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Social Security Tax Debate: A Fact Sheet

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Social Security Tax Rates

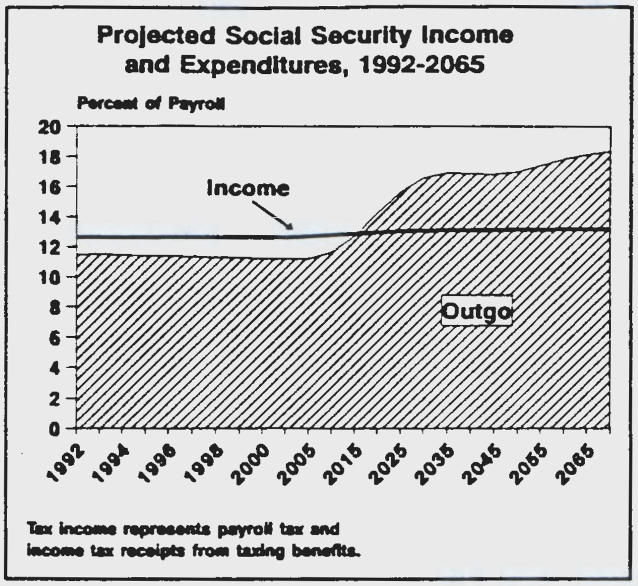
	Employee & employer, each	Self-employed*
Social security**	6.20%	12.40%
Hospital insurance	1.45	2.90
Total	7.45	15.30

* One-half of self-employment taxes are deductible for income tax purposes.

** Has two parts: one for Old Age and Survivors Insurance and another for Disability Insurance.

The social security tax rate is higher than needed to meet today's social security costs. The resulting excess taxes are deposited in the U.S. Treasury along with all other taxes and are accounted for through the crediting of Federal bonds and related securities to the social security trust funds. Various proposals offered by Senator Moynihan and others during the past few years to bring the rate more in line with actual costs reopened the debate about how social security should be financed and treated in the Federal budget and whether social security taxes should be cut to stimulate the economy. Senator Moynihan proposed a "pay-as-you-go" social security system under which the social security tax rate first would be cut from 6.2 percent (the current rate for employee and employer each) to 5.1 percent or 5.2 percent. Beginning in 2010, it would be raised gradually to an eventual level of 8.1 percent to keep pace with steep cost increases arising from the retirement of the post-World War II baby boomers and subsequent generations.

The debate: Support for the idea of cutting the tax rate originally arose from the complaint that surplus social security taxes were "masking" the Federal deficit and being spent on other programs. It also came from those who see social security taxes as regressive, some of whom wanted to force policymakers to consider increasing income taxes. Others contrasted a social security tax cut to cuts being sought in the capital gains tax--i.e., more tax relief would go to workers if social security taxes were reduced--and argued that a social security tax cut would increase consumer spending and thereby help stimulate the sluggish economy. Yet others contended that if the surpluses were allowed to continue, pressure would mount to liberalize social security benefits thereby adding to the system's long-range cost. They wanted to remove this temptation and, at the same time, give the public a clearer perception of the higher taxes the system will need in the next century to meet the benefits already promised under current law.



Critics pointed out that without making up for the revenue loss through spending reductions or increasing other taxes, the immediate reduction in social security revenues would increase the amount of money the Government must borrow from financial markets and thereby reduce the amount of resources available for private investment. They complained that the tax cut would impair the Nation's savings rate, already too low in the view of many economists. They asserted that the surplus social security receipts should be used to reduce the budget deficit on the grounds that the Government then would borrow less, making more money available for investment in the economy. With regard to the tax cut's immediate impact on the economy, they argued that the stimulative effects would be short-lived. They reasoned that the higher Government borrowing caused by the cut eventually would put pressure on financial markets and lead to higher interest rates. They further argued that if the economic assumptions upon which the tax cut were based proved to be optimistic, the system's financial solvency could be threatened.

Legislative action in the 101st and 102nd Congresses: Although the Senate leadership twice permitted Senator Moynihan to bring up his measure for a vote, once in 1990 and again in early 1991, both times it was set aside because of procedural objections (the first time because it violated rules under the budget act--it would have cut social security taxes without offsetting spending reductions or other tax increases--and the second time because of a tabling motion). Later in 1991, however, as the recovery from the recession weakened, new calls were made for tax cuts to stimulate the economy. Among them was a package of tax changes proposed by House Ways and Means Committee Chairman Rostenkowski that included income tax credits based on the level of one's social security taxes. Social security taxes were not to be affected directly. Early in 1992, the House passed a modified version of that package (H.R. 4210), including the tax credit idea. An alternative tax bill passed by the Senate did not include the proposal, but a scaled-down version of it was included in a compromise bill agreed to by House and Senate conferees. The proposal died, however, when President Bush vetoed the bill on March 20, 1992.

For additional information, see: U.S. Library of Congress. Congressional Research Service. *Social Security Tax Debate*. Issue Brief No. IB90033, by David Koitz and Geoffrey Kollmann. Updated regularly; and *The Social Security Surplus: A Discussion of Some of the Issues*. CRS Report No. 88-709 EPW, by David Koitz. Nov. 21, 1988.