



Social Security Choice

SOCIAL SECURITY THIS WEEK

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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DeMint Plan Shakes Things Up on the Hill

Sen. Jim DeMint's (R-S.C.) reform plan for Social Security was debated privately by Republican legislators this week, but those discussions ended with a very public endorsement from GOP Conference Chairman Rick Santorum, who had yet to endorse any specific piece of reform legislation.

The [DeMint option](#) takes the current surpluses in Social Security and diverts them to individual accounts, creating individual "lockboxes," so to speak. Michael Tanner, Director of the Cato Institute's Project on Social Security Choice, said in *CQ Today*, "The idea is, they don't expect it to pass, but it really puts the onus on the Democrats." Tanner added that since various versions of the DeMint plan limit investment options to bonds, the plan essentially contains no risk. "It takes nothing out of the Social Security system—how can you be against it?"

Without investment risk as a point in the debate, opponents of Social Security reform are forced by the DeMint plan either to make the case for preserving the current system, in which payroll taxes confer no legal entitlements and returns are subject to revision by Congress, or to propose an alternative reform solution.

On its own terms, the plan does more than jump-start the debate. The individual accounts can be transferred through inheritance, eliminating situations that exist at present in which workers and their families who have contributed payroll taxes see no return from Social Security in cases where death precedes retirement. DeMint also hopes to win support from other fiscal conservatives, like Santorum, who hope that taking Social Security's annual surpluses off the general revenue ledgers will keep spending in check.

Sen. DeMint's plan is different in several respects from the Cato Institute's "[6.2% Solution](#)." Both plans offer voluntary accounts, but the account sizes in the DeMint plan are smaller, averaging 5.1 percent compared to the across-the-board 6.2 percent carve-out proposed by Cato. While the DeMint plan does allow for inheritability, this is achieved through annuities paid to the individual's children in instances where there is no spouse to inherit, whereas the Cato plan allows for the accounts to be fully inheritable. Both plans contain a minimal guaranteed benefit.

Cato Scholars Testify before Congress

Michael Tanner, director of Cato's Project on Social Security Choice, testified again before Congress this week, this time before the Senate Banking Committee, specifically, the Subcommittee on Securities and Investment. His testimony, on the possible administrative structure of Social Security personal retirement accounts, is available [here](#). It was his fourth congressional testimony in the last five weeks.

On Thursday, June 16, [Ian Vásquez](#), director of Cato's Project on Global Economic Liberty, testified on the success of pension reform in Chile, in particular noting their adoption of a system of private accounts. His testimony is available [here](#).

And next Tuesday, William Shipman, co-chair of the Cato Project on Social Security Choice, will testify before the Committee on Ways and Means on the subject of protecting and strengthening Social Security. Additionally, Mr. Shipman had a recent commentary in *The Hill*, which is now available on the Cato website [here](#).

Mike Pence: Don't Raise the Payroll Tax

Writing this week in [USA Today](#), Rep. Mike Pence (R-Ind), chairman of the Republican Study Committee, argued against Rep. Robert Wexler's legislation, which calls for a 6 percent payroll tax on all income over \$90,000. As Pence illustrates convincingly, Wexler's bill would do far more harm than good. His commentary follows.

"Last year, President Bush put Social Security reform on the national agenda. His proposal to save Social Security by giving younger Americans the option to choose personal savings accounts has been met, to date, by ridicule and silence among the loyal opposition in Congress.

"That silence ended last month when Rep. Robert Wexler, D-Fla., introduced legislation that he described as 'Social Security Forever.' I admire him for his leadership on behalf of his philosophy of government, and also for his honesty as he proposes to cure Social Security with that antidote that Democrats most often run to: Higher taxes.

"Make no mistake, increasing taxes—either by raising the Social Security tax rate or raising the amount of income subject to Social Security taxes—would amount to the largest marginal tax rate increase in a generation and result in an enormous burden on working families, small businesses and farms.

"According to the Heritage Foundation, raising the payroll tax cap would directly raise taxes on 9.8 million American workers, including 3 million small-business owners. This would also reduce Gross Domestic Product by \$33 billion per year, on average, over its first 10 years and reduce total employment by an average of 340,000 jobs per year over that period. For these reasons, House conservatives vigorously oppose proposals to 'reform' Social Security by raising taxes.

"The American people now see a very clear choice before them: The president's bold vision for reform based on fiscal discipline and choice, and the Democrat vision for

reform based on higher taxes. The cure for what ails Social Security is new ideas, not higher taxes.”

Kitchen Sink Approach Might Not Work in the House

House Ways and Means Chairman Bill Thomas might meet with opposition from his own party, as his plans to introduce PRAs as a part of a mammoth “comprehensive retirement package” meet with skepticism from some members of the Republican leadership.

According to *CQ Today*, “The GOP is divided on whether the best approach to restructuring Social Security and preserving pensions is the multifaceted retirement security legislation Thomas, R-Calif., has in mind or the narrowly focused measure envisioned by Senate Finance Chairman Charles E. Grassley, R-Iowa.

“Thomas is entertaining suggestions in an attempt to solidify support from lawmakers, companies and unions. And he has begun dropping clues about the kinds of incentives he may embrace.

“On Tuesday, Thomas said his catchall legislation might ease restrictions on 401(k) plans and other retirement savings. ‘Currently, the tax code inhibits or prohibits...doing certain things,’ he said.

“With fewer restrictions, for example, life insurers could market hybrid annuities that can be converted to long-term health care plans.

