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2024 ImpACT

SOA ANNUAL CONFERENCE

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Session 1K: Updates on the Financial Status of Social Security and Proposals

October 28, 2024

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What Do We Want to Share Today About Social Security and "Entitlements"?

1. What was new in the 2024 Trustees Report (released May 6) regarding Social Security's actuarial status?
2. What options can be considered for closing the financing gap?
3. How do Social Security and Medicare ("entitlements") figure in the fiscal status of the federal government and the economy?

What was new in the 2024 Trustees Report (released May 6) regarding Social Security's actuarial status?

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Three Primary Changes For the 2024 Report

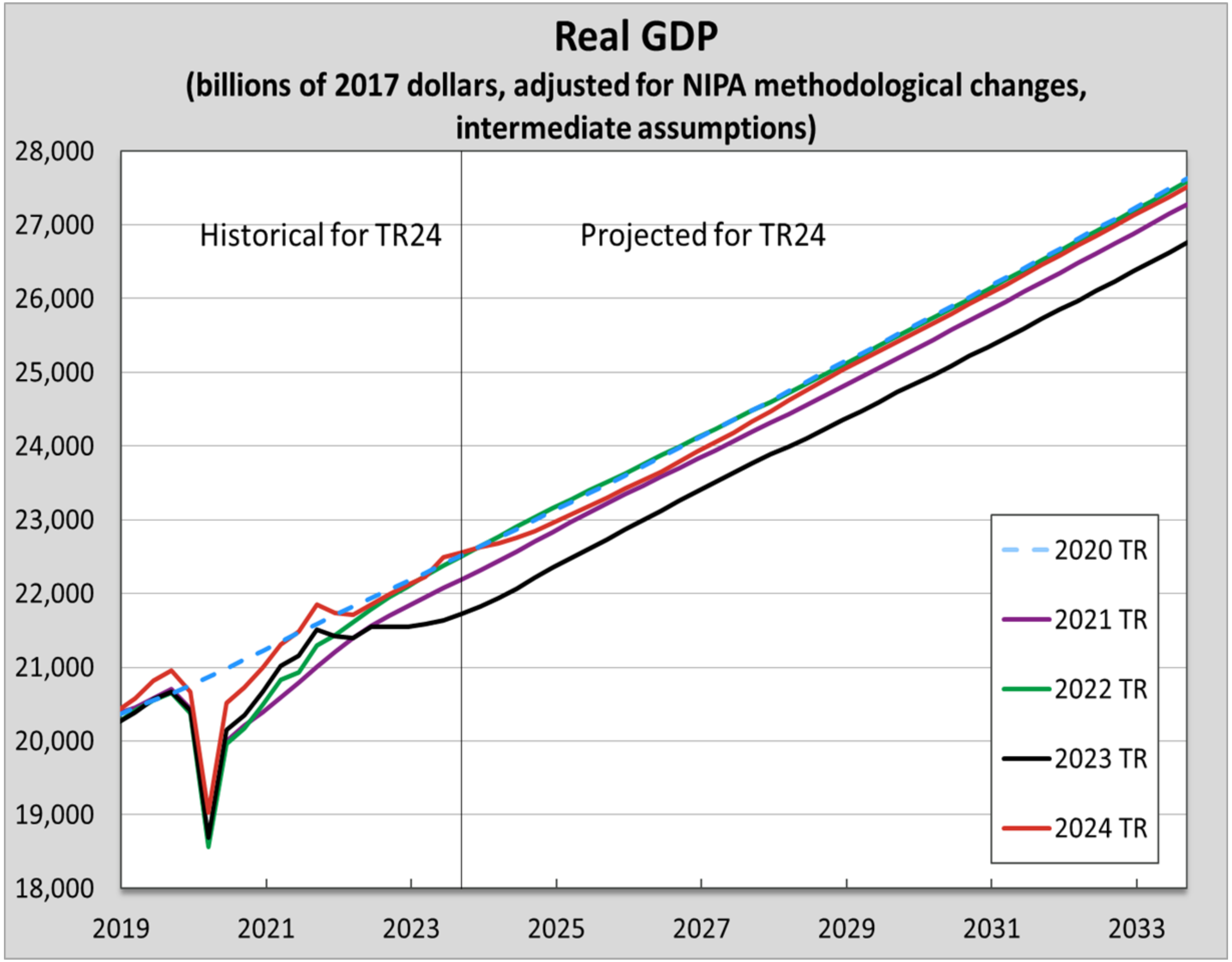
1. Economic: Given the unanticipated strength of the economy through 2023, the Trustees increased the level of labor productivity and the employment rate over the projection period. This offset the 3-percent permanent drop in the level of labor productivity and GDP assumed in last year's report.
2. Disability: The assumed ultimate disabled worker incidence rate was lowered from 4.8 to 4.5 per thousand, as applications for and awards of disability benefits have continued at low levels.
3. Demographic: The assumed ultimate total fertility rate (TFR) was lowered from 2.0 children per woman reached in 2056 to 1.9 children per woman reached in 2040, given continued low level of the TFR in recent years.

OASDI actuarial deficit now at 3.50 percent of payroll, down from 3.61 in 2023 report.

Primary Change 1: Higher GDP Level in 2024 TR Than in 2023 TR

As a result of recent economic developments, including strong growth in 2023, the assumed sustainable trend level of GDP for the 2024 TR is assessed to be about 3 percent higher than the level assumed in the 2023 TR.

The assumed ultimate trend growth rate of GDP is the same in both the 2023 and 2024 reports.

