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A PROGRAM FOR RESEARCH ON

## **SOCIAL AND ECONOMIC DIMENSIONS OF AN AGING POPULATION**

**2½ Proposals to Save Social Security**

**Deborah Fretz and Michael R. Veall**

**SEDAP Research Paper No. 35**

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## 2 ½ Proposals to Save Social Security\*

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**Abstract:** This is a review article of three books that deal with the problems facing the U.S. Social Security system. One deals with the OASDI (Old-Age, Survivors and Disability Insurance) financial shortfall and proposes an alternative plan with both a tier one benefit and a tier two provision based on personal saving accounts. A second considers the social insurance system more comprehensively, arguing for a grand reform which would include new programs, particularly in the areas of child care and housing. A third largely confines itself to arguing against those who wish to change the OASDI plan because of the financial projections, although it also argues for a more comprehensive health care insurance system. The review concludes that key differences expressed in the books, particularly between the first and third, rest on different value judgments regarding intergenerational equity and the role of government.

\* This is a review article of three books on the United States social security system: *The Real Deal: The History and Future of Social Security*, by Sylvester J. Schieber and John B. Shoven. New Haven: Yale University Press, 1999. Pp. xix, 450; *True Security: Rethinking American Social Insurance* by Michael J. Graetz and Jerry L. Mashaw. New Haven: Yale University Press, 1999 and *Social Security: The Phony Crisis* by Dean Baker and Mark Weisbrot. Chicago: University of Chicago Press, 1999. Pp. xi, 175. A version will appear in the January 2001 issue of the *Southern Economic Journal*. We thank Byron Spencer and an anonymous referee for helpful comments and acknowledge the support of the Social Sciences and Humanities Research Council of Canada to the research program on the Social and Economic Dimensions of an Aging Population (SEDAP).

## 1. Introduction

A number of countries have recently reformed their plans for retirement support. Chile famously has adopted compulsory individual retirement accounts, Australia has moved to a kind of compulsory 401(k) superannuation plan, Switzerland to a system of compulsory occupational pensions and Sweden to a system of compulsory notional accounts, where individual contributions are recorded by the government and accumulate as individual entitlements that do not correspond to private sector investments. Canada, facing a projected Canada Pension Plan shortfall, adopted the perhaps predictable approach of simply raising payroll taxes, yet even here there was significant change with a plan for direct investment by the pension authority in the stock market that has not yet been broadly controversial. Interesting attempts (e.g. Robson, 1996) to advance Chilean-type solutions for Canada did not find much political traction.

But in the United States, the trustees of the major public pension plan, Old-Age and Survivors Insurance and Disability Insurance (OASDI), have been forecasting for about 15 years (essentially since immediately after the implementation of the last reforms designed to “save” Social Security) that the plan as structured could not meet its obligations through a 75 year forecast window. But there has been no legislative correction. There certainly have been a number of proposals: indeed the 1994-1996 Advisory Council on Social Security came up with three. Here we review a newer proposal presented in book form: *The Real Deal: The History and Future of Social Security* by Sylvester J. Schieber and John B. Shoven. We also review a second book *True Security: Rethinking American Social Insurance* by Michael J. Graetz and Jerry L. Mashaw. This book is also about “saving social security”, but the problem

is thought of as not so much about OASDI financial projections but instead (p.5) “that the long-term political support for social insurance could come unglued” unless the effectiveness of current social insurance, broadly defined, is improved. Finally, a third book, *Social Security: The Phony Crisis* by Dean Baker and Mark Weisbrot, focuses on discussions of OASDI solvency (although it discusses aspects of health insurance as well) but argues that current action to restructure OASDI is *not* required to “save” it. Hence we have counted this in our title as only one-half a proposal: no pejorative connotation is intended.

We begin in Section 2 with a brief annotated outline of each of the three books. We put most of our emphasis on OASDI issues, as do Schieber-Shoven and Baker-Weisbrot; as noted Graetz-Mashaw covers a very wide range of social insurance programs. In Section 3 we make some more general observations. A central point is the reminder that a positive economics approach cannot choose among these or any proposals: to a large extent these proposals are different simply because their authors have different values. Section 4 concludes.

