Social Security Retirement Benefits

WHEN IS THE BEST TIME TO BEGIN

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Introduction

- Social Security is a very important part of retirement planning.
- Nearly 90% of Americans age 65 and older receive Social Security benefits.
- 65% of those get half (1/2) or more of their income from Social Security.
- Nearly 30% get 90% or more of their income from Social Security.

Outline of Program

- How are retirement benefits calculated?
- How does the Spousal Benefit work?
- How does the Survivor Benefit work?
- What happens if I continue working after starting my benefit?
- Will my benefits be taxed?

How are Benefits Calculated?

LET'S INTRODUCE YOU TO:

JOE AND ALICE RETIREE

Joe is …

- 62 years old
- He currently makes $40k per year
- And has $200k in a 401(k)

Alice is …

- 62 years old
- She currently makes $25k per year
- And has $100k in a 401(k)

How to determine the Social Security Benefit

3 Steps

1) Determine your Average Indexed Monthly Earnings (AIME)

2) Calculate Primary Insurance Amount (PIA) using current Bend Points

3) Benefits can be reduced or increased depending on the age when benefits are taken

Step 1: Average Indexed Monthly Earnings

- A Retiree must have had earnings subject to FICA taxes for at least 40 Quarters (10 years) to qualify for benefits
- If the Retiree meets the threshold, an average of the Retiree's 35 highest earning years are used to calculate his benefit
- Past years are indexed for inflation. (Income after age 60 is not indexed).
  - For example: You turn 60 in 2013. The national average wage index for 2013 was 44,888.16. The index is 1.28 percent higher than the index for 2012. Therefore, when you apply for benefits, SSA will increase your recorded earnings in 2012 by 1.28 percent.

Step 1: Average Indexed Monthly Earnings

- Earnings are capped: Because only those earnings below an annual limit are taxed each year, that limit also serves as the cap on recorded earnings for any particular year. This is known as the Contribution and Benefit Base.
  - For 2015, this base is $118,500.
  - For 1988, the base was $45,000 (or $104,477 when indexed for inflation)

- The 35 highest indexed earning years (capped at the Contribution and Benefit Base) are averaged and divided by 12 to arrive at the AIME

Step 2: Primary Insurance Amount formula

- For an individual who is eligible for Social Security benefits in 2015 (i.e., turns 62 in 2015), his/her PIA will be the sum of:

(a) 90%* of the first $826 of his/her AIME, plus

(b) 32% of his/her AIME between $826 and $4,980, plus

(c) 15% of his/her average indexed monthly earnings over $4,980.

* May be adjusted if Windfall Elimination Provision (WEP) applies

Joe's PIA

Current Age	62
Year Born	1953
Year turned 62	2015

Current Salary	$ 40,000.00
Avg Indexed Annual Earnings	$ 27,928.92
Avg Indexed Monthly Earnings (AIME)	$ 2,327.41

Bend Points			
Amt of AIME up to $826	$ 826.00	90%	$ 743.40
Amt between $826 and $4980	$ 4,154.00	32%	$ 480.45
Amt of AIME over $4980	$ -	15%	$ -

Primary Insurance Amount	$ 1,223.85
Annual Total	$ 14,686.22

Alice's PIA

Current Age	62
Year Born	1953
Year turned 62	2015

Current Salary	$ 25,000.00
Avg Indexed Annual Earnings	$ 17,575.01
Avg Indexed Monthly Earnings (AIME)	$ 1,464.58

Bend Points			
Amt of AIME up to $826	$ 826.00	90%	$ 743.40
Amt between $826 and $4980	$ 2,799.36	32%	$ 204.35
Amt of AIME over $4980	$ -	15%	$ -

Primary Insurance Amount	$ 947.75
Annual Total	$ 11,372.96

Step 3: Early or Late Retirement

- Retirement benefits depend on age at retirement.
- If a worker begins receiving benefits before his/her normal (or full) retirement age, the worker will receive a reduced benefit.
- A worker can choose to retire as early as age 62, but doing so may result in a reduction of as much as 30 percent.
- Starting to receive benefits after normal retirement age may result in larger benefits. With delayed retirement credits, a person can receive his or her largest benefit by retiring at age 70.

