American Academy of Actuaries

Issue Brief

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Helping the 'Old-Old'—

Possible Changes to Social Security to Address the Concerns of Older Americans

The objective of this issue brief is to explore possible design changes to Social Security that address financial security issues faced by a growing part of our population that may attain advanced ages and lack adequate resources.

Background and Identification of the Issue

Life spans of retirees have been increasing for the past few decades. The combination of declining birthrates and increasing life expectancy has resulted in the older segments of the population of the United States to increase both in absolute numbers and as a percentage of the entire population. This trend is most pronounced at the highest ages, as illustrated in Table 1. In 2050, the percentage of the population age 85 and over is projected to approach the percentage of the population age 65 and over in 1930 (which was the year of the last decennial census before the inception of Social Security).

Table 1: United States Population Aged 65 and Over by Age: 1930 to 2050
(Numbers in thousands)

Year	Total Population	65 and over		65 to 74		75 to 84		85 and over	
		Number	Percent	Number	Percent	Number	Percent	Number	Percent
CENSUS DATA									
1930	122,775	6,634	5.4	4,721	3.8	1,641	1.3	272	0.2
1940	131,669	9,019	6.8	6,376	4.8	2,278	1.7	365	0.3
1950	150,697	12,270	8.1	8,415	5.6	3,278	2.2	577	0.4
1960	179,323	16,560	9.2	10,997	6.1	4,633	2.6	929	0.5
1970	203,212	20,066	9.9	12,435	6.1	6,119	3.0	1,511	0.7
1980	226,546	25,549	11.3	15,581	6.9	7,729	3.4	2,240	1.0
1990	248,710	31,242	12.6	18,107	7.3	10,055	4.0	3,080	1.2
2000	281,422	34,992	12.4	18,391	6.5	12,361	4.4	4,240	1.5
2010	308,746	40,268	13.0	21,713	7.0	13,061	4.2	5,493	1.8
PROJECTION									
2020	333,896	55,969	16.8	32,796	9.8	16,480	4.9	6,693	2.0
2030	358,471	72,774	20.3	38,593	10.8	25,236	7.0	8,946	2.5
2040	380,016	79,719	21.0	35,465	9.3	30,140	7.9	14,115	3.7
2050	399,803	83,739	20.9	37,554	9.4	28,206	7.1	17,978	4.5

Source: United States Census Bureau, Current Population Reports, *65+ in the United States: 2010* by Loraine A West, Samantha Cole, Daniel Goodkind and Wan He, 2014.

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Greater longevity is obviously a positive development, but it does entail challenges. Among them is the financial security of people we will refer to as the "old-old": those who survive beyond actuarially anticipated life expectancy. It is possible but by no means a certainty that a significant segment of the population could be subjected to financial hardship in old age. How many old-old citizens will be faced with hardship due to diminished financial resources in the future is not possible to predict with any certainty. It is possible that longevity improvements could cease or that retirement savings will last longer than expected due to effective financial management and beneficial financial market performance. Whether this should be left to chance or whether programs should be initiated to address this likely (though not certain) problem should be explored.

Potential Causes of the Financial Challenges Among the Old-Old

Several factors have led to the financial challenges being addressed in this issue brief. First, more people might outlive their resources such that more old-old rely exclusively on Social Security. The decline in the availability of traditional defined benefit plans could make this even more likely in the future. Second, people may have inadequate inflation protection in retirement. Social Security provides inflation protection (cost-of-living adjustments are made to benefits annually based on the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W)), but even most traditional defined benefit plans do not adjust benefits as prices increase. Some retirees may be faced with a significant change in financial circumstances upon the death of a spouse. Finally, medical expenses or other care costs may deplete the resources available, and affect the ability of retirees to make the effectiveness of Social Security benefits meet their other basic living needs.

The current Social Security Old Age and Survivors Insurance Program does have features that help to mitigate some of the financial challenges of the old-old. Since its inception, the purpose of Social Security has been to provide financial support to individuals after their working years, when they are financially most vulnerable. However, unlike social safety net programs, Social Security does not base benefit eligibility on a specific demonstration of financial need, such as income and/or assets below a certain threshold. Rather, Social Security benefits are based on a participant's membership in one or more groups within the general population. Originally, benefits were payable only to workers age 65 and over who had left the labor force, *i.e.*, retired. Later, benefits were extended to the surviving spouses and other dependents of deceased workers and to disabled workers under age 65. Since 1971, benefits have been indexed to inflation, recognizing that, as life expectancy increases, Social Security beneficiaries have become more vulnerable to reduction in the buying power of their benefits due to inflation. However, for many old-old these features may not be sufficient to avoid financial hardship in advanced old

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age. This issue brief examines some possible enhancements or modifications to Social Security designed to alleviate potential financial insecurity of the old-old.

