COMMITTEE ON WAYS AND MEANS
CHAIRMAN DAVE CAMP

Social Security Benefit Adjustments

Summary

Current Law

Benefit Formula

Social Security benefits are determined by applying a benefit formula to a measure of average lifetime earnings. Social Security benefits are calculated by first averaging the monthly equivalents of each of the highest 35 years of earnings, after adjusting for growth in wages over time, known as the averaged indexed monthly earnings (AIME). The adjustment for growth in wages over time ensures that a worker's future benefits reflect the general rise in the standard of living that occurred during his or her working lifetime.

The benefit formula is applied to the AIME to determine the basic benefit amount, called the primary insurance amount (PIA). The benefit formula is tiered to provide progressive benefits (90 percent of the first $791 of AIME, plus 32 percent of AIME between $791 and $4,768, plus 15 percent of AIME above $4,768 and up to $9,475). The percentages in the benefit formula (90, 32, 15) are referred to as PIA factors, while the dollar amounts are referred to as bend points (because the formula, when graphed, appears as a series of line segments joined at these amounts). The bend points in the formula are indexed to growth in wages each year to ensure the replacement rate—initial benefits as a percentage of career-average earnings—remains constant for each successive generation of workers. While the replacement rates remain the same, the buying power of benefits increases for every successive generation.

Retirement Age

Monthly retirement benefits derived from the PIA may be higher or lower than the PIA depending on their full retirement age (FRA). Reduced benefits are paid when a person retires before his/her FRA, in order to ensure that the total amount of lifetime benefits is not affected by when benefits are claimed. A person cannot collect retirement benefits before age 62, which is the earliest eligibility age (EEA). In the case of a person retiring at exactly age 62 in 2013 (born in 1951 and who has a FRA of 66), the benefit will be 25 percent less than the person's PIA.

Benefits can be higher than the PIA if one retires after the FRA. The credit given for delayed retirement will gradually reach 8 percent per year for those born in 1943 and later. No delayed retirement credit is given after age 70, so the maximum increase is 32 percent.

The effects of early or delayed retirement on retirement benefits are illustrated here.

The FRA has been gradually increasing from 65 (for those born before 1938) to 67 (for those born in 1960 or later).

Special Minimum Benefit

A special minimum PIA, known as the Special Minimum Benefit, was intended to provide adequate benefits to long-term low earners. This minimum benefit may be paid to workers with more than 10 years in Social Security covered employment. The minimum benefit amount paid to a retired worker is based on, and rises with, the number of years he or she worked in covered employment. The value of the minimum benefit has increased with prices since 1979. However, according to the Social Security Administration, the special minimum benefit last exceeded an actual worker's wage-indexed PIA in 1998, because wage growth has typically exceeded price growth.

Assumptions

Based on conversations with staff from the Simpson-Bowles Commission, the start date of the benefit formula change has not been altered to hold those over age 55 harmless.

Proposals

Simpson-Bowles Commission:

Retirement Age

The proposal would index the FRA to the increase in life expectancy for those reaching 62 in 2022 and later. The EEA, currently age 62, will increase at the same time to maintain a 5-year difference between the EEA and FRA. The EEA for widow(er)s, currently 60, is assumed to increase concurrently. The number of months during with delayed retirement credits can accrue is assumed to stay constant.

As a result of the EEA increase, the number of years included in the calculation of average lifetime earnings will increase concurrently. For example, under the proposal, when the EEA reaches 63, the number of years used to calculate benefits will be 36. The Commissioner is instructed to develop a hardship exemption to the retirement age increase to protect those who are unable to work longer.

All beneficiaries subject to an increase in the EEA and FRA will have the option to claim up to half of their benefits at age 62.

Benefit Formula

As introduced in December 2010, the proposal would slow the growth of initial benefits beginning for certain beneficiaries turning 62 in 2017 and later. When introduced, the proposal would have held those over age 55 harmless (age 58 today).

Special Minimum Benefit

As introduced in December 2010, the proposal included an increase in the special minimum benefit beginning in 2017, to equal 125 percent of the 2009 Federal Poverty threshold for those who worked with at least 30 years in jobs covered by Social Security. Since the provision referenced the Federal Poverty threshold as of one year before the proposal's announcement, the 2012 Federal Poverty threshold is assumed.

Domenici-Rivlin Task Force:

Benefit Formula

The proposal would reduce the PIA factors to account from increases in longevity beginning in 2023.

The proposal would gradually reduce the third PIA factor by one-third (from 15 to 10 percent without interaction with any other provision), beginning in 2023 and phasing in over 30 years.

Special Minimum Benefit

As introduced in November 2010, starting in 2012, the proposal would enhance the special minimum benefit at a level equal to 133 percent of the 2009 Federal Poverty threshold for those with earnings of at least 20 percent of the "old law taxable maximum[i]" in at least 30 years. Up to 8 years of childcare can count towards years for eligibility determination. Since the provision was effective two years after the proposal's announcement, an effective date of December 2015 and later, as well as a Federal Poverty threshold from one year prior (2012), is assumed.

[i] The "old-law" contribution and benefit base for 2013 is $84,300. This is the base that would have been effective without the enactment of the 1977 amendments to the Social Security Act. The present-law contribution and benefit base, $113,700, is substantially higher than the old-law base.