Statement of Eric Kingson[1]
Professor, Syracuse University School of Social Work
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before the
United States Senate Committee on Health, Education, Labor and Pensions
Subcommittee on Primary Health and Aging
Hearing on "The Recession and Older Americans: Where Do We Go From Here?"

Tuesday, October 18, 2011

Chairman Sanders, Ranking Member Paul and other distinguished members of the Senate Committee on Health, Education, Labor and Pensions Subcommittee on Primary Health and Aging, as you know well, the recession has destabilized the finances of many retirees and people nearing retirement as well as the economic prospects of younger working persons. Thus, it is important that you have chosen to examine how Older Americans are faring in these very difficult times, and it is an honor to appear before your panel.

My name is Eric Kingson. I am a professor at the Syracuse University School of Social Work. My scholarship and research address the political and economic consequences of population aging. Previously, I directed a study for the Gerontological Society of America in 1984-5 which examined various ways of framing policy discussion about the aging of America, and I served as an advisor to the 1982-3 National Commission on Social Security Reform and to the 1994 Bipartisan Commission on Entitlement and Tax Reform. I also co-direct Social Security Works and co-chair the Strengthen Social Security Campaign (www.strengthensocialsecurity.org). To summarize my main points:

- Nothing provides the surety of protection afforded by Social Security, the single most important source of income for the overwhelming majority of retirees.

- Former presidents, beginning with Richard Nixon, and former congresses were wise to establish and maintain Social Security's automatic Cost-of-Living-Adjustment (COLA).

- The CPI-W, currently used to calculate the COLA, does not fully take into account the impact of rising health care costs on Older Americans (and persons with severe work disabilities and survivors). It falls short of assuring that Social Security benefits maintain purchasing power, no matter how long a retiree, disabled worker or survivor lives.

- The alternative "Chained-CPI" doesn't pass the "smell test" and would cut benefits of all retirees, survivors, and persons with severe work disabilities, a clear violation of promises made to Social Security beneficiaries and persons nearing retirement.

- The Consumer Price Index for the Elderly (CPI-E) for Americans 62 and older, an index whose development was mandated by the 1987 Amendments to the Older Americans

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Act, does a better job of maintaining the purchasing power of benefits because it takes into account the disproportionate and rising cost of health care for the old and disabled.

Which measure Congress chooses matters greatly to the lives of everyday Americans. Consider for a moment what a choice of indexes would mean for Jane Smith, a hypothetical never-married woman described in Appendix A who worked for 40 years as legal secretary at a salary that was roughly equivalent to the average earner in the U.S. economy (e.g., about $43,000 in 2010). She begins with a yearly Social Security benefit of $15,132.

- Assuming current law (i.e. the CPI-W) correctly measures the impact of inflation of retirees, the purchasing power of her benefits will remain the same, no matter how long she lives, $15,132 in 2011 dollars.

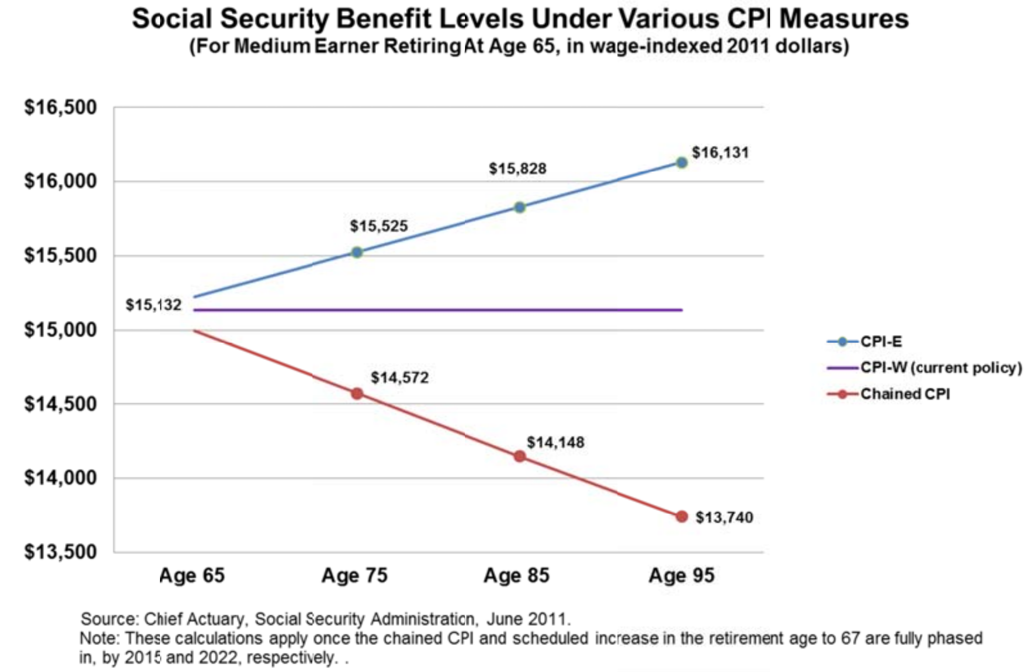
- But if the chained-CPI is used to determine COLAs, her annual Social Security benefit would lose $560 in purchasing power (in 2011 dollars) at age 75, $984 at age 85, and $1,392 at age 95, a cumulative loss of $24,019 if she reaches that age.

