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Current Social Security Issues

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Abstract

Social Security is the focus of intense public interest. Projected long-range funding problems, public skepticism about its future, and a growing perception that Social Security will not be as good a value for future retirees as it is today are fueling calls for reform. This report, updated regularly, discusses a number of the major Social Security issues currently drawing congressional attention.

Current Social Security Issues

Summary

Social Security is the focus of intense public interest. The system is projected to have long-range funding problems, and public skepticism about its future persists. Although the system's income currently exceeds its outgo, its board of trustees projects that on average over the next 75 years its expenditures will exceed its income by 16% and by 2032 its trust funds will be depleted. This adverse outlook is mirrored by public opinion polls where fewer than 50% of respondents express confidence that Social Security can meet its long-range commitments. Accompanying this skepticism is a growing awareness that Social Security will not be as good a value in the future as it is for today's retirees. Until recent years, a typical retiree could expect to receive far more in benefits than he or she paid in Social Security taxes. However, because Social Security tax rates have increased and the age for receipt of "full" benefits is scheduled to rise from 65 to 67, it has become increasingly apparent that the system will be less of a good deal for future recipients.

These concerns and a belief that economic growth could be bolstered by changes to the system have led to a number of proposals for varying degrees of reform. They range from restoring long-range solvency with as few changes as possible to totally revamping the system toward private-sector models. Such a range of ideas was presented in the January 1997 report of a legislatively mandated Social Security Advisory Council. Bills designed to reform Social Security, in whole or part by using private accounts, also have been introduced in the 105th Congress.

The potential economic toll of federal entitlements overall also has raised the specter of change. The concern is that if left unchecked, entitlement spending will place a large strain on federal budgets far into the future, limiting fiscal policy options and forcing future generations to bear an enormous tax burden, especially when post-World War II baby boomers retire and draw on these programs. One approach frequently discussed is means testing. Means testing is shorthand for targeting entitlement benefits on those most in need. Such proposals often include Social Security because it accounts for 40% of all entitlement spending. A related concern arises from the provision of automatic inflation adjustments to Social Security and other entitlement benefits, as well as to various aspects of the income tax system. These adjustments are based upon the U.S. Department of Labor's Consumer Price Index, which has been criticized for possibly overstating inflation. Overstatement of inflation translates into higher benefit outlays and lower tax revenues.

In his State of the Union address on January 27, 1998, the President pledged action on the issues early in 1999. He stated that he wanted to conduct bipartisan forums around the country this year to draw out the public's views (one of which has already occurred), hold a White House Conference on Social Security in December, and convene congressional leaders next year to craft bipartisan legislation. Speaker of the House, Newt Gingrich, has suggested forming an intergenerational panel to conduct a *national dialogue* on the issues and a high-level commission to forge a bipartisan plan. This approach is reflected in H.R. 3546, introduced by Representative Archer et. al. and passed by the House in April 1998. No Senate action has yet been taken on the bill. The Administration has argued that the panels are unnecessary.

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Introduction

Social Security is the focus of intense public interest. The system is projected to have long-range funding problems, and public skepticism about its future persists. Although currently the system's income exceeds its outgo, its board of trustees projects that on average over the next 75 years its expenditures will exceed its income by 16% and that by 2032 its trust funds will be depleted. This adverse outlook is mirrored by public opinion polls in which fewer than 50% of the respondents express confidence that the system will be able to meet its long-range commitments. Accompanying this skepticism is a growing awareness that Social Security will not be as good a value in the future as it is for today's retirees. Until recent years, a typical retiree could expect to receive far more in benefits than he or she paid in Social Security taxes. However, because Social Security tax rates have increased and the age for receipt of "full" benefits is scheduled to rise from 65 to 67, it has become increasingly apparent that the system will be less of a good deal for future recipients.

Although Social Security was not a central issue in the 1996 elections, a number of proposals to make far-reaching changes have been suggested, and the debate seems certain to grow in the coming months. Concerns about the financing problems, skepticism about the system's survival, and a belief that economic growth could be bolstered by certain changes to the system have led to a number of proposals for reform. They range from restoring long-range solvency with as few changes as possible to totally revamping the system toward private-sector approaches for providing retirement income. The specter of change also has been heightened in part by apprehension about the potential economic toll of federal entitlements generally. The concern is that entitlement spending, if left unchecked, will place a large strain on federal budgets far into the future, limiting fiscal policy options and forcing future generations to bear an enormous tax burden, especially when the post-World War II baby boomers retire and draw on these programs. Social Security accounts for 40% of all entitlement spending. A related concern arises from the automatic annual inflation adjustments made to Social Security and other entitlement benefits, as well as to various aspects of the income tax system. These adjustments, based upon the U.S. Department of Labor's Consumer Price Index (CPI), have come under criticism for possibly overcompensating recipients and taxpayers for inflation. Overstatement of inflation translates into higher benefit outlays and lower tax revenues.

