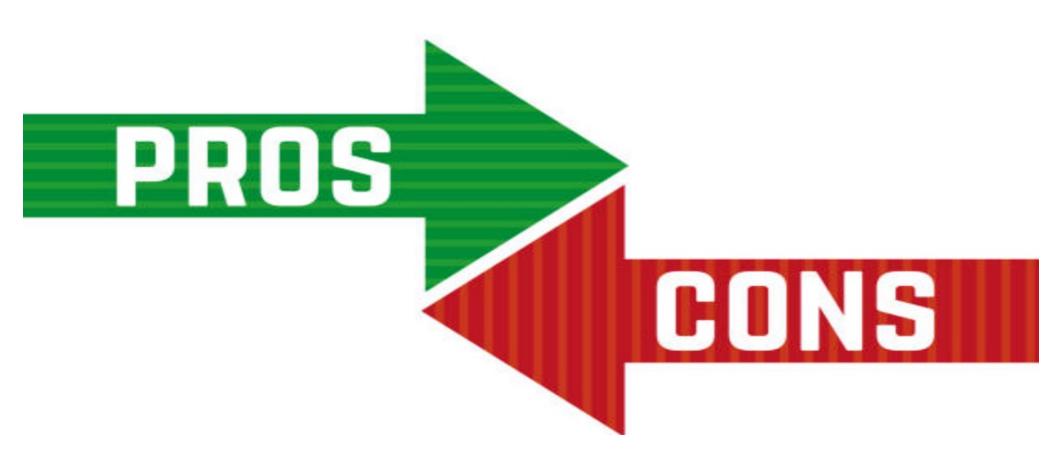# Strategies for Fixing the Social Security program

Options we considered Monday:

1. Cut benefits for retirees
2. Reducing the cost-of-living adjustment

Solution: Cut benefits for retirees

- **Ways to cut benefits for future retirees**
  - Use the highest 40 (rather than highest 35) years of income to set benefits (lower the AIME and result in lower PIA)
  - Adjust the "bend points" to force lower PIAs
- **But: Promises would have to be broken**
  - **Lower standard of living for seniors**
  - **Higher poverty level among seniors**
- **But: Political fallout?**

Solution: Reduce the cost-of-living adjustment

- Remember: **someone in 2023 gets higher _real_ benefits than someone who retired in 2000.** Why?
  - Benefits grew with nominal wage rates, and wages grew faster than inflation
  - COL increase over the past 20 years has been higher than inflation
- But: Reduced standard of living for retirees if inflation runs rampant

Solution: Increase payroll taxes

1. Raise the SS tax rate on earning above 6.2% (12.4%)
2. Raise the cap on SS taxable earnings

https://www.youtube.com/watch?v=_URf3WB_V78

Predicted impact of raising taxes

1. Impact on the economy
2. Disincentive to work in the economy

1.3 min

Very strong political opinions FOR raising taxes

1.3 min

SOCIAL SECURITY REFORM

fund will not be fully funded
by 2033,

MSNBC

Solution:
Increase payroll taxes

How?

Proposals

- Raise "earnings cap" to $300k on income subject to the 6.2% tax
- Eliminate the "earnings cap" on income subject to the 6.2% tax, making <u>All EARNED INCOME</u> subject to the tax
  - More money coming into the trust fund
  - Higher-income individuals "paying their fair share"

Is Bernie Sanders right?

Would eliminating the SS income cap completely solve the structural deficit in the SS program?

