SOCIAL SECURITY

MEMORANDUM

Date: June 22, 2000 Refer To: TCC

To: Harry C. Ballantyne
Chief Actuary

From: Stephen C. Goss, Deputy Chief Actuary
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Subject: Estimated Long-Range OASDI Financial Effects of the " Bipartisan Social Security Reform Act of 2000" -- INFORMATION

This memorandum provides estimates of the effect on the financial status of the OASDI program of a plan developed by Senators Gregg, Breaux, Kerrey (B), and Grassley. The plan specified below reflects our understanding of sponsors' intent as described by their staff. All estimates are based on the intermediate assumptions of the 2000 Trustees Report, with adjustment for the recent enactment of the elimination of the retirement earnings test for workers who have reached their normal retirement age.

Long-Range Financial Effects

The plan would improve the OASDI actuarial balance by an estimated 1.92 percent of taxable payroll, eliminating the actuarial deficit of 1.89 percent of taxable payroll under present law and resulting in a positive actuarial balance of about 0.02 percent of taxable payroll. The level of OASDI trust fund assets as a percentage of annual OASDI cost (the trust fund ratio) would be expected to decline after reaching 296 percent in 2012, to a low point of 44 percent at the beginning of 2049. The trust fund ratio would rise after 2049, reaching a level of 127 percent at the end of the long-range (75-year) period, at which point the trust fund ratio would be relatively stable, rising by about 4 percentage points each year. Table 2, attached, provides estimated annual cost rates, annual income rates, annual balances, as well as annual estimated trust fund ratios.

The balance of this memorandum provides descriptions of the provisions of this bill as they would affect the Social Security program.

Description of Provisions

Table 1, attached, provides financial estimates for each of the individual provisions of the plan.

Section 101 would, beginning 2001, redirect 2 percentage points of the OASDI payroll tax to " Individual Savings Accounts" (ISAs) for all covered workers born after December 31, 1937. OASI benefits (including those to converted disabled workers after reaching NRA) payable based on the earnings of workers with any taxes redirected to ISAs would be reduced (offset) in the future (see section 103).

This section would also add a General Revenue contribution to the ISAs of workers with low earnings. However the additional contributions would not be included in the calculation of the benefit reductions in section 103.

Section 102 would provide for a $1,000 contribution at birth to the ISA of each person born in the United States in 2001 and later. Also beginning in 2001, $500 would be deposited into the ISA of each person at their attainment of each age 1 through 5. These amounts would be indexed by the SSA average wage indexing series for years after 2001. Contributions would be made from the General Fund of the Treasury. One half of the contributions at ages 0 through 5 would be included in the calculation of OASDI benefit reduction in section 103.

Section 103 would reduce (offset) OASI benefits based on the earnings of a worker who had any contributions into his/her ISA. The reduction would be based on a hypothetical accumulation of the amount of payroll taxes redirected to the individual account(plus one half of contributions under section 102), using the yield rates on special government bonds held by the trust funds, up to the date of initial entitlement to OASI benefits. At that time, the ratio of the value of the hypothetical accumulated account to the present value of all OASI benefits expected to be paid based on the worker's earnings (without regard to this section) would be calculated. Future OASI benefits paid based on the workers account would then be reduced by this ratio.

The amount by which income taxes on OASI benefits are reduced by this provision would be assessed against the accumulated account of the worker and transferred to the OASDI trust funds. No other assessment (clawback) against the ISA balance would be made for the benefit of the OASDI trust funds at death.

Section 201 would create a new PIA bend point between the current two bend points, splitting the PIA bracket where the 32-percent PIA factor currently applies in two. Rather than 32 percent, PIA factors of 70 and 20 would apply above and below the new bend point within this bracket. The PIA factor of 15 percent would be replaced with 10 percent above the top bend point. This provision would be phased in gradually between 2006 and 2015, and is designed to have no net effect on the long-range cost of the OASDI program.

