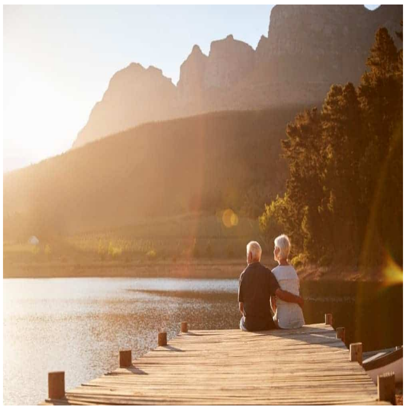

Canada Pension Plan: Is it Smart to Start Payments at Age 60 or 70?

Description

Should the timing to take the Canada Pension Plan (CPP) really matter? The CPP is a mandatory, universal, contribution-based public retirement pension plan. Any Canadian over 18 years old and above with employment earnings must contribute to the CPP.

The default retirement age is 65. If you've been contributing to the CPP during your working years, you may apply for full benefits at 65. However, even with this pension provision, the CPP is flexible and offers two other choices. A CPP user can start payments earlier at 60 or defer until 70. But which one is a smarter move?

Typical take-up

A would-be pensioner must carefully assess when to begin CPP payments. You don't want to risk financial dislocation in retirement. Remember, too, that CPP contributions are tax deductible under the Income Tax Act. CPP determines an individual's benefit by calculating the average earnings throughout a person's career.

Employers and employees make equal annual contributions, while the self-employed contribution rate is double the employer and employee rates. The average CPP monthly pension for June 2020 is $710.41, assuming you're 65 and claiming your pension today. Very few new recipients get the maximum of $1,175.83. You can visit or log into your My Service Canada Account to get an estimate.

Drawback or incentive

CPP users desiring to start payments when available have a drawback. If you start monthly pensions at age 60, the implication is a 7.2% cut for each year before 65. Hence, your CPP reduces by 36% permanently if you can't afford to wait until 65. Also, collecting CPP too soon could bring down your after-tax income in retirement.

In reverse, the delay option offers an incentive. Every year you delay the payments before 65, the annual top-up is 8.4%, or a significant increase of 42% overall. If you're in excellent health, taking the CPP later makes sense, because you mitigate the longevity risk while receiving higher CPP benefits.

Tailor-fit for retirees

Know early on that your CPP pension will only cover 25%, at least, of the average lifetime earnings. The amount might not be enough to fund the lifestyle you envision. Many Canadian retirees tap other income sources apart from the Old Age Security (OAS). Dividend investing is the way to go to create lasting income.

Bank of Montreal (TSX:BMO)(NYSE:BMO) is an investor-friendly and reliable asset for retirees. No publicly listed company in the TSX can outstrip the fourth-largest bank in Canada of its lengthy dividend track record. BMO was the first company ever to pay dividends. It dates back to 1829, or 191 years and running.

This bankable income stock trades at $97.43 per share and offers an enticing 4.35% dividend. A $197,500 investment will produce a monthly pension-like income of $715.94, slightly higher than the average CPP per month. If you don't touch the principal and keep reinvesting the dividends, you'll have a nest egg of $462,824.22 in 20 years. Analysts forecast the stock to climb to $116 in the next 12 months.

Save more

Individual circumstances, health, and financial resources are the determining factors with regards to CPP claims. But whether the verdict is 60 or 70, users or would-be retirees need to save more than the pension.

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