Kiplinger

How Misinformation from Social Security Can Cost You Tens of Thousands of Dollars

We'll put you on the right path to maximize your benefits.

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Social Security will pay out nearly $1 trillion in benefits this year. For more than half of all recipients, the payments are more than 50% of their retirement income. But for the eighth year in a row, this critical pay-as-you-go program will take in less in taxes than it pays out in benefits. If nothing is done to change the system and the economy behaves as expected, a financial catastrophe demanding across-the-board benefit cuts will arrive in 18 years.

You've heard this lament before, of course, along with assurances that, sooner or later, members of Congress will get around to doing something to shore up the system. But focusing on the long-term crisis masks a much more immediate threat, one that can explode long before 2035—perhaps when you, or someone you know, walks into a local Social Security office, takes a number and waits to talk with an agent about claiming benefits. The chances are all too good that you will get incomplete or misleading information that could cost you a small fortune in missed benefits.

That's what happened one day last December to Joseph and Christine Biernat of Southington, Conn. Their goal was to arrange for Christine's benefits to start flowing when she turned 65 in February 2017 and to check out Joe's options. Social Security got it half right.

Christine, a registered nurse who spent many of her working years as a homemaker, knew that her "full" benefit of $814 would be trimmed to $762 because she was claiming a year before her full retirement age (FRA is 66 for those born from 1943 through 1954 and will gradually increase to age 67 for those born later). Applying was a breeze, and she got her first payment via direct deposit in March.

Joe wasn't so lucky. He knew he had just missed the deadline for a potent claiming strategy known as file and suspend, which allowed older married beneficiaries to claim benefits at FRA, then immediately suspend the claim. The maneuver opened the door for a spouse to claim benefits on the worker's record while he built up delayed-retirement credits to boost his own benefit by as much as 32% by age 70. Congress abolished the file-and-suspend strategy as of spring 2016. But, Joe asked, wasn't there a way he could claim spousal benefits on Christine's record while waiting for his own benefit to grow?

Afraid not, he was told. Congress eliminated that option, too.

That was fake news.

A second opinion

A couple of weeks later, Joe sat down with the latest edition of our sister publication ***Kiplinger's Retirement Report***. He "read and re-read and re-read again" a story explaining that the strategy to restrict an application is still available. When Congress changed the rules, lawmakers kept the door open for those who turned 62 by January 1, 2016. At age 66, they can claim benefits on a spouse's record to pull in some cash while allowing their own benefit to grow by 8% a year until age 70.

Joe returned to the Social Security office and uttered what turned out to be the magic words: *restricting an application*. "As soon as I said that, I could see the question marks going off in the person's head," he says. He was soon meeting with a supervisor who fully understood the rules and walked Joe through the application.

He's now receiving a spousal benefit of $407 a month—half of Christine's full-retirement-age benefit. In addition to the financial help, the benefit simplifies Joe's life. His Medicare Part B premium is subtracted from it, so he doesn't have to worry about paying that bill. The leftover amount is more than enough to pay the premiums for his medigap policy. (This strategy is called restricting an application because Social Security usually pays you the highest amount you deserve automatically, including the benefit based on your own work record. At age 66, though, those who qualify can restrict their application to receive spousal benefits only, so their own benefit can accrue delayed-retirement credits.)

Had Joe filed for his own benefit when he turned 66 in March, he would have received $2,615 a month. Now he plans to collect the spousal benefit until he's 70. At that point, he'll switch to his own supercharged benefit of $3,452 (plus all intervening cost-of-living adjustments). When Joe claims his benefit, Christine will switch to a spousal benefit based on Joe's record, boosting her benefit to about $1,300 a month.

Depending on how long Joe and Christine live, the couple could have missed out on tens or even hundreds of thousands of dollars of lifetime benefits had they accepted the misinformation doled out on their first visit to Social Security.

