STATEMENT FOR THE RECORD

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On

The Role of Social Security, Defined Benefits, and Private Retirement Accounts in the Face of the Retirement Crisis

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Introduction

On behalf of our members and all Americans age 50 and over, AARP would like to thank Chairman Brown and Ranking Member Toomey for convening today's hearing to highlight the critical role Social Security plays – and will continue to play -- in the lives of millions of Americans, especially given the significant retirement crisis that is looming. The gap between the financial assets Americans will need to acquire to maintain their standard of living in retirement and what they are on a path to acquire is startling and suggests that for millions of today's workers their retirement security is even more likely to depend on Social Security. AARP appreciates the opportunity to testify today on some of the significant issues surrounding the current and future state of retirement security of American workers and their families, and more broadly, on the important contributions Social Security makes to families and to the economy, beyond providing a foundation of retirement income for most Americans.

A major priority for AARP has long been to assist all Americans in accumulating and effectively managing the resources they need to supplement Social Security and maintain an adequate standard of living throughout their retirement years. Unfortunately, both economic and social trends over recent decades, and notably developments affecting employer-provided pensions, have made the necessity of achieving and maintaining an adequate income in retirement more challenging than ever before. The three-legged stool of retirement—Social Security, pensions, and assets and savings—is increasingly tottering on the Social Security leg alone. According to a recent calculation by the Center for Retirement Research at Boston College, the "retirement income deficit" for American households ages 32 to 64 is estimated to be roughly $6.6 trillion. In fact, 57 percent of workers in 2013 reported that the total value of their entire household's savings and investments (not just for retirement), was less than $25,000, and 28% had less than $1,000.

These trends underscore the critical importance Social Security plays, and will play, in the retirement security of both current and future generations of Americans, and the need to have a conversation about the future of Social Security that is separate from political debates about deficit-reduction. Social Security was designed to provide only a foundation of an individual's retirement security and was not intended to be the sole source of income for people who have retired. However, due to shortcomings in other traditional components of the retirement security framework that help individuals achieve and maintain an adequate level of income for their golden years – employer-based pension plans, personal assets and savings, and affordable health care –for most older Americans, including middle-class families, Social Security is the primary source of retirement income. Moreover, for nearly all Americans, Social Security is the only source of retirement income guaranteed to last a lifetime and keep pace with inflation.

Social Security Deserves Its Own Conversation

In recent years, proposals have been made to reduce Social Security benefits in order to shrink the federal budget deficit. AARP believes that reducing the nation's deficit and restoring confidence in our budget is important, but we also understand that Social Security is vital to the economic security of older Americans, surviving spouses and children, and the disabled. Social Security is a separate, off-budget and self-financed program with its own dedicated funding source and it is not the cause of our federal deficits. Therefore, AARP strongly opposes cuts to Social Security in order to reduce the federal deficit.

According to the Social Security Trustees, even with no changes at all, Social Security has sufficient income from payroll contributions and assets in Treasury notes to pay 100 percent of promised benefits for the next 20 years, and can continue to pay approximately 75 percent of promised benefits thereafter. Social Security is therefore not in an immediate crisis, but the projected funding gap should be closed.

AARP believes that the current Social Security funding shortfall should be addressed sooner rather than later so that the fundamental structure of the program can be retained and the critical income security it offers to almost all workers and their families can be protected and even enhanced. However, any such changes to the Social Security system must be made within the proper framework of maintaining and improving the retirement security of real people and protecting current beneficiaries who have paid into the program during their working lives.

Social Security deserves its own national conversation that focuses on preserving and strengthening the retirement security of Americans and their families for generations to come. AARP welcomes that conversation and stands at the ready to engage with

Congress, our members and other Americans on ways to strengthen Social Security now and in the future.

The State of Retirement Plans Today

It is widely accepted today that workplace retirement plans and 401(k)-type plans, including those sponsored by state and local governments, have become the core retirement savings vehicles for the vast majority of Americans. AARP strongly believes that all workers need access to a workplace retirement plan that supplements Social Security's strong foundation for retirement income.

