

**Testimony of Stephen C. Goss, Chief Actuary, Social Security Administration
To the Committee on the Budget, U.S. House of Representatives
Wednesday July 13, 2011
Medicare and Social Security: The Fiscal Facts**

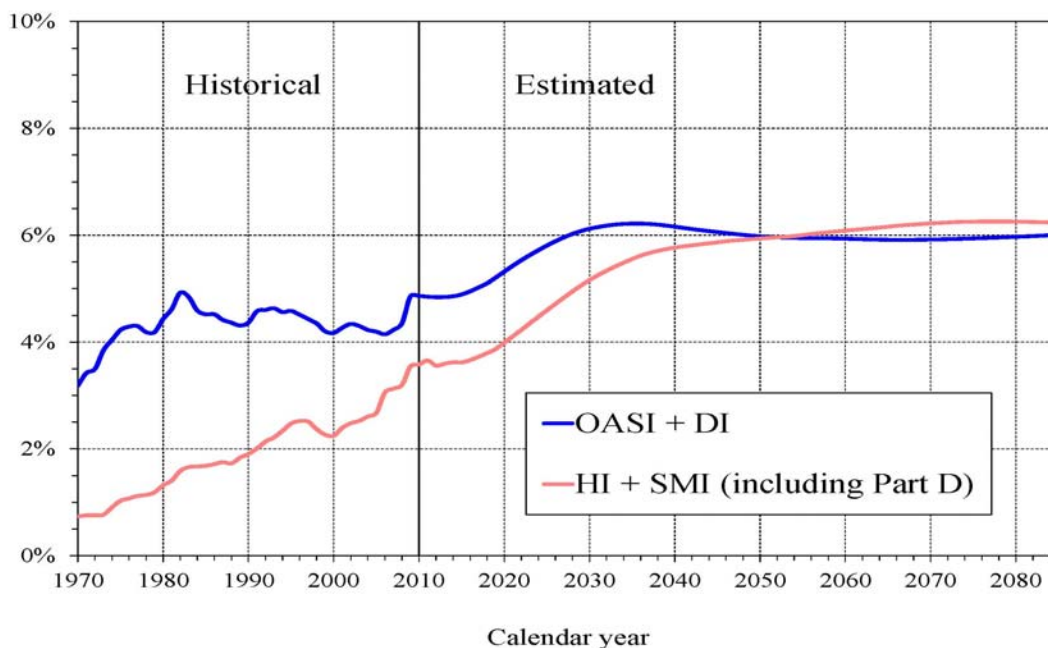
Chairman Ryan, Ranking Member Van Hollen, members of the committee: thank you for the opportunity to discuss with you today the fiscal status of these programs. The 2011 Annual Reports issued by the Boards of Trustees on May 13 have clearly laid out the projected future cost and financing for these programs under current law and our best assessment of future economic and demographic conditions.

We must consider two fundamental questions in developing any future changes for the Social Security and Medicare programs.

- The first relates to the level of cost for these programs in the national economy. This is simply a question of what we want from these programs and how much are we willing to pay. “**Program sustainability**” depends on our addressing both what we want and what we are willing to pay -- and finding the balance that the American people desire.
- The second is whether scheduled financing is sufficient to pay the scheduled cost of these programs in the future. This is the “**Trust Fund solvency**” perspective and is the central focus of the annual reporting of the Trustees. The law requires that the Trustees report on the actuarial status of the Trust Funds.

Let me first address *Program Sustainability*, which may best be considered by looking at the cost of these programs expressed as a percentage of Gross Domestic Product (GDP).

Projected Cost of Social Security and Medicare as Percent of GDP



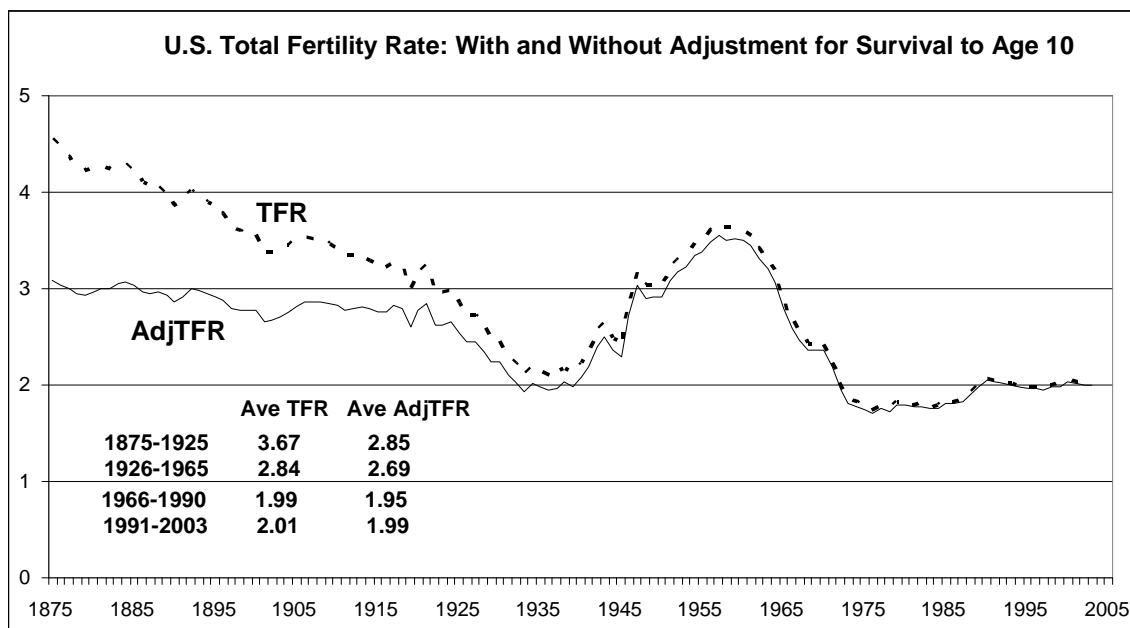
In 2008, prior to the effects of the recent economic recession, Social Security expenditures were 4.3 percent of GDP and Medicare expenditures were 3.2 percent of GDP. Social Security expenditures were essentially stable at about 4.3 percent of GDP from 1975 through 2008. Medicare expenditures rose from 1 percent of GDP in 1975 to 3.2 percent in 2008. The cost of both programs as a percent of GDP rose temporarily in 2009 due to the economic recession.