In his State of the Union address on January 27, 1998, the President pledged action on the issues early in 1999. He stated that he wanted to conduct bipartisan forums around the country this year to draw out the public's views (one of which has already occurred), hold a White House Conference on Social Security in December, and convene congressional leaders next year to craft bipartisan legislation. He also urged the Congress to "reserve" use of any federal budget surpluses until action is taken to strengthen the Social Security system. Speaker of the House, Newt Gingrich, has suggested forming an intergenerational panel to conduct a *national dialogue* on the issues and a high-level commission to forge a bipartisan plan. This approach is reflected in H.R. 3546, introduced by Representative Archer et. al. and passed by the House on April 29, 1998. No Senate action has yet been taken on the bill. The Administration has argued that the panels are unnecessary.

A Troubling Long-Range Financial Outlook

Currently Social Security's income exceeds its outgo. However, its board of trustees projects that over the next 75 years its expenditures will exceed its income on average by 16%. The primary reasons are demographic: an aging post-World War II "baby boom" generation and increasing life expectancy are creating an older society. The number of people 65 and older is predicted to rise by 75% by 2025, whereas the number of workers whose taxes will finance future Social Security benefits is projected to grow by only 12%. As a result, the ratio of workers to Social Security recipients is projected to fall from 3.4 to 1 today to 2.0 to 1 in 2030.[1]

The Projected Slide Towards Insolvency

— *Spending exceeds tax revenues in 2013*
— *Combined OASDI trust funds peak in 2020*
— *Disability Insurance (DI) fund becomes insolvent in 2019*
— *OASI fund becomes insolvent in 2034*
— *Combined OASDI funds become exhausted (have a zero balance) in 2032*

Excess Social Security revenues are invested in U.S. government securities recorded to the Old Age, Survivors and Disability Insurance (OASDI) "trust funds" maintained by the Treasury Department (OASDI being the formal title for Social Security). In April 1998, the trustees projected that the balance of these trust funds would peak at $3.8 trillion in 2020. However, OASDI spending would begin to exceed tax receipts in 2013. At that point general revenues would be needed, first to pay interest on the securities held by the trust funds, and then beginning in 2020 to draw them down. By 2032, the trust funds would be fully depleted and the system would be technically insolvent.

The problem is not unprecedented. In 1977 and 1983, Congress enacted a variety of measures to address financial problems similar to those currently being forecast. Among them were increases in payroll taxes, partial taxation of the Social Security benefits received by higher-income recipients, and a gradual increase from 65 to 67 in Social Security's "normal retirement age," which is the age required to

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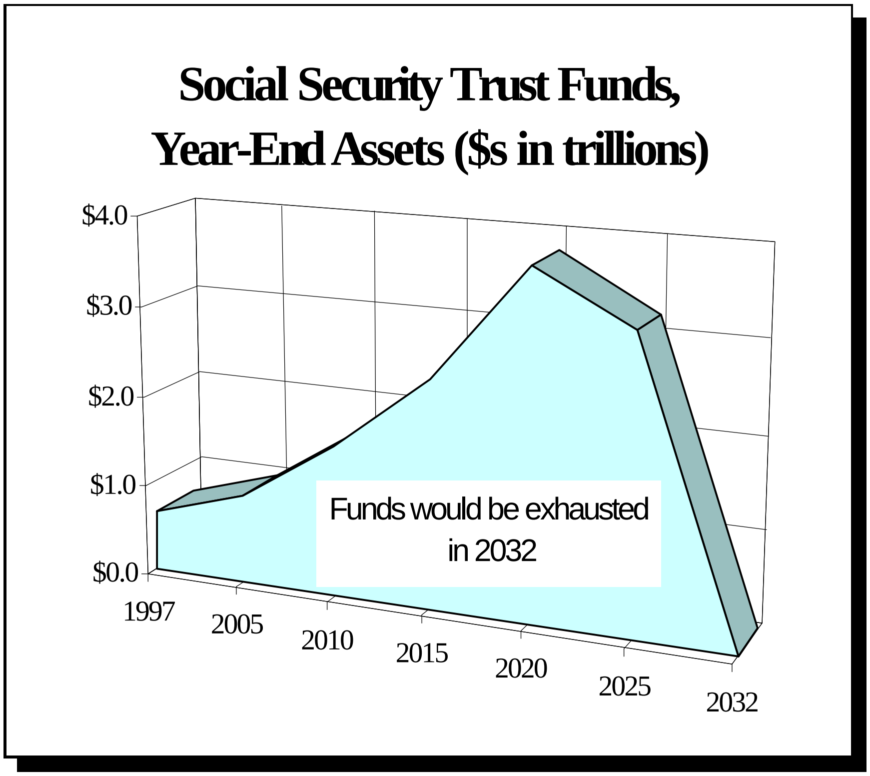
[1] See the 1998 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, Intermediate projections.



receive full benefits. Since that time birth and economic growth rates have not kept up with projections made then, and new long-term deficits are forecast.

