The National Council of Social Security Management Associations, Inc.
GREYSTONE GROUP WASHINGTON REPORT
Legislative Report 8-2012
June 29, 2012

Overview

On Thursday, June 21, 2012, the U.S. House Committee on Ways and Means Subcommittee on Social Security held an oversight hearing on the 2012 Annual Report of the Social Security Board of Trustees. The hearing focused on the findings in the recently released 2012 Annual Report of the Board of Trustees of the OASDI Trust Funds, the effect of the trust funds' current cash flow deficit status and future exhaustion, and the cost of delaying actions to address Social Security's fiscal challenges for workers and beneficiaries.

Two witnesses were asked to testify on a single panel. The written testimony of the witnesses can be found at the link below:
http://waysandmeans.house.gov/Calendar/EventSingle.aspx?EventID=299570

Panel 1

Dr. Charles P. Blahous III, Trustee, Social Security and Medicare Boards of Trustees
Dr. Robert D. Reischauer, Trustee, Social Security and Medicare Boards of Trustees

The following Members of Congress attended the hearing:
Chairman Sam Johnson (R-3rd-TX)
Representative Kevin Brady (R-8th-TX)
Representative Aaron Schock (R-18th-IL)
Representative Rick Berg (R-At Large-ND)
Representative Adrian Smith (R-3rd-NE)
Representative Kenny Marchant (R-24th-TX)

Ranking Member Xavier Becerra (D-31st-CA)
Representative Pete Stark (D-13th-CA)

Hearing Background Provided by the Subcommittee

The Board of Trustees of the Federal Old-Age and Survivors Insurance (OASI) and the Federal Disability Insurance (DI) Trust Funds was established under the Social Security Act to oversee the financial operations of the OASDI Trust Funds. The Board is comprised of six members, four of whom serve by virtue of their positions in the Federal Government (the Secretary of the Treasury, who also serves as Managing Trustee, the Secretary of Labor, the Secretary of Health and Human Services, and the Commissioner of Social Security), and two members of the public who are appointed by the President and confirmed by the Senate. The Deputy Commissioner of SSA serves as Secretary of the Board.

The Social Security Act requires that the Board, among other duties, report annually to the Congress on the financial status of the OASI and DI Trust Funds. The overview section of the 2012 report concluded, "Under the long-range intermediate assumptions, annual cost for the OASDI program is projected to exceed non-interest income in 2012 and remain higher through the remainder of the long-range period. The combined OASI and DI Trust Funds are expected to increase through 2020, and then to decline and become exhausted and unable to pay scheduled benefits in full on a timely basis in 2033. However, the DI Trust Fund becomes exhausted in 2016, so legislative action is needed as soon as possible."

In the absence of intervening Congressional action or changes in projections, the Trustees project that incoming Social Security revenues would be sufficient to pay about three-quarters of scheduled benefits starting in 2033 and over the rest of the 75-year period.

In their "Message from the Public Trustees," the Public Trustees concluded that Social Security's finances had deteriorated primarily because of a weak economy and higher-than-expected inflation. The 2012 report said the Social Security outlook has worsened significantly relative to the 2011 report. The actuarial deficit in its combined trust funds is now 2.67 percent of taxable payroll, the highest recorded since the last major Social Security financing reforms roughly three decades ago. The report also said, "While there is no way to know what mixture of additional revenue and restraints on benefit growth will prove to be the most palatable means of strengthening Social Security's financial position, lawmakers should be aware that it will become increasingly difficult to avoid adverse effects on current beneficiaries, those close to retirement, and low-income beneficiaries in all birth cohorts if legislative actions are delayed much further."

