Wealth Management

the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES

Daniel Kelly
Tél. : 519-675-2528
daniel.kelly@rbc.com

Gary Gorham
Tél. : 519-661-2510
gary.gorham@rbc.com

Chris Alexander
Tél. : 519-675-2667
chris.alexander@rbc.com

Lauralee Bushan-Jazey, CIM, FCSI
Tél. : 519-661-2557
lauralee.bushan-jazey@rbc.com

Jessi da Silva-Couto
Tél. : 519-675-2664
jessi.dasilva-couto@rbc.com

N6A 5P3

Canada Pension Plan

Understanding the government income that may be available to you in retirement

After years of contributing to the Canada Pension Plan (CPP) you may wonder how this plan will help you in retirement. This article examines how the plan works, your choices and the implications of those choices. Although the CPP provides retirement and disability benefits, this article focuses only on the retirement benefits. Any reference to spouse in this article includes a common-law partner.

What is the CPP?

The CPP provides retirement benefits for individuals who've contributed to the CPP or to both the CPP and the Québec Pension Plan (QPP). The CPP also provides death and survivor benefits for the families of those who have contributed to the CPP or to both the CPP and QPP. Most individuals who work in Canada contribute to either the CPP or QPP. CPP applies to individuals who work in provinces and territories outside of Quebec.

Eligibility for CPP retirement pension

If you've worked in Canada, made at least one valid CPP contribution and are at least 60 years of age, you qualify for CPP retirement benefits. The standard age to begin receiving a CPP retirement pension is the month after your 65th birthday; however, you may receive a reduced CPP retirement pension as early as the month after your 60th birthday or an increased CPP retirement pension if it starts after your 65th birthday. There is more information about the impact of receiving your CPP retirement pension before or after you 65th birthday later in the article.

I've contributed to the CPP and the QPP. Do I get retirement benefits from both plans?

The CPP and the QPP have sharing agreements and offer similar benefits at retirement. The retirement benefit you receive takes into account all contributions made to both plans. Keep in mind that you don't have to apply to both plans; if you contributed to both the CPP and QPP, you should apply to receive QPP if you live in Quebec when you apply and to CPP if you live anywhere else in Canada. If you live outside of Canada, apply for CPP or QPP according to the last province or territory where you lived.

Applying for CPP

CPP retirement benefits don't start automatically. You must apply in order to start receiving CPP retirement benefits. You can apply up to 12 months before the date you would like your pension to start.

If you apply for CPP after your 65th birthday, you can request retroactive payments for up to 12 months (11 months, plus the month you apply), or back to the month after your 65th birthday, whichever period is shorter. To be eligible for retroactive payments, you must be at least 65 plus one month when you make the request. There are no retroactive payments available for a CPP pension started before age 65. Retroactive payments can only be made for 12 months and as a result, if you apply after the month you turn 71, you will lose some benefits because you will only receive benefits for the previous 12 months. Therefore, the latest you should apply to obtain your full pension entitlement is the month you turn 71.

CPP enhancement

Up until 2019, the CPP retirement pension replaced one-quarter of your average work earnings. As of 2019, CPP is gradually being enhanced and will eventually grow to replace one-third of the average employment earnings you earn after 2019. As part of the enhancement, CPP contributions will gradually be increased over a seven-year period beginning in 2019. In exchange for increased CPP contributions, you'll receive higher CPP retirement benefits. Note that the CPP enhancement will only affect you if, as of 2019, you work and make contributions to CPP. If you are already receiving a CPP retirement pension and are no longer contributing to CPP, you will not be impacted by these changes.

Prior to January 1, 2019, if you were an employee, you and your employer were each required to contribute 4.95% of your earnings above $3,500 up to the Year's Maximum Pensionable Earnings (YMPE) to CPP. If you were self-employed, you contributed 9.9% of your earnings above $3,500 up to the YMPE to CPP.

As of January 1, 2019, increases to CPP contributions are gradually being phased in using two steps:

1. From 2019 to 2023, the contribution rate for employees will gradually increase by one percentage point (from 4.95% to 5.95%) on earnings between $3,500 and the YMPE.

2. Beginning in 2024, a second earnings limit, known as the Year's Additional Maximum Pensionable Earnings (YAMPE), will be introduced. A separate additional contribution rate of 4% for both an employee and employer and 8% for self-employed persons will apply to earnings above the YMPE up to the YAMPE. The YAMPE will be phased in over two years. It will be 7% higher than the YMPE in 2024, and 14% higher than the YMPE by 2025. It is important to note that this additional contribution rate will only have an impact on you in years when your employment or self-employment income exceeds the YMPE.

Your monthly CPP retirement pension is based on how much you have contributed, how long you have been making contributions at the time you want your pension to start and your age when you start receiving your retirement benefit.

