NATIONAL CENTER FOR POLICY ANALYSIS

Statement of

Pamela Villarreal

Senior Fellow

National Center for Policy Analysis

on the

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Ways and Means Committee

Social Security Subcommittee

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Mr. Chairman and members of the Subcommittee, I am Pamela Villarreal, a senior fellow at the National Center for Policy Analysis. We are a nonprofit, nonpartisan public policy research organization dedicated to developing and promoting private alternatives to government regulation and control, solving problems by relying on the strength of the competitive, entrepreneurial private sector. I welcome the opportunity to share my views about the 2012 Social Security Trustees Report.

Regrettably, the Social Security and Medicare Trustees reports have become reruns of years past, with the combined unfunded liabilities exceeding the capacity of the average American to understand – more than $63 trillion. Little is offered in the way of viable solutions to solve the looming financial catastrophe. In the 2012 report, actuaries estimated that the unfunded liabilities of Social Security are $20.5 trillion. At a minimum, the federal government should have that much in the bank today, earning interest, in order to fund the Social Security programs into the future. Alas, the trustees inform us that there is only $2.6 trillion in the Social Security Trust Fund, nowhere near enough to cover the promises Congress has made to future seniors.

By the way, the Social Security Trust Fund is nothing more than IOUs written to the Treasury while the money has been borrowed and spent on other programs. Technically, this money belongs in the net unfunded liability column, bringing the total unfunded liability into the infinite horizon to more than $23 trillion.

It almost goes without saying (yet nobody seems to be listening) that the current Social Security system is unsustainable because Congress has made promises without paying for them. So what are the options? The NCPA has examined five scenarios (the details can be accessed at http://www.ncpa.org/pdfs/st337.pdf) that should be of interest to the Subcommittee:

(1) **Retain current law benefits**. If Congress decides to continue with the current Social Security system, they should find a way to pay for it. According to NCPA research, an additional 3.2 percent would need to be added to the current 12.4 percent payroll tax to eliminate the unfunded obligation while retaining current law benefits. But a tax hike would have devastating effects on the fragile economy. Increasing taxes on labor (which is what the payroll tax is) during a tepid economic recovery and high unemployment is not advisable.

(2) **Progressive price indexing**. Moving to a price index instead of a wage index for those at the top of the taxable earnings distribution would reduce the unfunded obligation to $3.2 trillion and shrink the Social Security program to about 82 percent of its current size. This option would still require a 0.6 percent increase in the payroll tax, but would result in a more progressive program. Workers at the lower end (below the 30th percentile) would stay with the current wage-indexed formula.

(3) **Change the benefits formula**. Without raising taxes at all, Social Security benefits could be reduced, with the benefits of higher earning workers declining the most. To eliminate the unfunded obligations, overall Social Security benefits would need to shrink to about 77 percent of their current size.

(4) **Raise the retirement age**. If Congress increased the retirement age by one month every two years, the unfunded obligation would shrink to $6.3 trillion. This option would still require a 1.3 percent increase in the payroll tax to achieve solvency. This would result in a Social Security program about 87 percent of its current size. However, an across-the-board increase in retirement age would disproportionately harm low-income workers since the increase in average life-expectancy is largely due to gains made among high-income workers.

(5) **Eliminate the taxable maximum**. By eliminating the current $106,800 cap, the unfunded obligation would shrink to $8.3 trillion. Immediate revenues would be available for Congress to borrow and spend on other priorities, but this option would result in a larger Social Security program over time because of higher future benefits that would accrue in the absence of a cap.

In addition to the five scenarios above, the National Center for Policy Analysis has done substantial work in the area of private retirement accounts. This is a viable solution worthy of the Subcommittee's consideration. In brief:

(1) **Put a portion of payroll taxes in personal retirement accounts**. While temporary payroll tax reductions just increase future debts, diverting those taxes to fund retirement accounts would reduce future government liabilities.

(2) **Transition toward a funded system**. Allow workers and employers to set aside part of their payroll taxes and workers' wages in personal retirement accounts. As balances grow over time, they will replace the government's unfunded promises.

(3) **Wise investments**. Workers and employers who are uneasy about private accounts should not be left to themselves to invest their retirement funds. Instead, funds can be invested in approved, diversified funds managed according to strict accounting and financial standards.

(4) **Reducing risk**. Everyone age 55 or older should receive all promised Social Security benefits. Younger workers could be guaranteed a minimum benefit level. If any qualifying worker's total benefit falls below the minimum, the federal government should supplement it.

There is much more at the NCPA.org website about private accounts and retirement reform. I appreciate the opportunity to submit my views on this important question and I offer any assistance I might give to help solve this significant public policy problem.