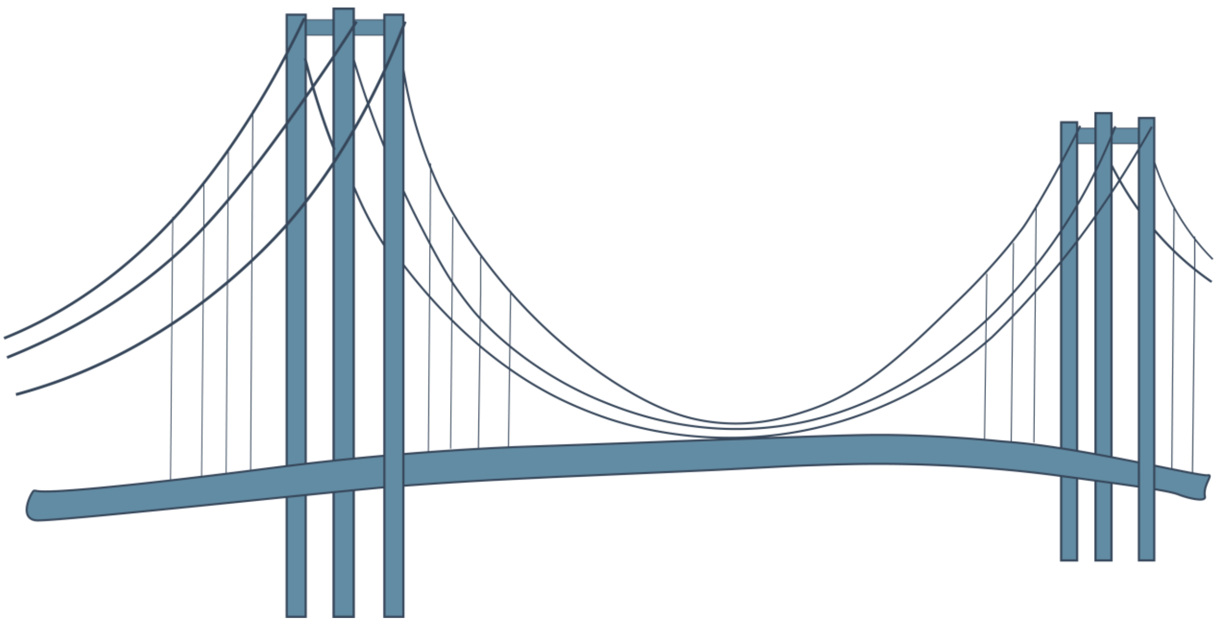
Get The Maximum Benefit from Social Security



RETIREVO

CONTENTS

Introduction to Social Security benefits

As employer-funded pensions become rarer, Social Security is one of the only sources of income (along with certain types of annuities) that you can rely on to continue for as long as you live.

Though Social Security was never meant to supply a person's entire retirement income, longer lives and lower savings rates mean that more people count on their benefit check to finance their retirement. In 2020, the average monthly Social Security benefit for retired workers was $1,543 ($2,596 for couples)[i], and for 50% of retired couples and 70% of retired individuals, this benefit represented at least half their household income[ii].

✓ CHECK YOUR WORK

You can sign up for an online account at the Social Security Association website (ssa.gov) allowing you to view your online work history summary. Compare the amount of income shown for each year that you worked to the total of all Social Security wages” (box 3) from your Form W-2(s) for that particular year. Or, if you were self-employed, compare to total earnings that you reported on your federal Schedule SE for that year.

Several crucial choices -- some of which you'll need to make before you are old enough to be eligible for benefits -- will determine your baseline level of monthly support from Social Security. It's worth taking the time to clearly understand the ramifications of these choices, as you won't be able to revisit them once each deadline has passed.

As you plan a retirement that will be partly funded by Social Security income, here are strategies you can consider to maximize your Social Security benefit.

Increase your earned income before you retire

In order to qualify for Social Security benefits, you'll need 40 credits earned at age 21 or later. This is generally equivalent to 10 years of work, earning at least the minimum required income each quarter. This threshold is $1,470 in 2021 ($1,510 for 2022[i]), with a maximum of 4 credits earned in a year. Social Security benefits are based on wages subject to FICA tax, so any earnings from pensions, annuities, and investments will not count toward your annual income for the purposes of figuring your eventual benefit amount.

