TAX & ESTATE PLANNING

When to start collecting Canada Pension Plan (CPP) and Old Age Security (OAS) benefits

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When it comes to deciding the right time to commence one's Canada Pension Plan (CPP) and Old Age Security (OAS) benefits, there are numerous factors to consider. Factors such as the individual's level of income, life expectancy, and overall situation can make this decision seem like a daunting task. Below, we discuss some key factors to think about when deciding whether to take CPP or OAS earlier or delay it during one’s retirement years.

Overview of the CPP

To qualify for the CPP retirement pension, an individual must have worked in Canada and made at least one valid contribution to the CPP. The amount of CPP retirement benefits an individual is entitled to receive is based on how much and how long they have contributed to the plan.

Importantly, CPP retirement benefits are not subject to income tests. Although the standard age to start receiving CPP retirement benefits is 65, the amount the individual is entitled to receive under the CPP is adjusted (reduced or increased) if the individual applies to receive their CPP retirement benefit before or after age 65. The earliest age to commence CPP pension payments is 60. If the payments commence before age 65, the CPP pension would be reduced by 0.6% for each month before age 65 (for up to 60 months).

For example, if an individual starts receiving CPP payments at age 60, their CPP pension would be permanently reduced by 36%. If the individual delays the payments, the pension amount is increased by 0.7% per month after age 65 (for up to 60 months). For instance, if the individual delays receiving CPP pension until age 70, their payment is permanently increased by 42% for the rest of their life. There is no benefit to delaying payments beyond age 70. A 2020 research paper published by FP Canada™ Research Foundation examines the merits of delaying CPP/QPP benefits for, "those Canadians in reasonable health who can afford to wait."[1]

Regardless of when an individual chooses to start receiving their CPP payments, the payments are indexed to inflation and recalculated annually to reflect increases in the Consumer Price Index (CPI). Having said this, because CPP benefits are dependent on the amount of credits one has accumulated over their working life, CPP payments are not affected by registered retirement savings plan (RRSP) and registered retirement income fund (RRIF) withdrawals.

When should an individual start receiving their CPP payments?

The decision to start taking CPP early or to delay is not a one-size-fits-all solution. Several factors should be considered when making this decision. While not an exhaustive list, here are some reasons why an individual might consider opting to start receiving their CPP benefits before or after age 65.

Reasons why an individual might consider starting CPP retirement benefits before 65

1. Reduced life expectancy: One of the most common reasons to take CPP early is due to a shortened life expectancy. By the time an individual reaches 60, they may have a better understanding of how long their money and savings need to last due to their health. If an individual has any reason to believe they may experience a shortened life expectancy, then taking the CPP at age 60 can make good financial sense to maximize the benefits received during their lifetime. If they qualify, individuals can consider applying for a CPP disability benefit instead, as the CPP disability amount will always be higher than a CPP retirement pension and will convert to a full retirement pension at age 65.

2. Needs funds to cover expenses or outstanding debts during early retirement years: Another reason an individual might consider taking CPP earlier than age 65 is if they require funds to cover their immediate expenses, debts, or if their health forces them to retire early.

While taking CPP early results in a permanent reduction of CPP retirement benefits up to a maximum of 36%, the individual may not have enough personal savings to sustain themselves in their 60s. Taking CPP benefits early can provide peace of mind and may make a difference in the individual's ability to financially sustain their retirement years.

Consider the following: An individual receiving the maximum CPP retirement benefit can receive up to $1,306.57 per month in 2023, which is equal to $15,678.84 per year indexed for inflation. If they choose to take their CPP at age 60, the amount will be reduced to $10,034.46 per year. However, having these funds available to cover lifestyle expenses and repay outstanding debts (particularly those with high interest rate) may prove beneficial to their overall retirement planning. Therefore, an individual should weigh the benefits of early payments against the permanent reduction in their CPP payments based on their personal financial situation.

