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Frequently Asked Questions about Social Security's COLA

In October 2016, Social Security's annual cost-of-living adjustment (COLA) for 2017 will be calculated, and Social Security beneficiaries will learn by what percentage their monthly benefits will be adjusted in the coming year to offset the effects of inflation. Social Security beneficiaries are expected to receive only a small COLA, likely less than one percent, in 2017—after receiving no COLA whatsoever in 2016. It is important to note that the COLA is calculated automatically and prescribed by law. Neither the President nor Congress has any influence over this automatic adjustment. This means that improving the COLA requires legislative action.

Although the annual, automatic COLA provides valuable protections against inflation, the current COLA is inadequate and needs to be improved to reflect the high healthcare costs of Social Security's beneficiaries. This FAQ provides an explanation of the COLA, its importance to Social Security beneficiaries, and recommended policy changes to ensure that the COLA can more accurately fulfill its intended purpose of ensuring that Social Security benefits maintain their purchasing power year after year.

How Large Will the COLA Be in 2017?

Social Security beneficiaries did not receive a cost-of-living adjustment (known as the COLA), in 2016, the third year without a COLA in four decades.[1] The COLA for 2017 has not yet been determined; however, it is likely to be small. In their 2016 report, Social Security's trustees estimated a 0.2 percent COLA for 2017,[2] while more recent CPI data from the Bureau of Labor Statistics suggests that it will be slightly higher, although still less than 1 percent.[3] Given that a 1 percent COLA would increase average monthly benefits by less than $13,[4] and Social Security beneficiaries did not receive any COLA in 2016, these COLA estimates are especially paltry. Seniors and people with disabilities spend a larger percentage of their incomes on health care and prescription drugs, which rise faster than overall inflation. Annual increases in their costs of living are higher than those experienced by urban workers or even the general population, yet the current COLA fails to reflect these high rates of inflation.

What is the COLA?

The COLA is an annual adjustment that protects Social Security benefits from eroding in value as a result of inflation. The COLA was added as a critical expansion of Social Security in 1972 to ensure that benefits would automatically increase to reflect changes in the cost of living without relying on continual, and often delayed Congressional action to ensure that benefits would not erode in value year after year.[5]

The COLA is calculated using the Consumer Price Index for Urban Wage Earners and Clerical Workers (the CPI-W), which measures month-to-month changes in prices for goods and services typically purchased by urban workers.[6] By definition, retirees are not part of those sampled in producing the CPI-W. Because Social Security benefits account for most—and in some cases, all—of the incomes of seniors and people with disabilities, these annual adjustments are intended to ensure that benefits maintain their purchasing power over many years and do not erode in value over time.[7] A better measure is necessary to meet that goal. In 1972, when automatic annual adjustments were enacted, the CPI-W was the only measure of consumer prices that the Bureau of Labor Statistics produced.[8] Today, it produces several others and has the capacity to refine those and produce more.

How Does the COLA Affect Social Security Beneficiaries?

The COLA is designed to ensure that Social Security benefits keep pace with annual changes in the cost of living. However, the index reflects the costs of living for workers, and does not even include in its sampling seniors or people who no longer work as the result of a severe and life-altering disability. Consequently, the CPI-W does not accurately measure and weight the costs of healthcare experienced by seniors and people with disabilities, who make up the vast majority of Social Security beneficiaries.[9]

In recent decades, health care costs have risen faster than other costs of living. Indeed, since 1992, the growth in out-of-pocket health care costs has surpassed Social Security's cost-of-living adjustments by more than a third.[10] As a result, Social Security's already modest benefits have failed to keep pace with beneficiaries' actual costs of living.

How Does the COLA Affect Medicare Beneficiaries?