Step 3: Early or Late Retirement

		Benefit, as a percentage of PIA, beginning at age--						
Year of Birth	**Normal Retirement Age**	**62**	**63**	**64**	**65**	**66**	**67**	**70**
1943-54	66	75	80	86 ⅔	93 ⅓	100	108	132
1955	66, 2 mo.	74 ⅙	79 ⅙	85 5/9	92 2/9	98 8/9	106 ⅔	130 ⅔
1956	66, 4 mo.	73 ⅓	78 ⅓	84 4/9	91 ⅑	97 7/9	105 ⅓	129 ⅓
1957	66, 6 mo.	72 ½	77 ½	83 ⅓	90	96 ⅔	104	128
1958	66, 8 mo.	71 ⅔	76 ⅔	82 2/9	88 8/9	95 5/9	102 ⅔	126 ⅔
1959	66, 10 mo.	70 ⅚	75 ⅚	81 ⅑	87 7/9	94 4/9	101 ⅓	125 ⅓
1960 and later	67	70	75	80	86 ⅔	93 ⅓	100	124

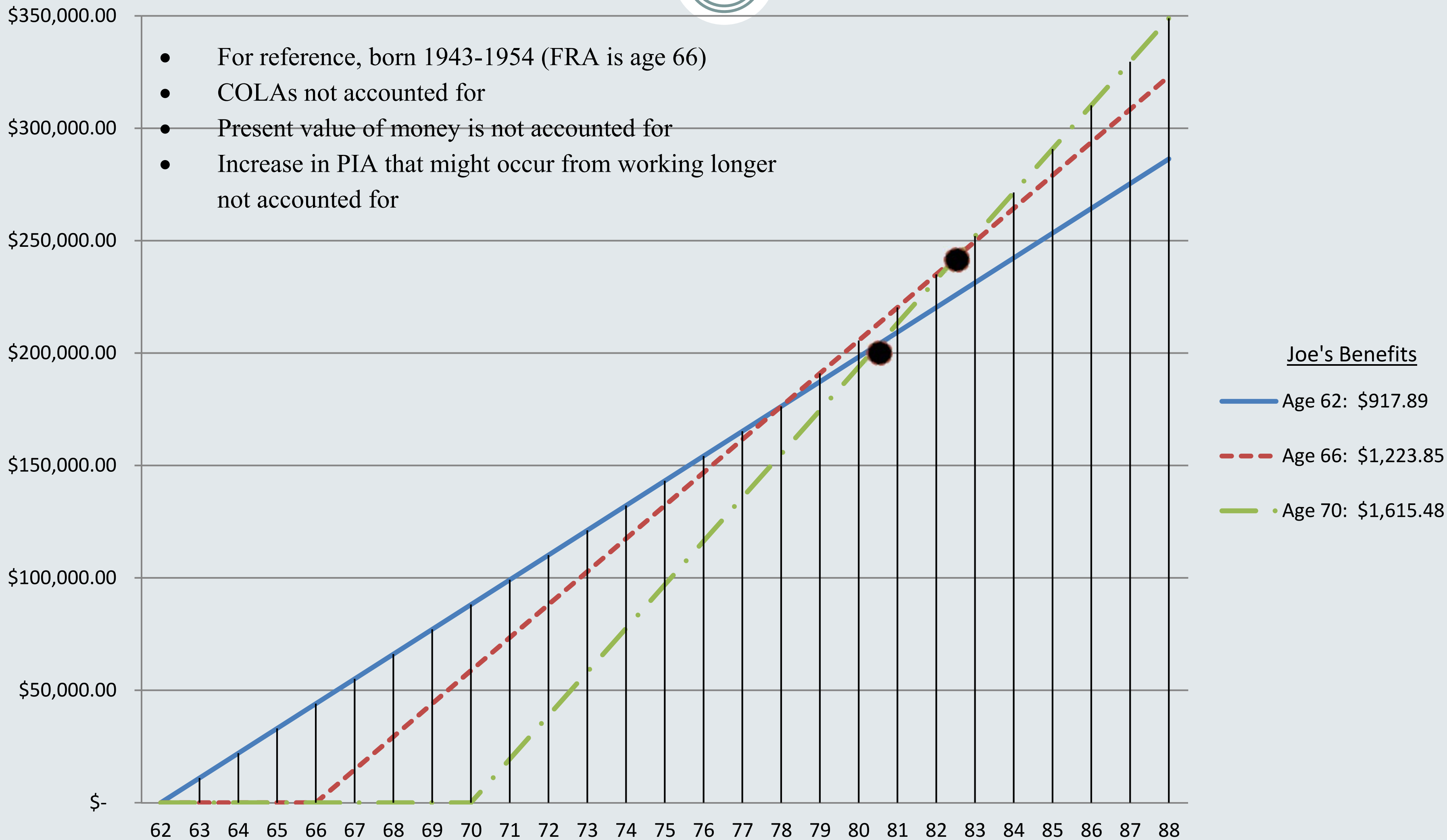
Benefit Amount if taken at age …

Joe's SSB		
Age	Deduction/ Credit	Total Amount
62	75%	$ 11,014.67
66	100%	$ 14,686.22
70	132%	$ 19,385.81

Alice's SSB		
Age	Deduction/ Credit	Total Amount
62	75%	$ 8,529.72
66	100%	$ 11,372.96
70	132%	$ 15,012.31

How waiting to take can pay off

- For reference, born 1943-1954 (FRA is age 66)
- COLAs not accounted for
- Present value of money is not accounted for
- Increase in PIA that might occur from working longer not accounted for



Planning

- For many individuals delaying retirement benefits can be advantageous.

- Questions to consider:
  - What is your personal life expectancy?
  - What are your needs now versus in the future?

- This is just the first part. Proper planning will consider how other factors, such as Spousal Benefits, Taxes, and working during retirement may impact your decision.

Spousal Benefits

HOW CAN WE MAXIMIZE BOTH SPOUSES BENEFITS

Qualifications for Spousal Benefit

- Married to an individual who has applied for a Social Security Benefit (the "primary individual")
- At least 62 years old (exception for raising a child under 18)
