SAVVY SOCIAL SECURITY STRATEGIES

Plus, 2 Social Security loopholes that can put $100,000-plus in your pocket

A special report by
The Yield Shark Research Team
Savvy Social Security Strategies

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You can’t read the business news without reading about another financial institution in serious financial trouble. Our nation’s biggest banks, brokerages, and insurers are overleveraged and in financial trouble, and several European nations are so deep in debt that they may default on their government debt.

There is one other US financial institution that is deeply in trouble: our Social Security Administration system.

When Social Security was created in 1935, it covered about half of the population. Many workers were excluded from coverage, and what’s more, the average life expectancy back then was about 60 years.

Source: http://factcheck.org

“We can never insure one hundred percent of the population against one hundred percent of the hazards and vicissitudes of life, but we have tried to frame a law which will give some measure of protection to the average citizen and to his family against the loss of a job and against poverty-ridden old age.”

– President Roosevelt upon signing Social Security Act
Today, few companies are offering pension plans, and Social Security is the only source of guaranteed retirement income for many of today’s retirees.

Nowadays, Social Security covers virtually everyone. The average American is living to age 76. And although the initial 1937 payroll tax rate of 2% (split between employer and employee) has risen to a combined 15.3%, the system still isn’t bringing in enough money to cover everyone.

Remember, Social Security is a “Pay-As-You-Go” system... meaning money comes in and goes out. That poses a big problem, especially with a huge number of baby boomers getting set to retire over the next decade, which means that a smaller pool of contributors will be paying for a larger and longer-living group of recipients.

Even the Social Security Administration’s website says so: “Social Security is not sustainable over the long term at present benefit and tax rates without large infusions of additional revenue. There will be a massive and growing shortfall over the 75-year period.”

The Social Security “tax holiday” that Congress passed in 2010 makes the problem even worse. Workers are temporarily paying 2% less, from 6.2% to 4.2%, in Social Security payroll taxes this year.

The government has to make up the shortfall out of general revenues, and the Congressional Budget Office estimates that the “payroll tax holiday” will cost the government’s general fund $29 billion in fiscal year 2012 (which started Oct. 1, 2011.)

Since every dollar of that will have to be borrowed, the combined effect of the “tax holiday” adds an additional $130 billion to our national debt.
“As the life expectancy of US residents continues to increase, the risk that retirees will outlive their assets is a growing challenge. Today, a husband and wife both aged 65 have approximately a 47% chance that at least one of them will live to his or her 90th birthday and a 20% chance of living to his or her 95th birthday. In addition to the risk of outliving one’s assets, the sharp declines in financial markets and home equity during the last few years and the continued increase in health care costs have intensified workers’ concerns about having enough savings and how to best manage those savings in retirement.”

– United States General Accounting Office; Report to the US Senate Special Committee on Aging

Whoa!

About 10,000 Americans turn 66 every day and make irrevocable decisions on how and when to collect Social Security.

Social Security has detailed rules governing the interplay of work and benefits, and making the right decisions adds tens of thousands of dollars in lifetime benefits.
While income in retirement varies widely by source, Social Security benefits are the foundation of income for nearly all retiree households. In aggregate, Social Security is the largest source of retirement income for households with someone aged 65 or older.

That means that making the right decisions, of which there are many options, on how and when to receive your Social Security payments is a very important piece of your financial security during retirement.

Navigating Social Security benefits takes more than a compass. And don’t expect a lot of help from the Social Security Administration (SSA).

According to the SSA, the vast majority of Americans (about 70%) elected to start receiving Social Security benefits early, between age 62 and their full retirement age.

Full Retirement Age or FRA falls somewhere between age 65 and 67, depending on when you were born.

No two people are alike, so the decision on when to start benefits depends on factors like gender, marital status, income, and health. For some, health concerns or financial necessity force them to take early benefits, but most would likely have been much better off financially by waiting at least to full retirement age, and perhaps as late as age 70, to trigger these paychecks.

Even the General Accounting Office concluded that waiting until age 70 to collect Social Security is the best move for most Americans.

For just about anyone of average health, delaying benefits is a good idea if they can afford it because Social Security’s rules encourage seniors to keep working at least until the full retirement age (FRA) of 66 because benefits are permanently reduced for every year that you file before the FRA.
However, they are permanently increased for every year that you wait, up till the age of 70.

For example, filing at 62 means you retired four years early, and the net effect is a permanent reduction in annual benefits of 25%. On the other hand, if you wait until age 70, your annual benefit will be 32% higher than if you started at age 66.

