

Social Security 101



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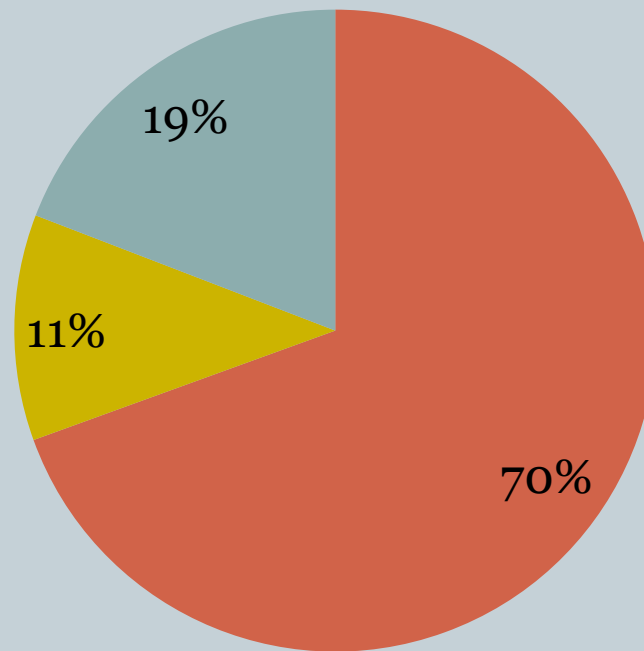
Social Security Benefits Everyone



Who Receives Social Security Benefits?



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



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

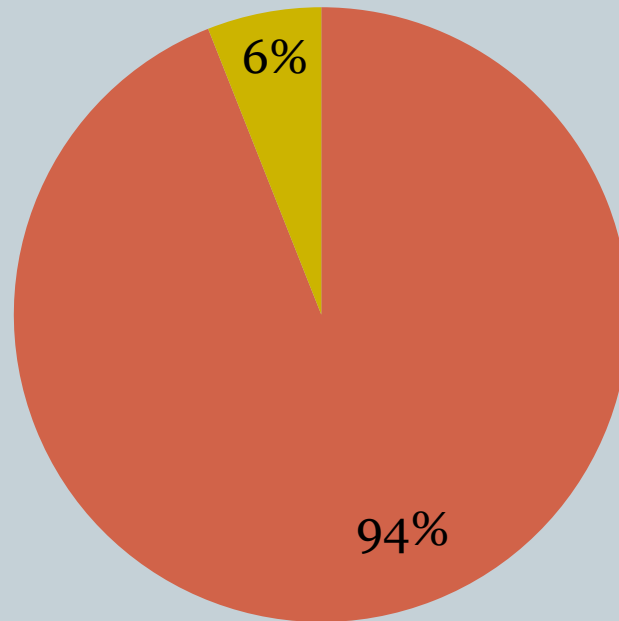
Source: SSA, <http://www.ssa.gov/oact/FACTS/index.html>

Note: As of December 2011

Who Pays into Social Security?



- About **19 in 20 workers** (159 million people)
 - This includes all Members of Congress—so tell your uncle!



■ Covered workers ■ Uncovered workers

Source: SSA, <http://www.ssa.gov/oact/FACTS/index.html>

Note: As of December 2011

How Much?

