A not-so-unkind cut - Social Security COLAs
Commentary
Richard W. Johnson

As Congress begins meeting off-camera to pursue the politically charged debate over Social Security for baby boomers, reducing the cost of living adjustments (COLAs) is sure to resurface as a strategy. For all the unpopularity of such a proposition, it may actually be the best way to bring down rising Social Security costs - expected to jump from just over 4.5 percent of GDP in 1999 to nearly 7 percent by 2030 - and avoid higher payroll taxes.

But such cuts must be accompanied by compensatory supports for the oldest and poorest who receive benefits, or else this vulnerable group will be hardest hit, and the ranks of the poor will swell.

Cutting COLAs - mainstays of the Social Security system since 1972 - began to seem politically possible around 1996. All at once, several studies suggested that the consumer price index (the base for adjustments) overstates inflation.

The Boskin Commission, created to study the CPI, noted that simply comparing the price of the same basket of goods and services every month doesn’t acknowledge the impact of consumer choice or technological change. Knock-offs or off brands, same-price goods that last longer than those in the basket, or new products and services can make CPI perennials obsolete and the CPI artificially high.

This insight sparked numerous proposals to control Social Security spending, either by setting COLAs below the CPI or by fiddling further with the way the CPI itself is computed. Either way, elderly couples and individuals in the bottom two-fifths fare the worst and the pain gets sharper as the years wear on.

If COLAs were set at one percentage point below the CPI, as some in Congress have proposed, the initial sting wouldn’t hurt much. But after 20 years, mean annual Social Security income would fall by nearly 11 percent (more than $1,100) for those over age 65. Within that group, those 65 to 74 would lose just over 7 percent (less than $800) while those 85 and over would endure a 17 percent (or $1,500) cut to their benefits.

Expressed as total household income, the cuts would be less dramatic, but the oldest and poorest would still be hurt the most. Those over 85 years would lose 8.5 percent of their income, compared with 2.5 percent for those aged 65 to 74.

Hard times among the very old and poor under these scenarios reflect more than the ravages of compound losses. The poorest two-fifths of the elderly depend on Social Security to meet 80 percent of their basic needs. By contrast, that monthly check provides only 18 percent of total income for Americans in the top fifth, and 45 percent among the second-highest fifth.

For the least well-off with few pension funds, or other sources of income, a cut in Social Security severs their financial lifeline. Ironically, the bottom 10 percent may not be as bad off as the next lowest 10 percent under these proposals because Social Security cuts may qualify them for Supplemental Security Income (SSI), a national needs-based program. Yet only half of those eligible for SSI ever collect it, perhaps because it carries a welfare stigma that Social Security does not.

Even if the many newly eligible do apply for SSI, the number of elderly below the poverty line is sure to rise if COLAs are cut. Our research indicates that up to 1.5 million elderly would slip below the poverty line if COLAs dipped to one percentage point below the CPI. Poverty rates would be especially high for nonwhites, unmarried women, and the very old.

The nation’s lawmakers have their work cut out for them keeping the Social Security system solvent. But they do have viable options that they had best consider before a failure forces major tax hikes or benefits cuts.
Coupled with cuts to COLAs or the CPI, they should consider increasing the minimum benefits payable by Social Security. Annual adjustments to retirement benefits thus could better reflect true cost-of-living changes while protecting the incomes of the poorest elderly.

Another option is to expand SSI payments and tender them without embarrassing Americans who have worked hard and shunned handouts their whole lives.

Still another approach would be to cut benefits to those in the top half of the income scale. Federal taxes on benefits could be raised for this group, or COLAs could be reduced only for those receiving the largest benefits (without hardship, since the bulk of their income would not be affected). Or the formula for replacing income could be tweaked to favor the poorest a bit more and the richest a bit less.

Abandoning proposals to cut COLAs because these cuts would be unfair if made across the board would be throwing out the baby with the bath water: Without cutting benefits, raising the retirement age, or increasing taxes, there is nowhere else to make the system solvent. But let’s not throw out the very old and very poor either. It isn’t necessary, and it isn’t right.

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