Introduction

It is accepted by both parties that the Social Security (SS) trust funds will be exhausted by 2036. Based on the 2010 Trustees report the National Commission on Fiscal Responsibility and Reform has said to "do-nothing … would lead to an immediate 22 percent across-the-board benefit cut for all current and future beneficiaries in 2037."[1] The 2011 Trustees' Report has moved the date benefits would be cut from 2037 to 2036 and would result in a 23 percent decrease in benefits.

Although often referred to as a single trust fund, social security is made up of two trust funds, the Old-Age and Survivors Insurance (OASI) trust fund and the Disability Insurance (DI) trust fund. According to the 2011 Trustees' Report, the OASI will become insolvent in 2038 and the DI will become insolvent in 2018. The 2036 date assumes OASI funds will be used to extend the DI fund's solvency.

The SS system is funded by payroll taxes, interest from U.S. securities held by the trust funds and taxes on SS benefits. At the end of 2010, the trust funds had combined assets of over $2.6 trillion.

"As recently as the early 1980s, the SS payroll tax covered 90 percent of wages (9 of every 10 dollars in wages were subject to the payroll tax). Since then, however, the taxable maximum wage cap (currently $106,800) has not grown as fast as wages above the cap; as a result, less than 86 percent of wages were subject to the payroll tax in 2009, and less than 83 percent will be subject to the tax by 2020."[2]

The SS system paid out more than it collected in payroll taxes in 2010 and is expected to pay out more in than it collects in 2011. "Although the system's revenues and expenditures are expected to return to balance temporarily in 2012, it will begin running deficits again in 2015 if interest from the trust fund is excluded and in 2025 including interest payments."[3]

Payments from the DI trust fund accounts for one-sixth of all SS benefits. "The growth in spending for Disability Insurance has been driven largely by an increase in the number of people receiving benefits. In 1980, 4.7 million people received DI benefits; by 2009, there were 9.7 million beneficiaries."[4]

About 157 million people work and pay SS taxes today and about 54 million people receive monthly SS benefits. Of the 54 million about 37 million are retirees. By 2035, about 93 million people will collect SS benefits. It was anticipated that the number receiving benefits would increase sharply as the baby boomers began to retire. However the recession forced many seniors who would like to work, to file for social security because they were laid off. This resulted in more funds going out, and less payroll taxes being collected.

Diverse proposals to restore SS's solvency have been made by the Trustees, the Congressional Budget Office, the National Commission on Fiscal Responsibility and Reform, the Bipartisan Policy Center's Debt Reduction task Force's Restoring America's Future Plan, the Center for American Progresses' A Progressive Framework for Social Security Reform and politicians such as Presidents Clinton and Bush and Republican Congressman Paul Ryan. We have used all in developing this issue paper. However before discussing solutions we would like to give a brief history of the social security system.

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[1] National Committee on Fiscal Responsibility and Reform, page 49
[2] National Committee on Fiscal Responsibility and Reform, page 51
[3] National Committee on Fiscal Responsibility and Reform, page 49
[4] Congressional Budget Office, page 24

History

1935 - SS signed into law by Pres. Roosevelt and provided retirement benefits only to workers.
1937 - The tax rate was 1% for both employee and employer.
1937 - The taxable maximum was $3,000.
1939 – Amended SS to include payments to the spouse and minor children of a retired worker and survivor benefits paid in the event of the premature death.
1940 - First monthly benefit checks were distributed and didn"t change until 1950
1950 - SS amended to give the first cost of living adjustment (COLA) and allowed those 75 and older to work and not to have their benefits reduced.
1951 - The self-employed began to pay into SS.
1954 - Amendment allowed those 72 and older to work and not to have their benefits reduced.
1956 - Amended to provide benefits to disabled workers aged 50-64 and disabled adult children.
1956 - Women were allowed to retire at 62 with reduced benefits.
1957 - The disability insurance payroll tax was collected for the first time.
1960 - SS was amended to eliminate the age-requirement for a disabled worker and their dependents to collect benefits.
1972 - Amendment made the annual COLA increases automatic starting in 1975, allowed men to retire at age 62 with reduced benefits, and granted an increase in benefits to those who delayed their retirement passed their full retirement age.
1977 - Amendment allowed those 70 and older to work and not to have their benefits reduced.
1983 - SS benefits were taxed for the first time, gradually increased the full retirement age to 67 and required all members of Congress, the President and Vice President to pay into social security.
1984 - Up until 1984, the self-employed paid less in SS taxes then what employees and employers paid combined.
2011 - The taxable maximum is $106,800.
2011 - Employees and the self-employed will have their tax rate reduced by 2%. Money will be transferred from the federal government's general fund to the SS trust funds to make up for the 2% reduction in the tax rate.

