



Social Security Choice

SOCIAL SECURITY THIS WEEK

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

WEEK OF JULY 23, 2004

Legislation Based on Cato's "6.2% Solution" Introduced

Reps. Sam Johnson (R-Texas), Pat Toomey (R-Pa.), and Jeff Flake (R-Ariz.) have introduced Social Security reform legislation based on Cato's "[6.2 Percent Solution](#)." The "Individual Social Security Investment Program Act" (HR 4895), which has more than a dozen cosponsors, will give workers the option of remaining in the Social Security system or having half of their FICA tax—6.2 percent of their salary—deposited into individual accounts. The other half of the payroll tax, the portion paid by employers, will help cover transition costs and underwrite disability and survivors' benefits. Workers already enrolled in the current system who opt for the new plan would receive a "recognition bond," redeemable upon retirement and fully tradeable, based on the amount they have paid into the old plan. The legislation is designed to create large individual accounts while minimizing transition costs. It is currently being scored by the Social Security Administration.

Johnson, Toomey, and Flake introduced the legislation at a press conference on Thursday, also attended by Cato president [Edward H. Crane](#) and Stuart Butler, vice president for domestic and economic policy at the Heritage Foundation. Crane praised the legislation, saying, "The impressive thing about this bill is that it ties together all the essential parts of sound Social Security reform. It is easy to understand—your share of the payroll tax is used to purchase real assets you own; the employer's share helps finance the transition. The '6.2 percent solution' creates accounts large enough to make a real difference. And best of all, the recognition bonds immediately create personal accounts that Congress cannot tamper with."

Original cosponsors of the Individual Social Security Investment Program Act include:

Sam Johnson (R-Texas)
 Pat Toomey (R-Pa.)
 Jeff Flake (R-Ariz.)
 John Shadegg (R-Ariz.)
 Nick Smith (R-Mich.)
 Tom Feeney (R-Fla.)
 Joe Wilson (R-S.C.)

Roscoe Bartlett (R-Md.)
 Pete Hoekstra (R-Mich.)
 Trent Franks (R-Ariz.)
 Jennifer Dunn (R-Wash.)
 John Doolittle (R-Cal.)
 C.L. "Butch" Otter (R-Id.)
 Joe Pitts (R-Pa.)

Rep. Paul Ryan Unveils Social Security Reform Plan

Rep. Paul Ryan (D-Wis.), working in conjunction with several other sitting representatives and former Congressman Jack Kemp of Empower America, introduced alternative reform legislation on Tuesday that would create large private retirement accounts as a solution to the crisis facing Social Security. In an Empower America media alert last week, Jack Kemp said, “This new legislation will allow every working man and woman the opportunity to become an owner and an investor and to prepare for their retirement through the use of large personal retirement accounts.”

Rep. Ryan made the case for his bill in an op-ed in Monday’s *Wall Street Journal*, an excerpt of which follows:

“The bill would allow workers 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 five percentage points on all taxable wages above that. With this progressive account structure, on average, workers would be shifting 6.4 percentage points of the 12.4% tax to their accounts.

“Workers choose investments by picking funds managed by major private investment firms, from a list officially approved for this purpose and regulated for safety and soundness, similar to how the Thrift Savings Plan for federal employees operates.

“Benefits payable from the tax-free accounts would substitute for a portion of Social Security benefits based on the degree to which workers exercised the account option over their careers. Workers exercising the personal accounts would receive traditional Social Security benefits based on the past taxes they have already paid into the program, in addition to the money from their personal accounts.

“The plan maintains a strong safety net, as the accounts are backed by a federal guarantee that workers would receive at least as much as Social Security promises under current law. The plan is voluntary. Anyone who chooses to stay in traditional Social Security would receive the benefits promised under current law. Survivors and disability benefits would continue as under the current system.

“The proposal achieves solvency without benefit cuts or tax increases because so much of Social Security’s benefit obligations are ultimately shifted to the accounts. In fact, the official score of the chief actuary shows that ultimately, instead of increasing the payroll tax to over 20%, as would be needed to pay promised benefits under the current system, the tax would be reduced to 4.2%, enough to pay for all of the continuing disability and survivors benefits. This would be the largest tax cut in U.S. history.”

CBO: Private Accounts Will Fix Social Security Financing

A recent report from the Congressional Budget Office (CBO) has found that a system of private accounts would help fix the long-term financial problems facing Social Security. The report found that private accounts would not only help to maintain the

system's long-term solvency, but it would provide greater benefits to retirees than the current system. The Senate Committee on Aging described the report in a [press release](#):

“A new report by the non-partisan Congressional Budget Office confirms that including personal retirement accounts within Social Security would help workers realize a more financially secure retirement in future years and permanently fix Social Security's long-term funding problems....”

