

Old-Age, Survivors, and Disability Insurance

by ARTHUR J. ALTMeyer *

Hearings on the Social Security Act were opened by the House Ways and Means Committee on February 28, with statements on the public assistance provisions. On March 23 the hearings on old-age and survivors insurance were opened, and on that date the Commissioner for Social Security made the following statement.

WHEN this committee began hearings on title I of the Social Security Act, I referred to public assistance as our second line of defense against destitution. My statement today is concerned with the first line of defense—a comprehensive system of contributory social insurance having as its aim the prevention of destitution.

These two lines of defense were established by the Congress in 1935 from the perspective of several decades of experience including the "boom" of the 1920's and the "depression" of the 1930's. Fourteen years of operation under the program have proved the wisdom of the decision Congress made in establishing the social insurance system.

Following the policies laid down by the Congress and guided by our experience in administering the program, we have recommended in our annual reports that the contributory social insurance program be improved and strengthened along the following lines: (1) extending the coverage of the old-age and survivors insurance program to practically all gainfully employed persons, (2) raising the level of benefits paid under the program, and (3) expanding the program to provide protection against disability as well as old age and death.

Old-Age and Survivors Insurance Benefits

As the Committee knows, the Federal old-age and survivors insurance program is the only part of the Social Security Act which is administered wholly by the Federal Government. Employers and employees have each been making contributions of 1 percent of taxable wages since January 1, 1937. Under the original provisions of the Social Security Act, monthly

benefits would not have been payable until January 1, 1942. The 1939 amendments, however, advanced that date to January 1, 1940. The 1939 changes also resulted in an increase in the payment of benefits during the early years of the system's operation. Above all, the amendments added dependents' benefits and survivors benefits so that now, in addition to the payment of old-age benefits to workers themselves, monthly benefits are also payable to the aged wife and young children of a living beneficiary and to the widow, children, and, in some cases, the dependent parents of an insured worker who dies. The face value of these survivors benefits is now about \$80 billion. Just as contributions are paid on the basis of wages received, so these benefits are paid on the basis of the past wages of the insured worker, and thus compensate for a portion of the wage loss sustained by his retirement or death.

I believe that the Ways and Means Committee has a right to be proud of the way this law has functioned to date. There were many persons in 1935 who doubted that this social insurance system could be simply and efficiently administered. However, at the present time there are 2.3 million aged persons, widows, and orphans receiving monthly benefits. By the end of this present calendar year the number will probably have increased to about 2.6 million. Contributions for the year 1949 are being collected at an annual rate of about \$1.8 billion, and disbursements are running at a rate of \$700 million.

This Federal old-age and survivors insurance system constitutes the largest permanent insurance system in the world. Therefore, unprecedented administrative problems have been encountered in putting it into effect. However, all of these problems have been solved. The total

cost of administration at the present time is 3 percent of contributions collected and less than 10 percent of benefit payments. This percentage is declining steadily and there is no question that as benefit rolls increase the cost of administration will decline to less than 3 percent of benefit payments.

At the present time accounts have been established for about 80 million living workers who have wage credits. The cost of maintaining these wage records is about 12 cents per account per year.

There can no longer be any doubt as to the effectiveness and practicality of this Federal old-age and survivors insurance system. However, the years that have passed have indicated various ways and means in which it could be improved and also demonstrated that its benefits could be extended to cover substantially all the gainfully employed persons, including the self-employed.

Extension of Coverage

The present Federal old-age and survivors insurance program covers, with certain important exceptions, employers of one or more employees. Despite these exceptions, social security account cards have already been issued under this program to some 90 million persons, of whom 80 million living workers already have had some wage credits posted to their accounts because of work in insured employment. It is apparent from these figures that a large proportion of the gainfully occupied population already has some measure of protection against old-age and death. However, it is also apparent that many persons pass back and forth between insured employment and uninsured employment. In 1948, while only 35 million individuals were engaged in insured employment at any one time, over 50 million individuals worked in insured employment during the year.

Since the amount of a benefit depends to a considerable extent upon the length of time an individual actually works in insured employment

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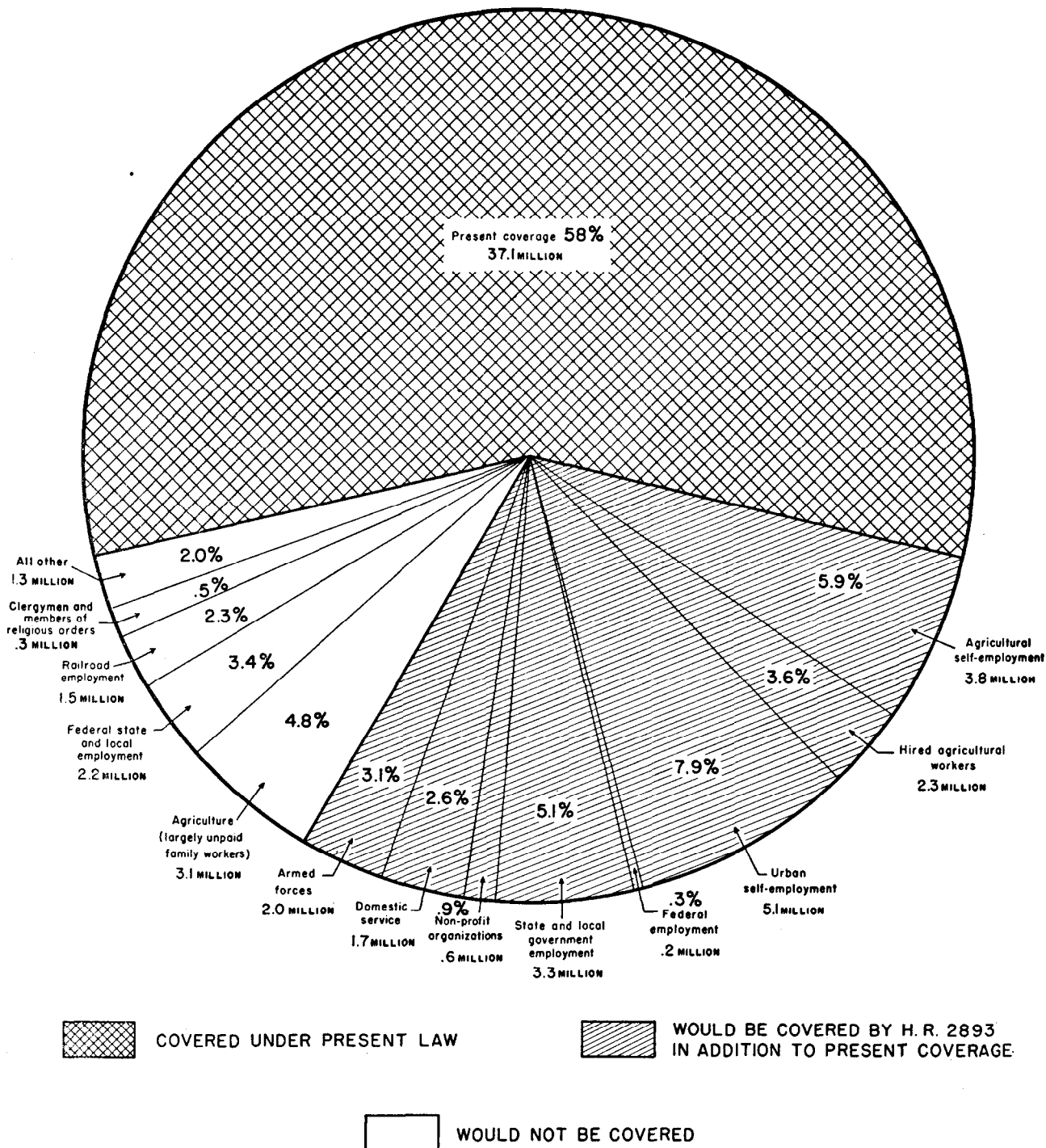
and the amount of his earnings in such employment, persons who pass in and out of insured employment get lower benefits than they would have if all their work had been in insured employment. Persons who always

work in uninsured employment are unable, of course, to develop any benefit rights whatsoever.

