

President's Commission
to Strengthen Social Security

*Thursday,
September 6, 2001*

Held at the
San Diego Marriott Hotel & Marina
San Diego, CA

Audio Associates
9537 Elvis Lane
Seabrook, Maryland 20706
301/577-5882

A T T E N D A N C E

Wednesday August 22, 2001

MEMBERS PRESENT:

Richard D. Parsons, Chairman

Leanne Abdnor
John Cogan, Ph.D.
Estelle James, Ph.D.
Gwendolyn S. King
Gerald Parsky
Timothy J. Penny
Mario Rodriguez
Thomas R. Saving, Ph.D.
Fidel A. Vargas

ALSO PRESENT:

Mike Anzick, DFO
Social Security Administration

I N D E X

Audio Associates
(301) 577-5882

	<u>PAGE</u>
Welcome and Opening Remarks	
Chairman Richard Parsons	5
Panel 1 - The Need for Reform	
Bob Bixby, Concord Coalition	13
Panel 2 - Social Security Investment: By Individuals or by the Government?	
John Shoven, Stanford University and Hoover Institution	41
Kent Weaver, Brookings Institution	49
Panel 3 - Social Security Reform and Wages	
Suzanne Taylor, National Association of Women Business Owners	85
Eloise Anderson, Claremont Institute	91
Lisa Maatz, Older Women's League	96
Panel 4 - Public Perspectives	
Bob Tilaro	142
Denise Lawson	144
Chuck Latimer	148
James Wittkower	152
Sally Acosta	155
Lori Chapin	158
Robert Prath	164
Michael Bateman	168
Panel 5 - Other Experiences: At home and Abroad	
Valerie Vandeweghe, Benefits Administrator, City of San Diego	172
Judge Holbrooke, Galveston, Texas	175
Anita Schwarz, The World Bank	180

I N D E X (Continued)

	<u>PAGE</u>
Panel 6 - Interested Groups from Across the Political Spectrum	
Peter Ferrara, Americans for Tax Reform	195
Roger Hickey, Institute for America's Future	204
David John, Heritage Foundation	207
Percil Stanford, National Committee to Preserve Social Security and Medicare	212

KEYNOTE: "----" Indicates inaudible in transcript.

President's Commission
to Strengthen Social Security

*Thursday,
September 6, 2001*

Held at the
San Diego Marriott Hotel & Marina
San Diego, CA

Audio Associates
9537 Elvis Lane
Seabrook, Maryland 20706
301/577-5882

WELCOME AND OPENING STATEMENTS

CHAIRMAN PARSONS: Okay. If we could come to order. Good morning, ladies and gentlemen. My name is Dick Parsons, and I am one of the co-chairs of the President's Commission to Strengthen Social Security.

Is Fidel -- do we know where Fidel is?

MR. : Fidel is going to be a late.

CHAIRMAN PARSONS: He is going to be a little late.

All right. Well, you have before you nine of the members of our 16-member commission, and we are delighted to be with you this morning in San Diego.

I want to start, of course, by welcoming first the members of the public and the members of the press who are here and last, but not least, those of you who will be appearing before us as witnesses. We are deeply in your debt.

Additionally, I would like to pay a special note of thanks to our local host and member of the commission, Gerry Parsky, who is with us today. And the other members you can see around the table are here because we are interested in hearing what folks have to say about this compelling subject.

The purpose of the hearing, as I think everyone knows, is really to hear from a broad cross-section of the American; their views about the matter of strengthening and modernizing the Social Security system.

All of the members of the commission agreed right at the outset that it was extremely important not only to increase public understanding about the circumstance -- I won't call it crisis because that is a charged word, but the circumstance in which we find ourselves in this country with a Social Security system that is unsustainable over the long-term.

But we also agreed that it was important to hear from the public about how we treat with that set of circumstances and how we deal with what many of us believe is a looming or an impending problem that affects every American, and we wanted to hear from the public and have an opportunity for input before we finalized our own thinking and made our recommendations to the President.

So, that is why we are here. We are here to listen and to learn and to educate ourselves, and hopefully in this process help to better educate all of the people about the nature of the problem and the nature of -- and tradeoffs involved in some of the ways we can go about solving it.

Now, since we put out the notice that we were going to have public hearings and asked for people to sort of self-identify and volunteer to testify, we have been deluged with E-Mails and faxes and letters and telephone calls from folks who were anxious to come before the commission and share their insights.

Unfortunately, as is always the case, we were not able to accommodate everyone's request. So what we tried to do was to select a series of panelists, and we have six panels that we will be hearing from today, who bracket, if you will, and represent the broad categories of concerns that have been expressed and views that have been shared.

Also, we asked -- we did receive written testimony, if you will, and submissions from a whole host of folks who you won't hear today. But those will be digested by staff and made a part of the commission's record so that everyone, in a sense, had an opportunity to have input. Even those who will not be appearing before us today.

In other words, we wanted to say publicly how grateful we are to those of you who took the time and had the interest and shared with us your perspectives on the problem, because even if you weren't called upon to be one of the testifying witnesses, your views will be given careful consideration.

We also want to say a particular note of thanks to Congressman Filner and Congressman Cunningham, both of whom were gracious enough to give us statements of welcome today, which also will be a part of our record.

Now, a word about where we are in our process. Well, there is our commission, Fidel. Come on up. I mean, there is no sense in trying to hide.

I think that most of you here would know that we did, as a commission, put out an interim report in the month of July, which really spoke to the nature of what we see are the challenges confronting the current Social Security system.

In a nutshell, the commission concluded that the system, as it is currently structured and funded, is not sustainable and that in order to restore both a sense of confidence on the part of people who will be, one day, beneficiaries of that system, namely working Americans, and to help restore the system to financial and fiscal soundness and to modernize the system, frankly, actions needed to be taken.

But what we wanted to do was first kind of point out the problems and then peak the public's interest in terms of helping us find solutions to recommend to the President to those problems. And so, we are post-interim report, but clearly pre-final report, and we are here to hear not only comments and criticisms of some of the findings that the commission has already made in its interim report, but frankly, to hear from people what they think we should be thinking about and looking at by way of solution.

Now, we have been given a set of principles by the President, who organized this commission and who has, in my judgement, frankly, shown the courage to tackle what is a

highly emotionally charged and sensitive set of issues. But understanding that they are an important set of issues for, as I say, the system touches all Americans.

The President, I think, has shown some courage in sort of stepping up to the plate and saying we need to do something about it. And I would like to get the input of knowledgeable Americans in terms of what are some of their thoughts, but I want to do that within certain limitations, because it is important always to remind folks of what we are not about, as well as talk about what we are about.

Let me articulate those principles. First is we are not going to cut. The recommendations of this commission will not result in a diminution of benefits to any people who are now beneficiaries -- not beneficiaries of the system, but are retired or who will soon or shortly enter retirement.

We are not going to raise the payroll taxes or recommend a raise in the payroll taxes. We are going to preserve Social Security disability and survivor's components. I think that is important, and I will say it again. There will be no altering or diminution of survivor's or the disability components of Social Security.

I have read a number of times in the press how those communities are concerned that somehow this commission is going to recommend diminution in their benefits. That is not the case.

We are also charged with exploring the creation of personal accounts, which I think the President feels and many of us on the commission feel that is an element of modernization to the current Social Security system. But exactly how that is to be done, how it is to be structured and how it is to be financed are open questions, and we want to hear from some of our witnesses today on ways in which they think that can be accomplished. Or, if they think that is a bad idea, why?

So we are open to all ideas, and we are going to spend the bulk of this day hearing. So let me just conclude by briefly telling you the six panels that we have selected and who we will be hearing from today.

The first panel will feature a gentleman named Bob Bixby, who is with the Concord Coalition. Because the Concord Coalition is a bipartisan organization representing both sides of the political spectrum, the Republicans and the Democrats alike, which is, by the way, how this commission is structured -- there are an equal number of Democrats and Republicans so that bipartisanship is assured -- we thought it might be well to give Mr. Bixby the first shot out of the block and give him an unimpeded opportunity to get himself into trouble here because, you know, we are going to be asking you questions, sir.

But we will start off with kind of a bipartisan

level view of the nature of the problem and what needs to be done.

The second panel will focus on how we can use savings and investment to strengthen the Social Security system, and there we have two witnesses who will advise us on whether this is best done through personal accounts or by collective investment of the Social Security trust fund by the Government itself.

The third panel will focus on how Social Security reform will impact on women, a subject that has drawn a lot of commentary in the press and elsewhere and one that is obviously important since more than half of us in the country are women.

We will then break for lunch and be back at 2:00 and start with our fourth panel, which is a panel that consists of eight citizens, selected from among the many citizens who wrote in, and simply have citizen comments on this.

One of the things we wanted to be sure to do was to hear from -- and I hope none of the eight of you will take offense by me putting it this way -- the man or woman on the street. You know, what does the typical American who is covered by this system and who, in their retirement, will look to this system for some measure of support, think about the current state of affairs and what we should do about it.

Our fifth panel will focus on perspectives, other perspectives and experiences, both from the international community and from the state and local levels, including the local San Diego retirement system, which I think has some interesting observations to share with us.

And finally, our sixth panel will include a number of so-called experts on the Social Security system who have offered to testify so that we will hear from -- we will run the gamut from those who have been studying this system and this problem professionally for years and years to just the average person in the street and hopefully capture the full range of -- or as much of the range of insight and expression as possible.

So again, we welcome you, we appreciate your interest and desire to be a part of what we think is a very important matter affecting all Americans. And with that, I want to welcome and call upon our first witness, Mr. Robert Bixby, who is executive director of the Concord Coalition.

Mr. Bixby, I would ask you, and as I will be asking all of the panelists and testifiers who come after you, to limit your oral presentation to about five minutes, if you can, which gives us an opportunity to sort of ask questions and interact with you and saves time for those who will come behind you. Thank you.

THE NEED FOR REFORM**By Bob Bixby**

MR. BIXBY: Thank you very much, Mr. Parsons, and I can assure you that in five minutes I can certainly get into that trouble that you mentioned, unimpeded or otherwise.

Let me first thank the commission for inviting me to testify on behalf of the Concord Coalition and its co-chairman, Warren Rudman, a Republican, and Sam Nunn, the Democrat, and former Commerce Secretary, Peter G. Peterson, who is the president of the Concord Coalition. We very much appreciate the opportunity and we very much appreciate the service of this commission.

All of you are volunteers. You could be doing other things, and you are choosing to do this, and we appreciate this service.

I will concentrate my remarks today on the need for Social Security reform, rather than the specifics of any reform options, because I think it is important. Sometimes we get a little bit ahead of ourselves on the debate on Social Security reform and start talking about the pros and cons of various reform options before fully consider the nature of the problem and without stopping to consider the full consequences of doing nothing.

The first point that I want to make is that Social Security reform really needs to be considered in context.

Social Security doesn't exist in a vacuum.

The truth is that this country, along with the rest of the developed world, is about to undergo a very costly and unprecedented demographic transformation. Now, the General Accounting Office in Washington has estimated that without changes or reforms the combined costs of Social Security, Medicare and Medicaid will double as a share of the economy by 2030 and nearly triple by 2050, and that is demonstrated in that chart over there.

This can only result in one of three outcomes: Large tax hikes, resurgent and unsustainable budget deficits or the withering away of the rest of government, allowing spending on every other priority, from education to defense to infrastructure to wither away. Certainly none of us wants that as a result.

Now, turning to the specifics of Social Security, three conclusions stand out. One, and probably the overriding one, is that changing demographics make the current pay-as-you-go system fiscally unsustainable over the long-term. And as the chart shows, this is nobody's fault. It is a matter of demographics.

There are going to be fewer workers paying into the system relative to the number of beneficiaries. And one thing that isn't always appreciated is we know that there is a growth in the retired population, but the work force growth

slows pretty much to a crawl over the long-term; to nearly less than a percent a year. Much slower than it is now.

This combination of factors will have a profound effect on Social Security's finances. In a chart that you used in July and to great effects -- so I thought I would repeat it. But it really is a good chart because it shows the basic trend lines; what is going to be happening in the future.

And it shows that in 2016 Social Security, which is now running ample surpluses, will begin to run deficits. These deficits will have to be financed out of general revenues from the Treasury. Between 2016 and 2038 it will cost somewhere over \$4 trillion to redeem the bonds in the trust fund, and by 2038 the trust fund will be depleted, leaving Social Security being able to pay 73 percent of promised benefits.

The chart that is up there just shows the difference between the short-term surpluses and the long-term deficits. Closing the gap in that year, 2038, requires a benefit cut of about 27 percent or a payroll tax hike of over 40 percent. Those are the options of doing nothing.

That is what former Senator Bob Kerry has written to you or spoken to us about, is the do nothing plan. Those are the options under the do nothing plan.

Let me close my prepared remarks simply by saying

that increasing savings is essentially to address this problem. We can make changes to Social Security, but we also need to remember that big picture issue of trying to grow the economy bigger in the future so that tomorrow's work force will be better able to afford the burdens of us aging baby boomers that we will place on them. So whatever you do in Social Security reform, increasing national savings has to be key to that.

And finally, this is really a generational issue. This is really about generational responsibility. The program is in fine shape for today's retirees and those who are about to retire. But it is not in fine shape for say somebody who is even 30 years old today, because I was just thinking about it. Today's 30-year-old is going to qualify for full benefits in the year 2038, and that is the year when the trust fund is insolvent.

So, if you are 30 years old or younger, it is not an abstract problem for you. And another thing to think about is that today's newborn -- if you are today's newborn, you are probably not thinking about the Social Security system. But those of us who think about newborns ought to be thinking about their future, and the Social Security system, in its current form, begins running a cash deficit before they even enter the work force.

So I have those comments as a lead off. I hope I

didn't get myself into too much trouble, Mr. Parsons, and I would be happy to take your questions.

CHAIRMAN PARSONS: We will see if we can't get you into a little bit more trouble than you haven't managed to do yourself. Let me start by saying I am going to ask my fellow commissioners to joint me.

But obviously, Concord has been around for quite a while. We talked a little bit about it. But could you give us a little bit more background on the group that you are working with and representing in terms of its genesis, its membership and its goals so that we have an understanding of where this testimony is coming from?

MR. BIXBY: Sure. The Concord Coalition was started in 1992 by the late Paul Songas and Warren Rudman and Pete Peterson. At that time we had large and unsustainable budget deficits facing us, and the whole fiscal policy of the nation was on an unsustainable track.

So the Concord Coalition was designed to work on a bipartisan -- really, a nonpartisan manner to try to bring about a sustainable fiscal policy. The first step would be trying to run annual balanced budgets. The second step would be trying to do that, excluding the Social Security surplus.

And then the third step is trying to reform the entitlement programs that are driven by the demographics; that if left on auto pilot, will make it impossible to run a

sustained fiscal policy over the long-term. So that is really where we are coming from. And then, when Paul Songas passed away in '97, Sam Nuun became the co-chairman.

And a lot of -- you know, it has always had a generational responsibility aspect to it. This is something that -- it is our job to fix this problem now for future generations.

CHAIRMAN PARSONS: Okay. Let me open it up to the commissioners assembled. Questions? Gwendolyn.

MS. KING: Thank you, Mr. Parsons. My question is a pretty basic one. I have three children; 35, 36 and 38, or thereabouts.

And as you pointed out, for a 30-year-old who is facing retirement at the same time the trust funds run out of money, it is going to be very hard for us to convince them that they should continue to sustain today's retirees for the future, if, in fact, when they turn 68 years old -- and I hope those cell phones disappear.

MR. BIXBY: I hope it is not mine. No. It is not. No.

MS. KING: They stand to gain nothing if we do nothing. From my perspective, we have a 30-year lead time in which to make changes as soon as possible that will make sure the system is there for them.

So my question of you is -- after I thank you for

laying out what you see is the problem, and I think most of agree with you that that is the problem and part of the reason why we are here. My question to you is what to do about it.

We are looking to the strengthen the system; to take advantage of the lead time that we have. We don't want to waste time. We know that doing nothing is not a viable option.

There are people who just say you can tinker with the system, and from my perspective as the former commissioner of Social Security, we have been tinkering with the system for many years now.

Does your coalition have some recommendation for us about a bold step that needs to be taken early on right now that you would like to share with us, because we are really looking for some input here?

MR. BIXBY: Well, here is where I can get into trouble.

CHAIRMAN PARSONS: I was going to say now you have got it.

MR. BIXBY: Here is my opportunity. Actually, we have avoided recommending or coming up with a specific plan. Again, because of our concern that people don't necessarily have it fixed in their head yet that there is a serious problem. So we like to concentrate on the problem.

But on reform strategies I do think that there are two things that are essential. One is restraining the growth of the current system, and that is, generally speaking, called the hard choices. But I don't see how we can reform Social Security to make it fiscally sustainable over the long-term without that.

And that has to take place regardless of whether we do private accounts or don't do private accounts, whether we pre-fund inside the system or outside the system. Those charts before that showed the imbalance between the benefits and the tax rate just inevitably mean that at some point either those -- the tax rate has to go up to a very significant level. You know, 18, 19 percent, and over 20 if you add in Medicare. Well over 20. Or, something needs to be done to sustain the benefit gross.

The fortunate thing is that you don't need to take option -- you don't need to do something to effect immediate benefits, because we do have this surplus for several years for now. So the type of -- this issue of benefit cuts always gets interpreted as, gee, you are going to cut today's recipients.

Look, my Social Security benefits have been cut twice, and I didn't even know about it. In 1977 and 1983. That type of benefit cut is the thing that we can do now, because it is phased in over several years, and so people

have time to work it into their planning. It makes the system fiscally sustainable.

So whatever -- you know, whether it is raising the normal retirement age, which is going up to 67 -- you know, there is a hiatus period. So one would save money to close that gap. You know, raise it further or close it faster.

You know, you could do something with the indexing of the benefits formula to alert is so that it is not linked to wages, so that it doesn't grow progressively in real terms over time and going to an inflation index benefit would result in too much -- not enough savings up front and too much savings over the long-term. Perhaps, you know, you could balance it. There are other changes that could be made to the benefit formula.

But my point is essentially that I don't think we can do this without any -- I'm sure we can't do this without any of those choices being made, and maybe it is wrong that they are called hard choices. I don't think they are that hard.

I mean, being a hard choice would be going to 2038 and then saying we have got to cut your benefits by 27 percent because we have no money. Or we are going to have to raise taxes, which is probably what would happen.

MS. KING: And those would be real cuts in benefits.

MR. BIXBY: Exactly. That would effect current people.

MS. KING: Today you are talking about slowing down the amount that the benefit will grow.

MR. BIXBY: That is right.

MS. KING: As opposed to cutting someone's check.

MR. BIXBY: That is right. And the second strategy -- that was all just the first strategy. The second strategy is what I spoke of before, which is increasing savings, and there are perhaps two strategies in that.

One is, you know, increasing the resources that are devoted to Social Security, and if we start now, over time they would build up. And if it is done through individual accounts, for example, younger people that begin to set aside some money in those individual accounts today, that money would be there to help -- it would be directly pre-funded their Social Security benefits over the long-term.

And so, that would mitigate some of the changes that need to be made to bring the rest of the system into fiscal balance over the long-term. It is not a quick fix, and it is certainly not a free lunch.

As the Concord Coalition has said many times, we favor pre-funding more of the system, but that means coming up with money to do it. And no matter how you do it, that means that somebody is going to have to start paying some

more money or workers receive less -- I mean, beneficiaries receive less over the long-term.

So nobody should think that just adding private accounts to the system is going to balance the system, but it is a way to increase the savings devoted to Social Security, and hopefully, at the same time, increase net national savings which is important to make these long-term burdens more affordable for workers in the future.

MS. KING: Thank you.

CHAIRMAN PARSONS: Thank you, Bob. I realize that I missed a step here. I introduce you to your inquisitors, but I didn't introduce your inquisitors to you or the audience. So let me do that now, and then we will get back to the questions.

On my far right and the audience's left is Professor John Cogan. John is with Stanford University now, but is a former director of OMB, which probably, next to the presidency, is the toughest job in the Federal Government.

Jim Penny is to John's left. Jim is a former Congressman from Minnesota and now affiliated with the Coalition, among other watchdog groups.

Gwendolyn King, who just introduced herself, is a former commissioner of the Social Security Administration and now runs podium pose.

Fidel Vargas, who is our former Mayor of -- is

Baldwin Park? Baldwin Park, California. Another tough job; being a Mayor closest to the people. Now with Reliant Equity.

To my left is Gerry Parsky who, in addition to being a local boy, is with Aurora Capital and former Assistant Secretary of Treasury.

To Gerry's left is Estelle James, who is with -- a consultant now with the World Bank. I always loved that name, the World Bank. It sounds terribly solid. To Estelle's left is Mario Rodriguez, who is President of the Hispanic Business Roundtable.

To Mario's left is Tom Saving, who is one of two public trustees of the Social Security Administration and is a professor at Texas A&M. And rounding out the field today to Tom's left is Leanne Abdnor. Leanne is former executive director of the Alliance for Worker Retirement Security. And I, of course, appreciate all of you coming to San Diego today to be a part of this as well.

Now we will move on with the questioning. Gerry and then John.

MR. PARSKY: Thank you, Mr. Chairman, and welcome, all of you, to San Diego. I just want to reiterate a little bit about what the Chairman said to make sure we have the framework for the Concord Coalition.

You characterized the group as cutting across the

political spectrum; bipartisan, nonpartisan. How would you characterize the make up of your group again?

MR. BIXBY: Well, it is basically nonpartisan. We have a -- we go out of our way to be bipartisan when we work on congressional issues, and we have a bipartisan chairman. We have grassroots members around the country and a field organization as well.

MR. PARSKY: Great. I think it is important to kind of make sure we understand that perspective. I would like to just focus on a couple of statements, one that you made in your oral statement.

I gather that those that would do nothing it would be appropriate to characterize as advocating tax increases in the future?

MR. BIXBY: Well, that is the inevitable consequence of doing nothing.

MR. PARSKY: I think a number of us would probably feel the same way; that those people that would say that nothing needs to happen to the system are really calling for tax increases.

MR. BIXBY: Or benefit cuts. I mean, --

MR. PARSKY: Right.

MR. BIXBY: In a political sense, I think I would guess that it is more likely that there would be a tax increase than a benefit cut.

MR. PARSKY: Okay. The second thing I kind of wanted to focus on was that I think in your statement you indicated that between 2016 and 2038 that the Social Security system faces a cumulative deficit of more than \$4 trillion in today's dollars. Right?

MR. BIXBY: In today's dollars. Right.

MR. PARSKY: Then you go on later, I think, to say in your statement that Social Security assets consist of the Treasury IOUs that can only be redeemed if Congress raises tax, cuts spending, uses surpluses or, in your words, borrows from the public. Therefore, the existence of these IOUs alone don't ease the burden of paying future benefits. Is that right?

MR. BIXBY: That is correct. Yes.

MR. PARSKY: Now, that sort of language I think has gotten a number of us and the commission generally in some trouble even before we started to think about our recommendations.

MR. BIXBY: Welcome to the group.

MR. PARSKY: So I want to be sure that at least there is some support coming from your nonpartisan, broad-based group that would support those underlying concepts. That is your point of view?

MR. BIXBY: Yes. And I don't think that -- this is going to sound strange to all of you. I don't think that is

a controversial description. I mean, it may have become controversial, but it is -- people get really hyper about the trust fund, but it is fairly simple to explain what goes on with it.

They are bonds credited to the trust fund. They do have the full face and credit of the government, and they are assets to Social Security and they are, at the same time, liabilities to the Treasury. So, if you are the Social Security Commissioner, you say, I have got these assets. If you are the Treasury Secretary, you say I have got these liabilities.

For those of us in the general public, you know, we need to understand that the assets that are building up in Social Security's trust fund are liabilities that will have to be satisfied out of general revenues at some point.

MR. PARSKY: Thank you.

CHAIRMAN PARSONS: John.

DR. COGAN: Thank you for your superb testimony. It is a very, very good description of the problem.

Our job is a difficult one, on the one hand. But on the other hand, the way I have thought about this is we are providing young people with an opportunity that they don't right now have. Most young people don't expect to get much out of Social Security, and my belief is that if we can fix the system and provide these young people with personal

accounts, we will be giving them an opportunity that will improve their lives.

And so yes. We have hard choices. Yes, they are tough. But the reality is in the end we are creating opportunities. That is the way I see it.

You mentioned the difficulty of making the public understand the dimensions and the scope and the timing of Social Security's problem. You also said that doing nothing is tantamount to a tax increase.

Can you give me some way of explaining to the public just how large this tax increase will be? That is, can you take it from the aggregate down to the level of a typical individual? That is, if the solution to providing benefits, the financing benefits, is to raise the payroll tax by 50 percent, for a typical American couple, how much money is that each year?

MR. BIXBY: Well, it depends a lot of their payroll. But on the payroll tax it gets up to, you know, about 18 percent of payroll, and we always have to consider up to the taxable maximum. And if we add on the Medicare, if we let Medicare rise also, let the Medicare payroll tax rise also, you get up into the -- you know, around 24, 25 percent of each worker's paycheck by 2030 or so. And people can do the math to figure out what that would mean for them.

You know, you truly have to think about is that the

legacy that we want to leave to today's newborn? You know, this is a system that if we do nothing, the first 25 percent or so of their paycheck is going to go to Medicare and Social Security.

DR. COGAN: So for a family that is making \$30,000, the husband is making \$30,000, the wife is making \$30,000; a \$60,000 income, the increase would be in excess of \$3,500?

MR. BIXBY: Yes. And, of course, that is just in payroll tax. They are going to have to pay other taxes as well.

DR. COGAN: Right. Now, if you chose to finance the unfunded liability through hikes in individual income tax, you would have to raise individual income taxes by what? Twenty-five percent?

MR. BIXBY: I don't know. I don't have a number for that.

DR. COGAN: Well, I made a little calculation. You said that for Social Security the system is now costing about four percent of GDP. It is going to go up to about six and a half percent of GDP. The gross domestic product now is about \$10 trillion. So it is going to go up about two percentage points in gross domestic product.

Each percentage point is \$100 billion in today's dollars, and so we have to raise annual taxes in today's dollars by about \$250 billion if we wanted to just finance

Social Security, not including Medicare. Individual income taxes are about \$1 trillion now, and so it is about a 25-percent increase in each and every individual income tax component.

So it is an across-the-board increase in rates of taxation, it is an increase in the tax on Social Security benefits, it is a 25-percent increase in the estate tax, it is a 25-percent increase in the alternative minimal tax and so on and so forth. So it does strike me that if you, Concord Coalition, can put these things in individual terms to show how individual taxpayers can be affected by this option of doing nothing, I think it would be a great help in the public education effort.

MR. BIXBY: I might mention that those GAO numbers that I used earlier are even higher as a percentage in GDP, because they make some assumptions about what would happen to a GDP gross if we need to fund -- borrow to fund the Social Security benefits. And so actually, their numbers, which they are going to update next week -- and we will have a new scenario from GAO next week, but it will look pretty much the same.

Social Security as a percentage of GDP is actually a little bit higher, and so is Medicare and Medicaid than the trustee's report. So...

DR. COGAN: If I might make on additional point. There seems to be an eroding of confidence, as you pointed out, in the Social Security system, and that eroding is particularly acute among young people. One reason that it is a so acute is that because they perceive Social Security to be of less and less value to them. They don't believe that they are going to get their benefits.

Even if they were to somehow get the promised benefits, what would the rate of return be to a typical person in their 20s today?

MR. BIXBY: Well, it would be about one percent or less. Very, very low.

DR. COGAN: And if you chose to solve this problem by raising the amount that they have to contribute to the system, you would just make that rate of return even lower, wouldn't you?

MR. BIXBY: Yes. Exactly.

DR. COGAN: Right.

MR. BIXBY: That is one of the inevitable consequences of a maturing pay-as-you-go system; is that the early retirees -- early people didn't get a very good return because they didn't pay too much in, and then over the time the people will get a worse return because it needs to fund the debt overhang from the earlier part.

And again, that is nobody's fault. It is the

design of the system. It was inevitably going to happen, and the question now is what do we do about it going forward?

DR. COGAN: Thank you very much.

CHAIRMAN PARSONS: Fidel and then Tim.

MR. VARGAS: Bob, thank you for taking the time to be here with us. First of all, I want to apologize to the commissioners. I was running a little late from the traffic down from Los Angeles. I, fortunately, made it not too late.

MR. PARSKY: There is no penalty here.

MR. VARGAS: Thank you.

DR. SAVING: We haven't exacted it yet.

MR. VARGAS: No. Not yet.

You know, one of the things that actually -- Gwen mentioned this and, John, you brought it up in your comments, which brought into focus something for me. You know, I am eligible for Social Security in the year 2035. So for me obviously, as one of those young people, this is a very important issue.

But on a topic related to what you were saying and something that I have been hearing and thinking about, a lot of people from both political parties think that the solution or a solution to Social Security's problem is the so-called lockbox, which is the surplus to pay down public debt.

I, like many other people, think that is a good pistol policy to pay down government debt, and I now you feel

the same way. But do you think that the lockbox is the best way to address the Social Security's problems?

MR. BIXBY: No, I don't. I think that in the absence of anything else I will take it, because in recent years the commitment to use the Social Security surplus for debt reduction has been the only sort of fiscal firewall in town. But as recent events have been showing, whether or not that firewall can actually hold is yet to be tested.

