Social Security Myths-Debunked

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Happy Birthday!

On January 1st, 2011, the first baby boomers turned 65. That day is significant because this year, on January 1st, 2012, those same baby boomers reached age 66, which is their full retirement age according to Social Security Administration. Each day, 10,000 boomers are joining them in reaching this milestone. With the biggest wave of retirees now drawing upon their Social Security retirement benefits, we are receiving more questions about Social Security benefits than ever before. When should I begin claiming benefits? Is the system going broke? Is it a big enough piece of my financial plan to waste brain cells thinking about it? After a lot of research, it was very apparent that there is a lot of misinformation about Social Security out there. So here it is, folks: the article to set you straight!

Myth #1: The system will be broke by the time I begin receiving benefits.

Yes, the Social Security system is broken. The costs of current retirement benefits being paid are currently more than the contributions to the system by members of the labor force.

We all know with simple math that this path isn't sustainable over the long haul. The 2011 OASDI Trustees report tells us that total income on trust fund assets, including contributions from the current labor force and interest on trust fund assets, will be sufficient to cover annual costs until 2023. Then, the trust fund is projected to be drawn down until assets are exhausted in 2036. At that point, only current contributions would be paying for benefits, which is projected to allow for 77% of scheduled benefits to be paid through 2084 and then 74% of scheduled benefits starting in 2085.

So what does all this mean? Although the math isn't working out for the long haul, for current baby boomers, it does not appear that retirement benefits are in jeopardy. Any changes made to the system will likely be phased in gradually and could range from a change in the benefit calculation for future retirees, an increase in payroll taxes for current workers, or an increase in the full retirement age for future generations.

Myth #2: It's such a small piece of my financial picture that it doesn't really have an impact.

Many of our clients see Social Security benefits as such a marginal piece of their current annual income resources, that they risk ignoring the significant role it can play in their overall financial success. However, because Social Security retirement benefits last for life and increase annually with inflation, the lifetime value of this asset can be substantial. For instance, a baby boomer who turns 66 this year and begins taking $2,513/ month will…

Collect Benefits for...	Lifetime Value of Benefits Received in Future Dollars...
10 Years	$342,000
20 Years	$794,000
30 Years	$1,389,000

* Assumes Annual COLA of 2.8%

With average life expectancy increasing, it is likely that an individual could potentially collect benefits for 30 years. Looking at the table above, the critical role that may be played by Social Security in your retirement becomes clear, especially for those who have relatively longer life expectancies.

Myth #3: It doesn't really matter when I start claiming benefits.

There used to be a loophole in the law that would allow you to start claiming benefits early at age 62,
and then, if you lived until age 70, you could repay the government all of the cumulative benefits received up until that time and begin claiming benefits as if you had waited to start at age 70 the whole time. That loophole has been closed, which means that the age a retiree begins to claim benefits is even more important as there are no "do-overs".
When you start claiming benefits does matter, as the amount that you receive is directly based upon your age when you file to receive benefits. First, let's get some SSA terminology under our belts. Primary Insurance Amount, or PIA, is calculated using a worker's previous earnings history. This equates to the monthly amount a worker could expect to receive upon full retirement age (FRA). A table reflecting full retirement ages (based on your year of birth) can be found at:
http://www.ssa.gov/retire2/agereduction.htm
If a worker begins to receive benefits prior to FRA, he will receive a discounted amount, as benefits may be received for a longer period of time. For a retiree with a FRA of age 66, the percentage of PIA received along with a dollar amount equivalent based on when benefits start is as follows:

Age	% PIA Received	Monthly Amt.	Monthly w/ COLA	Annual Amt.	An-nual w/ COLA
62	75%	$1,785	$1,785	$21,420	$21,420
66	100%	$2,380	$2,658	$28,560	$31,896
70	132%	$3,142	$3,918	$37,699	$47,019

* Assumes Annual COLA of 2.8%

Using the example above, if we have three retirees, Frank, Sue and John, who are all age 62 with a FRA of 66, what would happen if they each began claiming at different ages?

Let's say that Frank begins at 62, Sue begins at 66, and John begins at 70. Who wins the retirement race? The answer is that it all depends on when they stop receiving benefits, or die. The summary for this example is as follows:

	Cumulative Benefits		
Death at Age	Frank (62)	Sue (66)	John (70)
70	**$215,843**	$168,662	$47,019
80	$527,798	$584,602	**$596,060**
90	$938,969	$1,132,831	**$1,319,722**
95	$1,191,263	$1,469,223	**$1,763,759**

* Assumes Annual COLA of 2.8%

Although it's unlikely that a client can tell us exactly when they plan to stop receiving benefits, we'd like to plan on them receiving them longer than not. You'll notice from chart above titled "Cumulative Benefits," that each year of deferral after reaching FRA currently earns the retiree an 8% credit to his or her benefit.

Couple this increase with the fact that it is currently also applied to any COLAs that are announced during the time period of delay and the increase in annual benefits received at age 70 versus 62 is astonishing. Plus, receiving benefits at age 70 allows you to insure yourself against longevity risk. If you're a married retiree, and your spouse will ultimately be claiming your benefit once you are gone, the longevity protection transfers to the surviving spouse as she will also receive the increased benefit (due to delayed retirement credits).

Conclusion

We believe that Social Security retirement benefits represent a valuable asset to the retiree. The decision on when to take benefits is a meaningful one and shouldn't be taken lightly. There are several factors that should be considered when making the social security decision, particularly if you are married, divorced, or a surviving spouse. Several strategies can be employed to help maximize the benefits received over one's lifetime and your individual circumstances impact this decision, that once made, is irrevocable. It's usually not a simple, one-size-fits all solution and you should consult your Wealth Manager to discuss your options.

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This information is based on our understanding of the current Social Security regulations and as these rules are complex and subject to change, please consult with an advisor of your choice prior to implementing any strategy regarding your Social Security payments.

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