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Social Security Finances: Findings of the 2010 Trustees Report

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Summary

In January 2010, 52.7 million people, or about one in every six U.S. residents, received Social Security benefits. The benefits are financed by dedicated taxes on earnings paid by workers and employers, by income taxes that upper income beneficiaries pay on part of their Social Security benefits, and by interest earned on accumulated trust fund reserves. According to the 2010 Trustees report, the Social Security trust funds will have an annual surplus of $77 billion in 2010. Annual surpluses are projected to continue for the next 15 years (2010-24) and reserves are projected to grow to $4,200 billion by the end of 2024. Beginning in 2025, reserves will start to be drawn down to pay benefits. In 2037, the reserves are projected to be depleted. At that time, tax income coming into the trust funds will cover about 78 percent of benefits due, according to the 2010 report of the Social Security Trustees.

What is the Trustees report?

The Social Security Act calls for a Board of Trustees for the Social Security trust funds and requires the Board to report annually to the Congress on the financial and actuarial status of the funds. The Board also reports on the Medicare trust funds, which are discussed in a separate report.

The Board has six members; the Secretaries of the Treasury; of Labor; and of Health and Human Services; the Commissioner of Social Security; and two trustees representing the public who are from different political parties and are appointed by the President and subject to Senate confirmation. The two public positions have been vacant for the past three years.

The report is a tool for Congress and the public to gauge the financial status of the Social Security system and to understand the size of the program's long-term commitments. The 2010 report is the 70th to be issued and is available on the website of the Office of the Chief Actuary of Social Security at www.ssa.gov/OACT.

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Who pays for Social Security?

Social Security is financed mainly by Social Security taxes (or contributions) paid by workers and employers as called for under the Federal Insurance Contributions Act (FICA). The tax rate for both workers and employers is 6.2 percent of earnings up to a cap ($106,800 in 2010). The combined tax rate is 12.4 percent. Self-employed persons pay both the employee and the employer share of the tax and get a deduction from their personal taxable income for half of the total tax. In addition, upper income Social Security beneficiaries pay income taxes on part of their Social Security benefits, and some of this income-tax revenue is dedicated to the Social Security trust funds. Finally, interest earned on accumulated trust fund reserves is a third source of income. According to the 2010 Trustees report, income from Social Security payroll taxes will account for 81.8 percent of trust fund income in 2010, while income taxes paid by beneficiaries will be 3.3 percent, and interest on reserves will be 14.9 percent (Board of Trustees 2010).

Who receives Social Security?

Social Security pays monthly benefits that replace, in part, income from wages lost when a worker retires, becomes disabled, or dies. Benefits are paid to the worker and to family members who relied on the lost earnings.

In January 2010, 52.7 million people, or about one out of every six Americans, received Social Security benefits (Social Security Administration (SSA) 2010a; U.S. Census Bureau 2010a). Nearly one family in four receives income from Social Security (U.S. Census Bureau 2010b).

Social Security beneficiaries include 33.7 million retired workers, 4.4 million widows and widowers, and 2.5 million spouses. About 7.8 million disabled workers receive benefits, along with 0.9 million severely disabled adult children of deceased, retired, or disabled workers. Another 3.2 million children under age 18 receive benefits because their parent died, became disabled, or retired (SSA 2010a).

How much does Social Security pay?

The average monthly benefit paid to retired workers was $1,166 (about $14,000 annually) in January 2010 (SSA 2010a). The average benefit was somewhat smaller for disabled workers ($1,064) and for widows and widowers age 60 or older ($1,125). Benefits are somewhat higher for families. Widowed mothers with two children received $2,404, on average, or about $28,850 a year, while disabled workers with a young spouse and one or more children received $1,797 a month, on average, or about $21,560 a year (SSA 2010b). For comparison, the 2010 federal poverty guideline for a family of three is $18,310 a year; for a family of four it is $22,050 (U.S. Department of Health and Human Services 2009).

Social Security is the main source of income for most beneficiaries 65 years of age or older. The benefits account for half or more of total income for one out of two

beneficiary married couples and 72 percent of nonmarried beneficiaries (SSA 2010c). For all but the highest-income 20 percent of older Americans, Social Security is the largest single source of income. For more information about the critical role Social Security plays in the lives of beneficiaries, see the Academy's 2009 report *Fixing Social Security: Adequate Benefits, Adequate Financing*.

