Social Security Privatization Would Lead to Benefit Cuts of 54 Percent For Young Workers

In June 2000, The Century Foundation (TCF) released a report entitled *Governor Bush's Individual Account Proposal: Implications for Retirement Benefits.* Written by Henry Aaron, Alan Blinder, Alicia Munnell, and Peter Orszag – four of the nation's leading experts on Social Security – the report finds that, if 2 percentage points of the current 12.4 percent payroll tax were diverted into individual retirement accounts, Social Security benefits would have to be cut by 54 percent for workers aged 30 and younger in 2002 in order to restore Social Security's long-term solvency. The following explains how TCF's report reaches that 54 percent figure:

- Over the next 75 years, Social Security faces a projected financing shortfall equal to roughly two percent of taxable payroll.

- Diverting 2 percentage points of the payroll tax into individual retirement accounts would necessarily increase that shortfall to nearly 4 percent of taxable payroll.

- This shortfall can be closed in only one of four ways: (1) by raising payroll taxes, (2) by investing a portion of the Social Security Trust Funds in equities, (3) by transferring general revenue into Social Security from the rest of the budget, or (4) by cutting Social Security benefits.

- Since President Bush has repeatedly ruled out the first two options and his tax and budgetary policies make the third impossible, TCF's report assumes a 2-percentage point privatization plan would have to be accompanied by sizable benefit cuts in order to achieve long-term solvency.

- TCF's report calculates that closing a gap of nearly 4 percent of taxable payroll would necessitate benefit cuts of 41 percent, if such cuts were imposed uniformly for all beneficiaries aged 55 and younger in 2002. If cuts were phased-in, such that older workers experienced smaller reductions, benefits would have to be cut by 54 percent for those workers aged 30 and younger in 2002. Workers between the ages of 55 and 35 would suffer benefit reductions of 25 to 46 percent under a phased-in scenario.

- TCF's report assumes that survivors' benefits would be subjected to the same level of cuts as retirement benefits. Yet, President Bush claims, as one of the principles for his Social Security Commission, that he will "preserve Social Security's disability and survivors components." If survivors' benefits were insulated from benefit cuts, much larger cuts in retirement benefits would be necessary.

- It should be noted that the 54 percent figure for Social Security benefit cuts does not include any payments from workers' individual accounts. However, TCF's report finds that even when the proceeds of individual accounts are included, single average wage workers aged 30 and younger in 2002 would experience a loss of retirement income of 20 percent, relative to current-law Social Security benefits. Low-wage workers and married couples would be even worse off. According to TCF's report, they could experience overall benefit reductions of up to 38 percent.