So the problem with the lockbox is really twofold, and again, I don't want to denigrate it in the sense that I think it is a good idea, in the absence of doing anything else, to wall off the Social Security surplus and use it for debt reduction. It is not only fiscally responsible, but it does help with the long-term problem of increasing savings and freeing up resources within the budget.

The reason that it is not -- that I have some skepticism of it is that first it is very difficult to enforce, for one thing. You know, it is a goal that can only be met by insuring that members of Congress and the administration will, year after year, be able to keep their hands off of the Social Security surplus, and that is difficult to do, you know, as we are seeing. Sometimes through no fault of their own. The economy weakens or whatever.

So, it is not as strong as it may appear to be; the

lockbox isn't very strong. The second part of the lockbox is that even if we were successful in doing that, saving the entire Social Security lockbox as projected, it would not solve the problem. It would buy time, but it would do nothing to reduce the long-term costs of the system.

You know, in response to the first question, I said there were two things, increased savings and reduce the long-term cost of the system. This would help us better finance the current system, but it truly is a buying time strategy.

There is a chart over there that I used in the written statement. In present value terms, if you assumed that we were able to save the entire projected Social Security surplus, it is a little less than \$1 trillion dollars, around \$900 billion, and you balance that against the present value of the deficits over the next 75 years of around \$5 trillion or so, and you see it doesn't plug the gap.

Now you can add the current trust fund balance on the top of the present value of the surpluses and say that that prior trust fund balance represent savings, and people can get into a discussion about whether or not that was water over the dam or whether it increased national savings. But even if you add that onto it, you still have a \$3 trillion gap or so.

And so -- you know, in response to the lockbox, I

prefer it to the do nothing in a sense; you know, as a way to help with the problem. But we can insure that it will actually work, and even if it does work, it doesn't solve the problem.

CHAIRMAN PARSONS: Tim.

MR. PENNY: Thank you, Mr. Chairman. Some of what you have just said in response to the question by Mr. Vargas may also apply to the question I am about to ask, because if you assume that we can draw on the trust fund, you still face the eventuality of the Social Security running out of any claim on those dollars by 2038, and then we need to find a way to fill the gap, which will be about 25 percent of benefits annually at that stage.

One way to do that would be, as you said in your testimony and as other experts, including the Social Security actuaries themselves, to increase the payroll tax rates by 40 to 50 percent. That is taking it from about 12.4 percent to roughly 18 percent, a five or six percentage point increase in payroll tax rates.

Others, however, have said that we really only face a 1.86 percent -- or really only face the need for a 1.86 percent increase in payroll tax rates to save the system. You called that a myth in your written testimony.

Can you elaborate on why you referred to that solution as a myth, or that proposed solution as a myth?

MR. BIXBY: Well, it would -- it is not a myth if the goal is to try to bring actuarial balance to the system.

But the reason that we have referred to that as a myth is that bringing actuarial balance to the system doesn't really solve the problem because it is a 75-year average. It doesn't change the nature of the problem. It pushes it out a couple of years.

Actually, I do have a chart that shows the 1.68 solution. What that would do is temporarily -- well, not temporarily. It would bring in some more payroll tax immediately, which would be credited to the trust, and so the trust fund balance would be extended out. But you still have the same basic problem. It just starts a couple of years earlier. I mean, a couple of years later.

And you really -- it is just feeding money into a system, you know, that has got a hole in it. And so it really wouldn't do anything to cure the problem that we are -- you know, that you are looking at.

MR. PENNY: It doesn't help us solve the cash flow problem except marginally in the long-term.

MR. BIXBY: That is right. It pushes it off, you know, a couple of years. But the general trajectory of the problem remains the same. By the way, that is about a \$77 billion tax increase I think in one year to do that. It is roughly around eight percent of -- that number I did have,

Mr. Cogan.

MR. PENNY: So the point you are making is that it sounds like sort of a modest little tinkering, but it is a pretty --

MR. BIXBY: Oh, it sounds like. Yes. I mean, it sounds very simple to say all we need is a mere 1.8 percent increase in the payroll tax, and it sounds like, well, how could that possibly be a problem. But it is an increase of roughly about eight percent of income taxes, if you want to look at it that way. And over 10 years that is an awful lot of money.

And like I say, it doesn't solve the problem. It just sort of puts it off a bit.

CHAIRMAN PARSONS: We have time for two more questions. Tom and Estelle.

DR. SAVING: Bob, currently right now something like a third of all of the Medicare benefits are paid out of the general fund of the Treasury, and a lot of people suggest that if we are only going to be at a 25 percent shortfall on Social Security, we could also take that out of the general fund of the Treasury.

Comment on the possibility of that being sort of the long run solution. We will just transfer more money out of the Treasury.

MR. BIXBY: Well, all we would -- what we would end

up doing within about 40 years or so is the Federal Government would be able to do nothing but write benefit checks for Social Security and Medicare or raise income taxes to a level that they have never been at a sustained rate.

I mean, you would have to go, you know, 25, 26 percent in rising of GDP to sustain that sort of thing. So it would result in a very, very different type of government than we have today, both on taxes and what the government is able to do.

You know, it cuts back on -- it eventually cuts into everything else the government needs to do if we just keep on the pay-as-you-go system the way we are going.

CHAIRMAN PARSONS: Estelle.

DR. JAMES: I just have a quick extension to the earlier question about the 1.86, if there were an immediate 1.86 percent tax increase.

It seems to me that -- as you said, that would increase the money going into the trust fund, which either would increase the IOUs that the Treasury then owes the Social Security system later on -- as you pointed out, that becomes a liability of the Treasury -- or the money could be invested outside U.S. bonds. And that gets into the whole range of issues of external investment, which the next panel is going to discuss.

But it seems to me that even if there were that tax increase, that this is another problem; that either it becomes a Treasury liability or you run into a range of problems associated with investing outside the Treasury. Could you comment on that?

MR. BIXBY: Yes. You would still be faced with the build up and the liabilities of the trust fund. So it would actually -- you know, it would increase the trust fund balance, which would increase the long-term liabilities. Where I thought maybe you were going was if you added something on like that and devoted it to personal accounts, would that help fund the personal accounts?

DR. JAMES: That is the third option.

MR. BIXBY: Yes. That is another way, if you were going to -- I mean, if you were going to use a 1.86 solution and use it to help the transition to personal accounts, that might be a different matter. Probably something that the Concord Coalition would be more in favor of.

DR. JAMES: Right.

CHAIRMAN PARSONS: Well, unfortunately -- I mean, I know there are other questions on the part of the commissioners and you are a fountain of knowledge, Bob, but we have got several other people to hear from today.

On behalf of all of the commissioners I want to thank you for leading us off and getting us off to a good start. We appreciate your thoughtful commentary, as well as your written submissions and your responses to our questions.

We are grateful and indebted to the Concord Coalition for making you available. Thank you very much.

MR. BIXBY: Thank you for inviting me.

CHAIRMAN PARSONS: The next witnesses we will hear from are Mr. Kent Weaver, who is with the Brookings Institution, and Mr. John Shoven, who is also from academe from Stanford University and the Hoover Institution, who are going to be making their comments with respect to investment of Social Security funds either by individual or by the government.

Gentlemen, again, on behalf of my fellow commissioners, I want to thank you for making time for us today. You are about to touch on a subject that is of keen interest to all of us, and I think to all people who are following this lively public discussion. So, without further ado, I am going to ask you, John, to start off and then you, Kent, to share your remarks.

And I would ask you both to keep your oral presentations to about five minutes, and then we will have at you.

SOCIAL SECURITY INVESTMENT: BY INDIVIDUALS OR BY THE

GOVERNMENT?**By John Shoven**

MR. SHOVEN: Well, thank you very much for the invitation. I thought you might find it of interest that I am teaching this fall a limited enrollment course for Stanford sophomores, and today is the first day of class.

The enrollment was limited to 14 students. Forty-five Stanford students wanted into the course, but we got 14 in. There was a little conflict that today was the first day of class and I was asked to testify here. So I have flown the 14 students here, and they are right here.

As you may know, I am --

CHAIRMAN PARSONS: Do they get credit?

MR. SHOVEN: Well, this is counting as a class day. So they have to pay attention.

DR. JAMES: And when are they going to retire?

MR. SHOVEN: We left at 4:45 this morning. So they have shown some dedication and interest in this topic.

MR. : That is a real sacrifice, because they are usually getting in around that time.

CHAIRMAN PARSONS: Yes. I was going to say that they should get two times the credit.

MR. SHOVEN: I am, as you know, a supporter of two-tiered Social Security plans. That is, I am a support of retaining defined benefit or formula driven benefit program.

Ultimately I think those benefits will have to be curtailed to live within the budget restrictions we have been talking about, and I am in favor of adding to that a program of individual accounts.

Having both types of programs, each subject to certain risks, actually is consistent with the first principle of finance. Namely, that you should diversify, particularly when you have two programs or assets whose risks are different than the sum of each; is the right answer and now all of one or all of the other.

Let me talk, since I have only a little bit of time, about the advantages of individual accounts over the central trust fund investing in private securities and equities in particular.

The first advantage I would mention is the issue of what I would call asset ownership. With individual accounts, the ownership of the assets is effectively transferred to individuals. But with central trust fund investment, the ownership remains with the government.

The government can deplete its trust fund by creating new benefits or by lowering payroll taxes, and as you know, there have been proposals to do both in recent years. Also, as you certainly know, in 1994 Congress voted to divert some of the funds going to the Social Security trust fund to help support the disability fund, rather than

reform the disability fund. Well, that can happen whether or not there are stocks in the trust fund.

The first issue I would mention is asset ownership. That would be essentially impossible. If the ownership had been divided into millions of individual accounts, the government is not going to be able to come in and divert resources for other purposes.

A second advantage I would give to individual accounts is simply looking at the history of the ability of the government to accumulate large trust funds. The history in the United States is that when the trust fund has been large or when it is projected to be large, new benefits are passed, and it, in fact, it doesn't grow as large as projected.

This happens with the Social Security trust fund. It happens many times. Often on even numbered years, for reasons that you may recognize. They tend to be election years.

It happens for the Medicare trust fund. As you know, we are currently debating how to add a prescription drug benefit to the Medicare trust fund, and there is a whole array of possible benefit increases for Social Security right now, including improving widows' benefits, including changing the calculation for women who take time off to care for elderly parents.

So my point is that it will be difficult to sustain large trust funds, and history certainly shows that to be the case.

A third element I wanted to mention is effectively the impossibility of having a universal -- by that I mean a program that everybody is in -- defined benefit Social Security program with the central trust fund invested in stocks. A defined benefit program is a program where the participants don't bear investment risks. Certainly that is the way we use it in the private sector.

In the private sector it is quite clear what happens. The investment risks are transferred to the shareholders of the employer. The workers don't bear any investment risks.

On the other hand, if you have a universal plan like Social Security invested in stocks, who are you going to transfer the risks to? Effectively, you can't. Effectively, everybody is in the plan, everybody bears the investment risks, and that means it is really not a defined benefit program. It is more like a defined contribution plan.

A fourth advantage that I think is very important between individual accounts invested in private securities and the central trust fund invested in private securities is the matter of choice. People differ in enormous ways, in terms of their financial circumstances, and in their

attitudes towards risk.

The right portfolio might be all inflation index government bonds for some household, and it might be an all stock portfolio for another household. But if the central trust fund does the investing, it is kind of a one size fits all solution. People are not allowed to sort themselves out according to their willingness to hold risk.

So I view allowing people to obtain a portfolio that meets their circumstances as a large advantage for individual accounts.

The fifth concern I have about the central trust fund investing in equities deals with the political pressures that would be felt about which investments to make. That is, I am concerned that the investments would be made for social and political reasons rather than purely financial reasons, and this is not simply a theoretical concern. I think it is a practical problem in states and in other countries.

And just to bring it home, here in California we have one of the biggest public pension programs, CALPERS. CALPERS has 1.2 million participants. Last October the CALPERS trustees voted to divest themselves of all of their tobacco holdings. So they basically you have an index philosophy, but they decided to be index minus tobacco. They sold \$575 million of tobacco stocks last October.

Since last October the portfolio has trailed all of

the indexes because tobacco, oddly enough, has been one of the best performing stock sectors on the market. So this is a case where the California workers have lost because of a political decision to be out of tobacco stocks.

Related to the political calculations in asset allocation or the political investments, is the issue of corporate governance. How is the Federal Government going to vote its share? What is it going to do if there is a merger proposed, which is clearly in the interest of the shareholders, but not clearly in the interest of the economy?

Is the Social Security trust fund going to vote in favor of the merger at the same time the Justice Department is going to oppose in the antitrust division?

There is an obvious conflict of interest, potential conflict of interest, in the governance issues, and I don't think the answer of, well, the Government would have non-voting shares is a very good answer. That means that Social Security participants would have non-voting shares and would have no say about the management of the companies that they are invested in. So I think there are some real problems with central trust fund investment.

Finally, I would say, at least in this regard -- I have one or two other comments after this -- the defined contribution structure, the individual account structure, is extremely popular in the private marketplace. It is the --

when people have choices, both firms and employees, this is the structure they choose.

As you may know and I have written in my testimony, I favor programs -- what I would call matching programs where participants contribute money and the government matches, very much like many 401K plans at work. But I guess my point is these individual accounts are quite popular. I think they could be deemed essentially a universal 401K plan.

And I think, if you have such a structure, you will get the willing participation of young Americans, where I don't think they have faith in the traditional Social Security system.

Just a couple of other remarks. I am going to skip over many of them. I am just going to add one final thing to stay roughly within my time limit.

You could do the country quite a favor if you demanded better overall calculations of the federal budget surplus. As you know, right now the surplus, as it is usually referred to with a \$100-and-some-odd or a \$200-and-some-odd billion surplus, that is counting as the surplus the accumulation of the trust fund assets of Social Security.

Those accumulations should be held outside of the budget, in my opinion, and the government should stop this business of saying we have, for next year, \$158 billion

surplus when about \$157 billion of that is Social Security.

But when you start down that road, you might further advocate good trust fund accounting. Social Security is not the only trust fund we have. Military retirees have a trust. The civilian workers of the government have a trust fund. Actually, there is a highway trust fund.

In fact, if you look at all of the trust funds, the projected surplus for next year is much smaller than the accumulation of assets in those trust funds. That is, the rest of the government is expected to be running a deficit.

Basically all I am appealing for, and you can start with the Social Security trust, let's have more accurate government accounting as to whether we are running a surplus or a deficit so we don't all get confused of why we have \$158 billion and we have got nothing to spend.

And you could do that if you would get the trust fund out of the usual surplus measure, the unified surplus measure, and move to something like a federal funds surplus measure. That would help.

I realize it is not your main mission, although I think it is important in this idea of keeping Social Security secure; would be to get the accumulation of Social Security trust fund assets out of the surplus calculation. Thank you very much.

CHAIRMAN PARSONS: Thank you, John. Kent.

**SOCIAL SECURITY INVESTMENT: BY INDIVIDUALS OR BY THE
GOVERNMENT?**

By Kent Weaver

MR. WEAVER: Thanks very much. I want to thank you again for the opportunity to testify before the President's Commission to Strengthen Social Security on this critical issue of whether Social Security funds should be invested collectively or through a system of individual accounts.

This, of course, is clearly related to the larger question of the extent to which Social Security should keep its current character as a program paying a defined benefit and is removed from risks of market fluctuations and inflation and move towards a system in which individual accounts play a greater role.

I think most observers accept the need for a multi-tiered retirement income system that includes a minimum floor, some kind of defined benefit, some form of tax advantage or mandatory retirement savings and voluntary savings for retirement on top of that.

Most industrial countries, including the United States, have adopted a mixed system. The questions we have to ask are which mix of those tiers is appropriate, what is affordable and how much room do we have to change, given our past choices. And if we do decide to change, how fast should we undertake those changes?

My perspective is a bit different from John Shoven's. I am a political scientist, and my research in recent years has focused mostly on the experience of other advanced industrial countries as they confront their pension issues and trying to figure out what lessons the U.S. can learn from those experiences.

But nevertheless, I think there are a lot of things on which John and I agree. I will state those first, and then some things on which we disagree.

First of all, I think we disagree that the retirement income -- we agree that the retirement income system in the U.S. should have multiple tiers. I think that little progress is going to be made until there is a lowering of the tone of rhetoric; until people on one side stop saying that individual accounts are the devil's handiwork, and on the other hand stop saying that collective investment is the devil's handiwork. There needs to be some sort of mix.

Secondly, I think we agreed that investment in equity, whether it is done collectively or through individual accounts, is not a free lunch that will solve the long-term financing problems that Social Security has. It is more like a healthy snack rather than a free lunch that is going to solve our long-term problem in Social Security.

Third, although I think we disagree on what role individual accounts should play, we agree that if you impose

them, what is the most cost effective way of doing so, which is piggybacking on existing payroll tax deduction systems.

Fourth, I think we agree that an optional carve-out from Social Security is not a good option because it would undermine the financing of the current system. And fifth, I think we agree that removing funds from the current Social Security payroll taxes to fund individual accounts is not a good idea.

But I think there are also some critical areas where we disagree. First, we disagree on the relative importance of the political and economic risks that are posed by the current defined benefit system and collective investment on the one hand and individual accounts on the other hand, and I will focus on those in just a second.

Second, I think we disagree on how big the defined benefit component, a stable, inflation protected benefit should be and should it be more earnings related or closer to a flat rate benefit?

I think the current replacement rates are certainly not very high by the standards of other advanced industrial countries, and I would be reluctant to see any proposal that proposed cutting them significantly.

Third, I think we disagree on whether we can rely on general revenues and voluntary contributions with tax incentives to finance individual accounts or a transition to

an individual account system in a way that will be an effective replacement for part of the Social Security defined benefit.

It appears that a non-Social Security budget surplus, this is in the last few years, are sort of like Brigadoom: One of those things that appears every 100 years or so and then disappears again very quickly; that they are just not politically sustainable. So I am very uneasy about any proposal that relies heavily on general revenue transfers.

Okay. I want to make four very brief points in my testimony. First of all, collective investment of Social Security surpluses I think has some important advantages over individual account plans. Pooling investment and keeping transaction and marketing and reporting costs down can allow higher returns on investments.

Secondly, it lowers the information cost for consumers. And third and most important, a defined benefit with collective investment provides a more stable retirement income that protects against the risks of fluctuating asset values, annuity prices and inflation. Just ask someone who was converting a 401K into an annuity 18 months ago versus doing it today.

Secondly, I think the risk of collective investment can be minimized through proper insulation mechanisms. What

are these insulation mechanisms? First of all, give the investment funds explicit organizational legislative mandates to maximize return on contributors' investment, consistent with a prudent approach to risk.

Secondly, have independent boards of trustees that do not have politicians on them.

Third, and most important, contract out portfolio management to professional fund managers.

Fourth, investment primarily in broad index investments.

And we can see the experience of many state investment funds. I think CALPERS is on one extreme. Massachusetts is on one extreme. We should certainly be aware of the risks that can take place and guard against them, but I don't think that we can make policies based on fears of just a worse case scenario.

I also think it is important, because of worries of fund size, to have multiple funds. Rather than a single collective investment fund, have many. Sweden current has seven to invest its pension savings.

You can index them to the size of the largest private sector pension fund and simply create a new one when they reach that size. That is one way to do it. Another way to do it is simply to mirror the flow of funds into 401K plans. Track those and then push Social Security funds into

the same sorts of retirement investment vehicles, which allow you to essentially mirror the choice that workers are making in the marketplace.

On the corporate governance issue, my suggestion would be simply don't vote the shares. It is not something that is without problems, but I think it is probably the best solution. Again, there are better and worse ways to do this, and these are some suggestions on ways to make it better.

The third point: Individual accounts pose a more complex set of design issues than investing, collectively, the Social Security funds. But once again, there are better and worse ways to do it.

Again, I agree very much with John Shoven about the centralized administration of individual accounts and the potential that it offers to lower the costs providing multiple fund choices. And equally important, in order to make this politically sellable, to lower opposition from employers. Especially small employers who don't want to bear administrative costs.

I also believe that if you are going to move in an individual accounts direction it is very important to require both diversification and to prevent any sort of borrowing against accounts. My concern is that people will think of these as being like my 401K plan that I can borrow against.

If it is supposed to provide a basic retirement

income, I think that it absolutely has to perform that function, period. For that reason I also favor full annuitization requirements, where I think I disagree with John.

But again, my concern is that there will be an erosion of the retirement only purpose over time in individual accounts, as we have seen with 401K plans.

The fourth point: Partial opt-outs from Social Security into individual accounts, which President Bush has favored during the presidential campaign, are not a compromise between the status-quo and privatization. They are the worst of both worlds, and I strongly urge you to reject it.

What are the problems? First of all, opt-outs are likely to lead to exit by higher income workers, which would undermine the funding of Social Security. Secondly, there is great uncertainty created if you allow opting back in, which I think you have to do, because of the different way that defined benefits and defined contribution credits are accumulated.

With defined contribution, if you contribute a dollar early in your career, then you get 40 years of accumulation. Under a defined benefit it doesn't matter when you do it.

What this has done in the U.K. is it has created an

incentive for older workers to opt back in to the defined benefit system, but it is not clear when they should do it. It creates enormous uncertainty in the system.

So, those are my main points. Just a couple of very quick concluding points. Again, I want to reiterate that neither collective investment nor individual investment accounts is the free lunch that will solve all the long-term funding problems of Social Security.

Secondly, I think strengthening the financial viability of the current defined benefit plan needs to be a central if political stalemate is to be avoided. Any plan that the commission proposes should lower the long-term deficit in Social Security.

Third and last, getting the design of collective investment or individual accounts right is as important as the choice between them. There are better and worse ways to do collective investment, better and worse ways to do collective accounts and you have to get those design issues right.

CHAIRMAN PARSONS: Okay. Thank you very much, Kent. We are ready for some questions. We will start with John.

DR. COGAN: Thank you both for coming and testifying. John from Norther California and Kent from Washington. Is that right?

Kent, I am very impressed with your optimism. Here we have got a government run program that has run up a \$12 trillion liability; a massively underfunded system.

We have got a temporary surplus, and you believe that the government can somehow change its gears and invest this money soundly and safely. I would say that we have given the government enough of an opportunity, but I think the debate is going to end up being who do you trust.

Everybody agrees that we could improve the system's finances by pre-funding or investing a portion of the surplus or all of the surplus, and I think the question is going to be who do you trust to do it.

Do you trust individuals to do it? Or do you trust the government to do it?

My question goes to this issue of risk. A lot of people have said or think that the traditional Social Security benefits are guarantee, that they are riskless and that personal accounts and individual accounts and equities carry some risks. I would like you both to talk a little bit about the amount of risk associated with each system.

And I know, Kent, you talked, to some extent, about how to minimize that risk with diversification and so forth.

But I would like to hear also from John about how personal accounts might be established to minimize any risks.

MR. WEAVER: Well, I will just respond to the who

do you trust question very quickly. I think my trust in government overall is probably a little higher than yours is.

But I would say that I trust professional investment managers, and I trust the independent boards of trustees of organizations that I have seen work, like the Canada Plan Investment Board; to hire responsible managers to manage those funds in a way that will protect the ability of the system to pay Social Security benefits in the future.

I don't -- I wouldn't trust members of Congress to run this. My sort of off the cuff suggestion would be that the American Congress should only play one role in managing these funds. They should get to name them.

Members of Congress love to name post offices after themselves and courthouses after themselves, and I would have no problem with, you know, Chuck Grassley Social Security Investment Fund or the Max --- Social Security Investment fund. But other than that, they should keep their hands off.

DR. COGAN: The Gary Condit?

MR. WEAVER: That is your suggestion. I will not go there.

DR. COGAN: Let's go to risk.

MR. SHOVEN: I can start. I think, like you, I wince a little bit when I hear about the guaranteed benefits of Social Security. Quicky, if the benefits were truly guaranteed, we wouldn't be here. Also, if they were truly

guaranteed, they wouldn't have been cut in 1977 and 1983.

As I think everybody knows, the system is largely run, and has been largely run for the last 50 years, on a pay-as-you-go basis. The financial viability of a pay-as-you-go basis depends on such things as future fertility rates, future mortality rates, future immigration rates and future rates of growth of worker productivity.

Those things are uncertain. We don't know what future developments in medicine will do to future mortality rates for instance. And if all of those things which are determining the financial viability of the defined benefit plan are uncertain, then the program itself is uncertain. So it has risks, and that is why we are here.

I would be quick to add the individual accounts have risks as well. They are a different kind of risk, and they partly depend on worker productivity as well, because the contributions depend on wage levels. On the other hand, most of the risk is the kind that we all sort of know. Namely, the risk of stock and bond markets.

Personally, I would control that risk in a couple of ways. One way I think would just occur naturally. People are not going to plunk thousands of dollars one day into the market via these accounts. They are going to probably contribute once or twice a month over 40 years. So this is kind of the ultimate in dollar cost averaging.

Times like now when the markets, I hope, are down, would actually, in some sense, would be opportunities. But some of the times you will be buying equities when they are expensive and other times when they are cheap. So there is the dollar cost averaging.

But I personally think that the menu of what is offered to individuals should be quite simple and quite restrictive. I would have a menu perhaps with as few as four options. The four options might be, first, the ultimate in safety. Namely, a portfolio of inflation indexed U.S. Government bonds.

If you don't want to take any risks, that would be what you would take and that would earn between three and three and a half percent today; real over and above inflation.

The second item I would offer would be a portfolio or an indexed portfolio of high grade U.S. corporate bonds. Slightly riskier than U.S. government bonds, not that much riskier; probably paying a half or one percent better return on average.

The third item I would offer would be an index fund. What I would call a total market index fund. Basically everything in the market.

And the last thing I would offer, and this would be partly for simplicity, would be a balanced index fund; an

index fund which includes both stocks and bonds for somebody who wants just one answer. Just check that one off and you are in 60 percent stock, 40 percent bonds or whatever the deal is. Other than that, that would be it.

You would not be allowed to have a sector fund; to put all your money in biotechnology or something else.

MR. WEAVER: If I can just add on the question of risk. John mentioned sometimes the risk that were imposed by policy changes in 1977 and 1983. Well, in 1977 is more of an example of the risk that policy makers will screw up, which they did in 1972. They had an indexing formula that was incorrect, and that was corrected.

So yes. Some people got overcompensated, but I think you can't say that the most future pensioners got a lesser deal than they could reasonably expect.

Yes, of course, there were cuts made in 1983, but let me remind you what the nature of the biggest of those cuts was. It was an increase in the retirement age that did not begin for 17 years and phased in over the next 20 years beyond that. People had a lot of time to respond to that change in policy. It was a risk that they could adapt to over a long period of time and change their behavior to adapt to that risk.

The stock market decline and increase in annuity prices that has occurred over the last 18 months is a very

different sort of risk that people simply would not have the opportunity to respond to over a long period of time by changing their behaviors, and I consider that to be a significant risk.

On the question of fund choices, let me just add that there are many different ways to do this. I am interested that John says, well, we will just have four or five choices with presumably four or five big funds, which are bigger than the funds that I would propose under a collective investment system, because I would probably see 10 or 15 funds developing over time.

But you can have multiple choices in a low-cost system if it is administered centrally. I brought along the fund choice system for the new Swedish individual account system. Swedes have to look through this and choose from among over 450 different funds that offer a choice of regional funds, money market funds; any kind of fund that you would want.

But because the funds are moved in block by a central agency, the administrative costs are kept relatively low.

MR. SHOVEN: Let me just mention one thing more on risk. In some ways it is a good example, and in other ways it is not.

The 1970s were not a particularly good period for

stocks. Not even a particularly good period for bonds. They also weren't a very good period for Social Security though. Social Security's finances deteriorated a lot. Why? Because there was the baby bust. Fertility was low. Productivity, real wages did not grow much at all in the 1970s. Unemployment was much higher than we ever would have expected at the beginning of the decade, and Social Security turned -- its finances deteriorated a lot in the >70s.

This is just an example that both systems are subject to risks and forecasts that don't quite turn out right. I still believe that in that world you want a sum of each solution.

CHAIRMAN PARSONS: Okay. Now I have got Fidel, Lee, Mario Gwendolyn and Gerry. I think we can probably get that in in the 25 minutes. Fidel.

DR. JAMES: ---

CHAIRMAN PARSONS: Well, Fidel, Lee, Mario, Gwendolyn, Gerry and Estelle.

MR. VARGAS: Kent, just so I am clear, from what I heard you say, you prefer kind of a joint government investment policy, but you don't necessarily -- you are not necessarily adamantly opposed to personal savings accounts and you see that if done properly or done with some consideration, that they actually could potentially work.

MR. WEAVER: Well, I put my maximum into 401K every

month. So I am not inalterably opposed to a personal savings account obviously, just as most people who favor a privatized system I think don't keep their parents from collecting their Social Security checks.

I think the question is what the role that each should play? I think that preserving a defined benefit program that provides an adequate replacement rate should be the first objective. And on top of that, voluntary 401Ks, mandatory savings programs, the kind of matching program that John talks about; I think all of those are worth exploring.

But I think the first question you have to ask yourself is what sort of defined benefit do we want to have?

How big should it be? How much can we afford?

Other countries that have recently partially supplanted their defined benefit programs with defined contributions are Sweden and Germany; were beginning from replacement rates of 66 percent in Sweden and 70 percent in Germany. Those are being brought down, and again, partially supplanted.