- On the other hand, if the CPI-E is the more accurate measure, then under current law, the purchasing power of Ms Smith's Social Security benefits will decline by $393 in (in 2011 dollars) at age 75, $798 at age 85, and $999 at age 95.

- And relative to the CPI-E, the chained-CPI would cut her benefits by $953 in (in 2011 dollars) at age 75, $1,688 at age 85, and $2,391 at age 95.

Bottom line, the chained-CPI poses a very significant danger to Ms. Smith, and by extension to all Social Security beneficiaries, now and in the future. It underestimates the impact of inflation on retirees, persons with disability and survivors (see figure 1).

Figure 1



The Importance of Social Security, for Today's and Tomorrow's Retirees

Today's retirees and persons nearing retirement are at great risk. Home equity and stock market losses have taken a large bite out of household assets. Employer-sponsored pensions offer less protection to working Americans. Many persons have reduced or stopped contributions to their retirement funds, and some, facing financial exigencies, are making premature withdrawals from their retirement funds (Brown, 2009). Historically low interest rates have resulted in lower than expected returns on 401Ks and IRAs. The key points to keep in mind are that:

- By far, Social Security is the most important source of income for today's old.
- While today's seniors are more comfortable than older populations of the past, their household incomes are typically modest, and many remain at financial risk.
- There is a great deal of diversity of economic circumstances among older populations, both at any one point in time, and as they age.
- The recession is placing the financial security of today's old and persons nearing traditional retirement ages at increasing risk.

