

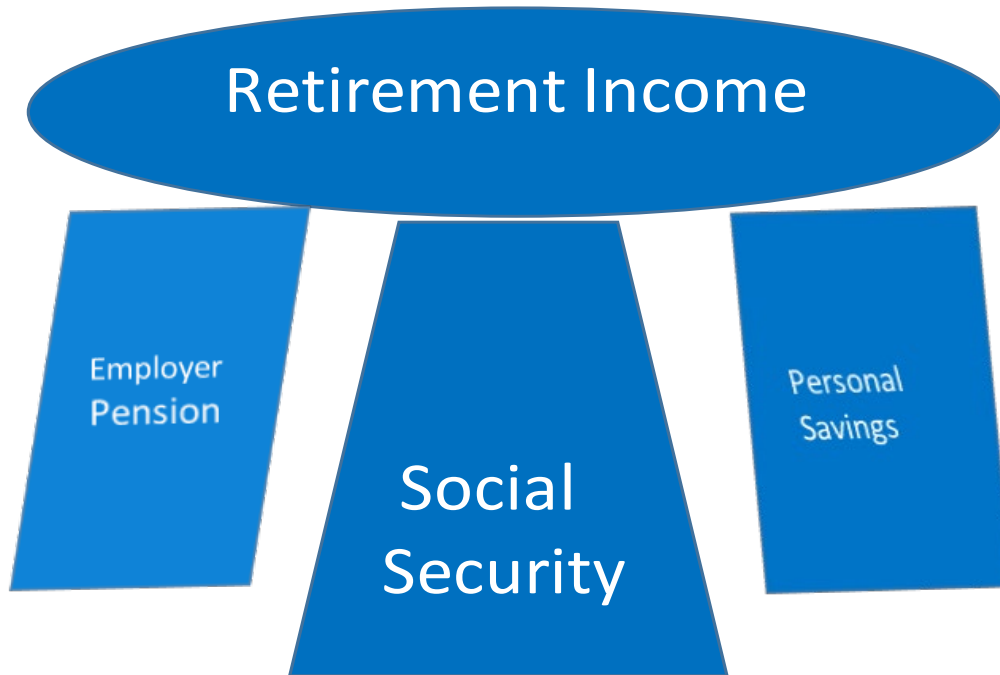
# **Social Security Financing and Benefits: Myths vs Facts**

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# Three Legged Stool: Basis for Retirement Planning

Common wisdom—aim for 75-80 percent replacement rate



# First, A Few Facts...

# Social Security: What Does It Provide?

- Retirement and survivor monthly benefits started in 1940
  - *Never missed a payment!*
- Eligibility age lowered from 65 to 62 in 1957 for women, 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 just CPI after eligibility*
- Payroll taxes roughly pay-as-you go
  - Rose from 2% to 12.4% as the system matured

# Social Security: Who Pays, Who Benefits

## WHO PAYS?

- 95% of workers contribute: 177 million in 2019 (2020 TBD)
  - 12.4% of earnings up to \$142,800 (6 percent of workers earn more)
  - 25% of State and local Govt employees are not in Social Security

## WHO BENEFITS?

- 65 million retirement, survivor, disability beneficiaries Dec 2020
  - 49 million retirees and their spouses and children dependent beneficiaries
  - Plus 6 million survivors
  - Plus over 10 million disabled workers and their dependents
- And 156 million workers are insured against disability or death

# Eligibility for Social Security is “Earned”

## Getting Insured

- Earn quarters of coverage (QCs)
  - \$1,470 earnings for a QC in 2021, maximum 4 earned in a year
  - “Fully Insured” = earned 1 QC for each year since 22, minimum 6
- For Retirement, Fully Insured, meaning 40 QCs generally
- For Disability, Fully Insured, plus “recent attachment”
  - earn 20 QC in last 5 years, or half the QCs since 22, minimum 6
- For Survivors, worker “fully insured” or “currently insured”
  - Earned 6 QCs of last 13 quarters

# How much is the Social Security Benefit?

## **First: Compute average indexed monthly earnings (AIME)**

- Computation years—35 for retirees, less for disabled under 62
- Average highest years of wage indexed earnings
  - Include zeros of necessary
  - Wage index up to 2 years before eligibility, i.e., 60 for retiree

## **Second: Primary Insurance Amount (PIA) 2021 eligibility**

- 90% of AIME up to \$996, then 32% to \$6,002, then 15%
- There is no maximum PIA, and now no special minimum

## **Third: % of PIA by benefit type, and age start benefits**

- Full PIA for workers and aged/disabled surviving spouse, half for dependents of workers, three fourths for other survivors
- Reduce for early start, increase for delayed start of benefits

# How much is the Social Security Benefit?

## Retired worker benefit reduction, and increment for age

- Reduce 5/9%/month up to 36, then 5/12% if start early
  - So, 70% of PIA if start benefit at 62, 80% at 64, with NRA 67
- Increase 8/12%/month if start after NRA
- Earnings test can reduce under NRA

## Aged spouse and aged widow benefits

- Aged spouse slightly higher reduction for age, 25% at 64
- Aged widow, 71.5% at 60, and for disabled widow at 50-59
- Widows “inherit” reduction and delayed credit from worker

## What is entitled to 2 benefits?

- Basically receive the higher of the 2, in total
- “Claiming strategies” now largely removed



# Social Security Financing

- Basically “pay-as-you-go”
  - Current workers provide for current beneficiaries
  - Social Security *cannot* borrow
  - Trust Fund securities provide a “contingency reserve”
- Current OASDI reserves (excess income) = \$2.9 trillion
  - Available to augment tax income as needed
  - About 3 times the annual cost of the program
- Reserves projected to deplete in 2020 Trustees Report
  - 2034 for OASI, 2065 for DI, 2035 on a combined basis
  - Updates for COVID: 2033 OASI, 2059 DI, 2034 combined
    - ***Expect Congress to act—as it always has***

# Now, a Few Common Myths

- 1) Social Security is bankrupt, insolvent, running out of money
- 2) Increasing longevity and disability are the problem
- 3) The money in the trust funds has been spent
- 4) I should start benefits as soon as I can
- 5) My tax contributions have been saved up for *me*
- 6) Benefits scheduled in the law would be all I need
- 7) Social Security is responsible for Federal debt
- 8) “Fixing” the Social Security shortfall will be hard

