

# Social Security 101



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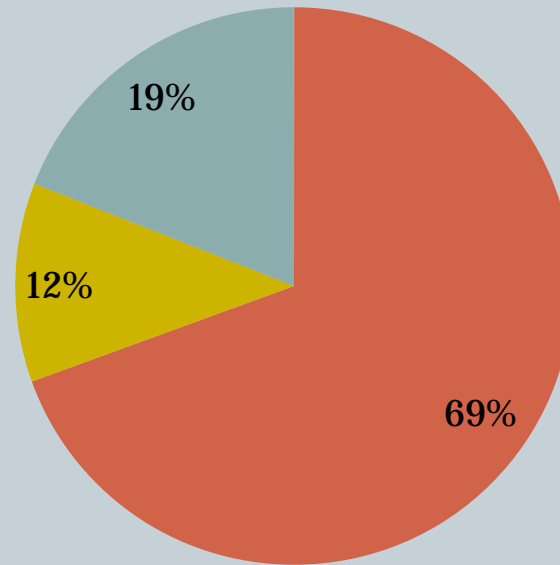
# Social Security Benefits Everyone



# Who Receives Social Security Benefits?



- About **1 in 6 Americans** (55 million people)



■ Retired Workers & Families   ■ Survivors of Deceased Workers   ■ Disabled Workers & Families

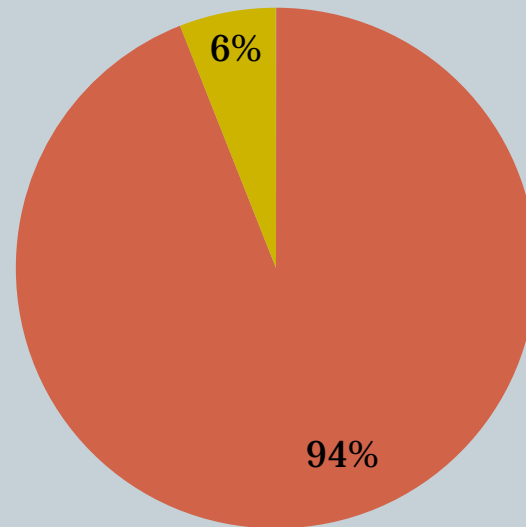
**Source:** Social Security Administration

**Note:** As of June 2011

# Who Pays into Social Security?



- More than **9 in 10 workers** (158 million people)
  - This includes all Members of Congress—so tell your uncle!



■ Covered workers    ■ Uncovered workers

**Source:** Social Security Administration

# How Much?

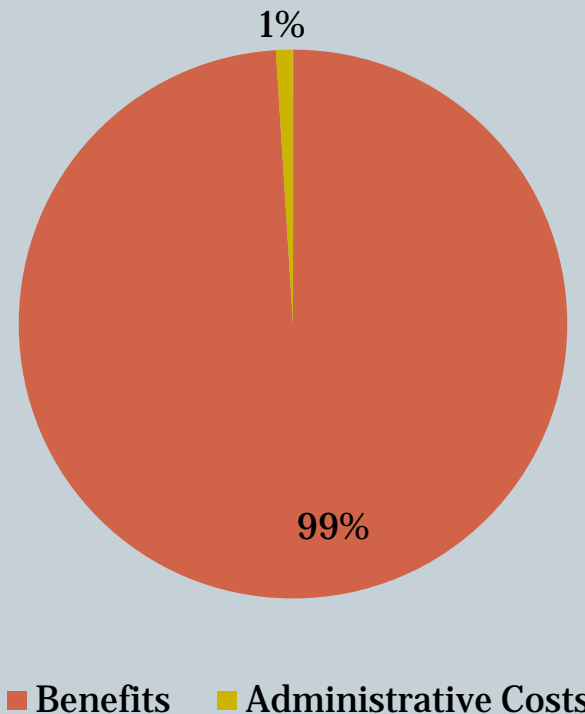


- **Payroll tax rate:**
  - Employers contribute 6.2% of earnings
  - Employees contribute 4.2% of earnings—*for 2011 only*
    - ✦ Typically, employees contribute 6.2%
    - ✦ Solvency and benefit calculation are *not* affected by tax holiday
- **Payroll tax cap:**
  - \$106,800 in earnings for 2011
- **Combined contribution in 2011 (10.4%):**
  - About \$4,000 for an average earner (~\$40,000/yr)
  - About \$11,000 for a maximum earner (\$106,800/yr)