- For a divorced spouse
  - Married for at least 10 years
  - Individual applying for spousal benefit must not be remarried
  - If divorced for at least 2 years, ex-spouse must be eligible, but need not have already applied

How much

- The maximum Spousal Benefit is equal to ½ of the primary individual's Primary Insurance Amount.*
- If the spouse is less than his/her own Full Retirement Age (FRA) the Spousal Benefit is reduced for each month before Full Retirement Age
  - For Example, If Alice began taking a spousal benefit at age 62, it would be 35% of Joe's Primary Insurance Amount.

* May be reduced by 2/3 of any Government pension that spouse receives if based on a job where spouse did not pay Social Security taxes

Putting it into Practice

- One Example: Suspended and Restricted Applications

- One spouse (the “primary individual”) files for his/her Social Security benefit at Full Retirement Age, and then suspends payments until age 70, maximizing his/her benefits. Since the primary individual has filed, the other spouse can begin taking the Spousal Benefit based upon the primary individual's benefit amount.

Suspended Application

- When Joe turns 66 (his Full Retirement Age), he can apply for Social Security Benefits then request that payments be suspended

- Joe can earn delayed credits and take his benefit at 70 equal to 132% of his Full Retirement Benefit

Restricted Application

- Since Joe has applied for his benefit, when Alice turns 66 (her Full Retirement Age), she can file a Restricted Application and choose to receive only the Spousal Benefit.

- When she turns 70 she can switch to her own benefit, which then would equal 132% of her benefit at Full Retirement Age.

