PART 2

Social Security

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

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Slowing Down Social Security's Retirement Age Increase

This article was originally published at E21 on November 18, 2010.

In 2010 the Simpson-Bowles fiscal responsibility commission, formed by President Obama, issued its recommendations for repairing the federal budget outlook. These included recommendations to balance the finances of Social Security, the federal government's largest mandatory spending program. The plan contained a provision to very gradually increase the Social Security eligibility age.

Whether you like or dislike the commission proposals, some of the shriller attacks on them bore little reasonable relationship to the commission's recommendations or their broader policy context. In particular, this piece points out that the allegedly heartless eligibility age increases proposed in Simpson-Bowles were actually more gradual than ones already in the midst of taking effect under current law, without significant public outcry or notable hardship. While there are many other policy issues in our national policy discussion that suffer from insufficient seriousness, debates over Social Security's eligibility age have long remained among the most intemperate, to our shared detriment.

HERE'S A MULTIPLE-CHOICE TEST QUESTION ON THE RECENT PROPOSAL from Alan Simpson and Erskine Bowles, cochairs of the president's fiscal responsibility commission.

Complete the following sentence correctly. The Simpson-Bowles proposal would

A. sharply accelerate future increases in Social Security's normal retirement age (NRA) relative to those already occurring in the near term under current law.
B. slightly accelerate future retirement age increases relative to those already occurring in the near term under current law.
C. continue at the same rate future retirement age increases already occurring in the near term under current law.
D. slow down future retirement age increases relative to those already occurring in the near term under current law.

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The correct answer is . . . D.

Surprised? Based solely on public commentary about the proposal, nearly anyone would be. AFL-CIO President Richard Trumka declared that the commission had told working Americans to "Drop Dead" and suggested that its draconian plan "would have killed" his coal miner father.[1] Dr. Paul Krugman charged that the commission had been "hijacked" and asked rhetorically of the retirement age increase: "Is that reasonable? The answer is no."[2] And one news report after another has talked of "dramatic" changes the blueprint would make to Social Security.

The fact is that the Simpson-Bowles proposal would effect a slower future increase in the retirement age than that already occurring under current law. Do you remember the hue and cry when the Social Security retirement age rose by two months each year early in the first few years of the twenty-first century? Most likely not, because there was very little. Meanwhile, the rate of change proposed by Simpson and Bowles is actually four times slower than the aforementioned increase, and slower on average than the current-law increases set to occur throughout the entire first quarter of the 21st century.

Let's examine this in somewhat greater detail. Figure 1 is a graph of the proposed Simpson-Bowles NRA change, by worker birth year.

Under current law the NRA is rising by two years, phased in from those born in 1937 to those born in 1960. Under Simpson-Bowles, a subsequent two-year increase in the NRA would be phased in from those born in 1961 to those born in 2007. This is thus a substantial deceleration in the currently ongoing rate of increase. For perspective, consider that Simpson-Bowles would affect the NRA for today's 26-year-old worker by a grand total of one year.

The NRA, while important, is not the primary determinant of when individuals file for Social Security benefits. The majority of claimants file at early eligibility age (EEA), now 62. Simpson-Bowles would also increase this EEA. Figure 2 shows historic and proposed ages for earliest Social Security benefit claims (we'll refer to male workers for purposes of illustration).

When Social Security was first established, benefits could not be claimed until age 65. The 1956 Social Security amendments allowed women to claim benefits as early as age 62, an option extended to men in the 1961 program

1. Kathy Kiely, "Trumka on Social Security: Don't Raise Retirement Age," *National Journal*, November 11, 2010.

2. Paul Krugman, "The Hijacked Commission," *New York Times*, November 11, 2010.

Figure 1. Current Law and Proposed Changes in the Normal Retirement Age (NRA)

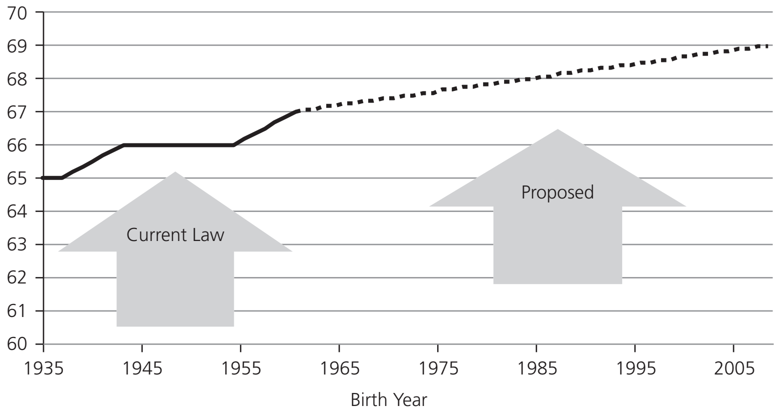
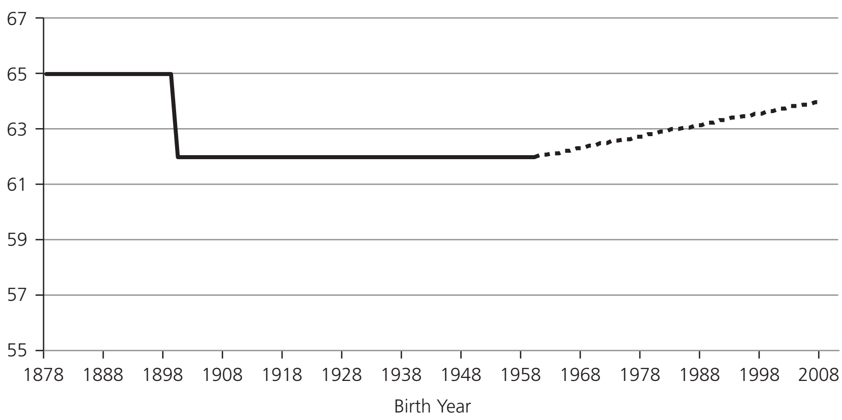


Figure 2. Historic and Proposed Ages of Earliest Benefit Eligibility



amendments.[3] Under Simpson-Bowles, the earliest age at which workers could claim benefits would gradually drift up again to approach—by the 21st century's end—only what it was originally under FDR. My four-year-old daughter would still be able to claim retirement benefits at an earlier age even than members of the generation that fought the Spanish-American war.

3. Library of Congress Congressional Research Service, Summary of Major Changes in the Social Security Cash Benefits Program: 1935–1996, December 20, 1996.

Is this "reasonable," given changes in worker health and longevity since Teddy Roosevelt's heyday, or should we avoid this adjustment and just hike my daughter's taxes instead? Let's remind ourselves of how longevity has changed over the last 70 years. For simplicity we'll use "period life expectancy," which only incorporates life expectancy changes to date rather than those anticipated over the rest of an individual's lifetime. (See figure 3.)

Clearly we are generally living much longer than when Social Security's retirement age of 65 was first established. This is one reason why the 1980–1981 Social Security Commission (less famous than the Greenspan Commission) recommended that Social Security's full eligibility age be raised to 68 by 2012.[4] Yet Dr. Krugman recently referred to the members of the Simpson-Bowles commission as "unserious people," in part for even considering a retirement age increase.[5]

We all have our own definitions of what constitutes "seriousness," but one of mine is that when one cites factual evidence in support of a policy argument, the evidence should actually substantiate that policy argument. In his criticism, Dr. Krugman argued that "the proposal seemingly ignores a crucial point: while average life expectancy is indeed rising, it's doing so mainly for high earners, precisely the people who need Social Security least. Life expectancy in the bottom half of the income distribution has barely inched up over the past three decades. So the Bowles-Simpson proposal is basically saying that janitors should be forced to work longer because these days corporate lawyers live to a ripe old age."[6]

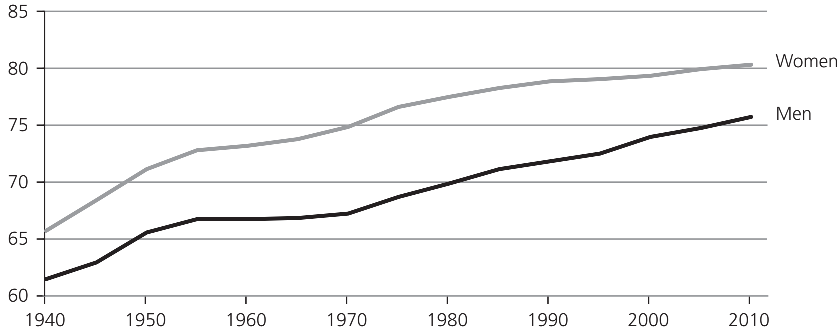
A perceptive reader presumably does not need to have the logical fallacy here spelled out, but let's do so anyway. Dr. Krugman's statement conflates two very different concepts:

1. There are mortality differences between professions and income levels,
2. Social Security's eligibility age for retirement benefits should not rise.

From a purely logical standpoint, the leap from concept 1 to concept 2 is a non sequitur. The fact that there are mortality differences does not by

4. National Commission on Social Security, *Social Security in American's Future*, March 1981.
5. Paul Krugman, "The Conscience of a Liberal," *New York Times*, November 10, 2010.
6. Krugman, "Hijacked Commission."

Figure 3. Period Life Expectancy by Birth Year



itself tell us what Social Security's eligibility age should be. It doesn't tell us whether it should be higher, lower, or the same as it now is.

Moreover, it would clearly make little sense to argue that simply because there is someone in America who is suffering from physical debilitation, the government should provide for subsidized retirement at age 62 for everyone. We arrive at sensible policies by determining what makes the most sense in the general case, and by providing for sufficient policy flexibility to address variations in individual experience.

The empirical evidence is clear that a physical inability to work is not the sole or even the primary determinant of workforce participation rates for those in their 60s. In 1955, 57% of American males aged 65–69 were in paid employment. By 1975, this had declined to 32%. This wasn't because American workers in 1975 were suddenly breaking down where those in 1955 had been leading comfortable, sedentary lives. Instead, this reflected a number of factors—including the increasing generosity of Social Security retirement benefits.

In any case, the Simpson-Bowles plan does not "ignore" the differential mortality issue. While it would gradually increase the retirement eligibility age in recognition of longer life spans, it would also provide physical laborers with greater flexibility in benefit claims with a new "phased retirement option" through which they could claim "half their benefits early and the other half at a later age."[7] The plan would furthermore direct the Social

7. "Co-chairs' Proposal," draft document, November 10, 2010.

Security Administration to design a new method to provide for early retirement benefits for those in "physical labor jobs."[8]

Thinking through the policy issues requires recognition that the Social Security program contains different components: a disability insurance component for those physically incapable of paid employment and an "old-age and survivors insurance" (OASI) program that provides benefits for individuals irrespective of their physical capacity to work. The Simpson-Bowles proposal to increase the eligibility age applies to the old-age program, not to the disability benefits for those physically unable to work.

Some may not realize that current Social Security law already facilitates a more lenient application of disability standards for physical laborers if the retirement age is increased. The Social Security Act is explicit that the age of the applicant is a factor in disability determinations.[9] Social Security Administration regulations also specify that the disability criteria applied at "advanced age" (over 55) are more lenient that those applied to young workers (and those applied to individuals "closely approaching retirement age" are more liberal still),[10] resulting in a greater likelihood of benefit awards for workers toward the end of their careers.

As American society ages, the question of Social Security's benefit eligibility ages reflects an important national value judgment. One possible choice is for us to translate our longer, healthier lifetimes solely into longer periods of paid retirement, resulting in substantially higher tax burdens on workers. A theoretical opposite choice would be to translate our longer, healthier lifetimes solely into longer working careers, lowering tax burdens per worker.

But while different individuals are entitled to make different judgments about the merits of these choices, no one is entitled to mischaracterize the judgments in the Simpson-Bowles proposal: that plan would still result in 21st century Americans spending a much greater share of their lives in retirement than they did in the 20th century. The Simpson-Bowles proposal does not ignore—but rather provides for—circumstances facing physical laborers. And their proposal is for a slower retirement age increase than the one already on the books.

8. "Co-chairs' Proposal."

9. Social Security Administration, "Compilation of the Social Security Laws Disability Insurance Benefit Payments," https://www.ssa.gov/OP_Home/ssact/title02/0223.htm.

10. 45 Fed. Reg. 55584 (August 20, 1980), as amended at 56 Fed. Reg. 57944 (November 14, 1991); 68 Fed. Reg. 51164 (August 26, 2003); 73 Fed. Reg. 64197 (October 29, 2008).

Is It Becoming Too Late to Fix Social Security's Finances?

This article was originally published at E21 on August 31, 2012.

This next piece has a theme of substantial importance to a public that cares deeply about Social Security—and a theme that requires no especial expertise to be grasped. Its message warrants far more attention than it generally receives.

The piece's essential point is that, for various reasons, our national window of opportunity to maintain Social Security's historical financing structure is now in the process of closing. Whereas previous program rescues occurred when it was still possible to repair program finances without significant near-term disruptions, waiting this time around until trust fund depletion is imminent will create a financing gap simply too large to close. This would likely require lawmakers to bail out Social Security from the general government fund, forever ending the perception of Social Security as a self-financed earned benefit—a perception that has historically given the program its unique political strength.

Properly understood, the reason Social Security finances are not now being dealt with is not because the problem is distant, but because the problem has already grown too large for elected officials to repair within the constraints of contemporary politics.

ONE OF MY DUTIES AS A PUBLIC SOCIAL SECURITY TRUSTEE IS TO EXPLAIN the program's financial condition, both formally as a signer of the annual board report and less formally in published summaries, articles, interviews, and congressional testimony.[1] This evaluation is written pursuant to that responsibility.

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1. OASDI Board of Trustees, *The 2012 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, April 25, 2012; Social Security and Medicare Boards of Trustees, "A Summary of the 2012 Annual Reports," 2012, Social Security Administration, https://www.ssa.gov/OACT/TRSUM/2012/index.html.; Charles Blahous, "A Guide to the 2012 Social Security Trustees Report," E21 (Manhattan Institute for Policy Research), April 26, 2012; Stephen Ohlemacher, "Social Security Surplus Dwarfed by Future Deficit," *Post-Bulletin*, August 16, 2012; Charles Blahous, "Statement of Charles P. Blahous, Public Trustee for Social Security, before the Subcommittee on Social Security of the U.S. House of Representatives Committee on Ways and Means," June 21, 2012.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Social Security's future, at least in the form it has existed dating back to FDR, is now greatly imperiled. The last few years of legislative neglect—due to a failure of national policy leadership coming just as the baby boomers have begun to retire—have drastically harmed the program's future financial prospects. Individuals now planning their financial futures, whether as taxpayers or as beneficiaries, should be pricing in a substantial risk that the federal government will not be able to maintain Social Security as a self-financing, stand-alone program over the long term. If Social Security financing corrections are not enacted in 2013, or at the very latest by 2015, it becomes fairly likely that they will not be enacted at all.

Below I will first explain how the Social Security shortfall is usually described and approached. Then I will explain why Social Security's financial prospects are much grimmer than is commonly understood. Finally I will explain why this matters: that is, the likely consequences if the president and Congress continue to fail to balance its books.

Common Measures of the Social Security Shortfall

Social Security's long-term financing shortfall is now estimated at 2.67% of the program's tax base (worker wages). Insolvency of the program's combined trust funds is now projected for 2033 (2016 for its disability program). Figures such as 2033 and 2.67% make it appear—incorrectly—as though there are several years remaining to act, and only a modest problem to solve.

Multiple Solutions

There is no shortage of Social Security reform proposals that would, at least on paper, successfully shore up program finances. I personally have put forward some, and the Social Security Actuary has scored several others.[2] Proposals from the right tend to focus on cost containment (e.g., slowing the growth of benefits and/or raising eligibility ages), whereas proposals from the left tend to focus on raising taxes.[3] As I explain below, this multitude of proposals in no way implies that a solution is readily achieved.

2. Charles Blahous, *Social Security: The Unfinished Work* (Stanford, CA: Hoover Institution Press, 2010); Social Security Administration, "Office of the Chief Actuary's Estimates of Proposals to Change Social Security," https://www.ssa.gov/OACT/solvency/index.html.

3. Peter Diamond and Peter Orszag, "No Revenue Means Steep Social Security Cuts under Romney," *Bloomberg View*, March 27, 2012.

Why a Solution Is Rapidly Becoming More Difficult

There are several reasons.

- The baby boomers are starting to retire. Lawmakers have historically been very reluctant to cut benefits for beneficiaries once they start receiving them. This means that any sacrifices will likely be concentrated on younger generations who already face net income losses through Social Security as it is.[4] With every further year of delay, lawmakers must therefore consider sharper benefit growth reductions and/or tax increases.
- A solution requires substantial compromise by one or both sides. If one person (or a unified political party) commanded total political power and was willing to use it, they could impose a preferred solution on those who disagreed. The last such opportunity was probably 2009–2010 when Democrats controlled both chambers of Congress and the White House. Had they so chosen, they could have shored up Social Security on their own terms. No such attempt was made. Today no one expects that either party will single-handedly control the White House, the House, and 60 votes in the Senate within the next few years. Thus if Social Security finances are to be repaired, someone must dramatically compromise: progressives must accept substantial benefit growth reductions, conservatives must accept substantial tax increases, or both. Unfortunately, as I will show below, we are already long past the point where there is precedent for a compromise of this magnitude.
- There is a huge disparity between the problem's urgency and the rhetoric applied to it by substantial factions of the body politic. Even as time is running out for a workable compromise, some continue to play a high-stakes gamble: that if the urgency is downplayed and action delayed past the next few elections, it can be dealt with when the political alignment may be more advantageous to one side.[5] This gambit has now been extended to the point of imperiling Social Security's long-term outlook. Too many key players, however, do not yet realize this.

4. OASDI Board of Trustees, *The 2012 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds,* April 25, 2012, B. Long-Range Estimates.
5. Jacob Lew, "Opposing View: Social Security Isn't the Problem," *USA Today*, February 21, 2011.

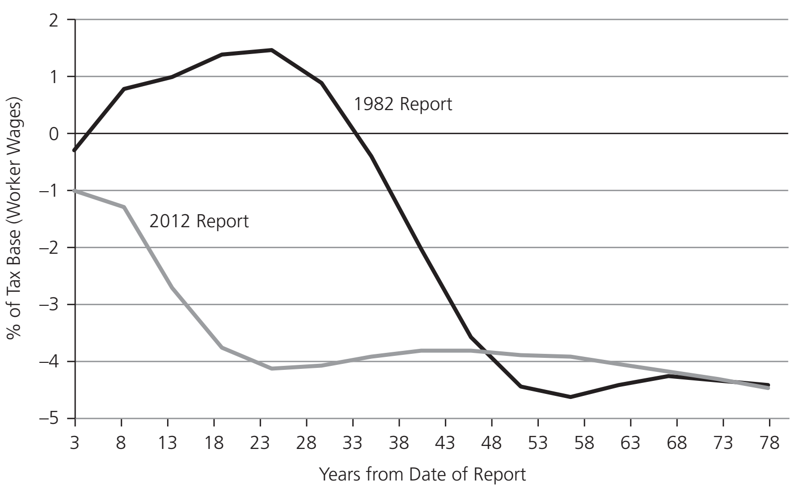
No Bipartisan Grand Bargain Has Ever Eliminated a Social Security Shortfall This Large

The historical high-water mark for a comprehensive bipartisan rescue was the 1983 Social Security amendments. The program was then saved from the brink of insolvency. Benefit checks had literally been just months away from being interrupted. Both sides agreed on the urgency and immediacy of the crisis, yet very nearly failed to reach agreement.

