

ISSUE BRIEF

Social Security Privatization

Some policymakers have proposed replacing part of Social Security’s guaranteed benefits with individual investment accounts as a way to address the system’s projected long-term financing shortfalls. Proposals to privatize Social Security typically require diverting current Social Security payroll tax revenues into individual accounts (often 2 percentage points of the 12.4 percent payroll tax) to be invested in stocks and other securities. While efforts to strengthen and protect Social Security are critical, Congress should reject privatization proposals because they jeopardize Social Security’s capacity to provide workers a guaranteed foundation of retirement and income security and undermine its family protections.

Social Security provides retirement, life and disability insurance for 96 percent of America’s workers and their families, according to the Social Security Administration (SSA). The SSA reports that nearly two-thirds (64 percent) of elderly persons rely on Social Security for half or more of their income, and more than three in 10 (31 percent) rely on it for nearly all (90 percent) of their income. In addition to the retirement program, which provides 32 million retired workers with benefits guaranteed for life and is adjusted annually for inflation, Social Security also provides guaranteed benefits to more than 5 million workers with disabilities, 4.8 million widowed spouses and 3.8 million children of deceased, retired or disabled workers, as shown by SSA statistics.

Taking money out of the trust funds would hurt Social Security. Diverting Social Security’s payroll taxes into individual accounts would seriously weaken the system’s finances. According to the Center on Budget and Policy Priorities (CBPP), so-called carve-out accounts would drain more than \$1 trillion out of Social Security in the first decade alone. The CBPP also calculates that diverting just 2 percentage points of the payroll tax out of Social Security to fund individual accounts would more than double the size of Social Security’s projected shortfall and push Social Security into financing trouble as early as 2026, compared with 2041 if no changes were made. That is because this money already has been earmarked to pay future benefits—it cannot be spent twice.

Privatizing Social Security will cut guaranteed benefits. To pay for private accounts and bring the system into balance, Congress would have to make deep cuts in Social Security’s guaranteed benefits, unless it were willing to earmark very large amounts of revenue from the rest of government or increase taxes. These cuts would affect everyone, even under privatization proposals that include “voluntary” individual accounts.

According to a seminal study by the nonpartisan Century Foundation, guaranteed retirement benefits would have to be cut by approximately 40 percent on average for future recipients if 2 percent of payroll taxes were diverted from the Social Security trust funds into individual accounts.

Privatization means less retirement security for working families. Income from individual accounts would make up for part, but not nearly all, of the cuts in guaranteed benefits. The Century Foundation also found that even after adding in income from the new account, an average single worker who puts in a full career and has good investment returns would see total retirement benefits cut by 20 percent. Many married couples would see greater total benefit cuts. Workers would be forced to make up the difference through employer-provided pensions or increased personal savings;

however, employers are cutting back significantly on traditional pensions, and there is a widely perceived savings crisis in the United States.

Unlike today's Social Security benefits, private accounts are risky. Individual accounts do not provide predictable, dependable benefits as a foundation of income. There are big differences in the amount of income an investment account might generate at retirement based on things that are completely outside any worker's control, particularly stock market performance over a worker's career and at retirement. The Wall Street sales pitches about historical average returns are meaningless to any individual worker. Replacing a guaranteed benefit with one that is dependent on the ups and downs of the stock market can have disastrous results for workers, as evidenced by Enron, WorldCom and other recent corporate debacles.

Privatization threatens benefits for survivors and people with disabilities, as well as retirees. Despite promises to "preserve" these programs, Social Security's crucial benefits for people with disabilities and survivors of workers who have died likely would be cut right along with retiree benefits. It would be difficult to maintain the current level of benefits while diverting 2 percent of payroll into private accounts. And it is highly unlikely that private account accumulation by a disabled or deceased worker not yet qualified for retirement benefits would be sufficient to provide the same level of benefits as current law for the needs of a surviving spouse or minor children.

Privatization could be significantly harmful to women. Social Security very clearly is designed in ways that help women. Women's longer life expectancies, lifetime low earnings and likelihood of outliving their spouses mean they rely on Social Security's guaranteed, lifelong benefits, its benefit formula that replaces a greater share of earnings for lifetime low earners and its family protections, particularly survivor benefits, as shown by the CBPP. As a result, Social Security plays a critical role in providing women with a secure foundation at retirement. Individual accounts do not replicate the special protections built into Social Security.

Privatization could be significantly harmful to people of color, as well. Three of four older African American and Latino households rely on Social Security for half or more of their retirement income, and a third count on it for all their income, according to the SSA. Because these groups are less likely to have pensions or savings income, they are more reliant on Social Security. Both groups benefit from Social Security's greater income replacement rate for low-income workers and special family protections. The CBPP has shown that African Americans, in particular, benefit from Social Security's disability and survivor protections. Replacing Social Security's guaranteed benefits with individual accounts cuts many of these special protections built into Social Security.