But, CBO analysis

- Raising the income cap to $300k would only solve about **34%** of the structural deficit

- Raising the income cap to $500k would only solve about **54%** of the structural deficit

- Eliminating the cap altogether would only solve **72%** of the structural deficit
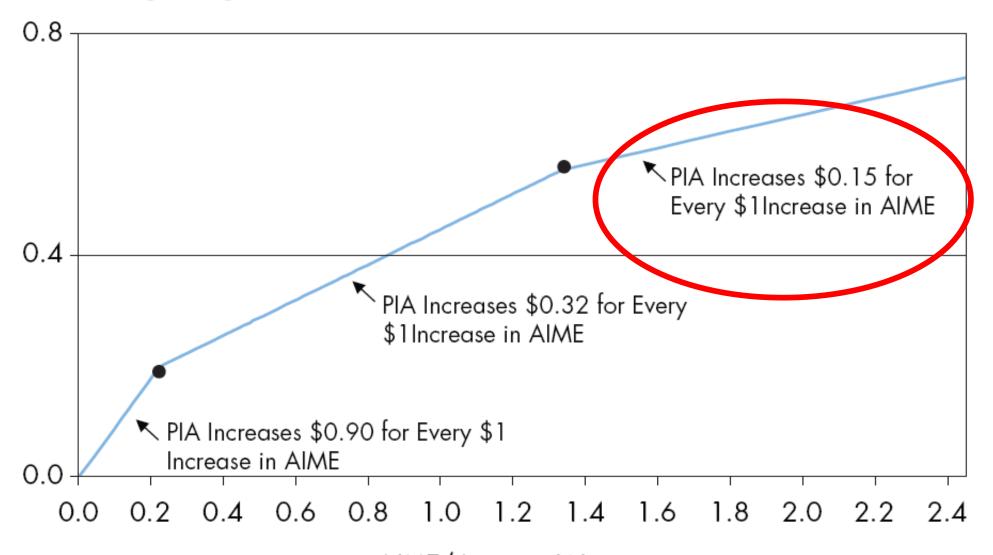
Conclusion: raising taxes alone **will not** solve the structural deficit

And, raising taxes, presents us with another problem = VERY large AIMEs

How would those additional taxes be credited into the PIA?

Figure 1: Current-Law Primary Insurance Amount Formula

https://www.ssa.gov/oact/cola/bendpoints.html

PIA/Average Wage

PIA Increases $0.15 for Every $1 Increase in AIME

PIA Increases $0.32 for Every $1 Increase in AIME

PIA Increases $0.90 for Every $1 Increase in AIME

AIME/Average Wage

AIME = Average Indexed Monthly Earnings

Source: Department of the Treasury

Credits for those additional taxes in the PIA

- How does one "credit" those earnings into the PIA formula?
  - 0.15 past the top bend point?
  - 0.03 past the top bend point?
  - 0% credit for those extra taxes?
- Is 0% <u>fair</u> to the higher earners?
- If positively credited at all, we would see <u>VERY high PIA</u> checks going to wealthy individuals

Credits for those additional taxes in the PIA

- If not credited at all?
  - How does that impact the SS financial principle of <mark>INDIVIDUAL EQUITY</mark>

How many people would be impacted by eliminating the earnings cap?

- Fact is that approximately **~81.4%** of all workers earn annual incomes BELOW the social security "earnings cap"
  - but tax was originally meant to apply to **90%** of earnings
  - Approximately 9% of earners would be impacted

- **Increase taxes?**
  - But: Political acceptability?
  - But: Impact on economic growth?

Solution:
Raise the normal retirement age

Solution: Raising the normal retirement age

- **Raise retirement age?**
  - "Normal Retirement Age" (NRA) **68**
  - "Early Retirement Age" (ERA) **62**
  - Let both increase over time:
    - *Motivation* = encourage longer work life and reduce length of time over which retirement benefits are paid

Raising Normal Retirement Age from 65/7 to 70: Effects on PIA

Year of retirement	62	65	66	67	70
Current benefits as a percentage of OIA	80	100	106	112	130
New benefits as a percentage of PIA	61.5	76.9	81.6	86.2	100
Percentage loss in benefits	23.1	23.1	23.1	23.1	23.1

9.27

Arguments for raising NRA:

- Government should not be encouraging people to retire earlier than needed given increasing *life expectancy*

Argument against raising the NRA:

