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Your Accounting for a New Economy

Social Security:

What Does the Future Hold?

Each year, the Social Security and Medicare trustees issue a report on the financial health of these two programs. The news hasn't been good. According to this year's report, in 2016, Social Security will begin paying out more money than it takes in, and will be able to pay promised benefits only until 2037; afterwards, the trust fund reserves will be exhausted and payroll tax income will be enough to finance only 76% of scheduled benefits until 2083.

Social Security reform has been a political hot potato, but that may be about to change. The decline of the financial markets has led to renewed focus on the importance of Social Security income to retirees, and on the need to address the growing burden that Social Security is placing on the federal budget.

Proposals to stabilize Social Security

Despite fears that Social Security will not be around for future generations, there have been no calls to eliminate Social Security, and the focus is on making the program sustainable. In fact, President Obama has repeatedly expressed his commitment to preserving Social Security. To help accomplish this, he favors a Social Security payroll tax on earnings above \$250,000 (currently no Social Security payroll tax is assessed on earnings above a certain maximum, \$106,800 in 2009). Many other potential solutions have also been suggested. For example, the Social Security Solvency Act of 2009, introduced in the Senate in February, proposes accelerating by five years the gradual increase in full retirement age to 67, and modifying the benefit calculation to reduce benefit growth. This year's trustees report mentions immediately increasing the payroll tax or reducing benefits as additional options.

The near future

The Congressional Budget Office (CBO) is projecting that for the first time since 1975, when cost-of-living adjustments (COLA) were first payable, Social Security beneficiaries will not receive an automatic increase next year (or for 2011), due to low inflation. According to the CBO, the absence of COLA will also affect the maximum earnings that are taxable for Social Security, because under the Social Security Act, the earnings maximum can only increase when COLA is payable. Therefore, the CBO is projecting that this year's earnings base of \$106,800 will remain the same for the next two years.

Medicare beneficiaries will be affected too. By law, for individuals who have their Medicare Part B premiums withheld from their Social Security checks, premiums cannot rise more than COLA increases for Social Security. Consequently, no annual COLA means that standard Medicare premiums will remain at their current level of \$96.40 per month for approximately 75% of Medicare beneficiaries. However, certain beneficiaries (those who do not have their premiums deducted directly from Social Security and those with higher incomes who pay higher income-related premiums) do not have this protection, and will see their premiums rise, perhaps substantially.

Stay informed

Most Americans rely on Social Security for at least a portion of their retirement income, but to ensure that Social Security will be able to pay promised benefits for many years to come, it's clear that the program must change. It's a good idea to follow the news to learn about legislative developments and model various income scenarios when developing your own retirement plan.