# Myth 1: Social Security Is Bankrupt, Insolvent, Running Out of Money

## Facts:

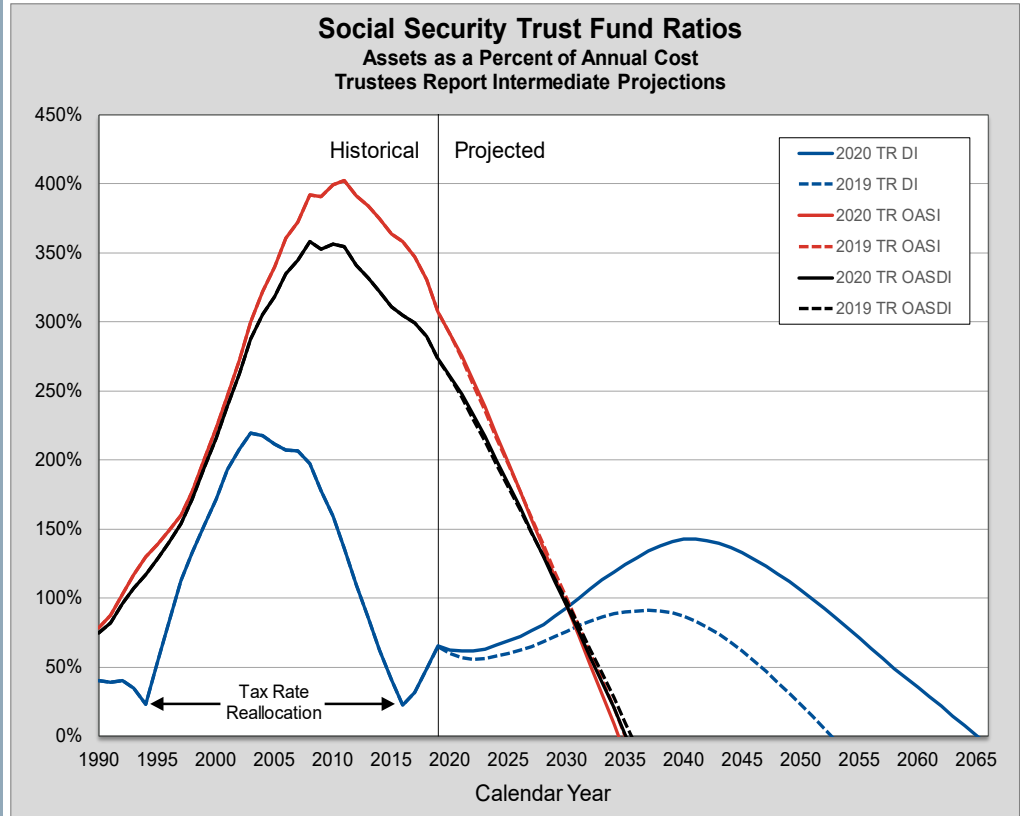
- a) Social Security ***cannot*** run out of money
- b) Even if Congress allowed trust fund reserves to deplete...
  - Continuing income would cover 79% of scheduled benefits in 2035
  - And 73% of scheduled benefits in 2094
- c) Over 85 years, Congress has always acted timely
  - Scheduled benefits have always been paid in full

# Solvency: OASDI Trust Fund Reserve Depletion in 2035 (same as last year)

Reserve depletion date varied from 2029 to 2042 in reports over the past 30 years (1991-2020).

DI Trust Fund – reserve depletion in 2065, thirteen years later than last year.

Due largely to low recent and near-term disability applications and awards, and an assumed lower ultimate disability incidence rate.

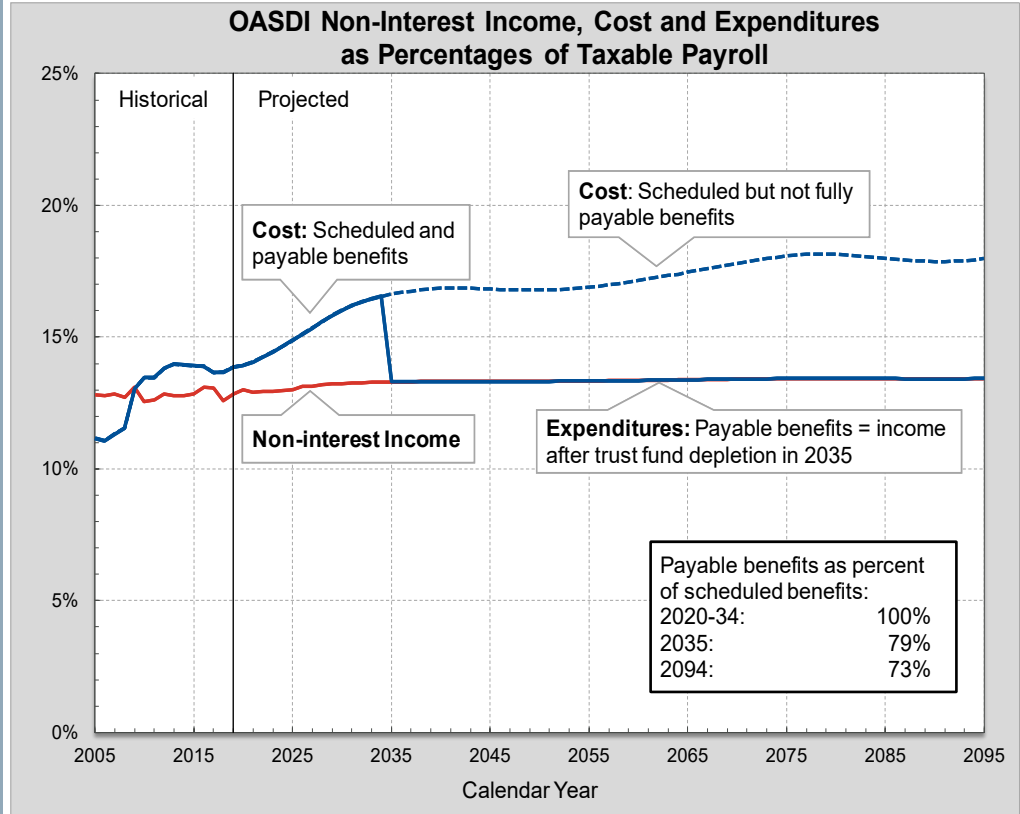


# OASDI Annual Cost and Non-Interest Income as Percent of Taxable Payroll

Persistent negative annual cash-flow balance starting in 2010.

