# SOCIAL SECURITY REFORM CHECK LIST #3

## The National Commission on Retirement Policy Plan

### Overview

The National Commission on Retirement Policy (NCRP), a bipartisan group convened by the Center for Strategic and International Studies, has endorsed a proposal that would fundamentally restructure Social Security. The plan channels two percentage points of the current payroll tax (12.4 percent of wages, divided equally between workers and their employers, with a cap at $68,400 in yearly income) into mandatory individual savings accounts. To compensate for the reduction in tax revenue and eliminate the projected shortfall in Social Security beginning in the year 2032, the NCRP plan cuts benefits substantially --in part by increasing the retirement age to seventy.

### Summary of Key Features

**Benefit Changes**. According to the Congressional Research Service, the NCRP plan would reduce guaranteed benefit levels set under current law by 33 percent for an average-wage-earning worker retiring at the age of sixty-five in the year 2025. By 2070, after the plan is fully phased in, benefits for the average worker (who retires at sixty-seven) would be 48 percent lower than under present law. The specific changes leading to those reductions include:

> Raising the normal retirement age from sixty-seven in 2029 (an increase that is already scheduled to be phased in under current law) to seventy. The plan would also increase the age of eligibility for reduced benefits from sixty-two to sixty-five by 2017. Raising the retirement age amounts to cutting benefits, since workers will receive lower lifetime benefits.
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> Reducing benefits for middle-income and high-income retirees. The portion of pre-retirement earnings that Social Security pays middle-income beneficiaries would decrease from 32 percent to 21.36 percent by 2020. For higher-income beneficiaries, the reduction would be from 15 percent to 10.01 percent by 2020.
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> Increasing the number of working years counted to determine benefit levels from today's thirty-five to forty by 2010. Adding more years would reduce benefit levels because the average past salaries that benefits would be based on would include more years when workers were young and earning less--or nothing at all. Those with long absences from the workforce –women more commonly than men--would end up with the largest reductions.
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> Reducing benefits to dependent spouses from 50 percent of their spouses' benefits to 33 percent.

**Tax Changes**. The plan would not increase payroll taxes, raise the cap on taxable earnings, or increase the taxation of benefits to help close the existing financing gap. But it would divert two percentage points of the current payroll tax into individual savings accounts.

**Structural Changes**. The NCRP proposal's structural changes to the Social Security program include:

> Introducing individual savings accounts modeled on the Federal Thrift Savings Plan, which allows workers to invest in several broad-based funds. At retirement, workers would be required to annuitize the majority of funds in their accounts -- that is, convert them from lump sums into monthly payments that are made for the duration of their lives.
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> Expanding Social Security coverage to include all newly hired state and local government employees.
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> Creating a new minimum benefit equal to 100 percent of the poverty line for those who have spent forty years or more working and 60 percent of the poverty line for those with twenty to thirty-nine years in the workforce.

## Evaluating the Plan

To assess the impact of various proposals to change Social Security, The Century Foundation organized a group of experts to develop principles for prudent reform. Here's how the National Commission on Retirement Policy plan stacks up against those principles:

### Principle 1

*Social Security should continue to provide a guaranteed lifetime benefit that is related to past earnings and kept up to date as the general standard of living increases.*

> ***Analysis:*** Although the plan retains a guaranteed benefit based on a worker's past earnings, the size of that benefit would be cut by 33 percent for the average worker retiring at 65 in 2025. Those reductions would be offset somewhat by provisions for new individual savings accounts and minimum benefits of 100 percent of the poverty line for those who spent forty years or more working and 60 percent of the poverty line for those with twenty to thirty-nine years in the workforce. But, in the process, benefit levels would become less closely tied to past earnings and more dependent on the performance of the investments in each worker's individual savings account.

### Principle 2

*American workers who have the same earnings history and marital status, and who retire at the same time, should receive the same retirement benefit from Social Security*.

> ***Analysis:*** While workers with similar earnings histories and marital status would receive the same, reduced baseline benefit from Social Security, the introduction of individual savings accounts would produce significant variations in overall benefits. Those who enjoyed better luck with their individual accounts, who invested more aggressively, and retired when their investments were at a peak would receive higher payments than workers who invested less wisely, opted for more conservative investments, or retired when their investments were down.

### Principle 3

*Social Security benefits should continue to be fully protected against inflation, and beneficiaries should continue to rest assured that they will not outlive their monthly Social Security checks*.

***Analysis:*** Although guaranteed benefits are cut substantially under the NCRP plan, they would still be indexed for inflation and continue until death. However, payments from individual accounts would not be protected against inflation. The NCRP plan would require retirees to convert most of their individual savings accounts investments into annuities upon retirement, but it does not mandate that these annuities make payments that are indexed for inflation. Unless workers chose to convert the accumulations in their accounts into annuities that are indexed for inflation, the value of each payment would decline over time as inflation reduced the value of the dollar. Today, inflation-adjusted annuities are very expensive and not widely available in the private market.

### Principle 4

*Retirees who earned higher wages during their careers should continue to receive a larger check from Social Security than those with lower incomes; but the system should also continue to replace a larger share of the past earnings of low-income workers.*

***Analysis:*** The NCRP changes in the benefit formula would result in middle-income and higher-income retirees receiving a lower percentage of their past earnings than is currently the case. This would represent a substantial cut in their benefits. Still, workers who earned more would continue to receive somewhat higher benefits than individuals who had lower incomes. And the new guarantee of benefits equal to 100 percent of the poverty level for workers who spent at least forty years in the workforce and 60 percent for those who worked twenty to thirty-nine years would offer protection for some low-income retirees--though less than the current system does in most cases.

### Principle 5

*Social Security's insurance protections for American families, including disability insurance, should be fully sustained*.

***Analysis:*** Although the NCRP plan would retain insurance coverage for the disabled and for surviving spouses, the reductions in guaranteed retirement benefits would dramatically reduce protections for workers whose earned income plummets for an extended period because of disability. The combination of delaying the retirement age, extending the number of working years counted in determining baseline benefits, and changing the formula for calculating those benefits would especially imperil those, like the disabled, who leave the workforce for years at a time.

### Principle 6

*Social Security's long-term financing problem should not be aggravated by diverting the program's revenues to private accounts and benefits should not be reduced to make room for private accounts; any such accounts should be supplementary to Social Security, entirely as an add-on*.

> ***Analysis:*** The NCRP plan imposes significant benefit cuts to allow two percentage points of payroll tax revenue to be diverted to individual savings accounts. The reduction in guaranteed benefits is far greater than the cuts that would be needed to assure that the system will be adequately financed throughout the next century.

### Principle 7

*In addition to securing Social Security as the foundation of income support for retirees, their dependents, the disabled, and survivors, more needs to be done to encourage private savings and pensions*.

> ***Analysis:*** The NCRP plan shifts assets accumulating in the Social Security trust funds to individual savings accounts, a process that would neither increase nor decrease national savings (the combined savings of the government, companies, and households), or personal savings levels. Many economists argue that increasing the nation's low savings level would help to promote long-term economic growth by supplying more capital for long-term investment.

12/10/98