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AMERICAN ACADEMY *of* ACTUARIES

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July 31, 2013

Representative Sam Johnson  
Chairman, Social Security Subcommittee  
Committee on Ways and Means  
U.S. House of Representatives  
1101 Longworth House Office Building  
Washington, D.C. 20515

Representative Xavier Becerra  
Ranking Member, Social Security  
Subcommittee  
Committee on Ways and Means  
U.S. House of Representatives  
1101 Longworth House Office Building  
Washington, D.C. 20515

Re: May 23, 2013 Hearing on Social Security

Dear Chairman Johnson and Ranking Member Becerra:

I am pleased to respond to your request for further comments regarding my May 23 testimony on increasing the Social Security retirement age. I testified to how the Social Security system could better reflect longevity improvements, including alternatives to increasing the retirement age. The American Academy of Actuaries<sup>1</sup> has advocated, for purposes of sustaining the financial solvency of the system, increasing the retirement age to reflect increases in life expectancy among American workers. Adjusting Social Security benefits for life expectancy should be a critical part of any changes to resolve the deficit between future benefits and future income.

You have asked me to address three questions:

- 1. In your testimony, you discuss the fact that Social Security's retirement age influences when someone decides to stop working. What are your views regarding addressing longevity through increasing the retirement age versus changing the benefit?**

A change to the benefit formula can provide the same amount of benefit as results from increasing the full retirement age, but it sends a far different message to the American worker. Workers look to both the earliest eligibility age and the full retirement age as goals or milestones. Experience points out how significant these milestones are: approximately 44 percent claim at the earliest eligibility age and almost 95 percent claim by the full retirement age.

Changing the formula but not the earliest and full retirement ages would have less influence on the retirement age selected by workers because of the signal that the eligibility ages provide. With a reduced benefit formula, many retirees would receive smaller payments because they claimed at the full retirement age, rather than working

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<sup>1</sup> The American Academy of Actuaries is a 17,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

longer and receiving a larger benefit. This change would be detrimental to the financial security of our elderly.

**2. Should the early eligibility age (EEA) of 62 be increased? What is the effect on the claiming age if the EEA is or is not increased?**

Increasing the early eligibility age has the beneficial result of encouraging most individuals to work longer. Individuals who remain in the labor force are a productive part of our economy and able to save more for their deferred retirement.

Increasing the EEA also helps prevent payment of benefits that may prove inadequate. The 1983 amendments changed the full retirement age (FRA) but not the EEA, allowing workers to retire up to five years prior to full retirement age. This increased the early retirement reduction in the benefit from 20 percent at three years to 30 percent at five years. Increasing the full retirement age beyond age 67 without also raising the EEA would mean that benefits at the early eligibility age would be reduced more than the current 30 percent. This reduction applies to the benefits over the full lifetime of individuals and may as a result prove to be inadequate to retirees' needs, potentially causing pressure for benefit increases. Raising the EEA in concert with the FRA would maintain the maximum reduction at 30 percent.

If the EEA is not changed, initial claims at age 62 (currently about 44 percent) will continue to be high. If the EEA is increased, more individuals will work longer and ultimately receive larger benefits.

Increasing the EEA does not significantly change Social Security's financial position because early retirement benefits are already reduced to the approximate actuarial equivalent payments.

**3. If the full retirement age (FRA) is increased but the EEA is not, an individual who claims at 62 would see a larger benefit reduction. For example, if the FRA is increased to age 70, the actuarial reduction at age 62 would be 43 percent. What is the impact of changing the size of the reductions so they are not actuarially neutral?**

Changing the reduction factors so that they are not actuarially neutral would increase the cost of Social Security and undermine the beneficial aspects of increasing the full retirement age (FRA).

Increasing the FRA brings with it a retirement signaling effect that sends a message to American workers encouraging longer work careers. At the same time, providing subsidies that facilitate early retirement encourages shorter work careers. These two messages are at odds.

The American Academy of Actuaries appreciates the opportunity to provide the subcommittee with these comments and would welcome the opportunity to assist in any further exploration of these issues. Please contact David Goldfarb, the Academy's pension policy analyst (202-785-7868; goldfarb@actuary.org) if you have any questions or would like to discuss these items further.

Sincerely,

Donald E. Fuerst, MAAA, FSA, FCA, EA  
Senior Pension Fellow  
American Academy of Actuaries

Cc: Members, Subcommittee on Social Security  
House Ways & Means Committee