

## **"Social Security Saved!"**

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**Address by Senator Daniel Patrick Moynihan  
Institute of Politics: Spring Exercise on Social Security Reform  
John F. Kennedy School of Government at Harvard University  
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**Let me begin with a proposition appropriate to our setting. Social Security in the United States is very much the work of academicians. It came about in an exceptional 14 months in the first Roosevelt administration, but economists had been planning it for a third of a century.**

**A second proposition. As with much social policy that originates with academic experts, the level of informed political support for Social Security within the electorate has always been low, and just now is getting lower.**

**This history goes back to the progressive era at the beginning of the century. It is to be associated, for example, with John R. Commons of the University of Wisconsin who helped found the American Association for Labor Legislation in 1906. The German government had created a workman's compensation system, a form of insurance against industrial injuries, and a sickness insurance program in 1884. In the academic manner, these ideas crossed the Atlantic, and were particularly well received by the north European populace of Minnesota. Edwin E. Witte, the author of the Social Security Act of 1935, a student of Commons, was, for example, of Moravian stock.**

**In a fairly short order workman's compensation became near universal among the states, and the reformers now looked to universal health insurance, a logical follow-on. In a mode we have experienced in our time, this proved too much. Business grew nervous. The American Federation of Labor, led by Samuel Gompers, "joined his fellow members in impassioned opposition." (1) Labor leaders of Gompers' generation looked with suspicion on government-provided benefits. They wanted trade unions to do that. World War I and its aftermath pretty much ended the era. As Witte's biographer writes:**

**No great popular enthusiasm developed for health insurance, and in the troubled days immediately following World War I it went down to defeat amid contradictory cries of "Made in Germany" and of "Bolshevism." (2)**

**In the event, when the political system was ready it had to send for the academics. Roosevelt, pressed by Huey Long, and the Townsend Plan, and the general distress of the Depression, needed a big bill. In June of 1934 he set up the Committee on Economic Security, headed by Frances Perkins, a knowledgeable reformer, albeit of the Gramercy Park variety. And also a woman with a magical ability to get strong men, from Tammany district leaders to Supreme Court Justices, to help her out because she was, well, so in need of help.**

**Madame Perkins brought Commons' student Witte from Wisconsin to staff her Committee on Economic Security, but it was left to her to figure out how to get a bill passed. She relates the sequence in The Roosevelt I Knew:**

**It is difficult now to understand fully the doubts and confusions in which we were planning this great new enterprise in 1934. The problems of constitutional law seemed almost insuperable. I drew courage from a bit of advice I got accidentally from Supreme Court Justice Stone. I had said to him, in the course of a social occasion a few months earlier, that I had great hope of developing a social**

insurance system for the country, but that I was deeply uncertain of the method since, as I said laughingly, "Your Court tells us what the Constitution permits." Stone had whispered, "The taxing power of the Federal Government, my dear; the taxing power is sufficient for everything you want and need." (3)

And so it came about that on August 14, 1935, when FDR signed the bill, standing at the President's right in the official photograph was Robert L. Doughton of North Carolina, Chairman of the Committee on Ways and Means.

I am not altogether comfortable with what I am about to say, but I will do so anyway in the hope that you will give the subject some thought. I suggest that giving jurisdiction over Social Security to the tax writing committees of the Congress (the Finance Committee in the Senate), has caused the program to be treated as a somewhat marginal concern by its congressional guardians. As an example, no one much objected when the originally independent Social Security Administration was folded into first one agency then another, to the point of near disappearing.

In 1993 I became Chairman of Finance and in time was able to re-establish an independent Social Security Administration. In the Congressional Directory of that year there were 278 names between the incumbent Secretary of Health and Human Services and the Administrator of Social Security, "Vacant." (4)

I even managed, as I put it, to decriminalize babysitting. Early in the Clinton administration, a number of senior appointees came afoul of the Social Security law. They had not paid payroll taxes on various types of household help. The taxes were due quarterly, in quintuplet forms and the like. And few persons knew they were owed. This was especially the case with babysitters. A fine rite of passage for young girls. And yet a taxable occupation. I was able to enact legislation putting an end to any of that for persons under age 18. As I related in Miles To Go, it may have saved my 1994 election. (5) People didn't know much about Social Security, but after a succession of prospective nominees for Attorney General had to be withdrawn, they realized that Social Security might send them to jail. Not what Frances Perkins had in mind.

