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"PROGRESSIVE APPROACHES TO SOCIAL SECURITY REFORM."

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CASSANDRA BUTTS: Welcome. My name is Cassandra Butts. This is the Center for American Progress and welcome to our panel discussion on progressive solutions on Social Security. I am the senior vice president and coordinator for economic policy.

This is the first significant event that we've done this year from the Center for American Progress on a domestic policy issue and it's very appropriate that the focus be on Social Security because with the president's efforts to privatize Social Security there's no doubt that the domestic agenda will be focused on Social Security and that's where the Center for American Progress will be in putting forward progressive ideas and analysis that will serve as a responsible counterpoint to the efforts on the part of the president to privatize Social Security, and the panel discussion here is the beginning of that effort.

In addition, I'd like to point to a publication that we put out that is made available, I think, in your seats or in the packet of information that you have in which the Center for American Progress sponsored an article that's going to appear in the February issue of *The American Prospect*, which explores Britain's experience in privatizing its retirement system and the implications for Social Security.

Without further ado, I will turn it over to our panel, but first let me thank you for coming and thank our panelists for agreeing to participate, and particularly Gene Sperling, who is a senior fellow, who helped me coordinate this effort. And our moderator for the day will be Jason Furman, who is with the Center on Budget and Policy Priorities. And I will turn it over to Jason.

JASON FURMAN: Thank you very much, Cassandra, and I think you framed the issue very well in terms of this is one of the most pressing issues facing the country and it's going to be one of the key legislative debates over the coming months. And there's no one better to begin the panel here than Dr. Dean Baker.

The debate over the next month is going to revolve largely around how serious the Social Security crisis is, with the president and his allies trying to talk up and exaggerate the imminence of that crisis, and there's probably no bigger expert on putting the Social Security crisis into perspective than Dean Baker. He is the author of – or the co-author of *Social Security: The Phony Crisis*, which laid out a lot of the arguments that you see today and, for example, a lead editorial in the *New York Times* and a story by Ed Andrews in the *New York Times*. He's also the co-director of the Center for Economic and Policy Research and a prolific author and researcher on a number of topics, including Social Security.

So, Dr. Baker, if you could (inaudible).

DEAN BAKER: Thanks for the introduction and thanks for organizing this. I appreciate the change to be on the panel here. I also really appreciated Gene's thesis – his piece in the *Times* and the piece I distributed today because I think it begins to reorient our focus towards what really should be at issue. I mean, in principle what we are concerned about is retirement income and Social Security is part of the story. And I'll argue in a second that Social Security is essentially fine. That's the fine – you know, we often talk about the three legs of retirement income and Social Security is the leg that is basically very solid. The other two legs – the pension system and individual savings – are the ones that are in crisis.

And Gene is raising the right question here. If we look at the pension system, defined benefit pension plans are disappearing rapidly and one of the – I shouldn't quite call it a scandal, but one of the things that policy people know about that hasn't gotten into the public debate very much is the Pension Benefit Guarantee Corporation is bankrupt, and I'm not using that term lightly. I think everyone who is familiar with it would agree. And that will need a bail-out, but no one's anxious to talk about that. That would be something worth talking about because that will be tens if not hundreds of billions of dollars when we eventually deal with that.

And then the other part of the pension system is the defined contribution system, and only half workers even have access to defined contribution pension at their workplace and many of those have very little in it, so it's not going to go very far when they get to retirement.

And the third leg, personal savings, as we know, that's not very well developed either. Savings rates – the latest numbers are about 0.4 percent. That will not get us very far in retirement.

The other part of the retirement picture that is worth more attention is, of course, the jobs story because we know that workers are working longer into their lives and one of the things that hasn't gotten as much attention as it deserves in the Bush administration, the bulk of the jobs that have been created since President Bush took office have actually been among workers over age 55, and if you looked at Friday's job report, actually all of the jobs – in fact, more than all of the jobs that were created on Friday went to workers over age 55. So one of the questions – again, we're not going to get to that here, but one of the questions we should be asking is what does the workforce look like for older workers? For better or worse, we're getting a lot of them and that has been neglected.

So, anyhow, I'll leave Gene to talk about the specifics of his proposal and I guess we'll have some back and forth in the discussion, but I do think it's very much a step in the right direction because we do have to talk about how you shore up the other legs of the retirement system, but I'll give my usual spiel about why Social Security is not in crisis.

And, again, I think first and foremost what we need in this discussion is an honest debate because if we have an honest debate, it's not that hard to get to a better situation than we're at today, but if we're having fear-mongering and crisis-mongering, it's very hard to talk about the subject in a serious and productive way.

Let's see if I've mastered the technology. Nope. There we go. Okay.

Okay, several points I'll make. First, the Social Security system is solvent long into the future. Crisis: again, that's a subjective term, but the trustees' report we're looking at 2042; the CBO analysis, 2052. If that's a crisis, the program's been in a crisis for most of its existence because we couldn't look 38 years out into the future in the '60s and the '70s and the '80s. It's a better situation than most.

The shortfall is relatively modest and I'll give you some comparisons. And Social Security taxes pose no threat to the living standards of future generations. This is often put as a generational issue. Fair enough, but the big point I want to make here is there is no story you could tell where our children or grandchildren are going to be in bad shape because they're paying high Social Security taxes. You just can't tell that story.

Privatization doesn't offer a solution. There's no manna from heaven in this story, and I'll go through some of the arithmetic on that. And I do want to at least talk briefly about some of the tricks that we've seen in this debate.

Okay, first off, this is straight from the Social Security trustees' report. What would be the payable benefit if we did nothing? We went to sleep, put the thing on autopilot, don't pay any attention to it whatsoever – you know, not just this year, but forever? We just leave that alone. And the point here is that the benefit rises in real terms. It's wage-indexed, as people are now becoming more aware with the White House debate. It's wage-indexed, so that means it rises through time. We get to 2042 and according to the trustees' projections at that point we don't have enough money to pay full scheduled benefits. Okay?

But, again, what that means is not that everyone's going hungry; there's nothing there; we've exhausted the trust fund. We're relying on the trust fund to pay benefits. They've been accumulating and we're going to continue to accumulate it for the next 16 or next 14 years according to the trustees. We'll be relying on that to pay benefits. In 2042, it's exhausted, but we would still have enough benefits – enough money coming in in taxes to pay a higher benefit than what retirees are getting today on average.

Again, you're welcome to call that a crisis, but the story that, you know, our children and grandchildren – there'll be nothing there for them – well, their nothing will be more than what typical retirees are getting today. Okay? So I'm not advocating that. It would be foolish. We don't want to see that, but the point is the baseline story is very far from a disaster. Okay?

The second point I want to make on this: the GDP growth numbers. There's a big issue on GDP growth. I'm going to indict Alan Greenspan here because this man's been on every side of this debate. Some of you may recall the last time we faced a shortfall in 1982. By that point – by the way, we were literally out of money, so it was like a 2043 situation. We were borrowing the money to make the monthly payments, okay. They didn't have the money in the trust fund to make the monthly payments, so we were literally out of money; so we set up a bipartisan commission chaired by Alan Greenspan.

At that point, they thought they had the program solvent pretty much indefinitely, okay? They didn't do too bad a job because if you go '83 to 2042, that's 59 years and if we take the Congressional Budget Office numbers that's 2052, so 69 years. They didn't do too bad a job, but they thought they had it much further. Now, why were they wrong?

The two biggest reasons they were wrong is, one, that they assumed wage growth would be considerably more rapid than it turned out to be. They thought wages, adjusted for inflation, would grow 2.1 percent a year. Okay, actual growth in the last 20 years has been a little under one percent, so wages have grown less rapidly than the Greenspan Commission thought in '83. Now, it's interesting Alan Greenspan is a great new economy optimist, but he's still not as optimistic as he was back in '83. If he were, we could push this way out – way, way out.

The other part of the story that turned out to be wrong was they didn't anticipate the upward redistribution of wage income. Back in '83, they set the ceiling on taxable income at a point where it covered 90 percent of wage income. Okay, what actually has happened over the last two decades? More and more wage income is going to high-end wage earners: doctors, lawyers, probably a lot of people in this room. And as a result of that it's over the top – it's over the cap. So today only 85 percent of wages are subject to the Social Security tax.

