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About-Face on Benefits Could Turn into Boon

by

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Apr. 27, 2008 (McClatchy-Tribune Regional News delivered by Newstex) -- A couple of months ago, this column discussed a do-over option for retirees who regretted taking Social Security early and locking themselves into smaller benefit checks for life.

This option requires that you withdraw your original application for benefits and repay all the money you have received. You can then reapply to get a bigger monthly check based on your current age. But some of you interested in this were told by local Social Security representatives that such an option doesn't exist.

Well, it does.

Granted, it's a strategy rarely used, and it's not for everyone. Yet, as word spreads, Social Security needs to make sure its staff is aware of this, because more and more retirees are going to ask for it. Many healthy retirees who are now, say, 70 can easily see themselves living another 20 or 25 years, and they might view their decision years ago to take early benefits as a financial mistake.

On paper, it's not supposed to make any difference if you take benefits at the earliest possible age, 62, or at your full retirement age or as late as age 70.

You get smaller benefits if you take them early, but you have more years to collect checks. Wait, and your checks are bigger but you get fewer of them.

In reality, if you live long enough, generally past 80, you will end up with less in

lifetime benefits by taking Social Security early. Almost half of retired beneficiaries have taken Social Security at 62.

If you think a do-over is for you, contact Social Security. The Social Security representative might not be familiar with this option or give you wrong information. Social Security spokesman John Johnston explains that this is such an unusual request that even staffers with decades of experience have never come across it.

So be persistent and ask to speak to a supervisor. Basically, you must fill out Form 521 to request that your original application for Social Security benefits be withdrawn. If your request is approved, you will then be required to repay all the Social Security benefits you've received to date without interest. If your husband or wife gets spousal benefits based on your work record, those benefits must be repaid, too.

You may be able to deduct a portion of your repaid benefits as a miscellaneous deduction on your tax return, according to the Internal Revenue Service. Check IRS Publication 915 for details.

Still, repaying years of benefits can add up to quite a sum, more than many retirees might have. And it's a gamble.

"If you pay back \$50,000 and you die three months later, that \$50,000 is lost forever," says Social Security's Johnston.

John Rothenhoefer figures it's a risk worth taking. The 70-year-old recently went to a Social Security office in Baltimore to withdraw his original benefit application from eight years ago. Nobody there knew what he was talking about, he says. "It was just like talking Greek," he says. He handed them a Form 521 downloaded from the agency's Web site.

A few weeks later, he got a letter telling him the amount he needed to repay. After sending in his check, he went back to Social Security to reapply for benefits. He says the representative told him that only one person in the office had bet that he would go through with it.

"I really did this for my wife," he says. Rothenhoefer's benefits haven't been restarted, but he figures the new amount will be about 76 percent higher than the

previous one. He says his wife, Charlotte, who has a modest Social Security benefit, could live well into her 90s given her family history. In the likely event that she outlives him, he says, his larger benefit will replace her smaller one.

Rothenhoefer has one warning for those who try this. Almost as soon as he withdrew his original application, his benefits stopped. Medicare and prescription drug premiums that had usually been taken out of his check couldn't be paid, and he got notices demanding payment.

To maximize your benefits using this strategy, you should reapply for benefits at age 70, says Mary Jane Yarrington, who writes a column on Social Security for the National Committee to Preserve Social Security and Medicare.

One reason is that for every year you wait beyond your full retirement age to take benefits, you get a 7.5 percent or 8 percent increase in annual benefits up to age 70. Once you're no longer building up this credit for waiting, there's no financial incentive not to take benefits, she says.

Laurence Kotlikoff, a finance professor at Boston University, advocates that retirees use this strategy. He says 70 is the optimal age but that even those a few years older might benefit. He crunches some numbers in "Double Dip on Social Security," a case study on his Web site, www.esplanner.com.

The title is telling, implying that retirees can game the system. And that doesn't sit well with those who see this strategy as benefiting only those who can afford to repay benefits. Basically, a wealthy person can take early benefits, invest the money, repay it without interest and then reapply for a higher benefit.

"It's really a distressing development," says Alicia Munnell, director of the Center for Retirement Research at Boston College. "The problem is that it will seem to be a two-tiered system. Poor people who make a mistake are not going to be able to rectify it, and higher income people will. ... That's not a system that everyone will have confidence in."

For now, retirees don't seem to be lining up to repay benefits. But if the wealthy end up abusing this option, Congress and a new administration can always restrict the practice when they get around to shoring up Social Security.