

STRENGTHEN SOCIAL SECURITY

...don't cut it.

Gingrich's "New" Social Security Privatization Plan Soundly Rejected in 2005

Surging GOP Presidential hopeful Newt Gingrich recently announced his plan to "fix" Social Security. A retread of a failed 2004 Social Security privatization bill that gained few allies in Congress, Gingrich's Social Security plan would cost trillions of dollars, explode the federal debt, and weaken the crucial protections that the program provides.

Gingrich expresses support for many types of privatization plans (Chile, the "Galveston Plan," Thrift Savings Plans), but he is most enthusiastic about a 2005 privatization bill co-sponsored by Rep. Paul Ryan and Sen. John Sununu.¹ The Ryan-Sununu bill sets up private accounts run by investment firms to manage people's retirement savings.² Current retirees would continue to receive and those nearing retirement would still be eligible to receive the Social Security benefits they paid for, while younger workers would receive hybrid benefits until the system is fully phased in. Gingrich claims that the accounts would be optional (traditional Social Security would remain for anyone who still wants it), and that the government would guarantee a minimal return of investment in case the funds do not perform well.

- **Gingrich is proposing a "fool's gold" fix to Social Security, a plan that is neither feasible nor fiscally responsible and that would "explode" the national debt.** Gingrich claims that privatization will solve the Social Security shortfall, but it only does so by borrowing tremendous sums from the rest of the government. Because Social Security is funded on a largely pay-as-you-go basis, when people divert money from Social Security to their private accounts, the Trust Fund will have to draw down its current surplus to pay for current beneficiaries. This problem that will become increasingly severe and require borrowing from general revenues *every single year*, for an astounding total of *\$10 trillion*.³
- **By relying on the market, the Gingrich plan increases vulnerability in an uncertain economic environment.** Private accounts submit individuals' retirement savings to the roller coaster of the stock market, which has the potential to cause instant damage to years of hard-earned resources.⁴ Benefits from private accounts are much less reliable, as they are tied to investment performance, which can fluctuate widely. For instance, IRAs and 401(k) plans lost \$2.7 trillion – 32 percent of their value – when the stock market collapsed from 2007 to 2009.⁵ And unlike Social Security benefits, income from private accounts is not guaranteed to last the lifetime of a beneficiary, nor is it protected against inflation.

- **The Gingrich plan intensifies risks for women and low-income workers.** On average, women live longer, earn less than men, experience discontinuities in their labor force participation as a result of caring for children, and are more likely to work part-time. Shifting from Social Security – a defined benefit plan which incorporates benefits for divorced and married spouses, benefits for widows (and widowers), and an annual cost-of-living adjustments – to a plan where benefit amounts more nearly reflect prior contributions is, on balance, disadvantageous to women. Similarly, the Gingrich plan places low- and moderate-income workers at significant risk. As currently structured, Social Security assures that lower-income workers get a better return on their contributions than higher income workers, a factor that keeps millions of the elderly out of poverty during their retirement years.⁶ But in separating out the interests of higher-income workers from the public portion of the program, privatization schemes ensure erosion of political support for the program's redistributive role – an outcome which would further increase the economic and social distance between rich and poor.⁷
- **The Gingrich plan weakens Social Security insurance protections and coverage.** Social Security provides life, disability, and retirement insurance. For unpredictable expenses – how long we will live, how much inflation there will be – savings cannot replace the insurance that Social Security provides. Social Security beneficiaries need not worry about their individual accounts running out, since the program guarantees fixed, inflation-protected benefits for life. In contrast, under a private scheme, because recipients have some discretion about how to use their savings, some may elect for shorter-term disbursements, potentially leaving them extremely vulnerable and without support in their old age. Further, a private plan based on defined contribution principles creates huge temptations for individuals and members of Congress to liberalize the distribution rules. If that happened, what was intended as retirement income savings could be used up on other purposes: medical emergencies, for instance, or making a down payment on a home.
- **The Gingrich plan harms future generations.** It is inconceivable that \$10 trillion – an amount greater than 2/3 of our entire national debt – will be transferred into Social Security to finance the creation of private accounts. For that staggering sum, the current program could (theoretically) not only be restored to long range balance, but its benefits could be increased across-the-board by over 20 percent.⁸ These massive costs can only be financed through “unspecified future reductions in government programs or increases in taxes (in order to fund the transfers) or by large increases in deficits and debt that would be dangerous for the economy.”⁹ In all of these scenarios, future generations lose, either by having their taxes increased, Social Security benefits cut, or the economy tied down with debt. In short, Gingrich’s plan masks the true costs of privatization by shifting the burden onto the federal government and future generations.

