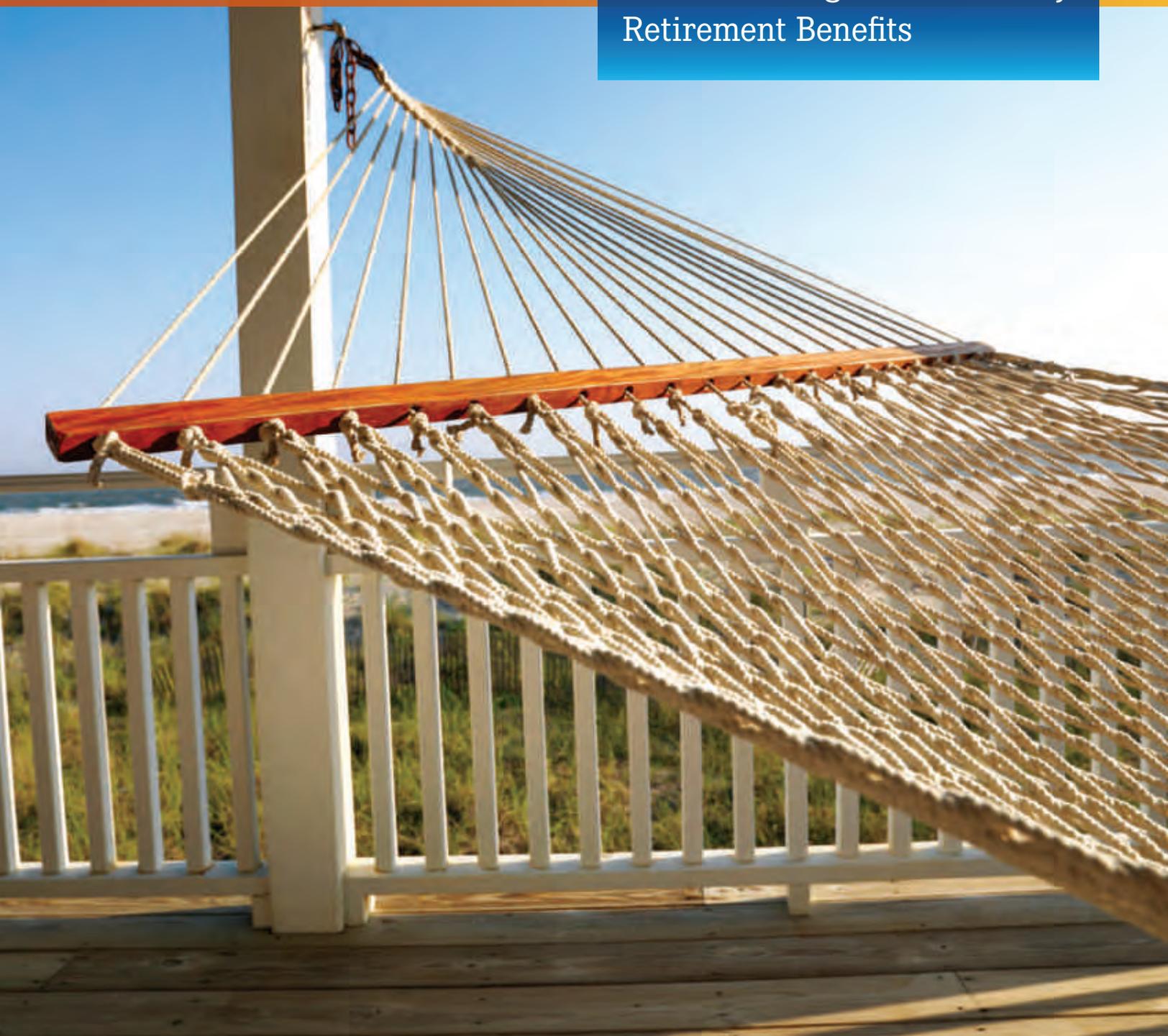


Understanding Social Security  
Retirement Benefits





**Conventional wisdom** holds that people should begin collecting Social Security retirement benefits as soon as possible, which is age 62. While this strategy has been prudent for millions of Americans until now, baby boomers are expected to live longer than any previous generation making waiting to collect potentially more beneficial. Deciding when to begin collecting Social Security benefits will have a significant impact on the retirement plans of those approaching retirement age.

This summary of Social Security retirement benefits is designed to assist you in creating an effective strategy for collecting your benefits. Work with your financial professional to ensure your decisions complement your overall retirement plan.

