The Daily Dish

The Future of Social Security

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Eakinomics: The Future of Social Security

Social Security is a critical component of the safety net. It provides inflation-adjusted retirement income for as long as a beneficiary survives (a real annuity), provides a greater replacement rate of lifetime wages for low-wage workers than high-wage workers (i.e., is progressive in the distributional sense of that word), and has proven to be a stellar anti-poverty program for the elderly. Its importance is reflected by its special budgetary treatment — the federal government pretends that payroll taxes (currently 12.4 percent of wages) are deposited into a retirement trust fund and pretends that retirement benefits are paid out of the trust fund. In reality, cash simply flows into and out of the Treasury, but the trust fund fiction dictates that benefits can only be paid as promised if there is enough combined money from payroll taxes and the trust fund.

By 2033 this will no longer be the case. The trust fund will be empty and benefits will be dictated by the funds available from payroll taxes – requiring a decline of nearly 25 percent. Will Congress change Social Security to avert this decline in retirement income? Who knows. This uncertainty means that Social Security has morphed from a program designed to reduce income uncertainty into a source of that uncertainty.

Elizabeth Warren has proposed recently to reform Social Security. She begins, however, by immediately making the financial problem worse:

- “Increases Social Security benefits immediately by $200 a month – $2,400 a year – for every current and future Social Security beneficiary in America.
- Updates outdated rules to further increase benefits for lower-income families, women, people with disabilities, public-sector workers, and people of color.”

Now, it is not crazy to contemplate some benefits increases, yet they are typically not across-the-board but focused on the minimum benefit and support for the most aged. But having done so, how do you solve the imbalance between promises and cash to make good on them? One approach would be to acknowledge that the most affluent have no need for regular Social Security benefits, or even Social Security benefits at all. This would mean cutting back on benefits to the affluent to bring the program into balance. But for some reason the left thinks it is “fairer” to raise $1 of taxes on the affluent (which would have damage to economic incentives on top of lowering the deficit by $1) than to cut $1 of benefits (which would improve economic incentives in addition to lowering the deficit by $1).

So, naturally, Warren proposes, “First, my plan imposes a 14.8% Social Security contribution requirement on individual wages above $250,000 – affecting less than the top 2% of earners – split equally between employees and employers at 7.4% each. Second, my plan establishes a new 14.8% Social Security contribution requirement on net investment income that applies only to the top 2% – individuals making more than $250,000 in annual income or families making more than $400,000 in annual income.”

In the end, this is simply old-school, tax-and-spend fiscal policy dressed up as Social Security reform. And in other cases, it doesn't even do much for Social Security. On Friday the Congressional Budget Office (CBO) released its analysis of the Social Security 2100 Act (H.R. 860). The bill would "increase Social Security benefits for most recipients, change the measure used to determine cost-of-living adjustments (COLAs), increase the minimum benefit for some new recipients with low lifetime earnings, and include earnings above $400,000 in the benefit formula. The bill also would increase revenues by gradually raising the payroll tax rate and subjecting earnings above $400,000 to the payroll tax." So, it is the same basic game plan of raising spending and high-income taxes.

What's the hitch? The Social Security 2100 Act extends the life of the trust fund only until 2041. A trillion dollars of taxes buys only 8 years; it does not eliminate the uncertainty facing seniors and near-retirees. Real reform is not over-promising (again) to retirees and damaging the economy with ever-higher taxes. Real reform is putting Social Security on a sustainable financial path, taking care of vulnerable seniors, and doing so in an economically and fiscally responsible fashion.