

STOP THE SPORK! A PROPOSAL FOR SOCIAL SECURITY REFORM

DAVID ZETLAND

President Bush's proposals for social security reform ran into strong opposition and died. I outline a reform that would make social security sustainable, support private retirement accounts and guarantee security for the elderly.



FIGURE 1. A Spork

Most of the debate over social security privatization centered on the share of public versus private management of the retirement system. These debates missed the essence of social security—that it does two things badly.

A SPORK DOES TWO THINGS BADLY

The spork's time never came. A combination of spoon and fork, it saved space, allowed decent functionality, and was popular with fast

Date: November 16, 2005. (Light Went On: Sep 7, 2005. First Draft: Oct 9, 2005.)
Thanks for Tom Jenney, Peter Lindert and Hugh Zetland for helpful comments.
1,600 Words.

food franchises. Consumers did not grab for the spork, however, because they preferred to eat ice cream with a spoon and spaghetti with a fork. Their inclination matched a well-known engineering guideline of one control for each motion. (Cars turn with the steering wheel, move forward with the accelerator, and stop with the brakes.)

Some people think that the Social Security Savings system (SSS) needs to be reformed because it's weak. Why? SSS is like a spork—one program with two goals: to ensure the elderly against poverty and to reward workers for effort. Any reform of SSS must separate and address these objectives, and this simple proposal does just that.

THE RESULTS OF SPORKINESS

Weak Security. SSS does not provides security: You and your family are eligible to receive social security payments only after a minimum amount of work. Elderly can slip through the cracks, if, for example, an unmarried sister lives with her brother and performs work-in-kind on the farm or in the shop. Payments in proportion to earnings also divide rather than unite citizens, weakening solidarity and thus security. The complexity of the whole system (through means-testing and lifetime tracking of a worker's contributions) creates multiple uncertainties (and anxiety) over contributions, future benefits, reforms, etc.

Weak Savings. The returns on Social Security withholding are low: 2 percent per year, versus 4.6 percent from a diversified portfolio of stocks and bonds (Michael Tanner (CATO), as quoted in Francis (2004).). These returns have lowered workers' faith in the strength of SSS while creating risk of future government obligations. Today's workers do not trust that *their* accounts will be protected against current demographic and fiscal forces and stop supporting the system. On the other hand, SSS's status as a government program encourages these same workers to save less for their retirement because they think (perhaps rightly) that the government will not abandon them in their hour of need.

SEPARATING SECURITY FROM SAVINGS

First, I propose that SSS be reformed to *only* support security. Every person over 65 who has been in the country for more than 20 years as either a Citizen or Permanent Resident should be given the same monthly payment. To be fiscally sound, this payment should be set at a low level (say, \$10,000/year), paid out of current taxes (social security taxes should be set to zero), and rise with the cost-of-living.¹

Second, the savings goal of social security should be privatized. All workers will be able to deduct from pre-tax income for their personal retirement savings (e.g., IRA) such that thrifty workers can supplement their \$10,000/year entitlement. It might be wise to require mandatory savings (say, five percent of wages) in bonds to add stability.

These suggestions will deliver the following benefits:

- Clarify that SSS is pay-as-you-go, not a Trust Fund where your contributions are “invested” in “your” retirement account.
- Make everyone’s future secure.
- Reduce the incentive for anyone to “game” a private-savings-only system by saving nothing and hoping for a rescue.
- Put retirement savings decisions in the hands of those who stand to benefit (or lose), while building an “ownership society”.

¹I have had comments in favor of both higher and lower amounts than \$10,000. For comparison, consider that the 2005 HHS Poverty guideline for a “one-person family unit” is \$9,570/year. The Social Security Administration paid 53 million recipients \$495 billion in FY2005 (2006 FY Budget is \$544 billion), or about \$9,340/each (From http://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/index.html). This number masks some asymmetric benefits, however, since Social Security/Insurance payments go to both retired/disabled (34.7/11.0 million) and children/spouses of deceased workers (7.0 million). The former group (receiving \$11,335/year on average) would receive payments under the proposed system. Those under 65 in the latter group would be excluded. Those over 65 who do not receive (or receive very low) payments would be (more) included. An over-65 couple with only one recipient today would have two under the proposed system. The only clear loser under the proposed system would be the child of a deceased worker, who could (and should) be the beneficiary of private retirement savings (or life insurance), not of an old-age pension, which would be sporky. This proposal is not linked to medical care (e.g., medicare for elderly, medicaid for poor), but 10.9 million disabled are still covered.

