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The Personal Lockbox
A First Step on the Road to Social Security Reform

by Michael Tanner

Executive Summary

With President Bush's call for comprehensive Social Security reform bogged down in the morass of partisan politics, many reform advocates have suggested starting the process with smaller steps. Recently, Sen. Jim DeMint (R-SC), Rep. Jim McCrery (R-LA), Rep. Paul Ryan (R-WI), Rep. Sam Johnson (R-TX), and others have proposed legislation to rebate Social Security surpluses to workers in the form of contributions to personal accounts.

Currently, the surplus, projected to be around $70 billion this year, is used for general government spending. In return, the Social Security Trust Fund is given a bond that will eventually have to be repaid out of future taxes. The Senate legislation (S1302) and House proposal (HR3304, known as GROW for Growing Real Ownership for Workers) are designed to prevent Congress from spending the surplus, which would allow individual workers to save that money toward their own retirement.

If the proposal were expanded to include interest currently attributed to the Trust Fund, workers would receive personal accounts averaging roughly 3.4 percent of wages over the next 10 years, only slightly less than the size that President Bush has recommended. That would give workers substantially more ownership, inheritability, and choice than they have under the current system.

At the same time, depriving Congress of the camouflage of the Social Security surplus may force it to be more fiscally responsible, curbing the growth in government spending.

GROW and S1302 are not—and should not be—the final word for Social Security reform. The proposals do little to address Social Security's looming insolvency. The accounts would be only temporary, expiring once the surplus was exhausted. A more comprehensive approach would still be needed.

However, S1302 and GROW represent an important down payment on larger reforms to come.

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As far back as 1998, Sens. Daniel Patrick Moynihan and Robert Kerrey proposed that Social Security be restored to a pay-as-you-go basis.

Introduction

On June 22, a group of leading Social Security reformers in the U.S. House of Representatives, including Reps. Jim McCrery (R-LA), chairman of the Ways and Means Committee's Subcommittee on Social Security; Sam Johnson (R-TX); Paul Ryan (R-WI), and Clay Shaw (R-FL) announced their support for a plan to use current Social Security surpluses to fund personal accounts as a first step toward Social Security reform. Known as GROW, for Growing Real Ownership for Workers, the proposal was introduced as legislation (HR3304) a few weeks later. The day after the House press conference, a group of senators, led by Jim DeMint (R-SC), introduced legislation (S1302) to accomplish the same goal.

This is not an entirely new idea. As far back as 1998, Sens. Daniel Patrick Moynihan (D-NY) and Robert Kerrey (D-NE) proposed that Social Security be restored to a pay-as-you-go basis, where workers are allowed to privately invest the amount they would save from initially lower payroll taxes through personal accounts.[1]

In 2000, then-representative Mark Sanford (R-SC) introduced legislation to rebate Social Security surpluses to personal accounts.[2] Sanford's bill drew 39 cosponsors at the time, including DeMint and many others who would go on to become leaders of the Social Security reform movement, including Senators Lindsey Graham, John Sununu, and Tom Coburn, all cosponsors of S1302.

A paper by American Enterprise Institute scholar Alex Pollock revived that idea this year. Pollock added a new wrinkle, recommending that the rebates be initially invested only in bonds.[3] With more comprehensive Social Security reform legislation bogged down by partisan politics, others—including Stephen Moore of the Free Enterprise Fund, John Fund of the *Wall Street Journal*, and Lawrence Hunter of the Institute for Policy Innovation—began championing the idea as a first step on the road to reform. In June, the proposal moved to Congress.

Although there are differences between the House and Senate versions of the proposal, at the core both are built around the same concept and provisions:

- Workers under the age of 55 could choose to remain entirely within the current Social Security system or participate in a personal account option.
- The accounts would be financed through a rebate of surplus Social Security taxes (directly in the case of S1302 and through an equivalent general revenue transfer in the House version). That surplus would be defined as the difference between all OASDI tax income for a given calendar year, minus the cost of paying Social Security benefits for that year, plus administrative costs. Each worker would receive a rebate of payroll taxes directly proportional to the size of the surplus as a percentage of the system's total tax receipts.[4]
- Initially, workers could invest in government bonds only. Unlike the special issue bonds issued to the Social Security Trust Fund, these would be fully marketable government securities. Beginning in 2008 under the Senate proposal and in 2009 under the House plan, workers would be offered additional investment options.
- Workers would own the funds in their accounts and those funds would be fully inheritable.
- At retirement, benefits from traditional Social Security would be reduced by an amount proportional to the account contributions, plus an offset interest rate equivalent to the realized yield on U.S. Treasury bonds less an administrative fee of 30 basis points.
- At retirement, workers could, but would not be required to, convert the funds in their account to an inflation-adjusted annuity.

The proposal does not pretend to be a comprehensive Social Security reform. It

does little to fix the program's long-term financial problems. The accounts would be small and the rebate of payroll taxes would expire in 2017, once Social Security's surplus was exhausted. Clearly, this is not the final word on Social Security reform. Still, it represents both good policy on its own merits and a good first step on the road to larger Social Security reform.

Stopping the "Raid"

Although Social Security's long-term finances are in desperate shape, the program is currently running a surplus, taking in more through taxes than it pays out in benefits. That situation will reverse by 2017, when the system will begin running annual deficits that will ultimately total more than $11 trillion.[5]

This year, Social Security will take in approximately $70 billion more in taxes than it pays out in benefits.[6] In theory, that surplus is saved through the Social Security Trust Fund to help fund benefits in the future. What actually happens is much more complex.

