Statement of
G. William Hoagland
Senior Vice President, Bipartisan Policy Center

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Committee on Ways and Means
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Mr. Chairman, Mr. Becerra, and Members of the Committee – thank you for inviting me here today to discuss the recommendations related to the Social Security program made by the Bipartisan Policy Center's (BPC's) Domenici-Rivlin Task Force. I was privileged to serve on this bipartisan, independent group that released its recommendations in November 2010. I should also note that I now serve as Senior Vice President at BPC.

The Task Force's report was designed as a total plan, consisting of policies to spur economic recovery and to reduce the debt as a share of our gross domestic product (GDP). At the time of our report, we set a goal to reduce our debt held by the public to 60 percent by the year 2020 – through spending restraints and revenue increases. We know that today's projections continue to place debt at over 70 percent of GDP ten years from now and rising thereafter. Although our proposals to reform Social Security represented a small piece of the total 10- and 20-year debt reduction that was proposed in the total plan, those savings would grow in the out years.

The Old-Age and Survivors Insurance (OASI) program – or Social Security, for short – has served as a retirement foundation for hundreds of millions of American workers ever since its creation in 1935. Today, low-income seniors – those with incomes below $20,100 – receive over 80 percent of their income from the Social Security monthly check. Even for those in the middle quintile – with incomes between $20,100 and $32,600 – over two-thirds of their monthly income is a result of Social Security. By any reasonable standard, Social Security has been the most successful antipoverty program in the nation's history. The program currently serves over 47 million Americans, and it must continue to serve as a social safety net in the future.

Social Security's fiscal outlook, however, is unsustainable, due largely to three factors.[1] First and foremost, the Baby Boom generation is on the cusp of retirement, carrying with it a wave of new beneficiaries who will draw upon (rather than contribute to) the Social Security Trust Fund. The

[1] The program is unsustainable with current law scheduled benefits and tax rates.

ratio of workers to retirees has been stable for many years, but the retirement of the baby boomers will rapidly shrink this ratio over the next two decades.[2]

Second, Americans are living longer than their predecessors, but today's workers are, on average, retiring earlier than previous generations. Therefore, workers are contributing fewer years of payroll taxes to the Trust Fund, while retirees are collecting more monthly benefits.

Third, due to the rising distributional disparity in wages, a smaller percentage of the nation's income is subject to the Social Security payroll tax, eroding funding for the program.

This combination of demographic, benefit, and revenue effects is already reducing the solvency of Social Security. In almost every year of the program's existence prior to 2010, it collected more revenues from payroll taxes than it paid in benefits to retirees. But in 2010, for the first time in many years, the program's Trust Fund became cash flow negative, meaning that it was taking in fewer revenues than it was paying out in benefits. As a result, Social Security had to draw on its "savings" that have accrued from prior payroll tax contributions.

Just last week, the Congressional Budget Office estimated that Social Security's primary deficit will reach nearly $40 billion this year and exceed $900 billion over the next decade.[3] As a result, unless changes are made, the program will continue to drain the Trust Fund until it is exhausted in 2035. At that point, current law would prohibit the program from borrowing additional monies to continue disbursing scheduled payments; thus, an across-the-board 25-percent cut in monthly benefits would occur, undoubtedly accompanied by severe consequences and hardship for millions of Americans.

While the Trust Fund is "off budget," the current negative cash flow does impact the total federal unified budget and will increasingly add to our public debt in the coming years. The current trajectory of Social Security's finances are unsustainable – both for the program itself and for the broader budget picture. Therefore, the issue is before the public today, not roughly 20 years from now, as some would argue, when the Trust Fund expires.

To ensure that Social Security can provide benefits for future generations of retirees, Congress should adopt measures that avert the impending drop-off in benefits and return the program to

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[2] In particular, the U.S. birth rate fell off its post-war high and appears to have settled at a permanently lower lever thereafter. Thus, there have not been a sufficient number of workers joining the workforce to compensate for the impending exit of the baby boomers (SSA). Also, see the long-range estimates in the 2012 OASDI Trustees report, Table IV.B2 – these can be accessed at: http://www.ssa.gov/oact/tr/2012/IV_B_LRest.html.

