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## Social Security Financing\*

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After nearly 2 years of study, the 1979 Advisory Council on Social Security submitted its findings and recommendations in December. In February the **Bulletin** published the Executive Summary of the Council's report. Because of the continuing wide public interest in the future of social security financing, the Council's detailed findings and recommendations on that subject are published below. The Council unanimously reports that all current and future beneficiaries can count on receiving the payments to which they are entitled. Among the recommendations it calls for are partial financing with nonpayroll-tax revenues. Suggested changes include hospital insurance (HI) financed through portions of personal and corporate income taxes and a part of the HI insurance payroll tax diverted to cash benefits with the balance of this tax repealed. The Council also recommends that the social security cash benefits program be brought into long-run actuarial balance—with a payroll-tax rate increase in the year 2005. It rejects the idea of a value-added tax as being inflationary. Parenthetical remarks represent additional views of the Council members cited.

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The social security system has met all its obligations over the last 40 years, and this council is thoroughly convinced that any fear that benefit payments will be interrupted is unjustified. But we cannot be indifferent to reports that 80 percent of Americans, according to a recent survey, have "less than full confidence" in the social security system, and 40 percent, particularly younger workers, have "hardly any confidence at all."<sup>1</sup>

Mindful of the extent and nature of these concerns, the council has reviewed carefully the present financial condition of the social security program, the projections of its future condition, and the history of congressional and public attitudes toward social security financing.

After reviewing the evidence, the council is unanimously convinced that all current and future social security beneficiaries can count on receiving the benefits to which they are entitled.

The financial security of the social security system rests on the determination of the American people and their elected representatives to levy the taxes required to meet

benefit commitments. Furthermore, recent long-range projections indicate that taxes over the next 50 years already in place are sufficient and that any additional taxes necessary to pay for future benefits would not be excessively burdensome.

For more than 40 years each President and Congress have demonstrated a deep and continuous commitment to social security beneficiaries, current and future, by recommending and enacting taxes sufficient to pay for benefits for a very long period into the future (currently 50 years). Each year, the Congress asks the executive branch for projections of the future costs of the social security benefits then provided in the law, the revenues to be raised by the taxes then scheduled, and the balance between costs and revenues. Whenever these projections have indicated a need for adjustments in revenues, Congress has responded.

The strength of social security commitments rests not on the results of any particular set of projections, but rather on the repeatedly demonstrated willingness to adjust the schedule of future revenues whenever projections suggest that it is necessary. Nevertheless, in order to provide further reassurance to future beneficiaries, it is important that these projections show that revenues will be sufficient to cover scheduled benefit payments in the years ahead.

Recent long-range projections show that revenues in the

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\*For further details on these and other recommendations, see **Social Security Financing and Benefits: Reports of the 1979 Advisory Council on Social Security**, Department of Health, Education, and Welfare, December 7, 1979.

<sup>1</sup> Louis Harris and Associates, Inc., **1979 Study of American Attitudes Toward Pensions and Retirement**, Johnson and Higgins, 1979, page 94.

cash benefits programs will cover benefit commitments for the next 50 years. These projections show large surpluses beginning in the mid-1980's and continuing into the early 21st century.

To some extent public concern about social security financing is focused on what may happen during the first half of the 21st century, when according to current projections, there will be a relatively large number of social security beneficiaries as compared with people of working age, and the cost per worker of social security will be higher than it is today. While these projections are useful in alerting us to possible future trends, they are highly volatile and uncertain and cannot be the sole basis for permanent and far-reaching policy changes. The fertility rate and rate of growth of productivity, for example, are both notoriously difficult to predict. If they turn out to be higher than now projected, the long-run deficit could disappear. On the other hand, if they turn out to be lower than projected, the long-run deficit could be larger.

(By Ms. Falvey and Mr. Miller: We should not be lulled into complacency by this possibility. The projections of the fertility rate and the rate of growth in productivity could well be lower than expected. In that case the long-run imbalance could be worse. We cannot be confident that the fertility rate and productivity growth rate will turn out to be higher than expected. Therefore we must not dismiss the need to address the likely impact of the large demographic change projected to occur when the post World War II "baby boom population" begins to retire around 2010 causing a dramatic increase in the number of aged beneficiaries.)

If present trends continue, there is more than enough time and there are several ways to deal with them. First, the higher social security taxes that would be needed are modest. The scheduled cost of the old-age, survivors, and disability insurance program in the middle of the 21st century could easily be met by a payroll tax rate well below the levels prevailing in many industrialized countries today. Nor would the entire cost increase necessarily fall on the payroll tax; other sources of revenue might be tapped. Other possibilities that could be considered are increasing the retirement age by two or three years or modestly reducing the growth of scheduled benefits.

(By Mrs. Burns, Mr. Glasser, Ms. Hill, and Mr. Seidman: now or in the future, we do not think it should be accomplished through higher payroll taxes, increasing the retirement age, or benefit reduction. We favor using payroll taxes to finance a major portion of social security expenditures but we see no reason to raise payroll tax levels. If additional funding is required, it should be obtained from general revenues. Mrs. Burns and Mr. Pechman support the use of taxes other than the payroll tax if revenues are to be increased. Mrs. Burns would not rule out future changes in the retirement age and Mr. Pechman would not exclude benefit reductions as a means for achieving financial balance in the system.)

Americans should keep in mind that in many European countries, where social security systems are much older than ours, hyperinflation has decimated the assets of the social security system or war has destroyed the programs' records, and still the systems have promptly recovered. If other social security systems have survived such devastating events, it is inconceivable that ours would succumb to foreseeable economic or demographic shifts.

The next section provides an overview of how social security is financed and reviews the current financial projections. In the following section the council makes a major recommendation to reduce reliance on the payroll tax by financing the hospital insurance program with earmarked portions of the personal and corporation income taxes. Adoption of this recommendation will not only improve the way hospital insurance is financed but also will, at the same time, reduce total payroll taxes and improve the financial condition of the old-age, survivors, and disability insurance (OASDI) programs.

The remaining sections set forth the council's recommendations in four other areas—the level of the social security earnings base, the role of financial projections for social security, current-cost financing and the role of the trust funds, and protecting social security against the consequences of serious recessions. The effect of the council's financing and program recommendations on the cost of the programs is discussed in detail in Appendix A of the report.

## Overview of Social Security Financing

The old-age, survivors, disability, and hospital insurance programs are financed primarily through taxes levied on covered wages and self-employment income up to a specified maximum annual amount. Wage and salary workers and their employers each pay social security taxes at the same rate and on the same base.<sup>2</sup> The OASDI tax rate on covered self-employment income has generally (before 1973 and after 1980) been equal to three-fourths of the combined employer-employee rate. The self-employed pay hospital insurance taxes at the same rate as employees.

