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HEARING ON SOCIAL SECURITY AT 75 YEARS:
MORE NECESSARY THAN EVER

SUBCOMMITTEE ON SOCIAL SECURITY
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

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Chairman Pomeroy, Ranking Member Johnson and Members of the Subcommittee: thank you for the opportunity to be here today to commemorate the 75th anniversary of the Social Security Act. The title of this hearing is absolutely true: Social Security IS more necessary than ever as workers, families, and elders face the economic risks of today's economy.
My remarks draw on policy education briefs and reports issued by the National Academy of Social Insurance: One report, ***Fixing Social Security: Adequate Benefits, Adequate Financing***, explains why benefit adequacy deserves attention in today's policy review, the state of Social Security finances, and policy options (including cost estimates) for about 30 ways to improve Social Security's future finances and a dozen ways to target more adequate benefits to vulnerable groups. Another report, ***Economic Crisis Fuels Support for Social Security: Americans' Views on Social Security***, presents findings of a survey the Academy did in collaboration with the Rockefeller Foundation about Americans' views on Social Security.

In my remarks today, I will make the following points:

1. We can afford Social Security in the future.
2. Benefits are essential to elders, children, and the broad middle class of Americans who depend on wages for their livelihood.
3. Americans value Social Security and are willing to improve it and pay for it.
4. We have options to target more adequate benefits to vulnerable groups.
5. History offers innovative solutions to end the long-term shortfall.
6. A timely solution will benefit American workers and their families.

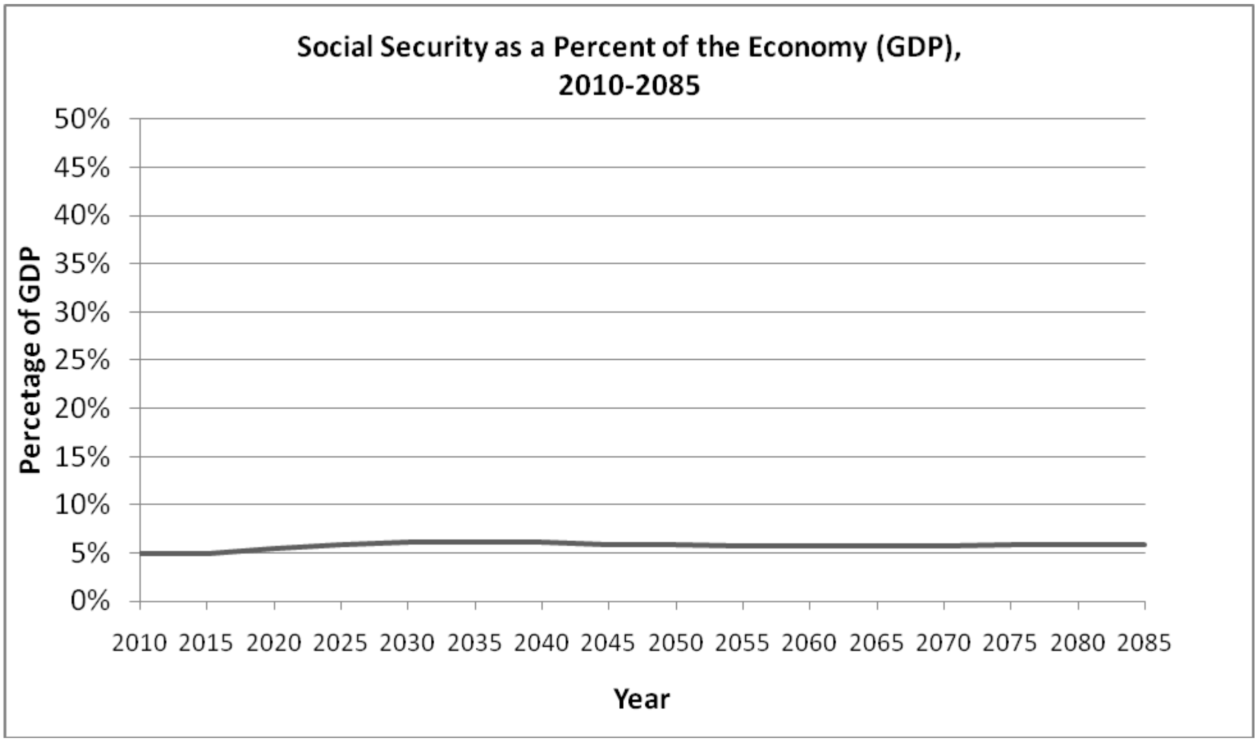
We Can Afford Social Security in the Future

The best way to assess the affordability of Social Security in the future is to compare benefits scheduled under current law with the size of the entire economy at the time benefits are due to be paid. According to the 2009 report of the Social Security Trustees:

- Social Security benefits are 4.9 percent of the economy, or gross domestic product (GDP), in 2010.