79 percent of scheduled benefits still payable at trust fund reserve depletion.

Annual Deficit in 2094: 4.51 percent of payroll – 0.36 percent larger than last year



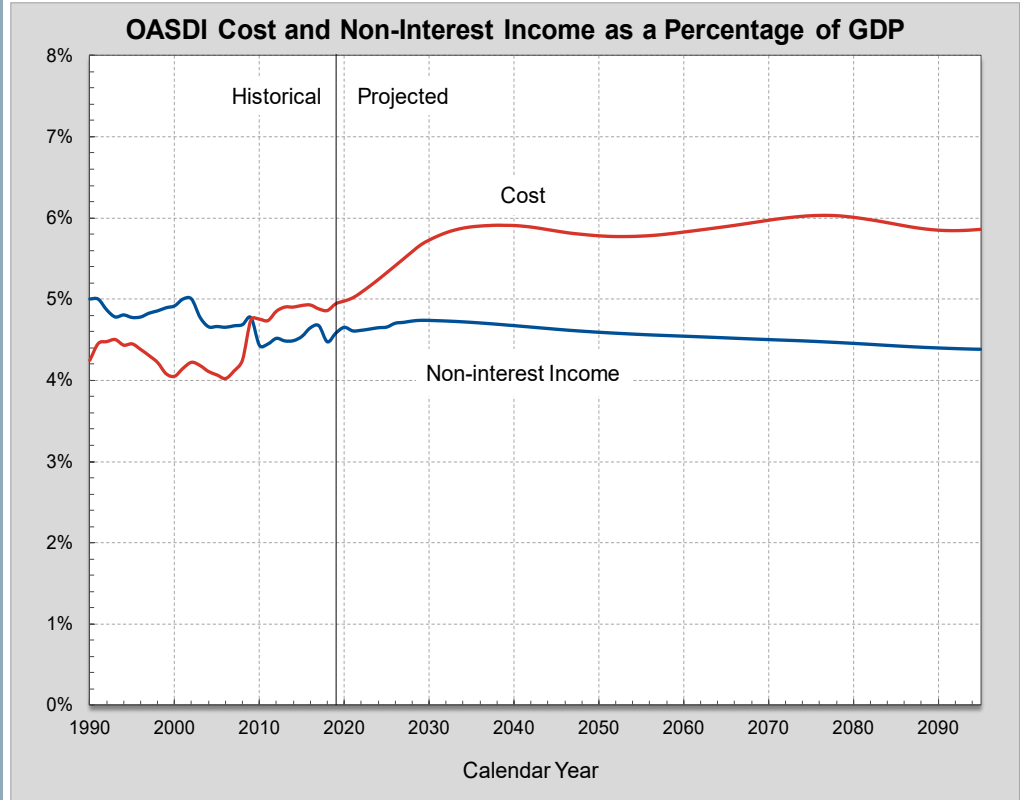
# Myth 2: Increasing Longevity and Disability Are the Problem

## Facts:

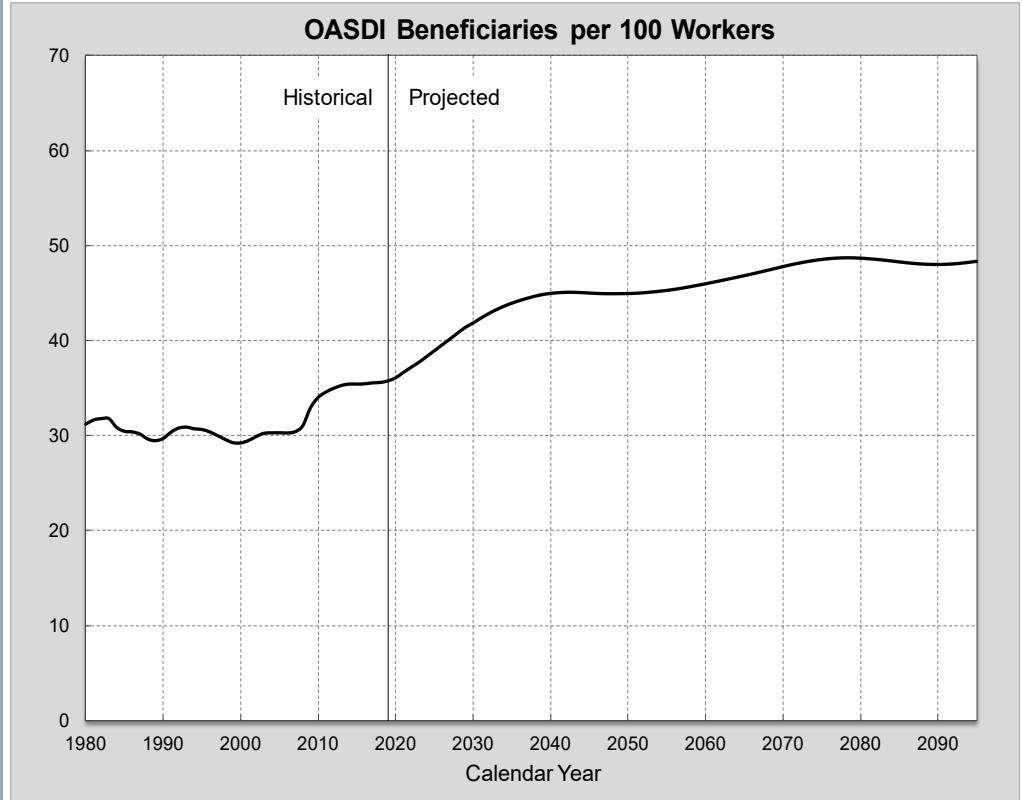
- a) The age distribution of the population is the most important factor in Social Security cost
- b) Population “aging” through 2035 is mainly due to birth rates
- c) Disability costs have matured, and are dropping

# SUSTAINABILITY: Cost as percent of GDP

Rises from a 4.2 percent average in 1990-2008, to about 5.9 percent by 2038, then declines to 5.8 percent by 2053, and generally increases to 5.9 percent by 2094.



