The Future of Social Security

The 57 million Americans currently receiving some type of Social Security benefit got a raise this year, for only the second time since 2009.

Prior to 1975, Social Security benefit increases were set by congressional legislation. But beginning in 1975, federal law requires the Social Security program to base annual benefit increases on the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). Consumer prices are compared in the third quarter of each year (July, August, and September) with the same months in the previous year. If prices decrease from one year to the next, payments don't go down, they just remain the same. But if prices increase, Social Security recipients automatically receive a higher benefit payment beginning the following January. This is known as a cost-of-living adjustment, or COLA.

A COLA was issued every year from 1975 until 2009, when Social Security payments increased by 5.8 percent, the largest increase in 27 years. As announced by the Social Security Administration on October 16, 2012, the COLA for 2013 is 1.7 percent. This is only about half of last year's COLA of 3.6 percent. There was no COLA for 2010 or 2011.

But that's not the only change that occurred to the Social Security program in 2013.

The temporary two-year reduction from 6.2 to 4.2 percent in the employee share of Social Security taxes expired on December 31, 2012. The amount of one's earnings subject to Social Security tax (the payroll tax cap) increased from $110,000 to $113,700. The maximum monthly Social Security benefit for a worker retiring at his full retirement age increased from $2,513 to $2,533. The amount one must make in a quarter to earn one credit of coverage in the Social Security system increased from $1,130 to $1,160 (a worker generally needs 40 credits [10 years] to be eligible for benefits). The limit on what those who receive early retirement benefits can earn without penalty if they continue to work increased from $14,640 to $15,120 ($1 in benefits is withheld for every $2 in earnings above the limit).

It should also be noted that the Social Security full retirement age has been gradually increasing at the rate of two months per year. The original retirement age was 65. It is currently 66, with reduced early-retirement benefits payable at age 62. But for those born in 1960 or later, it will be 67 by the time they are eligible for benefits.

But all is not well with the Social Security system.

Financial Trouble

The six-member Board of Trustees of Social Security recently released its 73rd annual report on the state of Social Security: "The 2013 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds." The board consists of the secretaries of Labor, Health and Human Services, and the Treasury; the commissioner of Social Security; and two public trustees appointed by the president and confirmed by the Senate. The Social Security Act of 1935 requires that the board report annually to Congress on the actuarial status and financial operations of Social Security's two trust funds.

The Old-Age and Survivors Insurance (OASI) program provides monthly benefits to retired workers, families of retired workers, and survivors of deceased workers. The Disability Insurance (DI) program provides monthly benefits to disabled workers and families of disabled workers. According to the trustees' report, at the end of 2012, the combined OASDI program was providing benefits to about 57 million people: 40 million retired workers and their dependents, six million survivors of deceased workers, and 11 million disabled workers and their dependents. It is estimated that 161 million people in 2012 had earnings covered by Social Security.

The Social Security System is funded by employee payroll-tax deductions that are matched by employers. When the taxes first began to be collected back in 1937, the original rate was two percent (split between employees and employers) on the first $3,000 of taxable income. According to a 1936 government pamphlet on Social Security, the rate was never supposed to rise above six percent, and the "contribution and benefit base" was not supposed to increase at all. Yet, like all government promises, this has not been the case. By 1960, the rate had risen to six percent; by 1970, it was over eight percent; by 1980, it exceeded 10 percent; and in 1990, it increased to the current 12.4 percent. The payroll tax cap steadily increased to $9,000 by 1972, and has risen every year (except 2010 & 2011) since then. It currently stands at $113,700. To be eligible for Social Security benefits, one must pay Social Security taxes for a minimum of 40 quarters, or 10 years. Benefits are determined based on one's Primary Insurance Amount (PIA), the average of a worker's 35 highest years of earnings (up to each year's wage base), adjusted for inflation.

The system seems like it will work just fine as long as there are many more people paying taxes than receiving benefits. Officially, taxes collected in excess of benefits paid are put into the OASI and DI trust funds and then invested in special interest-bearing, non-marketable U.S. government securities. Benefit payments and administrative costs are the only disbursements permitted from the trust funds. But this has not stopped the trust funds from being plundered for other government programs, since the "securities" filling the funds amount to IOUs.

