www.guidewayfinancial.com

Guideway Financial, LLC
Sharon and Jim Lear
512-487-7762
info@guidewayfinancial.com

AUGUST 2016

Proposed Cuts in Social Security Benefits

Background

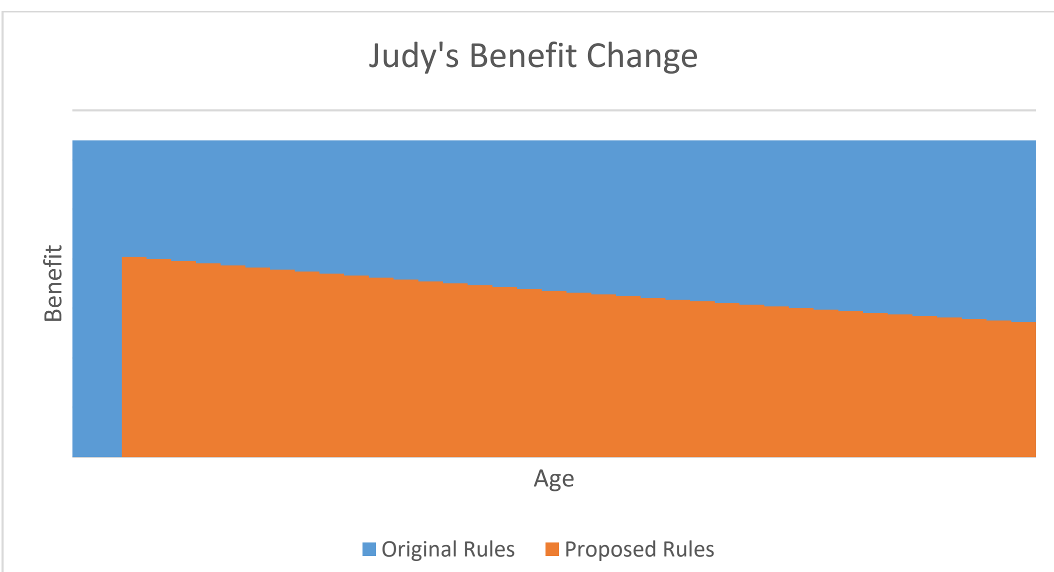
For many people, their Social Security retirement income benefit (Old Age and Survivor Insurance, or OASI) is the most valuable asset they own. The overall value is often well over $1 million per worker. It provides a very reliable supplemental retirement income for life that protects the recipient from the potential ravages of increasing prices. With pensions going the way of buggy whips, Social Security is one of the few remaining sources of steady, inflation-protected, guaranteed retirement income. Because of its importance, changes to this program can have significant effects on a retiree's quality of life, the age of retirement, and on the investments that the retiree will need.

No one knows how Congress will change the OASI rules, but the Bipartisan Policy Center (BPC), founded by former senators Tom Daschle and Bob Dole, has recently put forth a set of policy changes that represent a reasonable estimate as to the ultimate changes that may occur. In reality, only two major variables can be changed by Congress: raising taxes and reducing benefits. The BPC proposal is designed so tax increases and benefit cuts are roughly equal. It's a middle of the road solution.

Until now, we had advised many of our clients to expect only about 50% of the benefit shown on the Social Security statement. Our analysis of the BPC recommendations indicates that estimate isn't unreasonable. Of course, the reality is far more complicated than a single number and many people will not suffer a 50% reduction in benefits, although some may experience more. Nevertheless, no matter of age, most are likely to see some type of reduction. To understand how the benefits would change under the BPC plan, consider a hypothetical example.

Example: Judy

Judy is a stay-at-home mother. At the age of 32, she decides her children are old enough to allow her to focus upon starting a business. So, she gradually builds her business to the point where she is earning $120,000 per year. Under existing rules, her benefits at the age of 67 are $2,664 per month. If the proposed rules are completely phased in, her benefit would be $1,684 per month, starting at age 69. Also, her benefits would decline by as much as 1.1% per year compared to benefits under existing rules. The following chart shows the difference. Over the income planning period, her total benefit is reduced by 50% by the new rules, and in her last years of life her benefits will be reduced by almost 60%.



The reduction varies from person to person. The following factors would reduce benefits:

1. **Earnings vary over career**. Those who start with low earnings and grow it over time (or vice versa) can receive 20% lower benefits than those with steady income, even if the average earnings are the same.
2. **Delaying the start of earnings**. Those who delay careers to attend school or have children can have their benefits reduced up to 6%.
3. **Being young**. Full retirement age is delayed more for younger people. This is a reduction of up to 6%.
4. **Inflation adjustments**. Reductions in cost of living adjustments can reduce overall benefits by up to 15%. This hits hardest when you are older and most vulnerable. In later years, payments may be up to 32% lower than the first year of benefits.
5. **Saving for retirement**. Currently up to half of benefits can be subject to income tax. The proposal taxes all social security benefits for some, reducing after tax benefits by 8% to 20%. The more you have invested in IRAs and 401(k)s to provide retirement income, the more your benefits will be taxed.
6. **Higher income**. The redistribution aspects are increased so that benefits for individuals making less than $40,000 will increase 12% to 20%. Those making more than $60,000 will see their benefits cut by up to 20%.

There are other factors to consider as well. For example, spousal benefits are going to be significantly reduced for stay-at-home mothers. To add salt to the wound for the young, not only are their benefits reduced the most, the taxes they pay into the system will be increased the most.

What Can You Do?

Your retirement plan must be adjusted to account for these upcoming changes. While the BPC is one of many proposals, it's a reasonable starting point for planning purposes. No matter which plan is ultimately adopted by Congress, your taxes will likely go up and your benefits go down. Here are some steps you can take:

1. Reduce your planned retirement income. Plan to adopt a more modest lifestyle in retirement.
2. Retire later.
3. Save more. This might be more challenging than expected since the benefit cuts are only half of the proposed solution. Your taxes will probably be higher, so you'll have less to save.
4. Invest better. Optimize your portfolio to squeeze the most out of your money.
5. Maximize your Social Security claiming strategy. When the time comes to retire, make sure you understand all the potential ramifications of claiming earlier or later than Full Retirement Age (FRA).

In summary, the proposed cuts in Social Security are necessary to keep the system solvent. Regardless of the ultimate form they may take, the changes are anticipated to impact the benefits of most Americans. The current proposal can help individuals plan for the future, and we will stay abreast of future details. Planning now can indeed help most individuals weather any reductions. Some of these calculations can be complicated, so if you need help, please contact us at (512) 467-7762, or visit our website at www.GuidewayFinancial.com, or email us.

Guideway Financial, LLC
(512) 467-7762

Sharon.Lear@GuidewayFinancial.com

Jim.Lear@GuidewayFinanical.com