In announcing the hearing, Chairman Sam Johnson stated, **"Americans have long known that without change, Social Security will be unable to keep its promises to the hard-working taxpayers who pay into the system. According to this year's report, not only is Social Security's outlook worse, it is clear that the longer we wait the harder it will be to protect benefits for those who rely on them most. I hope this hearing will help lead us to find commonsense solutions to secure Social Security's future."**

<u>Opening Statements</u>
The opening statements of Chairman Johnson and Ranking Member Becerra can be accessed at the respective links below:

Subcommittee on Social Security Chairman Sam Johnson (R-3rd-TX)
http://waysandmeans.house.gov/News/DocumentSingle.aspx?DocumentID=300324

Subcommittee on Social Security Ranking Member Xavier Becerra (D-31st-CA)
http://democrats.waysandmeans.house.gov/press/PRArticle.aspx?NewsID=12163

<u>Panel Opening Statements</u>
Following opening statements from Chairman Johnson and Ranking Member Becerra, the panel presented their oral remarks. The first to present was Dr. Charles P. Blahous, Trustee, Social Security and Medicare Boards of Trustees. Dr. Blahous began by noting that Social Security costs are rising, most of which will play out from 2008 to 2035. The primary driver of the cost increase is demographic, stated Dr. Blahous. On the revenue side, the main driver is growth in the number of workers. The ratio of beneficiaries to workers is very important when it comes to Social Security financing, stated Dr. Blahous. This ratio is in the process of dropping. In 2007, noted Dr. Blahous, there were slightly over

three workers supporting every beneficiary, today there are around 2.8 workers for every beneficiary. Under current projections, it will be down to 2.0 workers for every beneficiary by 2035. Part of the change in the ratio is due to increases in longevity, but the bigger factor is fertility patterns, noted Dr. Blahous.

Under the current projections, stated Dr. Blahous, the Social Security Trust Funds will be depleted in 2033, which is three years earlier than was projected last year. In 2033, there will only be sufficient funds to pay about 75 percent of scheduled benefits. The Social Security Disability Trust Fund is in worse shape, as it is expected to be depleted in 2016, which is two years sooner than last year's projection. One of the most recent strains on the system is the recent cut in the payroll tax rate from 12.4 percent to 10.4 percent, noted Dr. Blahous. This reduction is due to the Congressionally-enacted payroll tax holidays.

There are significant costs associated with delay in addressing the Social Security shortfall. To minimize either a significant tax increase, or some other drastic change, it is important that the Social Security shortfall be addressed very soon, noted Dr. Blahous.

Next to testify was Dr. Robert D. Reischauer, Trustee, Social Security and Medicare Boards of Trustees. Dr. Reischauer began by noting if one were to judge the health of the Trust Funds simply by the exhaustion date, then the Funds have significantly deteriorated since the 2011 report. Combined, the two Trust Funds are currently expected to be depleted in 2033. Really though, a more complete way to look at the current condition of a Trust Fund is its actuarial balance over a 75-year period. The actuarial measure is essentially the difference between the annual income and costs of the program summarized over a 75-year period and expressed as a percent of taxable income, stated Dr. Reischauer. Currently, it would take either an increase in the revenue rate or a decrease in the cost of the program of over two percent for the Trust Fund to be balanced for the next 75 years.

There are many reasons that the actuarial balance may go up or down, added Dr. Reischauer. Some of the reasons may be that the evaluation period changes, updated demographic starting values are used, or different economic assumptions are applied. Most of the change in the actuarial balance from last year to this year comes from changes in economic assumptions because of changes in the economy, stated Dr. Reischauer.

In closing, Dr. Reischauer noted that the deterioration of Social Security's actuarial balances underscores the need for legislation to get the program on a more sustainable path. The sooner we address this problem, the less drastic the actions that we take will have to be, and the more time we will have to phase-in and spread out any such changes, noted Dr. Reischauer.

<u>Question and Answer</u>

Following the oral statements by the witnesses, the question and answer session between members of the Subcommittee and the witnesses began. The following details a few key exchanges during this session.

