Summary of Policy Options for the Lunchtime Exercise

National Academy of Social Insurance
Summer Intern Academy:
Demystifying Social Insurance

Office of the Chief Actuary
Social Security Administration
July 18, 2024

Our team today

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Agenda

- Introduction
- Options to increase revenue for solvency
- Options to reduce benefits for solvency
- Options to increase benefits for adequacy
- Putting it all together

Role of the Office of the Chief Actuary

- Evaluate financial status of Social Security (OASDI) and future cost of Supplemental Security Income (SSI)
- Project future population, workforce, employment, tax revenue, benefits, and (for OASDI) the status of trust funds
- Projections for the President’s FY Budget and Mid-Session Review
- Projections for Annual OASDI Trustees Report
- Projections for Annual SSI Report
- ***Estimate effects of all changes considered for law and regulations by the Administration and Congress***

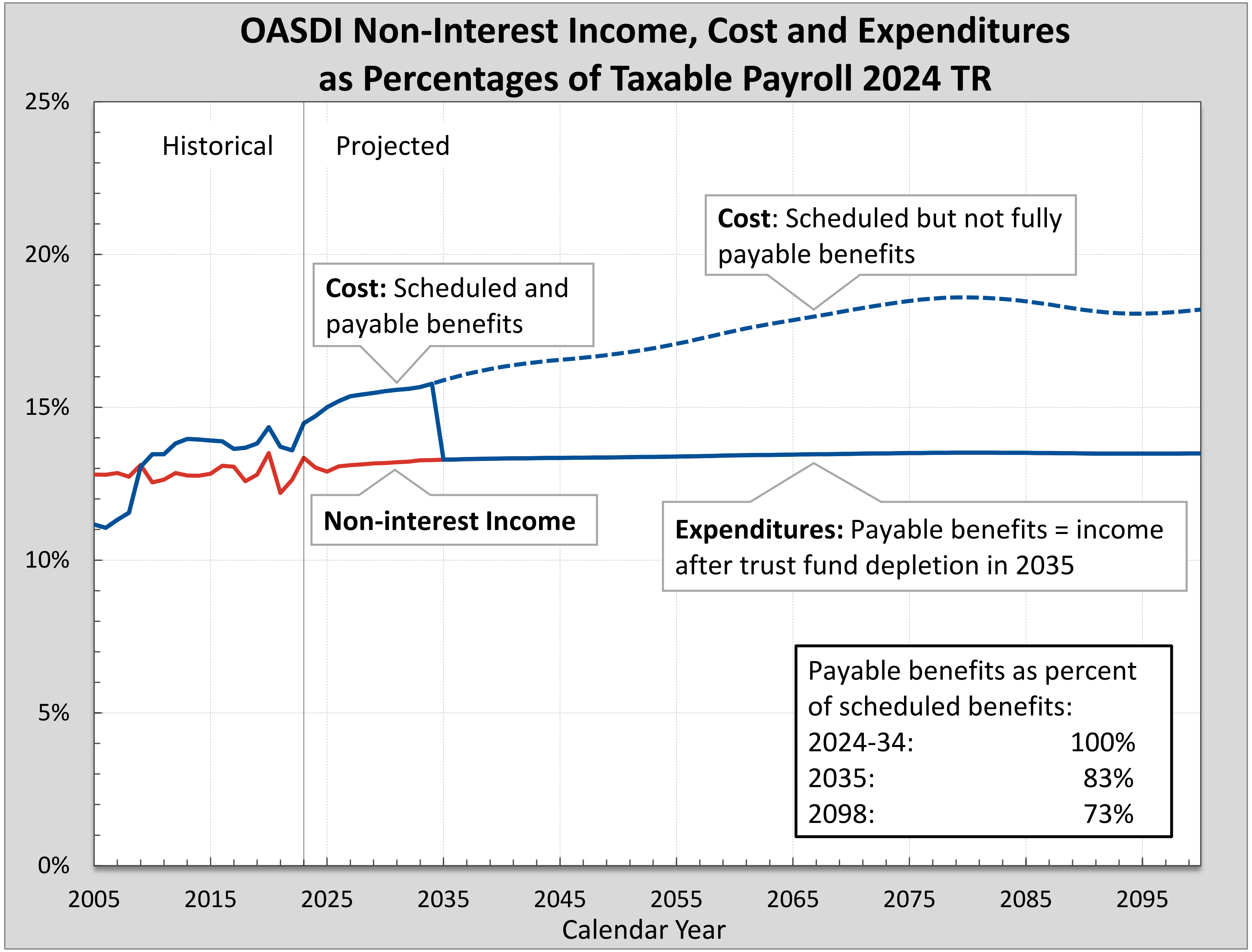
OASDI Annual Cost and Non-Interest Income as Percent of Taxable Payroll

