Working in Retirement: A Rulebook

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For 67-year-old Marilyn Arnold, finances played a role in her decision to keep working when she retired 4 years ago from her position as a managing partner at New York Life Insurance Company after 29 years in the insurance business.

"I felt that if I could continue to work doing something I wanted to do and not have to start taking Social Security, or draw from my retirement funds too much, it would be a win all around," she says.

Tapping into her childhood love of sewing, she opened her own small business, Marilyn Arnold Designs, in Lee's Summit, Missouri. Her forte: creating pillows and blankets as keepsakes made from wedding gowns.

Many older Americans are continuing to work during retirement for a plethora of reasons—from a personal reward like rediscovering a childhood passion and staying socially connected with a network of people to doing something that provides a sense of purpose and a chance to give back.

A paycheck, too, is a silver lining for many workers who worry that they will outlive their money. Many people want to continue working well past "normal retirement age." But intentions and reality don't always match when it comes to working in retirement. In fact, according to a Fidelity-sponsored survey, only 3% of pre-retirees and 32% of recent retirees surveyed said they wanted to retire at or before age 60. Most wanted to keep working. However, 38% of recent retirees actually retired at or before age 60–many because of layoffs or forced early retirement. Bottom line: Far fewer people actually work in retirement than *say* that they want to work in retirement.

For some, saving more money for retirement earlier in their career may be a smart move, especially if they leave the workforce earlier than planned.

"People are clearly concerned about not having enough savings to last for their lifetime, especially since we're living longer, on average," says Chris Farrell, author of *Unretirement: How Baby Boomers Are Changing the Way We Think About Work, Community, and the Good Life*. "For many people, earning an income well into the traditional retirement years shores up household finances. Their goal is to preserve their quality of life with age."

The payback can be far more than purely financial, though, even if finances are a primary incentive. "The activity of working, of using your brain, of interacting with others is extremely valuable for your health and your happiness," says Steven Feinschreiber, senior vice president of research at Fidelity. "Research suggests that working can actually help you live a longer and healthier life."

Regardless of why you decide to keep working in retirement, there are certain financial rules and regulations to keep in mind.

Contributing to retirement accounts

A key advantage of ongoing income is that you can regularly contribute to your retirement savings accounts, says Farrell.

For 2019, total contributions to all your traditional and Roth IRAs can be up to $6,000 ($7,000 if you're age 50 or older), or your taxable compensation for the year, if your compensation is less than this dollar limit, per Internal Revenue Service rules.

One caveat: You can't make regular contributions to a traditional IRA in the year you reach 70½ and thereafter. However, you can still contribute to a Roth IRA and make rollover contributions to a Roth or traditional IRA regardless of your age. You must also take the required minimum distribution (RMD) from your traditional IRA beginning at 70½, regardless of your work status. If you have a Roth IRA, RMDs don't apply to it during your lifetime.

Your 401(k), or similar employer-based retirement plan, is a different story. In general, you can continue stashing away money in your current employer-provided plan as long as you're still working there, even part-time. And you can delay taking your RMD until after you retire. You will, however, need to take the RMD from any former employer's plan beginning at age 70½, unless the money was rolled into your current employer's plan.

Employees may contribute up to $19,000 to their 401(k) plans in 2019, with a higher total contribution limit (employer plus employee) of $56,000. For those age 50 and older, an additional "catch-up" employee contribution of up to $6,000 is also allowed. "To have enough money to pay for your expenses in retirement, we generally recommend saving at least 15% of your income per year," explains Feinschreiber. "That's total—your contributions and your employer's combined, and assumes working to age 67. It may make sense to continue working past age 62, so you can contribute more to your 401(k) and other retirement savings accounts."

Social Security benefits

Another plus of working longer is that you can delay filing for Social Security benefits. You can begin taking monthly Social Security retirement benefits at age 62, but the amount will be reduced by about 30% versus the amount you would receive if you wait until you're what Social Security calls full retirement age (FRA)—66 or 67 if you were born from 1943 to 1959; 67 if you were born in 1960 or later.

If you can delay Social Security beyond FRA, your Social Security benefits are boosted by 8% a year (over the amount at FRA) for every year you postpone receiving checks from your FRA to age 70. That's a powerful boost.

Earning income after you reach your FRA or older doesn't affect your benefits, no matter how much you earn. For those who opt to apply for benefits before they reach FRA and continue to earn income, there's a temporary hitch. By law, if you're younger than FRA and receiving Social Security benefits, you can earn up to $17,640 in 2019, according to Social Security rules, without a reduction in your benefit amount.

