Social Security COLA Can Sweeten Your Finances

If you're receiving Social Security benefits, you will see some bigger checks in 2025. How can you best take advantage of this increase?

First, here's some background: Each year, the Social Security Administration adjusts payments based on the inflation rate. In 2025, this cost-of-living adjustment, or COLA, will be 2.5%. While this figure is lower than the 3.2% bump for 2024, and significantly lower than the 8.7% increase in 2023, when inflation was much higher, it's still close to the 20-year average of 2.6%.

The actual dollar increase you'll see will depend, of course, on the size of your regular Social Security payments. In any case, though, you may find that the bigger checks can help in these areas:

• *Withdrawals from investment portfolio* — Once you retire, you'll likely have to start tapping into your traditional IRA, 401(k) and other investment accounts. Naturally, your goal is to avoid taking out so much in your early retirement years that you risk running low on money later. A higher Social Security payment may allow you to keep withdrawing the same amount, or possibly even lower your taxable withdrawals. This is especially important when the inevitable market downturns occur — as much as possible, you'll want to avoid withdrawing money, which essentially means selling taxable investments when the market is down.

• *Cash reserves* — It's generally a good idea for retirees to keep up to 12 months' worth of portfolio withdrawals in cash, so the money is readily available when you need it, along with another three to six months of spending kept in an emergency fund. Having these reserves available can help you avoid dipping into your long-term taxable investments to pay for short-term needs, such as a major car repair or a needed home improvement.

• *Debt reduction* — If the higher Social Security payments allow you to improve your cash flow, you might be able to pay down some debts, especially those that carry a high interest rate. And lowering your debts, just like building your cash reserves, can help protect you from increasing your withdrawals from your retirement accounts.

In addition to implementing the new COLA, the Social Security Administration is also raising the earnings limit for those reaching their full retirement age, which, for most people, will be between 66 and 67. If you are under your full retirement age for all of 2025, Social Security will deduct $1 in benefits for every $2 you earn above the new limit of $23,400, up from $22,320 in 2024. If you reach your full retirement age in 2025, Social Security will deduct $1 in benefits for every $3 you earn above $62,160, up from $59,520 in 2024. Starting with the month you reach your full retirement age, you can earn as much as you want without having your benefits reduced. At that point, Social Security will also recalculate your benefit amounts to give you credit for the months you received reduced benefits due to your excess earnings.

And here's one final COLA-related change: For 2025, the Social Security tax limit will rise to $176,100, up from $168,600 in 2024.

It's not all that often when a source of your guaranteed income goes up. So, start thinking now about how you can use these COLA changes to improve your financial situation in 2025.

This article was written by Edward Jones for use by your local Edward Jones Financial Advisor. Edward Jones, Member SIPC

Nov. 8, 2024
547 words