## **2. Overviews**

### *The Real Deal: Schieber and Shoven*

This is a substantial and worthwhile book. Schieber and Shoven have devoted several chapters to a history of United States Social Security from its inception. They then discuss current problems in depth, provide a discussion of a number of recent reform proposals and give a significant proposal of their own.

According to their history, right from the beginning the central issue facing OASDI was to fund or not to fund, that is, whether there would be a fund to cover the public pension

promises being made to current workers (and hence a long delay before any significant benefits would be paid) or whether instead there would be a reliance on subsequent generations to cover the promises in the future (and hence transfers could begin relatively quickly). The initial plan signed into law by Roosevelt in 1935 was a funded one. But by the 1939 amendments, this was changed to a largely unfunded plan by a coalition of liberals who wanted to alleviate current poverty among the elderly and conservatives who argued that the accumulation of a trust fund would lead to untoward government intervention in the economy through “social investment”. The authors note (p. 92) that a strong case can be made that the way benefits were introduced led to a program much larger than a simple universal pension paid from general revenues. Hence not only did the first beneficiary, Ida May Fuller, receive a grand total of \$22,000 in lifetime benefits, but the genesis of the plan probably contributed to the illusion that this was somehow a financial return commensurate with the \$25 in payroll taxes paid by her and her employer. It is not surprising that Social Security was a popular program.

Schieber and Shoven describe the further benefit expansions through the 50s, 60s and 70s, the most famous example being the great overindexing error that was part of the 1972 amendments that first pushed the system into a shortfall not fully eliminated by the 1977 and 1983 retrenchments. They further point out that the current problem was predicted by the proponents of funding when the program was initiated in the 1930s: eventually there would be losers. It has happened. The last cohort for whom the pension plan was a good financial deal (in the sense that the contributions “earned” a return in excess of the government bond rate) has now retired; essentially all current cohorts of workers will do worse.

The historical discussion (which includes analysis of recent policy proposals) builds toward the single chapter in which they describe their own proposed plan, centered on “personal security accounts” and called PSA 2000. The most immediate target of the plan is the Year 2037 problem<sup>1</sup>: sometime around that year OASDI cannot meet all its obligations and will require the equivalent of a 30 percent increase in payroll taxes to do so. As do almost all the proposals on the table, Schieber and Shoven wish to forestall that event by current action: indeed their plan would postpone it indefinitely. The most important provisions of their PSA 2000 plan are (1) leaving the OASDI employer/employee payroll tax unchanged at 12.4 percent of earnings up to the current real annual ceiling of \$72,600 (2) requiring workers to contribute an additional 2.5 percent of payroll to private investment vehicles called personal security accounts (PSAs) that they could not draw upon until retirement, with at least of half of that withdrawal necessarily through inflation-indexed life annuities (3) matching the workers’ contributions dollar for dollar using part of the 12.4 percent payroll tax, the remaining 9.9 percent being used to meet current promises and fund a flat rate tier one benefit paid to all full career workers of \$500 per month, indexed to average wages (4) moving to a retirement age of 67 at a faster rate than currently legislated, with the retirement age thereafter indexed to life expectancy and with a similar advancement of the early retirement age (5) removing the earnings test for beneficiaries at normal retirement age (6) maintaining some tier one spousal and widow benefits, and (7) having a long smooth phase-in until roughly 2045, during which benefits would be calculated as appropriate averages with those of the current system and all remaining state and local employees would be brought into the plan.

The plan is reasonably but not fully detailed; the book does not reference a source for the

full plan. Both the analysis of the plan and the description of the methodology of the analysis are not especially detailed. In terms of solvency analysis, Schieber and Shoven somewhat loosely (but in our view credibly) assert that their calculations show that under their plan taxes would stay unchanged “for several decades” and then “in the distant future” could be reduced after transition costs had been paid. This is rather refreshing compared to plans which do not ensure solvency but simply postpone the problem to a point outside the 75 year window.

