State Supplemental Social Security

John Burbank, Economic Opportunity Institute
Aaron Keating, Economic Opportunity Institute

Submitted as part of the Social Security Policy Innovations Challenge

December 2019
State Supplemental Social Security

Social Security provides sufficient income to keep more than 90 percent of seniors above the federal poverty level. Without it, 22.1 million more Americans would live in poverty, according to an analysis of the March 2018 Current Population Survey.\(^1\)

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Percent in Poverty Excluding Social Security</th>
<th>Percent in Poverty Including Social Security</th>
<th>Number Lifted Above Poverty Line by Social Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children Under 18</td>
<td>19%</td>
<td>17.5%</td>
<td>1,106,000</td>
</tr>
<tr>
<td>Adults Ages 18-64</td>
<td>14.1%</td>
<td>11.2%</td>
<td>5,629,000</td>
</tr>
<tr>
<td>Elderly Age 65 and Over</td>
<td>39.2%</td>
<td>9.2%</td>
<td>15,333,000</td>
</tr>
<tr>
<td>Total, All Ages</td>
<td>19.1%</td>
<td>12.3%</td>
<td>22,068,000</td>
</tr>
</tbody>
</table>

Source: Center on Budget and Policy Priorities, based on data from the Census Bureau Current Population Survey, March 2018

By itself, however, Social Security is insufficient for a dignified retirement, especially as it fails to cover the increasing costs for health care and other basic needs associated with aging.\(^2\) The average monthly benefit is just $1,413 – yet among Social Security beneficiaries over age 65, 48% of married couples and 69% of unmarried persons receive 50% or more of their income from Social Security.\(^3\)

Notionally, workers have been expected to rely on private, employer-sponsored plans and individual savings to fill the gap between what Social Security provides and what they need to be economically secure, but in practice, such plans most often fall short.\(^4\)

According to the Federal Reserve’s 2017 Survey of Consumer Finances (SCF), only 27 percent and 33 percent of households have defined-benefit and defined-contribution plans, respectively, at their current jobs – and in total, just 56 percent of households have an employer-sponsored pension plan (ESPP) associated with their current or previous


\(^2\) The Center for Retirement Research at Boston College estimates that a middle-income two-earner couple born between 1960-1962 will need to replace 76 percent of their income excluding health care and long term care costs, and 98 percent including these costs. See: Center for Retirement Research at Boston College, Long-Term Care Costs and the National Retirement Risk Index, Issue Brief No. 9-7, March 2009.


employment. Among households that do not have an ESPP, only 20 percent utilize any IRAs or Keogh accounts.\(^5\)

Even among those households that do hold retirement accounts, the SCF finds many have low account balances. The median (50th percentile) household of all ages holds only $1,100 in its retirement account. Even the 70th and 80th percentiles of households have only about $40,000 and $106,000 in their retirement accounts, respectively. Among pre-retirement households (headed by people ages 56-61) that have a positive retirement account balance, the median value is only around $25,000.

This paucity of retirement savings is compounded by a lack of household savings, as shown below.\(^6\) For the vast majority of pre-retirees, the retirement stool does not have three legs, but one: Social Security.

The result is that many workers are at risk of living out their retirement years in or close to poverty, with a diminished quality of life. But it doesn’t have to be this way.

---


\(^6\) Source: Federal Reserve, FDIC, and Magnify Money estimates, June 2019. Cohorts with median balance of $0 indicate more than 50% of these households have no savings.
Proposal: Main Concept

Supplemental Social Security programs, funded and operated by states, can provide additional benefits on top of federal Social Security payments. While the impact in individual states will vary depending on economic and demographic circumstances, overall such a program would particularly benefit:

- **Workers who lack access to, or do not participate in, a workplace-based retirement plan:** Thirty-five percent of private sector workers age 22 and older do not work for an employer that offers a defined contribution plan or a traditional defined benefit plan.7 Less than half of nongovernment workers in the United States participated in an employer-sponsored retirement plan in 2012, the most recent year for which detailed data were available.8