3. Entitlement to defined benefit (DB) pension plan benefits: Longevity risk is the risk that an individual may outlive their investments, savings, pensions, and other sources of retirement income. Retirees with a DB pension plan may consider an early start to their CPP benefits. This is because DB pension plans already offer protection against longevity risk, which means that the need for higher CPP payments later (as a hedge against longevity risk) may be reduced for such individuals. Opting for earlier CPP payments allows the individual to begin enjoying their CPP benefits earlier, despite the reduced payment amounts.

4. Financial situation impacted due to market fluctuations: Retirement planning can be tricky, and changes in an individual's financial situation due to market fluctuations can make it even more challenging, which can directly affect carefully crafted retirement plans. This risk is sometimes referred to negative sequence of return risk, particularly at the start of one's planned retirement age.

For example, an individual may have initially planned to start taking their CPP at age 65 and use their RRSP/RRIF or non-registered account to support their income from age 60 to 65. However, market fluctuations can reduce the value of investments, making it unwise to make withdrawals from them as planned if it means less funds overall will be available when needed in retirement. In such situations, starting to withdraw from CPP earlier than age 65 can help supplement income while waiting for markets to recover. It is always recommended to work with a financial advisor to help structure an appropriate investment portfolio to help mitigate this risk as one approaches retirement.

Reasons why an individual should consider commencing CPP retirement benefits after 65

1. Higher payments: As noted above, the maximum monthly CPP retirement pension payment for 2023 at age 65 is $1,306.57 ($15,678.84 per year). However, delaying an individual's CPP payment until age 70 could increase the maximum benefit amount to $22,263.95 per year (or $1,855.33 per month).

This substantial increase compared to the standard CPP benefits can be considered by individuals with relatively good life expectancy and sufficient funds to “bridge” themselves to age 70, and who are concerned about longevity risk. Also note that for each year an individual delays the start of their CPP benefits, they will also receive the periodic indexation increase on a larger dollar amount, further increasing future payments — particularly in high inflation years. As pointed out in the FP Canada research paper, many Canadians in reasonable health would benefit, financially speaking, by delaying receipt of their CPP payments.[1]

2. Effective income withdrawal planning opportunities: Retirees who choose to delay starting to receive their CPP benefits until after age 65 can implement strategies to efficiently withdraw their investments and savings to fund their retirement years.

For example, an individual can choose to withdraw from their RRSP or other investments to fund their early retirement years from age 60 until the time they opt to take their CPP retirement pension. Once they start receiving their CPP retirement benefits, they can reduce RRSP withdrawals. This strategy may be more beneficial if the individual has a larger RRSP balance for retirement purposes. It also reduces the amount of funds that must be rolled over into a RRIF, which must pay out a minimum amount annually calculated based on the account value and the annuitant’s age. From an income tax perspective, this may smooth out the individual’s taxable income over the retirement years.

Before implementing any retirement strategies, it is crucial to consider all other financial aspects, including income level, expenses, and retirement goals. Individuals who require assistance should consult with a financial advisor to evaluate their situation.

3. Protection against longevity risk: Delaying CPP retirement benefits until after age 65 may be one of the ways to mitigate longevity risk because of the permanent increase in the amount of CPP retirement benefits for the rest of one's life. This will lower the possibility of running out of funds during retirement.

4. Become/remain eligible for the Guaranteed Income Supplement (GIS): The GIS is a non-taxable, income-tested monthly pension supplement for OAS pensioners who are resident in Canada and aged 65 or older with little or no other income. The adjustment to the amount of GIS income received is generally calculated on certain income reported on the individual's income tax and benefit return for the previous year. Examples of income sources included in the calculation are the following: CPP or QPP benefits, other pension income (i.e., superannuation, RRIF, or foreign pensions), investment income, taxable Canadian dividends, capital gains, net rental income, and net employment income (to name a few).

Certain deductions may also be allowed, such as RRSP deductions, registered pension plan (RPP) deductions, pension income splitting, moving expenses, and childcare expenses. A full list of the income and deductions included for the purposes of the GIS income test is referenced in Service Canada form ISP-3026, *Statement of Income for the Guaranteed Income Supplement, the Allowance or Allowance for the Survivor for payment period of July (20XX) to June (20XX) with Information Sheet*.

