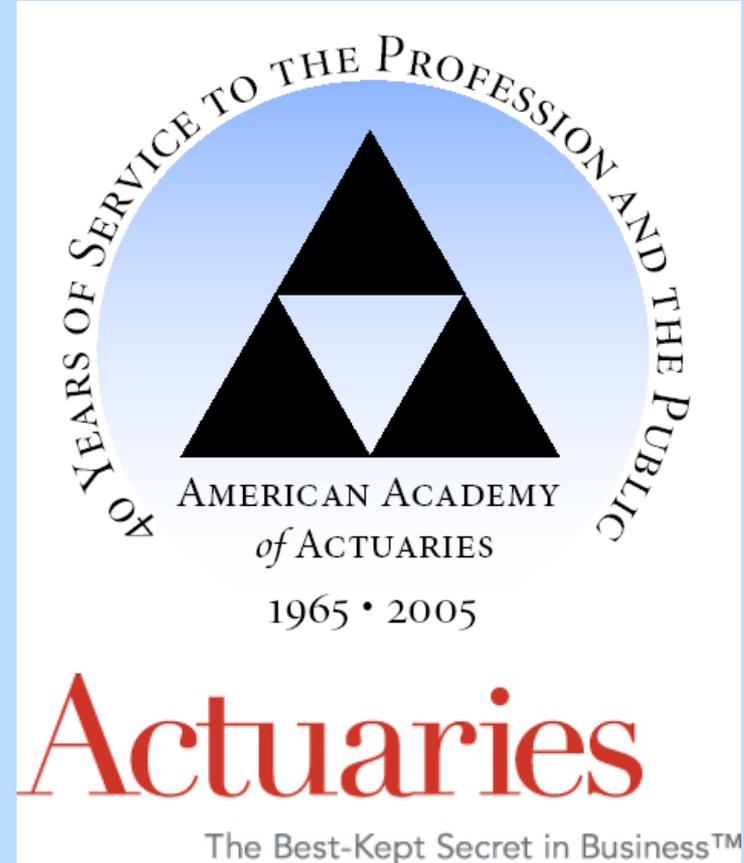




Actuaries Club of the Southwest

Bruce Schobel

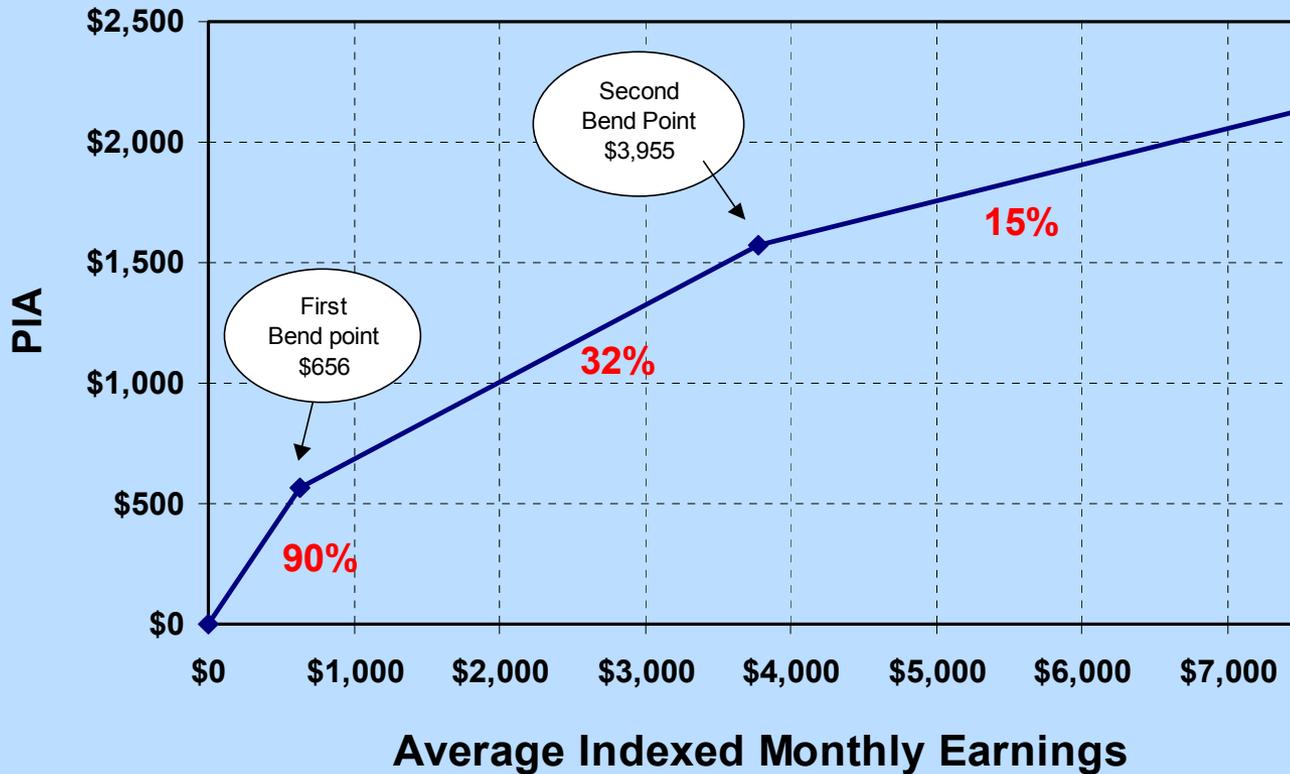
*Pension Practice Council
Retirement Principles Task Force
Social Insurance Committee*





