SOCIAL SECURITY UPDATE

By Linda F Bowen
October 26, 2016

More than 65 million Americans, living in about one in four households, receive Social Security benefits, with about 70% going to retired workers and families and the rest going to disabled workers and survivors of deceased workers. Every month, approximately 10,000 baby boomers retire. Usually one of the first things they think about is social security. Choosing the date to start could be one of the most important financial decisions you will ever make as it will determine the amount you will receive each month for the rest of your life. It is also important to understand how social security works.

The earliest you can start receiving social security retirement benefits will remain age 62 when you will start receiving 75% of the full retirement age monthly benefit for the rest of your life. If you were born between 1943 and 1954, your full (normal) retirement age is 66. If you are born in 1960 or later, your full (normal) retirement age is 67. If you were born between 1955 and 1960, your full (normal) retirement age is between 66 and 67. See the chart at: https://www.ssa.gov/planners/retire/agereduction.html. At full retirement age you will receive 100% of your benefit. If you chose to delay receiving benefits beyond your full retirement age, your benefits will increase a certain percentage depending on the year of your birth. The increase will be added each month from the time you reach full retirement age, until you start taking benefits or reach age 70, whichever comes first.

As a general rule, early or late retirement will give you about the same total social security benefits over your lifetime. If you retire early, the monthly benefit amounts will be smaller to take into account the longer period you will receive them. If you retire late, you will get benefits for a shorter period of time but the monthly amounts will be larger to make up for the months when you did not receive anything.

There are advantages and disadvantages to taking your benefit before your full retirement age. The advantage is that you collect benefits for a longer period of time. The disadvantage is your monthly benefit is reduced. Each person's situation is different, so remember that if you delay your benefits until after full retirement age, you may be eligible for delayed retirement credits that would increase your monthly benefit. Also keep in mind that there are other things to consider when making the correct decision about your retirement benefits

Spousal Benefits

Even if you never worked, you may be able to get spouse’s (you must be legally married) retirement benefits if you are at least 62 years of age. If you start receiving benefits as a spouse at your full retirement age, you will get 50% of the monthly benefit your spouse would receive if his or her benefits started at full retirement age. If you start receiving benefits at age 62, you will get 35% of the monthly benefit instead of 50% because you will be getting benefits for an additional 48 months. If you qualify for benefits on your own record, that amount will be paid first. If the benefit on your spouse's record is higher, you'll get an additional amount on your spouse's record so that the combination of benefits equals that higher amount. Benefits paid to you as a spouse will not decrease your spouse's retirement benefits.

Survivors Benefits

The earliest a widow or widower can start receiving survivor benefits based on age is 60. Widow's or widower's benefits based on age can start any time between age 60 and full retirement age as a survivor. If the benefits start earlier than full retirement age, they are reduced a fraction of a percent for each month before full retirement age. If you receive widow's or widower's benefits *and* qualify for a retirement benefit greater than your survivors benefit, you can switch to your own retirement benefit as early as age 62 or as late as age 70. Also, your unmarried children who are under 18 can be eligible to receive social security benefits when you die.

Divorce and Spousal Benefits

Social security operates with the philosophy that a legally divorced person from a legal marriage may deserve a personal benefit, having been the long-term partner (10 years or longer) of a member of the workforce, legally divorced for a minimum of two years, age 62 or older and unmarried. Social security is gender neutral so the rules apply whether you are a divorced man or woman. Also, any benefits that a divorced spouse might receive would have no effect on the amount of benefits the ex-spouse gets.

Any retirement benefit that you, the divorced spouse, are entitled to receive based on your own work record must be lower than the benefit you would receive from your ex-spouse's record. If your ex-spouse also receives a pension based on work not covered by social security, such as government work, his or her social security benefit on your record may be affected. Basically, you collect whichever benefit is higher. You can't collect both which is an important consideration.

Changes in Social Security in 2016

The biggest change to social security for 2016 is the loss of the file-and-suspend strategy, which is part of the budget deal Congress passed in November 2015. Social security beneficiaries who don't need the money are allowed to suspend their payments and then resume higher payments at a later date. In the past, spouses and dependent children could claim payments based on your work record while your payments were suspended and continued to grow. However, beginning in May 2016, suspending your payments also suspends payments for anyone else receiving payments based on your work.

