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FUTURE DIRECTIONS IN SOCIAL SECURITY
UNRESOLVED ISSUES: AN INTERIM
STAFF REPORT

PREPARED FOR THE
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(Prepared by Dorothy McCamman, Consultant)

PREFACE

Social Security, which will celebrate the 40th anniversary of enactment in 1975, has become an ingrained feature of the American scene.

Close to \$5 billion is paid each month to more than 30 million persons for retirement, disability, or death benefits.

Approximately 21 million beneficiaries are elderly.

But other recipients are youngsters deprived of a parent, as well as disabled persons of all ages.

In one form or another, Social Security touches the lives of almost every American family.

Nearly 31 million persons—one out of every seven Americans—receive retirement, disability, or survivor benefits. Approximately 100 million workers now contribute to Social Security. And they are building protection for themselves and their dependents.

More than 90 percent of all persons 65 or older are eligible for Social Security payments. About 80 percent of all men and women in the 21 to 64 age category are protected in the event a family breadwinner suffers a long-term disability. And 95 percent of all mothers and dependent children are eligible for benefits if the father in the family dies.

In a very real sense, Social Security is family security. It is also the economic mainstay for the vast majority of older Americans. Social Security represents over half of the income for two-thirds of aged single beneficiaries and one-half of elderly couple beneficiaries. And it accounts for almost the entire source of support—90 percent or more of total income—for 30 percent of single elderly beneficiaries and 15 percent of older couples.

Huge computers and tens of thousands of employees are needed for the Social Security Administration to do its job.

In many small and even medium-sized communities, monthly Social Security checks constitute the largest single source of income.

Clearly, the Old Age, Survivors, Disability and Health Insurance (OASDHI) program—commonly known in all its parts as Social Security—must, of necessity deal in huge numbers and must aim for clean efficiency of operation.

But for all its bigness, OASDHI must also retain one of its most precious assets: the confidence of individual persons who, by paying into the system during their working years, are *entitled* to the many protections offered by the system.

It's not enough for the checks to arrive on time—a common dole could do that.

The people of the United States must also believe—as they have, overwhelmingly, for nearly four decades—that Social Security is *their* program, based on *their* earnings, attuned to *their* changing circumstances.

To a large degree, Social Security has made that belief not only valid, but deeply ingrained. It has the trust of the public; it adjusts, even while fundamental values and concepts remain fixed.

Confidence, however, is best maintained when its underpinnings are examined fairly frequently and sometimes skeptically.

As Chairman of the Senate Special Committee on Aging, I began hearings on "Future Directions in Social Security" in January 1973.

At that time, I said:

Our goal is to take a reflective look—at a time when legislative units of the Congress have completed work on historic Social Security legislation—at the significance of recent accomplishment as well as actions that must ultimately be taken to build upon that accomplishment.

The "significant accomplishment" to which I referred included:

A 20 percent across-the-board increase in Social Security benefits enacted in 1972.

Authorization of an automatic cost-of-living adjustment mechanism to keep Social Security benefits current with upswings in prices.

Approval of a federalized assistance program for the aged, blind, and disabled—the Supplemental Security Income program, or SSI, as it became known.

Despite these and other improvements the "Future Directions" hearings were deemed necessary in order to deal with issues that must be resolved if the generally favorable impression of Social Security is to be maintained, and if the program is to remain viable and responsive to changing conditions.

Thanks to fine testimony by persons thoroughly familiar with Social Security, the "Future Directions" hearing transcripts have become source books for information and ideas about OASDHI, present and future.

For the serious student of OASDHI, the transcripts are well worth intensive study.

For others who are concerned about Social Security but need a more concise reference, the Senate Committee on Aging offers this interim report.

Dorothy McCamman, who provided invaluable leadership during the Committee's "Economics of Aging" study in the late 1960's, has played a major role in the "Future Directions" study. As the author of the first half of this report, she summarizes testimony received thus far on:

Social Security financing, including discussion of the impact of payroll contributions on low- and middle-income workers.

Suitability of the means by which automatic increases in benefits are determined.

Shortcomings or anomalies in present coverage.

The need for an independent Social Security Administration.¹

¹On January 27, 1975, Senator Church introduced S. 388, the Social Security Administration Act. S. 388 would (1) establish the Social Security Administration as an autonomous agency outside the Department of Health, Education, and Welfare and place it under the direction of a three-member governing board appointed by the President with the advice and consent of the Senate; (2) prohibit the mailing of notices with Social Security and Supplemental Security Income checks which make any reference whatsoever to elected Federal officials; and (3) separate the transactions of the Social Security trust funds from the unified budget. Cosponsors of S. 388 include Senators Clark, Humphrey, Kennedy, Biden, Ribicoff, Williams, Hart (Michigan), Burdick, Tunney, Huddleston, Hatfield, Schwelker, and Jackson.

Throughout the hearings, there has been strong support for the introduction of general revenue financing, but only if it does not weaken the contributory principle and only for well-selected, limited, and measurable purposes. Long-range forecasts about the future of the Social Security financing structure, made early in 1975, suggest a clear need for judicious use of general revenues, *but only when absolutely needed and only for clearcut objectives.*

At forthcoming hearings, the Committee will consider such topics as: Improving SSI, treatment of women and minorities, long- and short-range projections of payroll contributions during periods of demographic change, overall "adequacy" of Social Security payments and relationships with private pensions, and issues related to mandatory retirement.

Obviously, a report now being readied for publication by the statutory Social Security Advisory Council will receive careful attention, as will an actuarial report released by the Senate Committee on Finance on February 10. The Finance Committee report has made it clear, in my view, that extensive changes must be made in financing the Social Security system, but that there is no real reason to rush into such changes. We seem to have time to weigh possible courses of fairly immediate action. From advance appraisals of the Advisory Council's likely findings, a generally similar conclusion seems likely to emerge from that body, as well.

Therefore, the "Future Directions" hearings will continue as they have in the past, unhurried and comprehensive. There will, however, be new emphasis upon the impact of inflationary pressures upon the Social Security system, particularly when inflation is accompanied by recession.

We will continue to recognize the enduring strengths of Social Security, even while we attempt to deal with its deficiencies.

PART 2: THE WHITE PAPER

For that reason, the Committee is particularly fortunate that within recent weeks, five former Health, Education, and Welfare Secretaries and three former Social Security Commissioners joined in endorsing a "White Paper" called: *Social Security: A Sound and Durable Institution of Great Value.*

The signers of the paper include Elliot L. Richardson, John W. Gardner, Wilbur J. Cohen, Robert Finch, and Arthur Flemming—all former H.E.W. Secretaries—and all three surviving former Social Security Commissioners, Robert M. Ball, William L. Mitchell, and Charles I. Schottland.

Their action was prompted by a rash of recent newspaper and magazine articles which cast doubt on the soundness and durability of Social Security. (One such series, I might add, appeared in my own daily newspaper in Idaho. I personally found the stories to be inaccurate and alarming; I was pleased when the same newspaper ran an article soon afterward challenging the earlier allegations.)

But even if there had been no attacks on Social Security, the White Paper would have been worthwhile because it provides an expert appraisal of Social Security's place in our society. In addition, it offers valuable insights into future financing and concludes that there will

be sufficient time to deal with the long-run change in the ratio of retired people to active workers.

In addition, the White Paper deals with the Congressional compact made with the people of this Nation on continuance and assurance of future benefit payments. It tells why Social Security is social *insurance*, rather than welfare.

In short, it is worth careful attention, by every citizen, young or old. It is reprinted as Part 2 of this report for study and for reference during future national debates on matters of concern to each and every one of us.

FRANK CHURCH, *Chairman.*

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FUTURE DIRECTIONS IN SOCIAL SECURITY UNRESOLVED ISSUES: AN INTERIM STAFF REPORT

(By Dorothy McCamman, Consultant)

PART 1

INTRODUCTION

When Senator Frank Church, chairman of the Senate Special Committee on Aging, announced on September 13, 1972, that the committee would hold hearings on "Future Directions in Social Security," he said in part:

It is clear, I think, that we in this Nation can no longer rely on catch-up benefit raises or even an automatic cost-of-living adjustment mechanism.

We have to grapple with other issues:

How can we make the payroll tax less onerous for so many workers?

What more can be done—besides adjusting the Social Security "retirement test"—to deal with one of the biggest complaints now made by the elderly—the feeling that they are being forced to give up work when they reach retirement age?

How can we make retirement more secure for women?

How can we deal fairly with elderly members of minority groups, so many of whom do not live to age 65?

Should general revenues be used for specific, limited purposes?

Five hearings held in Washington, D.C., in 1973, heard testimony from the following witnesses:

January 15, 1973, Robert M. Ball, Commissioner of Social Security.

January 22, 1973, Nelson H. Cruikshank, president, National Council of Senior Citizens.

January 23, 1973, John A. Brittain, the Brookings Institution; J. Douglas Brown, provost and dean of the faculty, emeritus, Princeton University; William L. Mitchell, former Commissioner, Social Security Administration, and consultant to National Retired Teachers Association-American Association of Retired Persons.

July 25, 1973, Wilbur J. Cohen, cochairman, Institute of Gerontology, University of Michigan-Wayne State University; dean, school of education, the University of Michigan; and Secretary of Health, Education, and Welfare, 1968-69, Max Manes, chairman of Seniors for Adequate Social Security, New York, New York.

July 26, 1973, Cyril Brickfield, legislative counsel, National Retired Teachers Association and the American Association of Retired Persons, accompanied by Hon. John Martin, consultant, and former U.S. Commissioner on Aging; James Hacking, legislative representative; Hon. William Mitchell, consultant, and former Social Security Commissioner; Peter W. Hughes, legislative representative; and Tom Borzilleri, economic consultant. Bar-

(1)

bara F. Marks, acting directing attorney, National Senior Citizens' Law Center; accompanied by Richard Michael Dull, attorney.

An opportunity to hear the views of senior citizens, many of them representing local programs or national organizations, was provided by a hearing in Twin Falls, Idaho, on May 16, 1974.