The main groups now excluded from old-age and survivors insurance are agricultural laborers, domestic

servants, employees of nonprofit organizations, public employees (Federal, State, and local), railroad employees, and self-employed persons (including small-business men and farmers).

Chart 1.—Estimated proportion of the employed labor force in covered and noncovered employment, June 1950



It is gratifying to note that various groups who have studied the contributory social insurance system have recommended that coverage be extended. The most recent was the Advisory Council on Social Security which, after careful consideration of the administrative and financial problems involved, recommended the extension of the insurance system to cover farmers and other self-employed persons, agricultural labor, domestic service, and other groups. A study undertaken by the Treasury Department at the request of your Chairman reported that "it is now evident that administrative considerations no longer constitute an important barrier to the expansion of coverage in the event the Congress decides to extend the protection of the system." A third and earlier study of the *Issues in Social Security* was made by the Technical Staff on Social Security of your committee. The resulting report, as you know, concludes, in part: "With the prospect of the addition of other kinds of social security benefits, it seems inevitable that availability of old-age and survivors insurance benefits must be all inclusive if the Nation's social-benefit objectives are to be attained."

A recent Gallup poll reports that 60 percent of farmers who expressed an opinion on the question favored the extension of social security benefits to farmers. Many small-business men, professional workers, and others who comprise the nonfarm self-employed, in groups and as individuals have urgently requested coverage under the program.

Of the 80 million living workers who have acquired some wage credits under old-age and survivors insurance, over 13 million are permanently insured and another 31 million have some insured status, the maintenance of which depends on their continuing to work in covered employment. Even for those who are permanently insured, however, shifting between covered and noncovered employment would damage their benefit rights by reducing the amount of benefits potentially payable. Of the nearly 36 million (approximately 44 percent of the total having some wage credits) who have acquired no insured status, many have shifted to a noncovered

occupation such as self-employment. Unless these individuals later return to covered employment, their contributions will have been lost to them. An outstanding result of extending the coverage would be the elimination of this uncertainty as to insured status.

Persons who have not worked in covered employment, of course, are unable to acquire any benefit rights under old-age and survivors insurance, and many of them have no protection under any other system. Even where protection is afforded under other retirement systems, workers who shift between jobs covered by different systems are at a disadvantage, and many fail to qualify for benefits under any system. In order to assure continuity of insurance protection, old-age and survivors insurance should be made the basic social insurance system of the Nation, coordinated with the special systems covering particular groups.

In addition to increasing the social insurance protection of the population generally, extension of coverage would have other beneficial effects. It would eventually reduce the costs of public assistance. In this respect it would be particularly beneficial for the predominantly agricultural States, where public assistance costs now are comparatively heavy because so little of the burden of dependency in those States is met by the contributory social insurance program. In view of the fact that the proportion of aged persons in the population is increasing, we can expect rising public assistance costs unless the social insurance program is enabled to assume its full share of the load.

The Social Security Administration believes that one of the ways in which the Nation's obligation to its veterans can be met is by giving the veteran a chance to provide for his own future. With broad old-age and survivors insurance coverage virtually all veterans would be able to provide for their own security and the security of their families.

The self-employed.—Farm operators and urban business and professional people make up the two main classes of the self-employed, each of which is much larger than any other group excluded from the present old-

age and survivors insurance program. The number of farm operators in the course of a year is about 6 million. The number of the urban self-employed has increased greatly since the war and is now about 7.7 million.

The self-employed were excluded from the original program largely because, at that time, there was no agreement on a feasible method of obtaining such reports of their income. Subsequent developments have indicated that most self-employed persons can report their income, for purposes of coverage, as a part of their income-tax returns.

Reports would be required only from self-employed persons with gross cash incomes from all sources of \$500 or more in a year, and with net incomes from self-employment of \$200 or more. The value of goods produced for home use would not be counted. There is, of course, the special problem of determining how much income is due to self-employment as distinguished from return on investment. However, a reasonable approximation of this can be made from items already in the income-tax return. Therefore, there are no insuperable administrative problems which would prevent extension of coverage to the self-employed.

The Federal Security Agency and the Treasury Department believe that a one-page form can be devised which would be simple for the taxpayer and which would present no major difficulties in administration for the Federal Government. Net income from self-employment could be determined entirely on the basis of two figures already included in the income-tax return, namely, income from business or profession (schedule C), and income from partnerships (schedule E).

Based on the experience of the Treasury Department with the taxation of low and middle income groups in recent years, it is our opinion that the coverage of the self-employed can be accomplished simply, effectively, and economically at this time.

Agricultural labor and domestic workers.—At present about 4.1 million hired workers on farms and about 3 million domestic workers in private homes are excluded from old-age and survivors insurance in the course of a year. In addition to the 4.1 million farm workers, an estimated 600,000-

700,000 people who do not work on farms are excluded from coverage by the definition of "agricultural labor" incorporated in the Social Security Act in 1939. A large group of these workers are engaged in the preparation of fruits and vegetables for market. Altogether, therefore, some 4.7 million persons are excluded from the present

coverage as "agricultural labor."

Both farm and domestic workers are low income groups and are even less able than urban wage earners to protect themselves against the risks of old age and death through their own efforts. A principal reason for the original exclusion of these two

groups was the administrative difficulty due to the large number of small employers involved and the fact that most of these employers do not keep books and would find difficulty in making reports. On the basis of studies made during the past 10 years, I believe that it is administratively

Extension of Coverage

Many wage earners not now covered under old-age and survivors insurance do not have any protection against the risks of old age, death, and disability. Many of those who shift between employment covered by the program and noncovered employment do not acquire insured status under the insurance program and derive no protection from the contributions they have made. An extension of coverage to substantially all gainful employment (including self-employment) would assure the basic protection of the program to members of the labor force, regardless of type of work or changes in jobs, and would at the same time strengthen the financial structure of the program.

Agricultural and domestic employees.—Workable solutions have been developed for the administrative problems of covering agricultural and domestic employees. On the basis of studies made during the past 10 years, it is administratively feasible to extend coverage to these groups through the use of a stamp-book system. The employer would place special social insurance stamps in books carried by the workers. The books would be accepted as evidence of earnings and the employer would not need to make any other report or keep any special records for this purpose. The problem of evaluating noncash wages, such as meals and lodging, could largely be met by the use of a schedule of presumed values. It would be advisable to exclude exchange labor, unpaid family labor, and casual labor. For regular workers on large farms, where pay-roll records are already kept, and for situations in which the employer found it more convenient, the system of pay-roll reporting used in industry could be used.

