Cross Border Retirement Income:
Canada Pension Plans, Canadian Old Age Security, U.S. Social Security and the Windfall Elimination Provision

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CROSS-BORDER WEALTH MANAGEMENT

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Calling all eligible benefit holders of the Canada Pension Plan (CPP), Canadian Old Age Security (OAS) and U.S. Social Security (SS).

Does you or your spouses' story narrate a history of employment in both Canada and the U.S.? If so, you may have the privilege of drawing from SS, OAS and CPP. The confusion lies amidst the qualifications and how these benefits interact with one another given the Windfall Elimination Provision (WEP).

Let's break it down...

Social Security (SS)

To qualify for retirement benefits under U.S. Social Security, you must have 40 credits of covered work. Each credit represents a quarter (i.e. 3 months) of full time employment. Thus, generally speaking, you must have 10 years of full time employment in order to qualify for retirement benefits.

All monthly benefits are based on your Primary Insurance Amount (PIA), which is the amount you would receive if you retired at your full retirement age (FRA). The FRA is 65 for people born before 1938, gradually increasing to 67 for those born in 1960 and later. You can choose to take it as early as 62, resulting in a 25% reduction in benefit. At a more granular level, the monthly PIA is reduced by 5/9ths of 1% for each of the first 36 months before FRA. You can also choose to earn delayed retirement credits (DRCs) for any month from FRA up to age 70. DRCs increase the benefit for the retired worker but not the spouse (if utilizing the spousal benefit). If you were born in 1943 or later, you earn 8% DRCs for each full year (prorated for months) up to age 70 for a total increase of 32%.

Individuals have the opportunity to take a SS benefit on the greater of their own record or 50% of their spouses.

Canadian Old Age Security (OAS)

The rules to qualify for full OAS benefits under the Canadian system are centered on residency in Canada beyond the age of 18, not employment history.

A full benefit is received when an individual has accumulated a Canadian residence history of 40 years. The pension can commence as early as the month following one's 65th birthday or be delayed as late as 70. By deferring one's OAS, the benefit increases by 0.6% per month/7.2% per year, which equals a 36% increase if OAS is deferred to age 70.

Partial OAS benefits may be available in certain situations. Let's review a few scenarios:

Let's assume you've lived in Canada less than 40 years, and you are currently residing in Canada. As long as you are 65 years or older, a legal resident of Canada or Canadian citizen, and have lived in Canada at least 10 years since the age of 18, you are eligible for a prorated benefit.

To take a step further, let's assume the same scenario with bit of a twist. Instead of currently residing in Canada, you are now living in the U.S. These circumstances dictate you must have resided in Canada for a minimum of 20 years since the age of 18 in order to receive a partial benefit.

If neither of these examples apply to you, there may still be an opportunity to collect on the benefit if the country in which you currently reside, has a social security agreement with Canada.

One final item on OAS; if one were to reside in Canada at the time of receipt of the OAS payment, the individual may be subject to OAS clawback. This would be created if your income exceeds certain threshold levels. For the 2022 tax year, the OAS clawback kicks in when income exceeds, $81,761. On the other hand, if OAS payments are made to a physical resident of the U.S. – and not a Canadian physical or tax resident - the claw-back provisions are eliminated, and the entire benefit is paid to the recipient. No OAS clawback would apply.

Canada Pension Plan (CPP)

Unlike Old Age Security, CPP is based upon your pension contributions through your employment record, subject to certain maximums. As long as you've made at least one contribution to the plan, you are entitled to receive a CPP benefit. The benefit is available at 65, or one can opt for a reduced benefit as early as age 60 (reduced by 7.2% annually) or a delayed benefit as late as age 70 (increased by 8.4% annually). In addition, the CPP benefit is not subject to any clawback.

How then do these benefits tie in with the Windfall Elimination Provision (WEP)?

Understanding the Windfall Elimination Provision

Under Title II of the Social Security Act, the Windfall Elimination Provision was born. It authorized the Social Security Administration to reduce an individual's Social Security benefit in the event the benefactor was also receiving a foreign pension (e.g. CPP). To understand the "why" behind WEP its important to comprehend how the SS benefit is calculated, specifically the Primary Insurance Amount (PIA).

A worker's PIA is based off their average monthly earnings separated into three amounts. These values are then multiplied utilizing three distinct factors. Here's an example:

For a worker who turns 62 in 2022, the first $1,024 of average monthly earnings is multiplied by 90%; earnings between $1,024 and $6,172 by 32%; and the balance by 15%. The sum of these three amounts coincides with the PIA which is either increased or decreased depending on when a worker decides to draw SS, before or after their full retirement age (FRA). This is how the monthly payment is determined.

Social security was meant to replace part of an individual's pre-retirement earnings. With the previous calculation in mind, one can conclude that workers with lower average monthly earnings have a higher percentage of their pre-retirement earnings replaced via Social Security than those with higher average monthly earnings. For example, a 62 year old worker with average earnings per month of $3,000 could receive a benefit at FRA of $1,554 (52 percent of their pre-retirement earnings) increased by cost of living adjustments. For a worker with $8,000 of average earnings per month, the benefit starting at FRA could be $2,843 (36 percent of their pre-retirement earnings) plus cost of living adjustments.

For those individuals whose primary job wasn't covered by Social Security, yet had their benefits calculated as if they were a long term, low-wage worker they would end up receiving a benefit that would cover a higher percentage of their earnings, plus a pension from a job for which they didn't pay Social Security taxes. This is true for the worker that spent time working for an employer in Canada, earning CPP credits.

As such, the calculation for a worker's Social Security benefit needs to account for the CPP payment under the Windfall Elimination Provision. The 90% factor on the first $1,024 of monthly average earnings (when estimating PIA), could be reduced depending on the number of years of U.S. earnings history. The WEP is eliminated once a worker has 30 or more years of substantial earnings in the U.S.

The U.S. Social Security Administration has an Online WEP Calculator that is available here.

In Summary

Although a worker's Social Security is potentially reduced by CPP, the good news is that OAS does not factor into the WEP calculation. Whether the WEP impacts your Social Security depends on the uniqueness of one's individual circumstances. If you think you might be impacted by WEP, we recommend you have a cross border financial planner such as Cardinal Point analyze your situation.

Furthermore, the analysis of your particulars should be carried out by a cross border planner. For more information contact Cardinal Point.

Contact Cardinal Point for more information

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