



# Social Security Choice

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

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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### ***Cato Analyst Cites Johnson-Toomey-Flake Bill as Best Approach to Social Security Reform***

Cato Social Security analyst Berna Brannon recently offered her views in a Cato Commentary on new legislation proposed last week by Reps. Johnson, Toomey, and Flake. Brannon argues that, given Social Security's impending insolvency, the Individual Social Security Investment Program Act of 2004 offers an immediate way for Congress to make the necessary changes to the system. The bill itself is based on Cato's ["6.2 Percent Solution."](#) The full text of Brannon's commentary follows.

"Social Security's day of reckoning is uncomfortably near. In 15 years it will pay out more in benefits than it collects in taxes, and the money in the purported trust fund has long been spent on other government needs. Social Security has gaping holes that cannot be fixed with only minor changes. But there is a solution, one that gives Americans more control over their own money, which means more freedom and more choices. And it's a solution that Congress can start implementing now.

"Supporters of reform know that waiting for the election before beginning the steps to reform is a luxury they cannot afford. Observers expect President Bush to again make this a central issue in his campaign this fall, allowing him to use the election results as a mandate for reform in 2005. For him to have any success in passing through Congress any Social Security reform, it is necessary for Congress to at least begin the process of proposing and vetting the various reform proposals currently under discussion.

"To that end, Reps. Sam Johnson (R-Tex.), Pat Toomey (R-Pa.) and Jeff Flake (R-Ariz.) introduced in recent days the "Individual Social Security Investment Program Act of 2004," legislation based on a plan developed by the Cato Institute's Project on Social Security Choice.

"As with nearly all reform plans under consideration, private accounts play a crucial role. In this bill, individuals would be able to voluntarily invest their half of the payroll tax, amounting to the entire 6.2 percent worker contribution, into individual accounts. The remaining 6.2 percentage points of payroll taxes would be used to pay the

transition cost and fund the Social Security disability and survivor benefits. Workers who choose to remain in the traditional system would have their benefit calculations gradually shift from wage indexing to price indexing starting by 2012.

“Workers who choose the individual account option would receive a recognition bond based on the accrued value of their Social Security benefits, i.e., the value of what they have already contributed to the system. These bonds, redeemable at the normal retirement age, would be fully tradable in financial markets with proceeds being deposited in the worker's account. This mechanism of recognizing past contributions is unique to this proposal.

“The investment structure would be a three-tier system: Tier I would be a centralized, pooled collection. Tier II would offer limited investment options with a 60/40 stock/ bond default portfolio. For individuals who accumulate \$10,000, Tier III would give a wider range of investment options. At retirement, individuals can purchase an annuity or take a programmed withdrawal. As long as either of these options provides an income above the minimum level, funds in excess could be taken out in a lump sum. The government would provide a safety net by guaranteeing a minimum benefit equal to 120 percent of the poverty level.

“This bill shows that giving workers ownership of their savings and equipping them with tools to secure their retirement can be done in a fiscally responsible way. Meanwhile, it transforms the pay-as-you-go system into one oblivious to whatever demographic trends may arise.

“Social Security has been one of the most popular government programs of all time, and politicians who attempt to change it in any way must proceed with caution. However, the current system simply cannot survive in its current state for much longer; to insist otherwise borders on demagoguery.

“The bill proposed by Reps. Johnson, Toomey, and Flake dramatically improves the fiscal imbalance while bringing personal accountability into the Social Security system.”

### ***NCPA Analyst Deduces Kerry's "Secret Plan" for Social Security***

Writing in a [guest commentary](#) on *National Review Online* last week, Sean Tuffnell, senior manager of media relations and special projects for the National Center for Policy Analysis, does some Internet research and uses deductive reasoning to reveal John Kerry's "secret plan" for saving Social Security. Since John Kerry is on record as opposing tax hikes, benefit cuts, retirement age increases, and privatization of the system, Tuffnell deduces that Kerry plans to slash the rest of the federal budget by twenty percent. In every department. Tuffnell's description of how he arrived at this conclusion follows.

