

Social Security Choice

SOCIAL SECURITY THIS WEEK

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

WEEK OF APRIL 1, 2005

The Hill: *Democratic Lawmakers Attempt a Bait and Switch*

[*The Hill*](#) reported this week that Democratic lawmakers are looking to replace the debate on Social Security with a debate on individual savings apart from the program, a strategy they will use in hope of moving Social Security reform entirely off the table. From *The Hill*:

“After months of criticizing President Bush on his Social Security reform plan, congressional Democrats are crafting their own retirement savings plan that does not call for any change to the entitlement system.

“The Democrats’ move signals a shift in their strategy on Social Security. Until now, the opposition party has opted to lambaste Bush while declining to reveal its own ideas for encouraging saving.

“Democratic senators on the Finance Committee this week quietly floated a document titled ‘Savings Options,’ which sources say is designed as a counter to Bush’s plan for personal accounts in Social Security. The document, obtained by *The Hill*, details several legislative possibilities, including a mandate on employers to provide payroll-deduction savings options for all employees.

“It also tackles low-income incentives for saving by setting up accounts at birth in which the government would deposit \$500 for each newborn and \$1,000 for families with below-average incomes. The accounts would allow parents to contribute more money until the child turns 18, ‘with a government match for contributions from lower-income parents.’”

Plans that divert attention from the financial problems of Social Security do little to help those who depend on the system the most. As Cato executive vice president David Boaz [wrote in a commentary](#) last week, creating new savings opportunities outside of Social Security might be good for people who can afford it, but it does nothing for those who have little income to put away in savings on top of the payroll tax. As Boaz wrote, “Among people with annual household incomes of \$75,000 or more, 84 percent own stocks or stock funds; among those with incomes less than \$30,000 stock ownership is only 26 percent. White households had an average net worth of \$468,200 in 2001, more than six times the \$75,700 of black households.

“That’s why Social Security personal accounts would mean so much to low-income families. If you make a modest income, it’s not easy to put 12.4 percent of your income into Social Security and save more on top of that.”

Mike Tanner: Ownership, Inheritability, and Choice Are Key

In a commentary this week, Cato’s Michael Tanner applauds the Bush administration for bringing Social Security to the forefront of political discussion, but urges supporters of reform not to get mired in the economic minutiae of the problems with the program. The winning arguments, Tanner points out, are ownership, inheritability, and choice—those are the real benefits of reform. Tanner’s commentary follows.

“The latest dispatches from the Social Security front indicate that Republicans may be in the process of winning the battle, but in danger of losing the war.

“Polls show that President Bush has been successful in convincing Americans that Social Security needs reform. The latest ABC/Washington Post poll showed that 71 percent of voters believe that the troubled retirement program is either heading for a crisis or facing serious problems. Even Congressional Democrats have been forced to admit that *something* needs to be done to fix the program.

“Yet, despite the general agreement on the need for reform, the polls also show that there remains skepticism about the President’s proposal for allowing younger workers to privately invest a portion of their Social Security taxes through personal accounts.

“In part this is because Republicans continue to portray Social Security reform as an accounting exercise, a question of matching income and expenditures. Thus, while they continue talking about ‘SSA scoring,’ ‘price indexing,’ ‘infinite horizons,’ and ‘transition financing,’ they ignore the most powerful arguments in favor of personal accounts.

“The first of these is ownership. Under the current Social Security system, Americans have no ownership rights to their benefits. In 1960, the Supreme Court of the United States ruled in *Flemming v. Nestor* that Social Security was just another tax-and-spend program, no more special than corporate welfare or farm subsidies. Social Security ‘contributions’ are a tax, the Court ruled. And ‘benefits’ are just another spending program. Workers have no legal, property, or contractual right to benefits. Under the current system, if you work hard, pay your taxes, and play by the rules, when you reach retirement, you are entirely dependent on 535 politicians in Washington to decide what you get for retirement. Congress is free to change or reduce your benefits at any time. Given Social Security’s \$12 trillion unfunded liability, such cuts are inevitable.

“On the other hand, with personal retirement accounts, Americans would own their Social Security retirement savings, or at least the portion they will have invested. The government could never take these benefits away. Each American would control his or her own future, not the government.

“The second vital principle Republicans need to vocalize is inheritability. Under the present system, your promised benefits go right back into the federal treasury when

you die. Think of it. You work hard your whole life having 12.4 percent of your wages taken out of your paycheck under the promise of a secure retirement. But if you should live only a few years into retirement, the government claims what is left over. You have amassed no legacy. You've nothing to pass on to your heirs. It is, essentially, a 100 percent death tax.