The reason for these rules is to keep the program actuarially fair, paying roughly equal lifetime benefits to everyone in the program. But delaying does deliver a major boost to monthly income – and it serves as an inducement to work longer and wait to receive benefits.

Source: http://www.socialsecurity.gov

Source: https://www.edwardjones.com
Claiming Social Security retirement benefits early may provide you with more checks, but this approach will likely lock in a smaller lifetime payout, especially for married couples. Starting your benefit at 62 means taking a 25% pay cut relative to your payout at full retirement age (age 66) if you were born between 1934 and 1954. You also have the opportunity to defer your benefit beyond full retirement age, earning yourself an 8% credit for each year you delay your claim. At age 70, your income will be 32% higher than at full retirement age and close to double your age-62 benefit after factoring in cost-of-living adjustments.

How long will it take for this larger, delayed paycheck to make up for the years of benefits you could have received if you started collecting early? Not long. You will break even at about age 77. Live beyond this age, and you will have locked in a higher total payout that could mean hundreds of thousands more in retirement income over your lifetime.

Plus, Social Security benefits are automatically adjusted for inflation.

**Working While Collecting Social Security**

If you decide to work before FRA (full retirement age) and collecting Social Security, your benefits will be temporarily reduced by the Retirement Earnings Test (RET).

The people running Social Security feel that people who work should not collect full benefits, but only people who retire before their full retirement age must pass this test.

For the purposes of the RET test, only wages from employment count as income. You don’t have to include any government or military benefits, investment earnings, interest, pensions, annuities, rental income, or capital gains when calculating the RET test.

You can work and receive Social Security payments at the same time. However, your monthly benefit can be reduced if your wage income is high enough. Your Social Security benefits will be reduced under two levels of RET rules:

- **People** between ages 62 and the year they reach full retirement age will have $1 of benefits withheld by Social Security for every $2 earned in excess of their allowable-earnings threshold. The allowable-earnings threshold was $14,640 in 2006. It is adjusted every year by Social Security based on a formula called the National Average Wage Index (NAWI). The new threshold information is released in the month of October, prior to the year it will be in force.

- **During the year you reach your full retirement** you will only have $1 of Social Security benefits withheld for every $3 earned above the allowable-earnings threshold. The threshold is $38,880 and will be adjusted every year by Social Security’s NAWI.

Once you reach full retirement age, you can work as much as you like without impacting your Social Security benefits. There are no earning limitations once you reach full retirement age.
Example: You can start receiving Social Security as young as 62, but if you continue to work, $1 will be deducted from benefit payments for every $2 that you earn over $14,640.

This will continue until the year you reach full retirement age, when the threshold increases to $38,880 and Social Security only takes $1 for every $3 you earn until your birthday.

Although this is often described as a penalty, the withheld benefits are added back to your benefits after you reach 66, using a complex actuarial formula.

Social Security and Taxes

Your Social Security benefits may be partially taxable depending on how much you earn from other sources.

For most retirees, only 50% of their Social Security benefit will be subject to income tax, though up to 85% of the benefits may be taxable for higher-income recipients.

The actual IRS formula takes your combined income and applies several tests to it to determine what portion of your Social Security benefits will be subject to income taxes.

- If you are married and your combined income falls between $32,000 and $44,000, then up to 50% of your Social Security benefits may be taxable. For singles, the threshold is $25,000 for 50%.
- If you are married and your combined income exceeds $44,000, then up to 85% of your Social Security benefits may be taxable. For singles, the threshold is $34,000 for 85%.

The definition of “income” to determine whether you will pay taxes on part of your Social Security may surprise you. This includes non–Social Security sources of taxable income, such as pensions, wages, interest, and dividends, and even interest from tax-free municipal bonds!

Married couples can coordinate these decisions to boost benefits through smart navigation of Social Security’s survivor and spousal benefits rules.

Worksheets in IRS Publication 915, Social Security and Equivalent Railroad Retirement Benefits, will help you compute the tax.

Spouse and Survivorship Benefits

The survivor rules permit widows to receive up to 100% of a deceased spouse’s benefit or her own benefit, whichever is greater; the spousal rules permit receiving the greater of her own benefit or up to half of a living spouse’s benefit.

The survivor rule has a very simple implication for retirement timing decisions: couples
usually benefit when the spouse with the higher lifetime earning history (which translates into a bigger Social Security check) delays filing.

