# ARTICLE

# THE STRIKING SUPERIORITY OF SOCIAL SECURITY IN THE PROVISION OF WAGE INSURANCE

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*From the original opposition to Social Security in the 1930s, through the controversy over the 2005 privatization proposals of George W. Bush, and now extending to the current Social Security debate and the so-called Bowles-Simpson proposal, the basic function of Social Security has been misrepresented, obscured, and misunderstood. Social Security is not a program of forced savings for life's expensive contingencies; nor is it a welfare program designed simply to relieve poverty. Rather, Social Security has from its inception been a program of wage insurance. Social Security insures wages against loss due to death, disability, or old age. Universal wage insurance performs an extremely valuable social function. As this Article demonstrates, no private arrangement designed to replace wages in the event of retirement, disability, or death can come even remotely close to Social Security in efficiency of its administration, security of its defined benefits, fairness of its distribution, or reach of its coverage. In light of a looming retirement income crisis, the United States should expand Social Security, while also taking the modest steps necessary to restore the program to long-range actuarial balance.*

## I. INTRODUCTION

Privatization is in vogue.[1] In recent years, state and federal legislatures have enacted schemes requiring or permitting private enterprises to run func-

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[1] *See* PAUL STARR, *The Meaning of Privatization*, YALE L. & POL'Y REV. 6–41 (1988); *see also* Joe Bailey, *From Public To Private: The Development of the Concept of "Private*," 69 SOC. RESEARCH 15 (2002); *see generally* Gillian E. Metzger, *Privatization as Delegation*, 103 COLUM. L. REV. 1367 (2003).

tions traditionally operated by the public sector, including prisons,[2] schools,[3] and the military.[4] Those advocating that the private sector take over functions traditionally operated by the public sector often seem to have a simplistic belief: to paraphrase the musical composer and lyricist Irving Berlin, anything the government can do, the private sector can do better.[5]

That view fails to recognize that the federal government performs some functions more efficiently and effectively than the private sector. Social Security is one of them. As this Article explains, Social Security is more universal, fair, efficient, secure, and effective than its private sector counterparts are or could ever be, irrespective of how those private arrangements are structured.[6] This striking superiority is rarely debated explicitly.[7] Instead, the debate over whether Social Security should be "privatized," or even what that means, generally occurs outside of any rigorous, intellectual framework.

This leads to remarkable ironies. Democratic policymakers vigorously opposed and ultimately defeated President George W. Bush's controversial Social Security proposal, which he advocated shortly after his re-election in 2004.[8] The Democrats objected that the proposal "privatized" Social Secur-

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[2] In 1990, 7,000 prisoners were housed in private prisons. By 2010, that number had grown to 126,000 or nine percent of the nation's prison population. Michael Brickner & Shakyra Diaz, *Prisons for Profit Incarceration for Sale*, 38 HUM. RTS. 14, 14–17 (2011).

[3] From 1999 to 2011, the number of students enrolled in charter schools increased from 350,000 to over two million. *The Public Charter Schools Dashboard: Students Overview*, NAT'L ALLIANCE FOR PUBLIC CHARTER SCHOOLS, http://dashboard.publiccharters.org/dashboard/students/page/overview/year/2012 (last visited Oct. 30, 2012); *see also* Diane Ravitch, *Why Public Schools Need Democratic Governance*, THE PHI DELTA KAPPAN, Mar. 2010, at 24, 24–27, *available at* http://www.jstor.org/stable/27755663.

[4] P.W. Singer, *Corporate Warriors: The Rise of the Privatized Military Industry and Its Ramifications for International Security*, INT'L SECURITY, Winter 2001–2002, at 186, 186–220; P.W. Singer, *Outsourcing War*, FOREIGN AFF., Mar.–Apr. 2005, at 119, 119–32.

[5] Paraphrasing the hit song, "Anything You Can Do, I Can Do Better," from the musical ANNIE GET YOUR GUN. (Rodgers & Hammerstein Organization 1946), *available at* http://www.rnh.com/show/5/Annie-Get-Your-Gun.

[6] *See* discussion *infra* Part IV. President Franklin Roosevelt understood this point. In a major address right before the 1936 election, just a year after the enactment of Social Security, he pointed out that Social Security "is far more favorable to [workers] than any policy that any private insurance company could afford to issue." President Franklin Roosevelt, Speech at Madison Square Garden (Oct. 31, 1936), *available at* http://millercenter.org/president/speeches/detail/3307. For more about the speech, see *infra*, note 86.

[7] One exception was a structured debate the author engaged in with Mark Warshawsky, a member of the Social Security Advisory Board at a conference sponsored by the National Academy of Social Insurance on January 28, 2012. During the debate, Warshawsky acknowledged that his objection to Social Security included ideological underpinnings. Though the debate was not transcribed, it was videotaped. The concession can be seen at 35:07; the question from the author, which provoked the question, begins at 32:50. *See* Mark Warshawsky & Nancy Altman, Meeting Today's Challenges in Social Security, Health Reform, and Unemployment Insurance, Session IV—A Debate—Two Strategies for Retirement Security: More Savings or More Social Security? (Jan. 27–8, 2011), *available at* http://www.nasi.org/events/119/agenda-videos.

[8] For details of the Bush proposal, see discussion *infra* Part III.B. For an account of the fight over the Bush plan, see NANCY J. ALTMAN, THE BATTLE FOR SOCIAL SECURITY: FROM FDR'S VISION TO BUSH'S GAMBLE 271–96 (2005).

ity.[9] The Democratic Party continues to express its opposition to "privatization" of Social Security.[10] Nevertheless, many powerful Democrats have embraced proposals that would privatize Social Security in much the same way that the Bush proposal would.[11] Moreover, these modern-day proposals, all championed by those who claim to support Social Security, would inexorably transform Social Security into what was being proposed as an alternative by the Republican Party in 1936, and indeed by opponents of the program in a steady march ever since.[12]

To see the similarities in all of these proposals and to understand why the private sector cannot compete with Social Security's efficiency, security, fairness, or universality, it is essential to understand what Social Security is and what it is not. Once Social Security's basic structure and function are understood, one sees that the label "privatization" confuses more than clarifies. When free of the blinders imposed by the limiting term "privatization," careful, rigorous analysis brings into sharp focus Social Security's striking superiority to private sector alternatives.

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[9] The term "privatization" was first used by the conservative Cato Institute's Project of Privatization and has been adopted by Republican politicians. However, Frank Luntz, a Republican messaging consultant, informed Republican candidates that "privatizing" Social Security was unpopular. By that time, the name was closely associated with the Bush proposal, and Democrats and the media continued to use it. *See id.* at 285.

[10] *See* 2012 Democratic National Platform, *available at* http://www.democrats.org/democratic-national-platform ("We will block Republican efforts to subject Americans' guaranteed retirement income to the whims of the stock market through privatization."). *See also* Stephen Ohlemacher, *Dems Slam Ryan Over Social Security Privatization*, ASSOCIATED PRESS, Aug. 19, 2012, *available at* Factiva, Doc. No. APRS000020120819e88j0008p.

[11] As explained in Part III.B, if President George W. Bush's private accounts proposal is to be considered privatization, so would the Social Security proposals put forward by the co-chairs of President Barack Obama's National Commission on Fiscal Responsibility and Reform (hereinafter, "the Bowles-Simpson Commission"). *See infra* text accompanying notes 134–44. Ironically, the co-chairs' proposal (hereinafter, the "Bowles-Simpson proposal") has been embraced by a number of leading Democratic elected officials, notwithstanding their stated opposition to "privatizing" Social Security. For instance, Senator Kent Conrad (D-N.D.) was a member of the Bowles-Simpson Commission and supported its recommendations. *See, e.g.*, KENT CONRAD, ADDITIONAL VIEWS OF KENT CONRAD (2010), *available at* http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/MemberStatements.pdf ("Eleven of us . . . have agreed on a far-reaching package that would . . . secure the solvency of Social Security for the next 75 years."). But he claims to oppose "privatization." *See Issues*: *Social Security*, OFFICIAL SENATE WEBSITE OF KENT CONRAD, http://www.conrad.senate.gov/issues/socialsecurity.cfm (last visited Oct. 31, 2012) (Conrad has "[f]ought against [Social Security] privatization schemes that would significantly reduce guaranteed benefits and require massive borrowing."). Similarly, Minority Leader Nancy Pelosi (D-Cal.) has said that she would vote for Simpson-Bowles but opposes privatizing Social Security. *See* Ryan Grim, *Nancy Pelosi Says She'd Back Simpson-Bowles Plan*, HUFFINGTON POST (Apr. 27, 2012), http://www.huffingtonpost.com/2012/04/27/nancy-pelosi-simpson-bowles-social-security-medicare_n_1453323.html ("If it were actually Simpson-Bowles, I would have voted for it.").

[12] *See infra* text accompanying notes 147–49. In this Article, the label "opponents" refers to people who are on record in favor of fundamentally changing Social Security. It is hard to know who is truly opposed to Social Security, because, today, Social Security is praised by virtually all politicians, even those, like President George W. Bush, who would radically change or undo it. *See infra* text accompanying note 170.

Part II of this Article analyzes what Social Security is and is not. Part III discusses the ambiguity in today's imprecise use of the word "privatization" in relation to Social Security.[13] In so doing, the discussion illuminates the ironies embedded in today's debate over Social Security: it highlights the fundamental similarity of leading proposals championed by many of today's proponents and self-proclaimed opponents of "privatization." In addition, it spotlights the similarity of those proposals to past attempts to radically transform Social Security. Part IV analyzes how and why Social Security is more efficient, secure, fair, and effective than all of its private sector counterparts. Part V proposes how to increase the economic security of America's working families, in light of Social Security's superiority over the alternatives. Finally, Part VI concludes.

## II. What Social Security Is and What It Is Not

The Social Security Act of 1935 consisted of eleven titles,[14] but only Titles II and VIII created the program commonly referred to today as "Social Security."[15] Although enacted at the height of the Great Depression, those two titles were not designed to alleviate the immediate conditions of the Depression. The statute provided that Social Security's first monthly benefits would not be paid out until 1942, more than six years after the program's enactment, and more than twelve years after the Depression's start.[16]

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[13] Others have noted different ambiguities in the term "privatization" when applied to Social Security, though those ambiguities tend to be more tangential, less central, and less fundamental than the ambiguity focused on in this Article. *See, e.g.*, Don Fullerton & Michael Geruso, *The Many Definitions of Social Security Privatization*, Economists' Voice (Mar. 2006), http://www.princeton.edu/~mgeruso/images/The%20Many%20Definitions%20of%20SS%20Privatization.pdf.

[14] *See* Social Security Act of 1935, ch. 531, Pub. L. No. 74-271, 49 Stat. 620 (codified as amended at 42 U.S.C. § 301 (2006)). The titles in the original Act have been expanded, replaced, and added to; so today, the Act includes twenty-one titles, including Social Security (i.e., Old-Age, Survivors and Disability Insurance), Medicare, Unemployment Insurance, Supplemental Security Income, Medicaid, Temporary Assistance for Needy Families, and child welfare and adult social services. *See Compilation of the Social Security Laws*, Soc. Sec. Admin., http://www.ssa.gov/OP_Home/ssact/ssact-toc.htm (last visited Oct. 31, 2012).

[15] Title II, Federal Old-Age Benefits, was separated from its dedicated source of revenue, Title VIII, in an effort to strengthen the defense against the claim that the scheme was unconstitutional. *See* Altman, *supra* note 8, at 82–83.

[16] The 1939 amendments moved the start date for monthly benefits to 1940. *See* Social Security Act Amendments of 1939, sec. 201, Pub. L. No. 76-379, § 202(a), 53 Stat. 1360, 1363–64. The statute requires that workers achieve insured status as a prerequisite to receiving benefits. Insured status is achieved by obtaining the requisite number of quarters of coverage, which are earned through employment in service that is covered by Social Security. Today, there are three types of insured status: fully insured, currently insured, and insured for disability insurance benefits. 42 U.S.C. §§ 414, 423(c)(1) (2006). The delayed start in the original statute allowed workers the time necessary to work the requisite number of quarters. Most mark the start of the Great Depression from the infamous stock market crash, colloquially known as "Black Tuesday," which occurred on October 29, 1929. *See, e.g.*, *Stock Market Crash of 1929 and the Effects on the Economy*, The Great Depression, http://web.olivet.edu/gradusers/kwatts1/stockcrasha.htm (last visited Nov. 1, 2012).

Those who designed the legislation recognized that welfare was all that could be implemented quickly to alleviate the poverty and hardship caused by the Depression.[17] Consequently, the 1935 Act authorized immediate appropriations for several new welfare programs.[18] For the long term, however, Congress believed that a better solution—one that prevented poverty in the first place—should be created.[19]

In an economy where most are dependent on wage income, the better solution was and remains insurance against the loss of wages. Workers and their families can lose wages as the result of unemployment, disability, death, or old age.[20] Insurance, paid for during working years, allows workers and their families to maintain their standards of living and prevent poverty if and when those insurable events occur and wages are lost. Unemployment insurance, though not commonly called "Social Security," was included in the 1935 Act.[21] So was old-age insurance.[22] Survivors or life insurance was added in 1939,[23] and disability insurance was added in 1956.[24] The last three forms of wage insurance—government-administered old-age annuities, life insurance, and disability insurance—constitute what in the United States is called "Social Security."[25]

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[17] For a description of the pressing need for so-called noncontributory pensions, or means-tested old age benefits, see generally *The Report to the President of the Committee on Economic Security*, Soc. Sec. Admin., http://www.ssa.gov/history/reports/ces/ces5.html (last visited Nov. 1, 2012) [hereinafter *Report*] ("Only non-contributory old-age pensions will meet the situation of those who are now old and have no means of support. Laws for the payment of old-age pensions on a needs basis are in force in more than half of all States and should be enacted everywhere.").

[18] Titles I, IV, and X provided grants to the states for means-tested, welfare programs of old-age assistance, aid to dependent children, and aid to the blind, respectively. These had immediate effective dates. *See* Social Security Act of 1935, ch. 531, 49 Stat. 620.

[19] *See Report*, *supra* note 17 ("The satisfactory way of providing for the old age of those now young is a contributory system of old-age annuities. This will enable younger workers, with matching contributions from their employers, to build up a more adequate old-age protection than it is possible to achieve with non-contributory pensions based upon a means test.").

[20] Inability to pay for health care costs can cause destitution even without the loss of a job. The Roosevelt administration considered the inclusion of universal health insurance in its proposed legislation, but the administration was concerned that the controversial nature of universal health insurance could bring down the entire bill. *See* Altman, *supra* note 8, at 39, 54–56, 67–68.

[21] *See* Social Security Act of 1935, tits. III, IX, ch. 531, 49 Stat. 620. Other nations have a broader definition of Social Security, including unemployment insurance. *See What Is Social Security?*, Int'l Soc. Sec. Admin., http://www.issa.int/Topics/About-social-security (last visited Nov. 1, 2012) [hereinafter *What Is*].

[22] *See* Social Security Act of 1935, tits. II, VIII, ch. 531, 49 Stat. 620.

[23] Social Security Act Amendments of 1939, sec. 201, Pub. L. No. 76-379, § 202(a), 53 Stat. 1360, 1363–64.

[24] Social Security Amendments of 1956, Pub. L. No. 84-880, 70 Stat. 807 (codified as amended in scattered sections of 42 U.S.C.). For a description of this legislation, see Charles L. Schottland, *Social Security Amendments of 1956: A Legislative History and Summary*, Soc. Sec. Bull., Sept. 1956, *available at* http://ssaonline.us/policy/docs/ssb/v19n9/v19n9p3.pdf.

[25] The term "Social Security" has a broader definition in other industrialized countries. *See What Is, supra* note 21. For how the term is used in this Article, see *supra* author's note.

Though Social Security is sometimes described as part of the social welfare system,[26] those who view Social Security simply as a government-transfer program financed by a tax like any other tax,[27] fail to recognize that it is wage insurance, as distinct from welfare or savings.[28] Indeed, opponents of Social Security have sometimes sought to mischaracterize the program as welfare and sometimes as forced savings, but it is neither. Subsection A of this Section explains what makes Social Security insurance. Subsection B explains the sharp and important distinction between insurance, including Social Security, and welfare.[29] Subsection C highlights the sharp and important distinction between insurance, including Social Security, and savings.

### *A. Social Security Is Insurance*

People faced with the possibility of a loss can protect themselves against the financial consequences of that loss, if it were to occur, by forming a group with others who face the same risk. Each member of the group contributes an amount of money related to the average likelihood that the

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[26] *See, e.g.*, Lawrence H. Thompson, *The Advantages and Disadvantages of Different Social Welfare Strategies*, Soc. Sec. Bull., Fall 1994, *available at* http://www.ssa.gov/policy/docs/ssb/v57n3/v57n3p3.pdf.

[27] *See, e.g.*, Cong. Budget Office, Social Security and the Federal Budget: The Necessity of Maintaining a Comprehensive Long-Range Perspective (2002), *available at* http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/36xx/doc3650/no3august.pdf ("Social Security and Medicare, by their size, are poised to crowd out other government spending and limit the availability of funding for other government functions.").

[28] With industrialization and urbanization, as workers become dependent on wages for the first time, wage insurance has been the response internationally. *See* Altman, *supra* note 8, at 9–11. Because Social Security is insurance designed to replace wages, Social Security has, from the beginning, had a Retirement Earnings Test to ensure that a beneficiary claiming retirement benefits has indeed retired. The original act prohibited benefits to anyone who had any income, but that was quickly determined to be too stringent. It has been liberalized many times since then. *See generally*, Larry DeWitt, *Research Note #7: Brief Legislative History of the Retirement Earnings Test*, Soc. Sec. Admin. (Apr. 2000), http://www.ssa.gov/history///ret.html. As a result of legislation enacted in 2000, the test no longer applies to people at or above the statutory "retirement age." *See Exempt Amounts, 1975–1999*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/rteahistory.html (last visited Nov. 1, 2012); *see also Exempt Amounts Under the Earnings Test*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/rtea.html (last visited Nov. 1, 2012). As a consequence of that legislation, Social Security would be more accurately described as providing annuities irrespective of wage loss for those workers who claim benefits on or after reaching the statutory retirement age. For those retiring before the statutory retirement age, there is an "exempt amount," which is an amount that can be earned and still receive all earned benefits. The exempt amount in 2012, for those reaching age sixty-six after 2012, is $14,640. For earnings above that amount, benefits are reduced $1 for every $2 earned. *See Exempt Amounts Under the Earnings Test*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/rtea.html (last visited Nov. 1, 2012). The Social Security Administration recalculates benefits when beneficiaries reach the statutory retirement age to credit any months in which benefits were not received as a result of the application of the Retirement Earnings Test. *See Retirement Planner: Can You Take Your Benefits Before Full Retirement Age?* Soc. Sec. Admin., http://www.ssa.gov/retire2/applying2.htm (last modified Oct. 18, 2012).

[29] In addition to insurance and welfare, a third arrangement, colloquially known as demogrants, involves flat payments to everyone who meets a particular demographic characteristic. *See infra* note 145 and accompanying text.

loss will occur. If and when the loss occurs, the group member or members experiencing the loss are paid from the group fund. Each group member is protected from a large possible loss by making a smaller but certain contribution.

This financial exchange is the essence of insurance, and it is the essence of Social Security. Like other group insurance, Social Security involves making payments and sharing the financial risk of particular, defined losses. In the case of Social Security, the risk is the loss of wages to support oneself and one's family in the event of disability, death, or old age.[30] The payments are the periodic payments mandated by the Federal Insurance Contributions Act ("FICA").[31] These FICA payments are paid by employers and workers, generally as deductions from pay checks, and held in trust for the sole purpose of paying Social Security benefits and related expenses.[32]

Those FICA payments are today commonly referred to as payroll taxes, but they are better understood as mandatory insurance contributions or premiums, rather than mere taxes.[33] In that regard, it is instructive to pause and note that the acronym for the Social Security payment is "FICA," which, as stated above, stands for the "Federal Insurance Contributions Act," the legislation authorizing these payments.

The Federal Insurance Contributions Act was enacted in 1939,[34] well before the days of paid political public relations consultants and so-called spin doctors. It is only relatively recently that policymakers have named legislation in the manner of Madison Avenue advertising—titles like the No Child Left Behind Act of 2001,[35] the USA PATRIOT Act of 2001,[36] the Defense of Marriage Act,[37] and the proposed Repealing the Job Killing Health Care Law Act.[38] In stark contrast, Franklin Roosevelt named his bills plainly

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[30] For discussion of a fundamental change enacted in 2000 for workers claiming benefits on or after the statutory retirement age, see *supra* note 28.

[31] Social Security Act Amendments of 1939, sec. 201 Pub. L. No. 76-379, § 608, 53 Stat. 1360, 1387. ("This subchapter may be cited as the 'Federal Insurance Contributions Act.'").

[32] 42 U.S.C. § 401 (2006). The surplus of income over outgo is, by law, invested in Treasury bonds at fair market interest rates, which are carefully accounted for and fully repaid with interest. *Id.* at § 401(d) ("Such investments may be made only in interest-bearing obligations of the United States or in obligations guaranteed as to both principal and interest by the United States."). As a result of the Social Security Amendments of 1983, about fifteen percent of Social Security's annual income results from the taxation of the benefits of higher income beneficiaries, the proceeds of which are placed in trust and dedicated to Social Security. *See* Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102 (2012).

[33] Calling FICA payments "payroll taxes" is a misnomer in two respects. First and most obviously, workers do not have payrolls; only employers do. More importantly, the deductions are better understood as insurance premiums, as explained in the text.

[34] *See* Social Security Act Amendments of 1939, Pub. L. No. 76-379, 53 Stat. 1360.

[35] Pub. L. No. 107-110, 115 Stat. 1425 (2002).

[36] Pub. L. No. 107-56, 115 Stat. 272 (2001).