The changes in this section would be computed fully for the PIA formula applicable for each future year prior to the application of changes in section 209.

Section 202 would gradually implement an option for the surviving spouse of a married couple to receive up to 75 percent of the benefit that would be payable to the couple if they were still both alive. The percentage of the couple benefit payable under the option would be 50 percent for surviving spouses newly eligible in 2001 or 2002, 51 percent for those newly eligible in 2003 or 2004, … , and 75 percent for those newly eligible in 2051 or later.

Eligibility for the option occurs when the survivor and the deceased spouse, if still alive, would each be eligible for a retired worker, aged spouse, or aged divorced spouse benefit. The benefit under the option would be limited to the retired worker benefit that would be payable to the survivor if he/she had had earnings at the level of the OASDI contribution and benefit base from age 22 through 61, with the retired worker benefit reduced as of the age at first actual entitlement to either retired worker, aged spouse, or aged surviving spouse benefit (but not less than 62).

Section 203 would eliminate the retirement earnings test for beneficiaries age 62 and above, effective in 2003.

Section 204 would gradually increase the PIA benefit computation period for retired workers from 35 to 40 years, except for the lower earner of a married couple. The provision would also allow the inclusion of earnings of all years in the numerator of the AIME, even if the number of years with earnings exceeds 40.

This provision would apply in determining benefits for retired worker and their dependents and for survivors of deceased workers. This provision does not apply in determining benefits for disabled workers and their dependents.

In calculating the AIME for a retired worker under present law, the highest 35 years of indexed earnings are used in determining the numerator of the AIME and a benefit computation period of 35 years is used in determining the denominator. Under this provision, the following changes are made in the calculation of the AIME for someone newly eligible for retirement benefits after 2001.

- The number of years of earnings, used in calculating the numerator of the AIME, is gradually increased, reaching all years of earnings in 2010.
- The benefit computation period, used in determining the denominator of the AIME, is gradually increased, reaching 40 years (5 additional years), except for the lower earner of a married couple. In the case of a two-earner couple, the benefit computation period for the earner with the lower PIA is 35 years.

The chart below indicates the schedule of the above changes.

Change in Calculation of AIME for Retired Worker
(assumes the retired worker is not the *lower earner of a married couple)*

Newly Eligible in Years:	2002 – 2003	2004 - 2005	2006 – 2007	2008 – 2009	2010+
Present Law					
Years in Numerator[1]	35	35	35	35	35
Denominator (in years)[2]	35	35	35	35	35
Proposal					
Years in Numerator[1]	37	39	41	43	all
Denominator (in years)[2]	36	37	38	39	40

[1] Years in Numerator: Refers to the number of years of earnings used in calculating the numerator of the AIME.
[2] Denominator (in years): Refers to the benefit computation period (in years) used in calculating the denominator of the AIME.

Under this provision alone, the number of benefit computation years used for the denominator of the AIME for a retired worker turning age 62 after 2009 would be 40. Under current law, the number of benefit computation years is determined by subtracting 5 dropout years from the number of elapsed years (years age 22 through the year prior to reaching EEA). Under this proposed provision, the increase in the number of benefit computation years would be accomplished by reducing the number of dropout years, ultimately to zero. In addition, each year, except for 2010, that the number of dropout years is reduced by one year, the number of years of earnings, used in calculating the numerator of the AIME, is increased an additional two years. In 2010, all years of earnings are used in calculating the numerator of the AIME for someone newly eligible for retirement or survivor benefits.

Section 205 would increase the indexing of the OASDI benefit and contribution base (the taxable maximum) to keep the percent of OASDI covered earnings that is taxable at 84.5 percent, the level projected for the year 2001 under current law. Under current indexing, the percent taxable is projected to fall below 84 percent for 2009 and later.

