



Confusion and Misconception Abound: Setting the Record Straight

It is funny how I am still amazed each time these situations happen.

On August 8, 2020, President Trump issued an executive order directing the Secretary of Treasury to use his authority to defer payroll tax from September 1, 2020 through December 31, 2020.(1)

This executive order has put Social Security front and center of many conversations. The part that amazes me and quite frankly disturbs me, are the number of discussions I have had, combined with things I have read, which mischaracterize how the Social Security system actually works.

In my humble effort to provide support, let me review some of the finer points of Social Security, all fully sourced, in order to combat the misconception some people have from blogs and other social media sources which are simply wrong.

A Quick Walk Down History

Let's start with an understanding of the history of the Social Security Act which was signed into law by President Roosevelt on August 14, 1935. This Act created a social insurance program designed to pay retired workers age 65 or older a continuing income after retirement.(2)

One of the first American books on social insurance was by a Columbia University economics professor named Henry Seager. In his 1910 book, "Social Insurance, A Program of Social Reform" his explanation of the principle of old-age security based on social insurance gives us some insight of what the program was designed to accomplish.

“As changing economic conditions are rendering the dependence of old people on their descendants for support increasingly precarious...new obstacles are arising to providing for old age through voluntary saving. The proper method of safeguarding old age is clearly through some plan of insurance...for every wage earner to attempt to save enough by himself to provide for his old age is needlessly costly. The intelligent course is for him to combine with other wage earners to accumulate a common fund out of which old-age annuities may be paid to those who live long enough to need it.” (2)

In 1934, with the nation in the throes of the Great Depression and confidence in the old order rattled to its core, President Franklin Roosevelt chose the social insurance approach as the “cornerstone” of his policy to remedy the outcry for economic security.

Once enacted and Social Security numbers were designated to Americans, in January 1937, the first Federal Insurance Contributions Act (FICA) taxes were levied and collected. Special Trust Funds were created for these dedicated revenues. Benefits were then paid from the money accumulated in the Social Security Trust Funds.(2)

Social Security Trust Funds

Over the years, more than \$8.7 trillion has been paid into the Trust Funds, and more than \$7.4 trillion has been paid out in benefits. The remainder is currently on reserve in the Trust Funds and will be used to pay future benefits.(2)

These Trust Funds are accounts in the U.S. Treasury and consist of two separate Social Security trust funds. The first is called the Old-Age and Survivors Insurance (OASI) Trust Fund and its purpose is to pay retirement and survivors benefits. The second fund is the Disability Insurance (DI) Trust Fund which pays disability benefits.(3)

The FICA tax paid, plus interest income, are placed into these accounts and benefits are paid from them. These Trust Funds are limited in what they can be used for and can only be used to pay benefits and administrative costs. (3)

Money that is not needed from the Trust Fund to pay benefits or administrative costs must be held in the trust and by law, must be invested in special Treasury bonds that are guaranteed by the U.S. Government. (3)

Myth That the Government Can “Raid” the Trust Funds

Suggestion that the government can “raid” the Social Security Trust Funds are simply not true. Part of the confusion may lie in the fact that the Trust Fund must invest in those special treasury bonds. In this arrangement, as is the case with any bond, the Treasury is in essence, borrowing money from the Trust Fund and in return, the trust fund receives a bond with a stated interest rate and maturity date.

Once the bond is issued, as with any treasury auction, the government can do whatever they want with the money.

The treasury has always paid the interest due on these bonds and repaid the principle. As seen below, the interest payment on these bonds generated over \$80 billion in interest payments in 2019 alone.(4)

FICA Tax – The Payroll Tax Currently in the News

Employers in 2020, are paying a 6.2% tax into the Trust Funds and employees are paying an additional 6.2 percent of their wages to the trust - up to the taxable maximum of \$137,700. People who are self-employed pay 12.4 percent.(5)

Myth: Undocumented Immigrants Are Depleting the Trust Funds

It is interesting to note that the notion that undocumented immigrants are depleting the Social Security Trust Fund is also a misconception.(6) If the immigrant is here illegally and they do not have a Social Security number, they cannot receive benefits. However, each year they contribute to the Trust Fund by having their 6.2% plus their employer's 6.2% taken out of their pay checks under false Social Security numbers.