- Benefits are projected to rise to 6.2 percent of the economy in 2035, when all baby boomers will be over age 65.

After 2035, Social Security will remain between 6.1 and 5.8 percent of the economy for the rest of the next 75 years (See Figure below). This increase of 1.3 percent of the entire economy is clearly affordable. It is smaller than the growth in spending for public education when boomers were children. Then the share of GDP spent on public schools rose by 2.8 percent. School districts had to respond quickly because the crowds of five-year-olds showing up for kindergarten came as a surprise. Social Security for retiring boomers six decades later is not a surprise. It is expected. We can afford it.



Source: Board of Trustees. (2009). *Annual report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*. Washington, DC: U.S. Social Security Administration: Table VI.F4, page 184.

Benefits Are Essential to Elders, Children, and the Broad Middle Class of Working Americans

Social Security prevents poverty among the elderly.

- If seniors had to count on only their income other than Social Security, almost one out of two would be living in poverty.

- With Social Security, about one in ten is officially counted as poor.

Children have an important stake in Social Security (Lavery and Reno 2008).

- About 6.5 million children under 18 – nearly 9 percent of all U.S. children – received part of their family income from Social Security in 2005. They included 3.1 million children who received benefits as dependents of deceased, disabled or retired workers and 3.4 million others who did not themselves receive Social Security, but lived with relatives who did.

- Social Security lifted 1.3 million children out of poverty and reduced the depth of poverty for another 1.5 million children.

- Social Security is the most widespread form of life insurance for working families. Through Social Security, almost all U.S. workers, including those in the armed forces, have life insurance protection for their children when tragedy strikes.

Social Security is the mainstay of retirement security for the broad middle class, not just the poor. The five pie charts on the next page show the shares of income that couples and unmarried individuals age 65 and older receive from five main sources: Social Security, pensions, earnings, asset income, and other sources. Each pie represents one fifth of the elderly population (quintile), ranked by their annual income in 2008:

- Elders in the bottom two fifths of the income distribution (with less than about $20,000 a year) get more than 80 percent of their income from Social Security.

