Next in Line for a Bailout: Social Security

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Don't look now. But even as the bank bailout is winding down, another huge bailout is starting, this time for the Social Security system.

A report from the Congressional Budget Office shows that for the first time in 25 years, Social Security is taking in less in taxes than it is spending on benefits.

Instead of helping to finance the rest of the government, as it has done for decades, our nation's biggest social program needs help from the Treasury to keep benefit checks from bouncing -- in other words, a taxpayer bailout.

No one has officially announced that Social Security will be cash-negative this year. But you can figure it out for yourself, as I did, by comparing two numbers in the recent federal budget update that the nonpartisan CBO issued last week.

The first number is $120 billion, the interest that Social Security will earn on its trust fund in fiscal 2010 (see page 74 of the CBO report). The second is $92 billion, the overall Social Security surplus for fiscal 2010 (see page 116).

This means that without the interest income, Social Security will be $28 billion in the hole this fiscal year, which ends Sept. 30.

Why disregard the interest? Because as people like me have said repeatedly over the years, the interest, which consists of Treasury IOUs that the Social Security trust fund gets on its holdings of government securities, doesn't provide Social Security with any cash that it can use to pay its bills. The interest is merely an accounting entry with no economic significance.

Social Security hasn't been cash-negative since the early 1980s, when it came so close to running out of money that it was making plans to stop sending out benefit checks. That led to the famous Greenspan Commission report, which recommended trimming benefits and raising taxes, which Congress did. Those actions produced hefty cash surpluses, which until this year have helped finance the rest of the government.

But even then, it was clear the surpluses would be temporary. Now, years earlier than projected, Social Security is adding to the government's borrowing needs, even though the program still shows a surplus on paper.

If you go to the aforementioned pages in the CBO update and consult the tables on them, you see that the budget office projects smaller cash deficits (about $19 billion annually) for fiscal 2011 and 2012. Then the program approaches break-even for a while before the deficits resume.

Social Security currently provides more than half the income for a majority of retirees. Given the declines in stock prices and home values that have whacked millions of people, the program seems likely to become more important in the future as a source of retirement income, rather than less important.

It would have been a lot simpler to fix the system years ago, when we could have used Social Security's cash surpluses to buy non-Treasury securities, such as government-backed mortgage bonds or high-grade corporates that would have helped cover future cash shortfalls. Now it's too late.

Even though an economic recovery might produce some small, fleeting cash surpluses, Social Security's days of being flush are over.

To be sure -- three of the most dangerous words in journalism -- the current Social Security cash deficits aren't all that big, given that Social Security is a $700 billion program this year, and that the government expects to borrow about $1.5 trillion in fiscal 2010 to cover its other obligations, about the same as it borrowed in fiscal 2009.

But this year's Social Security cash shortfall is a watershed event. Until this year, Social Security was a problem for the future. Now it's a problem for the present.