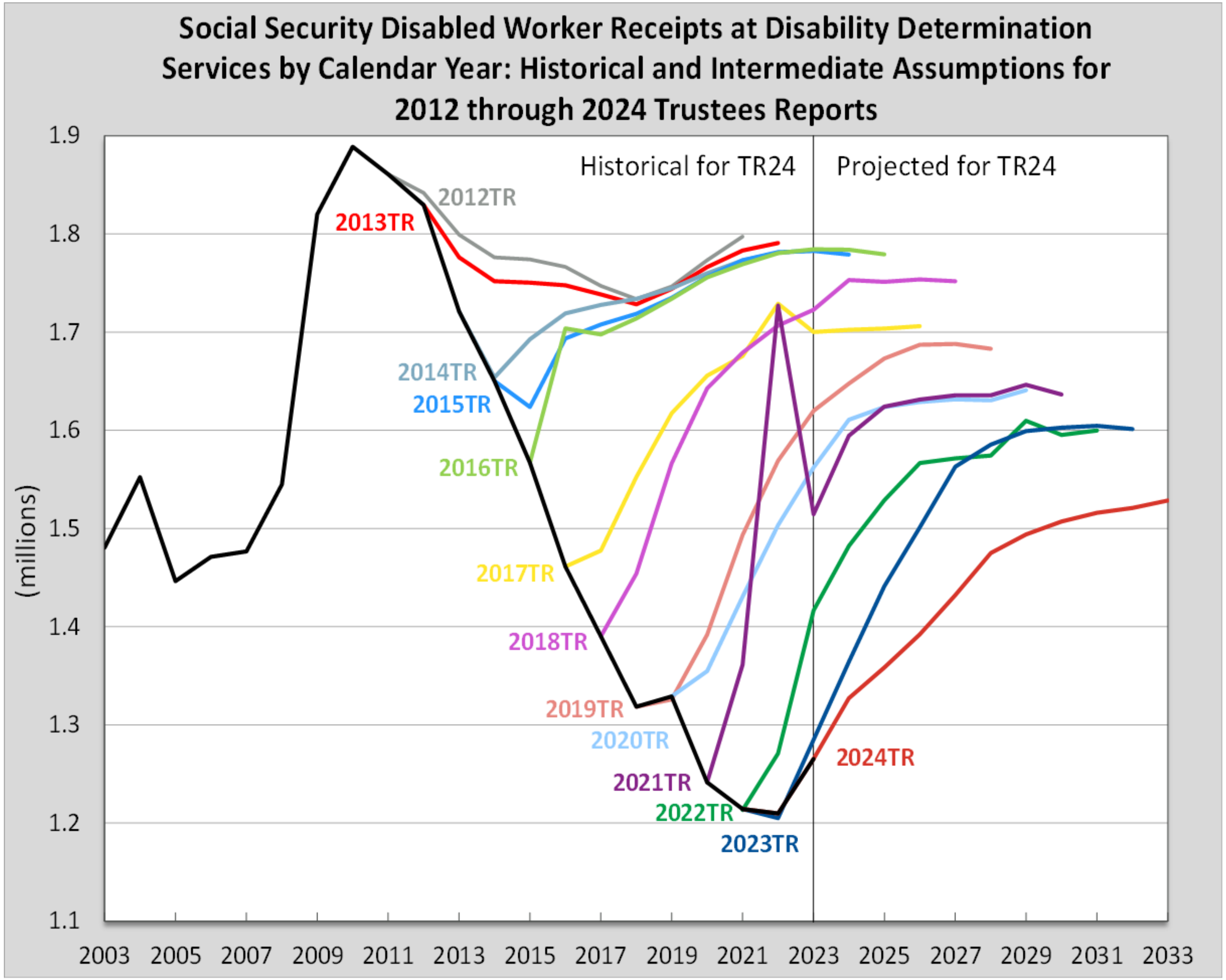


Primary Change 2: Applications for Disability Benefits Remain Near Historically Low Level

At the peak of the last economic cycle in 2007, applications were low, but increased rapidly in the 2008 recession from 1.5 million in 2007 to 1.9 million in 2010.

In 2017 through 2022, applications have dropped below the 2007 level.

Applications increased in 2023 but remain near historically low levels.

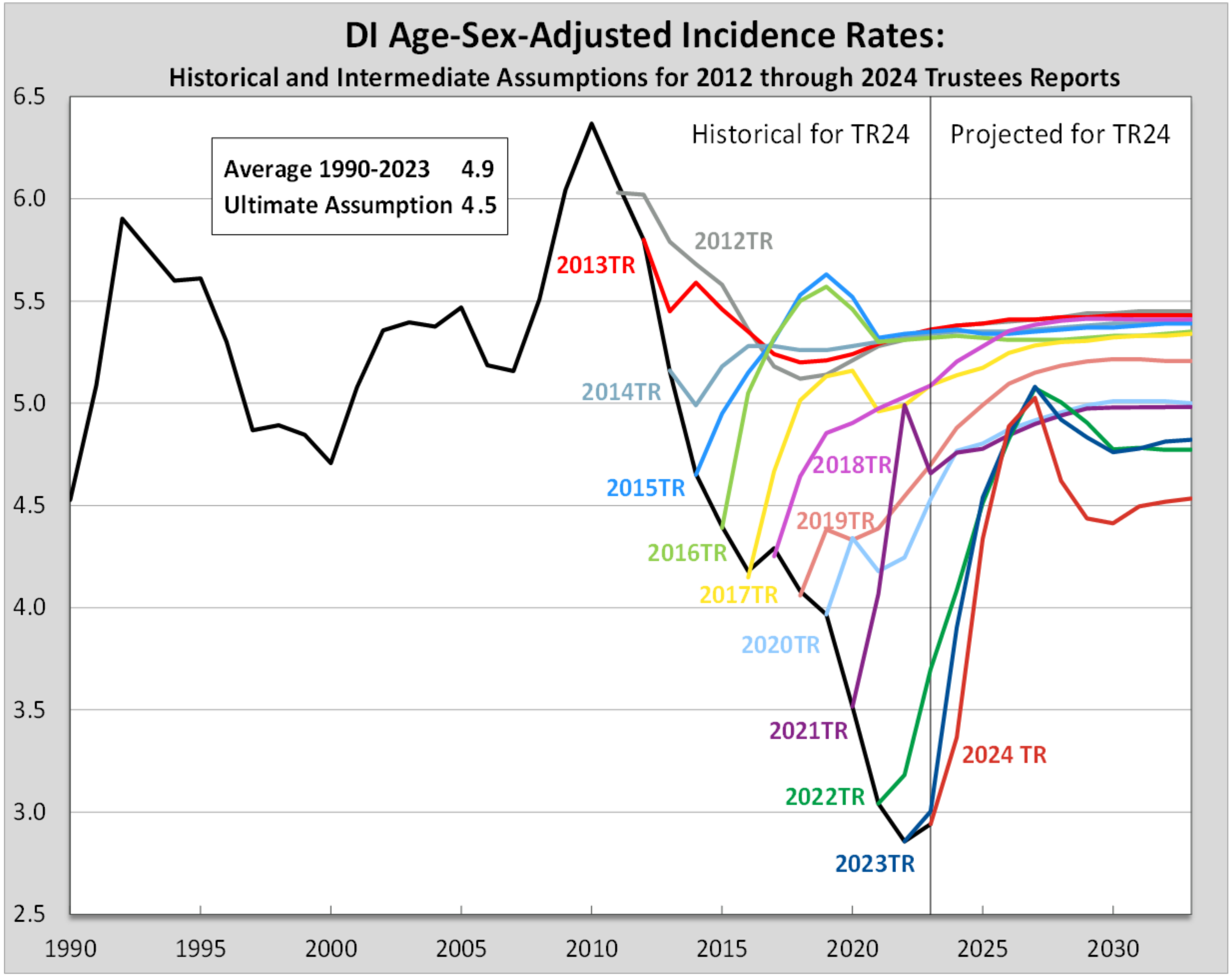


Primary Change 2: Disability Incidence Rate Also Remains At Historic Low Level

DI disabled worker incidence rate rose sharply in the 2008 recession and has declined since the peak in 2010 to extraordinarily low levels in 2016 through 2022.

Incidence rates increased slightly in 2023 and are projected to surge in order to reduce pending claims (assuming increased staffing).

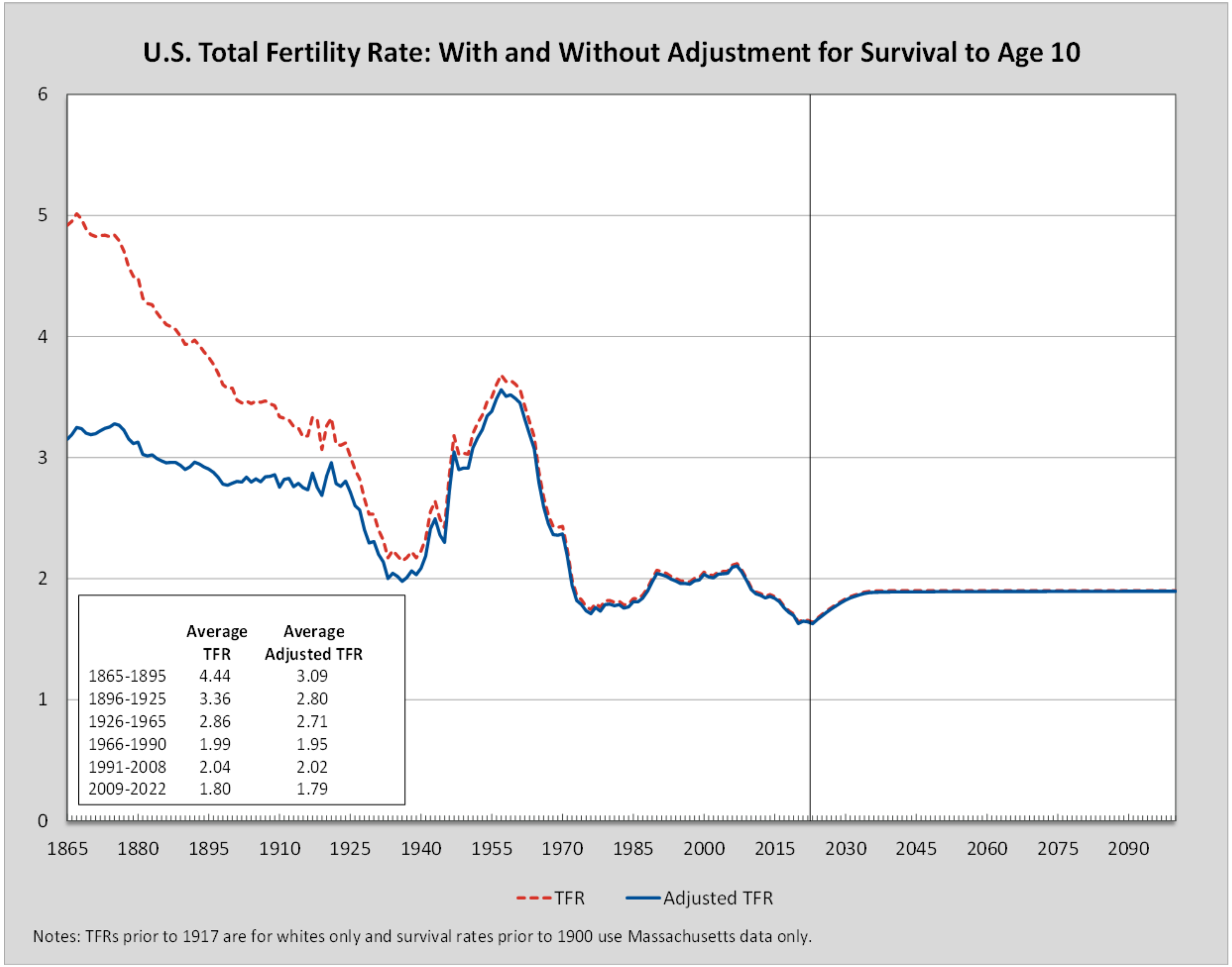
Note recent rise in pending claims due to limited staffing: see Actuarial Note 163.