Employees of nonprofit institutions.—No administrative problems would be involved in covering nonprofit employees. If religious organizations desired, clergymen and members of religious orders might continue to be excluded from coverage. The legislation might also declare that coverage of nonprofit employment is not intended to violate the traditional tax-exempt status of nonprofit organizations.

Federal civilian employees.—Extension of coverage to civilian employees of the Federal Government, coupled with appropriate adjustment in the civil-service retirement system, would be of substantial value to most workers. Workers who shift between Federal employment and employment covered under old-age and survivors insurance would have con-

tinuity of coverage, and career employees would have more valuable survivorship protection in the early years of their employment. The rights of annuitants and employees under the civil-service retirement system would, of course, be preserved, and the separate administration and financing of that system would be continued. Until agreement can be reached on the necessary adjustments in existing Federal retirement systems. Federal employees who are not protected by any retirement system should be covered under the old-age and survivors insurance program.

Employees of State and local governments.—Constitutional difficulties in the levy of a tax against State governments could be avoided by authorizing the Federal Security Administrator to enter into voluntary agreements with States for the coverage of their employees. Local governmental units could participate in the State agreements. Compulsory coverage might be provided for some groups of proprietary employees.

Railroad workers.—While the survivor benefits of the railroad retirement program are coordinated with those of old-age and survivors insurance, the retirement benefits of the two programs are separate. If old-age and survivors insurance were extended to railroad employment, workers who shift between employment covered by old-age and survivors insurance and railroad employment would have continuity of retirement coverage. As in the case of governmental employees, no loss of present rights need be involved.

Members of the armed forces.—Extension of coverage to service in the armed forces would assure continuity of coverage for individuals who spend only part of their working lifetime in military service. The survivorship protection that would be provided career servicemen would be especially valuable to them after they leave military service. In 1946 Congress provided free term-insurance protection to veterans in the event of death during the 3 years following separation from active service. This provision has ceased to have effect for most veterans. Instead of extending this provision, credit for World War II service should be given veterans somewhat as in the railroad retirement and civil-service retirement plans.

Self-employed persons.—A separate statement describes the method for providing old-age and survivors insurance protection for the self-employed.

feasible to extend coverage to these groups through the use of a stamp-book system.

Under such a system each employee would receive a stamp book in which stamps would be placed by his employer to evidence contributions made by the employer and the worker. In rural areas the employer could purchase these stamps from the mail carrier, and in urban areas they could be purchased at post offices. A stamp plan could be used also by small industrial and commercial establishments which found it more convenient.

For regular workers on large-scale farms, where pay records are already kept, the system of reporting now used in industry might be most convenient. For the rest—that is, for the workers on small farms and the temporary help employed during rush seasons—it might be more convenient to use a stamp plan. Whenever he paid his workers, the farmer could place special social insurance stamps in books carried by the workers. Half the cost of these stamps would be borne by the employee. The books would be accepted by the Social Security Administration as evidence of earnings, and the farmer would not need to make any report or keep any special records for the purpose.

Public employees.—It would be entirely feasible to extend the basic protection of the social insurance system to all public employees—Federal, State, and local.

The special retirement systems which now cover public employees, like those in private industry could be constructed so that their benefits would supplement those payable under the basic social insurance system. Such revisions should of course be made in such a way as to increase the total protection afforded to public employees without reducing their retirement benefits.

Until agreement can be reached on the necessary adjustments in existing Federal retirement systems, at least those Federal employees who are not protected by any Federal retirement system should be covered under the basic old-age and survivors insurance system.

Opportunity for State and local government employees to be covered

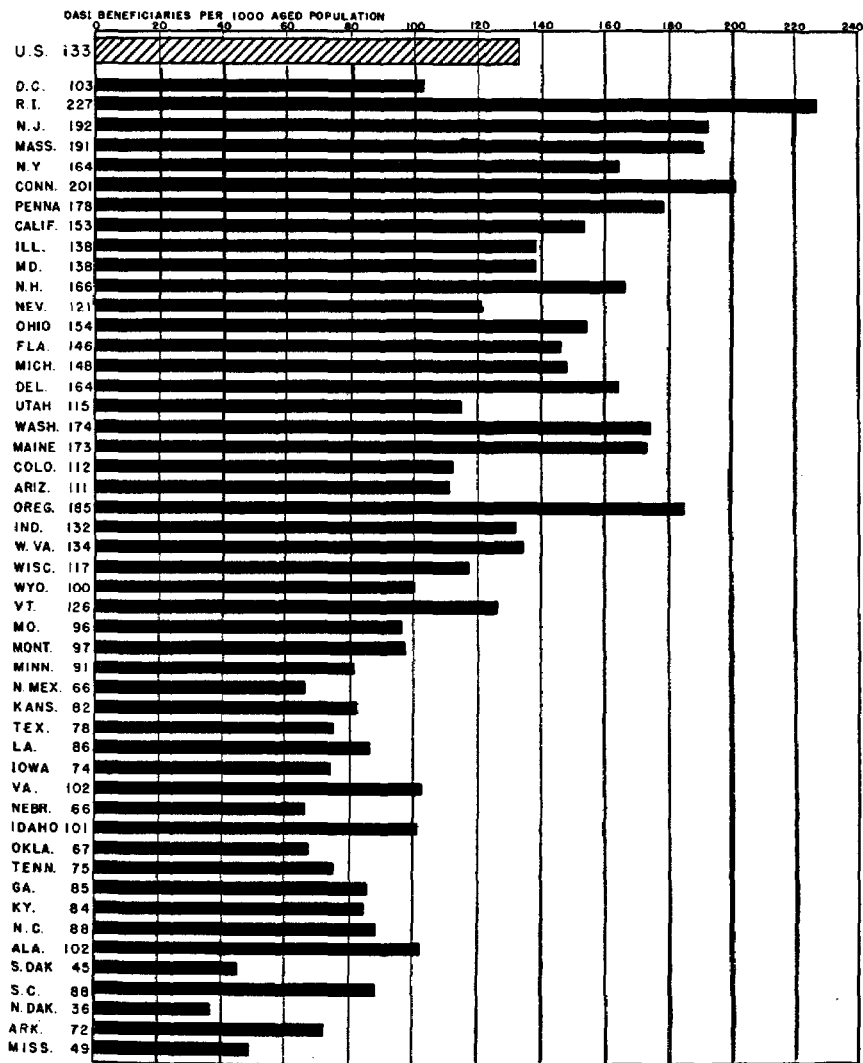
should be afforded through voluntary agreements with the States, provided the social insurance system is protected against adverse selection. Voluntary coverage is proposed in this field only because of the constitutional problem involved in taxing State and local governments.

The armed forces.—Active service in the armed forces should be included under the old-age and survivors insurance system. The establishment of a citizen army during peacetime has made permanent the problem which arose during the war of protecting the old-age and survivors insurance rights of those who devote a few years to the service of their country but who do not

stay in the armed forces long enough to qualify for the benefits of the retirement systems set up by the various services. Credit for active service should be counted beginning with the outbreak of World War II. Protection against disability and superannuation is offered by military retirement systems only for career members of the armed forces. The large group of individuals who serve for periods of less than 20 years in the armed forces would still not accumulate rights to any kind of benefits under the special systems, and should be afforded protection under the old-age and survivors insurance system.

