

Commentary

BUFFIN PARTNERS INC.

INVESTMENT AND ACTUARIAL RESEARCH

Social Security Strengthens Solvency

Trustees Report Improved Financial Outlook

In the just-published 2002 Annual Report, the Social Security Trustees provide an update on the financial condition of the system and present results of 75-year projections extending to 2076. These include the actuarial balance of the system over various projection periods on each of three different sets of economic and demographic assumptions (intermediate, low-cost and high-cost). The actuarial balance concept compares the value of future income and current assets of the system to the value of future benefit and other costs plus a reserve of one year's benefit outgo. The Trustees report that, on the intermediate basis, the actuarial balance strengthened compared to 2001 and is above 100% over the next 35 years and equals 97% for 40 years, 94% over 50 years and 88% for 75 years. On the Trustees' low-cost basis, the actuarial balance exceeds 100% over the full 75-year period. On the Trustees' high-cost basis the actuarial balance exceeds 99% for 25 years, and is projected at 81% and 74% for 50 and 75 years respectively. On the intermediate projection basis the Trustees indicate that bringing the system into actuarial balance over the next 75 years would require an increase of 1.87% to the payroll tax rate compared to 1.86% from the 2001 Trustees' report. The principal components of this net increase of 0.01% arise from an increase of 0.07% from extending the projection period to 2076 and an offsetting net reduction of 0.06% due to changes in projection methods and assumptions to reflect the improved outlook. The report also presents a more optimistic outlook for maintaining a positive balance in the fund, extending by three more years to 2041 the period for which the fund is able to maintain payment of 100% of projected benefits without a need for supplemental funding.

New Thoughts on Social Security Funding

The Society of Actuaries is sponsoring a June symposium to provide "new thoughts and insight among many disciplines as professionals discuss ways the aging population and changing family structures are changing retirement today." One of the papers, presented by Robert Brown of the University of Waterloo, is entitled "Qualified Pension Plans and Health Care for the Elderly: the Perfect Macroeconomic Immunized Portfolio." Based on a model for Canada, the paper demonstrates how increased tax revenues collected by the Canadian government from income payable from qualified pension plans to baby boom retirees will match the increased funds needed by the government for their health care delivery. This concept is adaptable to the US with respect to the expected taxable cash flow from future retirement income and assets of the US baby boom retirees, including defined benefit and defined contribution pension plans and other taxable retirement income sources, such as individual retirement accounts as their accumulated balances produce taxable cash flows. The extent of this flow of tax revenue to the government is quantifiable under various plausible scenarios and could be weighed against the projected strain on the Social Security and Medicare programs that the retirement years of the baby boom generation will produce. If general revenues are made available to bring the Social Security System into 100% actuarial balance over successive 75-year projection periods as the baby boom generation moves through the retirement years, then as Robert Brown has demonstrated in his model for Canada, there will be a mitigating effect from the tax revenues generated by these same baby boom retirees.

A Tribute to Robert M. Ball

Robert M. Ball was formerly Social Security's chief administrator and he continues to be a leading contributor to public policy debates on Social Security. His influence on the development of Social Security over the last six decades and his major contributions as Social Security advocate, philosopher and architect are recorded in a Century Foundation book entitled "Insuring the Essentials—Bob Ball on Social Security" comprising a selection of 22 of his articles and essays. The wisdom, objectivity and insight of Bob Ball are in evidence in every article and essay. Of particular note for their relevance to the current policy debate over the future direction of Social Security are the chapters on "Social Security in the Decades Ahead: The Case for the Traditional Program", "Making Policy: A Job for All of Us", "Supporting Social Security from General Revenues", "Getting the Facts Straight about the program's financing, 75-year forecasts and prospects" and "A Program for the Future." His comments on the nature of the 75-year forecasts are noteworthy, asserting that a 75-year estimate can never be exact but is in reality a best-guess estimate. He observes that the results of the process convey a misleading sense of precision and that the public and media misinterpret the middle-range estimate as precise while disregarding the range of possible outcomes between the low-cost and high-cost estimates.

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