



# Social Security Choice

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

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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### ***Rep. Sam Johnson: Reform Bill Will Help Individual and Government Finances***

In a letter to the editor of the *Washington Times*, Rep. Sam Johnson (R-Texas) outlines some of the specifics of the Social Security reform bill he recently introduced in the House of Representatives. In addition to describing the key elements of the bill, which is based on the Cato Institute's "[6.2% Solution](#)," Johnson also makes a convincing case that Social Security reform must happen sooner rather than later given the magnitude of the fiscal problems ahead. The text of Rep. Johnson's letter follows.

"The Op-Ed column by Leanne Abdnor and Tim Penny ('Dollars and sense,' Aug. 19) was correct in pointing out that Social Security is facing a problem sooner than the Congressional Budget Office and others have wanted to admit. However, I fear they also are too optimistic about when we will start to face this problem.

"In 2018, the Social Security system will stop collecting the surpluses that subsidize our other overspending. However, it is only until 2009 that Social Security surpluses will continue to grow—after that point, Social Security surpluses will begin to dwindle. Every year between 2009 and 2018, the budget subsidy from Social Security is expected to decline. For every billion dollars the subsidy falls, the federal appetite for spending will have to be weaned from Social Security surpluses.

"When Social Security surpluses start to decline—long before they go into deficit—the rest of the federal budget will begin to feel the pain. There will be less subsidy for roads, the military, child nutrition, medical research and the thousands of other things on which we spend money, or we will have to borrow more money or raise taxes just to continue this spending spree. These difficult decisions will be made not a generation from now, but in 2009, just outside of the next presidential term. We must talk about Social Security reform on this urgent timetable. The year 2018 is just a moment when the cash flow changes from positive to negative. The party will be over long before 2018.

"The question is: What do we do with those surpluses between now and then? I have introduced legislation that would permit people born since 1950 to deposit their entire 6.2 percent of their salary into a personal Social Security account. In these

accounts, Americans can build real wealth instead of unrealistic expectations of benefits from a system doomed to failure.

“Before we begin making difficult decisions about spending, borrowing and taxing, the first decision we should make is to begin pre-funding Social Security retirement with cash in personal accounts. With real assets in accounts, rather than more promises of benefits in the future, we can then face our obligations to those who already are retired and those near retirement. My legislation would continue Social Security retirement benefits for those born before 1950 and for those who do not choose to opt into personal accounts, and it would continue disability and old-age survivor benefits to be funded with the 6.2 percent of salary tax on employers.

“My legislation also creates a fully tradable ‘recognition bond’ that would pay a lump sum representing the benefits people have earned so far in the current system. They could sell this bond on open markets and then deposit the proceeds in their own accounts to continue growing in the market.

“The last major component of my bill is a guarantee of 120 percent of poverty for those who do not accumulate enough assets in their accounts or face market losses.

“There are those who claim such a bold proposal is the ‘third rail of politics—touch it and you die.’ I don’t believe that for a moment. My legislation has more co-sponsors (14 original) than have ever been on a Social Security reform proposal. I think we have already been this successful because we have been so bold and do not shrink from making tough decisions.

“The American people are ready to hear about this problem and want a solution that deals with it in a straightforward method.”

### ***National Journal “Insider Interview”: Michael Tanner on Social Security***

Cato’s Michael Tanner was recently interviewed by NationalJournal.com’s Cameron Williams about the future of Social Security reform. In the interview, Tanner candidly discusses the benefits of privatization, the silence thus far from the Kerry campaign on the issue of Social Security, and the Bush administration’s chance at really selling the idea of PRAs to voters this election year. Several of the questions and answers from the interview follow.

**Williams:** You’re a very strong advocate for Social Security privatization and President Bush frequently expresses support for personal retirement accounts. John Kerry is opposed to privatization. Do you think Social Security privatization will be a major selling point for the race over the next three months?