We are beginning with a replacement rate that is now 46 percent for the average worker and will decline over time for a worker retiring at age 65. How big a defined benefit do we want to have and what do we do on top of that I think is the first question to ask.

MR. VARGAS: And from where I am sitting and

listening to both of you, one of the things that has been frustrating is, again, the kind of beating each other over the head with who has the right idea. And I think from what I have heard and both of you are saying, you are coming from different perspectives, but you see the value of --

MR. WEAVER: Of a multi-tiered system. Absolutely.

MR. VARGAS: Absolutely.

MR. SHOVEN: If Kent was forced to design individual accounts, I would agree with most of his decisions.

MR. VARGAS: Although you didn't address this, very quickly, in kind of a bullet point fashion, because this is one of the issues that we are dealing with, you both said that neither personal savings accounts alone or investing in equities from the government's perspective would solve the long-term problem.

So what are the specifics? And again, in bold point form. You don't have to explain it. You know, the three or four or five things that you see need to be done in order to deal with that long-term issue.

MR. WEAVER: If fundamental problem can be summarized as over the long-run, the system is short on money, then you have to decide whether you want to get new sources of money. I would probably prefer doing it via a matching program where employees put in or perhaps employers

put in --

MR. VARGAS: Sorry to interrupt. I want you to tell me what you think, not the options. What you think. You have a tremendous amount of expertise on this arena, and I really would like to hear from you; what your solution would be.

MR. SHOVEN: My solution would be --

MR. PARSKY: Are your students listening?

(Laughter.)

MR. SHOVEN: Let me mention the two choices I think you have, and I will tell which one I prefer. Right now real benefits are projected to grow. One possibility would say let's hold fixed real benefits for a period until we can kind of grow into -- until we can afford to raise real benefits.

As you know, benefits go up as real wages grow. They could go up only as prices went up, and that would give you one possible solution. Curtail the growth of real benefits.

The other possibility is -- and you can obviously do this in combination; is to find new revenue. And I think there is a way to find new revenue without raising taxes. That is, set up a matching program where the new money -- the way you get the new money, attract the new money in, is you say if you put in two percent of your pray, the government, basically through a carve-out, would match it and you would

have a four percent account. A combination of a carve-out and an add on, if you want to call it that.

If I were in your position and I had to choose between the two, I probably would go with the latter. I would probably try to find new money in the form of matching money.

MR. WEAVER: Okay. First of all, I think that it is important to set yourself up with a manageable problem. If the Social Security Reform Commission that met in 1983 met -- decided to balance the funds actuarially over the lifetime of the funds, you know, 60 or 75 years into the future, that is a tough task, but a manageable one.

Don't try to solve the problem for all time, because I don't think you will be able to do it. Set yourself a manageable problem.

If you can't completely --

MR. VARGAS: I'm sorry. I hate to interrupt. That is very vague. This is the problem --

MR. WEAVER: Basically what I am saying is if you can reduce the long-term Social Security funding deficit by 80 or 90 percent, --

MR. VARGAS: How?

MR. WEAVER: -- I would go with it. Okay. Well, here are two options. Two options.

MR. VARGAS: Let me say one thing first. I don't

mean to be rude. I apologize. What the frustration is that we need to get specifics.

MR. WEAVER: I understand that.

MR. VARGAS: We need to get as much information as much as possible, --

MR. WEAVER: Fine.

MR. VARGAS: -- and people are reluctant to be specific.

MR. WEAVER: Okay. Here is specifics: Two options. The first one I prefer goes outside the President's mandate. The second one is probably closer to the President's mandate, but further from my preferences.

The first option would be raise payroll taxes by one percent. That would extend the life of the Social Security trust fund to 2054 and allow us to pay 78 percent of currently promised benefits thereafter.

Secondly, use collective investment to further extend the life of the Social Security trust fund. Third, use general revenues to fund some of the non-actuarial elements of the current Social Security system. That is, particularly the high replacement rates that you get on the first dollars of earnings and things like spousal benefits.

Fourth, consider addition of a demographic factor that shares the cost of increased longevity over time. Germany and Sweden are both -- Sweden has adopted it.

Germany has considered it, which is, okay, if life expectancy increases in the future, then that is a risk that we all face collectively. Government will bear part of it and retirees will have to bear part of it.

These things alone would, I think, take care of more than two thirds of the long-term financing problem. I will leave the other third to you.

The second option, again, further from my personal preferences, I call this a bridge building or drawing on what former Texan Agriculture Commissioner, Jim Hightower, called the dead armadillos approach. That is to say there is nothing on the road but yellow lines and dead armadillos, which is where we seem to be going on Social Security.

If we look at the experiences of other countries, the big tradeoff that I think we can see is conservatives accept more money in the form of payroll taxes and liberals accept that that money be devoted to individual accounts; that money not be diverted from the current system, but that more money -- that any additional revenues go into individual accounts.

So, for example, increase the payroll tax by two percent. All that money goes into individual accounts, and the objective that both conservatives and liberals share is keep something like the overall replacement rate from those two things together at about the level that they are now.

If you do that, then I think you need to add a more generous income floor. Our current supplemental security income is a disgrace. Both the benefit levels and eligibility standards are appalling, and we have one of the highest rates among poverty -- poverty among elderly women in the world. But those are some concrete steps.

CHAIRMAN PARSONS: Okay. Lee

MR. SHOVEN: Let me just mention an area of agreement just very quickly. The idea of once the retirement age reaches 67, indexing to longevity is a very good idea. I think we would both endorse that.

MR. WEAVER: I would change the benefits, not the retirement age itself.

MR. SHOVEN: One area would I just philosophically disagree with Kent is that I don't think you want to be looking at other western European countries, like Sweden and Germany, and see if they have got the answer. They have got more problems than we have. They are trying to emulate us. We shouldn't be emulating them at the moment.

CHAIRMAN PARSONS: Lee.

MR. SHOVEN: Just let me briefly disagree with that. They are facing the problems we are facing thirty years from now. So I think we have a lot to learn from them.

MS. ABDNOR: All right. Thank you. And thank you both for being here and your testimony.

I have a follow-up question to Fidel's question of you, and thank you both for being straightforward and specific. We need the specific solutions and your ideas on what we need to do.

In particular, Mr. Weaver, you talked about the trust fund. You know, extending the number of IOUs in the trust fund until the trust fund is extended out 2052 or something like that. But, sir, how can you help us understand? Or do I assume, from what you say then, that because there is IOUs in the trust fund that will then be a draw on income taxes, that, in fact, what you are suggesting is that trillions of dollars of income taxes be used to, in part -- fund the Social Security system. Is that correct?

MR. SHOVEN: No. Absolutely not. What I am suggesting is that money be invested now collectively in markets to get around this question of are there real assets behind the funds. Well, let's -- if Treasury securities are not considered to be real assets, then let's use the current surpluses to buy real assets.

MS. ABDNOR: What would you do with the IOUs that are already in the trust fund? You know, at that point that the Social Security system needs it, would you just ignore those or what?

MR. SHOVEN: No. No. No. My understanding is that Mr. Greenspan is having difficulty finding Treasury

securities that he can buy. So I would say, well, let's let Social Security sell a few of those to the fed and invest those monies in markets and create more real assets.

MS. ABDNOR: Okay. When I first heard about this government investment, the idea of the government investing, several years ago, to be honest, I am still perplexed with what -- it comes down to me as kind of a -- succinctly to put it, which is how does the Government sue Microsoft and invest in Microsoft at the same time?

And I struggle with the issue and I appreciate your comments about how do you keep politics out of it. But when this first came up a few years ago as a proposal -- if I could take a moment to read you a letter that was sent to members of Congress in 1999 by several labor unions about the possibility of government investment, of Social Security's investment in the stock market. And I quote.

AWe are deeply troubled that stock market investment of Social Security surpluses would result in public tax revenues being used to finance the construction of runaway steel mills in Thailand, apparel shops in Malaysia, auto plans in Mexico, electronics plants in China and similar foreign projects undertaken by private corporations.@

AAAt a minimum, we believe that any taxpayer funds should not be used to assist corporations that fail to adhere to certain standards of conduct, such as neutrality and union

organizing drives, paying all of their taxes, avoiding even the appearance of discrimination, providing health insurance and pension benefits and refusing to contract with businesses and benefitting from sweatshops and child labor.@

It seems that the threat of political influence is already with us, even with the idea of the proposal being on the table. You said earlier that you really don't trust -- you do trust fund managers, Mr. Weaver, you do trust independent boards, but not members of Congress.

I am wondering what would prevent members of Congress from responding to special labor groups, business groups, all kinds of special groups? What would keep them from saying, no, I am not going to respond to this pressure that is coming from outside groups? Because you and I both know that that pressure will already be there.

MR. SHOVEN: Oh, sure.

MS. ABDNOR: What will make them not?

MR. SHOVEN: First of all, let me say this is a problem that every country that is considered collective accounts has faced, and I think most of them have managed to step up to the plate and address it fairly well.

The American system, for all its -- one of its major advantages is it promotes a lot of stalemate. It is hard to get a lot of things through if they face opposition because of the multiple beat up points in the system.

Conservatives might oppose buying stocks of companies that do stem cell research, of hospital companies where abortions are performed.

Liberals may not want to invest in Myanmar. They may face the similar concerns that you addressed that labor unions have. I think that it is highly likely in the American political system that once you established a mandate that this will not be done and put it in law and had the other checks in place, that it would be very tough to get it around them.

Why? Because conservatives are going to say, do I want to go along with this proposal that labor unions have proposed? Well, yes. It might set a precedent that I can use in preventing investment in stem cell research companies later on.

But on the whole, I think most groups and most legislatures are more sensitive to not making themselves worse off, to giving an advantage to their opponents than they are to getting something that they want.

Can I say that there is absolutely no risk? Of course I can't. Can I say there is absolutely no risk in anything? No, I can't. But are the risks manageable and is there experience out there with good management practices that have avoided these sorts of influences? Yes, and I think we can follow them.

MS. ABDNOR: Well, I think that if you are -- what you are suggesting is that there will always be an equal and countervailing force. Thus, a stalemate. And I think, if that were the case, we wouldn't have seen a lot of things that have passed in the last few years pass. Or we had better hope that that is what the case is.

I think you have more trust in the willingness of politicians to avoid pressure from a lot of different directions than I do.

MR. WEAVER: Well, the world is full of slippery slopes, but we don't all live at the bottom of the slope in a big heap. So, you know, we have to live with some risks.

CHAIRMAN PARSONS: Okay. Mario.

MR. RODRIGUEZ: This is a follow-up. One of my questions is to John. John, you were talking about CALPERS, how they -- it seems like politics got involved in deciding that they were going to sell certain stocks.

The question I have is how is that -- with that investment fund, how are those decisions made to sell those certain stocks?

MR. SHOVEN: You know, I don't know precisely, but let me give you my impression. The CALPERS board I believe has labor representatives. I think the California legislature has a representative. Maybe the executive branch. So it has a coalition of people representing

different groups.

But in the fall, with tobacco under great attack and legal attack, they made the decision to get out of tobacco. I think it is true, if you went back further in history, you would find they had divested themselves of companies that were doing business in South Africa. So this is not the first time this has happened.

On the tobacco one they may have said, well, we really think the tobacco companies are in a lot of legal trouble. That is actually not a very good reason to sell tobacco stocks. Everybody knew the tobacco companies were in legal trouble and that is why they were so low, and that is why they bounced back.

This decision was not made by financial experts. It was made by, as I said, union representatives, political leaders, but not by financial managers.

MR. WEAVER: Which is the reason to keep them off the board. Incidentally, there is a recent study by Alicia Manell and Anaka Sinden that looks at the investment practices of state retirement boards and finds that there has been substantial improvement over the last two decades in the insulation of most plans.

CALPERS is again an exception and Massachusetts is an exception from that kind of political interfering.

CHAIRMAN PARSONS: Gwen.

MS. KING: Thank you both for coming. Professor Shoven, I struggled on the plane with a paper you wrote on long-term rate of return and got down to the last sentence where you said your best guess was three percent to three and a half percent, and I thought who is this guy who is going to give us his best guess?

But I am glad you did, and I thank you for coming. I was interested in what you call your two-tiered system; that you see the larger Social Security program going forward, but then there is a role also for a personal retirement account.

I would be curious -- and I am not going to ask you to do it all here today if it is going to take too long. But I would be curious to get your views on you transition from where we are now to that two-tiered effort, if you will, assuming that personal accounts become a reality, that we can actually make the transition.

I have been concerned that we not have one independent fund manager. I am sort of far down the road, but it just seems to me that so many people would be involved, numbers like we have not seen before in any program.

Could you give us your thoughts on how those personal retirement accounts might be administered? And when you do that, would you also add whether or not you would

prevent any borrowing at all during the entire lifetime of those personal retirement accounts?

MR. SHOVEN: I believe it is important -- and Kent and I would agree on this -- to contain administrative costs.

So you really do have to look for a simple plan. You have to look for some shortcuts, like raising the money via existing payroll deduction mechanisms.

I personally think you can stay in the world of passive investment or index investment and away from the world of active managers, which costs much more. I would be in favor of -- if you have widespread choice, I would be in favor of having a cap on administrative expenses, and I think you could live with a cap of something like 0.75 percent or something of that order.

I believe these accounts could be -- first of all, I completely endorse the introductory remark; that no person currently receiving Social Security would have any reductions, and anybody near Social Security, you basically wouldn't change their plan. This is a plan for today's young people, and it would take a while to grow into it.

But I think the accounts could be set up rather quickly for young people, and they would be -- these accounts, in some sense, would be immature for a long time, in the sense that money would be set into them, but the withdrawals are not going to start in large amounts for 20,

30, 40 years. So it would take a while.

At first they would be just basically collecting and managing assets. As I have already kind of said, my favorite type of plan would involve a one-for-one match. That is, the government would offer a 100-percent match for individual contributions up to two or two and a half percent of payroll.

Left to my own devices, and I am not on your commission, I probably would have it mandatory to be honest.

But if it is voluntarily, first of all, I think with a one-to-one match, most moderate income and high income people will be attracted by that, and then I would see having a low income cashable credit to make sure that the low income people participate. So I think you can get pretty close to universal participation with a 100-percent match if you do it correctly.

On borrowing I am very much in agreement with Kent, and that was one of the reasons I said, if he was forced to design a plan, I would probably endorse a lot of his designs.

An individual accounts plan. I think you want to restrict borrowing. I do not think you want to say this can be taken out for the first house or for extraordinary medical expenses.

Before you know it, you don't have a retirement plan at all. So I think you want to be very harsh on not

allowing pre-retirement withdrawals.

Personally, I am still open minded on whether you want to completely force annuitization at the time of retirement. In the plan that I wrote up with Sill Scheiber in the book called, *AThe Real Deal,*@ we had that half of the money had to be annuitized and half you would have a choice of what you want to do with it, the argument being half the money came from the government.

The government says, okay, a one-for-one match. Half of the money came from the government. You have to annuitize that. Your own money; you have a choice at the time of retirement.

MS. KING: Thank you very much.

CHAIRMAN PARSONS: Estelle.

DR. JAMES: Okay. I actually had two questions, one kind of broad and one narrow, but time is moving along and we want to make sure to allow enough time for the next panel. So I am just going to ask the narrow question and maybe I can talk to you later about the broader one.

My narrower one concerns annuitization, which you touched on at the end, and Kent has referred to that, because you point out if someone annuitized purchasing a fixed income annuity a year ago, they would have faired much better than if they purchased it today, because they would have had a much larger accumulation in that account a year ago than they

would today.

In fact, I think it is quite risk if you force people to annuitize at a particular date, such as the date when they retire. You introduce a whole new risk that is probably avoidable if the system is well constructed.

So I wanted to ask the two of you for your suggestions on how that payout or annuitization issue should be handled to avoid this kind of date of annuitization risk.

You know, I can think of some ways myself, such as allowing variable annuities, having gradual purchase of annuities and so forth.

But I would be interested in the designs that the two of you would suggest that would avoid that particular risk, which I think is avoidable, if we design it well.

MR. SHOVEN: You know, I haven't thought too much about that. But as you know and have already hinted, there are so-called immediate annuities and deferred annuities. A deferred annuity is annuity that you buy where the payout starts in a few years. Right?

So you could have a system where effectively people start buying their annuities, you know, at age -- I don't know -- 57 or whatever. In other words, they are buying some at 57, they are buying some at 58, they are buying some at 59 and so forth, and they are getting, in some sense, dollar cost averaging on their annuity purchase.

Another feature which you mentioned that is worth exploring is whether you would want to have these annuities have any equity participation. Annuities are great. There is a lot of uncertainty about how long you are going to live. So annuities, I think, are wonderful.

On the other hand, people are retiring at relatively young ages; 62. They have a chance of living 30, 40 years. That is a long time to be out of the equity market. So you don't want just a bond based annuity. You may want to have some equity participation.

But I agree with you. My sense is that the details here can be worked out so that you don't put an extraordinary amount of risk on the level of the market on the day that you retire.

MR. WEAVER: Okay. My answer would differ, depending on whether you consider this to be part of what you would call the basic pension. In other words, are you partially supplanting Social Security benefits or is it something that is an add on?

If it is part of the basic pension, if it is going to supplant part of Social Security, I would require full annuitization. I would have a single annuitizer, the government. I would have the annuity rates be set based on a 10-year average of annuity prices; that it be done on a gender neutral basis.

Recently New Zealand -- one of the reasons that their proposed private account system fell apart was, well, women were going to have to pay one third more for their annuities than men, and how are we going to get around this problem? And they eventually said, well, government will just give women one third more to buy an annuity with.

You know, I think we need to get around that. We need to avoid that problem.

And finally, going back to the question of integrating -- having a more centralized administrative system, I would like to see a statement which says -- that comes out to you every month or every quarter that says this is what your Social Security defined benefit is going to be, and based on your portfolio investments and what we think the current annuity rate would be, this is what your monthly benefit from this component to the system would be.

In other words, to get people's minds off of that big balance, which they then start thinking of this is my money to play with however I want, just like with their 401Ks and think of it as a monthly income stream that is going to have to last them for life.

CHAIRMAN PARSONS: Gerry very quick, and then we will move on.

MR. PARSKY: Just very quickly because I know we are running out of time. First of all, I really appreciate

the testimony both of you had. That is a very complex subject, and you have given a lot of details.

I take away -- this is somewhat simplistic, but correct me if I am wrong. I take away from this panel presentation, briefly, that if we don't invest the payroll taxes in personal accounts, if that is a decision that we moved away from entirely, then the alternatives are raising taxes; collective investment of the funds. Am I missing something?

MR. WEAVER: No. I think that is right, but I think we both agree that collective investment of funds alone won't solve the problem. You are going to have to do something with benefits or taxes.

MR. PARSKY: Thank you.

CHAIRMAN PARSONS: Okay. Gentlemen, very spirited. I hope that the Stanford students felt that it was worth getting up at 4:15 or 4:45 or whatever ungodly hour you were forced to arise. Thank you for your participant, Professor Shoven and Dr. Weaver. We appreciate it very much.

DR. SHOVEN: Thank you.

MR. WEAVER: My pleasure.

CHAIRMAN PARSONS: And I because we are running a little late, we are going to go right into our next panel.

DR. JAMES: Can't we have a 5-minute break? Or I am going to have to miss what they say.

CHAIRMAN PARSONS: We will brief you, because this is going to be my favorite panel. I am sure. Let's be quick about it, Estelle. Be quick about it. Don't pay any attention to Estelle, ladies and gentlemen. I couldn't help myself.

All right. The panel that we are moving into now consists of three distinguished young ladies who are going to talk to us about Social Security reform and women. And our panelists are Suzanne Taylor, who is with the National Association of Women Business Owners, Eloise Anderson, with the Claremont Institute, and Lisa Maatz, who is with the Older Women's League.

Ladies, thank you very much for joining us. We look forward to hearing you. We would ask, again, that you -- we have your written statements, which will be made a part of the record. But for the benefit of those who are assembled here, if you could limit your oral presentations to five minutes each, that would give us a sense of where you are coming from and then a basis on which to sort of launch some inquire.

So, Suzanne, if you would start off, we would be grateful.

SOCIAL SECURITY REFORM AND WOMEN

By Suzanne Taylor

MS. TAYLOR: Good morning, Chairman Parsons and

members of the President's Commission to Strengthen Social Security. Welcome to our lovely State of California, and I must say I am pleased that the experts preceded us. That makes our life a little easier, and I can just talk to you a little bit about small business and being a small business owner.

My name is Suzanne Taylor, and I am CEO of Safety Alert, Incorporated, with offices in San Diego, Ventura, Santa Barbara and St. Louis. Safety Alert provides mobile crisis intervention services, training and consulting.

In addition to being a small business owner, I am a founding member of WIPP, which is Women Impacting Public Policy. I am also the past national president of the National Association of Women Business Owners, and I think at this time we are in about 83 cities across the United States.

WIPP is a national bipartisan public policy organization that advocates for and on behalf of women business owners, strengthening their spirit of influence and the legislative process of our nation, creating economic opportunities and building bridges and alliances to other small business organizations.

WIPP and NAWBO represent this country's 9.1 million women business owners. Women business owners today employ 27.5 million workers, voters, and generate \$3.6 trillion in revenue. WIPP has surveyed its membership of 200,000 and

Social Security reform was one of the top five issues that we found.

The Center for Women's Business Research, which was formerly the National Foundation for Women Business Owners, our research arm, found the following statistics for you about the State of California. California has more than 1.2 million women business owners, and that represents 39 percent of all firms in the state. California women business owners employ 3.8 million workers and generate \$549 billion in sales.

There are 102,700 women business owners in San Diego County. This represents 40 percent of all of the firms in the county, and here we generate \$46.2 billion in sales and we have close to 600,000 workers.

The problem for small business: The three-legged stool of Social Security, personal savings and public and private pension plans is being increasingly threatened. The pay-as-you-go system will become a serious drag on the economy and will limit economic growth if it does not reform soon.

The projected growth and the cost of Social Security will crowd out other programs. We are faced with a Social Security system that is unfound, a rapidly aging population and unaccepted low rates of personal savings. We need significant public policy and social responses to these

issues.

Apart from questions of the system's solvency, there are various factors that lead to differential treatment of women under the Social Security system. Women, on the average, live longer than men. Women, on the average, have lower lifetime earnings than men. Higher poverty rates for elderly women persist under the current system, with warnings signs for tomorrow.

Most women owned businesses are small or sole proprietors, thus the FICA tax is the largest and most burdensome tax for these businesses.

American women are more likely to live in poverty during their retirement years than men and are also comparatively more likely to rely on Social Security to provide the majority of their retirement income. The projected cash and balances pose a disproportionate threat to women's retirement security.

The rates of return on Social Security are abysmal, especially for single persons and double wage earners; couples. Small business is severely and more quickly impacted by slow downs in the economy. The current system is a serious threat to the health of small business because of its damaging impact to the economy, the uncertainty of the growth in Social Security base, which must be matched by we employers and the ever increasing cost of other benefits for

employees.

Proposed actions to address the Social Security problem: Congress must stabilize the Social Security system.

This may involve reforms of benefit formulas and/or payroll and benefit taxation, because any reform will, in fact, the current populous and future generations, small and large businesses and the federal budget. In summary, our country's entire economic base.

Each consideration must be carefully analyzed as part of a whole. WIPP and NAWBO's members believe the following principles may apply to the reform process: Number one, permit workers to invest the retirement payroll taxes, FICA, in individually directed personal retirement accounts; insure ownership to women and stay-at-home spouses through a shared earnings rule.

Number two, oppose an increase in payroll taxes. Did I say that loud enough? Number two, oppose an increase in payroll taxes.

Number three, guarantee a safety net minimum government benefit for all retirees that is more progressive and lifts women out of poverty. Number four, preserve the benefits of retirees and near retirees. Number five, oppose government investment in the stock market. And number six, oppose general revenue transfers, primarily income taxes, to Social Security in the absence of structural reforms.

Other organizations have joined with us in the alliance for worker retirement security to support these principles to affect real reform in the system. A viable Social Security reform proposal will reduce a projected growth of tax burdens upon future generations.

Each proposal must be subject to a rate of return analysis that relates total benefits to total tax contributions. We know the problem and must rebuild the structure in a fair and equitable manner. We must concentrate on financial literacy training for society as a whole; any way we can help women invest their money in order to live on it.

The private sector could step forward to reach out to those requiring assistance now when our corporate partners in the financial industry provide a successful example of an ongoing training program provided to novel members through corporate sponsored seminars and conferences in the area of financial literacy training.

Thank you for allowing me the opportunity to present these ideas to the commission. WIPP and NAWBO stand ready to support structural reform in the system together with you. Thank you.

CHAIRMAN PARSONS: Thank you, Suzanne.

Eloise.

SOCIAL SECURITY REFORM AND WOMEN**By Eloise Anderson**

MS. ANDERSON: Good morning. I think it is still morning, and thank you for inviting me. I was asked not to read my paper, which I won't. So I am going to try to come at this probably from a different perspective than you have had anyone else come at this.

For the past 30 years I have spent most of my life trying to undo one of the Social Security titles, which was called AFDC. So my look at this program is probably somewhat different than most peoples' looks that you have had before, because I have looked inside of it very differently than most other people.

So I am going to probably go over some data that you have already heard, but I want to kind of lay out how I am thinking about this so when I get to it, I have got to say you won't fall off your chairs and you will understand where I am at.

Spending on the elderly in this country amounts to about a third of the federal budget. I see this as a move towards socialism, and when I hear people talk about other industrial countries, most of which are high socialistic countries, I see a push towards that. I am very concerned about that.

And then there is half of the domestic spending in

this country is spent on the elderly. I have spent most of life looking at what happens to children and families. This concerns me greatly.

The assumptions of the program that were built in the 1930s had a very different assumptions than we now live in and the demographics were totally different than they are now. When I was born -- I am not a baby boomer. I am older than a baby boomer. So when I say I was born, 53 percent of the males and about 60.6 percent of females were expected to reach 65.

Today 76 percent of the males and about 86 percent of the females are expected to reach 65. So this is a little bit different. Also, in the >40s, when I was a young kid, when a male reached age 65, he was expected to live 12.7 years and a female 14.7. Today it is 16 years for a male and 20 years for a female, and it is going up.

More of us will make 65 and live longer than ever before, except poor people don't have the same kind of life expectancy as wealthy people. We tend to think of poor males as not living as long, but poor females do not live as long.

I tease in my family and I say, if you didn't like the money *Driving Ms. Daisy*, you would hate Social Security.

In the 1950s every 100 workers took care of six Social Security recipients. Now it is 27, and it is going up. So there are a lot of implications into this worker stuff that I

think we need to think about.

The system design is that of a welfare program, except that it is not the poor that are beneficiaries. Low income women have a shorter life expectancy than middle and upper income women. They have a longer work history. They tend to go to work early and work longer years, and they often divorce earlier in their marriages, which is an important issue here considering the structure of Social Security.

Remember, this program is an old age and survivor's program basically, based on the assumption that women stayed home and raised children and then they took care of their husbands, of which many of us don't do anymore, and small income women have more children than middle and upper class women.

Raising children is what most women do in their younger ages and most low income women raise children usually without the support of a male high income. And if they are low income, their husbands are usually low income as well.

They will pay Social Security taxes when they may not be paying income tax. So how I am often looking at this is that low income women, in their prime of their life when they are raising their children, usually take money out of their families to pay for the elderly who are better off than they are.

So, in many cases, the Social Security tax is taken away from children of low income families.

The Social Security system is not a wealth establishment system. We like to think of it as a redistribution system. I agree. Usually it redistributes money from the poor to the wealthy.

When she dies, let's say she dies at 60 and her children are adults, she has not accumulated any property into this system. This money that goes into the system is not hers, and if she is low income, it is usually that she hasn't much else to give her children. This does not go to them nor her grandchildren.

Politics has a lot to do with the purposes of this program, and as I have watched it through the years, depending on who is in Congress, depends on who we get out of it. Now a lot of people think this is an insurance program, but in 1937 I believe the Supreme Court said, no, it is a pay-as-you-go system, which is what we like to call it.

But what does that really mean? Isn't that kind of really hiding the fact, when we say it is a pay-as-you-go system, that it is really a welfare system, like we would like to call it something else?

So one of the things that I think we need to do in this country is be honest with the American people about what this program really is and what it is not, so that we won't

get so panicky about talking about change.

I believe that gradually, because nothing that we do fast usually works out well -- I am not even sure gradually works out well when government is involved in it. But we should gradually move to a personal account system and where we need to have lots of education behind it, particularly in our high schools. We need to have serious economic classes in high school so students actually understand the system that they live and actually begin to understand how to invest and think about that.

The most conservative programs right now actually pay a better return on the money than Social Security. So even an all bond program would do better than this present system than we have now.

The very people that have been badly educated or not educated in our present system will, in the future, have to bear the burden of paying for the people who are now living much better than them. I believe, without a serious change, we are going to be setting ourselves up for generation warfare. Now, why do I believe that?

One is that we have a system which people who are getting the benefits will tax the other people who have to pay for it. And as we have more and more older people in the system compared to younger people, what will they do? They will tax people who have to pay for it, which I believe will

set up a revolt in this country.

The next one, which bothers me even more, is that there are less and less households with children in them, which means families who have children have less and less voice in terms of how to protect themselves and their children from what I would consider the taxpayers finding out how to go to the pool and take care of themselves.

