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Social Security Strategies To Provide Flexibility In Retirement

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When to collect Social Security and which strategy to use has become a popular topic over the last few years, and a lot of ink has been spilled on the subject. Usually it focuses on how much you might be able to collect through retirement by waiting, or perhaps how much you would give up by collecting early if you were to live a long time. One item that is not often mentioned is that by possibly waiting to collect, or at least planning ahead, can give you a lot of flexibility in retirement; especially if you have other retirement accounts such as IRAs or 401(k)s.

Often times people retire at 62 or so and say that they will start drawing their Social Security and perhaps not touch their retirement assets. While this can work for some people, it can potentially lock you into an inflexible spending plan in retirement. What that means is that once you turn your Social Security on, you only have a year to decide if you want to turn it off for some reason. After that, you are now stuck with your payments for the rest of your lifetime. Meanwhile, you have decided to not touch your retirement accounts, and they continue to grow. This is not necessarily a bad thing, but here's the catch, at 72 the IRS will require that you start taking your Required Minimum Distributions whether you want the money or not. The amount starts at 3.65% of the balance the first year and goes up from there. Remember, this is all income that you will be taxed on. A lot of times people find that they do not need the money, but are now paying taxes on it and need to either reinvest or save it.

Another option can be deciding to wait on Social Security and instead drawing on the investment accounts to fund your retirement. For a lot of people, this can be a scary thought to draw on your retirement accounts and savings, and perhaps watch them drop a bit, but remember you are now waiting to eventually start collecting your Social Security. In the meantime, you can fill up your tax bracket and help manage your tax situation in retirement.

And because you still have control over how much you may want to take out of your retirement accounts, you can either use the money to enjoy retirement, or perhaps conduct a Roth conversion where you move some money from your pre-tax retirement accounts to Roth IRA accounts. If you haven't reached the upper limit of your current bracket, you may be able to move money to a Roth IRA at a fairly low rate now, and it would not be subject to Required Minimum Distributions down the road. A married couple can make approximately $104,000 in a year and after taking the standard deduction still be in the 12% bracket. So let's say $70,000 covers living expenses, which leaves potentially $30,000 or so that could be converted to a Roth IRA, now grow tax free, and no longer be subject to RMDs down the road. On the other hand, if someone had started collecting their Social Security at 62 and it was a $2,300 dollar a month benefit then that would be about $28,000 a year in added income and would now be eating up most of that 12% bracket, which would not leave much room to do a Roth Conversion at the lower rate.

By potentially converting $30,000 a year to a Roth for 10 years, that is $300,000 plus growth that will not be subject to RMDs in the future and is now in a tax free account. Another advantage is that if you would like to leave a legacy for future generations, they can now inherit this money tax free. With the new rules that they have to take the money out within 10 years, converting the 401(k) to a Roth provide a huge advantage.

There are many more options when deciding how to spend your money in retirement, which is why working with a fee only wealth manager cannot only help keep your investments on track, but also help with your legacy and tax planning as well. These overlooked details can add as much to your overall wealth as having the right investment allocation. As always, please remember to consult with a financial advisor when making these important decisions.