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Social Security – Timing is Everything

While Social Security is not the primary source of retirement income for most Americans, it can serve as an inflation-protected annuity during retirement years. As such, it is important to understand the rules surrounding eligibility and the timing of initiation of benefits. Prior to the passage of the Bipartisan Budget Act of 2015, married couples could benefit from several planning strategies to maximize the receipt of benefits. While this legislation discontinued the availability of these strategies, there are still opportunities to maximize benefits through careful consideration of the timing of electing benefits.

ELIGIBILITY FOR BENEFITS

To be eligible for Social Security benefits, an American worker must pay into the system for 40 quarters or 10 years. The work need not occur in consecutive years and benefits are based on how much was earned during those working years. Aside from earnings, the key determinant of the amount of benefit received is the age at which benefits begin.

Full retirement benefits are payable based upon a person's full retirement age. Full retirement age has slowly been increasing such that for individuals born in 1960 or later, it will be upon reaching age 67. Benefits may be received as early as age 62 or as late as age 70. There will be a reduction in benefits if they are received before full retirement age and, conversely, benefits will be increased if initiated beyond full retirement age.

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DIVERSIFIED TRUST

SPOUSAL BENEFITS

Spouses are also eligible for benefits based upon a working spouse's work history in addition to any benefits they personally accrue. Spousal benefits may not exceed ½ of the working spouse's total benefit. Spousal benefits are only available once the working spouse has filed for his or her own benefits. The recipient spouse must be age 62 or older unless they are caring for a child who is younger than age 16 or is disabled. Spousal benefits are reduced until the spouse reaches his or her full retirement age. A working spouse may file for benefits and then suspend those benefits until a future date to allow greater benefits to accrue. Unlike under prior law, this suspension of the worker's benefits now also suspends the spousal benefit. A spouse will only be allowed to collect a benefit on a worker's record if the worker is actually receiving benefits.

Divorced Spouses

A divorced spouse is entitled to spousal or survivor benefits based on the earnings of their ex-spouse if they were married for 10 years prior to the divorce, has been divorced for at least 2 years prior to applying for benefits and has not remarried prior to age 60. If a divorced spouse remarries after age 60, they may choose the highest benefit among their current spouse and prior spouse(s). Benefits paid to a divorced spouse do not affect the benefits due to a current spouse or children.

Widows and Widowers

Widows and Widowers may begin receiving Social Security benefits at age 60 (age 50 if disabled). Their benefit is equal to the amount their deceased spouse was receiving but will be reduced on a percentage basis if they begin receiving before their own full retirement age. If they are eligible for their own benefit as well, they can receive their full retirement benefit upon reaching their full retirement age or continue with the survivor benefit, whichever is greater.

> **Example:** Husband dies at age 72 while receiving a full retirement benefit of $2,000 per month. Wife is 67 at the time of his death. Since she is at her full retirement age, she can receive his full benefit as a widow. She decides to claim her retirement benefit at age 70 which is equal to $2,500 per month. She will receive the greater of the two benefits at that time.

WORKING AND SOCIAL SECURITY

An increasing number of Americans are working into their retirement years. This does not impact Social Security benefits unless benefits are received prior to full retirement age. For example, if someone begins receiving benefits at age 62 and continues to work while receiving benefits, there is a maximum that can be earned or benefits will be reduced. In 2025, this amount is $23,400. Therefore, for every $2 that is earned in excess of $23,400, Social Security will reduce benefits received by $1. There is a special rule for the year in which the full retirement age is reached. In that year, the earnings limit is $62,160 and benefits are reduced by $1 for every $3 earned in excess of this limit. Once full retirement age is reached, full benefits are paid regardless of earnings received.

If benefits were reduced due to earnings in the years prior to full retirement age, benefits will be increased at full retirement age to reflect the benefits withheld due to the earnings limit.

Special Payments

Payments for work done prior to the receipt of Social Security benefits are not counted toward the earnings limit. Examples of special payments are bonuses, vacation pay, commissions, sick pay and deferred compensation from a nonqualified plan.

TAXATION OF SOCIAL SECURITY

Social Security benefits are nontaxable in very limited situations. Taxability is determined based upon combined income. Combined income is defined as the sum of:

- Adjusted gross income
- Tax-exempt interest
- One-half of Social Security benefits

The table below illustrates the taxable portion of Social security for taxpayers based on their combined income:

	TAXABLE PORTION OF SOCIAL SECURITY	
TYPE OF TAXPAYER	**COMBINED INCOME :: 50%**	**COMBINED INCOME :: 85%**
Single or Head-of-Household	Over $25,000	Over $34,000
Married Filing Jointly	Over $32,000	Over $44,000

For married taxpayers who file separately, 85% of Social Security benefits are taxable regardless of income level.

TIMING OF BENEFITS

As stated earlier, full retirement benefits are payable upon reaching full retirement age. The earliest age at which benefits may begin is 62. For a person whose full retirement age is 67, if benefits are initiated at age 62, there will be a 31% reduction from the full retirement benefit amount. Conversely, if benefits are not initiated until age 70, there will be a 25% premium over the full retirement benefit.

Future social security benefits are adjusted for cost of living adjustments (COLA) as measured by the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). The increase in benefits for 2025 is 2.5%.

Below is an example of the impact of the timing of receipt of benefits assuming a full retirement age of 67 and an annual COLA of 2.4%:

	TOTAL BENEFITS RECEIVED				
INITIAL BENEFIT AMOUNT	AGE	DEATH AT AGE 75	DEATH AT AGE 80	DEATH AT AGE 85	DEATH AT AGE 90
20,700	62	339,650	491,000	661,406	853,265
30,000	67	297,425	492,246	711,594	958,559
37,500	70	238,940	465,741	721,096	1,008,601

As you can see, with a longer life expectancy, it is more advantageous to defer benefits as long as possible.

Married Couples

The timing of benefits for married couples is very complex with several considerations. Factors to consider include:

- the amount of benefits to which each spouse is entitled
- age difference between the spouses
- life expectancy of each spouse

It is critical to weigh all the options prior to age 62 to insure that benefits are maximized for each spouse.

ESTIMATING BENEFITS

The first component in the planning process is to obtain the projected amount of each individual's benefit. The Social Security Administration does make it easy to obtain a current estimate. This can be done by visiting their website at **www.ssa.gov**. Below are the instructions for creating an account and obtaining a statement of benefits:

- Click on Sign In/Up in the top right corner of the home page
- Click on my Social Security
- Click Create an Account and agree to the terms of service
- Click Next and enter your personal information including the creation of a user name and password
- Login using the user name and password created and agree to the terms of service and Click Next
- Click Print/Save Your Full Statement

The Social Security Statement provides details of the estimated benefit at retirement as well as a full record of earnings.

CONCLUSION

While Social Security may not be the primary source of retirement income, it can provide an effective inflation-protected supplement to other cash flow sources. Therefore, careful consideration should be given to the timing of benefits.

Contact us if you have questions or would like assistance with assessing the specific timing and distribution options available to you and your spouse. This paper is intended to be educational in nature and does not replace the need for analysis of individual circumstances.

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