

# The US Social Security Program & Debate About Reform



Author Eric Lundell

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The “modern era” of US social welfare programs began in the 1930s with initiatives of the Roosevelt administration during the Great Depression. Since then, the US government has continued to develop various welfare benefits programs designed to support targeted segments of the US population, such as senior citizens, low income citizens, children, and other demographic groups. Today, the government’s network of social welfare programs includes efforts such as Medicare (health care for seniors), Medicaid (health care for low income families), unemployment benefits, disability benefits, food assistance programs (e.g. “food stamps”), and other benefits/entitlement programs.

Arguably, the most significant and popular US welfare program is Social Security, which provides monthly cash benefits to retired or disabled workers. Public opinion polls consistently indicate that the public strongly supports Social Security, across both political party and demographic lines.

This article examines the development of the Social Security program over the last 80 years and current debate about the future of the program.

Welfare program reform has been a major topic of discussion and debate in the United States for several decades. Current debate is driven by numerous factors, to include both specific policy issues, such as program management and budgeting, as well as broader political discussion regarding the US fiscal environment, the role of the government in providing welfare benefits, and the impact of welfare programs on society and the economy.

In summary, few people in the US are “completely satisfied” with the current web of welfare programs. However, there is significant disagreement about how welfare programs should be revised and amended. For example, at a fundamental level, some political factions argue for the reduction of welfare programs, while others argue for their expansion. Given this fundamental political division on the appropriate future of welfare programs, debate over the reform of specific management and funding processes for US welfare programs, to include Social Security, has been contentious.

However, at the same time, the Social Security program also faces increasingly severe long-term funding issues. As such, reform of this publicly popular program remains an imminent task facing the US government, political system and American people.

## Origin & Basic Structure of the US Social Security Program

The US Social Security program originated with the Social Security Act of 1935, which established a federal commitment for providing a minimum level of income for older US citizens (e.g. retired workers). Eligibility for Social Security is based on the concept that beneficiaries “earn” their “retirement benefits” through payments into the program prior to their retirement. These payments are made through a payroll tax paid by both employees and their employers on wages. As such, US Social Security is often referred to as a “self-financed” program (and does not currently contribute to the US government’s fiscal deficit). The Social Security program has also generated revenue by investing its funds in interest-earning federal securities.

On average, Social Security pays a benefit of about \$1,265 a month. However, an individual’s benefits level is related to the amount the person pays into the program throughout their life. The program was also designed to be progressive in that it is weighted to replace a larger share of low-wage workers’ income compared to higher-wage workers’ (i.e. the program uses a progressive wage-indexed benefit formula).

For most of the program’s history, the age at which full benefits become payable, known as the full retirement age (FRA), was 65. As part of the Social Security Amendments of 1983, the US Congress

raised the FRA through a gradual phase-in from 65 to 67 over a 22-year period (2000 to 2022). A person can also elect to “retire earlier” at age 62, subject to a permanent reduction in benefits.

## Evolution of the Program

One of the first major modifications of the program came with the Social Security Amendments of 1939, which expanded the program to dependents and survivors of retired workers. Since that time, the US Social Security program has generally continued to expand (albeit with some modifications made to limit the program in certain areas).

For example, in 1956, the government established disability insurance (DI) under the program. The formal name for Social Security became Old-Age, Survivors, and Disability Insurance (OASDI), and the inflow and outflow of funds in the program are accounted for in two separate trust funds: the Federal Old-Age and Survivors Insurance (OASI) fund and the Federal Disability Insurance fund.

Benefit levels have also increased over time, and, in 1972, Congress created a system of “automatic” annual increases known as cost-of-living adjustments (COLA) linked to inflation.

To account for expansions in the program, the payroll tax rate to fund the program also increased over time from around 2% (1% from employees and 1% from employers) in the 1930s to 12.4% today

Source: Social Security Administration



President Roosevelt signing the Social Security Act of 1935

Source: Social Security Administration



President Reagan signing the Social Security Amendments of 1983

As noted above, the Social Security program comprises two separate trust funds: the OASI fund and the DI fund. In 2012, the combined funds had total receipts of \$840 billion (\$731 billion from payroll taxes and \$109 billion in interest earnings) and total expenditures of \$786 billion. In other words, the program's revenue exceeds its expenditures. However, this is only due to interest earnings. Accumulated assets of the program stood at

(6.2% from employees and 6.2% from employers). The amount of income subject to the Social Security payroll tax also has increased from \$3,000 at the beginning of the program to over \$100,000 today.

\$2.7 trillion.