They also conduct two more formal analyses. First, they compare future projected benefits under their plan to the existing plan. The lower limit of the 80 per cent confidence interval of the year 2045 PSA 2000 benefit (which is uncertain because of the uncertain financial returns to the personal security accounts) is just above the benefit projection for the existing plan, with the important exception that PSA 2000 will provide significantly larger benefits for those with low monthly earnings because of the indexed tier one benefit. For example, eyeballing their Figure 23.2 suggests that in 2045, for those with average indexed monthly earnings of \$3000 (year 2000 dollars), under PSA 2000 the estimated lower bound of the 80 per cent confidence band is \$1400 per month benefit (year 2000 dollars), about the same as the projected existing benefit. But the estimated expected value of the benefit in 2045 is over \$2000 (year 2000 dollars) per month. The differences between the lower bound of the confidence interval and the expected value are larger for larger incomes.

A second analysis uses historical financial returns (back to 1858!) to compare their plan to the plan produced by Robert Ball for the 1994-1996 Advisory Council on Social Security. Under assumptions that are not detailed but nonetheless seem reasonable, they pretend that both plans had been in place historically and then use the historical record of financial returns



to compare the benefits received by a low-wage worker. According to their analysis, in the twentieth century the worker would almost always have done better with PSA 2000, sometimes substantially better.

Particularly the first exercise demonstrates that there is still risk to retirees under PSA 2000 (i.e. there is an estimated one chance in 10 that the actual outcome will be below the 80 per cent confidence bounds). A central theme in the Schieber-Shoven argument is that some sort of risk (the political risk of benefit reductions, the risk of lack of wage growth in the economy etc.) is inevitable. They write (p. 307) that, “You can’t offer ‘safe’ benefits funded by risky revenue sources without running into one financial crisis after another”. Later (p. 379) they note that their preference for individual accounts is “based on a belief that the young should be given a choice regarding the risks they assume”.

A final mode of analysis is the comparison of their PSA 2000 to a set of principles they postulate for a redesign. Their principles (p. 387) have some tension (between “progressivity” and “increasing the link between contributions and benefits” for example) but provide an informal but reasonable scorecard. Perhaps worthy of special note is the principle that disability and early-survivor parts of OASDI be preserved (they argue that their plan provides enough resources to do this) and that equity between one- and two-earner couples needs to be increased (which means a one-earner moderate or high income household would have much lower benefits under PSA 2000 because the spousal benefit applies only to the tier-one benefit).

It seems to us that the plan is a well-crafted one, in the sense that there are no important holes<sup>2</sup> and the numbers seem plausible. Considering two other options for solving the same

Year 2037 problem, the proposal of Feldstein and Samwick (1998) suggests putting 2 percent into PSAs (perhaps funded using federal government budget surpluses) and gradually phasing out the existing plan's pension component while a "naive" proposal (apparently so naive that no one actually proposes it, even though that is more-or-less what happened in Canada) is to keep the existing plan and raise payroll taxes now by a bit less than 2 percent. Schieber-Shoven is something of a cross between the two plans: unlike Feldstein-Samwick it provides a long-term tier one benefit (and the payroll tax to sustain it) and through that approach preserves some of the defined benefit features of the current plan including strong redistributive aspects. Unlike the naive proposal, it establishes personal savings accounts and keeps the system solvent not only until 2075 but beyond, with the likely prospect of a declining payroll tax. In terms of intergenerational winners and losers, the current working generation is a material loser: we will discuss this aspect more fully in Section 3.

*True Security: Graetz and Mashaw*

This is an ambitious book. Graetz and Mashaw undertake a comprehensive discussion of all social insurance programs, not just the ones that are perceived to be in trouble and not just the ones that are commonly thought of as social insurance (so that for example there is a discussion of housing policy including the mortgage interest deduction). They write (p. 6) about the lack of a "national conversation about social security as a whole" and attempt to fill this gap. As mentioned, their book is about saving social security through improving its political support, in turn by making overall social insurance more effective.

