The Nature of Social Security

Social Security “contributions” are not contributions at all, but taxes. Were they contributions, the money collected would go into an account in the worker’s name. Instead, the money collected is paid into the Treasury like any other tax and is not earmarked in any way.

Further, Congress can cut or eliminate Social Security benefits at any time. In short, Social Security is neither a pension fund (since the workers do not own the money collected) nor is it insurance (since Congress can unilaterally reduce or even abolish Social Security benefits at any time).

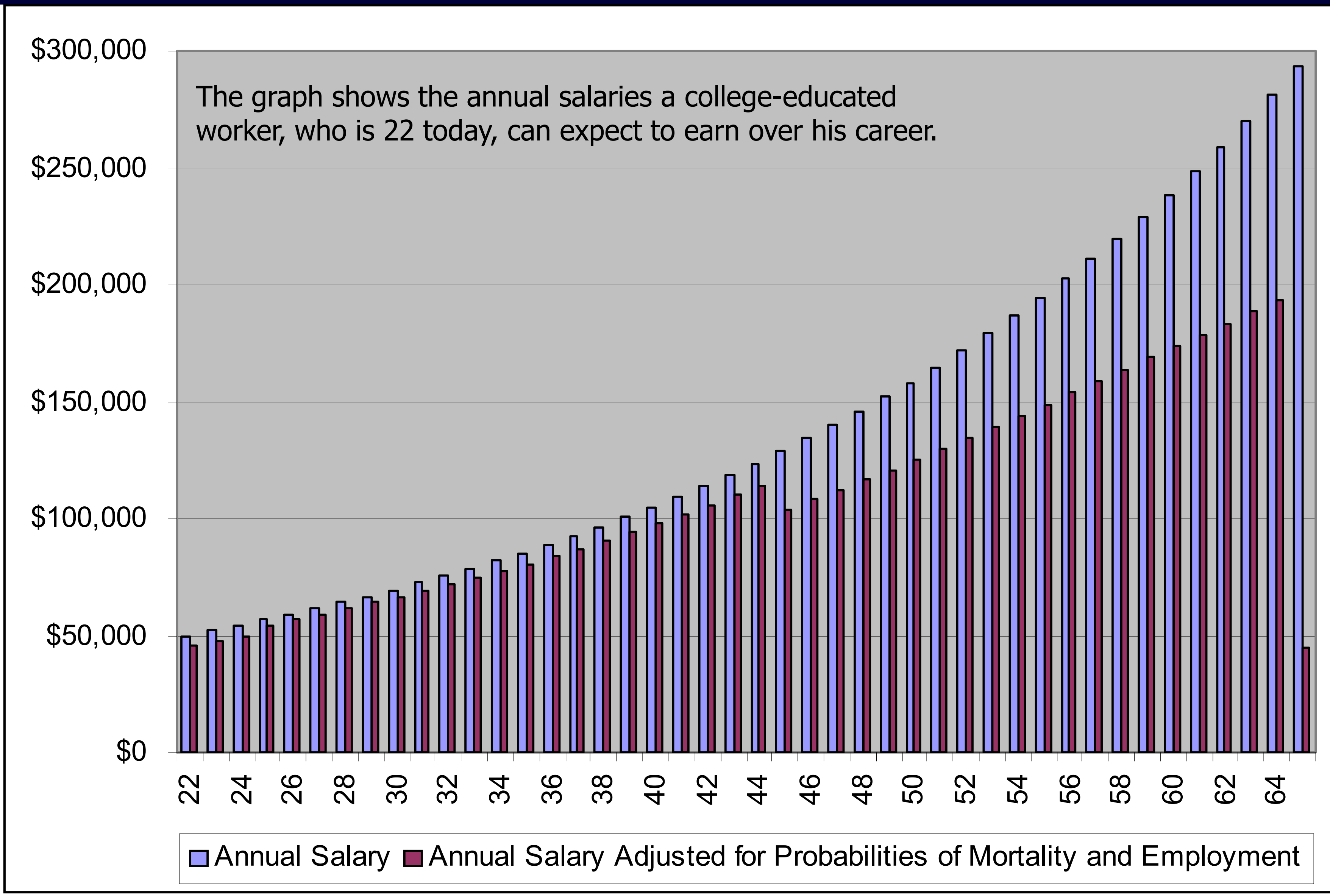
Issues Involving Social Security Reform

1. How much can you expect to pay into Social Security over your life?
2. How much can you expect to receive in Social Security retirement benefits?
3. How much could you expect to receive if Social Security were completely privatized?
4. How risky is a private retirement account?