- Some people have no choice about when to retire
  - **Physically demanding jobs** - cannot work longer
- Post-retirement **jobs** for elderly are scarce
- Unfair to people with **reduced life expectancy** (gender, race, health status)
- AND - could have zero-sum savings (*offsetting effect*) if early retirees apply for other federal programs like **SSDI** to support themselves during the time from retirement to eligibility for SS

Effectiveness of Raising the NRA

- Will they work?:
  - The Social Security actuaries estimate that increasing the full retirement age to **69** for those turning 62 in 2023 or later would eliminate **only 29** percent of the 75-year funding gap.
- *Conclusion?*
  - Just raising the retirement age will not be sufficient to close the Social Security structural deficit

Strategy:
Universal FLAT benefit for Retirees

- All retirees <u>pay into</u> the system
- All retirees get <u>the same flat</u> benefit
- This benefit would be enough to keep income <u>above the poverty line</u>

THE PERFECT SOLUTION TO FIX SOCIAL SECURITY

https://www.youtube.com/watch?v=WulsqjB7Rdc
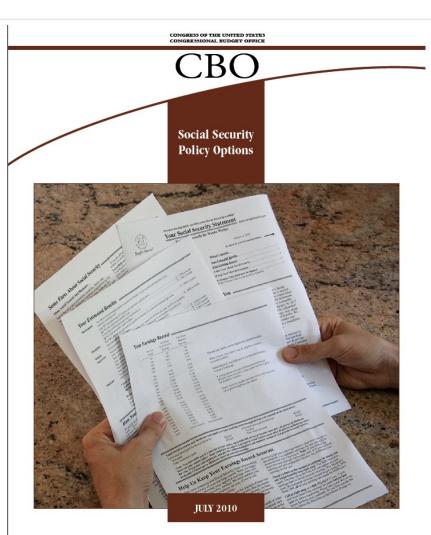
What strategies can we piece together to save Social Security for Future Generations?

Congressional Budget Office

Federal agency

CBO

**Social Security
Policy Options**

JULY 2010

So, what does the CBO say will work to fix the Social Security Program?

Which of these proposals would solve the Social Security structural deficit?
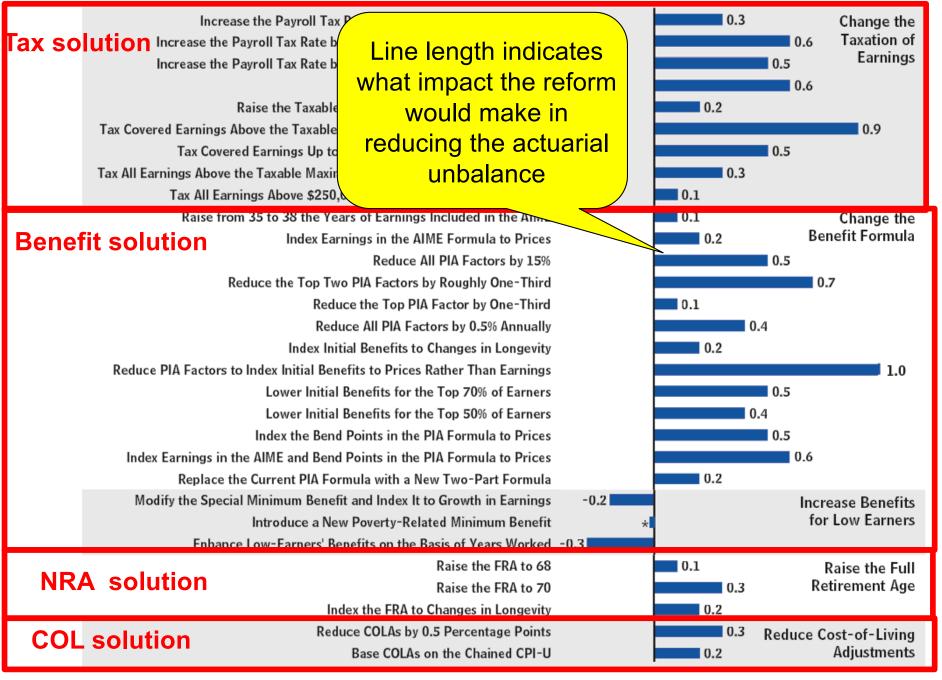
CBO Analysis of reform options

- Tax solutions
- Benefit solutions
- Cost of living adjustment solutions
- Retirement age eligibility solutions

Graphic representation of reform solution impact

Summary Figure 1.