The fundamental *Program Sustainability* issue for these programs is illustrated by the projected future growth in cost as percent of GDP under the Trustees' intermediate assumptions. The cost of providing benefits scheduled in current law is projected to rise to about 6 percent of GDP for each of these programs by 2040. Social Security cost increases by about one-third and Medicare cost nearly doubles. The Congress, on behalf of the American people you represent, will need to decide whether (a) we are willing to pay 12 percent of GDP to maintain currently scheduled benefits, or (b) we will accept lower benefits at lower cost.

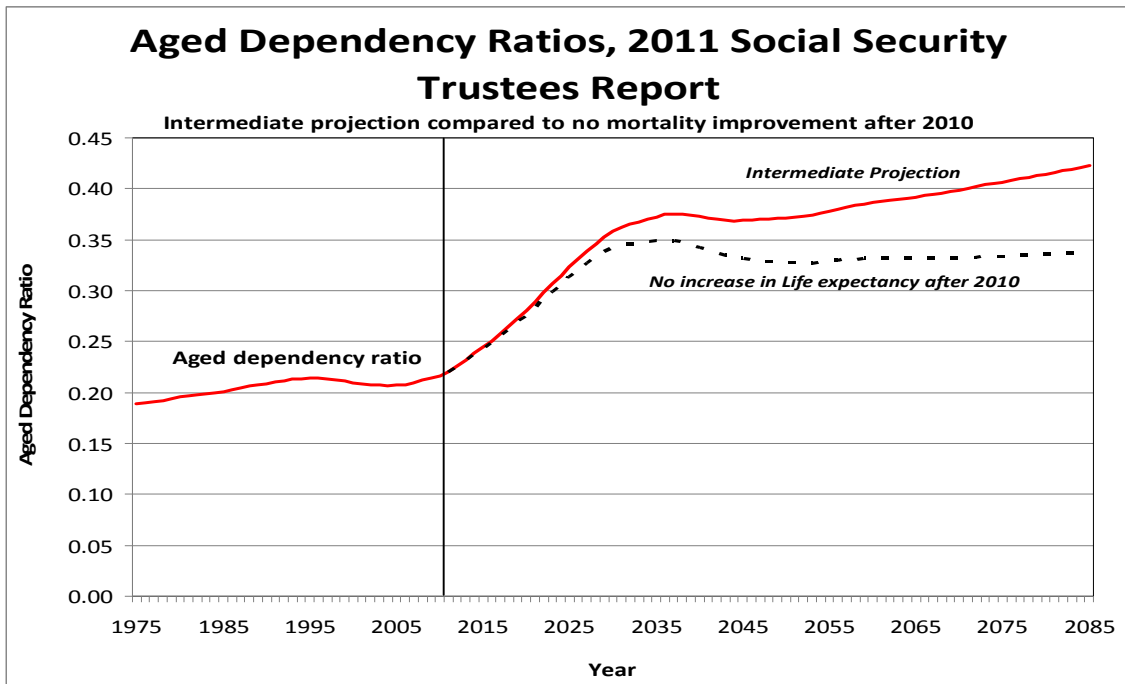
Why is Program Cost Projected to Shift to a New Level by 2040?

The projected shift up in cost by 2040 for both programs is largely due to the aging of our population. The "baby boomers" born in 1946 through 1965 will be moving from working age to retirement age during this period. However, the reason the population as a whole is aging is that birth rates dropped after 1965, leaving relatively fewer people entering the workforce just as the boomers are retiring. Lower birth rates are the cause of this substantial and permanent shift in the cost of Social Security as a percent of GDP from 2008 to 2040. Lower birth rates are also a large part of the cause for the increase in Medicare cost as a percent of GDP over the same period.

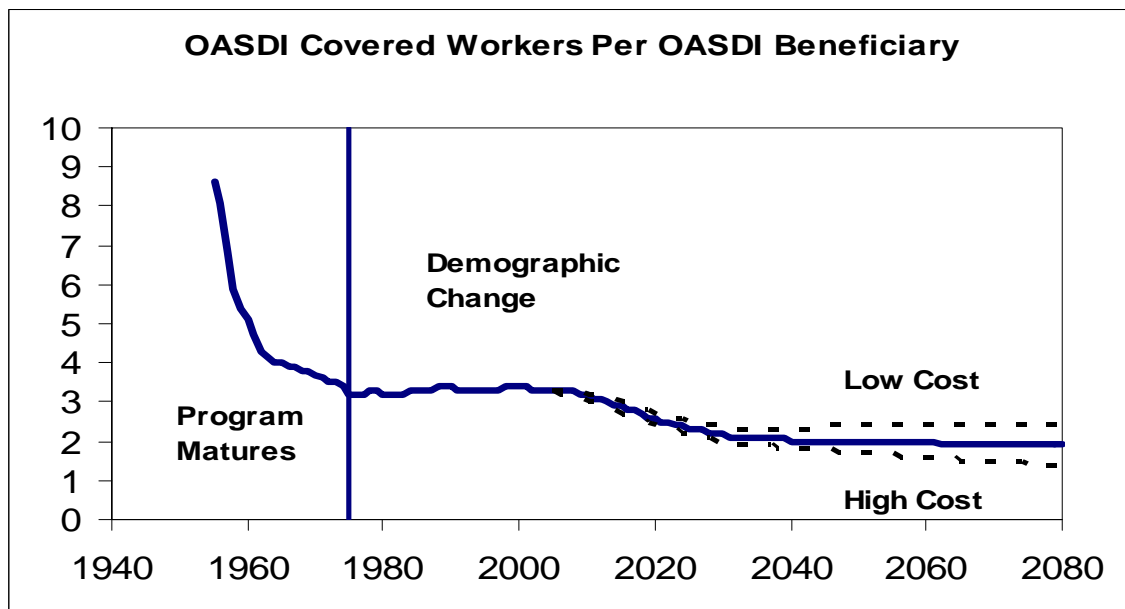
The adjusted total fertility rate (TFR) dropped from a long-term historical average level of about 3 children per woman surviving to age 10 to just 2 children per woman by 1975, and is expected to remain at this lower level. If birth rates had remained at around 3 children per woman after 1965, the cost of Social Security would not be shifting up in the future.



