Financing Social Security

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Introduction

- The Social Security Act was signed into law by President Roosevelt on August 14, 1935

  - “We put those payroll contributions there to give the contributors a legal, moral, and political right to collect their pensions […] With those taxes in there, no damn politician can ever scrap my Social Security program.”

  - FDR went on to say, "If I have anything to say about it, it will always be contributed, both on the part of the employer and the employee, on a sound actuarial basis. It means no money out of the Treasury."

The Old-Age & Survivors Insurance (OASI) Trust Fund

- Created in 1940 to address public concern about the use of OASI tax revenues for general purposes
  - Form over substance regarding the use of Social Security taxes
  - Did not and still does not prevent the use of OASI revenues for general purposes
  - Forces legislative intervention to prevent Trust Fund insolvency and for other transfers

- Legally distinct subdivision within the Treasury
  - Under current law, the Trust Fund may not borrow from the TGF nor accept transfers from another trust fund
  - Both restrictions overridden in prior years to satisfy trust fund solvency when necessary to pay benefits in full or to make up suspended tax payments (COVID)

- Holds government bonds
  - Since 1960, only non-marketable bonds (NMBs), redeemable at par
  - Interest rate determined statutorily by the Social Security Act
  - NMBs are recognized as part of the national debt
  - NMBs represent deferred publicly-held debt

Financing Process

- While FDR's sentiments remain in place in the view of many people today, they are no longer a reality, if they ever were.
    - The OASI Trust Fund does not pay Social Security benefits; they come from general revenues (the Treasury General Fund, TGF)
    - The OASI reserve/trust fund, while a distinct unit within the Treasury, does not hold tax "dollars" but rather non-marketable government bonds (NMBs)
    - Social Security taxes are commingled with other government revenues and are available for any government expense; they are not held in the Trust Fund

Financing Process

- OASI Trust Fund
  - Credited with the value of OASI taxes, taxes on Social Security benefits, and interest on NMBs
    - Tax “dollars” are used to “purchase” NMBs from Treasury bonds with proceeds returned to TGF and available for any government expenditure
    - Interest on NMBs comes from the Treasury, is used to purchase additional NMBs, and is returned to the Treasury; therefore, it is a wash and does not affect the Treasury’s balance sheet
    - Trust Fund assets (NMBs) = Treasury liabilities; hence, a wash within the Treasury
  - Debited with the value of benefit payments and expenses
    - NMBs are redeemed at par by being sold back to the Treasury using funds from the Treasury
    - Proceeds are added to the Treasury General Fund and used to pay benefits and expenses
    - Elimination of NMBs results in a reduction in Trust Fund assets and Treasury liabilities (a wash)

Financing Process

- Social Security is and always has been a pay-as-you-go system (no advance funding)
  - If Social Security taxes exceed benefit payments, the excess is used for other general expense purposes, avoiding an increase in publicly-held debt while increasing total debt outstanding (+NMBs)
    - The federal deficit is lowered
  - If Social Security taxes are less than required to pay benefits, the balance is paid by redemption of NMBs and an increase in publicly-held debt while leaving total debt outstanding unchanged (all other things being equal)
    - The federal deficit is increased
    - Benefit payments have exceeded noninterest income (Social Security taxes and taxes on Social Security benefits) in the 1970s and continuously since 2010

Financing Process

- Social Security is and always has been a pay-as-you-go system (no advance funding)

