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NATIONAL COMMISSION ON SOCIAL SECURITY REFORM RECOMMENDATIONS

HEARING

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY AND INCOME MAINTENANCE PROGRAMS

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

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NATIONAL COMMISSION ON SOCIAL SECURITY REFORM RECOMMENDATIONS

TUESDAY, FEBRUARY 15, 1983

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 1:44 p.m., in room SD-215, Dirksen Senate Office Building, Hon. Robert J. Dole (chairman) presiding.

Present: Senators Dole, Danforth, Chafee, Heinz, Wallop, Armstrong, Grassley, Long, Matsunaga, Baucus, Boren, Bradley, Mitchell, and Pryor.

[The committee press release announcing the hearing and the prepared statements of Senators Dole, Heinz, and Wallop follow:]

[Press Release No. 83-103]

FINANCE COMMITTEE SETS HEARINGS ON NATIONAL COMMISSION ON SOCIAL SECURITY REFORM RECOMMENDATIONS

Senator Robert J. Dole, Chairman of the Senate Finance Committee, announced today that the Committee has scheduled hearings on the recommendations of the National Commission on Social Security Reform for February 15, 22, 23 and 24, 1983. Social Security Commission Chairman, Dr. Alan Greespan will testify on February 15, 1983, followed by public witnesses on February 22, 23 and 24, 1983.

The hearings will begin at 1:00 p.m. on February 15 and at 10:00 a.m. on February 22, 23, and 24 in Room SD-215 (formerly Room 2221) of the Dirksen Senate Office Building.

In announcing the hearing, Senator Dole noted "the National Commission on Social Security Reform, through difficult deliberations of over one year, has developed a bi-partisan package of recommendations for reform of the Social Security program. These reforms, if adopted by the Congress, could lead to both short- and long-term solvency for the system. The hearings will be comprehensive and we hope to hear from all interested public parties and from the Administration.

"With the expiration of interfund borrowing, the Finance Committee will want to be prepared to move quickly on the reform proposal. We face a July 1 deadline for taking action to continue benefit payments. Additionally, the implementation of certain proposals will require early passage," Senator Dole said.

OPENING STATEMENT OF SENATOR DOLE, SOCIAL SECURITY HEARINGS, FEBRUARY 15, 1983

On behalf of the Finance Committee. I am pleased to welcome the members of the National Commission on Social Security Reform. I know I speak for Senators Armstrong. Heinz, and Moynihan, who also served on the Commission, when I say that it has been both a pleasure and an honor to work with this distinguished group of public servants. Reaching a consensus on social security reform would have been impossible had it not been for the diligence and the spirit of cooperation shown by each members of the National Commission. I would like to point out at the start that Robert Beck and Lane Kirkland are unavoidably absent due to conflicts in their schedules.

As my colleagues well know, just a year ago, prospects for a bipartisan consensus were remote. The social security program had been mired in political controversy for nearly a year when the National Commission was created. The system moved closer to insolvency as proposals for financial reform were subjected to partisan political attack. As a group with widely divergent views, we probably seemed incapable of reaching any true bipartisan consensus.

Yet on January 15, with the cooperation and approval of President Reagan and House Speaker O'Neill, the National Commission issued a consensus reform package with broad bipartisan support. As is clear from the 12 members who support the package, both political parties were represented in our negotiations as were the interests of the elderly, organized labor, and general taxpayers.

The package will require concessions from all of the parties who have a stake in social security—current and future beneficiaries, taxpayers, and government employees who do not now contribute to the system. Not surprisingly, therefore, no one is happy with each and every specific recommendation. The important fact, however, is that agreement was reached on the essential provisions of a social security solution.

On January 26, Commission members Moynihan and Heinz joined me and eight other Senators in introducing S. 1. The bill is intended to mirror the recommendations of the Commission and, as such, leaves unresolved a number of legislative decisions. Among other things, we will want to consider ways to eliminate the notch created by the provision to tax benefits; options for minimizing the impact of the COLA delay on low-income recipients who are also on SSI; and the merits of offsetting the self-employed tax increase with a tax credit or deduction. In the course of the next 5 days of hearings, we are likely to learn of additional areas requiring refinement or clarification.

As I am sure we will hear today, members of the National Commission recognize that many details remain to be worked out within the legislative process. To the greatest extent possible, however, the Commission's recommendations will have to be considered as a package. The final product carefully balanced many interests. An unraveling of any single provision would clearly jeopardize the entire package.

We have a big job ahead of us in Congress. We face many difficult decisions as to the details of the legislation, and in light of the preliminary excerpts from the 1983 Board of Trustees report, we will have to carefully consider the adequacy of the measures proposed. Needless to say, we in the Commission fashioned our consensus recommendation on the basis of the best and most up-to-date information we had available. I feel confident that we can tailor the package to meet greater financial needs if that should become necessary.

The balance of the long-term deficit also remains to be addressed. In my view, a balanced solution to this problem will involve bringing the cost of social security into line with the ability of our working population to finance the system. The tax burden is already heavy, and the confidence of young people critically low.

The American people—the 36 million people receiving benefits as well as the 116 million working people who support the system—deserve the speedy consideration of this bipartisan package of recommendations. Confidence in the long-term viability of social security will be restored only by enacting measures that put the system on a sound financial footing and do so without imposing an unrealistic tax burdens on present and future workers.

Once again, I welcome my colleagues on the National Commission. I look forward to hearing your testimony.

Opening Statement by Senator John Heinz, Senate Finance Committee, February 15, 1983

As a member of this Committee who had the distinct privilege of serving on the National Commission on Social Security Reform I believe the package of recommendations we came up with is entirely fair and reasonable. There are, of course, individual elements of the package which are unattractive by themselves. Indeed, any proposal in this package, or, for that matter, any single proposal of social security, taken by itself, would be unlikely to receive support from a majority of Members in either the House or the Senate. However, taken together the proposals in this package fairly balance the burdens of financing social security to assure solvency in the coming decades.

It is this balance which has been so important in gaining the support of the President, the Speaker, and the Senate Majority Leader, and will, I believe, be key to the success of a social security financing package in the Congress. Ultimately, there is no painless solution to social security's financing problems. But the Commission's recommended package spreads the pain that there is as evenly as possible. About a third of the $168 billion in new financing would affect employers and workers, another third would affect other accounts in the budget, and a third would affect beneficiaries. Because the financial burdens are broadly shared, they are minimal for any particular group of individuals.

In addition, the timing and sequence for implementing the various proposals in the package is designed to cushion their impact. The substantial immediate financing need in social security would be met primarily through transfers from other accounts in the budget. A transfer of $18 billion from the general fund in the first year would provide over 80 percent of the financing needed initially, and would avoid having to resort to immediate benefit cuts or increased payroll tax rates. For the next 4 years, intra-budget transfers would play a minor role, while significant payroll tax increases would be postponed until 1988 and 1989 to mitigate any adverse consequences for economic recovery. As a result, between 1984 and 1987, changes affecting beneficiaries, then beginning to take effect, would supply half of the financing during this period. Finally, the acceleration of the 1990 tax rate in 1988 and 1989 would provide half of the revenues needed at the end of the 7 years. The sequencing of the National Commission's recommended proposals makes it possible to provide sufficient financing for social security in the early years without drastic or immediate changes in the structure of the system.

EMPLOYERS AND WORKERS

Some groups have expressed concern that the tax burden from this package would be excessive. Yet over the 7-year period, only 32 percent of the financing of this package would affect workers and employers. Furthermore, these proposals would not increase social security tax rates beyond those already scheduled in the law. The schedule that exists for rate increases would be stepped up, however, and the rate for the self-employed would be set equal to the combined employer-employee rate. In the first 5 years, the effects of these changes would be relatively small—producing only 14 percent of the total financing in the package during this period. Three-quarters of the net new tax payments would be made in 1988 and 1989. Even the 1988-89 acceleration would only raise rates for those years by 0.36 percent each on employer and employee, for a net increase of about 4 or 5 cents per hour per job. Of the total financing in the 7-year package, only 12 percent would come from net additional taxes on employers and only 9 percent from employees.

The self-employed, who have been paying three-quarters of the combined employer-employee rate because they cannot deduct the tax as a business expense, would have this situation reversed. The self-employment tax rate would rise by 3.35 percent in 1984, but half of all OASDI taxes would be deductible. Because the tax deduction would only offset the added social security tax for those at a 50 percent marginal tax bracket, most of the self-employed would have a net tax increase. For the average self-employed individual the net increase would amount to about $5.80 per week.

In addition, some employees of nonprofit organizations would join social security. Over 4 million nonprofit employees, 85 percent of all nonprofit employees are already covered, and nothing would change for them. Only 15 percent of the nonprofit employees would pay new taxes. For many, these added taxes would be partially offset by a reduction in payments to alternative pension and insurance plans.

INTRABUDGET TRANSFERS AND FEDERAL EMPLOYEES

Other concerns have been voiced that this package relies too heavily on transfers within the budget and does not do enough to reduce budget deficits. In fact, the smallest portion of the total financing would be provided through changes that will only affect accounts within the budget. Intrabudget transfers and coverage of new Federal employees will account for only 30 percent of the financing in the package and about 3 percent of revenues from all sources that social security will receive during this 7-year period. About half of this amount is realized almost immediately so that neither outright benefit cuts nor new payroll tax increases will be necessary.

The largest single transfer is an immediate, one-time $18 billion payment to compensate for inadequate social security tax contributions for military personnel in the past. In later years, the largest effects on other budget accounts will come from reduced tax revenues due to the tax deduction for the self-employed and the 1984 tax credit.

New Federal employees hired after the end of 1983 would pay into and be covered under social security, rather than make contributions to the civil service retirement fund. This proposal would not increase contributions for new employees. Nor would it necessarily affect the earnings replacement provided through their pension benefits, since they would be offered a largely employer-financed supplemental retirement plan. It is important to note that this change would be beneficial to those Federal employees who work only partial careers in Federal service, since it will provide them with fully portable social security credits for that service. Under the current system, half of the Federal workers who leave the Government before retiring receive no Federal pension benefits. There has been some concern on the part of Federal employees that this proposal would jeopardize the financing of the current retirement system, because it would raise the cost to the taxpayer of retirement programs for Federal employees. In fact, coverage under social security would almost certainly reduce the annual budget cost of Federal retirement, quite simply because Federal employees hired after this year would work an average of three years longer before drawing retirement benefits. Today the average retirement age is 64 for a social security retiree compared to 61 for a Federal employee.

BENEFICIARIES

Finally, some groups have expressed concern that the financing package would place a disproportionate burden on beneficiaries. In fact, 38 percent of the total financing package comes from provisions affecting beneficiaries—much of it affecting only the wealthiest beneficiaries. There is no doubt that these changes will make it somewhat more difficult for many retired persons to maintain their living standards, but taken in the context of the other financing measures, they are fair and modest. The 6-month COLA delay would pay the scheduled July 1983 benefit increase in January 1984. As a result, an average retired beneficiary receiving $416 a month in benefits would still receive the full $22 per month increase, but it would come 6 months late. Two million of the poorest social security beneficiaries would be fully compensated for and protected against the 6-month delay through an adjustment in their monthly SSI payment amount.

The wealthiest 10 percent of the social security beneficiaries will also begin paying income taxes on the half of their benefits related to tax-free contributions of their employers. Under the Commission's proposal, people receiving social security benefits with additional income in excess of $20,000 (single) and $25,000 (joint) would begin in 1984 adding half of their social security benefit to taxable income. A single elderly taxpayer with an adjusted gross income of $30,000 and $6,000 in social security benefits would pay less than 2 percent of his or her income in additional income taxes between 1983 and 1984. These changes would still leave the relatively wealthy elderly with more favorable tax treatment than the nonelderly. A nonelderly taxpayer with the same gross income and deductions as this elderly individual would pay $1,029 more in income taxes in 1984, in addition to the social security and other payroll taxes he pays that the retired person does not.

In short, the social security proposals recommended by the Commission would affect a broad range of individuals, but should place an undue burden on none. This is a package that carefully balances the concerns of workers and beneficiaries and the interests of the various groups involved. Most importantly, it is a package that will restore solvency to social security for several decades.

REMAINING CONCERNS

That is not to say that this is a technically perfect package. Clearly, there are a number of areas in which this Committee and the Senate House Ways and Means Committee will be modifying and improving the package. I would like to discuss briefly four areas about which I have concerns.

First, while the Commission recommended the entire long run financing shortfall equal to 1.8 percent of taxable payroll be eliminated, there was consensus among the members on changes to eliminate only two-thirds of the shortfall. I believe we must fully resolve the long-run financial problem in order to restore public confidence in social security. Within reason how this is done is not nearly as important as that it be done. I have supported, in the Commission, a gradual increase in the retirement age to age 66 by 2015, with further increases in the future to maintain a constant ratio between years or work and years of retirement. This is conditioned on the premise stipulated in the recommendation that it be coupled with improvement in the disability insurance program to meet the special needs of those precluded by poor health from working longer. This gradual change should complement the effort we as a nation should make to expand employment opportunities for older workers.

A second concern I have is that in delaying the social security COLA to January, we not unintentionally reduce the incomes of those on social security or SSI. I raise this point because the Commission recommendations left unsettled the question of how to schedule the SSI COLA or the SMI premium increase. With regard to SSI, the COLA in that program is currently tied to the social security COLA. The SSI COLA will be delayed along with the social security COLA unless it is explicity "uncoupled". If it is delayed, the increase recommended by the Commission in the disregard for social security income will only protect 2 million SSI beneficiaries. Whatever is done, an effort should be made to maintain the real value of the SSI benefit for the 4 million elderly and disabled who depend on this program. In addition, a supplementary medical insurance (SMI or Medicare Part B) premium increase is scheduled for July. The effect of this increase combined with a six month delay in the social security COLA could be to actually reduce the monthly incomes of some elderly beneficiaries. It is important that the SMI premium increase be delayed to avoid this unintentional effect. While these issues are not strictly social security financing concerns, they will inevitably be addressed, either directly or indirectly, in the financing legislation.

A third concern I have is that the tax deduction for the self-employed will only afford full protection to those self-employed with the highest incomes. Those with low incomes will bear nearly the full burden of the increased self-employment tax. While it may be necessary for the self-employment tax. While it may be necessary for the self-employed as a group to pay more in net taxes, it is important that the burden be distributed as equitably as possible among them.

Fourth, the Commission proposal to tax social security benefits would result in a undesirable "notch", as the Commission indicated in its recommendations. An individual whose adjusted gross income is $1 above the $20,000/$25,000 cutoff would pay tax on half of his social security benefit, while an individual with an income a dollar below the cutoff would pay no tax on his benefits. This inequity can be easily corrected, for example, by taxing the individual on the amount by which half his benefits take him over the cutoff when added to his adjusted gross income.

These are only relatively technical problems, and in no way detract from the overall fairness of the total package.

I believe that the Commission's recommendations overall provide an excellent foundation for an early legislative remedy to social security's urgent financing problems. The package of proposals recommended by the Commission is an equitable, comprehensive, and realistic means available to the Congress to restore social security to financial health. And, we in the congress have no more important responsibility than to restore the public's confidence in our most successful and most important social program.

Social security proposals a balanced package

	Billion
Workers and employers:	
Payroll tax increase	$40
Tax credit payments	−4
Self-employed tax increase	18
Tax adjustment from deduction	−12
Coverage of non-profit/Prevention of State and local termination	11
Increased payroll tax	69
Reduced income tax	−16
Net (31.5 percent)	53
Beneficiaries:	
6-month COLA delay	40
Increased payments from SSI	−5
Women's equity	−1
Taxing benefits	30
Decreased income	70
Increased SSI and women's equity	−6
Net (38.1 percent)	64
Federal employees and intrabudget transfers:	
Coverage of New Federal employees	12
Military service credits	18
SSI payments to beneficiaries (see above)	5

Income tax adjustments to workers (see above)	16
Total (31.4 percent)	51

DISTRIBUTION OF SOCIAL SECURITY SOLVENCY COSTS BY CATEGORY AND YEAR

[Calendar years in billions of dollars]

	1983	1984	1985	1986	1987	1988	1989	Total
Employer/employees		5	2	2	4	19	21	53
Beneficiaries	4	5	8	10	11	12	13	64
Intrabudget Transfers	21	5	3	5	5	6	6	51
Totals	25	16	13	17	20	37	41	168

Note: Some totals may not equal the sum of individual items due to roundings.

FINANCE COMMITTEE STATEMENT BY SENATOR MALCOLM WALLOP ON SOCIAL SECURITY

Mr. Chairman, When President Carter signed the 1977 Social Security Financing Amendments, he declared, ". . . from 1980 to 2030 the social security system will be sound." Yet, this summer, the social security retirement fund will be depleted to a point where the program will not be able to issue monthly benefit checks. This is not 2031, this is 1983. Obviously, something has gone wrong.

Six years ago, the Congress passed a bill to rescue social security. The rescue operation relied on the largest tax increase in our history. It also involved correcting mistakes made in 1972 when automatic indexing of benefits was adopted. In 1977, we chose the easy course. We avoided correcting structural problems. Instead, we placed the burden for social security solvency on the future. We gambled that productivity would flourish, that real output would increase at historic levels. Inflation would run at only 4 percent annually. Real wages would grow by almost 2 percent annually. We would have full employment. As one writer has stated we were relying on utter fantasy. I decided to vote against the bill when I realized that the package merely pushed the problem off until tomorrow. It was a tomorrow that many hoped would never come, yet now it is here.

The problem facing social security is well known. By the end of the decade, the social security program will have a deficit of $150 to $200 billion. The 1977 bailout has failed simply because the unrealistic economic growth necessary to save the program has not occurred. Productivity actually dropped since 1977, and increased by only about seven-tenths of 1 percent in 1982. Inflation since 1977 has been explosive. The rate reached double digits by 1980, and has been close to the projected annual rate of 4 percent only in 1982. Full employment has been as elusive as finding the Holy Grail. Proponents of the 1977 legislation gambled that prosperity would finance social security solvency. It was a poor bet.

In addition to optimistic prosperity, there was a dependence on long-term population growth. There would be an influx of new workers to bear the payroll tax burden in the next century. The baby boom generation will eventually retire. They will place a great demand on social security. Since the program is a pay-as-you-go system, many new workers will be necessary to provide the income transfers to fund the baby boom's retirement benefits. To date, this second baby boom has not happened. A substantial deficit in social security looms over the long run.

Spending on social security amounts to one-fourth of the Federal budget. Any shortfall in social security frustrates our efforts to balance the Federal budget. The Federal budget should not be balanced by creating huge reserves in social security. But, we cannot allow social security to run a deficit, small or huge, over the next few years. To do so would lead to the type of economic chaos that lead to the creation of the social security program back in 1935.

We have heard a lot about structural deficits lately—deficits that will remain once we achieve full employment. Even Lord Keynes would not condone such an achievement. The structural deficits result from three factors—in the cost of rearming America, the cost of our national debt (we will expend $75.5 billion in 1973 just on interest), and the cost of entitlement programs. These three factors account for Eighty Percent of the budget.

Most entitlement spending is for work-related benefits. Social Security, including medicare and medicaid, represents 60 percent of all entitlement spending. The program will account for 75 percent of entitlements by 1988. The growth in needs-tested entitlements has stopped. But, work-related benefits will increase by 73 percent between 1980 and 1985.

As work-related entitlements, our income transfer programs, absorb more and more of our gross national products, we accelerate the paralysis of productive activity. We are hindered in our ability to raise the standard of living for everyone. As Government-financed debt expands, we extinguish private savings. Such savings are vital to providing the new tools and new products to reindustrialize our economy.

I do not always agree with Alice Rivlin, but I think she hit the nail on the head when she recently observed, while discussing the budget deficit, that the sooner we address the problem, the more easily we can make the gradual adjustments to correct it.

The longer we postpone action, the more abrupt, and disruptive, will be the adjustments. We can no longer avoid making choices.

The most encouraging sign that we can sensibly control Federal spending is the recommendations of the Commission on Social Security Reform. There are few observers of political life who believe that the proposals from any commission would ever become law. Establishing a commission is a wornout device for avoiding decisions. The Commission on Social Security Reform may be the exception. It has worked only because the Commission included our colleagues who take the most active interest in social security.

The reform package has been ably described by other members. There are aspects I do not like. Moving up the scheduled payroll tax increases is a burden on economic recovery. Increasing the tax on the self-employed is a blow to small business. But, there are components I strongly endorse. The proposal makes structural adjustments in benefits which will ensure that social security in the future will not increase faster than economic growth. I think we can do more in this area, and will propose legislation to more sensibly calculate benefits after we finish with this reform package.

I agree with Congressman Conable that the package is unsatisfactory to everyone, but superior to other alternatives. The proposal does not reduce current benefits, it does not raid general revenues, but it does keep the program solvent.

The package does not solve all the long-range problems. For this reason, I have joined in cosponsoring S. 76, which provides for a gradual increase in the retirement age in the next century. This route is far preferable to an increase in the payroll tax, one suggested alternative. Today, I want to ask Chairman Dole to add me as a cosponsor of S. 1. I hope we can move quickly on this legislation.

The CHAIRMAN. On behalf of the Finance Committee, I am certainly pleased to welcome members of the National Commission on Social Security Reform. I know that I speak for Senator Armstrong, Senator Heinz, and Senator Moynihan, who also had the privilege of serving on the Commission, when I say that we appreciate very much your efforts. I think those in the private sector contributed a great deal more than those of us who happen to be Members of Congress, because you were able to be perhaps more objective in the pursuit of the compromise. We appreciate the fact—most of us do—that a consensus was reached. To me, it can set the stage for a number of cooperative efforts in the Congress this year.

I think very honestly the reason we are having negotiating now on a jobs bill is because first of all we had a compromise on social security. There are indications that this will set the stage for further compromises between the President and the Congress on critical issues.

Now, as I understand, Dr. Greenspan will be the first witness. We would also like to hear from and address questions to each member of the Commission.

We know that there are some on the committee who have different views, and we certainly want everyone to have a chance to be heard. We know that there is some little opposition to the package.

As I said, I think it's strength is probably its weakness. This will probably be revealed as we get into the hearings.

Are there other members who would like to make brief statements before we hear the witnesses?

Senator CHAFEE. Mr. Chairman, I would just like to say that we all share a deep appreciation for the time and energy and constructive effort that the members of the Commission put into this report.

As one member of this committee I am deeply concerned over whether the proposed solution really solves the problem, and of course we will get into that in Mr. Greenspan's presentation and the others'. But we have now been through two crises in this situation—the social security—in the 7 short years that I have been here; in 1977 we had it, and of course in this year, in 1982 and now 1983.

It seems to me when we get to these crisis situations the answer always is, basically, to increase the taxes, since any change in benefits must require a long-time phase-in in order to avoid unacceptable dislocations or disruptions in the planning of those who are counting on certain benefits at a certain time.

My only hope, Mr. Chairman, is that whatever we do—not just in dealing with this report but in making modifications, should they be necessary—that whatever we do be a truly long-term solution so that we can take care of this problem for the foreseeable future, whatever that is, maybe up to the year 2020.

That is my hope, Mr. Chairman. Thank you.

The CHAIRMAN. Thank you, Senator Chafee.

Senator Heinz.

Senator HEINZ. Just briefly, Mr. Chairman.

First, I have some remarks I would like to put in the record.

Second, I would like to commend Alan Greenspan and you and my former colleagues with whom we spent so many long hours and had so many meals.

Third, I would just like to say that I think all of us are aware that what we have proposed as a Commission both on the short term and on the long term, where for a portion of the long term there is an agreement to disagree, is going to receive a lot of criticism from any of the affected parties. Because the proposal is balanced and in that sense very fair indeed, it affects a lot of parties.

I would hope that those who don't like the fact that there are adjustments to the growth of benefits, that there are increases in taxes on employees and employers, that there are methods of recapturing social security benefits through the taxation of high-income benefits, or that we are including Federal employees, new ones in the system would understand that for us to change the package would necessitate a heavier burden being placed on some other group.

The only other comment I would make, Mr. Chairman, is that I have detected some comment—not on the Senate side, so far—that if the missing element of the package, which is the one-third of the long-term 1.82 percent which has not been resolved by consensus of the Commission, comes to the floor of the other body, or for that matter this body, with a solution that even though it may be the will of the Congress is unacceptable that that should cause the entire package—short term and long term—to fall. I caution any of my colleagues in the House and Senate against taking such a self-defeating point of view.

None of us went in as members of the Commission with any bottom line, with any preconditions. We had our prejudices, certainly. We had our favorites, certainly. But for anybody to say that if the Congress works its will on the last 10 or 15 percent of the total package involving the long term, and it's not exactly what they want for that it violates some new rule, I think that would be not only dangerous but highly irresponsible. It might carry with it the consequence of some kind of stalemate on this package, and that indeed would be the ultimate jeopardy of the senior citizens who depend—some 39 million of them—on this package.

The CHAIRMAN. Senator Wallop.

Senator WALLOP. Thank you, Mr. Chairman.

Let me add my congratulations and appreciation to all of you for the work that you put in and the product that you came up with.

I agree, I think, with Congressman Conable who said, "The package is unsatisfactory to everyone, but superior to any other that was around." And surely that has to be the case.

This whole business is sort of the search for the Holy Grail, and King Arthur's roundtable knew nothing of the problems of trying to solve social security, when everybody's emotion gets attached to every single element of any solutions.

There would, if I were king, be many things I would do differently, and I suspect the same thing is true with each member of the Commission, both political and from the public. But we have to do something.

I think it is clear and it ought to be clear that the most irresponsible thing that any member of any party could do now would be to duck the issue and let it go away unresolved, even assuming that the resolution is not perfection and that further things have to be done in the decade or more.

It seems to me that the longer we postpone any action now, the more critical and the more disruptive and more painful any actions we take ultimately are going to be. Each day that we put it off the wrench that ultimately has to come is going to be worse.

So I hope that we can get on with this. I hope that there is a little sense of the lemming, that maybe if we perhaps join arms together and all march over the cliff or into the ocean, or whatever is necessary, but to take the political heat, to show a little leadership, but to resolve some of the insecurity in the country's financial markets and other things.

Mr. Chairman, with that in mind and recognizing that if I were king there would be some differences in it, I would nonetheless ask you to put me on as a cosponsor of S. 1.

The CHAIRMAN. I appreciate that.

Senator WALLOP. I ask that my full statement be included in the record.

The CHAIRMAN. Thank you. It will be included.

Senator Grassley.

Senator GRASSLEY. Even though the members of this committee tell you we appreciate what you have done in reaching this point where 12 out of 15 Commission members can support this compromise package—I'm sure that we really aren't going to appreciate what you have gone through until we have gone through it ourselves, and that process is just now starting.

So I do want to express my appreciation, but I think I am going to appreciate your efforts much more 6 weeks from now.

Having said that, I do have some reservations about the package. I think the Commission's report is too long on taxes and too short on reform, and I say that from my experience in the House of Representatives in 1977.

We cannot solve social security's financing problems by relying predominately on tax increases. The Social Security Amendments of 1977 and the fact that we are here today serve witness to the fallacy of that course of action.

The inherent problem of the current social security system is not going to vanish with repeated reliance on revenue infusions to shore up the trust funds. We clearly can't afford to make those past mistakes of thinking we have solved the funding problem when in fact we have merely increased the burden on small businesses and on the hard-working taxpayers. I recall all too well from previous debates the statements in 1977 lauding that reform measure. Such memories are the basis for my caution as I evaluate this latest solution to social security's funding shortfall. I voted against those tax increases in 1977, but I am hopeful that this go-around we will have the courage to more completely address social security's ailments.

Today and throughout these hearings I intend to look at all options for returning solvency to the system, but my bottom line is always going to be a commitment, as other members have expressed, to maintaining the economic security of current and future retirees.

Probably the thing that bothers me the most is that this package is two-thirds of a loaf. Now, we've always said in legislation "half a loaf is better than none," and I suppose two-thirds of a loaf is still better than half a loaf; but I would like to go away from this debate with a commitment that any package we adopt deals with the long-term problems of social security.

I am taking this position before I lend my support to this package, because I think a long-term solution can be worked out. I think public support at the grass roots is to find a complete long-term solution to this problem, not two-thirds of a loaf, because people were promised a full loaf in 1977 and they ended up with a heck of a lot less.

There is nothing too difficult about proposing new and higher taxes; that's a relatively easy way of solving the problem, particularly if these taxes are effective at some later date. That's the situation here.

I sincerely hope this Congress is going to be different than the Congress in 1977. I hope it will distinguish itself by actually looking long and hard at the structural problems of social security rather than to repeat past legislative mistakes.

I am confident that with careful and complete analysis we will be able to fashion a bill that won't just raise enough revenue to get us through this decade but that will finally provide for a sound social security system.

Mr. Chairman, I hope that we could reach that point. I hope that we can go away from here with a full loaf.

The CHAIRMAN. Thank you.

Senator Mitchell.

Senator MITCHELL. Thank you, Mr. Chairman.

Welcome, Mr. Greenspan and the other witnesses from whom we are about to hear.

I commend them at the outset for the effort that they put into dealing with what is clearly one of the most serious problems that we face in the Nation today. It is a crisis of funding, but it is more importantly a crisis of confidence in the system.

I think there has been a truly remarkable revolution in American attitudes toward the social security system in the space of just a few years, and it has been a negative revolution, a startling decline in public confidence in the system, widespread, indeed pervasive among persons in their younger years, and consisting of fear and anxiety among people who are retired or who are approaching retirement.

Like many of the other members of the committee who have followed this matter very closely, I do not agree with all of the provisions, and I expect to ask some questions of the members regarding the methods by which they reached some of their decisions regarding their specific recommendations.

But I believe their work is important because I think social security does represent one of our Nation's great achievements despite its current problems.

I think it is most instructive, and I would recommend it to everyone, to go back and read some of the social history of the twenties and thirties and the circumstances which caused or led to the creation of the social security system, and compare those to what the system has accomplished in terms of permitting millions of Americans to live out their lives with some measure of dignity, pride, and self-respect, the need for which I am coming to believe does not decline with advancing years but in fact increases. As one moves out of work and out of other areas where self-respect and self-esteem are created and moves into retirement, the need for it is even greater.

So I commend you. I do have a large number of questions, as I'm sure other members of the committee do, but I think you have helped move a long way toward a resolution of the serious problem of funding, and more importantly the national crisis of confidence in this area.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Mitchell.

As I understand, there are no other opening statements.

I'm not certain how the Commission members would like to proceed, but I know our colleague Mr. Waggoner does have a 4 departure time. We will just proceed on an informal basis in order to accommodate any member who has a plane to catch. Dr. Greenspan, if you would begin.

I would only say that we are going to move as quickly as we can on this legislation. The House is moving very quickly, and we appreciate their leadership. We intend to move just as quickly.

There will obviously be, differences, and we will try to work out as many as we can. But we have to face up to this issue and hopefully have this bill on the President's desk before March 26

STATEMENT OF DR. ALAN GREENSPAN, CHAIRMAN, NATIONAL COMMISSION ON SOCIAL SECURITY REFORM, AND CHAIRMAN AND PRESIDENT, TOWNSEND-GREENSPAN & CO., NEW YORK, N.Y.

Dr. GREENSPAN. Thank you, Mr. Chairman. We very much appreciate having the opportunity to appear here, comprising almost half a commission.

In view of that fact, I suspect it might well be better if I would just make a very short opening statement and others add whatever qualifications they want, so that we can spend as much time as we have available for questions. As you all know, it is very difficult to have six people give statements and then open for questions at 4 a.m. in the morning, which is the most reasonable expectation.

The CHAIRMAN. Could I just add one other word?

Dr. GREENSPAN. Certainly.

The CHAIRMAN. Senator Moynihan cannot be here today, and I think the record should indicate his great leadership in this compromise effort. He is a cosponsor of S. 1. He is unavoidably not present today, but I think everyone would agree that he made an invaluable contribution to the process.

Dr. GREENSPAN. Indeed he did.

The report of the National Commission on Social Security Reform, presented to the President and the Congress on January 20, would raise an estimated $168 billion for the old age and disability trust funds during the calendar years 1983 through 1989.

It is the judgment of the Commission that this should meet any reasonably conceivable shortfalls that could arise for the rest of this decade.

There are exceptionally adverse economic scenarios, however, which during the years immediately ahead could create temporary problems for the trust funds. Such problems, in my judgment, are appropriately addressed by the Commission recommendation of a fail-safe mechanism. This would set into motion certain changes in receipts and/or outlays which would prevent the trust funds from falling below the minimum levels required to maintain monthly benefit payments. The Commission offers various ways in which this specific issue can be addressed, but no single recommendation is offered for its solution.

The 75-year deficit to be addressed and eliminated is judged by the Commission to be 1.8 percent of taxable payroll.

We recognized, as a commission, that making judgments about the size of the deficit over such an extended period of time is subject to a rather substantial margin of error. Nonetheless, I suspect that most if not all of us concur that the probability that the deficit could in fact be zero and hence need not be addressed is exceptionally small.

Hence, the Commission agreed to a set of recommendations which would eliminate a deficit amounting to 1.8 percent of taxable payrolls through the year 2056.

The short-term measures to which we subscribe have a long-term deficit-closing effect of 1.32 percent of taxable payroll. We agreed to additional delayed retirement credit amounting to 0.10 percent for the long term, and agreed that the remainder—that is, 0.58 percent of taxable payroll—should be closed in one of two ways: A majority recommends it be accomplished through an increase in the normal retirement age; a minority through an increase in payroll taxes. I should emphasize, however, that at least 12 members recommend that one or the other of these be chosen.

As a Commission we decided to exclude the financing issues of medicare from our deliberations, not because we didn't think they were important, but because they are of a different type.

We realized early in our deliberations that it would be very difficult for us to tackle medicare, given the short timeframe. We purposefully decided to leave the medical part of social security for the deliberations of the Advisory Council on Social Security currently underway, which was specifically charged with reviewing the medicare program.

Thank you, Mr. Chairman.

The CHAIRMAN. Do you have an order in which you wish to proceed?

Dr. GREENSPAN. Why don't we go sort of one side and the other, with Bob Ball being the next since he would be taking the other side.

I must say, Mr. Chairman, I purposely left out from my comments the issues which I presume will be raised in the question period relevant to the unanswered questions in the longer term. And I would request that my full statement be submitted for the record.

The CHAIRMAN. Fine, and it will be made a part of the record.

[The prepared statement of Dr. Greenspan follows:]

EXCERPTS FROM THE TESTIMONY OF ALAN GREENSPAN*

The report the National Commission on Social Security Reform presented to the President and the Congress on January 20th would raise an estimated $168 billion for the Old Age and Disability Trust Funds during the calendar years 1983 through 1989. It is the judgment of the Commission that this should meet any reasonably conceivable shortfalls that could arise for the rest of this decade. There are exceptionally adverse economic scenarios, however, which during the years immediately ahead could create temporary problems for the trust funds. Such problems, in my judgment, are appropriately addressed by the Commission recommendation of a fail-safe mechanism. This would set into motion certain changes in receipts and/or outlays which would prevent the trust funds from falling below the minimum levels required to maintain monthly benefit payments. The Commission offers various ways in which this specific issue can be addressed, but no single recommendation is offered for its solution.

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*Dr. Greenspan is president of Townsend-Greenspan & Co., Inc. and chairman of the National Commission on Social Security Reform.

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As a Commission, we decided to exclude the financing issues of medicare from our deliberations, not because we didn't think they were important, but because they are of a different type. We realized, early in our deliberations, that it would be very difficult for us to tackle medicare, given the short timeframe. We purposefully decided to leave the medical part of social security for the deliberations of the Advisory Council on Social Security, currently underway, which was specifically charged with reviewing the medicare program.

Nonetheless, it is important to remember, as this committee grapples with the financing of the OASDI system, that there are very significant potential problems in Medicare. The financing problems, at least as now currently projected, are very large. But while OASDI and HI are two problems, they draw from one pot of revenues. It is important to emphasize that the solutions to medicare are very difficult and that should be kept in mind, as the committee focuses on the issue of the retirement and disability financing systems.

There can be little doubt that a number of financial arrangements are biasing medical costs higher than they need be—the main one being that the initiator of the scope of service, usually a physician, is rarely the person who pays the bill.

Nonetheless, even were the financial and anticompetitive factors which create an inflation bias eliminated, it is unlikely that the burgeoning growth of medical expenditures could be significantly subdued. The reason is that in recent years medical and associated technologies have taken a leap forward and currently exhibit little evidence of slowing down. The advent of the artificial heart is only the leading edge. Partly as a consequence, average life expectancy has increased significantly during the past decade and is expected to continue to do so.

Any industry whose technological advances outstrip the average for the nation as a whole will show a marked tendency to grow faster than the GNP. It is certainly not surprising that telecommunications has increased its share of GNP in recent years (neither should the share rise in medical services). Endeavoring to suppress growth is as difficult in one, as it is in the other.

I should like to address the rest of my time to the final issue which divided the Commission: the question of increasing the normal retirement age as part of the solution for the post-1990 period. Let me say first that I do not consider the question of extending the age for full retirement benefits as a question of the appropriate level of benefits; it is a key long-term stabilization issue. Continuation of financing the Old Age and Survivors Insurance system through payroll taxes, requires that there be rough equality (in present value terms) between the amount of taxes paid into the social security trust fund by each retiree and the amount that he or she ultimately withdraws. That, as we are all aware, has not been the case in recent years. Benefits have far exceeded the combined taxes paid by individual workers and their employers plus interest over the life of their employment. It is clear however, that if the number of years in which the average retiree receives benefits continues to increase relative to the number of years in which he contributed to the trust funds, the ratio of benefit payments to payments into the fund is almost surely going to fall, that is, the replacement ratio must continuously decline. Projected over the long run this leads to levels of monthly benefits which probably would fall far below the poverty level. Short of a noncredible acceleration in productivity or massive increase in immigration over the next half century and beyond, this conclusion is irresistible.

Ultimately, the age of the full retirement benefits is going to have to be linked to longevity. The longer we wait to do this, the greater the long-term pressure on the OASI Trust Funds. The majority of the National Commission recommends an increase in the normal retirement age which would raise 0.6 percent of taxable payroll. The normal retirement age would be gradually increased to 66 by the year 2015 followed by indexing to longevity thereafter.

As I understand it, the major argument against the increase in retirement age is that, despite the uncontested significant improvement in longevity in the past decade, there is serious question whether the ability to work has increases as well. As people age the number of disabled individuals must, of course, be expected to rise. Given a hypothetical group of individuals who in an earlier period would have died at age 65 but in the current period will live to the age of 67, one must presume that a significant proportion of those whose life has been extended will be in less than perfect health and that a significant number substantially disabled. On the other hand, a large number of those whose life has been extended from 65 to 67 must represent individuals whose health is adequate to continue working. As Jacob Feldman of the National Center for Health Statistics told the Commission last June, of all men between 65 and 67, in recent years 63 percent were fully able-bodied with respect to work and another 13 percent had limited work capability. Moreover, even if work disability were far more prevalent, one should not treat the issue with an old age retirement program. It should be dealt with directly. The OASI systems should reflect what it truly was endeavored to be—a retirement system, not a disability system. The majority of the National Commission, in fact, recommends generous disability benefits to those between age 65 and the increased retirement age for OASI.

This also applies to the group of individuals who have toiled in jobs requiring heavy labor throughout their lives, and have great difficulty working beyond their early sixties because of the physical requirements of their occupation. However, the number of such jobs in our economy is dwindling and will continue to do so. Hence, the number of people who retire from heavy labor will be a declining number in the decades ahead. If this is a serious coincern, it can and should be handled as a special case. One should not craft the major government retirement system in this country to accommodate a special case.

The CHAIRMAN. Mr. Ball, I would be happy to recognize you. Again, I think the record should reflect that you are one of those who spent the better part of 2 or 3 weeks on a daily basis trying to hammer out a compromise. Much of the credit for the fact that we did work out a compromise undoubtedly goes to you, Mr. Ball, and we appreciate your contribution.

STATEMENT OF ROBERT M. BALL, VISITING SCHOLAR, CENTER FOR THE STUDY OF SOCIAL POLICY, WASHINGTON, D.C., AND FORMER COMMISSIONER OF THE SOCIAL SECURITY ADMINISTRATION

Mr. BALL. Mr. Chairman, thank you very much. The accomplishment, of course, was shared by all members of the Commission.

I want to particularly compliment our chairman, who from the very beginning gave full assurance to those of us who were in the minority on the Commission of a very fair development of the issues and a fair study and a fair handling of all the meetings that we had. I think the compromise wouldn't have been possible without the kind of atmosphere that the chairman created.

Mr. Chairman, like Dr. Greenspan, I feel that it would be much more important to get rather quickly to the questioning, and that almost everything that I would have to say can be brought out in that way.

I do have a rather long statement that I would like, with your permission, to have introduced into the record.

The CHAIRMAN. It will be made a part of the record.

Mr. BALL. And, with that, I would just like to emphasize two or three points, mostly because I think there may be some misunderstanding about them as a result of the way the agreement has been reported.

It is an extraordinarily complicated subject, and I'm not at all faulting the reporters and the TV people who have handled this, but when you have to do it in a short time it is bound to lead to some misunderstanding.

The major point on which I think there is misundertanding is the question of the long-run. I have seen it said from time to time that the Commission dealt with the short run and not with the long run. Well, as has been brought out here already today, the agreed-upon parts of the Commission recommendation do reduce the longrange goal we had in mind from 1.8 percentage of payroll to 0.58 percentage payroll, and that's two-thirds of the official long-term deficit.

Then we went further and agreed, as the chairman said, that we would both make proposals for solving the remaining 0.58 percent.

So I just want to stress that we did address and intend to back the Congress addressing the entire financial short-fall, both short term and long term.

This leads me to say that another possible misinterpretation is that the short term has been defined between now and 1990. Then there is some tendency to report that problems begin in 1990, as if the recommendations addressed only the situation between 1983 and 1990, when even under present law I think it should be emphasized that the period from 1990 to around 2010 or 2015, in all likelihood—you can make economic scenarios where this would not be true, but in all likelihood—during that 20- to 25-year period, even under present law, the cash benefit part of social security is in very good shape, with large increases of income over outgo during those years according to the more pessimestic of the central set of assumptions. It just isn't true that the system is in bad shape and it keeps getting worse. Present law, for very simple reasons, starts to produce large surpluses beginning about 1990.

And the reasons are that the birthrates in the years of the Big Depression, the thirties, were low—people didn't have much money, and they didn't have very many children.

That means that during the 1990's and the early part of the next century there will be a slowing down in the rate of increase in the number of people over 65. Yet, at the same time during that period the workforce grows as a result of the baby boom which occurred after World War II.

So you have a continuation of the present ratio of workers paying in to beneficiaries taking out, which is now three workers paying in to one beneficiary taking out. You have that continuing, under the trustees' assumptions, for about the next 30 years, with the result that increases in productivity actually reduce the cost of social security as a percent of payroll or as a percent of GNP during this period.

If you add to that the fact that the Congress has already scheduled a tax increase to come into effect in 1990, you get large excesses of income over outgo, so that in 1991 alone the estimate is somewhere around $20 billion added to the trust funds, and then those amounts grow annually during the middle period that I am talking about.

We addressed the question of getting to 1990, then a good period, and then we have specifically also addressed the estimated demographic problems that would occur after that period, as the chairman of the Commission indicated. We have dealt with the entire long-range problem for the full 75 years over which the estimates are made.

Mr. Chairman, with that I will conclude. I have lots of points I would like to bring up, but I'm sure they will come up in the questions.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Ball follows:]

STATEMENT OF ROBERT M. BALL ON THE MAJORITY RECOMMENDATIONS OF THE BIPARTISAN NATIONAL COMMISSION ON SOCIAL SECURITY REFORM

Mr. Chairman and members of the committee: My name is Robert Ball. From April 1962 until March 1973 I was Commissioner of Social Security, serving under Presidents Kennedy, Johnson, and Nixon. Prior to becoming Commissioner, I served for approximately 20 years in various positions in the Social Security Administration and its predecessor organization, the Social Security Board, and for the 10 years prior to becoming Commissioner, I was the top civil servant in the Social Security organization. Since leaving the Government I have continued my deep interest in social security and have written and lectured extensively on the subject. I am currently a visiting Scholar at the Center for the Study of Social Policy, Senior Consultant to the Study Group on Social Security, and a member of the Executive Committee of the Save Our Security (SOS) Coalition. I am appearing today, however, as one of the five persons appointed to the National Commission on Social Security Reform by the Democratic leadership in the Congress, and the views in my testimony do not necessarily represent those of any other organization with which I am associated.

INTRODUCTION

I would like to begin by complimenting our able chairman, Dr. Alan Greenspan, and to thank him for the fairness with which he conducted all the work of the Commission. I would also like to express appreciation to the other members of the Commission for their fine spirit of public service and cooperation. I would like to thank the staff for their excellent work—both those formally assigned to the Commission and the many others who helped in the Commission's work. It has been a privilege to be on this Commission.

SUMMARY OF POSITION

Taken as a group of interrelated recommendations, I fully support the consensus recommendations. The recommendations are endorsed by all 5 of the Commission members who were appointed by Demoncrats* and 7 out of 10 of those appointed by Republicans. As you know, the proposals are backed by the President, the Speaker of the House, and the Majority Leaders of both the House and the Senate, among many others.