“However, because you would own your personal retirement accounts, you could bequeath their accumulated wealth to your children and grandchildren. This important feature of personal retirement accounts holds tremendous promise for low-wage workers and minorities in America who might otherwise never get the chance to build a nest egg.

“Finally, Republicans need to stress that universally appealing principle, choice. The current Social Security system locks American workers into a one-size-fits-all retirement plan that offers a roughly 1.6 percent return today, and may not even be solvent down the road. Given a choice, most Americans would never include such an investment in their portfolio. No wonder Congress doesn't want people to decide for themselves.

“But a reformed system would give Americans options and participation in the system would be completely voluntary. If workers wanted to remain in the current Social Security system they would be free to do so. But those younger workers who wanted another option would be given the option to choose for themselves.

“What I am suggesting here is that Republicans take off their green eyeshades and start talking about the real benefits of personal accounts. Ownership, inheritability, and choice: That's what this debate is really about.”

White House Remains Committed to Personal Accounts

The [*Washington Times*](#) reported this week that President Bush remains adamant about his desire to allow younger workers to open personal retirement accounts within the Social Security system. The renewed pledge to continue fighting in support of personal accounts comes as opponents of the reforms—including some members of his own party who would like to see the accounts scaled back—continue to assail his plans. Regardless of the criticism, the *Times* reports, the president's commitment remains strong. Excerpts of the article follow.

“President Bush yesterday pledged to ‘keep pounding the issue’ of Social Security reform in the face of Democrats in Congress who are determined to stop him and Republicans who want to scale back his plan.

“I'm going to be stubborn on the issue, and we're going to keep working this until we get something done,’ Mr. Bush said in Cedar Rapids, Iowa, the 20th state he has visited since his second inauguration to push his idea of incorporating private retirement accounts into the Social Security program.

“Now is the time to address tough problems, before it becomes acute for younger generations of Americans,’ he said.

“The president's barnstorming campaign for Social Security reform resembles his presidential campaign, where he preferred dealing with local reporters to the national

press corps. In Iowa, Mr. Bush granted an interview to the morning host on WHO radio while sitting in the Spring House Family Restaurant.

“Mr. Bush said he agreed with Federal Reserve Chairman Alan Greenspan’s view that the Social Security ‘safety net’ is ‘unsustainable,’ and he will continue working to fix it....”

“One lawmaker whom Mr. Bush will need on his side for his plan to pass is Republican Sen. Charles E. Grassley of Iowa, who has expressed reservations about Mr. Bush’s private-accounts proposal, and suggested last week that it should be scaled back.

“Mr. Bush yesterday applied gentle pressure on Mr. Grassley, the chairman of the Senate Finance Committee, where any Social Security reform bill would be born.

“Both Senator Grassley and I have dedicated ourselves to taking on the tough problem of Social Security,’ Mr. Bush said.

“The people ‘expect a president to lead, and they expect the chairman of the Finance Committee to lead as well,’ Mr. Bush said. ‘And, fortunately, the good state of Iowa has got such a man in Charles Grassley. I’m looking forward to working with him on this issue.’”

New York Sun: Resistance to Larger Accounts Is a “Disappointment”

In an editorial this week, the *New York Sun* expressed its dismay with what appears to be White House opposition to large personal accounts funded from the entire employee portion of the payroll tax, or 6.2 percent of wages. According to the *Sun*, backing away from larger accounts runs counter to the pro-growth and pro-ownership arguments for reform. The text of the editorial follows.

“The [*New York Times*](#) glossed over it in a front-page story Monday as an anecdote illustrating the influence on policy of a top aide to President Bush, Karl Rove. But to free-market, growth-oriented followers of the debate on a Social Security reform, the vehemence of the White House’s opposition to the Ryan-Sununu plan on the issue came as a real disappointment.

“The *Times* on Monday described Jack Kemp’s advocacy of Ryan-Sununu as ‘causing problems for President Bush’s drive to overhaul Social Security.’ Mr. Rove was said by the *Times* to consider Ryan-Sununu ‘unworkable.’ A White House spokesman, Kenneth Lisaius, backed away from that a bit when we reached him Monday.

“‘The administration is open to a variety of approaches and ideas including many ideas in Ryan-Sununu,’ Mr. Lisaius said. ‘The president appreciates anyone, including Rep. Ryan and Senator Sununu, who come forward with ideas that lead to permanent solvency and engage in this important debate.’”

