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Social Security and the federal budget: Another instance of the emperor's new clothes

by Robert J. Myers

General agreement exists throughout the country that the United States has a very serious problem with regard to its mammoth federal budget deficits in the past decade and those projected for years to come. Unfortunately, little agreement exists as to what should be done.

The budget deficit widely quoted for the fiscal year ended September 30, 1994, is $203 billion — a horrendously high figure, especially because since 1983 it has never been less than $150 billion per year; for eight years, it has exceeded $200 billion. To make matters even worse, perhaps the greatest hoax — even fraud — that has been imposed on the public is the information that the federal government gives about the relationship between the general budget and the various trust fund programs, such as Social Security and Medicare. Few "little boys" are present in political circles to point out that "the emperor really doesn't have any clothes on!"

Under the so-called unified budget procedure, the operations of these programs are included within the general operations of the federal government. Thus, any excess of income over outgo from sources outside the federal government is shown as reducing the general budget deficit. This does not really happen, because such excesses are invested in government bonds and other obligations that are part of the national debt. If the trust funds had not had such excesses to invest in government obligations, the general public would have had to purchase obligations of similar amount, and the national debt would have been exactly the same size. Thus, in reality, in fiscal year 1994, the real general budget deficit was $292 billion, or $89 billion higher than the deficit shown under the unified budget procedure.

This deceptive unified budget procedure was first effective for fiscal year 1969, and it showed a surplus of $3 billion, which was the last year when a surplus occurred. The immediately preceding years of surplus were 1956 and 1957, when equally small surpluses occurred. Actually, the real deficit in 1969 was about $300 million higher, but for the next year, it was $12 billion higher than the $3 billion reported on the unified budget basis.

Further, under the unified budget procedure, the interest paid to the trust funds on their investments is not counted as interest but rather as an intergovernmental transaction. However, such interest is real interest and adds to both the general budget deficit and the national debt in just the same manner as any other interest paid on obligations of the federal government. The interest on the national debt is now running at about $300 billion per year, rather than the horrendous $200 billion quoted under the unified budget procedure.

The operations of the Social Security trust funds with respect to self-supporting payroll-tax-financed programs should not be considered in connection with the great deficit problems of the general budget. In fact, if all other government programs and activities were equally self-supporting, we would not have the budget deficit problems that we now have. Further, the unified budget procedure causes many people to believe, quite understandably, that the trust fund monies have been "stolen" and used for the general expenses of the federal government. This is, of course, not true, because the government obligations held by the trust funds are just as valid and valuable as those held by private investors.

For about the next 15 to 20 years, the excess of income over outgo of the Social Security program will, under present law, be quite large each year. This, under the unified budget procedure, will hide the real extent of the true general budget deficit. However, thereafter the tide will turn, and the inclusion of the operations of the Social Security program in the unified budget procedure will result in larger figures for the general budget deficit than the true ones being shown. As a result, some are now advocating that Social Security benefits should be cut back, more or less immediately, to remedy this situation and to even go beyond it and reduce the deficit more and sooner.

It is almost certain that some changes will need to be made to the Social Security program over the long run to keep it fiscally viable, i.e., self-supporting. However, such changes can and should be done on a deferred, gradual basis. The changes should be made solely for the sake of the Social Security program and not at all for the sake of the general budget deficit. At the same time, policymakers and the general public should recognize the grossly misleading nature of the budget deficit figures that arise for the next few years (and even decades) under the unified budget procedure. Then, action should be taken to solve this problem, which is much larger than the mammoth one that is currently reported under that procedure.

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