

WERE BENEFITS UNDER THE ORIGINAL SOCIAL SECURITY PROGRAM  
ON AN INDIVIDUAL-EQUITY BASIS?

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From time to time over the years, statements have been made that the original Social Security Act of 1935 provided benefits which would be on a completely actuarially-equivalent, individual-equity basis. In other words, every individual who is covered by the program would receive exactly his or her money's worth--no more and no less. Accordingly, it is asserted that only pure "insurance" was involved and that no "welfare" or "social-adequacy" elements were present.

The provisions in the original 1935 legislation never went into effect insofar as monthly benefits were concerned, because they were superseded by the 1939 Amendments. The latter, it is often asserted, introduced social-adequacy elements and thus changed completely the nature of the program. That this is not so can be shown from material in an actuarial study issued in 1938. The relationship was examined between the actual benefits to be payable and those on an actuarially-equivalent basis, assuming an appropriate mortality table and interest rate (and not making any allowance for administrative expenses), for individuals entering the system at its inception on January 1, 1937 and remaining steadily covered thereunder until retirement at age 65.

The procedure was to determine first what portion of the taxes was necessary to provide the lump-sum death benefit (the excess, if any, of 3 1/2 percent of cumulative creditable wages over any monthly benefits received). Next, the amount of actuarially-equivalent annuity from the remainder of the taxes was computed. The necessary calculations were relatively simple to make because the original program provided only retirement benefits (and no auxiliary or survivor benefits) and lump-sum refund payments. The computations were made considering alternatively (1) only the employee taxes and (2) the combined employer-employee taxes.

Table 1 presents the results of the computations on the basis of the combined employer-employee taxes, assuming retirement at age 65. Table 2 gives corresponding figures using only the employee taxes. Under either basis, it can be seen that those near retirement age when the system began had actual benefits which were far in excess of the actuarially-equivalent ones. For example, even considering the combined employer-employee taxes, the actuarially-equivalent

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benefit for a person entering the program at age 60 was only 13 percent of the actual benefit payable under the maximum-earnings case (\$250 per month) and was much less than this for lower earnings cases.

The situation was considerably different for persons who would be in the program for an entire working lifetime. If only the employee tax were considered, individuals would always receive more than the actuarially-equivalent benefit. Thus, from Table 2, for the maximum-earnings case, the ratio was 74 percent, while for an average earnings case (\$100 per month), it was 47 percent, and for a very low-earnings case, it would be as small as 27 percent. On the other hand, when the combined employer-employee taxes were considered, the actual benefit for a young new entrant would be significantly less than the actuarially-equivalent benefit for persons with average or higher earnings. For example, for the maximum earnings case, the ratio was 179 percent.

The ratios of the actuarially-equivalent benefit to the actual benefit are, for any particular wage level, higher for those with low wages than for those with high wages. This intra-generational transfer, which results from the weighted benefit formula, is one aspect of the social-adequacy nature of the program (which was present in the original law, and is still present, although in varying degree).

Similarly, when the ratios are considered for different ages at entry (in 1937), but with the same wage level, they are much larger for the youngest ages than for the older ones. Again, this results from the social-adequacy element present, in that relatively large benefits were to be payable for those near retirement age when the program began. Thus, inter-generational transfer was also present.

In summary, the analysis of actuarially-equivalent benefits under the original Social Security Act, as computed and presented some 43 years ago, clearly demonstrates that the benefit structure as initially developed was not on a strictly individual-equity basis, but rather it contained a considerable mix of social adequacy and individual equity.

Table 1

COMPARISON OF ACTUAL AND ACTUARIAL-EQUIVALENT BENEFITS UNDER ORIGINAL  
 OLD-AGE BENEFITS PROGRAM, RETIREMENT AT AGE 65, USING COMBINED  
 EMPLOYER-EMPLOYEE TAXES

<u>Age at Entry</u>	<u>Actual Benefit</u>	<u>Actuarial-Equivalent Benefit a/</u>	<u>Ratio</u>	<u>Actual Benefit</u>	<u>Actuarial-Equivalent Benefit a/</u>	<u>Ratio</u>	
		Monthly Wage of \$25				Monthly Wage of \$50	
20	\$23.75	\$15.22	64%	\$35.00	\$ 30.44	87%	
30	21.25	9.02	42	30.00	18.04	60	
40	18.75	4.75	25	25.00	9.50	38	
50	16.25	1.89	12	20.00	3.78	19	
60	*	.32	*	15.00	.64	4	
		Monthly Wage of \$100				Monthly Wage of \$250	
20	\$53.75	\$60.89	113%	\$85.00	\$152.22	179%	
30	47.50	36.08	76	75.00	90.21	120	
40	37.50	19.00	51	62.50	47.49	76	
50	27.50	7.56	27	50.00	18.90	38	
60	17.50	1.27	7	25.00	3.18	13	

\* Not eligible for monthly benefits (but rather only a lump sum of \$52.50).

a/ Based on U.S. White Males Life Table for 1920-29 at 3% interest.

Source: Actuarial Study Number 8, An Analysis of Benefits and the Progress of the Old-Age Reserve Account under Title II of the Social Security Act, Robert J. Myers, Social Security Board, June 1938 (Table 9).

Table 2

COMPARISON OF ACTUAL AND ACTUARIAL-EQUIVALENT BENEFITS UNDER ORIGINAL  
 OLD-AGE BENEFITS PROGRAM, RETIREMENT AT AGE 65, USING ONLY EMPLOYEE TAXES

<u>Age at Entry</u>	<u>Actual Benefit</u>	<u>Actuarial-Equivalent Benefit a/</u>	<u>Ratio</u>	<u>Actual Benefit</u>	<u>Actuarial-Equivalent Benefit a/</u>	<u>Ratio</u>	
		Monthly Wage of \$25				Monthly Wage of \$50	
20	\$23.75	\$ 6.33	27%	\$35.00	\$12.65	36%	
30	21.25	3.69	17	30.00	7.39	25	
40	18.75	1.93	10	25.00	3.86	15	
50	16.25	.77	5	20.00	1.54	8	
60	*	.14	*	15.00	.28	2	
		Monthly Wage of \$100				Monthly Wage of \$250	
20	\$53.75	\$25.31	47%	\$85.00	\$63.27	74%	
30	47.50	14.77	31	75.00	36.93	49	
40	37.50	7.72	21	62.50	19.29	31	
50	27.50	3.08	11	50.00	7.71	15	
60	17.50	.55	3	25.00	1.38	6	

\* Not eligible for monthly benefits (but rather only a lump sum of \$52.50).

a/ Based on U.S. White Males Life Table for 1920-29 at 3% interest.

Source: Actuarial Study Number 8, An Analysis of Benefits and the Progress of the Old-Age Reserve Account under Title II of the Social Security Act, Robert J. Myers, Social Security Board, June 1938 (Table 9a).