SOCIAL SECURITY: NOTHING TO FEAR BUT FEAR ITSELF

Hedayeh Samavati, Indiana - Purdue University - Fort Wayne
Carolyn Fabian Stumph, Indiana - Purdue University - Fort Wayne
David A. Dilts, Indiana - Purdue University - Fort Wayne

INTRODUCTION

In 1933 a national debate was begun concerning the plight of widows, orphans, the disabled, and the elderly. It is particularly important that we remember why this national debate began. The driver of that national debate was poverty, and all the societal ills associated with deprivation. President Franklin D. Roosevelt, speaking to the issue of the deprivation of the Great Depression, warned the American public that we had “nothing to fear, but fear itself.” Precious few of us alive today remember those “fireside chats” and the economic woes of the period that made those radio broadcasts such important landmarks in the political terrain of the day.

Tom Brokaw’s book memorializing the views and experiences of those whose lives were indelibly etched by the Great Depression only gives a glimpse of what that generation endured. The Greatest Generation lived through the trials of economic collapse, and was then asked to sacrifice its youth on the altar of the Second World War. Rather than to embitter the Greatest Generation they seemed to emerge from the Second World War with a commitment that their children would not suffer as they had. They willingly shouldered the burden of the so-called “entitlement programs,” the education of their children, and President Johnson’s “War on Poverty.” They did all of this during a period that was marked by international tensions between competing ideologies that produced an unprecedented “Cold War” and the domestic tensions of the emergence of domestic social change providing more equal opportunities for all Americans. The so-called Greatest Generation provided much of the opportunity the “baby boomers” enjoyed. The increased educational opportunities, establishment and protection of civil rights, and the so-called “entitlements” provided for a certain level of security for the members of American society heretofore never experienced.

In the 1930s there were those who did not believe that the economy was broken and that the total welfare of society could not be increased by solutions which strayed from reliance on free and unfettered markets. The economists of the day, Irving Fisher, primary among them, argued that the economy was self-correcting, and that the trade-off for economic freedom, was perhaps less economic security. However, one can argue that this trade-off is fine as long as one is not among those who are disabled, widowed, orphaned, or elderly. No dosage of free market is going to supply economic security for those with little, if anything, to offer in the marketplace. Yet, it is precisely those individuals for whom Roosevelt led the charge to provide for a more secure future through social responsibility.

The debate of the 1930s was focused on the provision of economic security for those who were unable to provide for themselves, and to assure those who reached retirement age that they would not be forced to live in poverty because they had inadequate resources for their retirement. Today, there has been a sudden turn away from these principles by which generations have lived. The once agreed-upon principle of providing a modicum of security across society seems again to be subject to a renewed debate based on previously-settled contentions. As we move away from the historic events that produced fundamental changes in the American way of life, we too often lose our institutional memory and forget what it was that caused these changes. The issue was framed in a particular and correct way in the 1930s, and is now being subjected to revision that is left wanting in the
face of the historic record, and economic evidence.

The purpose of this essay is to examine the contentions and assumptions that are being proffered in the current attempt to undo the “New Deal” legislation of the 1930s. In particular, the intent of the paper is to examine the data to ascertain whether future generations of Americans are facing a genuine Social Security crisis or if the so-called Social Security crisis is merely a “phony crisis” as is alleged by some scholars such as Baker and Weisbrot (1999).

Reform of the Social Security System was pronounced to be the centerpiece of President Bush’s second-term domestic policy agenda. Were Americans right when they firmly rejected President Bush’s plans or initiatives to “reform” the Social Security system? Did we miss a golden opportunity to fix a looming crisis in the future? The paper seeks to examine the information to provide some answers to these questions.

BACKGROUND AND FACTS ABOUT SOCIAL SECURITY

The Social Security or the Old-Age, Survivors, and Disability Insurance (OASDI) program was signed into law in August of 1935. Social Security is an earned benefit program because only those who work and pay taxes for a certain period of time become eligible to receive benefits. It provides:

- Retirement benefits to workers, their spouses, and their dependents such as children and elderly parents. Workers can receive early retirement benefits if they reach the earliest age that retirement benefits can be paid (currently 62) and they must have worked at least 10 years. Benefits, however, will be reduced by 20% relative to what the retiree would have received at the normal retirement age of 65. In 2002, 29.2 million retirees and 3.2 million spouses and children of retirees received benefits.

- Survivorship benefits to family members of a deceased worker. To receive these benefits a worker must have worked, on average, at least one quarter for each year since he/she turned 21. In 2002, 6.9 million received survivors benefit.

- Disability benefits to workers who become disabled (physical or mental impairment) before their retirement. In 2002, disabled workers who received disability benefits numbered in 5.5 million and another 1.7 million were the spouses and children of disabled workers who received benefits.

The total number of beneficiaries has grown from 1.3 million in 1945 to 47 million (one in every 6 Americans) at the end of 2003. The average amount of benefits are tied to the worker's earning history. Because women tend to have lower life time earnings, they receive a lower average benefit. In 2002, for example, women received an average monthly retirement benefit of $773.90 while men received an average monthly benefit of $1,008.10. Furthermore, women are less likely to have pensions through their employers. In 2002, 44 percent of women and 47 percent of men had private pensions. For those women who do have private pension, it tends to be less because, relative to men, more women tend to work part time and spend some time out of the labor force. Thus, Social Security is particularly important to women.

