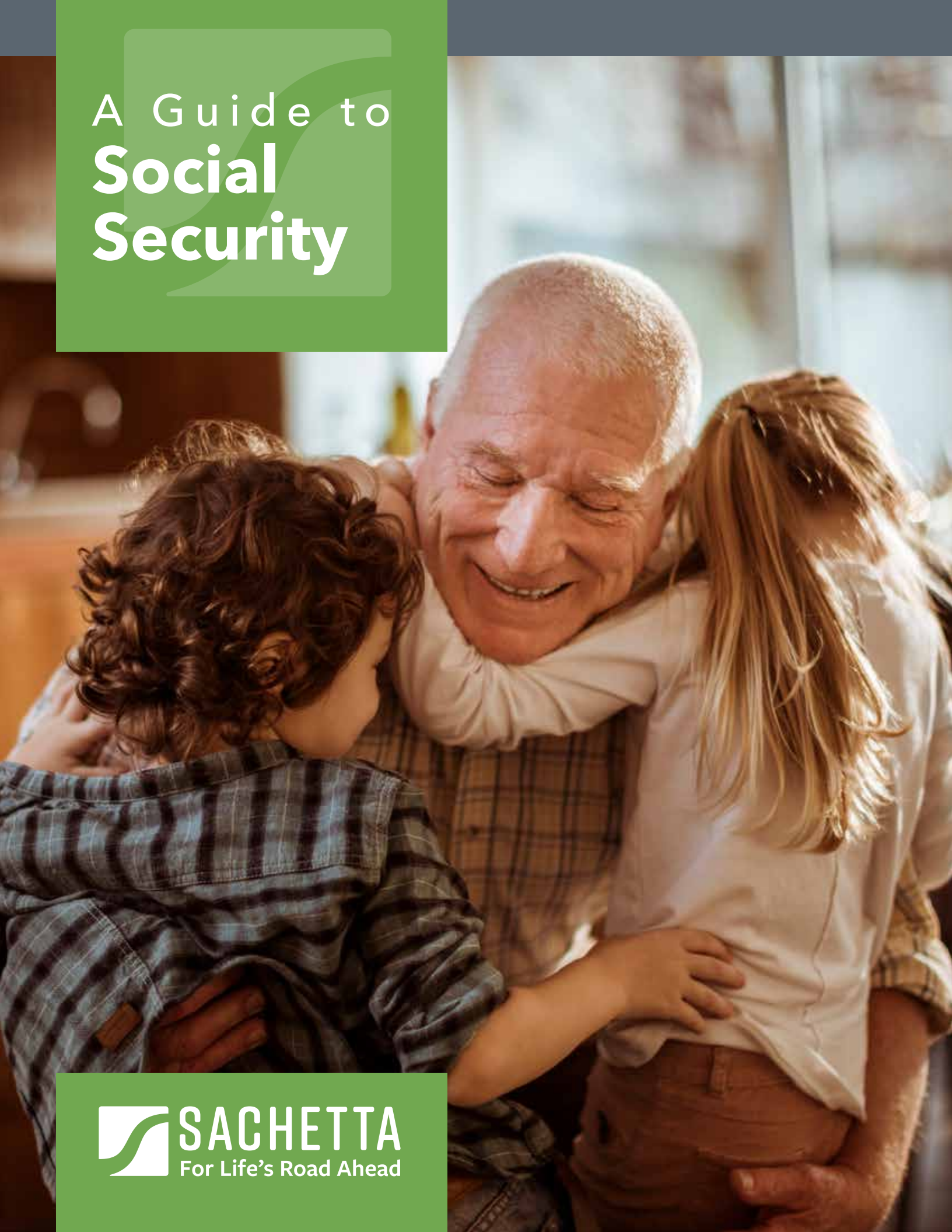


A Guide to **Social Security**





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About 180 million American workers are covered by Social Security, and an estimated 65 million people receive Social Security benefits every month. Social Security can be a lifeline for retired and disabled people who have little to no income. For other retirees, Social Security benefits are just one part of a diverse financial plan.

Social Security is a massive program with a lot of complicated rules and regulations. Whether you're nearing retirement or just starting to think about Social Security benefits for the first time, here's what you need to know.

Social Security Primer



What is Social Security?

The Social Security Act of 1935 created the Social Security program. The average life span had risen by 10 years since 1900, and improved health conditions meant that there were more retired, disabled and vulnerable Americans who were unable to work and lacked economic stability.

Social Security was created to maintain their welfare, and to guarantee that retired workers would continue to receive monthly income after they turned 65. Most people working today won't qualify for monthly retirement benefits until they're 66 or 67, but the principle is the same: Social Security benefits provide a reliable income source for workers and their families in their senior years.

How Does Social Security Work?