$ SAVING STILL PAYS

You may be concerned that contributing pre-tax dollars to a Health Savings Account (HSA) or Individual Retirement Account (IRA) during your working years might reduce the annual earnings amount used in calculating your Social Security benefit. It will not. Income taxes are calculated using box 1 of your Form W-2, which excludes pre-tax contributions to investment and savings accounts such as HSAs and IRAs, whereas Social Security taxes (and retirement benefits) are based on box 3, which does not exclude such contributions.

Once you have earned your 40 credits, you will be eligible for a retirement benefit as early as age 62. However, continuing to work even after you reach your full retirement age could increase your eventual benefit amount. That’s because your monthly benefit is calculated using your highest 35 years of indexed earnings. This calculation is based on your annual earnings up to an earnings cap ($142,800 in 2021 $147,000 in 2022[i]) that is indexed annually for inflation.

If you have earned above the earnings cap ($142,800, indexed annually for inflation), earnings above the cap will not increase your monthly benefit. However, if you continue to work and you earned less than the cap during some of those years, then your current earnings may increase your monthly Social Security payments.

Continuing to work will have the biggest impact for those with fewer than 35 years of income, because the years with no income are counted as zeros when computing your historical average income. Each additional year of earned income will replace one of those zeros, raising your average income and corresponding monthly benefit. Even with an income history of more than 35 years, your current year's earnings may be higher than one of your 35 highest years of indexed earnings, in which case the lower income will be replaced by the higher one and your average will be recalculated, increasing your monthly benefit.

You may choose to work beyond your full retirement age (which will fall between 66 and 67 for those retiring in the 2020's) to increase your eventual monthly benefit. If you need the additional income, you can start receiving Social Security benefits while you continue to work, though this strategy may incur additional taxes. Your 35-year average annual indexed income will be recalculated each year that you have reported earnings, and your monthly benefit amount adjusted accordingly, even while you are receiving Social Security benefits.

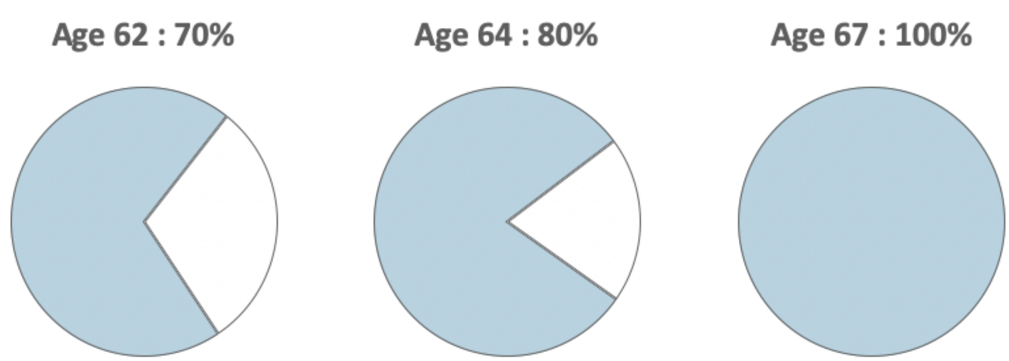
You may choose to claim your Social Security as early as age 62, to supplement your income as you continue working. Although this will reduce the percentage of the full benefit you receive for the rest of your life, changes in your highest-35-year indexed earnings average might still increase your monthly payment from when you began receiving it, and it will be increased by a cost-of-living adjustment each year as well, assuming a COLA is declared.

Also be aware that, before you have reached your full retirement age, earning wages above an annual income threshold ($18,960 in 2021) will cause the Social Security Administration to withhold your monthly benefit checks until they reach a total of $1 for each $2 you earn above that threshold. During the year that you reach full retirement age, your earnings limit is higher and applies to earnings up to the month before you reach Full Retirement Age. In 2021, your earnings limit for the months before full retirement age is $50,520. The Social Security Administration will deduct $1 in benefits for every $3 you earn above that. These withheld benefits will, however, boost the monthly amount you receive at your full retirement age to account for the months that benefits were previously withheld[iii]. Once you reach your full retirement age, you can earn an unlimited amount and still receive your entire monthly benefit.

Delay claiming benefits up to age 70

The age at which you start receiving Social Security benefits influences the formula by which your benefit payment is calculated.

Claiming Social Security Benefits Early for Persons Born 1960 or Later*



* For persons born 1960 or later, full retirement age is 67.