There is no agreement about what should be done, but a consensus appears to be forming that action should be taken soon. The view is that the longer corrective action is delayed, the more drastic it will need to be. Although a legislative-mandated Social Security Advisory Council, which issued a report on ways to deal with the problem in January 1997, was unable to agree on a specific plan, one of the issues its members did agree about was that the sooner action was taken the better.[2] This perspective echoed that of the earlier 1994/1995 Bipartisan Commission on Entitlement and Tax Reform (better know as the Kerrey-Danforth Commission).

Legislative proposals: Over the past several years a variety of proposals have been advanced to fix the system. During the 103rd Congress, bills to raise the system's "full benefit" age to 70, modify cost-of-living adjustments (COLAs), and make other benefit reductions were introduced by Representatives Pickle (H.R. 4275), Penny (H.R. 4372 and H.R. 4373), and Nick Smith (H.R. 5308), while Representative Rostenkowski (H.R. 4245) sought a mix of benefit reductions and tax increases. In the 104th Congress, more far-reaching proposals encompassing not only some of these changes, but also seeking to privatize a portion of the program, were introduced by Senators Kerrey and Simpson (S. 825) and Representative Nick Smith (H.R. 3758). Senator Kerrey also introduced a bill (S. 818) that separately called for retirement age increases.

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[2] Report on the 1994-1996 Advisory Council on Social Security. U.S. GPO, Washington, 1997.

In the 105th Congress, Senator Gregg introduced a bill (S. 321) that would raise the full and early retirement ages gradually to 70 and 67, respectively, becoming fully effective for those born in 1967 (after which they would rise another month every 2 years), and, beginning in 1998, reduce COLAs by 0.5 percentage point annually. In addition, the bill would mandate that, beginning in 1998, for workers under age 55, 1 percentage point of their OASDI tax rate be diverted to a personal investment fund maintained either in the U.S. Treasury in the same manner as the Thrift Savings Fund for federal workers or by banking institutions. Future Social Security benefits would be scaled down to take account of the personal accounts (the House companion bill to S. 321 is H.R. 2782 by Representative Sanford).

Later in the 105th Congress, additional bills designed to reform Social Security, including the use of private accounts, were introduced by Representatives Sanford (H.R. 2768), Porter (H.R. 2929), Nick Smith (H.R. 3082), Pete Sessions (H.R. 3683) and Senator Moynihan (S. 1792).

H.R. 2768 and H.R. 2929 would allow workers to divert 8 and 10 percentage points, respectively, of the OASI tax rate into individual accounts, while H. R. 3082 would limit the amounts to be placed in such accounts to $2,000 and deposit in them a proportional amount of the yearly excess of Social Security revenue over expenditures and one-third of any federal budget surplus. To bolster Social Security's financing, H.R. 2768 would gradually raise the full retirement age to 70 for those born after 1966; alter the basic benefit formula to produce lower benefits; reduce annual COLAs and spousal benefits; and extend Social Security coverage to all newly hired state and local government workers. H.R. 2929 would gradually raise the full retirement age to 70 for those born after 1966 and alter the basic benefit formula to produce lower benefits. H.R. 3082 would raise the full and early retirement ages gradually to 69 and 66, respectively, for persons born in 1953, and thereafter index them to longevity; alter the basic benefit formula to produce lower benefits; reduce spousal benefits; withhold benefits for persons who are projected to receive more from Social Security than they and their employers paid in Social Security taxes and whose annual income exceeds $50,000 (single) or $100,000 (couple); and extend Social Security coverage to all newly hired state and local government workers. H.R. 3683 would allow workers to opt out of the system entirely if they elect to set up a new personal accounts (after 5 years they would forfeit all Social Security benefits).

S. 1792 would allow workers and employers to each have a 1 percentage point Social Security tax cut. If the worker used it to create an individual savings account, his or her employer would have to match it. It also would raise the tax rate in future decades to match the cost of the program; reduce COLAs by 1 percentage point annually; increase and extend the taxation of benefits to all recipients (i.e., to those now exempt because their incomes are under the thresholds of $25,000 for single persons and $32,000 for couples); raise the full retirement age gradually to 68 for persons born in 1955, and thereafter index it to longevity; lengthen the earnings "averaging period" for computing benefits; eliminate the earnings test; raise the maximum amount of earnings subject to taxation to $97,500 in 2003 ($14,700 higher than current law); and extend Social Security coverage to all newly hired state and local government workers.

