Retirees: Here's How Little CPP Pays You

Description

If you're retired, you're probably counting on CPP to finance your retirement.

Perhaps you're lucky enough to have a generous employer-sponsored pension. But if you're like most Canadians, you probably don't have one. Outside of the public sector, defined benefit pensions are increasingly rare. Defined contribution pensions are still common but not universal, and they're vulnerable to market swings.

So, unless you've got a lot of savings, you're relying on CPP to pay for your retirement. Unfortunately, it won't pay you enough to cover all of your expenses. You may already know that CPP pays very little, but it actually pays even less than you've probably heard. Here's why.

Taxes eat into CPP and OAS income

According to WealthSimple, CPP pays $689 on average. OAS pays a flat $635 (assuming no clawbacks). So, if your CPP is average, and your OAS isn't clawed back, you should get about $1,324 per month.

Sounds like a decent amount, right?

Not really.

The thing is that CPP and OAS are both fully taxable. CPP is taxed at your marginal tax rate. OAS is also taxed at your marginal rate PLUS has the recovery tax on top of that. If you earn $126,000, your OAS gets clawed all the way back to zero! Of course, if you're earning that much money, then you don't need to worry about CPP and OAS amounts: you're doing fine. But if you're a Canadian relying on *just* CPP and OAS, then the potential taxes could hit you in the pocketbook.

If you make $1,324 every month, that works out to $15,888 per year. In Ontario, you'd pay $1,132 in total taxes on that. So, really, you only get $1,229 per month. That's a bit of a problem, because the average Toronto apartment now costs over $2,000. Even if you own a home, there's always property taxes and utilities to watch out for. And, of course, groceries, internet, cell phones, etc., all cost quite a bit of money when you put them all together.

Invest in a TFSA to secure a wealthy retirement

The bottom line about CPP and OAS is this:

Unless you have a generous employer pension coming to you, you need to invest to supplement your CPP and OAS income. For most retirees, the two benefits just don't pay enough. Sure, you can wait until 70 to take CPP and boost your benefits that way. But retirement is meant to be enjoyed. Who wants to spend their 60s working just to boost CPP payments? Nobody does.

So, what you want to do is supplement your CPP by holding index funds like **iShares S&P/TSX 60 Index Fund** (TSX:XIU) in a TFSA. Index funds are great, low-risk investments that hold diversified portfolios of stocks. They typically perform pretty well over the long term, and the inherent diversification lowers the risk involved.

XIU holds 60 stocks and has a low, 0.16% fee. So, you won't lose too much of your returns to the fund managers. By holding the fund in a TFSA, you won't lose your returns to the CRA, either. Holding such a fund in a TFSA can be a wise choice. Of course, you should speak to a financial advisor before buying XIU or any other fund. But researching these funds is a great place to start.

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