JOINT ECONOMIC COMMITTEE

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Challenges Facing Social Security

Social Security has a serious financial problem that will deteriorate if policymakers do not act to prevent it. While Social Security's income from payroll taxes currently exceeds its outgo in benefit payments, Social Security's trustees project that outgo will exceed income in 2017.[1]

Unless policymakers make significant changes, Social Security must then begin to draw down its trust fund to pay benefits. After 2017, the trustees project that the gap between benefit payments and payroll tax receipts will widen. By 2030, projected benefit payments will exceed projected payroll tax income by 27 percent.

The Social Security trust fund invests in U.S. Treasury debt securities. To use the trust fund to pay benefits, Social Security must redeem these bonds from the Treasury. In 2030, the trustees project that Social Security will draw $256 billion (in 2005 dollars) from the general fund. To meet the Treasury's obligations to Social Security, policymakers will confront three choices: (1) restrain the growth in other federal spending substantially, (2) increase federal taxes dramatically, or (3) run significantly larger federal budget deficits.

By 2041, the trustees project that Social Security will exhaust its trust fund. Over an infinite time horizon, the trustees project that Social Security's unfunded obligations are $11.1 trillion (in 2005 dollars).

Demographics drive Social Security's financial problem:

- Many more people are living long enough to collect retirement benefits. Policymakers in the 1930s assumed that relatively few people would reach age 65. By 2005, however, life expectancy at birth had increased to 74.8 years for a man and 79.6 years for a woman. The trustees project that the death rate will continue to decline by about 0.71 percent a year through 2079.[2]
- Once retired, people are collecting benefits for more years. The trustees project that either a man or woman who reaches age 65 in 2030 will live 1.5 years longer than either a man or a woman who reaches the same age in 2005.[3]
- The birth rate has declined. From a peak of 3.7 children per woman in 1957, the U.S. birth rate declined and then stabilized at about 2.0 children since

[1] Statistics are based on the intermediate cost scenario in *The 2005 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds*, found at http://www.ssa.gov/OACT/TR/TR05/tr05.pdf.

[2] Life expectancy at birth is based on period life expectancy. Period life expectancy is calculated for a given year using the actual or expected death rates at each age for that year. Thus, period life expectancy is closely related to the death rate.

[3] Life expectancy at age 65 is based on cohort life expectancy. Cohort life expectancy answers the question: "What is the expected average remaining lifetime for an individual at a selected age in a given year?" Cohort life expectancies are calculated using death rates not from a single year, but from the series of years in which the individual will actually reach each succeeding age if he or she survives.

1990. The trustees project that the birth rate will remain generally unchanged.

- Immigration is projected to fall. The trustees project that net immigration will decline from about 1.08 million in 2005 to 900,000 in 2025 and will remain unchanged thereafter.[4]
- People are retiring earlier. While people who retire before the normal retirement age receive lower benefits, the benefit reductions may not be large enough to be economically neutral. Thus, early retirement may increase the financial woes of Social Security.

Together these mostly demographic changes mean that fewer workers will be paying into Social Security, while more retirees will be drawing benefits for longer periods. In 1940, approximately 16 workers supported each beneficiary. In 2005, this ratio is 3.31 to 1. The trustees project that this ratio will fall to 2.17 to 1 in 2030.

Under current law, future retirees will draw higher real (inflation-adjusted) benefits than current retirees. For example, a worker who earned the average wage during his or her career and retired in 2005 at the normal retirement age will receive $15,335 (in 2005 dollars) a year in retirement benefits. A similar worker who retired in 2030 would receive 28 percent more in real benefits ($19,679 in 2005 dollars).

Because of demographics and scheduled increases in real retirement benefits, Social Security will consume an ever-increasing share of U.S. GDP. The trustees project that the cost of Social Security will increase from 4.26 of GDP in 2005 to 6.14 percent of GDP in 2030.

There is a widespread recognition that Social Security has a serious financial problem that will only grow worse unless policymakers decide to take corrective actions.

[4] Immigration includes both legal and illegal immigration.