[3] Congressional Budget Office, "Combined Old-Age, Survivors, and Disability Insurance Trust Funds – May 2013 Baseline." http://cbo.gov/sites/default/files/cbofiles/attachments/44208_Old%20AgeSurvivorsDisabilityInsuranceTrustFunds.pdf.

long-term solvency. Doing so will require bipartisan cooperation and a modest amount of sacrifice by workers and retirees, but addressing the problem now in a rational and equitable manner will be far easier than waiting until the crisis is near, when much more severe actions would be necessary.

BPC's Domenici-Rivlin Debt Reduction Task Force, after considering an extensive list of options, assembled a package that includes modifications to benefits, revenue increases, and the incorporation of currently uncovered populations into Social Security. As we examined the various options to address the program, the overarching question was not "how do we produce savings for the program," but more, "how can we improve the current system, make it fairer, and ensure that a similarly-robust program is around for decades to come?"

The package in its entirety was scored by the Chief Actuary of the Social Security Administration (SSA), who projected that it would achieve "sustainable solvency" – a metric that means the program would be on stable financial footing for the next 75 years and beyond.

We recognized that Social Security is a defining piece of the country's social fabric. On signing the Social Security Amendments of 1983 into law on April 20, 1983, President Reagan stated:

> "A tumultuous debate about Social Security has raged for more than two decades in this country; but there has been one point that has won universal agreement. The Social Security system must be preserved … Today we reaffirm Franklin Roosevelt's commitment that Social Security must always provide a secure and stable base so that older Americans may live in dignity."

The Task Force's plan, taken in its entirety, would restore the faith of younger generations in the program and restore its viability for them in their old age, thus fulfilling the commitment that society owes to the current generation of American workers, as well as their children and grandchildren.

Our Social Security proposal had eight components – five focusing on benefits, two on payroll taxes, and one on program coverage – but I will primarily discuss four of our benefit adjustment recommendations below, which are the focus of today's hearing: 1) Index the benefit formula to account for longevity; 2) Reduce the growth in benefits for roughly the top one-quarter of beneficiaries; 3) Provide a more robust minimum benefit; and 4) Implement a modest benefit bump for older beneficiaries.

1) Index the Benefit Formula for Longevity

Life expectancies at older ages are continuing to increase in the U.S. and other developed countries. This clearly positive development, however, also increases upward pressure on Social Security spending. Today, the life expectancy of a 65-year-old man has reached 83 years, and that of a 65-year-old woman, 85 years.
Additionally, as a large cohort of baby boomers is set to retire soon, the number of retired workers between now and 2023 is expected to increase by nearly 50 percent, from 37 million today to nearly 55 million. Including survivors, the number of beneficiaries will reach around 63 million.

Beginning in 2023 (after the scheduled increase of the normal retirement age to 67 is completed), we proposed adjusting the benefit formula to account for improvements in life expectancy. Specifically, the replacement rates used to calculate benefits each year for new beneficiaries would be 99.7 percent of what they were in the previous year – which over time would offset about two-thirds of the additional costs associated with estimated longevity increases.

Compensating for increasing life expectancies is the single most important step to ensure Social Security's sustainability for future generations. This policy of indexing the benefit formula to longevity comprised nearly half of the solvency achieved by the Task Force for the 75th year of the Trust Fund. Essentially, indexing for longevity would compensate the Trust Fund for the aggregate life expectancy increase, but protect retirees from individual risk by providing an annuitized benefit that would be unaffected by how long they live. Further, indexing the benefit formula for longevity, as opposed to increasing the age at which a worker could claim benefits, would importantly retain the option to retire at age 62 for those who are unable to work longer. This is especially important in hard industries, such as mining, fisheries, natural resources, and steel mills.