- **Workers who have to retire early:** More than 4 in 10 retirees retire earlier than they had anticipated – most often because of a health problem or disability, or changes at work such as a downsizing or workplace closure.9 For every month a person claims their Social Security retirement benefit before reaching full retirement age, their initial monthly benefit is permanently reduced.10

As shown below, lower-income workers tend to retire earlier than those with higher incomes: average labor-force participation rates for those age 55 and above are lowest for those with a high school diploma or less, and highest for those with a BA degree or more. (While education isn’t a perfect proxy for lifetime earnings, the two are highly correlated.) This represents an overall reduction in lifetime benefits – especially for workers in physically demanding jobs, or for whom life expectancy is lower than average due to socioeconomic or other circumstances.

---


10 The earliest age at which Social Security retirement benefits can be claimed is 62 years. The full retirement age is 67 years for those born in 1960 or later. Benefits are reduced by five-ninths of 1% per month (6 2/3% per year) for up 36 months before full retirement age, and by five-twelfths of 1% per month (5% per year) for every month beyond 36 months. See: Social Security Administration, Benefit Reduction for Early Retirement, [https://www.ssa.gov/OACT/quickcalc/earlyretire.html](https://www.ssa.gov/OACT/quickcalc/earlyretire.html).
Households with limited savings: If faced with a $400 emergency expense, four in 10 adults would either borrow, sell something, or not be able to pay; more than one in six adults are not able to cover their current month's bills, and one in four skipped necessary medical care in the past year due to an inability to pay. One in four participants in defined contribution plans taps into some or all of such plans for non-retirement needs.

Expected cost of proposal, including its impact on the long-term financing of Social Security

Costs would vary according to the level of benefits. For example, in Washington, a total payroll premium of 1.8% (0.9% employee, 0.9% employer) – with no cap on taxable wages, so as to capture the outsized growth in wages at the top end of the income spectrum, would generate about $4.3 billion in 2021, enough to finance inflation-indexed lifetime benefits of:

---


• 1.5% of a worker’s federal Social Security benefit for each year a worker pays state Supplemental Social Security premiums (up to 30% of their federal benefit); or
• $1000/year for all currently retired workers, and an additional benefit of $400/year for each year a worker pays state premiums (up to $4,000 total). This which would increase the redistribution and equity impact of benefits, particularly for current and future low-wage and manual workers who have, or will soon be, forced into early retirement.

The excerpt below from our preliminary financial forecast sketches an initial financial pathway in Washington for the first option noted above. Of public financing interest: note the significant trust fund development (in the hundreds of billions of dollars), which could be invested in state and local bonds for infrastructure projects and capital construction, as well as private investments.

<table>
<thead>
<tr>
<th>Year</th>
<th>PREMIUM</th>
<th>BENEFIT</th>
<th>FINANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Average yearly wage</td>
<td>Average yearly premium (worker share)</td>
<td>Years of premiums paid</td>
</tr>
<tr>
<td>1</td>
<td>$67,641</td>
<td>$609</td>
<td>0</td>
</tr>
<tr>
<td>5</td>
<td>$74,348</td>
<td>$669</td>
<td>4</td>
</tr>
<tr>
<td>10</td>
<td>$83,892</td>
<td>$755</td>
<td>9</td>
</tr>
<tr>
<td>15</td>
<td>$95,137</td>
<td>$856</td>
<td>14</td>
</tr>
<tr>
<td>20</td>
<td>$108,603</td>
<td>$977</td>
<td>19</td>
</tr>
<tr>
<td>25</td>
<td>$124,891</td>
<td>$1,124</td>
<td>24</td>
</tr>
<tr>
<td>30</td>
<td>$145,059</td>
<td>$1,306</td>
<td>29</td>
</tr>
</tbody>
</table>

Revenue collection would take place via a payroll premium (paid by employers, or split between employer and employee). Most states have such a mechanism already in place, whether for unemployment insurance, temporary disability, income taxes, or a similar system. Every worker (including sole proprietors and the self-employed) would contribute. Assets would be pooled by the state and invested through each state’s investment board (such as the Washington State Investment Board) which manages state retirement and public funds.