In addition, African Americans earn lower incomes in the course of work-life relative to whites and thus will receive lower average monthly benefits. In 2002, the average monthly retirement benefits for African Americans was $779.80 and that for whites was $911.70. Similarly, the importance of Social Security benefits to a majority of elderly cannot be exaggerated. Even though Social Security benefits are modest, they are the most important source of income for the majority of elderly households. Figure 1 below shows that, according to data collected by the Social Security Administration in 2001, Social Security benefits accounted for over half of income for sixty five percent of elderly households (65 years or older), and for one-third of these households the benefits were 90 to 100 percent of their income.
The importance of Social Security benefits to elderly will be appreciated when considering that the elderly households, in general, have lower income relative to the rest of population. Figure 2 shows that while only 9% of households had an annual income of $10,000 or less, this percentage for the elderly was more than double that percentage or 21%. Also, 40% of the elderly had incomes in the range of $10,000 to $25,000 while half that or 20% of other households had incomes in this range. The opposite is true at the high end of the income distribution where only 15% of the elderly enjoy incomes of $50,000 or more relative to 44% for the other households.

FINANCING SOCIAL SECURITY

The issues surrounding the reasons for and the importance of the Social Security Program were addressed in the previous sections. A burning question that remains for most people is, “when will the money run out?” The term money here is at the heart of some of the debate. The outflows from Social Security funds are straightforward and consist of payments to beneficiaries. An understanding of the inflows, on the other hand, is not as straightforward and is the source of much of the misinformation surrounding this issue.

Sources of funds that the Social Security system draws upon can be considered as three separate elements. One is the money paid in payroll taxes by current employees and employers (6.2% each). The second consists of interest earned on the surplus built up in the Social Security trust fund. The 1983 Social Security Commission, chaired by Alan Greenspan, deliberately designed a system that would build up a surplus by taxing more than was necessary to pay benefits (Baker, 2006). This money has been borrowed by the US government and the assets now exist in the form of government bonds. That is the surplus is being invested in non-tradable government bonds. In 2003, the effective annual interest earnings of all bonds held in the trust fund were about 6% (EPI, 2005). The federal government is naturally obligated to repay these bonds which leads to other economic questions, but not to uncertainty for the Social Security trust fund. The third entity is the amount of funds that have been accumulated in the trust fund itself.

There are then three time periods that become of interest in any analysis. One period of time that will be important in planning for the possible “crisis” is the date when the outflows exceed the money coming in from current employees and employers’ payroll taxes. The second date of interest is the time at which the outflow exceeds this income plus the interest income earned on the trust fund accumulation. The third is the date at which the trust fund accumulation (designed to allow for the retirement of the Baby Boomer generation) is exhausted. Since, by current law, these programs are not allowed to borrow, this is the date at which the Social Security account will no longer be able to pay anything approaching current payout levels.

If one is considering the first scenario in which outflow exceeds the income paid in by current employees and employers (the theory behind the pay-as-you-go system), then the consensus is that the funds will run out sometime in between 2016 and 2022 (Congressional Budget Office (CBO), 2001 and Social Security Administration, 2005). This can be seen graphically in Figures 3 and 4 below.

If, however, one considers the interest income from the Social Security Trust Fund, then the date of the crisis is extended to sometime in the late 2020’s (CBO, 2001). If we look at the date when all funds are exhausted and payments to retirees would cease, then we are interested in the date when all three assets go toward zero (since the system would presumably continue to tax current workers and employers, it would not be completely depleted). This can be seen in the following two figures which look at the Trust Fund ratio. The trust fund ratio is a useful indicator of the adequacy of the
financial resources of the Social Security Program at any point in time. In the year that the trust fund ratio becomes negative, the program will no longer be able to cover the full amount of benefits for that year under the current law (Social Security Trustees’ Report, 2005). Figure 5 shows projected estimates for the trust fund ratio.

{FIGURE 5 HERE}

The Congressional Budget Office predicts that the trust fund assets will be exhausted in the year 2052 (with 80% certainty). Clearly, we should be mindful of the fact that these funds can and will be exhausted. However, forty years from now the economy and, in fact, the world will be a very different place.

When considering the financial situation of retirees and employees in the years beyond 2052, one is reminded of a couple of quotes by famous economists reflecting on the analysis of long run macroeconomic issues. The first is Robert M. Solow who asked why current generations should be asked to sacrifice for future generations who will no doubt be made better off by technology (paraphrased) (Solow, 1985). The second, perhaps more famous, quote is by John M. Keynes who made the profound announcement that, “in the long run, we are all dead.” Over the past years since the Social Security Act has been enacted, we have faced a number of crisis periods in its history and responded with a number of measures such as delaying COLA and, perhaps the greatest change, gradually raising the age at which retired workers could receive full benefits. No doubt, when the time comes, future voters will be called upon to make these difficult decisions.

CONCLUSIONS

Social Security, which is recognized as one of the most successful anti-poverty social programs, in spite of some critics’ dire warnings, is not in danger of going bankrupt. Claims of the Social Security system being in “crisis” are equally suspect. Currently, the nonpartisan Congressional Budget Office does not project a shortfall until 2052. Perhaps, the wisdom of American people, in aggregate, is confirmed when they rejected the assault on Social Security as a pillar of the American way of life. To paraphrase Samuel Clemens, “the reports of Social Security’s demise have been highly exaggerated.”

Further avenues of research in this area include an analysis of the effects of the proposed reforms on various societal groups and an analysis of the assumptions used to generate the data contained in this report.

REFERENCES


Figure 1: Importance of Social Security benefits to those aged 65 and older

Figure 2: Elderly households have lower incomes


Figure 3: Income, Outlays and Balances of the Social Security Trust Funds 2001 to 2037

FIGURE 4
Long-Range OASI and DI Annual Income Rates and Cost Rates
[As a percentage of taxable payroll]
Source: 2005 OASDI Trustees Report

Figure 5: Trust fund ratio projections