So my concern is that if we stay in this system long-term, the very people that cannot afford to pay for this will have to carry on their backs a larger part of this population. Thank you.

CHAIRMAN PARSONS: Thank you, Eloise.

Lisa.

SOCIAL SECURITY REFORM AND WOMEN

By Lisa Maatz

MS. MAATZ: Sure. Chairman Parsons and distinguished members of the commission, I appreciate your invitation to testify on women's profound stake in the Social Security program and commend you for recognizing that a discussion of Social Security and its future cannot be had without addressing the unique state of women in the system, as well as the realities of women's lives.

As the majority of beneficiaries, women are not only the face of Social Security, we are an important constituency of this commission.

OWL is the only national grassroots membership organization to focus exclusively on issues unique to women as we age. While OWL and its members work to improve the status and quality of life for mid-life in older women, we are also concerned about the young women of today, women who remain the most vulnerable to poverty and retirement tomorrow.

My testimony will reflect the following realities of women's lives, some of which have been articulated by my fellow panelists here: Women earn less, we take more time out of the workforce for unpaid care giving, we don't typically receive pensions and we live longer than men.

This result, of course, is that women then are poor in retirement. On this there is little dispute. But OWL further asserts that women can't trust the stock market to make up for lower earnings years out of the work force and a longer time in retirement.

The inflation adjusted lifetime benefits of Social Security are more than a safety net. They are a solid financial base on which women can depend.

Some say the current system does not work for women, using that as a rationale for privatization. If women's retirement security were truly the goal, there are ways to improve equity without radical changes that undermine the social insurance nature of Social Security.

Let me begin with these realities of women lives: As I said, they earn less. Unfortunately for a lot of women poverty begins, especially for women of color, the first day they enter the work force. On average, women earn about 72 cents on the dollar that a man earns, while that decreases to 65 cents for African American women and 52 cents for Latinos.

While I agree with the commission's emphasis on increasing savings, I would submit that you can't save and invest money that you do not earn, which women cannot save their way to parity with men. Women also take time out of the work force for unpaid care giving; in their younger years for child rearing and in mid-life for spouses and parents.

For the average woman care giving will mean about 14 years out of the paid work force. Women also live longer, as we know. If today's trends continue, women will still out live men by an average of about six years. Living longer may be a blessing, but it is also a financial nightmare.

Without the lifetime benefits of Social Security, women would face the very real threat of out living their assets. So the result, of course, is that women are poor in retirement. Today the average woman in America struggles to make ends meet on a limited annual income of roughly \$15,615. This is compared to almost twice that for men.

So, depending on this mythical three-legged stool of retirement, Social Security pensions and personal savings

has never worked especially well for women. Our work patterns and lower wagers make the last two legs unsteady at best, and while not perfect, Social Security is still the most reliable foundation for women's retirement. Without it, OWL estimates that half of our older women would fall into poverty.

A system of private accounts would disadvantage women from the outset. Women would start out with less to invest, would lose the often desperately needed cost of living increases, and because of our longevity, could outlive out assets.

How would a privatized system provide a safety net for divorced women, widows, survivors with young children, women with disabilities and others? Social Security is just that; a social insurance policy to provide security when life takes tragic or unexpected turns.

A 35-year-old widow would probably not have enough saved in her or her husband's private accounts to help keep her family from financial ruin, but Social Security would protect them.

Privatization advocates are pitching such reforms with a lure of a better rate of return, an argument that I think sounds appealing. But I think this is also misleading because it simply compares apples to oranges.

The size of women's Social Security benefits are a

reflection of the lack of pay equity and time out of the work force for unpaid care giving. It is not from a poor return on the dollar, yet you can't compare Social Security's guaranteed inflation protected lifetime benefits, not to mention the disability and survivor's insurance with an individual account that carries no such protections and many more risks.

The commission's interim report also looks at quirks in the benefit structure that could pose problems for certain groups of women. It is true that more than anything else race and marital status will determine a woman's financial security in retirement, but private accounts could only exacerbate these disparities.

The progressive nature of the program is critical for all women. Especially women of color. Further, women of color and their children are more likely to need Social Security survivor and disability benefits, a critical protection of the program that privatization plans have yet to duplicate. Divorced women also stand to lose.

If we use the example of private pensions, under private accounts a woman would no longer be automatically covered by her ex-husbands's work record in the event of a disability, his early death or retirement. Even if she was to win a share of his private account in a divorce settlement, a lump sum could not match Social Security's

inflation adjusted lifetime benefits.

His private account simply cannot offer what Social Security does.

In light of these criticisms, the first question that is thrown at opponent's of privatization is usually, well, what would you do to fix it, and that is a fair enough question. But I think, in some ways, that is also misleading because this implies that privatization is somehow a solution to any potential solvency problem when, in fact, it actually hastens a shortfall by as much as 15 years.

OWL wants to address long-term solvency questions to insure the longevity and the health of this critical program, but we reject alarmist proposals that threaten Social Security's fundamental guarantees. It is a balancing act, and there is no silver bullet. But there are adjustments that can make the system more secure far into the future.

First, Social Security can be strengthened by using general revenues, in addition to the current direct payroll taxes, to guarantee the program will be able to meet all of its obligations in 2038 and beyond.

Second, we should consider making more earnings subject to the payroll tax and credit them benefit calculations, thereby closing as much as 75 percent of the solvency gap. We might also invest a portion of the trust

fun in stocks. This maintains the shared risk/shared benefit nature of Social Security, while potentially growing the trust fund surplus at a faster rate. Private pension plans often use this tactic to share the risks, while maximizing the return.

Lastly, we should discuss increasing the payroll tax for employers and employees around the year 2020. Now I know this is not a favorite option, but this proposal still has a place in the solvency discussion, as you can hear. Every panelist has talked about it in some way or another.

If it helps to preserve the universal social insurance nature of Social Security where no one individual is left to sink or swim on their own, then it may very well be worth the cost.

I thank the commission for the opportunity to testify, and I welcome your questions.

CHAIRMAN PARSONS: Okay. Do you want to start us off, Tim?

MR. PENNY: I guess I could do that. I would like to pose this question to the final witness, Ms. Maatz.

You talk about increasing the level of income subject to the payroll tax as one possible of way filling the gap that will certainly exist as this program moves forward.

Yet, just a few short years ago, our previous President, Mr. Clinton, rejected that notion, indicating, for a variety

of reason, that it would undercut broad base support for the program, making the system more of a transfer program. A signal to certain taxpayers that their return on investment would be significantly worse simply to sure up the overall nature of the system.

How do you respond to that dilemma of public support for a system which almost certainly will be difficult to maintain if our only answer to the system's future is to increase payroll taxes on all workers or to expand the amount of income subject to payroll tax, which will have nothing to do with any increased return for those higher income workers?

MS. MAATZ: Right. I think that is an excellent point, because I think one of the things -- regardless of where we are coming at in terms of Social Security reform, one of the things we can all agree on is the fact that part of the issue is that we don't have the level of public awareness that we need in terms of accurate information so that people understand what their benefits are or what they could be entitled to; what their stake would be in a system that was changed. That is a really good point to follow-up on.

I think part of what is going on now is that in terms of the progressive nature of the program it is not just replacing income and retirement. So we can't look at it just as a return on an investment, so to speak. It is not an

investment vehicle.

Social Security is of a social insurance nature, which means that unfortunately, while some of these folks may think that they are not getting a good return in terms of a rate on the dollar and compare it to the stock market, I think unfortunately -- or one of the things that we need to do is educate them that there are other benefits that they are receiving.

They are receiving disability insurance. They are receive survivor's insurance for spouses and for their children in the event of an untimely death; so that there are other benefits to the Social Security program. And if we educate people to see it more than simply as an investment vehicle for retirement, that they can be, I think, taught to appreciate the other benefits that come to play.

MR. PENNY: Well, if we admit that it is essentially an income transfer program, it is clearly better to admit that by just following your first suggestion to make this a general fund transfer, because that is progressive tax.

What do you see as the benefits or disadvantages of simply dealing with Social Security's future through a general income tax transfer into the Social Security system?

MR. MAATZ: What do I see as the disadvantages of --

MR. PENNY: Pros and cons.

MS. MAATZ: I'm sorry. What?

MR. PENNY: What do you view as the pros and cons of primarily relying on a general fund or an income tax transfer in the Social Security system? You know, based on your answer to the previous question, it seems to me that you don't have a problem with burdening higher income individuals with support for the Social Security system because it supports these safety net aspects, and I think we all want to preserve the safety net aspects.

But a general funds transfer basically makes sure that the contributions are made in progressive fashion and that the benefits paid out are divorced from any anticipation that you are going to get a return in your investment, that you are basically just transferring -- that we are deliberately transferring income in this fashion.

Could you speak to the pros and cons of this approach as opposed to continued reliance on higher payroll taxes for the same purpose?

MS. MAATZ: Well, actually I think -- I don't think any one of these things that I talked about, in terms of items for discussion, would obviously on its own take care of any problem. And so I think part of this is that there would be different elements of this brought into the mix, and other ideas as well.

I don't admit here to be an economist, but I am looking at things from the perspective of my members and the kitchen table economics that they use. So from their perspective, the notion of using general surpluses to fulfill the promises of Social Security is not a bad deal, particularly when, back in the 1980s, some changes were made into the system.

We intentionally increased the payroll tax so that we would build a surplus and so that we could be prepared for the baby boomers. American workers, in good faith, paid that tax, and I don't think they are unreasonable in assuming that that tax money, regardless of all of the discussions that we have had here about whether they are IOUs and exactly what the trust fund is and whether it is an asset or not.

I don't think that -- I think it would be unfair to the American worker to then go back and say, well, that money that you paid as an intent for that surplus is not going to be used for that or that their benefits are somehow going to be cut because we won't use all of it.

MR. PENNY: All of your options essentially rely on higher taxes to deal with the long-term cash flow problems in the system. But in some respects it comes down to this: You pay more, but it doesn't get you more.

So that seems to me to come right to the same point that you have just rejected, that you want all of these extra

taxes to give people some sense of return on those taxes. But if we keep going in that direction, this doesn't buy them anything more. If we keep -- you know, whether it is a general fund transfer, which is income taxes, or a payroll tax increase and an expansion of the income subject to payroll tax.

All of this means putting more money into the system, but it doesn't give any of these individuals any additional benefits back from the system. So doesn't that run out of steam at some point?

MS. MAATZ: Well, I agree with earlier panelist, Mr. Weaver's, supposition about doing some investing in the stock market with some of the surplus funds. So I don't think everything that I am talking about here is going to raise taxes.

I think there are other ways that we should explore to try and maximize the surplus while we have got one, and I also recognize that some of the things that I have proposed as ideas for discussion are somewhat outside of the commission's purview in terms of what you were charged with doing.

But the notion of using additional tax revenue, of using -- of raising taxes on the minimum level of income that is available to be taxed for Social Security I think are all good things that could be used to guarantee this minimum

floor, this minimal level of benefits that people need.

I think one of the things that is important about Social Security is that it is one of the most successful anti poverty programs of all time, and while we recognize that there are things here that we need to fix so that we insure that it is for our children and our grandchildren, I don't think that you throw out the baby with the bath water.

And so what you try to do is keep a program that has these protections and these insurances and this minimum floor for eligible people based on work, and you do what you can then to improve the solvency based on a variety of options that a lot of great minds are working on.

CHAIRMAN PARSONS: Estelle.

DR. JAMES: First of all, in your comments you referred a few times to the importance of survivor's and disability insurance for women, and I just want to reassure that no matter what else we do, there certainly will be survivors and disability insurance provided under whatever reform to strengthen the Social Security program there is.

I mean, no one is thinking of a eliminating that component. In fact, in every country that has introduced a two-tier partially tax, financed partially individual account system, all of these systems include survivor's and disability insurance.

Sometimes the role of providing that is shared

between the public and private sectors, but that insurance is always there and it is always mandatorily there. So I just want to reassure you on that score.

MS. MAATZ: Thank you. I appreciate that. You won't mind if I hold you to it, will you?

DR. JAMES: You see, everyone agrees with me.

Secondly, I have actually been doing some research on the impact of Social Security reforms on men versus women, looking at the experience of other countries. And I am in the middle of that research now. So we don't have all of the results.

But two results -- two kind of generalizable results are clear, and that is, first of all, it sometimes doesn't help matters to just talk about women versus men, but rather, women and men are differentiated in many ways and there are many different categories of women. There are women who work and women who don't work and women who work part of the time and rich and poor women and so forth.

And one of the things we found is that both the old tradition -- and I think these findings incidentally would apply to the U.S. as well as other countries, which is why I am mentioning them.

Both the old systems and the new systems treated these different groups of women somewhat differently. So, for example, it is not unusual in the U.S. and elsewhere that

women who are spouses -- women who haven't worked and are married to men who may be high earners have received rather generous benefits just by virtue of their husbands working.

And in comparison you might look at a dual career family that has only modest earnings, and the woman has been contributing all of her life and may end up getting no additional benefit by virtue of those contributions than she would have if she hadn't made any of those contributions at all.

And so, you could say that those two women receive very different treatment or different returns under the old system, and indeed they will also be treated differently in a new system where one might be contributing to an individual account and the other isn't. So that is one important difference.

You have to think of the needs of different groups of women and prioritize and think which are the most important; which are the most pressing that we should bear in mind. So that is one general conclusion.

The second conclusion is that the impact of both old pay-as-you-go system and a new system that includes a new individual account component depends a lot on the details of how the old system is reformed and how the individual accounts are constructed.

So the two questions I would like to ask you coming

out of that are if you were to prioritize the needs of different groups of women, which do you see as most pressing and most important for us to bear in mind.

And secondly, how would you -- what are some of the detailed changes that you would suggest? There will certainly be a role for a continuation of a pay-as-you-go part of the system. Whatever ultimately emerges from our recommendations, there will certainly be some continuing pay-as-you-go part.

So how do you suggest that that be changed in a detailed way, besides reliance on general revenues? But how would you suggest that the formulas and the distribution of the benefits be changed? And how would you suggest that the individual account component should be constructed so as to bear the needs -- the most pressing needs of women?

MS. MAATZ: Is that for me completely or ---

DR. JAMES: It is for all. I welcome suggestions especially on the second. Well, yes. On both of those. I can say that is a question for all three panelists. Yes.

MS. MAATZ: The devil is always in the details, and quite frankly, I do not envy the commission; your task in shifting through all this information and trying to come up with -- and doing your good faith best effort in trying to come up with something that you think can be plausible. I think that is a difficult task.

In terms of different groups of women, I think there are a variety of different needs in terms of the current Social Security system and certainly any reform system that would be under consideration.

For women of color, who traditionally tend to be lower wage workers and who also traditionally tend to use the disability and survivor aspects of the program more currently, those are obviously issues we need to take into account. What would be the minimum floor of benefits and is that going to be adequate.

What is going to happen precisely in terms of disability issues and survivorship issues, especially for children who are survivors of parents who die early?

I think we also need to pay a lot of attention to what is going to happen to single and never married women, which is an increasing cohort now; women who will never, regardless of the -- kind of some of the inconsistencies and quirks of the current system and be able to rely on a partner, spouse or retirement income.

So again, we need to look at minimum floors of income. We also need to look at some of the disability benefits. Particularly for them. Because in all likelihood, if they are single and never married, they may not have other support systems that will be helpful for them.

Certainly, if we talk about married women, things

that they need that they are going to be concerned about, obviously survivorship issues. They are going to be very concerned about their children if something happens to the breadwinner in their family. It certainly will be concerned about something happening to their spouse and how they are going to maintain the standard of living for themselves and their children.

And also, obviously the widow's benefits there. We know, for most women, that we tend to outlive our spouses. And so part of what every family struggles with when they sit down at the kitchen table is trying to figure out, in the event that this happens, how are we going to handle this?

What are you going to be left with and how are you going to pay the bills and do what you need to do? So for widows, I think that is something that we would have to pay a lot of attention to. I will let my other panelists jump in here on different groups of women.

MS. ANDERSON: I am a believer in owning property, and I think that the old system was structured for male head of household, single worker, women at home raising children. And so, as you look at the benefit structure around anything that could possibly happen, that is the basic design.

I think we probably need to move closer to everybody having their own individual account that is theirs and the ability to, if something happens to them, pass it on

to whoever they want. A spouse, ex-spouse, whatever.

One of the things that is very interesting to me is that people get divorced very quickly, and so a lot of people who reach -- have married early in their life and never get married again think they get a part of their dead ex-spouse's Social Security and find out that they didn't live up to the 10-year marriage rule and they don't get anything.

So you have all these. And then you have got if I marry four or five times, depending on how I do this, I actually more. So, I mean, you have got a lot of games in this system that I think are just wonderful games. But they are not really understandable for most people, and they are still based on the structure of the guy goes out and kills the bear and brings it home to eat and mom is going to fix the dinner.

I think we ought to move to a structure where if you work, you establish an account and that account is yours. And if you are married and something happens to the other, you get that account, because that is the way we kind of do things.

Now there are kinds of other things that happen to people in life. Some of us get disabled, some of us die early; all kinds of things go on and there are other ways to deal with those other issues.

Right now, if you don't make enough money in the

present system, we have an SSI program, which we don't like to talk about it. But it sits there to underpin the poor. So maybe what we want to think about is if we have a floor, it is up to the SSI system. Not necessarily to put that issue inside this program. So you have a retirement program, which we like to call an insurance program, which I beg to differ with you.

But it is a program that tries to do too many things, and my concern is it is like a car. If you have got a car that has all of these little things, when one goes wrong, everything goes wrong in it.

So my view is back out of all of these things we are trying to do in this program and try to do one thing and maybe do that well, which is to provide a retirement program, which is property for people that we can pass on to them.

Now, can we get there fast? I don't think so, and I don't think we can get there fast because you have got people around my age and older who don't believe anything you tell them, because this is what we have been telling them since the 1930s; that this program is something that it isn't.

Then you have got younger people who have no faith in this program at all who are much more willing to invest and take more risks. So you are going to have to try to figure out how to take care of those of us who are older and

want to hang on to this program while you create a new system for those who are young.

And whatever you do, don't make it gender specific. Make it worker. And if you can in any way, make it cover everybody who is a citizen or resident of this country. Don't have it if you work, you get it, and if you don't, you don't and let everybody be able to put in it.

Now, how you create this new monster I do not know. But whatever you do, don't make it do more than one thing. Don't make it try to solve poverty. Don't make try to do disability. Don't make it try to do all of these other things. Just have it be there for retirement, and then let's do all those other things in some way.

And then I think we will get out of this confusion, and we won't be trying to hold on to this because we want to take care of the disability, hold on to this because we want to take care of survivors, because we want to take care of the poor. We can do that in other ways, and that may be a more honest way to go about this.

And we might get far more support if we say, yes, we are going to take care of the poor who are elderly in the general fund. I mean, I know we don't like it, and the reason we don't like it is because of the stigma attached to it. I mean, we might as well put that out there.

I don't' want to be in a welfare program. I worked

all my life. I don't deserve to be in a welfare program. Call it whatever you want to. But in reality, that is what it is, and so my view is to develop individual accounts, figure out how to take care of the poor, figure out how to take care of the disabled, figure out how to take care of the survivors and let everybody who lives in America and works in America be able to go into the system.

MS. MAATZ: If I could just respond, if I might. My concern with a good portion of that is that if we -- obviously, if you dismantle the systems, that it doesn't have all of these other protections. You are taking away the kind of fundamental we are all in this together flavor of Social Security, which I think is actually one of its great benefits.

But beyond that if we, for instance, just made Social Security a retirement vehicle and thought about the issues of poverty and disability issues and survivorship issues later, I would be really concerned about that, because we all know and we have seen it in the last 10 years easily and certainly years before that, that programs for the poor are the first ones to be cut. They are the easiest targets.

You can look at welfare reform five years ago. You can look at a myriad of programs, both statewide and national. But programs for the poor are usually the most vulnerable. So something that doesn't have those protections

I think would be cause for concern.

CHAIRMAN PARSONS: Suzanne

MS. TAYLOR: I am going to jump in with a little different bat maybe. I have been thinking a lot about this, knowing that we were going to testify today, and I think one of the ways that small businesses, which, as you know, is one of the fastest growing arenas, both women and minority owned businesses could help in this is -- I talked a little bit a literacy training program.

I think we need to sit down with our employees and take a look at helping them with their own resources, but also wanting the government to understand that as a small business and a woman owned business my first goal is to pay as much money as I can to my employees.

Eighty percent of my staff are women, and I would say 50 percent are minorities. What that does for me is allow me to bring people into a training program within my own company and to give them higher and higher wages; that if I have to face higher and higher taxes, not knowing that there is going to be a limit, then I have -- as government funded programs I have to reduce my expectations for what I can do in helping people.

And I think we, again as small employers, have an obligation to our employees, and I think that is where -- if we look at how fast women business owners are growing in this

country, minority owned business, work with us so that if we are on a ceiling rate or if we want to pay people more money and -- there is this whole battle around minimum wage right now.

I haven't paid anybody minimum wage. I don't even know when I last did that, but a number of employers do. It is an issue for them. How do you work with us so that we might participate with you as employers and be able to take care of our employees?

And then, for people who don't have that safety net of being in a company that is working towards higher wages for them, that is where I think the literacy program needs to come in, and I think that can be done also with corporate America.

We have an excellent relationship with banks and financial institutions as NAWBO, but it allows us to train our women who are just coming into being a women business owner who don't have all of the tools.

But here is this corporation, like Wells Fargo or Principal Finance, that is saying let me help you learn about retirement accounts. Let me help you learn about how to set it up and structure it so that your employees know what kinds of taxes they should be paying and how they should set aside money, which brings me two other issues.

One is the 401K program. My current company has

been in business five years. I would very much like to set up a program with matching firms, but I am limited by a ceiling in my government contracts which says that that is not really something they want me to get from their funds that they give me. It is pretty much a line item budget.

So how do I set up individual retirement accounts without just saying to my employee, here, you do it. I will set it up for you, but it is going to cost me over \$1,000 to administrate it, and I can't match it; if we had some freedom around that perhaps and being able to set up retirement accounts and the profit margin and not worry about taxation.

The other thing that has happening, I think, out there, and I am sure there is not a lot of sympathy for it, is the dot.com-ers who went in and a lot of young people put their trust in stock options, and now they are paying taxes on stock options that they have lost.

And that is something we need to take a look at too, because as much as we all supported it and the venture money rolled into all of the dot.com-ers, a lot of us out here are running solid businesses everyday. And for women, four percent of the venture capital dollars come to women.

Now, there is something wrong also with that statistics. So, those are just some of my thoughts.

CHAIRMAN PARSONS: Okay. Gwen and then Fidel.

MS. KING: They are excellent thoughts. I thank

you for them.

We have made a point of saying over and over that our intent here is not to alter in any way the survivors and disability programs. I think it is important also to reiterate that our work will not at all overturn or undo benefits that people are currently receiving on Social Security.

Current retirees who are receiving Social Security benefits will continue to receive Social Security benefits, and people who are nearing retirement are also not going to be under the umbrella of the changes we are proposing. For those who are saying what does that mean, does that mean one year away or two years away?

We really haven't settled on nearing retirement. But those who are currently receiving benefits will continue to receive benefits. So I don't want people to be confused by the discussion here around possible changes. I want you to understand what it is we are trying to do.

But specifically, to the points that were raised by Ms. Anderson and Ms. Taylor, I think it is going to be very important for us to think about getting that kind of information and training to people at a fairly young age.

Ms. Anderson, I think you and I are about the same age, from what I could tell from your testimony, and I won't put any numbers if you don't.

MS. ANDERSON: Okay.

MS. KING: But I know that growing up in New Jersey and going through high school and even going through college I somehow missed having to do anything by way of financial preparation, even though I worked from the time I was 16 years old, and I paid into Social Security.

And when I get my personal earnings and benefit estimate form, I see that I actually paid in from the time that I worked. But I didn't really understand how important that was going to be until now that I am staring retirement in the face.

I think if people at a very early age, particularly young women, understand how important it is for them to begin a savings program, it will hold them in good stead as we move forward towards the time when Social Security will not be able to do it all.

And so, I am very focused and very interested in the idea that financial literacy training is something that NAWBO has an interest in. I think it is good for young men and young women to understand that if they put aside even a small amount on a regular basis and that if they -- if they don't touch it, that has the potential for real growth, and that is really what I am focusing on when we look at a personal retirement account.

For my part, a personal savings account, if I had

done that 30 years ago, I would be in fat city right now. But I didn't. You know, again, Eloise, to your comment. You raise your children, you do all the things that you have to do -- somebody said she is already in fat city.

But let me tell you that you had to scramble the last 10 years in your working career to get there. Okay? And it is not easy. It is not something that comes easily. So you don't want to fritter it away. You don't want to fritter away the time.

And so, I am interested in your view on what it is we need to do with young people, particularly before they get to 50, 60 years old, by way of having them understand how important retirement programs are, how important the Social Security program is for survivors, for disability for old age and why there should not be an understanding that if you are low income when you are elderly, it is okay to appreciate what comes to you no matter what it is called. And I am speaking now to the stigma issue of SSI.

MS. ANDERSON: Well, when I was in high school, which was many moons ago, we actually did have it called Home Economics. And in that Home Economics course was a thing called AKnow Your Money,@ and one of the things that they talked about then was how to pay for retirement. Most of us were from blue collar backgrounds.

Many of us came from black families who didn't have

all of the insurance things that white families had. So we didn't have -- many of us didn't have the benefit of being in Social Security because our jobs were not covered by Social Security. I think our view now is very different than my view of growing up in the system.

So there were a lot of occupations in the earlier years that were not covered. Many of those occupations -- black females particularly found themselves and domestics weren't covered.

So when I got to high school, there was a lot of input on savings, and I remember my mother belonging to a group. We didn't come from a very rich family. So this notion that poor people can't save is malarkey. They had what they called a savings club, and I believe this was before mutual funds came out.

They would all get together once a month and they would look at the stock market and figure out what they were going to do, and there were five or 10 of them, like a book club. And then, when my mother came to live with me and she brought her little portfolio, I was like where did that come from?

But one of the things with Social Security, in terms of how it handles the poor, is it pushes out the ability for poor people to save, because it is busy taking their money. So where a poor person could save -- and it

doesn't sounds a lot for those of us -- maybe \$10.00 a month, well, that goes off to the taxpayer now.

So as we talk about taxing more and more and more, we forget that poor people have to pay the taxes as well, even though they don't pay the other taxes. So my belief, in watching poor families over the years, is that the Social Security tax has actually pushed out their ability to save and it pushed out their thinking that they needed to save.

So those two things together to me I think are very important. If I tell you I am going to take care of you, you are going to spend everything you can right now. I mean, let's have the good life, because I don't have any incentive to take care of myself. And government has said I am going to take care o . So, in taking care of you, I don't look at my future; I don't take care of it.

I think we have to, as a country, get out of that notion that we are going to be taken care of from cradle to grave and start putting some of that responsibility back on the individual person. As we do that, I think you will see more and more people step up to this.

You may not remember this, but there was a time when we didn't believe that Americans could take a 20-year mortgage and pay for it. Oh, you have got to pay for your house up front because we didn't trust the American people could do that. Guess what? Most of us do 20 and 30-year

mortgages and we pay for them.

We have to start trusting ourselves; that we are not stupid. We know how to do these things, and just because we are poor, it doesn't mean that we won't save. It doesn't mean that we won't take care of our future, if we have some trust in us. We don't need government to do everything for us.

CHAIRMAN PARSONS: Fidel.

MS. KING: Eloise, thank you very much. You are younger than I am. We only made gathered skirts with zippers in them in Home Economics.

CHAIRMAN PARSONS: At least there were zippers.

(Laughter.)

CHAIRMAN PARSONS: Fidel.

MR. VARGAS: Thank you again for taking the time to be with us today. I think I am the last question. No. There is one minute. Okay. I was going to do a wrap up, but I will let her do that.

What I heard from all of you that you had in common were three things, and I think they are three things that I am focused on as well. One is the issue of equity, in terms of how women are treated in general.

You all mentioned that currently with the system now and any proposed changes in the future. You all talked about the system of a minimum guarantee. For you it is a

little different than for Lisa, but there is a sense that the government, at some point, has a responsibility, whether you call it Social Security or whether you call it something else and you take the other side out of it. I think that is critical.

And finally, although you didn't touch on this, Lisa, but I would say that you wouldn't disagree with it, is the issue of building personal wealth and financial independence, that that is an issue that you are interested in at some level. And you didn't touch on it, but you wouldn't be opposed to that.

So again, I see a commonality; somewhere where we can all agree and that, to me, is a good start.

And now for Lisa, one of the things that you mentioned -- and I want to say something. You are a Democrat. Right? Because I am a Democrat. I just want to make sure that --

MS. MAATZ: OWL is a nonpartisan organization.

MR. VARGAS: Okay. I apologize.

(Laughter.)

MR. VARGAS: My point is that the positions that you are advocating can tend to be associated with people who are more liberal or democrats or what have you, and I consider myself a pretty progressive Democrat.

And you said some things that actually concerned

me. You said we are all in this together. And the issues that you brought up, in terms of how to deal with the shortfalls of the long-term problems, are the kinds of issues that I think FDR back then and even someone like Robert Ball, who I served on the Social Security Commission with in >94 and >96 would argue -- would undermine the support that currently exists for Social Security by going to the point where it goes from being progressive to being absolutely a blind wealth transfer.

