Bipartisan Policy Center

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Before the U.S. Senate Committee on the Budget Hearing:

Saving Social Security: Expanding Benefits and Demanding the Wealthy Pay Their Fair Share or Cutting Benefits and Increasing Retirement Anxiety

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Good morning, Chairman Sanders, Ranking Member Graham, and distinguished members of the committee. Thank you for inviting me to testify today about the long-run sustainability and efficacy of Social Security. I commend the committee for focusing on this critical issue in a bipartisan manner.

My name is Shai Akabas, and I am the director of the Economic Policy Project at the Bipartisan Policy Center, a non-profit organization that combines the best ideas from both parties to promote health, security, and opportunity for all Americans. The organization was founded in 2007 by four former Senate majority leaders: Howard Baker, Tom Daschle, Bob Dole, and George Mitchell. BPC drives principled and politically viable policy solutions through the power of rigorous analysis, painstaking negotiation, and aggressive advocacy.

Social Security serves as the foundation upon which most Americans build their lives in retirement. For 85 years, it has paid out benefits to people with disabilities, older people, and their family members, lifting millions of households out of poverty and providing essential financial support. But Social Security faces a serious challenge—the benefits being paid out are outpacing the program's income (mainly payroll tax revenues). The recently released 2022 Social Security Trustees Report underscores this fact, projecting that the Old-Age and Survivors Insurance (OASI) Trust Fund is on track to deplete its reserves in 2034.[1]

My testimony will summarize the ominous outlook facing Social Security today and summarize a package of bipartisan reforms that could address these challenges.

I hope our conversation today leaves you with the following takeaways:

1. Time is running out. To address this problem, Congress must act quickly and in a bipartisan fashion. Delaying necessary reforms will only serve to make them more politically difficult and cause added uncertainty for workers and retirees.

2. There is no silver bullet. Several factors play into Social Security's financial imbalance, requiring a nuanced and thoughtful package of reforms. Failing to enact a comprehensive package of reforms will simply kick the can down the road, pushing responsibility for a long-term solution onto future lawmakers.

3. Enhancing Social Security benefits—particularly for those who most rely on them in retirement—and putting the program on a fiscally sustainable path are not mutually exclusive.

Rather, tackling both e goals simultaneously will be vital to garner the necessary bipartisan support.

The Social Security Situation

For several decades starting in the 1980s, Social Security's income exceeded its expenses, which led to a large buildup in the program's OASI Trust Fund. Unfortunately, that dynamic has flipped, and annual benefits now exceed dedicated revenue—a situation that is projected to persist indefinitely. After the OASI Trust Fund runs out of reserves in 2034—a reality that has long been anticipated absent action from Congress—incoming revenue will only cover 77% of the obligations for OASI, necessitating abrupt benefit cuts that would be devastating for many beneficiaries.[2]

The recent Trustees Report contains some sobering conclusions: To ensure solvency of the combined OASI and Disability Insurance (DI) Trust Funds through the 75-year projection period, Congress would need to immediately raise the payroll tax rate by 3.24 percentage points to 15.64%; reduce benefits for all current and future beneficiaries by around 20% (or around 24% for only beneficiaries who become eligible in 2022 or later); or adopt some combination of these approaches.[3]

If policymakers wait until the combined Trust Fund's depletion in 2035, much larger changes will be required—and the burdens will fall on narrower group of Americans. Specifically, lawmakers would then have to raise the payroll tax by one-third (4.07 percentage points) to 16.47%; reduce benefits by one-quarter; or adopt some combination of these approaches. The alternative would be an unprecedented departure from the pay-as-you-go structure of the program, with legislative changes instead allowing it to begin permanently drawing from general government revenue. This would sacrifice Social Security's special status as a program walled off from the rest of the budget, making it compete for resources with other priorities at a time when the nation's fiscal house is already in rough shape, with debt held by the public nearly equal to gross domestic product and headed higher.[4] This would be irresponsible policymaking.

