CPP Pension Users: 3 Smart Ways to Avoid the OAS Clawback

Description

The Canada Revenue Agency (CRA) is not planning to extend tax-filing and -payment deadlines. Instead, the government agency's website is telling everyone to prepare for their taxes on the April 2021 deadline.

The coming tax season will also be another year when retirees will battle with the Old Age Security (OAS) clawback. It is safe to say that no retiree wants any of their retirement income reduced due to the recovery tax.

I would advise beginning preparations for your taxes in April as early as you can. If you want to avoid the 15% recovery tax on your OAS payments, there are three smart ways you can avoid the CRA from dipping into your retirement income.

1. Defer your OAS

One option to reduce or entirely avoid the clawback's impact on your OAS is deferring the pension income until you turn 70. The strategy is ideal for Canadian retirees between 65 and 70 years old when their income is high. Delaying your OAS will give you two benefits:

- Your OAS benefit will increase by 36% if you delay starting it until you are 70 instead of beginning it at 65.
- It will also increase the ceiling you can earn before not receiving any OAS. It means that you can receive more than the maximum while still receiving some OAS, and it will take more income for the CRA to claw it back due to higher OAS benefits.

2. Early RRSP withdrawal

Another smart move to avoid your OAS clawback is withdrawing the funds from your Registered Retirement Savings Plan (RRSP) early. This strategy can work best if your income before retirement is in a lower-income bracket. Taking out your RRSP early can maximize your OAS benefits when your

RRSP becomes depleted later on.

3. Improve your tax-free income

The Tax-Free Savings Account (TFSA) is an exceptional method to generate passive income. The CRA will not consider any revenues you earn through the tax-sheltered account during your retirement when it is calculating your net income for the OAS clawback threshold. Optimizing your TFSA to generate reliable passive income through dividend-paying stocks can help you earn more income without triggering the OAS clawback.

Bank of Montreal (TSX:BMO)(NYSE:BMO) can be an exceptional addition to your TFSA portfolio to generate reliable passive income, because of its virtually guaranteed dividend payouts. BMO is the fourth-largest Canadian bank and is known to be investor friendly.

BMO has a dividend-paying streak that stretches almost two centuries. It means that the bank has delivered payouts to its shareholders virtually every year since it started paying dividends. The stock is trading for $98.13 per share at writing. At its current valuation, the stock is paying its shareholders a juicy 4.32% dividend yield.

Foolish takeaway

Canadian retirees can tend to worry a lot due to the 15% OAS clawback reducing their retirement income. However, using these three smart tricks can help you reduce or completely avoid the OAS clawback and keep all your retirement income free from CRA's clutches.

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Author
adamothman