

SUMMARY

With all of the gloomy headlines about Social Security, many people are understandably nervous when it comes to this federal retirement benefit. This year marks the first in over three decades that recipients of the benefit did not get a cost-of-living increase. The latest projections have the Social Security trust fund being exhausted in 2037, four years earlier than previously thought. Despite the pessimism, Social Security remains a critical piece of the retirement puzzle, providing the majority of income for more than half of the people age 65 and up. Declining home values and 401(k) balances make it even more important. All this makes it even more important to take time to strategize about making the most of this important benefit.

The first thing to keep in mind is that despite its financial woes, the program is not going away. Because of all the negative publicity, most people may need some reassurance about this. For people age 55 and older, it should not even be a concern. All others should be made to understand clearly that even if the government makes no changes to the program, and the trust fund that funds the benefit does run out, that does not mean the Social Security program itself would become completely insolvent. There is a scheduled payroll tax that would be able to pay out benefits that about 75% or 80% of current levels. Social Security would continue to be a very important part of anyone's retirement income, so individuals should make sure that they make the best use of it that they can.

CLAIMING BENEFITS

The next step to consider is the fundamental question of what age you will begin claiming benefits. Often the answer is: the later, the better. Currently about half of retirees start claiming security benefits as soon as they become eligible at age 62. Perhaps this is partly because of the fear that the program may not always be there. Retirees may not realize the financial advantages most people gain by waiting a few years to begin. They are electing to receive benefits as soon as they become available, but in point of fact, if you can wait until age 70 before you start claiming, you'll get a monthly benefits that is 75% higher. Even if you wait until age 66, your check would be one third higher.

An individual's base retirement benefit - the amount you receive at the "full retirement age" of 66, is calculated based on your highest 35 years of earnings. If you start claiming earlier, you get a smaller check, and vice versa. The reason is that the amount of your benefit is designed to be actuarially fair to someone with average life expectancy. The Social Security Administration assumes that for someone who is 65 today, a man can expect to live an average of 17 more years, and a woman 19 more years. But by definition, half of the people will outlive the average age and profit by collecting greater benefits over their lifetime. Conversely, if a person is in poor health, collecting benefits starting at age 62 makes sense.

If an individual is earning his or her highest level in the years just before retirement, that will bump up the amount of the check even more, by substituting a year of higher income for previous year of lower income. It is also important to work a few more years if an individual has contributed to Social Security for fewer than 35 years, for example due to years spent out of the workforce while raising children.

BENEFITS FOR SPOUSES

Married clients must also take into account the expected lifespan of each spouse, since the surviving spouse will continue to collect the benefit. In a typical baby boomer couple, if the husband is the higher earner and the wife is younger, the couple should plan for the scenario that the wife is likely to live 6-7 years longer on her own while collecting her husband's benefits. If you're healthy and married there an enormous incentive for you to retire later, since the longer you postpone, the higher the benefit your widow would receive. It is like inflation adjusted extra insurance for your widow. Many people tend to underestimate how many years of retirement the couple as a unit may need to fund. If you're married and both age 62, the chance that one spouse will survive to age 90 is 40%.

Chances that one person in a married couple, both age 62, will live...

