Statement of Robert D. Reischauer

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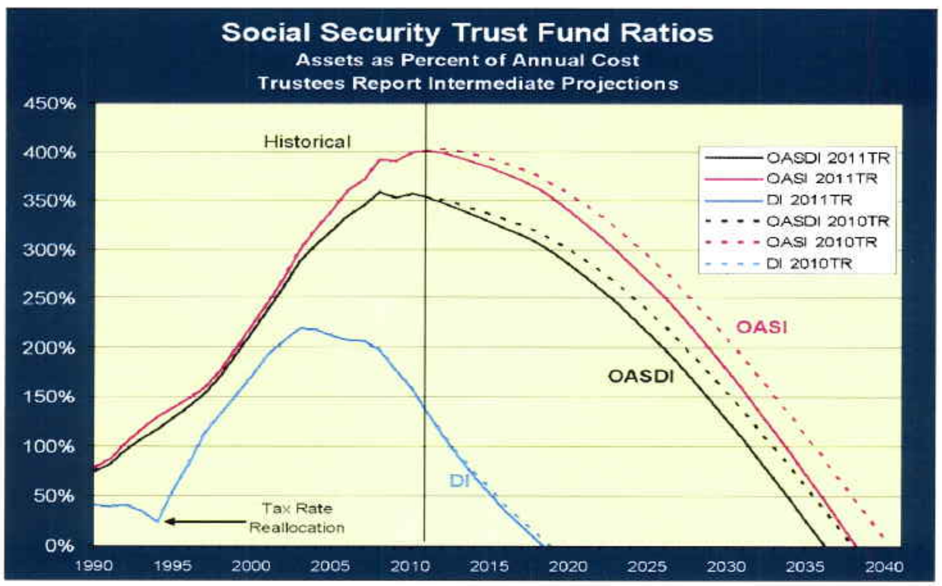
Subcommittee on Social Security, Committee on Ways and Means

U.S. House of Representatives

June 3, 2011

Chairman Johnson, Ranking Member Becerra, and members of the subcommittee, I appreciate this opportunity to discuss the 2011Social Security Trustees Report with you. So as not to repeat the points made by my fellow Public Trustee, Dr. Charles P. Blahous, who covered the basic operations and projected financing shortfall of the program, my statement focuses on the changes in the financial outlook from last year's report and the impact that a weak economy can have on this vital program. To illustrate my points, I have included in my statement several charts that were prepared by the Office of the Chief Actuary of the Social Security Administration.

The projections in the Trustees Reports of the financial health of the Social Security program change each year, sometimes by small amounts, sometimes by moderate amounts, and sometimes by large amounts. As an indicator of how significant the year-to-year changes are, the media and the public tend to focus on the changes in the dates at which the various trust funds are projected to be exhausted. By this measure, the changes between the 2010 and 2011 Reports of the Trustees are small, albeit in a negative direction. (See Chart) The exhaustion date of the OASI Trust Fund is now projected to be 2038, two years sooner than was projected in last year's report. The projected exhaustion date of the DI Trust Fund remains unchanged at 2018 and the combined OASDI Trust Fund exhaustion date, at 2036, is projected to come one year sooner than was projected last year.



[1] The views expressed in this statement should not be attributed to the Urban Institute, its sponsors, staff, or trustees.

A more comprehensive measure of a trust fund's financial condition is its actuarial balance over the 75-year valuation period. This balance is essentially the difference between annual income and costs, summarized over the 75-year projection period, and expressed as a percentage of taxable payroll.

An actuarial deficit can be interpreted as the percentage points that would have to be either added to the current-law income rate or subtracted from the cost rate for each of the next 75 years to bring the fund into actuarial balance. By definition, balance requires that the assets in the trust fund at the end of the 75th year equal the 76th year's cost.[2] While the actuarial balance of the DI Trust Fund, at -0.30 percent of taxable payroll, has not changed since last year's report, that for the OASI Trust Fund has deteriorated from -1.62 percent of taxable payroll to -1.92 percent of taxable payroll and that for the combined OASDI Trust Fund from -1.92 percent of taxable payroll to -2.22 percent of taxable payroll. (See Table) Along with an equal sized deterioration that occurred between the 2008 and 2009 Trustees Reports, this -0.30 percentage point change is the largest single-year deterioration in Social Security's actuarial balance since the 1994 Trustees Report.

