THE CENTURY FOUNDATION

ISSUE BRIEF

# TEN REASONS NOT TO CUT SOCIAL SECURITY BENEFITS

**By Greg Anrig**

Social Security is widely recognized as the most effective and popular governmental program in the United States. It provides essential insurance to the disabled, families of deceased workers, and retirees. The poverty rate among the elderly has declined from over 35 percent before 1960 to about 9 percent today, largely because of reforms to Social Security that extended its coverage and enhanced benefit levels. Without Social Security, about 45 percent of the U.S. population aged 65 and over would be in poverty today.[1]

In recent weeks, a variety of groups, including the National Commission on Fiscal Responsibility and Reform, have proposed reducing the benefits that the program provides. The primary rationale given for those cuts is to decrease future budget deficits. It is important to recognize, though, that the federal government's high and rising debt would be much *larger* without Social Security, which for many years has collected substantially more in taxes than it has paid out in benefits.

Forecasts of unsustainably high levels of federal debt in the future are almost entirely attributable to rapidly rising health care costs, not Social Security. As the Baby Boom generation retires, Social Security's outlays are expected to rise only at a relatively modest, predictable rate before leveling off. The long-term gap between revenues already dedicated to Social Security and promised benefits is relatively small and not a major contributing factor to the anticipated escalation in federal deficits and debt.

Nonetheless, a consensus appears to be emerging among some prominent Democrats, as well as conservative Republicans who have always been hostile to Social Security, that the only fiscally responsible course of action is to curtail payments to the program's beneficiaries. Here are ten reasons why that perspective is wrong.

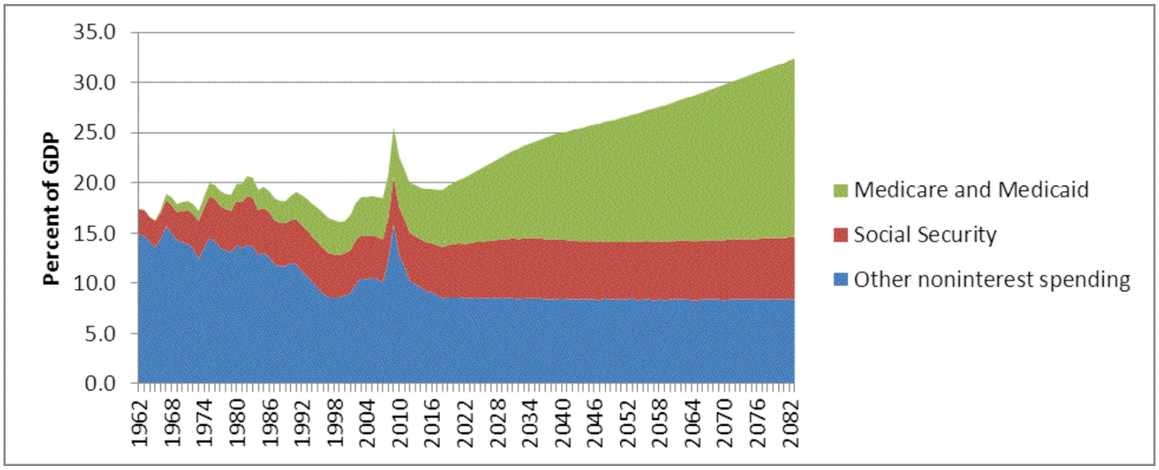
## 1. Social Security is not responsible for federal deficits.

Federal budget deficits currently are unusually high, but Social Security bears no responsibility for today's shortfalls. Keep in mind that the federal government was experiencing budget *surpluses* at the end of the 1990s, but those quickly were transformed into deficits early in the 2000s because of large tax cuts and increased governmental spending on the wars in Iraq and Afghanistan, as well as homeland security. The nation's fiscal situation worsened when the recent economic downturn caused federal revenues to collapse along with taxable incomes and profits, greatly widening budget deficits.[2] Because Social Security continued to collect hundreds of billions of dollars more from payroll taxes than it spent on benefits throughout the decade, however, the program actually *reduced* overall federal budget deficits far below what they otherwise would have been.