The records of these hearings, published in six parts, also include numerous statements and letters from concerned organizations and individuals.¹

Also in the series of hearings on "Future Directions in Social Security"—but not included in this Interim Report—were two that focused on the new Supplemental Security Income program. These hearings were held in Washington, D.C., on July 15 and 16, 1974. (Parts 7 and 8.)

The Interim Report has a dual purpose: (1) to summarize the unresolved issues in our Social Security program that were identified by the witnesses, along with their suggestions for improvement, and (2) to delineate areas that need detailed attention through future hearings.

The Interim Report concentrates on the cash benefits of the OASDI system, largely ignoring the health benefits of Medicare. This is not because the committee is unaware of the essential importance of health protection to economic security. Indeed, the committee agrees wholeheartedly with the finding of the 1971 White House Conference on Aging that "This Nation can never attain a reasonable goal of income security so long as heavy and unpredictable health costs threaten incomes of the aged." Medicare and Medicaid, however, have been the subject of intensive scrutiny by the Subcommittee on Health of the Elderly, which will continue to concern itself with an evolving program of national health insurance.

The new program of Supplemental Security Income is considered only in relation to its effect on OASDI, not with respect to the program itself. Here, too, the committee is holding intensive hearings on the adequacy of SSI payments and the operation of the assistance program.

The records of the six hearings are thus broader in scope than this Interim Report.

FINANCING

Unquestionably, the witnesses consider that the major unresolved issue in future directions in Social Security is the financing of the system.

While the most recent benefit increase has been achieved without an increase in the overall contribution rate, there is no doubt that the payroll tax already places a heavy burden on workers with low or modest wages. Furthermore, new long-range forecasts released in June 1974, significantly change previous projections and indicate that after

¹ "Future Directions in Social Security," hearings before the Special Committee on Aging, United States Senate, 93d Congress:

Part 1. Washington, D.C., January 15, 1973 (pages 1-94).
 Part 2. Washington, D.C., January 22, 1973 (pages 95-164).
 Part 3. Washington, D.C., January 23, 1973 (pages 165-235).
 Part 4. Washington, D.C., July 25, 1973 (pages 237-283).
 Part 5. Washington, D.C., July 26, 1973 (pages 285-469).
 Part 6. Twin Falls, Idaho, May 16, 1974 (pages 471-531).

10 years there will likely be a need for an 0.5 percentage-point increase in the current tax rate of 5.85 percent.² At the time of the Senate committee hearings in Washington, projections then available permitted the assumption that the current tax rate for cash benefits was sufficient to finance payments—including increases related to the cost of living and higher earnings—up to the year 2011.³ The question of financing of the system has thus become even more acute than when these hearings were held.

The payroll tax—when considered without relation to benefits—is unquestionably regressive. One witness, concerned primarily with the regressivity of the payroll tax, suggested that the ultimate goal be the financing of the system exclusively through general revenues. Recognizing that full replacement of the payroll tax by the income tax “would require an increase in income tax yield on the order of 50 percent” which would be difficult to put through the legislative process, the witness also suggested a more modest internal reform of the payroll tax structure “by means of exemptions and deductions from pooled earnings identical to those under the income tax.”⁴

But to consider the contributions without regard to benefits was analogous, said the witness who followed him, to the research of a panel of aerodynamicists who found that “the wings of a bumblebee provided insufficient lift to support the bumblebee in flight.”

As with bumblebees, so with many social institutions, if they are dissected into their separate parts, those parts appear to a specialist to be ill-designed and unworkable. But through long evolution as integrated entities, the institutions have gained a mysterious capacity to survive and function effectively.

* * * * *

Contributions and benefits in social insurance are not separable entities, artificially stuck together, but are, rather, inseparable, interlocking elements in a single concept. Without this interlock, you end up with a program of doles financed by general taxation.⁵

Overwhelmingly, the testimony favored preservation of the contributory principle of Social Security, with benefits as an earned right. How then can principles that have such widespread acceptance be preserved at the same time that the burden of payroll taxes is lowered, especially for those with relatively low earnings? And specifically, how can general revenues share in the costs of the system, with the share of financing and the level of benefits predetermined rather than left to the action of each Congress? Following are some of the proposals.

General revenues equivalent to prior service credits. Nelson H. Cruikshank, president of the National Council of Senior Citizens, advocated use of general revenues to finance the benefit costs equivalent to prior service credits—that is, the cost of paying full benefits to workers who are so close to retirement when first covered that contributions paid by them and by their employers finance only a portion of the benefit. Mr. Cruikshank reaffirmed the position stated in an earlier report he prepared for the committee:

I went on to say in the report I prepared for this committee 3 years ago, “There is sound justification for financing through general revenues that part of

² See Appendix 1, pp. 25–29.

³ *Ibid.*, Part 1, p. 34, Robert M. Ball.

⁴ *Ibid.*, Part 3, pp. 178–9, John A. Brittain.

⁵ *Ibid.*, Part 3, pp. 188–9, J. Douglas Brown.

Social Security costs which is equivalent to prior service credits. Workers already close to retirement age when the system was first started, or when coverage was extended to their employment, received full benefits even though the contributions they and their employers paid would finance only a small part of the benefit. While this was sound public policy and kept many old people off relief, it did mean that these benefits had to be financed from future contributions. There is no justification for expecting presently covered workers to pay for this 'accrued liability'—estimated in the long run to amount to one-third of the total cost of the program—through a regressive payroll tax. A far fairer method would be to finance this share from general revenue sources to which all taxpayers contribute and through a more progressive tax structure."

I stand on this position today—that the best way of financing our Social Security system is to introduce general revenues in combination with a higher wage base, thus preserving the essential value of earned rights and at the same time lessening the regressivity of the tax. (Part 2, p. 124.)

The same purpose would be achieved by the proposal of Wilbur J. Cohen, former Secretary of Health, Education, and Welfare, that a Federal contribution out of general revenues be considered for meeting the cost of benefits paid to individuals with fewer than 40 years of contributions—in effect, benefits above the amount paid for by employer and employee contributions. Specifically, he said:

Therefore, I favor at some point when Congress has the money, Congress paying the difference between the cost of what the individual paid for his benefit and what the benefit did produce, which is roughly about one-third of the total cost of benefits in perpetuity. That seems to me, if you want to reduce the contribution rates at some point and have a logical method of introducing a general revenue subsidy, that is an intelligent, rational way which pension systems use to finance the transitional cost when the system has started with the longrun cost. (Part 4, p. 252.)

Refund of contributions to low-income workers. To reduce the regressivity of the payroll tax and still retain the psychological advantages of the contributory system, it was suggested that the income tax system be used to make refunds to low-income families to compensate for the Social Security taxes they had paid.

Mr. Cohen testified:

The proposal advocated by Senator Russell Long of the Senate Finance Committee, which has passed the Senate by an overwhelming vote in 1972 as a part of H.R. 1, to refund to low-income individuals 10 percent of their earnings—roughly the combined Social Security contribution—warrants support. (Part 4, p. 251.)

Mr. Brittain suggested:

An alternative means of substituting the income tax for the payroll tax is to integrate the two: the income tax could absorb the employee's share of the payroll tax directly, or the employee's payroll tax payments could be credited against his individual income tax. The burden of the employee tax would be fully removed if cash refunds were paid to those whose employee payroll tax exceeded the income tax. Any psychological advantage of the earmarked tax could be retained with either of these devices, while in effect the income tax was substituted for the employee tax. Integration of course need not be restricted to the employee tax. The taxpayer could also receive credit for the employer tax paid in his name. This would be consistent with the finding that the employee also pays that tax as a result of the restraint it imposes on real wage rates. (Part 3, p. 180.)

Mr. Brown spoke strongly against such proposals, on grounds of social insurance principles as well as administrative complexities, saying:

What I keep coming back to, sir, is that any way you work it, a reduction of contributions for the low-income person is essentially introducing an individual needs test into a system designed to avoid a needs test. (Part 3, p. 191.)

No contributions before age 25. Only touched on in the prepared statement of the NRTA-AARP is the suggestion that workers not be taxed before age 25, thus offsetting the shorter years of contribution of college graduates and higher degree recipients who tend also to have relatively higher earnings and higher benefits. (Part 5, p. 353.) Not explored, therefore, was the effect of such a change in denying survivors and disability protection to young workers below the age of 25.

Increasing the wage base. Several witnesses advocated a substantial increase in the maximum earnings base, as a means of reducing the regressivity of the payroll tax and providing some additional revenue to the system. Mr. Cohen advocated returning to the relationship adopted by Congress in 1939 (then \$3,000 and probably \$16,000-\$18,000 in 1973) which would permit some reduction in the rate charged low-wage workers as well as higher benefits for those with earnings above the then current maximum of \$12,600. (Part 4, pp. 252-3.)

Self-employment contribution rate. Not infrequently, complaints are heard from the self-employed about the inequity of charging them one and one-half times the employee contribution rate. One possibility—not explored through hearings thus far but suggested in the additional material submitted by Mr. Cohen—is to allow the self-employed to deduct from their income tax one-half of their contribution as a business expense. (Part 4, p. 279.)

Use of general revenues limited to Medicare. "I would personally rather like to see the concept of contributions from general revenue held at least in the near future to the health insurance area," testified Commissioner Ball. He went on to say:

Now, in the cash benefit program, if you leave the program on the benefit side, with the level of protection we have talked about, and do not intend to greatly liberalize that, a logical point at which one might consider general revenues is way down the road, when the contribution rate has to go up. (Part 1, p. 39.)

This recommendation, however, was made at a time when long-range forecasts indicated that the payroll tax for cash benefits would be adequate until 2011. The long-range estimates subsequently available could lead to a different conclusion, forecasting as they do the need for a much earlier increase in contributions for cash benefits.

General revenues for the total system. The case for general revenue sharing in the total system (cash benefits and Medicare) was stated by Mr. Brown, as follows:

I am convinced that the time has come to implement more fully a sound principle of contributory social insurance which is widely accepted abroad, which was fully supported by the planners and the earlier Advisory Councils, and was recognized by Congress from 1944 to 1950. It is that the Government should participate in the financing of a contributory social insurance system. The principle holds for the total system, but it is most urgent at this time that it be more fully implemented in respect to a merged and integrated Medicare program.

