Cost-of-Living Adjustments

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Cost-of-Living Adjustments

- Since 1975, Social Security’s general benefit increases have been based on increases in the cost of living, as measured by the Consumer Price Index (CPI)

- Effective for December benefits, payable in January

- Benefits keep pace with inflation
Consumer Price Index (CPI)

- Bureau of Labor Statistics produces monthly data
- COLAs are based on the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W)
- COLA = percentage increase (if any) in the average CPI-W from Q3 of last year to Q3 of current year
# COLA series, 1975-2018

<table>
<thead>
<tr>
<th>Year</th>
<th>COLA</th>
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</table>
Simple, right?

- Bureau of Labor Statistics produces monthly data on changes in prices paid for a **representative basket of goods and services**

- CPI-W (and CPI-U) based on experience of the relevant average household (spending habits survey of 7,000 families)

- Other indices, other approaches
Chained CPI (C-CPI-U)

- Based on idea that in an inflationary environment, consumers will choose less-expensive substitutes
- Lower-level vs. higher-level substitution bias
- By age 85, benefits would be about 6.5% lower
- OCACT estimates C-CPI-U would reduce the annual COLA by 0.3 percentage point, on average
CPI for the Elderly (CPI-E)

- Basket of goods and services for those age 62+
- Certain expenditure groups, such as medical care and housing, are given greater weight
- By age 85, benefits would be about 4.6% higher
- OCACT estimates CPI-E would increase the annual COLA by 0.2 percentage point, on average
Other variations

- Proposals to reduce or increase annual COLA (as currently calculated) by a set amount

- Chained CPI-W, chained CPI-E

- Hold disabled (DI), lower earners harmless

- No COLA for high earners
Small changes, big results

- Switching from CPI-W to chained CPI-W starting December 2020 = 21% of shortfall **eliminated**

- Switching from CPI-W to CPI-E starting December 2021 = **14% increase** in shortfall

- Reducing the annual COLA by 1 percentage point starting December 2020 = **66% of shortfall eliminated**
Resources

- About 140 provisions scored annually:
  https://www.ssa.gov/oact/solvency/provisions/index.html

- Cost-of-living adjustment provisions:
  https://www.ssa.gov/oact/solvency/provisions/cola.html

- Bureau of Labor Statistics – Consumer Price Index:
  https://www.bls.gov/cpi/home.htm