“Mr. Kemp had declined to comment to the *Times*, but he told us yesterday that he has written 10 newspaper columns in support of the Ryan-Sununu plan and doesn’t intend to stop. ‘I believe that the logic is inherent. It will be proven the most efficacious of all the reforms,’ he said.

“He compared the current resistance to the Ryan-Sununu plan to the resistance he initially encountered when he first introduced the Kemp-Roth reductions in marginal tax rates that eventually became law in the Reagan administration.

“He called Ryan-Sununu ‘very bold,’ but at the same time ‘a very solid, thoughtful, positive, progressive reform.’ He said the plan dramatically shifts the debate on Social Security ‘away from solvency alone, to the democratization of our capitalistic economy.’

“Rep. Paul Ryan, a Republican of Wisconsin, told us that he speaks to Mr. Rove about his Social Security legislation about once a week. Under the Ryan-Sununu plan, workers would be able to shift to their personal accounts 10 percentage points of the current 12.4% Social Security payroll tax on the first \$10,000 of wages each year, and 5 percentage points on all taxable wages above that.

“The average account contribution among all workers would be 6.4 percentage points. That makes for much larger accounts than the plan Mr. Bush outlined in his State of the Union address, which capped the private accounts at 4 percentage points.

“‘The bigger the accounts, the bigger the short-term transition costs,’ Mr. Ryan told us. ‘That is something that the administration is worried about. ... They are afraid it’ll mess up their short term budget number.’

“Messrs. Ryan and Kemp both emphasized to us they are not seeking a fight with the White House. ‘We’re all on the same team,’ Mr. Ryan said. Quoth Mr. Kemp: ‘I’m 70 years old. I’m not picking fights with anyone.’

“It’d be a terrible mistake for the Bush White House to try to sideline the Ryan-Sununu plan, which strikes us as one of the most promising of all the ways on the table to overhaul Social Security. It’s been scored by the chief actuary of the Social Security administration as a way of fixing the program without cutting benefits or raising taxes.

“Mr. Bush is trying to convince the American people that personal accounts are a good idea. Mr. Rove isn’t doing the president any favors by scaring the public with the idea that if the accounts are too big it’ll somehow be bad for the economy.

“A more growth-oriented message would be that the bigger the accounts, the greater the benefits. At the least, it’s time for the Republicans in Washington to start moving away from negotiating among themselves and toward a debate with the Democrats.”

Rep. John Linder Challenges Opponents to Come to the Table

Noting the inescapable shift in demographics and the growing fiscal imbalance of Social Security, Rep. John Linder (R-GA) challenged opponents of reform to join in the process of finding solutions that will fix the system for future generations. Writing in the [Atlanta Journal Constitution](#) (registration required), Linder accurately identifies the urgency of reform: a lack of action now limits our choices for reform in the future and

necessitates that changes will be more drastic and more abrupt. His commentary follows.

“If you’ve attended one of my town hall meetings, you are accustomed to my use of facts and figures.

“I have always focused on numbers and statistics during my years of public service—for they can assist us in projecting financial benefits and financial challenges of legislative changes into the future.

“Now, I’d like to outline some grim financial statistics facing Social Security. These numbers show a financial shortfall that will undermine our children’s retirement security. Social Security has to be fixed, and I want to describe the problem we face. First, it is true that Social Security is heading toward bankruptcy. Second, Social Security will not be changed for Americans born before 1950. For these Americans, your benefits are secure.

“But it is clear that the numbers do not add up, and we must acknowledge that the current system design is unsustainable.

“How did the financial numbers arrive in such a state of disarray?

“One cause of Social Security’s growing fiscal problem is demographics. Americans are living longer—which is certainly good news. However, in terms of the Social Security system, today’s life expectancy of 77 years was not contemplated when Social Security was designed. In 1935, the average American did not live long enough to actually collect benefits. In addition, millions of baby boomers will begin retiring in just three years, doubling the number of retirees by 2031. Finally, our families are having fewer children. All of these factors are causing a dramatic shift in the worker-beneficiary ratio.

“This worker-beneficiary figure leads us to a critical systemic problem.

“When Social Security was conceptualized in the 1930s, President Franklin D. Roosevelt envisioned a system in which each generation of workers would support its own retirement. Changes instituted in 1939 embraced the current pay-as-you-go financing, in which workers support current retirees.