This drop in birth rates fundamentally changes the age distribution of our population for the future, meaning more people at age 65 and over compared to the number at working age, 20-64. (The ratio of population age 65 and over to that aged 20-64 is referred to as the aged dependency ratio.) Improving life expectancy has a much more gradual effect on this ratio.



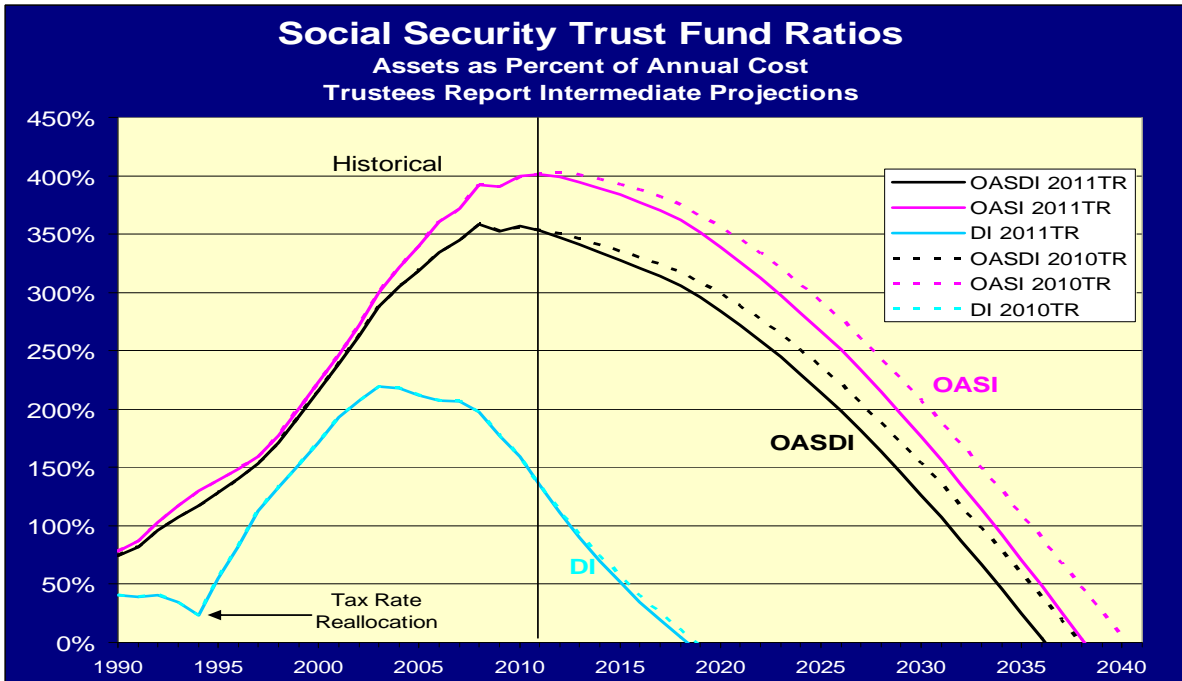
The changing age distribution of the population directly affects the numbers of workers we will have for each beneficiary in the future.



The timing of the level shift in the cost of these programs as percent of GDP and the timing of the increase in the ratio of aged to working age population is no coincidence.

