Retirement Security for All Americans: The Role of Social Security

American Academy of Actuaries Briefing on
"Modernizing the U.S. Retirement System –
Aligning Policy With Reality"

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Social Security: What Does It Provide?

- Retirement and survivor benefits started in 1940
- Eligibility age was lowered from 65 to 62 in 1957 for women and 1962 for men
  - Full retirement age rises from 65 to 67 by 2022
- Disability benefits started in 1957

- Benefits rise with average wage *across generations*—but with CPI after eligible
- Payroll taxes are roughly pay-as-you go
  - Tax rate rose from 2% to 12.4% as the system matured
  - Minimal advance funding left investment in private hands

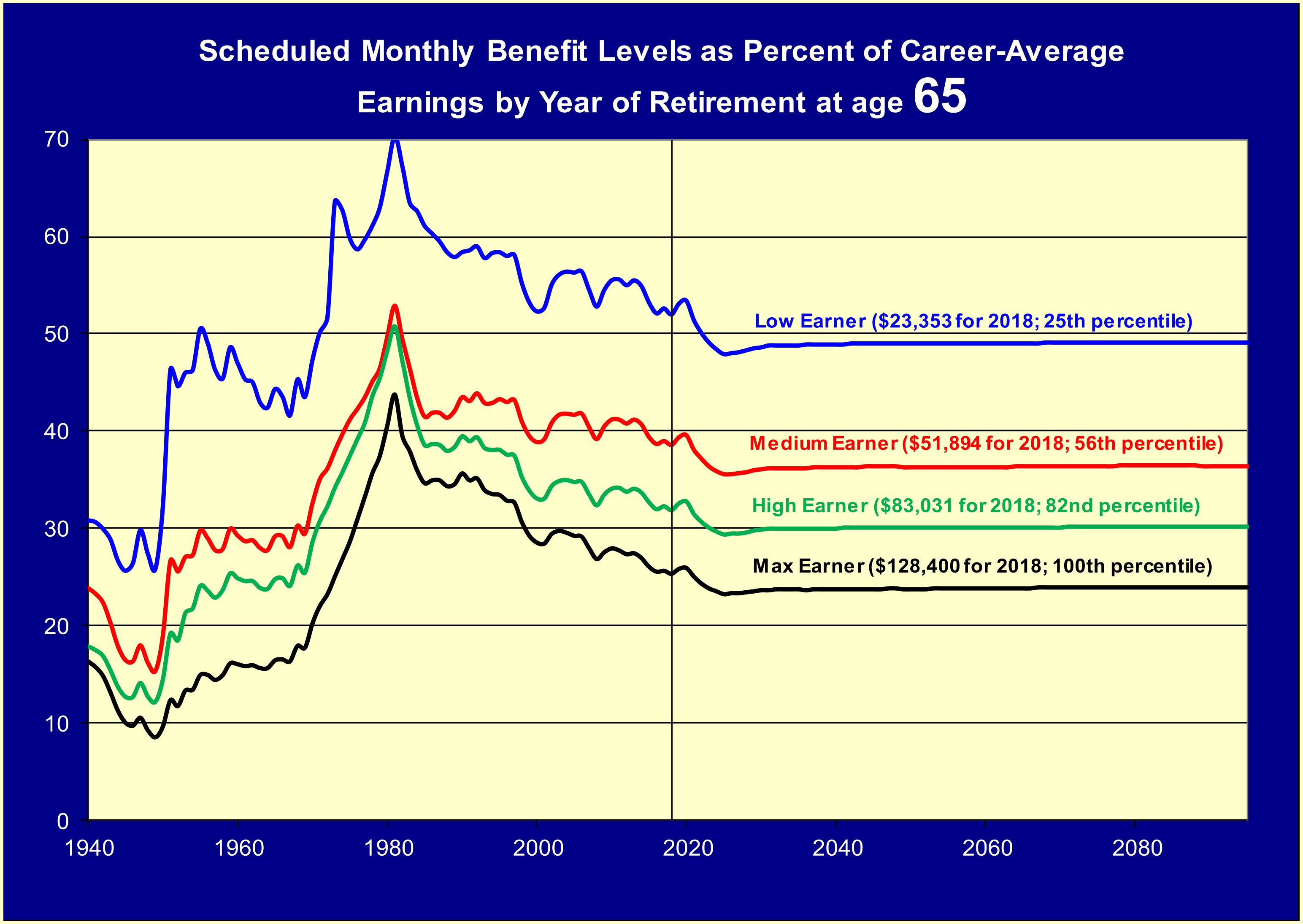
Social Security: What Does It Provide?