With unemployment still stubbornly high, federal deficit spending helps keep the economy from falling back into a recession while protecting the most vulnerable Americans, so short-term deficit spending is needed. Looking forward, however, after high employment eventually returns, the prospect of large and rising deficits into the next decade is a genuine cause for concern. Letting the federal debt grow to the point that it is larger than our economy and still continue to escalate indefinitely could cause interest rates to rise, dampening private sector economic activity and bloating the government's debt service costs.

As Figure A shows, the dominant cause of the projected long-term debt problem is not Social Security, nor short-term deficit spending to aid economic recovery, but rather the expectation that health care costs will continue to rise much more rapidly than overall inflation. Projections show that combined Medicare and Medicaid outlays for the federal government will double, from about 5 percent of gross domestic product (GDP) today to about 10 percent by 2030.

## Figure A. Medicare, Medicaid, and Social Security as a Percentage of Government Spending




*Source:* Congressional Budget Office, *The Long-Term Budget Outlook 2009* (Washington, D.C.: Government Printing Office, 2009), Figure 1-1.

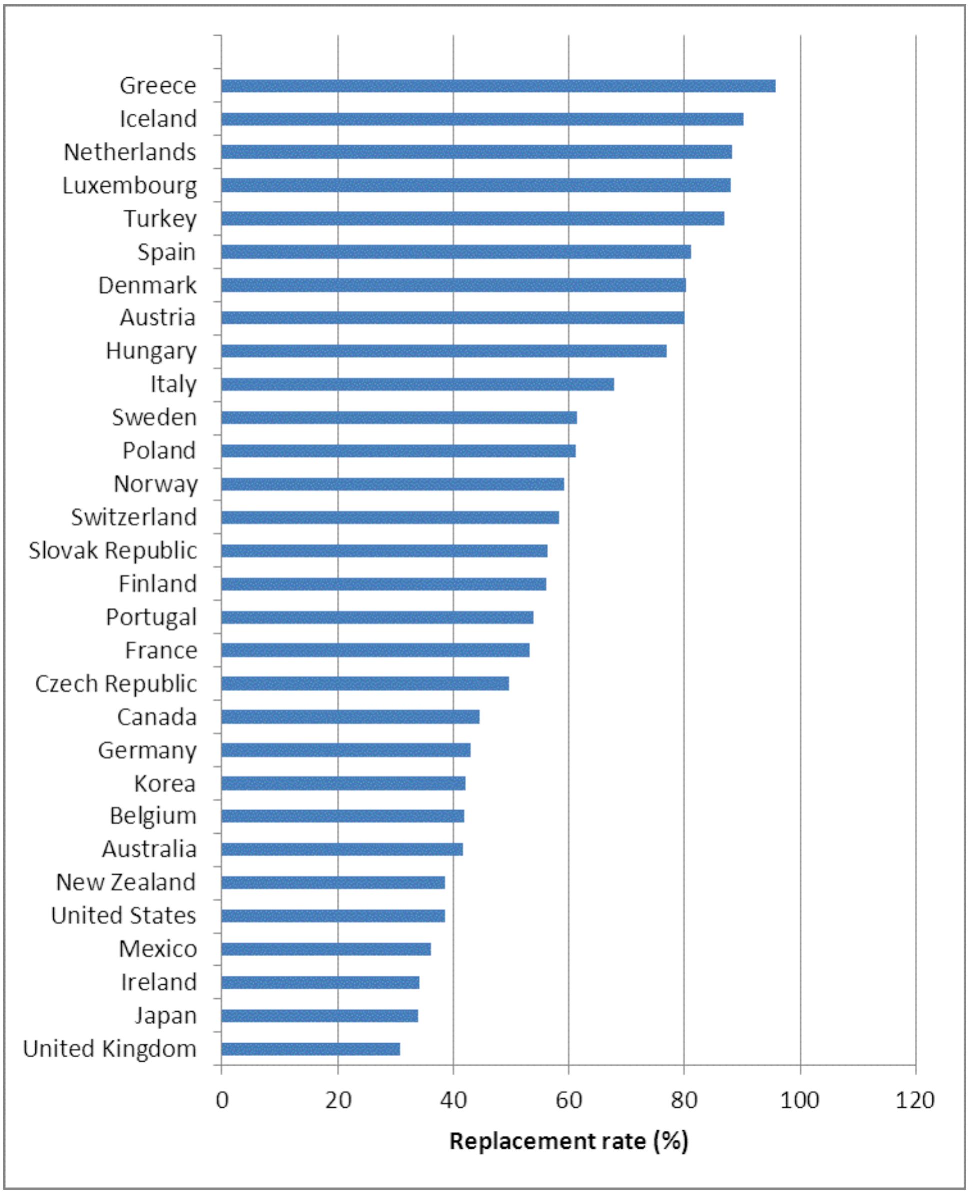
Social Security's expected growth is expected to be far more modest, and much more manageable, gradually rising from the same 5 percent of GDP today to about 6 percent by 2030, as the Baby Boom generation retires. Throughout that period, the revenues dedicated to the program from payroll taxes and commitments from its large and growing trust funds will be more than sufficient to pay benefits in full until around 2037. At that point, if nothing is done, benefits would have to decline by about a fifth. But even under that unlikely scenario, overall federal deficits would not increase, because the program's payments would decline to match tax revenues. Over the next seventy-five years, Social Security's projected shortfall between dedicated revenues and promised benefits is just 0.6 percent of GDP. That is just a small fraction of the overall gap between government revenues and outlays that is projected to arise.

