



DO ANALYSTS USE ATYPICAL WORKERS TO EVALUATE SOCIAL SECURITY?

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TO EVALUATE SOCIAL SECURITY REFORM, analysts and policymakers examine its effects on workers with different incomes. They develop “typical” workers at each wage level to represent real-life counterparts. Typical workers are often defined as low-, middle-, and high-wage earners in relation to the average wage. However, new research sponsored by the Social Security Administration (SSA) suggests that traditional calculations yield workers who are not representative of their intended income groups. If this is true, reformers may be designing proposals based on prototypes that bear less resemblance to real life than they think.

A middle-income worker, as defined by SSA, earns the average taxable wage. Other workers are seen in relation to this: A low-income worker earns 45 percent of the average wage and a high-income worker earns 160 percent of the average wage. The average wage is calculated each year by factoring in the earnings of all current workers.¹ However, not every participant in the Social Security program works every year. Many take time off for school, children, disability, or early retirement. SSA's conventional calculations ignore these zero-earning years.²

A recent research project undertaken by SSA, Modeling Income in the Near Term (MINT), calculates the average wage differently. Instead of relying on hypothetical workers based on annual average wages, it uses historical records to gauge the lifetime earnings of participants in the Social Security program, capturing even those who have spent time away from the labor market. These earners can then be divided into low, average, and high categories so that a third falls into each.

Because traditional SSA calculations don't average in the zeros of nonearners, the average wage in any given year is deceptively high. MINT workers, on the other hand, have significantly lower average earnings (figure 1). Indeed, a MINT middle-wage earner has an income closer to that of the conventional SSA low-wage worker; the MINT low-wage earner is not even represented on the conventional SSA scale. These differences are largest among women, who are therefore especially misrepresented by the traditional method.³

MINT changes perceptions of how Social Security benefits and taxes are distributed. The higher a worker's income, the greater his or her Social Security benefits. Therefore, if MINT workers are earning less than SSA workers, their benefits are also slightly lower. However, in some ways the Social Security benefit formula favors these new lower-earning

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1. The disparity between the average earnings of workers and the average earnings of all Social Security participants is shrinking due to increases in total hours worked and in female labor force participation.
2. Many people have low earnings due to zero-earning years, not low wages when they work, so low earnings are not always indicative of need.
3. Some women receive spousal and survivor benefits that are in excess of the benefits based on their own earnings, so other parts of the safety net may still provide a source of protection.

S T R A I G H T T A L K

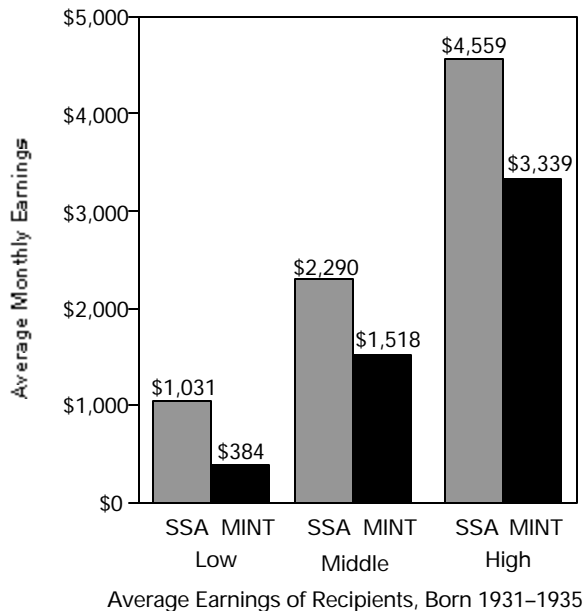
on Social Security and Retirement Policy

MINT workers. For example, lower-income workers have a higher rate of return: They get more back for each tax dollar than do higher-income workers. In addition, their replacement rate—the percentage of their old incomes that is now paid by Social Security—is higher.

The policy implications of the differences between the SSA and MINT calculations are significant. For example, some reformers have proposed a minimum

benefit to help low-earning Social Security recipients.⁴ However, when such a proposal is evaluated using the traditional SSA calculation, it appears to do little for the low-income workers it is designed to help; if assessed using MINT calculations, it may appear to do much more for them. If reformers want to better understand how their proposals affect workers, they must start with an accurate reflection of their true earnings.

Figure 1.
Two Definitions of Typical Workers: SSA and MINT



Note: Earnings are wage-indexed.
Source: MINT Project.

4. Gene Steuerle suggested a minimum benefit that was incorporated into the National Commission on Retirement Policy plan and was later modified for the Congressional bill sponsored by Representatives Kolbe and Stenholm. Under this minimum benefit, it has been estimated that the worker's own benefit would rise for about 50 percent of females and about 20 percent of males, although once spousal benefits are accounted for the net gain would apply to about 20 percent of all individuals.

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