So the main reason that Alan Greenspan was wrong in 1983 about what his fix would do was, first, wage growth was much less rapid than he had projected and it's projected by the trustees to continue to be less rapid, and secondly we've had this big, upward redistribution of wage income that's expected to stay in place. Okay, so it's important.

You know, I sometimes like to say – I mean, I understand we all have to work from the same numbers, but it's not absurd to think that maybe Alan Greenspan was right – maybe we would see more rapid wage growth. And certainly it's something reasonable to hope for. Obviously you don't make your bets based on a best-case outcome, but it's not unreasonable to hope that that might be the case.

Okay, some bases of comparison. The Social Security shortfall – we could pull in a few other numbers here, but I'm actually too pessimistic here. I realized I took this from an old trustees' report. If we took the most recent, instead of being 0.73 percent it would be 0.70 percent, and again let's have a basis of comparison. We increased defense spending by 1 percent of GDP if we go back to 2000 to what we're spending today.

Again, I don't mean – you know, people say that's not small. No, it's not small, but I don't know anyone who says the economy has been destroyed because of the increase in defense spending over the last four years. Again, that's a drain, no doubt about it, but it hasn't been destroyed.

And it's also important to point out if we instead of take the Ss trustees' numbers we take the CBO numbers – they're a little more optimistic, not hugely so – it would just be 0.4 percent. Okay, 0.4 percent of GDP. And some other comparisons we could use: President Bush's tax cuts were about 2 percent of GDP. The portion of tax cuts that went to the richest 2 percent were about 0.8 percent of GDP. So again, none of these are trivial numbers, but the point is we often see much bigger numbers and they don't have us quite shaking in our boots. And, again, we hear numbers often used; I think it's important to put them in some context.

Okay, the next point: we've been here before. Again, you know, you get into these arguments. People want to say it's a crisis – it's not a crisis. And, again, it's – you know, I don't care what people want to call a crisis, but if anyone who wants to call today's situation a crisis – they must think the program has always been in a crisis because we've had to raise taxes before. So, you know, the tax increase – and, again, this is taking the trustees' estimate – if I took the CBO estimate, the shortfall, what we'd have to raise taxes tomorrow to have it balanced over 75 years, would be 1 percent of payroll. So we've seen much bigger tax increases than this in the '80s, in the '70s, in the '60s, in the '50s. Again, no one will ever want to see a tax increase. That's a safe bet. Tax increases are not good. That's true, but the point is we've seen this before, so, again, those people who think it's in a crisis – they must have always thought the program was in a crisis.

Okay, this next point – there was a memo leaked from the White House some of you probably heard about where the author of the memo was wondering what justification (unintelligible) be that 40 years from now retirees would get benefits that are 40 percent higher than current retirees. Well, we could also ask the question, what justification is there that their salaries will be 40 percent higher than current salaries?

We're getting richer. I mean, this is kind of good. You know, that 20, 30, 40 years out from now everyone will be better off and to me it doesn't seem so surprising that we would also want people who are retired 40 years from now to be better off than they are today, but flipping this over there's no story you could tell that our children and grandchildren are going to somehow be bankrupted. They're clearly going to be better off, at least just taking a look at wage growth and the little blip I have down here where this falls in the 40s – what I'm saying here is let's suppose we just pay enough taxes to always pay benefits. Okay, so what happens to wages? These are after-tax wages. Well, they'll fall in '42 because we have to have this big tax increase, but then they start growing again so, you know, they're back up beyond that.

Okay, that's not anyone's ideal scenario, but the point is you can't tell the story that we're going to have – you know our children and grandchildren are going to be bankrupted by Social Security. They're clearly going to live much better off than we do, at least barring some other catastrophe, but Social Security isn't going to be this big burden on them.

Okay, next point – I'll just go over this quickly because Gene I am sure will have a little more to say on this, but one of the points I think is tremendously important when we look at the privatized systems – if we think what Social Security is designed to do, just give a core retirement income, something we want to build on, the great thing though – to my mind one of the great things about Social Security is it's incredibly efficient. I actually looked at this again – I was overly pessimistic. The number there on Social Security should be 0.5 percent, not 0.6 percent. And centralized systems – I'm taking the estimates from the Bush Commission – from their own analysis, and that's I think an optimistic one, but we're given that. It gets to be about 5 percent and then the actual experience where we have systems in place like in England or in Chile, the better ones have costs that are 15 percent – administrative costs that are 15 percent of annual flows.

One more point on that, by the way, there's a lot of deception. I've been on a lot of panels where they go, the administrative costs of the privatized system will just be 30 basis points – 0.3 percent. Okay, I'm often opposite Ph.D. economists who should know the difference between a stop and a flow. Okay, in other words, if I have $100,000 in my account the cost might be 0.3 percent of the stop – the $100,000. The flow on that's going to be something like $6,000 a year, right? That's how much income it will generate, so you've got to compare apples to apples. Okay, so $300 on $6,000 is 5 percent where I come from. So, again, we just have to compare apples to apples and it's a lot of wasted money in my book.

Okay, I'll skip over that one.

Stock returns. I've had a lot of fun with these folks. We need a realistic discussion on this, and it goes beyond just the Social Security debate. But we have this argument that we're going to get – there's this bonanza in the stock market, and I didn't bring it with me, but I have this No Economist Left Behind test. Most of you learned to add two numbers – second grade, third grade. You know, you could add to six, six and half, seven. Most of you – anyone who can't do that here?

Okay, the White House doesn't seem to have anyone who can do that. I don't know why, but they say that they're going to get 6.5 or 7 percent returns on stock. That's in excess of inflation. And I go, "How do you know that?" And they go, "Well, that's what we got in the past." And I go, "Well, if we just apply the past to the future, the fund is solvent. The reason why we're assuming there's a problem is we're assuming growth will be much slower in the future than in the past, so let's derive it. Why don't you just tell me – stock returns are either dividend yields or capital gains. Write it down. I don't care: put down 2 percent dividend yields, 4.5 capital gains. You know, whatever you want. Any mix you want."

Well, no one will ever do that and the reason why they won't do it is because you can't do it. It doesn't make sense. You either have to put down that you're paying out all of your earnings as dividends, which is not plausible, or you have to have capital gains. You have to have stock prices rising more than corporate earnings, which can happen this year, next year, the year after. It can't happen for 30, 40, 50 years. You've got things like price-to-earnings ratios of 200 to 300 to one, and no economist wants to be associated with writing down that they think the price-to-earnings ratio is going to be 300 to one.

So what we need in this is a real debate. We need real numbers and they're scared to give us real numbers. If they gave us real numbers, it would be somewhere around 4.8 percent return on stock, which gets rid of most of the supposed benefit. This isn't even risk-adjusted, by the way. I'm not talking about risk-adjusted. These are just – you know, what is the average return you could expect on stock given current price-to-earnings ratios in the market and projected profit growth?

And it would be a real tragedy if they're just allowed to get through this debate with made-up numbers, so I intend to go around with my No Economist Left Behind test everywhere.

Okay, a couple tricks. I will just run through this quickly. Expressing a shortfall in trillions. We get $10.4 trillion over the infinite horizon, which is rounded up to $11 (trillion). I don't understand that, but anyhow, no one knows what the infinite horizon is. We have exact figures expressed as a share of GDP. Okay, it's about 1 percent. I think it's 1.2 percent of GDP over an infinite horizon if you care about the infinite horizon. I gave you the numbers for 75 years: 0.7 percent in the trustees' report, 0.4 percent according to CBO.

The future ratio of retirees to workers. I don't know how many times I've been with people and go through all the numbers from the trustees' report and they go, "What about the baby-boomers?" So I think, oh, we forgot about them. You know, no. We knew about the baby-boomers. Those are in the numbers, so when they give you that, we knew about them.

Trust fund always with (unintelligible). This is going to be really important in the debate because this is really kind of to my mind just a dishonest trick that we deliberately built up the trust fund. We're taxing people more than is necessary with the idea that beginning now in 2018 we're going to start drawing first on the interest and then on the bonds themselves. The trust fund uses the money to buy government bonds. It's the only thing you can do with it.

