U.S. Senate Special Committee on Aging

Analytical Report
Majority Staff

An Analysis of the President's Commission to Strengthen Social Security Models

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U.S. Senate Special Committee on Aging

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The Status Quo Is Unsustainable

Social Security is the most successful government program in the United States. However, the Social Security Board of Trustees has consistently found in its annual reports that the program will become insolvent, and is unsustainable with the combination of benefit levels and tax rates scheduled in current law. Along with Medicare, these two programs will begin to put a serious burden on the federal budget **within five years**. [1]

The good news is that Social Security **benefits for today's retirees and those near retirement will be there regardless** of any changes currently under consideration.

Social Security is in need of strengthening if we intend for the children and grandchildren of today's retirees to receive the benefits they have been promised.

Pressures on the Social Security program begin in 2008 with the retirement of the baby boom generation -- those born between 1946 and 1964. The number of retirees is expected to rise by 76 percent between 2000 and 2025, from 35.9 million to 63 million Americans.[2] Conversely, the number of workers is projected to grow by only 16 percent. As a result, the number of workers paying into Social Security per beneficiary is projected to decline from 3.3 today to 2.2 by 2030 and to 1.8 by 2075. [3] This trend could be worsened by medical breakthroughs further extending the life expectancy of Americans.

There is still time to modernize the system without painful adjustments. In recent testimony before the Senate Special Committee on Aging, Chairman of the Federal Reserve Board Alan Greenspan made the point that choosing the Social Security status quo is unsustainable at current benefit levels. The Social Security Administration says that, "*the probability of achieving solvency over the 75-year period under current law is very low*" [4] In this year's report, the Social Security Board of Trustees, using a stochastic analysis, found there is less than a 2.5 percent, or a 1-in-40, chance that Social Security will remain solvent absent Congressional action to strengthen the program.

> ***"Acting soon reduces the likelihood that Congress will have to choose between imposing severe budget cuts and benefit cuts or unfairly burdening future generations..."***
>
> *David Walker, Comptroller General, General Accounting Office.*
> *July 29, 2003 before the Senate Aging Committee*

[1] Statement of Thomas R. Saving Public Trustee of the Social Security and Medicare Board of Trustees before the Senate Special Committee on Aging. July 29, 2003.

[2] "The Financial Outlook for Social Security and Medicare", The Congressional Research Service. April 28, 2003.

[3] Ibid.

[4] 2003 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, March 17, 2003.

> ***"When the trust fund is exhausted, there would be a 27 percent reduction in scheduled benefits. Benefits would continue to decrease every year thereafter, and by 2077, the reduction would be 35 percent."***
>
> *James Lockhart, Deputy Commission, Social Security Administration.*
> *July 29, 2003 before the Senate Aging Committee*

The 2003 Social Security Trustees Report shows cash flow to the Social Security trust fund turns negative in 2018. **The Social Security trust fund will be exhausted by 2042**. At that point the system will only be able to pay 73 percent of the benefits it currently promises and by 2077 it will only be able to pay 65 percent of promised benefits. [5]

The Social Security Trustees report shows that worker under the age of 27 will not reach full retirement age until after the trust fund is exhausted. The system that they have paid into throughout their lives will be unable to pay the benefits promised throughout their working career.

More importantly, under current law Social Security is bound to put an unbearable burden on the federal budget. By 2020 the program's **annual deficits** will reach $57 billion, by 2025 it will reach $164 billion, and by 2035 it will reach a deficit of $322 billion. In the long run, by 2078, the program will have incurred a $25 trillion total actual debt (in 2003 dollars) between promised benefits and payroll taxes.[6]

Social Security will not be "*fixed*" even if the 75-year deficit is resolved. Critics of strengthening Social Security with personal retirement accounts claim that the program's problems can be solved by raising payroll taxes to match "*the average percentage difference between revenues and outlays*" over the 75-year period. This is a misleading argument because it ignores the annual deficit during the 76th year.

As each year passes, the system loses one year of surplus at the front of the 75-year window and adds another year of deficit at the end of that 75-year window.

For every year we wait to modernize Social Security, we worsen the problem and make any solution more painful.

> ***"The program's annual cash flow is projected to become negative in 2018. Social Security's annual cash deficit will place increasing pressure on the rest of the Federal budget..."***
>
> *David Walker, Comptroller General, General Accounting Office.*
> *July 29, 2003 before the Senate Aging Committee*

5 Ibid.

6 Ibid.

The President's Commission to Strengthen Social Security

Guiding Principles

President Bush appointed 16 members to the Commission to Strengthen Social Security in 2000. The Commission included eight Republicans and eight Democrats. Members included the late Senator Daniel Patrick Moynihan, who served as a co-chair for the Commission. The President directed the Commission to recommend ways to "*modernize and restore fiscal soundness to the Social Security system*" in accordance with six guiding principles:

- ***Modernization must not change Social Security benefits for retirees or near-retirees.***
- ***The entire Social Security surplus must be dedicated to Social Security only.***
- ***Social Security payroll taxes must not be increased.***
- ***Government must not invest Social Security funds in the stock market.***
- ***Modernization must preserve Social Security's disability and survivor's components***
- ***Modernization must include individually controlled, voluntary personal retirement accounts (PRAs), which will augment the Social Security safety net.***

The Commission's Report

On December 21, 2001 the Commission issued a final, unanimously approved report including three options for reforming Social Security. Each of the three plans would allow workers to choose to invest in PRAs.

Model 1

• Workers would be able to invest 2 percentage points of their Social Security payroll taxes into a PRA.

• Workers who invest part of their payroll taxes in a personal account would receive all of the benefits accumulated in the account. In exchange, current law benefits would be reduced by the amount that investment would have purchased form the traditional retirement system, assuming a 3.5 percent real rate of return. Total benefits will be higher if personal accounts exceed a 3.5 percent return.

• No other changes would be made to the program.

• **General Revenue Flow** requirements would be $1.8 trillion lower than required to maintain solvency over the next 75 years. The general revenues required to maintain solvency are $22 trillion under promised benefits. Model 1 **general revenue flow** requirements are $20.2 trillion.

• Plan one **would not restore solvency over the 75-year projection window** to the system.[7]

[7] Assumes 67 percent participation in personal retirement accounts, per the Social Security actuary.

> ***"Our Social Security challenge is more urgent than it may appear. Failure to take remedial action will, in combination with other entitlement spending, lead to a situation unsustainable for both the federal government and, ultimately, the economy…"***
>
> *David Walker, Comptroller General, General Accounting Office July 29, 2003 before the Senate Aging Committee*

Model 2

• Workers would be able to invest 4 percentage points of their payroll taxes to a PRA account up to an annual maximum of $1,000, which would be indexed to average wage growth.

• Workers who invest part of their payroll taxes in a personal account would receive all of the benefits accumulated in the account. In exchange, their benefits would be reduced by the amount that investment would have purchased form the traditional retirement system, assuming a 2 percent real rate of return. Total benefits will go up to the extent that their personal account beats a 2 percent return.

• Plan 2 includes a **minimum benefit** (120 percent of the federal poverty level for those who earned the minimum wage for at least 30 years) and **enhanced widow(er)s' benefits** (75 percent of the couple's pre-death benefit).

• **General revenue flow** requirements would be $15 trillion lower than required to maintain solvency over the next 75 years.[8] The general revenues required to maintain solvency are $22 trillion under promised benefits. Model 2 **general revenue flow** requirements are $5 trillion.[9]

• **Plan 2 would restore solvency over the 75-year projection window AND *sustainable solvency beyond the 75-year window*** to the Social Security system.

Model 3

• Workers would be able to invest 2.5 percentage points of their payroll taxes to a PRA account up to an annual maximum of $1,000 a year if they choose to contribute 1 percent of their annual earnings to the accounts.

• Workers who invest part of their payroll taxes in a personal account would receive

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Memo from Stephen C. Goss, Office of the Chief Actuary, Social Security Administration, "*Revisions of Estimated Unified Budget Effects and Summary General Revenue Requirements for Commission Models—Information*"

[8] The 2003 Social Security Trustee's Report uses a discounted present value in 2002 dollars to determine the unfunded promises of the current system. $3.4 trillion unfunded promises is equal to the status quo.

[9] Assumes 67 percent participation in personal retirement accounts, per the Social Security actuary. Memo from Stephen C. Goss, Office of the Chief Actuary, Social Security Administration, "*Revisions of Estimated Unified Budget Effects and Summary General Revenue Requirements for Commission Models—Information*"

all of the benefits accumulated in the account. In exchange, their benefits would be reduced by the amount that investment would have purchased from the traditional retirement system, assuming a 2.5 percent real rate of return. Total benefits will go up to the extent that their personal account beats a 2.5 percent return.

• Plan 3 also includes a **minimum benefit** (up to 111 percent of the federal poverty level for those who earned the minimum wage for at least 30 years) and **enhanced widow(er)s' benefits** (75 percent of the couple's pre-death benefit instead of 67 percent as provided under current law).

> ***"Early initiatives to address the economic effects of the baby-boom retirements could smooth the transition to a new balance between workers and retirees. If we delay, the adjustments could be abrupt and painful."***
>
> *Alan Greenspan, Chairman of the Federal Reserve Board. February 27, 2003 before the Senate Aging Committee*

• Plan 3 calls for new (unspecified) dedicated revenue sources for Social Security just as the benefits "*promised*" benchmark.

• **General Revenue Flow** requirements would be $11.8 trillion lower than required to maintain solvency over the next 75 years. The general revenues required to maintain solvency are $22 trillion under promised benefits. Model 3 **General Revenue Flow** requirements are $10.2 trillion. [10]

• **Plan 3 would restore solvency over the 75-year projection window** to the Social Security system.

The GAO's Report on the President's Commission to Strengthen Social Security

On January 15, 2003 David Walker, Comptroller General of the General Accounting Office, testified before the Senate Special Committee on Aging. The Comptroller General outlined the GAO's assessment of the report of the President's Commission to Strengthen Social Security.

The GAO's report, titled "***Analysis of Reform Models Developed by the President's Commission to Strengthen Social Security***," validated several goals highlighted by the Commission's work.

Focus of the GAO Report

The GAO focused their analysis on Model 2 of the three models put forth by the President's Commission to Strengthen Social Security. **In all three of the models, the current benefit structure for current and near retirees is maintained**.

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[10] Assumes 67 percent participation in personal retirement accounts, per the Social Security actuary. Memo from Stephen C. Goss, Office of the Chief Actuary, Social Security Administration, "*Revisions of Estimated Unified Budget Effects and Summary General Revenue Requirements for Commission Models—Information*"

> ***"In my view, there is a window of opportunity to craft a solution that will protect Social Security benefits for the nation's current and near-term retirees, while ensuring that the system will be there for future generations…."***
>
> ***"I believe it is possible to structure a Social Security reform proposal that will exceed the expectations of all generations of Americans…"***
>
> *David Walker, Comptroller General, General Accounting Office*
> *January 16, 2003 before the Senate Aging Committee*

Commission Model 1 was projected to not be solvent within the 75-year actuarial window, and therefore was not included in the GAO's report. Commission Model 3 did prove to be solvent but judged to be potentially less sustainable than Model 2 outside the 75-year window. **Commission Model 2 achieves both projected solvency over the 75-year projection window used by the Social Security actuary and sustainable solvency beyond the 75-year window.**

Major Findings of the GAO Report

- GAO shows the Commission's personal account framework (Models 2 and 3) would provide for **FULL** payment of promised benefits to beneficiaries now in or near retirement. GAO states, "*Model 2: Maintains current benefit structure for current and near retirees*." -- p. 38. Same finding for Model 3 -- page 79. Model 1 was not studied by GAO but also contains no changes for current and near retirees.

- GAO shows that those choosing personal accounts (Models 2 and 3) would receive higher Social Security benefits than those who do not choose personal accounts. GAO states, "*Median monthly benefits. . . for those choosing individual accounts are always higher. . . than for those who do not choose the account, and this gap grows over time*." -- p.6.

- Average monthly benefits under the Social Security personal account framework would be highest for low-income individuals: *See Figure 7, p. 42*, showing greatly increased benefits for low-income earners and for all but one birth years shown.

- GAO shows the Commission's Model 2 would fix Social Security permanently (beyond the SSA actuaries' 75-year window. GAO states, "*As estimated by the actuaries, Model 2, with either universal or zero participation in voluntary individual accounts, is solvent over the 75-year projection period, and the ratio of annual income to benefit payments at the end of the simulation period is increasing.*" – p.4

Benefit Levels Relative to General Revenue Flow

One of the most stunning features of the President's Commission framework that is often overlooked by analysts and the press is the generally **favorable tradeoff between higher benefit levels and lower general revenue flows compared to benchmarks**. This feature more than any other, exceeds the expectations set for personal retirement accounts by critics and advocates. It also exceeds public expectations of the personal retirement account framework for strengthening Social Security.

Higher benefit levels are especially important for low-income earners and the disabled. Lower general revenue flows compared to the benefits "*promised*" benchmark put reduce the pressure for increased public debt financing, increased tax burdens, and pressure to reduce spending on other government programs including Medicare, medical research, education, transportation, and other federal priorities.

The charts at the end of this report highlight the Social Security actuarial benefit projections for benefits "*payable*," benefits "*promised*," today's benefit, and three yield (rate-of-return) assumptions. These benchmarks are presented for four different annual earnings assumptions ranging from $15,875 to $84,900 per year for six representative cohorts of retirees (2012, 2022, 2032, 2042, 2052, and those retiring in 2075—all at age 65).

The Commission's personal retirement account models provided two key positive features: (1) provide full benefits for current and near retirees, and (2) reduced **General Revenue Flow**, projected to be $22 trillion[11] if we continue to pay retirees their "*promised*" benefits financed by debt, income tax revenue, or cuts in other programs.

The following is an analysis of how the benefit levels of personal retirement accounts relate to the overall amount of **General Revenue Flow** for Model 2 and Model 3 as compared to both the current "*payable*" benefits and current "*promised*" benefits of the Social Security System. Similar to the GAO, we will focus on the plans that are solvent over the 75-year projection window—Models 2 and 3.

Rates-of-return (or yield) assumptions were made by the Social Security actuary to help understand the range of possibilities for projected benefit levels. Yield assumptions used by the actuaries for analyzing the President's Commission models were 3.0 percent per year, 4.6 percent per year, and 5.3 percent per year.

It should be noted that the rates-of-return (or yield) provided by the Social Security actuaries are based on real dollars. In short, these rates represent yields over and above inflation. For example, if inflation is projected to be 1 percent and the real rate-of-return is projected to be 3 percent (as in the low-yield benefit projection), this corresponds to a 4 percent overall (or nominal) return.

Also, rates-of-return provided by the Social Security Administration actuaries only pertain to the accumulation (pre-retirement) phase. The lowest fixed-annuity real return (3 percent) is assumed for projections in retirement years. Using a consistent real rate-of-return throughout the retirement years would produce higher benefit

[11] In constant 2002 dollars

estimates for the personal account models shown in Commission report.

There are two benchmarks used for this analysis. The first benchmark is benefits "*payable*." The benefits payable benchmark assumes that no action is taken to prevent benefit cuts in the future. Benefit cuts would range from 27 percent to 35 percent if no action is taken to strengthen Social Security. This is often referred to as the "*do nothing*" or "*status quo*" plan.[12]

The second benchmark used by the Social Security Administration actuaries for this analysis is referred to as the benefits "*promised*" benchmark. This benchmark assumes large **general revenue flows** financed by either significant increases in national debt, higher income taxes, or drastic cuts in other federal programs. Another action to support this level of benefits would be to raise payroll taxes by 3 to 4 percent of payroll.

The following analysis can be verified by viewing the charts at the end of this report.

Model 2

Restoring long-range solvency to the Social Security trust fund would be accomplished under Model 2 of the personal retirement accounts designed by the President's Commission on Strengthening Social Security. Not only would solvency be restored, it would also be accomplished with a **much lower General Revenue Flows than <u>the full "*promised benefits*" level over the 75-year projection window</u>**. The following are examples of this feature of the Commission Model 2.

<u>Low-Income Earner ($15, 875 Annual Earnings in Constant 2002 $)</u>

Model 2 projects a **$15 trillion lower General Revenue Flow**[13] than under the current "promised" benefits benchmark. Under this model, a low-income earner retiring in 2012 would receive 1.5 percent higher benefits than under the current "*promised*" benefit level[14], even under the lowest (3 percent per year) real rate-of-return assumption used by the Social Security Administration actuaries[15]. The benefits received are even higher for higher rate of return assumptions.

Under Model 2, a low-income earner retiring in the year 2042, (the year that the Social Security Trustees project insolvency), would receive an 11 percent higher benefit per month under the middle (4.6 percent) real yield assumption, providing $100 more than the current "*promised*" benefit. This would be 54 percent higher than a current low-income beneficiary, or a $349 per month higher benefit.

Using the Social Security Actuaries highest assumption, a low-income earner would receive $118 more per month than the current "*promised*" benefit.[16] Again, in addition to the strong likelihood of higher benefits for low-income earners, the

[12] *The Case for Strengthening Social Security: Facts You Need to Know.* March 2003, US Senate Special Committee on Aging.

[13] Calculated from *The Cato Project on Social Security Privatization*, August 2002, pg 36 (see charts for Model 2).

[14] Using current Social Security formula calculations, the amount promised to individuals in constant 2002 dollars.

[15] 3 percent real yield, Trustees Report 2003

[16] Middle assumption = 4.6 percent real yield; high assumption = 5.3 percent real yield

General Revenue Flow is projected to be $15 trillion lower than under the current "*promised*" benefits under Model 2. Using the 4.6 or 5.3 percent real yield assumptions, this means beneficiaries will receive means **HIGHER INDIVIDUAL BENEFIT LEVELS COMBINED WITH LOWER NATIONAL DEBT LEVELS, LOWER TAX BURDENS, AND/OR MORE RESOURCES FOR OTHER FEDERAL PROGRAMS (MEDICARE, MEDICAL RESEARCH, EDUCATION, TRANSPORTATION, ETC.).**

The Social Security Trustees' Report, March 2003 calculated assumptions of return out to the year 2075. By the time a low-income individual retires at age 65 in the year 2075, the current benefit "*payable*"[17] to that retiree would be about 25 percent lower than the lowest (3 percent per year) assumption of the personal retirement accounts ($655 compared to $853).

Moderate-Income Earner ($35,277 Annual Earnings in Constant 2002 $)

Moderate-income earners retiring in 2012 receive roughly the same level of benefits under Model 2 compared to current "*promised*" benefits. The **General Revenue Flow required would be $15 trillion lower than the benefits "*promised*" benchmark's General Revenue Flow of $22 trillion under Model 2**. This means **FULL INDIVIDUAL BENEFIT LEVELS COMBINED WITH LOWER NATIONAL DEBT LEVELS, LOWER TAX BURDENS, AND/OR MORE RESOURCES FOR OTHER FEDERAL PROGRAMS (MEDICARE, MEDICAL RESEARCH, EDUCATION, TRANSPORTATION, ETC.).**

The results developed by the Social Security Administration's actuaries—while technically accurate for persons retiring at age 65 in the years 2022 and 2032—are somewhat misleading. The benefit projections imply that these cohorts will receive lower benefits using the Commission's personal account framework. These projections assume the "*do nothing*" plan or the "*status quo*" continues without any policy changes. However, federal budget pressures will require changes in benefits and/or taxes prior to the statutory insolvency of the program to pay full benefits. Consequently, the calculated benefits "*payable*" benchmark is likely to be overstated for these two cohorts.

In 2042, a moderate-income retiree would see higher benefits under Model 2. Model 2 would deliver about $123 higher monthly benefits under the lowest real yield assumption (3 percent) than the current benefits "*payable*" to the beneficiaries. As in the case of the low-income earner, benefits would rise with increases in real yield.

By the year 2075, an individual retiring who has chosen the personal retirement account under Model 2 would receive a significantly higher benefit with the 4.6 percent real yield or the 5.3 percent real yield compared to "*payable*" benefits under the "*do nothing*" plan. The **General Revenue Flow is $15 trillion lower than benefits "*promised*" benchmark's General Revenue Flow of $22 trillion under Model 2**.

[17] The amount the Social Security Trust Fund could actually afford in 2002 constant dollars.

Model 3

While most policy attention has been placed on Model 2 because it is both solvent and sustainable, it is important to review Model 3 as a viable option because it does achieve solvency over the 75-year window. Model 3 would also **restore long-range solvency** to the Social Security trust funds. Solvency would be achieved with **about half the General Revenue Flow** (financed by debt, taxes, and/or spending cuts in other federal programs) needed compared to the benefits "*promised*" benchmark for Social Security.

<u>Low-income Earner ($15, 875 Annual Earnings in Constant 2002 $)</u>

The Social Security actuaries project a **$12 trillion lower General Revenue Flow**[18] for Model 3 compared to the current "*promised*" benefits (Cato Report, pg 36). Under this model, a low-income earner retiring in 2012 would receive a slight increase in benefits compared to the current "*promised*" benefits benchmark, even under the lowest real yield assumption. Logically, benefit amounts increase as the real yield increases.[19]

A low-income earner retiring in the year 2042, would receive roughly the same benefit as under the "*promised*" benefit benchmark. This translates into a 26 percent higher benefit compared to the benefits "*payable*" benchmark using the lowest (3 percent per year) real yield assumption. Again, the **General Revenue Flow is projected to be $12 trillion less than** under the current "*promised*" benefits. Middle assumption for a low-income earner in 2042 about $100 more than the current "*promised*" benefit benchmark. Using the Social Security actuaries' highest (5.3 percent) real yield assumption, a low-income earner in Model 3 would receive $132 per month higher benefit than the current "*promised*" benefits benchmark amount. This means **HIGHER INDIVIDUAL BENEFIT LEVELS COMBINED WITH LOWER NATIONAL DEBT LEVELS, LOWER TAX BURDENS, AND/OR MORE RESOURCES FOR OTHER FEDERAL PROGRAMS (MEDICARE, MEDICAL RESEARCH, EDUCATION, TRANSPORTATION, ETC.).**

By the time an individual in the year 2075 retires at age 65, the current benefit "*payable*" to that retiree would be about 25 percent less than the lowest assumption of the personal retirement accounts ($825 compared to $1,062) and the **General Revenue Flow would, again, be $12 trillion lower than the benefits "promised" benchmark.**

<u>Moderate-Income Earner ($35, 277 Annual Earnings in Constant 2002 $)</u>

Low-income earners and the moderate-income earners would receive a slight increase in benefit under the lowest assumption. The biggest benefit would be the **$12 trillion decrease in General Revenue Flow**.

While **maintaining the $12 trillion lower General Revenue Flow**, retirees in the year 2042 under Model 3 would receive a monthly benefit at the lowest assumption of almost $300 more than what the current "*payable*" amount would be (a 21 percent increase in benefits). As in the case of the low-income earner, benefits would only rise to above the current "*promised*"

[18] Calculated from *The Cato Project on Social Security Privatization*, August 2002, pg 36.

[19] See Model 3 charts.

amount as the real yield percentage slowly increases.

By the year 2075, an individual retiring who has chosen the personal retirement option under Model 3 would receive a $54 to $146 greater monthly benefit than the current "promised" amount under the middle assumption and high assumption levels respectively. While the lowest assumption would yield a 18 percent smaller benefit than the current "promised", an individual's benefit would still be 18 percent greater than what the current Social Security system could afford in year 2075, all the while maintaining a **$12 trillion less General Revenue Flow**.

Low-Income and Disabled

A key factor for low-income individuals affecting the benefit level of Social Security is earnings. The calculated formula of Social Security is progressive. It is designed to replace a larger proportion of earnings for low-income individuals than it does for high income individuals.[20]

The GAO found that median monthly benefits for the lowest lifetime earners tend to be higher than the benefits received under the "*benefits reduction*" benchmark. The Social Security actuary data also show that the low earner has higher benefit levels than even the benefits "*promised*" benchmark in every case under all three Commission models through 2052 using the middle real yield assumption (4.6 percent per year).

Because low-income persons are more likely to be disabled, the benefit levels are also likely to be higher for disabled persons using the Commission's personal retirement account framework.

Widows, Divorcees, and Survivors

Benefit projections include comparisons for one-earner and two-earner couples but do not include surviving spouses or divorced persons. The Commission's personal account proposals appear best under these family circumstances compared to the current system.

Social Security was originally an old-age retirement program. In 1939, Social Security Amendments added two categories of benefits: dependent benefits paid to the spouse and minor children of a retired worker, and survivor benefits paid to the family after the death of a covered worker.[21] Personal retirement accounts as part of Social Security reform would benefit not only the low-income, disabled, and minority individuals, it would also benefit widows, survivors and divorcees.

For below average-income widow(er)s Model 2 and 3 presented by the President's Commission to Strengthen Social Security would increase survivors benefits from the current 50 percent to 75 percent of the couple's prior benefit.[22]

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[20] As reported by GAO, April 2003 in *Social Security and Minorities: Earnings, Disability Incidence, and Mortality are Key Factors that Influence Taxes Paid and Benefits Received.*

[21] GAO, *Social Security and Minorities: Earnings, Disability Incidence, and Mortality are Key Factors that Influence Taxes Paid and Benefits Received*, April 2003.

[22] The Cato Project on Social Security Privatization, *Perspectives on the President's Commission to Strengthen Social Security*, Andrew Biggs, August 2002.

For example, a retired couple receiving a combined monthly benefit of $1,500 prior to the death of a spouse would leave a $1,000 monthly benefit for the survivor after the death of a spouse under the current Social Security system. Under Models 2 and 3 of the personal retirement accounts, a couple receiving that same combined monthly benefit of $1,500 prior to the death of a spouse would leave a $1,125 monthly benefit for the survivor upon death. This is a 12.5 percent increase in benefit for survivors compared to current law. [23]

Two to three million widows would see benefit increases from Models 2 and 3. Eight-five percent of Americans currently collecting survivors' benefits are aged widows and widowers. Future surviving spouses and children would fare much better under personal retirement accounts than under the current benefit system, not only inheriting the balance of the personal retirement account, but also the traditional defined benefit survivors monthly payment.

All three models of personal retirement accounts call for retirement account assets to be split in the event of divorce. Currently, if divorce occurs before 10 years of marriage, a spouse is not eligible to receive any benefits based on the husband or wife's earnings. Under all three models for personal retirement accounts, a spouse would receive half of the husband's or wife's account assets. For the spouse of an average-wage worker, if these assets were left to accumulate until retirement, it could result in lump sums ranging from $10,000 to $40,000.[24] Women and divorcees are statistically among the most vulnerable to poverty in retirement.[25] The personal retirement account framework would provide significantly higher assistance to this particularly vulnerable group.

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Note on Charts

Benefit levels are expected values based on a mix of investments using 6.5 percent real equity yield and 3 percent real bond yield assumptions. "*Real yield*" means the return after being reduced for annual expected price inflation of goods and services. The 3.0 percent real yield portfolio is assumed to hold only government bonds, with a yield, net of administrative costs, of 2.7 percent annually. The 4.6 percent real yield is assumed to consist of a portfolio with 50 percent stocks (6.5 percent annual real yield), 30 percent corporate bonds (3.5 percent annual real yield), and 20 percent government bonds (3.0 percent annual real yield), net of 0.3 percentage points for administrative costs. The 5.3 percent real yield portfolio assumes that 60 percent is invested in stocks, 24 percent in corporate bonds (3.5 percent annual real yield), and 16 percent in government bonds (3.0 percent annual real yield). It should be noted that upon reaching normal retirement age, all account assets are assumed to be invested in government bonds (3.0 percent annual real yield).

Senate Committee on Aging staff Scott Nystrom, Stacy Smith, and Brian Wonderlich produced this analysis.

[23] Dollars are illustrative calculations and do not represent the survivor benefit threshold.

[24] The Cato Project on Social Security Privatization, *Perspectives on the President's Commission to Strengthen Social Security*, Andrew Biggs, August 2002.

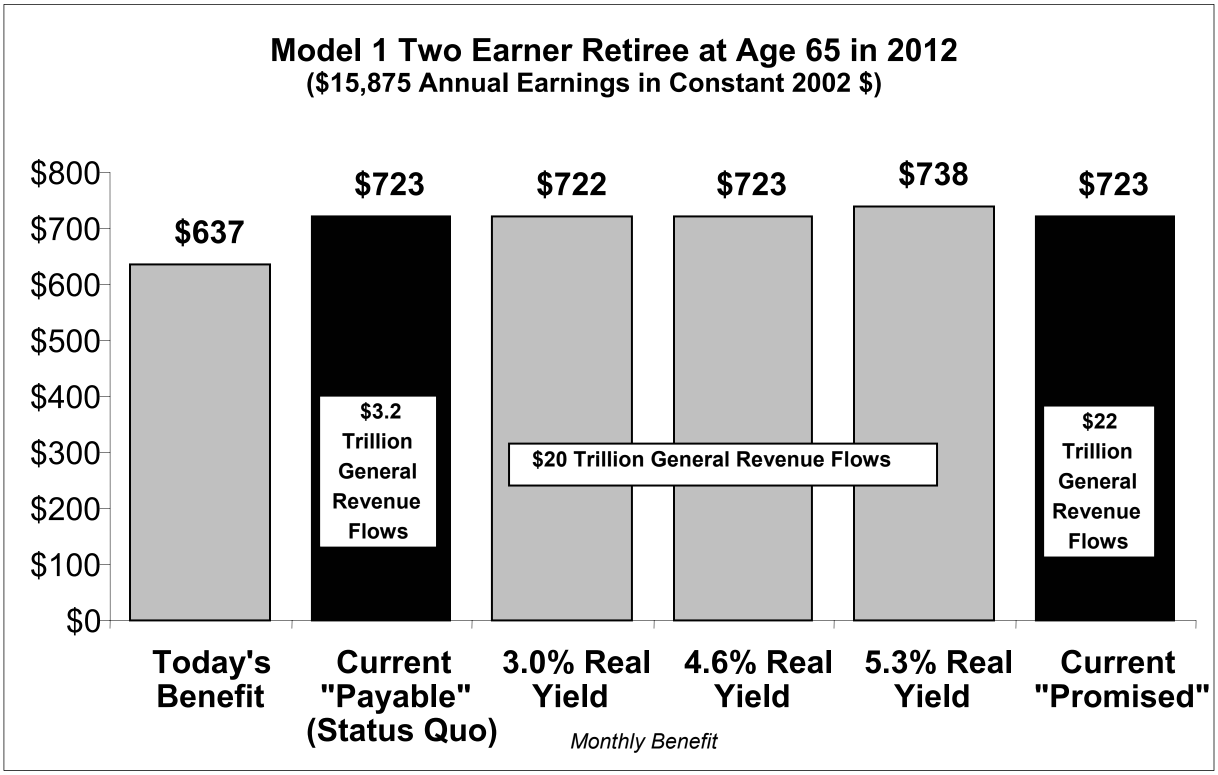
[25] The Cato Project on Social Security Privatization, *Perspectives on the President's Commission to Strengthen Social Security*, Andrew Biggs, August 2002.

