Social Security Planning Strategies

Basic Social Security Planning Strategies

One of the biggest decisions a retiree and their family will face is when to start collecting Social Security retirement benefits. There are several basic issues that every worker should consider to help determine the appropriate age.

Continuing to Work While Receiving Benefits

While workers are eligible to begin benefits at age 62, many find that they are continuing to work well beyond that age. Until a worker reaches Full Retirement Age, income earned as an employee or while self-employed can greatly reduce, and even eliminate, retirement benefits. Once a worker reaches FRA, however, that person can have unlimited earnings and not see his or her Social Security benefit reduced. While the FRA varies based on your year of birth, it is generally between ages 65 and 67.

If a worker retires early, starting Social Security can be an easy way to replace a portion of that lost income stream. Immediate replacement of income should be weighed against the permanent reduction that takes place by taking a benefit before full retirement age.

If a worker decides to stop working yet defers benefits until a later age, the worker should also consider whether or not they have other income that can provide support until Social Security benefits are collected.

Health/Family History

The general rule of thumb on when to start receiving Social Security benefits is that the longer you expect to live, the better off you are deferring the start of your payments. If a worker or retired individual is in relatively poor health and expects his or her life expectancy will be shorter than average, it will likely be beneficial to start receiving Social Security benefits as soon as possible. On the other hand, individuals in relatively good health should consider delaying benefits as long as possible, as the likelihood of that person living the necessary number of years to collect more from the larger annual benefit is greater. Family health history also comes into play in this decision.

Other Retirement Income Sources

Having other sources of retirement income beyond Social Security can allow a retiree to defer the start of benefits, which can ultimately lead to a larger annual benefit. For example, personal investment accounts, an employer pension, or even part-time work during retirement can all help bridge the expense gap during the early years of retirement. When using investment accounts as an income source while deferring Social

Security, there is an opportunity cost to consider. On the one hand, using personal savings in the early years of retirement allows you to take advantage of the delayed retirement credits you receive for deferring Social Security beyond your Full Retirement Age. On the other hand, perhaps that delayed retirement credit will be less than the investment return you could have earned on your personal savings Unfortunately, there's no way to predict which option will provide you the best return. In addition, using personal savings sooner also eliminates liquidity that otherwise would be available for any unexpected expenses that may arise in the future.

Other Family Members May Be Entitled to a Benefit

A spouse, minor or disabled children, and dependent parents can all potentially be eligible to collect benefits based on one worker's earnings history. If that worker begins collecting a Social Security benefit, other family members may also be entitled to receive benefits, up to the family maximum. Taking benefits early and allowing other family members to receive benefits, even if for a relatively short time, could be more advantageous than deferring retirement and collecting a larger annual benefit later. Receiving more early has to be weighed against waiting and receiving a higher amount later along with a potentially reduced survivor benefit. It is important to consider the circumstances of each particular family's situation carefully before a decision can be made regarding when to begin benefits in this case.

Oftentimes, taking a benefit before full retirement age just to trigger dependent benefits does not lead to the highest cumulative benefit received by the family, due to the lifetime reduction in that individual's benefit coupled with the fact that any widow(er)'s benefit would also be reduced.

Medicare Considerations

- **Automatic Enrollment in Medicare.** If someone is collecting Social Security and have also attained age 65, they will automatically be enrolled in Medicare Parts A (hospital insurance) & B (coverage for doctor visits). While an individual can decline Part B if they have coverage through another provider, they are required to be enrolled in Part A at this point. While the vast majority of people do not have to pay a monthly premium for Part A, if they have a Health Savings Account through an employer plan, they will no longer be eligible to make contributions to that plan (employee or employer).
- **Hold Harmless Rule.** There is a special rule for Social Security recipients, called the "hold harmless rule," that ensures that Social Security checks will not decline from one year to the next because of increases in Medicare Part B premiums. The hold harmless rule applies to most, but not all, Social Security recipients. Most people who receive Social Security disability or retirement benefits and Medicare Part B (coverage for doctor visits) are eligible for protection under this rule. Whether this rule comes into play in a particular year depends on the amount of COLA and the Medicare Part B premium increase. To receive this protection, you **MUST** have your Medicare Part B premiums withheld from your Social Security check.
  - Individuals who **do not** qualify for the hold harmless provision include:
    - New Medicare beneficiaries,

- Higher-income beneficiaries (modified adjusted gross income greater than $85,000 for individuals and $170,000 for couples), and
- Beneficiaries whose Part B premiums are paid by the state through one of the Medicare Savings Programs (MSPs) due to Medicaid eligibility.

