



# Social Security Choice

## ***SOCIAL SECURITY THIS WEEK***

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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### ***Post/ABC Poll: Individual Account Support Still Strong***

Despite a relentless assault by opponents, including the AARP, some Congressional Democrats, and the media, a substantial majority of Americans continues to support proposals to allow younger workers to privately invest a portion of their Social Security taxes through individual accounts, according to a new *Washington Post/ABC News* [poll](#). (registration required). According to the poll of 1,007 adults, taken January 12-16, Americans support individual accounts by a margin of 55 to 41. Not surprisingly, results were sharply split by age, with 71 percent of those 30 and younger and 65 percent of those under age 45 supporting the idea, but only 35 percent of seniors backing individual accounts. Republicans (75 percent) and Independents (55 percent) strongly backed accounts, but there was also surprisingly strong support among Democrats (41 percent).

Support for individual accounts is driven in part by the widespread belief that Social Security will not be able to pay promised future benefits. Fully 60 percent of Americans say that “there will not be enough money in the system to pay you the benefits you are entitled to.” Young people overwhelmingly believe that Social Security will not be there for them (80 percent of those 30 and younger and 75 percent of those under 45 say Social security will not have enough money to pay promised benefits).

Support for another widely discussed Social Security reform, changing the benefit formula from wage indexing to price indexing was more mixed. Although the question was phrased in an extremely negative way (asking about “reduc[ing] the rate of growth in guaranteed benefits for future retirees by up to one and a half percent a year.”), Americans were equally divided on the idea, 47 percent supporting, 48 percent opposed. Interestingly, young people who were most likely to be affected by such a change backed the proposal (57 percent support), while seniors, who would not be affected, opposed it (52 percent against). However, when the price-indexing proposal was combined with a proposal for individual accounts, support rose to 54 percent, with support again driven strongly by younger Americans, with 72 percent of those 30 and under backing the idea. This suggests that support for individual accounts is so strong among younger

Americans that they are willing to accept reductions in traditional Social Security benefits in exchange for being able to privately invest some of their Social Security taxes.

### ***Rep. Thomas Wants Wide-Ranging Entitlements Debate***

Rep. Bill Thomas (R-CA), chairman of the House Ways and Means Committee, wants to tackle a wide variety of entitlement reform issues during Congress' next term, according to the [Los Angeles Times](#) (registration required), and personal accounts for younger workers are a good start. In a symposium sponsored by the *National Journal*, Thomas said that Congress has a rare opportunity to consider a wide range of looming problems and formulate a comprehensive approach to reforming Social Security and Medicare.

Thomas called for examining the payroll tax itself and whether it should be adjusted or replaced by a different kind of tax. Congress may also want to consider whether women and men should get equal Social Security benefits, given that the gap between women's and men's longevity is increasing. Lawmakers should determine whether the retirement age needs to be changed. Medicare reform should accompany any plan to reform Social Security, since its rising costs are pushing the program toward insolvency.

This broad debate on Social Security, Medicare, and other retirement issues should be marked by a spirit of bipartisan cooperation, said Thomas. "My hope is that as we look at what we're doing, we will address the problems of today and tomorrow. I hope that we don't fight the political and ideological wars of yesterday." Thomas also warned Democrats not to play these issues for short-term political gain.

If a plan is introduced that "cannot, given the politics of the House and the Senate, be placed on the president's desk, every breath that's spent on discussing that plan is an attempt to lay a political ground war for the next election," Thomas said. "Save those breaths. Talk about what we need to do now that the president's plan is on the table so that we can address, in a legislative way, a solution on a bill the president can sign."

### ***Cheney Outlines Reasons for Social Security Reform***

Last week, Vice President Dick Cheney [delivered a talk](#) at Catholic University in Washington D.C. to announce the administration's plan to overhaul Social Security and broadly outline a proposal for reform. Cheney quickly identified the root problem facing Social Security: "With an aging population, and a steadily falling ratio of workers to retirees, the system is on a course to eventual bankruptcy." After serving seniors well for nearly 70 years, the current system is simply unsustainable.

Cheney elaborated on the guiding principles behind the administration's efforts. First among them is fairness: there will be no benefit cuts for seniors at or near retirement

age. Second is the avoidance of payroll tax increases. The problem cannot be fixed by increasing taxes, Cheney said, and doing so would only put a damper on economic growth. Most importantly, the administration wants younger workers to have the option of diverting some of their payroll taxes into personal accounts to be invested in securities. Personal accounts would help bridge the unfunded liability of the current system and foster “upward mobility and individual independence.” Personal accounts are a cornerstone of Bush’s broader mission to create an ownership society, and they would give many more people an opportunity to build wealth that they can pass on to their children, said Cheney.