There is no member of the Commission who is pleased with each of the recommendations taken separately. No one would have come up with exactly these recommendations if he or she had been free to design the proposals alone.

They represent a compromise within the Commission and between the Commission members and the administration, but taken together, they are, in my opinion, as good a compromise as could be designed to get the widespread legislative support and the signature of the President that are necessary to solve the Social Security financial problems. In the words of the Washington Post, "It is as close to absolute fairness as any social security revision can ever be."

Given the fact that between now and 1990, social security income is estimated to fall about 5 to 10 percent short of expenditures, it is necessary during this period to increase income or reduce expenditures. To get agreement within the Commission and to design a group of recommendations that could win wide support, it was clearly necessary to do both—to have some reduction in expenditures and some increase in income. This the plan achieves in a fair and balanced way. All share in the sacrifice necessary to restore full financial health to social security—current beneficiaries, contributing workers, employers, and the general public, but none are asked to bear a large additional burden. The changes proposed are modest and reasonable.

Taken together, the consensus recommendations eliminate the shortfall between now and 1990, and according to the more pessimistic of the intermediate estimates (II-B) of the Board of Trustees, the trust funds will return to fully satisfactory levels

* Mr. Kirkland dissented from the coverage of new Federal employees and instead proposed taxing the entire employer payroll.

in the 1990's. The agreed-upon recommendations also bring the long-term deficit of the program within the range of what has traditionally been considered close actuarial balance, plus or minus 5 percent of expenditures over the 75 years for which the estimates are made. That is, the consensus recommendations reduce the official 1.8 percent of payroll deficit (1982 II-B estimate) to 0.58 percent of payroll, which is 4.5 percent of what the estimated expenditures over the next 75 years would be after the adoption of the Commission recommendations.

The consensus was, however, that we would go further and propose ways of reducing the 0.58 percent of payroll deficit to approximately zero. We could not agree on how best to eliminate this final 0.58 percent, but the five members who were appointed by Democrats have proposed scheduling an increase in the contribution rate of a little less than one-half of 1 percent of earnings in the year 2010, with the employee share to be offset by a refundable tax credit.

It now appears that the 1983 Trustees Report will show a slight increase in the remaining deficit, perhaps 0.7 as compared to 0.58, and the Congress will need to decide whether it is desirable as part of strengthening public confidence in the long-run financing of the program to cover this additional small deficit. Clearly, treating 75-year estimates as if they could be made with such a high degree of exactness is unrealistic, but there may be some public relations advantage in having the official estimates show no deficit at all. It does not seem to me of great importance either way.

The Commission also agreed on three steps that would strengthen the financing of the system should actual economic performance fall outside the range of the rather pessimistic assumptions the Commission used. First, the Commission agreed that authority for Old-age, Survivors and Disability Insurance (OASDI) to borrow from the Hospital Insurance (HI) fund should be continued as a fail/safe procedure through 1987. Second, the Commission agreed on a "stabilizing provision" to the effect that beginning in 1988, a drop in trust fund assets to unacceptable levels trigger a temporary change in the indexing procedure. Third, the Commission agreed that the law should contain a provision that would ensure timely payment of benefits if unexpectedly adverse conditions occurreed with little advance notice. The Commission did not agree on the specifics of this ultimate fail/safe, but the five members who were appointed by Democrats recommended that the law be amended to allow short-term borrowing from the general fund at interest in the unlikely event that the other measures recommened prove insufficient in some emergency situation.

There has been some suggestion that it might be desirable to strengthen the short-run financing of the program even further. A group of private insurance actuaries appearing before the Social Security Subcommittee on Ways and Means on February 9, for example, testified that under the Commission plan the estimated assets in the funds at the beginning of some years seemed low to them in relation to the next year's estimated outgo. This perception of a posible cash flow problem in some years arises because of the practice of crediting Social Security taxes to the trust funds gradually over the course of a month, while Social Security checks are, of course, charged against the funds at the beginning of the month when issued.

If in the future social security receives credit at the beginning of the month for taxes collected during the month—as has been proposed—there would be a considerable difference in the ratio of trust fund assets to the outgo in a subsequent period, since on average, collections are quite close to outgo. Under the conservative II-B assumption for the 1983 Trustee's Report, the Commission's plan, given this new procedure, would produce trust fund ratios of 20 percent or more through 1988, rise to 33 percent in 1989 and increase rapidly thereafter. These ratios are clearly ample. With the three changes described above—interfund borrowing, the introduction of a stabilization procedure and authority to borrow from general revenue—the Commission's proposals will provide for the full and timely payment of benefits under even much more unfavorable economic conditions that those assumed in the new II-B estimates.

All in all, the proposals of the Commission solve both the short- and long-term financing problems of OASDI.

THE DEFINITION OF SHORT-TERM AND LONG-TERM FINANCING GOALS

The Commission decided early in its deliberations not to deal with the medicare program. The current statutory Advisory Council on Social Security established a few months ago by Secretary Schweiker will be concerned exclusively with making recommendations about that program. We did not feel that we could deal adequately with both HI financing and the financing of OASDI in the time available. Moreover, the considerations involved in HI financing are quite different from those involved in the cash benefit program. The increasing costs of HI under Medicare are caused by the same factors in medical economics that are driving up the cost of private insurance, and many of us felt that in this program the proper emphasis was not merely to increase the funds or reduce benefits to conform to actuarial projections, but rather to consider the extent to which the rate of increase in the cost of providing services can be controlled. The entire report of the Commission and its recommendations, therefore, relate to OASDI, except for the recommendation to extend the interfund borrowing provision that expired in 1982.

Short-term

Under present law, there is a shortfall in expected income for OASDI as compared to expected expenditures between now and 1990. The gap is not large relative to the size of the program—5 to 10 percent—but it is real and must be addressed. The boundaries of the shortfall would appear to be between $75 and $200 billion, depending upon the economic assumptions used.

The members of the Commission have agreed that since trust fund balances for OASDI are now at dangerously low levels, it is prudent to set short-term goals on the basis of quite pessimistic economic assumptions. We are not necessarily agreed that there is a shortfall between income and expenditures in the range of $150 to $200 billion as has been publicized, but we are convinced that it could be this high under adverse economic conditions. Should the economy perform better than was assumed in setting these target figures, the resulting more rapid buildup in trust fund balances would be desirable, in any event.

Mid-term

The shortfall between now and 1990 is followed by a period of 20 to 25 years when OASDI, even under present law, will have substantial annual surpluses of income over outgo, with the trust fund building up at the rapid rate. Although it is possible to construct economic projections where this build-up would not occur under present law, the Commission's recommendations—including a shift to wages or prices whichever is the lower should the trust funds drop below 20 percent of the next year's outgo—would go a long way toward guaranteeing that the expected buildup in the 1990's and the early part of the next century takes place.

Basically, the reason for the favorable period from roughly 1990 to 2015 is demographic. Birth rates were low in the great depression years of the 1930's with the consequence that the increase in the number of older people which we have been experiencing will slow down. In addition, the baby-boom generation born after World War II will be swelling the labor force so that the ratio of workers to beneficiaries is expected to stay about the same as it is today—three workers for each beneficiary—for at least the next 30 years. Under these circumstances, increases in productivity reduce the cost of Social Security measured as a percent of payroll or gross national product. At the same time, the present law already provides for an increase in the contribution rate beginning in 1990, with the result that very large annual excesses of income over outgo are expected. In the 1 year, 1991, the excess is expected to be over $20 billion, and during this middle period the excess will grow year by year.

Long-term

The Commission also agreed that the estimated long-range deficit of 1.8 percent of payroll (1982 II-B estimate) should be reduced to approximately zero. We differed among ourselves as to why we took this position. Personally, I have considerable skepticism about our ability to know, within very wide limits, what the demographic, economic, and social situation of the United States will be 50 to 75 years from now, and the projected deficit occurs almost entirely in that far-off period. However, as a matter of restoring confidence in the financing of the program, it seemed best to all of us to design a plan that would result in the Board of Trustees saying officially that the program was in actuarial balance in both the short and long run.

The consensus agreement alone comes very close to this goal, providing for a reduction of 1.22 percentage points in the 1.8 deficit. The five members of the Commission who were appointed by Democrats proposed, in addition that the law be amended to provide a contribution rate increase of 0.46 percent of payroll in the year 2010 (refundable to the employee) as a way of eliminating the remaining 0.58 percent of the long-term deficit. Such an increase may not actually be needed and, of course, as 2010 approaches such an increase would not be allowed to go into effect unless estimates then being made showed that it was desirable. Moreover, by that time there might be support for some other way of financing part of the social security program. Yet it is of some importance to put the increase in the law now and thus show the intent of Congress to meet the full cost of the program over the entire 75 years for which the estimates are made. The proposal made by other members of the Commission to meet this remaining 0.58 percent deficit would be to raise the age of first eligibility for full benefits to 66 by 2015, and then after that date have the age rise automatically in accordance with increases in longevity, ultimately reaching 68 in about 2055 under the asumptions in the 1982 Trustees' Report.

Mr. Chairman, we have agreed on the specifics of so much within the Commission—a plan to meet the short-run problem, and a plan to meet by far the largest part of the estimated long-run deficit—that I hesitate to spend much time on this difference of opinion aobut two approaches to a problem which may very well not even exist. The five members of the Commission who were appointed by Democrats have included a supplementary statement in the Commission report that tells why we are against raising the age of eligibility for full benefits and I have attached that supplementary statement to this testimony. Suffice it to say here that, aside from whether or not it is desirable to raise the age of first eligibility for full benefits, it seems to me unwise to index additional social security provisions. Under the indexing proposal, no one would know ahead of time at what age full benefits would be available. Private pension planning and private savings for retirement would be made more difficult. Surely some social security questions can be left to the determination of future Congresses.

THE CONSENSUS AGREEMENT

The major provisions affecting the financing of the program are as follows:

Rescheduling the social security tax rate.—Under present law, the OASDI tax rate rises from the 5.4 percent of earnings now being charged to 5.7 in 1985 and to 6.2 in 1990. Under the agreed-upon plan, workers would not have to pay any more than under present law until 1988, and then there would be a higher rate for 2 years, an increase of 0.36 percentage points in 1988 and 1989, with a return to the present schedule in 1990. (The OASDI trust fund would get additional income from moving the 1985 rate to 1984, but the increased Social Security tax for workers would be exactly offset in that year by a refundable tax credit.) Employers, who can count the social security tax as a business expense, would be charged 0.3 percentage points more than present law in 1984 and as is the case with employees, 0.36 percentage points more in 1988 and 1989.

Although this rescheduling of tax rates contributes $40 billion to the short-term goal of $150 to $200 billion, the increase for individuals is relatively slight—nothing until 1988 and then for a $20,000 earner, for example, $1.38 per week for 2 years. (See Attachment No. 2 for the short-term and long-term savings or costs attributed to each Commission recommendation.)

Putting the social security tax for the self-employed on a basis comparable to other covered workers.—When the self-employed were first brought under social security, the rate for them was established at one and a half times the employee rate, and although it has varied somewhat from that basic rate from time to time, it is approximately at that level today and under present law would soon be exactly one and a half times the employee rate again. The self-employed, of course, get the same protection as everyone else, but for others the rate paid is the employee rate plus a matching amount by the employer. Because the self-employed pay less, everyone else under the system pays somewhat more. This isn't fair.

The proposal is to remedy this inequity by charging the self-employed two times the employee rate and to treat one-half of it as the employer's contribution is treated—allowing the self-employed to deduct one-half of their total contribution as a business expense. This proposal will increase income to the social security system between now and 1990 by $18 billion, but $12 billion will be offset in the general budget because of the business deduction. This change also reduced the long-term, 75-year average estimated deficit by 0.19 percent of payroll. One way of easing the transition to this new tax basis for the self-employed would be to allow them a refundable tax credit in 1984 for the increase in the employee rate, 0.3 percent of earnings. The Commission Report does not address this question, but such treatment would be consistent with the recommendation to treat half of the self-employed payment as an employer contribution and half as an employee contribution.

Crediting the trust funds for past military service credits and unnegotiated checks.—Employers and employees have to pay for social security benefit credits when they are earned, but in the case of certain military service credits that are paid for by the Federal Government, the amounts due are not paid to social security until the benefits are paid. Putting payment for military service credits on a basis more comparable to other benefit credits and recrediting to the trust funds outstanding checks which have gone uncashed for a considerable period of time would mean that the OASDI Trust Funds would receive a lump sum payment of $20 billion in 1983.

The military have been covered under social security for many years, but they pay contributions only on the cash paid to them. The government pays the cost of the benefit credits made in lieu of allowances for room and board. However, under present law, the Government does not make payment currently (but only when benefits are paid) for these credits. Moreover prior to 1957, free credits of $160 per month were granted for service in the Armed Forces and these credits, too, are paid only when benefits are paid, and the cost is amortized over a long period of time. The proposal is to pay up for the back amounts owed by the Government in a lump sum, and then in the future to pay currently the equivalent of employer and employee contributions on the wage credits in lieu of allowances.

Mandatory coverage of all nonprofit employees and Federal employees newly hired after 1983.—Social Security is a system with a national purpose through which just about everyone who works contributes toward the payment of benefits to make up for income lost because of retirement in old age, total disability, or the death of a wage earner in the family. It is anomalous that Federal employees do not take part in this national effort.

The Commission recommends mandatory coverage of newly hired employees and establishment within the civil service retirement system of a special supplementary plan for these newly hired employees, independent and completely separate from Social Security in every way, just as private pension plans are supplementary to Social Security and separate from it. The supplementary plan should be designed so that when combined with social security it will supply, overall, as good protection as the present civil service system does alone. Current civilian employees of the Federal Government (the military are already covered under social security) would continue to be covered by the present civil service retirement system for their employment by the Federal Government, but would not be under social security.

For many new Federal employees, this arrangement of social security plus a supplementary plan would undoubledly be better than the present civil service plan alone. Social security with its weighted benefit formula is generally more favorable to low-paid employees than the civil service System, and Social security is better for those who move in and out of Federal employment. Moreover, full survivorship and disability protection is more quickly achieved under social security.

Covering those non-profit employees not now covered (15 percent and newlyhired Federal employees will add $20 billion in income to the Social Security system between now and 1990. Moreover it will reduce the long-range deficit in social security by 0.3 percent of payroll. This is true because today, while about 80 percent of Federal annuitants age 62 and over are also eligible for social security when they reach 65, they will have paid into social security for relatively short periods and will receive benefits that are excessive in relation to the contributions that they have made. For this reason, everyone else in the country is paying somewhat higher social security contribution rates because Federal employees are not covered.

One would think that present Federal retirees and present Federal employees would not have much standing in making a case against the coverage of Federal employees who have not yet been hired, but they have been arguing that (1) new Federal employees will be asked to "bail out" the social security system to their own disadvantage, and (2) present retirees and present employees will be hurt because the new employees will not be paying into the civil service retirement system or not paying in as much as they otherwise would. Both of these arguments are fallacious. Under the plan, new employees will be asked to do just what all other employees in the country are asked to do, pay into social security throughout their working careers in return for social security protection. Then, in addition, they will share with about half of the private labor force the additional protection of an independent, supplementary plan. Far from "bailing out" social security, this arrangement will end the unfair situation where others have to pay more for social security because Federal employees get social security benfits at bargain rates from working in social security covered employment for short periods of time. Second, it just is not true that the present civil service retirement system will be less well financed because the proposal. At the present time, the protection furnished by the civil service retirement system is worth about 40 percent of payroll. Employees are paying only 7 percent of their earnings toward this protection. Under present law, the benefits of present workers will be paid for mostly from general revenues, not the contributions of the newly hired.

The contribution that the newly hired employees would make toward a specially designed benefit plan within the civil service system would mingle with all other contributions to that system, which today is not a single plan and will not be in the future. Today the system covers, with special provisions, Members of Congress and congressional employees, air controllers etc., as well as the bulk of executive branch employees. The lower contributions to be paid by new employees (because, of course, the supplementary plan on top of social security will be cheaper than the design of the present plan for the presently employed) will be balanced by the fact that the newly designed plan will have lower long-term costs and create less liability for the civil service retirement system. The system as a whole will not be injured.

There is apparently widespread misunderstanding among Federal employees about these facts, some even believing that the civil service retirement system is adequately financed by a combination of the 7 percent contributions that they pay and matching contributions from their agency. It is important that these misunderstandings be corrected.

Delaying the cost-of-living adjustment for 6 months so that in the future any automatic increases will be made for the month of December rather than for June as in present law.—The five members of the Commission who were appointed by Democrats agreed to this change with great reluctance. We did so because it was essential to an agreement which we believe, overall, is in the best interest of present beneficiaries and contributors. It is worth some sacrifice on the part of all to assure both the short- and long-range financing of the system and remove the fear of drastic cuts that has haunted beneficiaries and contributors for the last 2 years. It is worth some sacrifice on the part of all to get this done promptly and without the bitter fight that might well have followed the failure of the Commission to reach agreement.

The agreement does not include any other reductions in present or future benefits—no reduciton in replacement rates or cuts disguised as increases in the age at which full benefits are first paid, although one-half the benefit of the 10 percent of beneficiaries with the highest incomes would be subject to income tax. It looks now as if the automatic increase in benefits due to the cost-of-living adjustment payable for this June under present law will be below 4 percent, perhaps an increase for the average retired beneficiary from the current monthly benefit of about $420 to a new rate of about $435.

Under the plan, the new rate of $435 for the average retired beneficiary would be delayed until the payment for the month of December. Moving the cost-of-living adjustment to the calendar-year basis will reduce expenditures about $40 billion between now and 1990 and reduce the long-range deficit by 0.27 percentage points.

It is possible that the CPI increases from the first quarter of 1982 to the first quarter of 1983 might be slightly less than 3 percent so that under present law no cost-of-living adjustment would be made in 1983. There would be widespread misunderstanding if in the same year that the COLA is moved to a calendar-year basis there was no increase at all for 18 months. Because of this possiblity, I believe it would be desirable to provide for the COLA for next December without regard to the 3-percent trigger in present law.

Under the agreement, those social security beneficiaries who also get supplemental security income (SSI) because their benefits and other income are too low to meet minimum standards of need will have their SSI benefits raised by $30 a month. In the future, $50 of social security benefits would not be taken into account in determining need under the SSI program instead of $20 as at present. The agreement did not cover the question of whether the cost-of-living adjustment for the SSI program should be advanced 6 months from present law, and the administration has now proposed this as part of its new budget proposal. I hope that the Congress will not agree to postponing the July cost-of-living adjustment for SSI recipients. By definition, these people need all the purchasing power they have and more. Two million of them—30 percent of the elderly and two-thirds of the disabled—are not social security recipients and will not benefit from the increase in the disregard from $20 to $50. Indeed few have anyhting but SSI.

I recognize that it is desirable in the future to keep the timing of the COLA for both programs the same. Otherwise what the dual beneficiaries gain from an earlier SSI increase, they may lose from the OASDI increase later, as it is offset dollar for dollar against the means-tested SSI program. Keeping the timing of the COLA's together is as readily accomplished by an SSI adjustment in July and again in January as it is by skipping the July increase. This is what I would recommend.

Income taxation of one-half of social security benefits of higher income beneficiaries.—

Social security benefits are not now subject to income taxation simply because in the early days of the program the Treasury ruled—I believe erroneously—that social security benefits are a gratuity. There is no legislative history. On the basis of this ruling, social security payments have been treated differently from other retirement income. The rule generally for retirement income is that it is subject to income taxation once the recipient has recovered what he has paid toward the retirement benefit, exclusive of interest. Thus, employer paid-for pensions are subject to income taxation immediately and in full, and contributory plans such as Federal civil service are taxed after the benefits exceed the employee's own contribution.

The special treatment of social security benefits hardly seems justified for higher income beneficiaries. Thus the Commission proposes that for single filing units with $20,000 or more in non-Social Security income and for those filing as couples with $25,000 or more (10 percent of beneficiaries), one-half the social security benefit be included in gross income for income tax purposes. The limitation to one-half rests on the rationale that although one-half the benefit can be thought of as being derived from the employee contribution on which a tax has been paid during one's working life, the other half, derived from the employer contribution, has not been taxed. It has not been taxable income for the employee and is treated as a business deduction by the employer.

The Commission recognized that this proposal needs refinement to eliminate triggering the taxation of a sizeable amount of social security income by having other income just barely over the thresholds recommended. One possible way of meeting this problem would be to include in taxable income $1 of social security benefits for each $2 of nonsocial security income above the thresholds, but the committee will undoubtedly want to study other possibilities. This proposal results in additional income to the system of $30 billion between now and 1990 and reduces the long-range deficit by 0.6 percent of payroll.

MEASURES TO PROTECT THE FUTURE FINANCIAL STABILITY OF THE PROGRAM

The short-term financing problem in social security is entirely due to recent poor economic performance. The present program is very sensitive to changing economic conditions, particularly the relationship of wages and prices and the amount of unemployment. Income varies according to the level of payrolls while benefits rise with increases in the Consumer Price Index. Usually wages rise faster than prices, and the resulting higher payrolls finance the more slowly rising cost-of-living increases. This is how the pay-as-you-go financing of the system ordinarily works. In several recent years, however, prices rose faster than wages, causing larger payouts and lower income than expected. in addition, high unemployment has further reduced payrolls.

As part of the agreed-upon package, the Commission proposes the adoption of an economic "stabilizer," which would go into effect in 1988 when reserve ratios are expected to have improved under these proposals. If ever again the OASDI reserves drop below 20 percent of the next year's outgo, wages or prices, whichever is the lower, would be paid until the 20 percent fund ratio was restored. When the fund ratio reached 32 percent, additional benefits would be paid to make up for any payments that were less than the increases called for by the price adjustment. The payback would be limited to amounts that would maintain a 32 percent fund ratio.

In addition to this modification of indexing designed to reduce the sensitivity of the program to economic factors, the consensus agreement includes a recommendation to extend the authority of the OASDI trust funds to borrow from the hospital insurance funds from the effective date of the amendments until the "stabilizer" goes into effect. It is not expected that either of these devices will be needed, but it is important to have insurance against the possibility of even poorer economic performance than is assumed in the projections underlying the basic recommendations.

The Commission has gone further and recommended that, beyond the stabilizer and inter-fund borrowing, there should be an ultimate fail/safe arrangement to tide the program over some completely unexpected short-term development. We were unable to agree on the exact nature of such a provision but, as indicated earlier, the five members of the Commission appointed by Democrats recommend that authority be granted to the program, under such limited circumstances, to borrow from general revenues at interest or, if it is considered preferable, to issue its own bonds, a device which would show that the debt was clearly a social security obligation.

OTHER PROPOSALS THAT EITHER HAVE NO FINANCIAL EFFECT OR RELATIVELY SMALL FINANCIAL EFFECT

The Commission has made several other proposals, many unanimously, which are important, even though most do not contribute significantly to the solving of the financial difficulty. These recommendations include prohibiting the withdrawal of state and local government employees, the great majority of whom are now covered under social security through voluntary agreements. (This proposal may have a significant financial effect.) Other recommendations include the elimination of windfall benefits for persons with pensions from non-covered employment, several proposals for providing greater equity under the program for certain groups of beneficiaries (primarily women), the gradual increase from 3 percent to 8 percent (after 1990) for each year in which the individual postpones benefits because of work, the reallocation of the amount of the social security tax now going to the OASI and the DI Trust Funds, the elimination of opting out of part of social security coverage through the use of a salary reduction plan (section 401(k) of the Internal Revenue Code), new investment procedures for the trust funds which will make clear that the investments are being properly handled, and the addition of two public members to the Board of Trustees. I support all of these proposals and their rationale is adequately developed in the report itself.

THE REMOVAL OF SOCIAL SECURITY FROM THE UNIFIED BUDGET AND THE ESTABLISHMENT OF THE SOCIAL SECURITY ADMINISTRATION AS AN INDEPENDENT AGENCY UNDER A BI-PARTISAN BOARD

Although the majority of the Commission favored taking the social security program out of the unified budget and treating its financing entirely separately, as was the case prior to fiscal year 1969, the division of opinion was fairly close. I agree with the majority. Only by such a separation can it be made unmistakably clear that social security decisions are being made for reasons internal to this separately financed program and not for the purpose of making a unified budget look better. Since social security funds can be used only for social security benefits and to pay for the cost of administration, I believe that separation is also better accounting practice.

It is easily understandable, however, that many are reluctant to make this change just when the adoption of the Commission's recommendations—which have been made entirely because of the internal needs of the social security system—would, as a by-product, reduce the unified budget deficit.

In any event, the administration has agreed that the OASDI program will be presented in the budget from now on as a separate budget function and not be included in the 600 function with other income programs. I believe this is an important step in the right direction, and even though this change could not be implemented in time for the budget just submitted, it is my understanding that during the current budget process OASDI will not be placed in competition with other programs in function 600.

There was more general agreement in the Commission on setting up social security as an independent agency, although some members felt that more study was required before action was taken. I believe it should be done now. I believe that setting up Social Security as an independent agency headed by a bi-partisan board would improve the operation of the program and help restore faith in the program.

We need to make some institutional changes in the way social security is handled in order to assure people that the program will continue to operate as an independent insurance system, protected against the short-term policy swings of elected officials and political appointees. Under social security, workers are creating rights for their retirement which may not occur for 40 or more years down the road. They should feel secure that those rights will be respected. It is not enough to have the system operate as part of a Cabinet department with a President appointing both the Cabinet Secretary and the Commissioner of Social Security. Social security should be handled in a way more in keeping with the obligations of the huge pension and group insurance plan that it is. I believe that the policy functions should be performed by a Board of Directors with staggered terms, appointed by the President and approved by the Senate, and that the Board, in turn, should have the right to hire and fire the chief executive officer without regard to usual civil service rules. The power to set benefits and the financing of the program would, of course, remain with the Congress and the President as it is today.

It would add significantly to public understanding of the trustee character of social security as a retirement and group insurance plan if the program were administered by such a Board direclty under the President. Social security has about 85,000 employees and some 1,300 district offices across the country; it is one of the very largest direct-line operations of the Federal Government. It does not make sense administratively to have this huge program, which intimately touches the lives of just about every American family, operated as a subordinate part of another Government agency. The management of social security could be made more responsive to the needs of its beneficiaries and contributors if it were free from the frequent changes in the levels of service to the public which grow out of short-term decisions about employment ceilings and the varying management value systems which follow the frequent changes of HHS Secretaries and their immediate staffs. But most important, an independent Board would be visible evidence that contributory social insurance was separate from other government programs.

Just about every American has a major stake in protecting the long-term commitments of the social security program from fluctuations in politics and policy. The administration of social security by a separate bi-partisan Board would strengthen public confidence in the security of the long-run commitments of the program and in the freedom of the administrative operations from short-run political influence. It would give emphasis to the fact that in this program the government is acting as trustee for those who have built up rights under the system.

CONCLUSION

There is one recommendation of the Commission which I have not yet commented on, and which, in some ways, may be the most important of all. The last few years have seen many sweeping attacks on the Social Security program and many radical proposals for change have been offered. However the Commission's #1 recommendation is as follows: "The members of the National Commission believe that the Congress, in its deliberations on financing proposals, should not alter the fundamental structure of the social security program or undermine its fundamental principles. The National Commission considered, but rejected, proposals to make the Social Security program a voluntary one, or to transform it into a program under which benefits are a product exclusively of the contributions paid, or to convert it into a fully funded program, or to change it to a program under which benefits are conditioned on the showing of financial need."

The social security system in essentially its present form has served the American people well. I do not believe that the American people want to change the program fundamentally or to cut back on social security protection. I believe current workers are willing to pay for a good system of social insurance in which they have confidence. Our major task is to give them once again a firm basis for full confidence.

Workers have a common interest with the retired, disabled, and surviving families of deceased workers in sound planning for income insurance. Everyone who is fortunate enough to live until retirement will need a regular, permanent income to replace the earnings that were previously the main source of support. We are all headed in the same direction—no one stays young. Also, any worker may become totally disabled before retirement, or he may die and leave surviving dependents. Planning for income security is not primarily a matter in which those at work help those who are not. We are planning together for the kind of protection that we all need.

[Attachment No. 1]

SUPPLEMENTARY STATEMENT BY COMMISSIONERS ROBERT M. BALL, MARTHA KEYS, (MEMBERS SELECTED BY THE DEMOCRATIC LEADERSHIP OF THE CONGRESS)

LONG-TERM FINANCING AND ISSUES OF SPECIAL CONCERN TO WOMEN AND MEETING THE REMAINING LONG-TERM DEFICIT

All of us supported the compromise agreement which is being recommended by a vote of 12 to 3 of the full Commission.[1] The agreement provides for fully meeting the Commission's short-term financing goal and also for meeting about two-thirds of the Commission's long-term goal—1.22 percent of payroll out of the 1.8 percent projected needed.

We recommend that the remaining 0.58 percent of payroll deficit be met by providing additional revenues starting in the year 2010, in advance of the period when the bulk of the deficit is projected to occur. Sufficient additional revenues would be provided by an increase of less than one-half of 1 percent (0.46 percent) in deductions from workers' earnings beginning in 2010 and a like amount in employer payroll taxes (with an equal combined rate for the self-employed) or the revenue could be supplied by an equivalent general revenue contribution, or some combination of the two. For purposes of present legislation we would support putting in the law now an increase in the contribution rate beginning in 2010 of 0.46 percent of payroll (with the employee contribution offset by a refundable income tax credit), recogniz-

[1] Mr. Kirkland is not joining in the recommendation to extend coverage to Federal employees and has filed a supplemental statement on the issue.

ing, of course, that in the next century the Congress may prefer to raise the money in some other way and that, in fact, such a rate increase would not be allowed to go into effect unless estimates at the time of the scheduled increase showed that it would be needed.

An increase of less than one-half of 1 percent in the contribution rates in all probability would not mean an increase in the burden of supporting OASDI because: (1) By 2010 real wages are likely to be substantially higher than they are now; and, (2) although levied at a higher rate, the rate will apply to a smaller portion of total compensation than today if the expansion of non-taxable fringe benefits projected in the estimates actually occurs. (If such expansion fails to materialize the contribution rate increase would be unnecessary.)

In contrast to our plan for meeting the part of the long-range deficit not addressed by the compromise agreement, some members of the Commission seek to meet the remaining deficit by raising the age at which full benefits are first payable and then continuing to raise the age automatically in relation to improvements in longevity. This proposal is a benefit cut. If the age is raised to 68, benefits would be reduced by 20 percent relative to those received at age 65; it it is raised to age 67, the cut is 13 percent; and if set at age 66, the cut is 7 percent.

The cut would be concentrated on those unable to work up to the newly set higher age and on those unable to find jobs. It would cut protection for those now young, the very group being asked to pay in more and for a longer period of time. And an automatic provision changing the age of first eligibility for full benefits would make it very difficult for people to paln for retirement. It would also greatly complicate private pension planning. In our opinion it is unwise to try to index social security for all possible future changes in society. Social security has enough indexing. Congress can act to make future changes in the long-run future as needed.

We favor the maintenance of the full range of retirement options in present law so that the program will be responsive to the great variety of occupations in the American economy and to the great variety of individual circumstances. It is one thing, for example, to consider a higher age of first eligibility for full benefits for white collar workers; something else again for those required to do heavy work. The system today has the required flexibility. It provides: (1) full benefits at any age for qualified workers who have long-continued total disability, (2) actuarially reduced benefits for those who apply between ages 62 and 65, (3) higher benefits for those who postpone retirement and continue to work between 65 and 70 (3 percent a year additional benefits under present law, to be raised to 8 percent during the 1990's under the Commission recommendations).

Some have argued for raising the age at which full benefits are first payable on the ground that as life expectancy increases, so will the ability to work. However, two leading Government authorities on health and the aging testified before the Commission that data on increased longevity carry no evidence that health improved commensurately. If anything, they said, what evidence there is indicates the contrary; more people living longer, but with more chronic illness and impairments. Moreover, recent increases in longevity may be related to retirement at earlier ages.

It is, of course, highly uncertain what the economy and the labor market will look like in the next century. Two major possibilities exist. A labor shortage may result from projected shrinkage of the proportion of persons in the 20 to 64 age group.[2] In that event, greater market demand for the services of older people would produce greater paid-work opportunities for them. Employers would be seeking older people and the benefit increase for work after 65 recommended by the Commission would encourage older people to work. If, on the other hand, a labor shortage does not materialize, raising the age of first eligibility for full social security benefits would force a large number of elderly persons into early retirement with lower benefits than current law provides.

We should not cut benefits in an attempt to keep older persons at work. Instead we should recognize and remove the impediments that stand between older workers and employment. Most important of all, economic arrangements should favor full employment and, then, the voluntary approach—the incentives prepared by the Commission—will have a change to work. Social security benefits are not so large as to cancel the lure of good wages. The best medicine for social social security is full employment and economic growth, not benefit cuts.

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[2] A labor shortage would result only if the relative reduction in the working age population were not offset by productivity improvements.

MEETING PROBLEMS OF SPECIAL CONCERN TO WOMEN

Since enactment of the Civil Rights Act of 1964, Federal law has sought to prevent and redress unequal treatment of women. Despite those efforts, substantial inequalities persist and much remains to be done.

In general, gender-based discrimination has been eliminated from the OASDI program through legislative change and court decisions, but in recent years there has been a growing concern regarding the extent to which the social security system has adapted to the changed roles of women in society and the economy. The labor force participation rate for married women has almost doubled in the last 25 years. Over 65 percent of all women aged 20 to 54 are now in the labor force. In addition, the divorce rate has increased significantly. Two decades ago, there was one divorce for every four marriages; in 1976 that rate had risen to one divorce for every two marriages.

Although the scope and urgency of economic considerations appropriately consumed most of the time of the Commission, it did give attention to some of the problems that currently exist for women in social security coverage. Four specific recommendations were made for important changes affecting certain groups of widows, divorced women, and disabled women.

Social Security has indeed given extensive protection to women and men. It provides benefits for 91 percent of women over 65 today (compared to 10 percent of women who received benefits from a private pension system in 1980). Nevertheless, the significant changes in women's roles in society and the economy have caused many inequities and unintended results for women beneficiaries.

Today, the majority (65 percent) of working age women are in the labor force; yet their benefits may be greatly reduced if they leave the labor force for a period of time for homemaking or child-caring. Also lower family retirement and survivor benefits exist for two wage-earner couples than for one wage-earner couples with the same family-earnings history (although there are some advantages to having benefits based on one's own earnings that are partly offsetting).

Homemakers have no individual coverage or eligibility to Social Security and no credits of their own on which to build with later employment because of early widowhood or any other reason. Divorced women may be severely affected by the arbitrary 10-year duration-of-marriage requirement and the inadequacy of the 50 percent dependent benefit for their independent economic needs. Currently, the benefit for the divorced woman depends upon the actual retirement of the former spouse; however, the Commission has recommended a change which will correct this problem. Disability protection exists only for women who remain quite continuously in the labor force and not at all for homemakers. It is often lost to working women during a period of time spent in the home.

Since the introduction in 1976 by Representative Martha Keys and Representative Don Fraser of legislation to implement the concept of earnings sharing, many have believed this to be the best solution to these anomalies. Earnings sharing is a recognition of marriage as an economnic partnership with equal respect given to the division of labor chosen by each couple. It accords the right of each individual to a retirement income based on half of the total retirement credits earned by the couple during their marriage. This is similar in concept to the sharing of income in the joint tax return of a married couple. Working women would have a continuous record of social security credits when they retire instead of zero credits for years spent in the home. It would respond to, and recognize, the economic value to the couple of full-time work in the home by either spouse.

Earnings sharing has been proposed in many forms and was recommended for consideration by both the 1979 Advisory Council on Social Security and the 1980 President's Commission on Pension Policy. Obviously, such a comprehensive change in structure requires careful development of a detailed proposal and thorough analysis of its impact. There are many technical and administrative questions to be worked out and special consideration must be given to continued strong protection for the family against death or disablement of its primary wage-earner. These are not insurmountable problems, however. We believe that earnings sharing is the most promising approach to the solution of Social Security problems of special concern to women and we urge renewed efforts to develop a comprehensive proposal based on this concept.

[Attachment No. 2]

TABLE A.—SHORT-RANGE AND LONG-RANGE COST ANALYSIS OF OASDI PROPOSALS

Proposal	Short-term savings, 1983–89 (billions)	Long-range savings (percentage of payroll)
Cover nonprofit and new Federal employees [3]	+$20	+.30
Prohibit withdrawal of State and local government employees	+3	
Taxation of benefits for higher-income persons	+30	+.60
Shift COLA's to calendar year basis	+40	+.27
Eliminate windfall benefits for persons with pensions from noncovered employment	+.2	+.01
Continue benefits on remarriage for disabled widow(er)s and for divorced widow(er)s	.1	
Index deferred widow(er)'s benefits based on wages (instead of CPI)	.2	.05
Permit divorced aged spouse to receive benefits when husband is eligible to receive benefits	.1	.01
Increase benefit rate for disabled widow(er)s aged 50 to 59 to 71½ percent of primary benefit	1	.01
Revise tax-rate schedule	+40	+.02
Revise tax basis for self-employed	+18	+.19
Reallocate OASDI tax rate between OASI and DI		
Allow interfund borrowing from HI by OASDI		
Credit the OASDI Trust Funds, by a lumpsum payment for cost of gratuitous military service wage credits and past unnegotiated checks	+18	
Base automatic benefit increases on lower of CPI or wage increases after 1987 if fund ratio is under 20 percent, with catch-up if fund ratio exceeds 32 percent		
Increase delayed retirement credit from 3 percent per year to 8 percent, beginning in 1990 and reaching 8 percent in 2010		[1].10
Additional long-range changes [2]		+.58
Total effect	+168	+1.80

[1] This cost estimate assumes that retirement patterns would be only slightly affected by this change. If this change does result in significant changes in retirement behavior over time, the cost increase would be less (or possibly even a small savings could result).

[2] Alternate methods for obtaining this long-range savings are presented in these additional statements of the members (in chapter 4).

[3] Includes effect of revised tax schedule.

Note.—See text for complete description of the proposals.

The CHAIRMAN. Let's proceed with testimony from Mary Fuller, then Martha Keys, then Sandy Trowbridge and Joe Waggoner.

STATEMENT OF MARY FALVEY FULLER, MANAGEMENT CONSULTANT, SAN FRANCISCO, CALIF.

Ms. FULLER. Thank you, Mr. Chairman.

I also feel that a lot of the points upon which I have opinions will come up in the questioning period. But I would like to address two general points now, by way of overall perspective before we move to the questions.

One is the issue that has been raised earlier in some of your colleagues' comments about balance, and that is the balance between relying on added revenues and taxes as well as relying on the restraint in the growth of benefits.

Clearly, the effort that we went through to arrive at a compromise was centered on that—that was the crux of the whole discussion—and all of us had individual opinions on what constitutes a fair balance.

I think, in the interest of the pressure on jobs, the pressure on employment, the pressure on the income of most individuals during this time, the package contains many provisions that will increase taxes but defer their effects to eliminate undue pressure in the very short run. These were felt to be necessary because of the need to get a compromise that would be enacted by the Congress in time to avoid an emergency infusion of general revenues at the last moment or a delay in the benefit checks, both of which would be worse than whatever compromise we could come up with.

I would say, though, that in light of the fact that there is such a heavy reliance on added revenues and new taxes in this package, that we should make sure in these deliberations that proceed with respect to the long term, with respect to the filling of that .58 percent of payroll, that we give serious consideration, and I would advocate personally very strongly, for the increase in the normal retirement age. I think that this would be an added element of the package that would really add to its credibility and to its balance in the eyes of the young people who are looking forward to a system that we are assuring them will be in place for them later, and in the eyes of rational people who are looking at the fact that the increase in longevity is self-evident.

In fact, if you take the proportion of a working person's life that the age 65 represented when it was enacted in 1939 and extrapolate that to the year 2015, which is the year we are talking about for a phased-in increase in the retirement age, that same proportion would result in a retirement age of 71. Splitting the difference between the retiree and the worker would result in a retirement age of 68.

The provision in the package that the majority of the Commission recommends, to increase it gradually to 66, would appear to be a very reasonable step in this direction. And I feel it's a very important one, so that what emerges will be a truly balanced solution.

The second point I would like to make has to do with the issues affecting women, which may or may not otherwise come up in the questioning, because this clearly could not be a top priority for the Commission in view of the serious liquidity problems that the system faces.

The problems affecting women really arise because of the changed roles of women in the work force, not because of any intended discrimination, ever, in the social security program.

The social security program was enacted at a time when most families consisted of one wage earner, usually the man, and one dependent spouse, usually the woman. Marriages were for the most part lifelong, and most people were married. Therefore, the system that has the benefits for a woman calculated as the function of her role as a dependent spouse was very appropriate during that time when that was the model of the family.

Today, with the substantial majority of women spending a majority of their lives in the paid work force, with a substantially higher divorce rate of which two-thirds of the divorces occur before 10 years of marriage, we now have some effects that disadvantage several elements of the work force.

The secondary earner, who is primarily but not necessarily the woman, but in most cases today still is, unless she earns more than one-third of the total family income her benefit as a worker is no greater than her benefit as a dependent, which means she gets no return for those social security taxes she paid during her working life. She does get disability protection as a worker, which she would not get as a dependent; but most people seriously question whether that provision justifies all the taxes she has paid.

Second, two-earner couples with the same earnings get less in benefits than one-earner couples.

Third, single people with the same earnings get less benefits than a married person with those earnings.

And finally, if a divorced spouse has been married less than 10 years she gets no benefits at all.

These things should be addressed at some point. I feel that, while obviously it would not be appropriate to put particular legislation into this package that would take effect immediately, I think the concept of earnings-sharing which is one based on the precedent of community property, where each member of a couple gets credit for half the total earnings of that couple throughout the life of that marriage, I think this concept can be worked into a program that would be of minimum cost, reasonable transition, and workable.

I think that in order to get something like this to happen, though, it is appropriate to get dialog during the course of all legislation affecting social security soon, because this kind of a program takes a while to create and to define and to design, with respect to provisions and with respect to transition.

So I urge that if it is possible in the course of your debate that you address this and that you give some consideration to earnings-sharing as a solution and give some kind of impetus to continuation of work on this problem so that it can be resolved until a solution that can be in effect before the end of this decade.

Thank you.

The CHAIRMAN. Thank you.

Ms. Keys.

STATEMENT OF HON. MARTHA E. KEYS, DIRECTOR, EDUCATIONAL PROGRAMS, THE ASSOCIATION OF FORMER MEMBERS OF CONGRESS, WASHINGTON, D.C., AND FORMER MEMBER OF CONGRESS

Ms. KEYS. Thank you, Mr. Chairman.

Members of the committee, it's nice to see some of my former colleagues on the House side who have moved across the Capitol.

I will not belabor the points that I am delighted Mary has already made so well, but I would like to speak just a little bit additionally about the context of the four recommendations made by our Commission.

Obviously, as one who introduced legislation for equity in social security back in 1976, I have been working on this issue a long time.

I think it is important that we let people know that the four specific recommendations made by the Commission at this difficult time do not begin to address the major problems that exist of largely unintended consequences on women beneficiaries. Quite appropriately we spent the majority of our time dealing with the immediate and tremendous financial and economic problems for social security. Nevertheless I think the entire Commission were greatly concerned about this whole area of problems.

It is important to recognize that although the Commission didn't have time to spend on the broad scope of these problems, they recognized the importance and agreed unanimously that at least we could make four changes, two of which are primarily technical, two of which are very important new changes affecting equity and also affecting adequacy of a small group of women beneficiaries.

They are important changes to the women they affect, and they are changes that were undertaken in this particular recommendation because they did not require a great deal of extra cost, and also they were targeted very carefully toward some severe problems for small groups of women.

I believe that all individuals in America—because indeed these unintended consequences for women beneficiaries affect not only them but those related to them—spouse or children should take a great deal of heart that the Commission, both in its report and in the supplementary statements, recognized the absolute importance of this being addressed very quickly.

I would ask, Mr. Chairman, that my testimony be introduced into the record. I do have a good bit more information in there, and I would only like to say further that I think we have before us, between now and 1990, the ideal time for this committee—and I know, Mr. Chairman, that you are a strong supporter and have been very influential in this particular area—and for the Ways and Means Committee of the House, and for the Social Security Administration, to face up to the kind of comprehensive change that will solve this problem.

It would be ideal for this change to be implemented beginning in 1990 when the system is not under severe financial pressures.

It's a change caused by sociological change in our society, and it is of equal importance in this system that serves so many of our people, but it can't be made at a time when there are strong financial pressures.

I feel that it is in good hands with your leadership—all of you on this committee and the Ways and Means Committee in the House—and with the very strong statements and recommendations and discussion that have come from other members of this Commission.

So, thank you.

The CHAIRMAN. Thank you very much. Your statement will be made a part of the record.

[The prepared statement of Ms. Keys follows:]

STATEMENT OF MARTHA KEYS, MEMBER, NATIONAL COMMISSION ON SOCIAL SECURITY REFORM

Thank you for the opportunity of presenting testimony to the Committee regarding Social Security. I am pleased to have been a member of the National Commission on Social Security Reform, which has spent a great deal of time during the past 13 months examining the current status of Social Security and needed changes in the immediate and long-term future.