Social Security Actuarial Projections of Benefit Levels Chart Table of Contents

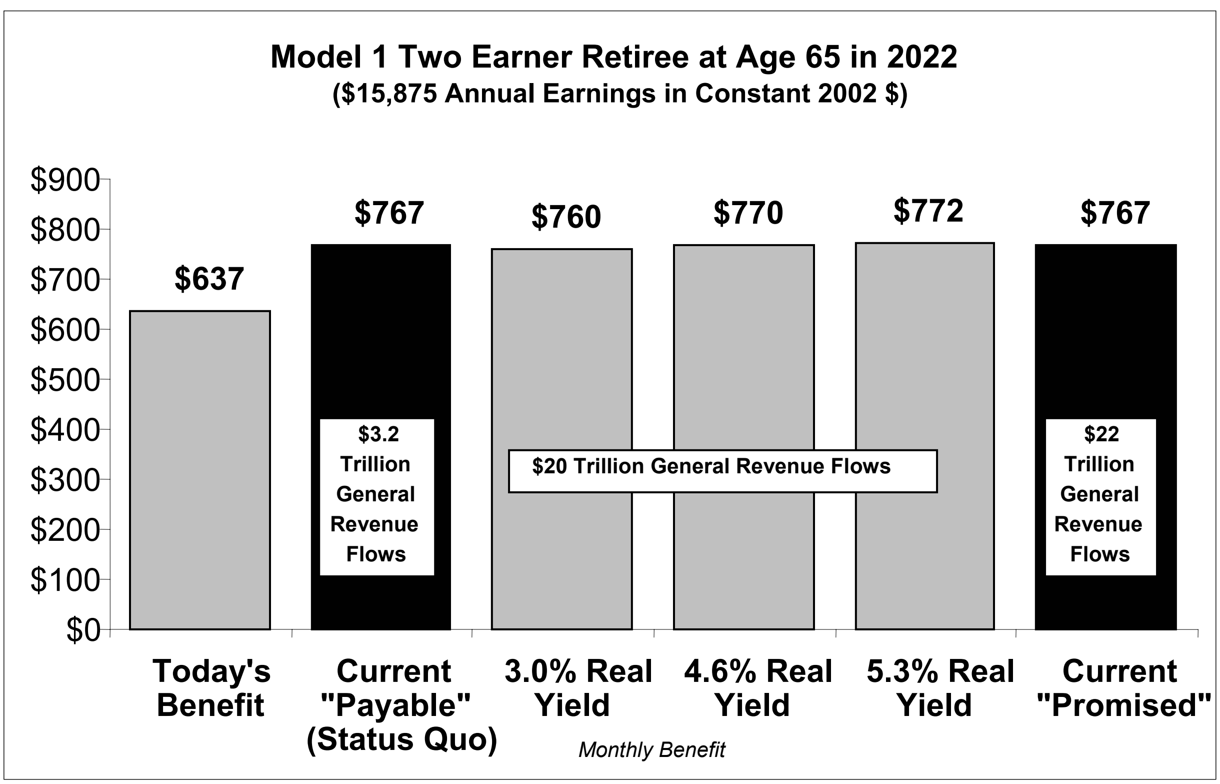
MODEL 1

MODEL 2

MODEL 3



Source: Actuarial Memo from Steve Goss, January 2002, in the President's Commission to Strengthen Social Security Final Report, 2003; Perspectives on the President's Commission to Strengthen Social Security by Andrew G. Biggs, The Cato Project on Social Security Privatization, August 22, 2002, pg. 36.



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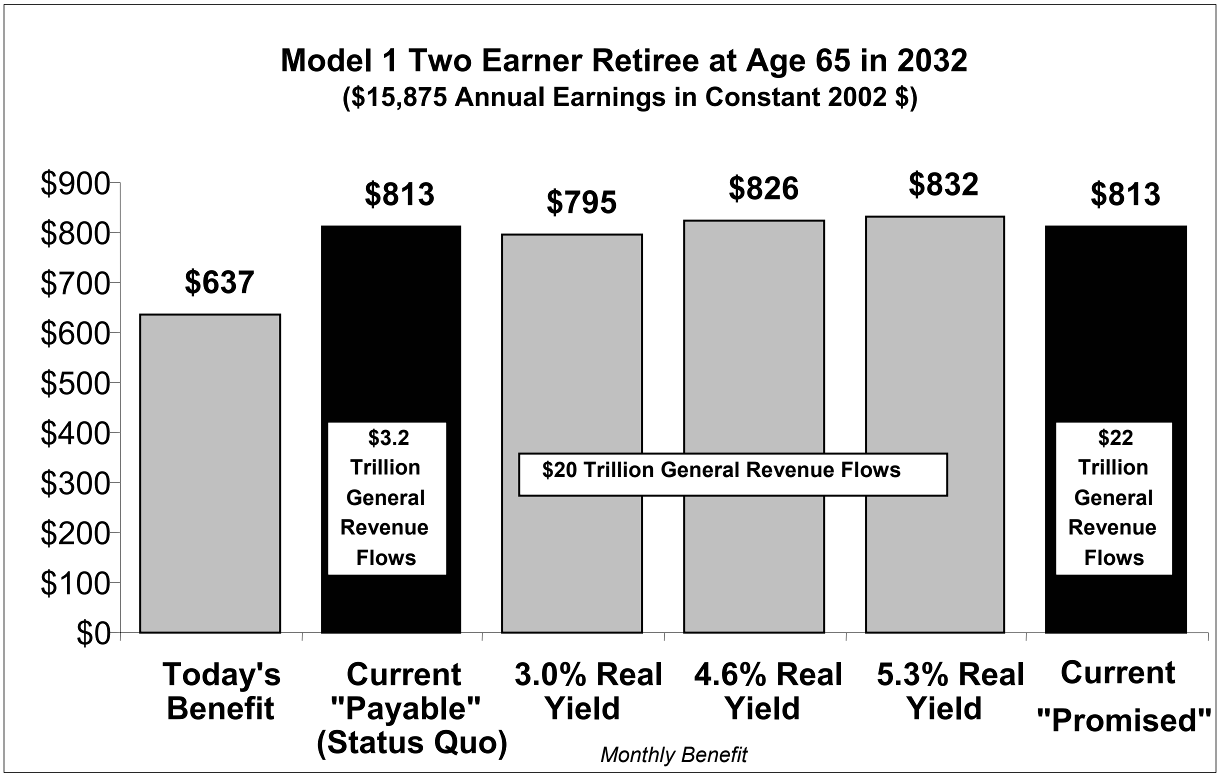

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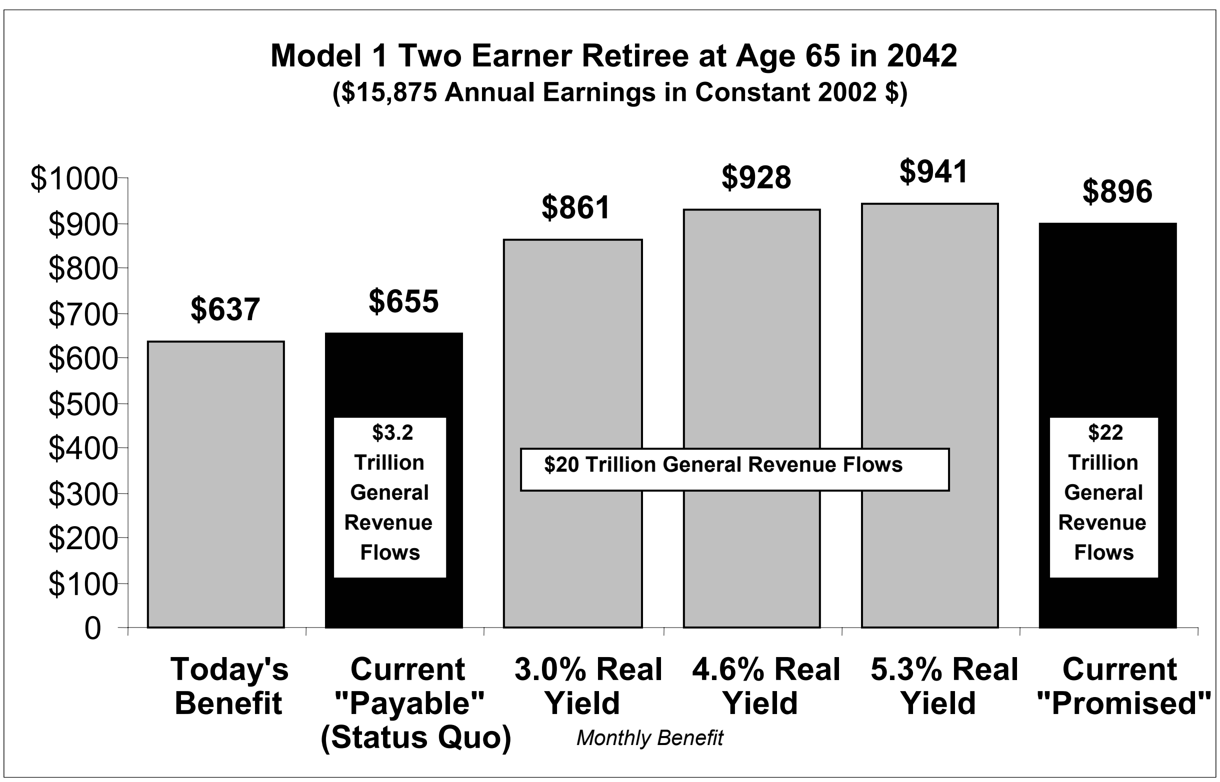

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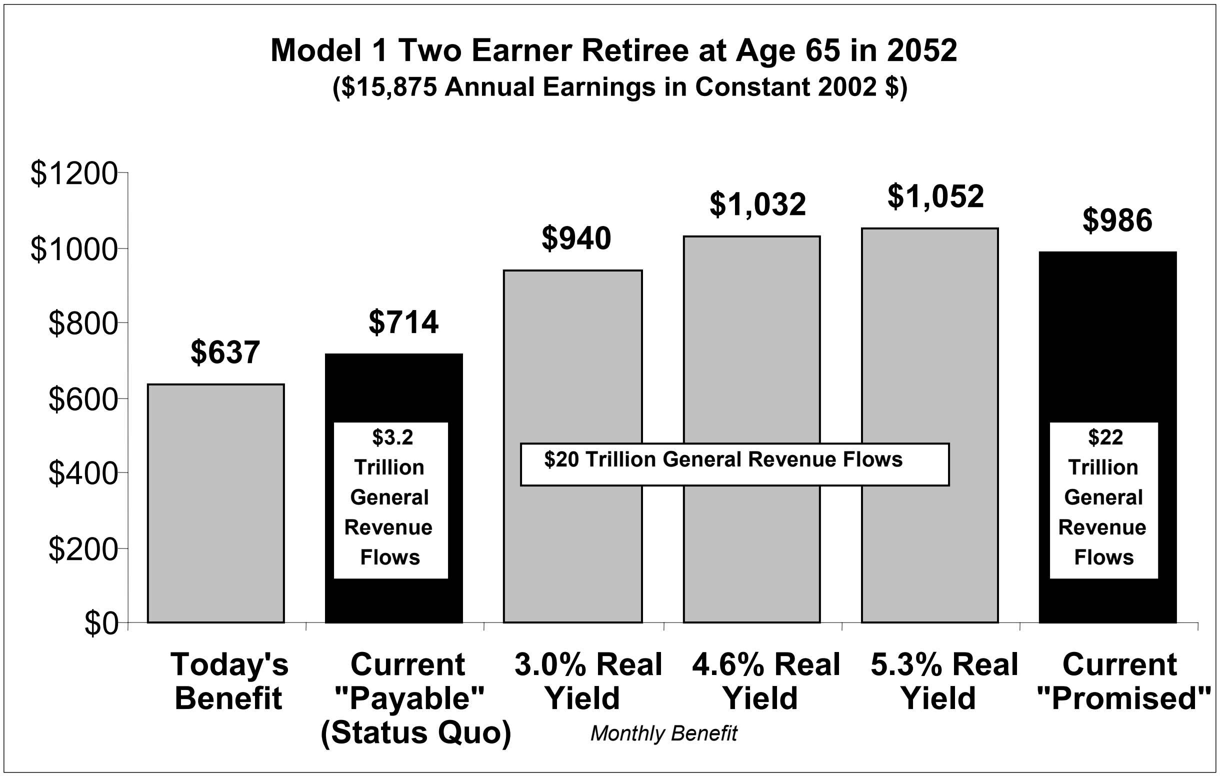

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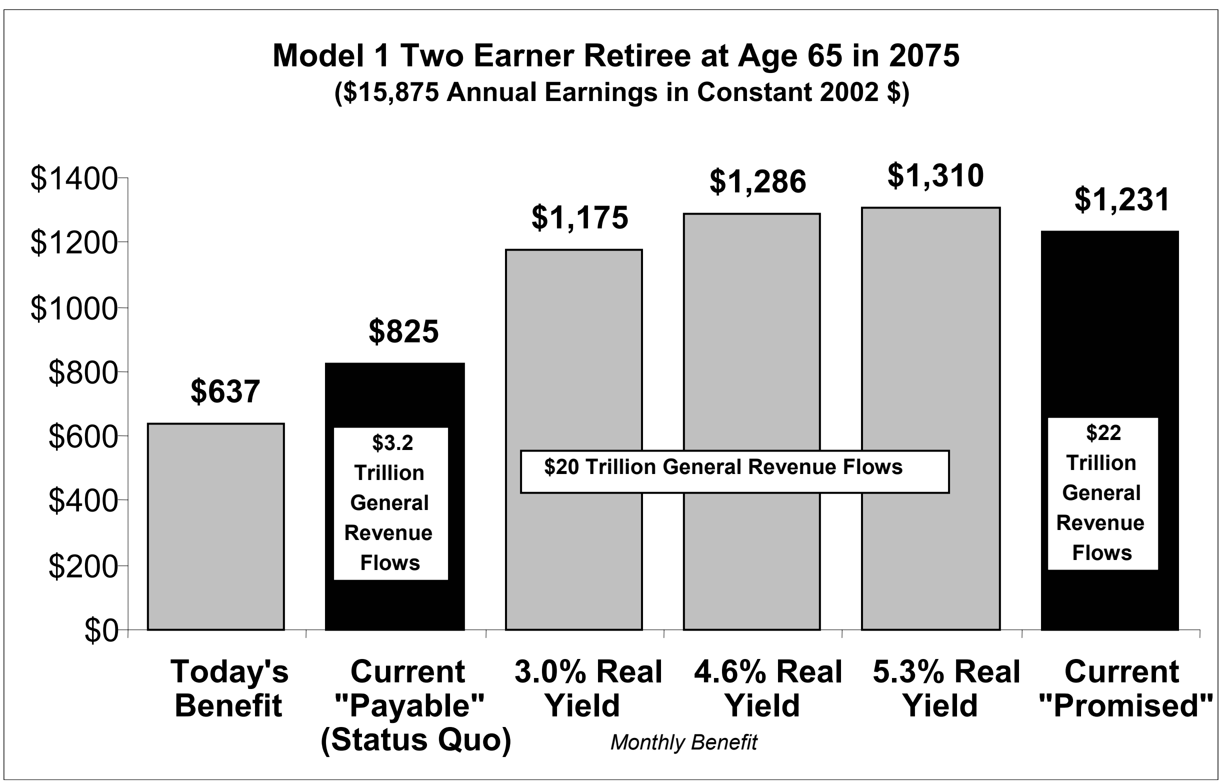

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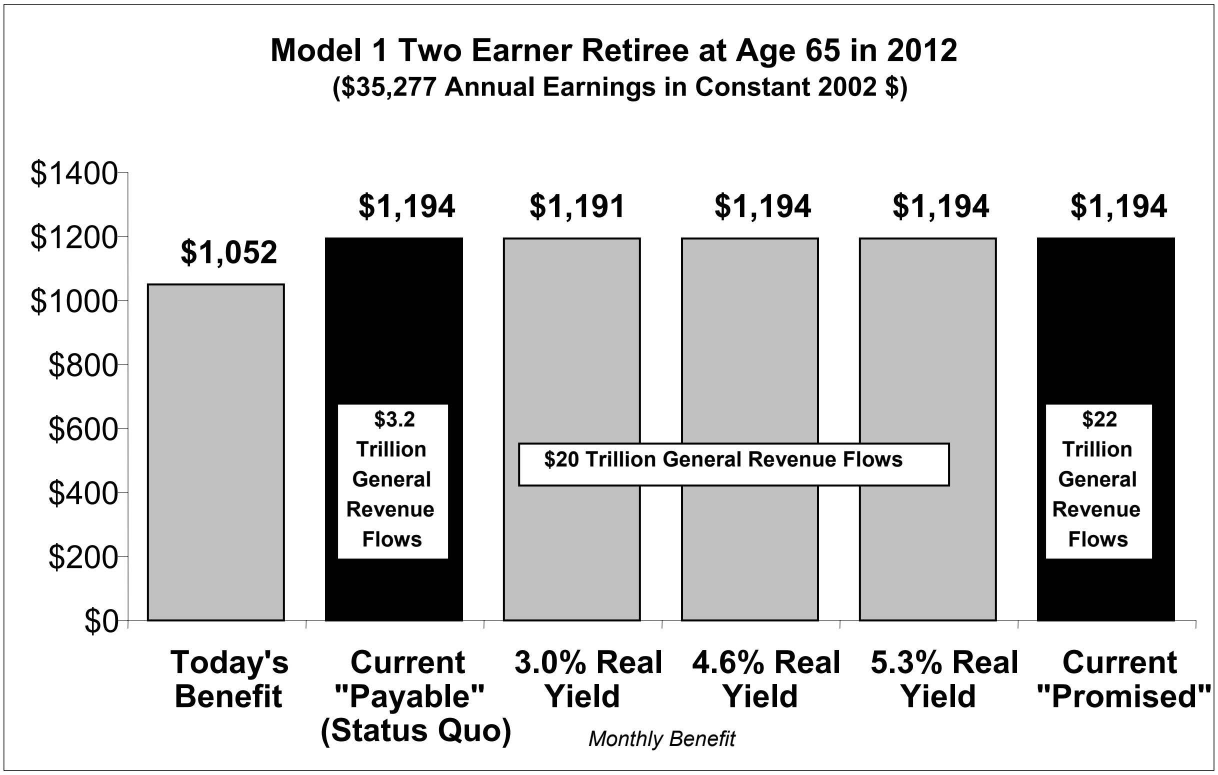

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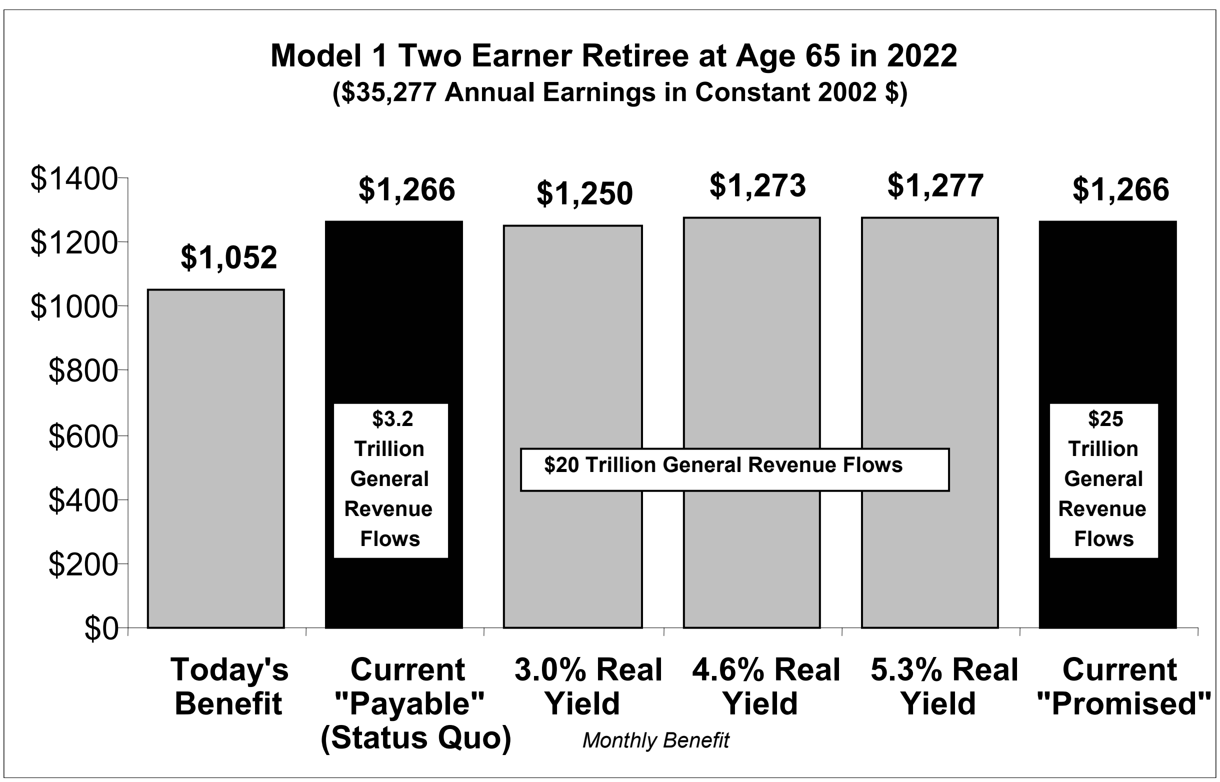

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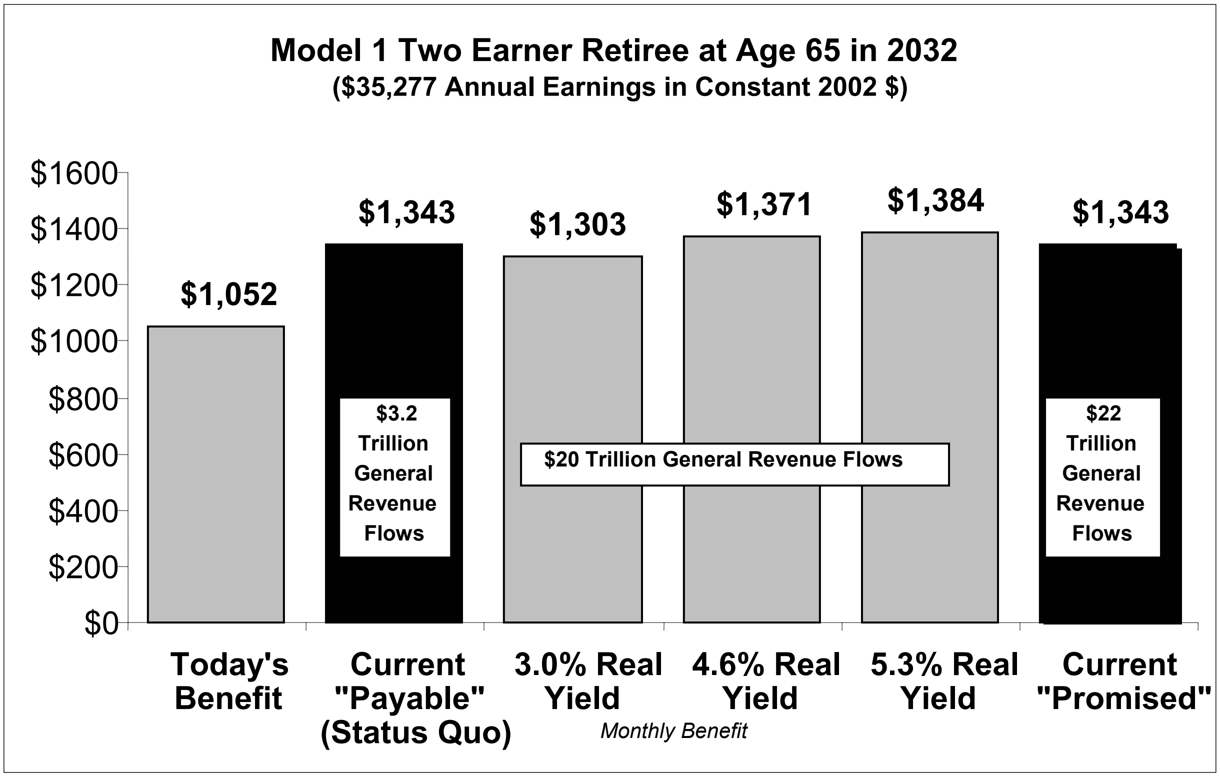

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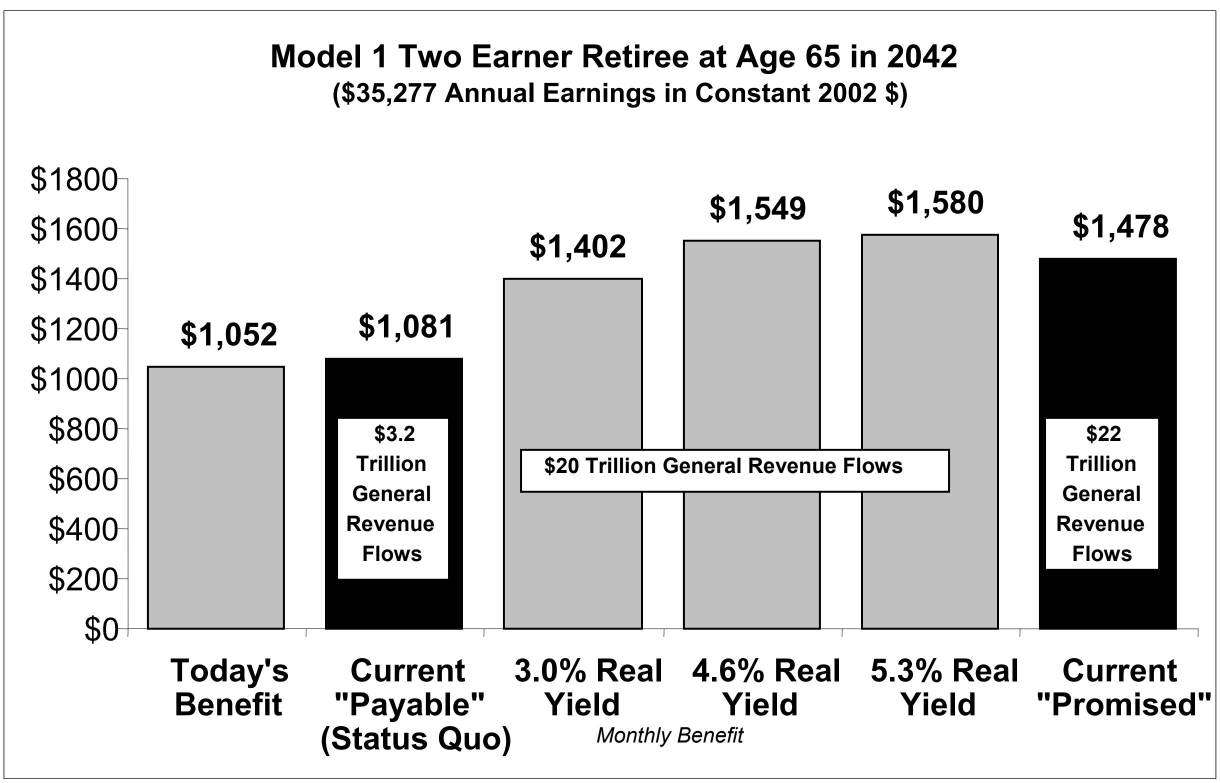

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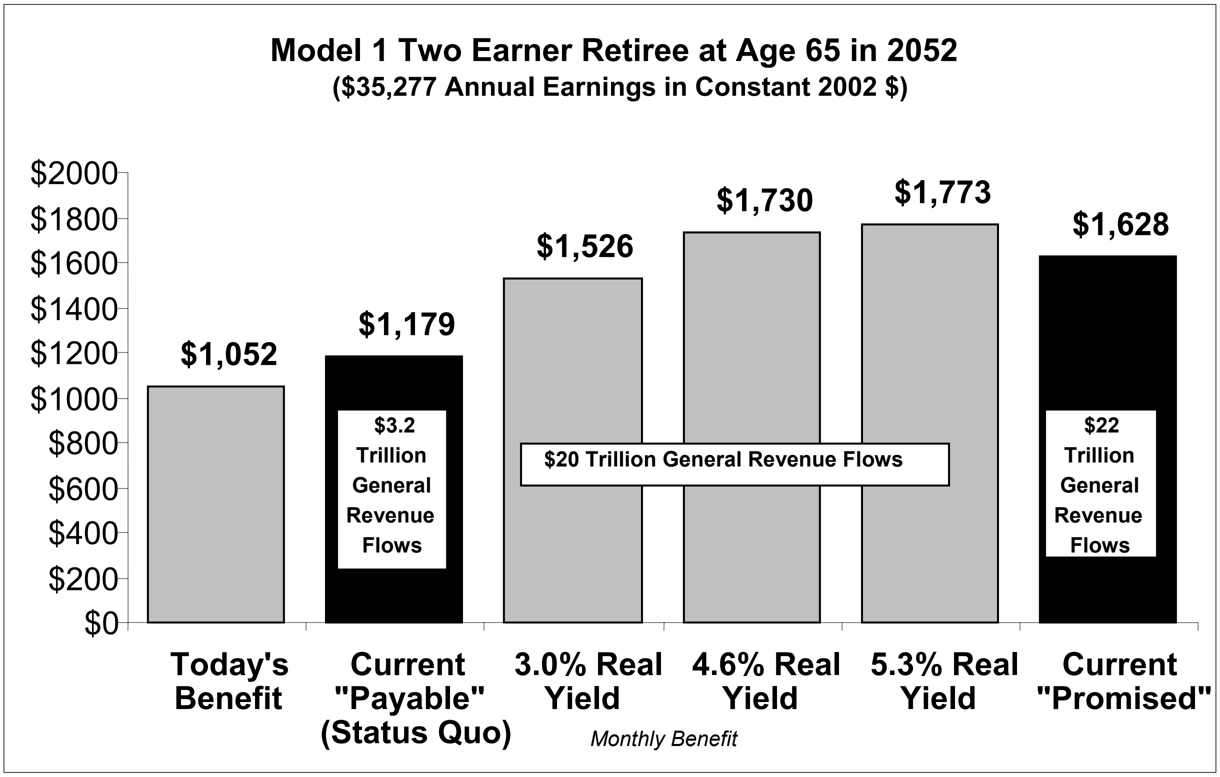