Another (more redistributional) approach is a payroll premium applied only to wages above the Social Security ceiling of $133,000 – above which employers do not pay Social Security payroll tax, nor Washington state Paid Family and Medical Leave premiums. This amounts to 6.35% of payroll for employers, or $2.4 billion in revenue in 2021. (Data from Washington state Employment Security Department). Employers of five percent of employees in Washington would pay this premium, and revenue would total 55% of total anticipated from the 1.8% universal payroll premium suggested elsewhere in this brief.
Since Supplemental Social Security is funded at the state level, it would not have a direct impact on the long-term financing of federal Social Security. However, a Supplemental Social Security program can reasonably be expected to provide economic benefits much like federal Social Security, where every dollar paid out translates to almost two dollars in additional spending.\textsuperscript{15} The resulting economic activity will generate additional federal revenue for Social Security, through the FICA contributions of workers employed through additional economic demand created by State Supplemental Social Security.

For example: in Washington, a state supplemental Social Security benefit equivalent to 20% of annual federal Social Security benefits received by residents would generate approximately $7.9 billion in economic activity, inclusive of more than 50,000 jobs – resulting in over $2 billion in additional employee compensation and additional FICA tax collections of approximately $258 million each year.\textsuperscript{16}

**Shortcomings of existing state policy efforts**

The retirement security policy approaches that have been examined or adopted by states so far – such as Auto-IRAs, small-business marketplaces, publicly-administered defined contribution plans, and Hybrid/MEP vehicles – all share the same goal: ensure workers have access to a retirement plans at work, and by extension, a greater degree of economic security in retirement.\textsuperscript{17} However, these policies have yielded mixed results. A review of Oregon’s auto-IRA program – called OregonSaves – highlights several such shortcomings.

OregonSaves is considered one of the most successful such state-facilitated retirement initiatives so far. It seeks to provide a retirement savings vehicle to more than 1 million workers (60 percent of the workforce) who lack access to an employer-sponsored retirement savings plan.\textsuperscript{18} Since full rollout (following a 2017 pilot program), OregonSaves has added an average of nearly 2,000 actively contributing employees per month. As of November 2018, approximately


22,000 workers in the program had balances in their accounts, totaling more than $10 million in assets.\textsuperscript{19}

But Oregon’s approach has significant drawbacks, especially in comparison to Supplemental Social Security:

**Limited participation:** One-third of eligible workers have chosen not to participate in OregonSaves – either by formally opting out of the program (29 percent), or setting contributions to zero (4 percent). These workers offered three main reasons for doing so: 30 percent said they could not afford to save, 19 percent said they had their own or another retirement plan (e.g. through a spouse), and 12 percent said they did not want to save through this particular employer.

**Significant pay reductions:** Participation in OregonSaves represent a sizeable reduction in pay, especially for low- and middle-income workers. The standard savings rate is substantial: 5% of gross pay, deducted on an after-tax basis, with a 1% annual increase in savings up to 10%. (Participants can reduce their savings rate at any time to as little as 1% or as high as desired, subject to IRS limits.)

