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Social Security, Medicare benefits outweigh taxes you paid

By Louis Jacobson, February 3, 2013

Last week, we published a story and several charts showing that average government spending on each elderly person is $26,355, compared to $11,822 for each child. Almost immediately, readers wrote to condemn us for overlooking what they considered a key issue.

"Your statements as to expenditures on the elderly is specious at best, and at the least, completely misleading," said one representative letter. "As you point out, most of the government spending on the elderly are Social Security and Medicare payments. These are not payments, but 'repayments' of money that we have been forced to hand over to the government to fund a Ponzi scheme during our working lives. It is not expenditures on the elderly — it is a partial refund of money we have been forced to hand over."

We thought this reader, and others, raised an interesting question: Are Social Security and Medicare payments actually a "partial refund" of what the beneficiary has already paid in? So we took a closer look.

The Urban Institute, a non-partisan research institute in Washington, D.C., produces statistics on this topic annually. Institute researchers figured out what people turning 65 in various years have already "paid in" to the system and what can expect to "take out" after they reach age 65.

Because marital status and family income can significantly affect both the amount paid in and the amount paid out, the institute offers its calculation for various types of family units. To make the final amounts comparable to what might have been done with the tax money had it been invested privately, the institute adjusted all dollar figures at 2 percentage points above the rate of inflation. (The authors note that different assumptions for long-term returns on investment would change the results.)

According to the institute's data, a two-earner couple receiving an average wage — $44,600 per spouse in 2012 dollars — and turning 65 in 2010 would have paid $722,000 into Social Security and Medicare and can be expected to take out $966,000 in benefits. So, this couple will be paid about one-third more in benefits than they paid in taxes.

If a similar couple had retired in 1980, they would have gotten back almost three times what they put in. And if they had retired in 1960, they would have gotten back more than eight times what they paid in. The bigger discrepancies common decades ago can be traced in part to the fact that some of these individuals' working lives came before Social Security taxes were collected beginning in 1937.

Some types of families did much better than average. A couple with only one spouse working (and receiving the same average wage) would have paid in $361,000 if they turned 65 in 2010, but can expect to get back $854,000 — more than double what they paid in. In 1980, this same 65-year-old couple would have received five times more than what they paid in, while in 1960, such a couple would have ended up with 14 times what they put in.

Such findings suggest that, even allowing for inflation and investment gains, many seniors will receive much more in benefits than what they paid in.

Jagadeesh Gokhale of the libertarian Cato Institute says it's possible to quantify exactly how much has been spent on beneficiaries beyond what they paid in, using an obscure line in the massive 2012 report of the Social Security trustees.

In wonk-speak, the figure he's referring to is the "closed-group unfunded obligation estimate for the Social Security program." In layman's terms, it's the inflation-adjusted dollar value of benefits paid — beyond the participants' tax payments — for all past and current beneficiaries by the time of their death.

According to this calculation, past and current generations will pay $71.3 trillion in payroll taxes but will receive $93.4 trillion in benefits. Adjusting for past and future transfers from the federal Treasury, the difference between "paid-in" and "paid-out" works out to $21.6 trillion.

"The $21.6 trillion number will change as soon as we change policies whereby today's generations pay more taxes or surrender some benefits," Gokhale said.

"But until that happens, the exhortation that today's generations are just getting what they are due based on their forced past tax payments is incorrect. 'We' are to get much more under current Social Security laws — to the tune of $21.6 trillion — than we'll pay into the system. The excess benefits are a 'return' on past and current generations' taxes of $71.3 trillion — and quite a handsome return it is!"

We should note a few caveats and complications.

First, this $21.6 trillion figure only addresses Social Security, not Medicare. And as it happens, there are some differences between how the two programs fare in the institute's calculations.

For an average-wage-earning, two-income couple turning 65 in 2010, the pay-in, pay-out ratio for Social Security by itself will actually be slightly negative —- the couple will have paid $600,000 in lifetime Social Security taxes and will receive only $579,000 in lifetime Social Security benefits. (Remember, the couple didn't literally pay out $600,000; that's the current value of what they paid out over the years, plus an additional 2 percent they may have gotten had it been invested.)

And even so, the Social Security shortfall will be more than evened out by the extra dollars the couple gets back from Medicare. The couple will have paid $122,000 in Medicare taxes but will receive $387,000 in benefits — more than three times what they paid in.

In addition, Timothy Smeeding, a public policy professor at the University of Wisconsin, notes that when judging Social Security, it's not just a question of dollars paid out, but also the intangible benefits bestowed. The program's future benefit checks provide a sense of financial security for one's retirement years, and beneficiaries get coverage for disability and survivors' insurance throughout their entire working careers. Such insurance would otherwise have to be purchased commercially.

"If you are 65 and crowing that you didn't get your money's worth, then you were lucky to never have used the other two parts of the safety net — disability insurance and survivor's insurance," Smeeding said.

Finally, the Urban Institute notes that, in a practical sense, Americans aren't paying their Social Security tax dollars into a personal account and then taking those dollars out, plus interest, once they retire. While there is technically a modest Social Security trust fund, the federal government has long paid out most Social Security revenues to beneficiaries, leaving the government and future workers with what amounts to an IOU to cover the next generation of beneficiaries.

The taxes paid by active workers help support today's generation of retirees — which is a big reason why some policymakers are concerned about the program's long-term solvency. In 1950, the average American lived for 68 years and retirees were supported by 16 active workers. Now, the average life expectancy is 78 and just three workers support every retiree.

By the time today's middle-aged workers reach retirement age, only two workers will be around to support their benefits. Promised benefits will exceed revenues by about 30 percent, and there will be no money in the trust fund to rely on.

Thus, Social Security is — and always has been — a transfer system from younger generations to older generations.

"We're not really entitled to get our money back since we didn't save it but rather spent it on our parents," said C. Eugene Steuerle, who helped assemble the Urban Institute's calculations. "Moreover, when 'things happen,' like a decline in kids per adult, society has to adjust regardless."