As the numbers make clear, delaying action on Social Security solvency has significant implications not only for taxpayers and retirees, but for political feasibility and intergenerational equity as well. Before delving further into the problems at hand and outlining possible solutions, I want to outline the two principles that must guide any reforms to the Social Security program:

1. <u>Acting as soon as possible is paramount.</u> The longer Congress waits to strengthen Social Security's finances, the more drastic the changes will have to be, and the more burden will fall upon those who played little or no role in creating the imbalance facing the program today. Moreover, any delay adds significant uncertainty to retirement planning for the large majority of Americans whose retirements will extend beyond 2034. Failing to enact reforms will simply kick the can down the road, pushing responsibility for a long-term solution onto future lawmakers, who will have to decide between inconceivable benefit cuts, impractical tax increases, or the abandonment of the program's historical financing mechanism.

2. <u>Any legislative action must garner significant bipartisan support.</u> Working across the aisle is not only a best practice in general for enacting durable policies but also a requirement for changes to Social Security, which require a supermajority in the Senate. Lawmakers should abstain from pronouncements like "no tax increases" and "no benefit cuts," whether they apply across the

board or for certain subsets of the population. Red lines such as these only put obstacles in the way of action. Social Security's financial challenge affects nearly our entire society, and the solutions will require a broad-based approach.

Drivers and Other Issues to Address

Shifting demographics in the United States work against Social Security's finances. Since 1965, the ratio of covered workers paying into the system to the number of Americans drawing benefits has dropped from four-to-one in 1965 to just under three-to-one in 2021. The ratio is projected to drop to under 2.5-to-one by 2030 as Baby Boomers continue to retire and increases in average life expectancies have not been accompanied by longer working lives.[5]

Moreover, Social Security's tax base is shrinking as a proportion of national earnings. Reforms to the Social Security program in 1977 raised the taxable maximum to $35,700, a level that covered 90% of total national earnings in 1983.[6] Today, the maximum remains indexed to average wage growth. While the portion of workers whose earnings are above the taxable maximum has remained steady since the 1980s at approximately 6%, because earnings for workers at the top of the earnings distribution have grown faster than average wages, the percentage of earnings above the taxable maximum has increased.[7] Indeed, for 2022, Social Security taxes are projected to cover only 80% of total national earnings.[8]

In addition to the financing challenge, Social Security benefits were not designed for a 21st century workforce. The current benefit structure falls short of achieving many retirement security objectives, such as incentivizing work and minimizing poverty.

Social Security benefits are linked to earnings. As workers near retirement, they continue to pay taxes on earnings to support the program, yet often accrue little or no additional benefits as a result.[9] This sends the wrong message, and the program should be recalibrated to encourage work at older ages. Working longer allows more time to accumulate savings, shortens the period of retirement consumption that must be financed by savings, and facilitates later claiming of Social Security benefits (which results in larger monthly payments). On top of these advantages for personal retirement security, a longer average working life yields additional payroll-tax revenue for the Social Security program and benefits the broader economy. Thus, better work incentives within Social Security would improve both retirement security and the financial condition of the program.

Because the program is designed as an earnings-based benefit, Social Security in isolation fails to adequately support individuals who have lower lifetime earnings. While the progressive benefit formula ensures that lower-earning workers receive a higher return in benefits relative to their contributions than higher-wage earners, many retirees near the bottom still struggle. This is especially the case if they had unstable employment, stopped working at a relatively early age, or both. Realistically, many of these retirees had insufficient earnings during their working years to accumulate any significant savings to supplement their Social Security benefits. Even among middle-income workers who enter retirement with outside assets, those who claim Social Security benefits early at a reduced level and live unexpectedly long lives may find their monthly income inadequate.