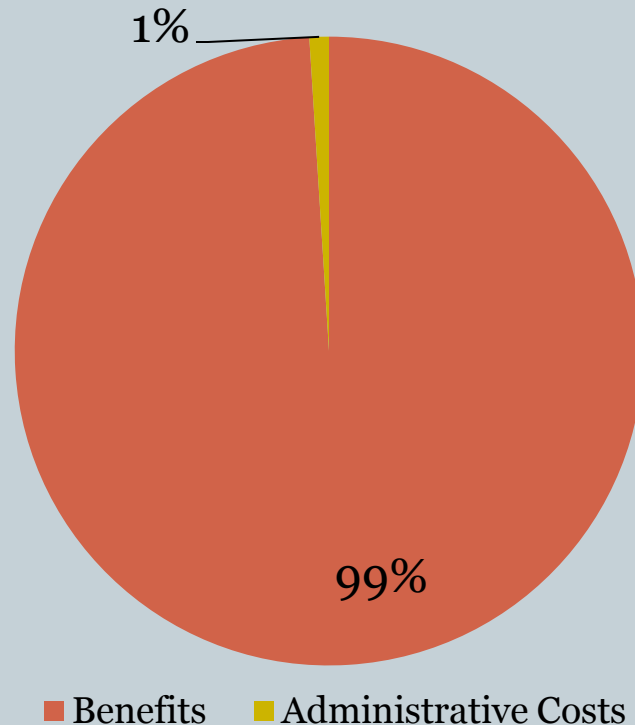


- **Payroll tax rate:**
 - Employers contribute 6.2% of earnings
 - Employees contribute 4.2% of earnings—*for 2011-12 only*
 - ✦ Typically, employees contribute 6.2%
 - ✦ Solvency and benefit calculation are *not* affected by tax holiday
- **Payroll tax cap:**
 - \$110,100 in earnings for 2012
- **Combined contribution in 2012 (10.4%):**
 - About \$4,000 for an average earner (~\$40,000/yr)
 - About \$11,500 for a maximum earner (\$110,100/yr)

Where Does the Money Go?



