A new idea: Supplemental Transition Accounts for Retirement (STARTs)

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These mandatory accounts are designed to help workers delay claiming Social Security

Gary Koenig of AARP, **Jason Fichtner** of the Mercatus Center at George Mason University, and **Bill Gale** of the Brookings Institution have proposed Supplemental Transition Accounts for Retirement (STARTs) to raise the age at which Social Security benefits are first paid, thereby reducing the total actuarial reduction that would apply to benefits claimed early and increasing monthly benefits over the life of the beneficiary. These mandatory add-on savings accounts funded by employees, employers, and a progressive government contribution would be fully integrated into the Social Security program. Every individual with a START – if electing to claim Social Security before their Full Retirement Age (FRA) – would be required to exhaust that account's assets before receiving retired worker benefits, age-based spousal, or survivor benefits.

The proposal would improve the adequacy of retirement income because Social Security benefits are reduced by about 6 percent for each year they are claimed before the FRA. When the FRA reaches 67 (for those born in

1960 or later), those claiming at 62 will receive only 70 percent of the full benefit. The actuarial reductions are designed so that lifetime benefits are, on average roughly the same regardless of the age when people claim. The reduction, however, results in an inadequate benefit. Nevertheless many people claim before the FRA, and those without an employer retirement plan are totally reliant on Social Security. By delaying the start of Social Security benefits, people would end up with higher monthly benefits, which will be increasingly necessary as retiree health costs continue to rise. And higher benefits for a retired worker also mean higher benefits for a surviving spouse.

START contributions would be required for all workers below the FRA. Both the worker and the employer would contribute 1 percent of earnings (2 percent combined) up to the annual Social Security maximum ($128,400 in 2018). In addition, the government would contribute up to 1 percent for low-income workers to reflect the progressive nature of Social Security benefits. For married couples, total contributions would be split equally between the spouses. The employer's contribution is pre-tax; the employee's contribution is after-tax. Income taxes would be levied on the pre-tax distribution at retirement, and these monies would be deposited in the trust fund to offset the government's contribution for low-wage workers.

Simulations suggest that this program would increase average income by about 5 to 7 percent and 10 percent for the lowest-earning workers. The range in the estimates depends on the extent to which participants reduce their other saving. Importantly, this income cannot be outlived or eroded by inflation.

Generally, mandatory account proposals for Social Security make me very nervous, but the START proposal differs from others in a number of ways.

Most importantly, money distributed from the account does not reduce Social Security benefits. Second, participants are not required to buy a private sector annuity but rather they can purchase an inflation-adjusted annuity through Social Security. Finally, the authors explicitly argue that any adjustments to Social Security benefits to address the long-run solvency problem should not take account of the START assets.

Despite all the strengths of the proposal, it faces a tough future. Essentially, it raises the payroll tax rates by 2 percentage points and uses that money to start a new program rather than to close the 2.83 percent 75-year deficit. That is a tough sell.

But STARTs made me think about other ways to use the proposal. What if, up until the FRA, people could not claim their Social Security benefits until they exhausted some portion – say, half – of their 401(k)/IRA balances? That requirement would counter people's resistance to drawing down their nest egg and enable them to purchase the best annuity in town! Requiring the use of a portion of 401(k)/IRA balances before claiming Social Security retirement benefits would involve a very simple change in the legislation that regulates 401(k)s/IRAs. The government has a dog in this fight since 401(k) plans and IRAs are supported by foregone tax revenues, and all taxpayers should want them used efficiently.