All OASDI taxes are deposited in three separate trust funds, one for old-age and survivors, another for disability, and a third for hospital insurance. All balances in these funds are invested in U.S. Government securities, and all benefit and administrative payments are made from the funds. The funds receive relatively small amounts of income from general revenues for interest on the investments of the trust funds and reimbursement for certain benefits.<sup>3</sup> The

<sup>2</sup> An employee who pays taxes on wages in excess of the annual maximum amount (because of work for two or more employers) is eligible for a refund of the excess taxes withheld, but no comparable refund is made to employers.

<sup>3</sup> Reimbursement is received for the cost of special cash benefits to noninsured persons age 72 and over, cash and hospital benefit payments resulting from noncontributory credits for military service, and hospital insurance benefits paid to certain people brought into the hospital insurance program when it was instituted, despite their ineligibility for social security cash benefits.

Secretaries of the Treasury, Labor, and Health, Education, and Welfare are designated as the trustees of the funds.

At least since 1950, it has been the practice to keep trust fund revenues in each year approximately equal to expenditures. Under this policy, known as current-cost financing, current revenues are almost immediately paid out to current beneficiaries. Future trust fund revenues collected from persons who will then be working will be used to finance the benefits that will be paid to then-current beneficiaries.

Under current-cost financing, the trust funds serve as contingency reserves against unforeseen increases in benefits or declines in revenues, such as may occur during a recession. The law does not permit benefit payments unless there is a positive balance or reserve in the trust fund.<sup>4</sup> The size of the reserve at the beginning of a year is generally expressed as a fraction of projected program outlays during that year.

(By Mr. Pechman: There is no need to interrupt benefit payments even when the trust funds are exhausted. All that is necessary is to provide a permanent authorization to make benefit payments. This would automatically allow continued payments of benefits from the general fund when the trust funds are exhausted and the trust funds could later be replenished by additional taxes. The proposal by the council to permit the trust funds to borrow (see below) is simply another way of accomplishing this result.)

High unemployment and slow growth in real wages reduced OASDI revenues well below expenditures in the mid-1970's. As a result, the combined OASDI trust funds declined from 73 percent of annual outlays at the beginning of 1974 to 29 percent at the beginning of 1979. One consequence of this decline in the trust funds is that until the trust funds have been rebuilt, a major, unforeseen slowdown in economic activity may exhaust the trust funds and require temporary increases in revenues to meet existing benefit obligations.

To counteract the trust fund losses attributable to the events of the mid-1970's, Congress in 1977 enacted major increases in revenues. The largest of these increases was not scheduled to take effect until 1981. In 1977, the decline in the trust funds was projected to continue until the 1981 rate increase took effect, after which a buildup of the funds was anticipated to commence. More recent economic forecasts, however, suggest that this buildup may not begin as soon as previously expected.

The fact that the trust funds are now relatively low means that a severe recession could reduce revenues enough to require increases in the tax rate or base that would not be needed if trust fund balances were at normal levels. This temporary situation is an aftereffect of the severe recession during the mid-1970's and has little bearing on the long-run financial strength of the social security system. Nonetheless,

<sup>4</sup> The Social Security Act provides that social security benefits shall be paid only from the OASI and DI trust funds (Sec. 201 (h) and the HI trust fund (Sec. 1815 (a)). If the trust funds were to be exhausted, legislation would be required to continue benefit payments from some other source.

this temporary situation cannot be ignored, and the council's recommendation for improving the financing of Medicare and the cash benefits programs would deal with it.

The long-term financial health of the OASDI system is assessed annually through 75-year actuarial forecasts. Under the intermediate assumptions in the 1979 trustees' report, surpluses are projected in each year between 1981 and 2010 when the combined OASDI trust funds will reach over three times annual outlays.

Starting around 2010, however, the trust funds are projected to decline as the large number of persons born in the years immediately after World War II begin to reach retirement age. The work force is not projected to increase commensurately because the fertility rate is now low and is projected to stay low by historical standards. The combination of these two trends would cause a significant increase in the average age of the American population. If these projections are borne out, social security revenues would have to be increased or benefits would have to be cut to keep the OASDI system in balance after the year 2030.

Table 1 summarizes the projected financial operations of the OASDI trust funds over the next 75 years as shown in the 1979 trustees' report.<sup>5</sup> In discussing the cost of social security, the use of numbers in absolute dollars can be confusing because there are continual changes in prices, wages, and other factors. In this table, therefore, and throughout this report, expenditures and revenues are expressed as average annual percentages of total taxable earnings. This measure of cost implicitly reflects future price and wage levels and focuses attention on the size of the tax burden to be borne by future workers and employers.

As can be seen at the bottom of table 1, the most recent projections show a surplus averaging 1.17 percent of payroll over the next 25 years,<sup>6</sup> a deficit of 0.86 percent of payroll over the following 25 years, and a deficit averaging 3.90 percent during the 25 years after that. The surplus during the first 25-year period is somewhat larger than the deficit during the second, leaving a slight surplus over the next 50 years.

Looking at the whole 75-year forecast period, however, the intermediate projections show the system to be 1.20 percent of payroll in deficit. However, for reasons set forth in the next section, great care should be exercised in interpreting such projections of revenue and expenditures many years in the future.

The hospital insurance program (Part A of Medicare), like OASDI, is financed almost entirely by taxes on covered earnings paid by employees, employers, and the self-

<sup>5</sup> 1979 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds. The figures shown are based on the intermediate set of assumptions, which represents the trustees' best guess of future economic and demographic developments. Projections are also made on the basis of less likely and less favorable assumptions, as well as on less likely but more favorable assumptions.

<sup>6</sup> In terms of today's taxable payroll, this represents an average of \$12.1 billion per year.