Bad advice is not a fluke

It would be nice to think the Biernats' story is an isolated incident. But despite Social Security's best efforts, with about 10,000 baby boomers applying for benefits every day, far too many fall through the cracks.

Mary Beth Franklin of Falls Church, Va., a former senior editor of this magazine, is now a certified financial planner who specializes in training advisers to help their clients get the most out of Social Security. She says she hears a steady drumbeat of complaints about "the bad advice that Social Security is giving." Most of the problems, she says, revolve around the restricting-an-application strategy. "I'm hearing from people who clearly are eligible to file a restricted claim for spousal benefits and are being denied the opportunity to do so." She points out that this strategy will be available for several more years. The last eligible workers will turn 66 on January 1, 2020. (If you were born on or before January 1, 1954, but are not yet 66, it's up to you to check into this opportunity if you are married or divorced when you reach that age.)

Franklin, a contributing editor for InvestmentNews, says she has also heard from applicants who have been told they can't claim spousal benefits until age 66. But spousal benefits can be claimed as early as age 62 if your husband or wife has claimed benefits. (You must be 66 to file a restricted application for spousal benefits only.)

Such problems are no secret. Last year, the Senate Special Committee on Aging held a hearing on how to help Americans make the most of their Social Security benefits. Sen. Susan Collins (R-Maine) set the stage: "Deciding at what age to begin claiming Social Security retirement benefits is the single most important financial decision that many Americans will ever make," she said. "Few, however, understand that making the wrong choice can end up costing them tens of thousands of dollars, or more, during their retirement years."

A Government Accountability Office study presented at the hearing showed that although Social Security provides a great deal of information to the public, "field offices . . . were not consistently provided key information that people may need to make well-informed decisions" about their benefits.

William Meyer, a witness at the hearing, was more blunt: "Currently, the Social Security Administration is providing neither the 'right' nor 'enough' information for someone to make an informed decision" on when and how to claim benefits. Meyer is the founder of Social Security Solutions, which has developed sophisticated software to help users maximize their lifetime benefits.

Beyond the restricting-an-application snafu that nearly tripped up the Biernats, be aware of these areas where misleading information or lack of information can cost you dearly.

Penalties and bonuses

You may know that if you claim benefits at the earliest possible age (62), you'll get 25% less than if you wait until your full retirement age. That's often derided as a *penalty* for claiming early. And if you postpone claiming past full retirement age, you earn delayed-retirement credits at a rate of two-thirds of a percent a month (8% a year). That's the sweet *bonus* for waiting.

These factors are Social Security actuaries' best effort to make sure that no matter when you start benefits, you'll receive about the same amount of total dollars before you die, assuming you die at the end of your estimated life expectancy.

For those with a full retirement age of 66, waiting until 70 means receiving 32% more than they would have received at 66 and about 76% more than if they had claimed at age 62. That enormous gap might lead you to believe most people wait. *Au contraire!* In fact, more than 45% of beneficiaries sign up as soon as possible, and about 75% claim benefits prior to FRA. Only about 3% wait until age 70.

Collins notes that there are many reasons people might want to begin receiving benefits as soon as possible—poor health, for example, or because their jobs require physical labor they can no longer perform. But in many cases, they could be unaware of the lifetime consequences of claiming sooner rather than later. The GAO cited a survey showing that 36% of respondents either didn't understand how benefits are adjusted or thought they'd receive the same amount no matter when they started benefits.

Social Security doesn't necessarily help on that score. For one thing, the GAO noted, telling claimants that lifetime benefits should be about the same for anyone who lives to average life expectancy, regardless of when they claim, may unintentionally convey to claimants that "the decision on when to claim does not matter." Social Security agents are not supposed to give advice on when to claim, but they are expected to provide accurate information to help workers decide what's best for them. Yet in eight of 26 in-office sessions observed by GAO researchers, agents did not mention the fact that delaying a claim would result in higher benefits for the claimant and, potentially, for his or her surviving spouse.

