

Economy:

Protecting Social Security

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Top Line

1. **Social Security is a vital program for reducing poverty, protecting seniors and disabled people, and strengthening our economy.**
2. **Without action by Congress, Social Security will have to cut benefits within less than 7 years.**
3. **Privatization (replacing the current system with individual investment accounts managed by individuals) is not an effective solution.**
4. **Protecting Social Security and ensuring its long-term financial viability will require responsible action from Congress – increasing revenues and decreasing long-term obligations. The sooner Congress acts, the less painful these actions will be.**

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Backup

1. **Social Security is a vital program for reducing poverty, protecting seniors and disabled people, and strengthening our economy.**
 - a. **Background – where Social Security came from**
 - Social Security in the United States grew out of the economic and political crisis of the Great Depression and was formalized in the Social Security Act signed by President Franklin D. Roosevelt on August 14, 1935. (1)

- The Great Depression produced mass unemployment and widespread destitution among older Americans, exposing the limits of local poor relief and private charity. (2) By the early 1930s, more than half of older Americans were living in poverty. (3)
- Fearing both social unrest and more radical, costlier pension schemes, the Roosevelt administration crafted Social Security as contributory social insurance, financed by payroll taxes so that benefits would be **an earned right instead of welfare.** (4)
- Unlike many European systems, U.S. Social Security was set up as an “insurance” program funded by compulsory contributions: taxes on workers’ wages and on employers’ payrolls, rather than direct general-revenue support. (5)
- The act also financed assistance to children, blind people, and unemployed workers, as well as vocational training and family health programs. (5)

b. How Social Security works

- Social Security is a federal social insurance program where current workers and employers pay payroll taxes that are used to provide monthly income to qualifying people who are retired, disabled, or survivors of deceased workers. (6)
- When you work, 6.2% of each paycheck (up to the cap, which is currently \$184,500), matched by your employer, or fully paid by you if you’re self-employed (12.4%), is sent to the Social Security Administration. (6)
- As you work in Social Security-covered employment, you earn “credits” based on your earnings; most people need 40 credits (about 10 years of work) to qualify for retirement benefits, while younger workers can qualify for disability or survivors benefits with fewer credits. (7)
- Your benefit amount is based on your lifetime earnings and the age at which you start benefits: claiming before your full retirement age permanently reduces your monthly amount, claiming at full retirement age gives your full benefit, and delaying up to age 70 increases it. (7)
- **Social Security is a “pay-as-you-go” system: taxes paid today fund today’s beneficiaries, while your future benefits will be funded by the taxes of future workers, with trust funds used to smooth gaps between incoming taxes and outgoing benefits.** (8)

c. **Social Security plays a major role in reducing poverty, protecting seniors and disabled people, and stabilizing the economy.**

- It keeps tens of millions of people, especially older adults and people with disabilities, out of poverty by replacing part of their earnings when they retire, become disabled, or die, leaving dependents. **Without Social Security benefits, 66% of elderly Americans would have incomes below the poverty level. With Social Security included the poverty rate for seniors is only 16%.** (9)
- Because the benefit formula replaces a higher share of earnings for lower-wage workers, **it reduces both income and wealth inequality** compared with a system that relied only on private savings. (10)
- Monthly benefits also arrive steadily, even in recessions, so beneficiaries keep spending on rent, food, and local services, which **softens economic downturns and supports jobs** in American communities. (11)
- Today, Social Security **pays benefits to over 71 million Americans** who have paid into this retirement system, approximately 20% of the total population. (12)

2. **Without action by Congress, Social Security will have to cut benefits within less than 7 years.**

- a. Benefits are growing faster than revenues, and the trustees project that by 2032 the program will lack enough resources to pay full scheduled retirement benefits, triggering roughly a **23 percent across-the-board cut** without congressional action. (13)
- b. Factors affecting this financial imbalance include: (13)
- **An aging population and longer lifespans** are increasing the number of beneficiaries relative to people paying in.
 - **Wage inequality has eroded the tax base:** a growing share of total earnings is above the taxable wage cap, so only about 83 percent of earnings are now subject to payroll tax, down from 90 percent in 1983.
 - **Inflation:** Annual cost of living adjustments increase benefits when prices rise. The faster inflation we are now experiencing makes program finances even worse. (14)
 - **Wage stagnation:** Slow or flat wage growth holds down payroll tax revenues, widening Social Security's long-term funding gap as benefit obligations keep rising. (14)

- c. Social Security's core financing problem is that, as the population ages, annual benefit costs will exceed what comes in each year from payroll taxes and interest, **forcing the trust funds to gradually draw down their reserves.**
- If policymakers do nothing, those reserves will eventually be depleted; at that point, incoming payroll taxes would still cover most promised benefits, but not 100 percent, so benefits would be automatically cut across the board to match available revenue.
 - It is a shortfall, not "bankruptcy": Social Security would continue operating, but with reduced payments. (15)
- d. Current projections from the Social Security Trustees and related analyses show that, absent legislative action, the Social Security trust funds will be depleted by 2032, at which point incoming payroll taxes and other dedicated revenues would still cover roughly 78 percent of scheduled benefits, implying an **automatic across-the-board cut of about 22 percent if Congress does not act quickly.** (13, 16)

3. Privatization (replacing the current system with individual investment accounts managed by individuals) is not an effective solution.

