



CONGRESSIONAL BUDGET OFFICE
U.S. Congress
Washington, DC 20515

April 5, 2006

Honorable Robert F. Bennett
Vice Chairman
Joint Economic Committee
U.S. Senate
Washington, DC 20515

Dear Vice Chairman Bennett:

As requested in your letter of April 3, the Congressional Budget Office (CBO) has analyzed the long-term effects of S. 2427, the Sustainable Solvency First for Social Security Act of 2006. The proposal would reduce scheduled Social Security benefits, primarily by adjusting the benefit formula but also by accelerating the increase in the normal retirement age.

The bill would generally result in improved federal budget balances and, CBO projects, in positive and large trust fund balances throughout the next century.

Under current law, the trust funds will become exhausted in 2052, CBO estimates, at which point annual benefits would be limited to annual revenues. Total benefits received by participants under S. 2427 would be lower than under current law from 2012 until 2052. The reductions would be largest for the highest earners and smallest for the lowest earners.

After 2052, total benefits under the proposal would be similar to those that would be paid under current law. Under the proposal, automatic transfers from the general fund would be made when necessary to ensure that the Social Security trust funds remained solvent, but CBO projects that no transfers would be necessary.

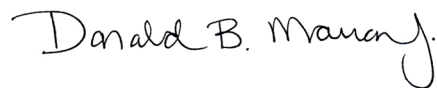
This analysis examines Social Security revenues and outlays on the basis of current law, meaning that outlays are limited to current revenues in years after trust fund exhaustion. The appendix contains a similar analysis based on scheduled benefits, which incorporates the assumption that those benefits are paid in full even after the trust funds are exhausted.

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The analysis does not reflect any considerations of the potential effects on the macroeconomy that might occur under the proposal. CBO has not produced a 10-year cost estimate.

The underlying data for the figures in this analysis are available on CBO's Web site (www.cbo.gov). If you would like any additional information on these analyses, we will be pleased to provide it. The CBO staff contact for the analysis is Noah Meyerson, who can be reached at 202-225-2592.

Sincerely,



Donald B. Marron
Acting Director

Enclosure

cc: Honorable Jim Saxton
Chairman
Joint Economic Committee
U.S. House of Representatives

Honorable Jack Reed
Ranking Democratic Member
Joint Economic Committee
U.S. Senate

Honorable William "Bill" M. Thomas
Chairman
Committee on Ways and Means
U.S. House of Representatives

Honorable Charles B. Rangel
Ranking Democratic Member
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Honorable Judd Gregg
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Honorable Kent Conrad
Ranking Democratic Member
Committee on the Budget
U.S. Senate

Long-Term Analysis of S. 2427,
the Sustainable Solvency First for
Social Security Act of 2006

April 5, 2006

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Overview

The Congressional Budget Office (CBO) has analyzed S. 2427, the Sustainable Solvency First for Social Security Act of 2006 introduced by Senator Bennett. The proposal would reduce scheduled Social Security benefits, primarily by adjusting the benefit formula but also by accelerating the increase in the normal retirement age. The benefit reductions would be linked, in part, to growth in life expectancy. The reductions would be greater for beneficiaries with higher earnings. The proposal also requires transfers from the general fund of the Treasury to the Social Security trust funds in the event that the balance of the trust funds falls below 100 percent of annual trust fund outlays.

The proposed benefit reductions would generally result in improved federal budget balances.

Total benefits received by participants would be lower than under current law from 2012 until 2052. The reductions would be largest for the highest earners and smallest for the lowest earners.

Under current law, the trust funds will become exhausted in 2052, CBO projects, at which point annual benefits would be limited to annual revenues. After that year, total benefits under the proposal would be similar to those that would be paid under current law. Under the proposal, automatic transfers from the general fund would be made when necessary to ensure that the Social Security trust funds remained solvent; however, CBO projects that transfers are unlikely to be necessary.

This analysis examines Social Security revenues and outlays on the basis of current law, meaning that outlays are limited to current revenues in years after trust fund exhaustion. The appendix contains a similar analysis based on scheduled benefits, which incorporates the assumption that those benefits are paid in full even after trust fund exhaustion.

The analysis is based on CBO's understanding of the bill's language and the sponsor's legislative intent. CBO made its projections using the 2004 Social Security trustees' demographic assumptions and CBO's January 2005 economic assumptions. The analysis does not reflect any considerations of the potential effects on the macroeconomy that might occur under the proposal. CBO has not produced a 10-year cost estimate.

Detailed Description of S. 2427

Decreases to Retirement Benefits

Progressive Price Indexing: Under current law, average scheduled benefits for newly entitled Social Security beneficiaries grow with average economywide earnings. Some proposals would link benefits to price levels rather than to earnings levels, so that average benefits would grow at the same rate as prices.¹ S.2427 would implement progressive price indexing, under which benefits for the highest-earning beneficiaries would grow with prices, benefits for the lowest earners would continue to grow with average earnings, and benefits for other groups would grow at a weighted average of those two rates.

Specifically, starting in 2012, initial benefits for a maximum earner (one who earned the taxable maximum for at least 35 years) would begin to be indexed to growth in the consumer price index for urban wage earners and clerical workers (CPI-W). The current benefit formula has three replacement factors: 90 percent, 32 percent, and 15 percent. The two dollar levels at which the rates change are called bend points. Under the proposal, a third bend point would be created at the 30th percentile of career-average earnings for new retired beneficiaries. (The level would be computed using data from workers who became eligible for benefits in calendar years 2001 through 2003.) CBO estimates that the new bend point will be equal to about 230 percent of the first bend point or about a quarter of the highest bend point. The two replacement factors below the new bend point, currently 90 percent and 32 percent, would be unaffected by this provision. The two replacement factors above the new bend point would fall annually by an amount sufficient to ensure price indexing for the highest-earning beneficiaries. CBO projects that the top two replacement factors will fall to zero after 2076. Thereafter, scheduled benefits would grow with earnings for all newly retired beneficiaries.²

Longevity Indexing: The longevity indexing provision would reduce the replacement factors to reflect changes in life expectancy at age 67.³ Beginning in 2018, the provision would multiply the factors by a ratio that captures the increase in life expectancy at age 67. Specifically, for a cohort becoming eligible for benefits in 2018 and later, the ratio

¹See Congressional Budget Office, “Long-Term Analysis of Plan 2 of the President’s Commission to Strengthen Social Security” (July 21, 2004; updated September 30, 2004).

²Under both current law and the proposal, a cost-of-living-adjustment, based on growth in the CPI-W, is applied to benefits each year after initial eligibility.

³A similar provision was included in H.R. 3821 during the 108th Congress. See Congressional Budget Office, “Long-Term Analysis of H.R. 3821, the Bipartisan Retirement Security Act of 2004” (July 21, 2004).

**Replacement Factors Under S. 2427
(Including Effects of Progressive Price Indexing and Longevity Indexing)**

	Bracket				Percentage of Current-Law Values			
	1st	2nd	3rd	4th	1st	2nd	3rd	4th
2010	0.9000	—	0.3200	0.1500	100.0	—	100.0	100.0
2020	0.8909	0.3168	0.2528	0.1185	99.0	99.0	79.0	79.0
2030	0.8615	0.3063	0.1937	0.0908	95.7	95.7	60.5	60.5
2040	0.8347	0.2968	0.1385	0.0649	92.7	92.8	43.3	43.3
2050	0.8103	0.2881	0.0903	0.0423	90.0	90.0	28.2	28.2
2060	0.7880	0.2802	0.0503	0.0236	87.6	87.6	15.7	15.7
2070	0.7679	0.2730	0.0178	0.0083	85.3	85.3	5.6	5.5
2080	0.7498	0.2666	0	0	83.3	83.3	0	0
2090	0.7328	0.2605	0	0	81.4	81.4	0	0
2100	0.7164	0.2547	0	0	79.6	79.6	0	0
2110	0.7006	0.2491	0	0	77.8	77.8	0	0

Notes: The second bracket is created in 2012.
Replacement factors for the third and fourth brackets are zero after 2076.

would equal the 2013 period life expectancy at age 67 divided by the period life expectancy at age 67 for the year four years previous to the year the cohort became eligible for retirement benefits. By 2100, that provision alone would result in a 20 percent reduction in replacement factors.

Retirement Age: Under current law, the normal retirement age rose to 66 for people who turned 62 in 2005. After 12 years, it will again climb in two-month steps for six years, reaching 67 for people who turn 62 in 2022 or later. The proposal would shorten the 12-year hiatus by five years. The increase of two months per birth year would start with the 1950 birth cohort, and the normal retirement age would reach age 67 for the 1955 cohort.

Conversion to Old-Age Benefits: Disability benefits would not be affected by the proposal. However, as under current law, once a disabled-worker beneficiary reached the normal retirement age, he or she would receive retirement benefits. Under current law, benefits do not change when a disabled-worker beneficiary reaches the normal retirement age, but under the proposal, they would fall. The reductions to retirement benefits for workers who were entitled to disability benefits at some point in their lives would be linked to the number of years, between ages 22 and the earliest eligibility age, that they were disabled. (Those reductions would include the effects of both the progressive price indexing and the longevity indexing provisions.) For example, a worker who was entitled to disability benefits at age 25 would receive retirement benefits that were only slightly

lower than current-law benefits. In contrast, someone who became disabled at age 60 would be subject to nearly all of the retiree benefit reductions specified under the proposal when they reached the normal retirement age.

Revenues

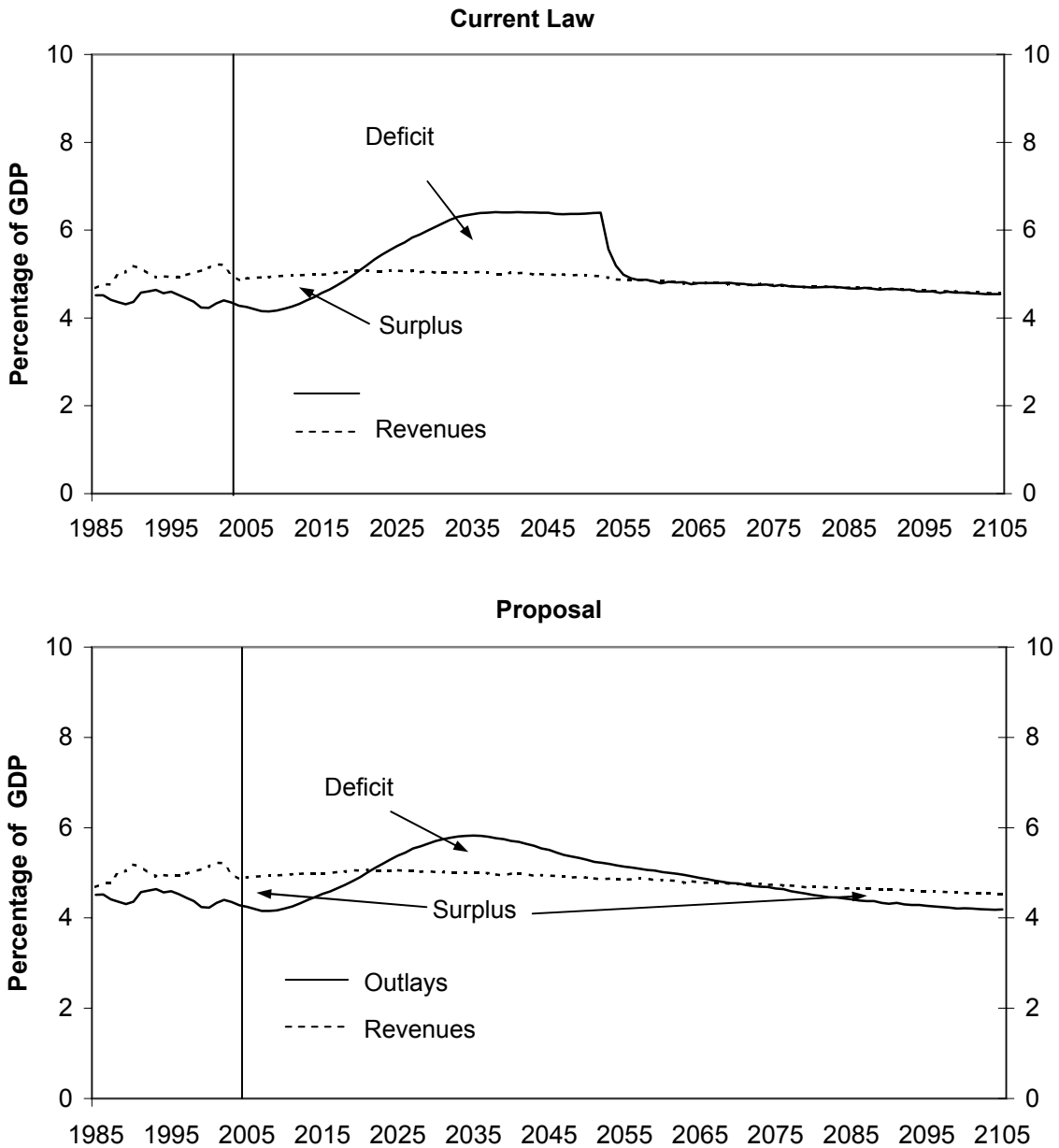
In any year in which the trust fund ratio (the ratio of the trust fund balance to annual outlays) falls below 1, the amount necessary to increase the trust fund ratio to 1 would be transferred to the trust funds from the general fund of the Treasury.

