KEATING
WEALTH MANAGEMENT

Social Security 101

Overview

Did you know that 84% of Americans age 65 and older receive Social Security payments?[1] As ubiquitous as it is, Social Security is also ferociously complex, with 12 benefits dictated by over 2,278 primary rules and tens of thousands of secondary rules.[2] However, understanding some relatively simple key concepts and ideas can guide you toward making decisions that will help you maximize your long-term retirement benefit. In particular, if you expect to live longer than the average life expectancy, as many college-educated, white-collar workers do, then you are better off delaying claiming Social Security until the latest possible age and collecting a higher retirement benefit for the rest of your life.

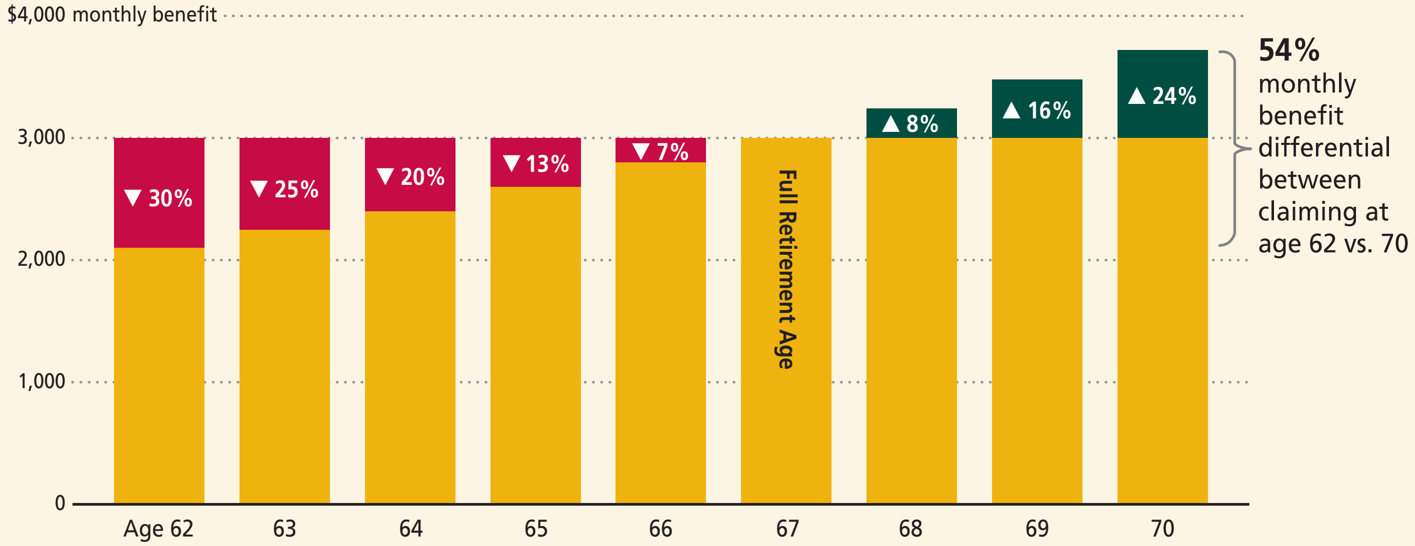
In this briefing, we provide a high-level overview of how Social Security works and how to maximize your benefits. Nevertheless, it's essential to consult with a qualified Social Security expert to create a plan tailored to your specific circumstances. Reading this guide should equip you to have an informed conversation with your financial adviser, who can develop a plan best suited to your needs.

How Social Security works

Over the course of your working life, your gross wages up to a specified cap are taxed a fixed percentage each year to fund the Social Security program. For 2020, the rate is 6.2% and the cap is $137,700.[3] If you have accumulated a total of 40 quarterly credits over the course of your career (equal to 10 years of taxable earnings, which do not have to be continuous), then you are eligible to collect Social Security benefits when you retire.

Social Security Benefit Amount Based on Claiming Age

Your benefit is permanently determined by your age at the time of initial claiming



Source: Social Security Administration

[1] *Glenn Ruffenach, "Where to Check Up on the Health of Your Pension Plan," Wall Street Journal, June 4, 2020.*

[2] *The Editorial Board. "Unrigging the Poverty Trap." Wall Street Journal, June 3, 2020.*

[3] *"Topic No. 751 Social Security and Medicare Withholding Rates," Tax Topics (Internal Revenue Service, February 14, 2020).*

The amount you will receive is based on the level of your earnings in your 35 highest-earning years according to a three-tiered formula. Based on your average monthly earnings, Social Security will replace:

- 90% of the first $960.
- 32% of the amount between $960 and $5,785.
- 15% of earnings above $5,785.

Social Security indexes your earnings to the national average wage indexing series in the year you turn 60 to ensure that your future benefits take into account standard of living changes over the course of your working life.[4]

While the exact formula is complex, the bottom line is that Social Security generally replaces about 40% of your annual pre-retirement earnings.[5] The average benefit is about $1,500 per month, and benefits are capped at around $3,000 per month—*unless* you allow your benefit to accumulate retirement credits.