Preventing federal debt from rising to unmanageable levels in the future will require significant revenue increases and spending reductions, coupled with fundamental reforms to America's deeply flawed health care system—reforms that the new health care legislation takes important steps in advancing. A blueprint from a collaboration of the Economic Policy Institute, Demos, and The Century Foundation—called Our Fiscal Security—spells out in detail changes that would greatly strengthen the nation's fiscal health without requiring cuts to Social Security.[3] When politicians and commentators argue that there is no responsible alternative to reducing Social Security benefits, that erroneous claim is itself irresponsible.

# 2. Social Security's benefit levels are far from overly generous.

Compared to the government-provided pension programs of other countries, Social Security ranks near the bottom in the share of a retired worker's past earnings that it replaces. As Figure B, shows, out of thirty OECD countries, America's Social Security system is twenty-sixth overall in the share of a median worker's earnings that is replaced by government pension programs.

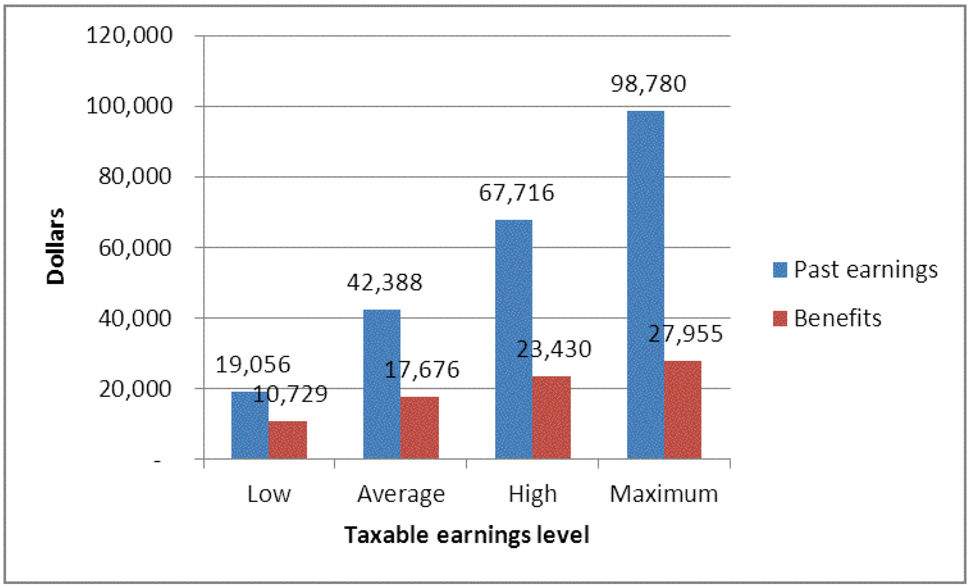
### Figure B. Social Security Replacement Rates in OECD Countries, by Income Level




*Source: Pensions at a Glance: Retirement-Income Systems in OECD Countries* (Paris: Organisation for Economic Co-operation and Development, 2009), 117.