Figure 1: Effect on Social Security Finances

Figure 1 displays Social Security outlays and revenues as a share of gross domestic product (GDP). Revenues include payroll taxes and income taxes on benefits, but they exclude interest credited to the Social Security trust funds and any intragovernmental transfers. Outlays include Social Security benefits and administrative costs charged to the trust funds.

- Under current law, outlays are projected to exceed revenues beginning in 2020 and to exceed the sum of revenues and interest credited to the Social Security trust funds beginning in 2033. The trust funds would be exhausted in 2052; thereafter, outlays in each year would be limited to current revenues.
- Under the proposal, outlays would generally be lower than under current law but are still projected to exceed revenues from 2022 through 2070. Thereafter, outlays would fall below revenues. The proposal specifies that if the trust fund ratio falls below 1, transfers are to be made from the Treasury to the trust funds. However, CBO projects that the trust ratio will remain above 1.

Figure 1.
Social Security Revenues and Outlays as a Share of GDP Under
Current Law and S. 2427, 1985 to 2105



Source: Congressional Budget Office.
 Note: GDP = gross domestic product.

Figure 2: Net Effect on the Federal Budget

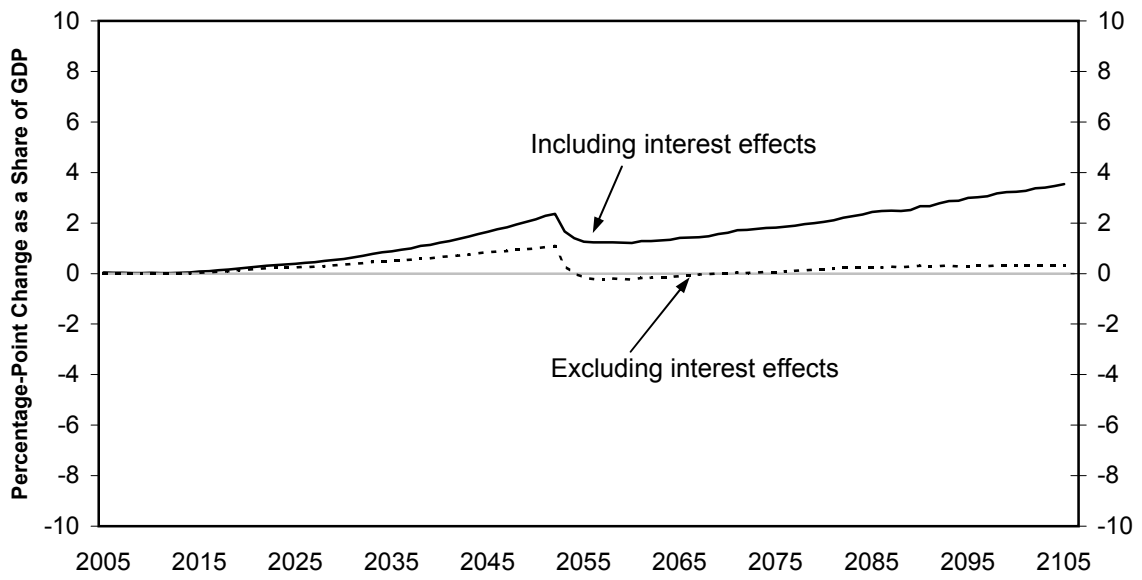
The effects on total federal budget balances as a share of GDP are illustrated in Figure 2. Negative numbers mean the proposal would increase the deficit (or reduce the surplus). Positive numbers indicate that the proposal would reduce the deficit (or increase the surplus).

The dotted line shows the effect of the proposal on the primary budget balance—the balance excluding interest effects. The solid line includes interest effects.

- For most of the projection period, the proposal would result in smaller primary deficits, because it would reduce Social Security benefits beginning in 2012.
- Under current law, benefits grow relative to GDP until trust fund exhaustion, projected to occur in 2052, when they fall sharply. Under the proposal, in contrast, outlays would increase relative to GDP until about 2035, but their rate of growth would be lower than under current law. Thereafter, outlays would decline gradually as a share of GDP. As a result, the primary budget balance would be higher under the proposal than under current law from 2012 until 2052, then lower until 2068, and higher thereafter.
- The proposal would result in lower public debt and would thus reduce interest outlays beginning in 2012. The budget balance including interest effects would be improved in every year after 2012. By the end of the projection period, interest outlays would be more than 3 percent of GDP lower than under current law.

Figure 2.

Effects of S. 2427 on Total Annual Budget Balances as a Share of GDP Relative to Current Law, 2005 to 2105



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table 1: Effect on Social Security Finances for Specific Years and Provisions

The top panel of Table 1 shows snapshot measures of Social Security finances under current law at 20-year intervals. Following trust fund exhaustion, benefits are automatically reduced so that annual outlays equal annual revenues. The fourth line shows the size of the automatic benefit reduction.

- Under current law, automatic benefit reductions begin in 2053 (as shown in Figure 1). By 2065, automatic benefit reductions total 1.68 percent of GDP; by 2105, they amount to 2.15 percent of GDP.

The middle panel shows the effects of the proposal's individual provisions on Social Security finances.

- Shortening the normal retirement age hiatus is effectively equivalent to a reduction in benefits for retired workers born from 1950 through 1959, so that provision would initially improve the annual balance. It would have no effect on the annual balance in later years, when affected workers would have died.
- Longevity indexing benefits would improve the annual balance. That effect would grow over time as life expectancy increased.
- Progressive price indexing would have the largest effect on the annual balance. The savings from that provision would begin in 2012 and grow over the projection period as the replacement factors were reduced.

The third panel shows measures of Social Security finances under the proposal.

- Under the proposal, there would be no automatic benefit reductions, CBO projects. By 2085, the primary surplus would equal 0.25 percent of GDP, and by 2105, it would increase to 0.35 percent of GDP.

Table 1.**Social Security Finances Under Current Law and S. 2427
as a Share of GDP, 2005 to 2105**

(percent)

	2005	2025	2045	2065	2085	2105
Social Security Finances Under Current Law						
Revenues ^a	4.90	5.07	4.99	4.78	4.70	4.57
Outlays ^b	4.25	5.64	6.39	4.78	4.70	4.57
Balance ^c	0.65	-0.57	-1.40	0.00	0.00	0.00
Automatic Benefit Reduction ^d	0.00	0.00	0.00	1.68	1.91	2.15
Effects on Balance Plus Automatic Benefit Reduction under Proposed Provisions						
Shorten NRA Hiatus by Five years	0.00	0.06	0.01	0.00	0.00	0.00
Longevity Index Benefits	0.00	0.03	0.22	0.47	0.71	0.93
Progressive Indexing Holding 30 Percent Harmless	0.00	0.18	0.68	1.25	1.74	1.95
Interactions Among Provisions	0.00	-0.01	-0.09	-0.14	-0.29	-0.38
Total Effects, All Provisions	0.00	0.25	0.83	1.57	2.16	2.50
Social Security Finances Under Proposal						
Revenues ^a	4.90	5.06	4.94	4.78	4.66	4.53
Outlays ^b	4.25	5.38	5.51	4.88	4.41	4.19
Balance ^c	0.65	-0.32	-0.57	-0.11	0.25	0.35
Transfers from Rest of Government	0.00	0.00	0.00	0.00	0.00	0.00
Automatic Benefit Reduction ^u	0.00	0.00	0.00	0.00	0.00	0.00

Source: Congressional Budget Office.

Note: GDP = gross domestic product; NRA = normal retirement age.

- Revenues equal payroll taxes and income taxes on benefits (but not interest credited to the trust funds or intragovernmental transfers) in the specified year.
- Outlays equal Social Security benefits plus administrative costs.
- The balance is the difference between revenues and outlays; it may not equal the difference of the previous two rows because of rounding.
- Automatic benefit reductions are equal to the difference between scheduled outlays and scheduled revenues in years after trust fund exhaustion.

Figure 3: Trust Fund Ratio

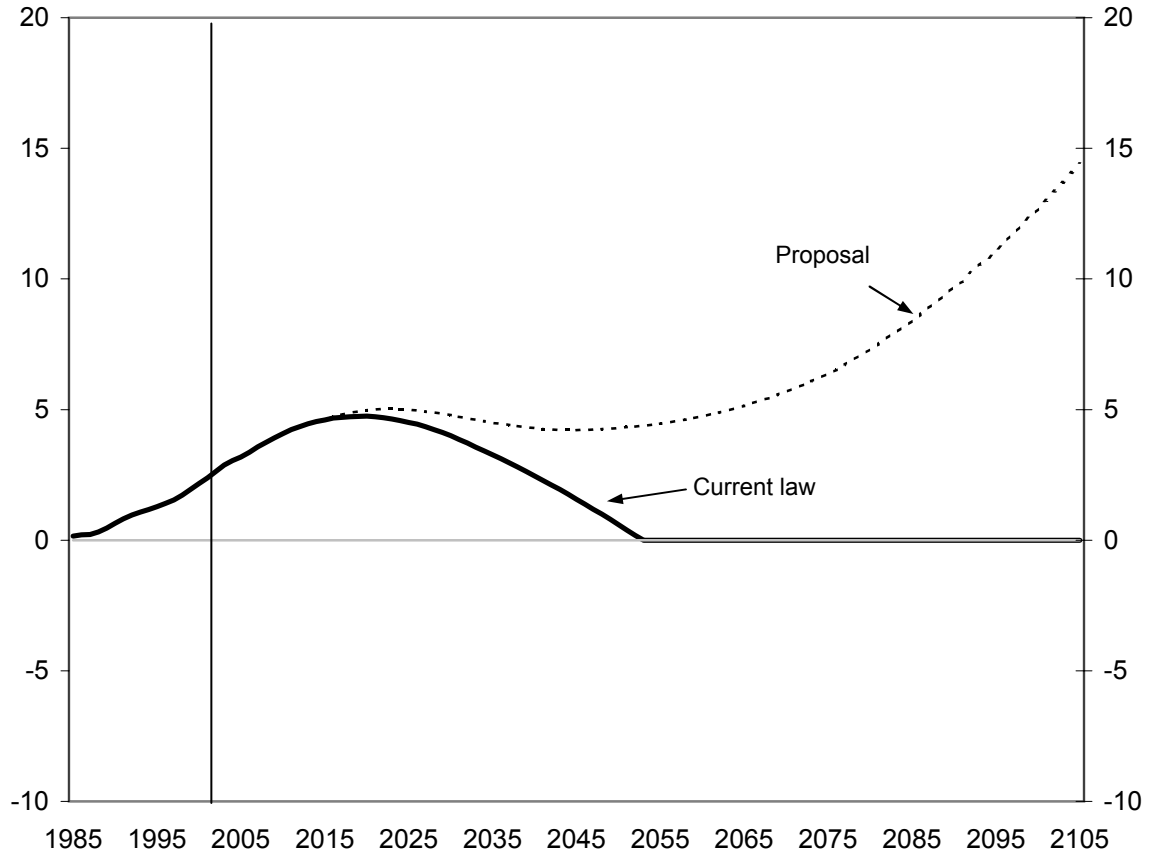
The trust fund ratio—a measure of the adequacy of the trust funds—is the ratio of the total trust fund balance at the beginning of the calendar year to total Social Security outlays during that year. After the trust funds are exhausted, outlays are limited to Social Security revenues, holding the ratio at zero.

All trust fund assets are included, regardless of their source. For example, an intragovernmental transfer to the trust funds would increase the trust fund ratio but would have no direct effect on the total federal budget. However, CBO projects that no intragovernmental transfers will occur under the proposal.

- The reduced benefits under the proposal would result in a larger trust fund balance than under current law beginning in 2013. Under the proposal, the ratio would rise above 5 in 2021, decline slightly to 4.2 in 2045, and then grow steadily. By 2105, the trust fund ratio would be more than 14.

Figure 3.