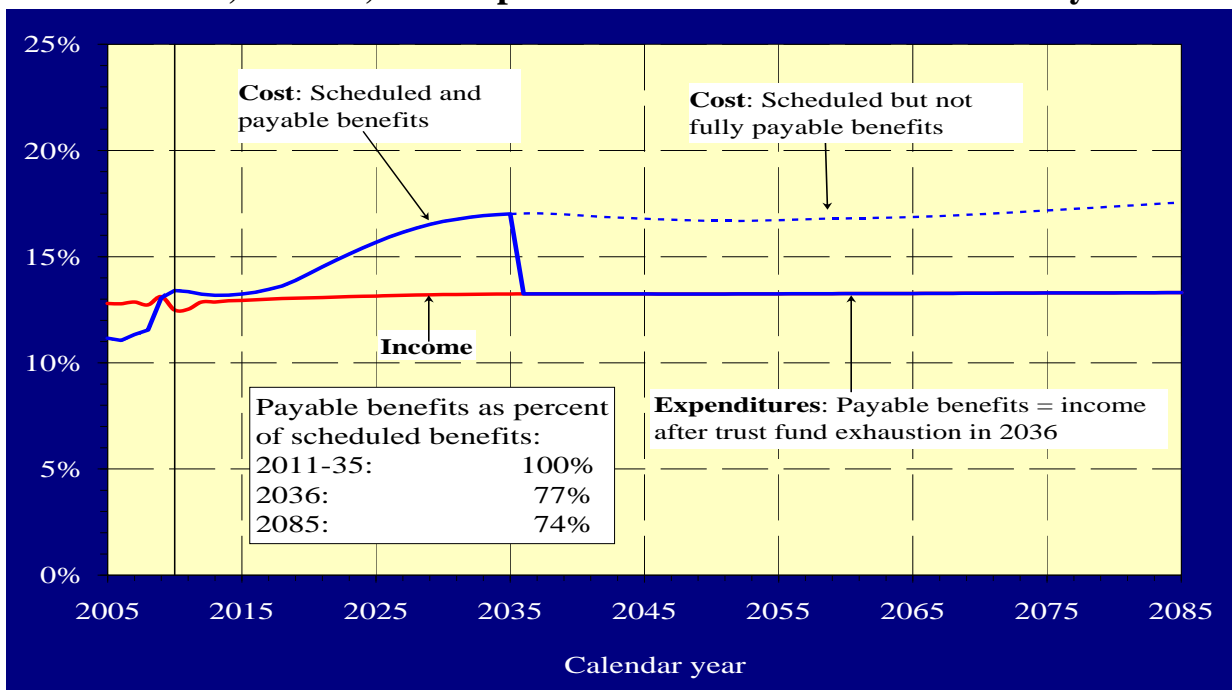
Trust Fund Solvency

Solvency requires a positive level of assets in order to pay scheduled benefits. Unlike most other Federal programs, the “trust fund” programs have NO borrowing authority.

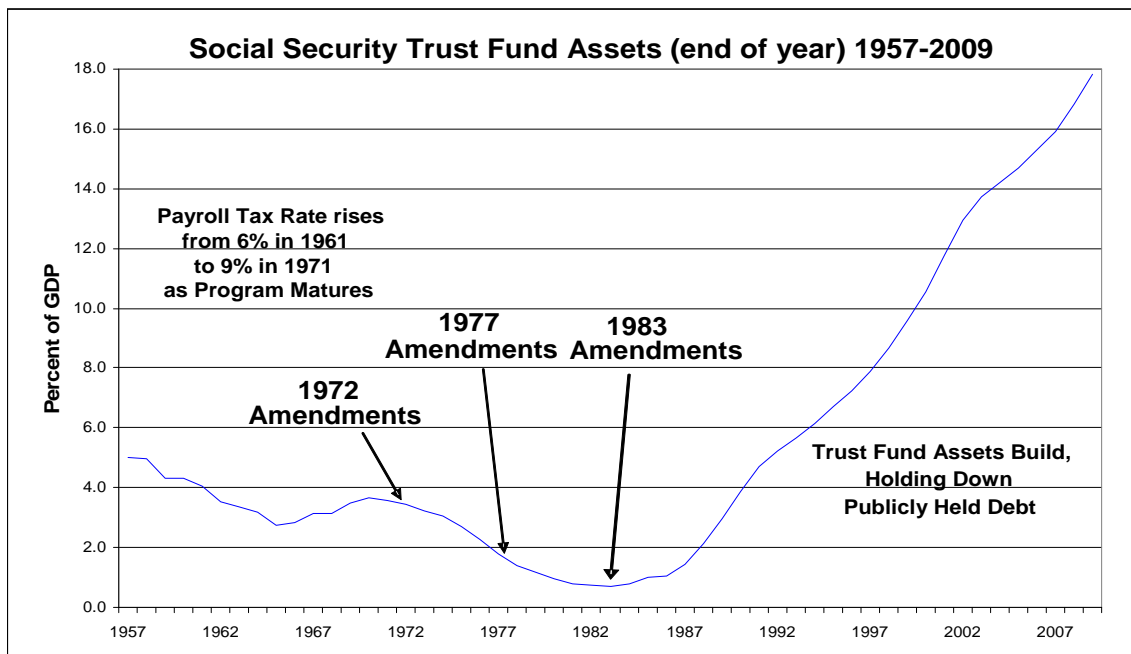


If a trust fund becomes exhausted, expenditures are limited to current revenue. For the Social Security OASI and DI Trust Funds this is critical. Should the combined OASI and DI Trust Funds become exhausted in 2036, only 3/4ths of scheduled benefits will be payable.

OASDI Cost, Income, and Expenditures as Percent of Taxable Payroll



This inability to borrow for the trust funds has forced congressional action in the past so that aggregate trust fund assets have always remained positive.



OASDI Trust Fund assets that were about 5 percent of GDP in 1957 declined to less than 1 percent of GDP by 1983, when the second of two major reforms was enacted to preserve solvency for the trust funds. Trust fund assets for OASI and DI have now risen to over 16 percent of GDP but will decline until exhaustion in 2036. Congressional action is needed again, before 2036, to maintain solvency for the OASDI Trust Funds.