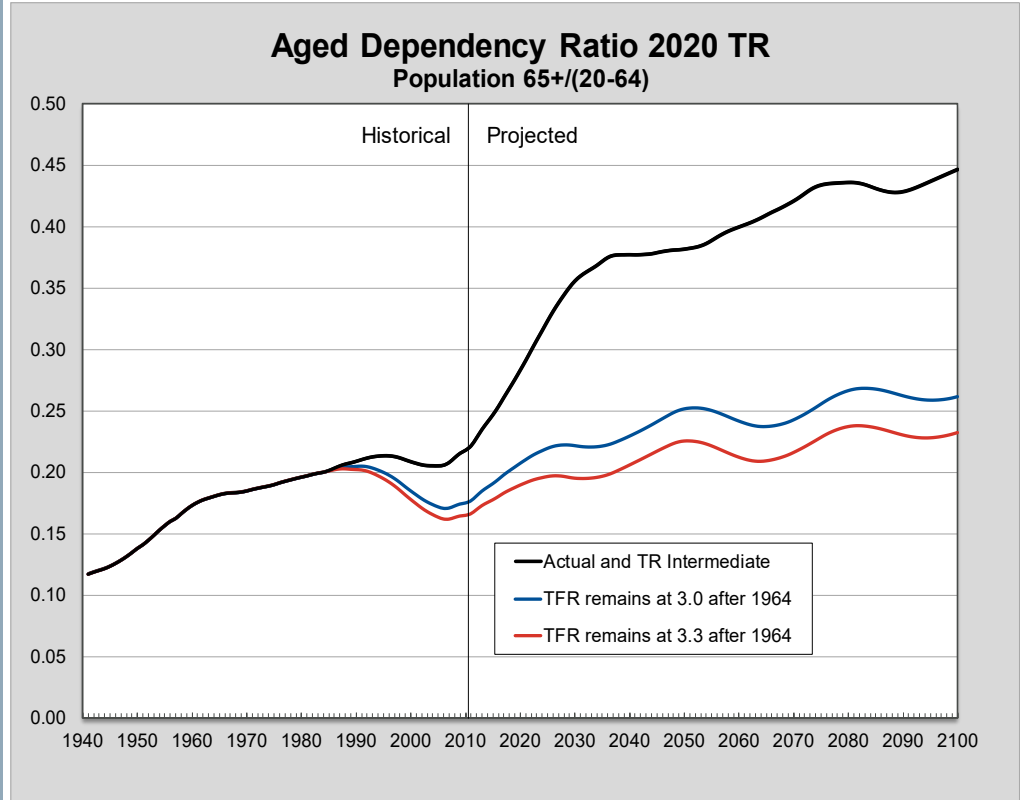
# OASDI Beneficiaries per 100 Workers





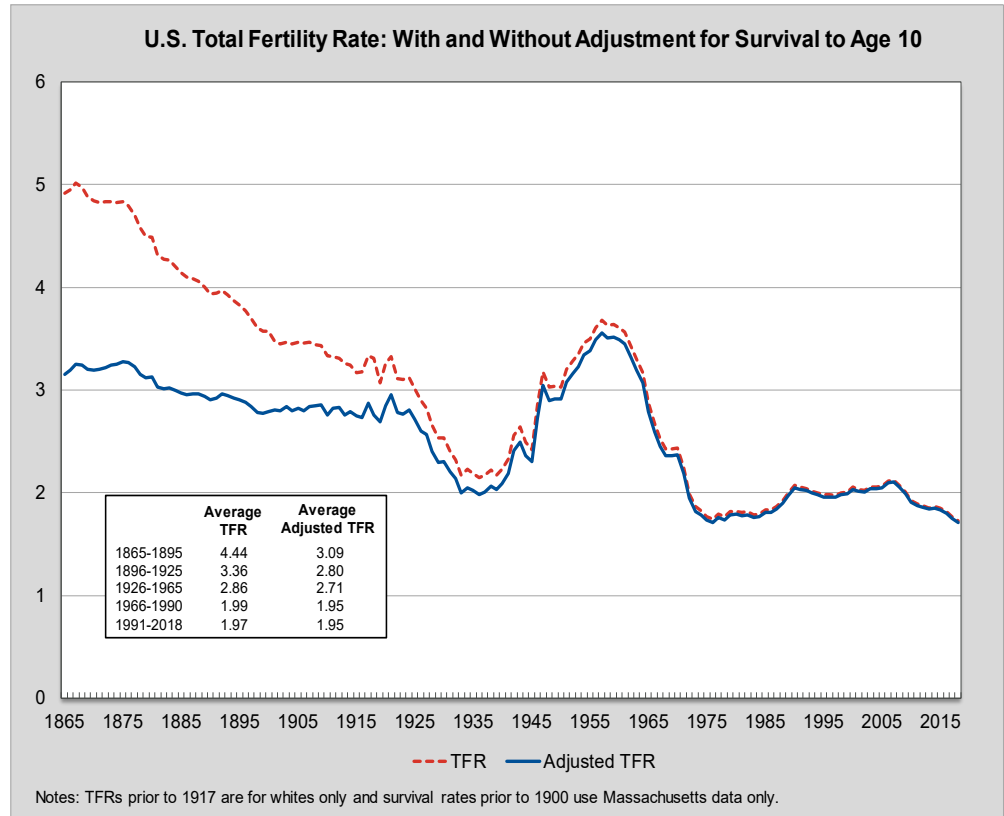
# Aging - Change in Age Distribution

Mainly due to drop in birth rates



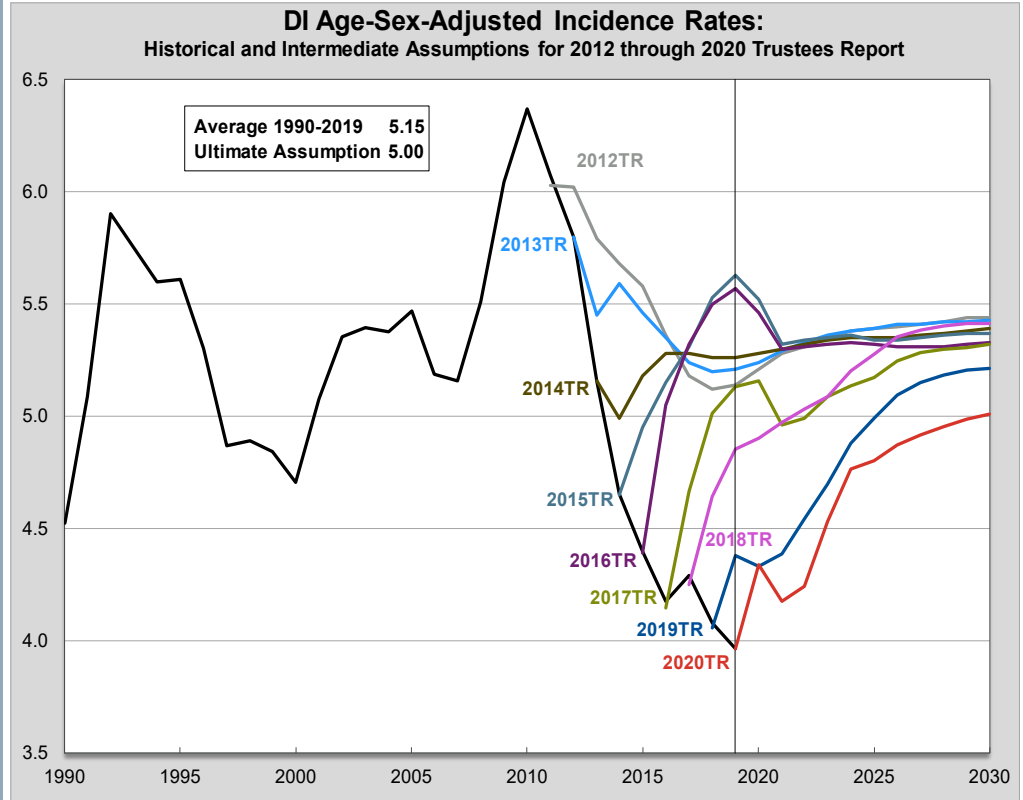
# Birth Rates

Average Total Fertility Rate falls from 3 to 2



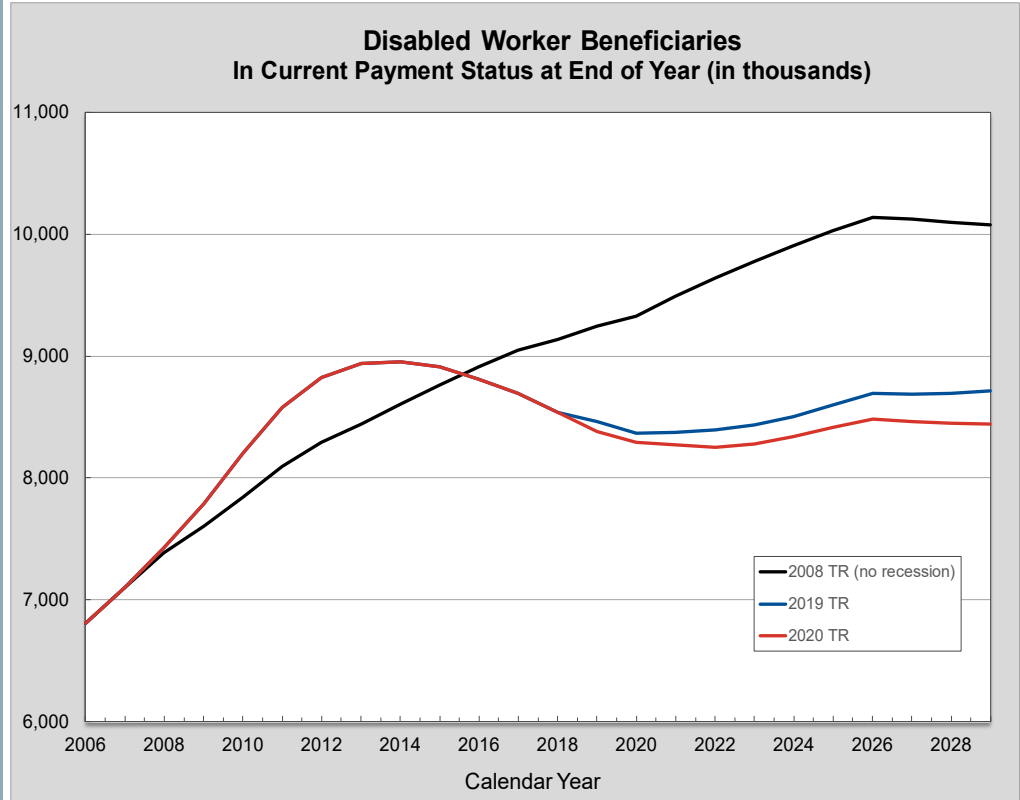
# Disability Incidence Rate Also Remains Historically Low

DI disabled worker incidence rate rose sharply in the recession, and has declined since the peak in 2010 to extraordinarily low levels in 2016 through 2020.



# Fewer Disabled Worker Beneficiaries

Fewer now and in near term based on recent applications and incidence rates.



# Myth 3: The Money in the Trust Funds Has Been Spent

## Facts:

- a) Every dollar of income is invested by law in ***interest-bearing securities backed by the full faith and credit of the United States***
  - These are not “worthless IOUs”!
- b) Securities are issued at market yield rates
- c) Securities held by the Trust Funds have always been honored, as have all other Treasury issues

# Myth 4: I Should Start Benefits As Soon As I Can

## Facts:

- a) Social Security retirement benefits are designed to provide about the same lifetime value regardless of when you start, ***on average***
- b) When to start is personal—you might want to wait if you are in average or better health
- c) If you delay by working or using other assets, Social Security increases your life annuity at terms available nowhere else

# Myth 5: My Tax Contributions Have Been Saved Up for *ME*

## Facts:

- a) Social Security is a “social contract”
- b) Basically, benefits paid today are financed from contributions by recent workers
- c) This is why the age distribution of the population is fundamental—the workers of the day share with the retirees, survivors, and disabled of the day
- d) This is true for advance funded systems as well