How much could I receive at age 65?

Your monthly CPP retirement pension is based on how much you have contributed, how long you have been making contributions at the time you want your pension to start and your age when you start receiving your retirement benefit.

You can get an estimate of your CPP retirement benefit from your CPP Statement of Contributions. The statement provides a record of your pensionable earnings and your contributions to the plan. It also provides an estimate of what your CPP pension benefit would be if you were eligible to receive it today. You can obtain your Statement of Contributions online by registering for the My Service Canada Account online service or by mail with Service Canada.

In general, to be entitled to the maximum monthly CPP payment amount at age 65, you must have contributed to CPP for at least 39 years and have made the maximum contribution towards CPP in each of those years. Until December 31, 2023, you will only have made the maximum CPP contribution for a particular year if your employment or self-employment income was equal to or greater than the YMPE for that year. Beginning in 2024, you will only have made the maximum CPP contribution for a particular year if your employment or self-employment income is equal to or greater than the YAMPE for that year.

Maximum monthly CPP payment amounts are indexed (annually) and posted on the Government of Canada website.

How do periods of zero or low earnings affect CPP?

Your contributory period is used to calculate the amount of CPP retirement benefits that you may become eligible to receive. Your contributory period for the base CPP begins

when you reach age 18 (or January 1, 1966, whichever is later). Your two contributory periods for the enhanced CPP also begin when you reach age 18 or January 1 of the appropriate year (2019 for the first part of enhancement and 2024 for the second part of enhancement), whichever is later. Your contributory period ends when you start receiving a CPP retirement pension, turn 70 or pass away (whichever happens earliest).

The CPP includes provisions which help compensate for periods where you may have had low or no earnings during your contributory period. For example, to accommodate periods of low or zero earnings, a "general drop- out provision" automatically excludes a number of months, when your earnings were lowest, from the CPP retirement pension calculation. Low or zero earnings periods can occur if you are at school, unemployed or if you leave the workforce to care for a family member. This provision affects 17% of your base CPP contributory period, allowing up to 8 years of your lowest earnings to be dropped from the calculation.

CPP also has drop-out provisions (or drop-in provisions (i.e. credited earnings)) for months you may have been disabled or for months you were at home caring for your children under the age of 7 during your contributory period.

Taking CPP before age 65

If you start CPP before age 65, your CPP is permanently reduced by 0.6% for each month you receive it before age 65, including the month you turn 65 (a reduction of 7.2% per year). If you start receiving CPP the month after your 60th birthday, for example, you will receive 36% less than if you start your pension at age 65.

Taking CPP after age 65

If you start receiving a CPP retirement pension after age 65, your CPP will permanently increase by 0.7% for each month you delay receiving it, starting the month after your 65th birthday. This means if you begin receiving CPP in the month after your 70th birthday, your monthly CPP retirement benefit will be 42% higher than it would have been if you'd begun CPP at age 65. Note that 42% is the maximum possible increase, so there's no benefit to delaying receipt of CPP retirement benefit after age 70.

When should I take my CPP retirement pension?

Determining when you should begin taking CPP involves many considerations and should include a complete analysis of your financial needs and resources. Consider the following factors in deciding when to start receiving CPP retirement benefits.

Taking CPP early

- If you need the money to support yourself and/or your family.

> If you start CPP before age 65, your CPP is permanently reduced by 0.6% for each month you receive it before age 65, including the month you turn 65 (a reduction of 7.2% per year). If you start receiving CPP the month after your 60th birthday, for example, you will receive 36% less than if you start your pension at age 65.

- If you choose to receive your CPP retirement pension early, this may enable you to reduce your working hours, while maintaining your current income level until you decide to completely retire. It can be a great way to ease into retirement.
- Consider your current health and family health history. If you have a shortened life expectancy or greater potential for health issues based on family history, it may make sense to take CPP early.
- If you do not need these monies to support your lifestyle and could invest your CPP payments taken early, consider the expected rate of return on these funds, and compare this with the guaranteed, inflation- indexed higher CPP payments you would receive if you waited to take CPP until age 65 or later.

Delaying CPP

- You may decide to delay receiving your pension if you have insufficient income or resources for a comfortable retirement. The longer you wait, the higher your benefit payments will be. CPP benefits are indexed and guaranteed for your lifetime. You may also decide to continue working and contributing to CPP.
- If you plan to continue working, have sufficient income for your desired lifestyle and are in a higher tax bracket, it may also make sense to delay taking your CPP retirement pension. If you take CPP now, you will keep less of your CPP income because you'll pay more of it in tax. By delaying CPP, your payment will be higher when you do start to receive it and you may be in a lower marginal tax bracket by then.