The Landscape for Social Security Reform

Primary Insurance Amount at NRA for persons reaching age 62 in 2006





Benefits

Social Security Benefits at Normal Retirement Age (and at Disability)



This and following graph show the primary goals of Social Security:

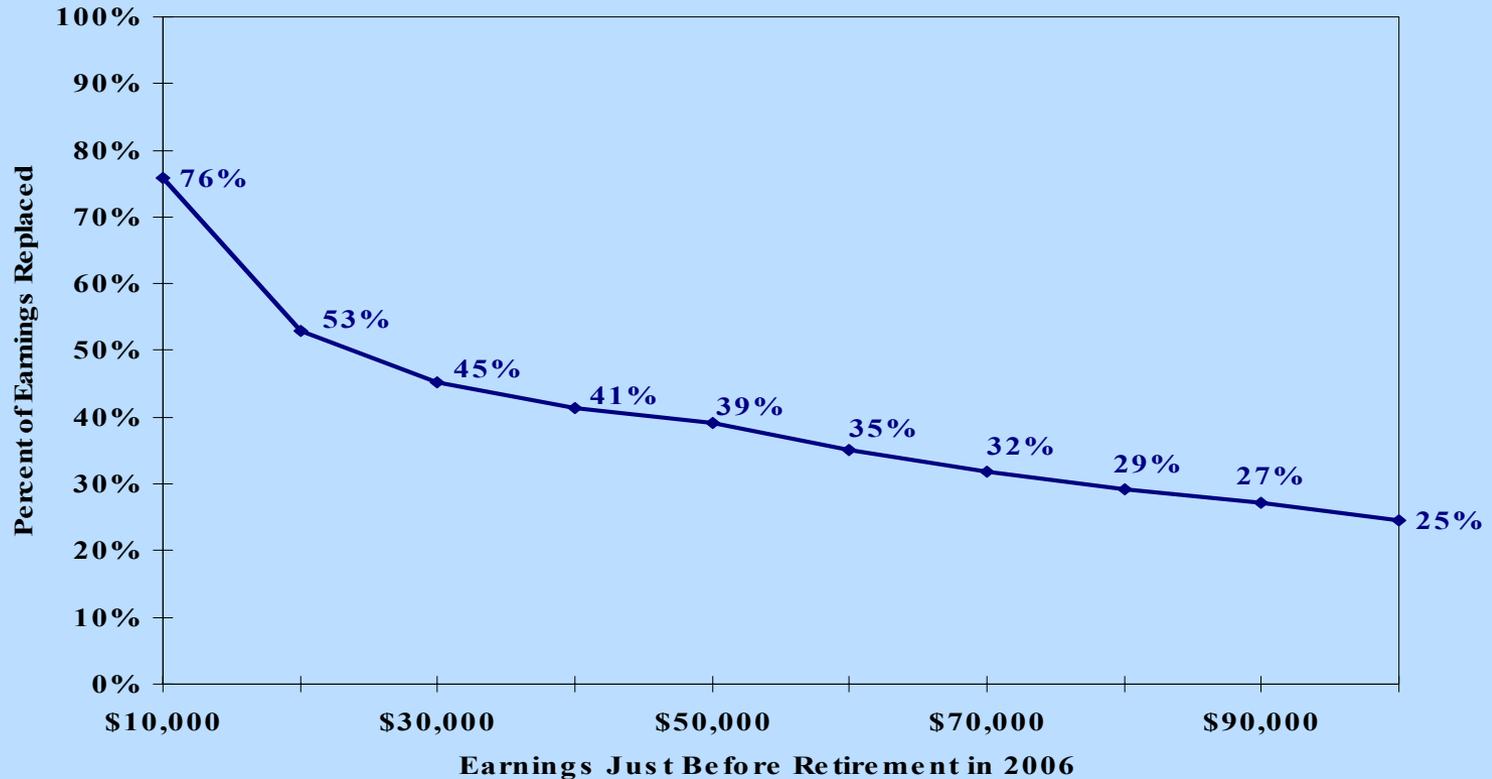
- (1) **Individually equitable** benefits (important to higher wage earners - the more contributed, the more received).
- (2) **Socially adequate** benefits (progressive benefits that are more important to lower wage earners)