I want to express my support for the report of the Commission and its recommendations. It is my belief that the recommendations were achieved after fair consideration of the interests of today's retirees, workers and employers and tomorrow's retirees, workers and employers. The major components are:

* Extension of coverage to all non-profit employees and newly hired federal employees.

* Acceleration of the present OASDI tax rate for 1985 to 1984 with a complete offset of the increased tax burden through a refundable tax credit.

* Acceleration of a portion of the present OASDI tax rate for 1990 to 1988.

* Fair reimbursement to the system for coverage of self-employed persons by increasing their contribution from 1½ times the employee rate (with no business expense allowance) to 2 times the employee rate with ½ of the contribution treated as a business expense.

* Recapturing a portion of the benefits paid to retirees with significant amounts of other income -- more than $20,000 for an individual and $25,000 for a couple -- by requiring ½ of their Social Security benefits to be included in taxable income.

* Shifting COLAs to a calendar-year basis, thus delaying in 1983 the payment of the COLA for 6 months.

It is clear that no one of these recommendations by itself would have received majority support of the Commission. Taken together, they constitute a carefully balanced solution to both the short-term financing problem and most of the long-term shortfall, by requiring some sharing by all in the solution. Most important, they preserve the basic tenets of the system, restore its financial strength and reiterate its importance to the American people as a society.

I will not comment on each of the recommendations, but of course, will be happy to respond to questions about them. Instead, I will spend most of this time discussing the problems of many women beneficiaries with respect to Social Security and addressing four specific recommendations made by the Commission.

Because of the scope and urgency of the economic considerations facing Social Security, most of the time of the Commission was quite appropriately consumed addressing these important issues. The assurance of appropriate revenues for the difficult 7-year period ahead is of utmost importance to all current beneficiaries, 19 million women, 13 million men, and 3 million children. Time was not available for full consideration by the Commission of the many problems, and unintended consequences for women beneficiaries, of Social Security. The Commission report and additional supplementary statements express the Commissioners' regrets regarding this omission.

Social Security has indeed given extensive protection to women and men. It currently provides benefits for 91% of women over 65 (compared to private pensions which pay benefits to only

10% of women over 65). Of those persons presently receiving Social Security, 54% are women, 37% are men and 9% are children. The weighted benefit formula has been especially helpful to women because of their generally lower earnings. However, there has been growing concern in recent years regarding adaptation of the Social Security system to the changed roles of women in society and the economy.

The labor force participation rate by married women has almost doubled in the last 25 years. Over 65% of all women aged 20 to 54 are now in the labor force. In addition, the divorce rate has increased significantly. Two decades ago, there was one divorce for every four marriages; in 1976 that rate had risen to one divorce for every two marriages.

Although the majority of working age women are in the labor force, many will receive low returns on their contributions to Social Security because they leave the labor force for periods of full-time homemaking or child-caring. The resultant zero years of earnings will lower the benefits of many so much that the 50% dependent benefit for a spouse will be higher than the benefits based on her own earnings record. In 1979, 2.4 million women found that their vested contributions to Social Security brought them no more retirement benefits than they would have received as non-working spouses. In addition, under the current system, a two wage-earner couple receives lower family retirement and survivor benefits than a one wage-earner couple with the same family earnings and contribution history.

Other problems exist for women under Social Security. Homemakers have no individual coverage or eligibility to Social Security and no credits of their own on which to build with later employment occasioned by early widowhood or other reasons. Divorced women are severely affected by the arbitrary 10-year duration-of-marriage requirement and the inadequacy of the 50% dependent benefit for their independent economic needs. Currently, the benefit for the divorced woman depends upon the actual retirement of the former spouse; however, the Commission has recommended a change which will eliminate this problem. Disability protection exists only for women who remain quite continuously in the labor force and not at all for homemakers. It is often lost to working women during periods of time spent in the home.

Since 1976, when Representative Don Fraser and I introduced legislation to implement the concept of earnings sharing under Social Security, I have strongly believed this to be the best solution to these anomalies. Earnings sharing is recognition of marriage as an economic partnershiup with equal respect given to the division of labor chosen by each couple. It accords the right of each individual to a retirement income based on half of the total retirement credits earned by the couple during their marriage. This is much the same as the sharing of income in the joint tax return of a married couple. Working women would have a continuous record of Social Security credits when they retire instead of zero credits for years spent working in the home. Such a record would respond to, and recognize, the economic value to the couple of full-time work in the home by either spouse.

Earnings sharing has been proposed in many forms and was recommended in some form by both the 1979 Advisory Council on Social Security and the 1980 President's Commission on Pension Policy. Obviously, such a comprehensive change in structure requires careful development of a detailed proposal and thorough analysis of its impact. There are many technical and administrative questions to be worked out and special consideration must be given to continued strong protection for the family against death or disablement of its primary wage-earner. These are not insurmountable problems, however; indeed they are legislative and administrative details. They should be given concentrated attention by this committee and the Social Security Administration in the immediate future.

A comprehensive structural change must be implemented with a transition period and should be accomplished at a time when there is not serious financial pressure on the system. Thus, 1990 is an ideal time for such a transition period to begin.

The Commission made four specific recommendations to address certain severe problems for specific, small groups of beneficiaries. Although the impact of these recommendations is small in terms of numbers, they are important changes for those women affected. The are:

1. Continued benefits for certain widow(er)s who remarry. Prior to the Social Security Act Amendment of 1977, the remarriage of a surviving spouse terminated benefits based on the deceased spouse's record, and allowed only a wife's (50%) benefit based on the present spouse's record. Effective January, 1979,

the situation changed for some surviving spouses. The 1977 amendments provided that remarriage of a currently entitled widow(er), age 60 or over, would not terminate benefits. The final version of the legislation did not (as the House bill had) include a similar provision for divorced surviving spouses and disabled surviving spouses.

The National Commission recommends that remarriage not terminate existing benefits for divorced surviving spouses and disabled surviving spouses who remarry. There is no data presently available regarding the number of beneficiaries affected.

The proposal is estimated to cost $100 million in the short-term and to be negligible in the long-term (less than .005 percent of payroll).

2. Independent benefits for divorced spouses. Under current law, a divorced woman must wait until her husband retires to receive a benefit. If the former spouse continues to work, his earnings can reduce or terminate her benefit although they no longer live in the same household.

The Commission recommends that spouse benefits for divorced spouses be payable when the divorced spouse reaches age 62 (the age at which eligibility for such benefits normally begins), if the former spouse is otherwise eligible for benefits, whether or not he has actually claimed benefits and regardless of the level of his earnings.

The Commission report adds the suggestion that there be a requirement that the divorce have occured a significant period before retirement age. I do not share the view, upon which this suggestion apparently rests, that the provison would be an incentive to divorce. However, if the suggestion is adopted, the period should be no longer than one year so as not to impose a hardship on those who are legitimately attempting to finance two households. The cost of the provision would be minimal, approximately $100 million in the short-term and .01 percent of payroll in the long-term.

There are presently 46,000 divorced spouses receiving benefits and 1,600 receiving reduced benefits because of earnings of the former spouse. There is no data regarding the number completely ineligible because the former spouse has not applied for benefits.

3. <u>Indexation of deferred widow(er)s benefits</u>. The Commission recommends that the wage-record of a spouse, who dies before the widow(er) is old enough to receive benefits, be indexed according to the increases in wages that occurred between the time of the death of the worker and the beginning of benefits to the surviving spouse. This is essentially a technical provision more important for future years of normal economic expectations regarding wage increases.

4. <u>Disabled widow(er)s benefit</u>. Under current law, reduced benefits for surviving spouses without dependent children are available at age 60-64 in the amount of 71.5% of the Primary Insurance Amount. Benefits are 100% of the PIA for surviving spouses collecting benefits at age 65 or over. Disabled widow(er)s are eligible for reduced benefits at age 50-59 in the amount of 50% of the PIA.

The National Commission recommends that the benefits rate for disabled widow(er)s age 50-59 should be the same as those for non-disabled widow(er)s at age 60 -- 71.5% of PIA.

This proposal would cost $1 billion in the short-term but would represent a modest cost of .01% of payroll in the long-term.

There are currently 113,000 disabled widows receiving benefits and 1,000 disabled widowers. Approximately, 29% of these are between the ages of 50-54 and 55% are between the ages of 55-59. Thus, the benefits would be raised for approximately 84% of these current beneficiaries.

These changes were recommended by the Commission because they clearly address the equity or adequacy of certain -- primarily women -- beneficiaries with severe problems. I hope that it is clear to members of the Committee, as it was to members of the Commission, that these changes do not begin to address the wide range of equity and adequacy problems for women beneficiaries. I believe that the members of this Committee will carry out that responsibility.

The CHAIRMAN. Mr. Trowbridge.

STATEMENT OF ALEXANDER B. TROWBRIDGE, PRESIDENT, NATIONAL ASSOCIATION OF MANUFACTURERS, WASHINGTON, D.C.

Mr. TROWBRIDGE. Thank you, Mr. Chairman.

I am Sandy Trowbridge, a member of the National Commission, appearing as an individual and also in my role as president of the National Association of Manufacturers, which I am pleased to report to you has looked at the recommendations of the Commission and in a very searching analysis has come to the conclusion that they deserve the full support of our organization.

This Commission had a remarkable makeup. I think we who are the noncongressional members owe a real vote of thanks to those who were congressional members of the Commission, serving from both the Senate—and four members of this committee did so extremely ably—and the House. I think that the mixture of persons with great knowledge of the issues and of the political realities, plus the members who were from the civilian side of the House, so to speak, was a remarkably good combination and was part of the reason why we were able to come to a consensus.

That consensus is one in which, obviously, not every one is satisfied with every aspect. There are parts of it which, as Senator Wallop described, if each were King Arthur we would design it in particularly different ways.

But, if I may, I would like to put into the record not only my statement but read the resolution of the board of directors of the NAM, which sums up our feeling toward this package:

In view of the overriding importance of assuring the continuation of a responsible Social Security program, the National Association of Manufacturers supports the package of recommendations of the National Commission, an essential part of which is to close the long-term funding gap through measures to control the growth of benefit payments. NAM strongly urges the adoption of this package by the Congress, recognizing that these recommendations represent a compromise, and in some respects, particularly those involving increased taxation, the recommendations contain elements inconsistent with NAM policy.

I would like to just briefly highlight two other points, Mr. Chairman. One is the portion of the Commission's recommendations dealing with the inclusion of new hires of Federal civil servants coming into service after January 1 next year.

I think here in Washington, and certainly around the country—there have been just innumerable messages in opposition to this recommendation, many of which I think have been very sweeping and basically erroneous in their claims.

I think you will recall that one of the earliest decisions which the Commission made in its meeting in Alexandria last November was not only that the social security problem was a real one and that it had definable dimensions and a target that we should all aim to solve, but that the inclusion of Federal employees as part of the social security system was one with which almost all of us, with the stated exception of Mr. Kirkland, felt we should begin our agreement.

Indeed at that time we were talking of a group of employees with 5 years or less of service who had not vested in the civil service retirement system. For assorted reasons, between that meeting in November of last year and our final report, we reduced the recommendation to cover only new hires on the belief that the legal and logistical difficulties of combining Federal employees with accredited, though nonvested, service into the social security system would be very difficult.

But consistently from the beginning we did urge that this be part of our package, and I think we should deal with the charges and the complaints.

One very effective document that I think has a very useful part to play in this is a memorandum which was prepared on January 31 by the very able Executive Director of the staff of the Commission, Mr. Robert J. Myers, regarding the controversy over our recommendation to cover new Federal hires. I have attached that, Mr. Chairman, to my testimony with the hope that it can be inserted in the record, because I think it does summarize the charges, and it certainly summarizes the basic proposal and why it should be implemented.

The CHAIRMAN. It will be made a part of the record.

Mr. TROWBRIDGE. Thank you, sir.

The only other point I would make would be on the question of the long-term gap, that portion of the Commission's recommendations which did not come under the 12-to-3 vote but which a majority of the Commission members did support, and that is the closing of the roughly one-half of 1 percent of long-term payroll.

In this case I voted with the majority of the Commissioners to alleviate the fiscal imbalance through a gradual increase in the age of first eligibility for full benefits from 65 to 66, beginning after the year 2000.

There are a number of reasons, Mr. Chairman, for supporting this. We can get into them if you wish in the question period.

I do have available for review, if the committee wishes, a survey of pension plan sponsors which was conducted by the CIGNA Corp., and the Employee Benefit Research Institute, which reveals that most plan sponsors support older workers staying active longer. And the majority felt that a legislated increase in the normal retirement age was an appropriate mechanism to achieve this result.

So I think there is growing support for that particular option. I would hope that it emerges as part of the full congressional approval of what is essentially a consensus package from this Commission, with a choice for closing the long-term payroll gap, that deals either with an increased payroll tax or an extension of the retirement age some number of years in advance, so that the people affected can have adequate warning and plan for their futures under new rules which hopefully will apply.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Trowbridge and the January 31 memorandum by Mr. Myers follow:]

Statement of Alexander B. Trowbridge, President, National Association of Manufacturers

Mr. Chairman and members of the Senate Finance Committee, I am Alexander Trowbridge, and I am President of the National Association of Manufacturers. Today I am appearing as a former member of the National Commission on Social Security Reform, and as an individual. In addition, I am most pleased to report that our relevant policy committees and our NAM Board of Directors have recently given their full support to the Commission's recommendations.

I wish to take this opportunity to commend this Committee, and especially the four members who served on the National Commission, for your leadership in seeking solutions to the financing problems of the Social Security system. I am sure that much remains to be accomplished in this difficult, but vital task. After the National Commission struggled long and hard over the past year with this issue, it's efforts deserve our support, and we at NAM look forward to working with this Committee and the Congress in the passage of appropriate legislation.

The consensus recommendations represent a reasonable proposal for assuring the financial viability of the Social Security program. For this reason I have joined the other Commissioners in supporting that compromise package. The recent endorsement by the NAM Board of Directors is noted in the following resolution:

"In view of the overriding importance of assuring the continuation of a responsible Social Security program, the National Association of Manufcturers supports the package of recommendations of the National Commission, an essential part of which is to close the long-term funding gap through measures to control the growth of benefit payments. NAM strongly urges the adoption of this package by the Congress, recognizing that these recommendations represent a compromise, and in some respects, particularly those involving increased taxation, the recommendations contain elements inconsistent with NAM policy."

In the remainder of my statement, I wish to briefly address two aspects of the National Commission's recommendations. Firstly, the Commission's consensus recommendation to include newly hired federal civil servants under Social Security after January 1, 1984; and secondly, the options to close the long-term funding gap which were outlined by the Commission but not included as part of the consensus recommendation.

Coverage of Federal Employees

Since the Commission issued its recommendations regarding coverage of new federal employees, we in Washington and citizens across the land have been bombarded with media advertisements condemning the idea of including federal civil servants. The attacks have been sweeping in their claims, and I believe they need a solid rebuttal.

It should be noted that one of the earliest decisions of the Commission, taken at our November meeting in Alexandria, Virginia, dealt with the definition and the scope of the Social Security funding problem, and also with the extension of coverage to non-profit organization employees and federal civil servants.

In fact, by a non-roll call consensus vote, the Commission members at that point were in favor of including all federal employees with less than five years of service -- with the stated exception of Mr. Kirkland. It was only sometime later that we reduced the recommendation to cover only new hires, on the belief that the legal and logistical difficulties of combining federal employees with credited (though non-vested) service with Social Security would be very difficult. In short, the Commission saw merit in extended coverage early in our search for a consensus, and that element never was withdrawn as the package was developed.

For the record, Mr. Chairman, I would like to submit a copy of a memo dated January 31, 1983, prepared by Mr. Robert J. Myers, who served as an extraordinarily able and dedicated director of the Commission's staff, dealing with the charges made by the opponents of extended coverage. I can summarize the charges, and the rebuttal, briefly for the Committee:

<u>Charge</u>: <u>Civil Service Retirement will be bankrupted because it will have no new entrants</u>:

The proposal would not substitute Social Security for CSR, nor would the system be merged, but rather a supplemental CSR program would be developed just as has been done in private industry. It is quite likely that, under the <u>total</u> retirement system for new hires, the total contribution rate for employees and for the employing agencies would remain the same as it is for present employees--namely, now 7%, plus the Hospital Insurance contribution rate and that the excess of the 7% rate over the OASDI rates would go into the CSR Fund.

Charge: Social Security will gain only over the short run, but will lose over the long run, due to the additional benefit liabilities created. Social Security coverage of Federal employees would give sizable cash-flow income to the Social Security program in the short range. Over the long run, such action would be favorable to its financing--not unfavorable. A significant long-range savings to the Social Security program is estimated to result--about 0.3% of taxable payroll, on the average, over the 75-year valuation period, according to the estimates of the Social Security Administration actuaries.

Charge: New hires will have only Social Security benefits, and these are not nearly as good as CSR ones. It has never been proposed that CSR would be completely eliminated, and only Social Security benefits be available. Rather, an independent, supplementary CSR plan would be developed--just as is done in the private sector and many employees such as short-service workers, would be better off under such a plan.

Charge: Taxpayers will have higher costs under the proposal. Much will depend upon the nature of the independent supplementary plan. Certainly, it is not the case for the reason sometimes given that the unfunded liability would have to be paid at once.

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Closing the Balance of the Long-Term Gap

The consensus recommendations of the Comission would close only two-thirds of the long-term gap of 1.82% of payroll. In consideration of this issue, I voted with a majority of the Commissioners to alleviate this fiscal imbalance through a gradual increase in the age of first eligibility for full benefits from 65 to 66 beginning after the year 2000.

I supported this specific recommendation for a number of reasons:

First, this proposal represents a demographic solution to a demographic problem. People will be living longer and should not pose a greater financial burden on the generation supporting their benefits than was placed upon them by the generation of retirees that they supported. Currently, 3.2 workers support each beneficiary. Once the Baby Boom generation retires, the "best estimate" is that there will be only about two workers to support each beneficiary. If those projections are modified to reflect continuation of current birth rates, as has been done by the Census Bureau, even fewer workers than expected will actually be supporting each beneficiary.

Second, the ability of senior citizens to continue working has increased. Certainly the demands of certain occupations may continue to make earlier retirement both desirable and necessary in some cases. However, the current 65-year old will live longer and will be potentially far more productive than his or her parent. A similar trend with his or her child's longevity and potential productivity may also hold.

Finally, attitudes toward senior citizens in the workplace have changed. A recent survey of pension plan sponsors conducted by CIGNA Corporation, an NAM member company, and the Employee Benefit Research Institute revealed that most plan sponsors support older workers staying active longer. A majority felt that a legislated increase in the normal retirement age was an appropriate mechanism to achieve this result. In the absence of any cost considerations most would have preferred using positive incentives, but the survey responses do demonstrate the positive and realistic approach to the Social Security problem which is the essential feature that will make its solution possible.

Legislating a gradual increase in the age of first eligibility for full benefits now would give individuals sufficient time to plan for their retirement. Such responsible action by Congress will assure the long-term as well as short-term health of Social Security. In all fairness to today's taxpayers, the needed structural reforms must be made today so that that the System will be available for them tomorrow.

Conclusion

In closing, I urge you to adopt the Commission's proposal to restore Social Security's immediate financial health and to close the remaining part of the long-term gap by changing gradually the retirement age as recommended by myself and a majority of the Commissioners.

A failure by Congress to enact the consensus package will have serious implications for the viability of the program and for the nation's overall fiscal integrity as well.

Thank you for this opportunity to present testimony on preserving the integrity of the Social Security program. I, as well as the members and staff of the National Association of Manufacturers, look forward to working constructively with this Committee and the Congress on this and the other critical issues affecting our nation's economic recovery.

NATIONAL COMMISSION ON SOCIAL SECURITY REFORM
736 JACKSON PLACE, N.W.
WASHINGTON, D.C. 20503

January 31, 1983

MEMORANDUM

TO: Members of the National Commission on Social Security Reform

FROM: Robert J. Myers
Executive Director

SUBJECT: Controversy Over Our Recommendation to Cover New Federal Hires

As you well know, several groups of Federal employees have mounted a strong campaign against our recommendation to cover new Federal hires under Social Security.

This campaign is based on several significant factual inaccuracies -- such as that it will bankrupt the present Civil Service Retirement system within a few years, that it will cost the Federal Government vast sums of money, and that it will cost the Social Security program more money over the long run, despite short-term cash-flow gains. None of these assertions are true. The attached memorandum analyzes the situation in detail.

Robert J. Myers

Attachment

RJM:ejd

NATIONAL COMMISSION ON SOCIAL SECURITY REFORM
736 JACKSON PLACE, N.W.
WASHINGTON, D.C. 20503

January 31, 1983

GENERAL MEMORANDUM

FROM: Robert J. Myers
Executive Director

SUBJECT: How Would the Financing of the Civil Service Retirement System be Affected by the National Commission Proposal

The National Commission has recommended that all Federal emplyees hired after 1983 should be covered under the Social Security program and that an independent, supplementary Civil Service Retirement (CSR) plan should be developed for these individuals. This would be exactly the same general procedure that is followed in the private sector and in much of the state-and-local-government sector.

Criticisms of Proposal of National Commission

A number of Federal-employee organizations have criticized this proposal, on several grounds. I do not believe that their criticisms are valid, however. I will consider each of the recently-heard arguments against this proposal and either point out the flaws or show that the recommended procedure is consistent with generally accepted pension-funding principles, particularly those that have been used over the years in analyzing and valuing the CSR system.

The principles of such criticisms are as follows:

(1) It has been claimed that covering all new hires under Social Security will bankrupt the Civil Service Retirement system, because there will be a decreasing group of active workers on whose salaries contributions will be paid by them and by the Government.

(2) It has been asserted that the Social Security system will have only short-term cash-flow gains, and the additional benefit liabilities created will put it in a worse position in the long run.

NOTE: Any views expressed in this memorandum are those of the author, and not necessarily those of the National Commission. However, any factual statements are completely objective and completely accurate.

(3) Some allege that new hires will be worse off, because they will have only Social Security benefits.

(4) Some claim that the Government -- and thus the general taxpayers -- will have higher costs, because they will be required, more or less immediately, to "pay off" the unfunded accrued liability of CSR (at least about $200 billion, but as much as $500 billion under some funding bases). Also, the Government will have reduced income-tax receipts, because a larger proportion of CSR pensions is taxable than for Social Security benefits.

Before reputing these criticisms, I will first give a general description of the CSR plan, especially as to its financing basis and principles.

<u>General Description of CSR System, Especially its Financial Basis</u>

First, and most importantly, it should be recognized that the CSR Fund is not <u>one</u> single retirement plan. It is a little-known fact that it is composed of a considerable number of plans. For example, it includes a plan for Members of Congress, another plan for congressional employees, another plan for air controllers, another plan for general employees, etc. It also includes a number of "closed" plans, for which there are no current active contributors -- only <u>pensioners</u>. Examples of such "closed" plans are the three separate plans which were prevalent in the mid-1930s, when one applied to persons in generally hazardous work (with a retirement age of 62), another applied to postal employees and blue-collar workers (with a retirement age of 65), and the third applied to general employees (with a retirement age of 70). For all three plans, the benefits formula -- which still applies to pensioners therefrom who are now on the rolls -- is far different from the one applicable to current contributors.

The financing for the CSR Fund is determined on a single aggregate basis for all of the plans considered as a whole including the "closed" plans. Thus, the establishment of a new plan for new hires only within the CSR Fund would not diminish at all the payroll base for purposes of contributions by the Government.

Considering only present general employees, their contribution rate is 7%, their employing agency pays another 7%, and -- although it is not always recognized or known -- the General Fund of the Treasury pays, on the average, over the long run -- an additional amount approximately equal to <u>26% of payroll</u>. It is sometimes erroneously stated that this latter amount of 26% is entirely due to the fact that the Government did not make proper (or any) contributions in past years. This is not the case; only a small part of the 26% arises from such insufficient payments. For further details and explanation of this matter, see the attached paper "How Much Has the Federal Government Contributed to the Civil Service Retirement System?"

This relatively high cost for CSR, amounting in the aggregate to about 40% of payroll is the result of several factors -- (1) the very low retirement ages provided (for general employees, age 55 with 30 years of service; age 60 with 20 years of service; or age 62 with 5 years of service); (2) the relatively high pension rates for long-service employees; and (3) the full indexing of benefits to the CPI.

The basic actuarial-funding basis of CSR, as it will be done in the future, is that the accumulated unfunded liability will never be liquidated. Rather, interest on it will be paid every year into perpetuity (as it has been in the past). This will provide adequate financing at all times, and it is a quite appropriate procedure for a Federal government plan. Such interest will be expressed as a percentage of payroll of the total then-active workforce, even though many of them -- eventually, all of them -- will not have had anything to do with the creation of the unfunded liability itself!

As to the matter of whether CSR is soundly and adequately financed -- which I believe is the case -- this could properly be said to be the case for the long-range future, because the present law provides that the General Fund of the Treasury will pay the balance of the cost over what is met by the 7% employee contributions and the 7% agency contributions! Of course, the Social Security program would also be soundly and adequately financed under the recommendations of the National Commission on Social Security Reform.

Answers to Criticism of Proposal of National Commission

(1) CSR will be bankrupted because it will have no new entrants. The proposal would not place CSR in jeopardy within a few years because "income would stop flowing into the fund", as some assert. The proposal would not substitute Social Security for CSR, nor would the system be "merged", but rather a supplemental CSR program would be developed, just as has been done so successfully in private industry. This supplemental system would be part of the CSR Fund, which now contains several retirement systems. It is quite likely that, under the total retirement system for new hires, the total contribution rate for employees and for the employing agencies would remain the same as it is present employees -- namely, now 7%, plus the Hospital Insurance contribution rate and that the excess of the 7% rate over the OASDI rates would go into the CSR Fund. In addition, the approximately 26% of payroll which now, on the average over the long run, goes into the CSR Fund from the General Fund of the Treasury (or a slightly different determined rate) as an aggregate residual payment to meet the cost of all of the various retirement plans contained in the CSR Fund would continue. Accordingly, no part of, and no separate plan in, the CSR Fund would be endangered.

(2) Social Security will gain only over the short run, but will lose over the long run, due to the additional benefit liabilities created. It is often stated that "Within the last three years SSA has testified before Congress that while coverage of federal employees would help the short-range financing problem, it would only add to the problem in the long-range". I am constrained to say that Deputy Commissioner Robert P. Bynum in testifying to this effect in 1979 before a congressional committee was completely wrong, and he was told so by the actuaries of the Social Security Administration and did not choose, either then or later, to correct his statement.

Social Security coverage of Federal employees would give sizable cash-flow income to the Social Security program in the short range. Over the long run, such action would be favorable to its financing -- not unfavorable. A significant long-range savings to the Social Security program is estimated to result -- about .3% of taxable payroll, on the average, over the 75-year valuation period, according to the estimates of the SSA actuaries. Moreover, despite what leaders of some Federal-employee organizations say, the SSA actuaries have always estimated that there would be a significant long-range savings to the Social Security system if coverage were extended to Federal employees (whether to only new ones or whether to present ones as well).

(3) New hires will have only Social Security benefits, and these are not nearly as good as CSR ones. No responsible group has ever proposed that CSR would be completely eliminated, and only Social Security benefits be available. Rather, an independent, supplementary CSR plan would be developed -- just as is done in the private sector. Many employees would be better off under such a basis, particularly short-service workers (who now have little or no current disability and survivor protection under CSR, and may continue to be in a disadvantageous position for some years after they leave Federal service and enter the private employment sector).

(4) Taxpayers will have higher costs under the proposal. This is not necessarily the case, depending upon the nature of the independent, supplementary plan. Certainly, it is not the case for the reason sometimes given that the unfunded liability would have to be paid off at once. I have demonstrated the fallacy of this criticism and approach in the last paragraph of the previous section.

The criticism that the general taxpayer will suffer because income-tax receipts with respect to the pensions of the "new hires" arising from both the new independent, supplemental plan and Social Security combined will be less than if the total pension were from CSR alone is quite true. However, this is a classic example of "walking on both sides of the street". Federal employees have -- quite rightfully -- been arguing for years that their pension income is unfairly taxed as compared with the (currently) tax-free Social Security benefits (although, in reality about 80% of CSR retirees aged 62 or over are also eligible for at least some tax-free Social Security benefits, based on "outside" employment!). In all logic, that portion of CSR benefits which is equivalent to Social Security benefits, less any actual Social Security benefits received, should be as tax-free as Social Security benefits. Now, some Federal-employee groups are using this inquitable, disadvantageous treatment as though they are being "patriotic" by being mistreated and want to continue to be so treated!

In summary, it really all boils down to the simple fact that, if the Government requires private employers to have Social Security for their employees instead of only a private pension plan (but with such plan being possible, and desirable), then why should it be different for its own employees? This is especially so for employees of the Social Security Administration. It is (or should be) extremely difficult, if not impossible, for an SSA employee to explain to the public what a great program Social Security is and be able then to give an adequate answer to the question, "Well, if Social Security is so great, why aren't you in it?"

Robert J. Myers

Attachment

RJM:ejd

HOW MUCH HAS THE FEDERAL GOVERNMENT CONTRIBUTED TO THE CIVIL SERVICE RETIREMENT SYSTEM?

BY

ROBERT J. MYERS*

Frequently, one hears that the relatively high cost of the Civil Service Retirement system to the General Fund of the Treasury is due to the fact that, for many years, the General Fund did not contribute its appropriate share. This article will consider this matter in some detail -- and especially the allegation that, for many years, the Federal Government did not make any contributions at all to the CSR system.

In FY 1981, the government contribution was $18.2 billion, or about 4½ times the employee contributions of $4.0 billion. It is likely that this ratio -- or possibly even one as high as 5 to 1 -- will occur in future years.

The accompanying table compares the employee contributions with the government contributions to the CSR system for selected fiscal-year periods in

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* Chief Actuary, Social Security Administration, 1947-70; Deputy Commissioner of Social Security, 1981-82; Executive Director, National Commission on Social Security Reform, 1982-83.

the past, going back to when the program first began operations. In the first 8 years, the government did not contribute at all, despite the fact that from the standpoint of sound financing, government contributions should have been made then. However, the total amount of employee contributions then was only $143 million. Thus, if the government had put up an equal amount (or even somewhat more), with accumulated interest over the somewhat more than 50 years, this would not have increased the existing fund balance by more than about $1 billion, or only 1% relatively.

From 1929 through 1969, the government contributions were slightly less than the employee contributions -- by about 10% in the aggregate. Once again, from the standpoint of sound financing, the government contributions should have been larger, but even so, the current fund balance would not have been much higher. In the last 12 years, the picture has changed greatly. The government contributions have been about 3 times as large as the employee contributions -- and, as noted previously, by as much as 4½ times in the last year.

In summary, then, it is true that the Federal Government did not contribute adequately to the CSR system in the first five decades of its operation, but that, recently, quite adequate contributions are being made. If more adequate contributions had been made in the early decades of operation, there would be higher interest income currently, but this would not <u>greatly</u> reduce the cost to the Federal Government, either currently or over the long run.

The average cost of the CSR program over the long-run future is currently estimated to be approximately 40% of payroll. After considering the employee contribution rate of 7%, this leaves a remaining cost to the Federal Government of about 33% of payroll (of which 7% comes directly from the employing agencies through their appropriations, with the remaining 26% coming indirectly from the General Fund of the Treasury). The Board of Actuaries of the CSR system estimates that the normal cost of the program is about 14% of payroll, using static economic assumptions (i.e., assuming -- quite unrealistically, in this real world -- that general wage and price levels do not increase in the future). On the basis of this figure, some people mistakenly believe that, because the employees contribute 7%, the cost to the Federal Government would really be only the remaining 7% if it had contributed properly in the past. This argument is fallacious for several reasons.

First, the normal cost applies only to new entrants. The relatively high cost for persons who came into the system initially at older ages with creditable past service is an appropriate part of the cost of the program and is not explained away by saying that past government contributions were not made.

Second, the interest rate used by the Board of Actuaries in computing the normal cost under the static assumptions is unrealistically high at 5%. Such a real rate of return is most unlikely to be achieved under conditions of no price inflation. Instead, a rate of 1% to 2% should be used under these circumstances, and this would produce a normal cost of about 30-37% of payroll.

In fact, the Office of Personnel Management, using the actuarial model developed by the Board of Actuaries, but with a 1% real interest rate, has estimated the normal cost to be 36.7% of payroll (in a report submitted in accordance with P.L. 95-595). Such a figure plus an addition to allow for merely paying interest on the unfunded accrued liability (which would be held constant in relation to payroll) -- both that which should have been funded by adequate government contributions in the past and that which would have existed nonetheless -- would show that the government cost for the CSR system is really at least 4 times the employee contribution rate of 7%.

EMPLOYEE AND GOVERNMENT CONTRIBUTIONS TO
CIVIL SERVICE RETIREMENT FUND

(in millions)

Fiscal-Year Period	Employee Contributions	Government Contributions	Ratio of Government to Employee Contributions
1921-28	$143	--	--
1929-45	1,321	$1,137	86%
1946-60	6,934	5,113	74
1961-69	9,799	10,197	104
1970-81	33,616	100,315	298
1921-81	51,812	116,764	225

The CHAIRMAN. Joe. Congressman Waggonner.

STATEMENT OF HON. JOE D. WAGGONNER, JR., CONSULTANT, BOSSIER BANK & TRUST CO., BOSSIER CITY, LA., AND FORMER MEMBER OF CONGRESS

Mr. WAGGONNER. Thank you, Mr. Chairman, and gentlemen of the committee.

I want to express my personal appreciation for the opportunity to appear today before so many of you that I have been privileged to serve with in this great institution. As I look around, perhaps the only member present at the moment that I did not serve with while here is Senator Bradley, but I was perhaps following him more then because of his endeavor than he was me at that particular time. But I know very well who he is, and I am privileged to be with each and every one of you.

Of course you and I, Mr. Chairman, understand that we have another bond with Senator Bradley that ties us in another way that we appreciate.

I am reluctant always to appear before a body of peers. My mother always told me in younger days that if I never amounted to anything along life's way, it would be good to associate with some who have. I feel like today I am privileged to do exactly that.

Another friend of mine, if you will remember, Bob Strauss, who is around town, used to say when I was in the House of Representatives that he would just like to breed me, Joe Waggonner, and Phil Burton and let him have the pick of the litter, because that ought to be some pup. Well, maybe that's the way this particular Commission is, Mr. Chairman, because we run the gamut. We go from A to Z almost, because I'm at one end of the line—now, maybe not just exactly the left spectrum all of the way.

But I am here today privileged to have been a member of this Commission, and I do thank our President for the opportunity to try to serve the best interests of this country, because we all do have the same thing in mind.

I have no prepared statement. I do have a prepared statement which is included in the Commission report, Report Statement No. 11, which is in the way of a dissent and I would hope that somewhere along the way you would find the opportunity to read that.

I found myself hard put, because after having left the Congress I found myself without a staff, and I had to write a dissent myself but then I had to get somebody else to type it—I couldn't even do it with a word processor. So I did have to go to work for a while.

I do not want this afternoon to try to kill you with emotion or with the rhetoric which has surrounded this issue for all too long. And because of too much rhetoric and too much emotion it really is difficult to face the problem itself.

It is necessary for me to be somewhat philosophical about what I have to say to you, because I have found through my years by way of experience that without a philosophy that has guided you, you will never believe anything and you will never have a conviction.

So what I have to say to you today is a conviction which, as the result of a maturing philosophy, which has caused me to take the position which I take today about social security.

If you are to help resolve the problem, and you are going to do that—in the final analysis it is your problem—I would only ask you to somewhere find some middle ground between your philosophy and your conviction rather than just being guided by what somebody spoon-feeds you. Don't, without question, accept the commission recommendation. You are entitled to know what I believe about social security—not just what I have believed, what I still believe about social security.

I recognize full well that you may disagree. You surely are entitled to do that. It may well be that you are right and I am wrong, but I do believe that I am right, and only time will tell whether or not I am wrong with my approach to what social security really ought to be.

I found many years ago it's not really what you say, it's how you say it. It really doesn't amount in the final analysis what you do, it's how you do it, and I will try to, in a way that you can understand, express only my point of view.

Somehow I suspect that quite a few people, maybe even more than some want to believe, that there are others out there who believe with me what I think social security was intended to be, is, and what it should be.

So what do I believe? First of all, I do believe very much in social security—not just because some people say it's here and it's here to stay. It's a great part of our life, and I do believe in this social security system. This country needs it.

Maybe there is a way to take this from our life now and replace it with something else—I really don't know what it is. And until somebody comes along with something that can be done, practically made to work, then I will continue to support without yielding any quarter what we have in the way of social security.

But in addition to believing in the social security system, I believe that, as it was intended, that social security should remain a self-financing program if it is in future years to be what it was initially intended to be.

I believe further that the framers of this program had great vision, perhaps greater vision, greater ESP, than we of this present age and day have, when they created a program which established a fundamental principle which was and still is, in my opinion, another major cornerstone of social security and that is the "earned-right" concept, for the the very specific reason to prevent the conversion of this great program to becoming a great big needs-tested oriented welfare program.

I believe that it was intended and still should be a basic floor of retirement income. If you want to say it another way, it was intended to be supplemental to other income.

There is more misunderstanding about social security, perhaps, than any other subject, because there has been a great deal of rumoring around the country which has hurt the effort to try to salvage, stabilize, this particular program.

You have heard it said, so have I, but I don't agree that our older people are financially less secure than are the younger people. I think it has been demonstrated by every study which has been done that those 65 and older are financially better positioned for life than others younger are.

We have a number of other programs which benefit them, benefit in one way or another many others. We have pension programs in ever-increasing numbers. This nation only had about 750 private pension plans when social security had life breathed into it—now we have about some 700,000 private pension plans, and the numbers grow each and every day, and that's good because it provides security for older generations of Americans.

We have, we in this Congress—I was here and a party to it with establishing the Keogh plan—we have, additionally, the IRA's, our individual retirement accounts. In addition, we have the CODA's. Not too many people are familiar with it yet, but they are important and are going to be ever increasingly important to the financial security of our elderly people, with our CODA's, our cash or deferred arrangements.

When people say that the older people are not doing as well, every study I have seen says at least 70 percent of our elderly people own their homes, and 80 percent of those people who do own those homes have no mortgage hanging over their heads. Some people don't want to admit it, but many have wealth.

But then we have our SSI program. We have many means testing programs for the elderly, not just SSI but housing assistance, food stamps, medicaid, energy assistance.

But now you know what I believe of social security. If it provides some rationale for you, you should know, you should at least review why the Social Security Commission exists. The Social Security Commission is in existence for one reason and only one reason: simply because all previous economic assumptions which have guided the social security program and the expansion of social security programs, as other facets, other cost benefits have been added, all previous economic assumptions have been wrong.

Never, ever have previous economic assumptions in the short range, and they accumulate over—just trickle over, lap over—to the long-range predictions, ever been right. They have never been right; they have always been wrong, always overly optimistic.

Now, my good friend Bob Ball and I will understand exactly what I mean. I have had his aspirin through the years. Mr. Ball has fed me those aspirins and had me take those aspirins and believe them for a while, that everything is going to be all right. He just never was right. He isn't right now. I am just through taking those aspirin. It's going to take more than just saying to you with a sedate aspirin that everything is going to be all right if you will just wait—if you will just wait, everything is going to be all right.

Well, I'm walking into the shadows of life, and things are getting worse, and they are getting worse by leaps and bounds, and you have to face that problem.

I note Mr. Ball is making some note there for his rebuttal, and I've got one for him when we reach that point, too.

To a point, however, having talked about the need for a Social Security Commission, I would be negligent and I would be wrong if I said the Commission has accomplished nothing. That would be wrong.

The Commission was needed, and the Commission has helped. It has been served by every member who has, out of conviction, expressed their opinion. And I sure do agree with that.

The Commission did an awful lot by recognizing the short-range problem and the long-range problem. People almost universally agree with this now, and I do agree, that we should have approached in an effort to stablize the program with the short range and with the long range.

But to a point the Commission failed. It failed—again, another personal appraisal. We lost our perspective, we lost our mission—again, from only my personal point of view. We lost our direction, and we quit trying to give our best recommendation about what best would serve the stabilization of this great program.

We became a third-party mediator in a political way between the administration and the Speaker of the House of Representatives. Maybe that's what it takes to do something, because something does have to be done. But I did not at the outset believe that we were to be mediators.

But what is the economic situation today? It is vastly different than it was in the sixties and seventies when I was here and we were spending money and adding costs of benefits to the social security program, and establishing many other programs.

But now we have to retrench ourselves, at least our thinking, to try to decide what we need or can afford.

I need not tell you, and I hope you don't object to my reminding you, of the drastic situation which surrounds our domestic economy. There are some who would tell you that you have to do just exactly what this Commission recommends, because if you don't take just this recommendation without any other consideration then a signal is going to go out to financial markets which will disturb the financial markets in a way that they will never be able to recover.

I don't believe that will have quite that effect upon financial markets. They need some stability; but let me tell you, let me tell you sincerely, that the problem has to do with Federal deficits.

What are our problems? Everybody has problems in this country—housing, farming, autos, steel, financial institutions, commercial banks, our savings and loans, energy, you name it. We've got our problems.

But the world economy isn't much better. Why would now the Congress be required to consider the appropriation, at least the authorization, of another $8.4 billion to the IMF? They need that money because of the state of the economy worldwide and for emerging nations and for some of our financial institutions. Where are they? Forty-five black governments in Africa—what is their economic situation? What is it in Mexico? What is it in Canada? What is it in Central America, South America, Europe, France, England? They have gone the route, having once been an economy such as ours, to a nationalization program in the Middle East and Asia.

But what are our problems? Two major problems with social security, many others; but, major, we have the problem of the COLA and the problem with demographics. These are in the short range and the long range the problems of social security.

What are our options? Whether you agree or not, we have four fundamental options. We can accelerate or increase taxes. I went that route again in 1977, and we were wrong. We led the people to believe and we were misled that we were stabilizing social security and we went just the tax route; because our economy has not performed we failed.

The second option to us is Treasury financing. And the greatest of all evils from my personal point of view is exactly this. Maybe you don't like this relationship, but it is not much different than the ill-fated family assistance plan which we considered quite some time ago. It's a good blood first cousin of it, you can believe me, because if you start financing out of the Treasury system any portion of it, and this proposal from the Commission gets by way of the Treasury more than half of its new money in the short range from the Treasury, you do know there is nothing more permanent in Government than something that is said to be temporary. Federal deficits are worse than the social security problem.

The third option is to combine accelerated or increased taxes and Treasury financing. The Commission recommendation does that.

The fourth option to me is viable and can be done. You can, without destroying, without reducing social security, but it will be required to slow down the future growth of this program if you are to tailor revenues to these benefits. But if you don't, what are we going to be faced with? This number comes from a question from the House Committee on Ways and Means during our appearance there. If you do nothing about the present program, if you leave the old-age survivors program where it is, leave disability where it is, leave HI where it is, when you reach the year 2035 the combined tax rate, by the most conservative estimate we've had, would be then 28 percent of payroll, and that number moves up from there.

What are some of my criticisms, and briefly can I tell you about those?

My friend Mr. Trowbridge has talked about universal coverage. I do believe in universal coverage, but I don't think they understand what is intended when they oppose universal coverage. But I see no reason to include even those who have not yet been under civil service retirement for 5 years until they become vested in that particular program.

You do know that the civil service retirement fund, coupled with the military retirement fund, is in the ballpark in deficit now of about $1 trillion.

Taxing social security benefits if you have income of $20,000 a year as an individual or with a joint return $25,000? I am not arguing the issue of taxing social security benefits. As honestly as I can be with you if I was still here—I am not, thank God; I had that opportunity—let me tell you what I would do. I think I would be inclined to tax all social security benefits, because there are exemptions for the low income and they would be protected.

But this is as is the case with unemployment compensation. And I think if I were here I would favor taxing those benefits, too. I know this is not popular, but let me tell you something—the idea of taxing social security benefits in isolation to all other tax policy is contrary to what this has always done with regard to the way of tax policy.

This is a major tax policy. It does provide for Treasury financing; it does provide a means test that allows social security benefits but not without penalty, which does not treat all alike.

You do have the creeping bracket problem, because notching will be involved. It is a disincentive: it will provide pressure to lower the tax levels of $20,000 and $25,000, just as we have had the pressure to increase—which we have been doing at regular intervals—that wage to be taxed.

The CHAIRMAN. I wonder if you might summarize, Joe. [Laughter.]

Mr. WAGGONNER. One other thing.

The CHAIRMAN. I didn't want to get the whole report.

Mr. WAGGONNER. I can go on and on, Mr. Chairman. [Laughter.]

The CHAIRMAN. You know, I've got a plane leaving Friday. [Laughter.]

Mr. WAGGONNER. I'll be there. I'll be in my bed sometime tonight. [Laughter.]

The only thing I want to tell you is, think. You can do it without the Treasury and without accelerating or increasing taxes. Look at the recommendations in part that I have given you included in my dissent in the report which do not violate any of these concepts, and you will best serve the interests of social security if you agree with me, and you will not greatly weaken this system of government.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

I want the record to indicate that Bob Beck, who is a member of the Commission, could not be here because of a schedule conflict. And Lane Kirkland, a very valued member of the Commission, cannot be here because of an executive meeting of the AFL–CIO in Bal Harbor this week.

