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Weaning Workers Off Failing Social Security

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It's coming time for the Social Security Board of Trustees to release its annual report, and no one should expect much to have changed since last year. For a sinking ship, that's not good news.

As of last year, the Board of Trustees projected that Social Security's expenses will exceed its revenues by 2022. At that point, it will need to start cashing in the more than $5 trillion in U.S. Treasury Bills the trust fund has accumulated over the years. By 2035, about the time that today's 50 year-olds will be retiring, the trust fund's pool of Treasury Bills will have run dry. At that point, retirees will have to take a benefits cut, workers will have to pay a lot more in Social Security taxes, or, more likely, both groups will have to give up something.

Not only is this a problem nearly a century in the making, it is one that the numerically literate have seen coming since today's retirees were landing their first jobs. The Board of Trustees projects that it can extend Social Security by a few more decades if Congress imposes cuts or tax hikes now. But that won't fix the problem; it will merely push it into the future. And the further Congress pushes the problem into the future, the more expensive it becomes to fix.

The real problem here is that the American people love programs that offer them money and services, but they only love them to the extent that they can extract more in benefits than they pay in taxes, and that is a losing proposition over the long term. Nonetheless, the government made promises and it needs to keep them. It is time, though, that politicians stopped promising things they can't deliver. And that means weaning people off Social Security starting now.

In one way, Social Security itself makes that goal relatively easy. The rate of return on the average worker's Social Security contributions is around 3 percent. That's almost nothing. A conservative 401(k) or IRA can return twice that. Aggressive investing — the sort that young workers should be making — can yield three or four times that.

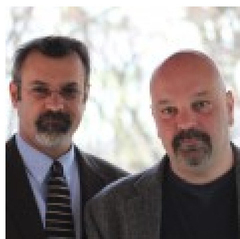
Because Social Security's rate of return is so low, the typical worker is actually better off paying into Social Security until about age 40, and then walking away — giving up all claim to retirement benefits but also being relieved of the 12.4 percent combined tax that the worker and the worker's employer pay.

If the typical worker, starting at age 41, invested that 12.4 percent in a 401(k) or IRA, she could expect to end up with a nest egg about the same size as the Social Security benefits she forfeited. In other words, Social Security is such a bad investment that the worker is better off walking away from 20 years' worth of retirement contributions than continuing in the system.

This points to a clear way out of Social Security. Tell workers 40 and younger that they will receive no Social Security retirement benefits, but that they must continue to pay Social Security taxes until their 41st birthday. From that point forward, they must invest in a 401(k) or IRA the 12.4 percent they were paying to Social

Security. This will start a wave of workers who are off Social Security. Over the course of the next 60 years, Social Security would gradually wind down, and then disappear.

We are 83 years into the Social Security experiment, and the laws of finance and mathematics are poised either to shut it down or to make its continuation prohibitively expensive. We would all be better served admitting that Social Security is simply too big to succeed and planning our way out of it — while there's still time.



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