The Advisory Council of 1969-71 recommended as follows:

"For financing purposes, supplementary medical insurance, (now financed through premiums and general revenues) should be combined with hospital insurance, and the Medicare program, as enlarged under the Council's recommendations, should be financed by one-third contributions from employees, one-third from employers, and one-third from general revenues."

This recommendation was the result of extensive study and discussion. Not only is there a limit to the proper use of payroll taxes, but especially under Medi-

care, there is a large degree of social redistribution of costs which should be supported by the general taxpayer.

Under Medicare, the low-wage beneficiary receives the same care as the high-salaried beneficiary. Also, when the system commenced in 1965, the whole cost for hospital benefits for those then retired was placed upon the current workers and their employers. This will be true again when the disabled are covered under hospital benefits in July of this year. (Part 3, pp. 193-4.)

THE RETIREMENT TEST

From the point of view of the beneficiary, the major unresolved issue in future directions in Social Security is the retirement test. Clearly, this is the most unpopular and least understood feature of the program.⁶

Organizations composed largely of beneficiaries that were represented at the hearings differ in their recommendations. The National Council of Senior Citizens has repeatedly recorded its support of a retirement test—kept up to date with rising earnings and costs—as the best way of using limited social insurance funds for those who have suffered a real loss in earnings and are therefore most in need of benefits. The National Retired Teachers Association-American Association of Retired Persons, which up until a few years ago favored eliminating the test altogether, testified on July 25, 1973 (when the test was \$2,400) that it sought an increase to \$3,600 (Part 5, p. 291), with one of its consultants, a former Social Security Commissioner, expressing his own view that there should be no further liberalization. (Part 5, p. 295.)

Subsequently, at the Twin Falls hearing, the chairman of the joint State legislative committee, NRTA-AARP, testified that “our organizations favor the complete abolishment,” and suggested that the costs of eliminating the test be financed from general revenues rather than the payroll tax. (Part 6, pp. 497 and 503.)

At the opening hearing, Commissioner Ball explained that the 1972 changes in the retirement test had removed the disincentive for working, saying:

I think the test that was in effect before the change in H.R. 1 was correctly subject to a lot of criticism. There was a situation in which a person could actually be worse off in terms of net income by working more and earning more, because there was a dollar for dollar reduction of benefits above a certain level of earnings.

That has been changed. Now, there is no reduction at all in Social Security benefits if earnings are less than \$2,100, but the real reform is that for all earnings above \$2,100, only \$1 in benefits is withheld for each \$2 of earnings. So you can now say to everybody, the more you work and earn, the higher your spendable income will be. There is no longer the disincentive to employment that there was in the old test. (Part 1, p. 30.)

Nevertheless, there are possibilities of further liberalization which—while maintaining the principle of a retirement test and keeping costs down—could make the test more acceptable. Some suggestions follow.

Age at which test no longer applicable. The NRTA-AARP suggested (Part 5, pp. 295-6) that in addition to liberalization of the

⁶ The Social Security program, designed to provide protection against the loss of earnings, includes an earnings test—usually known as the retirement test—which withholds or reduces benefits for workers under age 72 whose earnings exceed a specified amount. Opposition to the test rests partly on its effect in restricting older people in worthwhile employment opportunities, partly on the fact that it relates only to earned income. To eliminate this test completely would result in significant additional costs (about \$4 billion a year), paid mostly to full-time workers. To apply it to unearned as well as earned income would significantly reduce the incentive for saving for old age, through private pensions or individual effort.

amount of the earnings test, consideration be given to lowering the age at which the beneficiary can have unlimited earnings (now age 72) to perhaps age 70.

No Social Security tax after 65. One individual, noting that hearings were being held, wrote to Senator Church, saying:

I believe that individuals over the age of 65 years who are gainfully employed or gainfully self employed should not be required to make any further contributions to Social Security. As a self employed individual this tax costs me in excess of \$500.00 a year now, and it keeps going up.

Increase in increment for work after 65. As a result of a recent amendment, benefits are increased by 1 percent for each year the individual postpones claiming retirement benefits after reaching age 65. Mr. Cohen testified:

If any further consideration is to be given to liberalization of the retirement test, then an increase in the 1-percent increment to 2 percent, after age 65, should be given priority. The repeal of the retirement test completely would cost \$4 billion a year, a little bit over one-half of 1 percent of the payroll. This, in my opinion, would be an undesirable use of several billion dollars worth of funds which are much more urgently needed for higher priority needs, such as raising benefits for the very lowest income people, and others that I am suggesting. (Part 4, p. 248.)

Test related to benefits plus earnings. Not suggested during the hearings but seeming to merit further consideration is a recommendation coming out of the Section on Employment and Retirement of the 1971 White House Conference on Aging. This was as follows:

Recommendation VII—Social Security Retirement Test—The earnings test that results in withholding of Social Security benefits constitutes a financial hardship for older people.

The retirement test should allow persons to receive Social Security benefits without reduction up to the point when the total of Social Security plus earnings equals \$5,000 per year. In no case should benefits be reduced for persons earning under \$1,680.

Tax exemption for earnings equivalent to benefit loss. Another possibility not considered at these hearings was that beneficiaries be excused from income taxes on those earnings that are equivalent to the benefit loss, thus recognizing that the lost Social Security benefits would have been exempt from income taxes.

THE BENEFIT LEVEL

Significant increases in the overall benefit level in recent years permit a focus on special problem areas that still remain. Some of these are identified here.

Replacement-ratio. Testimony by Mr. Brickfield on behalf of the NRTA-AARP urged early attention to the appropriate ratio of earnings to be replaced "now that the goal of providing an adequate income floor will be primarily the responsibility of the SSI program."

Divested of the income support function and, hopefully, of the "floor of protection" philosophy, OASDI can now function primarily as a mechanism to replace an adequate degree of earnings lost as a result of retirement, disability, or death.

* * * * *

Moreover, since the aged of tomorrow will be better educated, more skilled and more sophisticated than the aged of today, they appear far less likely to accept the lower standard of living which presently attends retirement.

The projected dimension of the future aged population and the assumed unwillingness on their part to accept in retirement a standard of living below that experienced prior to retirement really define the challenge which confronts us here today.

Now, as to the standard of adequacy for the replacement of earnings lost due to retirement, since Social Security will probably remain the primary instrument of earnings replacement for the foreseeable future, the optimum degree of earnings to be replaced through Social Security should be determined now in order that the modifications in the benefit structure and financing mechanism may be carried out in time to accommodate future needs in the most efficient manner.

Basically, our associations believe that the living standard of the future aged should be related directly to a standard of living experienced prior to retirement.

Moreover, the standard selected should not, in any case, result in a post-retirement living standard appreciably lower than that enjoyed immediately prior to retirement. (Part 5, p. 288.)

Mr. Cruikshank, president of the National Council of Senior Citizens, stated:

It is time, therefore, that we come to grips with the question of the level of income intended for future generations of the elderly and the part Social Security benefits should play in achieving this level.

In this respect, we have much to learn from the trend abroad in recognizing that the adequacy of income in retirement should be measured in terms of the amount of pre-retirement income replaced. The trend there has been toward establishing earnings replacement levels between 60 and 80 percent of variously defined measures of pre-retirement earnings. In contrast, as a result of our most recent Social Security amendments, the retirement benefit for men retiring at age 65 amounts to about three-fourths of average monthly earnings of \$200, just under 60 percent at \$400, and drops to below half for workers qualifying in the future with an average monthly wage of \$700. (And in assessing these figures, we must remember that more than half of all men starting to draw benefits are under age 65 and receive a reduced benefit.) There has also been a trend abroad to increase the ceiling on contributions and creditable earnings to take into account the total earnings of all except the very highest earners. Furthermore, most foreign systems now base benefits on earnings during the period just prior to retirement, rather than on earnings over the working lifetime. (Part 2, p. 150.)

Period of earnings on which benefits are based. As noted immediately above, the more "dynamic" pension systems abroad exclude early years of earnings in determining the amount of preretirement income to be replaced by the benefit.

On this point, Mr. Brickfield testified:

Prof. James H. Schulz of Brandeis suggests that the appropriate standard could be based on the average highest earnings in 10 of the 15 years immediately prior to retirement and this is Professor Schulz's suggestion, the 10 of the 15 years immediately prior to retirement.

Others have suggested standards based on average earnings in 5 of the 15 or 20 years immediately preceding retirement, the average of the highest earnings in any 5 years, or in any 10 years.

* * * * *

While our organizations tend to agree with the recommendation of Professor Schulz, we also believe that a standard based on average lifetime earnings adjusted, however, to account for cost-of-living and real wage increases, has considerable merit.

However, the administrative burden and attendant cost consequences of such a standard may be so onerous as to render it unfeasible. (Part 5, p. 289.90.)

Benefits for low wage workers. The level of assistance guaranteed under the SSI program bears an important relationship to benefits earned by workers with low wages. With respect to this relationship, Mr. Brown recommended:

The OASDI benefits for normally employed, lower-wage workers should be sufficiently better than the level of assistance grants to justify their lifelong contributions. This is not a matter of a higher arbitrary minimum, but rather

of an appropriate scale giving proper recognition to the relatively higher imputed need of beneficiaries at the lower end of the scale compared to their average lifetime earnings.

The major bend point⁷ in the lower part of the OASDI benefit scale has not been changed since it was set at \$110 in 1954. There is a good reason to believe that a higher bend point is now justified, even if the slope above that point might need to be slightly less steep. This would give beneficiaries in the lower part of the scale a better adjustment to their normal needs, still graduated according to their past earnings. (Part 3, p. 195.)

Actuarial increase for retirement after 65. The NRTA-AARP suggested that careful consideration be given to providing "an actuarially increased Social Security benefit for each year beyond age 65 up to age 70 just as the benefit is actuarially reduced for retirement prior to age 65." (Part 5, p. 437.)

