

Social Security 101



KATHLEEN ROMIG
SOCIAL SECURITY ADMINISTRATION

Why Social Security?



**WHAT ARE ITS GOALS?
WHY SOCIAL INSURANCE?**

Goals of Social Security



- **Equity**

- What you get out is based on what you put in
- Mandatory saving protects both the short-sighted people who won't save *and* those who would be forced to bail them out

- **Adequacy**

- Insures against disability and premature death
- Supplements incomes of those who wouldn't have a decent standard of living, even if they did save

Social Insurance vs. Welfare



Social Insurance	Welfare
Qualify based on contributions	Qualify based on need
Benefit amounts based on earnings	Benefit amounts means-tested
Supplements workers' savings	Discourages savings
Replaces lost wages	Provides a floor of income/benefits
Near-universal participation	Limited participation
Funded through payroll tax	Funded through general revenues
Pools of risks & resources among all	Richer people assisting poorer people
Poverty prevention	Poverty alleviation

Social Security Taxes

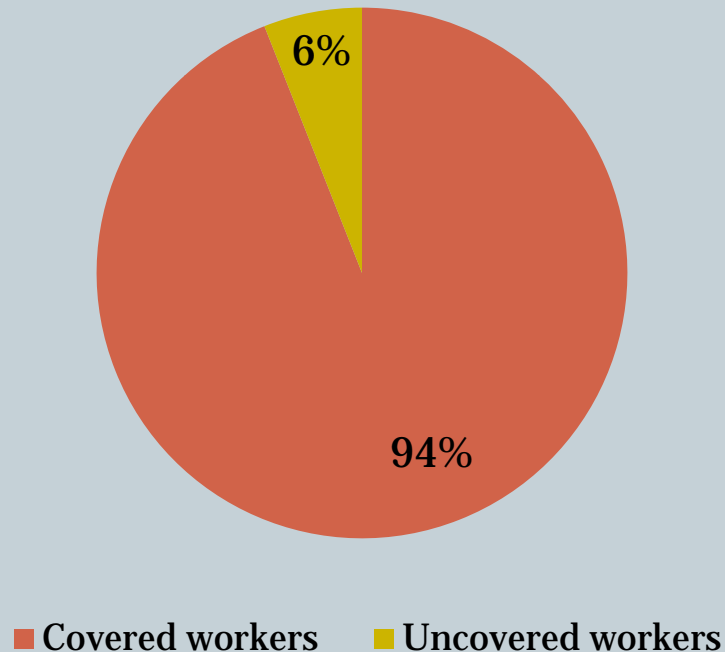


**WHO PAYS?
HOW MUCH?
WHY PAYROLL TAXES?
WHY HAVE A CAP?**

Who is Covered by Social Security?



- About **19 in 20 workers** (165 million people)
 - This includes all Members of Congress—so tell your uncle!



Source: SSA, <http://www.ssa.gov/oact/FACTS/index.html>

Note: As of December 2013

How Much Do We Pay?



- **Payroll tax rate:**
 - Employers & employees each contribute **6.2%** of covered earnings
- **Payroll tax cap:**
 - **\$117,000** in earnings for 2014

Why Payroll Taxes?