Members of today's workforce pay for current Social Security benefits through a dedicated payroll tax. Collected taxes are kept in two trust funds, the Old-Age and Survivors Insurance (OASI) fund and the Disability Insurance (DI) fund. Money from the OASI fund is used to pay for retirement and survivors benefits, while the DI fund pays for disability benefits. Any surplus money is invested in Treasury bonds to further bolster the reserves.

Once you're eligible for Social Security retirement benefits and decide you're ready to claim them, you'll receive a monthly payment for the rest of your life. The size of your retirement benefit depends on how much you earned during your career and how old you are when you take your benefits.



Who's Eligible for Social Security?

You become eligible for Social Security retirement benefits by “paying into” the system with payroll taxes. Workers are eligible for benefits after earning 40 work credits, which generally takes 10 years.

A deceased worker's family members may also be eligible for survivor benefits earned on the worker's record. Survivors don't have to earn work credits to qualify for these benefits, but must meet other conditions.

When Does Social Security Start?

Eligible applicants can claim their retirement benefits at any point beginning at age 62, but many choose to wait until after they reach their full retirement age (FRA). Your FRA is determined by the year of your birth; it's 66 or 67 for today's workforce.

It pays to delay claiming benefits, which is why financial planners often recommend this strategy. The Social Security Administration calculates your "primary insurance amount," or the amount you're entitled to receive as a monthly benefit, using your earnings record. When you claim Social Security starting at your full retirement age, you get 100 percent of that amount every month. Claiming benefits early reduces the benefit by a fraction for every month remaining until your FRA. Or, if you delay benefits beyond your FRA, the amount continues to grow until you turn 70.

It's advisable to apply for disability benefits as soon as you become fully disabled. There's an automatic five-month waiting period for these benefits, so payments won't begin until at least six months after the date that the SSA decides a disability began.



How Do You Claim Social Security Benefits?

Once you decide to claim Social Security retirement benefits, the process is simple. The easiest way to claim benefits you've earned is to complete an application through your mySocialSecurity account on SSA.gov.

Applying for disability benefits is a little more complicated, since applicants have to submit medical evidence as part of the process.

Applications can also be submitted through the SSA's website.

How is Social Security Taxed?

Social security is taxed based on what other income you have in a given year. If your combined income (adjusted gross income + nontaxable income + $\frac{1}{2}$ of your SS benefits) is between \$25k and \$34k as a single person (\$32k and \$44k married filing jointly), then 50% of your social security benefits will be included in your income for tax purposes. If your income is above the \$34k amount (\$44k married) then 85% of your social security benefits become taxable.



Is Social Security in Trouble?

Fears about the future of Social Security are justified, but there's no reason to panic. As of the Trustees' 2020 report, reserves in the Old Age and Survivors Insurance (OASI) fund are projected to only pay for full benefits through 2034. When the reserves run out, payroll taxes from current employees will be the only source of funding for Social Security benefits. The SSA projects that this income will be enough to cover about 76 percent of scheduled benefits.

(The news is better for people who rely on SSDI benefits. The DI fund should be solvent through 2062, and the SSA currently expects that tax income will cover 92 percent of disability benefits after that.)

So, yes, the future of Social Security is shaky. But a lot can happen before 2034. Legislative reform could increase tax revenues or make other changes to the program. It's still safe to count on your benefits as part of your family's financial future—just make sure those benefits are only one part of a comprehensive financial plan. Social Security alone probably won't be enough to finance the kind of retirement you're envisioning.



What Determines My Benefit?

Can you count on at least \$3,000 a month, or should you be planning on a monthly retirement benefit that's closer to \$2,000? What about your spouse's benefit?

It's hard to do any meaningful retirement planning if you have no idea how much your Social Security benefit is going to be. The amount you receive each month from Social Security is determined by your lifetime earnings and the age at which you claim benefits, so it's in flux while you're still working and paying into the system. Your benefit amount isn't "locked in" until you apply and are approved for benefits; from that point forward, you'll receive the same amount every month for the rest of your life. Understanding how your Social Security benefit is calculated allows you to get that number as high as possible before you retire.



Qualifying for Your Social Security Benefits

Make sure you qualify for Social Security benefits before counting on them as part of your retirement plan. Nearly all workers do qualify; just ~3.5 percent of people between 60 and 89 don't or won't receive benefits. They're generally people who either didn't work consistently or who held jobs but didn't pay Social Security taxes on their earnings.

Specifically, Social Security eligibility is determined using a measurement called work credits. You earn credits by earning income, with each worker being allowed to earn a maximum of four credits each year. For 2022, workers earn one credit for every \$1,510 they earn in taxable income. So anyone who pays Social Security taxes on an annual income of at least \$5,880 will earn the

full four credits this year. How many credits a person needs depends on what kind of benefit they're claiming.

Workers over 62: You must earn at least 40 credits to qualify for retirement benefits. If you've been working for at least 10 years, you've probably already fulfilled this requirement.