The vice president also addressed several criticisms of personal accounts in his speech. The primary argument against them, he said, is that they are too risky. But this should not be a major concern, as basic guidelines and regulations will ensure the financial soundness of all investment choices, much as they do currently with the government’s Thrift Savings Plan. Cheney also corrected the misconception that Bush wants to make personal accounts mandatory; in fact, they will be entirely voluntary. He addressed the challenge that the transition costs will be too high. In reality, Cheney pointed out, the costs of doing nothing or delaying action will far exceed those of tackling the problem now. The Bush administration realizes that the elderly deserve to grow old with dignity and security, and is committed to reforming Social Security for those ends.

### ***Jonathan Rauch: Social Security Reform Is a Moral Issue***

While Social Security reform has important economic and political ramifications, the idea of personal retirement accounts is primarily a moral issue—a question of values, argues Jonathan Rauch in the [\*National Journal\*](#). Rauch quotes Michael Tanner, director of Cato’s Project on Social Security Choice, who says that private accounts will encourage a culture of personal savings and responsibility and reduce the class warfare that plagues our current political system. Excerpts from Rauch’s article follow.

“Earlier this month, a White House aide named Peter Wehner (director of strategic initiatives) sent selected conservatives a memo making the case for Social Security reform. ‘We consider our Social Security reform not simply an economic challenge, but a moral goal and a moral good,’ he wrote. ‘If we succeed in reforming Social Security, it will rank as one of the most significant conservative governing achievements ever.’

“The emphasis was revealing. The memo had little to say about long-term growth and other economic effects of reform. It stressed moving ‘away from dependency on government and toward giving greater power and responsibility to individuals.’ At the libertarian Cato Institute, Michael Tanner, the director of the project on Social Security choice, makes the same case. ‘We’re changing fundamentally the relationship of people to their government,’ he says. It would be ‘the biggest shift since the New Deal.’

”Bingo. Once you cancel the zeros on both sides of the equation, neither creating private Social Security accounts nor ratcheting down the growth of future benefits would be an economic milestone. Conservatives need to frame Social Security reform as a dollars-and-cents issue, but that is not really why they are excited. What they really hope to change is not the American economy but the American psyche.

“Conservatives used to speak derisively of liberal social engineering. The attempt to create private Social Security accounts is, so to speak, conservative social counter-engineering. Government should help provide for unforeseeable contingencies: tsunamis, unemployment, open-heart surgery. But if there is one event in all of human life that is wholly foreseeable, it is the advent of old age. Why, then, shouldn’t people save for their own retirement, instead of relying on welfare from the government—which is what Social Security, as currently constituted, really is?

“Tanner argues that people who own assets behave differently and see their place in society in a different light. Private accounts, he says, would encourage a culture of saving and personal responsibility; they would discourage political class warfare; they may, he argues, improve work habits, and even reduce crime and other social pathologies. Create private Social Security accounts, and millions of low-income Americans will be stockholders and bondholders. Republican political activists look at the way portfolio investors vote—and salivate at the prospect of millions more of them.

“The 2004 exit polls suggested, to many conservatives, that ‘moral values’ won the election for Bush. It may seem odd, then, that his boldest post-election priority is not abortion or gay marriage or schools, but Social Security. The key to the paradox is that Social Security reform is not, at bottom, an economic issue with moral overtones. It is a moral issue with economic overtones.”

### ***WSJ: Private Accounts Are What the Doctor Ordered***

President Bush will revisit his primary domestic goal of building an “ownership society” in his inaugural address, and despite protestations from some quarters of the Democratic Party, Bush is only trying to save and strengthen a program that was once the cornerstone of the New Deal, says George Melloan in a *Wall Street Journal* [op-ed](#) (subscription required). Young workers today face the prospect of higher payroll taxes, reduced benefits, or both, unless Congress can pass into law a proposal that will change the structure of Social Security from a pay-as-you-go system to a funded one.

Furthermore, common criticisms of personal accounts don’t withstand scrutiny, says Melloan. Excerpts from his piece follow.

“Defenders of the 70-year-old status quo cry that the system isn’t broke. It isn’t, but only because of past increases in the payroll tax. The Bushies respond that another such fix will be necessary to keep it solvent in a few years, so why not go for a permanent solution? At that, the cohorts of Teddy Kennedy, who enjoys the benefits of a huge fortune built by a market-savvy father, raise the ‘risk’ goblin. What if the market crashes and the worker is left with nothing? That’s nonsense. The accounts will be restricted to conservative investments, so don’t worry about workers taking flyers on dot-coms with no earnings.

“It would be unbelievable if a funded system got a lower return than today’s unfunded system, which has no return at all. John P. Meehan, a retired pension-fund manager in Orlando, Fla., has taken the trouble to examine payouts on stocks and bonds over 40-year spans that constitute normal working careers. The first such span he checked was from 1871 to 1911.

