FIVE COMMON MYTHS ABOUT SOCIAL SECURITY

By: David Stubblefield, CFP®, CDFA®

There's no doubt about it—Social Security is an important and popular source of retirement income for most Americans. According to a recent AARP survey, it's supported by more than 90% of the population and critical to older Americans' financial health, with four out of five of those polled expecting to rely on Social Security during their later years.[1]

Of course, Social Security provides a cash benefit during your retirement years. But perhaps during your retirement planning process you discovered it's a smaller portion of retirement income than what you likely expected or would need to live on through your later years. With that important piece of knowledge in hand, you probably focused on saving as much for retirement as possible by contributing to tax-deferred vehicles such as Individual Retirement Accounts (IRAs), 401(k)s, and employer-sponsored plans, as well as investing in stocks, bonds, mutual funds, and annuities.

YOU'RE IN GOOD COMPANY

Likely Social Security benefits are a big part of your retirement financial plan. You're not alone—according to a recent "U.S. News and World Report" article, approximately 65 million Americans received Social Security benefits amounting to more than $1 trillion during 2020.[2]

Yet many Americans, even those who are already retired and receiving benefits, still struggle with fully understanding how the Social Security system works. There are too many misconceptions about the program to tackle here, but hopefully we can provide some clarification around five of the most common myths.

MYTH #1: SOCIAL SECURITY GRANTS FULL RETIREMENT BENEFITS AT AGE 65.

Let's start at the beginning. It's true when Social Security was created back in 1935, the age of 65 was established as the age of eligibility to draw full retirement benefits. Later on, the minimum eligibility age was lowered to 62 years so individuals could claim a reduced benefit. However, at that time 65 years remained the age for collecting full retirement benefits.

But in 1983, in order to reduce Social Security costs, the government raised the full retirement age to 66. Currently this is the threshold for when workers qualify to file for 100% of the benefit based on their lifetime earnings history. Individuals born in 1954 reached that milestone in 2020.[1]

Over the next five years the threshold increases by two months each year, settling at age 67 for those born in 1960 and beyond.

WHAT IS YOUR FULL RETIREMENT AGE?

If you were born in:	Your full retirement age is:
1943-1954	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 and later	67

Note: If you were born on January 1 of any year, refer to the previous year to determine your full retirement age.

MYTH #2: SOCIAL SECURITY IS SIMILAR TO A RETIREMENT SAVINGS ACCOUNT.

Contrary to popular belief, your Social Security account is not like a retirement savings account. The government doesn't put your payroll tax contributions in a personal account for you to accrue interest and be paid out upon your retirement. In reality, your Social Security benefit is calculated on your earnings during your working years, not on the money you contributed to the program. Social Security is essentially a pay as you go system where current retiree benefits are paid by current payroll taxes.

According to AARP, Social Security equals about 40% of a beneficiary's preretirement earnings. Calculations are weighted so benefits replace a higher percentage of income for lower-wage workers and a lower percentage of income for upper-income earners.[1]

With all the focus on retirement benefits, it's easy to overlook the fact that the program also offers protection against long-term disability. Once you receive retirement or disability benefits, your family members may be eligible to receive benefits too.

Another valuable source of support for your family is Social Security survivor's insurance. If you were to die, certain members of your family—including your spouse, children, and dependent parents—may be eligible for monthly survivor's benefits to help replace lost income.

MYTH #3: INDIVIDUALS EARNING MONEY AFTER RETIRING WILL LOSE THEIR SOCIAL SECURITY BENEFIT.

If you earn wages and take your social security benefit prior to full retirement age there are limits on to how much you can draw from social security based on your earnings. If you face this type of social security reduction based on earnings your social security benefit will be a little bigger later. You don't permanently lose any benefits, they are "rearranged". Once you reach full retirement age, you can earn as much as you want without affecting your benefit. If you are under full retirement age, $1 in benefits will be withheld for every $2 you earn under a certain annual limit. For 2021 that limit is $18,960.[3]

- In the year you reach full retirement age, $1 in benefits will be withheld for every $3 you earn above a certain annual limit until the month you reach it. If you reach full retirement age in 2021, that limit is $50,520.[3]
- There is no limit for workers who are full retirement age or older for the entire year.[3]

MYTH #4: SOCIAL SECURITY BENEFITS ARE NOT TAXABLE.

This was true until 1984—at that time the Social Security overhaul passed by Congress the previous year included a provision that made a portion of the benefit taxable depending on your income level. You pay federal income tax on up to 50% of your benefits if your annual income is $25,000 to $34,000 for an individual filer and $32,000 to $44,000 for a couple filing jointly. Above those thresholds, up to 85% of benefits are taxable.[1]

Because the rules on state taxing vary widely, you should consult your tax advisor about any taxes you may owe on your Social Security income.

MYTH #5: I DON'T GET BENEFITS BECAUSE I NEVER WORKED OUTSIDE THE HOME.

If your spouse worked and qualified for Social Security you are entitled to a spouse's benefit up to half the amount of the working spouse's benefit. In fact you can qualify for spousal benefits on an ex-spouse if you were married 10 years or longer.

STILL HAVE QUESTIONS?

Regardless of whether you're already retired or just starting to plan for this important milestone, it's important to answer your questions about Social Security in the context of your broader retirement plan. Contact Commerce Trust Company today—we will answer your questions, evaluate or update your retirement plan, and discuss other income and cash flow options that can help supplement your benefits.

[1] Andy Markowitz, AARP, "10 Social Security Myths That Refuse to Die," https://www.aarp.org/retirement/social-security/info-2020/10-myths-explained.html#, updated September 20, 2020.

[2] Rachel Hartman, "8 Myths About Social Security," https://money.usnews.com/money/retirement/social-security/articles/myths-about-social-security, U.S News & World Report, July 8, 2020.

[3] Source: Social Security, "Cost of Living Adjustment (COLA) Information for 2021," https://www.ssa.gov/cola/, accessed January 18, 2021.

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David is a financial planner with Commerce Trust Company. He is a member of the financial advisory services team, a dedicated financial planning practice within Commerce Trust that provides objective financial advice to clients. Following a thorough assessment of a client's unique situation and thoughts regarding wealth, David develops holistic and coordinated plans to help clients meet their short-term and long-term goals as well as take full advantage of various planning, tax, and investment strategies along the way. His areas of focus includes planning for financial independence, retirement, divorce, executive compensation, estate preservation, and business succession. David joined Commerce in 1995 and has held positions in private banking, credit analysis, commercial business development, and retail sales. David received his bachelor of science degree in business administration from Southeast Missouri State University. He holds both the CERTIFIED FINANCIAL PLANNER™ and Certified Divorce Financial Analyst™ designations. Additionally, David is a member of the Financial Planning Association and the Institute for Divorce Financial Analysts.