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## Collecting Retirement Benefits Based on Your Own Work History

### Qualifying for Retirement Benefits

When you work and pay taxes as mandated by the Federal Insurance Contributions Act (FICA), you earn “credits” toward Social Security (SS) retirement benefits. The credits are based on your annual earnings. You can earn up to four credits per year. Once you have acquired 40 credits (approximately 10 years of employment), you are fully insured and eligible to receive retirement benefits. FICA tax for old-age, survivors and disability insurance (OASDI) is withheld from each paycheck until you have earned up to the taxable earnings base for the year.

2012 FICA Amounts	
Taxable Earnings Base	\$110,100
Earnings Required to Earn One Credit	\$1,130

### Collecting Benefits at Full Retirement Age

All benefits are derived from your primary insurance amount (PIA). Your PIA is the monthly benefits for which you are eligible at your full retirement age (FRA). FRA was originally age 65 but, as a result of longer life expectancies, is gradually increasing to age 67.

Full Retirement Age	
Year Born	FRA
1937 or earlier	65
1938-1942	65 + 2 months for every year after 1937 until 1943
1943-1954	66
1955-1959	66 + 2 months for every year after 1954 until 1960
1960 and later	67

To determine your PIA, your average indexed monthly earnings (AIME) is calculated using your best 35 years of employment. If you have not worked for 35 years, some of your best years may be zero. For more information, please visit the Social Security Administration’s website at [www.ssa.gov](http://www.ssa.gov).

If you continue working after reaching FRA, the Social Security Administration (SSA) will automatically recalculate your benefits

each year you continue to work. If your current income is greater than your previously calculated “best 35 years,” your benefits will be automatically adjusted upward. The increase will generally be made in October of the following year but will be retroactive to January 1.

In addition to increases from additional years of working, SS retirement benefits are automatically increased each year to reflect cost-of-living adjustments (COLAs). COLAs are based on the Consumer Price Index for Urban Wage Earners and Clerical Workers and have averaged around 2.5% over the last 10 years.

Historical COLAs			
Year	COLA (%)	Year	COLA (%)
2003	1.4	2008	2.3
2004	2.1	2009	5.8
2005	2.7	2010	0.0
2006	4.1	2011	0.0
2007	3.3	2012	3.6

### Collecting Benefits Early

While your PIA is payable at your FRA, you are entitled to collect benefits as early as age 62. However, if you choose to collect benefits early, you will permanently reduce your benefits. Your benefits will not be adjusted when you attain your FRA. The amount of your reduction will depend on two things – your FRA and the number of months until you attain it. If you commence benefits at age 62, you will receive the maximum reduction. Your reduction will be smaller for each month delayed after age 62 but prior to reaching FRA.

Reduced Benefits at Age 62	
FRA	Monthly Benefits Reduction (%)
65	20
66	25
67	30

*When collecting before FRA, always consider the net (after-tax) benefits you will receive. A working spouse may cause more of your benefits to be taxed, and at potentially higher tax rates.*

## Working While Collecting Benefits Prior to FRA

Since SS retirement benefits are intended to be supplemental retirement income, the SSA has imposed consequences to collecting your benefits early if you have not actually retired and are still receiving wages or a salary. If you collect benefits prior to FRA, you will be subject to an earnings test every year until you reach FRA. If your earnings exceed certain thresholds, the SSA will withhold part or all of your benefits. The earnings test looks only at salary or wages of the individual collecting early benefits. It does not consider salary or wages of a spouse or any other type of income.

2012 Retirement Earnings Limits	
<b>Under FRA</b> \$1 of benefits withheld for every \$2 in earnings above the limit	\$14,640/year
<b>Year individual reaches FRA</b> \$1 of benefits withheld for every \$3 in earnings above the limit for months prior to attaining FRA	\$38,880/year
<b>Month individual reaches FRA and beyond</b> Reduction no longer applies	Unlimited

## Withheld Benefits

If benefits are withheld, they will not be refunded. However, your benefits will be adjusted to account for the benefits that were withheld on a go-forward basis when you reach FRA. For example, if your FRA was age 66 and you began collecting benefits at age 62, there would have been a 25% reduction applied. Assuming you returned to work at age 63, the SSA may have withheld the equivalent of two years' worth of benefits by the time you reached FRA. The SSA would then lessen your reduction of 25% to give you credit for the two years of benefits you lost. Your new reduction would be as if you started collecting benefits at age 64 (13.3% reduction) rather than age 62 (25% reduction).

## Waiting to Collect Benefits

If you elect to defer collecting benefits beyond your FRA, the SSA will give you a delayed retirement credit (DRC) for every month you defer up to age 70. This increase will be in addition to the COLA each year. Depending on your year of birth, your increase will range from 7% to 8% annually.

