WHEN SHOULD YOU TAKE SOCIAL SECURITY?

By *Charles Schwab*

Key Points

- Taking Social Security benefits before you reach full retirement age may not be in your best interest.
- We'll cover Social Security benefit eligibility and factors to consider when deciding when to take Social Security.
- The strategies for maximizing benefits can get complex—talk to your financial planner or tax professional if needed.

When you start receiving full Social Security retirement benefits is a key question for your retirement plans. The first thing to understand is that the concept of "full retirement age" is a moving target that depends on your birth year (see table below).

You can elect to take benefits as early as age 62 (or earlier if you are a survivor of another Social Security claimant or on disability), or wait until as late as age 70. There's no "correct" claiming age for everybody. But, if you can afford to wait, starting Social Security later than age 62 can pay off over a long retirement.

Here we'll take a look at some of the rules and guidelines.

What's full retirement age?

Full retirement age (also known as normal retirement age) is when you're eligible to receive full Social Security benefits. The full retirement age used to be 65 for everyone. That has changed.

Under current law, if you were born in 1951 or later, your full retirement age is now some point after age 65—all the way up to age 67 for those born after 1959. If you were born before 1951, you've already reached age 66 and full retirement age.

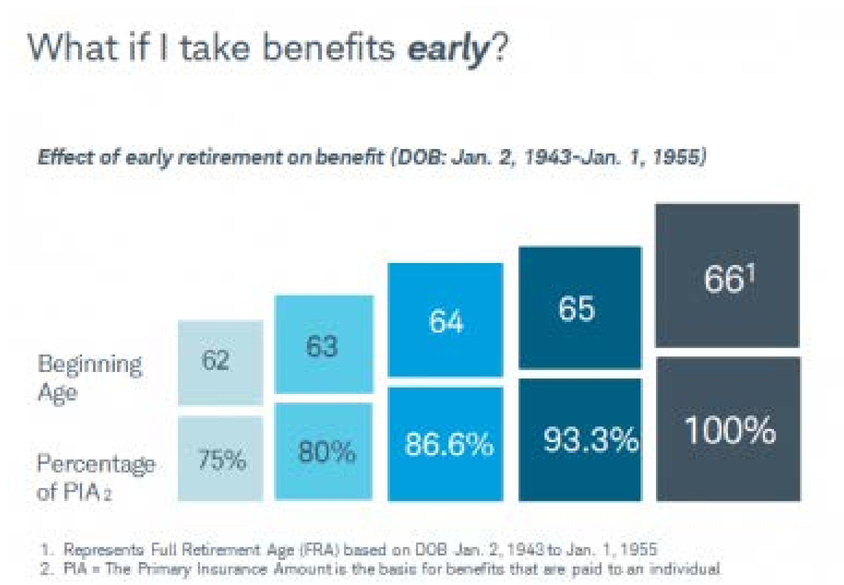
Retirement ages for full Social Security benefits

If you were born in ...	Your full retirement age is ...
1950 or earlier	You’ve already hit full retirement age
1951-1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 or later	67

Source: ssa.gov.

Your full benefit is reduced if you take Social Security early...
If you choose to start receiving your Social Security check up to 36 months before your full retirement age, be aware that your benefit is permanently reduced by five-ninths of 1% for each month. If you start more than 36 months before your full retirement age, the benefit is further reduced by five-twelfths of 1% per month, for the rest of retirement.

For example, if your full retirement age is 66 and you elect to start benefits at age 62, the reduced benefit calculation is based on 48 months. This means that the reduction for the first 36 months is 20% (five-ninths of 1% times 36) and 5% (five-twelfths of 1% times 12) for the remaining 12 months. Overall, your benefits would be permanently reduced by 25%.

