

# Understanding Social Security Retirement Benefits

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# Agenda

- Social Security eligibility
- Key Social Security questions
  - What is your benefit amount?
  - When to start benefits?
  - What if you work while receiving benefits?
  - How are the benefits taxed?
- Benefit planning strategies
- Social Security Outlook

## Social Security Eligibility

- Once you have 40 quarters of earnings history, you are eligible for benefits
  - For 2015, you earn one quarter for each \$1,220 of earnings (max of 4 quarters per year)
  - Example:
    - Earn \$2,500 for two months of work during the year
    - Earn 2 credits for that year
- Quarters of coverage do NOT impact eventual benefits

# Key Social Security Questions

What is your benefit amount?

What if you work during retirement?

How are benefits taxed?

## Calculating Your Benefit Amount

- Benefit is based on earnings over your 35 highest-earning years
  - If you only worked 30 years, you have five \$0 years that lower your overall benefit
- Earnings over annual maximum don't impact benefits
  - 2015 maximum - \$118,500
  - Check your earnings history for accuracy
- Worker with maximum income each year would earn maximum benefit
  - \$2,663/month for 2015 retiree at Full Retirement Age

## Worker's Benefit

Worker is eligible for standard retirement benefit at Full Retirement Age (FRA)

Year of Birth	Full Retirement Age
1943-54	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 or later	67

# Taking Benefits Before FRA

- 6.7% annual decrease for up to 3 years early
- 5% annual decrease for more than 3 years early

Apply at age	If FRA = 66	If FRA = 67
62	75.0% (100%*)	70% (100%*)
63	80.0% (107%*)	75% (107%*)
64	86.7% (116%*)	80% (114%*)
65	93.3% (124%*)	86.7% (124%*)
66	100% (133%*)	93.3% (133%*)
67		100% (143%)*

\* As compared to age 62 benefit

# Taking Benefits After FRA

- Delayed Retirement Credit (DRC) of 8% per year deferred, plus inflation adjustments

Apply at age	If FRA = 66	If FRA = 67
66	100% (133%)*	93.3% (133%)*
67	108% (144%)*	100% (143%)*
68	116% (155%)*	108% (154%)*
69	124% (165%)*	116% (166%)*
70	132% (176%)*	124% (177%)*