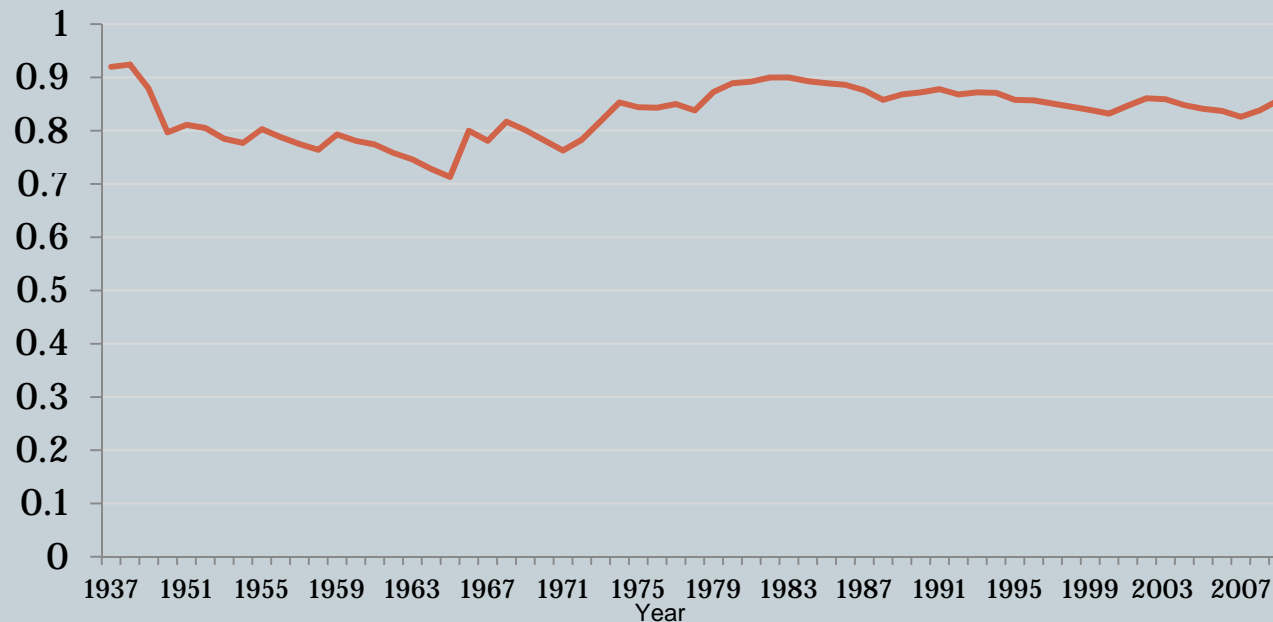
- *“We put those payroll contributions there so as to give the contributors a legal, moral, and political right to collect their pensions and their unemployment benefits. With those taxes in there, no damn politician can ever scrap my social security program”*

○ *Franklin Delano Roosevelt, 1941*

The Tax Max Over Time



- The percentage of covered earnings subject to payroll taxes has varied over time
 - Set at 90% of covered earnings in the 1983 reforms
 - In 2008, about 83% of covered earnings were taxed



SOURCE: Whitman (2011).

Social Security Benefits



THE BASIC FORMULA
BALANCING EQUITY & ADEQUACY
COLAS & OTHER ADJUSTMENTS
FAMILY BENEFITS
FULL RETIREMENT AGE
NOT-SO-SPECIAL MINIMUM

The Basic Benefit Formula (2014)