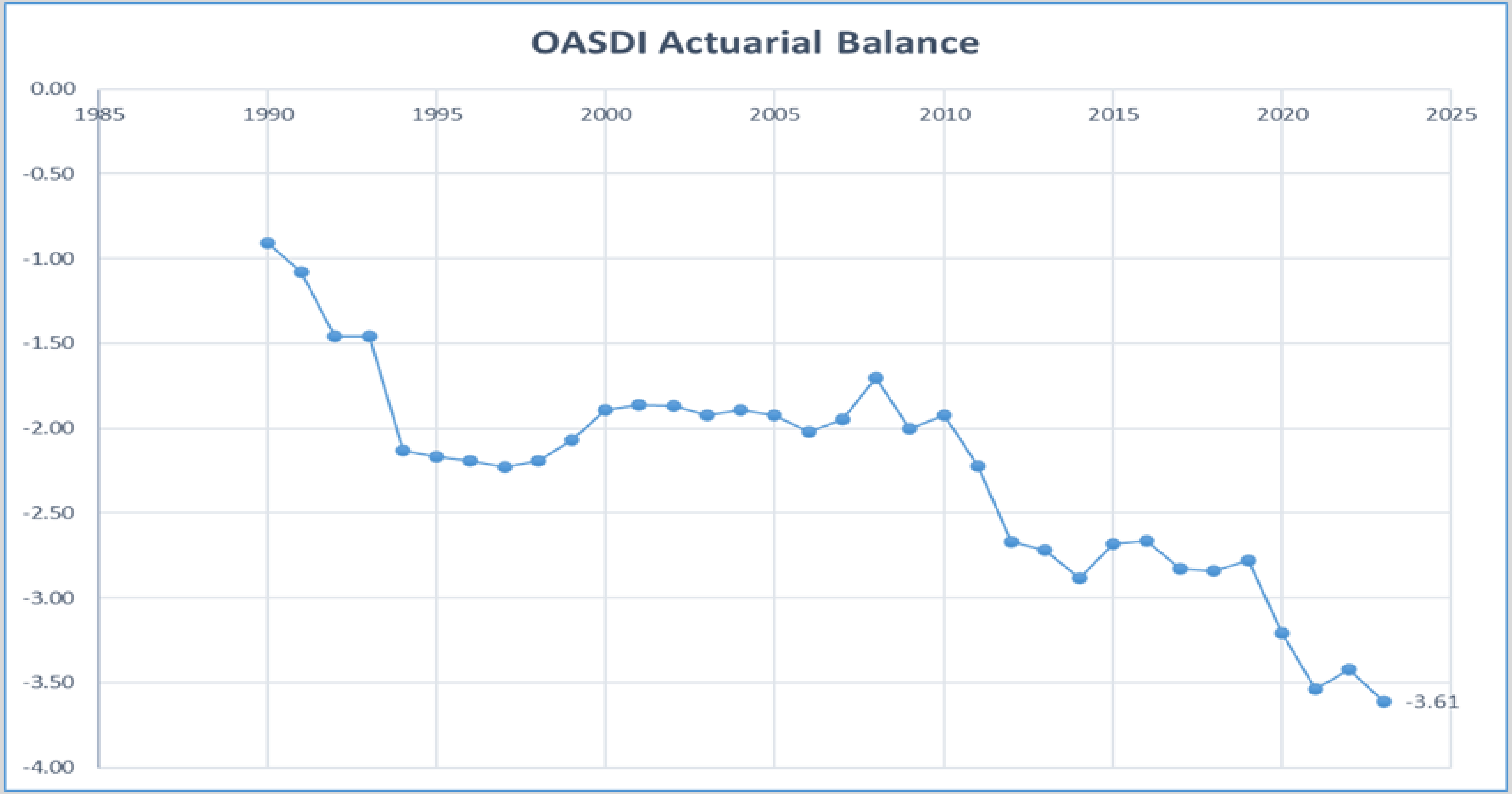
  - If the NMBs are insufficient to pay benefits and expenses, avoidance of benefit reductions is accomplished by Congressional authorization to transfer from another trust fund or the Treasury's General Account to the General Fund from which expenditures are made
    - Transfers from DI Trust fund occurred in 1982 and from the General Fund to the OASI trust fund occurred in 1983-89 and 2010-13

  - If the Trust Fund and NMBs never existed, all other things being the same, the total federal debt position of the US would not be different than it is today nor would it have been different at any time in the past