Discussion of Proposals

Proposals to address SS's solvency problem include getting a better return on investment on the assets in the trust funds, diverting payroll taxes to private accounts, decreasing benefits and/or increasing taxes. Not all proposals are included in this discussion.

Private Accounts

In May 2001 Pres. Bush signed an Executive Order establishing the President's Commission to Strengthen Social Security. The goal was to provide recommendations to restore fiscal soundness to SS. Any recommendation made by his Commission "must include individually controlled, voluntary personal retirement accounts."[5] President Bush's Commission came up with three options all of which allowed individuals to divert part of their social security tax to personal accounts.

In 2010 Republican Congressman Paul Ryan from Wisconsin in his Roadmap for America's Future also proposed allowing individuals to divert part of their security tax to personal accounts.

According to proponents of personal accounts, they "would allow workers to build a significant nest egg for retirement that far exceeds what the current program can provide."[6] Opponents argue that individual accounts expose workers' guaranteed retirement income to market downturns. Opponents also argue that diverting SS taxes from the trust fund would put the SS benefits for those currently retired or those

[5] President Bush's Commission to Strengthen Social Security
[6] Congressman Ryan's A Roadmap for America's Future

not taking part in private accounts in jeopardy. Proponents argue that those retired or those "nearing" retirement would not have their benefits reduced.

The money diverted to private accounts would no longer be part of the federal budget. Right now the portion of SS taxes not required for administration and to pay benefits is invested in government debt obligations. General revenue funds are then used to pay the interest and the cost to redeem these debt obligations. Private accounts would therefore reduce the government's liabilities.

Investment of Trust Fund Reserves in Marketable Securities

In 1999, Pres. Clinton proposed investing some of the SS trust fund's reserves in the financial markets. This would have the same effect of reducing the amount of debt obligation that would be kept on the government's books, while allowing for a potential greater return on investment. The Trustees in their 2009 report have also proposed allowing SS to invest part of the trust fund's reserves in equities, corporate bonds, etc.

Opponents of this proposal argue that the government by getting involved in the market place would be creating winners and losers.

Change how the cost-of-living adjustment (COLA) is calculated

Shift the calculation of annual COLAs from the Consumer Price Index to the "chain-weighted" Consumer Price Index (CPI). The chained-weighted CPI accounts for changes in consumers' purchasing patterns. For example, when the price of apples goes up, people can reduce the impact by substituting oranges.

Based on projections by the Congressional Budget Office using the chain-weighted CPI would result in annual COLA increases growing on average an estimated 0.3 percentage points per year more slowly then if the current CPI calculation were used.

Move to a more progressive formula to determine initial benefits.

Initial benefits are currently calculated using a three-bracket formula. Under a proposal by the National Commission on Fiscal Responsibility and Reform, SS would gradually move to a four-bracket formula which would slow benefit growth, particularly for higher wage earners.

Index the benefit formula to reflect longevity

The Bipartisan Policy Center's Debt Reduction task Force's Restoring America's Future Plan proposes adjusting the initial benefit formula to reflect improvements in life expectancy. "This proposal marginally reduces the replacement rates for each successive cohort of beneficiaries, meaning that retirees will receive very slightly smaller monthly benefits, but for longer periods of time."[7] This proposal would reduce the initial benefits for all beneficiaries.

Raise the social security payroll tax on both employers and employees

The Trustees have made several proposals to raise the payroll tax. Several of the proposals raise the payroll tax gradually over forty to sixty years, One proposal would increase the payroll tax by less than 1%, another by 4%. One proposal raises the payroll tax by 2.2% immediately.