If you qualify for benefits, you can choose to start receiving monthly payments as early as age 62. However, choosing to receive benefits before you reach your full retirement age (which depends on the year you were born) means that you will receive only a portion of the full monthly benefit to which you would be entitled should you wait. The percentage reduction is 5/9 of 1% per month for the first 36 months and 5/12 of 1% for each additional month, up to 60 months (the time period between ages 62 and 67). For a person whose full retirement age is 67, that's a 20% reduction at age 64, or 30% at age 62.

℞ MIND THE GAP

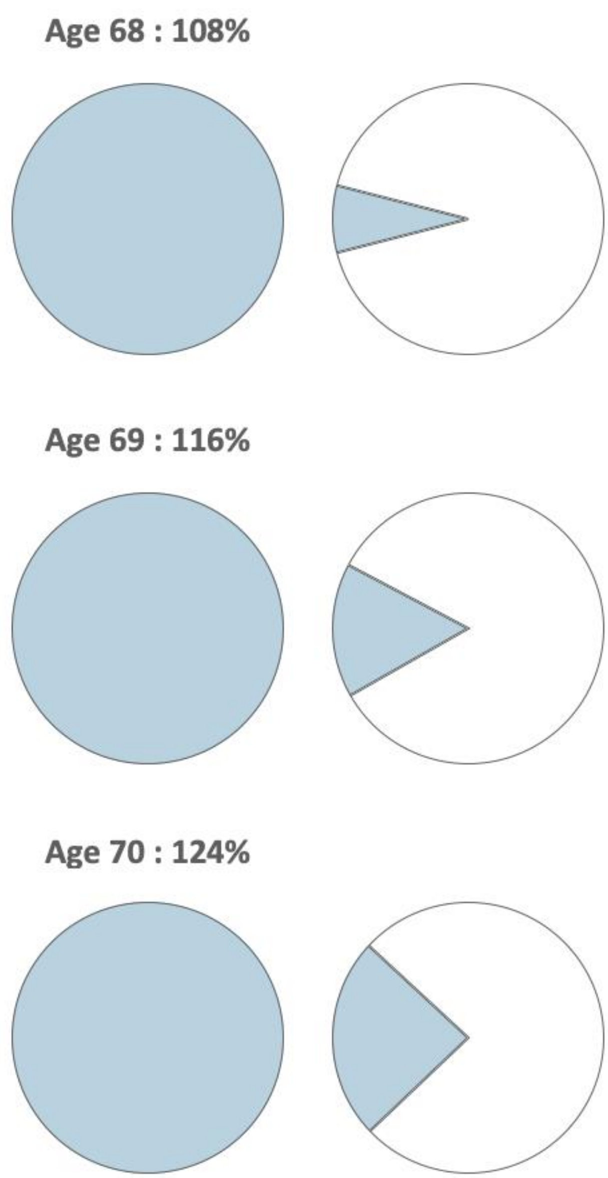
Medical care costs may be a factor to consider if you plan to quit working at age 62 and your employer currently pays for your health insurance. You won't be eligible for Medicare until age 65, so that will leave a period of years during which you will need to cover your own medical costs (including health insurance premiums).

Another option is to delay receiving benefits until after your age of full retirement; in this case, your benefits will be increased by 2/3 of 1% for every month that you delay until you reach the age of 70. This will increase your Social Security benefits by 8% for each 12 months that you delay, up to a maximum of 124% for those born in 1960 and later, and up to 132% for those born 1943 to 1959. Thus, for every 12 months from your full retirement age to age 70 that you delay receiving your benefits, your delayed Social Security will yield an additional guaranteed 8% (or 16%, or 24%) every year throughout your lifetime, and the lifetimes of survivors receiving benefits based on your earnings record.

As an example, if you were born in 1960 or later, and at your full retirement age you happen to qualify for an amount equal to the 2020 average monthly benefit of $1,543, then your monthly payment could range between $1,080 (70% of $1,543) and $1,913 (124% of $1,543), depending on when you choose to claim your benefits.

After the age of 70, there is no financial gain in continuing to delay claiming your benefits. Your benefits will not increase any further, and there is no earnings limit should you also choose to work. This means you can still improve your annual average income and thus raise your baseline benefit, while enjoying the additional income from your Social Security benefits.

Delay Claiming Social Security Benefits for Persons Born 1960 or Later*



* For persons born 1960 or later, full retirement age is 67.