Suspended and Restricted Application

- Joe will begin receiving 132% of his Full Retirement Age benefit at age 70

- Alice will take a Spousal benefit equal to ½ of Joe's full retirement benefit at her Full Retirement Age

- Then Alice can begin receiving 132% of her Full Retirement Age benefit at age 70

Let's look again at the Cumulative Effect on Joe and Alice

- For purposes of this comparison

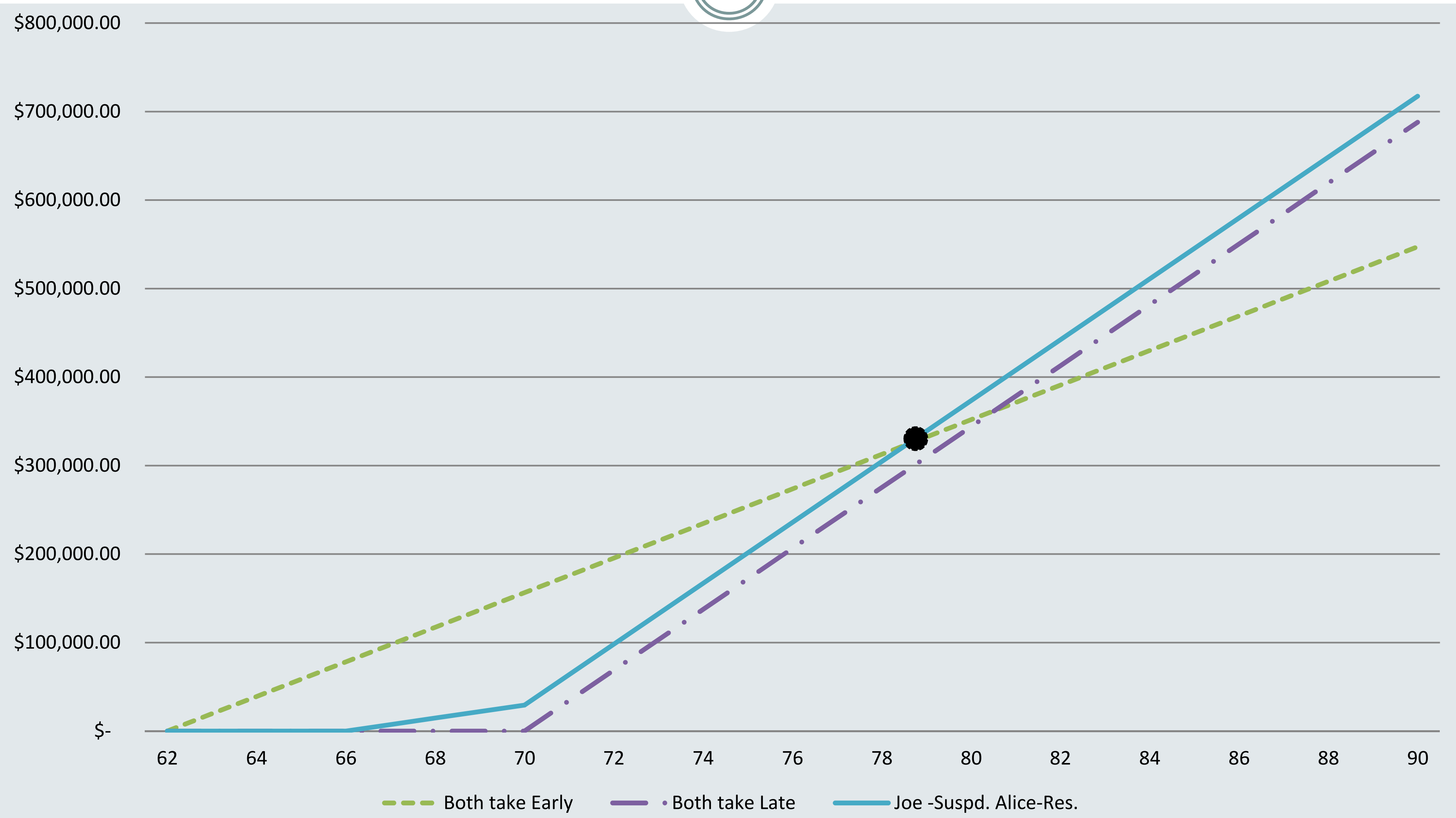
  - Joe is 62 and
  - His PIA/benefit at FRA (66) would be $1,223/ month

  - Alice is also 62 and
  - Her PIA/benefit at FRA (66) would be $947/ month

What is the cumulative value of their benefits at age 90?

