Saving Social Security

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Outline

- What is Social Security?
- Why is Social Security in Trouble?
- Principles for Saving Social Security.
- A Bipartisan Solution.

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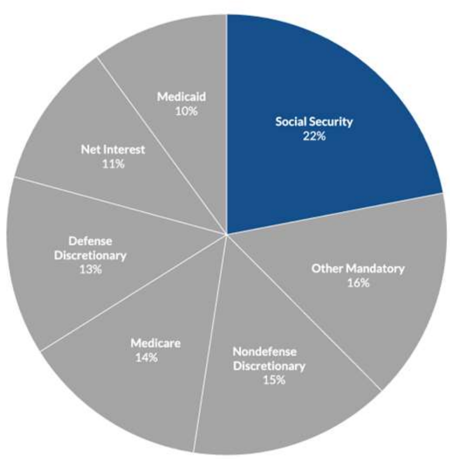
What is Social Security?

- Social Security is a federal social insurance program that provides financial support to workers and their families.
- Different benefits:
  - **Retirement Benefits**: Social Security provides monthly payments to qualified retirees based on their lifetime earnings.
  - **Disability Benefits:** It provides financial support to individuals who are unable to work due to a disability.
  - **Survivor Benefits:** Social Security offers benefits to the families of deceased workers, including spouses and children.

Soc Sec is The Single Largest Gov't Program

2023 Outlays: $6.1 Trillion



Source: Office of Management and Budget • Get the data • Embed • Download image
Note: Outlays for Social Security include non-retirement benefits.

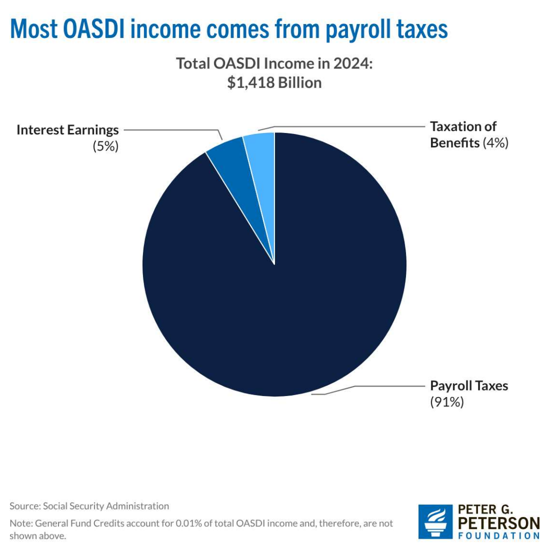
PETER G. PETERSON FOUNDATION

Source: https://www.pgpf.org/article/9-facts-about-social-security-and-the-need-to-strengthen-it/

The Mechanics of Social Security

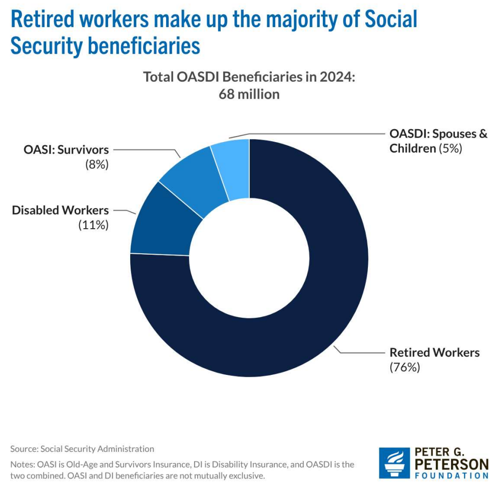
- **"pay-as-you-go" system**
  - Payroll taxes are collected from current workers.
  - These pay for the benefits of the currently retired, or otherwise eligible.
- **Taxes**
  - Payroll taxes amount to 12.4% of earnings.
    - Workers pay 6.2% of earnings as payroll taxes.
    - Employers also pay 6.2% of worker's earnings.
  - ***Earnings Cap.*** Not all earnings are subject to payroll taxes.
    - In 2026, only the first $184,500 of earnings are taxed.
    - Earnings above that level are not taxed.

Sources of SS Revenue



In addition to payroll taxes, up to 85 percent of social security benefits are subject to income taxes.