The six members of the Commission we have heard from, however, should demonstrate to every member of our committee that we have had outstanding members on the Commission. They have each made very valuable contributions.

I have very much appreciated the opportunity and privilege to serve on that Commission. I share the view expressed-by Commissioner Waggonner and others that this is not a perfect package; but I do believe that it is in our interests to move as quickly as we can. Therefore, under the early-bird rule, Senator Chafee will be first recognized to ask questions and then Senator Grassley.

Senator CHAFEE. Thank you very much, Mr. Chairman.

Mr. Greenspan, Ms. Fuller noted the increase in longevity in her statement. My question is, are you confident that the statistics which the Commission worked with as regards longevity fully take account of what seems to me an extraordinary and wonderful increase in the length of life of Americans today, particularly as regards, when they reach 65, the chances of them reaching 70, and when they reach 70 the chances of them reaching 75, and so on up, rather than the tables beginning with birth?

Dr. GREENSPAN. Yes, Senator. The data we have on the question of longevity is perhaps the most solidly founded set of numbers that, for economic forecasts, we have.

As you well know, the increase in life expectancy from birth has gone up extraordinarily in the last decade. That also is the case for those age 65 and over.

It's one of the reasons why a majority of us who had been concerned about the significant rise in the proportion of years which the average beneficiary is to receive benefits relative to the number of years in which he has worked and contributed to the fund is something which cannot go on indefinitely. While there are those who consider that the issue of increasing the age of full benefits, appears as a cut in benefits—that's true only in the very narrow sense of taking life expectancy as a fixed absolute number.

If one endeavors to conceive of a retirement system as somehow taking a segment of one's life and saying, "That's the period in which I am retired," one would presumably consider that the appropriate way of viewing benefit payments is that the proportion of work years to retirement years should reflect the fact of increasing retirement age.

So what I would say to you is that I find the data sufficiently convincing on this question to argue very strenuously for a variable to retirement age as an issue of the stabilization of the fund and the system itself as distinct from, as some would look at it as, a pairing of benefits.

Senator CHAFEE. Did you run any statistics on not changing the age 65 but gradually changing the age-62 early retirement? Do you have runouts on that, what the cash consequences would be of that?

Dr. GREENSPAN. There have been a number of simulations which have been involved. In almost all instances, however, it has been our judgment that the age of early retirement, wherever that is set, should be actuarily related to the age when full benefits are paid. And I don't think there has been strong support for a significant move in the relationship of the age of early retirement to the age of full benefit payments.

Senator CHAFEE. Do you mean a 3-year differential?

Dr. GREENSPAN. Yes.

Senator CHAFEE. You track that right along, do you?

Dr. GREENSPAN. Yes, basically; or its equivalent, as you increase the age.

Senator CHAFEE. Now, Mr. Trowbridge mentioned that he is including with his testimony the arguments as he found them convincing for this increase to the age 68 that some of the Commission voted for. I will be interested in seeing that.

Maybe I should ask Mr. Ball—what is the best argument against this? Is there some prepared statement that you have on that? Is it included, or where might I locate it?

Mr. BALL. Senator Chafee, the five of us who were appointed by Democrats included in our supplementary statement why we opposed increasing the age of eligibility for full benefits. I have also included it as a supplement to my prepared statement today, if you have that there. It occurs as an attachment toward the back.

Senator CHAFEE. Fine.

Mr. BALL. I think at some point, Mr. Chairman—I don't know whether this is the time—it but at some point, since the arguments have been made in oral testimony for increasing the age of first eligibility for benefits, that it would be appropriate for me to make the contrary arguments. I don't know whether you want me to do it now or some other time.

Senator CHAFEE. Not on my time, please.

Mr. BALL. All right.

Senator CHAFEE. But I will be glad to hear the argument.

The CHAIRMAN. We'll do that, Bob.

Senator CHAFEE. I think that is a good thing, but I only have a limited time.

Mr. BALL. Surely.

Senator CHAFEE. But I'm surely going to read it. As you mentioned, it's in the supplement.

Mr. BALL. Yes.

Senator CHAFEE. Fine.

And finally, Mr. Greenspan, the thing that bothers me about the self-employed—and I'm sure you have considered this—is that, as I understand, the self-employed in a certain year will pay the total tax that is now equal to what the employer and the employee pay—14 percent or whatever it would be, 16 percent as we go along.

My problem is that that individual will then, if he is in the certain brackets, will then still be entitled to having half his benefits taxed even though he has paid for all his benefits.

Dr. GREENSPAN. Well, the problem, Senator, is the fact that what we are endeavoring to make the issue symmetrical with respect to a small corporation or a private individual. In other words, at the moment what the proposal does is to essentially create a situation in which a single individual as a proprietor or as an incorporated business is treated in precisely the same way as he would be if he were incorporated. So the same problem does exist for a corporate owner as well. He is then an employer.

Senator CHAFEE. Well, except eventually he is going to be taxed on half his benefits—that is, starting in 1984.

Dr. GREENSPAN. But remember though, the benefits on which he is being taxed are those which had not been taxed previously, because half of the tax which either a business or he as an employer puts in comes out tax-free. In other words, it's essentially a deduction, and he is not taxed on that.

In other words, what happens in the system is that what the taxation of benefits endeavors to capture is the amount of contribution into the funds which had not been taxed previously.

Senator CHAFEE. My time is up. Thank you.

The CHAIRMAN. Senator Grassley.

Senator GRASSLEY. Thank you, Mr. Chairman.

The short-term goal of any recommendation such as this is to keep the checks coming. I understand July 1 of this year is the magic date for dealing with the social security financing crisis.

But I hope that in the process of dealing with social security we can also accomplish some long-term goals. One change I would like to accomplish is to get away from a situation where Congress is always responding to a crisis, or is trying to manage a crisis. It is also imperative to restore some confidence of the younger workers in the system so they know there is going to be a system when they retire.

In regard to that, my first question deals with the automatic stabilizer that is first authorized in 1988. It's purpose is to protect the system when the reserves fall below 20 percent, and I understand there is a possibility it could get as low as 11 percent in the next 2 years.

My first question is on the adequacy of a package that could be deficient in meeting social security payments for even 2 full years; and second, why did the Commission recommend 1988 as the effective date when in fact the need for the mechanism may occur even sooner?

Dr. GREENSPAN. Senator, there were a great number of issues on which there were differences of fairly significant dimension within the Commission, this being one of them.

There are those who take one side of this, and I would like Mr. Ball to comment after I do, but there are a number of issues on which we have all agreed that compromise represents a position which neither group chose in the beginning. The 1988 issue is part of a compromise and is an issue which some of us would have agreed with you on; others wouldn't. I would like Mr. Ball to express his point of view, which comes on the other side of this issue.

We have agreed that if we are going to come to an agreement, there are going to be issues such as this where some of us would feel more comfortable with different positions; but there is no way to strike a compromise with this type of problem without very significant——

Senator GRASSLEY. What you are saying is, we ought to leave in place a system where there could be another crisis, in perhaps 2 or 3 years.

Dr. GREENSPAN. Well, why don't we do this: Let's let Bob Ball continue on this, and I will follow on afterward, and you will see what the nature——

Senator GRASSLEY. I shouldn't be accusatory in my statement; rather, let me ask, isn't there a possibility we might still have a problem 2 or 3 years down the road?

Dr. GREENSPAN. I personally don't believe that. I think that's unlikely. There are problems in the middle years which have a small chance of occurring, but I think they would be more appropriately addressed with a fail-safe mechanism than advancing the stabilizer.

My own judgment is that the stabilizer won't be of any great assistance, and it's of no particular value in the years 1983 through 1986, largely because I think that since productivity has been so extraordinarily deficient in the last 4 or 5 years that chances of it continuing that way are actually quite small.

The obverse of the very extraordinary rise in the unemployment rate is that we've set into position a period of major productivity improvement. That means that we will not get anything remotely close to triggering—or, I will put it this way, you won't get anyplace where the use of wages or prices, the lesser is going to make any difference; because wages will almost surely—whatever they are—increase more in prices.

Bob, why don't you address this?

Mr. BALL. Senator, I think that Dr. Greenspan has made the major point, and that is that something else needs to be relied on as a fail-safe in the short run—not the question of wages or prices, whichever is the lower. I think that has an important stabilizing effect for the long run, but since the high probability is that wages are going to be higher than prices, the short run isn't helped very much by moving that forward. That's the first point.

But the reason that we postponed it coming into effect until 1988 is that, under the estimates as we were looking at them at the time, the trust funds for the cash benefit part of social security—OASDI—are so low that if you were to say you trigger at 20 percent of the trust fund ratio for the next year's outgo and there put wages or prices into effect, the provisions would have been immediately effective. It would have been the same as saying: we will put into the law—not as a stabilizer but as an immediately effective proposal—a substitute for the cost-of-living provision, wages or prices, whichever is the lower.

Many of us felt that that was not a good change. We supported it as a longrun stabilizer, but not as a substitute for trying to keep the cost-of-living adjustment.

Senator GRASSLEY. I appreciate your response to that. I would like to direct my second question to you, Mr. Ball.

This is in regard to the goal of reestablishing confidence in the system among the younger workers, and it deals with the solution of the problem through tax increases. Of course, there are honest differences of opinion between people on the Commission and the Congress, whether or not tax increases should be used to deal with the long-term deficits.

My question deals directly with what the feeling was among the Commissioners in looking at the other side of the equation: the tax increase for the workers and what this might do to their confidence in the sytem?

Mr. BALL. Senator Grassley, you are referring to our proposal to deal with the——

Senator GRASSLEY. To speed up the tax increases.

Mr. BALL. In general, or just to the residual part of the long term that was left, the 0.58 percent of payroll?

Senator GRASSLEY. No; I am talking about the first, what is instituted in the majority recommendation.

Mr. BALL. Right now?

Senator GRASSLEY. Yes.

Mr. BALL. Well, I believe all 12 of us agreed that a part of the solution necessarily was an acceleration of the tax increases that were already in present law.

It became very clear early that, since we had agreed that there was a deficit——

Senator GRASSLEY. Excuse me. I meant the long-term solution; the additional five-eighths of a percent increase in taxes. Would you address that point? I'm sorry I misled you.

Mr. BALL. Certainly, Senator.

Our proposal is to, in 2010, increase the contribution rate on both employers and employees by 0.46 percent of payroll. Now, that is designed to meet the full remaining part of the deficit for the whole 75 years over which the estimates are made. That's the figure you would need, doing it through tax increases.

We also proposed, on the employee side, that there be a fully refundable tax credit that would completely offset the increase.

We took this view basically, Senator, because we do not believe the system at its present level of protection is at all excessive—quite the contrary. The present system seems to us, in the protection that it promises for the long run, to be reasonable. I'm not pressing for improvements, but I certainly think it would be bad to cut back on social security protection for the long run.

Now, the major practical alternative you have to scheduling a tax increase in the future is a reduction in protection. And the chairman has suggested that at sometime, when it's not on your time or another member of the committee's time, I will address why we think the cutback or the change to age 66 on the automatic provision that was proposed by the others is a cut in benefits, and why we think that's a bad idea. It's really because of the alternative of cuts that we came to favor tax increases.

Senator GRASSLEY. Thank you, Mr. Ball.

The CHAIRMAN. Thank you, Senator Grassley.

Senator Heinz, Senator Wallop.

Senator WALLOP. Thank you, Mr. Chairman. I just sort of assumed Senator Heinz was right here beside me still.

I just, again, think that as we face this it's interesting to watch that retired people don't like the taxation of benefits over $20,000, and farmers don't like the increase in taxes of self-employeds. You can sympathize individually with each of those until you have sympathized yourself out of any solution whatsoever, and I think that's a real danger that we face.

But one of the things that happened to us 7 years ago, and I recall voting against it for that very reason, was the outrageously rosy economic forecasts that were used to substantiate the proposals to take us to 2030; and this is not 2031, but it's 1983.

I wanted to ask you, Dr. Greenspan, what is different about the economic predictions used by the Commission from those in past practices?

Dr. GREENSPAN. They are lower, and more importantly I think——

Senator WALLOP. You figure yours are low?

Dr. GREENSPAN. No; my answer was they are lower.

Senator WALLOP. Oh, "lower."

Dr. GREENSPAN. Yes.

Senator, let me just say that one of the problems we identified very early on was that there was no way to solve this problem by getting the correct economic forecast. What is very clear about the nature of this system is that it is highly sensitive to how the economy performs, and there is no set of recommendations which will insure the trust funds short of a massive increase in either taxes or a massive reduction in benefits.

In other words, to absolutely insure against any conceivable adverse economic scenario you would have to put in place recommendations which are probably twice as large as the ones that we recommended eventually in our compromise solution.

As a consequence, we asked ourselves, is there any way in which we can construct a set of changes in the way the system functions which would desensitize the trust funds from the types of errors that occurred as a consequence of the 1977 legislation. And we concluded that there are two:

One is the so-called stabilization device which is put in place later in this decade, which we have just been discussing, whose essential purpose is to try to guard against a special type of event where productivity is either falling or, more exactly, prices are rising faster than wages. That's the major type of event which can do the trust funds in.

The second, and in one sense the ultimate protector of the system, is what we call a fail-safe mechanism, which is a particular procedure which specifies what should happen to either benefits or taxes when the trust funds run down to a level in which the maintenance of monthly benefits becomes threatened.

So what we have in our proposals is not something which we say will guarantee the solidity of the trust funds merely by changes in taxes and/or benefits, because there is no way to do that. That's the reason why we have concluded that, rather than attempt an overkill, which is the only way to insure the system, to introduce techniques and institutional changes which in effect desensitize the system from that sort of problem.

Senator WALLOP. Thank you.

Mr. Chairman, I think one thing that absolutely ought to be engraved in marble in all our considerations of Dr. Greenspan's statement is that there is no way to do that.

I don't think that we ought to concern ourselves here with the ultimate perfection in a solution but try to get on with a broader-based solution as such is proposed.

But one of the problems that we correct in 1977, at least to some extent, was the wage-replacement rate—perhaps the only really constructive piece of that legislation. And it will decline somewhat from that high of 51 percent over the next couple of years.

I just wanted to ask you or Mr. Ball if you believe that we can make further adjustments to lower the wage replacement rate and, if so, if it wouldn't be feasible to have a lower replacement rate for social security now that the private pension plans and IRA's are expanding?

Dr. GREENSPAN. Well, Senator, that is obviously one of the issues which we debated, and the outcome of the compromise was that long term adjustments would occur as a consequence of certain short-term measures that we've taken. The taxation of benefits and especially the 6-month freeze, reduces the replacement rate modestly—less than a lot of us would like, clearly, but more than others of us wanted. It is a compromise, and that's the reason why the significant change in the replacement rate other than that which is programed into the compromise solution would unwind the solution, because that's one of the things on which we compromised

Senator WALLOP. Well, I guess we can and even should accept that. I would like to just ask one other thing, especially in light of Mr. Waggonner's statement that you ended out as a third-party mediator between the two parties.

Assuming that we can pass this, and I think that we can and should, would it be the Commission's recommendation that we somehow or other get back to the sort of fundamental issues that are still outstanding—Ms. Fuller mentioned some, and there are obvious ones which are implicit in my question—and try somehow or another to put aside some political differences and go on with the remaining things that are on the plate?

Mr. TROWBRIDGE. Senator, I certainly would urge that this problem not be considered solved once the passage of legislation takes place, because there are a number of issues that I think do require continued study. One of them clearly is the whole question of the hospital insurance fund, which is a great big problem coming up over the horizon. We know it's out there. We did not deal with it as a commission, but it will have a very strong impact on the entire social security system unless ways and means of reducing the growth of medical costs can be agreed upon.

That is an example of an area in which a lot more work has yet to be done.

Senator WALLOP. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Danforth?

Senator DANFORTH. Mr. Greenspan, do we have the luxury of doing nothing?

Dr. GREENSPAN. I don't believe so, Senator. I think there are so many problems which now confront this country, its economy, its budget, that unless we start rather quickly to resolve them sequentially we are risking degrees of instability in not only our economy but in the international financial system which I consider unacceptable

While none of us on this Commission likes this compromise, in many respects I suspect nobody should, it is a combination of least-worst alternatives to a problem which we all desire to solve but recognize the individual elements were a series of unacceptable individual choices when considered by themselves.

Senator DANFORTH. Let's assume that we do nothing—we pass no bill—and further assume that down the road we don't pass any bill, that we are just in a permanent state of stalemate. What in your view would be the consequences for social security; and, second, what would in your view be the consequences for the economy as a whole?

Dr. GREENSPAN. Well, first of all, should we literally do nothing, legislatively the OASI fund would run out of its legal authority to pay checks sometime this year.

Senator DANFORTH. And what would happen then?

Dr. GREENSPAN. I would say that somebody would produce a bill in the House and in the Senate to extend interfund borrowing.

Senator DANFORTH. Let's assume there is no legislation though: Assume that we get stalemated, that we cannot decide what to do, that we not only don't take this opportunity to fix the system but we don't take any opportunity to fix the system. Then, what is the law?

Dr. GREENSPAN. The law is that no checks are paid.

Senator DANFORTH. No checks could be paid. We could not pay out a partial check?

Dr. GREENSPAN. Until you have funds to pay a full monthly benefit you cannot pay any checks. In other words, as I understand it, you will miss a check or two, and you will be unable to make sequential monthly checks. That's the way the law reads, doesn't it, Bob?

Mr. BALL. Mr. Chairman, I think what would probably actually happen is a delay in the checks, and you would have to wait in July for I don't know how long, but a day or two, until the money had accumulated, then you could pay it. The next month it would be a little longer, and so on.

Dr. GREENSPAN. What would happen is, it would sequentially get to a point where you would be paying checks every 35 days, then every 40 days.

Mr. BALL. If you wait long enough.

Mr. TROWBRIDGE. Senator, if I could just add a note as to what the operative conditions were at the time when this fell into place, in the last hours of January 15, I think there was a scenario that when you asked:

> Compared to what?

The answer came back:

> We would come up with a Commission that had no particular set of consensus recommendations; that the Congress would be greeted with this sort of menu from which to choose; that choice would probably not be made by May 1; and if that were not done by May 1. the ability to postpone the cost-of-living allowance which was part of the package after July 1 would have been lost, and we would have gone on

through June with the probability of no legislative action and a situation, in which the checks just would not go out.

Senator DANFORTH. All I wanted to do was just to assume that Congress does nothing. It was my understanding that if Congress does nothing the effect of that is that there would be delays, and the length of time between would be stretched out, and it would be in effect an unlegislated cut in benefits.

Now, let me ask you another question: Assume we do nothing. What would be the effects on the economy?

Dr. GREENSPAN. Well, as a practical matter, Senator, I think nobody perceives that that is in fact what will happen. What is presumed will happen, so far as those in the financial community are concerned, is that the Congress will introduce a borrowing authority from general funds in the Treasury, by temporary emergency legislation.

If that happens the general belief would be that we have significantly altered the structure of the social security system into essentially a means-tested system, and it will just be a matter of time before the self-financing characteristics of the system will be perceived as breaking down. And that will be perceived by the financial community as a major signal that our budgetary processes are out of control, that the fiscal process is collapsing, and that would be perceived as a signal that the budget deficits that we are now looking at are only way-stations to budget deficits which are significantly higher.

Senator DANFORTH. All right. Let me ask you just one other question on the matter of unraveling.

This package, as I understand it, was put together after a very long process of negotiation. There was some doubt as to whether or not the Commission could come forward with a consensus proposal, and in forming that consensus there was a lot of compromise and a lot of give on all sides.

I would like to ask you, Mr. Greenspan, and then you, Mr. Ball, if you view this as a package which should be kept intact for fear that if it is not kept intact it will fall apart.

Putting it another way, we have been urged by some to keep our powder dry with respect to committing ourselves for this package. If we do keep our powder dry for a long period of time, could it just explode and blow the whole thing up?

Dr. GREENSPAN. Well, Senator, I can't answer that; having been party to the negotiations, I can tell you that we have squeezed out all of the areas of agreement that exist and put them into the compromise. There is very little leeway in which significant alterations could occur without unwinding the package. I think this is as tightly structured a compromise as I have ever seen.

Senator DANFORTH. Unwinding the package, meaning that those who made the package would just fall off? Is that correct?

Dr. GREENSPAN. In effect.

Senator DANFORTH. You would no longer have a consensus?

Dr. GREENSPAN. That is correct.

Senator DANFORTH. Tip O'Neill, Claude Pepper, and so forth, would fall off, right?

Dr. GREENSPAN. I can't speak for them specifically, but I could certainly make the general judgment that that's what I expect to happen.

Senator DANFORTH. Could you comment, Mr. Ball?

Mr. BALL. Senator Danforth, as everyone has said, there are parts of this package, although different parts, that each of us dislike when taken separately; but by putting it together, there has been a remarkable degree of support across groups and individuals that usually find it very hard to agree.

Mr. Trowbridge testified to the National Association of Manufacturers' support; the AFL-CIO is supporting it; the Coalition of Statewide Security Groups, of which I am a member of the executive committee, will testify in favor of this. One or two of the groups out of 140 did not go along with that consensus, but you have the support of groups that are ordinarily associated with liberal positions and labor positions and business positions, and this all hinges on the fact that I believe this is very well balanced, that everybody is asked to sacrifice something but nobody is asked to sacrifice tremendously.

The degree of sacrifice that is in the judgment on these packages isn't so much whether individual Commission members would fall off, it's that the groups now supporting it would fall off, and that leading political leaders who have backed this, from the President to the Speaker to the majority leaders of both the House and the Senate, might find it very difficult to put together something else that they could agree with.

Now, it seems to me that that applies to the major elements in this package and that it would be very difficult to reconstruct something else. It doesn't mean there aren't some little parts of it that could be changed.

The CHAIRMAN. Senator Armstrong?

Senator ARMSTRONG. Mr. Chairman, I am somewhat at a loss to understand why if this is such a good proposal everybody has such unhappy looks on their faces. As I look around the room, it's a toss-up as to whether the press or the witnesses or the members of the committee seem to be more dismayed by the prospect of this compromise package which we must enact lest it blow up.

I just want to say to Senator Danforth, I have long wondered whether or not anybody reads my "Dear Colleague" letters, and "keep your powder dry" is a buzz word, and I appreciate your introducing it in this afternoon's proceeding, and I assure you that the notion that any any compromise cannot be refashioned with a slightly different coalition is not borne out by the experience of this committee.

In fact, I was thinking, as Dr. Greenspan and Mr. Ball expounded on how if we ever blew this compromise out of the water that we would never be able to do anything else, I was thinking of how often the Treasury Department and other witnesses have come before us and warned that if we didn't adopt their preconceived idea, and particularly if we adopted some particular amendment that they didn't adhere to, that it would be impossible to legislate in this area perhaps for years to come; and yet, how often such constructive changes have been adopted by the Finance Committee. So I was glad you brought that up.

Mr. Chairman, as I listened to the testimony this afternoon from our distinguished witnesses, I was struck again by what a wonderful experience it was to be a member of the National Commission on Social Security Reform. I want to pay tribute to Dr. Greenspan for his leadership, which has been extraordinary, and for his mastery of the subject and his expertise and his courtesy to the members of the Commission and to each of my fellow Commissioners.

I note that there does seem to be a quorum of the Commission present in the room, and I'm wondering if it's too late for us to move to reconsider the recommendations that have been adopted. [Laughter.]

This is not the moment, obviously, for me to press my own views. I do have a couple of questions.

One question which I would ask all Commissioners to reflect upon but not to answer at this time is whether or not if, as I fully expect, we have to revisit this matter in 1985 when the trust fund runs dry again, whether or not we would all be willing to serve as members of a similar commission. I would hope we would, because we have some experience in this. We have been working on it, and I think we could do this job again in 1985 with great pleasure.

Mr. Chairman, let me make just one general observation, then I do have a question which I want to address particularly to Dr. Greenspan and to Mr. Ball.

I don't want to rehash what my objections to the main thrust of the Commission's recommendations are—I will get to that on another occasion, perhaps—but I do acknowledge there are some things in here that are very worthwhile:

I think, for example, the military prepayment is a good idea. I think that's fair. I like the idea of accelerating the State and local deposits; I particularly like the provision that relates to divorced spouse; although I would say to those who have provided leadership on this that within a few days I am going to be introducing legislation which I think will solve this problem in a better way—a slightly more costly way, but a way in which I think most divorced spouses will feel is better, and that will be one of the elements that I expect to include in my final package.

My question is this, and I ask it having reviewed rather carefully the projections of the trustees over time, that is the estimates of future economic performance and future performance of the trust fund, and compare that with the actual results.

What I have seen in reviewing this is that there has been a quite pronounced tendency toward overoptimism; in other words, actual results have proven to be a lot worse than what we have estimated them to be.

Then I note with some concern the testimony before the House Ways and Means Committee of the Commission on Social Security and the reports which have emanated either officially or informally from CBO and from the actuaries, all of whom seem to be indicating that we are skating very, very close to the edge of thin ice with our recommendations.

Even if you approve of the policy considerations, which I do not, the question is: Are these recommendations sufficient to keep us out of trouble? Will we be back at the same stand in 1985? Now, that's my question.

How confident are we that we are not going to have the trust funds running dry again? I don't want to be too insistent, but, Dr. Greenspan, if you would care or if Mr. Ball would care to give us on a scale of 1 to 10 how confident you are of that—I recognize there are no certainties and you can't outguess the performance, but do you think it is a 9 or an 8 or a 6? Are you quite confident, or only so-so?

Mr. BALL. Well, Senator, obviously it depends on the fail-safe mechanism. If the Congress passes a fail-safe mechanism, then the answer is——

Senator ARMSTRONG. Well, that would not affect 1985, would it?

Mr. BALL. Sure. I mean, basically what the fail-safe mechanism would endeavor to do is to prevent the trust funds from falling below those levels required to meet monthly payments. So, if enacted prior to—let's assume it were enacted effective January 1984, it would clearly be 100 percent effective.

Senator ARMSTRONG. You are not referring as the fail-safe mechanism the lower of prices and wages.

Mr. BALL. No; that's the stabilization proposal. No; that wouldn't do it. The fail-safe is basically that part of the proposal which when the trust funds reach a certain level that a certain operation triggers, which would basically prevent the trust funds from going lower. You will remember we could not agree on a single plan.

Senator ARMSTRONG. But in that sense, even if we followed Senator Danforth's scenario, technically it is impossible for trust funds to go dry because the money simply would not be paid out until there was enough to—but I'm not referring to that condition, nor am I referring to the condition that might arise if we enact some unspecified fail-safe. I'm really trying to obtain your professional opinion of how accurate these estimates are or whether or not additional steps will be necessary.

Mr. GREENSPAN. Well, the reason why I was a strong supporter of a fail-safe mechanism is the recognition that there is no set of proposals which will guarantee that you won't run into trouble.

Nonetheless, without a fail-safe mechanism, I would say that the odds that this specific set of proposals will solve the problem is at least 2 to 1 and maybe significantly higher than that, because it requires a set of adverse economic conditions which I think are quite unlikely.

Senator ARMSTRONG. Fair enough. Mr. Ball, this is an area of your professional expertise over a long period of time. Do you agree, is a 2 out of 3, or a 2 to 1 expectation about what you have, or do you think it's better than that?

Dr. GREENSPAN. I'd say at least.

Senator ARMSTRONG. Dr. Greenspan said at least 2 to 1, and perhaps better.

Mr. BALL. Senator Armstrong, I ought to correct an impression that Congressman Waggonner and you may have, and also say something in defense of the social security actuaries. I did not make these estimates. The actuaries did, and their record up until about 1975, from the very beginning of the program up until 1975, in estimating the short-run costs of this program was extraordinary. They came out very close right along.

It was the introduction of the new factor of cost-of-living adjustments combined with an extraordinary economic change that we had not had before in this country, a very serious inflationary situation after 200 years of relatively modest price changes. It was that combination that created the situation that they—along with everyone else—did not foresee.

Senator ARMSTRONG. Well, Mr. Ball, I have just reviewed the projections from 1972, and I'll just insert them in the final report of this committee. I think you will find that they are widely at variance from the actual results.

Mr. BALL. Well, the 1972 projections for years from 1975 on were off. I agree with you. That's what I'm trying to say. But up until that point they were extraordinarily accurate and did an excellent job.

Now, to respond to your direct question, I can't put a figure on it, but I will say this: I would not want to rely on the fail-safe as if that were going to come into effect; it means exactly what it is called, a fail-safe. And we should have a financing plan that we have a good degree of confidence in without resorting to the fail-safe.

Senator ARMSTRONG. But you would agree that there is at least a 50-50 chance that the numbers recommended by the commission will be——

Mr. BALL. Oh, I think it's much, much higher than that, if you do one thing that has been suggested.

Senator ARMSTRONG. At least 2 to 1 or better?

Mr. BALL. Oh, I think so, if you do one thing that has been suggested. The present situation for social security is that in addition to the other sensitive features, there is always the possibility of a cashflow problem in the system because the benefits are paid out and charged against the fund in the early part of the month, right at the very beginning. On the other hand, income to the fund is credited to social security over a period of a month.

Now, that has a very important possibility of creating a cashflow problem because we are talking about a system which is essentially pay-as-you-go, and you are collecting month-by-month about as much as you pay out.

Under the proposal that would credit taxes paid during the month at the beginning of the month, the trust fund ratios that look thin in the middle years, under the II-B assumptions, are greatly improved. Just doing that one thing—what has been called normalization of tax transfers—results in trust fund ratios above 20 percent in all years.

Now, this should be done, of course, without the trust funds gaining interest.

Senator ARMSTRONG. Well, Mr. Ball, maybe you should take a moment just to elaborate on that. I believe I am familiar with that proposal—I'm not sure other members of the committee are—but it amounts to borrowing from the general fund for periods of less than a month.

Mr. BALL. Oh, I don't think it needs to be considered a "borrowing", Senator Armstrong.

Senator ARMSTRONG. Well, if the general fund didn't have it the Treasury would have to go out and borrow the money in order to transfer it to the OASDI fund.

Mr. BALL. The question of borrowing and interest here I think is a very important point. It would not be considered reasonable under these circumstances certainly for the trust funds to draw interest on that money, I certainly agree with you. That would constitute a subsidy from general revenues, and I certainly wouldn't do that.

Senator ARMSTRONG. You mean to pay interest?

Mr. BALL. Well, the paying of interest to the general fund would result in an offset. If you were to pay interest to the general fund on the amounts that were credited at the beginning of the month, then those amounts that the trust funds have at the beginning of the month could be invested—so that's a wash.

I think it would be wrong, however, for the trust funds to draw interest without paying interest to the general fund. That would constitute a subsidy, but not just a moving-up the crediting of estimated income.

Senator ARMSTRONG. Mr. Chairman, I think my time has expired, but I am going to note that Mr. Ball is quite confident that the Commission's recommendations will in fact be borne out by experience.

The CHAIRMAN. Senator Mitchell?

Senator MITCHELL. Thank you, Mr. Chairman. I would like to just comment briefly on this cost-of-living adjustment change that you have proposed.

Dr. Greenspan, you referred to the circumstance of prices rising at a faster rate than wages as a special event; Mr. Ball referred to it as extraordinary.

Obviously, when the change was made in 1972 that really is the cause of the current problem. No one foresaw that, particularly given the economic history of the previous three decades.

But I must say I'm really surprised, in view of the history of recent years—that is, our inability to predict future events—you, Dr. Greenspan used the phrase "almost certainly" in saying that making the change that Senator Grassley suggested earlier, that it almost certainly would have no effect in the next few years because the high rate of unemployment has such a dramatic effect on productivity. It seems to me that what we ought to have learned from 1972 and 1977 is that there is very little that can be deemed almost certain in predicting future economic events.

I have to say to Mr. Ball, for whom I have great admiration, that I find his reasons for not agreeing to make the change quite unpersuasive. Perhaps there are other better arguments that have not been made here, but if that is the principal cause of the current situation—the 1972 change which indexed benefits-to-prices and increased the wage base in accordance to wage increases—why haven't you taken what seems to be the simple and forthright step of making the change to the lesser of the two effective immediately, unconditioned by any level of the trust fund?

I think the failure to do so, frankly, underestimates the willingness on the part of elderly Americans to participate in a change that, although it represents some sacrifice on their part, once they understand it they are prepared to make that kind of sacrifice, indeed want to do something to demonstrate a contribution in that respect.

I know it's easy to second-guess, to be a Monday-morning quarterback, and I am aware of the internal pressures to which you referred, but I think it would have been a relatively forthright step that would have gotten a great deal more support than perhaps was anticipated.

Let me move to another area and ask a couple of questions regarding universal coverage.

Table A in the Commission's report lists the proposals and the cost analysis. The very first one is that if you cover nonprofit and new Federal employees, the short-term savings is $21.7 billion.

Do you, Dr. Greenspan, or does anyone have a breakdown of that tool as between those two elements? That is, nonprofits and new Federal employees?

Mr. BALL. Senator, if I remember correctly, about $12.4 billion of that is nonprofit. Remember, on the nonprofit you are covering the total outstanding group of about 15 percent of nonprofit employees right away, whereas it is only new hires for the Federal employees. That's my memory.

Senator MITCHELL. Your memory is, about a third of that is the nonprofits and about two-thirds the new Federal employees?

Mr. BALL. Yes.

Senator MITCHELL. As you are all aware and as Mr. Trowbridge alluded to, there is considerable apprehension and opposition to this proposal by those persons who are not now subject to social security and who would become subject to it. That raises two questions.

In your report you state your belief that an independent supplemental retirement plan should be developed for Federal new hires, and then in the same paragraph you say that it is important to note that present Federal employees will not be affected, and the financing of their benefits over the long run will not be adversely affected.

I think their concern is that what basis is there for any reasonable expectation on their part that either of these things will occur in a manner to which they can look forward. They are, are they not, subject to whatever the Congress decides after the fact, if we pass this package? That's obviously going to come before a new independent supplemental retirement plan, so they don't know what that plan is going to be.

Second, what basis, legal or otherwise, is there to tell them that they can be assured that the financing of their benefits over the long run will not be adversely affected? Does not Congress have plenary power in this area? Can't we change that at any time?

Dr. GREENSPAN. Certainly, Senator. Private employers and private employees are engaged in a very much similar sort of problems, discussions, promises, and the like.

I see no reason why Federal employees should be distinguished from the rest of the work force. As an ex-Federal employee I find that there are certain characteristics of Federal employment, especially in this area, which are far superior to anything I have seen in the private sector. The record of the Congress in seeing to it that

Federal employees are well-pensioned has been extraordinary. If I were a Federal employee now my concern would be minimal to nonexistent.

So, certainly the Commission stipulated that we believe the Congress will do that. We are recommending that they do that. There is no way we can have a proposal which reverses the sequence without in a sense going forward and endeavoring to also develop a strong secondary civil service system for the first hirees subsequent to January 1, 1984; but we have done similar things on innumerable occasions. I would see no reason why they should be concerned that the Congress will not appropriately address this question.

Senator MITCHELL. Well, you say there is no reason for them to be distinguished in any way, but the fact is that they are because there is an existing system, which obviously does very well by them, and they want to hang on to it—a very understandable human reaction.

Dr. GREENSPAN. No; remember what we are talking about are those people who are not yet Federal employees. There is a valid case to be argued for those who are currently in the system, who have been there for years. One should not change a system without very considerable study.

All I am saying is, one of the conditions of being hired after January 1 would be the awareness that, for the moment at least, this is an uncertainty.

Senator MITCHELL. Well, that's quite correct, and that goes to the first part of the question, but it does not address the second part of the question, which is that the financing of the benefits of current Federal employees over the long run will not be adversely affected.

If you are going to take new Federal hires and put them into social security, a substantial portion of the current contributions into the civil service retirement system will be denied to that system. They will inevitably, will they not have to be made up by increasing the annual Federal appropriation, to which there will undoubtedly be considerable opposition, and the more that grows, the larger the pressure against it. It seems to me to be a very tenuous situation for them.

Dr. GREENSPAN. Well, Senator, I would suggest that the submission of our Executive Director, Robert J. Myers, which addresses this issue, which will be part of the record, be reviewed.

There is nothing inherent in the system which in any way specifies that current employees of the Federal system, in the Federal Government, will have their expected benefits in any way changed.

Currently a very substantial part of the civil service pension fund, as you well know, is funded through direct contributions by the Treasury. It has been an increasing proportion for a number of years and probably will continue to be. Whether the Congress chooses to adjust that or not is, I think, an important issue; but I find it hard to believe that that issue will rest in any significant manner at all on this particular Social Security Commission proposal.

Senator MITCHELL. Well, my time is up and I don't want to belabor the point, but it is clear that the civil service retirement system now receives revenues from a number of sources, one of which is employee contributions.

To the extent that you put new Federal employees under social security and construct a separate supplemental system, you deny to the current system that portion of revenues. It seems to me it will have to come from somewhere else, and Federal appropriations is the only place.

Dr. GREENSPAN. Senator, if you don't do what we are suggesting, you are going to have to solve the social security system with something else.

The CHAIRMAN. Senator Baucus is next, but I would like Mr. Bob Ball to comment. This is an important point.

Senator BAUCUS. I will just confront this very point, too.

The CHAIRMAN. All right. I think Mr. Ball would just like to say a word before that.

Mr. BALL. Mr. Chairman, just before I get to that, could I correct a previous answer that I made? I didn't remember correctly. The division between nonprofit and Federal employees is really the other way. Under the 1983 alternative II-B assumptions of the trustees which I believe has been furnished to the committee, the new Federal employees amount between now and 1990 is $9.3 billion, and all nonprofit employees is $12.5, for a new total of $21.8.

Now, I would also like to point out, though, that the long-range saving of 0.3, the contribution of extending coverage to the reduction of the 1.8 deficit, for the long run, comes largely from the Federal employees—very little from the nonprofit. That's the 0.3 savings.

Now, on this point that Senator Mitchell has raised, it is a very important point. And I would like to first emphasize that the civil service retirement system is not a single system; it is divided into several benefit packages all within the same system, and the money from them is mingled and not kept separate.

You have, in addition to the coverage of the executive branch, the special provisions that relate to the Congress, to the congressional staffs. The air traffic controllers have special provisions. So it is all part of the same system, and the funds are commingled.

It is presumed that a supplementary system set up to social security coverage for these newly hired people would be treated in the same way, so that whatever contribution that would be made by new employees to a supplementary system would also go into civil service.

Now obviously, the supplementary system would be designed to be much less costly than the present system, because these people would be covered by social security, and you would be aiming to have the two together provide roughly the same protection; so that the liabilities of the new system, the liabilities of the system that you have created to supplement the Social Security coverage of the new hires, would also be lower. Their contributions would be lower. They would go in, and to an extent help finance going benefits, but the liabilities to the system would also be much lower.

In general, Senator Mitchell, I think it might be good for the record to indicate that the present civil service retirement system is estimated to cost about 40 percent of payroll—that's the overall liability of this civil service retirement system. Federal employees pay in now 7 percent, so that you have a very large part of future benefits paid to existing retirees and existing employees dependent upon general revenues either paid as the employer, the matching 7 percent, or just revenue support.

Senator MITCHELL. Well, Mr. Ball, if I may interject, it is high, but it is not as high as the indication in your remarks is, because if you subtract 7 from 40, you get 33. In fact, there are other contributing factors—there is the agency contributions and the return on investments—so that the Government share exclusive of those is somewhat less than 30 percent.

Mr. BALL. I agree with that. I didn't mean to say anything that was contrary to that, Senator.

Now, it's sort of, to me, like the situation in which every new employee that comes into the Federal civil service system creates a liability for the Federal Government of—I don't know whether these are the exact figures—about four and a half times what that individual will contribute. And I can hardly see how getting more and more people into the system under these circumstances makes the system more secure. On the contrary, cutting back the liabilities of the civil service retirement system by having less of the coverage protection for new employees paid for by the civil service retirement system seems to me an advantage to the system.

Now, I am sure you will want to have the civil service retirement system's actuaries testify here. They testified before the Ways and Means Committee and in effect said much what I am saying now.

The CHAIRMAN. Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

I want to compliment the Commissioners on their obvious attempt to reach an even-handed better balanced solution to a very vexing problem. I think the Commission has done an admirable job and a very good job, in fact, trying to find, as Dr. Greenspan mentioned, "the least-worst set of alternatives," because obviously everybody is going to be impacted by this, and you have to do it in a way that is the least harmful to the widest number of people.

The problem, though, is this: I have had hearings in Montana on the Social Security Commission package during the last week. The Deputy Commissioner of the Social Security Administration, Mr. Simmons, was out in Montana, as were other people who are experts in this area.

I can tell you, based upon the hearings that I have held that there is some relief on the part of senior citizens, and there is some relief on the part of various groups; but there are a couple of soft spots, and one is the one addressed by Senator Mitchell as well as Mr. Ball and the chairman of the committee—that is, Federal new hires.

Obviously the present beneficiaries of the social security system feel somewhat relieved, not very much, they don't like the delay in the COLA, but somewhat relieved that maybe the Commission and the Congress is finally getting hold of this and doing something about it.

On the other hand, Federal retirees, employees, and potential new hires see Congress coming up with something that is going to potentially harm them.

Now, I frankly believe that we have to in some way address that soft spot if we are going to shore up as much of the support we would like to have for the Commission's package.

Mr. Myers' report, which Mr. Trowbridge very helpfully suggested be included in the record, frankly does not go very far to solve that worry, that concern. I have that report before me, and basically Mr. Myers' words are that a supplemental CRS program would be developed, and it speaks in conditional future terms, which doesn't really satisfy the concerns of Federal new hires or even Federal employees or retirees.

So I would ask the Commission to help the Congress in flushing that out; that is, adding a little meat and blood to that. And the earlier we can do that, the better; because otherwise I think we are going to have a big problem on our hands.

Civil servants know that Uncle Sam now pays roughly 65 percent of the total amount, and what the matches are, and they know they have been doing pretty well by the present system. And obviously, the more those facts come out, the more other people who are not civil service employees begin to wonder who is getting the better deal here.

Nevertheless, I strongly suggest that the Commission help us and the Congress—both sides, the House and the Senate—address that problem in advance and soothe those concerns as much as we possibly can. Mr. Myers' memo is helpful; it does not go far enough.

Dr. GREENSPAN. Well, Senator, one difficulty we have is that we legally go out of existence on the 20th of the month, but we will endeavor to be of whatever assistance we can.

Senator BAUCUS. I hope you do, because I do think it's this part that has to be shored up.

The second concern, the second soft spot I detect, is in the area of small business self-employment tax. It just seems to me that the small businesses are in a more difficult position to absorb the acceleration of the payroll tax increases than, say, big business that can't pass on the cost quite as well; and, second, the self-employment tax as well as the payroll tax of small business, even though there is a business expense deduction, impacts more heavily upon smaller businesses—that is, those whose income tax liability is in the lower brackets—than it does in sole proprietors or others who are in a higher income tax bracket. I'm wondering what advice you might have for us as we attempt to solve that problem?

Mr. TROWBRIDGE. Senator, I think you are clearly right in that the small business community by and large sees this as just one more increase in the cost of employment, and it is of great concern to them.

I don't have any magic formula as to how to lessen that load. It doesn't seem to me that we can make a distinction on the basis of size.

It would also strike me that the compromise package is fair, in that it does bring the self employed into the same level of treatment of employer-employee contributions as the incorporated business. And I think that is one strength of the proposal.

Going back, if I may just for a moment, to the Federal employees and their concern, it was part of our assumption as you know from the report that the Congress would put in place a supplemental civil service retirement system to cover those new hires. I believe in the House of Representatives the appropriate committee has already begun to hold hearings or at least give consideration of how to design such a parallel action on the part of the Congress that would presumably take place in time to apply, as this does, on the 1st of January next year.

Senator BAUCUS. I appreciate that. I also feel, as the Commission states, that this package largely has to rise and fall together. It's the unraveling point that Senator Danforth mentioned.

On the other hand, as you mentioned, Bob, certainly we can make some adjustments. One person's adjustment might be some other person's unraveling, but nevertheless I think in these two areas, in these two soft spots I mentioned, we can certainly make some adjustments. And we'll have to.

Mr. BALL. Senator Baucus, on the self-employed, I would like to make two quick points.

One is that to my mind this is one place where the Commission recommendation is correcting an inequity. Everybody in the system, other than the self-employed now pays somewhat more because the self-employed are only paying one and a half times and are getting the same protection.

Now, there is a way that you might want to consider of easing into this a little bit; that is, the suggestion I am about to make was not covered by the Commission, and I am not doing anything to unravel it thereby.

You remember that in the Commission's recommendation the employee contribution, while it moved up from 1985 to 1984, is offset in a refundable tax credit. We never really addressed the question of how to treat the employee side in 1984 when we adopted the rationale that the self-employed should pay both the employer and the employee tax. We did address the point that the employer's share should be a business expense and deductible, but we didn't really address the question of should the employee share of the self-employed tax be treated, for the 1 year of 1984, as a refundable tax credit, as the employee tax will be treated.

I think it wouldn't take much of an extension of our philosophy to say, "Well, as a way of easing in the self-employed to this, you might consider that."