You can begin collecting Social Security benefits as early as age 62 and as late as age 70 (see illustration on page 1). If you wait until 70, you will accumulate retirement credits, thus increasing your permanent monthly Social Security payout for the rest of your life. If you choose to claim benefits before your "full retirement age"—67 for anyone born in 1960 or later—your retirement benefit will be permanently reduced. For most people, this is a financial planning mistake that will result in a lower lifetime benefit.

Although you won't receive any benefits until the age you choose to start collecting, with a higher monthly benefit, you will eventually make up for the payments you passed up earlier. Most likely, you'll break even sometime in your early 80s, and from that point on, your lifetime Social Security payout will be higher than if you had started collecting earlier.

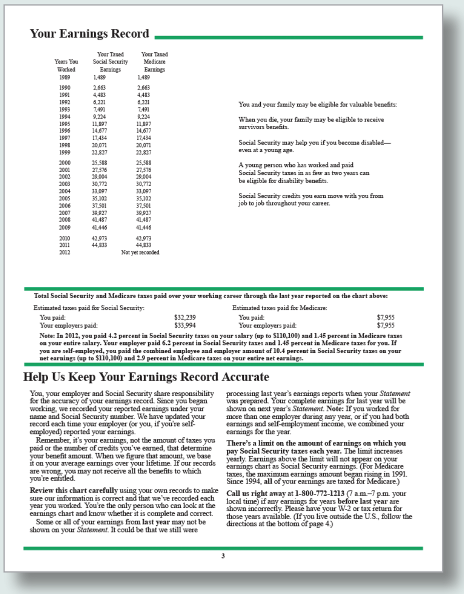
The time when you begin collecting Social Security does *not* have to coincide with when you actually retire. If you can afford to live off other savings until age 70, we strongly recommend you delay claiming your Social Security benefits until then, as there are no alternative investment options that can *guarantee*—with the backing of the U.S. government—an 8% annual growth in earnings.

There are some situations that warrant claiming reduced benefits early. For example, you should collect early if you have a shorter than typical life expectancy. You may also wish to collect early if you have no spouse who would be entitled to a survivor benefit.

Your Personal Benefits Statement

You can easily access your own personal Social Security benefits statement, including your earnings history and projected benefits, at www.ssa.gov/myaccount. Setting up an account is simple and quick. Select "Create an Account," and then provide the necessary identifying information, including your name, address, email address, and Social Security number. You will be prompted with several questions to confirm your identity, and then you will be able to log in and access your information.

www.ssa.gov/myaccount



Your Earnings Record

Years You Worked	Your Taxed Social Security Earnings	Your Taxed Medicare Earnings
1989	1,489	1,489
1990	2,663	2,663
1991	4,483	4,483
1992	6,221	6,221
1993	7,491	7,491
1994	9,224	9,224
1995	11,897	11,897
1996	14,677	14,677
1997	17,434	17,434
1998	20,071	20,071
1999	22,827	22,827
2000	25,588	25,588
2001	27,576	27,576
2002	29,004	29,004
2003	30,772	30,772
2004	33,097	33,097
2005	35,102	35,102
2006	37,501	37,501
2007	39,927	39,927
2008	41,487	41,487
2009	41,446	41,446
2010	42,973	42,973
2011	44,833	44,833
2012	Not yet recorded	

You and your family may be eligible for valuable benefits:

When you die, your family may be eligible to receive survivors benefits.

Social Security may help you if you become disabled—even at a young age.

A young person who has worked and paid Social Security taxes in as few as two years can be eligible for disability benefits.

Social Security credits you earn move with you from job to job throughout your career.

Total Social Security and Medicare taxes paid over your working career through the last year reported on the chart above:

Estimated taxes paid for Social Security:		Estimated taxes paid for Medicare:	
You paid:	$32,239	You paid:	$7,955
Your employers paid:	$33,994	Your employers paid:	$7,955

Note: In 2012, you paid 4.2 percent in Social Security taxes on your salary (up to $110,100) and 1.45 percent in Medicare taxes on your entire salary. Your employer paid 6.2 percent in Social Security taxes and 1.45 percent in Medicare taxes for you. If you are self-employed, you paid the combined employee and employer amount of 10.4 percent in Social Security taxes on your net earnings (up to $110,100) and 2.9 percent in Medicare taxes on your entire net earnings.

Help Us Keep Your Earnings Record Accurate

You, your employer and Social Security share responsibility for the accuracy of your earnings record. Since you began working, we recorded your reported earnings under your name and Social Security number. We have updated your record each time your employer (or you, if you're self-employed) reported your earnings.

Remember, it's your earnings, not the amount of taxes you paid or the number of credits you've earned, that determine your benefit amount. When we figure that amount, we base it on your average earnings over your lifetime. If our records are wrong, you may not receive all the benefits to which you're entitled.

Review this chart carefully using your own records to make sure our information is correct and that we've recorded each year you worked. You're the only person who can look at the earnings chart and know whether it is complete and correct.

Some or all of your earnings from **last year** may not be shown on your *Statement*. It could be that we still were processing last year's earnings reports when your *Statement* was prepared. Your complete earnings for last year will be shown on next year's *Statement*. **Note:** If you worked for more than one employer during any year, or if you had both earnings and self-employment income, we combined your earnings for the year.

