

Social Security and City of Chicago Pensions

**Chicago FABF
Retirement Seminar
September - 2023**



Introduction: the Three-legged Stool

Social Security is one “leg” of a three-legged stool of retirement income:

Pension

Social Security

Personal Savings

Social Security is a complex program that is not “sponsored” by a local government. But uniformed and civilian **employees** can master simple information on specific provisions that affect them

Social Security and Illinois Governments

Nationwide, many State and Local employees do not participate in Social Security (SSA). In Illinois, it is governed by agreements from the 1950's setting forth who is in or out of SSA.

Out: teachers, university employees, Cook County, ***City of Chicago***, most downstate/suburban fire and police.

In: most state employees, non-Chicago municipal and county (IMRF). Also, *some fire and police* in small towns or towns that were small in the 1950's.

What Social Security Benefits are Paid to Illinois Public Employees?

| | |
|-----|---|
| IN | Those “in” Social Security earn the same benefits as private-sector civilian employees. <i>The same!</i> |
| OUT | Those “out” still earn a benefit from qualifying civilian work. Their benefits are lower than most workers because of their long absence from Social Security. Also, benefits are calculated using modified formulas, but this does NOT result in a reduction compared to the civilian workforce, based on the % of earnings replaced. |

Social Security Basics

Established in 1935. Provides retirement, disability and survivor benefits.

Funded by contributions from employee wages, an employer match and a small amount of taxes on Social Security benefits. Current employee rate is 6.2% of wages. Wages over \$160,200 are not taxed (2023).

All public employees are in Medicare if hired after March 1986.

Long-term projections for funding show a need for improvement either in revenue (higher taxes), benefit reduction, or a combination. But the program will be there in the future.

Earning Social Security Benefits

- Attained by earning 40 “credits” in Social Security covered employment.
- A credit is earned in 2023 by making \$1,640. Up to four credits may be earned each year.
- Generally, a benefit is earned if you work for 40 calendar quarters, or 10 years total.
 - Most Illinois sworn personnel will qualify for some Social Security benefit.
 - You will know if you qualify when you obtain a *Personal Earnings and Benefit Statement* or inquire to ssa.gov.

What Benefits are Earned?

Replacement Rates for age 65 - 2021

| Category | Wages | Benefit | Rate |
|----------|-----------|----------|------|
| Low | \$25,010 | \$12,835 | 51% |
| Medium | \$55,758 | \$21,162 | 38% |
| High | \$88,924 | \$28,009 | 31% |
| Maximum | \$136,710 | \$34,180 | 25% |

Source: National Academy of Social Insurance

Social Security Benefits

Provisions that May Affect Public Employees

The “*Government Pension Offset*”
(Publication 05-10007)

The “*Windfall Elimination Provision*”
(Publication 05-10045)

Use: www.ssa.gov

Government Pension Offset

(affecting benefits earned from a spouse's record)

Spouse Benefits Explained:

A retiree receives Social Security benefits either from his or her own work record or he receives **one-half of his spouse's benefit** if that will result in a higher payment.

Spouse Benefits – Example # 1

| | |
|--|-----------------|
| Al's Social Security Benefit: | \$ 2,000 |
| Peggy's Benefit from her work record: | \$ 800 |
| Peggy will receive a monthly check of: | <u>\$ 1,000</u> |
| The couple will receive in total: | \$ 3,000 |



Spouse Benefits – Example # 2

| | |
|---------------------------------|---------------|
| Ward's Social Security Benefit: | \$ 1,500 |
| June's work record benefit: | \$ 0 |
| June will receive: | <u>\$ 750</u> |



**The couple will
receive in total: \$2,250**

But, the Government Pension Offset changes this for many public employees:

The GOVERNMENT PENSION OFFSET provides for a reduction in Social Security Benefits *from a spouse's record* of 66.6 cents for every dollar received in government pension from work *outside* the Social Security System.

Government Pension Offset (when applicable)

The sole example:

| | |
|--|-------------|
| Molly's Social Security Benefit: | \$ 3,600 |
| Lt. Tom's Spouse Benefit?: | \$ 1,800 |
| Tom's Actual <i>Spouse</i> Benefit: | \$ 0 |

Why?

