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Social Security Benefits

With all of the discussion on the news recently regarding public employee's pensions, I thought it might be worthwhile to look at the private sector program; Social Security. Based on personal experience, I have found that most people under the age of 40 really don't have a clue how much they will receive in benefits and when they can receive them. So I thought I would shed a little light on the subject in hopes that friends and family members will take the necessary steps now to prepare for their future retirement.

Program Parts

Social Security or the Old-Age, Survivors, and Disability Insurance program (OASDI) includes three major programs:

Retirement:

Provides a monthly income for qualified workers once they reach their retirement age. Retirement benefits depend on contributions made while working. Contributions are based on gross earnings.

Survivors:

Provides a monthly lifetime income to the surviving spouse of a deceased worker once he or she reaches retirement age. The amount received depends on both spouses income while they were working. The program also pays benefits to children under the age of 18 and a surviving spouse caring for them. These benefits end in most cases when the surviving children reach age 18.

Disability:

Program provides monthly income to workers who are disabled and in some cases to their spouses and children under the age of 18. These benefits depend on the workers earning history.¹

As a side note, Supplemental Security Income (SSI) is administered by the Social Security Administration but is a separate program paid for with general tax revenues, not FICA payroll taxes.

Funding

Social Security is funded through payroll taxes (FICA) in which both the employer and the employee pay 6.2% of gross wages up to a limit known as the social security wage base. A tax holiday for 2011 only changed the employee rate from 6.2% to 4.2%. The current wage base is

¹The Heritage Foundation. Social Security Basics. 09/02/2002.

<http://www.heritage.org/research/reports/2002/09/social-security-basics#1>

\$106,800.00. Self-employed individuals pay self-employment tax on their net earnings of which the social security portion is 12.4% (with some minor deductions made on the individuals 1040) up to the maximum wage base.

Eligibility

“As you work and pay taxes, you earn Social Security “credits.” In 2011, you earn one credit for each \$1,120 in earnings—up to a maximum of four credits per year. (The amount of money needed to earn one credit usually goes up every year.)

Most people need 40 credits (10 years of work) to qualify for benefits. Younger people need fewer credits to be eligible for disability benefits or for family members to be eligible for survivors benefits when the worker dies.”²

Retirement Age

There are essentially three categories of retirement ages; Early Retirement, Full Retirement, Delayed Retirement.

Early Retirement

“You may start receiving benefits as early as age 62. However, if you start early, your benefits are reduced. The reduction is about one-half of 1 percent for each month you start your Social Security before your full retirement age. For example, if your full retirement age is 66 and you sign up for Social Security when you are 62, you would only get 75 percent of your full benefit.

NOTE: *The reduction will be greater in future years as the full retirement age increases.”*³

Full Retirement

If you were born from 1943 to 1960, the age at which full retirement benefits are payable increases gradually from 66 to age 67. Anyone born prior to 1943 is already eligible for benefits.⁴Currently, for anyone born after 1960, full retirement age is 67.

Delayed Retirement

“If you choose to delay receiving benefits beyond your full retirement age, your benefit will be increased by a certain percentage, depending on the year you were born. The increase will be added in automatically each month from the time you reach full retirement age until you start taking benefits or reach age 70, whichever comes first. The percentage of the increase is based on when you were born.”⁵

Benefits

So how much can you expect at retirement? Benefits are calculated using a complex formula

²Social Security Administration. Understanding The Benefits, 2011. <http://ssa.gov/pubs/10024.html>

³Social Security Administration. Understanding The Benefits, 2011. <http://ssa.gov/pubs/10024.html>

⁴Social Security Administration. Understanding The Benefits, 2011. <http://ssa.gov/pubs/1002>

⁵Social Security Administration. Understanding The Benefits, 2011. <http://ssa.gov/pubs/1002>

which is based on how much was paid into the program using the workers highest 35 years of earnings. I will write another paper explaining this in more detail. As of this writing, the average monthly social security benefit is \$1,177 or \$14,124 annually.⁶ Not a lot of money. The current maximum benefit for someone who reached full retirement (66 years old) in 2011 is \$2,366 a month or \$28,392 a year.⁷ But keep in mind this would be for someone that contributed the maximum taxable amount for at least 35 years of their working careers, which would not apply to the vast majority of us. In my profession I see a lot of Social Security statements and would say that the average annual benefits were between \$17,000 to \$20,000.

So for someone in my age bracket, if you started working at age 20 and waited till the full retirement age of 67, that is (obviously) 47 years you would have to wait before you could receive benefits. Even if we are a little generous and throw an extra three or four thousand on top of the average, we are still only talking about an annual benefit between \$17,000 to \$18,000. Again, not a lot of money, especially considering the additional health cost which come with aging (as a side note Medicare premiums are often deducted from gross Social Security, so subtract something like another \$1000 to \$1500 from that annual amount). Bottom line, living on Social Security alone would be very difficult. If you are a private sector worker and you are not saving for retirement, start now. If you already are saving, make sure it is enough.

(This of course assumes there will be a Social Security program in the future and that it is not radically changed. I look at some of the issues facing the program in my Blog titled "Federal Debt II")

⁶Social Security Administration. Average monthly Social Security benefit for a retired worker.

http://ssa-custhelp.ssa.gov/app/answers/detail/a_id/13/~/average-monthly-social-security-benefit-for-a-retired-worker

⁷Social Security Administration. Maximum Social Security Retirement Benefit.

http://ssa-custhelp.ssa.gov/app/answers/detail/a_id/5/related/1/session/L2F2LzEvdGltZS8xMjk5MjQ2NTYyL3NpZC9ickNWSzRvaw%3D%3D