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TESTIMONY

Social Security's Finances

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Committee on Ways and Means
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Chairman Ferguson, Ranking Member Larson, and Members of the Subcommittee, thank you for inviting me to testify about the Social Security program.

Social Security faces a significant financial challenge in the coming decade. Its two components, Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI), are financed by revenues from payroll taxes and from income taxes on Social Security benefits. But those revenues, which are credited to the components' separate trust funds, are not sufficient to cover the benefits that are due under the program.

- In the Congressional Budget Office's projections, the balance of the OASI trust fund reaches zero in fiscal year 2033, and the DI trust fund is exhausted in 2061. If the two trust funds were combined, they would be exhausted in fiscal year 2034.
- The trust fund balances would be sufficient to pay benefits as scheduled under current law through 2098 if payroll tax rates were increased immediately and permanently by about 4.4 percentage points or benefits were reduced by an amount equivalent to that change. A combination of changes to taxes and benefits or a transfer from the Treasury's general fund could also be sufficient.
- Such long-term projections are uncertain. Demographic and economic factors are key sources of that uncertainty. For instance, if the economy grew more quickly than projected, the trust funds' annual revenues would be greater, and the changes to taxes or spending that would be necessary to pay benefits as scheduled under current law through 2098 would be smaller. If, instead, the economy grew more slowly than projected, revenues would be smaller, and the necessary changes would be larger.

CBO's long-term projections for Social Security, which provide estimates of the trust funds' balances and of other aspects of the program over the next 75 years, are based on a detailed microsimulation model that starts with data about individuals from a representative sample of the population and simulates demographic and economic outcomes for that sample over time.[1] CBO produces long-term projections of Social Security's finances under two scenarios that are based on different assumptions about the amounts of benefits that would be paid after the trust funds were exhausted:

- A **scheduled-benefits scenario**, in which people's benefits are paid as scheduled under current law, regardless of whether balances in the program's trust funds are sufficient to cover those payments; and
- A **payable-benefits scenario**, in which total benefit amounts are limited to annual revenues from payroll taxes and income taxes on benefits after the combined trust funds are exhausted.

In this testimony, I will discuss CBO's two sets of projections of Social Security's finances, differences in initial benefits received (by beneficiaries' birth cohort and lifetime earnings), and key sources of uncertainty in the agency's projections for the program.

Scheduled-Benefits Scenario

CBO's baseline budget projections for Social Security are required by statute to reflect scheduled benefits.[2] The agency projects that if Social Security benefits were paid as scheduled, the program's actuarial deficit over the next 75 years would equal 1.5 percent of gross domestic product (GDP), or 4.4 percent of taxable payroll.[3] In other words, CBO estimates that trust fund balances would be sufficient to pay scheduled benefits through 2098 if payroll tax rates were increased immediately and permanently by about 4.4 percentage points (before the effects of such changes on the economy are accounted for). Such an increase would boost payroll taxes paid by workers and employers from 12.4 percent to 16.8 percent—a 35 percent rise. Alternatively, if scheduled benefits were reduced by an amount equivalent to 4.4 percent of taxable payroll (a 24 percent reduction in benefits), those smaller benefits could be paid through 2098. A combination of changes to taxes and benefits or a transfer from