Okay, well, to say that 2018 is a crisis – why is that a crisis? This is the way the program was designed. Now, that's a burden on the federal budget, yes. So the people who are very concerned about that should be saying, well, maybe we have to raise taxes; or if you want, cut spending. I don't care, but that has nothing to do with Social Security. Again, this is the law. It's not what Dean Baker thinks. I mean, that's what the law says.

You know, they could go and change the law and say, okay, you know, we're just going to default on those bonds. We're going to tell all the workers of this country, "You stupid suckers. You thought you were paying a Social Security tax and we actually were using that for whatever." You know, they're welcome to do that, but this is what the law says, so I don't see why any serious person should view 2018 as a crisis. If they change the law, then it will be, but as it stands now, 2018 has nothing to do with the program.

Okay, next point: Medicare and Social Security. We have a huge problem with our Medicare system because we have a huge problem with our healthcare system. Healthcare costs are going through the roof. Roughly half of our healthcare costs are picked up through the public sector, primarily Medicare, but also Medicaid. We should be talking about our healthcare system. We're not. But – you know, put in anything with Medicare. Put in roads with Medicare. Put in NASA with Medicare. Yes, that's a real big number, but we're not talking about healthcare. Get Medicare out of the sentence.

Lastly, privatization will allow workers to get higher returns. Again, let's see the numbers. No one will write them down. If they don't know arithmetic, they shouldn't be in the debate.

Okay, in conclusion there are just – you know, again the point is that the program's basically sound and I'll just defer here to Gene. We should be focusing on the larger issue of retirement income. There is a crisis of retirement income. Social Security is the part that's fine. We have to worry about the rest of the system.

So I'll stop there.

MR. FURMAN: Thank you, Dean, for a very helpful presentation.

And now we'll turn next to our panelist Gene Sperling, who is a senior fellow at the Center for American Progress and was one of the chief architects of President Clinton's Saving Social Security First, and was also one of the chief architects of one of the most sweeping and ambitious policy proposals that most of the people in this room have never heard of, and that's universal savings accounts, or USA accounts.

Gene has been tirelessly promoting reforms, including to the tax system and the overall pension system to encourage people to save and to develop accounts outside of Social Security and the debate has swung back entirely his way with just a tremendous amount of demand on Capitol Hill and in the progressive community for exactly these types of ideas and plans.

So, Gene, if you could.

GENE SPERLING: Well, thank you very much. Thank you, Dean, for your presentation, of which I think I agreed with almost all of that. Jason is also – we have a moderator here who is an expert – worked at the White House on Social Security reform, was the economic policy director for Senator Kerry and led much of the Social Security back and forth during the presidential campaign.

I think on behalf of everybody I think one thing we'd probably like to note while we're here discussing Social Security is the recent passing of Congressman Matsui. At his memorial service people understandably talked about his role as the son of a family interned during World War Two and then as a member of Congress being able to provide long compensatory justice for that injustice, but for many of us what we knew Congressman Matsui for was being the lead Democrat on Social Security in the House Ways and Means Committee. He was a wonderful man to work with, highly intelligent. I heard was working on Social Security literally in his last 48, 72 hours of life and I think all of us miss him personally, but we'll also miss his voice in this debate.

With that, let me go to my presentation. While I agree with much of what Dean says, I would like to reframe the discussion in the following way: I don't think what progressives should be asking themselves is whether or not a Social Security crisis exists or doesn't exist. I feel like what we should be asking ourselves is are there challenges in our overall retirement security system, including Social Security, that require a progressive response to help average working families have more economic dignity at retirement and a chance at upward mobility. And I think the answer is definitively yes.

I agree that the long-used three-legged system is a good way to think about retirement security. It's a good reason to think about it because that's how it affects average people. Their economic dignity at retirement is based on a combination of, one, their private savings or home equity; two, their pension – their employer pension; and three, their Social Security. So it is good when you're asking how these things affect people to look at all three of them together.

Now, I think – when it comes to Social Security, I think that there is a long-term demographic challenge. There is not, as Dean has powerfully showed, some kind of crisis that requires radical restructuring. That part is an exaggeration and a deception at best. On the other hand, with any long-term challenge, it's better to act earlier than later. If we can find a responsible way to act earlier, we should engage in that exercise if it's responsibly done.

Now, in looking at these three legs of the retirement stool, it is worth noting that the private savings and employer pension have lots of risk involved in that. We just saw people – sad, terrible stories of people who lost their pensions because they were overly concentrated in the market or NASDAQ or a particular company. We've seen families – seen their housing equity go down at the wrong time as they're retiring. They already have significant market risk in these areas.

What's special about Social Security is that it's the one leg that is risk-free and guaranteed, so the question is not should we try to have more people engage in investment and wealth creation. We should. The question that the White House and conservatives have never been able to answer is why does one have to inject that degree of risk into the one part of the three-legged stool that is risk-free? So I believe if we can engage in a responsible exercise to act earlier, to increase savings, to keep Social Security solvent as we know it, we should engage.

Secondly, on the private – on the other two retirement legs, we do have a serious problem. We have a Swiss cheese retirement savings system. If you are as fortunate as I have been in the last 10 years, I have been in jobs for 10, 12 years now where I get money automatically taken out of my paycheck, I get an automatic match from my employer. It is a terrific system – terrific. The more automatic it is, the better it is. The greater the match, the better it is. But it is a Swiss cheese system. For people in the top 20 percent, four out of five have no employer-provided pension. Seventy-three percent of employees of small business have no employer-provided pension; 75 percent of Hispanics, 60 percent of African-Americans.

This is a Swiss cheese system in which the holes are greater than the cheese and the people being hurt and left out are the people progressives should be trying to address. The median pension savings – market savings for somebody 55 to 59 in our country is a whopping $10,400. That cannot be considered adequate.

Now, while I'm much harsher on the White House and conservatives, I don't think either side of the political spectrum has done very well in addressing this retirement security issue. On the conservative side, we have seen this focus on private accounts – partial privatization of Social Security.

Now, one thing that has come out more, even in the White House memo, even from Senator Lindsey Graham of South Carolina is a greater understanding that private accounts really in and of themselves do virtually nothing to help fix the one leg of the retirement stool, Social Security. What we're seeing, whether it's in model two of the president's Social Security plan, is that it's the benefit cuts for the president or privatizers' plans that fix Social Security solvency. It's benefit cuts. It's not the private accounts themselves. The Congressional Budget Office actually found the private accounts, because of the transaction costs Peter talked about, actually hurts solvency.

What's even less discussed, though, is the (data?). Those who support these private accounts within Social Security have never even made a case as to why it increases private savings. It is an assertion. I don't understand even the mechanism. Perhaps they will give us an explanation, but there is at this point no design that explains why it's going to strengthen the second or third stool of the retirement stool – the second or third leg of the retirement stool. I do believe with them that having people have more individual savings can get people more into the culture of savings and wealth creation. That I support, but I've never seen an explanation as to why it should be inside Social Security.

And it leaves progressives and Democrats with the following sneaky suspicion, which becomes more and more confirmed every day, which is that the goal is neither to fix Social Security or to fix the second or third leg of the retirement stool. The goal is an ideological one to start a slippery slope to undermining the broad-based political support for Social Security. And there is no reason for progressives to engage in that exercise.

Now, on the other hand, progressives how have done a good job at times of defending why we need a defined, guaranteed benefit structure in Social Security have been largely missing in action on addressing the need for wealth creation and private savings and greater pension retirement savings for typical working families. We spend more time criticizing what's wrong with the Republican privatization plan than coming up with our own agenda, and the goal is not to come up with an agenda for political posturing. The reason we should have a powerful response to savings is because it's a real problem – because, as I said, there's something wrong when 75, 80 percent of lower-income workers aren't engaging in savings. Why are we not looking out for their savings, their wealth creation, their employer-provided pensions? We should have our own solution not as a response, but because it's the right thing policy-wise.

So what I put forward in this paper that we're releasing today is really a framework for engagement for Democrats and progressives. The framework for engagement says we should go forward if we can achieve the following three things: if we actually are increasing national savings and generational responsibility; two, if we are truly seeking to responsibly take early, reasonable steps to fix Social Security in a way that increases savings and has mutual sacrifice and fair sacrifice among the population; and three, if we are actually outside of Social Security, but as part of a retirement security compromise doing something meaningful about helping people save and create wealth who are now falling through the cracks.