Advanced Planning Strategies and Opportunities

The complexity of the Social Security retirement system can make determining when you receive a retirement benefit, and which benefit to take, seem overwhelming. The following planning ideas lay out some more advanced and lesser-known strategies that have been used successfully to help a worker and his or her family maximize their Social Security benefits over a lifetime.

The "File and Suspend" Strategy for Couples Who Have a Large Income or Age Discrepancy

One strategy to maximize Social Security retirement benefits for a married couple applies when one spouse has earned substantially higher income over their lifetime than the other spouse, or when there is a several year gap between the couple's ages. The Senior Citizens' Freedom to Work Act of 2000 allows a worker to "file and suspend" Social Security benefits once that person reaches his or her full retirement age. This allows the lesser earning spouse to collect spousal benefits early, and allows the higher earning spouse to continue working and defer benefits beyond full retirement age—enjoying an 8% delayed retirement credit to his or her benefit between full retirement and age 70. Once the higher earning spouse stops working, this higher benefit is then locked in for both of their lives. In addition, if the higher earning spouse predeceases the lesser earning spouse, the lesser earning spouse's smaller benefit steps-up to the deceased spouse's larger benefit.

A Strategy for Couples Who Have Similar Incomes

If a married couple has earned similar incomes over their lifetimes and their Social Security benefits would be comparable at the same age, a worker could file for only spousal benefits at full retirement age and delay the start of their own, higher benefit based on their earnings history. Later, they could switch to their own benefit based on their earnings history and would then be able to collect that higher benefit for their lifetime.

- **Example**: A husband and wife are both 66 years old and each is entitled to receive a monthly retirement benefit of $1,500 at that age. If she decides to retire and he wants to continue working, he can apply for spousal benefits based on her earnings history, which would be worth $750 per month in this example. He can then delay claiming a retirement benefit based on his earnings history until up to age 70. If he waited until age 70, his monthly benefit would be approximately $2,000. If he would predecease her, her survivor's benefit would also be $2,000, which she could continue receiving for the rest of her life.

It is important to note that if either a spousal benefit or a benefit based on a worker's own work history is taken before full retirement age, a permanent reduction is applied, even if they were to switch from one benefit to the other at some point in the future. The benefit can still increase, often times substantially, but a reduction for starting the benefit before full retirement age still applies.

Opportunity to Change your Social Security Retirement Date ("Do-Over" Option)

Because of the difficulty in picking the right start date for Social Security benefits, some retirees decide to begin their benefits as soon as they're eligible. After a period of time, they realize they would have been better off waiting to start. There are two little known provisions in the Social Security rules allows retirees a "do over" when it comes to their decision on a start date.

Under the first provision, you can **withdraw your Social Security claim**, pay back the total Social Security amount collected (without interest or penalties), claim a tax credit or deduction for any income taxes paid, and then re-file for the larger benefit amount that you would be entitled to at that later age.

Effective December 8, 2010, a retiree is limited to one Social Security application withdrawal per lifetime, and this **withdrawal must occur within 12 months** of the first month of entitlement.

The process for stopping your Social Security benefits and then starting them at a later date is described below:

- A retiree who is currently receiving Social Security benefits would submit the Request for Withdrawal of Application form (Form SSA-521) to the Social Security Administration. This would then stop all retroactive, current, and future benefits.
- The retiree would need to pay back all benefits collected up to that point. The amount that needs to be paid back is simply the total of all benefits received up until that point. No interest or penalties are required to be added to that amount.
- Any income tax that was originally paid on the benefits could be recovered by either claiming a tax credit or an itemized deduction in future years.
- At a future date, the retiree would re-apply for retirement benefits. The benefit received would be based on the retiree's age at that time and also factor in any additional employment income that may have been earned over that time period.