In order to qualify for the GIS, an individual's income for the purposes of the GIS income test must be below the maximum annual income threshold, which is based on the individual's marital status. The GIS benefit is generally reduced from the maximum payable at a rate of approximately one dollar for every two dollars of income, up to the maximum annual threshold, at which point the GIS payments would be zero.

Retirees who have low income may benefit from CPP deferral because it may help them qualify for the GIS between ages 65 to 70. As CPP retirement benefits are included as part of the individual's income for the purposes of the GIS income test, deferring their CPP can keep their income low and thus increase their GIS entitlement from age 65 to 70.

It should be noted that deferring CPP payments until age 70 will result in a permanent increase to the CPP retirement benefits an individual receives for the remainder of their life, which could directly affect the amount of GIS payments receivable after the individual reaches 70 years old (i.e., taking an increased CPP amount may reduce or eliminate the GIS the individual would have otherwise received).

Despite this, the long-term benefit of a possible 42% permanent CPP increase may offset the loss of GIS. Furthermore, delaying CPP may also allow for increased investment growth from the individual's RRSP or non-registered accounts, which could provide additional retirement income beyond age of 70.

Ultimately, an individual should take a holistic view of their retirement funding. Delaying CPP benefits for one single reason (e.g., to increase GIS benefits) should not be viewed in isolation without considering the whole picture.

5. Working past the age of 65: If an individual chooses to work past the age of 65, it is mandatory for them to make contributions to their CPP unless they are already receiving CPP benefits at that time. Nevertheless, it could be beneficial for an individual to defer their CPP past the age of 65, particularly if they intend to work beyond that age, because further contributions could potentially increase their CPP benefits (in addition to the 0.7% monthly increase in CPP retirement benefits through deferral) when they eventually take their CPP retirement benefits. The fact that they're still earning income after age 65 also means financially they may not need CPP benefits right away. However, it is important to exercise caution, as making further contributions to CPP may not be beneficial if the individual has already maximized their contributions to the plan.

For individuals who are uncertain about whether contributing to their CPP past the age of 65 will result in additional CPP retirement benefits, they should review their CPP Statement of Contributions. This statement can be accessed by contacting Service Canada or viewing it through their My Service Canada Account. Furthermore, should an individual require further guidance or advice, it is recommended that they seek the assistance of a financial advisor.

Overview of the OAS

The OAS is a taxable government benefit for seniors aged 65 and is based on years of residence in Canada after age 18. From April to June 2023, the maximum monthly amount of OAS that an individual can receive is $691 for those aged 65 to 74, and $760.10 for individuals aged 75 and over.

A fixed OAS benefit amount is received and is subject to a "clawback" when the individual's annual income exceeds a minimum income recovery threshold of $86,912 in 2023. The OAS benefit amount is completely clawed back when the individual's income exceeds the maximum income recovery threshold (approximately $142,124 in 2023 for individuals aged 65 to 74 and approximately $147,645 for individuals aged 75 and over).

The clawback begins to occur when an individual's net income before adjustments (as shown on line 23400 of their income tax return) exceeds the minimum income recovery threshold. Where an individual's net income before adjustments is equal to or greater than the maximum income recovery threshold, the full OAS pension will be subject to clawback.

Generally, the following types of income (not an exhaustive list) are typically included in the net income test for the purpose of calculating an individual's OAS recovery tax amount:

- Private pension income and superannuation income
- Foreign pension income

- RRSP and RRIF withdrawals
- Employment income
- CPP or Quebec Pension Plan (QPP) benefits
- Interest and other investment income
- Taxable capital gains (before applying net capital losses of other years)

The OAS benefit is reduced by 15% of the excess income above the minimum OAS income recovery threshold, until the maximum income recovery threshold is reached. Where an OAS recipient's benefits are subject to clawback in a year, an appropriate amount will be deducted from their future OAS pension payments as a recovery tax. To avoid having an individual repay a lump sum when filing their income tax return, the repayment (deductions) will be spread over 12 monthly pension payments starting in July of the following year.