A 66¢ reduction in Tom's \$ 1,600 Spouse Social Security benefit for every \$1 of a \$ 2,700 or higher public pension (from outside Social Security) will **eliminate all of Tom's Social Security benefit *from Molly's earnings record.***

Spouse Benefits and City of Chicago Employees

Simple Rule #1:

You will *not* receive a Social Security benefit off of your spouse's work record.

In fact, few Americans receive a spouse benefit now that most homes are two-income families.

A Social Security Benefit from *YOUR* Work Record

An understanding of how Social Security benefits are calculated is helpful.

For comparison, consider your government pension; calculated using your final salary and percentage based on your years of service.

Example: 75% of salary after 30 years
The “replacement rate” is 75 %

Social Security Benefits

Calculated by averaging a retiree's salary over his/her working life (with indexing of that average for inflation).

The average wages are then “replaced” using a formula with varying replacement rates.

The 2023 formula is:

First \$ 1,115 in monthly Wages 90%

Next \$ 5,606 in monthly Wages 32%

Over \$ 6,721 of Taxable Wages 15%

Examples of Civilian and Some Police/Fire Retirees' SSA Benefits

| Monthly Wage | Calculation | Benefit | Percent |
|--------------|---|---------|---------|
| \$800 | \$800 @ 90% | \$720 | 90% |
| \$1,300 | \$1115 @ 90% \$185 @ 32% | \$1,063 | 82% |
| \$7,500 | \$1115 @ 90% \$5,606 @ 32% \$ 779 @ 15% | \$2,914 | 39% |

Windfall Elimination Provision

- ✓ Under the so-called “**Windfall Elimination Provision (WEP)**,” workers who receive a pension *from work outside of Social Security* have a different benefit formula.
- ✓ **Under this modified formula**, the first increment (called a “*bend point*”) of wages is replaced at a lower percentage than in the standard formula. All other factors stay the same.

Modified Formula for Public Employees not in Social Security

| | |
|---------------------------------|-------------|
| First \$ 1,115 in monthly Wages | 40%* |
| Next \$ 5,606 in monthly Wages | 32% |
| Remainder of Taxable Wages | 15% |

As opposed to **90% - all other factors are unchanged*

Examples of Police Retirees' SSA Benefits

| Monthly Wage | Calculation | Benefit | Percent |
|--------------|-----------------------------|---------|---------|
| \$800 | \$800 @ 40% | \$320 | 40% |
| \$1,300 | \$1115 @ 40% \$185 @ 32% | \$505 | 39% |

Workers' Benefits and the Illinois Public Pension

Moderately Simple Rule: If attaining age 62 in 2022, WEP affected Public retirees (those not in SSA) would receive a Social Security Benefit from their work records that is **44% to 55% lower but not more than \$558 lower** than the benefit that would be calculated using the standard formula.

Not So Simple (*but a good idea*): Go to ssa.gov and register an account in your name. Download your earnings history and plug it into the “Online Calculator (WEP Version)”.

Tales of Three Retirees

- 1) Ted
 - A retiring private-sector accountant
 - Has average monthly earnings of \$7,500.
- 2) Bob
 - A police officer in Bartlett, covered under both Article 3 pension and SSA.
 - He also has average monthly earnings of \$7,500
- 3) Julie
 - A firefighter in Chicago (a city that is *not* in SSA for public employees).
 - Has average monthly Social Security earnings of \$1,300 from various civilian jobs.

Tales of Three Retirees (cont.)

Ted
(CPA)

- \$7,500 in Social Security covered wages.
- \$2,914 Social Security benefit.
- **39% of wages replaced.**

Bob
(BPD)

- \$7,500 in Social Security covered wages.
- \$2,914 Social Security benefit.
- **39% of wages replaced.**

Julie
(CFD)

- \$1,300 in Social Security wages.
- \$6,000 in police wages (outside of SSA)
- \$505 Social Security benefit.
- **39% of Social Security wages replaced.**

It's the same!

Lessening the Impact of the Windfall Elimination Provision

- 30 or more Years of “Substantial Earnings” under Social Security negates impact.
- 21 to 29 years of Substantial Earnings lessens the impact.
- A year of Substantial Earnings in 2022 was \$27,300. It was lower in the past; will be higher in the future.