Break-even backfire

One point Social Security is not supposed to discuss when you're deciding when to claim benefits is how long it would take for higher benefits, due to later filing, to make up for the benefits missed while you delayed. Let's say your full benefit at 66 is $2,000 a month. If you claim at 62, you'd get $1,500, but if you delayed to 63, your benefit would be $1,600. By waiting a year, you'd give up $18,000 in order to get an extra $100 a month starting at 63. It would take 15 years of that extra $100 to make up the $18,000 you left on the table. Your break-even age would be 78.

That might seem like a sound analysis. But it can mislead, GAO says, "in part because people fear the potential loss of benefits if they die early more than they fear outliving their retirement savings." It also ignores the impact of cost-of-living adjustments, which would shorten the break-even time frame, and the potential benefits of delaying for a surviving spouse.

The Social Security website used to have a break-even calculator, but it was determined several years ago that it could mislead applicants into claiming benefits sooner than would be in their best interest. Although Social Security has removed the calculator and advised agents not to discuss the issue, in six of 26 office visits observed by GAO researchers, claims specialists presented a break-even age. In one case, the agent said the break-even analysis showed "it pays to file early."

Applying online won't necessarily protect you from well-intentioned but misleading advice. A Washington, D.C., woman reports that after she filed online for benefits to start in two months, when she reached her FRA, she got a call from a Social Security agent to review her application and to suggest that she start her benefits right away. It would take years, he told her, for the slightly increased benefit to make up for the loss of two months' benefits. She agreed—and will receive reduced benefits for the rest of her life.

Beware retroactivity

If you're older than 66 when you apply, don't be surprised if an agent offers you what sounds like a great deal: the chance to pocket up to six months of retroactive benefits in a lump sum. If your full benefit is $2,200, for example, that could put $13,200 in your pocket.

Before you bite, though, recognize this: Taking the offer effectively means filing six months earlier—and forfeiting six months' worth of delayed-retirement credits. Taking the lump sum would mean reducing benefits by 4% for the rest of your life.

The official Social Security manual advises agents on how to determine eligibility for retroactive benefits, but it does not instruct them to tell claimants that taking the dough will result in permanently lower future benefits. In fact, in only one of the live visits the GAO observed did the agent explain the trade-off.

Whether claiming sooner rather than later will pay off depends, of course, on how long you (or your spouse, if you're married) will live to collect benefits. The GAO study notes that increasing life expectancies raise the potential cost of claiming early. Social Security says the average life expectancy for a 65-year-old man is age 84.1, and it's 86.5 for a 65-year-old woman. Remember, those are averages. About one in every four 65-year-olds will live past 90, and one in 10 will live past 95.

Retroactive benefits don't always come with a dark side. A Chicago-area executive was 67 when he first heard of the restricting-an-application strategy mentioned earlier in this story, and his wife was already receiving benefits. When he applied for spousal benefits only, he got six months' worth retroactively in a lump sum and is now receiving about $250 a month as he builds up delayed-retirement credits for his own benefit. The lump sum won't affect that benefit when he switches to it.

Survivor protection

One argument for claiming benefits as soon as possible is that if you die before you reach average life expectancy, or before you claim benefits, you'll get less than you deserve. But that's not necessarily true if you are married, or used to be.

Megan Hess, a physician in Altoona, Pa., died last summer at age 55, the victim of metastatic breast cancer. That was seven years before she could apply for retirement benefits. For most of her career, Hess earned a good salary and paid the maximum Social Security tax on her earnings. Was it all for naught? Far from it.

Her husband, Christian, a stay-at-home dad while their two sons grew up, is now receiving $2,344 a month in survivor benefits based on Megan's earnings record. This is a clear reminder that Social Security is an insurance plan as well as a retirement program. When a worker dies before full retirement age, the survivor benefit is calculated as if she had reached FRA. The estimate on the deceased worker's most recent Social Security benefits statement is a close approximation of what the surviving spouse will receive. A survivor can take the benefit as early as age 60 (or as early as 50 if disabled), but the benefit is reduced if claimed before full retirement age.