The program's long-term shortfall in 1982 was measured as 1.82% of the program's tax base. Today it's measured as 2.67%—much larger even on the surface. Yet many don't realize that the trustees' methodologies were changed in 1988 to make the shortfall appear smaller. If we still measured as was done in 1983, today's shortfall would be 3.5% of the tax base—nearly twice as large as the 1983 gap.

Figure 1 compares current projections with those made at the time of the 1982–1983 crisis, specifically for the 75-year period immediately following each report. The graph shows projected differences between annual "non-interest" income (payroll taxes, benefit taxes, and any general revenues) and the cost of paying benefits, in relation to the program's tax base. Points above the zero line indicate an annual surplus; points below indicate an annual

Figure 1. Projected Social Security Annual Balances (2012 vs. 1982 Reports)



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deficit. Because in 1982 long-term projections were only specified for years that were multiples of 5 (2015, 2020, etc.), I mark the estimates at spans of 3, 8, 13, etc., years from the dates of the respective reports.

It's immediately visually apparent that today's long-term problem is not only worse than in 1982–1983, but much worse. Shortfalls over the long term equal roughly 4% of the program's tax base in either case. The big difference is in the near term; we're now 20 years closer to deficits of that magnitude than policymakers were then, and must effectuate large corrections much more rapidly.

In the early 1980s policymakers merely had to get through a relatively small near-term solvency crisis before entering decades of previously projected surpluses as the baby boomers moved through the workforce. The 1983 reforms could thus be much gentler than those required today.

Yet even the 1983 adjustments were nearly more than the political system could bear. Lawmakers had to delay cost-of-living adjustments by six months, bring federal employees (and their payroll taxes) into the program, and expose beneficiaries to new benefit taxation, among other measures. These measures were intensely controversial and strained the limits of political salability—yet were far less drastic than a solution today requires.

A solution enacted today would require Left and Right to cede roughly twice as much ground as they did in the 1983 reforms, or one side must cede still more. Each year that passes, influential players must retreat still further from their preferred policies. At some point (which we may well be past already), one side, the other, or both will reach the limit of how much it is willing to swallow.

The fate of the Simpson-Bowles Social Security proposal exemplifies how difficult forging a compromise has become.[6] That proposal, developed by the bipartisan cochairs of President Obama's fiscal responsibility commission, was Solomonically divided almost 50–50 between revenues and cost constraints (46–54, exactly). The Obama White House distanced itself from the proposal after it was repeatedly attacked by many of the president's political allies.[7] It failed to receive the requisite support on the commission, with defections on both the Republican and Democratic sides. Such political

6. Social Security Administration Office of the Chief Actuary, *Letter to the National Commission on Fiscal Responsibility and Reform*, December 1, 2010.

7. "Strengthen Social Security . . . Don't Cut It: The Bowles-Simpson Plan Would End Social Security as We Know It," *Strengthen Social Security*, accessed May 31, 2012.

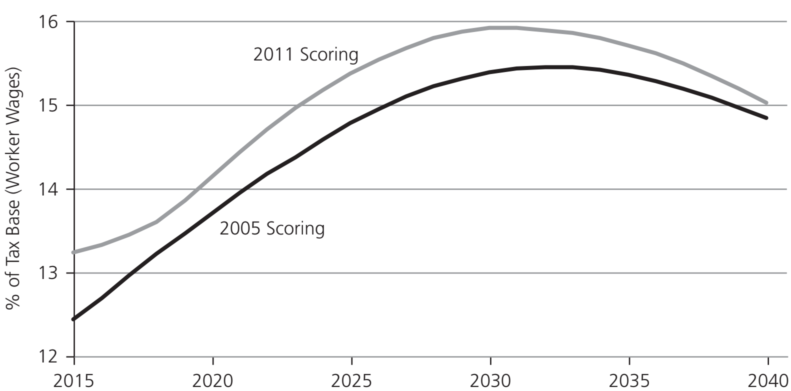
heat is only going to grow more intense: due to subsequent deterioration in system finances, the next solution debated will need to impose even tighter financing constraints than Simpson-Bowles proposed.

Some of the Toughest Solutions Proposed Already No Longer Work

As another illustration of the growing difficulty of solution, let's look at the competing approaches of containing cost growth and raising taxes. One longstanding proposal has been to slow future benefit growth to the rate of price inflation for high earners, while allowing low-income earners the higher growth rate of wage inflation and leaving previous beneficiaries unaffected. But already, even if we slowed everyone's benefit growth—from the poorest to the richest—to price inflation, we could no longer maintain solvency while holding harmless those over the age of 55. (See figure 2.)

The graph shows how six years of delay have increased the cost of this particular approach. Had across-the-board price indexing been enacted in 2005, it could have kept Social Security fully solvent, left those over 55 untouched, and generated additional funds to provide for faster benefit growth on the low-income end. Enacted last year, however, such across-the-board price-indexing would no longer be enough; costs would be substantially higher and the trust funds would be depleted in 2040 unless further measures were taken. And if rescored under 2012 assumptions, this proposal would fare still worse.

Figure 2. Annual Social Security Costs If Benefits Are Indexed to Prices



The efficacy of tax-increase solutions is also fading with delay. Advocates on the Left sometimes argue to increase the amount of Social Security wages subject to the payroll tax. The most extreme version of this proposal would be to raise the amount of wages subject to the full 12.4% payroll tax—$110,100 today—up to infinity. Yet even this drastic measure would now fail to keep Social Security in long-term balance.

We are thus approaching the point where each side would have difficulty balancing Social Security finances even if it could dictate the solution—and rapidly passing the point where a compromise solution remains reasonably likely. What does this mean for Social Security's future?

Toward a Very Different Social Security Program

If a financing solution cannot be reached, then Social Security's self-financing construct would need to be abandoned. Assuming the program continues to pay benefits, it would have to permanently rely on subsidies from the general fund, as Medicare now does. This would be a valid policy choice, but it carries unavoidable consequences. It would mean an end to one of the program's foundational principles: the requirement that Social Security pay its own way through a separate trust fund. It would also mean an end to FDR's conception of an "earned benefit" program in which workers are seen to have paid for their own benefits.

Upon merging into the general fund, Social Security benefits would be far less secure going forward. Benefit payments would have to compete with other annual spending priorities, and would be limited to those deemed affordable given pressures elsewhere in the budget. They would thus be much more susceptible to sudden reductions, means-tests, and other episodic changes to which general fund–financed programs have long been subjected.

If this all happens, and renders tomorrow's Social Security benefits less secure than today's, it would be a tragic irony: the outcome would have been brought about largely by supporters of Social Security having countenanced the tactics of delay to the point that the program's unique political protections could no longer be preserved. Those who care about the Social Security program need to clearly understand the consequence of this ongoing neglect: that time for a realistic financing solution has nearly run out.

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(Arlington, VA: Mercatus Center at George Mason University, 2020).

The End of Social Security Self-Financing: What Next?

This article was originally published at E21 on October 10, 2012.

As with several other pieces in this volume, this article was based on a longer study performed for the Mercatus Center. The title of the piece was deliberately provocative, perhaps best understood as half a description of what has already taken place and half a prediction of what will become inevitable. Its purpose was to acquaint readers with a critical divide that has recently opened: While on the one hand most people still think of Social Security as a standalone system, on the other hand its self-financing framework is eroding, both in terms of concrete policy changes and as a governing philosophical ethic.

Growing sections of the body politic are no longer willing to sustain Social Security's self-financing framework in practice even as they express support for it in principle. A smaller but also-growing political faction is abandoning the self-financing principle itself. The result, for better or for worse, is that Social Security is likely in the process of becoming a dramatically changed system without most of the public even being informed of the change, much less approving it.

TODAY [OCTOBER 10, 2012] THE MERCATUS CENTER IS RELEASING MY study titled "The End of Social Security Self-Financing: What Does It Portend for Social Security's Future?"[1] The piece explores the implications of the Obama administration and Congress having recently cut the Social Security payroll tax and financed benefit payments from the general government fund, thereby ending decades of bipartisan commitment to FDR's original vision for Social Security—that it be a self-financing program in which total benefits were limited by the amount of worker contributions. This financing change has the potential to fundamentally transform the future Social Security debate, possibly affecting important policy choices ranging from its rate of benefit growth to whether a contribution-benefit

1. Charles Blahous, "The End of Social Security Self-Financing: What Does It Portend for Social Security's Future?" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2012).

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

link is maintained to how eligibility ages are set to whether formal means-testing is adopted.

News reports indicate that the payroll tax cut will be allowed to expire at the end of this year.[2] There are, however, no indications that lawmakers will reverse the substantial general revenue subsidies that were deposited in the Social Security trust funds to compensate for it. Approximately $217 billion in such subsidies have been provided to Social Security. These subsidies do not reflect any incoming tax collections and their costs are simply being added to the national debt. Moreover, because these transfers to the trust funds earn interest, by 2033 they will have compounded to require future taxpayers to subsidize roughly $600 billion in Social Security benefit payments beyond what beneficiaries paid for. It remains to be seen what effect this policy change will have on public perceptions that Social Security is an "earned benefit."

My study details the following aspects of the policy change.

The Long History of the Self-Financing Principle

A foundational idea underlying Social Security historically was that it was not supposed to be welfare. In a welfare program it's not required that tax contributions and benefit payments balance, individually or collectively. One individual might receive benefits despite having never paid taxes, whereas another might contribute taxes but draw no welfare benefits. FDR wanted Social Security to be different. He insisted that it be financed under contributory insurance principles, with total benefits limited to the amount of worker contributions plus interest. The perception that workers had—at least as a group—paid for their benefits was FDR's means of safeguarding the program's political support. As he put it,

> We must not allow this type of insurance to become a dole through the mingling of insurance and relief. It is not charity. It must be financed by contributions, not taxes. . . . I expressed my opinion that full solution of this problem is possible only on insurance principles. It takes so very much money to provide even a moderate pension for

2. Annie Lowrey, "Payroll Tax Cut Is Unlikely to Survive into Next Year," *New York Times*, September 30, 2012.

> everybody, that when the funds are raised from taxation only a "means test" must necessarily be made a condition of the grant of pensions.[3]

For decades, a strong, bipartisan majority remained firmly committed to FDR's vision. The political Right valued the contribution-benefit link as ensuring critical fiscal discipline, whereas the Left valued it for protecting benefits from having to compete annually with other programs for funding. Social Security advisory councils over the decades repeatedly endorsed self-financing, up to and including President Clinton's 1994–1996 council, which unanimously opined that Social Security should be financed "without other payments from the general revenue of the Treasury."[4]

Cracks in the Consensus

This consensus commitment to self-financing first began to erode in the late 1990s. In 1999 President Clinton proposed transferring general revenues to the trust funds to "save the surplus" for Social Security. In the following decade many other left-of-center advocates suggested breaking the program's contribution-benefit link by having higher-income taxpayers contribute additional taxes to the program without earning associated benefits.[5]

As the commitment to Social Security self-financing ebbed in some quarters, there arose a parallel desire to cut low-income workers' payroll tax burdens. This occurred for several reasons.

- One was a misperception that the payroll tax was "regressive." Actually, Social Security net tax burdens (taxes net of benefits) are quite progressive, as figure 1 shows. The misperception that its financing system is regressive is based on viewing only one side of the equation: the payroll tax assessments but not the benefits they create. Because the Social Security payroll tax would clearly never

3. Social Security Administration, "FDR's Statements on Social Security," https://www.ssa.gov/history/fdrstmts.html.

4. Social Security Administration, *Report of the 1994–1996 Advisory Council on Social Security*, vol. 1, *Findings and Recommendations*, January 1997.

5. Social Security Administration, "Memorandum on Estimates of Financial Effects for a Proposal to Restore Solvency to the Social Security Program," October 8, 2003; Social Security Administration, "Memorandum on Estimated OASDI Financial Effects for a Proposal with Six Provisions That Would Improve Social Security Financing," April 14, 2005; Social Security Administration Office of the Chief Actuary, Letter to Rep. Peter DeFazio, March 3, 2011; Social Security Administration Office of the Chief Actuary, Letter to Senator Bernard Sanders, September 7, 2011; Social Security Administration Office of the Chief Actuary, Letter to Rep. Robert Wexler, July 2, 2009.

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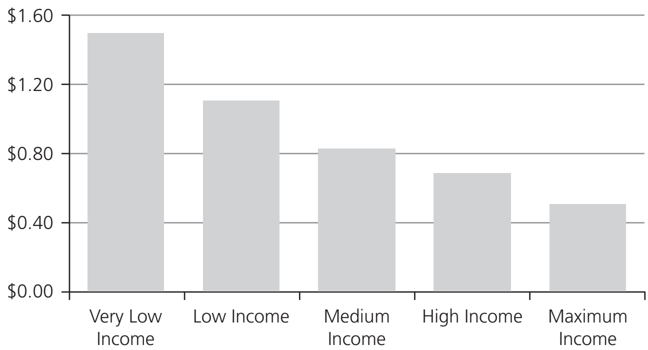
have been established without accompanying benefits, this one-sided view is incomplete at best.

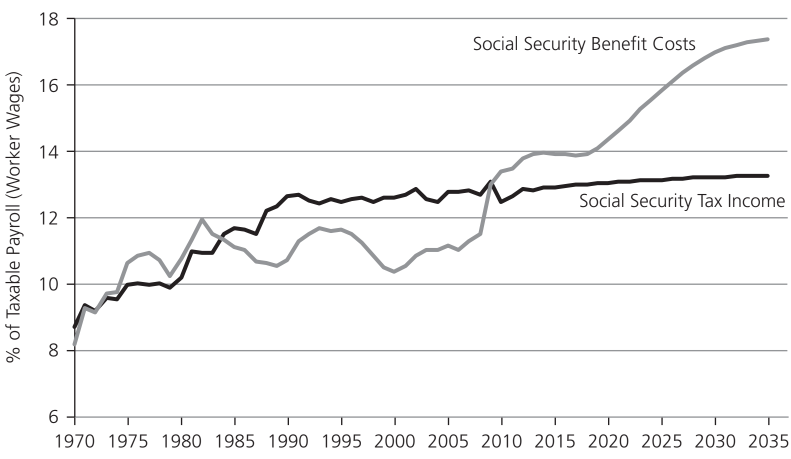
- Second, Social Security benefits have steadily risen to levels requiring higher tax burdens than lawmakers remain comfortable assessing throughout good times and bad. (See figure 2.)

Figure 1. Lifetime Benefits Received for Each $1 of Payroll Tax Contributions (Two-Earner Couple, Birth Year 1964)



Source: Social Security Administration Office of the Actuary.

Figure 2. Annual Social Security Cost Burdens Relative to Worker Wages



Source: Social Security trustees' report.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

- Third, policymakers intermittently wish to provide "tax relief" to workers who pay no income taxes—a contradiction often resolved by misportraying refundable tax credit payments as payroll tax relief (even when policymakers had no intention of actually cutting income to the Social Security Trust Fund, nor the benefits these payroll taxes finance).
- Finally, some (especially younger) left-of-center advocates now take it for granted that Social Security's ongoing political support will remain strong even if the historical self-financing principle is abandoned.

The rising desire to replace Social Security's contributory payroll tax financing with general fund subsidies was by no means shared by all left-of-center Social Security policy advocates. Some, such as Nancy Altman, strongly criticized the recent payroll tax cut out of a conviction that Social Security's self-financing principle remained the cornerstone of its future viability and political strength.[6]

Abandoning Self-Financing

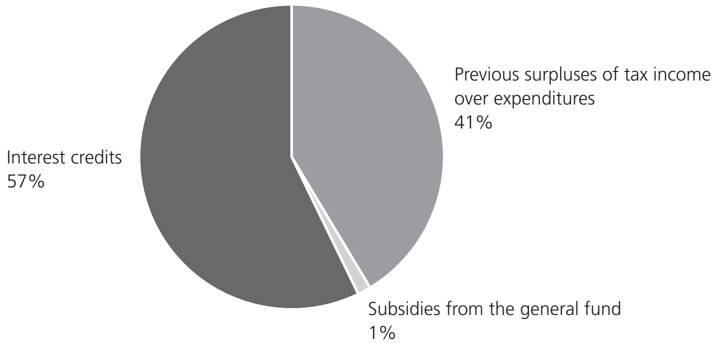
In 2011–2012 lawmakers cut the Social Security payroll tax to its lowest level in decades. The legislation included the following language:

> There are hereby appropriated to the Federal Old-Age and Survivors Trust Fund and the Federal Disability Insurance Trust Fund established under section 201 of the Social Security Act (42 U.S.C. 401) amounts equal to the reduction in revenues to the Treasury by reason of the application of subsection (a). Amounts appropriated by the preceding sentence shall be transferred from the general fund at such times and in such manner as to replicate to the extent possible the transfers which would have occurred to such Trust Fund had such amendments not been enacted.

Overnight this provision transformed Social Security from a program in which general revenue financing had historically been negligible to one that relied significantly on subsidies from the general fund. By the end of 2012, only 28% of the Social Security trust funds balance will reflect prior surpluses of Social Security tax income over expenditures. (See figures 3 and 4.)

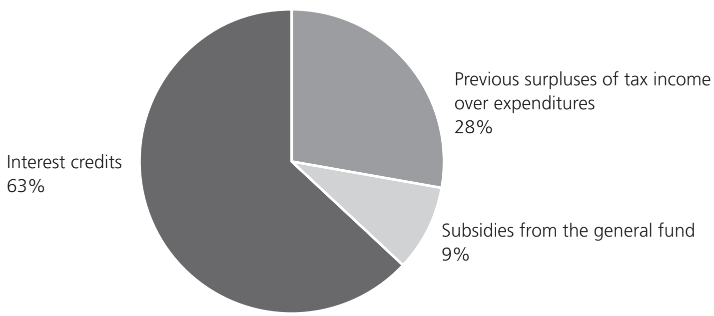
6. Nancy Altman, "The End of Social Security," *Shadow Proof*, December 7, 2010.

Figure 3. Components of the Social Security Trust Funds, End of Year 2010



Note: Percentages do not sum to 100 due to rounding.

Figure 4. Components of the Social Security Trust Funds, End of Year 2012



Potential Policy Implications

There are essentially four possible future courses for Social Security policy, given the recent incorporation of substantial general revenue subsidies.

1. *Continuation*. Social Security continues to receive substantial subsidies from the general fund while its historical ethic of self-financing is tacitly abandoned.
2. *Recurrence.* The current general revenue subsidies are allowed to terminate on schedule, but a precedent is established whereby lawmakers feel few inhibitions about resuming such subsidies whenever they believe other policy considerations warrant doing so.