Replacement Ratios

Social Security Replacement Ratios at Normal Retirement Age (and at Disability)



See History of Provisions at www.ssa.gov/OACT/HOP. Past wages based on National Average Wage Index
These percentages decrease by about 5 percentage points over the next 20 years, per Table VI.F10 in 2006 rpt.





Normal Retirement Age (NRA) = Age for starting full (unreduced) benefits. Age 62 is the earliest starting age for retired-worker benefits.

Reductions for retiring before NRA are 6 2/3% for each year before NRA (up to 3 years), plus 5% for each additional year.

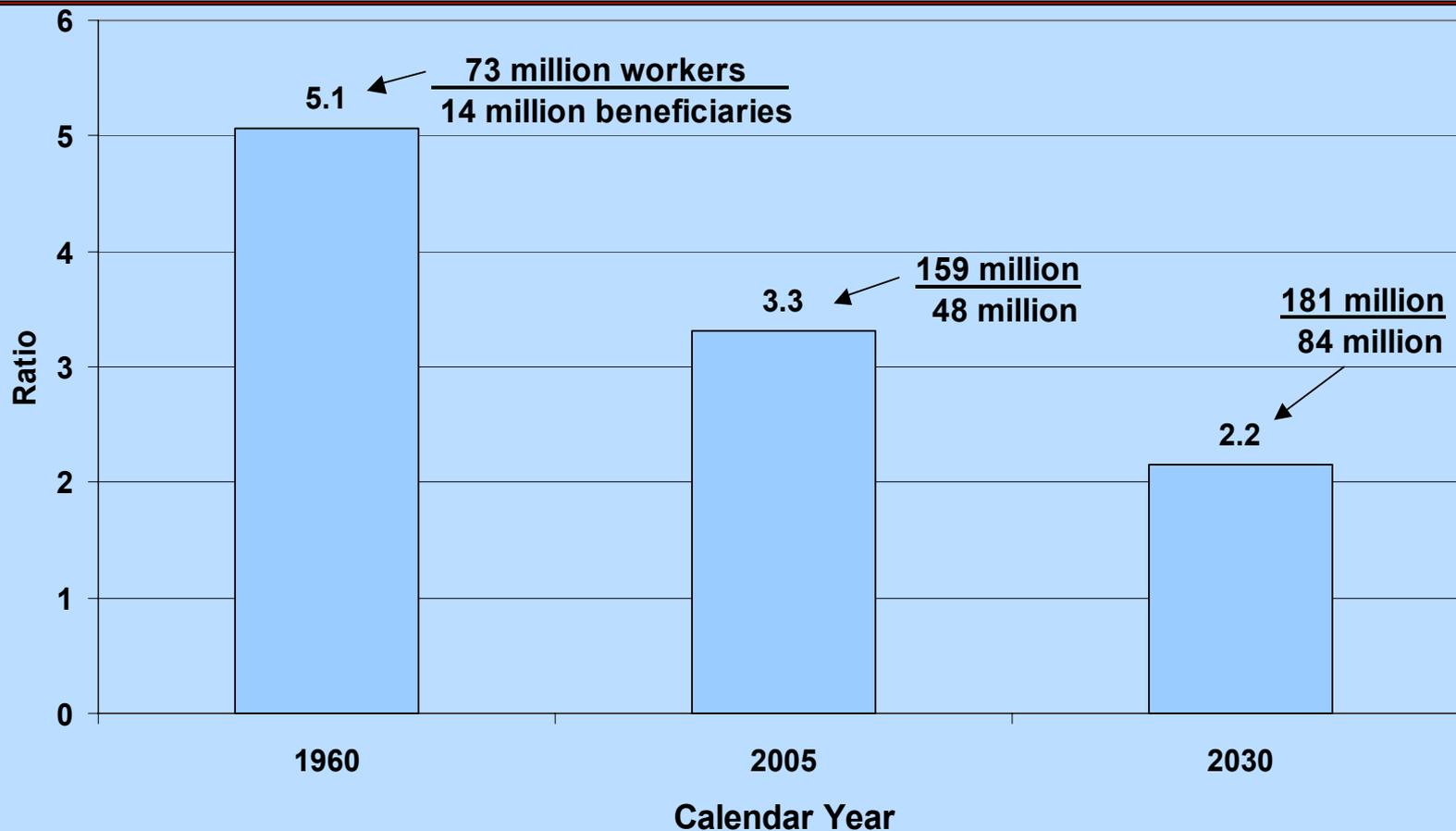
Increases for retiring after NRA are now 8% per year until age 70.