The size of Medicare premium increases is directly affected by the low COLA. Premiums for Medicare are typically deducted directly from beneficiaries' Social Security benefit checks, and these premiums increase every year. The estimated Medicare Part B premium, for those who will see an increase, is expected to be $149 per month, a $27 increase over the monthly premium for 2016.[11]

About seventy percent of Medicare beneficiaries are protected by a "hold-harmless" provision, meaning that the dollar increase in their Medicare premiums must be limited to the dollar increase in their Social Security.[12] As a result, for a majority of Social Security beneficiaries in years with a low Social Security COLA and a high Medicare premium increase, any benefit increase from the COLA is effectively eliminated by the corresponding increase in the Medicare premium.[13] This means that, regardless of the actual COLA for 2017, many Medicare beneficiaries will receive the same monthly benefit in 2017 as they received in 2016—even though their costs of living will have increased.

For the approximately 30 percent of Medicare beneficiaries who are not held harmless from the increase in Medicare premiums, the low COLA is even more harmful. These beneficiaries—who include new enrollees in 2017, Medicare beneficiaries not receiving Social Security, and beneficiaries who are already paying higher, income-related premiums—are expected to shoulder the remaining cost of the premium increase by themselves.[14] As a result, when the COLA is significantly smaller than the increase in Medicare premiums, these beneficiaries face a sharp increase in their monthly Medicare costs. In 2016, when the COLA did not increase at all, beneficiaries who were not held harmless faced a premium increase of 52 percent.[15] Although Congress took action to protect these Medicare beneficiaries somewhat from a sharp increase,[16] beneficiaries who are not held harmless are not protected from experiencing a large increase, as the result of the tiny COLA announced in October. As a result, Medicare beneficiaries who are not held harmless could see their monthly Medicare premiums increase significantly in 2017.

Who Else Is Affected by the COLA?

A low COLA is not only harmful to Social Security and Medicare Beneficiaries, but to veterans, Supplemental Security Income (SSI) beneficiaries, and civil servants as well. Many veterans benefits administered by the Department of Veterans affairs are also adjusted annually using the Social Security COLA, including Disability Compensation benefits, Pension benefits, Military Retirement Pay, the Subsistence Allowance for veterans participating in vocational rehabilitation and employment services programs, survivor annuities for deceased veterans' family members, educational allowances for veterans' surviving family members, and Veterans' Monetary Burial Benefits (a plot allowance). For veterans and their family members who receive Social Security as well as any of these other benefits, the lack of a COLA increase will have a double impact. SSI monthly benefits and federal Civil Service Retirement Service (CSRS) benefits are also increased using the Social Security COLA.[17]

How Can the COLA Be Adjusted for Inflation?

Social Security beneficiaries who face high healthcare costs need a more accurate COLA to ensure that their benefits maintain their purchasing power year after year. Until a truly accurate measure for the inflation actually experienced by seniors can be developed, many policymakers propose basing the COLA on the CPI-E, a price index which somewhat more accurately reflects the higher healthcare spending of senior households. Since 1982, the CPI-E has generally risen faster than the CPI-W, at an average of 0.25 percent above the CPI-W each year between 1983 and 2015.[18] Basing the COLA on the CPI-E would provide Social Security beneficiaries with an estimated COLA of about 1.4 percent in 2017—still modest, but larger than the current COLA estimates.[19]

However, the CPI-E is not based on a dedicated survey of the spending patterns of elderly households. As a result, it likely understates the full impact of healthcare costs and other inflation experienced by seniors and people with disabilities who rely on Social Security for most, if not all of their incomes. Given that Social Security benefits are already modest, and that people who have been receiving benefits for many years have already seen their benefits eroded as a result of growing healthcare costs, a fairer and more accurate COLA should be based on the growth in wages, which reflects increases in productivity, or, even better, the CPI-MED, which tracks the rate of inflation of medical goods and services.[20] Basing the COLA on the increase in wage growth would result in an estimated COLA of 2.9 percent for an average monthly benefit increase of $36,[21] and basing it on the CPI-MED would result in an estimated COLA of 4.7 percent in 2017, for an average monthly benefit increase of $58.[22]

What Can Legislators Do To Improve the COLA?

