U.S. REPRESENTATIVE • 4TH CONGRESSIONAL DISTRICT • OREGON

PETER DEFAZIO

REPORTS

Congress of the United States
House of Representatives

January 2002

Dear Friend:

For far too long, Congress has delayed serious debate about the future of Social Security—a program that provides a lifeline not only to countless senior citizens, but to millions of families and children (see article below).

There's no immediate crisis, but we've known for years, with the retirement of the Baby Boomers and changes in society, that Social Security faces demographic and financial challenges. According to current projections, after 2038, Social Security will only be able to honor 70 percent of its commitment to beneficiaries. The sooner we address this shortfall, the less-drastic steps we will have to take to fix the problem (p. 2).

In May 2001, President Bush hand-picked a commission to make recommendations to preserve Social Security for tomorrow's seniors and future generations. The President laid out criteria for the commission—their Social Security plans must: keep benefits intact, use the Social Security surplus only for the program, not increase taxes, not allow the government to invest funds in the stock market, preserve disability and survivor benefits, and privatize Social Security. However, it's impossible to reach all these objectives in one plan (p 3).

On December 11, the President's commission on privatizing Social Security released three plans. Each fell short of the goals set by the President, and none of them ensured the long-term solvency of Social Security. Their plans would require some combination of huge transfers from the general fund which would result in major deficits, accelerating the insolvency date of Social Security, raising the retirement age, and cutting future retirees' benefits (p. 3).

I introduced a bill that preserves Social Security for future generations, cuts taxes for 95 percent of wage-earning Americans, increases benefits for those most in need, and keeps the program intact. (For details of my plan see p. 2, and comparison of plans see p. 4.) Please join me at one of my town hall meetings to discuss the future of Social Security (p. 4).

Sincerely,

P.S. --Again, as I mentioned in my last newsletter, mail service to my DC office has not returned to normal since the discovery of an anthrax-tainted letter in Senator Tom Daschle's office. Please continue to correspond through e-mail, fax or my toll-free phone number (1-800-944-9603) to share your views and opinions, or for assistance with a federal agency. Your thoughts and concerns are important to me.

Why Everyone Should Care About Social Security

In 1935, President Franklin Roosevelt signed into law legislation that established the most popular and effective anti-poverty program the federal government has ever created--Social Security.

Before Social Security was approved by Congress, more than half of America's elderly citizens lived in pove rty. Thanks to Social Security, fewer than 11 percent of today's seniors fall below the poverty line.

Only about one-third of all retirees receive private pensions. Social Security is the sole source of income for nearly 20 percent of seniors. However, it is **much more than a program to protect retirees**.

Social Security is a family protection plan that provides life and disability insurance for American workers and their families. Today, Social Security delivers monthly benefits to more than 44 million people, including: 31 million retired workers and dependents, 6 million disabled workers and dependents, and 7 million survivors of workers who have died, including 4 million children.

The disability and life insurance benefits Social Security provides are **important to young workers** who haven't had enough time in the workforce to accumulate sufficient private savings to provide for themselves and their families if they die or become disabled.

Of the 44 million Social Security beneficiaries, 6 million are disabled workers. A 20-year-old worker has a 3-in-10 chance of becoming disabled, and a 1-in-5 chance of dying before reaching retirement. Social Security benefits replace up to 65 percent of the earnings of a 25-year-old average-wage worker with a very young child if he or she becomes disabled, and replaces up to 80 percent of the earnings of a worker who dies leaving two young children and a spouse.

Photo Credit: Library of Congress

In 1935, President Franklin Roosevelt signed Social Security into law. Today, the program is facing financial challenges.

Social Security is the mainstay of retirement income for women. More than half of all women 65 or older are widowed, divorced or never married, and rely on Social Security for 71 percent of their income, compared with 64 percent for men. Only 27 percent of the people who get pensions are women, 47 percent are men, and one out of four women relies on Social Security for all her income.

Retired workers and their families rely on Social Security for most of their income. Average middle-income older Americans receive 66 percent of their retirement income from Social Security, only 15 percent from private pensions, and just 10 percent from savings.

Debunking Social Security Myths

Demographic changes (a growing number of retirees, proportionately fewer workers, and longer life-expectancy) create manageable challenges for Social Security. **The program is fundamentally sound and can remain so for the next 75 years and beyond with only a few changes.**

Currently, Social Security is collecting more in payroll taxes than is needed to fund benefits for today's recipients (70 cents of every dollar in payroll taxes collected is paid out immediately to current beneficiaries). These excess payroll taxes are credited to the Social Security Trust Fund and then invested in government bonds that pay interest to the Trust Fund. The Trust Fund already has assets of more than $1 trillion, which will grow to around $6.5 trillion by 2024.