Unfortunately, employer-provided retirement plan coverage in the U.S. private-sector has generally hovered around a modest 50 percent for decades, with larger employers more likely than smaller ones to offer retirement plans. Overall, roughly 78 million American workers (both public and private) do not have access to a workplace retirement plan, such as a pension or 401(k) plan. For those workers who are fortunate to work for employers who offer a workplace retirement vehicle, many of their employers have moved away from providing defined benefit (DB) plans and increasingly offer only defined contribution (DC) plans, such as 401(k) plans. Today, only about 18 percent of workers have DB pension coverage on their current job, compared to 41 percent who have DC plan coverage. While DC plans can be valuable to many, they transfer investment, longevity, inflation, and interest rate risks entirely to the individual, and could make it more likely that an individual would outlive his or her retirement nest egg. As a result of these trends, few individuals adequately save for retirement on their own, and many are currently retired, or will retire, with less than enough money to meet their basic needs, relying on Social Security as their sole source of income in retirement.

In response to this significant problem, AARP has been a strong supporter of proposals such as the Auto IRA, which would help bridge this coverage gap and provide access to a workplace retirement vehicle to tens of millions of American workers. Specifically, this proposal – as well as related proposals recently sponsored in numerous state legislatures – would allow workers without access to an employer plan to voluntarily fund their own individual retirement accounts through payroll deductions. Harnessing the power of regular, automatic payroll deductions at work can encourage and simplify saving and significantly improve the retirement security of millions of Americans.

In addition to coverage issues, the actual participation rate of workers in private-sector pension plans varies with age, income, education, ethnicity, size of employer and type of employment. Older, better-educated, full-time, better-paid workers are more likely to be plan members than younger, less educated, part-time, lower-paid workers.

In an effort to increase participation rates in 401(k) plans, AARP supported the auto-enrollment provisions in the bipartisan Pension Protection Act. A May 2011 Aon Hewitt study found that "(t)hree in five employers automatically enrolled employees into their defined contribution plans in 2010, up from 24 percent in 2006. For employees who were subject to automatic enrollment, Aon Hewitt's analysis found that 85.3 percent participated in their DC plan, 18 percentage points higher than those that were not subject to automatic enrollment."

Social Security's Critical Role as an Income Source for Millions of Americans

As a result of the diminishing presence of defined benefit pensions and the volatility of personal retirement accounts and private assets, even those lucky enough to have access to a workplace retirement plan are more likely than ever to find that Social Security is the only guaranteed income stream they will not outlive during their retirement.

Social Security is the only lifetime, inflation-protected, guaranteed source of retirement income that most Americans will have. It is the foundation of retirement security that keeps millions of older Americans out of poverty and allows them to live independently. But Social Security also provides some measure of economic security for families who face a loss of income because of the disability or the death of a wage earner. We often do not think of Social Security as a family income protection plan—but that is exactly what it is.

Picture, for a moment, that you're a 30-year-old mother of one, with a baby on the way, who learns her husband has just perished in an accident at work. Imagine that, in your grief, you have no idea how you're going to feed your family and keep a roof over your heads. Now, imagine the relief of discovering a program that will help you support your children until they become adults – all because your husband had earned benefits to protect the family. That blessing is Social Security, and the family was mine. My father died before I was born. My mother worked incredibly hard as a part-time seamstress, but Social Security survivors' benefits were the difference between eating and not eating in our house.

At the end of 2012, about 57 million people received benefits from Social Security. The majority of these beneficiaries were 36.7 million retired workers. Social Security beneficiaries, however, also included 8.8 million disabled workers, 4.4 million children, 4.3 million widows, widowers, and parents and 2.4 million spouses. In fact, Social Security pays more benefits to children than any other government program. Social Security is also a critically important source of income for millions of children who live with their grandparents. For many of these beneficiaries and their families, Social Security is the one source of income that stands between them and poverty – without it, more than 21 million additional men, women and children would be in poverty.

While the number of beneficiaries who rely on Social Security is enormous, the benefit amount itself is quite modest, and in light of how millions of beneficiaries lack additional significant sources of income, may not be sufficient to maintain their standard of living. Today, half of those 65 and older have annual incomes below $20,000, and many older Americans have experienced recent and significant losses in retirement savings, pensions, and home values. Every dollar of the average Social Security retirement benefit of a little over $15,000 is absolutely critical to the typical beneficiary. For older American households receiving benefits, Social Security is the principal source of income for nearly two-thirds, and roughly one third of these households depend on Social Security for nearly all of their income. Reliance on Social Security as a source of guaranteed income only increases as people age.

Social Security benefits are particularly important for women, who, on average, live longer and earn less than men. Women also spend more time out of the labor force or work part-time to care for children and other family members. Fifty two percent of all women aged 65 and older depend on Social Security benefits for 50 percent or more of their family income. Moreover, in 2012, older minorities relied on Social Security for a significant share of their family income. Thirty-four percent of African Americans and 35 percent of Hispanics who are 65 and older depended on Social Security for 90 percent or more of their family income. Finally, the poor and near-poor also rely on Social Security for a significant share of their income; in 2012, over 60 percent of older Americans who were poor near-poor relied on Social Security for 90 percent of more of their family income.