“These findings support [a report issued last month](#) by the non-partisan General Accounting Office which also found that personal accounts in Social Security can help shore up retirement security for younger workers when they retire,’ Craig said. ‘This is good news for young Americans.’

“Both the GAO report released last month and the new CBO report examined what is known as ‘Model 2’—a specific proposal presented in 2001 by the President's Commission to Strengthen Social Security. Under the Model 2 approach, those currently in the workforce could voluntarily redirect 4 percent of their Social Security payroll taxes, up to \$1000, to a personal retirement account.

“The CBO study also found that the Social Security financing problem would be permanently fixed by 2050 if the Model 2 Social Security personal retirement account option was adopted.

“The Chairman of the Senate Committee on Aging emphasized, as he always does, that current retirees are in good shape when it comes to their Social Security benefits.

“Those currently on Social Security and those about to retire will not be affected by any reforms we are discussing—but young people of today will face benefit cuts years from now if we do nothing. And in contrast, if we can get Congress to adopt a personal retirement account option to Social Security, future seniors will enjoy a more financially secure retirement,’ Craig said.

“The newly released CBO study found that owners of personal accounts would have a greater certainty of higher benefits if they invested a portion of the Social Security funds into a conservative, balanced portfolio—with 20 percent in a broad government bond index fund, 30 percent in a broad corporate bond index fund, and 50 percent in a diversified stock index fund like the S&P 500.

“The nonpartisan economists found that if nothing is changed, federal officials will be unable to pay scheduled Social Security benefits starting in 2053 and Social Security outlays will exceed revenues from payroll taxes and taxation of benefits beginning in 2019.

“If we do nothing, we're going to hurt future retirees, future taxpayers, or both. But both the GAO and CBO reports make it clear that if we follow the personal account option, we have an opportunity to exceed virtually everyone's expectations, and put Social Security on a sustainable path,’ Craig said.”

USA Today: Bush and Kerry Have “Squandered Opportunity” to Court Young Voters

Although polls indicate that voter turnout amongst the under-30 demographic will be much higher than years past, an editorial in [USA Today](#) suggests that neither John Kerry nor George W. Bush has reached out to young voters in any meaningful fashion; though both pay lip service to the issues that interest young people, neither has really addressed them. By focusing on geographic rather than demographic voting trends, the two candidates for president have largely ignored this critical, and typically undecided, age group. As the following brief excerpt makes clear, this is especially true where Social Security is concerned.

“Bush and Kerry have largely ignored young voters’ fears. Polls show that they believe by a wide margin that the program will be broke when they retire. Bush favors using some Social Security taxes to create personal accounts, a plan backed by 82% of voters under 30, according to a USA TODAY/CNN/Gallup Poll last fall. But he rarely touts the plan. Kerry has no specific plan to fix Social Security.”

Bush Says Social Security Reform to be Part of Second-Term Agenda

Reforming Social Security by allowing younger workers to privately invest a portion of their payroll taxes through individual accounts will be an important part of his second-term domestic agenda, President Bush told supporters this week. Speaking at a fundraiser for Republican congressional candidates, the president told the more than 7,000 donors that he would push for proposals that would allow workers to “own a piece of their retirement.” The president called for “a new era of ownership in America, with an agenda to help all our citizens save, and build, and invest.”

Aides later told reporters that Bush will speak frequently on the issue of Social Security reform during the coming campaign, but that he will not put forward any specific plan. Rather, he will stress the need for reform, the importance of individual accounts, and the need to work with Congress on final details.

Scott Burns Lays Out the Basics of Social Security

Dallas Morning News columnist Scott Burns offers [a primer on the Social Security crisis](#) this week. In his usual candid style, Burns addresses the history of the PAYGO system, the existence of a Social Security “Trust Fund,” and the ability of economic growth to handle the debts that the current system will soon incur. Ultimately, Burns argues that despite the arguments of the naysayers who believe Social Security can survive with only minimal adjustments, the system is surely headed for fiscal ruin if drastic changes aren’t made. In the following excerpt, Burns discusses the system’s PAYGO status and the changes over the years that have effectively turned Social Security surpluses into a giant congressional slush fund:

“Pay-as-you-go or funded trust?”

“When Social Security was created in 1935, it was designed as a pay-as-you-go program. The employment tax would transfer money from people who were working to people who were retired.