# Where Does the Money Go?



- In 2010, Social Security spending was **\$713 billion**



**Source:** 2011 Social Security Trustees Report, intermediate assumptions

# Social Security Benefits in Perspective



# How Much Do Average Beneficiaries Get?



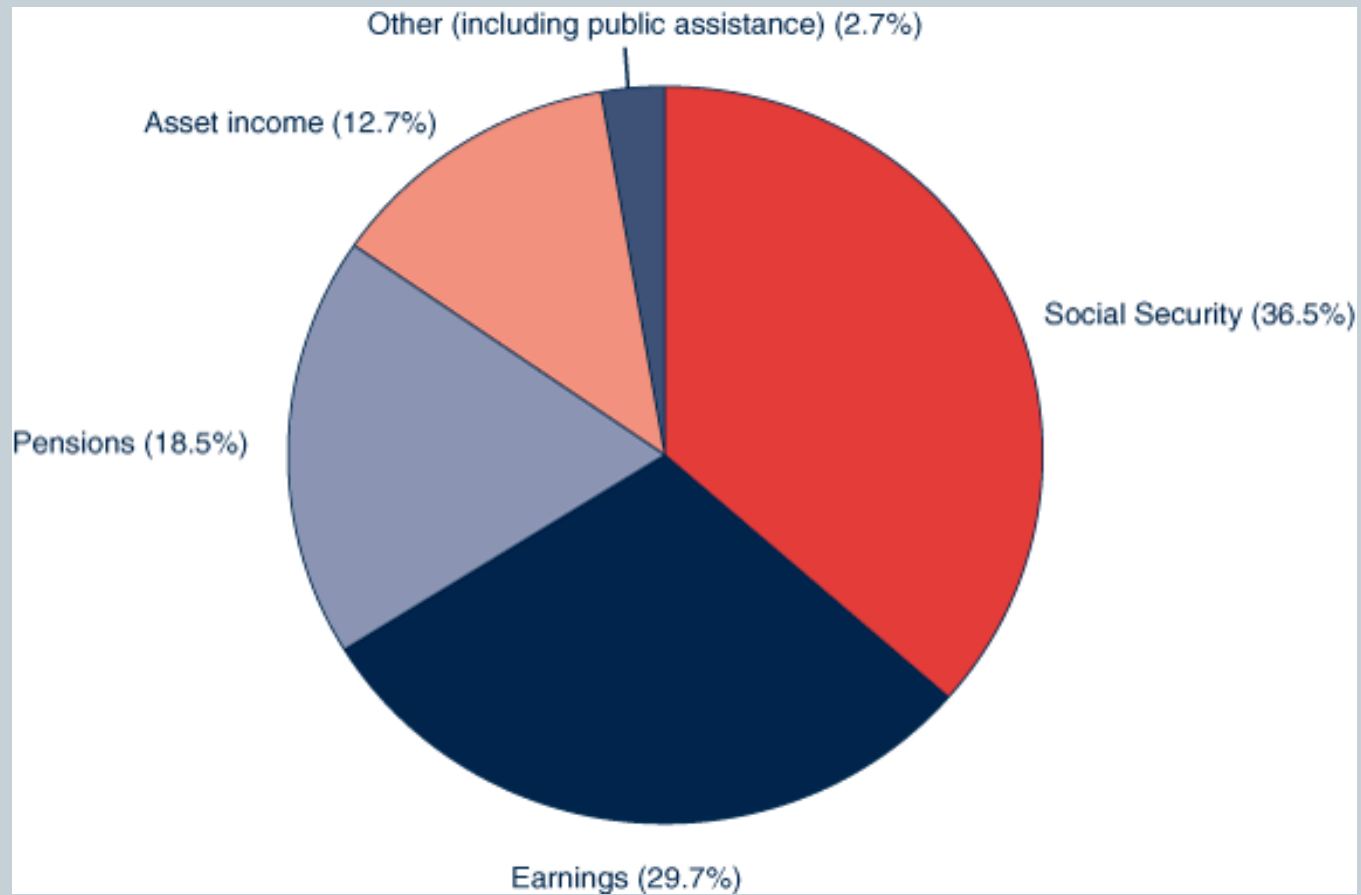
<b>Benefit type</b>	<b>Average monthly benefit</b>	<b>Average annual benefit</b>
Retired workers	\$1,181	\$14,000
Disabled workers	\$1,070	\$13,000
Aged widow(er)s	\$1,139	\$14,000
Surviving children	\$755	\$9,000
<i>Poverty threshold</i>	<i>\$908</i>	<i>\$10,890</i>