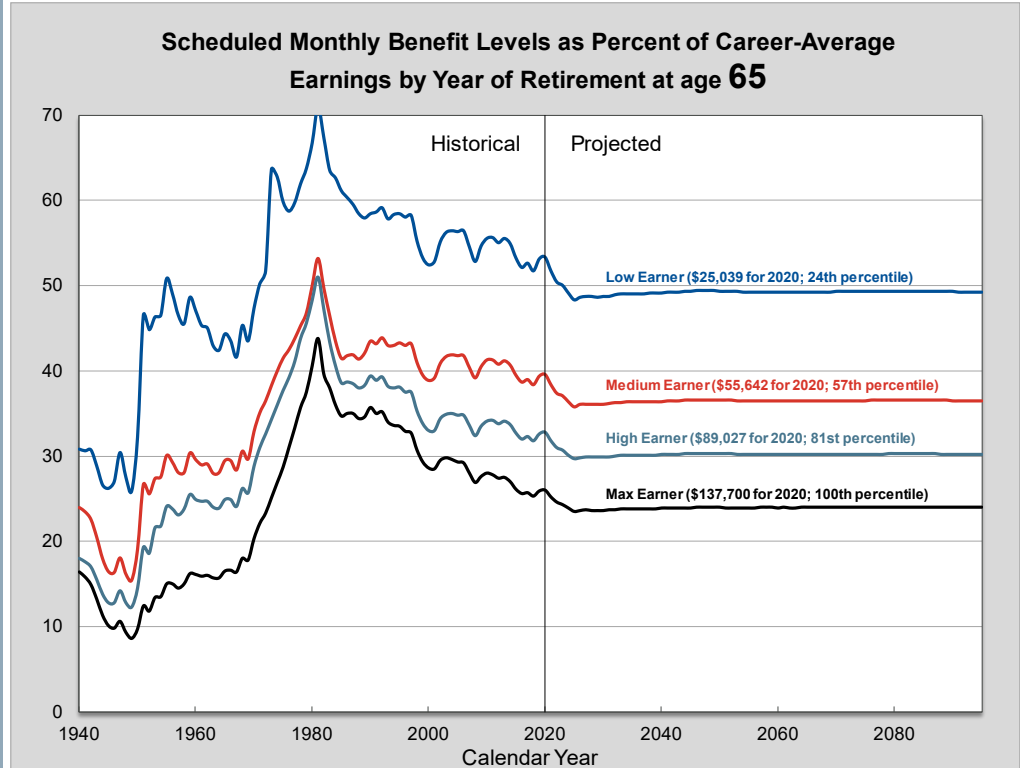
# Myth 6: Benefits Scheduled in the Law Would Be All I Need

## Facts:

- a) Recall the 3-legged stool: 75-80% in retirement
- b) Social Security provides about 40% of career-average earnings (varies from 25% to over 80%)
- c) So the other legs of the stool—personal savings and private pensions—are needed
- d) But increasingly, Social Security is the primary source of lifetime income