“It was a good idea because most Americans had seen their savings wiped out during the Great Depression. Social Security would put purchasing power in the hands of people who didn’t have any. The money would stimulate the economy. It would also stave off the rising tide of socialism and communism.

“Basically, Social Security was a welfare program for elderly Americans. It was never discussed as a welfare program, though. All the language used to describe it—such as ‘your account’ and ‘trust fund’—was done to create greater public acceptance.

“The trust fund isn’t a funded trust; it’s just a buffer account. It was designed to handle the year-to-year ups and downs of employment tax collections. Although money in the fund has earned interest since 1940, interest earnings have never been a significant part of the money paid out by Social Security.

“In 1975, for the first time, benefit expenditures exceeded employment tax revenue. The trust fund, which had enough money in 1974 to pay about eight months of benefits, started to shrink. By 1983, it hit rock bottom. It ended the year with only \$19.7 billion in assets—enough to pay about two months of benefits.

“Since then, after recommendations from a committee led by economist Alan Greenspan, employment taxes have been increased, retirement ages were advanced, and benefits have been subject to taxation.

“The idea was to build the trust fund. It would do far more than buffer minor economic ups and downs. It would smooth out the retirement of an entire generation, the baby boomers. It would do this by building a large balance that could be drawn down over a period of decades.

“By the end of 2003 the trust fund had accumulated Treasury obligations of \$1,355.3 billion. That’s three years of benefit payments. The fund increased \$137.8 billion from the previous year. An impressive \$75.2 billion in interest was credited to the fund. And the Internal Revenue Service collected \$12.5 billion in taxes on benefits.

“As boomers start to retire and benefit payments again exceed employment tax collections, the trust fund will peak at five years of benefits in 2015, the trustees predict.

“It will be exhausted in 2042. That’s when, according to Social Security Commissioner Jo-Anne Barnhart, benefits would have to be cut 27 percent.

“Bottom line: Social Security *is* a pay-as-you-go program. But future tax payments won’t cover the promised future benefits.

“There would be no problem if Congress hadn’t spent the money

“For better or worse, money for Social Security isn’t like the money in Scrooge McDuck’s vault. Employment tax dollars come into the U.S. Treasury. The trust fund is credited with Treasury obligations for revenue not spent. It is also credited with interest on the accumulated Treasury obligations.

“Social Security has trust fund assets, and the U.S. Treasury has a liability that is exactly equal. They zero each other out.

“Unfortunately, total government spending has exceeded government revenue collection in virtually all of the last half-century. Our employment tax dollars *were* spent. What Social Security got was an IOU from the Treasury.

“The higher employment taxes paid by everyone who has been working since 1983 became a megabillion-dollar slush fund for politicians of both parties. The Social Security surplus meant Washington could spend more. Politicians didn’t have to raise income taxes because every worker was paying more employment taxes.

“If you visit the government Web site that keeps daily track of all government debt, you’ll learn that debt has increased in every single year. This includes the years Democrats and Republicans celebrated as years of ‘surplus.’

“You can see how this works by examining a broad summary of government finances published monthly in ‘Economic Indicators’ by the Council of Economic Advisors.

“‘Off Budget’ is primarily a record of surpluses for Social Security and related trust funds. The ‘On Budget’ is regular government operations. And the ‘Unified Budget’ is the combination of both.

“The Off Budget has had large, growing surpluses. The On Budget has enjoyed small surpluses in just three years: 1999, 2000 and 2001. The Unified Budget shows surpluses in 1998, 1999, 2000 and 2001.

“But our gross debt has increased in every single year!

“The problem coming our way is simple. With government debt growing by \$500 billion a year, will Social Security be able to redeem its hoard of Treasury IOUs when benefit payments again exceed payroll tax collections?”

Upcoming Events

The Center for Retirement Research at Boston College will be holding its annual conference at the National Press Club in Washington, DC, August 12–13. The conference, entitled “The Future of Social Security,” will feature a variety of panel discussions and distinguished speakers. To see the agenda for the event, or to register, visit the Center’s website, http://www.bc.edu/centers/crr/events_con.shtml.

Publications

Earlier this month, the American Enterprise Institute published a paper by AEI resident scholar Leon Aron on the privatization of pensions in Russia. Privatization of the Russian system, writes Aron, has “highlight[ed] and test[ed] the quality of key institutions and instruments central to such a system: transparency and liquidity of banks and mutual funds, probity and competence of state regulatory agencies, and stability of equity and bond markets. Still, the reform’s most significant consequence might be strengthening the Russian people’s trust in the market’s ability to replace and outperform the state in controlling vital assets and delivering benefits.”

To read the entire paper in PDF format, click [here](#).

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