Reilly Financial Advisors

Wealth Strategies

Social Security

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Wealth Strategies: **Social Security**

Deciding how and when to take Social Security can add undue stress to an already highly stressful time. While you are transitioning, or planning how to transition, into retirement, you have the added pressure of solving the Social Security riddle. There are rules, calculations, confusing acronyms, deadlines, and complex strategies all adding up to one not-so-simple decision: how and when to begin taking Social Security benefits.

The Role of Social Security

What is Social Security? We go all the way back to August 1935, when President Franklin Roosevelt signed the Social Security Act of 1935 as part of the New Deal. America was suffering and fighting its way through the Great Depression, and prosperity and financial security seemed unobtainable to most Americans. In order to help ensure economic stability, Social Security was established to provide benefits for retirees, disabled persons, and the families of retired, disabled, or deceased workers. Today, about one in four households benefits from some type of Social Security. Designed as a pay-as-you-go system, the benefits of Social Security recipients are funded by the payroll taxes of current workers.

The Not-So-Basic Rules

There are many complexities within Social Security and a long list of tedious rules to remember. Your Social Security benefit is determined by taking your highest 35 years of earnings and indexing them for inflation. These indexed earning years are added together then divided by 420 (35 years in months). This number is what is known as average indexed monthly earnings (AIME). Once AIME is calculated, the next step is to derive the primary insurance amount (PIA). PIA is the sum of three separate percentages of different portions of AIME. PIA is the benefit amount a person receives at full retirement age (FRA), as explained in more detail below. As of 2020, the maximum Social Security retirement benefit for a worker at FRA is $3,011 per month.

The best way to stay up to date on your Social Security benefit is to create an account at ***www.ssa.gov/myaccount***. This site allows you to keep track of your annual earnings and project what your future benefit will be. While you're there, double check that your earnings history is accurate. You can also make sure your address and personal information are correct in order to receive any important updates.

When Is the Right Time?

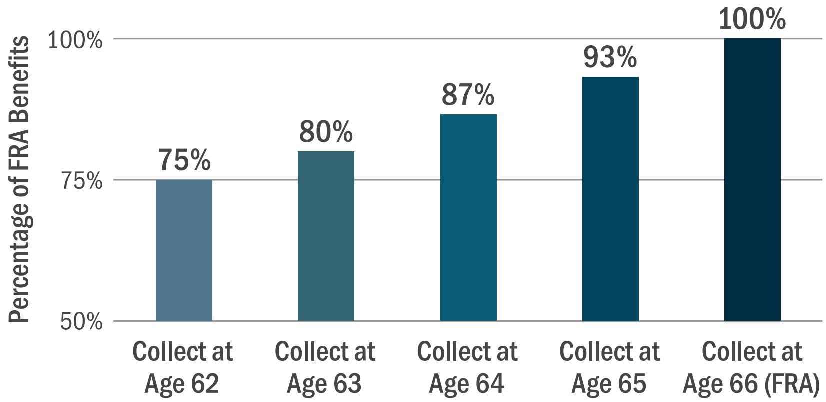
Like most things in the world of finance, there is no one-size-fits-all approach or answer. What is right for one person is likely not right for you and your individual financial situation. Several factors go into making the decision of when to begin taking Social Security. These include your existing savings, current income, and life expectancy. Let's start with the basics.

Full retirement age (FRA) is the age at which you are entitled to your full (unreduced) retirement benefit through Social Security. FRA is based on the year in which you were born, and therefore it's not the same for everyone.

Year of Birth	Full Retirement Age
1937 or Earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943–1954	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 and Later	67

Note: If you were born on January 1 of any year, you should refer to the previous year. If you were born the first day of any month, your benefit at full retirement age is as if your birthday were in the previous month.

Be warned, however, that taking your benefits earlier than FRA reduces your monthly benefit. At right is a chart showing the reduction to your PIA for collecting before you reach FRA (based on someone born between 1943 and 1954).



Source: Social Security Administration (www.ssa.gov). Assumes full retirement age of 66.

The bottom line is this: the longer you wait, the larger each check will be. For most of us, the decision comes down to three factors:

Existing Savings

If you have accumulated sufficient savings and can make do for a few years without Social Security income, it's likely better to wait and let your Social Security check amount grow.

Current Income

If you still have income, you likely don't need that additional check rolling in. And let's not forget that if you're making too much money, some of that check is going to be withheld to pay taxes, thus decreasing the benefit of filing early. For those of you who are still working at age 62, odds are you will want to wait to file until the bulk of your outside income has halted.

Life Expectancy

The greater your life expectancy, the more advantageous waiting becomes, as you will be receiving a larger check for a longer time. Once you know your PIA, a breakeven point can be calculated. Your breakeven point tells you how long you would have to live for the delayed claiming strategy to be more advantageous. For most people, this breakeven point is around 80 years old. In October 2019, the Society of Actuaries reported that a 65-year-old male has a 50% chance of living to age 84.7, while a 65-year-old female has a 50% chance of living to age 87.4. Based on this, if you are of at least average health, delaying your benefits will make sense. However, if your family history and health indicate you might not live to age 80, you may want to consider claiming earlier.