An added factor to consider is that not all Americans have seen longevity gains over the past several decades. As of 2014, life expectancy at age 50 for the lowest-income quintile had actually decreased in recent years, while high-income individuals have experienced large increases. This dynamic has a significant effect on the distribution of benefits within the system.[10]

Spousal and survivors benefits are other aspects of the Social Security program that seem outdated or ineffective at ensuring income adequacy. Spousal benefits, for example, were developed in the context of early-20th century assumptions about family structure. In 1950, just one-third of women over the age of 16 participated in the workforce (compared to more than 86% of men), making Social Security benefits a necessary source of support for spouses throughout much of the income distribution. Today, in contrast, workforce participation of women has nearly doubled to roughly 57% while the rate has dropped to 68% for men.[11] Yet, even as women have far more opportunities for employment today, the benefit structure for non-working spouses remains the same, providing unnecessary support to the spouses of high-income individuals, who can in some cases receive greater monthly benefits than a full-career, low-income worker.

Survivors benefits—where a surviving spouse is provided the larger of the couple's two earned benefits—were also designed for a workforce in which one-earner couples were predominant. As a result, many widows and widowers now struggle to support themselves after the death of a spouse. After that moment, household Social Security benefits can fall by as much as half, but household costs rarely decline commensurately.[12] Thus, survivors benefits often do not provide adequate income to maintain a widow's or widower's standard of living, and the sudden loss of income can even push some below the poverty level.

Finally, it is important to recall that Social Security is a social *insurance* program. As of Urban Institute data from 2014, Social Security benefits comprised more than 70% of disposable income for older Americans in the bottom 40% of the lifetime-earnings distribution.[13] In contrast, for higher earners, Social Security is just a small slice of their overall retirement picture. That is consistent with President Franklin Roosevelt's vision for the program, when he stated: "We can never insure one hundred percent of the population against one hundred percent of the hazards and vicissitudes of life, but we have tried to frame a law which will give some measure of protection to the average citizen and to his family against the loss of a job and against poverty-ridden old age."[14] When considering reforms, policymakers should strive to preserve and enhance this insurance component for those who have struggled in life while modestly scaling back support for those who have been more financially successful.[15]

For millions of Americans, Social Security benefits provide the critical foundation for both planning and realizing a secure retirement. Yet, those who rely on the program do not know what changes to expect in the context of the program's troubled financial future.

A Comprehensive Approach

In 2016, BPC convened a bipartisan Commission on Retirement Security and Personal Savings, co-chaired by former Senator Kent Conrad and Jim Lockhart, the former deputy commissioner of the Social Security Administration. The Commission spent two years studying the status of retirement security in the U.S. and made recommendations in six key areas, including "Strengthening Social Security's Finances and Modernizing the Program."[16] The Commission's recommendations would make Social Security solvent for 75 years and beyond, avoid the 23% benefit cut that is set to take effect, and give Americans certainty about what to expect from the program as they prepare for retirement.[17] Moreover, the recommendations reflect a balanced blend of new revenue and restraints on benefits.

To accomplish this solvency, the Commission's plan included 13 recommendations:[18]