\* As compared to age 62 benefit



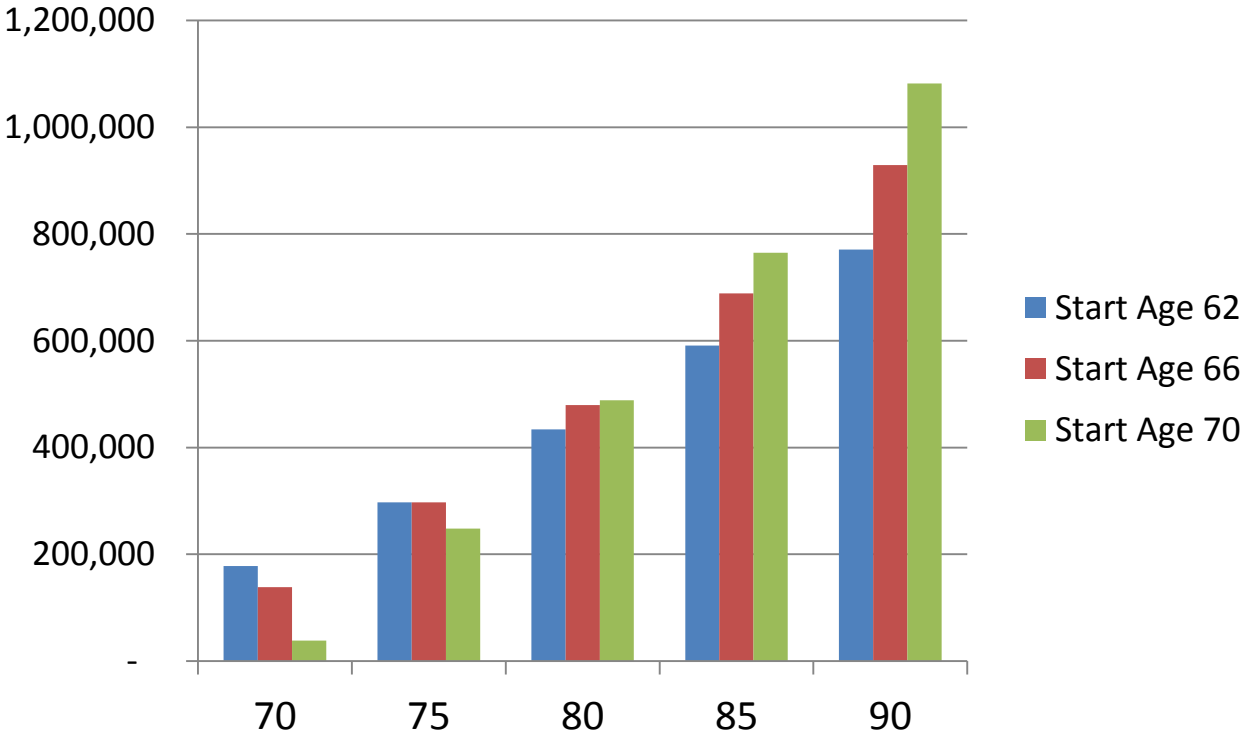
## When to Begin Taking Benefits

- So, when does it make sense to start taking benefits?
- Typically a function of Life Expectancy

## When to Begin Taking Benefits

- Example:
  - Worker retires at end of 2014 at age 62
  - Retiree could receive SS benefits at FRA (age 66) of \$2,000/month
  - By starting at age 62, benefit would be reduced by 25% to \$1,500/month
  - By deferring to age 70, benefit is increased by 32% to \$2,640/month

# When to Begin Taking Benefits



## What if You Work During Retirement?

- Once you reach Full Retirement Age (FRA), income you earn doesn't impact Social Security benefits
- Before FRA, however, benefits can be reduced
  - Earnings threshold for 2015 = \$15,720
  - Benefits reduced by \$1 for every \$2 over that amount
- Monthly earnings test applies in the year of retirement
  - $\$15,720 / 12 = \$1,310$

## What if You Work During Retirement?

- Example:
  - Begin taking benefits at age 64
  - Earn \$25,000 during the year, plus receives \$12,000 in Social Security
  - Excess earnings = \$9,280 ( $\$25,000 - 15,720$ )
  - Lost benefits = \$4,640 ( $\$9,280 / 2$ )
  - Net benefit = \$7,360 ( $\$12,000 - 4,640$ )

## How Much of Your Net Benefit is Taxable?

- As Modified AGI goes up, more of your benefits become taxable

<b>Married</b>	<b>Single</b>	<b>Amount Taxable</b>
Less than \$32,000	Less than \$25,000	0%
\$32,000-\$44,000	\$25,000-\$34,000	50%
Over \$44,000	Over \$34,000	85%

# Tax Rules for Social Security

- Modified Adjusted Gross Income includes:
  - All sources of income
    - Investment income, capital gains, pensions, IRA withdrawals, etc.
  - Tax-exempt interest income
  - 50% of the Social Security benefit itself
- 14 states still tax benefits in some form\*
  - CT, CO, IA, KS, MO, MN, MT, ND, NE, NM, RI, UT, VT, WV
- 29 states exempt benefits from income tax (plus DC)\*
- 7 states have no income tax
  - AK, FL, NV, SD, TX, WA, WY

# Spousal Planning Strategies



## His, Hers and Theirs

- One worker can provide benefits to many individuals:
  - Themselves
  - Spouse
  - Surviving spouse, minor children
  - Ex-spouse
  - Surviving ex-spouse
  - Parents

## Spousal Benefits

- Spouse is eligible for larger of:
  - Benefit based on their own work history
  - 50% of benefit based on spouse's work history (aka spousal benefit)
- **Can't claim spousal benefit until working spouse files for benefits**
- Surviving Spouse is eligible for larger of:
  - Benefit based on their own work history
  - 100% of benefit based on deceased spouse's work history

# Advanced Planning Strategies

# Spousal Benefit Planning

- Contradiction in planning:
  - Spouse can't get spousal benefit until worker files for benefits
  - Beginning at age 70 gives a larger lifetime benefit in most cases due to 8% DRC
- Dilemma:
  - How do we earn the 8% DRC while also maximizing the spousal benefit?
- **Answer:** File & Suspend and Restricted Application

## File & Suspend Technique

- Law change in 2000 allows working spouse to file for benefits, but then suspend receipt
  - Filing allows lower-benefit spouse to claim spousal benefit
  - Working spouse's benefit continues to earn Delayed Retirement Credits (8% per year plus inflation)