Year of Birth	Normal Retirement Age
1937 & earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943-54	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 & later	67





Workers per Beneficiary



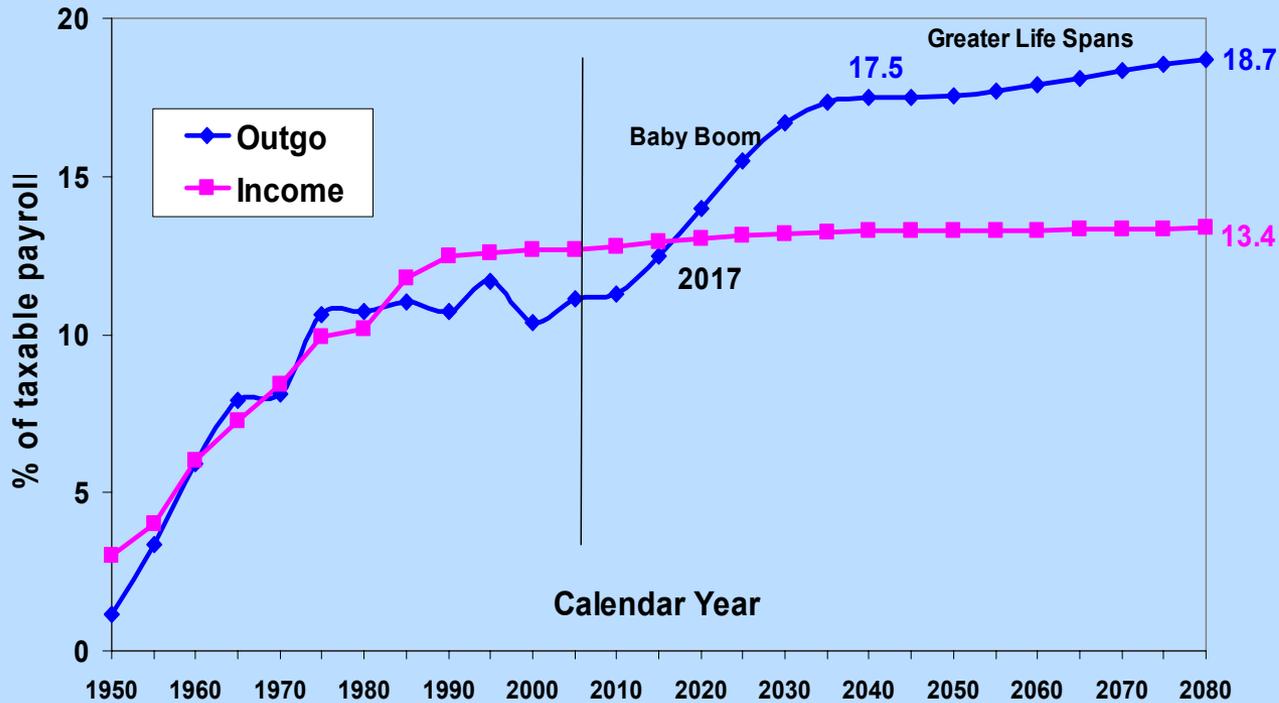
The number of workers supporting beneficiaries decreases dramatically due to baby boomers & longer lifespans. Source: 2005 SSA Trustees' Report, Table IV.B2





