

# Social Security Choice

## ***SOCIAL SECURITY THIS WEEK***

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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### ***Democratic Retirement Plan Ignores Social Security***

House Democrats unveiled a retirement savings plan this week, partly in response to criticism of their long-standing refusal to engage in the debate on the Social Security crisis. The plan relies heavily on changes to the 401(k) savings scheme but does not propose any changes to Social Security, leaving taxes, benefits, and the impending bankruptcy of the system unaltered.

House Minority Leader Nancy Pelosi announced the initiative, calling it “a plan to affect the long-term retirement security of the American people.” The Washington Times [reported](#) the details:

“The Democrats’ “[AmeriSave](#)” proposal is a combination of changes to pension rules and the creation of new incentives for people to save more in 401(k)s and other existing retirement accounts. The Democrats’ plan, through a tax refund, would match dollar-for-dollar the first \$1,000 contributed to an individual retirement account, 401(k) or similar account. It also would create a tax credit for employers who offer such savings plans, encourage employers to automatically enroll employees in these types of accounts, and institute various changes to make it harder for companies to dump their pension plans. The plan is estimated to cost \$75 billion over 10 years.”

The announcement follows on the heels of last week’s pledge by House Ways and Means Committee Chairman Bill Thomas (R-CA) to introduce a Social Security reform plan in September. Thomas told reporters on July 19 at the National Press Club that he intended to push the Ways and Means Committee to consider the issue as part of a comprehensive retirement bill.

Democrats took criticism for conflating savings policy and Social Security reform. The plan would leave Social Security insolvency unaddressed, focusing instead on tax incentives for middle-class workers to participate in 401(k) schemes. While certainly strengthening savings is an important priority on its own merit, simply increasing savings does not by any means preclude the need for Social Security reform. Indeed, even with better access to 401(k) style options, millions of Americans will still be unable to adequately save for their retirements. A reform that could create savings opportunities from taxes that people already pay would be far preferable for most families to coming up with additional money to put in a 401(k).

The cost of the Democrats' plan, at \$75 billion, represents a large outlay at a time when Congress has the option of passing bills based on the DeMint plan, which seeks to lock the Social Security surplus into the system for the first time. Thus choosing AmeriSave over the DeMint plan in effect entails a massive outlay at a time when most thought on the matter has been concerned with possibilities for saving the funds already within the system.

### ***Administration Officials Talk Strategy at White House Briefing***

President Bush reiterated his support for Social Security reform at a White House briefing this week, at which members of the grassroots group Students for Saving Social Security (S4) and officials from various business associations, including the Alliance for Worker Retirement Security, were present. In particular, the president commended the efforts of S4, a non-partisan student organization established to promote the benefits of personal accounts for younger workers. Their efforts have led to the development of 180 S4 chapters in over 40 states. The President expressed his gratitude for the group's work and encouraged them to continue their efforts.

President Bush also used the opportunity to re-emphasize his commitment to substantial personal accounts, adding, "Not only am I not going to quit, but I'm more determined than ever."

Patrick Wetherille, co-founder of Students for Saving Social Security, said, "After hearing the President today, there is no doubt he is committed to Social Security reform."

Bush's comments, echoing remarks at a recent town hall meeting in Atlanta, came amidst a pause in the campaign to reform Social Security while Congress works on CAFTA and the Supreme Court vacancy. The White House has not endorsed any current bills, including those based on the DeMint plan to retain the surplus within the system, holding out instead for larger accounts and a reform package that addresses the solvency issue.

Also speaking at the briefing were Deputy White House Chief of Staff Karl Rove and Treasury Secretary John Snow. Rove told the group that the White House was anticipating movement from the House in September, with the Senate following shortly thereafter. Rove's assertion was backed up by a statement this week by House Ways and Means Committee Chairman Bill Thomas (R-CA), who told reporters that his committee would have a bill to the floor "probably in early September," [according to \*The Hill\*](#).

### ***GROW Accounts Bill Unveiled***

House Republicans officially unveiled Social Security reform legislation this week based on Sen. Jim DeMint's plan to create personal retirement accounts out of the annual Social Security surplus. Rep. Jim McCrery (R-LA), chairman of the Ways and Means Committee's subcommittee on Social Security, was joined by about a dozen other lawmakers for the announcement.

The following specifics were reported by the Baton Rouge *Advocate*:

- The GROW accounts (Growing Real Ownership for Workers) would end in 2017 but would at least get the accounts established, co-sponsors said. “It’s a small step,” said U.S. Rep. Clay Shaw, R-Fla. “But it’s a step forward.”
- GROW accounts would be created for workers who were under the age of 55 at the beginning of 2005, unless they don’t participate.
- The Social Security surplus would be invested in U.S. Treasury securities. As of the close of the day Monday, Treasury bonds were earning an average of 4.35 percent.
- An independent board of experts, responsible for ensuring safe investment, would be established to manage and administer GROW accounts. In 2009, the board would submit a plan to Congress providing options to diversify GROW accounts through broader investments.
- Retirement payments would be a blend of account investments and Social Security benefits and the accounts would be inheritable, co-sponsors said.