3. *Termination with lasting policy effects.* The general revenue subsidies terminate on their current schedule and are not revived, but public perceptions of Social Security's role are significantly affected by awareness that benefit payments have been subsidized from the general fund.
4. *Termination with no lasting policy effects.* The general revenue subsidies terminate on their current schedule, public awareness of the subsidies remains limited, and lawmakers henceforth treat the 2011–2012 practice as a one-time exception to longstanding policy.

There is no way to know which course will be taken, but under three of these four scenarios Social Security's future is likely to be quite different from its past. Historically, programs financed from the general fund have been treated very differently from Social Security. These differences reflect a dynamic in which general fund financing induces many lawmakers to value the interests of income taxpayers on a par with those of beneficiaries.

Benefits in general-fund-financed programs have historically been much more changeable than Social Security's, with revisions of eligibility criteria and means tests being particularly frequent. Moreover, certain features of current Social Security benefit growth (such as wage-indexing of its initial benefit formula) are extremely atypical of other federal programs, which are usually indexed to grow more slowly. Finally, if it is no longer required that Social Security tax collections be sufficient to finance its benefit payments, the historical pattern of payroll tax rate and base increases may well discontinue.

Table 1 summarizes possible changes to Social Security policy in the post-self-financing era.

A fuller discussion of why general revenue financing may lead to these specific policy changes is included in my study.[7]

In sum, the recent policy of cutting the Social Security payroll tax and financing the program from the general fund represents a fundamental departure from its longstanding financing basis and a philosophical break with the vision of FDR. The long-term policy implications are not yet clear.

7. Blahous, "End of Social Security Self-Financing."

Table 1. Possible Changes to Historical Social Security Policy Principles under General-Fund Financing

Policy factor	Historical principle	Possible change
Payroll taxes	Raise periodically as necessary to finance scheduled benefit obligations.	Argument for future payroll tax increases weakened; acceptable for payroll tax collections to fall short of benefit obligations.
Means testing	Full benefit eligibility for all contributors regardless of non-Social Security income.	Eligibility based in part on need in the manner of other general revenue–financed programs.
Wage indexing of initial benefit formula	Benefits indexed to remain a constant share of pre-retirement wages.	Benefits grow with price inflation in the manner of other general revenue–financed programs.
Contribution-benefit link	Benefit entitlement a reasonably direct function of individual payroll tax contributions.	Formula redrawn to provide limited safety-net benefit for all, irrespective of individual tax contributions.
Eligibility ages	Set to ensure that vast majority can withdraw old-age benefits.	Raised to target benefits on those most at risk of outliving pre-retirement savings.

To the extent, however, that the current general-fund subsidies are either precedential or undermine perceptions of Social Security as an earned benefit, they could mean an end to political dynamics that historically have rendered Social Security unique, prompting renewed consideration of policy options traditionally applied only to what have been popularly thought of as welfare programs.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Understanding Social Security Benefit Adequacy: Why Benefit Growth Should Be Slowed

This article was originally published at E21 on January 31, 2013.

This is probably one of the more important pieces in this collection, insofar as it draws on substantial research performed for the Mercatus Center, presenting Social Security benefit information not widely available elsewhere. Often lost in the recurring debate over whether and how to adjust Social Security benefit schedules is a broader explanation of the speed at which benefits grow already under current law. Many people are vaguely aware that Social Security benefits are indexed to grow automatically in some way, but discussions of proposed reforms still foster the misimpressions that changes would result in "cuts" from current benefit levels or reductions relative to the rising cost of living. Neither perception is typically accurate.

The piece explained three phenomena concerning Social Security benefits: first, that the rate of benefit growth is already sufficiently rapid that the burden of financing its costs causes worker standards of living to decline relative to retirement benefits; second, that current policy pushes low-income people into suboptimal choices with respect to savings and workforce participation; and third, that Social Security over time pays rising benefits for a given real wage level. Thus, as the piece notes, the program's benefit formula implicitly reflects a highly questionable value judgment that "as society grows generally richer, the federal safety net should expand so that benefits for workers with a given real wage level automatically become more generous." The system operates counter to the value judgment many people make instinctively, that poorer people need more government assistance, and thus that a wealthier society should need less.

MANY FEDERAL POLICYMAKERS ARE AWARE THAT THE SOCIAL Security program faces a substantial financing shortfall requiring correction.[1] Correction would involve either increasing program taxes or slowing the growth of benefits—most likely both, given the size to which the shortfall

1. Social Security and Medicare Boards of Trustees, "A Summary of the 2013 Annual Reports," 2013, Social Security Administration, https://www.ssa.gov/OACT/TRSUM/2013/index.html.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

has already grown in addition to the fact that neither party enjoys sufficient political power to impose its preferred solution on the other.

Social Security tax increases and benefit growth restraints are both politically unattractive; but at least one or the other is necessary to balance the program's books if we intend to maintain Social Security as a self-financing program. Tax increases have obvious downsides that I have written about elsewhere and are not the subject of this article.[2] The consequences of slowing benefit growth also concern many policymakers—specifically, whether Social Security can continue to offer adequate income protections if current benefit growth schedules are slowed.

As it turns out, however, it is not only possible to preserve Social Security benefit adequacy while slowing benefit growth, it is actually necessary if policymakers wish to avoid forcing participants into sub-optimal outcomes.[3] This is good news, suggesting that Social Security cost restraints may embody a rare "win-win" policy opportunity. By slowing benefit growth, lawmakers can improve not only system finances, but the treatment of individual participants as well.

Background: Replacement Rates

To fully understand the issue of Social Security benefit adequacy, some familiarity is required with the "replacement rate" concept. Very loosely, a replacement rate is the ratio of one's post-retirement to pre-retirement income. Financial planners often invoke the concept when advising individuals on how much to save for their retirement. A typical financial planner might suggest that retirement income needs to be at least 70%–80% of pre-retirement income to maintain a consistent standard of living.

The current Social Security benefit formula is designed to hold replacement rates constant across time for certain similarly situated workers (as I will show, a very important specification) if benefits are claimed at the normal retirement age (NRA). To accomplish this, benefits are indexed under current law to grow with the national average wage index from one class of retirees

2. Charles Blahous, "Why Raising Social Security's Tax Cap Wouldn't Eliminate Its Shortfall," E21 (Manhattan Institute for Policy Research), April 12, 2011.

3. Charles Blahous, "Understanding Social Security Benefit Adequacy: Myths and Realities of Social Security Replacement Rates" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2012).

to the next. Since wages tend to rise over time relative to price inflation (CPI), this formula produces benefits that grow faster than consumer prices. (This wage-indexing of the initial benefit formula should not be confused with the often-discussed issue of what version of CPI should be used to calculate annual Social Security cost-of-living adjustments).[4]

Occasionally it is mistakenly said that Social Security benefits are scheduled to "decline" because under current law replacement rates at a fixed age, such as 65, will decrease.[5] This is not actually a benefit decline but an artifact of the fact that under current law Social Security's NRA will rise gradually to 67 by the early 2020s. Thus, individuals who retire at 65 thereafter will be subject to the reduction applied to early retirement benefits.

Calculating replacement rates at age 65 is clearly not the right way to measure benefit adequacy when the NRA is rising to 67. The scheduled NRA increase reflects a policy reality that, as Americans live longer lives, the optimal age for entering retirement also rises; no sensible retirement planning strategy calibrates benefits at a forever-unchanging retirement age without taking into account how long individuals are expected to live. It also makes little analytical sense to assume the policy goal is to enable individuals to retire at age 65 with a full benefit when lawmakers have deliberately chosen to raise the NRA to 67.

For these and other reasons, Social Security replacement rates—if invoked at all—are properly calculated at the NRA, when the individual is first eligible for full Social Security benefits. From this vantage point, there are a number of reasons why current-law Social Security benefit growth should be slowed, purely from a benefit-equity perspective.

Reason 1: The Current Formula Causes Pre-retirement Standards of Living to Decline Relative to Post-retirement Living Standards

The idea behind the current wage-indexing formula was to preserve benefit equity between generations; that is, to ensure that later cohorts received

4. Charles Blahous, "Reforming CPI: Not a 'Grand Bargain' but a Prudent Reform," E21 (Manhattan Institute for Policy Research), July 12, 2011 (republished in this collection).

5. John A. Turner, "Social Security Financing: Automatic Adjustments to Restore Solvency" (Research Paper #2009-01, AARP Public Policy Institute Pension Policy Center, Washington, DC, February 2009).

benefits that were as high a percentage of their pre-retirement earnings as previous generations did.

This, however, neglects the important factor that as the number of beneficiaries increases, the cost of maintaining wage-indexed benefits imposes larger tax burdens. Table 1 shows the rising cost burden successive generations must carry to fund the current benefit formula. The existing formula does not create income equity; instead it forces later generations to accept relatively lower pre-retirement living standards. It actually causes retirement benefits to grow faster than pre-retirement after-tax income. To correct this requires a reduction in the rate of benefit growth.

Reason 2: Social Security Replacement Rates Are Higher Than Commonly Assumed and Force Many Low-Income Workers into Suboptimal Income and Consumption Patterns

Most financial planners calculate retirement income replacement rates as a percentage of individual earnings prior to retirement. Social Security instead reports replacement rates as a percentage of an obscure and poorly understood figure named the average indexed monthly earnings (AIME), which adjusts one's prior earnings for intervening growth in the average wage index. As a result, Social Security replacement rates are typically around 20 points higher than they are often misunderstood as being—indeed, they are high enough to cause many low-wage workers to have less income while working than they expect after claiming Social Security benefits.

Table 1. Current Social Security Benefit and Cost Schedules

Year worker turns 65	Benefit replacement rate as % of pre-retirement earnings	Approximate Social Security cost burden during working years	Benefit replacement rate as % of after-Social-Security-tax pre-retirement earnings
1985	41.5%	5.9%	44.1%
2020	40.0%	11.8%	45.4%
2055	41.1%	16.2%	49.0%

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Andrew Biggs and Glenn Springstead found that when Social Security replacement rates were calculated as done in typical financial planning, and taking into account the sharing of taxes and benefits by married couples, individuals in the lowest income quintile expect Social Security benefits equal to 137% of their pre-retirement earnings (77% for individuals in the second-lowest quintile).[6] This creates obvious disincentives for individuals either to extend their working careers or to engage in discretionary retirement saving. Perhaps most importantly, however, it means that the cost of supporting this level of Social Security benefits forces many low-income individuals to suffer lower living standards when working than they later experience as beneficiaries. Again, to correct this situation would require reductions in the growth of scheduled benefits.

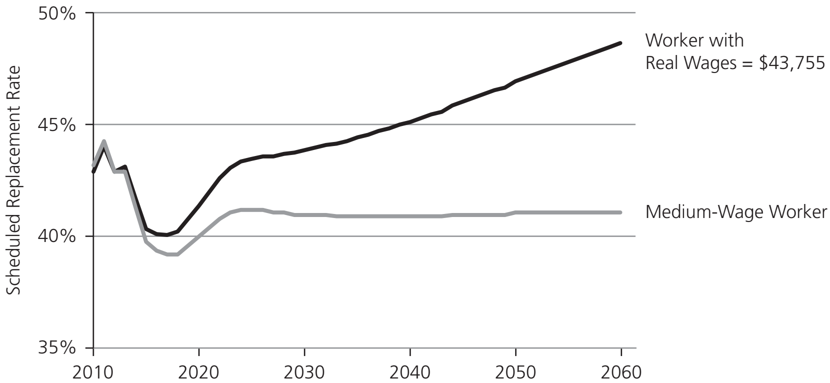
Reason 3: Real (Inflation-Adjusted) Social Security Benefits Are Growing Relative to Real Wages

It is sometimes inaccurately assumed that, because Social Security benefits are tied to wage growth, individuals with the same real wages must receive the same real benefits. This is not true. The current benefit formula causes Social Security replacement rates to rise over time relative to a given level of real wages. It is designed to pay the same replacement rates to so-called "similarly situated workers," not to two workers with the same real wages born in different years. (See figure 1.)

The current Social Security benefit formula implicitly reflects a subjective value judgment that as society grows generally richer, the federal safety net should expand so that benefits for workers with a given real earnings level automatically become more generous. This is clearly not the only value judgment that could be made. One could alternatively argue that a given level of real wages should always return the same level of real benefits. One could just as reasonably argue that as society grows wealthier and more self-sufficient, individuals should receive relatively less in government benefits rather than more, relative to the real value of their Social Security contributions. Under either of these latter approaches, considerable reductions in Social Security benefit growth would be in order.

6. Andrew G. Biggs and Glenn R. Springstead, "Alternate Measures of Replacement Rates for Social Security Benefits and Retirement Income," *Social Security Bulletin* 68, no. 2 (2008).

Figure 1. Scheduled Replacement Rates, Workers Retiring at Normal Retirement Age



Source: Author's calculations based on data from the 2012 Social Security trustees' report.

Policy Corrections

Whether the policy goal is to prevent pre-retirement living standards from declining relative to retirement benefits, to keep from forcing low-wage workers into suboptimal lifetime income patterns, or to maintain a constant relationship between real wages and real benefits, Social Security benefit growth must be slowed substantially. Doing so would not only produce substantial systemic cost savings—e.g., maintaining constant replacement rates for a constant real wage would itself solve the majority of the financing shortfall—it would improve equity across generations.

Perhaps most importantly, a Social Security solution can honor the focus of left-of-center policy advocates on benefit adequacy, while also addressing the cost-containment concerns of right-of-center advocates. The first necessary step in such a discussion is to fully appreciate the limitations of certain common benefit adequacy measures as well as the adverse consequences that arise under current benefit formulas.

For more details, see my November 2012 paper on this subject published with the Mercatus Center.[7]

7. Blahous, "Understanding Social Security Benefit Adequacy."

Don’t Worsen Social Security’s Soaring Cost Problem

This article was originally published at E21 on December 23, 2013.

There are many symptoms of growing political polarization. One of them is the increasing tendency of political parties to adopt positions rendering it more difficult to hammer out reasonable bipartisan compromises to critical national challenges. This article addresses one example—the drive by some advocates to render Social Security’s worsening financial problems even more intractable by increasing benefits above and beyond already-unaffordable schedules. For many years there was a shared bipartisan understanding that the growth of Social Security obligations was outpacing projected revenues, meaning that cost growth must be slowed, revenues must be increased, or some combination of these two actions must be taken. This latest push to expand benefits seeks to redefine the realm of political possibilities so as to shatter this historical bipartisan consensus.

The most obvious problem with proposals to expand Social Security benefits is that all evidence points away from the conclusion that our political system is willing to tax American workers at a level sufficient even to fund now-scheduled benefit obligations. But, as the previous piece details and this piece implies, the policy problems do not end there. Even if benefit growth above and beyond current schedules can be afforded, it would exacerbate a number of serious policy problems—including inequities across generations, imbalances in the treatment of workers and beneficiaries, and workforce participation and saving behavior. One need only look at the many troubled state and local pension plans around the nation to see the inevitable consequences of politicians promising benefits that they have no plan for financing.

FOLLOWERS OF POLITICS MAY HAVE NOTICED A RECENT PUSH FROM the left to expand Social Security benefits above and beyond the current-law growth schedule (which itself remains unfinanced). Such an expansion has received support from MoveOn.org, Paul Krugman, and even some sitting US senators.[1] While expanding a popular program carries an obvious

1. Nick Berning, “New MoveOn.org TV Ad: Let’s Increase Social Security Benefits,” *MoveOn.org*, December 11, 2013; Paul Krugman, “Expanding Social Security,” *New York Times*, November 21, 2013; Greg Sargent, “Elizabeth Warren: Don’t Cut Social Security. Expand It!” *Washington Post*, November 18, 2013.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

political utility, any reasonably careful analysis of Social Security reveals the idea to be highly problematic at best. Listed below are 10 factors to bear in mind whenever proposals to change Social Security benefits are discussed.

Factor 1: On the Positive Side, These Proposals Acknowledge That the Social Security Benefit Formula Should Be Changed

Historically, partisan advocates have too often fueled the misperception that any changes to Social Security benefits violate what Americans "paid for" based on the amount of their tax contributions. This is incorrect, as these latest proposals implicitly acknowledge. Over the years the program's benefit formula has changed repeatedly; it does not even attempt to reflect the amounts each worker's contributions have earned. Proof of this lies in the fact that scheduled Social Security benefits exceed the value of total worker contributions by trillions of dollars.[2] Thus, a review of Social Security's benefit formula is a good thing; the question is what changes to it would treat participants more equitably.

Factor 2: Social Security Benefits Are Already Increasing Substantially under Current Law, and Would Continue to Increase under Various Proposals to Maintain Solvency

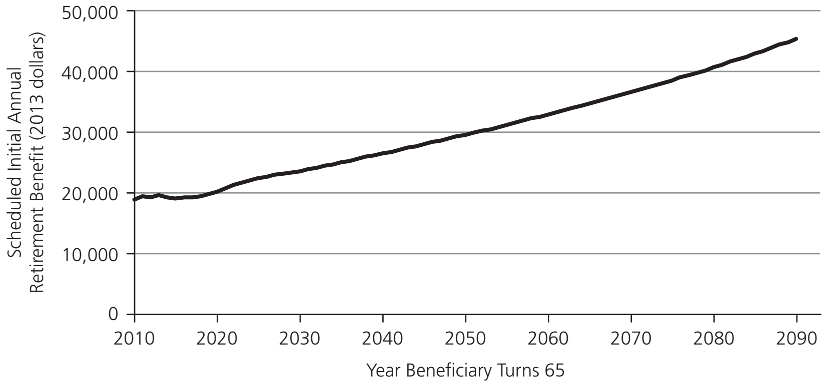
The basic benefit formula is indexed to growth in the average wage index, which tends over time to rise faster than price inflation. As a result, real per-capita Social Security benefits are already rising substantially under current law. Partisans sometimes apply the misleading terminology of "benefit cuts" to proposals to adjust benefit growth to sustainable rates, but the reality is that under virtually any plausible reform scenario, benefits will still rise in real terms relative to what seniors receive today. (See figure 1.)

