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Social Security Financial Status: How the 2021 Annual Report Addressed the Impact of the COVID-19 Pandemic

Background

Social Security is a self-financing program that in 2021 covers approximately 176 million workers and provides monthly cash benefits to over 65 million beneficiaries. It is the federal government's largest program in terms of both the number of people affected (i.e., covered workers and beneficiaries) and its finances. Social Security is composed of Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI), referred to collectively as OASDI.

The financial status of Social Security helps to determine the program's ability to pay fully scheduled benefits on time—that is, the ability to provide monthly payments to current and future beneficiaries. At a basic level, the financial status of Social Security is simply the relationship among revenues, cost, and the holdings in trust funds.

COVID-19

News articles during the Coronavirus Disease 2019 (COVID-19) outbreak and the ensuing recession highlighted potential ways that Social Security and its beneficiaries could be adversely affected. If the totality of pandemic-related events were to result in a worse-than-expected relationship between program revenues and cost, it would likely result in a sooner-than-anticipated date for trust fund reserve depletion (i.e., the date at which the program could not support full and on-time payment of scheduled benefits). Furthermore, conditions that negatively impact economic and demographic factors in the future could also result in a lower percentage of payable benefits (i.e., incoming revenues could support lower benefit levels than pre-pandemic conditions). Changes in other economic factors such as inflation—and changes in demographic and program factors—could have additional effects on program revenues, program costs, and the trust funds.

The Board of Trustees 2021 Annual Report acknowledges the continuing uncertainty regarding the long-term (75-year) impacts of the COVID-19 pandemic. Although the trustees assumed that “the pandemic will have no net effect on the individual long-range ultimate assumptions,” they further acknowledged their intent to “monitor developments and modify projections in later reports.”

The 2021 report did discuss many changes to the near-term (10-year) assumptions that were necessary to incorporate the potential effects of the COVID-19 pandemic. This report reviews how the most recent near-term projections—under the intermediate assumptions in Board of Trustees 2021 Annual Report—addressed the impacts of the COVID-19 pandemic on the financial status and how COVID-19-related projections have changed from previous reports and guidance.

Revenues, Cost, and the Trust Funds

Revenues for Social Security are generated primarily through taxes. In 2020, 93.2% of total income was from dedicated tax revenue: (1) payroll taxes paid by employers, employees, and self-employed individuals and (2) federal income taxes paid by about half of beneficiaries on a portion of their benefits. The remainder of the program's income came in the form of interest earned by assets held in the trust funds. *Costs* for Social Security primarily consist of benefit payments. In 2020, 99.0% of total costs went toward monthly retired-worker, disabled-worker, and dependent benefit payments.

The Social Security *trust funds* are an accounting mechanism used to track revenues and cost. The trust funds also provide a means to hold any accumulated assets (holdings). Currently, the combined Social Security trust funds hold about \$2.9 trillion in asset reserves that are available for future program spending. If, in any year, *costs* are greater than *revenues*, the cash-flow deficit is offset by selling some of the accumulated holdings of the trust funds to help pay benefits.

Changes that increase revenues, increase the trust funds, or decrease costs have a beneficial effect on the financial status. Changes that decrease revenues, decrease the trust funds, or increase costs have a negative effect on the financial status.

Long-Term Projected Shortfall

Over the long term, Social Security has an unfavorable relationship between projected revenues and projected cost. Costs are projected to increase faster than revenues, leading to projected cash-flow deficits starting indefinitely in 2021. The accumulated assets held in the trust funds can be used to augment revenues until 2034—the projected date of depletion for the trust funds. That is, trust fund reserves are projected to decline steadily from their current peak—\$2.9 trillion—to zero in 2034. At the time of depletion, incoming revenues would be insufficient to fully pay scheduled benefits.

The 2020 Annual Report (April 2020)

The trustees released the 2020 Annual Report on April 22, 2020, which reflected the trustees' understanding of the Social Security program at the beginning of 2020. Thus, it did not incorporate any potential effects of the COVID-19 pandemic. The trustees stated: “Given the uncertainty associated with these impacts, the Trustees believe that it is not possible to adjust their estimates accurately at this time.” The trustees went on to write that the magnitude of both near-term and long-range effects on the population and the economy was still too unclear.

Under the 2020 intermediate assumptions, the trustees projected a depletion date for the combined reserves held in the trust funds to be 2035. The actuarial deficit—the amount by which the payroll tax rate would have to be increased to support the level of benefits scheduled under current law throughout the 75-year projection period—was projected to be 3.21% of taxable payroll.