“Political conventions, while no longer the news-making festivals of yesteryear, still serve a critically important function for our democracy. They provide the two major political parties the chance to present an unfiltered picture to the American electorate of

who their leaders are, what they stand for, and what they would do if they were given the opportunity to govern. While many in the news media bristle at our modern day conventions as nothing more than ‘infomercials,’ if they at least ‘inform’ then they have served their purpose.

“So what have we learned from the gathering in Boston, other than that the Democrats have a general distaste for the war and anything having to do with George W. Bush? Not much, unless you listen very, very closely. What have I gleaned from a close inspection of Democrat speeches? If you take the rhetoric at face value, it appears that Sen. John Kerry has a secret plan to cut all government programs except for Social Security by 20 percent.

“How in the world did I deduce that, you ask? It’s elementary my dear Watson. On the opening night of the convention, former President Bill Clinton announced to the world that John Kerry has a ‘good idea ... to save Social Security.’ This was great news, because Social Security faces serious challenges.

“While it’s one of the government’s most popular programs, having provided a source of retirement security for many seniors, Social Security is structurally flawed. It is built on the premise that each generation of workers can fund the retirement of their parents and grandparents, and that as a reward their retirement will be secured by the payroll taxes paid by their children.

“The problem comes with demographic realities. First, through healthy living and the miracles of modern science, we are living longer. In 1940, life expectancy was 61.4 years for men and 65.7 for women. By 2000, life expectancy was 74.2 for men and 79.5 for women; by 2050, life expectancy will be 79.2 for men and 83.4 for women. This is great for us, but bad for Social Security—it means the pool of retirees collecting benefits is increasing.

“At the same time, Americans for several decades have been having fewer kids. No longer do we regularly see families with three or four children. Now the increasing norm is for couples to wait to get married, wait to start having children, and when they do, they often only have one. The result has been dramatic. In 1940, there were 42 workers per retiree. Today the ratio is 3-to-1; by 2050 it will be 2-to-1. The burden on each individual worker will increase substantially and we will no longer be able to keep our promises to retirees at current payroll-tax levels. The funding gap caused by this demographic shift begins to open in 2018 and will eventually reach approximately \$11 trillion.

“That gap can only be bridged by one or more of the following prescriptions: cut benefits by up to 30 percent, raise payroll taxes up to 50 percent, increase the general debt up to \$11 trillion, or generate additional revenue using existing resources, such as allowing workers to invest a portion of their payroll-tax contributions in personal retirement accounts (an approach endorsed by President Bush).

“Back to the Democratic convention. President Clinton’s announcement of Kerry’s Social Security plan raised a red flag when I heard it. After all, for well over a year Kerry has been on the campaign trail speaking on every topic from Iraq to gay

marriage. Not once do I remember him dedicating a speech, or even five minutes of a speech, to his great idea for saving Social Security.

“Then, on the second night, Massachusetts’s senior senator, Ted Kennedy, echoed President Clinton’s assertion, saying: ‘John Kerry offers hope, not fear. The hope ... of Social Security that is always there for the elderly.’ There it was again, a vague reference to Kerry having a plan for Social Security.

“If both the former president and Kerry’s Senate partner believe he has a plan, there must be one somewhere. Time to do a little research. Unable to find policy details in the convention speeches, I decided to look at the party platform—the place we are supposed to find policy details. Here’s what it says:

‘We are absolutely committed to preserving Social Security. ... Democrats believe in the progressive, guaranteed benefit ... not subject to the whims of the market or the economy. We oppose privatizing Social Security or raising the retirement age.’

“It goes on about the importance of Social Security but offers no other policy prescriptions.

“Okay, so as a party the Democrats want to maintain the current structure and benefit levels of Social Security, but they don’t want to generate new revenue through personal investment. That still leaves me wondering about this plan for saving it.