Some critics of Social Security have claimed that the bonds held by the Trust Fund are "worthless IOUs." But like a bank, the money you contribute to Social Security is not stacked up and locked away until you retire; the money is used by the government to pay current beneficiaries, fund other government programs, or pay down debt. Yet, no matter what the surplus has been used for, the Social Security Trust Funds have always received a U.S. Treasury Bond in return. U.S. Treasury bonds are the safest investment in the world. In fact, the bonds held by Social Security state, **"The bond is incontestable in the hands of the Federal Old-Age and Survivors Insurance Trust Fund. The bond is supported by the full faith and credit of the United States, and the United States is pledged to the payment of the bond with respect to both principal and interest."**

That said, as the Social Security system redeems these bonds over the next several decades, the government has to find the money to honor this debt. There are a number of ways to do this. For example, the current Social Security surpluses could be dedicated to paying off our national debt, thus saving billions of dollars a year in interest that could then be devoted to Social Security. Another option is to collectively invest a portion of the Trust Fund in equities other than federal debt in order to increase the rate of return to the Trust Fund. I have introduced legislation to allow this sort of investment (see article below for details).

All these numbers can get confusing. But, the bottom line is that payroll taxes, in combination with the Trust Fund, are sufficient to pay 100 percent of promised benefits through at least 2038—nearly four decades from now. Even after 2038, Social Security will never be "bankrupt" in the sense that it couldn't pay any benefits whatsoever. If Congress sat on its hands and made no changes to Social Security, the program would still be able to pay at least 70 percent of promised benefits after 2038.

Even that "deficit" is highly speculative since it is very sensitive to underlying economic and demographic assumptions. For example, a slightly higher rate of economic growth or modest changes in assumptions about wages or life expectancy can shrink the deficit significantly. The deficit in Social Security assumes a future economic growth rate of a dismal 1.5 percent. If economic growth is actually just one percent higher, half of the deficit disappears.

Key Dates

2016

Payroll taxes coming into Social Security will be insufficient to cover all promised benefits. The SSA will begin to draw on the interest earned by the Social Security Trust Fund to help pay full benefits.

2025

Incoming payroll taxes plus interest income from the Trust Fund will be insufficient to pay all benefits. The SSA will begin redeeming bonds in the Trust Fund to cover full benefits.

2038

All the bonds in the trust fund will be redeemed. Even after 2038, however, payroll taxes coming into Social Security will still be able to cover around 70 percent of promised benefits.

A Secure Social Security Plan For All Americans

Rep. DeFazio talks with seniors about Social Security and other important issues during a recent visit to Douglas County.

The privatization commission alleges that Social Security will go bankrupt in 2016. They assume that the federal government will not, as required by law, put its full faith and credit behind the Trust Fund, or continue to pay interest on those funds. That's simply not true. The commission makes these false claims in order to generate support for their own privatization proposals, despite their shortcomings (see p. 3).

According to the Social Security Trustees 2001 Report, Social Security is financially sound until 2038. After that date, revenues generated by payroll taxes - called the Federal Insurance Contribution Act (FICA) taxes - will cover only around 70 percent of promised benefits.

With relatively minor changes we can forge a secure retirement program for Americans of all ages, while boosting the economic health and productivity of our nation.

I have offered legislation that the Social Security actuaries have certified will cover 100 percent of benefits for the entire 75-year planning period.

Unlike the many privatization plans, my legislation does not decrease COLAs, increase the retirement age, accelerate insolvency, drain the general fund, or cut benefits. My bill provides additional benefits for those over age 85 and protects benefits for stay-at-home parents.

As a bonus, my plan would actually cut Social Security payroll taxes for the majority of American workers, by exempting the first $4,000 in wages from the FICA payroll tax.

The plan would be funded in part, by lifting the cap on earnings subject to the payroll tax. Currently, all wages are subject to the Medicare payroll tax, but income above $84,900 is not subject to the Social Security tax. Workers earning less than $84,900 pay Social Security payroll taxes on all their income, but those making more than $84,900 do not.

My plan merely makes the payroll tax burden more equitable by raising the wage cap and treating wages the same for Social Security as for Medicare. This change would only impact the top five percent of wage-earning Americans, and would actually reduce the tax burden for those who earn less than $88,900. So, the average Oregonian who earns $30,872 a year, would receive a tax cut under my plan.

My plan, "The Social Security Stabilization and Enhancement Act," HR 3315, also allows the Social Security Trustees to collectively invest a portion of the Trust Fund surpluses in equities to increase returns.

