AMERICAN ACADEMY *of* ACTUARIES

August 15, 2011

Representative Sam Johnson
Chairman, Social Security Subcommittee
Committee on Ways and Means
U.S. House of Representatives
1101 Longworth House Office Building
Washington, D.C. 20515

Representative Xavier Becerra
Ranking Member, Social Security Subcommittee
Committee on Ways and Means
U.S. House of Representatives
1101 Longworth House Office Building
Washington, D.C. 20515

Re: July 8, 2011, Hearing on Social Security's Finances

Dear Chairman Johnson and Ranking Member Becerra:

Thank you for the opportunity to participate in the Social Security Subcommittee's July 8 hearing on Social Security's current and future benefit expenditures. I testified on behalf of the American Academy of Actuaries[1] as chair of its Public Interest Committee. The Academy is the nonpartisan professional association representing all actuaries in the United States. Our mission is to serve the public by providing independent and objective actuarial information, analysis, and education to help in the formation of sound public policy.

My testimony focused on increasing the Social Security retirement age, a change that the American Academy of Actuaries believes should be part of any comprehensive plan to address the system's long-term actuarial imbalance. Included in my written testimony were comments on ways to mitigate the effects of certain consequences of increasing the Social Security retirement age—including policies that would facilitate employment at older ages, such as reductions to the payroll tax.

During the question-and-answer phase of the hearing, Chairman Johnson inquired further about boosting older workers' incentives to work. This letter responds to that query in the context of long-range incentives. We are aware that, in the short term, higher employment levels among workers of all ages may be considered the more pressing national issue. Our comments also assume the maintenance of Social Security and Medicare disability benefits when continued work is difficult or impossible, which is more likely for older workers.

Retirement has become a highly individualized decision influenced by a myriad of factors and circumstances. There are, however, policy-based ways to provide incentives for older Americans to work longer. We comment on four general approaches:

- Social Security benefit levels

[1] The American Academy of Actuaries is a 17,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States

- Social Security tax levels
- Retirement policy and tax code provisions
- Other behavioral factors

Social Security benefit levels already increase—and thus provide incentives—for most people who continue to work beyond the minimum eligibility age. But the increases tend to be small for workers who don't have significant gaps in their earnings histories. To expand incentives for working longer, those increases could be enhanced for those who choose to stay longer in the workforce. Possible adjustment mechanisms include the PIA (Primary Insurance Amount) formula itself, early- or delayed-retirement adjustment factors, the timing and/or nature of indexing, or the benefit commencement age itself.

Social Security taxes could be adjusted downward or even eliminated for those opting to work beyond a certain age or longer than a specified number of years. For administrative simplicity, tax incentives probably should be handled through individual income-tax returns rather than employer withholding. Somewhat different issues need to be considered when evaluating changes to the employer share of the tax, rather than to the employee share.

Retirement policy in the US is heavily influenced by tax incentives. The tax code could be amended to more closely align features of corporate-sponsored retirement plans with longer working careers. Most importantly, the tax code could be amended to remove barriers to normal retirement at ages older than 65, remove mandatory commencement of qualified plan benefit payments at age 70.5, and remove barriers to benefit receipt during periods of phased retirement.

In addition to financial incentives, behavioral factors may influence work and retirement decisions, which can be effected by societal norms, peer behavior, and social signals. Research conducted by the Society of Actuaries as part of its forward-looking Retirement 20/20 initiative[2] points to the importance of "signals"—the parameters in law and custom that influence people's behaviors. Better alignment of retirement age features across Social Security, Medicare, and qualified retirement plans would signal to workers that they should plan to work longer and retire later.

The availability and cost of health insurance may also play a significant part in work and retirement decisions, for both employees and employers. Social Security provides for actuarial adjustments to benefit amounts before and after the normal retirement age, whereas Medicare has no adjustments around the age 65 start for the non-disabled.

The relative effectiveness of any particular incentive or disincentive is likely to depend on other important linkages, including:

- The traditional linkage between the earnings subject to Social Security payroll taxes and the earnings used to compute Social Security benefits;

[2] http://retirement2020.soa.org/

- The amount of Social Security income in relation to the household's availability of cash benefits from other, non-Social Security sources, such as employer-provided pensions, account-based plans, and personal savings;
- The advantages of particular changes versus the administrative practicalities and associated costs; and
- The linkage between the separate and somewhat independent decisions (1) to reduce or stop working and (2) to begin receiving Social Security retirement benefits. Workers can (and often do) work while receiving Social Security benefits or stop working without receiving benefits.

Such considerations involve economic and policy judgments, but the actuarial profession may be able to assist by testing and modeling various policy options to aid in understanding their likely financial implications.

The American Academy of Actuaries appreciates the opportunity to provide the subcommittee with these comments and would welcome the opportunity to assist in any further exploration of particular policy ideas. Please contact Jessica M. Thomas, the Academy's senior pension policy analyst (202-785-7868; thomas@actuary.org) if you have any questions or would like to discuss these items further.

Sincerely,

Thomas S. Terry, FSA, FCA, MAAA, EA
Chairperson, Public Interest Committee
American Academy of Actuaries