Let me go through these three parts of my framework hopefully somewhat quickly. Number one, increasing generational responsibility and national savings. You know, in the 1990s you could have a debate like this and the one thing everybody would agree on was the following: the goal of acting early was so that this generation would consume a little less and save more so there'd be greater productivity and less debt to the next generation. Everybody agreed that you needed to increase savings as you got closer to the baby-boom retirement years of 2008. And something happened to that consensus and it was the election of 2000.

President Bush not only didn't move forward don this notion of increasing savings, we took two giant – three giant steps backwards. We actually passed consumption-oriented tax cuts in the face of higher terrorism and defense costs that actually created a hole three times as large as the initial Social Security problem. And this is – you know, Dean mentioned this and Peter Orszag and Bob Greenstein have published quite a bit on this, but the size of the tax cut was three times larger over time than the hole in Social Security solvency. The tax cut for the top 1 percent alone was larger, by the CBO analysis, than one would have needed to completely fix Social Security.

Now, does that mean we shouldn't have given any middle-class tax cuts? No. I think we should have given some middle-class tax cuts. Does that mean we should do it all this way? Not necessarily. But the notion that we could afford all of that, but that the only way to fix Social Security was a radical restructuring is a clear deception based on these numbers.

And it also was a break with consensus on national savings. In the Clinton years, net national savings almost doubled from 3.1 to 5.9 percent. Now, question: how much of the increase in national savings was due to an improvement in our fiscal situation? The answer is 100 percent. Now, what's happened since President Bush got in office? If you look at the last seven quarters – so I'm not just picking on one quarter – you'd get an average of around 1.4 percent. That's the lowest seven-quarter average in net national savings since 1934.

Now, what's remarkable to me is that when people are judging the conservative plans they say, well, look at this plan. It does nothing on net – bad on national savings for 20, 30 years and it actually cuts some benefits in the future. They say that's the new gold standard. Look, that's responsible. Well, all that is doing is locking in the harm that's already been done. It's keeping us two steps backwards and I have to point out: doing nothing on national savings is not generationally responsible. If I'm a college president and I know our buildings are going to deteriorate two decades from now and I send a memo to the next president saying, "You ought to do something about this two decades from now," that's not really being generationally responsible. Plans that simply tell the next generation how to cut benefits does not increase our pool of national savings. This is the bigotry of low expectations. How low the gold standard has become.

Second, if we're engaging in Social Security reform, if you accept my view that we should be willing to engage in this effort if it is done responsibly and protects the guaranteed benefit of Social Security as we know it, we as progressives should ask for some sense of mutual sacrifice. Now, I think that in our country if a member of Congress goes home and says, "We have no choice but to do some kind of painful measure for our national security," Americans will support it. I believe if people go home and say, "We have absolutely no choice but to even take some tough measures on Social Security because it's the only way we can keep it solvent," I believe the public could support it.

Now, let me ask you this. How could a member of Congress go home to a town meeting like this and say, "We have no choice but to cut your benefits. We just cannot fix Ss any other way than by changing it to price-indexing so that instead of getting 36 percent of your current earnings in retirement you'll only get 20 percent. Imagine what that would be now, but we have no choice to do that." What would you say to the first person in the audience who put up their hand and said, "Well, let me get this right. You just gave a tax cut to people making over $300,000 that would have been large enough to not have to cut any of our benefits at all, so it's not that we have to do this. You've made a policy choice – a value choice. You would rather take a certain amount of funds and direct it to the top 1 percent and pay for that, essentially, by letting our benefits be cut. Or, to put it another way, leave no choice but for our now benefits to be cut."

Nobody could possibly answer that person in a town-hall meeting. What could they say? Now, I think for that reason there are a lot of progressives who are saying we ought to fix Social Security entirely by repealing the tax cut for the top 1 percent. Why should we cut anyone's benefits? I think that there is a reasonable case to be made for that, but I also believe that any Social Security progress requires a degree of bipartisan compromise, so I think it's reasonable for progressives – for us to say we don't want to fix all of Social Security by simply repealing the tax cut for the top 1 percent, but we cannot go to our town meeting and ask for sacrifice unless we could show it was fair.

And the fair way that I have suggested in this paper is that we have a 3 percent surcharge on all income over $200,000. A 3 percent surcharge on all income over $200,000 whether it's divided, capital, or wage income. Now, this would affect perhaps 1.5 to 2 percent of Americans. It would cause no distortions in people doing tax strategies to avoid paying wage income as opposed to capital income. And this alone could fix 60 to 70 percent of the solvency gap under Social Security.

Now, people talk about increasing the wage cap and I think that's a policy that should be in the mix and I think it's good and I compliment Republican Senator Lindsey Graham for putting that proposal forward, but I will say that this is a more fair way to get that amount of contribution from the most well off because it does not hit, for example, a self0employed worker with a 12.4 percent additional tax on income up to $130,000 to $140,000, so while I think that should still be part of the mix, I think if one was looking for a primary effort that this would be a very strong one.

Now, what President Bush could do, which would be reasonable under our current situation, is to say, "I'm willing to put this on the table if Democrats are willing to sit down and come up with a comparable amount of savings on the other side." I think if the president was willing to put forward this type of compromise to fix Social Security without privatization, then it would be responsible for Democrats to engage in fixing the rest of the hole through the more traditional measures, hopefully in a progressive fashion.

So that would be the second framework: that I would have asked for a threshold of mutual sacrifice before we engage. Otherwise, I simply do not know how we defend it to our workers.

Finally, as Jason said, I have been long supporting President Clinton's USA account. I worked on that. I worked on – Vice President Gore had a similar proposal. Jason and I worked on that together. But I have called this proposal the universal 401(k) and I think that is the right name for it because I do think, as we said, that the 401(k)s at their best are truly an American success story and we should recognize that matching funds work. We should recognize that having automatic deductions taken out of your paycheck work and we should ask how to spread things broader.

But here is the problem. One, I just went through how big the holes were, but we have another problem, too. Our progressive tax system gets turned on its head when it comes to retirement savings. We only have one way of encouraging retirement savings in our country: tax deductibility. Think about what that means. If you're in the 35 percent bracket and you basically don't need an incentive to save, whenever you put forward a dollar, you get a 35 percent deduction from the government. You get 35 cents on the dollar, even though you don't need much of an incentive to save, even though you have various opportunities, and even though you probably have a matching 401(k) at work.

Somebody in the 15 percent bracket is unlikely to have any employer-provided pension, any matching funds, and when they invest what do they get? Fifteen percent. Now, I used to say that if you put this system on an SAT test and you said, what is the logical rule that this must follow, the only possible right answer would be that our system says that the easier it is for you to save, the more we help you. The harder it is for you to save, the less we help you. So if we want to get serious about savings, we should be looking for a way of strengthening the second and third legs with a universal 401(k) that fills the hole and turns this upside-down system right side up.

Here's what the components – and I'll not go into every detail so that we can get to questions and answers. One, turn it right side up by having a progressive refundable tax credit, meaning people in the lowest part of the income bracket have the hardest time saving. They need the greatest incentive. But here's the good news: when you get them to save, you actually increase national savings. When you give tax incentives to well off people what studies show is they just shift their existing savings around. It's a windfall that does not increase savings. When you leverage people in the bottom 40 or 50 percent to save, you actually not only fulfill the progressive goal of helping more people have wealth and savings, you also increase net national savings.

I believe we should have a two to one match so that for up to the beginning of $2,000 account. And what I mean by that is that a lower-income person could put $667 into an account and get the rest matched so they have $2,000. When you move up into more moderate incomes, it could be a dollar to dollar match.

Then, for everyone else what we could at least have is a flat tax incentive. In other words, why not have a 30 percent refundable credit for everybody when they save? Why should a CEO get the 35 percent deduction, but the person who cleans their office may not have enough income to get any incentive? Why not even beyond the progressive match say that when they save they each get the same thing?

People talk about a flat tax. Well, I'm proposing here a flat tax incentive for retirement savings. Let's at least do that. That would help – mean that when people in the 15 percent bracket even went beyond what they could match they could get a 30 percent credit instead of 15 percent. That would double their savings.