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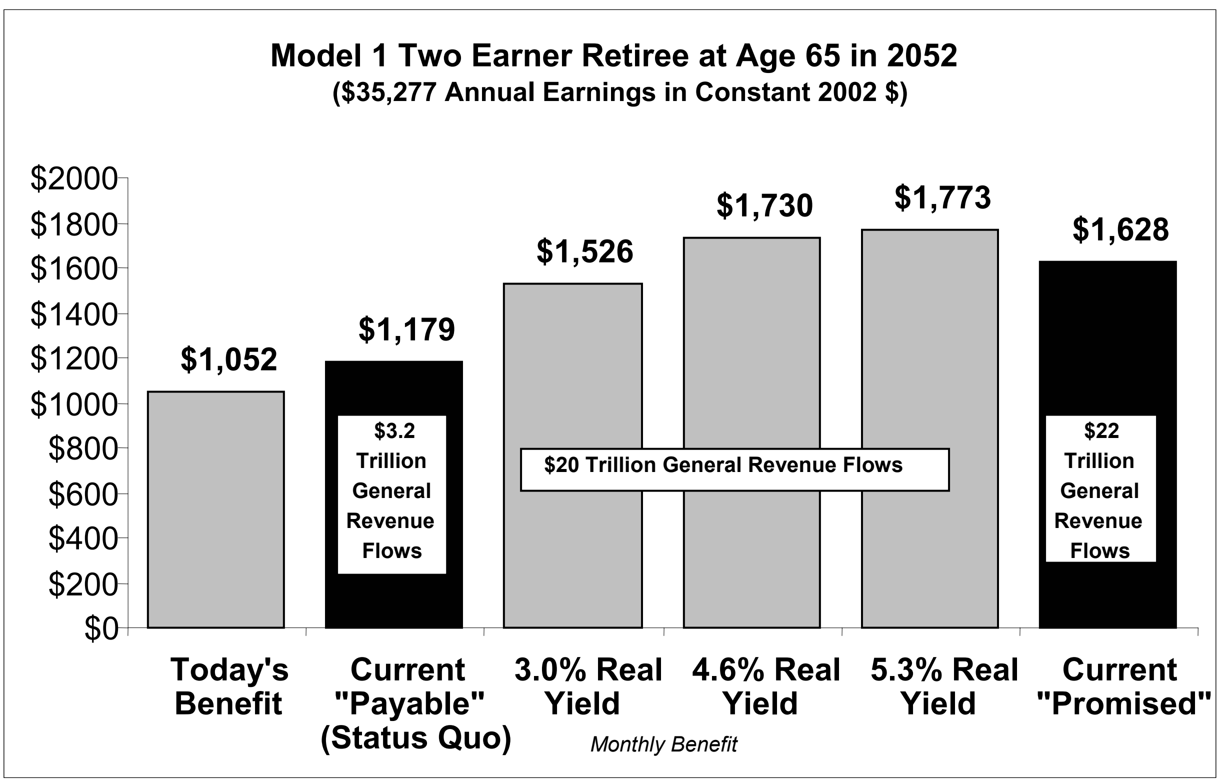

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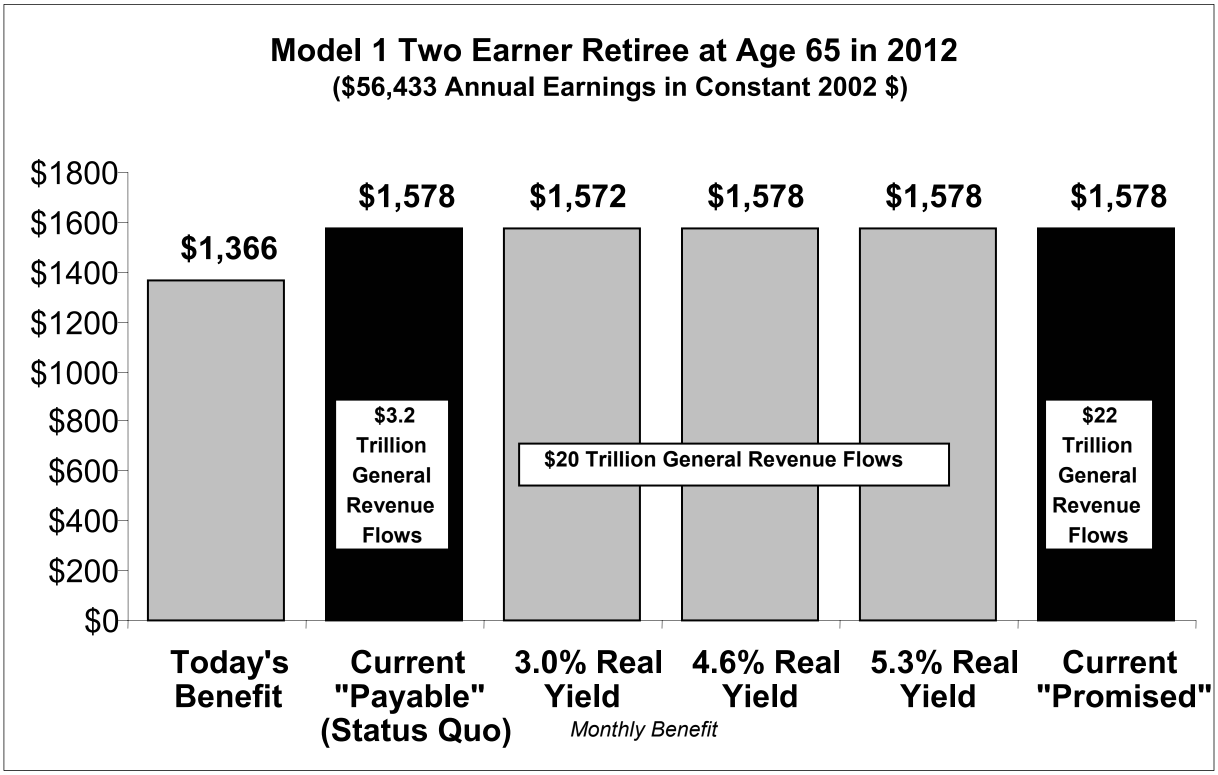

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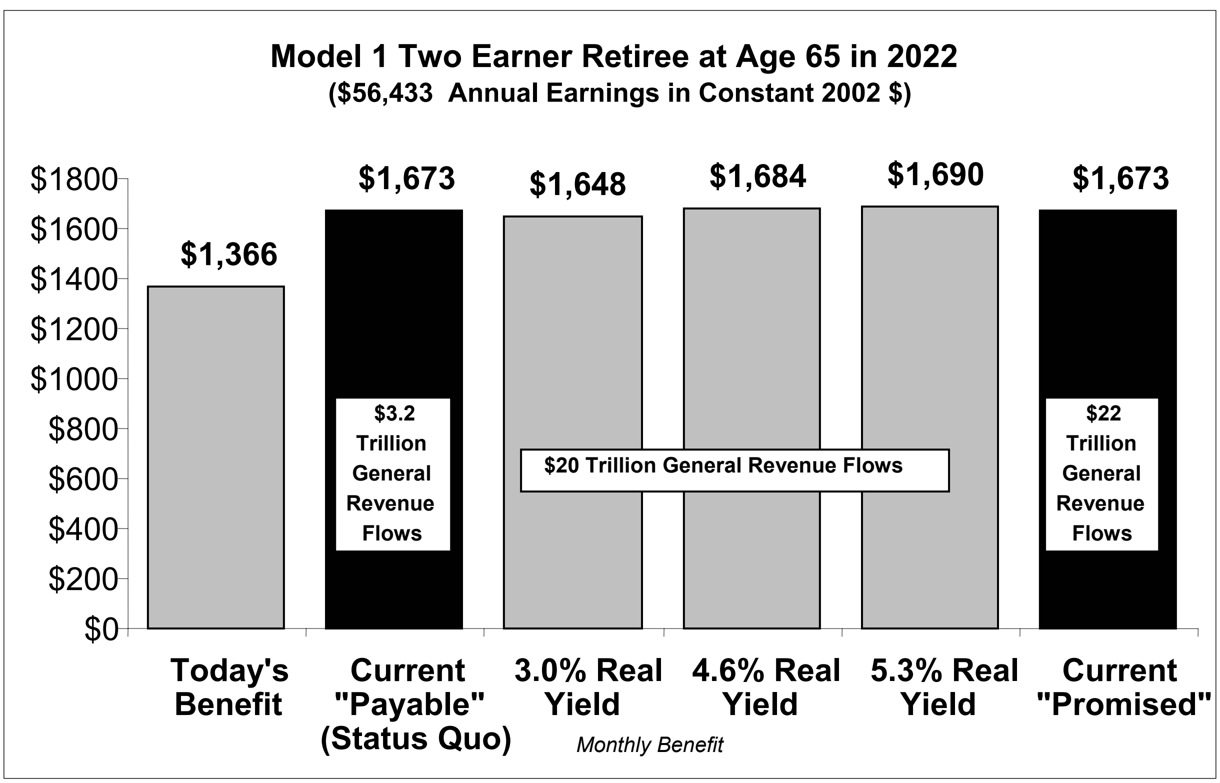

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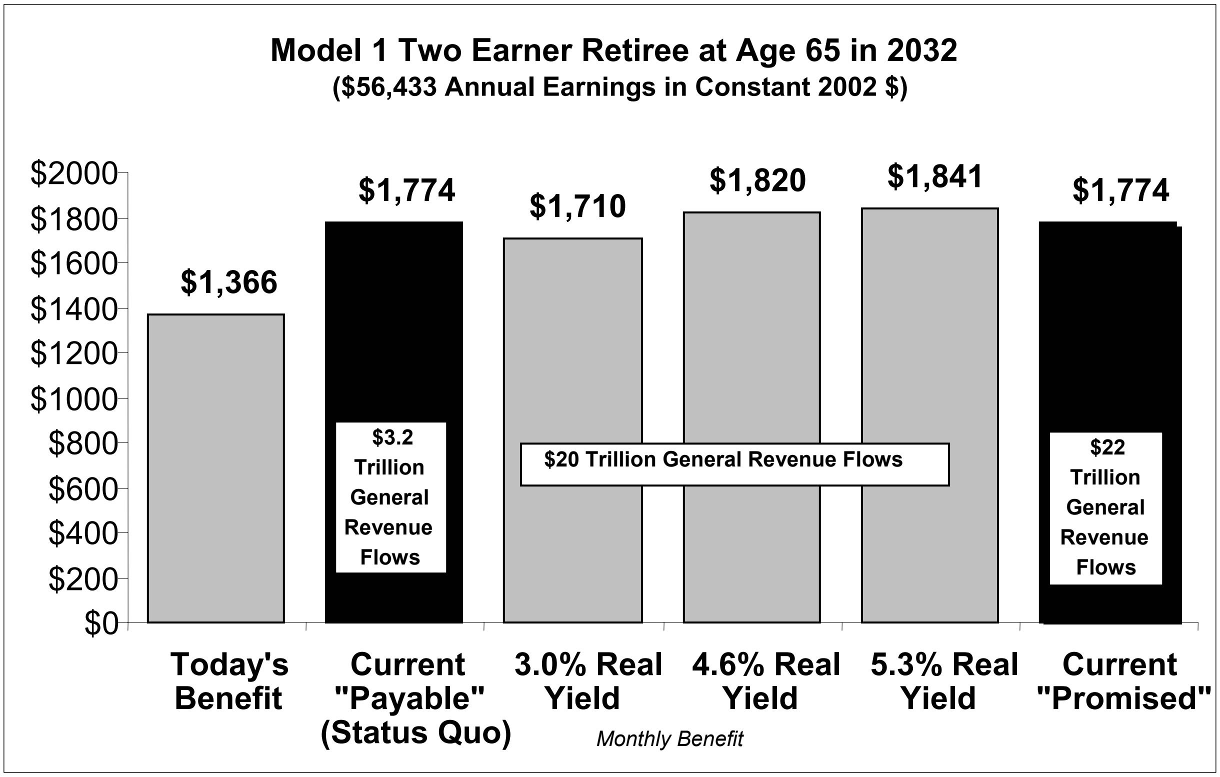

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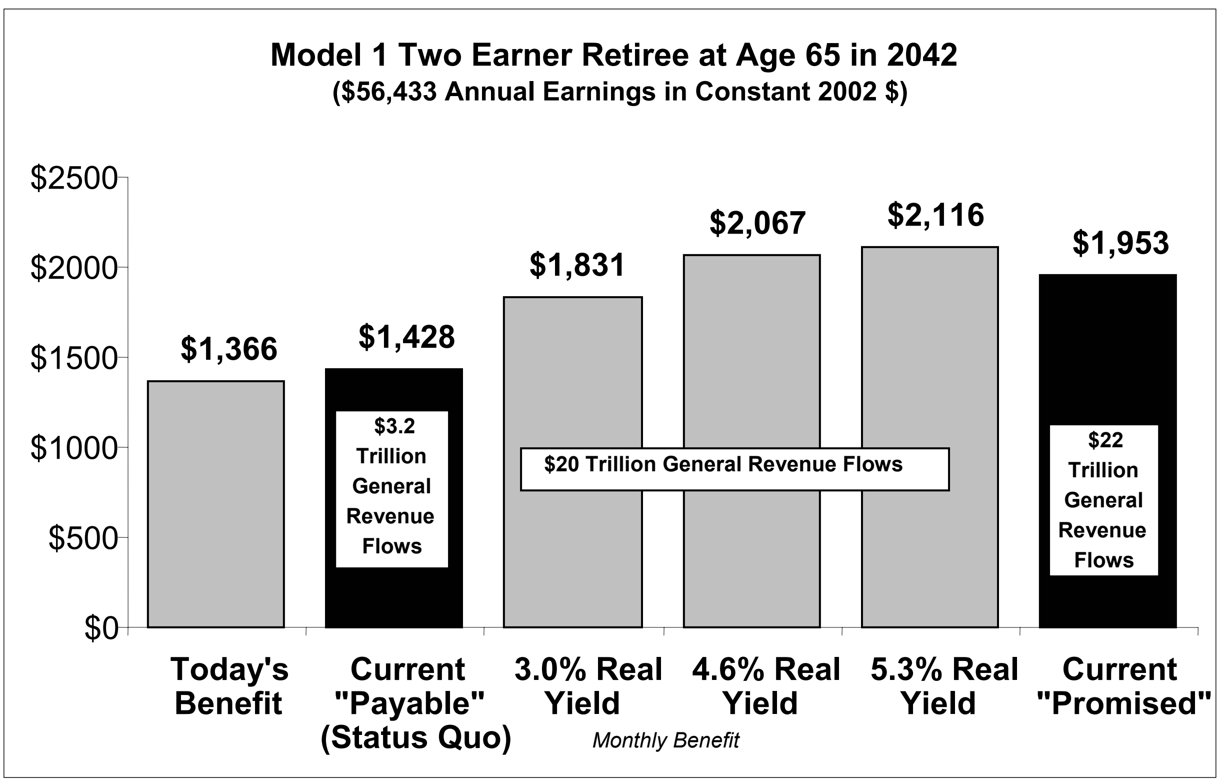

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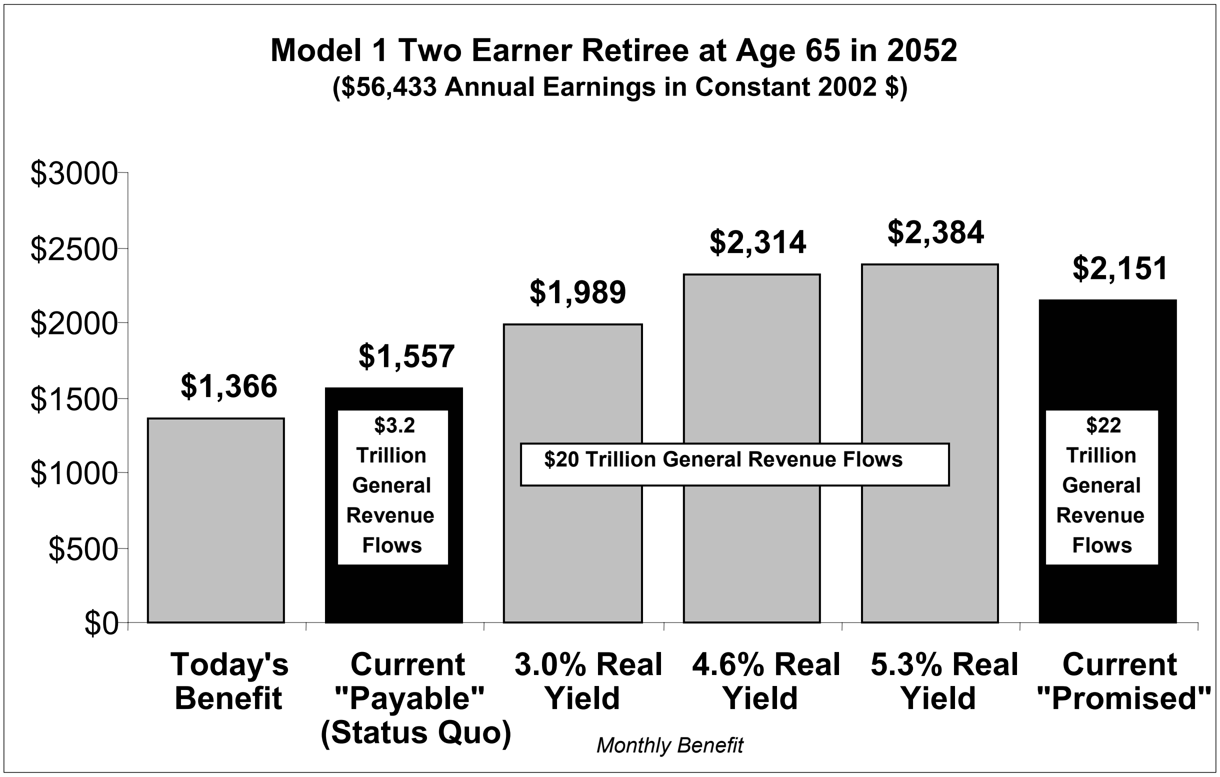

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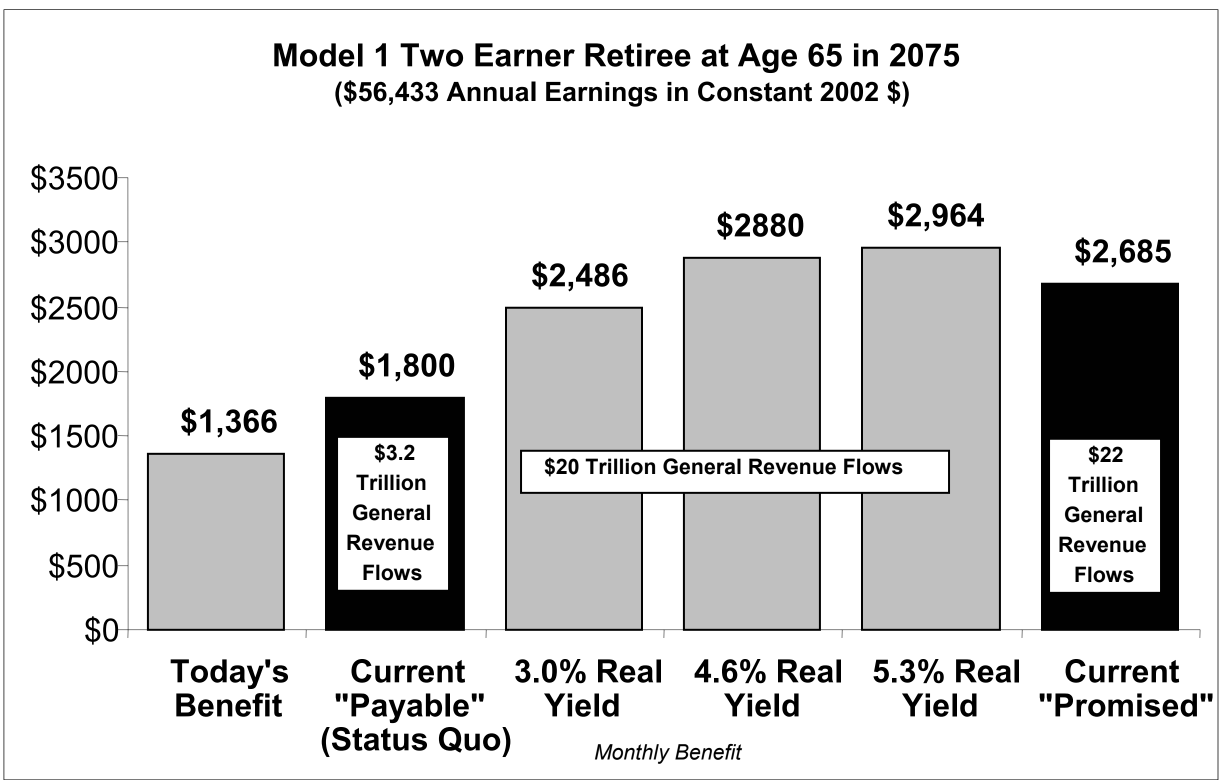

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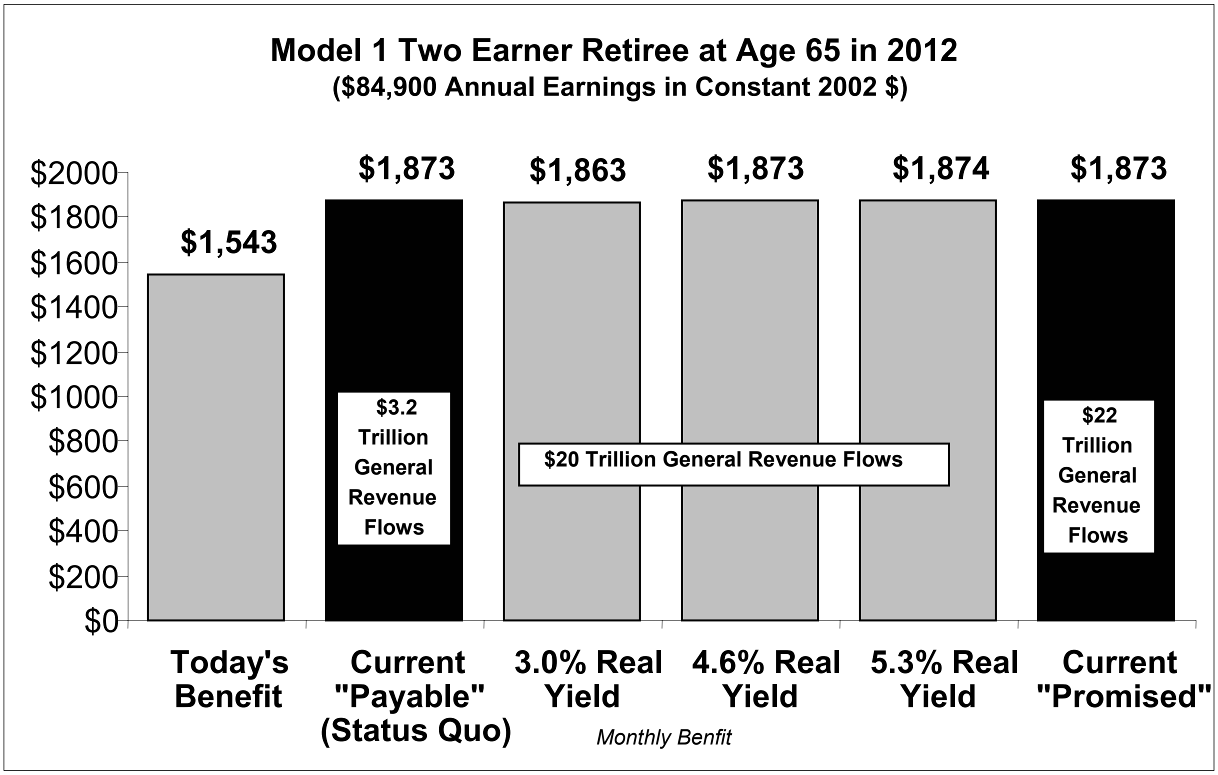

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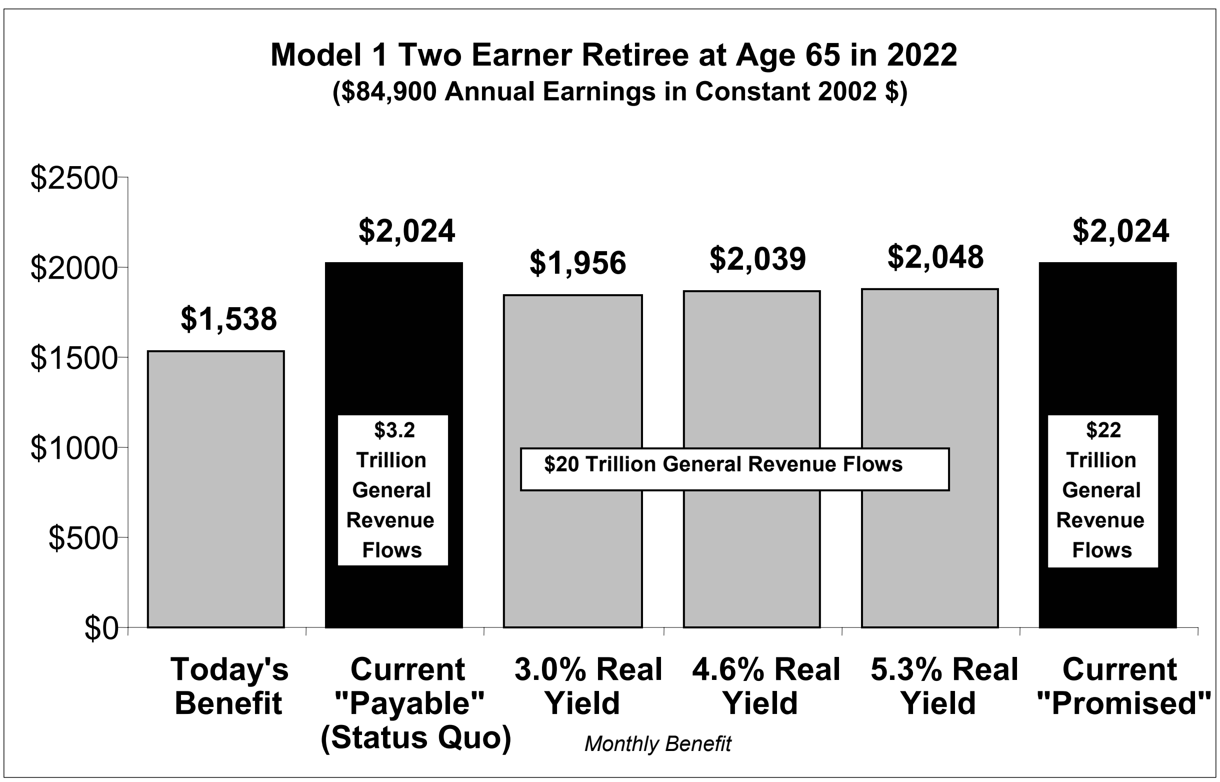

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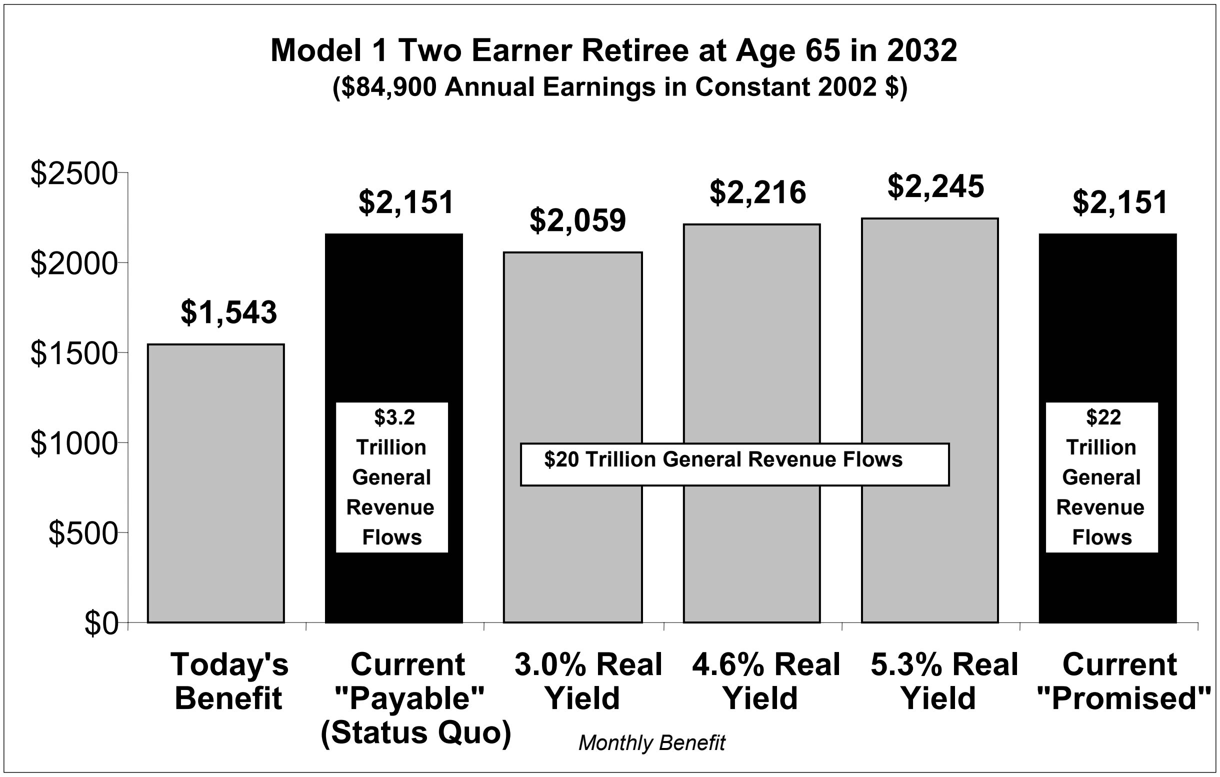

