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SOCIAL SECURITY'S 70TH ANNIVERSARY: SURVIVING 20 YEARS OF REFORM

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Social Security turned 70 on August 14, although no national celebration marked the occasion.[1] Rather, our top policymakers in Washington continue to suggest that the system is "unsustainable." While our nation's most successful social program, and among its longest lived, has allowed generations of Americans to live with dignity in retirement, many think it is time to retire Social Security itself. They claim it is necessary to shift more responsibility to individuals and to scale back the promises made to the coming waves of retiring baby boomers.

Even the nonpartisan Social Security Administration has been enlisted in the effort to lower expectations, posting on its website the following caution to today's 26-year-old: "Unless changes are made, when you reach age 62 in 2041, benefits for all retirees could be cut by 26 percent and could continue to be reduced every year thereafter. If you lived to be 100 years old in 2079 (which will be more common by then), your scheduled benefits could be reduced by 32 percent from today's scheduled levels." Private accounts, lower benefits, and—perhaps—higher taxes are the prescribed remedy for "unfunded" trillions of commitments we have made to tomorrow's seniors.

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In this note, I provide a brief assessment of the curious transformation of America's most popular and efficient safety net into a program that is widely regarded as requiring thorough reform.

There is no question that Social Security has been under attack by well-organized and well-funded opponents for the past two decades. As my colleague Max Skidmore has documented, the enemies of the program have been there from the beginning, but they have had little success until recently (Skidmore 1999). Originally, the program was criticized on the basis that it was socialistic. However, the framers of the Social Security Act anticipated such claims and consequently formulated the program as if it were an insurance plan, with payroll taxes that could be counted as "contributions" and "benefit payments" that bore some relation to the contributions. Americans came to believe that they earned benefits because they "paid into" the program. And because the program was never means tested, it enjoyed wide support. Hence, rather than socialistic welfare, the program has been viewed as little different from a pension plan. For several decades, this misconception effectively quashed criticism, so the program was expanded, rather than cut (Wray 2001).

However, beginning in the 1980s, the critics seized on an apparent weakness. Slower economic growth after 1970, lower birth rates, longer life spans, and especially the coming retirement of a wave of baby boomers all supposedly threatened the long-run financial viability of Social Security. The enemies of the program formulated a two-pronged attack. First, they began a campaign to convince younger people that because of shaky finances they would never collect benefits equal to what they paid into the program (Skidmore 1999). This became an increasingly easy sell for younger, high-income workers because the redistributive aspects of the program provide fairly low "money's worth" returns for the "pension" provided by Social Security. (Note that the debate mostly ignored all the "nonpension" aspects of the program, such as disability and survivors' benefits, which make it a good deal for just about all Americans.) Second, the Greenspan Commission was formed in 1983 to resolve the long-run financial problems with "reforms" that included large payroll tax increases and a gradual rise of the normal age of retirement (Papadimitriou and Wray 1999a). These changes reinforced the claim that Social Security was a bad deal for younger workers, who were already seeing take-home pay fall during a period in which labor was under attack by the Reagan administration.

After the Greenspan Commission had "solved" the financial problems, the Social Security Administration adopted increasingly pessimistic assumptions for its long-run forecasts—as documented by Skidmore (2001) and by actuary David Langer (2000). Not surprisingly, a "looming financial crisis" reappeared, and hysteria about reforming Social Security was revived. Taxes would have to be raised, benefits would have to be cut, and, more importantly, the return on Trust Fund assets would have to be increased. As the stock market performed well throughout most of the 1980s and then picked up the pace in the 1990s, the enemies saw a chance to privatize the program while playing the role of savior. At the same time, the "friends" of Social Security, mostly Democrats and Big Labor, also saw a chance to exploit popular fears. They would play along with the enemies, pretending there really was a financial problem, so that *they* could save Social Security and thereby win votes. Polls consistently show that voters trust Democrats more on Social Security; hence, given a choice between Republican schemes to "save" the program through privatization or Democratic plans to "save" it by placing the Trust Funds off limits, the voters would choose the Democrats.