In fact, in a 2013 report, the Chief Actuary of the Social Security Administration estimated that undocumented immigrants contributed \$12 billion to the Social Security Trust Fund and will be ineligible to receive any benefits.(7)

How was Social Security Funded in 2019

In 2019, \$944.5 billion or 89 percent of total Old-Age and Survivors Insurance (OASI) and Disability Insurance income (DI) came from payroll taxes discussed above. The remainder that was paid out was provided by interest, earning \$80.8 billion for a total of 7.6 percent, and revenue from taxation of OASDI benefits of \$36.5 billion. This accounts for the remaining 3.4 percent.(5)

Status of Trust Funds

At year-end, Social Security's 2019 reserves were \$2.9 trillion, an increase of \$2 billion. It is estimated by the Trustees that the Old-Age and Survivors Insurance (OASI) Trust Fund, the trust people will depend on for Social Security income benefits, will be able to pay full benefits on a timely basis until 2034. This is unchanged from the previous year.(8)

The Disability Insurance (DI) Trust Fund is now projected to be able to pay full benefits until 2065. This is 13 years later than indicated in last year's Social Security report due to disabled-worker applications substantially declining since 2010 and the number of disabled-workers receiving benefits decreasing since 2014.(8)

President Trump's Payroll Tax Deferral Program

As seen from the source of funding for Social Security, some of the concerns surrounding the deferral and promised elimination of the payroll tax which funds Social Security could result in an almost \$1 trillion short fall that is generated by the tax.

In August, President Trump said at a news conference, "If I'm victorious on Nov. 3, I plan to forgive these taxes and make permanent cuts to the payroll tax. I'm going to make them all permanent. In other words, I'll extend beyond the end of the year and terminate the tax."(9)

President Trump said that if the tax is eliminated, the funding for Social Security will come from the General Fund.(10) It would not be the first time the General Fund has been used to pay Social Security benefits.

In 2011 and 2012, in an effort to stimulate the economy, Congress lowered the payroll tax by 2% but also authorized moving \$225 billion from the general fund to make up the difference so the reduction of the tax would not affect the Social Security Trust Fund.

Congress also used the General Fund in 1957 and 2001 to pay for extra benefit credits to active-duty military. It was also used as a special benefit for people not covered by the program by 1968, as a payroll tax credit in 1984, and for a variety of other reasons. Overall, nearly \$260 billion has been transferred from the General Fund since 1965.(11)

One of My All-Time Favorite Final Fun Myths

Since life expectancy in 1930 was age 58 for men and age 62 for women, many people argue that the system was designed as a scam. Workers paying tax into a system that they would never benefit from since they were not expected to live to retirement at age 65, which of course is when the benefit was scheduled to begin.

On the surface, it makes sense, doesn't it?

Not when it is understood that life expectancy from birth at that time was low primarily due to high infant mortality. Clearly, this together with accidents and diseases that caused death at an early age, would lower the overall life expectancy and are included in the average.

However, if a male made it to age 21, 54% could expect to live until age 65 and for those attaining age 65, they would average 13 years of receiving Social Security benefits and that number was even higher for women.(12)

Understanding the full scope of the mortality tables in the 1930s, it is easy to see that it was not a scam but instead a valuable program to take care of the elderly.

With Social Security at the forefront of current discussions, hopefully this has shed some light on its finer points and has served as a useful guide against the misconceptions some people have about this useful government program.

Sources:

- (1)Memorandum on Deferring Payroll Tax Obligations in Light of the Ongoing COVID-19 Disaster
- (2) Historical Background And Development Of Social Security
- (3) What are the Trust Funds
- (4) Investment Holdings
- (5) How Social Security is Financed
- (6) Undocumented immigrants quietly pay billions into Social Security and receive no benefits
- (7) Social Security Administration, Stephen Goss 2013 report on Undocumented Immigrants
- (8) Status of Social Security and Medicare Programs
- (9) Trump weighs permanent payroll tax deferral, says it won't impact Social Security
- (10) Trump terminates payroll tax security?
- (11) General Revenue Social Security trust funds
- (12) [ssa.gov id-19-disaster/](https://ssa.gov/id-19-disaster/)

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