- In 2011, Social Security spending was **\$736 billion**

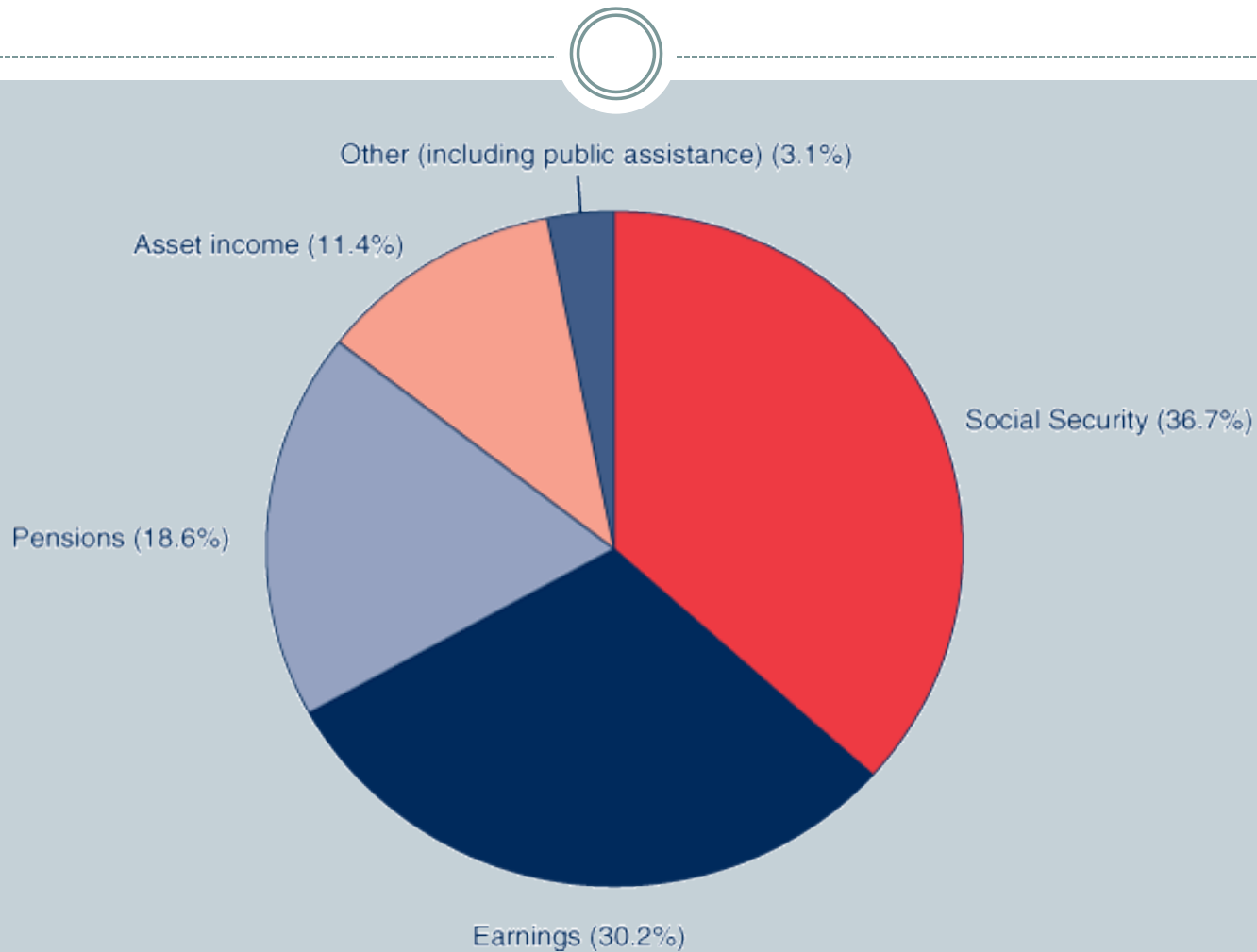


Source: 2012 Social Security Trustees Report,
http://www.ssa.gov/oact/TR/2012/II_B_cyoper.html#94983

Social Security Benefits in Perspective

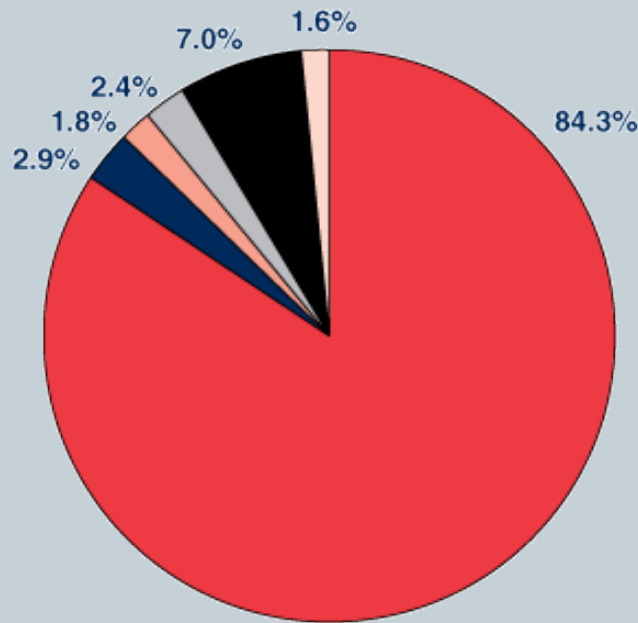
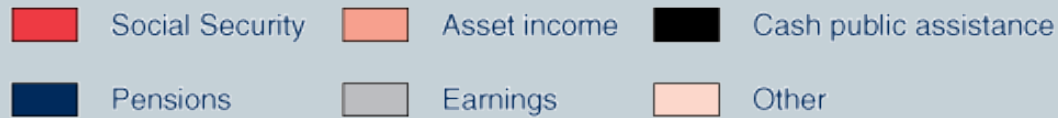