I have been writing about Social Security since the late 1980s, and in 1990, I published a critique of *Can America Afford to Grow Old?,* a book by Henry Aaron, Michael Bosworth, and Gary Burtless that argued that the only way to take care of baby boomers would be to immediately increase national saving (Wray 1990, 1990–91; Aaron et al. 1989; Aaron 1990–91). This could be done, according to the authors, by running budget surpluses, adding to national savings, and increasing the size of the Trust Fund. Hence, this book could be seen as a road map for the evolving Democratic party position during the Clinton years. However, I argued at the time that a larger Trust Fund could not in any way provide for future retirees, nor would it add to national savings. Rather, the Trust Fund represents a leakage that lowers aggregate demand; all else being equal, this lowers economic growth and thus makes it more difficult to take care of future retirees. Aaron wrote a response to my piece, arguing that he had thought that such "vulgar Keynesianism" was "blessedly extinct" (Aaron 1990–91). According to Aaron, running budget surpluses to add to the Trust Fund would indeed increase saving and lower interest rates, thus stimulating investment and economic growth, making it easier to take care of retirees.

As we now know, the Clinton budget did turn sharply toward surplus, and those surpluses were projected at the time to continue for at least a generation. A number of economists advocated "saving" this surplus for future retirees. As laid out in the plan by Aaron, et al., President Clinton proposed to take a portion of each year's surplus and add it to the Trust Fund (Wray 1999a, 1999b). Essentially, this would allow double counting of the surplus run by Social Security, since most of the budget surpluses accrued during the Clinton years were due to payroll taxes that far exceeded program benefits. During the 2000 presidential race, Al Gore used Social Security "lockboxes" as a primary campaign issue, confusing an internal bookkeeping operation (as Social Security's assets in the Trust Fund equal the Treasury's liabilities to Social Security, this is a case of the government owing itself) with availability of "finance" for the government as a whole. A wide variety of economists (including Aaron) embarrassed themselves by claiming that this was "good economics," going so far as to sign a petition in support of the plan (Wray 1999b).

I was told by economic advisors to top Democrats and big unions that they realized lockboxes were nonsense but believed it was politically pragmatic to endorse irregular accounting as a means to "save" the program. I responded that there was no need to run budget surpluses in order to credit Social Security's Trust Fund; the government can immediately credit the Trust Fund with trillions of dollars of assets, offset by the Treasury's commitment to make timely benefit payments when and as necessary (Wray 1999b). Most importantly, I worried about the long-term damage that would be done to the program by creating a false crisis and then resolving it with a preposterous gimmick. Of course, the Democrats' strategy did backfire: Gore lost the election, the Clinton budget surpluses brought down the economy and morphed into huge deficits "as far as the eye can see," and President Bush took on Social Security "reform" as a major goal of his administration. Ironically, the Republicans now quote President Clinton whenever Democrats try to deny that the program faces a crisis, leaving Dems in the untenable position of either admitting they were lying in the 1990s or that they are lying now (Wray 2005).

During the Clinton years I wrote a series of pieces critical of alternative plans to "save" Social Security, including those proposed by Democrats as well as those advanced by Republicans (Wray 1999a, 1999b; Papadimitriou and Wray 1999a, 1999b). After reading one of these critiques (Papadimitriou and Wray 1999b), Charles P. Blahous, policy director for Senator Judd Gregg (R-NH), engaged me in a series of e-mail exchanges. He accepted my critiques of the Clinton plan, but was bothered by my critique of the Gregg-Breaux proposal (which, briefly, included partial privatization, a government-subsidized savings plan, and a combination of benefit cuts and tax hikes; Blahous had apparently played some role in formulating the plan, and many of its features were included in later reform proposals). He also insisted that there really was a Social Security crisis and that the only feasible solution would be to privatize. He raised a number of issues that appeared at the time to be rather bizarre: that the crisis would begin as soon as tax revenue fell below benefit payments (that is, long before the Armageddon date cited by many economists as the year in which the Trust Fund is expected to be depleted); that faster economic growth would make the problem *worse*; that under current law, benefits would have to be cut by more than a quarter as soon as the Trust Fund was depleted; and that Social Security was a terrible deal for blacks and for women. More interestingly, when President Bush appointed his Reform Commission to study the problem, none other than Blahous was picked as executive director.[2] Blahous's hand could be seen all over the various reports issued by the Commission, with many of the same arguments that he had made previously in e-mails to me. The Commission claimed that Social Security was "broken" and required a "complete overhaul"; it bemoaned the bad deal cut for women and minorities; it engaged in a sleight of hand by comparing its "reforms" against "current law benefits" that were actually a quarter below those promised in the current benefit formula (none of the proposed reforms came close to providing the legislated benefits); it claimed that the present value of Social Security's shortfall was $3.2 trillion; and it proposed partial privatization and benefit cuts as the solution (Wray 2001).[3] What appeared then to be bizarre claims are now commonplace.