Next, it should be – it would be portable and continuous. Right now what happens is when people, particularly women often, come home to save, they lose their retirement system, they lose an incentive to save, they don't have income, they don't have a progressive match. A universal 401(k) would be family friendly. It would be working parent stay-at-home friendly because it would continue to give a matching incentive to save even while you are caring for your child.

Also, we could put many of the things that many people have been promoting to make things more automatic. Do provisions to increase to increase automatic, the default being that you put a contribution into your universal 401(k) unless you decide otherwise. Split refunds – allow people to split part of their tax cut and send it into the universal 401(k) and design it so it works with the employer system and actually makes it easier for people to make their nondiscrimination rules so it doesn't encourage matching.

And finally, just how I would pay for this. If we took the estate tax and let it go from $3 million a couple to $5 or $7 million a couple, what – let's make sure we understand what that means. That means that on your first $5 to $7 million of your estate, you pay zero taxes. Zero – not a penny. That's 99.7 percent of all estates. If you just went that far and didn't repeal, you could use the money to fund a very generous universal 401(k) account. Even if you were – the universal 401(k) were able to help just 50 million Americans save more – 50 million more – because this would only affect 10,000 estates, what's the ratio of tax cuts? There would be 5,000 people who would get refundable tax cuts to save under the universal 401(k) for every one estate that would see higher taxes above $7 million. So I have to say, even if you're a tax cutter, isn't a 5,000 to one ratio a pretty good ratio and isn't the idea of letting more people have a chance to someday create wealth and have their own estate worth keeping some taxes on the most well off estates?

This plan together, because it uses the estate tax, because it leverages in private savings through the universal 401(k), because of the 3 percent surcharge would increase net national savings now. It could fix Social Security and it could be a bold step forward to make sure all Americans have a universal 401(k) to create wealth and have retirement savings.

Thank you.

MR. FURMAN: Thank you very much, Gene. I thought that was – and Dean, I thought those were both very helpful presentations in terms of both putting a perspective on the challenges that we face and describing some of the responses to them.

Before opening it up to questions, I did want to take advantage of being the moderator to put one or two other progressive plans that are floating around and have been proposed pretty seriously on the table so that people can consider those and include them in part of the discussion.

But before doing that, just to briefly put a little bit of my own at least take on the problem and the challenges that we face here, I think there is two real challenges. The first is the macroeconomic challenge that the United States has one of the lowest savings rates of any advanced industrial economy. What that means is we have less money for investment and economic growth. We're forced to rely on foreign capital, which carries with it an associated risk that you have a hard landing as well as the fact that you eventually need to repay it.

And that this problem with our national savings is only projected to get worse and worse because one of the reasons that we have such low net national savings is we have a very large budget deficit and the budget deficit is only going to grow over time as we go through the demographic changes. That's not primarily a Social Security problem, but Social Security is one of the elements; not anywhere near the top two or three elements, but one of the elements of that story.

The second challenge we face is one that Dean talked about and Gene outlined I think an excellent solution to – is what savings is like at what I would say the microeconomic level or the individual level where people retire and are forced to see a dramatic decline in their standard of livings because Social Security replaces only 42 percent of your income that you earned during life and that percentage is expected to fall, and that people don't save enough to make up the difference in terms of what they need to live in retirement with the same sort of dignity and standard of living that they had during life.

And I think ideally we want something that is going to help us address both of these challenges; both what national savings means at a macroeconomic level for the United States and what it means at a microeconomic level for families.

Individual accounts, for a lot of reasons that Dean and Gene have alluded to, aren't really going to help you solve that problem. The encouraging individual savings in the way Gene talks about will help you solve both of those problems. I wanted to talk about what one might want to consider and just put it down on the table for discussion, not personally endorsing it in any way. Another component of that solution, which is reforming Social Security itself to solve what is certainly a challenge in terms of dealing with the demographic changes we're going to have in terms of the baby-boom, longer life expectancies, and falling fertility.

The first plan I just wanted to throw out for consideration is one from Peter Diamond and Peter Orszag – a professor at MIT – and Peter Orszag at the Brookings Institution. They have a plan that makes a modest set of adjustments to Social Security benefits and Social Security taxes to bring the system into long-term balance. Their plan matches the same goal that the president has put forward of putting the system in balance over an infinite horizon. They do that with a number of changes, first of all to reflect the fact that people live longer and a result collect more in benefits today than when the system was first established.

They pay for that longer life expectancy by a combination of a modest reduction in benefits so that your benefit will stay the same when you add in the extra years as the sort of present value of it stays the same, and a modest increase in taxes. To reflect the increased earnings inequality and the effect that has had on the Social Security system, where an increasing amount of payroll taxes have gone uncollected because they're earned above the threshold, which is about $90,000 a year, they would raise the taxable maximum so that it covers the historical value of 90 percent of earnings. And finally, they would address the legacy debt in the Social Security system with an additional 3 percent surtax on people above the taxable maximum.

If you take this plan together – just to give you a perspective on what one thing you could do is – anyone 55 and older would see no change in benefits. For a 45-year-old you would see an average a 1 percent reduction in benefits; slightly larger for upper-income 45-year-olds. For a 25-year-old you'd see a 9 percent reduction in benefits. Those are important numbers to have in your head when you compare them to something like the shift to price index and what you see in the president's proposal, which would cut benefits by 25 percent growing to 40 percent. The reason that those large benefit cuts are necessary in the president's proposal is that he needs to pay not just for fixing Social Security but also needs to pay for his individual accounts, and that's why he's proposing such more dramatic cuts in guaranteed benefits. The plan would also have a modest increase in payroll taxes.

That's one plan I wanted to put on the table. The second one is one that former Social Security Commissioner Bob Ball, who was a commissioner under Democratic and Republican administrations, has put forward, and it was introduced by Congressman Obey. This plan would not solve Social Security over an infinite horizon, but what an argument is is that we only have voters who are age 18 and older today. They shouldn't be making choices for every generation in the future today. Each generation can make its own set of choices. So an argument for this would be you solve the system, add a number of decades to the life of Social Security, and let the next generation figure out what the next steps it wants to take – how it wants to balance revenues, benefits, and the other changes you could make.

What the Obey-Ball plan would do is, first of all, keep the estate tax at $7 million a couple in 2009 and maintain it at that level. The vast majority of people would see their estate taxes eliminated under that, but the remaining revenue would be enough to solve anywhere from one quarter to one half of the Society Security problem, depending on whose estimates you're looking at. Second of all they would raise the taxable maximum in the same way that we described before: gradually so that eventually it covers 90 percent of earnings. That, again, is enough to solve between one half and one third of the Social Security problem.

And finally, they would implement some fixes in the way that the consumer price index is calculated to – and Dean has opinions on this issue as well – to fix what many people see as one of the biases in the way the CPI is calculated. That would result in slightly slower growth and benefits after retirement but they would still match the goal of keeping up with inflation, properly measured, if you take that perspective. Taken together on CBO scoring, the Ball-Obey plan would fully solve Social Security's problems for the next 75 years, and on the actuary's estimates, which are a little bit more pessimistic, it would solve about two-thirds of the problem.

These are two of the leading sort of purely Social Security plans that are out there, and the argument for undertaking either of them today rather than waiting would be two things. A more minor argument is it would help people plan for their future and plan for their retirement if they knew that their benefits were going to be like in the future. If anything, people might actually be surprised to learn that they only need a 9 percent benefit cut after so much time and effort has gone into persuading them that they're not going to get any benefit at all.

Second of all is the – to go back to the very beginning point – is national savings. Anything we can do to reduce government expenditures or raise government revenues, whether it's through the Social Security system or outside the Social Security system or linked to the Social Security system; like using this as the most politically feasible way to restore the estate tax and keep it in place. Any of those would start to raise national savings today, start to increase the capital stock today, and put us in a better position a generation from now because you will have those fewer workers but they're going to have more machines to produce more products to support the larger number of retirees.

With that I wanted to open it up to questions. We would like to first take questions from anyone from the press who is here – if there is anyone. And there is a traveling microphone. And if you could also please identify yourself.