“‘It could be that the value of a retirement fund would return less than the total amount put in,’ he writes, ‘but that has never happened in the 89 consecutive years from 1911 to 1999. To alleviate such worry, an insurance policy against such an event could be purchased for a small premium or could be self-insured by the government through a reserve fund set aside for that purpose.’ Indeed, the government would be quite safe in providing a guaranteed minimum return when you consider how much a funded system could be expected to grow.

“The fallback argument is that there would be huge transition costs. Setting aside some of the payroll taxes for personal accounts would cut into Social Security’s cash flow. That would depend on how much was set aside. But the prospect of having to finance that cash-flow shortage doesn’t seem to worry Wall Street, the industry that would be most affected by a sharp rise in federal borrowing.

“To the contrary, Treasury Secretary John Snow told a group of *Journal* editors in New York last week that results of his visits on the Street just before he arrived were universally favorable. Wall Street, he said, is always happy to fund short-term obligations designed to reduce a long-term obligation. And make no mistake, the promises the government has made to future retirees are long-term obligations just as surely as the 30-year bonds Uncle Sam issues, even though they are off-budget. Moreover, there are other big promises out there, like Medicare, that make it all the more important to get some of those obligations off the table.

“Present retirees, getting scare messages from the avowedly ‘nonpartisan’ American Association of Retired Persons, need not worry either. As Mr. Snow said, anyone over 55 can simply ignore whatever changes are made. They won’t be affected. He notes in passing that AARP doesn’t seem to have a compunction about selling mutual funds to its members, one of its many money-making ‘nonprofit’ sidelines. AARP’s claim to speak for all its members, by the way, is a bit like Merrill Lynch claiming to represent all its account holders or GM everyone who drives a Chevy.”

## **White House Adviser Mankiw: Don't Buy Naysayers' Rhetoric**

A top White House economic adviser charged this week that anyone who opposes Bush administration plans to reform Social Security was being willfully ignorant about the problems of the current system. Gregory Mankiw, chairman of the Council of Economic Advisers, said that “the sophistry of those opposed to reform” should be avoided because it denies the real problems facing Social Security. “Reasonable people can debate what kinds of reforms are best, but don't let the ‘Ostrich Caucus’ convince you to put your head in the sand,” Mankiw [said](#). Under current law, he says, the benefits promised for future generations are “...empty promises. Unless a listener is discerning, empty promises will always have a superficial appeal.”

## **SS Trust Fund: Not a Myth, But Not the Answer**

Larry Eichel of the *Philadelphia Inquirer* takes a [closer look](#) at the Social Security Trust Fund and concludes that the trust fund, while not the worthless entity that some have claimed, is not the answer to Social Security's long-term solvency. The real trust fund exists only in electronic form and consists of U.S. Treasury bonds that are essentially IOU's. The trust fund has value because the government guarantees the bonds and has never defaulted on its debts. The problem is that there is no money set aside to pay for them. When it comes time to start tapping the trust fund to make Social Security payments, the government will have to figure out a way to make good on the bonds. The impact on the federal budget will be enormous.

The trust fund cannot be salvaged because the government has no way of simply saving money for future use; the best it can do is buy bonds from itself, which are problematic for the reasons detailed above. So while the trust fund is not a myth, it is a fundamental flaw of the Social Security system, and any long-term solution for fixing Social Security must do away with it. Excerpts from the article follow.

“Understanding the trust fund is essential for assessing the urgency of the case for remaking the federal retirement system. Invariably, Social Security's timetable for distress is expressed in terms of when the fund has to be used and when it runs dry.

“So do the bonds in it have any financial value?

“For all the rhetorical obfuscation in the Social Security debate, there is little dispute among experts over some basic aspects of the trust fund.

“They agree that the fund has real value, if only because the government says it does, and that it carries a real price.

“In a report last year, the Congressional Budget Office called the trust fund mainly an ‘accounting mechanism’ that contains ‘no economic resources.’ It described the bonds as legal commitments to pay, as opposed to the ability to do so. All of which has been said by other agencies in other years.

“Yet those commitments are of great significance, even if they do represent promises (IOUs) made by one part of the government to another. Such commitments are the basis on which all government securities are issued. Not to honor the pledges would amount to default.

“One way or another, the bonds will have to be honored. But there is no money set aside to pay for them.

“When the bonds come due, the government will have to adjust its finances by reducing other spending, increasing other borrowing, or raising other taxes. There are no other options.

“As early as 2022, the impact on the federal budget would be the equivalent of what it costs to run a half-dozen major government departments, according to Michael Tanner, director of the Cato Institute’s Project on Social Security Choice.

