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TAX ALERT: BUDGET ACT ELIMINATES STRATEGIES FOR MAXIMIZING SOCIAL SECURITY PAYOUT

The Bipartisan Budget Act of 2015 contains a provision that may significantly affect retirement planning for many Americans, likely costing them thousands of dollars in Social Security benefits.

The provisions eliminate two strategies that many married couples have used to maximize these important retirement benefits. Some couples, however, may be able to take advantage of "grandfathering" and a grace period to continue using the strategies. And certain married and unmarried individuals who act quickly may have an opportunity to use Social Security benefits as a quasi-insurance policy.

Social Security benefits in a nutshell

Currently, the full retirement age to receive Social Security benefits is 66 for those born in 1943 through 1954, and it will gradually rise to 67 for those born in 1960 or later. Full retirement age is the age at which a person may first become entitled to full or unreduced retirement benefits.

Retirement benefits may also be claimed as early as age 62. There are reduced benefits for each month before your normal retirement age, and you could lose as much as 30% of your retirement benefits if you choose to begin receiving them early, according to the Social Security Administration. For example, if you begin taking retirement benefits at full retirement age in 2016, the maximum monthly benefit would be $2,787.80. However, if you retire at age 62 in 2016, the maximum benefit would be only $2,102.

On the other hand, holding off on taking your retirement benefits will result in greater benefits due to "delayed retirement credits." Individuals born after 1942 earn an 8% credit for each year they delay benefits after reaching full retirement age, up to age 70. For example, if you begin taking retirement benefits at age 70 in 2016, the maximum benefit would be $3,576. It is this opportunity to delay and compound benefits that forms the foundation for the two strategies that were eliminated under the budget act.

The file-and-suspend method

Under previous law, upon reaching full retirement age, an eligible Social Security recipient could file for your retirement benefits and then suspend receipt of the benefits until an election was made to begin receiving them (typically at age 70). Under this method, the retiree receives delayed retirement credits during the period benefits are suspended. These credits in turn increase the amount of survivors benefits after death. Why bother filing just to suspend receipt of the benefit? Because a spouse may not claim spousal benefits based on his or her spouse's earnings unless that spouse has already filed for retirement benefits.

This strategy was particularly appealing for married couples where one spouse had earned substantially more than the other. After the higher-earning spouse had filed and suspended receipt of benefits, the other spouse could receive spousal benefits based on the higher-earning spouse's earnings record. Spousal benefits for spouses who have reached their full retirement age are generally 50% less than the higher-earning spouse's full retirement amount.

Under the new law, a spouse cannot receive a Social Security benefit based on the earnings of their spouse unless their spouse is currently *receiving* Social Security retirement benefits. Filing and suspending payments is no longer an option. . Likewise, an individual who suspends his or her retirement benefits may not receive benefits on the basis of another individual's earnings.

The elimination of this strategy may have far-reaching implications, yet some married couples will be able to take advantage of "grandfathering" provisions. Those who have already been using the file-and-suspend method and other eligible individuals who file a claim for benefits within 180 days of November 2, 2015, may continue to use the strategy. In other words, if you are at full retirement age (age 66) before May 1 of this year, you can file and suspend by April 29 in order to preserve your spouse's ability to claim a spousal benefit .Your retirement benefits continue to grow through "delayed retirement credits" until you turn age 70.

The restricted application method

Under the restricted application method (also known as the "claim now, claim more later" method), a spouse reaching full retirement age who is eligible for both retirement benefits and spousal benefits could file a restricted application for spousal benefits only and delay applying for his or her own retirement benefits, allowing those benefits to build. The spouse could switch to his or her own retirement benefits at any time up to and including age 70.

So a higher-earning spouse who has reached full retirement age could delay claiming their own retirement benefits and instead claim spousal benefits (assuming the lower-earning spouse has already filed for his or her retirement benefits). The higher earner grows his or her retirement benefits while receiving 50% of the spouse's full retirement benefit, regardless of whether the spouse has reached his or her full retirement age.

When the higher earner later switches to his or her own retirement benefits, the spouse that previously filed for their own retirement benefits can then switch to a spousal benefit based on the higher earner's retirement benefits at full retirement age (assuming that amount is greater than the spouse's own retirement benefits). This approach allowed some married couples to increase their benefits by tens of thousands of dollars.

Anyone who was born in 1953 or earlier will still be able to file a Restricted Application for spousal (or divorced spouse) benefits, even if the filing occurs in later years.

Social Security benefits as "insurance"

The file-and-suspend method also operated as a quasi-insurance policy to the advantage of both married and single individuals. Prior to the new law, one could file and suspend at full retirement age but later opt to receive a lump-sum payout back to the date of the application.

The new law prohibits the payment of retroactive benefits for those who do not file and suspend before April 29, 2016. Those turning 66 before May 1, 2016 should file and suspend to preserve the option of retroactive payouts.

Be prepared

Even without the file-and-suspend and restricted application strategies available, decisions regarding when and how to claim or otherwise maximize Social Security benefits require careful consideration of many factors including current health, family medical history and other resources. We can review your situation and help you make the right choices regarding these important retirement benefits.

For more information

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