Program cost rose above tax income by 2010 and is still rising

Trust fund reserves will be depleted by about 2035

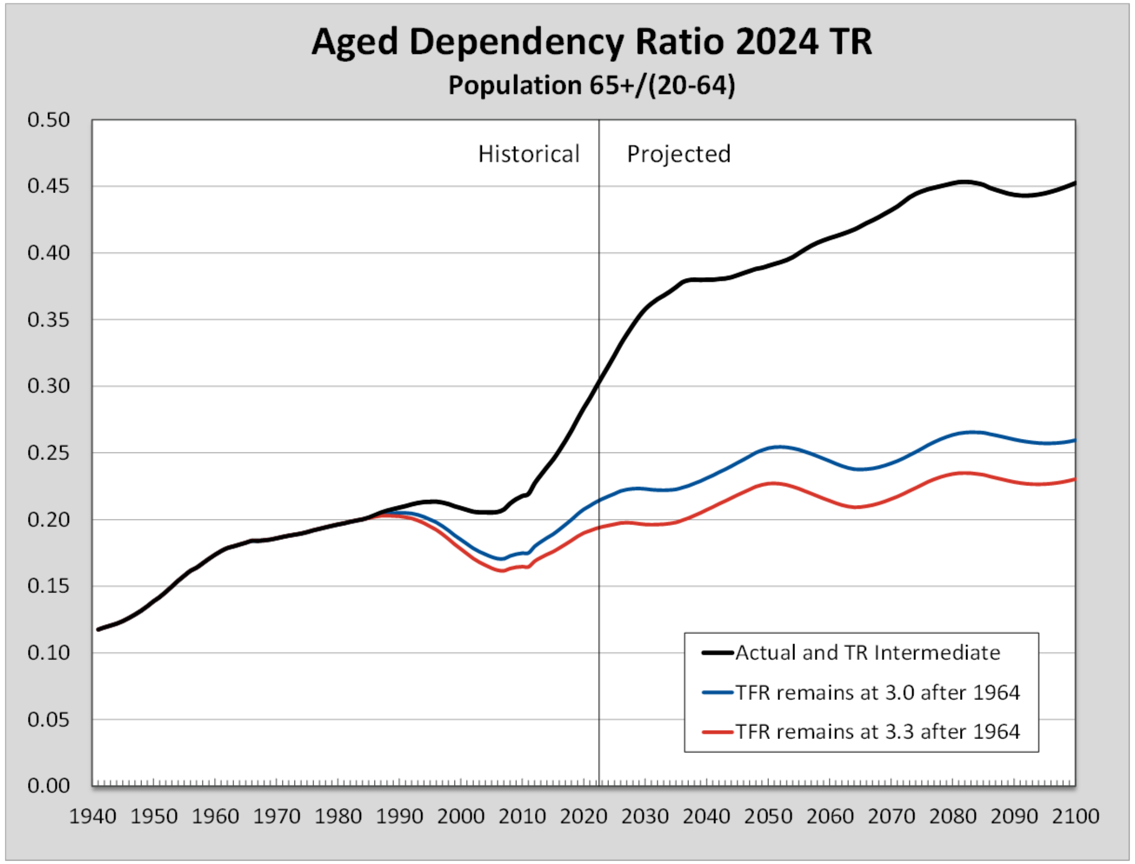
But 83 percent of scheduled benefits are still payable at trust fund reserve depletion