Table 1. Average Monthly Benefits, January 2010

Type of Beneficiary	Benefit
Retired workers	$1,166
Aged widows and widowers alone	$1,125
Disabled worker alone	$1,064
Widowed mother and two children	$2,404
Disabled worker, young spouse and one or more children	$1,797

Source: Social Security Administration 2010b.

How do actuaries project the future?

Each year the Social Security actuaries review the performance of the economy, take into account new laws and regulations, and reassess assumptions about future economic and demographic trends that will affect the Social Security system – including employment, wage levels, productivity, inflation, interest rates, birth rates, death rates, and immigration.

The actuaries make projections for three scenarios: low-cost; high-cost; and intermediate. The trustees review and agree on assumptions for each scenario. The intermediate scenario is considered their "best estimate" and is most often cited. In general, the low-cost estimate uses a more optimistic set of assumptions (such as higher economic growth, lower unemployment, and low inflation) whereas the high-cost estimate employs more pessimistic assumptions as they pertain to the trust funds' future financial outlook. For each scenario the Trustees report projects the status of the funds for the near term (the next 10 years) and the long term (the next 75 years).

What do the Trustees project for the next few years?

In 2010, the Social Security trust funds will receive income of $791 billion and pay out $715 billion, leaving an annual surplus of $77 billion. Almost all outgo is used to pay benefits; less than 1 percent of outgo is spent on administrative costs.

By law, the annual surpluses – amounts not needed for current expenditures – are invested in interest-bearing U.S. government securities. The invested assets, or trust fund reserves, are estimated to be $2,617 billion by the end of 2010.

Social Security benefits generally increase each year by an annual cost-of-living adjustment (COLA), which is based on the Consumer Price Index (CPI-W). Because the CPI-W declined after the December 2008 COLA was determined, no COLA occurred at the end of 2009 and no COLA is expected at the end of 2010. Under the law, the cap on taxable earnings (the taxable maximum) does not increase if no COLA is provided. Thus, the taxable maximum for 2011 is expected to remain the same as for 2010.

Under the intermediate assumptions, the Social Security trust funds are projected to have surpluses in each of the next 15 years (2010-2024). That is, income from taxes and interest will exceed outgo for benefits and administrative costs and the reserves will continue to grow. By the end of 2024, the reserves are estimated to be $4,200 billion.

What do the Trustees project for the next 75 years?

Under intermediate assumptions, income to the trust funds will not cover all scheduled benefits over the next 75 years. According to the 2010 Trustees report:

- In 2025, tax revenues plus interest income to the trust funds will be less than total expenditures for that year. Reserves will then start to be drawn down to pay benefits.

- In 2037, the reserves will be depleted. Income coming into the funds then is expected to cover about 78 percent of the scheduled benefits and administrative costs.

- By 2084, the end of the 75-year projection period, assuming no changes in taxes or benefits, tax income is projected to cover about 75 percent of costs.

The long-range actuarial deficit is 1.92 percent of taxable payroll. This means that to close this gap solely with a tax increase, the Social Security tax rate (FICA) could be increased by 1.98 percentage points, starting this year. The necessary tax increase is higher than the actuarial deficit due to the assumed response of employees and employers to an increase in taxes. This change would raise the Social Security tax rate paid by employees (and matched by employers) by 0.99 percentage points, from 6.2 to7.19 percent. This summary measure shows the size of the long-range deficit in relation to taxable earnings, which are the main source of income to the system. For more information on eliminating the funding shortfall see the Academy's 2009 report *Fixing Social Security: Adequate Benefits, Adequate Financing*.

The Trustees also project Social Security tax income and outgo in relation to the total economy, or gross domestic product (GDP). In 2009, Social Security tax revenue coming into the system and outgo from the trust funds were both 4.8 percent of GDP. By 2035, tax income is projected to be 4.9 percent of GDP while outgo is projected to rise to 6.1 percent of the total economy. By 2084, the end of the 75-year projection

period, outgo will be slightly lower than projected for 2035, but tax income will have declined more as a share of GDP (Table 2).

Table 2. Social Security Tax Income and Outgo as a Percent of Gross Domestic Product

	Tax Income	Outgo
2009	4.8	4.8
2035	4.9	6.1
2084	4.6	6.0

Why will Social Security cost more in the future?

