SOCIAL SECURITY: WHAT'S BEST FOR CLIENTS

By Jim Cornfeld

The traditional view of taking Social Security benefits has been to simply filing for benefits as soon as retirement happens. If people retired at 62, they took benefits then. If they waited until 67, they took benefits then.

However, our job as advisors requires that we make recommendations in our clients' best interests. This includes helping our clients maximize their Social Security benefits. Done correctly, you can add tremendous value to your clients in their retirement years. Our firm has developed a calculator for determining optimum filing strategies, and this often means filing for benefits later than they otherwise would.

Effectively helping clients with Social Security decisions will likely mean knocking down some of their preconceived notions. Specifically, we found there are three big reasons why clients want to take Social Security sooner rather than later:

• They fear that Social Security isn't sustainable, and want their money before government reduces their benefit.

• They fear dying early, so they want to get as much as possible before then.

• They think they can do better by taking Social Security as early as possible and investing it.

Each item involves a legitimate concern, but investors may be missing the overall picture if they latch on to one of these ideas. Let's look at each one separately and see why investors shouldn't fear them.

Sustainability
Certainly, there's been a lot of press about the viability of the Social Security system, and many (if not most) people believe changes are coming. However, the correct response isn't to panic and take out what they can. Social Security should be incorporated into the financial plan, and contingencies should be made.

It's important to note that most of the proposed legislation involves changing Social Security for people still in their working years, or said another way, people who can still make adjustments in their savings to account for potential reductions in Social Security benefits. Such proposed changes include:
• Increasing the retirement age.
• Increasing the maximum income subject to Social Security taxes.
• Increasing the Social Security tax rate.
• Changing the cost-of-living adjustment

This doesn't mean that more drastic measures aren't possible, but it's important to remember that nothing in investing is a given. Financial plans involve projecting rates of return needed to achieve objectives. In many cases, the returns actually experienced by investors don't match with the projections. This can be good (higher returns leading to hitting goals ahead of schedule) or bad (lower returns requiring more risk taking, working longer or scaling back retirement plans).

Investors should think of Social Security in the same light. Advisors can help them project their retirement assuming that Social Security will be around in its current form, then outline what steps would be taken if Social Security were reduced or eliminated.

Benefits Before Death
It's important to remind investors that no matter when they start taking benefits, the total payments will be the same for people living until their average life expectancy. Thus, it doesn't matter if investors begin taking benefits at 62 (earliest) or 70 (latest). Investors would receive the same total benefit (in present value terms) if they lived to their expected lifespan.

But let's say a husband who is the high-earner of a couple is in poor health and doesn't expect to live to life expectancy. The natural instinct may be to take benefits as soon as possible to get the most possible out of the system. However, this may be shortsighted, as he's forgetting about his spouse. Once the husband dies, his wife is eligible for a survivor benefit, based on the amount her husband was receiving. If he took Social Security as soon as possible, he permanently reduced the benefit his wife would receive. Investors who want to take Social Security early need to understand what they're giving up by doing so, and that it's not just about them.

Now, let's suppose the husband's health takes a turn for the better, and he ends up living longer than the average life expectancy. Although filing early would have earned more money prior to average life expectancy, filing later means more money afterwards. In this case, the couple would not only potentially be leaving money on the table for the survivor benefit, but for the regular filing benefit as well.

Investing Benefits

Some clients think they can do better by taking Social Security benefits and investing them, which also means their advisor now has more assets to manage.

However, the key to this decision from an advisor perspective is what to do with the assets. If you had access to an investment that gave your clients about an 8 percent return, wouldn't that be near the top of your list? If so, then tell your clients they should delay taking their benefits.

As an example, let's assume an investor would receive a monthly benefit of $1,000 upon turning full retirement age (or 66). Taking benefits as soon as possible (at age 62) means only receiving $750 per month. Delaying as long as possible (until age 70) means receiving monthly benefits of $1,320 or 76% more.

This compares favorably with purchasing an annuity. Continuing with our example, let's say the investor delays filing for one year, thus giving up $12,000 total in benefits for the year. The following year (at age 67), this investor would receive $12,960 for the year. An annuity (indexed to inflation and with a 100 percent survivor's death benefit) that would make up the difference would cost about $21,000, not the $12,000 given up by delaying Social Security benefits.

If we knew exactly what the Social Security program would look like in the future, how long retirees would live and what future market returns would be for the rest of their lives, we would know exactly what to recommend for Social Security filing. Of course, life is not so simple, and we must develop strategies that maximize the chances for helping clients meet their goals. Social Security benefits can play a major part in structuring a strategy.

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