Spouses of eligible workers: An individual may earn partial Social Security benefits on their spouse's earnings record, even if the spouse has no work credits.

Family members of eligible workers: Survivors benefits may be paid out to a worker's widow/er, minor children, dependent parents and other relatives in certain circumstances. Whether survivors qualify depends on the deceased's earnings records.

How Social Security Benefits are Calculated

When you decide to claim Social Security and start receiving benefits, the SSA calculates your monthly average earnings over the 35 years in which you earned the highest income. (The amounts are indexed to account for inflation.) That “35 year rule” may be important as you think about when you want to claim Social Security. The SSA always averages your income over 35 years, which means retiring early could reduce your benefit. Say you retire after working for 30 years. The SSA will calculate your average income by averaging 30 years of earnings and five years of zero income.

Once the SSA has determined your averaged indexed monthly income, a complex formula is used to determine your primary insurance amount (PIA). It's the amount you'll get each month if you start claiming benefits when you reach your full retirement age.

Taking Social Security before your full retirement age reduces your benefits by 5/9 of 1 percent for each month before your full retirement age, up to 36 months. If you claim benefits more than 36 months before your FRA, the amount is further reduced by 5/12 of 1 percent for each month. Also keep in mind that if you start collecting social security before full retirement age, your benefit may be reduced if you also work. For 2022, if you collect social security prior to full retirement age, once you make more than \$19,560 your benefit will be reduced by \$1 of benefit for every \$3 you earn. Ultimately, taking Social Security at 62 can cut your monthly benefit by as much as 30 percent. But if you delay benefits, and don't claim Social Security at your full retirement age,

your benefit is increased by as much as 8 percent per year until you reach 70. You don't have to start collecting Social Security at 70, but your benefit amount is capped at this point so consider this the last date you'd conceivably claim benefits.

If your spouse claims spousal benefits on your record, they're entitled to half of your PIA. Spousal benefits are reduced when they're claimed before the spouse's full retirement age, and increased when they're delayed.

Maximizing Social Security Benefits

In most cases, the goal with Social Security planning is to delay benefits for as long as possible. Waiting until 70 locks you into your maximum possible benefit for the rest of your life. But everyone's financial plan is unique; sometimes it makes better sense for someone who needs to retire at 62 to take Social Security early than to tap into their savings, for example.

It's easy to access information that helps you estimate your future benefits. Use your mySocialSecurity account at SSA.gov to see projections based on when you claim benefits. Your financial advisor can then help you evaluate and compare all the potential scenarios to find the Social Security strategy that best supports your goals.

A financial planning strategy is also key for making sure you're on track with long-term retirement goals. Having a financial plan for your 60s that doesn't rely entirely on Social Security allows you to let your benefit grow without sacrificing any comfort in early retirement.



Finding Answers to Common Questions

As a general rule, you won't regret waiting to start taking social security payments. Perhaps you have more nuanced questions, such as, what is your eligibility if you are divorced, or you're not sure which spouse should be the first to start claiming. You can always speak with your financial advisor about your unique circumstances.

As a starting point to understanding your unique circumstances and potential payments, we also recommend creating a portal on the Social Security website. From there you can use their benefits calculator to determine your payment amount based on whatever factors you choose. You can also confirm that the agency has all of your information recorded correctly. An error in your income history, marital status or other details could impact your payment calculation. Confirm the accuracy of your information to help ensure you're not leaving money on the table. In fact, if you were to come to our office, this is the first thing we would do together to start to discuss your benefits.



Disability Insurance

Usually when people talk about Social Security benefits, they're talking about retirement benefits. However, Social Security also pays out benefits for people who are permanently disabled through the Social Security Disability Insurance (SSDI) program, and provides survivors benefits for family members of deceased workers.

Benefits are paid from the DI fund for individuals who qualify for Social Security disability benefits. SSDI is available to people who are disabled or blind, and who have paid into Social Security in the past. This program differs from the Supplemental Security Income program (SSI), which provides for low-income elderly and disabled people; SSI is administered by the Social Security Administration but isn't funded by Social Security taxes.

Eligibility

Like Social Security, qualifying for disability benefits also requires work credits. The number of credits required depends on the person's age at the time they became disabled.

How many credits a person needs to qualify for disability benefits depends on the age at which they become disabled; generally, an applicant needs to have earned at least two work credits per year between the time they turned 21 and the time their disability began. The SSA also requires medical documentation verifying the disability.

Take the Next Step

Planning for retirement can be complicated, and it's never too soon to start. Understanding your Social Security benefit is an important part of creating your long term financial plan. Start by creating your portal on the Social Security Administration website and confirm your account details. From there, discussing Social Security with your financial advisor can help you maximize your benefits and incorporate those benefits into your financial plan following retirement.

Looking for assistance?

The financial advisors at Sachetta are here to help. Contact us today.

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