**Tanner:** I think this is a clear area of differentiation between the two candidates. While President Bush has not been as forceful or specific as I would like, it is clear that he supports the idea of allowing younger workers to privately invest at least a portion of their Social Security taxes through individual accounts. Senator Kerry has ruled that out. He has also ruled out any form of benefit cuts. Now, one wonders what it is exactly he would do to fix Social Security. ...As former President Clinton said, you can raise taxes, you can cut benefits or you can invest privately. That’s really the only options you have. Senator Kerry has taken private

investment and benefit cuts off the table. One wonders if that means he's in favor of tax increases.

**Williams:** Bush campaigned on personal retirement accounts in 2000, but aside from a commission to investigate various privatization proposals, there hasn't been much movement on the topic. Do you think terrorism has kept Bush from further addressing the issue? And are you confident he will push for Social Security reform if he wins a second term?

**Tanner:** I think the domestic agenda in general got pushed aside by 9/11, and then the war in Iraq. Social Security was not unique in this regard. The president has told me and other advocates that he is intending to push for Social Security reform as part of a second term agenda. I take him at his word.

**Williams:** The *New York Times*'s Paul Krugman, in a column published on Aug. 13, suggests that privatization was scrapped in President Bush's first term because nobody figured out where Social Security benefits for older generations will come from if younger workers siphon their payments into private accounts. Do you see this multi-trillion dollar hole that Krugman writes about?

**Tanner:** Well, there's no doubt that Social Security reform involves short-term costs. It also provides long-term savings. The fact is, no one has shown where they can get the 26 trillion dollars necessary to prop up the current Social Security system. What you've got is pay a little bit now, or pay a lot later. In many ways, it's like refinancing your mortgage. You have to pay the points up front, but you will save money in the long term.

**Williams:** I saw several congressmen hold a press conference on your bill in July. What are the selling points of your plan? And in what way is your proposal moving forward in Congress or in other avenues?

**Tanner:** Our proposal was introduced by Representatives Sam Johnson [R-Texas], Pat Toomey [R-Pa.], and Jeff Flake [R-Ariz.], with more than a dozen other cosponsors of the bill. The bill is basically designed to try to achieve large individual accounts while remaining fiscally responsible. It would allow workers to invest half their Social Security taxes through individual accounts. It would also give them a recognition bond equal in value to the benefit they have already accrued under the traditional Social Security system. At the same time, it recognizes that there is no free lunch and that any Social Security reform is going to have to minimize the transition costs and make some of the tough decisions, in terms of holding down the expense of the plan.

**Williams:** Do you have faith that Bush will be able to work with Congress to get a bipartisan solution passed?

**Tanner:** Well, the whole issue of Social Security reform is unfortunately becoming much more partisan. Many of the Democrats who were willing to address the issue, people like Pat Moynihan and Bob Kerrey and Chuck Robb, are gone. Even [John] Breaux, who was one of the last supporters of individual accounts on the Democratic side of the Senate, is now leaving. This means it's going to be much more of a partisan political battle. On the other hand, the polls

show the American people strongly supporting individual accounts, and I think that if the people speak out, they can get it.

**Williams:** You wrote on your [Web site](#) that the greatest aspect of your proposal is it reduces Americans' reliance on government. I think most voters might disagree that financial support from a government program like Social Security is a bad thing. How do you respond to a charge that you're less interested in reforming Social Security than in tearing down a program you might have ideological problems with?

**Tanner:** We want to give individuals ownership and control of their retirement money. Under the current Social Security system, you pay 12.4 percent of your wages into the system, and you have no legal rights to benefits at all. The Supreme Court ruled in *Nester v. Flemming* in 1960 that Social Security simply was a tax and a government spending program. So paying your taxes doesn't necessarily get you any retirement benefits. You're entirely dependent on the whims of 435 politicians in Washington. Individual accounts would give you true ownership of your money, and I think one of the things that we want to create in America is an ownership society.

**Williams:** But the system has worked for 60 years.

**Tanner:** Well, like any pyramid scheme, the people at the top of the pyramid do well. The fact is, you did get back a lot more than you paid in if you retired 20 years ago, but younger workers can expect a poor and possibly even negative rate of return.

**Williams:** You said your proposal is more progressive for minorities and women. What do you mean by that, and why isn't Bush doing more to appeal directly to these voters with this issue?

