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SOCIAL SECURITY STILL NEEDS FIXING

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Thanks largely to recent strength in the economy, the Social Security Old Age and Survivors Insurance and Disability Insurance programs (OASDI) are projected to run operating surpluses — taxes in excess of outlays — through 2014, a year longer than in last year's Report. The deficit spending authority given by the system's trust funds is expected to cover subsequent deficits until 2034, two years longer than in last year's Report. At that point, how-ever, OASDI revenue from payroll taxes and taxing benefits will cover only 73% of benefits, and the system will not be able to make its payments on time.

> ***[In 2035] OASDI revenue from payroll taxes and taxation of benefits will cover only 73% of benefits, and the system will not be able to make its payments on time.***

Long term, the annual OASDI shortfalls are projected to grow very large. The deficits will exceed 5 percent of taxable payroll by 2035, after the baby boom has retired, and over 6.5 percent of taxable payroll by the end of the 75 year planning period. Ultimately, either the payroll tax will have to be boosted by more than 6.5 percentage points, or benefit growth will have to be trimmed, or some other tax revenue will have to be diverted to OASDI. (Add in the deficits projected for Medicare's Hospital Insurance program, and the increase would have to exceed 10 percentage points.)

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It is not true, as some may claim, that a 2 percentage point hike in the payroll tax would fix the system. The OASDI system is sometimes (unfortunately) summarized by its 75 year average annual surplus or deficit. The 75 year balance is now a negative 2.07 percent of payroll, less of a shortfall than the negative 2.19 percent of payroll in last year's Report. In past years, advocates of the status quo for Social Security have claimed that the 75 year average deficit indicates that the system is not in serious trouble, and that an immediate but (in their opinion) modest hike in the payroll tax of a bit over 2 percentage points would fix the system "for the long term". This is misleading.

The 75 year balance adds together the current trust funds, projected short run surpluses, and never-ending deficits thereafter (cut off at 75 years, with a target end of period trust fund balance), and expresses the result as a percent of taxable payroll. The trust funds (past OASDI surpluses plus interest) are only a record of money that the government has spent on other federal programs. The projected near-term surpluses

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will be spent to reduce the national debt (if the rest of the budget is also in surplus and does not need the revenue). None of that money will be available to pay benefits in the distant future, when OASDI will be in deficit by more than 6.5% of payroll. Boosting the current surplus with a 2 percentage point tax hike would only pay down the national debt faster, and would still leave the system short of balance by 4.5% of payroll at the end of the planning period.

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Every few years, the system's defenders push for a one or two percentage point payroll tax hike, increased taxation of benefits, or other changes to "fix" the system by bringing the 75 year average into balance. Then, as the calculation period moves forward, additional years of deficit are brought into the average, the long term imbalance reemerges, and the system's advocates ask for another "fix". In this manner, Congress and the public are tricked into a series of gradual tax increases to fund the system. The 1977 and 1983 Social Security Amendments and the 1993 Budget Act are cases in point.

If the Congress and the public were more aware of the full scope of Social Security's costs and imbalances, they might opt for a real change. Ideally, that change would involve reduced reliance on the pay-as-you-go Social Security tax-transfer system, and increased reliance on real private saving for retirement.

The only correct way to view the Social Security system is to look at its future surpluses and deficits on a year by year basis. If Social Security is in deficit in a given year, the Treasury must borrow, raise taxes, or cut other spending in that year to make ends meet. And those deficits will require drastic action, the new Trustees Report notwithstanding.

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Note: Nothing written here is to be construed as necessarily reflecting the views of IRET or as an attempt to aid or hinder the passage of any bill before Congress.