

Financial Insight

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When Should I Start Social Security?

by Deborah H. Levenson, CFP®

One of the most frequent questions we are asked by clients is when to start

Social Security. Since there is no easy, one-size-fits-all answer, our goal here is to provide some general guidance. Decision-making for couples regarding Social Security can be especially tricky, so in the interest of simplicity, this article will deal with individual decision-making. The biggest factors that go into your decision are your health, expected longevity, employment status, cash flow needs and expectations of future changes to program benefits and taxation. Clearly, these are not simple factors to evaluate.



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Where to Begin?

A good starting point is to examine your annual Social Security statement. It documents your earnings history (if it is inaccurate, get it corrected) and estimates your expected monthly payment at three different ages - your full retirement age (see table), an "early" option and a "delayed" option. The longer you wait to start your benefits (up to age 70), the higher your monthly payment will be. Historically, the increase you receive by delaying has been significantly greater than the rate of inflation, so by waiting you are rewarded with higher monthly payments in real terms.

How is Your Health?

The good news is that, once activated, Social Security payments will continue for your entire lifetime, even if you live well past 100. They will increase each year based on cost-of-living adjustments (thereby removing any inflation risk). Your

anticipated longevity is important because the primary risk in delaying Social Security is that you die before reaching the break-even point where waiting pays off. The break-even point is the age you need to reach when the extra money you

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Company News - New President to Lead BWM

We are pleased to announce that David J. D'Amico, CFA has joined us as the new President of Braver Wealth Management. Dave has more than 20 years of experience in the investment management and private client business and, most importantly, shares our core



David J. D'Amico

value that client needs come first. Most recently, he was a partner and head of Private Investment Management at Lee Munder Investments, Ltd. in Boston where he had overall responsibility for relationships totaling \$1.5 billion in assets.

In addition to business strategy and development, Dave has experience in all areas of investment management including security analysis, equity and fixed income portfolio management, relationship management, operations, sales, and marketing. Dave earned a BS in Accounting from Bentley and a Masters in Finance from Boston College. He earned his CFA designation in 1996.

With Dave as President, the current management team members will continue to serve in their present roles. Joe Ludwig, the past President, will now focus primarily on client service. Dave can be reached at 617-969-0223 or ddamico@thebravergroup.com. ■

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Window Opens to Capture Long-Term Gains with 0% Capital Gains Taxes



If you want to sell some long-term investments but have been holding back because you would face substantial capital gains taxes, you may have a window to do so with lower tax consequences. Beginning this year and extending through 2010, the long-term capital gains tax rate for individuals in the 10% and 15% income tax brackets will drop to zero.

What hasn't been widely reported in the financial press, however, is that even if your taxable income exceeds the 15% bracket, you may still be able to qualify for the 0% rate for at least a portion of any capital gains you realize in 2008 through 2010. The reason for this is the progressive structure of our tax rates, where the last dollar is typically taxed at a higher rate than the first.

Who qualifies for 0%?

Based on the 2008 tax brackets, individuals must make less than \$32,550 in taxable income while couples have to remain within the \$65,100 tax bracket to take advantage of the 0% capital gains tax break. Taxable income includes all sources of income less any allowed "above-the-line" adjustments – itemized and standardized deductions, and exemptions.

2008 Income Tax Brackets

Tax Rate	Single	Married Filing Jointly
10%	Not over \$8,025	Not over \$16,050
15%	\$8,025 - \$32,550	\$16,050 - \$65,100
25%	\$32,550 - \$78,850	\$65,100 - \$131,450
28%	\$78,850 - \$164,550	\$131,450 - \$200,300
33%	\$164,550 - \$357,700	\$200,300 - \$357,700
35%	Over \$357,700	Over \$357,700

Which investments qualify?

The favorable capital gains treatment applies to net long-term capital gains minus net short-term capital losses, but excludes sales from collectibles, qualified small business stock and sales of depreciable real property. For most taxpayers, this is simply the sum of net capital gains from the sale of stocks, bonds, or mutual funds. If you sell a stock for \$60,000 that you purchased for \$40,000, only the \$20,000 gain counts as taxable income.