Social Security Trust Fund Ratios Under Current Law and S. 2427, 1985 to 2105



Source: Congressional Budget Office.

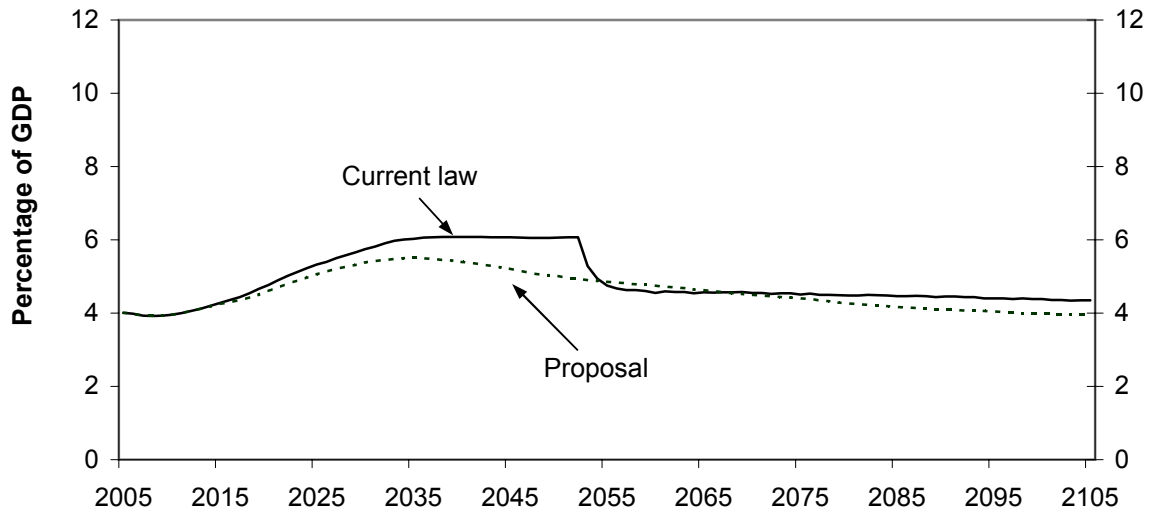
Figure 4: Total Social Security Benefits

Figure 4 shows Social Security benefits received by beneficiaries.

- From 2012 through 2052, Social Security benefits would be lower under the proposal than under current law because of the proposed benefit reductions.
- Under current law, benefits would be automatically reduced upon trust fund exhaustion; from 2053 through 2067, total benefits would be slightly higher under the proposal. After 2067, benefits would again be lower under the proposal as progressive and longevity indexing further reduced benefits relative to those under current law.

Figure 4.

Social Security Benefits as a Share of GDP Under Current Law and S. 2427, 2005 to 2105



Source: Congressional Budget Office.

Note: GDP = gross domestic product.

Table 2: First-Year Retirement Benefits

Table 2 shows first-year benefits (net of income taxes paid on benefits and credited to the Social Security trust funds) for the median retired worker in three lifetime earnings quintiles. This table shows results only for retired workers. For example, the effects of changes to widow(er) or disabled-worker benefits are not shown.

For ease of comparison, benefits are computed assuming all workers claim retirement benefits at age 65, even though most workers claim at earlier ages. First-year annual benefits are computed, on the basis only of earnings through age 61, for all workers who under current law are eligible to claim Old-Age Insurance benefits at age 62 and who have not yet claimed any other benefit. Benefits are adjusted to put them into 2004 dollars.

- The proposal would not affect workers born before 1950.
- Most beneficiaries born in the 1950s and later would receive average benefits that are lower under the proposal than under current law. Reductions for workers in the lowest household earnings quintile would be smaller than those for workers in the middle and upper earnings quintiles. That occurs because although workers at all earnings levels would be affected by the acceleration in the increase in the normal retirement age and longevity indexing, the progressive indexing would result in larger reductions for higher earners and would not affect the bottom 30 percent of the earnings distribution.
- Workers who are both in the lowest earnings quintile and in the 1990s and 2000s birth cohorts would receive higher benefits under the proposal than under current law. For that group, the reductions in scheduled benefits under the proposal would be smaller than the reduction in benefits that would occur under current law after trust fund exhaustion.
- For workers born after 1950 in the middle and highest earnings quintiles, benefits under the proposal would be smaller than benefits under current law, even after taking into account the automatic benefit reductions that would occur upon trust fund exhaustion.
- As shown in the final column, CBO projects that no intragovernmental transfers would be required under the proposal.

Table 2.

First-Year Total Annual Benefits Under Current Law and S. 2427 for the Median Retired Worker If Benefits Are Claimed at Age 65, by Birth Cohort and Lifetime Earnings Level

(2004 dollars)

10-Year Birth Cohort Starting in Year	Current-Law	Proposed	Percentage of
	Social Security Benefits	Social Security Benefits	Benefits Financed with Intragovernmental Transfers
Median in Lowest Household Lifetime Earnings Quintile			
1940	7,500	7,500	0.0
1950	8,300	8,000	0.0
1960	9,000	8,800	0.0
1970	9,800	9,200	0.0
1980	10,200	9,800	0.0
1990	9,300	10,800	0.0
2000	10,000	11,700	0.0
Median in Middle Household Lifetime Earnings Quintile			
1940	15,500	15,500	0.0
1950	15,800	14,500	0.0
1960	16,200	14,300	0.0
1970	18,600	14,800	0.0
1980	20,500	15,400	0.0
1990	18,300	15,900	0.0
2000	20,000	16,700	0.0
Median in Highest Household Lifetime Earnings Quintile			
1940	20,200	20,200	0.0
1950	22,200	19,900	0.0
1960	23,300	19,000	0.0
1970	26,200	18,600	0.0
1980	29,200	18,300	0.0
1990	26,200	17,900	0.0
2000	28,800	17,700	0.0

Source: Congressional Budget Office.

Figure 5: Ratio of Benefits Received to Taxes Paid Over a Lifetime

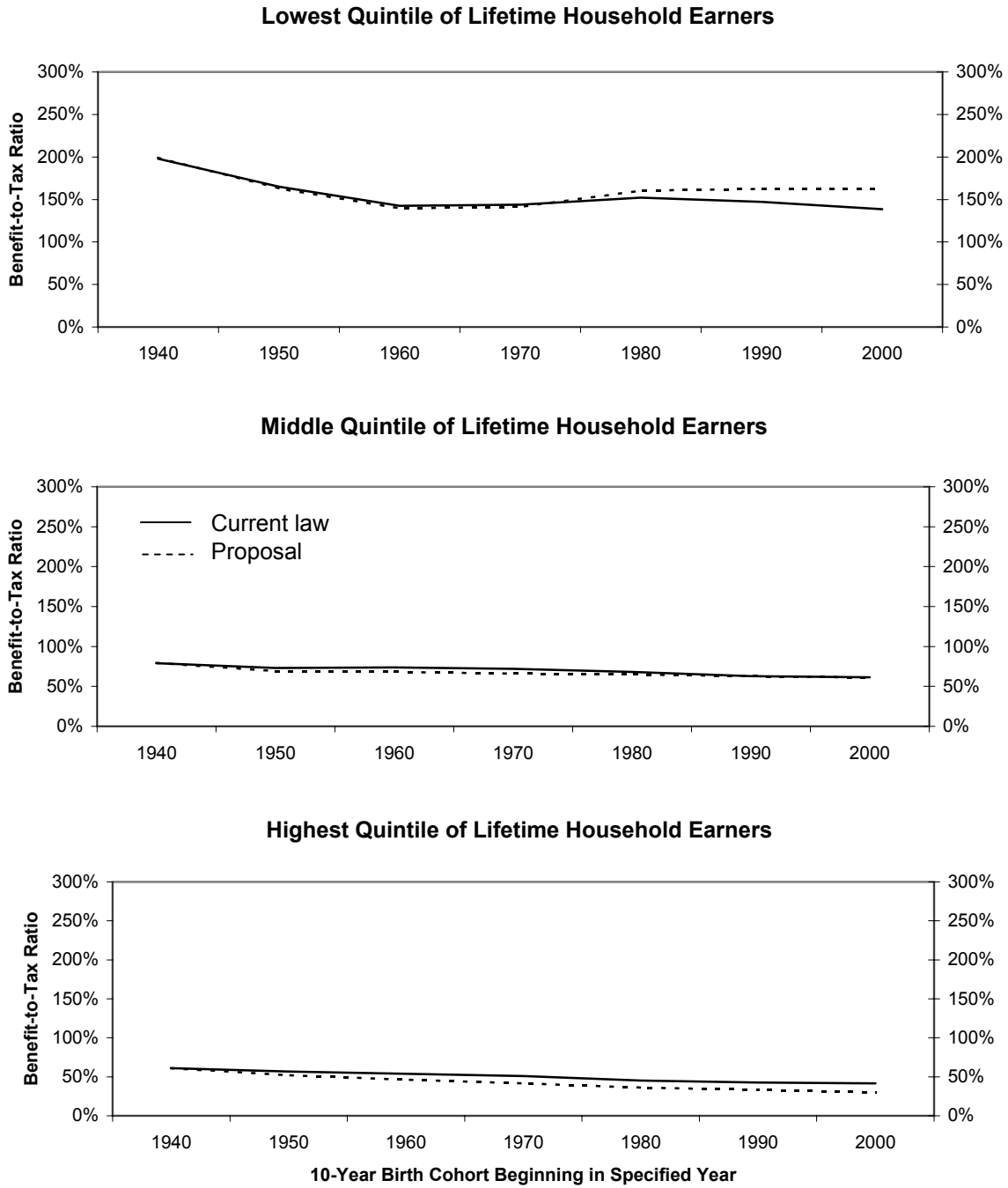
Figure 5 compares the present value of total Social Security benefits received (from both Old-Age and Survivors Insurance and Disability Insurance, net of income taxes paid on benefits) with the present value of total payroll taxes paid (by both employers and employees) over a lifetime for all individuals who live to at least age 45.

- The benefit-to-tax ratio for cohorts shown in Figure 5 will average less than 100 percent. The ratio exceeds 100 percent for the lowest earnings quintile mainly because of that group's high disability benefit receipt rates.
- The proposal would have little effect on the benefit-to-tax ratio for the earlier cohorts in the lowest earnings quintile. The proposal would raise the benefit-to-tax ratio above current-law levels for the 1980s and later cohorts in that earnings group because the proposal would reduce benefits by less than the current-law reductions after trust fund exhaustion.
- The proposal would lower the ratio for the middle quintile of earners born in the 1950s through the 1970s. The ratio would be about the same as under current law for the 1980s and later cohorts.
- The highest earnings quintile would have a lower benefit-to-tax ratio under the proposal beginning with the 1950s cohort. That group would be most affected by progressive indexing.

	Benefit-to-Tax Ratios			
	<u>1950s Cohort</u>		<u>1990s Cohort</u>	
	<u>Current Law</u>	<u>Proposal</u>	<u>Current Law</u>	<u>Proposal</u>
Lowest Earnings Quintile	165 %	163 %	147 %	162 %
Middle Earnings Quintile	73 %	69 %	63 %	63 %
Highest Earnings Quintile	57 %	52 %	43 %	33 %

Figure 5.

Ratio of Lifetime Dedicated-Tax-Financed Benefits to Lifetime Taxes Under Current Law and S. 2427, by Birth Cohort and Lifetime Earnings Level



Uncertainty Analysis

The preceding analysis presents estimates generated through a simulation in which demographic and economic assumptions are set at their most likely values.

The following section contains range estimates that are based on 500 stochastic simulations. Those simulations are based on a probability distribution of possible future outcomes for the various demographic and economic inputs used in the projections. The distribution of each assumption is centered at its most likely value, but the variation around those values is based on historical experience.

In its results, CBO gives its estimates of the 80 percent range of uncertainty in figures and the 10th and 90th percentiles in tables. There is an 80 percent chance that the actual outcome will fall in the displayed range, a 10 percent chance that it will be higher, and a 10 percent chance that it will be lower. Likewise, there is a 10 percent chance that the outcome will be below the 10th percentile and a 10 percent chance that the outcome will be above the 90th percentile.

In some cases, CBO presents the median—or middle—of the range of outcomes in the uncertainty analysis. Those median values and the results in the first section both indicate “typical” results; however, the median results may differ somewhat from the single-simulation results presented earlier.