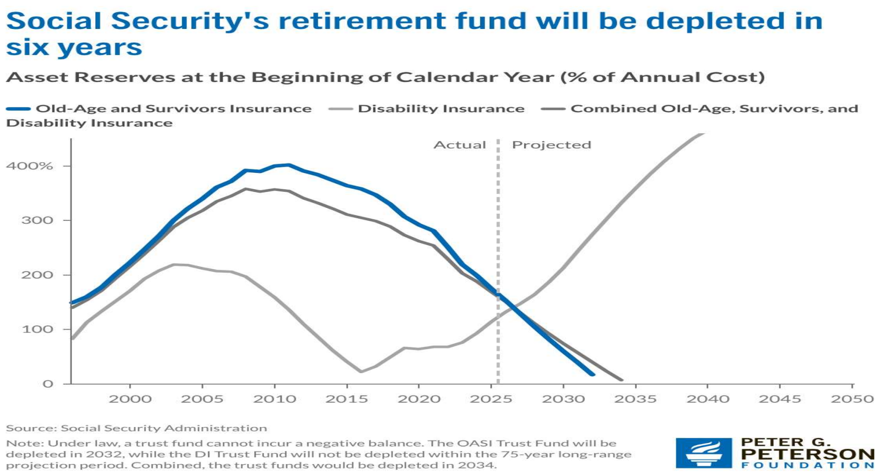
Where Does the Money Go



What if Payroll Taxes Don't Match Benefits?

- **The Trust Fund**
  - If revenues exceed benefits, the trust fund is credited with **non**marketable government securities by the amount of the surplus.
  - If benefits exceed revenues, the trust fund redeems **non**marketable securities by the amount of the deficit.
  - Really just one branch of government lending to another
  - **The existence of the trust fund has no economic significance: The amount the government must borrow depends on total federal spending (including Social Security) less total tax revenue (including Social Security taxes).**
- **But the existence, or lack thereof, has enormous political significance: If the Trust fund is exhausted, Social Security benefits by current law are limited to Social Security income.**

The Problem: Trust Funds are Running Out



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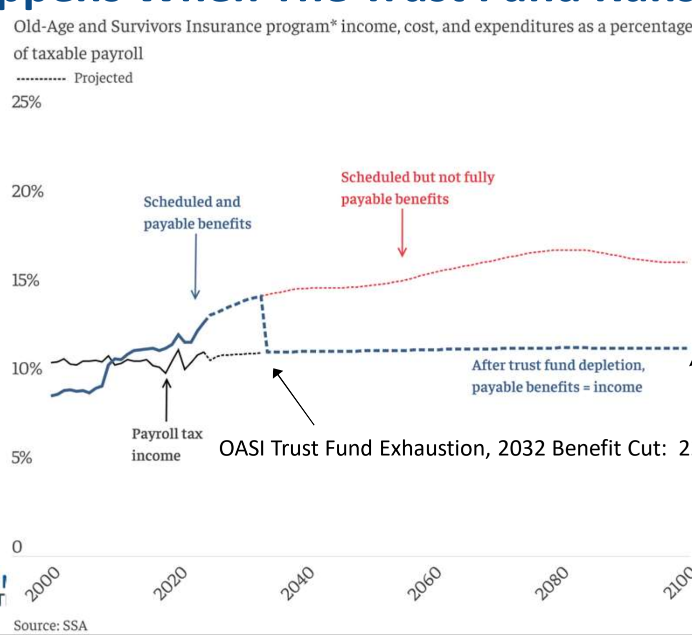
What Happens When The Trust Fund Runs Out?



Benefit Cut: 26% 2098

OASI Trust Fund Exhaustion, 2032 Benefit Cut: 22%

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Why Are Costs Rising Rapidly

Aging population: more beneficiaries and fewer contributors (workers).

1. Boomers are collecting benefits
2. Baby Bust: lower birth rates: 2030 deaths will exceed births.
3. Net immigration is way down.
4. Life expectancy: In 1980 a 65-year old female could expect to live to 83, now 86.
5. Workers per SSA beneficiary: 1966, 3.9; 2026, 2.6; 2046, 2.2.