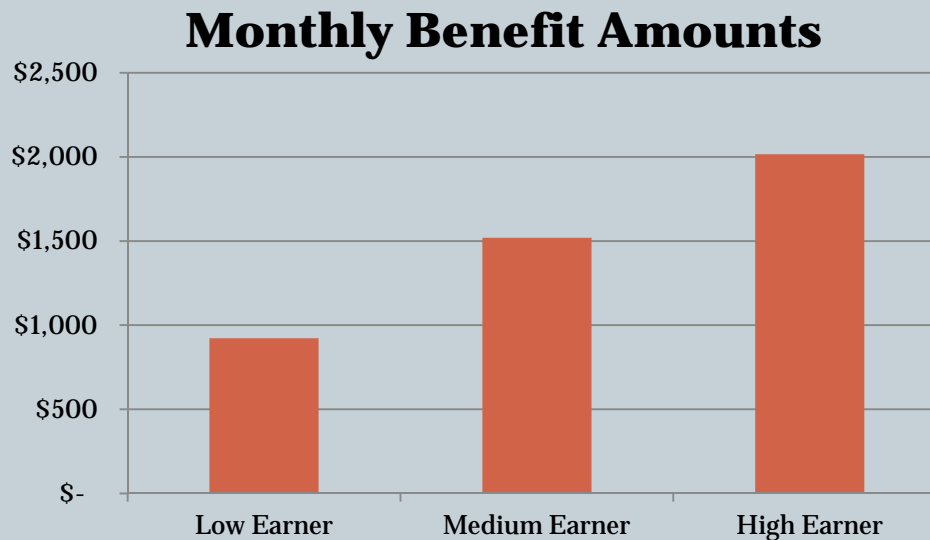


- **Calculate the worker's average indexed monthly earnings (AIME):**
 - Indexed to wages at age 60
 - Average of the highest 35 years of earnings
- **Calculate the basic benefit amount (or primary insurance amount, PIA):**
 - 90% of the first \$816 of AIME, plus
 - 32% of AIME over \$816 up to \$4,917, plus
 - 15% of AIME over \$4,917 (up to the tax max)

Balancing Equity & Adequacy



- **Higher earners have greater monthly benefits** than lower earners, since benefits are based on earnings



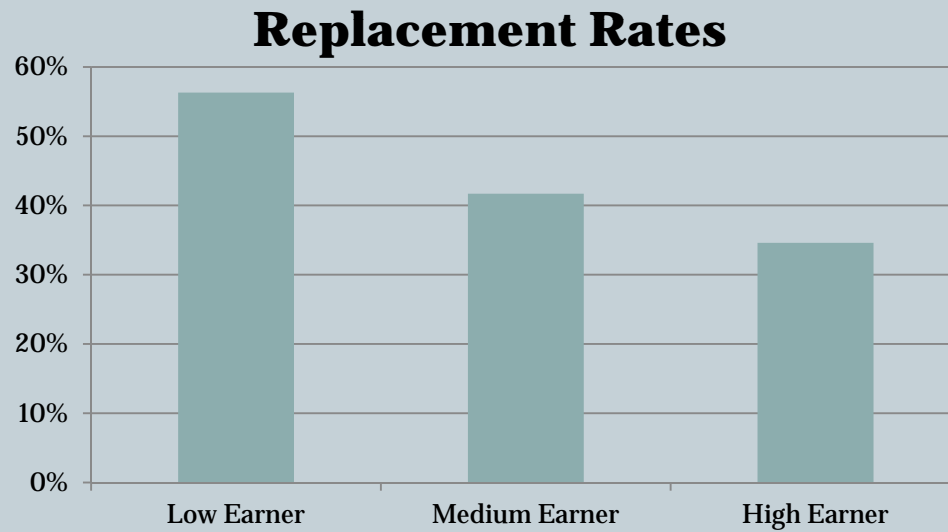
Note: Hypothetical scaled earners who turn 65 and retire in 2013

Source: 2013 Social Security Trustees Report, intermediate assumptions

Balancing Equity & Adequacy



- **Lower earners have higher replacement rates** than higher earners, since the benefit formula is progressive



Note: Hypothetical scaled earners who turn 65 and retire in 2013

Source: 2013 Social Security Trustees Report, intermediate assumptions

COLAs & Other Adjustments



- Initial benefits are indexed to **wages** (AWI), which:
 - Allows beneficiaries to reap the benefits of rising living standards;
 - Provides a steady replacement rate to new beneficiaries;
 - Recognizes that workers' Social Security payroll tax payments increase as their wages rise.
- After the first year, benefits rise with **inflation** (CPI-W), which:
 - Allows benefits to maintain purchasing power over time;
 - This is called the COLA (cost-of-living adjustment)