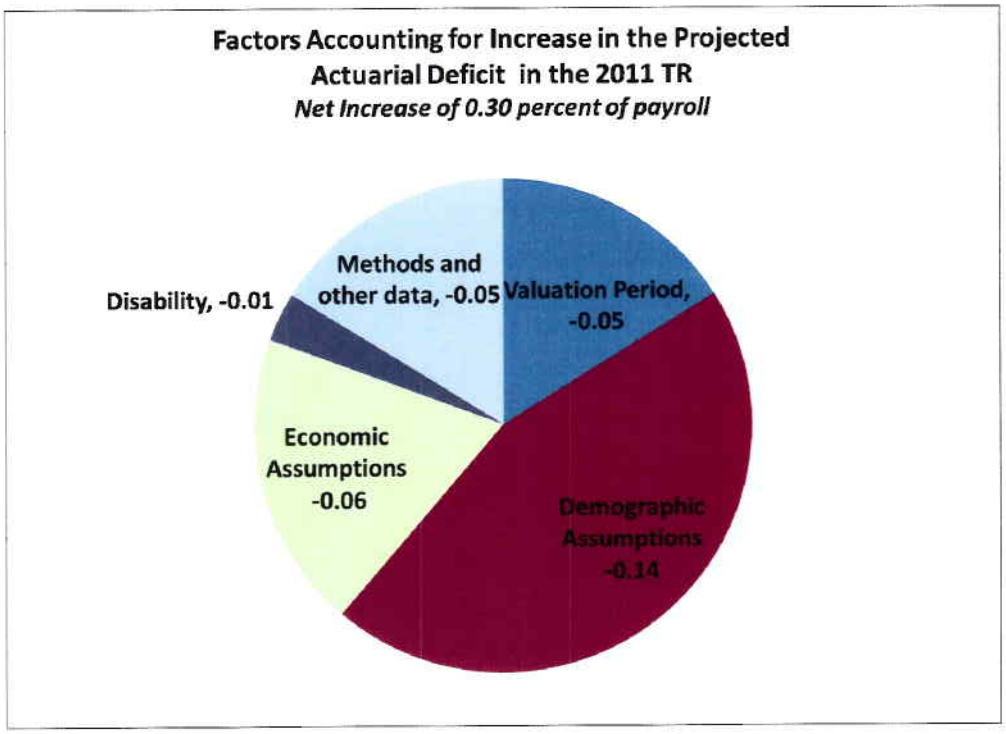
Long-Range Actuarial Deficit of the
OASI, DI, and OASDI Trust Funds
(percent of taxable payroll)

	OASI	DI	OASDI
2010 Trustees Report	-1.62	-0.30	-1.92
2011 Trustees Report	-1.92	-0.30	-2.22
Difference	-0.30	0.0	-0.30

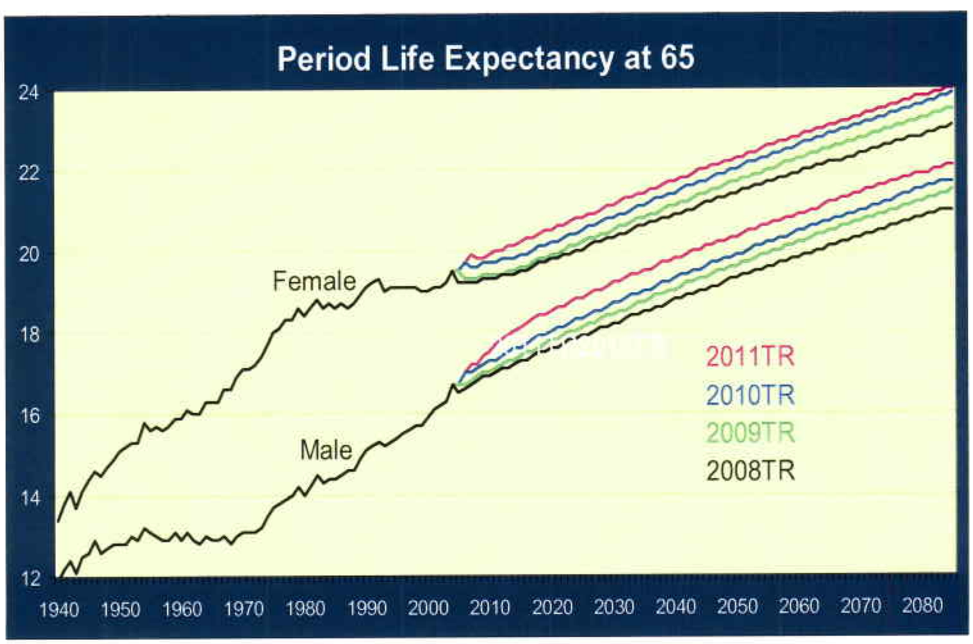
Year-to-year changes in Social Security's projected financial situation always occur because the valuation period is moved one year forward. Changes can also occur because new legislation is enacted, underlying economic and demographic assumptions are modified, administrative practices are revised, projection methodologies are refined, and new data becomes available.