That’s most often the man because men can expect their wives to outlive them. A delayed filing by the higher-earning husband usually sets the stage for the widow to receive a higher benefit down the road, after his death.

**Two Social Security Secrets That Are Worth Thousands of Dollars in Your Pocket**

**Social Security Secret #1:**
**Filing a restricted application.** Here is an under-utilized but perfect legal way for a married couple to increase their Social Security payments.

Scenario: Dick is 66 and eligible to collect the maximum monthly Social Security benefits of $2,100. However, he is still working and doesn’t need the money. So he plans on delaying his benefits until he is 70, which would ultimately raise his benefit amount and make him eligible for the government’s 8% a year bonus, or credit, bringing his monthly benefit up to $2,772.

His wife, Jane, is 66 and has been collecting Social Security since she was 62. She gets less than the $1,750 a month she would have gotten had she waited until she was 66.

What’s the secret? Dick is allowed to collect half of Mary’s benefit – $875 a month – from when he is 66 to 70. That comes to $42,000 for the four years. By filing a “restricted application,” Dick gets access to his Jane’s benefits.

For those to whom the situation applies, disabled and minor children (up to age 16) are also eligible to receive half of a parent’s retirement benefits.

**Social Security Secret #2:**
**File and suspend (also known as file and re-file later).** This little-known maneuver known as a “file and suspend” can put tens of thousands of extra dollars into your pocket. Legally!

This is a strategy for when a higher-earning spouse wants to keep working and delay his/her benefits to keep accruing credits toward a larger Social Security benefit.

The lower-earning spouse, however, files for spousal benefits on the higher-earning spouse’s record.

Here’s how the “file-and-suspend” works:

1. The higher-earning spouse files for benefits at his FRA but immediately files a notice to suspend benefits.
2. The lower-earning spouse elects to receive spousal benefits.

3. The higher-earning spouse continues to accrue higher payments for whatever point he elects to begin receiving benefits.

Let’s put some numbers to this strategy. Take the same set of facts as above, except Jane is also 66 and only gets $100 a month in benefits. If Dick wanted to wait until he was 70 to collect benefits, Jane would get her $100 and he would get $50 a month from filing a restricted application.

Or, instead of doing that – and here is the secret – as soon as Dick turns 66, he can file for his own benefits and suspend them immediately. Once he does that, Jane is eligible for spousal benefits based on Dick’s benefits. Jane can get up to one-half of Dick’s full retirement age benefit of $2,100 a month. So she goes from $100 a month to $1,050 – an extra $950 a month or $45,600 over that four-year period.

### 5 Key Factors for Maximizing Social Security

**Longevity:** Your health and longevity is an important factor when making the decision when to start collecting benefits. Nobody has a crystal ball, but your family history and current health should be considered. In general, delaying benefits until age 70 means you have reached an age between 77 and 82 in order to break even, depending on your projected investment returns.

**Marital Status:** If you’re married, you have several options. Do one or both spouses work? Does one spouse earn substantially more than the other? How large is the age difference?

**Working Status:** In 2012, if you take benefits early and make over $14,640 per year, Social Security will take back $1 for every $2 earned over the limit. This will continue until the year you reach full retirement age, when the threshold increases to $38,880 and Social Security only takes $1 for every $3 you earn until your birthday.

**Taxes:** Currently, up to 85% of Social Security benefits may be taxable, depending on the recipient’s Adjusted Gross Income. There is no age forgiveness when it comes to paying taxes on benefits, so it’s extremely important to keep income thresholds in mind to minimize tax exposure.

**Financial Condition:** The reason many people take benefits early is that they haven’t accumulated money elsewhere in order to live. For those that have the means to wait, they’ll earn roughly 8% on their yearly benefit each year they delay receiving benefits until age 70. Calculate your income from other sources, retirement accounts, investment assets, and pensions, to support you until you do start collecting benefits.

Take your time to examine all of your options.
No matter how rich you are or how many dollars you have accumulated, you have paid into Social Security for years, and maximizing the amount you get back from it is just good financial sense.

Check out the Social Security Administration webpage.

If you use the calculator on the Social Security Administration’s website to determine your projected Social Security benefits during retirement, you’ll get three data points: the monthly amount you can expect to receive at your full retirement age, the larger monthly figure you’d get if you delay drawing benefits until age 70, and the sum you can collect at age 62, the earliest age at which you can begin collecting a check.

Go to [http://www.socialsecurity.gov/estimator/](http://www.socialsecurity.gov/estimator/)