**Tanner:** Well, first of all, our proposal actually increases the minimum Social Security benefit to a level of 120 percent of poverty, much higher than the current minimum benefit. Second, our program would allow people with shorter life expectancies, such as minorities and low-income individuals, to pass their Social Security benefits on to their heirs, something that doesn't happen today. In fact, today one out of three black men will pay into Social Security and then die before they collect their benefits. It's a very unfair system.

As for the political ineptness of the Bush administration, I never underestimate it.

### ***Treasury Secretary John Snow Discusses Social Security***

An interview with U.S. Treasury Secretary John Snow ran in the August 22 edition of the *South Florida Sun-Sentinel*. Among the topics discussed was Social Security. Excerpts of Snow's remarks on the need to reform the swelling entitlement program follows.

We've got some period of time before Social Security, for instance, becomes a negative on an annual basis for the deficit. And we're going to have to deal with that problem. I agree with you 100 percent. It's simply arithmetic. We started out with Social Security and we had 16 workers to 1, and we now have 3 or so and we're headed off to having 2. And it's a pay-as-you-go system and in any pay-as-you-go system, the math gets pretty bad as the number of contributors declines relative to the number of recipients. So we have a real problem here.

The president has put forth some ideas on that that really showed leadership four years ago in the campaign. Your congressman down here [Clay Shaw] has put forth some important ideas as well. Both the president and Congressman Shaw have talked about these personal accounts, some way to augment, supplement the Social Security benefits system with independent accounts, giving people an opportunity to control their own destiny by making investments that would have an equity premium to it, the opportunity to earn an equity premium. [President Bush's commission on Social Security] found that by deploying personal accounts appropriately you could keep the system financially viable.

### ***Chicago Sun-Times: Reform Can Satisfy Young and Old Alike***

An editorial appearing last week in the *Chicago Sun-Times* makes a strong statement in favor of reforming Social Security to a system of private retirement accounts. The editorial makes the case for PRAs by pointing to the success of investment accounts such as 401(k)s and noting that such long-term funds fare well over longer periods of retirement saving. The text of the editorial follows.

"Social Security was created during the Great Depression in order to protect elderly Americans from the specter of spending the end of their lives in dire poverty. To that end it has worked extraordinarily well. While financial problems remain a real issue among elderly, millions and millions of Americans over the decades have been spared from experiencing the lash of utter destitution.

"But as the New Deal program enters its golden years—it will be 70 next year—it is time to retire the program as we know it and introduce it in a reconstituted form for future generations of workers, one that will allow participants more control over where their hard-earned money goes.

"Times have changed. The stock market is no longer the plaything of a wealthy few. Americans have learned to invest their money themselves. A huge chunk—42 million workers—have 401(k) investment plans, accounting for nearly \$2 trillion in assets. They are counting on that money to augment the subsistence offered by Social Security.

"The government should encourage retirement savings. It is presumptuous and undemocratic for the government to continue to force workers to contribute to a program that by all accounts will collapse upon itself in the future decades. Americans

are living longer and having fewer children, and with fewer workers supporting more retirees, Social Security cannot continue in its present form without either cutting back its benefits or demanding ruinous payments from a relatively smaller pool of younger Americans.

“Given that Social Security will, at one point, have to be reformed, the question becomes: How? Allowing younger employees to direct a certain percentage of their Social Security payments into retirement accounts would not only return more control of their financial futures to those who earned the money, but pave the way for easing Social Security from an all-encompassing role that it will no longer be able to fill when there is one retiree for every two workers.

“The standard criticism for such a program is that it would cast the fates of millions of Americans on the uncertain mercy of the stock market. But as we have seen in recent reports, most Americans fared well with their 401(k)s, even during the recent bear market of 2000 to 2002. The average 401(k) account at the end of 2003 was up nearly 30 percent from the year before. This was because they followed a long-term investment strategy, including diversification of assets. Retirement investing is based on decades, not years, of returns.

