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Social Security and Other Entitlements



NEWS UPDATE

- 2022 Social Security recipients will receive a boost of 5.9% in benefits as a result of recent high inflation rates. This is the largest boost in 39 years (www.ssa.gov).
- Many eligible families missed out on the 2021 expanded Child Tax Credit because they didn't file federal personal income taxes. Even though the expansion has been terminated, people will have one last chance to request this expanded benefit when they file their 2021 tax returns. The expanded Child Tax Credit was estimated to reduce child poverty by half.

PURPOSE

This is the last of four chapters focused on social issues and government social programs, and we address the Social Security program, Medicare, and a few other entitlements. Terminology is important, insofar as Social Security and Medicare are universal entitlements, as opposed to public assistance programs. We also distinguish between social insurance programs and private insurance programs. As part of this discussion, it is important that students understand that while Social Security is *not* a public assistance program, it does prevent poverty among a lot of people who would otherwise be poor. The stereotype of the elderly poor largely belongs to the past. As we consider additional entitlements proposed by the Biden administration, we realize that many of these can also rightly be considered investments in human capital (or in human infrastructure — a more common term in today's politics). While Social Security is a popular program, our students are worried it may not be there for them when they retire. While this concern has been exaggerated, it is true that the major problem affecting the future of Social Security is the declining worker-to-beneficiary ratio. This problem, along with rising healthcare costs, will challenge the funding of the Medicare program as well.

WHAT'S NEW?

1. The Social Security program hasn't changed, but conservatives have been more outspoken about reducing it (especially in the context of the budget deficits created by the 2017 tax bill).
2. Future inflation will cause an increase in Social Security benefits, so you may want to watch for this.
3. Similarly, the Medicare program hasn't changed, though conservatives also have this program on their radar for reducing it. President Biden, on the other hand, sought to expand this program by adding hearing, vision, and dental coverage, though this met with resistance in Congress.
4. Medicare was addressed by the Democratic candidates for president back in 2020. You (but perhaps not your students) will recall Bernie Sanders's advocacy of "Medicare for All" (single-payer healthcare), and Joe Biden's more moderate call for expanding the Medicaid and the Affordable Care Act instead. This was mentioned in Chapter 7.

5. Upon entering the office of president, Joe Biden proposed three large spending bills, two of which passed by Congress (though the third did not). The American Rescue Plan and the Bipartisan physical infrastructure bill were huge expansions of government spending on items that included new universal entitlements (though some of these programs could not be defined as universal entitlements once an income cap was placed on them). The third bill, a human infrastructure bill, sought universal entitlements and other kinds of assistance programs that would vastly expand our nation's safety net, including items like two years of free pre-kindergarten and two years of free community college, paid sick leave and maternity leave, expanded childcare, continuation of the expanded Child Tax Credit, and others.
6. The text has expanded discussion of topics that have become more popular in recent times, including a universal basic income and various tax credits targeted to low-income households.
7. Finally, the clock continues to tick down as we watch the data and see a continued drop in the ratio of young workers relative to a growing elderly population. This, of course, projects difficulties for the future financing of Social Security and Medicare. Since immigrants tend to be relatively young, increased immigration can help solve this financing problem.

TEACHING SUGGESTIONS

➤ *Student Interest*

- Students worry about whether Social Security will “be there” for them, so they are interested in the sustainability of the program. This presents a good opportunity to talk about our aging population, and perhaps even discuss whether we should undertake efforts to try to turn it around (have more babies?). You can discuss the role played by typically young immigrants paying into the Social Security system, and you might note that illegal immigrants pay into Social Security but will never receive benefits. You can also discuss modifications that could be made to the Social Security system to make it more sustainable. Students may have some of their own ideas.
- Ask your students if they have any family members who rely on Social Security. Is the money they receive adequate to live on?
- Similarly, do your students have family members who receive Medicare? If so, is Medicare adequate for their needs, or do they pay for a supplemental insurance?
- Ask your students if they think there is stigma associated with receiving Social Security? Is there stigma associated with receiving food stamps? Is there stigma for children receiving reduced price school lunches? What is the difference among these? Is this fair?
- What share of the student's paycheck goes to Social Security? Discuss the regressivity of the Social Security tax and ways it could be made less regressive or not at all regressive.

