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AMERICAN ACADEMY *of* ACTUARIES

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**Statement of**  
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Chairperson, Public Interest Committee  
American Academy of Actuaries

**To the**  
**Committee on Ways and Means**  
**Subcommittee on Social Security**  
**U.S. House of Representatives**

**Hearing on**  
Social Security's current benefit expenditures, proposed changes to  
future benefits and the impact those changes would have on the  
program, future beneficiaries, workers, and the economy.

**July 8, 2011**

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.

Chairman Johnson, Ranking Member Becerra—and distinguished members of the subcommittee. Thank you for the opportunity to appear before you today to address Social Security's current and future benefit expenditures.

I appear before you today on behalf of the American Academy of Actuaries, where I currently serve as the chairperson of the Public Interest Committee. The Academy is the non-partisan 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.

*The time has come to increase the Social Security retirement age.*

It is in this spirit that the actuarial profession, through the American Academy of Actuaries, decided in 2008 on a course of action that had never been taken in its 45-year history—for the first time the Academy would advocate for a position. Actuaries, as you might know, do not have out-sized reputations for being risk-takers. Risk-evaluators, yes. Risk-takers, no. But, because of the long-range solvency challenges facing Social Security, and recognizing current and future demographic trends, actuaries believed it was necessary to strongly recommend for the expeditious consideration of an adjustment to the Social Security program to help put it on a path toward sustainable solvency. I'm referring specifically to increasing the Social Security retirement age, a subject that I will focus on in my remarks today.

For two decades, Social Security's trustees have been telling us—annually—that the system is not in actuarial balance. What does that mean? It means that at some point in the foreseeable future—2036 according to the most recent Trustees Report—absent corrective legislation, the program will be unable to pay benefits in full in a timely fashion. Adjusting the system today means that changes can be phased in slowly over many years. But ignoring the projections and deferring needed adjustments to the future will result only in more difficulty down the road. The adjustments necessary at a long-deferred date to bring the program to actuarial balance will require more immediate and more drastic measures, measures that will have a more severe impact on beneficiaries and the taxpaying public.

Over the years, actuaries have evaluated numerous proposals to prevent us from reaching a point where drastic action is necessary. Among the many options that would alleviate the imbalance, one became immediately obvious: increasing Social Security's retirement age. As life expectancy increases, and the number of working years remains relatively constant, the proportion of workers' lives spent in retirement continues to grow. This shifting balance between working years and retirement years has contributed to the system's long-term actuarial imbalance. As actuaries, we see this as a demographic problem that demands a demographic solution.

While we understand that an increase in retirement age could reduce overall lifetime benefits, we need to keep in mind the highly relevant relationship among retirement age, benefit growth, and retirement security. When the Social Security retirement age remains

fixed over time, increasing life expectancy means a de facto *automatic expansion* of benefits in terms of increasing *lifetime* benefits (and, of course, system costs). In other words, while people are retiring at ages that, even after the 1983 reform adjustments, are relatively close to the program’s original retirement age, their life expectancy, or longevity, has increased and continues to increase significantly. This means that retirees will be collecting Social Security benefits over a greater period of time than previous generations. Increasing the retirement age can contribute significantly to stemming this demographic trend and help put the program back on track toward actuarial balance.

In 1940, when Social Security began paying monthly retired-worker benefits, the normal retirement age was set at age 65. At that time, workers who survived to age 65 had a remaining life expectancy of 12.7 years for males and 14.7 years for females.

In 2010 life expectancy at age 65 was 18.6 years for males and 20.7 years<sup>1</sup> for females. In other words, since Social Security began paying monthly benefits, life expectancy at age 65 has increased by about six years for both males and females. In addition, Social Security’s Board of Trustees anticipates additional, significant improvements in life expectancy during the 75-year projection period. If the projections are borne out by actual experience, life expectancy at age 65 will have increased by about 10 years from 1940 to 2085. For more information, please view the table located in the appendix.

So, where are we today? The 1983 increases in the normal retirement age gave partial recognition to the improvements in life expectancy since 1940. These scheduled increases were part of a package of changes adopted to fend off near-term program insolvency. Under the 1983 adjustments, the normal retirement age has gradually increased to age 66 for workers born in 1943 (who will reach age 66 in 2009). The normal retirement age then remains at age 66 for 12 years, before gradually increasing to age 67 for workers born in or after 1960 (who will reach age 67 in 2027 and later). These increases are summarized in the table below.