There is, however, another problem that is even greater: Taxes collected are no longer in excess of benefits paid. According to the official summary of the trustees' report:

> Social Security's total expenditures have exceeded non-interest income of its combined trust funds since 2010, and the Trustees estimate that Social Security cost will exceed non-interest income throughout the 75-year projection period. The deficit of non-interest income relative to cost was about $49 billion in 2010, $45 billion in 2011, and $55 billion in 2012. The Trustees project that this cash-flow deficit will average about $75 billion between 2013 and 2018 before rising steeply as income growth slows to the sustainable trend rate after the economic recovery is complete and the number of beneficiaries continues to grow at a substantially faster rate than the number of covered workers. Redemption of trust fund asset reserves by the General Fund of the Treasury will provide

> the resources needed to offset Social Security's annual aggregate cash-flow deficits. Since the cash-flow deficit will be less than interest earnings through 2020, reserves of the combined trust funds measured in current dollars will continue to grow, but not by enough to prevent the ratio of reserves to one year's projected cost (the combined trust fund ratio) from declining. (This ratio peaked in 2008, declined through 2012, and is expected to decline steadily in future years.) After 2020, Treasury will redeem trust fund asset reserves to the extent that program cost exceeds tax revenue and interest earnings until depletion of total trust fund reserves in 2033, the same year projected in last year's Trustees Report. Thereafter, tax income would be sufficient to pay about three-quarters of scheduled benefits through 2087.

All this simply means that the Social Security system in its current form is insolvent. The trustees' report calculates the present value of the system's unfunded obligation over a period extending indefinitely into the future as $23.1 trillion. But the current Social Security shortfall is actually worse than it appears.

Total Social Security expenditures in 2012 were $785.8 billion — the largest expenditure of the federal government. Net payroll tax "contributions" were $589.5 billion. This makes a deficit of $196.3 billion. Yet, the Social Security Administration reports that for 2012 its income was $840.2 billion. This figure includes not only payroll taxes collected, but also $109.1 billion in interest income, $27.3 billion from the partial taxation of some Americans' Social Security benefits, and a $114.3 billion "reimbursement from General Fund of the Treasury." This was "to 'replicate to the extent possible' revenues that would have occurred in the absence of the payroll tax reduction." But only the $27.3 billion is real money. Not only is there no actual trust fund; there is no interest income or reimbursement from the government's general fund either. All three are just figments of creative accounting practices. The whole system is one gigantic fraud. Payroll taxes collected are deposited in the government's general fund and immediately spent on current Social Security benefits, foreign aid, research grants, corporate welfare, the DEA, NSA, TSA, EPA, and countless other black holes the government pours billions of dollars into every day. No American has a retirement or investment account in Washington, D.C., with his name on it, earning interest, just waiting until he reaches retirement age and signs up for Social Security.

Among other things, the problem with Social Security is simply one of numbers. At the end of December of 2011, 55,404,480 Americans (retirees, widows, the disabled, and children) were receiving Social Security benefits of some kind. At the end of 2012, that number had risen to 56,758,185. And as of June 30, 2013, 57,469,232 Americans are now receiving benefits. The nation's first official baby boomer, born just after midnight on January 1, 1946, filed for Social Security at a public event on October 15, 2007. According to the then-commissioner of Social Security, "Over the next two decades, nearly 80 million Americans will become eligible for Social Security benefits, more than 10,000 per day."

The Social Security program is clearly unsound, unstable, unsustainable, and untenable. Yet, it has overwhelming bipartisan support in Congress. Even Republicans who talk the most and the loudest about adherence to the Constitution, limited government, and fiscal conservatism are passionate supporters of Social Security. What, then, is the future of Social Security?

Saving the System

A myriad of proposals have been put forth over the years to reform, strengthen, modernize, preserve, or "save" the Social Security System.

