a report from

2nd congressional district of Arizona

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Keeping Social Security Secure

Of all the social programs ever enacted, Social Security remains one of the best. It has worked well for millions of Americans. It has kept a bargain struck back in 1935, when the Social Security Act became law, to provide a small measure of economic security to Americans as they grow older.

Within the last two or three years, however, Social Security has faced the most serious threat ever. The program itself wasn't floundering. But the economy was, and Social Security took a pounding. A prolonged recession and high unemployment cut deeply into the payroll tax receipts that are used to finance Social Security. That was the short-term problem. But there was a long-term problem as well. We were told that an expanding older population would put heavier and heavier strains on the system in the years ahead. Young people began to wonder whether Social Security would be there when they retired.

Something had to be done. But what? Present-day recipients didn't want their benefits cut; many depended on their Social Security benefits to make rent or pay for groceries. Present-day contributors felt that they were already paying too much out of their paychecks, especially if Social Security wasn't going to be there when they retired. In the midst of this debate, some even talked about a "war between the generations." All in all, it was a tough issue. But some thing had to be done.

It is always tempting to duck the tough issues. But this one had to be faced. And it was. Congress and the Administration faced it squarely. In the process a lot of hard bargaining was done. At times it seemed like no agreement could be reached. But in the end an agreement was reached. A bipartisan commission made its recommendations. And with only minor changes, those recommendations were accepted by Congress and the President. The Social Security agreement is now law. It is not exactly the way I would have drafted it, but I support it.

Some Background

Before laying out those changes, let me offer a brief history of Social Security and set the record straight about some common misconceptions.

One popular misconception is that Social Security, alone, should provide enough income for retirees to live on. It is a myth, and one that has been perpetuated for years, and it simply is not so. Social Security, from the outset, was intended to supplement a worker's other retirement income, and nothing more. Last year, the average monthly retirement benefit was only $406. Many received less.

Social Security frequently is referred to as a secured trust fund. That's not exactly right. What it is, is a transfer account, and it works like this: Americans who are employed today see part of their salary or wages go to Social Security. And their employers kick in an equal share. That money doesn't go into an account with their name on it, although the government does keep track of how much everyone has paid into the system.

The money paid by those working Americans is soon, if not immediately, distributed to retired citizens -- just as their contributions during their working years went to the retirees of their generation.

Now and then, mail arrives on my desk from an irate taxpayer complaining that Washington has squandered the money he paid into Social Security and saying that's the cause for the whole mess. But Social Security payments are not kept in something resembling a savings account. They never have been. At any given time there is a net balance or "reserve" in the Social Security trust fund, but only an amount equal to several months of benefits. Money paid in today by workers soon goes out tomorrow to retirees.

In that sense, Social Security is less a "trust fund" and more a "trust agreement" between the generations. Until lately, at least, it has worked well. Forty-eight years ago, when the Social Security system was established, it was based on the best economic principles of the day: it would be financed by a gradually growing Gross National Product, an ever-increasing rate of productivity, and most importantly an expanding work force. If everything worked according to plan, there would always be enough payroll tax receipts to pay current beneficiaries.

So what happened?

In part what happened is that the economy faltered. It did not perform to the expectations of Social Security planners. And when that happens, it can pull apart the best intentions -- or predictions. Washington didn't squander Social Security, but high unemployment and shrinking payroll tax receipts undermined it badly.

When Congress in 1977 passed the last adjustments in Social Security payroll tax rates it was assumed that unemployment would decline to 5 percent by 1982. At the time, that seemed like a pretty good bet. That was about the average for the preceding ten years. But it didn't work out that way. Unemployment last year averaged nearly 10 percent. As unemployment rates rose, payroll tax receipts fell. In fact, they fell so far as to threaten the solvency of the system. We were told that, if we did nothing to correct the situation, benefits would have to be cut or benefit checks delayed by the summer of 1983.

But that wasn't the only problem. There was a longer-term problem as well. We were told that if the economy performed well the retirement fund would accumulate some reserves between the years 1990 and 2015. That's because the small "depression-era" generation will reach retirement during those years and the large "baby boom" generation will be reaching its peak earning years and helping to support the system. The good news, however, would turn into bad news between the years 2015 and 2050 when the baby boom generation reached retirement. The system would go in the red again.

At the present time, there are 116 million workers paying into the system and 36 million retirees drawing benefits. That's a ratio of 3-1. (When the Social Security system first started, the ratio was 12-1). But by early in the next century, the ratio of contributors to retirees is expected to fall to 2-1. That posed real problems. If the retirement age remained unchanged and benefit levels were maintained, payroll tax rates would have to be nearly doubled by the year 2015 in order to keep the system solvent. But no one expects that to happen. That's why some young people began to doubt whether Social Security would be there when they retired. Many asked, "Why should I pay Social Security taxes now, if the whole system is going to collapse by the time I retire?" The trust agreement" between the generations was about to fall apart.

That's why it was important that Congress act this year to solve both the short and the long-term financing problems. And I think we succeeded. It required a lot of compromise. And a lot of sacrifice. Everyone had to give up something. But I am happy to say that the package is a fair one. Not the fairest perhaps. But a fair one. Let me explain what Congress did to clear up the short and long-term problems and how the solutions affect you as a retiree or worker.