1. Increase the progressivity of the benefit formula. The formula for calculating a Social Security beneficiary's primary insurance amount (PIA) is progressive, with earnings at lower levels replaced at higher rates. This formula is applied to the average of a worker's highest (wage-growth-adjusted) 35 years of covered earnings, known as average indexed monthly earnings (AIME). The current benefit formula includes two "bend points" at which the marginal replacement rate for earnings, known as the PIA factor, changes. The plan would revise these bend points and PIA factors to make the benefit structure more progressive.
2. Apply the benefit formula annually to earnings to reward continued work more evenly. The current Social Security benefit formula does not distinguish between higher earners who work fewer years and lower earners who work many years, often unintentionally redistributing income toward households with little need for extra support. A related issue is that Social Security provides limited work incentives to nearly all workers as they reach older ages. To address these skewed incentives, the plan would apply the replacement-rate formula to each individual year of a worker's earnings to calculate an "annual PIA." These amounts would then be added up and averaged to calculate a worker's actual Social Security benefit, much in the same way as a typical defined benefit program.
3. Establish a basic minimum benefit to enhance Social Security for beneficiaries with low incomes. Millions of older Americans live with very low incomes, in or near conditions of poverty. Some of these individuals worked intermittently and for low wages, due to a variety of circumstances, and therefore earn only meager Social Security benefits. Thus, the plan would establish a new basic minimum benefit (BMB) within Social Security to supplement standard benefits and reduce poverty among these OASI beneficiaries.
4. Index the retirement age to longevity to reflect ongoing increases in average life expectancy. To reflect changes in life expectancy, the plan would gradually raise both the "full retirement age," currently set at 67, and the maximum benefit age, currently 70. Each would rise at a rate of one month for every two years, roughly paralleling projected increases in longevity.
5. Use a more accurate measure of inflation for Social Security's cost-of-living adjustments. Social Security beneficiaries receive an annual cost-of-living adjustment (COLA) on their benefits to reflect inflation, as measured by the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). Many economists believe that the CPI-W overstates actual inflation because the measure insufficiently accounts for consumers' ability to change purchasing patterns in response to relative price changes (among other computational issues). The plan would link COLAs to the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), an alternative measure of inflation developed by the Bureau of Labor Statistics that better accounts for substitution effects and fixes technical issues with the CPI-W. Notably, the C-CPI-U is now used for federal income tax brackets, as well.
6. Cap and re-index the spousal benefit. Individuals who are either married or divorced (after a marriage that lasted at least 10 years) may be entitled, regardless of their work history, to a Social Security spousal benefit of up to half of the PIA of the individually entitled worker. The current spousal benefit, however, fails to reflect changes in women's workforce participation since the time when Social Security was first enacted. As a result, the spousal benefit provides the greatest advantage to certain high-income families who can afford to have only one earner and, in this way, undermines the progressivity of Social Security. The plan would start by limiting

spousal benefits for high lifetime earners and then slow spousal benefit growth for more households over time.

7. Enhance survivors benefits to help widows and widowers maintain their standard of living. On average, survivors experience roughly a one-third reduction in household OASI benefits when their spouse dies. For two-earner couples with similar earnings, household benefits can drop by as much as half. With more two-earner couples in the workforce than ever before, this reduction often means that remaining benefits are inadequate, as expenses for the surviving spouse generally do not fall by half. The plan enhances survivors benefits so that widows and widowers receive 75% of their deceased spouse's benefit in addition to the entirety of their own benefit while offsetting the cost of this change by modestly lowering benefits when individuals in married households first claim.
8. Reinstate benefits for college-aged children of deceased beneficiaries and certain other Social Security beneficiaries. Most young adults receive some support from their parents during their college-age years. The plan would allow adult children who are enrolled in an institution of higher education to collect benefits up to age 22 (instead of the current maximum age of 18).
9. Raise the maximum taxable earnings level. While the maximum level of taxable earnings (also known as the "taxable maximum") for Social Security's payroll and self-employment taxes is indexed to average wage growth, the percentage of earnings above the taxable maximum has increased over time since earnings for workers at the top of the wage distribution have grown faster than average wages. The plan would increase the taxable maximum to generate additional program revenues and prevent further erosion of Social Security's tax base.
10. Gradually increase the payroll-tax rate by 1 percentage point. The plan would increase the payroll- and self-employment-tax rates by 1 percentage point (0.5 percentage points for both employees and employers). The increase should be implemented gradually, by raising the combined payroll tax paid by employees and employers 0.1 percentage points each year for the next 10 years.
11. Increase taxes on benefits for high-income beneficiaries. The plan would include in taxable income all benefits received by Social Security beneficiaries with adjusted gross incomes (AGI) of over $250,000 (or $500,000 for couples) and index both thresholds to average wage growth.
12. Replace the windfall elimination provision (WEP) and government pension offset (GPO) with a pro-rated benefit for workers with non-covered earnings. The WEP and GPO are designed to limit Social Security benefits for people who worked most of their careers in non-covered employment, but the details are quite complicated and sometimes produce inequitable outcomes. Instead, the plan would pro-rate benefits by the fraction of an individual's total lifetime earnings that were covered by Social Security.
13. Improve the Disability Insurance (DI) program. In 2015, Congress and the president acted to address the impending exhaustion of the Disability Insurance Trust Fund, testing reforms to reward returning to work and reallocating payroll tax revenues between the two trust funds to extend solvency. The legislation included some policies that had been recommended by the Bipartisan Policy Center's Disability Insurance Working Group, which proposed a variety of ways to improve the DI program to better meet the needs of Americans with disabilities. But more needs to be done, and the other recommendations of the working group are a good place for policymakers to start.[19]

