THIRD WAY

REPORT *Published May 31, 2013 • 13 minute read*

It's Time for a National Commission on Social Security

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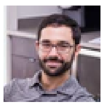

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With the near-term deficit in decline and talk of a major deficit package effectively over, the time is ripe for fixing Social Security. Why now? With short-term deficits under control, policymakers can focus on fixing Social Security for the right reason—ensuring solvency for future generations—and not the wrong reason of hitting a deficit target. Fixing it now would require modest adjustments, whereas delaying until even mid-way through the next presidency could require far more disruptive steps. Moreover, the fixes would not kick-in for years, thus doing no harm to our still-fragile economic recovery. And finally, today's divided government provides optimal political cover for both parties.

In this memo, we argue that a national commission to fix Social Security is not only the best way, but the only way to achieve long-term solvency. Though Washington may feel "commissioned out," history shows that this is how Social Security gets fixed. And a Social Security commission won't have the structural flaws of Bowles-Simpson which, though admirable, was far too big in scope and designed in such a way to have little realistic chance of enactment.

The Problem

When it comes to Social Security, Republicans and Democrats have done little right in recent years. Republicans made privatization of Social Security the cornerstone of their economic agenda in 2005. Even before the financial crisis, that was a risky idea for a program that absolutely has to be there rain or shine. Post-financial crisis, the idea is now, thankfully, a non-starter.

Democrats responded by sticking their heads in the sand. They argued that Social Security's approaching insolvency wasn't critical and that it could be solved, eventually, by expanding the FICA tax to cover all wages of high-income workers. But the Social Security Trust Fund is a mere two decades from expiration—a blink of an eye in the world of green eye-shaded actuaries. At that point, all Social Security recipients would see one-fourth of their benefits simply vanish. [1] And the tax-only approach to curing Social Security is (as we discuss later) a pipe-dream.

Meanwhile, voters have rejected both parties on Social Security. Although Democrats have spent billions of dollars over the past decade to bludgeon Republicans for seeking to privatize Social Security and voucherize Medicare, the only age group that Democrats cannot seem to win is senior citizens. In 2012, President Obama lost them by 12 points and congressional Democrats lost them by 11.

As for Republicans, seniors may be voting for them but not for their policy ideas for Social Security and Medicare. Polls show that senior voters do not want to privatize Social Security, they do not want to replace Medicare with a voucher, and they don't like premium support.

So what's to be done?

We argue that Congress should charge a national commission with crafting a Social Security solvency plan, which would be guaranteed an up-or-down vote in 2015. To facilitate that goal, this brief has three parts: (1) the policy case for a commission, (2) the political case for a commission, and (3) how a commission will succeed.

Why Now? The Policy Case

Insolvency is 20 years away. Some progressive leaders say it's better to wait, and even the House Republican Budget proposes making no changes to Social Security in the next ten years. So why Social Security, and why address it now?

1. Insolvency is certain without action.

In 2010, Social Security spent more than it received in payroll taxes. Once that threshold is crossed, it's only a matter of time until the Trust Fund runs dry. The expected insolvency date for Social Security is currently 2033. [2] Over the course of several decades, the expected insolvency date has only moved forward—from 2042 five years ago to 2033 today. [3] These projections are grounded in unavoidable demographics. Over the next two decades, the number of people over 65 will increase by 77%, while those of working age—25 to 64—will increase just 7%. Simply put, Social Security stands to be grossly underfunded for future generations.

2. Postponing a fix is costly and risky.

The problems facing Social Security are not so large as to require an overhaul involving privatization or draconian benefit cuts. Instead, modest course corrections taken now can preserve these programs for future generations—but only if they are done with enough lead time. For example, if part of the commission's package includes Chained CPI and a FICA cap increase, the resulting savings would have 20 years to accrue in the Trust Fund—but only if done today. While in the Trust Fund, those proceeds would earn interest and could mitigate the need to raise taxes further or trim benefits deeper down the road.

We also know from history that safety net fixes are most feasible under divided government, because no one party wants to carry the load alone. So today's closely divided government presents as conducive an environment for reform as any future balance of power. Waiting for the next election and some perceived optimal political environment could mean waiting until it's too late.

