



Social Security Choice

SOCIAL SECURITY THIS WEEK

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Reform Can Include Large Accounts and Fiscal Responsibility

Philosophical and fiscal supporters of Social Security reform can back the same program, according to former Cato Social Security analyst Andrew Biggs. Social Security reform that incorporates large, personal accounts without violating fiscal constraints is possible, according to a Social Security Paper released today by the Cato Institute.

In “Large Accounts and Small Cash Deficits: Increasing Personal Account Size Within a Fiscally Responsible Social Security Reform Framework,” Biggs offers an option that will satisfy philosophical and fiscal reformers.

According to Biggs, there are two different groups, with different goals that support Social Security reform. Philosophical reformers see personal accounts as a good end personifying the American values of ownership and personal control. Fiscal-responsibility supporters view personal accounts as a means to reduce the financial burden of the current system and its negative impact on younger workers and the federal budget.

By structuring individual accounts to incorporate existing government debt, Biggs shows that it is possible to create much larger individual accounts than under most congressional plans, without requiring significant subsidies from general revenues.

“A broadly supported personal accounts proposal need not be a watered-down compromise that pleases neither advocates of individual ownership nor guardians of fiscal responsibility,” Biggs concludes. “In fact, it is possible to construct personal account plans that garner enthusiastic support across the broad spectrum favoring reform.”

Click for Biggs’ Social Security Paper, “[Large Accounts and Small Cash Deficits: Increasing Personal Account Size within a Fiscally Responsible Social Security Reform Framework.](#)”

Moynihan: Accounts Good Policy for Low-income Workers, Minorities

Denison Smith, colleague and friend of late Sen. Patrick Daniel Moynihan (D-N.Y.), praises Moynihan’s pursuit of Social Security reform in an April 20 *Washington*

Times editorial. Smith is the chairman of [For Our Grandchildren](#), a grassroots network organization dedicated to increasing the understanding of all Americans about the urgent need for Social Security reform and the various options under consideration. Excerpts of Smith's editorial follow:

"America lost a great patriot and a brilliant leader last month with the death of former Sen. Daniel Patrick Moynihan. ... He had become a passionate advocate of allowing workers the freedom to choose to substitute personal savings and investment accounts for part of their Social Security coverage.

"Social Security reform based on personal accounts is all about the little guy, Pat told me. He had worked to advance the idea as chairman of President Bush's National Commission to Strengthen Social Security.

"Pat knew firsthand how well [personal retirement accounts] would work for the average worker. Federal employees have their own personal retirement account system under the Thrift Savings Plan. When I first visited him he pointed to his secretary and said: 'She has a bigger retirement account than I do because she chose the equity fund and I chose the fixed payment debt fund. In fact, her account is 3 times larger than mine.'

"Pat was concerned that more Democrats were not focusing on the issue and were missing what he felt was the best opportunity to advance the economic interests of working people, low-income workers, and minorities.

"These accounts are the only chance low and moderate income workers have to develop their own substantial wealth and personal investment in the nation's capital markets. Unlike in the current Social Security framework, each worker would personally own his or her own account and would have broader freedom of choice to use it to benefit his or her family.

"The accounts would earn much better returns in the marketplace and pay much higher benefits than the current system can. Even if all currently promised Social Security benefits are somehow paid, these benefits will represent a low, below market, real rate of return of 0 to 2 percent for most young workers today on the Social Security taxes they and their employers pay into the system.

"... [T]his reform is about personal ownership and freedom of choice, not stocks. Workers would have a choice of a wide range of investment alternatives besides stocks, all of which would pay much higher returns and benefits than Social Security. These include corporate bonds, government bonds, which are directly guaranteed by the government, bank certificates of deposit, again federally guaranteed, mortgage pools and others.

"Moreover, since workers would personally own and control these account funds, at death they would be able to leave any remaining funds to their children or other heirs. With today's Social Security system, you have no accumulated funds to leave at death, and the survivors benefits the program offers are difficult to qualify for and meager in amount.

"Such accounts would be particularly beneficial to African-Americans who have below average life expectancies and, therefore, live fewer years in retirement to collect

benefits. Indeed, a black male born today has a life expectancy of 65.8 years. But the future Social Security retirement age under current law will be 67.

“With direct ownership and control of their own funds in personal accounts, African-Americans could pay themselves higher benefits during their fewer retirement years. And they could leave remaining funds at death to children or other heirs. Imagine the long-term impact on minority communities as older workers start to leave their families substantial funds to build their futures.