The retirement age issue: Interest in raising the ages at which full and reduced Social Security retirement benefits are payable, as a way to deal with the long-range financing shortfall, stems from improvements in life expectancy since Social Security benefits were first paid in 1940. Back then an average 65 year old was expected to live another 13 years. Today, life expectancy at 65 is 17 years, and by 2030 it is projected to be 19 years. This trend made increasing Social Security's "full benefit" age an attractive means of achieving savings when the system was facing major financial difficulties in the early 1980s. Congress boosted the "full benefit" age from 65 to 67 as part of the Social Security Amendments of 1983 (P.L. 98-21). This change will be phased in by 2-month increments starting with those born in 1938, with the full 2-year hike affecting those born after 1959. It will not raise the first age of eligibility — which is age 62 — but the benefit reduction for retiring at 62 will rise from 20% to 30%. Proponents of raising one or both of these ages further see it as reasonable in light of projected longevity and health improvements of the elderly. Opponents say it will penalize today's workers who already get a worse deal from Social Security than do current retirees, those who work in arduous occupations, and those who are members of racial minorities that have relatively shorter life expectancies.

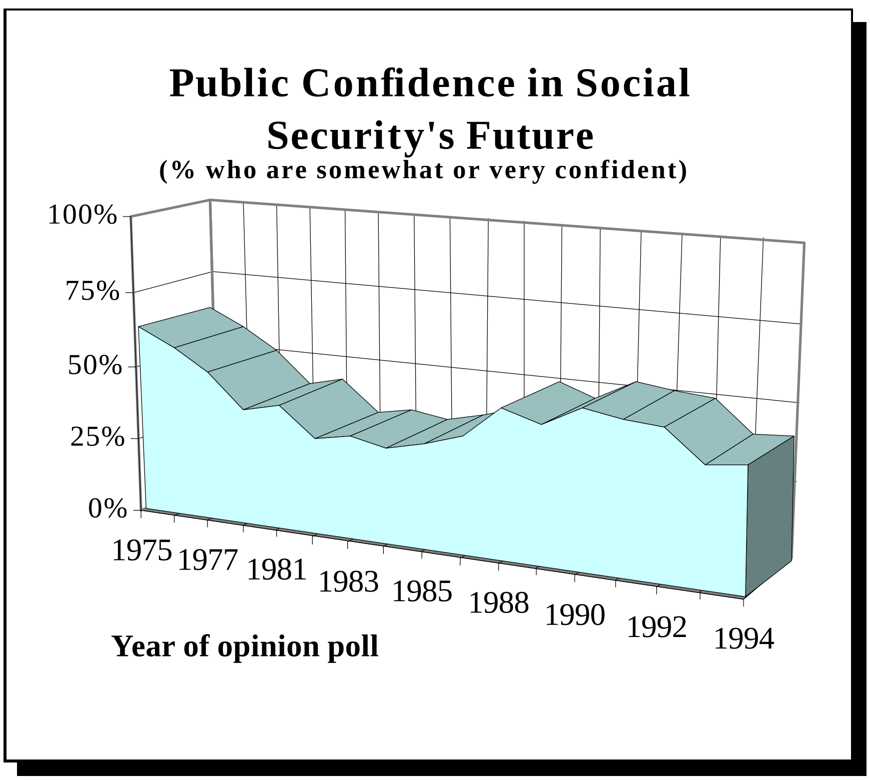
The Recommendations of the 1994-96 Advisory Council on Social Security: Although the recent Advisory Council on Social Security could not reach a consensus on a single approach, its report contains three different proposals to restore the system to long-range solvency. The first, labeled the "maintain benefits" plan, keeps the program's benefit structure essentially the same by addressing most of the long-range deficit through revenue increases, including an eventual rise in the payroll tax, and minor benefit cuts. To close the remaining gap, it recommends that investing part of the Social Security trust funds in the stock market be considered. The second, labeled the "individual account" plan, restores solvency mostly with reductions in benefits, and in addition requires workers to make a 1.6% of pay contribution to new individual savings accounts. The third, labeled the "personal security account" plan, achieves long-range solvency through a major redesign of the system that gradually replaces the current earnings-related retirement benefit with a flat-rate benefit and individual savings accounts funded with a 5% of pay contribution.

Social Security and the Balanced Budget Amendment: Social Security's financial situation also became embroiled in the recent debate about its treatment under a possible constitutional amendment to require a balanced federal budget. Early in the 105th Congress, unsuccessful attempts were made (H.J. Res. 1 and S.J. Res. 1) to pass the amendment, which would have included Social Security in the budget calculations, as did similar constitutional amendments proposed in 1995 and 1996. On each occasion, critics of the amendment attempted to remove Social Security from calculations of the budget. While these attempts did not succeed, the balanced budget amendment itself failed each time in the Senate to get the requisite votes for passage. Opponents of including Social Security argued that it would cause the program's surpluses to be used to cover deficits in the rest of the budget and could lead to future cuts in Social Security benefits. Those who wanted to keep it in the calculations argued that it wasn't their purpose to cut Social Security, but that the program represents too large a share of federal revenues and expenditures to be ignored and that removing it from the calculations would make the goal of achieving a balanced budget much more difficult.