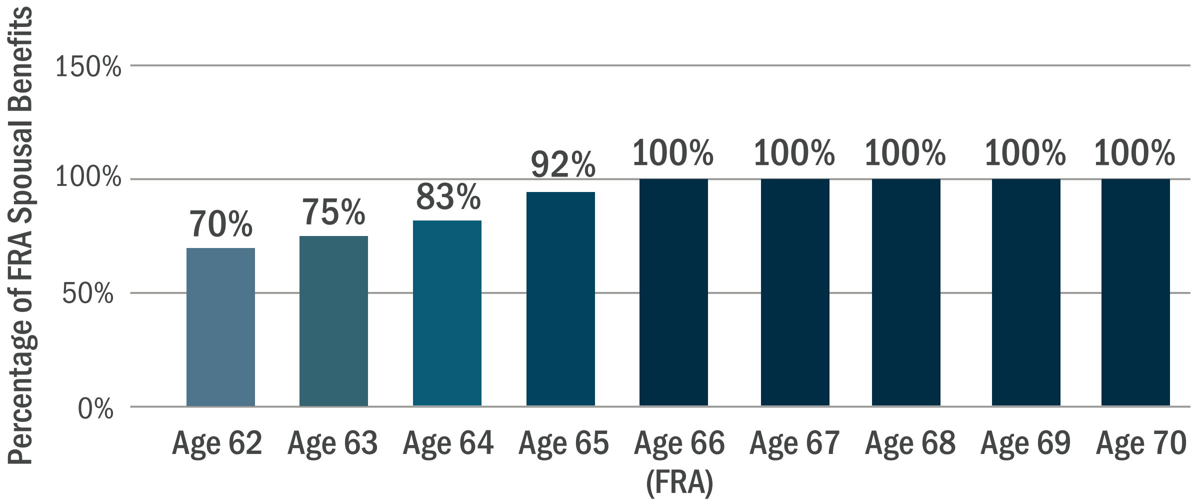
Maximize Your Spousal Benefits

Some households have income levels that vary greatly between the two partners. Perhaps one person took years off to stay at home and raise children. Perhaps one spouse never worked at all. Even though one person may have had limited or no work history, they are still entitled to a Social Security benefit.

The Social Security administration allows for a spousal benefit to alleviate these types of situations. Once a person has reached FRA, they are entitled to up to half of the working spouse's retirement benefit. If the person is eligible for a retirement benefit based on their own earnings history, they will receive 50% of the spouse's benefit amount or 100% their own benefit amount, whichever is greater. But be careful—taking a spousal benefit before FRA, even if the earning spouse is at FRA, reduces the benefit amount.

For example, let's say the working spouse is age 66 (FRA) and begins taking their benefit of $2,500. The non-working spouse decides to begin taking their spousal benefit at age 63 (three years before their own FRA of 66). The benefit the non-working spouse receives will not be $1,250 but rather 75% of $1,250 (for a total of $937.50). If the working spouse takes their own retirement benefit earlier than FRA, not only is their benefit reduced but the spousal benefit is reduced as well; the non-working spouse will only receive 50% of the working spouse's monthly benefit. For many married couples, having at least the person with the higher benefit delay until age 70 is the right choice. This will ensure that if the higher earner dies first, the survivor will have the highest possible survivor benefit.

An often overlooked but very important feature of the spousal benefit is that it is also available to those who have been divorced or widowed. If you are at least 62 years of age and currently unmarried (but were married to your ex-spouse for at least 10 years), you may be eligible to receive half of your ex-spouse's benefit. It's important to note that claiming the spousal benefit from an ex does not affect that ex's claim at all, and he or she will not be notified of your application.



Source: Social Security Administration (www.ssa.gov).

What If I Change My Mind?

Perhaps you filed all your paperwork and began cashing your Social Security checks only to realize you made a mistake. What now? Are you stuck taking the benefit? The answer is no.

If you're under age 70, there are a few options available to you even after making your election to receive Social Security benefits. If you have not yet reached FRA and it has been less than one full year since you began receiving checks, you can simply withdraw from Social Security. Once you have withdrawn, you are eligible to re-enroll at a more advantageous date. Of course, there are a few catches. First, you have to write a large check to the government. Every penny of the benefits you've received must be repaid. This includes checks made out to you, your spouse, or any dependents, living or deceased. It also includes money that you never received, such as money that was withheld to pay for Medicare part B, C, or D as well as any voluntary withholding or garnishment on your benefit checks.

Be extra careful this time around. You can only elect to withdraw once per lifetime.