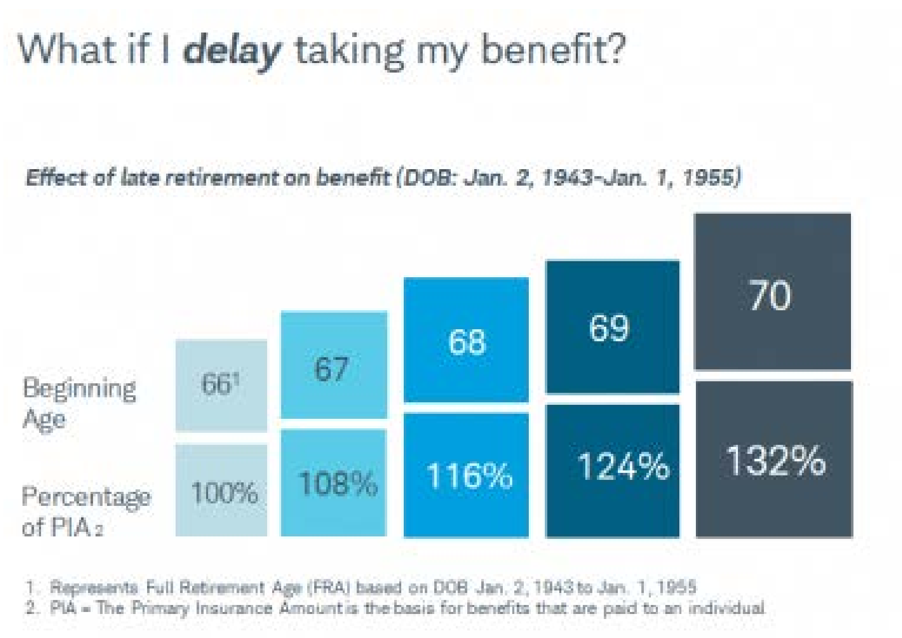


Source: ssa.gov

... and you'll get credit for delaying

If you retire sometime between your full retirement age and age 70, you typically get a credit. For example, say you were born in 1951 and your full retirement age is 66. If you started your benefits at age 68, you would receive a credit of 8% per year multiplied by two (the number of years you waited). This makes your benefit 16% *higher* than the amount you would have received at age 66.

That higher baseline lasts for the rest of your retirement, and serves as the basis for future increases linked to inflation. While it's important to consider your personal circumstances—it's not always possible to wait, particularly if you are in poor health or can't afford to delay—the benefits of waiting can be significant.



Source: ssa.gov.

To review your situation, your annual Social Security statement will list your projected benefits at age 62, full retirement age, and age 70. If you need a copy of your annual statement, you can request one from the Social Security Administration (SSA).

If you feel like it will be difficult to wait, you're not alone. Even though many people in good health would probably be better off in the long term by delaying benefits, more than two-thirds of eligible workers take Social Security early.[1]

Factors to consider

Consider the following factors as you decide when to take Social Security.

1**. Your cash needs**. If you're contemplating early retirement and you have sufficient resources (adequate investments, a traditional pension, other sources of income), you can be flexible about when to take Social Security benefits. However, if you'll need your Social Security benefits to make ends meet, you may have fewer options. If possible, you may want to consider postponing retirement or work part-time until you reach your full retirement age—or even longer so that you can maximize your benefits.

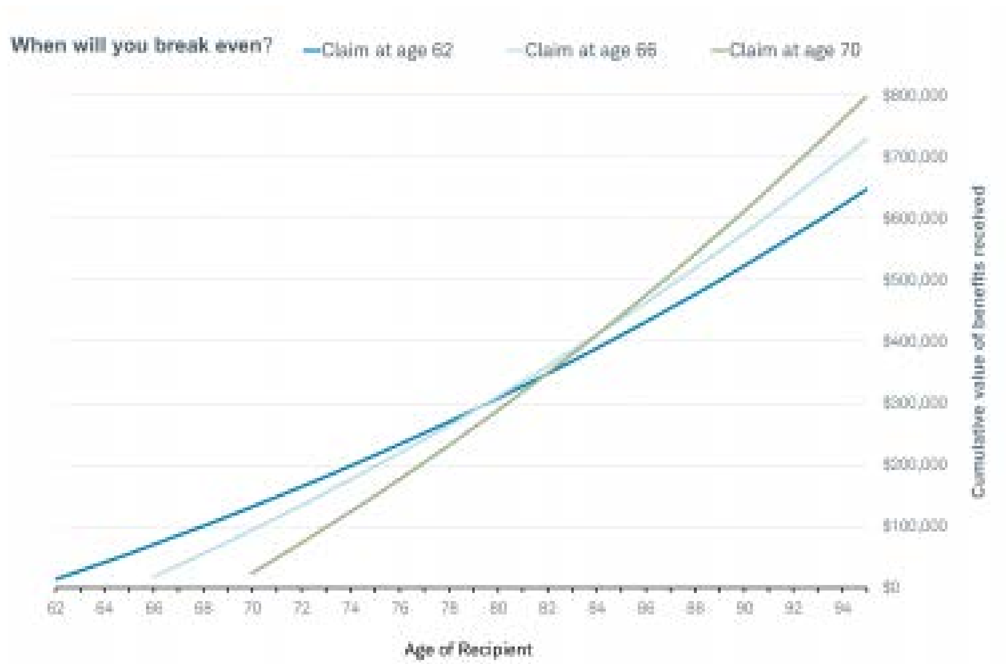
2. **Your life expectancy and break-even age**. Taking Social Security early reduces your benefits, but you'll also receive monthly checks for a longer time. On the other hand, taking Social Security later results in fewer checks during your lifetime, but the credit for waiting means each check will be larger.

