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Fiction on the Social Security Trust Fund

By Dean Baker
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Public opinion polls consistently show that Social Security is the most popular government program. With almost 50 million current beneficiaries, nearly everyone either receives Social Security themselves or knows someone who is currently dependent on the program.

In many ways Social Security is a model program in that does exactly what it was designed to do. It provides a core retirement income that ensures retirees a decent standard of living. In addition, it provides insurance for workers and their families in the event of disability or early death. There is very little fraud in the program, and the administrative costs of Social Security are less than 1/20th as high as the cost of private insurers.

This background is crucial because it explains the Social Security "crisis." The public fully appreciates what Social Security does and would never support efforts to privatize the program if they believed that Social Security was fundamentally sound. Therefore, proponents of privatization have undertaken a massive effort over the last quarter-century to convince the public that Social Security is going bankrupt.

The logic is simple; if the public is convinced that the Social Security program can't be sustained, then there is no alternative to privatization. If people buy the Social Security crisis story, then privatization may be the only way to save the program.

A big part of the crisis story is to convince the public that the Social





Security trust fund is just an "accounting fiction." Politicians, columnists, and even policy analysts routinely repeat this assertion. They have gone to great lengths to imply that the trust fund is some bizarre and confusing entity that cannot be relied upon to help sustain Social Security. For example, last year President Bush visited the site where the bonds held by the trust fund are stored and announced that these bonds were "just sheets of paper."

Bonds are sheets of paper (like stock certificates), but those of us who live in a modern economy should not be troubled by this fact. In a modern economy, claims to wealth are most often just accounting entries - as everyone who uses a bank account presumably understands.

There is no real mystery about the trust fund. In 1983, Congress voted to raise the Social Security tax by more than was necessary to help pay for current benefits. The intention was to build up a large trust fund which the program could then draw upon to pay for the retirement of the baby boom generation. The trust fund is approaching \$2 trillion, more than \$13,000 for every active worker.

Under the law, the trust fund must be held in US government bonds. Government bonds are not very mysterious - the vast majority of the public holds some amount of government bonds, either directly or through a retirement account. The bond commits the government to pay interest each year, and then to repay the bond in full when it comes due (usually in 5 years, 10 years, or 30 years). That is exactly how the bonds held by the trust fund work.

The Social Security privatizers try to make this process sound strange or confusing. They claim that repaying the bonds just means that the government is pulling money out of one pocket and putting it into another. While this is true, the important point is that the pockets belong to different pairs of pants.

Under the law, the bonds will be repaid from general government revenue. This money comes overwhelmingly from the individual and corporate income taxes. These are relatively progressive taxes; this money will come disproportionately from wealthy people like Bill Gates. On the other hand, the Social Security tax is very regressive. It is paid only from the first \$94,000 of wage income. Income from high salaries, stock, and businesses is not subject to the tax. In effect, the bonds require the government to tax high income people to pay Social Security benefits to ordinary workers.

Of course, high income people don't want to pay the taxes to repay the bonds. That is why they are so anxious to convince the public that the trust fund is not real. I calculated that defaulting on the trust fund would transfer more than \$1 trillion from the bottom 95 percent of the income distribution to the richest 5 percent ("[Defaulting on the Social Security Trust Fund Bonds: Winners and Losers](#)"). The richest 1 percent of families would walk away with nearly \$750,000 each.

In short, there is a lot of money at stake in convincing the public that the Social Security trust fund is not real. That is the reason we hear it called a fiction. In reality, there is nothing more confusing about the trust fund than an ordinary bank account. The public absolutely should demand that the government not default on the bonds held by Social Security and that the politicians and pundits start talking more honestly about the program.

Dean Baker is the co-director of the Center for Economic and Policy Research (CEPR). He is the author [The Conservative Nanny State: How the Wealthy Use the Government to Stay Rich and Get Richer](#) (www.conservativenannystate.org). He also has a blog, "Beat the Press," where he discusses the media's coverage of economic issues. It can be found at the CEPR website, www.cepr.net.

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