



## The Truth about Social Security



We hear many conflicting reports about Social Security in the news, reports which lead to a great deal of confusion and concern about the viability of future Social Security benefits. The truth is often much different than what we hear, and the situation with Social Security provides us with a timely illustration. Although it is true that Social Security is currently bringing in less from taxes than it is paying out in benefits, the Social Security trust fund is not projected to be exhausted until around 2035. Even after a complete trust fund depletion, Social Security is still projected to provide an equivalent of 75% of ongoing benefit payments. Though the reality is far short of the “bankruptcy” we hear bandied about frequently by our politicians, it is clearly a situation that needs addressing.

Social Security was created on August 14, 1935, with the signing of the Social Security Act by President Roosevelt. At the time 34 nations around the world had already implemented some form of Social Security, starting with Germany in 1889. Although the programs varied, all were founded with the intent to support individuals and society at large. Since its beginnings in the US, Social Security has undergone many changes, first to expand the benefits and then later to address pending financial difficulties. Currently, Social Security functions as a pay-as-you-go system designed to redistribute wealth from one generation to the next by transferring taxes from current workers to pay benefits to current recipients.

Social Security is funded from 3 different sources. Current workers pay into the system through FICA taxes on employment income. Workers pay 6.2% (4.2% in 2011) on the first \$106,800 (2011) of earnings, and their employers pay an additional 6.2% for a total of 12.4%. In 2010 this accounted for \$544.8 billion. In addition, higher income Social Security recipients pay taxes on a portion of the benefits they receive, accounting for \$22.1 billion in 2010. The remainder of the funding comes from interest earned on Social Security trust fund assets. In 2010, \$108.2 billion was generated from this source. Social Security paid out \$577.4 billion in benefits in 2010.

So what is the problem? In 1939 President Roosevelt created a Social Security trust fund to hold surplus funds created in years when tax revenues exceeded benefit payments, with the intent to use these funds in years in which outgoing benefits were greater than incoming tax revenue. This occurred in 2010. As the retiring of the baby boomer generation continues, this deficit is expected to expand, exhausting all of the trust fund assets somewhere around 2035. At that time current benefits will only be paid by then current FICA taxes, which is estimated to cover approximately 75% of those benefits, leaving a shortfall of approximately 25%. This is the “bankruptcy” so often referred to. In addition, Social Security is expected to maintain this benefit payment level far into the future.

What is the solution? This is not the first time SS has faced an impending depletion of funds. Changes have been made in the past to handle situations involving potential financial insolvency, once in 1977 and again in 1983. Changes generally fall into 1 of 4 categories:

- increase taxation on earnings,
- change the formula for calculating benefits,
- reduce cost-of-living adjustments, or
- raise the retirement age

Any one of these changes has the potential to fully offset the shortfall the system currently faces. Since most legislative proposals tend to project phase-ins over time, it is unlikely that those close to retirement will suffer a consequential impact to their earnings. Younger clients are more likely to suffer a more substantial change in their benefits as they have more time to prepare.

In any event, while there is an excess of fear being evoked by our current politicians regarding the health of our Social Security system, it is clear that it is not in the dire state they would like us to believe, and that Social Security is not “going away”. Although changes will certainly need to be made, they should not be so impactful as to cause serious disruptions to any taxpayer’s current financial situation. Want to read the full report? Go [here](#)

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