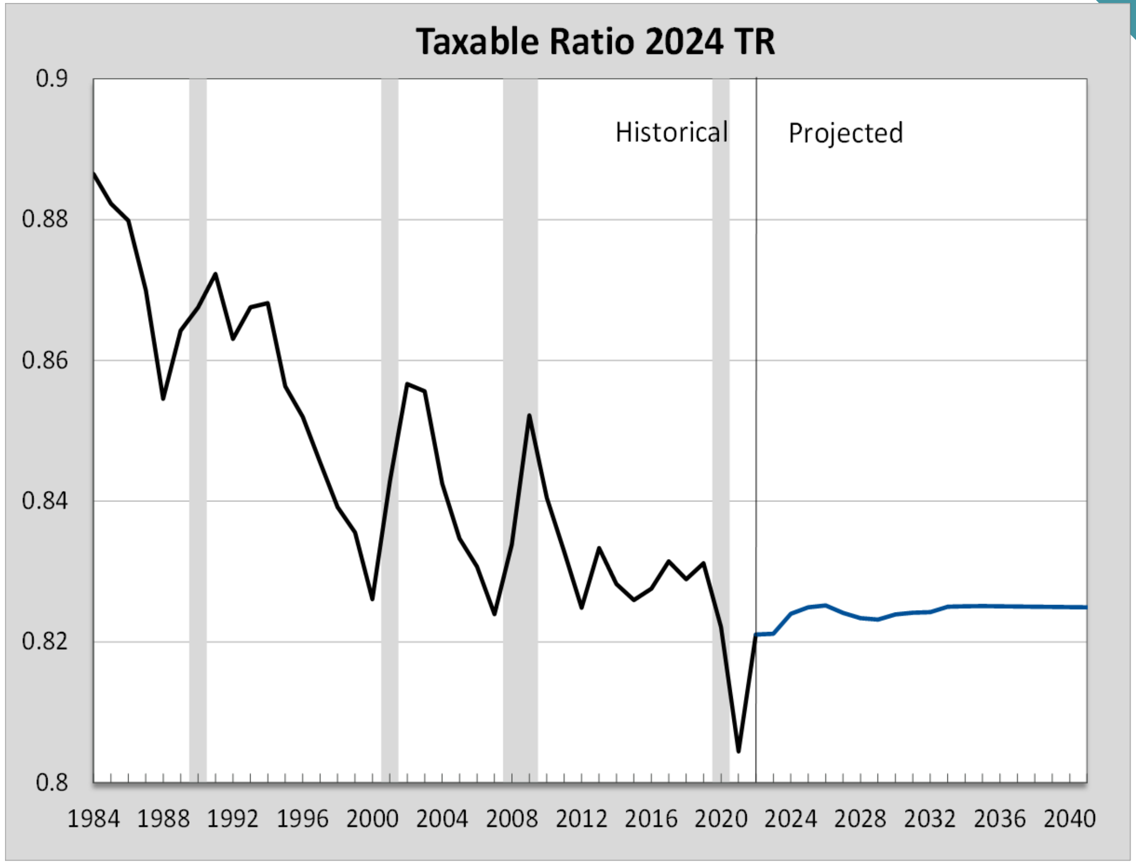
73 percent payable by 2098



Why the Shortfall?

(1) Expected change in age distribution due to lower birth rates
(2) Unexpected drop in share of earnings that are taxable





How to Eliminate Social Security's Long-Term Actuarial Deficit

- Make choices addressing OASDI shortfall 2035-2098:
  - Raise scheduled revenue by 2035 by about one-third
  - Reduce scheduled benefits by 2035 by about one-fourth
  - Or some combination of the two
- This is your job today!

Payroll Tax Contribution Rates for the OASDI Programs

- Employees in covered employment, and their employers, each pay 6.2 percent of the employee’s taxable earnings (12.4 percent is the combined rate)
- Self-employed individuals pay the full 12.4 percent
- Could simply increase these tax rates: *see Policy Options 2a and 2b in the handout*

Contribution and Benefit Base

- This is an annual dollar amount above which earnings in employment covered under the OASDI program are neither taxable nor creditable for benefit computation purposes; sometimes called “the taxable earnings cap”
- $168,600 for calendar year 2024—this means:
  - $10,453.20 is the maximum Social Security tax a person in covered employment, and their employer, will pay in 2024
  - The maximum amount of earnings for 2024 that can be used in the Social Security benefit calculation is $168,600
- This is an *average-wage-indexed* amount