The surplus is used to purchase special issue Treasury bonds. When the bonds are purchased, the Social Security surplus is mixed with general revenue and is then spent on the government's annual general operating expenses. What remains behind in the Trust Fund are the bonds. Interest payments attributed to the bonds are also paid in bonds, rather than cash. Government bonds are, in essence, a form of IOU, a promise against future tax revenue. When the bonds become due, the government will have to repay them out of general revenue.

That approach is fundamentally flawed in two ways. First, it gives the misimpression that saving is taking place in a way that will make possible the future payment of Social Security benefits, although recent studies suggest that there has been no actual increase in net government assets. Any increase in Trust Fund assets comes with an equal increase in government obligations, so the net financial position of the government is not improved.

Second, it has enabled Congress to hide the true size of the federal non–Social Security budget deficit and, thus, encouraged fiscal irresponsibility.

The accumulation of Social Security surpluses, through the Trust Fund or any other mechanism, represents savings only in so far as it reduces the level of publicly held debt. That is, if offset by increased borrowing elsewhere in the government, no actual savings has taken place. That is precisely what is happening today.

The Social Security Trust Fund was set up in 1939, largely as a political mechanism to ensure that Social Security taxes were not "misused." Indeed, for much of the program's history, Social Security funds were used primarily for the program. However, this does not mean that they were "saved." Generally, the program operated on a pay-as-you-go basis, and accumulating surpluses were very small. When surpluses did accrue, Congress nearly always responded by increasing benefits or expanding eligibility, thereby dissipating those surpluses.[7]

However, two important decisions by the federal government changed that. The first was the enactment of the "unified budget" in 1970. Prior to that, Trust Fund surpluses (or deficits) were counted in the little used federal "consolidated cash budget," but not in the more generally cited "administrative budget." In 1969, however, the Nixon administration adopted a series of recommendations from President Johnson's 1967 Commission on Budget Concepts, including the creation of a single budget to "include all revenues and all spending for all regular Federal programs and trust funds, including off-budget Federal programs."[8]

Just as significant was the decision by the Greenspan Commission in 1983 to try to "prefund" a portion of future Social Security benefits by building up large Trust Fund accumulations. Social Security taxes were deliberately raised above the amount necessary to pay benefits on a pay-as-you-go basis.

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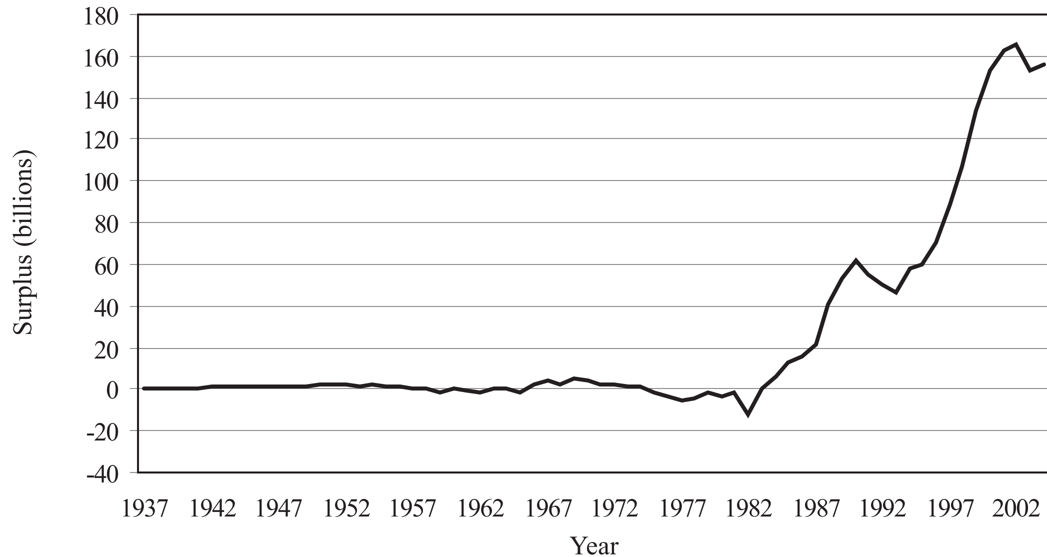
Figure 1
Social Security Surpluses, 1937–2004



Source: Social Security Administration historical data.

The decision to begin building Trust Fund accumulations coincided with a massive increase in general federal spending that led to large government deficits.

As Figure 1 shows, Social Security surpluses, which had been tiny prior to 1983, escalated rapidly thereafter.

The decision to begin building Trust Fund accumulations coincided with a massive increase in general federal spending that led to large government deficits (see Figure 2).

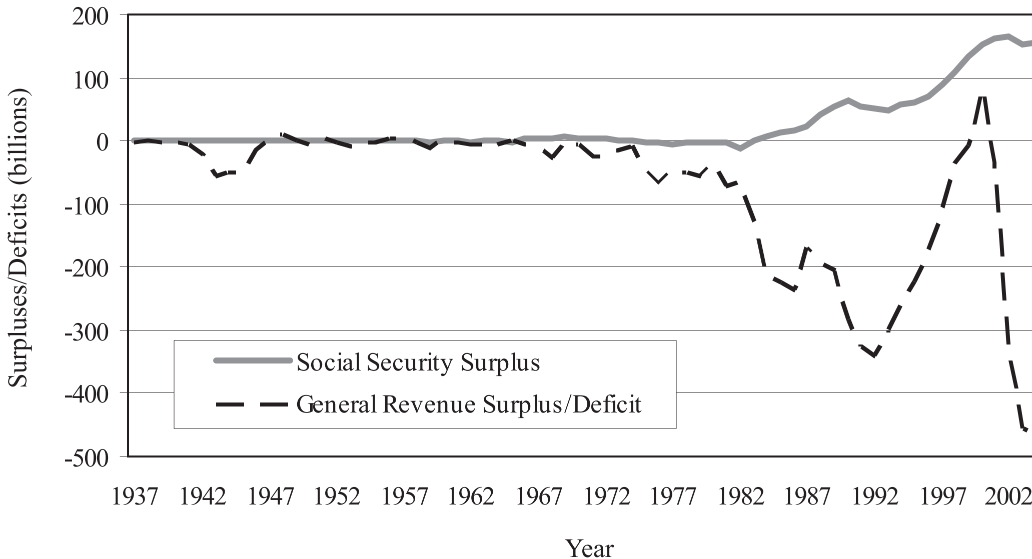
Some observers have argued that the spending increase was unrelated to the growing Trust Fund. If it is true that the money would have been spent anyway, then borrowing from the Trust Fund simply substituted one form of borrowing for another. In that case, payroll tax surpluses can be said to have increased national saving and thus "pre-funded" future benefits in a macroeconomic sense. Without the surplus, we'd have had an increase in government debt but no increase in assets; with the surplus, we get an increase in both debt and assets.