The American Association of Retired Persons (AARP) lists 12 such proposals in "The Future of Social

Security: 12 Proposals You Should Know About":

- Raise the Full Retirement Age
- Begin Longevity Indexing
- Recalculate the COLA
- Increase the Payroll Tax Cap
- Eliminate the Payroll Tax Cap
- Reduce Benefits for Higher Earners
- Increase the Payroll Tax Rate
- Tax All Salary Reduction Plans
- Cover All Newly Hired State and Local Government Workers
- Benefit Improvements
- Increase Number of Years Used to Calculate Initial Benefits
- Begin Means-Testing Social Security Benefits

Most of these are fairly straightforward. Longevity indexing refers to periodically adjusting the retirement age, whether raised or not, to account for the fact that people are living longer. Recalculating the COLA using the "chained consumer price index" would reduce the size of yearly benefit adjustments; using the "elderly index" would cause the benefit adjustments to increase in size. Taxing salary reduction plans (plans that allow employees to contribute pre-tax income to a tax-deferred retirement plan) and covering newly hired state and local government workers would broaden the Social Security tax base. Benefit improvements would increase benefits for surviving spouses, those who dropped out of the workforce to care for a family member, and chronically low-paid workers. (These "benefit improvements" would actually increase payments, not help to "save" Social Security.) Increasing the number of years used to calculate initial benefits, because it would include more years of lower earnings, would decrease average earnings and therefore lower benefits.

The report of the Social Security trustees recommends that "for the combined OASI and DI Trust Funds to remain solvent throughout the 75-year projection period":

> (1) revenues would have to increase by an amount equivalent to an immediate and permanent payroll tax rate increase of 2.66 percentage points (from its current level of 12.40 percent to 15.06 percent);

(2) scheduled benefits during the period would have to be reduced by an amount equivalent to an immediate and permanent reduction of 16.5 percent applied to all current and future beneficiaries, or 19.8 percent if the reductions were applied only to those who become initially eligible for benefits in 2013 or later; or

(3) some combination of these approaches would have to be adopted.

Conservative think tanks such as the Heritage Foundation have likewise recommended reforms to the Social Security system. In *Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity*, Heritage proposes redesigning Social Security from a "defined-benefit" program to "real insurance" that focuses on those in need and phases out by income for those who are not. Under the Heritage plan, there would be "a gradual transition to a flat benefit that pays retirees who qualify for a full Social Security check." The normal and early retirement ages would be gradually raised as well, and indexed to longevity. Meanwhile, right now, benefits would be means-tested.

Libertarian think tanks such as the Cato Institute have also come up with reform plans. Under Cato's *The 6.2 Percent Solution: A Plan for Reforming Social Security*:

> • Individuals would be allowed to divert their half (6.2 percentage points) of the payroll tax to individually owned, privately invested accounts. Those who chose to do so would agree to forgo all future accrual of retirement benefits under the traditional Social Security system.

• The remaining 6.2 percentage points of payroll taxes would be used to pay transition costs and to fund disability and survivors' benefits.

• Workers who chose the individual account option would receive a "recognition bond" based on the accrued value of their lifetime-to-date benefits. Those bonds, redeemable at the worker's retirement, would be fully tradable in secondary markets.

• Those who wished to remain in the traditional Social Security system would be free to do so, accepting a level of benefits payable with the current level of revenue.

Both conservatives and libertarians have called for the whole Social Security system to be privatized. President Bush even said after leaving office that the biggest failure of his administration was that he was not able to privatize Social Security.

Two Fundamental Flaws

There are two common denominators in all of these reform proposals. Although there are some differences in opinion regarding how the Social Security program should determine benefits, be funded, and operate, all are agreed: (1) That it is the proper role of government to have a Social Security system; and (2) That the Social Security system should be reformed, improved, strengthened, or saved. The legitimacy and constitutionality of Social Security is never even questioned.