Family Benefits



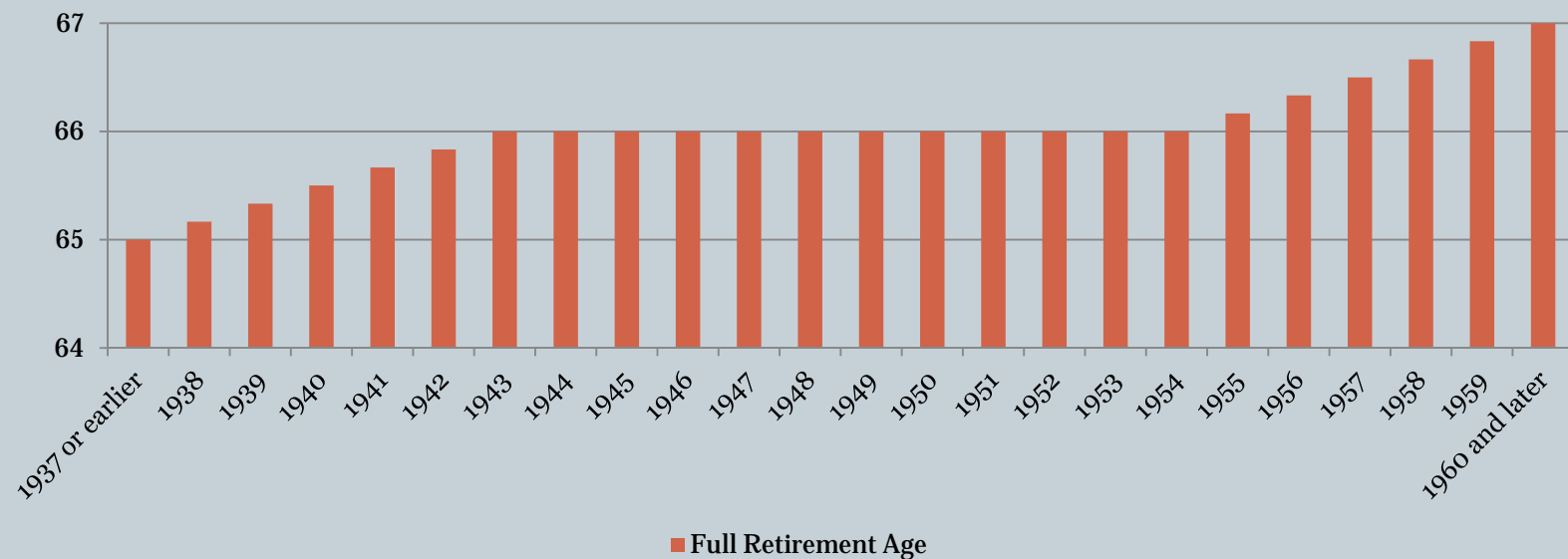
Family Relationship	Max % of Worker's Basic Benefit
Spouse of retired/disabled worker	50%
Surviving spouse (with child in care)	75%
Surviving spouse (aged)	100%
Child of retired/disabled worker	50%
Surviving child	75%

Note: Benefits may not be payable or may be reduced for: dual entitlement (i.e., earning a higher worker benefit of one's own), earnings, age, family maximum rules

The Rising Full Retirement Age



- The **full retirement age (FRA)** is the age at which a person can receive unreduced retirement benefits
- Increases to the FRA reduce benefits for *all* retired workers, regardless of the age they retire