Beyond making Social Security financially sound, enacting these recommendations would dramatically reduce poverty among retirees by making Social Security's benefit distribution more progressive and by enhancing benefits for widows and widowers. Over a lifetime, the average household in the bottom two quintiles of earners would receive higher benefits than scheduled levels under these proposed reforms, and middle earners would receive benefits roughly at scheduled levels. Nearly all the benefit savings would come from beneficiaries in the top two quintiles of the lifetime earnings distribution.[20]

Although this framework represents a balanced and nuanced approach to restoring solvency, it was recommended six years ago. Since then, the problem has grown, and the time to address it has shrunk. In order to restore long-term solvency today, policymakers would either need to phase in these policies much more rapidly, increase the size of the proposed adjustments, incorporate additional benefit or revenue changes, or some combination. Let me be clear: If you wait another six years to act, it will become nearly impossible to retain Social Security's traditional structure without aggressively curtailing benefits for current beneficiaries.

Improving Claiming Behavior

Any discussion of enhancing Social Security's capacity to strengthen Americans' finances in retirement would be incomplete without mentioning the importance of the claiming decision and policymakers' ability to improve outcomes in that area. One of the key financial decisions facing older Americans is when to claim Social Security retirement benefits. Although these benefits are available as early as age 62, claiming later permanently raises monthly benefits, with the maximum benefits available to those who claim at age 70. Delaying claiming is thus equivalent to purchasing a greater inflation-adjusted annuity that will be paid for as long as the beneficiary lives. Most people, however, do not claim Social Security at their optimal age, usually because they claim too early.[21] By some estimates, sub-optimal claiming decisions will cost current retirees $3.4 trillion in retirement income.[22]

Unlike the contentious debates over solvency, this is an example of how public policy could enhance retirement security simply by providing better information at better times. One way that lawmakers could help would be by creating a safe harbor for workplace retirement plan sponsors that responsibly assist participants in making informed decisions about when to claim Social Security benefits or about using their private retirement savings to bridge to a later claiming age. Congress could also instruct the Social Security Administration to rename the program's claiming ages with terminology that better informs prospective beneficiaries or to revisit the efficacy of the Retirement Earnings Test, which is poorly labeled and often misunderstood in a way that discourages work.[23]

In addition to improving individual retirement outcomes, better claiming decisions can lead to better decisions about when to retire. This, in turn, can result in more Americans in the workforce, easing labor market supply shortages and supporting stronger economic growth.

BPC is currently providing technical assistance to a bipartisan group of Senate offices on legislation that would help people make more-informed decisions about when to claim Social Security. I would be happy to discuss this promising area further in the Q&A.

The Three-Legged Stool

Although Social Security plays an integral role in Americans' retirement security, it is only part of the picture. Private savings and workplace retirement plans form the other posts of the proverbial "three-legged stool" model of retirement security. BPC's Commission approached its charge holistically because that is how people think about and plan for retirement.

Many Americans are anxious about retirement (if they believe they will be able to retire at all), and for good reason—the three-legged stool is unstable at best. Beyond Social Security's unsustainable finances and outdated structure, too many Americans lack access to workplace retirement savings plans, do not have enough personal savings for short-term needs, risk outliving their retirement savings, fail to build and use home equity to support retirement security, and lack basic knowledge about personal finance.[24] But the solution is to reinforce—not throw out—the stool.