Section 206 would redirect to the OASDI trust funds the revenue from taxation of OASDI benefits that is currently transferred to the Medicare HI trust fund. Revenue collected by the IRS from Federal income taxes payable on OASDI benefits, in excess of the tax on 50 percent of such benefits, would be redirected from the Medicare HI trust fund to the OASDI trust funds. The provision would redirect 10 percent of this revenue for 2005, 20 percent for 2006, ... , and 100 percent for 2014 and later.

Section 207 would change the early retirement factors and delayed retirement credits in an attempt to reflect the fact that the marginal increase in the full (PIA) benefit level for earnings after reaching retirement age is, generally, relatively small. (Reduction and increment factors provided under current law are intended to provide actuarially equivalent lifetime benefits payable at different starting ages for a fixed earnings history.) This relatively small marginal increase results from the weighted PIA benefit formula, which provides a larger marginal amount of benefit per dollar of AIME for low, or early-in-career, earnings. This provision is intended to eliminate the marginal disincentive to work past EEA that is provided by the weighting in the PIA formula. Because the extent of this marginal effect depends upon the level of earnings a worker has had in earlier years, no absolute adjustment can be provided that would be appropriate for all workers. Rough estimates of adjustments to the reduction and increment factors have thus been used.

The chart below displays the proposed monthly early retirement reductions that are applicable for retired worker beneficiaries for the first 36 months for which benefits are received prior to NRA under both current law and the provision. (Different factors apply to aged spouse beneficiaries and aged widow beneficiaries.)

Similar increases for aged spouse beneficiaries would be applied, increasing the monthly reduction for the first 36 months of entitlement before NRA from 25/36 percent under present law to 30/36 percent under the provision.

Monthly Reduction in Benefits for Each of First 36 Months of Retirement Before NRA

Age 62 in:	2000	2001	2002	2003	2004	2005+
Present Law	20/36%	20/36%	20/36%	20/36%	20/36%	20/36%
Proposal	20/36%	21/36%	22/36%	23/36%	24/36%	25/36%

The ultimate reductions that are proposed for the 37^{th} through 60^{th} month before NRA are 18/36% per month (current law reductions are 15/36% per month) for both retired worker and aged spouse beneficiaries. These modified reductions are phased in according to the following schedule:
16/36% for individuals reaching age 62 in 2001 and 2002,
17/36% per month for those reaching age 62 in 2003 and 2004,
and 18/36% for those reaching age 62 after 2004.

The delayed retirement credit (DRC) is scheduled to increase to 8% per year under present law for workers attaining age 65 in 2008 and later. Under this section, the DRC would continue to increase by 0.5 percentage point every two years after 2008. An ultimate factor of 10 percentage points per year would be reached for workers reaching 65 in 2016 and later. The delayed retirement credit applies for each month for which no retired worker benefit is received by an eligible individual between NRA and age 70.

The ultimate percentages of PIA payable for retired workers by age at initial benefit entitlement are shown below.

Ultimate Percent of PIA Payable for Retired Worker Beneficiaries by Age at Initial Entitlement to Benefits

Age at Initial Entitlement:	NRA-5	NRA-4	NRA-3	NRA-2	NRA-1	NRA
Present Law	70%	75%	80%	86.7%	93.3%	100%
Proposal	63%	69%	75%	83.3%	91.7%	100%

The percentage of PIA payable for non-disabled aged widow beneficiaries newly eligible at age 60 would remain at 71.5 percent. The percentages payable for those newly eligible at ages between 60 and the NRA would scale linearly between 71.5 and 100 percent, as under present law.

Section 208 would ultimately reduce the OASDI cost-of-living adjustment (COLA) to the measured increase in the CPI-W less 1/3 percentage point, on average. The change would be phased in gradually, providing for 0.1 percent reductions in all future COLAs for beneficiaries newly eligible in 2001, 0.2 percent for those newly eligible in 2002, and 0.3 percent for those newly eligible in 2003. For beneficiaries newly eligible after 2003, reductions in COLAs would follow a repeating three-year cycle: 0.3 percent for COLAs in 2004 and 2005, 0.4 percent for COLA in 2006, etc.