**Source:** Social Security Administration

**Note:** As of June 2011

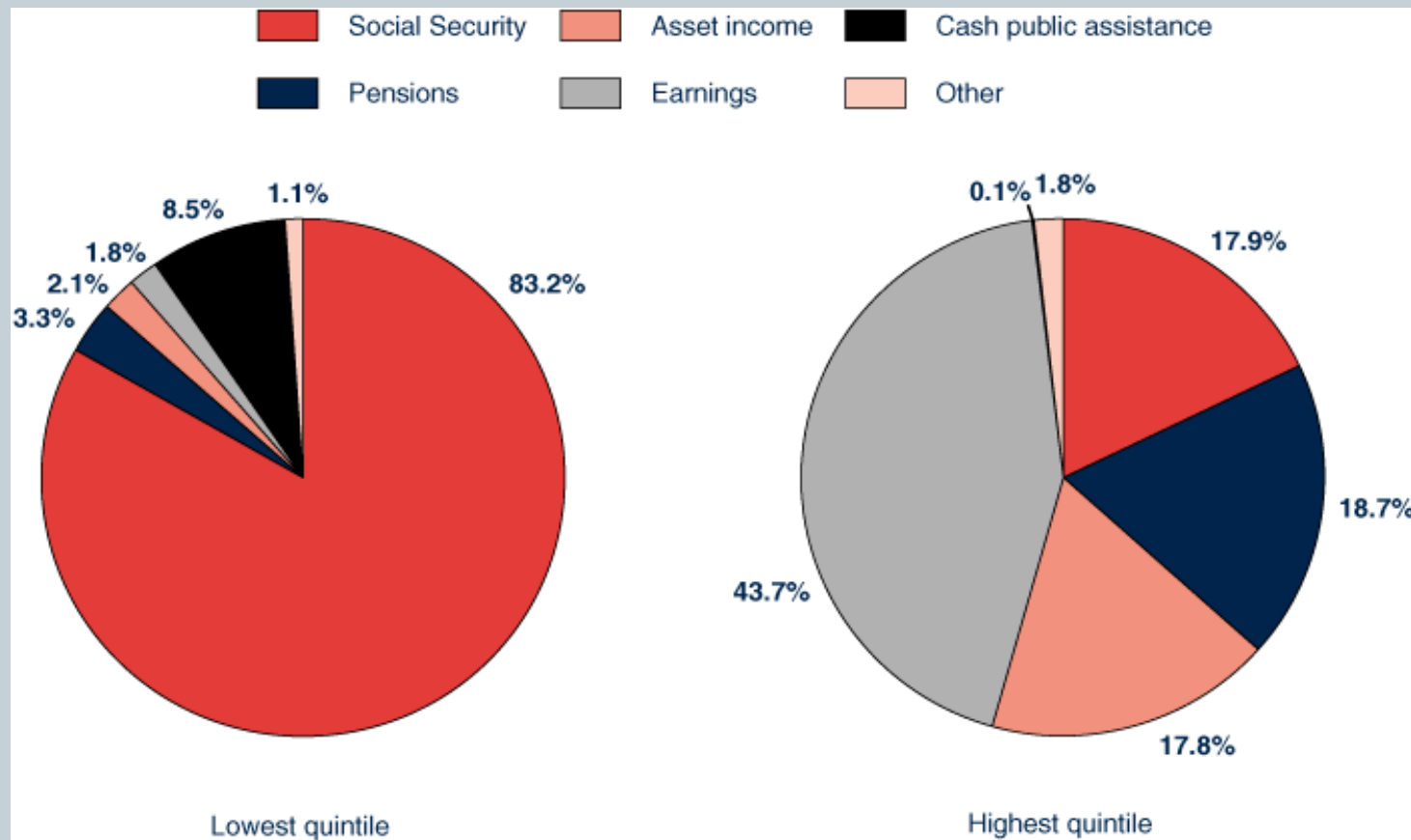