**Table 1.—Combined OASI and DI trust funds under Intermediate Assumptions in Trustees' Report, 1979-2055**

Calendar year	Estimated expenditures <sup>1</sup>			OASDI		
				Combined employer-employee scheduled tax rate	Difference	Trust fund ratio <sup>2</sup>
	Total	OASI	DI			
1979	10.36	8.97	1.39	10.16	-0.20	30
1980	10.56	9.16	1.40	10.16	-.40	25
1981	10.39	9.03	1.36	10.70	.31	22
1982	10.41	9.06	1.36	10.80	.39	23
1983	10.44	9.08	1.36	10.80	.36	26
1984	10.48	9.11	1.37	10.80	.32	29
1985	10.50	9.12	1.38	11.40	.90	32
1986	10.51	9.12	1.39	11.40	.89	40
1987	10.51	9.11	1.40	11.40	.89	48
1988	10.49	9.08	1.41	11.40	.91	56
1989	10.60	9.18	1.42	11.40	.80	64
1990	10.70	9.27	1.42	12.40	1.70	70
1991	10.69	9.25	1.45	12.40	1.71	85
1992	10.68	9.22	1.47	12.40	1.72	100
1993	10.68	9.19	1.49	12.40	1.72	16
1994	10.67	9.16	1.52	12.40	1.73	131
1995	10.67	9.13	1.54	12.40	1.73	147
1996	10.66	9.08	1.58	12.40	1.74	163
1997	10.64	9.02	1.62	12.40	1.76	179
1998	10.64	8.98	1.66	12.40	1.76	195
1999	10.64	8.94	1.70	12.40	1.76	211
2000	10.65	8.90	1.74	12.40	1.75	228
2001	10.66	8.87	1.78	12.40	1.74	243
2002	10.69	8.86	1.82	12.40	1.71	258
2003	10.74	8.87	1.86	12.40	1.66	272
2005	10.83	8.89	1.95	12.40	1.57	299
2010	11.58	9.46	2.12	12.40	.82	335
2015	12.79	10.57	2.22	12.40	-.39	323
2020	14.29	12.04	2.25	12.40	-1.89	263
2025	15.67	13.49	2.18	12.40	-3.27	170
2030	16.44	14.35	2.08	12.40	-4.04	<sup>3</sup> 59
2035	16.58	14.53	2.05	12.40	-4.18	( <sup>4</sup> )
2040	16.29	14.21	2.07	12.40	-3.89	( <sup>4</sup> )
2045	16.12	14.00	2.12	12.40	-3.72	( <sup>4</sup> )
2050	16.15	14.02	2.13	12.40	-3.75	( <sup>4</sup> )
2055	16.27	14.16	2.10	12.40	-3.87	( <sup>4</sup> )
Projected average:						
25 years:						
1979-2003	10.59	9.07	1.52	11.76	1.17	.....
2004-2028	13.26	11.12	2.15	12.40	.86	.....
2029-2053	16.30	14.21	2.09	12.40	-3.90	.....
75 years:						
1979-2053	13.38	11.47	1.92	12.19	-1.20	.....

<sup>1</sup> As percent of taxable payroll. Taxable payroll is adjusted to take into account the lower contribution rates on self-employment income, on tips, and on multiple-employer excess wages, compared with the combined employer-employee rate. Estimated expenditures are based on an assumed 9.8 percent benefit increase for June 1979. The actual benefit increase of 9.9 percent would make the estimated expenditures slightly larger than those shown for each year after 1978.

<sup>2</sup> Assets at beginning of year as a percent of expenditures during the year.

<sup>3</sup> The DI trust fund will retain a reserve equal to more than seven times outlays, but the OASI trust fund is projected to be exhausted.

<sup>4</sup> Fund projected to be exhausted.

employed. Actuarial forecasts, however, are made for only 25 years into the future because of the great uncertainty in any longer-range forecast of the relationship between future medical costs and general wage and price levels. Under current projections, revenue in the hospital insurance trust fund will grow in relation to annual outlays in the early 1980's and will decline rapidly thereafter. If the projections of the trustees for hospital insurance are borne out, additional financing or reductions in program costs would be

required to assure sufficient resources after about 1992. The costs of hospital insurance, like those of OASDI, will also be significantly affected by the fact that an increasing proportion of the population in the early 21st century will be elderly.

The supplementary medical insurance (SMI) program (Part B of Medicare) is the only element of social security not financed by payroll taxes. The revenues of the SMI trust fund are derived from payments from general revenues and premiums paid by eligible people who voluntarily enroll in the program.

When the SMI program began, the premiums from participants were intended to finance approximately half the cost of the program, with the remaining half to come from general revenues. The 1972 amendments, however, limited the rate of growth of the premiums to the percentage by which cash benefits were increased. As a result of this amendment and subsequent changes, general revenue payments to the SMI program have increased and now represent almost 70 percent of SMI revenues.<sup>7</sup> About 20 percent of parts A and B of Medicare combined are derived from general revenues.

### Reducing Reliance on the Payroll Tax

The council unanimously finds that the time has come to finance some part of social security with nonpayroll tax revenues. The majority of the advisory council recommends that the hospital insurance program be financed entirely through earmarked portions of the personal and corporation income tax and, beginning in 1980, that part of the current HI payroll tax be reallocated to the cash benefit programs to guarantee their financial soundness, and that the balance of the HI payroll tax be repealed. (If Congress elects not to implement this proposal in full at this time, the council unanimously recommends that the 1981 increase in payroll tax rates for hospital insurance—0.25 for employers and employees each—be replaced with general revenues.) (See supplementary statements on the use of general revenues by Ms. Davis, Ms. Falvey, Mr. Miller, Mr. Porter, and Mr. Van Gorkom and by Mr. Glasser, Ms. Hill, and Mr. Seidman.) The council majority recommends that the social security cash benefit programs be brought into long-run actuarial balance by scheduling a payroll tax rate increase in the year 2005. (See supplementary statement on the role of the trust funds and long-range projections by Mrs. Burns, Mr. Glasser, Ms. Hill, and Mr. Seidman.) The council unanimously rejects the use of a value-added tax to finance social security.

Over four decades successive advisory councils have recommended using general revenues to finance part of social security:

<sup>7</sup> Another factor in the increase in the amount of general revenue financing for the SMI program is the fact that when Medicare coverage was extended to disability beneficiaries, the premium rate for the disabled was limited to the rate charged the elderly.

• The 1938 advisory council recommended that general revenues eventually be introduced into social security and gradually be increased to the point where the program would be one-third financed from general revenue.

• The 1948 council concluded that there were "compelling reasons" for an eventual general revenue contribution to social security but that there was no current need to decide on the timing or amount of the general revenue infusions.

• The 1965 council recommended that a small general revenue contribution (equivalent to 0.15 percent of payroll for 50 years) be used to finance the cost of Medicare benefits for those already retired or disabled when the program began.

• The 1971 council recommended that one-third of parts A and B of Medicare taken as a whole should eventually be financed by general revenues.

• The 1975 council recommended that general revenues gradually be introduced into the hospital insurance program and that payroll taxes scheduled for the hospital insurance trust fund be gradually shifted to the old-age and survivors' and disability insurance trust funds.