- If both J and A take Early (62) ... **$566,787**
- If both J and A take Late (70)... **$722,360**
- If J makes a Suspended Application and A makes a Restricted Application ... **$751,733**
  - The best part is that the extra ~$30,000 comes in the early part of retirement

Total Benefits Over Time



Deemed Filing Rule

- Both spouses may not receive a Spousal Benefit. Only one spouse may make a Restricted Application.
- If a spouse applies for a Spousal Benefit before his/her Full Retirement Age that spouse cannot make a Suspended or Restricted Application. Instead, the SSA will <u>deem</u> the individual to be filing for every benefit to which he/she is eligible, including the Spousal Benefit.
  - If the spousal benefit is greater than the spouse's own benefit, the spouse will automatically receive a combination of his/her own benefit and the spousal benefit (the "excess" spousal benefit).
  - But if his/her own benefit is greater, then he/she will simply receive his/her own benefit, and no Spousal Benefit.

Excess Spousal Benefit

- As an example: Let's say Joe and Alice are married, with PIAs of $2,200 and $800 respectively. Joe is 66 and Alice is 64. Joe files and suspends at age 66, his Full Retirement Age, and Alice then applies for the Spousal Benefit at her current age of 64.
- Since Alice files before her FRA, there is a "deemed filing."
- SSA reduces Alice's own monthly benefit to $693 because she is taking early.
- Since Alice is taking her own benefit, she will receive an "Excess" Spousal Benefit. To calculate the Excess Spousal Benefit, SSA takes Alice's unreduced PIA and subtracts it from half of Joe's unreduced PIA ($1,100 minus $800 = $300). This is the Excess Spousal Benefit base amount.
- Since Alice is under her FRA, SSA reduces the Excess Spousal Benefit. To do so, SSA determines the number of months before Alice's FRA – in this case, at age 64, she is 24 months before age 66.

Excess Spousal Benefit (continued)

- SSA multiplies the Excess Spouse Benefit base amount by a number determined by subtracting that number of months from 144. For, Alice, $300 times (144 minus 24) equals $36,000.
- SSA divides that amount by 144. In Alice's case, $36,000 divided by 144 equals $250, which is her reduced Excess Spousal Benefit.
- Finally, SSA adds the reduced Excess Spousal Benefit ($250) to Alice's own reduced retirement benefit amount ($693) to find her total monthly benefit of $943 ($11,316/year).
- It should be noted that if Alice applied more than 36 months before FRA (such as if Alice was 62 when Joe is 66), then the above calculations are modified.
- If Alice waited until FRA and filed a restricted application for only the Spousal Benefit, she would receive the "normal" Spousal Benefit: 50 percent of her husband's full retirement benefit, or $1,100 (13,200/year).

When do Spousal Benefits end?

- At the death of either the spouse or the primary individual (switch to Survivor Benefits – next section)
- At divorce, if not married at least 10 years
  - Unless already 62 years old
- Upon remarriage of spouse claiming spousal benefit
  - If primary individual gets remarried this will not affect the spousal benefit
- When child reaches 18, if spouse is under 62 and claiming dependent child exception

Planning

- For many couples, applying for Spousal benefits is a great way to maximize the benefit of Retirement Insurance Benefits.

- It is also one of the least understood areas, and thus the easiest place to leave money on the table.

Survivor Benefits

Overview

- Survivor Benefit is a lifetime benefit based upon the deceased spouse's benefit which is available for surviving spouses, surviving divorced spouses, and other family members.