“In any event, the federal government has no mechanism through which it can save money for later use, at least not in a way that makes sense to people who aren’t economists.

“So the trust fund continues to exist and grow, with government bonds its only holdings.

“What happens to the fund if Social Security is changed?

“Some proposals involving personal accounts would draw down the fund more quickly than under current projections; others wouldn’t affect the schedule. Most plans involving new taxes and benefit cuts would extend the fund’s life.

“The fund, then, is neither a joke nor a hoax. But it’s not Social Security’s long-term salvation either, no matter how many pieces of paper there are in that file drawer in West Virginia.”

### ***Thomas Sowell: No Magic Bullet for Social Security***

Some critics of President Bush’s plan to reform Social Security claim that there is no Social Security “crisis.” Others concede that Social Security does face long-term problems, but that personal retirement accounts aren’t a “magic bullet” solution. But, as Thomas Sowell writes in his most recent [column](#), no public policy is a panacea or perfect cure-all. Policymakers are faced with comparing different policies and choosing the best alternative to the current system. And personal accounts are the best alternative to the existing Social Security system for many reasons, Sowell explains. His column follows.

“The latest liberal spin on Social Security is that there is no problem. Of course, there is no problem with any obligation if you are willing to welsh when it comes time to pay it.

“Politically, the bottom line of this approach is that President Bush’s plan is ‘not a magic bullet,’ in the words of Businessweek magazine. When people start talking about how

this or that policy 'is no panacea' or 'not a magic bullet,' then you know their argument is not serious.

"Why don't we all stipulate, once and for all, that no policy on any subject, anywhere or anytime, is a panacea or a magic bullet. Then we can start talking sense like adults.

"If we are serious, we can compare one alternative to another, instead of comparing one alternative to perfection. What is different with the private retirement accounts that the President is proposing, compared to the Social Security system as it exists now?

"The biggest difference seems to get the least attention: With private accounts, money is invested in the economy, creating additional wealth, from which pensions can be paid. With Social Security, the money is spent as soon as it gets to Washington.

"Is it better to invest for the future or to keep spending the Social Security taxes now and leave it to someone in the future to figure out what to do when today's young workers retire and there is not enough money to pay them what they were promised?

"Many people are unaware that the money that is taken out of their paychecks for Social Security is not—repeat, not—being put aside to pay for their retirement. That money is paying for people who are retired right now, and anything that is left over is being spent by politicians in Washington for anything from farm subsidies to Congressional junkets.

"There is a legal and accounting fiction called the 'Social Security Trust Fund.' All that this means is that the Social Security system gets government bonds in exchange for the Social Security tax money that is being spent today instead of being saved. But you cannot spend and save the same money, no matter what accounting gimmicks you use.

"Government bonds are not an investment that adds to the country's wealth. They are a claim on future taxpayers. Without those bonds, future taxpayers would still be on the hook to provide the money to cover future Social Security pensions that are not covered by future Social Security taxes. The bonds change nothing.

"The other big difference between privatized pensions and Social Security is that the individual owns the pension he has paid for. This is not a fine philosophical distinction but a major practical difference.

"No matter what the law says or promises when you pay your Social Security taxes, Congress can pass a new law changing all that any time they want to. They have already done it and those who say that there is no problem with Social Security also say, as Businessweek does, that 'tax hikes' and a 'reduction of the benefit' can fix the Social Security problem.

"Of course it can. If you owe a million dollars, that is no problem, if you can decide to pay it off for whatever amount you can comfortably afford. It is just that most creditors take a much narrower view of the situation.

“If I tell the bank that I can’t afford to make the mortgage payment because my income is not as high as I thought it would be, they are going to throw me out in the street and take the house.

“But no matter how much money you have paid into Social Security over the years, and no matter what you were promised when you paid it, the government always has the option to pay you back only what future politicians decide they can afford, given all the other things they might prefer to spend the money on.

“Owning your own private pension plan means that those who owe you have to pay you what they promised. It also means that if you die without ever using it, you can leave it to your family, instead of having the government keep the money.

“Liberals are desperate to keep Social Security the way it is, because that means they can keep spending your money as they see fit and keep you dependent on them. That’s what the welfare state is all about.”

## ***Events***

The Cato Institute will hold a two-day conference on Social Security on February 8–9, 2005. Confirmed speakers include Nobel Laureate Edward Prescott, as well as Lea Abdnor, Andrew Biggs, Robert Bixby, Jesse Brown, Robert de Posada, Martin Feldstein, Jagadeesh Gokhale, Stephen Goss, Douglas Holtz-Eakin, Rep. Sam Johnson (R-TX), Rep. Jim Kolbe (R-AZ), Maya MacGuineas, Thomas Saving, Kent Smetters, and Michael Tanner, among others. For more information or to register, click [here](#).

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