Effects of the Policy Options on the OASDI Trust Fund Actuarial Balance

Tax solution

Option	Value	Category
Increase the Payroll Tax R...	0.3	Change the Taxation of Earnings
Increase the Payroll Tax Rate b...	0.6	
Increase the Payroll Tax Rate b...	0.5	
	0.6	
Raise the Taxable...	0.2	
Tax Covered Earnings Above the Taxable...	0.9	
Tax Covered Earnings Up to...	0.5	
Tax All Earnings Above the Taxable Maxi...	0.3	
Tax All Earnings Above $250,...	0.1	

Benefit solution

| Option	Value	Category
Raise from 35 to 38 the Years of Earnings Included in the AI...	0.1	Change the Benefit Formula
Index Earnings in the AIME Formula to Prices	0.2	
Reduce All PIA Factors by 15%	0.5	
Reduce the Top Two PIA Factors by Roughly One-Third	0.7	
Reduce the Top PIA Factor by One-Third	0.1	
Reduce All PIA Factors by 0.5% Annually	0.4	
Index Initial Benefits to Changes in Longevity	0.2	
Reduce PIA Factors to Index Initial Benefits to Prices Rather Than Earnings	1.0	
Lower Initial Benefits for the Top 70% of Earners	0.5	
Lower Initial Benefits for the Top 50% of Earners	0.4	
Index the Bend Points in the PIA Formula to Prices	0.5	
Index Earnings in the AIME and Bend Points in the PIA Formula to Prices	0.6	
Replace the Current PIA Formula with a New Two-Part Formula	0.2	
Modify the Special Minimum Benefit and Index It to Growth in Earnings	-0.2	Increase Benefits for Low Earners
Introduce a New Poverty-Related Minimum Benefit	*	
Enhance Low-Earners' Benefits on the Basis of Years Worked	-0.3	

NRA solution

Option	Value	Category
Raise the FRA to 68	0.1	Raise the Full Retirement Age
Raise the FRA to 70	0.3	
Index the FRA to Changes in Longevity	0.2	

COL solution

Option	Value	Category
Reduce COLAs by 0.5 Percentage Points	0.3	Reduce Cost-of-Living Adjustments
Base COLAs on the Chained CPI-U	0.2	

> Line length indicates what impact the reform would make in reducing the actuarial unbalance

Source: Congressional Budget Office.

What combinations of decisions will close that 75-year actuarial gap?

Let's see what you think…….

Social Security Game

- http://socialsecuritygame.actuary.org/
- Choose the ==SMALLEST== combination of solutions that would solve the long-term social security structural deficit.
- Paying particular attention to the **political viability** of the solution

THE SOCIAL SECURITY GAME

Revenue Increases

Raise Payroll Tax Rate

Subject Higher Wages to Social Security Payroll Tax

Subject Benefits to Higher Taxes

Apply Payroll Tax to Health Care Premiums

THE SOCIAL SECURITY GAME

Benefit Reductions

Gradually Increase Full Retirement Age

Reduce Cost-of-Living Adjustments (COLA)

Reduce Benefits for Future Retirees

Lower Benefits for future High-Income Retirees

THE SOCIAL SECURITY GAME

Put your own set of <mark>SMALL</mark> solutions together to solve the actuarial balance problem, remembering the **political feasibility** of the solutions you suggest.

Optional ASSIGNMENT

- Maximum one typed page
- Identify specific set of solutions that solves the 75-year structural deficit
- One paragraph commenting on the political feasibility of the solution you propose