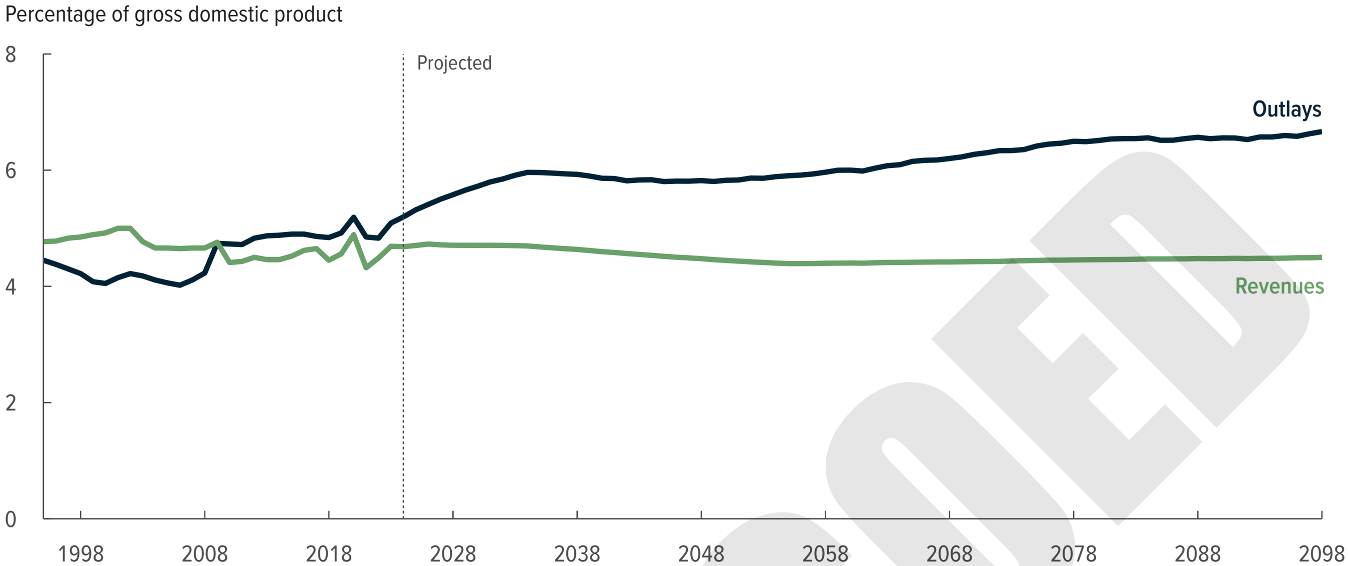
1. Congressional Budget Office, *An Overview of CBOLT: The Congressional Budget Office Long-Term Model* (April 2018), www.cbo.gov/publication/53667.

2. Congressional Budget Office, *CBO Explains the Statutory Foundations of Its Budget Baseline* (May 2023), www.cbo.gov/publication/58955.

3. An actuarial deficit is a negative actuarial balance. The actuarial balance is the sum of the present value of projected income and the current trust fund balance minus the sum of the present value of projected outlays and a year's worth of benefits at the end of the period. (A present value is a single number that expresses a flow of current and future income or payments in terms of an equivalent lump sum received or paid today. Such a value depends on the rate of interest, or discount rate, used to translate a cash flow in a future year into current dollars.)

Figure 1.

Social Security Outlays and Revenues Under the Scheduled-Benefits Scenario



Data source: Congressional Budget Office. See www.cbo.gov/publication/60281#data.

the Treasury's general fund to the Social Security trust funds could also suffice.[4]

Such policies would not, however, ensure Social Security's solvency after 2098. Policies that increased taxes or reduced benefits by a constant percentage equivalent to those specified here would create annual surpluses over the next three decades, but thereafter, annual deficits would still occur.

CBO projects that if Social Security paid benefits as scheduled, outlays for the program would equal 5.2 percent of GDP in 2024 and 6.7 percent in 2098. In the agency's projections, most of that increase occurs over the next decade as members of the large baby boom generation retire (see Figure 1).

From 2024 to 2034, the number of Social Security beneficiaries increases by about 12 million, from 68 million (or 20 percent of the population) to 80 million (or 22 percent of the population). Over the next 64 years, the number of beneficiaries continues to rise, though more slowly; it increases by 38 million over that period, reaching 118 million (or 29 percent of the population) in 2098. The rise in the number of beneficiaries slows after 2034, when the youngest members of the baby boom generation turn 70—the age by which nearly everyone claims Social Security benefits. The growth in Social Security outlays slows thereafter, though it continues to rise throughout the 75-year projection period as life expectancy increases.[5]

Unlike outlays, revenues for Social Security are projected to change little in relation to GDP over the 75-year period. They average 4.5 percent of GDP from 2024 to 2098 in CBO's projections. Measured as a percentage of GDP, payroll tax revenues decrease, and receipts from income taxes on Social Security benefits increase over that period.