Senator BAUCUS. Would you support that?

Mr. BALL. I don't think my supporting it matters very much, but I would, yes.

Senator BAUCUS. Would anyone on the Commission disagree with that change?

[No response.]

The CHAIRMAN. As a member of the Commission, I'd like to say that we didn't consider a refundable tax credit. However, we did consider a credit early in the negotiations and we were told by a representative of the NFIB that they preferred a tax deduction. They wanted to be treated like other employer entities.

To accommodate Mr. McKevitt and others who opposed the package, we changed that credit to a deduction and this was adopted by the Commission. Refundability caused some problems, but the credit itself was not a major point.

Mr. TROWBRIDGE. Senator, I might just add that within the Commission I think there was a good deal of disagreement on the basic tax philosophy of that refundability credit for the employee, particularly in that it took the employer-employee 50-50 relationship out of balance for 1 year.

It was one of those things we swallowed hard on and said we'll live with for a year, and we are confining strictly to one year.

Senator BAUCUS. Right.

Ms. FULLER. I'd say that the existence of the refundable tax credit with its infusion of general revenues was the most difficult part of the package for me to agree to. I think to extend that any further—I can't see how I could support that.

Senator BAUCUS. All right. Thank you very much.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Bradley?

Senator BRADLEY. Thank you very much, Mr. Chairman.

First let me say to the Commission that I think you have performed extremely well, and I think you have played a very important role in this whole process. I think if we can look at the MX Commission and a variety of other potential commissions, you will probably be called upon to play any number of roles in the next few years; but I think from the standpoint of social security your suggestions and the bipartisan nature of the body, and the ability to ultimately reach a compromise suggestion, has been extremely helpful, I think, for all of those of us up here who believe that Government isn't just a matter of those who are in Government but all of us. So I want to thank you very much for your work.

I would like two areas of questions. One is, I am sure that you are aware, I think Mr. Ball said that it was the first thing you agreed upon, which was the Federal employees. But there is a very real sense out there that somehow or another if you go to a system where new Federal employees are included in social security, that this will have an effect on those who are currently in the civil service system. What would be your response to that?

Dr. GREENSPAN. It is very difficult to answer those questions, on the grounds that almost anything that happens in legislation affects something.

Ultimately, you are asking us to forecast how the Congress will behave, and clearly we are not the most appropriate people to do that.

Our suggestions are that Congress do certain things with respect to this, but——

Senator BRADLEY. Your suggestions are that the Congress in another committee would devise a civil service retirement system that would get those new retirees up to the present level of the existing retirees. Is that not correct?

Dr. GREENSPAN. That's implied in much of our recommendations, although we do not specifically stipulate in any considerable detail what the Congress should do; but I think a large number of us have explicit assumptions which pretty much go in that direction.

Senator BRADLEY. Is there any other suggestion that you could make—or range of suggestions, not one but several—that you think we might consider, to try to alleviate this fear on the part of current recipients that somehow or another their retirement is going to be affected if we do adopt the provision that you have recommended on new retirees?

Dr. GREENSPAN. Senator, my major problem with that is that I think they are mistaken. What you are asking me to do is to construct a rationalization or rationale to try to convince somebody who is factually mistaken.

Senator BRADLEY. All right. They are factually mistaken how?

Dr. GREENSPAN. Well, they are factually mistaken in the sense that there is a liability out there with respect to the Civil Service retirement, and there is a history of how the Congress has behaved.

There has never been any semblance or a sense of ungenerousness on the part of the Congress—if anything, a lot of people have argued that it's been the other way around.

I have been a Federal employee. It never entered my mind that one thing about Federal employment was that the pension system was inadequate.

Remember there are really two issues here. One is a question of what extent does the new hirees' input significantly affect the current system, and I think Mr. Ball appropriately addressed that.

The second question is that the new hirees are not now in Government. They won't be in Government, by definition, for——

Senator BRADLEY. They will enter Government with the understanding——

Dr. GREENSPAN. Yes; when one gets hired, one understands the conditions of employment, and one can either chose or not chose to become a member of the Federal Government.

Senator BRADLEY. So you are saying, essentially, that while there is this theoretical gap out there for present retirees, meaning that somehow or other the Federal Government won't fund its portion of the liability, it is there now for all intents and purposes.

Dr. GREENSPAN. Yes.

Senator BRADLEY. The record indicates that indeed Government has always funded its part of the retirement system.

Dr. GREENSPAN. Yes, sir.

Senator BRADLEY. That's basically your argument.

On the taxing of benefits, does it make any sense to think about taxing half of the benefits received of nonsocial security incomes over $25,000 in a joint return only after the individual has received everything they have put into the system plus interest, which would be roughly 3½ years? If so, how would that affect the revenue numbers?

Dr. GREENSPAN. Senator, that was one of the issues which was considered and ultimately discarded. I do not recall the revenue effect of that, but it is probably not insignificant.

Senator BRADLEY. What was the nature of the debate? Anyone else on the panel?

Dr. GREENSPAN. Well, I do recall we did discuss it. Bob, do you recall?

Senator BRADLEY. Let me ask Mr. Ball. Does that make any sense?

Mr. BALL. Senator, it would make sense to me if you were putting social security on an exactly parallel basis or close to a parallel basis with other retirement income. It is not, and hasn't been.

For example, the general tax policy for a contributory private plan is to do what you suggest—once the individual has recovered his own contribution, then the entire benefit is taxable. For an entirely employer-paid-for plan, the whole benefit is taxable right away.

Now, we have approximated that for these higher-income people by saying,

> Well, one-half of the benefit can be attributed to the employer's tax and one-half to the employee, and for that reason we are suggesting that you tax, at a maximum, one-half of the social security benefit, the part attributable to the employer.

The employee, after all, has paid an income tax throughout his working career on social security contributions.

Now, if you were to make the kind of a modification that you suggest, I suppose then, one would tax the entire social security benefit after the contributions had been paid back as you do in civil service.

Senator BRADLEY. No, what I am trying to address—I am sure all of us having come back from a recess of being out there are reacting to what people have said, but one of the things that I found was not known was how quickly you get back everything you put in plus interest. Now, that's going to increase over time, but right now it is not a very long period of time.

The second thing I found out there was that people are afraid of the taxing because, while you say $25,000 now, they feel you have broken the threshold and gradually you will come down.

An antidote to that that I found was if you simply say that you won't have to pay any tax until you have gotten back everything you have put in plus interest. My question was, if you have the number, what would be the effect of the revenue if you did that?

Mr. BALL. Senator Bradley, just a point on the way by—and I am trying to find a number in here that might help your factual question.

To be parallel to other retirement income policy you wouldn't want to include interest. In civil service you start to tax the entire civil service benefit as soon as you have recovered what you yourself have contributed, usually within a couple of years—1½ to 2 years.

If I could take the time, Mr. Chairman, it might be worthwhile on this taxation issue to show how extraordinary the tax treatment of social security benefits is, as compared with everything else, and how it happened. .

Social security is currently the exception, in having it exempt from income tax. There is no legislative history; it's entirely on the basis of an early Treasury ruling—a ruling which I personally think was mistaken—in which they held that social security benefits were a gratuity. A gratuity, not being taxable to the receiver, was not taxed. In the Commission, we came to the conclusion that that was not sustainable for people who had quite high incomes—and this proposal, of course, applies only to about 10 percent of the social security beneficiaries.

Now, I say that in a preliminary way to saying that if it developed that over time the social security benefit became taxable to more people, always with the limitation of one-half on the theory that that's the half attributable to the employer's contribution I see no reason why that wouldn't be acceptable.

The argument about postponement until contributions are recovered applies, I think, to the employee side of the tax. Our proposal for immediate taxation applies to the part of the benefit that was paid for 100 percent by the employer. It was never taxable to the employee, and the employer charged it as a business expense. But I don't see the justification in the postponement you suggest on the basis of general tax policy, unless you were to end up taxing the entire benefit.

Senator BRADLEY. Thank you.

The CHAIRMAN. I wonder if we might accommodate Mr. Waggonner. I think Senator Long had some questions he wanted to ask Mr. Waggonner, who has to catch an airplane. Would that be all right with Senator Boren and Senator Matsunaga and Senator Long?

Senator LONG. Mr. Waggonner, I may be putting you on the spot, and I hope you don't object to what I'm getting ready to say.

You are one of the President's appointees on this Commission, and I would think that the President is probably disappointed when he sees that the Commission came up with a recommendation where Mr. Greenspan and Mr. Ball could get together on it; Mr. Dole and Mr. Pepper could get together on this; Mr. Trowbridge, representing the National Association of Manufacturers, and Mr. Percutt, representing labor, could get together; Mr. Conable and Mr. Moynihan could get together; Mr. Heinz and Ms. Keys could get together over the matter; President Reagan and Speaker O'Neill could get together; but you couldn't agree with them.

I fear you might have reduced your influence with the President. I've got my doubts that he is going to put you on another commission to make a recommendation, Mr. Waggonner.

I know that you did what you thought was a point of honor, and I know that the same thing is true of two Republicans who had a responsible position, Mr. Archer who is a ranking member on the subcommittee over on the House side and Mr. Armstrong who is chairman of our Social Security Subcommittee.

I wish you would respond in support of your position, and tell us what you think will happen if we do nothing. In other words, if we don't pass this recommendation, or something very close to it, then I would think that there will be difficulty getting what we do agreed to on the House side, and some people would say that this would jeopardize the effort to save the social security system.

I wish you would tell us, as a fellow who has been in this legislative mill down through the years and who has been a very responsible member of the Committee on Ways and Means, what scenario do you picture in terms of what our options are in the event that we don't buy this commission package?

Mr. WAGGONNER. Thank you, Senator.

When the President asked me to serve on the Commission, he didn't ask me what I would do. If he had asked me for a commitment beforehand, I wouldn't have taken it, either, if I could not come to express my point of view. But nowhere along the way did he ask me what I might would do; but if I didn't have a track record after nine terms here, he had missed the reading of history, at least about what my opinion about social security might be. I think he respects conviction and independence.

But the thrust of your question is, first, why we have the luxury of doing nothing.

Senator LONG. I am just asking you the same question that was asked by Mr. Danforth, basically, what do you think our options are? What scenario do you picture? That's what I want to get at.

Mr. WAGGONNER. You do not have the option of doing nothing. You must do something, and I am confident that you will do something.

On the House side, if I remember correctly, Congressman Vander Jagt said this just happens to be the only game in town. It is the only game in town if you don't want to play any other game. If you don't want to give any consideration to anything that adds to or takes from the recommendation, and if you make the political judgment that if, by changing that, then you lose the opportunity to do anything, that you ought to go with this, then that would be a logical decision.

I do not believe that either body will take the point of view that we need not, we should not do anything. If you can you should improve it.

If I still sat on the House Committee on Ways and Means, it would still be my observation and my approach that I had disenfranchised not just myself as a member of the committee but everybody I represented if I was not allowed the opportunity to do what I thought might be better, even now or in the long run.

I would not take the point of view even now, if I was there, if I sat on Ways and Means, and I have not and would not say, if I had a final vote on that committee or on the House floor, that I would vote against this package to at least go to conference; because if I got shut out of a conference, I would lose my voice. I would play some politics, too. I always like to stay in the circle.

But I would not want to be put into the position that I could do nothing except, Yep, this or nothing. I would want the opportunity.

I do believe that in a matter of 2, 3, 4, days that in some of these major issues you people can consider it. If you want another game, improve the part if you can. I think you ought to.

I don't criticize my colleagues of this Commission for having done what they have done; my criticism is, if I was a member of the Congress still, I am not sure that I would want this Commission making my political decision for me like what I ought to vote for, when the time comes, if I had a better idea. Do I explain myself?

Senator LONG. I think you did.

Mr. WAGGONNER. I do have some criticisms, some major criticisms, about certain aspects of it, and maybe in the final analysis, neither committee, neither body, nor the conference would do anything better. If they didn't, I would go ahead and do something; but there are some major, major problems here.

I do take issue with the idea that in the short range we are home safe. I think it's very, very fragile. I think almost everybody agrees that it's a much worse situation in the long range.

The Commission has recommended nothing about a fail-safe device. We've talked about one, but I think it should be a major part of the legislation, just for its own sake.

Senator LONG. It seems to me, if we do amend this bill in the Senate, then the House is going to have to talk to us and at least consider our amendments.

Now, I know there will be a suggestion made that we have no choice but to go along with the House bill, that it's that or nothing if we do amend the bill in the Senate. I would just like to have your thought about the matter. You are familiar with the legislative process, what it is like to go to conference. What is your thought about that?

Mr. WAGGONNER. Well, I would like the opportunity to go to conference with two different bills. I just think you, right here in the Senate, can do a better job than what the Commission has recommended.

Look, the Commission has given further than I would at this point to get a consensus. I just think that you would come with a better bill if you took some other options and then made some decisions in your conference, when you do get to conference with the House of Representatives.

I think you can write a fail-safe provision. I think you can strengthen it in the long range. And look, Mr. Pickle was completely correct when he told Mr. Pepper that it was inevitable somewhere, at some point in time, something is going to have to deal with the facts of life as far as demographics are concerned.

But Mr. Pepper is completely wrong when he says, "Don't now, don't ever, do anything about it. I'll be opposed to anything that's ever done." He's not that good. He is making decisions for future generations without their views.

Senator LONG. Thank you very much.

The CHAIRMAN. Senator Boren?

Senator BOREN. Thank you, Mr. Chairman. If I could come back to Senator Bradley's question just 1 minute ago, I wonder if anyone on the Commission does have the number, what revenue would have been produced if we strictly applied the same rule to social security that we applied to civil service, and that is taxation of the portion once the amount paid in were returned to the recipient, income tax being applied to the remainder? How much would that have raised? Your figure is what? About $40 billion that would be raised over the next 5 years by taxing one-half, as I recall.

Dr. GREENSPAN. Yes, but I think Mr. Ball raises an interesting question, which is, that principle then presupposes that you then tax 100 percent of the contributions after all moneys come in.

Senator BOREN. Yes, I understand that. I am just wondering what the figure is.

Dr. GREENSPAN. But that would be a higher rate of taxation. That would raise more revenue.

Senator BOREN. Yes; I know it would. I just wondered what that number would be.

Dr. GREENSPAN. I don't know. We don't——

Senator BOREN. Do you have that number?

Dr. GREENSPAN. I don't think it has ever been calculated.

Mr. BALL. I think the figure, under the new estimates, for taxing one-half of the benefits under the proposal would be $26.6 billion.

Senator BOREN. Right.

Mr. BALL. If you would leave that just the same or not have it go into effect for the next couple of years you would move all these numbers forward, I suppose, and you would lose the higher years, of course.

Senator BOREN. Right.

Mr. BALL. So that just roughly, I would think, if that's what you did, it might be as much as $13 billion—almost half of it would be lost.

Senator BOREN. Right.

Did I understand the Commission did consider increasing or phasing up the retirement age over a long period of time? This did get a majority of support but not a sufficient support to constitute a consensus? Is that correct?

Dr. GREENSPAN. That's correct.

Senator BOREN. I think that's disappointing. In the public hearings that I held in Oklahoma there was very strong support, particularly among younger people. You just looked at the figures of what's happening to the longevity in our society, and I think any rational person looking at those figures would realize that that's a long-range reform that has to be made.

What about another proposal that received almost unanimous support, and I was surprised by the very strength of it because there were a number, I would say half of the people in the audience at each hearing were civil service employees, and that was adding to the number of quarters necessary to be a part of the base to qualify for social security benefits, to obtain coverage. In other words increasing the present 7½-year period and making that 15 years or some substantial longer period of time. Did the Commission consider that? Was any vote taken in the Commission on that?

Dr. GREENSPAN. There was no vote taken. It was discussed, but there was apparently, as I recall it, no strong support to move in that direction.

Senator BOREN. Couldn't that potentially save a great amount of money and also prevent the problem of what we call traditional double-dipping in the future?

Dr. GREENSPAN. Yes. Senator, I think you could probably list 10 more similar such suggestions, and I would personally probably agree with 9 of them.

Senator BOREN. Right.

Dr. GREENSPAN. The trouble, however, is that we were confronted with a very odd type of problem, an absolute necessity for solving this particular fund shortfall, with a whole series of recommendations on which we could find a mechanism by which we would get the aggregate amounts of dollars we need——

Senator BOREN. Right.

Dr. GREENSPAN. In a manner in which we could get people to sign off——

Senator BOREN. I understand. I understand the problem. I think the nature of the problem is the reason that the Congress and the administration previously defaulted and handed this ball off to the Commission.

Dr. GREENSPAN. This is precisely the reason why this is one of the rare cases in which having a Commission probably does work, in the sense that you have so many elements with which to deal that, if you go through, unfiltered, the whole legislative process, it is an extraordinarily difficult type of compromise to reach.

Senator BOREN. Right.

Dr. GREENSPAN. The Commission has been trying to predigest a lot of this stuff in a manner in which we would have very much the same kinds of problems.

Senator BOREN. Right.

Dr. GREENSPAN. We are, in effect, surrogates for the legislative and the executive branch——

Senator BOREN. I understand.

Dr. GREENSPAN. That's truly the only way I can answer you.

Senator BOREN. I commend you for trying to fulfill this difficult role and doing it very, very well.

Let me just ask this as a point of information: Did the Commission also consider the proposal that we not continue, at least in the future, to qualify nonresident aliens for benefits, from this point forward at least, benefits over and above what they themselves paid in? That's a proposal Senator Lugar and I and others have made in the past.

Dr. GREENSPAN. Senator, there were a number of such issues which were discussed at various different times, and we excluded them not because we thought they were poor ideas, but we decided that if we were to get involved in a long series of individual items over and above which we had agreed upon, we probably would lose our consenses somewhere along the line. We would be raising more problems for the consensus that——

Senator BOREN. Time became of the essence to get a conclusion reached.

Let me go back to one question again, because I am intellectually having difficulty in understanding the answer to the same question. We have gone around this barn three or four times now with the civil service and the social security; so let me try to phrase it a little differently, having listened to the answers to earlier questions.

If we create a dual system, which I gather the Commission envisions. If we call it a supplemental civil service benefit plus social security, then I presume that the idea would be that the benefits to be paid out by the combination of the two would be—and I have a little difficulty with figuring that out, I suppose—would be roughly equal to what the civil servant is getting now. So it would be a greatly scaled down supplemental civil service which, if added to the social security benefit, would give that employee roughly the same total benefit that it gives now. This was the concept. In other words, it would also. create the same total liability—I guess you could say it that way. If he is getting the same benefit, if he is entitled to social security plus this supplemental civil service, if you add A and B together, then that——

Mr. BALL. The greatest part of it is now social security, of course.

Senator BOREN. I understand that. The greater part would be social security, but you get the same thing, and you come up with C, his present civil service benefit; but now you are going to give him A plus B, instead, the greater part of it being social security in the future.

All right. Now, I presume also that you would have him pay in the same amount, total; unless you were going to have a further deductible. In other words, if it is going to be neutral on the Government employee, he is going to end up with the same combined benefit—social security plus supplemental civil service, and he will be paying in the same amount, unless you are going to give him a raise in pay or make him have a further cut in his take-home pay like we did with the medical insurance. Wouldn't that be correct?

Dr. GREENSPAN. Well, Senator, one way of coming at this is that we envisaged the unified budget effect to this whole process to be zero.

Senator BOREN. It would be neutral. All right. Well, that is exactly the point I was trying to get to. So the critics are absolutely right. In other words, if you are going to pay in—and we have to be concerned.

Social security—we have heard the comment about civil service, that you are paying in 7 percent, but the actual cost is 40 percent. So in other words you are getting back between $5 and $6 for every dollar really funded by the Government, plus whatever it has yielded in investment. It's not quite to that degree in social security, but it isn't just a whole lot better; it's to some degree better. Well, it would be significantly better if you add the employee and the employer; it's maybe half.

But even so, you are not meeting the full cost, obviously, of social security, either, by the employer plus employee contribution plus what it earns. You are maybe coming up with a third of its ultimate liability, I think. What is that? Four and a half or five years? You are going to draw for 16?

Mr. BALL. Senator, once the long-range deficit of 1.8 that we have been talking about is met by changes, then the entire cost of social security over the long run would be met by employer-employee contributions.

Senator BOREN. All right. I guess what I am getting at is this—and the answer is that it is revenue-neutral when you look at the unified budget. That is really the point, because when we look at the total impact on the total budget, if you say, well, the Government employee is not going to be paying in any more, and we are not going to be changing the total liability when we add civil service and social security together, then you have in the long run a neutral effect as far as adding to, as far as relieving the Government of any financial burden. It seemed to me that the only way in terms of the unified budget—I look at this really more in terms of the unified budget, because I know sooner or later we end up having to bail out whoever it is that gets in trouble, and we have to raise the money, whether we raise the money and pay it into an earmarked fund or we raise the money and pay it into the general fund; I realize there are all sorts of philosophical differences between those two approaches—you have to come up with the money.

It just seems to me reasonable that, if you are not reducing the liability, you are going to really give that civil servant the same combined benefit that you are now giving him; you are just going to give it to him out of two funds instead of out of one. If you are not going to increase what he pays in, in total, that you are not doing anything to relieve the problem for the unified budget, that you have zero impact.

Dr. GREENSPAN. Senator, that is exactly right, and it's precisely the answer which basically one could address to Senator Bradley.

Senator BOREN. Right.

Dr. GREENSPAN. In effect, you and he are looking at the same issue from different points of view.

Senator BOREN. Exactly, I was just trying to come at it again.

Dr. GREENSPAN. The fact of the matter is that the general thrust of this recommendation is not to address or have any signficant effect on the unified budget.

Were it to be the case, then the question is, how could one then argue that the purpose of the recommendation is not to reduce the benefits? Now, in fact, we can't have it both ways.

Senator BOREN. No.

Dr. GREENSPAN. The point is, either it is or it isn't. What we are stipulating is, we view this as being neutral with respect to the unified budget.

Senator BOREN. If the Congress were to implement it in a way that kept it as neutral, if we are increasing our income into the social security fund temporarily, it would have to follow that in the long run we are, therefore, increasing the liability of the other fund, in the long run. It may just be a matter of what part of the unified budget pays, and at what point in time it pays.

Dr. GREENSPAN. Sure. But Senator, that is not to say that what we as a commission are saying is that we consider that the civil service pension system is sound. I mean, that is not to say that the Congress should not address this de novo or review it as it always has.

All we are saying is that, with respect to this specific recommendation, we do not view it as something which improves the unified budget.

Senator BOREN. Well, I think that is a very important point, because I have been listening to people in Oklahoma say that all week long. They didn't say it does not improve the unified budget, but they said:

> You know, if you are going to be paying out the same amounts from two funds that you were going to pay out from one, and you are only going to be paying in the same amount you were previously paying in, I don't see how your total financial picture is any better.

In fact, one man got up and said, "You know," he talked to a man in the poultry business who is losing one penny on every chick he raised, and he said, "if he didn't have such a high volume, he'd be in real financial trouble." [Laughter.]

I just want to make sure we don't get ourselves into the same sort of shape.

But again, thank you for letting me run over, and I want to thank the Commission again, and all of you. You have contributed so much for it.

I think especially the Members of the Congress and especially the members of this committee realize exactly the cross currents you had to deal with and how difficult the task has been, and you have both all of our sympathy and all of our appreciation for what you have done.

The CHAIRMAN. Thank you.

Could I ask Mr. Ball to comment briefly before Senator Matsunaga?

Mr. BALL. Senator Boren, there is just one place where the solution of having part of the protection under social security and part supplementary civil service is cheaper. It's not a major part, and I agree generally with what Dr. Greenspan said, but we do cure one situation in which people who both get social security benefits and civil service benefits today are in effect getting amounts under social security that are higher than can be justified. They are getting it because they have short periods of employment in social security covered employment and——

Senator BOREN. Which can be secured by adding quarters.

Mr. BALL. All right. We have another proposal that goes in the same direction as what you are suggesting, to get rid, more or less, of the weighted-benefit formula as it applies to them.

Well, when you do cover people under social security and make their coverage under civil service retirement supplementary to that, there is an actual saving to the social security trust fund of 0.3 percent of payroll that is not made up for by the civil service system.

If you turn that around, you could say that the present situation is causing the rest of the country to absorb in their contributions what is really an unfair advantage for Federal employees.

I don't think many Federal employees understand exactly what I'm saying now, but we would be correcting a bargain situation that they are now getting and shouldn't get, and that is a saving for the unified budget, too.

Senator BOREN. Which is by actually reducing the combined liabilities, as I was saying a while ago.

Mr. BALL. It is for this group who have two types of coverage. You wouldn't want to retain the kind of bargains they now get.

Dr. GREENSPAN. You have to address that as a social security and not a civil service question.

Senator BOREN. Right.

Dr. GREENSPAN. In other words, the double-dipping issue is not related to the civil service issue; it's basically an issue of what constitutes the appropriate liability and payment under the social security system of those whose major, proportion of work experience is in the Federal Government.

The CHAIRMAN. Senator Matsunaga?

Senator MATSUNAGA. Thank you, Mr. Chairman.

I wish to join with my colleagues in commending the members of the Commission who have worked so hard in formulating these proposals.

Sometimes I think, that since you were appointed and not elected to the Commission, you were able to lay down a basis from which the Congress can at least come up with some legislation.

As former Congresswoman Martha Keys knows, we will need to carefully review these proposals. The one which has elicited the most discussion today and on which we are now receiving extensive mail the inclusion of new civil servants under social security. I wish that you would come up with arguments which could be raised in opposition to the ads which have been aired on TV and radio—"You can't cure a sick system by making a healthy system sick." Now, that is the type of advertising going on which is very effective and which generates a lot of mail.

So I think in States such as Hawaii, where there are so many civil servants—and I'm sure there are other States similarly affected—you need to find solid arguments to let people know all of the facts on this matter.

I would like to request a response for the record, rather than having the answers now. I would request that any additional points you would like to make be submitted to the committee.

Senator MATSUNAGA. Congresswoman Keys, do you wish to add something?

Ms. KEYS. Thank you my friend, I merely wanted to point out, that we went through this once before—the flood of mail, et cetera—with some attempt to legislate on this issue, in the 1977 bill. It seems to me as the Senator from our beautiful State of Hawaii, you ought to be able to tell people that they do gain a number of very positive things by being covered under the system: The survivor protection is so much better, the disability protection is so much better in social security; and back in 1977 when we were going through it, I, coming from the State of Kansas as the chairman does, had the occasion of having numerous casework of people who, because of their transferral from long years in covered social security employment at a fairly late age to Federal employment, found themselves facing a major disability and slipping through the cracks, of leaving the recency of work tests that would qualify them for social security coverage and disability and not having worked long enough yet to be covered under disability from the Federal employment.

So there are a good many features, particularly with regard to family protection and survivor protection, that you who are present leaders and we on the outside should continue to try to be as supportive and helpful in talking with groups should make and press.

Senator MATSUNAGA. Yes, Mr. Trowbridge?

Mr. TROWBRIDGE. Senator, I'm not sure whether you were present at the time that I introduced into the record Mr. Myers' memorandum on this very subject, trying to answer the charges as we have heard them in every form and every media.

Senator MATSUNAGA. Good. I'll take a look at it.

Mr. TROWBRIDGE. I think there are some good points in rebuttal there in that memorandum.

Senator MATSUNAGA. Fine. I'll be sure to read it.

There is just one specific question I would like to ask. We are asked this question quite frequently by people who don't know. Just for the record, your proposal would not require the payment a greater social security tax over and above the contribution of a Federal employee into the Civil Service pension plan.

In other words, would the new Federal employee be paying more because of his coverage under social security than a similar Federal employee who was hired, say, the day before coverage?

Mr. BALL. Senator, it certainly was not our intention or the intention of anyone, as far as I know, to have the newly hired Federal employee pay both the present level of contribution that now goes into civil service, plus social security. That would be, of course, very high.

By redesigning for the new hires a supplementary system to social security, it is of course much less expensive. So it would be social security plus something else.

Now, exactly what that something else would be we did not specifically address within the Commission. The Post Office and Civil Service Committee in the House and the comparable committee in the Senate will have to address that.

Senator MATSUNAGA. That, I believe, is going to be a problem which we are going to need to address.

Now, there is this other proposal of the Commission in which State and local governments which have elected social security coverage be prohibited from withdrawing from the social security system.

Do you foresee any constitutional problems in mandating that State and local governments pay the employer part of the tax if they wish to withdraw from the system?

Dr. GREENSPAN. This is an issue, Senator, which created a great deal of discussion within the Commission.

I don't think that the issue addresses the particular aspect, however, of the recommendation.

Bob, you are more familiar on that question than all of us at this stage.

Mr. BALL. Senator, in our recommendation we limit the use of the Federal power, you might say, to preventing withdrawal on the part of those groups who have elected to come in.

There is certainly a serious constitutional question about the ability of the Federal Government to just start to tax the States on a compulsory basis for those who have not come in voluntarily.

I am not expert enough to know whether this other approach will be subject to some challenge; it may well be. But it was the thought of the people that we consulted that it was much less of a problem, at the very least, in requiring people to stay in who had elected in, than it would be to bring in the others.

Senator MATSUNAGA. Well, the time is getting late. One more question, though: According to your report, you expect to raise, and we expect to raise if we adopt your proposal, $168 billion.

You have been hearing a lot lately about the jobs program, and obviously if we create a jobs program with more people employed paying into the social security system, the revenues would be greater.

Now, was your proposal based on any percentage of assumed unemployment?

Dr. GREENSPAN. Senator, we examined a wide variety of potential economic forecasts which obviously, each having in it a different unemployment rate, addressed the question.

We originally came up with a judgment that what had to be raised was somewhere between $150 and $200 billion, and we did that because a wide variety of forecasts, including those with high unemployment, lower unemployment, different levels of productivity and wage and price increases, gave us a spectrum of where the variety of different things would come out.

There is no question, obviously, that the higher the rate of unemployment, the lower the rate of receipts in the trust funds and the more difficulty the system would have.

In our judgment the types of recommendations that we made would address all but fairly unlikely economic scenarios with respect to the issue of unemployment.

Senator MATSUNAGA. Assuming that a jobs program is put into effect, then of course perhaps the answer is obvious—the $168 billion in receipts might even be increased. Is that not so?

Dr. GREENSPAN. Well, Senator, earlier today I testified before the Joint Economic Committee that I didn't think the jobs program was going to create very much in the way of jobs. I know of nothing that has changed my mind since this morning. So I would personally have to say that it has very little effect.

Senator MATSUNAGA. How about Mr. Ball, or Mr. Trowbridge or any of the others? Any comments on this? Because Dr. Greenspan has committed himself before another committee and changed his mind—even if he thinks otherwise. [Laughter.]

Mr. TROWBRIDGE. I would agree with Mr. Greenspan in that the real generator of new jobs is going to be economic recovery, Senator, as you well appreciate.

Senator MATSUNAGA. Yes.

Mr. TROWBRIDGE. I don't think that the numbers of new jobs that are being discussed as a result of the various so-called jobs programs would be of that magnitude that it would make that much of a difference in this particular case.

Senator MATSUNAGA. I agree with you, Mr. Trowbridge, but, the proponents of the make-jobs program could also have that in mind.

I for one have consistently proposed that we put small businesses back on their feet and give them incentives so that they will hire more people. Of course that would help the economy as well as create jobs.

While I'm on record for that, a news magazine recently quoted me on that, reporting as I would advise the President to do so.

Thank you, Mr. Chairman, and thank you for your patience. It's 5:00 now. I think it's about time we end this session.

The CHAIRMAN. Right. When does your authority expire? [Laughter.]

I think we have a little more time.

Dr. GREENSPAN. I'm inclined to say 15 minutes; but it's not a factual statement.

The CHAIRMAN. Mine expires in 15 minutes.

I think Senator Mitchell and Senator Grassley have a couple of questions. I have just one or two.

As a member of the Commission, I understand the concerns raised by other members. I just wonder after having heard all of the concerns expressed, is there some proposal that we overlooked in the Commission deliberations? Some painless way to raise additional revenue?

Dr. GREENSPAN. If I may speak for myself, Mr. Chairman, we were acutely aware that there are an innumerable set of proposed solutions to the size of the problem, and that each individual Member of the Congress would have a large number of suggestions, and we clearly have not been disappointed in that. It reinforces my own personal view that there is no simple ideal solution to this problem, that this compromise looks to me better and better as a potential solution every day that goes on.

I personally am concerned that in our desire to continuously look for alternatives we will end up with nothing. If we end up with nothing, the Nation will suffer problems which we have not yet really focused on, in my judgment.

The CHAIRMAN. Well, that's a concern. Although we want to move quickly, we certainly don't want to preclude anyone from offering additional ideas, and there may be some. One of the ideas I am hearing from various groups is, "don't cover us in the package." But that doesn't help. That could take away almost $20 to $30 billion. Others say, "don't tax benefits; don't include new hires; don't accelerate the payroll taxes," and my mother tells me not to delay the COLA.

Dr. GREENSPAN. My mother said the same thing. [Laughter.]

The CHAIRMAN. Well, if you do all of that you don't have anything.

Dr. GREENSPAN. Well, Senator, I suggest that perhaps you have hearings on means to increase funds into the trust funds, and then we'll perhaps get a whole series of different ideas from that side.

The CHAIRMAN. Both Mary and Martha have indicated some areas we should address, as far as women's equity is concerned. I would hope we might be able to include some of these provisions and make them effective, as you suggest, Martha, in the early 1990's. They are not that costly. Otherwise, if we determine that it shouldn't be done in this package, we at least ought to start looking at the options immediately.

We are looking at pension discrimination, equity in the pension system, which is another very sensitive area. And we hope we might be able to accommodate in this package the concerns that you and others on the Commission have expressed.

Senator MATSUNAGA. Mr. Chairman, if I might make a parting comment—I have an appointment to keep—I am very fortunate, my mother is in heaven.

The CHAIRMAN. Well, that's a point.

Ms. KEYS. Mr. Chairman, could I just respond, because I made the statement about 1990 without clarifying why I thought a comprehensive change such as earning-sharing would require waiting until that time.

The immediate recommendations, of course, I would hope would be immediately enacted.

The CHAIRMAN. Sure.

Ms. KEYS. As we know, there have been many earning-sharing proposals. They range in long-range cost from 0.06 to 0.36 of long-range payroll, depending on what is done.

Probably the best modified earning-sharing proposal was studied in depth by the 1979 Advisory Council and had a 0.12 percent of payroll cost; but basically the cost resides in two factors—transitional cost, which balloons and then diminishes, and whether or not you add new benefits such as the adding of disability benefits for all women that presently do not exist in the system.

Now, people differ on that. I personally think it's a good idea to do, but I think everybody should realize it isn't that it's a massive thing; it really is more complex because of its technical and administrative changes that would be required in such a restructuring.

Thank you.

The CHAIRMAN. I want to make certain, too. I think Congressman Jim Wright raised the question when he testified.

As I understand, it was the Commission's intent that Members of Congress be covered in this package. Is that correct? Even though Congressman Conable rightly pointed out that in some cases it might lead to a tax reduction rather than a tax increase for certain Members who have other income.

That would help us answer our mail. Under S. 1 the Social Security Commissioner would also be in the program.

There is another area of some concern that I haven't discussed. I indicated in my statement for the Ways and Means Committee that I would hope that we would try to keep the social security package pretty much the way it is, without adding unemployment compensation, and prospective payment, and railroad retirement, and civil service reform.

There are a number of ideas being generated on the House side, and I am certain if they are cooking over there they are boiling over here. Everybody has a few little things they would like to tuck into this package that don't really relate to the problem.

I hope you understand our real problem. If we start accepting amendments—all the tax amendments and other social security amendments that might be desirable at a later time—it could severely delay enactment of the package. Based on what Dr. Greenspan said earlier, the quicker we move, the quicker will be the response from the financial markets. Quick action would also allay a lot of the fears that people have that Congress just can't face up to tough problems.

So, if you can help us to encourage our colleagues not to load up this legislation—it's a little early for Christmas trees—we are going to try to keep it fairly clean over here.

Senator Grassley, do you have an additional question?

Senator GRASSLEY. Yes; I hope the subject of interfund borrowing wasn't discussed while I was out, because I want to ask a question on that topic.

The CHAIRMAN. It did not come up, not directly anyway.

Senator GRASSLEY. All right.

First of all, why did you continue interfund borrowing? My position is that once you find a solution, as your package supposedly does, for two-thirds of the long-range problems, why then it is necessary? Isn't the fact that interfund borrowing is included, evidence that it is not as sound a package as we have been led to believe?

My question comes from three standpoints: First, interfund borrowing isn't sound fiscally; second, it seems like the fact it is included in the Commission's recommendations made it easier not to include some other measure that required a little tougher decision; and third, and maybe most importantly, when you continue interfund borrowing you are just hastening the day we have to appoint a commission on medicare.

We hoped to have you serve a function to solve the social security problem forever. However, I don't want to have part of that decision make the situation worse for medicare. The mere fact that we know there's a medicare problem means we ought to be dealing with that now, not in 1986. But we don't have the capability of doing that, as evidenced by the fact we didn't deal with social security last year, or even 2 years ago, but waited until the last possible moment.

Dr. GREENSPAN. Well, Senator, we are certainly signalling in our report an acute awareness of problems of the various different funds. Our basic judgment about interfund borrowing in general really related essentially in the longer term to the disability and OASDI funds, and largely because the Congress has been continuously shifting those things back and forth.

Certainly, if there were no interfund borrowing you would have to deal with each individual fund separately, and it would be different. It is easier, obviously, with interfund borrowing than without it. There is no question about that, and that clearly is one of the reasons why we were moving in that direction.

Mr. BALL. Senator, if I could just add to that, I want to be sure that the record is clear on what the proposal is.

We suggested the continuation of interfund borrowing only through 1987, not for the long term.

Senator GRASSLEY. Yes; I am aware of that.

Mr. BALL. It was our idea that it was only a backup idea, that it is our expectation that you would never have to turn to it.

It was also, as is the 1982 form of interfund borrowing, only OASDI from hospital insurance.

Now, it is quite clear that it is going to be necessary for the OASDI program to repay medicare at interest. This is not a question of weakening the hospital insurance fund; it's a temporary borrowing authority which we hope will not be exercised. If it is, it will be necessary to pay back with interest, and the debt will be carried as an asset in the hospital insurance trust fund.

Senator GRASSLEY. I assume what is borrowed to this point is going to be paid back under your plan?

Mr. BALL. Yes, indeed.

Dr. GREENSPAN. That was very explicitly stated.

Senator GRASSLEY. You could argue, then, that your plan does at least put the medicare fund back at square one. Is that the assumption?

Mr. BALL. It makes it whole. It makes it so that it has not be injured by interfund borrowing.

Senator GRASSLEY. All right.

I bring this up again from recollection of a debate in 1977. At that time, in what I thought was one of the more responsible decisions of the House, we decided not to have interfund borrowing, and we also decided not to have borrowing from general revenues. I hope we are not losing ground in regard to the latter option.

Mr. BALL. Well, we haven't really talked about the ultimate failsafe that we all agreed should be in the program but couldn't agree on what it should be. I ought to make clear that the five of us who signed the same supplementary statement felt that the proper failsafe, which we hoped we would never have to reach, would be borrowing from general revenue, at interest, to be repaid. I didn't want to leave you under any false impressions.

Senator GRASSLEY. Well, assuming a responsible Congress, I think that's a responsible approach. But you can't always assume a responsible Congress.

Mr. BALL. Well, in social security, Congress really has performed extraordinarily responsibly over the whole life of the program. I have to defend the record of the Congress, really since 1935.

I wasn't there at the very beginning, but I must have been at almost all conferences between the House and the Senate from about 1950 on. Every change in the program right up to the 1977 amendment, every change was, in the judgment of the professional actuaries—I'm not saying they weren't wrong sometimes, but in the judgment of the professional actuaries—was completely and 100 percent soundly financed over both the short and the long term. The exception came in 1977 when there was no attempt to address the last 25 years of the 75 year estimate. Under the estimate it was sound for 50 years, but not 75.

The CHAIRMAN. Senator Mitchell?

I understand Dr. Greenspan has to leave.

Senator MITCHELL. Then I have a very brief line of questioning regarding the economic assumptions. I have reviewed the report. It is very complete, and you have printed certain tables of selected economic assumptions from the trustees' report.

I have been unable to locate in any single place a set of economic assumptions or a range of economic assumptions that you used in arriving at the figures in here.

I would like to ask you now, what are the economic assumptions upon which this entire report is based, and why are they not included? If they are, I would ask you to direct me to them. If not, why aren't they?

Dr. GREENSPAN. Senator, let me explain why there is no explicit set. We started off with the 1982 trustees' report, and it became fairly evident early on that neither the so-called alternative II-B or the alternative III were useful. The II-B was clearly far too optimistic. The alternative III had productivity numbers which just didn't make any sense.

In short, we had no specific set of economic forecasts which we found sufficiently useful to address the problem. As a consequence, we asked the Bureau of Economic Analysis of the Department of Commerce to employ their model to run a series of simulations for us in which we came up with a whole different set of potential funding requirements. Since there were a broad variety of them what we did, essentially, was to see what the shortfalls were and to try to make judgments which we all could subscribe to.

While we, obviously, could make all of those data available, we felt that largely because we were continuously moving along and that we did not in fact subscribe to any individual assumption, we believed that it was necessary to construct a set of recommendations which would resolve the problem within a fairly broad range of assumptions. Then, superimposed on top of that, we recognized that no matter what we did we could not fully insure the system against any conceivable economic disaster.

Senator MITCHELL. Nonetheless, in order to even arrive at a range—you used the figures repeatedly $150 billion to $200 billion—you had to have a range of economic assumptions.

Dr. GREENSPAN. Oh, yes, indeed we do. In fact, we have a whole series of runs by the Department of Commerce which we will be more than willing to make available to you.

Senator MITCHELL. Well, I would like to have, if I could, all of the data upon which you based that, because it has an implication on a lot of things—for example, taxing benefits for persons whose income other than social security exceeds $20,000 a year. You say that will raise $30 billion over a 6-year period. Clearly, you assume no increase in that level during that 6-year period.

Dr. GREENSPAN. Correct.

Senator MITCHELL. You also have to have assumed in the threshold determination of the range of deficit a certain level of inflation during that 7-year period, which means, effectively, an erosion of the $20,000 figure down to what level by 1990?

Dr. GREENSPAN. Well, that's quite correct, Senator. What I would like to point out, however, is that we did not use a single-base forecast for all calculations. The reason we didn't is that these deliberations were going on for over 1 year, and we were required to make adjustments along the way so that we were internally consistent as best we could. However, you will find that they are generally consistent, and certainly consistent in the range to make policy recommendations, and we will make those data available to you in what form you would like to see them.

Senator MITCHELL. Given the history of the economic projections in the past decade, I can understand a reluctance to rely on a specific set of numbers, and to publish them anywhere, because of the possibility of somebody coming up and saying 10 years from now, "Well, look, I told you so; look how far off you were."

But it seems to me—and I don't want to appear to throw a monkey wrench into this whole thing—one of the real problems that we have is the overselling of what has been done in previous years. There is a widespread—it is no longer scepticism, it is cynicism by people who just don't believe what anybody has said about this.

I think you have done a terrific job. Really, sincerely, I mean that. Yet, it seems to me, we ought to know before we vote on this what are the economic assumptions on which you are making these judgments? Because this could very well be, 3, 4, 5 years from now, a situation where we are back again.

Dr. GREENSPAN. Senator, we will make those data available to you, and we will see to it that whatever additional information is required to fill in those gaps will also be made available.

Senator MITCHELL. Thank you very much. Thank you, ladies and gentlemen, especially for your patience.

The CHAIRMAN. Could I just say in the same way that we really appreciate your willingness to come a long distance, in Mary's case, and to spend this time with the Senate Finance Committee. We have had 14 committee members here this afternoon; 12 of those 14 asked questions, so there is a great deal of interest. Two or three of the others are trying to get back to town. It is an indication that we very much appreciate and respect the work done by the Commission and your membership on that Commission.

I think it is important to state for the record that, obviously, the Commission could not address every single point that we are going to have to deal with in the committee. We have a notch problem in the proposal for taxing benefits and we have to address that. I assume we are going to have to find some way to pick up some additional revenue when we do that.

So there are a number of significant areas that we will have to reconcile in the committee deliberations or on the Senate floor. But without this compromise, in my view, we would have had a political bloodbath for 3 or 4 months to come. We would have had everybody pointing fingers at someone else until July when the retirement fund couldn't pay benefits any longer.

I believe, not just because I was one of those on the Commission, but also as an observer, that we owe a great debt of thanks to the Commission—particularly to the private sector members, Lane Kirkland and Bob Beck who could not be here today and the six who are here. We appreciate their work very much.

Senator MITCHELL. Mr. Chairman, could I also just say that I want to make clear that I did not mean to suggest that anybody here was overselling it. In fact, I have seen Dr. Greenspan on several television shows and have read his statements, and I commend him for his restraint in presenting this and in fact what I assume is his awareness of the overselling that has occurred in it.

Dr. GREENSPAN. Thank you.

The CHAIRMAN. We will recess until 9:30, at which time we will have Congressman Archer, Congressman Pepper, and Congressman Conable, followed by the Social Security Commissioner, Jack Svahn.

