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Vast Borrowing Seen in Altering Social Security

By RICHARD W. STEVENSON

Published: November 28, 2004

WASHINGTON, Nov. 27 - The White House and Republicans in Congress are all but certain to embrace large-scale government borrowing to help finance President Bush's plan to create personal investment accounts in Social Security, according to administration officials, members of Congress and independent analysts.

The White House says it has made no decisions about how to pay for establishing the accounts, and among Republicans on Capitol Hill there are divergent opinions about how much borrowing would be prudent at a time when the government is running large budget deficits. Many Democrats say that the costs associated with setting up personal accounts just make Social Security's financial problems worse, and that the United States can scarcely afford to add to its rapidly growing national debt.

But proponents of Mr. Bush's effort to make investment accounts the centerpiece of an overhaul of the retirement system said there were no realistic alternatives to some increases in borrowing, a requirement the White House is beginning to acknowledge.

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"The administration hasn't settled on any particular Social Security reform plan," Joshua B. Bolten, the director of the White House's Office of Management and Budget, said in an e-mail message in response to questions about overhauling the system.

"The president does support personal accounts, which need not add over all to the cost of the program but could in the short run require additional borrowing to finance the transition," Mr. Bolten said. "I believe there's a strong case that this approach not only makes sense as a matter of savings policy, but is also fiscally prudent."

Proponents say the necessary amount of borrowing could vary widely, from hundreds of billions to trillions of dollars over a decade, depending on how much money people are permitted to contribute to the accounts and whether the changes to Social Security include benefit cuts and tax increases.


Borrowing by the government could be necessary to establish the personal accounts because of the way Social Security pays for benefits. Under the current system, the payroll tax levied on workers goes to benefits for people who are already retired. Personal accounts would be paid for out of the same pool of money; they would allow workers to divert a portion of their payroll taxes into accounts invested in mutual funds or other investments.

The money going into the accounts would therefore no longer be available to pay

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benefits to current retirees. The shortfall would have to be made up somehow to preserve benefits for people who are already retired during the transition from one system to the other, and by nearly all estimates there is no way to make it up without relying at least in part on government borrowing.

Mr. Bush and Republicans in Congress have paid little political price in the last four years for the swing from budget surpluses to deficits. But some polls show that Americans consider reducing the deficit to be a higher priority than many other goals, including cutting taxes, and embracing a new round of borrowing could pose political as well as economic risks.

A reasonable amount of borrowing now, the proponents say, would avert a much bigger financial obligation decades later. They say personal accounts would yield higher returns for individuals than the current system and could be a catalyst to broader changes that would bring the benefits promised by Social Security into line with what the system, which is also about to come under intense financial strain from the aging of the baby boom generation and the increase in life expectancies, can afford to pay.

Mr. Bush has vowed to push hard to remake Social Security. Republicans in Congress say the White House has signaled to them that Mr. Bush will put the issue at the top of his domestic agenda in the coming year.

But the White House has never answered fundamental questions about Mr. Bush's plan. In particular, it has not explained how it would deal with the financial quandary created by its call for personal accounts.

Some conservative analysts and Republicans in Congress say a portion of the temporary financial gap that would be created by personal accounts could be closed through measures like holding down the growth in overall government spending. But nearly everyone involved in the debate over Social Security agrees that some borrowing will be necessary.

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The main Republican players in Congress on the issue say they expect to endorse an increase in borrowing to finance the transition to a new system. But they remain split over whether to back plans that would include larger investment accounts and few painful trade-offs like benefit cuts and tax increases - and therefore require more borrowing - or to limit borrowing and include more steps that would be politically unpopular.

"Anybody who thinks borrowing money for the transition to personal accounts is going to solve the problem of the long-term solvency of Social Security doesn't understand the size of the problem," said Senator Charles E. Grassley, Republican of Iowa, the chairman of the Senate Finance Committee, which has jurisdiction over the retirement system. Advertisement

Mr. Grassley said Congress would also have to put benefit reductions and tax increases on the table, in part to hold down the need for borrowing and in part to assure that any changes restore Social Security's long-term financial stability.