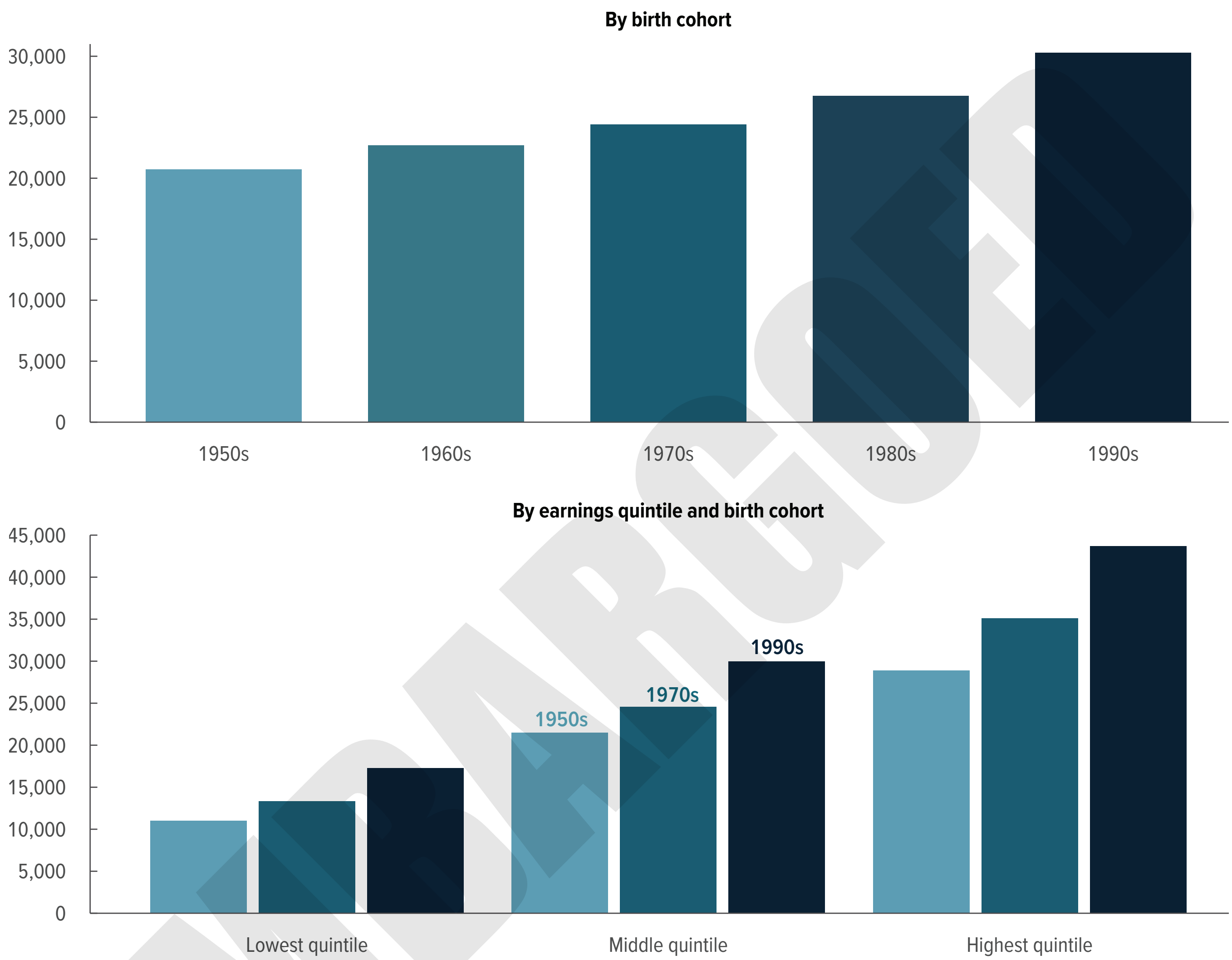
4. For a discussion of policy options that address the Social Security program's finances, see Congressional Budget Office, *Options for Reducing the Deficit, 2023 to 2032—Volume I: Larger Reductions* (December 2022), www.cbo.gov/publication/58164, *Options for Reducing the Deficit, 2023 to 2032—Volume II: Smaller Reductions* (December 2022), www.cbo.gov/publication/58163, "How Changing Social Security Could Affect Beneficiaries and the System's Finances" (interactive tool, April 2019), www.cbo.gov/publication/54868, and *Social Security Policy Options, 2015* (December 2015), www.cbo.gov/publication/51011.

