

Don't Privatize Social Security!

The Bush administration's plan to partially privatize Social Security (SS) would be disastrous for the program and our nation. The program is not in as much trouble as the Bush administration claims, even taking into account the cautious Social Security annual forecasts used by most analysts. Unfortunately, the Bush administration is not giving us the full truth about their reasons to privatize.

Critical Numbers and Dates

Current forecasts say that Social Security will become insolvent in 2042, though even then incoming revenue would be able to cover about 70% of the benefit payments. The Congressional Budget Office (CBO) has revised their projected insolvency estimate date to 2052.

Here's what they're telling us about Social Security:

- The Social Security surplus is now about \$1.6 **trillion**.^{*} This surplus will peak at about \$3.8 trillion around 2022.
- Incoming payments will exceed payouts until about 2018. After that interest earned on these trillions will have to be spent to cover payouts.
- By 2028 we'll also have to spend surplus principle to cover payouts.
- By 2042 (or 2052 or...) all of the surplus will be used up so the only income to the system will be the monthly intake.

Surplus funds are invested in Government bonds to earn interest, but the plot thickens around 2018 because *all* of the surplus has been used by the Federal Government to pay other bills and will be closer to \$600 billion. So far, the Social Security surplus has been used to make the budget problem look better than it actually is. (The projected federal deficit for this year is approximately \$420 billion.)

Here's another way to put the so-called shortfall into perspective: "...in the next 75 years...President Bush's plan to lock in his tax cuts would cost about three times what it would take to fix Social Security. Now *that's* alarming." (New York Times editorial, pA26, 10/2/2004)

Solution #1: Just Lump it All in One Account

One school of thought says that we should lump income tax, social security tax into one account as we do now, but keep books to track of how much belongs to the Social Security account. It would be easy to "fix" Social Security: just pay it! We know that it's

^{*} Grasping trillions can be difficult. Consider that, roughly, in 2000 the GDP (Gross Domestic Product) was around \$10T, and the Federal budget was about \$2T. These normally grow each year).

a great program because today a senior is less likely to be beneath the poverty line than a non-senior, and before Social Security the opposite was true

One irony is that Social Security is a regressive tax! For example, a person who earns \$176K/year will be taxed at a rate half of that of a person who makes less than \$88K/yr. Why? Because Social Security tax is levied only on the first \$87,900 earned, as set in 1983. This \$87.9 increases to \$90K this year (2005).

Solution #2 - Increase Taxes--Slowly

The New York Times solution (from the editorial cited earlier in this article) says that we should increase taxes slowly. In 1983 only 10% of all wages escaped the payroll tax. Today that number is 15%. Over the next 40 years we could slowly increase this cap until we reach the point of 1983. That is, only 10% of all wages escape the payroll tax. We would then index this cut off figure and 10% of the Social Security shortfall problem would disappear. In addition, we would:

- *Tax earnings above the cut off, but at a lower rate.* This would be a rate such as 3 or 4%, imposed over a 40 year period. This alone would correct about 33% of the imbalance.
- *Link benefits to life expectancy.* Make small automatic reductions in future benefits and modest increases in the payroll tax. For example, raise the tax rate a tenth of a percent every 10 years until it reaches 12.7% (instead of the current 12.4%). For a 35 year old today, the benefit paid in 2036 would be a reduction equivalent to about \$300 a year. These two items together would cover about 33% of the long-term financial gap.
- *Expand the base of people covered.* Bring the 4 million state and local government employees into the system. Another 10% solution! Increase this 0.2% and the problem is solved!

The main point is that there are a variety of very reasonable ways to make up this projected shortfall...and there is time to work it out!

False Alarm

Even using the overly cautious projections of the Social Security Board of Trustees (OASDI), there is no Social Security crisis! We can make up the shortfall with changes that are smaller than any of the previous tuning adjustments that have been made so far. Eventually, the revenue "lost" by making President Bush's tax cuts permanent is four times the projected shortfall!

For example, if Bush's tax cuts were rolled back, just one fourth of that renewed revenue flow would easily cover the worst case Social Security projected shortfall. With more optimistic projections this would be about 5 or 6 times the projected shortfall! Even when the projected shortfall date is reached there would still be many resources available. For example, with the CBO projection of 2052 (instead of the OASDI's projection of

2042), the program could still fund 81 cents of every dollar of their obligation beyond 2052. This is not a major problem! This is fixable!

Shoddy Analysis

OASDI uses 1.8% for the GDP growth rate beyond 2020, and the White House Office of the Management of the Budget (OMB) uses 2.6%. The Stock Market just assumes traditional return on investments and traditional GDP has been 3.4%.

So, here is the scenario:

OASDI says Social Security will run out of money in 2042. The White House agrees even though their own projected growth rate is 45% ($2.6/1.8 = 1.45$) greater than the OASDI projection. We would invest our privatized account into the market, based on historical data (assuming on an even bigger 3.4% GDP!).

If the country's growth rate slows to 1.8%, will our market still perform the same? Has anyone looked into this? I asked my conservative, pro-privatizing, stockbroker neighbor if the market would perform as well with a GDP of 1.8% as it has with a GDP over 3.0%. He said of course not. That's not much more than trading water!

The Bush administration hasn't analyzed this because no one really believes in the OASDI forecasts and the driving reason to privatize is actually ideological (which is also Paul Krugman's opinion). There is a scary similarity to Iraq here. What the Bush administration says is their reason is not their real reason. And they were able to sell the Iraq war twice – with the November election as the second time. They have already convinced most young Americans that Social Security is on its last legs because it is virtually totally bankrupt. Using these tactics, protecting Social Security is a difficult battle to fight.