Income and Outgo

Social Security Income & Outgo
Intermediate Assumptions



2006 Report Table IV.B1. Using low (high) cost assumptions, the 2080 outgo is 13.5% (27%), & the 2017 date is 2022 (2013); 2020 per CBO. The unfunded obligations over the next 75 years = \$4.6 trillion = -2.02%, -5.17 & 0.35% of taxable payroll for the intermediate, high, & low cost assumptions, per Table IV.B4 (1% per CBO). Table IV.B6&7 show it is \$13.4 trillion or -3.7% of payroll (1.3% of future GDP) over the infinite future (although we could increase SSNRA in the future). Future workers pay for themselves.

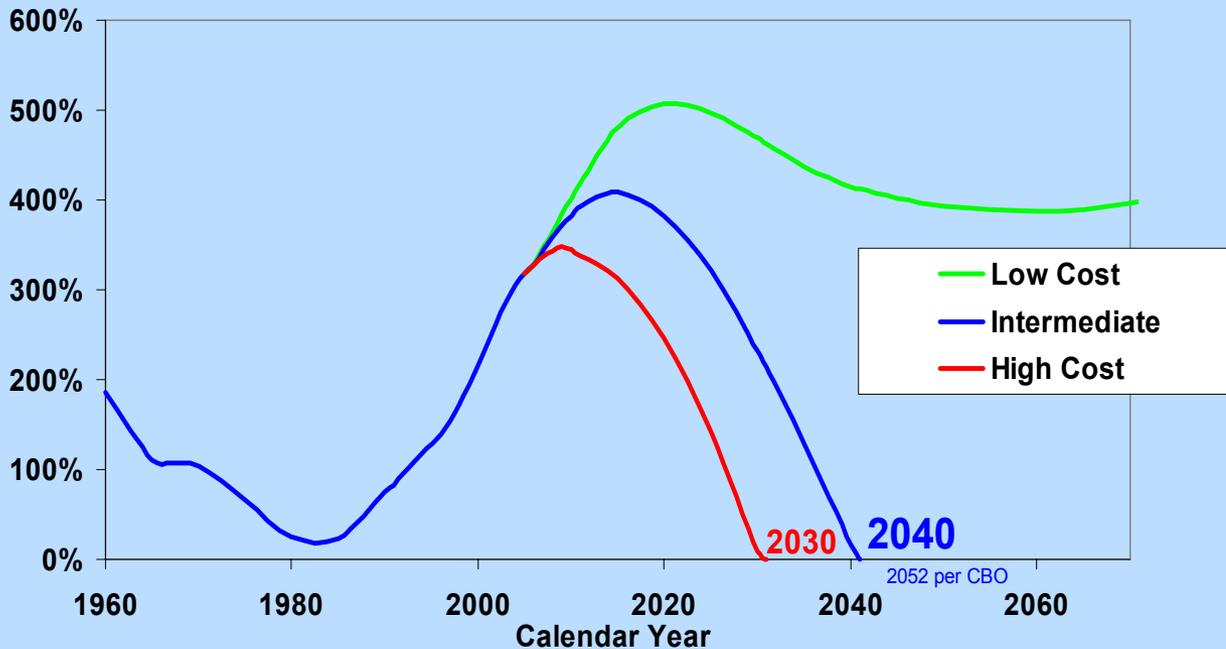




Social Security Trust Fund Ratios

(Beginning of Year Assets as a % of Expenditures)

Social Security Trust Fund Ratios
(Beginning of Year Assets as a Percentage of Expenditures)