Delayed Retirement Credits	
Year of Birth	Annual Increase (%)
1939-1940	7.0
1941-1942	7.5
1943 or later	8.0

## Withdrawal of Application

If you start collecting your benefits and change your mind, you can file a “Request for Withdrawal of Application” form with the SSA, which will review your request. If your request is granted, you need to repay the SSA all of the payments you and anyone else have collected to date based on your work history. You do not have to pay any penalty or interest on the amount repaid. You can subsequently refile. The SSA recently restricted withdrawals to within 12 months of collecting benefits and will only allow one withdrawal per lifetime.

If any of the benefits repaid were subject to federal income tax in earlier years (discussed later), you may be entitled to an itemized deduction on your tax return in the year of repayment. If the amount of benefits previously taxed is \$3,000 or less, you may be entitled to claim a deduction on Schedule A (Form 1040), line 23, subject to the 2% of adjusted gross income (AGI) limit. If the amount exceeds \$3,000, you may be entitled to claim a deduction on Schedule A, line 28. This is not subject to the 2% of AGI limit. Please refer to IRS publication 915 for other tax options when amounts exceed \$3,000.

## Windfall Elimination Provision (WEP)

If you work for an employer who does not withhold FICA taxes from your salary, such as a government agency, the pension you receive based on that work may reduce your SS retirement benefits. WEP primarily affects individuals who earned a pension in any job where FICA taxes were not paid and who worked in other jobs long enough to qualify for SS retirement benefits.

## Taxation of Benefits

About one-third of people who collect SS benefits have to pay income taxes on them. Individuals with high total incomes must include up to 85% of their benefits as income for federal income tax purposes. Special step-rate “thresholds” on provisional income determine the amount on which you may be taxed.

To determine your provisional income for this purpose, you must include all of your earnings (including pensions, dividends and taxable interest from investments and other sources) plus interest on tax-exempt bonds and 50% of your SS benefits. The thresholds for taxation of your benefits are not currently indexed for inflation.

Provisional Income	
Single or Head of Household	Married, Filing Jointly
Base amount \$25,000 = not taxed	Base amount \$32,000 = not taxed
\$25,000–\$34,000 = up to 50% taxable	\$32,000–\$44,000 = up to 50% taxable
Above \$34,000 = up to 85% taxable	Above \$44,000 = up to 85% taxable

*Requests for Withdrawal of Application are intended to be used by individuals who commenced benefits early and returned to work. It is not, however, limited to just these individuals.*

*WEP closed a loophole that enabled people who worked in both covered and non-covered employment from appearing to be low-wage workers and receiving higher benefits.*

*Roth distributions do not currently impact the taxation of SS benefits.*

## Collecting Retirement Benefits Based on a Family Work History

### Beneficiaries Entitled to Collect Off Your Benefits

If you are entitled to collect retirement benefits, certain other individuals may be entitled to collect benefits based on your work history once you file for yours. If you have been married for at least one year, your spouse may be entitled to collect spousal benefits. Additionally, any children you have may be entitled to benefits.

Beneficiaries Entitled to Collect Off Your Benefits	
Your Spouse	Your Unmarried Child
<ul style="list-style-type: none"> <li>▶ Age 62 or over</li> <li>▶ Any age if caring for your child who is under age 16 or disabled before age 22</li> <li>▶ Age 60 if widower</li> </ul>	<ul style="list-style-type: none"> <li>▶ Under age 18, or up to age 19 if in high school</li> <li>▶ Any age if disabled before age 22</li> </ul>

### Maximum Family Benefits

The amount of benefits that members of a family may receive on the earnings record of one worker is limited. The limit varies between 150% and 188% of the worker's PIA. If the total benefits due to your spouse and children are more than the limit, their benefits will be reduced proportionately to bring the total within the limit. Your benefits will not be affected. Any benefits payable to an ex-spouse (addressed later) are not included in the family maximum.

### Collecting Benefits as a Spouse

If you are married to an individual who files for SS retirement benefits and you are at least age 62, you may be entitled to collect spousal benefits. Spousal benefits will be equal to 50% of your spouse's PIA. If you are entitled to your own benefits, your benefits will always be paid first. If your benefits are less than 50% of your spouse's PIA, spousal benefits will be paid in addition to your own. These combined benefits will equal 50% of your spouse's PIA, assuming you start collecting at FRA or later. For example, the husband described below has a PIA of \$2,200. The wife is entitled to 50% of that amount, or \$1,100, as spousal benefits. However, because she is entitled to her own benefits and has her own PIA of \$600, the spousal benefits will be reduced by that amount. The wife, starting to collect at FRA, will receive a combination of benefits – \$600 (own) and an additional \$500 (spousal) to equal \$1,100.