5. The long-term projections in this testimony are consistent with the extended baseline projections that CBO published in March 2024. See Congressional Budget Office, *The Long-Term Budget Outlook: 2024 to 2054* (March 2024), www.cbo.gov/publication/59711.

Figure 2.

Average Initial Annual Social Security Benefits for Retired Workers Under the Scheduled-Benefits Scenario

2024 dollars



Data source: Congressional Budget Office. See www.cbo.gov/publication/60281#data.

A quintile is one-fifth of the distribution.

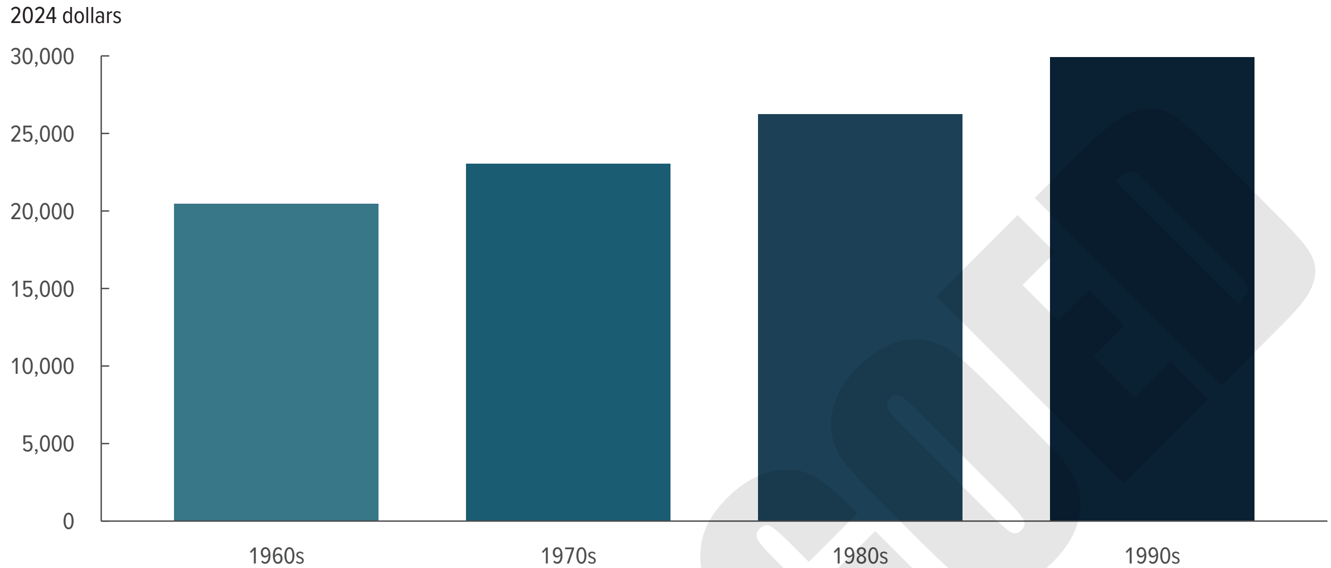
The Distribution of Scheduled Benefits

In CBO's projections, initial annual Social Security benefits—that is, the real (inflation-adjusted) benefits that people receive in the first full year that they claim them—grow over time in a scheduled-benefits scenario because real earnings are expected to continue to rise (see Figure 2). That growth in initial benefits for retired workers is partly offset for some birth cohorts because the increase in the full retirement age from 66 (for people born from 1943 to 1954) to 67 (for people born after 1959) reduces their initial benefits. (The analysis of initial benefits reflects the assumption that all eligible beneficiaries would claim benefits at age 65.) In addition, initial Social Security benefits are larger, on average, for retired workers with higher lifetime household earnings because people's Social Security benefits are based on their earnings history.