- A surviving spouse is generally entitled to the deceased spouse's benefit if they were married for at least 9 months.* Generally, a surviving spouse must be unmarried to qualify, unless remarried after becoming 60 years old (or remarried after 50, if disabled).

- The Survivor Benefit is generally equal to (1) the deceased spouse's benefit amount, and then (2) reduced depending upon the surviving spouse's age.

*A surviving divorced spouse must have been married to the deceased worker for at least 10 years to be eligible

How much

- Survivor Benefit is based upon the deceased spouse's benefit.
- If the deceased spouse was receiving benefits at the time of his/her death, the Survivor Benefit is equal to one of three amounts: 1) the amount of benefit that the decedent was actually receiving; 2) the reduced benefit based on the PIA of the decedent and the survivor's age; or 3) 82.5% of the PIA of the decedent.
- If the deceased spouse was not already receiving benefits and died at FRA or later, the base benefit amount is the amount that the decedent would have received, including all delayed credits.
- If the deceased spouse dies before FRA and had not yet begun receiving retirement benefits, the surviving spouse is entitled to a base benefit equal to 100% of the deceased spouse's PIA.

Reduced for Surviving Spouse’s Age

- Survivor Benefits can be claimed as early as age 60, rather than age 62 as with regular retirement benefits. The benefit is reduced if taken before the Survivor Benefit Full Retirement Age.

- For example, if taken at age 60, the Survivor Benefit is reduced to 71.5%.

- The reduction factor is gradually eliminated up to the Survivor Benefit Full Retirement Age

Planning

- Filing for Survivor Benefits has no impact on filing for Social Security benefits based on your own record – other than the fact that you cannot file for both benefits at the same time.

- Coordinating these two benefits can take a couple of different paths: for example, a surviving spouse could file for the Survivor Benefit first, allowing their own benefit to accrue Delay Credits up to as late as age 70; or they could file for their own benefit first, and then later file for the Surviving Spouse benefit.

Working in Retirement

Senior Citizens' Freedom To Work Act Of 2000

- Eliminated the Social Security retirement earnings test after a person attains Full Retirement Age (FRA)

- Now only two concerns
  - Earnings in years before reaching FRA
  - Earnings in the year that retiree reaches FRA

What income counts?

- Earnings, for this purpose, includes
  - Wages for employees
  - Net earnings for self employed

- But does not include
  - Government Benefits
  - Investment Earnings
  - Pensions
  - Annuities
  - Capital Gains

- The amount of earnings for a given year are self-reported by the retiree at the beginning of the year and later adjusted if actual earnings are more or less than projected

Earnings Before Full Retirement Age

- Social Security benefits are reduced by $1 for every $2 the retiree earns over a set amount
  - In 2015 that amount is $15,720

- For example:

  Joe is 64 years old, earns $25,720 in 2015, and his Social Security benefit for this year is equal to $24,000. His annual benefit will be reduced by $5,000 to $19,000.

Earnings in the Year Retiree reaches Full Retirement Age

- Social Security benefits are reduced by $1 for every $3 the retiree earns over a set amount, if earned in the months before the month of FRA.
  - In 2015 that amount is $41,880

- For example:

  Joe will turn 66 (his FRA) in November of 2015. He will earn $50,880 from Jan. to Oct. of 2015, and his Social Security benefit for this year is equal to $24,000. His annual benefit will be reduced by $3,000 to $21,000.

Special Rule for First Year of Retirement

- If individual retires in the middle of a year, the earnings rule is calculated on a monthly basis for those months after retirement
  - In 2015, the monthly allowed earnings is $1,310 ($15,720/12)

- For example:

  Joe is 64 years old. He earns $80,000 from January to October 2014, and then retires in November. Working as a consultant, he earns $1,000 a month in November and December. His 2015 annual Social Security benefit will not be reduced.

How the Benefit is Reduced

- Payments are withheld each month until withheld amount equals reduced amount

- For example:

  Joe's yearly benefit is reduced by $4,000 due to earnings over the limit. His monthly benefit is $2,000. January and February's payments will be withheld and normal payments, $2,000, will resume in March.