Lessening the Impact: the WEP formula does not apply to survivor benefits

- Widow(er)s of Chicago employees are **not** impacted by the WEP. *Beware of rumors to the contrary. Continuing.....*
- Widow(er)s are entitled to SSA benefits from their own records without modification, even if they receive a police/fire survivor pension benefit.
- Also, they may receive SSA survivor benefits from the fire/police employee record using the standard (non-WEP) formula.

Why a Modified Formula?

- Social Security uses a **progressive formula**; lower income workers receive more.
- A police officer, firefighter or teacher or similar employee is not a low-income worker.
- *Use of the standard formula for people who are not in Social Security for their career work would result in a “**windfall**” benefit reserved for poorer citizens.*
- The “**Windfall Elimination Provision**” corrects this.

What does this all mean to typical Chicago public employees?

Hard to say, everyone's situation will be different.

- Example of One Chicago FD Employee who is “out” of SSA:
 - Has annual civilian earnings of \$5,000 from age 19 to 21, \$35,000 until age 25, nothing until age 55, then \$50,000 to age 65 receives a Social Security benefit of **\$527 per month**.
 - Earn more and the amount will be higher, earn less and the amount will be lower.
- All earnings estimates in **2023** dollars.

Social Security Rumors

“A lie gets halfway around the world
before the truth gets its pants on.”

- *Winston Churchill*

Some rumors are right, but most not...

| | |
|-----------------|--|
| Good | Chicago and Evanston Police/Fire feedback on benefits. |
| Real Bad | Illinois teachers get no Social Security, even from non-school work. |
| Bad | Suburban school aide (IMRF member) subject to WEP. |
| Real Bad | When I die, my fire survivor pension will reduce my wife's Social Security she earned on her own record. |

... MOST are WRONG!

How to Deal with Bad Information

- You are now an expert.
- **Always go back to the SSA Publications.**
Police/Fire/Teacher benefits may be impacted by the Windfall Elimination Provision (WEP) and the Government Pension Offset (GPO).

If it's not in the publication, it's not true.

- Check the information, request the source of the other data. If the source is “*some guy*,” forget it !

Help Social Security Get it Right!

Question 14(a) of the Social Security Retirement Application:

*“are you entitled to, or do you expect to be entitled to, a pension... based on **your** work **not** covered by Social Security?”*

- ✓ IMRF members, police/fire who do participate in Social Security *and surviving Chicago police spouses* will answer: **NO**.
- ✓ City of Chicago retirees will answer: **YES**.

Legislative Initiatives

There are two types of legislative initiatives being considered to “deal” with the impact of the WEP and GPO on public employees:

- (a) complete repeal and;
- (b) modification of the WEP.

Legislative Proposals H.R. 82

H.R. 82, *many* sponsors.

Would repeal both the WEP and the GPO. Has passed the House Committee.

But not likely to pass (Dan's opinion).

- Same old proposal that always fails.
- Attempts to address inequities that are not there.

Legislative Proposal HR 5834: Equal Treatment of Public Servants Act

Bipartisan Proposal. Other similar legislation.
Leaves Government Pension Offset intact.

Modifies Windfall Elimination Provision.

Calculates Social Security benefits using each worker's total lifetime earnings, and then adjusts for the proportion of earnings that came from a job covered by Social Security.

Estimates show this would increase most recipient's benefits modestly.

Questions ?

Questions so far on the impact on
Social Security benefits by an Illinois
public pension?

Social Security Claiming Strategy: An Overview

- **Social Security can be claimed at different ages**, from 62 to 70. The later the age, the higher the benefit.
- **For married couples**, benefits can be claimed at different times. A wife could start her benefit (on her record) at age 66 but the husband might delay until age 70.
- It is also possible for the lower-earning spouse to begin receiving payments on her or his own record and then switch to a spousal benefit when the higher wage earner applies for benefits.

