Despite Slight Improvement, We Need to Fix Social Security Now

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Acting soon allows baby boomers to share the burden and reduces the size of the changes.

The **2015 report** from the Social Security Trustees shows a slight improvement in the system's finances from last year. The deficit over the next 75 years declined from 2.88 percent of taxable payrolls in 2014 to 2.68 percent in 2015. The date when the trust fund assets are exhausted for the system as a whole moved from 2033 to 2034. The assets in the Disability Insurance trust fund are still projected to run out next year.

The new 75-year deficit means that if payroll taxes were raised immediately by 2.68 percentage points – 1.34 percentage points each for the employee and the employer – the government would be able to pay the current package of benefits for everyone who reaches retirement age at least through 2089. Alternatively, benefits would have to be cut by about 16 percent – or by about 20 percent if the reductions were limited only to new beneficiaries.

If Congress does nothing* until the trust funds are depleted in 2034, the payroll tax would have to be increased by 3.7 percentage points at that point, with the increase rising to 5.0 percentage points by 2089. Alternatively, benefits would have to be cut to match scheduled taxes, which would require a 21-percent cut in 2033 rising to 27 percent in 2089. So restoring balance early requires much smaller tax or benefit changes.

*In fact, Congress must do something in 2016. Although the outlook for Social Security is usually reported on a consolidated basis, the program consists of two trust funds – one for Old-Age and Survivors Insurance (OASI) and one for Disability Insurance (DI). Under the intermediate projections, the DI trust fund will be exhausted in 2016. Since Social Security is precluded from spending money it does not have, it would have to cut benefits by about 20 percent to accord with DI payroll tax revenues. Congress is unlikely to allow such a circumstance to arise. In 1994, the last time the program was about to run out of money, Congress reallocated 0.6 percentage points of the payroll tax from the OASI program to the DI program. It will probably do the same thing this time. Such a change has no impact on the finances of the program as a whole.

Acting sooner also is fairer to young workers, who are already scheduled to contribute more than they will get back in benefits. If the change were made this year, the second half of the baby boom (who are mainly in their 50s today) would contribute to solving the problem; if we wait, the entire baby boom gets to escape entirely from helping to solve a problem that has been evident during their entire working life.

How should we eliminate the deficit? Policymakers have spent decades putting together alternative packages of tax increases and benefit cuts. All the options are known. But in this current environment, the likelihood of agreeing on a complicated combination of cuts and tax increases seems unlikely. So let's just go ahead and raise the tax rate by 1 percentage point each on employees and employers and raise the taxable earnings base to about $230,000 so that it covers about 90 percent of earnings. That should do the trick for the next 75 years.

Is it sensible policy to raise taxes and forget about benefit cuts? I would say "yes." We live in a world where 401(k)/IRA balances for the typical household with a 401(k) approaching retirement are only $111,000, so people are going to need every penny they can get from Social Security.

If employer plans start to provide meaningful retirement income, we can make cuts in Social Security benefits down the road. Solvency will remain an issue because any package of reforms that restores balance only for the next 75 years will show a deficit in the following year, as the 75-year projection period moves forward and picks up a year with a large negative balance. Therefore, any change we make in the next year or so should realistically be seen as a down-payment on a permanent solution. So let's get on with it.