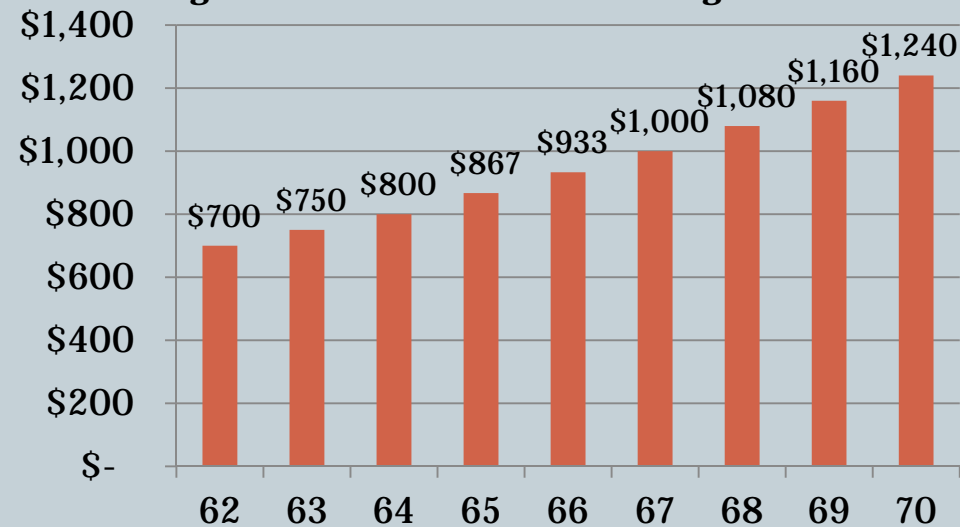


Sliding Scale Benefits



- **How much you get depends on when you retire**
 - Early retirement = permanent benefit reduction, up to 30%
 - Delayed retirement = permanent benefit credit, up to 24%

Monthly Benefit Amounts Differ Based on the Age You Decide to Start Receiving Benefits



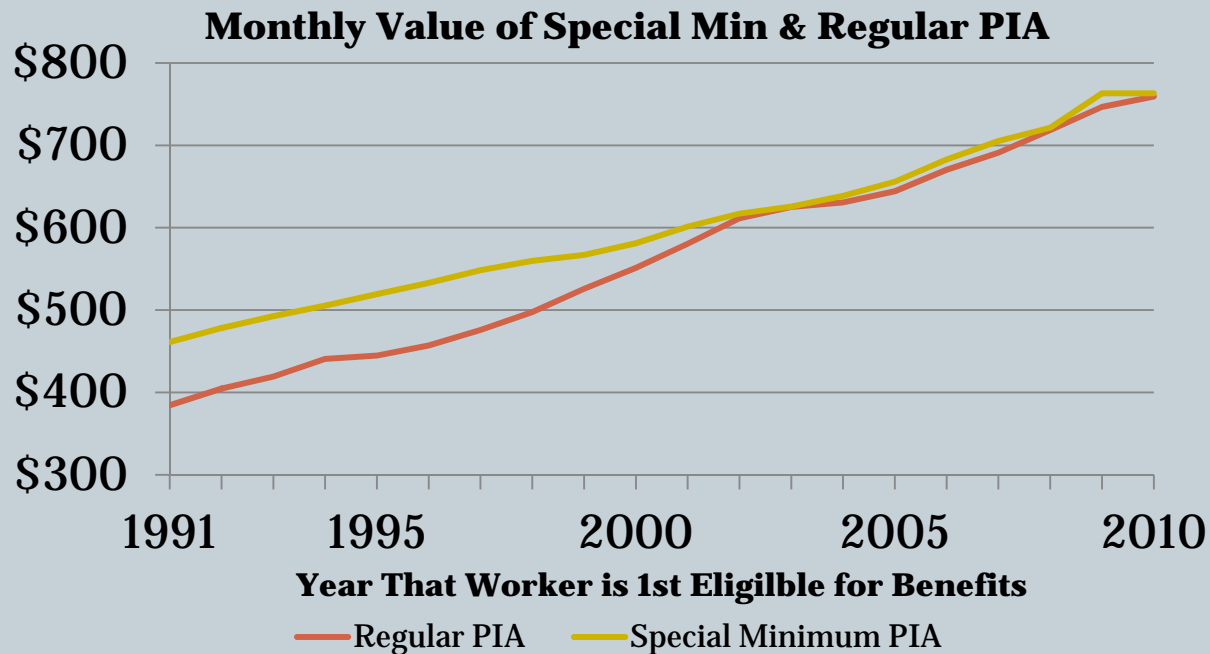
Note: Illustration assumes benefit of \$1,000 at full retirement age of 67 (i.e., born in 1960 or later).

Source: Social Security Administration

The No-Longer-So-Special Minimum Benefit



- **Social Security's special minimum benefit:**
 - Enacted in 1972 to boost benefits for long-term low earners and indexed to inflation (not wages)
 - Since 1998, no new beneficiaries have received it



Good Luck!