Figure U1: Effect on Social Security Finances

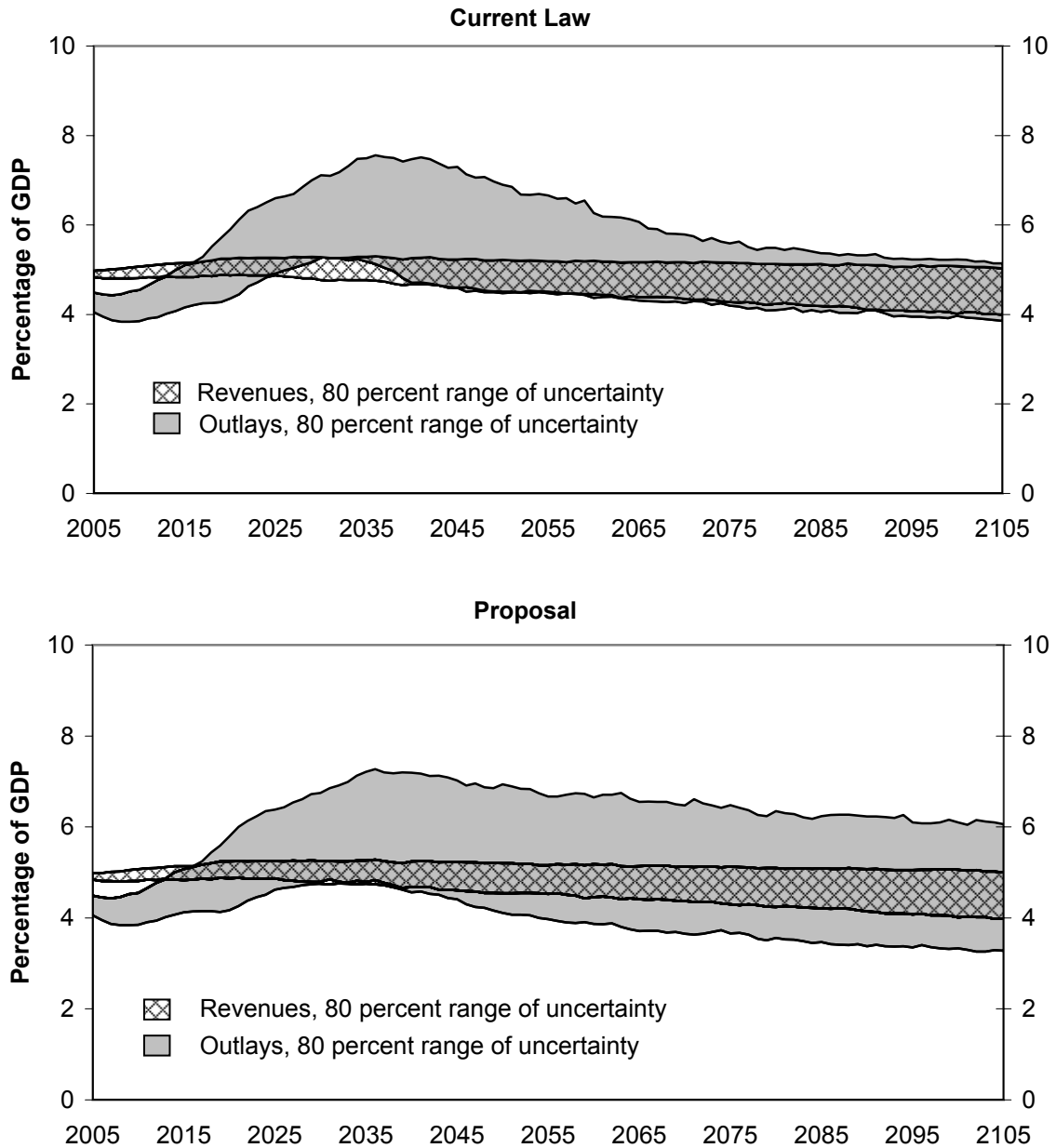
The uncertainty about Social Security revenues as a share of GDP results primarily from uncertainty about the level of taxable earnings as a share of GDP. For example, if a larger-than-expected share of compensation is paid in the form of health benefits, then taxable earnings—and thus Social Security revenues—will be a smaller-than-expected share of GDP.

- Under current law, it is very likely that the trust funds will become exhausted within the 100-year projection period. After exhaustion, annual outlays will be limited to revenues in that year, and the uncertainty about outlays will be approximately equal to the uncertainty about revenues.

Uncertainty about outlays in the years before trust fund exhaustion is driven by uncertainty about future economic and demographic conditions, such as productivity growth and fertility. (For more information, see Congressional Budget Office, *Quantifying Uncertainty in the Analysis of Long-Term Social Security Projections*, November 2005.)

- As shown in the figure, outlays could be lower than revenues under the proposal.
- Under the proposal, the trust funds would remain solvent throughout the projection period because intragovernmental transfers would be made to them if the trust fund ratio fell below 1. As a result, scheduled outlays could be paid even if they were higher than revenues.

Figure U1.
Potential Range of Social Security Revenues and Outlays as
a Share of GDP Under Current Law and S. 2427, 2005 to 2105



Source: Congressional Budget Office.
 Note: GDP = gross domestic product.

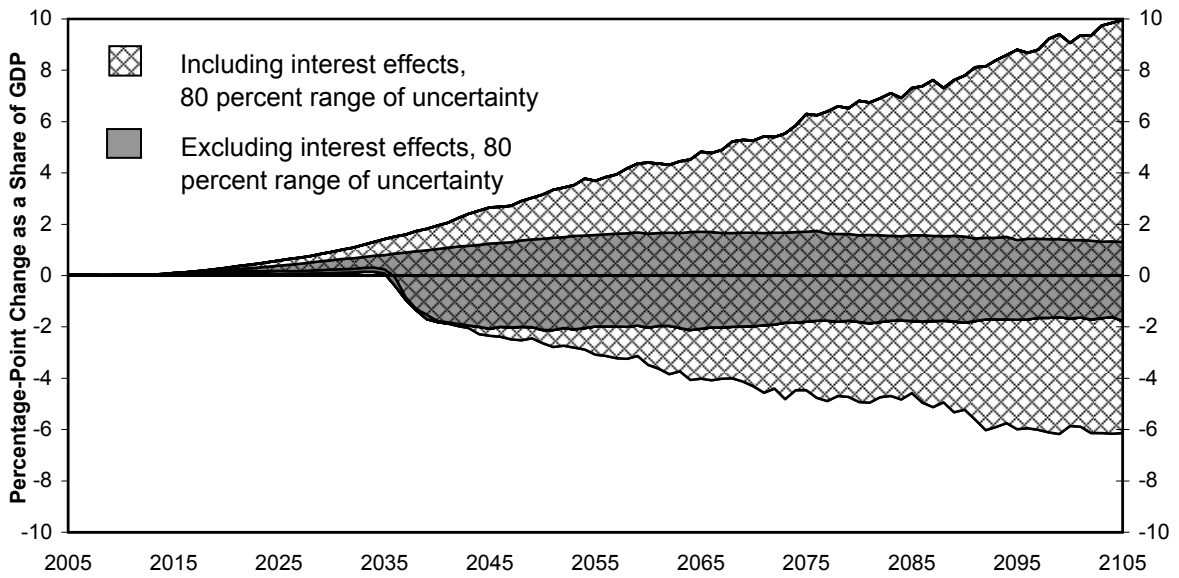
Figure U2: Net Effect on the Federal Budget

Recall that negative numbers mean that the proposal would increase the deficit (or reduce the surplus). Positive numbers indicate that it would reduce the deficit (or increase the surplus).

- As shown in Figure U1, uncertainty about outlays under current law declines over time because after trust fund exhaustion, annual outlays will be limited to revenues in that year. Uncertainty about outlays under the proposal would be larger and would always be equal to uncertainty about scheduled outlays.
- As a result, from 2007 to around 2035, there is little uncertainty about the proposal's effects on future budget balances relative to current law. After 2035, there is a 10 percent chance that the trust funds would become exhausted under current law, and so the uncertainty increases.
- In later years, the differences relative to current law would be larger, so there would be greater uncertainty about the proposal's effects on budget balances.

Figure U2.

Potential Range of Effects of S. 2427 on Total Annual Budget Balances as a Share of GDP Relative to Current Law, 2005 to 2105



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table U1: Effect on Social Security Finances for Specific Years

The top three lines show the 10th, 50th, and 90th percentiles of Social Security annual balances under current law at 20-year intervals. Following trust fund exhaustion, benefits will automatically be reduced to reach a balance of zero. The next three lines show the size of possible automatic benefit reductions.

- Under current law, the range for the balance includes nonzero numbers in every year because there is some probability that the trust funds will not be exhausted, allowing the system to run a deficit. There is also some probability that the system will run a surplus in any given year.

The bottom section of the table shows the same information under the proposal.

- Under the proposal, transfers would be made to the trust funds in the event that the trust fund ratio fell below 1, so there would never be any automatic benefit reductions. The median transfer in every year is zero, but transfers do occur at the 10th percentile of the distribution.

Table U1.**Potential Range of Social Security Finances Under Current Law and S. 2427 as a Share of GDP, 2005 to 2105**

(percent)	2005	2025	2045	2065	2085	2105
Balance Under Current Law^a						
10th Percentile	0.45	-1.52	-2.29	-1.18	-0.37	-0.20
Median - 50th Percentile	0.64	-0.66	-0.65	0.00	0.00	0.00
90th Percentile	0.80	0.00	0.13	0.21	0.25	0.25
Automatic Benefit Reductions Under Current Law^b						
10th Percentile	0.00	0.00	2.57	3.80	4.38	5.07
Median - 50th Percentile	0.00	0.00	0.00	1.60	1.99	2.36
90th Percentile	0.00	0.00	0.00	0.00	0.00	0.51
Balance Under Proposal^a						
10th Percentile	0.45	-1.34	-2.16	-2.00	-1.67	-1.55
Median - 50th Percentile	0.64	-0.41	-0.74	-0.16	0.02	0.12
90th Percentile	0.80	0.31	0.42	1.00	1.14	1.21
Transfers from Rest of Government Under Proposal						
10th Percentile	0.00	0.00	1.63	1.44	0.92	0.43
Median - 50th Percentile	0.00	0.00	0.00	0.00	0.00	0.00
90th Percentile	0.00	0.00	0.00	0.00	0.00	0.00

Source: Congressional Budget Office.

Note: GDP = gross domestic product.

a. The balance is the difference between revenues (which do not include interest and intragovernmental transfers) and outlays.

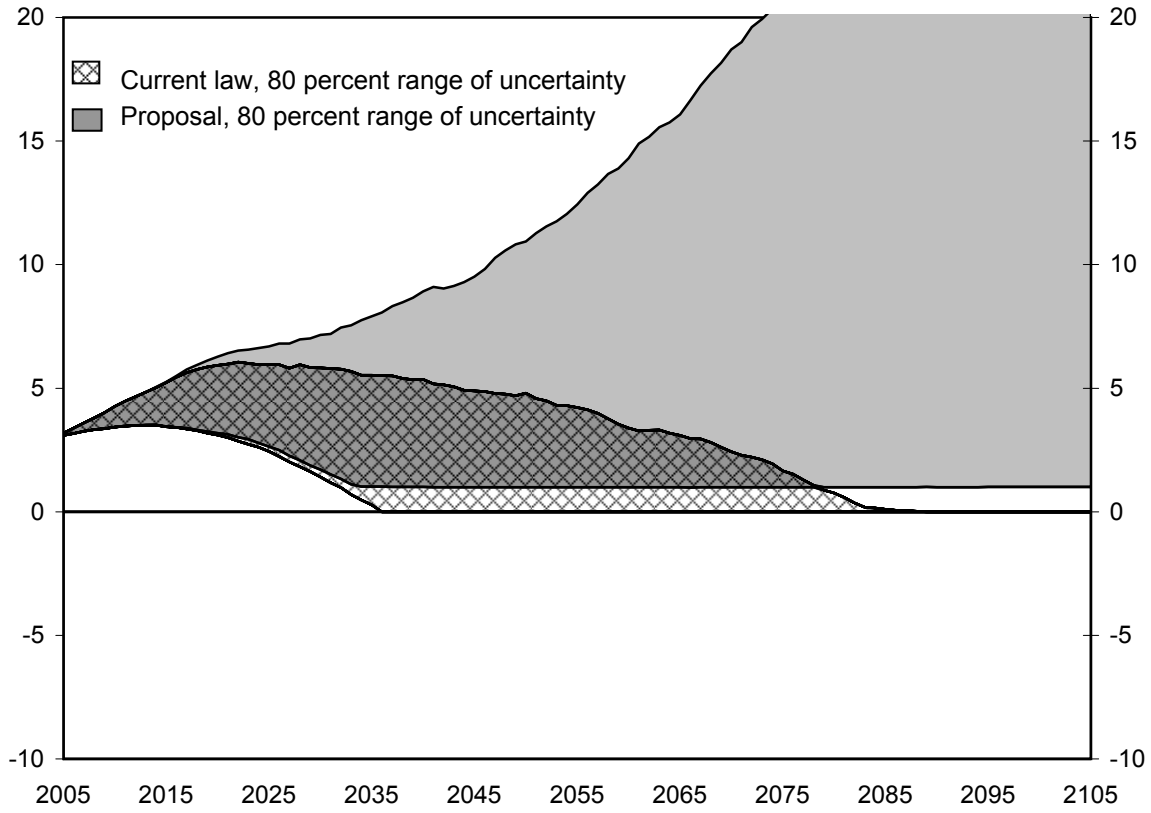
b. Equal to the difference between scheduled outlays and scheduled revenues in years after trust fund exhaustion.