Source: https://www.pgpf.org/article/how-does-social-security-work/

A Closer Look at Retirement Benefits?

Benefits are Based on Your Primary Insurance Amount (PIA)

PIA which depends on:

- **Your work history.**
  - Your average highest earnings over 35 years, where earlier years are indexed to wage inflation.
  - Except that earnings for any year are "capped," currently at $184,500
- **Income Cap roles:**
  1. Remember earnings above the cap are not taxed.
  2. But, earnings above the cap do not affect individuals' average SS Income.
- **PIA determines Retirement Benefit of a single retiree at Full Retirement age, 67**

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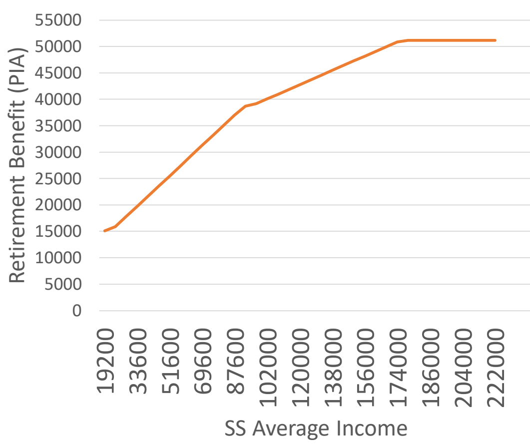
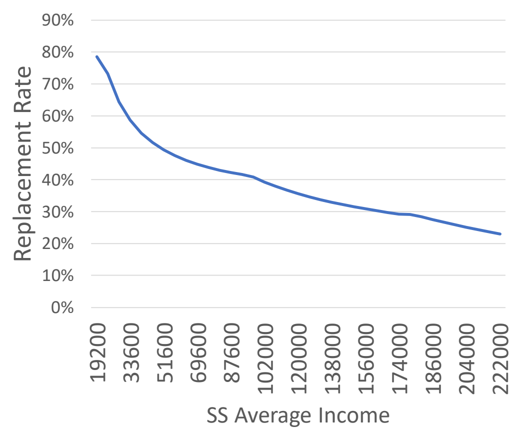
Benefit Formula is Highly Progressive





For every dollar average income exceeds $93K, benefits increase by 15 cents

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Benefit Adjustments to PIA

- **Benefits payable for life and indexed to CPI inflation**
- **Marital Status:**
  - With nonworking spouse adds 50% of PIA at full retirement age.
  - Workings spouse can claim off own earnings record if it is greater
- **Age when claiming**
  - Early: 62, 70%; 63, 75%; 64, 80%; 65, 86.67%; 66, 93.33%
  - Delayed, 68, 108%, 69, 116%; 70, 124%
  - Designed to be (roughly, on average) actuarially fair.

Remember We Have a Problem

- **Solving the Social Security problem is simple:**
  More revenues and/or
  Reduced benefits

- **Why hasn't this happened?**
  Politics!

Personal Opinion: Disingenuous & Unhelpful

Scott Bessent, Treasury Secretary at his confirmation hearings:

"These entitlements are massive. I think the next four years isn't the time to deal with them, that we've got to deal with the discretionary portion of the budget…then the next step is for a future administration to have the confidence to be able to deal with entitlements."

Total Federal Spending last fiscal year $7 trillion: 60% Mandatory (mostly Social Security and Medicare); 27% was discretionary, and 14% was interest on the debt.

One Big Beautiful Bill and Immigration Policies are a major reason Social Security Finances got worse in 2025.

https://www.foxbusiness.com/politics/treasury-secretary-nominee-scott-bessents-3-3-3-plan-what-know

So, Let's Consider Some Options

But the appropriate choices depend on the goals of the program!

Not mutually exclusive goals of Social Security:

1. **Partial earnings replacement via forced savings.**
2. **Social Insurance: protect workers against risks that are hard to insure privately.**
3. **Poverty Prevention among the elderly.**

1. SS as One Leg of the Three-Legged Stool

Why Forced Savings?