In 1946, Congress provided what

Chart 2.—Aged beneficiaries of old-age and survivors insurance per 1,000 aged population, December 1948, by States ranked according to percentage of their total population on farms in 1940



was in effect free term-insurance protection to veterans in the event of the death of a veteran during the period of 3 years immediately following separation from active military or naval service. This period of time enables veterans to acquire at least currently insured status if they enter insured employment for as much as one-half that period. However, for those vet-

erans who do not enter insured employment this insurance protection ceases upon the expiration of the 3-year period. Even those veterans who enter insured employment suffer some reduction in their benefits because military or naval service is not insured employment. Thus, their average wage upon which benefits are based is less and they do not receive the 1-per-

cent increment which is provided for each year that a person is in insured employment. This provision has already ceased to have any effect for most veterans. Instead of extending the provisions, wage credits for World War II service should be given to veterans somewhat as in the railroad retirement and civil-service retirement plans.

Improvement of Old-Age and Survivors Insurance Benefits

Increasing the size of benefits.—Benefit amounts under the formula adopted in 1939 proved to be inadequate even before the war. Since then the cost of living and wage levels have risen sharply. The program cannot provide the basic security intended without the following major amendments:

<i>Present law</i>	<i>Proposed revision</i>
Formula: 40 percent of \$50, 10 percent of \$200.....	} 50 percent of \$75, 15 percent of \$325
Increment: 1 percent.....	
Average wage: Lifetime.....	Best 5 years
Minimum benefit: \$10.....	\$25
Maximum benefit: \$85.....	\$150
Maximum wage base: \$3,000.....	\$4,800

(a) *Benefit formula.*—The present formula should be revised to permit a larger replacement of the wages which are lost because of death or retirement. The 1-percent increment for each year of coverage should be retained in order to give higher benefits to persons who contribute longer than others.

(b) *Average monthly wage.*—As now computed, the average monthly wage, on which benefits are based, is often much less than the monthly wage ordinarily received by the worker. It would more nearly reflect a worker's actual monthly wages and produce higher benefits if based on average wages over a 5-year period during which employment was fairly regular and the worker was employed at his most developed skill and highest wages. This method would also reflect the rising trend in wages.

(c) *Continuation factor.*—Workers who have been in covered employment full time should receive higher benefits than workers who are in such employment for less than full time. Differentiation in the size of the benefits of the two groups will be better understood by those affected if it is made directly instead of through the average monthly wage as under the present law.

(d) *Minimum benefit.*—If most noncovered occupations are brought under the act, the minimum primary benefit should be raised from \$10 to \$25. With the proposed changes in benefit structure, few persons in covered employment would earn a benefit of less than \$25.

(e) *Maximum benefit.*—The present ceiling on family benefits should be increased from \$85 to \$150. The limitation of 80 percent of average monthly wage

should be retained but the limitation of twice the primary benefit unduly restricts benefits to survivors and should be eliminated.

(f) *Maximum wage base.*—The \$3,000 limit on wages credited for benefits should be raised to \$4,800. The \$3,000 limitation, established in 1939, permitted the inclusion of the total annual wages of 97 percent of all covered workers. A wage base of \$4,800 is needed to include total annual wages of about the same proportion of all covered workers.

(g) *Liberalization of benefits for children.*—The payment for the first child in a family should be raised from 50 percent to 75 percent of the primary benefit.

Qualifying conditions.—The requirements now imposed for qualification for benefits also should be revised.

(a) *Insured status.*—Existing insured status requirements (1 quarter of coverage for each 2 elapsed quarters after 1936 or age 21 and before age 65 or death) would be too severe on newly covered workers, even if they had a few previous quarters of coverage. It would be better to reduce the required quarters of coverage to 1 for each 4 instead of for each 2 elapsed quarters.

(b) *Qualifying age for women.*—In only about one-fifth of the cases can a wife now become entitled to monthly benefits at the same time her husband reaches age 65 and is first eligible for his primary benefits, although both benefits may be needed for their support. This is because wives are usually younger than their husbands. If the qualifying age for wives was lowered to 60, both the husband and wife would become eligible for benefits when he is 65 in about three-fifths of the cases. As a matter of equity, all women beneficiaries should have the same qualifying age as wives.

Retirement test.—In view of present wage levels, the limit of \$14.99 which may be earned by a beneficiary in covered employment without suspension of benefits is inadequate; it should be increased to \$50.

Lump-sum death payment.—Lump sums should be payable on the account of an insured worker whether or not he has a survivor who is immediately entitled to benefits. The extra expense at death imposes as great a burden on those who draw monthly benefits as on those who do not. If primary benefits are increased, the lump-sum payment could be reduced from six to three times the primary insurance benefit.

Employees of nonprofit organizations.—Service performed for religious, educational, charitable, and similar nonprofit organizations should be included under the insurance plan.

I believe that compulsory insurance coverage would not endanger the tax-exempt status accorded to these organizations. Specific provisions affirming this status could be included in the legislation. Coverage for employees of these institutions should not be contingent on election by their employers. Any plan that provides elective coverage would be both administratively and actuarially unsound, and in addition would be unfair to those employees whose employers did not elect coverage.

In the event that it is believed desirable public policy not to require nonprofit employers to pay their share of the old-age and survivors insurance contribution, provision could be made that the employee contribution would be compulsory—thus assuring all nonprofit employees and their families of insurance protection. The payment of the employer contribution could be made voluntary and wage credits correspondingly reduced if the employer contributions were not paid.

Employer-Employee Relationship

The definition of an "employee" for purposes of social security should be restored to that under which we operated until June 14, 1948, when Public Law 642 was enacted. The repeal of sections 1 and 2 of this law would restore rights under the old-age and survivors insurance system to an estimated total of from 500,000 to 750,000 workers, who are "employees" as a matter of economic reality but not according to the usual common-law rules required by Public Law 642. Many of these are salesmen, taxicab operators, insurance agents, or home workers. Repeal of the resolution is recommended even though the self-employed are covered under the program.

Newly Insured Groups

If these recommendations relative to broad extension of coverage of the old-age and survivors insurance system are enacted into law it will be necessary to adjust the eligibility re-

Table 1.—Old-age insurance benefits payable to retired persons who have been contributing for 12 years

Average monthly wage	Present law		Proposed legislation	
	Single person aged 65 and over	Couple aged 65 and over	Single person aged 65 and over	Man aged 65 and over, and wife aged 60 and over
\$100.....	\$28.00	\$42.00	\$46.20	\$69.30
200.....	39.20	58.80	63.00	94.50
300.....	44.80	67.20	79.80	119.70
400.....	44.80	67.20	96.60	144.90

quirements and the method for determining the average monthly wage upon which benefits are based so that the newly insured groups will not be unduly disadvantaged because of their late entrance into the system. As the law now stands a person who has not been working in insured employment for roughly one-half the time since the law went into effect on January 1, 1937 (or one-half the time since the date he became 21 years of age, if that date is later) is not fully insured and therefore not entitled to an old-age retirement benefit. Therefore, it would take a farmer who had never worked in insured employment previously and who attained age 60 this year about 8½ years before he could qualify for an old-age retirement benefit. Since 12 years have already elapsed, his average monthly wage would be less than half the average income he would earn during his period of coverage because his earnings would be averaged over the whole period after January 1, 1937, and until he is insured—a period of about 20 years.