# The Largest Source of Elderly Income



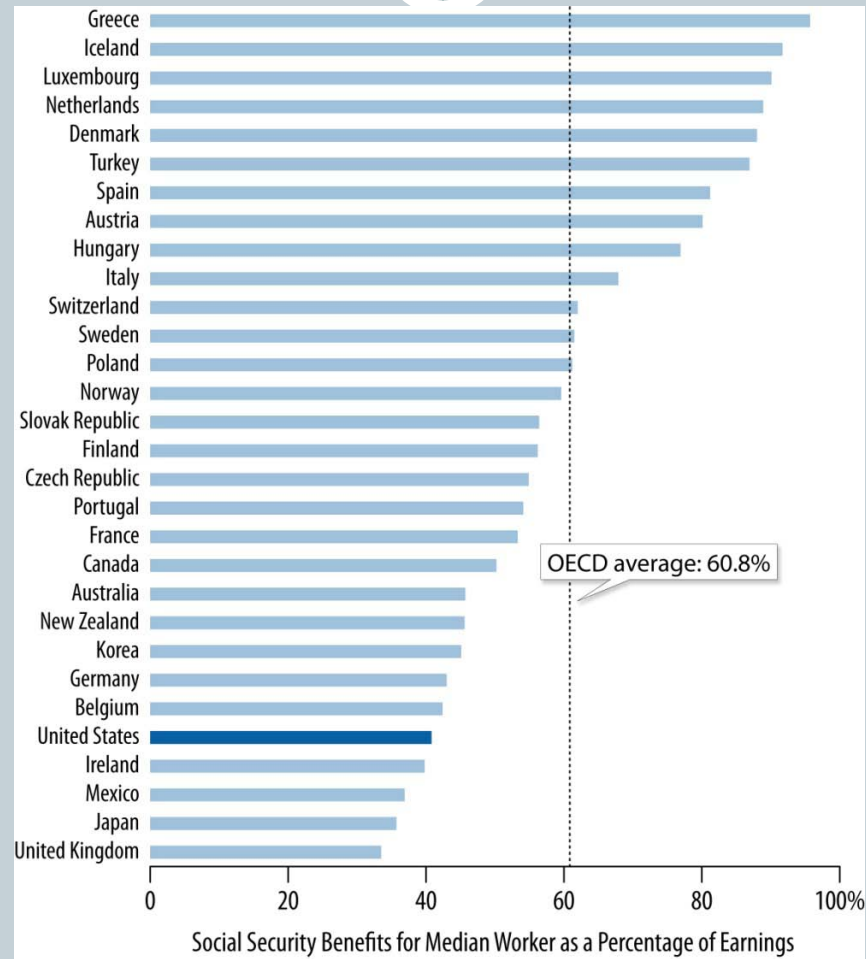
**Source:** SSA, Income of the Aged Chartbook, 2008