Despite these recommendations the Congress has, with only minor exceptions, financed social security exclusively with payroll taxes. The council majority believes, however, that the passage of time has diminished the need for exclusive reliance on payroll taxes.

The council majority believes that the payroll tax suffers from two shortcomings as the sole source of funds for all social security benefits. First, the payroll tax falls more heavily on persons with relatively low incomes than does the personal income tax. (See supplementary statement on the regressivity of the payroll tax by Ms. Davis, Ms. Falvey, Mr. Miller, and Mr. Van Gorkom.) There are several reasons for this:

- There is a limit on the amount of earnings subject to the payroll tax.
- The payroll tax has no exemptions or deductions.
- The payroll tax rate is constant rather than increasing at higher income levels.
- Income from interest, rents, and profits is not subject to the payroll tax at all, and most of this income is received by persons in the highest income brackets.

Second, increases in payroll taxes contribute to inflation. They do so because the employer's portion of the tax directly adds to labor costs per unit of production. At a time when inflation is a major economic problem, increases in payroll taxes work directly against price stability. (By Mr. Miller: It is not necessarily true that increases in payroll taxes work directly against price stability. Many economists believe that increased employer payroll taxes are not passed on to the consumer in the form of higher product prices, but are passed on to the wage-earner in the form of lower wages or lower wage increases. Also, the increased employee payroll taxes reduce consumer demand and thus would tend to

lessen inflationary pressures rather than raise them. Furthermore, payroll taxes, even if they should net out to be inflationary, are less inflationary than deficit financing—particularly if the deficit is financed by government borrowing from the Federal Reserve Bank.)

Despite these shortcomings, the payroll tax is an appropriate source of revenue for the social security cash benefit programs. These programs pay benefits that are related to a person's earnings, and the council believes that they should be financed by a tax on those same earnings. (By Mr. Ackley, Mrs. Burns, and Mr. Pechman: A more appropriate way to finance social security cash benefits would be to rely on the personal income tax to provide at least part of the required revenues. The income tax, which is a much superior tax to the payroll tax, should be used to finance a major portion of the social security system.) Some council members believe that the payroll tax should provide the sole source of support for the cash programs; some believe it should be the major source of revenues but be supplemented from general revenues.

This argument in favor of payroll tax financing does not apply equally, however, to the hospital insurance program (Part A of Medicare). Everyone who is eligible for Medicare receives exactly the same protection. The amount of benefits actually received is related not to prior earnings but to the need for hospital care and related services.

Although there is no compelling reason to finance hospital insurance benefits from an earmarked payroll tax, there are at least two sound reasons for continuing to finance Medicare through some form of earmarked tax:

- Using a highly visible earmarked tax imposes fiscal discipline on the executive branch, the Congress, and the public. Any increase in coverage or the cost of benefits must be accompanied by a visible tax increase sufficient to pay for it.
- The use of earmarked taxes helps assure the payment of benefits as promised and without a means test. Because most beneficiaries will have paid taxes during their working years devoted explicitly toward their Medicare protection, it would not be politically acceptable to make major cutbacks in protection or to deny benefits by the introduction of a test of means. (See supplementary statement on the use of earmarked income taxes by Mr. Ackley, Mrs. Burns, Mr. Glasser, Ms. Hill, and Mr. Seidman.)

The council majority therefore recommends that starting in 1980 the hospital insurance program be financed entirely from an earmarked portion of the personal income tax and from a matching payment to the trust funds drawn from corporation income taxes. (By Mr. Pechman: Although I do not object to earmarking taxes for the hospital insurance program, I believe it is mere window dressing. The visibility of the payroll tax which finances hospital insurance now has not exercised any constraint on cost. Moreover, whatever the source of financing, there is no reason to expect hospital insurance to be means tested now that benefits have been paid for over a decade.)

The council further recommends that a part of the tax rate currently scheduled for hospital insurance be shifted to the OASDI program and that the balance of the currently scheduled hospital insurance tax rate be repealed in order to allow a reduction in the total payroll tax rate. Together, these two changes could allow the total 1980 social security tax rate to be less than the total 1979 and 1980 payroll tax rate of 6.13 percent (including hospital insurance). The rate for 1981 would be significantly less than the 6.65 percent rate (including hospital insurance) scheduled for 1981. The change also would allow the scheduled ad hoc increases in the earnings base to be eliminated, as the council recommends in the next section of this report. And it would remove any possibility of short-term cash flow problems in OASDI in 1983 and 1984.

Based on the intermediate economic assumptions underlying the 1979 trustees' report, an OASDI tax rate of 5.6 percent beginning in 1980, together with the repeal of the 1980 and 1981 ad hoc increases, would produce by the end of 1984 a balance in the combined funds equal to 48 percent of 1985 expenditures. While this level is below what the council believes is a desirable target, it represents reasonable progress. The council recognizes that the future direction of the economy is uncertain at the time this report is being prepared. If, at the time the Congress is considering action, economic projections are less favorable than those in the 1979 trustees' report, the appropriate OASDI tax rate may be somewhat higher than 5.6 percent. Modifying the OASDI tax rate to reflect new economic projections would be both appropriate and consistent with the council's basic recommendation.

The precise method by which this reform in the financing of social security should be implemented depends critically on overall economic conditions and the tax policy that is appropriate for those conditions. For example, the council is aware that many experts believe that taxes should be reduced in the near future to combat a slowdown in economic activity and that others favor tax reductions to offset the tendency of inflation to push people into higher income tax brackets.

The council is not qualified to pass judgment on when or by how much total tax collections should be reduced. The reforms in the financing of social security that we advocate, however, can be undertaken whether total federal taxes are reduced or not.

The council's recommendations to reduce the total payroll tax rate from 6.13 to 5.60 percent in 1980 and to eliminate the scheduled ad hoc increase in the earnings base would reduce 1980 payroll tax collections by about \$14 billion. If this decrease is considered too small for purposes of economic stabilization, Congress could enact such further reductions in personal or business taxes or undertake other countercyclical measures indicated by economic conditions. If the tax decrease is considered too large, other taxes could be raised.

(By Mr. Ackley and Mr. Pechman: If additional tax

reductions are needed for stabilization purposes in the near future, Congress should make additional reductions in the payroll tax.)

In either case, a portion of each taxpayer's personal income tax liability would be designated on the taxpayer's return as that individual's (or couple's) payment for hospital insurance. The part of the personal income tax allocated to hospital insurance would not exceed a given amount for each taxpayer. This source of income would raise half the money needed to pay hospital insurance benefits under Medicare.<sup>8</sup> The general fund of the Treasury would make a matching payment to the hospital insurance trust fund designated as coming from corporation income tax collections.

