



SOCIETY OF ACTUARIES

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## ACTUARIES AND SOCIAL SECURITY

by K. Arne Eide

"Social Security: Perspectives for Reform" contains much that should be of interest to the actuary. However, one cannot obtain a clear understanding of the book by merely reading the authors' statements of objectives as cited in the review in the *Transactions*, by reading the review itself or the authors' letter to *The Actuary*. If one cannot find time to read the entire book, a reasonably accurate picture may be obtained through reading the summary at the end of each chapter.

There are many facets of the Pechman, Aaron and Taussig book that might provoke discussion. In commenting on some points that have arisen in the reviews and the authors' letter, I do so with the reservation that my few remarks can by no means cover all the basic issues. What might be written to *The Actuary* simply is not comprehensive enough to illumine to great depth a subject as complex as Social Security.

The authors, along with a growing number of others interested in the broad field of public welfare, express dissatisfaction with present welfare programs. Social assistance programs have grown over the years both in scope and magnitude of outlay without seemingly achieving desired objectives. Recently advocated programs encompassed by the Administration's proposal for welfare reform and the report of the Heineman Committee would attempt to provide benefits to those in poverty or near poverty levels, whether working or not working, in an attempt to raise their income and standard of living. Social Security (OASDI primarily) would, as heretofore, continue to provide basic economic support for most workers,

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## THE RETIREMENT TEST UNDER SOCIAL SECURITY

by Harry E. Blagden

When the Social Security Act was first passed in 1935, it was during a depression and the psychology engendered thereby led to the provision that earning as little as \$15 in covered employment in any calendar month disqualified an otherwise eligible recipient from receipt of Social Security old age benefits.

There is, of course, a need for some kind of retirement test because there seems little sense in paying *tax free* Social Security benefits to a person working full time after age 65 and earning as much as \$50,000 a year.

Unfortunately, the philosophy which led to the kind of retirement test initially provided has, with some modifications, persisted, with significant changes in amounts involved and with the desirable change that earnings in any employment (not only covered employment) are taken into account.

Currently one can earn as much as \$1,680 in a calendar year with no loss of benefits. For each dollar of the next \$1,200 in excess of \$1,680, fifty cents is lost in Social Security benefits. For each dollar earned (and subject to tax) in excess of \$2,880 a dollar of tax free Social Security benefits is lost.

There is, however, an important exception to this — a loophole. An employee can earn as much as \$140 in any calendar month without losing Social Security benefits for that month regardless of how much he earned in the calendar year in which such calendar month occurs. Furthermore, if a self-employed person can demonstrate successfully that for any calendar month he does not "render substantial services," he is entitled to receive Social Security benefits for such calendar month re-

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## FURTHER COMMENTS ON SOCIAL SECURITY

by Robert J. Myers

The December 1969 issue of *The Actuary* carries comments by Pechman, Aaron, and Taussig on the review of their Brookings Institution report "Social Security: Perspectives for Reform" made by Ray Peterson and me. I should like to make a rebuttal of some new points raised by the authors. I believe that the detailed comments that I made in my *TSA* review are still pertinent and accurate and have not been answered by the authors.

I disagree most thoroughly with the authors' contention that "the widespread habit of regarding social security as a form of insurance is misleading and harmful." The difficulty on the part of the authors is that they equate "insurance" only with individual insurance and that they do not have knowledge of the differences in concept and approach of group insurance and group pension plans as against individual insurance. In fact, I believe that it is fair to say that group insurance and pensions have more in common with OASDI (social insurance) than they do with individual insurance. The authors apparently never studied the financing principles of private pension plans.

I am convinced that the American public approves the insurance concept in the Social Security program and that this viewpoint is beneficial for the program and the nation. People want to feel that they and their employers are providing that part of their economic security which comes through this channel and that the Government has only the function of setting up the administrative machinery necessary therefor. People do not want a basis for the Social Security program that implies

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## Comments by Myers

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that the Government is taking care of them—as is the approach in the Soviet Union and as the authors seem to propose.