You know, general fund revenues, increasing the payroll tax. What is your sense about how the American taxpayer would respond to something like that and how would it pay out?

I am curious because these are some pretty -- and another thing is I want to commend you because you put the specifics into this. Most people haven't taken the time, as far as I have seen, to put these specifics in, and they are fairly progressive I would argue.

But what do you see as the response to this and how practical do you think these solutions are going to be in terms of how they would play out.

MS. MAATZ: Thank you. And I do need to preface, of course, that I am not an economist. I am coming at this, as I said, from kind of the kitchen table economic perspective that my members represent.

All of these -- as I said earlier, you know, there isn't a silver bullet. It is a balancing act, and the problem -- or the issues that we are facing with Social Security are difficult issues.

In terms of how the average taxpayer would react, I don't know. I mean, I am an average taxpayer, and I know, from personal experience that, for instance, the disability benefits are critical.

So, you know, in terms of how the average taxpayer would react I think that most taxpayers don't like to necessarily see tax increases. But at the same time, if they feel like they are getting an appropriate benefit for that money, regardless of what it is, they are more prone to accept it.

The other thing is that there are a lot of taxpayers who don't like certain programs and pay their taxes anyway. There are a lot of folks who don't like certain elements of defense. There are a lot of folks who don't understand how much of their taxes go to the highway trust fund and go to, you know, research on geese in Michigan, for instance, that is important for ecological standpoints.

But I am just saying there are a lot of taxes out there, but not every person, every lay tax person, understands precisely where their money is going. You know, I don't want to get philosophical, but it is a democracy, and

we elect people to make these choices for us and would hope that then, in that situation, they make the best choices.

MR. VARGAS: And I know that you said you are not an economist, but the reason I am bringing that up is it would be interesting for you to get really clear as to the -- just the staggering nature of the increase, in terms of taxes, that it would take to not fix the long-term problem, but just to sure it up, as you are suggesting.

And my sense is it wouldn't be an issue of I don't -- I would rather spend money on education versus spending money on defense. It would be an issue of huge chunks of income being literally appropriated from people's paychecks in order to support a system, and I think what it would do, as I have heard others argue, is absolutely undermine the support that there currently is for Social Security, even with the progressive nature that it has now.

And I think that is something that we are interested in maintaining and strengthening, but when you talk about some of these suggestions, the numbers, when you go through them, are staggering.

MS. MAATZ: I think part of it though too are -- you know, I have seen polls that have been done with younger workers, and young workers inevitably always say that they believe the elderly and other folks, in terms of survivors and disability insurance, should get a fair benefit that will

help keep them out of poverty.

The other thing though that I think we overlook here is that for younger people there is a certain amount of enlightened self-interest, in the sense that if we have a safe and secure Social Security program, that is perhaps then funds that we may not have to draw from our income that we use to help support our parents, that we use to help support someone in our family who has a disability; so that that is that money then that we could perhaps use for our own retirement or perhaps -- you know, at least for our children's education or whatever; so that there is that generational compact I think we need not to get away from.

MR. PENNY: But that needs to run both ways.

MR. VARGAS: And, Lisa, I would be really interested in continuing this conversation with your organization and others like yours that are advocating this, and the reason is it is important to get to the specifics, because once you start getting to the specifics, as opposed to just making the proposals, what you begin to see is the unintended consequences of some of these proposals.

And it doesn't make them wrong. It is just another point of view. And to continue that dialogue I think is going to be important for trying to create a bipartisan approach to really strengthening and solving our problems and dealing with the issues that all of you have mentioned as

they relate to women, as they relate to minorities; as they relate to all low income wage earners.

MS. MAATZ: Right. Thank you very much. I would be happy to have that chat.

CHAIRMAN PARSONS: And now our anchor person. Lee.

MS. ABDNOR: Thank you. And thank you all for coming. All of your testimonies are most interesting, and I think we could keep going all afternoon. I want to make one or two points, and I would like to address my question to Lisa, if I could.

I know that you care deeply about the welfare of women, particularly older women, and I think that there is no difference at all in how we feel about that. I think we all want the same thing. We all want for, among other things, elderly women to live lives that are free of poverty; full lives where their basic needs are being taken care of.

I have a master's in social work, and I have lately been working with elders and have gotten to know some women in -- particularly women in nursing homes and have become friends with them, a few of which are on Medicaid and have nothing else.

And so having been with them and listening to you, I mean, I know we care about the same thing. Maybe we just have a little bit different way of getting to the same end. One thing I would like to reassure you, Lisa, about is we are

not in any way, in any shape or form, wanting to undermine the insurance function of the program.

We are not talking about an either/or. It is not either we want personal accounts or we are going to undermine and with that then that will mean we will undermine the insurance function of the program. I don't think anybody would stand for that. And so, I get to my question of you.

Let's say that -- just assume that we had an absolute guaranteed minimum benefit for everybody. And, in fact, to play with it a little bit, let's assume that we raise that minimum benefit. Let's say that -- because the minimum benefit right now is low. Probably too low.

MS. MAATZ: It is a little bit below poverty actually.

MS. ABDNOR: It is below the poverty line, which, in my mind, is terrible. So let's say we lift that up. So we, thus, bring even more of our elders, most of who, at that point are women, out of poverty, and so we strengthen the insurance function of the program.

My question is that the President is talking about a voluntary program for personal accounts, not a mandatory. So let's say we strengthen the insurance function. Would you then support a voluntary personal retirement account where women would have the choice then to say, yes, I think that is a good idea or, no, I think that is a terrible idea? If it

were voluntary.

MS. MAATZ: I think part of my concern about private accounts, voluntary or otherwise -- and some of the things I have read about voluntary accounts bring to mind some questions about who would take advantage of the voluntary account.

There is a lot of work out there saying that the folks who would be most likely to take advantage of the voluntary account would be the highest wage earners, because those are the folks who are more used to using that kind of account and kind of feel more comfortable with it.

So the reality, if that is indeed the case, would be that we could take that much more money because it is percentage based, the higher wage earners that are taking their money out of the current system to put into a voluntary account and have even more problem with the social insurance aspect of the program that would remain, because the folks who could still be in that program who may opt to stay in it and not do the two percent carve out, or whatever it is, would be contributing less because they tend to be lower wage earners.

So fundamentally, I would have some concerns about the dollars and sense of that kind of a program.

MS. ABDNOR: You are saying that personal accounts then would weaken the social insurance functions essentially?

MS. MAATZ: I think essentially that they could.

M S. ABDNOR: Let's say that it didn't. Let's just say that it didn't, that that was a rock solid guarantee and even stronger than it is today.

MS. MAATZ: And you are saying that for those who stayed in the current system their disability benefits and their benefits would not be cut at all?

MS. ABDNOR: Well, let's say that. Yes. And I am not talking about, Lisa, staying in the system or moving out of the system. Everybody would stay in the system with a guaranteed benefit, and we would strengthen the minimum benefit. So everybody is there.

In addition to that, that people would have the choice to take a portion of their payroll taxes, to invest it and then proportionately reduce -- their decision, their choice. Proportionately reduce that guaranteed benefit. Would you support that if it were voluntary?

MS. MAATZ: If it was absolutely positively not going to effect retirement benefits or survivors or disability benefits, --

MS. ABDNOR: No. No. I am not saying that. I am not saying it wouldn't effect them, because, in fact, what some people are talking about is a personal account where you would then voluntarily proportionately reduce your benefit.

I am saying strengthen the insurance function of

the program, and then, in addition to that, would you agree that a voluntary personal account, a carve out, would be -- you would support something like that?

MS. MAATZ: I don't think at this point I could say I would support that unequivocally. I think that I could be fair. And I especially appreciated the comments of Mr. Vargas; that I would sit down and have a conversation about it.

I think I would like to see the numbers, and I would like to say how it would play out.

Ms. James had an excellent point, that all of this was going to be different depending on the women in question, whether you are a divorced women or you are widowed or you have never been married or if you have children. And so, you know, on behalf of my constituency, I would need to look at a lot of different scenarios. But I would be happy to have the conversation.

MS. ABDNOR: Well, I really appreciate your response to that, your open mindedness about it. I have to tell you that a few years ago there was a press conference in Washington, when I was in Washington working, on this issue.

And at that press conference was a series of women who represented women's groups. Patricia Arlin, with NOW, and Heidi Hartman, who I love, but -- you know, she heads a large coalition that you are part of. I know.

They had this press conference with a panel, and they all talked about how terrible personal accounts were. And I stood up and I said, let me ask you a question. If they were voluntary, if women had the choice, would you support it? And they absolutely said, across the board, no.

And I have to tell you I am glad to hear that you are open minded, because I have to say that I was really, really disappointed in hearing their response, their absolute flat opposition to giving women the choice to decide for themselves.

And what it said to me was that, frankly, these other groups are willing to say that women are smart enough and wise enough to make decisions about their bodies and their babies, but not their bank accounts; that women couldn't decide for themselves. Frankly, I was really disappointed and appalled.

I don't believe that that is representative of many millions of women in this country who would like to have the choice as well on what they do about ownership and their retirement and their future. And I think that they are more than smart enough and wise enough to make the decisions for themselves on what is good for them and what makes good sense and what is not and might take advantage of them.

I think that we need to go beyond that one issue that we have all -- which I support as well.

MS. MAATZ: I will be honest with you. I think that would be a tough sell, but the reality is that I represent --

MS. ABDNOR: Well, evidently it was. They were absolutely against it.

MS. MAATZ: Right. I can't speak to their comments in terms of the appropriateness or not, because I wasn't there. But the reality is that I represent the Older Women's League, and if you can convince older women, you can convince anyone.

CHAIRMAN PARSONS: On that note, which is an eternal truism, you can convince an older woman --

MS. ABDNOR: But don't you --- women who are 40 and above in OWL?

MS. MAATZ: Yes. Absolutely. It is made up of older women, but our members are nothing, if not pragmatic. It is part of the reason why they are so faithful to the Social Security system, because they have seen the benefits of it throughout their lives.

MS. ABDNOR: Good. Right.

MS. MAATZ: But I think that our members -- as I said, if you can convince a member of OWL that this is a good idea, then you will have done something pretty impressive.

CHAIRMAN PARSONS: Unfortunately, ladies and gentlemen, we have overshot the runway here. But this have

been a very stimulating and enlightening panel. Thank you to our panelists. We appreciate it.

And to the members of the public and the press who are here, we are going to take a little lunch break here. But we will be back at 2:00, and we have got three more equally stimulating panels to hear from. We look forward to seeing you at 2:00.

(Whereupon, at 12:51 p.m., a lunch recess was taken.)

A F T E R N O O N S E S S I O N

(2:09 p.m.)

CHAIRMAN PARSONS: While we are rustling up the rest of the commission, I might make a couple of requests. One is that we, earlier on in the morning hearings, had a number of cell phones go off during the course of individual's testimony or response to questions.

And I would ask those of you who have cell phones, if you would put it on vibrate or, you know, sort of silent ring or however it is you can get in touch with whoever is calling you without it having, you know, give us the, you know, the trumpet tympani. That would be much appreciated.

Secondly, just for the benefit of our panelists, who I will introduce to the group in a minute as soon as the other commissioners are here, is we have everyone's written submissions and testimony, and we have got eight members of this panel. So what we would ask is that you try and confine your oral presentation to five or six minutes each, and we will just go right down the line.

And because we have so many folks on this panel, I am going to ask all of the commission to refrain from asking questions unless there is something so urgent that reference to the written materials can't solve the problem.

And even though one of our commissioners must be stuck on the phone, Gerry Parsky, because people have

schedules that they have to speak, we are going to kick off.

Now again, to the members of the public who are visiting, welcome. We appreciate your interest and hope that you will find these hearings as informative as we are finding them. The morning hearings were really both informative and animated, and I expect that this afternoon we will have at least as much of interest going on.

The next panel, which is panel four, really is a panel that I am looking forward to hearing from, because it consists of -- I said this earlier this morning for those of you who weren't here. I hope you don't take offense.

But the man and the woman in the street; the average American. The non-expert, but the person who understands that Social Security affects us all and that it is important to us all and who has a point of view and a perspective that they want to share with the commission. So we really do look forward to hearing from you.

We have got eight participants in this panel. Moving right along, this panelist is, by far, the largest, consisting of eight participants who are just here from the community and who are going to kind of share the perspective from the community and from the middle of America with the commission.

So, we look forward to hearing from you. The first four panelist are Bob Tilaro, Denise Lawson, Chuck Latimer

and James Wittkower, and we will go in that order. Bob, you are first, and I would ask you again just to bear in mind that five or six minute oral presentation time frame that we are trying to hit.

MR. TILARO: Thank you very much.

CHAIRMAN PARSONS: And please speak into the microphone so the young fellow over here can hear you.

PUBLIC PERSPECTIVES

By Bob Tilaro

MR. TILARO: Okay. Thank you. Once again, my name is Bob Tilaro. I started as an employee of the City of San Diego in 1986, and when I was first introduced to the City of San Diego SPSP plan, I was very hesitant and skeptical. As a matter of fact, my first reaction was this is way too good to be true; I must be misunderstanding this program.

And at first I just contributed the mandatory amount until I had an opportunity to check with some friends and some other resources and researched this subject, and then I realized that it wasn't too good to be true; that it, in fact, was true and it was a great opportunity for me.

About five years ago the city diversified our investments and gave us greater opportunity for growth than ever before, and through the city and the administrator of this program we have been given opportunities for education and training. And through this education and training it has

made me feel very comfortable investing in the stock market.

It gives me a feeling that I have control over my money, that I have an opportunity to make the decisions; where it is going to be invested, when it is going to be invested and how it is going to be moved around. And I also determine when I will access the money.

And another unique aspect of this program is the borrowing power that we have against our program. If you borrow a money from a bank or a lending institute, at the end of the term of that loan you have whatever you have purchased back to you, and that lending institute your money and your int.

If you borrow money from your SPSP pension plan, at the end of that term you have the product that you purchased, plus all of the money that you have paid back to yourself, plus interest, and I consider that a tremendous bonus for this program.

Over the past 15 years I have spoke to numerous -- probably hundreds of city employees, and at no time have I heard a negative comment about this. As a matter of fact, I have had the opportunity to speak with several of my personal friends that work outside of this city and have different plans, and every one of them is envious our program.

I also have a friend that owns a pension company. He writes pension plans for people all across the country,

and I have had him review our pension plan. And it is his opinion that this is the greatest plan he has ever seen, and that is coming from an expert; an individual that makes a living doing this.

And at the end of my career, at 55 years old, not only am I going to have my retirement based on my years of service, but a substantial amount of money that had been set aside for me in this plan. And to add to that, Social Security is available to me at -- I believe it is the age of 62. This plan is available to me at the age of 55.

That is going to allow me seven years of retirement and financial comfort that I would not have with the Social Security program. That is seven years that my wife and I and kids and grandkids can spend having fun, and that is why I think this plan is just -- these are just a few of the aspects of this wonderful plan.

CHAIRMAN PARSONS: Denise. Thank you, Bob. I take it you like the plan.

MR. TILARO: Yes, sir.

PUBLIC PERSPECTIVES

By Denise Lawson

MS. LAWSON: My name is Denise Lawson. I was here earlier when the meeting opened up, and Mr. Parsons gave an overview of what the agenda would be for today. And when he got this portion, he said we would hear from the common

people, and he hoped that we wouldn't get offended when he said that.

And I just want to say to you, Mr. Parsons, I am not at all offended because you are talking about the great people that have made this nation great. You're talking about the everyday working people. That is who I represent, and I consider it an honor to be able to give my perspective as a common person.

I am going to read my statement or portions of it because -- for time constraints, because it is such an emotional issue for me and it is such a critical issue for me that I don't want to leave out the important things that I wrote.

I entered the work force when I was 16 years of age. So already I have been working 31 years, and I have another 18 to 20 years to go. So when I hear politicians talking about raising the retirement age, I just want to let you know I am not for it, because already I'm tired.

I've made mandatory contributions into a system that I don't own. I can't transfer it, and if I live long enough to collect it, they're telling me I'm going to get 88 cents on the dollar. I want to go on record as saying I'd rather put my money in a mattress because then at least I can get out of it what I put into it.

To me the current system is an enormous risk

because, as all of you know, when we started this thing out we had 44 workers contributing for every one person retiring and receiving benefits. Now we are down to four, and by the time I retire, I can expect we will be running a deficit. And I have a problem with that.

When I hear the word risk, I don't think of stocks or bonds or mutual funds. No. That is not what I think of.

When I hear the word risk, I think of the Supreme Court ruling in 1960, Fleming vs. Nestor, that upheld a 1937 decision that says my benefits can be cut or eliminated at any time. There is no guarantee for me. That is a risk.

And a thought comes to my mind. I have a loving husband who takes care of me. He provides for my family. He is a good man. But should he decide, in some mid life crisis, to take a hike, I will be left to join the 29 percent of elderly black women that retire in poverty in this nation. I've got a problem with that.

The current system is an even greater risk for African American males. This is what they are telling me. They're saying that our men die, typically die, at 64.8 years of age. Yet, like me, they have entered into the work system at a very young age. I have four adult children who have entered, must like me, into the work force in their teens.

They will work 40 or 50 years and typically they will die before they can collect one dime. They won't

collect anything, and it is not transferable to their children. It is not transferable to their wives. That is a disgrace. I have a problem with that.

Now I haven't researched Social Security in an extensive way. I just talked to the common people, and the common people are telling me, the common women of these men who have died are telling me that they can receive the difference between his benefit and hers if his is greater.

But, in essence, she is forfeiting all that she has contributed into the work system all of her working years. I have got a problem with that.

And the children. Let's talk about the children. What will they receive? Nothing. This man has put thousands of dollars into a system and his children won't receive anything, unless, of course, he has minor children. How many 64-year-old men do you know that still have minor children?

It is a rip off, and they don't even know they're being ripped off. They're working so hard. They're living from paycheck to paycheck. I have a problem with that.

So, in my humble opinion, I think personal retirement accounts are the best way to go, because it brings dignity to hard working people who have made this nation great. And they are so great a people and they deserve to have ownership in the American dream that they have created for all of you and be able to transfer some of that ownership

to their children and retire in dignity and each generation not having to start over again in poverty.

We are the greatest nation in the world, and the poor people have worked hard, and I think they deserve to have some ownership in the wealth that they have created.

(Applause.)

CHAIRMAN PARSONS: Thank you, Ms. Lawson. I gather the audience did not have a problem with your statement.

Mr. Latimer.

PUBLIC PERSPECTIVES

By Chuck Latimer

MR. LATIMER: That's a hard act to follow. My name is Chuck Latimer, and I retired from --- for more than 37 years and served -- and on behalf of other retirees in San Diego County, I'd like to thank you for the opportunity to express our views on Social Security reform.

Now, I will read. Nearly 385 residents in San Diego count on Social Security benefits each month. While most of them are retired workers, a great many get benefits for other reasons. Roughly, 27,000 of them are children. Another 74,000 are spouses of workers who have retired, who have become either disabled or died. Another 34,000 are severely disabled workers.

We know the risk that families face, and nearly three in 10 workers will need Social Security disability

insurance protection at some point before retirement, because they will become severely disabled. Nearly one in five workers will die before reaching retirement. We see this on the jobs in our families and our communities.

Members of the commission may see this in government statistics, showing that almost two out of three older Americans count on Social Security for half or more of their income and nearly one in five families of disabled workers get almost all of their income from disability benefits.

We see every day how much Social Security means to our members; our families, our neighbors and their ability to put food on the table and live independently.

While he created this commission, President Bush ordered it to come up with a plan to treat individual investment accounts within Social Security. We strongly oppose these proposals that replaces any part of Social Security benefits and family protection with individual retirement accounts.

We read and hear about the promise of more benefits, but this does not add up. The government already predicts that Social Security will have not enough money to pay full benefits beyond 2038. But taking money away from Social Security to fund individual accounts only makes the problem worse.

And the President has said he will not support next taxes to pay for these accounts, and his tax cuts and budget plan mean that there's no room left in the budget to fund them. Under the conditions laid out by the President, individual accounts will lead to big cuts and benefits, even after income from those accounts are added in in Washington and working families cannot afford to cut their benefits.

Claims about individual accounts never really mention what we give up when we replace Social Security with individual investment accounts. But the prospect is real and will be paid by working families.

Individual accounts will not provide more for the families. They pay only what is in the account. There is no supplemental benefit that take into account a spouse who spent all or part of her working years raising a family instead of at a job in the paid work force with the needs of children or grandchildren still being raised by the worker.

Individual accounts do not insure that workers who become disabled have a secure foundation in retirement income, in addition to disability benefits during their working years. Individual accounts do not provide lifetime benefits that do not run out, and they do not provide secure benefits for a base of income for Americans who have a lifetime in low paying jobs.

Families in our communities cannot afford cuts in

Social Security because far too few have the opportunity to participate in pension plans or to accumulate savings, and many of these same workers face soaring medical costs and growing numbers have no coverage beyond Medicare, which does not cover the fastest growing part of their health care bill, prescription drugs.

Instead of creating individual accounts that cut benefits and weaken family protection, we should take action now to secure Social Security for the future. We can do that first by using some of the future budget surpluses that the President and Congress have earmarked for tax cuts.

According to the Nonpartisan Center of Budget and Policy Priorities, the cost of recent enacted tax cuts over the long haul is over two times as large as the deficit predicted for Social Security. The responsible thing to do is to cancel some of those future cuts and dedicate the money to strengthening Social Security.

Second, on the wages that are subject to payroll taxes should be increased; increase in the Social Security cap so that includes 90 percent of all earnings and work covered by Social Security, in combination with the budget surplus. It would solve almost all of the deficit project. And thank you for letting me talk with you gentlemen and ladies.

(Applause.)

CHAIRMAN PARSONS: Thank you, Mr. Latimer. We appreciate your comments.

Mr. Wittkower.

PUBLIC PERSPECTIVES

By Mr. Wittkower

MR. WITTKOWER: Thank you. My name is James Wittkower, and I retired from E Systems in 1987 after 39 years as vice president of employee relations for the Florida operations. A number of my years were in employee benefits.

I appreciate the opportunity to present my views on allowing workers to invest a percentage of the 12.4 percent of income workers and employers currently pay into Social Security.

During my career I served on E Systems' task forces to develop, analyze and implement a flexible benefit plan when they became permissible, a 401K plan when they became permissible, and prior to that, to reward and motivate our employees, we had established an employee stock ownership plan. I look at these as building blocks for retirement.

For many years, including the mid 1950s, nationally a number of employees were without retirement benefits of any type and relied solely on Social Security. Other did have retirement plans, which would be a building block on top of their Social Security and whatever, of course, they were able to save from their salaries or wages.

Legislation authorizing flexible benefit plans, also known as cafeteria plans, was a new building block for employees. In our plan it enabled them to invest in a savings plan, to select from different levels of hospital, medical and surgical plans, to put money away for medical deductibles or co-payments, and also, to select from different levels of life insurance plans.

The next building block for workers was when the IRAs, the individual retirement accounts, were established in 1983. I only wish that I had had that opportunity at the beginning of my career, rather than in the twilight years.

I feel strongly that we need to allow workers to invest a portion of their and their employer's Social Security taxes as an additional building block for retirement income. This action will lesson baby boomer's reliance on Social Security, and over 20 to 30 years, it should provide a higher rate of return, despite the ups and downs of the stock market. And, of course, we have seen the downs more recently.

Employees who have a 401K plan and/or retirement plan throughout their career and hopefully the possibility of investing part of their Social Security taxes should be well prepared for retirement and substantially rely less on Social Security benefits.

I have read articles by groups who oppose this

approach, and that is what makes America great. We have different opinions. But I think that the intelligence of the American people has been underestimated. I think that most Americans have the capability of making decisions or seeking competent advice on financial investment.

Employees, I think, should have the option of participating in investing their own -- a portion of their Social Security or opting not to.

In closing, please keep in mind that the individual investment of Social Security taxes can add a building block to the foundation for retirement savings, and I sincerely hope that my daughters and my grandchildren have this opportunity in future years that I did not have. Thank you.

CHAIRMAN PARSONS: Thank you, Mr. Wittkower.

(Applause.)

CHAIRMAN PARSONS: That is a more responsive audience than we had this morning. That is very good.

We appreciate the first four panelists, hearing from you, obviously, a diversity of views. But that is what we are after, to get a full range of a kind of expression out there.

Thank you very much. I hope you will stick around and support the next group of panelists who are going to come and give us their view. They are Sally Acosta, Sally Chapin, Robert Prath and Michael Bateman.

(Pause.)

CHAIRMAN PARSONS: I will again remind those in the audience listening and the press that the commission is refraining from questioning these witnesses since we had so many on this panel, and we are more interested in what they have to say than what our comments might be.

So, why don't we start with Sally Acosta.

PUBLIC PERSPECTIVES

By Sally Acosta

MS. ACOSTA: Good afternoon to everybody. My name is Sally Acosta. I'm a member of the California Commission on Aging, a member of the California Senior Legislature, it is my sixth term now, I'm the vice president south of the Congress of California Seniors, I'm a retired social worker and public health --- of Los Angeles County, and I am a member of the National Committee to Preserve Social Security and Medicare.

Social Security was never intended to be a person's sole source of retirement income. Instead, it is a guaranteed base which should be supplemented by private pensions and personal savings. Also, many people invest the bulk of their personal savings in private markets.

In light of this, Social Security does not need another component of risk to Social Security benefits by tying them to stock market performance. Can you imagine a

young worker of say 18 -- from 18 to 21 years old probably starting with McDonald's earning the minimum wage to be able to determine which of the stocks and bonds he will buy and at least project to himself how much he will earn between now and 10 years from now. It is just like asking for the weather forecast 10 years from today.

Several decades into the 21st century the Social Security trust fund is projected to experience funding shortfalls due to changing demographics. The senior citizens now are living up to 95. Bob Hope is now 98. He is still alive. I do not think this is a crisis.

There is ample time to make more changes in revenues and benefits to insure that Social Security will be financially sound for future generations, and some of these are, one, bringing on newly hired state and local government employees under the Social Security system. About 3.7 million are not in the system.

Raising the retirement age. You may not agree with this, but we are living longer, as I just said. Raising the retirement age higher than is stated under current law as more Americans enjoy longer and healthier lives.

Three, carefully investing a portion of the trust fund surplus in the private markets to increase the rate of interest paid on the funds instead of resorting to individual accounts which puts retirees at risk.

In Los Angeles County our retirement funds are invested very well. That is why we retirees can enjoy our retirement from there even if we -- for the rest of our lives while we are receiving our pensions. Our Social Security retirement is not as much as what we get from our pensions, because they have -- that is just the way it is.

If you work, you can get something. If you don't, you don't get anything.

In the year 2038, if necessary, slightly increasing the Social Security payroll tax by .08 percent each between employers and employees, from the 2001 report of the Social Security Board of Trustees it projected, one, to have ample assets to pay 100 percent of all benefit obligations.

Two, incoming revenue will be sufficient to pay about 70 percent of benefit obligations throughout the 75 year forecasting period. See? The projected date of insolvency has been moved from 2029 to 2038.

Next, the Social Security currently is running at annual surpluses. In calendar year 2000 Social Security trust funds grew by \$153 billion. In December 2000 the Social Security trust funds balance totaled an estimated \$1049 trillion and these reserves are expected to grow to \$6.5 trillion by 2024.

In calendar year 2000 Social Security trust funds earned \$64.5 billion in interest. Administrative costs for

Social Security were about 0.9 percent of total expenditures in the year 2000.

From the Social Security Administration, this is what they claim: Social Security surplus funds are invested by law in the U.S. Government Treasury Bonds, which are backed by the full faith and credit of the U.S. Government and are as strong as corporate bonds.

And the last is Social Security is self-financed. Benefit obligations are paid entirely from payroll tax contributions, interest earning and taxation of benefits.

Thank you very much for giving me this opportunity.

CHAIRMAN PARSONS: Thank you, Ms. Acosta.

Lori Chapin.

PUBLIC PERSPECTIVES

By Lori Chapin

MS. CHAPIN: Thank you. My name is Lori Chapin, and I have been a city employee for 16 years. The City of San Diego does not participate in Social Security. We opted out in 1982 under the then voluntary withdraw program, and as a result the city had to offer other retirement benefits that were at least equal to or greater than that offered by Social Security. And they did big time.

You have already heard from one of the speakers about one of our programs, our supplemental savings and pension program, and I am going to mention that because it is

important.

But really, the city's plan is based on two different approaches, and so I am here today because one issue that troubles me as a City of San Diego employee is an issue raised by Ms. Acosta, and that is mandating coverage in Social Security of all state and local government employees.

And that is concern to me in light of the wonderful retirement I look forward to, and I really don't want to see it jeopardized.

But at the same time, I don't want to come up and just whine and say please don't bring us on. I would like to share with you some of the things the City of San Diego has done with its retirement package, because I think there are futures that are in the plan that I enjoy as a city employee that would be wonderful and that could be used in Social Security to strengthen Social Security.

The plan that is probably most like Social Security is our defined benefit plan. It's called the San Diego City Employees Retirement System. This is a plan that you work and that at a certain age -- and in my case, because I'm a general member, meaning I'm not a police officer, firefighter or a lifeguard, at age 62, if I have worked for the City for 10 years and I have contributed and my employer contributes as well, then I would be guaranteed a benefit based on my hire year salary, times the years I have worked, times the

retirement factor, which at this point is two and a quarter percent a year. That's very nice.