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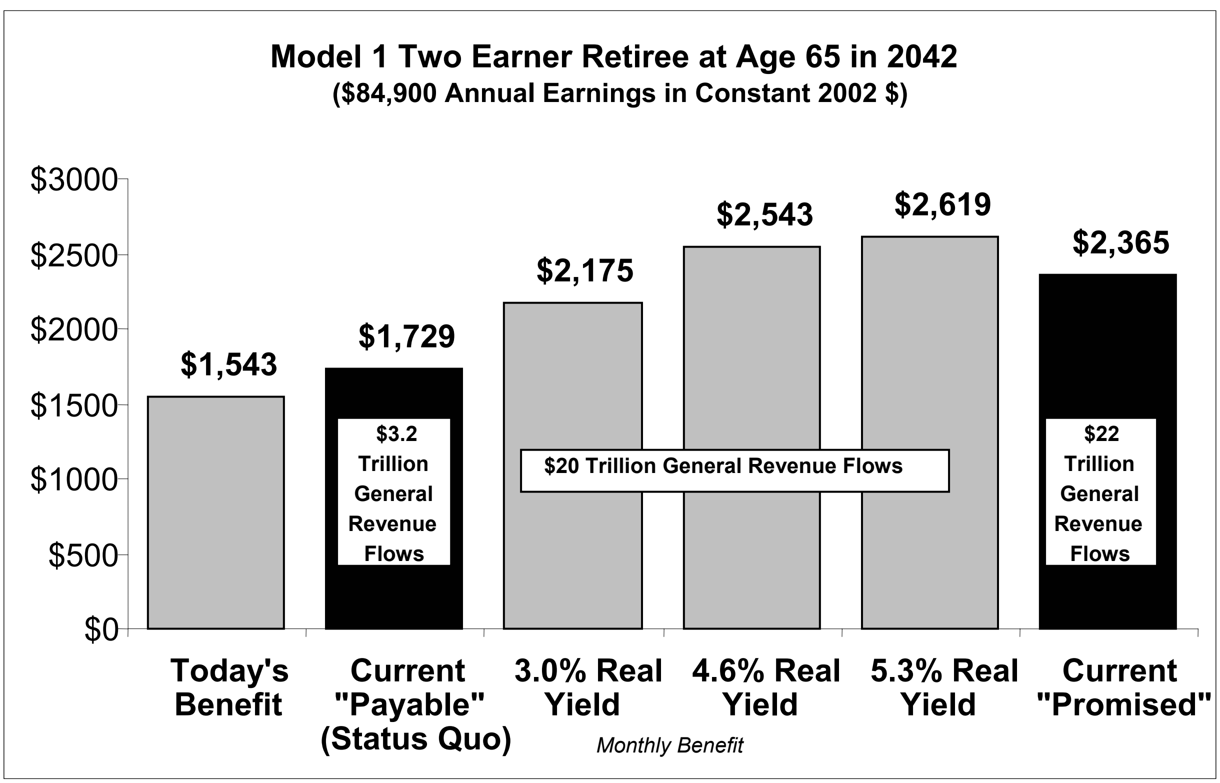

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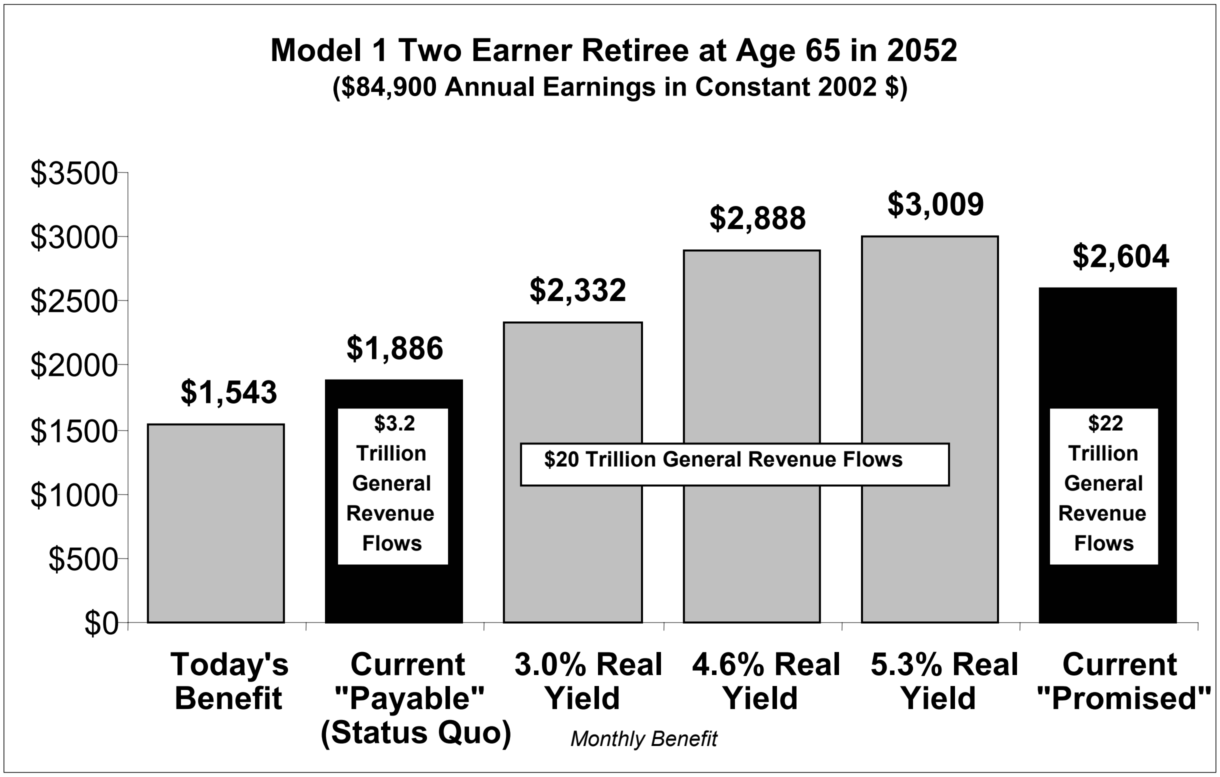

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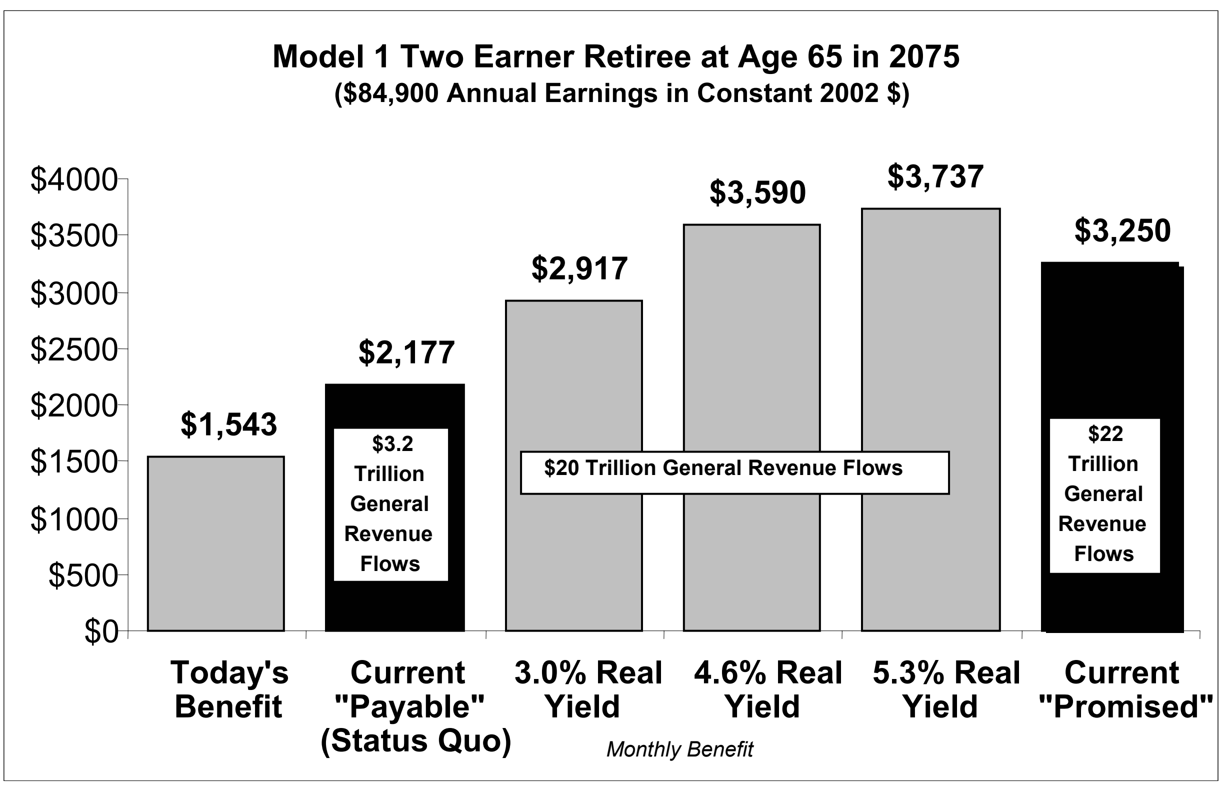

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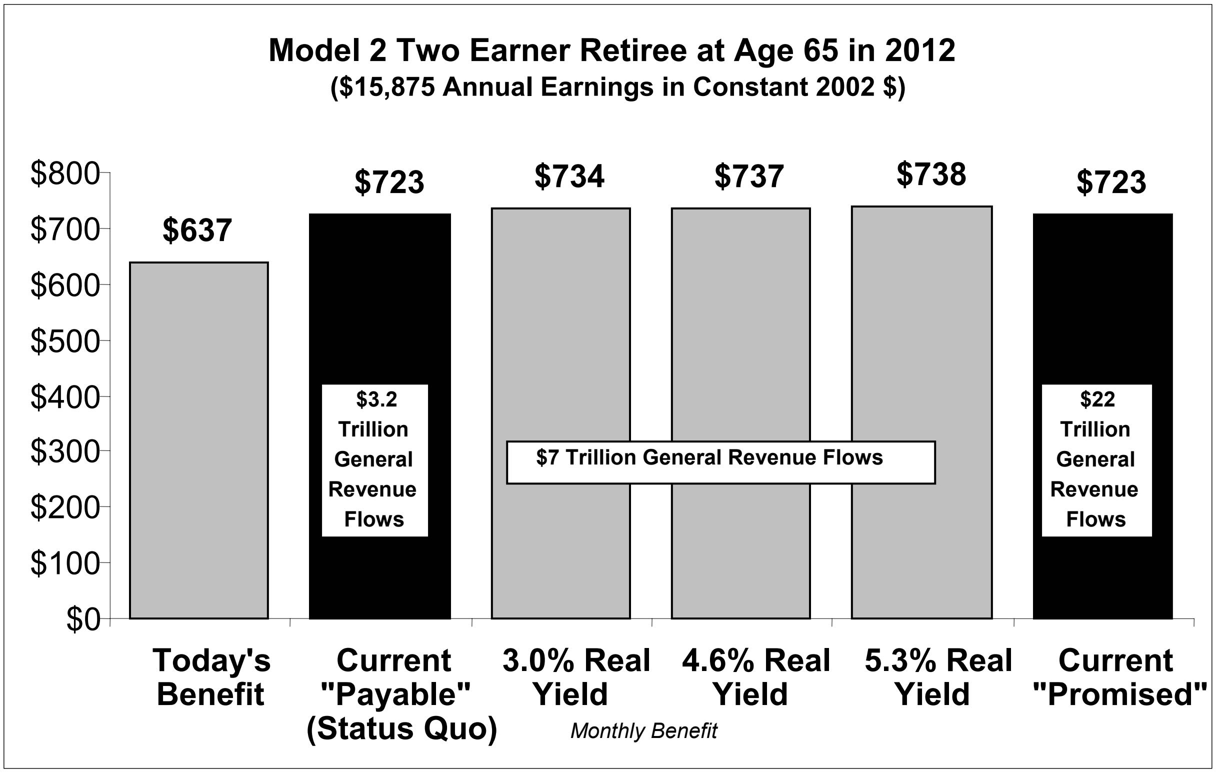

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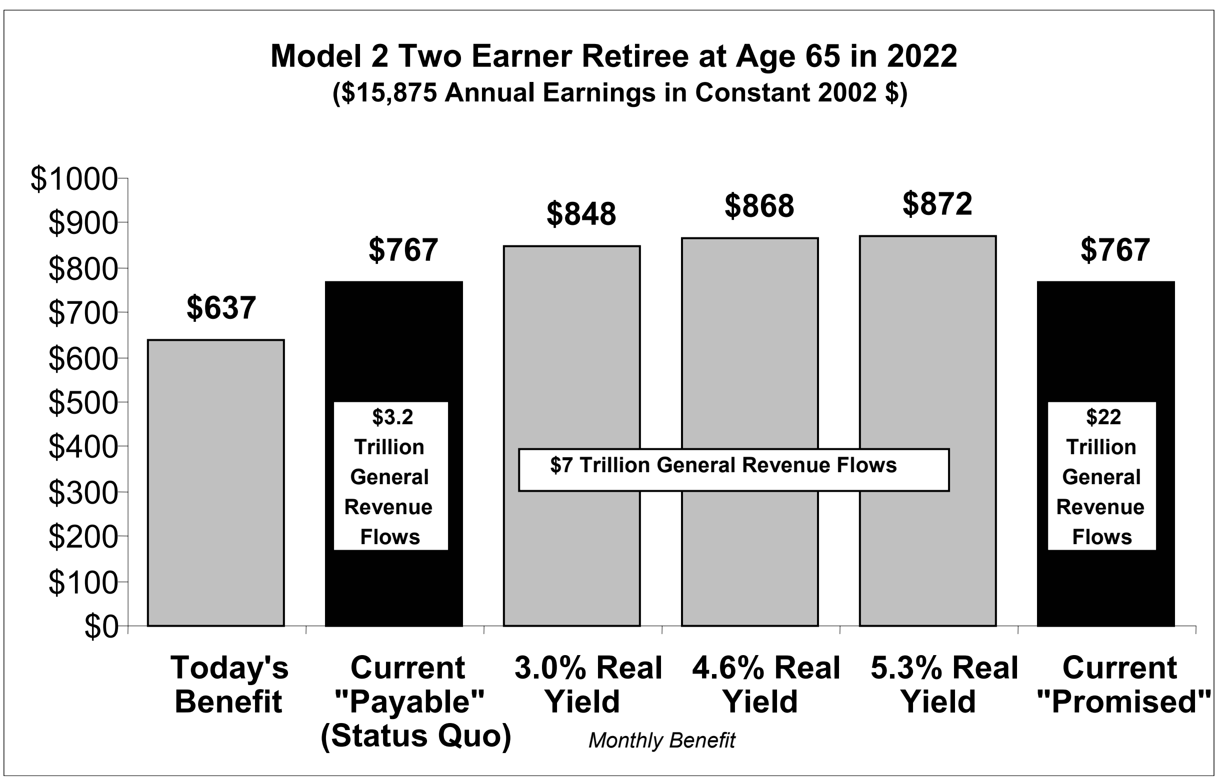

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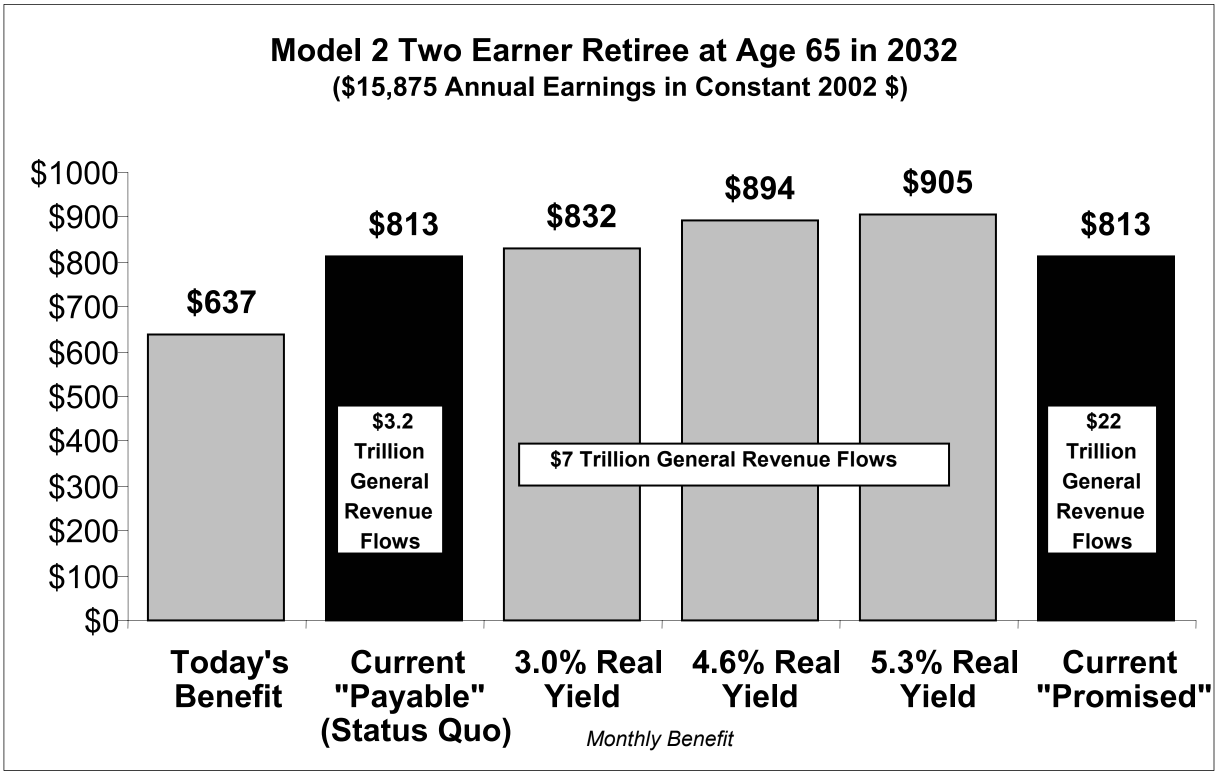

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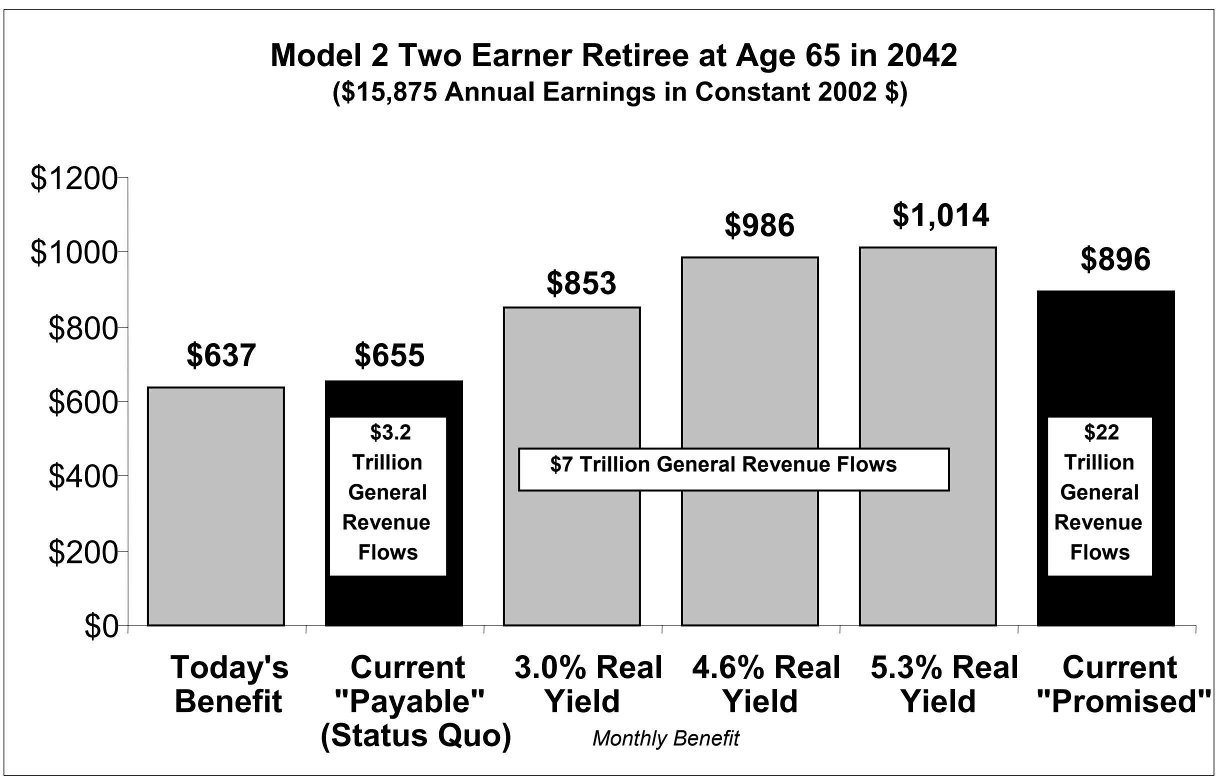

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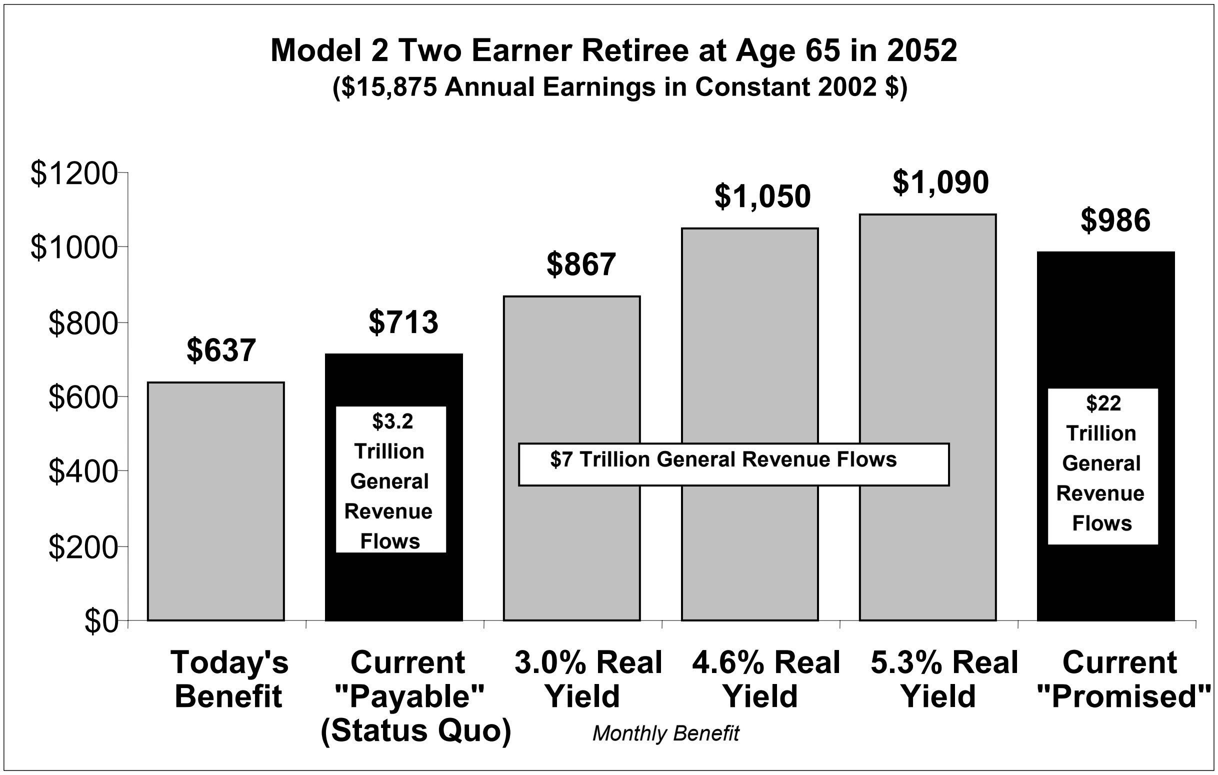

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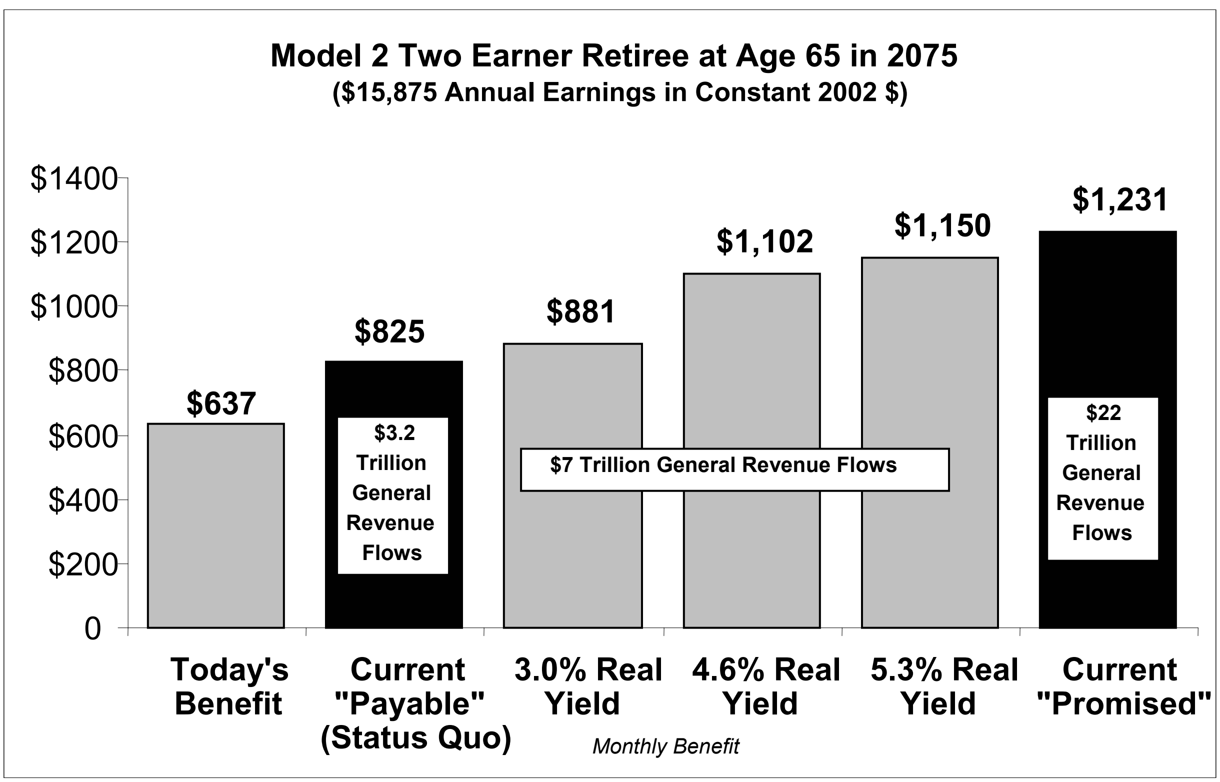

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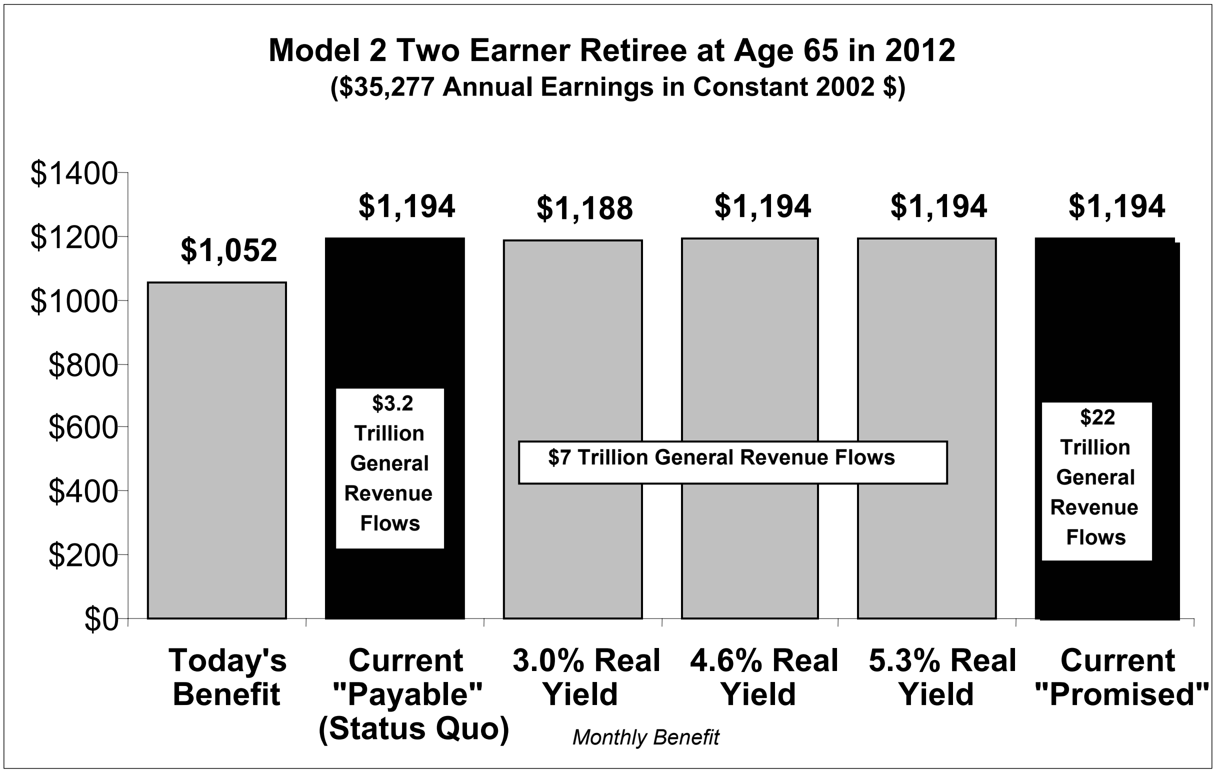

