

The **Perils** of Privatization

**Social Security Privatization
Cuts Lifetime Benefits;
Makes Senior Citizens Vulnerable to Poverty**

**The Impact on
Women**

August 7, 2008

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Social Security Privatization

Cuts lifetime benefits for women by as much as \$240,264

Makes more than 5.6 million women senior citizens vulnerable to poverty.

Institute for America's Future

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Social Security is back in the news. In a town-hall event on July 7, 2008, a young woman asked Arizona Senator John McCain if she was likely to receive Social Security benefits someday. In his reply, McCain lamented Social Security's design and structure and, as he had elsewhere, indicated that he would radically change this successful program.¹ He said, "Americans have got to understand that we are paying present-day retirees with the taxes paid by young workers in America today, and that's a disgrace, it's an absolute disgrace and it's got to be fixed."²

We've been here before. Three years ago, President Bush declared that Social Security faced a financial crisis, and his solution was privatization — taking payroll taxes we all pay into the system and investing a portion of those funds in private stock market accounts. Now John McCain is bringing the idea back. In March 2008, McCain told the Wall Street Journal, "As part of Social Security reform, I believe that private savings accounts are a part of it — along the lines that President Bush proposed."³ The idea became more concrete in July 2008, when McCain named economist Martin Feldstein, the "chief intellectual force behind privatization," as a surrogate on his campaign.⁴ These moves revive an idea that the American people rejected three years ago.

This report updates research published by the Institute for America's Future at that time. It estimates the reduction in Social Security benefits that a typical woman resident can expect and the number of seniors exposed to poverty if Social Security were privatized.

For future generations, Social Security privatization would:

- Cut life-time benefits for women by \$240,264
- Makes more than 5.6 million women senior citizens vulnerable to poverty.

Social Security Works

Social Security is not a "disgrace." It is a successful social program and a profound intergenerational promise. Every generation pays into Social Security during its turn, and withdraws from Social Security when its time comes. Social Security has been successfully operating that way for over 70 years.

Social Security works. It lifts 1.3 million children and nearly 13 million senior citizens out of poverty.⁵ Social Security provides 73 percent of the typical retiree's income, compared to 17 percent from pensions and 10 percent from savings and other sources.⁶

Before Social Security, nearly half of American seniors lived in poverty. Today, fewer than 9 percent of seniors spend their “golden years” in poverty.⁷ Social Security is especially important now, with private sector pensions disappearing and savings scarce. According to the estimates by the Economic Policy Institute, without Social Security, more than 35 percent of Americans aged 65 and older would be living in poverty.

Social Security and Women

In 2006, over 25.4 million adult women received Social Security benefits; over 19.8 million of whom receive retirement benefits.⁸ Studies have shown that the progressive benefit structure, survivors and disability benefits, and inflation-protected benefits greatly benefit women because they live longer and tend to have lower incomes.⁹ In 2006, women represented 57 percent of all Social Security beneficiaries age 62 and older and approximately 70 percent of beneficiaries age 85 and older.¹⁰ The American Association of Retired Persons notes that in 2001 the poverty rate for older women would be significantly higher without Social Security—increasing from 12 percent to over 50 percent.¹¹

Real Security. Created Crisis.

Some politicians and conservative privatization advocates have created a myth that Social Security is in crisis. They issue dire warnings and predict imminent bankruptcy. McCain told the young woman in the July town hall event that it was “unlikely” she would receive her benefits. President Bush tells a story of a poll of young people who “think it's more likely they're going to see a UFO than get a Social Security check.”¹² The White House web site elaborates: “If we do not act to fix Social Security now, the only solutions will be dramatically higher taxes, massive new borrowing or sudden and severe cuts in Social Security benefits or other government programs.”¹³

The proclamations work. One poll says that 73 percent of Americans believe Social Security has “major problems” or is in “crisis.”¹⁴

The reality is far different. Social Security currently has a surplus of \$2 trillion. The surplus is projected to increase to over \$4 trillion by 2016, more than four times the amount needed to pay benefits in that year.¹⁵ According to cautious estimates by the Congressional Budget Office, the Social Security trust fund would not be depleted until 2046.¹⁶

Privatization: Risks and Realities

Privatization means diverting deductions from the Social Security trust fund into private accounts run by private investment companies. Conservatives have touted privatization for years as a way to increase returns on investment. Privatization, however, has a variety of problems.

