2021 Social Security Trustee's Report Released

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The 2021 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds was finally released on August 31, 2021. Normally, we have seen this report distributed in April of every year (the 2020 report was released on April 22, 2020). The news is not good – worse than prior reports.

What are the Social Security and Medicare Trust Funds?

Social Security: The Social Security program consists of two parts. Retired workers, their families, and survivors of workers receive monthly benefits under the Old-Age and Survivors Insurance (OASI) program; disabled workers and their families receive monthly benefits under the Disability Insurance (DI) program. The combined programs are referred to as OASDI. Each program has a financial account (a trust fund) that accumulates the Social Security payroll taxes that are collected to pay Social Security benefits. Other income (reimbursements from the General Fund of the U.S. Treasury and income tax revenue from benefit taxation) is also deposited into these accounts. Excess deposits that are not needed in the current year to pay benefits and administrative costs are invested (by law) in special Treasury bonds that are guaranteed by the U.S. government and earn interest. As a result, the Social Security Trust Funds have built up reserves that may be used to cover benefit obligations if payroll tax income is insufficient to pay full benefits.

Social Security is the foundation of most Americans' retirement security, and it is by far their single largest retirement income source. The Trustees sum up the magnitude of benefits from Social Security this way, "Social Security will play a critical role in the lives of 65 million beneficiaries and 176 million covered workers and their families during 2021."

Note that the trustees provide certain projections based on the combined OASI and DI (OASDI) Trust Funds. However, these projections are theoretical, because the trusts are separate, and generally one program's taxes and reserves cannot be used to fund the other program.

Medicare: There are two Medicare trust funds. The Hospital Insurance (HI) Trust Fund helps pay for hospital care (Medicare Part A costs). The Supplementary Medical Insurance (SMI) Trust Fund comprises two separate accounts, one covering Medicare Part B (which helps pay for physician and outpatient costs) and one covering Medicare Part D (which helps cover the prescription drug benefit).

Trust Funds to be Depleted Sooner Than Previously Expected

Social Security: The Social Security trustees have moved up, by one year, the date for which the projected depletion of Social Security's reserves will require payouts to be reduced. Now benefits will need to be reduced in **2034** rather than the previous guess of 2035, if nothing is done to remedy the problem. Medicare is still expected to exhaust its reserves by 2026, which is just **five years** from now.

The problem is pretty straightforward – outflows are higher than inflows. To quote the Social Security Trustees report, "Social Security's total cost is projected to be higher than its total income in 2021 and all later years. Social Security's cost has exceeded its non-interest income since 2010." The Trustees expect that the Social Security Old-Age and Survivors Insurance (OASI) trust fund will deplete its reserves by **2033** and the Social Security Disability Insurance (SSDI) trust fund by 2057. The theoretically combined trust funds will exhaust their reserves by **2034**, at which point current 54 year-olds reach the full retirement age and today's youngest retirees turn 75.

What does this mean to you? At that point, all beneficiaries will face a 22 percent, across-the-board, benefit cut, growing to 26 percent by 2095. Do you know anyone on Social Security who would enjoy having their benefit reduced by that much? We have no idea how our government will resolve the problem. One possibility is that they will look to protect the incomes of individuals who have no resources other than Social Security Income by reducing the Social Security Incomes for those who have additional resources. In other words, if you have other assets or incomes, you may see your Social Security Income benefits reduced by MORE than 22%.

Medicare: The outlook for Medicare is even worse. The Medicare Trustees project the Medicare Part A Hospital Insurance (HI) trust fund will run out of reserves in only five years, by 2026. Upon insolvency, Medicare Part A spending must be cut by 9 percent, with those cuts growing even more to 22 percent by 2045. The Trustees estimate the actuarial shortfall would require the equivalent of a 16 percent benefit cut, or 27 percent increase in the standard payroll tax rate to keep benefits at their current level.

When the Social Security trust fund is depleted, the government expects to be able to pay 78% of scheduled benefits, the report states. Experts who prepared the Social Security report said recent increases in inflation mean the cost-of-living adjustment for 2022 will be about 6%. A big jump from the 1.3% COLA awarded for 2021, and the largest in 38 years. In an article dated August 23, 2021, Forbes Magazine believes this increase could be as big as 6.2%. The Medicare "Part B" premium for outpatient coverage is projected to rise by $10 a month in 2022, to $158.50 under the report's intermediate assumptions.

Public Members: One concern that has existed now for many years is that the two positions on the Board of Trustees for Public Members have remained vacant. Trustees serve for four years, and their terms can be extended. President Obama, toward the end of his administration, re-nominated the incumbent public trustees for a second term. But with 2016 elections approaching, the Senate didn't take a final vote and the posts have been vacant ever since. President Trump also nominated Public Members, but the Senate did not act on those either. When the positions where created decades ago, it was believed that having non-governmental representatives could increase the diversity of outlook on the Board of Trustees.

What can be done?

All in all, there are serious concerns at the Social Security Administration. You may ask, why don't our politicians step up to resolve these issues? After all, this situation is like a train headed for a landslide – we can see the train wreck coming well down the track. The earlier action is taken, the less painful the solution will be.

Unfortunately, solving the problem is not that easy. Among politics, Social Security is sometimes referred to as "the third rail" – a reference to electrical rail systems where, in addition to the two weight bearing rails, there is a "third rail" that carries the electricity to power the engine. Touching the rail can be painful, if not deadly. Politicians who try to address the Social Security problem have to confront some constituency to either raise costs or lower benefits. That constituency then vocally opposes the farseeing politician and votes him or her out of office. We recommend reaching out to your Senators and Congressional Representative and nudging them towards a solution – sooner rather than later.

As the Social Security Trustee's report notes, "Implementing changes sooner rather than later would allow more generations to share in the needed revenue increases or reductions in scheduled benefits." We could not agree more.

What should you do now? When you do your next Financial Review with your advisor request that they do an alternate plan that shows at least 22% less Social Security benefit. Also consider making sure that you have fully factored in healthcare costs for retirement, perhaps adjusting the alternate scenario to show slightly higher healthcare costs to help you plan for what may be a reality in the near future. We will do our best to keep you updated with any changes that will affect you. Above all, keep safe and healthy!

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