



Social Security Choice

SOCIAL SECURITY THIS WEEK

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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NYT Editorial: "Political Will" Necessary for Social Security Reform

The *New York Times* ran an [editorial](#) last weekend outlining the various options for preventing the projected insolvency of Social Security. Though the editorial significantly understates the problems facing the ailing system and pays only lip service to the benefits of personal retirement accounts, it concludes with the important message that it isn't a lack of options on the table, but a lack of "political will" that thwarts meaningful public debate on the matter.

Apart from the cursory look at privately owned accounts, several other options for reform are briefly discussed. Among them are increasing the age of eligibility, tweaking the cost-of-living adjustment process, changing the initial benefit level index to reflect prices instead of wages, and increasing taxes. Benefit reductions, though not explicitly mentioned, are strongly implied in each of the first three options. "Although none of these approaches are perfect," say the authors, "our preference would center on increasing the wages subject to the Social Security tax and changing the cost-of-living index."

Michael Tanner, director of Cato's Project on Social Security Choice, points out that the editorial board's preferred reforms would do little to address the problems facing the system. On raising the payroll tax cap, Tanner writes, "Even total repeal of the cap would extend the payroll tax solvency of Social Security by only an estimated seven years." In "[No Second Best: The Unappetizing Alternatives to Social Security Privatization](#)," Tanner discusses in great detail the suggestions laid out in the *Times* piece, concluding that allowing workers to privately invest their Social Security taxes is highly preferable to the alternatives.

Survey Finds Retirement Optimism Is Unwarranted

The Retirement Confidence Survey (RCS), released this week by the Employee Benefit Research Institute, the American Savings Education Council, and Mathew Greenwald & Associates, examines Americans' attitudes towards retirement savings. A [news release](#) announcing the general findings of the survey notes that despite the economy's recent improvement, retirement saving among Americans has not increased. Furthermore, the study shows that, although most workers are optimistic for a

comfortable retirement, Americans who are currently saving for retirement aren't saving very much. Reasons cited for the low retirement savings include workers being able but unwilling to cut spending for increased saving, workers being unable to save, and workers not knowing about the scheduled phased-in increase in the eligibility age for Social Security benefits.

Dallas Salisbury, president and CEO of EBRI, had the following to say about this year's survey:

"In the 14 years that we have done the RCS, the aggregate level of worker confidence in having enough money to retire comfortably seems to remain unrelated to whatever economic conditions exist. This year, one-quarter (24 percent) of workers are *very* confident and more than 4 in 10 (44 percent) are *somewhat* confident. Almost half of workers (47 percent) who have not saved for retirement are at least *somewhat* confident about having enough money in retirement, with expectations that their retirement money will inevitably come from somewhere. America appears to be a nation of optimists when it comes to retirement, but for some people the retirement dream may turn into a nightmare."

Changing Social Security to a system of private accounts could solve a number of the problems revealed by the RCS. Workers unable to put away savings on top of their Social Security contributions would enjoy a much higher rate of return than they'll get from their payroll taxes, while workers unwilling to save would be able to accrue significant retirement savings without curbing current spending levels. According to William Shipman, co-chairman of Cato's Project on Social Security Choice, "Long-term benefits of investing in stocks and bonds far outweigh the arguments for leaving Social Security the way it is." A system of private, individually owned accounts is a solution that should generate justified and sincere optimism from American workers.

IRET President: Benefit Formula is the Problem, Private Accounts the Solution

The Institute for Research on the Economics of Taxation recently released an IRET Congressional Advisory newsletter about the *2004 Social Security Trustees Report*. Stephen J. Entin, president and executive director of IRET, suggests that the problems revealed in the report are not the same problems discussed by Alan Greenspan in his recent testimony. It is the initial benefit formula and changing demographics that are most to blame for Social Security's current crisis, says Entin, not the cost-of-living adjustment, as Greenspan suggested. Entin adds that the most logical solution is not to slow benefit growth or raise taxes but to allow private personal pension funds. The newsletter (Congressional Advisory No. 169) can be accessed from the [IRET website](#). An excerpt briefly describing the need for personal retirement accounts follows:

"The COLA is not the source of the system's deficits. It makes little sense to give people a certain initial benefit, and then let it be whittled away by inflation. If the initial benefit formula is giving real benefits that are too high, then fix the initial real benefits, and then give them a full COLA. Greenspan argues that the national CPI index may overstate inflation by a small amount. That is possible, but the cost of living for the elderly may be rising a bit faster than that of the average citizen due to heavy outlays for

medical care, not all of which is covered by Medicare or the new prescription drug benefit.

“Of course, trimming benefit growth would make Social Security’s retirement system, already a bad financial investment compared to private saving, an even worse deal. But raising taxes to cover projected benefits would also lower the rate of return, and would be the worst deal of all, because holding more of a bad investment is worse than holding less of a bad investment. Fortunately, the adverse effects could be offset by allowing people to put some of their Social Security tax “contribution” aside to earn a higher return in a personal pension fund invested in private sector stocks and bonds. That arrangement would require the federal government to trim its own spending to pay for the diversion of the payroll tax. That is only fair, because the government should never have promised these unaffordable benefits to begin with, knowing that the worker/retiree ratio was bound to drop. If future Congresses have less money to spend because of the misbehavior of past Congresses, so be it. Better that than putting a crushing tax burden on future workers.”

Entin concludes that faster wage growth and increased immigration could extend the solvency of the system by a nominal amount, but that “even with such improvements, it would still be necessary to shift over time to a system of personal accounts; but the transition would be much easier with a more rapidly growing economy.”