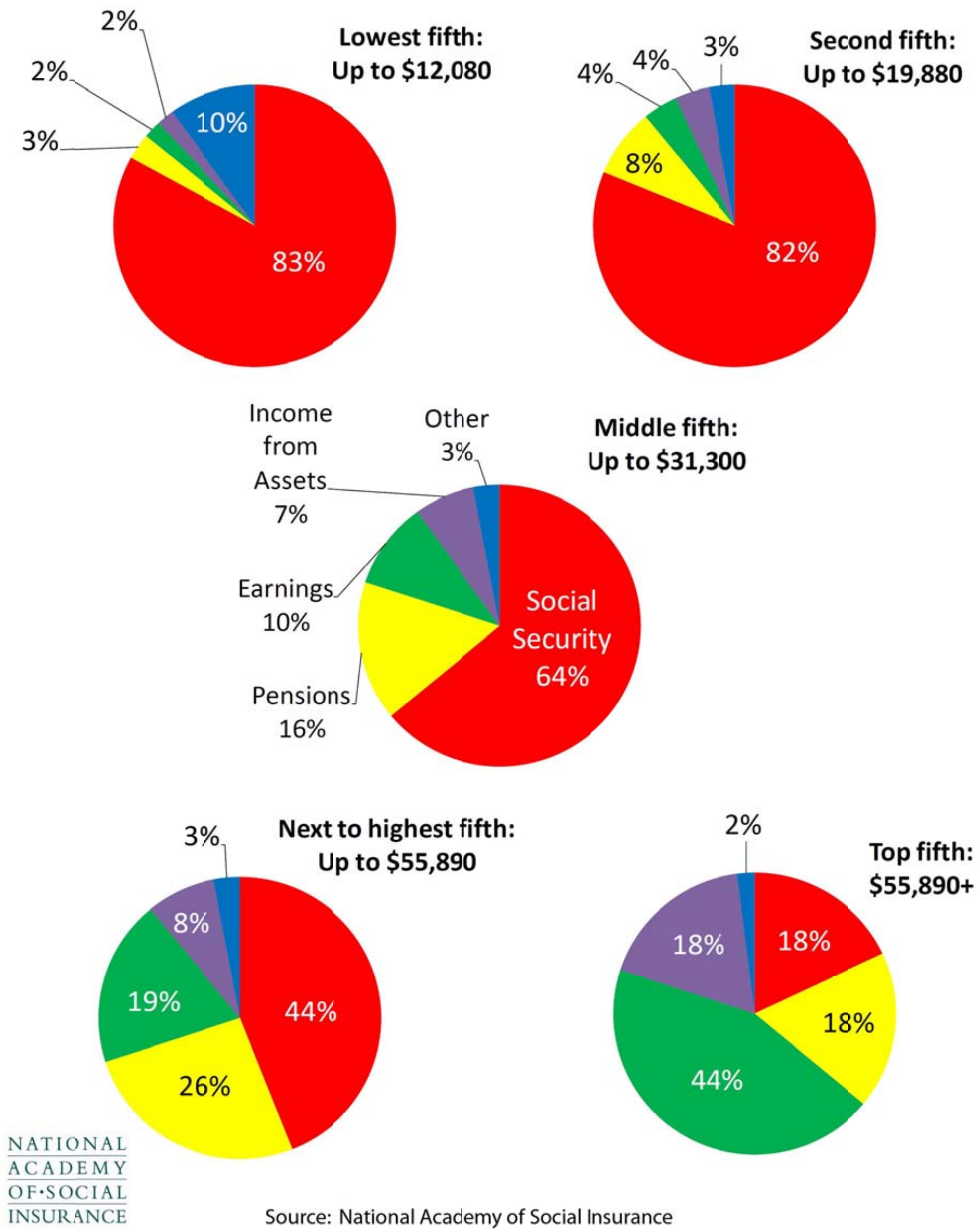
The only pension protection available to six out of ten working persons in the private sector, Social Security is the foundation of the nation's retirement income system. Social Security is the largest single source of income for the overwhelming majority of retirees.

Social Security is the heart of the nation's retirement income system. More than 75 percent of the income going to aged (65 and over) households in the bottom 60 percent of the income distribution – households with less than $31,300 -- comes from Social Security. Only for those in the highest twenty percent of the elderly income distribution (with incomes above $55,890), do occupation pension and assets income equal or, as with earnings, eclipse Social Security in terms of their aggregate contribution to household income. Occupational pensions make significant contributions to the aggregate incomes going to households in the three highest quintiles. Assets income and earnings are not unimportant but with the exception of the highest quintile fall short of Social Security. While not unimportant, the aggregate contribution of cash welfare benefits to the 5.8 million aged households (8.5 percent) with incomes below $12,080 in 2008 Census Bureau, 2011) is substantially less than that of Social Security (83 percent) (see Figure 1).

The economic status of today's older Americans is greatly improved from the days when the Poor House loomed as a major fear of the old. The median income of elderly households was $31,408 in 2010, compared to $56,575 for households 55 to 64 and $62,485 to those 45 to 54. In terms of elderly poverty – defined as individuals aged 65 and over with less than $13,180 and couples with less than $14,953 in 2010 – 3.5 million persons (9%) are defined as poor (Census Bureau, 2011). This is because, as a report recently issued by the Institute for Women's Research notes, Social Security lifts nearly half of elderly persons above the poverty line – 14 million in 2009. One-third of women ages 65–74 are raised above poverty by Social Security, one half of women 75 years and older (Hartmann, Hayes and Drago, 2011).