For example, if an individual receiving OAS has a net income of $100,000 in 2023, then the following year's OAS benefits from July 2024 to June 2025 would be reduced by $1,963.20 (($100,000 - $86,912) ×15% = $1,963.20). A recovery tax of approximately $163.60 per month ($1,963.20 ÷ 12 months) would be deducted from the individual's OAS benefits starting in July 2024.

Deferring OAS

As of July 2013, an individual may choose to defer receiving their OAS for up to 60 months (i.e., 5 years). If an individual delays receiving their OAS pension, the monthly OAS pension payment will be increased by 0.6% for every month they delay receiving it, up to a maximum of 36% at age 70.

When should an individual commence their OAS?

There are several reasons that individuals may wish to consider taking their OAS payments at age 65 or deferring until after reaching that age, many of which parallel those for the CPP. Nevertheless, we have outlined a few reasons from an OAS standpoint below.

Reasons why an individual should consider commencing their OAS at age 65:

1. Reduced life expectancy: Much like taking CPP early, an individual may choose to commence their OAS payments "earlier" (i.e., at the standard age of 65) if they have reasons to believe they may experience a shortened life expectancy or if they see no value of delaying the benefits. This strategy could potentially maximize the OAS benefits received during their lifetime.

2. Financial need: Deferring OAS is a financial option generally reserved for individuals with adequate savings to sustain their lifestyle during the wait. For those who require immediate access to government benefits to meet their essential needs, deferring OAS may not be a practical solution.

3. Emotional and inheritance considerations: Deferring OAS to a later year may require individuals to withdraw a greater amount from their personal savings, such as from an RRSP, RRIF, or non-registered account, to cover their lifestyle while they wait to receive OAS. This may lead to the accelerated drawdown of their RRIF and other assets, which some individuals may find uncomfortable. Additionally, delaying OAS payments may result in a faster depletion of personal savings (e.g., RRSP, RRIF, or non-registered accounts) before death, leaving the individual with fewer funds to pass on as inheritance.

Reasons why an individual should consider deferring their OAS until after age 65

1. Higher payments: By deferring one's OAS pension to age 70, an individual can receive an enhanced benefit of up to 36% more than the maximum monthly payment of $691 (for the period of April to June 2023). To illustrate the impact of deferring OAS to age 70, consider the maximum monthly payment of $691 at age 65. By deferring OAS, the benefit increases by 0.6% for each month of deferral, resulting in a total increase of 36% by age 70. This would bring the annual OAS pension from $8,292 at age 65 to $11,277.12 at age 70 (a $2,985.12 difference), and the OAS pension payments will be adjusted for inflation for the rest of the individual's life. This substantial increase should be considered by individuals with relatively good life expectancy.

2. Reducing OAS clawback: Individuals between the ages of 65 and 70 who earn more than the income recovery threshold may benefit from deferring their OAS pension as they are able to avoid repaying part of or the entire amount of the OAS pension when their income is relatively high. If they delay receiving the payments until they have a lower income, they will be able to keep more of the OAS pension. In addition, they will benefit from an increased OAS pension amount calculated by the number of months deferred. It should be noted that there is no financial advantage in deferring an OAS pension past age 70. Rather, the individual risks losing benefits.

3. Protection against longevity risk: Similar to the reasons listed above to defer CPP, an individual may choose to defer their OAS payments to protect themselves against longevity risk. By delaying OAS, the individual will receive a permanent increase in the amount of OAS benefits for the rest of their life. This can reduce the possibility of running out of retirement funds later in their retirement.

Final note

Determining the optimal age to begin receiving CPP and/or OAS benefits is not a straightforward process and there is no universally applicable approach. The decision of when to start receiving CPP and/or OAS payments should be based on the individual's financial status, personal circumstances, and retirement goals, in addition to the considerations listed above.