While the Task Force proposed maintaining the early eligibility age at 62, we also recommended that SSA be required to inform recipients more fully about the costs and benefits of taking early retirement. Recent estimates have found that half of American workers declare retirement and begin collecting Social Security benefits at age 62.[4] To the extent possible, extending employment for seniors beyond the early retirement age is a positive to the individual, to society, and to the economy at large.

Retirees have not sufficiently heeded the warnings from SSA about the disadvantages of early retirement – most importantly, reduced benefits for the rest of the retiree's life. This proposal would direct SSA to highlight the benefits of delayed retirement. Each additional year in the workforce translates to higher Social Security benefits each month, regardless of how long the worker lives. Years later, this benefit boost could mean the difference between poverty and a

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[4] John Turner, *Promoting Work: Implications of Raising Social Security's Retirement Age*, Center for Retirement Research at Boston College, Boston College, MA, http://crr.bc.edu/images/stories/Briefs/wob_12.pdf.

more comfortable lifestyle. Yet workers currently appear to be making uninformed or uncalculated decisions.

Specifically, our proposal suggested directing SSA to aggressively revise its communications and messaging regarding the retirement choice, gleaning lessons from the emerging field of behavioral economics. The material provided to workers during their careers about retirement decisions must more clearly show the implications of collecting benefits at different ages. It must highlight the permanent financial consequences of this choice, not only for workers, but for spouses and survivors as well. In particular, SSA should remind workers of uncertainties in retirement, such as potential healthcare costs and the possibility of living for many years after retiring.

There are a variety of potential steps that SSA should consider in its attempts to better inform recipients about the disadvantages of early retirement. For example, SSA should consider providing more potent warning measures that every Social Security participant will notice. The periodic Personal Earnings and Benefit Estimate Statement (PEBES) sent to every worker should more emphatically state that delayed retirements are far more generous on a monthly basis. Another possibility is renaming Social Security's "Early Eligibility Age" as, for instance, the "Reduced Benefit Early Option." Other efforts should improve the ability of older workers to stay in their jobs or transition to less strenuous occupations.

This combination of education and functional approaches will give workers the flexibility to continue making their own choices about retirement, but with the information and incentives to make prudent decisions. The Task Force believed that policies influencing behavior are preferable to those that force people to delay retirement. With workers spending more years in the labor force, production would rise and more retirees would have increased savings and standards of living.

2) Slightly Reduce the Growth in Benefits for Roughly the Top One-Quarter of Beneficiaries

In determining a worker's benefits, Social Security's progressive benefit formula is applied to the worker's average indexed monthly earnings. Currently, this formula for an individual reaching age 62 in 2013 equals:

- 90 percent of the first $791 of the worker's average monthly earnings;
- plus 32 percent of any average monthly earnings between $791 and $4,768;
- plus 15 percent of any average monthly covered earnings above that.

The dollar amounts of $791 (at which the 90 percent replacement rate ends and the 32 percent replacement rate begins) and $4,768 (at which the 32 percent rate ends and the 15 percent rate begins) are known as the program's "bend points." The placement of the bend points is adjusted each year to reflect the change in average wages. If a worker retires before the normal retirement age, the monthly benefit is actuarially reduced, whereas if the worker retires past the normal retirement age, the monthly benefit is actuarially increased.

Beginning in 2023, our Task Force proposed reducing the replacement percentage in the top bracket of the benefit formula from 15 percent to 10 percent over a 30-year period. Thus, under this option (and momentarily ignoring that it will be phased in over time), the benefit formula for an individual turning age 62 in 2013 would equal:

- 90 percent of the first $791 of the worker's average monthly earnings;
- plus 32 percent of any average monthly earnings between $791 and $4,768;
- plus 10 percent of any average monthly covered earnings above that.