To make it possible for newly covered workers to become eligible for insurance benefits within a reasonable period of time the provision of the existing law should be changed to permit a person to be deemed insured if he had covered wages in 1 out of each of the 4 quarters elapsing since 1936 or since age 21. Anyone who had 40 quarters would, of course, continue to be fully insured. The 1-out-of-4 provision would permit newly covered workers to be treated the same as retired workers will be treated when the insurance system is mature, since under the present law, for the long-run future, a worker will only need to have 10 years of coverage out of approxi-

mately 40 years of his working life. If the Congress were to extend coverage to all of the persons now excluded so that the insurance system would be a truly universal coverage plan then it would be possible to require only the same qualifying period for an older worker as was required when the system began operation in 1937.

Liberalizations in Benefit Amounts

Benefits under existing provisions of the law are not adequate for the basic security which the Nation and the Congress expected would result from old-age and survivors insurance for insured persons and their families. The present level of benefits has been found to be inadequate even at the level of the economy in 1939, when these provisions were enacted. Since then, the cost of living has risen between 70 and 75 percent.

Benefit formula.—The average primary benefit in 1940 was about \$22, or a little above the national average for old-age assistance payments—\$20. However, many beneficiaries had only small resources of their own, and those whose benefits were lowest were most likely to be entirely without other resources. As the cost of living rose, the benefit amount became even less adequate. Today the consumers' price index is more than 70 percent above that in 1939. In spite of the considerable increase in average wages—about 125 percent in manufacturing industries—and the consequent need for higher benefits to replace wages lost by retirement or death, the formula adopted in 1939 has permitted the average benefit to increase only 12 percent, to about \$25. The average old-age assistance payment, in contrast, is \$42.

Some 10 percent of the insurance beneficiaries have to have public assistance, and many more rely on help

Table 2.—Survivors insurance benefits payable to a widow and two children, assuming 12 years of insurance coverage

Average monthly wage	Present law	Proposed legislation
\$100.....	\$49.00	\$80.00
200.....	68.60	126.00
300.....	78.40	150.00
400.....	78.40	150.00

from relatives. Obviously the insurance benefits are inadequate to provide even what the Nation as a whole regards as essential for people in need, and such benefits cannot successfully prevent dependency in a large percent of cases. Therefore, the present formula should be changed to 50 percent of the first \$75 (instead of 40 percent of the first \$50)

of the average monthly wage plus 15 percent (instead of 10 percent) of the remainder.

Maximum wage base.—Another important change which should be made is to permit the average monthly wage to be as high as \$400 per month. This would be the result if the taxable wage base were increased to \$4,800 instead of \$3,000.

In 1939, about 97 percent of all covered workers received wages below \$3,000. At today's wage levels, \$4,800 would include the total wages of about 96 percent of the workers. Thus, this proposed change is necessary to give workers the same degree of protection against wage loss that they were accorded in 1939. If the wage base is not raised, the differential between benefits for low-wage and high-wage workers will not adequately represent their differences in levels of living and the benefit structure will tend more toward a flat level.

Calculation of average monthly wage.—Benefits are based on the worker's wages from covered employment averaged over all months after 1936 (or his later attainment of age 21), whether or not he had covered wages in all such months.

The purpose of basing benefits on such an average monthly wage was to permit benefits to be related to a worker's usual earnings even though he retired within a few years after the program began, without permitting excessive payments to persons who will retire many years hence. At the same time, the average monthly wage, and hence the benefit amount, was reduced for persons who moved in and out of covered employment, whether on account of noncovered employment, unemployment, or disability. This method of calculating the average wage has been criticized for several reasons.

First, while most persons recognize the justice of higher benefits for persons who pay contributions regularly than for those who work some of the time outside the program, the concept of an "average" wage lower than that which the worker ordinarily is paid is difficult to understand.

Second, any periods of disability which the individual suffers should not reduce his average monthly wage or benefit amount, even though periods when an individual was not in the labor force or was working in noncovered employment should result in lower benefits based on his covered employment.

Third, an "average monthly wage" figured over an individual's entire working lifetime, as the present formula will require in the long run, will not be representative of his wage loss

Coverage of the Self-Employed Under Old-Age, Survivors, and Permanent Disability Insurance

Present status.—The majority of self-employed persons (farmers, small-business men, professional persons) are just as much in need of old-age, survivors, and disability insurance protection as are wage earners. A number of social insurance programs in foreign countries now cover the self-employed. Under our present program, many self-employed persons now pay contributions on behalf of their employees who are covered, and so are very conscious of their own exclusion. The owner of a business large enough to be incorporated acquires protection as an officer of the corporation, but the owner of a small unincorporated concern has no similar advantage. Moreover, many self-employed persons work at times as wage earners but fail to build up and maintain an insured status because their income from self-employment is not credited toward such status. Experience gained in the administration of the income-tax law has made it possible to develop adequate methods of meeting the problems involved in coverage of the self-employed.

Reporting.—Contributions and benefits would be based on income from self-employment. For both the self-employed person and the Government, the simplest way of reporting such income is as part of the income-tax return. Social security reporting would be required only from persons whose annual gross income is \$500 or more (exclusive of income in kind for home use) and whose "net income from self-employment" is \$200 or more. Consistent with the provisions for employees, the maximum annual net income from self-employment on which contributions would be payable would be \$4,800, less the amount of any wages received during that year from other covered employment.

Contribution rate.—Various suggestions have been made for determining the contribution rate for the self-employed. The self-employed could be required to pay only the employee rate or the combined employee and employer rate. Taking into account the nondeductibility of the self-employed person's contribution under the income tax, the inability to exclude all investment income from the contribution base, and the likelihood of later retirement, a rate of $1\frac{1}{2}$ times the employee rate (excluding temporary disability) is recommended. If the employee rate is set at $1\frac{1}{2}$ percent of pay roll, then the self-employed rate would be $2\frac{1}{4}$ percent of his net income.

Net income from self-employment.—Net income from self-employment would be determined entirely on the basis of two figures already included in the income-tax return, namely, income from business or profession (schedule C) and income from partnerships (schedule E).

Retirement test.—One month's benefit would be withheld for each month during which a beneficiary engaged in any self-employment activities resulting in net earnings of more than \$50.

at death or retirement. It will include the low wages when he was learning his trade or business. Also, since there is a long-term upward trend of wages, it will fail to remain reasonably representative of current wage levels. It seems better to base benefits on the average wages a worker has during a reasonably limited period when he was working fairly regularly at his most developed skill and hence earning his best wages. Ordinarily, such a period would be toward the latter part, although not necessarily the end, of his working lifetime and benefits based on it would fairly represent the general wage level when he retires.

A change in the present method of figuring the average monthly wage will, of course, be necessary when the act is extended to cover a number of occupations heretofore excluded. Otherwise, the employees in such occupations would for many years have a very low average monthly wage and would probably receive very small benefits. Averaging wages over a limited period such as the individual's best 5 years rather than all years since 1936 would prevent undue hardship to the newly covered workers and improve the benefit structure generally.

