"AN AMERICAN MODEL FOR SOCIAL SECURITY REFORM"

Statement By Galveston County Judge Ray Holbrook (ret.)
for the President's Commission to Strengthen Social Security

INTRODUCTION

It is a great honor to submit my statement to President Bush's Commission to Strengthen Social Security. For I am a retired Judge. I know how important the personal testimony of an eyewitness can be. And I want you to know first and foremost that I am not a theorist when it comes to Social Security reform. I am an eyewitness.

I know personal retirement accounts can work. Because I have one.

I know a commission can design a better system. Because I was part of one.

I know it's possible to build public support for bold reform. Because I did it.

I know it's possible to change the heart of a skeptic. Because I was one.

Twenty-one years ago, three Texas counties – Galveston, Brazoria and Matagorda, plus two cities and an appraisal district – developed an alternative to Social Security. Despite initial fear and anxiety, the details were explained and debated and workers approved the plan by a 3 to 1 margin. The results have been extraordinary. Our plan provides better retirement, survivorship and disability benefits than Social Security. Our plan provides a better rate of return – between 7% and 8% per year, compared to less than 2% under the current Social Security system. And our plan uses no stock market investments, only commercial banking products, annuities and bonds that provide guaranteed fixed interest rates and no risk.

With all due respect to the "New Deal," I believe it is time for "A Better Deal." Thus, what I ask the President and the distinguished members of his Commission to consider is not a Chilean model, or a British model, or an Australian model or a Swedish model of Social Security reform, though I'm sure those are all fine as far as they go.

What I ask the President and his Commission to consider is an American Model, a real life American success story found deep in the heart of Texas.

THE BACKGROUND

My story begins back in the late 1970s. Just like today, everybody who paid attention to such issues knew that Social Security was in serious financial trouble. I certainly knew. The economy was bad. Unemployment was high. Inflation was rampant. And serious cracks in the foundation of Social Security were becoming apparent.

In 1960, there were about fifteen workers paying into the Social Security system for every retiree drawing benefits. But by the late 1970s, that ratio was plunging. I believe at the time it was down to about three or four to one. And as you well know, by 2030, the ratio will plunge down to 2 to 1. This is a disaster waiting to happen.

What made these disturbing facts particularly troubling to me way back in the late 1970s was that I was in a position of authority, a position to do something to make retirement better for the county workers under my care.

Perhaps some of you know how county governments in Texas are run. Decisions are made by four county commissioners and a presiding county judge. I was the Galveston County Judge from 1967 until I retired in 1995.

As such, my colleagues and I knew something needed to be done. We knew Social Security's "pay as you go" system wasn't working. We knew bankruptcy was looming. And we faced a choice: we could either keep our people in the existing system with all its imminent tax increases and increased retirement ages and potential benefit cuts, or we could try to come up with a better, safer, more secure system.

Back then, local governments had the option under federal law to withdraw from Social Security and set up their own retirement programs. The Social Security Administration did require, however, a two-year written notification prior to withdrawal. This was all changed with Congress' so-called Social Security "reform" of 1983. Local governments no longer have an opt-out provision. But back then, thank the Lord, we did.

So Galveston County's forward thinking Legal Department Director, the late William D. Decker, submitted a notification letter in January of 1979 and started the two-year waiting period. During this time, the issue was studied very carefully and discussed by the Galveston County Commissioners Court and all the county employees.

<u>THE PLAN</u>

The Court brought in two consultants, Don Kebodeaux, Chairman of First Financial Capital Corporation of Houston, and Rick Gornto, Don's colleague and the President of First Financial. We tasked them to design us an "Alternate Plan" to Social Security, based on several fundamental and non-negotiable principles.

First, the Alternate Plan would have to have the exact same or better benefits – including retirement, survivorship and disability benefits – than Social Security. Under no circumstances were we going to cut corners or cheat workers out of expected benefits. We believed a promise made should be a promise kept and nothing less would do.

Second, there could be no tax increases. The program could not cost the county and its employees more than Social Security. Otherwise, what would be the point?

Third, there could be no risk. Yes, we wanted to consider the increased benefits of higher interest rates and market returns on our retirement savings. We wanted to consider personal retirement accounts that were a form of private property for each worker and whose value could be passed on to family members upon death. And we wanted rock solid private insurance for our workers. But we did not want to put people's money at risk in the stock market. We did not want to be accused of gambling with workers' retirement savings. So we needed a plan that would minimize or eliminate market risk.

Was it even remotely possible to design an Alternate Plan to Social Security that gave workers better benefits, with no tax increases and without risk of losing some or most or all of their hard-earned money? I'll be honest. I didn't think so. I was a skeptic – "big time," as the Vice President might say.

But the plan developed over the course of a year by the experts at First Financial accomplished all three goals. It comprised of a life insurance element for employees, which would protect families of deceased employees. It had a disability insurance element as good as Social Security. It also had a retirement element with annuities purchased from major life insurance companies designed to surpass Social Security's benefits. Indeed, the more I learned about the plan, the more impressed I was.

The true genius of the Alternate Plan was that it was <u>not</u> based on an "Investment Model" of retirement savings. In other words, it did not use – much less rely upon – direct investments in the stock market by way of individual stocks or stock index funds or even mutual funds to grow workers' payroll taxes into a larger pool of retirement savings.