Most observers believe, however, that suddenly blessed with a new pot of money, Congress was unable to resist spending it. By obscuring the actual size of the federal deficit, the unified budget made it easier for Congress to avoid the consequences of its actions and to spend more than it otherwise would have. As Federal Reserve Chairman Alan Greenspan has suggested, "if those funds had been removed from the unified budget and 'locked up' . . . Congress would, in fact, have responded by taking actions to pare the deficit."[9]

As long ago as 1989, a GAO report to Congress stated the following:

> The changes to Social Security enacted in 1983 are not producing the result of lessening the burden of paying for the retirement benefits of the baby boom generation. The budgetary reality is that the payroll taxes are being used to finance the current operations of government and are masking the size of the on-budget deficit. *The economic reality is that the Trust Fund reserves consisting of Treasury securities that are financing current consumption rather than productive investment are illusory.* They will remain so until the rest of the government achieves approximate balance between revenues and outlays.[10]

Figure 2
Social Security Surplus and General Revenue Surplus/Deficit 1937–2004



Source: Social Security Administration, Old-Age and Survivors Insurance Trust Fund, 1937–2004; Congressional Budget Office, historical data.

The GAO's assistant comptroller general Lawrence Thompson put it even more bluntly: "We shouldn't kid the American people into thinking extra savings is going on."[11]

The very next year, the GAO's head, Comptroller General Charles A. Bowsher, warned, "the luxury of these reserves has provided a convenient excuse for avoiding the tough choices needed to cut the general fund deficit."[12]

In other words, the GAO found that the on-budget balance was not independent of the Social Security balance; larger surpluses in Social Security facilitated larger deficits elsewhere. Or, as Bowsher put it: "The growing Social Security surpluses are serving more as a substitute for other deficit reduction action than as a net addition to national savings. . . . If we do not use the accumulating Social Security reserves to increase our national savings rate, we will be in no better position to meet our obligations to future retirees than we would be if we had remained under pay-as-you-go financing."[13]

In fact, the overwhelming body of recent research suggests not only that Congress increases its spending to offset every dollar of Trust Fund accumulations, but the availability of Social Security surpluses actually encourages Congress to increase its non–Social Security spending even beyond the size of the surplus. That is, studies indicate that for every dollar of Social Security surplus, Congress increases non–Social Security spending by $1.50–$2.00.[14] As Cato senior fellow Jagadeesh Gokhale notes, "Social Security's current institutional setup promotes *negative* savings."[15]

Politicians from both parties have denounced this situation for years. During the 2000 presidential debates, Al Gore repeated to the point of parody his call for a Social Security "lock box," which makes sense *only* if he also believed that payroll tax surpluses are not truly saved. In his acceptance speech to the 2000 Democratic National Convention, he called for "putting both Social Security and Medicare in an iron-clad lockbox where the politicians can't touch them. To me, that kind of common sense is a family value. Hands off Medicare and Social Security trust fund money. I'll veto anything that spends it

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The only way to turn Social Security surpluses into actual savings is to take away Congress's ability to spend that money.

for anything other than Social Security and Medicare."[16] George W. Bush essentially agreed, promising, "The Social Security surplus must be locked away only for Social Security."[17]

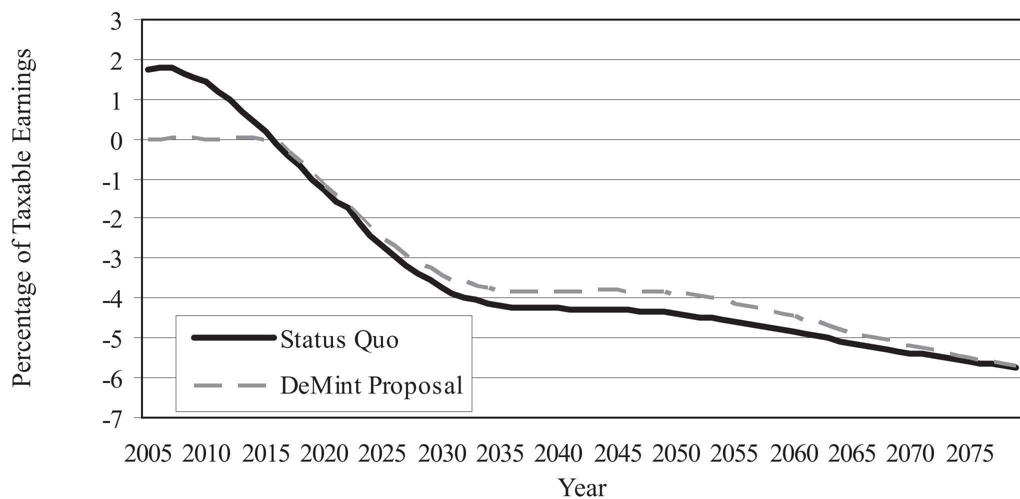
During his last reelection campaign, Senate Minority Leader Harry Reid told seniors he would "reserve all of the Social Security surpluses for Social Security."[18] In March of this year, House Minority Leader Nancy Pelosi declared, "President Bush and the Republicans in Congress should stop their deficit spending and stop robbing the Social Security trust fund of its money."[19] Republican leaders have trumpeted similar sentiments. But, despite all these protestations, Congress has continued to spend the money.