If paid as scheduled, initial benefits for disabled workers would also be larger in the future than they are today, CBO projects, because real earnings are expected to continue to rise (see Figure 3).

Figure 3.

Average Initial Annual Social Security Benefits for Disabled Workers Under the Scheduled-Benefits Scenario, by Birth Cohort



Data source: Congressional Budget Office. See www.cbo.gov/publication/60281#data.

Payable-Benefits Scenario

Under current law, after one of the program's trust funds is exhausted, Social Security outlays for that part of the program are limited to amounts payable from annual revenues. For this analysis, CBO considered the two separate trust funds combined as the Old-Age, Survivors, and Disability Insurance (OASDI) trust funds. The agency projects that the combined trust funds would be exhausted in fiscal year 2034; at that point the Social Security Administration would no longer be able to pay full benefits. It is unclear how payments to specific beneficiaries would be reduced if total benefits were limited to the amounts payable from dedicated funding.[6]

CBO estimated the amount of the annual reduction in total benefits that would be necessary for the program's outlays to match its revenues after the combined funds were exhausted. In 2035, Social Security revenues are projected to equal 79 percent of the program's scheduled outlays, resulting in a 21 percent shortfall. Thus, CBO estimates that Social Security benefits would be reduced by 21 percent in 2035 under the payable-benefits scenario.[7] For this analysis, CBO assumed that benefits paid to all existing and new beneficiaries would be reduced by the same percentage.[8] In CBO's projections, about 82 million people (roughly one-fifth of the population) receive OASDI benefits in 2035.

In CBO's assessment, the reductions in benefit amounts under the payable-benefits scenario would have four important effects on the nation's economic output—one that would decrease it in the short term and three that would increase it in the long term:

6. Barry F. Huston, *Social Security: What Would Happen If the Trust Funds Ran Out?* Report RL33514, version 34 (Congressional Research Service, September 28, 2022), https://tinyurl.com/3v5t6a28.

7. The annual shortfall—and thus the amount by which Social Security benefits would need to be reduced for the program's outlays to match its revenues—generally rises slightly over time. In 2054, for instance, a 25 percent reduction would be required under the payable-benefits scenario.

8. If a trust fund was depleted and its expenditures continued to exceed its receipts, two federal laws would come into conflict. Under the Social Security Act, beneficiaries would remain legally entitled to full benefits. However, under the terms of the Antideficiency Act (which prohibits agencies from spending more than the amounts available in an appropriation or fund), the Social Security Administration would not have legal authority to pay those benefits on time. It is unclear what specific actions the Social Security Administration would take if a trust fund was insolvent. See Barry F. Huston, *Social Security: What Would Happen If the Trust Funds Ran Out?* Report RL33514, version 34 (Congressional Research Service, September 28, 2022), https://tinyurl.com/3v5t6a28.

- Retirees would have less income and would be able to consume less, dampening the overall demand for goods and services and causing output in the years immediately after the trust funds' exhaustion to be lower than CBO currently projects.[9] If benefits were reduced equally for all Social Security beneficiaries after the trust funds were exhausted, the number of beneficiaries in poverty would increase.[10]
- Some people would find it necessary to work more or to remain in the labor force longer than they would have otherwise, which would expand the supply of labor and thus the economy's output in the long term.
- Some workers who have not yet retired would respond to the prospect of smaller benefit payments by boosting their saving and reducing their spending. Those changes would lessen the effect that smaller future benefit payments would have on households' future income and spending. The resulting increases in saving would boost the stock of private capital and output in the long term.
- Federal debt would be less than it is in CBO's extended baseline projections. That smaller debt would increase the amount of money available for private investment in capital goods and services, boost the stock of private capital, and increase output in the long term.

CBO estimates that lifetime spending would decrease by a larger percentage, and lifetime hours of work would increase more, on average, for households with less lifetime income than for those with more lifetime income.