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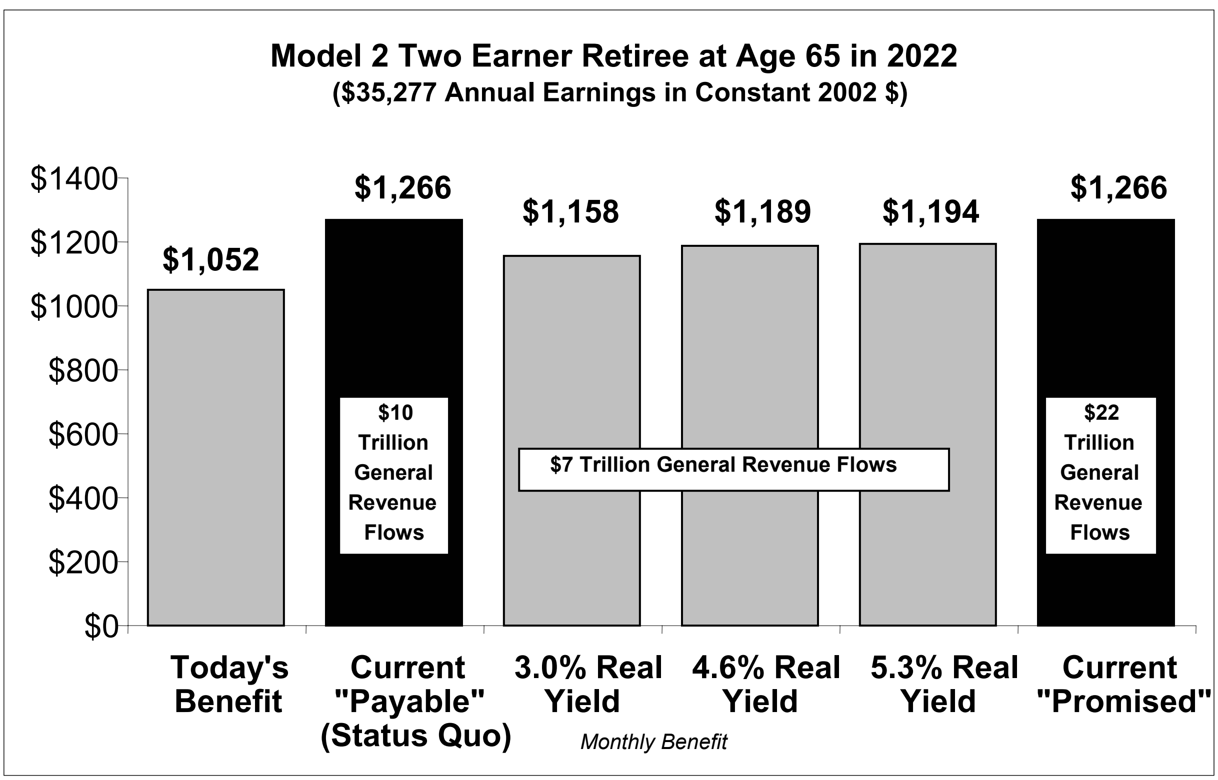

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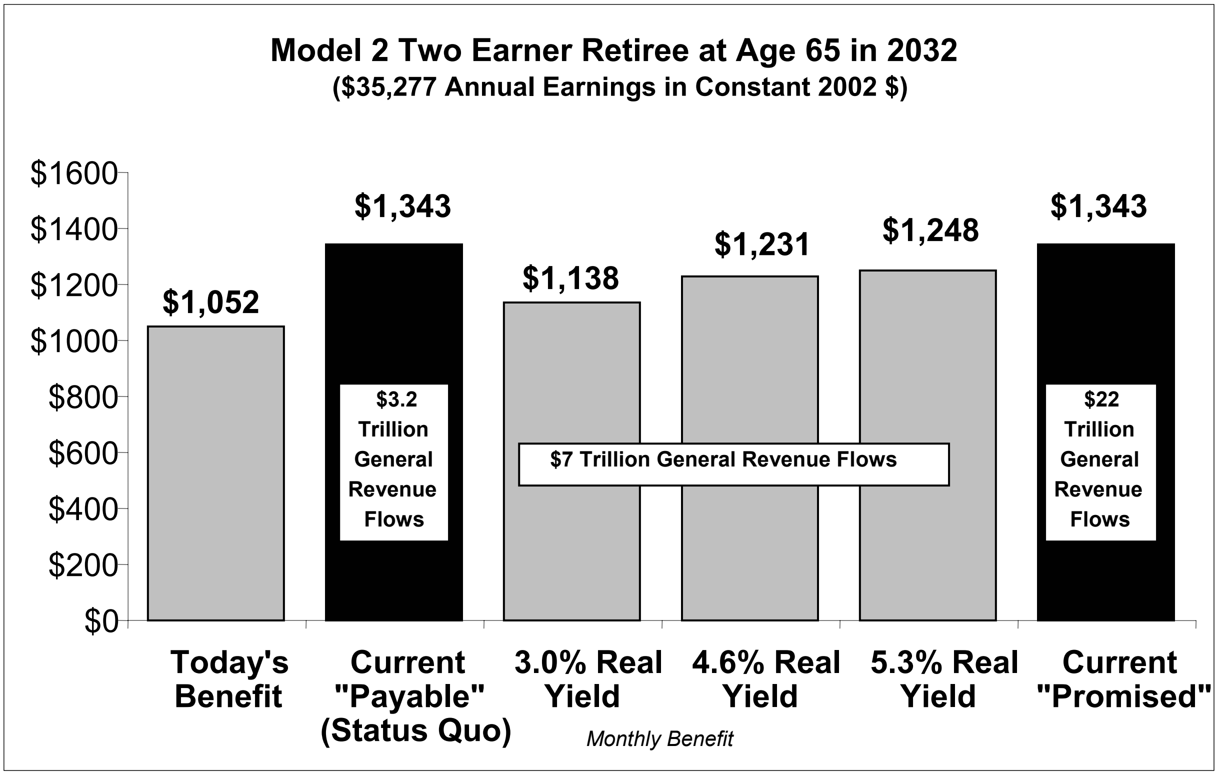

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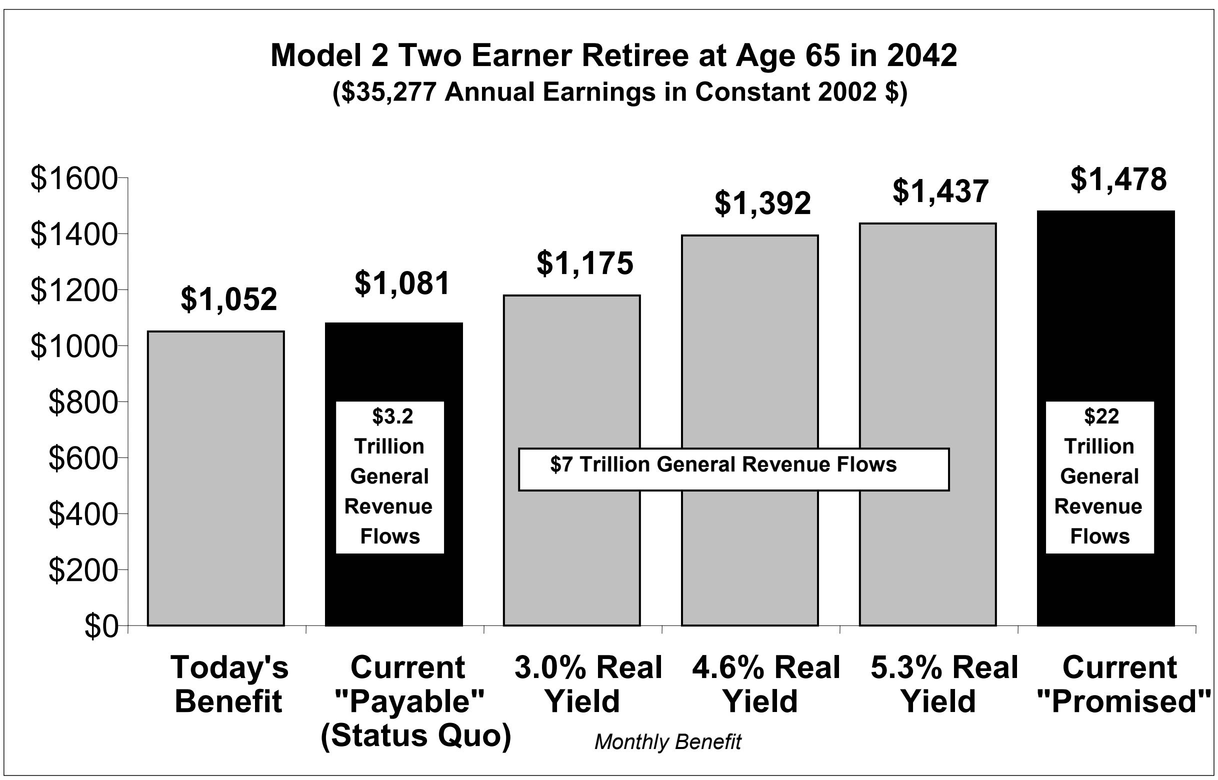

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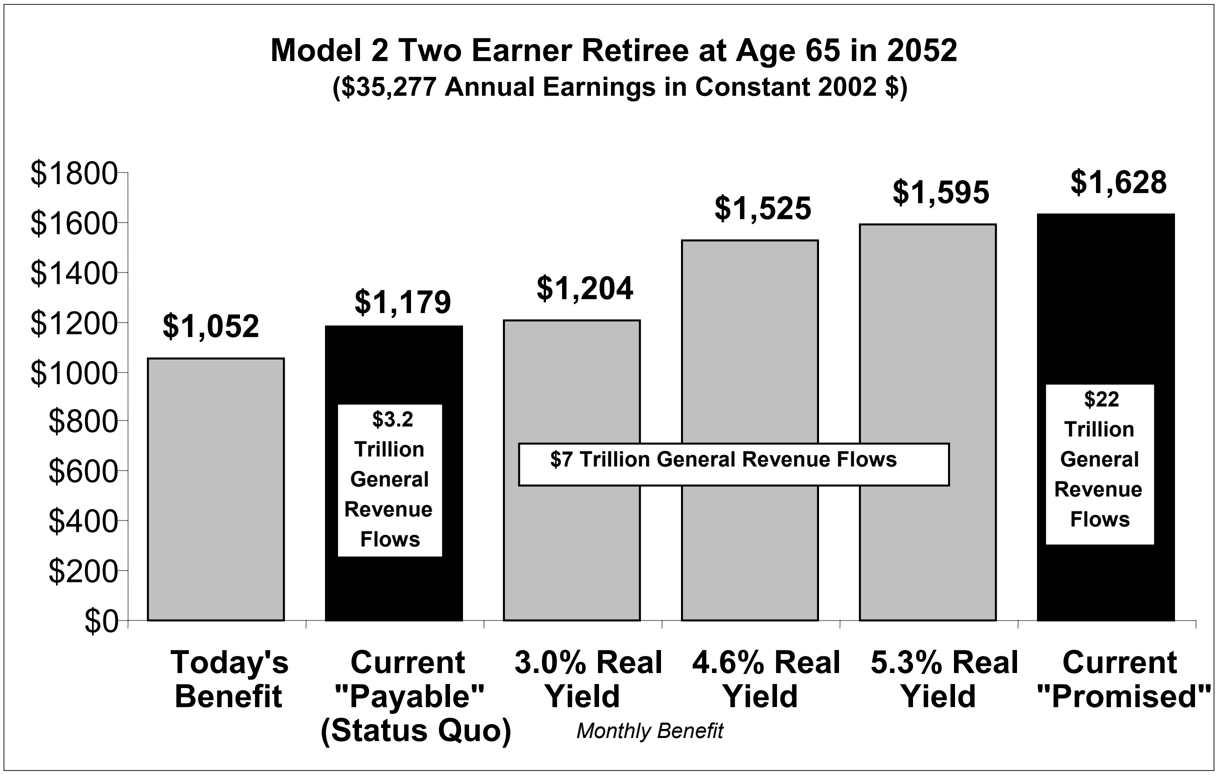

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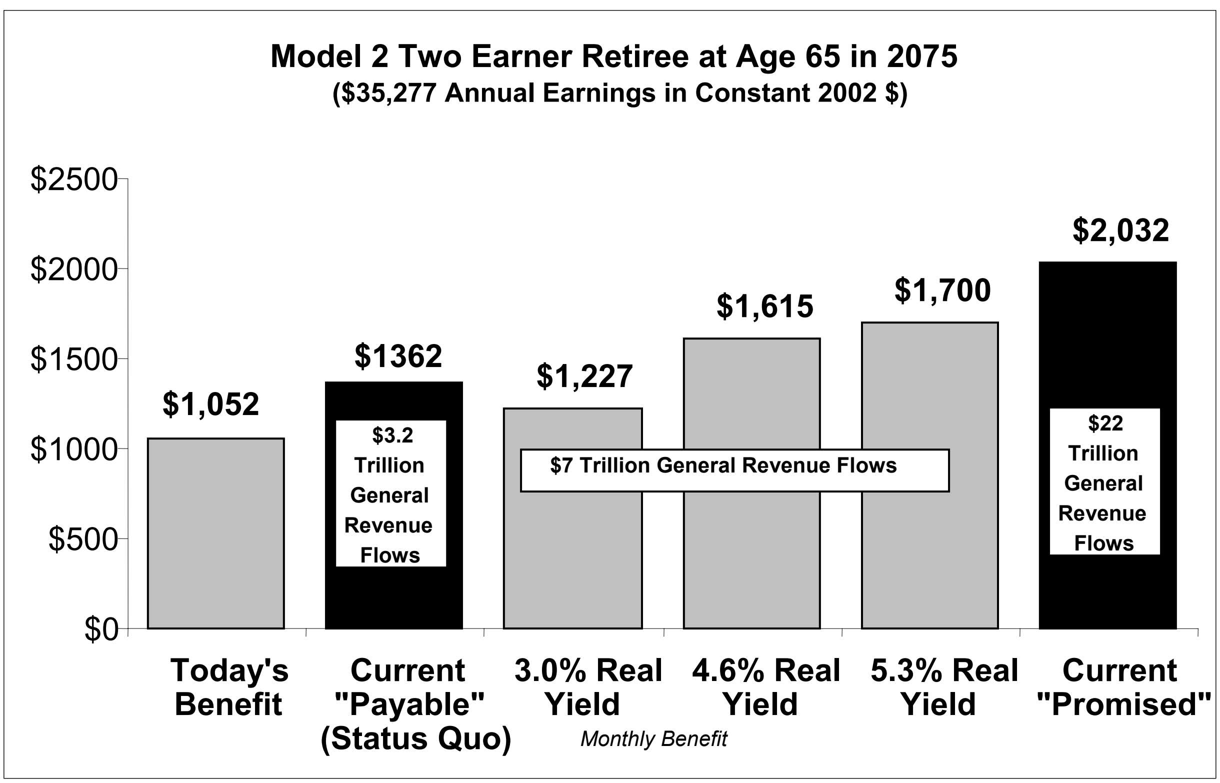

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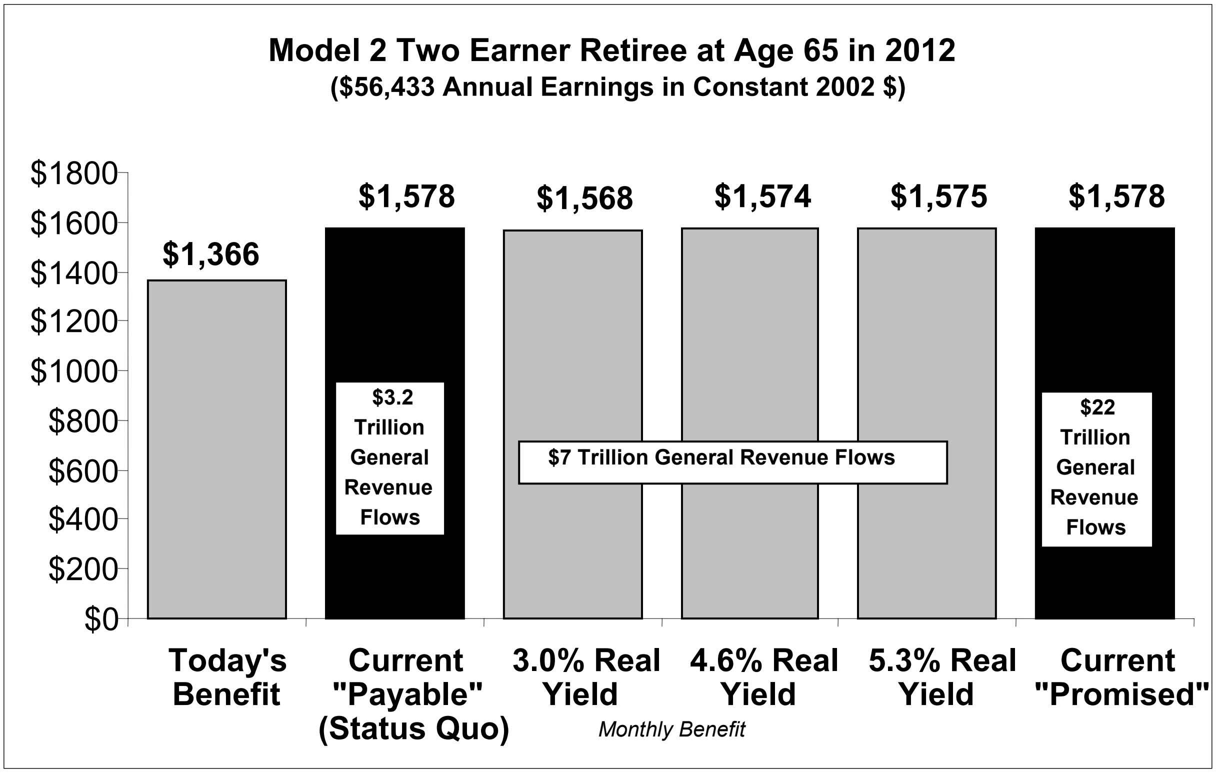

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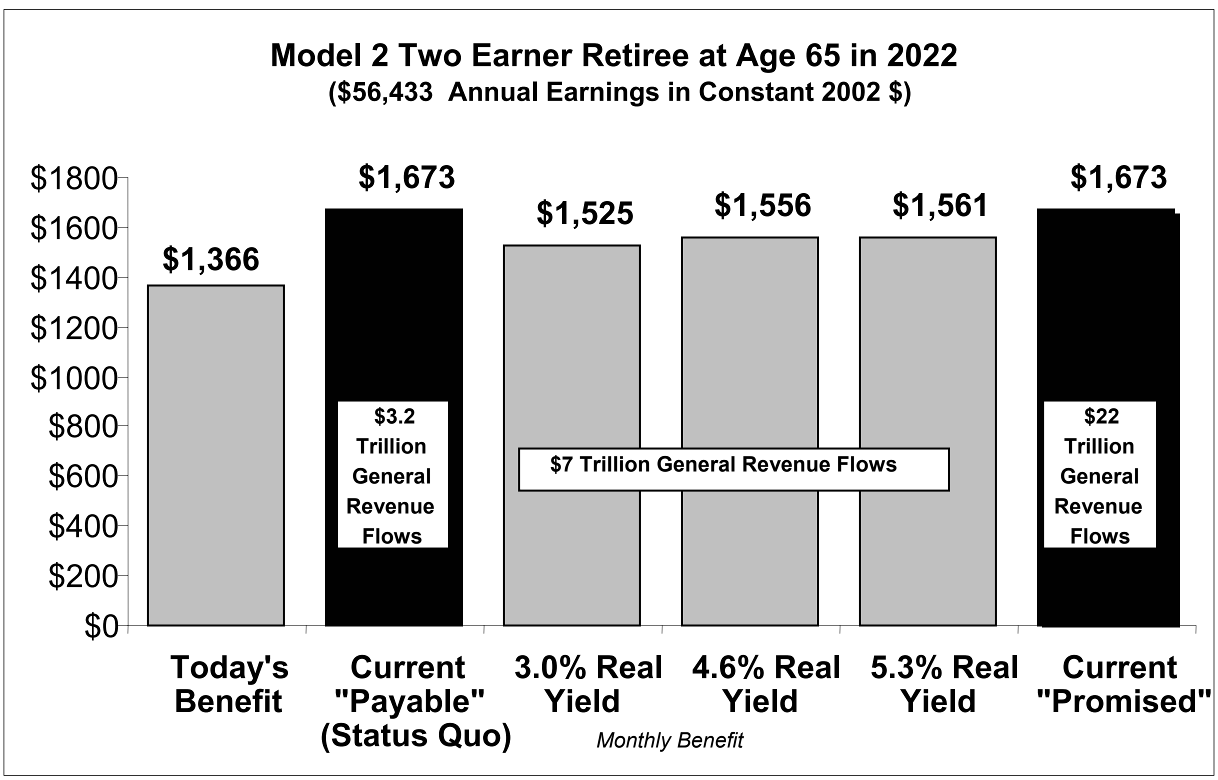

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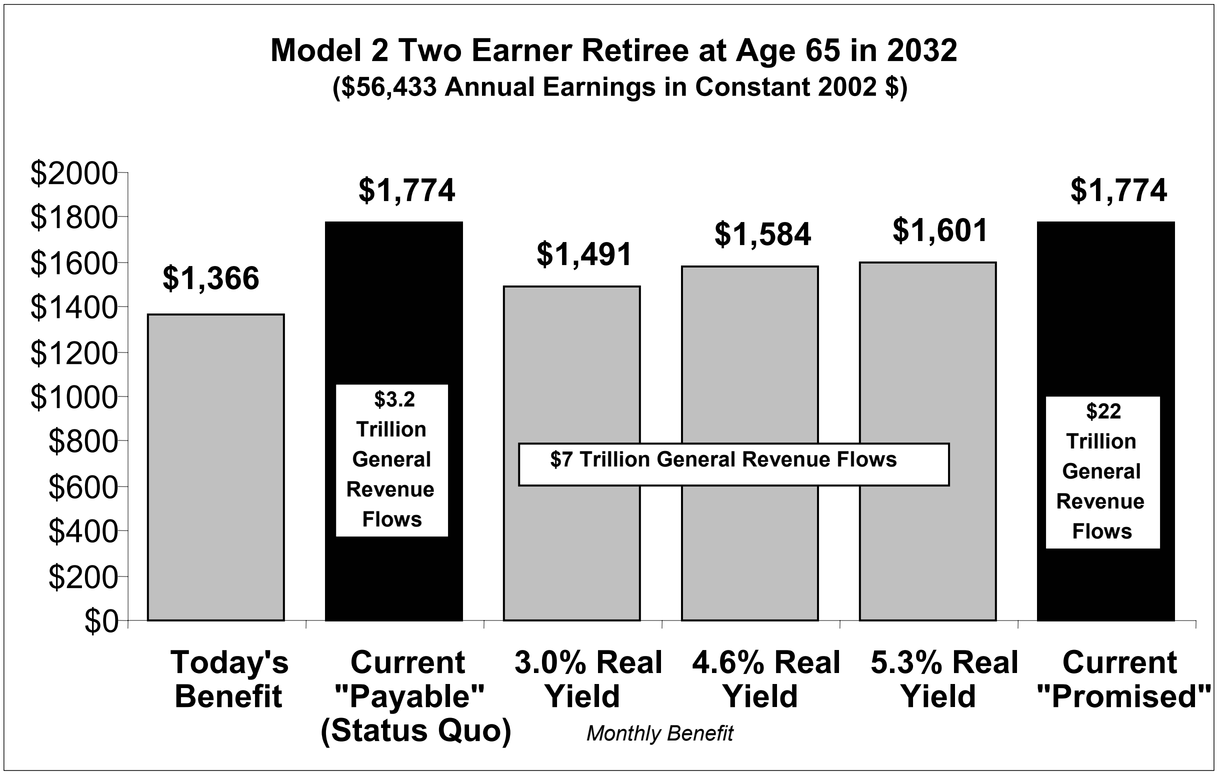

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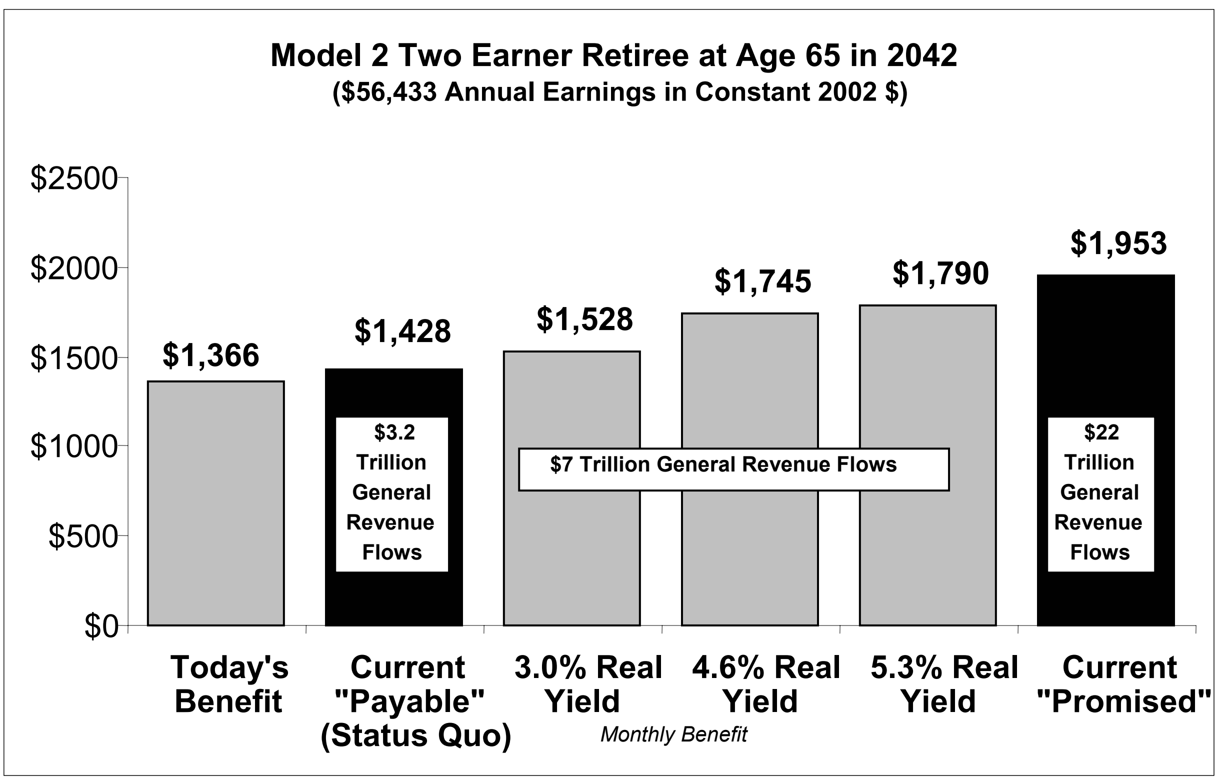

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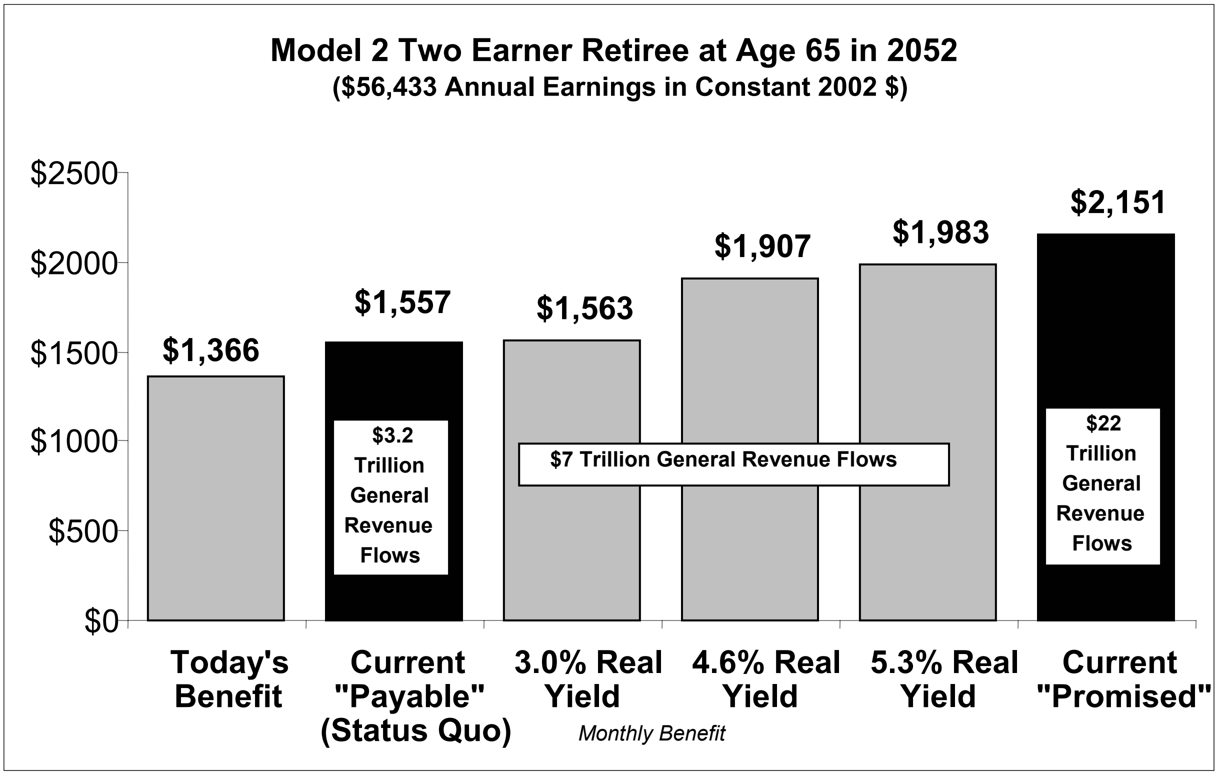

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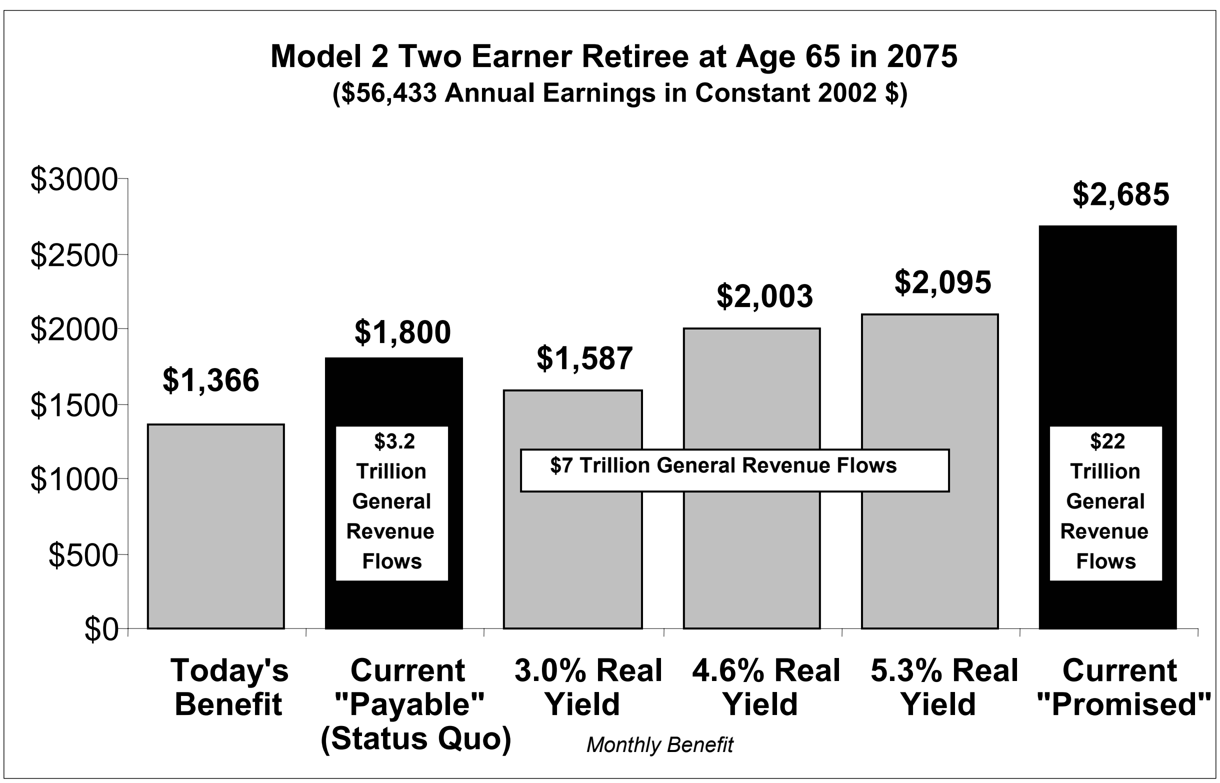