Figure 2

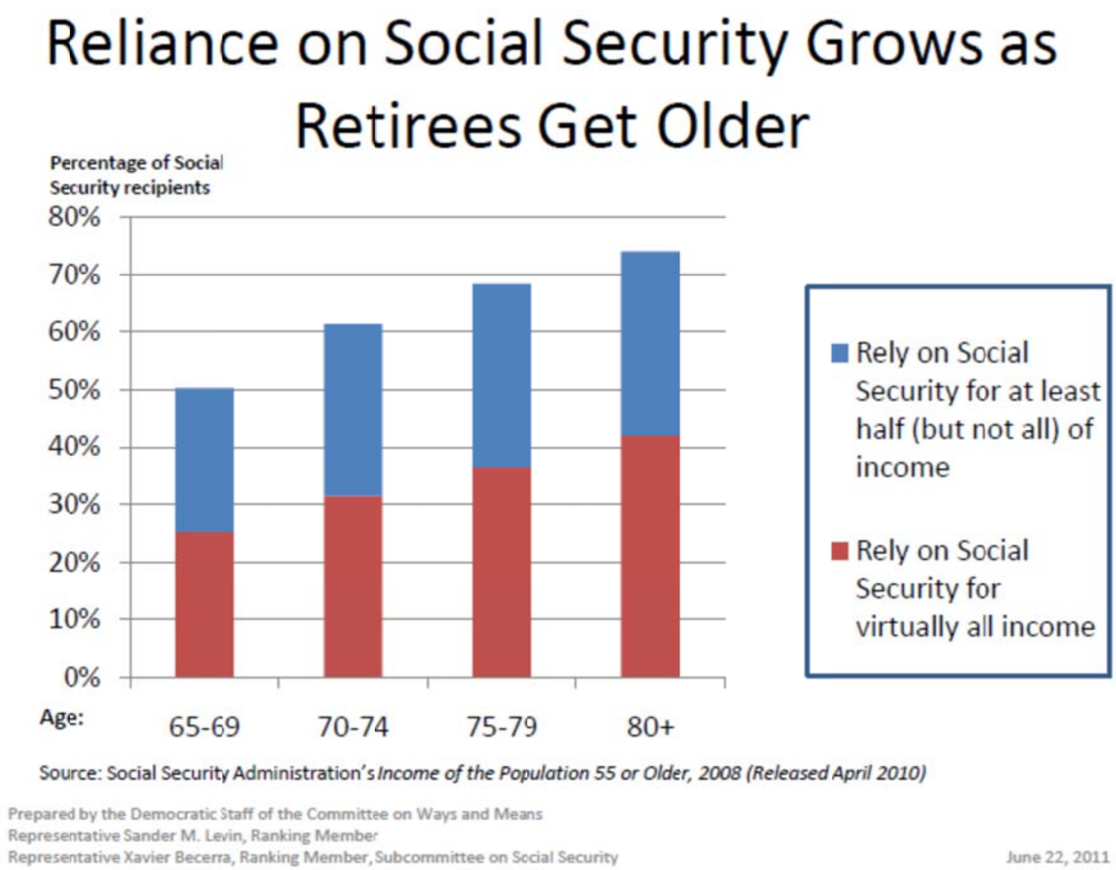
Shares of Income from Specified Sources by Income Level, 2008
Married Couples and Unmarried Persons Age 65 and Older



Source: National Academy of Social Insurance

That the standard of living for elderly households has improved over the past 50 years does not mean that the living standard of the old is excessive or that most older people are without significant financial risk. Especially as they age, develop health problems or lose a spouse, even those in the upper 20 percent of the elderly income distribution (more than $55,890), can deplete their savings quickly and become vulnerable. Indeed, on average, Social Security income becomes significantly more important as a share of household income as individuals and couples get older (see figure 3).

Figure 3



Two other recent reports highlight the economic diversity of older persons as well as the economic diversity across race and Hispanic ethnicity. When poverty data for the old is disaggregated, it shows substantially higher poverty rates among unmarried elders, women and persons of color. For example, 6.8 percent of white alone, non-Hispanic elders have below-poverty incomes in 2010, compared to 18.0 percent of African-American elders, alone and 14.0 percent of Asian alone elders, and 18.0 percent of Hispanic elderly persons of all races (Census Bureau 2011). People of color are also less likely to work for employers with occupational pension coverage, and thus rely more heavily on Social Security than white Americans (Commission to Modernize Social Security 2011).