# Reliance Varies Widely by Income Level



**Source:** SSA, Income of the Aged Chartbook, 2008

# Replacement Rates Less than OECD Average



**Source:** OECD, *Pensions at a Glance, 2009*, public pensions for median earner

# How Are Benefits Calculated?



# The Basic Benefit Formula (2011)

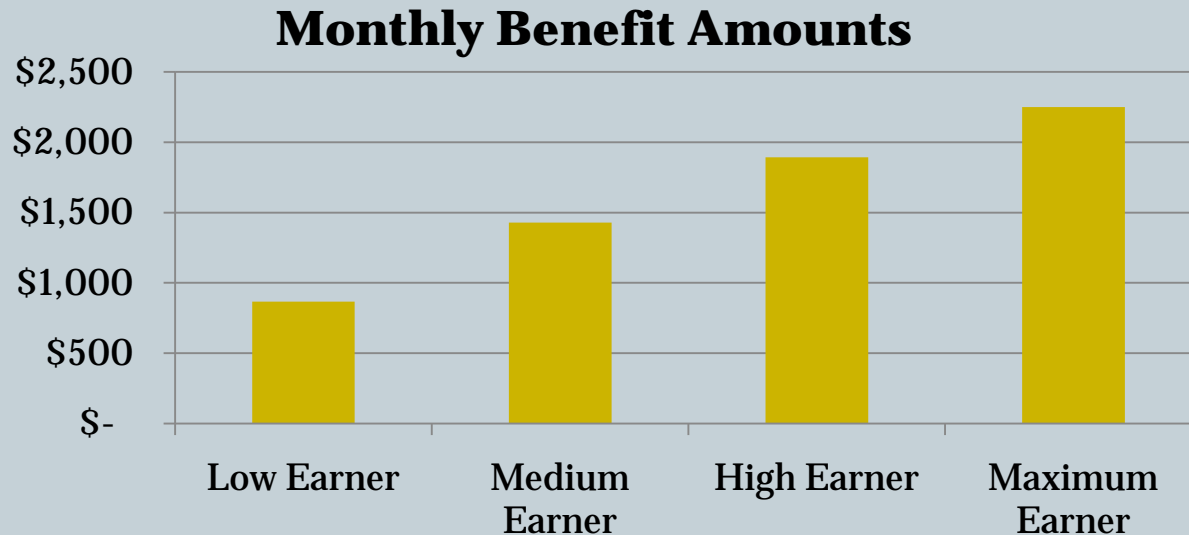


- **Calculate the worker's average indexed monthly earnings (AIME):**
  - Indexed to wages at age 60
  - Average of the highest 35 years of earnings
- **Calculate the basic benefit amount (or primary insurance amount, PIA):**
  - 90% of the first \$749 of AIME, plus
  - 32% of AIME over \$749 up to \$4,517, plus
  - 15% of AIME over \$4,517 (up to the tax max)

# How Does the Benefit Formula Work?



- **Higher earners have greater monthly benefits** than lower earners, since benefits are based on earnings



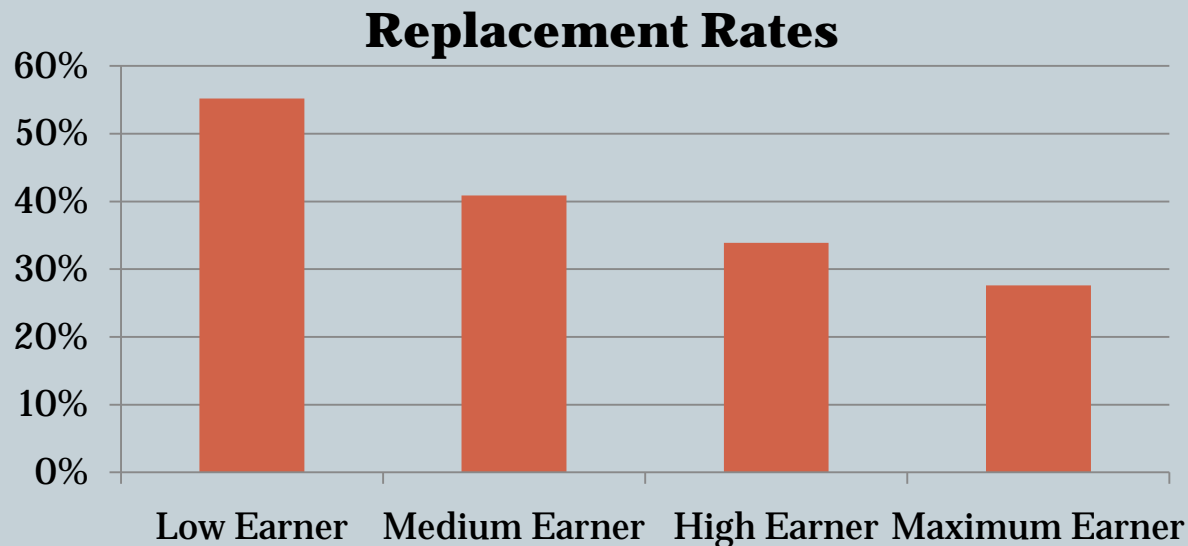
**Note:** Hypothetical scaled earners who turn 65 and retire in 2011

**Source:** 2011 Social Security Trustees Report, intermediate assumptions

# How Does the Benefit Formula Work?



- **Lower earners have higher replacement rates than higher earners, since the benefit formula is progressive**



**Note:** Hypothetical scaled earners who turn 65 and retire in 2011

**Source:** 2011 Social Security Trustees Report, intermediate assumptions

# Wage-Indexing: What It Means & Why It Matters



- ***Initial* Social Security benefits are indexed to wages**
  - In other words, benefits rise with the Average Wage Index
  - Since wages generally rise faster than prices, the standard of living rises with each generation
- **Wage-indexing . . .**
  - . . . allows beneficiaries to reap the benefits of rising living standards.
  - . . . provides a steady replacement rate to new beneficiaries.
  - . . . recognizes that workers' Social Security payroll tax payments increase as their wages rise.



