

INFORMED BUDGETEER

SOCIAL SECURITY
A BAD DEAL FOR THE MIDDLE CLASS

- At a recent Senate Budget Committee hearing, Dr. Jagadeesh Gokhale of the Cleveland Federal Reserve gave a sobering account of Social Security’s outlook based on an analysis that he and his colleagues completed recently (“Social Security’s Treatment of Postwar Americans” by Steven Caldwell et al., in Tax Policy and the Economy, James Poterba ed., NBER, forthcoming).
- It is commonly assumed that it would take an immediate and permanent 2.2 percentage point increase in the payroll tax to ensure Social Security’s solvency. However, this is based on a limited 75 year horizon. If one wants to ensure solvency indefinitely, Gokhale noted that taxes would need to be raised by 4.7 percentage points, a 38 percent increase from present levels. Alternatively, benefits could be cut by 25 percent.
- Tax increases or benefit cuts would reduce the already meager rates of return that Social Security (SS) offers participants.

RATES OF RETURN			
Current Rules & Alternative OASI Policies; By Percent			
Birth Year	Current Rules	38% Tax Hike	25% Benefit Cut
1945-54	1.91	1.64	1.06
1955-64	1.77	1.27	0.92
1965-74	1.77	1.05	0.94
1975-84	1.86	0.97	1.03
1985-94	1.98	1.06	1.15
1995-2000	1.87	0.92	1.01

SOURCE: Caldwell et al.

- These returns are all far lower than the 3.5+ percent yield available on the 10-year Treasury Inflation Protected Securities (TIPS). This shows why Social Security is a poor deal for most post-war Americans.
- This latter conclusion can be shown in an even more vivid way. Using a more representative discount rate, Gokhale and his colleagues calculate an individual’s Lifetime Net-OASI Tax Rate (LNTR) by subtracting the “lifetime SS benefits received” from “lifetime SS taxes paid” and comparing this to “lifetime earnings”.
- They found that the middle class will pay more lifetime SS taxes than they will receive in benefits, meaning that SS is actually a net tax on the middle class. In fact, the average participant will pay 5 percent of her lifetime income to the government for which she will receive nothing in return.

LIFETIME NET-OASI TAX RATES				
Current Tax & Benefit Rules; By Percent; Lifetime Earnings				
Birth Year	Lowest 20%	Middle 20%	Highest 20%	All
1945-54	-5.7	5.7	5.0	5.2
1955-64	-4.4	5.8	5.0	5.2
1965-74	-3.5	5.9	5.2	5.5
1975-84	-4.0	5.7	5.2	5.4
1985-94	-3.5	5.5	5.1	5.4
1995-2000	-2.8	5.6	5.3	5.3

SOURCE: Caldwell et al.

- What does a lifetime net tax rate of 5.2 percent mean for today’s youth, on average? Under current rules, this is equivalent to saying that they will have to make a one-time tax payment to the government of \$270,000 upon retirement for which they will receive nothing in return. If one assumes that taxes are raised 38 percent to ensure SS’ long-run solvency, this one-time payment skyrockets to \$414,000.

LIFETIME NET-OASI TAX RATES			
Alternative OASI Policies; By Percent			
Birth Year	Current Rules	38% Tax Hike	25% Benefit Cut
1945-54	5.2	5.6	5.8
1955-64	5.2	6.1	5.8
1965-74	5.5	7.3	6.1
1975-84	5.4	8.3	6.1
1985-94	5.2	8.2	5.9
1995-2000	5.3	8.4	6.0

SOURCE: Caldwell et al.

- It is clear that Social Security faces even larger financing problems than commonly assumed and that it offers unattractive returns to future retirees. This bespeaks the need for Social Security reform which allows participants to control their own contributions and to earn higher rates of return — this would improve SS’ finances and ensure that Americans accumulate more pension resources under SS.

SOCIAL SECURITY’S PROJECTED SURPLUSES

- The President’s State of the Union address highlighted the need to revisit the size of SS’s surpluses and trust fund reserves over the next fifteen years. In his address he said he would transfer \$2.7 trillion of projected budget surpluses to the SS system. Big deal? Not exactly - that is the about the estimate of what will happen anyway!
- According to the 1998 Trustees’ Report, the surpluses and reserve estimates are as follows.

Social Security Trust Fund Surplus & Reserve Estimates			
(\$ in Billions)			
	Assumptions		
	Intermediate	Optimistic	Pessimistic
Assets end of:			
Calendar year 2000	978.1	1,002.8	950.6
Calendar year 2015	3,354.9	4,647.6	1,826.2
Cumulative Surplus:			
2000 to 2015	2,376.8	3,644.8	875.6

DOMENICI BUDGET PROCESS REFORMS

- On January 19th, Senator Domenici introduced two budget process reform bills. His first bill was S. 92, the Biennial Budgeting and Appropriations Act. This is the same bill he introduced in the last Congress.
- The second bill he introduced is a comprehensive budget process reform bill. Senator Domenici’s second bill is S. 93, the Budget Enforcement Act of 1999. S. 93 contains five titles and makes the following changes to the budget process (note that title I of S. 93 is identical to S. 92):

Title I: Biennial Budgeting and Appropriations (S. 92)

- Requires the President to submit a two-year budget at the beginning of the first session of a Congress and requires Congress to adopt a two-year budget resolution and enact 13 appropriations bills covering a two-year period during the first session of a Congress.
- Devotes the second session of a Congress to consideration of biennial authorization bills and oversight of federal programs and provides a majority point of order against authorization and revenue legislation that cover less than two years except those measures limited to temporary programs or activities lasting less than two years.
- Modifies the Government Performance and Results Act of 1993

(the Results Act) to incorporate the government performance planning and reporting process into the two-year budget cycle to enhance oversight of federal programs.