Persistent Public Skepticism

Social Security's financial problems are mirrored in general skepticism about the system's future. Public confidence in the system's ability to meet its long-run commitments dropped after funding problems emerged in the 1970s and early 1980s. Repeated polling done over the past 20 years, under the sponsorship of the American Council of Life Insurance, shows a majority of Americans expressing a lack of confidence in the system. Although skepticism abated for a few years following the enactment of legislation in 1983 shoring up the system, it appears to be rising again with 55% voicing a lack of confidence in 1994. Younger workers were particularly skeptical; nearly two-thirds of those below age 55 expressed a lack of confidence in the system, compared to fewer than one-third of those 55 and older.[3]

Some observers caution that too much should not be inferred from polling data, noting that public understanding of Social Security is limited and often inaccurate. They argue that a major reason confidence is highest among the retired and those nearing retirement is that, being more immediately affected, they have learned more



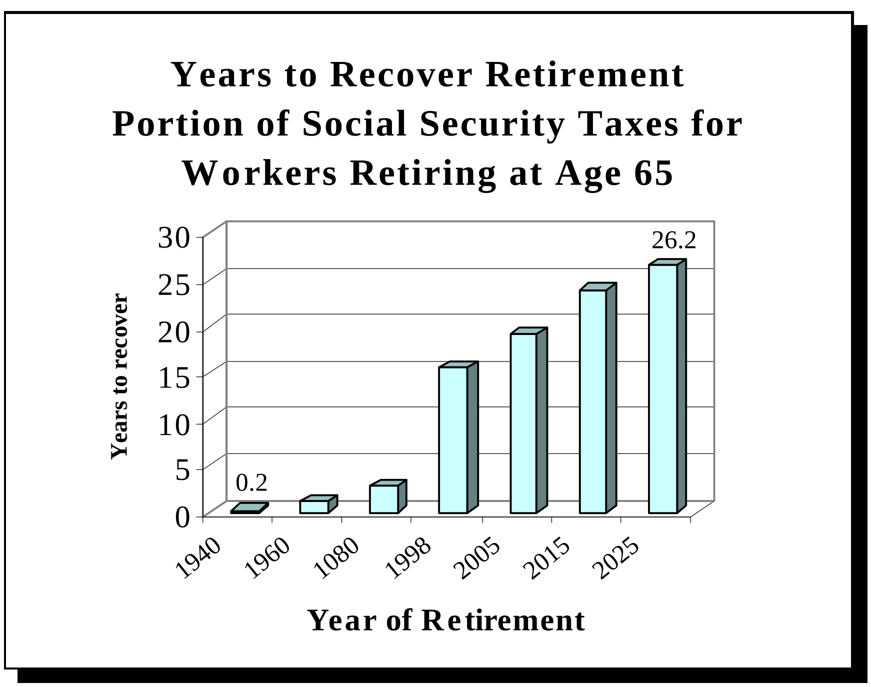
[3] American Council of Life Insurance. Monitoring Attitudes of the Public. In Baggette, Shapiro and Jacobs. The Polls-Poll Trends: Social Security, An Update. *Public Opinion Quarterly*, fall 1995. p. 424-425.

about the program. Younger workers receive little information about Social Security unless they request it, which very few do. In 1995, the Social Security Administration (SSA) began phasing in a system to provide annual statements to workers, which some argue will make workers more aware of their promised benefits and thus more trusting of the system.

Others, however, suggest the skepticism is justified by the system's repeated financial difficulties and its diminished "money's worth" to younger workers. Moreover, in recent polls reform of Social Security ranked high as a legislative priority. A survey conducted in October 1997 for NBC News and the Wall Street Journal showed that 66% of the respondents ranked reform of Social Security as a "top priority" for the Congress.[4]

Increasing Doubts About Money's Worth

Until recent years, it was clear that Social Security recipients received a very good deal for the taxes they paid to support the system. Most current recipients receive more, often far more, than the value of the taxes they paid. However, because Social Security tax rates have increased over the years and the age for full benefits is scheduled to rise, it is becoming increasingly apparent that Social Security will be less of a good deal for many future recipients. For example, workers who earned average wages and retired in 1980 at age 65 took 2.8 years to recover the value of the retirement portion of the combined employee and employer shares of their Social Security payroll taxes plus interest. For their counterparts who retired at age 65 in 1998, it will take 15.5 years. For those retiring in 2025, it will take 26.2 years (base



[4] The survey was conducted over the period October 25-27, 1997 by Hart and Teeters research Companies.

on the assumptions used by the Social Security trustees in their intermediate forecast).[5]

Some observers feel these discrepancies are inequitable and endanger public support for the system. Others, however, discount their importance, arguing that Social Security is a social insurance program serving social ends that transcend questions of whether some individuals do better than others. For example, the program's anti-poverty features by design replace a higher proportion of earnings for low-paid workers and provide additional benefits for workers with families. Also, today's workers, who will receive less direct value from their contributions than today's retirees, are in large part relieved from the burden of supporting their parents, and the elderly are able to live independently and with dignity. These observers contend that the societal worth of these aspects of the system is not valued in individual calculations of taxes paid and benefits received.