ADJUSTMENT OF BENEFITS

Now that benefits are to be adjusted automatically, careful attention must be directed to the appropriateness of the adjustment method.⁸

But whether adjustment is automatic or through act of Congress, it is essential that the adjustment adequately reflect the effect of price changes on the elderly. This requires a fresh look at the adequacy of the Consumer Price Index as a measure of the impact of inflation on the aged population in a period when food, shelter, and medical care—items which take practically all of older people's budgets—are escalating especially rapidly. Materials submitted by the Social Security Administration in response to a question raised at the January 15, 1973 hearing related to the situation prior to 1970 and may no longer be relevant. (Part 1, pp. 63–66.)

In submitting these materials, Commissioner Ball wrote: "It should be noted that the CPI has provided an effective means of adjusting annuities under the civil service retirement system to increases in the cost of living since 1962." This analogy suggests that consideration be given to the possibility that the automatic adjustment provision in the Social Security Act—like that relating to civil service annuities—should also include an additional 1 percent as a cushion, recognizing the time lag before the adjustment reaches the beneficiary. Consideration should also be given to more frequent increases than the once-a-year provision enacted in 1972.

For the long range, consideration should be given to increases in benefits that take account of rising standards of living and not just rising costs. Identifying this as "the most important future direction for Social Security to take," Mr. Cohen said:

The "dynamic" character of the program should be further improved and extended. That is the relationship to future economic situations. Social Security should be improved as productivity and earnings increase. It is not sufficient to increase Social Security benefits to retired individuals solely in relation to cost-of-living increases as it is incorporated in the present law.

⁷ The benefit formula is designed to provide a larger benefit in relation to earnings for low-paid than for high-paid workers. To achieve this, the benefit is calculated as a higher percentage below the "major bend point" and each successive bend point than above.

⁸ The 1972 amendment for automatic adjustment of benefits provides that—in the absence of congressional action to increase benefits—benefits will be increased proportionate to prices (as measured by the BLS Consumer Price Index) when the CPI has increased at least 3 percent. Automatic increases are to be made no more often than once a year and the first possible increase under the amendment was for January 1975. (In recognition of the rapid rise in prices, the Congress acted to increase benefits in 1973.)

It is recommended that a special study be made of Social Security systems in other countries where benefits are automatically related to changes in earnings in the economy. In other words, Senator, if the cost of living goes up, let us say, 3 percent a year, and wages and productivity go up 5 percent a year, and retired people only get benefit increases of 3 percent a year, in the course of 5 or 10 years they are going to be at a lower relative level than the other people in the economy.

Therefore, in the cost-of-living increases for retired people, an important and satisfactory step was taken in 1972 and 1973, which can only lead 10, 15 years from now to our aged being treated in a way that will put them at a relative disadvantage. (Part 4, p. 244.)

Mr. Cruikshank's testimony on this point reads as follows:

This Nation took a giant step forward in adopting the 1972 amendment to provide automatic adjustment of benefits to increases in the cost of living. An important future direction for Social Security, one also endorsed by the White House Conference on Aging, is acceptance of the concept of measuring income adequacy in terms of rising national standards of living, not just rising prices. In this respect, we have much to learn from the experience of other countries, notably West Germany and Sweden, in adjusting pension benefits to rising wage levels, thus allowing retirees to share in economic growth. (Part 2, p. 150.)

COVERAGE

Still unresolved at the time of the hearings was the issue of bringing under the nearly universal coverage of Social Security two groups of employees: (1) Railroad workers who then had what amounted almost to coverage for the lower part of their protection through an interchange arrangement with the Railroad Retirement System, and (2) Federal civilian employees whose system is uncoordinated with Social Security.

In the opening hearing, Commissioner Ball pointed out that the report of the Commission on Railroad Retirement called for covering railroad workers under Social Security "just like everybody else and move the upper part of railroad protection into an arrangement that is supplementary to Social Security similar to the protection that is so common in private industry in general." (Part 1, p. 16.)

In October 1974, the Railroad Retirement System was restructured into two components: the first tier reflecting a basic Social Security benefit calculated on the basis of Social Security covered employment and railroad services, and the second tier, a pension based on a formula applicable only to railroad service.

With respect to civil service employees, additional material submitted by Commissioner Ball in response to a question read:

The problems resulting from the lack of coordination between social security and the CSR system have been the subject of much study over many years but the various solutions which have been proposed have proved very controversial and many have involved high costs. Of the various plans which have been proposed, the coverage-coordination approach, more than any other, has the potential for assuring a reasonable relationship between benefits and lifetime contributions and service in the case of people who shift between Federal employment and other work. Under this approach, social security coverage would be extended to employment covered under the CSR system with some reduction in CSR benefits and contributions to take account of the contributions and benefits of the social security system. One of the most significant features of this approach is that it would provide prepaid hospital insurance protection under the Medicare program for all Federal employees. The coverage-coordination approach has in the past been unacceptable to the principal organizations of Federal employees; they are opposed to an approach which would reduce benefits now provided under the CSR

system on the basis that it would weaken the CSR system and would tend to limit future improvements in the protection of Federal employees to changes made in the social security program.

Another, more limited, approach would be to transfer earnings credits from the CSR system to social security where there is no benefit eligibility under the CSR system when the worker dies, becomes disabled, or retires. This approach would be less costly than coverage coordination and would fill the major gaps in protection of those who move between employment covered by the CSR system and jobs covered under social security.

The House Committee on Ways and Means has directed the Social Security Administration to give further study to ways in which limited coordination between social security and the CSR system could be achieved and to consult with the Civil Service Commission and Federal employee unions on what would constitute a workable proposal. We are now engaged in this study. (Part 1, p. 63.)

The Senate Committee on Aging will wish to pursue the question of Social Security coverage for civil service employees in future hearings.

ADMINISTRATION OF SOCIAL SECURITY

Several major witnesses wholeheartedly endorsed the proposal, initially made at the January 23d hearing by William L. Mitchell, for the establishment of a bipartisan board or commission to administer the Social Security program.

Mr. Mitchell, noting that the new provision for automatic adjustment might diminish "the thorough, periodic review of the system needed to insure its continued dynamism," stated:

With this new provision, and with the addition of Medicare and the adult categories of public assistance to OASDI, I suggest that this may be an appropriate time to consider the desirability of setting up a bipartisan board to help guide the future destiny of these programs. It will be recalled that the original Social Security Act of 1935 provided for such a board and the program was under its administrative supervision for the first several years of its existence.

Surely the wisdom, objectivity, and intense work of that body contributed immeasurably to the design and development of an organization which today is known for its excellence and efficiency. The policies and principles which that board developed still guide an organization which has responsibly disbursed billions of dollars in benefits with never a breath of scandal and which continues to enjoy the confidence and respect of the American people.

Such a board could be expected to provide continuity to the policies and practices of the past and would be sensitive to the wishes of both the Congress and the President, as well as to political considerations. This is not the place, nor am I prepared to go into detail regarding formulation of this board, but I am convinced that it would serve the same worthwhile purpose as it did originally. (Part 3, pp. 205-6.)

Mr. Cohen too suggested reestablishment of something like the original Social Security board, saying:

If consideration is to be given to any administrative changes in the program, by either the executive branch or the legislative branch or any review, then I would like to suggest that one possibility would be to reestablish something like the original Social Security Board to administer the program.

This board would consist of three persons, that is illustrative of what the original board was, three persons nominated by the President with the advice and consent of the Senate for 6 years, staggered terms, with no more than two members from any one political party.

Social Security is getting so big and so involved and so complex and I have been so concerned with the possibility of political involvement of the executive branch that I have been thinking more and more that the Congress ought to reestablish an independent board to administer the whole program so as to be sure that no political involvement becomes a factor in the Social Security system. (Part 4, p. 246.)

Mr. Brickfield, testifying on behalf of NRTA-AARP, said:

I now come to the establishment of a bipartisan Social Security Board. Our associations believe that steps should be taken to assure the type of continuity with respect to supervision, direction, and development in Social Security that the country enjoyed in the past.

We think one important step in this direction would be a return to the former three-member bipartisan board form of administration which, in our judgment, contributed so importantly to the early success of the system and to the public's confidence in its administration.

Now that the Social Security Administration has the responsibility for supplemental security income as well as the old age, survivors, disability and health insurance programs, we believe that a three-member bipartisan board would best assure integrity, competence, and impartiality and provide protection against purely partisan political intervention.

We recommend that two of the three members be from the majority party and that all three be named by the President with the advice and consent of the Senate. The President could select the chairman and all members would serve for fixed terms. The board would be concerned primarily with policy formulation but would operate through an executive director who would have to qualify under Civil Service rules and serve at the pleasure of the board. (Part 5, p. 297.)

Mr. Cruikshank, in expressing wholehearted endorsement of administering the Social Security programs through an independent non-political agency, pointed out a number of advantages:

Such an independent agency would underscore in the public mind the essential difference between these social insurance programs and other operations of the Government. It would also provide greater visibility and prestige as well as optimum responsiveness to the constituents—and again I point out that the constituency encompasses all our people, regardless of age. An important specific charge to this agency should be to develop and carry out an aggressive informational program. Our observation of social insurance programs in other countries indicates that this informational responsibility is an important part of the right to know on the part of beneficiaries, and of the effective administration of the program.

An independent, nonpolitical agency could assure continuity in both the review of the system's effectiveness and in its day-to-day administration—a continuity that cannot possibly be achieved under the present system when the administering officials are subject to change every few years and the program is reviewed only intermittently by an advisory council or by the Congress.

Another advantage is that it would be made clear that the agency has its own source of funding through the trust funds it administers. Indeed, our Social Security system now has, but this is a fact not commonly recognized by the general public who are surprised to learn that *their* Social Security system owns its own buildings and equipment and finances its own operations.

An important essential would, of course, be removal of the Social Security trust fund expenditures from the consolidated budget. Thus, Social Security expenditures could be assessed on their own merits and in relation to sound actuarial principles rather than primarily through their immediate impact on the annual Federal budget. Furthermore, the other programs now under DHEW would be relieved of the need to absorb more than their reasonable share of Department-wide budget cuts when they are imposed—cuts that are heavily weighted by the sheer size of the Social Security program and its irreducible obligations. (Part 4, p. 281.)