“So I did a little more research. My next stop was the Kerry campaign website I looked under issues to see if his plan was posted there. Unfortunately, his [index of issues](#) left me perplexed: There were links to information about children and families, civil rights, the economy, education, energy, environment, health care, homeland security, national security, national service, rural America, science and technology, stronger communities, veterans, and women. Nowhere was there a link to Social Security, retirement security, or even seniors’ issues. Frustrated, I tried looking under economy, but found no mention of Social Security there either.

“Digging deeper, I finally found some instances where Kerry made comments on Social Security during the campaign. In January, at a presidential debate in Des Moines, Iowa, Kerry said, ‘I will never privatize Social Security. I will never try to extend the retirement age for Social Security. And I will not cut any benefits for Social Security.’

“On NBC’s *Meet the Press* in April, Kerry said, ‘I’m not going to cut Social Security benefits. I’m not going to extend the retirement age. ... And we’re not going to have to raise the premiums.’

“If benefit cuts, retirement-age increases, personal retirement accounts, and tax hikes (raising the ‘premiums’) are off the table, there are only two options left: increase the debt by \$11 trillion or cut all other government programs by 20 percent. And since Sen. Kerry has routinely criticized President Bush for increasing the debt, one can deduce he’s not about to come out in favor of increasing the debt by \$11 trillion.

“So it’s simple really. Through a simple process of deduction, it becomes clear that Sen. Kerry has a secret plan to cut spending on everything from health care to education to defense by 20 percent. And you thought conventions had no value anymore.”

## ***Young Voters Want Social Security Leadership from Presidential Contenders***

An op-ed in the [\*Seattle Times\*](#) by Chris Collins addresses a number of issues important to young voters this election year. Among those issues is Social Security, which Collins calls “the money gobbler.” Only President Bush has offered a real solution to restoring solvency and creating savings, writes Collins. That solution is private retirement accounts. He concludes by suggesting that younger voters should start paying attention to this issue and that they should demand that politicians address the program as they campaign. The section of the op-ed dealing with Social Security follows.

“There’s really no other way to describe the Social Security program. Congress debates endlessly about what to do with the non-defense discretionary spending that makes up roughly 18 percent of the federal government’s \$2.3 trillion annual budget. This portion includes education, training, science, technology, housing, transportation and foreign-aid spending.

“In contrast, Social Security makes up 22 percent of the annual budget, or \$475 billion—about the size of South Africa’s entire annual economic output. Between 2000 and 2025, the number of people age 65 and older is predicted to grow by 76 percent. But the number of workers supporting the system will grow by only 17 percent, according to a June report from the Congressional Research Service.

“Both Republicans and Democrats acknowledge the program is destined for bankruptcy at this rate.

“So what plans do the White House candidates have in mind? Kerry vows to never ‘privatize’ Social Security—that is, he doesn’t want to allow workers to decide where to invest their money. While acknowledging Social Security’s fiscal crisis, he offers no real solutions other than giving optimistic sound bytes about growing the economy, fiscal discipline and bipartisanship.

“Bush’s strategy, in contrast, offers specific solutions. He doesn’t want to eliminate the program, but he does want to allow workers to funnel some of their Social Security taxes into personal retirement accounts.

“A bipartisan presidential commission found that Bush’s plan would ‘lead to increased national saving.’

“Social Security is the fiscal boa constrictor in the room. It’s going to increasingly squeeze our paychecks thin in coming years if politicians looking to reform the system are not elected.

“Politicians of all stripes and colors frame the Social Security issue as something that only senior citizens care about—we will surely protect your Social Security, they tell the 50-and-over crowd.

“Not even lip service is given to the concerns of my generation. We need to start making Social Security our issue, as well.”