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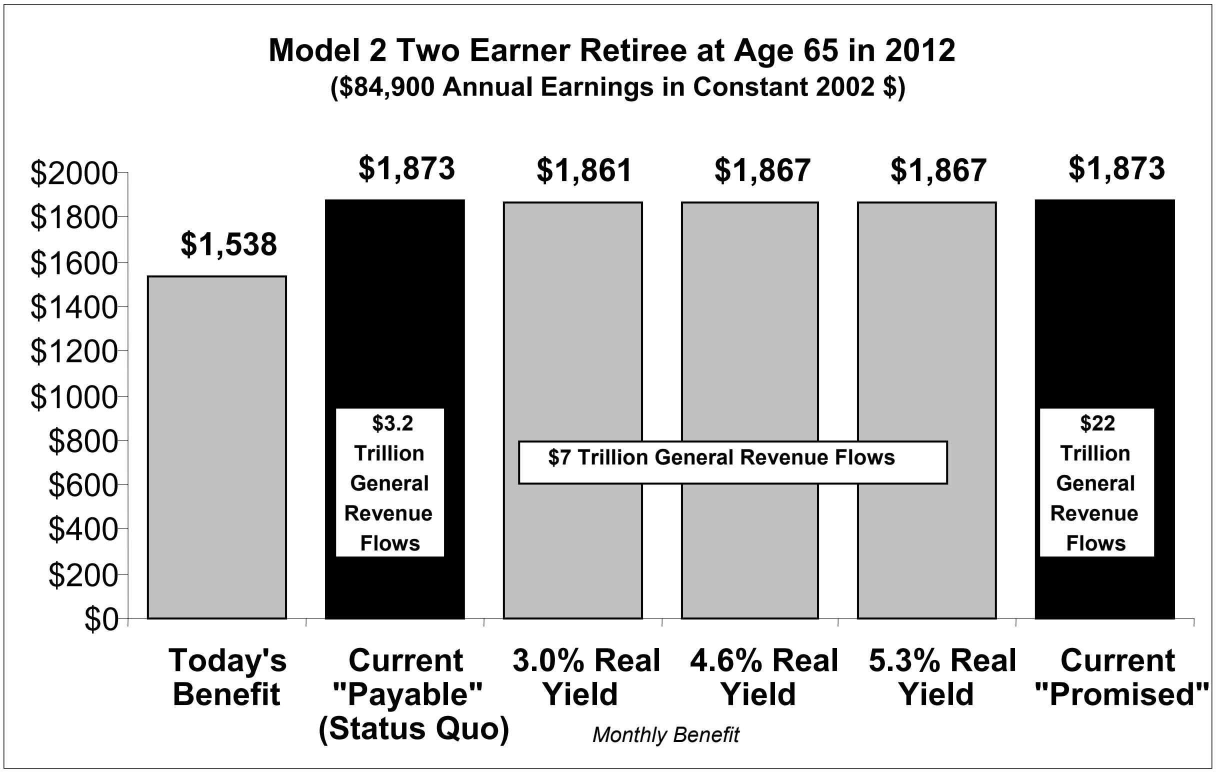

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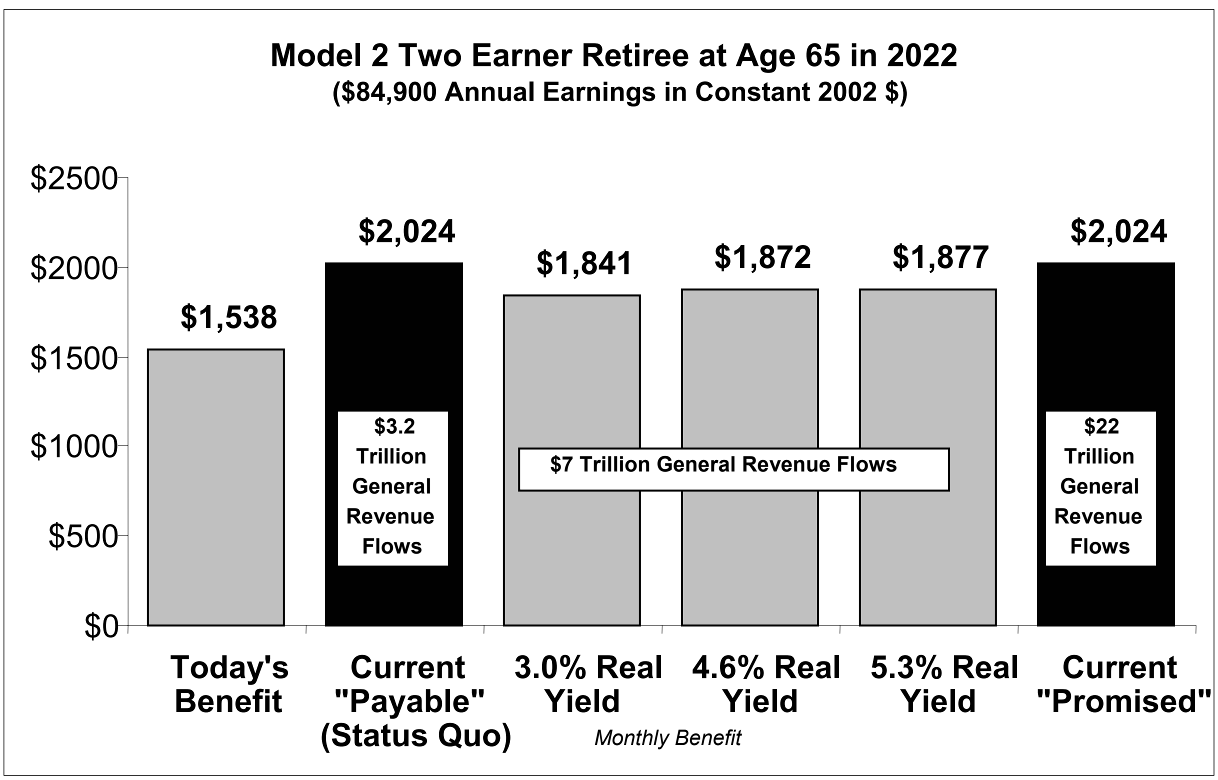

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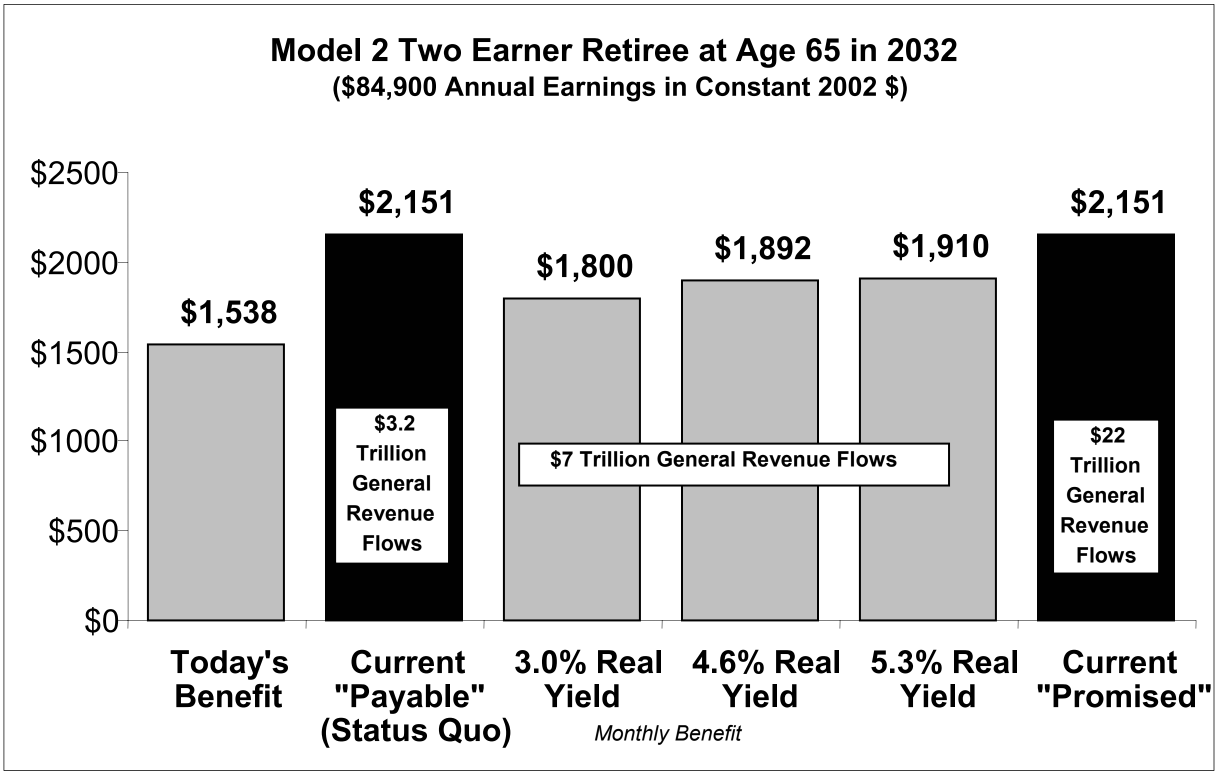

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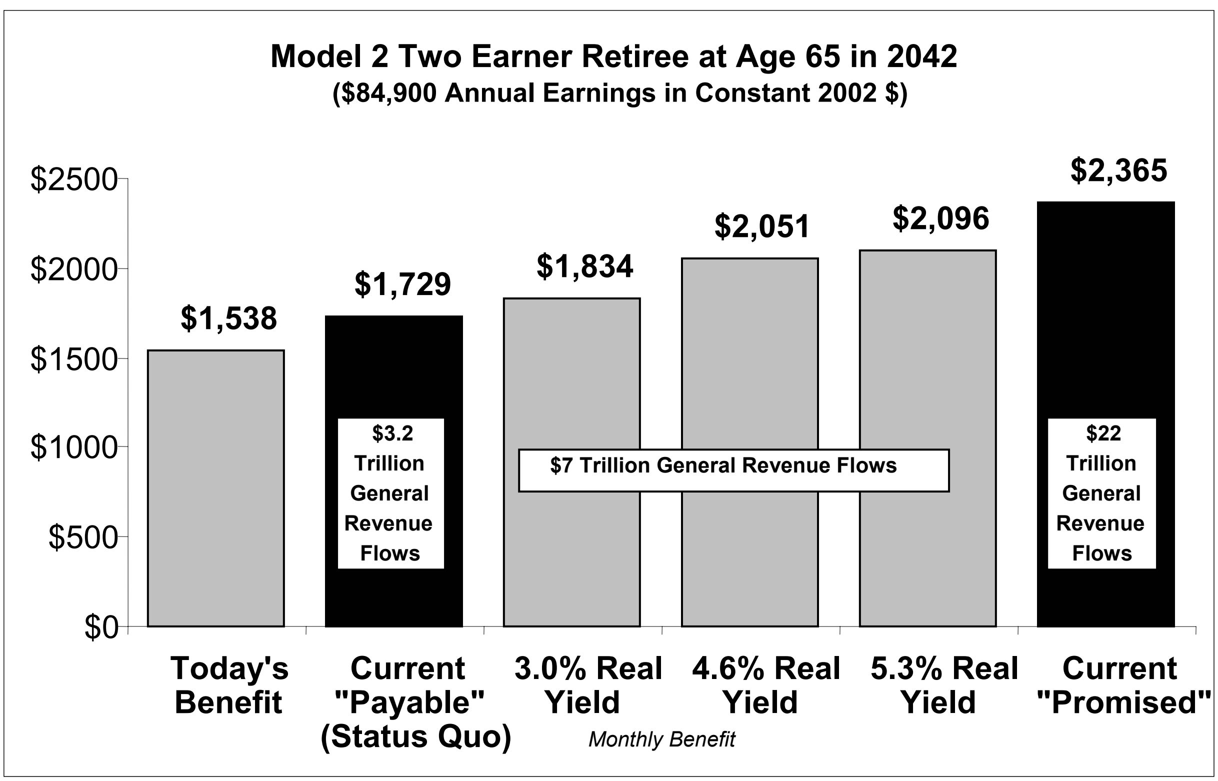

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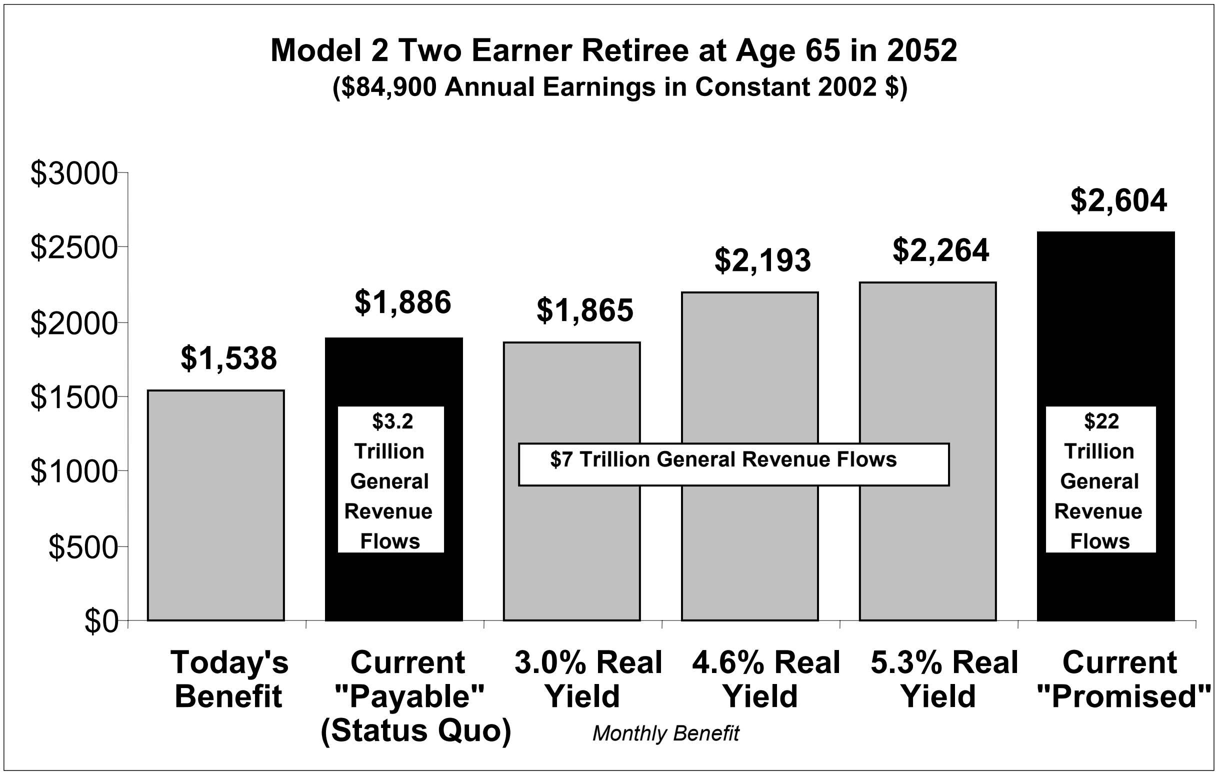

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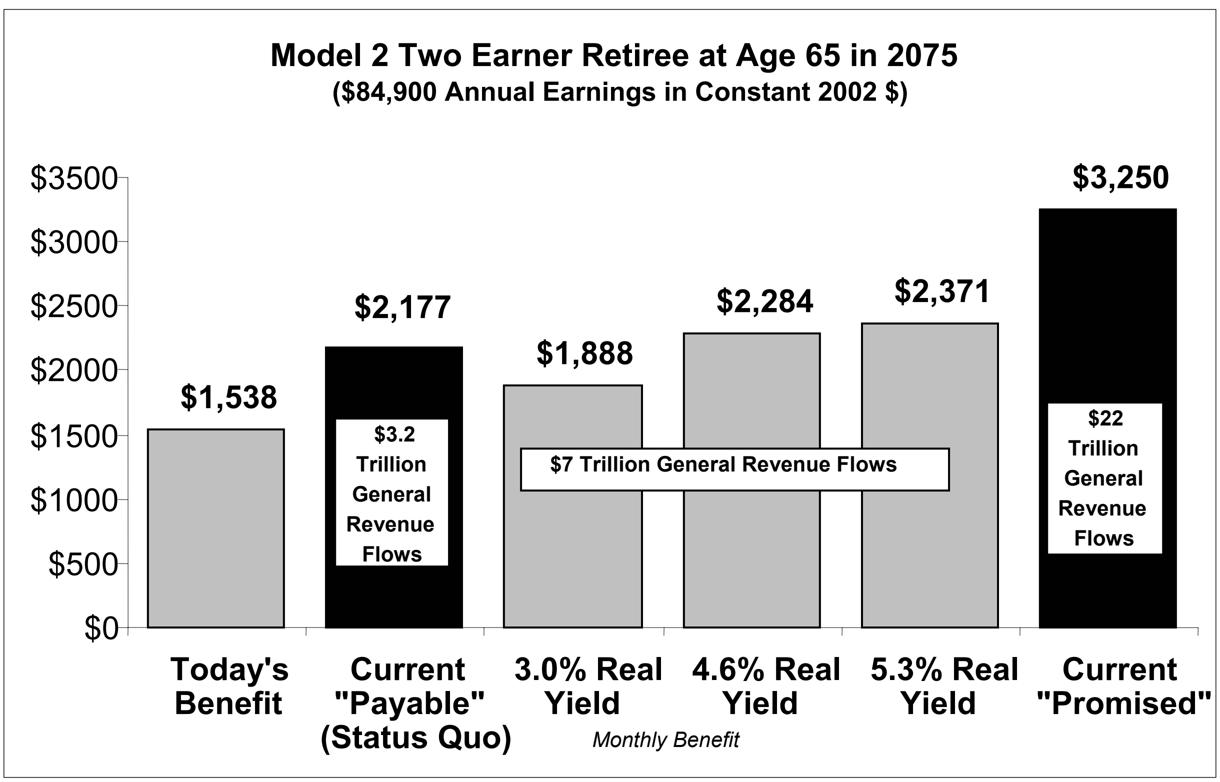

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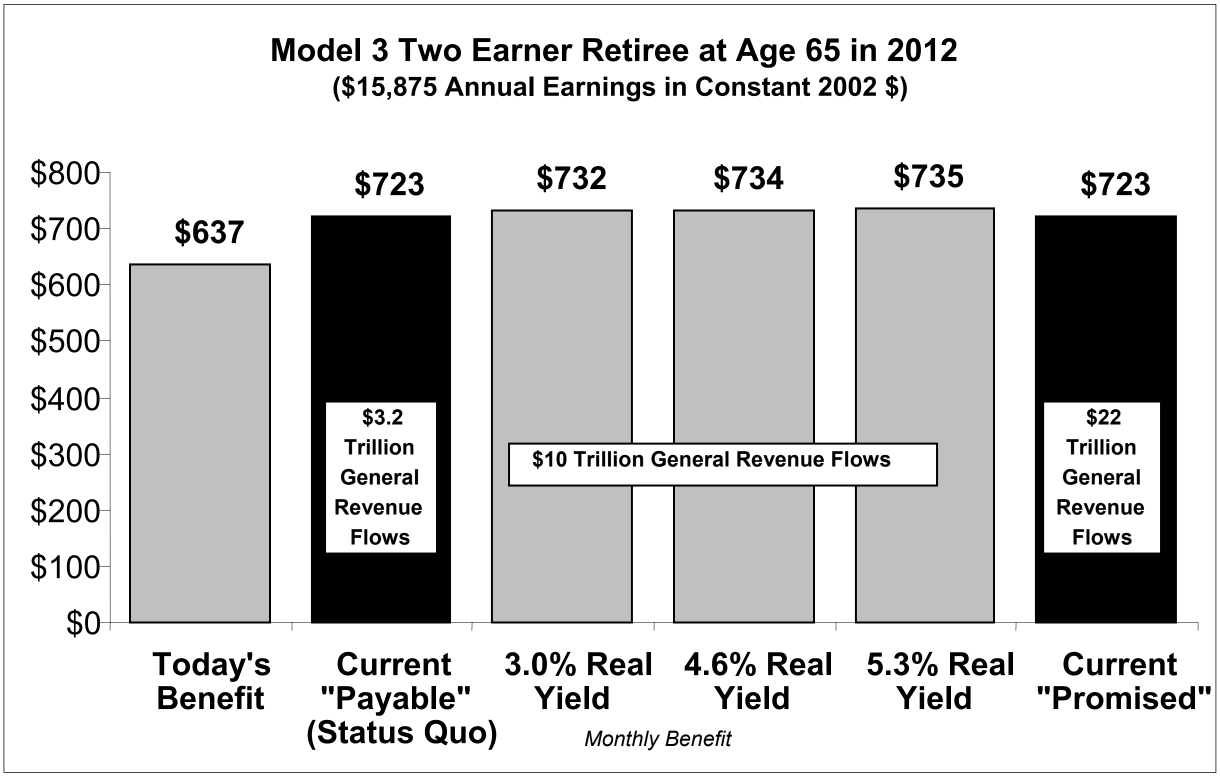

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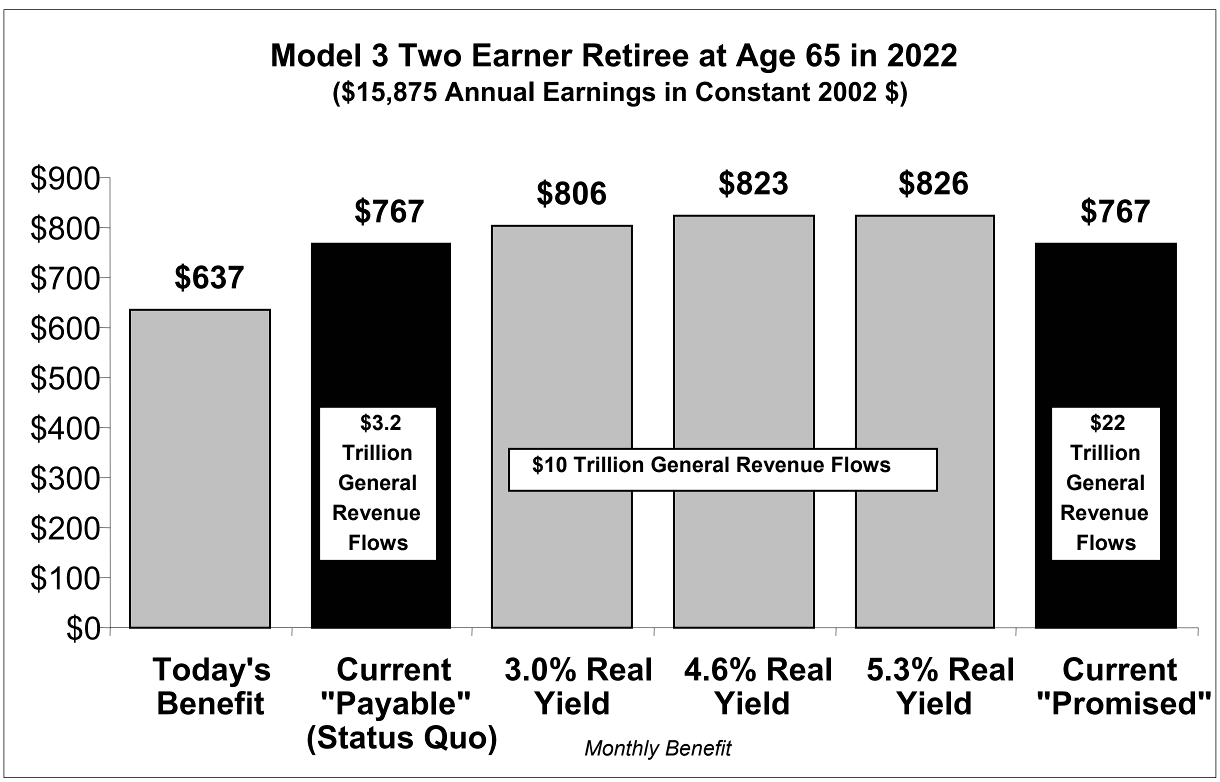

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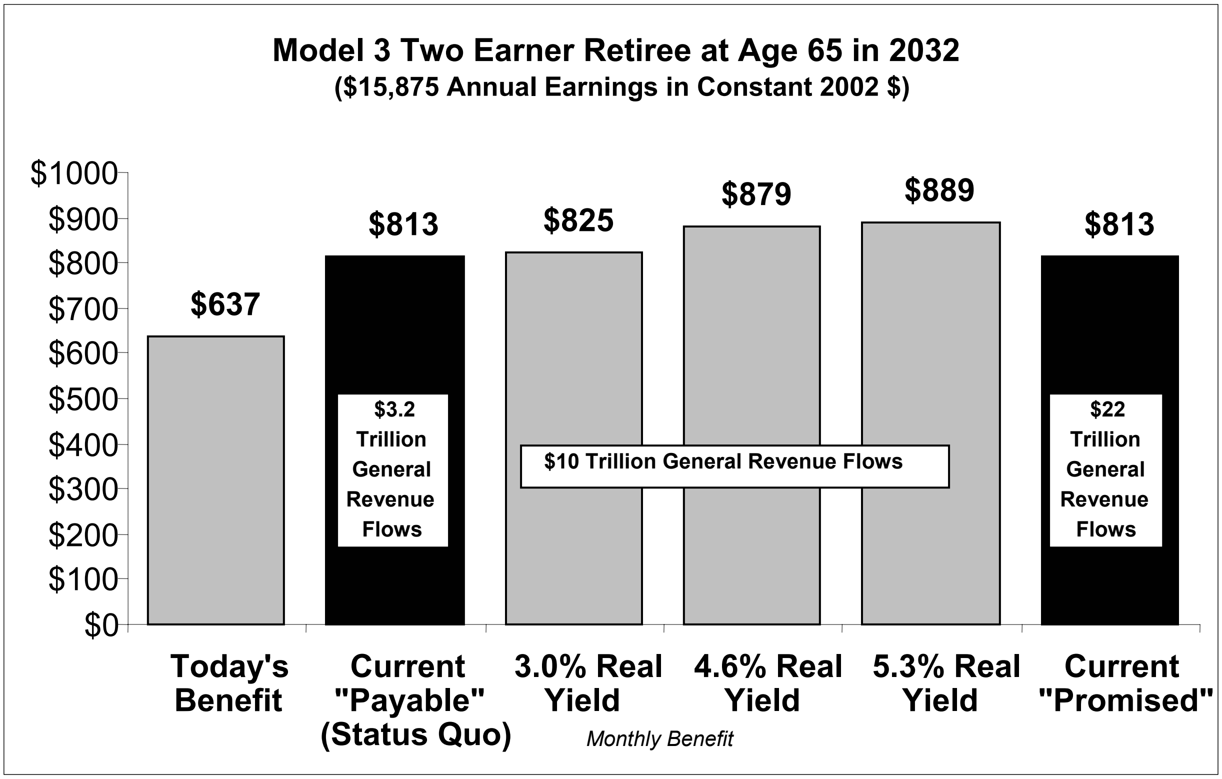

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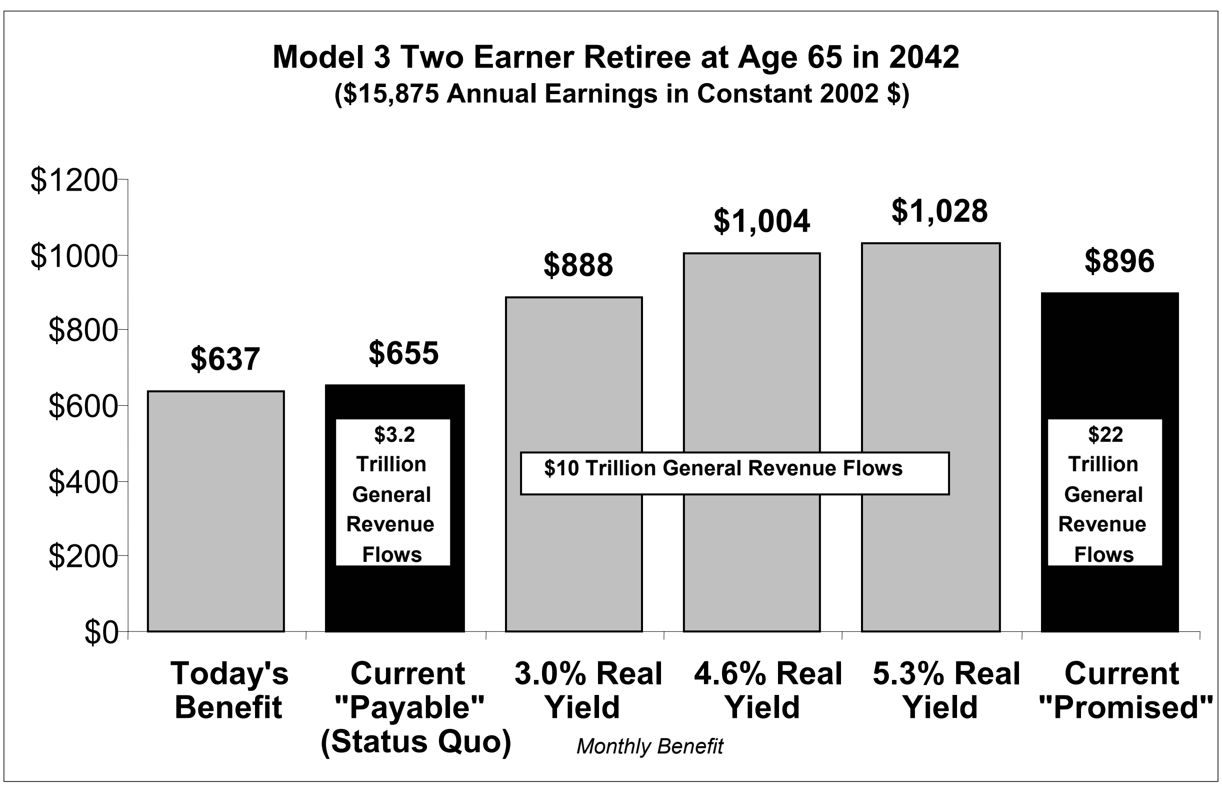