There are tools available on Service Canada's website that can help you determine the best time to start your CPP retirement pension and get an estimate of how much you might receive.

Working while receiving CPP

You don't have to stop working to start receiving CPP. However, if you're under age 65, receiving CPP and still working, you and your employer must both contribute to

CPP when your annual earnings are over $3,500. If you're self-employed, you have to pay both the employee and employer portion. If you're age 65 to 70, still working and receiving CPP, you can elect not to contribute to CPP.

If you contribute to CPP while receiving a CPP retirement pension, the contributions you make go towards a lifetime benefit, which will increase your retirement income. This additional benefit is called the Post-Retirement Benefit (PRB). Similar to the CPP retirement pension, the amount of each PRB will depend on how much you earn, the amount of CPP contributions you made during the previous year and your age as of the start date of the PRB. The maximum PRB you can receive in one year equals 1/40th of the maximum CPP retirement pension. If you contribute less than the maximum, your PRB will be proportionate to your contributions. For example, by contributing half the maximum contribution level, you'll receive 50% of the maximum PRB.

You will be paid the PRB automatically the year after your contributions have been made, effective January 1 every year. The first PRB payment of the year is usually made in April and will include a lump-sum payment calculated back to January. The PRB for the rest of the year is then paid monthly, with your CPP retirement pension, as a single payment. For each year in which you generate a new PRB, the new PRB is added to any PRB you earned previously, up to a maximum PRB of 1/40th of the maximum CPP retirement pension.

If you're age 65 or over and receiving your CPP retirement pension, you may want to consult with a qualified tax advisor as to whether you should continue contributing to CPP. You will want to consider the cost of contributing, which takes into account your earnings and whether you are an employee or self-employed, as well as the annual amount of the PRB that you'll receive.

You will receive the PRB or the retirement pension supplement, even if you're already receiving the maximum CPP retirement pension.

Non-residents and CPP

You can receive your CPP retirement benefits even if you decide to leave Canada. If you receive CPP while living outside of Canada, non- resident withholding tax of 25% will be withheld from your CPP pension payments, unless this rate is reduced by a tax treaty between Canada and the country where you are resident.

If you're a U.S. resident receiving CPP, the Canada-U.S. Tax Treaty reduces the non-resident withholding tax to nil. Note that the maximum percentage of your CPP pension that may be subject to tax in the U.S. is 85%.

You can receive your CPP retirement benefits even if you decide to leave Canada. If you receive CPP while living outside of Canada, non- resident withholding tax of 25% will be withheld from your CPP pension payments, unless this rate is reduced by a tax treaty between Canada and the country where you are resident.

Cancelling CPP

You can cancel your CPP pension up to six months after you begin receiving it. You must request the cancellation in writing and repay all of the CPP benefits you received.

Sharing CPP retirement pensions

CPP retirement benefits are taxable to the recipient in the year received and are not eligible for the pension income tax credit. You cannot split your CPP pension with your lower-income spouse under the pension income splitting rules in the Income Tax Act. CPP rules do, however, allow "pension sharing." This is different to pension income splitting but it can result in tax savings if one spouse is receiving a higher CPP retirement pension than the other spouse and is also in a higher tax bracket than the other spouse.

If you want to share your CPP retirement pension, you must apply to do so. Pension sharing involves an actual transfer of payments from one spouse to the other, but the overall benefits paid don't change. Note that retirement pension sharing is based on the period that you and your spouse lived together while accumulating retirement benefits.

For more detailed information on this strategy, please ask your RBC advisor for the article on CPP retirement pension sharing.

Splitting CPP credits/earnings after separation or divorce

If you separate or divorce, you can divide the CPP contributions you and your spouse made during the time you lived together. You can divide CPP contributions even if only one spouse contributed to CPP. This is called "CPP credit splitting."

Eligibility for CPP credit splitting varies depending on when you divorced or separated and whether you were married or living in a common-law relationship. You or your former spouse can request a CPP credit split by completing an application form and providing other required documentation. Note that a marriage contract

or cohabitation agreement generally does not prevent a credit split, unless you entered the agreement before June 4, 1986, or you live in a province which allows couples to agree not to split CPP pension credits.

CPP survivor benefits

The CPP provides three types of survivor benefits on your death. The following is a very brief description of the three types of benefits.

CPP death benefit

If you contributed to CPP for at least one-third of the calendar years in your contributory period (and this must be a minimum of 3 calendar years), or 10 calendar years, your estate is entitled to a CPP death benefit. As of January 1, 2019, the amount of the CPP death benefit for all eligible contributors is a flat rate of $2,500. With respect to the CPP death benefit, if an estate exists, your executor can apply for the death benefit, and should do so within 60 days of death. If no estate exists, or your executor does not apply for the death benefit, the death benefit may be paid to other persons who apply for the benefit in the following order of priority: the person or institution that has paid or is responsible for paying for your funeral expenses, your surviving spouse, or your next-of-kin.