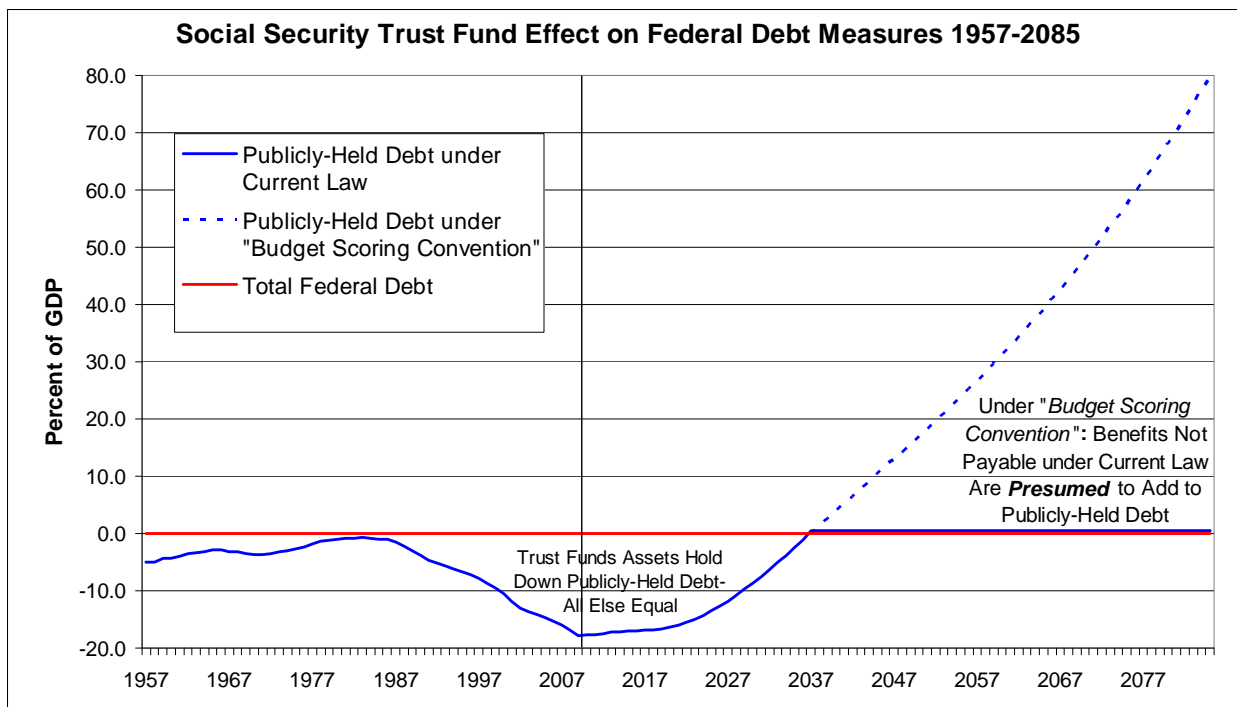
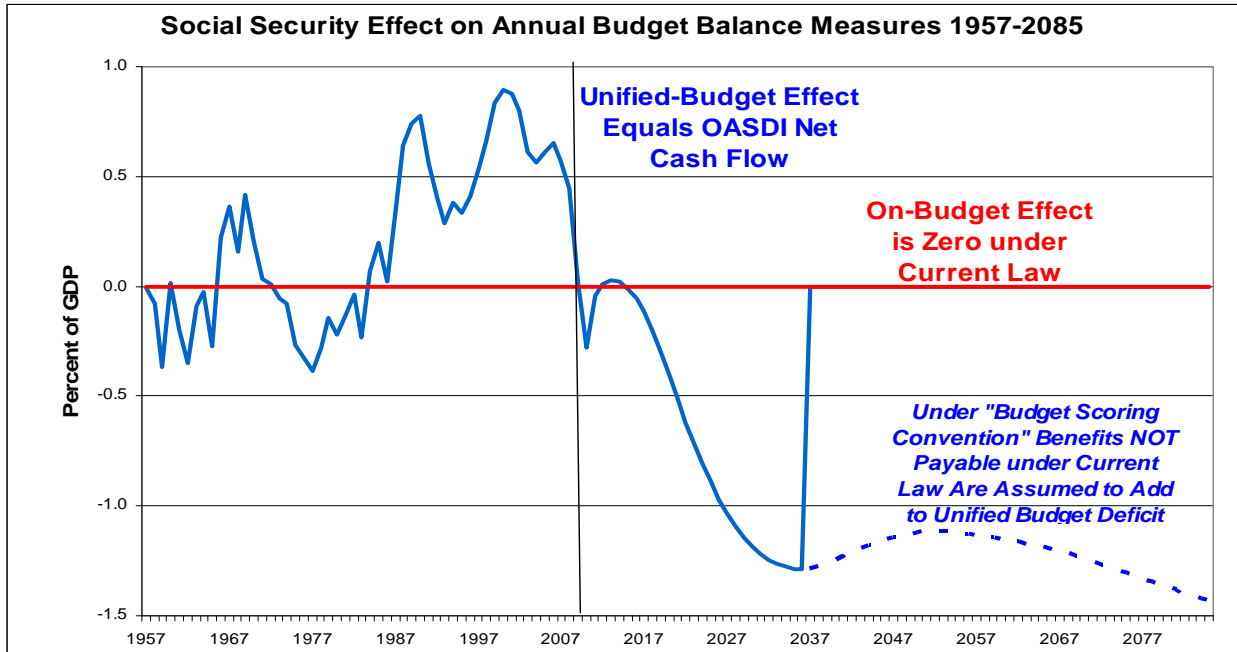
For years after 2036, we need to either (1) increase OASDI income by one-third, (2) reduce scheduled benefit cost by one-fourth, or (3) enact some combination of these changes. Enacting changes relatively soon, even if the changes were not implemented for some years into the future, would provide advance notice for those who will be affected, and would remove uncertainty about the solvency of the program for the future. The 1983 Social Security Amendments provide a good example. These amendments included an increase in the normal retirement age that did not begin to be implemented until 17 years after enactment.

Effects of Social Security on the Federal Budget and Federal Debt

There are two important facts to note about budget accounting for these trust-fund programs.