Over the years, the original excitement surrounding Social Security faded; and few noticed. When a time came that a majority of non-retired young adults had concluded they themselves would never get Social Security, few showed any great concern. Some elements within the Republican Party seem always to have been inclined to the thought that the whole scheme was a Rooseveltian fraud, and the public seemed to agree. (A Ponzi scheme, was the phrase, current in the 1930s.) Then in the late 1970s a combination of high inflation and overindexing did indeed move the Trust Funds perilously close to insolvency. There was no great danger. At worst, checks might have been delayed a few days. But this did not prevent President Reagan's budget director from stating in the spring of 1981 that "Unless both the House and the Senate pass a bill in the Congress which can be signed by the President within the next 15 months, the most devastating bankruptcy in history will occur on or about November 3, 1982." (6) A Presidential Commission was set up, chaired by the redoubtable Alan Greenspan, with Robert J. Myers as staff director, Myers -- a lifelong Republican -- having come from the Midwest to help out Witte in 1934! But no agreement could be reached by the time the commission expired at the end of 1982.

Then the shade of Frances Perkins intervened. On January 3, 1983, Robert J. Dole, Senate Majority Leader, published an article on the op-ed page of *The New York Times*, entitled "Reagan's Faithful Allies." It seemed that many people thought Congressional Republicans weren't giving the President the support he needed and deserved. Not so, Senator Dole said, we are with the President and there are great things still to be done. Then this:

Social Security is a case in point. With 116 million workers supporting it and 36 million beneficiaries relying on it, Social Security overwhelms every other domestic priority. Through a combination of

relatively modest steps including some acceleration of already scheduled taxes and some reduction in the rate of future benefit increases, the system can be saved. When it is, much of the credit, rightfully, will belong to this President and his party. (7)

That day I was being sworn in for a second term in the Senate. I had read the article and went up to Senator Dole on the Senate Floor and asked if he really thought that, why not try one last time? And he did think it. A year of listening to Myers had altered a lifetime of Republican dogma. We met the next day. The day after that Barber Conable was brought in, a Republican who both understood and believed in Social Security. On January 15th, 13 days from our first exchange, agreement was reached at Blair House and the crisis passed. (In a November 2, 1997 interview on "Meet The Press," Senator Dole cited this as his greatest accomplishment in his Senate career. And well he might.)

Social Security was secure for the time being. Indeed, the payroll tax generated a considerable surplus which we have lived off ever since, and will continue to enjoy for yet a few years. But the loss of confidence was grievous. Had we, indeed, just barely escaped bankruptcy? What then did the future hold but more such crises? In the meanwhile the academic world had changed. Energetic and innovative minds (one thinks of Martin Feldstein here at Harvard) had turned away from government programs -- "the nanny state" -- toward individual enterprise, self-reliance, free markets. As the 1990s arrived, and the long stock market boom, the call for privatization of Social Security all but drowned out the more traditional views.

This was for real. In 1996, Congress enacted legislation, signed by the President, which repealed Title IV-A of the Social Security Act, Aid to Families with Dependent Children. The mothers' pension of the progressive era, incorporated in the 1935 legislation, vanished with scarcely a word of protest.

Will the Old Age pensions and survivors benefits disappear as well? What might once have seemed inconceivable is now somewhere between possible and probable. I, for one, hope that this will not happen. A minimum retirement guarantee, along with survivors benefits, is surely something we ought to keep, even as we augment retirement income in other ways. What is more, this can readily be done. Let me outline a solution.