The employment and retirement income prospects of those nearing retirement, already worrisome before the recession, are more so today. Utilizing its National Retirement Index, a

2008 report from the Retirement Research Center at Boston College estimates that "even if households work to age 65 and annuitize all their financial assets, including the receipts from reverse mortgages on their homes, 44 percent will be 'at risk' of being unable to maintain their standard of living in retirement." That number rises to 61 percent when the anticipated out-of-pocket costs for health and long term care are factored into the assessment (Munnell, Muldoon and Sass, 2009).

While the labor force participation rates of persons 55 and over have increased modestly in recent years and their unemployment rates remain lower than younger workers, "recent BLS data indicate that the average period of unemployment for job seekers aged 55 and over was 40.6 weeks, compared to 31.6 weeks for younger job seekers." Also, "more than half of older job seekers (53.5%) have been out of work for 27 weeks or longer, relative to 41.5% of younger job seekers" (Heidkamp, Corre, Van Horn 2010).

History of Bi-Partisan Support for the COLA

President Richard Nixon signed the automatic COLA into law on July 1, 1972 as a rider to a debt-extension bill. The rider was proposed by Democratic Senator Frank Church and supported by the overwhelming majority of Democratic and Republican members of the House and Senate. On signing the bill, the President highlighted the importance of the COLA, saying:

> This provision is one which I have long urged, and I am pleased that the Congress has at last fulfilled a request which I have been making since the first months of my Administration. This action constitutes a major break-through for older Americans, for it says at last that inflation-proof social security benefits are theirs as a matter of right, and not as something which must be temporarily won over and over again from each succeeding Congress (Social Security Administration).

When the COLA was enacted, the Bureau of Labor Statistics (BLS) only had one measure of inflation, what we now call the CPI-W, or the Consumer Price Index for Urban Wage Earners and Clerical Workers, measuring the inflation experienced by 32% of the population, still used to index Social Security benefits. Today, by law, a "COLA is effective for December of the current year [and] equal to the percentage increase (if any) in the average CPI-W for the third quarter of the current year over the average for the third quarter of the last year in which a COLA became effective" (Social Security Administration, 2011).

In 1978, BLS added the CPI-U, covering about 87% if the population including retirees, and which, today, is used to index income tax brackets. As part of the 1987 Amendments to the Older Americans Act, Congress mandated the BLS to develop an "experimental" index using a market basket of goods and services which more closely tracks the spending of the population ages 62 and over –- the CPI for Elderly Consumers, or, CPI-E. The growth of the various CPI indices was slowed in 1999 by a technical change that took into account the tendency of consumers to substitute within categories, for instance, to buy fewer Macintosh apples and more Delicious apples when Macintosh apples become more expensive relative to Delicious apples (Veghte et. al, 2011). In 1999 the BLS also established an alternative "chained-CPI-U" to take into account how Americans change their spending when they make substitutions across dissimilar categories of goods and services; that is, to account for the tendency to substitute less expensive goods and services, for example, to take vacations by automobile when the cost of airline flights go up (Strengthen Social Security Campaign, 2011).

The last Social Security COLA was 5.8% for 2009, primarily reflecting the spike in oil prices that took place during the 2008 summer. Following that spike, oil and other prices dropped, and so there has been no COLA for the past two years, 2010 and 2011, because the average third quarter CPI-W in 2009 and 2010 did not exceed the 2008 average third quarter CPI-W.

Because oil and other prices have once again begun to rise, this week Social Security is expected to announce the COLA for 2012, thoughts to be in the neighborhood of 3.2 to 3.6 percent.

Because it would make little sense of have a national retirement, disability and survivor pension that results in beneficiaries losing purchasing power the longer they live, the COLA is a critical source of protection for today's beneficiaries, a provision that is valued by the public.

Why the Current CPI Shorts Retirees

The CPI-W understates the impact of inflation on elderly (Bivens, 2011; Vegne et. al., 2011; Goda et. al., 2011) and by extension also on persons with disabilities. One study of people born in 1918 shows that, net of out-of-pocket medical expenses, the average man who retired at age 65 in 1983 and survived to 2007, has seen the value of his Social Security benefit drop by 20 percent, 27 percent for the average woman (Goda et. al, 2011). The existing COLA understates inflation because:

- **The current Social Security automatic COLA, which is based on the CPI-W, simply does not account for the disproportionate impact of health expenditure for households of retirees and persons with disabilities**. In 2009, households with disabled and elderly Medicare beneficiaries spent almost 15% of their budgets out of pocket for health care, roughly three times as much as non-Medicare households (Kaiser Family Foundation, 2011). "Health care costs have been rising faster than prices for other goods and services for over three decades – 5.5 percent per year on average, compared to 3.1 percent for non-medical costs" (BLS, 2011 as referenced in SSSC, 2011). Not surprisingly, health care costs increase with age.