The 75-year valuation period used in the 2011 Trustees Report (2011-2085) adds the year 2085 and drops 2010. This change from the previous report alone accounts for one sixth of the increase in the actuarial deficit. (See Chart)

[2] Because Social Security's annual deficits, expressed as the difference between the cost rate and income rate, are projected to increase gradually from 2015 to 2038, to decline slightly during the 2039-52 period and then to increase through 2085, the single tax rate increase for all years starting in 2011 sufficient to achieve actuarial balance would result in large annual surpluses early in the period followed by increasing deficits in later years. The relatively large deficits at the end of the 75-year projection period—equal to 4.24 percent of taxable payroll in 2085—indicate that sustained solvency would require payroll tax rate increases or benefit reductions (or both) by the end of the period that are substantially larger than those needed on average for the valuation period (2011-85).

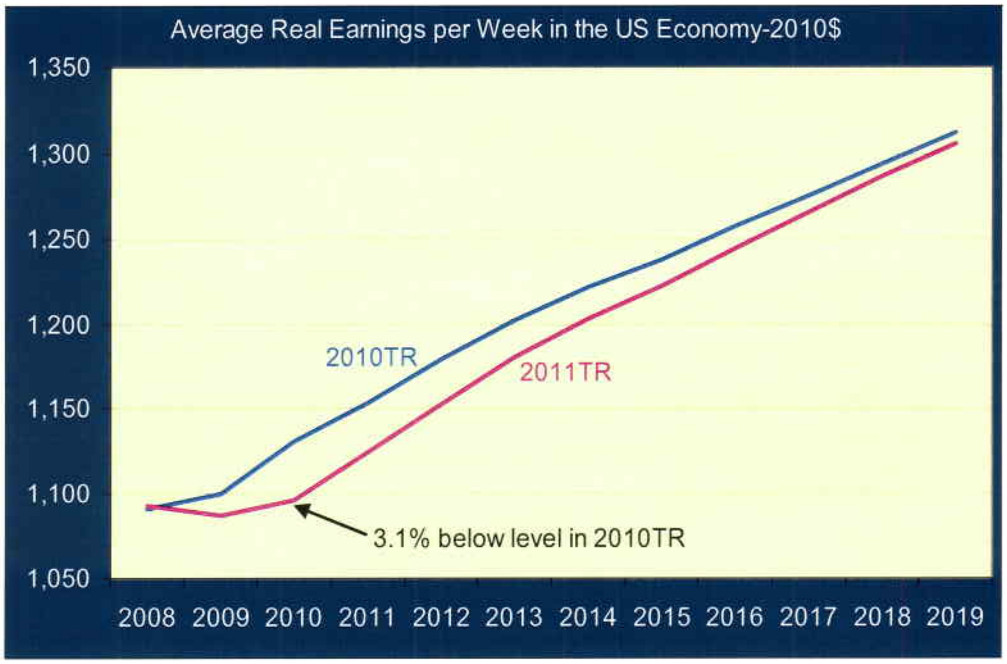


No legislation enacted during the past year significantly affected Social Security's long-range financial position. However, changes in the demographic and economic assumptions used for the 2011 Report did have significant impacts. Lower recent and projected mortality for those age 65 and older account for one third of the increase in the long-range actuarial deficit projected in the 2011 report. As the next chart shows, this bit of unabashed good news is not a new story since mortality improvements have been reflected in all of the recent Trustees Reports.



The recent and projected decline in net immigration of those other than legal immigrants, attributable largely to the recession and weak recovery, account for another one sixth of the deterioration in the long-run actuarial balance between the 2010 and 2011 reports.

