Canada Revenue Agency: How Retired Couples Can Get an Extra $567 Per Month Tax-Free

Description

Canadian seniors face rising expenses that might outpace the annual CPI-based increases to their CPP and OAS pension payments.

Consumer Price Index

The CRA raises Canada Pension Plan (CPP) and Old Age Security (OAS) payments according to increases in the Consumer Price Index (CPI). The CPI is designed to follow price changes for a basket of goods and services normally purchased by Canadians.

The base year for the CPI is 2002. Statistics Canada allocates a value of 100 for the CPI in this year. The CPI in January was 136.8, so the same basket of goods now costs 36.8% more than it did 18 years ago.

CPP and OAS increase rules

The government makes adjustments to the CPP annually. The changes, if any, go into effect in January. If the CPI increases over the 12-month period, the CPP goes up by the same percentage. In the event the CPI drops, the CPP payments remain the same.

OAS is reviewed four times a year, in January, April, July, and October, to help ensure seniors are covered when the CPI jumps sharply during a shorter time period.

An increase would require a jump in the average CPI over the most recent three-month period compared to the previous three-month period in which the OAS payment increased.

As with CPP, the OAS payments are not reduced if the CPI value drops.

Every person’s cost of living is different. The CPI system is a broad-based measurement, and it is possible some people see their average living expenses rise much more than the changes in the CPI.

In fact, many retired couples might argue their rent, health costs, food prices, property taxes, and general maintenance expenses for the house or cars have outpaced the increases to their CPP and OAS pensions.

Tax impact

The CPP and OAS pensions are taxable, so the net amount available to spend depends on your marginal tax bracket. People who also receive company pensions and other income might be at risk of OAS clawbacks, as well. The net world income threshold for the OAS pension recovery tax is $79,054 in 2020.

How to earn tax-free pension income

Seniors can use their Tax-Free Savings Accounts (TFSAs) to hold income-generating investments. All interest, dividends, and capital gains generated inside the TFSA are tax-free. In addition, the CRA does not use the withdrawal of TFSA earnings to determine net world income for possible OAS clawbacks.

GICs are safe, but they offer very low rates today. As a result, many seniors are turning to dividend stocks to get better returns. Stocks come with risk, as we witnessed in recent months, but the top companies with strong businesses and long track records of revenue growth should be solid buy-and-hold picks.

Many of these companies now offer very attractive yields.

For example, **Royal Bank of Canada**, **BCE**, **Fortis**, and **TC Energy** all pay dividends that should be safe through the current recession and will likely continue to grow once the economy recovers.

Royal Bank is Canada’s largest financial company and remains very profitable, even in the current difficult times. The dividend yield is 4.6% right now.

BCE is a long-time favourite among retirees. The stock currently offers a 5.9% yield.

Fortis raised its dividend in each of the past 46 years and intends to boost the payout by 6% per year through 2024. The yield is 3.6% today.

TC Energy has a strong capital program that should support a dividend increase of 8-10% in 2021 and average hikes of 5-7% in the following years. The existing payout provides a 5.5% yield.

The bottom line

The current TFSA contribution space is as high as $69,500 per person. That means a retired couple could hold $139,000 in top dividend stocks. The four companies mentioned above would be a good start for a diversified portfolio and would provide an average yield of 4.9%.

This would provide $6,811 per year in tax-free income on a $139,000 portfolio. That’s $567.58 per month!

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