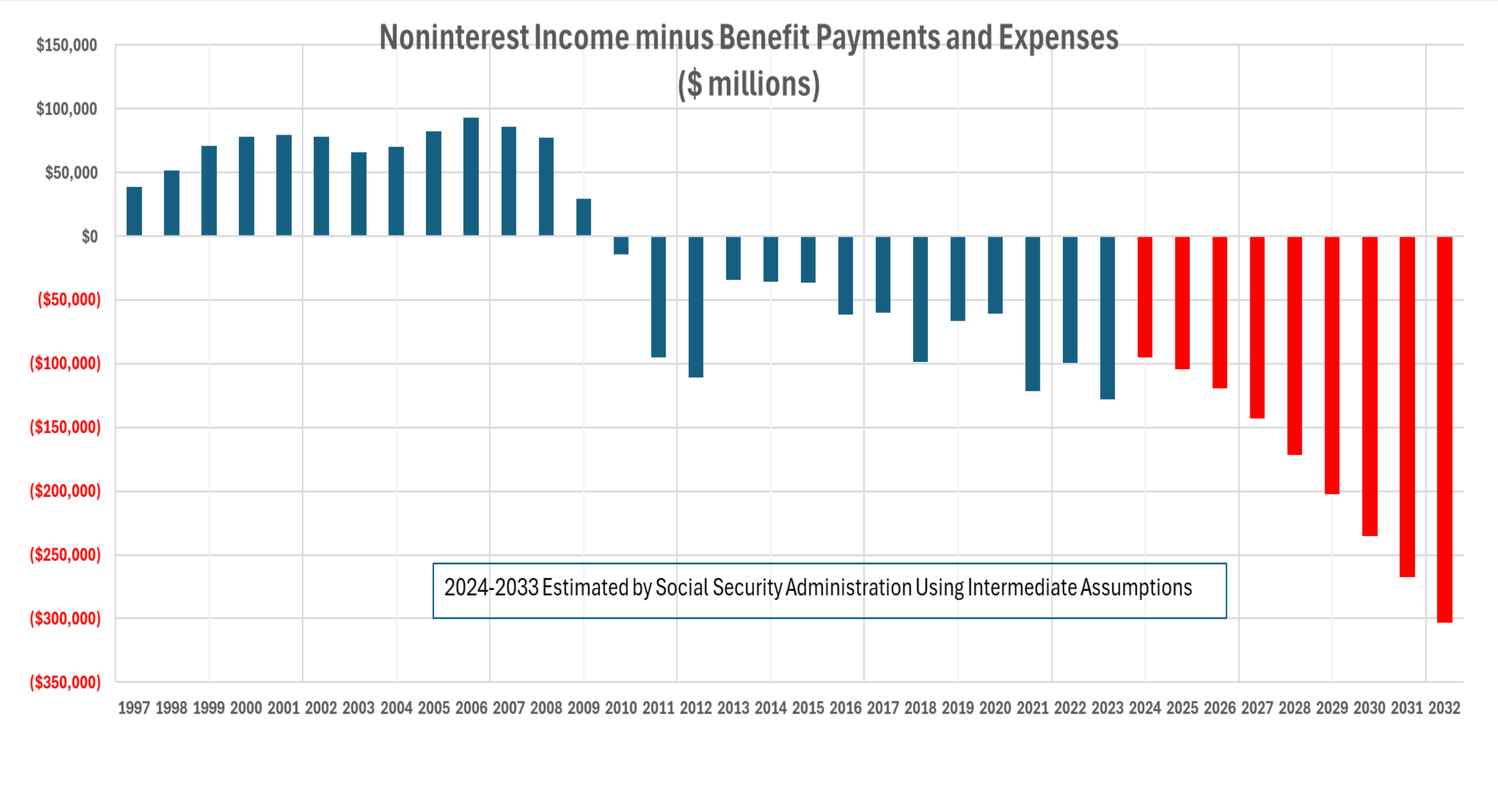
Social Security Solvency

- Trust Fund structure and existing law limits benefit disbursements to what can be covered by incoming OASI taxes and Trust Fund assets (NMBs)
- Since Social Security's inception in 1935, the Trust Fund has faced insolvency only twice
  - In the early 1980s when Congress authorized borrowing from the Disability Income (DI) and the Hospital Insurance (Medicare Part A, HI) Trust Funds to cover the shortfall
  - On a projected basis, in 2033, the OASI Trust Fund is again expected to become insolvent resulting in a potential reduction in benefits of roughly 25%
    - Over the next 10 years, scheduled benefit payments and expenses exceed payroll taxes by an estimated $273 billion in in 2024, growing to $546 billion in 2032
    - Neither the DI Trust Fund nor the HI Trust Fund or a combination have enough resources meet the OASI Trust Fund shortfall
    - Neither sufficient benefit reduction nor tax increase would be politically feasible to eliminate the projected Trust Fund insolvency
    - As a practical matter, if the current projections prove to be close to accurate, only borrowing or outright transfers from the Treasury's General Account or statutorily increasing the number of NMBs can prevent the projected OASI Trust Fund insolvency