[37] Pub. L. No. 104-199, 110 Stat. 219 (1996).

[38] H.R. 2, 112th Cong. (2011).

and straightforwardly. His tax bills were labeled Revenue Acts,[39] his legislation to ensure the right of workers to unionize, the National Labor Relations Act,[40] and his Federal Insurance Contributions Act[41] specifies the contributions workers and their employers make in exchange for Social Security wage insurance.

FICA requires that workers pay, and employers match, 6.2 percent[42] of workers' wages up to a maximum amount of wages.[43] Some scholars have criticized the Social Security FICA contributions as a regressive tax.[44] Seen simply as a tax, FICA contributions are structured regressively with respect to workers making above and below the maximum. All workers pay the same flat rate on their first wages earned, but the highest paid workers pay a zero percent rate on wages above the maximum.

FICA's structure no longer appears regressive, though, when one understands that Social Security is wage insurance and that the FICA payments are premiums, rather than mere taxes. The wages upon which FICA contributions are assessed are the wages that are insured against loss.[45] The employee earning at the maximum and the employee earning ten times that amount each pay the same insurance contribution or premium for their Social Security protection. If an insurable event occurs—death, disability, or old age—they receive the same Social Security benefits, all other circum-

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[39] *See e.g.*, Revenue Act of 1935, Pub. L. No. 74-407, 49 Stat. 1014; Revenue Act of 1937, Pub. L. No. 75-377, 50 Stat. 813.

[40] Pub. L. No. 74-198, 49 Stat. 449 (1935).

[41] Social Security Act Amendments of 1939, Pub. L. No. 76-379, 53 Stat. 1360.

[42] The 6.2% rate, which has been the rate since 1990, was reduced to 4.2% with respect to 2010 and 2011 for workers as a purported temporary measure to stimulate the economy. It is scheduled to expire on December 31, 2012. *See* Patient Protection and Affordable Care Act, Pub. L. No. 111-148, § 9015(b)(2), 124 Stat. 871 (2010) (amending 26 U.S.C. § 1401 (2006)). *See also infra* text accompanying note 125 for a more complete discussion of the reduction.

[43] The maximum taxable wage base is indexed to average wages. In 2012, the maximum taxable wage base is $110,100. In other words, FICA is applied to the first $110,100 of wages earned in employment covered by Social Security. *Contribution and Benefit Base*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/cbb.html (last visited Oct. 31, 2012).

[44] *See, e.g.*, Michael J. Graetz, *The Troubled Marriage of Retirement Security and Tax Policies*, 135 U. Pa. L. Rev. 851, 864 (1987). *But see* Nancy J. Altman, *The Reconciliation of Retirement Security and Tax Policies: A Response to Professor Graetz*, 136 U. Pa L. Rev. 1419, 1424–38 (1988).

[45] Social Security's benefits are based only on the wages on which FICA contributions are made. A worker's benefit is calculated by indexing and averaging his or her career earnings to determine the average indexed monthly earnings ("AIME"). In determining the AIME, only wages up to the maximum are counted. The AIME is translated into a monthly benefit by inserting it into a benefit formula. The formula for an individual who attains age 62 in 2013, or who dies or becomes disabled in 2013 before age 62, is the sum of:

(a) Ninety percent of the first $791 of his/her average indexed monthly earnings, plus

(b) Thirty-two percent of his/her average indexed monthly earnings over $791 and through $4,768, plus

(c) Fifteen percent of his/her average indexed monthly earnings over $4,768.

*Primary Insurance Amount*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/piaformula.html (last visited Oct. 31, 2012).

stances being the same.[46] These workers pay the same price, though different percentages of their incomes, for private insurance, food, cars, or any other economic good or service. In the same way, they purchase their identical Social Security benefits for the same dollar amount, even though the dollar amount translates to a different percentage of total earnings.

Workers with total earnings at or below the maximum pay the identical proportion of their wages for their Social Security insurance. Though the FICA contributions or premiums are proportionate, Social Security's benefits are progressive.[47] Workers who have earned higher salaries, on average, over their careers receive benefits that are larger in absolute dollars, but are smaller in proportionate terms, than those received by lower paid workers, despite having paid the same flat contribution rate. For example, a worker who earns around $40,000 a year and claims Social Security benefits starting at age 65 in 2012 receives a Social Security benefit of around 40 percent of his or her wages, while a worker earning around $20,000 a year receives an annual benefit starting at age 65 of around 55 percent of his or her salary.[48]

Some have argued that Social Security's explicitly redistributive benefit formula makes Social Security welfare,[49] but it does not. Redistribution is not a feature unique to welfare. All group insurance redistributes. Life insurance redistributes from those who live beyond average life expectancies to those who die prematurely. Old age annuities do the opposite, redistributing from those who die prematurely to those who live beyond their average life expectancies. Disability insurance redistributes from those who do not become disabled to those who do.

In recognition that those with lower wages or periods of unemployment have less ability to save and are likely to need a higher proportion of their pre-retirement wages to maintain their standards of living, the designers of Social Security created Social Security's benefit formula to redistribute from

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[46] In addition to wages on which contributions are assessed, benefits depend on factors such as the age at which benefits are claimed. *See infra* note 63.

[47] Because the formula looks to career average earnings, workers who have a lifetime of low wages or periods of unemployment, receive larger proportionate benefits, though smaller benefits in absolute dollar amounts, than workers with higher earnings or fewer years of unemployment. The result is produced mainly by means of Social Security's progressive benefit formula. *See supra* note 45. The formula achieves progressivity in much the same way as the federal income tax. The formula brackets wages and replaces a larger percentage of earnings with respect to the lower brackets, or first dollars of wages earned, than with respect to the subsequent brackets, or last dollars at higher wage levels. *Primary Insurance Amount*, Soc. Sec. Admin., http://www.ssa.gov/oact/cola/piaformula.html (last visited Oct. 31, 2012).

[48] To be precise, Social Security replaces, for workers claiming at age 65 in 2012, 27.4% of the wages of workers who consistently earned the maximum amount of covered wages; 40.8% of a lifetime of scaled medium wages; and 55% of a lifetime of scaled low wages. Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102, at 142–43 (2012). For a more complete discussion of replacement rates, including how they are gradually declining, see *infra* text accompanying notes 226–28.

[49] *See, e.g.*, Peter J. Ferrara, Social Security: The Inherent Contradiction (1980).

those with higher wages over their careers to those with lower wages.[50] That design is perfectly consistent with the idea of group insurance and pooled risk. Looking forward, at the start of working life, even people with careers that promise high remuneration do not know whether they will, at the end of their lives, have had a lifetime of high wages. They might have had to take time off from those careers as the result of illness or accident, for example, or other intervening events that change the trajectory of their earnings. Social Security, which is often referred to as "social" insurance, redistributes in this and other ways that are not generally found in private group insurance but are socially beneficial.[51] Nevertheless, for all the reasons articulated in this section and the next one, Social Security, including its progressive benefit formula, is completely consistent with the concept of insurance and completely inconsistent with the concept of welfare.[52]

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[50] The original benefit formula was based on cumulative earnings rather than average earnings. *See* Social Security Act of 1935, Pub. L. No. 74-271, 49 Stat. 623. In 1939, the benefits were changed so that they were based on average earnings, which allowed those closer to retirement to receive larger benefits. *See* Social Security Act Amendments of 1939, sec. 201, Pub. L. No. 76-379, § 202(a), 209(e), 53 Stat. 1360, 1363–64, 1376; *see also* Robert M. Ball, *The 1939 Amendments to the Social Security Act and What Followed*, *in* THE REPORT OF THE COMMITTEE ON ECONOMIC SECURITY OF 1935 AND OTHER BASIC DOCUMENTS RELATING TO THE DEVELOPMENT OF THE SOCIAL SECURITY ACT 165–67 (50th anniversary ed. 1985).

[51] *See* ROBERT M. BALL, SOCIAL SECURITY: TODAY AND TOMORROW 4–11 (1978).

[52] Social Security has had, from its enactment, other design features found in insurance. All insurers keep reserves to ensure that they can cover the cost of benefit payouts. From its start, Social Security has maintained a reserve. For most of the history of Social Security, the reserve has been contingent, equal to about one year of outgo. In anticipation of the retirement of the baby boom generation, the trust funds have been built up in the last few decades. *See* H.R. DOC. NO. 112-102, at 142–43 (2012). In recognition that Social Security must be cautious and trustworthy with the contributions of American workers, though, the law has required, from the beginning, that those reserves be invested only in the safest, most secure investment available—interest-bearing obligations backed by the full faith and credit of the United States. Social Security Act of 1935, Pub. L. No. 74-271, § 201(b), 49 Stat. 622. This has led to claims, from the beginning, that Social Security's reserves are simply "IOUs," or gimmicks, involving the government simply lending money to itself. *See, e.g.*, DAVID C. JOHN, THE HERITAGE FOUND., MISLEADING THE PUBLIC: HOW THE SOCIAL SECURITY TRUST FUND REALLY WORKS (2004), *available at* http://www.heritage.org/research/reports/2004/09/misleading-the-public-how-the-social-security-trust-fund-really-works. The law has also required, from the beginning, valuations using sound actuarial assumptions. *See, e.g.*, Social Security Act of 1935, Pub. L. No. 74-271, § 201(b), 49 Stat. 622. For budget purposes, five years is a reasonable time horizon, and anything over ten years is quite distant. In contrast, because insurers typically face a time lag—often, a substantial time lag—between the receipt of premiums and the expenditure of benefits, they must, to be prudent, employ lengthy periods of valuation, well beyond ten years. As a responsible insurer, Social Security's Board of Trustees employs over forty actuaries whose job it is to project the program's income and outgo for the next seventy-five years. The projections appear in a report that the Trustees present each year to Congress. Annual reports have been issued every year once benefits began to be paid. *See* Larry DeWitt, *Research Note #14: Key Data From Annual Trust Fund Reports*, SOC. SEC. ADMIN. (June 2001), http://www.ssa.gov/history///trustchart.html.

### *B. Social Security Is Not Welfare*

The distinction between Social Security and welfare is fundamental but not well understood today.[53] Viewing Social Security simply as a government-transfer program, as it commonly is in today's dominant policy frame, blurs this essential distinction. Social Security and welfare are intrinsically different, having developed from two very different and distinct historical roots.

Humans have always sought security from life's dangers. Generally, the most effective actions against life's insecurities have been collective in nature. Collective action to enhance physical security has taken the form of armies, police forces, and militias. Collective action to enhance economic security has taken two separate forms, welfare and insurance—each quite distinct from the other.

The antecedents to modern welfare programs can be traced from biblical prescriptions, such as the command that "thou shalt not wholly reap the corners of thy field, neither shalt thou gather the gleanings of thy harvest. And thou shalt not glean thy vineyard . . . ; thou shalt leave them for the poor . . . ."[54] In England, the practice of voluntary tithing to the church to help the poor evolved into compulsory tithing, then into the English poor laws, and then to America's welfare laws, which were transplanted from England by the colonists. Those early welfare arrangements evolved into today's welfare programs.[55]

In contrast, a second, equally rich but fundamentally different tradition—social insurance—developed where workers dependent on wages sought to protect themselves and their families from the loss of earnings by banding together and pooling their risk. As far back as the Middle Ages in England and Europe, individuals who had a common trade or craft joined together to form mutual aid societies or guilds, which, in addition to regulating the craft, provided a variety of wage-replacement benefits to its members.[56] Similarly, in the mining districts of central Europe as early as the sixteenth century, workers formed customary funds, which provided benefits for sickness and accidents.[57] Building on these models, Chancellor Otto von Bismarck was the first to provide compulsory, universal social insurance, and the concept spread quickly around the world.[58] Barbara Armstrong, the chair of President Roosevelt's working group developing Social Security, was a leading expert on social insurance. Prior to her work on Social Secur-

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[53] For an excellent essay highlighting the difference between welfare and social insurance, see Bob Ball, Insuring the Essentials: Bob Ball on Social Security 33–51 (2000).

[54] *Leviticus* 19:9–10 (King James).

[55] *See generally* Blanche D. Coll, Perspectives in Public Welfare (1969).

[56] Ball, *supra* note 51, at 12.

[57] Ball, *supra* note 51, at 12–13.

[58] *See* Abe Bortz, Historian, Soc. Sec. Admin., Lecture on the History of Social Security, *available at* http://www.ssa.gov/history/bortz.html.

ity, she had authored *Insuring the Essentials*, a landmark treatise that exhaustively surveyed social insurance programs in other countries.[59]

Welfare programs involve arrangements among financially unequal parties—those materially better off providing assistance to those less advantaged. Eligibility for welfare is based on need and is determined by an examination of the potential recipient's income and assets to ensure that he or she is really in need. Welfare benefits are generally an amount designed to provide the recipient with enough to get by, to subsist, as judged by the provider.[60]

In contrast, insurance programs involve arrangements among equals who are pooling their risks. Eligibility for insurance is based on achieving insured status, irrespective of need. Benefits result from experiencing the event covered by the insurance. They are paid irrespective of need.

Welfare programs are essential as long as there is poverty, but they have inescapable, inherent weaknesses not found in insurance arrangements. The necessity of determining need inherently discourages work and savings. If the potential recipient is earning enough to get by, as defined by the arrangement, he or she is not in need of the community's help. As a result, those people who can earn no more than the designated welfare amount have no financial incentive to work, and, indeed in a sense, are disadvantaged, compared to their nonworking counterparts, by their work effort.[61] Moreover, if a person has savings upon which to draw, he or she is also not in need of the assistance of others. As a result, because only those with no or limited savings can receive benefits, thrift is penalized. Those who have been thrifty in the past generally must exhaust their savings before they are eligible to receive welfare.

Insurance has none of these shortcomings. Indeed, if the insurance is wage insurance, where work is a condition of reaching insured status and the insurance benefit is higher as a result of higher wages and more years of work, the arrangement rewards increased work effort. Unlike welfare, savings do not disqualify a person from the receipt of insurance benefits. Rather, savings provide an additional source of income from which to draw, and so are encouraged.

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[59] In addition to surveying social insurance programs, the treatise also examined other arrangements including welfare for the old and minimum wage laws. *See* BARBARA NACHTRIEB ARMSTRONG, INSURING THE ESSENTIALS: MINIMUM WAGE PLUS SOCIAL INSURANCE—A LIVING WAGE PROGRAM (1932); *see also* Lillian Liu, *Special Study #8: Foreign Social Security Developments Prior to the Social Security Act,* SOC. SEC. ADMIN. (Dec. 2001), http://www.ssa.gov/history/pre1935.html.

[60] *See* BALL, *supra* note 51, at 4–11.

[61] In response to the inherent work disincentives, some programs have benefits phase out, rather than end abruptly. *See* MICHAEL C. BARTH ET AL., TOWARD AN EFFECTIVE INCOME SUPPORT SYSTEM: PROBLEMS, PROSPECTS, AND CHOICES 34–35 (1974). Other programs simply include a work requirement. *See Temporary Assistance to Needy Families (TANF) Overview*, DEP'T HEALTH & HUMAN SERVS., http://www.hhs.gov/recovery/programs/tanf/tanf-overview.html (last visited Nov. 2, 2012).

A comparison of Social Security to the Supplemental Security Income program[62] ("SSI"), illuminates the stark differences between the two forms of arrangements. Like Social Security, SSI provides benefits to people who are old[63] and people with disabilities,[64] but unlike Social Security, eligibility for benefits is based on need. Under Social Security, both work and savings are encouraged.[65] Under SSI, both work and savings are discouraged.[66]

Under Social Security, the higher one's earnings that are insured and the longer one works, the larger the dollar amount of the benefit received.[67] In contrast, both earned and unearned income reduce SSI payments, which, in 2012, provides a maximum monthly federal benefit of $698.[68] Nonwage income, such as Social Security benefits, reduces a recipient's monthly SSI benefit dollar for dollar, with the exception of a disregard of the first twenty dollars of income.[69] For every dollar earned in a month, one's SSI benefit is reduced by fifty cents, with the exception of a disregard of the first sixty-five dollars of earnings.[70]

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[62] 42 U.S.C. §§ 1381–1383(f) (2006).

[63] Low-income seniors who are sixty-five or older are eligible for SSI. 42 U.S.C. § 1382(c)(a) (2006). All workers who have achieved insured status and are sixty-two or older are eligible for Social Security's old age benefits.

[64] SSI has one set of rules for low-income people who are disabled and a somewhat more lenient set of rules for low-income individuals who are blind. For example, people with disabilities cannot engage in substantial gainful activity, defined as earning more than $1,010 a month in 2012. That requirement does not apply to people who are blind. *See Understanding Supplemental Security Income If You Are Disabled or Blind*, SOC. SEC. ADMIN., http://www.ssa.gov/ssi/text-disable-ussi.htm#sgact (last visited Nov. 1, 2012).

[65] Past work is encouraged because the effort is reflected in the benefit levels. *See supra* text accompanying note 45. Because Social Security was originally intended for people who were retired, it imposed a retirement test, which discouraged work. Concerned about the impact on work effort, Congress repeatedly liberalized the retirement test and eventually eliminated it for workers who claimed benefits on or after their statutory retirement age. Those who claim benefits prior to their statutory retirement age, but have their benefits reduced as the result of the Retirement Income Test, will have their benefits recalculated and will receive higher benefits once they reach their statutory retirement age. *See supra* note 28.

[66] To alleviate the inherent work disincentives of welfare, SSI allows a small disregard and a phasing out of benefits, rather than a dollar-for-dollar offset, for earned income, as described in the text. The dollar-for-dollar reduction of unearned income above the $20 disregard constitutes conceptually a 100% tax. Losing 50¢ for every dollar earned above the disregard is equivalent to a 50% tax rate, a higher rate of taxation than the top marginal rate of the federal income tax code. In order to encourage people with disabilities who are receiving federal benefits to return to work, SSI has additional provisions to alleviate the work disincentives inherent in welfare arrangements. *See Understanding Supplemental Security Income—SSI Work Incentives*, SOC. SEC. ADMIN., http://www.ssa.gov/ssi/text-work-ussi.htm (last visited Nov. 1, 2012).

[67] *See supra* notes 43–45 and accompanying text.

[68] States may choose to supplement the federal maximum and a number do. *See* 42 U.S.C. § 1382(c) (2006).

[69] The $20 income disregard can be applied against either unearned or earned income but not both. 42 U.S.C. § 1382(c)(b)(2) (2006).

[70] *See Understanding Supplemental Security Income—SSI Income*, SOC. SEC. ADMIN., http://www.socialsecurity.gov/ssi/text-income-ussi.htm (last visited Nov. 1, 2012).

Past work is irrelevant unless it has resulted in savings of more than $2000; savings of that amount disqualify an individual from receiving SSI.[71] Indeed, if resources are given away or sold, not only by a potential recipient but also by the recipient's spouse or co-owner, for less than fair market value, the potential recipient may be ineligible for SSI for up to thirty-six months.[72]

In contrast, savings are immaterial to the determination of Social Security benefits. Because Social Security's benefits are too low to allow most workers to maintain their standards of living in retirement, savings are implicitly encouraged.

In recognition of the desirability of supplementing Social Security's modest benefits, the Internal Revenue Code provides preferential tax treatment for those who save for retirement.[73] Those who take advantage of the preferential tax treatment will receive their full Social Security benefits, but will be ineligible for SSI if the savings, together with other countable assets, are in excess of $2000. Even if the retirement savings account is below the threshold for eligibility for SSI, the withdrawals from it will be offset dollar for dollar, once the twenty-dollar monthly disregard of income is reached.

In order to ensure that the income and assets limitations are not exceeded, SSI recipients are required to regularly report numerous details of their lives. Every month, for example, they must take or mail all pay stubs to the Social Security Administration.[74] They must report any changes to the income of spouses, if living together, as well as changes in assets, including those of their spouses.[75] They must report, within ten days, changes in living arrangements, such as a change in the number of people in the household.[76] SSI recipients who receive help with food, utilities, or housing costs must report that and suffer a reduction in their benefits.[77] In contrast, Social Security beneficiaries are not required to file burdensome and intrusive reports about the details of their lives.

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[71] 42 U.S.C. § 1382 (2006). The limit is $3000 for a married couple. Primary residences and a select list of personal property items are not counted toward the assets limit. *See Understanding Supplemental Security Income—SSI Resources*, Soc. Sec. Admin., http://www.ssa.gov/ssi/text-resources-ussi.htm (last visited Nov. 1, 2012).

[72] *See Understanding Supplemental Security Income—SSI Spotlight on Transfers of Resources*, Soc. Sec. Admin., http://www.ssa.gov/ssi/spotlights/spot-transfer-resources.htm (last visited Nov. 1, 2012).

[73] *See infra* note 116.

[74] *See Reporting Wages for People Who Receive Supplemental Security Income (SSI)*, Soc. Sec. Admin. (Jan. 2011), http://www.ssa.gov/pubs/10502.html#a0=0.

[75] *Id.*

[76] *Id.*

[77] *See Understanding Supplemental Security Income—Living Arrangements*, Soc. Sec. Admin., http://www.ssa.gov/ssi/text-living-ussi.htm (last visited Nov. 1, 2012). If recipients live with their children and do not reimburse them totally for the cost of food and shelter, for example, their SSI benefits may be reduced by up to one-third. *See Understanding Supplemental Security Income—SSI Spotlight on the One-Third Reduction Provision*, Soc. Sec. Admin., http://www.ssa.gov/ssi/spotlights/spot-one-third-reduction.htm (last visited Nov. 1, 2012).

The different way that assets and income are treated in the determination of benefits results directly from the inherent difference between welfare and insurance programs like Social Security. Welfare is designed by those financially better off for people who are already poor; insurance is designed by equals to prevent members of the group from becoming poor in the first place.[78]

Welfare discourages work; wage insurance encourages it. Welfare discourages savings; wage insurance encourages workers to save to the extent it simply provides a floor of protection.[79] To qualify for and continue to receive welfare, recipients must prove something negative about themselves—that they do not have enough to get along on their own. In contrast, beneficiaries of Social Security must prove something positive—that they have worked and contributed long enough to qualify for benefits.