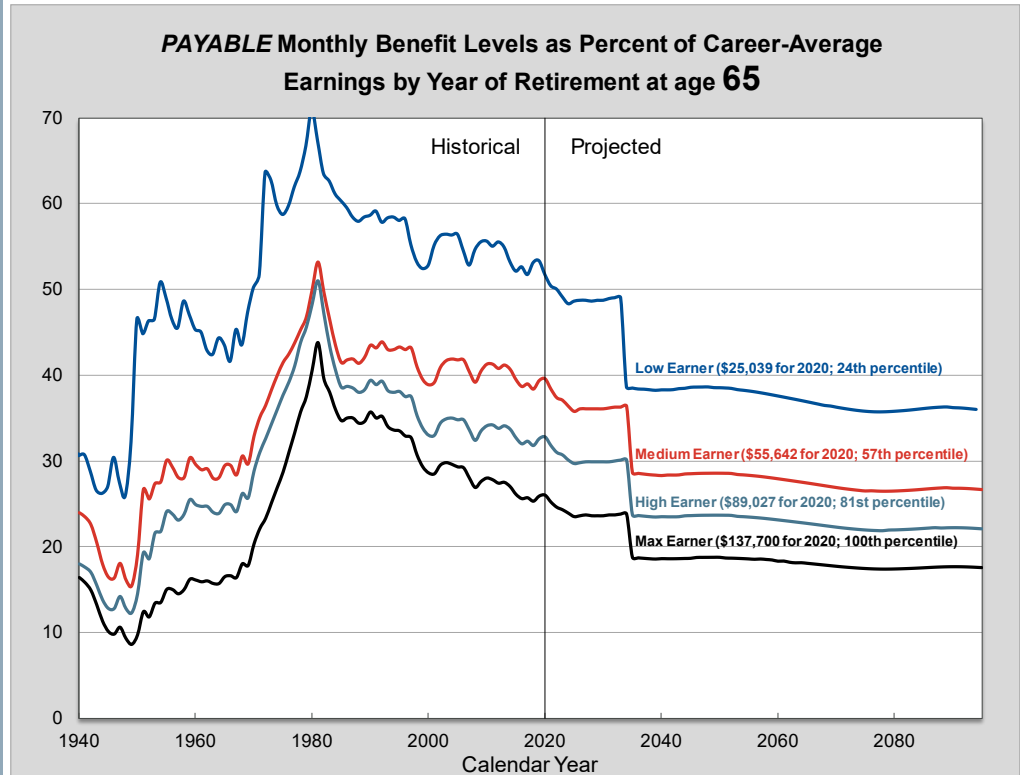


# Replacement Rates Based on the 2020 TR



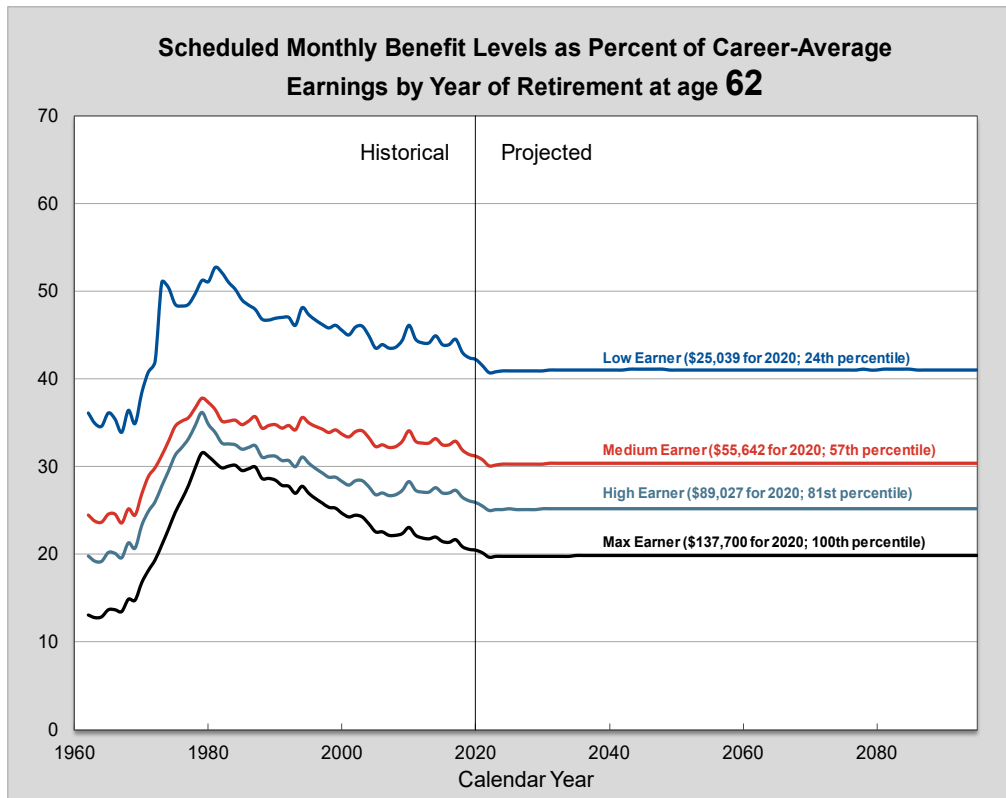
Source: Annual Recurring Actuarial Note #9 at [www.ssa.gov/oact/NOTES/ran9/index.html](http://www.ssa.gov/oact/NOTES/ran9/index.html)

Payable Benefits Under the Law, After Trust Fund Reserves Are Depleted, Are Even Lower



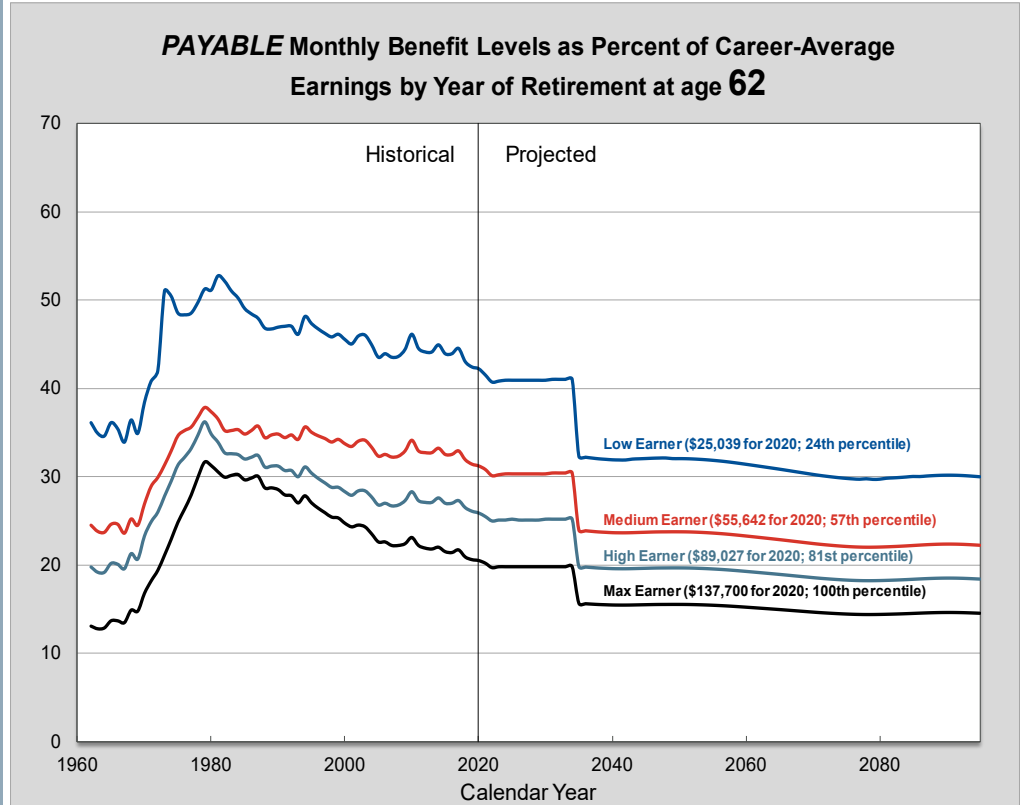
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# How About at Age 62, Where Many Start Benefits?



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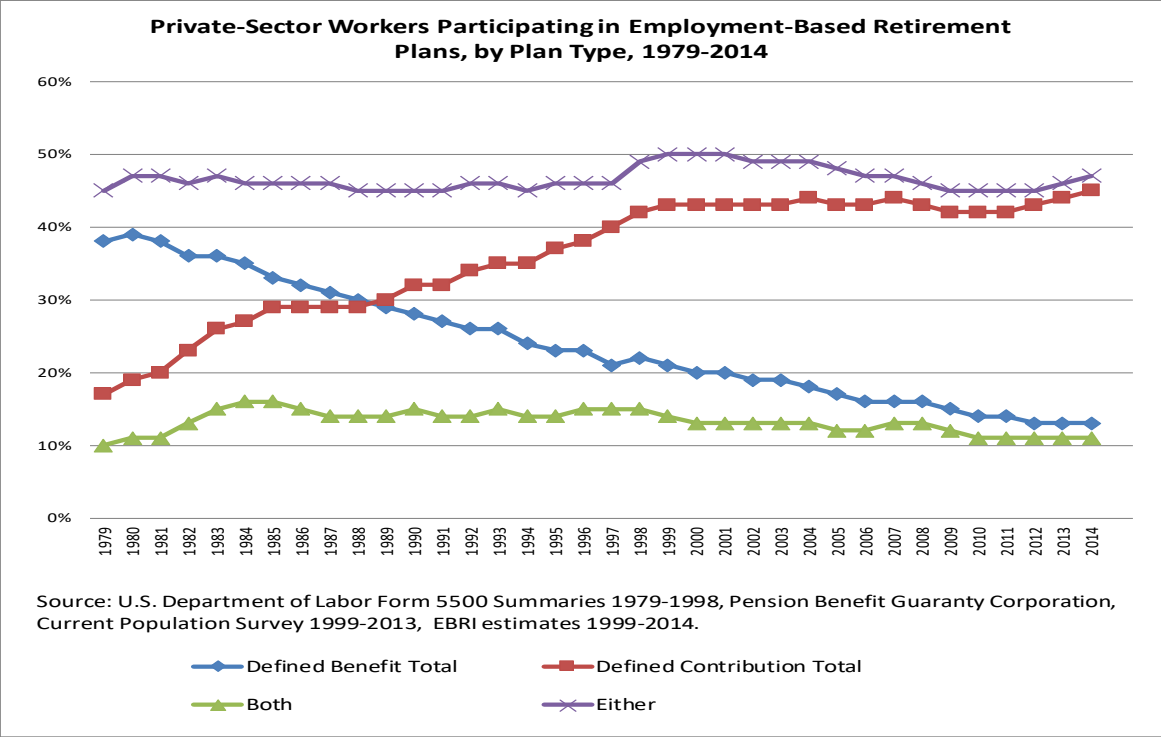
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# Defined Benefit Plans Replaced by DC Plans