Contribution and Benefit Base Proposals

- Could eliminate the "cap" completely, and either
  - Count the additional earnings toward benefits …
  - … or not!
- Raise the "cap" so that it reaches a certain taxable ratio by a certain year
  - For example, raise the contribution and benefit base until 90% of all covered earnings are taxable
  - As a reference, a base of roughly $350,000 would mean that 90% of covered earnings are taxable in 2024
- *See Policy Options 1a and 1b in the handout*

Social Security Retirement Age

- At full retirement age, also called “normal retirement age” or NRA, the full basic Social Security benefit is paid (Primary Insurance Amount or PIA):
- For individuals age 62 in 2024, the NRA is 67
  - Can file to start retirement benefits as early as 62 in 2024 with a 30% reduction of the “full” benefit (PIA); age 62 is called the earliest eligibility age or EEA
  - Can file to start retirement benefits at age 70 or later with a 24% benefit increase, 8% per year of delay in starting benefits
  - Those benefit reductions/increases are permanent, with annual cost of living adjustments

Implications of Raising NRA

- Raising the NRA:
  - If no change in an individual's age at retirement, then monthly benefits are reduced
  - Would have to delay start of benefits by the amount of the increase in the NRA to get the same monthly benefit
  - Would extend/increase payments made by Disability Insurance Trust Fund, and would lead to additional applications for (unreduced) disability benefits

Implications of Raising NRA (continued)

- Workers (in general) are living longer, healthier lives
  - Many workers are able to remain longer in the workforce
  - Workers will need more time to save for a longer retirement
- Possible difficulties
  - Will workers want to remain longer in the labor force?
  - Will more jobs be available for older workers?
  - Will older workers in strenuous jobs be adversely affected—not quite meeting disability status per Social Security standards?
- *See Policy Options 3a and 3b in the handout*

Benefit Indexing

- The amount of a worker’s monthly Social Security benefit is based on the worker’s lifetime earnings, which are averaged and wage indexed
- Each year’s earnings are adjusted upward to keep pace with changes in the average wage level
- Thus reflecting improvements in productivity and the general standard of living (more than just price increases) during the individual’s working years

Adjusting Benefit Indexing for Higher Earners

- One option is to reduce growth in benefits for higher earners (in generations in the future) to rise by less than the average wage increase provided in current law
- Because prices generally rise more slowly than wages, price indexing would result in lower retirement benefits
- Benefits for relatively higher earners in the future would be indexed from one generation to the next by something between wage and price increases, and benefits for individuals with lifetime taxable earnings at or above the contribution and benefit base ($168,600) would be indexed to prices alone
- This is sometimes called ***progressive price indexing***
- *See Policy Options 4a and 4b in the handout*

Cost-of-Living Adjustments

- Since 1975, Social Security's general benefit increases have been based on increases in the prices of goods and services experienced by urban wage and salary workers, as measured by the Consumer Price Index (CPI)
- These cost-of-living adjustments, or COLAs, are effective for December benefits, payable in January
- Benefits keep pace with inflation

Chain-Weighted CPI (C-CPI-U)

- Based on idea that consumers will tend to shift consumption toward categories of goods and services with smaller price increases, even though the categories are not substitutes for each other ("higher-level redistribution")
- Lower-level vs. higher-level redistribution
- By age 85, benefits would be about 6.5% lower
- OCACT estimates C-CPI-U would reduce the annual COLA by 0.3 percentage point, on average
- *See Policy Option 5a in the handout*

CPI for the Elderly (CPI-E)

- Basket of goods and services for those age 62+
- Certain expenditure groups, such as medical care and housing, are given greater weight
- By age 85, benefits would be about 4.6% higher
- OCACT estimates CPI-E would increase the annual COLA by 0.2 percentage point, on average
- *See Policy Option 5b in the handout*

Special Minimum Benefit

- The special minimum benefit is a special minimum primary insurance amount (PIA) enacted in 1972 to provide adequate benefits to long-term low earners. The first full special minimum PIA in 1973 was $170 per month. Beginning in 1979, its value has increased with price growth and is about $1,067 per month in 2024 for a worker with 30 years of coverage.
- Virtually no one is receiving this benefit today, because benefit levels are designed to increase with average wages (not prices) across generations

Increase the Special Minimum Benefit

- One option is to increase Social Security's special minimum benefit to pay 125% of the poverty level for 2024 at full retirement age for someone who has worked 30 years or more.
- The poverty level is currently $15,060 a year for one person, so the new full special minimum PIA would be about $1,569, almost 50% higher than under current law
- The initial special minimum PIA level would be wage-indexed across generations going forward
- Targets benefit increases for lower wage workers
- *See Policy Option 6 in the handout*