President Roosevelt was committed to structuring Social Security as insurance, not welfare. The commitment was deeply held and of long standing. In 1931, in his annual message to the New York legislature, then-Governor Roosevelt stated:

> In 1929 I recommended to the Legislature a commission to report on Old-Age Security against want. The report of this commission resulted in the passage of the Old-Age Security bill, by the last Legislature, and actual payments under the new law went into effect on January first of this year. I have many times stated that I am not satisfied with the provisions of this law. Its present form, although objectionable as providing for a gratuity, may be justified only as a means intended to replace to a large extent the existing methods of poor-house and poor-farm relief. Any great enlargement of the theory of this law, would, however, smack of the practices of a dole. Our American aged do not want charity, but rather old age comforts to which they are rightfully entitled by their own thrift and foresight in the form of insurance. It is, therefore, my judgment that the next step to be taken should be based on the theory of insurance by a system of contributions commencing at an early age. In this way all men and women will, on arriving at a period when work is no longer practicable, be assured not merely of a roof over head and enough food, to keep body and soul to-

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[78] Insurance is designed to protect against significant financial losses and risks. Not everyone with insurance would be poor in the event of an insured loss without insurance, but all would be poorer. Indeed, Social Security is our nation's most effective anti-poverty program, lifting about 20 million Americans out of poverty and preventing 45.2% of people aged sixty-five or older from having incomes below the poverty line. Paul Van De Water & Arloc Sherman, *Social Security Keeps Twenty Million Americans Out of Poverty*, CTR. ON BUDGET & POLICY PRIORITIES (Aug. 11, 2010), http://www.cbpp.org/cms/index.cfm?fa=view&id=3260.

[79] *See, e.g.,* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-193SP, SOCIAL SECURITY REFORM: ANSWERS TO KEY QUESTIONS 3 (2005), *available at* http://www.gao.gov/new.items/d05193sp.pdf ("While Social Security was never intended to guarantee an adequate income by itself, it provides an income base on which to build.").

> gether, but also enough income to maintain life during the balance of their days in accordance with the American standard of living.[80]

Roosevelt's strong commitment to structuring Social Security as insurance, not welfare, may have resulted in part from his own personal experience. Having suffered the ravages of polio, he understood what it meant to be dependent.[81] Frances Perkins, President Roosevelt's Secretary of Labor and long-time associate, witnessed Roosevelt undergo "a spiritual transformation during the years of his illness . . . . The man emerged completely warmhearted, with humility of spirit and with a deeper philosophy. Having been in the depths of trouble, he understood the problems of people in trouble."[82]

His own experience perhaps taught him on a visceral level that people would be uplifted in spirit if they worked hard and joined together to provide a common pool of funds from which to draw when working days were over. His dependence resulting from his polio perhaps illuminated for him, on a personal level, how demeaning it was for people to have to prove to some other person that they could not support themselves without help, and how crippling in spirit to feel oneself to be helpless and a failure.[83]

Roosevelt recognized that to get immediate assistance to people in need—to alleviate the immediate suffering caused by the Depression—there was no alternative to welfare. But for the long term—once the Depression was history and the economic health of the country was restored—the President wanted a system of insurance in place to guarantee for posterity that people would have a reliable, stable source of income from which they could draw in old-age. Acutely conscious of the debilitating quality of fear, he wanted all workers to have the peace of mind, the security of knowing that they would be insured against their dependency on wages.[84]

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[80] *See* Joseph P. Harris, *Brief in Defense of Old-Age Benefits as provided in the Social Security Bill,* Soc. Sec. Admin., http://www.ssa.gov/history/reports/ces/ces2harrisbrief.html (last visited Nov. 1, 2012) (quoting President Roosevelt's 1931 message to the state legislature while governor of New York).

[81] Roosevelt's discovery of Warm Springs, Georgia and his ability to swim reportedly helped restore some measure of independence, together with hand controls which allowed him to drive an automobile. *See History—FDR*, Roosevelt Warm Springs Instit., http://www.rooseveltrehab.org/pages/view/156 (last visited Nov. 2, 2012).

[82] Frances Perkins, The Roosevelt I Knew 29 (1946).

[83] In his 1935 State of the Union Address, in explaining the legislation that would become the Social Security Act of 1935, President Roosevelt stated:

> The lessons of history, confirmed by the evidence immediately before me, show conclusively that continued dependence upon relief induces a spiritual disintegration fundamentally destructive to the national fiber. To dole our relief in this way is to administer a narcotic, a subtle destroyer of the human spirit. It is inimical to the dictates of a sound policy. It is in violation of the traditions of America. . . . The Federal Government must and shall quit this business of relief.

Franklin D. Roosevelt State of the Union Address of 1935 (Jan. 4, 1935), *available at* http://www.albany.edu/faculty/gz580/his101/su35fdr.html.

[84] In just the fourth sentence of Roosevelt's first inaugural address, he said, "So, first of all, let me assert my firm belief that the only thing we have to fear is fear itself—nameless,

In a fireside chat explaining his plan for Social Security, President Roosevelt observed that Social Security would be self help, where Americans were "to use the agencies of government to assist in the establishment of means to provide sound and adequate protection against the vicissitudes of modern life—in other words, social insurance." Perhaps to emphasize that Social Security, unlike welfare, is a program among equals, he reminded those listening, "We remain, as John Marshall said a century ago, 'emphatically and truly, a government of the people.'"[85]

### *C. Social Security Is Not a Savings Plan*

In the closing weeks of the 1936 presidential campaign, Republican standard-bearer Alf Landon made repeal of the recently enacted Social Security program a central theme.[86] In a major address on Social Security, delivered on September 26, 1936, Landon mischaracterized Social Security as forced savings:

> Now in broad terms there are two ways to approach the development of a program of economic security. One is to assume that human beings are improvident—that it is necessary to have the stern management of a paternal government to force them to provide for themselves—that it is proper for the government to force them to save for their old age. The other approach is to recognize that in an industrial nation some people are unable to provide for their old age—that it is a responsibility of society to take care of them.
>
> The [Social Security] Act passed by the present administration is based upon the first of these approaches.[87]

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unreasoning, unjustified terror which paralyzes needed efforts to convert retreat into advance." Franklin D. Roosevelt, First Inaugural Address (Mar. 4, 1933), *available at* http://www.bartleby.com/124/pres49.html.

[85] Franklin D. Roosevelt, Fireside Chat 5 (June 28, 1934), *available at* http://millercenter.org/president/speeches/detail/3302.

[86] Social Security was vulnerable to attack because contributions were to begin the following January, but the first monthly benefits were not to be paid for more than six years. *See supra* note 16. President Roosevelt responded forcefully to the attacks on Social Security during the 1936 campaign. On the Saturday before the 1936 election, in a major address in Madison Square Garden, Roosevelt condemned the Republican National Committee's orchestrated attack against Social Security, which included mass mailings of millions of pamphlets, posters, and pay envelope inserts. *See* ALTMAN, *supra* note 8, at 102–07. Though he did not directly refute the claim that Social Security is forced saving, he called Social Security "old-age insurance" explaining that half of the premium for the policy was paid for by employers, that the unemployment insurance premiums are completely paid for by employers, and asserting that it "is far more favorable to him than any policy that any private insurance company could afford to issue." Franklin D. Roosevelt, Speech at Madison Square Garden (Oct. 31, 1936), *available at* http://millercenter.org/president/speeches/detail/3307. Roosevelt won in a landslide. *See Election Of 1936: A Democratic Landslide*, U.S. HISTORY, http://www.u-s-history.com/pages/h895.html (last visited Oct. 31, 2012).

[87] *Landon Hits Social Security as 'Cruel Hoax' in Milwaukee Speech*, THE DAY (Sept. 28, 1936) [hereinafter *Landon Hits Social Security*], http://news.google.com/newspapers?nid=

Just as Social Security and welfare are different, so are Social Security and savings.[88] As discussed above, Social Security's wage insurance, and indeed all insurance, involves the pooling of resources and risk, exchanging the possibility of a larger loss for a smaller, certain payment, as a way to manage the risk of a financial insecurity. It requires the use of statistical data and mathematical methods to assess the probabilities of various contingent future events and the attendant costs of those contingencies. Assumption of the risk of those future events is then exchanged for a share of the attendant costs.[89] In contrast, savings are the straightforward accumulation of assets. Depending on how invested, those assets might appreciate or depreciate. They might generate income or not. They might be eroded by inflation.[90]

Insurance, not savings, is what is needed to prepare for the possibility of substantial financial losses which are predictable for a group but unpredictable for individuals. To manage the risk of the financial loss associated with the loss of a home as the result of fire, homeowners purchase fire insurance; they do not simply save for the contingency. Similarly, car owners have car insurance, not car-accident private accounts. To manage the risk of lost income as the result of disability, death, or old age, wage insurance like that provided by Social Security, is necessary, not savings.

It is easy to confuse wage insurance in the event of old age and retirement savings accounts because both are focused on protection in old age, a state virtually all of us hope to reach and most of us will. However, this similarity obscures fundamental differences. Although achieving old age is probable, it is not certain. Moreover, at the start of one's adult life, there are

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1915&dat=19360928&id=XqktAAAAIBAJ&sjid=Z3EFAAAAIBAJ&pg=999,2342658 (quoting Landon's speech).

[88] Some insurance products have savings components. So-called whole life insurance, for example, generally refers to insurance that is combined with an investment fund. *Ultimate Guide to Retirement: What Is Whole Life Insurance?*, CNN MONEY, http://money.cnn.com/retirement/guide/insurance_life.moneymag/index4.htm?iid=EL (last visited Oct. 31, 2012). Social Security has been described as "pure" insurance, because, unlike insurance products such as whole life insurance, it lacks any element of savings. Conversely, most bank deposit savings are insured through the Federal Deposit Insurance Corporation ("FDIC"), which was created in 1933 under the Banking Act of 1933, more commonly known as the Glass-Steagall Act. The Banking Act of 1933, Pub. L. 73-66, 48 Stat. 162 (codified as amended in scattered sections of 12 U.S.C.).

[89] *See supra* text accompanying notes 42–46.

[90] Interest-bearing bonds preserve the underlying principal, assuming the issuer of the bond remains able to repay the borrowed amount, but, even so, they provide no inflation protection. Bank savings accounts provide interest as well, and since 1933, are insured up to a maximum amount by the federal government through the FDIC, but, again, they provide no inflation protection. FDIC insures deposits, including accrued interest, held in insured banks. The maximum amount of the coverage for each account is $250,000. *Your Insured Deposits*, FDIC, http://www.fdic.gov/deposit/deposits/insured/basics.html (last visited Aug. 22, 2011). Equities historically have provided returns that are higher than interest rates and inflation. Recent economic literature shows that while equities are a better hedge against inflation than bonds, they are not immune to the risks of rising prices. *See* ELROY DIMSON ET AL., CREDIT SUISSE GLOBAL INVESTMENT RETURNS YEARBOOK 2012 15 (2012), *available at* https://www.credit-suisse.com/investment_banking/doc/cs_global_investment_returns_yearbook.pdf. Moreover, equities provide no protection of principal, which can be completely lost.

numerous uncertainties, including, for example, how long one will live, how high future wages and future standards of living will be, whether there will be periods of no wages as the result of unemployment or other circumstances, whether there will be intervening expenses, such as medical costs resulting from serious illness or injury, costs associated with the presence of dependents, educational expenses, or other conditions that require a diversion of savings.

Even if and when an individual reaches old age, there is the uncertainty of how long one will live and therefore need wages replaced—the so-called longevity risk. The language is jarring—most people would not describe a long life as a "risk," but it is, in financial terms.[91] The risk is outliving one's money. One can outlive savings, but not insurance that guarantees monthly payments for life.

Retirement savings are, at best, poor substitutes for wage insurance. Most workers in this country find that they have insufficient savings even for short-term needs,[92] but even if a worker were willing and able to sacrifice current consumption in order to maintain his or her standard of living in retirement, he or she would confront unanswerable questions. How much savings is enough? How much is too little? How much is more than necessary? If too little is saved, one risks destitution if wages are lost. Even if complete destitution is avoided, saving too little may force people to sell their homes, move from their neighborhoods, and cut all expenses drastically. If too much is saved, one needlessly reduces one's standard of living decades in advance of the contingent event, which may never occur.

Most experts believe that around seventy percent of pre-retirement wages is necessary for average-waged workers to maintain their standards of living in retirement, once wages are gone.[93] Higher percentages are needed for low-paid workers, somewhat lower for the highest paid.[94] But how does

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[91] It may be easier to think of longevity as a chance, like winning the lottery, which is the mirror image of a risk. Similarly, when actuaries at the Social Security Administration and elsewhere calculate mortality rates in calculating future costs of Social Security or private annuities, they consider increases in life expectancy, a "pessimistic" assumption. *See* BD. OF TRS., FED. OLD-AGE & SURVIVORS INS. & FED. DISABILITY INS. TRUST FUNDS, 2012 ANNUAL REPORT 76, 78–79 (2012), *available at* http://ssa.gov/oact/TR/2012/tr2012.pdf.

[92] In the last few years, the personal savings rate has increased, but it is still low. In August 2012, it was 3.7% of disposable income. *See* Massimo Guidolin & Elizabeth A. La Jeunesse, *The Decline in the U.S. Saving Rate: Is It Real and Is It a Puzzle?*, 89 FED. RESERVE BANK OF ST. LOUIS REV. 491 (2007), *available at* http://research.stlouisfed.org/publications/review/07/11/Guidolin.pdf (discussing the possible explanations for the low personal savings rate in the United States).

[93] Less than 100% is needed, because people no longer have work expenses and, instead of saving, start to dis-save. *See* Nancy J. Altman, *Rethinking Retirement Income Policies: Nondiscrimination, Integration, and the Quest for Worker Security*, 42 TAX L. REV. 435, 495–96 n.223 (1987); *see also* ALICIA H. MUNNELL, ANTHONY WEBB & LUKE DELORME, CTR. FOR RET. RESEARCH AT BOS. COLLEGE, A NEW NATIONAL RETIREMENT RISK INDEX 3 tbl.1 (2006).

[94] *See* Altman, *supra* note 93, at 496 n.224; *see also*, MUNNELL ET AL., *supra* note 93, at 3 tbl.1.

seventy percent of final pay translate into annual savings over the years available before retirement?

Workers who want to save over their working lives the precise amount needed to replace seventy percent of pre-retirement wages each and every year until their deaths must know all sorts of eventualities that actuaries know for groups, but no one knows for an individual. Those worker-savers have to know in their late teens or twenties, at the start of their working lives, what their wages will be at the time of their retirements decades away. They have to know at what age they will retire and whether they will have worked and saved every year until that retirement date or whether they will have had periods of no wages or even periods of dis-saving for more immediate expenses, such as child care, medical costs, and other necessities. They also have to know their rate of spending in retirement. Extensive medical costs or the need for long-term care can result in the rapid drawdown of savings. Those saving for retirement also have to know how long they will live, for if they do not live until retirement, they will not need to save anything for that eventuality. On the other hand, if they will be fortunate enough to live to the age of 105, they will have to save substantial amounts—20 more years of support than they will need if they die, for example, at age 85.

Worker-savers could avoid the risk of outliving savings that accompanies the uncertainty of how long beyond retirement they will live, by buying insurance—a life annuity or, to protect a spouse, a joint and survivor annuity—but waiting until retirement creates its own problems. They will need to know what return, in real terms, minus inflation, they will receive on their savings prior to the purchase of the annuity. If they plan to invest their retirement savings in equities, they will have to know how their stocks are performing at the time they will be purchasing the annuity, decades away. It has been calculated that workers with identical forty-year careers, identical wages, all investing six percent of those wages in equities, all retiring at the same age of sixty-two and all selling their equities to purchase level life annuities, can have dramatically different benefits based on nothing other than market timing. According to those calculations, a worker retiring in 1980 at age sixty-two would have been able to purchase an annuity equal to forty-seven percent of past earnings; if that worker turned sixty-two and retired just one year later, the worker's stock portfolio would have purchased an annuity providing benefits equal to sixty-eight percent of past earnings; if the worker turned sixty-two in 1993, he or she would receive only forty-two percent of past earnings; if he or she turned sixty-two, just four years later in 1997, the worker would receive seventy-two percent.[95] Moreover, those worker-savers have no protection if they become permanently and seriously disabled or die leaving dependent children or spouses, before reaching retirement age.

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[95] Robert M. Ball, The Century Foundation, Straight Talk About Social Security 44 (1998) (citing research by Gary Burtless of The Brookings Institution).

Unlike savings, insurance pools all of these various risks. Wage insurance like Social Security, where the benefit is explicitly designed to replace wages, is precisely geared to the goal and, in the case of Social Security, protects in the event of death or disability before reaching retirement.[96] Wage insurance, not savings and not welfare, is the most effective way to protect workers and their families when wages are lost as a result of disability, death, or old age.

Private group life insurance, disability insurance, and old age annuities are assets, which involve redistribution and are sometimes purchased from accumulated savings. Yet they are neither welfare nor savings. In the same vein, Social Security is group insurance, not welfare and not forced savings.

## III. What It Means to "Privatize" Social Security

The debate over the appropriate division between the public sector and the private sector goes back perhaps to the start of civilization.[97] The term "privatization" seems to have first been coined in the 1930s or early 1940s.[98] The use of the term in connection with Social Security is of much more recent vintage.[99] Though the use is new, the concept behind "privatizing" Social Security is not. A close analysis of what it means to "privatize" Social Security reveals that the term is obfuscating rather than illuminating.

The phrase has become synonymous with a proposal to allow workers to divert a portion of their Social Security insurance contributions to individual retirement savings accounts. The idea gained national attention when it was put forward by President George W. Bush shortly after his re-election on November 2, 2004.[100] As has just been discussed, though, insurance is qualitatively different from savings. Government provision of wage insur-

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[96] Moreover, Social Security protects against a number of other serious risks, protection not generally found in the private sector. *See infra* text accompanying notes 276–78.

[97] *See* Graeme A. Hodge, *Privatisation*, *in* 3 International Encyclopedia of Public Policy 545 (Phillip Anthony O'Hara ed., 2009), *available at* http://pohara.homestead.com/Encyclopedia/Volume-3.pdf (discussion of private sector tax collectors in the New Testament).

[98] *See* Germà Bel, *Retrospectives: The Coining of "Privatization" and Germany's National Socialist Party*, 20 J. of Econ. Persp. 187, 189–90 (2006) (discussing the use of the term "re-privatization" in connection with Nazi-era economic policy in Germany).

[99] The Cato Institute, a libertarian think tank, formed the Project on Social Security Privatization in 1995 to tout the idea of substituting private accounts for a portion of Social Security's insurance protection, a plan it had been promoting since 1980 with its publication of Ferrara, *supra* note 49. For further discussion, see Altman, *supra* note 8, at 266–67.

[100] For a description of the lengthy fight over the proposal, *see* Altman, *supra* note 8, at 271–96. The details of the proposal were never completely developed. *See* Christian E. Weller, *Primer on President Bush's "Plan" for Social Security Privatization*, Ctr. for Am. Progress (Mar. 5, 2005), http://www.americanprogress.org/issues/economy/news/2005/05/05/1462/primer-on-president-bushs-plan-for-social-security-privatization.

ance directly or indirectly[101] is totally different from the government requiring or inducing workers to save for retirement.

If one defines "privatization" as having the private sector operate the same services now operated by the public sector, then privatizing Social Security should mean transferring the government's role in providing wage insurance to private insurance companies or to private employers.[102] It would require the substitution of private insurance in the event of disability, death, or old age for the public insurance provided by Social Security. Alternatively, one could employ a broader definition of what "privatization" of Social Security means. One could define "privatization" of Social Security simply to mean the substitution of any form of private retirement income arrangement, whether insurance, savings, family assistance or some other private sector arrangement, for Social Security.

The lack of rigor in defining "privatization" and the effort to demonize some proposals but not others with that label has resulted in, as the cliché goes, more heat than light. When the smoke from the heat clears, one sees that under the narrow definition, the first and only time privatization of Social Security was proposed was in the Senate in 1935, as Subsection A describes. Under the broader definition, the Bush proposal would indeed be privatization, but so would other proposals currently being debated, notwithstanding their advocacy by some who vociferously insist that they oppose privatizing Social Security.[103] In addition to illuminating this point, Subsection B also reveals the conceptual underpinning and continuous line of proposals that unite the Bush proposal and other proposals currently being debated with a proposal put forward in 1936 by those who sought to repeal the just-enacted Social Security Act.

### *A. Defining Privatization Narrowly*

The one and only serious effort to "privatize" Social Security, as narrowly defined, came close to succeeding or at least to derailing Social Security. It was part of a hard-fought battle over Social Security during the consideration by Congress of the Social Security Act of 1935.[104]

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[101] Currently, the government provides wage insurance directly through Social Security and indirectly through preferential tax treatment for defined benefit pension plans established by employers. *See* Altman, *supra* note 93, at 436.

[102] The wage insurance described in this Article is more typically referred to as defined benefit pension plans when provided by private employers. See the text accompanying *infra* notes 215–223 for a discussion of those retirement arrangements. Indeed, some have labeled Social Security's wage insurance "the people's pension." *See, e.g.,* Eric Laursen, The People's Pension: The Struggle to Defend Social Security Since Reagan (2012).

[103] *See supra* note 11 (discussing the varying degrees of Social Security privatization).

