

Withholding Judgment on the Social Security Commission Report

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[1] The issuance of an interim report by the Social Security Commission appointed by President Bush was followed by a firestorm of protest. (See *Tax Notes*, July 30, 2001, p. 589 and p. 715 of this issue.) The immediate attention to potential conflict, however, detracted from a closer look at what the report said and -- just as importantly -- didn't say. In particular, the report hints that the commission may tackle issues surrounding the treatment of the poor -- especially as represented among women and some minorities -- in ways that go well beyond anything to do with individual accounts. At the same time, the report appears to carefully avoid boxing the commission in on what types of reforms it will eventually suggest.

[2] The front pages of most newspapers today closely resemble their sports pages. Fights generate the most attention and elicit sales. When it comes to social security reform, le combat du jour is over the creation of individual accounts. In point of fact, any individual account proposal is likely to involve about 2 percentage points of earnings or payroll. The existing old age, survivors, and disability (OASDI) tax rate, however, is 12.4 percentage points. Even if money for individual accounts were carved out of the existing rate -- and this is still unclear -- this particular fight is likely to be over, at best, about 15 percent of the funds that are spent on social security.

[3] Add in Medicare and other programs for the elderly, and the share falls to 10 percent or less as we move into the future. Moreover, the net amount of money for such individual accounts might not come entirely out of the existing social security revenues; almost all proposals at a minimum have sought some other source of funds, such as general revenues, to finance some transition to a new system.

[4] What this means is that the fight over individual accounts is like focusing on the hind end of the dog. It ain't the tail, but it ain't the whole dog either. The basic benefit system in social security is much larger and, for that reason alone, deserves considerable attention in any reform effort.

[5] Here the commission's report can be cast in a light very different from that given it by most of the press. The interim report -- largely written by staff and accepted by the commission -- gave special attention to the impact of the system on some lower-income women and minorities. Admittedly, much of the language centered on rates of return, which brings to mind immediately the issue of whether one can get a higher "rate of return" in a reformed system that might include some amount of individual accounts.

[6] The rate of return issue is quite complicated, but a variety of research, including one performed by Lee Cohen, Adam Carasso, and myself, has shown that the redistribution to many lower-income groups under social security through a progressive benefit formula is offset significantly by higher mortality rates among those groups. Since all returns in the current system are in the form of an annuity, the higher mortality rates disfavor lower income individuals.

[7] At one level, then, one can interpret the report's language on women and minorities as simply favoring individual accounts if returns on those accounts do not have to be annuitized. Therefore, it is not surprising that many have interpreted this language to be just another pitch for individual accounts.

[8] However, the issue is much more complex. The existing system has many ways in which it redistributes to rich and poor alike. Among the most important are spousal and survivor benefits. Unlike private pensions, the worker does not pay for any additional spousal and survivor benefit through an actuarial reduction in his or her own benefit, but instead the burden is shifted to the general social security taxpayer.

[9] Well, guess who has no access to this very large and generous additional transfer system? Single people, including many low-income single female heads of household who have scattered work histories because they

bear the full brunt of child raising. Another problem with the existing system is that the very old tend to have lower benefits than younger beneficiaries. The net consequence is that the current system has an unacceptably high poverty rate associated with it.

[10] By raising the issue of returns to minorities and women, therefore, the commission may be indicating some willingness to tackle their problems in the basic system, whatever its eventual size. I have been attempting to get this item on the social security agenda for several years now, beginning with a proposal for a minimum benefit that was adopted by the earlier bipartisan National Commission on Retirement Policy. The current system could easily remove all the elderly from poverty, and it does not. Its need for reform extends well beyond issues related either to trust fund imbalance or saving in individual accounts.

[11] A second aspect of the report has also received little attention -- what it did not say. In the end, it did not make excessive promises about what a reformed system could provide, nor, as best as I can tell, did it bind the commissioners from considering any policy change one way or the other. Some have criticized the report for not laying down more specifics on its final suggestions, but I think this would have been a mistake. Having been involved in many reform processes over the years, nothing throws a monkey wrench into the works more than having constraints put on the process at the beginning before all the details have been worked out. Revenues are always inadequate for what people want to do, and compromises are required. For the commission to have boxed itself in at the beginning would have been a procedural mistake with potentially grave consequences later.

[12] In the end, therefore, the report may be "under- interpreted" for what it suggests about dealing with the problems of the poor and "over-interpreted" for what it says about the reforms it will finally propose. For myself, I think I will wait and see.

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