<b>Year of Birth</b>	<b>Current Law Social Security Normal Retirement Age</b>
<b>1943—1954</b>	66
<b>1955</b>	66 and 2 months
<b>1956</b>	66 and 4 months
<b>1957</b>	66 and 6 months
<b>1958</b>	66 and 8 months
<b>1959</b>	66 and 10 months
<b>1960 &amp; older</b>	67

<sup>1</sup> 2011 *Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*  
[http://www.ssa.gov/oact/TR/2011/V\\_A\\_demo.html#221776](http://www.ssa.gov/oact/TR/2011/V_A_demo.html#221776)

From today's perspective, however, these 1983 scheduled increases in normal retirement age accounted for only two of the additional six years of life expectancy that we're experiencing today. Additional increases are needed to bring the retirement age in line with the expectations of the program when it was founded.

This is not to say that the 1983 amendments were fundamentally flawed in any way. To the contrary, those amendments, including the bump in normal retirement age from 65 to 67, represented a package of changes that accomplished the objective at that time. But that reform package in no way was designed to maintain a stable proportion of working years to retirement years in the long run, especially in the context of continuing improvements in life expectancy.

Before proceeding with a discussion of where to set future retirement age levels, let me make clear that although the Academy now advocates for inclusion of retirement age in efforts to restore Social Security's long-term actuarial balance, we do not advocate for any one proposal or approach. Nor do we intend for an increase in the retirement age to be seen as a solution that will address the entire imbalance in the system. It is but one component, though a necessary one, of restoring Social Security's long-term financial health.

Some approaches for increasing the Social Security normal retirement age include the following:

Increases to the normal retirement age—There are various ways to increase the retirement age. The Social Security Administration's Chief Actuary Steve Goss and his staff have developed eight examples, the most rapid—beginning the increase in the normal retirement age from age 66 to age 67 immediately, followed by increases by one month (in retirement age) every two years (in birth-date years) until the normal retirement age reaches age 70—reduces the long-range actuarial deficit by about a third. A rate of increase more rapid than one month every two years would be necessary to further reduce the long-range deficit.

Pay benefits for the same number of years—The normal retirement age could be indexed so that life expectancy at the normal retirement age remains constant over time. For example, life expectancy at age 65 (weighted between males and females and rounded to the nearest whole year) is now nearly 20 years. Based on expected increases in longevity from the Trustees Report, the normal retirement age would have to increase by about one month every year or two for life expectancy at normal retirement age to remain 20 years. This method would decrease system costs over time, because the payout period for benefits would remain the same while the period over which payroll taxes would be paid would increase. The savings from this change alone would not be sufficient to restore actuarial balance. But indexing the normal retirement age by one month every two years in combination with other changes to the system could restore actuarial balance. Another method of indexing that might make more sense than using a formula (i.e., one month every two years) would be to index retirement age based on demographic trends as they

develop since there is some disagreement among experts on the long-term rate of mortality improvement.

Keep the ratio of retirement years to working years the same—The normal retirement age also could be indexed so that the period from workforce entry age to the normal retirement age increases at the same rate as life expectancy at normal retirement age. This method, which was recommended in 1983 by a majority of the members of the National Commission on Social Security Reform, would increase the normal retirement age a little more slowly than maintaining a constant life expectancy at normal retirement age and, therefore, would reduce program costs to a lesser degree. But by using this method, policymakers may intend that some portion of the increase in life expectancy at normal retirement age may reflect years of unhealthy life during which workers could not continue working and that extra years of life expectancy should be split in some manner between work and retirement.

Adjust the normal retirement age to maintain actuarial balance—If Social Security were restored to actuarial balance by an ad hoc increase to the normal retirement age or by some other change or combination of changes, actuarial balance could be maintained by automatically adjusting the normal retirement age as necessary to achieve this goal. An adjustment of this nature also could be combined with automatic adjustments to the payroll-tax rate or benefit amounts to maintain actuarial balance. Automatic adjustments of this nature have been adopted by other developed countries for their national retirement systems. These issues are discussed in greater depth in the Academy's issue brief, *Automatic Adjustments to Maintain Social Security's Long-Range Actuarial Balance*.

Indexing the PIA formula for longevity—The Bipartisan Policy Center's Debt Reduction Task Force introduced a way to adjust benefits for longevity by decreasing the 90 percent, 32 percent and 15 percent factors used in calculating the primary insurance amount (PIA) as people live longer. The factors would be multiplied by the ratio of life expectancy of someone reaching age 67 in 2018 to the life expectancy of someone reaching age 67 in the fourth year before benefit eligibility. The task force's proposal also would apply to disabled workers at the time of conversion to disabled worker status, with the ratio only applying to the proportion of the benefit earned while not disabled.

Finally, it is important to remember there are ways to lessen the impact on working Americans and certain segments of the workforce who could be inequitably affected by any increase in the Social Security retirement age:

- Gradually phase in any change over an extended period of years, even decades, to accommodate the changes in retirement behavior that would be needed to make the policy successful—a longer phase-in period would allow for more time for society to adapt to the new work-life reality.
- Disparate distribution of longevity gains across the population—with wealthier socioeconomic groups recently showing more longevity improvements than

poorer socioeconomic groups—could be addressed by modifying the progressivity of the benefit formula in conjunction with retirement age changes.