[104] In addition to the fight in the Senate described in this Subsection, a fight over Social Security also occurred in the House of Representatives. Social Security was the target of an almost-successful motion to strike in the Ways and Means Committee. During its consideration by the full House of Representatives, several additional efforts were made to strike old age insurance from the bill. A motion to recommit the bill to committee with instructions to strike

Concerned that Social Security would unfairly compete with private sector pension products and destroy private pensions, Walter Forster, a principal in the insurance brokerage firm of Towers, Perrin, Forster, and Crosby, developed an amendment which Senator Bennett Champ Clark (D-Mo.) championed in both the Senate Finance Committee and on the Senate floor. The amendment would have allowed employers the ability to opt out of Social Security on behalf of their employees, if they provided their employees equivalent protection under their own plans.[105]

Supporters of Social Security believed the amendment, if enacted, would make Social Security unworkable. Thomas Eliot, who had helped draft the legislation, explained:

> This [amendment] threw a panic into the insurance-minded people who had helped to devise the original old-age insurance program in the bill. This, they pointed out, would destroy its actuarial soundness. It would exempt many of the so-called best risks from the plan and would throw all their calculations out of kilter. Another thing that did worry a good many people was the possibility that companies could get out of the old-age insurance requirements and, at the same time, have a "phony" retirement plan. Too often during those weeks we were brought into contact with people who gave us the evidence that they, as employees, had been covered by a voluntary retirement plan which promised them a retirement pension when they reached sixty-five in the companies which employed them and who had been fired a week before their sixty-fifth birthday so that the company didn't have to pay them any benefit after all. How were you going to prevent this, even if you wanted to do what Mr. Forster and Senator Bennett Clark of Missouri wanted to do? How were you going to prevent the fly-by-night plan from destroying the old-age insurance system? How would you avoid exempting large numbers of employees [sic] who weren't really making adequate provision for their employees?[106]

Notwithstanding the opposition of the administration, the amendment passed the Senate by a vote of 51 to 35.[107] Nearly every Republican senator and half

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the old age and unemployment insurance provisions and increase spending on the welfare provisions, for example, received 149 votes, including all 103 Republicans but one. *See* ALTMAN, *supra* note 8, at 72.

[105] The Clark amendment lost in the Senate Finance Committee on a tie vote, with several members who might have voted for it not in attendance. It was then offered on the Senate floor. Debate lasted two days. There was heavy lobbying on both sides. Forster, the author of the amendment, acknowledged privately that his company spent $50,000 on the effort. *See* ALTMAN, *supra* note 8, at 77.

[106] Thomas H. Eliot, Speech at General Staff Meeting of the Social Security Administration: The Legal Background of the Social Security Act (Feb. 3, 1961), *available at* http://www.ssa.gov/history/eliot2.html.

[107] Larry DeWitt, *Research Note #9: The Clark Amendment to the 1935 Social Security Act*, SOC. SEC. ADMIN. (Aug. 2000), http://www.ssa.gov/history/clarkamend.html.

of the Democratic senators voted for it. It then went to the conference committee.

After a month of deliberations, the conference committee had reconciled every issue but the Clark amendment. Unable to reach agreement, the conferees sought guidance from their respective bodies. Both bodies instructed their conferees to hold firm on the Clark amendment. At this point, Congress was within weeks of adjournment. To try to resolve the innumerable technical problems generated by the opt-out provision, the conferees assigned three staff members[108] the job of redrafting the Clark amendment so that it was workable. After three weeks of working around the clock, seeking to resolve the various intractable issues, the three reported that it would take many months, well beyond the end of the legislative session, to resolve the thorny issues. Among other issues, the amendment raised complicated problems concerning adverse selection, determination of equivalent protection, fiduciary responsibility, financial soundness, reporting, disclosure, and portability.[109] Finally, unable to resolve the issue in a timely manner, with adjournment looming, the conferees agreed to report the bill without the Clark amendment in exchange for the appointment of a special joint committee to develop a workable proposal to be introduced and passed in the next session.[110]

In early 1936, the Senate Finance Committee appointed a subcommittee to revise and report out a workable Clark amendment. In addition, the Finance Committee met a few times with the Ways and Means Committee, but the issue was not made a priority.[111] Eliot, who was by then General Counsel for the Social Security Board (predecessor of the Social Security Administration), contacted Senator William H. King (D-Utah), the acting chairman of the Senate Finance Committee, who had been one of the strongest supporters of the Clark amendment. In response to Eliot's offer to assist in the development of a new proposal, Senator King, according to Eliot, responded as follows:

> [Senator King] laughed and he said, "Oh! Mr. Forster was in the other day. You can forget the amendment. Mr. Forster said he'd made a terrible mistake. He thought that the passage of the old-age insurance bill would ruin his business of selling private pension plans. Instead the passage of the Social Security Act has got everybody thinking about pension plans. He doesn't want any Clark Amendment. You can forget it forever."[112]

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[108] The three staff members were Leonard Calhoun, an attorney from St. Louis chosen by Senator Clark, Thomas H. Eliot, a lawyer on the staff of the Committee on Economic Security, and another staff person named Bill Woodward. *See id.*; *see also* ALTMAN, *supra* note 8, at 78.

[109] *See* ALTMAN, *supra* note 8, at 78.

[110] ARTHUR J. ALTMEYER, FORMATIVE YEARS OF SOCIAL SECURITY 42 (1966).

[111] *Id.*

[112] *See* Eliot, *supra* note 106; *see also* ALTMEYER, *supra* note 110, at 42.

This was the first and last effort to privatize Social Security in the sense of substituting private insurance for Social Security's direct provision of old age annuities. No subsequent attempts have ever been made to privatize, as narrowly defined, Social Security's retirement income protection. No proposals have ever been put forward to substitute private sector life insurance or disability insurance for Social Security's survivors and disability protections.

### *B. Defining "Privatization" Broadly*

The part of President Bush's Social Security proposal that produced the most attention and was referred to by the shorthand moniker, "privatization," would have allowed workers to divert four percentage points of their FICA contributions up to a maximum dollar amount into a 401(k)-type retirement savings account.[113] At retirement, those workers who had exercised the option would have their Social Security benefits reduced by the nominal amount of the diverted premiums plus three percent imputed interest above inflation.[114]

Although criticized sharply by then-Senator Obama (D-Ill.) and other leading Democrats,[115] the Bush proposal can be seen as part of a continuum of proposals that would use governmental power to encourage or mandate retirement savings. On one end of the continuum is current law, where individuals receive preferential tax treatment as an inducement to save for retirement through individual retirement accounts or 401(k) plans.[116] On the other end of the continuum, some have proposed that the federal government re-

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[113] CONG. BUDGET OFFICE, AN ANALYSIS OF THE PRESIDENT'S BUDGETARY PROPOSALS FOR FISCAL YEAR 2006 47 (2005), *available at* http://cbo.gov/sites/default/files/cbofiles/ftpdocs/61xx/doc6146/03-15-presanalysis.pdf. *See infra* note 116 for a discussion of 401(k) plans.

[114] Weller, *supra* note 100.

[115] *See* Barack Obama, Speech at the National Press Club (Apr. 26, 2005), *available at* http://obamaspeeches.com/014-National-Press-Club-Obama-Speech.htm. *See generally* ALTMAN, *supra* note 8, at 279, 288, 291.

[116] Since the enactment of the Employee Retirement Income Security Act of 1974, individuals have had the ability to receive preferential tax treatment for income placed in Individual Retirement Accounts under Section 408 of the Internal Revenue Code (colloquially known as "IRAs"). I.R.C. § 408 (2006). Established originally for individuals not covered by employer plans, the law has been amended and the tax treatment modified a number of times, so that today almost everyone is eligible to take advantage of these savings vehicles. *See* THOMAS L. HUNGERFORD & JANE G. GRAVELLE, CONG. RESEARCH SERV., RL30255, INDIVIDUAL RETIREMENT ACCOUNTS (IRAS): ISSUES AND PROPOSED EXPANSION (2010), *available at* http://aging.senate.gov/crs/pension38.pdf. In 1978, Congress added Section 401(k) to the Internal Revenue Code (colloquially known as "401(k) plans"). Pub. L. No. 95-600, 92 Stat. 2763 (1978). That provision allows employees to receive favorable tax treatment with respect to compensation they choose to contribute to employer-sponsored retirement savings accounts. For a discussion of the history of section 401(k) plans, see generally EMP. BENEFIT RESEARCH INST., HISTORY OF 401(K) PLANS: AN UPDATE (2005), *available at* http://www.ebri.org/pdf/publications/facts/0205fact.a.pdf.

quire that all workers save for retirement.[117] In between those two approaches are: (1) a proposal put forward by President Obama where private employers would be required, at a minimum, to make deductions from employees' wages of three percent of those wages and place the funds in individual retirement accounts, unless the employees opted out or opted for a different percentage;[118] and (2) President Bush's proposal to allow employees to opt to have employers make deductions from their wages of up to four percent of those wages and place the funds in individual retirement accounts; those employees so choosing would have their FICA contributions reduced dollar for dollar and their eventual Social Security benefits reduced by the dollar amount of their reduced FICA contributions plus imputed interest.[119]

Some draw a bright-line distinction between so-called carve-out accounts, such as President Bush proposed, which consist of funds diverted from Social Security contributions, and add-on accounts, such as President Obama proposes, where contributions are not diverted.[120] The distinction seems overly formalistic in the context of today's projected Social Security shortfall, however.[121] Carve-out accounts, which divert Social Security contributions, result in increased pressure to cut Social Security's benefits, because they increase Social Security's projected shortfall. Similarly, mandatory add-on accounts, which divert potential Social Security contributions, result in increased pressure to cut Social Security's benefits, because a traditional source of increased revenue has been eliminated. To provide a sense of scale, the Obama proposal requires employers to withhold three percent of all their workers' wages and deposit those withholdings into individual retirement accounts. It is well worth noting that Social Security could be restored to complete actuarial balance if employers withheld just 2.67% of that portion of employee wages equal to or less than the Social Security maximum ($110,100 in 2012[122]), and deposited the withholdings into the Social Security pension trust funds.[123]

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[117] *See, e.g.*, Concord Coal., Personal Retirement Accounts: Should They be Voluntary or Mandatory? (2005), *available at* http://concordcoalition.org/publications/2005/0622/social-security-series-private-accounts-should-they-be-voluntary-or-mandatory.

[118] *See* Dep't. of the Treasury, General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals 15–18 (2012), *available at* http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2013.pdf (Under the proposal included in the 2013 Budget, employers in business for at least two years and with at least ten employees would be covered by the mandate, if they do not otherwise provide an alternative arrangement.).

[119] *See generally* Cong. Budget Office, *supra* note 113.

[120] *See, e.g.*, Andrew Samwick, *Carveouts*, Vox Baby (June 20, 2006, 12:29 PM), http://voxbaby.blogspot.com/2006/06/carveouts.html (responding to a debate that ensued at an American Enterprise Institute event over carve out and add on accounts).

[121] *See* Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102, at 4 (2012) ("For the 75-year period, the actuarial deficit is 2.67 percent of taxable payroll . . . .").

[122] *See supra* note 45.

[123] *See* Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102, at 61. The Obama proposal only

Some commentators have referred to the position that Social Security benefits should be cut while individual retirement savings should be expanded as "back-door privatization."[124] Moreover, President Obama succeeded in having enacted a two percentage point reduction in Social Security's FICA contributions paid by workers. The change was broadcast as a temporary "holiday," but has been extended beyond its initial termination date.[125] The experience of the so-called Bush tax cuts, which were initially enacted as temporary, but, as of this writing, have been extended once and may be extended again at the end of 2012, reveals that reductions are easy to enact, but hard to let expire.[126] If the FICA reduction became permanent, if the automatic IRA proposal were enacted, and if Social Security benefits were cut as part of a "balanced" package, as President Obama and other leading Democrats have called for,[127] the line between what self-proclaimed opponents of "privatization" support and what President Bush proposed would be even blurrier.

When one looks past the label "privatization" and its narrow focus on the explicit diversion of Social Security contributions into private accounts, one sees more clearly. Lower Social Security benefits mean that workers who stop working must, by necessity, look to the private sector to replace wages previously replaced by Social Security. If Social Security plays a smaller role in replacing lost wages, the private sector necessarily must play a larger role, if those wages are to be replaced and workers and their families are to be able to buy basic necessities. Whether private savings are mandated, provided as an optional alternative to Social Security, or simply encouraged by favorable tax treatment is immaterial. What is key is not the

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requires the withholding if the employer is not providing an alternative retirement arrangement, and workers can choose not to participate or choose different percentages, unlike Social Security contributions, which are mandatory. On the other hand, the Obama proposal applies to all income. If Social Security contributions were imposed on all wages, little or no additional rate increases would be required. *Id.*

[124] *See, e.g.*, Monique Morrissey, *What We Should Talk About When We Talk About Social Security*, ECON. POLICY INST. BLOG (May 7, 2012, 11:43 PM), http://www.epi.org/blog/social-security-debate-talking-points.

[125] The Temporary Payroll Tax Cut Continuation Act of 2011, Pub. L. No. 112-78, § 101, 125 Stat. 1280, 1281–82 (extending the temporary reduction in the payroll tax to February 28, 2012); *see* The Middle-Class Tax Relief and Job Creation Act of 2012, Pub. L. No. 112-96, § 1001, 126 Stat. 156, 158–59 (extending the reduction in payroll tax again from February 28, 2012 to December 31, 2012).

[126] Nancy Altman, *The End of Social Security*, HUFFINGTON POST (Dec. 7, 2010), http://www.huffingtonpost.com/nancy-altman/the-end-of-social-securit_b_793366.html.

[127] *See*, *e.g.*, Interview by Mark Halperin with David Axelrod, Senior Strategist, Obama for America (Sept. 24, 2012), *available at* http://thepage.time.com/2012/09/24/social-security-and-specifics/?iid=sl-main-arenapage (Axelrod stated the President's support for a "balanced [package]," implying one that includes both revenue and benefit cuts.). Some have argued, however, that in light of past legislation, it would be more balanced to simply have revenue, with no cuts. *See, e.g.*, JANICE M. GREGORY ET AL., NAT'L ACAD. OF SOC. INS., SOCIAL SECURITY BRIEF NO. 35: STRENGTHENING SOCIAL SECURITY FOR THE LONG RUN (2010), *available at* http://www.nasi.org/sites/default/files/research/SS_Brief_035.pdf.

structure of the private arrangement, but the void left from the reduction of benefits.

When one removes the blinders produced by the label "privatization," which focuses myopically on explicitly, in one legislative proposal, permitting workers to choose to substitute private savings for Social Security, one is able to see a broader landscape and make larger connections. While the Bush proposal to divert part of Social Security's contributions into private accounts received most of the attention of the media, policymakers, and the public, President Bush also proposed changing the manner in which Social Security's benefit formula is automatically adjusted.[128]

Because wage insurance is designed to replace a set amount of wages, Social Security's formula for calculating initial benefits is indexed to the annual increase in average wages nationwide—a method colloquially referred to as wage indexing.[129] Wage indexing has the desired result of maintaining over time Social Security's progressive benefit formula, despite the growth in the nominal and real value of wages. Wage indexing keeps Social

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[128] To address the fact that diversion of part of Social Security's revenues into private accounts would worsen rather than improve its long-range financial projections, the latter being the ostensible reason for the proposal, Bush advocated for "progressive price indexing" by stating that "benefits for low-income workers will grow faster than benefits for people who are better off." Press Conference of the President (Apr. 28, 2005), *available at* http://www.ssa.gov/history/gwbushstmts5b.html#04282005; *see also* Press Release, The White House, Fact Sheet: Strengthening Social Security For Those In Need (Apr. 28, 2005), *available at* http://georgewbush-whitehouse.archives.gov/news/releases/2005/04/20050428-7.html. For a critique of the proposal, see Jason Furman, *An Analysis of Using "Progressive Price Indexing" To Set Social Security Benefits*, CTR. ON BUDGET & POLICY PRIORITIES (May 2, 2005), http://www.cbpp.org/cms/?fa=view&id=48. It is noteworthy that Republican President Gerald Ford considered proposing price indexing to address Social Security's projected shortfall in the 1970s, but for the reasons discussed in the text, he proposed wage indexing instead. *See* ALTMAN, *supra* note 8, at 217–18. The Ford proposal was never considered by Congress, but it was proposed again by President Jimmy Carter and enacted as part of the Social Security Amendments of 1977, Pub. L. No. 95-216, 91 Stat. 1547. *See* ALTMAN, *supra* note 8, at 219.

[129] The dollar amounts in the benefit formula are adjusted each year. The question was whether those dollar amounts should be indexed to the annual increase in prices or wages. As discussed in the text, price indexing would have caused benefits to decline steadily as a percentage of wages; wage indexing causes replacement rates to stay reasonably stable. Prior to 1972, Congress regularly increased Social Security's benefits to take into account increased wage growth and inflation, but these ad hoc increases were somewhat irregular in timing and amount, and consequently, caused benefits to erode between Congressional actions. *See* ALTMAN, *supra* note 8, at 221. In response to this problem, President Nixon proposed and Congress enacted automatic annual adjustments to Social Security's benefits. *See* ALTMAN, *supra* note 8, at 221; Social Security Amendments of 1972, Pub. L. No. 92-603, 86 Stat. 1476. Within just a few years of the enactment, the nation underwent an unprecedented period of high inflation and low wage growth, which caused over-indexing of benefits, a flaw that was only disclosed by unusual economic conditions. *See* ALTMAN, *supra* note 8, at 221. In response to the flaw, some experts proposed that the formula for determining initial benefits be corrected by indexing the dollar amounts in the formula to increases in prices, a procedure colloquially labeled price indexing. *See* U.S. GOV'T PRINTING OFFICE, REPORT OF THE CONSULTANT PANEL ON SOCIAL SECURITY TO THE CONGRESSIONAL RESEARCH SERVICES 3 (1976), *available at* https://www.socialsecurity.gov/history/reports/hsiao/hsiaoIntro.html. Dollar amounts are colloquially called bend points. For the 2012 formula with bend points, see *Primary Insurance Amount*, SOC. SEC. ADMIN., http://www.ssa.gov/oact/cola/piaformula.html (last visited Nov. 2, 2012).

Security's progressive replacement rates constant over time.[130] In contrast, price indexing, an alternative that was considered but rejected at the time wage indexing was enacted, causes benefits to decline as a percentage of wages. Under price indexing, benefits would erode inexorably over time so that ultimately, all beneficiaries would receive the same low benefit largely unrelated to wages.[131]

President Bush proposed that the adjustment of Social Security's benefit formula be switched from a wage index to a price index. To ensure that benefits did not fall below a minimal level, however, he proposed continuing to use wage indexing in calculating the benefits of the first dollars of wages earned (which, in the case of the lowest income workers, are the only dollars earned), a proposal labeled "progressive" price indexing, by its supporters.[132]

Under the Bush proposal to substitute progressive price indexing, most workers would receive a very low benefit in relation to their wages. Progressive price indexing would require the private sector to play a larger role in providing retirement income if most workers would have even the possibility of maintaining their standards of living without working in old age. Eventually and inexorably, price indexing would cause Social Security's wage-replacement insurance to disappear as a practical matter. If workers were to be able to maintain their standards of living as they aged, they would either have to keep working or supplement the minimal payment from private sources.

If privatization of Social Security is defined broadly to mean reducing the amount of retirement income provided by Social Security and having more provided through the private sector, then progressive price indexing also could be seen as privatization. Like the other part of the Bush proposal—allowing workers to divert a portion of their Social Security premiums

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[130] *See* BD. OF TRS., FED. OLD-AGE & SURVIVORS INS. & FED. DISABILITY INS. TRUST FUNDS, 2012 ANNUAL REPORT, H.R. DOC. NO. 112-102, at tbl.V.C7 (2012).

[131] For detailed analysis of the impact of price indexing and progressive price indexing, see generally KATHY A. RUFFING & PAUL N. VAN DE WATER, CTR. ON BUDGET & POLICY PRIORITIES, "PROGRESSIVE" PRICE-INDEXING WOULD SIGNIFICANTLY CUT SOCIAL SECURITY BENEFITS FOR MANY RECIPIENTS (2010), *available at* http://www.cbpp.org/files/11-17-10socsec.pdf.

[132] In 2001, President Bush established the President's Commission to Strengthen Social Security. *See* Exec. Order No. 13,210, 3 C.F.R. 13,210 (May 2, 2001), *available at* http://www.gpo.gov/fdsys/pkg/FR-2001-05-04/pdf/01-11505.pdf. The Commission's report proposed three alternative reform packages, the second of which included price indexing of the benefit formula, but, in recognition of the impact of this change on the lowest wage workers, proposed mitigating the impact by having those benefits continue to grow with increases in wages for nine years, and only then, grow with increases in prices. *See* THE PRESIDENT'S COMMISSION TO STRENGTHEN SOCIAL SECURITY, STRENGTHENING SOCIAL SECURITY AND CREATING PERSONAL WEALTH FOR ALL AMERICANS 119–30 (2001), *available at* http://www.socialsecurity.gov/history/reports/pcsss/Final_report.pdf. Four years later, one of the members of the commission, Robert C. Pozen, proposed price indexing with the gloss of allowing the lowest wages to grow not just for nine years but continually with increases in wages, and referred to this modified proposal as "'progressive' price-indexing." *See* Robert C. Pozen, *Why My Plan to Fix Social Security Will Work*, USA TODAY, June 12, 2005, at A13.

into private accounts and receive lower Social Security—Social Security's benefits would be reduced and workers would instead have to look to the private sector for the remainder of the income they hope to have in retirement. Indeed, since progressive price indexing reduces the benefits of all workers and since there would be no government requirement that workers save but simply the incentive to do so through preferential tax treatment, one could argue that the role of government would be smaller under that proposal. Seen in that light, the proposal would privatize Social Security to a greater degree than under the Bush proposal generally labeled "privatization."