Thank you.

[Whereupon, at 5:20 p.m., the hearing was recessed, to be resumed at 9:30 a.m., Wednesday, February 16.]

NATIONAL COMMISSION ON SOCIAL SECURITY REFORM RECOMMENDATIONS

WEDNESDAY, FEBRUARY 16, 1983

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 9:34 a.m., in room 2221, Dirksen Senate Office Building, Hon. Robert Dole (chairman) presiding.

Present: Senators Dole, Chafee, Heinz, Armstrong, Grassley, Pryor, Long, Bentsen, Moynihan, Baucus, Boren, and Bradley.

[The opening statement of Senator Dole follows:]

OPENING STATEMENT OF SENATOR BOB DOLE

It is my pleasure today to welcome three of my colleagues on the National Commission on Social Security Reform and in Congress—Congressmen Pepper, Conable and Archer. As I pointed out yesterday, when we heard from the noncongressional members of the Commission, reaching a consensus would have been impossible had it not been for the diligence and the spirit of cooperation shown by each of the members. We are particularly honored today as there are few, if any, Members of Congress whose knowledge of social security and dedication to the program surpasses that of these three gentlemen.

By now, the Ways and Mean Committee has completed its hearings on the recommendations of the National Commission and is preparing to mark up legislation. It is my hope that our House colleagues can both alert us to possible problem areas as well as provide us guidance as to achieveing out common objective—a social security financing bill on the President's desk by the end of March.

I would also like to welcome Social Security Commissioner Svahn. The committee will certaily benefit from the perspective he can provide after 2 years of service as Commissioner. We will be interested in his views on the broad issues of social security financing and the administration's position on the consensus package as well as on the more technical issues pertaining to the implementation of the provisions in the package.

For the information of the public, our hearings will continue with public witnesses on Tuesday, February 22, at 10 a.m. We plan to have 3 full days of hearings.

Once again, I welcome our witnesses this morning and look forward to hearing their testimony.

The CHAIRMAN. This morning we continue hearings on the recommendations of the National Commission on Social Security Reform.

I am very pleased to welcome this morning three of our colleagues who served on the National Commission. Yesterday we heard from six Commission members from the private sector. Two members, Mr. Beck and Mr. Kirkland, were unavoidably absent.

We are particularly honored to have the three key Members of Congress from the House who spent a lot of time working on the compromise. There hasn't been total agreement, but I think the point is that we all understand there is a serious financing problem. Every one of the members of the Commission, whether they were able to vote for the compromise or not, understand the need for Congress to act very quickly.

I would be very pleased at this time if my colleagues—Congressman Archer, Congressman Conable, and Congressman Pepper—could all come up. It's not a panel. You can proceed individually, but I thought we would like to have you all up here so we could look at your smiling faces.

Mr. PEPPER. I always like to be in good company, Mr. Chairman.

The CHAIRMAN. Claude, do you want to start?

Mr. PEPPER. Whatever your pleasure.

The CHAIRMAN. Fine.

STATEMENT OF HON. CLAUDE D. PEPPER, A U.S. REPRESENTATIVE FROM THE STATE OF FLORIDA

Mr. PEPPER. Mr. Chairman and members of the distinguished committee, it's a great privilege for me to be here this morning joining my distinguished colleagues in support of a package which I think will stand out significantly as a great accomplishment of our time in the preservation of a great program, one of the greatest of our time—social security.

I can sum up what I'm going to say altogether very succinctly. By the way, Mr. Chairman, I have a written statement, if I may offer it for the record.

The CHAIRMAN. It will be made a part of the record.

Mr. PEPPER. Thank you.

[The prepared statement of Mr. Pepper follows:]

TESTIMONY OF HON. CLAUDE PEPPER, CHAIRMAN, HOUSE COMMITTEE ON RULES

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TESTIMONY OF THE HONORABLE CLAUDE PEPPER
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U.S. HOUSE OF REPRESENTATIVES

February 16, 1983

No single function of government affects as many Americans as profoundly as the retirement, survivor, disability and health insurance protection provided by the nation's social insurance system: social security. Over 94 percent of America's aged receive a monthly retirement check, and 24 1/2 million disabled workers and their spouses and children receive disability insurance benefits every month. Altogether, more than 36 million beneficiaries receive a check every month and 116 million workers contribute through the payroll tax to social security.

Between its inception in 1939 and the present date, social security has transformed the economic well-being of virtually every man, woman and child in America. The dramatic reduction in the incidence of poverty among the aged, for example, can be attributed almost completely to social security. If not for social security, 15 million elderly Americans would live below the poverty line — about four times the present number. Social security is the primary source of income to 60 percent of all persons aged 65 or over, and is virtually the sole source of income for 28 percent of the elderly.

Although most Americans think of it as an old-age pension, social security is far more important, broad-based and comprehensive than any pension program. All 116 million contributing workers are building vital protection for themselves and their families. Social security is important to current workers not only because of the retirement, life and disability insurance protection it provides — social security relieves them from the financial burden of caring for aging parents, giving independence and dignity to each generation.

Currently, 139 million people of all ages are insured in the event of death or disability, and 95 out of 100 children have inflation-proof survivor protection. In short, Mr. Chairman, social security is a program for the ages, and for all ages.

Recent concern over the financing of the nation's social insurance system has placed social security at the center of a national debate, the outcome of which will be felt by everyone in America. The National Commission on Social Security Reform, on which I had the honor to serve as an appointee of the Speaker of the House, was a product of this national debate. Before proceeding with a discussion of the provisions of the Commission report, I would like to address the question of the system's financing.

(The Commission chose to limit the scope of its recommendations to the cash benefit programs — the Old Age, Survivors' and Disability Insurance system. In general, the factors affecting the financing of the cash benefit programs such as real wage growth and employment are distinct from those which affect the financing of the Hospital Insurance program such as health care costs and utilization. Accordingly, the quadrennial Advisory Council on Social Security will limit the scope of its 1983 report to the HI program.)

OASDI Financing in Perspective

The Short Range (1983-1991)

One of the most important by-products, and certainly the most tragic, of the recent financing debate has been a considerable erosion in the confidence of the American people in their social security system. Millions of young workers believe that, when their turn comes to collect from the system that they have paid into for decades, no funding will exist for the payment of benefits. In short, they believe that the U.S. government will have sold them out.

For too long, public officials, elected and otherwise, serving in responsible positions have abused the public trust by shamelessly engaging in scare tactics. The shrill references to "impending collapse" and "going broke" have needlessly frightened millions of Americans with loved ones dependent upon social security. These dire, doom-and-gloom predictions had more basis in ideological hope than in fiscal reality.

The truth is that those reports of imminent bankruptcy were greatly exaggerated. social security's funding problems are basically of a cash-flow nature, with incoming contributions falling barely short of the amount needed to cover all benefit obligations.

Social security cash benefits are financed from current payroll tax contributions. The contribution rate is set to coincide with the OASDI cost rate so that current contributions will roughly equal current benefit obligations. Any surplus of revenues over outlays is held in the OASI and DI trust funds, to be held for future years in the event that outlays exceed revenues.

The OASDI trust funds are simply a contingency reserve. It is no catastrophe for the trust funds to be drawn on — that is precisely the purpose for which they were created. If an extended duration of deficits occurs, the drawing down of the trust fund assets allows an uninterrupted flow of full benefit payments. This buffer provided by the trust funds gives the Congress the time necessary to adjust the contribution rate or to consider other financing measures.

As a contingency reserve, the trust funds do not contribute significantly to the system's financing. They are comprised of assets built up during years in which benefit obligations did not entirely consume incoming revenues, and they serve to fill in the gap when incoming revenues do not entirely cover benefit obligations. In short, the Commission was considering and we are here discussing the financing of OASDI at the margin — most of the future benefits promised by the system are already funded under current law.

Specifically, between now and 1991, the OASDI trust funds will collect $2.230 trillion in payroll tax contributions and disburse about $2.267 in benefit payments under current law. This amounts to a discrepancy of about 2 percent; that is, contributions will fall short of benefit obligations by about 2 percent of the latter. While this amount may be large in terms of dollars — social security is, after all, a large program — a 2 percent shortfall is hardly of sufficient magnitude to justify the chicken-little cries of an impending collapse.

Nor is the shortfall the result of some basic flaw in the benefit formula or some other fundamental defect in the system. Rather, the funding shortfall is attributable to the poor performance of the economy during the past decade.

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By their very nature as part of a contributory social insurance system, the OASDI programs are sensitive to the performance of the economy. Because system revenues are based on wage growth and the proportion of contributing workers, and outlays are keyed to price growth, fluctuations in the rate of employment and the growth rates of wages and prices have a dramatic impact on the stability of the program.

For example, the social security actuaries estimate that each percentage point of unemployment costs the OASDI programs $3.5 billion in lost revenue annually. At full or near-full employment (4 percent unemployment), the OASDI programs would be solvent for at least the next half-century. Unfortunately, the present record levels of unemployment are robbing the system of its revenue base, and are even increasing its benefit obligations to the extent that older discouraged job-seekers are forced into claiming early retirement benefits.

Real wage growth, the other crucial determinant of the system's fiscal health, plummeted to unprecedented levels during the 1970's. Historically, the real wage differential exceeded 2 percentage points prior to 1970; that is, wages in covered employment grew faster than prices as measured by the CPI by 2 percent annually. During 1970-82, however, recurrent cycles of inflation and recession produced 7 years of negative wage growth. At the very time that low wage growth cut into the OASDI revenue base, high levels of inflation substantially increased benefit obligations.

The extended duration of poor economic performance shrank the OASDI trust fund reserves from $35.3 billion at the end of 1972 to $17.3 billion at the end of 1982. Not surprisingly, the performance of the economy will be the most influential factor affecting the system's financing in the next few years.

Table I illustrates the enormous impact of the economy on the cash benefit programs. Under the more pessimistic of the two mid-range sets of assumptions (alternative II-B) the excess of outgo over income during 1983-1991 is $37 billion, or 2 percent of expenditures. Approximately $65 billion in additional revenues would be required to maintain adequate reserves for uninterrupted payment of benefits under this economic scenario. It should be noted that a cost-of-living adjustment of 7.9 percent is projected for 1983 under this assumption, while the actual COLA is now expected to be about 4 percent.

Looking at the other of the two intermediate sets of assumptions, alternative II-A, substantial surpluses begin to accumulate in 1985, with a total net increase in trust fund reserves of $168 billion during 1983-91. By the end of 1991, the OASDI trust funds would have reserves exceeding $185 billion, or about 59 percent of the next year's outgo.

TABLE 1

Estimated operations of the OASDI trust funds
on the basis of the 1982 Trustees' Report assumptions,
calendar years 1983-1991*

(dollars in billions)

	Alternative I	Alternative II-A	Alternative II-B	Alternative III
income	$2348.0	$2287.4	$2230.0	$2,248.2
outgo	2042.2	2119.3	2267.2	2,545.1
net increase in funds	$ 305.8	$168.1	$ -37.2	$-296.9
additional funding required**	—	—	65.4	312.5
1983 trust fund balance***	10%	10%	11%	11%
1991 trust fund balance	82%	40%	-12%	-59%

SOURCE: Tables 5a-5d, Appendix K. Report of the National Commission on Social Security Reform, January 1983.

* OASDI programs as modified by the Tax Equity and Fiscal Responsibility Act of 1982

** amount of additional revenues or outlay savings required for uninterrupted payment of benefits

*** assets at beginning of year as a percentage of outgo during year.

The so-called "optimistic" and pessimistic" assumptions (alternatives I and III, respectively) illustrate the impact of economic extremes on the OASDI programs. Under the pessimistic scenario, annual average deficits of $33 billion would result. Conversely, surpluses averaging $34 billion annually would occur if the optimistic assumptions prove correct. I would add that the 1982 pessimistic assumptions have been revised in order to account for current experience of higher unemployment and lower inflation, which results in a somewhat smaller deficit.

The long range (75 years)

Although much is said and written about the projected status of the trust funds 75 years from now, the truth is that very little is known. Assumptions made with respect to inflation, wage growth, GNP, employment, longevity, immigration, interest and birth rates are just that — assumptions. I would submit that there will be other factors which affect OASDI financing, ones we cannot even contemplate at present, that will emerge in the future. In short, I believe that we should approach the long-term financing of OASDI with due humility and respect for the limitations of our ability to predict a future three-quarters of a century away.

As projections are made further into the future, accuracy and reliability markedly diminish. Most nations with social insurance systems make 25- or 50-year cost projections, but almost never beyond the latter. Only the U.S. and Canada make 75-year actuarial projections. With this in mind, it is important to note that virtually all of the problems associated with long-term OASDI financing occur during the last 25 years of the 75-year valuation period.

This does not mean that the social security actuaries' long-term projections are useless. Rather, the 75-year projections are guideposts which help to reveal general trends in OASDI financing under a given set of demographic and economic assumptions. What these projections reveal is generally dependent upon the eye of the beholder.

To the extent that the long-term estimates are used to set policy 75 years away, I would urge that the more pessimistic of the two intermediate sets of assumptions (alternative II-B) be used as a guidepost. The alternative II-B assumptions are generally regarded as the "best guess" estimate, as they contain conservative assumptions regarding economic growth and demographic changes. For this reason and for reasons having to do with the uncertainty of the future, the National Commission unanimously agreed to use the alternative II-B assumptions when considering the long range costs of OASDI.

The most striking aspect of the long-range financing picture is that under current law the OASDI programs are in close actuarial balance over the next 50 years. Demographic trends very favorable to OASDI financing which allow the buildup of large trust fund surpluses during the 1990's and the first decade of the 21st century account for this little-known fact. Table 2 illustrates the actuarial balance for the cash-benefit programs over the next 50 years, both as a percentage of taxable payroll and as a percent of program expenditures (OASDI is considered in close actuarial balance in the long run if estimated contributions are within 5 percent of estimated outlays).

TABLE 2

Comparison of estimated OASDI average tax rate with estimated average OASDI cost rate by alternative, calendar years 1982-2031

(as percent of taxable payroll)

	1982-2006	2007-2031	50-year average
average tax rate	12.01%	12.40%	12.20%
Alternative I			
average cost rate	9.75	11.30	10.52
surplus or deficit (as % of program expenditures)	+ 2.26	+ 1.10	+ 1.68 (16.0%)
Alternative II-A			
average cost rate	10.46	13.15	11.80
surplus or deficit (as % of program expenditures)	+ 1.55	-.75	+ .40 (3.4%)
Alternative II-B			
average cost rate	11.37	14.08	12.72
surplus or deficit (as % of program expenditures)	+ 1.64	- 1.68	- .52 (-4.1%)
Alternative III			
average cost rate	12.73	17.84	15.28
surplus or deficit (as % of program expenditures)	- .72	-5.44	- 3.08 (-20.2%)

SOURCE: 1982 Report of OASDI Trustees

Even absent any long-term financing measures by Congress, the cash-benefit programs are adequately financed for the next half-century. The reliability of estimates beyond 50 years are questionable at best. At worst, the projections for 50-75 years in the future have served as a rationale to make dramatic changes in the obligations of the nation's social insurance system. Because the system relies on the contributions of participants whose benefit obligations may not be paid for decades, I have opposed dramatic changes in social security's benefit obligations based on assumptions about what may or may not occur 50 to 75 years from now.

Nevertheless, I will support this committee's efforts to bring the OASDI programs within close actuarial balance along the lines of the National Commission agreement. As the provisions of the Commission agreement indicate, it is possible to close the 75-year financing gap without reductions in benefit protection.

When the long-range estimates are considered in perspective, it is not difficult to see how this is true. With no changes in current law, the average annual cost of OASDI is 14.09 percent of payroll over the next 75 years. During that time, the present law average annual contribution rate is 12.27 percent of payroll, leaving a deficit of 1.82 percent of payroll.

Virtually all of the deficit accumulates during the final third of the 75-year valuation period, when the estimates are the least certain. Moreover, the shortfall amounts to 12.9 percent of program expenditures. In fact, the closer one examines the long-term financing of social security, the more that claims of "impending calamity" and "intergenerational warfare" ring hollow.

Traditionally, the long-term cost of OASDI has been measured in terms of taxable payroll, which the Social Security Trustees believe will substantially shrink over the next 75 years. The Trustees' projections assume that cash wages (which are subject to the payroll tax) will decline from 84 percent of total compensation at present to 62 percent. However, if the cost of OASDI is measured in terms of the relative burden on current and future workers, it becomes clear that the cost of social security cash benefits will, on average, remain virtually the same as it is today.

For example, if it is assumed that the taxable wage base does not erode substantially (that workers continue to receive 84 percent of their compensation in the form of wages), then fully one-third of the entire long-term deficit (0.6 percent of taxable payroll) is eliminated. Under this assumption, revenues would increase enough to cover the benefit obligations projected under current law (about 14.0 percent of payroll). However, higher earnings credits would boost benefit obligations to about 15.2 percent of payroll, leaving a gap of 1.2 percent of payroll or about 7.8% of program expenditures — just outside the range of close actuarial balance.

On the other hand, if Congress were to adjust the payroll contribution rate for the erosion in the payroll tax base anticipated by the trustees, virtually the entire long-term deficit of the system (1.61 percent out of every 1.82 percent of payroll) is eliminated. Although this particular method of maintaining the system's revenue base at its current level would have negative income redistribution effects, I have included it as an illustration of how closely the current OASDI benefit structure conforms with our ability to finance it.

As a percentage of Gross National Product, the OASDI programs are remarkably stable over the long run. Under the alternative II-B assumptions, cost as a percentage of GNP dips from its current level of 5.16 percent to 4.97 percent in 1990, 4.53 percent in

2000 to a low of 4.35% in 2004. With the projected relative decrease in workers-to-beneficiaries, system costs begin to rise to 4.92% of GNP in 2015, 5.9% in 2025, and peak at 6.1% in 2030. Thereafter, the cost of OASDI drops steadily, reaching 5.44% of GNP in the year 2060.

The relative stability of OASDI costs as a proportion of GNP is shown by Table 3. Over the entire valuation period, the expenditures of the cash-benefit programs are projected to be 5.28 percent of GNP — roughly what they are today. Even under the pessimistic assumptions, the long-term cost of OASDI is 6.7 percent of GNP.

TABLE 3
Estimated cost of the OASDI system
as percent of GNP by alternative,
calendar years 1982-2056

Alternative	I	II-A	II-B	III
1982	5.07	5.08	5.16	5.19
2056	4.37	5.49	5.54	8.61
25-year averages:				
1982-2006	4.25	4.40	4.75	5.25
2007-2031	4.67	5.11	5.30	6.50
2032-2056	4.70	5.67	5.78	8.34
75-year average				
1982-2056	4.54	5.06	5.28	6.70

I would submit that much of the rhetoric surrounding this issue stems from a basic misunderstanding of how social security operates and is financed. It is impossible to read a newspaper or listen to the news without some reference to the "intolerable burden" of social security: how it will give young workers a "poor return" on their contributions, how it will claim an ever-increasing share of our resources, and how it could be replaced by a "sounder" system of private investment mechanisms. For this reason, I recently issued a report, "Social Security: Myth, Misconception and Reality," which I have included at the end of my testimony. I believe that it will help to show that the reports of social security's impending collapse are greatly exaggerated.

Mr. Chairman, this discussion of the system's long-range financing is intended to illustrate one simple fact: it is simply untrue that the benefit protection offered by social security constitutes an unwieldy burden for tomorrow's workers. While it is true that the workers of the future will not benefit from the artificially low contribution rates employed at the program's inception, it is also true that their relative payroll contribution burden will remain virtually what it is today. More importantly, the benefit protection promised to future workers can and should remain at the levels enjoyed by today's retired and disabled workers.

Report of the National Commission

On January 15, 1983, 12 of the 15 members of the National Commission on Social Security Reform agreed to issue, on a bipartisan basis, a series of recommendations to Congress which would:

— completely finance the OASDI programs over the short term;

— finance more than 2/3 of the system's long-term deficit; and

— bring the system into range of what the actuaries consider close actuarial balance (projected revenues would fall into the range of projected costs plus or minus 5%).

This agreement was the product of the dedication and perseverance of Commission members from both political parties. In particular, the almost inexhaustible patience of Commission Chairman Alan Greenspan and the invaluable expertise of Executive Director Robert Myers enabled 15 members with extremely divergent and seemingly irreconcilable views to come to an historic political agreement. Largely through the tireless efforts of these men and other Commission members, including the Hon. Robert Dole, Chairman of this distinguished Committee, and former Commissioner of Social Security Robert Ball, the Commission came to an agreement on some very fundamental principles as well as to a package of refinancing proposals.

<u>Principles Endorsed by the Commission</u>

During its lifespan, the Commission considered various alternatives to the present structure of social security. Such alternatives included a voluntary system, a system structured like a retirement annuity, and an advance-funded system. The Commission also considered proposals to substantially scale back benefit protection as provided under the present benefit formula. These proposals were rejected.

Instead, the Commission agreement is an endorsement of the fundamental principles on which the social security program was founded. These fundamental principles include:

— benefits as replacement of lost earnings

— receipt of benefits as a matter of right based on past contribution

— primary financing through payroll contributions

— avoidance of a means test as condition of benefit receipt

— for the common good, a balance between social adequacy and individual equity.

These principles are embodied in the Report of the House Committee on Ways and Means accompanying H.R. 6635, the Social Security Act Amendments of 1939* which explained the importance of the contributory basis of social insurance:

* House Report No. 76-728, p.6

"It is essential then that the contributory basis of our old-age insurance system be strengthened and not weakened. Contributory insurance is the best-known method of preventing dependency in old age by enabling wage earners to provide during their working years for their support after their retirement. By relating benefits to contributions or earnings, contributory old-age insurance preserves individual thrift and incentive; by granting benefits as a matter of right it preserves individual dignity. Contributory insurance therefore strengthens democratic principles and avoids paternalistic methods of providing old-age security. Moreover, a contributory basis facilitates the financing of a social-insurance scheme and is a safeguard against excessive liberalization of benefits as well as a protection against reduction of benefits."

The progressivity of the benefit formula and other social adequacy aspects of social security were incorporated into the original act by design. According to the 1935 Report of the Senate Committee on Finance accompanying H.R. 7260, the Social Security Act,* the social adequacy aspects of the program were to benefit the common good by lowering the costs of needs-based assistance:

"During the depression period the country has become keenly conscious of the problem of providing security for aged people who are without adequate means of support. Dependency in old age is a hazard which faces everybody."

"In view of the growing number of the aged, the great cost which title I (Old Age Assistance) is almost sure to entail in the future years, if no other provisions are made for old-age security, and the desirability of providing old-age security as a right and not as public charity, this bill proposes also inauguration of a system of Federal old-age benefits, computed on a reserve basis. Under this system it will be possible to pay annuities which will provide something more than merely reasonable subsistence. The benefits to be paid are related to the wages earned, but there are adjustments favoring the lower paid employees."

In reaffirming these fundamental principles, the Commission rejected proposals to alter the basic structure of social security for the same reasons that these alternatives were rejected at the program's inception.

A voluntary system was rejected as the antithesis of social insurance under which members of society pool their contributions against a variety of risks — death, disability, and retirement. Very simply, a voluntary program would not work. Adverse selection would drive the cost of a social insurance system to prohibitive levels, particularly for those who would most need its protection. As a consequence, many workers who need protections could not participate or would choose not to do so. Before the enactment of social security, millions of workers could not or did not make adequate provisions for retirement.

The Commission also rejected transforming OASDI into a simple retirement annuity, with benefits based exclusively on contributions. While benefits are related to contributions under the OASDI benefit formula, a progressive replacement rate in favor

* Senate Report No. 74-628, pages 4 and 7

of lower wage workers exists. A pure retirement annuity system would result in insufficient or minimal protection for low-wage workers, workers who become disabled early in their careers, and survivors of workers who died at young ages.

Transforming OASDI into an advance-funded system was rejected in favor of the current pay-as-you-go approach. Dramatic tax increases would be required to build a fully-funded system. Moreover, the size of the fully accumulated trust fund would be approximately $6 trillion, roughly twice the nation's current Gross National Product. As Robert Myers indicated, such a fund would not only retire the accumulated Federal debt, but what was left would exceed the value of all the shares traded on the New York Stock Exchange and the American Stock Exchange combined. Under current law, the value of promised social security benefits is guaranteed by the authority of the Federal Government to continue to levy the payroll tax, and ultimately, its intention to honor those commitments.

This consideration was a factor in the Commission's decision to reject a reduction in the value of basic benefit protection. Under current law, the real value of social security benefits (known as the "replacement rate") will remain constant, absent action by the Congress. In 1977 Congress froze the OASDI replacement rate, which ensures that benefits in the future will replace a constant percentage of preretirement or predisability wages. In fact, the ultimate replacement rates which take effect in 1982 are actually lower than those in place during the previous nine years because of the "decoupling" of the benefit formula in 1977. However, they are roughly the same as those set by the 1939 Act.

The Commission agreement turned away from proposals to reduce the basic benefit level by lowering replacement rates by 5 percent, 10 percent or more. These proposals would have been implemented by altering the indexation of the formula "bend points" so as to reduce future real benefit levels. In addition to reducing benefit protection to levels which would have dramatically increased aged poverty, I believe that the "bend point" proposals constituted a surreptitious benefit cut.

Instead, the Commission agreed that the value of maintaining the social security program far exceeds the magnitude of its current financing problems. We concurred that the value of benefit protection to young workers — directly in the form of protection against the financial hazards of disability or death, and less directly in the form of a systematic way for them to help meet their responsibilities to support their parents and grandparents — is worth preserving and maintaining.

Proposals Endorsed by the Commission

The Commission agreement represents a compromise for each of the 12 Members who were part of the agreement. Not a single member of the Commission would endorse every component of the package as an individual proposal. But as a package, as a bipartisan agreement, I believe it deserves the full consideration of this Committee and of the entire Congress, and I intend to work toward its passage.

The package represents a uniquely cooperative effort of members of diverse political factions. It entailed the cooperation of the President, the Speaker of the House, and the President of the Senate. Additionally, in the House, the agreement is supported by the majority and minority leaders, by the Ranking Republican of the Committee on Ways and Means and the Chairman of the Committee on Rules. In the Senate, it is supported by the majority and minority leaders, by the Chairman of the Committee on Finance, the Ranking Democrat on that Committee's Subcommittee on Social Security, and the Chairman of the Special Committee on Aging. The mainstream labor and business groups, represented by the president of the AFL-CIO, the chairman of the board and chief executive officer of the Prudential Insurance Company, and the president of the National Association of Manufacturers, all support the Commission agreement.

The changes made in the Commission agreement are designed to make the social security system safe, solvent, sound and secure, for now and for future generations. The Commission agreement will provide the means to more than finance social security's obligations over the next few years, for the next half-century, and will bring the system into close actuarial balance over the long term.

Today's agreement turns away from the easy path of relying on hopeful assumptions to produce a solution. Such a solution might have fallen short of the amount needed to shore up the system if the recession continues. Instead, we have prepared for the worst in developing our recommendations. By doing so we can guarantee the viability of the social security system under virtually all contingencies. So while it will be considered strong medicine, today's agreement will go a long way toward restoring the trust of America's workers and retirees.

The Commission chose to avoid the mistakes of the 1977 Amendments, which relied on overly optimistic assumptions. Instead, the Commission used the 1982 Trustees' pessimistic assumptions, modified for recent economic trends, for projecting the short-term deficit. Under this "revised pessimistic" alternative III estimate, $173 billion in additional revenues would be required during 1983-89 in order to attain a trust fund ratio of 15 percent at the beginning of 1988. About $152 billion would be required to maintain an uninterrupted flow of benefits during 1983-89 under the same pessimistic assumptions.

Even if the economy performs according to the revised pessimistic estimate, the Commission package will contain sufficient funding to weather the storm. Approximately $168 billion during 1983-89 is provided by the consensus package. It is important to note that the cost estimates for the package were developed using the Administration's FY 1984 budget assumptions. If economic performance is more in line with the revised alternative III estimate, the Commission package will raise $185 billion.

Finally, the package represents a fair and equitable sharing of sacrifice. Beneficiaries are asked to defer their cost-of-living adjustment (COLA) for six months. Those with the highest incomes will incur slightly higher income tax obligations; those at the low end will be protected from the COLA delay. Workers are asked to pay a 0.36 percent FICA tax increase during 1988 and 1989, and the self-employed are asked to pay more in payroll taxes only partially offset by an income tax cut. Even the general revenues will pitch in. In effect, everyone in America will give a little in order to get a lot.

Let me be more specific. Current beneficiaries of the system will continue to receive all of the benefits they are entitled to receive under current law, save for a one-time, six-month delay. As the Chairman of the Select Committee on Aging during the last 3 Congresses, I can share with this Committee exactly how much this means to the elderly people of this country. To these people, many of whom are primarily or entirely dependent on these benefits, social security is their lifeblood. The proposals made by some study groups, business leaders, Administration officials, Members of Congress and even the President to reduce these benefits created a climate of sheer terror for millions of elderly, widowed and disabled people. For many, the proposed reductions would have meant a difference in the quantity and quality of food, clothing, and medicine. The knowledge that these benefits will continue in their full amount will be a comfort to the elderly and disabled of America.

The Commission agreement is also a tremendous victory for the workers of America. Even as some elected officials were hiding behind promises to preserve benefits for current recipients, they were advocating massive reductions in benefits for today's workers. In order to achieve a short-term political gain by "protecting" today's elderly, they would bargain away the rights of tomorrow's.

These are the same politicians who were claiming that social security was a "bad deal" for young contributors. It is to take leave of common sense to suggest that reducing future benefit protection would somehow make social security a better deal. Mr. Chairman, nothing could undermine confidence in the social security system more than to renege on the commitments of the U.S. Government, simply because they will not be due for years to come. The decision of the Commission to preserve future benefit levels will avoid a major intergenerational conflict.

Elements of the Commission Package

The Commission package includes six major short-run changes — a revised tax-rate schedule, general revenue reimbursements for military wage credits, extension of coverage, an increase in the self-employed tax rate, inclusion of 1/2 of OASDI in adjusted gross income for income tax purposes, and a shifting of the COLA to a calendar-year basis. The last four changes provide the bulk (1.36 percent of payroll) of the long-term savings. The cost impact of the Commission proposals resulting in savings or costs to OASDI are detailed in the table that follows.

TABLE 4

Short- and long-range cost impact of Commission proposals
Savings to OASDI

	Short-term 1983-1989 (billions of $)	Long-term 75 years (% of payroll)
Revenue Changes		
Extended coverage*	$23	.30%
Revised tax rate schedule	40	.02
Inclusion of OASDI in AGI	30	.60
Revise self-employed tax rate	18	.19
General revenue reimbursement	18	--
Net Revenue Changes	$129	1.11
Benefit Changes		
Shift COLA to calendar year basis	40	.27
Equity changes: windfall benefits	0.2	.01
Equity changes: spousal benefits	-0.5	-.07
Increased delayed retirement credit	--	-.10
Net Benefit Changes	$39.3	.11
Total Savings	$168.3	1.22%
(additional long-range changes		.58%)

Notes:
* assumes revised tax-rate schedule

** assumes no change in retirement patterns. Substantial change would reduce projected cost or even result in net savings.

In addition to the items with major cost impact, there are equity changes in the areas of spousal and short-term worker benefits, delayed retirement incentives, and stabilization changes. The Commission agreement also covers 68 percent of the long-range deficit, leaving the remainder for Congress. For the purposes of discussion, these proposals are grouped in terms of their impact on OASDI revenues and OASDI benefits.

In the short run, just under 23.4 percent of the cost savings are attributable to changes in benefits. In the long range, however, the benefit reductions are somewhat offset by some benefit increases in the areas of spousal benefits and delayed retirement incentives. As a result, about 9 percent of the long-range savings are from benefit changes.

Revenue Changes

Advance scheduled 1990 tax rate/make contributions partially income-tax creditable - Prior to enactment of the 1977 Amendments, the financing status of OASDI was extremely critical both in the short run and the long run. Trust fund reserves were projected to maintain uninterrupted payment of benefits only through 1980, and the 75-year actuarial deficit was four times greater than the deficit now projected. A defect in the 1972 benefit formula which overcompensated persons becoming entitled to benefits after 1972 and insufficient real wage growth throughout the decade were the primary causes of the system's precarious state in 1977.

The 1977 Amendments addressed these problems primarily by correcting ("decoupling") the indexation in the 1972 benefit formula and by enacting a payroll tax increase apparently sufficient to guarantee the system's financing for the next half-century — an ultimate rate of 7.65 percent by the year 1990. The 1977 Amendments raised the tax in a series of steps — to 6.13 percent in 1979, 6.65 percent in 1981, 6.7 percent in 1982, 7.05 percent in 1985, and 7.15 percent in 1986 — before reaching 7.65 percent in 1990. The intention was for each step of the scheduled increases to keep the system adequately financed — albeit barely — as system costs rose as a percent of payroll until 1990 when demographic conditions more favorable to the system's financing would result in large trust fund surpluses. The stepped-rate schedule of increases failed, however, to provide an adequate margin of safety to insulate the system against further economic downturns.

Earlier implementation of the 7.65 percent rate would have sufficiently financed the cash benefit programs through the next half-century. In view of the poor performance of the economy in recent years and the resultant precarious financial status, there appeared to be little justification for delaying the implementation of the scheduled 7.65 percent tax rate until 1990. As a compromise, the Commission agreement moves the 1985 OASDI contribution rate for employers and employees to 1984; retains the current law rate of 5.7 percent for 1985-87; reschedule the 1988-89 rate to 6.06 percent; and make not change in the tax rate for 1990 and thereafter. The following table compares the proposed tax rate schedule with current law (increases in bold):

TABLE 5
OASDI tax rates — current law and proposed,
employers and employees, each
calendar years, 1983-1990

	Current law	Proposed change
1983	5.4%	5.4%
1984	5.4	**5.7***
1985	5.7	5.7
1986	5.7	5.7
1987	5.7	5.7
1988	5.7	**6.06**
1989	5.7	**6.06**
1990	6.2	6.2

* to be offset with refundable income tax credit

Commission members appointed by the Democratic leadership had insisted on a refundable tax credit in order to neutralize any change in the individual workers' tax burden. Other members were strongly opposed to such a credit. As a compromise, we agreed to recommend that a refundable income tax credit offset the 1984 payroll tax increase, but not the tax increase scheduled for 1988 and 1989. I strongly urge this committee to retain the income tax credit at least for the tax increases scheduled for

1988 and 1989, and to consider a permanent income tax credit for any rate increase beyond the current 5.4 contribution rate. Such a credit would have no impact on the unified budget. If OASDI is removed from the unified budget, the tax expenditure could be offset by a partial repeal of the indexation of the income tax scheduled to take effect in 1985.

This recommendation will be a major step towards correcting an anomaly in the tax code under which (with minor exceptions) employee contributions to retirement and disability systems, including OASDI, have been made from aftertax income. This has applied to contributions for both private pension plans and social security. The result of this anomaly is that a young couple trying to raise a family, buy a house, and meet other expenses from the lower salaries usually available to younger workers is also transferring a substantial amount of income to retired people and is paying income tax on the amount transferred.

Recent legislation to enact and to expand vehicles for private retirement savings have acknowledged this anomaly by creating "individual retirement accounts" (IRA's) into which workers can build a source of retirement income through pre-tax contributions. The tax treatment of IRA contributions reflected the concern that young workers need not be strapped with the twin burdens of deferring needed income for decades while being taxed on that income. I believe that this concern should prevail in the context of workers' contributions to social security. Changing the tax treatment of OASDI contributions would properly align it with the tax treatment of IRA contributions and significantly contribute toward better coordination of the nation's retirement income policies.

Extension of coverage to Federal and nonprofit employees for all new hires - Social security coverage is compulsory to all gainfully employed individuals in America except civilian employees of the Federal government, employees of State and local governments, and employees of non-profit organizations which have elected to "opt out" from providing coverage. Employees of the Federal government were originally excluded from social security because they were already covered by the Federal Civil Service Retirement system.* State and local government employees were exempted from compulsory coverage because of the uncertainties caused by the possible applicability of the constitutional prohibition against taxation of the States by the Federal government. Employees of nonprofit organizations were exempted because their employers were exempted from Federal income taxes.

With these exceptions, 95 out of every 100 Americans today are insured against the loss of earnings on which they are dependent through social security coverage. The failure to completely extend coverage throughout the workforce has created problems associated with gaps in survivor and disability coverage and inequities associated with the manipulation of various benefit formulae in order to gain favorable treatment in relation to the social security-covered workforce. The Commission believes, in principle, that every gainfully employed American should be covered by social security. Specifically, the Commission is recommending extension of coverage, effective 1984, to

* references made to the federal Civil Service Retirement system include other plans covering federal employees such as the Foreign Service and Central Intelligence Agency plans.

all new employees of the Federal Government, and to all employees of non-profit organizations.*

Nonparticipation in social security is advantageous to a small, albeit visible, segment of the recovered population. By and large, these are highly-paid, long-service participants in the Federal Civil Service Retirement system (or other nonintegrated Federal plan) who spend a relatively short time performing social security-covered work. For them, the noncoordination of social security and pensions based on noncovered work results in the receipt of what is commonly known as "windfall" social security benefits. In addition to receiving retirement annuity benefits substantially larger than the average OASI benefits (as is the case with Federal CSR and many nonintegrated Federal government plans), these dual beneficiaries receive OASI benefits which reflect the heavy weighting of the benefit formula intended for low-wage earners.

This advantage comes at the expense of millions of noncovered employees who are deprived of all or much of the valuable social insurance protection provided under the social security system. Even the Federal Civil Service Retirement system — considered the best of plans for noncovered workers — cannot match the package of family, survivor and disability benefits offered by social security.

Social security provides family benefits to replace the lost earnings of retired and disabled workers. Family benefits are paid to aged spouses, unmarried dependent children, and spouses caring for eligible children, based on the retired or disabled worker's earnings record. social security provides survivor benefits for spouses, children and dependent parents — whether the worker is active or retired. Social security disability protection is, in general, unmatched by other government plans, especially with respect to low- or average-earnings workers.

Nonparticipants in social security also lack most or all of these important protections:

- portability of earnings credits;
- wage-indexation of earnings credits;
- tax-exempt status of benefits;
- complete inflation protection of initial benefits;
- nonforfeitability of spouse protection; and
- weighting of the benefit formula to protect workers with low, average or noncontinuous earnings histories.

The Commission recommends extension of coverage to all new hires in the Federal workforce as of 1984. This recommendation recognizes that nonparticipation in social security undermines confidence in the system from the standpoint of the contributing worker. It has long been a source of resentment and confusion to covered workers who

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* a non-profit organization operated by a religious sect which is conscientiously, or because of religious principles, opposed to acceptance of public insurance should be exempt from extended coverage.

observe that the people who are entrusted with making program policy, managing the program, and carrying out its operations on a day-to-day basis are themselves exempted from coverage. The Commission recommends that the social security program should, bv and large, cover **every** American worker including the President, Vice-President, Members of Congress and Federal Judges*.

In short, the Commission believes that permitting continued nonparticipation in social security by this significant portion of the population is poor public policy from an equity, adequacy, and perceptual point of view. Universal coverage would end the real and perceived inequities associated with "double dipping," restore confidence in the social security system, and ensure that no American be denied valuable protection from the loss of their earnings because of retirement, disability or death.

I would emphasize that I am opposed to the termination of the Federal Civil Service Retirement system or any other nonintegrated public employee system. I believe that the benefits offered under these plans are part of the total wage package needed to induce workers into government employment and are a reward for years of dedicated public service. These plans should exist as a tier to supplement the basic social insurance protection provided by social security, as private plans do, and should continue to offer benefits which, when considered in combination with social security, offer the same aggregate level of protection offered currently by the Federal Civil Service retirement system.

Extending coverage in the manner the Commission has proposed, exempting only Federal Government employees hired before 1984 would expand the OASDI revenue base significantly while preserving the rights of current noncovered employees and the long-term interests of future employees. Universal coverage also results in significant long-run savings, which are the net of expanded payroll tax receipts minus increased bneefit obligations. The greater magnitude of the former is a function of the fact that current benefit obligations to these groups are substantially greater than current payroll tax receipts (because of the different benefit formulae). This proposal will result in increased revenue to the combined OASDI trust funds of $23 billion by 1991, and an excess of tax receipts over benefits equalling 0.30 percent of payroll over the 75-year valuation period.

Additional coverage issues - Employees of State and local governments may be covered under social security at the option of the State and in agreement with the Secretary of Health and Human Services. Coverage may be terminated if the State gives 2 years' written notice of such intent. Notice can only be given after a State or local group has been covered for at least 5 years. Once coverage is terminated, the group can never again be covered under social security.

During 1959-1981, 881 State and local government entities, school systems and hospitals have "opted out" of social security. Of that total, 606 terminated coverage after 1975. Fueled by concern over the system's financing and proposed reductions in benefit protection, the relatively small number of withdrawals has substantially increased. In 1981 alone, more than 100 entities, representing 172,000 employees, terminated coverage. These 1981 withdrawals alone will cost the OASDI trust funds $200 - $250 million annually entities are pending for the next 2 years. If all 9,000,000

* for Constitutional reasons, the Commission did not recommend mandated coverage of State and local government entities

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employees of State, county and city governments, school systems, hospitals and other employees of non-profit organizations terminated coverage, the cost to the trust funds would be $18 billion annually.

The Commission proposes to no longer permit State and local governments which have elected social security coverage for their employees to terminate such coverage. In addition, pending termination notices would be invalid.

The Commission recommendations also close a loophole which permits employers to reduce their FICA taxes under "salary reduction" plans. Section 401(k) of the internal revenue code allows employers to set up a plan in which employees can opt to have a portion of their pay set aside in a tax-sheltered fund. In addition to the income tax exemption, the deferred salary is also exempt from the payroll tax. As a result, participants in such plans receive smaller earnings credits and revenue is lost to the trust funds. The Commission recommends that, for both the payroll tax and earnings credit purposes, any salary deferred under a Section 401(k) plan be considered as cash wages.

Equalize Self-Employed Tax/Make Contributions Partially Income-Tax Deductable - All covered workers make contributions at a combined employer-employee rate on 13.4% of their taxable payroll. Self-employed workers, who pay only 75% of the combined OASDI contribution rate and 100% of the HI contribution, comprise the sole exception to this rule. At the time self-employed persons were brought into the system, this exception represented a compromise based on two considerations. The rate reflected a political compromise between those who believed the contributions of the self-employed should not exceed that of any other employee and those arguing that since the self-employed receive the same protection as all other workers they should be equivalent of the employee-employer contribution. Secondly, the tax code allows deductions of business expenses (including payroll contributions on behalf of employees) in figuring a corporation's income tax. Since self-employed persons in unincorporated businesses were unable to take advantage of this business deduction, a rate less than 100% of the combined employer-employee tax was considered equitable. This has the unfortunate effect, however, of systematically reducing revenues to the social security program.

In the past, proposals to equalize contribution rates between employees and the self-employed would have dramatically increased the out-of-pocket burden on self-employed workers because no compensating treatment in the tax treatment of the payroll tax contribution was advanced. The Commission believes that the time has come to prevent the further loss of income to the program by equalizing the contribution rates without causing undue hardship to the self-employed. The Commission recommends that, beginning in 1984, one-half of the self-employed workers' contribution become income-tax deductable and that the contribution rate for self-employed workers be equalized with the combined employer-employee contribution rate. The combined impact of these two recommendations will ensure that self-employed individuals are not faced with a substantial increase in their tax liability. This will result in additional revenues to the combined OASDI trust funds of $18 billion by 1989/1991 and 0.19% of payroll over the next 75-year valuation period.

Partial inclusion of OASDI benefits in AGI for income tax purposes - Social security benefits have been excluded from gross income for purposes of income tax under a series of rulings in 1938 and 1941 by the Internal Revenue Service. The tax-free treatment of OASDI has received widespread public support, largely because the contributions of employees and the self-employed were already taxed at the time they were made.

In 1979, the quadrennial Advisory Council on social security recommended that one-half of OASDI benefits be subject to the income tax, on the grounds that the employer contribution was not taxed when made. Largely because of the misperception that this change would result in higher tax liabilities for low-income beneficiaries, the proposal was soundly rejected. Indeed, as Chairman of the Select Committee on Aging, I recall how the terrified response of low-income elderly and disabled social security recipients constituted the strongest opposition to the proposal. Ironically enough, these were precisely the people who would have remained unaffected.

In recognition of this widespread perception, the Commission recommended that one-half of OASDI benefits be included in adjusted gross income only if other adjusted gross income exceeded the following thresholds: $25,000 for a joint return and $20,000 for a single taxpayer or a married taxpayer filing a separate return. As currently constituted, this provision would affect only 11 percent of the aged population — those with the highest incomes.

Even for this highest-income segment of the elderly population, the additional tax burden will not be unduly onerous. For a single, aged taxpayer with AGI of $30,000 and a $500 a month benefit, the additional income tax would be 1.9 percent of total income. For a married elderly couple with AGI of $40,000 and a $1,093 benefit, the additional tax liability would be 2.7 percent of total income.