**High fees:** OregonSaves collects an annual asset-based fee of approximately 1% (approximately $1 for every $100 in a participant’s account) to pay for program administration and the operating expenses charged by the underlying investment funds in which the program’s portfolios are invested. This is an extraordinarily high fee. In 2018, industry-wide fees for actively managed funds fell to an average 0.67%, and for passive funds, to 0.15% overall.\textsuperscript{20}

Since the OregonSaves fee is taken annually as a percentage of the portfolio’s value, the larger the portfolio, the more the investor pays. By comparison, Vanguard – an acknowledged industry leader in low-cost investing – charges only a $20 annual fee for fund accounts with a balance under $10,000.\textsuperscript{21}

**Greater financial risk:** OregonSaves offers no guarantees to participants. Its primary savings vehicle is a Roth IRA – and building a substantial retirement fund in a defined contribution, 401(k)-style plan hinges on many factors that are outside of a worker’s control or expertise, including:

- being provided low-fee investment options that match employee needs,
- making adequate contributions, choosing appropriate investments,
- following a structured withdrawal plan,
- exposure to ups and downs of the financial sector (and therefore the value of their account),


\textsuperscript{21} Vanguard, “Vanguard mutual fund fees & minimums”, \url{https://investor.vanguard.com/mutual-funds/fees}.
Limited portability: A person changing jobs to another employer utilizing OregonSaves can continue to participate in the program by payroll deduction. However, if the employer doesn’t have that connection, the worker must initiate the process of making their own contributions, or initiate a roll over or transfer to an IRA outside of OregonSaves, if that IRA will accept it.

Low social equity: OregonSaves reinforces and carries inequitable income distributions into retirement, with more affluent workers able to save much more for retirement, while low wage workers save relatively little, even if they save a higher percentage of their income.

Advantages of State Supplemental Social Security

State-based policy efforts like OregonSaves are only able to offer an incremental improvement – and for only some workers – due to a fundamental policy limitation: they are designed to promote and facilitate individual workplace-based retirement savings plans. As such, and in order to avoid entanglements with the federal Employee Retirement Income Security Act (ERISA), they are built on worker-only defined contribution models that rely upon individual investments in speculative asset markets.

By contrast, a state Supplemental Social Security program is designed as social insurance for all workers who have paid premiums once a triggering event has occurred – such as turning 65 years of age. This avoids ERISA issues, and offers a number of other significant policy advantages, including:

- universal coverage (all workers pay premiums and are eligible for benefits),
- full portability from job to job (all employers required by state to participate),
- lower fees due to administrative advantages (estimated at 0.4%)23,
- progressive benefits (with coverage for survivors and/or dependents), and
- professionally-managed assets, pooled to minimize both fees and risk.

Start-up costs for Supplemental Social Security could be financed by the state, or via a federal grant. The federal Social Security Administration (SSA) could also provide technical assistance to states in preparing and review projected finances for their programs, again financed via a federal grant. It’s also possible states could partner with the SSA for benefits disbursement, as is the case with many State Supplements to federal SSI benefits.24 Such a partnership would also help track participants who move out of state.

---

22 This is similar to Washington’s Family and Medical Leave Insurance program, which collects a shared premium from both employers and workers. Premiums are paid in the event of a triggering event, such as the birth or adoption of a child, or off-the-job injury or illness that prevents an employee from working.

23 Universal participation and the absence of means-testing make federal Social Security very efficient to administer: administrative costs for non-disability benefits amount to only 0.4 percent of total annual benefits. See: https://www.ssa.gov/OACT/STATS/admin.html. The cost for states to administer their programs would be similarly low, especially done by or in partnership with the federal Social Security Administration (SSA).

The Washington State Investment Board (WSIB) would provide the investment vehicle(s) for state Supplemental Social Security premiums. WSIB has 8.77% annualized for the past 27 years, and 10.31% for the past ten years. This can be compared to Social Security Trust Fund returns of 2.9% in 2018. Confirm that your proposed concept would not adversely impact the existing DI system and, if needed, provide detailed back-up.

To limit potential negative interactions between State Supplemental Social Security and federal Disability Insurance, states should disburse the Supplemental Social Security benefit upon commencement of either federal disability insurance or old age insurance payments, with no penalty to a worker for doing so as the result of a successful disability claim before full retirement age.