Claim benefits under another person's earnings record

It may be possible for an individual to qualify for benefits under two different earnings records, and perhaps even collect benefits for a period of years under one of those earnings records and then switch to receiving a higher benefit based on the other record. A widowed spouse, for instance, can begin taking reduced Social Security survivor benefits at age 60 (50 if disabled) based on their spouse's earnings record, then switch to their own retirement benefit as late as age 70, if that benefit amount would produce a higher lifetime benefit. The opposite is also true. If a widow or widow's retirement benefit will produce a smaller benefit than the survivor benefit, he/she can choose to first file for their own retirement benefit and then switch over to the survivor benefit at their survivor FRA, which is the point at which the survivor benefit would not be reduced.

Dependent children whose parents have retired, become disabled or died, disabled dependent adults, spouses, and ex-spouses with at least 10 years of marriage prior to divorce, and widows/widowers who were married at least nine months may all be eligible for Social Security benefits based on another person's earnings record. Qualifying factors include the age and marital status of the claimant, and in some cases, whether the primary earner has begun claiming benefits[iv].

Therefore, the choice that you make about when to begin receiving your Social Security benefits could affect not only your own benefit amount but also the benefits available to your spouse and your dependents while you are living, as well as after your death. It's worth carefully considering the alternative approaches, and if you are married, making a joint plan for when each spouse will begin claiming benefits and under which earnings record, in order to maximize your household Social Security benefits.

Spousal Benefit as a Function of Age*

Age at Claiming	Primary Benefit Received	% of Full Primary Benefit	Spousal Benefit Received	Spousal % of Primary Benefit Received **	Spousal % of Full Primary Benefit
Primary is 62, Spouse is 62	$1,080	70.0%	$351	32.5%	22.8%
Primary is 62, Spouse is full retirement age	$1,080	70.0%	$540	50.0%	35.0%
Primary is 62, Spouse is 70	$1,080	70.0%	$540	50.0%	35.0%
Primary is full retirement age, Spouse is 62	$1,543	100.0%	$501	32.5%	32.5%
Primary is full retirement age, Spouse is full retirement age	$1,543	100.0%	$772	50.0%	50.0%
Primary is full retirement age, Spouse is 70	$1,543	100.0%	$772	50.0%	50.0%
Primary is 70, Spouse is 62	$1,913	124.0%	$622	32.5%	40.3%
Primary is 70, Spouse is full retirement age	$1,913	124.0%	$957	50.0%	62.0%
Primary is 70, Spouse is 70	$1,913	124.0%	$957	50.0%	62.0%

* Data in this simplified table are based on the assumption that both parties were born 1960 or later, using the 2020 average retirement benefit of $1,543.

** Spousal Benefit Received will not be reduced below 50% of Primary Benefit Received in cases where the spouse is caring for a qualifying child, except when benefits are subject to maximum allowable family benefit.

The maximum amount you will be able to collect based on a living spouse or ex-spouse's earnings is 50% of their monthly benefit and only then, if the spousal or ex-spousal benefit produces a higher benefit than your own. An exception exists only for individuals born prior to January 2, 1954. In certain cases, these individuals may elect to restrict their claim to spousal benefits only and later switch to their own higher retirement benefit as late as age 70. If you think that this may apply to you, consult with a knowledgeable financial or tax consultant.

The maximum you can collect based on a deceased spouse or ex-spouse's earnings is 100% of the amount they were collecting at the time of their death or what they were entitled to collect. This means that if the deceased spouse earned delayed retirement credits, these too will pass on to the survivor!

Keep in mind that, just like a spousal benefit while both spouses are alive, a survivor benefit taken prior to the survivor's FRA will also be reduced.

Also, unlike benefits that are based on your own earnings history, your spousal benefit or survivor benefit will not increase after you reach full retirement age, so there is no incentive to delay claiming it past that age.

♡ SAVE THE BEST FOR LAST

For a married couple with the ability to "stagger" their claim dates, having the higher wage earner delay taking benefits will maximize the lifetime benefits for both spouses, and could also increase the lower earning spouse's survivor's benefits. Also, each month of delay for the higher earner will yield a larger increase in eventual monthly payments.

If your household needs the income and delaying would present a financial hardship, then even if the need is only temporary, it may make sense for one or both spouses to claim Social Security benefits before full retirement age; one or more partial benefits could boost your household income enough to give you financial stability and peace of mind, and that might be worth forfeiting a higher lifetime income in later years.

For more help with exploring different income scenarios based on multiple beneficiaries and earnings records, you can use the spousal benefit calculator at ssa.gov[v].

