Retirees: Delay the CPP Until You’re 70 and Avoid OAS Clawbacks by the CRA

Description

Delaying the receipt of the Canada Pension Plan (CPP) payouts can benefit retirees in several ways. While some may view it as counterproductive, there are two major reasons to delay your CPP.

According to the Canada Revenue Agency (CRA), retirees generally start withdrawing CPP at the age of 65. However, you can start these payments as early as age 60 or delay them until you reach 70. In case you delay the pension until 70, the CPP payout will increase by 42%.

For example, the maximum annual CPP payment for a 65-year-old in 2020 stands at $14,109.96. This maximum figure increases to $20,036.14 for someone starting pensions at the age of 70.

Another reason for delaying your CPP is to save on CRA taxes. The Old Age Security (OAS) is also a pension program. The maximum OAS monthly payout is $613.53, which means the maximum annual payout is $7,362.36.

However, if your net annual income exceeds $79,054, the CRA will levy a 15% tax on your OAS. Further, if your annual income exceeds $128,137, you be ineligible for the OAS. We can see that if retirement streams arrive simultaneously, it can result in lower payments due to CRA clawbacks.

A retiree’s cumulative annual RRIF, CPP, and OAS withdrawals may be over the above-mentioned threshold limits. You can look to delay your CPP payouts to avoid taxes and benefit from a higher payout in later years.

Replace a part of your CPP with TFSA investments

We have seen the benefits of delaying CPP payments. Another way to avoid CRA taxes and generate a passive stream of income is by maximizing your TFSA (Tax-Free Savings Account). While the contributions to this account are not tax deductible, any capital gains or dividend withdrawals are tax-free.

The TFSA contribution limit for 2020 is $6,000, while the maximum contribution limit is $69,500. If you decide to delay CPP, you can generate a passive stream of tax-free income by allocating dividend stocks to the TFSA.

For people who do not have the time or expertise to pick individual stocks, investing in ETFs such as the **BMO Canadian Dividend ETF** (TSX:ZDV) is a good option. ETFs, or exchange-traded funds, provide investors enough diversification, as they hold a basket of stocks across different sectors.

You can invest in an ETF without having to spend hours analyzing individual company financials. ETF investing provides a simple way to access the stock market and diversify risk considerably.

ETFs have a lower expense ratio compared to mutual funds. Further, as they are traded on exchanges, ETF investing provides investors with enough liquidity and flexibility in terms of buying and selling these instruments.

The BMO Canadian Dividend ETF has exposure to quality Canadian dividend-paying stocks. The ETF is currently trading at $14.35, which is 23% below its record highs. It has a dividend yield of 5.6%. This means a $69,500 investment in ZDV will generate about $3,892 in annual dividend payments.

The Foolish takeaway

While some dividends are at risk due to the ongoing market uncertainty, owning a diversified portfolio reduces this risk significantly. Most of the ETF's top holdings, such as **Enbridge** have a solid history of increasing dividend payments, and this trend is likely to continue over the long term.

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