

# Understanding Social Security Benefits

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## The Gervais Group

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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
- Outlook for Social Security

## Social Security Eligibility

- Once you have 40 quarters of earnings history, you are eligible for benefits
  - For 2014, you earn one quarter for each \$1,200 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?

When to start benefits?

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
  - 2014 maximum - \$117,000
  - Check your earnings history for accuracy
- Worker with maximum income each year would earn maximum benefit
  - \$2,642/month for 2014 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



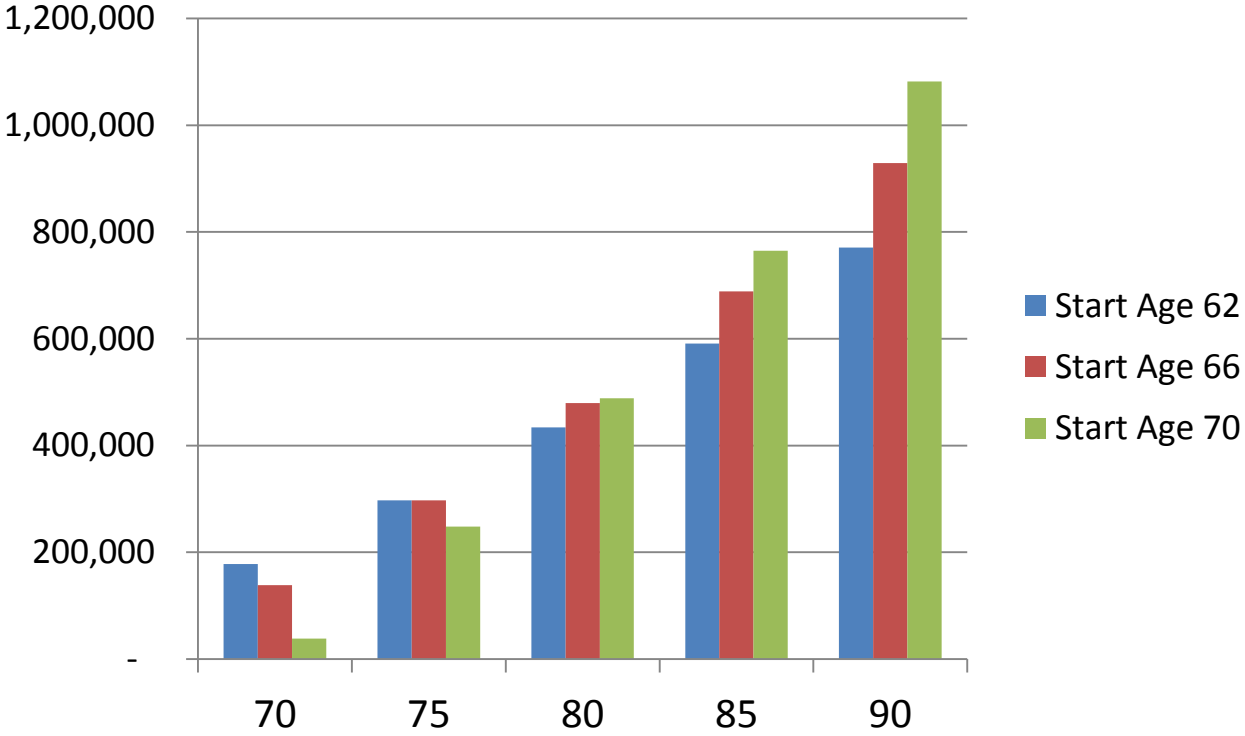
## When to Begin Taking Benefits

- 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 2013 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



## Working While Receiving Social Security

- 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 2014 = \$15,480
  - Benefits reduced by \$1 for every \$2 over that amount
- Monthly earnings test applies in the year of retirement
  - $\$15,480 / 12 = \$1,290$

## Working While Receiving Social Security

- Example:
  - Begin taking benefits at age 64
  - Earn \$25,000 during the year, plus receives \$12,000 in Social Security
  - Excess earnings = \$9,520 ( $\$25,000 - 15,480$ )
  - Lost benefits = \$4,760 ( $\$9,520 / 2$ )
  - Net benefit = \$7,240 ( $\$12,000 - \$4,760$ )

## 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%

## How Much of Your Net Benefit is Taxable?

- 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
- 29 states fully or partially exempt benefits from income tax
  - AL, AZ, AR, CA, DE, GA, HA, ID, IL, IN, KY, LA, ME, MD, MA, MI, MS, NJ, NY, NC, NE, NH, OH, OK, OR, PA, SC, VA and WI
- 8 others have no state income tax
  - AK, FL, NV, SD, TN, TX, WA and WY

# Benefit 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

# Planning Strategies

- File & Suspend
  - Married couples
  - Single individuals
- Restricted Application
  - Voluntarily choose a lower benefit for a period of time