This moderate reform would be a particularly progressive change to the benefit structure, and would hold harmless approximately the bottom 75 percent of beneficiaries. While not a major part of the solution, the formula adjustment would help Social Security's sustainability by reducing program costs.

3) Update the Special Minimum Benefit and Include a Child Care Credit

Social Security began to provide the special minimum benefit in 1972 to raise benefits for people who had low earnings over a long working lifetime. The concept behind the minimum benefit was similar to the principle behind Social Security itself: Americans who have contributed to the economy with a full career should be protected and kept free from poverty in retirement.

Unfortunately, the minimum benefit is now outdated. Today, the minimum monthly benefit for an individual ranges from $39 a month for 11 qualifying work years to $804 for 30 years of work coverage. The original minimum level was indexed to prices, whereas benefits under the standard Social Security formula are indexed to earnings. Because earnings have grown faster than prices over the years, standard benefits have risen in real terms while the minimum benefit has not, rendering it largely obsolete.[5] Moreover, the standard Social Security formula has consistently failed to provide decent assistance for career minimum-wage earners; in fact, their benefits put them below the poverty line.

The Task Force proposed updating the special minimum benefit to 133 percent of the federal poverty level (approximately $1,250/month) for retirees with at least 30 years of creditable

[5] For more information, see http://www.socialsecurity.gov/retirementpolicy/projections/special-minimum.html.

work.[6] Updating the minimum benefit would reinforce the program for many retirees in the bottom half of the earnings distribution.

Additionally, consideration should be given, through the implementation of a child care (or caregiver) credit, to long-term workers who take time out of their careers to care for young children. The credit would count as "creditable work" up to eight years of caring for a child under the age of six. Care-giving can cause shocks to work ability and, thus, irregular work histories for individuals. This can lead to inadequate benefits for these individuals when they become eligible for Social Security. Time and income forfeited from working and/or advancing a career to care for a child can have large negative impacts on Social Security benefits to the point that a secure retirement can be jeopardized. The goal of these credits would be to give Social Security benefits to caregivers that more accurately capture an individual's work history and added value to society.

4) Protect the Most Vulnerable Elderly with a Benefit Bump

One of the most vulnerable retiree categories consists of workers who outlive their savings and face increasing medical costs in old age. The percentage of elderly people in poverty rises with age, and the problem is especially prevalent among older women. Many elderly Americans outlive their savings and find it hard to survive on Social Security benefits alone. Older retirees tend to rely on benefits for an increasing proportion of their retirement income. With an eroding savings base and rising medical costs, seniors who live in retirement for many years often find themselves near or below the poverty line.

To address that issue, our Task Force proposed providing beneficiaries with a modest benefit bump – equivalent to 1 percent of the average worker's monthly benefit amount – in each year between ages 81 and 85. This benefit increase will be a uniform dollar amount across the wage distribution, meaning that while the bump would help all older retirees, in particular it would give adequate support to low-income beneficiaries who are most in need.

Measures like the benefit bump for elderly beneficiaries, the increase in the minimum benefit, and the implementation of a child care credit would, if not lift hundreds of Americans out of poverty, at least lessen the burden on them in retirement. These provisions would guarantee that the system continues to provide a good standard of living in old-age for *all* working Americans.

[6] The revised special minimum benefit would ensure that a long-term earner is eligible for a benefit equal to 133 percent of the federal poverty level (about $1,250/month) at the normal retirement age. Earnings required for a year of qualifying coverage would remain at 20 percent of the "old-law" taxable maximum ($15,880 in 2010), but a creditable year would be worth nearly $42 per month (i.e., 30 years * $42 ≈ $1,250/month), rather than approximately $25 under current law. The credit would be indexed to average wage growth rather than prices. A maximum of 30 years of qualifying coverage could be applied, a minimum of 20 years would be required, and up to eight years of caring for a child under age six could be classified as a qualifying year.