BPC's Commission put forward a comprehensive package of bipartisan proposals to address these key private-sector challenges facing American households—proposals that complement one another and create a policy solution far more effective than a piecemeal approach. In particular, federal policy that helps to ensure nearly all working Americans have access to a well-designed workplace retirement savings plan can dramatically increase the funds that households are able to accumulate with the support of their employer. Modeling conducted for BPC's Commission showed that these additional savings can more than offset necessary Social Security benefit adjustments for Americans in the upper half of the lifetime earnings distribution. This type of integrated solution can ensure that conversations about Social Security solvency do not just entail painful decisions about curtailing benefits and raising taxes, but rather improved retirement security for nearly all Americans.

In sum, policymakers must shore up Social Security's OASI Trust Fund, but they should not stop there, and I hope you consider the full package of reforms outlined in the report.

Need for Bipartisanship

The BPC Commission's report is far from the only solvency plan that has been proposed in recent years. In fact, several have been submitted by current members of Congress. Whether it is Chairman Sanders' and Congressman Peter DeFazio's (D-OR) Social Security Expansion Act (2019, updated for this hearing), Congressman Sam Johnson's (R-TX) Social Security Reform Act (2016), or Congressman John Larson's (D-CT) Social Security 2100 Act (2019), all these members deserve significant credit for putting forth credible solutions to this politically vexing challenge. But as mentioned, the ultimate fix will need bipartisan support, so while components of these proposals can be part of a package, the red lines embodied by each of them must be relaxed.

This retirement security challenge—headlined by Social Security's financial shortfall—has existed for a long time, and unfortunately, as of 2018, it had spurred little recent action from policymakers. Out of that reality, we launched the Funding Our Future initiative, in partnership with Ric Edelman of Edelman Financial Engines, to showcase the broad and collaborative base of support that retirement security has and requires. The U.S. retirement system's shortcomings are significant and will not disappear overnight. Our coalition's strength is directly tied to the bipartisan nature of this issue, allowing many voices to come together with the shared goal of making long-term financial security a reality for households across the country. Because of this broad tent, we now have roughly 60 organizations involved in this effort, spanning the academic, nonprofit, trade association, and corporate sectors. Our work also recognizes that retirement security cannot be viewed in a vacuum—preparing for retirement is a lifelong pursuit that can get knocked off course by all sorts of financial pressures.

Although the coalition does not take a stance on legislation, the effort strives to elevate the solutions available—at both the federal and state levels and within the private sector—to tackle these challenges.

Three key goals representing the financial lifecycle are shared by all our partners: (1) make saving easier for Americans at all ages; (2) help them transform nest eggs into retirement income; and (3) ensure that Social Security continues to be financially stable, both for current and future retirees.

The function of our coalition is to highlight the gaps in our existing system, encourage more people to save, advance financial literacy, and promote solutions that ultimately improve financial security for all Americans as they age. We have been honored to collaborate with several members of Congress from both parties in our work, and we welcome the opportunity to engage further with any of you who are looking to advance this critical issue.

I want to conclude by thanking the Committee once again for convening this hearing. Social Security solvency often feels like an intractable problem, but with your continued leadership and bipartisan collaboration—as was recently on display with COVID-relief and the infrastructure law—progress is possible. I look forward to your questions.

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[18] CRSPS, 89.

[19] For the complete recommendations of the Working Group, please see: BPC's Disability Insurance Working Group, *Improve the SSDI Program and Address the Impending Trust Fund Depletion*, August 2015. Available at: http://bipartisanpolicy.org/library/ssdi-program/.

[20] CRSPS, 84.

[21] Jason J. Fichtner, Gary Koenig, Shai Akabas, and Nicko Gladstone, *How to Help Americans Claim Social Security at the Right Age*, August 2020, 4. Available at: https://bipartisanpolicy.org/report/how-to-help-americans-claim-social-security-at-the-right-age/.

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[24] CRSPS, 7.