Big Changes for CPP in 2021: How Much Payout Will You Get?

Description

The Canada Revenue Agency (CRA) is introducing big changes to the Canada Pension Plan (CPP) in 2021. These changes will impact your salary, taxes, and CPP payout. I have discussed the first two impacts in my previous articles. Here, I will discuss how these changes will impact your CPP payout.

The CPP 2021

The main idea behind creating CPP was to help Canadians and their employers contribute toward retirement planning. The CPP plans to give you 25% of your average work earnings when you retire. But the rising cost of living is forcing many Canadians to extend their retirement. Hence, the CRA launched CPP enhancement in 2019, under which it will increase the contribution rate and maximum pensionable earnings till 2025.

For 2021, the CRA has increased the CPP contribution rate to 5.45% from 5.25% in 2020. It has also increased the maximum pensionable earnings to $61,600 from $58,700 in 2020. By collecting higher CPP contributions, the CRA intends to pay 33% of the average work earnings you receive after 2019.

If you contributed to the CPP for a significant number of years, the CRA will pay you a monthly pension once you turn 65. But you have to apply for a CPP payout. You can apply for a payout as early as 60 years of age or as late as 70 years of age.

What's your CPP payout?

The CRA calculates your CPP payout based on:

- Your average earnings in your working life;
- Your CPP contributions; and
- The age you start your CPP payout.

If you want to maximize your CPP payout, delay your payout till you turn 70 and continue contributing to CPP between 65-70 years of age. The higher and longer you contribute, the higher will be your payout.

For 2020, the maximum CPP payout for new retirees (age 65) increased by $20 to $1,175.83 per month. The CRA has not revealed the maximum payout for 2021, but it will be $20-$30 above the 2020 payout. In the future, the CRA plans to increase the maximum CPP payout by 50% if you contribute to the enhancement plan for 40 years.

Remember, the CRA will add CPP payout to your taxable income. However, it will also gives you many tax breaks like the age amount and basic personal amount tax credit that can help you reduce your tax bill.

A pension the CRA can't tax

All other forms of pension you collect in your retirement are taxable. One way you can earn a tax-free pension is through the Tax-Free Savings Account (TFSA). In TFSA, the CRA taxes your contribution, but exempts the money you earn from investments. You can withdraw any amount from your TFSA without worrying about taxes.

This is a good time to plan your TFSA pension as the COVID-19 pandemic has created a once-in-a-decade dividend sale. Dividend Aristocrats like **Enbridge** (TSX:ENB)(NYSE:ENB), **RioCan**, and **Suncor Energy** are trading at a 20%-40% discount. This has inflated their dividend yields.

If you have to choose one stock, I would suggest Enbridge, as it has been increasing its dividends every year at a CAGR of 11% for the last 25 years. The stock has proved its ability to withstand the 2009 financial crisis and the 2014 oil crisis headstrong.

It increased its dividends during these crises and is likely to increase dividends even during the pandemic crisis. The pandemic forced many companies to cut dividends. If Enbridge increases its dividend per share in the first quarter of 2021, the stock could see a significant jump.

Enbridge stock has already surged 22% on COVID-19 vaccine news and has the potential to grow another 30% in a year or two.

Investor corner

If you already have some investments in TFSA that are giving you less than 7% returns, encash some of that amount and put it in Enbridge. A $40,000 investment in Enbridge will fetch you $260 in monthly dividend income.

If Enbridge increases its dividends at an average annual rate of 8%, your monthly dividend income will increase to $566. This incremental income will beat inflation.

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