The average annual Social Security benefit for retired workers is only $14,105. In 2010, 95 percent of retired workers received monthly benefits of less than $2,000. As Figure C demonstrates, the program's payments are structured so that retirees who earned relatively high incomes during their working years receive a smaller share of their past earnings than those with lower incomes. So retirees whose annual incomes exceeded $100,000 receive back a much smaller share of the taxes they paid into the Social Security system than workers with lower incomes.

### FIGURE C. SOCIAL SECURITY BENEFITS COMPARED TO PAST EARNINGS, 2010



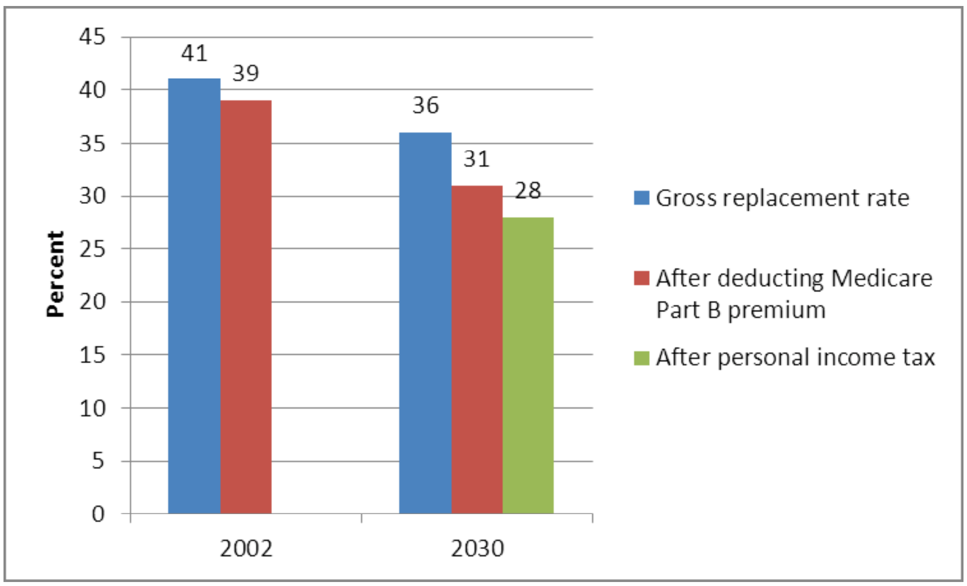

Source: The 2010 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds (Washington, D.C.: Government Printing Office, 2010), Table VI.F10, http://www.ssa.gov/OACT/TR/2010/VI_OASDHI_ dollars.html#119381.

## 3. THOSE MODEST PAYMENTS ALREADY ARE SCHEDULED TO BE REDUCED SUBSTANTIALLY.

Even if no additional benefit cuts are enacted, future retirees will receive somewhat lower payments relative to today's beneficiaries. One main reason is that the age when full retirement benefits can be collected, which already has been increased from 65 to 66, is scheduled to be increased further to 67 by the year 2022. The effect of that increase is to reduce the size of benefits for future retirees *regardless of what age they choose to begin collecting benefits*.

In addition, net Social Security benefits will be lower in the future under existing law because of two other factors. One is that a higher portion of beneficiaries will owe income taxes on their benefits, which applies on earnings above $25,000 for individuals and $32,000 for married couples—thresholds that do not increase over time with inflation. The other reason is that Medicare Part B premiums, which are subtracted from Social Security benefits, are expected to rise more rapidly than Social Security payments. As Figure D demonstrates, the effect of all those factors that will apply in the years ahead under current law will be to reduce the net replacement rate for an average worker retiring at the age of 65, from 39 percent of past earnings in 2002 to 28 percent by 2030.