Social Security Claiming Strategy (cont)

- For married couples, certain sophisticated/complicated *Claiming Strategies* were terminated effective April 1, 2016. These involved allowing a person to file for benefits then “suspend” receipt in order to qualify a spouse for a spousal benefit. Persons who were age 62 by 4/1/16 may have some eligibility for these prior strategies.
- *This, and all Claiming Strategy issues, may need research or professional consultation. **Dan is not an expert in Claiming!***
- **Selecting the proper strategy is always important**, but often less impacting for retirees who have very small SSA benefits.

SSA Full Retirement Ages

The SSA formulas estimate or determine benefits at the so-called Full Retirement Age (FRA). **Your FRA is:**

| Year Born | Full Retirement Age |
|----------------|-------------------------|
| Thru 1954 | 66 years old, 0 months |
| 1955 | 66 years old, 2 months |
| 1956 | 66 years old, 4 months |
| 1957 | 66 years old, 6 months |
| 1958 | 66 years old, 8 months |
| 1959 | 66 years old, 10 months |
| 1960 and later | 67 years old |

Social Security Benefits: Claiming Early

- If you claim your benefit before your Full Retirement Age, the benefit is reduced for each month before the FRA and your benefits will be subject to annual wage limitations. **The annual limitation in 2022 is \$21,240.**
- If you earn above that amount in a year, your next year's SSA is reduced by 50-cents per \$1 you were over the limit.

If your FRA is 66 and you claim your benefits before that age, the reductions are as follows:

| Claiming Age | Reduction |
|--------------|----------------------------|
| 62 | 25% |
| 63 | 20% |
| 64 | 13% |
| 65 | 7% |
| 66 | No reduction, full benefit |

Social Security Benefits: Delaying to a Later Age

If you claim your retirement benefits *after* your Full Retirement Age, the amount paid increases each month on a uniform increase of 8% per year.

Examples at an FRA of 66 years old:

| Claiming Age | Increase |
|--------------|----------------------|
| 67 | 8% higher |
| 68 | 16% higher |
| 69 | 24% higher |
| 70 | 32% higher |
| Above 70 | No further increases |

Examples: Social Security Benefits of \$1,000 at FRA of Age 66

| Claiming Age | Benefit |
|--------------|----------------|
| 62 | \$750 |
| 63 | \$800 |
| 64 | \$870 |
| 65 | \$930 |
| 66 | \$1,000 |
| 67 | \$1,080 |
| 68 | \$1,160 |
| 69 | \$1,240 |
| 70 | \$1,320 |

Social Security Claiming: What's the Best Age?

- There is no best age. The formulas are neutral, based on system-wide life expectancy. Joe draws at 62, Dan at 66, and Mary at 70. They all made a good decision if it fit their needs.
- Considerations for Delaying. Formulas are based on system-wide life expectancies. People with educations at high-school and above, middle class incomes and health insurance will usually live longer. Delaying makes sense if you are going to live longer than the average American.
- The formulas don't take gender into account, but since women live longer, women should consider delaying Social Security.
- Considerations for Not Delaying. I'm single and want to build up savings for an estate or charity.

Social Security Claiming: What's the Best Age ? – continued...

- One Approach: if you need it, take it. If you don't need it, delay claiming Social Security in order to increase your benefit and/or a spouse's benefit later in life.
- Bad Approaches:
 - (a) calculating a breakeven age, and
 - (b) being afraid that Social Security is going to run out of money.

Wrap Up – Summary

- ✓ Remember the “three-legged stool” of retirement income:
 - 1) Pension
 - 2) Social security
 - 3) Personal savings
- ✓ **For some in Illinois**, Social Security is a full, strong leg.
- ✓ **For City of Chicago retirees**: the Social Security leg will be lessened by their careers outside of SSA but they will still receive an equitable benefit. Perhaps more equitable if newly introduced legislation passes.
- ✓ “Claiming Strategies” take some thought and research.
- ✓ **There is always a benefit to earning Social Security credit.**

Questions and Resources

- Questions?

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GovernmentPensionOffset.com

- Resources:

- *Social Security for State and Local Government Employees*, Daniel W. Ryan, Amazon.com. \$8.39.

- Coming in 2024: *IPPFA Retirement Guide for Chicago Fire and Police: Pensions, Social Security and Deferred Compensation.*

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