“Social Security is a promise that must be kept for those retired or about to retire. We need to make sure that, for the generations with decades of working life remaining, it doesn’t become a promise that can’t be kept. Adding a voluntary personal retirement component to Social Security, while still keeping our promise to those under the traditional system, will help both the program and the people it serves.”

### ***Bush Campaign Likely to Avoid Social Security Reform Details***

Peter Wallsten of the *Los Angeles Times* takes a thorough look at the Social Security debate and suggests that while Social Security will feature largely in the president’s campaign rhetoric, specific details of reform will likely be left unanswered in the run-up to the election. Details to be omitted from the discussion, Wallsten adds, include the most controversial aspects of privatization: financing the transition and what percentage of the payroll tax would be diverted into the accounts. An excerpt of the article follows.

“The decision to stick to generalities also reflects the political complexities facing Bush as he tries to outline a domestic agenda for a second four years in office. Towering budget deficits resulting in part from his tax cuts have given him little room to maneuver. And what critics see as his confrontational leadership style has fostered implacable hostility among Capitol Hill Democrats, whose support would be critical for anything as substantive as changing Social Security.

“Some Republicans are hesitant to act on Social Security because of poll data showing that seniors have been unhappy with Medicare’s new prescription drug benefit and have responded to Democrats’ charge that the legislation was more of a boon for pharmaceutical companies than beneficiaries.

“The [GOP] leadership gets very nervous about what happens in the marginal [House] districts’ when Democrats focus their attacks on Republican stewardship of Social Security and Medicare, said Michael Tanner, director of health and welfare studies at the Cato Institute, a libertarian think tank.

“Still, advocates of partial privatization said that presented in the right way on the campaign trail, the plan could appeal to younger voters who worried they would never reap the rewards of the taxes they paid into Social Security.

“The advocates said that talking about the proposal in general terms would allow Bush to claim a mandate for change if he won in November.

“But Rep. Robert T. Matsui of Sacramento, the ranking Democrat on the House committee that oversees Social Security funding, said he couldn’t foresee his colleagues going along with Bush on creating private accounts, especially if the president did not address the tough questions surrounding it.

“He has an obligation to put down a plan,’ Matsui said. ‘To talk about it conceptually is meaningless. We all want to solve the problem and maintain benefits and not increase payroll taxes and make everybody happy. But he can’t just say that and expect to get a mandate out of it.’

“White House officials say they are watching six separate proposals pending in Congress, all of which they say meet Bush’s standards for changing the Social Security system.

“Still, that offers little clue to what his position in a second term might be, since the bills vary widely—ranging from so-called ‘free lunch’ plans that envision large personal accounts and no benefit cuts or tax increases, to what experts say are more realistic proposals that would create smaller accounts accompanied by benefit cuts and tax hikes.

“White House aides will not discuss the bills in detail.

“Many think Social Security is facing a crisis as the first wave of baby boomers are nearing retirement. Historically a pay-as-you-go system, with workers’ payroll taxes being used to fund retirement benefits for current seniors, the program is projected to begin paying out more than it takes in as early as 2018.

“Charles Blahous, who heads the White House’s review of Social Security, said Bush would strive to build public support by making a case for change that outlined the challenges facing the system and how ‘ownership’ could foster a permanent fix.

“Graham said he had urged Bush and chief White House political strategist Karl Rove to be bolder during the campaign, arguing that Social Security was not the politically dangerous issue it once was. He noted that Bush won in 2000 while talking openly about a shift to private accounts.

“The more specific, the better politically,’ said Graham. Such an effort ‘is an opportunity to tell the nation that we’re interested in solving real problems, that we’re going to level with the public on how to get there, and that we’re going to lead.’

“Critics and supporters alike say any serious move toward privatization would require strong bipartisan support because it would transform Social Security’s guiding principle. The program has been a social compact in which each generation of workers paid for the benefits of retirees. Under privatization, workers would have more responsibility for what their own retirement income might be.

“Many Democrats and liberal economists do not agree that a Social Security crisis exists or that such a big change is needed to save the system.