Other Components Essential in Achieving Sustainability for Social Security

Change to More Accurate Annual Cost-of-living Adjustment Calculation

The current measure of inflation used to calculate cost-of-living adjustments for Social Security does not accurately capture changes in consumer spending patterns, and it overstates overall inflation. Our Task Force proposed shifting the calculation of annual cost-of-living adjustments from the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) to the "chain-weighted" Consumer Price Index for All Urban Consumers (CPI-U), an alternative measure of inflation developed by the Bureau of Labor Statistics.

This proposal is one that has been stressed in many different reports. Adopting the Chained CPI-U calculation would more accurately capture changes in the cost-of-living without endangering the welfare of low-income and older beneficiaries of Social Security, particularly when combined with the benefit changes that the Task Force recommended.

Expand Social Security Coverage to Newly Hired State and Local Workers

About 96 percent of all workers contribute Social Security payroll taxes and are eligible for benefits upon retirement. The largest group of workers that is not covered consists of about one-quarter of state and local government employees. Unlike private-sector workers (and some public-sector workers), these employees currently are not required to enroll in the system. Our Task Force proposed that all newly-hired employees of state and local governments after 2020 be required to be covered under Social Security. This proposal reflects the goal of increasing the universality of Social Security.

Finally, while we acknowledge that the purpose of this hearing is to address benefits, we feel a balanced approach dealing with additional reforms to Social Security, including increases in revenue, is essential to the viability of the program.

Gradually Raise the Amount of Income Subject to Payroll Taxes

In the 1977 amendments to the Social Security Act, Congress attempted to stabilize the taxable share of covered earnings at the 90 percent level by raising the cap and then indexing the dollar amount of the cap to average annual wage growth. Over the past quarter-century, however, earnings at the top of the wage scale have grown much faster than average wages. As a result, the share of earnings above the cap (and thus untaxed) has grown.

The payroll tax that funds Social Security is currently collected on wage income only up to a maximum of $113,700 – a level that, under normal economic conditions, encompasses about 83 percent of total national wages. Our Task Force proposed raising the cap very gradually, over a 38-year period, to a level covering 90 percent of national earnings. After reaching the 90 percent target, the cap would be adjusted annually to maintain the 90-percent standard.

Cap and Phase Out the Tax Exclusion for Employer-Sponsored Health Insurance (ESI)

Under current law, employer contributions to employee health benefits are not taxable to the employee, causing a revenue loss of hundreds of billions of dollars per year; in fact, the exclusion is the single largest tax expenditure. In addition, many employers have set up a mechanism through which employee contributions come from pre-tax income. The tax exclusion for ESI makes benefits, including high-cost health insurance, a more attractive form of employee compensation than cash wages. In addition to the revenue loss, the exclusion is regressive; it generally subsidizes high-income individuals more than those at lower incomes. We saw no reason for having such an open-ended subsidy mainly for upper-income individuals.

As a result, The Task Force proposed phasing out the tax exclusion for employer-sponsored health insurance. Taxing these insurance premiums (or the increased wage compensation) as regular income would provide additional payroll tax revenue for Social Security, increasing the solvency of the program.

Disability Insurance

While the Domenici-Rivlin Task Force recognizes that the Disability Insurance program must be reformed – its Trust Fund is projected to be exhausted by 2017 – our group did not possess the necessary expertise to put forth comprehensive and specific reforms for that piece of the federal budget.

Conclusion

Social Security reform is a necessity for millions of Americans. Since it was enacted in 1935, Social Security has served as a reliable safety net for beneficiaries throughout retirement. But if the system in place today remains unchanged and continues to run high deficits, as projected, it will exhaust its funds by 2035. The longer policymakers wait to address Social Security reform, however, the more severe and abrupt these changes will have to be to achieve the ultimate goal of long-term solvency.

A number of reputable sources have produced plausible and detailed reports outlining proposals to achieve this objective. I believe that Congress can reach a similar conclusion through bipartisan efforts to enact Social Security reform.

