

Social Security Choice

SOCIAL SECURITY THIS WEEK

A WEEKLY NEWSLETTER ON SOCIAL SECURITY REFORM

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NYT: Social Security Will Be a Defining Issue This Election Year

Though national attention is currently focused elsewhere, Edmund L. Andrews [writes in the *New York Times*](#) that it's only a matter of time before the heated Social Security debate taking place behind the scenes reaches the surface. Andrews expects that Social Security will become a defining issue this election year, one that he says boils down to one basic question: "Should Americans save for old age collectively as a nation, or as individuals through private savings and investments?" Andrews goes on to discuss how the debate is developing and what we can expect to see from both sides of the issue as this election year unfolds. An excerpt of that discussion follows:

"Warning that Social Security is headed straight toward bankruptcy, Mr. Bush and supporters are building a case for partially replacing the old-age program with a new system of private accounts.

"Trustees for the Social Security and Medicare trust funds project that the Social Security fund for old-age benefits will be out of money by 2042 and that the Medicare trust fund will be insolvent by 2019—just 15 years from now.

"The danger is not in doing something—the danger is in avoiding the obvious,' said Terry Holt, a spokesman for the Bush-Cheney election campaign. 'You cannot just cling to the status quo, and people understand that.'

"Democrats are sounding their own alarms, accusing Republicans of trying to shred the social safety net and impoverish the elderly.

"The Republican approach is that you have individual responsibility for maintaining your retirement, and if you are unsuccessful then you should have done better,' said Representative Robert T. Matsui, Democrat of California.

"Though President Bush has refrained from any specific proposals on Social Security, advocacy groups are already mobilizing.

"SocialSecurityChoice.org, a conservative group that is pushing for private savings accounts, plans to spend up to \$2 million in May on television commercials that

will run in Washington, D.C., and in several swing states. ‘This is not an issue that the Democratic leadership can demagogue on anymore,’ said Bob Costello, the group’s president. ‘We are at the tipping point on this issue.’

“Liberal advocacy groups are firing back. The Center on Budget and Policy Priorities, a research group in Washington, has published a stream of reports contending that projected shortfalls for Social Security have been greatly exaggerated and can be fixed by modest adjustments to future benefits or taxes.”

For more information on why the private accounts hailed by the Cato Institute and SocialSecurityChoice.org are preferable to the “modest adjustments” sought by others, see Michael Tanner’s [“No Second Best: The Unappetizing Alternatives to Social Security Privatization,”](#) SSP No. 24, January 29, 2002.

Abdnor and Vargas: PRAs Are a Better Choice for Women and Minorities

Though Social Security as it currently exists could be considered a bad deal for just about everyone, it is particularly unfair to some women and minorities, according to Leanne Abdnor and Fidel Vargas of For Our Grandchildren. In an op-ed in the [Rocky Mountain News](#) discussing options for reforming Social Security, Abdnor and Vargas argue that while raising payroll taxes is unfair to young workers, cutting benefits disproportionately harms older women and minorities who frequently rely on Social Security benefits as their primary source of retirement income. Private Retirement Accounts, they conclude, are the solution for reform most likely to provide greater wealth and retirement security for all Americans. The text of the op-ed follows:

“Americans learned once again from the recent Social Security Trustees Report that our federal retirement system will begin running a deficit in 2018. While the clock continues ticking for all Americans, the alarm is already ringing loudly for women and minorities. We simply cannot afford for policymakers to continue hitting the snooze button.

“Our 1935-model Social Security system is in dire need of repair. Its original structure—where one generation of workers pays the benefits of their elders—was fine when more than 16 workers paid benefits for each retiree, but today just three workers support each retiree. And, when 80 million baby boomers are seeking retirement benefits, only two workers will be paying for each retiree.

“Attempting to sustain the system with tax increases would require a 50 percent increase in Social Security taxes. In addition, such a move would work against young workers seeking to build wealth for their families. But the alternative—sharp benefits cuts—would especially hurt older women and minorities who count heavily on Social Security.

“Nearly 40 percent of unmarried women rely on Social Security for 90 percent or more of their retirement income. And, according to a Social Security Administration

study, more than 40 percent of African-Americans' and Hispanics' retirement income comes from Social Security.

“The 1930s-style retirement system—designed at a time when the single-earner family was the norm—penalizes millions of working women who are married, single or divorced. Almost two-thirds of married working women receive no additional benefits for the taxes they contribute to Social Security. In addition, a low-wage single woman who worked and contributed her entire life actually receives lower monthly benefits than a stay-at-home spouse from a high-income household. In high-income households with one worker, the income producer (typically the husband) receives 100 percent of his earned benefit, while his wife receives a ‘spousal benefit’ of an additional 50 percent even though she did not contribute to the system. In order for a divorced woman to receive the ‘spousal benefit’ at retirement, she must have been married 10 years. However, the average duration of marriages that end in divorce in this country is less than eight years.