### ***Concord Coalition Says Social Security Liabilities Even Worse than Commonly Said***

The newest volume of *Facing Facts*, a fax alert from the Concord Coalition, takes a critical look at the standard assessments of Social Security’s future liabilities and finds that the numbers most often used in discussing Social Security are misleading and incomplete. “Looking behind the Colossal Liability Numbers,” by Neil Howe and Richard Jackson, takes issue first with the use of “actuarial balance,” finding it to be a measure that vastly underestimates the “long-term cost challenge” of Social Security.

They write: “Until recently, the only widely reported liability measure was ‘actuarial balance,’ the official indicator of Social Security’s and Medicare’s trust-fund solvency. The Trustees define actuarial balance as the present value of trust-fund revenue over the next seventy-five years plus current trust-fund assets minus the present value of trust-fund expenditures over the same period. As of the beginning of 2004, Social Security’s actuarial balance was a deficit of \$4.0 trillion—or the equivalent of an extra 1.9 percent of U.S. worker payroll each year starting today.

“Defenders of the entitlements status quo like to cite Social Security’s actuarial deficit because it makes the long-term problem seem modest. Yes, the defenders say, an extra two percent of payroll may be a significant levy, but surely we cannot regard it as a catastrophic imposition on future workers.

“Actuarial balance, however, is a highly misleading measure of the long-term cost challenge. To begin with, it counts trust-fund assets as genuine savings, even though these assets aren’t going to reduce future tax liabilities by one dime. The CBO, GAO, and OMB all concur: The trust funds represent a claim on future tax revenues, not real savings that can be drawn down to defray future benefit costs. If we exclude trust-fund assets from the calculation, Social Security’s unfunded liability leaps to \$5.5 trillion.

“There’s another problem with actuarial balance: the arbitrary seventy-five-year time horizon. This limit assumes that future Americans will allow Social Security to run off a financial cliff in 2079. In other words, it assumes that our children, come the year 2025 or 2050, will be utterly unconcerned with the fate of their own children. To assess Social Security’s true financial status, we need to look at its liabilities over a longer—indeed infinite—time horizon. While this may strike some readers as unusual, it is actually the seventy-five-year cut-off that is odd. Private financial markets routinely value income and expenditure in perpetuity. Perhaps taking a cue, the Trustees now calculate and publish an ‘infinite horizon’ liability estimate for Social Security. It is \$11.9

trillion excluding trust-fund assets—or three times Social Security’s official actuarial deficit.”

They continue: “All of the numbers discussed so far are ‘open group’ liabilities—that is, they assume that new generations of participants will join the Social Security and Medicare systems. They measure the extra burden of continuing to pay current-law Social Security and Medicare benefit promises, and thus the programs’ fiscal sustainability. They say nothing directly, however, about the programs’ generational equity—in other words, about how much of the extra burden will be borne by ourselves and how much by our children.

“The Trustees also calculate another liability measure, known as a ‘closed group’ liability, that answers this question. The closed group measure assumes that Social Security and Medicare will be closed to all new entrants. It then determines what today’s workers and retirees are due to receive in future benefits over and above what those same workers and retirees are due to pay in future contributions. Private pension plans calculate something similar called a ‘termination liability.’ Indeed, federal law requires them to do so.

“As of the beginning of 2004, Social Security and Medicare had a combined closed group liability of \$42 trillion. This number represents the subsidy that today’s adults expect from future generations, which is another way of saying that it measures the extent to which future generations will fail to get a fair return on their contributions. It also tells us the cost of transitioning from today’s pay-as-you-go entitlement system to a new funded system. It is the sunk debt that future generations would have to liquidate before they can invest their own contributions free and clear.

“Whichever measure you pick, we are talking about a vast sum. The \$42 trillion closed group liability for Social Security and Medicare is *ten times* greater than our publicly held national debt (\$4 trillion). The \$74 trillion infinite future liability exceeds our nation’s total net worth (\$42 trillion, which includes all property owned by U.S. residents—real and financial). Paying it off would require taxing away an *extra 18 percent of workers’ earnings forever—again, starting today.*”

To read this complete volume of *Facing Facts*, click [here](#).

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