Impose a 3% surcharge on all income over $200,000

In 2005, the Center for American Progresses' A Progressive Framework for Social Security Reform proposed a 3 percent surcharge on all income over $200,000, whether the income was from wages,

[7] Bipartisan Policy Center's Debt Reduction task Force's Restoring America's Future Plan. Page 78

dividends or capital gains. The author of the report, Gene Sperling, is currently the director of President Obama's National Economics Council

Increase the income subject to the social security payroll tax.

There are several proposals to increase the maximum taxable income from the current $106,800.

Proposals by the Bipartisan Policy Center's Debt Reduction Task Force and President Obama's National Commission on Fiscal Responsibility and Reform would gradually increase the taxable cap to once again cover 90 percent of wages. If we were taxing 90 percent of all earnings today, the maximum taxable cap would be $180,000.

Two proposals by the Trustees would eliminate the taxable maximum cap therefore subjecting all earnings to the social security payroll tax.

One of their proposals would make all earnings subject to the payroll tax and credit them for benefit purposes. The other proposal would not credit for benefit purposes earnings above the taxable maximum. Under their second proposal the taxable maximum under current law would still be used to calculate benefits.

Expand Social Security Coverage to Newly-Hired State and Local Workers

Today there are about 4 percent of workers who do not pay SS payroll taxes. The largest group of workers, about 5.7 million in 2007, who do not pay SS taxes are state and local government employees. The Bipartisan Policy Center's Debt Reduction task Force's Restoring America's Future Plan has proposed requiring all newly-hired employees of state and local governments after 2020 to pay SS taxes.

Increase the Early And the Full Retirement Age

The National Commission on Fiscal Responsibility and Reform has proposed gradually increasing the full retirement age to 68 and the early age to 63 by 2050 and increasing the full retirement age to 69 and the early retirement age to 64 by 2075.

The Trustees have made eleven proposals affecting the full and/or early retirement age. Some would quicken the date the full retirement age would be set at 67, some would increase the full retirement age, from between 68 to 70 over a period of time and some would gradually increase the early retirement age, up to 65, over a period of time.

Policy Position

We do not have access to all data nor do we have the technical expertise to develop a comprehensive plan to solve SS's solvency problem. Our role as a progressive organization is to support proposals that will help restore the program's solvency over a 75 year period, (the time period used by the Trustees to determine solvency) that will maintain SS as a defined government benefit program, and provide financial security in citizens' senior years.

Therefore we strongly oppose diverting payroll taxes to private accounts because this will begin the process of moving social security away from a government-controlled program. No other proposal has the potential of having bigger negative impact on changing the SS program than private accounts.
We also strongly oppose increasing the current payroll rate because the payroll tax is a regressive form of taxation. Those earning under the maximum salary cap pay a bigger percentage of their income in payroll taxes than higher income individuals.

We hold judgment on whether the government should be allowed to invest excess SS trust funds until this proposal has been thoroughly debated. The prospect of bigger returns and less government liability are very alluring but we believe this proposal has not yet received the examination such a major change requires.

If changing the COLA formula, moving to a more progressive formula for determining initial benefits or indexing benefits for longevity results in a decrease in benefits, than we oppose these proposals.

Raising the retirement age can be problematic for some in demanding jobs or those requiring extended travel time. It will also increase the unemployment rate.

We support expanding social security coverage to include state and local workers who are currently exempt. Having more workers pay into the system increases the programs solvency.

We support imposing a 3% surcharge on all earnings above a certain amount. Payroll taxes only capture wages, leaving other forms of income such as capital gains exempt from contributing to SS. A surcharge, especially on non-wage forms of income, would capture income that now avoids payroll taxes.

We support raising or preferably eliminating the maximum taxable income. This would make the payroll tax system more progressive.

In conclusion, we advocate for a solution that at least raises the taxable maximum income to once again capture 90 percent of wages and adds a surcharge to non-wage income for high income individuals. We also oppose any solution that moves SS towards privatization by allowing individuals to divert part of their SS taxes to personal accounts that increases the current SS payroll tax or decreases benefits.

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