Increase in benefit amounts for continuous employment.—Because the average monthly wage is reduced by any months since 1936 when an individual had no covered wages, benefits are larger for workers who are in covered employment all their working lives than for persons in such occupations for proportionately less time. Even when coverage is broadly extended, some provision is needed to assure substantially larger benefits to those persons who work continuously than for others, like women who leave the labor force upon marriage, who become eligible for benefits but have not engaged continuously in covered employment. Otherwise, the unduly large benefits of persons irregularly in covered employment, or even irregularly in the labor force, will be largely financed by regularly covered workers and their employers. If such variation is made directly in the benefit amount, rather than in the average monthly wage, those affected would understand it better.

Minimum benefits.—If most occupations now excluded are covered, as

proposed, the minimum primary insurance benefit should be increased. The present amount, \$10, does not represent even the minimum economic security intended in 1939, when the figure was set. If the proposed revisions in coverage, benefit formula, and method of computing the average monthly wage are enacted, the minimum benefit could be established at \$25 without exceeding the computed benefits of the majority of those who customarily support themselves.

Maximum benefits.—Under existing provisions, family benefits may not exceed \$85 a month, twice the amount of the worker's primary benefit, or 80 percent of the average monthly wage, whichever is least. If a \$4,800 wage base is used, a higher dollar maximum, such as \$150, is needed to permit a man with a high average wage and his wife to draw the full amount of their benefits when the man has been in covered employment for a fairly long period. The requirement that benefits may not exceed twice the amount of the primary benefit is unduly restrictive on survivor families at the middle income levels which include most insured workers' wages. Therefore, it is recommended that this particular requirement be eliminated, but that the other two be retained.

Qualifying Age for Women

Women should be eligible for benefits at age 60. Wives are generally a few years younger than their husbands. Requiring a wife to be aged 65 before her benefits can be paid means that only about one-fifth of the married men who retire at age 65 have wives immediately eligible for wife's benefits. Some families must, therefore, live on very inadequate benefits for several years until the wife is eligible for benefits. If women were permitted to draw benefits at age 60, about three-fifths of the married men would have wives immediately eligible for wife's benefits when the men attain age 65. Furthermore, a widow between ages 60 and 65 could also draw benefits immediately. Women workers themselves, as a matter of equity, should also be eligible for primary insurance benefits at age 60.

Retirement Test

Benefits are not paid for any month in which a beneficiary earns more

than \$14.99 in covered employment. Although benefits are intended for workers who have retired from substantial employment, beneficiaries should be permitted to do some part-time work, paying up to about \$50 a month, without loss of benefits.

Lump-Sum Death Payment

Such payments may now be made only if the insured worker leaves no survivor who could immediately become entitled to monthly benefits. The extra expenses of death impose as great a burden on those who draw monthly benefits as on those who do not. The lump sum should be payable upon the death of any insured worker, irrespective of the payment of monthly benefits. On the other hand, since the primary insurance benefit would be increased, the lump-sum payment might well be three times rather than six times the primary insurance benefit.

Disability Benefits

Our existing social insurance program provides some protection against wage loss due to unemployment, old age, and death. But we have provided no social security against a hazard which is equally, sometimes even more, disastrous to a family—the temporary sickness or injury which keeps the wage earner off his job for weeks or months, or the more serious disability which incapacitates him for a longer period—perhaps for the rest of his life.

Every day nearly 4 million men and women of working age are suffering from some disabling condition. Over 2 million of them have been disabled for 6 months or longer. To the wage earner who is unable to work and to his family, which depends on his earnings, the loss of income has the same social and economic impact whether it is caused by labor-market upheaval or physical incapacity.

Temporary disability caused by illness or injury and extended disability resulting from accident or chronic disease are economic risks against which most workers find it virtually impossible to budget on an individual basis. To most workers the cost of private disability insurance is prohibitive; comparatively few have the pro-

Disability Insurance Benefits Under Old-Age and Survivors Insurance

Need for disability protection.—Each day about 2 million persons recently in the labor force are kept from working by disability which has lasted less than 6 months, and 2 million or more persons aged 14 to 64, who otherwise would be gainfully employed, are affected with serious disabilities which have continued for more than 6 months. While it exists, disability may be economically more disastrous for a worker and his family than unemployment, death, or forced retirement. The fact that the incidence of disability is reasonably predictable in the aggregate—although not individually—makes it an insurable risk and one which, like old age and death, can be effectively met through contributory social insurance.

Temporary disability insurance.—Employees with fairly recent attachment to the labor market who are disabled for 7 consecutive days or longer by reason of illness or injury should receive cash benefits to partially replace their lost earnings. These temporary disability benefits would be payable if the disabled individual cannot engage in his usual, most recent, or reasonably similar work.

The weekly benefit amount is designed to tide the worker and his family over relatively brief periods of sickness. During short illnesses, most regular living expenses cannot be deferred or substantially reduced, and benefits ought to be geared, therefore, to the individual's recent wages and the number of his dependents. For a single individual, weekly benefits might approximate 50 percent of recent full-time wages up to a maximum of around \$30 a week and, with an additional allowance for dependents, the maximum for an individual with three or more dependents should be \$45 a week. The payment would continue for a maximum of 26 weeks of sickness.

Extended disability insurance.—Monthly cash benefits should be payable to insured workers who are afflicted with serious disablements when these have lasted more than 6 consecutive months. Such extended disability benefits should be payable only if the worker is found incapable of engaging in any substantially gainful work.

To receive benefits, a disabled worker should have extensive, as well as fairly recent, covered employment. Benefits would, of course, be terminated if recovery occurred, and beneficiaries would be required to undergo periodic examinations to determine whether disability still exists.

Benefits should be payable regardless of age, and the total of benefits payable in any one case should be in relation to the number of the disabled worker's dependents. More than half the cases of protracted disability occur at younger ages when the worker has heavy family responsibilities and has not had an opportunity to build up savings or insurance. The disabled worker and his wife and children could receive monthly benefits computed in the same way as the

benefits of an aged, retired worker and his dependents. It also would seem reasonable that an aged disabled husband or widower, if he is the dependent of a woman worker, should have the same type of protection as the dependents of a male worker.

Protection of insured status.—Under the existing program, a period of prolonged unemployment due to disability may cause the complete loss of a worker's insurance protection. If benefits for extended disability are added, the worker's insurance protection for subsequent retirement or death benefits could be maintained during a period of disability.

Rehabilitation and work.—Many persons formerly considered "permanently and totally" disabled can be rehabilitated to again become self-supporting, productive workers. Insurance funds should be used to rehabilitate disabled workers where it appears that they can be returned to employment. If a disabled person is able in a month to earn more than \$50 he ordinarily should not receive benefits for that month. While actually engaged in a program of rehabilitation, however, he should be given special encouragement to try out his skills and attempt to return to substantially gainful work.

