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Commentary

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The Social Security Trust Fund: The Lent or Spent Dilemma

A controversial question is being widely debated as to whether the Social Security trust fund has been lent or spent. According to the trustees, the fund holds assets of $2.6 trillion invested in US Treasury securities; this represents the accumulated value of surplus amounts transferred from Social Security to the Treasury. The issuance and maturity of these special issue Treasury securities is a routine process that operates continuously and smoothly; the US Treasury regularly meets its obligations for interest payments and scheduled principal payments as the securities reach their respective maturity dates. This is the *de jure* position, meaning that these securities are legal obligations of the US Treasury to the Social Security trust fund and are subject to the full faith and credit of the United States.

Recent negotiations to raise the national debt limit by Congress have brought attention to the possibility that the US might conceivably default on its financial obligations. There has even been speculation that a failure by Congress to increase the debt limit might jeopardize the ability of the Treasury to disburse Social Security benefit payments. A logical and oft-repeated question during these negotiations was: “If the Social Security trust fund has $2.6 trillion in assets (equivalent to about three and a half years worth of benefit payments) why is there any doubt about the timely payment of benefits”? From the perspective of a typical senior citizen entitled to Social Security, this was a “show me the money” moment. The explanation for this paradox is that the proceeds of the bonds are used by the Treasury for a variety of current expenditures. However, the Treasury is obligated to repay the principal at some future date (such as fifteen years later) as well as interest on the principal amount. To meet its emerging obligations, the Treasury must generate sufficient revenues from taxation, or apply existing reserves, or borrow through the issuance of new securities. Due to its practice of running current budget deficits, the ability to borrow becomes essential to avoiding default and hence necessitates an increase in the authorized “ceiling” for the national debt limit. The recent concerns over a possible default arose from a liquidity problem within the US Treasury due to deficit spending. Without an increase in the authorized national debt limit, the Treasury would have faced a liquidity crisis that could have affected its ability to meet current payments when due.

Although the *de jure* view of the Social Security trust fund is indisputable, there is an alternative *de facto* view that is based on economic realities. This alternative view arises from the fact that Treasury has used the proceeds of its special bond issues (received in the form of surplus transfers from Social Security) for current expenditures. This practice temporarily obviates the necessity for greater current tax revenues and/or more borrowing to meet current expenditures. However, this process essentially transfers the funding of current deficits to a future date. The availability of cash transfers from Social Security has resulted in the obfuscation of the true extent of deficit spending. This *de facto* view of the trust fund emphasizes the diversion of Social Security surplus revenues to the Treasury for use to meet current government expenditures. It essentially takes a view that the Federal Insurance Contribution Act (FICA) contributions in the form of payroll taxes are simply a part of the aggregate current tax revenues and are not specifically reserved for current and future Social Security benefit payments. Adherents of this view claim that the Social Security surplus has been spent not lent. Obviously, Social Security surpluses cannot be used both for current expenditure and for future benefit payments. The *de facto* view implies that from the government’s perspective the economic effect is that benefit payments must be met from future general tax revenues or from future borrowing by the Treasury. This line of reasoning then leads to the conclusion that the Social Security trust fund has no real assets and that it is merely a product of arcane accounting procedures.

While it may be claimed that from a purely economic standpoint the *de jure* and *de facto* views of the Social Security trust fund do not differ in their effect, it is an irrefutable fact that the special issue securities held by the trust fund are a legal obligation of the Treasury and are subject to the full faith and credit of the United States. This fact makes clear that there is an important distinction to be made between the *de jure* and *de facto* viewpoints concerning the Social Security trust fund. The *de facto* position could only be substantiated in the unlikely event of the government actually defaulting on its legal financial obligations to the Social Security trust fund.

Buffin Partners Inc.

P.O. Box 1255
Sparta, NJ 07871
Phone: (973) 579-6371
Fax: (973) 579-7067
Email: commentary@buffinpartners.com