Section 208 also provides for a transfer to the OASDI trust funds from the General Fund of the Treasury increasing from 0.40 percent of OASDI effective taxable payroll in 2001, to 0.5333 percent in 2020, and 0.6667 percent in 2040. This transfer is intended to " recapture" the revenue gains from lowering the CPI-indexing of income tax brackets by 1/3 percentage point in 2000 and later.

Provision 209 would gradually reduce the size of all of the PIA factors in a manner that would roughly approximate the effect of increasing the NRA at 2 months per year for 2006 through 2011, with indexing based on expected changes in life expectancy between 2012 and 2016, as well as between 2023 and 2053. These changes, combined with the scheduled increases in the NRA in current law would change benefit levels by an amount roughly equivalent to raising the NRA by an additional 2.5 years, to 69 years and 6 months by 2053.

Rather than modifying the NRA, the provision would reduce each of the PIA factors (90, 32, 15 under current law, and 90, 70, 20, 10 after effecting section 201) by 1.2 percent (multiply by 0.988) each year 2006-11, and by 0.03 percent (multiply by 0.997) each year 2012 through 2016 and each year 2023 through 2053. Under this bill, the reductions in this section would be applied for the PIA formula of each future year, only after the full application of section 201.

The PIA factors would ultimately (for individuals attaining age 62 in 2053 and later) be reduced by about 16.5 percent under this provision, from levels of 90, 32, 15 to levels of 75.13, 26.71, 12.52, under current law, or from 90, 70, 20, 10 to levels of 75.13, 58.43, 16.70, 8.35 after section 201. The modified PIA would apply to benefits payable for most retired worker, aged spouse, and aged surviving spouse beneficiaries. The current-law, unmodified PIA formula would apply for disabled worker beneficiaries, and to retirement benefits payable to disabled workers converted to retirement status at NRA (and their dependents).

Section 210 would provide a mechanism designed to facilitate development and implementation of a remedy for any projected insolvency of either the OASI or DI Trust Funds based on the intermediate assumptions of any future Trustees Report within the 75-year projection period of such report.

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Attachments

Table 1. Estimated Long-Range OASDI Financial Effect of the "Bipartisan Social Security Reform Act of 2000

	Section	Estimated Change in Long-Range OASDI Actuarial Balance (percent of taxable payroll)
201	Establish a new bend point in the PIA formula equal to 197.5% of the present law first bend point. PIA formula factors would be initially set at 90, 32, 32, and 15 (yielding the same benefit as current law). Beginning with new eligibles in 2006, the second formula factor would be *increased* each year by 3.8, the third formula factor would be *decreased* each year by 1.2, and the fourth formula factor would be *decreased* each year by 0.5, until reaching factors of 90, 70, 20, and 10 for newly eligible beneficiaries in 2015 and later.	[1]
202	Beginning with aged surviving spouses newly eligible in 2001, phase in (by 2051) a benefit option equal to 75-percent of the combined benefits that would be payable if both were still alive. Limit to amount payable if survivor had always been single and a steady maximum earner.	-0.11
203	Effective 1/1/2003, eliminate the retirement earnings test for individuals who are 62 or older.	-0.01
204	Increase the benefit computation period by up to 5 additional years for individuals newly eligible to receive OASI benefits (by one additional year for new eligibles in each year 2002, 04, 06, 08, 10). For two-earner couples, however, cap the benefit computation period for the earner with the lower PIA at 35 years. Phase in inclusion of earnings for all years in the numerator of the AIME, in conjunction with increasing the benefit computation period (denominator of the AIME).	0.24
205	Maintain the benefit and contribution base so that 84.5 percent of covered earnings are taxable.	0.06
206	Credit all revenue from taxation of OASDI benefits to the OASDI trust funds by 2014 (phase revenue from HI to OASDI during the period 2005-2014).	0.33
207	Increase the size of early retirement factors between 2001 and 2005 and delayed retirement credits between 2010 and 2016.	0.34
208	Reduce the OASDI COLA by up to 1/3 percent for beneficiaries newly eligible in 2001 and later.	0.42
209	Multiply all benefit formula factors (90, 32, and 15 under current law) by 0.988 for each year 2006-2011 and by 0.997 for each year 2012-2016 and 2023-2053. For 2053 and later, factors are reduced by about 16.5 percent, to 75.13, 26.71, and 12.52. The PIA formula factors for disability beneficiaries, both before and after conversion to retired workers are unaffected by this provision.	0.84
210	Mechanism for remedying unforeseen Social Security insolvency.	[1]
Total for Sections Above (including interactions among provisions)		**2.03**
101 & 103	Beginning in 2001 for workers born after 1937, redirect 2 percentage points of the OASDI payroll tax to individual accounts. Additional voluntary contributions would be permitted, with a match from General Revenue for low income workers. Reduce OASI benefits based on the accumulation of these accounts at the interest rate earned by the OASDI Trust Funds.	-.64
102	Beginning in 2001, deposit money at start of the first six years of life into individual accounts from General Revenue. The amount of money for the year 2001 would be $1000 at start of first year of life and $500 for each of the next five years. After 2001, the dollar amounts would be indexed using the SSA average wage indexing series. Half of the accumulated value of these deposits (at the trust fund interest rate) would be used to offset OASDI benefits.	0.01
208	Transfer from General Revenue to the OASDI Trust Fund the following amounts, specified as a percent of taxable payroll: 0.4% each year 2001-2019, 0.5333% each year 2020-2039, and 0.6667% each year after 2039.	0.51
Total for All Sections Above (including interactions among provisions)		**1.92**