Some married individuals who are 66 or older have been claiming social security benefits twice. They first collect spousal payments and then later switch to payments based on their own work, which will then be higher because they claimed it at an older age. However, workers who turn 62 in 2016 or later will not be able to claim both types of payments, but must select one or the other. Thus the option of the restricted application is going away.

Taxes and Social Security

Some people have to pay federal income taxes on their social security benefits. This usually happens only if there is other substantial income in addition to your benefits. Taxes are tied to what social security calls *combined income* which is your adjusted gross income, any tax free interest and 50% of your annual social security benefit. You can choose to have federal taxes withheld from your benefits. Also, 13 states tax Social Security retirement benefits: Colorado, Connecticut, Kansas, Minnesota, Missouri, Montana, Nebraska, New Mexico, North Dakota, Rhode Island, Utah, Vermont and West Virginia. Rates and terms of taxation of the benefits vary by state.

Social Security Payroll Taxes—How It Works

After federal and state income taxes, FICA taxes (social security and Medicare) make up the bulk of the other taxes routinely taken out of your paycheck. The majority of the FICA tax revenue goes toward funding the US government's Social Security trust programs, which include: retirement benefits, survivor benefits, and disability benefits. Costs associated with administering the plan also come directly from the trusts, but they're pretty minimal; less than one cent out of every dollar collected pays for administrative costs, according to the Social Security Administration. However, the taxes collected can exceed the cost of current benefits. When this occurs, the money is put in the trusts and invested to pay for future program benefits. These investments allow the US government to essentially borrow against the surplus to fund other parts of the government. This practice, (among other concerns about the social security programs) has many concerned about the longevity of these social security programs. But so far, the government has also repaid its loans from the Social Security trusts — with interest.

According to the annual Trustees Report released June 22, 2016, the long-term outlook for social security old-age and disability benefits, combined remains the same as a year ago, with100% of promised benefits payable until 2034 and then-without changes to the law-79% of promised benefits payable through 2090.

Cost of Living Increases

Social Security annually weighs whether to give beneficiaries a cost of living adjustment (COLA) based on the inflation rate during the third quarter of each year, compared to the last year the COLA was awarded. Beneficiaries didn't receive a COLA for 2016 because the inflation rate had fallen; this was the third time since 2010 they didn't get a bump in payments. The 0.3% COLA increase for 2017 will begin with benefits payable in January.

Mistakes

Mistakes in your earnings record could lead to reduced future benefits. Typically, you have three years, three months and 15 days after the year in which you earned the wages to fix mistakes. Social security makes an exception if, for example, you have documentation of earnings or the error is obvious.

Conclusion

Deciding when to start social security is an individual decision. Living longer gives you time for the higher payment to offset the money you passed up during the delay. Delaying benefits to (full retirement age) or delaying until age 70 will maximize your social security income in retirement. To choose among these options, you must know the actual size of each benefit and weigh factors like immediate cash needs, taxes, continuing to work part-time, and life expectancy. The Social Security Administration provides several online calculators for exploring your situation. You should develop a comprehensive financial plan before making your decision.

Sources:
http://www.aarp.org/work/social-security/info-2016/social-security-benefits-and-the-irs-taxes-hinden.html
http://www.aarp.org/work/social-security/info-2016/start-social-security-benefits.html
http://www.aarp.org/work/social-security/info-2016/divorced-social-security-benefits.html
http://www.aarp.org/work/social-security/info-2016/small-2017-cola-increase-for-social-security-recipients.html
http://www.aarp.org/work/social-security/info-2016/10-surprising-facts-about-social-security.html?intcmp=AE-RET-SOSC-spot2
https://www.ssa.gov/planners/retire/1943.html
https://www.ssa.gov/planners/retire/agereduction.html
https://www.ssa.gov/planners/survivors/survivorchartred.html
https://www.ssa.gov/planners/retire/yourdivspouse.html
https://www.ssa.gov/planners/retire/applying6.html
https://www.ssa.gov/news/cola/