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Commentary

THE BUFFIN FOUNDATION SOCIAL AND ECONOMIC DEVELOPMENT ISSUES

Social Security Solvency Strengthens Slightly

The United States Social Security system, formally known as Old-Age, Survivors and Disability Insurance (OASDI) is subject to a process of statutory annual reviews of its financial condition and submission of reports to Congress under the direction of its six appointed trustees. The recently released 2015 Social Security report of the trustees discloses some encouraging news regarding the system's solvency and sustainability. After a sequence of four years over which the key solvency metrics indicated a moderately negative trend, the 2015 report discloses a reversal of this trend and an extension of one year until 2034 for the future period for which the system meets the key 100% solvency test for payment of scheduled benefits. The report also indicates some improvements in the actuarial balance and the degree of solvency over future 25, 50 and 75-year projection periods. The change in the actuarial balance, compared with the previous year, represents an improvement of 0.20% of covered payroll with respect to the projected deficit over 75 years. According to the detailed analysis of this change presented in the trustees' report, there are five separate components of this 0.20% improvement in the level of the actuarial balance. Methodological improvements in projected benefits for newly entitled worker beneficiaries and other improvements and updates to methods and programmatic assumptions accounted for a gain of 0.17%. Economic data and assumptions, more specifically an increase in ultimate real wage differential, starting values and economic assumptions, accounted for a gain of 0.10%. The change in the 75-year period by one year to 2089 accounted for a loss of 0.06%. Changes in legislation, particularly relating to immigration, resulted in a gain of 0.02%. Changes in demographic data and assumptions, including lower than expected fertility, higher than expected mortality, and revised immigration data, produced a net loss of 0.03%. The solvency ratios for 25, 50 and 75 years are now projected to be 95%, 88% and 85% respectively, compared with corresponding values of 94%, 87% and 84% a year ago. On the basis of a more favorable low-cost scenario, the solvency ratios for 25, 50 and 75 years are 107%, 103% and 102% respectively. On the basis of a less favorable high-cost scenario, the solvency ratios for 25, 50 and 75 years are 84%, 75% and 70% respectively.

The reported value of the Social Security trust funds at the end of 2014 is 2.79 trillion dollars. During the calendar year 2014, the amount of the system's revenues exceeded disbursements by 25 billion dollars. Since the inception of OASDI in 1935, total revenues have amounted to 18 trillion dollars and disbursements for benefits and administration have amounted to 15 trillion dollars.

The accumulated surplus from operations is invested in US Treasury securities with maturities ranging up to fifteen years. Interest on these treasury securities is credited to the trust funds. The rates of interest on the securities held on December 31, 2014 ranged from 1.375% to 6.50%; the average rate earned on these securities in 2014 amounted to 3.6%.

Around the turn of this century, certain prominent politicians and advocates for reducing the amount of future scheduled social security benefits falsely proclaimed that Social Security was bankrupt. A Presidential Commission with the Orwellian Newspeak objective of "Strengthening Social Security" was in fact given a mandate to develop recommendations for converting part of the system to provide diversion of social security contributions into individual accounts that would not provide protection to individuals against investment market risk, consumer price inflation, or longevity risk. Fortunately, the recommendations of that Presidential Commission were never implemented. Instead advocates for the preservation of the existing system urged that greater emphasis be placed on achieving solvency and sustainability for the system. Reaching the goal of achieving full projected solvency of the system beyond 2034 is reasonably affordable. A simple adjustment in the payroll tax rate from its present level of 6.20% to approximately 7.18% would be sufficient to produce 100% solvency for the next fifty years. An adjustment to approximately 7.46% would be required to produce 100% solvency for the next 75 years. Alternatively, many other relatively minor parametric changes to the system could be implemented to achieve 100% solvency. One such parametric change would be to increase the ceiling on covered earnings that are subject to the social security payroll tax.

A better way to assess the economic cost of the Social Security system is in relation to the nation's gross domestic product (GDP). In comparison with most developed countries, the economic cost of the US Social Security system is relatively low. The long-term projection of this economic cost for the United States is around 6% of GDP, whereas for many developed countries, particularly in Europe, the cost of social security provision is significantly higher, often at around 10% of GDP.

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