Connections to and Focus on Existing Policy at the Federal Level

When federal Social Security was enacted in 1935, 28 states were operating their own “old-age pension” programs. Colorado and Alaska still fund and administer programs for low-income seniors today. Supplemental Social Security can be initiated in one state, spread to others, and eventually be federalized, especially when a large sector of the American workforce and retiree populations will already be benefitting from it. Further, the widespread understanding of and support for federal Social Security means such a proposal at the state level will be fairly easy for people to grasp and to support.

Today, the policy skirmishes around Social Security often focus solely on federal power (and more often, result in gridlock), which stymies policy innovation and diminishes both public morale and political will to advance public policies that buttress and build social insurance systems. Incubating Supplemental Social Security at the state level makes it possible to avoid beltway politics while leveraging the sense of what is possible from state-level advances in Washington and elsewhere.


27 The federal process (put simply) is: if a person files for and receives disability insurance at any age (prior to filing for old age benefits), their benefit is calculated at full retirement age – the age at which that individual qualifies for 100 percent of the benefit amount determined by lifetime earnings – using a shorter AIME (average indexed monthly earnings) period. At full retirement age, the disability benefit automatically converts to a retirement benefit, in most cases at the same amount. The outcome for an individual doing the opposite – claiming retirement benefits early, then SSDI – depends on the status of their disability claim. If rejected, the individual’s retirement benefit will be reduced for life. See: “Can you switch from Social Security retirement benefits to disability benefits?”, AARP, https://www.aarp.org/retirement/social-security/questions-answers/retirement-to-disability/.

Passage of state Supplemental Social Security programs will support and bolster federal Social Security by demonstrating the political appetite of workers for improving their retirement security, and by making a positive, proactive case for the role of government in doing so. Building a growing network of states successfully advancing state Supplemental Social Security provides the foundation for eventual federalization. Individual states might also enact specific benefits that the federal government has reduced or eliminated, such as survivor benefits for children until age 22 for full-time students.

Supplemental Social Security would provide additional retirement/old-age insurance, in addition to federal benefits. The state benefit can be structured as a percentage of a retiree’s federal Social Security benefit, a flat amount based on the number of years a worker has contributed premiums to the state program, or a combination of the two. The benefit could at a minimum completely offset Medicare Part B withdrawals from monthly Social Security checks, which total $1,626 a year.  

Supplemental Social Security benefits would be taxable. As such, certain high-income households may find some of their income subject to the “taxation of benefits provision” of Social Security. However, this would not impact the vast majority of beneficiaries. Under current law, taxation kicks in for single beneficiaries with incomes in excess of $34,000 and couples with incomes in excess of $44,000. Many seniors do not earn enough to pay federal income tax – more than 80 percent of those age 75 or older are non-payers.  

Since Washington (unlike most other states) presently has no state income tax, there would be no tax implications in that state. But even if it did – and in those states that do have an income tax – the overall economic security of these higher income retirees (who would pay the tax) as well as those of other, lower-income workers – will be enhanced by the guaranteed, predictable and progressive benefits provided by a Supplemental Social Security program, as will the redistributional aspects of progressive taxation.

**Practical and Easy to Implement With or Without Federal Support**

The federal government can play a significant role in promoting state Supplemental Social Security programs through grants that support start-up costs, as well as partnerships for benefits administration, actuarial/financial projections, and by providing other expertise. The run-up to the 2020 election – with a large field of candidates seeking to distinguish themselves from others with innovative policy ideas – offers potentially fertile political ground to plant the seeds for federal support of this state-level innovation.

But even absent proactive federal support, the states are the laboratories for democracy, and we can plant the seeds now for fruition at the federal level within the next decade. If even one

---

29 2019 Medicare Part B premiums
state passes a Supplemental Social Security program, voters and policymakers in other states will take notice, and endeavor to do the same.

Washington is an excellent place to undertake this policy initiative, and from which to spread this innovative policy to other states and eventually the federal government. This approach is similar to the EOI’s approach on paid family and medical leave, in which our policy director is now looked to across the country and in our nation’s capital for expertise in family and medical leave policy, as developed at both the state and federal level.