Figure U3: Trust Fund Ratio

- Under current law, there is more than a 90 percent chance that the trust funds will be exhausted by 2090.
- The proposal requires transfers from the general fund into the trust funds if the trust fund ratio falls below 1, so there is no possibility of trust fund exhaustion under the proposal. At the 10th percentile, such transfers would occur, and the trust fund ratio would never fall below 1.

Figure U3.

Potential Range of Social Security Trust Fund Ratios Under Current Law and S. 2427, 2005 to 2105



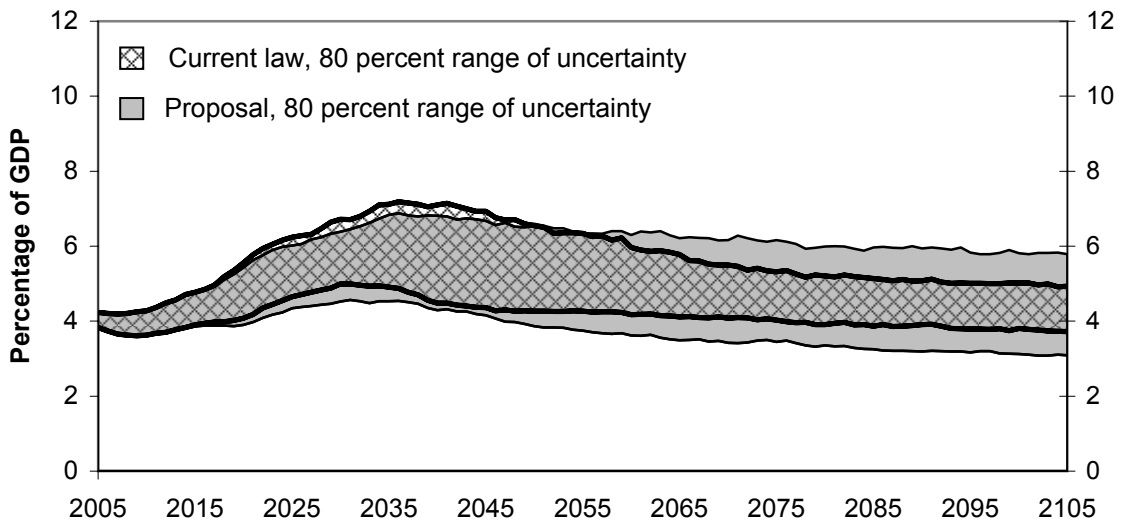
Source: Congressional Budget Office.

Figure U4: Total Social Security Benefits

- The potential range of Social Security benefits as a share of GDP is larger under the proposal than under current law. Under current law, the trust funds are very likely to become exhausted, and so benefits are likely to be limited to current revenues, which are relatively predictable. Under the proposal, the trust funds could not become exhausted, so the uncertainty about benefits would be equal to the uncertainty about scheduled benefits. As a result, there would be greater uncertainty about benefits under the proposal.

Figure U4.

**Potential Range of Social Security Benefits as a Share of GDP
Under Current Law and S. 2427, 2005 to 2105**



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table U2: First-Year Retirement Benefits

- The proposal would not affect workers born before 1950.
- Within the 100-year projection period, most workers would receive lower benefits under the proposal than under current law. Because of the progressive price indexing provision, the reductions would be smallest for the lowest earners and largest for the highest earners.
- Under current-law indexing, an individual's benefits are affected by average earnings growth in the economy. Under price indexing, benefits are not as sensitive to the rate of earnings growth. Therefore, there would be less uncertainty about benefit levels, especially for higher earners. In contrast, there would be greater uncertainty about the relationship between average benefits and average earnings in the economy (known as the replacement rate).
- In some cases, the benefits shown would be financed in part by transfers from the general fund of the Treasury.

Table U2.

Potential Range of First-Year Total Annual Benefits Under Current Law and S. 2427 for the Median Retired Worker If Benefits Are Claimed at Age 65, by Birth Cohort and Lifetime Earnings Level

(2004 dollars)

10-Year Birth Cohort Starting in Year	Current-Law Social Security Benefits			Proposed Social Security Benefits		
	10th percentile	50th percentile	90th percentile	10th percentile	50th percentile	90th percentile
Median in Lowest Household Lifetime Earnings Quintile						
1940	7,100	7,500	7,800	7,100	7,500	7,800
1950	7,100	8,100	9,200	6,900	7,900	8,900
1960	7,000	8,800	10,600	6,900	8,500	10,400
1970	5,700	9,300	11,900	7,000	8,900	11,200
1980	5,100	8,900	13,100	7,000	9,200	12,000
1990	5,400	8,700	14,900	7,500	10,100	13,700
2000	5,300	9,000	16,500	7,800	10,800	15,600
Median in Middle Household Lifetime Earnings Quintile						
1940	14,500	15,400	16,100	14,500	15,400	16,100
1950	13,500	15,500	17,500	12,900	14,300	15,700
1960	12,600	15,700	18,900	12,000	13,800	15,700
1970	10,700	17,600	22,300	12,200	14,200	16,300
1980	10,400	17,900	26,300	12,300	14,600	17,100
1990	10,700	17,300	29,500	12,500	15,000	18,400
2000	10,700	18,200	33,000	12,500	15,400	20,700
Median in Highest Household Lifetime Earnings Quintile						
1940	18,800	20,000	20,800	18,800	20,000	20,800
1950	18,900	21,700	24,600	17,600	19,400	21,200
1960	18,100	22,500	27,100	16,500	18,200	20,100
1970	14,800	24,800	31,400	15,900	17,600	19,300
1980	14,700	25,400	37,600	15,600	17,400	19,400
1990	15,400	24,700	42,200	15,100	17,000	19,500
2000	15,500	26,000	46,500	14,800	16,900	21,100

Source: Congressional Budget Office.

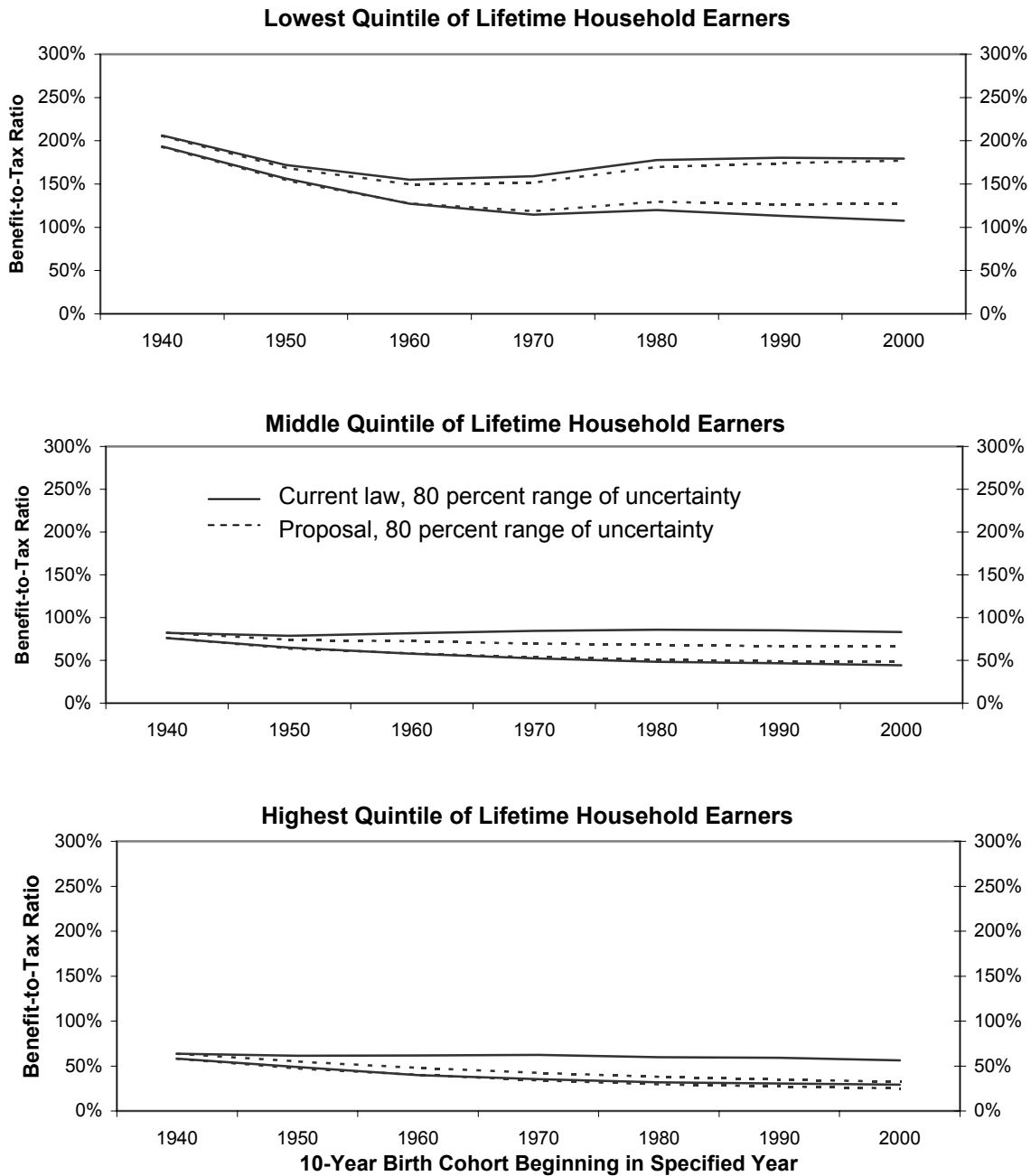
Figure U5: Ratio of Benefits Received to Taxes Paid Over a Lifetime

- Although in some cases, general funds would be transferred to the trust funds under the proposal, the ultimate source of those transfers is undefined, so they cannot be distributed to individuals. Therefore, this figure does not include such transfers, and automatic benefit reductions are applied in cases in which the trust funds fall to zero.
- There is generally less uncertainty under the proposal than under current law because there would be no possibility of trust fund exhaustion under the proposal.
- The ratio for the lowest quintile of earners would be almost as high under the proposal as under current law. And at the 10th percentiles of the distributions, the ratios under the proposal would be higher for the 1970s and later cohorts.
- For the middle quintile of earners, the ratio at the 10th percentile of the distribution would be about the same as under current law. Beginning with the 1950s cohort, the ratio would be lower under the proposal at the 90th percentile.
- Because of the shift toward price indexing, the 80 percent range of uncertainty under the proposal is very narrow for the highest earners. In addition, the benefit-to-tax ratios would be lower for all cohorts born in 1950 or later.

Benefit-to-Tax Ratios				
<u>1950s Cohort</u>	<u>Current Law</u>		<u>Proposal</u>	
	<u>10th Percentile</u>	<u>90th Percentile</u>	<u>10th Percentile</u>	<u>90th Percentile</u>
Lowest Earnings Quintile	156 %	172 %	154 %	169 %
Middle Earnings Quintile	65 %	79 %	64 %	74 %
Highest Earnings Quintile	49 %	61 %	47 %	55 %
<u>1990s Cohort</u>	<u>Current Law</u>		<u>Proposal</u>	
	<u>10th Percentile</u>	<u>90th Percentile</u>	<u>10th Percentile</u>	<u>90th Percentile</u>
Lowest Earnings Quintile	113 %	180 %	126 %	174 %
Middle Earnings Quintile	47 %	85 %	49 %	67 %
Highest Earnings Quintile	31 %	59 %	27 %	35 %

Figure U5.

Potential Range of the Ratio of Lifetime Dedicated-Tax-Financed Benefits to Lifetime Taxes Under Current Law and S. 2427, by Birth Cohort and Lifetime Earnings Level



Appendix: Scheduled-Benefits Scenario

The Social Security Administration would not have the legal authority to pay full benefits after trust fund exhaustion, so outlays would be limited to current revenues. That restriction is reflected in the current-law analysis described earlier.