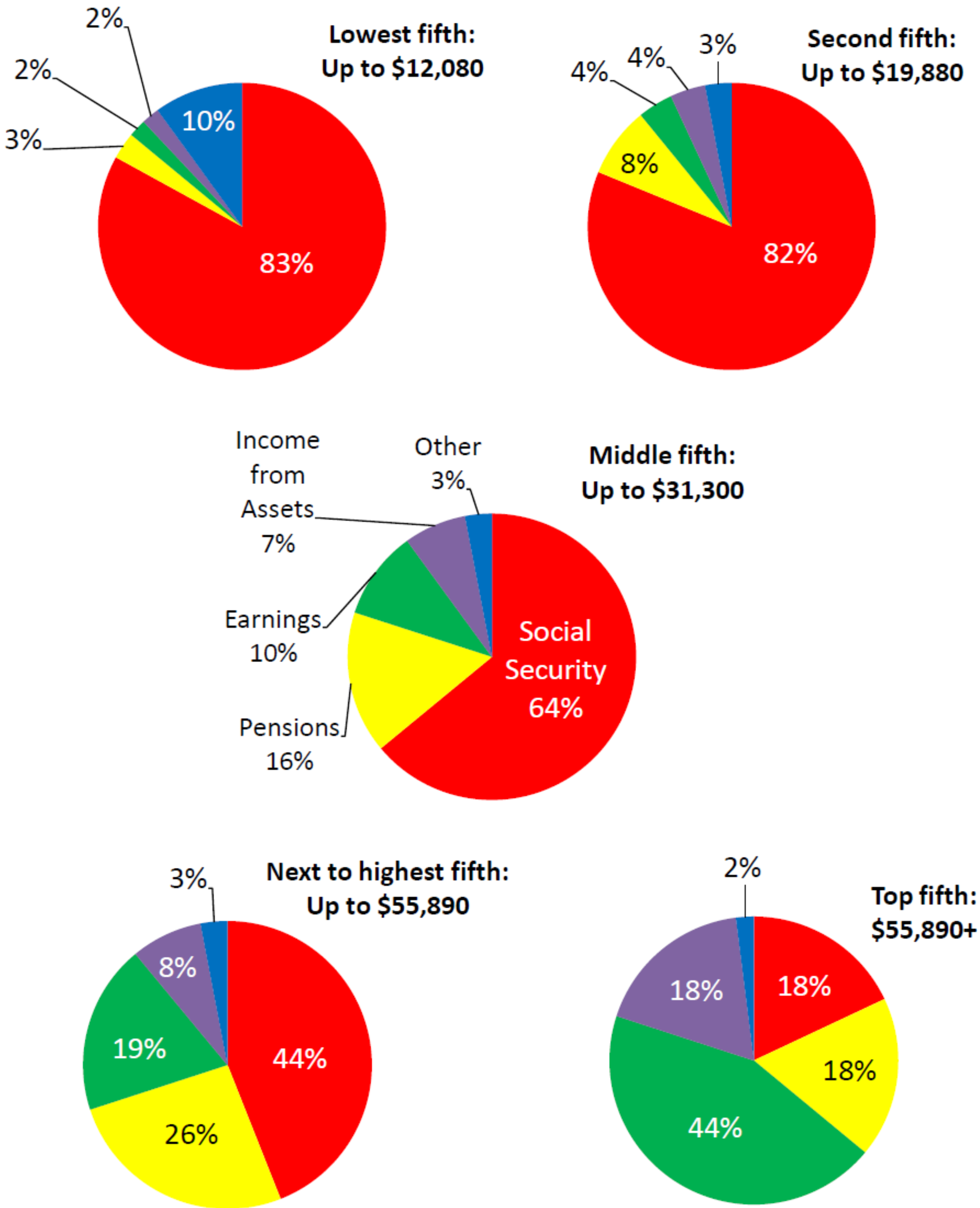
- Elders in the middle group (with incomes of about $20,000 to $31,000) get nearly two thirds of their income from Social Security. Pensions are the second largest source.

- Elders in the upper-middle income group (about $31,000 to $56,000) get nearly half their income from Social Security.

- Only in the top group (with incomes over $56,000) is Social Security not the main source of income. Earnings are their largest source because most couples and unmarried elders in the top income group are not yet fully retired. When and if their earnings cease, remaining income is likely to come in roughly equal shares from Social Security, pensions and income from assets.