The Short-term

In addressing the short-term problem, Congress had to come up with $155 billion in "savings" to keep the system solvent through the year 1999. We did slightly better than that, we came up with $165 billion in prospective savings -- enough to provide a margin of safety in case our economic projections were too optimistic. Here's how we came up with the money:

Coverage:

Beginning Jan. 1, 1984, all new federal employees will be required to participate in Social Security, including Members of Congress, the President and Vice President and employees of the legislative and judicial branches of government. A supplemental, optional plan for new federal employees will also be available.

New Revenue: $9.4 billion.

Beginning Jan. 1, 1984, all employees of non-profit organizations will be required to participate in Social Security. A special provision allows those near retirement to be fully included in the Social Security program.

New Revenue: $12.5 billion.

State and local government employees will no longer be allowed to leave the Social Security system.

New Revenue: $3.2 billion.

Benefits:

There will be a 6-month delay in the June, 1983, Cost of Living Allowance (COLA) to December, 1983. Thereafter, COLAs will be paid annually in January.

Savings: $39.4 billion.

Revenue:

Beginning in 1984, Social Security benefits will be subject to federal individual income taxes. But benefits will be taxed only for recipients whose taxable income plus half of his Social Security benefits exceeds a base amount of $25,000 for an individual or $32,000 for a married couple filing jointly.

Added Revenue: $26.6 billion.

Tax Rate:

Increases in payroll tax rates already scheduled for 1985 and 1990 will be advanced. That means that the payroll taxes for Social Security retirement and disability will rise from 5.4 percent of taxable wages or salary to 5.7 percent next year and 6.06 percent by 1988.

Added Revenue: $39.4 billion.

Starting in 1984, tax rates for self-employed people will be equal to the combined employer-employee rate. To help offset this added cost of running your own business, the self-employed will be allowed an income tax credit against self-employment taxes.

Added Revenue: $18.8 billion.

Treasury

A one-time, lump sum payment from the general fund of the Treasury to Social Security will be made. This represents payment for Social Security wage credits granted to members of the armed forces and reimbursement for uncashed Social Security checks.

Added Revenue: $17.7 billion.

Together these steps should correct the short-term problems. The system won't go broke. But, of course, everyone had to give up something. Beneficiaries have to accept a six-month delay in the annual cost-of-living increase. Workers must pay a small increase in their payroll taxes. Members of Congress will have to pay into the system. And so will new federal employees. But Social Security will be preserved.

The Longer-term

While the recommendations of the bipartisan Commission on Social Security did not deal with the longer-term problem, Congress did. We thought it was important to settle the issue now, so that young people would not lose faith in the system. I personally thought it was important that we solve the long-term problems now, so that young workers could make their retirement plans accordingly. Here's what was done:

* Beginning with 1985, if the reserves in the Social Security Retirement and Disability funds fall below 15 percent of estimated annual payments, the cost-of-living adjustments that year would be based on the lower of the increase in consumer prices or the increase in wages.

* Between 1990 and 2010, credits for delaying retirement past the age of 65 will gradually be increased.
* The retirement age will gradually be increased to 67, between the years 2000 and 2027.
* Finally, the amendments include provisions for borrowing between the three trust funds, for revised accounting procedures that will allow Social Security to invest payroll tax revenues the same month they are received,

and a requirement that the trustees report back to Congress if the reserve in any trust fund is too small along with recommendations on how to remedy the situation.

These steps are expected to keep the Social Security system solvent through the year 2050. Here too, some hard choices had to be made. Some wanted to schedule sharp increase in payroll taxes instead of gradually raising the retirement age beginning in the year 2000. I thought the proposed increases in payroll taxes were unrealistic. I don't think the next generation of workers will want to pay payroll taxes of over 8 percent. I thought it was better to provide in advance for an increase in the retirement age.

Over the years, we have increased the payroll tax in order to keep the system solvent and preserve benefit levels. But since 1940 the life expectancy of Americans has increased by 12 years. That increase in longevity means that workers of tomorrow will spend a smaller part of their lives working and added years collecting benefits. Making further increases in a payroll tax which arguably feeds inflation and unemployment and weighs heavily on low-income workers seemed unfair and unwise.

Parting Thoughts

In addition to solving the financial problems of Social Security, th enew law also makes a prospective change in the "earnings test." Beginning in 1990, the earnings test for retirees will be liberalized. Instead of reducing benefits by $1 for every $2 of outside earnings above $6000 a year, they will be reduced only $1 for every $3 of out

side earnings. While this is a helpful change, I would like to see something done about it today, instead of 1990. The present law works an injustice on those retirees who need to earn outside income to make ends meet. If Social Security is designed as a supplemental retirement income, the law should not unduly penalize those who must work to supplement their Social Security retirement income.

One problem that was not dealt with in the recent law is the growing cost of Medicare and the financing of Medicare through the Health Insurance Trust Fund. Like the Social Security and Disability trust funds, the Hospital Insurance Trust Fund has run into financial difficulties in recent years. At the moment, there are plenty of reserves. But some changes will have to be made if we are to keep this system solvent. The National Advisory Council on Social Security is scheduled to report to Congress on this issue in July. I hope we can do something soon.

Finally, let me say a few words about the fairness of the recent Social Security package. In any compromise, there has to be honest give and take. And that's what was needed to reach agreement on Social Security. Everyone had to give something. Workers. Retirees. Old. Young. Federal employees. Employees of non-profit groups. But we all "take out" of this a Social Security system that is sound and truly "trustworthy."

I hope you will support the new law, I think it's a good one. More importantly, it's a vitally necessary one.

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