- **Health care expenditures increase as people age, often greatly diminishing disposable income in very old age.** Thus, even if the annual COLA more accurately measured the impact of health care on all the old, there would still be the problem of disproportionate impact on the very old.

- **Medicare Part B and Part D premiums are a growing, relative to the Social Security benefits** of elderly and disabled beneficiaries, except for low-income beneficiaries who are not required to pay these premiums. These premiums are increasing well in excess of Social Security's COLAs, especially for higher income beneficiaries. Individuals with $85,000 and couples with $170,000 of income in 2010) must pay income conditioned Part B premiums ($154.70 to $353.50 per month in 2010) and 35 to 80 percent of the cost of Part D. Because these thresholds are not adjusted for inflation from 2010 to 2019, increasing numbers will be paying larger premiums (Kaiser Health Foundation, 2011). Bottom line, even with an accurate COLA measure, when Medicare premiums are taken into account, the purchasing power of Social Security benefits of seniors and persons with disabilities would not maintain their purchasing power.

Why the Chained-CPI Doesn't Pass the "Smell Test"

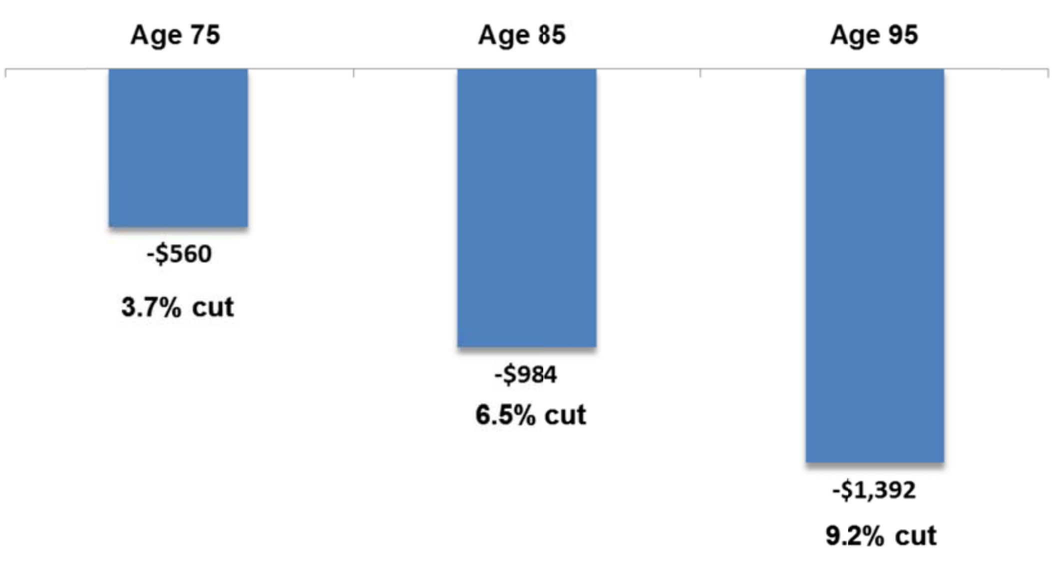
Switching to the chained-CPI has emerged as a proposal in the context of federal deficit reduction talks, especially those now taking place under the jurisdiction of "Super Committee" established under the Budget Control Act of 2011. Proponents argue that it represents a more accurate way of measuring the impact of inflation on older populations. This assertion is just plain wrong.

- **As discussed, the weight of evidence strongly suggests the existing COLA understates inflation**, eroding the purchasing power of Social Security benefits for retirees, survivors and persons with disabilities.

- **The chained-CPI would make the current situation still worse**. Substantial benefit losses would be sustained, especially as people receive benefits over many years (see figures 1 and 4).

