinces, except Quebec, have reached an agreement in principle, which makes it likely that the proposals will move forward. Quebec, the only province with its own pension plan, has not yet agreed to the CPP expansion proposals but continues to be part of the discussions.

The information in this article is not intended to provide legal or tax advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax advisor before acting on any of the information in this article.

What are the changes?

- The proposed changes would increase the income replacement provided by CPP from one quarter to one third of pensionable earnings. This means that, at maturity, a Canadian with $50,000 in constant pensionable earnings throughout their working life would receive a yearly CPP benefit of approximately $16,000 ($50,000/3) instead of the $12,000 ($50,000/4) they would currently receive, or $4,000 more per year.
- The enhancements are expected to include a 14% increase in the amount of income subject to CPP. The maximum earnings subject to CPP is projected to be equal to approximately $82,700 in 2025 (in 2016 maximum earnings subject to CPP is $54,900).
- These changes will be implemented gradually over a 7-year period beginning January 1, 2019 with full implementation expected by 2025. The phase-in will be done in two steps: (1) in the first 5 years, contribution rate increases

will be phased-in beginning January 1, 2019; (2) after that, in the following 2 years increases to the upper earnings limit will be phased-in.

Additional proposed changes

Additional proposed changes to complement the CPP proposals and help to offset its impact include:

- Enhancements to the federal Working Income Tax Benefit (WITB) to mitigate the effect of the higher CPP contributions for low-income earners.
- Introduction of a tax deduction for employees for the enhanced portion of employee CPP contributions. A tax credit will continue to apply to existing employee CPP contributions.

Impact on employers, employees and self-employed individuals

The new agreement is expected to result in a gradual increase in the CPP contribution rate applied to "pensionable earnings" of 1 percentage point higher for employers and for employees (total increase of 2 percentage points higher) by 2023. Pensionable earnings is equal to an employee's earnings up to the yearly maximum pensionable earnings (YMPE) less the year's basic exemption amount which is $3,500.

- In 2016, employers' and employees' CPP contribution rate is 4.95%, each applied to pensionable earnings. This contribution rate is expected to gradually increase to 5.95% by 2023.
- Self-employed individuals currently making both employer and employee contributions at a contribution rate of 9.9% are expected to make contributions of 11.9%, by 2023, based on their pensionable net self-employment income (i.e. net self-employment income up to YMPE less the year's basic exemption amount of $3,500).

The long phase-in period is intended to make it easier for employees and employers to adjust to the new increased contribution amounts.

In step 2 of the phase-in period beginning in 2024, a separate contribution rate (expected to be 4% each for employers and employees) will be implemented for earnings above the YMPE at that time up to an upper earnings limit. The upper earnings limit will be equal to YMPE for every year up to 2023. However, it will be increased over a 2-year period starting in 2024 and is expected to reach $82,700 in 2025. The 4% contribution rate will be confirmed through an independent actuarial assessment by the Office of the Chief Actuary. Appendix I illustrates the phase-in for expected contribution rates and the upper earnings limit over the 7-year period up to 2025. Appendix II provides an example of the impact of the enhancements to CPP on an employee and employer where the employee is earning $100,000.

Impact on retirees – enhanced CPP Benefits

Each year of contributing to the enhanced CPP will allow employees to accumulate partial additional benefits. It is projected that full enhanced CPP benefits will be available after approximately 40 years of making enhanced CPP contributions. However, partial benefits will be available sooner and will be based on years of contributions and the amount of contributions. Individuals that are already receiving CPP benefits and those that will retire before implementation will not benefit from these changes.

Do the proposals affect the Quebec Pension Plan (QPP)?

The proposals do not affect the Quebec Pension Plan (QPP). Quebec is the only province that did not sign the agreement but has agreed to remain part of the discussions moving forward. The Quebec government indicated its intention to submit proposals to its citizens regarding enhancements to QPP.