HR 3315 is an alternative to privatization plans that divert resources from the Trust Fund into private accounts—which would double the program's financing shortfall. My plan:

- Exempts the first $4,000 in wages from the Social Security payroll tax, and lifts the wage cap, so anyone who earns less than $88,900 will see a reduction in FICA taxes.
- Increases benefits for those currently age 85 and over. Americans over 85 are mostly women and widowed, and often outlive their savings.
- Allows a portion of the Social Security Trust Fund to be collectively invested in equities (stocks, corporate bonds etc.) by a private board, similar to the Oregon Public Employees Retirement System (PERS).
- Fully protects disability benefits.
- Increases the years of earnings used to compute benefits from the 35 highest years to the 38 highest years of earnings (to adjust for the longer working lives of Americans). However, it gives individuals three years to stay home to care for children without being harmed by the change.

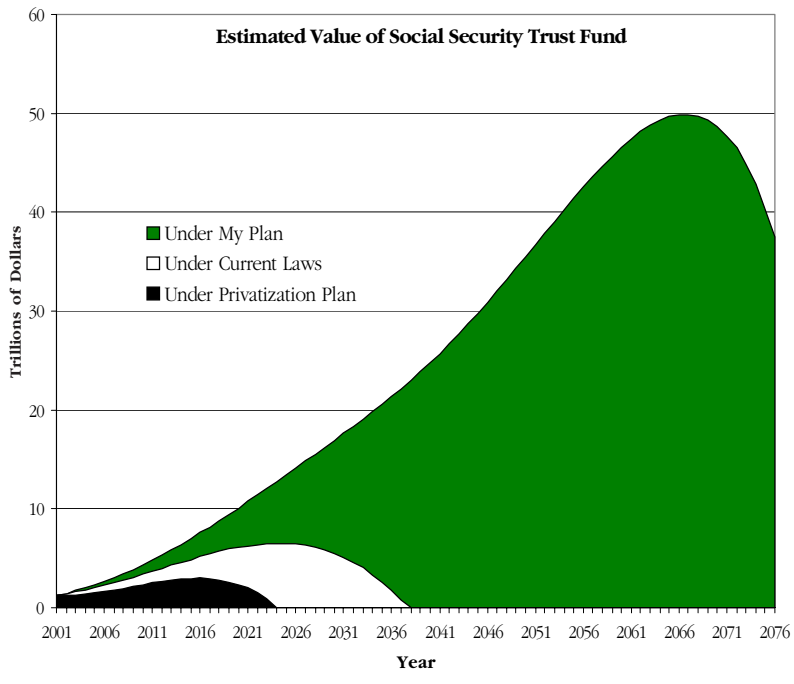
Pitfalls of Privatization

Transition Costs

Because the vast majority of payroll taxes that come into the system go out immediately to pay benefits, diverting two percent of payroll taxes into private accounts creates a huge gap in financing of $1 trillion over the next ten years, and $3 trillion over the next twenty.

The President's commission recommended a mix of benefit cuts and general revenue transfers in order to fill the financing gap. Unfortunately, transferring general revenue could require a return to budget deficits since currently, the non-Social Security surplus has disappeared. The only other option is raising taxes, which would result in double-taxing young people: once to fund current benefits and again to fund their individual accounts.

Further, diverting payroll tax revenue to private accounts actually accelerates the financial challenges facing Social Security. Currently, Social Security can pay 100 percent of benefits through at least 2038. Under the commission's privatization plans, benefits could be paid only through 2024—14 years sooner (see graph).



Benefit Cuts

The commission actually recommends benefit cuts in order to pay for some of its privatization proposals. Privatization proponents have suggested raising the retirement age, cutting already dismal cost-of-living adjustments, and tying benefits to changes in the consumer price index, rather than the wage index (while complicated, this essentially means that the standard-of-living for beneficiaries would decrease with each generation since prices tend to rise slower than wages).

Numerous studies have placed the necessary benefit cuts in Social Security due to privatization at 40-54 percent. While an individual's private account could offset some of these devastating cuts, experts believe the total benefit cut would still be at least 20-40 percent. Under the plans proposed by the President's privatization commission, benefit cuts would apply not just to retiree benefits, but also to survivor's and disability benefits.

Rates-of-Return

In order to make privatized individual accounts sound attractive, privatization proponents assume very high rates of return from an individual's investment in the stock market. But at the same time, in order to claim a crisis in Social Security, they create a false sense of alarm by assuming that future economic growth will be slow. They can't have it both ways. In dealing with people's economic security and retirement, everyone would be better served to use consistent, conservative economic estimates.

Similarly, proponents have not even been able to show how the stock market would be able to yield seven percent returns in the future when economic growth is projected to be only around half of what it's been in the past. Many analysts predict that the stock market is likely to provide only a 3.5 percent rate-of-return in the future, given projected economic growth rates.

Privatizaton proponents also downplay the risk of investing in stocks. While the market has a general upward trend, there were fifteen years in the past century in which the value of the stock market fell by more than 40 percent over the preceding decade. **If a worker, dependent on an individual account, retired during a downturn they would see a substanial reduction in their retirement earnings.** Investing the Trust Fund collectively, as I've proposed, would limit the risk for individuals and offers the ability to weather a market down-turn.