Updated Baseline for Actuarial Status (November 2020)

A memorandum released on November 24, 2020, by the Social Security Administration’s Office of the Chief Actuary presented an updated baseline for estimates of the effects of the pandemic and pandemic-induced recession on the program’s projected financial status at the time.

The update presented several new assumptions for the near term. With regard to demographic assumptions, the new baseline assumed lower fertility, lower immigration, and higher mortality. For economic assumptions, the new baseline assumed lower productivity, lower average wages, and higher unemployment, among other changes. The new baseline also assumed higher average disability incidence (i.e., new beneficiaries awarded benefits) and higher disability termination (i.e., beneficiaries no longer collected disability benefits due to recovery, age, or death). These updated assumptions combined to bring the project depletion date of the combined trust funds to 2034 (one year earlier than under the intermediate assumptions of the 2020 Annual Report). The updated assumptions also increased the actuarial deficit to 3.28% of taxable payroll.

The 2021 Annual Report (August 2021)

The trustees released the 2021 Annual Report on August 31, 2021. In their report, the trustees noted that the “projections presented include the Trustees’ best estimates of the effects of the COVID-19 pandemic and the ensuing recession, which were not reflected in last year’s report.” Further, the trustees stated, “The pandemic and precipitous recession have clearly had significant effects on the actuarial status of the OASI and DI Trust Funds, and the future course of the pandemic is still uncertain.”

Immediate Economic Effects

The 2021 Annual Report acknowledged that the “substantial” drop in employment, earnings, interest rates, and gross domestic product (GDP) that occurred in 2020 had a significant effect on the actuarial status of the trust funds. The trustees project that each of these factors will rise gradually until full recovery in 2023.

The trustees project “sustained moderate” economic growth (i.e., positive) after completion of the recovery (in 2023) from the COVID-19-induced recession. The trustees also project a permanent decrease of 1% in the level of worker productivity. Consequently, as worker productivity is an input of GDP, a permanent decrease of 1% is assumed for GDP as well. Thus, assuming a return to pre-COVID-19-pandemic trends in economic data, the trustees still project a permanently decreased GDP.

In addition to these economic assumptions, the trustees discussed changes to demographic assumptions. Some of the demographic changes are discussed below.

Near-Term Fertility Assumptions

The trustees project lower fertility rates in 2021 and 2022 but that in 2023, fertility would increase to the rate that would have been projected absent the COVID-19 pandemic. From 2024 to 2026, elevated birth rates would make up for the previous years’ lower rates before once again returning to rates that were projected to have been observed before the COVID-19 pandemic in 2027.

Near-Term Immigration Assumptions

Similar to delays in birth rates, the trustees project delays in immigration. Specifically, they project a decrease in total net immigration in 2021, while for 2022 they project no change from what would have been estimated absent the pandemic. Immigration for 2023-2025 is estimated to be higher and have an offsetting effect on the COVID-19-reduced immigration in earlier years.

Near-Term Mortality Assumptions

The trustees project increased mortality through 2023. For those 15 and older, the trustees estimate higher death rates through 2023 by about 7% more than what would have been estimated absent the pandemic. Death rates for those under 15 are estimated to decrease but to a lesser degree than the increase for those 15 and older. That is, the change in projected death rates between age groups do not offset each other. After 2023, death rates are assumed to return to levels estimated pre-pandemic.

COVID-19-Related Effects on the Financial Status

As stated in the 2021 Annual Report: “Taken together, these data and assumptions cause the reserve depletion date for the combined OASI and DI Trust Funds under the intermediate assumptions to change from 2035, shown in the 2020 report, to 2034 for this report. These changes also result in a small but significant reduction in the actuarial balance for the OASDI program.”

The 75-year actuarial deficit projected in the 2021 Annual Report increased to 3.54% of taxable payroll. In the 2020 report, the actuarial deficit was projected to be 3.21% of taxable payroll. (The updated November 2020 baseline estimated the actuarial deficit to be 3.28% of taxable payroll.) Thus, projections for the short-term effects of COVID-19 contributed to a sooner-than-anticipated depletion date and larger actuarial deficit.

Additional Resources

CRS In Focus IF10522, *Social Security’s Funding Shortfall*

CRS Report RL33514, *Social Security: What Would Happen If the Trust Funds Ran Out?*

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