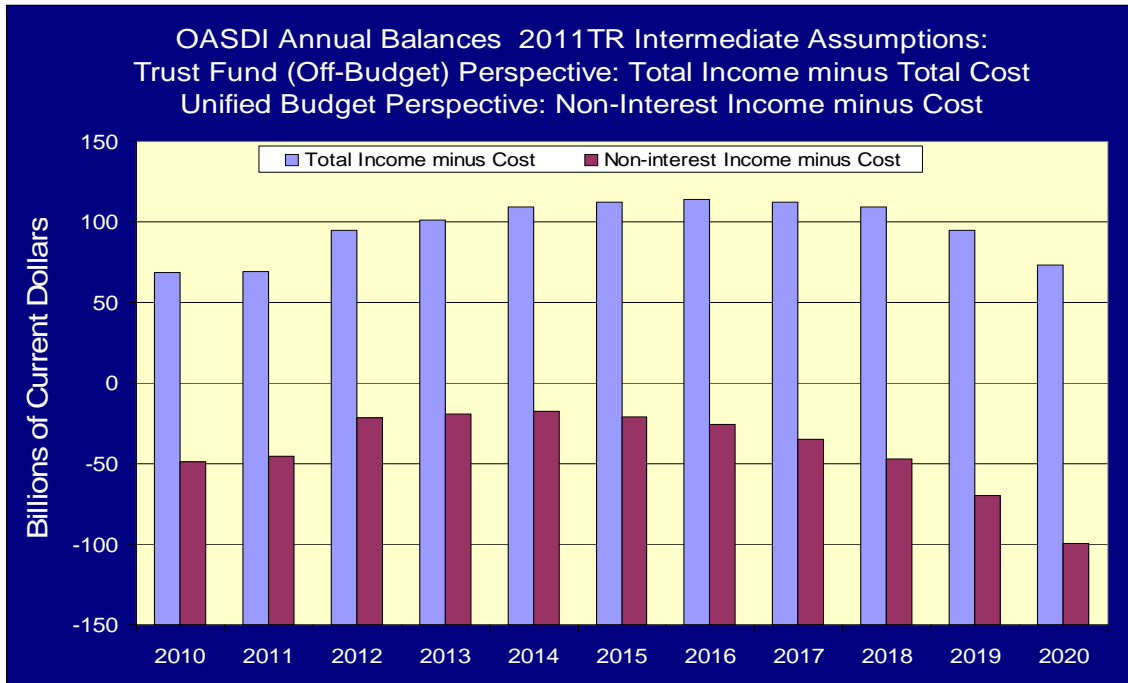
- First, assets in the trust funds have been borrowed by the rest of the government in lieu of additional borrowing directly from the public. Publicly held debt, currently about \$10 trillion, is lower than the total Federal debt of about \$14 trillion solely due to the borrowing from the trust funds. If the trust funds had not run cumulative surpluses, loaning \$4 trillion to the Treasury, then the General Fund would now have \$14 trillion in publicly held debt. Social Security financial operations and assets thus have no direct effect on either on-budget operations or total Federal debt subject to the ceiling.

- Second, the budget scoring convention that reflects shortfalls in Social Security financing after the trust funds are exhausted is inconsistent with the law. Because the trust funds have no borrowing authority, financial shortfalls after trust fund exhaustion would not be met. Such shortfalls would not cause either the increase in unified budget expenditures or the increase in publicly held debt that are presumed under budget scoring convention.