“Bush’s Democratic challenger, Sen. John F. Kerry, said last week that revamping the program required only a ‘tweak here, tweak there.’ In campaign appearances, Kerry tries to put Bush’s ideas in stark terms, telling crowds, ‘I will not privatize Social Security.’

“Opponents of private accounts contend that using tax credits and other incentives to help middle- and lower-income people save for their retirement could reduce the strain on the system.

“Social Security faces a long-term deficit, but calling it a crisis is an exaggeration,’ said Peter Orszag, an economist at the Brookings Institution, a nonpartisan think tank. ‘The scale of the problem is manageable. If your car has a flat tire, you don’t get rid of the car.’

“Polls show a majority of voters back the creation of personal accounts, particularly when the question is posed without mention of potentially higher taxes or shrinking benefits.

“A Gallup Poll last fall showed that more than six in 10 voters backed a shift to private accounts. But it also showed a stark generational divide—82% of voters younger than 30 backed the privatization proposal, but support steadily declined among other age groups, to less than 30% among those at least 65.”

### ***National Journal Tracks Efforts at Reform and Hopes for the Future***

Writing this week in the *National Journal*, Julie Kosterlitz tracks the recent history of efforts to reform Social Security. She also discusses the party divide that continues to make reform so controversial and assesses the opinions of various advocates and experts on how the reform debate will continue to play out. Two excerpts of the piece follow.

“For nearly two decades, the GOP has been haunted by the memory of how Senate Republican leaders’ bid to trim Social Security benefits cost Republicans control of the Senate in 1986. Bush’s embrace of a Social Security overhaul in his 2000

campaign seemed to mark a bold break with his party's taboo against even mentioning the program. But since Bush has been in office, the White House has sent mixed signals.

"Indeed, the past four years have been something of a roller-coaster ride for many small-government enthusiasts, employers fearful of higher payroll taxes, and some deficit-hawk centrists of both parties eager to see this Depression-era program radically changed. Besides [Derrick] Max's group [Alliance for Worker Retirement Security], standard-bearers include the Cato Institute, the Heritage Foundation, Americans for Tax Reform, the Club for Growth, and FreedomWorks (the group formed by the recent merger of Jack Kemp's Empower America and Citizens for a Sound Economy).

"Advocates' hopes soared when Bush convened a blue-ribbon commission in early 2001 to flesh out the idea of private accounts. But the commission, relying on signals from White House officials, produced several 'model' options rather than a specific reform plan that Bush would have to embrace or reject. The commission's subsequent bid for obscurity—it released its final report a few days before Christmas that year—was helped by the nation's post-9/11 focus on terrorism.

"After two years in the wilderness, private-account enthusiasts took heart last fall when Bush started making oblique promises to help individuals 'own a piece of their retirement,' in his speeches touting an 'ownership society.' The latter term encompasses several Bush initiatives to encourage individuals to accumulate enough personal assets to weather life-cycle risks—such as illness, or outliving one's retirement savings—while the government scales back its support programs."

PRA advocates were surprised by the president's State of the Union address, which was rumored to contain a strong endorsement of privatization, but which instead had only a passing reference to Social Security, Kosterlitz continues:

"Administration aides have said recently that the silence was merely strategic. 'If they had talked about it too early, no one would listen' in the crucial weeks before the election, Americans for Tax Reform President Grover Norquist says he was told.

"But the lack of presidential TLC has taken a toll. At least two issue-focused groups that were formed to spread the private-account gospel have all but closed down. One is SocialSecurityChoice.Org, an Evanston, Ill., group that was created in 2002 by veterans of the term-limits movement; it sponsored a \$500,000 advertising campaign in the midterm elections. 'We're in hiatus until the president provides leadership,' said John Tillman, president of the Glenview, Ill.-based Americans for Limited Government, which is currently tending the other group's phones and Web sites. For Our Grandchildren—a project indirectly bankrolled by Oregon door-and-window manufacturing magnate Dick Wendt—had staff in five early primary states but now employs just a skeleton crew.