Assumptions

- Social Security tax rates will remain at their current levels.
- Maximum wages subject to Social Security taxes will grow at the rate of inflation (the historical average).
- Inflation will average 3.2% annually (the historical average).
- Wages will grow at 4.2% annually (the historical average).
- Probabilities of mortality, labor force participation, and unemployment match those for the average American worker.
- Career begins at age 22. Retirement is at age 66.
- Social Security benefits are given by the Social Security Administration (www.ssa.gov/retire2/AnypiaApplet.html).
- Starting salary at age 22 is $50,000.
- Private retirement accounts earn 8% annually (the historical average).

Salary Accounting for Likelihood of Employment



Compiled from data published in 2003 Statistical Abstract of the United States, U.S. Bureau of the Census

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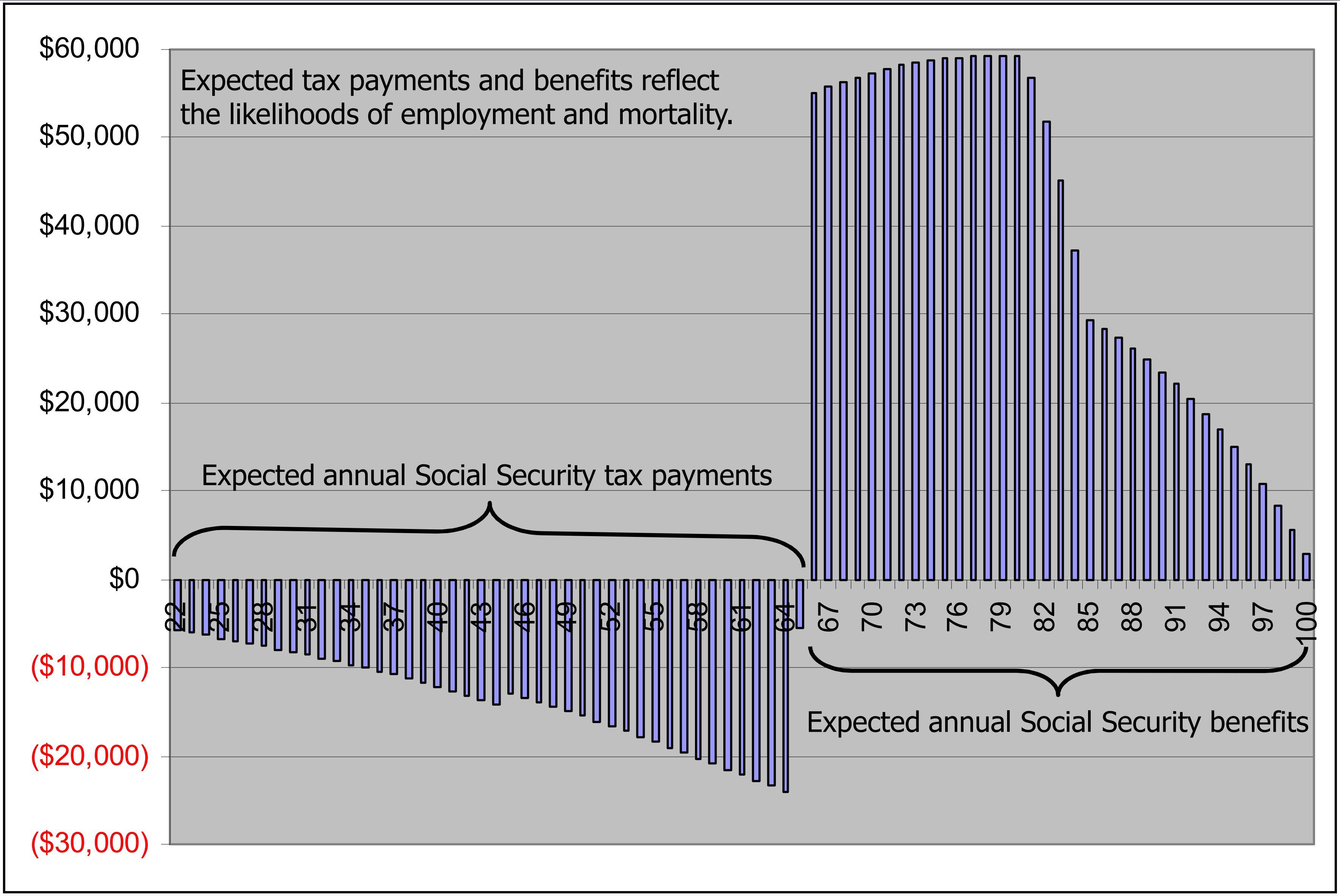
Expected Social Security Taxes and Benefits