Strategies to consider:

(1) If you have a choice of sources of income, such as withdrawals from a tax-deferred retirement

account or liquidating stock and bond positions with long-term capital gains, you may want to consider using the proceeds of capital gains sales before other sources of income. For example, assume you file a joint return and have taxable income from various sources of \$30,000, and capital gains of \$50,000. You would pay no capital gains tax on the first \$35,100 of capital gains; this is the difference between the \$30,000 of other income and the \$65,100 maximum for the 15% bracket. You would pay 15% capital gains tax only on the remaining \$14,900, the portion that exceeds the \$65,100 maximum.

(2) If you provide financial assistance to any individuals in the 10-15% tax brackets, consider gifting highly appreciated stock or bonds that you have held for over a year. The investments can be sold without capital gains taxes as long as the recipients' income remains under the maximum income levels for the 15% tax bracket. Individuals can give up to \$12,000 a year, per person, without having to file a gift tax return. For married couples, this can mean \$24,000 a year without having to deal with gift-tax rules. If you're considering gifting to a child, be aware that the kiddie tax rules have been extended through age 23 for children who are full-time students, if their income is less than or equal to half the amount of their support.

(3) This may be the time to take losses, start a small business or make certain expenditures that will reduce your taxable income to the 10-15% tax brackets to take advantage of the 0% capital gains taxes.

(4) Consider using the 0% capital gains tax opportunity to rebalance taxable portions of your portfolio to

reduce individual stock risk, or to refine your asset allocation.

With only a three-year window, time is limited to take advantage of this 0% capital gains tax rate. Barring action from Congress, 0% capital gains rates are scheduled to sunset in 2011, and revert to the pre-2001 rates of 15%, 28%, 31%, 36%, and 39.6%, depending upon your income bracket.

As with all strategies to reduce taxes, be mindful of unintended consequences. Be sure you will qualify for the 10-15% tax brackets before you begin selling assets. ■

Emotion and the Investor

Volatility made the past year a difficult one for investors. With every fall or upward move in the market, we were treated to a host of financial experts proclaiming either ongoing doom or the resurgence of the bull market. But if there was one prevailing emotion for investors in the past six months, it was fear. Fear of losing money, and fear of missing out on opportunities to rebuild portfolios that were still feeling the pain of the 2000-2002 market decline.

Behind that fear were a number of very reasonable concerns ranging from the housing market to the sub-prime lending debacle, energy prices, consumer indebtedness, inflation and more. The problem with fear, however, and for that matter any emotion, is that it hurts you as an investor.

One of the latest studies of the mental processes of successful investors is a field called neuroeconomics that explores the role biology plays in economic decision-making, by combining insights from cognitive neuroscience, psychology and economics. Among the neuroeconomists' work was an interesting study in 2005 that looked at the investing success of individuals who had suffered damage to the region of the brain that controls emotions, inhibiting their ability to experience basic feelings such as fear or anxiety. The researchers' conclusion: the individuals' lack of emotional responsiveness actually gave them an advantage when playing investment games.

A different side of the emotional spectrum comes into play when individuals invest for the pleasure of winning. When small wins no longer bring the same jolt of pleasure, the investor ups the ante, risking increasingly larger amounts to regain the pleasurable experience of winning.

Behavioral finance theorists are also quick to point to emotions as the reason many investors sabotage their own financial success. Among the common mental mistakes identified by behavioral finance is allowing emotional connections to override reason.

The challenge for investors is to remove emotion from the investment process as much as possible. That starts with recognizing that we are vulnerable to emotions and that those emotions can make us act counter to what is good for us. The next step is to set up rules that help remove emotion as much as possible from the decision process.

In our management of client assets, we do this through quantitative decision models that depend on mathematics and trend analysis rather than

subjective judgments. We let the market tell us what is happening rather than trying to impose an emotional decision that may not necessarily be based on facts. ■

Behavioral Finance Concepts

Behavioral finance is based on the belief that investors act irrationally and make the same mistakes over and over. These mistakes tend to be emotion based and undermine logical decisions.

- *Overconfidence.* Investors tend to overestimate their investing skills, with men more overconfident than women.
- *Anchoring.* Investors have a habit of basing decisions on the past by “anchoring” to prior events and not rationally adjusting to changes.
- *Framing.* The way in which a situation is presented affects how people react. This ranges from buying the “sizzle” of an investment and not considering potential problems to loss avoidance, where investors are too conservative with their capital.
- *Disposition Effect.* Investors are unwilling to recognize losses by selling assets that have fallen in value, and more willing to recognize gains — i.e. holding losers too long and selling winners too soon.
- *Heuristics.* Heuristics refers to using rules of thumb to make decisions. This can create shallow thinking and biases that undermine investment decisions.
- *Mental accounting.* This is the tendency to compartmentalize investments into mental boxes by the source of the funds, how people invest those funds, and their tolerance of risk, even though it violates one of the basic rules of economics — that money is interchangeable. For example, a tax refund might be considered “found” money available for pleasure spending, while a paycheck is for essential expenses and savings.