The second option is to **voluntarily suspend** receipt of benefits. This option is only available to individuals that have reached their full retirement age. By suspending benefits, the individual is able to earn delayed retirement credits for the months that their benefit is suspended. The delayed retirement credits are added to the amount the individual was previously receiving. While voluntarily suspending benefits will increase the amount individual was receiving, it will not restore the benefit to their originally-projected age 70 amount. During the period when benefits are suspended, the individual would also need to pay their Medicare premiums another way and would not be eligible for the protection against premium increases offered by the Hold Harmless provision.

Combining a Widow(er)'s Benefit with a Surviving Spouse's Own Retirement Benefit

A widow(er) has the ability to determine the best way to maximize their Social Security benefits by deciding when to take their own retirement benefit and when to take a surviving spouse's benefit. A widow(er) may decide to take the surviving spouse benefit for a period of time and then later apply for a full retirement benefit based on their own earnings history.

For example, a surviving spouse who has worked her whole life could claim the widow's benefit as early as age 60. She could then re-file and replace the widow's benefit with the higher benefit based on her earnings history at any point up until age 70. This higher benefit amount would then last for the rest of her life.

It is also possible to do the opposite and take her own retirement benefit for a period of time and switch to the surviving spouse benefit at a later age. The surviving spouse would not want to make the switch any later than her full retirement age, as the widow(er)'s benefit does not earn delayed retirement credits.

This strategy is typically best when a surviving spouse has an earnings history that would provide a smaller retirement benefit than what the widow's benefit would provide, could still meet their retirement income needs in the early years while taking the smaller benefit, and expects to live at least until their actuarial life expectancy.

If the widow(er) is still working and under full retirement age while collecting benefits, the individual's Social Security benefit (own or survivor's) will be reduced if they earn employment income above the earnings threshold.

Spousal Benefit vs. Widow(er)'s Benefit when Re-Marriage Occurs

There is an advantage to being able to receive a widow(er)'s benefit when compared to receiving a spousal benefit. Part or all of a spousal benefit could be lost if the divorced spouse's new spouse is under full retirement age and works, earning more than the Social Security limits. The widow(er)'s benefit, however, is unaffected by the new spouse's earnings.

Strategies for Minor Children when a Parent Begins Collecting Retirement Benefits

Older individuals who are widowers or divorced and later get remarried could marry into a family with younger children or start a second family. If the worker retires and begins receiving Social Security benefits, eligible dependent children will also receive a benefit worth up to 50% of the retired worker's PIA. This benefit can be reduced by the family maximum.

The proceeds received could be used to fund college savings accounts, such as a 529 plan. This could potentially stretch the Social Security benefit even further by offering tax free growth if the proceeds of the account are used for qualified education expenses.

Receiving a Lump Sum Payment After Voluntarily Suspending Benefits

If a worker voluntarily suspends their Social Security benefit at or after Full Retirement Age (FRA), the worker could reinstate suspended benefits, which would allow the individual to receive all of the suspended benefits as a lump sum payment. However, the worker would *not* receive delayed retirement credits from age 66 through their current age. When their benefit resumes, the monthly amount would be reset to their benefit amount at age 66, rather than their current age.

- **Example:** Brad files for Social Security benefits and immediately suspends receipt of his monthly check at age 66. At age 69, Brad becomes ill and incurs a large, unforeseen medical expense. Because of his illness, Brad would now benefit more from receiving a lump sum cash payment than receiving a higher monthly Social Security benefit going forward. Brad chooses to reinstate his voluntarily suspended benefits. This results in Brad receiving a lump sum payment of all benefits he would have collected from age 66-69. Going forward, his monthly Social Security benefit will be based on the amount he would have received at age 66, adjusted for inflation. The cost of receiving the lump sum payment is that he will not receive the delayed retirement credits he would have earned by waiting until age 69 to start collecting benefits.

This option minimizes the risk of waiting to receive benefits. If a retiree chooses to delay claiming retirement benefits in order to earn delayed retirement credits, they run the risk of not living long enough beyond the delayed retirement age to receive enough of the larger payments to make up for missing out on the benefits they would have received at an earlier age. This option allows for a worker to delay receiving benefits in hopes of receiving a higher monthly payment later while also ensuring that a surviving spouse will receive the highest possible survivor benefit, yet still allows for them to change their mind and receive a lump sum payment if their circumstances should change before age 70. For single individuals, this strategy reduces, but does not eliminate the risk of dying prematurely. For married couples, it adds flexibility to their planning strategies if they choose to delay receipt of benefits beyond full retirement age.

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