Will Social Security Bankrupt America?

My wife and I took Social Security early. We figured we might as well take the money while it was still available. Current events indicate it was a wise decision. Social Security is in trouble.

I read somewhere that Social Security payments started in 1940 with 1 beneficiary per 600 workers. By 2033 it looks as though there will be 1 beneficiary for every 2 workers. Our Social Security "surplus" is projected to begin its inevitable downward trend in 2009. By 2018 Social Security will be running an operating deficit that will increase with each passing year. There won't be enough worker income to pay for the beneficiary outgo.

How did we get into this financial mess?

There are three basic reasons.

Problem One: Demographics.

We keep having babies. After World War 2, returning GI's celebrated the joy of life by starting the Baby Boom. By 1964 they, and their happily nubile companions, had started a whole new generation that would shape the American economy for the next 75 years. The Boomer generation created outsized demands for diapers, bicycles, schools, cars, college educations, jobs, housing and health care.

And so here we are. Next on the Boomer agenda: Retirement.

Between 2008 and 2033 over the hill Boomers, their elders, and the 4.5 million immigrants who came to America during the same period, will be hitting the retirement rolls. Twenty three percent of the projected American population. Eighty five million beneficiaries. They will all need food, clothing, housing and medical care. Most will also need some form of senior care before they die.

Problem Two: Congressional prevarication.

Most Americans believed they were buying old age and survivors insurance based on rules set up by the 1935 Social Security Act. Each participant had a separate account. Wage earners paid into their accounts under the Federal Insurance Contributions Act (FICA). Self employed individuals paid into their accounts according to the rules of the Self Employment Contributions Act (SECA). Each account was backed by the financial integrity of the U. S. Government. Benefits would be paid according to the amounts credited to each account. Americans were led to believe that Social Security would provide a financial foundation for their retirement.

Big mistake. Congress used the money to fund the Federal budget. It's gone.

Problem Three: Social Security accounting is done with smoke and mirrors.

- First of all, it has been assumed that future deficits can be financed with current surpluses. That assumption is false. Our inability to switch even a portion of Social Security cash flow to private accounts is a tacit admission that there is no actuarial basis for the accumulation of individual account benefits. If Social Security were actuarially solvent, then the adoption of private accounts would simply mean we would be replacing one asset class with another investment vehicle.

- Second, despite claims to the contrary, there is no such thing as a "Trust Fund". Social Security "investments" are merely bookkeeping entries in which one branch of the Federal Government (the Treasury) promises to repay loans made to another branch of the Federal Government (Social Security). Congress then spends the money without regard for the ultimate value of the underlying "asset" which may in fact be worthless - or not even exist. Instead of requiring that our Social Security funds be spent on revenue producing capital investments, Congress has simply used the money to pay current expenses. Hence, any associated value is only backed by the "full faith" of the U. S. Government. Other than taxes, debt, or fund transfers from other Federal accounts, there is no way to satisfy future claims.

- Third, it has always been assumed that the Federal Government of the United States has sufficient credit to finance future Social Security payments. That assumption – as we will discuss below - is also false.

Boomers will demand increased benefits.

Read the Congressional Budget Office (CBO) analysis. About 25 percent of Boomers are not financially prepared for retirement. They will have to depend on Social Security for most or all of their income. Another 25 percent of the Boomer generation have some other income: a pension, a retirement plan, an annuity or two, and/or some money in the bank. They appear to have – with a little luck, careful money management, and the adoption of a sharply "downsized" lifestyle - the means to survive their senior years. Retirement financing for the remaining 50 percent of our Boomer generation ranges from "adequate" to "ample".

But the CBO's analysis sugar coats the fact that probably 18 to 20 percent of retirees will be living in poverty, and another 22 to 24 percent will be living an economically deficient lifestyle. Forty four percent do not have the means to replace at least half their pre-retirement income. Over 60 percent will not be able to afford the medical and institutional costs of old age. These people will have to survive on Social Security, Medicare, Medicaid, welfare, and whatever income they can scrape together. It will not be enough.

But only a fool would think the Boomers will be content to suffer economic indignity. Not the Me generation. Protest runs in the blood. And when they do, Congress will do the politically expedient thing: increase the benefits.

Everybody has a solution.

Congress has a solution: squabble and pontificate.

The Congressional Budget Office (CBO) has reported that it believes the American Social Security program can fund scheduled benefit levels through 2052. After that date, there will be a growing gap between Social Security benefit obligations and available funds. Unfortunately, all too many members of Congress look at this far distant date and conclude there is no crisis. At least for them. They figure we can fix Social Security by tweaking the benefits and increasing the tax income. By the time 2052 rolls around, their success or failure will only be a page in the historical record.

The Congressional Budget Office has a solution: work longer.

"Every additional year of work leaves members of a household with more income, a shorter retirement to finance out of pocket, more time to save and earn returns, and higher annual Social Security benefits, which are largely tax-exempt. Taken together, those factors can substantially reduce the private assets that the members of the household need to accumulate to maintain their working-age standard of living in retirement." (Reference: *A series of issue summaries from the Congressional Budget Office,* May 12, 2004.).

The Administration has a solution: reduce the benefits.