3. Public investments are starving.

In the mid-1960's, federal investment spending was three times that of entitlement spending. But today, spending on Social Security, Medicare, and Medicaid is three times that of federal investment spending. By 2022, that ratio will be five to one. [4] And this trend will only accelerate as the Boomers grow old, forcing us to spend less and less to educate kids, build roads, and cure diseases. This fiscal path translates to a less skilled workforce, lower rates of job creation, and an infrastructure unfit for the 21st Century.

Progressives like to argue that the real entitlement problem is not Social Security but, rather, the rising cost of health care faced by Medicare and Medicaid. It's true that health care programs are growing even faster than Social Security. But Social Security spending as a share of the economy will increase by 22% over the coming decades. [5] That is not insignificant. There is a limit to what taxpayers will allow the government to spend. If the major entitlements grow unabated, something else will certainly get cut. It is hard to envision a scenario in which the victims won't be investments in kids, roads, research, and science.

4. A FICA-Only Solution is a Fantasy.

New revenue would likely be part of a commission-led solution. But a FICA-only solution that eliminates the earnings cap—as some progressives cling to—will never happen and should never happen for several reasons:

- *This would be a $1.6 trillion tax increase over ten years.* [6] This solution would be a large tax increase on all individuals making over $113,700 and the businesses that employ them. This is far more revenue than is being seriously considered in the current budget debate. Even if this were feasible, raising taxes of this magnitude would make it impossible to raise any more revenue in the future for critical public investments—in roads, education, and research.

- *The federal top marginal tax rate would near 50%.* Without the Social Security tax cap, the top marginal federal tax rate for an individual with taxable income of $400,000 or more would be 48.2%, well above the Clinton-era rate of 41.1%. This higher marginal rate would consist of: income taxes (39.6%), Social Security taxes (6.2%), Medicare taxes (1.45%), and the Additional Medicare Tax under the Affordable Care Act (0.9%). When state income taxes are included, the top marginal rate would be 53.2% in Illinois, 53.4% in Massachusetts, 57.0% in New York, 57.1% in New Jersey, and 60.5% in California.

- *It doesn't achieve solvency.* The latest analysis by Social Security Actuary Stephen Goss states that eliminating the cap would close only 79% of Social Security's long-run deficit. [7] Even if this proposal were enacted, Social Security would not be able to pay all of its promised benefits over the next 75 years.

- *It breaks the Social Security contract.* An important part of the Social Security contract is this: every dollar of income subject to the payroll tax boosts a worker's benefit level by some meaningful amount. And even though upper middle class workers get only fifteen cents on the dollar for the last half of their covered wages ($57,216-$113,700), they get a reasonable deal overall. In stark contrast, a recent progressive proposal by Senator Tom Harkin (D-IA) to remove the cap and tax all salary and wages would give these higher income workers an undeniably raw deal: only 5% of earnings above $113,700.

Social Security Bend Points (2013)

Portion of average annual earnings	Rate of earnings replacement
$0 — $9,492	90%
$9,492 — $57,216	32%
$57,216 — $113,700	15%

5. A fix would narrow the gap between spending and revenue.

Democrats and Republicans like to say that Social Security's finances do not contribute to the deficit. But the reality is that, in the unified budget that everyone uses, Social Security counts. Therefore, a Social Security fix would have the ancillary benefit of diminishing the gap between spending and revenue by roughly $800 billion over the first decade and significantly more over the next. [8] That improvement would help to eliminate the deficit as the central policy debate in Washington.

Why Now? The Political Case

In 1981, Social Security was near broke. Congress and President Reagan appointed a commission, chaired by Alan Greenspan, to restore Social Security solvency. In 1983, negotiations by key commission members prompted Congress to increase the payroll tax, raise the retirement age, and make several other changes. Social Security was made solvent well into the next century.

What is the political case today for such a commission?

1. It's the only way to fix Social Security.

The Greenspan Commission set a precedent that will now be the way Social Security is fixed in perpetuity. The commission model worked because it created a balanced solution that no party would have created on its own.

2. Social Security can only be fixed under divided government.

There is a reason that Social Security was never fixed during periods of one-party rule in Washington. Neither party wants to bear the burden of raising taxes or trimming benefits on its own. Neither party can afford the political blowback of a Social Security plan that gets zero votes from the other party.