I have a bill entitled "The Social Security Solvency Act of 1998." Senator Robert Kerrey and I will introduce it in the Senate this week. Here are the specifics:

### ***I. Reduce Payroll Taxes and Return to Pay-As-You-Go System with Optional Personal Accounts***

#### ***A. Reduce Payroll Taxes and Return to Pay-As-You-Go***

As I first proposed in 1989, this bill would return Social Security to a pay-as-you-go system. That is, payroll tax rates would be adjusted so that annual revenues from taxes closely match annual outlays. This makes possible an immediate payroll tax cut amounting to about \$800 billion over the next decade, with the lower rates remaining in place for the next 30 years. We would cut the payroll tax from 12.4 to 10.4 percent between 2001 and 2024, and the rate would stay at or below 12.4 percent until 2045. Even in the out-years, as we say, the pay-as-you-go rate under this plan will increase only slightly above the current rate of 12.4 percent. It would top out at 13.4 percent in 2060. And in order to ensure continued solvency, the Board of Trustees of the Social Security Trust Funds will make recommendations for a new pay-as-you-go tax rate schedule if the Trust Funds fall out of close actuarial balance. Such a new tax rate schedule would be considered by the Congress under fast track procedures.

There is a matter of fairness here. Of families that have payroll tax liability, 80 percent pay more in payroll taxes than in income taxes.

### ***B. Voluntary Personal Savings Accounts***

Beginning in 2001, the bill would permit voluntary personal savings accounts, which workers could finance with the proceeds of the two percent cut in the payroll tax. Alternatively, a worker could simply take the employee share of the tax cut in the form of an increase in take-home pay equal to one percent of wages. (Economists will argue that workers who do not opt for voluntary personal savings accounts will also, eventually, receive the employer share in the form of higher wages. But that's a discussion for another time.)

The magic of compound interest will enable workers who contribute two percent of their wages to these personal savings accounts for 45 years (2000-2045) to amass a considerable estate, which they can leave to their heirs. Some examples, in nominal dollars, for workers at various earnings levels:

**Real Rate of Interest**

<b>Earnings Level</b>	<b>3 Percent</b>	<b>4 Percent</b>	<b>5 Percent</b>
Minimum Wage (\$12,000)	\$110,000	\$135,000	\$175,000
Average Wage (\$30,000)	\$275,000	\$350,000	\$450,000
Maximum Wage (\$70,000)	\$660,000	\$850,000	\$1,100,000

### ***C. Increase in Amount of Wages Subject to Tax***

Under current law, the Social Security payroll tax applies only to the first \$68,400 of wages in 1998, indexed to the annual growth in average wages. At that level, we are taxing about 85 percent of wages in covered employment. That percentage has been drifting down because wages of persons above the taxable maximum have been growing faster than wages of persons below it.

Historically, about 90 percent of wages have been subject to tax. Under this bill, we propose to increase the taxable maximum to \$97,500 (thereby taxing about 87 percent of wages) by 2003. We then resume automatic changes in the base, tied to increases in wages, as under current law. (The taxable maximum is projected to increase to \$82,800 in 2003 under current law.)

## ***II. Indexation Provisions***

As students of the Congress, you know by now that every tax cut requires an offset. So how do we offset the payroll tax cut in this bill? By two indexation procedures, and some other changes that most observers agree are needed.

### ***A. Correct Cost of Living Adjustments by One Percentage Point***

We propose to correct cost of living adjustments by one percentage point. This adjustment would apply to all indexed programs (outlays and revenues) except Supplemental Security Income.

This is an issue that has been with us for a long while now. Some 35 years ago in the Kennedy Administration I was Assistant Secretary of Labor for Policy Planning and Research, with nominal responsibility for the Bureau of Labor Statistics. The then-Commissioner of the Bureau of Labor Statistics, Ewan Clague, could not have been

more friendly and supportive; he and his staff undertook to teach me, to the extent I was teachable. Although the BLS statisticians were increasingly confident of the accuracy with which they measured unemployment, business and labor were still distrustful. By contrast, the Consumer Price Index, begun in 1918 (monthly unemployment numbers only begin in 1948) was quite a different matter. It was beginning to be used as a measure of inflation in labor contracts and such like. Our BLS economists knew that the CPI overstated inflation, but no one seemed to mind. Business could make that calculation in collective bargaining contracts. And if they failed to do, well, it was good for the workers. Indeed, on taking office in 1961, the Kennedy Administration had waiting for it a report by a distinguished National Bureau of Economic Research committee headed by George Stigler, who would go on to win the Nobel Prize in economics. The Stigler report, "The Price Statistics of the Federal Government," (8) concluded that the CPI and other indexes overstated the cost of living.