### Figure D. Social Security Replacement Rates for an Average Earner Retiring at Age 65 in 2002 and 2030



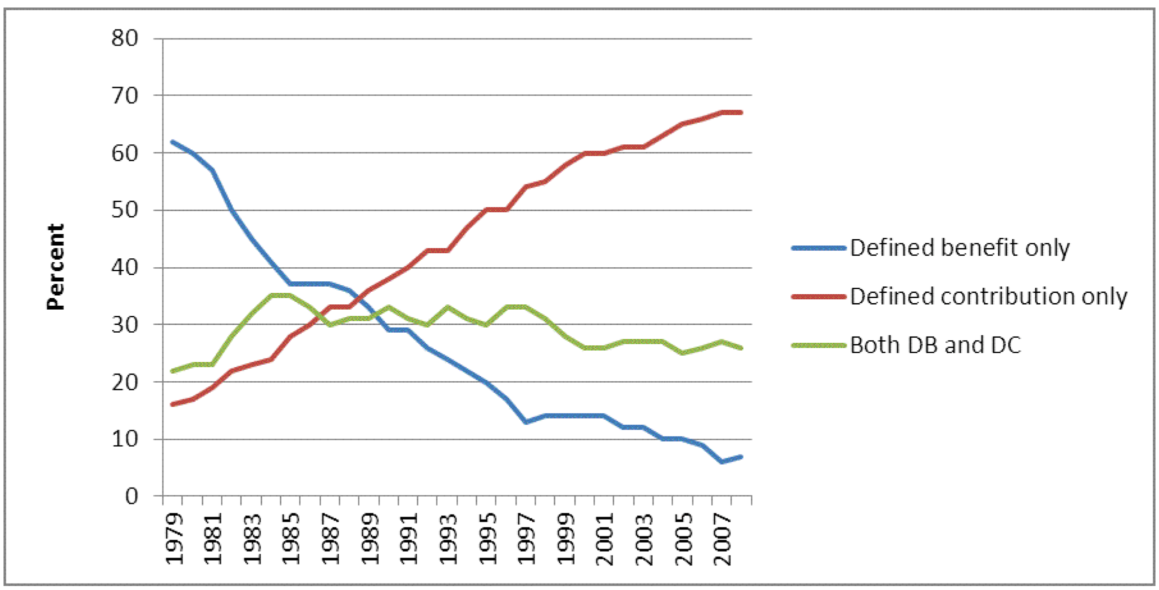

*Source:* Alicia H. Munnell, *The Financial Crisis and Restoring Retirement Security,* Testimony before the Committee on Education and Labor, U.S. House of Representatives, 111th Cong., 1st sess., February 24, 2009, Figure 4, http://democrats.edworkforce.house .gov/documents/111/pdf/testimony/20090224AliciaMunnellTestimony.pdf.

## 4. Private pension coverage is weak and uncertain.

In the past, many workers could rely on so-called defined benefit pensions provided by their employers, which promised retirement payments based on a worker's salary and years of service. In the private sector, those once-common pensions have all but disappeared. To a large extent, they have been replaced by defined contribution plans such as 401(k)s. The value of the newer brand of pensions depends largely on how much workers have paid into them and how successfully the investments in the accounts perform. The shift from defined benefit to defined contribution plans essentially has transferred the burdens and risks associated with providing retirement savings from employers to workers.

Figure E shows this sea change in private sector pensions. Among workers with some form of retirement plan, the share with only a defined benefit pension declined from 62 percent in 1979 to 7 percent in 2008. Sixty-seven percent of workers with a retirement plan in 2008 had only a 401(k)-type defined contribution plan. The decline of defined benefit plans has reduced the retirement security of a large share of the workforce, making them more reliant on highly unpredictable and volatile savings plans. In addition, middle- and lower-income workers, who are less likely to participate in defined contributions plans, are now less likely to have any form of pension support at all.