*Withholding is in full month increments only. If the final month withheld results in a withholding greater than the amount of the required reduction that excess is added to retiree's benefit in the following year.

Reductions for Earnings are withheld not Eliminated

- If some Social Security benefits are withheld because of earnings, the retiree's monthly benefit will increase starting at the retiree's full retirement age to take into account those months in which benefits were withheld.

- For example:

Joe applies for retirement when he is 64. His earnings between 64 and 66 are enough for SSA to withhold a full year of benefits. At age 66, the SSA will recalculate the debit applied to his monthly benefit to an amount equal to the debit that would have been applied if he had retired at age 65. His benefit after FRA will only be reduced by 6.67%, not 13.33%.

Reductions for Earnings Affect Family Benefits

- Excess earnings are charged against the total monthly family benefit, which includes all monthly benefits payable to you and anyone else entitled to benefits on your earnings record (e.g., the Spousal Benefit).
- If the benefits of someone entitled to benefits on your earnings record are withheld due to excess earnings, those withheld benefits are lost and not recaptured.

Retirement Benefits and Taxes

HOW IS SOCIAL SECURITY INCOME TAXED

Combined Income

- The percentage of benefits that are taxable depends on your combined income.
- First determine Joe and Alice's Combined Income
- Combined Income = ½ of SSB + Adjusted Gross Income (AGI) + Nontaxable Interest
  - Joe's Annual Benefit =$30,748
  - Alice's Annual Benefit = $16,895
  - Adjusted Gross Income (Excluding SSB) = $15,000
  - Nontaxable Interest Income = $0
- Joe and Alice's Combined Income = $38,821

Percentage of Benefit Taxed

- For a couple filing a joint tax return:
- If Combined Income < $32,000, SSB is not taxable
- If Combined Income $32,000-$44,000, 50% of SSB is taxable
- If Combined Income > $44,000, 85% of SSB is taxable
    - For single recipients the cutoff points are $25,000 and $34,000

Final Amount included in Taxable Income

- For Joe and Alice, since their Combined Income is between $32,000 and $44,000 ($38,821):

- 50% of their SSB, or $23,822, will be included in their taxable income

- Retirees who think their benefits will be taxed can choose to make estimated quarterly tax payments to the IRS, or choose to have amounts withheld from their benefits

Examples

APPLYING THE SOCIAL SECURITY RULES

Let's look at Bob and Mary

Bob is …

- 66 years old
  - He turned 66 in Aug 2015
- He made $60k in 2014
- And has $300k in a 401(k)

Mary is …

- 62 years old
  - She turned 62 in Jan 2015
- She made $40k in 2014
- And has $125k in a 401(k)

If Bob and Mary started taking benefits Jan. 2015

- Bob would have taken 8 months before his FRA
- His $2,077 PIA would be reduced by 5.5%
  - His benefit will be $1,962/month or $23,553/year

- Mary would have taken 4 years before her FRA
- Her $1,639 PIA would be reduced by 25%
  - Her benefit will be $1,230/ month or $14,760/ year
    - She is also eligible to an excess spousal benefit, since Bob has already applied. However, since half of Bob's PIA is less than her own PIA, she will only receive her own benefit.

How much from Savings

- Bob and Mary have already decided that they need $60k a year (before taxes) to pay for all of their expenses in retirement*
- In addition to their $38,313 in Social Security benefits, they will need to take out $21,687 from their 401(k)s
- If they withdraw $21,687 from their 401(k)s every year their savings will last for 19.6 years, or until Bob is 85 and Mary is 81**

* This is in today's dollars **Not taking into account growth of 401(k)s

A Final Alternative

- Now let’s imagine that Bob and Mary instead decide to delay taking Social Security retirement benefits.
- Neither of them does anything until he or she reaches Full Retirement Age.
- After Bob turns 66, he files a Suspended Application and delays actually taking a benefit until age 70.
- Once Mary turns 66, she files a Restricted Application. She takes the full spousal benefit until she turns 70 and then switches to her own benefit.

