



## Arcane but Important

The federal budget surplus for fiscal year 1998 produced glee in some quarters, but others have gloomily observed that, without Social Security surpluses, a river of red ink would still be pouring from Washington. The distinction sounds esoteric, but much of the confusion surrounding the issue stems from the appearance of smoke and mirrors in the accounting. The basics of the accounting are, in fact, rather simple.

First, what are Social Security surpluses? As with any defined-benefit pension plan, Social Security receipts (mostly taxes and interest income) do not typically match expenditures (mostly benefits). Recently, receipts have exceeded expenditures (see chart). A private pension plan buys assets when it has a surplus. So does the Social Security system. There are legal restrictions on the portfolio of a private pension plan, but the restrictions are much tighter for the Social Security trust funds; they are allowed to buy only U.S. Treasury securities. In terms of accounting, this restriction has no effect on the total indebtedness of the U.S. government. If the rest of the federal government runs a \$10 billion dollar deficit, it must raise \$10 billion by selling securities. The rule only affects who ends up holding particular assets—the trust funds or the public.

So how do trust fund operations show up on the government's books? Consider the first column in the table on page 17. This is the total indebtedness of the U.S. Treasury. Taxpayers will ultimately have to pay off this amount (minus most of what is held by Federal Reserve Banks). Some will be paid to people redeeming bonds, some to Social Security recipients and beneficiaries of the other trust funds. At the end of fiscal 1998, the Social Security trust funds held assets worth \$730 billion, an increase of \$99 billion over the end of fiscal 1997. This \$730 billion shows up as part of the 1997 entry in the second column. Thus, Social Security surpluses are a big part of the gap between the two lines in the "Change in Federal Debt" chart—

about two-thirds of it in fiscal 1997.

Apart from a few minor accounting issues, the official (unified) budget deficit is the change in the third column, debt held by the public.

So much for the accounting. Is the unified budget deficit economically meaningful, or should we exclude trust fund surpluses and look at change in total debt instead? The unified deficit captures the impact of current federal borrowing on credit markets; it is how much the federal government borrows from everybody else. Some economists view this statistic as a measurement of how much private borrowers are "crowded out" and believe that crowding-out is important for current economic performance. That conclusion is controversial among economists, however. Looking at the change in total debt, on the other hand, gives a bit better reading on how current policies change taxpayers' future liabilities. But it is no substitute for careful policy analysis; many policies have little immediate effect on receipts, outlays, or borrowing but can hit hard in the long run.

—Joseph A. Ritter

Surplus of Social Security Trust Funds