There is no reason to believe that this situation will change in the future. In fact, as Prof. David I. Walker of Boston University has suggested, the entire concept of "collective public saving" may be fundamentally flawed. He points out that government may be even more myopic than individuals when it comes to the need to save; that there is a "collective action problem" in that current generations are unwilling to accept fiscal restraint given that there is no way to bind future generations to similar restraint; and that current consumers of government spending vote, whereas future generations do not. Walker concludes that building public surpluses is simply not politically feasible.[20]

Therefore, the only way to turn Social Security surpluses into actual savings is to take away Congress's ability to spend that money. As Chairman Greenspan put it in his March 2005 testimony to the Senate Special Committee on Aging, "we need, in effect, to make the phantom 'lock-boxes' around the Trust Fund real."[21] Greenspan went on to suggest that the best way to accomplish that was through the creation of personal accounts: "The major attraction of personal or private accounts is that they can be constructed to be truly segregated from the unified budget and, therefore, are more likely to induce the federal government to take those actions that would reduce public dissaving and raise national saving."[22] That is precisely what S1302 and GROW attempt to do.

Social Security's finances would be improved by the change, although only marginally. True, because surplus payroll taxes would be redirect-

Figure 3
Social Security Deficit, S1302 vs. Current System



Source: Derived from memorandum from Stephen Goss and Alice Wade to Sen. Jim DeMint, "Estimated Financial Effects of a Proposal to Finance Individual Accounts with the OASDI Cash-Flow Surplus," June 23, 2005.

ed to individual accounts, future Trust Fund balances would be lower than under current law. However, changes in Trust Fund balances would be countered almost dollar for dollar by the accumulation of assets in the personal accounts. From a system perspective, any loss of income due to the carve-out would be roughly matched by reductions in benefit obligations.[23]

More significantly, the date at which Social Security begins to run a cash-flow deficit—a more important measure of Social Security's financial health—would also remain unchanged. And in the out years, the annual cash-flow deficits would be reduced due to the benefit offsets (see Figure 3).[24] Overall, the proposal would reduce Social Security's unfunded future obligations by roughly $519 billion (in present value terms), a tiny amount compared to the program's estimated $12.8 trillion future shortfall, but a step in the right direction.[25]

Assuming that the federal government took no action to reduce projected spending (or increase revenue) with the personal "lockbox" in place, the unified budget deficit would be increased between 2006 and 2017. After 2017, the unified budget's cash flow would be slightly improved since the Social Security benefit offsets would reduce the amount of general revenues needed to finance Social Security's cash shortfalls (see Figure 4).

The total publicly held debt and unified budget balances would worsen slightly due to interest on the increased debt.[26] The distinction between publicly held and intragovernmental debt, however, is largely a matter of accounting. That is particularly true in this case, where the government would not have to find new sources of borrowing from private markets to finance the debt.[27]

Ownership, Inheritability, Choice

Solvency should not be the sole—or even the most important—reason for reforming Social Security. Far more important are three fundamental flaws with the current structure of Social Security.

First, under the current Social Security sys-

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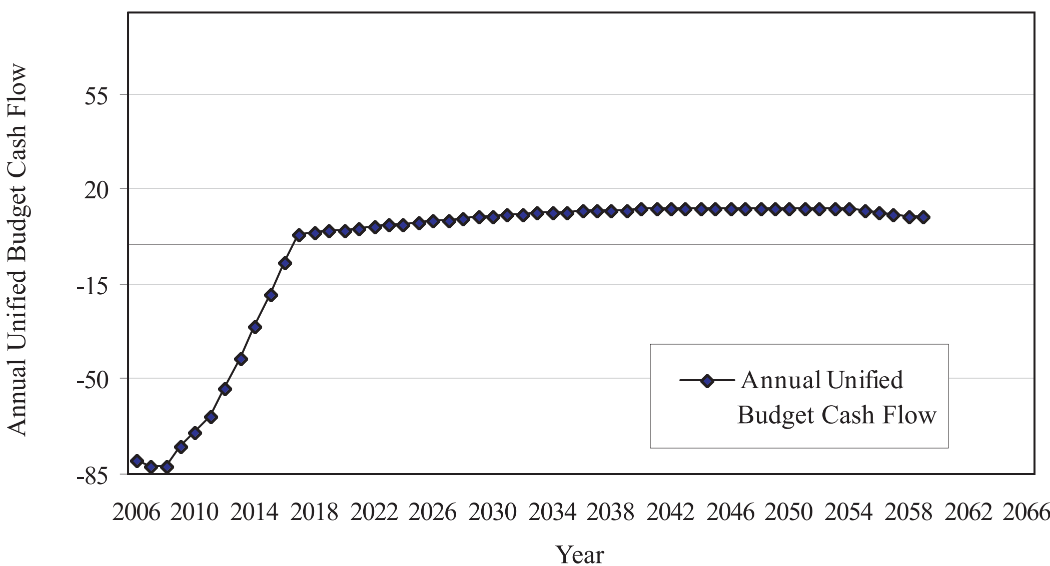
Figure 4
Change in Unified Budget under S1302



Source: Derived from memorandum from Stephen Goss and Alice Wade to Sen. Jim DeMint, "Estimated Financial Effects of a Proposal to Finance Individual Accounts with the OASDI Cash-Flow Surplus," June 23, 2005.