The amount of the earmarked taxes would be adjusted from time to time as needed to maintain a satisfactory working balance in the hospital trust fund. The earmarking procedure would not, however, affect an individual's or a corporation's total income tax liability, which would continue to be determined by broad tax policy considerations. Changes in the rates of the personal and corporation income taxes could be made at any time without disturbing the funds earmarked for hospital insurance.

Should Congress not accept this recommendation in full at this time, the council unanimously recommends that, at the very least, the 1981 increase in payroll tax rates for hospital insurance (0.5 percent combined) be replaced with general revenues. This move would be fully consistent with the council's broader recommendation.

The council also recommends that the social security cash benefit programs be brought into long-run actuarial balance by scheduling a payroll tax rate of 7.25 percent in the year 2005 and thereafter. Scheduling this rate would remove any basis for questioning the financial soundness of social security and show that the program can be financed for the foreseeable future without an undue burden on payroll taxpayers.

There are two reasons, however, that this rate increase would probably not go into effect in precisely this form. First, the 7.25-percent rate is a level rate designed to balance the system over the 50-year period from 2005 to 2055. The rate necessary to finance the system on a current-cost basis would be less than 7.25 percent early in that period and more than 7.25 percent later on. Second, the social security system could equally well be brought into balance when the time comes through other means, such as the use of general revenues or reductions in the rate of growth of real benefits.

Although the council supports financing the hospital insurance program through earmarked personal and corporation income taxes, we unanimously reject the introduc-

<sup>8</sup> The amount of revenue needed in 1981, for example, could be raised by a tax of 1.23 percent of taxable personal income up to \$27,000 for single individuals and \$54,000 for married couples. Alternatively, the revenue could be raised through a personal income tax surcharge of 6.7 percent, with a maximum payment of \$400 for single individuals and \$800 for married couples.

tion and use of a value-added tax to finance HI or any other part of social security. The introduction of a value-added tax at this time would aggravate the already intractable problem of inflation. It would represent federal intrusion into a revenue source—sales taxation—customarily reserved for States and localities. It is a less desirable source of revenue than the personal income tax because it makes no allowance for personal exemptions or deductions and because its rates are proportional to consumer purchases rather than progressive in relation to income. All estimates suggest that the distribution of burdens under a value-added tax would be regressive over much of the income distribution (even if necessities were exempt), because consumption represents a considerably smaller fraction of income for high-income than for low-income people.

The payroll tax has many of the same characteristics as the value-added tax (it too is regressive, if viewed apart from the benefits it finances), but as compared to the value-added tax it has some important advantages. The payroll tax is levied on the same base used to compute social security cash benefits and thus helps sustain the principle that social security benefits are an earned right. Because the payroll tax is a tax on the earnings that determine the amount of a person's benefits, it has a compelling logic that the value-added tax does not have. Also, because the payroll tax is highly visible, it helps preserve fiscal discipline. (By Mr. Pechman: The visibility of the payroll tax has not retarded the growth of benefits and therefore it has not contributed to the preservation of fiscal discipline.)

All members of the council agree that for the foreseeable future, payroll taxes should form either the major or the sole source of revenue for OASDI cash benefits. The council sees no point in replacing payroll taxes with value-added taxes, a move that would significantly worsen the distribution of tax burdens, aggravate inflationary problems, and undercut important principles of social security financing.

### Level of the Earnings Base

The council majority recommends that the social security earnings base be set at a level that captures the same fraction of aggregate earnings as was covered in 1979. (See supplementary statement on the level of the earnings base by Ms. Davis, Mr. Glasser, Ms. Hill, and Mr. Seidman.) The

majority also recommends that the payroll tax rate at which employers pay social security taxes continue to be the same as that for employees. Further, the council majority recommends that as long as inflation remains a serious problem the base on which employers and employees pay taxes remain equal.

The earnings base plays two roles in the social security program. First, it limits the amount of an employee's earnings and an employer's wage payments that are subject to the payroll tax. Second, it is the maximum annual amount of earnings that can be credited to a worker for subsequent benefit computations.

Under current law the earnings base is ordinarily adjusted automatically to keep pace with rising wage levels. Unless this automatic adjustment process is overridden by a legislated ad hoc change, the relationship between the wage base and average earnings will remain constant.

In 1978, all of the earnings of about 84 percent of all workers in covered employment were subject to the social security tax, and some 84 percent of the aggregate covered earnings was taxable. Legislated ad hoc increases, effective in 1979, 1980, and 1981, however, will increase the fraction of workers having all earnings subject to taxation to 92 percent in 1981, and the fraction of covered earnings subject to tax will rise to 89 percent.

The council majority believes that these ad hoc increases will raise the earnings base unnecessarily. It believes that beginning in 1980 the base should be increased only as the result of the automatic adjustments so that the relative level of the base attained in 1979 will be maintained on a long-term basis, as shown in table 2. At the 1979 earnings base, about 90 percent of workers have their entire earnings taxable and about 87 percent of aggregate covered earnings is subject to the tax. (See supplementary statement on the level of the earnings base by Mr. Ball.)

Raising the earnings base for employees beyond this level will cause an undesirable intrusion into areas better left to private saving and pensions. Social security was designed from the beginning to work in combination with private pensions and saving. Increasing the earnings base beyond its current level would extend social security coverage to a level of income where forced saving is unnecessary and where the provision of additional retirement income is better left to private saving and pensions.

**Table 2.**—Effect of advisory council proposals on tax rate and earnings base under Intermediate Assumptions in Trustees' Report, 1979-2055

Calendar year	Tax rate (employer and employee, each)						Earnings base	
	Total		OASDI		HI		Present law	Council
	Present law	Council	Present law	Council	Present law	Council		
1979 .....	6.13	( <sup>1</sup> )	5.08	( <sup>1</sup> )	1.05	( <sup>1</sup> )	\$22,900	( <sup>1</sup> )
1980 .....	6.13	5.6	5.08	5.6	1.05	0	25,900	\$24,900
1981 .....	6.65	5.6	5.35	5.6	1.30	0	29,700	27,000
1982 .....	6.70	5.6	5.40	5.6	1.30	0	32,100	29,100

<sup>1</sup> No change.

It is also very important that the earnings base be predictable. Because the earnings base determines the social security benefits of high-wage workers, it also determines the supplementation needed from private pensions and saving. Private pension plans cannot be designed and informed decisions on personal saving cannot be made if the social security earnings base, and thus future benefits, are adjusted in an erratic and unpredictable way. The council prefers that the earnings base be stabilized at its 1979 level. If that is not done, however, there should be no further ad hoc increases after 1980 or, at the very least after 1981. The council recognizes that elimination of the scheduled ad hoc increases in the earnings base will require additional financing from a different source. Consequently, a majority of the council favors retaining the present law earnings base for 1980 and 1981 unless the revenues lost as a result are replaced through another means such as is provided by the OASDI tax rate increase recommended earlier.