Emerging Interest in "Privatization"

Concerns about Social Security's financing problems, growing skepticism about its survival, and a belief that economic growth could be bolstered have led to a number of proposals to "privatize" part or all of the system, reviving a philosophical debate that dates back to its creation in 1935.

The three alternative proposals by the 1994-1996 Advisory Council previously mentioned all feature some form of privatization. The first, the "maintain benefits" plan, recommends that investing part of the Social Security trust funds in the stock market be considered in order to bolster the program's finances (stocks would be presumed to produce a higher return than the Treasury bonds the system now invests in). The second, the "individual account" plan, would require workers to make a 1.6% of pay contribution to new individual savings accounts to make up for Social Security benefit cuts it calls for to restore long-range solvency. The third, the "personal security account" plan, would redesign the system by gradually replacing Social Security retirement benefits with a "flat-rate" government benefit for each worker and individual private savings accounts funded with 5% of pay (part of which would take the place of Social Security taxes).

One approach garnering a great deal of attention is the reform that Chile enacted in 1981. It replaced a troubled state-run, pay-as-you-go system with one requiring most workers to invest a portion of their earnings in individual savings accounts through government-approved private pension funds. Similar approaches for reforming the U.S. system, and scaled-down versions that would run in conjunction with the existing system, have been introduced in the 104th and 105th Congresses. They would permit or, alternatively, require that workers invest some or all of their Social Security taxes into a personal account similar to an IRA. These include bills

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[5] The payback time is somewhat faster for low-income workers and somewhat slower for high-income workers. For more information, see *Social Security: The Relationship of Taxes and Benefits for Past, Present, and Future Retirees*, CRS Report 95-149, by Geoffrey Kollmann, Table 1.

by Senators Kerrey and Simpson (S. 824 and S. 825), and Representatives Porter (H.R. 2953), Thomas (H.R. 2971) and Nick Smith (H.R. 3758) in the 104th Congress, and by Senators Gregg (S.321) and Moynihan (S. 1792), and Representatives Sanford (H.R. 2768 and 2782), Porter (H.R. 2929), Nick Smith (H.R. 3082) and Pete Sessions (H.R. 3683) in the 105th. S. 824, S. 1792, H.R. 2768, H.R. 2929, H.R. 2953, H.R. 3082, H.R. 3758, and H.R. 3683 call for a voluntary system; S. 321, S. 825, H.R. 2782 and H.R. 2971 envision a mandatory one. To compensate for the revenue losses, most of these bills call for future Social Security benefits to be reduced or forfeited.

Still another approach, recently suggested by Representative Kasich (H.R. 3456), Speaker of House Gingrich, and Senator Roth would require that future budget surpluses be used to set up individual accounts to supplement Social Security benefits for those who currently pay Social Security taxes (they proposed no changes to the existing system).

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Yet other bills (H.R. 491 in the 104th Congress, H.R. 336 in the 105th) by Representative Solomon would create an investment board empowered to invest surplus Social Security funds in stocks and bonds as well as government securities. This is similar to the approach suggested in the Advisory Council's "maintain benefits" plan.

Many proponents of privatization see it as a way of reducing future demands for governmental financing and countering skepticism about the existing system by giving workers more of a sense of ownership of their retirement savings. Others feel that private investments would yield higher returns and a better retirement for workers since stocks and bonds generally have provided higher rates of return than are projected from Social Security. In concert with this, they argue that privatization would increase national savings and promote economic growth. Some feel that privatization would correct what they see as Social Security's contradictory mix of insurance and social welfare goals — that its benefits are not based strictly on a person's (and his or her employer's) contributions as a private savings plan would be, yet because it is not a means-tested program, many of its "social" benefits go to well-to-do recipients. Still others argue that privatization would prevent the government from using surplus Social Security revenues to camouflage borrowing or avoid raising taxes for other programs, thereby fostering spending cuts generally.

Opponents argue that Social Security's problems can be resolved without altering its fundamental nature. They fear that privatization would erode the social insurance nature of the current system protecting low-income workers, survivors and the disabled. Others are concerned that it would pose insurmountable transitional problems by requiring today's younger workers to save for their own retirement while simultaneously supporting current retirees. Some doubt that privatization would increase national savings, arguing that increased governmental borrowing would offset the increased private savings. They also contend that the investment pool created by privatization could be enormous, potentially distorting capital markets and subjecting the system to intense political pressure. Still others argue that privatization would expose participants to excessive market risk for something as essential as core retirement benefits and, unlike Social Security, which provides annual cost-of-living adjustments, would provide poor protection against inflation.