➤ *Controversy*

Ask your students what they think about the following:

- The American Rescue Plan
- The Bipartisan Physical Infrastructure Bill
- The proposed Human Infrastructure Bill (Build Back Better)
- The U.S. safety net in comparison with that of other countries, such as Norway.

➤ *Economic Theory and Models*

- The negative income tax has been discussed among economists for decades. The newer concept of a universal basic income is very similar and is gaining favor among economists.
- Tax credits, including the Earned Income Tax, the Child Tax Credit, and the childcare tax credit can all be highly effective in reducing poverty.
- Investments in human capital, such as the proposed free pre-K and community college education, can be extremely cost-effective in current benefits and enhanced future productivity.

➤ *Fundamentals*

- What is the impact of the regressive Social Security tax on income distribution?
- What would be the impact of eliminating or privatizing Social Security on income distribution?

CLASSROOM EXERCISES

1. The last year Sarah worked, her earnings were \$20,000. Her Social Security retirement benefits are \$10,000 a year. What is her replacement rate? [50%]
2. Suppose the 2025 ceiling on earnings to be taxed for Social Security is \$200,000, the tax rate is 6.2 percent, and two different people have annual work earnings of \$60,000 and \$300,000. Also assume that the higher earner has an additional annual income of \$200,000 in the form of dividends and interest income, but the lower earner has no income other than the \$60,000 in work earnings. How much Social Security tax will be paid by the lower earner? [$0.062 \times \$60,000 = \$3,720$] By the higher earner? [$0.062 \times \$200,000 = \$12,400$] What share of total income will the lower earner pay in Social Security taxes? [$\$3,720 / \$60,000 = 0.062$] What about the higher earner? [$\$12,400 / \$500,000 = 0.025$] Clearly the Social Security tax is highly regressive.
3. Continue with the two earners in #2, but consider what would happen if, instead of a ceiling of \$200,000, a \$200,000 floor is established for the Social Security tax. This means that earnings below \$200,000 are not taxed, but all earnings above \$200,000 are taxed for Social Security. None of the lower earner's earnings would be taxed (it is below \$200,000), but \$100,000 of the higher earner is taxed (this is the excess in earnings above the floor of \$200,000). If we continue to assume non-labor sources of income are not taxed for Social Security, then what share of total income will be paid by the lower earner? [$0 / \$60,000 = 0$] How much Social Security tax will be paid by the higher earner? [$0.062 \times \$100,000 = \$6,200$] What share of total income will be paid by the higher earner? [$\$6,200 / \$500,000 = 0.012$] The tax is now progressive. (It would be even more progressive if non-labor income was taxed in addition to earnings.)

SAMPLE TEST QUESTIONS

Multiple Choice Questions

1. The reason the Social Security tax is regressive is:
 - a. only earnings from working are taxed for Social Security.
 - b. only earnings up to a ceiling are taxed for Social Security.
 - c. a large share of the income of higher income people is not taxed for Social Security.
 - d. all of the above**
2. When we say that the Social Security tax is a matching tax, we mean that:
 - a. the government doubles the amount that each worker pays.
 - b. both workers and their employers pay the Social Security tax.**
 - c. workers pay the tax twice, when they are paid and again when they file their tax returns.
 - d. the benefits a worker will receive are proportional to the taxes they paid in.
3. A major difference between social insurance and public assistance programs is that:
 - a. social insurance covers the entire eligible population, but public assistance covers only the needy.**
 - b. receiving social insurance benefits is widely regarded as shameful, but this is not so with public assistance.
 - c. social insurance is a statutory right, but public assistance is a contractual right.
 - d. social insurance is financed by general tax revenues, and public assistance is financed by earmarked payroll taxes.
4. When we say the Social Security tax is regressive, we mean that the tax takes a larger:
 - a. percent of the income from high-income workers than low-income workers.
 - b. amount of tax dollars from high-income workers than low-income workers.
 - c. percent of the income from low-income workers than high-income workers.**
 - d. amount of tax dollars from low-income workers than high-income workers.
5. The worker's retirement benefits as a percentage of their final working year's earnings is the:
 - a. benefit rate.
 - b. transfer rate.
 - c. entitlement rate.
 - d. replacement rate.**
6. Which of the following is a public assistance program?
 - a. Social Security
 - b. Medicare
 - c. Food stamps**
 - d. all of the above
7. The long-run problem of Social Security is that:
 - a. the system is going bankrupt.
 - b. the ratio of workers to recipients is declining.**
 - c. the trust funds are invested in junk bonds and other risky investments.
 - d. there are too many young people relative to old people in today's economy.