At what age will you break even and begin to come out ahead if you delay Social Security? The break-even age depends on the amount of your benefits and the assumptions you use to account for taxes and the opportunity cost of waiting (investment returns you could have made, inflation, etc.).

The SSA has several handy calculators you can use to estimate your own benefits. For example, if you're a top wage earner turning 62 this year, then your break-even ages are as follows:

Monthly Social Security benefits	Retirement age	Break-even age
$2,102	62 vs. 66	Between 77 and 78
$2,806	62 vs. 70	Between 80 and 81
$3,721	66 vs. 70	Between 82 and 83

In this example, if you wait until age 66 to take Social Security instead of taking it at age 62, you'll come out ahead as long as you live to at least age 77-78. The break-even age goes up the longer you wait. See the graph below for an illustration of sample break-even points.



Source: Estimates based on data from ssa.gov, shown in today's dollars, using SSA's Quick Calculator as of 10/31/2017 for a person born 5/1/1954, with earned income equal to or greater than the maximum Social Security wage base. The SAA calculator and table above does not include a cost of living adjustment. The chart above includes 2% annual cost of living adjustment to include that in the break-even calculation. Time value of money is not considered in the example.

Theoretically, it shouldn't matter when you start to receive your checks, provided you have an average life expectancy. However, if you think you'll beat the average life expectancy, then waiting for a larger monthly check might be a good deal. On the other hand, if you're in poor health or have reason to believe you won't beat the average life expectancy, you might decide to take what you can while you can.

While it may be tempting to look only at your break-even point and think about Social Security as a math equation or an investment decision, another approach may be to think about Social Security as a form of insurance.

Unlike conventional investments, Social Security isn't affected by stock market changes, provides protection against inflation and is designed to pay out no matter how long you live. Social Security also provides guaranteed, inflation-adjusted income—which can be expensive and difficult to replicate with investments.

A quick note about life expectancy: According to the Social Security Administration, average life expectancy for a 65-year-old male is 84.3 years and 86.6 for females. Married individuals tend to live even longer, with a greater than average probability of at least one spouse living to age 90. To compute your own life expectancy, use *the life expectancy calculator at SSA.gov.*

Remember, though, that the average is just that—an average. If you have a shorter life expectancy than average, then early withdrawals might be a better option for you. If you don't, starting Social Security later can be particularly beneficial if you live longer than average.

3. **Your spouse**. If you have a spouse covered by Social Security, you can explore additional strategies to maximize the benefits you receive between you. Start by taking your spouse's age, health, and benefits into account, particularly if you're the higher-earning spouse. The amount of survivor benefits for a lower-earning spouse could depend on the deceased, higher-earning spouse's benefit—the bigger the higher-earning spouse's benefit, the bigger the benefit for the surviving spouse.

Strategies for married couples

For spouses with equivalent work histories and life expectancy, it may make sense for both of them to delay their benefits up to age 70, if possible. In other cases, especially when there are material differences in work history, it might make sense for the lower-earning spouse to file earlier while the higher earner waits until age 70. This is called a 62/70 split strategy.

62/70 split strategy

With this strategy, the lower earner files early at age 62 (or at full retirement age) based on his or her own benefit. The higher earner later files at age 70.

When a lower-earning spouse files for benefits at age 62, the benefits are reduced based on the number of months before full retirement age.

- If the higher earner has not yet filed, the reduced benefit will be based on the early filer's own earnings record.
- If the higher-earning spouse has already filed for benefits at his or her own full retirement age, the lower earner would receive an amount equal to 35% of the higher earner's full retirement age benefit or their own benefit, whichever is greater.

Even though an early-filing penalty would still apply to any benefits the lower-earning spouse received before full retirement age (whether they're calculated based on that spouse's own earnings record or the higher-earning spouse's record), in the event of the spouse's death, the surviving spouse would be entitled to their own, or their spouse's benefit, whichever is higher. In the meantime, the lower earner can still collect something while the higher earner waits until age 70 for their maximum benefit.