### Wife's Estimated Benefits

Retirement Age	Monthly Benefits (\$)
62	450
66 (FRA)	600
70	792

### Husband's Estimated Benefits

Retirement Age	Monthly Benefits (\$)	Spousal Benefits (\$)	Adjusted Spousal Benefits (\$)
62	1,650		350
66 (FRA)	2,200	1,100	500
70	2,904		308*

\* Assumes wife started collecting both her own benefits and spousal benefits at age 70.

### Collecting Spousal Benefits Early

If you collect spousal benefits prior to your FRA, your adjusted spousal benefits (amounts in addition to your own benefits) will be reduced. If your spouse collects benefits prior to FRA, it will not reduce the amount you are entitled to receive. Only if you collect early will your spousal benefits be reduced.

### Waiting to Collect Spousal Benefits

Unlike your own benefits, spousal benefits will not receive guaranteed annual increases if you defer collecting them beyond FRA. Spousal benefits are at their maximum when you reach FRA, so there would not be any advantage to defer collecting them.

### Collecting Survivor (Widower) Benefits

If you have been married for at least nine months and your spouse passes away, you may be entitled to survivor benefits. The amount of your survivor benefits is dependent on when your spouse commenced benefits. If the death occurs prior to your spouse collecting benefits, your survivor benefits will be equal to 100% of your spouse's PIA when you attain FRA. If your spouse had begun collecting benefits, your survivor benefits will equal his or her actual benefits, assuming you have attained FRA. The only exception is if he or she were collecting benefits that were reduced more than 17.5%. In that case your survivor benefits will be 82.5% of the decedent's PIA.

The survivor benefits will replace your other benefits if higher. The chart below shows the expected survivor benefits for an individual who began collecting benefits at age 62, FRA and age 70.

Husband's Estimated Benefits		
Retirement Age	Monthly Benefits (\$)	Survivor Benefits (\$)
62	1,650	1,815
66 (FRA)	2,200	2,200
70	2,904	2,904

You can collect survivor benefits as young as age 60. If you collect at age 60, your survivor benefits will be reduced by up to 28.5%. It is possible to collect reduced survivor benefits at age 60, and then convert to your own unreduced benefits at FRA or later. If you remarry before age 60, survivor benefits will not be paid unless the subsequent marriage ends. Remarriage after attaining age 60 does not prevent or stop entitlement to benefits.

## Filing and Suspending

If you are at least FRA, you can elect to file for benefits but suspend collecting them until a later date. This would enable your current spouse to collect spousal benefits while your own benefits earn DRCs. Filing and suspending also enables you to retroactively start collecting as of your filing date if you change your mind about suspending.

## Choosing Between Benefits

If you are entitled to both individual and survivor benefits, you can choose to begin collecting one and then switch to the other at a later date. Similarly, if you are at least FRA and married, you can claim spousal benefits only and then switch to your own benefits (including any earned DRCs) at a later date.

## Government Pension Offset

Individuals who receive a pension from a federal, state or local government based on work where FICA taxes were not withheld may have their spousal and/or survivor benefits reduced. SS benefits will be reduced by two-thirds of the government pension. Consider the following scenario: The wife will receive a government pension of \$1,500 a month, while her husband will receive SS benefits of \$2,200. Generally, she would be entitled to spousal benefits equal to 50% of her husband's PIA, or \$1,100. Because she is covered by a government pension, her benefits will be reduced by two-thirds of her pension, or \$1,000. She will receive spousal benefits of \$100. The same \$1,000 reduction will also be applied against any survivor benefits she may be entitled to.

Wife's Government Pension	
Monthly Pension (\$)	Gov't Pension Offset (\$)
1,500	1,000

Husband's Social Security Benefits				
Age	Monthly Benefits (\$)	Spousal Benefits (\$)	Adjusted Spousal Benefits (\$)	Survivor Benefits (\$)
62	1,650		0	815
66	2,200	1,100	100	1,200
70	2,904		100	1,904

## Divorced Individuals

If you are not married but had previously been married to the same individual for at least 10 years, you would be entitled to collect spousal and/or survivor benefits as discussed earlier. As an unmarried divorced spouse, you may be entitled to spousal benefits once both you and your ex-spouse reach age 62. You are not required to wait until your ex-spouse files for benefits. Amounts payable to an ex-spouse will not reduce any benefits to which the worker or his or her current spouse are entitled.

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Sources: BlackRock; Social Security Administration; Internal Revenue Service.

Please see the Social Security Administration's website at [www.ssa.gov](http://www.ssa.gov) for more information, restrictions and limitations about Social Security benefits.

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