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The News You Need to Know

Left to right: Andrew Woolley, Andrew Barninger, Christopher Miller, Steven Bell and Alan Loss.

How to Make a Lifetime Impact
For Your Grandkids

Personal Wealth Advisory, LLC

Please join us for our next webinar:

How to Make a Lifetime Impact For Your Grandkids:
5 great ways you can improve the lives of your grandchildren other than leaving them money.

September 29, 2020
1:00 PM

Please register here:
https://us02web.zoom.us/j/88287031556

Is Social Security Really Going Bankrupt?

Recently, there has been much talk about Social Security going "bankrupt." Many people have heard about a year in the future (2033, 2035, etc.) when there might no longer be money in the fund to pay monthly benefits. This concern often causes people to consider taking their benefits earlier than normal just so they can "lock them in" or get as much as they can before the system runs dry. Social Security going broke is a scary thought. Let's explore what this means and if it is worth being stressed about it. First, we have to understand how Social Security is funded. Most of the money that is used to pay monthly benefits comes from payroll taxes. In 2020, 12.4% of the first $137,700 that a worker earns is paid to Social Security. Usually, employers pay half of this and the employee pays the other half. Self-employed people pay the full amount. Social Security also makes money by taxing the Social Security benefits paid to those with incomes over certain levels.

Every year, money that comes out of worker's paychecks goes to Social Security and then is paid out in benefits. The issue right now is that Social Security pays out more in benefits each year than it brings in from payroll tax deductions. When this happens, the Social Security Trust Fund is used to make up the difference and pay the rest of the monthly benefits. The Trust Fund is basically a bank account that is drawn from when needed. Generally, 20-25% of Social Security benefits come from the Trust Fund each year.

It is the Social Security Trust Fund that is expected to be depleted in 2035. Benefits could still be paid using payroll taxes but, without the Trust Funds to supplement, only about 75-80% of the benefits could be paid out.

So, while this is still a big potential problem, it is not Social Security that is going bankrupt. The Trust Fund will simply run dry if nothing is done.

Personal Wealth Advisory, LLC
Wise strategies for your wealth and your life

630 Delp Rd., Suite 100
Lancaster, PA 17601
p: 717.735.1170 f: 717.735.1181
www.pwallc.net
info@pwallc.net

What can be done to fix this?

Fortunately, Congress has many options for fixing this issue and 15 years to figure it out. Here are a few of the potential solutions that Congress could decide to use:

1. As mentioned, a maximum of $137,700 of wages for each worker are currently taxed at 12.4% for Social Security. This income level could be raised. There have also been proposals where the dollar limit is changed to a fixed percentage of income (90% of all income, for example.) Here is an example of how that might work:

   In 2020, someone earning $400,000 per year pays 12.4% (half by employee and half by employer) to Social Security on the first $137,700 of income. The rest is not taxed. This amounts to $17,075 of tax per year. If the rule was changed and Social Security tax was paid on 90% of income, the same worker would pay $44,640 of tax per year. Again, half is paid by the employer.

2. The Full Retirement Age for Social Security could be raised above 67.

3. Change how Cost of Living Adjustments are calculated.

4. Social Security benefits could be reduced for high-income earners.

5. A mix of one of more of these or other options.

There are a lot of people who rely on Social Security in retirement. Congress has a lot of incentives to act on this issue and prevent benefit disruptions to retirees. It is likely that steps will be taken before 2035, but it is also likely to be pushed to the last minute and become a hotly contested political issue when the time comes.

For now, you should know that, yes, there is an issue with Social Security. However, the problem is not that the whole system is on the brink of collapse but rather the supplementary funding from the Trust Fund will run dry in 2035 if nothing is done to fix it.

Student Loan Payment Suspension Extended–How to Take Advantage

The suspension of federal student loan payments has been extended to 12/31/2020. Before the extension, suspended federal loan payments were set to begin repayment in October. This means that borrowers whose federal student loan payments were suspended will continue to qualify for suspension through the end of 2020. Loans that qualify for the payment suspension are:

- Direct student loans
- Perkins loans
- Parent Plus loans
- Grad Plus loans
- Some FFEL and HEAL loans (those that are owned by the Department of Education)

During this time, there will continue to be a 0% interest rate on the loan balances. It is likely that borrowers will receive (or have already) a notification from the Department of Education about the continuation of the payment suspension.

Those who have private loans should know that this extension does not apply to those loans. Private lenders have been flexible by offering their own payment suspensions and other assistance. However, private loan borrowers should check with their lender to see what options, if any, the lender is offering. The extension of the federal loan payments does not mean that a private lender who has offered assistance will continue that assistance longer than indicated. It is best to check with the loan company to make sure that you know all your options.

How to make the best of the payment suspension

1. Borrowers working towards Public Service Loan Forgiveness should take advantage of the suspension by electing not to make payments. Those seeking the PSLF program will receive credit for the months of October, November and December of 2020 as if they have made payments. This means, there is no incentive for you to make payments during this time.

2. Those who have lost jobs or had their income reduced during the pandemic should continue to avoid making loan payments, if their loans qualify for payment suspension. If you have had a significant drop in income, it is worth exploring an Income-Driven Repayment plan.

   All borrowers can apply to switch their payment plan at any time and there is no cost. For someone who has lost a job or is earning less, switching to the IDR plan may lower their monthly payment significantly once the repayment period begins in 2021. The best way to explore this option is to log into StudentAid.gov to learn more and apply.

3. Consider using the money to pay down high-interest debt such as credit cards, private student loans or personal loans.

4. If you do not have high-interest debt and your income is stable, now is a great time to focus paying down your federal loans with the highest interest rates. This

way, once payments begin again in 2021, your high-interest balances will be lower, and you will end up paying less in interest on those loans over time.

5. Now is not a good time to refinance your student loans into private loans. Right now, banks and lenders are heavily advertising student loan debt refinancing. Normally, this is a good option to consider as the rates and payments might be lower. However, once your federal loans become refinanced into private loans, they will no longer qualify for federal payment suspensions in the future. It is best to wait until early 2021 to explore refinancing your federal loans so you can take full advantage of the current payment suspension.

References:

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