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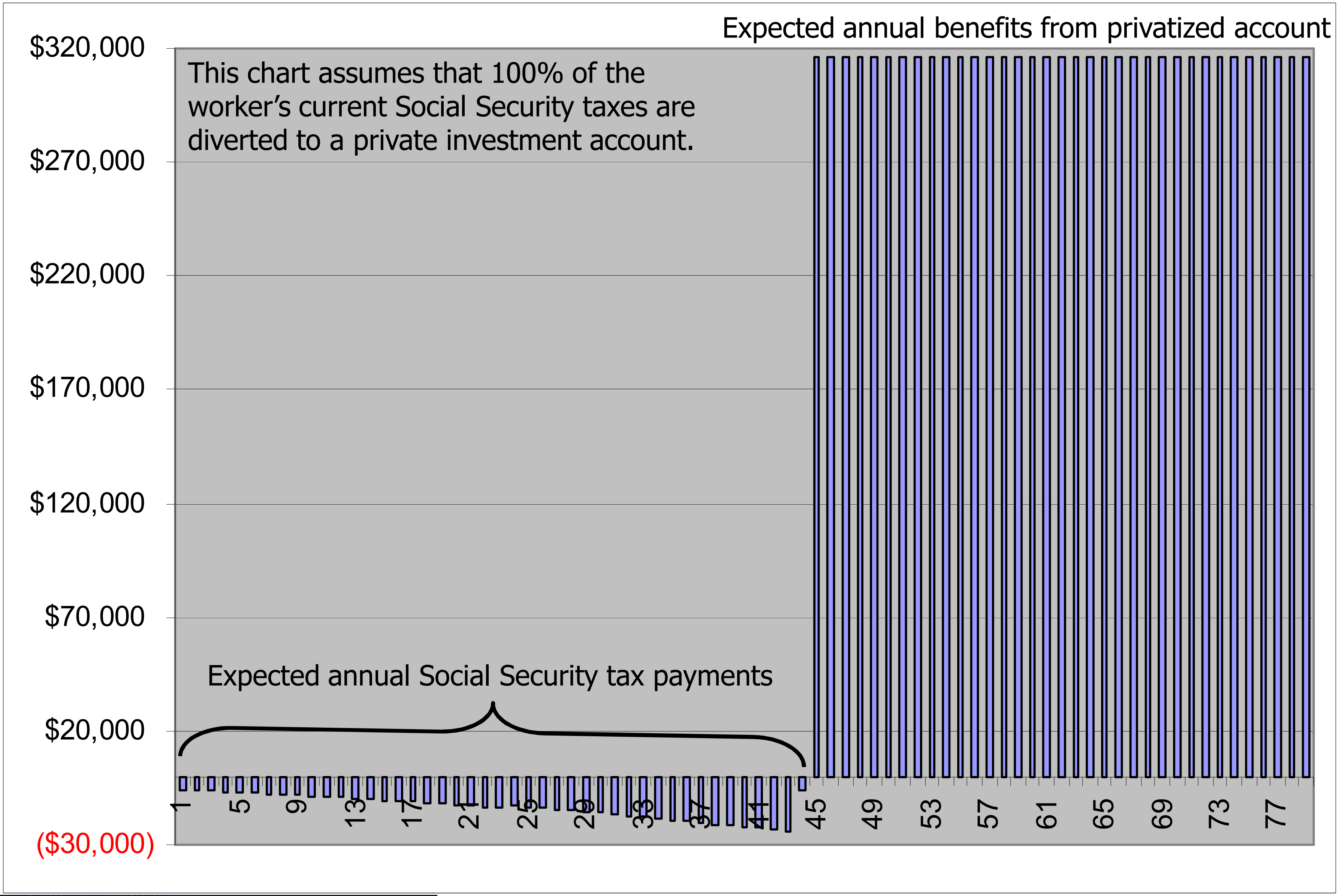
Expected Taxes and Benefits from Privatized Account



