Social Security Reform: What Would FDR Do?

BY SYLVESTER J. SCHIEBER

In recent months, Jack Lew, director of the White House Office of Management and Budget, and Senate Majority Leader Harry Reid have asserted that Social Security is not part of the federal budget problem. The federal government’s biggest program, they say, has ample resources to cover legislated benefits over the next 25 years. Therefore, lawmakers need be in no hurry to tackle Social Security’s long-term funding gap.

As a long-time analyst of U.S. retirement policy, I believe these claims are fatally flawed. In fact, Social Security’s financing costs already are adding to the federal government’s overall debt burden. Moreover, the longer we wait to rebalance the program, the higher the economic and political costs of the adjustments that must be made.

From a progressive perspective, I find it disconcerting that, instead of strengthening Social Security for future generations, leading Democrats are instead finding excuses not to deal with the system’s real but quite manageable fiscal gap. Having studied and written about Social Security’s history, I can’t help but compare such evasions with the rigorous sense of fiscal responsibility and intergenerational justice shown by the system’s creator, Franklin D. Roosevelt.

As they debate where Social Security reform fits in a comprehensive fiscal reform package, U.S. policy makers could do worse than ask themselves, what would FDR do? The historical record is clear: Roosevelt refused to embrace a funding scheme for Social Security that would result in large deficits that future generations of workers would have to close. Should contemporary progressives be any less scrupulous in rejecting political expediency and defending the principle of intergenerational equity?

Some Basic Facts
In 2010, Social Security’s official revenues, including interest, equaled $781.1 billion and total spending was $712.5 billion, so the system’s
bookkeeping net surplus was $68.6 billion. The interest is paid on bonds held by Social Security’s trust fund – essentially IOUs for money the U.S. Treasury has borrowed from the system in previous years when it raised more in revenue than it paid out in benefits. In a unified federal budget, however, interest paid on bonds is considered income to Social Security as well as an expense for government; the two exactly offset each other.

Leaving out interest payments, Social Security’s net income equaled $663.7 billion, falling short of expenditures by $48.9 billion. Since the federal budget was in deficit, Social Security added to the deficit by exactly that amount, and is expected to make increasingly larger claims for the foreseeable future as the baby boomers retire. The trust fund’s IOUs, as long as they last, represent a lawful claim on the federal government’s resources to meet Social Security payment obligations. As any OMB chief must surely recognize, continuing to cash trust fund bonds while the overall federal budget is in deficit will add to those deficits under budgetary accounting rules.

Social Security’s actuaries project that the trust fund will be depleted in 2037 under current law; CBO analysts project the date as 2039. All policy analysts accept these dates as the time frame over which the program could operate without having to modify current law. Virtually everyone also agrees that, if no changes are made in Social Security before the trust fund runs dry, benefits at that time will have to be reduced between 20 and 25 percent immediately for all contemporary beneficiaries.

An abrupt cut of that magnitude, of course, would impose drastic economic hardships on retirees and trigger a fierce political backlash. Not to worry, says Dean Baker, co-director of the Center for Economic and Policy Research (CEPR) a research arm of the AFL-CIO:

“If a shortfall really was imminent, it is likely that Congress would make the necessary adjustments to keep the program paying full benefits. This is exactly what happened in 1982-83, when the program literally did run out of money. Congress took steps to ensure that benefits were paid each month... Adjustments of the size put in place in 1983 could keep Social Security fully solvent into the 22nd century even if we waited until 2030 to act.” ¹

Baker may be right but he glosses over some big ramifications of his proposal. One is that Congress “fixed” Social Security in 1982 mainly by raising payroll taxes and expanding the number of workers covered by the program. Lawmakers did not slash benefits, though they did very gradually raise the “normal retirement age” to 67. Between 1980 and 1990, the combined income rates for Social Security programs rose from 10.2 percent of covered payroll to 12.7 percent, an increase of nearly 25 percent. These
big tax hikes help to explain why most working Americans pay more in payroll taxes than they pay in income taxes.

Raising the cap on earnings subject to the payroll tax – an expedient many liberals call for today – shifted the tax burden slightly more onto workers with higher earnings but the effect was modest. There are a number of proposals today to increase the cap on covered earnings to 90 percent of all earned income—the high water mark of earnings taxation under the program. President Obama’s Fiscal Commission endorsed this step, but it would only solve about one-third of the projected financing shortfalls. Taxing earnings above 90 percent would change the fundamental character of the program, and there is no serious proposal to do so.

Almost certainly, the further tax increases that Baker promotes and that Budget Director Lew and Senator Reid have implicitly endorsed will fall to a considerable extent on rank-and-file workers. Given today’s dire budget projections, there is little prospect of finding spare cash from new revenue streams to pay the bill. If we simply sit on our hands until the 2030s and then raise the payroll tax to cover the financing shortfall, we face the prospect of a rapid increase in the payroll tax of about 3.5 percent of covered pay—about 40 percent more than the 1980s boost.