Shares of Income from Specified Sources by Income Level, 2008

Married Couples and Unmarried Persons Age 65 and Older

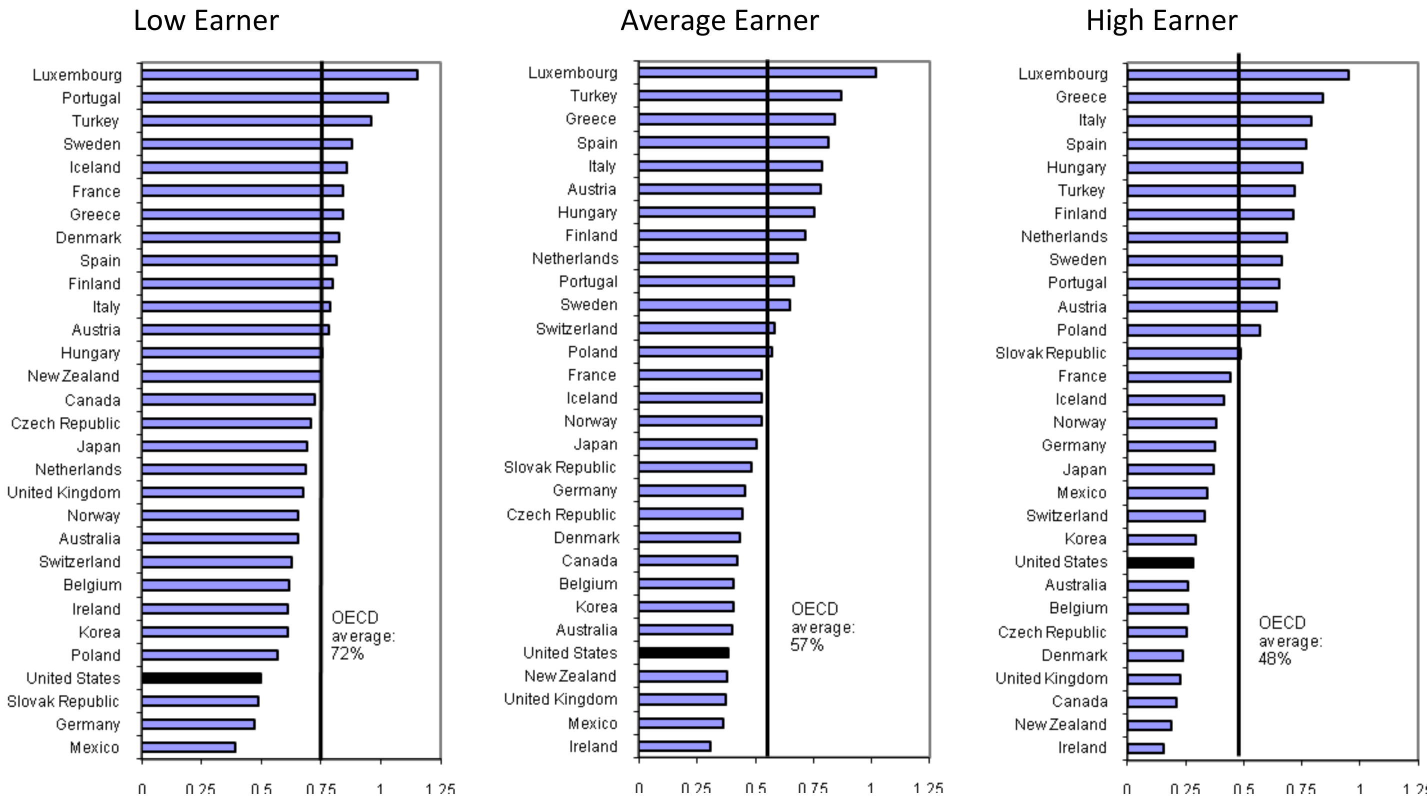


Source: Social Security Administration: *Income of the Population 55 and Over, 2008*

Social Security Benefits are Modest

The average monthly benefit for retirees was $1,166 in January 2010 or about $14,000 a year. The adequacy of retirement income is often measured by replacement rates – the percent of prior earnings that benefits replace. By international standards, U.S. Social Security replacement rates are modest. The Organization for Economic Cooperation and Development (OECD) found that U.S. replacement rates rank near the bottom among its 30 member countries. U.S. replacement rates were 4th from the bottom for low-earning workers (at 50 percent), 5th from the bottom for average earners (at 39 percent), and 9th lowest for high earners (at 28 percent).

Social Security Replacement Rates* in OECD Countries by Earnings Level



*Illustrative workers are assumed to draw benefits from each country's mandatory pension program at the normal retirement age. Low earners earn half of the average wage, while high earners earn twice the average wage.

Source: Organization for Economic Cooperation and Development (OECD). (2005). Pensions at a Glance: Public Policies across OECD Countries. Paris: OECD.