Factor 3: Unless Current-Law Benefit Increases Are Substantially Slowed, Younger Workers Will Shoulder Unprecedented Cost Burdens

The number of Social Security beneficiaries is increasing dramatically as the large baby boom generation hits the benefit rolls. Paying rising per capita

2. OASDI Board of Trustees, *The 2013 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, May 31, 2013.

Figure 1. Real Social Security Benefits Increase under Current Formula



Note: Calculations are for a scaled medium earner.

benefits to a swelling beneficiary population comes with a heavy price. When the boomers began to hit the rolls in 2008, the cost of financing Social Security benefits amounted to 11.6 cents of each taxable dollar American workers earned. Per figure 2 (from the latest trustees' report), unless benefit growth is slowed the cost of financing scheduled benefits will rise to 17 cents on the dollar by the mid-2030s.[3]

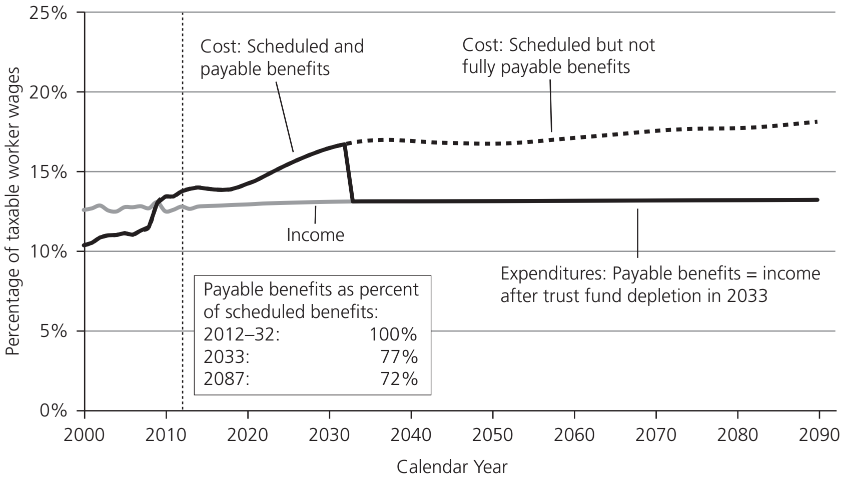
Factor 4: The Left's Latest Proposals Embody a Conscious Effort to Recast the Social Security Debate by Adopting a Policy Position Well Outside of Longstanding Mainstream Opinion

For years, policy analysts have grappled with how to reconcile the growing gap between Social Security's scheduled benefits and the financial resources available to pay for them. Conservatives generally prefer to slow cost growth and progressives to raise taxes, while bipartisan proposals such as Simpson-Bowles land roughly halfway in the middle.[4] By their own account, the

3. OASDI Board of Trustees, *2013 Annual Report*, table VI.F2: "OASDI and HI Annual Income Rates, Cost Rates, and Balances Calendar Years 1970–2090," https://www.ssa.gov/oact/TR/2013/lr6f2.html.

4. Charles Blahous, "In Defense of the Simpson-Bowles Social Security Plan: Part 2," E21 (Manhattan Institute for Policy Research), March 2, 2011.

Figure 2. Social Security Cost and Tax Income



Note: This figure shows hypothetical combined trust funds as a percentage of taxable worker wages.
Source: OASDI Board of Trustees, *The 2013 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds,* May 31, 2013, 12.

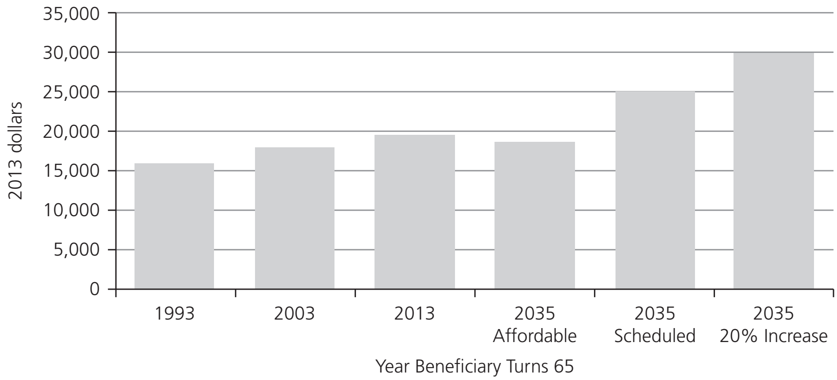
backers of these latest benefit-expansion proposals are trying to reset the Social Security debate by positioning themselves far afield from this bipartisan ground.[5]

Figure 3 gives a sense of how radical this attempted paradigm shift is. Social Security benefits have been growing steadily relative to inflation for many years. Even if Social Security were denied additional tax revenue to maintain solvency, beneficiary standards of living in 2035 would be nearly what they are today; by contrast, the program's scheduled benefit growth could only be funded with a substantial tax increase. Further increasing benefits by, hypothetically, 20% would mean more than a 50% rise in beneficiary living standards by 2035, and would also require workers to provide over 20% of their taxable wages to support one federal program.

In some respects the recent maneuvering repeats the tactic employed with the Affordable Care Act. Prior to the ACA, mainstream analysts had debated how much of the government's enormous healthcare financing

5. Michael Lind, "Take That, Paul Ryan! Elizabeth Warren Beats Back Social Security Plot," *Salon*, December 15, 2013.

Figure 3. Initial Benefits at Normal Retirement Age



Note: Calculations are for a medium wage earner.

shortfall should be closed by raising taxes, and how much by slowing benefit growth. The ACA leapfrogged previous bipartisan discussion by increasing federal health spending commitments even beyond those deemed unaffordable under prior law.[6] That radical shift is one reason why the ACA lacked bipartisan support, why its passage polarized the body politic, and why opposition to it remains entrenched within the political center and Right nearly four years later. Proposals to further increase Social Security benefits represent a similar effort to dismiss bipartisan standards of fiscal responsibility.

Factor 5: Looking Solely at Social Security Benefits Is Uninformative; a Meaningful Analysis Must Compare Both Ends of the Equation—the Taxes Social Security Collects from Workers as Well as the Benefits It Later Pays

This seems obvious, but it is striking how many discussions revolve around the adequacy of Social Security benefits without considering their relationship to the taxes required to finance them.[7] If Social Security benefits could materialize from thin air, then obviously everyone could be made better off by increasing them. But they do not; proposals must therefore be evaluated for whether Social Security benefit levels justify the worker tax burdens associated with them.

6. Congressional Budget Office, *Letter to Speaker of the House John Boehner*, July 24, 2012.
7. Lind, "Take That, Paul Ryan!"

Factor 6: Further Increasing Social Security Benefits Does Not Increase Total Resources Available to Finance Retirement Income

Theoretically, a belief that retirement security is inadequate could justify proposals to increase national retirement saving. But Social Security is not a savings program; to the contrary, most analyses find that Social Security reduces national saving.[8] Accordingly, further increasing Social Security benefits at best simply increases some participants' retirement security at the expense of others'. The important thing to know is whether such additional income transfers would improve or worsen program equity.

Factor 7: Further Increasing Social Security Benefits for Current Participants Would Worsen Existing Inequities

Because of how Social Security is financed (i.e., by having younger generations pay for the benefits of older generations), those now entering employment can expect to lose over 4% of their lifetime wages (net of benefits received) through the program under current law.[9] For younger Americans, the program will lower lifetime income and reduce economic security. These income losses can only be ameliorated if benefit growth is slowed for current participants. If instead current participants' benefits are further increased, younger Americans' net income loss through Social Security will worsen, further undermining the program's long-term efficacy as income protection.

Factor 8: Social Security Benefits and Cost Burdens Are Already Increasing Faster Than Participants' Pre-retirement Income

The growth of per capita benefits in excess of price inflation, coupled with the rising number of beneficiaries, causes workers' Social Security tax burdens to rise over time, reducing their after-tax income. As a result, the current benefit formula causes Social Security retirement benefits to grow faster than pre-retirement income—in effect, steadily depressing pre-retirement living

8. Congressional Budget Office, "CBO Memorandum on Social Security and Private Saving: A Review of the Empirical Evidence," July 1998.

9. OASDI Board of Trustees, *2013 Annual Report*.

standards relative to post-retirement living standards.[10] Further increasing Social Security benefits would worsen this problem. (See figure 4.)

Factor 9: Social Security Benefits and Costs Have Already Risen to the Point of Destroying Many Individuals' Ability and Incentive to Save

The continual lowering of worker living standards relative to beneficiary living standards is a particular problem for low-income individuals. Andrew G. Biggs and Glenn R. Springstead have shown that individuals in the lowest income quintile experience lower standards of living as taxpaying workers than they expect as Social Security beneficiaries.[11] This creates obvious disincentives for individuals to remain in the workforce, to engage in discretionary saving, and to contribute to economic growth. It is small wonder that recent research has found that many low-income groups have no significant savings at all;[12] this is the predictable result of imposing high tax burdens on limited incomes to support a retirement program that does no saving. Further increasing Social Security benefits and costs would worsen this trend of forcing low-income individuals into lower standards of living as workers than as beneficiaries.

Factor 10: Social Security Benefits Are Already Growing So Fast That Americans' Reliance on Social Security for Retirement Income Increases Even as National Incomes Rise

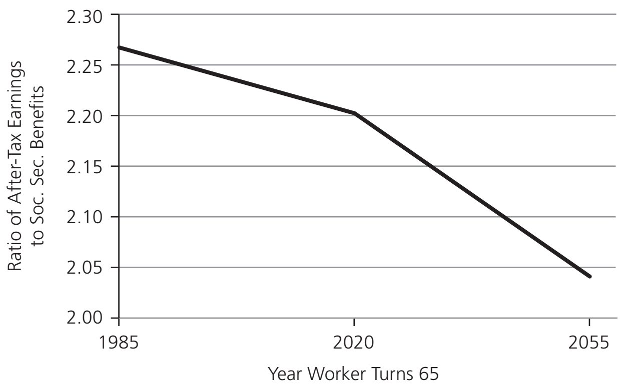
If a central purpose of social insurance programs is to provide protection against need, then logically it follows that a wealthier society should be relatively less dependent on such programs. But that is not what happens under current Social Security law; instead, Social Security is designed to expand automatically as American incomes grow. Specifically, as worker incomes rise, Social Security automatically pays higher benefits for a constant level of worker wages. (See figure 5.)

10. Charles Blahous, "Understanding Social Security Benefit Adequacy: Myths and Realities of Social Security Replacement Rates" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2012).

11. Andrew G. Biggs and Glenn R. Springstead, "Alternate Measures of Replacement Rates for Social Security Benefits and Retirement Income," *Social Security Bulletin* 68, no. 2 (2008).

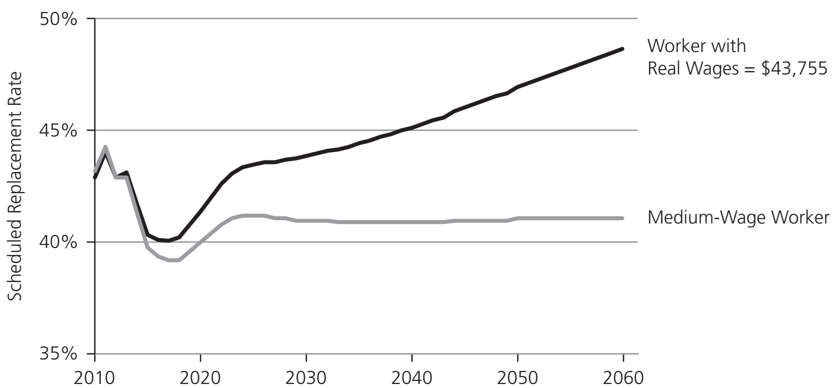
12. Michael A. Fletcher, "Many Blacks, Latinos Have No Retirement Savings, Report Finds," *Washington Post*, December 9, 2013.

Figure 4. Worker Standards of Living Relative to Social Security Benefits



Note: This figure shows career average (wage-adjusted) earnings after Social Security taxes for a medium-wage worker retiring at the normal retirement age.

Figure 5. Social Security's Benefit Formula Causes Benefits to Increase for a Given Real Level of Wages



Note: Calculations are for workers retiring at the normal retirement age.

Source: Author's calculations based on data from the 2012 Social Security trustees' report.

Further increasing Social Security benefits only makes sense if we believe that, as American society grows wealthier, individuals should become more reliant on government and less on their own saving. If we do not believe this, benefit growth should be significantly slowed from current schedules.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Summary

Backers of proposals to expand Social Security benefits acknowledge their intent to recast the Social Security debate to draw new attention to thinking well outside the longstanding spectrum of bipartisan opinion.[13] But there are good reasons why such proposals have not been supported by mainstream Social Security analysts to date. Not only would such a benefit expansion render it still more difficult to maintain Social Security solvency without large, economically damaging tax increases, it would worsen many existing program inequities, depress worker living standards, and further undermine low-income individuals' ability and incentive to put aside savings of their own. Though such proposals may have a superficial political attraction for some, the policy consequences of their actual enactment would be hugely damaging.

13. Lind, "Take That, Paul Ryan!"

Warning: Disability Insurance Is Hitting the Wall

This article was originally published at E21 on January 15, 2015.

Before congressional action in 2015 to shore up the Social Security Disability Insurance (DI) trust fund, I and the other five Social Security trustees had warned of its impending depletion. As the threat grew imminent we intensified these alarms, calling for prompt legislation to shield vulnerable disabled beneficiaries from sudden interruptions in benefit payments.

As trustees, our primary responsibilities pertained to presenting program financial information to lawmakers. Public trustees (of which I was one of two) also performed a more informal role as curators of relevant policy history. This role became more important during this period. In the time leading up to the aforementioned legislation, some advocates had argued that lawmakers should do nothing more than reallocate taxes from Social Security's OASI trust fund to its DI trust fund to paper over the DI shortfall. Some even suggested that this was the standard method historically for dealing with such shortfalls.

These advocates' representations were incorrect. Standalone tax reallocations between the trust funds do not represent the historical norm. To the contrary, past inter-fund tax reallocations typically took place only in the context of other actions to address Social Security's larger financial operations. It would have been an especial departure from precedent to enact a reallocation solely for the purpose of postponing necessary financial corrections. Accordingly, the House of Representatives adopted a rule to ensure that appropriate precedent would be followed, and that Social Security's financial balance would be improved in the course of any tax reallocation. This piece detailed the relevant background on the historical handling of similar situations, emphasizing the positions adopted by our predecessors as public trustees.

FOR YEARS SOCIAL SECURITY'S TRUSTEES (OF WHICH I AM ONE) HAVE warned that lawmakers must act to address the troubled finances of the program's disability insurance trust fund.[1] Congress has nearly run out of time to do so. Legislation will be required during this Congress or, at the

1. Social Security and Medicare Boards of Trustees, "A Summary of the 2014 Annual Reports," 2014, Social Security Administration, https://www.ssa.gov/OACT/TRSUM/2014/index.html.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

very latest, in a rush at the beginning of the next one to prevent large, sudden benefit cuts. The House of Representatives recently passed a procedural rule to prepare for the coming legislative debate.[2] In this article I explain the issues in play.

The Problem

The problem in a nutshell is that Social Security's disability trust fund is running out of money. The latest trustees' report projects a reserve depletion date in late 2016. By law, Social Security can only pay benefits if there is a positive balance in the appropriate trust fund. (There are two trust funds: one for old-age and survivors' benefits, the other for disability benefits.) Absent such reserves, incoming taxes provide the only funds that can be spent. Under current projections, by late 2016 there will be only enough tax income to fund 81% of scheduled disability benefits. In other words, without legislation, benefits will be cut by 19%. (See figure 1.)

The Cause

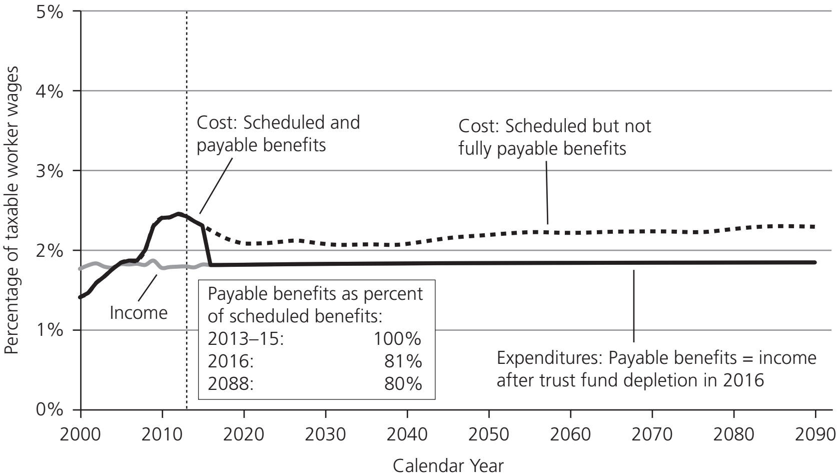
The cause of the problem is that DI costs have grown faster than the program's revenue base. In 1990, the cost of paying DI benefits equaled 1.09% of taxable wages earned by workers. This year the relative cost is more than double that: 2.37% of the tax base. (See figure 2.)

The detailed reasons for the cost increase are beyond the scope of this column. (A good first source on these issues is the Social Security chief actuary.)[3] The biggest reason is the growing number of beneficiaries, though real per capita benefits are also growing. Disabled population growth reflects several factors, including most notably the historically large baby boom generation moving through the ages of peak disability incidence (45–64). In addition, today more women have been employed long enough to be insured for disability benefits than was the case in earlier decades.

2. H. Res. 5 (2015).

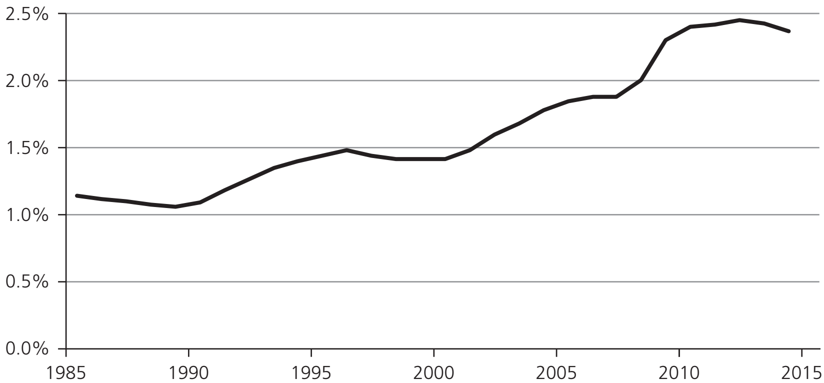
3. Stephen C. Goss, "Statement of Stephen C. Goss, Chief Actuary, Social Security Administration, before the House Committee on Ways and Means, Subcommittee on Social Security," March 14, 2013.

Figure 1. Projected Disability Insurance Income, Cost, and Expenditures as a Percentage of Taxable Worker Wages



Source: Board of Trustees, *The 2014 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 28, 2014, 13.

Figure 2. Disability Insurance Benefit Costs as a Percentage of Taxable Worker Wages



The growth in beneficiaries exceeds prior projections even after taking these factors into account. For example, the chief actuary reports that "the prevalence of disability among insured workers on an age-sex adjusted basis" rose by 42% from 1980 to 2010, even though there is no evidence suggesting that actual disability is much more common than it was 30 years ago. Instead, the rise reflects causes ranging from a liberalization of eligibility criteria in 1984 to a surge in disability benefit applications when unemployment rose during the Great Recession.[4]

Policy Ideals

Let us set aside political considerations from the outset and focus only on good policy. From a pure policy perspective the best solution is comprehensive reform shoring up Social Security financing on both sides (OASI and DI). Annual trustees' reports have made it clear that "lawmakers should address the financial challenges facing Social Security and Medicare as soon as possible" and that "earlier action will also help elected officials minimize adverse impacts on vulnerable populations."[5]

The worsening Social Security shortfall has already grown roughly twice as large as the one corrected with so much difficulty in 1983.[6] Further delay in enacting comprehensive reforms would mean that still larger adjustments to taxes and benefits are required. Procrastinating for much longer worsens the risk that Social Security's shortfall cannot be corrected at all, and that its historical financing structure will eventually have to be abandoned.