It is important to recognize that President Bush's proposal to adopt progressive price indexing is extremely similar to many other Social Security proposals, past and present. In 2010, President Obama established the National Commission on Fiscal Responsibility and Reform.[133] The Commission co-chairs, Erskine Bowles and former Senator Alan Simpson (R-Wyo.), included a variety of changes to Social Security in their recommendations.[134]

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[133] *See* Exec. Order No. 13531, 75 Fed. Reg. 7,927 (Feb. 18, 2010), *available at* http://www.whitehouse.gov/the-press-office/executive-order-national-commission-fiscal-responsibility-and-reform. The executive order, issued by President Obama, defined the task as proposing recommendations that "balance the budget, excluding interest payments on the debt, by 2015," and "that meaningfully improve the long-run fiscal outlook, *including changes to address the growth of entitlement spending* and the gap between the projected revenues and expenditures of the Federal Government." *Id.* (emphasis added). The executive order implicitly urged the lumping together of Social Security, Medicare, and Medicaid under the rubric, "entitlement spending." Obama's executive order refers opaquely to this phrase, a budgetary term that could include numerous mandatory spending programs, as well as provisions in the Internal Revenue Code, sometimes referred to as tax entitlements. But the reference is insider code, well understood as Washington-speak, for Social Security, Medicare, and Medicaid, three extremely different programs with different structures, goals, budgetary impacts, and financial outlooks. The work was framed in this way despite the fact that cutting Social Security benefits or increasing its revenue does not change the amount of federal debt subject to limit. *See Perspectives On Debt Reduction: Social Security Before the S. Comm. on Finance*, 112th Cong. 10 (2011) (statement of Nancy J. Altman, Co-Director, Social Security Works), *available at* http://www.finance.senate.gov/imo/media/doc/051011natest.pdf. For the connection of the co-chairs to a Clinton commission seeking to cut Social Security, see *infra* text accompanying note 182.

[134] *See* The Nat'l Comm. on Fiscal Responsibility & Reform, The Moment of Truth: Report (2010), *available at* http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12_1_2010.pdf. Although the report bills itself as a report of the Commission, the executive order establishing the commission required a super majority for a final report, which was not obtained. The executive order stated:

> Sec. 5. Reports. (a) No later than December 1, 2010, the Commission shall vote on the approval of a final report containing a set of recommendations to achieve the mission set forth in section 4 of this order. (b) The issuance of a final report of the Commission shall require the approval of not less than 14 of the 18 members of the Commission.

Exec. Order No. 13531, 75 Fed. Reg. 7,927 (Feb. 18, 2010). No formal vote was taken on the Bowles-Simpson proposal, but members of the Commission did present statements of their views. One member, Senator Conrad, said in his formal statement:

> Even though the Commission's final report, "The Moment of Truth," did not get the necessary 14 votes to ensure it is taken up by Congress, the Commission has made a

Though the Bush proposal and the Bowles-Simpson proposal differ in their technicalities, the impact on benefits is nearly identical.[135] Both change Social Security's benefit formula in a way that drastically reduces most workers' benefits as a percentage of their wages.[136] Both protect the benefits of the lowest wage workers.[137]

The following graphs reveal the similarity.[138] Figure 1 displays Social Security's current benefit structure.[139] It illuminates both Social Security's progressive benefit structure as well as its function as a vehicle to replace wages. The lines have a downward slope during the period when the current-law increase in the retirement age is phasing in.[140] They then level off,

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> major contribution by putting this issue on the national agenda. . . . Eleven of us—five Democrats, five Republicans, and one Independent—have agreed on a far-reaching package that would provide nearly $4 trillion in deficit reduction by 2020.

*Hearing on the Final Proposal Put Forth by the Chairmen of the President's National Commission on Fiscal Responsibility and Reform Before the S. Fiscal Comm.*, 112th Cong. (2011) (statements of all members), *available at* http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/MemberStatements.pdf. Five members, Senator Max Baucus (D-Mont.), Rep. Xavier Becerra (D-Cal.), Rep. Jeb Hensarling (R-Tex.), Rep. Jan Schakowsky (D-Ill.), and former SEIU President Andy Stern, stated that they were opposed to the proposal. *Id.*

[135] The benefit formula consists of so-called percentage factors and bend points. *See supra* note 129. The Bush proposal gradually reduces the bend points; the Bowles-Simpson proposal reduces the percentage factors. Progressive price indexing continues the downward trajectory; the part of the Bowles-Simpson proposal that does that is indexing retirement age to increases in longevity.

[136] *Supra* note 129. In addition to the benefit formula change, the Bowles-Simpson proposal includes several other cuts. The proposal would change the index used to measure inflation from the CPI-W to the chained-CPI-U. Although the change mainly affects benefits after they have begun to be paid, it also reduces initial benefits. *See* THE NAT'L COMM. ON FISCAL RESPONSIBILITY & REFORM, THE MOMENT OF TRUTH: REPORT 51–52 (2010). In addition, Bowles-Simpson indexes the early and full Social Security retirement ages to average increases in longevity. Because of the way that Social Security benefits are calculated, the proposal is indistinguishable from a gradual but continual across-the-board benefit cut. *See, e.g.*, Trudy Lieberman, *What a Higher Retirement Age Really Means: A Social Security Mini-Primer*, COLUM. JOURNALISM REV. (Sept. 13, 2012), http://www.cjr.org/swing_states_project/what_a_higher_retirement_age_r.php.

[137] The Bowles-Simpson proposal would increase the so-called special minimum benefit to 125% of poverty for very low-income workers who have worked in covered employment for 30 or more years. *See infra* note 142. *See also* Letter from the Chief Actuary to the Co-Chairs at 2 (Dec. 1, 2010), *available at* http://www.ssa.gov/OACT/solvency/FiscalCommission_20101201.pdf. Together with SSI, this change would increase the lowest benefits so all lines on the graphs would eventually converge. *See infra* text accompanying notes 141–144.

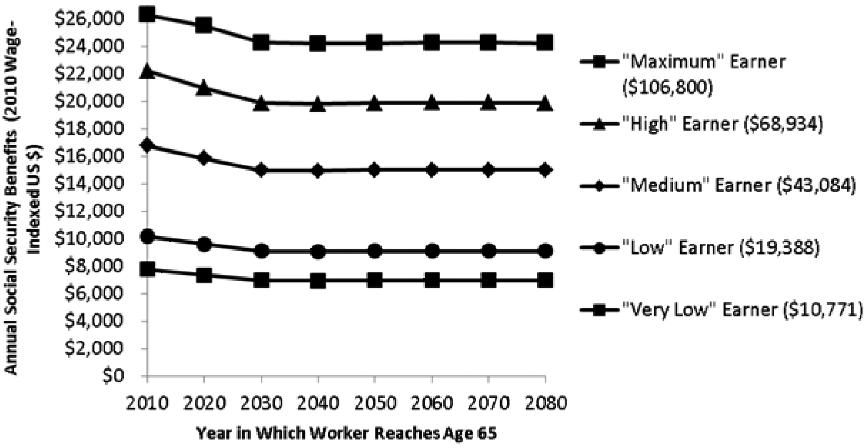
[138] All of the graphs were created by Daniel Marans, Policy Director of Social Security Works, based on data from the Chief Actuary of the Social Security Administration. *See* Letter from Steven C. Goss, Chief Actuary of the Soc. Sec. Admin., to Mr. Bowles, et al. (Feb. 2, 2011), *available at* http://ssa.gov/oact/solvency/BowlesSimpsonRivlinDomenici_20110202.pdf. Social Security benefits under President Bush's progressive price indexing plan were calculated by applying percentage reductions in benefits to scheduled benefits in the score of the Bowles-Simpson plan cited above (the 2005 estimates included percentage reductions, but not dollar amounts). Memorandum from Stephen C. Goss, Chief Actuary of the Soc. Sec. Admin., to Bob Pozen (Feb. 10, 2005), *available at* http://ssa.gov/oact/solvency/RPozen_20050210.pdf.

[139] The numbers were generated when the maximum taxable wage base was $106,800. *See supra* note 43.

[140] The increase in the statutory retirement age is fully phased in for workers who reach age sixty-two in 2022 or later. *See supra* note 28. As described in *supra* note 136, raising the

presenting a constant replacement rate for various levels of earners. Higher earners receive higher dollar amounts but lower percentages of wages:

FIGURE 1




In contrast, Figures 2 and 3 reveal the impact of the Bush proposal to adopt progressive price indexing and the Bowles-Simpson Social Security proposal, respectively.[141] In both graphs, the top three lines have a sharp downward trajectory and begin to converge with the fourth. The top lines in Figure 2 have a steeper slope, and so, converge sooner, but if the horizontal axes of both graphs were extended further in time, the top four lines of both would converge eventually into a single line.[142] The fifth and lowest line of Figure 3 represents very low-wage workers. Under Bowles-Simpson, about

statutory retirement age is mathematically indistinguishable from an across-the-board cut in benefits for retirees.

[141] Figure 3 shows the combined impact on benefits of all elements of the Bowles-Simpson proposal, including the change in the benefit formula bend points, the change in the statutorily-defined retirement age, the change to the chained-CPI, and the increase in the special minimum. According to Social Security's Chief Actuary, about sixty percent of actual "Very Low" earners, those with annual earnings of around $10,771, would have their benefits cut under the Bowles-Simpson proposal, because they would neither qualify for a hardship exemption, nor be helped by the proposed minimum benefit. The Chief Actuary assumes that the hardship exemption would require twenty-five or more years of covered employment. As under current law, the full enhanced minimum benefit would only be available to workers with thirty years of covered employment. *See* Memorandum from Stephen C. Goss, Chief Actuary of the Soc. Sec. Admin., to Mr. Bowles, et al., *supra* note 138 (stating workers might have fewer than twenty-five years of covered employment if they have worked in the cash economy where their wages were unreported, if they were unemployed, or for other reasons).

[142] Current law has a so-called special minimum benefit for long-time low income workers. The lines would converge with that benefit, under the Bush proposal. The Bowles-Simpson proposal increases the minimum to 125% of poverty. The 2012 poverty line is just under $10,830 for an individual aged sixty-five or older. *See* U.S. CENSUS BUREAU, 2012 STATISTICAL ABSTRACT (2012), *available at* http://www.census.gov/prod/2011pubs/12statab/income.pdf.

forty percent of those workers would have their benefits increased. The dotted line on the graph indicates the convergence of the bottom two lines with respect to those forty percent. Sixty percent of very low-wage workers would not satisfy the requirements necessary to receive the increased benefit,[143] but they would be eligible to receive an SSI benefit and a small Social Security benefit, just as they would under the Bush proposal.[144]

FIGURE 2

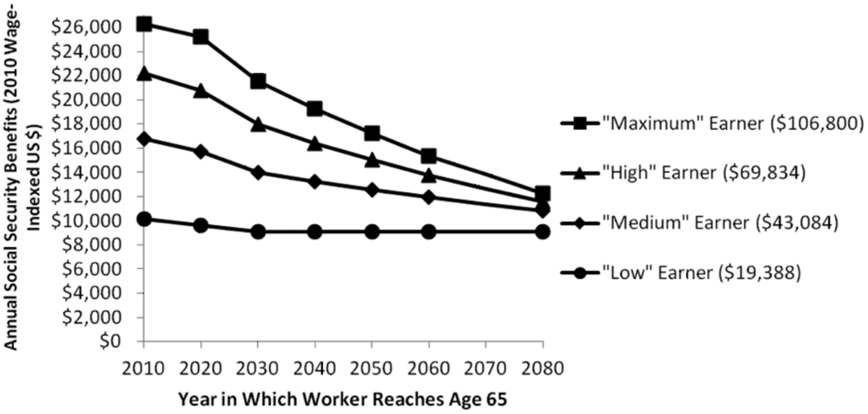
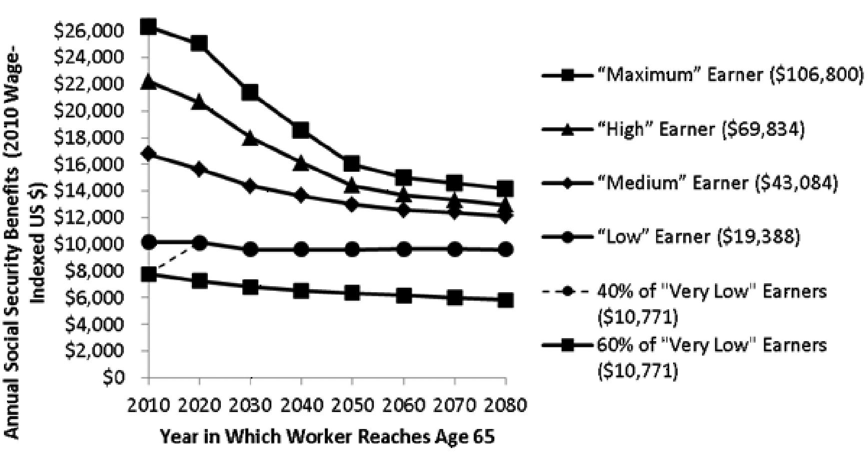



FIGURE 3




[143] Without extensive years of employment covered by Social Security, they would not receive the increased minimal Social Security benefit proposed by Bowles-Simpson, because they would not meet the requirement of service time.

[144] See description of the SSI program in *supra* text accompanying notes 62–79.

The similarity in the proposals is even greater if one compares the Bush proposal not just to Bowles-Simpson by itself, but also in combination with: (1) President Obama's proposal to require employers to deduct a percentage of their employees' wages and place the funds in individual retirement accounts; and (2) the temporary reduction in Social Security's FICA contribution rate, a measure proposed by President Obama to stimulate the economy and championed by Democrats. If the temporary reduction were to become permanent, if the president's so-called auto-IRA proposal were to be enacted, and if the changes proposed by the co-chairs of his fiscal commission were to become law, the three proposals taken together would be even more like the Bush proposal that the president and other leading Democrats denounce as "privatization."

It is important to understand that the concept underlying both the Bush proposal and the Bowles-Simpson proposal (with or without the additional Obama proposals) form a continuous line with proposals that have come before. The idea of replacing Social Security's wage-related benefit with a flat benefit for all and of having individual savings make up the difference is not a new idea. It has been championed frequently over the decades by conservatives opposed to the concept of government-provided wage insurance.[145]

During consideration of the Social Security Act in 1935, opponents unsuccessfully sought to defeat the proposed compulsory insurance.[146] Recognizing the popularity of addressing old age insecurity, the position of the Republicans in 1936 was not simple repeal. Just as Bush and Bowles-Simpson advocate, the 1936 Republican Party proposed to replace Social Security with a subsistence-level benefit and allow people to save on their own. As an alternative to Social Security, the 1936 Republican Party platform proposed: "Every American citizen over sixty-five should receive the supplementary payment necessary to provide a minimum income sufficient to protect him or her from want."[147] On the campaign stump, Republican presidential nomi-

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[145] Depending on the starting point, this is not necessarily a conservative idea. Though the 1936 Republican Platform would have provided significantly lower benefits and would have changed the overall conceptual underpinning of Social Security, it would have, nevertheless, immediately covered many more people. *See supra* text accompanying note 87. The idea of a demogrant as a universal floor of protection has been proposed by both conservatives and liberals. Senator George McGovern (D-N.D.) proposed, as the 1972 Democratic Presidential nominee, that the personal income tax exemption be replaced with a refundable income tax credit of $1000, which was similar to conservative economist Milton Friedman's proposal of a negative income tax. *See* Theodore White, The Making of the President 125 (1st Harper Perennial Reissue ed. 2010).

[146] *See supra* text accompanying notes 87, 104–116.

[147] *See* 1936 Republican National Platform, *available at* http://www.presidency.ucsb.edu/platforms.php. In a major address in Milwaukee, Wisconsin, Republican presidential nominee Alf Landon embraced the idea, advocating for the replacement of Social Security with a program of subsistence level benefits "for every American citizen over 65" in an amount "necessary to give a minimum income sufficient to protect him or her from want." *Landon Hits Social Security*, *supra* note 87.

nee Governor Alf Landon mischaracterized Social Security as "forced savings," and he advocated allowing people to save on their own.[148]

It may be hard to see the fundamental similarities of the Bush proposal, the Bowles-Simpson proposal, and the 1936 proposal. The difficulties in seeing the basic similarities are at least threefold. First, price indexing, other changes to the Social Security benefit formula, other indexing changes, and retirement age changes appear to be adjustments to Social Security, not fundamental replacements with an entirely different structure and underlying conceptual basis like the 1936 proposal. It is important to remember, though, that the Bush and Bowles-Simpson proposals have a totally different starting point from that of the 1936 Republican Party proposal. The 1936 proposal could simply and straightforwardly repeal the not-yet-begun Social Security and replace it with a flat, subsistence-level universal benefit. In contrast, today's proposals must unravel an existing system, so the changes must be phased in gradually.[149]

In 1936, Social Security had just been enacted the year before. Though it was intended ultimately to cover the entire work force, it was limited, at the recommendation of then-Secretary of the Treasury Henry Morgenthau, to commercial and industrial workers—about fifty-six percent of the work force.[150] Moreover, because workers needed to have time to achieve insured status, none of the elderly who had stopped working were eligible. Insurance premiums were not to start being collected until the following year. In stark contrast, today, ninety percent of those age sixty-five and over receive Social Security; ninety-four percent of workers are covered by Social Security.[151] Moreover, a huge bureaucratic structure is in place, collecting revenue routinely and regularly from wages. Careful records are kept for each worker regarding wages earned and amounts paid in. Thus, the recent proposals must account for this existing system and slowly unravel what exists.

The second difficulty in seeing the similarities is that the Bush proposal is explicit about private savings as an alternative to Social Security, while the other two are not. While the Republicans in 1936 did not explicitly re-

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[148] *See supra* text accompanying note 87.

[149] Workers in their early twenties could still be receiving Social Security seventy-five or eighty years from now. Social Security's Trustees have in the past employed valuation periods as long as eighty years. Since 1965, they have consistently employed valuation periods of seventy-five years. *See* DeWitt, *supra* note 52. To unravel Social Security totally, there would need to be conforming amendments eliminating, for example, the requirement of being insured. *See supra* note 16.

[150] *See* William J. Nelson, Jr., *Employment Covered Under the Social Security Program, 1933–1984*, 48 Soc. Sec. Bull. 4, 33–34 (1985), *available at* http://www.ssa.gov/policy/docs/ssb/v48n4/v48n4p33.pdf. The intent was for Social Security to be universal, but at a hearing about the proposal in the House Ways and Means Committee, Frances Perkins has written that she was blindsided when Secretary of the Treasury Morgenthau, testifying on a panel with her, announced that Treasury proposed for administrative reasons limiting the initial scope of the program. *See* Altman, *supra* note 8, at 66–67.

[151] Press Release, Soc. Sec. Admin., Social Security Basic Facts (July 30, 2012), *available at* http://www.ssa.gov/pressoffice/basicfact.htm.

quire individual savings for retirement, however, they took as an implicit assumption that people would save on their own, as a result of the necessity to do so.[152] Like the 1936 proposal, the Bowles-Simpson proposal is silent about individual retirement savings, though workers have the incentive of preferential tax treatment for doing so.[153]

Despite these differences, the reality is that under all three plans, workers would have to look to the private sector to make up the shortfall in what Social Security currently provides and what it would provide under the three proposals. By necessity, workers would have to look to private sector arrangements, under all three schemes, if they were to be able to cease work voluntarily and maintain their standards of living until death.

A third difficulty in seeing the similarities is that the Republicans of 1936 were straightforward in their objections to Social Security and their desire to replace it with a different structure. Today's opponents are much more opaque. They talk about "strengthening" and "fixing" Social Security, and they even praise it. President Bush, for example, in defending his plan to transform Social Security, said:

> One of America's most important institutions, a symbol of the trust between generations, is also in need of wise and effective reform. Social Security was a great moral success of the 20th century, and we must honor its great purposes in this new century. The system, however, on its current path, is headed toward bankruptcy. And so we must join together to strengthen and save Social Security.[154]

Because of Social Security's enormous popularity,[155] few if any of today's politicians straightforwardly criticize Social Security as past opponents of the program did.[156]

When one overcomes these difficulties in seeing the similarities, what is revealed are extremely similar proposals. Though the starting points are different, requiring a very long transition period, the endpoints are essentially the same. Under all three, Social Security's benefits would cease to be based on a worker's wages, but rather would ultimately provide largely the

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[152] *See Landon Hits Social Security*, *supra* note 87 (The 1936 Republican presidential candidate Alf Landon asserted: "The [Social Security] act passed by the [Roosevelt] administration . . . assumes that Americans are irresponsible. It assumes that old age pensions are necessary because Americans lack the foresight to provide for their old age. I refuse to accept any such judgment of my fellow citizens.").

[153] For a description of the preferential tax treatment, see Altman, *supra* note 93, at 440–42.

[154] George W. Bush, Address Before a Joint Session of the Congress on the State of the Union (Feb. 2, 2005), *available at* http://georgewbush-whitehouse.archives.gov/news/releases/2005/02/20050202-11.html.

[155] Social Security has been polled throughout its history by many different pollsters. The results consistently show its overwhelming popularity. *See, e.g.*, *Highlights of Voter Opinions About Social Security*, STRENGTHEN SOCIAL SECURITY CAMPAIGN, *available at* http://strengthensocialsecurity.org/sites/default/files/Polling%20Highlights.pdf.

[156] *See infra* text accompanying note 165.

same subsistence-level benefits for all. If workers were to be able to maintain their standards of living once wages were lost, they would have to rely on the private sector to do so.

Under the Bush proposal, workers could reduce their Social Security payments even more in exchange for being able to divert a portion of their Social Security insurance contributions into private investment accounts administered by the government. Under the other proposals, Social Security would provide a low benefit without the option to lower it further. Nevertheless, tax incentives would presumably continue to be available to save for retirement on one's own. At base, the reduction in Social Security benefits under all of the proposals would put pressure on virtually all workers to save more if they had a hope of retiring.