When compared to the 2010 report, the 2011 report assumes a slower economic recovery, lower base-year real earnings and a slower return to the long-run average (See Chart), and lower real interest rates on trust fund assets that, together with other small changes in economic assumptions, account for a bit more than one sixth of the year-to-year deterioration in the projected actuarial balance.

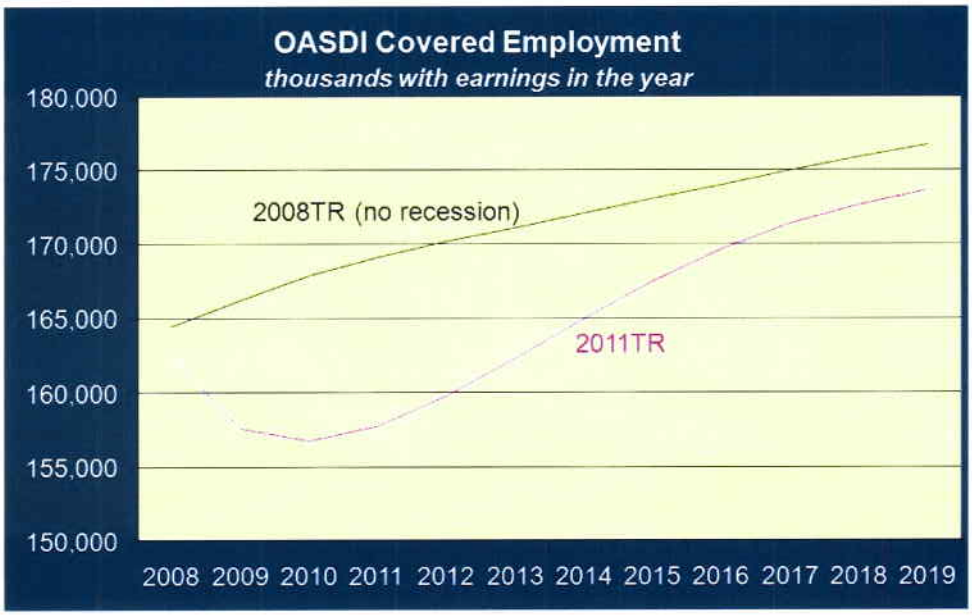


Numerous improvements in methods and data were introduced in the 2011 report and, on balance, they accounted for about one sixth of the increase in the projected long-run actuarial deficit.

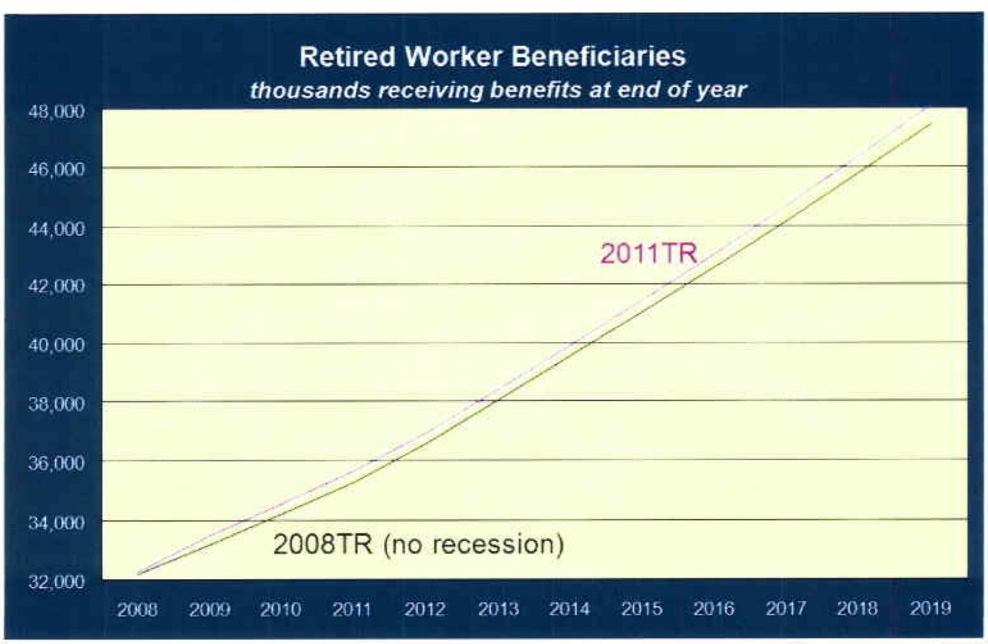
The previous discussion underscores how important a strong economy and healthy long-run growth rate are to the Social Security program. While much of the impact of temporary weakness in the economy is assumed to be offset over the long run, prolonged periods of weakness can affect the economy's potential, the productivity of the work force, and patterns of labor force participation even over decades.