Figure 4

Annual Cut in Social Security Benefits Under Chained CPI
(For Medium Earner Retiring At Age 65, in wage-indexed 2011 dollars)



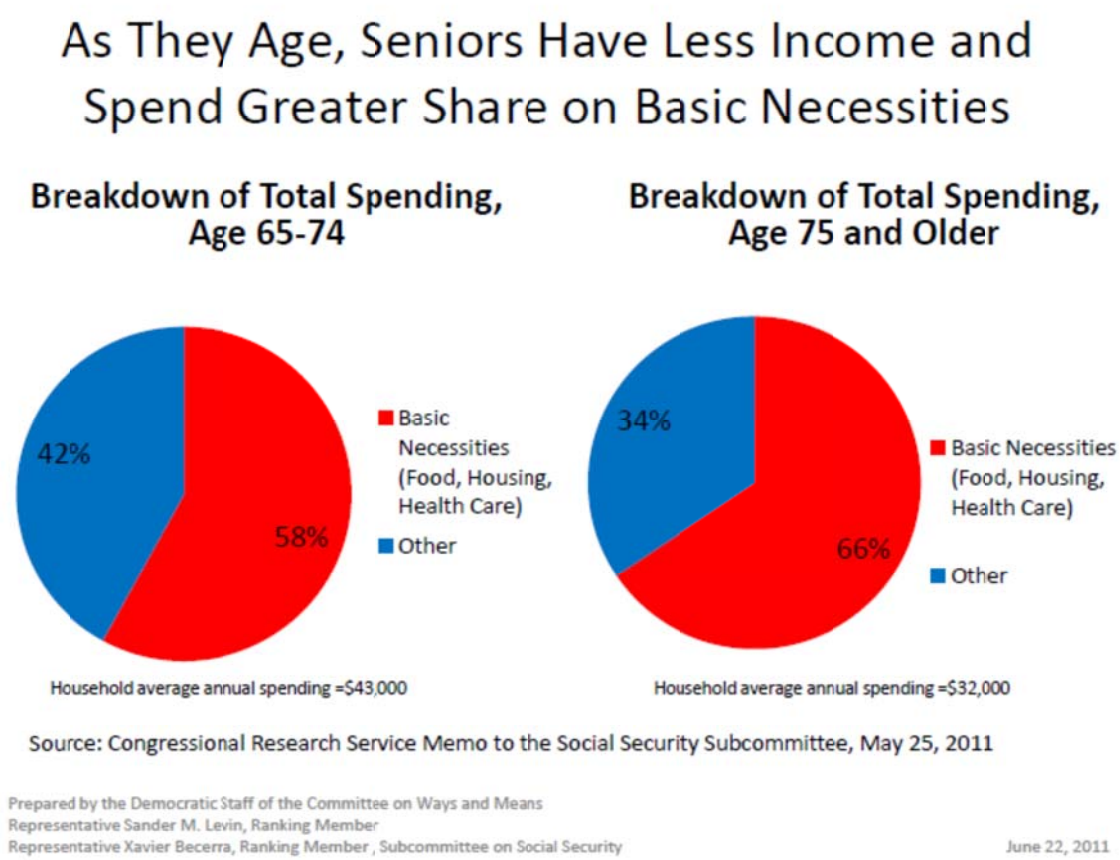
Source: Chief Actuary, Social Security Administration, June 2011. Note: These calculations apply once the chained CPI and retirement age increase are fully phased in, by 2015 and 2022, respectively.

- **Shrouded in technical language suggesting greater accuracy, the proposal to switch to the chained-CPI is best understood as a "stealth-like" attempt to implement benefit cuts in Social Security and other similarly indexed programs.**

- **Enactment of the chained CPI would violate promises made to hold-harmless current beneficiaries and persons 55 and over who are nearing retirement.** Current beneficiaries would be affected, regardless of whether it was implemented in 2011 or 2021**.**

Yet another problem, the chained CPI assumes that households can lessen the impact of inflation by changing their spending patterns. But seniors, with a larger proportion of their budgets devoted to necessities, do not have the same flexibility as younger persons (see figure 5):

Figure 5



Why the CPI-E Does a Better Job of Measuring Inflation for Retirees

Recognizing that the expenditures of elderly households differ from those of the general population, as part of the 1987 Amendments to the Older Americans Act, Congress directed the BLS to develop an index designed to more accurately reflect the impact of inflation on seniors. As noted, BLS complied by developing the CPI-E, making a new series of inflation data available projected back to 1982. From 1983 to 2007, the CPI-E has faster relative to the CPI-W, to 126.5 percent while the CPI-W rose to just 110 percent (Stewart, 2008).