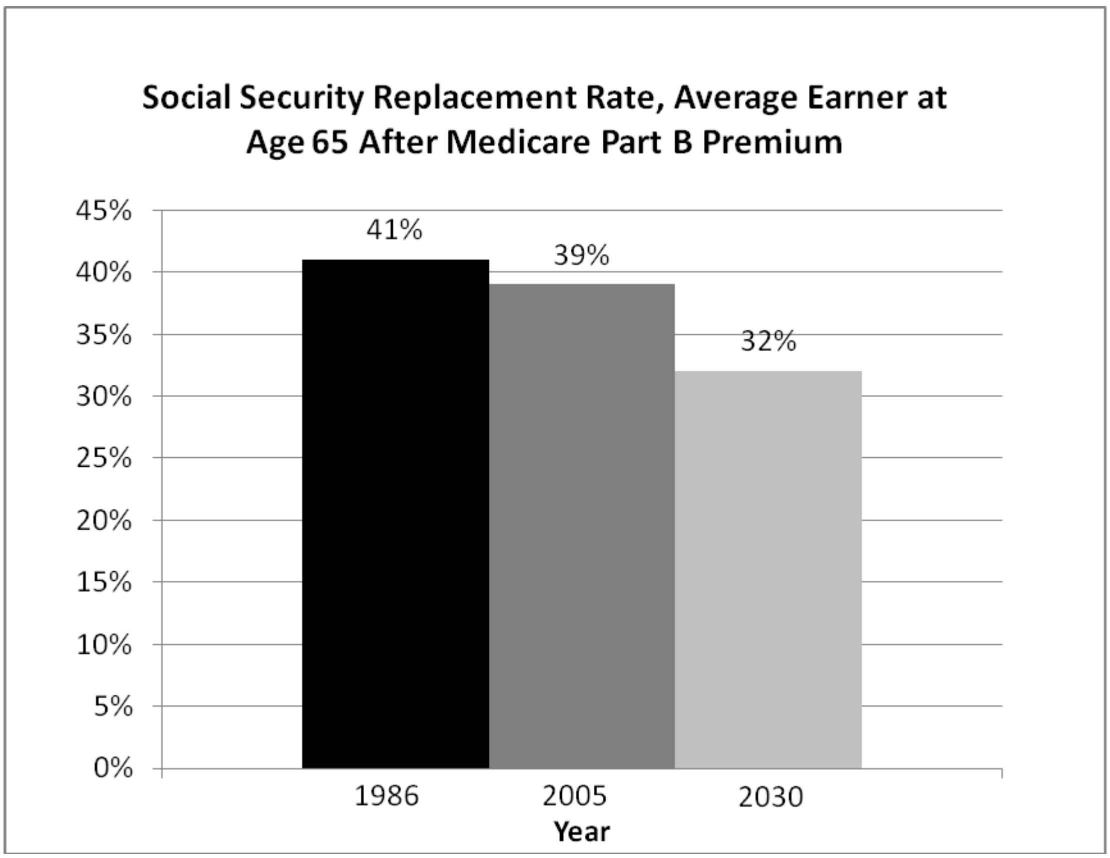
Social Security Replacement Rates Will Be Less Adequate in the Future

Social Security replacement rates have been stable for the past 30 years, but net replacement rates will gradually decline in the future for two reasons.

- First, Medicare part B premiums that are taken directly out of benefits will take a bigger bite in the future because those premiums go up with the cost of health care, which is projected to rise faster than Social Security benefits.

- Second, in 1983 Congress scheduled a gradual increase in the age for receiving full benefits from 65 to 67. The change is fully effective for people born after 1960. It lowers retirement benefits at any age they are claimed.

For an average earner retiring at 65 in 2005, benefits after Medicare Part B premiums replaced about 39 percent of earnings. That replacement will fall to 32 percent by 2030, a reduction of nearly one fifth.



Source: Munnell, Alicia H. and Steven Sass. (2006). *Social Security and the Stock Market: How the Pursuit of Market Magic Shapes the System.* Kalamazoo, MI: W.E. Upjohn Institute for Employment Research: page 12.

Americans Would Rather Pay More Than See Benefits Cut

Americans' support for Social Security transcends partisan politics. Opinion polls over the years have found that working Americans would rather pay somewhat more for Social Security than see benefits cut. A recent survey by the National Academy of Social Insurance and the Rockefeller Foundation found that Americans are willing to pay for Social Security because they value it for themselves (72%), for their families (75%) and for the security and stability it provides to millions of retired Americans, disabled individuals, and children and widowed spouses of deceased workers (87%). Large majorities of Democrats, Republicans, and Independents said they are willing to pay for Social Security for each of these reasons, as shown below.

Reason Don't Mind Paying Social Security Taxes by Party Affiliation

I'm going to read a list of statements and after each one, please tell me if you agree, or disagree with the statement. "I don't mind paying Social Security taxes because:
Q. 30: I know that I will be receiving the benefits when I retire."
Q. 31: I know that if my parents, grandparents, or other family members did not receive Social Security, I would have to support them in their retirement."
Q. 29: It provides security and stability to millions of retired Americans, the disabled, and the children and widowed spouses of deceased workers."

Reason don't mind paying Social Security taxes	**Total**	**Democrats**	**Independents**	**Republican**
Total (number of interviews)	1488	497	601	390
Total percent	**100**	**100**	**100**	**100**
	Percent who strongly or somewhat agree			
I will be receiving it when I retire	72	84	69	63
If they did not receive it, I would need to support parents, grandparents, or other relatives	75	82	76	68
It provides security and stability to millions of retired Americans, the disabled, and children and widowed spouses of deceased workers	87	93	85	81

Source: Social Security Survey sponsored by the National Academy of Social Insurance and the Rockefeller Foundation, July-August 2009.