Extend Student Benefits

- Extend student benefits until age 22 for children of deceased or disabled workers if the child is a full-time student in college or vocational school
- Currently, a “student beneficiary” refers to an 18-year-old child of a retired, disabled, or deceased worker who is enrolled in secondary school or below
- From 1965 through 1981, these benefits continued until age 22 if the child was a full-time student in college or vocational school
- *See Policy Option 7 in the handout*

Increase All Benefits

- One option is to increase the monthly benefit amount for all beneficiaries now and in the future by 5% of the average Social Security benefit
  - 5% of the average benefit would be about $94 a month in 2024
  - Same dollar increase for all beneficiaries, which would increase in the future by about the increase in average wage
- *See Policy Option 8 in the handout*

Increase Benefits for Older Beneficiaries

- Another option is to increase the monthly benefit amount for all beneficiaries aged 85 and older now and in the future by 5% of the average retired worker benefit
    - 5% of the average retired worker benefit would be about $96 a month in 2024
    - Same dollar increase for all beneficiaries 85+, which would increase in the future by about the increase in average wage
    - Older ages targeted due to higher risk of inadequate benefit levels
    - Further insurance against longevity
- *See Policy Option 9 in the handout*

Caregiver Credits

- Provide Social Security earnings credits for up to 5 years to parents with young children under 6 years of age
  - The amount of the earnings credit would be up to one-half of the Social Security Average Wage ($31,898 in 2022)—that is, “topping up” earnings to that level if less
  - Under current law, retired worker benefits are calculated using highest 35 years of earnings
  - Would replace as many as the 5 lowest earning years in which the worker has a child under age 6
- *See Policy Option 10 in the handout*

Putting it all together…

- Each table has 30 minutes to come up with a package of options that will eliminate (or at least narrow) Social Security's long-term financing gap
- Review the handouts, and discuss pros and cons at your table
- Assume the percent effects are additive (although this is not strictly true!)
- We will be serving as table experts and are here to help
- Be prepared to present your solutions to the whole group—we will call on tables to briefly share your ideas and rationales

Example

Option No.	Description	Percent of financing gap closed
1b	Taxable Earnings Cap – completely eliminate	57%
3a	Retirement Age – gradually raise from 67 to 68	15%
4a	Benefit Indexing – reduce benefit calculation for those with earnings above the 30th percentile	44%
5b	COLA – increase the COLA by using the CPI-E	-12%
	TOTAL:	**104%**

Good luck!