Chairman Johnson (R-3rd-TX) asked the panel if we continue to replace Social Security revenue with income tax revenue, how much longer will it be before the Social Security program starts to no longer be seen as an earned benefit, and what would that do to the confidence of individuals in the program? Dr. Blahous responded that no one knows when the confidence or the perception of the program may change. Over the years, Social Security has had a particular reasoning behind the way the program's funding has been spent, dating all the way back to President Roosevelt. The intermingling of Social Security funds and General Account funds puts the program at great political risk. Dr. Blahous also mentioned the tax holiday was essentially paid for by the individuals that invest in U.S. Treasury bonds, as Social Security was reimbursed, from the General Fund, the amount lost because of the tax holiday.

Ranking Member Becerra (D-31st-CA) asked Dr. Reischauer if the fact that we have had a steady stream of immigrants coming into the country helps the Social Security system as far as being able to continue to pay out benefits. Dr. Reischauer stated that the influx of immigrants has increased the size of the labor force as well as increased the number of individuals paying payroll taxes, which over the short-run clearly helps the program to pay benefits. But ultimately, it is much more complicated than that, as there are also long-term draws that immigrants have on the system, stated Dr. Reischauer.

Representative Brady (R-8th-TX) asked the witnesses how quickly Congress should act to address the shortfall in the Social Security Trust Funds. Both witnesses stated that Congress needs to act very soon. Dr. Reischauer added that he hoped Congress would act within the next five years. Representative Brady followed up by asking the witnesses if Congress should continue the payroll tax holiday. Dr. Blahous noted that he thinks Social Security should go back to its 12.4 percent rate, which Dr. Reischauer also agreed with, but noted he believes it should be done in a phased manner.

Representative Aaron Schock (R-18th-IL) asked the witnesses what will be in store for the younger generation of Americans if we do not fix the Social Security Trust fund very soon. Dr. Blahous responded that the mathematical part of the answer is that young Americans will be facing a net income loss. Overall, this would be around a four percent net income loss through Social Security, after benefits are paid out. From a political perspective, the younger generation may face a lack of political will to keep the program operating on a purely self-financing basis. Dr. Reischauer noted that future generations will also run a greater risk when it comes to disability. Dr. Blahous stated that the Social Security program has not faced an actuarial deficit as large as it is now, since before the 1983 reforms.

Representative Pete Stark (D-13th-CA) asked the panel what the shortfall would be in a dollar amount, from 2033 through the remaining period of the 75-year evaluation window. Dr. Blahous stated that the shortfall would be approximately $8.6 trillion.

Representative Kenny Marchant (R-24th-TX) asked the witnesses to discuss the amount of the shortfall of the Disability Trust Fund, from 2016, through the rest of the decade. Dr. Blahous responded that the approximate amount is about $30 billion a year from 2016 through the rest of the decade. Additionally, to keep benefits paid in full, out of the Old Age Survivor Trust Fund, starting in 2035, it would require approximately $200 billion a year of additional appropriated resources. These numbers are calculated, assuming that nothing changes between now and 2016 or 2035. Dr. Blahous also noted that for revenues to be transferred from the General Fund, to the Social Security Trust Fund, it would require, under current law, an act of Congress. Ranking Member Becerra, then expanded on this line of questioning, noting that by law the Social Security Trust Funds cannot run a deficit.

Representative Adrian Smith (R-3rd-NE) next asked the witnesses whether the Social Security Trust Funds add to the federal deficit. Dr. Blahous noted that approved revenue transfers, like the one from the General Account to the Social Security Trust Funds, for the tax holiday, do add to the deficit. But whenever the Trust Funds rely on payroll income, it does not add to the deficit. Where most of the disagreement comes is when you start to consider the interest payments made to the Social Security Trust Funds. From now up until 2033, Social Security will largely rely on the interest payments to keep the program afloat.

If you are interested in watching the video of the hearing, you can access the archived webcast at the link below:
http://waysandmeans.granicus.com/MediaPlayer.php?view_id=2&clip_id=343

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