1. **Private Pensions**
   - But, only 50-55 percent of private-sector workers are covered mostly by Defined Contribution Plans, as opposed to old-style Defined Benefit Plan.
2. **Private Savings**
   - But, roughly 50 percent of workers aged 55-64 have little or no private savings (does not include housing wealth).

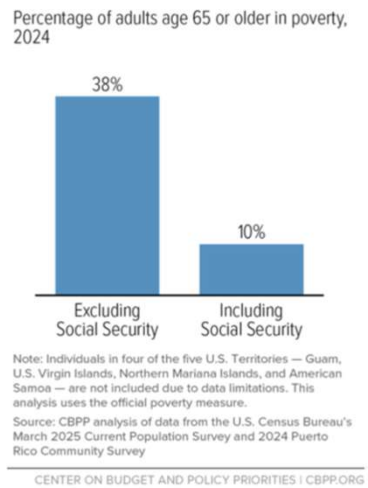
The weaknesses of these 2 legs is worse the poorer the household. Also, both these legs are subject to investment and inflation risk.

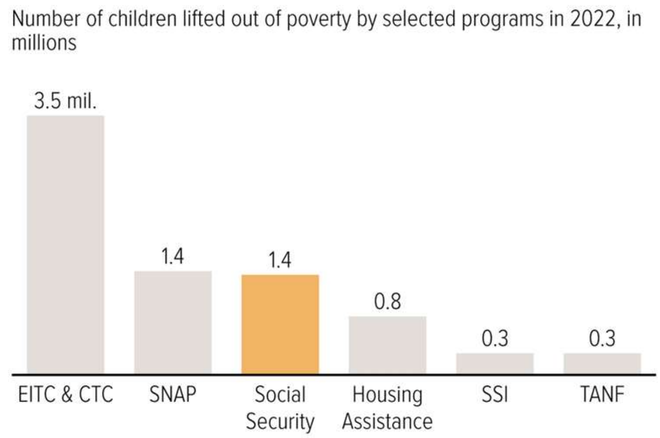
(From 1970-2025 the S&P 500 fell by 20% or more 7 times).

2. SS Insures Against Significant Risks

1. **Protects against becoming disabled.**
2. **Protects survivors, widow(er)s and children.**
3. **Protects against outliving resources because it acts like a lifetime annuity with the important added benefit that benefits are indexed to inflation**

3. Soc Sec Significantly Reduces Poverty





Implications of 3 Different Goals

If there were only one goal (which there is not), what would be the implications for saving Social Security?

1. **Forced Savings: Maintain a link between taxed earnings and benefits.**
2. **Social Insurance: Survivor and disability benefits are central. Progressivity in benefits is appropriate because low earners face greater risk.**
3. **Poverty Prevention: Payroll tax links to benefits is a historical artifact. Means-tested benefits. (Conflicts with 1.)**

Brookings Principles for a Solution

Principles:

1. **Bipartisan which means benefit cuts and tax increases.**
2. **Solvency (increase revenues and lower benefits by 4.42 % of taxable payrolls. Eliminate the "GAP")**
3. **No benefit reduction for current recipients (?)**
4. **No general fund financing (Pay benefits from SS taxes)**
5. **Improve Progressivity.**
6. **Increase risk protection. (improve benefits for dependents)**
7. **Universal participation**

How do these principles reflect the goals of Social Security?

https://www.brookings.edu/articles/fixing-social-security-blueprint-for-a-bipartisan-solution/

My Interpretation of Brookings Principles

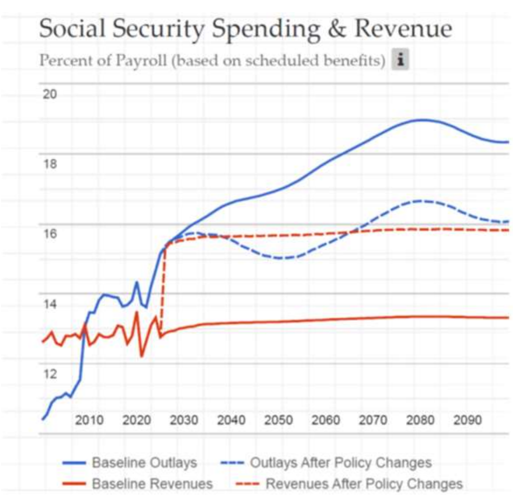
- **While the goal of preventing poverty among the elderly is important, so too are the other two goals**
  - "this link between wages and benefits has been a central principle… and a foundation of it political support."
  - Universal participation because of **social** insurance.
  - Increased risk protection.
- **Bipartisan: I would go further: Don't try to fix the inequities of the federal tax system with social security reform**
  - Preserve the traditional view that Social Security is a different type of government program.
  - SS reform is tough enough and the problem is urgent.