“When the system was first designed, there were 42 workers to support each retiree. Today, 3.3 workers support each Social Security beneficiary. When today’s younger workers retire, there will only be two workers paying for every one beneficiary.

“These numbers mean that just 13 years from today, the government will begin to pay out more in Social Security benefits than it gets in revenue—and that is when the shortfalls begin growing. When today’s younger workers begin to retire in 2042, the system will be bankrupt.

“The financial numbers our children and grandchildren will face are staggering. Doing nothing to fix our Social Security system would mean that our children and grandchildren would have to borrow an estimated \$10.4 trillion—or \$93,693 for each American household. Each year we wait costs an additional \$600 billion.

“Social Security needs to be fixed soon. President Bush wants to work with anyone who has a good idea.

“Retirement security for the next generation should not be compromised by politics, and that is why the president and this Congress believe we must have an open review of options to strengthen Social Security—with Republican and Democratic support.

“This is an American problem that affects the retirement security of our children and grandchildren. Postponing a review of possible solutions in the face of this looming financial crisis is not in the American spirit of solving our problems.

“Federal Reserve Chairman Alan Greenspan stated that Congress has the choice to do something in advance, or ‘wait until the problem is right on you, in which the solutions are going to be very painful.’

“At a Ways and Means Committee hearing I participated in recently, the Public Trustees of the Social Security Trust Fund stated, ‘The reason to act soon is to avoid the forced necessity of more precipitous action later.’

“That advice seems prudent. I do not want to face the day when we realize that our lack of action was the cause of the loss of our children’s financial freedom.”

We Should Prepare for, Not Insure against, the Inevitable

In a commentary on [Tech Central Station](#), Cato policy analyst Will Wilkinson asks a question that is not asked enough of those who favor a conception of Social Security as an insurance program: Why do we continue to insure against old age as though it were a remote risk, rather than a certainty? When Social Security was developed, there was a minimal risk of living much past retirement, he argues. But that is no longer the case. Social insurance against an inevitability is a financial loser. Wilkinson’s explanation of the problems with insuring against old age follows.

“Do you think Social Security gives you a raw deal? I do.

“Every two weeks my wages are docked by 12.4 percent—not chump change. If the Social Security system doesn’t collapse under the weight of smug complacency, I can expect a modest Social Security retirement benefit that pays about half my current modest wages.

“However, if I had the option to invest half my payroll taxes in a personal account, along the lines laid out by the Cato Institute’s Michael Tanner, I could buy an annuity at retirement that would pay me thousands of dollars more than Social Security every year from retirement to the end of my life.

“Maybe I’ll have a fat IRA by the time I hit retirement, and won’t especially need the money in my personal account. In that case, I could buy the minimum annuity, which pays 120 percent of poverty, and continue to grow the remainder of the savings in my personal account. Because that money is mine, not the government’s, I can pass it on to my wife or kids when I die.

“I like that. I like the idea of having choices, having freedom, and having more. So why *shouldn’t* I have it? Why shouldn’t you?

“According to opponents of reform, I’m guilty of a fundamental confusion. The *New Republic’s* Jonathan Chait writes, ‘Privatizers portray Social Security as a kind of

low-performing 401(k) plan. But the program was never intended as a personal retirement plan. It's a form of social insurance, designed to spread risks throughout the population.'

"On the popular academic blog Left2Right, University of Michigan philosopher Elizabeth Anderson criticizes the Heritage Foundation's Social Security calculator on the grounds that 'It forgets that Social Security is a form of social *insurance*, not a simple retirement plan. So it's comparing apples with oranges.'

"However, if insurance is about spreading risk, one might wonder how retirement counts as one. When Henry Rogers Seager wrote his pioneering tome *Social Insurance: A Program for Reform* way back in 1910, the life expectancy for Americans was about 50 years, and so it made some sense to write about the problem of 'living long enough to become superannuated.'

"When Social Security was enacted in 1935, life expectancy hovered around 65, the retirement age. So there was a point in time at which outliving your ability to take care of yourself was unlikely, but possible, and therefore a 'risk' to guard against.

"But not today. Retirement, like paying the mortgage, is an inevitability to *prepare* for, not a risk to insure against. As Seager put it, 'If the need is one the wage earner clearly foresees as certain to arise, then I should be the last person to wish to relieve him of responsibility for meeting it.'

"By removing retirement from the category of 'risk,' demographic trends have largely removed Social Security from the 'old-age insurance' business. So what business is it in? For most people, it's in the business of supplementing their retirement plan.