That theme was picked up again by Professor Robert J. Gordon in an article in the Public Interest in 1981. (9) Gordon wrote "It is discouraging that so little has been done [by the BLS] . . . for so long." The bias identified by Stigler was still present in the CPI, which Gordon pointed out was "the single most quoted economic statistic in the world."

In 1994, in a celebrated memorandum entitled "Big Choices," then- OMB Director Alice Rivlin noted that "CPI may be overstated by 0.4% to 1.5%." It then fell to the Senate Finance Committee to pursue the issue. We held three hearings and in short order found that the BLS itself acknowledges that the CPI is not a cost of living index. In the BLS pamphlet "Understanding the Consumer Price Index: Answers to Some Questions" there is the following Q & A:

Is the CPI a cost of living index? No, although it frequently (and mistakenly) is called a cost-of-living index. (10)

In 1995, the Finance Committee appointed the Advisory Commission to Study the Consumer Price Index. Chaired by Professor Michael J. Boskin of Stanford, who had been Chairman of the Council of Economic Advisers under President Bush. Also on the Commission were two eminent members of the Economics Department here at Harvard: Zvi Griliches and Dale Jorgenson. Their final report concluded that the CPI overstates changes in the cost of living by 1.1 percentage points. (11)

It is true that recently the Bureau of Labor Statistics has made some improvements, a routine of some 80 years now, but most of these were already anticipated when the Boskin Commission issued its final report. That bias has not been corrected. It is not in the nature of this beast. Speaking before the annual meetings of the American Economic Association and the American Finance Association in Chicago in January of this year, Alan Greenspan said:

Despite the advances in price measurement that have been made over the years, there remains considerable room for improvement.

So our legislation includes the one percentage point correction, but it also establishes a Cost of Living Board to determine on an annual basis if some further refinement is necessary.

### *B. Increase in Retirement Age*

In our 1983 agreement, the retirement age was increased, over time, to age 67 for those turning 62 in the year 2022. This legislation would make gradual increases in the retirement age by two months per year between 2000-2017, and by one month every two years between years 2018 and 2065. This increase is a form of indexation which results in retirement ages of 68 in 2017 (for workers reaching age 62 in that year), and 70 in 2065 (for workers reaching age 62 in that year.)

I refer to the increase as a form of indexation because it is related to the increase in life expectancy. Persons retiring in 1960 at age 65 had a life expectancy, at age 65, of 15 years and spent about 25 percent of their adult life in retirement. Persons retiring in 2073, at age 70, are projected to have a life expectancy at age 70 of about 17 years, and would also spend about 25 percent of their adult life in retirement. These are persons not yet born today. And they can expect, on average, to live almost to age 90. And that may be a conservative estimate as we don't know where medical technology will take us.

### ***III. Program Simplification -- Repeal of Earnings Test***

The so-called earnings test would be eliminated for all beneficiaries age 62 and over, beginning in 2003. (Under current law, the test increases to \$30,000 in 2002.) The earnings test is a relic of the Depression years. When Social Security was enacted in 1935, the Federal government was trying to discourage elderly workers from remaining in the labor force because there were not enough jobs. Today, the unemployment rate is down to 4.6 percent, and we should do everything possible to encourage workers to remain in the labor force. The earnings test is also an administrative burden with about one million beneficiaries submitting forms to the Social Security Administration so that benefits can be withheld -- reduced -- if the beneficiary has wages in excess of the earnings test. All for naught because higher benefits -- roughly offsetting the loss in benefits -- are paid in the future for each month for which benefits are withheld.

### ***IV. Other Changes***

All three factions of the 1994-1996 Social Security Advisory Council supported some variation of the following three provisions. (12)

#### ***A. Normal Taxation of Benefits,***

We propose to tax Social Security benefits to the same extent private pensions are taxed. That is, Social Security benefits would be taxed to the extent that the worker's benefits exceed his or her contributions to the system. Consequently, about 95 percent of Social Security benefits would be taxed. (For private pensions, the percentage taxed varies according to how much of the plan is funded by employee contributions. In many private pensions, the employee makes no contribution, so 100 percent of the pension benefits are taxed.)

