

THE CONCEPT OF "ACTUARIAL SOUNDNESS"

As the social security system has developed in the United States, the concept of "actuarial soundness" used by the Social Security Administration has been reduced to the single question of whether expected revenues from contributions and interest will be sufficient to meet expected benefit payments and administrative costs. To quote one description by the Division of the Actuary:¹²

The concept of actuarial soundness as applied to the OASI program differs to a considerable extent from this concept as it is applied to private insurance. Certain points of similarity exist, especially in comparison with private pension plans. The most important difference arises because OASI can be assumed to be perpetual in nature, with a continuing flow of new entrants resulting from the compulsory nature of the program.

Accordingly, it may be said that the OASI system is actuarially sound if * * * future contribution income plus future interest receipts will support the outgo for benefits and administrative expenses over the long run. * * *

This aggregative concept might more accurately be called a concept of fiscal control. This is because the main effect of the principle is to insure that revenues will be forthcoming to meet expected benefits. The principle does not insure that individuals now entering the labor force will necessarily "get their money's worth."

An essential purpose of standards of "actuarial soundness" is to insure that funds will be available to meet claims and benefits. This purpose may be consistent with various contribution schemes and financing methods. In private individual insurance, the relation between an individual's contributions and his expected benefits is necessarily an important element in "ratemaking," the equivalent of contribution schedules in social insurance.

The declining importance of the individual equity principle in OASDI is reflected in the infrequent use of the "actuarial rate" in discussions of the cost of social insurance. On the basis of private individual insurance, " * * * the actuarial rate expresses the value of the benefits to the individual."¹³ With the weighted benefit schedule of the OASDI system, such an actuarial rate would be a group rate:

Low wage earners get large benefits in relation to their contributions than do high wage earners, and the actuarial rate represents the average value of the benefits for persons in each age group that has the opportunity to contribute over a working lifetime.¹⁴

Just how much redistribution from higher to lower wage earners is consistent with such a group "actuarial rate" has never been specified. The differentials in contribution-benefit ratios vary not only with earnings levels but also with marital status, retirement age,

¹² *The Financial Principle of Self-Support in the Old-Age and Survivors Insurance System*, Social Security Administration Actuarial Study No. 40 (Washington, D.C.: 1955), p. 8.

¹³ Robert M. Ball, "What Contribution Rate for Old-Age and Survivors Insurance?" *Social Security Bulletin*, July 1949, p. 4.

¹⁴ *Ibid.*