Because the survivor benefit far exceeds the benefit on his own work record, Christian will collect it for the rest of his life. In some cases, though, it pays for a widow or widower younger than 70 to claim a survivor benefit first, permit his or her own benefit to grow with delayed-retirement credits, and then switch to the higher benefit at age 70. Divorced spouses may also qualify for a survivor benefit, if the marriage lasted for at least 10 years and the survivor did not remarry before age 60.

Social Security is enormously complex, and you need to arm yourself with information to navigate the system successfully. The program's website, **www.ssa.gov**, is packed with helpful information and calculators.

One of the best ways to avoid bad advice from Social Security may be to avoid talking with a live person. CFP Franklin says the easiest and surest way to file a restricted application for spousal benefits, for example, is to do it online. If you visit a Social Security office or discuss benefits with an agent over the phone, be prepared to ask plenty of questions, and ask to talk with a supervisor if you need clarification on any point.

The not-so-rosy future

Payroll taxes being paid into Social Security are no longer enough to cover the benefits being paid out. The shortfall was $73 billion in 2015.

For now, the deficit is being made up by interest earned on nearly $3 trillion in the Social Security trust fund. But in a couple of years there won't be enough interest to fill the growing gap. Starting in 2020, the program will begin dipping into trust-fund principal to meet its obligations. The latest estimates suggest that by 2035, the trust fund will run dry. At that point, tax revenues will cover just 77% of promised benefits.

No one expects benefits to be cut by 23% come 2035. Everyone believes that Congress will eventually do something to fix Social Security. Many "solutions" have been proposed over the years, from raising the tax rate paid by employees to hiking the retirement age to slowing cost-of-living increases to privatizing a portion of the system.

Rep. Sam Johnson (R-Texas), chairman of the House Ways and Means Social Security subcommittee, has come up with a proposal he says will "permanently save Social Security." Among other things, he would gradually hike the full retirement age, now scheduled to be 67 for those born after 1959, to 69; change the way cost-of-living adjustments are calculated; and eliminate COLAs altogether for higher-income beneficiaries. Johnson's plan also calls for ending the "earnings test" and, by 2054, making benefits tax-free. President Trump campaigned on a promise not to change Social Security. He sees its salvation in a stronger economy pumping more tax revenue into the system.

We'll keep an eye on all the machinations in Washington. In the meantime, as the accompanying story points out, it's up to you to make the most of the system as it stands.

Earnings-test misunderstanding

Although the law says it's fine to claim benefits as early as age 62, you can't necessarily collect the cash if you keep working. If you apply for Social Security prior to your FRA, you'll be asked whether you plan to keep working and, if so, how much you expect to earn. Your answers determine whether and how severely you'll be stung by the earnings test.

For 2017, the test applies if you make more than $16,920. For every $2 you earn over that limit, you'll lose $1 in benefits. Suppose you claim benefits at age 62, your monthly benefit is $1,500 and you estimate that you'll earn $30,000 during the year. Because $30,000 is $13,080 over the limit, you would lose $6,540 in benefits—half of the amount by which your earnings exceed the limit. (A less stringent test applies in the year you reach full retirement age, and once you reach that age, earnings cannot squeeze your benefits.)

Although the earnings test is often derided as an unconscionable 50% surtax—because $2 in earnings can cost you $1 in benefits—it's not as evil as critics complain. Benefits lost to the test are not gone forever. Rather, the law is designed so that you recover any forfeited amount via higher monthly benefits later.

Unfortunately, the payback side of the earnings test isn't well known. The Government Accountability Office study mentioned in the accompanying article cited a survey that found that 71% of those questioned thought the reduction in benefits was permanent. And in only seven of 17 observed claiming sessions did Social Security agents explain that any benefits withheld due to the earnings test would be repaid when benefits were recalculated at FRA.