The program's board prepares an annual report on the current and projected financial status of the program. In its 2013 report, the board stated that, under current financing and benefit structures, benefits can be paid in full and on time until 2033. To be more specific, the 2013 Annual Report indicated that:

### Management of the Program

The US Social Security program is administered by the Social Security Administration (SSA), which is overseen by a board of trustees. Currently, the board comprises six members, including the secretary of the Treasury (as the managing trustee), secretary of labor, secretary of health and human services, and the SSA commissioner. The president also appoints and the Senate confirms two other members to serve as representatives of the public.

Source: Social Security Administration



Over the years, the Social Security program moved around within the US government structure. For example, in 1939 the government created the Federal Security Agency to oversee Social Security as well as other social welfare programs. The SSA was subsequently transferred to the Department of Health, Education and Welfare in the 1950s and to the Department of Health and Human Services in 1980. In the 1990s, the SSA once again became an independent agency.

- Social Security expenditures will exceed tax revenues each year through the end of the 75-year valuation period that the board uses to evaluate long-term performance of the program.
- Only when interest income is taken into account is Social Security projected to have an annual surplus — but only through 2020. Beginning in 2021, annual costs will exceed total income, and reserves begin to decline.
- The board currently projects that the trust funds will have a positive balance until 2033; at which point, the assets of the funds will be exhausted based on current financing and benefits structures and related projections.

Social Security's projected long-range funding shortfall is attributed primarily to demographic factors (such as lower fertility rates, increasing life expectancy, and a decreasing ratio of workers to retirees) and increasing benefits under current program design features (such as the annual COLAs).

In their 2013 report, the board concluded that for the trust funds to remain solvent throughout the 75-year projection period:

### Current Status of the Program

As of early 2013, there were 57.3 million Social Security beneficiaries. Of those, 40.1 million (about 70%) were retired workers and family members, 11.0 million (19%) were disabled workers and family members, and 6.3 million (11%) were survivors of deceased workers.

Source: Social Security Administration



Social Security Administration Headquarters, Woodlawn, Maryland

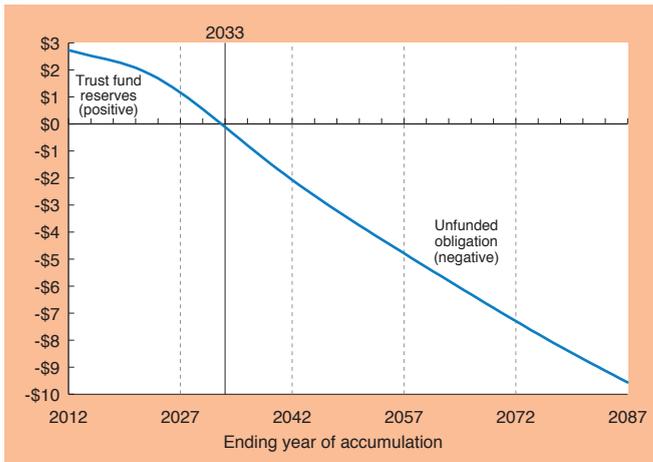
- Revenues would need to increase by an amount equivalent to an immediate and permanent payroll tax rate increase of 2.66 percentage points (from its current level of 12.40% to 15.06%); or
- Benefits would need to be reduced by an amount equivalent to an immediate and permanent reduction of 16.5% applied to all current and future beneficiaries, or 19.8% if the reductions were applied only to those who become initially eligible for benefits in 2013 or later; or
- Some combination of these approaches would have to be adopted.

In effect, the parameters of the policy adjustments needed to stabilize the Social Security program are well defined. The trustees have stated that "With informed discussion, creative thinking, and timely legislative action, Social Security can continue to protect future generations." They also have emphasized that implementing changes as soon as possible would allow for more moderate adjustments in tax increases and/or reductions in benefits.

CHART 1

## Cumulative scheduled OASDI income less cost, from program inception through 2012-87

[present value as of Jan. 1, 2013, in trillion \$]



Source: 2013 OASDI Trustees Report

### Reform of the Program

Since at least the 1970s, discussion regarding Social Security has become increasingly focused on addressing the long-term financing problems facing the program — and various reforms have indeed been implemented over the years. However, Social Security’s financial problems continue and further reform is an issue of ongoing debate by US policymakers.

The Democratic administration of President Barack Obama has repeatedly stated that it is committed to protecting and strengthening Social Security. In terms of reform objectives, the president maintains a politically “liberal” or “progressive” position. For example, he has stated that no current beneficiaries should see their basic benefits reduced and that he will not accept an approach that “slashes benefits for future generations.”