[1]Negligible (between -0.005 and .005 percent of payroll) change in the OASDI long-range actuarial balance.

Based on the intermediate assumptions of the 2000 Trustees Report under present law, the long-range actuarial balance for the 75-year period (2000-2074) is –1.89 percent of taxable payroll.

Social Security Administration
Office of the Chief Actuary

June 8, 2000

Table 2 a Gregg,Breaux,Kerrey, Grassley-0.33%CPI-PIA Cut Thru 2053 ISA Cntrb 2 %, Ben Offset 100.0 %

With Ult Real TF Int Rate of 3.0
With Ult Real ISA Yld Rate of 3
With Annuity Net Yld Rate 3

Year	Cost Rate*	Income Rate	Annual Balance	TFR 1-1-yr	Change in OASDI Contrib Rate	OASDI Contrib Rate	ISA Contrib Rate
2000	10.48	12.66	2.18	216		12.40	0
2001	10.44	11.07	0.63	240	-1.600	10.80	2.00
2002	10.47	11.07	0.60	250		10.80	2.00
2003	10.62	11.08	0.45	257		10.80	2.00
2004	10.68	11.08	0.40	264		10.80	2.00
2005	10.73	11.10	0.38	270		10.80	2.00
2006	10.78	11.13	0.35	276		10.80	2.00
2007	10.84	11.15	0.31	281		10.80	2.00
2008	10.91	11.18	0.27	286		10.80	2.00
2009	10.99	11.21	0.23	290		10.80	2.00
2010	11.09	11.24	0.16	292		10.80	2.00
2011	11.19	11.27	0.08	294		10.80	2.00
2012	11.32	11.31	-0.01	296		10.80	2.00
2013	11.46	11.35	-0.11	296		10.80	2.00
2014	11.62	11.39	-0.23	295		10.80	2.00
2015	11.78	11.41	-0.37	293		10.80	2.00
2016	11.95	11.43	-0.53	291		10.80	2.00
2017	12.13	11.45	-0.68	286		10.80	2.00
2018	12.32	11.47	-0.84	281		10.80	2.00
2019	12.51	11.50	-1.01	275		10.80	2.00
2020	12.69	11.65	-1.04	267	0.1333	10.93	2.00
2021	12.87	11.68	-1.19	260		10.93	2.00
2022	13.03	11.70	-1.33	252		10.93	2.00
2023	13.18	11.73	-1.46	243		10.93	2.00
2024	13.33	11.75	-1.58	234		10.93	2.00
2025	13.46	11.77	-1.69	224		10.93	2.00
2026	13.58	11.79	-1.78	214		10.93	2.00
2027	13.68	11.82	-1.86	203		10.93	2.00
2028	13.75	11.84	-1.92	192		10.93	2.00
2029	13.80	11.85	-1.95	180		10.93	2.00
2030	13.83	11.87	-1.96	169		10.93	2.00
2031	13.84	11.89	-1.95	158		10.93	2.00
2032	13.83	11.90	-1.93	146		10.93	2.00