"Private-account partisans would like to see Bush talk directly about Social Security—contending that in recent years, the issue has lost much of its political toxicity. Not only did candidate Bush survive tough attacks by Vice President Gore on the issue late in the 2000 campaign, they note, but, in the 2002 midterms, at least half a dozen

Republican Senate candidates won despite attacks on their support for private accounts. Even in a campaign dominated by national security and broad economic issues, they say, talking up Social Security can help. 'It energizes the base,' Max says.

"In the House, where most Republicans still see campaigning for private accounts as politically risky, several conservative GOP House members—Reps. Paul Ryan of Wisconsin, Sam Johnson of Texas, Jeff Flake of Arizona, and Pat Toomey of Pennsylvania—recently introduced bills that would let individuals steer about half of their payroll taxes into private accounts; that ceiling is about 50 percent higher than Bush's commission suggested.

"Opponents say Bush is reluctant to get into specifics, because diverting money from Social Security's revenue stream would require unpopular benefit cuts, massive borrowing, or both. 'The best that [advocates] can hope for is that Bush talks in coded words, gets re-elected, and they can say, therefore, he has a mandate,' says Roger Hickey, co-director of the labor-backed Campaign for America's Future, which ran ads in 2002 slamming congressional candidates who supported private accounts.

"Polling on the issue provides fodder for both sides. Upward of 60 percent of Americans routinely say they favor letting people put some of their payroll tax money into personal investment accounts, although the percentage briefly dipped into the high 50s, along with the stock market, in the latter half of 2002.

"But when confronted with possible consequences, such as high transition costs and investment risks, the public's support quickly diminishes, says John Rother, director of policy and strategy for AARP. The seniors lobbying group opposes proposals for diverting payroll taxes into private accounts.

"Public support for private accounts falls sharply with age—and voter turnout rates tend to increase with age. 'The people for whom this is a voting issue are older people, who are concerned about it,' Rother said.

"But the Social Security issue doesn't lock up seniors for the Democrats. Exit polls in 2000 showed that seniors in Florida—where Gore attacked Bush hard on his support for changing Social Security—were nearly evenly split between the two candidates. That was true even for those who named Social Security as an important issue. Although polls show that Democrats still enjoy a significant advantage on Social Security-related questions, exit polls over the past eight years reveal that that advantage has shrunk substantially—from 41 percentage points in 1996 to about 18 points in 2000. A March 2004 Gallup Poll showed Democratic candidate John Kerry leading Bush on Social Security by 14 points.

"That gives Bush an opening. 'Any time [one party] has more than a 20-point margin, it's difficult for the other side to engage on the issue,' Republican pollster David Winston said.

"Democrats say their advantage still matters—especially in a race where the parties are fighting for every last vote. 'It has been, and remains, a Democratic issue,

and it will be an advantage for Kerry,' said Doug Usher, a vice president in the Mellman Group, which does polling for the Kerry campaign.

"A few days after Bush's Annandale appearance, Kerry assured a friendly crowd of seniors at a recreation center in Henderson, Nev., that he would 'never privatize Social Security, ... cut the benefits,' or 'raise the retirement age in this country—period.' He contended that Bush's proposal would cost \$1 trillion and argued that the best medicine for the program is a healthy economy and periodic congressional 'tweaks.'

"Bush's defenders hope to parry such blows by painting Bush as a man with a plan to address a looming problem, while drawing Kerry out on his plans. Says the Cato Institute's Michael Tanner, 'What you will see is more pressure on Kerry to say what he would do' to shore up the nation's retirement program. After all, the first wave of Baby Boomers becomes eligible for benefits in just four years."

## ***Publications***

The Center for Retirement Research has just released a new issue brief, "How Do Individual Accounts Work in the Swedish Pension System?" by Annika Sundén. The brief, [available here](#) in PDF, looks closely at Sweden's Premium Pension program, a second-tier aspect to Sweden's recent pension reforms, which leave the bulk of retirement funds in a government-run PAYGO system.

**Edited by Brooke Oberwetter, [boberwetter@cato.org](mailto:boberwetter@cato.org). To subscribe or unsubscribe to *Social Security This Week*, please contact Feliz Ventura at (202) 789-5202 or [fventura@cato.org](mailto:fventura@cato.org).**