The first fundamental flaw of Social Security is that it is an unconstitutional and illegitimate function of government. Now, even from this perspective, one could argue that any reform proposal that results in fewer people receiving benefits or less total benefits paid is a *good thing*; therefore, raising or indexing the retirement age; allowing people to opt out; recalculating, freezing, or eliminating COLAs; or reducing, recalculating, or means-testing benefits *should* be undertaken. One could also argue that any reform proposal that results in a higher tax rate, more people paying taxes, more overall taxes collected, or more benefits paid is a *bad thing*; therefore increasing the tax rate, broadening the tax base, increasing or eliminating the payroll tax cap, or making benefit "improvements" *should not* be undertaken. But because the fundamental problems with Social Security have nothing to do with the program being financially unstable, inefficient, and unsustainable, all attempts to reform and perpetuate the system are illegitimate.

It is simply not the job of government to institute or operate a retirement plan, an insurance program, a saving account, an investment account, or a pension plan. It is just not the job of government to pay anyone retirement, disability, survivors, or spousal benefits. And neither is it the job of government to have a trust fund, maintain a safety net, keep people out of poverty, help those who cannot help themselves, take care of the aged and disabled, or assist those who have failed to plan for their retirement. Even if Social Security were solvent, efficient, voluntarily funded, and optional, the federal government still has no authority to operate a retirement and disability plan for anyone except government employees. And any plan funded by mandatory contributions with mandatory participation can hardly be called "privatized."

The second fundamental flaw of Social Security is that it is *not* a real retirement plan, an insurance program, a saving account, an investment account, or a pension plan. In its essence, Social Security is an intergenerational, income-transfer, social-engineering, wealth-redistribution program. Social Security has operated the same way from the very beginning. Government takes money from the working population, calls it a Social Security contribution, and then immediately spends the money on an assortment of boondoggles and other unconstitutional programs. Then, when that population reaches retirement age, it takes more money from the current group of workers and gives it to the former group in the form of Social Security benefits. Social Security is, and will always be, a system where money is taken from those who work and given to those who don't. It is based on lies, funded by theft, maintained by force, and dependent on worthless government promises.

A common objection is that paying Social Security taxes entitles one to receive benefits. Nothing could be further from the truth. There is no connection between Social Security taxes paid and benefits received. Social Security benefits are paid out of the U.S. Treasury, not some mythical trust fund. There is no contractual right to receive benefits, as the Supreme Court ruled in 1937 and 1960. Congress may, at will, increase payroll taxes, decrease benefits, means-test benefits, reduce or eliminate COLAs, or increase eligibility requirements. Those who die before signing up for Social Security forfeit every penny they "contributed" to the system.

The Social Security trustees recommend that "lawmakers address the projected trust fund shortfalls in a timely way in order to phase in necessary changes and give workers and beneficiaries time to adjust to them." They believe that "with informed discussion, creative thinking, and timely legislative action, Social Security can continue to protect future generations."

The future of Social Security in a nanny-state, repressive, and collectivist society is higher taxes, a broader tax base, and more people dependent on the government. The future of Social Security in a free, compassionate, and voluntary society is its elimination as efficiently, humanely, and completely as possible. The question really concerns what type of society Americans want to live in. Because Social Security is first and foremost a political question, it is Americans' attitude toward entitlements that must first be changed.

Laurence M. Vance is the author of Social Insecurity.

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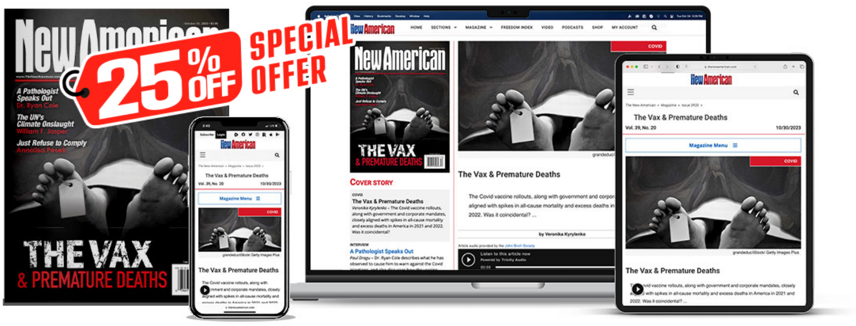

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