Q: Yes, I'm Jason Ross. I'm here with EIR, Executive Intelligence Review, and Lyndon LaRouche. One of the things that I'm not sure was addressed is the urgency that Bush feels in pushing through the Social Security privatization plan so soon after a hotly contested election, so adamantly after the challenge on Thursday. One of the things that I think needs addressing – and Mr. LaRouche does as well – is that the folks around Bush, like Schultz, the sort of (unintelligible) behind the scenes, need the cash from Social Security very urgently to prop up the financial system that's seeing words like "Armageddon," "gigantic crisis" – you're seeing these things in the *Economist* and publications all around the world.

Now, what he's proposing is that you use this to go for Bush's jugular instead of compromising or looking for a way to get along with them. Attack Bush on the fact that he's promoting Chile's Pinochet plan for Social Security, that he's going to let elderly people die with huge benefit reductions rather than pay back the IOUs that are due in 2018. So I was wondering what you think about using this issue rather than how can we compromise and get along but using it to absolutely attack and destroy the Bush administration.

MR. BAKER: I think the Bush administration has been incredibly dishonest, obviously, in the whole debate. I mean, they're claiming a crisis in Social Security. There isn't any one – any crisis by any normal use of the term "crisis." We do have very serious problems with our economy. It's hard for me to see how Social Security privatization would fix that. So let's say, you know, he got his wish tomorrow and he got through Congress his plan, suddenly our budget deficit goes up on the order of $150 billion a year, and frankly – I was just in Philadelphia at the American Economic

Association – the only people in the world who thinks that that is okay because you'll pay it back in 50 years were there, you know. (Laughter.) No one else thinks that makes sense that we wrote down we're going to cut benefits in 2040 so that's okay that we're borrowing, you know, another $150 this year, next year, and the next decade.

So it's hard for me to see how Social Security privatization would alleviate the problems that you're facing with the dollar falling, with inadequate savings in the economy – I'll go on – the housing bubble. I mean, you have lots of serious economic problems right now. To my mind, Social Security privatization probably makes those worse. I don't see how it makes it better.

MR. SPERLING: Look, I don't think one should look at this as trying to compromise or get along or any of – you know, should start ever with that political posture, and I think the right thing to do at the start is ask, what do people who feel the government should help every American – lower, moderate-income – have a fair chance to have economic dignity and create wealth creation – what do we think would make progress? What I've tried to do essentially is lay out what I think is a constructive framework for engagement. It's not for the purpose of getting along; it's for the purpose of helping typical Americans to have more economic dignity and wealth and savings in their life.

If the Republicans want to engage in that kind of responsible exercise, I think it makes sense to go forward. And I think whenever you're in that situation you always have to figure out at what point does your compromise move the ball backwards as opposed to forward? But my feeling is one is going – you know, I'm putting this forward because this is what I think would be good for the country; this is what I think would be good for helping Americans because I feel that the fact that we have this upside-down savings incentive system is scandalous. Look, I've lived it. You know, I get to make a little bit more money now; I get to see all the benefits of all the different bankers coming to you with all the different prospects and I know what it's like to make $10,000 – $12,000 a year and it's just really this upside-down system. The better off you are in this country, the more we throw every different type of incentive and windfall to help you accumulate even more and more, and the lower income you are, the more you need help saving because you're living paycheck by paycheck, the less we do for you. I think we ought to try to fix that if we can. We should do it because it's the right thing to do.

MR. FURMAN: Are there any other questions from the press? Yes, if you could also please identify yourself?

Q: (Off mike.)

MR. FURMAN: Ma'am, could you wait for the mike?

Q: Gene, you make the assertion that the real agenda of the Bush administration here with the idea of privatization is an ideological one aimed at undermining the broad base of public support for the entire Social Security program. Could you be a little more explicit as to precisely how it would do that?

MR. SPERLING: Yeah, sure. Well, in a sense, the framework that I'm putting forward is an effort to take them at their word. In other words, if they are interested in protecting Social Security and having it be the guaranteed benefit that it's been for generation after generation, and if they're interested in increasing individual ownership and having more savings and wealth creation, then I tried to put forward a framework that would allow progressives and conservatives, Democrats and Republicans, to come together.

What I don't think that they have done is that they have never made a case for why private accounts in Social Security achieve either of those goals. Now, if somebody is doing something and it doesn't fulfill either of their stated objectives, it's reasonable to ask, what is the true motivation? If the true motivation is to have individual accounts and greater individual savings, then let's sit down and do something tremendous for the American people. That can happen now.

But why right now – why are they – when they could sit down – my guess is Nancy Pelosi and Harry Reid would be very happy to come sit down with President Bush today and talk about a bold, progressive saving account that gives progressive match for low-income Americans. The question is why instead are we gearing up for this divisive fight? Why do you have to divide Washington by carving up Social Security? I don't think they've made that case. Again, if you're look even at the White House memo, what does it say? Individual accounts alone – look, what individual accounts alone do is it adds risk to your portfolio. You could end up worse; you could end up better. CBO says if you adjust for risk you'll end up just the same.

So what's the reason there? All it does is really add high transaction costs, tremendous confusion. You know, somebody who retires in '99 versus 2001 gets higher benefits or lower benefits – all this complication, and what is the reason for it? It doesn't increase national savings as they've designed it. If you're taking – you have 12.4 percent payroll tax, right? And they take – well, now we'll take 3 percent and move it to a different account. You still have 12.4 percent, so where is it increasing savings? I don't see it increasing savings. I see, if anything, we're talking about borrowing and having high transaction costs.

So I think that – you know, I once had a conversation with a Republican senator who asked me why Democrats were so opposed and I said, "I think that a lot of them feel that even though it's just a couple of percent, that the idea is to make that so attractive that people want to break away from the compact of Social Security and go to a system where savings is totally based not on progressive social insurance but all on individual choice, every saver for themselves so to speak."

And this particular senator, reflecting, said, "Well, there's no question that is the motivation behind a lot of the people doing it." Now, I'm not saying that they necessarily have ill will; that's just their view, but I do believe that Social Security has been a progressive compact for all of these years and it has been an American success story. It has incredibly low administrative costs, dramatic reduction in poverty, tremendous public support. It's a progressive program that helps poor people that has broad support from the middle class, and I think that some people perhaps would like to start a slippery slope to unravel that.

But what I'm saying, Karen, is if that's not true; if the goal really is increasing national savings, number one; two, increasing individual ownership; and three, saving Social Security benefits, then what I've tried to do is provide a structure that actually takes them at their word and says we can get this done. And I think the real question to them is why are they not saying yes to this? Why are they insisting on this divisive fight when they could do something bold by working on a universal 401(k) with Democrats.

MR. BAKER: If I could throw in a couple more points to Gene's in terms of why I think there's a very good case that (closed?) ideology is the motivation here, at least a good chunk of it. If you look at the design of plan two, you actually have a subsidy for people who choose the private accounts, you know, so one could say, okay, good; you want a private account, go ahead. Why should all of us here have to subsidize those people who want to get a private account if those people just want a guaranteed benefit? You're not doing me a favor. So why do you have the subsidy in there?

Secondly, the way to structure the clawback is – you know, the idea is, okay, you're going to put your money in the private account; you just don't walk off with your benefit and your private account. Well, the original proposal, if you go back to what Martin Feldstein was talking about a few years back, you paid back 75 percent of your account. Now you're not paying back your account; it comes out of your guaranteed benefit. So if you carry that out 40 or 50 years, a typical worker, their replacement from their guaranteed benefit is going to be about 10 percent of their wage. They're not going to care about that. So you're going to create a situation where once you get out 30, 40, 50 years the guaranteed benefit looks like a joke for your typical worker. The only people that need that are those at the bottom end.

So you've very successfully fractured this idea that you have a system that is providing a core retirement income for the bulk of the workforce, and that's totally the design of the system. You can still have the accounts and not have that structure.

MR. FURMAN: Great. Any more questions from the press?

If I could just ask the first question and then I'll open it up, which is, you've both talked a little bit about the mathematics and the theory of individual accounts and those types of Social Security reform. I just wanted to ask – and I don't know if you've had the chance to read yet this excellent article in *The American Prospect* that the Center for American Progress commissioned by Norma Cohen, which describes a lot of the experience in the UK in which a partial privatization there has turned out, pretty much from almost everyone's perspective, much more disastrously than expected in terms of the complications, the administrative costs, the confusion, and the falling stock market.