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SUMMARY OF POLICY OPTIONS

Option No.	Description	Percent of financing gap closed	Page # for details
Options to increase revenues for solvency (Remember: *positive* numbers *reduce* the financing gap)			
1a	**Taxable Earnings Cap**: Lift the taxable earnings cap ($168,600 in 2024) over a 10-year period until 90% of all covered earnings are taxable in 2033. (For reference, a cap of about $350,000 would mean that 90% of earnings are taxable in 2024.) Credit additional earnings to benefits.	19%	Page 2
1b	**Taxable Earnings Cap**: Completely eliminate the taxable earnings cap ($168,600 in 2024) over 10 years, and credit those additional earnings toward benefits.	57%	
2a	**Tax Rate** (currently 6.2%): Raise the tax rate for workers and employers to 8.1% in 2024.	102%	
2b	**Tax Rate** (currently 6.2%): Over 20 years starting in 2029, raise the tax rate by 0.05 percentage points per year for workers and employers each. By 2048, the tax rate would be 7.2% for workers and employers each.	41%	
Combinations of revenue options: Certain combinations of individual options produce interaction effects, meaning their combined impact is more than the sum of the two changes individually.			Page 3
	1a and 2a	127%	
	1a and 2b	63%	
	1b and 2a	176%	
	1b and 2b	106%	
Options to reduce benefits for solvency (Remember: *positive* numbers *reduce* the financing gap)			
3a	**Retirement Age**: Gradually raise the full retirement age from 67 to 68.	15%	Pages 4-5
3b	**Retirement Age**: Gradually raise the full retirement age from 67 to 70.	25%	
4a	**Benefit Indexing**: Reduce benefits for higher lifetime earners by changing the benefit calculation formula so that individuals with earnings above the 30th percentile of earnings (currently about $35,000) would receive benefits further reduced in proportion to their lifetime earnings than workers with earnings at and below the 30th percentile.	44%	
4b	**Benefit Indexing**: Reduce benefits for higher lifetime earners by changing the benefit calculation formula so that individuals with earnings above the 60th percentile of earnings (currently about $68,000) would receive benefits further reduced in proportion to their lifetime earnings than workers with earnings at and below the 60th percentile.	23%	
5a	**Cost-of-Living Adjustment** (COLA): Lower the COLA by basing it on the chain-weighted Consumer Price Index (C-CPI-U), which reflects the economy-wide tendency to shift consumption toward categories of goods and services with smaller price increases.	17%	
Options to increase benefits for adequacy (Remember: *negative* numbers *increase* the financing gap)			
5b	**Cost-of-Living Adjustment** (COLA): Increase the COLA by basing it on the CPI-E, which specifically measures the inflation experienced by consumers over age 62.	-12%	Pages 6-7
6	**Benefits for Lifetime Low-Wage Workers**: Increase Social Security's special minimum benefit to pay 125% of the poverty level at full retirement age for someone who has worked 30 years or more. Index the initial special minimum benefit level by average wages across generations.	-5%	
7	**Children's Benefits for Students**: Reinstate student benefits until age 22 for children of deceased or disabled workers if the child is a full-time student in college or vocational school.	-1%	
8	**Benefits for All Beneficiaries**: Increase monthly benefits for all beneficiaries.	-22%	
9	**Benefits for Beneficiaries Aged 85+**: Increase monthly benefits beginning at age 85.	-4%	
10	**Caregiver Credits**: Provide Social Security earnings credits to parents with young children for up to 5 years.	-6%	

Options to Increase Revenues for Solvency

1. Social Security's Taxable Earnings Cap: Currently, annual earnings above $168,600 are not taxed for Social Security or counted toward benefits. About 6% of workers earn more than that amount. In the early 1980s, Social Security taxed about 90% of all covered earnings by American workers. Currently, the cap means that only about 82.5% of covered earnings are taxed, because earnings at the top of the earnings distribution have increased more than wages in the middle and bottom of the distribution.

Option 1a: Lift the taxable earnings cap (which is $168,600 in 2024) over a 10-year period until in 2033, 90% of all covered earnings are once again taxable. (For a point of reference, a cap of about $350,000 would mean that 90% of covered earnings are taxable in 2024.) Provide benefit credit for earnings up to the revised taxable maximum.

- The top 6% of earners would pay somewhat more into Social Security, receiving somewhat higher benefits in return.
- This change alone **reduces** the financing gap by <u>19%</u>.

Option 1b: Phase-in the complete elimination of the taxable earnings cap over 10 years and credit those additional earnings toward benefits at a lower rate.

- The top 6% of earners would pay Social Security taxes on all of their earnings all year, just as other workers do.
- In return, they would get somewhat higher benefits. These top earnings would count toward benefits at a lower rate. This would preserve the link between earnings and benefits, yet avoid the need to pay very high Social Security benefits even when all earnings are subject to Social Security taxes.
- This change alone **reduces** the financing gap by <u>57%</u>.

2. Social Security Tax Rate: Currently, workers pay 6.2% of earnings up to the earnings cap, which is $168,600 in 2024. Employers match that amount. Earnings above the cap are not taxed or credited toward benefits.

Option 2a: Raise the tax rate for workers and employers – from 6.2% to 8.1% in 2024.

- For a worker earning $50,000, the change would mean an increase of $18.27 per week, matched by the employer.
- This change alone **reduces** the financing gap by <u>102%</u>.

Option 2b: Over 20 years starting in 2029, raise the tax rate by .05 percentage points (5 cents per $100 of earnings) per year for workers and employers each. By 2048, the tax rate would be 7.2% for workers and employers each.

- For a worker earning $50,000, this would mean an increase each year of 50 cents per week, matched by the employer. The ultimate increase would be $9.62 a week for a worker making this much.
- This change alone **reduces** the financing gap by <u>41%</u>.

See next page for combinations of options 1 and 2.

