Social Security: What You Don't Know About Your Biggest Retirement Benefit

Nearly half of Americans age 50 and over failed a 5-question true/false quiz on Social Security. Here's what you need to know to get an "A".

By Robert Powell
Updated May 15, 2018 9:00 PM EDT

TheStreet Video

You would not be alone if you didn't know how Social Security works. Nearly half (47%) of Americans age 50 and over failed a basic true/false 5-question quiz on Social Security retirement benefits, according to the MassMutual Social Security retirement benefits survey.

To be fair, that's an improvement over a survey MassMutual conducted in 2015. Back then, six in 10 Americans age 50-plus failed a broader 10-question true/false quiz.

So, it's encouraging. But it's still a bit alarming. "The good news is that we've made a little bit of progress, but effectively about half of the people have not done well on five basic questions," David Freitag, a Social Security expert with MassMutual, said in an interview.

The reason that these findings are so alarming, according to Freitag, is that Social Security represents such a large part of a household's retirement income plan. In fact, if you calculate the present value of a household's monthly Social Security benefits, it could total more than $1 million. "They really need to know how it works," said Freitag. "Knowledge is power when it comes to Social Security and retirement."

Others also agree knowledge is power and that misinformation is dangerous. "There is probably no greater source of misinformation, poor financial decisions and 'advice from friends' than with Social Security," says Abe Ringer, a certified financial planner with Breakwater Financial.

Among other things, the MassMutual survey found:

At What Age Is Your Social Security Benefit Reduced?

About half of Americans age 50 and older don't know that their benefit will be reduced if they claim at age 65. That's a bit shocking especially since the full retirement age, or FRA, has been moving up for the better part of 16 years now. Consider: If you born in 1937 or earlier, your FRA -- the age at which you would receive 100% of your primary insurance amount (PIA) -- was 65.

But for those born between 1938 and 1959, the FRA ranges from 65 and two months to 66 and 10 months. And for those born in 1960 or later the FRA is later; it's age 67.

In other words, unless you were born in 1937 or earlier, your Social Security benefit will be reduced from the full PIA if you claim before age 65. For those born in 1938 and later, this chart will tell you how much your benefit will be reduced if you claim before age 65 as well as before your FRA.

Unfortunately, Freitag says, there's a lot of confusion around the age at which you would get 100% of your PIA and the ages at which you would receive a reduced benefit. "Most people think 65 is full retirement age," he says. "But the reduction in benefits is based on full retirement age."

And that's not 65 anymore. "It's important for people to know their full retirement age," says Freitag.

Others agree. "Clients don't often know their full retirement age, meaning the age when they are eligible to receive unreduced Social Security benefits," said Rita Cheng, the president of Blue Ocean Global Wealth.

Spousal Benefits and Earnings History

Just 54% of those surveyed by MassMutual know their spouse would be eligible to receive Social Security retirement benefits, even if he or she had no individual earnings history. Read more about that from the Social Security Administration.

And that means some 46% of those surveyed didn't understand that this form of retirement savings can really be for two people, said Freitag. "Not only the worker, but the worker's spouse," he said.

And now that there are many two-income families, Freitag says it's especially important to coordinate the timing of benefits, given different the earnings history of spouses and age differences. "They both need to understand how these benefits work," he said.

Other share this point of view. "The biggest thing that people should know when it comes to Social Security is that your claiming decision does not just affect you; it affects your spouse as well," said Sarah Graham, a certified financial planner with VLP Financial Advisors. "Many times, it is advisable for the spouse with the higher benefit to delay claiming until age 70 to maximize the benefit. When one spouse passes away later on, the surviving spouse will keep the higher benefit and give up the lower benefit."

Financial planners also say their clients are not much different from those surveyed by MassMutual. "Many of my clients came to me with very little knowledge about Social Security and lots of misinformation," said Francine Duke, a certified financial planner with Aqua Financial Planning. "They are often unaware as to how their benefit is calculated."

What's more, she said, many boomers are unclear about how to optimize their benefits, especially in the case of married couples.

Others concur. "(Individuals) should know that Social Security-related decisions cannot be made in a vacuum," said Ringer. "They need to be considered in conjunction with all of the material elements of their financial plan. For example, if the higher-earning spouse starts taking benefits early, did they consider how that decision will impact their spouse if the higher earning spouse passes away?"

Duke also said there is a great deal of confusion about benefits for divorcees and widows as well as divorcees whose ex-spouse has since passed away. In his practice, Mark Beaver, certified financial planner with Keeler & Nadler, said ex-spouses often forget that they could be entitled to a spousal benefit based on a former spouse.

What Else Don't We Know?

For his part, Byrke Sestok, president of Rightirement Wealth Partners, says most people have no idea what they are doing when deciding when to begin Social Security. "This is a major decision; as large as buying a home," he says.

He recommends talking with a certified financial planner about when to take Social Security. Visit PlannerSearch.org or LetsMakeAPlan.org to help find a financial professional.

"Most CFPs will develop a financial plan for you on a flat fee basis and show you exactly how your net worth and cash flow will change based upon when you start Social Security," says Sestok. "Making this decision correctly is an investment in your retirement, not an expense."