# Cost-of-Living Adjustments (COLAs)



- After the first year, Social Security benefits rise with **inflation**
  - In other words, benefit rise with the CPI-W
  - Currently under discussion: a switch to the chained CPI, which would effectively reduce the cost-of-living adjustment (COLA)
- Annual COLAs . . .
  - . . . allow benefits to maintain **purchasing power** over time

# The Rising Full Retirement Age



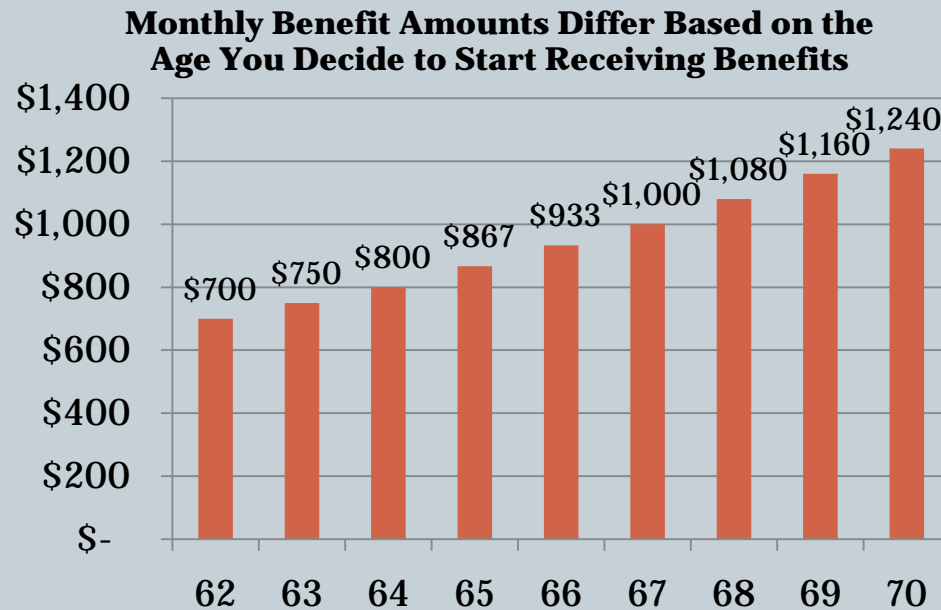
- The **full retirement age (FRA)** is the age at which a person can receive unreduced retirement benefits
  - **65**: The FRA for most of Social Security's history
  - **66**: The FRA for beneficiaries retiring now
  - **67**: The FRA for beneficiaries born in 1960 or later
- Increases to the FRA reduce benefits for all retired workers, regardless of the age they retire

# Adjustments to Basic Benefits



- **Based on Age at Retirement**

- Early retirement = permanent benefit reduction, up to 30%
- Delayed retirement = permanent benefit credit, up to 24%



**Note:** Illustration assumes benefit of \$1,000 at full retirement age of 67 (i.e., born in 1960 or later).

**Source:** Social Security Administration

# Adjustments to Basic Benefits



- **Based on Post-Retirement Earnings**
  - *Retirement Earnings Test (RET)*: Benefit amounts may also be reduced for beneficiaries who work before their FRA
  - Beneficiaries affected by the RET receive higher benefits in the long run—on average, it all comes out in the wash

# Benefits for Workers' Families



- **Beneficiaries' family members may be covered, including:**
  - Spouses
  - Former spouses
  - Children
  - Dependent parents
- **The amount of family members' benefits is based on the worker's benefit amount**

# Social Security Will Be There for You



# Will There Be Anything Left for Me?



- Yes!
- As long as people are working, Social Security benefits will be paid
- Even if we do *nothing at all*:
  - Payroll tax contributions will be enough to fund more than  $\frac{3}{4}$  of promised benefits if the trust fund is exhausted (~2036)
  - That's about the same dollar amount as today's beneficiaries receive, adjusted for inflation