The president has also stated opposition to privatization of the program. (Former Republican President George W. Bush called for a transition of Social Security toward personal savings accounts through partial privatization of the system, as favored by free market advocates and some members of the right wing of the US political spectrum.) Obama, however, has stated that the future of “hard-working Americans” should not be “left to the fluctuations of financial markets.” (In this regard, some of the enthusiasm in the US for Social Security privatization during the Bush administration has diminished following the stock market fluctuations of the past several years.)

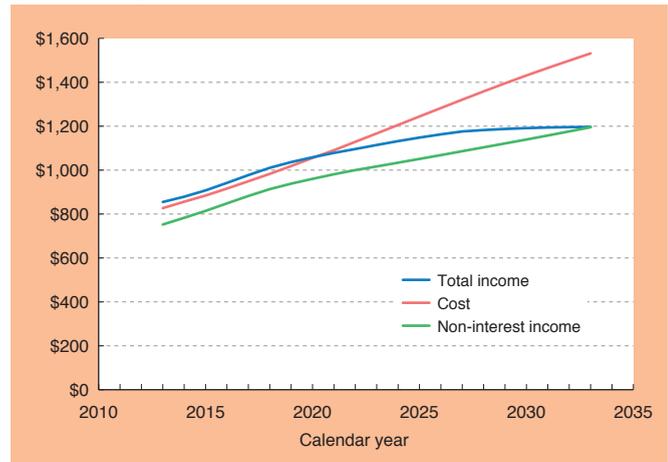
In 2010, Obama created a special task force to provide recommendations on improving the US government’s long-term fiscal outlook and addressing the growth of entitlement spending. This National Commission on Fiscal Responsibility and Reform (informally known as the Simpson-Bowles Commission after its chairs, Alan Simpson and Erskine Bowles) released its final report in December 2010.

In terms of Social Security reform, the commission presented an overall methodology under which “The most fortunate will have to contribute the most, by taking lower benefits than scheduled and paying more in payroll taxes. Middle-income earners who are able to work will need to do so a little longer. At the same time, Social Security

CHART 2

## Estimated OASDI income & cost in CPI-indexed 2013 dollars, based on intermediate assumptions

[in billion \$]



Source: 2013 OASDI Trustees Report

must do more to reduce poverty among the very poor and very old who need help the most” (e.g. a combination of raising taxes, cutting benefits, and extending the retirement age — while protecting benefits for the lowest-income Americans). The commission also emphasized that failure to take action (which it called a “do-nothing plan”) would lead to a 22% across-the-board benefit cut for all beneficiaries once the Social Security trust funds are depleted (e.g. around 2033). The commission made several recommendations, including:

- *Make the retirement benefit formula more progressive.* The commission proposed gradually moving to a more progressive benefit formula that slows future benefits growth, particularly for higher earners (e.g. reduce benefits growth for high-income Americans).
- *Gradually increase retirement ages.* The commission proposed increasing the retirement age to 68 by about 2050, and 69 by about 2075.
- *Gradually increase taxable maximum wages.* The program’s taxable maximum wage cap has not grown as fast as wages above the cap. As a result, less than 86% of wages were subject to the payroll tax in 2009. The commission proposed gradually increasing the taxable maximum so that it covers 90% of wages by 2050.
- *Adopt different inflation-adjustment measures.* A key reform proposal that has been discussed in Washington has been to use “chained CPI” to calculate COLAs for Social Security beneficiaries. Since 2002, the Bureau of Labor Statistics has released an “alternative” inflation calculation to CPI called chained CPI. It tends to find smaller changes in consumer prices than the bureau’s traditional CPI by accounting for the way consumers gradually adjust their spending as prices change. Differences between the two measures are small, often about 0.3% a year. However, over time, basing COLAs on chained CPI would have a significant impact. Obama supported this measure in his FY2014 budget proposal now under debate by Congress.
- *Begin a broader dialogue on the importance of personal retirement savings.* The commission also emphasized the need for the

government to educate Americans on retirement savings. It emphasized that Social Security was only intended to provide a secure minimum income for seniors and was never intended to be the sole source of retirement income for Americans.

However, political disagreement over the commission's conclusions has resulted in inaction regarding Social Security reform throughout 2011 to today. For example, following the commission's work, the Budget Control Act of 2011 established a Joint Select Committee on Deficit Reduction. Social Security program changes were among the measures considered by the committee. However, once again, no agreement was reached on legislative reforms.