Reduce or eliminate tax on Social Security benefits

When making the choice about when to begin claiming your benefits, you may want to consider tax efficiency, or the amount of your Social Security income that you'll keep after paying income taxes on your benefit. In 2020, about 40% of beneficiaries owed federal income tax on some portion of their Social Security income[vi].

→ PAY AHEAD

If you know you'll be taxed, you can choose to have federal tax withheld from your Social Security benefits so you won't be surprised at the end of the year by a large tax bill.

Up to 85% of your Social Security benefit is potentially subject to federal tax. Generally, if your only income is from Social Security, you will fall below the minimum adjusted gross income (AGI) thresholds, but for higher incomes, any portion of your AGI above the minimum threshold will be subject to federal income tax as shown in the following table.

AGI Federal Tax Thresholds*

	individuals	couples
not taxable	$25,000	$32,000
up to 50% taxable	between $25,000 and $34,000	between $32,000 and $44,000
up to 85% taxable	above $34,000	above $44,000

*Adjusted gross income (AGI) is defined by the IRS as net income plus 1/2 your Social Security annual income plus any income from interest, dividends, bonds, and wages. These income thresholds are not adjusted for inflation each year.

If you don't need the money to live on, you could use different strategies to try to reduce your amount of taxable Social Security income. If you have any flexibility in timing your income from different sources, you may be able to reduce your total tax burden. Delaying your initial claim until age 70 and using income from other sources first offers a double incentive, both reducing taxes on your Social Security and increasing your baseline benefit. Another possible strategy would be to time IRA distributions and other income to create alternating years of higher and lower AGI, so that your Social Security will only trip the taxable threshold every other year.

Another potential strategy for reducing your taxable Social Security income is to fund a Roth IRA in your pre-retirement years, then use it as a supplemental tax-free income source during retirement. You may also be able to lower your taxable income with tax-deferred investments, including certain types of annuities.

Keep in mind that federal taxes are not the only taxes to consider. Your Social Security income may be subject to an additional state tax, depending on where you live[vii]. Living abroad in certain countries could exempt you from paying U.S. taxes on your Social Security benefits[viii]. Relocating can therefore affect how much of your Social Security income you are able to pocket, and what kind of lifestyle it funds.

Finally, even if the maximum amount (85%) of your Social Security benefit is subject to taxes, it still compares favorably to income from traditional IRA distributions and 401(k) payouts, 100% of which will be taxed at your current rate.

Disclaimer

The information in this material is not intended as tax or legal advice. Please consult legal or tax professionals for specific information regarding your individual situation. The opinions expressed and material provided are for general information.

Citations

[i] Fact Sheet: 2021 Social Security Changes. Social Security Administration, October 13, 2020. Available at ssa.gov/news/press/factsheets/colafacts2021.pdf

[ii] Fact Sheet: Social Security. Social Security Administration, July 2020. Available at ssa.gov/news/press/factsheets/basicfact-alt.pdf

[iii] For details about these calculations, see "How Work Affects Your Benefits." Social Security Administration Publication No. 05-10069, January 2021. Available at ssa.gov/pubs/EN-05-10069.pdf

[iv] For a full explanation of eligibility rules for spouses, ex-spouses, survivors, and children, as well as strategies for claiming multiple benefits, see "What Every Woman Should Know." Social Security Administration Publication No. 05-10127, January 2021. Available at ssa.gov/pubs/EN-05-10127.pdf . Also see "When to Start Receiving Retirement Benefits." Social Security Administration Publication No. 05-10147, January 2021. Available at ssa.gov/pubs/EN-05-10147.pdf

[v] You can access the Social Security Administration's spousal benefit calculator at ssa.gov/OACT/quickcalc/spouse.html

[vi] "Retirement Benefits." Social Security Administration Publication No. 05-10035, January 2021. Available at ssa.gov/pubs/EN-05-10035.pdf

[vii] The 13 states that tax Social Security income are Colorado, Connecticut, Kansas, Minnesota, Missouri, Montana, Nebraska, New Mexico, North Dakota, Rhode Island, Utah, Vermont, and West Virginia. For a comparison of state-specific tax implications for Social Security income, see Cammenga, Janelle. "Does Your State Tax Social Security Benefits?" The Tax Foundation, August 9, 2020. Available at taxfoundation.org/states-that-tax-social-security-benefits/

[viii] "Social Security and Equivalent Railroad Retirement Benefits." Internal Revenue Service Publication 915. Available at irs.gov/publications/p915