

# What the Administration Proposes to Do with the Projected Budget Surpluses over the Next Five Years—and Beyond

**Summary, 2000-2004:** Under current law, the administration projects \$828 billion in budget surpluses over the next five years, with 86% of that (or \$714 billion) reflecting surpluses in the Social Security trust funds. The administration proposes to use \$138 billion of the projected five-year surplus for increased spending (mainly defense) and to devote \$96 billion to tax cuts for “universal savings accounts.” Counting the \$24 billion in added interest payments these spending increases and tax cuts entail (compared to using all the surplus for debt repayment), the proposed \$259 billion in total new spending and tax cuts would turn a projected \$114 billion non-Social-Security surplus into a deficit of \$145 billion. Nevertheless, the administration plan leaves \$569 billion in net surpluses available to pay down the national debt (or increase government assets).<sup>1</sup>

**Social Security (and Medicare):** The administration’s budget plan would, for the first time ever, devote Social Security’s surpluses (or at least most of them) to their intended purpose: reducing the national debt.<sup>2</sup> This pro-national-savings approach has been widely praised. But there is an additional and controversial twist to the administration proposal.

As current law provides, Social Security would, of course, be credited with the \$714 billion in surpluses it is projected to run over the next five years under current law.

On top of that, the administration proposes to make what it calls “contributions” to the Social Security and Medicare trust funds exactly equal to the \$569 billion in net budget surpluses it projects over the next five years—\$445 billion to Social Security and \$124 billion to Medicare. What these “contributions” mean—if anything—has generated much debate.

Some argue that the proposed accounting transfers to the trust funds have no economic substance. Indeed, the administration admits that “the transfers . . . do not require funding”

| 2000-04 surpluses (\$-billion)                        |               |
|---|---------------|
| <b>Current law surpluses:</b>                         | <b>\$ 828</b> |
| Social Security                                       | 714           |
| Rest of budget  | 114           |
| <b>Proposed new initiatives:</b>                      |               |
| Defense increase                                      | \$ 110        |
| Other spending increases                              | 28            |
| Universal savings accts.                              | 96            |
| Added interest on debt                                | 24            |
| <b>Total new initiatives:</b>                         | <b>\$ 259</b> |
| <b>Remaining surplus/deficit</b>                      | <b>\$ 569</b> |
| Social Security                                       | 714           |
| Rest of budget  | -145          |
| <b>Proposed uses of remaining surplus:</b>            |               |
| Reduction in natl. debt                               | \$ -380       |
| Increase in govt. assets                              | +189          |
| <b>IN ADDITION:</b>                                   |               |
| New IOUs to Soc. Sec.                                 | \$ +445       |
| New IOUs to Medicare                                  | +124          |
| Change in Social Security's claim on future resources | \$ +1,160     |

<sup>1</sup>The gross debt owed to the public would decline by only \$380 billion, because \$189 billion would be used to increase government assets—\$86 billion in direct student loans (owed by the public to the government) and \$104 billion in Social Security stock market investments. But the government’s overall balance sheet would improve by the full \$569 billion in remaining surpluses.

<sup>2</sup>Prior to 1983, Social Security was a pay-as-you-go system, with payroll tax revenues sufficient only to pay current benefits. But starting in 1983, Social Security payroll taxes were increased and benefits for better-off retirees were cut in order to build up trust fund reserves for the future. The idea was that by running a surplus, Social Security would add to national savings, which would lead to increased private investment, which would in turn raise the incomes of future workers so that they could afford the cost of future Social Security benefits. But implementation of this theory ran into immediate political trouble.

Rather than using the Social Security surpluses to reduce government borrowing, lawmakers diverted Social Security’s reserves to cover part of the cost of the giant regular budget deficits that President Reagan’s income tax cuts and defense build-up produced. This practice continued unabated through most of the 1990s. So, while Social Security trust fund reserves built up on paper, they did not lead to additional national savings.

—since they merely move money on paper from one government account to another. But the administration also says that these “contributions” of future budget resources to the Social Security and Medicare trust funds will extend the financial viability of these programs for many more years.

Supporters of the administration’s approach commend it as a politically potent reinforcement of the government’s moral commitment to maintain Social Security and Medicare benefits in the future—and to enact whatever eventual combination of general tax hikes, regular-budget program cuts or borrowing it takes to do so. But some critics counter that if that’s what the plan entails, then it will bankrupt the rest of the government in the long run. And still others wonder whether by muddying the concept of a trust fund built up from worker payroll taxes, the administration’s plan might actually reduce Social Security’s moral and political claim to resources in the future.

**Beyond 2004:** From 2005 to 2014, the administration projects ongoing large overall budget surpluses under current law—totaling \$4 trillion over the ten years. It proposes to devote 28% of those surpluses to increased spending and tax cuts, with the rest used to pay down the national debt or expand government assets. The debt owed to the public is predicted to fall from 50% of the gross domestic product in 1993 to only 7% by 2014. The administration also proposes to continue to double-credit the \$2.9 trillion in remaining projected surpluses over the ten years to Social Security and Medicare on top of the trust funds regular surpluses.

According to the administration, these enormous new infusions of government IOUs into Social Security on top of Social Security’s actual surpluses (and coupled with the plan to invest some trust fund assets in the stock market) will extend Social Security’s ability to pay currently scheduled benefits to the year 2055, compared to 2032 as projected under current law.

| <u>2005-2014 surpluses (\$-billions)</u>   |                 |
|--|-----------------|
| Current law projection   | \$ 4,026        |
| To increased defense & other spending  | 344             |
| To universal savings accts.  | 440             |
| To increased interest  | 362             |
| <b>Remaining surplus</b>   | <b>\$ 2,880</b> |
| <hr/>  |                 |
| <b>“Contributions” to Soc. Sec. &amp; Medicare (in addition to regular trust fund surpluses)</b> |                 |
| Social Security  | \$ 2,319        |
| Medicare   | 562             |
| <b>Total “Contributions”</b>   | <b>\$ 2,880</b> |

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