There's a limit on the amount of earnings on which you pay Social Security taxes each year. The limit increases yearly. Earnings above the limit will not appear on your earnings chart as Social Security earnings. (For Medicare taxes, the maximum earnings amount began rising in 1991. Since 1994, **all** of your earnings are taxed for Medicare.)

Call us right away at 1-800-772-1213 (7 a.m.–7 p.m. your local time) if any earnings for years **before last year** are shown incorrectly. Please have your W-2 or tax return for those years available. (If you live outside the U.S., follow the directions at the bottom of page 4.)

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[4] *"Indexing Factors For Earnings," Social Security (Social Security Administration), accessed June 8, 2020.*

[5] *"Your Social Security Statement," Social Security (Social Security Administration, May 1, 2020).*

Types of benefits

The primary worker who has been paying into Social Security through the tax on his or her wages is always entitled to benefits, but so are a number of secondary beneficiaries, as we will discuss in more detail below.

The following chart organizes the 12 basic types of benefits that Social Security provides into five categories.

12 Types of Social Security Benefits

Retirement	Survivor	Disability	Medicare	Supplemental Security Income
❶ Primary worker	❺ Survivor	❻ Primary worker	❾ Primary worker	⓫ Disabled adults and children
❷ Spouse		❼ Spouse	❿ Spouse	⓬ People age 65 and older
❸ Ex-spouse		❽ Children		
❹ Children				

Social Security for married couples

To explore some of the basic concepts of Social Security, let's look at the case of a typical married couple with one higher-earning spouse and one spouse with lower or no earnings.

If both spouses are eligible for Social Security retirement benefits, the higher-earning spouse should delay collecting those benefits, if at all possible, until age 70. There are two reasons for this approach: First, it maximizes the couple's total income over the course of retirement, and second, it maximizes the survivor benefit for the other spouse.

A survivor benefit is worth up to 100% of what the deceased worker was receiving or was entitled to receive at the time of death, as long as the surviving spouse waits to collect until his or her own full retirement age. Holding out for the highest possible survivor benefit ensures that the surviving spouse will be taken care of long after the worker's death.

If the higher-earning spouse delays collecting benefits until the last possible moment, the lower-earning spouse may wish to begin collecting early to bring in some additional income for the household in the meantime.

Secondary beneficiaries

In addition to collecting your own Social Security retirement benefits, you are entitled to benefits for secondary beneficiaries, including a spouse, former spouse, and children.

Spousal benefits are worth up to 50% of the primary worker's benefit at full retirement age. However, the non-earning spouse cannot collect spousal benefits until the earning spouse begins collecting Social Security. A lower-earning spouse who is entitled to individual benefits can "top off" a lower personal benefit with a spousal benefit when the higher-earning spouse begins collecting.

For example, say one spouse is entitled to $800 per month in personal benefits and the other is entitled to $2,400 per month. The lower-earning spouse can start collecting benefits as early as age 62, and can then receive up to an additional $400 per month when the higher-earning spouse begins collecting Social Security.

Divorced spouses are also entitled to benefits, as long as all three of the following criteria are met:

❶ The marriage lasted at least 10 years.

❷ Both spouses are at least 62 years old.

❸ The ex-spouse seeking the benefit did not remarry before age 60.

If the couple has been divorced at least two years, the ex-spouse seeking benefits does not even have to wait until the eligible worker files for primary Social Security.

Finally, older parents can capitalize on Social Security benefits for their children under age 18 (and up to age 19 for children who are still in high school). Each child is entitled to 50% of the parent's full-retirement-age benefit, regardless of when the parent claims benefits.

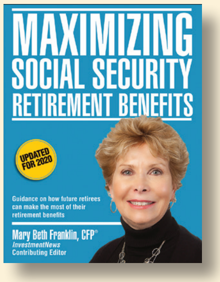
There is a cap on total family benefits. This cap is based on a complex formula, but works out to 150% to 188% of the worker's full-retirement-age benefit.[6] If the combination of worker, spousal, and child benefits exceeds that cap, all secondary benefits are proportionally reduced. Nevertheless, the payment of child benefits may be a good reason to collect early. If you do so, you can suspend your primary benefits once your youngest child turns 18, so your own benefits can continue to grow until you turn 70.

Earnings cap

One final element of Social Security to consider—and another incentive to delay collecting benefits—is the earnings cap. If you are still working before full retirement age, you are restricted in the amount of benefits you can collect every year. Basically, if you begin claiming early and are still working, much of your Social Security benefit will be deferred anyway.

The earnings cap goes away at full retirement age. At that point, you can earn any amount without reducing your benefits.

Further Reading



It is impossible to cover such a complex and nuanced a topic in only a few pages. If you are interested in more detailed information, we highly recommend Mary Beth Franklin's 40-page eBook, *Maximizing Social Security Retirement Benefits*, a comprehensive resource that explains the ins and outs of claiming strategies for many different circumstances.

[6] *"Can My Children Get Benefits on My Social Security When I Retire?" AARP, March 25, 2020.*

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