I also have the option of retiring earlier than age 62. I can leave at age 55 with 20 years of service, that same retirement factor and again with my salary, which is a very attractive benefit.

One of the things that I like about that is that the San Diego City Employees Retirement System, the money that I put in there and the money that my employers puts in, it goes into a trust fund. A true trust fund.

It is managed by a board of trustees that consists of employee representatives, City of San Diego management representatives, a retiree representative, and then we have taxpayers that serve on our board as well. They're 13. And they invest our money.

They're professionals. They know what they are doing. They diversify all of the money. Some of the money is in equity, private and international. Some of it is in bonds and real estate. But when something is going up in the market and something is going down, hopefully the fund is maintaining and that benefit is guaranteed to me.

And that is probably what is more important about that plan, is that it is guaranteed. I can sit here today and I can plan my retirement in the future knowing how much money I can look forward to having, because what I put in is

going to come back to me.

It's actually better than that, truth be known, because what I put in -- let's say all the contributions that I put in and all of the contributions that the city puts in, I live to be a Bob Hope. I'm going to live longer than Bob Hope. I'm going to live to 100, 110.

Well, those contributions are long since going to be used up, but my monthly allowance is going to continue to be paid to me. And in addition, I have the option of leaving a benefit of 50 percent to my surviving spouse, should I predecease him, or to my children.

This is a wonderful plan and it provides wonderful security, but that is not all. The City of San Diego also offers a supplemental pension savings plan. This is the plan that your first speaker, I just met him today, another fellow employee, Mr. Tilaro, spoke about.

Now, this is not a defined benefit plan. This is a defined contribution plan, which is a plan where, again, I put in money and the employer puts in money, and as Bob mentioned to you, there is a mandatory contribution. I have to put in three percent. Actually, I came a little earlier. I put in four and a half. No.

I put in three percent, but the City allows me the opportunity to put in another four and a half percent. Well, when I first started I thought, well, why do I want to put

any extra money into a plan? I don't think that's such a good idea.

And then I went home and I spoke to my husband, and he goes, are you kidding? Have you thought about that? The City is going to match, dollar for dollar, your mandatory and your voluntary contribution. I think you should rethink that. So I went, oh, three, four ... 15 percent of my income. That is a good deal. That is going into this account.

And this was the retirement plan that was established when we opted out of Social Security. So with that plan we moved along. It has been wonderful. But then the City being, I feel, the generous employer that it has been to me, gave us investment choices.

They said, we're not going to administer this plan anymore. We are going to have a third party administer, and we're going to have participant directed accounts, which is very scary. But, you know, it's taken root. It's not something that I think all city employees really enjoy because they have the advantage of having the opportunity of both retirement vehicles.

The City of San Diego is not limited to one. We've got both. We've got the opportunity to invest in the stock market, and there are those of us, like me, who choose not to use that opportunity.

I'll confess to you. It's so scary to me that I want the professionals to manage my money. So I leave my money in one account that is available to me that has the low risk, and I'm really trying to broaden my horizons and perhaps I will soon. But I'm not there yet. But through the educational opportunities I hope to get there.

In conclusion, I really wanted to just suggest that that's really the difference between Social Security and what we have in the city right now, and that is the whole idea to guaranteed benefits. I know what I am going to receive at retirement, and that's very important to me.

And the other issue is that it is, interest eh City of San Diego, a true trust fund. That's what we have, and I know that that money situation going to be there and it's free from political interference, and that is very important to me.

So I would urge you, as you look forward to hear more speakers and hear all kinds of suggestions, because I'm sure you're going to hear a gazillion, that when it comes to the issue of mandatory coverage for state and local governments, please don't break something that's not broken.

We're doing really well, and we're not a burden on the taxpayers and we really feel that what we've done could be a guiding light to Social Security and perhaps some of the features that the City of San Diego and other states who

don't participate in Social Security could be used. Many of these features could be used to strengthen Social Security.

So again, I thank you for the opportunity of providing comment today.

CHAIRMAN PARSONS: Thank you, Lori.

(Applause.)

CHAIRMAN PARSONS: Bob.

PUBLIC PERSPECTIVES

By Mr. Prath

MR. PRATH: Good afternoon. My name is Bob Prath, and I appreciate the opportunity to testify before this distinguished commission this morning. My comments mostly pertain to your early report and quite conveniently segue to previous comments.

I commend you for pointing out that contrary to long held public positions, government offices and courts are headed towards the opinion that Social Security has questionable legal authority to pay obligations from this government held trust fund.

The legal status of the trust fund itself is not a make or break issue in terms of promised Social Security. Even national priority prevails over the printing of Social Security checks. But should the trust fund turn out to be a rotten trick we placed on ourselves, then loss to public trust and confidence will stifle change in any direction.

I recommend that we seek resolution to the questions you raised and that aside from modernization solutions, you recommend that the Attorney General elevates cases to the courts to help us define where we stand and guide a path for us to investigate --- privatizing, if you must, Social Security funds and obligations.

We need to clear the question and otherwise make it --- discuss a trust fund that has no bearing on the solution and observe politics that also be reduced. We could put trust funds in lock boxes --- boxes. The President's key principle, that the entire Social Security surplus must be dedicated to Social Security, makes no sense if it turns out the surplus is now and always will be equal to zero.

I'm kind of proud that my excess of payroll taxes were keeping payments on national debt in America and building a secure future for some baby boomers. I'm disappointed to hear, from respective sources, that it won't be the case and the sooner I know the finality of this, the better.

I also have concern with public focus on a stake building --- to some degree. We discussed the disability and the poverty issues of Social Security, and I remember why this government program is judged on a competitive rate of return while most others are judged by social benefits.

I have about 27 years invested in a program that

there is no monetary issue involved, and I think this is a bad precedent. We are --- as citizens to contribute to this country's welfare, giving --- in some cases, and --- rate of return in the family financial legacy for that.

While I reportedly get a lousy monetary rate of return, I support joining other Americans, and I have, to promote the general welfare through programs like Social Security, but I don't understand how private accounts belonging solely to me --- integrated into a government program, and I am suspicious.

The American trust fund issue teaches us that what starts out as with honest intent --- completely to different interpretations in another. Why would I want to be party to a Aprivate investment account@ that is regulated by a growing government pile of regulations, and I have already heard some started here -- worked out between investment lobbyist and politicians when the government had no stake in my individual outcome?

The --- investment issues that starts out as voluntary becomes mandatory when the government eventually used accounts to manipulate my personal investment --- Federal Reserve determines --- national savings rate, and the report actually touches on that crucial issue as part of this program.

I am far more comfortable with the competitive

contracts awarded with large firms that collectively invest excess payroll taxes, and these have been addressed. This would meet the President's principles since Social Security participants could voluntarily elect to participate and direct government purchases of securities is avoided.

Benefits could be based on how much was paid and how well one chose among major funds. The government's huge pension systems are already --- in this manner, and the system seems to avoid conflicts of interest. I heard something about a Microsoft letter, and I appreciate that. But we have to trust our politicians to deal with things like that right now, and that is a problem. We just have to have trust in it.

Risks and assets are shifted out over the government reach, but the government can be a friend in the process because they indeed would still have an indirect but vital stake in how well the collective outcome was.

Finally, this report repeatedly appoints the fundamental cause of Social Security risks and --- demographics, and I know this is outside of the box. But it is an all hands problem requiring an all hands solution.

Labor should be challenged to find ways to increase able bodied older workers to continue workers, and the Treasury should recommend sensible integration policy that address our needs. Just south of here we have a country with

an enormous unemployed youth population.

We can find and improve ways to integrate them into America, as well as --- as it is starting to do now.

As to the future I have great hope. Once there was a promise --- within Social Security. The rest is up to our national priority. I don't envy your sessions, and I believe --- a lot of head shaking. But I believe what you are doing here is important to gaining a national consensus that we need to work on this problem. Thank you.

CHAIRMAN PARSONS: Thank you, sir.

(Applause.)

PUBLIC PERSPECTIVES

By Michael Bateman

MR. BATEMAN: Good afternoon. It's an honor to be here. My name is Michael Bateman, and I'm a 34-year-old entertainment industry professional. The cyclical nature of employment in the movie business often allows me to have another profession in the summer months as an ocean lifeguard, and that's how I'm current employed.

Now, before I dive into what I think is a raw deal, pardon me, my generation is getting with regard to Social Security, let me first say how grateful I am to be an American and to live in this day and age.

I am currently reading *The Greatest Generation*, by Tom Brokaw, and as I turn each page, I'm reminded of the

selfless sacrifices previous generations have made to make this country great and how good I have it. This great nation has a proud tradition of each generation building for future generations, dating back to the founding fathers of our country.

The Social Security system was born of this endowment mentality. The family, as your commission's interim report makes clear, seems to have lost its way. It seems it has become a system where a generation will pay more and get less.

As with my peers, this deeply troubles me, because this means for decades I will knowingly contribute to a system that is taking advantage of me. And if that doesn't undermine young people's faith in government, I don't know what does. Beyond this there is a larger point that I encourage you to be more aggressive in pointing out to my generation.

A poor rate of return means that people my age will not be able to retire with dignity, and creating a system that enables low wage workers of my generation and that those that follow to retire with dignity should be the goal of your reform.

We should learn a lesson from today's seniors, the majority of whom rely on Social Security for a majority of their income. A generation that is over-reliant on Social

Security is a generation that is, by and large, just scraping by. Narrowly escaping poverty is not dignity.

This commission's goal should be to provide all workers with at least two streams of income at all age, not just one. The goal of the 20th century was to lift seniors out of poverty. Our society was remarkably successful in meeting this objective.

The goal for the 21st century should be to provide dignity in retirement. As long as you and the administration act as passionate advocates for dignity in old age, no one can question your motives. Specifically, I support the idea of individually controlled voluntary personal accounts for younger taxpayers such as myself.

Having read your report and having followed this issue closely for the past 10 years, there is no way to make a valid promise to my generation without short changing today's retirees and without overtaxing the children of my generation. And if you fail to make this promise, you will lose the confidence of my generation. And worse, we will be robbed of our ability to make this promise to the next generation and continue our nation's great tradition of building for the future.

For me, dignity in retirement will be having the honor of knowing that the children of my generation will have it better than I did. And let me end with a plea to my

peers.

Americans in their teens, 20s and 30s and perhaps also the Stanford delegation behind me must become engaged in this debate, no matter how far off the problem seems. Right here congress members, write to your senators, write to this commission and above all vote, for if we do not seize this moment now, our leaders will be free to balance this burden on our backs and on the backs of our children, and we will have no one to blame but ourselves. Thank you.

(Applause.)

CHAIRMAN PARSONS: Thank you, Mr. Bateman. And thank all of the panelists for your very thoughtful remarks.

I think this worked as well as I hoped it would, which was hearing from folks who aren't experts, but who clearly understand that the system affects us all.

That is the fourth panel. Our fifth panel, which is entitled, AOther Experiences at Home and Abroad,@ is going to -- we are going to go back to the pattern we had. We only have three panelists here, which I will introduce in a minute, and we will hear a little bit -- first we are going to hear some more about the San Diego system that was referenced by several of the panelists on panel four. Just understanding how that system works and what lessons we might take from it.

And then we will hear about a system in Dallas,

Texas and then some systems -- how other countries -- we have heard reference to that earlier today. We will have one of our panelists who is an expert on that and will give us a sense of how other countries are dealing with this problem, because we are not alone.

So, if I could call to the witness table now Valerie Vandeweghe, who is a benefits administrator for the City of San Diego; Judge Holbrooke, from Galveston, Texas and Anita Schwarz, from the World Bank, we can kick it off.

Welcome to all of you. Thank you for your willingness to be a part of these proceedings and the time you put into preparing. Why don't we start with you, Valerie.

OTHER EXPERIENCES: AT HOME AND ABROAD

By Valerie Vandeweghe

MS. VANDEWEGHE: Okay. Thank you very much. My name is Valerie Vandeweghe. I'm the benefits manager for the City of San Diego. This afternoon you heard from two of our city employees about the SPSP plan, and this afternoon my goal is to give you a little bit of history and overview about the plan.

In 1981 the City of San Diego took advantage of opting out of Social Security for its employees. In its place the City established the Supplemental Pension Savings Plan, more commonly referred to as SPSP. This is a mandatory

defined contribution plan for all city employees, or I should say the majority of city employees.

At the time that we opted out police officers and firefighters were not covered by Social Security, and therefore, we did not need to replace a plan for them.

Employees are required to contribute a mandatory three percent of compensation on a biweekly basis. They then have an available contribution that they can contribute, from 3.05 percent to 4.5 percent, depending upon when they were hired. The city matches each dollar, and it goes into a separate account for the city employee.

At the time that SPSP was created all of the investments were invested by our city treasurer's office in very safe general accounts, generally government securities.

Five years ago the City of San Diego decided to, and it was endorsed by the city employees because they do have to vote about the changes in our plan, to move to a third party administrator and allow what is called self-directed investment options.

This gives control to the city employees to invest not only their contributions but also the city's match. Under our plan, after five years of employment, the employee is vested or owns the city's match as well.

When we invested or initially went with our third party administrator, the city employees were given five

investment options, one of which was very similar to the way that the City treasurer invested the monies. This is called the managed income fund. There were four other investment options that they had available to them that were varying mutual funds that ranked in different risk levels.

The reason that this was done is because the city did recognize that this investment thing was new to city employees and that they might be hesitant, even somewhat skeptical, they may not know about investments and would be very uncomfortable with going into the investment market.

Over the past five years the investment options are now up to 14. The investment options are selected by a trustee panel of five that oversees the investment options with the assistance of an investment consultant.

How are we doing? The city employees, in the past five years, have invested 50 percent of the SPSP assets into various mutual funds. Fifty percent of the monies are still sitting in the managed income fund.

Over the past five years the return on the safest investment option, the managed income fund, has earned 6.33 percent. The other investment options are ranging anywhere from 4.75 percent, because of the down market, up to as high as 16 percent.

We also offer what we call lifestyle funds for those employees who are not comfortable with investment

options, don't want to take the time to understand investments or to track their investments. These lifestyle funds invest or diversify the money for the employee, depending upon the time frame that they have.

If you have a young city employee that has 30 years to work, they can tend to be more aggressive even with the down cycles. Overall, we believe that the city employees are very happy with our program. They are very happy with having the investment options, because -- even one of them being the safest investment option. But they have control, and when they retire, the money is theirs. Thank you.

CHAIRMAN PARSONS: Thank you. Next.

Mr. Holbrooke.

OTHER EXPERIENCES: AT HOME AND ABROAD

By Judge Holbrooke

JUDGE HOLBROOKE: Yes. Thank you very much, ladies and gentlemen. My name is Ray Holbrooke. I'm from Sante Fe Texas; a retired county judge in Galveston County after 28 years of service, a Social Security recipient and a graduate of Texas A&M University.

I'm honored to have this opportunity to testify before this commission to strengthen Social Security. I'm here in my own capacity and also as a grassroots leader for the United Seniors Association, a national association with 550,000 citizen members dedicated to uniting the generations

and expanding retirement and investment freedom, health freedom and economic and tax freedom.

Over the past 10 years the United Seniors Association has vigorously warned citizens and politicians alike that the Social Security trust fund was at risk due to both demographic and political pressures and needed to be protected and strengthened immediately.

Today the United Seniors Association is an active member of the Alliance for Worker Retirement Safety, the national alliance dedicated to expanding wealth to all Americans, with special concerns for minorities, women and those at lower income levels who suffer most under the present system.

As a retired county judge I know how important the personal testimony of an eye witness can be, and I'm not a theorist. I'm an eye witness and a practitioner. I know personal retirement accounts can work because I have one. I know a commission like you can design a better deal because I was part of one.

I know it's possible to build public support for bull reform, because I did it at a political level. I know it's possible to change the heart of a skeptic because I was one.

Twenty-one years ago three Texas counties, initiated by Galveston County, and then including Brazoria

and Matagora County, just southeast of Houston, Texas, plus two cities developed an alternative to Social Security, retirement, disability and survivorship programs. That was at a time when local government could still opt out of Social Security. Of course, that is not the case now. That was changed in 1983.

So despite initial fear and anxiety, the details were exactingly explained and very stringently debated in public. We had probably 50 meetings with employee groups around the county and then we had an election, because we were fearful of the political consequences. But the election carried by a three to one margin, and the results since that time have been extraordinary.

Our plan provides better retirement, survivorship and disability benefits than Social Security. Our plan provides a better rate of return, between seven and eight percent, compared to less than two percent under the current Social Security system. And our plan is a banking model.

This was also for political purposes. We use no stock market investments, only commercial banking products, annuities and bonds that provide guaranteed fixed interest rates and no risk. We would have been far better off over the past 20 years to have been in the stock market, but I doubt very much it would have carried in the employee election if we had put it on that basis.

Most importantly though, minorities, women and lower income workers in the county and those who may die prior to reaching retirement age have clear economic advantages compared to Social Security. We have done very, very well without taking any risks.

Over the course of 20 years we have averaged between seven and eight percent per year on our personal retirement accounts. That is at least three or four times better than workers who would have received had we stayed in Social Security, and all our money is safe and secure and there is no politician spending that money in Galveston County.

Our disability insurance pays 60 percent of a worker's salary, up to \$5,000 a month, and our life insurance program, which replaced the survivorship part of Social Security, pays three times a worker's annual salary, at least \$50,000, and up to \$150,000, depending on salary. These are significantly better than Social Security.

Financially, workers have the peace of mind that their money is truly safe, that we are getting guaranteed fixed interest rates and they can take it to the bank, rather than have to live with the great anxiety that certain stocks and market sectors would go up and down perhaps like a roller coaster.

Politically, that made our reforms much easier to

sell to the curious and skeptical work force in Galveston County, and these successes matter to real people. One county commissioner associate of mine died in his early 40s. His widow was quite young. About 40.

From Social Security she received a lump sum of \$255.00. That's not per month or per year. That's just one figure of \$255.00. From our alternate plan she received a lump sum survivorship benefit of \$150,000, and she's entitled to a reserve account of \$125,000, which she can leave to draw interest, if she chooses to, or she can take it out any time.

From our plan she has received more than a quarter of a million dollars or one thousand times what she received from Social Security. That is why though I respect very much the new deal.

And I ran as a Democrat in eight elections in Texas. I think the President and this commission ought to look seriously and carefully at our approach because it is truly a better deal for workers and their families.

Finally, let me emphasize that our workers have true financial security for themselves and their families. This is wealth building personal accounts that are their own property and the opportunity to escape from poverty, especially for women and minorities, and this is not a theory.

We have a real model, an American model, a Texas

model that has worked for 20 years, and we believe that the President and the Congress could readily adapt it to national usage. So I urge you to come down to Galveston and see our plan.

Now, don't come in the summer time. It's too hot. It's not like San Diego. But we'd be glad to have you down there and we'd be glad to answer your questions and calm your fears.

It's my fondest hope that we have created a model for the rest of this country that all of us can benefit from, and I'm especially concerned, just like many of you, about my children and my nine grandchildren.

Thank you very much for an opportunity to testify before this commission.

CHAIRMAN PARSONS: Thank you.

(Applause.)

CHAIRMAN PARSONS: Anita Schwarz.

OTHER EXPERIENCES: AT HOME AND ABROAD

By Anita Schwarz

MS. SCHWARZ: Good afternoon. It's a pleasure to be here. I've been asked to speak about the international experience with private retirement accounts. I was asked to speak only about five minutes, and it's hard to synthesize all the global experience into five minutes, so I am going to concentrate on four main points.

The first is where they have been implemented and why, the second is how they have been implemented, the third is how the system is functioning, and finally, the fourth is a little bit about the popularity of these accounts when people have been given the choice of joining the system or not.

In terms of where they have been implemented, there is a map up in the first graphic that shows that private retirement accounts are increasingly a part of world social security. There are currently 10 Latin American countries that have adopted them, seven high income OECD countries, such as Sweden and Switzerland and Australia, five former socialist countries and Hong Kong, which doesn't really show up on the map.

Why have countries adopted these? The next graphic. What we see, and I think you have heard this many times this morning, is that the world is aging. The purple bottom portion shows you the number of people that are potentially of working age, and the third turquoise portion shows you the people that are of retirement age.

And what you can kind of see from the graphic is that in the year 2000, which is the left hand portion, there are three workers per retiree, and by the year 2040 there is going to be less than two workers per retiree. Setting aside reserves is one way to deal with the aging issues; however,

this moves us to the third graphic.

The experience with public management of pension fund reserves is abysmal. The rates of return received by publicly managed pension funds have tended to be way below the rates received by privately managed pension funds in the same country, and what you can see -- you probably can't see it well. But all the countries that are -- have bars to the left of the axis are countries where the publicly managed pension fund reserves have earned lower rates of returns than bank deposits would earn in those same countries.

So the -- because the experience, the international experience of public fund management has been so bad, many countries have turned to private fund management. How have these been implemented?

In many countries they have actually -- private retirement accounts have been used to replace all of Social Security. This is true in Mexico. This is true in Chile. In other countries they have been added on to existing Social Security systems. Australia is an example; Switzerland, the Netherlands, Sweden.

In other countries part of the existing contribution has now been used to fund private retirement accounts. Examples of these are Argentina, Poland and Hungary. The criteria, a generalization at least of the criteria for whether you add on to social security, the

existing system, or whether you use part of the existing contribution to fund the private retirement accounts, tends to be the level of the initial contribution.

In countries with low contributions you usually add something to it. If you have a high contribution, like Argentina's 27 percent, it's hard to add something on to that. So you take out of it and you fund the private retirement accounts that way.

The graphic, which I don't know if you can see very well, shows the -- the U.S. is sort of purple color at the very right hand side, and it shows the relative rates of contribution to Social Security in the U.S. relatives to other OECD countries. Just so that you get a sense of where we are.

The other thing that you see in how these are implemented is that in the large part of the countries they tend to be mandatory, particularly for new workers and voluntary perhaps for existing workers. The reasoning behind this is that high income individuals already have access to supplemental retirement income, either through employers or through mutual funds, through access to all kinds of financial instruments.

It is low income people that don't always have equal access to these instruments. So, from an equity standpoint, often there's been a decision to make these

mandatory.

Secondly, if the objective initially is that these public Social Security systems are not financially sustainable, given the aging of the population and that something has to be done, the parameters have to be adjusted.

You can't adjust the parameters if only some people have supplemental income, because that would drive many people into poverty.

So the only way that you can make the system fiscally sustainable is if everyone can then count on a supplemental source of income.

The level of contribution to most of these funded systems, and this is now the last graphic, is generally greater than five percent. I don't know if you can see this in the audience, but the green bars show you the level of contribution to the funded system in various countries.

And what you find is that only in three countries that have used funded private retirement accounts is through contribution rates. Are the contribution rates less than five percent?

The logic behind that is that you do need a significant base of money to be able to accumulate assets in order to really make it worth the effort. Let me very quickly talk about -- just mention that generally in the countries that have adopted these accounts the accounts are

working well.

Small problems have arisen mostly in the developing countries, our client countries, not so much in the higher income countries, related to whether there are investment choices are available, what the regulatory regime is and the level of administrative costs. But most of these would not really be an issue as far as the U.S. is concerned.

The very last point that I would like to make is something regarding the popularity of these accounts. As we watch these pension reforms unfold through the World Bank perspective, we followed a lot of these pension reforms from the beginning stages, as you are in here, to the very end of how these pension reforms get implemented, and there is always a lot of controversy and tension.

Pension reform seems to be one of the most politically difficult reforms to undertake, and usually people say that -- you know, people want security, they don't want this choice and so forth.

But when a pension reform is actually implemented and when people are actually given a choice, in country after country they overwhelmingly choose this private option. Let me give you one example.

In Uruguay there are 600,000 contributors in the national Social Security system, and before they implemented the reform they had done all of these surveys that showed

that only 80,000 people were probably opt for the private choice. When the choice was given to people, more than 400,000, more than two thirds of the contributors, actually chose the private option.

So despite the political rhetoric that, oh, nobody wants these, these aren't popular, overwhelmingly individuals, people, really do like them. Thank you.

CHAIRMAN PARSONS: Thank you very much.

(Applause.)

CHAIRMAN PARSONS: Questions from the commission?

MR. RODRIGUEZ: Thank you to all three of you so much. This is for Valerie and for the Judge, if you don't mind, Judge. It seems to me you are both very happy with your plans. Let me ask you.

Have you had many workers in this plan say they would like to return -- since they have been in this plan say they would like to return to Social Security?

MS. VANDEWEGHE: I don't know the numbers. I do know that when city employees are first hired, if they have not heard about our SPSP plan, they may be a little concerned that they no longer are participating in Social Security. However, once they understand the plan, they -- we don't hear from them again.

Also, you have to remember that the City of San Diego -- the SPSP plan is only one piece of the retirement

plan for the city employees. We also have a defined benefit plan, which is what I would equate to Social Security, where an employee has a monthly pension that they will receive based on their years of service and percentage of their highest year salary.

So this coupled with the defined benefit, most people don't ask to go back into Social Security.

JUDGE HOLBROOKE: The answer in Galveston County is no. We had a lot of opposition when we had this employee election, from organized labor, the county labor unions and some from some of the old line democrats who thought that anything Franklin Roosevelt did was gospel and nothing should be changed.

But I don't think there is a single person in Galveston County, in the employ of the county, that would like to change it now.

CHAIRMAN PARSONS: Gwendolyn.

MS. KING: It is a question for Anita. Anita, you have a seen a number of these systems around the world, and I suspect you have seen situations where governments themselves have invested the funds and situations where individuals have been allowed to invest the funds.

Can you just give us an idea of which, in your opinion, seems to be a preferred approach?

MS. SCHWARZ: If you look at the international

experience, while there are periods and there are governments that are better than other governments, in terms of investment, you generally find that private fund managers have been able -- even within the same country have tended to earn higher rates of return on the pension fund returns than publicly managed funds.

And often what happens is that the publicly managed funds may be compelled by the government to invest in government bonds only, which, of course, are never going to pay as high a rate of return as a more diversified portfolio.

So there may be sort of political and social constraints that limit the public fund manager's portfolio choices relative to the private fund manager.

And the private fund manager is not looking out for what does the government have to pay and this is a good deal for the government. They are only managing the funds for the workers' best interest, and that tends to be the best rate of return, given the reasonable amount of risk.

MS. KING: So would you say that there is probably more political interference with the one than with the other?

MS. SCHWARZ: Definitely. Definitely.

MS. KING: Yes. Thank you.

CHAIRMAN PARSONS: Tom and then John.

DR. SAVING: Anita, I have kind of question that -- because I think you brought up there is this overwhelming

popularity of the private plans. And have you looked at the relation between the percentage of people who opt in and the fiscal sustainability of the public system?

I mean, is there some relation there in those countries?

MS. SCHWARZ: It depends on the countries and the way that the system is structured. If the system is structured so that part of the Social Security contribution is being taken out to put into the private retirement accounts, for a period of time there is going to be a fiscal transition cost involved.

I mean, it is instead of the entire contribution going to the public social security system. Now a portion goes to the private retirement accounts. That means there is less revenue going into the public system, and so there is a short-term problem.

But usually this is a problem that is going to be taken care of pretty much after one generation, and then, as people have access to their own individual accounts, then there is a possibility of downsizing and maybe better targeting the public system to cover people who wouldn't have adequate retirement from their own individual retirement accounts.

So it is a transition problem more than a permanent problem.

DR. SAVING: Well, that was interesting. I'm glad you said that, but that really wasn't my question. My question was the popularity, as measured, for example, by the proportion of the people who opted into the system, I am asking is that affected by the fiscal sustainability of the public system as they view it when they're comparing opting in or staying in the public system?

And the question would be if the public system is unsustainable -- say Uruguay, for example, and they say they can't ever pay these benefits and then you would say once people are given the opportunity to get out of the system that they don't ever expect to get anything from, they opt out. And that was my question.

Is there some relation between the proportion of people who opt out and what, say, the World Bank views? Not what those individuals view, but what the bank views as the sustainability of the system in that country.

MS. SCHWARZ: I think there definitely is. I mean, if you ask a person the question, do you like having the government take care of you, most people will say yes. But if you ask the question, do you really think the government is going to do a good job and are they really going to do it, then -- I mean, by the fact that people are voting by their feet and choosing to join the private systems, it suggests that they -- even if the rate of return in a very generous

system, as Uruguay actually had before they did the reform -- people were walking away from what looked like higher rates of return to a system that probably would pay market rates of return, and they were doing it voluntarily.

The only reason to do that is if you don't have faith that the government is actually going to pay.

DR. SAVING: Thank you.

CHAIRMAN PARSONS: I have a question for you, Valerie. I don't see any other hands up. One of the issues that we face on this commission -- in fact, I heard some testimony earlier in the day about it -- is the risk of allowing people to manage some portion of their own future, that the stock market, bond markets are risky and people will somehow fritter their dough away because they're not sophisticated.

Now, I think you said that five or six years ago San Diego moved to a posture where individual employees can now manage their own accounts or direct the management of their own accounts.

MS. VANDEWEGHE: That is correct.

CHAIRMAN PARSONS: And I assume that the municipal plan here in San Diego covers sort of the full range of working people, from blue collar to white collar, low income to high income; the whole spectrum.

MS. VANDEWEGHE: That's correct. Yes.