Workers would be able to accumulate significant assets and have substantially more ownership and control than under the current system.

tem workers have no legal, contractual, or property rights to their benefits. As the U.S. Supreme Court has ruled, in the case of *Flemming v. Nestor*, there is no relation between the money that workers pay in Social Security taxes and the benefits that they receive. Congress can change, cut, or even take away those benefits at any time.[28]

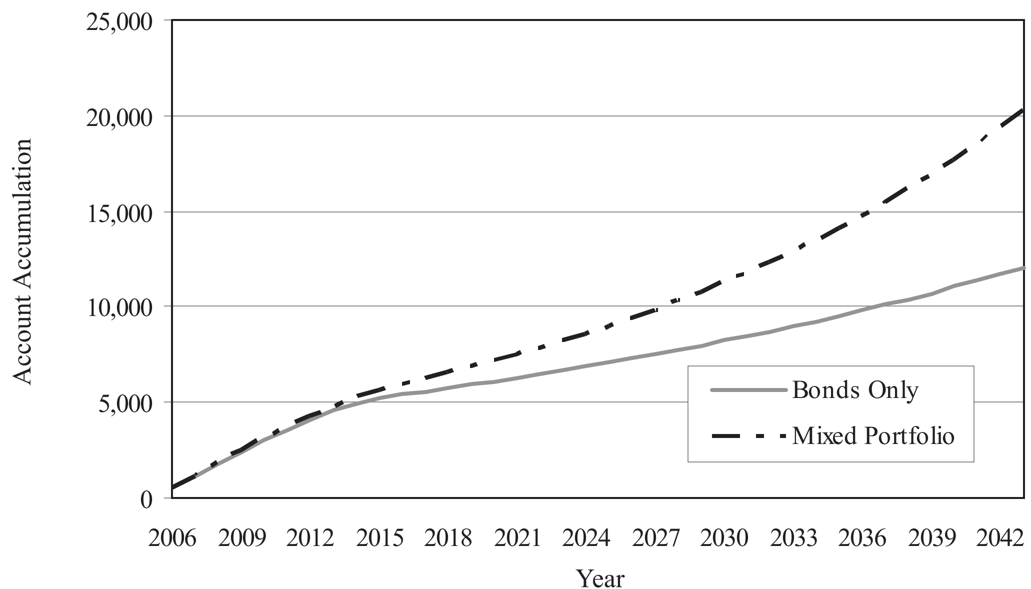
Moreover, because workers don't own their Social Security benefits, those benefits are not inheritable. Millions of workers who die early are not able to pass the value of their accumulated payroll taxes on to their loved ones. That is a tragedy, particularly for low-income workers and minorities who have shorter life expectancies and fewer non–Social Security assets.

And, finally, the current Social Security system forces all workers into a "one size fits all" program that cannot pay promised future benefits, that offers a return far below that of private capital markets, and that gives workers no legal right to benefits. Of course, some workers may prefer this system, judging the political risks of traditional Social Security to be preferable to the volatility of private capital markets. However, others would almost certainly prefer the option of saving and investing a portion of their Social Security taxes for themselves. The current Social Security system gives workers no choice.

GROW and S1302 would help fix those problems. The accounts would be a worker's property. While the accounts would be much smaller than many reformers have advocated, workers would nonetheless be able to accumulate significant assets and have substantially more ownership and control than under the current system.

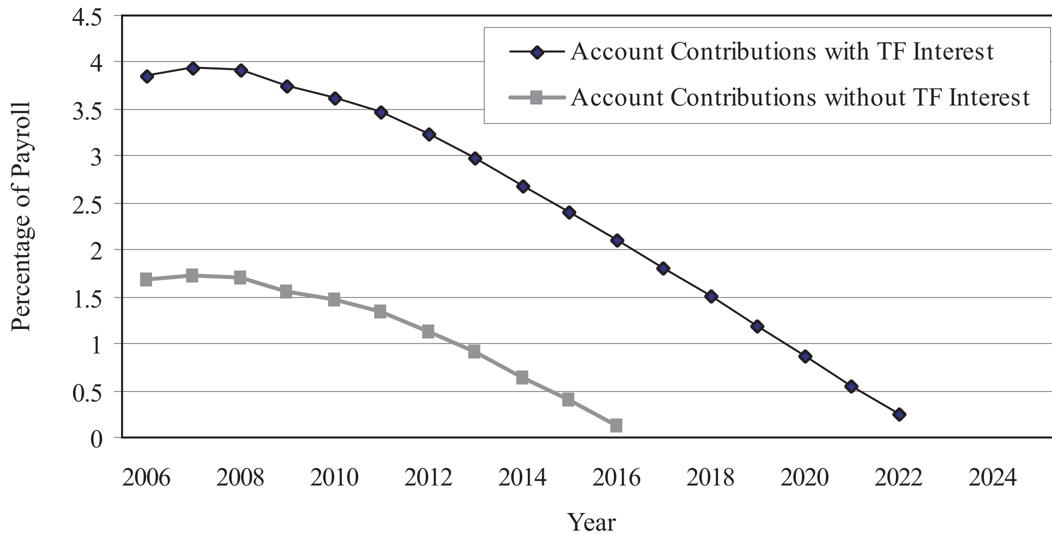
In 2006, the first year the rebate would be in effect, workers could save approximately 1.7 percent of their wages in a personal account.[29] A worker earning the median U.S. wage of $34,000 would be able to contribute $575 to his account. By the time the surplus runs out in 2016, the worker would have contributed slightly more than $4,700 to his account, and earned an additional $730 in interest, making the account worth $5,470.[30] Moreover, even after the worker stops making contributions, the funds in the account would continue to earn interest. A hypothetical worker who starts the account at 30 years of age, invests only in

Figure 5
Expected Account Performance, Bonds vs. Mixed Portfolio



Source: Author's calculations based on 2005 Trustees Report.