Concerns

When examining any proposed changes to Social Security, one should be sensitive to two very important aspects of the program. First is the issue of the *sustainable solvency* of the program. Sustainable solvency means that the program is not expected to run out of funds at any time in the projection period (75 years) and that the program assets at the end of the period are stable or increasing. The Social Security system does not currently meet this criteria. According to the 2016 Trustees Report, expected future income to the system combined with the current trust fund balance will cover only 83.3 percent of expected benefit payments and administrative expenses on a present value basis over the 75-year valuation period. Years beyond the valuation period are expected to add to this deficit. Unless legislative changes are made to either increase Social Security tax income or reduce benefits or some combination of both, the system can only support the full promised benefits until 2033, after which benefits would be reduced so as not to exceed available income. Enhanced benefits for the old-old would more than likely come with a cost that exacerbates the problem of achieving sustainable solvency. These enhanced benefits would need to be paid for by increasing revenue or reducing other benefits to an even greater extent than if no enhancements were made for the specific benefit of the old-old.

The second aspect to keep in mind is the balance between the *individual equity* and *social adequacy* aspects of the program. Despite an emphasis on helping those who earn lower incomes during their working years, Social Security still pays benefits even to the wealthiest Americans. Because thewealthier wage earners pay more into the system in taxes, under the Social Security benefit formula they receive the highest benefits when measured by dollars, although not when measured as a percentage of pre-retirement income or taxes paid. Providing higher benefits to those who pay more in taxes is generally called "individual equity," while providing proportionately higher benefits to those at the lower end of the wage scale is generally called "social adequacy."

Since its establishment, Social Security has included elements of individual equity and social adequacy. This balance has not been static, but has shifted over the years as new benefits were added and the benefit formulas changed. There is no agreed-upon theoretically correct balance. The actual balance has emerged from decades of legislative changes to the program. Should benefits be increased for the old-old, this balance will most likely shift yet again. It is important that the resulting modifications to Social Security are considered with recognition of the impact on both the individual equity and social adequacy elements. How best to effectively target those with the greatest likely financial need upon reaching more advanced old age is a challenge within itself. This balance between individual equity and social adequacy adds another layer to this challenge.

Finally, not all will benefit from improved longevity to the same degree. Enhancing benefits for the old-old would direct additional resources to those who experience greater longevity. This issue brief addresses changes to Social Security that specifically focus on the concerns of the old-old and does not the address potential impacts on beneficiaries who may not benefit from such changes or more generally of payroll taxpayers. Those topics are beyond the scope of this brief.

With possible program modifications, some questions need to be considered: Who should be the recipients of changes to the program that focus on improving financial security for the old-old? Is there a target age? Should there be a qualification requirement based on income and or assets? Should there be specific consideration for those who had significant assets when they retired but did not plan properly for the possibility of a long retirement and now are vulnerable? These questions and others should be seriously considered for their impact on Social Security's solvency, beneficiaries, and taxpayers as alternatives are explored.

Strategies

Although Social Security's solvency does not face imminent crisis, its financial situation as outlined above has drawn attention to the need to make changes to the system. There is disagreement about the changes to make. Certain proposals include changes that focus benefits more narrowly on the financially vulnerable. Such changes include adjusting the benefit formulas to increase the disparity in benefits as a percentage of pre-retirement income between higher- lower-paid workers, or introducing means testing to eliminate or reduce benefits to retired workers with high incomes, assets, or some combination of the two. The latter approach would entail a significant change to how the program has historically operated. Providing enhanced benefits for the old-old should not be done in a manner inconsistent with any general approach to reforming Social Security.

There are many possible strategies for changing Social Security for the benefit of the old-old. This issue brief does not consider any strategies under which enhanced benefits for the old-old are contingent on a demonstration of financial need. While such an approach would be more cost-effective, it is not consistent with the design of the Social Secuirty program. The strategies considered in this issue brief are in keeping with the nature of Social Security as a social insurance rather than a welfare program. The strategies are based on the concept of presumed need, *i.e.*, eligibility is based only on the attainment of broadly defined eligibility requirements rather than on a beneficiary's specific financial situation. Some of these strategies could be designed to be revenue-neutral while others will add to the cost of the program.

The following are the alternative old-old benefit improvements considered in this paper:

1. Targeted benefit supplements
2. Longevity benefit riders
3. Enhanced cost-of-living increases
4. Modification of widow/widower survivor benefits through use of optional benefit forms
5. Changes to the Social Security Retirement Age

Targeted benefit supplements

Targeted benefit supplements provide a direct solution to providing additional income to the old-old. Enhanced monthly benefits could be provided based on a revised formula once a beneficiary reaches a specified age (age 80 or 85, for example). This new benefit could be provided to all benefit recipients or only those meeting certain conditions (for example, those with a Social Security benefit below a specified monthly amount). Or, a minimum benefit could be established, perhaps relative to the poverty line.

