10.9% CPP Pension: Your Take-Home Pay Will Be Smaller in 2021

Description

Under normal economic conditions or in a year of abundance, contributors to the Canada Pension Plan (CPP) wouldn't mind the gradual increases in contribution rates. However, COVID-19 affected the earning capacities of Canadian workers.

If you're self-employed, your take-home pay will be smaller in 2021. In the third year of the enhanced CPP, the contribution rate is 10.9%. The rate is half, and the employer will also contribute 5.45% to make it 10.9% for employed individuals.

Sense of urgency

The framers of the CPP enhancements in June 2016 felt a sense of urgency to help Canadians save more for retirement. Thus, it becomes imperative for them to implement the changes effective in 2019. The increases in contributions will significantly benefit individuals without a workplace pension plan.

A CPP user shouldn't feel disadvantaged even if it will hurt financially in the short-term. Instead, look at the positive effect in the future. Your take-home pay will decrease from 2019 to 2023 or later. Once fully phased in, a CPP pension will replace 33.33% of the average worker's lifetime earnings.

Two phases

In terms of absolute amounts, the maximum annual self-employed contribution in 2021 is $6,332.90. Meanwhile, an employer and its employee will contribute an annual maximum amount of $3,166.45 each. People earning $3,500 and below need not contribute to the CPP. The period from 2019 to 2023 is just the first phase, as the enhancements are continuing until 2024.

The second phase commences in 2024, where there will be changes to the maximum pensionable earnings. An additional contribution of 8% (split 4% between employee and employer) will apply in2024 and 2025 to earnings between the Year's Maximum Pensionable Earnings (YMPE) at the timeand a new earnings upper limit.

If you're making contributions under the newly enhanced CPP, your pension will start to grow in 2019. When the enhancements are entirely in place, a retiree CPP can expect to receive almost $21,000 annually in today's dollars.

Lifelong income source

Canadians with a comprehensive retirement plan know that the CPP is not part of the program. The pension is the foundation but not the primary source of retirement income. A retiree needs a different wellspring to provide the bulk of sustenance in the sunset years.

Many retirees live off dividends or investment income from **Canadian Utilities** (TSX:CU). This $8.81 billion pays a lucrative 5.39% dividend. If you have $175,000 to invest today, your nest egg will be half-a-million in 20 years. Assuming the yield remains constant until 2040, your annual income would be $26,953.48.

Canadian Utilities holds the record (50 consecutive years) for the longest dividend-growth streak on the TSX. The business is enduring, and the utility assets globally consist of electrical power lines (87,000 km), pipelines (64,000 km), and 21 generating plants (2,500 MW in total capacity).

This high-end utility company derives 86% of its earnings from regulated sources, while the rest comes from long-term contracted assets. Don't pass up on an income stock that increases its dividend every year.

Seven years

CPP users must be aware that contributions will increase over seven years. Next year is only the third installment. However, you'll say when you retire, the seven-year sacrifice is all worth it.

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