MSN Money Columnist: Real Fixes for Social Security Won’t Be Easy

According to *MSN Money* writer Liz Pulliam Weston, the book, *The Coming Generational Storm: What You Need to Know About America’s Economic Future*, is a great resource for people who “might understand, in a general way, that the system is in trouble,” without knowing “how seriously out of whack our national retirement system has become or how painful the solutions will have to be.” The book, by Laurence J. Kotlikoff and Scott Burns, plainly lays out the problems that face the system. Weston’s abbreviated version follows:

- “There’s a \$45-trillion gap, in present value terms, between the future money the government is expected to take in and what it’s promised to pay out, with Social Security and Medicare accounting for virtually all of the shortfall. That’s according to economists Kent Smetters and Jagadeesh Gokhale, who studied the issue for the U.S. Treasury Department. (You can read [testimony Smetters gave to Congress](#) on the topic here.)
- “To put this mind-numbing figure in perspective, the Federal Reserve estimates the total net worth of every person in the U.S. to be around \$40 trillion. Our massive U.S. national debt is about \$7 trillion.
- “Net tax rates would have to *double* to pay for all the benefits promised, Kotlikoff and Burns say. If you think you pay too much now, think about handing over twice as much.

- “Just dealing with the Social Security deficit would require a 4.5 percentage point increase in payroll taxes, the authors say. Such an increase would take the combined Social Security tax to nearly 17%. (Currently Social Security takes 6.2% of workers’ checks while employers contribute another 6.2%, for a total of 12.4%.)
- “All these calculations were made before Congress passed the prescription drug benefit for Medicare. That’s expected to add another \$6 trillion to the gap.
- “Waiting to fix the system just makes matters worse. The gap could grow to more than \$76 trillion if lawmakers delay reforms another 15 years.”

Weston also provides a quick rundown of the proposed solutions to the problems and Kotlikoff and Burns’ treatment of them, pointing out that, “There aren’t any easy fixes. Kotlikoff and Burns argue persuasively that most of the ones routinely offered—delayed retirement, increases in productivity due to technology or more immigration—won’t come anywhere close to realistically solving the problem. (Relying on immigrants to maintain the ratio of workers to beneficiaries, for example, would require an influx of 4 million to 6.5 million immigrants a year, the authors say. That compares with the 825,000 legal immigrants and 400,000 or so illegal ones we get annually now.)”

Private retirement accounts are the solution presented in *The Coming Generational Storm*, though Weston isn’t totally convinced.

“The authors may be right that this is the most logical, workable solution to the mess we’re in. I’m not quite as ready as they are, though, to ditch that all-important safety net. It’s not too hard to imagine scenarios where poor market returns would make for too paltry a benefit to sustain our most vulnerable elderly. Rather than a guarantee of principal, I’d like to see some guarantee of subsistence-level income before I’d sign off on such a change.

“Of course, the odds are depressingly good that nothing significant will be done to reform Social Security anytime soon. Nobody wants to pay more taxes, or suffer benefit cuts, or actually *think* about what we’re doing to our kids.

“Given the world we’re setting up for them, twentysomething workers should be marching on Washington right now with pitchforks and torches. The reason they aren’t is probably because, like most everybody else, *they just don’t get it*.

“At least not yet.”

Readers should note that the Cato Institute’s proposal, “[The 6.2% Solution: A Plan for Reforming Social Security](#),” by Michael Tanner, provides the “safety net” feature that Weston desires. The Cato plan would insure that no worker’s retirement income would fall below 120 percent of the poverty level by providing a supplement sufficient to buy an annuity at that level.

A recent Cato Book Forum featuring Laurence J. Kotlikoff, co-author of *The Coming Generational Storm*, is available in Real Video or Real Audio [here](#).

Publications

In the upcoming volume of *Cato Journal*, [James A. Dorn](#), Vice President for Academic Affairs at the Cato Institute, presents a study on the future of China's highly fragmented social security system, "Pension Reform in China: A Question of Property Rights." China's aging population and the prevalence of state-owned enterprises make reform of the current pay-as-you-go system difficult. Dorn's study addresses the need for "broad-based change in China's ownership structure." Though proposals have been made to move China's pension program to a multi-pillar system that includes both pay-as-you-go benefits and compulsory individual accounts, Dorn uses property rights theory to make the case for large-scale privatization. He writes: "A sound understanding of the importance of private property rights for the future of capital markets in China is an essential first step toward reform." *Cato Journal* will be released on April 15.

The Social Security Administration has released its latest publication of the newsletter "[International Update](#)." The publication for the month of March discusses the most recent international developments concerning pension reform. In this month's issue, movements toward reform in Russia, Switzerland, the United Kingdom, Kenya, Chile, and Uruguay are all discussed in detail.

Events

The National Press Club will be hosting a forum called "Fixing Social Security" next Tuesday, April 13 at 6:30 PM. Panelists from the Concord Coalition, AARP, the Heritage Foundation, the Alliance for Worker Retirement Security, and the Brookings Institution will discuss possible solutions to the Social Security dilemma, including private accounts, higher payroll taxes, lower benefits, tapping general revenues, linking benefits to income, and more. For more information, visit the [National Press Club website](#). NPC members and their guests can make reservations at (202)662-7501.

Edited by Brooke Oberwetter, boberwetter@cato.org. To subscribe or unsubscribe to *Social Security This Week*, please contact Feliz Ventura at (202) 789-5202 or fventura@cato.org.