Primary Change 3: Reduce Ultimate Total Fertility Rate from 2.0 to 1.9

Average “adjusted” total fertility rate falls from 3 to 2 after 1965.

Will birth rates rebound from recent historic low as in 1990-2008? If so, by how much? How about immigration?



	Average TFR	Average Adjusted TFR
1865-1895	4.44	3.09
1896-1925	3.36	2.80
1926-1965	2.86	2.71
1966-1990	1.99	1.95
1991-2008	2.04	2.02
2009-2022	1.80	1.79

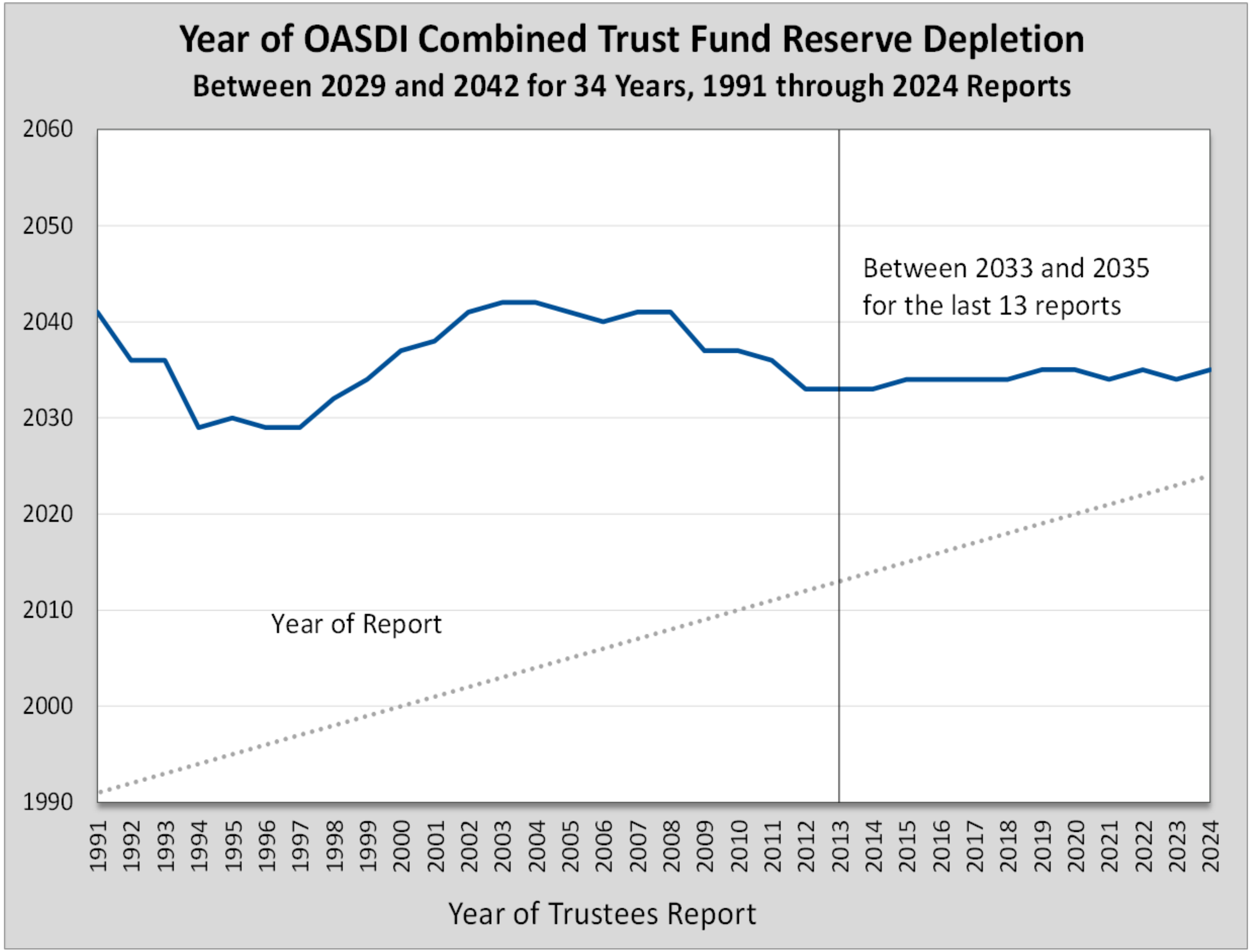
Notes: TFRs prior to 1917 are for whites only and survival rates prior to 1900 use Massachusetts data only.

Changes in Timing of Trust Fund Reserve Depletion in 2024 Report

1. OASDI reserve depletion is 2035: 13 months later than last year’s report
   a) Economic and disability changes are positive for the trust funds throughout the 75-year projection
   b) The change in the fertility rate assumption partially offsets the economic and disability changes in the long-term—but not until well after 2035
2. OASI reserve depletion is again 2033: but 7 months later than in last year’s report
3. DI reserves do not become depleted over the 75-year long-range projection period: same as last year
   a) Applications and benefit awards are both near historically low levels in 2023
   b) Reduced ultimate incidence rate
   c) Gradual increase in initial applications to their ultimate levels

Year of OASDI Combined Trust Fund Reserve Depletion

OASDI reserve depletion date varied from 2033 to 2035 in reports over the last 13 years (2012-2024) and from 2029 to 2042 in reports over the last 34 years (1991-2024).



But Wait—After the 1983 Amendments, the 1983 Trustees Report Projected Reserve Depletion in 2063