The integration of the disability and retirement components of Social Security also warrants a comprehensive response. The two sides use the same basic benefit formula to prevent discontinuities in benefit levels when the disabled reach retirement age. Criteria for benefit eligibility are integrated as well. A failure to address the two sides in tandem runs the risk of creating unintended inequities.

4. David H. Autor and Mark G. Duggan, "The Rise in the Disability Rolls and the Decline in Unemployment," *Quarterly Journal of Economics* 118, no. 1 (February 2003); Goss, "Statement of Stephen C. Goss."

5. Social Security and Medicare Boards of Trustees, "A Summary of the 2014 Annual Reports," 2014, Social Security Administration, https://www.ssa.gov/OACT/TRSUM/2014/index.html.

6. Charles Blahous, "Is It Becoming Too Late to Fix Social Security's Finances?," E21 (Manhattan Institute for Policy Research), August 31, 2012 (republished in this collection).

Reallocating Taxes Isn't a Fix by Itself

Some have suggested that DI's funding problem be addressed merely by giving DI some of the taxes now going to OASI (currently DI receives 1.8 points of the 12.4% payroll tax, OASI 10.6 points).[7] As I have explained before, this suggests a misdiagnosis of the problem.[8] The problem is not that DI commands too small a share of the tax relative to its obligations; to the contrary, OASI actually faces the larger actuarial imbalance. DI is hitting the wall first largely because the baby boomers hit their peak disability years before their retirement years; it is the first crisis triggered by the unsustainable financing arrangements threatening DI and OASI alike. Transferring funds from OASI to DI would weaken Social Security's retirement component, which is in even worse long-term condition.

Lawmakers face a spectrum of choices. The most responsible and ambitious choice would be comprehensive reform shoring up Social Security as a whole. The most irresponsible (other than doing nothing at all) would be reallocating funds between DI and OASI for the purpose of delaying these necessary reforms, further increasing the risk of the shortfall growing too large to fix. The latter would be a national version of the tactics of avoidance that led to crises in many state pension plans.[9]

Congress must determine the highest point on the responsibility scale at which it can produce legislation. Many outside experts are putting forth proposals to help lawmakers in this effort.[10] The recently passed House rule allows for the full spectrum of responsible options, precluding only the worst outcome of making no net financing improvements whatsoever. Specifically, the rule requires that any tax reallocation occur in the context of broader

7. Shawn Fremstad, "A Simple but Critical Fix Is Needed Now for the Nation's Disability System," *National Journal*, September 11, 2014.

8. Charles Blahous, "A Guide to the 2014 Social Security Trustees Report," E21 (Manhattan Institute for Policy Research), August 4, 2014.

9. *The Economist*, "Illinois Risks Default If It Doesn't Tackle Its Public Pension Crisis," *Business Insider*, December 28, 2014.

10. Rollcall staff, "A Repair Plan for the Social Security Disability Insurance Program," *Roll Call*, September 17, 2014; Bipartisan Policy Center, "Commission on Retirement Security and Personal Savings"; Jason S. Seligman and Jason Fichtner, "Public Disability Insurance Programs in the Context of Pension Reforms," in *Pensions: Policies, New Reforms and Current Challenges*, ed. Thom Reilly, 167–85 (Hauppauge, New York: Nova Science, 2014).

reforms to improve Social Security finances, as recommended by the program's six trustees in our annual message:

> Lawmakers may consider responding to the impending DI Trust Fund reserve depletion, as they did in 1994, solely by reallocating the payroll tax rate between OASI and DI. Such a response might serve to delay DI reforms and much needed financial corrections for OASDI as a whole. However, enactment of a more permanent solution could include a tax reallocation in the short run.[11]

The Historical Record

Some have suggested that a stand-alone payroll tax reallocation would be a routine action in keeping with historical precedent.[12] This reflects substantial confusion about the historical record, which tells a wholly different story.

The last time Social Security taxes were reallocated was 20 years ago, in 1994. The situation then (and surrounding other reallocations) was very different from today. DI costs had risen after the 1984 legislation liberalizing award determinations, rising further during a subsequent recession. Unlike the situation today, DI's actuarial imbalance had then grown rapidly worse than OASI's and much worse than prior projections.

In response to that looming insolvency threat, the program's trustees recommended a number of actions, including a reallocation of taxes from OASI to DI. They were explicit that this proposed tax reallocation was to buy time (specifically, 10 years) to enable comprehensive reforms.

In written testimony before Congress in 1993, the public trustees stated that while comprehensive reforms were the appropriate goal, there was yet "insufficient information to design specific proposals for the long term. . . . The proposed reallocation for the short term will provide the time and opportunity to prepare and enact any needed changes in a careful and orderly manner."[13] The trustee present at the hearing, Stan Ross, cited a "prudent"

11. Social Security and Medicare Boards of Trustees, "A Summary of the 2014 Annual Reports."

12. Michael Hiltzik, "On Day One, the New Congress Launches an Attack on Social Security," *Los Angeles Times*, January 6, 2015.

13. Social Security Board of Trustees Recommendation to Reallocate a Portion of the Social Security Payroll Tax to the Disability Insurance Trust Fund, 103rd Congress (April 22, 1993).

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

goal "to meet short-term solvency so that both funds meet the 10-year test, and then to work on the long-term problems of both funds."

In their 1994 message, the public trustees again voiced support for a temporary tax reallocation to avoid insolvency projected for 1995, but spent more of their message stressing that the purpose was to buy time for broader reforms:

> The 1994 Report continues to project that the DI fund will be exhausted in 1995. Therefore, we again strongly urge that action be taken as soon as possible to ensure the short-range financial solvency of the DI trust fund. We also strongly urge the prompt completion of the research efforts undertaken by the Administration at the Board's request. This research may assist the Congress as it considers the causes of the rapid growth in disability costs and addresses, as necessary, any substantive changes needed in the program. Disability Insurance under Social Security is nearly 40 years old. While some reforms have taken place over the years, the public is entitled to a thorough policy review of the program. The recent dramatic growth suggests the possibility of larger underlying issues related to the health and employment circumstances of workers and the need for responsive adjustments in the program.[14]

As recommended, lawmakers reallocated OASI/DI taxes in 1994. Rather than treat this as a resolution, the public trustees in their 1995 message made a further point of stressing that the tax reallocation was intended only to buy enough time for lawmakers to analyze, design, and implement comprehensive reforms to control program cost growth:

> While the Congress acted this past year to restore its short-term financial balance, this necessary action should be viewed as only providing time and opportunity to design and implement substantive reforms that can lead to long-term financial stability. The research undertaken at the request of the Board of Trustees, and particularly of the Public Trustees, shows that there are serious design and administrative problems with the DI program. Changes in our society, the workforce and

14. Social Security and Medicare Board of Trustees, "A Message to the Public [Summary of the 1994 Annual Reports of the Social Security and Medicare Trust Funds]."

> our economy suggest that adjustments in the program are needed to control long-range program costs. Also, incentives should be changed and the disability decision process improved in the interests of beneficiaries and taxpayers. We hope that this research will be completed promptly, fully presented to Congress and the public, and that the Congress will take action over the next few years to make this program financially stable over the long term.[15]

Despite these warnings, lawmakers have not yet implemented reforms as recommended by the trustees for several years. To reallocate taxes again in the absence of such reforms would be in direct conflict with the express purpose of the last reallocation. Clearly the last thing intended then was for lawmakers today to simply reallocate the taxes yet again, further postponing necessary reforms until both trust funds are on the precipice of insolvency.

Conclusion

The recently enacted House rule conforms to the guidance repeatedly given by the program's trustees on a bipartisan basis over several years. Those who suggest that DI's impending reserve depletion warrants no action beyond taking revenues away from the Social Security retirement fund appear to be unfamiliar with the basis for the current allocation as enacted in 1994. Lawmakers should begin work now, with the assistance of responsible outside experts, on a bipartisan package of reforms to strengthen the disability program and Social Security as a whole.[16]

15. Social Security and Medicare Board of Trustees, "A Message to the Public [Summary of the 1995 Annual Reports of the Social Security and Medicare Trust Funds]."
16. Rollcall staff, "Repair Plan."

Future Work Still Needed after Budget's Disability Fix

This article was originally published at E21 on November 2, 2015.

One of the more curious episodes of my public policy career played out in 2016 during Senate consideration of the nominations of my co-trustee Robert Reischauer and myself to serve second terms. Representations were made that I had fought against lawmakers' recent actions to shore up the DI trust fund. This was a bizarrely false allegation, for not only had I not fought against congressional action, I had occasionally taken the lead role among the trustees in calling for it. Indeed, a central portion of my remarks at the 2015 press conference on the annual trustees' reports' release was devoted to calling for legislation to shore up DI. I had also (in the previous piece in this collection) explained why the procedural approach the House had adopted, which governed the contours of the eventual fix, was in keeping with both historical precedent and the recommendations of previous public trustees.

After the fix became law I published this piece, expressing support for the action and explaining how it improved the outlook for DI finances. Yet, even to this day, a quick internet search for my stance on disability policy will turn up several claims that I had fought against the legislation. There isn't a shred of truth to the charge, but this hasn't stopped the story from circulating online.

THE BIPARTISAN BUDGET BILL JUST PASSED BY CONGRESS CONTAINS several provisions affecting Social Security disability insurance (DI) operations as well as Social Security finances generally. The purpose of this piece is to explain key effects of the disability provisions. I will not speak to the merits of the budget deal as a whole, which is already the subject of many others' analysis and commentary.[1]

1. "Budget Deal Truly Offsets Only Half Its Cost," Committee for a Responsible Federal Budget, October 25, 2015.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

The details of the disability provisions are complex and likely of interest only to those steeped in Social Security disability policy. So before proceeding to describe them, I will stress three bottom-line conclusions:

1. The provisions represent a slight improvement to disability program operations.
2. The provisions represent a substantial improvement over the likely result if legislative action had been further postponed until nearer to projected DI trust fund depletion in late 2016.
3. Passage puts the program in better condition, but it will rapidly grow worse unless legislators enact further Social Security reforms in short order (e.g., after next year). This worsening has nothing to do with the budget bill provisions. It is because time is the enemy of Social Security finances. Until comprehensive corrections are enacted, the shortfalls facing Social Security, including disability, will continue to grow worse.

Some background may clarify these points.

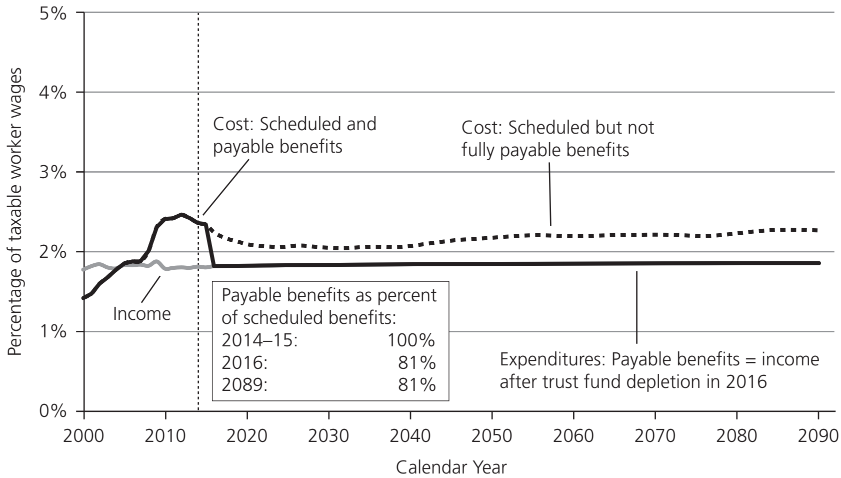
Social Security DI has been running a deficit of tax income relative to benefit spending, forcing the program to draw down the spending authority of its trust fund at a rate that would result in depletion in late 2016. This threatened beneficiaries with sudden benefit reductions of approximately 19%. (See figure 1, reproduced from the 2015 trustees' report.)

Second, while the disability component of Social Security faces insolvency soonest, the program's retirement trust fund is in even worse long-term condition. As I noted in a previous piece, the retirement side "actually faces the larger actuarial imbalance. DI is hitting the wall first largely because the baby boomers hit their peak disability years before their retirement years."[2] Figure 2 (also from the trustees' report) shows shortfalls in Social Security's combined trust funds emerging later but also being larger than those in disability alone. Thus, shifting funds from Social Security's retirement side to its disability side wouldn't by itself fix the underlying problem—it would merely facilitate further delay in dealing with it.

A third critical point is that continued delays would render these problems much more difficult to solve. As I noted in another previous piece, "If

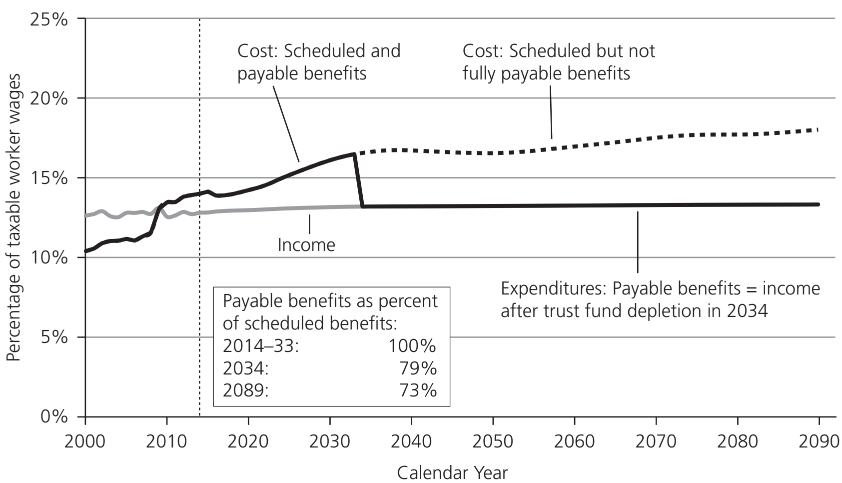
2. Charles Blahous, "Warning: Disability Insurance Is Hitting the Wall," E21 (Manhattan Institute for Policy Research), January 15, 2015 (republished in this collection).

Figure 1. Disability Insurance Income, Cost, and Expenditures as a Percentage of Taxable Wages



Source: OASDI Board of Trustees, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 22, 2015, 14.

Figure 2. Social Security Income, Cost, and Expenditures as a Percentage of Taxable Wages



Source: OASDI Board of Trustees, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 22, 2015, 13.

legislation enacted today held current [Social Security] beneficiaries harmless, long-range financial balance could be restored by reducing scheduled benefits for future beneficiaries by 19.6%.[3] If, however, such a strategy were attempted after employing delaying tactics until 2034, by then even 100% elimination of benefits for new claimants would be insufficient to avoid depletion of the combined trust funds."[4]

These factors framed a spectrum of choices facing legislators confronting the projected depletion of DI's trust fund next year:

- The most responsible and ideal result—but also the most ambitious and politically difficult—would have been comprehensive legislation shoring up the entirety of Social Security's finances, as last occurred in 1983.
- The worst choice would have been inaction, allowing 11 million Social Security disability beneficiaries to experience interruptions of their benefits, effectively reducing their Social Security income by 19%.
- The second worst choice would have been to do nothing other than paper over the problem for several years into the future by shifting funds between Social Security's accounts. This would irresponsibly allow the shortfalls in disability, and in Social Security as a whole, to grow to the point where they could no longer plausibly be corrected.

Negotiators opted for incrementalism, introducing some slight improvements to program finances while transferring just enough funds between Social Security accounts to ward off a disability financing crisis in the near term, but without sanctioning an extended period of destructive, and potentially fatal, further delays.

Let's now return to and explain the bottom-line conclusions.

3. OASDI Board of Trustees, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 22, 2015.

4. Charles Blahous, "Time Is Running Out to Fix Social Security," E21 (Manhattan Institute for Policy Research), July 28, 2015.

Conclusion 1: The Provisions Represent a Slight Improvement to Disability Program Operations

As seen in the Social Security chief actuary's memorandum on the bill, its dent in Social Security's long-term shortfall is very small (between 1.0% and 1.5%) but there will be some expected improvements in program integrity.[5] The biggest savings come from two provisions. One closed loopholes that had allowed Social Security benefits to be claimed and suspended in ways causing higher-than-intended benefit payments to secondary household beneficiaries. The other would require that the medical portion of disability reviews be completed by an appropriate physician, psychiatrist, or psychologist. Other provisions, not scored as achieving significant savings, would expand the use of electronic payroll data and cooperative disability investigations units to "reduce fraud and overpayments." Still others would allow for demonstration projects aimed at clearing the way for disabled individuals to return to work. It is reasonably possible that these reforms, taken together, could produce more savings than now projected for them, but Social Security's financial shortfalls are far too large to be corrected by such program integrity measures alone.

Importantly, unlike a standalone reallocation of revenues between Social Security's trust funds, this bill would improve both disability and combined Social Security finances without significant weakening of the program's retirement trust fund. The bill does this by generating savings within the retirement trust fund that are roughly comparable to the revenues being shifted to disability (specifically, 0.57% of workers' taxable wages from 2016 to 2018, enough to extend projected DI solvency until 2022).

Conclusion 2: The Provisions Represent a Substantial Improvement over the Likely Result If Legislative Action Had Been Further Delayed

Although the provisions represent only a slight immediate financial improvement, it's important to bear in mind that without action things were about to get worse in a hurry. Disability trust fund depletion and 19% benefit cuts were projected for late 2016—an intolerable result legislators would

5. Stephen C. Goss, Chief Actuary of the Social Security Administration, to John Boehner, Speaker of the House, October 27, 2015.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

almost certainly not have permitted. In a last-minute election-year crisis situation, it would likely be prohibitively difficult to legislate reasonable reforms, increasing the risk of simply papering over the problem by shifting funds between Social Security accounts (allowing overall program finances to grow still worse).

The bill's combination of modest reforms and a modest tax reallocation is only a slight improvement over previous law. But it is worlds better than bailing out disability with retirement trust fund revenues with no reforms at all, which is quite possibly where we'd otherwise be headed.

Conclusion 3: After an Initial Improvement, Things Are Going to Get Rapidly Worse Again Unless There Is Prompt Follow-Up Action (Presumably after 2016)

With this bill's passage, it's unlikely Congress will act again on Social Security disability before the 2016 elections. But lawmakers can't afford to wait much longer after that, and certainly not to dither until DI's new projected insolvency date of 2022. Consider, for example, that the budget deal improves Social Security finances by something less than 0.04% of taxable worker wages, whereas the program's long-range shortfall grows by 0.06% of wages every year.[6] Even this understates the actual worsening because, by the time the program's combined trust funds are projected to be insolvent, annual deficits requiring closure look to be well over 3% of taxable worker wages. Given that reasonable proposals to restore long-term solvency tend to reduce annual deficits to not much more than 1% of wages by the 2030s, we basically have less than 20 years to effectuate annual improvements equaling over 2% of wages.[7] In other words, the practical task currently grows more difficult by at least 0.11% of wages every year, an annual worsening roughly triple the improvement in the budget bill. Remember also that the current

6. OASDI Board of Trustees, *The 2015 Annual Report*, table IV.B7, "Reasons for Change in the 75-Year Actuarial Balance, Based on Intermediate Assumptions," https://www.ssa.gov/oact/TR/2015/IV_B_LRest.html#219298.