CHAIRMAN PARSONS: And how many people are in the plan altogether?

MS. VANDEWEGHE: There are probably 7,800 employees that participate in SPSP, again because the police officers and the firefighters do not.

CHAIRMAN PARSONS: Okay. So in that period of time, in the period of time that these -- let's call them 8,000 -- folks have been permitted to have some dominion control and guidance over the management of their accounts, has anyone lost all of their money that they have had under their management?

MS. VANDEWEGHE: No. That has not happened. Is the potential there? Yes, it is. Not in the past five years market however. And again, the returns that I had mentioned where if an employee, again, is not savvy about investment, has no interest in investments, if they are in the managed income fund, over the past five years the earnings have been 6.33 percent with virtually no risk at all under this plan.

CHAIRMAN PARSONS: That is the default option?

MS. VANDEWEGHE: That is correct.

CHAIRMAN PARSONS: And that is someone who chooses not to?

MS. VANDEWEGHE: That's correct.

CHAIRMAN PARSONS: But I am talking about those who felt, you know, sufficiently content to exercise some

control. Has anyone actually even lost money? That is to say come out of this period with less than they put in?

MS. VANDEWEGHE: Not in looking at the returns. Over the past five years, since they have had that option available to them, there has been no fund that has returned a negative earning. It has all been a positive return.

CHAIRMAN PARSONS: It would be fair to say that there are risks, but the experience that your system has over the last five or six years, you know, with 8,000 individuals, it is more theoretical than real?

MS. VANDEWEGHE: That's correct.

CHAIRMAN PARSONS: Thank you. Are there any other questions for this distinguished panel?

(No response.)

CHAIRMAN PARSONS: Well, thank you very much. I appreciate it. We may take you up on that Galveston office, but it will be in December.

JUDGE HOLBROOKE: Right. However, if you can't come to Galveston, well, you ought to come to Texas A&M and have a meeting at the Bush Library.

CHAIRMAN PARSONS: Thank you very much. Well, we have actually managed to pick up a little time here. I don't know if all of our panelists for the sixth panel, which are, you know, the experts, the other interest groups from across the political spectrum, are here. So let me see.

We may take a break. But if they are all here, I think we should just push off and get going. So, Peter Ferrara?

MR. FERRARA: Present.

CHAIRMAN PARSONS: David John? Oh, he is there. Percil Stanford? Percil. Excuse me. I'm sorry. The hour is late. Roger Hickey? Do we have a Roger Hickey?

(No response.)

CHAIRMAN PARSONS: Well, in fairness to Mr. Hickey, who I know came some distance today, he is from the Institute of America's Future -- anybody from such a well titled institute deserves an opportunity to testify.

I am going to suggest we take a five-minute break, and we will be back here in five minutes. And we will see if we can round up Mr. Hickey, who I know is here, and we will get going again. So, five minutes.

(Whereupon, a brief recess was taken.)

CHAIRMAN PARSONS: All right. We are going to get going. Again, our panelists are Peter Ferrara, who is with Americans for Tax Reform; David John, who is with the Heritage Foundation; Percil Stanford, who is with the National Committee to Preserve Social Security and Medicare; and Roger Hickey, who is with the Institute for America's Future.

If nothing else, this panel represents the most

distinguished sounding groups of all the previous panels to be sure. We feel safe in your presence. Peter, why don't you start us off.

INTERESTED GROUPS FROM ACROSS THE POLITICAL SPECTRUM

By Peter Ferrara

MR. FERRARA: All right. Thank you very much, Mr. Chairman. What an exciting and tremendous, truly historic opportunity each of you has as members of this commission, for the reform that President Bush has so wisely and bravely asked you to study and report on, granting workers the freedom to choose a personal account option for Social Security, is the most progressive idea on the national agenda today.

Indeed, it is the most progressive idea we've seen come along in many years, for no other reform that we could adopt could do so much to help working people, African Americans, Hispanics, women and the lowest income workers.

We have heard much in recent years about a growing wealth gap in America. Well, in the last 20 years those in the top half of the income population have been riding the capital market boom with investments in IRAs, 401ks, stock options, et cetera. But those in the bottom half of the population have been losing out, because they don't really have significant funds to invest and participate in the capital markets.

So they are losing out twice. Not only do they have lower wages than their colleagues, but now their colleagues are getting a double hit in the capital markets as well as the labor markets, and people in the bottom half of the income distribution don't have an opportunity to participate in that.

The personal accounts are the one real opportunity we have to grant lower income and moderate income working people the freedom to participate in these capital markets, as well as the higher income workers. And the studies going back many years show -- Martin Felstein, for one, did a study even 25 years ago, which showed that shifting to a personal account type system in place of Social Security would reduce the national concentration of wealth by 50 percent.

More concretely, a personal account system offers the prospect of granting lower income workers much higher benefits. I want to offer you an example from a book that I wrote with Mike Tanner that was published by the Kato Institute in 1998, *A New Deal for Social Security*.

In there was one of the examples. We offered the case of a husband and wife entering the work force, and they are both career minimum wage workers. They will earn the equivalent throughout their career of the minimum wage their entire lives.

And we examined the case. Suppose they could save

and invest what they and their employers would otherwise pay in Social Security into a personal account system. And we accounted for survivors benefits, we accounted for disability benefits, we accounted for administrative costs and everything else that we have heard so much from the critics about.

And what we found is by the time these workers reach retirement, assuming just a real rate of return of four percent, which is just over half the average return earned in the stock market over the last 75 years, a real return of four percent, they would retire with \$375,000 in today's dollars.

That would be enough to pay them over twice what Social Security promises but cannot pay.

Perversely, Social Security offers an even worse deal to African Americans and other minorities with below average life expectancies. As we have heard before, a black male born today has a life expectancy of 64.8 years.

I am going to let the spokesman from the Heritage Foundation speak about this, but they produced a path breaking study a couple of years ago that showed extremely low returns that African Americans could expect from Social Security even if it could pay its promised benefits, and so they, in fact, have the most to gain from a personal account option.

I discuss here in my testimony how you could structure a personal account option to enable African Americans and others with this issue to avoid the negatives of the lower life expectancy. For example, you could allow them to invest in investment programs through social organizations, like the NAACP or other organizations that has -- whose membership is predominantly African American.

And then, because the pool would all have these lower life expectancies, the benefits that they pay out would take these lower life expectancies into account. So they would be able to get higher benefits with the funds that they saved and invested.

And also, when they died, they would have real concrete funds that they could leave to their children, which would help to promote economic growth within the African American community. Moreover, the long-term Social Security financing crisis.

You know, low income people cannot afford -- modern income people cannot afford lower Social Security benefits. They cannot afford to pay higher taxes now. The personal Social Security accounts offer the one real chance for them to avoid that dilemma by shifting to an alternative system that will, in fact, provide them better benefits over the long run.

Finally, personal accounts would broaden personal

ownership of business and industry. All workers would own a share of the nation's business and industry. Think of that as practically a socialist dream. The workers are all participating in capital ownership.

But, of course, as this ownership would be direct rather than through the government, the result would be more appropriately called worker capitalism, and that broad ownership would promote social and economic harmony and solidarity.

Workers in other countries around the world are, in fact, already earning increased benefits through these personal account type systems, and polls consistently show that a substantial majority of American workers by that they would get a better deal through these personal accounts as well.

Self-appointed elitist who would deny them these choice are not benefitting or truly representing the working people of America. All true progressives I believe would have to support a truly liberating personal account option for Social Security.

And the final point I want to make I discuss in detail in my testimony. I think the commission should focus on designing a progressive personal account option that will make good on these possible benefits for working people. Most importantly in that is the question of if people

exercise the personal account option, what happens to their Social Security benefits?

And I am concerned that you have a strict proportionately in that offset; so that if a worker opts out of say 30 percent of the Social Security taxes over his entire career, he foregoes 30 percent of the Social Security benefits in retirement, no more than that, and then he has the benefits from his personal accounts, which would more than make up for that.

So we want workers to be able to reap the promise of a good deal that a shift to these personal accounts offer.

I would also support adding a progressive feature to the plan where the government would provide some sort of match for the contribution for the lower income workers, thereby giving them a double hit.

So not only will they get much higher returns, now they have contributions, their contributions are matched and they would have even higher retirement benefits in the future. All of this must be backed up by a government guaranteed minimum benefit. Every country around the world that has shifted to personal accounts has had a guaranteed minimum benefit.

And through this feature all of those who are running around saying, oh, this is a cut in guarantee benefits, blah, blah, blah, would be proven to be wrong

because you can -- I, in fact, advocate that you guarantee, as a guaranteed minimum benefit, that workers would receive under the reform at least what they were promised under the old Social Security system. That, in fact, would be an increase in benefits for lower income people because the current system cannot pay those benefits.

Finally, I just wanted to make a couple of points about the transition. I have been working and writing about this for over 20 years, and from the very first paper I wrote about this we all said, all of us who favored a personal account option, you have to use general revenues to finance the transition.

There is just no other way you can do this. I, in fact, would urge you not to try to cut Social Security benefits at all to finance the transition. Make this a positive, progressive, populous reform that truly and clearly benefits working people. And so, you have to turn to general revenues.

I discuss in my testimony a mechanism for doing that. We can go into that more in the questions and answers.

But the question is where are we going to get these general revenues from. And I discuss that not only in here, but in many of the books that we have written over the years, published with the Kato Institute, the Heritage Foundation and many others.

First of all, the new savings and investment in the personal accounts themselves. The new savings and investment in the personal accounts will generate new revenues, feeding back into the system.

If you generate new capital income, part of that will be taxed at the business level, and that will generate new revenues. I believe Martin Thomas Saving has written about this, Martin Felstein has written about this, Phil Graham has written about this, and this is an important source for you to look at.

Despite what we hear about the critics of President Bush's tax cuts, we haven't reached the end of total federal surpluses, and I believe you are going to see, once the economy rebounds, the reappearance of federal surpluses outside the Social Security system and that will be available to help finance the reform.

Over the long run the personal accounts themselves will help to reduce the Social Security financing gap because people will be relying on the personal accounts in place of part of their Social Security benefits, and so the long-term gap would be reduced.

And there are many other areas where you can get general revenues to help finance the transition. But to close, I would urge all of you to -- this is a tremendous opportunity you have. You want to make good on this. The

them here, in my opinion, is that this is a tremendous opportunity to benefit working people and lower income Americans, and I congratulate you on your efforts and your bravery. Thank you very much.

CHAIRMAN PARSONS: Thank you, Peter. You slightly changed the order by the way you are seated, but let's go with the way you have seated yourself. Roger.

INTERESTED GROUPS FROM ACROSS THE POLITICAL SPECTRUM

By Roger Hickey

MR. HICKEY: Well, I want to thank you all for holding the proceeding until I could be located, and I apologize to those of you who are thinking about hitting those early flights back east. I do want to note for the record this commission started this session half an hour early, and I hope that bodes well for hitting other deadlines that you have set for yourself in this very ambitious effort.

President Bush has given you a very, very difficult mandate. He has asked you to strengthen Social Security. At the same time he has asked you to look into privatizing, at least partially privatizing the system, and he has tied your hands by passing a tax cut that uses up most of the available non-social security federal surplus.

I don't believe there is such a thing as a free lunch. You are going to have a very, very difficult job in trying to square this circle.

I represent the new Century Alliance for Social Security, a broad coalition of groups which believes that the President's goal will weaken, not strengthen, the Social Security system. We believe that in order to carry out President Bush's mandates it is virtually certain that you will have to make dramatic cuts in Social Security's guaranteed benefits, probably raise the retirement age, probably both, because privatization will worsen rather than solve the financial problems, whatever financial problems are currently facing Social Security.

So it is well known that there are proposals to strengthen Social Security without privatizing and without across the board benefit cuts or tax hikes. They have been put forward by many experts; Henry Aaron, former commissioner Robert Ball, economist Peter Diamond at MIT, Dean Baker and others. We should be debating the details of these pragmatic plans we believe.

Yet ironically, President Bush's proposals and the commission's work may turn out to be impediments to a real national debate about thinking about Social Security, about making it financially stronger, and it is my strong belief that we are going to have to get through this debate about privatization before we can get back to the real debate that we ought to be having about strengthening Social Security.

Therefore, I would urge you to accelerate your

efforts. I would urge you to move ahead with the agenda that you intend.

Now, it is important that you hear from critics of privatization, and I am glad I have this five minutes. But I have to take some of that five minutes and note that you have invited no one from the National Urban League, the National NAACP, the National Council of LARASA, the League of United Latin American Voters; all of these groups have done important studies and expressed concerns about the impact of privatization on their -- the people that they care about, especially low income Americans.

No one will testify here today from the wide array of disability rights organizations who are concerned about the impact of your recommendations on survivors and disability benefits.

You have invited a representative of one women's organization, OWL, a group that is critical in privatization, but where are the leaders of many other women's groups? NOW, the National Women's Law Center, Business and Professional Women, The Feminist Majority, the Institute for Policy Research?

All of these groups have warned that privatization represents a bad deal for women. You will not hear from some of the major senior citizen groups. The Reliance for Retired Americans, AARP. No one from the American labor movement is

testifying here today. Church organizations, conservative and liberal, have spoken out against privatization, but they are not represented here, and you have not invited one organization representing young people who, after all, when they reach retirement age, will bear the brunt of whatever plan is passed on Social Security's future.

The commission is not listening sufficiently I believe to the critics of privatization, but I would like to end by expressing a little sympathy for the challenge you now face. This hearing requires you to go through the motions, but the fact is that President Bush has given you a charge that really requires that you ignore our voices.

He wants you to produce a plan that partially privatized Social Security, and short of rebelling against the President's mandate, the best thing you could do for the country is to produce a privatization plan that is clear and honest and transparent about the costs and trade offs of going to private accounts.

If your privatization plan requires benefit cuts or reductions in costs of living adjustments or if it will raise the retirement age, tell the public clearly and in details. And if your projections of a rapidly growing stock market depend on a booming economy in the future, be sure to explain that a booming economy would also go a far distance to solving the problems facing Social Security financially.

If disability and survivors benefits are to be cut, let the people know, and try to estimate accurately the added management costs of administering millions and millions of private accounts, as compared with Social Security's less than one percent overhead.

For many years the debate about privatization of Social Security has had an abstract shadow boxing quality about it because the specifics were not being debated. If your commission can clarify the real choices and the hard trade offs involved, I believe the American people will reject your plan. But whatever the outcome, you will have done a true service to our public debate and to our democracy. Thank you very much.

(Applause.)

CHAIRMAN PARSONS: Thank you, Mr. Hickey. David John, from the Heritage Foundation.

INTERESTED GROUPS FROM ACROSS THE POLITICAL SPECTRUM

By David John

MR. JOHN: Thank you. I would like to thank you for holding the hearing, and I especially would like to thank you for holding it in San Diego. I have always wanted to see the city.

This is not a theoretical discussion. If we look, for instance, at what this means to my 15-year-old daughter, Meredith, because this is the reason that I'm involved with

this debate, Meredith retires in 2050. At that point the Social Security trust fund, whatever it consists of, will be a distant memory. It will have been gone for 12 years.

Anyone who is born after 1971, and there are several of them in this room, basically are going to retire after the trust fund is long gone.

Now, when Meredith retires in about 2050 or so, the Social Security deficit, if we do nothing, basically will be of a size so that her kids and her grandchildren are going to have the choice of either funding something like the Department of Defense or all of the domestic discretionary programs of the U.S. Government or paying her full retirement benefits.

As a parent, I don't think it is responsible to leave her with that kind of a situation, and I don't want to leave that kind of a choice.

Now, I believe that personal retirement accounts are essential to the solution, but there has been an awful lot of discussion about why, and I'd like to turn to how. I'd like to make a couple of specific relatively practical points.

Point one, if you are going to put in a personal retirement account, I think it should be styled as Social Security Part B. Make the original system Social Security Part A. That way it is very clear that this is part of

Social Security, and when you retire, your benefits will be a combination of Social Security Part A and Social Security Part B.

Second, I think one way to preserve the current progressive benefit structure of Social Security is to have a progressive personal retirement account contribution system, such as a person might put in four percent, five percent or whatever of their first \$10,000 of earnings, three percent of their next \$20,000 earnings or something along that line.

This way the lower income individual will have a real opportunity to mass some real wealth rather quickly. Next, for married couples, I am very concerned that my daughter is going to face a situation to the current Social Security that if she stays home with her kids, and she says very definitely that that is what she wants to do right now, that she is going to get zero retirement credit. That is the way it is under the current system.

Now on the other hand, if she and her husband split their contributions to their personal retirement accounts, not only does that take care of the situation where, in most cases, a woman's lifetime earnings is lower than a man's, but it also means that during the time that she stayed at home with her kids, that her personal retirement account will continue to grow. We think this can be done with a minimal administrative cost.

Next, we think that the Social Security Administration, while a very organization and does a wonderful job of determining benefits, we think they should not be involved in any form of regulation of these personal retirement accounts. As I say it has a fine record with determining benefits, but it has absolutely no record at all or no experience with financial regulation.

We think that if there is a regulation, and we think there should be, that it should be done like something like the SCC. The SCC knows the markets very well.

Finally, I would like to suggest that as much as I'd love to sit here and say that people should be allowed to put all of their money in government bonds, that the simple fact is that there is not enough return in government bonds to allow them to build a sufficient personal retirement account to replace a significant portion of the Social Security Part A.

As a result, I think it is going to be necessary to put some form of a -- or the personal retirement account contributions in other types of investments, whether those are corporate bonds, equities, stock index funds, something along those lines, is up to you to decide. Personally, I like the idea of stock index funds and corporate bond funds.

Last, but not least, I want to say one thing about what I think would be a serious mistake. Various sundry

people have suggested that one of the things we can do is to bust the wage cap. In other words, let's charge Social Security benefits to everyone regardless of their wages.

Now, it is fine and dandy to talk about taxing the rich, but the simple fact is you are going to have to stomp on an awful lot of middle class people in order to get to them. There are very few people who make what Tony Gwynn or Bill Gates or Donald Trump make. There are an awful lot of people who make much lower than that, but still who are outside of the earnings cap right now.

We did a study a couple of years ago and said, first off, it doesn't save Social Security. It adds about six years to the life span. Second, it raises taxes for about 9.2 million Americans, the biggest amount of them 1.4 million, which happens to be here in California.

Of those 80 percent are married couples, 46 percent have children, about a 10th of them are union members, and about 10 percent of them are nurses, teachers, truck drivers, farmers, police, mechanics, et cetera.

It is fine, as I say, to talk about taxing the rich, but most of the people you would be hitting in this case are not rich. Thank you.

CHAIRMAN PARSONS: Thank you, sir. Percil Stanford, do you want to bring us home, and then we will get to the Q&A part.

INTERESTED GROUPS FROM ACROSS THE POLITICAL SPECTRUM**By Percil Stanford**

MR. STANFORD: Co-Chairman Parsons and members of the commission, I appreciate the opportunity to come and testify today. I am professor and director of the Gerontology Program at San Diego State University, and I am here representing the National Committee to Preserve Social Security and Medicare. It is one of the major organizations representing millions of older people here in our country.

One thing that I am very pleased about is that the commission is focusing on strengthening Social Security, and I think that is what we need to underscore. Social Security provides benefits in a manner that is progressive and fair. No other wage replacement program, public or private, offers the protection of Social Security, old age survivors and disability insurance programs.

Thirty-eight percent of all Social Security benefits are paid to disabled individuals, spouses of retired and disabled workers, dependent children and survivors, and I think we need to underscore that.

Although Social Security is currently running a sizeable annual surplus, the trustees anticipate that changing demographics will lead to shortfalls over the long run. While these projected shortfalls present challenges, I would like to be clear that, in our opinion, Social Security

is not in crisis and I want to underscore again radical restructuring is not necessary and is unwarranted at this time.

The National Committee to Preserve Social Security and Medicare remains committed to maintaining Social Security as a system of social insurance that pools the risk among all workers. What about the Social Security insolvency question?

Beginning in the year 2025 interest in tax revenues combined will be insufficient to meet demands, and the program will need to redeem some of the bonds held in the trust fund. In the year 2038, if no changes are made, the trust fund will be exhausted and incoming revenues will meet about 72 percent of its obligations. Even at this point Social Security will not be broken.

As Americans live longer, the inescapable conclusion is that it will cost more to support them in their retirement years.

Perhaps the biggest argument against transporting part of Social Security into a system of individual retirement accounts is the tremendous cost of the transition, which has been mentioned previously. Although individual accounts are often presented as a way to save Social Security, diverting money into individual accounts may worsen the Social Security's long-term projected shortfall.

Indeed, funneling two percentage points of payroll

out of Social Security and into private accounts serves to more than double the long-term shortfall. The level of individual risks privatization would introduce to Social Security is quite unacceptable.

Proponents of privatization like to talk about market averages; however, there is no such thing as an investor who earns the market average each year. The National Committee has begun to receive letters, phone calls and petitions from those detailing their concerns about the market downturns.

One such person, 63 years of age, purchased stock at \$39.00 per share. That stock is now worth 85 cents. That person would be destitute without Social Security.

Individual accounts could work well for upper income earners and earners without dependents. They would not work well for low income workers, people of color, disabled workers or families.

What are some of the alternatives? There are some alternatives that we would like for you to seriously consider. First, supplementing payroll taxes with general revenue. An influx of dollars from general revenues would help meet the increase demand of an aging population. Increasing the maximum wage base might be another.

Currently only the first \$80,400 of earned income is subject to payroll tax. The base should be increased to

at least 90 percent of covered earnings and then indexed thereafter.

Expanding the coverage: Newly hired state and local workers could be brought into the Social Security program. They would have, number one, increased retirement security; second, greater freedom in changing jobs; and three, added protection from the eroding effects of inflation on income.

The last: Government investment of a portion of the trust fund reserves. Private investment of a portion of the reserves should be seriously considered and debated. Some of the reserves could be invested in an index selection of stocks to allow Social Security to realize a higher return on its investments.

Co-Chairman Parsons, members of the commission, thank you for the opportunity to come before you today.

CHAIRMAN PARSONS: Thank you.

(Applause.)

CHAIRMAN PARSONS: We will get to the questions in just a moment. I do want to clarify, for your benefit, Roger, and for the benefit of anybody else who might be concerned that we didn't reach out far enough in connection with this hearing and the people we invited to testify at this hearing, there will be another hearing from the commission to hear from the public in Cincinnati on the 21st

of September.

Indeed, some of the groups that you referred to and some of the unions not only have been invited to testify, but have accepted. A number of the people you mentioned who were invited to testify did not pick up our offer. But I just want everybody to know that this isn't the only place and the only time and the only time in which we are going to be hearing from the public, both the critics of the direction in which the commission is heading and proponents of the directions.

So, having said that, do we have any questions for this panel? We will start with Estelle.

DR. JAMES: I have a question for all four of the panelists. My question concerns actually a topic that none of you talked about. It concerns retirement age and how that should adjust in a period when longevity is increasing and may increase very rapidly in the future.

I understand this is one of the most sensitive issues and people have very strong feelings about retirement age and whether we should change the retirement age. But even though it is a very sensitive issue, I think we do have to think about it and talk about it in the spirit of Mr. Hickey's comment that we have some very difficult trade offs to make, and I think this is one of them.

Just to give a little arithmetic example of the

importance of this, the choice of retirement age, if we think of a very stylized system, a pay-as-you-go system where people say enter the labor force at age 25 and retire at age 85 and suppose you have a stable population across generations, so we are not dealing with the baby boom problem here, then if people retire at the age of 70, the ratio of retirees to workers will be three to one, and you could provide an ala carte. You could provide say a 40 percent replacement rate with a 13 percent payroll tax in that case.

On the other hand, if people retired at the age of 65, then the ratio of retirees to workers increases to two to one, and either your tax rate has to increase by 50 percent or your benefits have to be cut by 33 percent. So it makes a huge difference, this retirement age makes a huge difference to what the costs will be or what the affordable benefits will be, and I think we have to think of the trade offs.

Of course, people want to retire earlier. Some of them are unable to work beyond a certain age, particularly people who do physical labor. On the other hand, a lot of the research, the data, indicate that people are not only living longer, they are also living healthier.

So, as I said, I think we have to think about this trade off about how much time we want to spend as a society in retirement years versus working years and what the costs are of continuing to retire early, the costs in terms of

lower benefits or higher taxes.

So I would like your opinions on what that trade off should be and how we should think about that in our deliberations. Whether we have an individual account system or not, this is an issue that we have to think about.

MR. FERRARA: All right. I'll go first. I don't think the commission should pick the retirement age. I think that one of the virtues of an individual account system is you can allow workers to individually to make that choice. Then they face the trade off.

Okay. I have accumulated so much in my account. If I retire earlier, the account can pay Ax@ in benefits.

DR. JAMES: But there would still be a remaining part of the pay-as-you-go system, unless you replaced it totally.

MR. FERRARA: Well, what I would urge you to do is to start down the road of the personal account option, and down the road then perhaps you would expand the personal account option and as people see the virtue of it and the benefits of it -- because I think this is a zero sum gain here. You are in a losing debate on the wrong -- playing the wrong game on the wrong field.

The public doesn't want you to raise their retirement age. Plain and simple. And you are just running up -- you know, this is a democracy and the people ultimately

get what they want.

A better system would be for you not to, as a sort of central planning operation, say this is this the retirement age for everybody. But to devolve that question out in a more market oriented system which says, okay, the more we go to personal accounts, the more you have the choice and the flexibility through those personal accounts to make that choice.

If you delay your retirement, you get full market compensation for that. If you want to retire earlier, you can plan earlier and make extra contributions.

For example, in some of the South American countries where they have this -- you are aware of this, where they have these personal accounts. People are able to plan at earlier ages and say, well, in addition to the required contribution, I'm going to contribute a little extra so I can retire earlier, because then I will be able to achieve my benefit target sooner.

So that is how I would urge you to address it. Address it through the personal accounts and give the workers the flexibility. Of course, as you know, there is not one answer for everybody.

You know, professionals who don't have a lot of manual labor, they can keep working until they are 80, particularly if they enjoy their work. Manual laborers want

to retire at 62, and a lot of them can't continue to work at the same proficient level.

So what you need is a highly flexible type of answer, and you can only get that through the personal accounts. I think it would be a big mistake to try to raise the retirement age for Social Security. I would not be in favor of it. I would favor adopting a personal account option and expanding it as quickly as possible.

MR. HICKEY: Let me start briefly by agreeing with Peter, which is unusual. I don't think that the American people want to see the retirement age raised. I don't think they understand that the retirement age has been raised, and I think that the American people, in general, see retirement age being held securely below 70 as a sign of economic progress; that more and more people, as you say, want to retire early. They are not pushing their retirement back.

Secondly, I would warn you very, very strongly that as a -- in the context of this privatization debate, it is a real loser. If this is seen as a trade off, as part of the trade off to get private accounts, people especially do not like it.

So, as I say, if we were debating how to strengthen Social Security -- I have this debate with my friends at Brookings and other places who think it is fine to work until you are 85 because they sit at a desk all day. Most

Americans outside of the beltway have really pretty tough jobs and don't want to have to work those tough jobs.

A waitress or somebody working construction wants to be able to look to a date certain at which point they can get off their feet. So I would especially warn you not to introduce raising the retirement age as part of the package of the private account system.

MR. JOHN: Great. Now I have got to agree with both Peter and Roger. Couldn't you have asked a hard question here?

The simple fact is that this is both an intellectual discussion and a political discussion, and while there is an intellectual reasoning behind raising the retirement age and there is a rationale for that, although it differs greatly for me where my greatest danger in a day is a paper cut and my grandfather, who was on a production line in Harley Davidson for most of his life and actually took a few days off because of industrial accidents.

However, as both Peter and Roger has said, there is a political area about this, and testing shows that the most unpopular single thing you can put into a plan is to raise the retirement age. So regardless of whether or not there is an intellectual rationale behind that, I would recommend against it.

MR. STANFORD: Well, I'm afraid I would have to

agree with my three colleagues here. Can we get a photographer up here?

(Laughter.)

MR. STANFORD: The first question I would ask is who are the losers when you raise the age? You have people who are just beginning to participate in the Social Security system in a way that it might make some difference in their lives, and suddenly, the ceiling is raised.

So my sense is that when you look at all of the studies that have gone on previously, going back to some of the midwest studies, it clearly shows that those persons who work the hardest and have the most, I guess, possible deficits in their lives are those who are the poor and near poor. So I would certainly say that we need to not consider raising the retirement age at this point under any circumstances.

DR. JAMES: So can I just summarize? A lot of Americans don't want to think about it. Are you also saying that if they had to think about it, they would be willing to pay more or to take benefit cuts? Or really, you are saying that this is such a politically sensitive issue people shouldn't even be asked to think about it?

MR. STANFORD: Could I add just one thing? When we talk about retirement, I think we really have to think about what mean by retirement in today's environment, because when

we talk about retirement in a traditional sense, it is not the same as it is in today's environment, meaning that people go from career to career or, in some instances, job to job, and they aren't looking, in some instances, to Aretire@ as we traditionally looked at.

So I think all of our answers may have some different connotations and the question may have some other different ring to it. But if you put it in the context of privatization or not, then it is a totally different question.

MR. FERRARA: The answer to the question also that you raised -- you know, I think if you personally sat down with each American and had a discussion with them you might be able to get many more of them to support the idea than will otherwise.