The Largest Source of Elderly Income

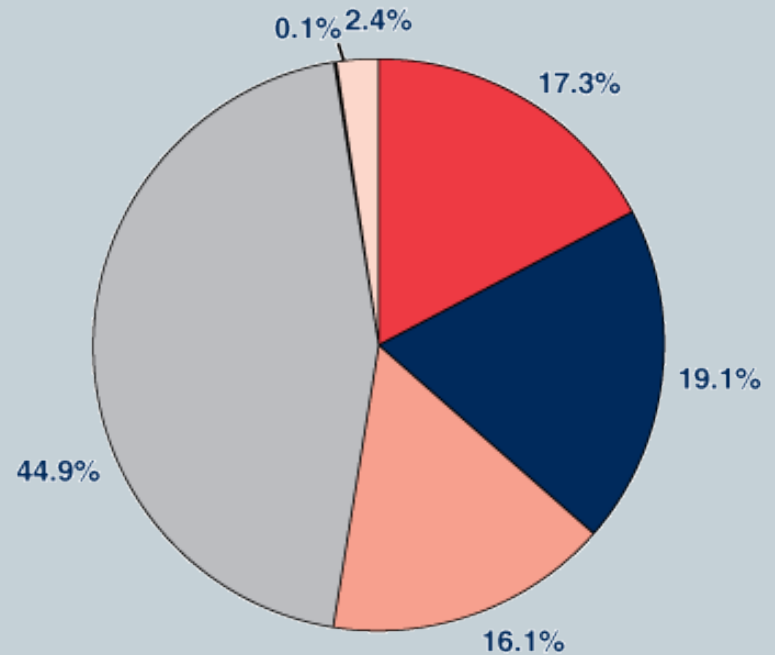


Source: SSA, Income of the Aged Chartbook, 2010,
http://www.ssa.gov/policy/docs/chartbooks/income_aged/index.html

Reliance Varies Widely by Income Level



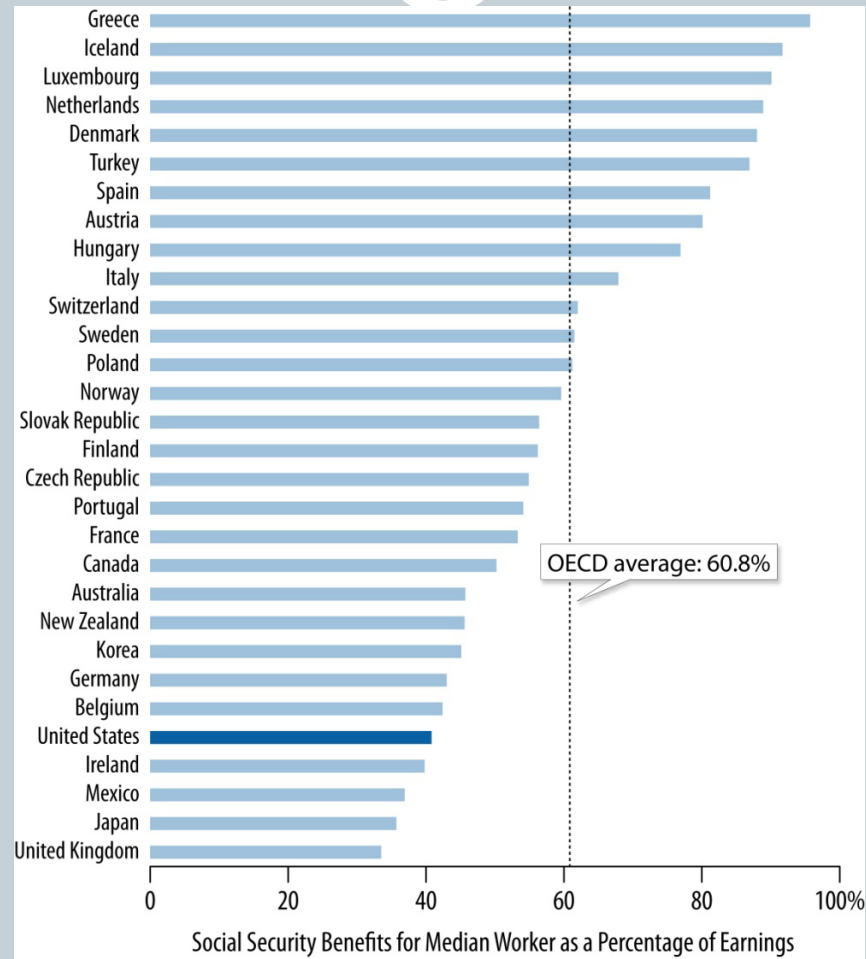
Lowest quintile



Highest quintile

Source: SSA, Income of the Aged Chartbook, 2010,
http://www.ssa.gov/policy/docs/chartbooks/income_aged/index.html