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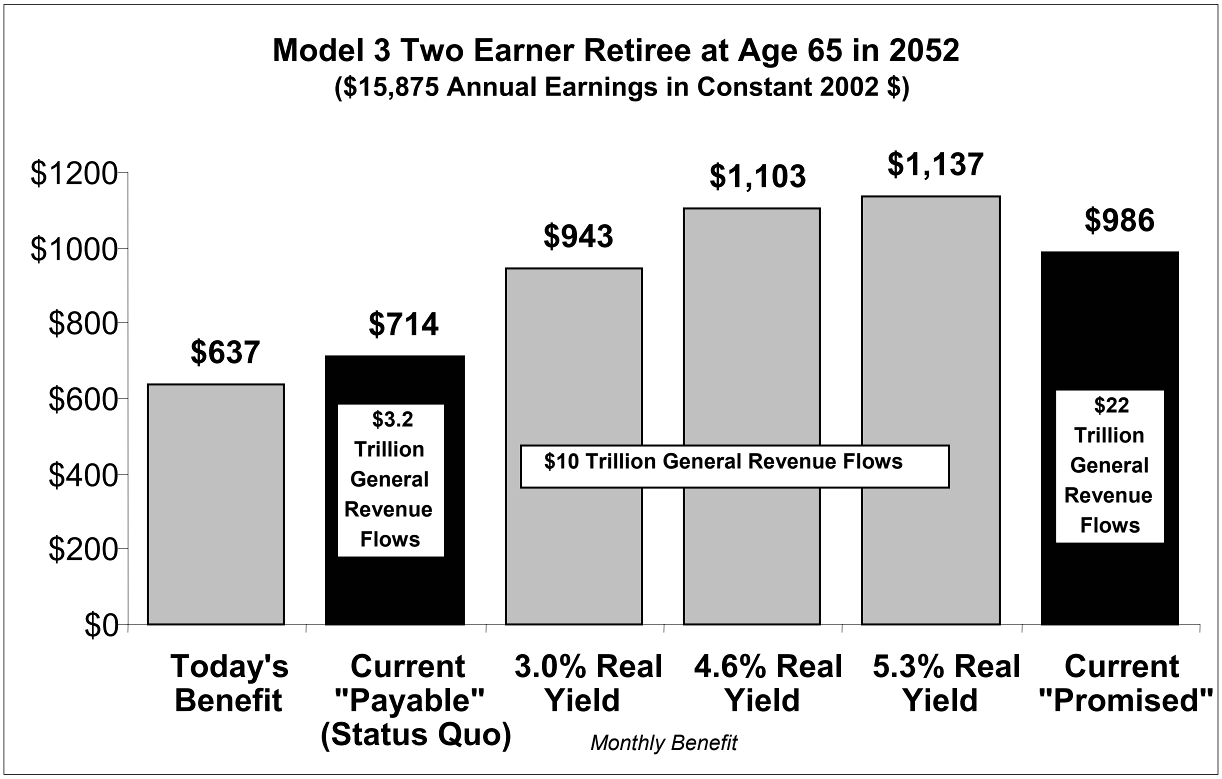

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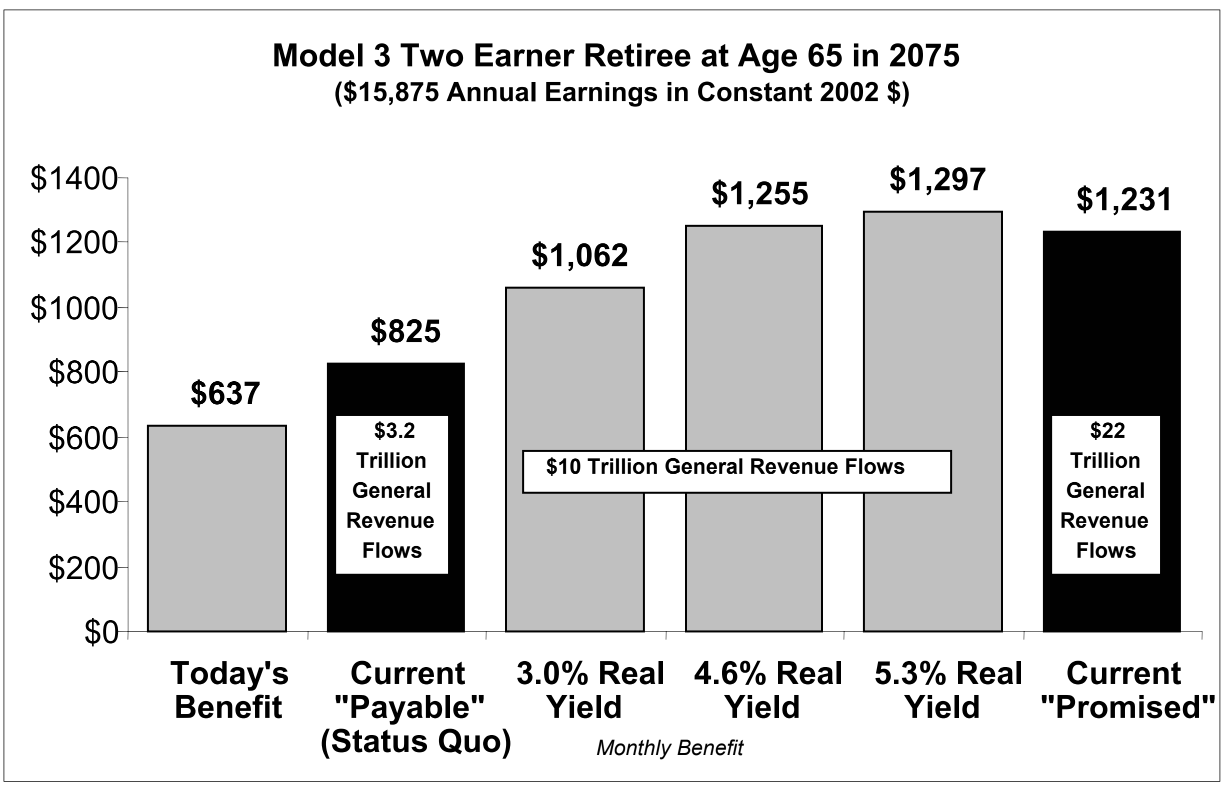

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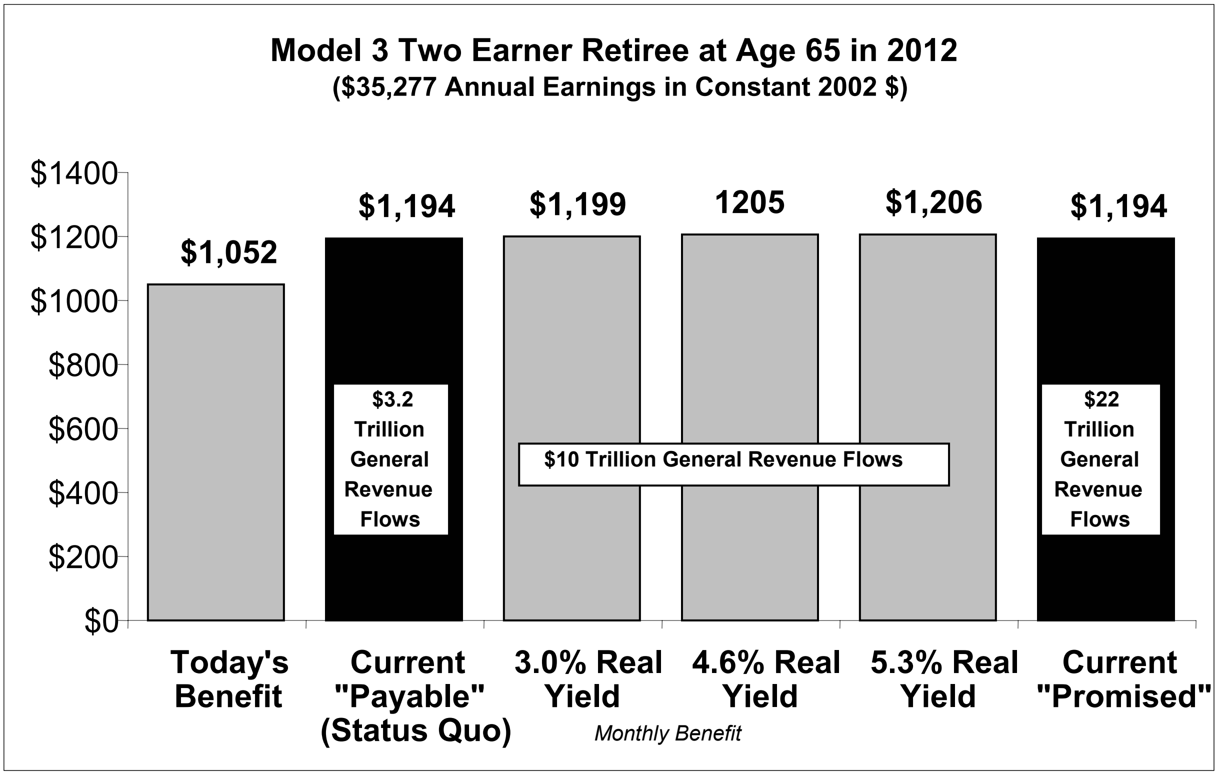

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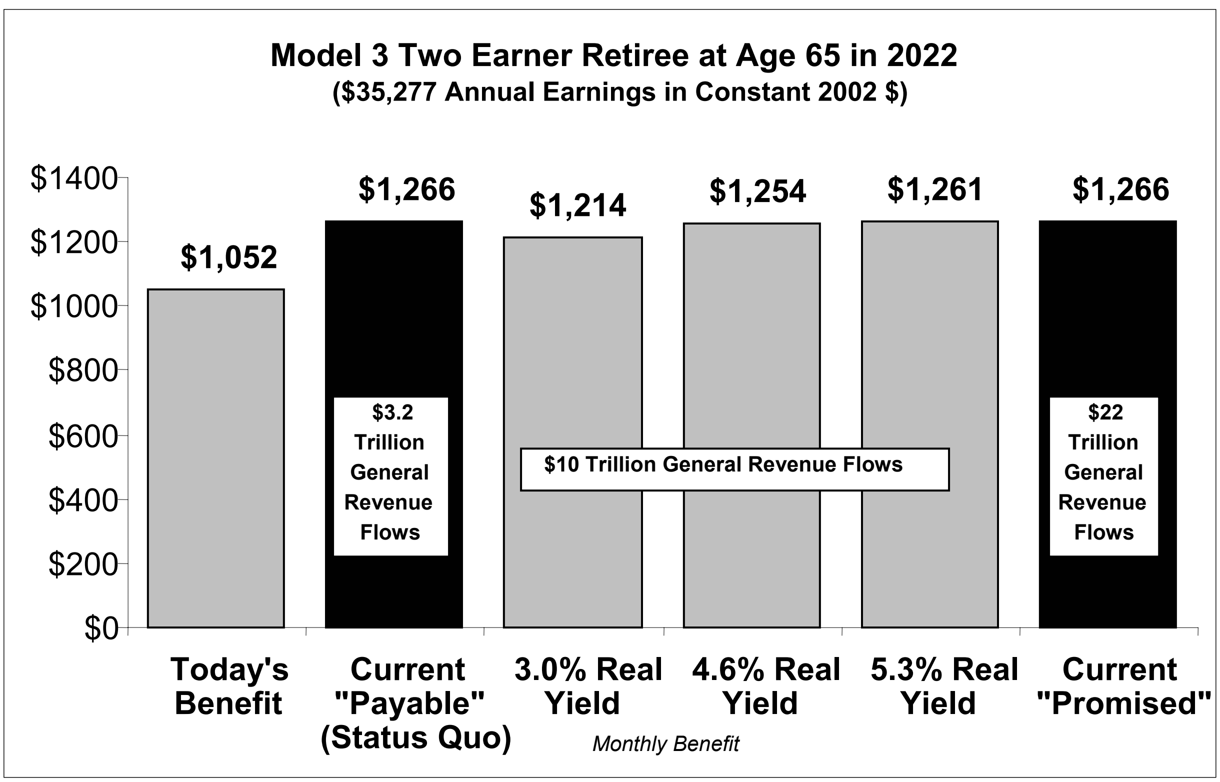

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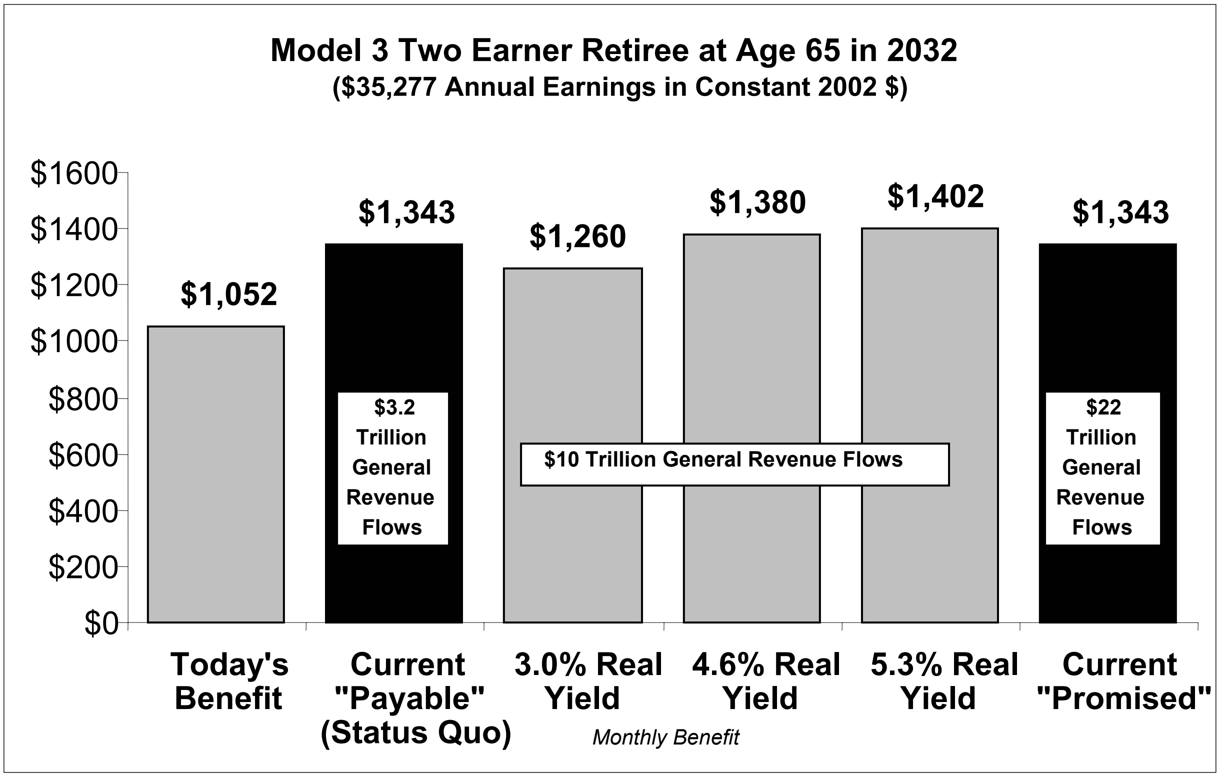

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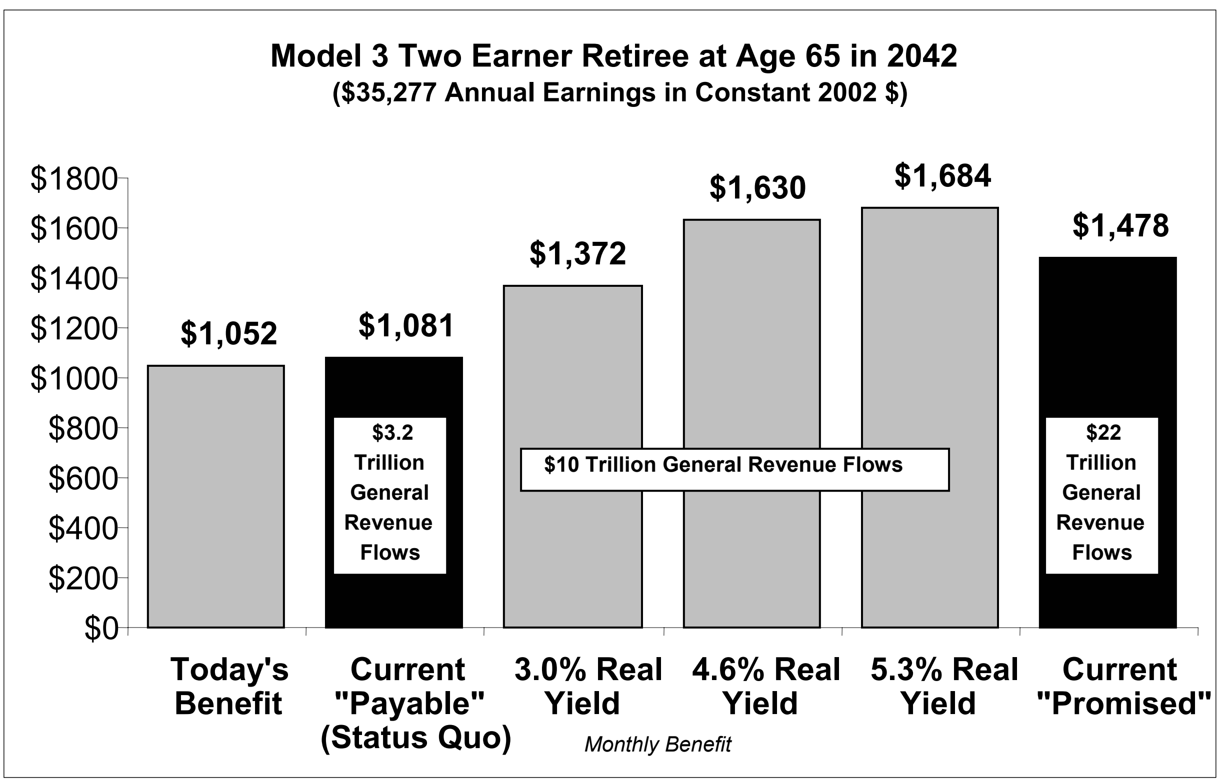

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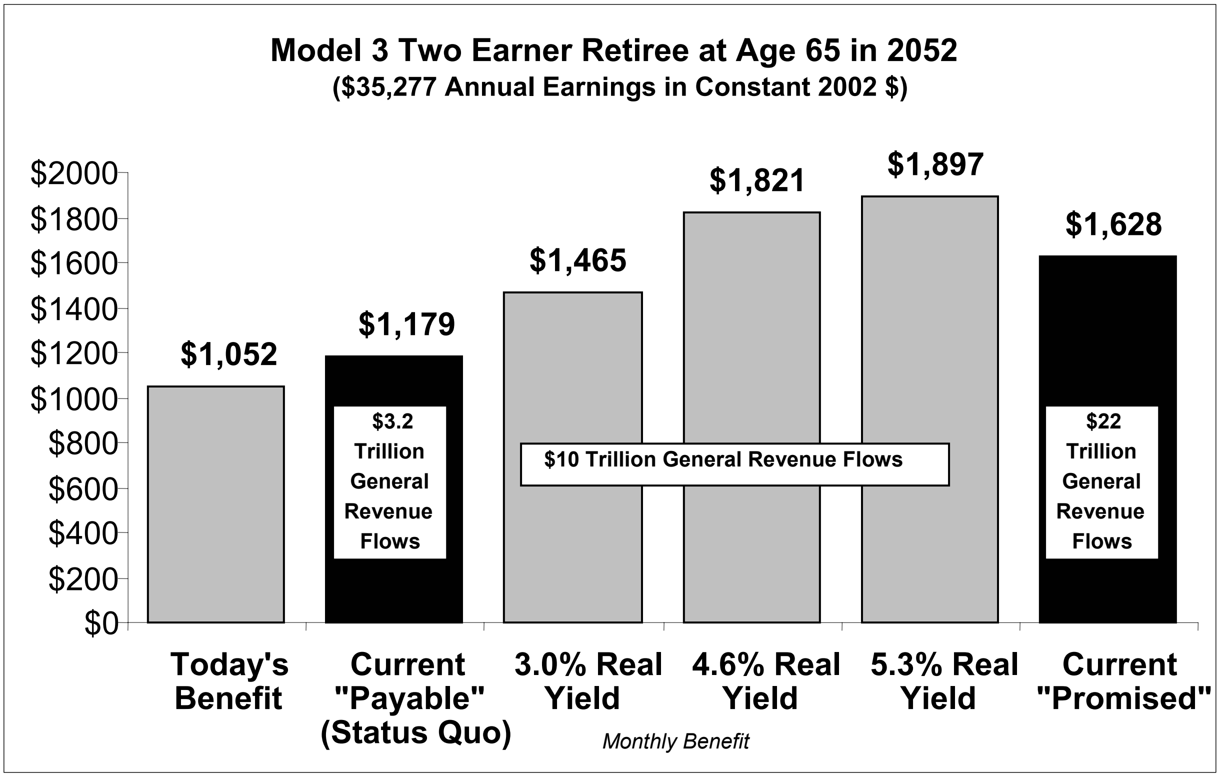

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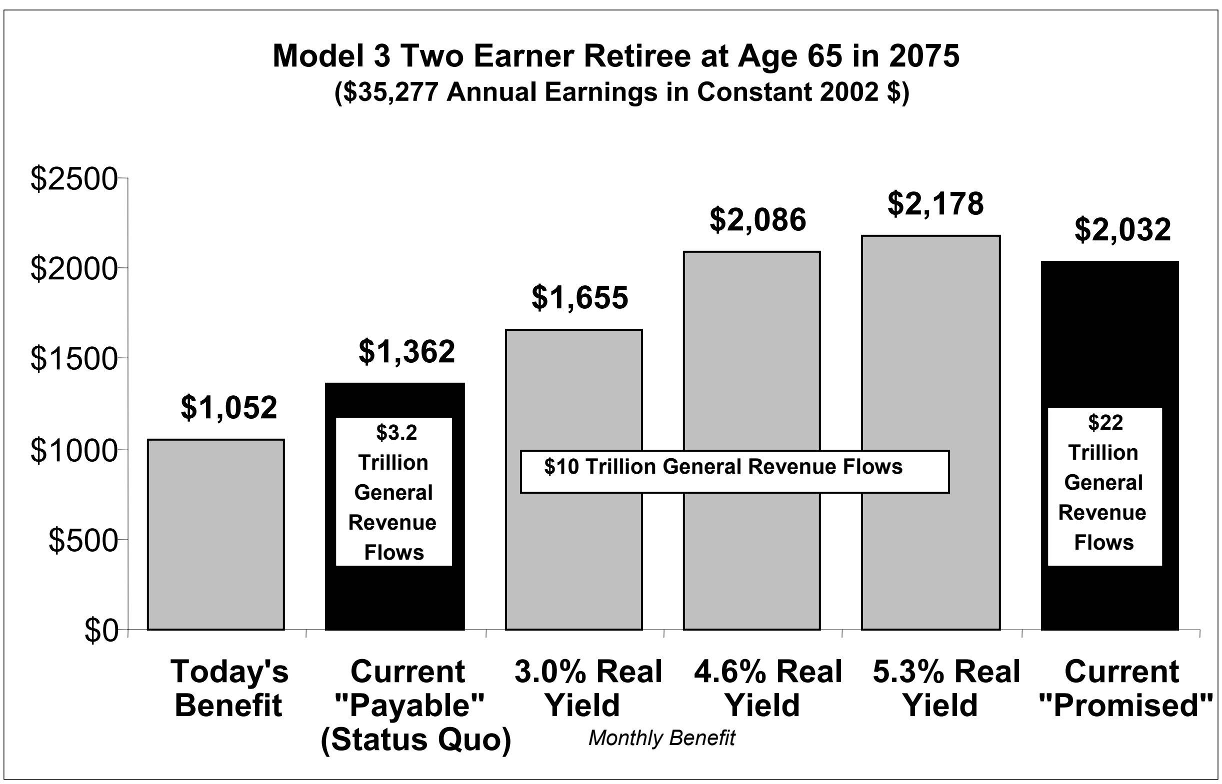

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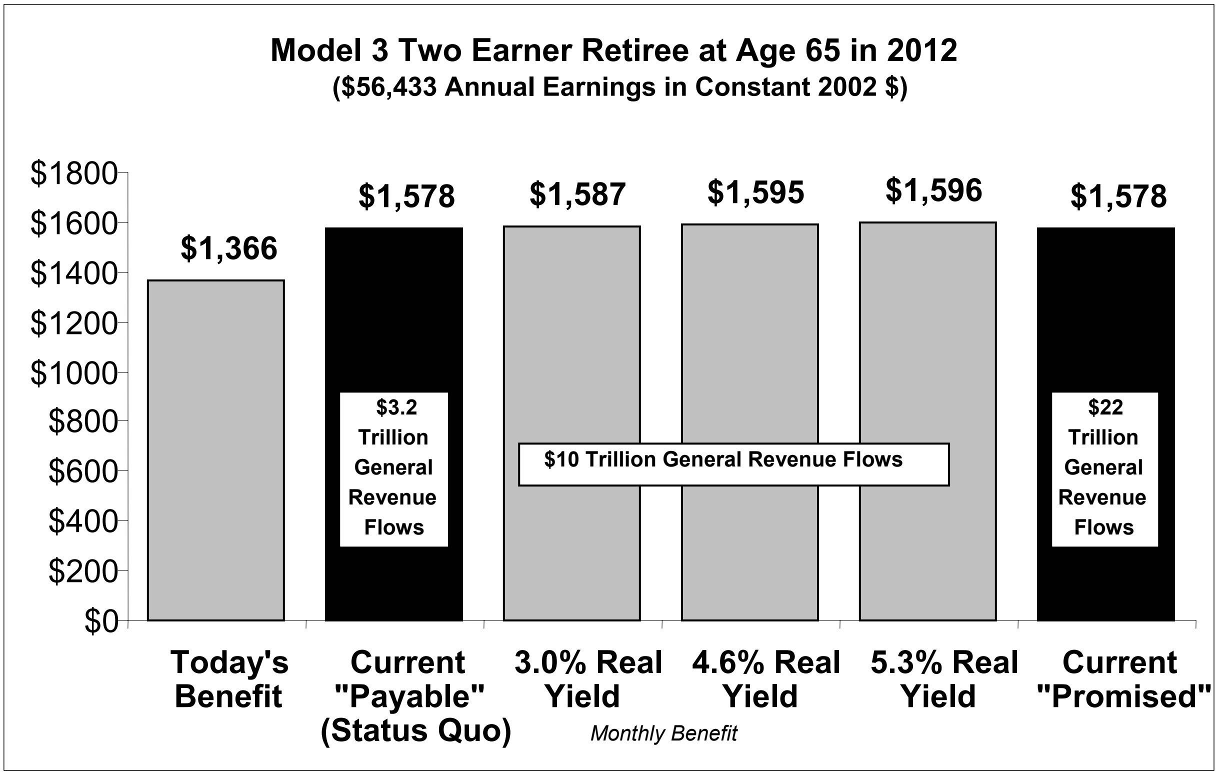

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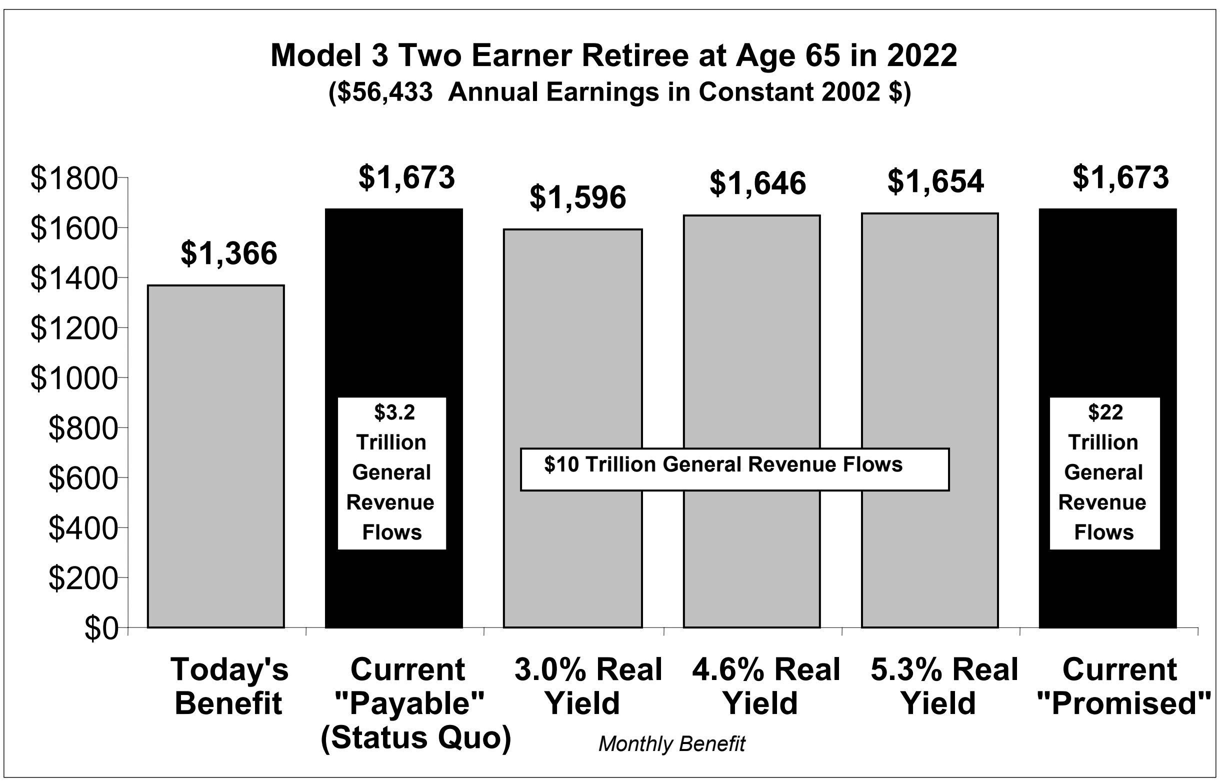