Two major problems with the Commission recommendations as currently constituted remain, however. The first pertains to a "notch" which exists between persons with incomes just above or just below the thresholds. Theoretically, the difference between two individuals with identical OASDI benefits and adjusted gross incomes of $19,999 and $20,000, respectively, is an additional $500 or more in tax liability for the latter.

We are all too familiar with the consequences of the "notch" created by the 1977 Social Security Amendments. I know that this Committee will act to ensure that individuals in similar circumstances are not treated substantially differently. A possible method for "smoothing out" the notch would include one-half of OASDI benefits in AGI, and subject those benefits to the income tax to the extent that they exceed the threshold.

An additional problem lies with the implementation of the proposal; that is, the manner in which the taxes are to be collected. Although Congress might be tempted to withhold a portion of benefits in order to satisfy the new tax liability, this would be perceived as a benefit reduction.

In order to ensure that the purpose of the proposal remains clear, I would urge this Committee to adopt the approach in S.1, the Social Security Amendments of 1983. Under S.1, the Secretary of HHS would be required to file information returns, similar to the W-2 form, detailing the payment of OASDI benefits during the taxable year. The individual would then include a copy of the form with his or her tax return.

Under this approach, the OASDI trust funds are prospectively reimbursed by the Secretary of the Treasury. The Secretary would transfer (on at least a quarterly basis under S.1) to the OASDI trust funds an amount estimated to equal the increased taxes raised under the proposal.

Accelerating general fund debt repayment for past military wage credits - Since 1946, the Congress has enacted no less than nine specific legislative provisions which provide that persons serving in the military service of the U.S. shall receive special social security wage credits in excess of the actual amount of the persons's military salary. However, no payroll taxes are levied on these special wage credits even though they are considered the same as other wages when benefits are computed and, therefore, raise the benefit costs of the program. Two types of credit were provided:

— Pre-1957 Wage Credits - World War II veterans were given noncontributory wage credits of $160 for each month of active military service. These credits were provided to protect veterans from losing social security coverage during their military service. This type of credit applies to military service from 1940 to 1957. Since 1977, the General Fund of the Treasury has paid the OASDI funds $446 million a year as reimbursement for the estimated benefit costs of granting special non-contributory gratuitous wage credits for military service prior to 1957. Under current practice, the trust funds will continue to receive these level payments of $446 million a year until the General Fund obligation of $17 billion owed to the OASDI trust funds is fully repaid in the year 2015.

— Post-1956 Wage Credits - Noncontributory wage credits of $300 per quarter for military service performed after 1956 to recognize the value of non-cash compensation such as food, shelter and medical services. In 1981 the General Fund paid the OASDI trust funds $74 million for the estimated 1981 costs of benefits based on non-contributory gratuitous credits for military service after 1956. If the general fund reimbursement had been based on the amount of payroll tax revenues which would have been paid, based on the amount of gratuitous earnings, it would have been about $130 million short of the revenues the trust funds could have received had the gratuitous wage credits been subject to the same FICA tax as real wage credits.

The Commission recommendation would credit the OASDI trust funds with the present value of the estimated additional benefits arising from the pre-1957 gratuitous military wage credits. For gratuitous wage credits from 1957 through 1982, the trust funds would be credited with a lump sum equal to the combined employer-employee taxes which would have been levied and the interest which would have accumulated, less the reimbursements already received. In the case of wage credits for noncash compensation in 1983 and beyond, the value of the employer-employee contribution on such credits will be credited annually to the appropriate trust fund.

Reimbursement for value of unnegotiated checks - The U.S. Treasury, manager of the OASDI trust funds, debits the trust funds for the amount of each month's benefit payments at the time they are paid rather than after they are cashed. This leads to the premature debiting of billions of dollars each month which reduces interest income and limits the flexibility of the trust funds to respond to the current cash flow problems. As a result, the OASDI trust funds have lost approximately three-quarters of a billion dollars, representing the value of debited benefit checks which have never been cashed and the value of interest lost.

Currently, the day that benefit checks are dated, usually the third of each month, is the day that the major drawing down of the trust funds is set into motion. On that day, securities equal in value to that portion of benefits paid by direct deposit — approximately one third of total benefit payments or about $4.7 billion — are redeemed by the Treasury. The remaining sum needed to pay the month's benefits is produced when additional securities held by the trust funds are liquidated two days later (usually the fifth of the month). This practice results in the trust funds being debited for 100% of all benefit payments within 2 days of the first date of redemption, even though less than half would have been presented for payment by that time. In fact, the SSA does not even consider a check to be late until three days after the delivery date, and no action is taken to follow up or replace lost checks until the sixth of the month.

The Commission recommends that the value of uncashed OASDI checks issued in the past be credited to the trust funds in a lump-sum payment. For uncashed checks in the future S.1 would require the Secretary of the Treasury to "take such actions as may be necessary" to ensure that the trust funds are credited on an ongoing basis. I would recommend that the Treasury Department's flow of funds procedure be changed to insure that the OASDI funds are debited after the checks are cashed rather than issued. This requires that the amount of benefits paid by electronic transfer be debited after recipient institutions make their demand for payment from the Federal Reserve.

Instituting these recommendations will not only assure that the Trust Funds are treated fairly, but will also result in a smoother level of disbursement throughout the month. Obviously, in order to facilitate this process, the Treasury could project the rate and level of disbursements and reconcile these estimates on an annual basis. A similar technique is already used for crediting FICA revenues.

Shift cost-of-living adjustment to calendar year basis/Increase SSI disregard - One of the most important elements of the social security system is the mechanism which maintains the purchasing power from the point of entitlement throughout a beneficiary's lifetime. The COLA ensures that the amount of goods and services that can be purchased by the monthly benefit will not be reduced because of inflation.

The COLA has been a popular target for budget cutters recently. Because of the COLA, they claim, the income of beneficiaries grows faster than those of workers. I have even heard some critics say that the COLA increases benefits faster than inflation. Would that these claims were true, the income status of America's poorest age group — the elderly — would be much better than it is today.

The plain truth is that the COLA simply preserves the value of the initial benefit. Wage growth has outstripped price growth for 28 out of the last 36 years, and it will continue to do so under all sets of assumptions.* So all of this talk about trimming the COLA in order to "slow the growth of benefits" is nonsensical doubletalk. When you cut the COLA, you are cutting benefits.

Many on the Commission wanted to do just that. Proposals were made to pay three-quarters or one-half of the CPI. Other proposals would have paid the CPI minus 2 or 3 or 4 percentage points. Finally, there was a great deal of discussion to peg the COLA to "wages minus X," whatever that is.

Others on the Commission, myself included, refused to go along with these proposals to alter the basis on which the COLA is paid. The Commission recommendation represents the resultant compromise.

The agreement proposes shifting the COLA to a calendar year schedule. Beginning in 1983, the COLA would be calculated on the December benefit (payable in January), rather than the June benefit, payable in July. In addition, the measuring period would also be shifted, in 1984, so that the adjustment would continue to come 3 months after

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* For a more complete discussion of these issues, see "Cost of Living Adjustments Under the Old Age, Survivors and Disability Insurance Program," U.S. House Select Committee on Aging, April 23, 1982.

the end of the CPI measuring period.

What this provision really means to the vast majority of aged and disabled beneficiaries is an additional six-month wait before their next regularly scheduled benefit adjustment. Instead of receiving the COLA in July, 1983, their checks will not be adjusted until January of 1984. In effect, they have lost the COLA for 6 months. Although the rate is adjusted thereafter, the lost purchasing power will never be recouped.

Mr. Chairman, no one can claim that the current beneficiaries of social security will not adequately share in the sacrifice needed to obtain this agreement. The COLA delay will cost the average retired beneficiary, now receiving about $400 a month, about $120 in 1983. During every year that beneficiary remains on the rolls, he will lag $120 (in real terms) behind the inflation-adjusted value of his current law benefit.

Fortunately, the very lowest-income beneficiaries will be shielded from the impact of the COLA delay. As part of this proposal, the monthly disregard of social security benefits under the supplemental security income program will be increased from $20 to $50. SSI pays general revenue-funded benefits to the neediest aged, blind and disabled. Therefore, the OASDI beneficiaries who fall into those categories — generally the very poorest — will receive an increase in SSI slightly larger than the lost cost-of-living adjustment.

I regret the appearance in this package of even this one-time six-month delay in the cost-of-living adjustment. It is my hope that the elderly and disabled will consider it as a heavy but necessary toll for achieving a politically workable and financially viable social security system.

Equity changes - spousal benefits - Strictly speaking, the OASDI program is gender-neuter; persons become entitled to benefits as a retired worker, disabled worker, a spouse, a disabled or divorced spouse, a surviving spouse, a child, a surviving or disabled child, or a parent regardless of sex. Substantial changes in women's roles in society have resulted in various adequacy and equity concerns for women beneficiaries, however. Although the Commission did not broadly address itself to these concerns, the Commission's recommendations include some low-cost, well-targeted benefit changes to address some of the groups most in need. Among them:

— Remarried divorced or disabled widow(er)s - benefits would no longer be terminated upon remarriage if the marriage occurs after the age of first eligibility for benefits. Disabled widow(er)s' benefits and disabled surviving divorced spouses' would be payable to those who remarry after age 50; surviving divorced spouses' benefits would be payable to those who remarry after age 60.

— Deferred survivors - benefits would no longer be based on outdated wage records. Under the proposal the earnings credits of the deceased worker would be indexed to reflect economy-wide wage increases instead of price increases.

— Divorced spouses - benefits would be payable at age 62 to divorced spouses (who have been divorced for at least two years) of eligible former spouses, irrespective of whether the worker has claimed benefits.

— Disabled widows and widowers - benefits would be increased to 71.5 percent of PIA at age 50, the age of first eligibility. Currently, benefits are payable on a graded scale, increasing from 50 to 71.5 percent of PIA at ages 50 to 60.

These proposals are modest in the context of the entire agreement, but they will make life a little less harsh for some groups of women in the most dire economic circumstances. These changes are long overdue, and I am pleased to support them.

Equity changes: windfall benefits (Elimination of short-term worker advantage for non-covered workers - The social security benefit formula is based on the dual concepts of individual equity and social adequacy. Individual equity is achieved by linking benefit levels to the amount of taxable earnings — i.e., higher levels of earnings result in a greater amount of benefits. Social adequacy is attained through a progressive benefit formula — i.e., higher levels of earnings result in proportionally smaller increases in benefits. Therefore, while the $275 monthly benefit currently paid to a 62-year-old lifetime minimum wage earner represents 47.2 percent of final earnings, the considerably larger $509 benefit paid to a 62-year-old maximum worker represents only 20.6 percent of the previous year's maximum earnings.

The current benefit formula is designed to replace an individually equitable and socially adequate proportion of the lifetime earned income of workers who spend their entire paid work careers in social security-covered employment. This formula, however, cannot distinguish between workers who have covered and non-covered work histories. Therefore, similar benefits will be paid to a person who earns $10,000 for 35 years and another person who earns $35,000 for 10 years, regardless of whether the short-term, higher paid worker is also eligible for benefits based on work in non-OASDI-covered employment. In these circumstances, individuals who did not spend their full paid work career in OASDI-covered employment receive an unintended windfall due to the graduated nature of social security's progressive benefit formula. For example, a 62-year-old OASDI-covered worker with a full working career* of 26 years of average earnings credited to his/her social security record since 1951 currently receives a benefit of $402. A 62-year-old short-term worker with 13 years of average earnings posted to his/her record since 1951 (half a full career total) receives a benefit of $240 or 59.7% of the full-career worker's benefit. Eight and three quarters years of average earnings (one-third of a full career) yields a benefit of $196 or 48.8 percent of an average full-career benefit.

In order to rectify the specific anomaly whereby workers who split their working careers between OASDI-covered and non-covered work receive an unintended advantage, the Commission recommended 2 possible revisions for persons who become eligible for pensions from non-covered employment in 1984.

Unfortunately, the method adopted in S.1 is the harsher alternative, identical to the proposal submitted by the Administration in May, 1981. This proposal simply and arbitrarily eliminates the 90 percent replacement rate applicable to the lower band of average indexed monthly earnings. Instead, the second percentage factor of 32 percent would apply. As detailed in a report issued by the Select Committee on Aging,** this

* Full working career is defined as the number of years in the benefit computation formula. For someone reaching 62 in 1982, a full working career is 26 years. This will increase by one each year, until reaching 35 in 1991.

** Impact of the Administration's Social Security Financing Proposals on Current and Future Beneficiaries, Select Committee on Aging, U.S. House of Representatives, Ninety-Seventh Congress, First Session, July 1981.

proposal would result in substantial and arbitrary benefit reductions, having little to do with the extent to which a worker relied on non-covered earnings to finance retirement income.

The alternative method presented in the Commission report is far preferable. Under this approach, earnings from both covered and non-covered work would be applied to the present benefit formula in order to determine the replacement rate. That replacement rate would then be applied to a worker's covered earnings. This approach was recommended by the Hon. J. J. Pickle, Chairman of the Subcommittee on Social Security, in his social security financing legislation in the 97th Congress.

Increased delayed retirement credit - As an alternative to those who would mandate an increase in the age of entitlement, the Commission recommended a long-overdue incentive for workers to postpone retirement. Under current law, a worker receives a bonus equal to an annual rate of 3 percent for each year between ages 65 and 70 that retirement is postponed. This 3 percent bonus, the delayed retirement credit, was considered too insignificant to influence any retirement decision.

Under the Commission agreement, the very slight incentive offered by the present-day delayed retirement credit would be substantially increased. During the years 1990 and 2010, the bonus would be gradually increased from 3 to 8 percent. When fully phased in, a worker would receive 140 percent of his primary insurance amount at age 70, as compared to 115 percent under current law.

Although this proposal is estimated to cost .10 percent of payroll in the long run, it is assumed that this proposal will not substantially alter the retirement patterns of older workers. If the incentive does induce a significant number of workers to delay their retirement, however, the cost of the proposal would be much smaller. Moreover, if the incentive is very successful, substantial net savings to the system could result.

Attempts have been made to force older workers to remain in the workforce longer. Ironically enough, due to both the current recession and decades of age discrimination, unemployment among older workers has never been higher. All that is accomplished with the approach of coercion is a harsh reduction in the benefit protection of millions of older persons who, for reasons of health, can no longer remain in the workforce. I wholeheartedly support the voluntary alternative contained in this recommendation.

Stabilizing Changes

Perhaps the greatest challenge to maintaining continued confidence in the system will come from the impact of economic trends on short-run program financing. Over the long run, benefit and contribution levels relative to each other have a high degree of predictability because they are both tied to the growth of wages. Given a particular set of demographic assumptions, the relationship of income to outgo over the long run lends itself to a high degree of predictability.* In the short run, however, the extreme sensitivity of the system to the economy places a considerable limit on the predictability of actuarial soundness during periods of poor economic performance. Most of the

* the demographic assumptions themselves (particularly with respect to trends expected to occur during the last third of the 75-year projection period) are subject to a wide range of variation.

system's sensitivity can be traced to the indexation of cash benefits to price increases upon entitlement.

Ironically, indexation of cash benefits was an effort to stabilize the financing of the OASDI system. Assuming demographic stability and a constant tax rate, the variable affecting contributions to the system would be linked to factors affecting system outlays. With a worker-beneficiary ratio stabilized at 3:1 as the system matured, growing wages would boost contributions at the same rate that they increased earnings records, resulting in concurrently higher outlays. The sole exception to this symmetrical relationship was price indexing of benefits upon entitlement.

At the time of its enactment as part of the 1972 amendments, providing a cost-of-living adjustment indexed to prices was adopted as a cost-reduction alternative to wage-indexing. Wage increases had outstripped the CPI in virtually every year prior to the 1972 amendments, and no set of assumptions projected negative wage growth. By all estimates, indexing the cost-of-living adjustment to increases in wages would have resulted in higher benefit outlays over the long term.

Beginning in 1974, however, the U.S. economy began a period of protracted negative wage growth. Between 1974 and 1979 the CPI outstripped wage increases by an average of 0.3 percent; in 1980 prices exceeded wages by an unprecedented 4.9 percent. As a result, system disbursements exceeded income for the first time in the history of the program during 1975 through the present.*

This phenomenon highlights the dramatic impact of indexing post-entitlement benefits to the CPI while other factors affecting system income and outlays are wage indexed: the OASDI trust funds become extremely sensitive to the economy in the short run. All other things being equal, periods of real wage growth (a "normal" economy) result in net annual surpluses in the relationship between income and outgo. This is because contributions (tied to wages) rise at a faster rate than benefit payments (tied to wages and prices). Conversely, during periods of economic contraction, relatively higher prices will boost outlays at a rate faster than payroll tax revenues.

This sensitivity to the economy is accountable for much of the uncertainty which characterizes short term financing considerations. For example, under the midrange (intermediate II-B) assumptions, $61 billion would be sufficent to maintain the timely payment of benefits between 1982 and 1991. However, under the pessimistic set of assumptions, more than $152 billion would be required. According to the optimistic set of assumptions, no additional funds would be required because the OASDI trust funds would remain in surplus (and would continue in surplus status during the entire 75-year valuation period).

This substantial range of short-term possibilities was the most intractable facing the Commission. By the best estimates, the cash-flow problems facing the OASDI in the short run will amount to only 2 or 3 percent of program expenditures. If the mid-range economic assumptions prove correct, relatively minor or incremental charges would be

* This is also attributable to an error in the indexed benefit formula enacted in 1972 which compounded wage and price increases. The 1977 "decoupling" amendments corrected the flaw, but not until after 5 years of new beneficiaries received unintended benefit increases and not until an additional group of persons becoming entitled between 1977 and 1981 received a transition guarantee.

sufficient to maintain an adequate cash flow. However, the possibility of a sustained recession, or that the economy would perform according to the pessimistic assumptions, would increase the magnitude of the shortfall. Given the system's sensitivity to the economy, accepting these prospects as inevitable would lead the Commission to the conclusion that only a dramatic, permanent reduction in social insurance protection could provide the "margin of error" needed to "restore confidence" to the system.

Rather, the Commission believed that a mechanism for insulating the OASDI programs from the temporary shocks of the economy is far preferable to locking in the kind of major benefit reductions which anticipate severe economic downturns that may never occur. In effect, the course the Commission is recommending will enable the program to weather periods of poor economic performance with adjustments which affect worker and beneficiary alike, without penalizing either worker or beneficiary if pessimistic economic assumptions do no materialize.

The Commission agreed to a package of three stabilizing proposals, but could not come to an agreement on perhaps the most important element: a "fail safe" proposal.

The three proposals for stabilizing the system include:

Wage-based COLA trigger with repayment mechanism- beginning in 1988, whenever the OASDI trust fund reserves fall below 20 percent of the next year's outlays, the COLA would be based on the lower of wage growth, or the increase in CPI. When the fund ratio returns to 32 percent or more at the beginning of a year, benefits based on full CPI increases would be reinstated and amounts foregone in previous years would be repaid.

Reallocation of OASDI tax rates - under the Commission proposal, part of the DI tax would be reallocated to the OASI trust fund in order to achieve roughly the same trust fund ratios for each. Similar reallocations took place as a result of 1980 legislation and the 1977 Amendments.

Temporary OASDI-HI interfund borrowing - through 1987, authorize interfund borrowing between the OASI and DI trust funds and from the HI trust fund.

I would have preferred stabilization proposal which relied entirely on new revenues. The combined effect of the Commission package would build the trust fund reserves to the 30 percent level - far above the trigger level for a wage-based COLA. In fact, even under the pessimistic assumptions, OASDI benefits are adequately financed in the short term.

Without a fail-safe measure and certain other refinements, however, the stabilizing package does not go far enough. Even the pessimistic estimate assumes a "straight-line" performance of economic indicators from 1983 through 1989. Our cyclical economy, however, is characterized by peaks and valleys. Although the Commission agreement would adequately finance the near-term shortfall in aggregate, it is possible to run into a cash-flow problem (particularly in 1984-86, when revenues raised are the least). Such a cash-flow problem, no matter how minor in the long run, would severely damage the credibility of the system, the Commission and most importantly the government.

I am therefore strongly urging this Committee to adopt the following proposals, which I will describe below.

Permit permanent interfund borrowing - The Old Age and Survivors' Insurance trust fund assets are maintained separate and distinct from those of the Disability Insurance trust funds. This practice stems from the enactment of the DI program in 1956, when concerns arose that unexpectedly high costs for the new program might adversely affect the OASI program. Although these concerns never materialized, Congress maintained separation of the funds in order to discourage the perception that the OASI trust funds were being "diverted" to pay for DI benefits.

For the purposes of financing, however, Congress is primarily concerned with the tax rate for the cash-benefit programs in aggregate rather than the specific allocation of the total tax rate between the two funds. This arrangement served well during previous years, when the tax rates exceeded, with a significant margin for error, the amount required to finance the obligations of each program respectively.

With the maturation of the program into a fully pay-as-you-go system, the combined tax rate is ideally sufficient to finance the benefit obligations of both programs and allow for a small excess to build the trust funds as a contingency reserve. Because the factors affecting income and outgo are not identical for both programs, it is possible for one trust fund to be drawn down precariously low even while the other builds up substantial reserves — all during a time when the combined tax rate is sufficient to finance the OASDI programs. When this occurs, the present arrangement requires an act of Congress to reallocate the tax rates — action which is inevitably accompanied by heavy media attention and needless public concern.

The most recent case in point concerned the 1977 trustees' report projections of imminent exhaustion of the DI trust fund. Ironically, the actual performance of the DI program was so much better than the dire projections assumed it would be that a substantial portion of the DI payroll tax was diverted to the less stable OASI fund. Yet this reallocation, the result of a law passed by Congress in 1980, was the cause of widespread public concern.

During periods when the combined payroll tax is sufficient to finance both the OASI and DI programs but one of the funds is low, the necessity for Congressional action to readjust the payroll tax incites scare headlines and causes needless fear among the general public. Moreover, the reallocation of payroll taxes is as mechanically imprecise as it is politically cumbersome. I believe that a mechanism which would allow fine-tuning of revenue allocations between the trust funds is necessary to avoid subjecting the public to political demagoguery and scare tactics when the reserves of one trust fund are ample and those of the other are low.

Starting in 1983, the OASI and DI trust funds should be permanently authorized to borrow from the other whenever needed to assure timely payment of benefits, with the loans made repayable with appropriate interest.

I would acknowledge the necessity of maintaining a separate accounting of the revenues and benefit obligations of OASI and DI. Information from such cost analyses and estimates is needed to enable policymakers and the public to track possible adverse trends in either program. While such separate accouting allows sound program planning and management, I believe that the adverse effects on public confidence outweigh the negligible benefits of requiring legislative action to reallocate taxes between the cash benefit trust funds. Because the factors affecting the expenditures of the Hospital Insurance program — medical costs and utilization — are fundamentally different and substantially more volatile than those affecting the outlays of the cash benefit programs, I do not believe that the HI trust fund should be included in the permanent interfund borrowing arrangement after 1987.

Countercyclical general revenues - The combination of financing mechanisms reocmmended by the National Commission is sufficient to address social security's cash flow problem even if the pessimistic economic projections materialize. One such mechanism which will help to insulate the system against economic shocks by relating the cost-of-living adjustment to wage growth has been outlined above.

There remains the possibility, albeit remote, that the economy will perform even worse than the pessimistic set of assumptions. There is an additional possibility that economic fluctuations will result in temporary periods of performance less favorable than the assumptions. In recognition of this possibility, I believe that:

(1) it is desirable to have an additional stabilizing mechanism in place to deal with this contingency should it arise, in order to maintain public confidence in the capacity of the system to weather economic downturns; and

(2) it is not desirable for the program's beneficiaries to act as the sole "shock absorbers" or "stabilizers" by having to absorb the brunt of economic downturns through reductions in benefit protection.

If, despite adoption of other short-term measures, the impact of a prolonged recession leaves the OASDI trust funds in a precarious position, I recommend that the trust funds be compensated for losses of revenue during periods of high unemployment. Specifically, whenever the combined OASDI trust funds fall to below 20 percent of annual outlays, a general revenue infusion equal to 0.1 percent of anticipated annual outlays should be made for each 0.1 percentage point of national unemployment in excess of 6 percent.

Backup general revenue borrowing authority/Issuance of social security bonds - In an extremely volatile economy, countercyclical general revenue infusions may be insufficient to guarantee timely benefit payments in a given year even though significantly different conditions during a period closely following might be conducive to trust fund buildup. Moreover, economic periods characterized by negative real wage growth and moderate unemployment would exert a negative impact on the program's financing which could not be addressed with countercyclical general revenues. In order to guarantee uninterrupted benefit payments even during sharp economic downturns, I recommend that the trust funds be authorized to borrow from the Treasury in the event that trust fund reserves fall below 5 percent of annual outlays. Repayments on such borrowing should begin when the trust fund levels reach 50 percent of annual outlays.

I am aware of the opposition to this proposal on the grounds that it might become a permanent, open-ended general revenue infusion. Such is not the intent of this proposal, which is offered only in the context of a Commission agreement which will finance the near-term shortfall even under the pessimistic assumptions. The intention was to come to agreement on a package substantial enough to make it unlikely that such authority would ever be used. For the sake of public confidence, however, I believe that this "fail-safe" mechanism is an essential part of the social security refinancing legislation to be reported by this Committee.

An alternative form of this proposal would be to allow the trust funds to issue social security bonds directly to the public. It would be appropriate to make such bonds due during a period of large anticipated surpluses in the trust fund reserves, such as the 1990's and the first decade of the 21st century.

Funding Over the Long Range

Impact of the Commission Agreement

As detailed earlier in my statement, the Commission agreement solves two-thirds of the long-term problem. Under current law, the deficit is about 12.9 percent of program expenditures (that is, only 87.1 percent of benefit obligations over the long run are adequately funded). The proposals included in the Commission agreement reduce the deficit to 4.1 percent of program expenditures (payroll taxes would cover almost 96 percent of projected benefits over the 75-year period. According to the social security Actuaries, this is within close actuarial balance. Moreover, benefit obligations would be more than adequately funded over the next 50 years.

Nevertheless, I feel that there should be adequate financing in current law to cover the benefits promised to today's young workers. Before addressing this point, however, I believe it is necessary to outline how not to resolve the remaining one-third of the long-range problem.

Proposed Benefit Reductions

As proposals to refinance the remainder of the projected deficits are debated, it will be difficult to ignore the temptation to cut future benefits. Some may consider reducing the benefits of young workers far off in the future, the politically expedient thing to do. Others may even tout it as an "act of courage." I fail to see how reducing the incomes of the elderly and disabled constitutes "courage," simply because they are affected in the distant future.

Two major benefit reductions may be considered. The first would reduce the benefit replacement rate which determines the real level of present and future social security benefits. Under this proposal, the benefit formula "bend points" would be shifted so as to reduce the average worker's replacement rate from 42 to 37 percent. This amounts to a 10 percent reduction in the benefit obligations of OASDI. More specically, it would constitute a 10 percent average across-the-board cut in benefits.

This technical-sounding proposal reduces benefits in an insidious manner. Over time, the benefit protection of future cohorts of young workers is ratchetted down in a surreptitious manner. The result of this "bend point" reduction would be to guarantee a lower relative standard of living for future beneficiaries.

The other proposal would increase the age of entitlement for full benefits. In addition, either the age of entitlement for actuarily-reduced benefits would be raised in tandem, or the actuarial reduction would increase. This proposal is also a benefit cut.

The arguments against his proposal are compelling, overwhelming, and have been stated at length before this Committee. In sum, however, raising the "normal retirement age":

- Ignores the needs of a substantial number, possibly a majority, of older workers to leave the labor force before age 65
- Uses compulsion when market forces are preferable to encourage later retirement

- Attempts to force older people to work longer but does not eliminate impediments to employment or assure jobs

- Proceeds on the assumption that because longevity is improving, health improves in tandem with longevity

- Constitutes a benefit cut

Particularly as an 82-year-old (or young) worker, I know that this proposal should have a certain amount of attractiveness. In fact, I know many people, now working past the traditional "age of retirement" who favor this proposal. But I suspect that most of the advocates of raising the age are engaged in self-satisfying occupational pursuits which are less than physically demanding. Many workers who joined the labor force at a young age, foregoing a college education, have worked for 45 years or more by the time they reach age 62. Often, these workers are engaged in physically debilitating labor, and do not have the capacity to stay in the work force any longer. I would submit that none of these workers sit on the policy boards of groups and institutions which advocate raising the retirement age to achieve laudable-sounding policy goals.

In short, Mr. Chairman, reducing benefits for today's young workers is unwise, unfair and unnecessary. Neither of these proposals belong in this Committee's refinancing legislation. <u>I would adamantly oppose a replacement-rate reduction or an increase in the entitlement age. There are far superior ways to finance the system's benefit obligations.</u>

<u>Proposed financing changes</u>

Administrative expenses of social security - During 1982, the OASDI trust funds will pay the general Treasury of the United States approximately $1.98 billion for the administrative costs of the OASDI program. The largest portion of this payment represents salaries, rent for property and equipment, building operating expenses, and charges for supplies purchased. In addition, the capital costs of constructing buildings and purchasing such major items as computers and vehicles are charged to the trust funds. The OASDI Trust Funds also pay the Treasury Department for collecting contributions, issuing benefit checks, and managing fund assets; the Department of Health and Human Services for expenses related to the overall administration and planning for the system; and the states for the costs of making disability determinations.

Using the assets of the trust funds to pay for administrative costs contributes to the common perception that large portions of FICA revenues are being siphoned off for non-OASDI benefit purposes. For instance, in a 1981 Roper survey, respondents indicated that they believe that 52 percent of social security's funds are spent on administration of the program. Actually, the $1.98 billion spent in 1982 represents only 1.3 percent of the total income of the OASDI trust funds.

Even though administrative expenses represent a small proportion of total income and expenditures on an annual basis, the trust funds have transferred over $21.9 billion to the general Treasury (not including interest) for administrative costs since 1940. In addition, the long-term costs of administrative expenses will approximate .15 percent of payroll or more than 25 percent of the remaining projected long-term OASDI deficit.

As a means of strengthening the public's perception that their social security contributions are being used for the purposes they intended - i.e., benefit purposes - I would urge that 1) <u>the administrative expenses of the OASDI program be paid from</u>

general appropriations; and 2) the trust funds be reimbursed for previous administrative expenditures. The second proposal could be enacted on a contingency basis, that is if the near-term performance of the economy is worse than anticipated.

This proposal will bring reimbursement practices with respect to the social security trust funds in line with those in effect for other Federally-administered trust funds. Currently the administrative expenses of the Highways, Airports, Federal Civil Service Retirement and Veterans' Insurance trust funds are paid from general appropriations without reimbursement from the respective trust funds. In addition, the general fund already reimburses the OASDI trust funds for the estimated expenses incurred in administering non-OASDI-related workloads. These workloads include the administration of the SSI program with its more than 4 million recipients and the processing of over 204 million annual reports of wages for the Treasury Department. During 1982, the OASDI funds will be reimbursed by approximately $920 million for these and other non-OASDI administrative workloads. Although SSA employs worksampling surveys to determine the proper reimbursement amount, it is difficult to judge whether the trust funds are being adequately compensated for these non-OASDI administrative functions. Full funding of SSA's administrative budget would assure that no trust fund monies are used to pay non-OASDI administrative costs.

The mechanics of funding OASDI's administrative expenses should not change by this proposal. Currently SSA must go before the Labor-HHS Appropriations Subcommittees of Congress to be granted annual appropriations for administrative costs even though the monies are actually derived from the trust funds. In fact, under this proposal there may be greater flexibility inproviding funds for administrative improvements, such as spending $500 million for necesary upgrading of the computer systems. The annual limitation on administration expenses and the growing reluctance to use the social security trust funds for non-benefit purposes might make necessary administrative improvements more difficult to accomplish if they are financed from the assets of the trust funds.

Contingent increase in the contribution rate - as a percent of GNP, and relative to a worker's total income, the payroll tax contributions needed to support current benefit obligations will diminish in the future. Under current law, a slightly higher payroll contribution rate would be needed if the wage base is substantially eroded, as forecasted by the social security actuaries. This projection is based on the assumptions that non-taxable fringe benefits will greatly expand, and that Congress will allow the growth of these payroll-tax loopholes.

Even if these assumptions are correct, the deficit could be entirely closed by a contingent increase in the employer/employee contribution rate beginning in the year 2010. If the above recommendation were adopted, an increase of 0.36 percent would entirely close the long-range funding gap. As a result, the OASDI payroll tax rate would be 6.56 percent as opposed to 6.2 percent under current law (for a total OASDHI tax of 7.99 percent v. 7.65 percent under current law). If the recommendation with respect to the administrative expenses of OASDI is not adopted, the increase would be 0.46 percent.

I would reemphasize that such a contingency rate increase would not increase the burden of supporting OASDI because:

— real wage levels are projected to be substantially higher by the year 2010 than at present; and

— although levied at a slightly higher rate, the payroll tax would be levied on a much smaller portion of total compensation than today.

— if the projected expansion of non-taxable fringe benefits does not occur, the contribution rate increase would be unnecessary.

Particularly because of the last reason, I strongly believe that the contribution rate increase should be made on a contingency basis. Under the Commission agreement, the program is well financed over the next 50 years and is in close actuarial balance over the next 75 years. The remaining problems some believe may occur are anticipated during the final years of the valuation period — precisely the years during which the estimates are the least reliable. We in Congress have a responsibility to approach this issue with one eye on maintaining confidence in the future of the social security system, and the other toward retaining a reasonable perspective on our ability to forecase a future three-quarters of a century away.

I have included two other alternatives to benefit reductions in order to illustrate the manageability of the remaining long-range funding gap:

Prevent erosion of taxable earnings base - the payroll tax is not levied on a worker's total compensation; rather, only a worker's cash wages (up to a wage-indexed annual limit) are subject to the FICA tax. "Fringe" benefits such as employee pension plans, prepaid health care, day care, parking and other in-kind compensation are exempt from the payroll tax as well as the Federal income tax. These tax incentives have spurred a substantial growth in non-payroll taxable fringe benefits: whereas 95% of total compensation was subject to the payroll tax in 1951, today about 84% is so taxable.

The intermediate II-B assumptions contained in the 1982 Trustees' Report project a straight-line continuation of this trend so that by the year 2056 only 62% of a worker's compensation would be in the form of cash wages and thus subject to the payroll tax. Under these assumptions, about one-third of the projected long-term deficit can be attributed to the erosion of the payroll tax base assumed to result from the growth of non-taxable fringe benefits. It appears unlikely that Congress would allow such a dramatic erosion in the tax base. This proposal would assure that such an erosion would not occur.

Under the proposal, the employers' share of the payroll tax would be applied to the total package of compensation offered to each employee (up to the taxable wage limit). At the same time, a compensating reduction in the payroll tax would be made to a level which would generate the same aggregate revenues as under current law. The change would take effect in 1990, but would use 1982 as a base in order to avoid manipulation of the taxable-to-nontaxable compensation ratio in the intervening years.

Among the advantages of this proposal is that it:

— reduces the long-term actuarial deficit by 0.8 percent of payroll

— retains the same real tax burden relative to total compensation

-- stabilizes the cost estimates by eliminating an important source of unpredictable variables in the assumptions

— is neutral as an influence on the growth of fringe benefits (does not artificially increase or decrease the incentive to offer fringes)

— prevents erosion of tax base if substantial fringe growth occurs, thereby preventing future tax increases or benefit reductions needed to compensate such erosion

— eliminates a "paper" deficit if substantial fringe growth would not have occurred.

Restore the wage base to its original level - Social security taxes are currently levied on about 90 percent of all earnings in covered employment. This is because all cash earnings above a wage-indexed annual limit are exempt from the tax (and also do not produce any earnings credits). This contributes to the perception of the social security tax as regressive.

Although the progressivity of the benefit formula reverses the regressive contribution mechanism, additional revenues raised through payroll tax increases do not result in higher earnings credits. As such, they substantially reduce the overall progresivity of the system. For this reason, the five Democratically-appointed Commission members recommended an offsetting income tax credit to be coupled with a payroll tax increase.

However, there are compelling reasons to increase the taxable wage base. Such an increase has the advantage of relying solely on payroll tax revenues. More importantly, no one below the taxable wage base would be affected. Raising the wage base would ensure that higher-income workers paid more of their share to finance the program. In return, these workers would receive higher wage credits, resulting in higher benefits. In addition, they would be contributing to a program which has done more to reduce reliance on means-tested public assistance than any other. The means used to finance such public assistance, the income tax, falls heaviest on the higher income workers.

Under the original Act, between 92 and 92.4 percent of earnings in covered employment were subject to the wage base. Congress allowed this proportion to dip as low as 71.5 percent in 1965, before gradually restoring the percent of wages taxable to 90 percent at present. I would recommend that, at least the original proportion of wages taxable — about 92.2 percent — be restored. This would generate $3.4 billion annually in the short run and .25 percent of payroll over the long run.* In combination with the payment of administrative costs, this proposal would raise .40 percent of payroll and would eliminate more than two-thirds of the deficit remaining after the Commission's recommendations. The remainder, .18 percent of payroll, could be eliminated by a .14 percent increase in the contribution rate.

I would also urge this Committee to consider raising the maximum taxable wage base so that it would include 95 percent of all covered wages. This would completely eliminate the remaining long-term deficit.

Table 6 lists four possible options for dealing with the 0.58 percent of payroll shortfall left unresolved by the Commission agreement. There are considerable variations on each of these options as well as various combinations of each. I respect the expertise and leadership shown by this Committee in the area of raising revenues, and I have confidence that this Committee will be able to finish the job that the National Commission started.

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* because of higher earnings credits, the net savings would be about .20 percent of payroll

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TABLE 6
Options for eliminating the remaining long-term deficit
(long-term savings as a percent of payroll)

Option 1		
—	contingency employer/employee contribution rate increase of .46 percent in 2010	+0.58
Option 2		
—	administrative costs from general revenues	+0.15
—	contingency employer/employee contribution rate increase of .36 percent in 2010	+0.44
Option 3		
—	administrative costs from general revenues	+0.15
—	contingency employer/employee contribution rate increase of .14 percent in 2010	+0.18
—	increase wage base from 90 to 92 percent of covered earnings	+0.25
Option 4		
—	beginning in 1990, apply payroll tax to all compensation, with offsetting tax rate reduction	+0.80

Mr. PEPPER. I can sum up basically the way I feel about this matter in this way. What we have done is something that most of us, I believe, who were members of the Commission did not approve of in all respects. Many of us tried strenuously to oppose to permit the adoption of some of the provisions that are in the package. But when we finally came to the decision in the early evening of January 15—the date of the expiration of the life of the Commission—to make the choice of supporting this package, did we think it was a good package. We believed it was a better package than could be put together in the Congress or anywhere else in the length of time we have available to us. In the opinion of 12 of our 15 members of that Commission, of whom I was one, that was the best package we could put together in the foreseeable future. That the assets of that package far exceeded the liabilities of it even to any groups that might be affected in any way by the provisions of the parts of the package.

For example, what we have affirmatively accomplished is to restore the confidence of the young people who have been cynical about the future of social security. Many of them have charged us, their elders, with ripping them off of their hard-won salaries or wages, of making them put their money in a system which would be gone by the time they came eligible to receive its benefits. That if there were a social security system when they reached the age of 62 or 65 there wouldn't be any money to pay the obligations that they had expected to receive, discharged to themselves.

We also send a message to the people who have been frightened who are already receiving social security benefits. Millions of beneficiaries have been gravely concerned as to whether they would continue to receive those benefits as long as they were entitled to or as long as they live, as were others who were yet to come to current benefit status. With our bipartisan support of this package, we told all of those people that the President of the United States and the Congress of the United States—if the Congress, as I hope it will, adopts this package—that the President and the Congress of the United States, that the two major political parties of this country committed themselves to see to it that for 75-years social security would be solvent and sound, that they will receive what the law said they would receive when they pay into the social security system.

I feel strongly that we should be able to add to that assurance that under this package there will not be any reduction in social security benefit protection during that whole 75-year period.

I know there are two separate reports before your honorable committee and before the Congress. I'm a party, as is the distinguished Senator from New York, to the report proposed by the democratically appointed members of the Commission. We proposed that if a serious shortage projected for the old age and survivor's insurance fund in the year 2015 that if there is any prospect of such a shortage, a payroll tax increase of 0.46 percent, which is a very small addition to the tax, would trigger in. I would hope that the Congress at that time would provide for an offsetting income tax credit to those who had to bear the burden of increased payroll tax payments.

So what I am saying is that we have assured the American people. I've been in a good many places around the country. I have been very much encouraged as I have seen the favorable response of the elderly people of this country to this package.

Yes; they didn't like to have to lose 6 months of their COLA, the cost-of-living adjustment. But I pointed out to them that if you were an average recipient of social security benefits receiving $400 a month your maximum loss in that 6-month period would be $120. They were pleased to hear that in order to take care of the people in the lowest income recipient category of social security—people making perhaps $200 a month—we were increasing what they could receive from SSI. If they received both social security and SSI, the SSI benefit would be increased $30 a month over what it is now. So we were giving to the lowest income beneficiaries more than they were losing by the COLA provision of the package. Of course, they were pleased to hear that.

There were others that were not happy at all about subjecting half of social security benefits for the first time to the income tax. But when one pointed out that only the top 11 percent of the recipients of social security were affected by that requirement, that it was intended to recover the tax not paid on the employer contribution, and that the tax imposed was the same as the recipient of unemployment compensation has to bear, and less than the recipient of civil service retirement benefits has to bear, it wasn't such an extraordinary burden that we were imposing. As I said, it would affect only about 11 percent of the recipients of social security, most of them in much higher income brackets than the $20,000 or $25,000 that we make the base in this case.

Millions of beneficiaries are concerned that Congress might lower these base amounts. Only last night in a question and answer show from Boston, I was asked about the prospect that Congress will lower that base of $20,000 or $25,000 for a couple, $20,000 for an individual person. I answered that a lower base was proposed in the deliberations of the Commission. The initial proposal set these holds at $12,000 and $15,000. Many of us opposed that and the Commission agreed on $20,000 and $25,000. I don't believe you are going to find any appreciable disposition in Congress now or in the foreseeable future to lower that below that base of $20,000 or $25,000.

Despite the substantial additional financing added by the Commission agreement, I find many people with shaken confidence in their future social security benefits. They tell me: "You have taken a much wiser course than the Congress took in 1977. You have envisioned the possibility that the economy might be a pessimistic economy; that conditions might be very bad. You have even provided for the contingency of that happening, I understand. That's true. What if there should be unexpectedly a recurrence of conditions that are pessimistic economically? What do you do then?"

I tell them that there is a moral obligation on the part of the President of the United States, whoever he may be, and the Congress of the United States, whatever may be its personnel, to implement for the emergency that might arise, the revenues so that we would continue to keep social security solvent and sound.

I have been in the Congress except for the 12 years between 1951 and 1963 when I was out of the Congress, almost the entire life of social security. I came in 1936; social security was covered in 1935. And I know of no instance in the history of social society where there has been such a strong acclamation by the President of the United States and the Congress of the United States to the people of the United States, present and future recipients of social security, that we are going to see to it that social society is kept solvent and sound for the future. That's an obligation that we have all assumed.

Our Commission's package proposes to put that obligation into the law by backing it up with a fail-safe principle, an automatic mechanism to assure the payment of benefits in the future if anticipated revenues fell off. We didn't specify as to just exactly how it would operate, but we recognized the possibility that there might be a temporary shortage even beyond what we have anticipated. So we established the principle in the package that would apply in such a case so that there would be a mechanism—and I don't think any President or Congress would fail to implement that mechanism—to respond to that temporary emergengy. This "fail-safe" would be a temporary measure because we would know that in the long run the financing of the system is sound, based on the changes proposed by the Commission.

We will recall that Mr. Myers who so ably served us as the Director of the Commission, stated and included in one of his memoranda that—once we got over the temporary shortfall period between 1983 through 1989, and made adequate provisions for that shortfall—that the payroll taxes already in effect under current law are adequate to assure that social security would be solvent and sound for the next 50 years.

Many of us on the Commission thought that 50 years in the future was as far as we could predict with a reasonable degree of accuracy. We could see little reason to predict what might occur to birth rates, mortality rates, inflation, productivity and so forth between 50 and 75 years from now. But the majority opinion prevailed to the effect that there might be serious problems that would arise in the last 25 years, and we didn't want to seem to shirk those problems and not to be aware of that possibility.

Well, we had come to the evening of January 15, 1983. The Commission has been deliberating since February 1982, working diligently with extremely competent staff people, with a remarkably able chairman. We had been working to find a consensus among our group to recommend to the President and the Congress on this matter. Twelve of the fifteen members came to an agreement on a package of proposals sufficient to solve the short-range problem and more than two-thirds of the long-range problem but we hadn't reached any agreement on the remaining one-third of the long-range problem.

At that point, the Chairman, I think, wisely said, "Well, there's a difference of opinion among the members of the Commission about the remaining long-range provisions or in the possible shortfall that might arise. Let each group make its own recommendation."

One of the groups recommended that we should meet any possible contingency by raising the age of eligibility beginning in the year 2000. To many of us, this was an out-and-out benefit reduction. If you delay the payment of my note due January of next year until January 1 of the following year, you diminish my asset. The same principle applies here. If you increase the age at which you are eligible, you defer the payment of an obligation. I thought that was cutting benefits.