“Thomas’ allies say his plan builds on his success last year in loading up a corporate tax overhaul with sweeteners including a tobacco buyout. ‘You’ ll see everything...except the kitchen sink,’ a House Republican predicted.”

Though a final draft is far from complete and negotiations continue, fiscal conservatives in particular should be wary of an all-encompassing retirement overhaul, which, in addition to being complex and difficult to understand, might bargain away too much.

Retirement Age Re-enters the Debate

The *LA Times* [reports](#) that GOP senators have been privately discussing an increase in the retirement age as part of Social Security reform. The proposal emerged during talks aimed at securing the future solvency of the system.

However, the Cato Institute Project for Social Security Choice pointed out in a recent [Daily Debunker](#) that simply raising the retirement age leaves unresolved the structural flaws in the system:

“Americans have been here before. Those workers who paid their payroll taxes since 1955 were told that they would be allowed to retire at 65. When Social Security hit its most recent previous crisis in 1983, the retirement age was bumped up, rising over time to 67 years. Since the system was running out of money, Congress decided to keep workers out of retirement for longer than promised....

“The only way to guarantee workers reliable retirement security is to grant them control of their money in the form of personal accounts. Workers would control these accounts, which would make them less reliant on current workers to fund their retirement benefits and would lighten the burden on taxpayers....

“A retirement age of 69 would discriminate against African Americans and others on account of lower life expectancies. As it stands, returns for African Americans are a full percent point lower than for whites and many do not live to see a single pay check. Again, personal accounts would solve this problem. Since personal accounts are owned and controlled by workers, individuals can pass on their retirement savings to their family if they die before retirement. This feature of personal accounts—inheritability—fixes the injustice of workers who pay their payroll taxes throughout their career but never see a return.”

That certainly isn't to say that, in crafting reform, legislators shouldn't take into account the fact that Americans are living longer and longer lives and are increasingly more able and willing to put in more years of work. However, inheritability must be a feature of any reform that calls for an increase in the retirement age in order to ensure that those who die before retirement have not paid their payroll taxes in vain.

National Council of La Raza Favors Add-On Accounts

Congressional Quarterly reports this week that the National Council of La Raza, the nation's largest advocacy group for Hispanics, has announced its opposition to current plans to reform Social Security. The group, which has hitherto not taken a position, added that they did not plan to actively campaign against the Bush administration proposals.

Opposition from La Raza centers on individual accounts. Eric Rodriguez, the director of La Raza's policy center, [specified](#) the grounds of their concerns, noting that “our analysis and our findings are that there's no reasonable way that you could design a carve-out account system that would be as beneficial to low-wage workers as it would be to high-wage workers.” Mr. Rodriguez did not assert that low-wage workers would not benefit from PRAs, simply that they wouldn't benefit *as much as* wealthier workers.

Rodriguez went on to express support for securing solvency and creating add-on accounts while strengthening other private savings vehicles. However, add-on accounts seem like an odd proposition for La Raza to endorse, given their concern about the treatment of low-income workers.

There are numerous problems with add-ons as they pertain to low-income workers. To start, many low-wage workers simply cannot afford to put away additional money for their retirement on top of the already extraordinarily high payroll tax. The best way to help low-income workers reap the benefits of investment is to let them make investments out of money they already pay.

Assuming the accounts would be voluntary, there would be no incentive for wealthier Americans to opt in unless they are able to devise ways to use the accounts as tax shelters, as argued by Darcy Olsen in [this 1999 Cato Briefing Paper](#). Otherwise, wealthy Americans, who have access to much less strictly regulated and much more

fruitful investment opportunities, will simply take their money elsewhere, a choice that lower-income workers don't have.

Featured Daily Debunker: Status Quo Is Bad for Agricultural Workers

Each weekday, the Cato Project on Social Security Choice provides new content on its website, www.socialsecurity.org. The Daily Debunker, the most frequently updated feature on the website, sets the record straight about the most egregious instances of misinformation about personal accounts that appear in newspapers and magazines. This week's featured debunker discusses the possible benefits of Social Security reform for agricultural workers. From the Debunker:

Bloomberg [reports](#) that various rural and farm groups announced opposition to Social Security reform this week. Keith Bolin, leader of the American Corn Growers Association, argues, "Social Security was one of the better-working programs the federal government ever did." However, as the Cato Institute's Jagadeesh Gokhale has [argued](#), Social Security as it stands presents real and serious problems for low-income workers.

Agricultural laborers get a particularly bad deal. All workers stand to gain from ownership, inheritability, and choice, as offered by personal accounts, but agricultural workers get a particularly bad deal from Social Security as it exists today. Life expectancies for agricultural workers are traditionally lower than those for other workers, which means that fewer rural laborers live to see any returns on their Social Security taxes. Contributions agricultural workers make to the current system enter general revenue and are not inheritable, unlike personal accounts. In effect, this means that agricultural workers' contributions in part take the form of a transfer from groups with low life expectancies to those with higher life expectancies, as groups with higher life expectancies end up receiving more of the overall Social Security funds.

Certain groups of workers are hit particularly hard. Migrant agricultural workers have a life expectancy of only 50 years, compared to a national average of 73 years. The current system makes no provision for inheritability. Rural groups seeking to help their most vulnerable members should support personal accounts that allow migrant workers to pass on their accumulated Social Security contributions to their families without losing their accumulated savings to general revenue upon death.

Edited by Brooke Oberwetter, boberwetter@cato.org. To subscribe or unsubscribe to *Social Security This Week*, please contact Christy Rhoton at (202) 789-5259 or crhoton@cato.org.