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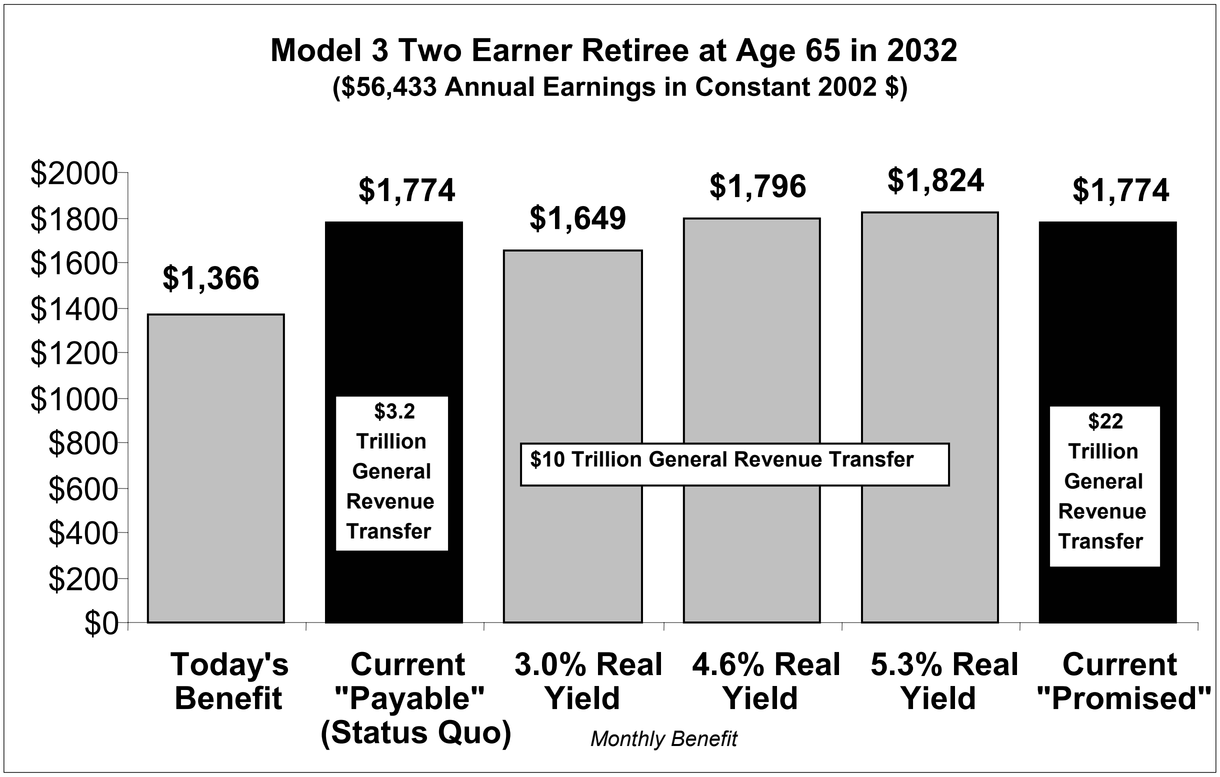

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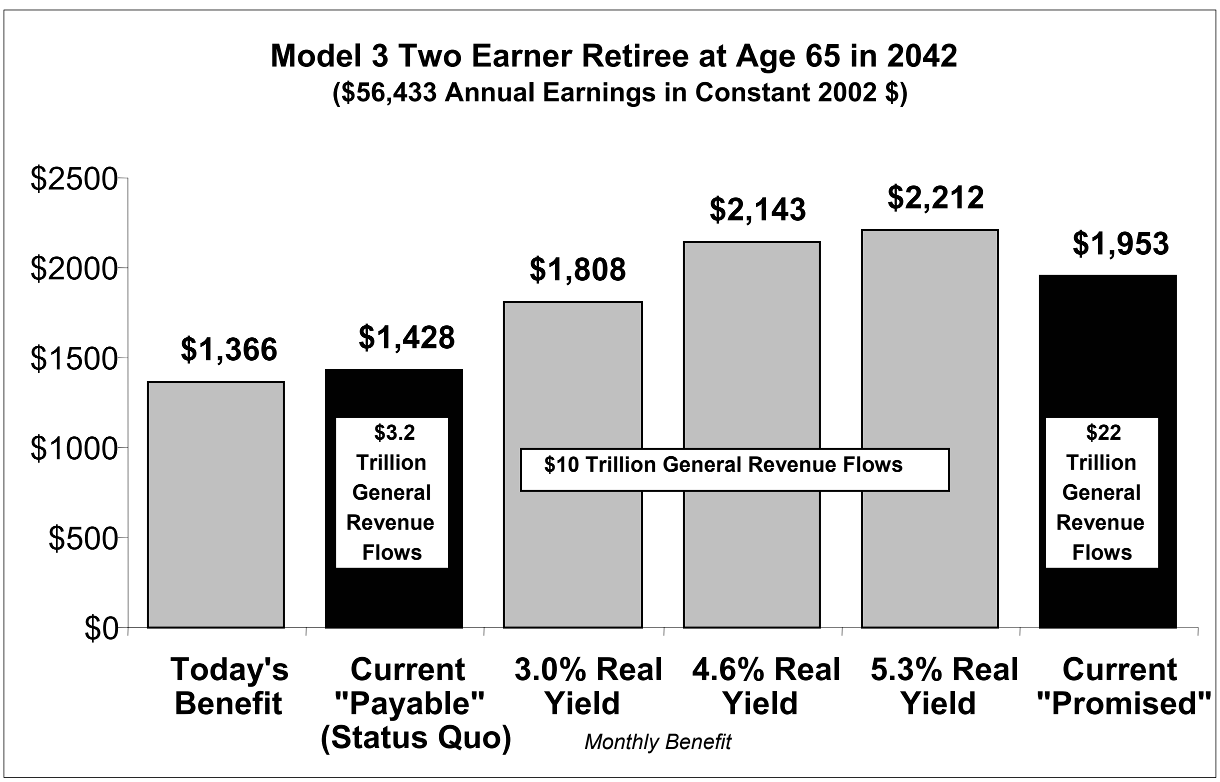

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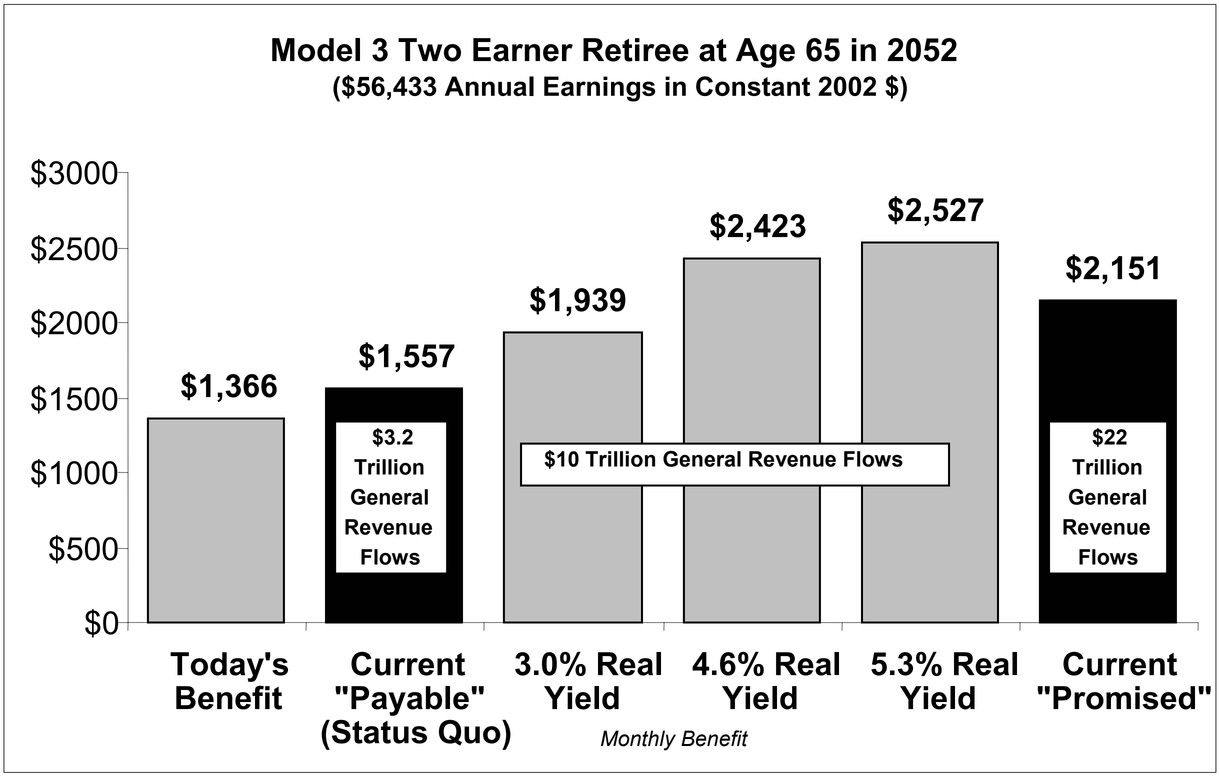

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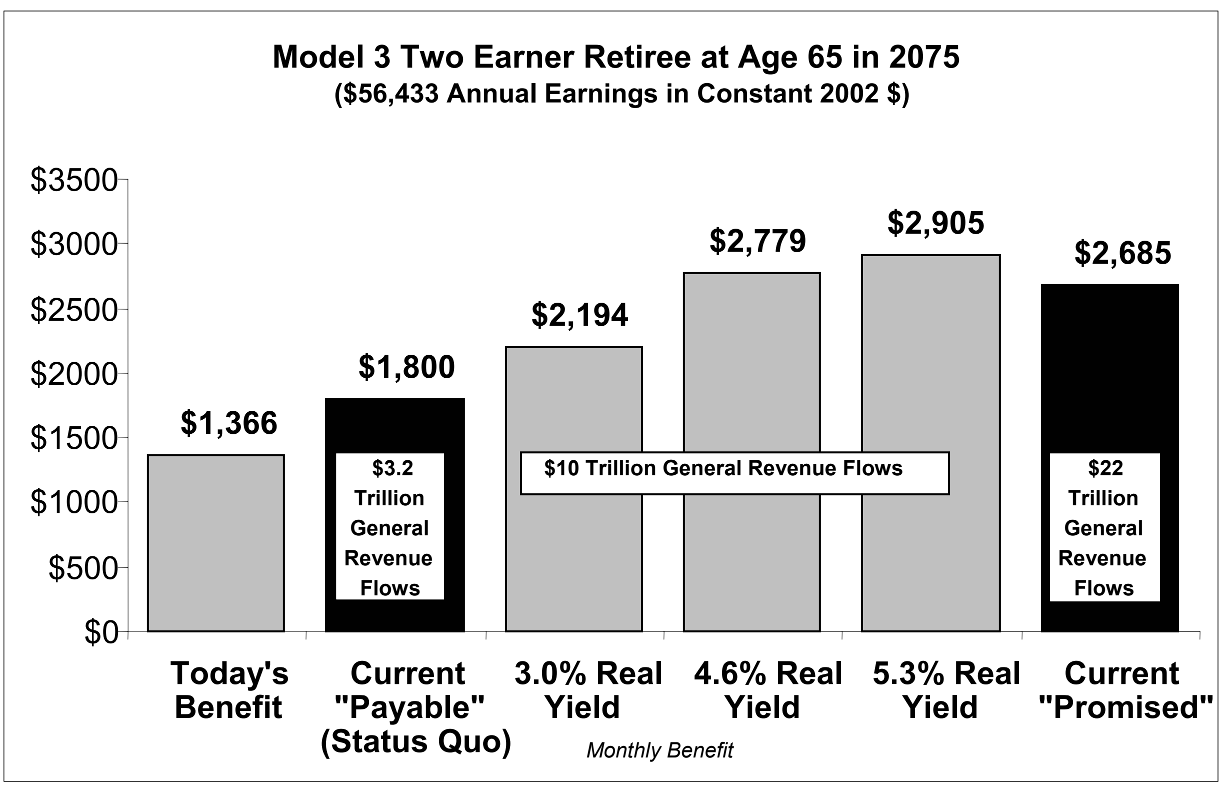

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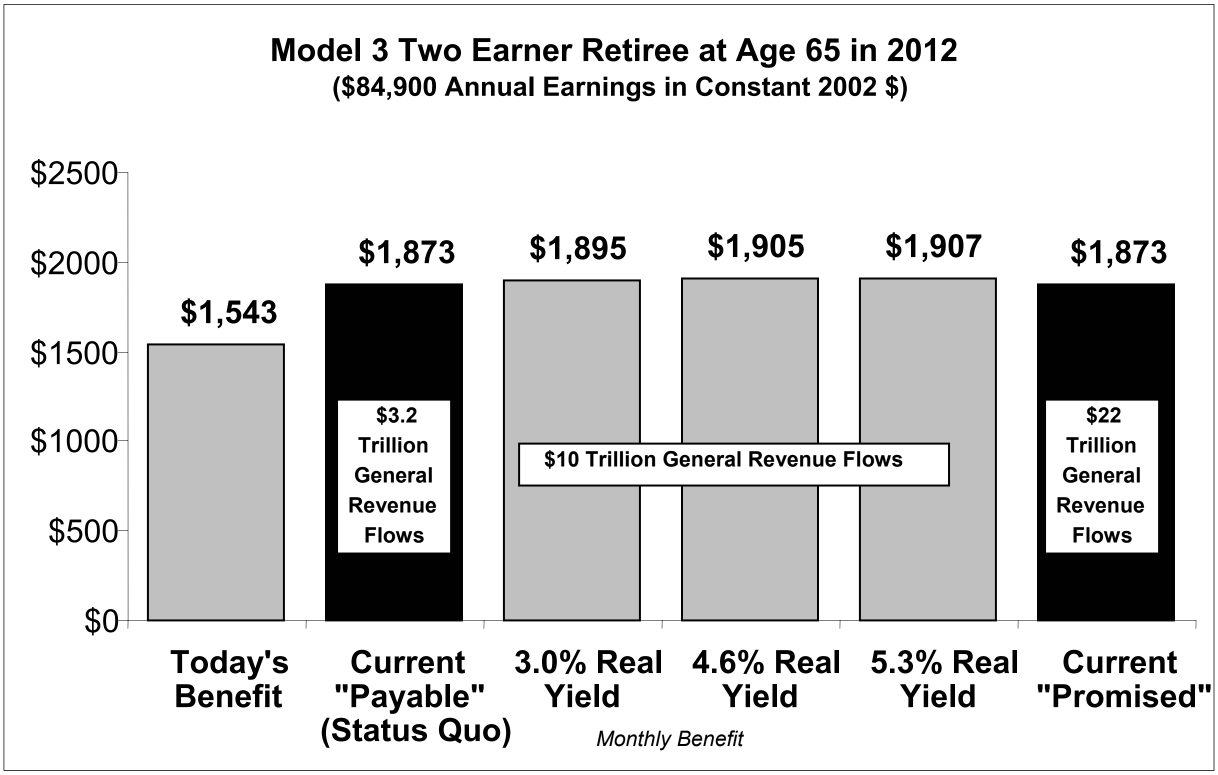

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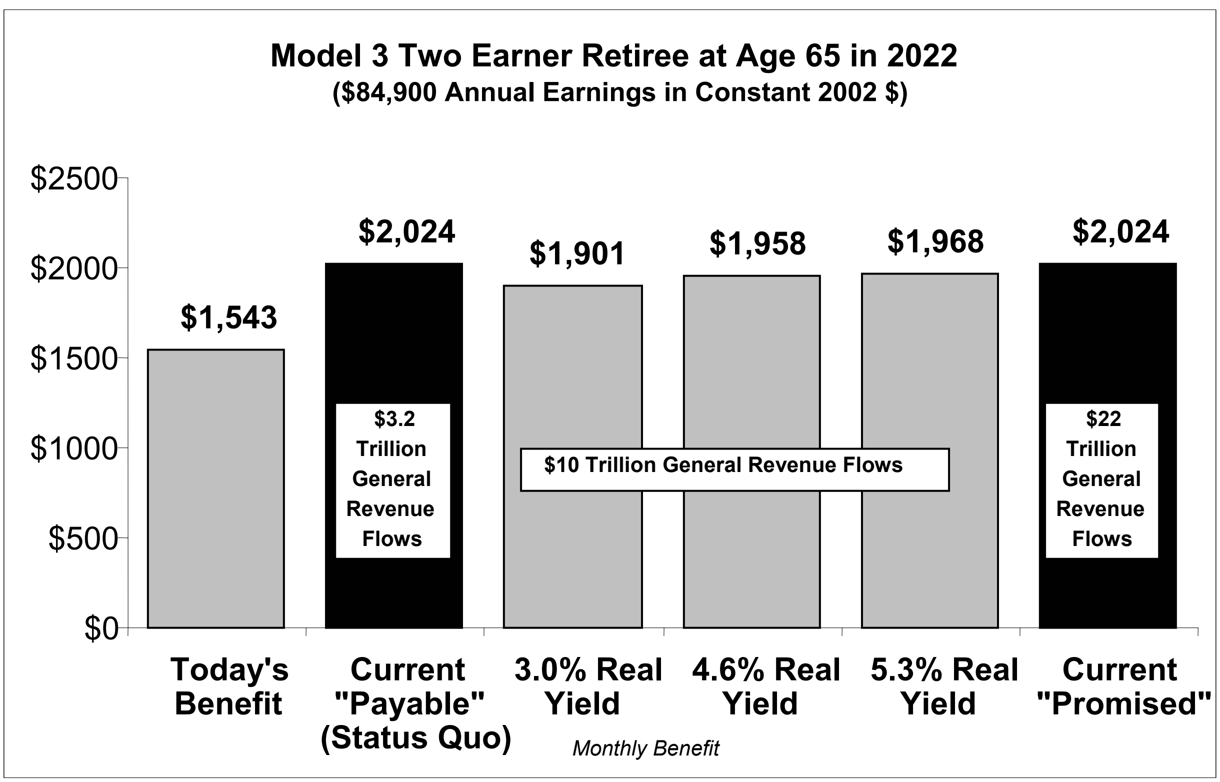

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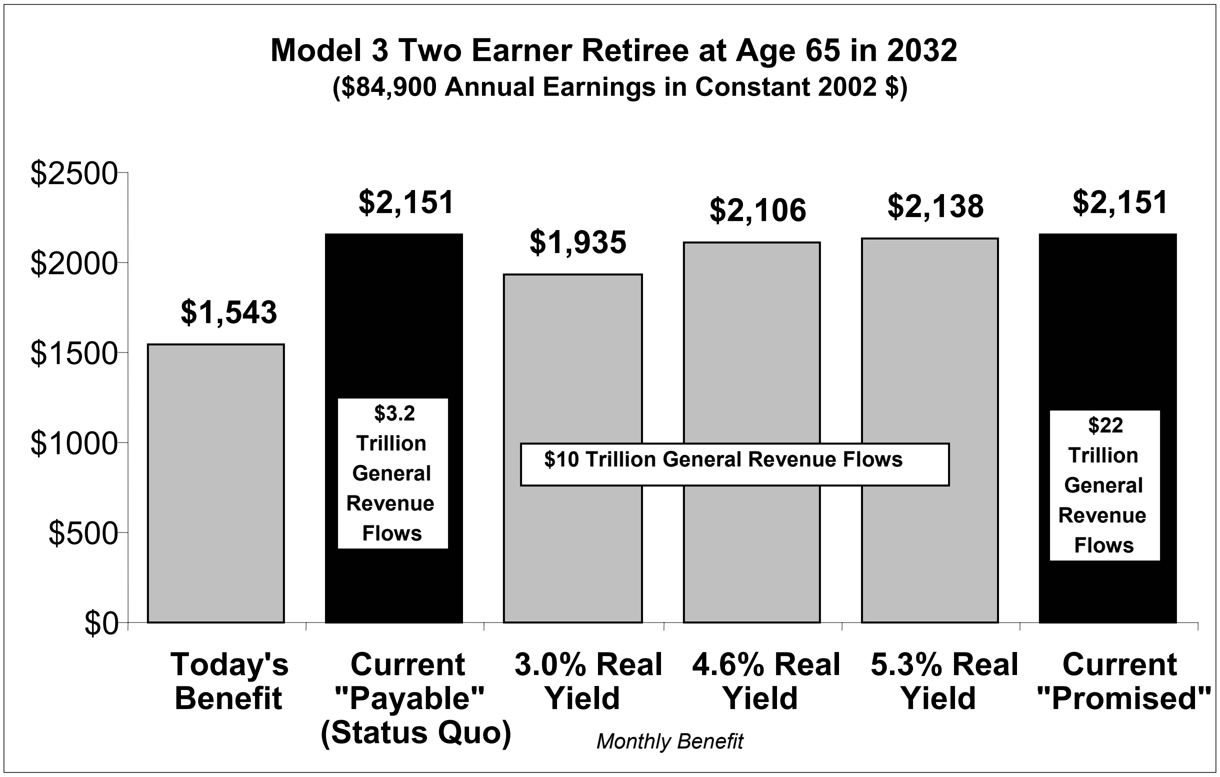

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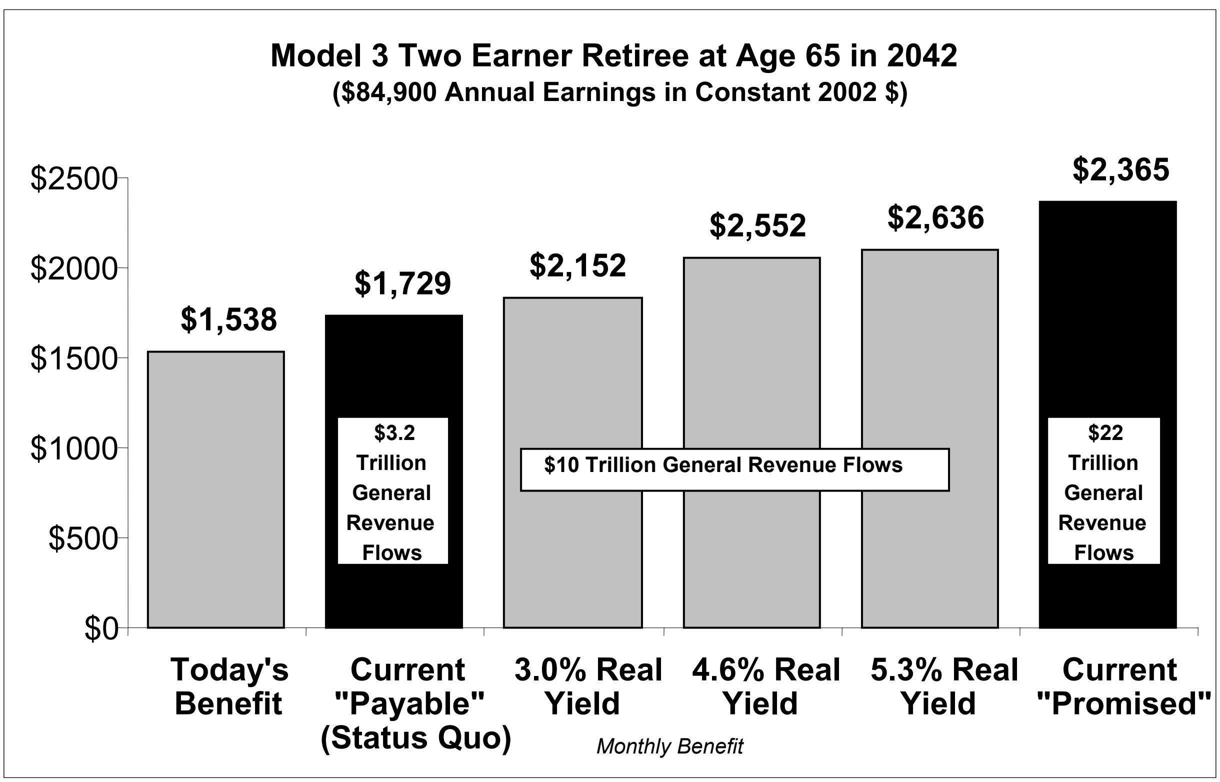

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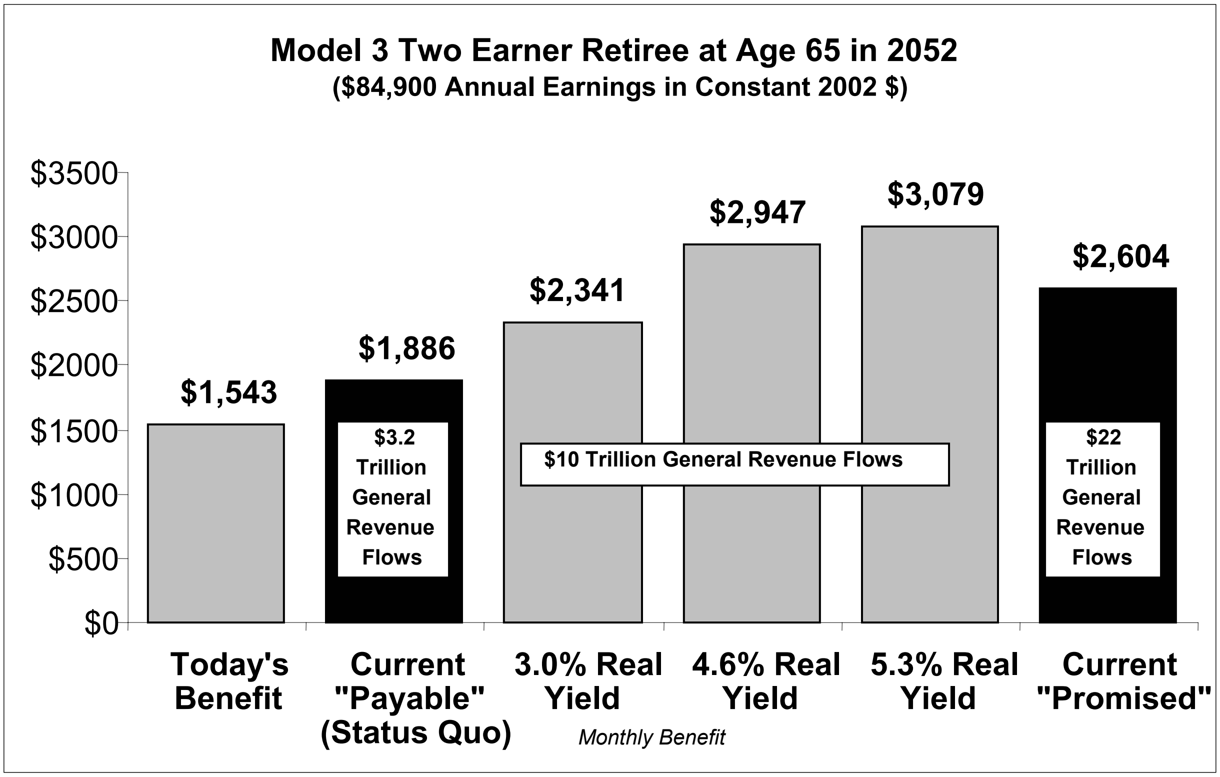

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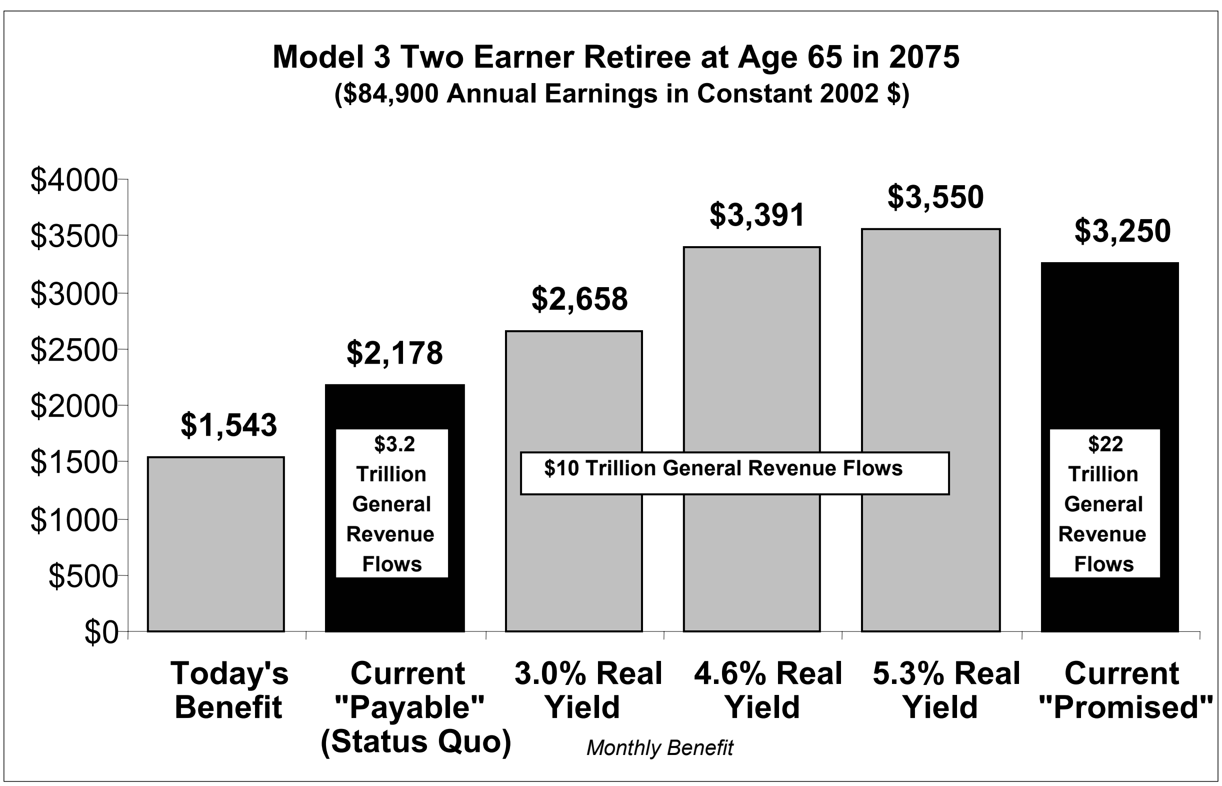

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