What unites all three proposals is a common conceptual underpinning, different from that of Social Security. All three would transform Social Security by eliminating the features that make Social Security wage insurance. Instead, Social Security would be scaled back into a minimal payment unrelated to wages, with workers effectively required, whether explicitly mandated or not, to save to have some measure of economic security in the event of lost wages as the result of death, disability, or old age.[157]

The link between today's proposals and that of 1936 is not some unintended coincidence. Rather, the current proposals form a direct and continuous chain with those that came before. From the moment Social Security was first debated in Congress, opponents sought to defeat it. For the next seventy-six years, until the present day, conservatives have advocated scaling back and transforming Social Security as the Republican Party of 1936 advocated, and substituting individual savings instead. Efforts to scale back and change Social Security's basic structure and function have formed a continuous thread, though with different actors.[158]

President Dwight D. Eisenhower's election in 1952 brought the first Republican administration in twenty years. In that same election Republicans gained control of both Houses of Congress.[159] With that shift in power,

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[157] Once phased in, an obvious next step would be the imposition of a means test, already advocated by some today. If no means test were added, the program would provide neither insurance nor welfare, but a so-called demogrant, a flat payment based on achieving old age, becoming disabled, or being dependent on the wages of a deceased, disabled, or retired worker. *See supra* note 145.

[158] The efforts to end or transform Social Security have been well documented. *See e.g.*, ALTMAN *supra* note 8; DEAN BAKER & MARK WEISBROT, SOCIAL SECURITY: THE PHONY CRISIS (1999); MICHAEL A. HILTZIK, THE PLOT AGAINST SOCIAL SECURITY (2005); LAURSEN, *supra* note 102; MAX J. SKIDMORE, SOCIAL SECURITY AND ITS ENEMIES: THE CASE FOR AMERICA'S MOST EFFICIENT INSURANCE PROGRAM (1999).

[159] *Party Division in the U.S. Senate, 1789–Present*, U.S. SENATE (Aug. 20, 2012), http://www.senate.gov/pagelayout/history/one_item_and_teasers/partydiv.htm; *Party Divisions of the House of Representatives (1789 to Present)*, OFFICE OF THE CLERK, U.S. HOUSE OF REPRESENTATIVES (Aug. 20, 2012), http://artandhistory.house.gov/house_history/partyDiv.aspx. Throughout the 1930s the Democratic Party controlled Congress and the White House. In 1939, the Supreme Court upheld the Social Security provisions as constitutional. *See* Helvering v. Davis, 301 U.S. 619 (1937). When energy turned to the war effort after the attack on

a powerful coalition led by Senator Carl Curtis (R-Neb.) and the Chamber of Commerce sought to convince the new president to replace Social Security with a minimal flat benefit paid to everyone sixty-five and older, irrespective of work history[160]—as the Republican Party proposed during the 1936 election, as President Bush implicitly proposed during his administration, and as Bowles-Simpson and others are implicitly proposing currently.[161] Within ten months of taking office, however, President Eisenhower championed legislative proposals expanding Social Security.[162] During his tenure, he signed into law four major bills—in 1954, 1956, 1958, and 1960—expanding Social Security.[163] Throughout his eight years as president, he issued many statements on Social Security, in which he demonstrated both his understanding and support for Social Security's wage insurance.[164]

Undeterred, ideological opponents of Social Security continued to argue their case. In 1964, while campaigning for the Republican Presidential nomination in New Hampshire, for example, Senator Barry Goldwater (R-Ariz.) responded to a reporter's question about Social Security, "I would like to suggest . . . that Social Security be made voluntary, that if a person can provide better for himself, let him do it."[165] Campaigning for Goldwater, Ronald Reagan made the same point, asking rhetorically, "[C]an't we introduce voluntary features [into Social Security] that would permit a citizen

Pearl Harbor, Social Security receded as an issue. During the war years, benefits were not increased and FICA contributions were frozen in place. Welfare during this period served more people, had higher benefits, and was much more significant in providing economic security than Social Security. Republicans regained control of Congress in 1946. In 1948, Congress passed several bills denying Social Security coverage to over a half million workers. President Truman vetoed every bill, but his vetoes were overridden. *See* Carmon D. Solomon, Cong. Research Serv., 86–193, Major Decisions in the House and Senate Chambers on Social Security 224–25 (1986), *available at* http://www.ssa.gov/history/pdf/crs86193.pdf; *see generally* Altman, *supra* note 8, at 137–71.

[160] *See* Altman, *supra* note 8, at 174–77.

[161] For example, another prominent proposal, which is a variation on the same theme, was developed by the self-appointed Bipartisan Policy Center's Debt Reduction Task Force. The proposal is better known as the Rivlin-Domenici proposal. For its details, see Letter from the Office of the Chief Actuary, Social Security Administration, to Alice M. Rivlin and Pete Domenici (Nov. 17, 2010), *available at* http://www.ssa.gov/OACT/solvency/BipartisanTaskForce_20101117.pdf.

[162] *See* President Dwight D. Eisenhower, Special Message to the Congress Transmitting Proposed Changes in the Social Security Program (Aug. 1, 1953), *available at* http://www.presidency.ucsb.edu/ws/index.php?pid=9662#axzz; *see also* Solomon, *supra* note 159.

[163] Solomon, *supra* note 159, at 33–46.

[164] *See Eisenhower's Statements on Social Security*, Soc. Sec. Admin., http://www.ssa.gov/history/ikestmts.html (last visited Nov. 3, 2012).

[165] *See* Rick Perlstein, Before the Storm: Barry Goldwater and the Unmaking of the American Consensus 269–70 (2001). *The Concord Monitor* reported his remarks in a story headlined, "Goldwater Sets Goal: End Social Security, Hit Castro." The Goldwater nomination represented part of a coordinated, multi-pronged effort to infuse conservative ideas more forcefully and consistently into public policy making—and it worked, though it took decades to see the fruits of the labor. *See* Altman, *supra* note 8, at 198–202, 213.

who can do better on his own to be excused upon presentation of evidence that he had made provision for the non-earning years?"[166]

In the 1970s, two developments aided the cause of those determined to transform Social Security from wage insurance. The enactment of automatic increases to Social Security in 1972 coincided with so-called stagflation, which caused Social Security's benefits to rise faster than its income, resulting for the first time in projections of actuarial shortfalls in the Social Security program.[167] This provided an opening to undercut confidence in Social Security's future.[168]

A second, seemingly unrelated development occurred around the same time. After a decade of effort, Congress enacted the Employee Retirement Income Security Act of 1974, which provided for the comprehensive regulation of private pensions.[169] It imposed new funding, fiduciary, and reporting requirements on traditional pensions, and established individual retirement accounts, a new savings vehicle with preferential tax treatment. Within a decade, about seventeen percent of the full-time workforce was contributing to an individual retirement account.[170] Section 401(k) of the Internal Revenue Code was added in 1978, and so-called 401(k) plans grew very rapidly after regulations were issued in 1981.[171] Just two years after the issuance, almost half of all large firms in the United States had adopted 401(k) plans or were considering doing so.[172]

Those opposed to Social Security took notice. George W. Bush, then running for Congress in Texas, asserted at a campaign stop, "[Social Security] will be bust in 10 years unless there are some changes. The ideal solution would be for . . . people [to be] given the chance to invest the money the way they feel."[173] The idea of explicitly replacing Social Security's wage insurance with tax-preferred individual retirement accounts was first put for-

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[166] Ronald Reagan, A Time for Choosing (Oct. 27, 1964), *available at* http://www.reagan.utexas.edu/archives/reference/timechoosing.html.

[167] *See* Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102 (2012); *see also* Altman, *supra* note 8, at 216–17. The Trustees Reports projecting shortfalls in Social Security were accompanied by alarmist language about Social Security's impending bankruptcy, but the language of bankruptcy is inaccurate. Social Security receives most of its income from worker and employer FICA contributions, which will continue as long as Americans are still working. Consequently, the 2012 Trustees Report projects that even if the Trust Funds were drawn down to zero, so that interest income ceased, there would still be sufficient income to pay around seventy-five percent of promised benefits. *See* H.R. Doc. No. 112-102 (2012).

[168] *See generally* Altman, *supra* note 8, at 215–35.

[169] Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C.).

[170] Cong. Budget Office, Tax Policy for Pensions and Other Retirement Saving 44 (1987), *available at* http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/50xx/doc5011/doc05-entire.pdf.

[171] *See* Emp. Benefit Research Inst., *supra* note 116, at 1.

[172] *Id.* at 2.

[173] Richard W. Stevenson, *For Bush, a Long Embrace of Social Security Plan*, N.Y. Times, Feb. 27, 2005, at A1 (citing a statement by George W. Bush given in 1978 in Midland, Tex.).

ward in a book, which was the first publication of the Cato Institute.[174] Cato aggressively marketed the idea. The initial funding for Cato came from Charles Koch, whose father has been described as "a powerful, Texas newspaper baron, [who] had opposed Social Security during the time of its creation."[175]

With the election of President Reagan, opponents of Social Security believed they finally had a president who agreed with them that Social Security was not an appropriate role of government. In campaigning for Barry Goldwater in 1964, he had echoed Goldwater's suggestion that Social Security be made voluntary.[176]

In the first year of his presidency, President Reagan proposed an immediate and deep cut in Social Security's early retirement benefits, a proposal that set off a political explosion.[177] To quench the political firestorm, President Reagan established the National Commission on Social Security Reform (often referred to as the Greenspan Commission after Alan Greenspan, who chaired it). The Greenspan Commission explicitly rejected substituting private accounts for Social Security's guaranteed benefits and endorsed its basic structure.[178] Instead of private accounts, it proposed a variety of changes consistent with Social Security's structure as wage insurance. Congress enacted the recommendations as the Social Security Amendments of 1983.[179] Just a few months after the enactment of the recommendations of the Greenspan Commission, Cato devoted an entire issue of its journal to a series of articles that criticized Social Security and the recently enacted reforms. A number of articles in that issue argued that Social Security be replaced with individual retirement savings accounts.[180]

President Bill Clinton, though a Democrat, greatly facilitated the efforts of those who wanted to transform Social Security from wage insurance to the minimal payment advocated in 1936 by opponents of the program. In 1993, Clinton established the Bipartisan Commission on Entitlement and Tax Reform, which popularized the idea that "entitlements," an opaque reference to Social Security, Medicare, and Medicaid, were unaffordable and so

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[174] LAURSEN, *supra* note 102, at 113–14; *see also* FERRARA, *supra* note 49.

[175] LAURSEN, *supra* note 102, at 605–06, 641.

[176] Reagan, *supra* note 166.

[177] The now-famous expression, "Social Security is the third rail of American politics: Touch it and you die," was uttered by then-Speaker of the House, Tip O'Neill (D-Mass.). The ensuing National Commission on Social Security Reform was hastily conceived by the Reagan administration to quench the political firestorm. *See* LAURSEN, *supra* note 102, at 51–65; *see also* ALTMAN, *supra* note 8, at 227–35.

[178] *See 1983 Greenspan Comm'n on Soc. Sec. Reform, Appendix C, Chapter 2, Findings and Recommendations*, SOC. SEC. ADMIN. (1983), http://www.ssa.gov/history/reports/gspan5.html; *see also* ALTMAN, *supra* note 8, at 243.

[179] Social Security Amendments of 1983, Pub. L. No. 98-21, 97 Stat. 65.

[180] *See* James A. Dorn, *Social Security: Continuing Crisis or Real Reform?*, 3 CATO J. 335 (1983).

had to be fundamentally restructured.[181] Although the Commission did not achieve its required supermajority of three-fifths, the co-chairs did offer a proposal, which was a close precursor of both the Bush proposal and the Bowles-Simpson proposal.[182] It included price indexing and a diversion of a portion of workers' Social Security contributions into private accounts, as the Bush proposal did. It also included a change in the Social Security benefit formula and an increase in the statutory retirement age, as Bowles-Simpson has advocated. The thread from this point forward is easy to trace. Simpson was a member of the entitlements commission, Bowles was deputy chief of staff to President Clinton at the time the report was released, and the chief of staff for the commission later worked in the Bush administration.[183]

In addition to his establishment of the entitlements commission, President Clinton chose, for the 1994–96 Social Security Advisory Council, a number of members who were on record favoring undoing Social Security.[184] The Council fragmented and produced three separate packages of recommendations.[185] One recommended replacing Social Security with a flat benefit as the 1936 Republican Party recommended, with mandatory individual retirement accounts on top.[186] A second proposed flattening Social Security's benefit formula, similar to what Bowles-Simpson proposes, and mandating individual retirement accounts.

With the election of George W. Bush, the president was not only a proponent of the approach put forth in the 1936 Republican platform but was willing to champion it. President Barack Obama gave his fiscal commission

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[181] "Entitlements" refers to a variety of mandatory spending programs and some use the word to refer to tax expenditures, but it has become shorthand for Social Security, Medicare, and Medicaid. *See* LAURSEN, *supra* note 102, at 203–10; *see also* Nancy J. Altman, *The War Against Social Security*, DISSENT MAG. (Fall 2012), at 103–07.

[182] *See generally* BIPARTISAN COMM'N ON ENTITLEMENT & TAX REFORM, FINAL REPORT TO THE PRESIDENT (1994), *available at* http://www.ssa.gov/history/reports/KerreyDanforth/KerreyDanforth.htm. The chief of staff of the entitlements commission later became President Bush's Assistant Secretary for Tax Policy in the Treasury Department. Vanessa Small, *New at the Top: Mark Weinberger, Chief Executive-Elect of Ernst & Young*, WASH. POST, Mar. 5, 2012, http://www.washingtonpost.com/business/economy/new-at-the-top-mark-weinberger/2012/02/02/gIQAOYmRsQ_story.html.

[183] *See generally* Altman, *supra* note 181.

[184] Sylvester J. Schieber and Carolyn L. Weaver, for example, had written prolifically and critically about Social Security. *See* Robert Dreyfuss, *The End of Social Security as We Know It?*, MOTHER JONES, Nov.–Dec. 1997, *available at* http://www.globalaging.org/pension/us/socialsec/socials.htm (describing Schieber as "one of the privatization advocates on the president's Social Security Advisory Council"); *see generally* Sylvester J. Schieber, *Why We Need Social Security Individual Accounts*, WATSON WYATT INSIDER (Mar. 2005), http://www.watsonwyatt.com/us/pubs/insider/showarticle.asp?ArticleID=14376&Component=The+Insider; CAROLYN L. WEAVER, THE CRISIS IN SOCIAL SECURITY: ECONOMIC AND POLITICAL ORIGINS (1982).

[185] *See generally* REPORT OF THE 1994–1996 ADVISORY COUNCIL ON SOCIAL SECURITY, VOL. 1: FINDINGS AND RECOMMENDATIONS (Jan. 1997), *available at* http://www.ssa.gov/history/reports/adcouncil/report/toc.htm. *See generally* LAURSEN, *supra* note 102, at 321–31.

[186] 1994–1996 ADVISORY COUNCIL ON SOC. SEC., REPORT: VOLUME I: FINDINGS AND RECOMMENDATIONS (1997), *available at* http://www.ssa.gov/history/reports/adcouncil/report/toc.htm.

the authority to cut Social Security and appointed as its co-chairs two men known for their desire to cut it back.[187] He also has championed so-called auto-IRAs and an unprecedented reduction in the Social Security contributions rate.[188] Together with the recommendations of his fiscal commission, these proposals, despite the anti-privatization rhetoric of the Democrats, are close to what President Bush proposed and indeed part of the line of proposals, starting in 1936, to change fundamentally Social Security.

If these or similar proposals to scale back Social Security's protections were to be enacted, the nation's retirement income system would become less efficient, universal, secure, fair, and effective, as Section IV explains.

## IV. Superiority of Social Security to Private Sector Alternatives

Social Security is designed to help workers and their families maintain their standards of living when wages are lost in the event of death, disability, or old age. In providing that economic security, Social Security is more efficient, distributionally fair, universal, secure, and effective than any of its private sector alternatives. To see that striking superiority, it is imperative that Social Security is clearly understood as the wage insurance that it is.

As explained in Section II, insurance, not welfare and not savings, is superior in replacing wages lost in the event of death, disability or retirement. Perhaps as a consequence of that superiority, opponents of Social Security historically have generally refused to concede that Social Security is insurance (or have explicitly denied that it is).[189] Indeed, if one is opposed to Social Security, one cannot concede that Social Security is insurance, not savings. While workers can save individually, only the most affluent can self-insure.

The failure to recognize that Social Security is insurance, not welfare and not forced savings, has distorted the public discourse. As Section III explained, it has generated confusion over what it means to privatize Social Security. More fundamentally, it has obscured Social Security's striking superiority over private sector alternatives, because it has led to arguments based on straw men.

Savings and welfare have their own strengths, but those strengths are not marks of their superiority to insurance. Savings and welfare are different from, but not superior to, Social Security. Subsection A of this Section traces the efforts by opponents of Social Security to obscure what Social Security is and is not, and how those efforts, together with the failure of rigorous

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[187] *See supra* text accompanying note 183.

[188] *See supra* note 123.

[189] *See, e.g.*, Reagan, *supra* note 166 ("But we're against those entrusted with [Social Security] . . . they've called it 'insurance' to us in a hundred million pieces of literature. But then they appeared before the Supreme Court and they testified it was a welfare program. They only use the term 'insurance' to sell it to the people.").

analysis, have obscured Social Security's superiority in providing workers and their families with economic security. Once that underbrush of straw has been cleared away, Subsection B of this Section then explains Social Security's striking superiority to wage insurance provided privately.

### *A. Identifying the Straw Men*

Starting with Alf Landon in 1936, some have mischaracterized Social Security as forced savings. Then, they have argued that private savings arrangements are superior to saving through Social Security. Some have argued, for example, that, if individuals could save on their own rather than through Social Security, they would control the funds. They could direct how the funds were invested and perhaps get higher rates of return by investing in equities. Some of those confusing Social Security and savings have touted substituting private accounts for part of Social Security's protection because savings in individual retirement accounts can be bequeathed.[190]

These supposed advantages of private savings vehicles are all straw men. Social Security's benefits are not determined by investment returns, but are defined by statute. The higher rates of return that can be obtained through investment in equities could be obtained, on a collective basis, through Social Security,[191] and that could increase Social Security's income, but investment performance would not and should not determine the size of benefits. As wage insurance, not an investment vehicle, Social Security benefits are appropriately pegged to wages, not to investment returns.

Another straw man is that private savings are superior to Social Security, because private savings are under the saver's control and can be spent and bequeathed in ways that Social Security cannot. If the goal is to replace wages in the event of disability, death, or old age, however, the fact that funds can be spent on non-insured events is a disadvantage. Diverting savings for immediate needs and wants means that they are unavailable if and when the insured event occurs. Similarly, if the goal of wage replacement in the event of death, disability, or old age, the ability to bequeath funds to adult children, nonrelatives, or charities is a disadvantage. Insurance allows the greatest concentration of the funds for the specified purpose. In the case of Social Security, benefits are only available in the event of death, disability, or old age. Moreover, even in the event of death, the benefits are not paid to adult children who can support themselves or to other nonqualifying

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[190] *See, e.g.*, George W. Bush, *State of the Union*, *supra* note 154. *But see* David Kamin & Jason Furman, *Social Security and Inheritance: The Dubious Promise of Private Accounts*, CTR. FOR BUDGET & POLICY PRIORITIES (May 3, 2006), http://www.cbpp.org/cms/index.cfm?fa=view&id=329.

[191] Some supporters of Social Security's current structure, including the author, have proposed elsewhere that Social Security's accumulated reserves be diversified and invested partly in private equities, not just government obligations, in order to achieve the higher returns that equities have enjoyed over bonds historically. *See, e.g.*, ALTMEYER, *supra* note 110, at 88–89. See also the Ball-Altman plan, in ALTMAN, *supra* note 8, at 303–06.

heirs, but instead are limited to spouses, divorced spouses, children who are eighteen or younger (nineteen in the event still in high school), or children who are adults but became disabled before age twenty-two.[192] These limitations result in more precise targeting, and therefore, greater efficiency and effectiveness in achieving the intended goal.

An interwoven thread, with its own straw-man arguments, has confused Social Security with welfare. President Reagan may have been the first to call Social Security a safety net.[193] The language subtly but inexorably leads to the view that Social Security is welfare, not insurance. A safety net is something you fall into when you are in trouble. It catches you if you fall. One is glad the safety net is there, but falling into it is to be avoided, if possible. Insurance, on the other hand, is what prudent people buy because they are aware of life's risks and are planning ahead. People who are prudent do not need or want safety nets. It is why they purchase insurance (and accumulate savings).

David Stockman, President Reagan's OMB director, similarly called Social Security, along with other federal programs, a "coast to coast soup line."[194] Along those same lines, former Senator Alan Simpson (R-Wyo.), co-author of the Bowles-Simpson proposal, has called Social Security, "a milk cow with 310 million tits [sic]!"[195]

Taking the imagery of a safety net one step further, Representative and former Vice Presidential candidate Paul Ryan (R-Wis.), in the 2011 Republican response to President Obama's State of the Union Address, asserted:

> We are at a moment, where if government's growth is left unchecked and unchallenged, America's best century will be considered our past century. This is a future in which we will transform our social safety net into a hammock, which lulls able-bodied people into lives of complacency and dependency.[196]

Similarly, at a private fundraiser on May 17, 2012, Republican presidential nominee, Mitt Romney, stated, in an apparent reference to, among

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[192] *See* "Benefits for Children," Social Security Administration Publication No. 05-10085, ICN 468550, Aug., 2012, *available at* http://www.ssa.gov/pubs/10085.html#a0=0 (last viewed on Aug. 17, 2012).

[193] *See, e.g.*, David E. Rosenbaum, *Reagan's "Safety Net" Proposal: Who Will Land, Who Will Fall*, N.Y. Times, Mar. 17, 1981, at A1, *available at* http://www.nytimes.com/1981/03/17/us/reagan-s-safety-net-proposal-who-will-land-who-will-fall-news-analysis.html?pagewanted=all.

[194] William Greider, The Education of David Stockman and Other Americans 141 (1982).