Replacement Rates Less than OECD Average

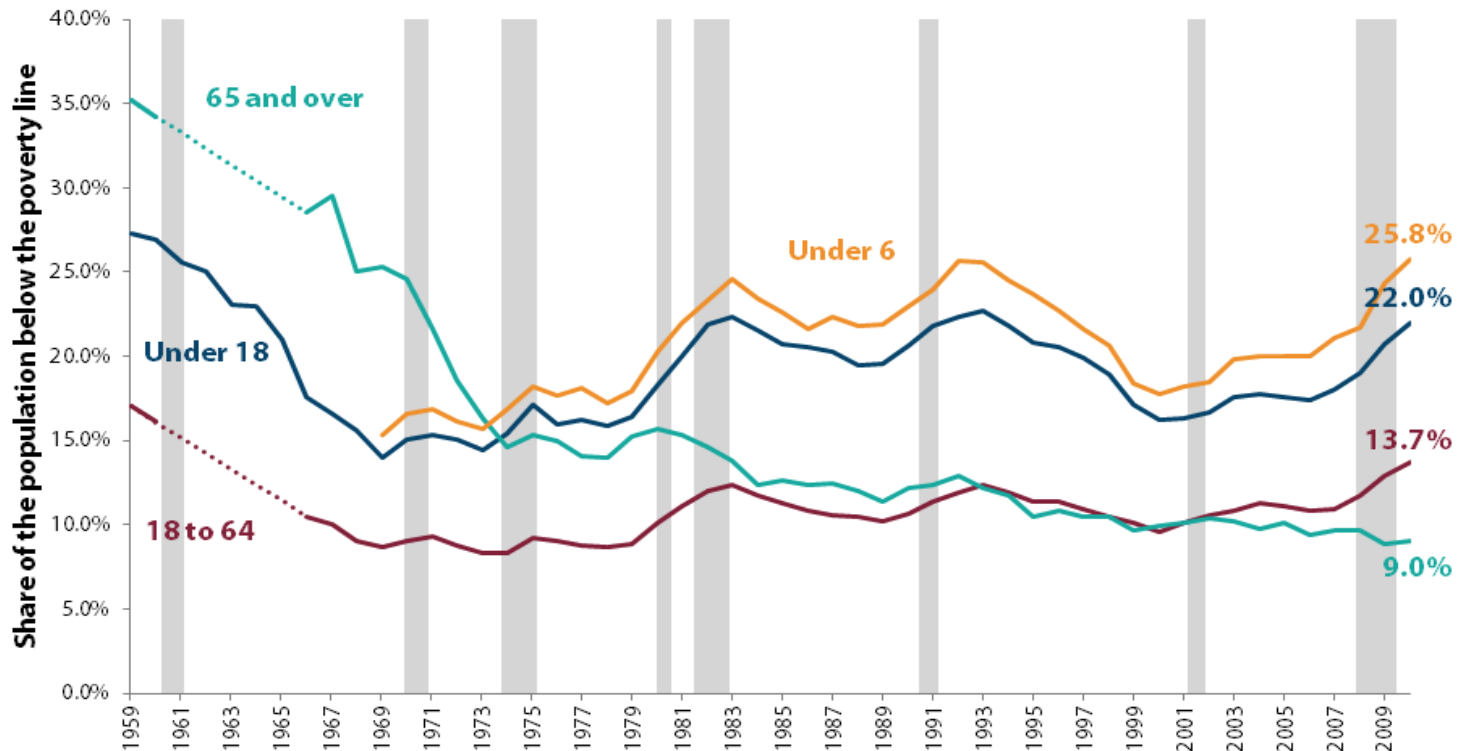


Source: OECD, *Pensions at a Glance*, 2009, public pensions for median earner

Elderly Poverty Over Time



Poverty higher for children
Poverty rates by age, 1959–2010



Note: Shaded areas denote recession.