Pros:

- Provides financial support for individuals who may not be able to supplement income from Social Security with additional income.
- Maintains social insurance framework by providing a uniform benefit formula to participants (only adding a new minimum or tier of Old Age benefits).

- May support improved availability and quality of end-of-life care.
- Addresses financial hardship directly, regardless of the cause.

Cons:

- Additional administrative burden.
- More difficult to explain and understand future level of Social Security benefits.
- Would alter the balance between individual equity and social adequacy.
- Additional cost to the program.

Longevity Benefit Riders

Longevity insurance is a deferred annuity providing a lifetime income upon survival to a specified future age. If funded through a reduction in an annuity payable immediately at retirement, the amount of the additional deferred lifetime income available at the "old-old" age will exceed the reduction in the immediate annuity amount. This is attributable to the shorter payout period beginning at a later date benefiting from both interest and mortality credits for the intervening period.

Many retirees have accumulated some funds for retirement, though most do not have sufficient amounts to last as long as 30 or 40 years. The use of longevity insurance allows for a cost-effective hedge against running out of funds. Though there is a private-sector longevity insurance market, it has yet to gain much popularity for reasons including but not limited to pricing, lack of competition, and general lack of awareness. Because Social Security is a near universal benefit, it may be of value to consider integrating a longevity insurance option within Social Security.

For example, retirees could voluntarily exchange a portion of their benefit payable at "initial retirement" for a longevity benefit commencing at an advanced age. Starting three to five years prior to eligibility for initial benefits, an individual would receive with their annual Social Security benefit statement an explanation of longevity insurance describing how the benefit works as well as how it might protect them from old age financial hardship. In addition, a table would include numerical illustrations for various combinations of retirement ages, longevity benefit commencement ages, and longevity benefit amounts. When the individual actually retired, he or she could elect the longevity benefit at a level of his or her choice.

The longevity benefits would be actuarially equivalent individually or determined to be actuarially equivalent in the aggregate based on utilization assumptions. In the latter case, benefits would provide a greater value at lower Primary Insurance Amounts (PIA)[1] to offset the expected lower utilization by low-income retirees (those at the greatest risk of experiencing financial hardship). Thus an individual with a PIA of $1,000 would be eligible for a larger benefit based on a $100 benefit reduction charge than an individual with a PIA of $2,000.

Pros:

- Cost-effective way to provide old-age protection for those who can afford reduced benefits at younger ages.
- Can be designed to provide greater benefit for those most likely in need.
- Universal program that all may participate in.
- Can be designed to not add to cost of the program.

1 The "primary insurance amount" (PIA) is the benefit (before rounding down to next lower whole dollar) a person would receive if he/she elects to begin receiving retirement benefits at his/her normal retirement age. At this age, the benefit is neither reduced for early retirement nor increased for delayed retirement.

Cons:

- Retirees may not fully appreciate the value of insuring a more secure retirement should they live to extreme old age.
- Additional administrative burden.
- Adverse selection issues.
- Requires public education regarding longevity risk and risk sharing.

Enhanced cost-of-living increases

One suggested means of improving the financial security for the most elderly group of retirees is to change the current cost-of-living index for Social Security benefits.

Currently, benefits are increased annually based upon the CPI-W, a measure of the increase in cost of living for the population in general. An enhanced increase for retirees could be implemented in various ways. For example, the cost-of-living increase could be set at CPI-W plus 1 percentage point commencing at an advanced age such as 75. The increase could also be restricted to those beneficiaries with lower income levels.

Pros:

- Simple to explain.
- Applies in a uniform fashion for eligible Social Security recipients, as does the current CPI-W.
- Easy to implement.

Cons:

- The reason the old-old have a higher incidence of poverty may not be due entirely to the effects of inflation, therefore changing the index that determines the cost-of-living increase may not appropriately capture the entire problem.
- This approach may be poorly targeted if too much of the increase in benefits goes to people who are not facing old-age poverty.
- A major expense for the elderly is related to medical care and long-term care. This suggests that it might be more efficient to mitigate old-age poverty by allocating more funding and benefits to Medicare and Medicaid programs rather than using an approach where extra payments are made to individuals who are not incurring these additional expenses.
- Adds to cost of the program.

Modification of widow/widower survivor benefits through use of optional benefit forms

Another area for consideration is whether changes in the benefit levels payable to surviving spouses would be helpful in tackling the old-old challenge. Under current law, a retiree is entitled to the greater of the benefit based on his or her earnings record or 50 percent of the benefit based on the earnings record of a spouse. A surviving spouse is entitled to the greater of the benefit earned on his or her record or that of a spouse.