And lump sum options increasing for DB plans

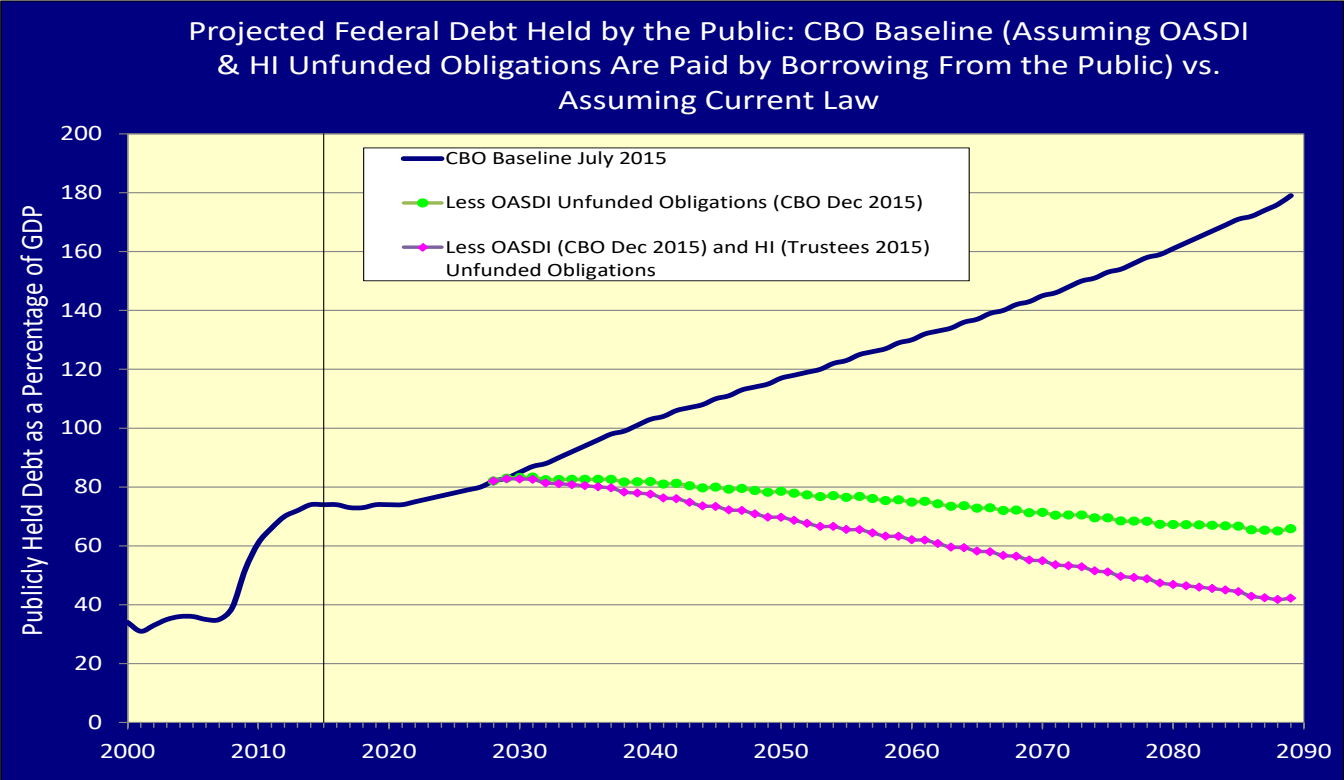


# Myth 7: Social Security Is Responsible for Federal Debt

## Facts:

- a) OASI, DI, HI Trust Funds do **not** add to the debt
- b) In fact, these trust funds finance part of the debt
- c) If trust fund reserves ever depleted, the programs **cannot** borrow
- d) Thus, the common “budget scoring convention” is misleading and inconsistent with the law

# So—What If We Project Federal Debt Consistent With the Law? Projection to 2090 Back in 2015



# Myth 8: “Fixing” the Social Security Shortfall Will Be Hard

## Facts:

- a) Need to adjust the benefits or revenue given the shift in the age distribution
- b) By 2035, lower scheduled benefits by 1/4, or raise revenue by 1/3, or some combination
- c) Question: what do the American people want?
- d) Many options are already under consideration



# Some Ways to Lower Cost

- Lower benefits for retirees—not disabled?
  - Increase normal retirement age (lowers OASDI cost, but increases DI cost)
  - Can exempt long-career low earners
- 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
  - But, some say increase it with the CPI-E (based on purchases of consumers over age 62)

# Some Ways to Increase Revenue

- 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

# For More Information Go To

<http://www.ssa.gov/oact/>

- There you will find:
  - All OASDI Trustees Reports: 1941-2020
  - Detailed single-year tables for recent reports
  - Our estimates for comprehensive proposals
  - Our estimates for the individual provisions
  - Actuarial notes; including replacement rates
  - Actuarial studies
  - Extensive databases
  - Congressional testimonies
  - Presentations by OCACT employees