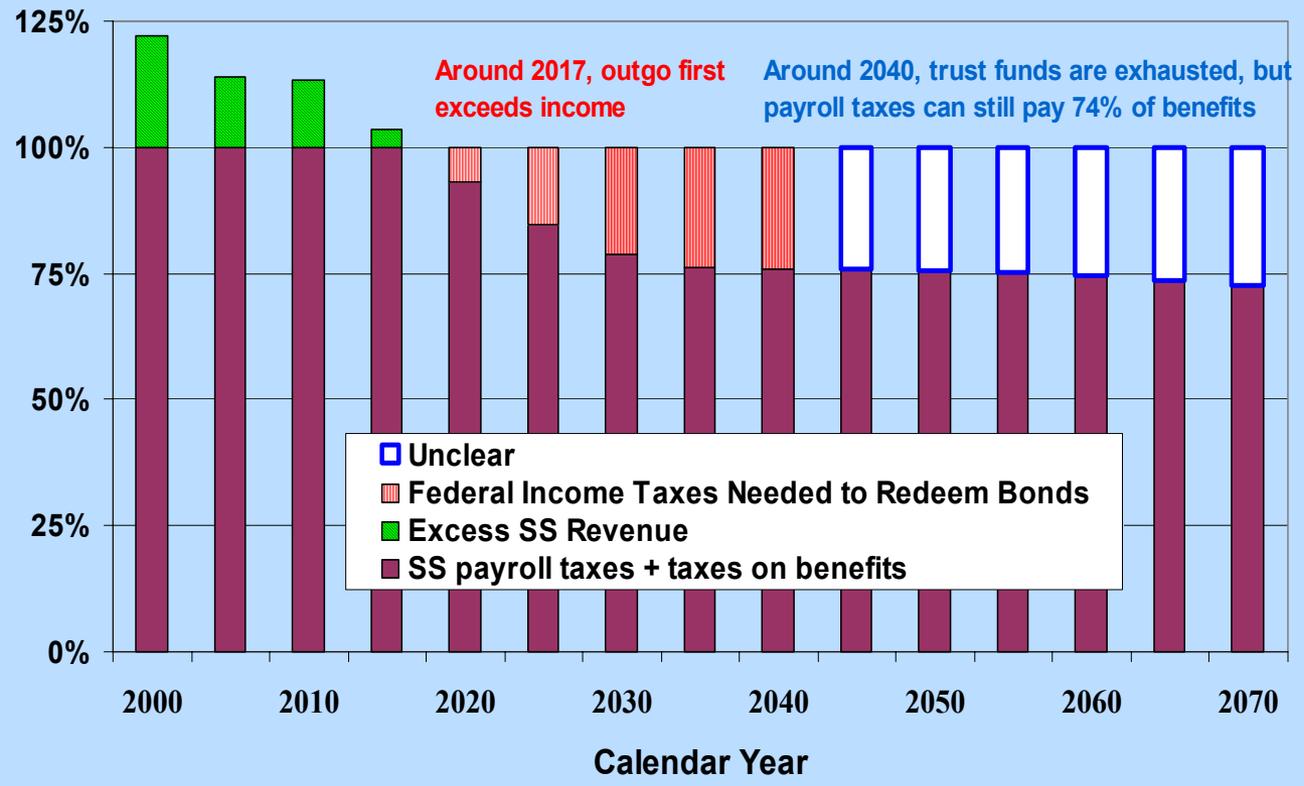
The Social Security Trust Funds are projected to be exhausted in 2040 using the Intermediate Assumptions. In 2040, tax income can pay 74% of benefits, per Figure II.D2 (70% in 2080). The assumptions are reasonable in the aggregate per GAO/PWC report & individually reasonable per SS Chief Actuary. Social Security solvent but may not meet the Sustainability Test (trust fund ratios stable or increasing around 75th year) on low cost figures. 2006 Trustees Report Table IV.B3. Historical ratios from VI.A4.





Social Security Payments

How Are Social Security Benefits Paid?



Source: 2006 SS Trustees Report Table IV. B1 Note: Redeeming SSA's Treasury Bonds requires General Revenue (surplus income taxes, more Deficits, or tax increase). Increased deficits (or stock redemption) increases borrowing costs.





