AMERICAN ACADEMY of ACTUARIES

THE BOTTOM LINE
-ON-
ASSUMPTIONS USED TO PROJECT SOCIAL SECURITY'S FINANCIAL CONDITION

The 2001 Social Security Trustees Report states that, under intermediate ("best estimate") actuarial assumptions, the trust funds will be exhausted in 2038. Understanding the trustees' assumptions is critical to evaluating the solvency of the Social Security trust funds as well as proposals to improve the program's long-term financing.

The American Academy of Actuaries' Committee on Social Insurance has updated its 1998 issue brief, *Assumptions Used to Project Social Security's Financial Condition*, to reflect the most recent Trustees Report. Key findings in the paper include:

- The Trustees Report relies on demographic and economic assumptions to present intermediate, low-cost, and high-cost projections. A 1999 technical panel to review the trustees' actuarial assumptions concluded that the trustees' projection methodology is "reasonable as a whole."

- Major demographic assumptions are used to project characteristics of the future population, while major economic assumptions are used to project wages, benefits, and tax and investment income of the Social Security program.

- Other entities have used assumptions different from the trustees' intermediate assumption set to make financial projections. For example, for its 10-year budget estimates, the Congressional Budget Office (CBO) uses more optimistic assumptions than the Trustees' report for the corresponding 10-year projection period.

The Academy also makes the following recommendations:

- All analyses of Social Security reform proposals that include financial projections should also include an explanation of the assumptions used;

- All analyses of proposals should rely on assumptions that are internally consistent;

- Where substantial uncertainty exists as to the appropriate level of a critical assumption, sensitivity analysis or a range of assumptions should be used;

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- When calculations for competing reform proposals use different sets of assumptions, comparisons of those proposals should recognize the effects of the differing assumptions.

For additional information, please see the Issue Brief on the Academy's web site (www.actuary.org) or contact Bridget Flynn, the Academy's Pension Policy Analyst, at (202) 223-8196.

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