Final Alternative, cont'd.

- If they both decide to quit working on Jan. 2nd, 2015, they will need to withdraw savings from their 401(k)s to support themselves.
- In order to have $60,000 before tax, they will need to take out $60,000 from their 401(k)'s for the first four years (2015-2018).
- In 2019, they will only need to withdraw $47,538 because Mary will begin receiving her spousal benefit (half of Bob's PIA, or $12,462/yr).
- In 2020-2022, Mary will still be receiving her spousal benefit ($12,462/year) and Bob will begin receiving his Social Security retirement benefit (now $32,904/year because of delayed credits). For those three years they will only need to withdraw about $14,600/year from their savings.

*All of the withdrawals are in today's dollars.

Final Alternative, cont'd.

- In 2023, both Bob and Mary will be receiving their own Social Security retirement benefits, including all applicable delayed retirement credits.
- Their combined Social Security retirement benefits will equal $58,869*
- Assuming they have enough savings to bridge the gap for eight years (~$332,000*), they will have enough income for their projected expenses no matter how long they live

* In today's dollars

Thank You

ANY QUESTIONS?

Additional Information on the Firm

Kennerly Montgomery is a general practice law firm that has provided legal advice to clients for almost 100 years. KM attorneys practice in a variety of areas, representing municipal clients, including local governments, agencies and public utilities.

Bill Mason, Kathy Aslinger, and Michael Crowder practice extensively in employee benefits law, which includes design, documentation, administration, audit, litigation, termination and qualification of employee health and welfare and pension plans for public, tax-exempt and private employers. The Firm sponsors various prototype retirement plans and prepares both interim amendments and discretionary amendments for all plan types as well as counsels with fiduciaries on ERISA and Federal & state law obligations. They represent clients before various agencies regulating employee benefits.

Michael Crowder and Alex Taylor practice extensively in estate planning by, among other things, helping individuals understand how Social Security benefits play into their retirement and estate plans. Kennerly Montgomery's estate planners take a compressive approach to estate planning, ensuring that assets are protected and passed to loved ones in accordance with the client's wishes and desires.

A Little About Your Presenters

Bill Mason received his JD from Harvard Law School in 1974, and has been practicing law for 40 years, most of that time in employee benefits for governments. He worked for the Tennessee Valley Authority from 1974 – 1986, Wagner Myers & Sanger PC, from 1986 – 1988, and William E. Mason PC from 1988 – 2009. Bill joined Kennerly Montgomery in 2009. Mr. Mason serves on the Board of Directors for the Legacy Park Foundation and the Education Subcommittee for the United Way of Greater Knoxville. He is the past Chair of the Hillcrest Healthcare Board of Directors.

As a leader of Kennerly Montgomery's employee benefits practice, Kathy Aslinger focuses on advising fiduciaries for the benefit of participants, assisting both private and governmental clients in the design, implementation and maintenance of their employee benefit plans, including 401(k), pension, cafeteria, and health plans. She commonly assists clients in maneuvering through the complex world of audits, fiduciary liability issues, DOL and IRS compliance, HIPAA, COBRA, ERISA and state law obligations, as well as Affordable Care Act compliance. Kathy has been practicing law for over 15 years and has been with Kennerly Montgomery since January 2010. In addition, Kathy serves on the Board of Directors for Uplands Village, a continuing care retirement community in Pleasant Hill, Tennessee.

Michael R. Crowder practices generally in estate planning and employee benefits. Michael serves individuals in drafting wills and trusts, retirement planning, and issues relating to retirement plan distributions. Michael graduated from the University of Tennessee, College of Law, with a Concentration in Business Transactions from UT's Clayton Center for Entrepreneurial Law. Prior to attending law school, Michael earned a Bachelor of Arts from Princeton University, where he majored in Religion and also played offensive line on the football team. Michael currently sits as a member on the Knoxville Estate Planning Council.

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