Reasons To Reform Social Security Sooner Rather Than Later

More Options are Available to Us

More People Can Be Included in Reform

Benefit Cuts and Tax Increases for Future Cohorts Can Be Smaller

Changes Can Be Phased In

People Can Plan Ahead

We Can Restore Faith in Social Security and the Government





Options for Reform

See Social Security Game at www.actuary.org

Actuaries Look At Options for Reforming Social Security

The American Academy of Actuaries has described below commonly discussed options for reforming Social Security, along with their impact on the solvency of the program's trust fund. You can use this to determine a combination of options that makes Social Security solvent again. (The total impact on solvency must equal or exceed 100%.) In addition, in order to keep Social Security solvent permanently, other adjustments would be needed in the future. This game is on our web site at www.actuary.org

Option	Supporters say...	Opponents say...	% Fix
1-Raise the retirement age to 70 by 2030 and keep adjusting the age as people live longer.	Since Social Security was enacted, life expectancy has increased from 61 to 76 years, and we are healthier at older ages. It makes sense to keep pace by asking people to work longer before claiming full retirement benefits, as they will prob live longer.	Could be hard on people with physically demanding jobs or who are partially disabled; employers may not want an older workforce with associated higher health care costs. Alt: Accelerate increase in retirement age to 67 and index thereafter	68% 36%
2-Reduce cost-of-living adjustment (COLA) by ½ percentage points	A Congressional commission felt that the Consumer Price Index (CPI) was overstated by 1.1 percentage points, meaning the annual COLA is too high.	BLS decreased the CPI estimate by 3/4%. COLA reductions are cumulative which mean oldest retirees fall far behind in purchasing power. Very elderly women already have very high poverty rates.	42%
3-Reduce benefits by 5% for future retirees.	Everyone should be part of the solution.	This would hit hardest people with low incomes who often rely entirely on Social Security for all their retirement income.	32%
4-Affluence Test: Reduce benefits for those whose total retirement income exceeds \$50,000 per year.	This option preserves benefits for those most in need. A couple with total retirement income (including investment earning & the value of Medicare) of \$70K would lose 30% of their Social Security benefit. Over \$120K, they would lose 85%	Discourages savings and encourages people to hide assets; changes Social Security from universal program to one based on need. Social Security needs universal support to survive. Some people might try to avoid paying taxes if they didn't get anything for them.	75%
5-Raise payroll tax on workers and employers by ½ percentage points each	Increasing the Social Security payroll tax from 12.4% to 13.4% (gradually) won't hurt because real wages are going up and it would solve half of the system's financial problems.	Because we may also have to increase the Medicare payroll tax, total taxation could be burdensome, particularly for low-income people. Workers might save less, employers pay less to pension.	51%
6- Increase wages subject to Social Security tax	Raising the current \$90,000 limit by about 1/4 th would increase FICA (& SECA) taxes for those who can afford it.	Makes Social Security a worse deal for those with higher incomes, who will get little for their additional contribution. Costly for employers too. Erodes universal support Alt: Eliminate cap	26% 92%
7-Tax Social Security benefits like pension benefits	Why aren't Social Security benefits taxed as much as pension benefits? Low-income retirees (30% of total) would still pay no income tax. It simplifies tax rules, but should be phased-in.	This will increase the taxes of middle income people	20%
8-Include new state and local government workers	State and local workers should pay their fair share to keep Social Security solvent. Universal SS has less problems.	These workers do fine under their own pensions; this would divert contributions from state and local government pension plans.	11%
9-Invest 40% of the Social Security Trust Fund in private investments such as stocks	Could boost return on investment with less risk to individuals; hiring investment managers and using indexes avoids government interference. Saves money outside government.	Social Security's assets could be 5% of private market; stock voting and stock selection could be politicized. Could increase income taxes, interest rates, and borrowing costs, as gov't gets less.	0%* to 48%
10-Create personal retirement accounts (Divert some payroll tax to a private account)	Could boost return on investment. Add-on would increase national savings and productivity. Saves money outside government. Gives individual more control over investments and responsibility for retirement	Individuals take on investment risk, inflation risk, longevity risk, leakage risk. Large transition costs must be paid to cover current retirees and administrative costs could eat into returns. Could increase income taxes, interest rates, and borrowing costs. Add-on reduces other saving and pension contributions.	0%**

* This is heavily dependent on the assumption for future investment returns.

** Model 1 of Bush's Commission to Strengthen Social Security, which was solely a plan to implement individual accounts (IA), did not reduce Social Security's deficit. Their Model 2 showed that the IAs could help workers make up some of the cuts in the Social Security guaranteed benefit if their investments do well.





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