- Over 95% of those over age 62 are eligible for benefits
- At the end of 2017, beneficiaries are:
  - – 42 million retired workers
  - – 9 million disabled workers
  - – 4 million widow(er)s
  - – 4 million children
  - – 2 million spouses

Social Security: What Does It Provide?

- Intent was a 3-legged stool
  - Social Security—floor of protection
  - Employer-provided pension
  - Personal savings
- Target 75-80% “replacement rate” in total?
- So how much has Social Security provided?
- And how much will it provide in the future?
  - First, consider benefit starting at age 65

Replacement Rates at Age 65



Social Security: What Does It Provide?

- The large majority start benefits by NRA (now 66+), because there is no earnings test after NRA

- Missed opportunity to purchase a CPI-indexed life annuity
  – By deferring start from age 66 to 70, the monthly payment increases by 32%
  – And this carries over to a surviving spouse

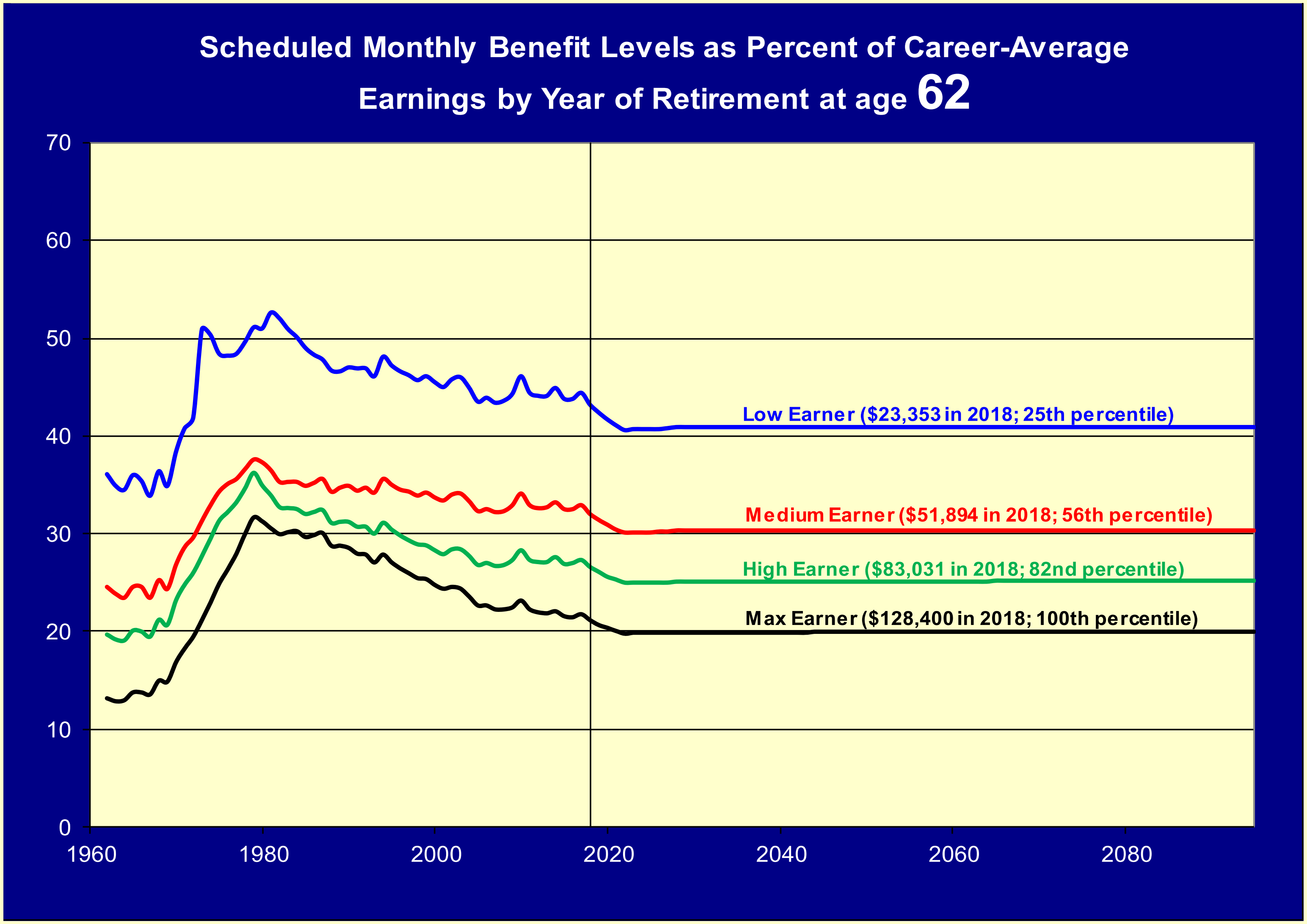
Social Security: What Does It Provide?