More Dishonesty and Gaps

We hear about how much an individual savings account would be worth by retirement time vs. traditional Social Security. This is like comparing apples and oranges because they are comparing an IRA to a *social security* (literal) program. And a pay as you go one at that! The Bush plan totally ignores the insurance part of the program that now covers the 40% of the 47M recipients of Social Security who are not retirees. Some 5M are spouses and children of disabled workers, 7M are spouses and children of deceased workers, and 5M are disabled workers.

Misleading inferences

Most citizens are led to believe that they could use their proposed new privatized accounts when they retire to buy a yacht (or Winnebago), fund a grandchild's college education, or try Las Vegas (or Cache Creek). In the plans presented so far, this is not so: all end up with the purchase of an annuity! This misconception is a really big deal. The annuity makes sense because the government doesn't want destitute seniors! *Unlike Social Security, annuities are not adjusted for inflation.* If these billions of dollars start coming in adjustable annuities would likely appear, but at a big cost.

A Trillion Plus Dollar Problem

Migrating a portion of Social Security to Privatized accounts will create a very quick shortfall in the remaining cash flow. About a trillion bucks are needed to cover this for the first ten years alone. This is in addition to the trillions of dollars of Social Security surplus funds that have been “borrowed” by the Federal Government to help pay general expenses. Today, the amount borrowed in this manner is around \$1.6T (that’s trillion). In 2022 it will peak at about \$3.8T – that’s a capital T, which rhymes with P which stands for Privatization. Yes we have trouble here in River City...and in Alabama, Maine,...Ohio, California...throughout this whole land.

Baby Boomers are Not the Problem!

In 2052, the youngest baby boomers will be 88, and the oldest 106. So the boomers are not the problem. The more realistic projected shortfall wouldn't occur until 2052 when these boomers are not a significant factor. However, using this argument is a convenient and, alas, effective ploy that is used by the Administration to scare the public and to promote their privatizing agenda.

What Really Drives the Urgency to Privatize?

The problem is not the baby boomers. It is not 2052. It is the looming obligation to have to start paying money back to the Social Security Trust Fund around 2018. The privatizers' thinking is, blame the boomers... let us save this program by privatizing... along the way reduce benefits... and blur the obligation that the government has to repay the Social Security Trust fund.

Privatizing is not Working in Britain and Chile!

From Paul Krugman’s Op-Ed article in the 12/17/2004 New York Times:

“Privatizers who laud the Chilean system never mention that it has yet to deliver on its promise to reduce government spending. More than 20 years after the system was created, the government is still pouring in money. Why? Because, as a Federal Reserve study puts it, the Chilean government must ‘provide subsidies for workers failing to accumulate enough capital to provide a minimum pension.’ In other words, privatization would have condemned many retirees to dire poverty, and the government stepped back in to save them.

The same thing is happening in Britain. The British Pensions Commission warns that those who think Mrs. Thatcher’s privatization solved the pension problem are living in a ‘fool’s paradise.’ A lot of additional government spending will be required to avoid the return of widespread poverty among the elderly – a problem that Britain, like the US, thought it had solved.”

Overhead Problems

The existing Social Security program operates on less than 1% overhead. It is a very efficient program. Estimates on Privatizing accounts overhead are around 15% to 20%. Think of millions of accounts, each putting \$60 in to their private account every two

weeks. And periodically moving the money around. And not just Wall Street, but the government would have to be involved here. This leads to...

False Government Concern

If investing in the market is what President Bush and company think is best, then they could lower the overhead by having the Social Security people invest \$X in the market. But this concept is anathema to them. Which leads to: It's an ideology thing.

A Few Words About Long Range Forecasting

Picture the 1929 actuaries trying to estimate GDP, fertility rates, life expectancy, inflation, immigration rates for 2004. Daunting. And the world keeps changing faster and faster. These 1929 folk could not even see October! The point is that these long range estimates must be taken with a large grain of salt. For example, today we are faced with a possible jobless recovery of the economy because of outsourcing. What we do know is that Social Security has been around since the 1930s and has performed its job very well. Sure, it has been adjusted periodically. This is to be expected, but the overall results have been excellent. As previously mentioned, before Social Security seniors were more likely to be beneath the poverty line than non-seniors. Today the opposite is true.

Summary

Social Security is **not** in dire straights. The projected shortfall that it faces can be corrected by modest adjustments, and these adjustments are smaller than any other set of periodic adjustments we've made to Social Security so far. Social Security does not need a radical change such as Privatization or partial-Privatization, and Privatizing would exacerbate rather than alleviate the fiscal issues.

Privatization will not work because of the excessive overhead and the MULTI- trillion dollar shortfall that would have to be filled in order to honor commitments to the existing Social Security participants. Furthermore, the government is misleading the public regarding the features of privatized accounts: doing whatever one wants to with this "nest egg" would not be an option.

However, this Administration was able to sell the Iraq war based on faulty reasons not once but *twice*. They are skilled. Social Security is a very math related program, and math tends to be a tad dry for most citizens. So the task is difficult. We must not let President Bush succeed in his privatizing effort.

Learn more by checking out the many good resources available on the Internet:

- The Century Foundation www.tcf.org
- Paul Krugman , Op-Ed articles in the New York Times (12/7 and 12/17/04, e.g.)
- TomPaineCommonsense www.tompaine.com
- Nat'l. Committee to Preserve S.S. and Medicare www.ncpssm.org

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