[195] E-mail from Alan K. Simpson to Ashley Carson (Aug. 23, 2010, 06:52 P.M.).

[196] Representative Paul Ryan, GOP Response to President Obama's State of the Union Address (Jan. 25, 2011), *available at* http://www.npr.org/2011/01/26/133227396/transcript-gop-response-from-rep-paul-ryan.

other federal programs, Social Security whose benefits are received by one in four households:[197]

> There are 47 percent of the people . . . who are dependent upon government, who believe that they are victims, who believe that government has a responsibility to care for them. . . . I'll never convince them that they should take personal responsibility and care for their lives.[198]

All of these comments conjure up a false image of Social Security and generate straw men. Those confusing Social Security with welfare, or what is pejoratively referred to as a government "handout," often claim, for example, that it results in dependency. They also argue that it is not well targeted because it goes to middle class and wealthier workers who don't "need" its benefits. In response to these straw man arguments, some policymakers have proposed scaling back the benefits along the lines of the Bowles-Simpson and Bush proposals, analyzed in Section III. Others have proposed subjecting Social Security to a means test, which would transform it from insurance to welfare, with all the attendant disadvantages discussed in Section II.[199]

Welfare, which is based on need, can discourage work and savings, arguably producing dependency. In contrast, Social Security is earned through working and contributing for the requisite quarters of coverage to achieve insured status. It is not and should not be limited to those who are determined by some objective criteria to "need" it. Its benefits appropriately are pegged to replacing wages. Scaling back the benefits of those who are middle class or wealthier does not make the program more efficient; it simply makes it less adequate for those whose benefits are reduced.

In short, opponents historically have mischaracterized Social Security as forced saving, and have then conveniently argued that it lacks the strengths inherent to savings. Opponents have also mischaracterized it as welfare, a government handout, rather than an earned benefit, and then conveniently attributed the shortcomings of welfare to it while simultaneously arguing that means-testing benefits or scaling back benefits for the higher paid will better target its benefits to those in need, making it more efficient.

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[197] *Social Security*, PEPPER INST. ON AGING & PUB. POL'Y FACTS ON AGING 1 (NOV. 2005), pepperinstitute.fsu.edu/content/download/44399/305729/file/FoA_v1-1_Social.pdf.

[198] *Full Transcript of the Mitt Romney Secret Video*, MOTHER JONES (Sept. 19, 2012, 1:00 AM PDT), http://www.motherjones.com/politics/2012/09/full-transcript-mitt-romney-secret-video#47percent.

[199] Some policymakers have proposed subjecting Social Security's benefits to a means test. Under those proposals, people would presumably have to disclose income tax returns and valuations of assets to prove that their incomes were within the specified means. Currently, contributors need only provide their Social Security numbers and proof of the insured event to receive benefits. Those proposals would convert Social Security from insurance to welfare, with all its attendant disadvantages discussed above. Progressive benefit formula is simply calculation of what an insured receives. Means testing would require an intrusive examination of income and assets. *See supra* text accompanying notes 74–77.

When Social Security is clearly seen as the wage insurance it is, these arguments are clearly seen as the straw men that they are.

### *B. The Striking Superiority of Social Security Over Private Insurance Counterparts*

The only time lawmakers seriously considered allowing private employers to provide equivalent coverage as an alternative was in 1935, and that proved extremely complicated. A comparison of Social Security to its private sector alternatives reveals not only why it was so difficult to privatize Social Security, as narrowly defined, but also why the provision of wage insurance by the federal government is inherently more efficient, secure, universal, and fair.

Subpart (1) of this Subsection explains why Social Security is more efficient than its closest private sector counterparts are or could be, however structured. Subpart (2) then takes a slight detour to compare two forms of employer provided retirement arrangements—defined benefit plans, a form of insurance, and defined contribution plans, a form of savings—as background to the concluding Subpart. Finally, Subpart (3) explains how and why Social Security is more universal in its reach, more secure, superior in its benefits package, and fairer than its closest private sector counterparts are or could be.

#### *1. Social Security's Greater Efficiency*

Insurance is most cost effective and efficient when the risk pool is as broad as possible and adverse selection is minimal.[200] The risk pool for wage insurance is broadest when all wage earners are covered. Adverse selection is virtually impossible when participants must pay premiums starting at the moment they first start earning wages, receiving their first pay checks.

The only entity in our society that can mandate coverage of all workers and require participation as soon as they enter the work force and begin to earn wages is the federal government. Private insurance companies have no power of compulsion; private employers can only mandate the participation of their workforces. However, the federal government can mandate the participation of all workers in the nation. Because the government is setting the rules, it can compel participation, which in turn creates a very broad risk pool and reduces costs to all participants.

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[200] Adverse selection involves asymmetry of information between the insurer and insured. It can occur when individuals are not compelled to join at the outset, but rather opt in when their risk factors increase. *See Economics A–Z Terms Beginning with A: Adverse Selection*, The Economist, http://www.economist.com/economics-a-to-z#node-21529329 (last visited Aug. 17, 2012).

Social Security's wage insurance employs these efficiencies and economies of scale. Nearly all workers—ninety-four percent[201]—are covered by Social Security and therefore are part of the wage insurance risk pool.[202] No adverse selection is possible[203] because every covered worker must pay Social Security insurance contributions or premiums as soon as they start to earn wages.[204]

In addition to the ability to impose coverage mandatorily and prevent adverse selection, the federal government possesses other efficiencies over private insurance. Because the federal government is not competing for market share, there are no advertising costs, broker fees, or other marketing costs. Overhead is lower, because it is administered by civil servants, not high paid CEOs, and there is no money taken out for profits.[205]

Not surprisingly, given all of these cost advantages, Social Security achieves levels of efficiency not found in the administration of private insurance. According to the most recent Social Security Trustees Report, less than a penny of every Social Security dollar collected and spent is used for administration.[206] Leaving aside Social Security's disability insurance, which is more expensive to administer, the administrative costs of the retirement and

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[201] There are an estimated 159 million covered workers. *Fact Sheet: Social Security*, Soc. Sec. Admin., http://www.ssa.gov/pressoffice/factsheets/basicfact-alt.pdf (last visited Aug. 18, 2012).

[202] The only substantial group of workers that are not mandatorily covered are those employed by states and localities, where there is a constitutional question about imposing coverage on those employers. Notwithstanding the absence of compulsion, seventy-five percent of state and local employees are covered by Social Security, because the governmental entities for whom they work have voluntarily opted in under voluntary agreements. *See* Social Security Act § 218, 42 U.S.C. § 418 (2006).

[203] The ability of those state and local workers not participating in Social Security to gain disproportionately large benefits by working a short time in covered employment was addressed in 1983 with the enactment of the Government Pension Offset, Social Security Act § 202(k), 42 U.S.C. § 402(k) (2006), and the Windfall Elimination Provision, Social Security Act § 215(a)(7), 42 U.S.C. § 415(a)(7) (2006).

[204] *See* 26 U.S.C. § 3101(a) (2006); 26 U.S.C. § 3111(a) (2006 & Supp. V 2011). "Wages" is defined as "all remuneration for employment." 26 U.S.C. § 3121(a) (2006 & Supp. III 2009). The term "employment" is defined as "any service, of whatever nature, performed . . . by an employee for the person employing him." § 3121(b). In addition to mandatory coverage of state and local employees, Congress has specifically exempted "service performed in the employ of . . . a school, college, or university . . . if such service is performed by a student who is enrolled and regularly attending classes at such school, college, or university." § 3121(b)(10)(B); 42 U.S.C. § 410(a)(10) (2006 & Supp. III 2009).

[205] In 2011, John R. Stranfeld, the CEO of Prudential Insurance Company, for example, earned $6.44 million in salary and bonus. *See* Prudential Fin., Inc., 2012 Proxy Statement 54 (2012), *available at* http://www3.prudential.com/annualreport/report2012/proxy/images/Prudential-Proxy2012.pdf. In contrast, Michael J. Astrue, the Commissioner of the Social Security Administration, has earned an annual salary of $199,700 since 2010. *See* 5 U.S.C. § 5312 (2006) (specifying the Commissioner as a Level I employee); *Salary Table No. 2012-EX*: *Rates of Basic Pay for the Executive Schedule (EX)*, U.S. Office of Pers. Mgmt. (Jan. 2012), http://www.opm.gov/oca/12tables/pdf/ex.pdf (showing Level I employee salaries at $199,700).

[206] In 2011, Social Security's combined OASDI trust funds recorded income of $805.1 billion and expenditures of $736.1 billion. The combined administrative costs totaled $6.4 billion, or 0.79% and 0.87% of income and expenditures, respectively. *See* Bd. of Trs., Fed.

life insurance part of the Social Security system are 0.5% of total income and 0.6% of total expenditures.[207]

In contrast, private life insurance companies spent twenty-one cents of every dollar collected and sixteen cents of every dollar spent (not including additions to the reserves) on administrative costs in 2010.[208] Disability insurance is a relatively rare benefit in the private sector, and administrative costs for these programs are generally higher than for life insurance and retirement insurance, where the determinations for benefits are straightforward. Therefore, these numbers may understate the comparative difference in the administrative costs associated with private insurers and the federal government providing these benefits. Employer-sponsored retirement arrangements also have much higher administrative costs.[209]

### 2. *Comparison of Private Sector Defined Benefit and Contribution Plans*

Employer-sponsored retirement arrangements are generally divided into two broad categories, defined benefit plans, where the benefit is specified, and defined contribution plans, where the contribution is specified. Defined benefit plan arrangements, including Social Security, define the benefit that a worker receives at retirement or, in some cases, at disability or death. The contribution is determined by actuaries who must project the amount needed to provide the specified benefit, which turns on a variety of factors including the likelihood that the benefit will be paid, as well as projected duration over which it will be paid. In contrast, defined contribution plans specify the contribution going into the plan. The benefit depends on the investment performance of the contribution and the costs of administering the funds. Defined benefit plans are insurance; defined contribution plans are savings.

Because defined benefit plans are insurance, they have a number of advantages over defined contribution (savings) plans, as discussed in Section II. Insurance is more targeted in protecting against defined risks. Wage insurance, for example, is precisely geared to the goal of replacing a set percentage of wages, in contrast to saving for replacement of wages, which requires virtually impossible guesswork for any particular individual, as op-

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Old-Age & Survivors Ins. & Fed. Disability Ins. Tr. Funds, 2012 Annual Report, 6 tbl.II.B1, *available at* http://www.ssa.gov/oact/tr/2012/tr2012.pdf.

[207] *See id.* (stating that Social Security's OASI trust fund alone recorded income of $698.8 billion and expenditures of $603.8 billion, with administrative costs totaling $3.5 billion).

[208] Am. Council of Life Insurers, Life Insurers Fact Book 2011 35, 49, *available at* http://www.acli.com/Tools/Industry%20Facts/Life%20Insurers%20Fact%20Book/Documents/2011%20Fact%20Book.pdf.

[209] Private-sector-defined benefit plans spent 2.5¢ on administrative costs of every dollar of income and 5¢ of every dollar expended in 2010. *See* 2009 Emp. Benefits Sec. Admin., Dep't of Labor Private Pension Plan Bull. 8 tbl.A4, *available at* http://www.dol.gov/ebsa/PDF/2009pensionplanbulletin.pdf. 401(k) administrative costs are often hidden and hard to detect, but generally higher.

posed to a group. It allows pooling of all the risks and payouts targeted to reimbursement if and when an insurable event occurs.

In contrast, defined contribution plans, by definition, promise only the amount being contributed. Consequently, under those plans the investment and other risks fall totally on the participant whose benefit is only as large as the investments permit. This is an advantage for employers, because it limits their commitment to simply the size of the contribution, but a serious insecurity for employees. Under defined benefit plans, it is the plan sponsor's job to ensure that sufficient funds exist to pay the promised benefit. The risk, therefore, is borne by the employer. This is an advantage for employees, but a disadvantage for private employers.

Furthermore, private savings can be withdrawn and used for other purposes, even when tax favored for a particular purpose and therefore restricted, as in the case of 401(k) and individual retirement accounts. For example, 401(k) plans generally allow so-called "hardship" withdrawals to cover medical or educational costs, or the costs associated with purchasing a home.[210] In addition, these plans generally allow borrowing of account balances, although if the loan is not paid back, tax penalties apply.[211] Moreover, when workers with 401(k)s change jobs, they may receive a lump sum payout, though again some tax penalties apply if the funds are not rolled over into another retirement savings vehicle.[212] Even at retirement, accounts may be distributed in a lump sum and used for purposes other than regular retirement income throughout the remainder of the retiree's life.[213]

At retirement, the so-called leakage problem of 401(k)s and other savings plans could be overcome by prohibiting lump sum distributions and instead requiring the purchase of an annuity at retirement, but that is simply requiring insurance rather than savings upon reaching retirement age. As discussed in Section II, this creates the risk of market downturns just as workers are ready to transform their savings into insurance.[214]

At the same time, private-sector-defined benefit pension plans have disadvantages, some of which make savings plans more attractive to some employees and employers. Because private-sector-defined benefit plans are not universal, are not identical from plan to plan, and are not portable from job to job, they too experience some "leakage." Since benefits are generally based on final earnings and years of service, they are excellent for older workers who have worked virtually their entire careers for the same employer. For the same reasons, they are inferior for mobile workers who may only be entitled to the non-indexed "final" pay earned at employment from

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[210] *See, e.g.*, ALICIA H. MUNNELL & ANNIKA SUNDÉN, COMING UP SHORT: THE CHALLENGE OF 401(K) PLANS 131 (2004).
[211] *Id.* at 125–31.
[212] *Id.* at 131–35.
[213] *Id.* at 131.
[214] *See* discussion *supra* Part II.C.

the start of one's work life which ended decades earlier.[215] Those workers often exercise the option to take a lump sum payment when they change jobs.

In addition, private pension plans, which promise annuities not payable for decades, are inherently insecure. The one paying the annuity may have insufficient funds when the time for payment arrives or, worse, may no longer be around. If funds are accumulated in advance, they may suffer investment losses, or worse, be embezzled.

The Employee Retirement Income Security Act of 1974 ("ERISA") sought to improve the security of private-sector-defined benefit plans,[216] yet the government regulation has made them less attractive to employers. These arrangements must be funded in advance and must meet minimum funding standards.[217] Federal fiduciary responsibilities are imposed on those who have responsibility for the plan operation and assets.[218] Benefits are required to be insured by the Pension Benefit Guaranty Corporation.[219]

Because these arrangements are voluntary, though, these and other requirements have made them less affordable and less attractive to employers. Historically, they have been established to serve employer interests. To the extent they must conform to federal requirements, they are less able to serve the employer.[220]

The issues that resulted in the enactment of ERISA are partly what have caused private-sector-defined benefit plans to be less prevalent today and also what caused the complexity in the negotiation over the Clark amendment during the conference committee meetings in 1935. As regulation of traditional private pensions has increased, as accounting rules have changed regarding how pension liabilities are to be reported, and as unions and manufacturing have declined, employers have increasingly terminated, frozen, or closed their plans to new employees.[221]

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[215] *See* Robert L. Clark & Fred W. Muzenmaier, *Impact of Replacing a Defined Benefit Pension with a Defined Contribution Plan or Cash Balance Plan*, 5 N. Am. Actuarial J. 32, 44 (2000), *available at* www.soa.org/library/journals/north-american. . ./naaj0101_3.aspx.

[216] Employee Retirement Income Security Act of 1974, Pub. L. No. 93–406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C.). ERISA also was intended to make private employer plans fairer by, for example, limiting the number of years of service needed to vest in the benefits that had accrued.

[217] *See* 29 U.S.C. § 1083 (2006).

[218] §§ 1101–1114.

[219] § 1322.

[220] *See* Altman, *supra* note 93, at 444; *see also* Altman, *supra* note 8, at 24.

[221] *See Defined Benefit and Defined Contribution Retirement Plans*, Nat'l Conference of State Legislatures (2005), http://www.ncsl.org/programs/fiscal/defineretire.htm. Defined benefit plans are ones where the benefit (e.g., fifty percent of final pay) is promised or defined. *Id.* Defined contribution plans, in contrast, are ones where the amount to be contributed is promised or defined. *Id.*

### 3. *Social Security's Superior Coverage, Security, Benefit Package and Distribution*

Social Security has all of the advantages of private-sector-defined benefit plans, but none of the disadvantages. Social Security has virtually universal coverage with the primary exception being about twenty-five percent of the employees of state and local government. It covers such hard-to-reach groups as household employees, farm workers, other intermittent and seasonal workers, part-time workers, full-time workers working part time for several employers, independent contractors, other self-employed, and all employees of small businesses, irrespective of the size. In contrast, private-sector-defined benefit pension plans have never covered more than about half the work force, and have never been feasible for smaller employers, notwithstanding much effort and incentives to make them so.[222] Currently, they cover only about twenty percent of the workforce, and the downward trajectory shows no signs of abating.[223] The plan of choice these days is the 401(k) plan, but it also covers less than half the workforce. Even if private sector defined benefit plans were mandated, it is hard to imagine how they could cover workers such as household workers and part time workers, who are covered by Social Security. Because Social Security has a nationwide pool, these and other groups can be covered at modest cost.

Social Security's guaranteed benefits are much more secure than private sector retirement savings, which can be lost as part of a market downturn or simply poor or unlucky investment decisions. They are also much more secure than private-sector-defined benefit plans or insurance offered by private companies. Social Security needs none of the safeguards of the Pension Benefit Guaranty Corporation. The plan sponsor is the federal government, which is permanent, and so will not go out of business and has the power to tax and borrow. For these reasons, it is much more secure than any private arrangement could be.

All risks are spread nationwide, not concentrated on single employers, insurance companies, or worse, individual workers. Furthermore, Social Security, unlike private-sector-defined benefit pension plans, is easily and completely portable from employer to employer, but imposes few administrative costs on them. It is carried from job to job; records are kept seamlessly by the Social Security Administration through the use of Social

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[222] *See, e.g.*, Dennis Jacobs, *Nearly Half of Small Business Owners May Never Retire*, GALLUP (Oct. 1, 2010), http://www.gallup.com/poll/143351/nearly-half-small-business-owners-may-retire.aspx; *see also Covering the Uncovered: Final Report of the Conversation on Coverage*, PENSION RIGHTS CTR. (May 2007), http://www.conversationoncoverage.org/about/final-report/covering-the-uncovered.pdf (describing innovative proposals to address the lack of coverage).

[223] Barbara A. Butrica, et al., *The Disappearing Defined Benefit Pension and Its Potential Impact on the Retirement Incomes of Baby Boomers*, SOC. SEC. BULL. (2009), *available at* http://www.ssa.gov/policy/docs/ssb/v69n3/v69n3p1.html.

Security numbers.[224] Wages from all covered employment are automatically recorded by the Social Security Administration and used in calculation of benefits. Consequently, with Social Security, there is no leakage, when workers move from job to job.

Indeed, there is no leakage whatsoever. The most effective way to prevent withdrawals before retirement and to target the funds where the financial risk is greatest is requiring purchase of wage insurance, not accumulation of savings, as soon as wages are earned. That, in short, is what Social Security does.

Moreover, because the plan sponsor is the federal government, Social Security's wage insurance includes features that are not found in the private sector. For example, private sector annuities and defined benefit pensions reduce the annuity amount of the primary insured if a spouse is added. In contrast, Social Security's annuities provide add-on benefits for the addition of a joint and survivor annuity without reducing by a penny the life annuity portion if the worker is married.[225] Moreover, if the worker has been divorced after having been married ten years, even if there have been multiple divorces involving just that one worker, there are add-on spouse and widow(er) benefits for the divorced spouse, no matter how many divorces, without reducing the life annuity portion.[226] Moreover, benefits are annually increased to offset the effects of inflation.[227] It provides complete inflation protection, regardless of the rate of that inflation. Consequently, unlike traditional private pension benefits which erode over time, Social Security maintains its purchasing power. It insures, as discussed in Section II, against low lifetime earnings as well.

From the beginning, Social Security has been built on the twin concepts of individual equity and social adequacy for the most disadvantaged among us. Wage insurance is crucial in a modern industrialized economy. Social Security's role in the provision of this vital economic security should be increased, not privatized.

## V. Increasing the Economic Security of Working Families

Multiple studies project that, even with Social Security, most of today's workers will not be able to retire and maintain their standards of living thereafter. The Center for Retirement Research, for example, has constructed a Retirement Risk Index, which reveals that fifty-one percent of households

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[224] *See* Altman, *supra* note 8, at 113–15 (describing the creation of Social Security numbers).

[225] ERISA requires that payments be made in the form of joint and survivor annuities, unless participants and their spouses opt out. *See* ERISA § 205, 29 U.S.C. § 1055 (2006).

[226] *See* 42 U.S.C. § 402 (2006); *see also Retirement Planner: Benefits for Your Divorced Spouse*, Soc. Sec. Admin., http://www.ssa.gov/retire2/yourdivspouse.htm (last visited Oct. 31, 2012).

[227] 42 U.S.C. § 415(i) (2006).

will not be able to maintain their standards of living in retirement even if they annuitize all of their assets.[228] It has found that sixty-five percent of American households are at risk of insufficient income at retirement, when one takes into account potential health and long-term care costs.[229] The Center has calculated an enormous retirement savings gap—the amount Americans have saved and should have saved at this point in their lives—of $6.6 trillion.

This looming retirement income crisis is just beginning to reach the attention of policymakers and the public.[230] Privatization of Social Security, however defined, would increase the already large retirement income deficit. In light of Social Security's near universality, efficiency, fairness in its benefit distribution, and security, the logical response to that deficit is to increase Social Security's benefits.