First, privatization would transfer huge administrative fees to Wall Street. Managing large numbers of small accounts is inherently inefficient. Administrative costs for private systems in Mexico, Chile and Argentina are between 1.8 to 2.4 percent of the program total; in England, administrative costs are 3.2 percent. In contrast, administrative costs of Social Security run less than one percent.¹⁷

Second, diverting funds would cause the trust fund's surplus to run out much sooner, leading to benefit reductions and retirement insecurity — the opposite of Social Security's intergenerational promise. The Center on Budget and Policy Priorities estimates that President's Bush's plan would have created \$17.7 trillion in additional debt by 2050.¹⁸

Third, and most importantly, privatization replaces the guaranteed floor of economic security with the uncertainty of the stock market. In 2007, Social Security guaranteed economic security to more than 49 million grandparents, parents and children worldwide.¹⁹ Individuals are free, of course, to invest their personal savings in the stock market – but Social Security guarantees a floor beneath which their fortunes will not fall. Furthermore, the risk of the stock market could provide great risks for women. The Economic Policy Institute notes, “Because women earn less than men do over their life times, they will be able to save less in their individual accounts. Thus income inequalities present during women's work lives would carry over into their retirement years [with private accounts].”²⁰

Research Findings

In the United States, 48.5 million count on their earned Social Security benefit every month—including more than 25.4 million women.²¹ In addition to the benefits that Social Security provides to women and their families, it also provides a stable level of individual income that fuels the United States economy. Thousands of businesses, and the state government, also depend on the Social Security guarantee. Fully \$580.5 billion in individual income flows into the United States' economy from Social Security each year – roughly \$48.4 billion every month.²²

Privatization could cast many women seniors below the poverty line. According to the U.S. Census Bureau, over 21.7 million women in the United States lived in poverty in 2006.²³ In 2006, 43 percent of all elderly unmarried females receiving Social Security benefits relied on Social Security for 90 percent or more of their income.²⁴ For nearly one in four women aged 65 and older, Social Security is their only source of income.²⁵ Today, the average Social Security check for individual retirees in the United States is \$1,088 per month.²⁶ But \$867 per month is needed just to stay above the federal poverty line. These individuals are close to the edge, and vulnerable to swings in the cost of food, housing or energy.

The Center on Budget and Policy Priorities calculated in 2005 that if a Bush-style privatization plan were enacted, children born around the time the plan started would have their annual guaranteed benefits cut by 50 percent when they retire.²⁷ If that were to happen to current-day women senior citizens in the United States, those with incomes up to 191% of the current poverty line would no longer have a guarantee that they would avoid poverty.²⁸ Social Security would have failed in its promise of security. More than 5.5 million women senior citizens in the United States would be left behind.²⁹

Second, benefits would be reduced even among people not plunged into poverty. Under a Bush-like privatization plan, a woman born today in the United States who retires at the current full retirement age of 67, would see a lifetime benefit cut of \$240,264 in today's dollars.³⁰ This is the benefit cut a woman would suffer even *after* accounting for earning an average 4.35 percent return on their private account investment.³¹

The Solution

Social Security is not going bankrupt. But we do need to pay attention to the impact the retirement of the baby-boom generation is having on the program. The solution is to strengthen the existing structures, not to reinvent them or privatize them. Currently, the Social Security payroll tax currently applies only to the first \$102,000 a worker makes — any earnings above that are tax-free. One simple solution is to apply the tax to some or all earnings above \$102,000. Lifting that cap is a fair and minor adjustment that could prevent any shortfall after 2046.³²

— Dean Baker, Co-Director of the Center for Economic and Policy Research, contributed technical assistance to this report.

ENDNOTES

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- ³ Bob Davis. "McCain's Economy Platform: Big Tax Cuts, With Caveats." *Wall Street Journal*. 3 March 2008. http://online.wsj.com/public/article_print/SB120451614688707083.html.
- ⁴ Carolyn Lochhead. "Friedman's 'heresy' Hit Mainstream: Private Social Security Accounts were His Idea." *San Francisco Chronicle*. 5 June 2005. <http://www.sfgate.com/cgi-bin/article.cgi?f=/c/a/2005/06/05/ING9QD1E5Q1.DTL>. Feldstein is widely acknowledged as the "chief intellectual force behind privatization" of Social Security. He wrote *The Case for Privatization* (<http://www.foreignaffairs.org/19970701faessay3782/martin-feldstein/the-case-for-privatization.html>) and *Privatizing Social Security: The Ten Trillion Dollar Opportunity* (<http://www.cato.org/pubs/ssps/ssp7.html>). Feldstein is also a surrogate of Senator John McCain. See: Senator John McCain. "Economists' Statement on John McCain's Jobs for America Economic Plan." 7 July 2008. *JohnMcCain.com*. <http://www.johnmccain.com/Informing/News/PressReleases/Read.aspx?guid=c90681b9-5dfe-4de4-8057-ceedb30c228d>. See also: Senator John McCain. "ICYMI: McCain Campaign Conference Call on John McCain's Jobs for America Economic Plan." *JohnMcCain.com*. 28 July 2008. <http://www.johnmccain.com/Informing/News/NewsReleases/Read.aspx?guid=37ce003f-9a85-4a45-ab1b-e5433a4c1693>.
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