In the early 1980s, Social Security's finances were in a similarly precarious position. The Trust Fund was nearly exhausted and Social Security checks to some 36 million Americans were on the verge of being held up. But President Reagan, Senate Majority Leader Howard Baker (a founder of the BPC), and Speaker Tip O'Neal established the National Commission on Social Security Reform (the Greenspan Commission) and brought together a bipartisan coalition that, along with the Pickle amendment to the Commission's product – which increased the age of full benefit eligibility to 67 – added roughly 50 years of solvency to the Trust Fund.

With the program running a primary deficit today, Congress should consider taking action now in order to gradually phase in the necessary reforms, and provide adequate time for future beneficiaries to adjust. Ensuring the sustainability of a program that means so much to so many should not be partisan. The sooner Congress and the Administration act, the sooner all Americans can rest assured that Social Security will be there for their children and grandchildren in the years to come.

Appendix: Actuarial Scoring of BPC's Domenici-Rivlin Social Security Plan

Bipartisan Debt Reduction Task Force Pan **As of November 10, 2010** (OASDI Trust Fund)	Change in 75-year Actuarial Balance (% of taxable payroll) Projected Deficit = **1.92**	Change in 75th year Annual Balance (% of taxable payroll) Projected Deficit = **4.12**
1) Increase taxable maximum 2 percent per year beginning in 2012 until a taxable ratio of 90 percent is achieved. Additional taxable earnings would enter in the benefit base. Current law bend points and PIA formula factors are unchanged.	0.60	0.68
2) Beginning with the December 2012 benefit adjustment, base the increase on the 3rd quarter to 3rd quarter increase in the Chain-weighted Consumer Price Index for Urban Consumers rather than the Consumer Price Index for Urban Wage-Earners and Clerical Workers. (Related 2009 solvency provision A3.)	0.49	0.70
3) Cover newly hired state and local government employees beginning in 2020.	0.16	-0.12
4) Phase out the income and payroll tax exclusion for employer-sponsored health insurance beginning in 2018. Set exclusion at the 75th percentile of premium distribution in 2018, with amounts above that subject to tax. Reduce the exclusion level by 10 percent annually with exclusion fully eliminated in 2028. (Related 2009 solvency provision F2, but phased-out over a 10-year period rather than all at once.)	0.93	1.06
5) Reduce the upper 15 percent PIA formula factor by 1/3 over a 30-year period beginning in 2023 and through 2052, with an ultimate factor of 10%. Affects OASI and DI.	0.07	0.20
6) Reconfigure the special minimum benefits to ensure that someone earning at least 20% of the old law tax max in each of 30 years would receive a PIA of 133 percent of the federal poverty level, with the formula phased up to 133 percent of poverty linearly for workers over 19 creditable years. Up to 8 years of care-giving could be used as creditable years for care of a child under the age of 6, if it is not otherwise counted as a creditable year (earnings < 20% old law tax max). Scale requirements for DIBs including child care credit years. Effective for new eligibles in 2012. Wage-index the poverty level from 2009 up to 2 years prior to benefit eligibility.	-0.09	-0.14
7) Tax all voluntary salary reduction plans like 401(k)s for payroll tax purposes, effective 2012.	0.22	0.13
8) For those attaining age 62 in 2023 and later, reduce all benefit formula factors by the increase in period life expectancy, with a 4-yr lag (2023 versus 2022 for the first year.) Apply for OASI only, with DI benefits proportionally reduced at conversion.	0.48	1.75
9) Provide the same dollar amount increase to the benefit level of any beneficiary who is 85 or older at the beginning of 2012 or who reaches his or her 85th birthday after the beginning of 2012. The dollar amount of increase equals 5 percent of the average retired worker benefit in the prior year. Phase in at 1% per year from 81 to 85.	-0.13	-0.18
10) Change in personal income tax structure	-0.01	-0.06
Effect of total proposal	**2.51**	**3.48**