“If you happen to be a minority, Social Security is often an even worse deal. Take Hispanics, for example. While many Hispanics disproportionately benefit under the current system due to low incomes and longer life expectancies, the regressive payroll tax actually perpetuates a cycle of poverty because it takes the only money low-income workers could save or invest to build family wealth.

“Currently, a 30-year-old Hispanic female can expect just a 1.57 percent return from Social Security. Raising the payroll tax to pay retirees would have a devastating effect on many younger minorities’ ability to save money and invest in order to build wealth for their families.

“Why should young workers who will retire in 2035 be forced to live with a system that was invented in 1935? If that same young worker had an option to invest her payroll taxes and earn just 4.5 percent (a modest historical rate of return) she would build a nest egg that would double her income at retirement. Such an investment option would lead to greater wealth for all people, not just a select few.

“In 1960, the Supreme Court ruled that none of us has a right to Social Security benefits. An option to divert a portion of one’s Social Security taxes into a Private Retirement Account (PRA), would allow today’s workers to hold on to Social Security’s safety net, while gaining the means to achieve a more comfortable retirement. PRAs also would give women and minorities a much greater opportunity to build an inheritance that they can then pass to their heirs. Such a feature would give future generations a sizable nest egg for continued growth.

“Our country is built on a foundation of opportunity, fairness and innovation. It is time for policymakers to use those building blocks to renovate Social Security and provide a path to prosperity for all Americans.”

For more information on women and Social Security in particular, see Leanne Abdnor’s paper, “[Social Security Choices for the 21st-Century Woman](#),” recently published by the Cato Institute’s Project on Social Security Choice.

Harvey: Tax Time Illustrates the Case for Reform

Tax time has now come and gone, but Joyce Harvey of the pro-reform group For Our Grandchildren is reminding Americans that their total tax bill is much larger than the amount recently sent to Washington. In an [op-ed](#) for the *Seattle Post Intelligencer*, Harvey points out, “If you earn \$25,000 a year, you pay \$1,550 annually in FICA taxes (or payroll taxes) to support the Social Security retirement program.” She goes on to note that for young workers, a large portion of their income is being allocated to a program that they don’t believe will exist by the time they retire. Harvey’s op-ed, which follows, points out that younger generations would be best served by a system of private accounts and that today’s workers and voters should actively campaign in favor of such a system.

“Another April 15 is upon us and it’s time to pay your taxes. Unfortunately, your tax bill is already bigger than you may think.

“If you earn \$25,000 a year, you pay \$1,550 annually in FICA taxes (or payroll taxes) to support the Social Security retirement program. That’s a pretty big chunk of change—especially for a growing number of young workers who don’t believe Social Security will still be in existence when they retire.

“Three out of four Americans pay more in FICA taxes than in federal income taxes. Look at your pay stub sometime to see how much comes out of your paycheck. But wait, there’s more. Because a financial crisis looms over Social Security, the huge tax bite that falls on Americans will only get bigger unless something changes. Social Security has to be fixed—now.

“Social Security is a pay-as-you-go program. That means the taxes you pay in are immediately paid back out in the form of benefits to current retirees.

“Congress borrows any surplus payroll taxes to spend on other programs (paving roads, building schools, etc.) and puts IOUs in the Social Security trust fund. The program has always operated this way.

“Early in the program’s history, many workers paid into the program and relatively few collected benefits. By 1950, there were 16 workers for each retiree. That meant payroll taxes stayed low. Today, people live longer and birthrates continue to decline, so fewer workers must pay increasingly higher taxes to provide benefits for a growing number of retirees. Today the ratio is less than 3-to-1 and it will be 2-to-1 by the time today’s 30-year-olds get ready to retire from their jobs.

“Faced with this, Americans must do something now to fix the Social Security retirement program. One option is to let workers choose to put a part of their FICA taxes into personal retirement accounts. Added to the existing Social Security program, these accounts could give greater financial security to millions of future retirees.

“Young people deserve the same level of security that their parents and grandparents enjoy today. Encourage your elected officials to fix Social Security by adding personal accounts. Make your tax dollars count.”

The Economist Surveys Retirement

The March 27 issue of *The Economist* featured a special section on aging and retirement. The section includes a number of articles dealing with issues that relate both directly and indirectly to the Social Security debate. Though each article in the special section focuses on something different, the magazine's constant position is that retirement in the future will be fundamentally different from retirement as we know it today, and those nearing retirement should understand what that will mean to them in terms of working, saving, and planning.