8. The argument that Social Security increases savings by encouraging early retirement is the:
- wealth effect.
 - replacement effect.
 - early retirement effect.**
 - savings effect.
9. The argument that Social Security decreases savings because it decreases the need to save privately for retirement is the:
- replacement effect.
 - early retirement effect.
 - dissaving effect.
 - Social Security wealth effect.**
10. Most of the revenues for Social Security come from the:
- general tax revenues paid to the federal government.
 - payroll taxes paid by workers and their employers.**
 - income tax paid on Social Security benefits.
 - interest on the Social Security trust funds.
11. Which of the following is correct?
- The replacement rate is higher for high-earning workers than low-earning workers.
 - Married workers are given the greater of retirement benefits on their own record or spousal benefits on their spouse's earnings record.**
 - The Social Security program only covers retirement not disability.
 - Public assistance benefits are based on the principle of individual equity.
12. Plans to partially privatize Social Security would reduce the Social Security tax and:
- require that workers establish investment accounts with the taxes saved.**
 - allow the Social Security Administration to invest in common stocks.
 - allow the Social Security Administration to invest in junk bonds.
 - allow workers to use the saved taxes for educational purposes.
13. Jane retires. The last year she worked, she earned \$30,000. Her social security benefits the first year after retirement total \$15,000. Her replacement rate is:
- 40%
 - 50%**
 - 60%
 - 200%
14. A tax takes \$1,000 from Joe, whose total income is \$10,000. The tax takes \$2,000 from James, whose income is \$100,000. The tax is:
- regressive.**
 - proportional.
 - progressive.
 - fair.

15. The idea that a social insurance program should put a minimum floor of income for the entire population is the:
- principle of individual equity.
 - principle of social adequacy.**
 - basis of capitalism.
 - basis of compassionate conservatism.
16. When Social Security is described as a pay-as-you-go system, it means that Social Security:
- cashes in government bonds each month to pay retirement benefits.
 - pays benefits out of the current taxes collected from people who are working.**
 - has to borrow to pay current retirees their benefits.
 - none of the above
17. Our largest social insurance program is:
- unemployment compensation insurance.
 - Medicaid.
 - Social Security.**
 - food stamps.
18. Why are the gaps in survivorship Social Security benefits primarily a women's issue?
- Women tend to live longer than men.
 - Women are still more likely than men to work in the home.
 - On average, men earn more than women.
 - All of the above**
19. Among the changes made to the Social Security program in 1983 was:
- decreasing the normal retirement age.
 - increasing the early retirement age.
 - increasing the normal retirement age.**
 - exempting Social Security benefits from income taxes.
20. The idea that a taxpayer who pays more Social Security taxes should receive higher retirement benefits is the:
- principle of individual equity.**
 - principle of social adequacy.
 - basis of capitalism.
 - basis of conservative philosophy.
21. Which of the following was part of the American Rescue Plan?
- Individual stimulus checks
 - Assistance to small businesses
 - Assistance to state and local governments
 - All of the above**
22. What is true about the bipartisan physical infrastructure bill and the human infrastructure bill?
- The physical infrastructure bill contains more traditional forms of infrastructure, such as roads and bridges.
 - One is an investment in physical capital whereas the other is an investment in human capital.
 - Both are investments intended to increase productivity.
 - All of the above**