However, the exhaustion of the trust funds would not affect a beneficiary's legal right to full benefits. The analysis in this appendix presents future spending for benefits under an alternative "scheduled benefits" scenario, in which outlays after trust fund exhaustion are assumed to include full benefits, despite any shortfall in the system's annual revenues. Those outlays would result in a negative trust fund balance, as if the system borrowed money.

Note that under the proposal, trust fund exhaustion cannot occur because the proposal requires that transfers be made from the Treasury to the trust funds in the event that the trust fund ratio falls below 1. As a result, the scheduled-benefits results for the proposal are identical to the results shown earlier.

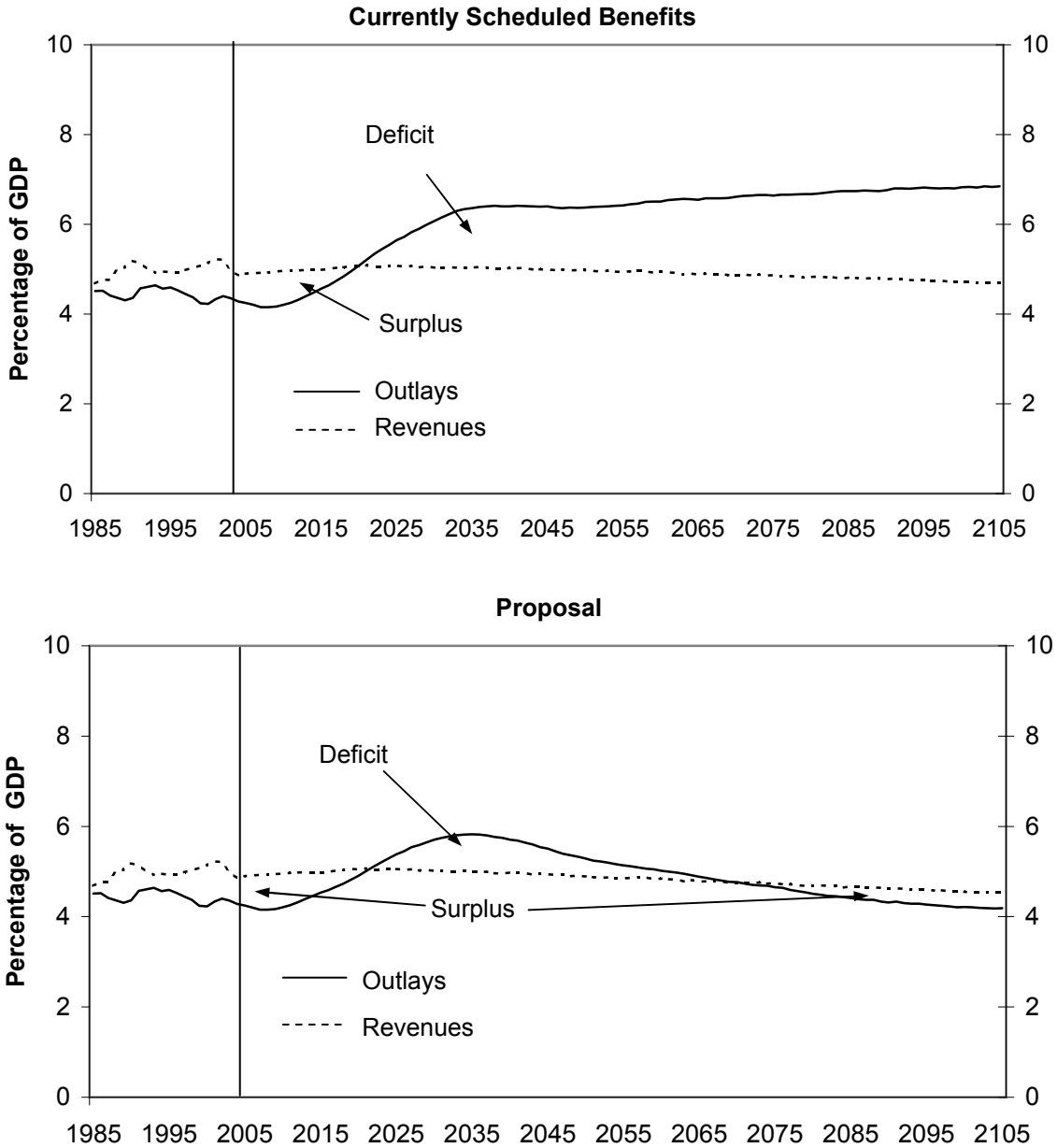
Figures 5 and U5 compare taxes paid with benefits received, but such an analysis cannot be done without fully specifying the source of the taxes. Because the financing source of some benefits is unspecified under the scheduled-benefits scenario, Figures 5 and U5 are not included in this appendix.

Figure 1 (Scheduled): Effect on Social Security Finances

- CBO projects that under currently scheduled benefits, outlays will exceed revenues beginning in 2020 and will exceed the sum of revenues and interest credited to the Social Security trust funds beginning in 2033. CBO projects that the trust funds will be exhausted in 2052.
- Under the proposal, outlays are projected to exceed revenues from 2022 through 2070. Thereafter, outlays would fall below revenues. The trust fund ratio would remain positive and large, CBO projects.

Figure 1 (Scheduled).

Social Security Revenues and Outlays as a Share of GDP Under Currently Scheduled Benefits and S. 2427, 1985 to 2105



Source: Congressional Budget Office.
 Note: GDP = gross domestic product.

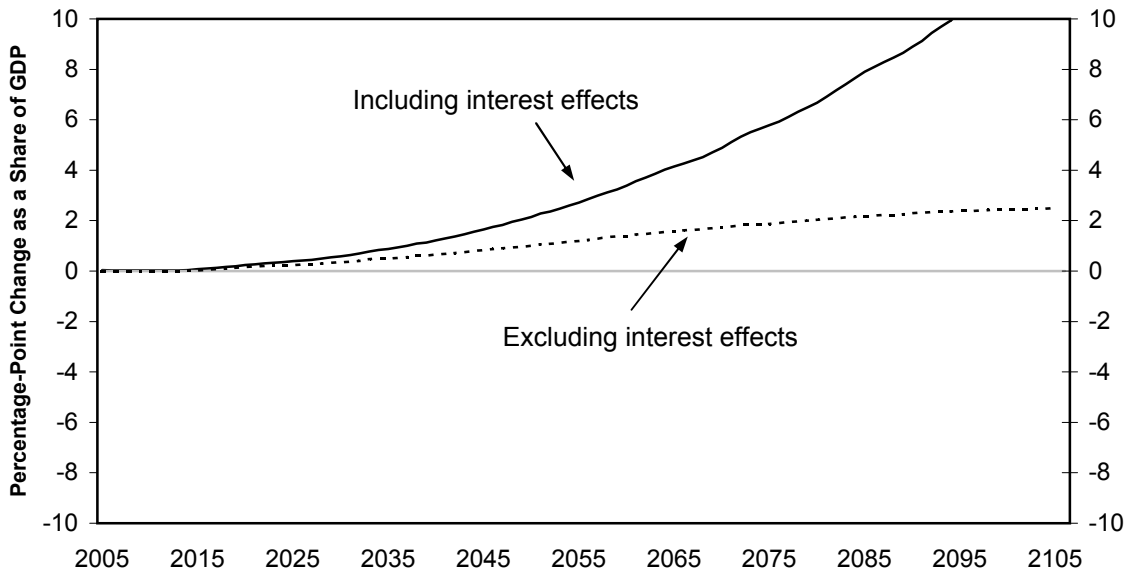
Figure 2 (Scheduled): Net Effect on the Federal Budget

Recall that negative numbers mean that the proposal would increase the deficit (or reduce the surplus). Positive numbers indicate that it would reduce the deficit (or increase the surplus).

- Beginning in 2012, the proposal would improve the annual budget balance because it would lower Social Security benefits. By the end of the projection period, the improvement in the annual budget balance (excluding interest) would exceed 2 percent of GDP. That improvement would result in a large reduction in federal interest payments; by the end of the projection period, the improvement including interest would be almost 13 percent of GDP.

Figure 2 (Scheduled).

Effects of S. 2427 on Total Annual Budget Balances as a Share of GDP Relative to Currently Scheduled Benefits, 2005 to 2105



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table 1 (Scheduled): Effect on Social Security Finances for Specific Years and Provisions

- This table is nearly identical to Table 1. The main difference is that under the scheduled-benefits scenario, there are no automatic benefit reductions.
- Under currently scheduled benefits, after trust fund exhaustion, revenues are about 0.1 percent of GDP higher than under current law (shown in Table 1). That is because of higher revenues from the taxation of benefits, which result from higher outlays.

Table 1 (Scheduled).**Social Security Finances Under Currently Scheduled Benefits and S. 2427 as a Share of GDP, 2005 to 2105**

(percent)

	2005	2025	2045	2065	2085	2105
Social Security Finances Under Currently Scheduled Benefits						
Revenues ^a	4.90	5.07	4.99	4.88	4.80	4.69
Outlays ^b	4.25	5.64	6.39	6.55	6.72	6.85
Balance ^c	0.65	-0.57	-1.40	-1.67	-1.92	-2.15
Effects on Balance Plus Automatic Benefit Reduction Under Proposed Provisions						
Shorten NRA Hiatus by Five years	0.00	0.06	0.01	0.00	0.00	0.00
Longevity Index Benefits	0.00	0.03	0.22	0.47	0.71	0.93
Progressive Indexing Holding 30 Percent Harmless	0.00	0.18	0.68	1.25	1.74	1.95
Interactions Among Provisions	0.00	-0.02	-0.10	-0.15	-0.28	-0.38
Total Effects, All Provisions	0.00	0.25	0.82	1.56	2.17	2.50
Social Security Finances Under Proposal						
Revenues ^a	4.90	5.06	4.94	4.78	4.66	4.53
Outlays ^b	4.25	5.38	5.51	4.88	4.41	4.19
Balance ^c	0.65	-0.32	-0.57	-0.11	0.25	0.35
Transfers from Rest of Government	0.00	0.00	0.00	0.00	0.00	0.00

Source: Congressional Budget Office.

Note: GDP = gross domestic product; NRA = normal retirement age

- a. Revenues equal payroll taxes and income taxes on benefits (but not interest credited to the trust funds or intragovernmental transfers) in the specified year.
- b. Outlays equal Social Security benefits plus administrative costs.
- c. The balance is the difference between revenues and outlays; it may not equal the difference of the previous two rows because of rounding.

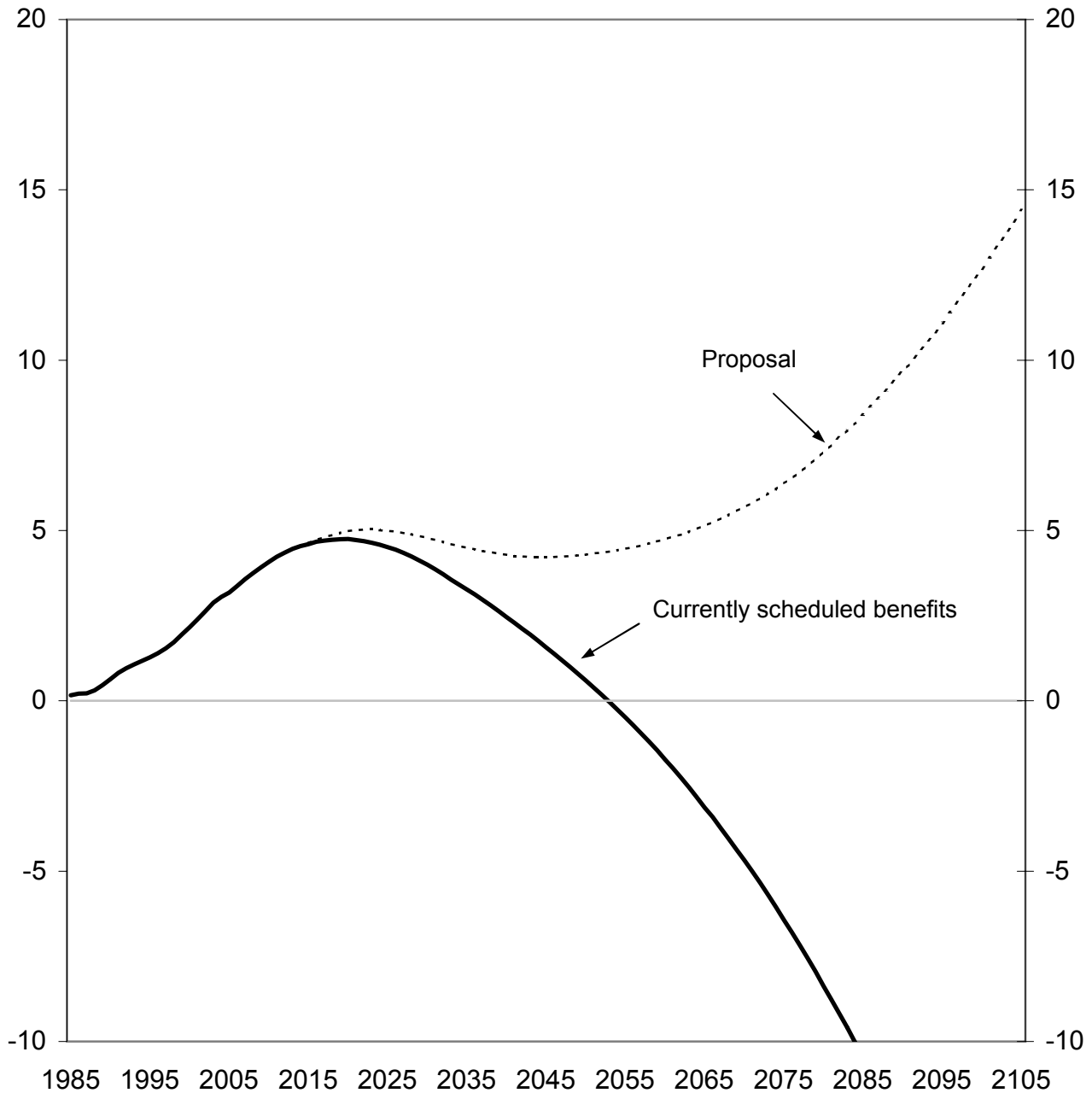
Figure 3 (Scheduled): Trust Fund Ratio

Under the scheduled-benefits scenario, the trust fund balance could become negative, representing net borrowing by the Social Security program.