So persuasive was the testimony of the above witnesses that, in the spring of 1974, Senator Church, chairman of the Senate Special Committee on Aging, introduced S. 3143 to establish an independent commission. Ways and Means Committee Chairman Wilbur Mills introduced a companion bill in the House. S. 3143 had 50 cosponsors by the time the session ended.⁹

⁹ On January 27, 1975, Senator Church introduced S. 388, the Social Security Administration Act, to accomplish the above objective.

SUBJECTS FOR FUTURE HEARINGS

Women and minorities. The committee plans to hold additional hearings that focus on treatment of women and of blacks and other minority groups under Social Security.

The hearing on women will provide an opportunity to explore the following proposal made by Mr. Cohen at the July 25 hearing:

Women who perform household and family duties should be able to contribute to the insurance program on an amount equivalent to the self-employment rate on the average earnings of all women working four quarters in the latest prior year. Women would then receive benefits in their own right with the provision that a married woman would always receive at least one-half as much as her husband did. Special consideration should be given to assuring equal treatment for women and men in the program.

* * * * *

Therefore, my proposal which is designed in part to overcome some of these difficulties is that a wife or mother or woman who stays at home and does not receive regularly earned income in the economy would have her work counted for Social Security at the presumptive rate of average earnings of all women who work four quarters during the year and pay, rather than the double contribution, the self-employment rates. I urgently speak to that as a possibility. (Part 4, p. 249.)

Another problem in relation to women was touched upon at the Twin Falls hearing when the statement submitted by the representative of the NRTA-AARP included these comments on the treatment of working wives under Social Security:

Today, many working wives feel that their Social Security contributions have been wasted in situations where they are entitled to receive benefits upon their spouses' earnings that are as high if not higher than those to which they are entitled on the basis of their own earnings. This criticism has become more pronounced in recent years as proportionately more women have been entering the labor force.

The dissatisfaction of working wives who, despite their Social Security contributions, receive no higher benefits than they would have received had they not worked in Social Security covered employment is the result of their non-acceptance of the rationale for paying the wife's benefit only to those who may be presumed to be dependent—that is, not paying those who have earnings records which defeat the presumption of dependency. This rejection of the "dependency" rationale is coupled with a lack of awareness of the advantages that working women have as a result of their eligibility for benefits based on their own earnings records. For example, married women who work usually have disability insurance protection, which is not available to nonworking wives. Should they retire at or after age 62, benefits will be payable to them on the basis of their own earnings records even though their husbands continue to work. Finally, in the event that they become disabled or die, monthly benefits on their earnings records are payable to their children.

Our organizations recognize, however, that neither the dependency rationale nor the expanded insurance protection available to working wives is likely to assuage the growing dissatisfaction with what they perceive to be inequitable treatment in terms of social security benefit amounts. We believe that the Congress will find it necessary to acknowledge the reality of the working wife by modifying the Social Security system so as to eliminate, to the extent possible, those situations in which a working couple receives less in total old age insurance benefits than another couple with the same total earnings where only the husband worked.

* * * * *

While it may not be possible to achieve precise benefit equity with respect to everyone, our organizations recommend that the Congress consider seriously the proposal advanced by the 1971 Advisory Council on Social Security to reduce existing inequities with respect to working wives. That proposal would provide

benefits for a married working couple equal to those provided now for a couple where only one spouse works and has all the earnings.

Under the council's proposal the earnings of a man and wife in each year would be combined and credited up to the maximum annual earnings creditable for the year. The benefits of the couple would be based on these earnings. In order to qualify for the combination, each would have to be fully insured, would have to be at least age 62, and would have to have applied for benefits. Both the husband and wife would be entitled to a benefit, before any reduction on account of early retirement, equal to 75 percent of the age 65 benefit based on the combined earnings. A widow would get a benefit based on the combined earnings of the couple. The earnings record would be separated on divorce, with each member of the couple receiving benefits as if the earnings records had never been combined. (Part 6, pp. 504-505.)

Other subjects. Throughout the forthcoming hearings of the Senate Committee on Aging in its study of "Future Directions in Social Security" will be the all-pervasive question of long-range financing, especially in view of the 1974 Trustees Report. Another area of special and timely emphasis will be suggestions for dealing with an inflationary situation: is there need for a special cost of living index for the elderly? Should the Government issue a constant purchasing power bond, for use both by individuals with small savings and as an investment device for private pension funds? Also underlying these hearings will be the basic problem of persons with low earnings and other low-income individuals and the role of the Social Security program in meeting their needs.

PART 2

SOCIAL SECURITY: A SOUND AND DURABLE INSTITUTION OF GREAT VALUE ¹⁰

Nearly every American has a personal stake in the social security system. Many millions rely on it to safeguard themselves and their families against economic catastrophe when earnings stop because of old age, disability, or death. Attacks on the system designed to create doubts of its soundness and durability are a disservice to the Nation.

Several elements of the system, to be sure—the level of benefits, for example, the test of retirement, the benefit rights accorded to women, the adequacy and equity of financing—are quite properly subjects of continuing public debate. Social security has not been and should not be a static structure, for it best serves its purpose if it is adapted to changing times and changing conditions. Public discussion addressed to improvement of the system is both necessary and helpful. But discussion of that kind is very different from assertions that the system is basically unsound, that it is bankrupt, or for some other reason doomed to collapse, or that it is a deception foisted on the American public. Charges similar to these have recurrently been made in the past, and as often have been found baseless. They have no more foundation now than they had when first made nearly forty years ago.

Social Security has been probably the most thoroughly and continuously studied, both within and outside government circles, of any program ever enacted by Congress. On five occasions, from 1938 to 1971, the system has been exhaustively reviewed by advisory councils established under congressional auspices and composed of economists and other social scientists and leaders of labor and business, including distinguished actuaries and leaders of the insurance industry. In each instance, the integrity of the system has been vigorously reaffirmed. This history, if it does nothing more, should foster a healthy skepticism toward the current destructive attacks.

The conclusions of these councils have carried much weight and have been an influential factor in bringing about the improvements that have been made in the system over the years. The current statutory advisory council will soon issue a report. Like its predecessors, it has a broad assignment—to review the entire social security program and advise how to make it best serve the public interest. We may well await the recommendations of this council and ensuing congressional hearings on substantive changes in the system which are being widely debated. But we should not wait to deal with irresponsible attacks on the soundness of the structure.

THE ASSURANCE OF FUTURE BENEFIT PAYMENTS

The most vicious of these attacks is the one charging that promised social security benefits may not be paid when they fall due twenty or

¹⁰ White Paper issued on February 10, 1975, endorsed by five former Health, Education, and Welfare Secretaries and three former Social Security Commissioners. See appendix 2, p. 30 for news release giving additional details.

thirty or forty years hence. To the worker who is compelled to contribute from his earnings every payday, who is counting on these benefits for his security in retirement and for the protection of his family in the meantime, planting seeds of unwarranted doubt is a cruelty.

What are the facts?

The first fact is that the payment of benefits is mandated by the law of the land. A claim to social security benefits is a legal right enforceable in court, and many claims are in fact so enforced when eligibility is unclear. However one may define a "legal right", it certainly embraces a payment commanded by law and judicially enforceable.

The second fact is that Congress has gone far—probably as far as any Congress can go in binding its successors—to assure that future legislators will not, by changing the law, weaken the obligation to pay these benefits. By earmarking the proceeds of social security taxes for the payment of benefits and depositing them in a trust fund for this purpose, by entitling the system insurance, by continuing actions to assure its financial soundness, and by innumerable pronouncements of congressional committees and individual spokesmen, Congress has made clear beyond question its pledge to the American people that the social security commitment will be honored.

The social security system is, in effect, a compact between the people of the United States and their government. Congress, it is true, retains the legal power to violate this compact, which would be a highly irresponsible act, altogether inconsistent with the Congress's 40-year record of responsible action on social security. If there are doubters among us, they should be reminded that a member of Congress who hopes for reelection will not vote to repudiate a promise to virtually his entire constituency. It is inconceivable that a majority of the members of each House of Congress will ever do so.

THE NATURE OF THE CONGRESSIONAL COMMITMENT TO CONTRIBUTORS

The social security commitment differs in an important respect from that of a private insurance company, which in writing a policy fixes its terms in every detail for the life of the policy. Congress, by contrast, has of necessity built an element of flexibility into the national social insurance system. Thus, when Congress has amended the law to improve the benefit structure it has generally given the advantage of the change to those already on the benefit rolls as well as to those who are still contributing. Occasionally, improvement of the structure involves substitution of one benefit for another, as when a provision in the original Act for refund of certain contributions was replaced by the far more valuable provision of dependents' and survivors' benefits. One cannot say that under no circumstances will any individual in this massive system suffer some loss in some future contingency as a result of overall improvements in the system. Such adjustments must, of necessity, fall within the range of flexibility that has been reserved to Congress. What one can say with confidence is that the congressional sense of fair play, reflecting that of the public, gives assurance that the power of amendment will not be abused.

SOCIAL SECURITY IS PROPERLY DESCRIBED AS INSURANCE

It is occasionally asserted that social security is not in fact insurance, that so describing it is misleading, and that its trust funds are grossly inadequate. These assertions have been used by some to foster doubt that the promised benefits will be paid. All these assertions are unfounded.

Although the propriety of its use is a semantic question, the term "insurance" is not without significance to either the congressional or the public perception of social security. Social insurance is a concept long and well recognized across the world, and is one into which social security fits neatly. For good reasons, social insurance differs in important respects from private insurance, but it embodies the central element of financial protection against defined hazards, through a pooling of contributions and a sharing of risks, with benefits payable as a matter of legal right on the happening of stated events. It is fallacious to argue, as some persons do, that the workers' payments are not insurance contributions because they are taxes—all taxes are compulsory contributions, either for the general support of government or for some particular governmental activity, and these payments are nonetheless contributions to an insurance system because they are also taxes. Congress used the word "insurance" in the statute as one indication of the character of the commitment it was undertaking, and the Supreme Court of the United States has stated that the term "social insurance" accurately describes the program. While anyone has the privilege of dissent, the Court's approval should have put an end to charges that the nomenclature is deceptive.