- Gingrich’s plan encourages risky investing and could lead to much bigger government transfers.** Acknowledging that the markets bear a certain amount of risk, Gingrich promises that “the government guarantees that all workers with personal accounts will receive at least as much in retirement as they would under the current Social Security system.”¹⁰ This means that the Treasury (i.e. taxpayer dollars) would act as a backstop to make up the difference between what the private account earned and what a person’s Social Security benefit would otherwise be. This incentivizes individuals to make very risky investments: if the returns are great, the individual wins; if not, the government (i.e. other taxpayers) will subsidize the losses so the individual doesn’t actually lose anything. What looks like a win-win deal for the individual has enormous repercussions at the national level, as the government is left to bear all the risks after encouraging individuals to take risky gambles in the market.

In short, Newt Gingrich has pulled the privatization page out of an old and discredited playbook. It didn’t work in 2005 and it will not today.

¹ Newt Gingrich, “Unleashing Growth and Innovation to Move Beyond the Welfare State,” November 21, 2011, p. 6-23. <http://www.newt.org/news/unleashing-growth-and-innovation-move-beyond-welfare-state>

² Social Security Personal Savings Guarantee and Prosperity Act of 2004: H.R. 4851, sponsored by Rep. Paul Ryan, and S.2782, sponsored by Sen. John Sununu. Because this bill is the chief model for Gingrich’s private accounts, unless otherwise noted, all calculations and comments hereforth about the Gingrich plan will refer to this bill. H.R. 4851 received a total of 6 co-sponsors in the House and only one in the Senate, failing to make it out of committee in either chamber.

³ Ibid. The \$10 trillion figure reflects the actuaries’ risk-adjusted estimate of the proposal; not adjusted for risk, the proposal would borrow \$8.5 trillion.

⁴ Ben Furnas, Center for American Progress, “Your Future on the Market: Social Security private accounts in a world of market instability,” October 2008. http://wonkroom.thinkprogress.org/wpcontent/uploads/2008/10/ss_report.pdf Gingrich tries to avoid this outcome by guaranteeing that the federal government will pay the difference between what the private accounts generate and what the normal Social Security benefit would have been. However, if this ever happened, it would put enormous strain on government resources and would send debt levels through the roof.

⁵ Economic Policy Institute calculation based on Federal Reserve Flow of Funds data, September 17, 2010, Tables L.118.c, L.213, L.225.i, prepared October 7, 2010. Unpublished. Economic Policy Institute calculation based on Federal Reserve Flow of Funds data, September 17, 2010, Tables L.118.c, L.213, L.225.i, prepared October 7, 2010. Unpublished.

⁶ There are two competing principles at play here, both central to how Social Security functions: adequacy and equity. While people who have worked hard at higher wage receive higher benefits in numerical terms, those who have worked hard at lower wages receive benefits that are proportionally higher (though lower in numerical terms).

⁷ Eric Kingson and John Williamson, “Why Privatizing Social Security Is A Bad Idea,” in *The Generational Equity Debate*, p. 204-220, 1997.

⁸ Virginia Reno and Joni Lavery, National Academy of Social Insurance, “*Fixing Social Security: Adequate Benefits, Adequate Financing*,” October 2009, p. 28. Increasing benefits by 20% would cost about \$3.2 billion, while eliminating the shortfall would cost about \$6.5 billion.

⁹ Furman, p. 2.

¹⁰ Gingrich Plan, p. 17.