As I travel around the country, I often hear people age 50+ express their passionate commitment to leaving the world a better place for their children and grandchildren. Recently, I've had the privilege of talking to college students, and they feel just as deeply about making sure their parents and grandparents are secure and independent. Social Security, the young and old understand, is a vital part of an intergenerational compact.

Family members depend upon one another, in daily expressions of intergenerational solidarity. Parents welcome children back to the nest; grandparents help pay for college; sons and daughters care for older or ill relatives – often while still raising their own children.

We hear sometimes that the young and old are rival armies in a struggle over finite resources. That's not what I see. I see family members who depend on each other. I see Americans at different stages in life's journey. Older people help younger people; later, the caregivers become the cared-for.

One day, the young will need the protections of Social Security every bit as much as seniors do today – and perhaps more so. Due to stagnating income, shrinking pensions, escalating personal debt and rising costs for education and health care, workers today are less likely than their parents or grandparents to enjoy the living standards of their working years when they retire. If these trends continue, Social Security will be the main source of income for all but the wealthiest retirees in the future.

Social Security's Contribution to the Broader Economy

The significant role Social Security plays in the financial security of its beneficiaries is growing. At the same time, the role those benefits play in both the national and state economies is only beginning to be fully understood. A recent report published by AARP, "Social Security's Impact on the National Economy," http://www.aarp.org/content/dam/aarp/research/public_policy_institute/econ_sec/2013/social-security-impact-national-economy-AARP-ppi-econ-sec.pdf, examined the impact of the $774 billion in benefits paid by Social Security in 2012. Social Security's economic impact starts when its recipients spend their benefits on goods and services. The businesses that receive these dollars use them to pay their owners and employees, purchase additional items to sell, and pay rent, taxes and the other normal costs of doing business. Their suppliers in turn use the revenue that they receive to pay their employees, suppliers, and others.

The report shows that every dollar of Social Security benefits generates about $2 of economic output. Social Security benefit payments help people keep or find over 9.2 million jobs that generate more than $370 billion in salaries, wages and other compensation. Benefit payments add almost $1.4 trillion in economic output (goods and services) to the overall American economy. Perhaps most surprisingly, Social Security benefits result in tax revenues for local, state, and federal governments exceeding $222 billion, including $78.9 billion in local and state taxes and $143.3 billion in federal taxes.

Every state – big and small – feels the effects of Social Security benefits being spent within their borders. Not surprisingly, California, with the largest economy of the 50 states, showed the biggest impact. In California alone, Social Security benefits supported 888,000 jobs, $147.4 billion in output, and $8.7 billion in state and local tax revenues. In Ohio, Social Security benefits supported just over 349,000 jobs, $51.7 billion in output, and $2.86 billion in state and local tax revenues. In Pennsylvania, Social Security benefits supported 470,442 jobs, $70.9 billion in output, and $4 billion in state and local tax revenues.

The results of our report are important to the discussions on how to close Social Security's long-term financing gap. According to the Social Security Administration, the Social Security program will face a funding gap that if left unaddressed will require benefits to be reduced across-the-board by about 25 percent beginning in 2033. Our report found that this cut in benefits--about $190 billion--would cost the U.S. economy about 2.3 million jobs, $349 billion in economic output, $194 billion in gross domestic product, and $93 billion in employee compensation. Too often, the choice for closing the funding gap facing Social Security is characterized as a choice between harming the vulnerable through benefit cuts and harming the economy through tax increases. In addition to the economic hardship that would be felt by individuals, our report shows that reducing benefits would also have a serious impact on the economy by damaging employment, retail and other spending, and lowering tax revenues for both the federal and state governments.

Conclusion

The promise of Social Security has endured for over 75 years. It is a promise that AARP believes embodies our deepest values as Americans – our obligations to one another – our obligations between generations – between parents and children – between grandparents and grandchildren – between those in retirement and those at work – between the able-bodied and the disabled. And AARP firmly believes that this promise must continue to endure as Social Security will continue to play a critical role in the lives of future generations of Americans.

AARP would like to thank Chairman Brown and the Sub-Committee for the opportunity to share our views and those of our members on the important role Social Security plays, and will play, in the lives of both current and future generations of Americans. We look forward to working with you and the other members of this Committee to ensure that any modifications to Social Security are done in a way that is consistent with the needs and wants of the American people.