**FIGURE E. PRIVATE SECTOR PARTICIPANTS IN AN EMPLOYMENT-BASED RETIREMENT PLAN, BY PLAN TYPE, 1979–2008**

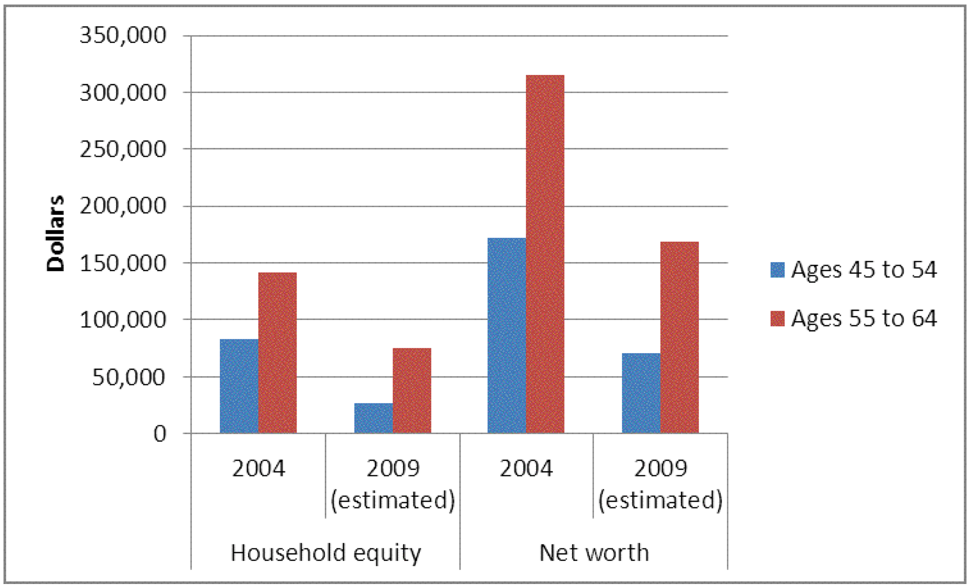



*Source:* "FAQs about Benefits—Retirement Issues," Employee Benefit Research Institute, Figure 2, http://www.ebri.org/publications/benfaq/index.cfm?fa=retfaq14.

## 5. REAL ESTATE EQUITY HAS PROVEN TO BE AN UNRELIABLE SOURCE OF RETIREMENT SAVINGS.

Until the recent collapse of the housing market, many American families had come to believe that owning a home would be an important way to help ensure that they would have a secure retirement. Prior to the bursting of the real estate bubble, housing equity accounted for nearly half of median net worth for families. The Center for Economic and Policy Research estimated that, for households headed by an individual in the age range of 55 to 64, median home equity values fell about 47 percent from 2004 to 2009—from $142,000 to $75,300.[4] (See Figure F.) Those levels show little prospect of recovering substantially in the foreseeable future, leaving most families approaching retirement age in a much weaker financial position than they expected.

### Figure F. Median Household Equity in Real Estate and Net Worth 2004 and 2009




*Source:* Dean Baker and David Rosnick, "The Wealth of the Baby Boom Cohorts after the Collapse of the Housing Bubble," Center for Economic and Policy Research, February 2009, 6.

## 6. Most retirees have minimal income sources beyond Social Security.

On average, Social Security provides about two-thirds of the income for Americans aged 65 and over. For about 20 percent of retirees, Social Security is the only source of income. As Table 1 indicates, only individuals in the top fifth of the income spectrum have significant pensions and other sources of earnings. Those individuals tend to be relatively young, married, and still in the workforce.

### Table 1. Social Security Benefits Make Up Large Share of Beneficiaries' Total Income, Beneficiary Units 65 or Older, 2008

| Benefit Quintile | Benefit Amount | Median Total Income |
|---|---|---|
| First (lowest) | Up to $9,989 | $10,517 |
| Second | $9,989–13,157 | $14,100 |
| Third | $13,157–16,757 | $20,579 |
| Fourth | $16,757–22,757 | $30,000 |
| Fifth (highest) | $22,757 and up | $49,906 |

*Source:* Social Security Administration, *Income of the Population 55 or Older, 2008,* Table 3.A6. Data are for "aged units"—unmarried people age 65 or older, and married couples in which at least one spouse is age 65 or older. Each quintile contains one-fifth of all such units, so that the third quintile represents the overall median.

## 7. It has become increasingly difficult for older workers to keep good jobs.

One common argument in favor of delaying the age when workers can begin Social Security retirement benefits, as the National Commission on fiscal Responsibility and Reform proposes, is that it would encourage Americans to remain employed later in life. But while that might seem like a worthy goal, the labor market has evolved in ways that have made it less likely that workers will remain in good jobs as they get older. Given those economic forces, any reductions in Social Security benefits are likely to elevate hardship among individuals who simply cannot find decent work as they approach their 60s.

In 2006, only 46 percent of men aged 58 through 62 were working for the employer they had at age 50, compared with 65 percent in 1983.[5] The reasons for that drop-off are complex, but one clear factor appears to be the decline of defined benefit pensions, which encouraged workers to remain with the same employer to maximize what they would receive in retirement. In addition, one study found that workers in their 50s who were laid off or otherwise pressured to leave their jobs were highly likely to experience such difficulties as multiple periods of unemployment and further severances.[6] In the aftermath of the Great Recession, the unemployment rate among workers over the age of 55 was the highest it has been since 1948, and the average duration of unemployment for job seekers in that age group was eleven weeks more than the national average.[7] As of January, the unemployment rate among Americans aged 55 and over improved to 7.2 percent.