Some have argued, and the Administration in 1977 proposed, that the limit on earnings subject to social security employer taxes should be eliminated. This step would increase revenues by 5 percent (the equivalent of 0.6 percent of taxable payroll) without resulting in additional benefit payments, because benefits depend on the earnings on which the employee pays taxes.

All members of the council agree that eliminating the employer base now or in the near future would be undesirable because of the inflationary effect of such a tax increase on employers. A narrow majority of the council would be prepared to consider this option when inflation abates.

(By Ms. Falvey, Mr. Miller, and Mr. Van Gorkom: Eliminating the maximum base on employer contributions is undesirable regardless of the reason used and should not be considered even in a less inflationary time. We believe that the present system of taxing employers and employees equally, which has been followed ever since the system began, is broadly accepted as an appropriate basis of financing. Higher employer payroll costs from abandonment of the maximum base will either be passed on to the public in the form of higher prices or to employees in the form of lower wages. Furthermore, such cost increases would likely result in fewer funds becoming available from employers for their employee pension programs.)

These members argue that the employer tax should be considered a contribution to the system as a whole, rather than a contribution on behalf of a specific individual. They view the employer contribution as the source of support for elements of social security benefits that advance social adequacy and under appropriate circumstances would support increases in these elements. Other members would favor increases in the employers' base rather than the employees' as a device of raising revenues without generating higher benefits for high-wage workers. A substantial minority of the council finds, however, insufficient merit in the proposal to warrant breaking the long tradition of equal employer and employee payments.

The majority of the council also rejects any move that would make the payroll tax rate paid by employers different from the rate paid by employees. (By Mr. Ackley and Mr. Pechman: There would be merit in reducing the employer tax rate at this time over and above any reduction in the employee tax rate in order to reduce business costs and help to moderate increases in prices.)

## Financial Projections For Social Security

The council finds that the methodology now used to make financial projections is sound and that the assumptions are reasonable. (By Mr. Ball, Ms. Davis, Mr. Glasser, Ms. Hill, Mr. Porter, and Mr. Seidman: We do not find the assumptions underlying the financial projections unreasonable but we have suggested in our supplementary statement on the long-range actuarial assumptions several ways in which we think they could be improved. If the assumptions were changed as we suggest, the long-range cost of the program would be shown to be significantly lower than in the official cost estimates. See also supplementary statement on long-range actuarial assumptions by Mrs. Burns, Ms. Davis, Mr. Glaser, Ms. Hill, Mr. Porter, and Mr. Seidman.) The council recommends, however, that more systematic account should be taken of the interrelationships among the different economic and demographic assumptions underlying the projections.

The council recommends that 75-year financial projections continue to be made; these projections focus public attention on long-run economic and social trends that will significantly affect the cost of benefits. Decisions to alter presently scheduled social security benefit payments or the present schedule for social security financing, however, should not be made primarily on the basis of economic and demographic projections more than 50 years in the future. (See supplementary statement on the use of long-range projections by Mr. Aaron, Mr. Ackley, and Mr. Porter.)

The advisory council appointed a panel of economists and actuaries to assist in evaluating the role of long-run financial projections in social security and the validity of the projections now being made. The panel concluded that policy need not respond immediately to forecasts of developments 50 or 75 years in the future, but recommended that the current practice of making 75-year financial projections be continued.<sup>9</sup> The council agrees with the panel's recommendation.

The long-term costs of the social security cash benefits programs depend on such future economic and demographic developments as the rate of growth of productivity, the birth rate, and longevity. Obviously, cost projections are progressively less reliable the further into the future they are extended.

For example, virtually everyone who will be in the labor force and will be paying social security taxes 20 years from now has already been born. On the other hand, fewer than

<sup>9</sup> This report is included as Appendix B to the full report.



half of those will be working 50 years hence and undoubtedly very few of those who will be working 75 years hence are now alive. Furthermore, birth rates have varied widely and unpredictably in the past and unquestionably will continue to fluctuate in the future.

Although no policy changes should be made solely on the basis of projections more than 50 years in the future, we believe that, for at least three reasons, 75-year projections should be retained. First, such long-range projections help assure that the possible financial consequences of benefit promises are understood. Social security, by its very nature, entails long-term commitments. Some people who retire this year will still be receiving benefits in 25 years. Young people now entering the work force will have only just begun to receive retirement benefits 50 years from now. Roughly half of those born this year will still be alive and receiving benefits in 75 years. In a system with such long-term commitments, we are obligated to take a long-term look into the future, even if the view at the end of the projection period is rather hazy.

The projections provide reassurance that the costs of social security will not become an intolerable burden on taxpayers in future years. If the projections turn out to be inaccurate, the costs of the system may turn out to be slightly greater or less than we now think, but the projected costs are unlikely to diverge from the actual to such an extent that major, unexpected tax increases will be required.

Second, long-run projections alert us to trends that have little immediate effect but eventually become very important. For example, the long-run projections alerted us to defects in the indexing method adopted in 1972; as a result, Congress in 1977 enacted a better method of indexing benefits. The long-run implications of the post-World War II baby boom and the recent decline in birth rates have also been brought to society's attention, primarily through social security's long-run financial projections. The uncertainty of future birth rates should not be allowed to obscure the consequences should our best estimates turn out to be approximately correct.

Third, however uncertain long-run projections may be, this would be a particularly inappropriate time to discontinue them. The system is now projected to be in balance over about the next 50 years and to be in deficit only in the last 25 years of the 75 year projection period. Shortening the projection period would reduce the margin of error implicit in the long-range projections and might reduce needless worry over a long-run deficit that may not occur; but many would portray such a change in established procedures as an attempt to cover up underlying problems in social security and to balance the system through actuarial legerdemain. Shortening the projection period might therefore lead to a reduction in public confidence in social security.

Projections of the distant future, however, are by themselves insufficient as a basis for current policy changes. The history of the official population projections illustrates the

need for caution in basing policy on long-run projections.

- In 1945, after a period of low birth during the Depression and World War II, official U.S. Census Bureau projections showed a long-run total fertility rate of 2.0 children per woman.
- In fact, birth rates rose dramatically; the official Census long-run projection was revised in 1957 to 3.3 children per woman.
- In the past 10 years birth rates have declined equally dramatically and the official Census projections now predict a long-run fertility rate of 2.1 beginning early in the next century.