23. Donald Trump supported the:
- 2017 tax bill.**
 - 2021 American Rescue Plan.
 - 2021 bipartisan physical infrastructure bill.
 - human infrastructure bill.
24. President Biden supported:
- the 2017 tax bill.
 - the 2021 American Rescue Plan.**
 - a physical infrastructure bill but not a human infrastructure bill.
 - all of the above
25. Which of the following is *not* a universal entitlement?
- food stamps**
 - a universal basic income
 - public education
 - Social Security

True / False Questions

- Since Social Security reduces poverty, it is considered a public assistance program. (F)
- Privatization means the transfer of assets or responsibility from the government to the private sector. (T)
- Social Security is similar to a private insurance program insofar as it is voluntary. (F)
- Social Security is similar to a private insurance program insofar as there is pooling of risk. (T)
- Social Security recipients live on a fixed income. (F)
- Universal entitlements are benefits that eligible people have a right to receive based on U.S. law. (T)
- In addition to retirement benefits, Social Security provides benefits for disabled workers and their dependents, and for survivors of deceased workers. (T)
- Payroll taxes are taken directly from a person's paycheck. (T)
- A "pay-as-you-go" system is one that collects taxes from workers and holds the money in a safe place until the time the worker receives Social Security benefits. (F)
- Although the Social Security payroll tax is regressive, Social Security benefits are progressive. (T)
- Social adequacy is the principle that benefits are sufficient to provide a minimum level of economic security to the population as a whole. (T)
- Social Security is a program for low-income workers only. (F)
- Public assistance programs are financed by earmarked payroll taxes. (F)
- The Social Security tax rate is the percentage of the tax base collected for Social Security. (T)
- To qualify for Social Security benefits, one (or one's spouse) must have worked and paid taxes on one's earnings. (T)
- Workers have a contractual right to Social Security benefits. (F)
- Earnings* refer only to that portion of a person's income obtained through working, whereas *income* includes all forms of money received. (T)

18. Social Security covers the entire eligible population and not just low-income people. (T)
19. Adverse selection is any situation in which the choices of insured persons lead to higher loss levels and costs. (T)
20. Social Security is a fully funded insurance system. (F)
21. Social Security is an entitlement to which eligible persons have a right by law. (T)
22. Because the taxpayer has a statutory right to Social Security benefits, Congress cannot unilaterally change the Social Security program. (F)
23. The purpose of both private and social insurance is the pooling of risk. (T)
24. An argument against making Social Security voluntary is that ultimately the costs per covered person would increase. (T)
25. There is a stigma attached to receiving Social Security benefits. (F)
26. The Social Security tax rate for workers is 6.2%. (T)
27. The combined Social Security tax rate for employers and employees is 12.4%. (T)
28. A public assistance program covers the entire population, whereas a social insurance program covers only the needy. (F)
29. If nothing is done to save it, Social Security will soon go bankrupt. (F)
30. Future retirees will be able to retire at age 60 and collect full Social Security benefits. (F)
31. The tax base for Social Security taxes is earnings from work *above* some specified level of earnings. (F)
32. The long-run problem of Social Security is the aging population. (T)
33. Social Security will likely go bankrupt within a few years. (F)
34. The tax base for Social Security is the maximum amount of an individual worker's earnings subject to the tax. (T)
35. Those on the economic right are more likely to support privatization of Social Security than those on the economic left. (T)
36. The immigration of young people to our country would help support our aging population. (T)
37. Economic liberals are more likely than economic conservatives to favor cuts in Social Security benefits. (F)
38. Medicare is a social insurance healthcare program for Social Security recipients. (T)
39. One problem with Medicare is that it may not provide full social adequacy. (T)
40. Medicare is facing rising healthcare costs as well as an aging population. (T)

Critical Thinking Questions

1. Some people suggest a way to make Social Security financially sound is to make it a means-tested program that would pay benefits only to people with relatively few assets and low income. Do you think this is a good idea?
2. Should Social Security be made voluntary? Why or why not?
3. What are the views of those of the economic left and those of the economic right on the Social Security program?