- Under currently scheduled benefits, the trust fund ratio would first become negative in 2052; under the proposal, the trust fund ratio would remain positive throughout the projection period.
- Because annual deficits would be much smaller under the proposal, the trust fund ratio would increase.
- At the end of the projection period, the trust fund ratio would be -22 under currently scheduled benefits but above 14 under the proposal.

Figure 3 (Scheduled).

Social Security Trust Fund Ratios Under Currently Scheduled Benefits and S. 2427, 1985 to 2105



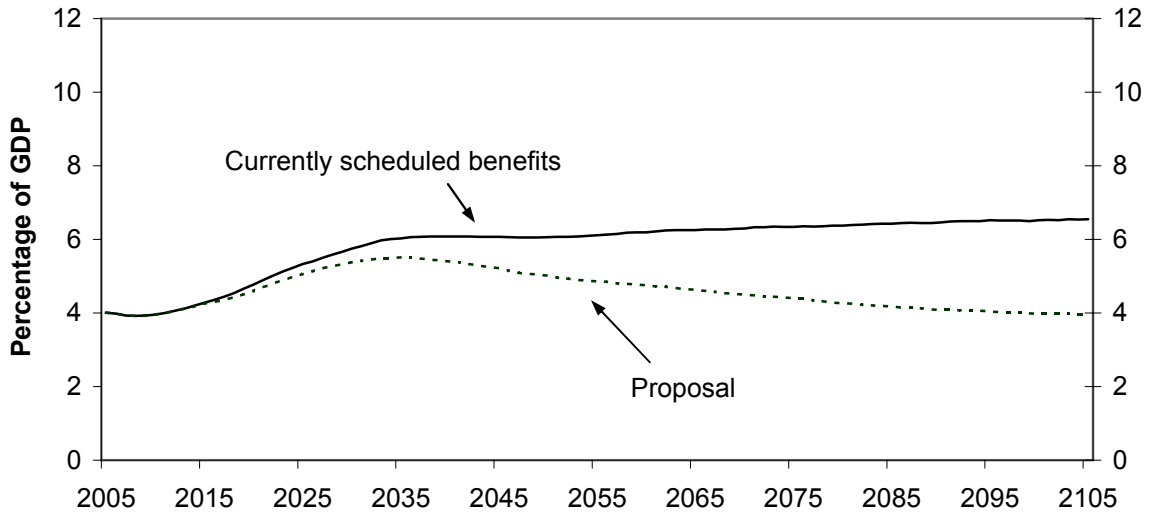
Source: Congressional Budget Office.

Figure 4 (Scheduled): Total Social Security Benefits

- Under the proposal, benefits would be lower than currently scheduled benefits beginning in 2012.
- By the end of the projection period, proposed benefits would be lower than currently scheduled benefits by more than 2.5 percentage points of GDP.

Figure 4 (Scheduled).

Social Security Benefits as a Share of GDP Under Currently Scheduled Benefits and S. 2427, 2005 to 2105



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table 2 (Scheduled): First-Year Retirement Benefits

- The proposal would not affect workers born before 1950.
- Workers born in 1950 and later would receive benefits that are lower under the proposal than under currently scheduled benefits because all provisions in the proposal affect workers born in 1950 and later.
- Reductions for workers in the lowest household earnings quintile would be smaller than those for workers in the middle and upper income quintiles—because although all workers would be affected by the acceleration in the increase in the normal retirement age and longevity indexing, the reductions from the progressive indexing provision would be greater for higher earners.

Table 2 (Scheduled).

First-Year Total Annual Benefits for the Median Retired Worker Under Currently Scheduled Benefits and S. 2427 If Benefits Are Claimed at Age 65, by Birth Cohort and Lifetime Earnings Level

(2004 dollars)

10-Year Birth Cohort Starting in Year	Currently Scheduled Social Security Benefits	Proposed Social Security Benefits	Percentage of Benefits Financed with Intragovernmental Transfers
Median in Lowest Household Lifetime Earnings Quintile			
1940	7,500	7,500	0.0
1950	8,300	8,000	0.0
1960	9,000	8,800	0.0
1970	9,800	9,200	0.0
1980	10,600	9,800	0.0
1990	12,200	10,800	0.0
2000	13,500	11,700	0.0
Median in Middle Household Lifetime Earnings Quintile			
1940	15,500	15,500	0.0
1950	15,800	14,500	0.0
1960	16,200	14,300	0.0
1970	18,600	14,800	0.0
1980	21,300	15,400	0.0
1990	24,100	15,900	0.0
2000	27,000	16,700	0.0
Median in Highest Household Lifetime Earnings Quintile			
1940	20,200	20,200	0.0
1950	22,200	19,900	0.0
1960	23,300	19,000	0.0
1970	26,200	18,600	0.0
1980	30,300	18,300	0.0
1990	34,300	17,900	0.0
2000	38,900	17,700	0.0

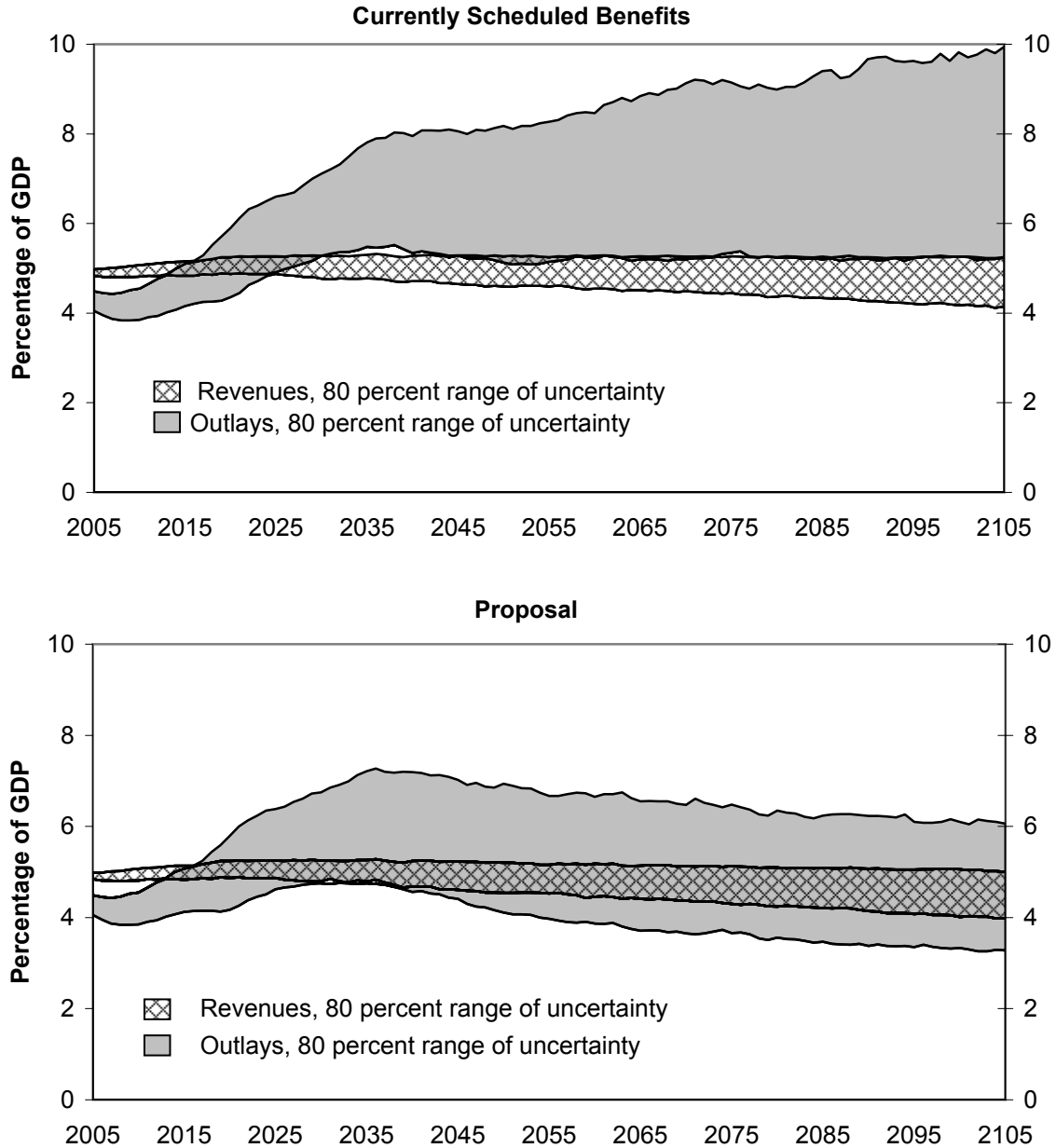
Source: Congressional Budget Office.

Figure U1 (Scheduled): Effect on Social Security Finances

- In the current-law analysis, annual outlays equal annual revenues following trust fund exhaustion, so uncertainty about outlays is limited after exhaustion (see Figure U1). There is no such restriction in the scheduled-benefits scenario, so there is much greater uncertainty about outlays in later years than in the current-law analysis.
- The range shown for outlays under the proposal is smaller only because the overall level of benefits is lower. Relative to the expected level of outlays, there is actually slightly greater uncertainty under the proposal. The longevity indexing reduces uncertainty. However, the shift toward price indexing removes some of the correlation between outlays and real wage growth and therefore also removes some of the correlation between outlays and the level of GDP, adding some uncertainty.

Figure U1 (Scheduled).

Potential Range of Social Security Revenues and Outlays as a Share of GDP Under Currently Scheduled Benefits and S. 2427, 2005 to 2105



Source: Congressional Budget Office.
 Note: GDP = gross domestic product.

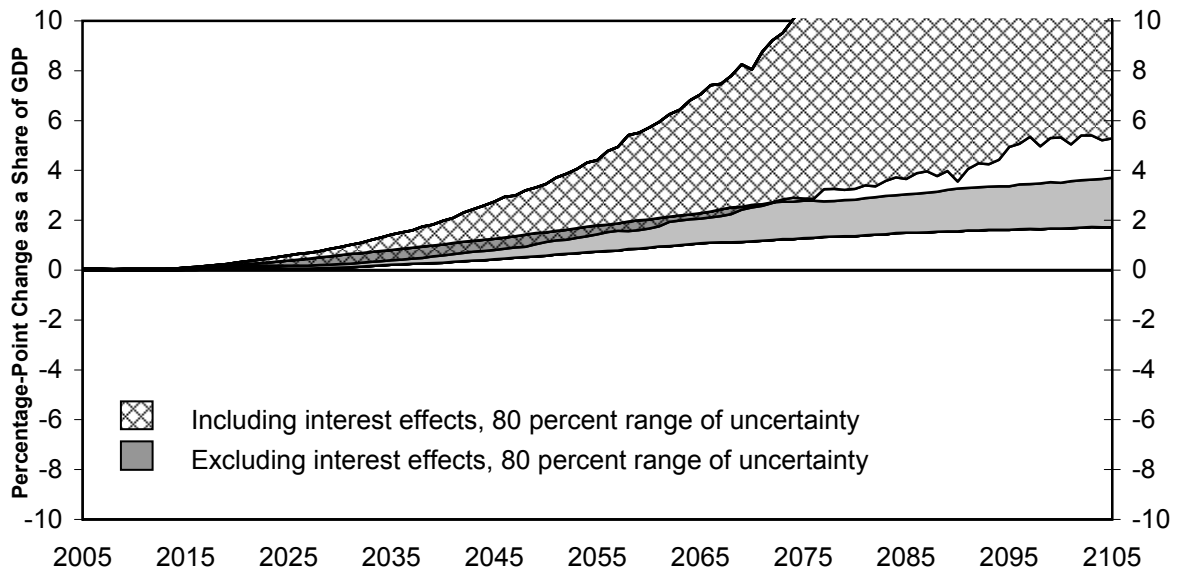
Figure U2 (Scheduled): Net Effect on the Federal Budget

Recall that negative numbers mean that the proposal would increase the deficit (or reduce the surplus). Positive numbers indicate that it would reduce the deficit (or increase the surplus).