Growing Entitlement Spending Prompts Calls for Means Testing

Entitlements have risen significantly faster than the overall federal budget during the last 25 years, and now account for over half of all federal spending. Hence, curbing entitlement spending is seen by many as essential to controlling the federal deficit. The Concord Coalition[6] has made means testing entitlement programs the centerpiece of its plan for eliminating the deficit. Means testing would target government resources on those most in need by weighing personal income and assets in determining program eligibility and benefit levels.

Proposals such as the Concord Coalition's often include Social Security because the program accounts for 40% of all entitlement spending and is the largest federal entitlement. Proponents question the appropriateness of providing benefits to recipients with substantial independent means, noting that the wealthiest 40% of Social Security recipients derive less than 35% of their income from Social Security yet receive almost half of all Social Security benefits.[7] In the 105th Congress, H.R. 3082 (N. Smith) would reduce benefits for persons whose annual incomes exceed $50,000 (single person) or $100,000 (couple) and who are projected to receive more from Social Security than they and their employers paid in Social Security taxes.

Opponents of means testing see it as a breach of Social Security's fundamental principles, arguing that it would break the linkage between earnings and benefits. They argue that this linkage has fostered a perception that Social Security is an "earned right," and contend that means testing would weaken public support by making it seem more like welfare. They maintain that means testing would be demeaning to recipients, would add substantially to the SSA bureaucracy, would unfairly penalize people who, as the government has previously urged, saved for their retirement, and might discourage future savings since assets and the income derived therefrom would cause a reduction in one's eventual Social Security benefits.

The means testing debate is linked closely to the issue of taxation of benefits, which many view as an indirect form of means testing because taxation affects comparatively affluent recipients the most and exempts low-income recipients entirely.

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[6] The Concord Coalition is a nonpartisan organization founded by former Senators Warren Rudman and Paul Tsongas to enhance public discussion of the necessity of reducing federal deficits and other national economic issues and to present and promote policy alternatives.

[7] CRS Report 94-791, *Means Testing Social Security Benefits: An Issue Summary*, by Geoffrey Kollmann, Table 1.

Benefit Increases May Over-Adjust For Inflation

Social Security benefits and those of a number of other major entitlement programs, as well as various aspects of the income tax system, are adjusted annually to reflect inflation. These COLAs are based upon the U.S. Department of Labor's Consumer Price Index (CPI). It measures price increases for selected goods and services provided in the economy, rather than the cost of living *per se*. Although the CPI's rise has subsided considerably over the past year or two, in recent years, it has come under criticism for allegedly overstating the effects of inflation, notably because the market basket of goods and services underlying the index is not revised regularly to reflect changes in consumer buying preferences or improvements in quality. A Bureau of Labor Statistics (BLS) analysis in 1993 found that the overstatement might be as much as 0.6 of a percentage point annually, while cautioning that measuring the error precisely may prove to be extremely difficult.[8] CBO estimated in 1994 that the overstatement ranges from 0.2 to 0.8 of a percentage point. A similar study by the Federal Reserve Board estimated that it might be between 0.5 to 1.5 of a percentage point. The FY1996 budget resolution assumed that the annual adjustment of federal benefits and tax rates would be reduced by 0.2 percentage points, effective in FY1999, when CPI-measurement changes are eventually made by BLS. An advisory panel studying the issue for the Senate Finance Committee reported in December 1996 argued that the overestimate on average is 1.1 percentage points.

The budget impact of these figures can be significant. Federal Reserve Bank Chairman Alan Greenspan testified in February 1997 that a 1.0 percentage point reduction in the adjustment for inflation-indexed programs and income taxes would result in a federal savings of $150 billion over 5 years. Social security accounts by far for the largest share of the adjustments, comprising 80% of the COLA spending for federal entitlement programs. According to the SSA actuaries, a downward CPI revision of 1.0 percentage point annually beginning in 1998 would eliminate almost two-thirds of Social Security's long-range deficit.

In response to its own analysis as well as the outside criticisms, the BLS has made various revisions in its measurement of the CPI. To some extent, these revisions may account for part of the slower CPI growth seen in recent years. However, calls for further adjustments continue.

While some view further changes as necessary to bring Social Security and other entitlement expenditures under control, others contend that changing the measurement of the CPI is really a backdoor way of cutting benefits. They argue that the market basket of goods and services purchased by the elderly is different from that

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[8] Fixler, Dennis. The Consumer Price Index: Underlying Concepts and Caveats, Anatomy of Price Change. *Monthly Labor Review*, December 1993. p. 3-11. Another BLS study found that the CPI for elderly consumers may rise somewhat faster than the CPI generally (Amble, Nathan and Ken Stewart. Experimental Price Index for Elderly Consumers. *Monthly Labor Review*, May 1994. p. 11-15). More recently, the BLS reported in December 1996 that an experimental index for persons age 62 and older had risen 13% faster than the CPI-W over the previous 5 years.

of wage earners and salaried workers (around whom the CPI is constructed). It is more heavily weighted with health expenditures, which rise considerably faster than the overall CPI, and thus they contend that the cost of living for the elderly is higher than reflected by the CPI.