Title II: Emergency Spending Reforms

- Makes any emergency spending in any bill subject to a 60-vote point of order in the Senate. If this point of order is sustained against any emergency provision, the emergency spending would be extracted from the bill under a Byrd rule procedure.
- Provides a reporting requirement for the President and Congress to justify proposed emergency spending and to document whether proposed emergencies meet five criteria: necessary, sudden, urgent, unforeseen, and not permanent.
- Makes any non-emergency provision in an emergency supplemental appropriations bill subject to a 60-vote point of order in the Senate. If this point of order was sustained, the non-emergency provision would be extracted from the bill under a Byrd rule procedure.

Title III: Clarifying Changes to Pay-as-you-go

- Amends the Senate's 10-year pay-as-you-go rule to make clear that an on-budget surplus can be used to offset the cost of tax reductions or direct spending increases.
- Amends the statutory pay-go system (enforced by OMB) to make clear that an on-budget surplus can be used to offset the cost of tax reductions or direct spending increases.
- Amends the Byrd rule to allow revenue losing provisions in reconciliation bills to be made permanent as long as they do not cause an on-budget deficit in the future.

Title IV: Government Shutdown Prevention Act

- If appropriations bills are not enacted by the beginning of the fiscal year, provides for an automatic continuing resolution (CR) at the lower of the President's requested level or the previous year's appropriated level.

Title V: Streamlining the Budget Process

- Reduces time on a budget resolution from 50 to 30 hours (20 hours of which would be reserved for amendments).
- Reduces time on amendments from 2 hours to 1 hour and establish filing deadlines establishes filing deadlines (1st degree amendments must be filed by 15th hour; 2nd degree amendments must be filed by 20th hour).
- After all time expires, requires vote on any pending amendments and then final passage.
- Make sense of the Senate amendments on budget resolutions nongermane.
- Adopt same procedures for reconciliation bills.
- Simplifies the budget resolution to totals for major categories of spending instead of 20 individual functions.

QUOTE OF NOTE

(Worth Repeating From the August 3, 1998 Budget Bulletin)

“How will you ever convince the American people of that, since they always believe the government would mess up a two-car parade? I mean, even if you're right, politically, how do we ever -- how do you make that sale to the American people? “

President Clinton, discussing a proposal for the government to invest and manage Social Security funds; July 27, 1998, Albuquerque, New Mexico; The Great Social Security Debate #3.

CALENDAR

BUDGET COMMITTEE HEARING SCHEDULE

All hearings will be held in Dirksen 608 at 10:00 am unless otherwise noted. Additional hearings may be scheduled.

January 25: The National Defense Budget: Are We on the Right Course?; Witness include: Dr. James R. Schlesinger, Chairman, MITRE; Robert Zoellick, President, Center for Strategic International Studies; Dr. Lawrence Korb, Council on Foreign Relations.

January 27: Budget Process Reform; Witnesses on Panel 1: Senator John McCain; Witness on Panel II: Representatives Jim Nussle and Benjamin L. Cardin; Witness on Panel III: Timothy J. Muris, George Mason University Law School, Martha Philips, Executive Director. *Note hearing will be at 9:30am in SD 106.

January 28: The United States Long-Term Fiscal Outlook; Witness: The Honorable Alan Greenspan, Chairman, Board of Governors of the Federal Reserve System.

January 29: CBO Economic and Budget Outlook; Witness: Dr. June O'Neill, Director, Congressional Budget Office.

February 2: The President's Fiscal Year 2000 Budget Proposal; Witness: Jack Lew, Director, Office of Management and Budget.

February 3: The President's Fiscal Year 2000 Budget Proposal; Witness: Robert Rubin, Secretary, Department of the Treasury.

February 9: The President's Fiscal Year 2000 Budget Proposal; Witness: Madeline Albright, Secretary of State (tentative).


February 11: The President's Fiscal Year 2000 Budget Proposal; Witness: Health & Human Services Secretary Donna Shalala (tentative).


February 23: The President's Fiscal Year 2000 Budget Proposal; Witness: William Cohen, Secretary of Defense; General Henry H. Shelton, Chairman, Joint Chiefs of Staff (tentative).

KEY BUDGET DATES

January 28: Congressional Budget Office releases their 1999 Economic and Budget Outlook FY2000-200. Release at close of business.

February 1: President Clinton releases FY 2000 Budget Proposal. Senate Budget Committee releases Instant Analysis of President's FY 2000 Budget Proposal.

 **EDITOR'S NOTE:** A memorial service to honor Governor, Senator, and Chairman Lawton Chiles will be held at 11 a.m. January 28 in the Senate's Russell Caucus Room. Staff who wish to pay their respects are invited to attend. We would like to take this opportunity to express our respect for former Budget Committee Chairman (1987-1988), our deep sorrow at his passing and sympathies to his family.

 **Reminder:** SBC Testimony is available on our web site.