- Initially, the possible range of effects of the proposal on annual budget balances would be the same as under the current-law analysis shown in Figure U2.
- In later years, there would be much greater uncertainty about the effects than is shown in the current-law analysis because there is much greater uncertainty about currently scheduled benefits, as shown in Figure U1 (Scheduled).

Figure U2 (Scheduled).

Potential Range of Effects of S. 2427 on Total Annual Budget Balances as a Share of GDP Relative to Currently Scheduled Benefits, 2005 to 2105



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table U1 (Scheduled): Effect on Social Security Finances for Specific Years

- The data shown here are similar to those in Table U1, but there are no automatic benefit reductions under the scheduled-benefits scenario.
- In general, the balance under the scheduled-benefits scenario is equal to the sum of the balance and the automatic benefit reductions in the current-law scenario.⁴

⁴That statement is true of each of the 500 scenarios that CBO ran to produce the probability distribution. However, it is not necessarily true of the data shown in the tables, because each set of data is sorted strictly numerically. Therefore, a given scenario may fall at a different place in the distribution of the current-law scenario than in the distribution of the scheduled-benefits scenario. In some simulations, the trust funds become exhausted in the 2030s. Under current law, annual balances automatically equal zero after trust fund exhaustion. The annual balance in most simulations is negative before trust fund exhaustion. After the trust fund becomes exhausted, the annual balance for that simulation will become zero, shifting the distribution to the right. As a result, the value at any given percentile will be higher. In the corresponding scheduled-benefits simulation, the balance will remain negative and there will be no such shift. As a result, for example, in the currently scheduled benefits scenario the 50th percentile of the balance in 2045 is -1.60 percent of GDP. Under current law, the corresponding value is -0.65 percent, and the 50th percentile of the automatic benefit reduction is zero.

Table U1 (Scheduled).

Potential Range of Social Security Finances Under Currently Scheduled Benefits and S. 2427 as a Share of GDP, 2005 to 2105

(percent)	2005	2025	2045	2065	2085	2105
Currently Scheduled Balance^a						
10th Percentile	0.45	-1.52	-3.12	-3.92	-4.70	-5.28
Median - 50th Percentile	0.64	-0.65	-1.60	-1.82	-2.16	-2.43
90th Percentile	0.80	0.01	-0.41	-0.46	-0.58	-0.83
Balance Under Proposal						
10th Percentile	0.45	-1.34	-2.16	-2.00	-1.67	-1.55
Median - 50th Percentile	0.64	-0.41	-0.74	-0.16	0.02	0.12
90th Percentile	0.80	0.31	0.42	1.00	1.14	1.21
Transfers from Rest of Government Under Proposal						
10th Percentile	0.00	0.00	1.63	1.44	0.92	0.43
Median - 50th Percentile	0.00	0.00	0.00	0.00	0.00	0.00
90th Percentile	0.00	0.00	0.00	0.00	0.00	0.00

Source: Congressional Budget Office.

Note: GDP = gross domestic product.

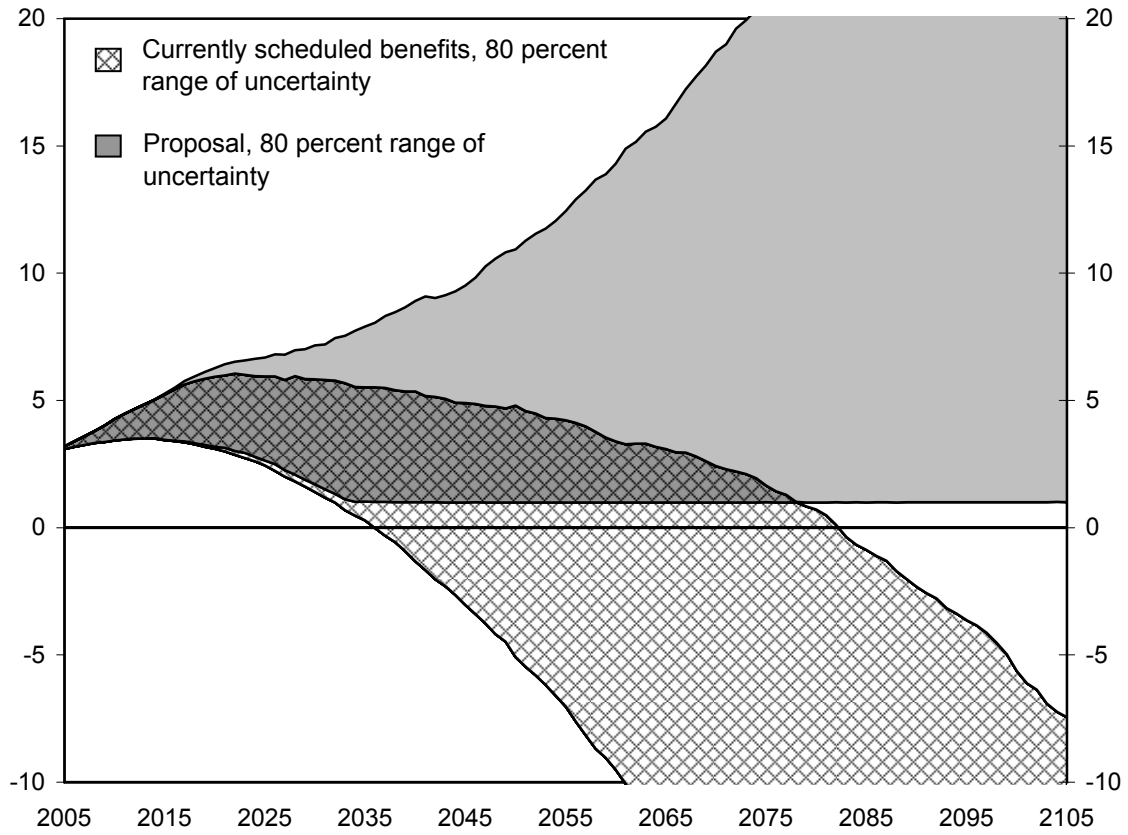
a. The balance is the difference between revenues (which do not include interest and intragovernmental transfers) and outlays.

Figure U3 (Scheduled): Trust Fund Ratio

- The uncertainty ranges fall below zero under the currently scheduled benefits scenario because there are no automatic benefit reductions.
- The trust fund ratio for the proposal is identical to that shown in Figure U3 because of the provision requiring intragovernmental transfers to the trust funds to maintain a trust fund ratio of 1.

Figure U3 (Scheduled).

Potential Range of Social Security Trust Fund Ratios Under Currently Scheduled Benefits and S. 2427, 2005 to 2105



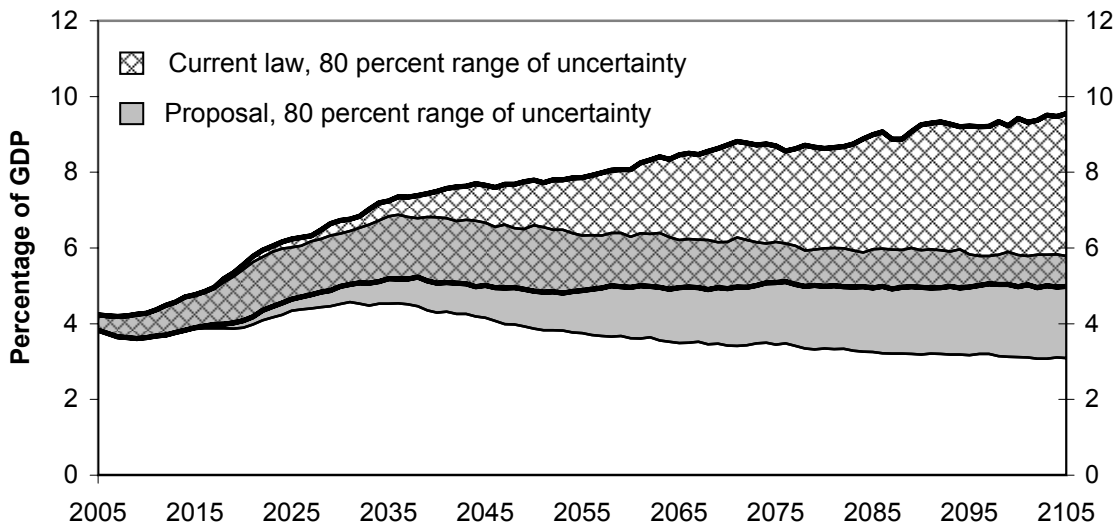
Source: Congressional Budget Office.

Figure U4 (Scheduled): Total Social Security Benefits

- The uncertainty about benefits as a share of GDP under the proposal is slightly less than the uncertainty under currently scheduled benefits.
- The longevity indexing reduces uncertainty. However, the shift toward price indexing removes some of the correlation between outlays and real (inflation-adjusted) wage growth and therefore also removes some of the correlation between outlays and the level of GDP—which adds some uncertainty.

Figure U4 (Scheduled).

**Potential Range of Social Security Benefits as a Share of GDP
Under Currently Scheduled Benefits and S. 2427, 2005 to 2105**



Source: Congressional Budget Office.
Note: GDP = gross domestic product.

Table U2 (Scheduled): First-Year Retirement Benefits

- At all points on the distribution, benefits are lower under the proposal. The uncertainty range, however, is smaller, especially for the highest-earning quintile. Benefits for that group would be closely linked to prices, so their benefits would generally be unaffected by variation in real earnings growth.

Table U2 (Scheduled).

**Potential Range of First-Year Total Annual Benefits for the Median Retired Worker
if Benefits Are Claimed at Age 65 Under Currently Scheduled Benefits and Scheduled
S. 2427, by Birth Cohort and Lifetime Earnings Level**

(2004 dollars)

10-Year Birth Cohort Starting in Year	Currently Scheduled Social Security Benefits			Proposed Social Security Benefits		
	10th percentile	50th percentile	90th percentile	10th percentile	50th percentile	90th percentile
Median in Lowest Household Lifetime Earnings Quintile						
1940	7,100	7,500	7,800	7,100	7,500	7,800
1950	7,100	8,100	9,200	6,900	7,900	8,900
1960	7,100	8,800	10,600	6,900	8,500	10,400
1970	7,500	9,500	11,900	7,000	8,900	11,200
1980	7,900	10,100	13,300	7,000	9,200	12,000
1990	8,500	11,600	15,600	7,500	10,100	13,700
2000	9,200	12,700	17,800	7,800	10,800	15,600
Median in Middle Household Lifetime Earnings Quintile						
1940	14,500	15,400	16,100	14,500	15,400	16,100
1950	13,500	15,500	17,500	12,900	14,300	15,700
1960	12,900	15,700	18,900	12,000	13,800	15,700
1970	14,200	17,900	22,300	12,200	14,200	16,300
1980	15,700	20,300	26,700	12,300	14,600	17,100
1990	16,900	22,900	30,900	12,500	15,000	18,400
2000	18,400	25,600	36,200	12,500	15,400	20,700
Median in Highest Household Lifetime Earnings Quintile						
1940	18,800	20,000	20,800	18,800	20,000	20,800
1950	18,900	21,700	24,600	17,600	19,400	21,200
1960	18,300	22,500	27,100	16,500	18,200	20,100
1970	19,900	25,400	31,400	15,900	17,600	19,300
1980	22,600	28,800	37,800	15,600	17,400	19,400
1990	24,100	32,500	43,800	15,100	17,000	19,500
2000	26,100	36,400	51,000	14,800	16,900	21,100

Source: Congressional Budget Office.