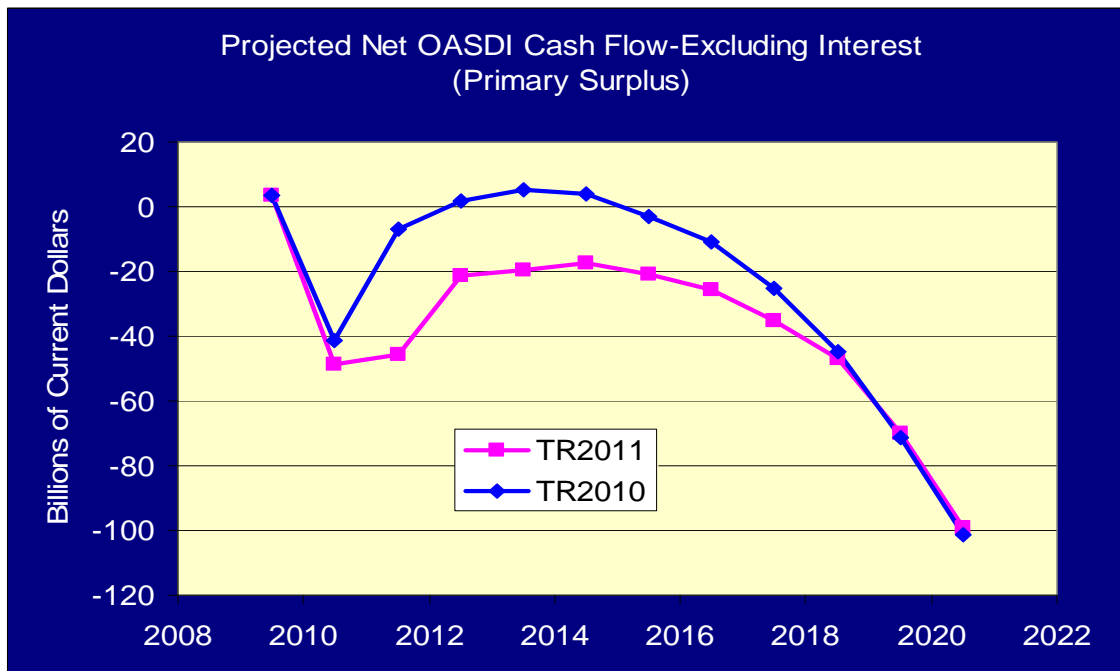


Social Security Financial Operations in the 2011 Trustees Report

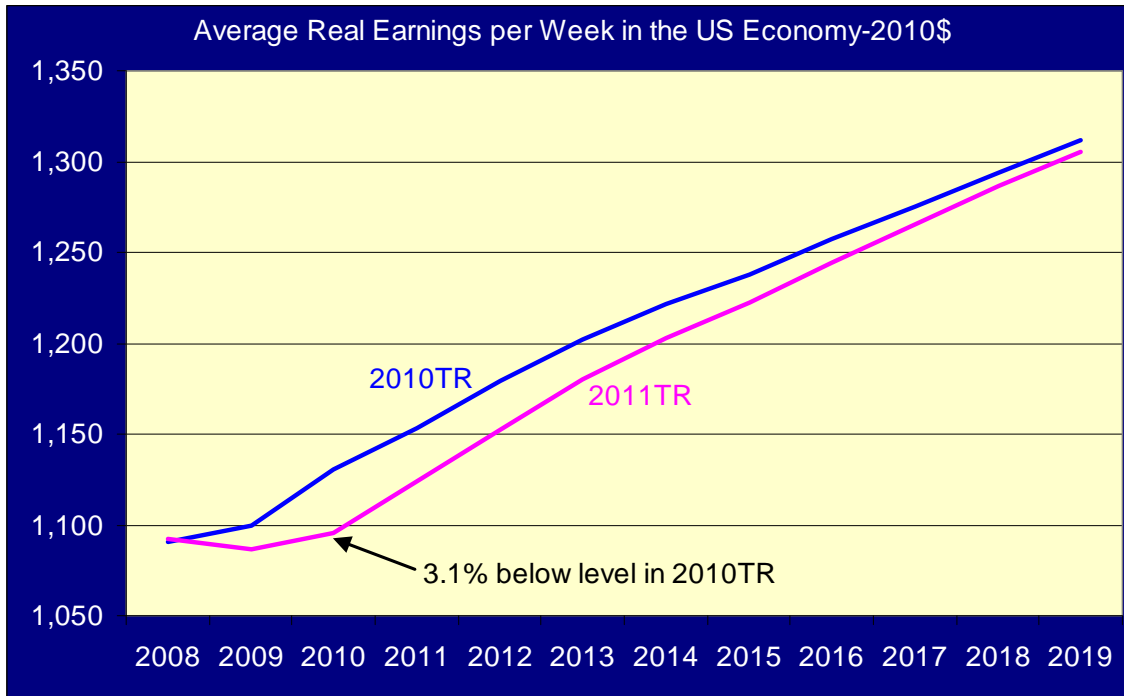
Total income for the combined OASI and DI Trust Funds, including interest, is projected to exceed program cost until 2023. Thereafter, the combined assets are projected to decline and become exhausted in 2036. OASDI net cash flow—excluding interest, consistent with a unified budget perspective—turned negative in 2010 due to the recent recession and slow recovery.



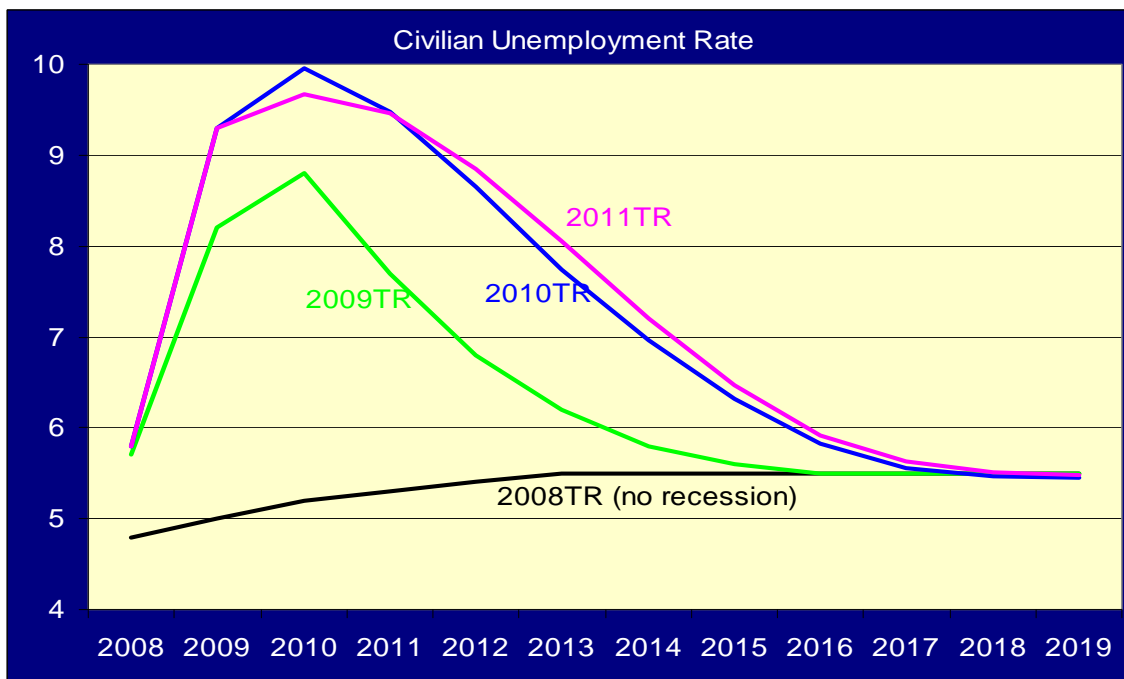
In the 2010 Trustees Report, a small positive net cash flow was projected for OASDI for 2012-14. Net cash flow in the 2011 report is projected at about \$20 billion lower for each of these years due to slower economic recovery, principally due to lower levels of average real earnings for workers.



While real GDP for 2010 was 0.4 percent below the projection in the 2010 report, average real earnings turned out to be 3.1 percent lower than expected. For 2013, the 2011 report projects real GDP to be 1.6 percent lower and average real earnings to be 1.9 percent lower than in the prior report.