7. Stephen C. Goss, Chief Actuary of the Social Security Administration, Alice H. Wade, Deputy Chief Actuary, and Christopher J. Chaplain, Supervisory Actuary, to Kay Bailey Hutchison, US Senator, October 27, 2015.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

shortfall is already substantially larger than the one closed with so much difficulty in 1983. Clearly we don't have further time to waste.[8]

Brokering a comprehensive solution to Social Security's financing shortfalls will be difficult. At the same time, there is clearly still some low-hanging fruit available. For example, President Obama's proposal to prevent double-dipping in DI and unemployment insurance benefits, also supported by Congressman Sam Johnson and Senator Orrin Hatch, remains out there to be enacted.[9] (Disability benefits are intended only for those who cannot engage in meaningful employment, whereas unemployment benefits are supposed to be available only to those currently searching for work; the two programs are drawn up such that individuals should only be able to receive from one or the other.) Again, however, savings from such program integrity provisions would be modest.

In sum, the budget deal slightly improves the outlook for Social Security disability. Things will shortly resume worsening, however, requiring legislators to return to this vital work after 2016.

8. Charles Blahous, "A Guide to the 2014 Social Security Trustees Report," E21 (Manhattan Institute for Policy Research), January 15, 2015.

9. Ian Smith, "Lawmakers Want to Stop 'Double Dipping' of Disability Benefits," *FedSmith.com*, February 13, 2015; Orrin Hatch, US Senator, "Hatch, Johnson, Ryan Introduce Bill to Prevent 'Double Dipping' in Disability Benefits," February 12, 2015.

How Social Security's COLA Politics Leads to Bad Policy

This article was originally published at E21 on November 22, 2015.

This piece might seem comparatively dry, but some policymakers have pointed to it as especially useful given recurring political difficulties surrounding annual cost-of-living adjustments (COLAs) to Social Security benefit levels. As many readers may know, each year Social Security benefit levels are automatically adjusted for changes in national price inflation as reflected in the consumer price index (CPI). That much is relatively straightforward and broadly understood. But the law also contains a number of counterintuitive, arbitrary, and problematic connections between the annual COLA calculation and several other features of Social Security and Medicare operations.

In general, when the Social Security COLA is small or (on rare occasion) zero, this a signal to a number of special interest groups to complain loudly and demand additional compensation for seniors. Yet, as this piece explains, for a number of quirky reasons years without COLAs are actually more good for seniors than bad. Such years produce some strange results that are perhaps undesirable from a larger policy perspective, but they do not harm most seniors.

ON OCTOBER 15, 2015, THE SOCIAL SECURITY ADMINISTRATION announced that there would be no cost-of-living adjustment for 2016.[1] Many perceived this as signifying a hardship for seniors.[2] Lawmakers afterward included a provision in the budget deal to prevent some seniors from facing huge Medicare premium increases, which were among the perverse effects that otherwise would have arisen from the zero COLA.[3] This piece explains the basics of Social Security COLAs, as well as how zero-COLA years can lead to confused politics and strange policy.

1. LaVenia J. LaVelle, *Law Does Not Provide for a Social Security Cost-of-Living Adjustment for 2016* (Washington, DC: Social Security Administration, 2015).

2. Nancy LeaMond, "With No COLA Increase, Congress Should Pass Medicare Fix," AARP, October 15, 2015.

3. House Amendment to the Senate Amendment to H.R. 1314, Offered by Mr. Boehner of Ohio (2015); Bipartisan Budget Act of 2015, Pub. L. No. 114-74, 129 Stat. 584 (2015).

How COLAs Work

The annual Social Security COLA is calculated by comparing the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) in the third quarter of the most recent year to its level in the third quarter of the previous year.[4] CPI-W is just one of multiple measures of general price inflation maintained by the Bureau of Labor Statistics.[5] Most economists believe it is less accurate than other measures, including the Chained Consumer Price Index for All Urban Consumers (C-CPI-U).[6] It just so happened that Social Security COLAs were first established in law before the other, more refined measures were developed.[7]

Other quirks of law surround Social Security COLAs. One is that when there is no COLA, neither is there an increase in the amount of wages subject to the Social Security payroll tax—even though normally the automatic annual tax base increases are computed differently from the COLA or CPI.[8]

Another provision of law (the so-called "hold harmless" provision) prevents most beneficiaries' monthly Social Security benefit checks, net of Medicare Part B premiums, from declining. This means that whenever there is a zero-COLA year, roughly 70% of seniors do not face a Medicare premium increase even though their benefit costs have likely gone up.[9] Under law, the resulting revenue loss to Medicare is supposed to be made up by higher premiums from high-income seniors and on behalf of low-income seniors (whose premiums are paid for them under Medicaid by the states). This in turn can mean huge premium increases for a minority of seniors on opposite ends of the income spectrum, as would otherwise have happened this year. These various provisions do not add up to a coherent policy, but rather

4. Social Security Administration, "Average CPI by Quarter and Year," https://www.ssa.gov/oact/STATS/avgcpi.html.

5. Stephen B. Reed and Kenneth J. Stewart, "Why Does BLS Provide Both the CPI-W and CPI-U?," *Bureau of Labor Statistics: Beyond the Numbers* 3, no. 5 (2014).

6. US Bureau of Labor Statistics, "Table 5. Chained Consumer Price Index for All Urban Consumers (C-CPI-U) and the Consumer Price Index for All Urban Consumers (CPI-U): U.S. City Average, All Items Index," https://www.bls.gov/news.release/cpi.t05.htm.

7. Social Security Administration, "Cost-of-Living Adjustment (COLA) Information," https://www.ssa.gov/news/cola/; Marc Goldwein, Jason Peuquet, and Adam Rosenberg, *Measuring Up: The Case for the Chained CPI* (Washington, DC: Committee for a Responsible Federal Budget, March 19, 2013).

8. Social Security Administration, "Cost-of-Living Adjustments (COLA) Information."

9. Social Security Administration, "Cost-of-Living Adjustments (COLA) Information."

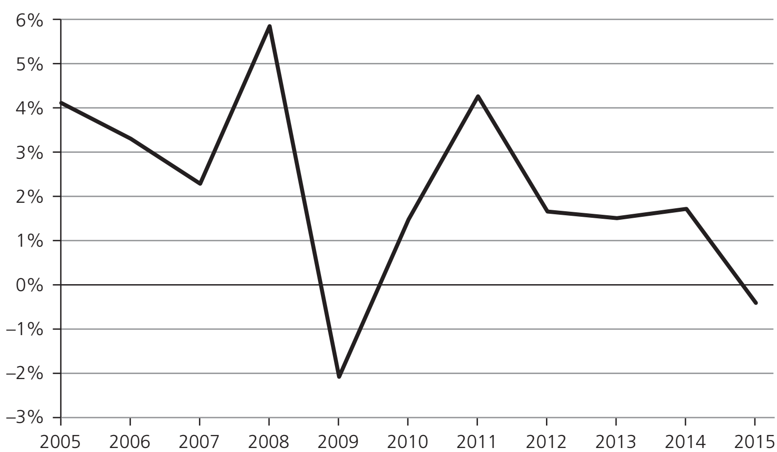
embody a patchwork of responses to the perceived policy and political challenges that accompany zero-COLA years.

Zero COLAs Are Usually More Good Than Bad for Seniors, Part 1

Despite what advocacy groups often say, a year without a COLA usually reflects a situation more good than bad for seniors. This is because there is no provision in law allowing for a negative COLA. Thus, if prices rise by a large amount one year but fall the next, beneficiaries get a large COLA after the first year but no reduction for the second year. This means that seniors receive higher benefit payments than they would have if current price levels had instead been reached via persistent, regular price inflation. Seniors continue to receive these higher payments in a lower-price environment, with this (usually very small) bonus never taken away.

As figure 1 shows, prices typically rise by a small percentage each year. But in 2015 prices (per CPI-W) have gone down slightly, modestly increasing beneficiaries' purchasing power. A similar, but more extreme, situation previously arose in the 2008–2011 period. Prices rose swiftly in 2008, producing a large COLA for 2009 even though prices went down during that year. Prices didn't return to 2008 levels until 2011 because the increase in 2010

Figure 1. Annual Percentage Change in CPI-W



was not as great as the decrease in 2009 had been. As a result, the purchasing power of Social Security benefits outpaced inflation during that period.

Zero COLAs Are Usually More Good Than Bad for Seniors, Part 2

As mentioned earlier, under law Medicare Part B premiums can't rise for most beneficiaries whenever there is no COLA. This is a clear advantage to seniors, who receive benefits of higher value without paying higher premiums.

Our Political Discussion Often Confuses the Concepts of Prices, Costs, and Spending

Economists generally agree that CPI-W overstates price inflation relative to a chained index such as C-CPI-U.[10] Yet whenever the annual COLA is zero or quite small, longstanding arguments reemerge that CPI-W actually understates price inflation as experienced by seniors. AARP, for example, has argued that an experimental senior price index (CPI-E) would be better, saying that CPI-W "does not accurately represent the buying habits of seniors," largely because seniors spend more of their income on healthcare, where costs tend to rise more rapidly.[11]

Much of this discussion confuses the different concepts of prices, costs, and spending. COLAs are intended to reflect price changes rather than other factors that increase total costs. Indeed, much healthcare cost growth does not arise from price inflation but rather from the adoption of new technologies.

In general, whether we spend more on any area depends on many factors other than prices. This year you might spend a lot more on plumbing services than you did last year—but not necessarily because the plumber's prices went up. Instead, this may simply reflect your greater need for plumbing services, or the plumber having new services to offer. The fact that seniors spend more on healthcare as technology progresses in response to their growing needs is indeed an important policy concern. But how much to help seniors afford

10. There isn't space in this piece to review the details, but the Committee for a Responsible Federal Budget explains some: see Goldwein, Peuquet, and Rosenberg, *Measuring Up*.

11. Nancy LeaMond, "With No COLA Increase, Congress Should Pass Medicare Fix," AARP, October 15, 2015.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

rising healthcare costs is primarily an income support issue or a healthcare policy issue. It is not primarily an issue of price inflation measurement.

Our Perplexing System for Assessing Medicare Part B Premiums Makes It Difficult to Construct Sensible Policy

As earlier noted, whenever there is no COLA, about 70% of Medicare beneficiaries are excused from financing a proportionate share of program cost increases. Under law the revenue loss is to be made up by assessing higher premiums on those who are not so excused: low-income beneficiaries (whose premiums are paid by Medicaid) and higher-income beneficiaries (who pay larger income-related premiums).

In 2015 the premium hikes would have been enormous had Congress not acted. The trustees' report contains an estimate that the relevant premium would have had to rise from $104.90 to $159.30 even without accounting for the still-higher premiums facing those on the high-income end.[12] Joseph Antos has estimated that monthly premiums would have risen to over $500 in the top bracket.[13]

Faced with this situation, lawmakers acted to limit the standard premium to about $120 (higher-income beneficiaries will still pay substantially more). The revenue loss resulting from the premium relief would jeopardize program finances, so lawmakers enacted a loan to Medicare from the general Treasury, charging affected beneficiaries an additional $3 a month until the loan is repaid.[14]

If you are confused by all this, you're not alone. Medicare costs keep rising even in a zero-COLA year, but the law's complexities make it very difficult to discern who pays for them. Most beneficiaries aren't doing so, due to the hold-harmless provision. Lawmakers also just excused high-income beneficiaries from much of the burden of doing so. High-income seniors will still pick up a bit of the cost, as will states (through Medicaid), which will then pass the cost on to their residents in various hard-to-track ways. Some of the

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12. Medicare Board of Trustees, *2015 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, July 22, 2015.

13. Joseph Antos, "No Medicare Premium Spike . . . for Now," *US News and World Report*, October 29, 2015.

14. Bipartisan Budget Act of 2015.

rest is being picked up by loans from the general US Treasury—for which all Americans must pay, though none of us knows our own share. None of this is a recipe for transparency.

The policy ideal would be a Medicare system in which costs do not rise faster than the ability of senior premium payers to bear. This would require tough decisions about fundamental reforms, eligibility rules, and benefit growth rates that the body politic has thus far been unwilling to make. Failing this ideal, the next best outcome would be a system in which beneficiaries and taxpayers each shoulder an appropriate and transparent proportionate share of rising program costs. But this in turn would mean Social Security checks net of premium payments declining in some years, the optics of which have long made for prohibitive politics. As a result, the opaque and seemingly arbitrary process of Medicare premium setting is likely to continue for some time.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

A Balanced Bipartisan Compromise for Strengthening Retirement Security

This article was originally published at E21 on June 23, 2016.

Good policy writing should generally focus on educational information rather than commentary, for the simple reason that the author's subjective policy views are no better than anyone else's. This piece nevertheless seemed worth publishing as a demonstration of how a reasonably designed bipartisan Social Security financing solution might be constructed. For roughly two years I had worked with a commission convened by the Bipartisan Policy Center (BPC) on a package of retirement security policy recommendations. The work was arduous and time-consuming, but was made fulfilling by the skilled bipartisan leadership of Kent Conrad and James Lockhart.

Retirement policy considerations aside, the commission experience was instructive of how successful negotiations can be conducted among a diverse array of experts embodying a wide spectrum of views. Adroit leaders such as Conrad and Lockhart listen carefully to where everyone is coming from and fashion a compromise reflecting the areas of common ground.

THE BIPARTISAN POLICY CENTER'S *SECURING OUR FINANCIAL FUTURE* report offers a new set of recommendations to strengthen Americans' retirement income security.[1] The report was developed by the BPC's 19-member Commission on Retirement Security and Personal Savings, cochaired by former Senator Kent Conrad (D-ND) and James Lockhart, former principal deputy commissioner of the Social Security Administration. I served as one of the commission members and was deeply impressed by the cochairs'

1. Commission on Retirement Security and Personal Savings, *Securing Our Financial Future: Report of BPC's Commission on Retirement Security and Personal Savings* (Washington, DC: Bipartisan Policy Center, June 2016). See especially the executive summary. See also the useful compendium of graphical information about the recommendations at Bipartisan Policy Center, "The 6 Challenges to Retirement Security," https://bipartisanpolicy.org/the-6-challenges-to-retirement-security/; as well as the video at the Bipartisan Policy Center website, "Securing Our Financial Future: Report of the Commission on Retirement Security and Personal Savings," June 9, 2016, https://bipartisanpolicy.org/report/retirement-security/.

leadership and process acumen, as well as by the other commission members and an exceptionally capable team of staff.

As the commission included experts holding a wide range of policy views, a consensus report was only possible because its work was relentlessly data-driven, and because the cochairs skillfully incorporated input from the entire commission to forge balanced compromise. It is fashionable in political circles to characterize genuine compromise as containing something for everyone to dislike; a more accurate description in this case is that compromise would lead to far better results than either Left or Right would receive under the status quo.

The commission's recommendations were organized into six main themes:

1. Improve access to workplace retirement savings plans, largely by making it easier for employers to offer plans and to enroll workers in them, and by simplifying the decisions facing participants.
2. Promote personal savings for short-term needs and preserve retirement savings for older age, largely by making it easier for workers to manage, shift, and maintain savings among their various retirement accounts.
3. Reduce the risk of outliving savings, largely by facilitating the offering of retirement plan distribution options that would provide income over a retiree's full lifetime.
4. Facilitate the use of home equity for retirement consumption, largely through the use of reverse mortgages.
5. Improve financial capability among all Americans, largely by implementing the recommendations of the President's Advisory Council on Financial Capability and by clarifying the nomenclature used in key government programs such as Social Security.
6. Strengthen Social Security's finances and modernize the program by balancing its income and expenditures and by targeting its benefits more directly at needy households.

The commission report provides full details of the recommendations in all six areas.[2] Here I will focus on Social Security, where my expertise is

2. Commission on Retirement Security and Personal Savings, *Securing Our Financial Future.*

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

concentrated. The BPC Social Security recommendations involve far more details than can be covered here. However, they can be roughly defined by the following general parameters.

Parameter 1

The proposals would strengthen Social Security finances through a roughly 50–50 blend of changes to revenues and costs (per the Social Security chief actuary, 54% revenues vs. 46% cost containment).[3] Under current law, per Urban Institute projections, Social Security costs would rise from 4.8% of GDP today to roughly 6.2% of GDP by 2034 when the program's combined trust funds would be depleted and benefits reduced by roughly 22%. Afterward the financing gap would continue to grow, with eventual costs (6.4% of GDP) being only 73% funded by income (4.7% of GDP) at the end of the valuation period. Under the commission proposals, costs would instead rise more gradually to 5.8% of GDP (at the peak of baby boomer retirements in the mid-2030s) and stabilize thereafter, hovering around 5.5% of GDP for most of the mid-21st century. The biggest revenue changes would be increases in the Social Security payroll tax rate (from 12.4% to 13.4%) and wage base (to $195,000 by 2020). The biggest cost containment mechanism would be a gradual indexing of the normal retirement age to national longevity gains, raising it by one month every two years starting in 2022. Per convention, this was counted by the commission as a benefit constraint—although in practice, an individual receives higher annual benefits if he or she delays his or her initial benefit claim. The second largest cost containment provision would be to link annual COLAs to the chained consumer price index (C-CPI-U), so that they more closely track national price inflation. (See figure 1.)

Parameter 2

Under the commission proposals, real per capita benefits would grow substantially. Under current law, program costs would grow at rates beyond what revenues can finance, resulting in sudden benefit reductions upon

3. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Kent Conrad and James B. Lockhart III, Cochairs of the Commission on Retirement Security and Personal Savings at the Bipartisan Policy Center, June 9, 2016.

trust fund depletion. Under the commission proposals, individuals would be spared these benefit reductions, allowing seniors' Social Security benefits and total disposable income to both grow steadily relative to price inflation. (See figure 2.)