In "Forever Young," the case is made that changing demographics must be addressed by policymakers in nations that have assumed responsibility for operating pension systems:

"The rise in the proportion of the world's old will be the century's defining demographic trend. In some countries it may also determine the nature of politics, rates of economic growth (aging countries will have slower rates of growth per head than those with younger populations) and global clout. In fact, three trends are running in parallel, each at a different pace. The first is a bulge in retirement, which will become noticeable in just over a decade. In many countries, especially in America, the birth rate rose sharply for some years after the end of the second world war. The older members of the American baby-boom generation are due to turn 62 (the minimum age at which Social Security allows early retirement) in 2008. The last baby-boomers retire in the late 2020s. But the generation, like a pig in a python, will guarantee an unusually large proportion of old folk—and then of very old folk—in the populations of most rich countries in this century's middle years.

"Its impact will be aggravated by a second trend: the widespread fall in fertility rates. In most countries women on average are not having enough babies to replace the people who die. Even in more fertile America, births only just equal deaths. In some countries, mainly in continental Europe and Japan, birth rates have been below replacement for a quarter of a century. When the baby-boomers retire, the size of the working population will plummet.

"That in itself is worrying enough. But there is a third problem: the old spend much more time in retirement than ever before. Life expectancy continues to rise, yet people are drawing their pensions earlier and earlier. A century ago most old people worked almost up to the end of their days. Now, by the age of 65, only 16% of men are still in the workforce in America and only 4% in continental Europe.

"Thus, a larger generation of old folk than ever before will need support for longer than ever before from a population of working age that is shrinking continuously in absolute size for the first time since the Black Death. And the level of that support is unprecedented. The triumph of Europe's welfare state and America's Social Security system has been more or less to eradicate poverty among the old. All rich countries—even America—now have health-insurance systems with near-universal coverage for the retired. The cost of these benefits, in effect, falls on those in work. This has prompted books with scary titles, such as "The Coming Generational Storm" by Laurence Kotlikoff, of Boston University, and Scott Burns, a journalist."

“Forever Young” goes on to make the important point that policy changes must come soon. “The longer that countries postpone the steps needed to make retirement sustainable, the more abrupt and damaging the transition will be. But given the will, change is possible.”

The link between retirement, shifting demographics, and public policy implications is further explored in the article “Enough to Live On.”

“To be old was once to be poor. No more: governments have taken over many of the costs and risks of aging. The burden of paying for pensions and health care therefore falls mainly on those in work. That has not seemed a problem as long as economies and the workforce have grown steadily and the old have been relatively few in number. However, within a decade that comfortable arithmetic will end. The fundamental decision about how to distribute the costs of old age between the elderly and their children will therefore become harder to resolve.

“In February, Alan Greenspan, chairman of America’s Federal Reserve Board, said that ‘we will almost surely be unable to meet’ the demands on resources that the retirement of the baby-boom generation will create. Almost everywhere else, the trouble is not—or not just—the baby-boomers, but the fall in fertility. The cost of pensions and of health care for the old must eventually be paid from the output of the current generation of workers. Even if birth rates recover a bit (and there are signs that they may), solving Europe’s pensions problem will be a nightmare. If the workforce shrinks and the number of dependants grows, no amount of fancy finance can fill the gap.”

When it comes to reform, the article continues, “two main issues dominate the debate: whether pensions should be financed from past savings or from current revenues; and whether the benefits they provide should be linked to past earnings or to some other predictable marker (‘defined-benefit’ schemes), or to savings and the return earned on them (‘defined-contribution’ schemes).”

Defined-contribution schemes, it is noted, “allow savers to see how much capital they have accumulated, which may make them think more carefully about the money they will need in retirement. Generally, American evidence suggests, they then decide to work longer.”

Other articles in the section deal with personal saving apart from government- or employer-funded pensions, the possibility of delaying or working part time during retirement, and what effect the aging population might have politically, given the political indifference of the much smaller generations that follow the boomers.

Events

The American Academy of Actuaries (AAA) will hold a news briefing on the Hill this Friday, April 16, 2004. The event, “Social Security Reform: Solutions Inside the Box,” will feature speakers Ron Gebhardtshauer, Eric Klieber, Bruce Schobel, and Robert Randall, all of the AAA. The event will start at 12:00 pm in the Rayburn House

Office Building, room B-354. For more information, contact Tracey Young at (202) 785-7872, or by e-mail at young@actuary.org.

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