For the 18–64 and 65 and over age groups, no formal data exists in the years between 1959 and 1966. The dotted lines denote a linear extrapolation between the earliest data point (1959) and the beginning of the complete series (1966). Data for under 6 age group dates from 1969.

Source: U.S. Census Bureau, *Income, Poverty and Health Insurance Coverage in the United States: 2010 – Historical Poverty Tables*, Table 3: "Poverty Status by Age, Race, and Hispanic Origin," Excel spreadsheet accessed November 29, 2011.

How Are Benefits Calculated?



The Basic Benefit Formula (2012)

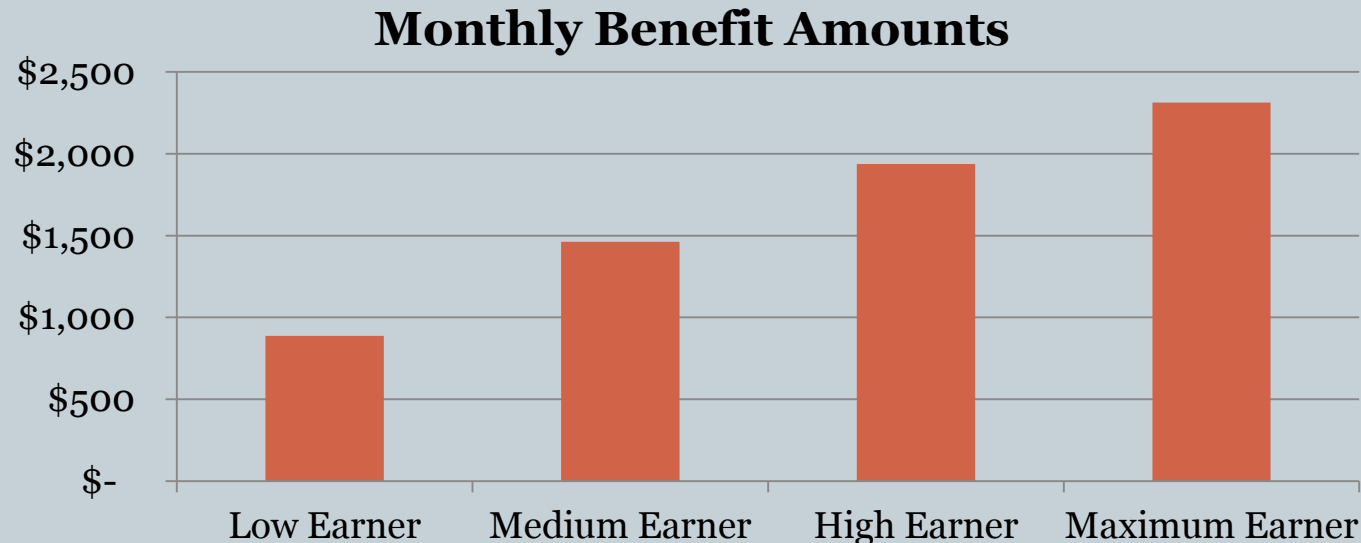


- **Calculate the worker's average indexed monthly earnings (AIME):**
 - Indexed to wages at age 60
 - Average of the highest 35 years of earnings
- **Calculate the basic benefit amount (or primary insurance amount, PIA):**
 - 90% of the first \$767 of AIME, plus
 - 32% of AIME over \$767 up to \$4,624, plus
 - 15% of AIME over \$4,624 (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