Consider this specific scenario that may lead to financial hardship among the old-old. Both spouses work a full career with roughly equivalent benefits. Upon retirement, the couple receives two full benefits. However, upon the first death only one benefit is payable, thus reducing the benefit by 50 percent. It is unlikely that expenses will also drop by 50 percent, thus creating hardship for a person relying very heavily on Social Security.

Changes to Social Security that would decrease the size of the income drop that occurs upon the first death could be considered. One way to approach this issue is by allowing Social Security retirees to elect a benefit form other than a life annuity. This would allow a retiree who is dependent on the income of his or her spouse to opt for a smaller initial benefit in exchange for a higher contingent survivor benefit payable upon the death of that spouse. This could be very effective in protecting against a large drop in income in the case of a two-earner couple with relatively equivalent benefits.

Pros:

- Provides option for increased longevity benefits for widowed seniors.
- Maintains basic Social Security framework.
- Adds no significant cost to the program.

Cons:

- No new option for unmarried people facing poverty.
- May still not provide adequate benefits.
- Additional administrative burden.
- Requires an understanding of the value of the benefit option by retirees.

Changes to the Social Security Retirement Age

When the Social Security program began paying monthly benefits in 1940, workers could receive unreduced benefits at age 65. This age is called the Normal Retirement Age (NRA). The law was changed in 1983 to increase the NRA gradually to age 67 according to the following schedule:

Year of Birth	Social Security Normal Retirement Age
1937 and earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943 through 1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and later	67

Many Social Security reform proposals include a provision for further increasing the NRA. Part of the rationale for continued increases in the NRA is that without changing the NRA, the value of the benefits provided increases as longevity increases. However, raising the NRA without changing the benefit formula constitutes an across-the-board decrease in the monthly benefits provided. At any given retirement age, a worker's benefit would be subject to a greater early retirement reduction and/or a smaller late retirement increase than before the change. For this reason, raising the NRA improves Social Security's financial situation, which is why it is a common feature of reform proposals.

Raising the NRA without changing the benefit formula does nothing to directly help the old-old, and indeed disadvantages those who are unable to delay retirement. This does not mean an increase in NRA should not be considered in the context of helping the old-old. The benefit formula could be increased so that, even as the NRA increases, benefits at any given retirement age remain roughly the same as currently provided. Such a change in the NRA could induce favorable behavioral changes. Some workers may decide to remain longer in the workforce, retire later, and qualify for original higher benefits. To the extent this behavior occurs, the old-old will be better off—not only because they receive higher Social Security benefits, but also because they have a greater opportunity to save for retirement outside of Social Security while still working. Even though the value of benefits does not change, a portion of the financial gains to the system remain, because workers who retire later pay taxes into the system for a longer period. Nevertheless, a primary purpose of increasing the NRA as discussed here is to alter the perception of the appropriate time to retire rather than to improve the system's financial situation.

One obstacle to this possible change in behavior is that other federal laws continue to consider the "normal" retirement age as 65. For example, most workers first qualify for Medicare benefits at age 65, and retirement plans governed by the Employment Retirement Income Security Act (ERISA) cannot define the normal retirement age later than 65 in most circumstances. These and perhaps other representations of the normal retirement age would need to change to gain the full behavioral and signaling effect of raising Social Security's NRA.

There are other possible variations to consider that could encourage delayed retirement where possible. For example, the benefit formula could be changed so that, as the NRA goes up, benefits at a given retirement age increase nominally for low-wage workers, but not for higher-wage workers. This strategy could be effective in keeping the old-old out of poverty, because most of those in danger of falling into poverty were low-wage workers before retirement. Another option, either alone or in combination with the preceding, is maintaining NRA for certain workers such as: (1) workers in physically demanding occupations prevented from working by conditions not serious enough to qualify them for Social Security disability benefits; (2) workers affected by workplace shutdowns or mass layoffs; and (3) workers in geographic areas experiencing high levels of unemployment. Like lower-wage workers, these groups are particularly vulnerable to experiencing financial hardships.

Pros:

- Benefit formula increases can be more generously targeted at those groups of workers most vulnerable at advanced ages.
- May not add to cost of the program.

Cons:

- This strategy relies on behavioral incentives that may not be effective.
- The incentives may be diluted by countervailing incentives in other government programs unless those programs are also changed.

Conclusion

Continued improvement in longevity could result in a significant increase in the number of old-old citizens facing financial security challenges. Social Security may be the best tool for addressing this potential problem if the program is to continue to support retirees—including the old-old—in an effective manner.

This paper is offered as a starting point, presenting several potential strategies for addressing the old-old challenge within the Social Security program. It is hoped that it will stimulate discussion on these and possibly other ideas.