This ambition is both the book's strength and its weakness, at least for an economist

readership. Because all these plans fit together, there are gains from considering a number of programs simultaneously: for example the problems of disability, unemployment and retirement have important interconnections. But while a longer book would have compromised readability, as it stands the interesting ideas in the book are not detailed well enough or costed well enough. For example, in considering a proposal of adding long-term health care for seniors to Social Security, the authors note (p. 276) it could “be financed by a very small addition to payroll taxes, no more than 0.5 percent”. On the next page they describe this addition to payroll taxes as “almost invisible”. But \$20 billion per year here, \$20 billion per year there and pretty soon you are talking real money. Schieber and Shoven chronicle (Chapter 17) attempts within the 1994-96 advisory council to eliminate the Social Security shortfall by saving and cumulating “slivers” as small as 0.1 percent of annual covered payroll.

We have put a selection of some of the more important Graetz-Mashaw recommendations that do not pertain to OASDI in Table 1. There are several themes to the Graetz and Mashaw reforms. First, they argue that a simple income-based program such as the negative income tax is an inadequate social insurance program because it cannot deal with the complexities of health care problems, disability, families in housing markets with varying costs and so forth. Their proposals would expand government programs, particularly in the areas of child care and housing. Second, they consistently argue for either federal programs or stronger federal intervention to prevent “the race to the bottom” as states try to keep payroll costs low to attract new investment. Third, they tend to support compulsory participation. Fourth, they pay attention to desirable incentives (e.g. to find a job, economize on housing expenditure) which while sometimes dampened are never eliminated. Finally, they pay for

many of their programs by eliminating personal income tax measures that often tend to benefit a different group, so for example their proposed 30 percent subsidy (up to limits) for housing for families with children would be paid for by reducing (probably eliminating) mortgage and property tax personal income tax deductibility. There would be a shift of benefits from those without children to those with children, from higher income households to lower income households and from those with mortgages to those without mortgages. Some of these aspects may affect the political prospects for their proposals.

With respect to the OASDI retirement component, Graetz and Mashaw support the continuation of current retirement benefits. They also support supplementary, mandatory personal saving accounts which would also be drawn upon in times of unemployment (see Table 1). In terms of the Year 2037 fiscal problem, they propose measures roughly similar to the Schieber and Shoven plans to move toward compulsory participation by all state and local employees and accelerate the increases in the normal retirement age. It appears that they believe much of the remaining shortfall will be solved by “correcting” the pension inflation adjustment which is based upon the Consumer Price Index (which the Boskin Commission has argued may overstate inflation by as much as 1.1 percentage points per year) and perhaps by finding higher private sector rates of return for the OASDI trust fund. They also emphasize reforming health care for seniors, with reforms along the lines they propose for the general population (see Table 1).

The analysis of Graetz and Mashaw is largely informal. While labor market incentives are mentioned, they do not draw upon the relevant empirical literature to put sizes on the various effects so that tradeoffs are not analyzed empirically. Distributional analysis also is

largely informal. As noted, costing is “back-of-the envelope”, although the resulting simplicity provides some clarity. Again the comprehensiveness in terms of number of programs considered leads to a lack of depth. As this book is really a political proposal, much of this should be excused. But political proposals for economic reforms must have an optimal size. Schieber and Shoven present a proposal that one can imagine being enacted through a single piece of legislation. The Graetz and Mashaw proposal is a map for many pieces of legislation by many different governments. To us, it seems unwieldy.

*The Phony Crisis: Baker and Weisbrot*

In this engaging and lively book, Baker and Weisbrot argue that there is no Social Security (OASDI) problem at all. In terms of the Year 2037 problem, they argue that the trustees’ intermediate economic growth assumptions may be too pessimistic: if economic growth is assumed to be 3 percent, as it has averaged over the last 75 years, rather than the less than 2 percent which is more representative of medium-term growth, there is no shortfall. (Along these lines, the recent burst of U.S. growth has been pushing back the estimated year of reckoning, from 2029 just three years ago to the current 2037, illustrating how sensitive these forecasts can be to economic performance.)