Key Sources of Uncertainty

Long-term projections, including CBO's long-term projections of Social Security's finances, are inherently uncertain. If demographic trends or economic conditions differ from those in the agency's projections, then actual spending and revenues for Social Security will also differ from the projected amounts. Such discrepancies could be especially large in the later years of the projection period because differences in the underlying projections would compound over time.

Projections of demographic factors—including fertility, mortality, and net immigration—are highly uncertain.[11] If changes in fertility diverged from those in CBO's projections (which reflect an anticipated delay in childbearing), overall fertility rates would also differ from the projected rates. In addition, mortality rates in the long term are uncertain because factors such as environmental conditions and the evolution of medical technology may have different effects in the future than they have had in the past. How long the recent slowdown in the decline of the mortality rate will continue is also unknown.

In addition, CBO's projections of net immigration, particularly for people in the other-foreign-national category, are uncertain because information about that group is hard to obtain.[12] Moreover, changing conditions in other countries or changes in federal immigration policy, even without changes in law, could significantly alter the number of people who choose to immigrate to the United States.

If the number of working-age people was greater than CBO projects, the amount of revenues paid into the OASDI trust funds would exceed the agency's projections. And if demographic changes resulted in more Social Security beneficiaries than projected, Social Security outlays would be greater than projected.

CBO's projections of Social Security's finances are based in part on the agency's projections of economic factors, which are also uncertain, especially over a long projection period. For example, GDP growth, which is affected by changes in demographics and other factors, is one key driver of the Social Security system's finances. When economic growth is strong, earnings growth is also strong, resulting in more revenues paid into the trust funds and more outlays for Social Security benefits. Inflation, which affects annual increases in benefit amounts, is another source of uncertainty, as are interest rates.

9. Congressional Budget Office, *The Long-Term Budget Outlook Under Alternative Scenarios for the Economy and the Budget* (July 2023), www.cbo.gov/publication/59233.

10. Kathleen Romig, *Social Security Lifts More People Above the Poverty Line Than Any Other Program* (Center on Budget and Policy Priorities, January 2024), https://tinyurl.com/2rpvpfxd.

11. Congressional Budget Office, *The Demographic Outlook: 2024 to 2054* (January 2024), www.cbo.gov/publication/59697.

12. The other-foreign-national category includes people in the following groups who have not become U.S. citizens or received legal permanent resident, asylee, or nonimmigrant status: people who entered the United States illegally, people who entered legally in a temporary status and then remained after that legal status expired, and people who were permitted to enter (typically through the use of parole authority) despite not being admissible as a legal permanent resident, asylee, refugee, or nonimmigrant—including people who may be awaiting proceedings in immigration court. See Congressional Budget Office, *The Demographic Outlook: 2024 to 2054* (January 2024), www.cbo.gov/publication/59697.

Moreover, differences from the economic projections underlying CBO's long-term Social Security projections could have significant implications for other parts of the federal budget—because those economic projections are consistent with the ones that the agency uses to prepare its baseline budget projections and for other purposes. For example, the projections of interest rates that underlie the agency's Social Security projections are consistent with those used to project federal debt. Higher projected interest rates would result in a smaller actuarial deficit for the Social Security program.[13] But when the federal budget is considered in its entirety, those higher interest rates would result in larger net outlays for interest, larger budget deficits, and more debt.

13. Higher interest rates result in a smaller actuarial deficit for the Social Security program because the years with larger shortfalls—those relatively far into the future—have a smaller effect on the actuarial deficit than they would have if discount rates were lower.

Xinzhe Cheng, Noah Meyerson, and Delaney Smith conducted the analysis for this testimony with guidance from Molly Dahl, Elizabeth Cove Delisle, Sam Papenfuss, and Julie Topoleski. Alia Abdelkader, Daniel Crown, Madeleine Fischer, and Charles Pineles-Mark also contributed to the analysis. Madeleine Fischer fact-checked the testimony. In keeping with the Congressional Budget Office's mandate to provide objective, impartial analysis, the testimony makes no recommendations.

Mark Doms, Jeffrey Kling, and Robert Sunshine reviewed the testimony. Bo Peery edited it, and Jorge Salazar created the figures and prepared the text for publication. The testimony is available at www.cbo.gov/publication/60281.

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