A growing number of legislators and policymakers are advocating for a more accurate Social Security COLA. Several bills would improve the COLA to ensure that benefits are protected against inflation, and that beneficiaries can maintain their standards of living year after year. One bill, The Seniors and Veterans Emergency Benefits Act, provides a one-time increase in recognition that there have been insufficient or even no COLAs in many years. Legislators who want to improve the COLA for Social Security beneficiaries should support the following bills:

- The Social Security Expansion Act (S. 731), sponsored by Senator Bernie Sanders (I-VT)
- The Social Security 2100 Act (S. 1904, H.R. 1391), sponsored by Senator Richard Blumenthal (D-CT) and Representative John Larson (D-CT-1)
- The Protecting & Preserving Social Security Act (S. 960, H.R. 1811), sponsored by Senator Mazie Hirono (D-HI) and Representative Ted Deutch (D-FL-21)
- The Fair Adjustment & Income Revenue for Social Security Act (H.R. 1984), sponsored by Representative Peter DeFazio (D-OR-4)

- The CPI-E Act of 2015 (H.R. 3351), sponsored by Representative Mike Honda (D-CA-17)
- The SAFE Social Security Act (S. 1940), sponsored by Senator Brian Schatz (D-HI)
- The Strengthening Social Security Act (H.R. 5952), sponsored by Representative Linda Sanchez (D-CA-38)
- The Seniors and Veterans Emergency Benefits Act (S. 2251, H.R. 4144), sponsored by Senator Elizabeth Warren (D-MA) and Representative Tammy Duckworth (D-IL-8)

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[1] SSA, "Cost-of-Living Adjustments," accessed October 5, 2016. https://www.ssa.gov/oact/cola/colaseries.html

[2] Social Security Trustees, "Table V.C1.—Cost-of-Living Benefit Increases, Average Wage Index, Contribution and Benefit Bases, and Retirement Earnings Test Exempt Amounts, 1975-2025," *The 2016 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, June 22, 2016. https://www.ssa.gov/oact/TR/2016/V_C_prog.html#1047210

[3] The COLA is calculated using the annual percentage change in the third quarter average of the CPI-W. Based on the third quarter data from 2015, and data for July and August of 2016, Social Security Works estimates that the 2017 COLA would be approximately 0.7 percent. CPI-W data from FRED Economic Data, "Consumer Price Index for Urban Wage Earners and Clerical Workers: All Items," Federal Reserve Bank of St. Louis, accessed October 5, 2016. https://fred.stlouisfed.org/series/CWUR0000SA0

[4] Calculation by Social Security Works using average monthly Social Security benefit for August 2016. SSA, "Monthly Statistical Snapshot, August 2016," September 2016. https://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/index.html?qs

[5] Geoffrey Kollmann, "Social Security: Summary of Major Changes in the Cash Benefits Program," May 18, 2000. https://www.ssa.gov/history/reports/crsleghist2.html

[6] Social Security Administration (SSA), "CPI For Urban Wage Earners And Clerical Workers," accessed October 5, 2016. https://www.ssa.gov/oact/STATS/cpiw.html

[7] Over 3 in 5 (61 percent) of Social Security beneficiaries over the age of 65 relied on Social Security for half or more of their incomes in 2014. In 2013, nearly 3 in 5 (59.8 percent) SSDI beneficiaries relied on Social Security for at least three-quarters of their incomes. Data on beneficiaries ages 65 and older: SSA, *Income of the Population 55 or Older*, *2014*, Table 9.A1, April 2016. http://www.ssa.gov/policy/docs/statcomps/income_pop55/2014/sect09.html. Data on SSDI beneficiaries: Michelle Stegman Bailey and Jeffrey Hemmeter, "Characteristics of Noninstitutionalized DI and SSI Program Participants, 2013 Update," SSA, Research and Statistics Note 2015-02, September 2015, Table 2. https://www.ssa.gov/policy/docs/rsnotes/rsn2015-02.html

[8] Clark Burdick and Lynn Fisher, "Social Security Cost-of-Living Adjustments and the Consumer Price Index," *Social Security Bulletin* 67, No. 3, 2007. https://www.ssa.gov/policy/docs/ssb/v67n3/v67n3p73.html