THE ADEQUACY AND INTEGRITY OF THE TRUST FUNDS

The matter of reserves has been a topic of confused debate almost since the ink dried on the original enactment of social security. In the early days it was said that the contemplated "reserve account" would be unmanageably large; now it is being charged that the social security trust funds are far too small. It was also said in 1936, and is occasionally even said today, that the funds are fictitious because they are invested in government bonds. Charges that social security reserves have been grossly inadequate and charges that they are fictitious have been emphatically rejected by every one of the advisory councils, and they were rejected unanimously as early as 1945 by the social security committee of the insurance industry. A government insurance system which has its future income assured by the taxing power has no need to build up large funds that a private insurer would require if it underwrote similar liabilities, and indeed, it would be unwise to the point of irresponsibility to accumulate such sums. The only need for a trust fund is as a contingency reserve large enough to tide the system over any temporary change in income and outgo; if an increase in revenues should be necessary, the trust fund would enable Congress to delay such action during a period of economic recession. As for the worth of the assets in the funds, one need only consider that if a private trustee held these government bonds they would be gilt-edged securities, and then ask oneself how their value disappears when the same bonds are held by government officers as trustees.

The funds reflect the fact that, now, with a substantially mature system, annual contribution income and annual outgo are roughly in balance. This is another way of saying what critics harp on as though it were a demerit, that the benefits paid this year to the aged, the disabled and their dependents, and to survivors of the deceased derive in the main from this year's contributions by workers and their employers. As long as his benefits are adequately assured by the government's ability to obtain future income, today's young worker need have no concern because his contributions are used to pay today's beneficiaries, or because his future benefits will be paid from future contributions.

OFF-REFUTED CHARGES

The charges thus far considered are, in their main outlines, repetition of earlier efforts to discredit the social security program, and they are no more valid now than they have been in the past. Repeatedly and consistently, Congress, after extended study by its responsible committees as well as the distinguished advisory councils, has found these charges to be without merit.

Other charges, though not new in themselves, have acquired a new emphasis because of the steady rise over recent years in the contribution rate and in the ceiling on taxable earnings, and these charges deserve consideration. The increase in the amount of contributions, of course, must be heavily discounted if one thinks in terms of purchasing power rather than of dollars, and in terms of the increase in personal incomes. But whatever the value of the dollar, providing a decent measure of economic security to the retired, to the disabled, and to widows and orphans is a hugely expensive undertaking. The questions that demand serious thought relate not so much to the total sum which the system raises by taxation as they do to the manner in which the burden is distributed.

THE SOCIAL SECURITY SYSTEM IS NOT REGRESSIVE

It is said, for one thing, that social security taxes are regressive because the wealthy pay smaller percentages of their earned income than do the poor, in contrast to the general income tax, under which the wealthy pay higher percentages. If social security collections were taxes for general support of the government, this charge would be unanswerable; one can hardly imagine that Congress would ever have imposed these levies, or would now allow them to remain on the statute books, except as a part of a social insurance system. This charge illustrates, indeed, the fallacy of looking at the two parts of social security in isolation from each other, an approach which inevitably distorts the issues and loads the argument. The issue here is not whether social security *taxes* are regressive but whether the social security *system*, taking into account both benefits and contributions, is open to this charge. The answer to that question is "no." The benefit formula is so designed as to give a larger return for each dollar of contributions to the low-wage earner than to the high. While there are other factors to be considered, some favoring the poor and some working against them, the net effect of the system is to transfer some income from the more affluent as a group to the less affluent. It is legitimate to argue

that the system ought to be made more progressive than it is, as for instance by the introduction of a government contribution derived from general revenues, but it is not legitimate to argue, by disregarding the benefit payments, that the system as now structured is regressive.

Another contention which has gained in prominence with the increasing amount of contributions is that, regardless of the liberality of future returns, the present burden is simply more than people in low- and moderate-income brackets ought to bear out of current earnings. It is often pointed out that many of these people pay more in social security than in income taxes, though the significance of this comparison is not apparent. Many persons pay more for any number of things than they pay in income taxes, and there is nothing inherently inequitable in charging them more for the protections afforded by social security than they are charged for the general support of government. No one can be dogmatic about what burdens on various income groups are tolerable, or represent good social policy, but to say that the poor are too heavily taxed for social security is to say either that their protection should be reduced or that it should be more largely subsidized by the wealthier segments of society. Not many argue for the former alternative, but the latter is widely and properly a matter of debate.

SOCIAL SECURITY GIVES CONTRIBUTORS A GOOD BARGAIN

Statements have been broadly disseminated that social security gives the contributor a poor bargain, and that he could do far better by investing the amount of his contributions in the private markets. This is not true. If we exclude speculative investments (including investment in the erstwhile "ever-rising stock market"), which can always yield some individual a windfall but can also yield a terrible loss, the individual under the social security system receives better value from the government than he could obtain elsewhere. With the automatic escalation of workers' benefit rights as wages rise, and the automatic cost-of-living increase for those already on the benefit rolls, there is no question at all that the worker receives protection worth more than his total contributions with interest. This is true even if all or most of the employer contribution is assumed to rest on the employee in final incidence (either in the form of lower wages or in terms of higher prices to him as a consumer). As long as protection for current workers is kept up to date via automatic escalation provisions there is no way for the social security contributor to get better protection for his or her money.

IMPROVING SOCIAL SECURITY FINANCING

Congress keeps a watchful eye on the actuarial balance of the social security system. It has sought, so far as knowledge available at any given time makes possible, to assure the system of adequate financing both for the short run and for the long run. Thus on the basis of all the information available at the time of the most recent amendments, it was thought that the system was adequately financed within a reasonable range for such estimates.

It now appears likely, however, that the system will require some additional financing. The current rate of inflation is so high that benefit increases tied to the cost of living are outrunning the additional income from higher wages. It is estimated that over the next 25 years income to support the cash benefit program will need to be increased by about 10% to 15%. Much less than this will be needed in the early part of this period and more in the latter part. The additional income could come, of course, in part from an increase in the maximum earnings base rather than entirely from the contribution rate or it could come from general revenues rather than from either. In any event, the size of the problem over the next 25 years is easily manageable and certainly does not constitute a financial crisis.

It is possible that in the very long run, say from 2010 on, the active labor force in the United States may be required to support relatively more retired people than was thought to be the case until recently. The fertility rate in the United States has been dropping steadily since 1957 and is now at a point slightly below the rate that would ultimately produce zero population growth. A continuation of fertility rates as low as those experienced in the last few years would mean that the population aged 20 to 65 would stabilize early in the next century but that the number of older people would continue to grow for some time. If this happens it is inevitable, of course, that a higher proportion of goods and services in the next century will need to go to older retired persons as compared with active workers. This is true quite aside from social security and applies equally to other devices for meeting the needs of older people such as private pensions, public assistance, or any other system that might be designed for that purpose.

Fortunately, the same assumptions that produce an increasing burden of support for older people reduce the burden of support for children. Thus active workers will not have to support any more non-workers than they do today as a result of these changed fertility rates, but under the assumptions they will be supporting more older people and fewer younger people.

There are many ways that the next generation may choose to deal with problems caused by an increasing proportion of older people in the population. One approach would be to increase the labor force participation rate for older people and thus reduce the burden of retirement benefits. And then, too, with smaller families more women might work, again reducing the ratio of retired people to active workers. It may be true, too, that over the long run productivity increases in the United States will help meet the problem of supporting an increasing number of older people.

The 1972 amendments provided for the automatic adjustment of benefits in accordance with increases in the cost of living. These amendments also provided that protection for current wage earners would be automatically upgraded as wages and prices changed. The way these provisions work can result in protection over the long run increasing at a rate either more or less than increases in wages, depending on the relative movement of prices and wages. Because of the specific wage and price assumptions used, current cost estimates project that, over the long run, benefit rates at the time individuals come on the rolls will have been increased more than increases in wages.

Congress may wish to consider substituting a formula which assures that protection will automatically keep up with increases in wages but will not exceed such increases. If in the future it seemed desirable for benefits to be increased even more, this could be done by legislation. Such a change in the formula would have two results: One, it would provide workers with a greater certainty that benefits would reflect their level of living at the time of retirement, or disability, or death; and, two, it would result in a substantially lower long-range cost than is shown by the current estimates.

WEIGHING THE ALTERNATIVES AND THEIR COSTS

Congress in the years ahead will by no means confine its attention to the problem of financing, but will examine a wide range of issues about particulars of the system. These particulars reflect past judgments of the best use to which available funds can be put, but those judgments have always been and are now open to reassessment. Some of these issues, however, have been seized upon by current critics of the system with the assertion that present provisions of the law are manifestly unjust and that this supposed injustice somehow affords a reason to abandon social security altogether or to change its basic characteristics as a contributory, earnings-related system. Neither part of this assertion holds water: each of these provisions is the product of a considered weighing of the equities, the costs, and of the arguments pro and con; each of them is subject to change, without disruption of the present system, if change of conditions or change of opinion is found to make that desirable.

THE RETIREMENT TEST

One of the provisions most frequently under attack is the test of retirement. This test, indeed, has been a bone of contention for many years with much support for its abandonment and for the automatic payment of benefits upon attainment of age 65. Basically, social security has been designed as insurance against loss of earnings, and loss of earnings does not occur automatically at age 65. The retirement test is the mechanism that is used to determine whether such a loss has taken place, its effect being reduction or suspension of benefits for periods in which earnings are above stated amounts. The amounts will be increased to keep up to date with rising earnings by the automatic adjustment provisions in present law and, of course, as in the past they may be further increased by amendments to the law, but the present structure of the test is probably as fair a method as can be devised if we are not to abandon retirement altogether as a condition of eligibility.