Integrated administration of disability insurance and old-age and survivors insurance.—Decided operating advantages would arise from the integration of old-age and survivors insurance with short-term and extended disability insurance. The existing facilities of the Bureau of Old-Age and Survivors Insurance, including the wage-record system and the field organization, would be available for the administration of disability benefits. Employers would keep one set of records; they would prepare a single wage report covering old-age, survivors, and disability insurance. Contributions would go into a single trust fund, thus providing greater flexibility in financing costs. The public would go to a single field office for all questions on earnings records, for filing death, retirement, and disability claims, and for general information. Facts established for one type of benefit, such as marriage or age, would be on record for use in subsequent claims for other types of benefits.

By using the same administrative machinery for short-term and extended disability a single medical case history could be used for both types of benefits. Overlapping of official medical examinations would be avoided, and the number of physicians and administrative personnel required would be kept at a minimum. The administration of rehabilitation services also would be facilitated. The effectiveness of rehabilitation is conditioned to a large degree upon its being started promptly. Since close contact would be maintained with disabled individuals while they were receiving short-term disability benefits, an early determination could be made as to whether and when rehabilitation should be undertaken.

Financing an Expanded Old-Age, Survivors, and Disability Insurance Program

Strengthening the actuarial basis of the program.—The recommendations for changes in coverage would strengthen the actuarial basis of the program, both in the immediate future and in the long run. Income from contributions would be increased while at the same time the relative cost of insurance benefits paid to the group of individuals who move between uninsured and insured employments would be reduced.

Long-run financial plans essential.—A long-range plan should be developed to assure ample funds to finance benefit disbursements not only in the years just ahead but in the more distant future, without necessitating abrupt changes in premium rates. The contribution rates in the present law are as follows: 1 percent each for employers and employees during 1949; 1½ percent each in 1950 and 1951; and 2 percent each for 1952 and thereafter.

Division of costs.—With practically complete coverage, an eventual Government contribution toward financing the program becomes equitable and appropriate. Such a contribution would be offset by the reduced Federal costs for public assistance if coverage is extended and disability benefits are included. Distribution of the ultimate cost of these benefits among employers, employees, and the Government should be governed by the degree to which coverage is extended and the method of financing other types of social insurance benefits.

Cost of present old-age and survivors insurance program.—If the 1939 estimates of the cost of the present law are adjusted to allow only 2-percent interest on reserves (the rate which is now used in making estimates) instead of 3 percent (the rate that was used in making estimates in 1939), the level premium cost from 1950 on is from about 6 percent to 9 percent of pay rolls and the intermediate figure would be about 7½ percent of pay rolls. The 1939 estimates are now out of date because of the great increase in wages and number of workers employed. Present estimates of the expanded program based upon present wages and level of employment will also turn out to be too high if wages and employment continue to increase as they have in the past.

Taking into account the changes that have taken place since 1939, the latest actuarial estimates in-

dicate that the level premium cost of the present law is somewhere between 3.3 percent to 5.7 percent of pay rolls or about 4.5 percent if we take an intermediate figure.

Cost of expanded old-age, survivors, and extended disability insurance program.—The level premium cost of the expanded program, based substantially on present employment and wage levels, is about 5.6 to 9.2 percent of pay roll, or an intermediate figure of around 7.4 percent. Thus, the cost of the expanded program is about the same as the level premium cost of the 1939 act based on 1939 assumptions (with the exception of the change in interest rate).

Our history indicates that the level of income and earnings in the future will be above that now prevailing. If the cost estimates are amended to take account of the long-term tendency for wages to increase, the intermediate level premium cost would be lowered from 7.4 percent to about 6 percent.

It is significant to note that the level premium cost of the present railroad retirement program is estimated at 13.6 percent of pay rolls, utilizing the 3-percent interest rate specified in the railroad law. For purposes of comparability with old-age and survivors insurance estimates which utilize a 2-percent rate the level premium cost of the railroad program would be about 15 percent of pay rolls.

Cost of temporary disability insurance.—It is estimated that a national system of temporary disability insurance—providing benefits, after a waiting period of 7 consecutive days, for up to 26 weeks during a benefit year—is likely to cost about 1 percent of covered pay rolls. This amount would be sufficient to provide benefits averaging with dependents' benefits about 50 percent of covered wages. Other specifications of the system assumed in this cost estimate are that the eligibility requirements include a test of recent attachment to the labor force; that there be adequate safeguards in claims administration, particularly as regards the requirement for medical certification of disability; and that temporary disability insurance would be administered as part of the national system of old-age, survivors, and disability insurance. By using the same wage records and field offices, administrative costs would be minimized.

tection offered by existing Federal and State retirement programs and other benefit systems. For these reasons disability continues to be a major cause of dependency.

In June 1948, 83,000 persons were receiving aid to the blind throughout the United States; and the families of about 90,000 incapacitated workers were receiving aid to dependent children. Of the more than a million

children receiving such aid, one-third were from families where one or both parents were incapacitated. Many of those on the assistance rolls have become destitute because disability forced them to stop work and use up all of their personal savings. Clearly, the cost of dependency is a heavy drain on the public purse; disability causes much of this dependency.

A program of social security falls

short of its basic purpose if it fails to protect workers and their families against the risk of disability. The best way to provide this basic protection in a manner consistent with the traditional American concept of dignity and self-respect is by a contributory social insurance program. Disability, like other economic risks, cannot reasonably be predicted on an individual basis; but in the aggregate

it is a predictable, insurable risk. Under a broad contributory social insurance system this necessary protection can be provided at a cost well within the reach of every worker.

For all insured wage earners and self-employed persons who have been disabled for 6 months or longer and cannot engage in any substantially gainful work, monthly benefits should be payable, beginning after a 6-month waiting period. These extended disability benefits should be comparable to the benefits payable upon retirement. For eligible wage earners only—to tide them over the first 6 months of disability—weekly disability payments should be payable. Only those whose earnings show regular attachment to the labor force should be eligible for benefits in either case—and only if their disability is medically demonstrable.

Disability insurance is part of the social insurance systems in practically all countries, and its administrative feasibility has been proved beyond question. This view has been recently affirmed by the Senate Advisory Council on Social Security in its recommendations for establishment of a permanent and total disability insurance program. In the United States we have had considerable experience with disability programs. The various special public retirement systems, the program for railroad workers, the veterans' program, workmen's compensation, the State cash sickness insurance programs, and commercial insurance have provided valuable sources of information and experience in planning a national program of disability insurance. Some of those who question the practicability of such a national program in this country are concerned over the fact that a number of private insurance companies discontinued writing disability contracts after unfavorable experience with them during the depression years. On that point we agree with the Senate Advisory Council, which said: "In our opinion, that experience is important but not conclusive."

The present old-age and survivors insurance system is already full geared to large-scale payment of benefits similar to those proposed for disability. The wage records system, the network of field offices, and other administrative facilities necessary for adminis-

tering a disability program would be largely the same as those for the retirement and survivors program. Thus, existing administrative machinery could be adapted with minimum effort and expense to payment of the new benefits.

The programs for both temporary and extended disability benefits should be integrated with the old-age and survivors insurance system.

The advantages to claimants, to doctors, and to the public generally in having only one field office to look to locally for information and action on old-age, survivors, or any form of disability benefits are obvious. Administrative savings to be obtained from such an integrated program would alone be sufficient reason for selecting full integration as the most desirable course.