## 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				Ages	File & Suspend			
His	Hers	Total	Cumulative		His	Hers	Total	Cumulative
24,000	12,000	36,000	36,000	66	-	12,000	12,000	12,000
24,672	12,336	37,008	73,008	67	-	12,336	12,336	24,336
25,363	12,681	38,044	111,052	68	-	12,681	12,681	37,017
26,073	13,036	39,109	150,162	69	-	13,036	13,036	50,054
26,803	13,402	40,205	190,366	70	35,380	13,402	48,782	98,835
27,554	13,777	41,330	231,696	71	36,371	13,777	50,147	148,983
28,325	14,163	42,488	274,184	72	37,389	14,163	51,552	200,534
29,118	14,559	43,677	317,861	73	38,436	14,559	52,995	253,529
29,933	14,967	44,900	362,761	74	39,512	14,967	54,479	308,008
30,772	15,386	46,157	408,919	75	40,618	15,386	56,004	364,012
31,633	15,817	47,450	456,368	76	41,756	15,817	57,572	421,585
32,519	16,259	48,778	505,147	77	42,925	16,259	59,184	480,769
33,429	16,715	50,144	555,291	78	44,127	16,715	60,842	541,611
34,365	17,183	51,548	606,839	79	45,362	17,183	62,545	604,156
<b>35,328</b>	<b>17,664</b>	<b>52,991</b>	<b>659,830</b>	<b>80</b>	<b>46,633</b>	<b>17,664</b>	<b>64,296</b>	<b>668,452</b>
40,558	20,279	60,838	947,893	85	53,537	20,279	73,816	1,017,968
-	41,694	41,694	989,587	86	-	55,036	55,036	1,073,004
-	42,861	42,861	1,032,448	87	-	56,577	56,577	1,129,581
-	44,062	44,062	1,076,510	88	-	58,161	58,161	1,187,742
-	45,295	45,295	1,121,805	89	-	59,790	59,790	1,247,532

Assumes 2.8% inflation adjustments. Example does not take into consideration taxes or investment earnings on the cumulative benefits. For illustration purposes only.

## 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
24,672	14,803	39,475	77,875	67	-	12,336	12,336	24,336
25,363	15,218	40,581	118,456	68	-	12,681	12,681	37,017
26,073	15,644	41,717	160,172	69	-	13,036	13,036	50,054
26,803	16,082	42,885	203,057	70	35,380	21,228	56,608	106,662
27,554	16,532	44,086	247,143	71	36,371	21,822	58,193	164,855
28,325	16,995	45,320	292,463	72	37,389	22,433	59,822	224,677
29,118	17,471	46,589	339,052	73	38,436	23,062	61,497	286,175
29,933	17,960	47,893	386,945	74	39,512	23,707	63,219	349,394
30,772	18,463	49,234	436,180	75	40,618	24,371	64,990	414,384
31,633	18,980	50,613	486,793	76	41,756	25,053	66,809	481,193
<b>32,519</b>	<b>19,511</b>	<b>52,030</b>	<b>538,823</b>	<b>77</b>	<b>42,925</b>	<b>25,755</b>	<b>68,680</b>	<b>549,873</b>
33,429	20,058	53,487	592,310	78	44,127	26,476	70,603	620,476
39,454	23,672	63,126	946,192	84	52,079	31,247	83,326	1,087,600
40,558	24,335	64,893	1,011,086	85	53,537	32,122	85,659	1,173,260
-	41,694	41,694	1,052,780	86	-	55,036	55,036	1,228,296
-	42,861	42,861	1,095,641	87	-	56,577	56,577	1,284,873
-	44,062	44,062	1,139,703	88	-	58,161	58,161	1,343,034
-	45,295	45,295	1,184,998	89	-	59,790	59,790	1,402,824

Assumes 2.8% inflation adjustments. Example does not take into consideration taxes or investment earnings on the cumulative benefits. For illustration purposes only.



## 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

## 2014 Retirement Benefits

- 1.5% increase in benefits for 2014
  - Third consecutive increase after two years of no increases
  - Average increase since 1975 – 4.03%
    - 2.83% average since 1983

## 2014 Board of Trustees Annual Report

- Short term outlook (2014-2023)
  - OASI funds (retirement benefits) will be “financially adequate”
    - Beginning in 2020, the cost of the program is projected to exceed income
  - DI (disability benefits) failed the short-term test for 2014
    - DI fund will be completely exhausted by 2016

## Key Dates for the OASDI Trust Funds

	2011 Report	2012 Report	2013 Report	2014 Report
First year outgo exceeds income excluding interest	2011	2011	Currently	Currently
First year outgo exceeds income including interest	2023	2021	2021	2020
Year trust funds are exhausted	2036	2033	2033	2033

- Beyond 2033, ongoing tax revenue will cover 77% of projected retirement benefits, 72% by 2088



## 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

	2011	2012	2013	2014
Payroll Tax Increase	2.2%	2.6%	2.7%	2.9%*
Reduction in Benefits	13.8%	16.2%	16.5%	17.4%*

\* By waiting until 2033, the tax increase would be 4.2% (increasing to 5.3% in 2088), or the benefit reduction would be 23% (increasing to 28% in 2088).

## 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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