A progressive alternative to hiking taxes on working Americans is moderately slowing the future growth in Social Security benefits for affluent retirees. Many people do not realize that the purchasing power of benefits for each subsequent wave of Social Security beneficiaries tends to rise over time under current law. For example, the average purchasing power of the monthly benefit for a worker retiring with average lifetime earnings in 2030 should be worth 15 percent more in today’s dollars than for a similar worker retiring today. By 2050, the benefit will climb to at least 45 percent more than the value for a worker retiring now.

Between 2010 and 2050, under current law, a worker who Social Security’s actuaries consider a “low earner” ($19,400 in 2010) retiring at normal retirement age will see his or her monthly benefits grow $407 per month in 2010 purchasing power. A “medium earner” ($43,100 in 2010) will see the monthly benefit grow $671 per month. A “maximum earner” ($106,800 in 2010) will see purchasing power growth of $1,151 per month. Trimming that growth for high earners, who are less dependent on Social Security for their retirement income, would substantially close the system’s funding gap. Many liberals oppose such adjustments on the grounds they pose some sort of ideological or philosophical threat to the fundamental commitment to income security for our retirees. Yet Social Security’s benefit structure has always been progressive; reducing future benefit growth for the wealthy would make it a bit more so. And the alternative – punishing tax hikes on working families – is distinctly unprogressive.
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Moderate increases in the retirement age to match gains in longevity would be another pragmatic way to address Social Security’s funding gap. In the early 1950s, the average claiming age for Social Security benefits was 68 and retirees received benefits over a remaining life expectancy of about 13 years. Between 2000 and 2005, the average claiming age was 62.5 and new beneficiaries were expected to be on the rolls an average of 21 years. There is every reason to believe that the long trend toward greater life expectancy will continue into the future. In 1983, that is exactly what Congressman Jake Pickle (D-TX), then Chairman of the Social Security Subcommittee of the House Ways and Means Committee, saw happening. He insisted on a gradual increase in the retirement age to moderate the effects of improving longevity on benefit costs. At the time, no one accused him of striking at the philosophical heart of Social Security. Yet many Democrats today adamantly refuse to consider this step, despite its endorsement by the President’s Fiscal Commission.

Whatever combination of tax hikes and spending cuts proves to be the most politically feasible, basic fairness demands that the work of reform must begin now. The reason is simple: Putting off closing Social Security’s fiscal gap is tantamount to leaving a bill for our children and grandchildren that we are not willing to pay ourselves.

What Would FDR Do?

There are 45 to 50 specific proposals to address Social Security’s financing shortfalls already published on the system actuaries’ web site that would resolve the funding problems. Some were developed by Democrats, some by Republicans and some jointly. In short, we already know the range of viable reform options and their varying political implications, but in refusing to embrace any of them, we seem to have lost the moral underpinning on which President Franklin Roosevelt based his original proposal for this vital program.

In the early 1930s, Roosevelt openly criticized and opposed two popular national retirement plan proposals because they included financing that would create significant future liabilities for taxpayers and the federal government. In early 1935, as FDR reviewed the initial draft of the legislative package which established Social Security, he discovered the plan would result in projected cash deficits beyond 1960 and that the system would require outside funding beyond the payroll tax by 1980. He felt that it would be “dishonest” to set up a program that would create burdens for future congresses and presidential administrations to deal with, burdens that would limit their ability to manage the government’s fiscal operations or other obligations. He understood the fundamental truth of any publicly-financed, universal retirement system: the government’s costs ultimately would have to be borne by workers. FDR therefore demanded that his own administration’s Social Security proposal be altered so the program would
be fully financed through the end of the projection period, then 1980, and be balanced at that time.

Juxtapose, if you will, our current situation with what FDR faced in 1935. He considered as “immoral” the prospect of Social Security running a cash shortfall some 25 years in the future and being unable to meet full benefit obligations some 35 years in the future. Today, we are already running a cash flow deficit in Social Security. We know to a certainty that we will be unable to meet full benefit obligations in about 25 years, and yet we seem resolved only to sit on our hands.

Given the strong sentiments about Social Security solvency that he expressed in 1935 and subsequently until his death, there’s little doubt FDR would be encouraging Democrats and progressives to fix Social Security now.

*Sylvester J. Schieber is the former chair of the Social Security Advisory Board.*


2 Actuarial analysis and opinion letter from Stephen C. Goss to Erskine Bowles and Alan Simpson, Co-chairs, National Commission on Fiscal Responsibility and Reform (December 1, 2010), Table 1B, found at: [http://www.ssa.gov/OACT/solvency/index.html](http://www.ssa.gov/OACT/solvency/index.html)


4 See: [http://www.socialsecurity.gov/OACT/solvency/index.html](http://www.socialsecurity.gov/OACT/solvency/index.html).
