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EDITORIAL & OPINION

The 'when' and 'how' of Social Security benefits can mean thousands

WEALTH MANAGEMENT

BY MONTGOMERY TAYLOR

For most middle income couples, Social Security makes up 20% to 50% of their retirement income–often totaling upwards of $500,000 in lifetime benefits. Obviously, that is a large sum of money for just about anyone. Doesn't it make sense to maximize that asset if you can?

This one decision can impact your retirement by tens of thousands of dollars. For some people, choosing the right Social Security election may be the most important decision of their retirement. How much you receive from Social Security depends on three primary factors: 1) your earnings record, 2) when you elect, and 3) how long you expect to live. Since you can't go back and change your earnings record, and you have minimal control over how long you live, calculating an expected lifetime benefit largely hinges on when and how you elect benefits.

In theory, if you elect early, you will get a smaller benefit for a longer period of time. If you elect later, you will get a larger benefit for a shorter period of time. Single people can do a simple "break-even" analysis to determine whether to take early or wait. But for married couples, the decision is much more complex.

For married couples, a simple break-even analysis will usually give the wrong answer, costing you benefit dollars. Why? Because Social Security offers three distinct benefits for married people:

1) Retired Worker Benefit – Based on your own earnings record.

2) Spousal Benefit – Provides your spouse with a benefit once you claim your own benefit.

3) Survivor Benefit – Provides your spouse with a benefit after your death.

Virtually all of the simple break-even calculators in use today ignore the spousal and survivor benefits. Of course, there are special computer software programs available which will do these complex calculations. Not wanting to bore you with these elaborate calculations, I will explain it in general terms and what is at stake.

What's at Stake for Married Couples?

The difference between the best and worst possible decision of when to elect Social Security can be well over $100,000! Here's an example: A 62-year-old couple with one above average earner and a lesser earning spouse, who both live to average life expectancy, could lose over $60,000 in family benefits by making the worst possible decision for when to take Social Security.

• If they both elect at age 62, they could be losing over $50,000.

• If they both elect at age 66, this couple could still be leaving $30,000 on the table.

• Simply delaying benefits isn't the answer either. If they both delay to 70, they could be losing over $40,000.

The Switch Strategies Approach

If you file prior to full retirement age, you are deemed to have filed for all benefits for which you are eligible. At full retirement age and beyond, you have several options to elect a limited benefit for a period of time, then convert to a larger benefit at some point in the future.

A recent study suggested that these options represent over $10 billion in unclaimed Social Security benefits. For an individual family, it is not uncommon to receive an additional $20,000 to $40,000 or more in benefits.

The Switch Strategies approach takes advantage of two basic techniques: the "restricted application," and the "file and suspend." When you go to the Social Security office, the individual you meet with has been trained to help you identify the highest benefit you can get today, not necessarily over your lifetime, and definitely not over the joint lives of you and your spouse. As a result, you are unlikely to hear about these techniques during a typical visit.

There is no room in this one column to properly discuss the details of these switch strategies. Just keep in mind that there are strategies available to increase your expected lifetime benefit. With so much at stake, I believe it is a valuable step in the retirement planning effort and shouldn't be overlooked. I just ran an optimization calculation for a couple recently and found that they could increase their benefit by $120,000 by carefully following the when and how of claiming their benefits.

Optimizing our Social Security is one of the building blocks in our financial structure. To keep some flexibility in our lives, we need to remember that there are a number of essential building blocks. I have written about annuities in past columns and will be covering other building blocks in upcoming columns. The point to this kind of planning, of course, is that we can't allow ourselves to run out of money, because when we're out of money–we're out of options.

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