Americans support Social Security even in the face of federal deficits and short-term economic hardship. In response to a forced choice question about how Social Security policy should respond to the economic downturn, Americans favor strengthening Social Security (66 percent) over cutting taxes and spending (28 percent) by more than a two-to-one margin (See *Economic Crisis Fuels Support for Social Security: Americans' Views on Social Security*, August 2009).

Americans Support Targeted Benefit Improvements

The survey found that Americans support improving Social Security benefits for vulnerable groups. For example:

- 78 percent support extending benefits to "children whose working parents have died or become disabled from the current cutoff of 19 years to 22 years old if the child is in college or vocational school."

- 76% support "increasing benefits by $50 a month for recipients over the age of 85 because they generally depend more heavily on Social Security."

- 76% support "improving benefits for widowed spouses of low income working couples who generally have inadequate benefits from life-long low-paid work."

- 69% support "guaranteeing that Social Security benefits for steady workers exceed the poverty line, even if workers receive early benefits at the age of 62."

- 64% support "counting time that working parents take off to care for children toward workers' future benefits so they do not receive lower benefits because of this gap in paid work."

History Offers Innovative Solutions to The Long-Term Shortfall

Social Security faces a shortfall 25 years from now because we lack a 75-year revenue plan to match the modest increase in outgo that will occur as boomers retire and Americans live longer after age 65. Through most of its 75-year history, Social Security has had one or more tax rate increases scheduled out in the future to keep it in balance. That ended in 1990.

Policymakers could act now to create a 75-year revenue plan. One such plan is shown below. It would:

- Gradually restore the taxable wage cap to cover 90 percent of all earnings;
- Treat all salary-reduction plans like 401(k)s – i.e., employee contributions would remain exempt from income taxes but would become subject to FICA for workers and employers; and
- Schedule future FICA rate increases out in the future when funds are needed.

A 75-year Revenue

Option #	Policy Options	% of taxable payroll (2.00% deficit)
8d	Gradually restore the taxable earnings cap (now $106,800) to cover 90 percent of wages	0.57
10	Treat all salary reduction plans like 401(k)s – i.e., employee contributions would remain exempt from income taxes but would be subject to FICA from workers and employers	0.25
7b	Schedule future FICA rate increases for Social Security out in the future: from 6.2% to 7.2% in 2022 and to 8.2% for workers and employers each in 2052	2.06

Source: Reno, Virginia P. and Joni Lavery. (2009a). *Fixing Social Security: Adequate Benefits, Adequate Financing*. Washington, DC: National Academy of Social Insurance: pages 13-19 and page 29.

The first two changes broaden the revenue base for Social Security. They reflect the intent of Congress expressed in the past. In 1977, Congress set the cap to cover 90 percent of earnings and indexed the cap to keep up with average wages thereafter. But the cap fell behind because wages for the 6 percent of workers who earn more than the cap grew faster than wages of other workers. In 1983, Congress explicitly decided that employee's tax-deductible contributions to 401(k) plans would be subject to FICA because Congress did not want these plans to erode the revenue base for Social Security and Medicare. That logic can also apply to "salary reduction plans" that are becoming more widespread today with regard to money employees set aside for medical care, dependent care, and commuting to work costs.

While Social Security does not need higher FICA contributions now, policymakers could act now to schedule rates out in the future when the forecast suggests that funds will be needed – say in 12 years, and again in 40 years, or even 60 years. To offset the FICA increase for low-paid workers, policymakers could adjust the earned income tax credit (EITC). If it turns out that the funds are not needed, future Congresses could reduce the scheduled FICA rates. In the meantime, scheduling future funds to cover current benefits and modest benefit improvements would be good policy. It would:

- Assure working Americans that Social Security benefits will be paid in full and on time for the next 75 years as they have been for the past 70 years;
- Bolster confidence in our capacity to deal with more difficult budget challenges outside of Social Security; and
- Let American workers know that policymakers are listening to what they say – they would rather pay somewhat more than see Social Security benefits cut.

In this case, good policy is good politics. It matches what people say they want. Thank you for the opportunity to share our research with you. I will be happy to answer any questions and to help you and your staff in any way we can. Our reports are available on our website www.nasi.org.

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