Second, they argue that even if the trustees’ intermediate estimate is correct, the United States will be a richer country in the 2030s and the required increase in the payroll tax to save OASDI (from 12.4 percent of payroll to say 16 percent) will be easier to bear than the smaller increase required today. Of course Medicare-associated payroll taxes will also increase and Baker-Weisbrot accept this is a problem. Indeed they argue that unchecked medical cost

inflation is potentially such a big problem both within and outside Medicare that it threatens to consume the entire economy. As a solution they promote universal public health care of the type provided in most other major industrialized countries. (They note that all of these have far lower aggregate health care expenditures per capita than the United States yet have no uninsured and attain comparable or better aggregate health care outcomes.)

In terms of current OASDI policy, they argue strongly against any cut in benefits including any possible CPI adjustment (as their view is that the Boskin commission was biased toward finding the CPI overestimates inflation by not considering reasons why the CPI might underestimate inflation) or extending the normal retirement age. The authors argue that the latter will have a disproportionate burden on black workers because of shorter life expectancies although we wonder how this can be assessed without comparing it to the alternative. For example, it would be conceivable that some groups of low-life-expectancy workers would choose increasing the retirement age over the alternative of increasing the tax rate (and forcing these workers to contribute more to what is already a bad deal for them).<sup>3</sup> They also reject increasing the number of years used in calculating average indexed monthly earnings (AIME) from 35 to 38, noting that this change would relatively disadvantage the poor because benefits are a nonlinear, progressive function of AIME. They only devote a single paragraph to balancing the current Social Security accounts over the 75 year forecast window if it was deemed to be necessary; their suggestions boil down to using general revenues and increasing the annual cap on earnings. Both changes are of course tax increases that would affect higher income participants more than a straight payroll tax increase.

In making their overall arguments, the authors (1) challenge generational accounting

calculations that show large increases in the percentage tax burden on future generations, (2) oppose the view that real stock market returns will continue at such high rates (part of the attraction to those who favor personal savings accounts) and (3) take what we think of as extreme positions that both the crowding out of physical capital formation by government borrowing and the link between saving and long-run growth are small. We cannot confirm every number they use (partly because of the occasional slip in updating the values that changed between the 1998 and 1999 trustees' report: a single basic table of numbers would have been useful) and there are other quibbles, but these are small shortcomings because they do not diminish the main thrust of the argument. There will be disagreement, but it is our view that the nature of the disagreement helps isolate the real issues underlying all these books and indeed all the proposals to change Social Security. We turn to these in the next section.

### **3. The Inability to Rank Proposals**

In this section we will consider the policy proposals in these books in very broad terms. We will make our points by focusing on Social Security retirement pensions (accepting that the Graetz -Mashaw book is much wider in scope and that the Medicare financing issue is at least as important a financing issue<sup>4</sup>). We will concentrate on two broad issues: first, *whether* to fund Social Security (the intergenerational issue) and second, if it is decided to fund, *how* to fund Social Security (public vs. private approaches).

#### *Whether to fund Social Security: intergenerational issues*

All three of these books give weight to within-generation distributional issues, although

of course there is no value-free way of choosing between different degrees of redistribution. But when we start thinking in terms of intergenerational redistribution, matters become even more difficult. Many proposals (including Schieber-Shoven) make at least some of the current generation materially worse off (by making it pay twice, both for the support of the previous generation and for some or all of its own public retirement support) in return for improving the material welfare of the next generation. The underlying view of “intergenerational equity” seems to be that the next generation should pay no higher a rate of payroll tax than the current generation pays. But note this maxim is much different from the oft-expressed ethic that this generation should leave to the next an “inheritance” as least as large as the one it received: as Baker and Weisbrot point out, the next generation will likely “inherit” a much higher standard of living than our own even if the payroll tax is higher (so that even if the after-payroll-tax *percentage* of their wage is smaller, the *absolute* amount is expected to be much larger). Note also that even if it is accepted that all parents have the common value that they wish to leave a better life for their children, this implies little for public finance, because parents can best accomplish that objective through investing in their children’s human capital and through gifts and personal bequests.

Looked at this way, the recommendations of Schieber-Shoven and Graetz-Mashaw simply reflect different values than those of Baker-Weisbrot. The first two proposals would tend to benefit future generations at the expense of those who will retire over the next thirty years (and the currently retired, if the index formula is changed as Graetz-Mashaw would allow). Baker-Weisbrot would prevent these changes and hence preserve the position of the current generation of workers and retirees.<sup>5,6</sup>



But all this assumes an ongoing system with full Social Security payments will be maintained regardless of current funding decisions. What might change to endanger the continuation of this entitlement? The only candidate factor seems to be the increased program cost from demographic change but the increase in the senior proportion of the population will also make it harder to effect political change that hurts seniors.