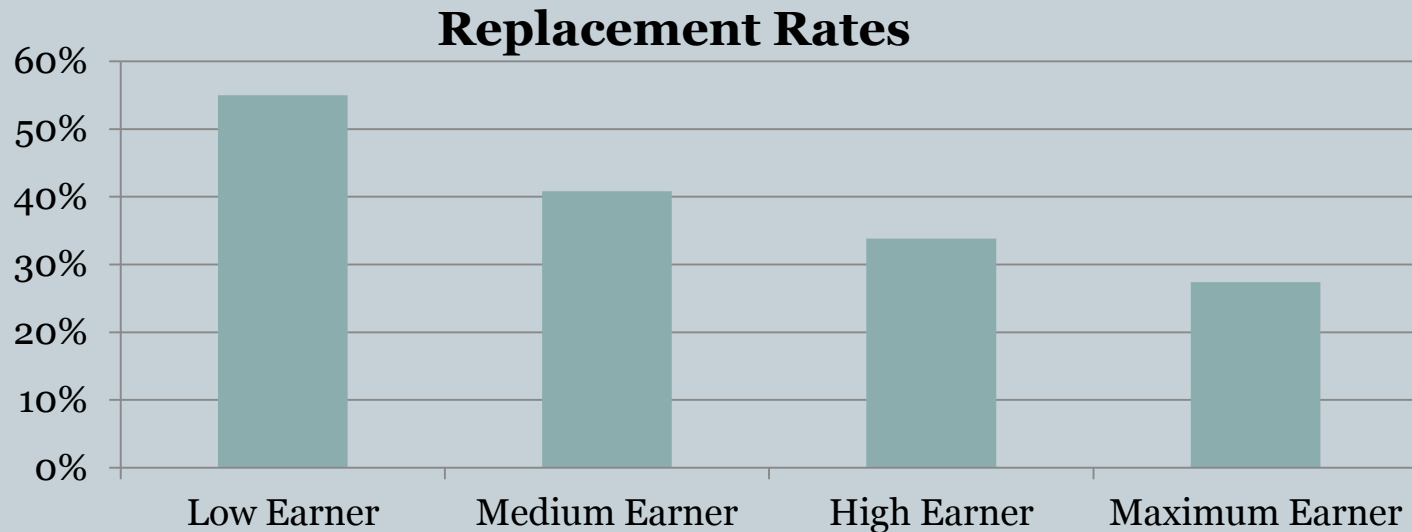
Note: Hypothetical scaled earners who turn 65 and retire in 2012

Source: 2012 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: 2012 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

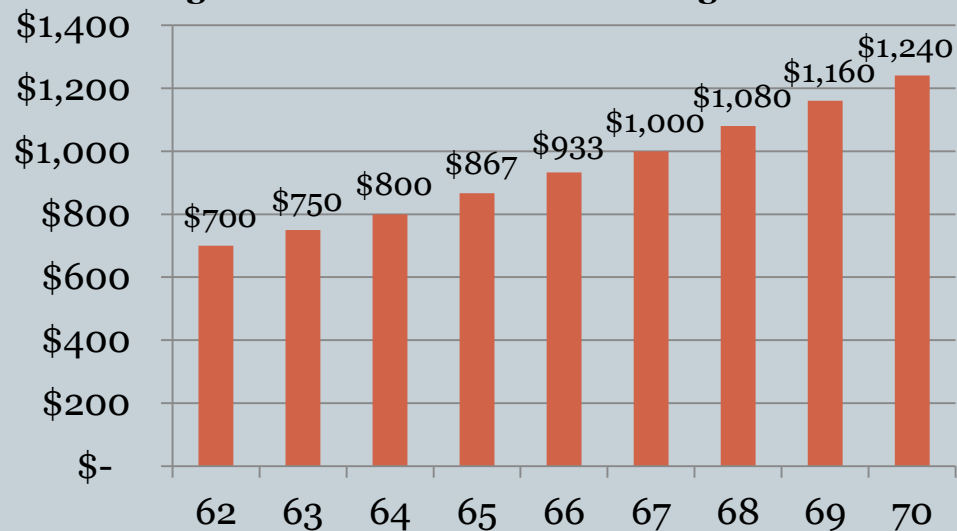
Adjustments to Basic Benefits



- **Based on Age at Retirement**

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

Monthly Benefit Amounts Differ Based on the Age You Decide to Start Receiving Benefits



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

Source: Social Security Administration

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