

Ernie the electrician understands Social Security

By [William Shipman](#) 12:24 PM 04/22/2011

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Ernie was pretty certain he had made the right decision after hearing the senators propose that the Social Security retirement age should be increased to age 70. At first glance it seemed to make sense. People are living longer so their benefits should start a little later. And this would help the system's finances. But looking back at his own career as a self-employed electrician, he began to question if it actually did make sense. He also wondered whether the senators knew what he knew. If they didn't, they should. If they did, why did they make such a proposal? Here's what he thought they should know.

Ernie started working in 1966 at age 21. He made \$6,900 his first year, and just average wages thereafter. But he was frugal, for his parents taught him to save no matter what. So he saved every year the same amount he paid in Social Security taxes that he assumed were set aside for his retirement. In the first year it wasn't much, just \$360.

He wasn't a sophisticated investor, so he took what he thought was good advice, and invested in broad indexes of stocks and bonds with a 70/30 percent mix. He didn't day trade, pick stocks, or try to time the market. He didn't know anything about that. The only change he ever made was at age 56 when he restructured the portfolio to a more conservative 50/50 stock/bond allocation. He retired at the end of last year, at age 66, the age at which he could receive full Social Security benefits.

When he applied for his benefits in 2010, he was advised by the Social Security Administration that his first monthly check would be \$1,664, and he would receive it in mid-January 2011. He was also told that if he chose Medicare Part B, the premium would be deducted from his benefit check. He earned \$48,000 in 2010 so his first year's benefit of \$19,968 totaled about 41 percent of his last year's pay check.

Ernie wanted to know how much he could withdraw from his portfolio to supplement his benefits. Finance not being his strong point, he sought help. He was advised to re-structure the portfolio to earn a more conservative 4.5 percent return. He was also told that a man of his age had a life expectancy of about another 18 years, but that he shouldn't take that as the number of years he would live. It was just an average. He should be conservative, and assume he'd live another 25 years to age 91. After he agreed to these points, his advisor told him how much he could withdraw.

Ernie was shocked. Even after including the stock market crash of 2008, he could take out \$37,000 in 2011, and increase it every year for 25 years by 3.0 percent, the historical inflation rate. Or he could buy an annuity providing a comparable benefit. Of course he could take out less, so as to leave some assets for his children. Or he may want to hedge whether he'll live longer than 91.

Ernie was confused. He couldn't figure out why saving and investing the same amount he paid the government resulted in almost double the benefit.

When he shared all of this with his children, they were angry that they were forced to pay the government their savings when they likely could earn more on their own. Not only that, if the senators' proposal became law, they wouldn't even get their full Social Security benefits until they were 70, four years later than their

father. The senators were proposing to cut their already-low projected benefits.

When they asked the financial advisor for his view, he spoke more broadly. He said that our government has grown way beyond the vision of our founding fathers. He said that Washington politicians from both parties, and bureaucrats, have for decades successfully decreased our freedom and liberties as they have regulated more and more of our lives, including our retirement. Without some spark, he didn't think it would change. He said the senators' proposal was typical; don't let folks keep more of the fruits of their labor, rather tax them, and then provide lower benefits, all in the name of protecting them, and saving a government program.

Ernie was even more concerned about his kids' future. They would need his help if the government kept on this path. To him, the senators' proposal was just another bit of evidence that it probably would. So he decided to take out a lot less than \$37,000, and leave the rest to his children. And though they didn't know it, the senators helped him make that decision.

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