So I just wanted to ask you, since this isn't entirely uncharted territory for the United States to be going into, what you think we can learn from international experience in this area.

MR. BAKER: Well, at this point there's a lot of international experience. England we tend to look to because obviously it's a country a fair bit like the United States but also throughout the developing world – Chile the example that's been most often mentioned. But you've had similar problems just about everywhere. You have very high administrative fees. I was being extremely generous when I said that the administrative fees on a privatized system would be 5 percent of annual payouts because that's taking the commission's estimate at their word and they might be able to achieve that. It's not impossible. That's a centralized system, you know, one size fits all, government, that sort of thing – all the bad things that they say about Social Security. You get 5 percent. But if you look at the history in England and Chile and other countries, it's been 15, 20 percent, sometimes as high as 30 percent in some of the less successful models. So you're adding a lot in terms of administrative costs.

It is complicated. It's one of these things – again, you know, from my mind I don't think I have to – and again, I'm an economist; I don't think that I want to tell a single mother when she comes home the most important thing for her to do is to look at her savings account and figure out what to do with that. Everyone should have that option, and I'm 100 percent with Gene: we should make that as easy as possible. But what you have is people don't often want to do that and that's fine and that's the great thing about Social Security. And what you had in England was you had a lot of people selling essentially bogus policies. The government had to bail out a lot of insurance companies that were making promises they couldn't keep.

So, again, for your core retirement income it seems to me to make a lot of sense to have something that's really simple, no effort, you don't have to do anything with it, like Social Security. Beyond that, yes, we have to worry about savings mechanisms. On top of that, again, both the experience of England and Chile and the other countries we could look to is that they don't, in general, provide an adequate retirement income. And in England there is just a study from the a government commission evaluating their program, saying, you know, things are okay now but when we carry this out 20, 25 years, retirees are not going to have enough money. And again, you're going to come back and probably there will be a lot of pressure on the government. Who knows what England's government – I don't know where our government will be in 20, 25 years, but there will be a lot of pressure on them to raise benefits, which again is probably the point I was making earlier with the Bush administration with their transition costs. They'll write something down today, and maybe they really do want to cut benefits for people 30, 40 years out – that's entirely plausible, but thankfully he won't be in office at that point. Maybe it'll be his daughter or granddaughter, I don't know.

But in any case, if you have a large population of retirees, which you will, and they don't have enough money to make ends meet, there will be, obviously, a lot of pressure on whoever is in power at that point to raise benefits. No matter what we put down there today, they aren't going to care.

MR. SPERLING: I think that one of the most important lessons is the transaction costs issue – perhaps the most boring phrase you could say. But I think – when we were working in the White House I think every once in a while you'd see something that really opens your eyes, and I think the notion that when you're talking about transaction costs and they seem like a 70 basis point or 1 percent, it doesn't seem a huge amount. And this is probably a problem even with the way many IRAs, et cetera, are managed today. When people know that over a 40-year period they can actually lose 20, 25, 30 percent of their benefit to transaction costs, that's rather remarkable, and I think if somebody went out and said, here's a new individual account for Social Security, and by the way we're going to do a 25 percent tax and send it all to well-off employees in the financial sector, that would not be very popular. But that is what individual accounts have meant in England and in Chile.

Now, the interesting thing – and this goes to the point Karen is asking, which I think is interesting – is what happens a bit is that whenever you raise these concerns about individual accounts, people reply in ways that move the idea further and further away from the way it's marketed. So what they say is, "Well, you know, we wouldn't actually let you make lots of choices in your individual account; you would just get a few broad index funds." Well, that makes good sense to me, but then again, what about the old individual choice and you own it? You own it but you can only do a certain amount of things with it? And I said, "Well, what about people who retire when the market's gone down?" "Well, maybe we can tax back 70 or 80 percent of it and create a pool of savings." I think, well, so the government is going to take money from good years and bad years and pool it together? Well, gee, that's kind of what Social Security does right now. (Laughter.)

So you get this thing where you go out and you market and then as you raise it they bring it back and make it so close to Social Security. My favorite is – which, again, I don't think is a terrible idea if you were going to do this – have it be a thrift savings plan with the government. That's good. Now, of course that means we add probably 10,000 workers just to answer the phone. But, so, you know, suddenly a proposal that's supposed to be individual accounts, individual choice ownership, to answer its critics on transaction costs, et cetera, ends up having large restrictions the Congress or somebody has to vote on subject to political interference; might be managed by a large government bureaucracy that would take lots of new people and have higher administrative costs, and it does start raising the issue of what is the point?

Now, the only positive thing I do want to say on the international experience is that when we were in the White House I believed very much in an open-door policy, and that meant that I had many people from Cato and Heritage and others come in, and one of the favorite guests to bring with me was Mr. Piñera, who was the creator of the Chile system. And the one thing he used to say is, "When people get their little book and they look and they really get into savings." And that's where I agree with the people who push private accounts. That's where I agree with them. I see it myself. It's true; when you get a 401(k) or something you do look at the statement, you do learn about the market, you do learn about the magic of compound interest. It just – once again, I can't understand why we think – we have been led to believe – that the only way we can achieve that is through carving up Social Security with this complicated, expensive privatization proposal.

So, yes, I think there are some benefits we've seen, and the lesson is actually there are benefits and they're best done outside of Social Security, not within it.

MR. FURMAN: One name for transaction costs is windfall revenues for financial institutions (laughter) or salaries for the tens of thousands of civil servants you need to hire to administer these.

But with that I'll open it up to you. If you could just identify yourself and wait for the microphone.

Q: Hi, my name is Arthur Morton and I'm a former senior economist for the Bureau of Economic Analysis, worked on the GDP, on the national defense portion of it.

And one of the issues that not too many people I think are aware of is that Congress gave the military billions of dollars worth of tax credits – FICA credits – from 1940 through 1957: $160 per month per person from the private all the way to the five-star general. Also, more recently, as late as 2001, they were still giving away FICA credits. These are obligations against the accounts. What it turns out to be is that the middle class, the working poor, have to pay this because the rich do not pay their share of it.

The other is that the Philippines were also included in that after Second World War because they were American territories, and if you go on the website for Social Security you'll find this.

One of the other things, when I was working on the national defense portion in the early '80s, DOD deferred their employer contributions until the employee – until the actual military retiree gained benefits. And so this was a large amount of money. I'm not sure if that's ever been fully paid for.

The last thing I just wanted to say is that it seems like the cap on FICA should be just eliminated. It would be a much fairer system. I think if we looked at a flat tax for income and said, well, okay, we'll cap it at $90,000, I think a lot of people would be really excited about that. I think we really need to take that cap off. I think it would make a much fairer system.

Thank you.

MR. SPERLING: Well, that was interesting information. I just would say in response to taking the cap off, and the idea is that the payroll tax would apply to higher income, we did do that in the Clinton administration for the 1.45 percent that goes on Medicare. I'm a little more – I think it makes sense as part of an overall deal to somewhat increase it, but I'm not sure, again, if that's the most fair way to ask for a greater contribution from the most well off, particularly in light of the most recent tax cut. And I worry that people would engage in all sorts of efforts to shift their income to dividend or capital gains to avoid it.

So that's why, in my proposal we asked for a 3 percent surcharge or tax on income over $200,000 regardless. It raises a significant amount but it's all income and doesn't lead to distortions. So that's just why I prefer that as the main way of doing that.

And if I can just deviate for one second I just wanted to – I didn't want this to end without thanking a young and an old person. The young person is Brian Deese, who did excellent work at the Center for American Progress on this report, and the older person is Bob Ball, whose plan was mentioned, who I talked to in response to this, and he was considering being a panelist. He is 90 years old and when I got off the phone with him I thought, you know, my aspiration is to, at some point in my life, have the clarity of thought that he has when he's 90.

MR. BAKER: Yeah, I'll second that on Bob Ball. I've also gotten a lot from my conversations with him over the years. Just a couple of quick points on that. One of the things – again, these are specifics, which – details you know much better than I do, but one of the things I have done over the years is clean up some of the mess so – part of the '83 reform plan was that we started to cover federal employees, and I believe – again, I can't say exactly how the Pentagon is handled, but I believe they were included in that. They didn't go backwards, but going forward I think they're now covered like any other worker.