✕ **Footnotes**

1 Source: Bonnie-Jeanne MacDonald, "Get the Most from the Canada & Quebec Pension Plans by Delaying Benefits", December 2020

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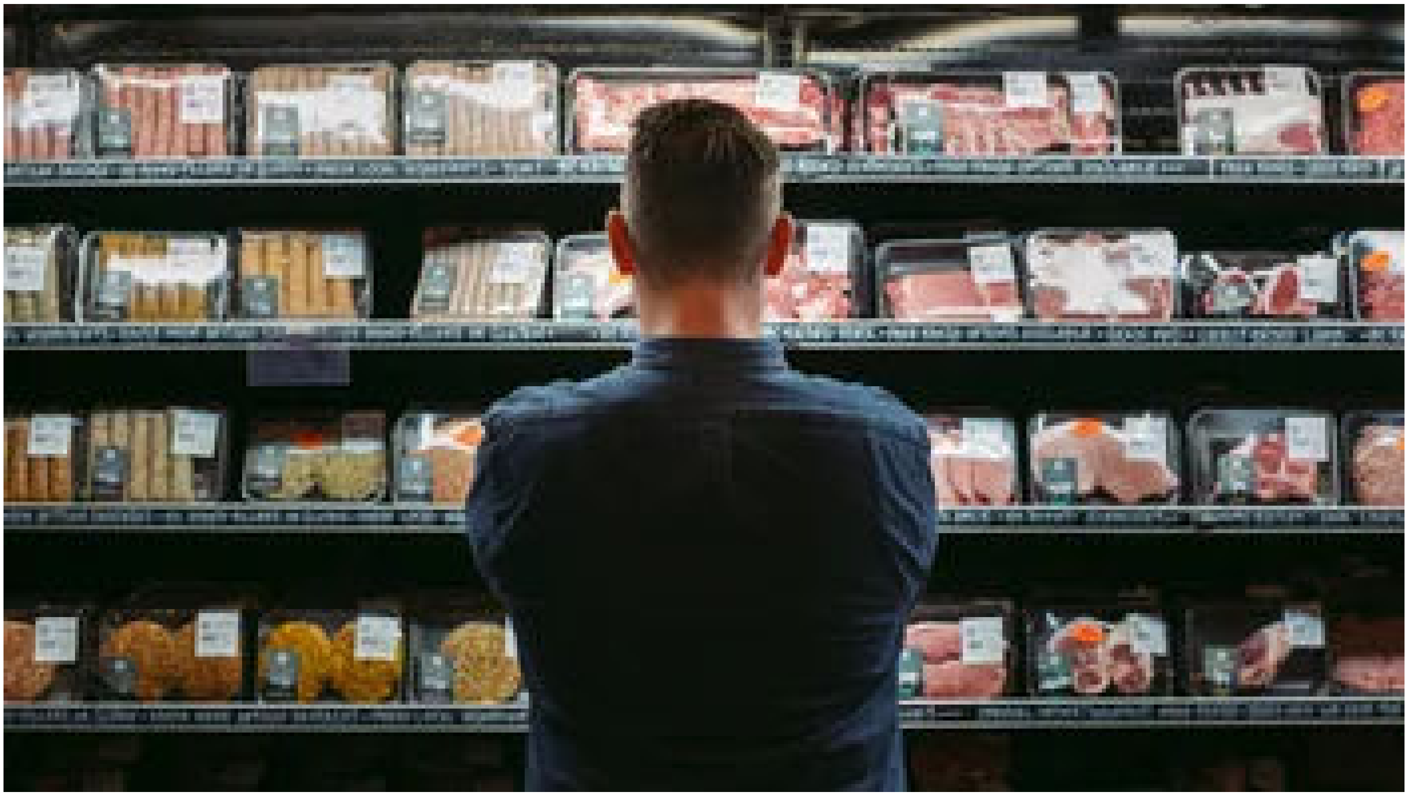

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