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Key Legislative Developments Affecting Your Human Resources

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2016 Save Our Social Security Act

While Congress remains on recess and all is quiet on the Hill, we circle back to take a closer look at recently introduced legislation aimed at addressing looming Social Security shortages.

The Social Security Problem

Annual reports from the trustees of the Social Security Administration (SSA) have warned of having to cut back benefits to the level supportable by incoming contributions two decades from now if nothing is done to rebalance the system. As with any balance sheet, there are a number of ways to mathematically rebalance the system: either increase inflows or decrease outflows. Options that have been suggested for increasing inflows include:

- Directly raising the social security payroll tax (FICA and SECA)
- Raising the compensation base for applying the tax rate
- Collecting more income taxes on benefits as they are paid
- Expanding the types of compensation subject to tax (such as health premiums)
- Increasing trust fund investment returns

Options that have been suggested for decreasing outflows include:

- Raising the full retirement age
- Reducing cost-of-living adjustments (COLAs)
- Reducing benefits for high-income retirees
- Generally reducing the level of benefits for current and/or future retirees

The 2016 OASDI Trustees Report estimates that, based on its intermediate assumptions, either a 2.58% increase in the payroll tax rate or a 16% reduction in all benefits for current and future beneficiaries would allow the program trust funds to remain solvent throughout the 75-year projection period.

Can You Fix the Problem?

Online resources allow the public to test possible approaches to fixing the Social Security problem. The American Academy of Actuaries offers **The Social Security Game** where multiple choice selections allow players to see the effects of variations on approaches to benefit cuts or payroll and income tax increases. A second interactive tool is offered by the Committee for a Responsible Federal Budget, whose **"The Reformer"** charts the changes to revenue and spending as the user selects from various benefit modifications and payroll tax rate changes.

S.O.S. – Save Our Social Security

Over recent history, many proposals have been advanced to solve the solvency problem — or nibble at the edges. The SSA offers a list of proposals and the cost estimates they have prepared for analyzing each one.

The most recent of these is bipartisan legislation introduced by Rep. Reid Ribble (R-WI) together with six co-sponsors. Known as the S.O.S. Act of 2016, H.R 5747 would take the following steps to increase inputs and decrease outputs:

- S.O.S. would increase the maximum wage base subject to Social Security taxes over the next five years, so that by 2021 it would be $308,750, more than 2½ times the current maximum of $118,500. After 2021, increases would be determined by the SSA taking into account 90% of the total earnings of all workers (compared with 84% currently).
- S.O.S. would gradually increase the full retirement age from age 67 to 69, starting in 2022 and ending in 2034, with further increases thereafter to keep up with mortality improvement. The maximum age at which deferred retirement credits are provided would also gradually increase from age 70 to age 72 over that time period. However, early retirement would remain at age 62.
- Although the bill would call for counting all pay up to the wage base in determining benefits, it would provide a smaller percentage of benefits on higher wages by gradually reducing the current factor of 15% of average indexed monthly earnings (AIME) over $5,157 ($61,884 annual) down to 5%. Based on the current maximum AIME of $8,782 at age 65, this would eventually produce a maximum monthly benefit that is $362 smaller per month, ignoring any other changes. In addition, a multiplier of just 2.5% would apply for the portion of the AIME between $9,875 ($118,500 annually) and the new higher covered earnings figures.
- The bill would change the methodology for calculating the cost of living adjustment increases to "chained CPI" (that is, from CPI-W to C-CPI-U), which would likely result in smaller annual COLA increases. Chained CPI accounts for how people switch their purchases as relative prices change. BLS explains chained CPI in FAQs.
- And it would nudge the benefit level lower by using 38 years of work instead of 35 years in calculating average wages used to determine benefits.

Corresponding Changes for Qualified Plans?

Many retirement plans coordinate benefit levels with Social Security through the "permitted disparity" provisions in their plans. Changes to Social Security benefits in the proposal should arguably trigger changes in the rules for qualified plans. For example, after the proposed change to the taxable wage base is fully phased in, defined contribution plans that are integrated with Social Security would allocate very little (if anything) on pay in excess of the base in light of the maximum compensation limit (currently $265,000). A similar, though delayed, effect will occur with defined benefit plans through the covered compensation calculation, for example. Would offering a plan that is integrated with social security still make sense?

Would the further increases in Social Security Normal Retirement Age lead to an increase in the latest allowable Normal Retirement Age under ERISA minimum vesting rules (which now generally require full vesting at age 65)? Would an increase in the maximum age at which Social Security provides delayed retirement credits to age 72 lead to modernization of the age 70½ required beginning date under the minimum distribution rules?

Other changes in S.O.S. would increase benefits. These proposals include:

- A minimum benefit at 125% of the federal poverty threshold for a family of one, phased in based on eligible working years (with the full minimum in effect after 40 years of coverage)
- A bump up in benefits for individuals who receive OASDI benefits for 20 years or more

A summary of the bill is on Rep. Ribble's website. The SSA's Office of the Chief Actuary's estimates of the financial effects of the bill on Social Security are available here.

Comment: Although it is unlikely that this bill will survive in its current form with election year politics and a new administration coming in 2017, it is interesting in that it shows the most palatable fix will likely involve many elements and there is no single magic pill for bridging the gap.

There is no limit on the amount of wages subject to the Medicare tax.

Looking Ahead

Congress continues on recess until after Labor Day. With the November elections looming for 34 Senate and all 435 House seats, congressmen are increasingly focused on re-election campaigns and maintaining (in the case of Republicans) or gaining (in the case of Democrats) control of one or both chambers. So for now, little real action is anticipated.

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