However, terrorism and security issues forced Social Security to the back burner during the first Bush term. After reelection, Bush felt he had a mandate to return to privatization of Social Security. At first, supporters of privatization claimed that it would resolve the "financial crisis"; eventually, the President admitted that the private accounts would worsen the program's finances (Wray 2005). Finally, he returned to the Commission's suggestion to drop wage indexing of future benefits (at least for all but the lowest-income workers) and hinted that he would consider elimination of the cap on wages subject to taxation (Wray 2005). If successful, these changes would substantially erode the support of middle- and upper-income earners, who would face huge cuts to benefits and higher taxes. Partial privatization would almost certainly lead to lower retirement payments for many lower-income workers (with management fees eating up the returns on their small accounts). Further, as many middle- and upper-income workers would opt for the privatization alternative, the amount of benefits received directly from Social Security by them would fall toward insignificance (Krugman 2005). Over the long haul, the nonprivatized portion of Social Security would be converted to a "welfare" program, important only to low-income people. This could be the last straw for what has long been America's most successful and popular government program.

The truth is that Social Security does not, and indeed *cannot*, face any financial crisis. It is a federal government program and as such cannot become insolvent. Social Security benefits are paid in the same way that the federal government makes expenditures for all of its other programs: by cutting a Treasury check or, increasingly, by directly crediting a bank account. Social Security is an unusual program only in that we pretend the payroll taxes "pay for" benefits; in reality, trying to maintain a balance between these flows is purely a politically inspired accounting procedure. Any federal government spending must be accounted for, but it cannot be *financially* constrained by specific or even general tax revenues. Further, the Trust Fund does not and cannot provide finance for Social Security. So long as the full faith and credit of the U.S. government stands behind the promised benefits, they can and will be paid, whether the Trust Fund has a positive or negative balance. Many proponents of the current system who understand this economic reality still want to accumulate a Trust Fund on the argument that it provides political protection. Perhaps the Trust Fund provided cover at one time, but it no longer serves even that purpose. It is precisely because there is a Trust Fund that the privatizers are making headway: if there were no Trust Fund, there would be nothing to privatize. Indeed, some of the privatizers see the trillion and a half dollars in the Trust Fund as a potential boost to flagging equity markets. Further, the eventual "exhaustion" of the Trust Fund plays a critical role in all of the schemes to increase returns on assets through privatization. Hence, the irregular accounting only hinders development of a clear understanding of the issues involved.

Social Security provides a substantial measure of security for aged persons, survivors, and disabled persons—and their dependents. It has never missed a payment, nor will it ever do so, as long as the full faith and credit of the U.S. government lies behind the program. Reform might be desired, and might even be necessary, but not because of any mythical looming financial crisis. Our nation is undergoing slow but important demographic changes that probably warrant informed discussion of the future shape of Social Security. While the baby boomers receive all the attention, other demographic and economic changes may be more important, including a greater proportion of female-headed households, higher immigration and the rising proportion of "minority" populations (already a majority in several states), and increasing economic inequality. Combined with the disappearance of employer-provided defined benefit pension plans and reduced employment security, these trends actually might strengthen the arguments for more generous and secure publicly provided safety nets—*not* for benefit cuts and privatization. However, none of these challenges rises to the level of a programmatic crisis; we will have years and even decades to make adjustments to Social Security should we decide they are necessary. In the meantime, happy 70th birthday, Social Security, with many happy returns.

Notes

1. Interestingly, the only reference to the anniversary available on the Social Security Administration's website is an *Orlando Sentinel* editorial by Jo Anne B. Barnhart, commissioner of Social Security, who notes that while the program has paid "approximately $8.4 trillion in benefits to nearly 200 million people," and while the benefits for "our parents, grandparents, and great-grandparents . . . are secure and will be paid . . . the same cannot be said for my teenage son and his friends" (Barnhart 2005).
2. Before that appointment, Blahous served as executive director of the business-sponsored Alliance for Worker Retirement Security from June 2000 through February 2001. He joined the National Economic Council on February 26, 2001, and now serves as special assistant to the president for economic policy.
3. See Diamond and Orszag (2002a) for a careful analysis of the Commission's reports. Blahous tried to defend the claims made for the various "reforms" in a memo characterized by *New York Times* columnist Paul Krugman as "hysterical. The number of non sequiturs and misrepresentations Mr. Blahous manages to squeeze into just a few pages may set a record" (Krugman 2002). See Blahous's response (2002) and Diamond and Orszag's rejoinder (2002b).

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