Canada Pension Plan: 1 Crucial Change in 2021

Description

Canada Pension Plan (CPP) users should view the ongoing enhancements as positive developments in the country's retirement system. The objective of the federal and provincial ministers that met in June 2010 was to increase pension coverage of millions of Canadian workers.

This year is the midpoint of phase one of the enhancements that took effect in January 2019. For CPP contributors, it means an annual contribution of $3,166.45 in 2021 instead of $2,898. The increase in total amount is due to a crucial change, particularly the higher employee and employer contribution rate of 5.45% from 5.25% in 2020.

Gradual and moderate increases

While the CPP enhancements will impact take-home pay, the crafters made sure the increase in contribution rates is gradual. Also, it would enable workers and employers to adjust to the moderate yearly increases. Over seven years, including phase two (2024-2025), the overall increase from 2018 is only 1%.

For self-employed individuals, the contribution rate is always double the employee and employer contribution rate. Thus, the rate in 2021 is 10.9%, which translates to an absolute annual amount of $6,332.90.

What comes with the enhancements?

The CPP enhancements will not alter the Year's Basic Exemption (YBE), whose amount since 1996 has been $3,500. You don't have to contribute to the plan if your income is equal to or lower than the YBE. However, the Year's Maximum Pensionable Earnings (YMPE) will increase in 2021 to $61,600.

YMPE pertains to the maximum salary amount on which you need to contribute to the CPP. If you earn more than $61,600 this year, you can't make additional contributions. The federal government caps it yearly. When the enhancements enter phase two in 2024, there'll be a separate contribution rate for income above the YMPE (4% employee and employer).

Augment your CPP pension

To live comfortably in retirement, it's a must to augment your CPP pension and Old Age Security (OAS). Most would-be retirees in Canada have a Registered Retirement Savings Plan (RRSP) and Tax-Free Savings Account (TFSA) from where they draw the bulk of retirement income.

Investing in established dividend payers like **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) can provide you with a pension-like income. It means the income you'll generate is also for life. Today, you can purchase the bank stock at $112.88 per share and partake in the 5.19% dividend.

Assuming you have $120,000 to invest, the bank stock will deliver $1,557 in quarterly, recurring income. In a 20-year investment horizon, you would have a nest egg of $330,118.87. The capital will compound, as you keep reinvesting the dividends.

CIBC is among the buy-and-hold stocks on the TSX, because of its outstanding dividend track record. This $50.46 billion bank has been paying dividends for 152 years, including the worst recessions and financial crises in recent history. CIBC's business banking, wealth management, and capital markets divisions contribute to the bank's steady performance.

Higher retirement income

The sacrifice of CPP users in the course of the seven-year phase-in will further increase retirement income. Younger workers and new additions to the workforce will benefit the most. But the most salient feature is the increase in replacement level. Instead of 25%, the CPP will replace one-third (33.33%) of the average workers' earnings.

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