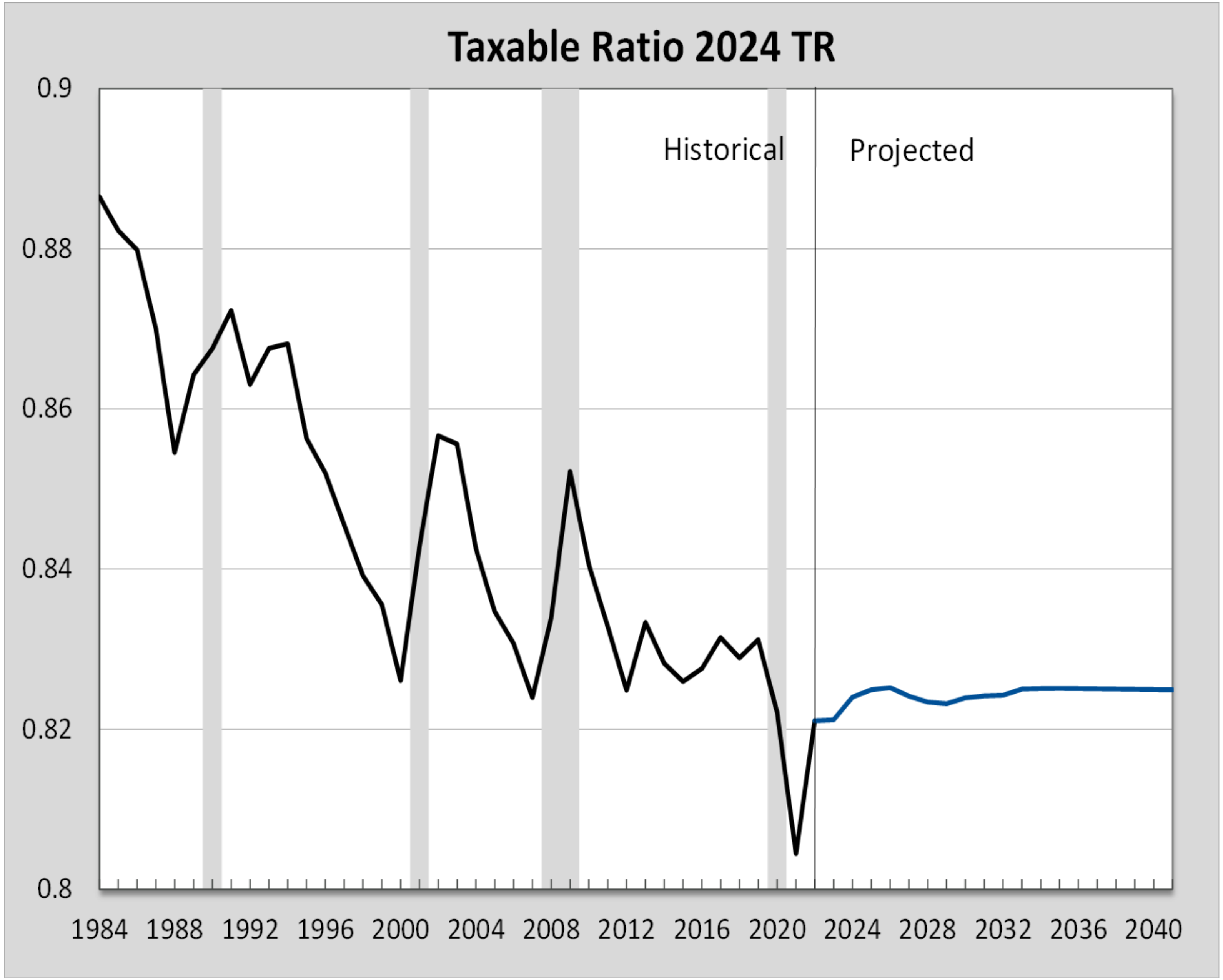
- So why is the reserve depletion date 2035 now, almost 30 years earlier than projected in the 1983 report?
- Lower birth rates were anticipated in 1983, and mortality projections were extremely accurate
- Over 80% of worsening in projections since 1983 Trustees Report was due to unanticipated economic experience

The Main Issue: Drop in Ratio of Taxable Earnings to All OASDI Covered Earnings

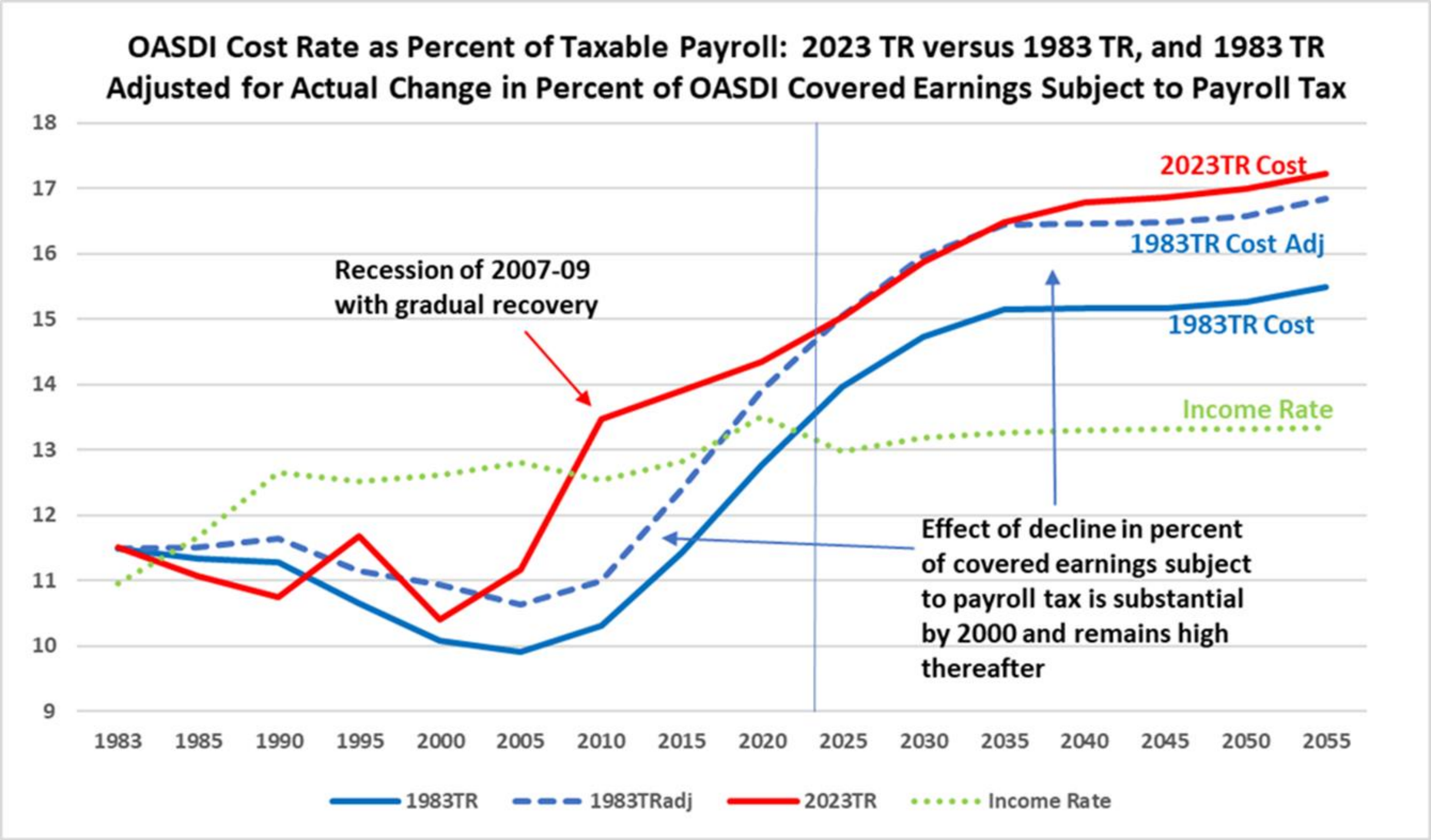
Declined since 1983 due to increasing concentration of earnings at the top of the distribution. Between 1983 and 2000, the average annual earnings for the top 6 percent of earners rose 62 percent more than CPI, but only 17 percent more for the other 94 percent of earners.

The ratio dropped to 82.5 percent by 2000 and has remained there except for cyclic effects.

This drop was NOT anticipated in 1983.



