Fix Social Security? Why Not Abolish It?

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The movement to privatize the Social Security system has gained force in recent years, thanks to Steve Forbes (whose platform in the 1996 Republican primary proposed letting people opt out of Social Security so they could invest for their own retirement) and to President Clinton's advisory council on Social Security, which included a detailed plan for privatization as one of three proposals it made in January.

Conservatives and libertarians are this movement's strongest backers--which is ironic, because the effect of privatization would likely be huge tax increases that would expand government. Under privatization, those currently paying Social Security taxes would be allowed to save part of the taxes in their own personal retirement accounts. This would be popular, since many people, especially those in their 30s, are convinced that they can do better by investing themselves.

But here's the problem: Social Security is a pay-as-you-go system: Almost all of the taxes people pay in this year will be paid out to recipients this year. So if current working people are allowed to invest what otherwise would have been payroll taxes, there will be a shortfall of hundreds of billions of dollars a year for many years. Where is this money to come from?

Some privatization advocates, like Forbes, duck the question. But others, especially economists, have detailed how the transition would be handled, and in all these proposals taxes would increase dramatically. Take, for example, Boston University economist Laurence J. Kotlikoff's plan. Kotlikoff would end the portion of the current payroll tax that is used to fund old-age benefits. But he would force people to save this money in a personal retirement account invested only in government-approved assets that can be drawn on only in retirement. To finance the transition, Kotlikoff would impose a national sales tax at the rate of 10%, falling to about 2%, claims Kotlikoff--within 40 years. The proposal of the pro-privatization members of the President's commission hikes payroll taxes by 1.5 percentage points for 70 years and requires $1.2 trillion in new federal borrowing.

Privatization advocates worry that if nothing is done now, taxes will have to rise even more in the future. To maintain promised benefits the Social Security tax rate would have to rise over the next 50 years from its current level of 12.4% to as high as 23%, according to government actuarial estimates. But who really believes that the government could get away with a 23% tax rate for just one program?

The best way out of all these problems would be to do the politically impossible: abolish Social Security. The government, after all, is not our parent and shouldn't make our decisions for us. To end the program, Congress could decree that people under age 30 will never be able to collect benefits and at the same time cut their payroll taxes accordingly.

The next-best solution--and the one that would-be privatizers should support--is to draw a line in the sand and say, 'No more tax increases.' Then those who want to preserve the current system would be forced to compromise. The current schedule that would raise the age for receiving full Social Security benefits to 67 in 2027 could be accelerated--to 70 by 2015. Social Security benefits could be indexed to a realistic inflation index. And the formula that sets future benefits could be changed to keep real benefits constant rather than increasing them, as it does now. These changes alone would probably eliminate the funding crisis that is otherwise likely to begin around the year 2012.

We would still be left with a government-run shell game that gives us a lousy rate of return and imposes drastic penalties on those who work beyond age 65 or save too much. But at least we wouldn't be saddling future generations with tax rates guaranteed to produce lower economic growth and--ultimately--a lower standard of living.