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EDITORIAL

Costly delay

by Marc Twinney

An intriguing development about the reform plans for Social Security financing proposed by the Advisory Council is the ease with which a consensus seems to develop in public meetings on the topic. Once people hear the explanation of the benefit payment's projected growth to 19% of payroll and the three reform plans, those attending easily find agreement. The majority coalesce around a version of reform known as the individual account plan.

The individual account plan is a compromise of the opposing views about reform. It offers a middle ground. The pay-as-you-go (PAYGO) part of the plan lives within the current law's 12.4% tax rate. It gradually slows the growth in the initial benefits to new retirees and provides a decent and adequate defined-benefit floor. The funded part adds small individual savings accounts for new contributions (1.6% of payroll) so that combined benefits from both parts do not decrease from current law. The 1.6% compares with the increase of 2.4 percentage points needed to continue indefinitely the benefits in current law. The 75-year period for actuarial balance requires 2.2 more points in tax. Either expression masks the true long-term financing problem, which climbs to a differential of more than six percentage points between benefits and taxes (as a percent of payroll).

The individual accounts would be held for the contributor by Social Security, but the contributor would choose from bond and stock index funds. With a typical asset mix, these accounts would have the potential to earn up to four-and-a-half times the 1% real rate of return that contributions are projected to return in a PAYGO benefit. The accounts would receive 11% of the contributions but provide 30% of the aggregate benefits when the new program matures in 35 years.

The idea of keeping the defined benefit on the basis of the best that 12.4% will buy and putting new money into the more efficient, personal form appeals to retired people receiving benefits as well as to working contributors. The total contribution rate of 14% is sustainable indefinitely; this speaks to those concerned about the burden on future generations and keeping promises.

So why do some people in Washington and elsewhere want to take more time before making any changes? Indecision is expensive here. There was talk of appointing a bipartisan commission to determine a more accurate CPI. This would help balance the federal budget as well as protect full COLA benefits, because an accurate CPI would end the pressure for some arbitrary adjustment to COLA. Alternatively, a commission on OASDI reform could be appointed to choose one reform plan and lessen partisanship. This eats up time, however, and time is valuable. It's the one free ingredient in lowering the cost of solving the long-term financing problem.

Social Security financing is a classic actuarial problem. The context is different than we find in most of our daily work, but the size of "n" is outstanding, making the actuarial projections quite credible. I hope you will take time to study Social Security financing and communicate your understanding to others. I can think of no better way the profession can serve the nation than by helping everyone understand the problem and what can be done to solve it.

The SOA Foundation's brochure "On the edge of change" is an excellent start. Call Kelly Mayo to obtain a copy (847/706-3509).