Long Island BusinessNEWS

Closing loopholes

By: Bernadette Starzee | November 16, 2015

Changes to Social Security benefits are coming and many retirees and future retirees are going to wind up with less money in their pockets.

"It's a sad day for the middle class," said Craig Ferrantino, president of Craig James Financial Services in Melville, referring to Nov. 2, when President Barack Obama signed the Bipartisan Budget Act of 2015 into law.

The bill eliminated the so-called "file-and-suspend" and related "restricted application" techniques popular with married retirees. These had enabled couples to increase their Social Security award by as much as hundreds of thousands of dollars over their lifetime, said Christopher Wills, director of wealth management for R.W. Roge & Co. in Bohemia.

Full retirement age is currently 66. Though individuals can begin collecting Social Security benefits as early as age 62 or as late as age 70, the longer they wait, the larger their monthly benefit will be. From age 66 to 70, monthly benefits increase by a sizable 8 percent per year.

"You can't get that rate of return on many investments these days," Wills said.

Married individuals have the option of collecting either their own full benefit or a spousal benefit, which equates to half their spouse's benefit. They can only file for a spousal benefit once their spouse has filed for benefits.

While it's difficult for many Long Islanders to wait until age 70 to start taking benefits, married people of full retirement age had a card up their sleeves to play in order to delay benefits – until now.

"Under the old rule, when I turned 66, I could file for benefits and then immediately suspend them without getting a single check," Ferrantino said. "By suspending the benefits for four years, I could earn 8 percent more per year and get a higher benefit at age 70. But the initial filing would have enabled my spouse to collect on my benefits and get half of my benefits while delaying her own benefits till age 70, so hers would have also increased by 8 percent per year."

For example, “say the higher-wage earner gets an annual benefit of $30,000 and the lower-wage earner’s benefit is $25,000,” Wills said. “The higher-wage earner files and suspends, and his or her annual benefit will grow to $39,600 by age 70. The lower-wage earner files a restricted application to collect spousal benefits while letting his or her own benefits grow. The lower-wage earner collects half of the higher-wage earner’s benefit – $15,000 per year (plus cost of living adjustments) – for four years, or more than $60,000 total.”

In the meantime, the lower-wage earner’s own benefit would have grown to $33,000 by age 70, at which point he or she could switch benefits.

“This is a strategy we have been recommending to clients for quite some time,” Wills said.

The file-and-suspend and restricted application provisions were signed into law in 2000.

“It’s been around for a while, but not a lot of people knew about it until about five years ago, when it started to become very popular,” said Evan Branfman, a financial advisor with Kuttin Wealth Management in Melville. “More people are going to financial advisors to help them navigate the Social Security system, because it’s confusing, and advisors have been recommending this strategy to those clients for whom it makes sense.”

“As baby boomers continued to move into retirement and more people were using this, the government was looking to close loopholes to tighten up payouts,” said Lawrence Sprung, president of Mitlin Financial in Hauppauge, noting uncertainty about the future of Social Security puts greater emphasis on the need to sit down with a professional and plan for retirement. “Some of the bad news can be mitigated with proper planning. People who are well-prepared for retirement will be more nimble and able to work with the hand they’re dealt.”

Individuals who file for benefits and then decide to suspend them – if, for instance, they go back to work or inherit money – will still be able to do so (this was the original intention of the file-and-suspend mechanism). However, their spouses will not be able to file for spousal benefits.

The new law will not go into effect until 180 days from its enactment.

“So if you’re 66 or are turning 66 in the next six months and want to do this, you should do it soon,” Wills said. Those who have already employed the strategy will be grandfathered in.

The bill not only impacted married filers, but divorcees as well.

“Until now, a divorced individual 66 or older who was married at least 10 years, but is currently unmarried, could claim benefits based on his or her ex-spouse’s earning record – the ex didn’t even have to know about it – while waiting for his or her own benefits to grow,” Branfman said. “But this loophole is going away for younger divorced people – if you turn 62 in 2015, you can still do this when you turn 66, but younger people will not be able to.”

The budget bill came on the heels of an announcement that there will be no cost of living adjustment for Social Security benefits in 2016 – for only the third time in 40 years. COLA is based on the Consumer Price Index, and lower energy costs were a major determinant in keeping benefits flat. For 2015, COLA was 1.7 percent.

“People have come to expect the cost of living adjustment, which means more to Long Islanders because the cost of living is so high here,” Sprung said.

Further, Medicare Part B premiums will rise by an average of 14 percent for seniors next year, Ferrantino said.

“All things being equal, retirees are going to have less money in their pocket at the end of January than they did at the end of December,” he said.