“My Democratic colleagues who reject this out of hand are wrong. ... Some of them have multimillion-dollar personal accounts of their own,’ [Moynihan] said, ‘and I don't see how they can say average Americans should not have the same chance of some real ownership and long term financial security.’

“Pat's last concern was to find a nationally prominent Democrat who would take up this cause and really do something to help women, the poor, minorities, and working people across the board, who are getting a raw deal from the current Social Security system.”

Personal Accounts Can Deter Intermediate and Pessimistic Forecasts

“Social Security and Medicare will consume an ever-increasing portion of workers' incomes as the government seeks to keep its promises to future retirees,” writes Matt Moore in his recent brief analysis, “Social Security and Medicare Forecast: 2003.” This may be well known; however, Moore, a Social Security analyst for the National Center for Policy Analysis, argues that the pessimistic assumptions of the 2003 Trustees Report “may be more accurate predictors of future health care expenditures.”

“Social Security and Medicare Part A payments are funded by a 15.3 percent payroll tax on wages. However, since those two programs together consume only 13.4 percent of taxable payroll, they run a small surplus each year. This will not last.”

“According to the trustees ‘intermediate’ forecast... [w]hen today's college students reach retirement age in 2050, their children and grandchildren will face a payroll tax rate of 17.3 percent just to pay Social Security benefits — a 40 percent increase over today's burden.”

Moore reminds us, “The estimates ... are based on the intermediate projections of the Social Security Trustees. ... The intermediate assumptions are touted as ‘most likely’ to happen. However, the pessimistic assumptions may be more accurate predictors of future health care expenditures. The intermediate projections reflect recent experience. In recent years, year-to-year inflation in medical costs has been moderate compared to the annual inflation increases of a few years ago. Many believe the recent lower inflation rate is due to temporary factors and that health care costs will soar.”

If the Trustees intermediate projections are accurate, “By 2030, about the midpoint of the baby boomer retirement years, the two programs will need about 36.5 percent of all federal income taxes to pay full benefits. By 2050, Social Security and Medicare will require more than half of federal income tax revenue — 54.2 percent — in addition to the payroll taxes they will receive. Again, these figures are based on the intermediate projections, so the reality could be worse.”

Moore notes that these financing problems are inherent of a pay-as-you-go (PAYGO) system. “Every dollar collected in payroll taxes is spent the very moment it comes in the door. Nothing is saved. Nothing is invested. The payroll taxes contributed by today’s workers pay the benefits of today’s retirees. Likewise, when today’s workers retire, their benefits will be paid only if the next generation of workers agrees to pay even higher taxes.”

To avoid both the intermediate and pessimistic projections, Moore concludes, “President Bush and others have proposed personal retirement accounts as a solution to Social Security’s financial problem. The Bush plan would allow younger workers to set aside some of their Social Security money in personal accounts, which would be invested in the market. The accounts would earn market returns over the workers’ lives and pay part of their Social Security benefits at retirement. Since each generation would save toward its own retirement, the burden of Social Security on future generations would be dramatically reduced.”

OECD: Slow Growth Unless Older Workers Remain Active

“Some of the world’s wealthiest countries will face labor shortages, slower growth and ballooning social security bills unless they take action to reverse the long-term trend to early retirement,” according to the [release](#) of a series of country evaluations conducted by the [Organization for Economic Cooperation and Development](#). “Although older workers, with their wealth of experience, can offer tremendous value to business and society, they are often discouraged from working or developing their skills after the age of 50.

“In a series of 20 country reports to be released over the next two years, the OECD will propose comprehensive measures for governments, employers and trade unions to take to counter the problem. ... The first two country reports, focusing on Sweden and Belgium, illustrate the difficulties facing many OECD countries and the types of measures required to improve job prospects of workers aged 50 and over.

“Sweden has one of the oldest populations of all OECD member countries. Although recent substantial reform of the pension system should strengthen incentives to later retirement, more action is needed.

“For its part, Belgium stands at an important crossroads. After encouraging early retirement for more than two decades as a way to minimize the impact on unemployment of adverse economic and social shocks, the country needs to reverse course and promote longer working lives, says the OECD. In 2001, just 41 percent of Belgians between the ages of 50 and 64 were working, 14 percentage points below the OECD average.

“In addition to Sweden and Belgium, country reports will soon be released for Spain, Switzerland, Korea and Japan. Reports are also planned for Australia, Austria, Canada, the Czech Republic, Denmark, Finland, France, Germany, Italy, Luxembourg, the Netherlands, Norway, the United Kingdom and the United States.”