In the past, couples were allowed to use a strategy called “file and suspend,” under which the higher-earning spouse would file and suspend their benefit at full retirement age, and then wait until age 70 to start collecting, so their partner could claim a spousal benefit. However, that strategy is no longer permitted.

In addition, unless you turned 62 before Jan. 1, 2016, you can no longer file a “restricted application” to claim a spousal benefit. If you are grandfathered into this option, however, you can still consider it. Here’s how it works: At full retirement age the lower earner could file for his or her own benefit, while the higher earner would file a restricted application for spousal benefits. The higher earner would then wait until age 70 to switch to his or her own benefit, at which time the lower earner would switch to a spousal benefit, if higher than their own.

The process of trying to optimize your Social Security benefits over a joint lifespan can be complex. Talk with an advisor (such as a Schwab Financial Consultant) to provide an assessment and help with options.

4. **Whether you’re still working**. Earning a wage (or even self-employment income) can reduce your benefit temporarily if you take Social Security early. If you’re still working and you haven’t reached your full retirement age, $1 in benefits will be deducted for every $2 you earn above the annual limit ($16,920 in 2017).

The reduction falls to $1 in benefits deducted for every $3 you earn above a higher limit ($44,880 in 2017), deducted only for income earned before the month you reach your full retirement age in the year you reach your full retirement age. Starting the month you hit your full retirement age, your benefits are no longer reduced no matter how much you earn.

Again, any reduction in benefits due to the earnings test is only temporary. You receive the money back in the form of a higher benefit at full retirement age, so don’t use the reduction as the sole reason to cut back on working or worrying about earning too much.

Taxes on Social Security

Keep in mind that Social Security benefits may be taxable, depending on your modified adjusted gross income (MAGI), also known as “provisional” income. Your provisional income is equal to your adjusted gross income (AGI), plus non-taxable interest payments (e.g. interest payments on tax-exempt municipal bonds), plus half of your Social Security benefit. As your MAGI increases above a certain threshold (from earning a paycheck, for instance), more of your benefit is subject to income tax, up to a maximum of 85%. For help, talk with a CPA or tax professional.

In any case, if you're still working, you may want to postpone Social Security either until you reach your full retirement age or until your earned income is less than the annual limit. In no situation should you postpone benefits past age 70.

For more information, see the SSA publication *How Work Affects Your Benefits, and IRS Publication 915: Social Security and Equivalent Railroad Retirement Benefits*.

Changing your mind

If you previously elected to receive early Social Security benefits at a reduced rate, but then change your mind, you have the option of paying back to the government what you've already received. After, you could restart benefits later to take advantage of a higher payout. But you can only do this for one year's worth of benefits.

For example, let's say you elected to receive early benefits at age 62, but then decided to go back to work at age 63. You could stop receiving Social Security, pay back the years' worth of benefits you received, go back to work, and then wait until a later age to restart your benefit checks at a higher level.

For important details about repaying benefits please read the *SSA publication If You Change Your Mind.*

What about the future of Social Security?

Are you skeptical about the future of Social Security or wary of potential changes such as means testing—which could reduce or eliminate benefits for the wealthy—or an increase in the full retirement age? If so, you may be tempted to start benefits early, under the assumption that it's better to have a bird in the hand than nothing.

The 2017 annual report from the Social Security Trustees projects that the Social Security Trust Fund has enough resources to cover all promised retirement benefits until 2035 without changing the current system. Over the longer term, changes such as later benefit dates or means testing (a reduction in benefits based on your other income sources) may be considered.

In any situation, if you're particularly concerned about the future prospects for Social Security, that's a good reason to save more, earlier, for your retirement.

To wait or not to wait? That is the question

Consider taking benefits earlier if …	Consider waiting to take benefits if …
You are no longer working and can’t make ends meet without your benefits.	You are still working and make enough to impact the taxability of your benefits. (At least wait until your normal retirement age so benefits aren’t further reduced due to earnings.)
You are in poor health and don’t expect to make it to average life expectancy.	You are in good health and expect to exceed average life expectancy.
You are the lower-earning spouse and your higher-earning spouse can wait to file for a higher benefit.	You are the higher-earning spouse and want to be sure your surviving spouse receives the highest possible benefit.

The bottom line

If you have a choice and are in good health, think seriously about waiting as long as you can to take your benefits (but no later than age 70). For retirees in good health, a long retirement, coupled with uncertainty about markets and inflation, are the biggest risks. Delaying Social Security, if you can, is effectively an insurance policy against those challenges.

Your situation may differ, however, and there are many factors to consider. Get help from your financial planner if you need it.