2033	13.81	11.92	-1.89	135		10.93	2.00
2034	13.76	11.93	-1.83	124		10.93	2.00
2035	13.66	11.94	-1.72	114		10.93	2.00
2036	13.56	11.94	-1.62	104		10.93	2.00
2037	13.46	11.95	-1.50	94		10.93	2.00
2038	13.34	11.96	-1.38	85		10.93	2.00
2039	13.21	11.96	-1.25	77		10.93	2.00
2040	13.09	12.10	-0.99	70	0.1333	11.07	2.00
2041	12.95	12.10	-0.85	64		11.07	2.00
2042	12.83	12.11	-0.72	59		11.07	2.00
2043	12.71	12.11	-0.60	55		11.07	2.00
2044	12.61	12.11	-0.50	51		11.07	2.00
2045	12.52	12.12	-0.40	49		11.07	2.00
2046	12.43	12.12	-0.30	46		11.07	2.00
2047	12.35	12.13	-0.22	45		11.07	2.00
2048	12.27	12.13	-0.13	44		11.07	2.00
2049	12.20	12.14	-0.06	44		11.07	2.00
2050	12.14	12.15	0.00	44		11.07	2.00
2051	12.09	12.15	0.06	45		11.07	2.00
2052	12.06	12.16	0.10	47		11.07	2.00
2053	12.03	12.17	0.14	48		11.07	2.00
2054	12.01	12.17	0.17	50		11.07	2.00
2055	11.99	12.18	0.19	53		11.07	2.00
2056	11.98	12.19	0.21	55		11.07	2.00
2057	11.97	12.20	0.23	58		11.07	2.00
2058	11.96	12.21	0.24	61		11.07	2.00
2059	11.96	12.21	0.25	64		11.07	2.00
2060	11.96	12.22	0.26	67		11.07	2.00
2061	11.97	12.23	0.26	70		11.07	2.00
2062	11.97	12.24	0.27	73		11.07	2.00
2063	11.96	12.24	0.28	77		11.07	2.00
2064	11.95	12.25	0.30	80		11.07	2.00
2065	11.95	12.26	0.31	84		11.07	2.00
2066	11.95	12.26	0.31	88		11.07	2.00
2067	11.95	12.27	0.32	92		11.07	2.00
2068	11.96	12.28	0.32	96		11.07	2.00
2069	11.95	12.28	0.33	100		11.07	2.00
2070	11.96	12.29	0.33	105		11.07	2.00
2071	11.96	12.29	0.33	109		11.07	2.00
2072	11.97	12.30	0.33	114		11.07	2.00
2073	11.98	12.30	0.32	118		11.07	2.00
2074	12.00	12.31	0.31	123		11.07	2.00
2075	12.01	12.31	0.30	127		11.07	2.00

	Summarized CostRt OASDI	IncRt OASDI	ActBal OASDI	Change in ActBal
2000 -2074	12.24	12.26	0.02	1.92

Based on Intermediate Assumptions of the 2000 Trustee's Report-Adj for Elim ET at NRA
With Ult Real Int Rate of 3.00
* Net of Benefit Offset/Clawback

Office of the Actuary
Social Security Administration
June 8, 2000