Disincentives to retain and hire older workers include their relatively higher health care costs and their experience in professions for which demand has declined. Existing age discrimination laws generally are not enforced energetically and are often difficult to apply in particular cases. So while delaying the age when Social Security first can be collected or otherwise reducing benefits certainly would create additional incentives to work longer, many millions of Americans in their 50s and 60s already have an extraordinarily difficult time retaining and finding decent jobs.

## 8. THE PUBLIC IS STRONGLY OPPOSED TO ALL FORMS OF BENEFIT CUTS.

Social Security has been the subject of numerous polls, extending over many decades, and the results of those surveys have been remarkably consistent in finding that the program is enormously popular with virtually every sub-category of the population. As professors Benjamin I. Page and Lawrence R. Jacobs have written, "Many more Americans want to *increase* spending on Social Security than want to decrease it—this has been true for decades. Virtually any sort of benefit cut is opposed by substantial majorities of Americans."[8]

The Peter G. Peterson Foundation, which has spent many millions of dollars attempting to build public support for Social Security benefit reductions, recently convened a project in which groups of Americans were asked to work on their own budget reforms. But even that effort, called America Speaks, demonstrated that participants opposed cuts to the program. Just 24 percent favored reductions in the index used for cost-of living adjustments, 24 percent supported a later age when benefits could first be collected, and 39 percent favored raising the age when full benefits could be received to 69. (In contrast, 60 percent favored raising the existing ceiling on earnings subject to Social Security's payroll tax—a change that would improve Social Security's finances without cutting benefits.) Other, more scientific polls have also consistently found little support for any type of benefit cut to Social Security.

## 9. There are less painful ways to ensure that Social Security will be adequately funded indefinitely.

According to Social Security's Trustees, the program will be able to continue to pay promised benefits in full until 2037. After that point, payroll taxes paid by workers will be sufficient to finance about 75 percent of promised benefits. The policy challenge is to close that future gap between the program's revenue sources and benefits, which amounts to about 0.6 percent of GDP and 2.0 percent of projected payroll income over the next seventy-five years.

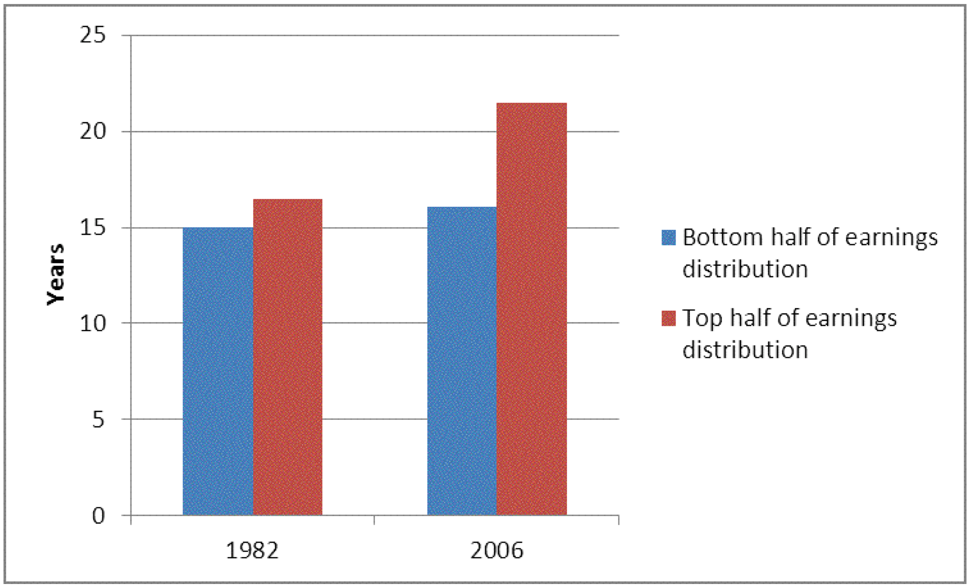
One straightforward change that would eliminate that entire future shortfall would be to eliminate the current ceiling on earnings subject to the Social Security payroll tax. Under current law, Social Security taxes are not collected on income above $106,800. If the 12.4 percent payroll tax—half of which is paid by workers and the other half by employers—were to be collected on all wage income, currently promised benefits could be paid in full indefinitely.

