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Will Social Security Be There When I Retire?

Social Security's future solvency has become one of the most commonly-discussed issues in retirement planning—and for good reason. Gallup polls show that an estimated 57% of retirees rely on Social Security as a major source of retirement income—a number that has held steady since the early 2000s. But when Generation X and Y individuals plan for their future retirement, they'll often ask their advisor to assume that Social Security won't be there for them 20 or 30 years down the road.

However, if you look closely at the numbers, you see a very different story. Up until 2011, the Social Security system actually collected more revenues from workers' FICA payments than it paid out—and that has been generally true since the 1940s. Most of the Social Security benefits that people receive today are simply a transfer; that is, the money is collected from worker paychecks (and, of course, employer matches), spends a few days at the U.S. Treasury and then is paid out to recipients. The surplus has been used to pay government operating expenses, and for seven decades, the government issued "special issue federal securities" (essentially fancy IOUs that pay interest) to the Social Security trust fund.

In 2011, the program crossed that threshold where benefit payments slightly exceeded the amount collected. Why? Because the number of beneficiaries, compared to the number of workers, has steadily increased. In 1955, there were more than eight workers paying into Social Security for every beneficiary. Today, that number is closer to three workers for every beneficiary, and by 2031, if current estimates are correct, that ratio will fall to just over two workers supporting every retired beneficiary.

When Social Security Administration actuaries crunch the numbers, they have to take into account the shifting demographics, and then make estimates of fertility and immigration rates, longevity, labor force participation rates, the growth of real wages and growth of the economy every year between now and 2078. After adding in the value of the government IOUs, they estimate that if nothing is done to fix the system, the trust fund IOUs will run out in the year 2033. At that time, only the FICA money collected from workers would be available to pay Social Security beneficiaries. In real terms, that means the beneficiaries would, in 2034, see their payments drop to 77% of what they were promised.

In other words, the money being transferred from current workers to beneficiaries through the FICA payroll program, assuming no course corrections between now and 2033, will be enough to pay retirees 77% of the benefits they were otherwise expecting.

The government actuaries say that if nothing is done to fix the problem over the next 63 years, this percentage will gradually decline to 72% by the year 2078.

So the first takeaway from these analyses is that today's workers are looking at a worst-case scenario of only receiving about 75% of the benefits that they would otherwise have expected to receive. This is far different from the zero figure that they're asking their advisors to use in retirement projections.

How likely is it that there will be no course corrections? There are two possible ways that this 75% figure could go up. One lies in the assumptions themselves. The Social Security Administration actuaries have tended to err on the side of conservatism, presumably because they would rather be pleasantly surprised than discover that they were too optimistic. But what if the future doesn't look as gloomy as their assumptions make it out to be?

To take just one of the variables, the actuaries are projecting that labor force participation rates for men will fall from 75.5% of the population in 1997 to 74% by 2075, while the growth in female workers will stop their long climb and peter out around 60%. If male labor force participation rates don't fall, and if female rates continue to rise, some of the funding gap will be eliminated.

Similarly, the projections assume the U.S. economy's productivity gains (which drive wage increases) will grow 1.3% a year, well below long-term U.S. averages and certainly below the assumptions of economists who believe that biotech and information age revolutions will spur unprecedented growth. If real wages were to grow at something closer to the post-Great Recession rate of 2% a year, then more than half of the funding gap would be eliminated. If the current slump in immigration (due to tighter immigration policies) is reversed, and the economy grows faster than the anemic 2% rates the Social Security Administration is projecting (compared to 2.5% recently), then the "bankrupt" system begins to look surprisingly solvent.

A second possibility is that Congress will tweak the numbers and bring Social Security's long-term finances back in balance, as it has done 21 times since the program originated in 1937. The financial press often cites the fact that the total future Social Security funding shortfall amounts to $13.6 trillion, but they seldom add that this represents just 3.5% of future taxable payrolls through 2081. Small tweaks—like extending the age to collect full retirement benefits from 67 to 68, raising the FICA tax rate by 3.5 percentage points or making the current 12.4% rate (employee plus employer match) apply to all taxable income rather than the $118,500 current limit—would restore solvency far enough into the future that today's workers would be comfortable adding back 100% of their anticipated benefits into their retirement projections.

How likely is it that Congress will take these measures, in light of recent partisan budget battles? It's helpful to remember that older Americans tend to vote with more consistency than younger citizens. The more you've paid into the system, the more you expect to at least get back the money you were promised.

The bottom line here is that if you're skeptical about Social Security's future solvency, then you should pencil in 75% of the benefits you would otherwise expect—rather than $0. Meanwhile, as you approach the age when you're eligible for benefits, watch for signs that immigration restrictions are loosening, the economy is growing faster than the SSA actuaries' gloomy projections, that more people are working during traditional retirement years or yet another round of tweaks from our elected representatives.