If you're younger than FRA, and earn more than the limit, Social Security deducts $1 from your benefits for each $2 you earn above the threshold. In the year you reach FRA, $1 in benefits is deducted for every $3 you earn above a different limit. After that, there are no earnings tests and no benefit reductions based on earned income.

The "earnings" counted are what you make from your job and/or your net earnings from self-employment. These include bonuses, commissions, and vacation pay, because they're all based on employment, but do not include investments, pensions, and other retirement income, or veterans' or other government or military retirement benefits.

In truth, you don't ultimately lose any of your Social Security benefit due to earning more than the income limits. If you exceed the limit allowed from age 62 to 66, the funds you were docked will be returned to you in the form of a permanent increase that the Social Security Administration (SSA) recalculates for you. The SSA website stipulates that after you reach FRA, "your benefit amount is recalculated to give you credit for any months in which you did not receive a benefit because of your earnings."

"It can be a bit of a shock when the reduction happens," says Farrell. "But you don't lose the benefit. Most people don't understand that."

The good news is that your Social Security benefits can actually ramp up as a result of your employment after you reach FRA, because they are calculated using your highest 35 years of earnings. If your earnings after FRA would replace any of your 35 highest-earning years used to calculate your benefit, then the SSA will do a recalculation, and your monthly benefits will bump up accordingly.

Keep in mind, of course, that SSA benefit could be subject to income tax if you are also earning compensation from a job or self-employment.

Tip: Even though your benefits are not lost from working and collecting Social Security at the same time, the earned income you receive while collecting Social Security could result in up to 85% of your Social Security income becoming subject to federal income taxes.

Health and medical

If you're planning on your former employer picking up part of the tab for your health care in retirement, think again. Only 25% of large companies offer health care benefits to retirees, down from 35% in 2004, according to a 2017 employer survey by the Kaiser Family Foundation.

So if you're hunting for a new job in retirement, consider seeking an employer who offers health insurance while you are employed at your "retirement job." At the very least, continuing to earn some income can help defray your health care bills before and after Medicare kicks in at 65. "Health care expenses are generally one of the largest expenses in retirement," notes Feinschreiber. Couples retiring at age 65 are expected to incur $285,000 in health care costs on average during their retirement years, according to the 2019 Retiree Health Care Cost Estimate by Fidelity Investments. The estimate doesn't include the added expenses of nursing home or long-term care and assumes traditional Medicare coverage. "This is the money on top of Medicare," Feinschreiber says. "So it's thousands of dollars per year, which may be more than many people can afford. Working longer, even part-time, can help."

Traditional pension plans

Although increasingly rare these days, you or your spouse may have qualified for a defined benefit plan that guarantees a specific benefit or payout upon retirement. Make sure you fully grasp how your benefit is determined before you decide to stay or leave your job. If you've maximized your pension income, it may give you the financial freedom to pursue an "encore" career. Some defined benefit plans calculate your benefit based only on a precise number of years you have worked for your employer. So ask your HR representative if your plan stops earning benefits after 30 years, if your benefit is frozen, or whether your pay may impact your final benefit.

In some plans, the pension benefit is calculated as a percentage of earnings during your final years on the job. So if you enter a "phased retirement" working arrangement and trim back your hours and earnings during your last few years, you might shrink your pension benefits too.

For some, staying on job later in your career may have more to do with qualifying for a retiree medical benefit. For example, you may have been offered an early retirement option at age 54. However, if you stayed on the job for another year, you may have qualified for an early retirement subsidy or other benefits at age 55 because you would have worked for at least, say, 10 years for the same employer. Do your homework and know your options.

Lastly, even if your pension benefit has stopped accumulating, you may choose to stay on the job because you want to continue your employer-sponsored health care coverage until you reach Medicare eligibility at age 65.

Impact on taxes

According to Farrell, it's possible that staying on the job an extra couple of years might push you into a higher tax bracket, especially if you begin to take taxable distributions from your IRA, or other pension benefits that count as income on top of your salary.

Employees can avoid being tripped up by knowing how close their current earned income level may be to the next tax bracket, advises Feinschreiber. If you need more money to live on than you're earning, or are required to take an IRA distribution, try to avoid using any other tax-deferred accounts (that don't yet require a distribution). Instead, consider taking remaining funds from your after-tax accounts, such as your checking accounts, savings accounts, or brokerage accounts, for which the bulk of the money has already been taxed.

For many people, like Arnold, the main thing about working in some fashion in their 60s and beyond isn't truly "about paying the mortgage and getting rid of debts—though that can be part of it—but it's typically, ‘Let's do something where I can use my knowledge, my skills, my experience, and have some fun,'" Farrell says.