Combinations of Revenue Options: Certain combinations of the individual options produce interaction effects, meaning that if the two options were implemented together, then their total effects would be different from the sum of the two changes individually. The following list of combinations provides a rough estimate of the interaction among the revenue options listed above, which affect the tax rate and tax base. For example, consider a tax rate increase in combination with broadening the tax base: Option 1b (phasing out the taxable earnings cap entirely) and Option 2b (gradually raising the tax rate) combined are estimated to close 106% of the financing gap – more than the sum of the two changes individually, which is 98%.

Combination	Percent of shortfall closed
Options (1a) and (2a)	127%
Options (1a) and (2b)	63%
Options (1b) and (2a)	176%
Options (1b) and (2b)	106%

Options to Reduce Benefits for Solvency

3. Social Security's Full Retirement Age: Currently, Social Security's full retirement age is 67 for workers born in 1960 and later. Workers may start collecting Social Security benefits before their full retirement age, starting at age 62, but benefits are reduced. Increasing the full retirement age is an across-the-board benefit cut at any age a worker takes benefits.

Option 3a: Gradually raise the full retirement age from 67 to 68.

- Starting in 2024, increase the full retirement age by 2 months each year until it reaches 68 in 2029.
- This change alone **reduces** the financing gap by 15%.

Option 3b: Very gradually raise the retirement age from 67 to 70.

- Starting in 2024, increase the full retirement age by just less than a month each year until the full retirement age reaches 70 in 2070.
- This change alone **reduces** the financing gap by about 25%.

4. Benefit Indexing: The amount of a worker's monthly Social Security benefit in retirement is determined by a number of factors, including the worker's lifetime earnings, which are averaged and wage indexed — that is, adjusted upward to keep pace with current wage levels and thus reflecting improvements in productivity and the general standard of living during the individual's working years. Benefits for all retirees have been wage-indexed since 1978 under a formula that pays comparatively higher benefits to lower-paid earners. One option is to further reduce benefits for higher earners by indexing part of their earnings to prices rather than wages. Because prices generally rise more slowly than wages, price indexing would result in lower retirement benefits as a share of prior earnings. Benefits for relatively higher earners would be indexed to a combination of wage and price increases, and benefits for individuals with lifetime earnings above the taxable maximum ($168,600) would be indexed to prices alone. This is sometimes called *progressive price indexing*.

Option 4a: Change Social Security's retirement benefit formula so that benefits for earners above the 30th percentile of wage earners (about $35,000 in annual earnings) would be reduced by being based on a combination of wage and price increases.

- Benefits for individuals whose earnings have been at or above Social Security's taxable maximum (currently $168,600) throughout their careers would be based on price increases alone.
- Benefits for workers whose earnings have been at or below the 30th percentile of earnings (about $35,000) throughout their careers would be based on wage increases alone.
- Effective for those newly eligible in 2030 and after
- This change alone **reduces** Social Security's financing gap by 44%.

Option 4b: Change Social Security's retirement benefit formula so that benefits for earners above the 60th percentile of wage earners (about $68,000 in annual earnings) would be reduced by being based on a combination of wage and price increases.

- Benefits for individuals whose earnings have been at or above Social Security's taxable maximum (currently $168,600) throughout their careers would be based on price increases alone.
- Benefits for workers whose earnings have been at or below the 60th percentile of earnings (about $68,000) throughout their careers would be based on wage increases alone.
- Effective for those newly eligible in 2030 and after
- This change alone **reduces** Social Security's financing gap by 23%.

5. Social Security's Cost-of-Living Adjustment (COLA): The purpose of Social Security's COLA is to maintain the purchasing power of benefits already awarded to retirees. The Social Security Administration adjusts the COLA when the cost of living increases.

Option 5a: Lower the COLA by basing it on the chain-weighted Consumer Price Index (C-CPI-U), which may more accurately reflect the economy-wide tendency to shift consumption toward categories of goods and services with smaller price increases, but not specifically the inflation experienced by seniors.

- The chain-weighted CPI takes into account substitutions across categories of goods and services (for instance, if the price of one category rises, households might buy something from another category instead instead). Some economists consider this measure to be more accurate, but others point out that seniors and low-income households have less flexibility to substitute spending. In addition, older households spend a greater share of their income on goods and services that typically have higher rates of inflation, such as medical care and housing.
- If average inflation from one year to the next is 3% under the current measure, but the chain-weighted CPI shows inflation was only 2.7%, using a COLA measure based on the C-CPI-U would increase a $1,000 monthly benefit by $27 instead of $30.
- Benefit cuts would add up over time, so the oldest seniors would experience the largest cuts. By age 85, benefits would be about 6.5% lower than they would otherwise be.
- This change alone **reduces** the financing gap by 17%.