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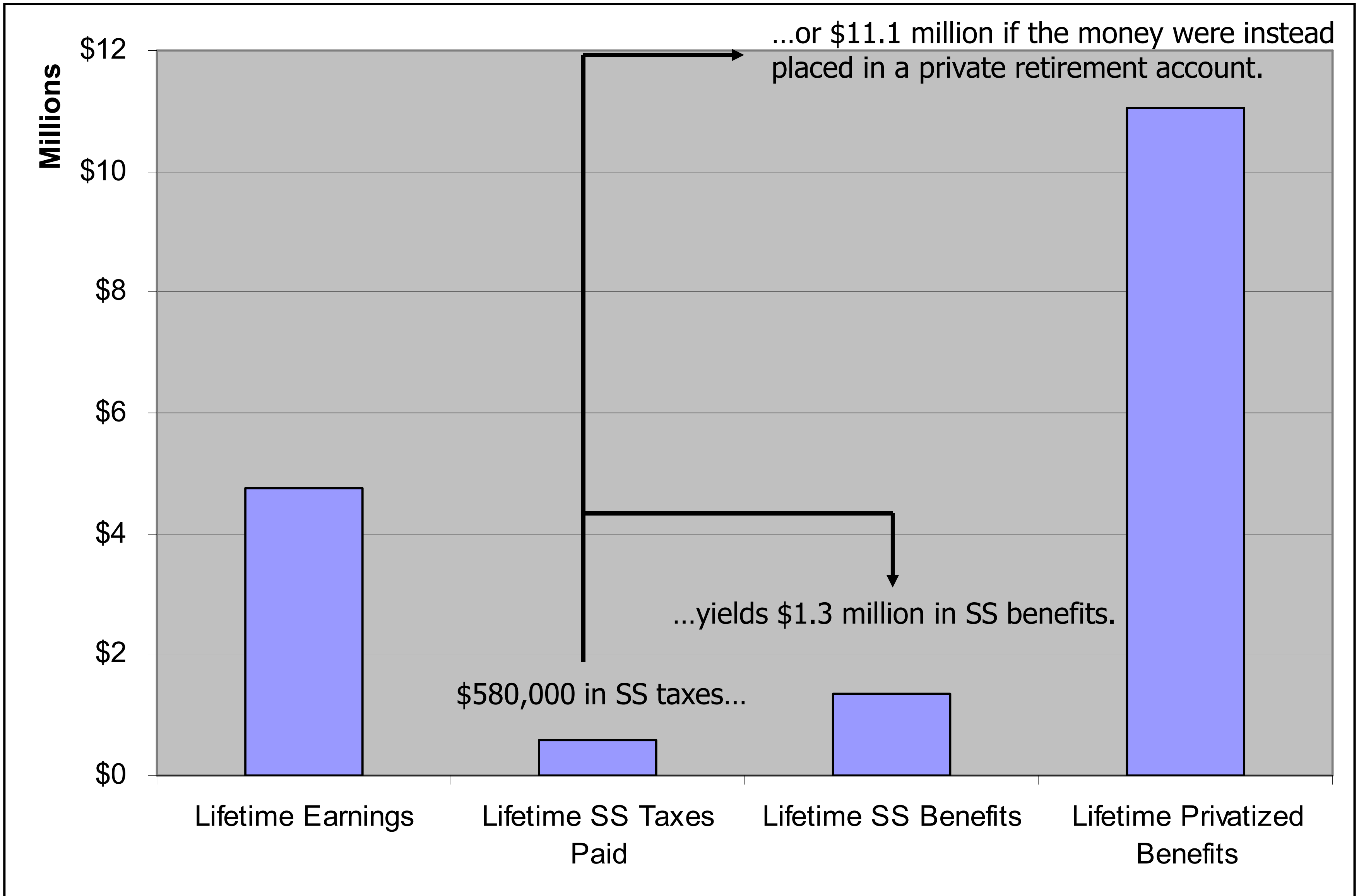
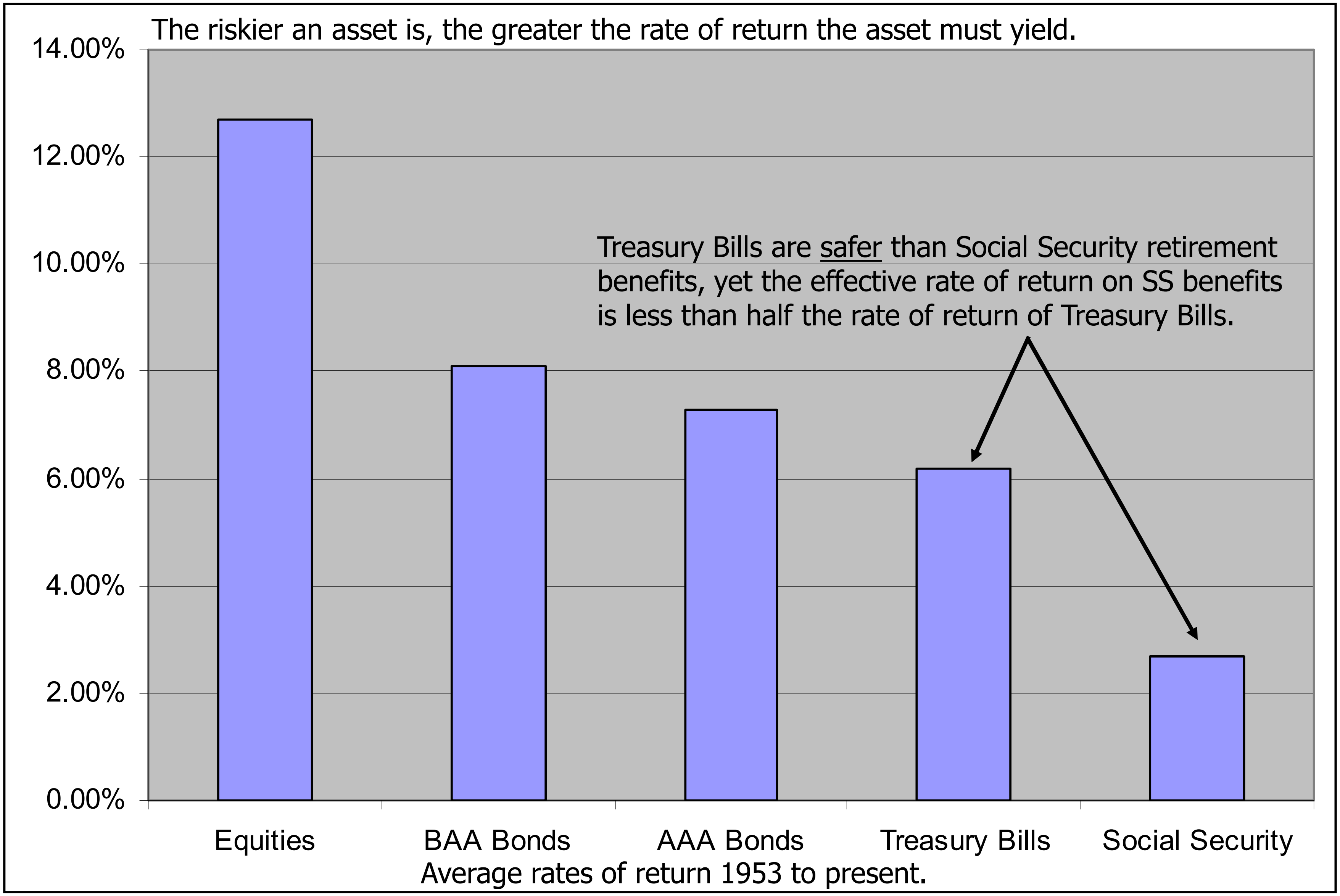
Lifetime Earnings, SS Taxes, and Benefits



Compiled from data published in 2003 Statistical Abstract of the United States, U.S. Bureau of the Census, and provided by the Social Security Administration

What About Risk?



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Conclusion?

Action	Result
Worker diverts 100% of his Social Security tax payments to a private retirement account that is a mix of equities and bonds yielding 8% annually.	• Worker incurs some risk as a result of investing in market assets. • Worker's expected retirement benefits would be 8.2 times greater than the worker's expected Social Security benefits.
Worker diverts 100% of his Social Security tax payments to a private retirement account that holds only long-term U.S. Treasury Bills.	• Worker incurs less risk than he faces with a Social Security retirement account. • Worker's expected retirement benefits would be 3.6 times greater than the worker's expected Social Security benefits.