*How to fund: public versus private*

Suppose it is accepted (and it is not obvious to us that it will be) that current funding should be increased. The most immediate issue will be whether this simply will involve increased payroll taxes or whether the funding will be implicitly accomplished through private savings accounts as in Schieber-Shoven and as strongly opposed by Baker-Weisbrot. There are objective differences to resolve here, for example regarding the cost of administering private saving accounts. In addition, all three books express worries that politics might affect the way the government would manage a portfolio of private securities (and presumably that the composition of the government portfolio could in turn influence government policies). But perhaps the most contentious issue is whether private securities will earn higher long-run rates of return than government bonds. History seems to suggest this and many run their personal finances under this assumption. Yet the Baker-Weisbrot argument that such rates of return are unsustainable seems to us to have merit<sup>7</sup>. Moreover, if private returns are so superior, the implications seem to be broader. Why should the higher private returns be used only toward Social Security? Should the government for example borrow to purchase a portfolio of private securities, and use the resulting profits to pay off its other obligations, such as its debt?

As all the books point out in one way or another, the second key issue is whether an expanding trust fund will lead the government to expand benefits or increase other types of expenditures (given it is cheap to borrow from the Social Security fund). For that is essentially what determines the impact of Social Security on national saving. Even if it is agreed that Social Security should be “walled off” to prevent such effects, is there “trust” in government to accomplish this? While clearly evidence can be brought to bear on the historical performance of government in situations like this (for example the conversion of what was initially intended to be a funded plan to an unfunded one), can differences between individuals on subjects like this be attributed to different readings of the objective evidence or do they largely reflect differences in values? We cannot be sure but we lean toward the latter view.

#### **4. Conclusions**

The United States Social Security problem is not just the prospect of a shortfall in the year 2037. That is just one aspect of the more general problem that Social Security is no longer a good financial deal for current contributors. (A similar problem faces comparable programs in other countries, including Canada.) The easiest way to make it a better deal would be to dump the current obligations (i.e. stop paying current retirees). But given that is not going to happen (nor would we so advocate), the question is what to do now. One way forward is to try to get a higher return either through investing the trust fund privately or blending in a program of compulsory private saving accounts. Clearly high returns are better than low returns but we note that this is a wider issue: if private returns are really substantially better, the government has an arbitrage opportunity and could pay off all its debt, not just the

Social Security unfunded liability, by borrowing to invest at the private sector rate of return.

Assuming as all these books do that higher private-sector capital returns are not going to solve the problem, at least fully, one view is that the current generation should take it upon itself to fix Social Security as a bequest to future generations. This seems to us to be the position of Schieber and Shoven<sup>8</sup> who argue that current workers should increase their contributions as a percentage of payroll to make it less likely that future workers will have to increase their payroll taxes to sustain the system. This is essentially what happened in Canada, although Canada did not include any compulsory personal savings accounts in its reform. Graetz and Mashaw appear to accept an approach such as Schieber and Shoven's, although they are also prepared to allow an adjustment through indexing which might tend to cut projected benefits. Baker and Weisbrot say no. The difference is one of preferences regarding the amount and composition of the collective legacy of the current generation, noting that some kinds of intergenerational transfers through Social Security might crowd out intragenerational transfers and that there are other ways of increasing intergenerational transfers, say by leaving a better natural environment, a more developed infrastructure or a smaller national debt.

These books are detailed and the differences in views clearly extend to other matters affecting the degree of within-generation distribution, the role of government and the linkage of saving and growth. Do we recommend reading them? Clearly any economist who wants to participate professionally in the U.S. public debate about Social Security or social insurance must read all three. More general economist readers might choose Baker and Weisbrot if they want to read a vigorous argument in defence of the current system or Schieber and Shoven if

they want a proposal for reform with a somewhat calmer tone or are interested in the system history (Chapters 2 to 13). Graetz and Mashaw will give the reader a general idea of the overall state of social insurance in the United States plus provide some concrete proposals which might shape discussions of change.