Currently, those benefits provide a strong foundation upon which to build sufficient retirement income but are far from adequate by themselves. Its benefits are modest by virtually any measure. As an absolute measure, they average just $13,500 a year, less than full-time, minimum wage work.[231] In relation to the wages they are designed to replace, they do not come close to replacing a large enough percentage of wages to allow workers to maintain their standards of living once wages are gone.[232] Moreover, these al-

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[228] *See* Alicia Munnell et al., National Retirement Risk Index: How Much Longer Do We Need to Work?, 3–4 (June 2012), *available at* http://crr.bc.edu/wp-content/uploads/2012/06/IB_12-12-508.pdf. McKinsey & Company has similarly constructed a Retirement Readiness Index, which similarly reveals that most families will have insufficient retirement income to maintain standards of living, with younger households and lower income households the least prepared. *See Restoring American's Retirement Security: A Shared Responsibility*, McKinsey & Co. 6–8 (Oct. 2009).

[229] Munnell et al., *supra* note 228, at 7.

[230] *See, e.g.*, *The Road to Retirement*, Editorial, N.Y. Times (Sept. 16, 2012), http://query.nytimes.com/gst/fullpage.html?res=9D0DE6D81331F935A2575AC0A9649D8B63.

[231] With regard to absolute measures, new research is underway to develop an Elder Economic Security Standard. Developed by the Gerontology Institute at the University of Massachusetts, Boston and Wider Opportunity for Women, the new standard seeks to be a more refined measure than the federal poverty line. The new standard takes into account expenses such as health care costs and transportation, not expressly taken into account in the poverty line measure. *See Elder Economic Security Standard Index: Frequently Asked Questions*, Wider Opportunities for Women 3–4, *available at* http://www.wowonline.org/ourprograms/eesi/ documents/NatlEESIIndexFAQs.pdf; *see also The National Elder Economic Security Initiative Program,* Wider Opportunities for Women, http://www.wowonline.org/pdf/NatlEESIdatasheet.pdf (last visited Oct. 18, 2012) (discussing what costs are included in the Elder Economic Security Standard). Average Social Security benefits are well below this new standard. For an elder homeowner, in good health, an average Social Security benefit covers only eighty-one percent of minimal expenses; for a renter, the percentage falls to sixty-three percent. *See id.* With respect to international comparisons, the United States Social Security system replaces a lower percentage of wages than other OECD countries. *See* Virginia P. Reno & Joni Lavery, *Social Security and Retirement Income Adequacy*, 25 Nat'l Acad. of Soc. Ins. (Issue Brief) 1, 3 (2007), *available at* http://www.nasi.org/usr_doc/SS_Brief_025.pdf.

[232] *See supra* note 48.

ready minimal replacement rates will be lower in the future, as the result of already enacted changes.[233]

Further, the current replacement rates, even ignoring future reductions, are extremely low by international standards. They rank toward the bottom when measured against the old-age benefits provided by other developed countries, as the following chart reveals:

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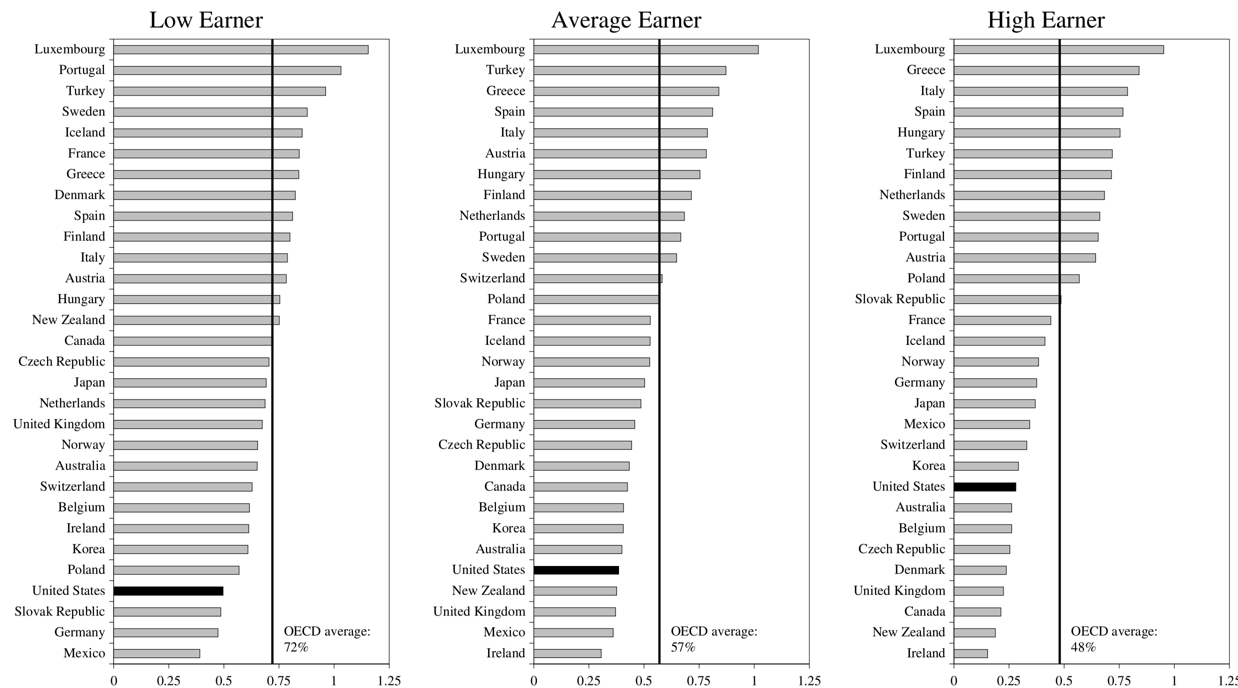
[233] The Social Security Amendments of 1983 included a gradual increase in the age at which retirees receive full benefits. The increase in Social Security's normal retirement age is in the process of being phased in. For those born in 1938, the normal retirement age, for Social Security purposes, is sixty-five and two months. For each subsequent year of birth, the normal retirement age increases by two months, until it reaches age sixty-six for those born in 1943 year of birth. The normal retirement age stays at age sixty-six until the year of birth 1955, when it again increases two months for every subsequent birth year, until the normal retirement age of sixty-seven is reached. *See generally Age to Receive Full Social Security Retirement Benefits*, Soc. Sec. Admin., http://www.ssa.gov/pubs/retirechart.htm (last updated June 19, 2012). Because of Social Security's structure, increasing the statutorily-defined "Retirement Age" is indistinguishable from an across-the-board benefit cut for retirees. *See* Lieberman, *supra* note 136. It amounts to around a 14% reduction in benefits for people born in 1960 or after. Lieberman, *supra* note 136. As a consequence, in 2030, only 49% of a low-income worker's wages will be replaced, rather than the current rate of 54%; for a medium-income worker, only 36.5% will be replaced, rather than the current rate of 40%; and for a worker earning at the maximum taxable wage base, the replacement rate will have fallen from 28% to 24%. *See* Alicia Munnell, Ctr. for Retirement Research, The Declining Role of Social Security 1 (2003), *available at* http://crr.bc.edu/briefs/the-declining-role-of-social-security. *See also supra* note 48. Moreover, the effective replacement rate will be even lower in the future because Medicare premiums, which are automatically deducted from Social Security benefits for most beneficiaries, are, as a result of the rapid increase in health care costs, increasing faster than inflation generally. That trend is projected to continue in the future. *See* Ctrs. for Medicare & Medicaid Servs., The 2012 Annual Report of the Bd. of Trs., Fed. Hosp. Ins. and Fed. Supplementary Med. Ins. Trust Funds 142–44 (2012), *available at* http://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/ReportsTrustFunds/Downloads/TR2012.pdf. As a result, an average wage earner retiring at age sixty-five in 2030 will receive only about 32% of pre-retirement wages, rather than today's 41%, when Medicare's increased premiums, on top of the change in the normal retirement age, are taken into account. Net benefits will be even lower, because an increasing number of people will be required to pay income tax on benefits, as a result of a 1983 provision which subjects taxpayers with higher earnings to count a portion of their Social Security benefits as taxable income. The provision did not index the earnings thresholds. As a result of that provision, that same median earner's net replacement rate is projected to fall to 29%. *See* Reno & Lavery, *supra* note 231, at 9.

SOCIAL SECURITY REPLACEMENT RATES IN OECD COUNTRIES BY EARNINGS LEVEL[234]




[234] Low earners earn half of the average earner, and high earners earn twice the average earner. *See Pensions at a Glance 2005*, OECD, http://www.oecd.org/els/socialpoliciesanddata/pensionsataglance2005.htm (last visited Nov. 2, 2012) (referring to single, full-career workers drawing pensions from the specific country's mandatory pension programs at the normal eligibility age).

In the past, traditional defined benefits plans picked up the shortfall for some employees.[235] Even at their height, though, they never covered more than about half the workforce, and now cover only about twenty percent of the workforce.[236] While defined contribution 401(k) plans have grown over recent years, they too only cover about half the work force.[237] Moreover, they have even more shortcomings than private-sector-defined benefit plans. These arrangements often lack employer contributions, shift the risks of investment and longevity to the individual, have high administrative costs, and are vulnerable to being cashed out before retirement.[238] Perhaps of greatest concern, accumulations in those plans are extremely low. In 2004—prior to the economic collapse—the median account balance for household heads aged fifty-five to sixty-four participating in a 401(k) plan was $60,000, a starkly inadequate sum of money for individuals who may spend fifteen or more years in retirement.[239] The recent economic downturn has cost the American people an estimated two trillion dollars in pension wealth.[240]

Although not generally recognized as such, Social Security is the largest asset most Americans have.[241] The Social Security Administration actua-

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[235] Reliance on private pensions and individual savings is, in some ways, an historical accident. Such reliance, which has many shortcomings, has never achieved complete retirement security for all the nation's workers. *See* Nancy Altman, Address at the National Academy of Social Insurance's 19th Annual Conference: Turning Perils into Opportunities: Perfecting Retirement Security in the 21st Century, 12–14 (Feb. 1, 2007), *available at* http://www.nasi.org/usr_doc/Session_III_Transcript_02_01_07.pdf.

[236] Traditional employer-sponsored pensions, so-called defined-benefit plans, which covered about forty percent of the private-sector workforce in 1977, covers only about twenty percent today. *See supra* text accompanying note 233.

[237] Even prior to the economic collapse, two-thirds of the elderly received half or more of their income from Social Security. The nonpartisan Center on Budget and Policy Priorities projected in 2005, again, well before the economic collapse, that without Social Security, almost half of people aged sixty-five and older would have incomes below the poverty line. *See* Van De Water & Sherman, *supra* note 78, at 1–2. ("Without Social Security benefits, 45.2 percent of elderly Americans would have incomes below the poverty line, all else being equal.")

[238] *See* Alicia H. Munnell & Annika Sunden, Ctr. for Ret. Research, 401(k) Plans are Still Coming Up Short 3–5 (2006), *available at* http://crr.bc.edu/briefs/401k-plans-are-still-coming-up-short.

[239] *Id.* at 5–6.

[240] *See* Emily Brandon, *Retirement Savers Lost $2 Trillion in the Stock Market*, U.S. News & World Rep. (Oct. 8, 2008), http://www.usnews.com/blogs/planning-to-retire/2008/10/08/retirement-savers-lost-2-trillion-in-the-stock-market.html.

[241] Some advocates have rhetorically used the Supreme Court case Flemming v. Nestor, 363 U.S. 603 (1960), to claim or imply that the right to Social Security is worthless: a naked promise subject to the whim of the government and much less secure than private sector retirement arrangements. *See, e.g.*, Deroy Murdock, Cato Inst., It's Not Your Money: Americans Have no Right to Social Security Benefits (1999), *available at* http://www.socialsecurity.org/daily/06-22-99.html. This is an overreading of the case, however. The case was brought by an immigrant who had been deported because of his membership in the Communist Party. He challenged as unconstitutional a statute terminating the payment of Social Security benefits to Communists who had been deported. The Court held, in a five-to-four decision, that "[it] must conclude that a person covered by the act has not such a right in benefit payments as would make every defeasance of 'accrued' interests violative of the Due Process Clause of the Fifth Amendment." *Flemming*, 363 U.S. at 611. However, it also stated,

ries have calculated that if a thirty-year-old worker earning around $30,000 (with two young children and a non-working spouse) died, then the present value of Social Security survivor benefits for this family would be around $550,000; if the worker became disabled at this age, then the present value of Social Security disability benefits for this family would be around $583,000.[242] In addition, the actuaries have calculated that the present value of retirement benefits for a sixty-five-year-old worker having career-average earnings around $43,000 (with a non-working spouse) is around $445,000.[243]

Moreover, like the assets of trusts generally, creditors of beneficiaries cannot reach Social Security benefits the way they can seize assets not held in trust. It cannot be sold or borrowed against. That inability to alienate increases the value of Social Security even more. Social Security benefits are always there when and if Americans need them—beyond the reach of creditors, swindlers, and poor personal decisions.[244] Unlike 401(k) accounts, not a penny of Social Security's value was lost in the recession. Rather, its monthly benefits continued unabated. Older workers who lost their jobs and their homes were able to secure monthly income by claiming those benefits.

Scaling back on Social Security while requiring or inducing additional retirement savings is the wrong way to go. Instead, Social Security should be expanded. Increasing Social Security's benefits can be done simply and quickly with no start up costs and no additional regulation. It would benefit

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"[t]his is not to say, however, that Congress may exercise its power to modify the statutory scheme free of all constitutional restraint. The interest of a covered employee under the act is of sufficient substance to fall within the protection from arbitrary governmental action afforded by the Due Process Clause." *Id.*

[242] The example, produced by the actuaries at the Social Security Administration, assumes that the worker is a medium income worker who started work at age twenty-one and became disabled or died at age thirty in 2012. He or she was a so-called "medium-scaled worker," and was earning, in 2012, $34,157 in the survivor's case, and $29,225 in the disability case. The worker's spouse was twenty-eight at the time of the disability or death, had no Social Security covered earnings, and does not remarry. They had two children aged two and newborn at the time of the disability or death. *See* Memorandum on The Insurance Value of Potential Survivor and Disability Benefits for an Illustrative Worker, from Michael Clingman, Kyle Burkhalter, and Chris Chaplain, Actuaries, to Alice H. Wade, Deputy Chief Actuary, Office of the Chief Actuary, Soc. Sec. Admin. (Sept. 27, 2012) (on file with the author). The present values, under the identical facts will be higher in future years.

[243] The example, produced by the actuaries at the Social Security Administration, assumes that the worker has indexed average earnings of around $43,000. The worker was born in 1947, started working at age twenty-one, and is claiming retirement benefits in 2012. The worker's spouse is assumed to be the same age as the worker but has no Social Security covered earnings. *See* Memorandum on The Insurance Value of Retirement Benefits for Illustrative Worker Cases, from Kyle Burkhalter, Actuary, Michael Clingman, Actuary, & Chris Chaplain, Actuary, to Alice H. Wade, Deputy Chief Actuary, Office of the Chief Actuary, Soc. Sec. Admin. (Aug. 8, 2012) (on file with the author). The present values, under the identical facts would be higher in the future.

[244] *See* Social Security Act § 207, 42 U.S.C. § 407 (2006). An exception was made under the Debt Collection Improvement Act, which permits the U.S. Treasury to garnish the lesser of fifteen percent or the amount over $750 of Social Security benefits for non-tax federal debts, such as student loans. Pub. L. No. 104-134, 110 Stat. 1321 (1996). These collections have begun. *See, e.g.*, Ylan Q. Mui, *Durbin Targets Private Student Loan Defaults*, WASH. POST, Mar. 20, 2012, at A13.

not just retired workers but also disabled workers, their families, and the families of deceased workers.

Despite the conventional wisdom that Social Security is "unsustainable," the nation can afford substantially increasing its benefits. At its most expensive, Social Security's cost will be much less, as a percentage of gross domestic product, than most other developed countries today spend on their public old age pensions.[245] In 2007, for example, Germany spent 7.9% of its GDP, Austria, 8.9%, France, 10.3%, Portugal, 8.7%, Japan, 7.5%, and Italy, 11.1% on their public old age pensions.[246] In contrast, today Social Security accounts for about 5% of GDP; in about a quarter of a century, Social Security is projected to account for just 6.4% of GDP and then gradually decline and stabilize around 6% thereafter.[247]

The increase of around 1.4% of GDP is not only manageable but also unsurprising and fully warranted.[248] At a time when the percentage of the population composed of people over age sixty-five will grow from thirteen percent to twenty percent, it is appropriate that they consume a larger percentage of the nation's goods and services.[249]

The question of whether to reduce Social Security's benefits and look to the private sector to provide the bulk of workers' income when wages are lost as the result of disability, death or old age, or alternatively, to expand Social Security's benefits is not a matter of mathematics or economics[250] but of political choices and values.

## VI. Conclusion

In light of virtually everyone's dependence on wage income, insurance against the loss of those wages is essential for basic economic security. Savings are important for economic security as well, but generally they will not be enough to replace all the wages lost, month after month and year after year, when workers become seriously and permanently disabled. Nor will they generally be sufficient to replace wages lost when workers die, leaving behind families dependent on those wages. Nor are savings likely to be

[245] *Social Expenditure—Aggregated Data*, Org. for Economic Co-operation & Development, *available at* http://stats.oecd.org/Index.aspx?QueryId=4549#.

[246] *See id.*

[247] Bd. of Trs., Fed. Old-Age & Survivors Ins. & Fed. Disability Ins. Trust Funds, 2012 Annual Report, H.R. Doc. No. 112-102 at 3 (2012). Currently, Social Security accounts for 5% of U.S. GDP. *Id.* at 3.

[248] Indeed, Social Security's entire projected actuarial imbalance is just 0.9% of GDP. *Id.* at 14.

[249] *See* Population, Federal Interagency Forum on Aging Related Statistics, AgingStats, http://www.agingstats.gov/Main_Site/Data/2012_Documents/Population.aspx (last visited Nov. 1, 2012).

[250] Professor Martin Feldstein has sought to show that Social Security depresses earnings. Many other economists have disputed his research. *See* Laursen, *supra* note 102, at 122–25.

enough to replace wages for all the retirement years of the overwhelming majority of workers.[251]

Even the thriftiest of individuals is not likely to be able to save sufficient amounts for these contingencies without the benefit of inherited wealth or an unusually large income.[252] Almost no workers are likely to be able to generate sufficient assets during their working years to replace a significant percentage of their lost wages for all the years that those wages might need to be replaced. Rather, what they need is insurance, which provides a steady, guaranteed source of income if and when wages are lost.

The federal government is permanent and has the power to compel participation. As a result of those and many other advantages, such as the power to tax, it can provide universal group wage insurance more efficiently, universally, fairly, securely, and effectively than the private sector—and it does, in the form of Social Security.

Social Security's striking superiority, together with the essential role that it plays in providing basic economic security, should put to rest designs to reduce its modest benefits and provide a larger role for the private sector. Indeed, in light of the nation's looming retirement income crisis, rational policymaking should result in legislation increasing Social Security's modest benefits.

The desire to privatize Social Security, however, does not derive from a dispassionate analysis of objective criteria like coverage, efficiency, distributional fairness, and security. Rather, a review of the history of Social Security reveals that the fight over whether to privatize Social Security is one rooted in ideology and values.

From the start, opponents have believed that Social Security is an unwarranted usurpation by the federal government that restricts the freedom of its citizens and breeds dependency.[253] In contrast, supporters believe that So-

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[251] If married, workers generally would want to ensure the savings lasted until their spouses' deaths as well. In addition to providing benefits to spouses and widows, Social Security also provides benefits to dependent children and sometimes grandchildren in the event of a worker's death or disability. Indeed, Social Security is the largest source of family income for grandparents rearing grandchildren.

[252] To provide a sense of perspective, the median household income in the United States in 2009 was slightly less than $50,000. That amount includes interest from savings accounts and other unearned income as well as wages and salaries. Half of all households had incomes lower than $50,000. *See* U.S. CENSUS BUREAU, THE 2012 STATISTICAL ABSTRACT, SECTION 13: INCOME, EXPENDITURES, POVERTY, AND WEALTH, tbl. 690, *available at* http://www.census.gov/prod/2011pubs/12statab/income.pdf.

[253] During the debate over the legislation, a Congressman asserted, "this bill opens the door and invites the entrance into the political field of a power so vast, so powerful as to threaten the integrity of our institutions and to pull the pillars of the temple down upon the heads of our descendants." Another argued that it was "compulsion of the rankest kind." *See* ALTMEYER, *supra* note 126; ALTMAN, *supra* note 8. In *Conscience of A Conservative*, Barry Goldwater claimed that Social Security and public assistance at the federal level inevitably lead to "unlimited political and economic power . . . as absolute . . . as any oriental despot." Beneficiaries and recipients are, according to Goldwater, transformed "into a dependent animal creature." He warns that "the collectivists have not abandoned their ultimate goal—to subordinate the individual to the State—but their strategy has changed. They have learned that

cial Security enhances freedom. People who have independent, reliable income have more freedom, not less. They can choose where they want to live rather than relying on the charity of relatives or friends. They have freedom from financial worry. It is noteworthy that the Universal Declaration of Human Rights, adopted by the General Assembly of the United Nations, provides that "Everyone, as a member of society, has the right to social security and is entitled to realization . . . of the economic . . . rights indispensable for his dignity . . . ."[254]

Despite Social Security's striking superiority, it is unlikely that those who favor privatizing Social Security will quit the fight. Consequently, those who value the continued provision of wage insurance through Social Security must be prepared to remain in the ring as well.

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Socialism can be achieved through Welfarism quite as well as through Nationalization." In similar language, Representative Paul Ryan (R-Wis.) has said that "Social Security right now is a collectivist system, it's a welfare transfer system." *See* Vincent Miller, *Secret Ryan Transcript: Social Security and Medicare are the Target*," ALL THINGS (Sept. 19, 2012), http://www.americamagazine.org/blog/entry.cfm?blog_id=2&entry_id=5368.

[254] It was adopted on December 10, 1948. Its full text can be found at http://www.un.org/en/documents/udhr.