Beaver also said workers often don't know that their government pension could reduce or eliminate their Social Security benefit. Read about the Government Pension Offset and the Windfall Elimination Provision from Social Security.

In his practice, Kevin Reardon, the president of Shakespeare Wealth Management, says clients often don't know how delayed retirement credits work. Social Security retirement benefits are increased by a certain percentage (depending on date of birth) if you delay your retirement beyond FRA.

Clients also don't know that Social Security is taxable.

According to the Social Security Administration:

- Some people who get Social Security must pay federal income taxes on their benefits. But, no one pays taxes on more than 85% of their Social Security benefits.
- You must pay taxes on your benefits if you file a federal tax return as an "individual" and your "combined income" exceeds $25,000. If you file a joint return, you must pay taxes if you and your spouse have "combined income" of more than $32,000. If you are married and file a separate return, you probably will have to pay taxes on your benefits.

See Benefits Planner: Income Taxes and Your Social Security Benefits for more information.

And, some individuals don't know that the option of filing a restricted application still exist for some married couples looking to optimize their Social Security benefits," says Michael Smith, a certified financial planner with D3 Financial Counselors. "Although limited, spouses born in 1953 or earlier, or on Jan. 1, 1954, remain eligible to file for the 'old' restricted application upon reaching full retirement age," he said. "This is one Social Security optimization strategy that still exist that is most often overlooked."

Some Encouraging Signs

The quiz results, meanwhile, were more encouraging with respect to survivor benefits and how working affects Social Security benefits before FRA.

Just 20% of those incorrectly believe if their spouse dies, they will continue to receive both their own benefit and their deceased spouse's benefit -- that their total Social Security benefits received would not change.

"You still have 20% that don't understand that Social Security represents a form of life insurance that can, in fact, be very important," said Freitag. "It's not just a retirement benefit."

Only 17% believe they will receive the same Social Security monthly benefit amount whether they start collecting before or after their FRA.

And only 15% didn't know that their benefit might be reduced, depending on their earnings and their age if they are still working when they claim Social Security. For instance, if you are under FRA for the entire year, Social Security deducts $1 from your benefit payments for every $2 you earn above the annual limit. For 2018, that limit is $17,040.

According to Freitag, people need to know about these obstacles, the earnings test and the reduction in benefit for early filing, so that they can make better decisions. "If you don't know what the hurdles are, you can't plan for them," he said.

Do You Have a My Social Security Account?

From his vantage point, the most shocking result of the survey was this:

A whopping 86% of those ages 50-59 have not yet created a "My Social Security" account where they can view their earnings history and benefit projections. As some might recall, the SSA no longer mails earning history and benefit projection statements to workers. That means workers may be foregoing the chance to correct their earnings history if there's a mistake. According to Freitag, corrections are generally limited to a short period of time.

"The folks who are most affected by this are folks who have changed jobs during the course of a year, or have had multiple income streams that come in from different employers," Freitag said. "Those are the kinds of people most susceptible to having an error on their Social Security statement... And usually if an error has been made, it's not in favor of the worker."

Ordinarily, you cannot correct your earnings after three years, three months and 15 days from the end of the taxable year in which your wages were paid, according to Freitag. He also estimated that about 10% of workers might have errors on their Social Security earnings history statements.

Advisers also say checking your statements is vital. "It's a good idea for everyone to review their statements, especially if they are self-employed, so that they are sure that their income is being correctly tracked," says Liz Revenko, a certified financial planner with Mosaic Financial Partners. "Best to check annually, as there is a time limit to make corrections. Social Security is a highly valuable benefit in retirement; a little due diligence is worth the effort."

Having a My Social Security account can also help with identity theft protection because only one account per Social Security number is allowed, according to MassMutual.

Of note, the SSA currently mails Social Security statements to workers age 60 and over who aren't receiving Social Security benefits and do not yet have a My Social Security account. The SSA mails the statements three months prior to your birthday.

Consider Your 401(k) and Social Security

Freitag also considers it critical that households consider both the value of their

401(k), which isn't always translated into a monthly benefit, and the monthly benefit of their Social Security, which isn't translated into a present value. "These are both important assets, both of them require some concentration," he said. "And we don't want to do 100% of just one. We really want a nice balance across these income streams in retirement."

Freitag also noted that the present value of Social Security benefits translates into what could be the largest asset a household has, larger than the value of a household's 401(k)s and IRAs.

Recommended for you:

GM's New Chevy Blazer Looks as Lame as the Stock Market Right Now

Dow Rises for First Time in 9 Days, Oil Jumps as OPEC Agrees to Boost Output

Howard Schultz to Jim Cramer: Starbucks Stock Is Cheap and Undervalued

---

Personal Finance | Savings | Social Security

More from Savings

What the Fed Rate Hike Means For You

Alexander Nicoll Jun 13, 2018 6:26 PM EDT

To Easily Get Out of Credit Card Fees and Charges - Just Ask the Right Question

Brian O'Connell May 31, 2018 4:07 PM EDT

How Technology Is Disrupting Retirement Planning

Robert Powell May 31, 2018 7:26 AM EDT

How to Calculate Your Net Worth and Pin Down Your Financial Health

Brian O'Connell May 24, 2018 11:03 AM EDT