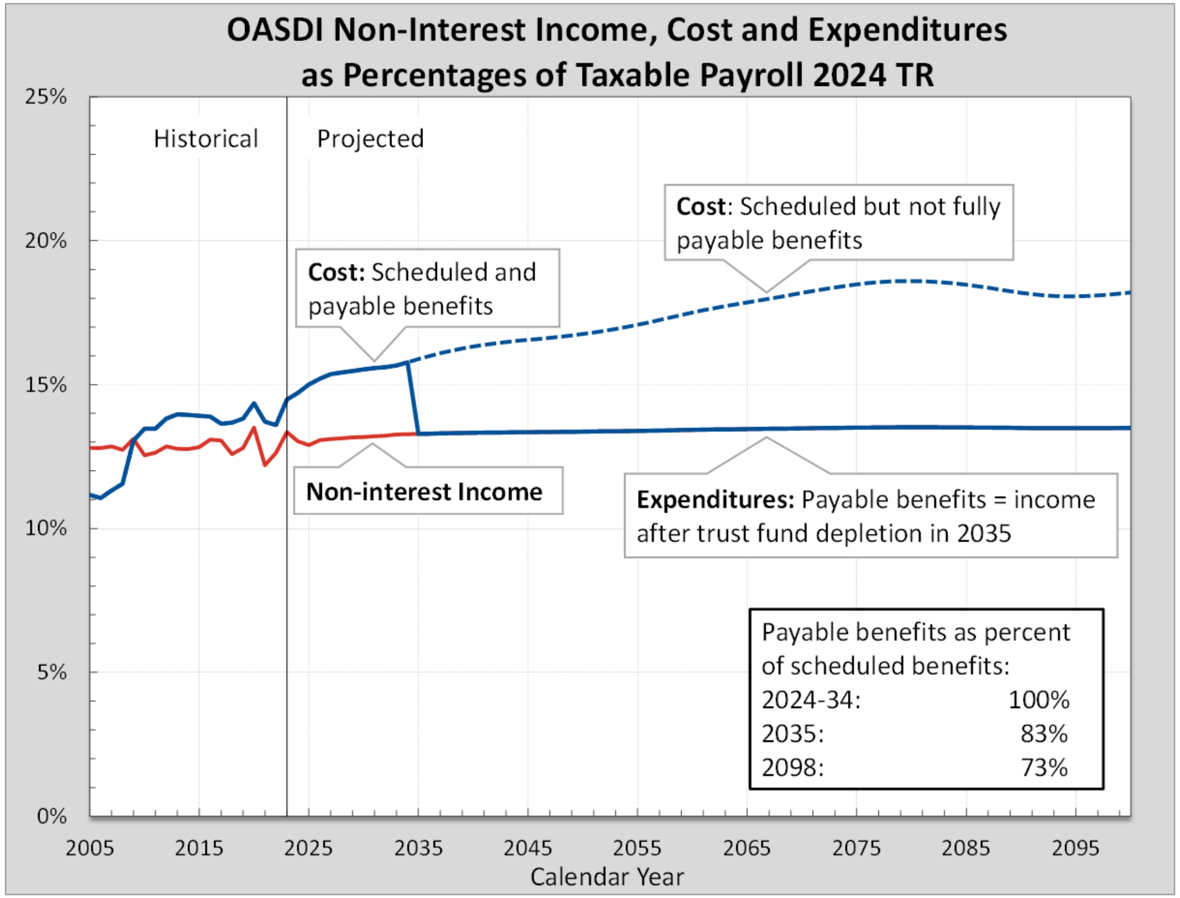
The Reduced Share of Earnings Subject to Payroll Tax Explains Most of the Increase in Cost as Percent of Payroll, Compared to the Projection in 1983

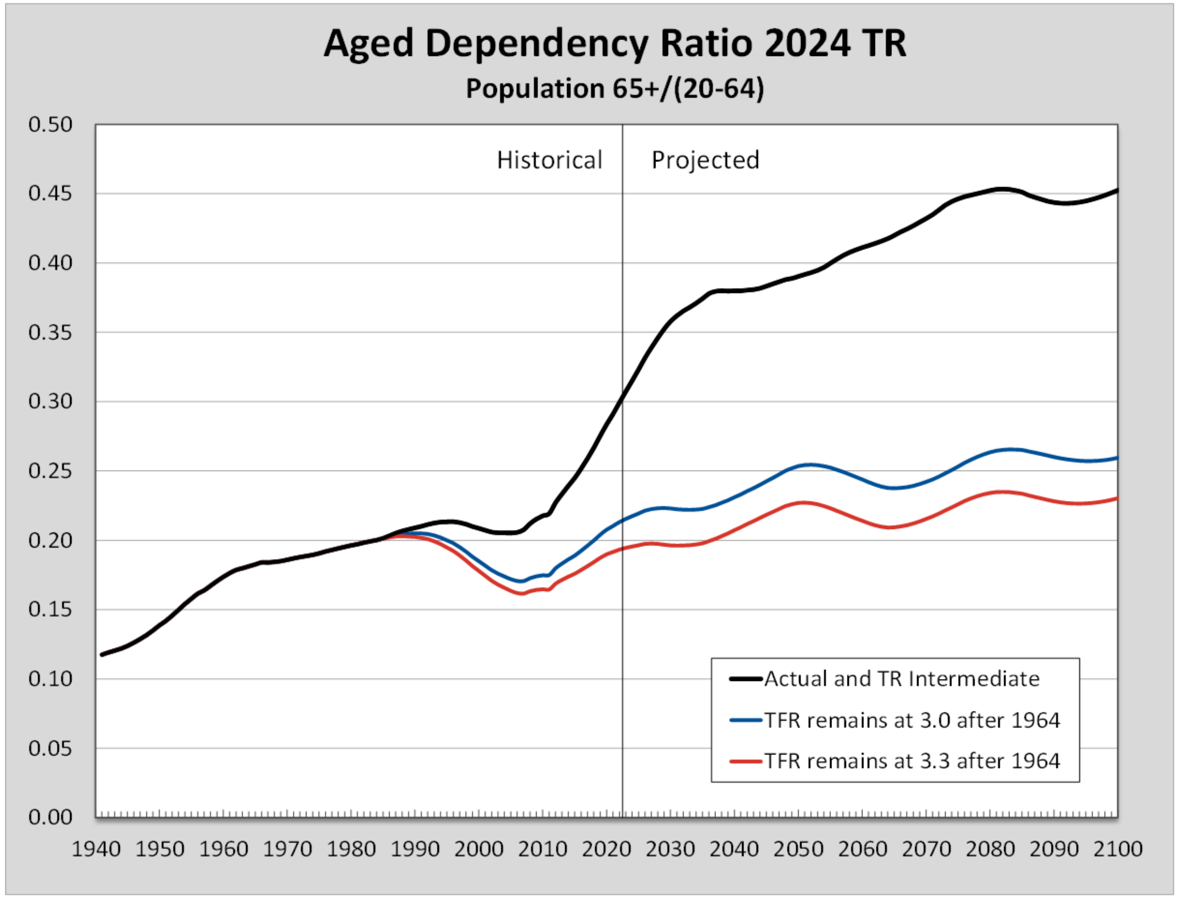


But the depth of the 2007-09 recession and slow recovery further reduced expected trust fund accumulation through 2019.