Decrease the benefits of upper income retirees, make the benefit distribution more "progressive", require Social Security applicants and beneficiaries to pass an annual "means" test, increase the participation age retirement, reduce the rate at which future benefits accumulate, reduce Social Security payments by understating the rate of inflation, and so on. In testimony before the House of Representatives on February 25, 2004, Federal Reserve Chairman Alan Greenspan suggested that a decrease in Social Security benefits would be "prudent". To quote: "The degree of uncertainty about whether future resources will be adequate to meet our current statutory obligations to the coming generations of retirees is daunting." ... "I believe that a thorough review of our spending commitments--and at least some adjustment in those commitments--is necessary for prudent policy."

As for the "Private Accounts" proposal, it's been condemned to legislative hell for no better reason than it would reduce the amount of money that Congress plans to spend on future Federal Budgets.

Whatever Congress Does – It will fail to fix Social Security.

Unfortunately, the acrimonious debate over Social Security is being conducted in an environment of deliberate legislative ignorance. No one wants to deal with the facts. Not the press. Not the Administration. Not Congress, the Liberal Establishment, the NeoCons, or the Beltway Bandits. No one wants to deal with reality.

That's too bad. Painful as it may be - reality is our future.

It's all in the assumptions.

Look at it this way. If you and I sat down at the kitchen table to predict the future of Social Security we would have to do what the CBO, the Social Security Administration, the American Association of Retired People, or anyone else does – we would have to make a whole bunch of assumptions. We would have to make estimates of future job creation, employment, unemployment, immigration, inflation, wages, income, Gross Domestic Product (GDP), as well as retiree demographics, benefits, retirement age, and supplemental income. Our kitchen table will be piled high with sheets of paper on which we have made innumerable calculations based on historical data.

But the past will not be the future.

No one – and I mean not a single soul – has dared mention the oil depletion factor. Every set of assumptions has been based on the belief that the next 25 years will be – with some minor adjustments - just like the last 25 years. That's really, really dumb. The next 25 years are definitely NOT going to be anything like that last 25 years. And because of this singular fact, every single published estimate of Social Security income and outgo is just plain wrong.

Oil depletion is real. Oil shortages will occur. And they will play havoc with our economy.

GDP

On a rate of change basis, GDP growth has been declining since the 1980s. There is a better than even chance GDP will be negative for one or more years long before 2025. So here we are, predicting that Social Security benefits will be a certain percentage of GDP.

What GDP?

Inflation

Inflation will derail any Social Security plan. Unless Congress acts to reduce benefits, higher prices will trigger increased Social Security payments. But no one has been willing to factor in the inflationary impact of oil depletion on the economy. Higher prices and shortages will increase the cost of living. That's for sure. We can even use historical data to prove our case. Two Middle East confrontations, one in 1974 and one in 1979, produced inflation rates of more than 10 percent.

In order to stimulate a recessive economy and pay for the cost of escalating welfare programs, Congress will add to the national debt. Government spending will increase as a percentage of GDP. Bush, Clinton and Congress will try to inflate the economy in order to avoid a recession. What happens to the financial future of Social Security if we have THAT kind of inflation? And by the way, how will Boomers in the lower 50 percentile of income be able to cope with non-stop increases in the cost of living?

Will the sinister specter of hunger and cold become a regular feature of our nightly newscasts?

Unemployment

Unemployment will also derail any Social Security Plan. Oil shortages and higher prices for petroleum products promise to drive a recessive economy. It has been assumed that Boomers will work longer, thereby easing the strain on Social Security funding. But if our economy is recessive, jobs for older Americans will be scarce. They will be forced to take early Social Security in order to survive.

And of course higher rates of unemployment will not only reduce the wage income that can be taxed to replenish the Social Security fund, out-of-work Americans will also demand additional unemployment benefits.

It all adds up to more debt.

The Federal Debt now stands at more than $7.6 trillion. Of this amount, the Treasury owes the Social Security "Trust" fund over $1.7 trillion. By 2018, the Federal debt will probably exceed $10.5 trillion. Annual interest payments will exceed $650 billion. Of these amounts, Treasury will owe America's Social Security beneficiaries over $3 trillion. Annual interest costs on Social Security debt will exceed $180 billion. Does this mean that America will have a negative net worth?

And that – as they say – is the crux of the problem. There will be a growing pressure to increase Social Security benefits in an era of decreasing national wealth. Will there be any money in the bank to pay the bills?

Probably not.

At some point the economic impact of oil shortages will trigger panic in the financial markets. Wealth destroying deflation is inevitable. Our stinking load of accumulated debt will have to be "restructured". A bankrupt America will not be able to finance its Social Security obligations.

The cultural shock will be incredible.

A Challenge

Neither the Bush Administration nor the Liberal establishment has faced up to the truth. All of the Social Security estimates are bogus. Non of the projections have attempted to assess the economic and cultural chaos of oil depletion. Congress is engaged in a bizarre debate about a surreal world that does not, and will not, exist.

So I close this article with a challenge to the Bush Administration and the NeoCons; to Senator Kennedy and the Liberals; get real. Either include the economic and cultural impact of oil depletion in your Social Security calculations, or prove that oil depletion is a myth.

Otherwise your acrimonious debate is nothing but political nonsense.

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