[9] Retired workers and workers with disabilities account for 82.1 percent of Social Security beneficiaries in August 2016. SSA, "Monthly Statistical Snapshot, August 2016," September 2016. https://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/index.html?qs

[10] Social Security Works, "Shifting More Medicare Costs to Seniors Is an Indirect Social Security Cut," January 2014. http://www.socialsecurityworks.org/wp-content/uploads/2014/01/Shifting-More-Medicare-Costs-to-Seniors-Is-an-Indirect-Social-Security-Cut_Final-Jan-27.pdf

[11] The Boards of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds, *2016 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, July 2016. https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/TR2016.pdf

[12] Juliette Cubanski and Tricia Neuman, "What's in Store for Medicare's Part B Premiums and Deductible in 2016, and Why?" The Henry J, Kaiser Family Foundation, November 11, 2015. http://kff.org/medicare/issue-brief/whats-in-store-for-medicares-part-b-premiums-and-deductible-in-2016-and-why/

[13] The Boards of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds, *2016 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, July 2016. https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/TR2016.pdf

[14] Juliette Cubanski and Tricia Neuman, "What's in Store for Medicare's Part B Premiums and Deductible in 2016, and Why?" The Henry J, Kaiser Family Foundation, November 11, 2015. http://kff.org/medicare/issue-brief/whats-in-store-for-medicares-part-b-premiums-and-deductible-in-2016-and-why/

[15] Alicia H. Munnell and Anqi Chen, "No Social Security COLA Causes a Medicare Flap," Center for Retirement Research at Boston College, no. 15-14, August 2015. http://crr.bc.edu/wp-content/uploads/2015/08/IB_15-14.pdf

[16] The Henry J, Kaiser Family Foundation, "Brief Explains Why Medicare Part B Premiums Will Increase by 16 percent, not 52 percent, in 2016 for 3 in 10 Beneficiaries Due to the Recent Budget Deal," November 11, 2015. http://kff.org/medicare/press-release/brief-explains-why-medicare-part-b-premiums-will-increase-by-16-percent-not-52-percent-in-2016-for-3-in-10-beneficiaries-due-to-the-recent-budget-deal/

[17] Gary Sidor, "Social Security: Cost-of-Living Adjustments," Congressional Research Service, October 29, 2014. https://fas.org/sgp/crs/misc/94-803.pdf

[18] Alicia H. Munnell and Anqi Chen, "Do We Need a Price Index for the Elderly?" Center for Retirement Research at Boston College, no. 15-18, October 2015. http://crr.bc.edu/wp-content/uploads/2015/10/IB_15-18.pdf

[19] Based on the third quarter data from 2015, and data for July and August of 2016, Social Security Works estimates that the 2017 COLA based on the CPI-E would be approximately 1.4 percent. CPI-E data from FRED Economic Data, "Experimental Consumer Price Index: All Items," Federal Reserve Bank of St. Louis, accessed October 5, 2016. https://fred.stlouisfed.org/series/CPIEALL

[20] Bureau of Labor Statistics, "Measuring Price Change for Medical Care in the CPI," April 12, 2010. http://www.bls.gov/cpi/cpifact4.htm

[21] Social Security Trustees, "Table V.C1.—Cost-of-Living Benefit Increases, Average Wage Index, Contribution and Benefit Bases, and Retirement Earnings Test Exempt Amounts, 1975-2025," *The 2016 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, June 22, 2016. https://www.ssa.gov/oact/TR/2016/V_C_prog.html#1047210

[22] Based on the third quarter data from 2015, and data for July and August of 2016, Social Security Works estimates that the 2017 COLA based on the CPI-MED would be approximately 4.7 percent. CPI-MED data from FRED Economic Data, "Consumer Price Index for Urban Wage Earners and Clerical Workers: Medical Care," Federal Reserve Bank of St. Louis, accessed October 5, 2016. https://fred.stlouisfed.org/series/CWUR0000SAM