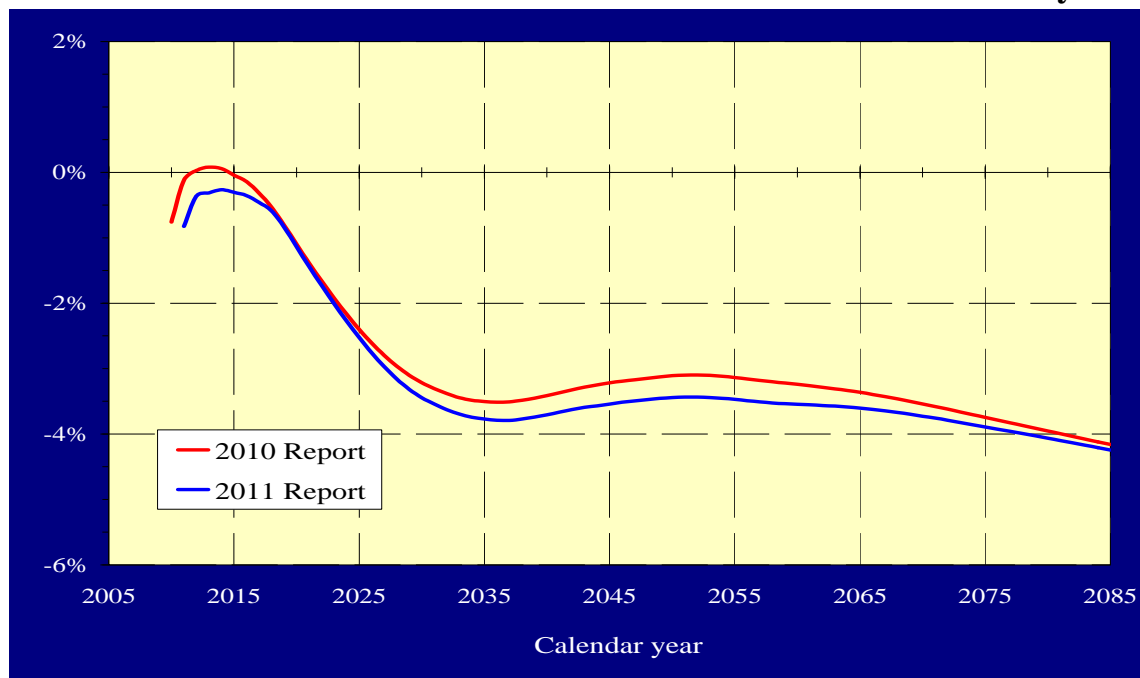


For the 2011 report, the Trustees assumed a slightly slower decline in the civilian unemployment rate, reaching the assumed ultimate average level of 5.5 percent by 2018.



Beyond 2020, OASDI annual balances (non-interest income minus cost as a percent of taxable payroll) are projected to be slightly lower for the 2011 report reflecting (1) lower than expected recent death rates for those age 65 and over and (2) lower than expected net immigration. Changes in life expectancy and net immigration explain most of the increase in the long-range OASDI actuarial deficit from 1.92 percent of payroll in the 2010 report to 2.22 percent of payroll in the 2011 report. These changes, along with the slower than expected economic recovery, resulted in projected trust fund exhaustion for 2036, one year earlier than was projected last year for the combined OASDI Trust Funds. The exhaustion date for the OASI Trust Fund is projected to be 2 years earlier, in 2038. The projected exhaustion date for the DI Trust Fund is unchanged at 2018.

OASDI Non-Interest Income Minus Cost as Percent of Taxable Payroll



Conclusion

We are at the beginning of a substantial and permanent shift in the age distribution of our population. The drop in birth rates from the long-time average level of about 3 children per woman through 1965, to just 2 children per woman since 1975, is responsible. By 2040, there will be only 2 workers for every OASDI beneficiary, down from 3 workers per beneficiary throughout the period 1975 through 2008. As a result, the cost of Social Security will shift from 4.3 percent of GDP in the period 1975 through 2008 to a stable level of 6 percent of GDP by 2040. Currently scheduled tax revenue will remain at about 4.5 percent of GDP. *Program Sustainability* will therefore require a choice to:

- Increase revenue by 33 percent after 2035,

- Reduce benefits by 25 percent after 2035, or
- Enact some combination of these changes

In the absence of legislation, the combined OASDI Trust Funds are projected to become exhausted in 2036, with only 75 percent of presently scheduled benefits being payable thereafter through 2085. Projected trust fund exhaustion is now 1 year earlier than in the 2010 report largely because of lower recent mortality and net immigration, and a slower than expected economic recovery.

Social Security total income will continue to exceed expenditures, causing the trust fund assets to grow, until 2023. Social Security non-interest income is now expected to be permanently below program cost starting in 2010, 5 years earlier than expected a year ago. Positive net cash flow of less than \$10 billion for each year 2012 -2014 projected in the 2010 Trustees Report has been replaced with projected negative net cash flow of less than \$20 billion for each of these years. While real GDP grew 0.4 percent less in 2010 than expected a year ago, the average real earnings of workers grew by 3.1 percent less.

Social Security and other trust fund programs are subject to a special constraint that does not exist for other Federal programs. The Trust Funds have no borrowing authority, so these programs must always maintain a positive cumulative net cash flow -- a positive asset level. If trust fund assets were ever to become exhausted, payable benefits would be limited to the continuing revenue of the program. In the case of Social Security, only about 75 percent of scheduled benefits would be payable after 2035. Congress has always taken action in order to prevent the precipitous drop in benefits that would be required at exhaustion of a trust fund.

Budget scoring convention presumes that Social Security shortfalls after trust fund exhaustion would be made up with revenue from the General Fund of the Treasury, requiring extensive borrowing from the public. In fact, the law would not permit this. If currently scheduled benefits are to be paid after 2035, the Congress will need to pass legislation providing more revenue. Graphs of the theoretical growth in publicly held debt after trust fund exhaustion based on the presumption that full benefits would continue with additional revenue from the General Fund of the Treasury may be impressive. However, the reality of a precipitous drop in benefits at trust fund exhaustion has actually proven to be a more certain motivation for Congressional action.

The total Federal debt subject to ceiling includes the amounts the Treasury has borrowed and owes both directly to the public and indirectly to the public through the trust funds. In the absence of the actual asset accumulation by the trust funds, the Treasury would simply have needed to borrow that much more directly from the public. The total debt subject to ceiling therefore depends entirely on the net past cash flows of all of the Federal programs that do not have trust funds. Changes in Social Security income and spending do not and will not have a direct effect on the total debt subject to ceiling.

Chairman Ryan, Ranking Member Van Hollen, and members of the committee, all in my office look forward to continued work with you and all members of the Congress in the development of legislation that will restore long-range sustainable solvency for the Social Security Trust Funds.