I would like to see, in time, state and local workers – that's the one major group that's still not covered – I would like to see them brought in. It does raise some money, but more importantly I just think we want a universal system, and as you're getting problems with those state and local programs I think it makes sense to bring those people in. And again, they could be phased in. I understand it's a problem with the state and local budgets. You don't do it tomorrow; you could phase people in through time. I consider that an important goal.

Immigrants – I just have to mention this having been among all these economists. There was actually a presentation there – someone there that sat there and figured out: suppose we could arrange to have immigrants come and work in the United States and pay their taxes and then go home and never get anything. That's one way you could alleviate the shortfall; not one I'd recommend though.

MR. FURMAN: Next. Again, if you could identify yourself and wait for the microphone.

Q: I'm Dave Koshgarian. I work for the Washington Council Ernst & Young. I actually want to follow up on something Gene was saying. Piñera's little story about the magic of the passbook and all that stuff – is there data yet on whether people do something more down the line? Do they get sort of swept up in this and start saving more beyond whatever the system is requiring you to save? Is there any indication what's happening there?

MR. BAKER: Could I take that one?

MR. FURMAN: Sure.

MR. BAKER: The World Bank actually just did a study reviewing the Social Security privatization programs in Latin America, and understandably much the focus is on Chile because that's the oldest and often thought to be the best. Roughly half the people don't participate at all in the Chilean system so they vote with their feet that they don't want to participate. Of those who do, roughly 40 percent, there's a minimum benefit if you contribute – and I won't swear by the number of years – I think it's 15. But if you contribute for this number of years, and regardless of what you've collected in your account at that point in time, if you don't have enough to maintain a certain standard of living tied to their minimum wage, you turn over your account, the government takes your money and they give you a minimum benefit. And something like 40 percent of the workers in the system target that minimum benefit. So you have workers within this private account system voting with their feet for a traditional Social Security type system.

MR. SPERLING: Let me clarify. I really do not know or remember what the actual data is for Chile, and I was not suggesting that I was endorsing their statements. What I am endorsing, however, is the concept, so let me give you an example I saw firsthand, though it's anecdotal.

In 1992 on the presidential campaign, you can't find a group that's less likely to be saving or thinking about the future than a group of young people on a presidential campaign in sleeping bags at the war room in Little Rock, Arkansas, yet once we came into the White House and they were offered this opportunity of a thrift saving plan, everywhere you went people were saying, "So let me get this right: if I put $2 in I get – if I put $3 in I get $3 back? What do I do?" Then people were, everywhere you went, asking you, "How should I invest it?"

What I'm saying is the concept that if you get people saving at an early age, that people do look forward to seeing their accounts – that they do follow that. That is something that I believe is true. I believe it perhaps based more on that kind of anecdotal experience but it's fairly widespread and I think a lot of people share it. My problem is that because I think progressives and Democrats have heard this case made to support privatizing Social Security where it doesn't make sense, we've somehow not adopted that as an important strategy for creating savings outside of Social Security.

So I believe in these wonderful plans like Melody Hobson at Aerial Capital is doing in Chicago to get kids and schools thinking about how to save. I think that if you had a progressive saving account and young people, when they went to work, were told, "By the way, you might want to take out $700 because you'll get matched 2 to 1," they're not going to care whether it's the government or their employer doing it; they're going to start saving earlier. And I do think – again, that's why I encourage progressives not just to have a rejection attitude towards this talk because it's done in a deceptive context. In the right context, in spreading out IRAs, universal 401(k)s, I think we should be for doing what we can to create the culture of savings and investment in our society and spread it broader among people of lower incomes – African-Americans, Hispanics – and that should be a progressive aspiration.

MR. FURMAN: Yes, the woman in the second row.

Q: Diana Porter with the Alliance for Retired Americans. I would like to add laudatory remarks about Bob Ball also. I think if anyone can be considered Mr. Social Security, it definitely would be Bob Ball and perhaps the center could provide a forum for him to present his plan.

There is one aspect of his proposal – and Dean perhaps would be the one who has remarks to make on it – and that is in the change to the calculation in the CPI.

MR. BAKER: Yeah, I've tried to avoid getting too technical on this, but what Bob Ball has proposed is changing the nature of the index to different indexes, and one question: how best to measure the cost of living? But the long and short is that the index Bob would move to would reduce the annual cost of living adjustment by roughly two-tenths of a percentage point. Now, everyone hears that and thinks, well, three-tenths of a percent; who cares about that? But the point is that's cumulative, okay? So if you're retired this year, you're 62, 65, you lose two-tenths of a percent this year, another two-tenths of a percent next year.

The people it has the biggest impact on are the oldest people, who we also know are the poorest people, most likely to be women. So if you say, okay, who is going to pay for this, you're talking about disproportionately older women in their eighties and nineties who have the highest poverty rates among the elderly. It just doesn't strike me as a terribly good cut.

And one of the issues, you know, when we had this big debate back in '97 over the cost of living, which I'm proud to say I was on the other side and we won; we kept them from changing the cost of living index at that time. But one of the issues that I and others tried to raise in that was if we're so concerned that we accurately measure the cost of living, let's look at the cost of living for the elderly. And the Bureau of Labor

Statistics actually does that and it consistently shows that that rises more rapidly than the overall cost of living. So no one wanted to talk about that.

So if we're concerned that somehow we're not doing what we think we want to do with the indexation formula, we could have a serious discussion but I would say let's start with what actually the cost of living is with people – the affected population: people over 65, the elderly. But, you know, as its stands – as I say, if I'm going to have to cut Social Security, my main target would not be older women in their eighties and nineties and that's who's hit primarily by this.

MR. FURMAN: Next question. You.

Q: Thank you. Just a factual question. I'm Virginia Reno with the National Academy of Social Insurance, and I was interested in your surcharge proposal: the 3 percent surcharge on all sorts of income over $200,000. Do you have an estimate of how much of the Social Security shortfall that is expected to meet over the 75 years?

MR. SPERLING: Here's what I have – the disadvantages of being outside of government is that you can't get these right at your fingertips. I think that I will have an official estimate on this shortly. I believe there are members of Congress interested. Based on very good information, though, I would predict that that would close about .6 percent. So what that means is it would close about 60 percent of what the Congressional Budget Office believes is necessary for solvency and about a third of what the Social Security trustees feel is ready for solvency.

Now, if one wanted to get more – if one could have, you know, 3 percent on income over $200,000 and another 2 percent on income over $500,000 – and that would probably go up another notch to about .8 percent of payroll.

So, again, I am not suggesting that we try to – that progressives insist that all of Social Security solvency be done by taking back – repealing the tax cut on those over $200,000, but I do think that if we have any sense of fairness, that progressives should know that there will be a substantial chunk done, and I think that the ability to sell a program, for the president or anyone else, to the public will be far greater if you can claim that everybody is pulling their share. I have no idea how the president can go with the current plan, which is individual accounts and cutting benefits, or the rumored plan, and explain to people why there is no choice to cut their benefits when, again, one could so easily lower the amount of adjustments to typical workers, typical Social Security recipients by taking back this amount of income.

And I guess my other thing is just that, again, I do think that if you're looking for a stable, longer source, you don't know how income might shift over 10, 20, 30, 40 years between dividend capital gains and wage income. But if it's 3 percent on any income, it should be a fairly stable source for Social Security, and again, prevent tax avoidance, distortion, and strategies to avoid it.

MR. FURMAN: Okay, we have time for one more very brief question and very brief answer.

Yeah, you.

Q: Yeah, I'm Neil Martin with the LaRouche Youth Movement. I would like to know – during the past 35 years, these same policies that George Schultz has been pushing, like privatization of Social Security, privatization of the education system, destruction of infrastructure throughout cities, destroying national banks, and actually having policies that depopulate countries. Now this has come to the United States of America. This is quite funny. But the thing to address is how come no one is addressing this as a fascist economic policy?

MR. FURMAN: Maybe I'll try to answer that very briefly to thank our panelists, who I think over the course of their discussion really described very well the challenges the system faces, some of the real pitfalls with individual accounts and that type of solution, and also pointed to us a better way to go forward to encourage individual savings and restore a greater sense of fiscal discipline than we've had over the last four years.

And thank you all for attending.

(Applause.)

(END)