Figure 1. After the Baby Boomers Retire, the Commission Proposals Would Stabilize Social Security Costs/Revenues as a Share of GDP

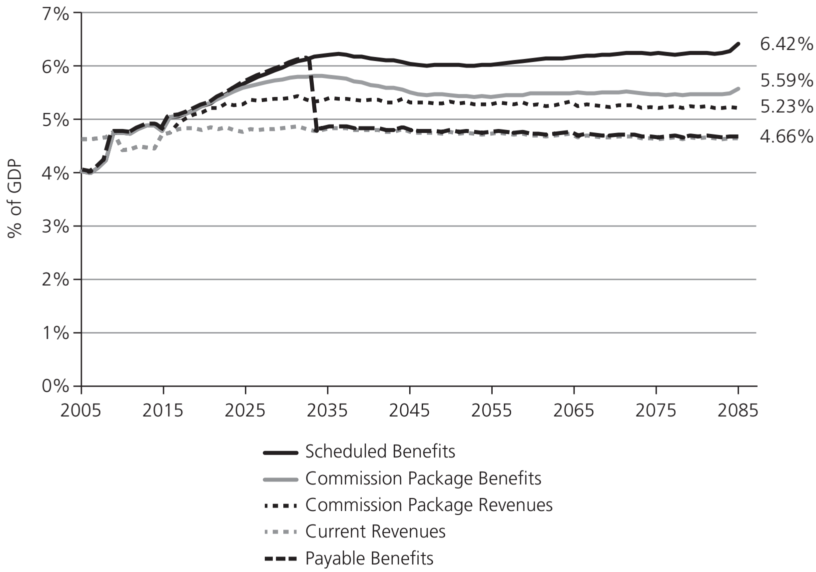
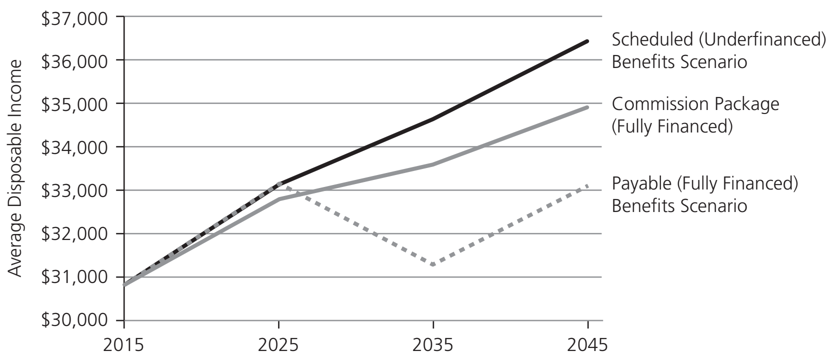


Figure 2. Projected Average Disposable Income (in 2015 Dollars) for Individuals 62 and Older



Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Parameter 3

The commission proposals would target benefit growth on low-income households and significantly reduce elderly poverty. For example, a two-earner couple born in 1993, in the bottom income quintile, working for 40 years with equal earnings would receive benefits 63% higher than could be paid under current law. Those in the second income quintile would receive a 49% benefit increase. Not only would these benefits be substantially higher than could be paid under current law, they are even higher (24% and 12% higher, respectively) than the current-law benefit formula that is significantly underfunded. Because of this faster benefit growth for low-income households, senior poverty levels would be substantially lower under the commission proposals, not only relative to current law but even relative to an imaginary scenario in which all Social Security's currently unfinanced benefits were somehow fully funded. (See figure 3 and table 1.)

Parameter 4

Returns on work would be higher under the commission proposals. It is often extremely difficult to design proposals that would provide substantial support

Figure 3. Senior Poverty Would Be Markedly Reduced under the Commission Proposals

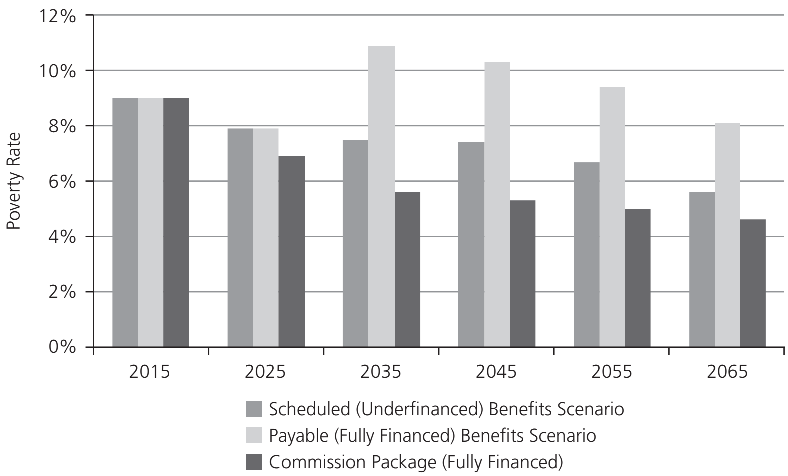


Table 1. Projected Lifetime Social Security/SSI Benefits for Workers Born in 1993

	Commission Proposals Relative to Benefits Payable under Current Social Security Law									
	Single individual					Two-earner couple (equal earnings)				
Work years	Bottom quintile	2nd quintile	3rd quintile	4th quintile	Top quintile	Bottom quintile	2nd quintile	3rd quintile	4th quintile	Top quintile
25	153%	156%	145%	127%	85%	152%	137%	127%	115%	81%
30	159%	156%	139%	120%	88%	151%	137%	127%	116%	90%
35	166%	153%	135%	118%	94%	153%	138%	131%	120%	98%
40	175%	158%	140%	125%	103%	163%	149%	142%	130%	108%
45	168%	147%	140%	128%	105%	159%	152%	147%	135%	110%

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

for low-income individuals while also providing adequate returns as individuals engage in paid employment. Table 1, however, shows that throughout the income spectrum, individuals would receive larger increases under the proposals the more years that they work. This is in sharp contrast with current law, in which returns on work decline dramatically for seniors, at precisely the point in their lives when they must make decisions about whether to remain in the workforce.[4] The commission proposals would accomplish this by reforming the benefit formula to accrue benefits with additional years of work rather than basing benefit levels solely on career average earnings.

Conclusion

The BPC retirement security commission proposals reflect a roughly 50–50 compromise between Left and Right as to how to shore up the finances of Social Security. All program participants would benefit from the stabilization of program finances, with the largest gains accruing to low-wage workers.

4. Charles Blahous, *Social Security: The Unfinished Work* (Stanford, CA: Hoover Institution Press, 2010).

Stabilizing Social Security without Raising Taxes

This article was originally published at E21 on January 4, 2017.

This piece can be thought of as a sort of companion to the previous one. Whereas the previous piece described a compromise Social Security financing plan as it emerged from two years of bipartisan negotiations, this one shows how a proposal might look if it reflected a particular viewpoint—in this case, former Representative Sam Johnson's goal to repair Social Security finances without imposing a tax increase.

This piece also walks through the general value judgments that must be made while putting together any Social Security reform package and explains where Johnson's proposal falls on the spectra of available choices.

THE INCOMING CONGRESS AND TRUMP ADMINISTRATION HAVE THEIR hands full with an ambitious economic policy agenda topped by, among other things, repealing and replacing the Affordable Care Act. However, a recent report by the Congressional Budget Office reminds us also of the worsening financial condition of Social Security, as did the annual trustees' report earlier this year.[1] This month Congressman Sam Johnson, chairman of the House Ways and Means Social Security Subcommittee, offered a detailed proposal to tackle the problem.[2]

Social Security reform proposals can be quite complex. It is often helpful to understand them in terms of the bottom-line value judgments they reflect. This article attempts to explain the Johnson proposal in those terms.

1. Congressional Budget Office, *CBO's 2016 Long-Term Projections for Social Security: Additional Information*, December 2016; OASDI Board of Trustees, *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.

2. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Sam Johnson, Chairman of the Committee on Ways and Means, Subcommittee on Social Security, December 8, 2016.

Value Judgment 1: The Total Sacrifices Required

This list begins with a trick entry. The total changes required to restore Social Security to financial balance do not actually embody a discretionary judgment. The Social Security shortfall is what it is; legislators can choose how to allocate the effects of closing it, but can't control the magnitude of the required corrections. When critics attack reform proposals for the hardships they allegedly inflict, they are being disingenuous in that any workable plan must require equally stringent measures.[3] If a plan makes fewer changes to benefits, it must make up the difference with larger tax increases. If a plan seems to require fewer corrections overall, it merely means additional income losses will be imposed on participants later that aren't yet being disclosed.

There's really only one way policymakers can affect the total measures required: by choosing when to act. Assuming we're not going to go back and cut benefits for people already collecting them, continued delay means greater income losses for those affected by measures required to maintain solvency. Thus, no one who offers a plan for action can rightly be blamed for imposing undue hardships. That blame belongs to those who delay the necessary corrections.

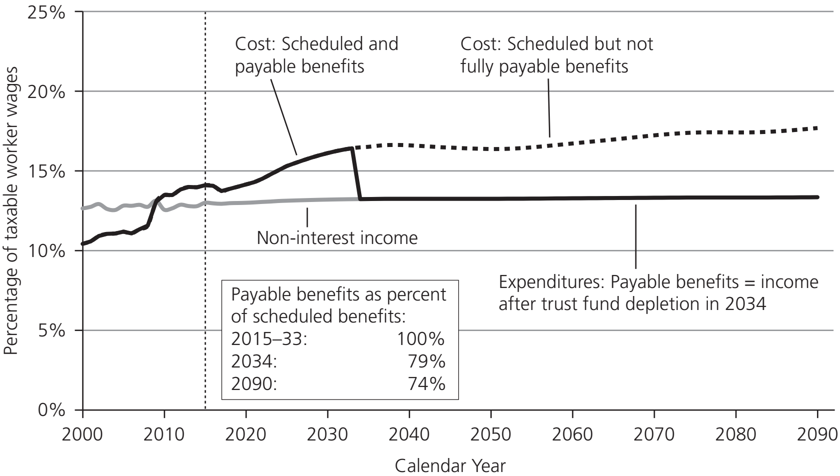
Before we move on, one quick technical point about the shortfall. The Social Security actuary tracks two measures of the long-term financing gap: the average gap over 75 years (2.66% of taxable worker wages) and the gap between taxes and expenditures in the 75th year (4.35% of taxable worker wages). (See figure 1, taken from the trustees' report). To achieve sustainable financing, a plan must eliminate both shortfalls, as the Johnson proposal would. Some proposals would close the shortfall by one measure but not the other.[4] Under such proposals, additional losses would await participants as the program's financing shortfalls later reemerge.

Value Judgment 2: Raising Taxes vs. Slowing Cost Growth

This is one of the most fundamental choices facing plan authors. Under current law, the cost of paying scheduled benefits well exceeds projected

3. John Wasik, "How GOP Social Security Cuts Will Hurt You," *Forbes*, December 14, 2016.
4. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Representative Reid Ribble, December 8, 2016.

Figure 1. Social Security Income, Cost, and Expenditures as a Percentage of Taxable Wages



Source: OASDI Board of Trustees, *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, 13.

program revenues. Should the gap be closed by slowing the growth of program costs, raising taxes, or some combination of the two?

The Johnson proposal would close the gap entirely on the cost containment side, without tax increases. One provision would calculate COLAs for most recipients using the chained CPI recommended by the Bureau of Labor Statistics as the best measure of inflation.[5] Another provision would phase in benefit formula changes to slow benefit growth for higher-income earners. Another provision would gradually increase the normal retirement age by three months a year starting in 2023 until it reaches 69 in 2030 (workers could still choose to claim benefits as early as age 62). Other provisions would affect program expenditures in roughly equal positive and negative amounts.

Existing plans run the gamut from those that would balance the system solely through cost containment to those relying on tax increases, with

5. Erica L. Groshen, "Statement of Erica L. Groshen, Commissioner, Bureau of Labor Statistics, U.S. Department of Labor" (Testimony before the House Committee on Ways and Means, Subcommittee on Social Security, April 18, 2013).

others roughly splitting the difference.[6] (In recent years, there have also been proposals to increase total costs even faster than current schedules, which would require still larger tax increases to sustain. These proposals have not generally been offered in a financially sustainable form.)[7]

There are of course arguments for every approach. The main arguments for Congressman Johnson's cost containment approach are

- the general desirability of keeping program cost growth from outpacing national economic growth (even a solution like Congressman Johnson's, based entirely on cost containment, will still see cost burdens rise through the late 2020s due to ongoing baby boomer retirements);[8]
- more equitable treatment of different generations (this is because the current shortfall consists entirely of an excess of scheduled benefits over taxes for people already in the system,[9] and leaving benefit schedules unchanged would lock in larger net income losses for younger generations as they are forced to make up the difference);
- Social Security cost burdens are already depressing after-Social-Security-tax wage growth relative to benefit growth, a situation that would be exacerbated by a tax-increase approach;[10]
- Social Security is an income transfer program rather than a savings program: hence, a tax-increase-based solution causes retirement benefit promises to increase without an accompanying increase in the national economic resources available to finance them.

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6. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Kent Conrad and James B. Lockhart III, Cochairs of the Commission on Retirement Security and Personal Savings at the Bipartisan Policy Center, October 11, 2016.

7. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Representative Linda Sanchez, December 8, 2016.

8. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Sam Johnson, Chairman of the Committee on Ways and Means, Subcommittee on Social Security, December 8, 2016.

9. OASDI Board of Trustees, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, table VI.F2, "Present Values of OASDI Cost Less Non-interest Income and Unfunded Obligations for Program Participants, Based on Intermediate Assumptions," https://www.ssa.gov/oact/tr/2015/VI_F_infinite.html#1000308.

10. Charles Blahous, "Understanding Social Security Benefit Adequacy: Myths and Realities of Social Security Replacement Rates" (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2012).

Value Judgment 3: Who Should Pay to Close the Shortfall

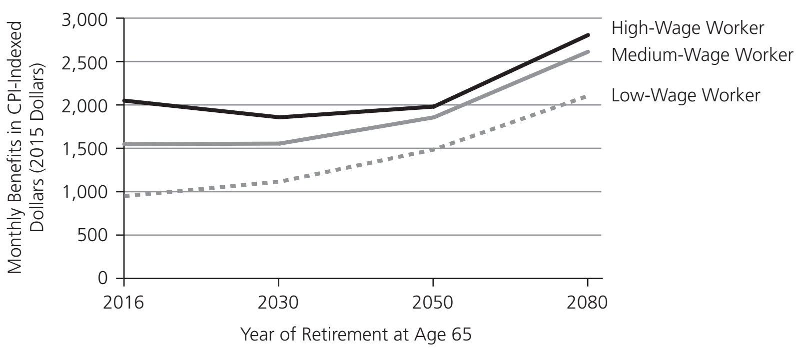
In the Johnson plan, the answer is very clear: higher-income beneficiaries. The proposal would eliminate COLAs for the highest-income participants who pay income-related Medicare Part B premiums. The plan's benefit formula constraints would impact roughly the upper half of income earners. Benefits for high-income, nonworking spouses would also be constrained to not exceed those earned by a low-income worker over a full career of program contributions. An increased special minimum benefit would be created for lower-income workers, growing with the number of their work years. The oldest beneficiaries at greatest risk of poverty would also receive a targeted benefit increase.

As a result, low-income workers working a full career would expect substantial benefit increases under the Johnson proposal, while the cost of restoring the system to financial balance would be borne by higher-income workers. (See figure 2.)

Value Judgment 4: Work Incentives

Another value judgment facing plan authors is whether, in the course of enacting financial corrections, to also correct other problems Social Security experts have identified. The Johnson proposal, like the BPC retirement

Figure 2. Monthly Benefits for Full-Career Worker, in 2015 Dollars



Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

security commission plan released earlier in 2016, attempts to repair specific work disincentives under current law.[11]

Experts have long understood that Social Security imposes a high marginal tax rate on employment earnings at precisely the moment in life when many are contemplating whether to retire,[12] and that individuals do respond to these incentives by leaving the labor market. Part of the problem is that Social Security calculates benefits based on lifetime average earnings rather than allowing individuals to accrue additional benefits with each further year of work, as the Johnson plan would. The Johnson plan would also eliminate the program's penalty for earnings after early retirement age, and give beneficiaries the option of receiving some delayed retirement credits as a lump sum, something other experts (such as Olivia Mitchell) suggest is attractive to workers.[13]

Conclusion

Reasonable people can and do make different value judgments about how best to stabilize Social Security finances. But for those who want to avoid tax increases, wish to correct problematic work disincentives, and wish to protect low-wage workers while requiring those with higher incomes to bear the cost of achieving financial stability, the Johnson proposal shows how these goals can be achieved.

11. Charles Blahous, "A Balanced Bipartisan Compromise for Strengthening Retirement Security," E21 (Manhattan Institute for Policy Research), June 23, 2016 (republished in this collection).

12. See, for example, Gopi Shah Goda, John B. Shoven, and Sita Nataraj Slavov, "Removing the Disincentives in Social Security for Long Careers," in *Social Security Policy in a Changing Environment*, ed. Jeffrey Brown, Jeffrey Liebman, and David A. Wise (Chicago: University of Chicago Press, 2009), 21–38.

13. James J. Green, "To Delay Social Security Claiming, Offer Lump Sum Benefit: Report," *ThinkAdvisor*, December 10, 2015.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Taxing More Earnings Won't Fix Social Security's Finances

This article was originally published at E21 on November 21, 2017.

H. L. Mencken memorably stated that "there is always a well-known solution to every human problem—neat, plausible, and wrong."[1] In Social Security policy, that solution is raising the annual earnings threshold above which Social Security taxes currently no longer apply. This purported answer to Social Security's financing shortfalls consistently polls better than any other, as most respondents believe it would only affect people richer than themselves. Virtually any discussion of the Social Security financing challenge features at least one individual advocating a taxable wage cap increase as the only necessary solution.

This collection includes another article sympathetic to the work of a Bipartisan Policy Center commission (on which I served) that included a Social Security tax cap increase among its recommendations.[2] But the fact remains that lifting the cap would fix very little of Social Security's long-term shortfall. Consequently, even proposals leaning heavily on that particular mechanism must also include other strong measures—usually ones the sponsors are less eager to discuss.

I published a previous article on this same subject back in 2011. Since that earlier publication, a focus on raising the tax cap has persisted on the left half of the American political spectrum. But at the same time the total Social Security shortfall has grown, rendering a tax cap increase even less effective for closing the shortfall. This piece, published in late 2017, updated the earlier material for more recent data and projections.

A FEW YEARS AGO, I EXPLAINED WHY THE FREQUENTLY FLOATED IDEA of increasing the amount of worker earnings subject to the Social Security tax would not fix much of the program's large and growing financing shortfall.[3] It seems worthwhile to update this information in the context of the evolving political climate surrounding Social Security, for two reasons. One

1. H. L. Mencken, *Prejudices: Second Series*, vol. 2 (New York: Alfred A. Knopf, 1920), 158.

2. Charles Blahous, "A Balanced Bipartisan Compromise for Strengthening Retirement Security," E21 (Manhattan Institute for Policy Research), June 23, 2016 (republished in this collection).

3. Charles Blahous, "Why Raising Social Security's Tax Cap Wouldn't Eliminate Its Shortfall," E21 (Manhattan Institute for Policy Research), April 12, 2011.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

reason is that the idea continues to turn up in more places, including congressional proposals, opinion columns, and options lists compiled by government scorekeepers.[4] The second reason is that Social Security's financial situation has deteriorated further since the original piece, so a tax cap increase today would solve even less of the problem than it would have back then.

The purpose here is not to oppose legislated adjustments to Social Security's maximum taxable annual earnings. To the contrary, I recently served on a Bipartisan Policy Center commission that included a tax cap increase in a package of retirement security recommendations I believe are worthy of lawmakers' strong consideration.[5] Moreover, political realities are such that virtually any bipartisan grand bargain to repair Social Security finances is likely to include such a provision. The purpose of this piece is instead narrowly informational: to explain why increasing (even eliminating) the cap wouldn't accomplish nearly as much financial improvement as many people believe.