Social Security will cost more in the future because the number of people receiving benefits will grow faster than the number of workers paying into the system. This occurs because: the large number of boomers born between 1946 and 1964 will start receiving benefits (the oldest boomers will reach age 65 in 2011); people are projected to live longer after age 65; and lower birth rates that followed the birth of the baby boom are projected to continue.

Why is Social Security income projected to decline as a share of GDP?

While Social Security payroll taxes are a constant share of taxable payroll, those revenues are projected to decline as a share of the entire economy, or GDP, as shown in Table 2. This occurs because workers' wages that are subject to Social Security taxes will grow more slowly than other types of income, according to the projections. As a share of the total economy, wages that are subject to Social Security taxes equaled 37.0 percent of GDP in 2009. That share is projected to decline to 34.6 percent in 2084. Key sources of income that are not taxed to pay for Social Security include: workers' earnings above the tax base ($106,800 in 2010); employers' contributions to workers' health insurance premiums, pensions, 401(k) plans, and other employee benefits; and income from property, such as interest, dividends, and rental income.

How do the 2010 "best estimate" projections compare to previous years' reports?

Table 3 compares some key results from the current and previous Trustees reports. The projections change due to changes in methods and assumptions, shifts in the 75-year projection period, and recent economic trends.

What do the low-cost and high-cost projections show?

Under the high-cost scenario, the Social Security trust fund reserves would be depleted in 2029 instead of 2037. Under the low-cost scenario, Social Security is solvent through the 75-year projection period. The difference among estimates reflects the great uncertainty about what will happen in the future.

Table 3. Comparison of OASDI Projections in Trustees Reports 1993-2010

Year of Trustees Report	Year when cost exceeds tax revenue and remains higher through the end of the projection period	Year when trust fund reserves become fully drawn-down	Long-range actuarial deficit (expressed as a percent of taxable payroll)
1993	2025	2036	1.46
1994	2018	2029	2.13
1995	2013	2030	2.17
1996	2012	2029	2.19
1997	2012	2029	2.23
1998	2013	2032	2.19
1999	2014	2034	2.07
2000	2015	2037	1.89
2001	2016	2038	1.86
2002	2017	2041	1.87
2003	2018	2042	1.92
2004	2018	2042	1.89
2005	2017	2041	1.92
2006	2017	2040	2.02
2007	2017	2041	1.95
2008	2017	2041	1.70
2009	2016	2037	2.00
2010	2015	2037	1.92

Source: OASDI Trustees' Reports, specified years

Where does the Social Security surplus go?

By law, Social Security's surplus funds are invested in interest bearing securities that are backed by the full faith and credit of the United States government. Currently all trust fund assets are invested in special issue securities, largely U.S. Treasury bonds. These securities earn interest that is credited to the trust funds. The securities can be redeemed whenever needed to pay Social Security costs. In financial markets, Treasury securities (bills, notes and bonds) are considered a very safe investment because they are backed by the full faith and credit of the United States government.

The sum of all Treasury securities makes up the national debt. Most of the debt is held by (or owed to) the public – that is, individuals, corporations, and other investors in the United States and abroad who have loaned money to the government by investing in government securities. At the end of 2009, 20 percent of the national debt was owed to the Social Security trust funds; another 17 percent was held by other federal trust funds or accounts (U.S. Treasury 2010a; Tables FD-1 and 3).

Interest on the national debt is a legal obligation of the federal government. At the end of fiscal year 2009, total interest on the debt was $383 billion (U.S. Treasury 2010b). Some people worry when they hear that Social Security annual cash surpluses are loaned to the U.S. Treasury and the government spends the cash on other activities. This is not a misuse of Social Security funds. Regardless of how the government uses the cash, the

Treasury securities held by the trust funds are a binding legal commitment for the Treasury to redeem the securities with interest when the money is needed to pay Social Security benefits.

The Social Security surplus helps lower the debt owed to the public. When the rest of the government budget is in deficit, a Social Security annual cash surplus reduces the amount that the government would otherwise have to borrow from the public and in that way slows the growth in the debt held by the public. When the rest of the government budget is balanced or in surplus, a Social Security annual cash surplus results in a reduction of the debt owed to the public. In either case, slowing the growth of (or actually reducing) the debt owed to the public will make it easier to afford Social Security and other activities of government in the future.

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