- What if start benefits earlier than age 65 (Medicare eligibility age), say at 62?

- Monthly benefits starting at age 62 are about:
  - 20% lower than if you start at 65
  - 25% lower than if you start at 66

  And the reduction is for life

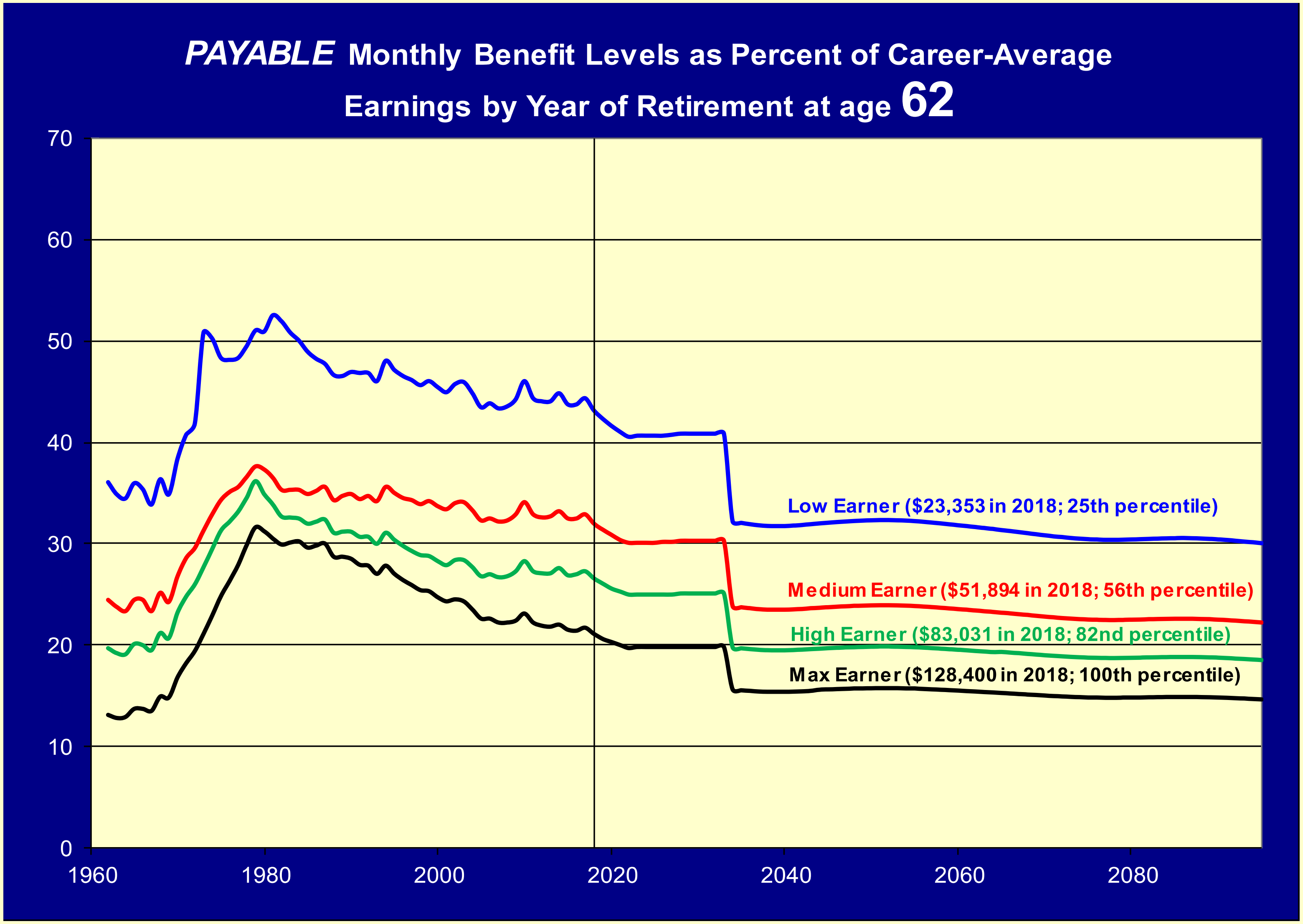
Replacement Rates at Age 62



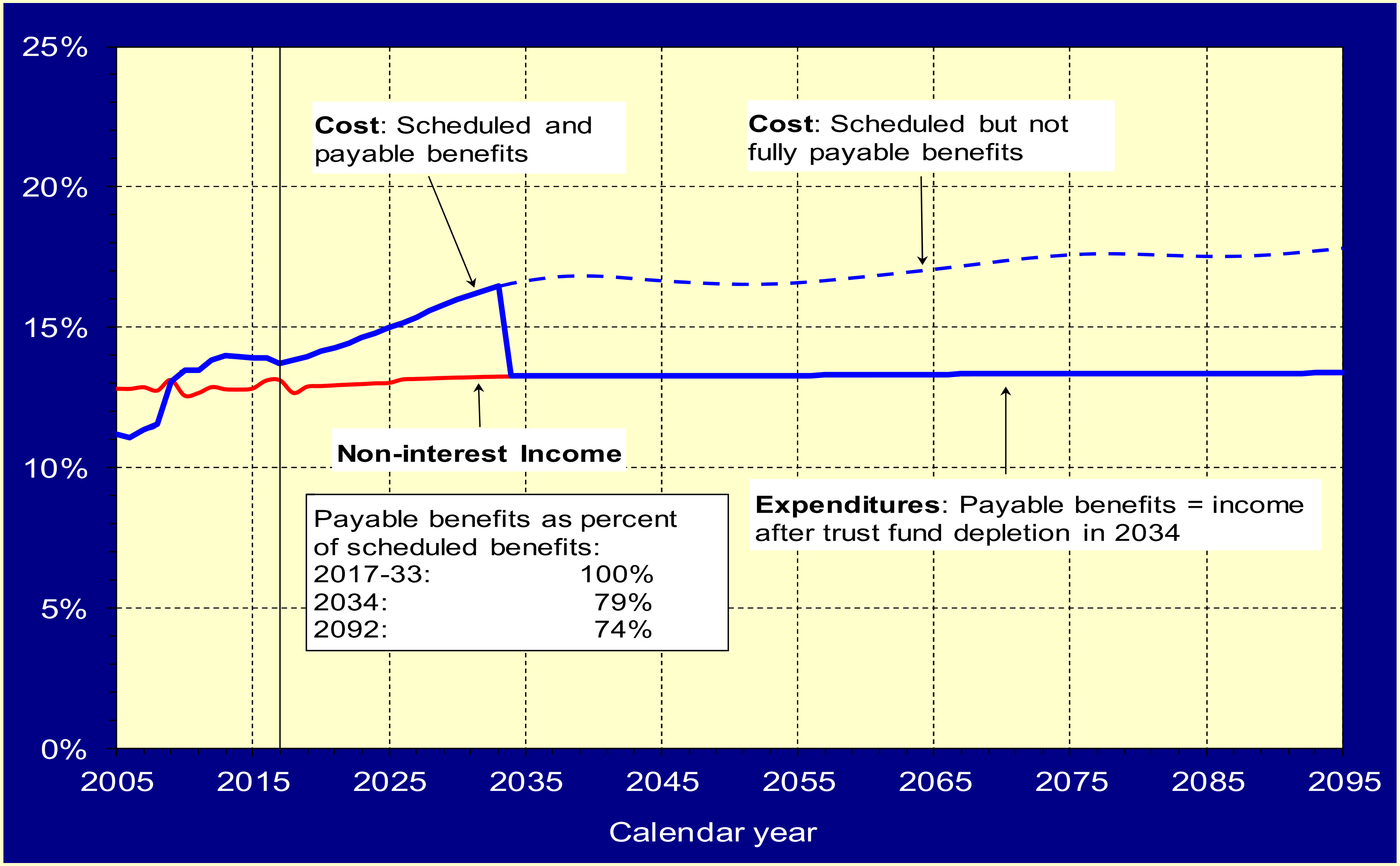
Social Security: What Does It Provide?