- a. **Privatization** generally means Americans stop paying today's payroll taxes and instead divert some of their income into individual investment accounts, reducing the traditional defined benefit and tying more of retirement income to market returns. Because Social Security is pay-as-you-go, any diversion of payroll taxes creates a big transition hole: the program would still owe full benefits to current retirees, but less money would be coming into the trust funds. (17)
- b. Analyses show that diverting even a small share of payroll tax revenue into private accounts would require trillions in new borrowing or immediate benefit cuts to keep paying current retirees. (18)
- c. Privatization replaces part of a guaranteed, inflation-indexed benefit with market-based returns that can fall sharply right before or during retirement, exposing people to stock market risk they cannot control. International experience (for example, Chile and Sweden's strong move toward individual accounts) shows

that **privatized systems often end up with higher costs, lower benefits, or both, unless the government steps in with large subsidies.** (19)

- d. Of course, individuals can (and should) save on their own for retirement. **But the strength of Social Security is that it removes market risk from a core component of retiree's long-term income.**

4. Protecting Social Security and ensuring its long-term financial viability will require responsible action from Congress.

a. Voters strongly support Social Security but have low confidence in its long-term viability. (20)

- 96% of adults across age groups agree that Social Security is an important program.
- 67% of retirees say they substantially rely on their benefits and another 21% say they somewhat rely on it.
- However, confidence in the program continues to decline year over year with **only 36% of Americans having confidence in the future of the program.**

b. Congressional gridlock and partisan divides make it much harder to fix Social Security's looming financing shortfall, even though there is broad agreement that the program should not be allowed to fail.

- Democrats generally favor closing the gap by raising revenues, especially by increasing taxes on higher earners or lifting the taxable wage cap.
- Republicans generally oppose tax hikes and instead emphasize cutting benefits, raising the retirement age, or restructuring the program. (21)
- Because every major plan to protect Social Security requires politically painful choices (tax increases, benefit cuts, or both), party leaders often prefer to delay action, which deepens the funding gap and leaves fewer gradual, low-disruption options available. (22)
- The result is stalemate: each side can block the other's preferred solutions, but neither side has yet built a durable bipartisan compromise, increasing the risk that Congress will wait until the trust funds are nearly depleted and then be forced into rushed, more abrupt and expensive changes. (23)
- Congress has known for decades that reforms are necessary and has chosen to push the problem onto future generations.

- c. **Education and awareness campaigns** can build broad, durable support for smart Social Security reform by closing the knowledge gap and turning unfocused concern into focused political pressure. Voters need to understand how Social Security actually works and why it faces a shortfall, and that action is long overdue to fully fund it. (24)
- d. The Social Security Trustees, in their annual analysis, estimate the year that Social Security will no longer be able to pay full benefits (2032), and urge Congress to act quickly to address this, but do not make specific policy recommendations. Instead, they outline three options: **“Congress must take prompt action to strengthen the actuarial status of the OASI (Old Age and Survivors’ Insurance) Trust Fund. Lawmakers could choose to increase revenues to the trust fund, reduce cost through modification of the OASI program benefit levels or eligibility requirements, or use a combination of methods to strengthen the trust fund’s financial condition.”** (29)
- e. Several organizations have mapped out potential solutions to the Social Security funding shortfall and estimated their effects. These plans generally include **both long-term benefits reductions and increases in revenues.**

Some of the specific actions to protect Social Security include:

- i. **Raise or eliminate the payroll tax cap.** Raising or removing the wage cap so that high earners pay Social Security payroll tax on more of their earnings would significantly strengthen the program’s finances, because the taxable maximum has not kept pace with rising earnings at the top, and proposals like the Brookings blueprint would gradually increase the cap until it again covers about 90% of all wages as it did before 1983. (25)
- ii. **Increase the payroll tax rate.** Slightly increasing the payroll tax rate over time to phase in roughly a 1-percentage-point increase split between workers and employers—spreads the adjustment broadly and predictably. The Congressional Budget Office analysis shows that a small, gradual rate hike can close a substantial share of the long-term shortfall without abrupt shocks for any single age group. (26)

- iii. **Adjust eligibility age and benefit formulas.** Currently, for workers born after 1959, the Full Retirement Age (FRA) is 67. Workers can claim benefits as early as age 62, but if they start taking benefits earlier than age 67 the amount will be lower. The Congressional Budget Office has proposed raising the FRA from 67 by two months per birth year for workers born between 1964 and 1981. So, for example, for workers born in 1969 the FRA would be 68, and for workers born in 1981 or later the FRA would be 70. Workers would still be able to start benefits at age 62, but they would be lower than they are now, and full benefits would not be received until the worker reached their FRA. (27)

- iv. **Strengthen the trust fund through investment diversification.** Allowing a portion of reserves to be invested in assets beyond U.S. Treasury bonds, such as broad-index equities or high-quality public securities would capture higher expected long-run returns and build larger reserves that can reduce the need for future tax increases or benefit cuts. This would require managing the trade-off that these assets are riskier and more volatile than Treasuries and require strong safeguards to insulate investment decisions from political interference. (28)

Without quick action, the Social Security funding challenge only grows larger. Solutions will require compromise from both parties. But failure to act only sends a larger problem to future workers and retirees.

More Information

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