World Wide Round Up

While some economies are forced to enact costly pension reforms that cut benefits and increase taxes, the United States has the opportunity to avoid a similar situation by promoting savings and growth with personal retirement accounts. The following pay-as-you-go pension systems around the world are unable to cope with demographic changes, early retirement, and stagnant growth rates:

Brazil: Forbes [reports](#), “Brazil’s Social Security Minister Ricardo Berzoini late on Wednesday laid out some of the details of the proposal the government plans to send Congress to overhaul the nation’s ailing pension system. ... He said at a news conference the changes should save the government 56 billion reais (\$18 billion) over 30 years, ensuring the pension system’s solvency. ... The minimum age to retire will be incrementally raised to 55 years from 48 years for women, and to 60 years from 53 years for men.”

Austria: The *Economist* reports, “Just about everybody, including all the main parties, agrees that pension reform is overdue. Some 10 percent of GDP is gobbled up public pensions. ... Few Austrians work full-time beyond 60. But as they live longer, the pay-as-you-go system is becoming unaffordable. If nothing is done, in 20 years almost half of gross wages will be needed to keep the system afloat, says Bernd Marin of the European Center for Social Welfare Policy and research in Vienna.”

Japan: The *Daily Yomuri Online* [reports](#), “Former Health, Labor and Welfare Minister Yuya Niwa has proposed a plan to increase the government’s contribution to the pension system in stages for five years starting next year to ensure the pension scheme has sufficient funds, it was learned Saturday. ... Niwa proposed increasing social insurance premiums with an upper limit of 32 percent of a person’s annual income from the current 22 percent in the future. This 32 percent includes 20 percent for pension, 10 percent for health insurance and 2 percent for nursing care insurance.”

Germany: *Deutsche-Welle’s* “[Reforming the Social Welfare State](#)” comments on German Chancellor Schroeder’s difficulties in passing adequate reforms to the country’s ailing pension system. “[I]n the 1950s, the ‘pay as you go system’ evolved, with each generation devoting a percentage of their income to finance the public statutory pensions of the generation that preceded them. At the time the contribution consisted of about 7 percent of an employee’s gross income – a very manageable figure.” Despite increased pension contributions to 19.5 percent, “The pension system only functions today because it is subsidized by the federal government and the benefits paid out have been decreased...”

France: Robert Graham of the *Financial Times* reports, “France’s center-right government is putting the finishing touches to plans for reforming the country’s costly pay-as-you-go pensions system by curbing the privileges of public sector employees. ... The basic government aim is to bring the period of contributions of the public sector – employing almost one in four of the French workforce – to the level of the private sector by 2008. This would mean adding an extra three years’ contributions to the public sector’s current 37.5 years. The phase-in period over five years would also be half that of the private sector, which was initiated in 1993. Some 550,000 people would be affected who are due to quit public sector jobs between now and 2010.”

Publications

The General Accounting Office issued a March report to the Senate Special Committee on Aging, "[Social Security Reform: Information on Using a Voluntary Approach to Individual Accounts](#)." The report sought to determine how voluntary plans can affect individuals, how they could affect the total costs of the system, and the role of educational efforts relating to the participation decision. GAO studied the voluntary individual account plans enacted by the Czech Republic, Germany, and the United Kingdom.

Upcoming Events and Announcements

Please join [Social Security Choice.org](#) president Bob Costello and Rep. Jim DeMint (R-SC) on Wednesday, April 30, 11:30 a.m. ET, as they participate in a [live discussion forum on WashingtonPost.com](#). You can submit questions of your own during the discussion, or [submit a question in advance](#). Jim DeMint believes current retirees and those nearing retirement should fully receive their promised Social Security benefits while younger workers should be given the choice of investing their Social Security taxes in personal retirement accounts.

The [2003 Annual Conference](#) of the University of Michigan's Retirement Research Consortium, "Securing Retirement Income for Tomorrow's Retirees," will be held on May 15–16, 2003, at the National Press Club in Washington, D.C. The conference will address the following issues: Participation and Impacts, Social Security Personal Accounts — The Nuts & Bolts, Savings Decisions, The Role of Earnings in Retirement Income, and Current Issues in Private Pension Plans.

Job Opening, Senior Social Security Analyst: The Cato Institute's [Project on Social Security Choice](#) is looking for a senior Social Security analyst. The successful applicant will have an advanced degree in economics or a related discipline or equivalent experience. The candidate should have detailed knowledge and understanding of the U.S. Social Security system, as well as the economic and actuarial issues associated with various proposals to reform the system. Excellent written and communication skills are a priority. Candidates should be committed to the principles of limited government and individual liberty, as well as to reforming Social Security through individual accounts. Submit résumé and writing samples to [Michael Tanner](#), director of Cato's Project on Social Security Choice.

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