Figure 6
Trust Fund Interest and Size of Private Accounts



Source: Author's calculations based on 2005 Trustees Report.

government bonds, and retires at age 67, would accumulate over $12,000. If, once additional investment options become available, the worker chose to invest in a portfolio of 50 percent bonds/50 percent stocks, he would accumulate more than $20,000 by retirement (see Figure 5).[31] Although that may not seem like a great deal of money, it represents more than a year of that worker's Social Security benefits at their currently promised rate, and roughly two years of the benefits that Social Security will actually be able to pay. In addition, because workers would own the money in their accounts, those funds would be fully inheritable.[32]

Finally, S1302 gives workers a choice. Participation in the personal account option is voluntary.[33] Even though the accounts are designed to be virtually free of market risk, workers who wished to remain in the traditional Social Security system would be free to do so. As additional investment choices were offered, workers could select investments that more nearly mirrored their personal risk preferences, potentially receiving higher retirement benefits than Social Security would be able to pay them.

Making a Good Proposal Better

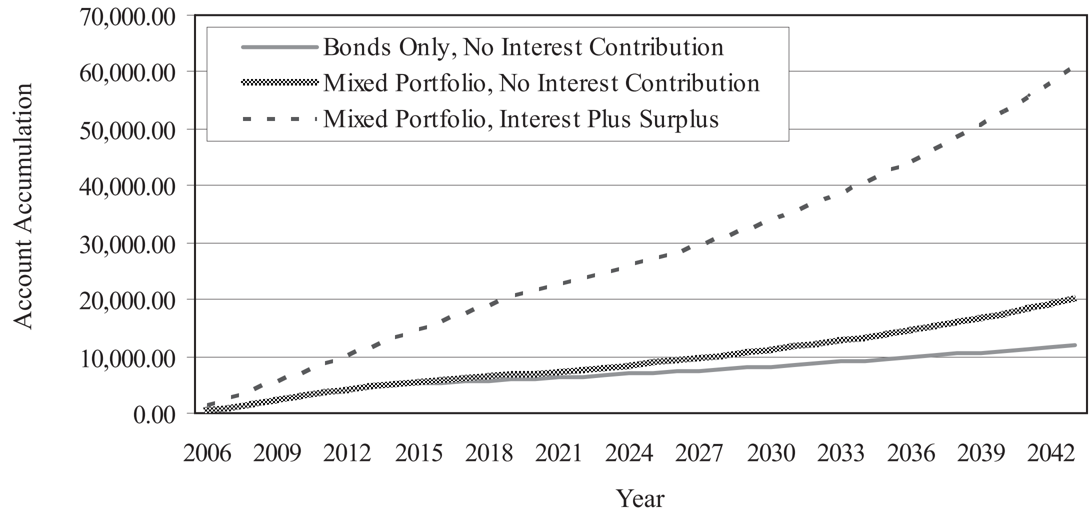
GROW and S1302 represent a significant step forward on the road to Social Security reform. But there are some changes that could make the proposals even stronger.

As currently proposed, neither S1302 nor GROW include interest that would otherwise have been attributed to surplus Social Security funds, estimated to be approximately $97 billion in 2006. This interest is "paid" to the Social Security Trust Fund only in the sense that additional bonds are issued to the Trust Fund. Therefore, it would be a relatively simple matter to issue those bonds directly to worker's personal accounts.[34] It would simply amount to a bookkeeping change, moving debt from the "intragovernmental" column to the "publicly held" column. Since the government would repay these funds in any case, there is no reason not to transfer them to individual ownership.

Doing so would more than double the account size. At their high point, the accounts would equal nearly 4 percent of wages and, over the first 10 years of the program, the

Participation in the personal account option is voluntary.

Figure 7
Account Performance by Portfolio Type



Source: Author's calculations based on 2005 Trustees Report.

As the Clinton administration pointed out, "The existence of large Trust Fund balances . . . does not by itself have any impact on the government's ability to pay benefits."

accounts would average 3.4 percent of wages (see Figure 6).[35] That would be only slightly smaller than the accounts President Bush has proposed. Moreover, allowing accounts to be funded with Trust Fund interest would extend account contributions beyond the end of surplus payroll taxes in 2017, perhaps through 2023.[36]

For workers, the increased account size could make a significant difference. Take the 30-year-old, median-wage worker discussed above. If interest were included in contributions to his account, his accumulated funds at retirement would triple from roughly $20,000 to more than $60,000, assuming a 50/50 stock/bond portfolio (see Figure 7).

Second, the House and Senate versions differ significantly in the mechanism used to fund the accounts. S1302 funds the account directly from "the OASDI annual cash-flow surplus."[37] The House proposal, in contrast, "would fund individual accounts with revenue from the General Fund of the Treasury in amounts equal to the OASDI annual cash-flow surplus."[38] In effect, whereas the Senate version is a true "carve-out," the House proposal allows surplus payroll taxes to be credited first to the Trust Fund where they would continue to be leant to the Treasury in exchange for special issue bonds.[39] Having purchased the bonds, the surplus then becomes General Revenue and is available to fund the accounts.