It is also important to keep in mind that the rate-of-return argument is essentially irrelevant to a social insurance program like Social Security. You don't complain if your rate of return on your fire insurance policy is zero, because that means your house didn't burn down. Social Security is an insurance program, not an investment program. It provides the equivalent of $300,000 in life insurance and $200,000 in disability insurance, in addition to a retirement benefit, to every family to protect men, women, and children against the death or disability of the primary wage earner.

Administrative Costs

Administrative costs would further reduce the meager return from private accounts. Administrative costs for Social Security are currently less than one percent of total expenditures. By contrast, under a privatized system, individuals would likely lose at least 20 percent of their benefits to administrative costs. Administrative costs in the partially privatized system in Britain have reduced the account of the typical worker by 36 percent.

Test Your Social Security Knowledge

1. What are the current administrative costs of Social Security?

A. 25%

B. 15%

C. less than 1%

2. How much would administrative costs reduce earnings in privatized individual accounts?

A. 15-20%

B. 1-5%

C. 45-55%

3. What percentage of Social Security beneficiaries in Oregon receive survivors or disability benefits (i.e. non-retiree benefits)?

A. 33%

B. 10%

C. 5%

4. What is the percentage of elderly Oregonians lifted from poverty by Social Security?

A. 10%

B. 40%

C. 25%

5. If two percent of the payroll tax is diverted to privatized accounts, what percentage would have to be cut from traditional Social Security benefits?

A. 10%

B. 25%

C. 40%

6. What percentage of Social Security beneficiaries have income below $20,000 a year?

A. 10%

B. 79%

C. 46%

Answers: 1. **C**, 2. **A**, 3. **A**, 4. **B**, 5. **C**, 6. **C**

At A Glance: Social Security Reform Plans

Criteria For Stabilizing Social Security	DeFazio Social Security Reform Plan	Presidential Commission Privatization Plan
Guarantees 100 percent of promised benefits for the entire 75-year planning period	☑	☐
Extends solvency for the Trust Fund for the next 75 years	☑	☐
Provides a payroll tax cut for all those earning less than $88,900	☑	☐
Makes payroll tax burden more fair for working Americans	☑	☐
Provides potential for increased rates of return, and investments in diversified equities.	☑	☑
Fully protects promised benefits for survivor and disability recipients	☑	☐
Boosts benefits for the most vulnerable seniors	☑	☐
Increases the rate of return received by Social Security in a way that minimizes adminstrative costs and individual risk	☑	☐
Requires an increase in the national debt or transfers money from other federal programs in order to address financing shortfall	☐	☑

Social Security Town Hall Schedule

Albany
Tuesday, Feb. 19
5:00 - 6:00 pm
City Council Chambers
333 Broadalbin SW

Brookings
Monday, March 18
9:00 - 10:00 am
Chetco Public Library
405 Alder

Cottage Grove
Monday, Feb. 25
9:30 - 10:30 am
Council Chambers, City Hall
400 East Main

Eugene
Monday, Feb. 25
12:00 - 1:00 pm
Campbell Senior Center
155 High

Eugene
Monday, March 11
7:15 - 8:15 pm
Harris Hall
125 East 8th

Florence
Monday, March 11
3:00 - 4:00 pm
Florence Events Center
715 Quince

Lakeside
Monday, March 18
2:00 - 3:00 pm
City Hall
915 North Lake

North Bend
Friday, March 15
12:00 - 1:00 pm
City Hall
835 California

Philomath
Tuesday, Feb. 19
10:30 - 11:30 am
City Council Chambers
980 Applegate

Port Orford
Friday, March 15
3:00 - 4:00 pm
City Hall
555 West 20th

Reedsport
Monday, March 18
4:30 - 5:30 pm
Conference Center, Umpqua Discovery Ctr.
409 Riverfront

Roseburg
Monday, Feb. 11
4:00 - 5:00 pm
Ford Community Room
Douglas County Library
1409 NE Diamond Lake

Springfield
Monday, Feb. 25
4:00 - 5:00 pm
Willamalane Senior Ctr.
215 West C

Springfield
Monday, Feb. 25
6:00 - 7:00 pm
Council Meeting Room
City Hall
225 5th

Veneta
Monday, March 11
5:30 - 6:30 pm
City Hall
88184 8th

Mark Your Calendar, and Please Join Me at One of My Town Hall Meetings.

NOTE: *Persons requiring special accomodations should contact Janice Kelly at 1-800-944-9603 at least 48 hrs. prior to the event.*

Congressman Peter DeFazio wants to hear from you.

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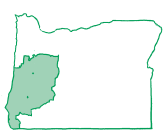

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