- But the trust fund reserves are projected to become depleted in 2034
  - If nothing is done, only 79% of scheduled benefits will be payable in 2034
  - And this drops to 74% by 2092
  - This is what can be provided with the currently-scheduled level of revenue for the program

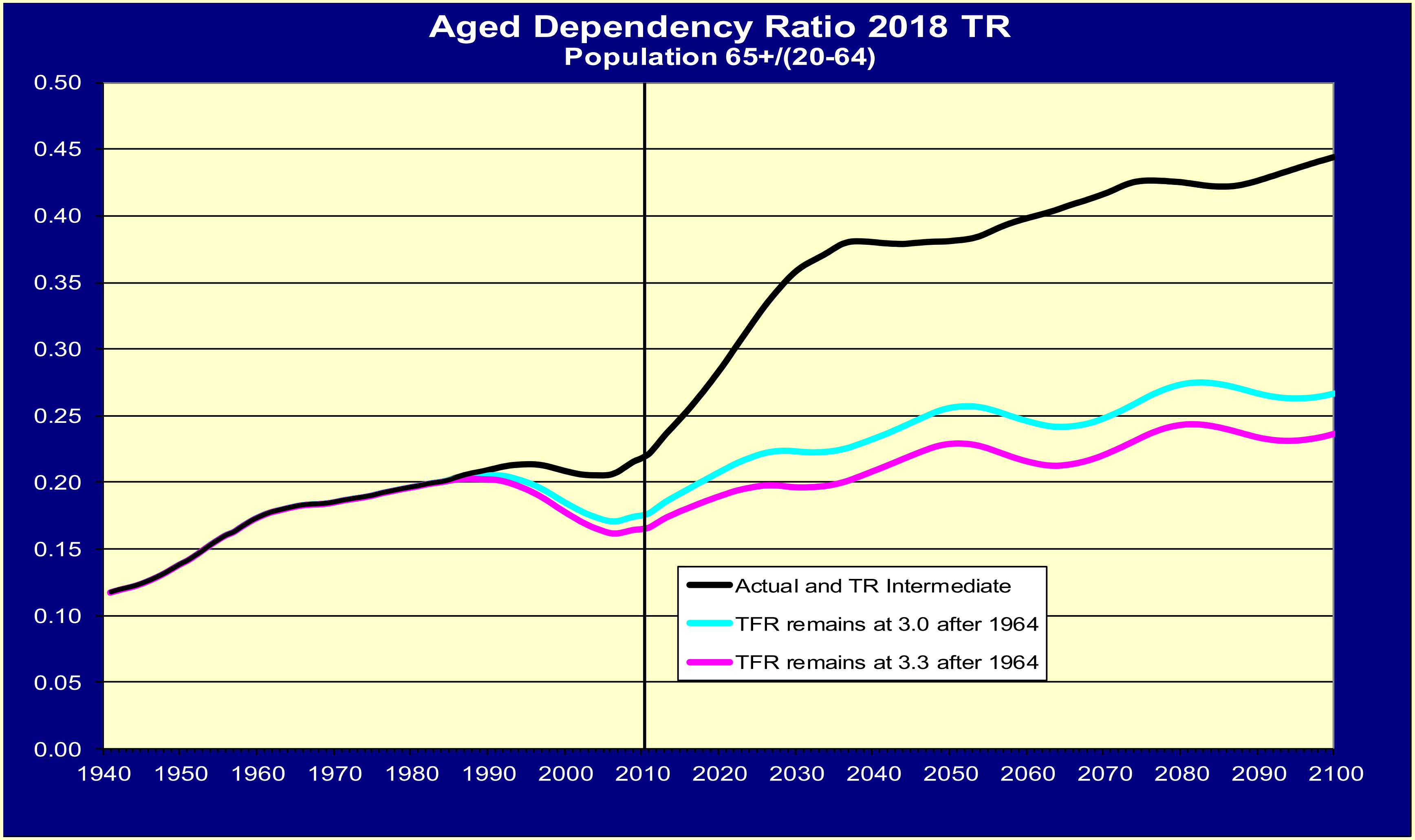
Replacement Rates at Age 62: Payable Benefits



OASDI Annual Cost and Non-Interest Income as a Percent of Taxable Payroll



Rising Cost as a Percent of Payroll due to Changing Age Distribution (affects all 3 legs)



