Social Security Considerations in Estate Planning

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The ideas in this presentation are for consideration and discussion among financial service professionals. The speakers are not engaged in the practice of law, and any concepts presented or discussed should *not* be taken as specific legal or tax advice.

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Introduction

- Why Social Security is an estate planning issue
- COVID-19 has brought the issues to the forefront
- Viewing Social Security as an estate planning concern make for better consumer decisions

- New research
- Socioeconomic and demographic considerations

Current Update - findings from 2021 Annual Trustees Reports (8/30/21)

- Factors in the effects of the COVID-19 pandemic: employment, earnings, interest rates and GDP
- OASI trust fund reserves will deplete in 2033 — one year sooner than the 2020 Trustees report projected
- The long-range 75- year actuarial deficit of the combined OASI and DI trust funds increased from 3.21% to 3.54% of taxable payroll since the 2020 reports
- The total fertility rate was raised from 1.95 to 2 births per woman
- The unemployment rate was reduced from 5% to 4.5%.

Current Update – possible outcomes from 2021 Annual Trustees Reports (8/30/21)

- Upon trust fund depletion, continuing tax income will be sufficient to pay 76 percent of benefits
- The Average Wage Index (AWI) is predicted to rise to 6.3% in 2021, meaning benefits to recipients born in 1960 and later might not be cut sharply, if at all.
- Congress has been awaiting these reports, and may now act upon them
- COL feature measure may be changed to the chained CPI approach
- Because of solutions likely to be used, planners may be assuming a benefit haircut for younger workers

Current Update

Socioeconomic factors that impact longevity:

Gender: After 62, the average life expectancy for women is 89.6; 87.3 years for men.

Income: lower mortality rates are associated with higher lifetime earnings.

- The richest 1 percent of men live 14.6 years longer than the poorest 1 percent; 10.1 years for women.
- The richest 10% live for approximately 2 years longer than the poorest 10% for white women, slightly under 2 years longer for men, and 4 years longer for black women
- Nearly 30 percent of women are the bread-winners in opposite-sex married households.

Current Update

Socioeconomic factors that impact longevity:

Education: Longevity for college-educated women is 2-3 years longer than non-college educated women.

- The percentage of women with 4-year college degree increased from 11 percent to 40 percent (aged 26-30).
- For individuals born after 1961, women are more likely to hold a college degree.

Current Update

Socioeconomic factors that impact longevity:

Employment:

- Labor force participation rates have increased 10% for women above age 60 between in the past two decades.
- 37% of women worked in 1950 vs. 71% of women work today (aged 20-64)
- Women-held “white collar” jobs increased by 22 percent from 1975 to 2010.

What does this mean? Higher-earning, college-educated women have the greatest life expectancies and highest longevity risk, making retirement planning even more important.

Social Security as a Retirement Benefit

- Benefit: 40 quarters; Primary Insurance Amount at full retirement age; COL feature
- File between age 62 and 70 (32%+ difference), with earnings limit before FRA
- Spousal benefit based on higher of the two benefits
  - MAX total benefit (2021): @70 $56,664 while both retired; $46,740 at death of either
  - No longer a “file and suspend” feature, but can switch benefits at death
  - Divorcees (10 years or more) do not have to wait for ex-spouse to file

Social Security as a Death Benefit

- Importance of spousal benefit as an estate planning tool
  - Surviving spouse can claim the higher monthly benefit
    - For non-working spouses, this is a valuable benefit
  - Dependents: survivor benefit paid to a child = 75% deceased parent's benefit
  - Subject to a maximum family cap/yr

To Claim or Not to Claim?

Claiming at age 62 results in a lower benefit over a longer remaining life expectancy.

Delayed claiming results in a higher benefit over a shorter life expectancy.

Which strategy is best? In a low interest rate environment, wealthy and healthy individuals (especially women) receive the greatest benefit by delaying claiming to age 68-70. When planning as a couple, generally, higher-earning spouses should claim last.

Women Benefit the Most From Delayed Claiming

Most women claim social security at age 62, and women are more likely to claim before reaching full retirement age.

What is the quantitative benefit of delaying social security for higher-earning women?

- Delaying SS claiming from age 62 to age 70 results in a GAIN of $179,999 for healthy women and $132,202 for women of average health (more than twice the value of delayed claiming for a males).

**using current low-interest rate environment*

Women Benefit the Most From Delayed Claiming

- Even with a 2 percent increase in real discount rates *and* a 21 percent reduction in income that may be imposed if the Social Security trust fund depletes in 2026, all women and most men benefit from delayed claiming.
  - The quantitative benefit ranges from $4,951 to $15,890 per year for healthy women.
  - Men of average health should avoid delayed claiming in a higher interest rate environment.

Women Benefit the Most From Delayed Claiming

Impact of delayed claiming on other assets:

- Delayed claiming increases the longevity of a $700,000 portfolio by 10 years*. Why?
  - Higher social security payments in later years require less drawdown from the portfolio when claiming begins
  - Taxation period for the social security benefits is compressed

*assuming 4 percent annual consumption over a 30-year period. Study conducted by Meyer and Reichenstein (2010).

Tax Considerations –Middle-class tax torpedo

- Income from tax-deferred retirement account distributions is treated harshly in the calculation of provisional income (PI). As PI rises, so does the tax on Social Security benefits. This can result in a marginal tax rate well above the current top rate of 37%.

- A possible outcome is depletion of remaining assets for surviving spouse and heirs

- The solution is to first draw down other assets and income, while delaying filing for Social Security until age 70. This increases the benefit while avoiding/lessening the tax torpedo

Tax Considerations – HNW and affluent retirees

- ISSUE: Is Social Security longevity insurance or an investment with a break-even point?
- CONSIDERATIONS:
    - COL benefit is difficult to replicate in an investment portfolio
    - HNW individuals often have better longevity, accelerating the break-even point
    - Replacing the benefit with a commercial annuity is cost prohibitive
    - The increased income from delaying could augment QTIP and related cashflow strategies
    - Affluent and HNW can usually afford bridging strategies needed in order to delay filing

Diminished Capacity Considerations

- Social Security advantages
  - Fixed income versus portfolio drawdown
    - SS benefits can be used for fixed living expenses (eg, LTC premiums), allowing other assets to grow
    - Less elder abuse risk than a large retirement account
  - Part B Medicare premium is subtracted from Social Security payment
  - COL benefit built in

Diminished Capacity Considerations

- Social Security Protections
  - Direct deposit
  - Representative payee program
    - SSA does not recognize powers of attorney!
    - Representative payee: Allows claimant to designate up to 3 representative payees. SSA must evaluate and approve the payee. Payee manages benefit payments on behalf of the claimant.
    - Protects against loss, theft, and scammers.

Social Security issues at death

- Each year the identities of nearly 2.5 million deceased Americans are used fraudulently*
- Coordinate with funeral home to [Report the death to Social Security]: call 800-772-1213
- In obituary, avoid dates of birth, maiden names, addresses
- Notify credit bureaus, department of motor vehicles, etc.

    - ❖ fraud prevention firm ID Analytics.

Conclusion

- New Social Security statements are coming
- Estate Planning advisors can help:
  - Filing decisions
  - Coordination with other advisors
  - Avoiding fraud

Forbes

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Coming Soon: Two New Tools For Calculating Your Retirement Income

Steve Parrish Contributor

Retirement

I write about retirement income planning – and risk.

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The Value of Delayed Social Security Claiming for Higher-Earning Women

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