The understandable goal is to hold the Trust Fund harmless, thereby avoiding demagogic attacks from critics of personal accounts. In reality, however, that would represent a double counting of payroll taxes. Each dollar of surplus payroll taxes would, in effect, create two liabilities—one to the Trust Fund and one to a worker's account. When the Clinton administration proposed a similar double accounting in 1997, it was rightfully criticized by fiscal conservatives and Social Security reformers.[40]

Furthermore, such a move would undermine the pressure on Congress to control non–Social Security spending. The Trust Fund would continue to hide the true size of the deficit. Congress could continue to overspend without increasing the unified budget deficit.

Therefore, the House should follow the lead of S1302 and avoid this fiscal sleight of hand.[41] Although this means Trust Fund balances would be lower than currently projected, as the Clinton administration pointed out, "The exis-

tence of large Trust Fund balances . . . does not by itself have any impact on the government's ability to pay benefits."[42]

Conclusion

GROW and S1302 are not—and should not be—the final word on Social Security reform. The proposals do little to address Social Security's looming insolvency. The accounts would be temporary and far too small to fully rectify Social Security's biggest problems: the lack of ownership, inheritability, and choice in the current system.

A more comprehensive approach would still be needed, either now or in the near future. Several worthwhile proposals have been introduced in Congress, most notably The Individual Social Security Investment Plan Act (HR530), sponsored by Reps. Johnson and Jeff Flake (R-AZ).[43] However, accounts funded out of the Social Security surplus can be seen as a reasonable down payment on larger reforms to come.

Importantly, these proposals take the first steps toward reform while avoiding many of the criticisms of more extensive proposals. For example:

- Critics of personal accounts have said that they take money out of Social Security. This proposal would only use Social Security surpluses. The government's general operating budget would be deprived of those funds, but Social Security's finances would not be touched. There is no "transition cost."[44]
- Critics have said that personal accounts are too risky. This proposal would let workers initially invest in government bonds only. All that would change is who holds the bonds. Instead of the Social Security Trust Fund keeping the bonds, individual workers would hold them. Workers would gain some of the benefits of ownership and inheritability without assuming significant market risk. Although additional investment options would later be added, an all-bond investment option would remain.
- For years, critics have said Social Security surpluses should not be used to fund non–Social Security spending. This proposal would represent a true "lock box," with the money going solely to workers' retirement. Without Social Security surpluses to hide behind, Congress would have to face up to the choices of running higher deficits, raising taxes, or—hopefully—spending less.

This proposal meets the critics on their own terms. In short, it calls their bluff. If their stated objections were removed, what would be left for them to oppose? The very idea of people owning and controlling their own money?

Every day that Congress fails to act, an additional $200 million is spent rather than being saved for workers' retirement.[45] It is time to get started on fixing Social Security.

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Notes

1. S21, Social Security Solvency Act of 1998.

2. HR4839, the Personal Lockbox Act of 2000, would have set up "a tax-exempt personalized retirement program for covered individuals through the designation of a personal retirement account for each individual that is funded by deposits from amounts in the Federal Old-Age and Survivors Insurance Trust Fund not otherwise required for immediate withdrawal."

3. Alex J. Pollock, "A New Approach to Personal Social Security Savings Accounts," *AEI on the Issues*, April 2005.

4. That is, if the surplus equals one-quarter of all taxes collected, the worker would receive a rebate equal to one-quarter of the taxes he or she paid.

5. The federal government will also have to repay $1.7 trillion in bonds currently held by the Social Security Trust Fund, making the system's total unfunded obligations in excess of $12.8 trillion. Social Security Administration, "The 2005 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds," http://www.ssa.gov/OACT/TR/TR05/.

6. Social Security Administration, "The Fiscal 2005 Budget," press release, http://ssa.gov/budget/2005bud.html#TFunds.

7. The existence of these small, temporary surpluses appears to have had little impact on the federal government's spending or borrowing patterns outside of the program itself. John Cogan, "The Congressional Response to Social Security Surpluses, 1935–1994," Hoover Institution Essays in Public Policy, 1998.

8. Sita Nataraj and John Shoven, "Has the Unified Budget Undermined the Federal Government Trust Funds?" National Bureau of Economic Research Working Paper no. 10953, December 2004.

9. Alan Greenspan, Chairman of the Federal Reserve Board, Testimony before the Special Committee on Aging, U.S. Senate, March 15, 2005, http://www.federalreserve.gov/boarddocs/testimony/2005/20050315/default.htm.

10. U.S. General Accounting Office, "Social Security: The Trust Fund Reserve Accumulation, the Economy, and the Federal Budget," January 1989, p. 6, http://archive.gao.gov/d15t6/137817.pdf. Emphasis added.

11. "Warning Issued by GAO about Social Security," *St. Louis Post-Dispatch*, January 29, 1989.

12. Charles A. Bowsher, Comptroller General of the United States, Statement before the Senate Committee on Finance, "The Question of Rolling Back the Payroll Tax: Unmasking the Deficit Illusion," February 5, 1990.

13. Ibid.

14. Nataraj and Shoven; Kent Smetters, "Is the Social Security Trust Fund a Store of Value?" *American Economic Review* 94, no. 2 (May 2004): 176–81.

15. Jagadeesh Gokhale, "Social Security Status Quo versus Reform: What's the Tradeoff?" Cato Institute Social Security Paper no. 35, July 12, 2005, p. 4.

16. Al Gore, Address to the 2000 Democratic National Convention, August 17, 2000, http://www.cnn.com/ELECTION/2000/conventions/democratic/transcripts/gore.html.