CPP survivor's pension

The CPP survivor's pension is a retirement pension paid to your surviving spouse on death. The amount of the CPP survivor's pension paid to your spouse will depend on whether you are under or over age 65 at the time of death and how much and for how long you contributed to CPP. It will also depend on your surviving spouse's age at the time of your death. The CPP enhancement will further increase the amount of the survivor's pension depending on how much and for how long you (the deceased contributor) paid into the enhancement.

If your spouse already receives a CPP retirement pension, the survivor's pension will be combined with it into a single monthly payment. There is a maximum amount (that is more than the maximum survivor's pension) that can be paid to a person where they are eligible for both a CPP retirement pension and a survivor's pension. The manner in which this maximum amount is determined will, in part, depend on the age at which the surviving spouse starts their own CPP retirement pension. The combined benefit is not necessarily the sum of the two separate benefits. Note that the enhancement portion of your spouse's survivor's pension will be added to the combined benefit and is not subject to this maximum.

The CPP survivor's pension is a retirement pension paid to your surviving spouse on death. The amount of the CPP survivor's pension paid to your spouse will depend on whether you are under or over age 65 at the time of death and how much and for how long you contributed to CPP.

The earliest a CPP survivor's pension can start is the month after the contributor's death, once the application to receive a survivor's pension has been processed.

CPP children's benefit

The CPP children's benefit is a monthly payment to dependent children of a deceased CPP contributor where the CPP contributory requirements for a CPP death benefit have been met. The monthly children's benefit is a flat rate for each child, adjusted annually for inflation. To qualify, the child must be under age 18 or between ages 18 and 25 and in full-time attendance at a recognized school or university.

This article may contain several strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance 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, legal and/or insurance advisor before acting on any of the information in this article.

This document has been prepared for use by the RBC Wealth Management member companies, RBC Dominion Securities Inc. (RBC DS)*, RBC Phillips, Hager & North Investment Counsel Inc. (RBC PH&N IC), RBC Global Asset Management Inc. (RBC GAM), Royal Trust Corporation of Canada and The Royal Trust Company (collectively, the "Companies") and their affiliates, RBC Direct Investing Inc. (RBC DI) *, RBC Wealth Management Financial Services Inc. (RBC WMFS) and Royal Mutual Funds Inc. (RMFI). *Member-Canadian Investor Protection Fund. Each of the Companies, their affiliates and the Royal Bank of Canada are separate corporate entities which are affiliated. "RBC advisor" refers to Private Bankers who are employees of Royal Bank of Canada and mutual fund representatives of RMFI, Investment Counsellors who are employees of RBC PH&N IC, Senior Trust Advisors and Trust Officers who are employees of The Royal Trust Company or Royal Trust Corporation of Canada, or Investment Advisors who are employees of RBC DS. In Quebec, financial planning services are provided by RMFI or RBC WMFS and each is licensed as a financial services firm in that province. In the rest of Canada, financial planning services are available through RMFI, Royal Trust Corporation of Canada, The Royal Trust Company, or RBC DS. Estate and trust services are provided by Royal Trust Corporation of Canada and The Royal Trust Company. If specific products or services are not offered by one of the Companies or RMFI, clients may request a referral to another RBC partner. Insurance products are offered through RBC Wealth Management Financial Services Inc., a subsidiary of RBC Dominion Securities Inc. When providing life insurance products in all provinces except Quebec, Investment Advisors are acting as Insurance Representatives of RBC Wealth Management Financial Services Inc. In Quebec, Investment Advisors are acting as Financial Security Advisors of RBC Wealth Management Financial Services Inc. RBC Wealth Management Financial Services Inc. is licensed as a financial services firm in the province of Quebec. The strategies, advice and technical content in this publication are provided for the general guidance and benefit of our clients, based on information believed to be accurate and complete, but we cannot guarantee its accuracy or completeness. This publication is not intended as nor does it constitute tax or legal advice. Readers should consult a qualified legal, tax or other professional advisor when planning to implement a strategy. This will ensure that their individual circumstances have been considered properly and that action is taken on the latest available information. Interest rates, market conditions, tax rules, and other investment factors are subject to change. This information is not investment advice and should only be used in conjunction with a discussion with your RBC advisor. None of the Companies, RMFI, RBC WMFS, RBC DI, Royal Bank of Canada or any of its affiliates or any other person accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or the information contained herein. ®/™ Registered trademarks of Royal Bank of Canada. Used under licence. © 2020 Royal Bank of Canada. All rights reserved. NAV0246 (10/19)