



How Are My Social Security Benefits Calculated?

Social Security sends an annual statement of benefits to everyone over age 25 who has paid Social Security taxes but has not started receiving benefits. To understand how to affect those estimated benefit amounts, the following describes how benefits are calculated.

First, individuals must work at least 10 years with annual earnings meeting a minimum amount to qualify for benefits. For 2009, they must earn \$4,360 or more to qualify for a full year of Social Security earnings credit.

To calculate the monthly benefit available at full retirement age, Social Security then takes every year of earnings and adjusts them for wage growth. The Social Security Administration (SSA) essentially accounts for wage inflation by adjusting each year of earnings to a wage individuals would earn when they are age 60. One advantage of working past age 60 is that the SSA does not adjust earnings made after the age of 60 downward.

After adjusting each year for wage growth, the SSA uses the 35 highest years of earnings to calculate an average monthly earnings amount. This is called the average indexed monthly earning (AIME). For those who have worked fewer than 35 years, the SSA will factor in annual earnings of \$0 to complete the 35-year calculation. Alternatively, those who have 35 years of earnings can replace lower-earning years with higher-earning years by continuing to work (assuming their current earnings are higher than others being factored into the calculation).

The final step is to apply a weighted average formula to the AIME. By doing this, the SSA makes the initial dollars earned worth more. This benefits lower-income earners more as each additional dollar earned becomes less significant in the benefits calculation. In 2009, the first \$744 of AIME gets a 90 percent weighting, while any dollars earned above the \$744 level were weighted somewhere between 15 percent and 32 percent.

The following is an example of how two people with different earning histories would calculate their benefits. John's AIME is \$2,000, and Jane's AIME is \$6,000. Although Jane's AIME is 66.7 percent higher than John's, her monthly benefit at full retirement age will not be 66.7 percent higher than John's due to the Social Security weighting formula. In fact, her monthly benefit will only be 48.8 percent higher than John's at full retirement age.

Monthly Benefit Calculations					
		John		Jane	
	SSA Weighting	Monthly Earnings of \$2,000	Benefit Breakdown	Monthly Earnings of \$6,000	Benefit Breakdown
Level 1: < \$744	90%	\$744	\$669.60	\$744	\$669.60
Level 2: up to \$4,483	32%	\$1,256	\$401.92	\$3,739	\$1,196.48
Level 3: >\$4,483	15%	\$0	\$0	\$1,517	\$227.55
		Total Monthly Benefit	\$1,071.52	Total Monthly	\$2,093.63

	for John		Benefit for Jane	
--	-----------------	--	-------------------------	--

Finally, no matter how much money is earned or how many years Social Security taxes were paid, there is a cap on the monthly benefit. For 2009, the maximum benefit at full retirement age is \$2,323 a month.

Copyright © 2009, Buckingham Family of Financial Services. This material and any opinions contained are derived from sources believed to be reliable, but its accuracy and the opinions based thereon are not guaranteed. The content of this publication is for general information only and is not intended to serve as specific financial, accounting or tax advice. To be distributed only by a Registered Investment Advisor firm. Information regarding references to third-party sites: Referenced third-party sites are not under our control, and we are not responsible for the contents of any linked site or any link contained in a linked site, or any changes or updates to such sites. Any link provided to you is only as a convenience, and the inclusion of any link does not imply our endorsement of the site.