The state recently passed and is now implementing paid family and medical leave insurance (FMLI) with progressive benefits: low-wage workers receive 90% of their previous compensation for 12 weeks, middle wage workers receive 70%, and high wage workers receive a maximum of $1,000 a week. Benefits begin January 1, 2020, financed through a shared premium of 0.4% of payroll. EOI was the central and catalytic organization in developing and realizing this state law for a progressive expansion of social insurance. Since passage, the states of Massachusetts, Connecticut, and Oregon have passed iterations of paid family and medical leave based on Washington’s policy template.

In addition, the Washington state legislature recently passed a long-term care (LCT) program, which provides a monetary benefit of $100 a day, for a full year, for workers and retired workers in need of long-term care, with the intent to enable retirees to remain in their own homes. The payroll premium for this program is .58%, contributed solely by workers.

Supplemental Social Security will build on both these platforms for implementation and administration: in particular the mechanism for collecting employee and employer FMLI premiums, and the framework created by the LTC Trust Program, which (via the Trust Commission) provides for joint administration of the LTC program by the Department of Social and Human Services, the Employment Security Department, the Health Care Authority, and the Office of the State Actuary.

The Economic Opportunity Institute is a key state organization in a number of multi-state networks, and as such has the ability to provide expertise and insight to other states which may be interested in replicating future success with Supplemental Social Security. Our existing coalitions can provide a starting point for the organizing and activism necessary for state Supplemental Social Security. Several prominent labor unions have already indicated interest, and we have begun outreach to other organizations as well.

**Innovative and Timely**

What is most innovative about Supplemental Social Security is that it does not try to substitute a private good (the private financial services sector) for a public one (economic security and dignity in retirement). Such substitutions primarily benefit the financial industry – and only secondarily, and with no guarantees, participating individuals. Our innovation is to build on an already overwhelmingly popular federal program with a state supplement that insures people against the risks of an uncertain economic future with a guaranteed benefit, without exposing workers and retirees to the vagaries of financial markets.
Developing and building the necessary grassroots support for Supplemental Social Security will reinforce the central and critical role of government in promoting broad-based economic security. In so doing, it will help rebuild the social contract and social wages of employment, by filling the void left by employers’ decisions to limit (or outright end) their larger social responsibilities for their employees and communities, especially in regard to pensions.

Social Security’s benefits are critical for the economic security of the nation’s retirees – and given the decreasing number of Americans covered by employer-sponsored retirement plans, its importance will only grow in the future. Yet federal efforts to expand and/or improve Social Security have been stymied by increasing antagonism toward social insurance programs: the only significant recent federal policy initiative on Social Security was the regressive (and ultimately unsuccessful) push to partially privatize the system in 2004-05, by then-president George W. Bush.

Given the nation’s demographic trends (with liberal/progressive populations concentrating in urban centers) and the profoundly undemocratic structure of the U.S. Senate, it is unlikely any significant nationwide progress in improving retirement security is going to be made at the federal level.

However, a “50-state solution” is possible – and many states have taken steps on that path. Since 2011, some 40 states have enacted or proposed policies designed to help overcome barriers and provide more access to retirement savings accounts for private sector workers. These approaches seek to ensure workers have access to a retirement plan at work, and by extension, enable a greater degree of economic security in retirement. As noted above, these policy innovations offer incremental improvements for some workers, but they simply do not go far enough.

State Supplemental Social Security programs offers numerous advantages over these policies, at a time when four-in-ten Americans say that by the time they retire, Social Security won’t have enough money to provide benefits, and say no cuts should be made to Social Security benefits in the future. American voters also support expanding Social Security: 66% of voters are more likely to back candidates who support expanding and increasing Social Security benefits, vs. 18% who are less likely.

Americans across the political spectrum recognize the need to improve retirement security – and State Supplemental Social Security provides a pathway to ensure all Americans can retire with dignity.