Instead, the Alternate Plan was based on a "Banking Model." The payroll taxes of workers were deposited in personal retirement accounts that then purchased commercial banking and life insurance products already available in the marketplace – like bank CDs (certificates of deposit) and annuities – as well as government and commercial bonds, all with fixed and guaranteed rates of interest. It was this approach that sold my colleagues, and me because it essentially eliminated risk from the program.

<u>**THE RESULTS**</u>

Let me be very clear on this point because I know the Commission is seriously considering an "Investment Model." It was a calculated decision we made not to invest in the stock market even though our retirement income would have been much higher for all our workers. Yes, perhaps we could have averaged 12% to 16% a year or better had we invested all this money in the stock market during the roaring 1980s and 1990s.

But we've done very, very well, without taking such risks. Over the course of the past 21 years, under this "Banking Model," we have averaged between 7% and 8% per year on our personal retirement accounts. That's between two and five times better than what our workers' would have received had we stayed in Social Security, and all the money has been safe and secure.

In my own case, I retired in 1995 and was truly astounded with how well the plan we designed and approved had done for me personally, compared to Social Security. After only 14 years in this Alternate Plan – compared to my 27 previous years in Social Security – my retirement income from the Alternate Plan is fully two-thirds of my Social Security income. Had I retired six years later, so as to be in our Alternate Plan for a full 20 years, my income from the Alternate Plan would have <u>equaled</u> my Social Security income. Had I retired after 30 years in the Alternate Plan, my retirement income from the Alternate Plan would have been double that of Social Security.

Now, I'm not against allowing people to choose some form of conservative investments, such as stock index funds and a range of good, strong mutual funds. And one of our counties is beginning to allow its workers some more freedom, some more options, when it comes to such conservative investments.

But I think that the approach we took 21 years ago was the right approach, financially and politically. Financially, workers had the piece of mind that their money was truly safe, that we were getting guaranteed fixed interest rates that they could "take to the bank," rather than have to live with great anxiety that certain stocks or market sectors would go up and down like a roller coaster. Politically, that made our reforms much, much easier to sell to a curious but skeptical work force.

In addition to getting a great annual rate of return of between 7% and 8%, our disability insurance pays up to 60% of a worker's salary, up to $5,000 a month. And our life insurance program pays three times a worker's annual salary up to $50,000 a year or a total of up to $150,000. These are significantly better benefits than Social Security.

This matters to real people. A county commissioner – a colleague of mine – passed away not long ago. His widow was quite young, about 40. From Social Security, she received a lump sum survivorship benefit of $255. Not per month. Not per year. That was it -- $255. What did she receive from our Alternate Plan? She received a lump sum survivorship benefit of $150,000. Plus, she is entitled to a reserve account of $125,000, available at any time she wants to draw it down. So, from Social Security this widow received $255. From our plan she received more than a quarter of a million dollars.

That's why though I respect the New Deal upon which Social Security was based, I ask the President and the Commission to look seriously and carefully at our approach, because it is truly a better deal for workers and their families.

THE ROAD TO REFORM, AND THE ROAD AHEAD

There was, of course, great skepticism that this Alternate Plan would be successful when it was first developed and debated. I have already told you that I was a big skeptic at first. But I was not alone. There was considerable opposition from labor unions, some minorities and some traditional liberal Democrats, including many Galveston County elected officials, all of whom were Democrats at the time.

So we decided to give the Alternate Plan a proper public hearing and get all the facts on the table. Some of the Commissioners and I participated with representatives of First Financial Capital – the designers of the Plan – in a series of employee meetings. In the end, I believe some sixty such meetings were held in three or four cities to give people a chance to hear the details, ask their questions and raise their concerns. We also asked the Social Security Administration to send representatives to debate the plan with us in the employee meetings, which they did.

An election was called for all county employees for the fall of 1980. Newly and completely sold on the Alternate Plan, my colleagues and I campaigned for its passage. It passed by a 3 to 1 margin. The Galveston Commissioners Court then voted 4 to 1 to implement the Plan on January 1, 1981. Brazoria and Matagorda Counties joined us in 1982. Harris County and some 50 other counties were ready to join but were blocked from doing so by what Congress did in 1983 when they raised taxes, raised the retirement age and closed the door on local governments developing better deals of their own.

As I conclude, let me repeat that our approach to Social Security reform has produced what the American people desire: a better deal. Our workers have true financial security for themselves and their families; wealth-creating private accounts that are their own property; and the opportunity to escape from poverty, especially for women and minorities. This is not a theory. We have a real model – an American Model – that the President and his Commission could readily adapt for use on the national stage.

I know there are Doubting Thomases out there. That's OK. Come on down to Texas. See for yourself. We'd be glad to have you. We'd be glad to answer your questions, calm your fears. But to all you critics who've got nothing but bad things to say about a good old fashioned American success story, I say: Don't mess with Texas!

Just listen to the story of Jane Breslin. Jane was a county clerk assistant. In 1980 she was deeply opposed to the Alternate Plan. One steamy Friday at an employee meeting, she stood up and began weeping. She begged us not to proceed.. Everyone felt for her. Understandably, she was anxious about her future. What if our Plan didn't work? What if she was left with nothing? Well, not long ago, Jane Breslin retired. Indeed, she retired better than she would have under Social Security. She says so herself. Indeed, every now and then I see her on TV or hear her on a radio show praising the Alternate Plan and explaining how grateful she is that it passed and she participated in it. Because it truly is "A Better Deal."

It is my fondest hope that we have created a model the rest of the country can benefit from as well.

Thank you very much.