3. Voters want Congress to do something.

Voters are certain that if it's not fixed, Social Security will be in deep trouble. When asked what concerned them more—Congress doing something on Social Security and Medicare or Congress doing nothing—by 78-17% they were more concerned that Congress would do nothing. [9] Only 6% of our respondents said that Social Security was on sound financial footing, and 89% said the programs had either major (53%) or minor (36%) fiscal problems. [10] In our focus groups, participants agreed unanimously that any fix would involve getting both new revenue and some benefit reductions. Voters may not be picketing for a Social Security fix plan, but they believe that having no plan means the end of the program. The lack of confidence that voters have in the solvency of Social Security (as well as Medicare) is likely the reason that billions of dollars in advertisements castigating Republicans on their privatization plans have failed to deliver senior voters for Democrats.

4. Democrats and Republicans each get wins.

- For Democrats, a Social Security fix is the surest path to more revenue, which would come almost entirely from high-income workers, likely through a partial lifting of the payroll tax.

- For Republicans, a Social Security fix would narrow the gap between spending and revenue by more than one trillion dollars.

- For Democrats, a commission-led fix would likely provide additional protections for low-income beneficiaries.

- For Republicans, a fix would end the Democratic drumbeat that Republicans are out to end Social Security as we know it.

- For both parties, it would lead to a shared solution that would keep Social Security solvent for 75 years.

Why This commission will Succeed where Bowles-Simpson did not

We supported the creation of Bowles-Simpson and endorsed its findings. But Bowles-Simpson had three fundamental flaws that a national commission on Social Security can—and must—avoid.

First, its scope was far too broad, encompassing taxes, defense, entitlements, and most other categories of federal spending. If enacted, the proposal would have remade the federal government. Second, it was stacked with too many elected officials. Unelected panelists voted 5-to-1 in favor of the plan, but elected panelists were split 6-to-6. And third, the vote threshold was too high. Eleven of the panel's 18 members voted for the proposal (surpassing the 60% threshold to defeat a Senate filibuster), but 14 votes were required to qualify for a vote in Congress.

Yet, while Simpson-Bowles failed, other commissions have succeeded. The Defense Base Closure and Realignment Commission (BRAC) effectively overcame tough politics five times over the last 25 years. The Greenspan Commission negotiated terms leading to the Social Security Reform Act of 1983, which extended the program's solvency for an estimated 50 years. The panel included five appointments each by President Reagan, Speaker Tip O'Neill, and Senate Majority Leader Howard Baker.

A new commission on Social Security should adopt the best practices of the BRAC and Greenspan commissions. In particular, we recommend several components:

- *Singular Mission*: The commission should present fixes that would achieve 75-year solvency, ensuring that Social Security remains strong for future generations.

- *Non-elected Panel*: The panel should minimize the seats allotted to current members of Congress. One way to structure the panel would be to require that at least 2/3 of the panelists consist of unelected experts. Fewer than half of the Greenspan appointments were sitting members of Congress, and the BRAC had *none* (two were retired members of Congress).

- *Post-midterm Vote*: Congress should establish the commission in 2013 and select panelists by the end of the year. The commission should present recommendations after the 2014 midterm election, with an up-or-down vote to occur in 2015.

- *Simple Majority*: A simple majority among panelists should be sufficient to send the proposal to Congress for a vote.

- *Expedited Congressional Procedure*: The commission's proposal should be expedited through the House and Senate, requiring a simple majority vote to pass in each chamber. Members should be able to offer amendments as long as they maintain 75-year solvency, as suggested by Senator Dick Durbin (D-IL) in public remarks. [11]

Conclusion

There is no better time to fix Social Security. Insolvency is near enough to focus the mind and far enough away to require only modest fixes. And with talk of more near-term deficit reduction effectively over, we have a perfect—yet narrow—window to fix the program before 2014 and 2016 election politics obstruct the potential for pragmatic policy.

Neither party wants to own a Social Security fix for justifiable political reasons. A commission would solve that problem. And learning from the structural flaws of Bowles-Simpson, a commission would give both parties the political cover to set in motion a process to strengthen retirement security. It's time for Congress to act.

END NOTES

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