Under current projections used by Social Security's trustees, the government will have to begin drawing on general tax revenue to pay benefits to retirees in 2018, the first year in which scheduled benefit payments will exceed revenues from the payroll tax dedicated to the retirement system. By 2042, the government will have exhausted the Social Security trust fund - its legal obligation to pay back to the retirement system the temporary surplus in payroll tax revenues it has borrowed over the last several decades to subsidize the rest of the budget - and after that Social Security would be able to pay only about three-quarters of promised benefits.

Opponents of Mr. Bush's approach say that Social Security's financial problems can be dealt with more easily without the addition of personal accounts, and that any large-scale borrowing would erase the presumed economic advantage of establishing the accounts: spurring more national savings, a goal that nearly all economists agree is worthy and important. Any increase in private, individual savings, they say, would be partly or wholly offset by an increase in public debt. National savings are what is left after counting up everything the nation spends. This pool of money goes to investing in the expansion and modernization of business. It is a vital component of economic health.

"To the extent that the transition is debt-financed, the ostensible macroeconomic benefits from individual accounts are undermined," said Peter Orszag, an economist at the Brookings Institution who has been critical of personal account plans. "In particular, you do not get an increase in national savings. It's engaging effectively

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in accounting gimmicks to make it look as if you're doing something when you're not."

In an effort to pressure the White House to acknowledge some of the financial trade-offs in its approach, Democratic leaders in Congress this week asked Mr. Bush to include in his next budget an accounting of the money that would be needed for his Social Security plan.

Only by including such figures in the budget, the Democrats said in a letter to Mr. Bush, "will Congress and the American people be able to weigh the difficult trade-offs between large-scale borrowing, Social Security benefit cuts, tax increases, and other spending reductions that may be required to fund your Social Security private accounts proposal. "

The White House, which has promised to cut the deficit in half while making Mr. Bush's tax cuts permanent, has signaled that it does not intend to include the figures in its budget, since the administration has not endorsed a detailed plan.

The budget deficit in the year ended Sept. 30 was \$413 billion. The total national debt is about \$7.5 trillion, including \$3 trillion owed by the government to itself, much of it in the form of the Social Security trust fund. Rising debt forces the government to pay out more of its revenue in interest payments, and can put upward pressure on the interest rates paid by businesses and consumers.

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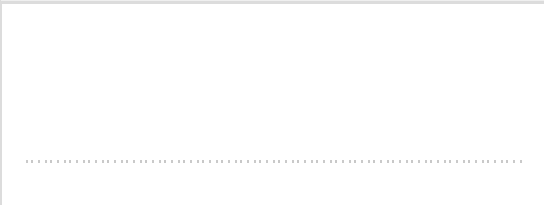
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Some Republicans in Congress are concerned that too much borrowing would carry large economic and political costs. Senator Judd Gregg, the New Hampshire Republican who will be chairman of the Senate Budget Committee next year, said he would support borrowing money for Social Security if it was part of a plan that also included modest benefit cuts and tax increases.

But he said the additional debt might have to be accounted for on the government's books in a way that would not technically show an increase in the budget deficit in coming years. Advertisement

"You've got to look at this as a very significant long-term fiscal policy decision where you're going to have a loss in the first 10 to 15 years and a significant move toward solvency in the last 20 to 30 years," Mr. Gregg said. "That mitigates against doing it in the context of a typical budget resolution."

To critics of personal accounts, Mr. Gregg's suggestion amounts to relying on budget gimmickry to hide the true costs. But supporters of the accounts say borrowing even a few trillion dollars now would be worthwhile, because it would help wipe out the retirement system's long-term unfunded liability - the difference between what it will owe retirees under current law and the amount it will take in - of around \$11 trillion.

Senator John E. Sununu of New Hampshire and Representative Paul D. Ryan of Wisconsin, both Republicans, have sponsored legislation that would allow workers to contribute more to their personal accounts than most other plans proposed by members of Congress and outside groups and would not require tax increases or benefit cuts. But by some estimates it would require nearly \$2 trillion in borrowing - and, in the view of its critics, much more - and even then would rely on the idea that the new system would create so much more economic growth that it would partly pay for itself by generating additional tax revenues for the government.

Representative Jim Kolbe, Republican of Arizona, said the government could probably keep new borrowing to \$800 billion over 10 years, but only if Congress and the administration are willing to back tax increases and benefit cuts as part of a broad overhaul of the retirement system.

"People do not understand that tough choices need to be made," Mr. Kolbe said.


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