Disability Measures

Disability Insurance (DI), which is part of Social Security, and Supplemental Security Income (SSI), a welfare program, provide monthly cash benefits to the severely disabled. In the first half of the 1990s the costs of these programs rose rapidly. The combined number of their recipients rose from 6.2 million in 1984 to 10 million in 1995, i.e., by 60%. Disability awards under SSI, which is a means-tested program (i.e., recipients must have low income and few assets) financed by general revenues, grew faster than under DI. The number of disabled SSI enrollees climbed 65% between 1985 and 1993; DI enrollees climbed 35%. Most pronounced was the rise in mentally disabled enrollees; they comprised an estimated 60% of the disabled on SSI.

In the 103rd Congress a measure was enacted to shift payroll tax revenues from the OASI fund to the DI fund (P.L. 103-387). The precipitous growth of the program, resulting from both rapid enrollment and a declining rate of terminations from the rolls, and a slowdown in tax receipts resulting from the 1990 recession, had eroded the balances of the DI trust fund and its depletion was projected to occur in 1995. With the enacted tax reallocation, the DI trust fund was projected to remain solvent until 2015 (it is projected to be solvent until 2019 under the latest trustees' report).

In the 104th Congress both DI and SSI received considerable scrutiny because of concerns that not enough recipients were being routinely reexamined, criticisms that payments to alcoholics and drug addicts were fueling their habits, and allegations that many children with only mild impairments were receiving SSI. In response, Congress passed measures eliminating DI and SSI payments for substance abusers and authorizing new funding for more reviews of disabled recipients (P.L. 104-121). Welfare reform legislation (P.L. 104-193) tightened SSI disability eligibility for children and increased reviews of their eligibility.

A still declining rate of terminations from the benefit rolls is of ongoing interest to lawmakers concerned that these programs create disincentives for potentially employable recipients to seek rehabilitation and a return to work. The House Ways and Means Committee recently approved H.R. 3433, the Ticket to Work and Self Sufficiency Act of 1998, which revamps the process of how recipients receive rehabilitation services. It allows a greater number of recipients to choose from a broader range of rehabilitation service providers (i.e., from private for-profit and non-profit agencies as well as the traditional State government providers), stretches out provider reimbursements for up to 5 years, authorizes demonstration projects permitting partial benefits when recipients return to paid work, and extends Medicare protection for 5 years (up from 3 under current law) after a recipient's cash benefits cease (i.e., for those who participate in the new "ticket to work" program).

For Additional Reading

Financial Outlook

CRS Report 95-543. *The Financial Outlook for Social Security and Medicare*, by David Koitz and Geoffrey Kollmann.

CRS Report 97-741. *Social Security Financing Reform: Lessons From the 1983 Amendments*, by David Koitz.

CRS Report 91-129. *Social Security: Investing the Surplus*, by Geoffrey Kollmann.

CRS Report 95-543. *The Long-Range Social Security Projections*, by David Koitz and Gary Sidor.

CRS Report 94-622. *Social Security: Raising the Retirement Age: Background and Issues*, by Geoffrey Kollmann.

Privatization

U.S. Congressional Budget Office. *Implications of Revising Social Security's Investment Policies*. CBO Papers. Washington. September 1994.

U.S. Congressional Budget Office. *Social Security Privatization and the Annuities Market*. February 1998.

U.S. General Accounting Office. *Social Security Financing: Implications of Government Stock Investing for the Trust Fund, the Federal Budget, and the Economy*. Washington. April 1998.

CRS Report 998-195. *Social Security Reform: How Much of a Role Could Privatize Retirement Accounts Play?* by David Koitz.

CRS Report 96-504. *Ideas for Privatizing Social Security*, by David Koitz.

CRS Report 97-990. *Social Security in the United Kingdom: A Model for Reform?* by Geoffrey Kollmann.

CRS Report 95-839. *Social Security: The Chilean Example*, by Geoffrey Kollmann.

CRS Report 96-32. *Social Security: Worldwide Trends*, by Geoffrey Kollmann.

CRS Report 97-81. *Social Security: Recommendations of the 1994-1996 Advisory Council on Social Security*, by Geoffrey Kollmann.

CRS Report 94-593. *Social Security Taxes: Where Do Surplus Taxes Go and How Are They Used?* by David Koitz.

Money's Worth

CRS Report 95-149. *Social Security: The Relationship of Taxes and Benefits for Past, Present and Future Retirees*, by Geoffrey Kollmann.

Means Testing

CRS Report 94-791. *Means Testing Social Security Benefits: An Issue Summary*, by Geoffrey Kollmann.

CPI and COLAs

CRS Report 95-670. *Adjusting Benefits for Inflation: Impacts of Policy Change*, by James R. Storey.

CRS Report 94-803. *Social Security: The Cost of Living Adjustment in January 1998*, by David Koitz and Geoffrey Kollmann.