While the chained-CPI would reduce COLA adjustments, on average, by a roughly 0.3 percentage points the CPI-E would, on average, increase benefits by roughly 0.2 percentage points, a difference of $953 (in 2011 dollars) at age 75, $1,688 at age 85, and $2,391 at age 95.

Conclusions

The public would be well-served if Congress and the President focused on funding the development and further testing of price indices that more closely track the spending of households with elders and persons with disabilities.

Unquestionably, switching to the chained-CPI would be ill-advised. Doing so would, over the next ten years, take an estimated $112 billion directly out of the pockets of Social Security beneficiaries. It would also cut Veterans Compensation and Pension benefits, federal pensions and other federal programs with COLAs – taking an additional $24 billion out of the pockets of veterans and $9 billion from other persons receiving federal benefits (Reno, Bethell, and Walker, 2011).

The implications of the chained-CPI are especially problematic for the most financially vulnerable aged and disabled who receive Supplemental Security Income (SSI) benefits. Because the annual adjustment to the federal SSI guarantee (currently $674 a month) is indexed to the CPI-W, both *before and after* receipt of SSI benefits, substituting the chained-CPI would result in benefit reductions every year prior to when they apply for benefits, and again, every year after they begin receiving benefits – a double hit on the most economically vulnerable.

Whether implemented in 2011 or 2021, the chained-CPI would violate promises made by members of Congress and the President that no changes will be made to Social Security that affect the benefits of persons ages 55 and over. It's bad policy and bad public relations because Social Security is a promise Americans expect their government to keep. This is true across virtually all demographic groups – young, middle aged and old, union and tea-party identified households – and across the political spectrum – Democrats, Independents and Republicans. Large majorities (ranging between roughly 70 and 80 percent) of each groups say, over and over again, do not cut their Social Security (see, for example, National Committee to Preserve Social Security and Medicare, September 2011). Americans are not easily deceived. They know a cut when they see one, and if the chained-CPI is implemented, tens of millions of Americans will understand that their government has let them down.

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APPENDIX A – Hypothetical Case of Jane Smith

Jane Smith turned 65 on January 1, 2011. She's healthy and looking forward to continuing her work on a part-time basis and to pursuing her life-long avocation as an amateur painter. She also plans to expand her volunteer service through her church. All things being equal, she will live another 20 years, very possibly longer.

Always careful with her money, she rents a modest one bedroom apartment that she shares with her dog and cat. She has $70,000 in her company 401(k) and another $40,000 in other assets (savings, bonds and stocks). Wanting the peace of mind that comes with knowing she has an assured stream of income, she buys a $70,000 single life income annuity (no payment to beneficiaries), guaranteeing that she will receive $4,670 a year, no matter how long she lives. Her assets spin off another $1,000 in 2011. She works part-time, anticipating about $12,000 a year in earnings. She starts receiving Social Security benefits on January 1, 2011, which will pay out $15,132 in 2011. This brings her first year income to $32,802, enough for her to live comfortably and to put her among the top 25% of households headed by unmarried persons 65 and over.

Things go along well for the first ten years and during most of those years she is able to add a few dollars to her savings, bringing the value of her assets up to $45,000. But little by little as inflation diminishes the purchasing power of her annuity, her household budget tightens. Part-time work is becoming more difficult, causing her to cut back on her hours, and, then to stop working all together when she has a hip replacement at age 78. Her medical expenses are increasing. Still independent at age 85, she now needs to employ someone several hours a week to assist with heavy household chores and she has to dip into her other savings. After 20 years, inflation has nearly halved the value of her annuity payments. Her budget is now very tight. Five more years pass. She never expected to be 90, but it's happened. She is only 4 years older than the average life expectancy for her cohorts who reach 65.

APPENDIX B – Social Security Works/Strengthen Social Security Campaign Fact Sheet Social Security COLA Cut: A Benefit Cut Affecting Everyone