Retiring at 60? You Can Get the Maximum CPP, But There's a Catch

Description

The impact of runaway inflation is heaviest on retirees who depend on pensions like the Canada Pension Plan (CPP) to fund their lifestyles. Fortunately, CPP benefits adjust for inflation on the first month of every year.

As of January 2022, the retirement pension at age 65 increased by 2.7%. The maximum monthly payment amount, after the adjustment, is now $1,253.59 ($15,043.08 per year). But because inflation has been running high since 2021, the increase in 2023 could be a bit higher.

Unfortunately, very few CPP users are qualified to receive the maximum benefit. Only those who have contributed the maximum length or a full 39 years are eligible. As of April 2022, the new average amount for new beneficiaries (age 65) is $727.61 per month, or $8,731.32 annually.

Early claim

CPP users can collect their benefits as early as 60. It's also possible to get the maximum pension. However, you can only qualify if your contributions started at age 21, or at least 39 years, by age 60. Otherwise, expect to receive a reduced benefit amount.

The pension payment reduces by 7.2% per year (36% in five years) if you start collecting before 65. Hence, the CPP monthly amount could be as low as $465.67 instead of $727.61. The financial consequence of an early claim is significant.

Incentives

Most Canadians take their CPP benefits at the default age or 65. However., some seniors avail of the incentive to boost pension payments. If you delay payments past 65, the pension amount increases by 8.4% per year until age 70 (42% in five years).

If you elect to receive your CPP benefits at 70, the monthly benefit amount becomes $1,033.21, or

$12,398.47 per year. Note that CPP benefit amounts aren't uniform but varying depending on the average salary, contribution, and years of contribution per individual

The Old Age Security (OAS) pension also increases if you start payment at 70. The overall increase in five years is 36%. Thus, instead of $666.83 per month (July to September 2022), you'll receive $906.89. Combine it with your CPP, and the annual pension is $23,281.14.

Use your tax-advantaged account

Financial planners suggest using the Tax-Free Savings Account (TFSA) as a retirement account. Use your contribution limits or available contribution rooms to purchase dividend stocks. **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM) can be your anchor in the tax-advantaged account.

The $60.77 billion bank, Canada's fifth-largest lender, pays an attractive 4.95% dividend. If you own $50,000 worth of shares (at $67.24 per share) in a TFSA, the investment can generate $618.75 in tax-free income every quarter. Given its dividend track record of 154 years, you can purchase the big bank stock and never sell.

Not a retirement plan

The Canada Pension Plan Investment Board, the fund manager of the pension fund, said the CPP is not a retirement plan but a foundation to build financial security. Since the benefit replaces only 25% of the average pre-retirement income, users need to fill the gap to have a comfortable retirement.

Future retirees can't leave everything to chance and simply rely on pensions. There are several reasons why retirement planning is important. Number one is that you don't want to run out of money in retirement.

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