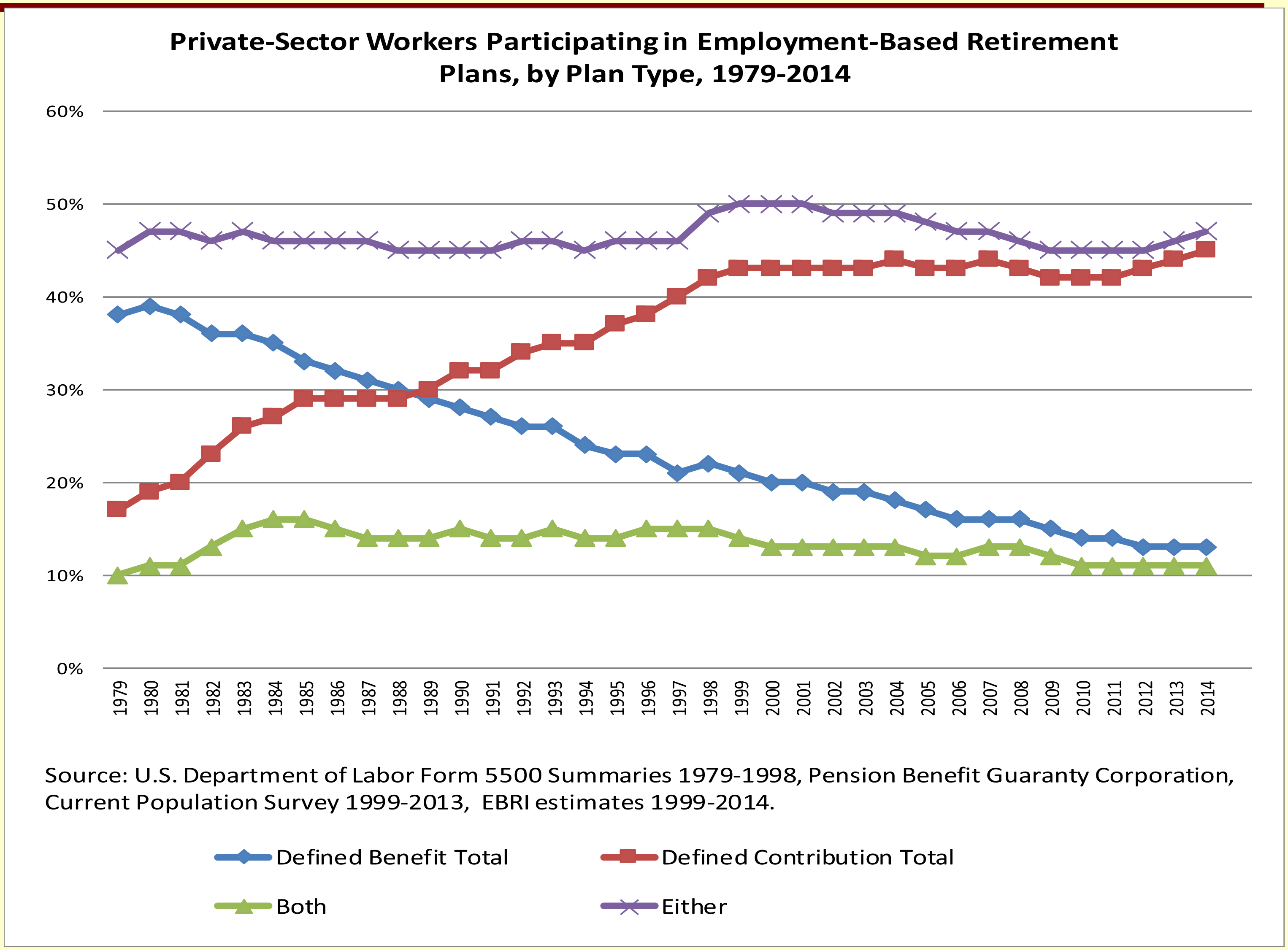
Solutions: Get to Sustainable Solvency (or at least make progress)

- By 2034, reduce cost by about 25% or raise revenue by about 33%
- Or some combination of these

- Lowering benefits and raising taxes will both put additional pressure on the other two legs

- Keep in mind, it is a PAYGO world, and accumulated assets are only worth what others will pay

The Big Shift in Employer-Sponsored Pensions: How Much Will Be in a Lifetime Annuity?



Some Ways to Lower Social Security Cost that Have Been Considered

https://www.ssa.gov/oact/solvency/provisions/index.html

- Lower benefits for retirees—not disabled?
  - Increase normal retirement age (lowers OASDI cost, but increases DI cost)
  - Can exempt long-career low earners (Simpson Bowles)
- Lower benefits mainly for high earners?
  - Reduce PIA above some level
  - Often combined with increasing PIA below some level, subject to work year requirements
- Lower benefits mainly for the oldest old?
  - Reduce the COLA by using a chain-weighted version
  - But some say increase it with the CPI-E (based on purchases of consumers over age 62)

Some Ways to Increase Social Security Income that Have Been Considered

https://www.ssa.gov/oact/solvency/provisions/index.html

- Raise the 12.4 percent OASDI payroll tax rate?

- Raise tax on highest earners?
  - Increase taxable maximum amount
  - Some tax on all earnings above the maximum

- Tax employer group health insurance premiums?
  - Affects only middle class if taxable maximum remains