## The Political Divide on Reform

Consensus has yet to develop on an overall approach for reforming Social Security. For example, most Democratic Party lawmakers focus on restoring long-range solvency to the program while maintaining (or even increasing) benefits. Some Democrats, especially those on the more liberal/progressive wing of the party, reject any reforms that would reduce benefits for lower-income Americans, favoring instead measures to increase taxes/revenue for the program or reduce benefits to higher-income Americans.

More moderate Democrats and Republicans debate how to find the "appropriate" balance between benefit reductions and revenue increases that would restore the program's long-term financial stability. More right-wing Republicans tend to focus broadly on constraining the growth in government spending on entitlement programs. Advocates of major reform view Social Security as an anachronism, created from Depression-era concerns about high unemployment and widespread poverty among the aged. For them, the prospect of reform is an opportunity to "modernize" how Americans saves for retirement (e.g. emphasis on personal savings over government welfare). Conservatives that support dismantling Social Security have sought to develop support among younger Americans based on arguments that the program is inappropriately shifting wealth from younger Americans to older Americans and will eventually burden young generations with future taxes.

However, at the same time, some Tea Party Republicans tend to maintain a strong distinction between reform of Social Security and Medicare (which they tend to support as "earned" entitlements that taxpayers have "paid into") from reform of "unearned" welfare programs such as Medicaid and food stamps, which they view more negatively as supporting lower-income Americans that have not "paid into" the system.

In other words, the debate on Social Security reflects political differences between lawmakers ranging from discussion on improving the adequacy and equity of benefits to deeper debate on redefining the appropriate role of the federal government in providing social welfare. Many in the US argue that the issues facing the program can be resolved with modest tax and benefit changes. On the other hand, some argue that Social Security will "bankrupt the nation" absent more fundamental reform, emphasizing that the program was designed as a "safety net" for retirees to guarantee only a minimum income, not to ensure a "comfortable retirement".

## Conclusions

Public opinion polls consistently indicate that the American public

supports Social Security, across party and demographic lines. According to a recent study by the National Academy of Science (NAS), large majorities of Americans support paying Social Security taxes. These findings hold constant across party lines (those that support Social Security taxes include 91% of Democrats, 86% of Independents, and 74% of Republicans) and across racial and ethnic lines (those that support Social Security taxes include 91% of African Americans, 84% of Hispanics, and 84% of whites).

Nearly nine in 10 Americans say Social Security is more important than ever to ensure that retirees have dependable incomes. These views cut across age and income lines: those agreeing include 84% of Americans in Generation X and 93% of the Silent Generation, as well as 89% of people with family incomes under \$30,000, 89% of those earning between \$50,000 and \$75,000, and 88% of those earning over \$100,000.

Moreover, Americans appear to support paying more to maintain Social Security's financing. More than eight in 10 say it is critical to preserve the program even if it means increasing Social Security taxes. An even higher percentage (87%) support increasing Social Security taxes paid by wealthy Americans to preserve the program. These findings again hold true across party lines, age groups, race and ethnicity, and income levels.

At the same time, public opinion polls also have shown that a majority of Americans in recent years lack confidence in the system's ability to meet its future commitments. Younger workers are particularly skeptical. For example, in one recent poll of non-retired adults aged 18 or older, 70% of those in the 18-49 age group said they did not think the Social Security system will be able to pay them a benefit when they retire, compared with 34% in the 50 or older age group.

In the end, the debate over reforming Social Security will come down to tax increases and/or benefit cuts based on whatever balance of these two basic means of reform is supported by the future political consensus. The NAS study indicated that seven in 10 Americans prefer a package of policy changes that both increases Social Security revenues and improves benefits. Support for reforms including both measures again cuts across political parties, age groups, income levels, and race and ethnicity. However, while general consensus exists on reforming the program, the details of this reform package remain politically elusive.

US politicians are keenly aware that Social Security reform presents tremendous political risks for their parties and their own careers. In a general sense, both political parties want to be perceived by the American public as the "defender" of Social Security. Neither party wants to make specific reform proposals that its opponents can use against it. (For example, some of Obama's opponents have criticized his support of using chained CPI for COLAs as a "failure" to defend Social Security.) Much of the debate in Washington can accurately be characterized as "political posturing" as each party and individual politicians seek to present themselves as the "defenders" of their constituents' best interests. Given that the program will not "run out of money" until into the 2030s, politicians tend to operate on the basis that there is "still time" for maneuvering before the truly difficult political negotiations and compromises become necessary. **JS**

*Eric Lundell is president of International Technology and Trade Associates, Inc. (ITTA), a consultancy based in Washington, DC. He holds an MA in international economics and has 20 years of experience advising clients on US business, policy and regulatory issues.*