The Current Financial/Actuarial Status of the OASDI Trust Funds

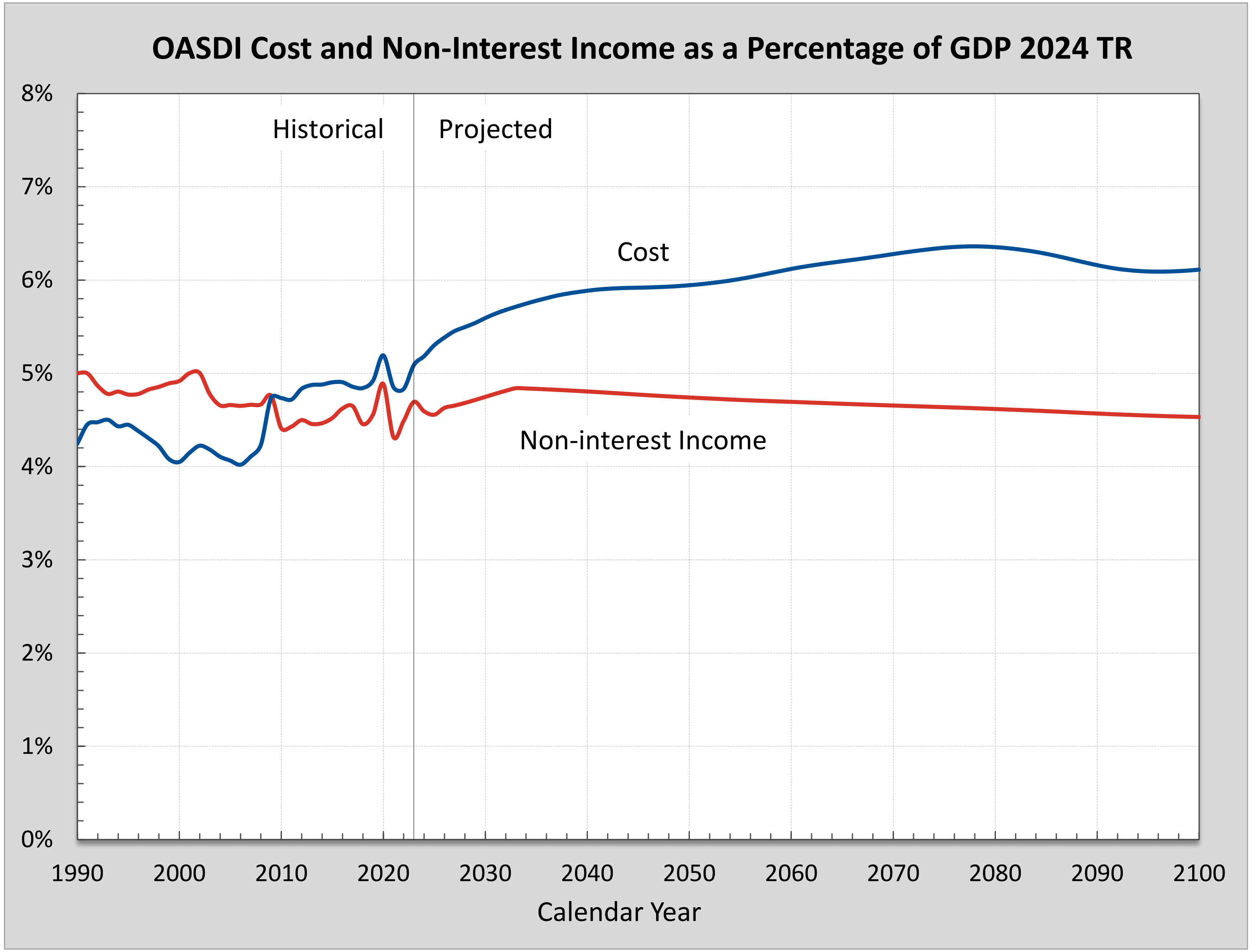
Cost is rising as a percent of payroll from 2008 to about 2040, mainly due to birth rates affecting the population age distribution





SUSTAINABILITY: Cost as percent of GDP

Rises from a 4.2 percent average in 1990-2008, to a peak of about 6.4 percent for 2078, and then declines to 6.1 percent by 2098.



What options can be considered for closing the financing gap?

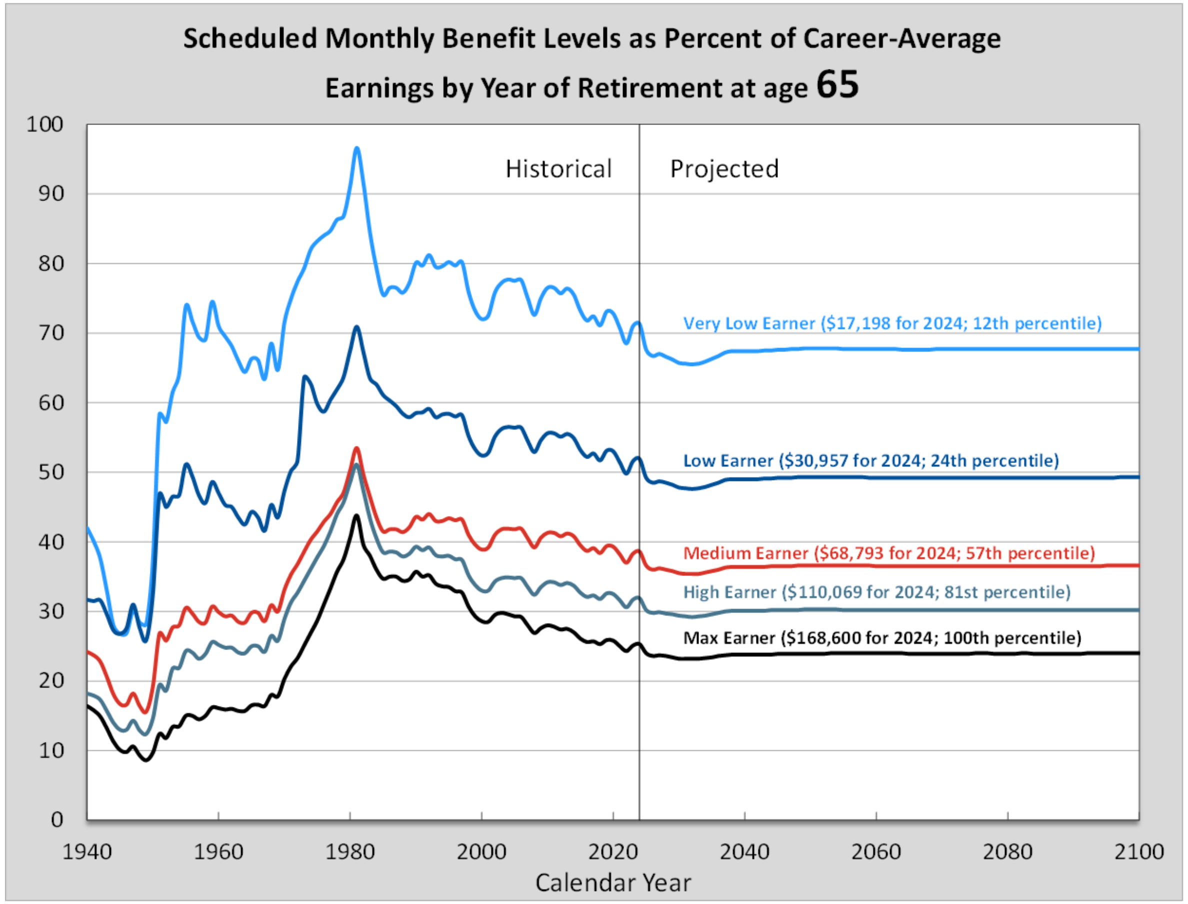
Changes Need to be Made by 2035—And Preferably Sooner

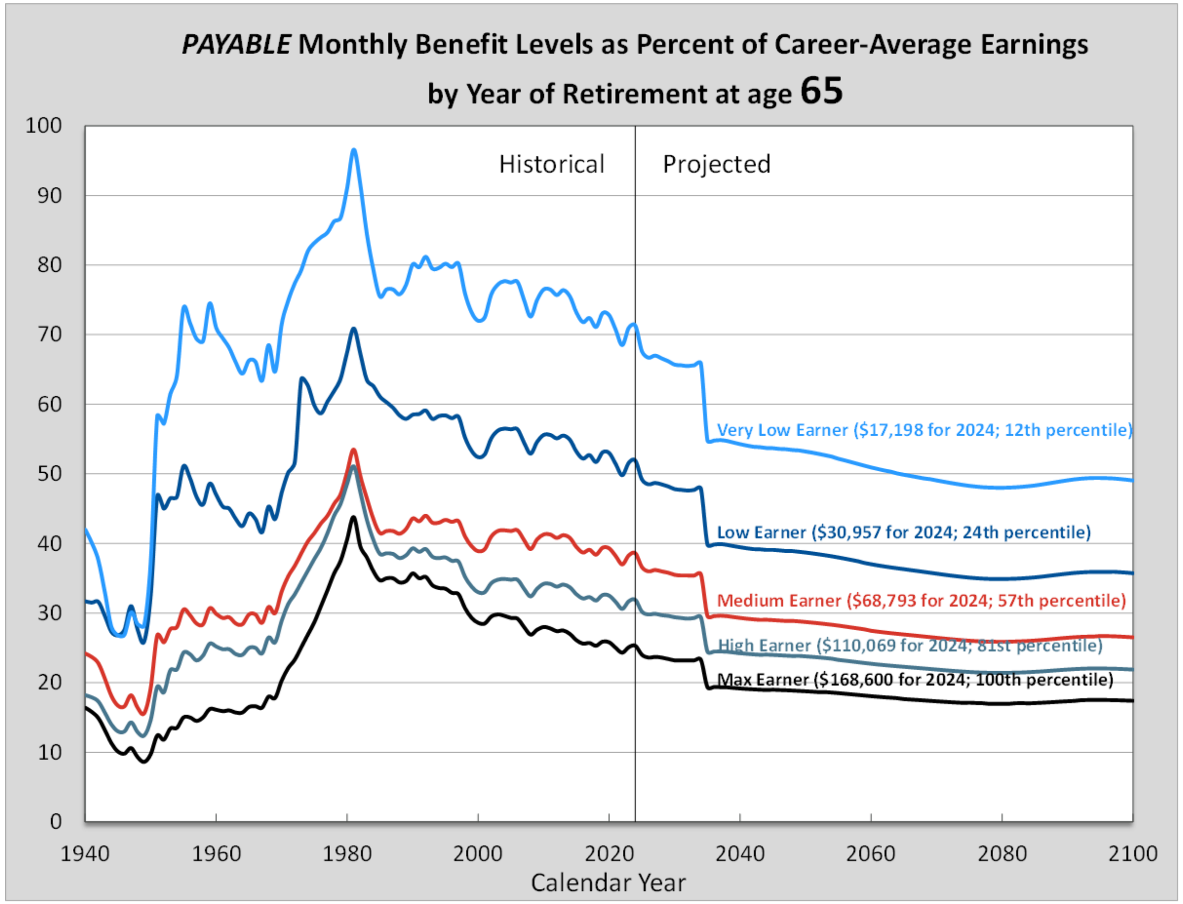
- Make choices addressing OASDI shortfall 2035-2098:
  - Raise scheduled revenue by 2035 by about one-third
  - Reduce scheduled benefits by 2035 by about one-fourth
  - Or some combination of the two
- Enacting sooner allows more options, more gradual phase in, and more advance notice