Background

The 12.4% Social Security payroll tax is assessed on worker earnings up to an annual limit currently set at $127,200.[6] The cap is statutorily indexed to grow (with rare exceptions) with growth in the national average wage index.[7] A worker's eventual benefits are based in large part on his or her career earnings subject to payroll taxation.

The reason the cap exists is rooted in Social Security's historical design as a contributory insurance program rather than a welfare program. President Franklin D. Roosevelt and other program founders wanted to ensure that

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4. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Representative Charlie Crist, August 2, 2017; Stephen C. Goss, Chief Actuary of the Social Security Administration, to Representative Ted Deutch and Senator Mazie K. Hirono, July 20, 2017; Mark Miller, "Time to Raise—or Scrap—the Social Security Payroll Tax Cap," *Reuters*, April 15, 2014; Congressional Budget Office, "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax," December 8, 2016.

5. Commission on Retirement Security and Personal Savings, *Securing Our Financial Future: Report of BPC's Commission on Retirement Security and Personal Savings* (Washington, DC: Bipartisan Policy Center, June 2016).

6. Social Security Administration, "Benefits Planner: Maximum Taxable Earnings," accessed November 2017, https://www.ssa.gov/planners/maxtax.html.

7. Social Security Administration, "National Average Wage Index," accessed November 2017, https://www.ssa.gov/OACT/COLA/AWI.html.

Social Security covered and would have wide support from Americans, rich and poor.[8] As a result, workers at all income levels pay into Social Security, and workers at all income levels earn benefits as they do so. Past a certain point, higher-income people don't need extra benefits, so both their contributions and their benefits stop.

Financial Effects of Raising the Cap

Absent fundamental changes to Social Security's design, raising the cap on taxable wages would bring in more revenue up front but trigger additional outlays later on. This is because to a first approximation, the more you pay in, the greater the benefits you earn. Raising the cap both delays and modestly reduces Social Security's financing shortfalls, with the modest improvements coming primarily because less generous benefit returns are provided for tax contributions at the upper-income end. There is also a sense in which part of the apparent financial improvement is illusory—i.e., an artifact of actuarial calculations that capture several cohorts' increased tax obligations but not their additional benefit accruals.

Overall, a tax cap increase is a very inefficient way to improve system finances because it increases both tax collections and benefit expenditures for those who need them least. (A further factor is also relevant: that higher-income people's longevity improvements are outpacing those of poorer people;[9] if that trend continues, raising the tax cap—and thereby paying more benefits throughout higher-income people's longer lives—would be even less efficient in improving program finances.)

Graphs published by the office of the Social Security chief actuary illustrate the inefficiency of a tax cap increase. Figure 1 shows the projected effects of an often-floated proposal to raise the cap to cover 90% of all national wages. CBO has estimated this would require raising the cap to roughly $245,000.[10]

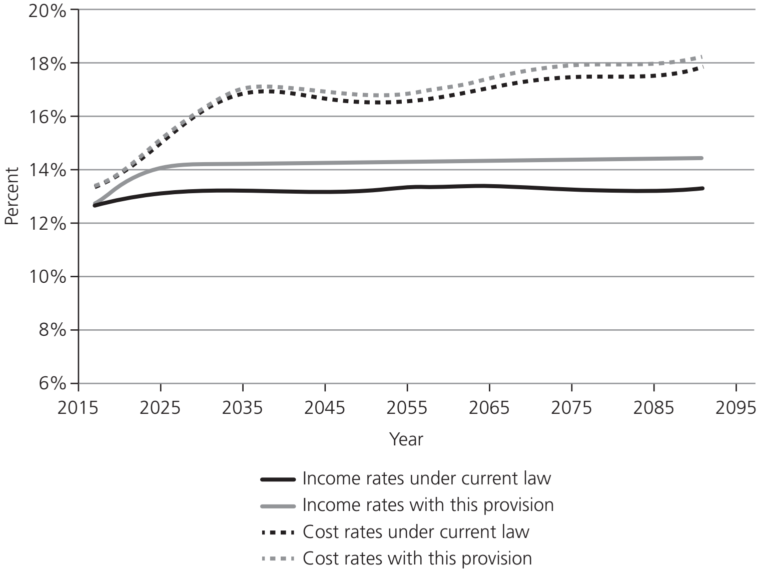
8. Franklin D. Roosevelt, "Address to Advisory Council of the Committee on Economic Security on the Problems of Economic and Social Security," November 14, 1934.

9. Steven H. Woolf, "How Are Income and Wealth Linked to Health and Longevity" (Income and Health Initiative Brief 1, Urban Institute and Center on Society and Health, April 2015).

10. Congressional Budget Office, "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax," December 8, 2016.

Excerpt from Charles Blahous, Decoding the Debates
(Arlington, VA: Mercatus Center at George Mason University, 2020).

Figure 1. OASDI Cost Rates and Income Rates (as a percentage of taxable payroll)



Note: "This provision" refers to the proposal to raise the cap on taxable wages to cover 90% of all national wages.

Source: Social Security Administration, "Summary Measures and Graphs," https://www.ssa.gov/OACT/solvency/provisions/charts/chart_run273.html.

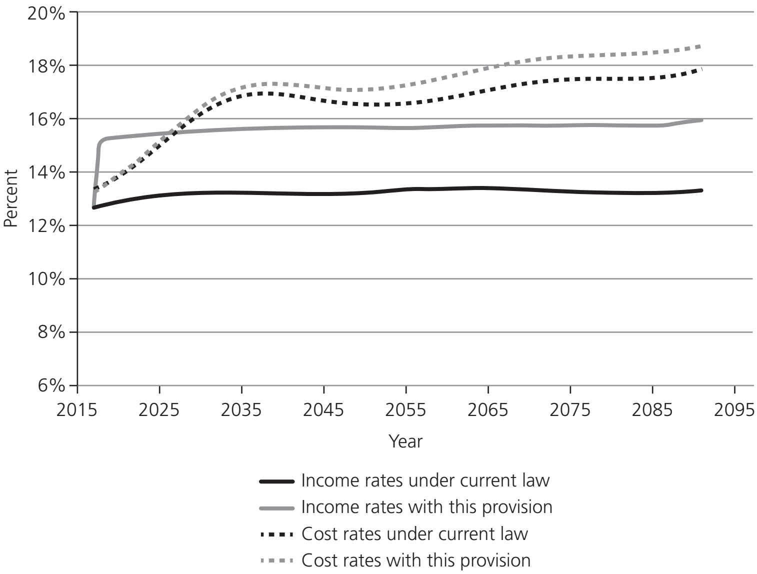
As figure 1 shows, raising the cap would cause tax collections to increase almost immediately (from the solid black line to the solid gray line) but would also cause expenditures to grow (from the dashed black line to the dashed gray line), reducing net annual shortfalls over the long run by only 14%.[11]

Even total elimination of the cap and exposing all US salary income to taxation (right on up to every last such dollar paid to Bill Gates) wouldn't fix most of the shortfall. In the out years, the annual gap between income and outgo would be reduced by roughly 36%,[12] leaving nearly two-thirds of the long-run financing problem in place. (See figure 2.)

11. Social Security Administration, "Summary Measures and Graphs," https://www.ssa.gov/OACT/solvency/provisions/charts/chart_run273.html.

12. Social Security Administration, "Detailed Single Year Tables," https://www.ssa.gov/OACT/solvency/provisions/charts/chart_run191.html.

Figure 2. OASDI Cost Rates and Income Rates (as a percentage of taxable payroll)



Note: "This provision" refers to the proposal to raise the cap on taxable wages to cover all national wages.

Source: Social Security Administration, "Detailed Single Year Tables," https://www.ssa.gov/OACT/solvency/provisions/charts/chart_run191.html.

The Hobson's Choice

Because of the situation illustrated above, proposals to raise the cap on taxable wages confront policymakers with a Hobson's choice between two alternatives:

- credit the additional contributions toward benefits, consistent with Social Security's historical design; or
- don't credit the additional contributions towards benefit, thereby abandoning Social Security's historical design.

Both choices are highly problematic. As noted above, choice 1 is very inefficient from a financing perspective, paying additional benefits to people who generally don't need them. Most experts would say choice 2 is even worse, because it would be a radical change to Social Security policy that leaves every participant's benefits less secure.

If and once the link between contributions and benefits were broken, this step almost certainly couldn't be undone. Moreover there is no reason to believe, once contributions above a certain income threshold are no longer counted toward benefits, that the specific dollar-amount cutoff will be set in stone forever. Ongoing financing pressures would virtually guarantee that the cutoff is frequently and perpetually adjusted downward, so that all of us would be at permanent risk of being forced to pay taxes into the program without receiving anything for those contributions.

There is a potential way out of this dilemma. An increase in the cap on taxable wages could be coupled with reductions in benefit accrual rates for higher earners. That way, less of the additional revenues collected would be sent inefficiently back out the door in the form of higher benefits. This would not fundamentally change Social Security's design, because higher earners already receive a lower return rate than lower earners: it would just be a matter of changing the number in the formula. A number of bipartisan proposals containing changes to the earnings cap have included variations on this approach, including that of the BPC retirement security commission as well as of the Simpson-Bowles commission.[13] On the other hand, one needn't raise the tax cap to slow the growth of higher-income participants' benefits in this way, improving finances and increasing program progressivity at the same time.

In any event, a tax cap increase by itself does very little to fix Social Security's financing problem. The pitfalls of the approach do not end there; they also include likely adverse effects on personal savings and economic growth, as well as the unwanted distributional outcome of hitting the upper middle class harder than the so-called 1%.[14] Still, the idea will undoubtedly remain part of the Social Security discussions because of the attractiveness to some of further taxing the rich. It just wouldn't do much to mitigate the other tough choices required to balance Social Security finances.

13. Commission on Retirement Security and Personal Savings, *Securing Our Financial Future;* National Commission on Fiscal Responsibility and Reform, *The Moment of Truth: Report of the National Commission on Fiscal Responsibility and Reform*, December 2010.

14. Charles Blahous, "Why Raising Social Security's Tax Cap Wouldn't Eliminate Its Shortfall," E21 (Manhattan Institute for Policy Research), April 12, 2011.

Seven Social Security Myths

This article was originally published at E21 on June 26, 2018.

This piece generated a surprising amount of positive feedback from colleagues, friends, and social media acquaintances. I had written in the past about persistent Social Security myths, but one resurgent internet trope—that Social Security, the prototypical federal entitlement program, somehow isn't an entitlement—was generating increased attention, prompting me to take on Social Security mythmaking in general. It won't be a surprise to most readers that a great many of the things written and circulated online about Social Security are simply wrong. This piece attempted to correct a few of the more prevalent myths in circulation.

AMONG PUBLIC POLICY ISSUES, SOCIAL SECURITY IS ESPECIALLY BESET BY myths and urban legends. These myths inhibit the enactment of legislation necessary to close its substantial financing shortfall. Press, public, and policymakers alike would do well to disabuse themselves of the following widely circulated canards.

Myth 1: Social Security Is Not an Entitlement

This is one of the more baffling myths in circulation of late. One encounters it on social media, on op-ed pages, even from members of Congress.[1] Social Security is not only an entitlement program, it is the largest and most prototypical federal entitlement program. Virtually any credible glossary of federal budget terminology will point to Social Security as the leading example of an entitlement (specifically, an entitlement is a program in which payments are obligated to beneficiaries according to eligibility criteria set

1. Bill Cruice, "Social Security Is Not an Entitlement," *Patriot-News*, February 21, 2013; Michael McIntee, "Video Replay & Transcript: Rep. Nolan Debates Challengers Mills & Sandman in Duluth," *The Uptake*, October 7, 2014.

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(Arlington, VA: Mercatus Center at George Mason University, 2020).

in law, without requiring annual legislation to appropriate funds).[2] Those who object to Social Security being referred to as an entitlement are in effect trying to change the definition to mean something other than what it always has. Whether a program is an entitlement has nothing to do with whether beneficiaries made previous contributions to it. In fact, in Social Security's case, it's precisely the individual entitlement to benefits arising from those contributions that makes it an entitlement program.

Myth 2: Social Security Wouldn't Be in Financial Trouble If Politicians Hadn't Stolen and Spent Its Money

There is actually a small kernel of truth underlying this myth: specifically, Social Security trust fund reserves are by law invested in US Treasury securities, which finance federal government spending. Furthermore, economists who have studied the issue generally conclude that government access to those revenues stimulated more federal spending than would have occurred otherwise.[3] But this phenomenon has nothing do with Social Security's shortfall. Social Security still owns all that money and earns interest on it. Whenever Social Security tax revenues fall short of its benefit obligations, as they have since 2010,[4] Social Security taps both the interest and principal of its trust funds to pay benefits. Social Security's shortfall exists *despite* the government's repaying those funds to Social Security, not because it won't. The program's financing problems arise instead from its benefits exceeding the revenue (including interest) that it generates.[5]

Myth 3: Participants Have Paid for Their Benefits

Again, there is a kernel of truth in this myth. Workers covered by Social Security contribute payroll taxes, which establish an entitlement to benefits for themselves and certain dependents. However, this does not mean they

2. Congressional Budget Office, "Glossary," January 2012; Office of Management and Budget, *OMB Circular No. A-11*, 2016, § 20; Bill Heniff Jr., "Basic Federal Budgeting terminology" (CRS Report for Congress, Congressional Research Service, November 26, 2012).

3. Kent Smetters, "Is the Social Security Trust Fund Worth Anything?" (NBER Working Paper No. 9845, National Bureau of Economic Research, Cambridge, MA, July 2003).

4. Social Security and Medicare Boards of Trustees, "Status of the Social Security and Medicare Programs," accessed June 2018, https://www.ssa.gov/OACT/TRSUM/tr18summary.pdf.

5. OASDI Board of Trustees, *The 2018 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, June 5, 2018.

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have paid for the full amount of their scheduled benefits. Many beneficiaries receive far more in benefits than their own contributions could ever fund, while others receive less. But, more importantly, Social Security has a shortfall precisely because in the aggregate, workers have *not* paid for their benefits: total scheduled benefits well exceed what workers' tax contributions, plus interest, can finance. So the existence of benefits has been earned, but the *scheduled amounts* have not. Benefit schedules would need to be substantially reduced from current law in order to match the benefit amounts workers have actually funded.[6]

Myth 4: Social Security Is Solvent until the 2030s, So There Is Still Plenty of Time to Fix It

One of the most misguided aspects of much press reporting on Social Security finances is the routine citation of its projected insolvency date (2034 in the latest report) as a proxy for its financial condition.[7] How soon Social Security's trust funds run out and how soon we must act are two entirely different things. By the time its trust funds are depleted, annual income and costs will be so far apart that there is no realistic chance of legislation closing the shortfall.[8] For example, even if all new retirees in 2034 were denied benefits, delaying corrective action until then would leave Social Security without enough revenue to continue sending the checks on time to those previously receiving them. When we must act is a function of how long the problem is still soluble, not when the funds finally run out. The window of opportunity for correction is closing now, if it hasn't closed already.

Myth 5: Because Social Security Is Self-Financing, It Doesn't Add to the Federal Budget Deficit

It is true that Social Security is technically "off budget" and has its own separate tax base and trust fund. But because the trust funds are invested in the federal Treasury, the general government fund plays a substantial role in Social Security financing. In the years before 2010, when Social Security ran

6. OASDI Board of Trustees, *2018 Annual Report*.
7. Mary Beth Franklin, "2034 Is a Pivotal Year for Social Security," *InvestmentNews*, June 5, 2018.
8. Bipartisan Policy Center, "Trustees Reports Highlight Social Security, Medicare Trust Fund Challenges," July 13, 2017.

a surplus, its operations reduced federal borrowing from the public. Since 2010, as Social Security's costs have exceeded its tax revenue, the federal government has been running larger deficits to fund the payments it owes to Social Security so that the program can continue to pay full benefits. A personal finance analogy might help. Suppose that during one month, you charge something to your credit card; then in subsequent months, you pay off the credit card debt, plus interest. In a certain sense you simply borrowed money from your bank that first month, then in the following months you paid it back. But during the months you are paying off that credit card debt, you tangibly experience a new and real financial strain, despite the fact that you were previously on the receiving end of credit. It's the same with the federal budget. The fact that the federal budget benefited from Social Security surpluses in the past doesn't make its ongoing deficit-worsening outlays, during the years it pays Social Security back, any less real.

Myth 6: Taxing Rich People More by Raising the Cap on Taxable Wages Will Fix the Problem

There's a statutory cap on each worker's annual earnings subject to Social Security taxes—it's $128,400 this year[9] and is indexed to grow automatically in most years. Above the cap, workers neither pay additional taxes nor accrue additional benefits, reflecting the program's design as a floor of income protection rather than an all-encompassing pension benefit. Whenever Social Security's shortfall is discussed, someone usually suggests raising this cap, to collect more taxes from the rich. That could certainly be done in the context of a solvency plan, but it doesn't solve much of the problem. Raising the taxable maximum from today's level all the way to about $350,000 in 2022 would only eliminate about 14% of the structural deficit,[10] in part because a worker's benefits are linked to his or her tax contributions and thus the tax increase would generate higher benefits for the well-off. That cost increase could of course be prevented by changing the benefit formula on

9. Social Security Administration, "Table 2.A3. Annual maximum taxable earnings and contribution rates, 1937–2018," https://www.ssa.gov/policy/docs/statcomps/supplement/2018/2a1-2a7.html#table2.a3, accessed June 2018.

10. Stephen C. Goss, Chief Actuary of the Social Security Administration, to Representative Reid Ribble, July 13, 2016; Social Security Administration, Office of the Chief Actuary, "Summary Measures and Graphs: Category of Change: Payroll Taxes (Including Maximum Taxable)," July 13, 2017.

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the high-income end; nevertheless, the point remains that without benefit formula changes, a tax cap increase by itself doesn't accomplish very much.

Myth 7: Social Security Privatization Is a Live Option

During election seasons there are always some partisans claiming that Social Security is at risk of being "privatized."[11] That was never true, and the claim is particularly absurd now. Many years ago when Social Security was running surpluses, presidents such as Bill Clinton and George W. Bush suggested that workers be given the option of saving them in personal accounts to shelter that money from being used to finance federal spending (see myth 2).[12] None of those proposals involved privatization, but instead would have allowed for individual saving within a publicly administered system. That opportunity vanished in 2010 when Social Security began running cash deficits. Since then there have been no surplus Social Security contributions to save, and every program tax dollar collected now is immediately sent out the door to pay current benefits. Despite the fact that this has long been a dead issue, occasional "privatization" fear-mongering continues.

The late Senator Daniel Patrick Moynihan was fond of saying, "everyone is entitled to their own opinions, but they are not entitled to their own facts." Social Security policy and politics are treacherous enough even when everyone agrees to respect the facts. If we are to see Social Security through to financial safety, we can no longer afford to indulge these seven myths.

11. Nancy Altman, "Trump and Ryan Agree: Let's Dismantle Social Security," *HuffPost*, May 16, 2016.

12. William J. Clinton, "Remarks by the President via Satellite to the Regional Congressional Social Security Forums," Albuquerque, New Mexico, July 27, 1998; George W. Bush, State of the Union address, February 2, 2005.

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