## File & Suspend

- **Example:**

- Both spouses at FRA (age 66)
- Current benefits based on own work history
  - Husband - \$2,000/mo; wife - \$600/mo
- Husband files for benefits, but suspends receipt
  - Wife files for spousal benefits at FRA, gets \$1,000/mo (50% of Husband's benefit)
  - Husband defers his benefit to age 70, gets \$2,640/mo, plus inflation

# Cumulative Retirement Benefit – File & Suspend

Both Benefits at FRA					File & Suspend			
His	Hers	Total	Cumulative	Ages	His	Hers	Total	Cumulative
24,000	12,000	36,000	36,000	66	-	12,000	12,000	12,000
24,648	12,324	36,972	72,972	67	-	12,324	12,324	24,324
25,313	12,657	37,970	110,942	68	-	12,657	12,657	36,981
25,997	12,998	38,995	149,938	69	-	12,998	12,998	49,979
26,699	13,349	40,048	189,986	70	35,243	13,349	48,592	98,572
27,420	13,710	41,130	231,116	71	36,195	13,710	49,904	148,476
28,160	14,080	42,240	273,356	72	37,172	14,080	51,252	199,728
28,920	14,460	43,381	316,736	73	38,175	14,460	52,636	252,364
29,701	14,851	44,552	361,288	74	39,206	14,851	54,057	306,420
30,503	15,252	45,755	407,043	75	40,265	15,252	55,516	361,937
31,327	15,663	46,990	454,033	76	41,352	15,663	57,015	418,952
32,173	16,086	48,259	502,292	77	42,468	16,086	58,555	477,507
33,041	16,521	49,562	551,854	78	43,615	16,521	60,136	537,642
33,933	16,967	50,900	602,754	79	44,793	16,967	61,759	599,402
<b>34,850</b>	<b>17,425</b>	<b>52,274</b>	<b>655,028</b>	<b>80</b>	<b>46,002</b>	<b>17,425</b>	<b>63,427</b>	<b>662,829</b>
39,854	19,927	59,781	938,464	85	51,175	19,927	71,102	1,005,301
-	40,930	40,930	979,394	86	-	52,557	52,557	1,057,858
-	42,035	42,035	1,021,429	87	-	53,976	53,976	1,111,834
-	43,170	43,170	1,064,599	88	-	55,433	55,433	1,167,267
-	44,336	44,336	1,108,935	89	-	56,930	56,930	1,224,197

Assumes 2.7% inflation adjustments. Example does not take into consideration taxes or investment earnings on the cumulative benefits. For illustration purposes only.

## Filing a “Restricted Application”

- If filing for benefits before FRA:
  - Must take largest benefit available to you
  - Could be your own, could be your own plus spousal
- If filing for benefits at FRA or later:
  - Can take just your own benefit
  - Can take your own plus spousal (if available)
  - Can “restrict application” to spousal only
    - Allow your own benefit to grow via DRC, then switch to it later



## File & Suspend – and Switch

- Current benefits based on own work history
  - Husband - \$2,000/mo; wife - \$1,200/mo
- Husband files for benefits, but suspends receipt
  - Wife files for spousal benefits at FRA, gets \$1,000/mo (50% of Husband's benefit)
  - Husband defers his benefit to age 70, gets \$2,640/mo, plus inflation
- Wife switches to her own benefit at age 70
  - Her \$1,200/mo has grown to \$1,584, plus inflation