Ontario Retirement Pension Plan (ORPP)

The Ontario provincial government has indicated that it does not intend to proceed with implementation of the Ontario Retirement Pension Plan (ORPP) if agreement on the proposed enhancements to CPP is reached and finalized. The ORPP would have provided a source of increased pension benefits to residents of Ontario who are employees and do not have "comparable" workplace pension plans. The phase-in of ORPP contributions were expected to start on January 1, 2018.

For more information on the CPP enhancement proposals, visit Department of Finance Canada website: http://www.fin.gc.ca/fin-eng.asp

Appendix 1 – Contribution rate phase-in

The table below illustrates the proposed changes to the contribution rates over the first 5-year period to 2023 and then the implementation of a new separate contribution rate for earnings over YMPE up to the upper earnings limit.

			Estimated Combined Employee/Employer Contribution Rate	
Year	Projected YMPE	Projected Upper Earnings Limit	Contribution Rate up to YMPE	Contribution Rate above YMPE up to Upper Earnings Limit
2018	$58,000	$58,000	9.9%	
2019	$59,700	$59,700	10.2%	
2020	$61,500	$61,500	10.5%	
2021	$63,500	$63,500	10.9%	
2022	$65,600	$65,600	11.4%	
2023	$67,800	$67,800	11.9%	
2024	$70,100	$74,900	11.9%	8%
2025	$72,500	$82,700	11.9%	8%

Source: The information used in this table was taken from or calculated using information provided on the Department of Finance Canada website – Background on Agreement in Principle on Canada Pension Plan Enhancement

Appendix II – Example of estimated CPP contributions over the phase-in period to full implementation

The table below shows an example of how an employee who earns $100,000 is affected by the proposed enhancements to CPP. We have assumed that earnings will remain constant over the 7-year phase-in period.

					Estimated Combined Employee/ Employer Contribution Rate		Estimated Combined Employee/Employer Contribution Amount	
Year	Earnings	Projected YMPE A	Year's Basic Exemption Amount B	Projected Upper Earnings Limit C	Contribution Rate up to YMPE D	Contribution Rate above YMPE up to Upper Earnings Limit E	Contribution up to YMPE (A-B) x D	Contribution above YMPE up to Upper Earnings Limit (C-A) x E
2018	$100,000	$58,000	$3,500	$58,000	9.9%		$5,396	
2019	$100,000	$59,700	$3,500	$59,700	10.2%		$5,732	
2020	$100,000	$61,500	$3,500	$61,500	10.5%		$6,090	
2021	$100,000	$63,500	$3,500	$63,500	10.9%		$6,540	
2022	$100,000	$65,600	$3,500	$65,600	11.4%		$7,079	
2023	$100,000	$67,800	$3,500	$67,800	11.9%		$7,652	
2024	$100,000	$70,100	$3,500	$74,900	11.9%	8%	$7,925	$384
2025	$100,000	$72,500	$3,500	$82,700	11.9%	8%	$8,211	$816

Appendix II continued on next page

Appendix II – Example of estimated CPP contributions over the phase-in period to full implementation

The table below continues with the same example above illustrating the increase in estimated combined employee/employer contributions compared to the current rules. This assumes that under the current rules, YMPE would be the projected YMPE from column A in the previous table but the combined employee/employer contribution rate would remain at 9.9%.

		Estimated Combined Employee/Employer Contributions		
Year	Earnings	Proposed Enhancements	Current Rules (based on projected YMPE)	Estimated Increase in Contributions
2018	$100,000	$5,396	$5,396	$0
2019	$100,000	$5,732	$5,564	$168
2020	$100,000	$6,090	$5,742	$348
2021	$100,000	$6,540	$5,940	$600
2022	$100,000	$7,079	$6,148	$931
2023	$100,000	$7,652	$6,366	$1,286
2024	$100,000	$8,309	$6,593	$1,716
2025	$100,000	$9,027	$6,831	$2,196

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