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Social Security's Unexpected Deficits Show Urgent Need for Reform

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Starting this year, Social Security will spend more in benefits than it will receive from its payroll taxes. This is somewhat unexpected as just last year, the 2009 cash surplus was predicted to be about $80 billion. Even in May of this year, the program's actuaries predicted a roughly $19 billion surplus. However, they failed to allow for the full effects of the recession, and the soaring unemployment both reduced tax collections and increased the number of workers who were forced to take early retirement.

This is very bad news for taxpayers, but worse is yet to follow. The 2009 deficit of about $10 billion will be followed by a 2010 deficit of about $9 billion. If there is a strong recovery—which is questionable at best—the program could briefly return to surpluses. But by 2016, deficits will return and continue permanently. A far more likely scenario is that Social Security will run deficits from this point on.

The Reality of the Trust Fund. These deficits do not mean that benefits will be cut, but they do increase the burden on taxpayers to pay them. On top of the $1 trillion-plus deficit predicted for this year to pay for the Obama Administration's programs, taxpayers will have to find still more money to pay Social Security's deficits. It is true that a trust fund exists that has been funded by $2.4 trillion of Social Security surpluses since 1983, but there is no real money in that trust fund.

As the Office of Management and Budget said in 2000, "These balances are available to finance future benefit payments…only in a bookkeeping sense. They do not consist of real economic assets that can be drawn down in the future to fund benefits. Instead, they are claims on the Treasury that, when redeemed, will have to be financed by raising taxes, borrowing from the public, or reducing benefits, or other expenditures."[1]

Congress has already spent every penny of that money, and all that is left are IOUs that must be repaid by the same taxpayers who paid the extra taxes in the first place. Taxpayers, not the trust fund, will end up covering Social Security's deficits.

Massive Deficits and an Even Worse Future. This May, Social Security predicted that it would first run deficits in 2016, and after that the picture was grim. After adjusting for inflation, annual deficits were predicted to reach $68.5 billion in 2020, $170.4 billion in 2030, and $293.6 billion in 2035. Now those deficits will come much sooner than expected.

In net present value terms, Social Security owes $7.7 trillion more in benefits than it will receive in taxes. This consists of $2.4 trillion to repay the special issue bonds in the trust fund and $5.3 trillion to pay benefits after the trust fund is exhausted in 2037. In other words, Congress would have to invest $7.7 trillion today in order to have enough

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money to pay all of Social Security's promised benefits between 2016 and 2083. This money would be in addition to what Social Security receives during those years from its payroll taxes.

According to the 2009 Trustees Report, Social Security is projected to owe $7.4 trillion after 2083, making a perpetual deficit of $15.1 trillion. Last year's number was $13.6 trillion. This means that Social Security's total deficit continues to grow well beyond the 75-year projection period. Therefore, any reform that just eliminates deficits over the 75-year window will not be sufficient to solve the program's problems.

Many opponents of reform claim that raising payroll taxes by about 2 percent (the average percentage difference between revenues and outlays over the 75-year period) would solve Social Security's problems. The reality, however, is that the program's future deficits are projected to be large *and* growing, so this tax increase would still leave a huge shortfall.

Short-Term Fixes. There are three ways to fix Social Security:

1. Reduce benefits,
2. Increase retirement savings, and
3. Raise taxes.

The first two will take years to have a real effect. Accounts of any size need to grow for about 20–25 years before they are large enough to pay much in the way of retirement benefits. Moreover, benefit changes are politically feasible only if current retirees and those close to retirement are not affected, which means that it would be several years before benefit changes start to take effect.

On the other hand, some prefer tax increases because they would immediately pump money into Social Security. But that band-aid would just delay the start of real long-term reform and make it much more likely that Congress would keep taking the easy way out by raising taxes.

Fix Social Security Now or Face the Consequences. Social Security's future has arrived early. After years of talk about how well-funded the program is, the reality is that never-ending deficits will eat up money that could be used for other programs or tax cuts. Despite reassuring words that these deficits are temporary, the reality is much worse. These deficits are likely to be permanent, and the only way out of this cash crunch is to fix the program.

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1. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2000: Analytical Perspectives* (Washington, D.C.: U.S. Government Printing Office, 1999), p. 335.