The authors repeat their simple example, which is obvious without algebraic trappings, that if the rate of population growth and increase in earnings exceeds the interest rate, then the chain-letter situation of all generations getting more than their money's worth is present. The trouble is with the assumptions, not the mathematics. Population growth will not always be positive (i.e., increasing) and may well be negative at times and close to zero over the long run. Interest rates should generally exceed rates of increase in earnings. In fact, it is possible that, in some economically mature society, earnings rates may be level, and prices will be the variable (i.e., moving downward as productivity rises). In any event, I repeat, over the long run, everybody cannot get more than their money's worth from a social insurance plan!

My criticism of the authors' analysis of individual equity under OASDI should not have puzzled them. Calculations of this type are difficult, if not impossible, to make on a fair, equitable basis, taking into account all the variables under the complex OASDI system. I merely stated that I adversely criticize such attempts which "show" that all participants get a "bargain," just as I do those attempts which "show" that none "get their money's worth." The choice of assumptions and methodology can "prove" almost anything! The truth

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least concerned with its course and ultimate role. The private sector has a tremendous stake in the provision of income security and through its investments also makes a most important contribution to capital formation so greatly needed for future expansion of productive capacity. This in itself should provide sufficient reason for showing more than a cursory interest in Social Security.

of the situation lies between the two extremes.

I criticized the authors for a lack of understanding of the cost estimates on the grounds of several specific points. One of these they deny—namely, the cost effect of a change in the interest-rate assumption—on the grounds that the data which I quote were published after they went to press. Specifically, they cite the 1968 OASDI Trustees Report, whereas they used the 1964 report as their source. Actually, the 1967 report (House Document No. 65, 90th Congress, page 42), which was published in February 1967, gave data indicating that a 1/2% increase in the interest rate "finances" only a 1% benefit increase.

The authors state that, when benefits are increased, the contribution rate and/or the earnings base are increased to maintain "actuarial balance" and that this is bad because it generates future surpluses, which start the cycle all over again. They continue to fail to realize the nature of the cost estimates and the underlying earnings assumptions. The use of level-earnings assumptions merely generates an actuarial surplus *after* earnings rise, and this can then be used to update the benefit structure (for both existing beneficiaries and active workers). The authors' statement is wrong in the light of history; benefit increases have not always been accompanied by changes in the financing provisions (note the 1969 amendments increasing benefits by 15%), while in other cases the benefit increase was financed by the available actuarial surplus and the "gain" from the desirable updating of the earnings base.

The authors apparently do not realize that the *ad hoc* method of increasing benefits in the past and the automatic-adjustment method proposed by President Nixon have the effect not only of increasing current benefits, but also of updating the average wage used for benefit purposes for active workers. Thus, one of the authors' criticisms—that benefits should be related to recent earnings—has already been answered in practice.

The most important flaw in OASDI, according to the authors, is the low level

of the minimum benefit, which is so much below the so-called poverty line. The authors fail to realize that a significant portion of those getting minimum benefits are not primary workers, dependent on their covered earnings or their benefits for their living. Instead, this group includes government workers receiving substantial other pensions, women who worked only part time and are dependent economically on their husbands, etc. As a matter of fact, a low-earnings, full-time worker almost always qualifies for far more than the minimum benefit.

## Concept of Poverty

In passing, I cannot avoid criticizing the concept of poverty, which the authors and many others nowadays use as though it were sacred and unquestionable. The main criticisms are that the base figures were, in fact, picked out of the air and are not the results of studies of what poverty really is and that, in measuring against the poverty line, no account is taken of the availability of assets and services furnished by others as offsets against "needed income." For example, home ownership and furnishing of room and board by relatives is completely ignored.

Finally, the authors renew their proposal that the payroll taxes paid by low-income workers and their employers should be refunded to such workers. I cannot see why social insurance contributions should be singled out for this special treatment. Why should not sales taxes, gasoline taxes, or other taxes be similarly treated? Or why should not low-income persons be refunded, out of the general treasury, part of the cost of the food, appliances, automobiles, life insurance, etc., that they purchase? If it is desired to give more income to this category, let it be done directly and forthrightly—and not by little subsidies hidden here and there. I insist that the "purchase" of social insurance should be considered in the same manner as any other purchase and, much more importantly, that this is how the average person considers the matter—and wants to consider it.