Most of these books are too lengthy and detailed for a Canadian reader interested primarily in Canadian social security issues. However, as a shorter reading, the introductory chapter of Baker-Weisbrot makes their basic case (Munnell 1997 might also be useful) while Schieber and Shoven Chapter 23 outlines their basic proposal (and hence might be read along with other U.S. proposals such as Kotlikoff and Sachs 1997; Feldstein and Samwick, 1998; as well as the summary of the current OASDI trustees' report at [www.ssa.gov](http://www.ssa.gov)).

Atkinson (1999, p. 187) concludes in his recent lectures on the economic consequences of rolling back the welfare state that policy proposals by economists "...are themselves part of the political process. We have not just endogenous politicians but also endogenous economists, whose behavior has to be explained." We agree, although perhaps our explanation of heterogeneous preferences is not fully satisfying. In any case, from the volleys back and forth between politicians to the serious debate contained in these books, the future of United States Social Security is being determined in a remarkably forward-looking discussion deeply rooted in different approaches to this generation's collective legacy and views about the role of government.

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<b>Program Area</b>	<b>Recommendations</b>	<b>Financing/Remarks</b>
Health Care	<ul style="list-style-type: none"> <li>-Compulsory purchase of catastrophic health insurance to cover all health expenditures (physician, outpatient, hospital, prescription drug) in excess of a given percentage of income, perhaps with copayments and a maximum out-of-pocket</li> <li>- public premium assistance that diminishes with increasing income</li> <li>-providers private but required to take all comers at same (perhaps age-conditioned) price, Medicare initially separate program</li> </ul>	<ul style="list-style-type: none"> <li>-payment by using fees for redundant Medicaid plus removing income tax deductibility of private health insurance</li> <li>-potential open-ended commitment by government to pay excess over catastrophic ceiling may make cost control difficult</li> <li>- difficult to prevent private providers from trying to attract better risks</li> </ul>
Unemployment Insurance	<ul style="list-style-type: none"> <li>-national program with common eligibility and payment rules;</li> <li>- abandon experience-rating by firm, workers face declining benefits</li> <li>-compulsory savings account of 3% of wages, debited for part of unemployment insurance withdrawals</li> <li>-improve coverage of part-time, benefits if worker leaves for child care, pregnancy</li> </ul>	<ul style="list-style-type: none"> <li>-paid for by FICA-like wage tax</li> <li>-large expansion of unemployment benefits on a nationwide basis: difficult to evaluate effects on labour market performance</li> </ul>
Worker Disability	<ul style="list-style-type: none"> <li>-reduced role for workers' compensation</li> <li>-short-term federal disability insurance, with opt-out if employer provides plan and contributes to financing of high-risk public pool</li> <li>-long term disability insurance through existing retirement or subsistence programs</li> </ul>	<ul style="list-style-type: none"> <li>-new short-term disability program financed by wage tax; state programs and much of workers' compensation then unnecessary</li> </ul>
Families with Children	<ul style="list-style-type: none"> <li>-stricter federal controls of current state-run Temporary Assistance for Needy Families programs, food stamps program converted to cash with asset test removed</li> <li>- 30% federal subsidy of the cost of adequate child care or a refundable federal tax credit for those who do not purchase care</li> <li>-30% housing subsidy to families with children up to fair market rent of appropriate size (can be used toward ownership)</li> <li>-other proposals to insure against premature death of parent, require child support</li> </ul>	<ul style="list-style-type: none"> <li>-financing discussion focuses on child care and housing subsidy, mostly provided by ending or reducing tax allowances and direct subsidies (e.g. "restructuring" mortgage interest and property tax deductibility)</li> <li>-housing subsidy only to families with children</li> </ul>