Clearly, no permanent and far-reaching policy changes should be made solely on the basis of such volatile projections. While the council has recommended balancing the financing of the system and further reassuring the public by scheduling a tax rate increase for the year 2005, for example, we have recognized that this increase might never actually have to go into effect or would be translated into an equivalent schedule of pay-as-you-go rates.

The panel of consultants also examined the assumptions and methodology underlying the current long-run financial projections and found them to be reasonable. Most of the specific changes recommended by the panel have been incorporated into the projections in the 1979 trustees' report, and the council therefore believes that the trustees' intermediate long-run projection is sound.

The panel also recommended, and the council concurs, that more systematic account should be taken of all known interrelationships among different economic and demographic assumptions underlying the forecasts. For example, while no one can be certain whether fertility will rise or fall in the future, it is probable that the higher female labor-force participation, the lower will fertility be. As another example, a decline in the number of younger workers may lead to increased employment of the aged. Taking account of such interactions would probably narrow the difference between the high- and low-cost projections customarily made by the trustees.

## **Current Cost Financing And the Role of the Trust Funds**

The council unanimously recommends that the social security system continue to be financed on a current-cost basis with the trust funds continuing to serve primarily as contingency reserves.

The council finds that a reserve balance of 75 percent of annual outlays is sufficient for contingencies in the absence of the council's proposals for countercyclical general revenues and borrowing authority, both of which are described below. If these proposals are adopted, a reserve of 60 percent of annual outlays is a sufficient contingency.

The council recommends that the trustees notify the appropriate committees of Congress promptly if the trust fund is expected to fall below these target levels or greatly to exceed them.

The desired size of the social security trust fund depends on the purpose the funds are supposed to serve. Possible purposes and implied reserve levels include:

- To "fully fund" social security benefits earned to date. This would require balances on hand sufficient (together with future interest earnings) to meet all benefit commitments and administrative costs based on earnings already recorded.
- To promote savings and capital formation. Balances would have to be sufficient to finance a substantial increase in private investment.
- To provide a contingency reserve against unforeseen economic and demographic developments. Balances would be needed only to cover temporary excesses of outgo over income.

It is generally agreed that, while full funding is desirable for most private pension obligations, it is not necessary in order to assure the payment of social security benefits. In contrast to private pensions, the participation of future workers in the social security system is required by law and the future revenues of the program are assured by the Federal Government's taxing power.

In addition, most people who have studied social security, including the concerned Congressional committees and every previous advisory council except one, have concluded that there is no need to accumulate balances beyond those necessary for a contingency fund. This council agrees with that conclusion. It believes that, with the possible exception of some advance funding in the 1990's and the early years of the 21st century to smooth out the social security taxes levied to provide retirement benefits to the baby boom generation, the social security system should continue to be financed essentially on a current-cost basis.

The trust funds have, in fact, gradually evolved into such a contingency reserve: Basically, current revenues are used to pay for current benefits and the trust funds have come to serve the role of absorbing unintended surpluses or covering unintended deficits.

In recent years, a few economists have urged the abandonment of traditional policy and practice and the accumulation instead of larger reserves in order to encourage capital formation. Some advocating this change claim that the availability of social security benefits has reduced private savings for retirement. Others hold that even if social security has not affected private saving, general capital accumulation needs to be increased and that creation of enlarged social security reserves would contribute to such an increase. It is argued that large accumulations in the trust funds would offset any tendency for social security to reduce savings, provided that fiscal policy was otherwise unaffected—that is, if the social security surplus were not offset by a general fund deficit.

The council considered these arguments and rejects them unanimously. We note that:

- The evidence on the effect of social security on saving is mixed and the size of the effect if any, is unclear.<sup>10</sup> (By Ms. Davis, Mr. Miller, and Mr. Van Gorkom: There cannot really be any serious doubt that social security has an effect on the formation of the nation's capital. The intense debate which rages on the subject today centers only on the nature and extent of that effect.)

- If more saving is desirable and if such saving should be financed by the U.S. Government, a social security surplus is neither necessary nor sufficient for achieving such an increase. It is not necessary because running a surplus in the general fund (the part of the Federal budget other than trust funds) would directly increase saving even without a surplus in the social security system. It is not sufficient because an increased social security surplus could be offset by increased deficits in the general fund.

- A governmental surplus would not automatically increase total saving; unless private investment increases, it would merely reduce aggregate income. Some economists believe that the effective way to increase private capital formation is to stimulate private investment directly, adjusting the general-fund balance as necessary to prevent excessive total demand.

Under the policy being endorsed by this council, the social security trust funds serve primarily as reserves against unforeseen economic fluctuations. As contingency reserves, the trust funds should have balances sufficient to ensure continuation of payments during a severe recession without an immediate tax increase.

The panel of actuaries and economists advising the council has considered the issues involved in determining the size of the needed contingency reserve and has recommended setting a trust fund goal of a minimum of 75 percent of annual outlays.<sup>11</sup>

The council endorses the panel recommendation if the council's proposal for countercyclical infusions of general revenues is not adopted (see the following section of this article). With the availability of countercyclical general revenues, a 60-percent reserve would provide the same protection as a 75-percent reserve would provide without countercyclical general revenues.

Because the trust funds have been seriously depleted over recent years, it is not possible to achieve the target trust fund balances immediately. The council believes, however, that substantial progress toward reaching the targets must be made as quickly as is prudent.

Finally, the council recommends that the trustees of the social security funds notify the appropriate committees of Congress whenever the trust fund is projected to fall below 75 percent of outlays (or 60 percent, with countercyclical general revenues) within the following 3 years or is projected to go considerably above that level.

<sup>10</sup> See Selig B. Lesnoy and John C. Hambor, "Social Security, Saving, and Capital Formation," *Social Security Bulletin*, July 1975; Louis Esposito, "Effect of Social Security on Saving: Review of Studies Using U.S. Time-Series Data," *Social Security Bulletin*, May 1978; Robert J. Barro et al., "Social Security and Private Saving: Another Look," *Social Security Bulletin*, May 1979.

<sup>11</sup> Report of the Panel of Consultants, Part IV.

## Protecting Social Security Against Economic Fluctuations

A majority of the council recommends general revenue payments to the social security trust funds during periods of high unemployment to compensate the trust funds for revenues lost due to high unemployment. Such payments would be made only if the reserves were less than 60 percent of annual outlays.

A majority of the council also recommends that the trust funds be authorized to borrow from the Treasury in the event that reserves fall below 3 months' payments of benefits.