"If Social Security functions for most citizens like a retirement plan, and *not* as insurance, then it makes sense for those citizens to judge it by the standards of a retirement plan. If the stream of Social Security checks is going to be part of our retirement income, whether we need it or not, it's right to ask whether we're getting a fair deal. If we're not, then it's right to demand that the government make it fair.

"Even if it made sense to think of retirement as a 'risk,' it remains that Social Security was never insurance in any intelligible sense. As Milton Friedman noted in a 1972 debate with Wilbur 'Mr. Social Security' Cohen:

'Social Security is not in any meaningful sense an insurance program in which individual payments purchase equivalent actuarial benefits. It is a combination of a particular tax—a flat rate tax on wages up to a maximum—and a particular program of transfer payments, in which all sorts of considerations other than the amount paid determine the amount received.'

Cohen's evasive, half-joking reply was that Congress, at his behest, defined Social Security as insurance, as did an article, from his pen, in the *Encyclopedia Britannica*. Congress or the encyclopedia: 'Take your pick,' Cohen said. When Friedman accused Cohen of committing deception through rhetoric, Cohen said, 'I believe in rhetoric because it makes a lot of things palatable that might be unpalatable to economists.'

"The rhetoric of social insurance is a spoonful of sugar for the middle class to help the medicine of redistribution go down. But words mean things, and the

combination of a tax and a government transfer, each part of which is subject to the vagaries of legislative whim, is not ‘insurance,’ even if you call payroll taxes ‘insurance contributions.’ (Here’s a risk: try not ‘contributing.’) A pig in a dress is not therefore pretty. And an apple in an orange peel can’t prevent an apples-to-apples comparison.”

Cato Institute to Launch Ad Campaign

The [Cato Institute](#) will begin a radio advertising campaign next week on the issue of Social Security reform. The ad campaign will begin on Tuesday, April 5th.

Cato will run five radio commercials in the Washington, D.C., media market. The spots focus on the features of personal retirement accounts that have been largely ignored thus far in the debate over Social Security reform.

The first ad, “Opportunity,” changes the focus of the debate from solvency to ownership. “But while politicians debate whether Social Security is facing a ‘crisis’ or only a ‘problem,’ we should see this as an opportunity to create a better retirement program for all Americans,” the ad reads.

The second ad, “Right to Social Security,” dispels the myth that Social Security benefits are guaranteed and highlights the virtues of a system that would allow Social Security ownership among younger workers.

The third spot, “Risk,” confronts the idea that personal retirement accounts are just too risky by pointing out risks associated with doing nothing to fix the broken system.

The fourth spot, “Easy Fix,” points out the folly in simply raising taxes or cutting benefits to “save” Social Security, when the real problem is that Americans have no ownership rights to their benefits.

And finally, the fifth spot, “Wealth Gap,” demonstrates how personal retirement accounts could help to reduce America’s growing wealth gap between rich and poor by allowing the working poor to create real, inheritable wealth they could pass on to their children and grandchildren.

“This ad campaign is designed to educate the public on the real issues involved with Social Security reform,” said [Michael Tanner](#), director of the Cato Institute’s [Project on Social Security Choice](#). “The real promise of personal retirement accounts can be summed up in three words: ownership, inheritability, and choice.”

Job Opening

The Cato Institute’s Project on Social Security Choice is seeking a Social Security Policy Analyst to join our team in promoting public understanding of the benefits of allowing younger workers to privately invest a portion of their Social Security taxes through personal retirement accounts. Essential qualifications for the position include knowledge of Social Security and the issues surrounding the current reform debate. In particular, we are seeking an individual with strong analytic abilities, including knowledge of statistics and/or actuarial analysis. Successful candidates will also have

demonstrated an ability to communicate to a wide public audience through writing and speaking, and a philosophical understanding and appreciation of free markets and a free society. Candidates should send a cover letter, resume, and writing samples to Michael Tanner at mtanner@cato.org.

Publications

The Social Security Administration has released the latest issue of its newsletter, "[International Update](#)." The publication for March looks at the most recent international developments concerning pension reform. This month's issue discusses movements toward reform in Denmark, Norway, Peru, South Africa, and South Korea.

The University of Michigan's Retirement Research Center has released its [newest newsletter](#). The newsletter includes articles on retirement, savings, and Social Security reform, including an abstract from a current working paper by Kent Smetters of the Wharton School and Jagadeesh Gokhale of the Cato Institute.

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