Social Security Solvency



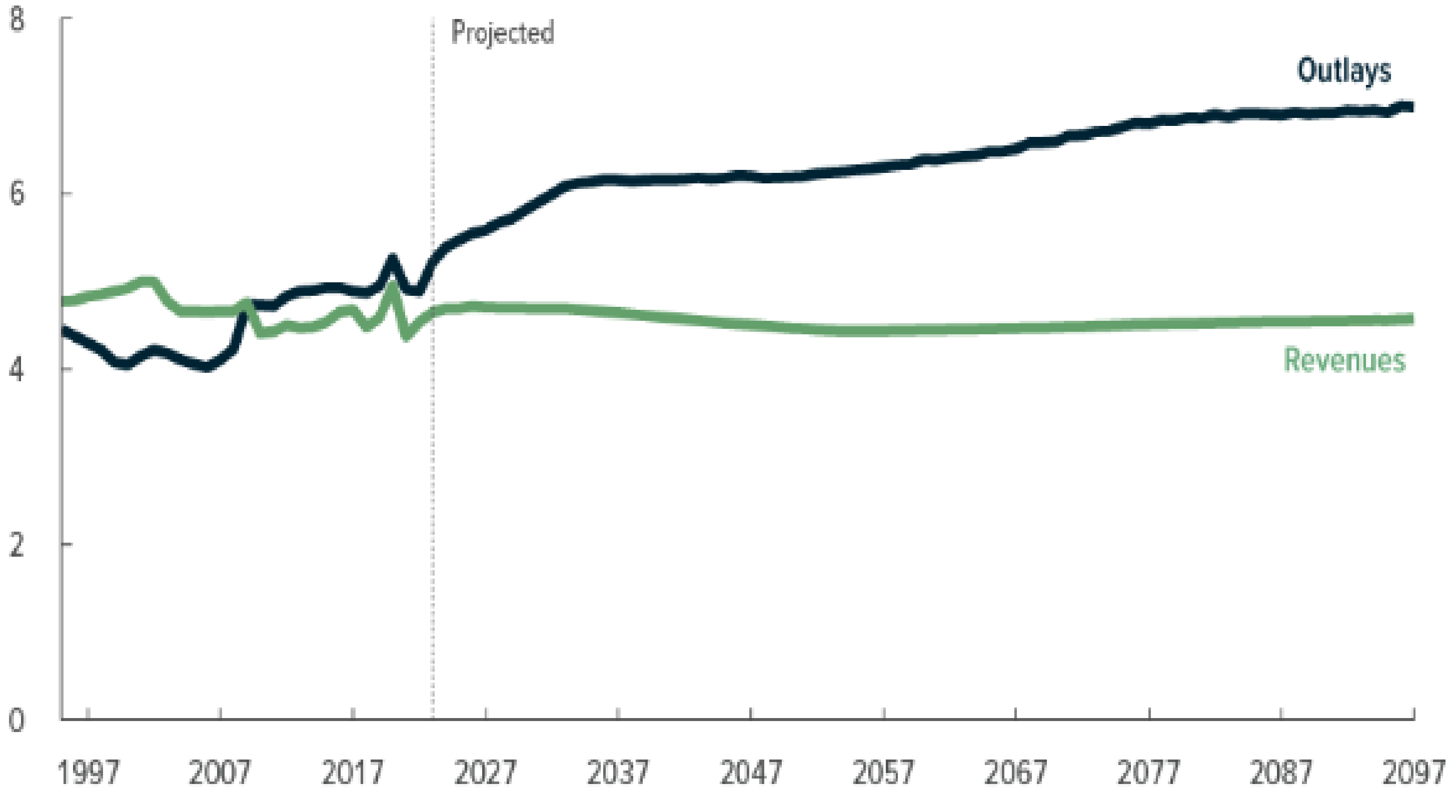
Social Security Solvency



Resolving Insolvency – Now and Forever

Social Security Outlays and Revenues, With Scheduled Benefits

Percentage of Gross Domestic Product



In CBO's projections, the gap between Social Security's outlays and revenues widens over the long term. Total spending on the program in 2023 is equal to 5.2 percent of GDP; by 2097, spending on the program reaches 7.0 percent of GDP. Over the same period, revenues remain at about 4.6 percent of GDP.

Resolving Insolvency – Now and Forever

Recommendations:

- Commit to funding shortfall with general revenues as in the past
- Replace the employee share of OASI taxes (which are regressive in nature) with an equal (deficit neutral) increase in the federal income tax rate
- Formally recognize Social Security operate as a pay-as-you-go system(s)
  - Eliminate OASI Trust Fund → Eliminate NMBs and convert to publicly-held debt, or
  - Retain the Trust Fund and NMBs and increase the interest crediting rate to something that keeps the Trust Fund out of insolvency, or
  - Retain Trust Fund and NMBs and provide legislation to support borrowing from the TGF
- Focus legislation on providing real resources

Questions

I welcome your comments and questions.

If you prefer, you can send your comments and questions to me at

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Thank you