# Cumulative Retirement Benefit – File & Suspend – and Switch

Both Benefits at FRA					File & Suspend - and Switch			
His	Hers	Total	Cumulative	Ages	His	Hers	Total	Cumulative
24,000	14,400	38,400	38,400	66	-	12,000	12,000	12,000
24,648	14,789	39,437	77,837	67	-	12,324	12,324	24,324
25,313	15,188	40,502	118,338	68	-	12,657	12,657	36,981
25,997	15,598	41,595	159,934	69	-	12,998	12,998	49,979
26,699	16,019	42,718	202,652	70	35,243	21,146	56,389	106,368
27,420	16,452	43,872	246,523	71	36,195	21,717	57,912	164,280
28,160	16,896	45,056	291,579	72	37,172	22,303	59,475	223,755
28,920	17,352	46,273	337,852	73	38,175	22,905	61,081	284,836
29,701	17,821	47,522	385,374	74	39,206	23,524	62,730	347,566
30,503	18,302	48,805	434,179	75	40,265	24,159	64,424	411,990
31,327	18,796	50,123	484,302	76	41,352	24,811	66,163	478,153
<b>32,173</b>	<b>19,304</b>	<b>51,476</b>	<b>535,778</b>	<b>77</b>	<b>42,468</b>	<b>25,481</b>	<b>67,950</b>	<b>546,103</b>
33,041	19,825	52,866	588,644	78	43,615	26,169	69,784	615,887
38,769	23,261	62,030	937,201	84	51,175	30,705	81,881	1,075,990
39,815	23,889	63,704	1,000,906	85	52,557	31,534	84,091	1,160,081
-	40,890	40,890	1,041,796	86	-	53,976	53,976	1,214,057
-	41,994	41,994	1,083,790	87	-	55,433	55,433	1,269,491
-	43,128	43,128	1,126,918	88	-	56,930	56,930	1,326,421
-	44,293	44,293	1,171,211	89	-	58,467	58,467	1,384,888

Assumes 2.7% inflation adjustments. Example does not take into consideration taxes or investment earnings on the cumulative benefits. For illustration purposes only.

## File & Suspend Technique

- Can only file & suspend once you reach FRA
  - Filing before FRA locks you into taking benefits (unless you withdraw application within 12 months)
- Only one spouse can file & suspend
  - Can't each take a benefit on the other's work history

## File & Suspend for Singles

- Activate dependent benefits
  - Children
  - Dependent parents

## Additional Benefit of Filing & Suspending

- Claim retroactive lump sum benefit
  - Change your mind about deferring
  - Claim a lump sum payout of benefits back to the date of your suspension
    - Normally limited to 6 months
  - Lose delayed retirement credits
  - Going forward, paid benefits based on age at suspension

## Other Considerations

- **Life Expectancy** – Key determinant, great unknown.
- **Personal Savings** – Enough in investments to provide income in place of Social Security?
- **Legacy Goals** – Someone with substantial legacy goals may wish to begin Social Security earlier to preserve their personal assets.

## Other Considerations

- **Continuing to work** – Social Security can be reduced by employment income
- **Health considerations** – Take Social Security earlier, while healthier and better able to enjoy the extra income
- **Medicare implications**
  - Automatic enrollment
  - HSA considerations

# The Outlook for Social Security



## 2015 Board of Trustees Annual Report

- Short term outlook (2015-2024)
  - OASI funds (retirement benefits) will be “adequate”
  - DI (disability benefits) failed the short-term test for 2014
    - DI fund will be completely exhausted in 4<sup>th</sup> Quarter of 2016
    - Ongoing income could pay 81% of scheduled benefits

# Key Dates for the OASDI Trust Funds

	2009 Report	2010 Report	2011 Report	2012 Report	2013 Report	2014 Report	2015 Report
First year outgo exceeds income excluding interest	2016	2015	Now	Now	Now	Now	Now
First year outgo exceeds income including interest			2023	2021	2021	2020	2020
Year trust funds are exhausted	2037	2037	2036	2033	2033	2033	2034

Beyond 2033, ongoing tax revenue will cover 79% of projected retirement benefits, 73% by 2089

## Possible Solutions

- Increase the payroll tax rate or income base
- Reduce annual benefit amount
- Means testing for benefits
- Extend the retirement age (currently max = 67)
- Increase the amount of benefits that are taxable (current max = 85%)
- Private accounts
- Chained CPI (reduced inflation increases)

# Trustee's Report

- Could resolve long-term deficiencies through **immediate** changes to payroll tax or benefit amounts

	2009 Report	2010 Report	2011 Report	2012 Report	2013 Report	2014 Report	2015 Report *
Payroll tax increase	2.0%	1.8%	2.2%	2.6%	2.7%	2.8%	2.62%
Reduction in benefits for all current & future retirees	13.3%	12.0%	13.8%	16.2%	16.5%	17.4%	16.4%

\* By waiting until 2034, the tax increase would be 3.7% (increasing to 5.0% in 2089), or the benefit reduction would be 21% (increasing to 27% in 2089).

## Helpful Resources

- Social Security Administration website – [www.ssa.gov](http://www.ssa.gov)
- IRS Publication 554, Tax Guide for Seniors – available at [www.irs.gov](http://www.irs.gov)

# Questions

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