Adequacy: How Much *Should* Social Security Provide? What Share of Pre-Retirement Earnings to "Replace"?

- Note that "career-average CPI-indexed earnings" are not the appropriate basis
  - The standard of living increases through time—new goods and services do not increase the CPI, but actually reduce its growth rate
  - Career-average wage-indexed earnings approximate late career earnings (Actuarial Note 155, 2014)
  - Career-average wage-indexed earnings are also the basis for determining Social Security benefit levels
- In total, financial planners generally suggest about 75% to 80% of late career earnings level

Retired Worker Benefit Replacement Rates, Both Scheduled and Payable Under Current Law





If Reduce Benefits, By How Much, and For Whom?

- **Increase NRA**—as done in the 1983 Amendments
  - Reduce monthly benefit for retirees (and most survivors) by about 7% for each year NRA is increased, but no change for disabled worker beneficiaries
- **Reduce the COLA**—affects the oldest increasingly more as they age
- **Reduce growth in benefits**—modify the PIA formula to increase benefits across generations using price inflation, not average earnings growth
  - 1976 Hsiao Commission—fix PIA factors at 80%, 35%, 25%
    - But index PIA "bend points" and AIME by only CPI inflation (current law index is AWI)
  - 1999 Kasich and 2001 Commission—true CPI indexing across generations
    - Reduce PIA factors (90, 32, 15) by real growth in average wage
  - Progressive Price Indexing—reduce for only the top half of career earners

If Increase Revenue, By How Much, and For Whom?

- **Increase payroll taxes** by raising the 12.4% tax rate or taxing some or all earnings above the current taxable maximum
  - Gradually raise the tax max to again apply to 90 percent of covered earnings
  - Apply the payroll tax to earnings over $250,000 (Sanders) or $400,000 (Larson, Whitehouse)
  - Apply to all covered earnings
- **Take advantage of returns on private-sector investments**
  - Invest trust fund reserves, in higher yield private securities—Kerrey-Simpson 1995
  - Tax net investment income, as in ACA—Larson, Sanders, Whitehouse
  - Tax active S-corporation holders and active limited partners—Sanders, Whitehouse

Other Options

- **Increase benefits for adequacy** for certain groups
  - Increase the COLA—use CPI-E to better reflect purchases of the elderly
  - Increase or reformulate the minimum benefit
  - Caregiver credits
- **Redesign or eliminate WEP/GPO** for public sector employees
  - Representatives Brady and Neal proposed altering the benefit formula to better reflect actual earnings covered and not covered by Social Security
  - Others (Representatives Graves and Spanberger) have recently suggested eliminating WEP and GPO altogether—with 327 cosponsors in the House

- **Eliminate income taxes on Social Security benefits**
- **Eliminate payroll taxation of tip income**

Notable Proposals Scored—Whitehouse/Boyle

Senator Sheldon Whitehouse and Rep. Brendan Boyle—July 11, 2023

- Just two provisions:
  - Apply payroll tax on earnings above $400,000, with no benefit credit
  - Add a 12.4-percent tax on net investment income (expanded definition to cover earnings from S-corporations and limited partnerships) above $400,000 for single filers and $500,000 for married couples filing jointly
- Making these changes would have lead to 75-year solvency
- See www.ssa.gov/OACT/solvency/WhitehouseBoyle_20230711.pdf

Notable Proposals Scored—Larson

Representative John Larson—July 12, 2023 *(original version July 2014)*

- Significant provisions:
  - Several benefit improvements similar to his prior bills, but for 10 years only
  - Apply payroll tax on earnings above $400,000, with a small benefit credit
  - Add a 12.4-percent tax on net investment income above $400,000
- Making these changes would lead to an additional 32 years of full solvency (reserve depletion in 2066)
- See www.ssa.gov/OACT/solvency/JLarson_20230712.pdf

Notable Proposals Scored—Johnson

Former Representative Sam Johnson—December 8, 2016

- Significant provisions:
  - Make benefit formula less generous but more “progressive”; change to mini-PIA approach; add a new minimum benefit
  - Raise Normal Retirement Age to age 69 (8-year phase-in)
  - Lower the COLA by using chain-weighted CPI; no COLA if high income
  - Eliminate taxation of Social Security benefits
- Making these changes would have lead to 75-year solvency
- See www.ssa.gov/OACT/solvency/SJohnson_20161208.pdf

Notable Proposals Scored—Bipartisan Policy Center

Bipartisan Policy Center—June 9, 2016

- Significant provisions:
  - Change to mini-PIA approach; add a new minimum benefit
  - Increase the taxable maximum to $195K in 2020; index with AWI + 0.5 ppt
  - Raise payroll tax rate from 12.4 to 13.4 percent over 10 years
  - Raise Normal Retirement Age to age 69 (48-year phase-in)
  - Lower the COLA by using chain-weighted CPI for OASI, not DI
- Making these changes would have lead to 75-year solvency
- See www.ssa.gov/OACT/solvency/BPC_20160609.pdf

Notable Proposals Scored—Simpson/Bowles

Simpson/Bowles Fiscal Commission—December 1, 2010

- Significant provisions:
  - Index NRA to maintain life expectancy at NRA/(NRA-20); EEA=NRA-5 but allow ½ at age 62; exempt AIME<250% poverty from increase in NRA, phase out at 400%
  - Increase the taxable maximum by AWI + 2 ppt until 90% of earnings taxed
  - Restore the special minimum benefit
  - Provide a uniform increase 20-24 years after eligibility: 5% of PIA at AIME=AWI
  - Reduce PIA factors above 50th percentile of AIME to 30%, 10%, 5%
  - Lower the COLA by using chain-weighted CPI
- Making these changes would have lead to 75-year solvency
- See www.ssa.gov/OACT/solvency/FiscalCommission_20101201.pdf

Timing for Changes

- Historically, Congress has waited until reserve depletion is imminent
  - Difficult to lower benefits or raise taxes until necessary
- Enacting sooner allows more options, more gradual phase in, and more advance notice
  - Best example: 17-year delay in implementing NRA increase in 1983 amendments
- OASDI reserve depletion now projected for 2035
  - One year later than in the 2023 Trustees Report
  - The date has varied between 2033 and 2035 over the past 13 years
  - And between 2029 and 2042 over the past 30 years

How do Social Security and Medicare (“entitlements”) figure in the fiscal status of the federal government and the economy?