Though plans to fund personal accounts from the Social Security surplus seem to be gaining momentum in Washington, the Bush administration has wisely withheld its support for the idea. According to administration officials, the president maintains that solvency must be addressed by reform legislation. GROW accounts do not have any effect on solvency, and in fact can only be funded as long as there is a Social Security surplus, which is only until 2017 under current projections.

### ***Reformers Should Stick with PRAs and Progressive Indexation***

In a lengthy article appearing in the *City Journal*, Nicole Gelinas writes in defense of the president’s proposal for Social Security reform: progressive indexing and personal retirement accounts. The article is a particularly useful recap of the developments in Social Security over the last several months, particularly the introduction of progressive indexation. An excerpt of the article follows, and the whole thing—which includes calculations about estimated benefits under several proposals—can be seen [here](#).

“Conservative reformers greeted President Bush’s late-April proposal for ‘progressive indexing’ of Social Security benefits with dismay—and prominent conservative leaders haven’t said much about it since. They’re wasting an opportunity. Yes, Bush’s proposal was meant as a giveaway to liberals—a politically calculated trade to win their support for reining in Social Security’s unsustainable growth. And it’s a fair deal, provided that conservatives get what they’ve always wanted from reform: personal accounts within Social Security, to entice millions of middle-income Americans to join the investor class.

“The president’s progressive-indexing idea is hardly revolutionary. It represents a change in degree, not in philosophy. Social Security benefits are already a radically

'progressive' income-transfer program, in which low-wage earners make out, relatively speaking, much better during retirement than do middle-income and top earners.

“Unlike the graduated income tax, which imposes a higher rate on higher earners, Social Security levies the same rate on all earners (within a \$90,000 annual earnings cap) during their working lives. But the system pays back higher-income participants at lower rates when they retire. Workers get more ‘credit’ for the payroll-tax payments they make on the first few hundred dollars they earn each month, and that credit drops precipitously for additional earnings.

“For Social Security purposes, politicians already define high earners as those who make just \$45,400 a year. So all middle-income earners underwrite a delayed income-transfer system to the poorest earners. In other words, this is already a tightly compressed welfare system. Though middle-income folks don't pay much attention to how much money they will eventually lose in retirement income to lower-income retirees, conservative leaders shouldn't be shy about reminding them that Social Security, despite the myths surrounding it, is by no means a fair retirement program.

“Though the president's proposal is still vague, its basic elements are clear enough. Let's start with the bad part before looking at what makes the overall scheme so attractive, and then consider how its underlying principles can best be realized.

“Bush would pare back Social Security's future payouts to middle and top earners, giving a huge relative boost to retirees whose lifetime earnings were low. Right now, the Social Security Administration determines a new retiree's initial benefit according to a formula based on how quickly U.S. wages increased during that worker's career. The president would like to preserve that formula for the bottom 30 percent or so of earners. But for higher earners, the initial benefit would be based on how quickly prices, rather than wages, increased during a worker's career—in other words, at the rate of inflation. Since wages usually rise more quickly than prices, future benefits for lower-income people would grow much faster over time than would benefits for middle- and higher-income people.

“This doesn't sound like enlightened reform, and understandably it has annoyed some conservatives. Columnist George Will objected on ABC's This Week in late April: ‘So what [Bush is] doing is making Social Security less and less relevant to a majority of the American people. You're stigmatizing it . . . by . . . means-testing Social Security so it becomes a poverty program.’ Republican senator George Allen of Virginia worried that the plan would ‘reduce the retirement security for . . . middle-income working people.’ Cato Institute senior fellow Alan Reynolds warned, ‘Any Social Security ‘reform’ that [is] increasingly generous to those who paid the least in taxes would be increasingly perceived as grossly unfair and therefore politically untenable.’

“But they're forgetting the good news in Bush's proposal: personal accounts, which will make Social Security more relevant to middle and upper earners, not less, since it will give them the ability to save for a middle-class retirement within Social Security, not despite it. Reform without personal accounts, or with tiny personal accounts for top earners, isn't real reform.”

## ***Upcoming Events***

Michael Tanner, director of Cato's Project on Social Security Choice will debate economist and columnist Paul Krugman on the future of Social Security at an event commemorating the 70th anniversary of the implementation of the program. Krugman has been an outspoken critic of any plan to create individual retirement accounts and has repeatedly denied that Social Security faces long-term challenges that need to be addressed, in spite of his [protestations to the contrary](#) during the Clinton years.

The debate, hosted by the Franklin and Eleanor Roosevelt Institute as part of a day-long event, will take place in Hyde Park, NY on Saturday, August 13. For more information, click [here](#).

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