- Reduce administrative effort for both bureaucrats and recipients—saving both time and money.²

ON FREERIDERS AND MEANS TESTING

Welfare in the United States is tainted by guilt and paranoia. It is part of our national character to worry about “welfare moms” and the undeserving taking advantage of our humanitarian and generous offers (See, e.g., Bénabou and Tirole (2005)). This proposal does not go so far as to advocate a Universal Basic Income, but a minimum guaranteed income for those *we have already decided are deserving and entitled*, i.e., the elderly and disabled. It modifies current policy by removing qualifications to the *level* of entitlement, currently a function of lifetime earnings. My proposal will not punish hard work, since private accounts will still exist. It does protect those who do not work “hard enough” or who fail to plan ahead—contributing to social security.

Advocates of fiscal sustainability might worry that a per capita guaranteed income transfer (subsidy) would overwhelm national resources. This worry can be ameliorated in several ways:

Predictability: Since the number of eligible will be known 20 years in advance, payments will be easy to budget.

Flexibility: Payments could be reduced if government receipts were in crisis, as part of an overall belt-tightening (very rare!).

Phase-in: Benefits might increase between 65 and 70 years from, say \$5,000 to \$10,000, to encourage continued work and thrift.

The current 65-69 population is 10 million; the 70+ population

²The Social Security Administration employs 65,000 workers to administer both Social Security Insurance and Medicare and has a FY2006 budget of \$9.5 billion. Simplification would eliminate some work (i.e., “Process 264 million earnings items to maintain workers’ life-long earnings records.” [and] “Issue 140 million Social Security Statements to advise workers how much they have contributed to Social Security and provide estimates of future benefits.”) and reduce the “approximately 58 million transactions [handled] through SSA’s 800-number” by perhaps 90 percent (from <http://www.ssa.gov/budget/2006bud.html>). Savings in time and reduction in complexity might cut SSA’s budget in half. Recipients, both current and future, would save time, money and stress because benefits would be clear.

is 26.3 million.³ Costs would therefore fall from \$363 billion to \$313 billion. (FY 2005 Spending was \$495 billion.) The addition of 10.9 million disabled raises the cost to \$472 or \$422 billion.⁴

Means-Testing: Those with incomes at a multiple of the basic guarantee (say, four-times), might become ineligible for benefits. This is the least-attractive “solution” because it invites both politicians and recipients to game the system and contradicts the solidarity component of the proposal.

Speaking of political fiddling, this system might destabilize if politicians decided to change the benefit formula (the pre-commitment problem). They may increase benefits to win a populist vote, or decrease them if voters were uninterested in security compared to other policies, e.g., tax breaks, etc. The current system is already under these strains, but the proposed system would lessen them in several ways:

- A transparent, simple, single payment system would be harder to manipulate.
- An increase in social solidarity would receive more support.
- Pressure to raise/lower benefits might dissipate if investment accounts were successful. (If they were not, raising them would address bad design or act as a counter-cyclical stabilization device.)

SOUND FAMILIAR?

I learned recently that Sweden’s *present* pension system very closely resembles my model (Nyqvist, 2005).⁵ I have adopted its mandatory bond investment. The remaining difference is the Swedish *requirement*

³Source: US Census Table NC-EST2004-01 at <http://www.census.gov/popest/national/asrh/NC-EST2004-sa.html>

⁴The disabled program fits the security and solidarity paradigm.

⁵Since this proposal is similar to at least one existing pension system, calling it “my” verges on plagiarism. I am only an advocate (though I may be the inventor of the “Spork” analytical framework). *Full disclosure:* I have reviewed neither academic nor policy literature on social security.

that individuals invest 2.5 percent of their wages in mutual funds. (Additional withholding is optional here.) It would be supremely ironic if this proposal were passed in the US; the US and Sweden would have converged to almost identical pension systems from opposite extremes.

CONCLUSION

America's Social Security System is schizophrenic; it tries to encourage thrift and guarantee safety. My proposal would separate and address these goals with separate instruments: guaranteed income for the elderly and disabled and private savings (with both mandatory and voluntary components) for the employed. The proposed reform would be simpler and encourage solidarity while maintaining incentives and rewarding effort. If this system were adopted and phased in over 30 years, under-35s could plan for the future and over-35's could stop bickering over reform and enjoy life.

David Zetland is a 36-year-old PhD Candidate at the Department of Agricultural and Resource Economics at University of California, Davis. He is willing to live under the new system and can be reached at dzetland@gmail.com

REFERENCES

- Bénabou, R. and Tirole, J. (2005). Belief in a Just World and Redistributive Politics. *NBER Working Paper*, 11208.
- Francis, D. R. (2004). One Man's Retirement Math: Social Security Wins. *Christian Science Monitor*, 27 Dec.
- Nyqvist, A. (2005). Transformers: Notions of Responsibility, Risk and the Boundaries of Market: A Study of the Reformation of the Swedish Pension System. Tenth International Karl Polanyi Conference, Istanbul (14-16 Oct).