A variation on that approach would be to remove the cap entirely on the employers' side and raise it to its historical level of 90 percent of benefits for workers. That step would close about three-quarters of the projected shortfall. Polls show that raising or eliminating the payroll tax cap is a far more popular solution than other approaches that involve reducing benefit levels. Such reforms also would put the burden on individuals who could most afford to pay, in contrast to benefit reductions, which would reduce the retirement security of less prosperous Americans.

## 10. Life expectancies vary widely among different groups of Americans.

The main argument for hiking the Social Security retirement age—which amounts to an across-the-board benefit cut of about 7 percent for each year it is raised—is that average life spans are increasing. But longevity improvements are highly concentrated among upper-income and well-educated Americans. Over the past twenty-five years, life expectancy at age 65 has increased by just one year for lower-income men, compared to five years for upper-income men. Men in the bottom half of the earnings distribution have shorter life expectancies today than men in the top half had back in 1982. (See Figure G.) For women in the bottom half of the earnings distribution, life expectancies actually have declined over the same period. Reducing benefits for everyone on the basis of longevity improvements for only the most prosperous Americans would be an inequitable and poorly reasoned policy response

## FIGURE G. MALE LIFE EXPECTANCY AT AGE 65




*Source:* Harry C. Ballantyne, Lawrence Mishel, and Monique Morrissey, "Social Security and The Federal Deficit: Not Cause and Effect," Briefing Paper #273, Economic Policy Institute, August 6, 2010, Figure F, http://epi.3cdn.net/99133adf653fd78719_qym6b95et.pdf.


WRITTEN BY GREG ANRIG, VICE PRESIDENT, POLICY AT THE CENTURY FOUNDATION



FEBRUARY 17, 2011




[11] Paul N. Van de Water and Arloc Sherman, "Social Security Keeps 20 Million Americans Out of Poverty: A State-by-State Analysis," Center on Budget and Policy Priorities, August 11, 2010, http://www.cbpp.org/cms/index.cfm?fa=view&id=3260.

[2] See, for example, Kathy Ruffing and James R. Horney, "Critics Still Wrong on What's Driving Deficits in Coming Years," Center on Budget and Policy Priorities, June 28, 2010, http://www.cbpp.org/cms/index.cfm?fa=view&id=3036; John Irons, Kathryn Edwards, and Anna Truner, "The 2009 Budget Deficit—How Did We Get Here?" Economic Policy Institute, August 2009, http://epi.3cdn.net/0974dad8645a9d3216_5tm6bnxqd.pdf.

[3] "Investing in America's Economy: A Budget Blueprint for Economic Recovery and Fiscal Responsibility," Demos, Economic Policy Institute, and The Century Foundation, November 29, 2010, http://tcf.org/publications/2010/11/investing-in-americas-economy-a-budget-blueprint-for-economic-recovery-and-fiscal-responsibility/pdf.

[4] David Rosnick and Dean Baker, "The Wealth of the Baby Boom Cohorts after the Collapse of the Housing Bubble," Center for Economic and Policy Research, February 2009, 6, http://www.cepr.net/documents/publications/baby-boomer-wealth-2009-02.pdf.

[5] Alicia H. Munnell and Steven A. Sass, "The Decline of Career Employment," Center for Retirement Research, Boston College, September 2008, http://crr.bc.edu/images/stories/Briefs/ib-8-14.pdf.

[6] Steven A. Sass and Anthony Q. Webb, "Is the Reduction in Older Workers' Job Tenure a Cause for Concern?" Center for Retirement Research at Boston College, December 2010.

[7] Annie Lowrey, "Too Young Not to Work but Too Old to Work," *Washington Independent,* June 17, 2010, http://washingtonindependent.com/87333/too-young-not-to-work-but-too-old-to-work.

[8] Benjamin I. Page and Lawrence R. Jacobs, "Understanding Public Opinion on Deficits and Social Security," Roosevelt Institute, June 27, 2010, http://www.newdeal20.org/wp-content/uploads/2010/06/tuespage-and-jacobs-public-opinion.pdf.