#### ***B. Coverage of Newly Hired State and Local Employees***

Effective in 2001, we would extend Social Security coverage to newly hired employees in currently excluded State and local positions. In 1935, State and local employees were not included in Social Security because it was believed that the Federal government did not have the power to tax State governments. However, subsequent actions by Congress providing for mandatory Medicare coverage of State and local employees have not been challenged. Then a unanimous Supreme Court decision in 1986 put the issue to rest. In Bowen v. Public Agencies Opposed to Social Security Entrapment, (13) the Court upheld a provision in the Social Security Amendments of 1983 that prevented States from withdrawing from Social Security. Including State and local workers is not only constitutional, it is fair, since most of the five million State and local employees (about a quarter of all State and local employees) not covered by Social Security in their government jobs do receive Social Security benefits as a result of working at other jobs -- part-time or otherwise -- that are covered by Social Security. Relative to their contributions these workers receive generous benefits. Our bill will bring these employees into the system, preventing them from getting a windfall.

#### ***C. Increase in Length of Computation Period***

We would increase the length of the computation period from 35 to 38 years. Consistent with the increase in life

expectancy and the increase in the retirement age, we expect workers to have more years with earnings. Computation of their benefits should be based on these additional years of earnings.

### BUDGET EFFECTS

Not only does this proposal provide for long-run solvency of Social Security, financed with payroll tax rates not much higher than current rates in the out-years, but it is also fully paid for in the short-run. The Congressional Budget Office's preliminary estimate indicates that for the 10-year period FY 1999-2008, the bill would increase the projected cumulative budget surplus by more than \$100 billion, from \$671 billion to \$803 billion. For the five year period FY 1999-2003, CBO projects that, under this plan, the cumulative surplus would be reduced by just \$6 billion. In no year is there a deficit. And, to repeat, all of this is accomplished while reducing payroll taxes by almost \$800 billion.

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Will this happen? I just do not know. In a manner that the late Mancur Olson would recognize, over time Social Security has acquired a goodly number of veto groups which prevent changes, howsoever necessary. There are exceptions as in 1983 when we did our work in 13 days and behind closed doors. But otherwise, stasis is the norm. Thus for the past three or four years almost all the major players in the Administration have recognized that we had to employ a better measure of price inflation. But repeatedly action was vetoed by the, well, veto groups.

They can go on in this manner if they choose. But if they do, in 30 years time Social Security as we have known it since 1935 will have vanished. The veto groups that prevented any change in the welfare system -- Title IV-A -- for so long, looked up one day to find the system had vanished. It is time then for courage as well as policy analysis.

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### NOTES

1. Theron F. Schlabach, *Edwin E. Witte: Cautious Reformer* (Madison: State Historical Society of Wisconsin, 1969), 83.
2. *Ibid.*
3. Frances Perkins, *The Roosevelt I Knew* (New York: The Viking Press, 1946), 286.
4. *Official Congressional Directory, 103rd Congress, 1993-1994* (Washington, DC: United States Government Printing Office, 1993), 803-825.
5. Daniel Patrick Moynihan, *Miles to Go: A Personal History of Social Policy* (Cambridge, MA: Harvard University Press, 1996): 24-25.
6. *Social Security Financing Recommendations*, Hearing before the U.S. House of Representatives Subcommittee on Social Security (28 May 1981) (testimony of David A. Stockman, Director Office of Management and Budget), 40-41.
7. Bob Dole, "Reagan's Faithful Allies," *The New York Times*, 3 January 1983, A 19.
8. Price Statistics Review Committee of the National Bureau of Economic Research, *The Price Statistics of the Federal Government: A Report to the Office of Statistical Standards, Bureau of the Budget* (Washington, DC: National Bureau of Economic Research, 1961), 35.
9. Robert J. Gordon, "The Consumer Price Index: Measuring Inflation and Causing It," *The Public Interest* 62 (Spring 1981): 134.

10. U.S. Department of Labor, Bureau of Labor Statistics, *Understanding the Consumer Price Index: Answers to Some Questions* (November 1997), 3.
11. Senate Committee on Finance, *Final Report of the Advisory Commission to Study the Consumer Price Index* (1996), 104th Cong., 2d sess. Committee Print, 1.
12. *Report of the 1994-1996 Advisory Council on Social Security* (Washington, DC), 184.
13. 477 U.S. 41 (1986).