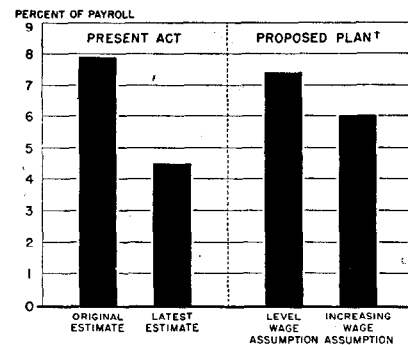
Three States—Rhode Island, California, and New Jersey—now have temporary disability programs. Our study of the operations of these and other programs has convinced us that a program of temporary disability benefits fits into a comprehensive insurance system embracing retirement, survivors, and disability insurance. Experience has shown that the two programs of temporary disability and unemployment insurance are so different as to require almost separate administration, with separate policies, separate procedures, and separate administrative staffs.

One of the major objectives of a program of disability insurance would be to finance the rehabilitation of disabled persons for return to gainful employment. Rehabilitation would be accomplished largely through existing State and local facilities. Our experience in administering the retirement and survivors program has demonstrated that much of the case development and incidental operations can be successfully decentralized to local offices. We expect that the opportunities for local operation would be even greater with a disability program.

Cost of Present Old-Age and Survivors Insurance Program

If the 1939 estimates of the cost of the present law are adjusted to allow only 2-percent interest on reserves

Chart 3.—Level premium cost¹ of proposed plan compared with that under present act (intermediate estimate²)



¹ Contribution rate beginning in 1950 that would make the insurance benefits self-supporting (from contributions and 2-percent interest thereon) from that year on.

² Average of low and high cost estimates as shown in Actuarial Study No. 28 (Division of the Actuary, Social Security Administration).

[†] Includes old-age, survivors, and extended disability benefits of H. R. 2893 but excludes weekly disability benefits.

(the rate which is now used in making estimates) instead of 3 percent, the rate that was used in making estimates in 1939, the level premium cost from 1950 on is from about 6 to 9 percent of pay rolls, with the intermediate figure about 7½ percent. Of course, these 1939 estimates are now out of date because of the great increase in wages and number of workers employed. Estimates of the expanded program based upon present wages and level of employment would also turn out to be too high if wages and employment continue to increase at the same rate as they have in the past.

Taking into account the changes that have taken place since 1939, the latest actuarial estimates indicate that the level premium cost of the present law is somewhere between 3.3 and 5.7 percent of pay rolls, or about 4.5 percent if we take an intermediate figure.

Cost of Expanded Old-Age, Survivors, and Extended Disability Insurance Program

The level premium cost of the expanded program, based substantially on present levels of employment and wages, is about 5.6 to 9.2 percent of pay rolls, or an intermediate figure of around 7.4 percent. Thus, the cost of the expanded program is about the same as the level premium cost of the

1939 act based on 1939 assumptions (with the exception of the change in interest rate).

Of course, actuarial estimates must be presented within a wide range since no one can predict accurately for several decades in the future economic conditions, mortality rates, population growth, retirement rates, and many other such factors upon which actuarial estimates must be based.

One fact is clear, however. As an individual's wages increase, he always receives a larger benefit but this benefit represents a smaller proportion of his wages. This is because the present old-age and survivors insurance law provides for the payment of primary benefits of 40 percent of the first \$50 in average monthly wages and 10 percent of the remaining amount up to \$200 additional. For instance, the individual receiving an average wage of \$100 per month receives basic old-age insurance benefit of \$25 per month or 25 percent of his average wage; the \$250-per-month individual receives \$40 per month, which represents 16 percent of his average wage. Thus, as the average wage of insured persons increases, the relative costs of the present benefits measured as a percentage of pay roll will decrease.

At the present time the average wage of persons contributing to the insurance system is substantially

higher than the average wages assumed in making the actuarial cost estimates in 1939. This single factor has resulted in a great reduction in the relative costs of the insurance plan. In calculating the costs of the proposals I have presented, it must be borne in mind that extension of coverage would result in including all the wages of many individuals who are already under the insurance system part of the time. This would increase their taxable wages and reduce the relative cost of the insurance plan.

The figure for the expanded program is predicated on the maintenance of existing wage levels over the next 40 or 50 years. However, our history indicates that the level of income and earnings in the future will be above that now prevailing. If the cost estimates of the present benefit provisions are amended to take account of the long-term tendency for wages to increase, the intermediate level premium cost of the expanded program (excluding temporary disability) would be lowered from 7.4 percent to about 6 percent, taking the intermediate figure for purposes of comparison.

In this connection it is significant to note that the level premium cost of the present railroad retirement program is estimated at 13.6 percent of pay rolls utilizing the 3-percent in-

terest rate specified in the railroad law. If an interest rate of 2 percent were used, to put the estimates on a basis comparable to that for old-age and survivors insurance, the level premium cost of the railroad program would be about 15 percent of pay rolls.

Cost of Temporary Disability Insurance

It is estimated that a national system of temporary disability insurance—providing benefits, after a waiting period of 7 consecutive days, for up to 26 weeks during a benefit year—is likely to cost about 1 percent of covered pay rolls. This amount would be sufficient to provide benefits averaging about 50 percent of covered wages, and representing higher proportions of earnings for the lower-paid workers and for workers with dependents. Other specifications of the system assumed in this cost estimate are that the eligibility requirements include a test of fairly recent attachment to the labor force; that there be adequate safeguards in claims administration, particularly as regards the requirement for medical certification of disability; and that temporary disability insurance would be administered as part of the national system of old-age, survivors, and disability insurance. Use of the same wage records and field offices would minimize administrative costs.

TEMPORARY DISABILITY

(Continued from page 2)

insurance system, both being administered by the Employment Security Department. Disability benefits under the State plan are the same as unemployment benefits in the same uniform benefit year, \$10-25 a week and \$150-650 in a year. Benefits under private plans must be as great as those under the State plan. Benefits are payable to individuals who are unable to perform their regular or customary work because of illness or injury, but they are not payable for illness arising from pregnancy unless the illness lasts more than 4 weeks after the termination of pregnancy.

New York's disability law is not related to the unemployment insurance law. The program is to be admin-

istered by the Workmen's Compensation Board along the same lines as workmen's compensation, with private insurance companies and the State fund competing. A special State fund is established to pay benefits to the "disabled unemployed." It is to be financed by equal employer and employee contributions of 0.1 percent of wages paid during the period January-June 1950, and thereafter by assessments against the carriers authorized to pay benefits under the act. To finance benefits for disability during employment, contributions are scheduled to begin July 1, 1950, with employees paying contributions representing 0.5 percent of wages up to 30 cents a week, and employers paying the "excess cost of benefits."

Benefits, which begin in July 1950, are payable at the rate of one-half the average weekly wage, and duration

is limited to 13 weeks in any 52 consecutive calendar weeks. The maximum weekly payment is \$26, and the minimum is \$10 or the average weekly wage, if less than \$10. Benefits are payable to an individual who is unable to perform the regular duties of his employment or any employment for which he is reasonably qualified by training and experience. Benefits are not payable for illness arising from pregnancy unless the illness occurs after the employee has returned to work for a covered employer for 2 consecutive weeks after termination of the pregnancy.

Enactment of these two statutes means that more than 27 percent of the workers covered under unemployment insurance laws, as estimated for 1946, will have some measure of protection under State laws against non-occupational disability.