But since that is not going to happen, the question you have to think of is how do you get from there to here, and you are not going to get there from here by saying, hey, folks, we here in Washington have decided that we are all going to raise the retirement age.

What you can do is if you have a personal account system you may find that people on their own decide to retire later, that they decide that they want to preserve their assets or they can get higher benefits if they do so, but you have to think a way around the impasse, and I think it is --

DR. JAMES: You are saying a way around basically is give people choice and give them incentive?

MR. FERRARA: Right.

MR. HICKEY: And I would reiterate my point that -- well, think about the people who would get the least out of a private account system, the people who would get very, very small minimal private accounts because of their low income wages. Those are the people who would most resent the idea of trading those private account systems for an increase in the retirement age. So it is a double loser for those people.

MR. FERRARA: Well, I have to disagree with that, because --

CHAIRMAN PARSONS: We have a number of -- I think we found the place where everybody was in agreement. Let's move on. We have got Lee, then Fidel, then Mario and then Gerry.

MS. ABDNOR: Thank you. Thank you all for coming to this hearing and for sharing your views with us, and I know most of you came a very long way. I would like to direct my question to Roger, and that is it would be very helpful for me and us if you could be more clear, more honest and more transparent if you will, to quote you, about what your organization supports to strengthen and sustain the system and to pay benefits in the future.

You talk in your testimony about devoting some of the general surplus, you know, the general fund surplus to the Social Security trust fund. Well, you know and I know that cash coming into the government, whether it be in the form of income taxes or Social Security taxes, cannot be held by the government, that there is, in fact, no account with cash in it. It is illegal. So the trust fund holds IOUs.

And if you are then relying on the trust fund to pay benefits starting in 2016, where does the money come from?

And the second question is your organization -- you represent lots of organizations. Tens, dozens. Right?

MR. HICKEY: Yes.

MS. ABDNOR: And you have been one of the leaders in the field in Washington for several years. I know at least as far back as my experience in it. And I guess -- so my second question is is there a plan that your organization supports for strengthening and sustaining the system? That is really kind of a similar question.

What plan do you support of those that have been put forward? Or have you put forward your own?

It seems, frankly, that I hear lots of attacks on personal accounts, but I don't hear any plan that your -- but I could be wrong. That your organization supports that will, in fact, meet the 75-year standard and the cash that is going

to be needed.

MR. HICKEY: Yes. I tried to be clear. I represent a coalition of groups that represents a diversity of views, and as you know, it is a broad array of groups. Some of them would invest the trust fund, for example, to get a better return collectively. Some of them would not.

My point is, number one, that we need a debate, a public debate about those various options to strengthen the existing guaranteed benefit of the Social Security system. I am not prepared to give you a plan right now.

We are here in the context of the President's commission, and I am simply warning that it is our view that private accounts get in the way of that debate. They get in the way of the solutions that we need to guarantee Social Security's future solvency, that we have a couple of good three or four or five years to have that debate, and we are probably going to have to wait until after this private accounts debate is dealt with.

I said that there are plenty of good proposals out there that achieve actuarial solvency --

MS. ABDNOR: What proposals do you like?

MR. HICKEY: Henry Aaron's proposal. Robert Ball's.

MS. ABDNOR: And they do what essentially?

MR. HICKEY: Well, it is a combination of investing

the trust fund, of -- in the stock market collectively. Adding -- raising some taxation on upper income earners. And also, adjustments, in careful ways, of benefits.

So I am not completely opposed to any of those things. I think we ought to be debating them, and we ought to be -- and my point is we will probably not get to that debate until after we have had this debate about private accounts.

MS. ABDNOR: Well, I think that -- and I appreciate what you just said, and I would like to make the point that Henry Aaron's plan, as I understand it, also increases the retirement age. Right? It does.

You just said that that is one that you support, so I would just like to make that point. That it doesn't seem that you support all of what is in that plan, because you just said you are against increasing the retirement age. Correct?

MR. HICKEY: I personally would not support increasing the retirement age.

MS. ABDNOR: Even though that is part of that plan. Okay. I guess what you are saying then, Roger, is if we take off the table personal accounts, then you are willing to enter into the debate on how we can strengthen the system.

But I would suggest to you that personal accounts is one of the things that should be on the table because it

is one of the things that a lot of people support and that we would like to engage. That is partly why we have invited you to come and need to hear your views.

Personal accounts are very much a part of what a large number of the American public support and they need to be on the table as well, and to say that they have to be off the table before we can sit down and say, okay, this is what we are going to support and this is what we are not, doesn't make any sense. It is like otherwise, I am going to take my ball and go home.

MR. HICKEY: You underestimate the importance of this commission.

MS. ABDNOR: I don't underestimate it at all.

MR. HICKEY: This commission is dominating the debate about the future of Social Security, and I'm here to tell you that there is a large constituency of organizations who think that private accounts, in any way, shape or form that you are likely to come up with, are likely to worsen the financial situation of Social Security, requiring drastic cuts in benefits and increases in the retirement age that we could not support.

CHAIRMAN PARSONS: I think the commissioner's point only is that is well and good as far as it goes, to say that we think you may be headed down the wrong road. Full stop.

The question was, all right, so what do you think

is the right road? And I guess where the two of you hung up is you are saying, well, let's have a debate. That is not a very helpful response to the second part.

One of the things the commission is looking for, and we stated this at the outset, are what are the alternatives? Not only was the analysis behind the first conclusion that private accounts may be wrong or wrong headed, but here is some alternatives that will get us to -- you know, this is called the commission to strengthen Social Security; that will strengthen the system and that will enable us to create a sense of confidence on the part of people that the promise -- we have been all calling it the promise, which I call the schedule. But the promise will be kept for future generations. I think that is what Lee is looking for.

MS. ABDNOR: Thank you. That is exactly right. We really need to get that input.

MR. HICKEY: And I would direct you to a number of proposals that have been put forward. None of them may be a test of purity, but all of them are in the range of proposals that should be discussed, debated and moved on if we are going to strengthen Social Security.

MS. ABDNOR: Like Henry Aaron's and --

MR. HICKEY: And Bob Ball's

MS. ABDNOR: And including -- so what you are -- if

I understand you, Roger, what you said was that we ought to be considering government investment in the stock market, we ought to be considering raising payroll taxes and possibly cutting benefits? Those were the three things that you mentioned as part of -- and I just wanted to be clear that that was what you said, that I understood that correctly.

MR. HICKEY: Not raising payroll taxes across the board, but lifting the cap.

MS. ABDNOR: Lifting the cap. But raising payroll taxes on the higher income or middle and upper, depending on where you put middle and upper.

MR. HICKEY: Yes.

MS. ABDNOR: Okay. I just wanted to clear exactly what you are suggesting. But to see a full blown plan that -- I am not sure that those things would sustain it for 75 years. It would be helpful to see, you know, a plan that would do that, since that is what we are coming up with as well.

But thank you for those comments. I appreciate it.

CHAIRMAN PARSONS: Okay. Fidel, Mario, Gerry and then Tom.

MR. VARGAS: Peter, your proposal actually is probably one of the most progressive that I have heard. You said fund the transition with general revenues, guarantee a minimum benefit and maintain, if not improve, the

progressivity of the system as it stands, and to do that -- so that we could have personal savings accounts.

And my question is -- I forgot your name. Roger. Roger. I apologize. Does that proposal, you know, at all lessen your concern.

You said personal savings accounts would worsen. Well, what if they didn't? Would you support them or not support them?

MR. HICKEY: Well, listen. If Leanne doesn't understand my proposal, I don't claim to understand Peter's at all. It came by us all very quickly, and it seems to claim to do everything for everybody without any pain at all.

MR. VARGAS: No. I think the pain comes in funding the transition with general revenues, and I am not saying that I would support that. That is why I said that is very progressive.

So I guess what I am trying to get at is why such the opposition to the idea of a personal savings account when we haven't even gotten to the point where we could say, you know, we could actually strengthen the system and add a component for a personal savings account.

MR. HICKEY: Yes. I am aware that there have been proposals put forward that claim to hold everyone harmless, and those tend to involve huge subsidies from the non-social security surplus or from the general revenues.

And you have a practical problem in dealing with those, in that we have -- President Bush has just advanced and passed one of the largest tax cuts ever that has virtually eliminated a huge national surplus that we might have devoted to that purpose.

I happen to believe that are other public needs that are not being met and that taking that surplus off the table through the tax cuts has prevented us from addressing important needs of children and other important goals.

MR. VARGAS: Wait a minute. So you oppose using general funds for the transition or suring up any other part of the Social Security system?

MR. HICKEY: I would much rather use general funds for dealing with a shortfall in a system of guaranteed benefits, rather than using general funds to fund a private accounts system. It would be an enormous, enormous transition cost that would not do anything to guarantee that people would be better off in a future Social Security system.

MR. VARGAS: My final question is first to you and then the entire panelists. You said we could, for example, repeal significant parts of President Bush's tax cuts and devote some of the resulting general fund surplus to the Social Security trust fund.

Now, I want you to explain how you think that trust

fund works, and assuming the actuarial assumptions and no changes are made, that we assume -- not us, but what the actuary says, what is going to happen in 2016 and 2038 and then -- and explain what you mean, because as far as I understand it, that money -- that surplus is paying off the national debt and has been paying off the nation debt and there is no money that is going anywhere, even if it weren't being spent in a tax cut.

So I am trying to get clear on what you mean by that. And since we have four experts, I still can't get a straight answer from most people on what they believe happens in 2016 and 2038, assuming that the actuarial assumptions are correct.

MR. HICKEY: I get your point that we will have to either borrow or find revenue to redeem those bonds. We made those borrowing commitments due to our plans to run us a deficit in the non-social security part of the government, and if we had not borrowed from the Social Security system, we would have borrowed from someone else.

So the -- we do face a problem with redeeming those bonds, but those are promises that we have made and those are debts that we had incurred in other parts of the government.

I do support a steady paying down of the debt in a slow and careful fashion; so that our country is going to be in better shape to finance those bonds when do need to redeem them.

But we are a wealthy country, and we are a financially healthy country and those bonds are as good as any in the world.

MR. VARGAS: Well, I'm sorry. What is repealing the tax cut going to do to the long-term problem to Social Security?

MR. HICKEY: Well, for one thing it would not require us to dip into the Social Security surplus as we may have to do this year.

MR. VARGAS: Again, what surplus? We are using that money to pay off the national debt. We are not using it to pay Social Security benefits. Is that correct? Or am I incorrect?

MR. HICKEY: That's correct.

MR. VARGAS: So we are using the money to pay off the national debt. We are not using it for Social Security. I don't understand why you are saying repeal the tax cut. I'm a Democrat by the way.

I don't necessarily support the tax cut, but I do support kind of intellectual honesty, and that is what I am trying to get at. What is repealing -- repealing the tax cut --

CHAIRMAN PARSONS: That is good for a Democrat.

MR. VARGAS: I'm sorry. Repealing the tax --- Roger, is not going to do anything to deal with the problem.

It is going to allow us to pay down the national debt. So let's just say that is what it is going to do, because that is what we are doing with the money.

Now, it is going to allow us to pay a little bit less now of the national debt because the surplus is a little smaller, but it is not going to do anything to strengthen Social Security.

MR. HICKEY: Well, it would allow to invest in education and other areas of the government, other areas of public need that would make this economy stronger.

MR. VARGAS: That is another debate though. That is not about Social Security.

MR. HICKEY: Well, I do believe it is about Social Security. I do believe that we in this country are starving the real sources of productivity in this country, and we are operating on the assumption that tax cuts are the be all and end that should be what we should use our surplus for.

MR. VARGAS: See, Roger, I don't disagree with you on that point. The problem is when we are talking about Social Security, I cannot honestly say that doing that is going to help me and what I am doing here today.

I agree we should be spending more money on education and the youth programs, but that is not my job here.

MR. HICKEY: Well, that is what I meant in my

testimony when I said that we should repeal part of the tax cut in order to be able to make investments that we are now ignoring; those investments which are very, very crucial to the further growth and productivity of our country, which is the basis of our ability to pay for Social Security in the future.

MR. VARGAS: That is different from what you wrote though.

MR. HICKEY: I'm sorry if I was unclear in my quickly assembled testimony. But my point was that the President is acting unwisely in assuming that all of this money is a surplus available to be sent back to the rich, when I believe that this money ought to be used to invest in young people, in growth, in job, in productivity enhancing investment that can assure that we will be able to pay our debts when that time comes.

MR. FERRARA: Can I answer your question now? You addressed it to all four of us, so let me take a swipe at it.

If you try to bail out Social Security by putting general revenues into Social Security on an ongoing basis, you do nothing to address the problem that Social Security offers workers today a very poor deal, a very low rate of return.

In fact, you are making that problem worse, because in addition to them paying payroll taxes, which they are already getting a bad deal, they now have to also pay some

income taxes into Social Security, and so that is going to make the return even lower.

And what I get from Mr. Hickey is that is too bad.

You could eat cake. You are going to get that bad deal and you are stuck with that bad deal and it is going to get worse forever and ever. This is the first time I have heard also an economic theory that says the way we increase economic growth is to increase taxes and increase government spending.

As to your question as to what happens in 2016, at 2016 the government -- the Social Security has to start turning in over \$5 trillion in government bonds, and the crisis starts there because the government has to come up with \$5 trillion from somewhere. And in 2038 they don't even have government bonds to turn on, and the government, on the current course, will either have to raise taxes or cut benefits.

That is what is in these other plans, Mr. Aaron's plans and all of these other plans, and all of that, again, will make the rate of return on Social Security even worse. If you cut benefits, it will make the rate of return worse. It will make it a worse deal. If you delay the retirement age, it will make it a worse deal.

If you raise taxes, it will make it a worse deal. How can you tell the American people you have to pay basically 1/8 of your wages into this program for a very poor

deal and that is it, we don't care, you are going to be stuck with that forever.

MR. JOHN: Let me try something slightly different.

If you took all of the economist in the world and laid them end to end, they still couldn't reach a conclusion.

Given that, you could take the entire surplus right now and heap it up in Qualcomm Stadium and burn it, and it is not going to make a blessed bit of difference as to how we pay for Social Security. Whether it is in 2016 or 2038.

Basically whether you use to fund programs, which I think would be a mistake, or whether you use it to pay down the national debt, which isn't a whole lot better, it doesn't help. 2016 is still going to come. 2016 is still going to have roughly the same deficit as it does right now.

The question of transition, to my mind, always needs to be answered as compared to what. Right now my daughter is facing \$5 trillion in today's dollars to pay off the bonds in the trust fund. Five trillion dollars.

Now, the question is what does she get for that money. I'll pay part of it. Is she going to end up with that \$5 trillion put towards a reformed system, whether it includes personal retirement accounts or not? Or does she have \$5 trillion that gets spent or what, and then we have got another \$17 trillion to spend of general revenues after that to keep the system in balance. That is the whole

question here.

So, if you look at a Social Security plan that Steve Gauss scores and is having a \$7 trillion transition cost, meaning that it would need some form of \$7 trillion say of general revenue transfers, that is \$5 trillion that you are going to spend on the trust fund, plus \$2 trillion more.

It is somewhat like refinancing a house. You pay some money now and you use that to save an awful lot of money later.

MR. STANFORD: I think part of the debate is where are we now and where have we come from in terms fo the way we have used some of the surpluses and the way we have used some of the revenues.

And when I said earlier on, you know, that if we made no changes, the trust fund would be exhausted and we would be able to meet about 72 percent of our obligations. So my sense is that regardless of what figures we use, we really need to start now to look at a base that really is reasonable.

And when we think about the surplus and when we think about the way in which the surplus is being used or are being used, I think we really have to say, whether it is education, whether it is Social Security or some other areas, what is it that the individuals that are concerned really want to use these monies for at this point in time. And

then, what does it mean for the future?

And if we don't have a real base, something to really hang our decisions on, we are going to continue to vacillate. The figures that everybody is using really sound good, sound impressive, but I think we really have to say what is it that we are after in terms of providing a base of support for the American people, period.

CHAIRMAN PARSONS: Mario and Gerry and then Tom.

MR. RODRIGUEZ: Roger, in your written statement you argue, and let me quote you, AWe should not significantly reduce Social Security benefits.@ When you say this, you leave the door open to at least some benefit reductions for at least some retirees.

So, can you please tell me whose Social Security benefits that you would be willing to reduce and how much would you be willing to reduce them by?

MR. HICKEY: No. My goal would be not to reduce Social Security benefits at all. I can imagine some future scenario in which there is a compromise proposal put forward in which some benefits are trimmed somewhat, but I would not be for it.

I can imagine it passing. I can imagine even possibly supporting it. But our goal should not be to lower the Social Security guaranteed benefits, which are low enough, in my mind, already.

MR. RODRIGUEZ: All right. Well, that still doesn't really answer what I am getting at. I mean, you are saying you are going to -- you are saying that we should not significantly reduce Social Security benefits, but tell me you are going to reduce them.

MR. HICKEY: And as I tell you, I can imagine a scenario where in which we do slightly trim some Social Security benefits, but that should not be our goal. And I ask you, when you do your work, to be clear on what kinds of benefit reductions your Social Security privatization plan will entail, because, as you know, shifting revenue from going to those benefits to paying for these private accounts will likely entail significant benefit reductions.

CHAIRMAN PARSONS: Gerry and Tom.

MR. PARSKY: I will try to be brief and not repeat. First of all, I want to thank you all very much for the detailed presentation you have made, which I have listened to and will read again with int.

I come away from this panel with a couple of concepts. One is that at kind of one end of the panel we ought to focus just on the personal account issue and not get deranged, if you will, or off into some of these other fiscal responsibility issues. Let's put it that way.

CHAIRMAN PARSONS: Further deranged.

MR. PARSKY: Further deranged. So I will take away

from this panel an idea of staying focused on personal accounts.

On the other hand, I also come away from this panel thinking that we should not focus on personal accounts at all, and we should deal with other proposals. Now, the only thing that concerned me about that request -- you seem to focus on Henry Aaron's proposal on one that we should, in turn, focus on, and I think as part of our deliberations we will.

However, you indicated that you do not want the retirement age increased, which Aaron does suggest. You have indicated that you do not want, as a goal, benefit cuts, which Aaron suggests will happen. And I think you would support some form of tax increases, which I gather Aaron's proposal would do.

So there is an element of that that I think you probably would concur with, but at least my reading of that would be that if we were going to look at the Aaron type proposal, then we would have to be considering benefit cuts, tax increases and moving the retirement age, which is something that we might want to consider.

I am not quite sure that you would garner a lot of support around this panel for those ideas.

The only other thing I would say is that I think of the five or six personal account proposals that are before

the Congress or that have been submitted to the Congress -- five of them didn't raise the retirement age at all. So perhaps we ought to add those proposals to what we ought to be broadly considering.

A final -- and this is really kind of just a question. In your proposal, in addition to reversing the tax cut for whatever reason -- I think I have got it focused now.

But in addition to reversing the tax cut, you would favor lifting the cap on levels of income.

Just so I get, your three colleagues, would you favor that?

MR. FERRARA: Well, no. If you raise the cap, in fact, on the taxable wage base, that only has a short-term effect, because over the long run -- see, you pay benefits on the income that is taxed.

So if you tax \$1 million, then \$1 million goes into the benefit base and you will be paying God knows what benefits to that person when he retires.

MR. PARSKY: Just a yes or no. Yes or no?

MR. JOHN: Oh, dear. Absolutely not, as I said in my comments.

MR. PARSKY: All right. Yes or no?

MR. STANFORD: Yes.

MR. PARSKY: Yes. Okay. Two on that subject is worth thinking about. Thank you all very much.

MR. JOHN: May I say one thing quickly, because I don't want to leave you with the wrong impression here?

We would be rather distressed if you only concentrated on the personal retirement account; that when it comes right down to it, you are creating an investment -- if you do an option with PRAs, you are creating an investment plan for Americans, and it needs to be able to answer all the questions, including what does your Part A and your Part benefit -- what will those be?

If you don't address all of those, you are going to have something like my colleagues on either side attacking your plan as being irresponsible.

CHAIRMAN PARSONS: Tom and then Lee, and then we are going to wrap it up. Oh. Tom, Lee, John and then we are going to wrap it up.

DR. SAVING: I get to say something. Two questions. One of them at Peter, because you had suggested that we capture the surpluses that are -- and these are the general on budget surpluses. And let's assume, for the sake of argument, the economy recovers and for the next decade we are going to have the projected surpluses.

How would you capture those for Social Security? I mean, how would we -- what is the mechanism which would allow us to actually capture? Since we haven't been able to actually capture any surpluses before, how would we capture

these?

MR. FERRARA: Okay. I have in the testimony a very specific proposal to do that. Just as historically, when they used to take the surplus out of Social Security and give to the government, the government used to spend it and they used to give a bond back to Social Security. And now we take the surplus out of Social Security, as Mr. Vargas said, and they use it to pay down government debt and give a bond back to Social Security.

What I suggest is that any time funds go into personal accounts from Social Security, Social Security be given back a bond. That bond is a claim on the general budget surplus.

It limits the Social Security claim on general revenues, but gives them a claim on general revenues to help to finance the transition. If you do that, then the personal accounts will not accelerate the data when the trust fund runs out, as so many critics have said and all of these other folks.

DR. SAVING: All right. That answers that question. Roger, I have got two kinds of questions for you.

One of them involves Hank Aaron's proposal. And I don't want you to feel like you have to answer for Hank, because he is perfectly capable of taking care of himself.

But if you -- part of his proposal is investing the

surpluses in a way equities, and evidently, you believe that that doesn't worsen the situation. But if you took that same investment in private accounts, the same thing and invested in equities -- it is just now private accounts that are going to offset some Social Security -- why does that worsen the situation when actually taking the surpluses and putting it into a general account that is commonly owned doesn't worsen the situation? I am trying to understand the difference.

MR. HICKEY: If I understand your question, the distinction is that we are simply -- the Aaron proposal is simply talking about taking in the available surplus and --

DR. SAVING: I am just saying take the available surplus and put it in private accounts.

MR. HICKEY: Whereas most private account proposals would simply determine a certain proportionate or certain percentage of the payroll and capture those taxes in --

DR. SAVING: I understand. My question had nothing to do with that. I suggest that this isn't about private accounts in particular. It is about a particular way of organizing them. Okay.

MR. HICKEY: Yes.

DR. SAVING: The second question I have, because you also mentioned Peter Diamond when you said these are certain proposals that were excellent proposals -- and I know Peter's idea is that there is not much of a problem here,

that we could simply tinker with the system; continue to tinker with the system, and he refers to the 1983 huge change in taxes and benefit cuts as a tinkering in the system.

And I am just wondering. Do you think that it is the kind of tinkering that -- is that a tinkering with the system or is that a significant change that happened in >83?

MR. HICKEY: I think most Americans supported that change.

DR. SAVING: That is -- my question was whether or not ---

MR. HICKEY: I did too.

DR. SAVING: The question was is that just a small tinkering with the system? Or do you think that was a major kind fo a change? Otherwise Peter is thinking about another major tinkering I guess.

He calls a tinkering a significant titanic running into the iceberg or something. And so, is it all under a definition of a tinkering or do you think that really was a tinkering?

MR. HICKEY: Listen, I would think that if we had this -- to deal with the entire unfunded liability with tax increases, it would be preferable to private accounts. I think that there are different ways to deal with that gap besides across the board increases, but --

DR. SAVING: Do you think tinkering is going to do

it?

MR. HICKEY: I think a little bit of this and a little bit of that will --

DR. SAVING: Is 1983 a little bit of this and a little bit of that? Is that what how you refer to a little bit?

MR. HICKEY: I think it was an appropriate change.

DR. SAVING: I didn't say it was appropriate. I asked you is that a little bit of this and a little bit of that.

MR. HICKEY: Yes.

DR. SAVING: Oh, it is. That size tax increase that we had in >83 is a little bit of tax increase. Okay.

MR. HICKEY: And supported by most of the American public.

DR. SAVING: Okay. Thank you.

CHAIRMAN PARSONS: Lee, John and then we are going to wrap up.

MS. ABDNOR: I just have a quick question. And for clarification, Roger -- and I hope you don't feel picked on, but I haven't talked to you in a long time.

MR. HICKEY: Not at all.

MS. ABDNOR: But just real quickly. In your statement you said that our mandate, as given to us by the President is, in other words, to privatize Social Security?

MR. HICKEY: That is the way I understood it.

MS. ABDNOR: My question is does that mean that a total -- does privatization mean that the President wants to dismantle, completely dismantle the program? Is that your understanding?

MR. HICKEY: No. I think I have specified that he has mandated you to partially privatize the system.

MS. ABDNOR: But not dismantle the system.
Correct?

MR. HICKEY: I don't think the President intends to dismantle the system. No.

MS. ABDNOR: I'm sorry?

MR. HICKEY: I don't think the President intends -- thinks that he is giving you a mandate to --

MS. ABDNOR: Okay. And the reason I say that is because a lot of people, when they hear the term privatize, they interpret it as we are going to do away with Social Security and dismantle it all together and replace it with that. I just wanted to be clear what your interpretation of that was. So, thank you.

MR. HICKEY: no. My point that I tried to make in my testimony clearly is that I think when you go down this road, when you pull on the string on part of an integrated system, the whole thing does start to unravel.

Nobody has explained to me how you are going to be

able to maintain survivors benefits, for example, and disability benefits when you are tampering with the retirement benefit, if, in fact, you do that. I do think that there is a danger of going down the road of private accounts, that the whole system starts to unravel and that you have something akin to dismantling of the system.

But I think that you have been asked to look at privatizing a portion of the Social Security system, and I think -- I hope that you will think through the implications of that.

MS. ABDNOR: Absolutely. But if I understand your answer, no, you don't mean to say that you believe the intention of the commission of the President is to completely to dismantle, but it could lead to that?

MR. HICKEY: Yes.

MS. ABDNOR: Okay. Thank you.

CHAIRMAN PARSONS: John.

DR. COGAN: Well, I want to thank you all for coming. Roger, I am not going to pile on. I do just want to respond to your point about personal accounts weakening Social Security.

We have heard a lot of evidence. We have had a lot of testimony, and the evidence is overwhelming to the contrary. I wish you could have been here to listen to the representative from the World Bank.

Twenty-two countries around the world have adopted personal retirement accounts and the vast majority of those systems have improved a lot of retirees. We heard from city workers from San Diego and from Galveston. Personal accounts has improved their retirement years.

We heard last month from representatives from the federal government. The federal government's program that allows individuals to choose personal accounts has improved their system.

Even the study that you cite in your testimony shows that when you combine the benefits of the traditional system with a personal account system, the combined benefits are larger than the benefits that can be afforded under the current system. And so the evidence to me is absolutely overwhelming.

You go to Congress. There has been numerous proposals; bipartisan support. All of them have personal accounts as their essential ingredient, and the Social Security actuaries have priced out many of them. And lock, stock and barrel, they improve Social Security's finances and provide for reasonable returns.

And so my sense is that we are on the right track, and I would hope that you would go back to your people that you represent and share with them some of the evidence that we have heard and see if you can get them to at least take

another look at personal accounts.

I mean, if Sweden can do it, if Mexico can do it, if Chile can do it, certainly we in the United States should be able to talk about is a viable option. Thank you very much.

CHAIRMAN PARSONS: Okay. Well, we have come to the end of a long, but very interesting day. I want to add my personal thanks and collective thanks again to this panel of witnesses for your thoughtful input, your preparation, your willingness to share your views with us.

I want to particularly thank all of those who sat through the day and listened and labored with us. And in particular, to the group from Stanford, Professor Shoven's class. You have had now an opportunity to kind of get a bird's eye view of a problem that some think of as intractable.

What is interesting about this problem is that the facts are not really very much in dispute. There is no one who came before you today that you heard that said the system is fine and is sustainable over the course of the next 75 years, which is the measuring period. Everyone sort of acknowledges that it is going to run out of money at some point in time, and we are going to have decrease benefits or increase taxes.

The so-called guaranteed benefits of Social

Security you have heard are not really guaranteed at all. They are promised, but nobody quite knows how we are going to pay for it going forward.

But what we are wrestling with is how to put that system on a sounder footing, how to put it on a course that will give, particularly people in your generation, more confidence that the promise will be close to a guarantee; that the promise will be kept and that there are revenues and sources of funds that are identifiable reasonably far out that can be earmarked to meet those obligations.

So that is what we are going to be wrestling with. And I would ask you, as you go back to Palo Alto and sort of paddle back up to Stanford, you might, Professor, give them a challenge to help us out, because if one among them can get their mind around this and synthesize all these facts and come up with the ultimate solution, I assure you they will light up the sky and be remembered forever.

So, thank you for your patience. Thank you for your input. We appreciate it all, and you will be hearing more from us as we go forward with additional hearings and with additional deliberations. And hopefully, some time around Thanksgiving or just after we will have some final reports and recommendations to the President.

Now, I should put that in context. What we have been asked to do is we have been asked to sort of reflect on

these problems and come forward with our best thinking on how to solve them. It will then be for the dually elected representatives of the people, namely the President and the Congress, to decide whether and how to move forward on whatever our recommendations are.

But we hope to be in a position to come forward with those recommendations some time after Thanksgiving, and I suspect that will set off a new round of interesting and highly emotional and charged conversations around this, and the debate will continue.

So, thank you again. You have been part of an important process effecting all the people. We appreciate it.

(Applause.)

(Whereupon, at 5:02 p.m., the hearing was concluded.)