Options to Increase Benefits for Adequacy

5. Social Security's Cost-of-Living Adjustment (COLA): The purpose of Social Security's COLA is to maintain the purchasing power of benefits already awarded to retirees. The Social Security Administration adjusts the COLA when the cost of living increases.

Option 5b: Increase the COLA by basing it on the Consumer Price Index-E (CPI-E), which specifically measures the inflation experienced by consumers over age 62.

- Those over age 62 spend a greater share of their income on medical and housing costs, which rise faster than inflation in general.
- If average inflation from one year to the next is 3%, but inflation experienced by seniors is 3.2%, using a COLA measure based on the CPI-E would increase a $1,000 monthly benefit by $32 instead of $30.
- By age 85, benefits would be about 4.6% higher than they would otherwise be.
- This change alone **increases** the financing gap by 12%.

6. Benefits for Lifetime Low-Wage Workers: Currently, people who work all their lives at low wages are at risk of living in poverty in retirement, even after paying Social Security taxes during all the years they worked. Increasing Social Security's *Special Minimum Benefit* would ensure that anyone who worked and paid Social Security taxes for 30 years or more can retire at age 62 or later and not live in poverty.

Option 6: Increase Social Security's special minimum benefit to pay 125% of the poverty level at full retirement age for someone who has worked 30 years or more. (The poverty level is currently about $15,060 a year for one person.) The initial special minimum benefit level would be increased by the average wage index (AWI) going forward.

- This means that someone who worked and paid Social Security taxes for 30 years or more can retire at age 62 or later and not be in poverty.
- This change does not affect most workers, whose benefits exceed this minimum adequacy level.
- Indexing to AWI means that the value of the special minimum benefit does not "fade away" across generations.
- This change alone **increases** the financing gap by 5%.

7. Children's Benefits for Students: Currently, children whose working parents have died or become disabled receive Social Security benefits until age 19. In the past, these benefits continued until age 22 if the child was a full-time student in college or vocational school; Congress ended these "student benefits" in 1981.

Option 7: Reinstate student benefits until age 22 for children of deceased or disabled workers if the child is a full-time student in college or vocational school.

- This would make higher education more affordable for young people in families that have lost a breadwinner's income.
- This change alone **increases** the financing gap by 1%.

8. Benefits for All Beneficiaries: The average Social Security benefit for all beneficiaries of Social Security's Old Age and Survivors protections is about $1,870 a month, or $22,440 per year.

Option 8: Increase monthly Social Security benefits for all beneficiaries.

- The increase would be a uniform dollar amount for all beneficiaries, set at 5% of the average Social Security benefit (or about $94 per month in 2024).
- This change alone **increases** the financing gap by 22%.

9. Benefits for Beneficiaries Aged 85+: Americans over 85 years old tend to depend more heavily on Social Security, as in general their capacity to work is diminished and their savings and other assets have become depleted. The average retirement benefit in May 2024 was $1,917 per month, or about $23,000 per year.

Option 9: Increase monthly Social Security benefits for all beneficiaries age 85 and older.

- The increase would be a uniform dollar amount for all beneficiaries aged 85 and older, set at 5% of the average retired worker benefit (or $96 per month in 2024).
- This change alone **increases** the financing gap by 4%.

10. Caregiver Credits: Many working parents, especially women, take time out of the workforce during their careers to care for young children. That gap in paid work affects the parents' future Social Security benefits by lowering their career-average earnings.

Option 10: Provide Social Security earnings credits for up to 5 years to parents with young children under 6 years of age.

- The amount of the earnings credit would be up to half of the Social Security average wage ($31,898 in 2022). If the parent earned less than that amount, Social Security wage credits would be increased up to that level.
- Children must be younger than age 6.
- This change alone **increases** the financing gap by 6%.

SOCIAL SECURITY'S FINANCING GAP: YOUR SOLUTION

Option No.	Description	Percent of financing gap closed
	TOTAL:	