Some people believe, however, that this condition of eligibility is basically unfair in depriving people of benefits for continuing to work after reaching 65, and that it is undesirable because it stands in the way of people on the benefit roll who wish to supplement their social security income as much as they can. Those who support the retirement test point out that its abolition would cost the equivalent of a one-half of 1% increase in the combined employer-employee contribution rate and would benefit less than one-tenth of the people over 65 who are otherwise eligible for benefits. They ask whether funds in this

amount are better used to supplement the incomes of those who still have substantial earning power or by spreading the funds among the nine-tenths who do not, or cannot, earn enough to bring them within the ambit of the retirement test. Arguments such as these have persisted over the years, but they have no bearing on the soundness or durability of the social security system; abolition of the retirement test would aggravate somewhat the problem of financing, but it would no more spell the doom of the program than does retention of the test. Congress has repeatedly considered this issue and has repeatedly concluded that adaptation of the test in response to rising levels of earnings is preferable to its repeal.

A different attack on the retirement test, however, does have destructive implications. This is the contention that if benefits are withheld on account of earnings, they should also be withheld on account of the receipt of private pension payments, dividends, interest, or other unearned income—in other words, that the payment of benefits should be conditioned on a means test. This change would deprive the program of one of its major strengths, its encouragement of people in their working years to supplement their social security protection through savings and private pension plans. The change, indeed, would in all likelihood mean the end of contributory social insurance, since the masses of self-supporting people would hardly put up with paying social security contributions if they knew they would get nothing in return unless they should ultimately fall into the ranks of the indigent.

SOCIAL INSURANCE—NOT A MEANS-TEST PROGRAM

Mechanisms for preventing destitution in old age or in the event of the death or disability of the family breadwinner are, broadly speaking, of two kinds, contributory and noncontributory. The Nation has chosen contributory social insurance as the primary mechanism, and those who would abandon that system must be prepared to substitute some form of noncontributory aid to those groups in the population who are now eligible for social security benefits.

A 100-percent noncontributory system, lacking the compact between government and contributors that is built into social security, could offer no comparable assurance to working people, or even to those already on the rolls, that the promised benefits would not be curtailed in times of budgetary stringency. Designing such a system, moreover, would raise many thorny questions in specifying who should receive benefits, how large they should be, and how, if at all, their amounts should be varied.

There is an almost infinite variety of theoretical answers to these questions but the hard reality is that a noncontributory system would almost inevitably come to rest upon a means tests so that no one would receive benefits until after poverty had overtaken him. Why, the argument would run, should the general taxpayer support persons who can support themselves if they have made no contribution to their own insurance protection? The experience of public assistance (commonly known as "welfare") augurs ill for the willingness of taxpayers to help their fellow citizens who are thought, rightly or wrongly, to be able in one way or another to support themselves. It is not likely that taxpayers would be willing or that Congress would be willing to compel

them to provide noncontributory benefits without a means test and at a comparable level of adequacy to the thirty million people who now receive social security benefits—the elderly, the disabled, and their dependents, the widows and the widowers, and the motherless or fatherless children.

The benefits these people now receive are earned rights based on their past work and contributions, or on those of family members, thus reflecting their previous standards of living and serving in some measure as a reward for diligence. The benefits are payable without scrutiny of individual means and needs and so permit supplementation by anything the recipients have been able to save. Because they are payable as an earned right, the benefits accord with the self-respect of people accustomed to providing for themselves. It is small wonder that Congress and the people have preferred contributory social insurance to a system benefiting only those who can show themselves to be destitute.

The working portion of our population must, in one way or another, support that portion that is not working and does not have enough resources to meet the cost of living. Most non-working wives and children are supported, in normal course, by family breadwinners. The retired and the disabled, the widows and orphans, on the other hand, commonly have neither family support nor savings sufficient to maintain them, and some governmental mechanism is essential if they are not to be allowed to go hungry.

The ultimate question posed by current attacks on social security is whether the American people should continue to support contributory social insurance which is designed to prevent poverty from occurring, or should place basic reliance on measures to relieve poverty after it has become a fact. Necessary as relief programs are, most of us think them a poor second to prevention.

Critics who say that social security is nothing but a "welfare" program probably intend the remark to be pejorative. If so, in using this word they speak more truly than they know. Social security is indeed "welfare" in the true sense of the word, which is the sense also in which the Constitution uses it. The system was created by an exercise of the power of Congress to raise and spend money to "provide for the . . . general welfare of the United States"—the welfare of all the millions of people who, though now self-supporting, would without social security quickly face destitution if or when earnings cease because of old age or disability, or support ceases because of death of a family breadwinner; as well, of course, as the welfare of the other millions who have already suffered one of these deprivations. "The hope behind this statute," said Mr. Justice Cardozo in 1937, "is to save men and women from the rigors of the poorhouse as well as from the haunting fear that such a lot awaits them when journey's end is near." That hope has been too largely fulfilled to make for tolerance of those who would now destroy it.

Appendix 1¹

ACTUARIAL STATES OF THE TRUST FUNDS

Factors Affecting Long-Range Costs

The estimates of the long-range cost of the Old-Age, Survivors, and Disability Insurance System are for the law as presently written and do not take into account any possible statutory changes in the future. The cost of these provisions as now enacted in the law will depend on demographic factors and on economic factors. It is also important to remember that any future legislation that results in changes in benefits or in the financing provisions will affect the actual cost of the program as it develops and that such changes would, of course, require new long-range actuarial cost estimates.

Table 16 in the section dealing with the expected short-range operations of the trust funds traced the history of the expenditures from the Old-Age, Survivors, and Disability Insurance Trust Funds as a percentage of taxable payroll. Several benefit increases are reflected in the expenditures; and several changes in the taxable earnings base are reflected in taxable earnings, as are changes in the earnings level of covered workers. Table 1 indicates when changes in the taxable earnings base have occurred and what relationship exists between (1) the expenditures as a percent of taxable payroll and (2) the contribution rates by employer and employee.

Substantial general benefit increases are responsible for the marked rise in expenditures as percent of taxable earnings since 1969. These increases are reflected in the percentages even after the substantial increases in the taxable earnings base that were enacted.

Long-Range Cost Estimates

The long-range cost estimates for the Old-Age, Survivors, and Disability Insurance System presented in this Report are computed under dynamic assumptions with respect to the future levels of the benefits and of the taxable earnings base. These assumptions are based on the automatic adjustment provisions in present law. The estimates do not take into account any other possible future modification in either the benefits or the financing.

The amendments to the Social Security Act enacted in 1972 and 1973 included financing schedules based on dynamic assumptions as recommended by the 1971 Advisory Council on Social Security. Estimates based on such dynamic assumptions basically assume that the provisions for automatically adjusting the benefit table in accordance with the Consumer Price Index and for automatically adjusting the taxable earnings base in accordance with the increase in covered earnings per worker will continue to be a part of the structure of the system.

Tax schedules based on such dynamic assumptions provide the financing needed to increase the benefit table in step with the Consumer Price Index. However, increases beyond those provided under the present law that may be enacted in the future will require additional financing.

Table 20 compares the long-range average-cost of the Old-Age, Survivors, and Disability Insurance System over the 75-year projection period (1974-2048) with the average rate in the tax schedule in present law. Under the above set of assumptions, the OASDI System

¹ Excerpt from the 1974 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, 93d Congress, 2d Session, House Document No. 93-313, pp. 34-38.

is shown to be underfinanced over the long-range, with a negative actuarial balance of about 3 percent of taxable payroll. This underfinancing is almost proportionately distributed between the two programs. Both OASI and DI have a long-range actuarial deficit equivalent to about 21 percent of their costs.

TABLE 20.—ESTIMATED ACTUARIAL BALANCE¹ OF OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE SYSTEM AS PERCENT OF TAXABLE PAYROLL,² DYNAMIC ASSUMPTIONS³

[In percent]			
Item	OASI	DI	Total
Average-cost of system.....	11.97	1.92	13.89
Average rate in present tax schedule.....	9.39	1.52	10.91
Actuarial balance.....	-2.58	-.40	-2.98

¹ As measured over the 75-year period, 1974-2048.

² Payroll is adjusted to take into account the lower contribution rates on self-employment income, on tips, and on multiple-employer "excess wages" as compared with the combined employer-employee rate.

³ See text for a description of the assumptions.

The results in table 20 are based on new actuarial assumptions as compared to those used in the past with respect to demographic factors as well as to economic factors. In regard to demographic factors, new population projections were prepared based on the results of the 1970 census under the assumption of significantly lower future fertility which have substantially affected the actuarial balance, as may be observed from table 21.

With respect to the economic factors, it is assumed that:

(a) The benefit table will be adjusted after 1974 to reflect increases in the Consumer Price Index.

(b) The taxable wage base and the exempt amount under the earnings test are both adjusted after 1974 to reflect increases in average earnings.

(c) Through 1980 the assumptions are similar to those used in developing the short-range cost estimates under Alternative I, which are presented earlier in this Report.

(d) Beyond 1980, the CPI will increase at an annual rate of 3 percent, while average earnings will increase at 5 percent.

The results in table 20 should be read with full recognition of the uncertainties involved in the projection of economic factors over long-range periods. Because of the sensitivity of the projections to changes in economic assumptions, as illustrated in Appendix Table D, these results are subject to wide margins of variation.

As compared with the long-range cost estimates prepared last fall when the Social Security Amendments (P.L. 93-233) were under consideration, the present estimates show substantially higher costs. These higher costs are attributed mostly to a change in the population projections that are used to project the costs of the social security programs. The new projections are based on an ultimate total fertility rate of 2.1 babies per woman, which is close to population replacement rates, while the previous projections were based on ultimate rates of 2.3 and 2.8 babies per woman. The lower fertility rate that is now being projected results in a higher projected ratio of aged persons in the population to workers and therefore in higher costs to the program expressed as a percentage of payroll.

Although most of the increase in cost is expected to occur after the turn of the century (when the effects of the changes in the population projections are fully felt), part of it will already occur within the next few years, thereby producing a marked decline in the near future in the ratio of assets to expenditures in the absence of an immediate increase in income to both the OASI and DI Trust Funds. In the very short run (for the next 5-10 years) a reallocation of the current contributions could cover this problem. The overall OASHDI contribution rate in present law would be enough, if reallocated, to adequately support all three trust funds (OASI, DI and HI) during this period. However, after the next 5-10 years, a tax increase or constraints in the growth of benefits will nonetheless be needed for each of the three programs.