In the event of such borrowing, repayment of the loan would begin automatically when reserves reached 5 months' payments. To assure repayment, payroll taxes would be increased automatically if the loan were not otherwise repaid within 2 years, and provided that unemployment was not greater than 6.5 percent.

(By Mrs. Burns, Ms. Davis, Mr. Glasser, Ms. Hill, Mr. Pechman, and Mr. Seidman: We support the council's recommendation for borrowing authority but repayments should be made without increasing payroll tax rates. We especially think that payroll tax increases should be delayed until the economy has recovered and employment has expanded sufficiently that the loans can be repaid.)

The council unanimously recommends the merger of the old-age and survivors' insurance trust fund and the disability insurance trust fund into a single fund but retention of separate annual cost analyses.

The council's major financing recommendation—set forth earlier in this article—is to strengthen the financing of social security by using earmarked personal and corporation income taxes to pay for hospital insurance benefits. That recommendation will also allow the OASDI payroll tax rate to be increased, a step that will provide enough revenue to pay for social security cash benefits for the foreseeable future. The council believes that several other features, however, should be added to the financing of the program to deal with any unforeseen problems that might conceivably arise in the future.

The council majority believes that social security should be insulated from recession by three mechanisms.

First, automatic payments to the trust funds should be made from general revenues when unemployment rises above a specified level. In 1977, President Carter proposed that the social security trust funds receive general revenue payments to compensate them for the decline in payroll tax income below levels that would accrue at a 6-percent unemployment rate. The council majority recommends such payments only if trust fund balances are less than 60 percent of annual outlays, but otherwise endorses the concept advanced in 1977. This proposal would:

- Reduce the chance that payroll taxes would have to be raised during a recession.

- Reduce the level of reserves needed for safe operation of the social security system. A reserve of 60 percent of outlays with countercyclical general revenue financing would provide as much protection against a recession as a reserve of 75 percent of outlays without this protection.

- Introduce general revenues in a way that strictly limits their use in the OASDI programs, (By Mr. Ackley, Mrs. Burns, Mr. Glasser, Ms. Hill, Mr. Pechman, and Mr. Seidman: We do not regard this as an advantage.)

Countercyclical general revenues will not, by themselves, assure that reserves are always sufficient to weather a recession. The council majority therefore recommends that if reserves fall below three months' outlays, the trust funds should be authorized to borrow from the general fund enough to bring the funds back up to the level of three months' benefits. Repayments of the loan with interest would begin whenever the balance in the fund reached 5 months' outlays. If the loan is not repaid within 2 years, payroll taxes should be increased automatically to repay the amount outstanding, provided that the national unemployment level is below 6.5 percent.<sup>12</sup>

The loan provision closely resembles one passed by the House of Representatives in 1977. Unlike the House-passed plan, however, the council's plan would not trigger a payroll tax increase so long as unemployment remains unacceptably high. In its 1977 report, the House Ways and Means Committee said, "In view of all the extensive publicity the financing difficulties of the program have received and the resulting concern about the financial soundness of the program... an appropriate guarantee such as that recommended by your committee is necessary and desirable." The council majority concurs in this assessment and believes that, as long as provision for automatic repayment is made, the borrowing authority does not represent a major departure from the current method of financing social security.

Our third recommendation, to combine the old-age and survivors' insurance and disability insurance trust funds into a single fund, would prevent the need for legislative action to readjust taxes when one fund is low and the other is ample. It is sound planning and management to maintain separate analysis of the costs and revenues of OASI and DI, but the council does not believe there is any longer a need to maintain separate trust funds.

When the disability insurance program was enacted in 1956, experience on which to base cost estimates was sparse. Congress feared that unexpectedly high costs for the new program could adversely affect OASI, and it therefore set up a separate DI trust fund to remove such a risk. In practice, however, the Congress has concerned itself primarily with the overall OASDI tax rate rather than the technical matter of the specific allocation of this total rate between the

<sup>12</sup> Particular figures cited in this discussion—three months' outlays, five months' outlays, and 6.5 percent unemployment—as well as similar figures cited in the countercyclical general revenue discussion should be interpreted as illustrative of the magnitudes the council majority believes appropriate. Slight variations in any of these parameters would be consistent with the council's recommendations.

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## Membership of the 1979 Advisory Council on Social Security

Henry J. Aaron, Chairman;  
Senior Fellow, Brookings Institution.

Replaced Stanford G. Ross, who  
resigned to become Commissioner  
of Social Security.

Gardner Ackley,  
Professor of Political Economy,  
University of Michigan.

Robert M. Ball,  
Senior Scholar, Institute of  
Medicine, National Academy of  
Sciences.

Eveline M. Burns,  
Professor Emeritus of Social Work,  
Columbia University.

Grace Montanez Davis,  
Deputy Mayor,  
City of Los Angeles.

Mary C. Falvey,  
Senior Vice President and Director,  
Blyth Eastman Dillon & Co., Inc.  
Replaced Jane Cahill Pfeiffer.

Melvin A. Glasser,  
Director, Social Security Department,  
United Auto Workers International Union.

Velma M. Hill,  
Vice President, American Federation  
of Teachers.

Morton D. Miller,  
Vice Chairman of the Board, The  
Equitable Life Assurance Society  
of the United States.

Joseph A. Pechman,  
Director, Economic Studies Program,  
Brookings Institution.

John Wilson Porter,  
President, Eastern Michigan University.

Bert Seidman,  
Director, Department of Social Security,  
American Federation of Labor and  
Congress of Industrial Organizations.

J.W. Van Gorkom,  
Chairman of the Board, Trans Union Corp.

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two funds. Nevertheless, if the total remains adequate but the allocation later needs to be modified, Congress must now legislate the reallocation.

The council believes that this procedure is cumbersome and can cause needless public worry about the financial integrity of the social security system. In 1977, for example, projections of the imminent exhaustion of the disability insurance fund contributed to a greater public concern about the solvency of social security than was warranted and than would have arisen if the OASI and DI funds had been combined. On the other hand, disability program experience since 1977 has proven more favorable than anticipated. Indeed, projections under the most pessimistic of the three sets of assumptions in the 1979 trustees' report show

that it might be necessary to reallocate income from the DI trust fund to the OASI fund in the early 1980's. The council's recommendation would obviate the need for such a reallocation and would prevent scare headlines and needless public concern.

The council believes, however, that separate cost analysis for OASI and DI should continue. Information from such estimates would warn policy makers and the public of potential adverse developments in either part of the program.

Finally, a majority of the council recommends that, if Congress in the future provides for other scheduled general revenue payments to social security, such payments should be timed to avoid raising payroll taxes during a recession.