- Difficulty in continuing to work in occupations that involve physical labor could be addressed by additional occupational bridge pensions, perhaps combined with revisions to existing disability programs.
- Greater difficulties that older workers sometimes face in finding jobs could be addressed by policies to facilitate employment at older ages (such as reductions to the payroll tax at older ages)

There will have to be considerable deliberation over the public policy considerations that go into a solvency reform package. In the end, proposals for solving Social Security's financial problems must be judged by how well they use the available revenues to fulfill the system's purpose—to provide a basic level of retirement income for all American workers.

*CPI – Part of the problem? Or Part of the solution?*

And now, I would like to spend the remainder of my time addressing another area that has been called into question because of concerns about overmeasuring or undermeasuring certain parts of the population in the economy. While controversy around issues pertaining to the consumer price index (CPI) methodology is not new, it of course becomes especially acute during economic downturns because of its relationship with the annual cost of living allowance (COLA) for Social Security. While the appropriate methodology resides in the field of economics, as an actuary I can provide some high-level observations as to how modifications to the automatic annual COLAs could affect the program.

There are currently several variations on what is commonly understood as the CPI that is applied to the COLA calculation, which has been dubbed CPI-W and reflects price increases for urban wage earners and clerical workers, about 32 percent of the population.

The alternatives include: CPI-E, consumer price index for elderly consumers, designed to reflect the different consumption patterns of consumers age 62 and older; CPI-U, which reflects the consumption pattern of all urban consumers, about 87 percent of the population; C-CPI-U, which is a second version of the CPI-U based on a “chain-weighted” formula that reflects changes in the distribution of consumer purchases among 211 broad categories (strata) of goods and services on a month by month basis; and what is called the Superlative CPI, which takes into account the tendency for consumers to substitute products whose prices have increased more slowly for those whose prices have increased more rapidly even among unrelated categories of goods and services.

To briefly sum up some key actuarial implications with these variations, my focus, of course is on the overall solvency impact.

Adjusting the CPI downward would improve the financial condition of the OASDI program.

For instance the current CPI-W has an historical average annual rate of 4.4 percent for the period 1969—2009. The Superlative CPI is projected to lower the annual increase in CPI by an estimated 0.3 percent. Generally, the rate of increase in the CPI-U has been very close to the increase in the CPI-W and for the future we do not expect any significant difference in the average annual increase based on difference in consumption of these two groups. Tracking of the chain-weighted version of CPI-U, C-CPI-U, has illustrated an increase of about 0.3 percentage point less than the CPI-U per year on average over the period it has been computed, and we expect this difference will continue into the future. Based on the data available for the CPI-E, it is estimated that over the long-term it will tend to increase at an average annual rate that is about 0.2 percentage point higher than for the broader indexes.

If Social Security benefits increased by 0.5 percent per year less than under the current program, the cumulative reduction would be about 5 percent after 10 years, and almost 10 percent after 20 years. This change would eliminate about 40 percent of Social Security's 75-year deficit according to a 2009 study done by the Social Security Office of the Chief Actuary<sup>2</sup>.

#### *Conclusion*

In closing, I again thank you for the opportunity to present some actuarial ideas to you today on these critical issues facing Social Security. There is no magic solution to the impending solvency challenges facing Social Security. And, certainly, no solution to adequately address the looming issue is going to be easy, simple, and without affecting beneficiaries, workers, or both. But by beginning this process sooner rather than later—when it is too late to employ measures aimed at mitigating those effects—we can ensure that the system lives on to provide the retirement safety net that it has provided for generations and for the generations to come. Thank you, and I would be happy to answer any questions you might have at the appropriate time.

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<sup>2</sup> [http://www.actuary.org/pdf/socialsecurity/Social\\_Security\\_Reform\\_Issue\\_Brief\\_6-15-10.pdf](http://www.actuary.org/pdf/socialsecurity/Social_Security_Reform_Issue_Brief_6-15-10.pdf)

Appendix

<b>Year (age 65)</b>	<b>Male</b>	<b>Female</b>
1940	12.7	14.7
1950	13.1	16.2
1960	13.2	17.4
1970	13.8	18.5
1980	14.7	18.8
1990	16.0	19.3
2000	17.5	20.0
2010	18.6	20.7
2035	20.3	22.3
2060	21.7	23.6
2085	22.9	24.8

Source: 2011 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds  
[http://www.ssa.gov/oact/TR/2011/V\\_A\\_demo.html#221776](http://www.ssa.gov/oact/TR/2011/V_A_demo.html#221776)