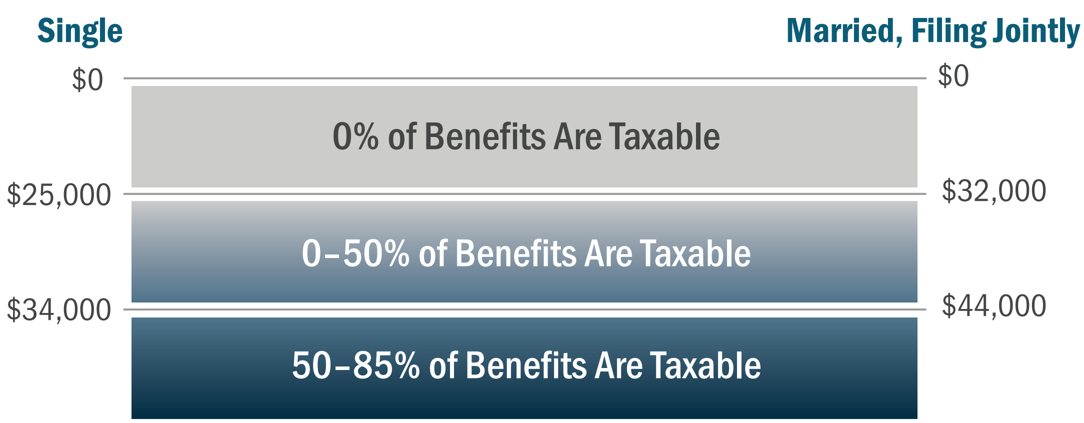
If, on the other hand, you've already reached FRA, you won't be able to withdraw your application; however, you can suspend your benefits. The big benefit to suspending your benefits is that there is no substantial check to write. You owe nothing. The drawback is that when you do begin receiving your checks, the monthly amount will be reduced by the dollar amount you have already received. Just remember that you will be billed separately for Medicare coverage and that failing to make those payments will jeopardize your medical coverage.

The Tax Man

Social Security benefits are not free money. It is important to remember that you may owe taxes on a portion of each check. To determine if you owe taxes on your Social Security benefits, you'll need to determine your provisional income.

There are two threshold points. Over the first, you may owe taxes on up to 50% of your benefit. Over the second, you may owe taxes on up to 85% of your benefit. No one pays taxes on more than 85% of their Social Security benefit. Because of this, $1 of Social Security benefit is worth MORE than $1 withdrawn from an IRA. This is further reason to consider delaying your Social Security benefit, even if it means spending down other assets first.

Provisional Income =
1/2 Social Security Benefits + Modified Adjusted Gross Income



Advanced Tactics

There were two advanced strategies previously available to Social Security recipients that were largely eliminated by the Bipartisan Budget Act of 2015: the File and Suspend strategy and the Restricted Application strategy.

File and Suspend was a strategy that allowed for one spouse to have their benefit amount continue to grow while still generating some Social Security income for the household. This strategy ended in April 2016.

The **Restricted Application** strategy was used to, in effect, "double dip." At FRA, a spouse could make a restricted application, allowing them to collect spousal benefits while allowing their own benefit to earn delayed credits. They could then elect to switch back to their own higher benefit as late as age 70. This strategy is still available for those born before January 2, 1954.

Start Planning Now

Deciding when and how to take your Social Security benefits is an important part of financial planning, and getting the most out of your benefits will go a long way toward securing a successful financial future. It's important to not only know but truly understand the options available to you.

Here are some questions to ask yourself as you move forward:

- **How much can I expect?**
- **When is my FRA?**
- **How can I maximize spousal benefits (if applicable)?**
- **Do any of the advanced strategies work for me?**

Just remember that timing is everything, especially when you have two or more members of a household to consider. It's imperative to plan ahead, and the answers aren't always clear. If you need help figuring out how Social Security can fit into your overall investment portfolio, reach out to your Senior Wealth Advisor or another Reilly Financial Advisors team member today. We would be happy to talk to you about your unique situation and needs as well as how we may be able to assist you.

Reilly Financial Advisors

Reilly Financial Advisors is a fee-only RIA aimed at helping clients both define and achieve their individual financial goals through four unique service offerings:

- **Wealth Building**
  For those still accumulating their investment portfolios
- **Wealth Management**
  For those who have amassed savings and have specific needs associated with their wealth
- **Wealth Legacy**
  For those who have accumulated a significant amount of wealth and face unique wealth transition needs
- **Corporate Retirement Services**
  Providing tailored solutions for plan sponsors and participants

Reilly Financial Advisors, founded in 1999 and headquartered in San Diego, California, serves clients around the United States and in more than one dozen countries worldwide.

As an independent advisor, Reilly Financial Advisors is able to provide clients with the highest level of fiduciary services, making investment decisions based solely on their best interests.

At Reilly Financial Advisors, it is our goal to be clients' first point of contact for all their financial needs, serving as their trusted financial partner for life.

If you would like to make a complimentary appointment to meet with one of our advisors, you may do so **on our website** or by calling us at **(800) 682-3237**.