Social Security Is Not Responsible for the Federal Debt

1) OASI, DI, HI Trust Funds do ***not*** add to the debt
2) In fact, these trust funds finance part of the total federal debt
3) These programs ***cannot*** borrow under current law
4) The "budget scoring convention" is inconsistent with the law

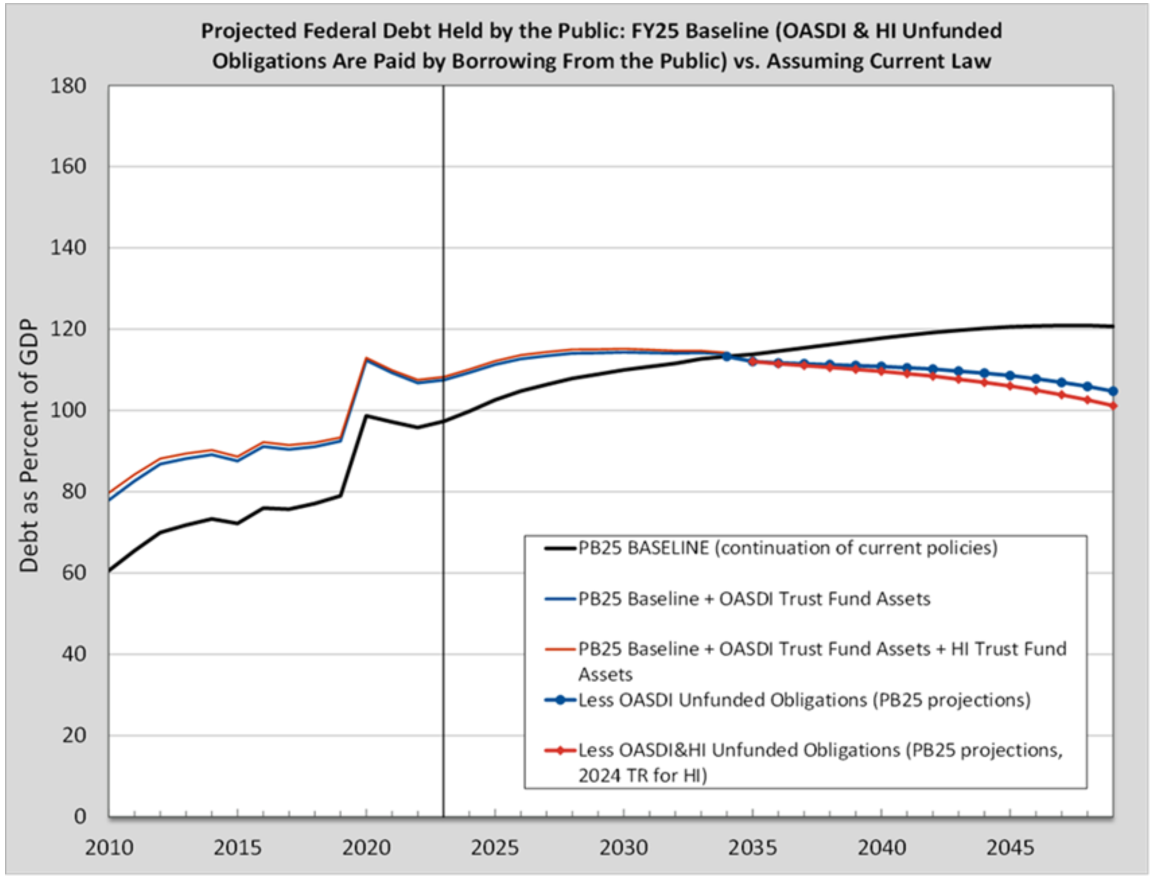
Sec. 257(b)(1) of the Balanced Budget and Emergency Deficit Control Act of 1985, P.L. 99-177:

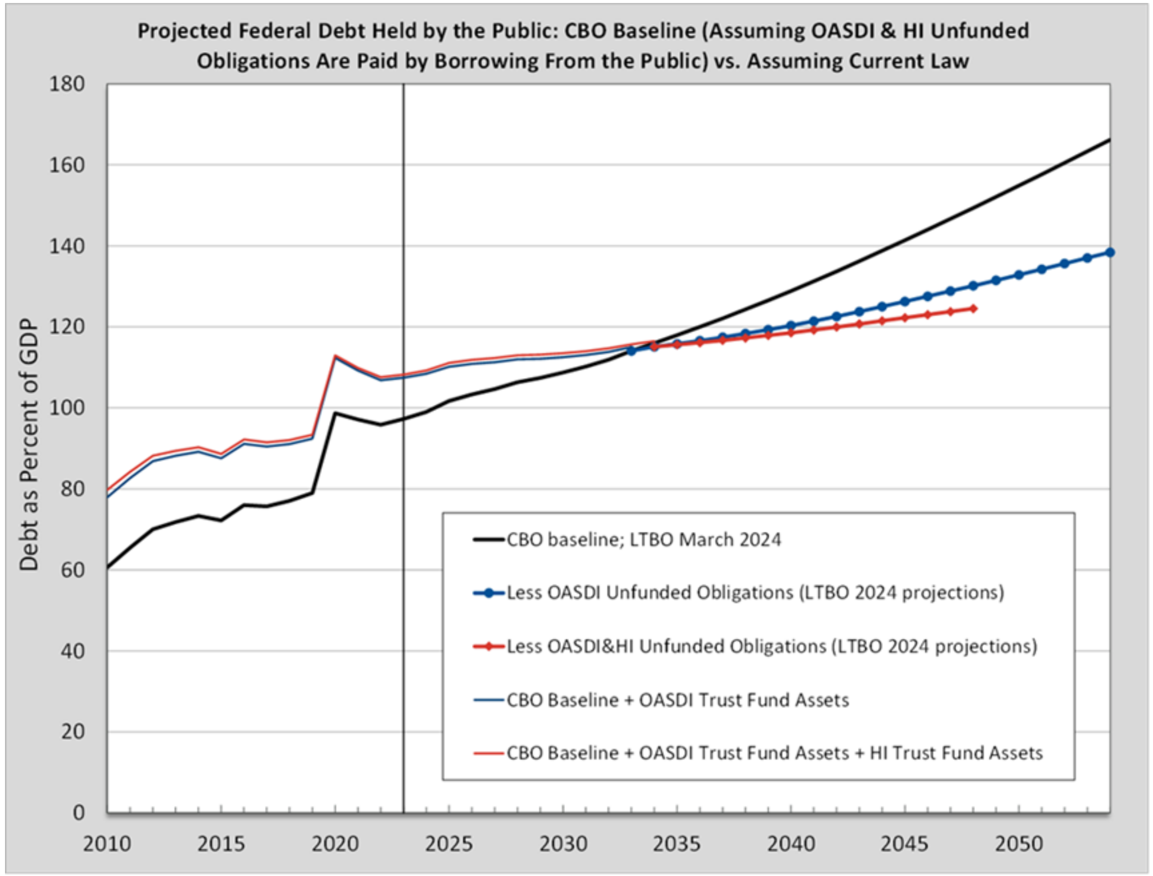
"Laws providing or creating direct spending and receipts are assumed to operate in the manner specified in those laws for each such year and funding for entitlement authority is assumed to be adequate to make all payments required by those laws."

Full scheduled payments are not required after trust fund reserve depletion; in fact, they are not even allowed.

What If We Project Federal Debt Consistent With the Law?

OMB Budget and CBO baselines assume borrowing Trust Funds from the public vs. projections consistent with current law, where OASDHI shortfalls must be met with added revenue or reduced cost; note Trust Fund reserves are part of total federal debt





The Bottom Line

- Long-term projections provide information to assess solvency and changes needed to eliminate shortfalls.
- If trust fund reserves were to become depleted:
  - Full benefits could not be paid timely
  - NO pressure on the Budget or Federal Debt
  - So Congress must act, as it always has
- Straightforward solutions:
  - Add revenue and/or lower cost for OASDI
  - Comprehensive changes ***implemented*** by 2035

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- The 2024 and all prior Social Security Trustees Reports
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- Our estimates for comprehensive proposals and individual provisions
- Actuarial notes and studies
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