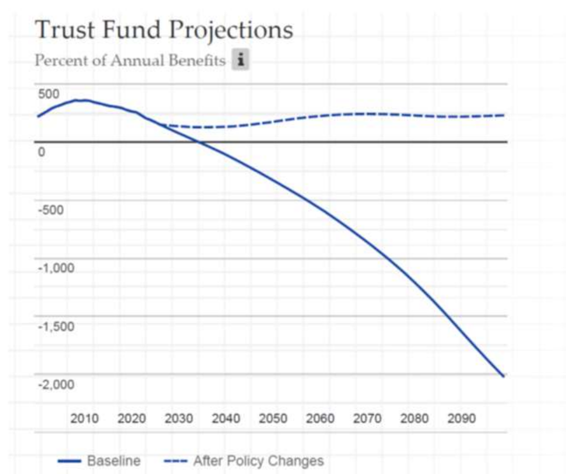
Example: Roughly Based on Brookings

1. Slow Benefit Growth for High Earners (41%, of gap removed)
2. Index COLA to "Chained" CPI (17%)
3. Phase out nonworking spouse benefit (5%)
4. Expand Widow(er)s Benefit to 75% of combined benefit (-3%)
5. Eliminate earnings cap *both* for payroll taxes and benefits (50%)

Bipartisan because it involves benefit reductions (60%) and tax increases (50%)

Results

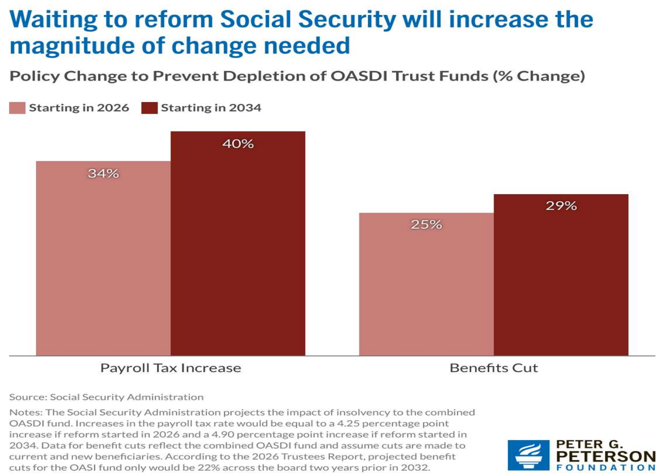




https://www.crfb.org/socialsecurityreformer/

The Sooner We Act the Better

We cannot afford to let the “best” be the enemy of the “good.”



Should Current Retirees Share the Burden?

- **Current retirees have less flexibility to adjust income and spending.**
- **That may argue for a smaller relative burden, but not zero.**
- **Also, higher income retirees have more flexibility in adjusting spending.**
- **My opinion, for intergenerational fairness and for social solidarity, the more affluent of our generation should bear some burden**

Summary

- **Social Security is an important part of the social safety net.**
- **The OASI Trust Fund is likely to be exhausted in 2032.**
- **Why are the funds being depleted?**
  - An aging population and slower growth in the labor force.
- **What happens when the funds are depleted?**
  - Benefits may have to be reduced by 22%, but the system will continue
- **Solutions abound. The problem is political will.**
  - The needed changes will be unpopular, but they are manageable. The longer we wait the bigger the problem.
- **There is hope: both the Senate and House are considering different bills to form a commission to make proposals.**

Let's Hear from You!

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Slides available

https://www.needecon.org/delivered_presentations.php

Additional Material

https://sites.google.com/view/macro-current-issues/social-security