Understanding these common mistakes can help investors pause and replace an emotional response with one that is rational. ■



Social Security

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receive by delaying the start of Social Security equals the cumulative value of payments that you would have received if you had chosen the earlier start date.

Example of breakeven calculation:

Assume you are eligible to receive \$2,150 per month at your full retirement age of 66, but only \$1,800 per month at age 63. If you start payments at age 63, you will receive \$64,800 (\$1,800 x 36 months) by the time you reach age 66. For delaying to make sense, you need to receive \$64,800 in extra payments beginning at age 66. Since you receive \$350 (\$2,150-\$1,800) more per month by waiting, it will take 185 months (\$64,800 divided by \$350) to reach break-even, or approximately fifteen years (185 divided by 12 months per year). So your break-even age is 81 years (age 66 plus fifteen years.) Caveat: this is a very simplistic example and does not include any adjustments for inflation, investment returns, taxes, etc.

Typically the break-even age for delaying payments is generally in the early to mid-80's, so delaying your start date is a great deal for individuals who live into their nineties and beyond. Many people don't recognize how quickly longevity is rising in the United States. For the average American couple who are age 65 today, there is a 50% chance that one will live to 92 and a 25% chance that one will live to 97 (typically it is the woman who survives her spouse). Realize that these are national averages, and if you are affluent and well-educated, your odds of living longer are significantly higher.

How long did your parents live? There are a number of online calculators to help you gauge your own life expectancy (one of the better ones is www.livingto100.com). No one likes to spend time thinking about how long they are going to live. But this is a key element in your timing decision. If you expect to live past your early 80's, you should strongly consider delaying Social Security.

Are You Still Working?

If you start Social Security before you reach full retirement age, any income you earn above \$13,560 (the 2008 annual limit) will reduce your benefits by one dollar for every two dollars earned. This is a disincentive to starting your payments early. Once you've reached your full retirement age, there is no penalty for any employment earnings, although your income level does impact the percentage of your Social Security payments that are subject to federal taxes. If you plan to continue working up until your full retirement age, then you should strongly consider delaying Social Security.

Do You Need the Money?

Sometimes you just cannot afford to wait. If you need the Social Security income to meet your monthly spending requirements in early retirement and you have no other options, then you should probably start your payments at the earliest possible date.

Will the System Continue in Current Form?

If you are close to retirement age, you should feel reasonably confident that the Social Security system will continue in its current form. The strong voting block of older Baby Boomers will likely protect benefit levels for years to come. Based on the Social Security Administration's 2007 annual report to Congress, the trust fund will be exhausted in 2041 and at that point the agency will be able to pay only 75% of promised benefits (if no changes occur). The seriousness of this situation is well-recognized in Washington but it is not clear yet what actions future Presidents and Congress may take. Options include raising the full retirement age further, reducing benefits to higher income recipients or taxing a greater percentage of Social Security benefit payments (currently a maximum of 85% of Social Security benefits are subject to income taxes). One item to note is that in 2007, for the first time, Medicare Part B premiums were means-tested; in other words, higher income beneficiaries started to be charged more. Perhaps that is a harbinger of what lies ahead for Social Security.

Nearly half of all eligible adults activate their Social Security benefits at the earliest possible date (age 62). Clearly, it is

tough to pass up money that's available to you just by filing a simple form. However our general advice would be to **at least** wait until your full retirement age (unless you need the money to live), and consider waiting until the "delayed" date if you think you are likely to live past 80. There is a break-even calculator at the Social Security website that you can use to determine your individual break-even date.

Where can you learn more?

The single best resource is the official Social Security website located at www.socialsecurity.gov. This website can help you find a local office, check your own benefits record, calculate your break-even age and learn more about potential upcoming changes. ■

Age to Receive Full Social Security Benefits	
Year of Birth	Full Retirement Age*
1937 or earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943-1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and later	67

* Note that "early" retirement age is 62 and "delayed" retirement age is 70 for all potential recipients, regardless of their current age.



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