17. Bush-Cheney 2000, http://web.archive.org/web/20001109020800/www.georgewbush.com/issues/socialsecurity.html.

18. Office of Sen. Harry Reid, "Senator Reid Unveils Agenda for Seniors," *Senior Newsletter*, Winter 2000.

19. Office of Nancy Pelosi, "Pelosi to Republicans: 'Stop Robbing the Social Security Trust Fund,'" press release, March 2, 2005. Pelosi appears to have later changed her mind on the subject. After House Republicans introduced GROW, she said, "there is a surplus in Social Security, and under the law Social Security can lend that money to the government for other purposes." Keith Koffler, "Pelosi Says Current System of Borrowing Surplus Is Sound," *CongressDaily PM*, June 24, 2005.

20. David Walker, "The Social Insurance Crisis and the Problem of Collective Savings: A Commentary on Shaviro's Reckless Disregard," *Boston College Law Review*, 2005.

21. Greenspan.

22. Ibid.

23. Because of the subsidy to cover administrative costs and losses to inheritance, this wouldn't quite be perfect balance. At the same time, since the accounts could eventually be invested at least partially in equities and would be assumed to earn a higher return, the system would likely end up paying out lower future benefits, thereby improving its long-term financial outlook. The above analysis is based on two assumptions. The first is that giving workers ownership of their personal accounts won't affect personal consumption. The more important assumption is that the federal government will actually reduce spending to offset the increase in the unified budget deficit. To the degree that these conditions are not met, overall publicly held debt might increase.

24. Memorandum from Stephen Goss and Alice Wade to Sen. Jim DeMint, "Estimated Financial Effects of a Proposal to Finance Individual Accounts with the OASDI Cash-Flow Surplus," June 23, 2005, Table 2.

25. Ibid.

26. Ibid., Table 1b. It should be noted that the cash-flow projections are entirely theoretical and include promised Social Security benefits that cannot be paid.

27. Ed Lorenzen, "Summary and Analysis of Senator DeMint's 'Stop the Raid on Social Security Act of 2005,'" CentristPolicyNetwork.org, June 24, 2005.

28. *Flemming v. Nestor*, 363 U.S. 603 (1960). For a fuller discussion of this issue, see Charles Rounds, "Property Rights: The Hidden Issue of Social Security Reform," Cato Institute Social Security Paper no. 19, April 19, 2003.

29. Account size will shrink and the ability to make contributions will eventually expire as Social

Security's surplus becomes a growing deficit. Over the first 10 years of the program, accounts would average about 1.2 percent of wages. However, the plan's proponents assume that the American public will demand that funding be found to avoid the shrinkage and expiration of their accounts. Social Security reformers hope that this funding will come in the form of an additional "carve out" from existing Social Security taxes.

30. Author's calculations, based on the 2005 Trustees Report, Table VI.f7. This assumes a 3 percent real interest rate.

31. Author's calculations. This assumes a 4.6 percent rate of return, net of administrative costs.

32. S1302, Section 257(b)(1)(C); HR3304, Section 259 (b) (1)(a)-(c).

33. S1302, Section 253 (b); HR3304, Section 253 (b).

34. Note that because the Trust Fund will not increase from its present size—because future surpluses will be diverted to personal accounts—the interest payment would essentially be frozen at $97 billion per year. Beginning in 2017, part of this interest payment would be offset by Social Security deficits, reducing and eventually eliminating the amount available to fund accounts.

35. Author's calculations. Note that because the accounts will continue to shrink as Social Security's surplus becomes a growing deficit, the accounts would average about 2.6 percent over the entire life of the program.

36. Author's calculations.

37. Goss and Wade to DeMint.

38. Memorandum from Stephen Goss and Alice Wade to Reps. Jim McCrery, Clay Shaw, Sam Johnson, Paul Ryan, and John Shadegg, "Estimated Financial Effects of the Growing Real Ownership for Workers Act of 2005."

39. HR3304, Sec. 254 (1).

40. See, for example, David C. John, "Clinton's Newest Social Security Plan: From Bad to Worse," Heritage Foundation Executive Memorandum no. 633, October 28, 1999; "Clinton's Social Security Proposal: Double-Counting *Plus* Interest," U.S. Senate Republican Policy Committee, February 18, 1999; Martin Feldstein, "Clinton's Social Security Scam," *Wall Street Journal*, February 1, 1999; William Niskanen, "Forget the Double Counting, Focus on the Phony Accounting," Cato Institute Daily Commentary, February 2, 1999.

41. S1302 simply requires a General Revenue transfer to the Social Security Trust Fund whenever the Trust Fund ratio falls below 100 percent of the amount required to pay full benefits, something that would occur anyway under current law. S1302, Section 254(C)4.

42. Executive Office of the President of the United States, *Budget of the United States Government, Fiscal Year 2000, Analytic Perspectives*, p. 337.

43. This legislation is based on ideas first developed by the Cato Institute. See Michael Tanner, "The 6.2% Solution: A Plan for Reforming Social Security," Cato Institute Social Security Paper no. 32, February 17, 2004; Michael Tanner, "A Better Deal at Half the Cost: SSA Scoring of the Cato Social Security Reform Plan," Cato Institute Briefing Paper no. 92, April 26, 2005.

44. It is worth noting that the entire concept of transition cost is misleading. There are short-term cash-flow financing issues involved in moving from a pay-as-you-go Social Security system to a prefunded one. However, properly designed, contributions to personal accounts would be offset by future reductions in traditional benefits. Looked at over the long term, there is no increased cost. See Gokhale.

45. "A Surplus Idea," *Wall Street Journal*, June 23, 2005.

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