Some insight into the magnitude of these effects can be gleaned by contrasting the projections contained in the last Trustees Report before the Great Recession with those of the 2011 Trustees Report which reflects the full depth of the December 2007-June 2009 downturn and subsequent weak recovery.

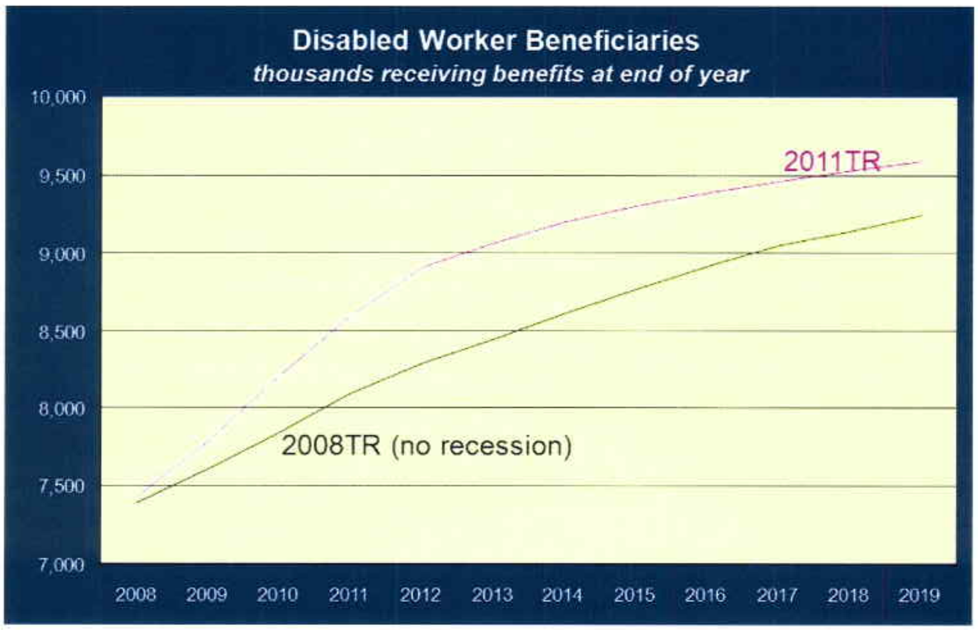
Today, there are well over 10 million fewer workers in covered employment contributing payroll taxes to the trust funds than was anticipated to be the case in the 2008 Trustees Report. Even by the end of the decade the shortfall will be several million under current projections.



While a number of factors have contributed to the increase in the number of retired worker beneficiaries projected in the 2008 versus the 2011 Trustees Report, the weak economy has been an important one. Faced with a weak labor market, some workers who have reached the age at which they are eligible for benefits and are laid off will decide to retire and draw benefits; others may supplement their diminished paychecks from part-time work or a lower-paying job with Social Security benefits.



The story is much the same for the workers with some level of disability. While they may be able to carry on in a job they have performed for a number of years, once laid off they face significant barriers to reemployment. Competing against many healthy and younger job seekers for the few available positions, more are likely to apply for DI benefits than would be the case in a stronger economy. While the disability rolls reflect a complex interplay of factors, the projected increase of half a million in the number of disabled worker beneficiaries in 2011 reflects, to a significant degree, the economic weakness that unfolded between the 2008 and 2011 Trustees Reports.



The fact that Social Security's financial viability is significantly affected by the strength of the overall economy in no way diminishes the undeniable fact that changes will have to made in currently scheduled benefits and payroll taxes if the program is to provide our children and grandchildren an adequate level of retirement security. The sooner we address this challenge, the less disruptive the changes will be. Those most adversely affected can be given the time they need to prepare, the burden can be more equitably shared across the generations, and the political animosity and public anxiety associated with the unavoidable changes can be moderated.