## ENDNOTES

1. The various books use different trustees' reports for projections as to the first year of OASDI shortfall. For clarity, we only will use the most recent year 2000 projection.
2. One issue might be that the flat rate benefit creates a relatively steep cliff facing either partial or full career workers whose earnings are just below the threshold. We are unclear as to what that Schieber-Shoven threshold would be but assuming current values, a worker who works ten years for \$2,900 (1999 dollars) a year is always just below the qualifying threshold and will receive no tier one benefits; a worker who works that same period for \$3,000 a year will receive the minimum flat rate tier one benefit of \$250 per month. This is a much steeper cliff than faces current workers because currently the \$3,000 a year worker would receive a much smaller benefit.
3. To take the extreme, consider a group of thirty-year olds whose life expectancy at age 65 is only one month. An increase in the retirement age to 66 might have a disproportionate effect on the benefits of this group yet they would likely prefer that to an equal-yield tax increase. More generally a sufficient case against changing the retirement age cannot be that there are different life expectancies by group. Schieber and Shoven (pp. 224-226) have some discussion of these points.
4. However the most recent year 2000 trustees' report indicates that financial projections for that program have improved dramatically.
5. Both Schieber-Shoven and Graetz-Mashaw have dedications to children or grandchildren, the former adding "and all the other workers of the Third Millennium". Baker-Weisbrot's dedication includes "the thousands of activists, including many senior citizens..."

6. In the theoretical models of Veall, 1986 and Lindbeck and Weibull, 1988, if it is assumed the social security program is ongoing, increased funding by the current generation will not improve its own retirement consumption level as the next generation will withdraw its contribution by an offsetting amount.

7. Indeed we wonder if the previous naiveté by some social security reformers regarding demographic and productivity forecasts is being replaced by an alternative naiveté regarding financial markets. The huge fall in Japanese stock prices in the 1990s is Exhibit A.

8. Schieber and Shoven (p. 371) write, “Maybe it is not fair that today’s workers have inherited such a system. But that wrong does not make it right for us to pass current, or, more likely, much larger debts on to future generations”.



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No. 35: 2 ½ Proposals to Save Social Security

D. Fretz  
M.R. Veall

1. Traditional approaches to the economics of population ageing. • Challenges and opportunities. 2. The multiple layers of economic effects in ageing societies. • The impact of the Silver Economy: increasing inequalities? 3. Taking a radical life course approach. • Ageing 4.0: Economic and social dimensions. • Employment at all ages and life-long learning facilitated. • Productivity gains • More appropriately skilled workforce.

for Research on Social and Economic Dimensions of an Aging Population (SEDAP) is an interdisciplinary research program centred at McMaster University with co-investigators at seventeen other universities in Canada and abroad. The SEDAP Research Paper series provides a vehicle for distributing the results of studies undertaken by those associated with the program. Authors take full responsibility for all expressions of opinion. SEDAP has been supported by the Social Sciences and Humanities Research Council since 1999, under the terms of its Major Collaborative Research Initiatives Program. The social and economic implications of an aging population are becoming increasingly apparent in many industrialized nations around the globe. With populations in places such as North America, Western Europe and Japan aging more rapidly than ever before, policymakers are confronted with several interrelated issues, including a decline in the working-age population, increased health care costs, unsustainable pension commitments and changing demand drivers within the economy. These issues could significantly undermine the high living standard enjoyed in many advanced economies.

Advanced Industr SEDAP-II -- Canada in the 21st Century: Moving Towards an Older Society. Major Funding from MCRI Program. SEDAP is a multi-disciplinary research program funded primarily by SSHRC and centered at McMaster University. It involves 46 academics from fourteen universities in Canada and 3 abroad. The program runs from Jan 3, 2005 to Apr 1, 2011. Summary of Research Plans and Funding Sources. The Implications of an Aging Population. The world is experiencing a seismic demographic shift—and no country is immune to the consequences. While increasing life expectancy and declining birth rates are considered major achievements in modern science and healthcare, they will have a significant impact on future generations.

Today's graphic relies on OECD data to demonstrate how the old-age to working-age ratio will change by 2060, highlighting some of the world's fastest aging countries. • There are many other social and economic risks that we can come to expect as the global population continues to age: The Squeezed Middle: With more people claiming pension benefits but less people paying income taxes, the shrinking workforce may be forced to pay higher taxes.