Another important factor that has affected the long-range cost of the program is the recent increase in the number of disabled-worker benefits that are being awarded. As was indicated in last year's report, a significant increase in the disabled-worker benefit awards has been experienced since 1971. The present cost estimates incorporate all the increases that have been experienced through the end of calendar year 1973.

As shown in table 21, other factors affecting the cost of the program are changes in economic assumptions, which include modifications in the projected labor-force participation rates and unemployment rates, short-range assumptions regarding increases in average earnings, and both short-range and long-range assumptions regarding increases in the CPI (with the long-range assumptions changing from 2-3/4% to 3%), as well as the elimination of the 3/8 percent margin used in previous long-range cost estimates. The remaining itemized factor affecting the actuarial balance is a small increase in the rates of retirement among the eligible aged population that has been observed in the last two years.

TABLE 21.—CHANGE IN OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE LONG-RANGE ACTUARIAL BALANCE AS PERCENT OF TAXABLE PAYROLL¹ BY TYPE OF ASSUMPTION

[In percent of taxable payroll]

	Old-age and survivors insurance	Disability insurance	Total
Actuarial balance under previous estimates.....	-0.43	-0.08	-0.51
Retirement rates.....	-.14		-.14
Disability rates.....		-.21	-.21
Population assumptions.....	-1.79	-.08	-1.87
Economic assumptions.....	-.18	-.01	-.19
All other factors (net).....	-.04	-.02	-.06
Change in actuarial balance.....	-2.15	-.32	-2.47
New actuarial balance.....	-2.58	-.40	-2.98

¹ Represents the difference over the 75-year period, 1974-2048, between the average tax rate and the average cost.

² Payroll is adjusted to take into account the lower contribution rate on self-employment income, on tips, and on multiple-employer "excess wages" as compared with the combined employer-employee rate.

Table 22 shows the current-cost of the OASDI System (including the cost of maintaining one year's expenditures on hand) for selected years over the next 75 years, expressed as percent of taxable payroll, in accordance with the dynamic actuarial assumptions.

It may be observed that the annual cost of the Old-Age, Survivors, and Disability Insurance System is projected to increase slowly throughout the remainder of this century and that after the turn of the century it will increase rapidly until leveling at about 17-18 percent of taxable payroll after the year 2025.

According to the present 75-year projections, the cost of the Old-Age, Survivors, and Disability Insurance System could be divided into three periods of 25 years each. The first period is projected to be a period of slowly increasing costs. The second period involves fast increases in cost, while the third period is characterized by high but level costs.

TABLE 22.—ESTIMATED "CURRENT-COST"¹ OF OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE SYSTEM AS PERCENT OF TAXABLE PAYROLL² UNDER DYNAMIC ASSUMPTIONS,³ FOR SELECTED YEARS, 1985-2045

[In percent]

Calendar year	Old-age and survivors insurance	Disability insurance	Total
1985	9.00	1.44	10.44
1990	9.52	1.51	11.03
1995	9.64	1.61	11.25
2000	9.54	1.77	11.31
2005	9.72	1.97	11.69
2010	10.56	2.13	12.69
2015	11.82	2.22	14.14
2020	13.47	2.24	15.71
2025	14.78	2.19	16.97
2030	15.46	2.14	17.60
2035	15.49	2.19	17.68
2040	15.49	2.28	17.68
2045	15.53	2.33	17.86
Average cost ⁴	11.97	1.92	13.89

¹ Represents the cost as percent of taxable payroll of all expenditures in the year, including amounts needed to maintain the funds at about 1 year's expenditures.

² Payroll is adjusted to take into account the lower contribution rate on self-employment income, on tips, and on multiple employer "excess wages" as compared with the combined employer-employee rate.

³ See text for a description of the assumptions.

⁴ Represents the arithmetic average of the "current-cost" for the 75-year period 1974-2048.

The increasing costs in the second period as well as the high costs in the third period are due principally, but not totally, to the demographic effect of the projected large aged population as compared to the working population. Some of the cost, however, is due to what could be considered anomalies in the automatic benefit adjustment provisions in present law. As is discussed in the appendix and as may be noted from Appendix Table C, the present automatic provisions are projected to result in awarded benefits that would increase faster than average earnings in the future. The differential in trends between average awarded benefits and average covered earnings would be relatively minor during this century (because of the way benefits are calculated under present law), but it is projected to increase substantially thereafter.

The Board of Trustees has suggested to the Department of Health, Education, and Welfare that the present Advisory Council be asked to study this matter, as well as other ways of dealing with the emerging long-range actuarial status of the trust funds.

CONCLUSION

The long-range actuarial cost estimates for the old-age, survivors, and disability insurance program prepared in accordance with dynamic assumptions as to both benefits and taxable earnings show an actuarial balance of -2.98 percent of taxable payroll over the valuation period of 75 years, which substantially exceeds the acceptable limit of variation of 5 percent of the cost of the program (0.69 percent of taxable payroll).

The principal reason for the increase in the actuarial imbalance, as compared to that reflected by the cost estimates used last fall by the Congress, is a change in the long-range population projections underlying the cost estimates, which are now based on the results of the 1970 Census and on lower future fertility assumptions than were previously used for such projections.

Although the new population and fertility projections will have a major impact after the turn of the century on the long-range cost estimates, they will not have a significant effect in the short run. According to present short-range cost estimates, action to increase the combined income of the OASDI and hospital insurance systems for the next 5-10 years is not necessary right now. Although, when considered separately, the Disability Insurance Trust Fund and, to some extent, the Old-Age and Survivors Insurance Trust Fund decline in terms of both absolute dollar amounts and as a percent of outgo, the Hospital Insurance Trust Fund is increasing more rapidly than previously projected, with the result that it is developing an excess of funds. The Board noted that one of the possible ways that the projected short-range excess of outgo over income in the cash benefit funds can be avoided is a reallocation of the total program income among the three funds (OASI, DI, and HI) by revising the contribution rates scheduled in present law without increasing the total rate. However, in order to maintain the HI Trust Fund in actuarial balance, any reduction in the HI tax rates in the early years would have to be offset by compensatory increases in later years.

The present assumptions as to the rate of increase in the CPI, in both the short-range and the long-range estimates, assume some deceleration from recent rates of increase. If this deceleration does not occur, or occurs more slowly than assumed, the reallocation noted above may not be sufficient over the next 5-10 years to prevent a decline in the funds. And, of course, if such deceleration does not occur and if, as is assumed, recent fertility trends should continue, the additional financing needed over the long-range will be increased.

Although there is of necessity a considerable degree of uncertainty inherent in the long-range demographic and economic assumptions and consequently in the projections that flow from those assumptions, it is certain that additional income to the cash benefits program or some adjustment in the benefit structure will be needed eventually. However, in view of this inherent uncertainty and the fact that the newly appointed Advisory Council on Social Security is studying the long-range financial status of the social security system, the Board is not recommending a specific increase in the combined OASDHI contribution rates scheduled in present law. The Board believes that there is ample time to await the Council's findings and recommendations before making specific proposals.

Appendix 2

PRESS RELEASE GIVING ADDITIONAL INFORMATION ON WHITE PAPER¹ ON SOCIAL SECURITY

Calling recent attacks on the social security program "a disservice to the Nation," five former Health, Education, and Welfare Secretaries and three former Social Security Commissioners—representing both political parties—joined today in endorsing a white paper that is designed to provide the basis for informed public discussion of changes and improvements needed to keep social security soundly financed, equitable, and up to date with the times.

The group hopes that the paper will be widely reprinted by newspapers, magazines, private organizations, and company publications for employees—and read by every citizen.

Those signing the 10-page white paper, "Social Security: A Sound and Durable Institution of Great Value," are former HEW Secretaries, Elliot L. Richardson, John W. Gardner, Wilbur J. Cohen, Robert H. Finch, and Arthur Flemming, and all three surviving former Social Security Commissioners, Robert M. Ball, William L. Mitchell, and Charles I. Schottland.

The development of the paper was originally prompted by a rash of newspaper and magazine articles casting doubt on the soundness and durability of the social security system. The authors of the paper characterize such attacks as "a disservice to the Nation."

The white paper points out that there are two financial problems facing social security which will need to be dealt with. One is the relatively short-term problem caused by the current high rate of inflation and which will require about 10 to 15 percent more income for social security over the next 25 years than had previously been anticipated. The second problem, which occurs largely in the next century, grows out of the fact that it now appears likely fertility rates will continue to be lower than had previously been assumed, with the result that in the long run there will be more retired persons drawing social security benefits in comparison to those of working age than had previously been estimated to be the case. The white paper points out that "the size of the problem over the next 25 years is easily manageable and does not constitute a financial crisis."

There is also sufficient time to deal with the long-run change in the ratio of retired people to active workers. If that situation comes to pass, the white paper points out, it will not affect just the social security program but our whole economy and way of life. And there will be offsetting factors—if the burden of supporting older people is increased, the burden of supporting and educating children will be reduced, and with smaller families more women will be able to work.

¹ The text of the white paper appears as part 2 of this paper.

An Advisory Council on Social Security is now concluding its review of the social security system, a review required by law every 4 years. Although this Council's report and recommendations will be submitted to the Secretary of HEW and to the Congress in about a month, the group of former HEW and Social Security officials feel that their paper should be given wide circulation now.

"We may well await the recommendation of this Council and ensuing congressional hearings on substantive changes in the system which are being widely debated," the paper notes, "but we should not wait to deal with irresponsible attacks on the soundness of the structure."

In addition to matters of social security financing, the white paper deals with the nature of the congressional commitment to the program's continuance and the assurance of future benefit payments; the nature of social security as social insurance; whether the worker could get a better buy if he invested his social security contributions on his own (he can't); the retirement test; and the "ultimate question"—whether the American people should continue to support contributory social insurance which is designed to prevent poverty from occurring, or should place basic reliance on relief programs that treat poverty after it has become a fact.