As far as I am personally concerned, I made commitments in many, many parts of this country that I cannot and will not support any reduction in benefits. I was so proud that we were able to say to the elderly people upon whom we had exacted some sacrifice in depriving them of 6 months of their COLA and subjecting them to some income tax on their social society benefits, that basically we had given them a safe social security system for 75 years and we have done it without cutting their benefits or benefit protection. The replacement rate, or real benefit level, is exactly the same as it is now and has been in the recent past—42 percent for an average worker. It has not been lowered. In the package, we have not raised the age of eligibility. We have not made other cuts in the permanent structure of the program.

I want to make clear to those who believe that we should add long-term benefit reductions to the Commission package that the agreement brings the revenues of the system to within 4 percent of the anticipated benefit outgo. The changes we propose in the so-called short-term package assures that we will be within 4 percent of what is called close actuarial balance. It is accepted actuarial procedure that when you are projecting a future as far away as 75 years that a 5-percent variation is generally acceptable. So we are within the range of acceptable variation even if Congress adds nothing to the Commission agreement.

But we wanted to comply with the Chairman's desire, which we shared, that the Commission report leave nothing undone. And so finally we agreed to issue separate recommendations to bridge this 4-percent gap.

Now I realize that there are conscientious differences of opinion about raising age limits. And I don't quarrel with anybody's right to have a view contrary to mine. But the other day when I was testifying before the Ways and Means Committee, I looked around in the room, and I said, "Mr. Chairman, we are talking about dealing with people out there around the year 2000, or 2020; I don't see any of those people here. I don't hear their voices before this honorable committee. They don't have a chance to defend themselves or to speak up. If they were, one of them might say:

> Listen, Mr. So and So, member of this committee, don't you recall during the course of the Social Security Commission proceedings that two representatives appeared from the National Institute of the Aging of the U.S. Government? Don't you remember one of them gave us some rather surprising information that while the percentage of elderly people in their older years was increasing, the percentage of healthy people, able to work people, was not increasing?

The same principle applied to the provision that was in the package at one time reducing the amount that one who retired at 62 would receive from 80 percent of what he would get if he retired at 65, as the law now provides, down to 76 percent. That change would have cut benefits by about $16 a month, diminishing the amount of protection provided under current law to an average early retiree now receiving $320 a month. Do you realize that about half of the people who retire at 62 do so on account of ill health?

The other day I made a TV taping with one of the members of the House from North Dakota, Mr. Dorgan. And in the course of his televised remarks to his own people in North Dakota, he said:

> Just a few days a lady came to me and said, Mr. Dorgan, please don't you all cut the benefits that one will receive at 62. I'm 60. I'm expected to be able to work until next year, and then retire at 62. She said that I have got arthritis so bad I can hardly get out of bed in the morning.

And Mr. Dorgan added, "I know this lady seemed to be in pain as she moved around."

Now she represents about half of the people who retire at 62. They are not just necessarily people who want to quit work and be idle. About half of them have physical health limitations on their capacity to work. We don't know what the health stress of older workers is going to be some 50, 60, 70, or 75 years from now. If we are going to raise the age of eligibility, it should be done at a time when it is apparent that workers would be able to remain in the labor force longer. There is plenty of time in the future when this great Congress, representing the people of this great country, is going to be in business. There is no need for us to take precipitous action in the year 1983 in February or March to remedy a problem which may or may not exist 50 or 75 years from now.

Accordingly, we believe that we can adequately meet the demands of the possibility that there will be a shortfall in the funds by the year 2035. Instead of a long-term benefit reduction, we would propose a contribution rate increase of less than one-half of 1 percent of payroll in the year 2010. It would seem to me that it would be so much better and so much fairer that if we are compelled to entirely close the small gap in the 75-year estimate that we adopt the Democratic proposal which is supported by the distinguished Senator from New York and the rest of the Democratically appointed Commission Members.

Mr. Chairman, I do have one final suggestion with respect to the provision which takes away the COLA for a period of 6 months. I would suggest the possibility that we might add into this bill a reimbursement provision without in any way contradicting what is in the package. There is a precedent elsewhere in this package, in the stabilizer provision.

You will recall that according to this provision, if by 1988 the trust fund falls to a point below 20 percent of the amount required for the next year's outlays, the basis of the COLA will be automatically shifted from the CPI to a wage increase until the trust fund is increased up to a satisfactory level. When the funds return to a satisfactory level then the people who lost some of that COLA during that period of transition would be reimbursed.

I have told a good many of the organizations representing the elderly who have been in to see me that I thought they might recommend something analogus to this to your distinguished committee and the Committee on Ways and Means in the House. I believe that the $168 billion provided in this package is going to prove to be more than sufficient. I think we should collect it nonetheless, of course, and build up our reserves. But it may entirely be possible and reasonable and proper for us to reimburse some of these recipients, some of these people who were denied their COLA during the period of 6 months. I would like that possibility to be considered.

So, Mr. Chairman, I would, of course, be glad to discuss any details of it. The gist of what I wish to say is that I think I'm about as sensitive of our obligation to the elderly people as any of our colleagues. I don't want to do anything to hurt the elderly. I've devoted many years of my life to trying conscientiously to help them in any and every way that I could. I think I have been faithful to that obligation. I think I've been wise in their advocacy in advocating this package. Because I think although it requires some concessions as are required generally to get good objectives, good accomplishments, the package that we have offered to the Congress and the President and the country, I believe, is a good package. I think that people will be proud when their Congress recognizes the wisdom that the Commission has exhibited, and adopts this package.

The CHAIRMAN. Thank you very much, Mr. Pepper. You made an outstanding contribution to the whole process. As you know, we are going to move as fast as we can on this side.

I wonder if you might have time so that we might hear Congressman Archer and Congressman Conable before we ask questions. We have a closed session of the Senate at 10:30 this morning, but we would hope to have a chance to ask a few questions before then. I know Senator Moynihan has to participate in that closed session.

Mr. PEPPER. Sure.

The CHAIRMAN. I'm going to call on Bill Archer now and then Barber can kind of wrap it up for the prosecution.

STATEMENT OF HON. WILLIAM ARCHER, A U.S. REPRESENTATIVE FROM THE STATE OF TEXAS

Mr. ARCHER. Mr. Chairman, thank you very much for this opportunity to appear before you. I want to compliment you and Senator Moynihan for the very conscientious work that you did on the Commission. It certainly was a pleasure for me to serve on the Commission with both of you as well as with Congressman Pepper and Congressman Conable.

I had hoped that I would be able to sign the report. I had hoped that the compromise would take shape in such a form that it would, in my opinion, be a true balance between outflow and inflow of funds. In my final evaluation, it did not meet that test. That is a subjective test, obviously.

I, therefore, filed, as you are aware, dissenting views, and I will not attempt to go into all of what I have placed in the record in the committee report in dissenting views. For the sake of time, will refer only to it and hope that the committee will take a look at it.

I think, generally, that what we should focus on in the Congress is some basic philosophy relative to social security. I think we should harken back to what Franklin Roosevelt had in mind when this program originally was presented. That it would be a supplementary program only; that it would not be a sole source of retirement income that would maintain people above the poverty level.

We have, I think, to a great degree recognized that over the years. We added SSI in recognition of it to supplement those people who were truly poor and assure that they had a basic living economically. I think we have got to state in that regard that benefits are 52 percent more in real purchasing power, after deducting inflation, than they were 15 years ago. They actually are three times more than they were 10 years ago across the board before allowing for inflation.

Taxes today are three times more on average than they were 10 years ago on the work force. I think we have got to take into account those basic facts. As we look at the short and the long term, it seems to me that we have a major responsibility to assure the young and the old alike that we have a program that they can find credible and affordable in the longterm. That, again, is a subjective decision as to what is affordable. Perhaps 15 percent of payroll is affordable. Is 30 percent of payroll affordable? These are questions that we have got to ask and we have got to answer.

I think we should also be able to tell the entire Nation that our ultimate decision is equitable within generations and between generations.

I, personally, do not find equity where in the early years of my work life I paid in 1 percent of my payroll on a base salary of $3,000 or $30 a year, and my children are looking potentially to pay in perhaps as much as 30 percent of payroll. That, to me, is not equity between generations when the benefit structure has basically remained the same, and actually is greater in real purchasing power, as I said, than it was 10 years ago or 15 years ago.

We have got to answer those questions. I don't think they are properly answered in the Commission's recommendations. That is, again, another reason why I did not sign the report.

I would like to highlight for the committee as succinctly as I can some additional objections. I'm concerned that the Commission's recommendations, at least as they now stand, do not fulfill the stated purpose of the Commission itself in its preamble because I do not believe that we can, with certainty, say to the people of this country that we have now, with this Commission recommendation, solved both the short- and the long-term financial problems.

I feel, as a friend of mine said to me last night, that what we have done is attach a 1-inch Band-Aid on a 6-inch wound. Acceptance of these recommendations without change, in my opinion, involves too much risk that we will be back here in a few short years trying to solve what we should have solved in 1983 in taking advantage of this moment.

Now things might be beautiful. Things might be wonderful in the next 6 or 9 years. We might have an economy that grows at 6 or 7 percent in real growth, in which case many of our problems certainly are reduced.

My friend, Claude Pepper, may be right that what the Commission is recommending more than meets the goal in the next 6 years, or he may be wrong. If he is wrong, we have to come back again. Then, where are we in the minds of the American people as far as assuring them that this program is a reliable one? I think there is too great a risk that we will be back some time in the next 6 years to cover additional shortfalls.

We, in Congress, must ultimately make the decisions regarding the Commission's recommendations. I believe we owe it to ourselves and the Nation to carefully examine not only the recommendations themselves, but also the assumptions on which those recommendations are based.

It seems to me that the assumptions should be considered on a very conservative side. If they have extra money in the fund as a result of making an error in that direction, wonderful. We have the ability to do one of the pleasant things in Congress, which is either to reduce taxes or increase benefits. That's a nice position to be in.

If we are wrong, then, as I mentioned, we have got great difficulties. History shows us that we have been overly optimistic in our assumptions ever since we went on the dynamic level of earnings concept in 1972. It makes it more difficult for the actuaries. We have been prone to take the intermediate actuary projection between the optimistic and the pessimistic and say that because it is labeled "intermediate" by the actuaries that, therefore, it has got to be realistic. But history has proved that that is wrong. In taking intermediary assumptions, we have caused ourselves to go into the position that we are in today because the last 3 years of actual economic experience have been worse. Not just in the pessimistic assumptions, but the most worse case assumptions that have been determined by outside groups.

Now if actual experience is worse, then even the worst case assumptions, which are below pessimistic, then there has got to be a worse case that is worse than actual experience that is conceivable and possible. We are not looking at a full range in the actuarial projections to be sure that we have truly taken a realistic approach.

I would hope that the committee pays close attention to the testimony of several outside actuaries whose business it is to be accurate without political pressures who have been testifying before you representing the American Society of Pension Actuaries and the Academy of Actuaries because they come up with a very different evaluation.

They believe that we are perhaps 2½ to 3 percent a payroll short in the long term. Now that—with due respect to my friend, Claude Pepper—is more than a 5-percent error rate compared to what the Commission has recommended. Far, far more than a 5-percent error rate.

Our job, as I see it, is to assess the problems and weigh the alternative solutions ourselves, taking into account changes in basic economic assumptions which have been brought to light even since the Commission reached its final recommendations.

I think it is important for us to question the basic approach taken by the Commission in attempting to close the deficit, even if we assume the basic accuracy of the assumptions on which those recommendations were made. The Commission chose to reduce the deficit almost exclusively through increased taxes and other new revenues. Virtually nothing was done to address the structure of the benefit side of the equation in the future.

We ought to, then, provide today's wage earners with realistic expectations that their social security retirement benefits will be there. The Commission report locks in unrealistic expectations which the economy of the next century will unlikely be able to support.

Interestingly enough, the one restraint on growth on the spending side is the delay of the COLA for 6 months. It would be ironic if inflation drops to 3 percent at the end of March for the preceding year on which we based the COLA for July because in that event there will be a 1-year freeze on the COLA under current law. The Commission's recommendations will have done absolutely nothing on the spending side of the equation. I don't say that is going to happen, but it's not an impossibility. The latest projections are roughly 3.2 percent. That strikes me as being an irony.

The independent actuaries of one of the Commission members himself who signed the report testified before our Committee in the Ways and Means that the combined OASDI and HI trust funds would require a 32 percent of payroll tax by the year 2030. Thirty-two percent. Is it realistic to expect the wage earners of that era to bear that level of tax burden in addition to the other taxes which will be required to maintain the rest of the Federal Government? I think not.

A far better approach would have been, in my opinion, a balance between new revenues and gradual reduction in the growth of benefits. That is not cutting benefits, I must say, but a reduction in the growth of the benefit outlays.

I intend to offer alternative proposals in the Ways and Means Committee to achieve that sort of balance. The Commission report shied away from any attempt at compromise in that regard. It also changed the fundamental structure of social security in what I believe is a total contradiction to its own stated intention not to do so; primarily, in the area of its recommendation to tax half of the benefits of those whose other retirement income exceeds specified limits. Because in my opinion this imposed, for the first time, a means test for eligibility for full benefits shattering the fundamental earned-right concept which has lent credibility to the system throughout its history.

It also penalizes those who save for their retirement, in total contradiction to the concept of social security as a floor to supplement other savings. On the one hand, you encourage participation in private pension programs and IRA's, and on the other hand, you penalize those who do so under the Commission's recommendation. I think that is totally inconsistent.

It is also important to note that the cost to the general treasury of the Commission's recommendations is $77 billion. That is the accommodation that is necessary in lost revenues to the general treasury in order to implement the Commission's report.

Any way you look at it, that changes the basic structure of social security. On top of that, almost to add insult to injury, because the Commission's report has been found wanting potentially in 1985, even by those who have supported it and proposed it, and perhaps we will have a shortfall in 1985 of paying the benefits, there has now been concocted a new term. It's called normalized tax transfers.

Now what "normalized tax transfers" means is simply this: There is not enough money in the fund at the beginning of the month to pay the benefits so the Treasury will estimate the amount of money that will come in at a later date, and infuse that presently at the first of the month into the fund, and lend out of general treasury the money to pay the social security benefits albeit a short-term loan. But, nevertheless, a loan from the general treasury to the social security fund.

Let's call it what it is. There are many who have been proposing this over the years, and I don't question their integrity in proposing it. I disagree with it. But they are having their way for the first time. The general treasury funds on a direct basis will be infused in the social security.

The fundamental concept of social security as a self-financing system, in my opinion, has been eroded significantly by the Commission's recommendations.

Another major flaw, in my opinion, is that there is no provision in the Commission's recommendations to pay back the HI fund for the moneys that have been borrowed. And the HI fund is going to be in severe difficulty at the end of this decade, perhaps bordering on bankruptcy itself.

I think that the Congress should do something about that. I intend to offer recommendations to do that in the House.

Also, there is a notable absence of even treating HI at all. Admittedly, at the time it was available to us, we all agreed not to get into it. But in an overall sense when we look at social security, we have got to take into account in the future the impact and cost of HI.

I was interested in the Commission's recommendation that the Defense Department put up $20 billion in a direct transfer to the social security fund in the next year to tie this fund over for 1 year. Particularly, as it is a departure from previous methods of handling this. But I was even more interested to see and dismayed, frankly, to see that this administration in the concoction of its budget for this year has for the first time in history transferred military retirement out of the Defense budget and over into a civil, domestic entitlement program in order to make Defense spending look less and domestic spending look higher.

I cannot for the life of me understand that, except that it seems to me that it is to accommodate a bad proposal, which is to bail out social security, and not have to face up to the added cost of the Defense Department.

There are numerous other flaws in the recommendations, which I have said I have discussed in detail in my dissenting remarks. I do apologize for the length of my comments this morning, but they are points that I felt were important to make. I think that there are ways to solve these problems, ways to deal within the structure of social security.

I think a pattern along the lines that Michael Boskins worked and has brought forth out of Stanford University is the kind of approach that will do it. I do not believe that this Commission's recommendations are going to be the ultimate solution, and I regret that.

I, respectfully, again state my dissenting remarks, and thanks for the time to come and testify before you, Mr. Chairman.

The CHAIRMAN. Thank you very much. Your entire statement will be made a part of the record. Also the statement of Mr. Pepper.

[The prepared statement of Mr. Archer follows:]

PREPARED STATEMENT OF CONGRESSMAN BILL ARCHER
MEMBER OF THE NATIONAL COMMISSION ON SOCIAL SECURITY REFORM
BEFORE THE SENATE FINANCE COMMITTEE
FEBRUARY 16, 1983

MR. CHAIRMAN:

I APPRECIATE THIS OPPORTUNITY TO APPEAR BEFORE YOUR COMMITTEE TODAY.

AS I AM SURE ALL OF YOU KNOW, I WAS ONE OF THREE MEMBERS OF THE NATIONAL COMMISSION ON SOCIAL SECURITY REFORM WHO DID NOT ENDORSE THE COMMISSION'S FINAL REPORT. THE REASONS FOR MY DISSENT ARE NOTED IN SEPARATE VIEWS I FILED WITH THE REPORT. IN THE INTEREST OF PRESERVING THE COMMITTEE'S VALUABLE TIME, I WILL NOT ATTEMPT TO RESTATE HERE WHAT IS ALREADY A MATTER OF RECORD.

INSTEAD, I WOULD LIKE TO TAKE A FEW MINUTES TO AMPLIFY SEVERAL OF THE POINTS WHICH I RAISED IN MY DISSENTING VIEWS.

FIRST, AND MOST IMPORTANTLY, I AM VERY CONCERNED THAT THE COMMISSION'S RECOMMENDATIONS AS THEY NOW STAND DO NOT FULFILL THEIR STATED PURPOSE. IN MY OPINION, ONE WHICH IS SHARED BY A NUMBER OF PEOPLE WHO TESTIFIED BEFORE THE HOUSE WAYS AND MEANS COMMITTEE, THEY DO NOT SOLVE THE SHORT AND LONG TERM FINANCIAL PROBLEMS OF SOCIAL SECURITY. ACCEPTANCE OF THOSE RECOMMENDATIONS WITHOUT CHANGE INVOLVES TOO MUCH RISK THAT WE WILL BE BACK HERE A FEW SHORT YEARS FROM NOW TRYING TO SOLVE PROBLEMS WHICH COULD HAVE BEEN -- AND SHOULD HAVE BEEN -- SOLVED IN 1983

We in Congress who must ultimately make the decisions regarding the Commission's recommendations owe it to ourselves and the nation to carefully examine not only the recommendations themselves, but also the assumptions upon which those recommendations were based.

Our job is to assess the problems and weigh alternative solutions ourselves, taking into account changes in basic economic assumptions which have been brought to light since the Commission recommendations were made.

I think it is also important for us to question the basic approach taken by the Commission in attempting to close the deficit -- even if we assume the basic accuracy of the assumptions on which those recommendations were made.

The Commission chose to reduce the deficit almost exclusively through increased taxes and other new revenues. Virtually nothing was done to address the structure of the benefit side of the equation in the future. Rather than provide today's wage earners with realistic expectations for their Social Security retirement benefits, the Commission report locks in unrealistic expectations which the economy of the next century will unlikely be able to support.

The independent actuaries of one of the Commission members who signed the report have testified that they expect the combined OASDI and HI trust funds to require 32 percent of payroll by the year 2030. Is it realistic to expect the wage earners of that era to bear that level of tax burden in addition to the other taxes which will be required to maintain the rest of the federal government? I don't see how they can.

ARE WE NOT BUILDING INTO SOCIAL SECURITY THE FRAMEWORK FOR TRAGIC INTER-GENERATIONAL CONFLICT IN THE NEXT CENTURY? ARE MY CHILDREN AND YOURS GOING TO BEAR THE IMMENSE BURDEN OF NEW TAXES DURING THEIR WORKING LIVES -- ONLY TO ENTER THEIR RETIREMENT YEARS WONDERING WHETHER THEIR CHILDREN WILL BE ABLE TO SHOULDER AN EVEN GREATER TAX BURDEN?

A FAR BETTER APPROACH WOULD HAVE BEEN, IN MY OPINION, A BALANCE BETWEEN NEW REVENUES AND A GRADUAL REDUCTION IN THE GROWTH OF BENEFITS. I INTEND TO OFFER ALTERNATIVE PROPOSALS IN THE WAYS AND MEANS COMMITTEE TO ACHIEVE THAT SORT OF BALANCE.

THE COMMISSION REPORT SHIED AWAY FROM ANY ATTEMPT AT COMPROMISE IN THAT REGARD. IT ALSO CHANGED THE FUNDAMENTAL STRUCTURE OF SOCIAL SECURITY -- IN TOTAL CONTRADICTION TO ITS OWN STATED INTENTION NOT TO DO SO.

THE RECOMMENDATION TO TAX HALF OF THE BENEFITS OF THOSE WHOSE OTHER RETIREMENT INCOME EXCEEDS SPECIFIED LIMITS IMPOSES A MEANS TEST FOR ELIGIBILITY FOR FULL BENEFITS -- SHATTERING THE FUNDAMENTAL "EARNED RIGHT" CONCEPT WHICH HAS LENT CREDIBILITY TO THE SYSTEM THROUGHOUT ITS HISTORY. IT ALSO PENALIZES THOSE WHO SAVE FOR THEIR RETIREMENT, IN TOTAL CONTRADICTION TO THE CONCEPT OF SOCIAL SECURITY AS A FLOOR OF PROTECTION TO SUPPLEMENT OTHER SAVINGS. ON ONE HAND, WE ENCOURAGE PARTICIPATION IN PRIVATE PENSION PROGRAMS AND I.R.A.S. ON THE OTHER, WE PENALIZE THOSE WHO DO SO. THAT IS TOTALLY INCONSISTENT.

IT IS ALSO IMPORTANT TO NOTE THAT THE COST TO THE GENERAL TREASURY OF THE COMMISSION'S RECOMMENDATIONS IS SOME 77 BILLION DOLLARS.

THE FUNDAMENTAL CONCEPT OF SOCIAL SECURITY AS A SELF-FINANCING SYSTEM HAS BEEN ERODED SIGNIFICANTLY BY THE COMMISSION'S RECOMMENDATIONS.

THERE ARE NUMEROUS OTHER FLAWS IN THE RECOMMENDATIONS WHICH ARE DISCUSSED IN MORE DETAIL IN MY DISSENTING VIEWS ON THE REPORT, AND WHICH WILL UNDOUBTEDLY BE THE SUBJECTS OF TESTIMONY THIS COMMITTEE WILL HEAR. I WILL NOT GO INTO FURTHER DETAIL ON THOSE POINTS AT THIS TIME.

INSTEAD, IN CLOSING, I WOULD LIKE TO POINT OUT SEVERAL AREAS IN WHICH I BELIEVE THE COMMISSION RECOMMENDATIONS CAN BE IMPROVED. I INTEND TO ADDRESS THESE SUBJECTS AS WE BEGIN MARK-UP IN THE HOUSE WAYS AND MEANS COMMITTEE -- AND WOULD COMMEND THEM TO YOUR ATTENTION AS WELL.

SOCIAL SECURITY'S STABILITY, AND CREDIBILITY, INTO THE NEXT CENTURY WILL DEPEND IN LARGE PART ON HOW WELL WE ACHIEVE A GREATER BALANCE BETWEEN NEW REVENUES INFUSED INTO THE SYSTEM AND REDUCTIONS IN THE RATE OF BENEFIT GROWTH. THAT BALANCE IS THE WAY WE CAN PROVIDE EQUITABLE TREATMENT FOR ALL GENERATIONS OF RETIRED AMERICANS.

THERE ARE A VARIETY OF OPTIONS WHICH SOULD BE CONSIDERED IN THAT REGARD. ALTERNATIVES INCLUDE IMPLEMENTING AFTER THE YEAR 2000 A GRADUAL INCREASE IN THE AGE OF RETIREMENT FOR FULL BENEFITS, AN IMMEDIATE CHANGE IN THE METHOD OF INDEXING BENEFITS SO THEY WILL NOT INCREASE MORE RAPIDLY THAN THE TAX BASE WHICH SUPPORTS THEM, AND A NUMBER OF OPTIONS DESIGNED TO RELATE BENEFITS MORE CLOSELY TO THE TAXES AN INDIVIDUAL CONTRIBUTES TO THE SYSTEM.

WE SHOULD ALSO ELIMINATE THE GREAT DISINCENTIVE TO CONTINUED EMPLOYMENT BEYOND THE RETIREMENT AGE WHICH NOW EXISTS IN THE EARNINGS LIMITATION. CERTAINLY DISINCENTIVES FOR RETIREMENT SAVINGS, SUCH AS THE TAXATION OF BENEFITS, SHOULD BE AVOIDED IN ANY LEGISLATIVE SOLUTION WE DEVELOP.

BY ACHIEVING GREATER BALANCE BETWEEN TAXES AND BENEFIT GROWTH REDUCTIONS, WE CAN ALSO ELIMINATE DISINCENTIVES TO UNEMPLOYMENT SUCH AS THE ESCALATION OF TAX RATES AND THE INCREASED TAX ON THE SELF-EMPLOYED. AT A TIME WHEN CONGRESS IS DEBATING LEGISLATION TO INCREASE EMPLOYMENT, I FIND IT INCONSISTENT THAT A SOCIAL SECURITY REFORM PACKAGE SHOULD HAVE THE EFFECT OF INCREASING UNEMPLOYMENT.

MY GREATEST HOPE WHEN THE COMMISSION BEGAN ITS WORK OVER A YEAR AGO, WAS THAT IT WOULD DEVELOP RECOMMENDATIONS TO CONGRESS WHICH WOULD PROVIDE STABILITY FOR SOCIAL SECURITY AS FAR INTO THE FUTURE AS THE ACTUARIES CAN PREDICT. WE ARE NOW HEARING FROM A NUMBER OF SOURCES THAT THE RECOMMENDATIONS CONGRESS HAS BEEN GIVEN DO NOT ACCOMPLISH THAT. THIS MAY INDEED BE 1977 REVISITED.

I THINK WE IN CONGRESS HAVE A HIGHER RESPONSIBILITY -- ONE WHICH MUST TRANSCEND THE POLITICAL EXPEDIENCY OF RUBBER STAMPING AN INADEQUATE, INEQUITABLE PROPOSAL. WE CAN FULFILL THAT RESPONSIBILITY, NOT BY CASTING ASIDE THE COMMISSION RECOMMENDATIONS, BUT RATHER BY IMPROVING UPON THEM. THE COMMISSION RECOMMENDATIONS ARE AN IMPORTANT STEP IN THE LEGISLATIVE PROCESS -- BUT THEY ARE JUST THAT, A STEP. AS THE PROCESS CONTINUES, THERE REMAINS ROOM FOR BIPARTISAN COMPROMISE.

IT IS IN THAT SPIRIT THAT I THINK WE SHOULD APPROACH THE DECISIONS BEFORE US IN THE COMING WEEKS.

THANK YOU VERY MUCH. I WILL BE GLAD TO RESPOND TO ANY QUESTIONS MEMBERS OF THE COMMITTEE MAY HAVE.

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The CHAIRMAN. I would like to ask Senator Moynihan to take whatever time he may wish because he needs to leave in a few minutes, and he wanted to make an observation. Is that all right, panel?

[No response.]

Senator MOYNIHAN. Mr. Chairman, I do thank you very much. The Senate is going into closed session on an intelligence matter and I have to be present at 10:30, or otherwise I would not want to miss a word, especially or not least, my colleague and friend from New York, Colonel Conable.

I would like to note, sir, and perhaps it would be useful to put in the record at this point, that the actuarial tables and estimates by the actuaries of February 5, which have just become available to us, showed the funds at the end of the year for the OASDI trust fund rising from $24.8 billion in 1982 to $257 billion in 1992. The estimates that we were working on seemed to agree with our judgment.

But mostly I wanted to express the honor that I have felt and I know the chairman felt to serve with persons of such strong views and complete knowledge of this system. Our country is well served, not just by your knowledge, but by the way you sharpen each other's wits by not always altogether agreeing.

Thank you.

The CHAIRMAN. Thank you, Senator Moynihan.

Congressman Conable.

STATEMENT OF HON. BARBER CONABLE, A U.S. REPRESENTATIVE FROM THE STATE OF NEW YORK

Mr. CONABLE. Thank you, Mr. Chairman, members of the committee. I may not literally have the last word here but I am appropriately placed in the middle.

I believe that my advice to this committee, particularly with someone on the panel like Senators Dole and Moynihan, is about as redundant as another snowstorm in Washington—I do wish to express my continuing support of the bipartisan compromise, and to address just briefly my hopes for the congressional matrix in which this compromise must move forward if it is to become law.

We are already hearing on both sides of the Capitol assumptions that the compromise will move forward without a hitch, and that, therefore, it becomes an appropriate vehicle for bearing additional freight. There may be freight appropriately attached, but I worry about excess freight weighing it down to the point where the compromise will not be considered on its own merits.

I have difficulties with the compromise. I am well aware of the realities of this system, but I'm also aware after 16 years of trying to deal with it in the House as a member of the Ways and Means Committee of the political realities affecting this system as well. Those are easily identifiable even in this room.

It seems to me that there is, as Senator Moynihan said in an excellent piece in the Washington Post, more at stake here than social security. The American people want the issue resolved with a degree of bipartisanship that can reassure them about the system's ability to handle sensitive issues affecting a great many people, and that reassurance will be drawn from our ability to do that.

It is not enough for the Commission to have made a bipartisan recommendation that must proceed and Congress, obviously, must participate in some sort of a professional process, which I hope among other things will deal with some of the objections that Congressman Archer has raised here today. It must deal with it in ways that do not change the basic structure of the compromise, however, or the compromise will come apart. In that respect, I would hope that just as we have limited the intrusions of general treasury money, both as to term and scope, so if we go to different fail-safes for the years 1985, 1986, and 1987, to which Congressman Archer has referred, we will not do it in some way that throws caution to the wind with respect to that particular problem.

In short, I hope we will maintain the spirit of this compromise realizing that there may be fine tuning—the serious notch problem, taxing of benefits or the reducing of benefits for high income people, whichever way you choose to look at that particular proposal. Just as we must have a bipartisan solution to meet the expectations that people now have about this particular crisis, so it must be a bicameral solution. To that end, I hope we can maintain the closest possible communication about the possible amendments that can be used to perfect the proposal.

I would hate to see us achieve some sort of a solution in each House only to find that each House had dug in its feet with respect to the details of that solution. So beyond bipartisanship, bicameral resolution of the problem is absolutely necessary.

My purpose in coming this morning is then to pledge my part in trying to keep the avenues of communication open. My determination to avoid excess baggage on this package; my intent to try to recognize both the realities and the political realities and to maintain the spirit of the system which has become terribly important to a very large number of Americans.

I acknowledge the attitude one has toward an institution of this sort is going to undergo some change in the course of this resolution. If it were not in trouble, that would not be necessary. If it were not in trouble, we would not have gone through this exercise, and we could still go brightly on with the system exactly as it was.

But the trouble is real, and it requires the very best in all of us. I would like to urge, then, that both Houses go forward as promptly as possible, doing what perfecting changes each seems to feel is necessary and staying in close communication throughout the process.

Thank you.

The CHAIRMAN. Senator Moynihan.

Senator MOYNIHAN. I have no questions, Mr. Chairman, except to wholly endorse Representative Conable's view that this must be a bicameral as well as a bipartisan measure. It couldn't be more correct.

Mr. CONABLE. Well, Senator Moynihan, over in the House we marvel at your rules sometimes. But, of course, you marvel at some of the fruits of our labor as well, I realize. [Laughter.]

The CHAIRMAN. I think you have just touched on a point that hasn't been addressed, and it may be addressed, I assume, first in the House. That is, what additions may be added to this so-called compromise.

Congressman Pepper, as chairman of the Rules Committee, will have a great deal of influence in what may be added on the House side. Maybe I am naive but I thought at the outset and it would be my hope now that we are going to try to pass a social security compromise, and not add on unemployment, civil service reform, railroad retirement, and prospective payment. But I get rumors of those additions and major tax measures also. Then it becomes insecurity instead of security because we have a lot of self-starters over here. The last time I counted, there were 100. [Laughter.]

The CHAIRMAN. They all have little amendments they would like to add onto this legislation. The bankers are hovering around town saying this is a good chance to repeal withholding. We have some other ideas for them that they won't like. But there are a lot of people feeling the pressure to add one little amendment to this package. I would hope that we might have some indication from the panel that we could try to keep it as clean as possible. Is that your hope, Mr. Pepper?

Mr. PEPPER. Mr. Chairman, there is one point that I would like to leave maybe to have you consider. Yesterday afternoon I had a protracted talk with representatives of the Government employees. Probably they are the most resistant group who are affected directly by the adoption of this package. They have very deep feelings about it.

I have tried to explain to them that we envision that current participants be protected in the system that they now have. And, as far as the new entrants who would be covered under social security, we envisioned that there would be an alternative system provided and enacted by the Congress which would be analogous to a pension system in private employment. That later when the new system was provided, that that new system plus social security would give them substantially the same protection they have now so that they are not really losing anything.

Of course, they have the same concern about something that has not yet been seen and not yet been done that perhaps some others have. So this thought developed in the course of our conversation. I said that if it could be determined as some have suggested—I don't know whether it is correct or not—that the amount of money the trust funds will receive from the first year of the inclusion of new Government employees is smaller perhaps than we anticipated in our report. If it could be determined that there would not be a substantial loss to the funds perhaps we could defer the effective date of coverage until January 1 of next year or until Congress would have an opportunity to enact an alternative program so that by the time it actually takes effect the Federal employees will see what they are getting; that we have done what we anticipated we would do and what we told them we were going to do.

However, I would not propose deferring coverage if the revenue loss was found to be substantial. Unless it could be done without serious injury to the package and the solvency and soundness of the program, I wouldn't advocate it. As Mr. Conable said, I realize this package is like a crossword puzzle. You take out one part and you have impaired the whole thing.

If you find that it could be done, though, it seemed to meet with a favorable reaction on the part of the Federal employees and I think they are more resistant, more determined in their opposition than any of the age groups are. I would just like to offer that for possible consideration.

Mr. CONABLE. Mr. Pepper, our proposal was that they not be covered until January of next year in the compromise. However, you are adding the suggestion that a contingency be adopted also so that in the meantime the Post Office and the Civil Service Committee get its work done, and that they know what the proposal will be before it triggers in. I understand that. That is always a possibility.

The CHAIRMAN. Can I ask Congressman Pepper the basic question? Is it possible to keep this compromise pretty free of a lot of extraneous amendments? There are going to be many efforts to add on major provisions on unemployment, civil service retirement, railroad retirement, and medicare. It would seem to me that it would be in our interest to pass a clear social security compromise. We have a deadline. We are told by the Social Security Administrator that we must have our work completed by early May. It seems to me the more we add to this bill, the more problems we will have.

Mr. PEPPER. Mr. Chairman, I can only say that I cannot predict what the Rules Committee will do. I don't know what sort of a bill the Ways and Means Committee is going to present to the Rules Committee, nor what the request of the Ways and Means Committee will be as to the kind of rule that they want.

As far as I am concerned as the chairman of that committee, we will do anything that can properly be done to give the Members of the House a full and fair opportunity to express their will without diffusing the package so much that it would perhaps provoke a result like the immigration bill—we had 100 amendments offered to that and it finally died. So we would certainly keep sharply in mind the desirability of the adoption of this package. We would do whatever we could properly do to further that end.

The CHAIRMAN. As I understand, the Commission wanted to deal with social security. That ought to be the priority—dealing with social security as quickly as we can. That doesn't mean that there may not be other worthwhile amendments, but I hope they will not be raised now. We are still going to have other opportunities to legislate.

Mr. CONABLE. It would be my assumption, Mr. Chairman, that if we don't keep it under control on our side, it would be a signal to the people in the Senate also that each can be his own initiator on the floor of the Senate. Unless we show some discipline, it will be difficult for you to maintain discipline on this side. Is that correct?

The CHAIRMAN. Well, it would be difficult anyway. [Laughter.]

We are very disciplined. We always try to limit ourselves to two or three amendments apiece. [Laughter.]

That's a total of 300.

Senator Chafee.

Senator CHAFEE. Thank you, Mr. Chairman.

My problem with this proposed solution, as it were, is that I just don't think it will take care of the situation for the long term. You acknowledge that. The problem is what do we do?

Mr. Pepper, in your remarks you said that if there is an emergency then Congress can act. But if there is an emergency, the only thing Congress can do in that emergency is to increase taxes because to me it is unconscionable to change benefits for the short term. You cannot—and you obviously agree with this, I believe—you cannot reduce benefits or change eligibility with a 1-year notice. Millions of people have made plans. Therefore, it seems to me that the time to enact the long-term solution is now. If it is determined that we have got to change the age, for example, now is the time to do it so people can make their plans that they are going to retire at 66 or 67 or whatever the figure is in 2015. But you certainly can't do it, as you suggest, by saying Congress can always act in an emergency. You can't change the age of retirement effective 1985 to the age of 66. You would wreak havoc with thousands of lives.

Mr. PEPPER. Senator, in the first place, we, I think, have made provisions adequate to meet virtually all the foreseeable circumstances in the future. One of the great accomplishments that I think is generally attributed to this Commission is that they divided the problem into two parts—short range and long range. The Commission concentrated on the components of each problem, especially the short-range problem. They came to the conclusion that if the economy performed according to the "best guess" projections, the so-called II-B assumptions, we would need more than $60 billion to supplement the old age and survivors' insurance fund between 1983 and 1989.

But if there were a poor economy, along the lines of the pessimistic assumptions, we might need as much as $150 to $200 billion to supplement the old age and survivors' insurance fund. This package raises $168 billion, which we think comes within the fair range of providing what we thought was needed.

Even if more is needed, the funding could be borrowed against the surpluses projected for the system in the future. For example, Mr. Robert Ball of the Commission, one of the most knowledgeable men in respect to social security, in the country—a former Social Security Commissioner under three Presidents—advised us several times that it was anticipated there would be a surplus in the old age and survivors' insurance fund by 1990. Large surpluses will begin to accumulate as a result of favorable demographic trends and the 1990 tax increase already scheduled under current law. Even if our Commission's proposals fall a little short of the system's need during 1983-89, and if we borrowed some money from the Treasury or allowed the trust funds to issue bonds or securities, Mr. Ball thought that amount borrowed could be paid back by the surpluses which would begin to accumulate by 1990.

Likewise, when we are talking about the 75-year estimate, Mr. Myers said that once we get over the short-range problem we are secure in the taxes already levied in the solvency and the soundness of the fund for the next 50 years. So the entirety of the long-term problem occurs in the period 50 to 75 years from now. That's precisely the period in which the estimates are the least likely to be accurate. That's because of how difficult it is to accurately determine what the birth rate is going to be; what the retirement rate is going to be or what the death rate is going to be 75 years from now. We may not be sure that we will have the right knowledge in respect to these matters so we have to just meet it the best we can. But as I said, Congress is going to be here for a long time. I think we have got a structure that has the capability to meet any likely emergency.

Senator CHAFEE. I don't want to disagree because you have given this a lot of thought, but it just seems to me we have been terribly burned by our estimates around here. We all sat here in 1977 and said this is great. I guess the President announced that this is going to carry us to the year 2020. It carried us about 3 years. It seems to me that the longevity is so significant. People are truly living considerably beyond the predicted figures of several years ago. I believe that is going to increase.

Mr. CONABLE. Senator, I couldn't agree more with the thrust of your remark. Our assumptions were, of course, moderate assumptions, not pessimistic. They chose the middle course. They were not the most optimistic or the most pessimistic. Clearly, we have to concern ourselves with what happens if we have a less than moderate economic pattern over this period of time.

But it's absolutely correct that while you can solve the long-term problem now, and should solve it now, if we have, in fact, a period that would justify the optimism that Senator Pepper shows here, it is always possible for us to back off. This Congress has demonstrated time and again that it can control benefits on people easily. However, you can't change the retirement age as of next Tuesday, and still avoid tearing the social fabric. So we ought to plan it now as to what might happen were the circumstances to be the worst. Future Congresses are perfectly capable of backing off if it isn't necessary.

Senator CHAFEE. Well, that's the point Mr. Archer made in his testimony that I thought was so telling. For one, I would like to see us solve this problem for whatever the foreseeable future is. Now I take it that 50 years is considered the foreseeable future. Is that the magic number?

Mr. CONABLE. Seventy-five is what——

Senator CHAFEE. Well, my time is up, but we will get back to this. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Bentsen.

Senator BENTSEN. Thank you very much, Mr. Chairman. Mr. Chairman, I have some comments I would like to put in the record. I thought it would save some time.

[The prepared statement of Senator Bentsen follows:]

STATEMENT OF SENATOR LLOYD BENTSEN

Chairman Dole, Chairman Greenspan, Senators Heinz, Moynihan, Armstrong, Congressmen Archer, Conable, Pepper, and each of the other members of the Commission deserve our deepest gratitude for the many hours of hard work and the care with which they crafted a package of recommendations designed to preserve the fiscal integrity of our social security system. As Senator Armstrong and Congressman Archer are especially aware, the compromise struck by the Commission contains provisions that—taken individually—are difficult, if not impossible to support with any enthusiasm.[1] Nonetheless, it is significant that the Commission did reach consensus on a number of issues that should enable us here in the Congress to proceed to the speedy consideration of several necessary policy and technical modifications in the current system. It is my hope that this committee will follow the example set by the Commission and arrive at a set of proposals through constructive deliberation—with the broadest range of views represented.

While none of us is completely satisfied with each of the Commission's recommendations, there are in my judgment, some very good proposals incorporated in the Commission's Report. The compromise provides long overdue incentives to encourage those who want to do so to stay in the workforce after the age of 65; it eliminates some serious inequities affecting women; it includes an indexing mechanism to link cost-of-living adjustments more closely to wages; and calls for a more appropriate allocation of the tax rates among the trust funds.

Members of the National Commission and of this committee recognize that much work remains for the Congress. Details of legislative language, transition arrangements, and the adequacy of individual proposals have yet to be debated and agreed to. The long-term gap between revenues and obligations must be considered, and adjustments made if the 1983 Trustee's Report finds major discrepancies between the assumptions underlying the Commission's recommendations and the projected solvency of the trust funds.

However, these as yet unresolved issues should in no way diminish the importance of what this Commission has achieved. I would like to extend my personal congratulations and thanks to each of you for your efforts. I am confident that with this beginning, we will develop and enact a package of provisions that will put social security on a sound financial footing and restore confidence in the System for millions of affected workers and retirees.

Senator BENTSEN. I share the concern expressed by Senator Chafee insofar as a long-term solution is concerned. And would like to see us address it if we can. But my No. 1 priority is what Barber Conable talked about—getting this compromise through. And that's why I am going to stay on course on this legislation.

If we can work out an accommodation and a compromise that lets people who are in their thirties and forties plan for the future, and look toward a retirement at an older age taking into consideration the realities of the advances in medicine and longevity then I want to do it, and will support that. But if it means jeopardizing the compromise then I will obviously oppose it. That is giving away my bargaining position early. I understand that.

But I think that the No. 1 priority must be to pass the compromise. One of the things that we ought to try to clear up, it seems to me, is this question posed by the Federal employees who have been quite adamant in their concern. As I understand it, what Robert Ball says, is that what we are talking about on the new Federal employees is using the social security system as a base just as you do in the private sector, often on a private pension plan. That there would be a supplemental contribution made by the new employee to the civil service retirement system.

Now one other point that has been made by Federal employees to me, and I think a very justified one, but probably a misunderstood one on their part is that what happens to the Congress is not clear in the Commission's recommendations. What happens to the Members of Congress? Now I believe that the bill, S. 1, takes care of that.

What is the Congressman going to do under the social security system? We, like the civil service employee, would have to pay the supplemental amount. And I think that's the way it ought to be. I

[1] Armstrong and Archer voted against the final Report.

think that ought to be clearly understood by the Federal employees. That Congress is putting itself under the social security system, and will not be an exception to it. And that what we are saying is applicable to them is going to be applicable to us.

I would like a comment by any one of you.

Mr. CONABLE. Of course, under the proposal by the Commission only new Members of Congress will be covered in this way. I must assure you that there are a number of people on the House side who want, in the usual tradition of congressional masochism, to be sure that all Members of Congress are covered as quickly as possible. I believe that will get an adequate airing on our side, whatever happens over here.

I must say that there are computations in such a move; particularly, in the Senate where everybody has unlimited outside earned income. You pay self-employment tax on all your outside earned income. That's to be covered as congressional employees, as Federal employees, and would involve a tax reduction for you from 75 percent of the social security rate to 50 percent. I think you have to keep that in consideration when you move quickly to cover Members of Congress that what you are doing is reducing your taxes if you, in fact, pay a self-employment tax as I assume you all do on your outside earned income for speech honoraria.

Senator BENTSEN. Since I don't receive any honoraria, I am not as familiar with the point as you might be.

Mr. CONABLE. That replies totally in the face of the eloquence of the gentleman from Texas. I am sure he has tremendous bargaining power with the groups that seek this.

The CHAIRMAN. In S. 1, Members of Congress will be covered as of January 1, 1984.

Mr. PEPPER. New Members of Congress, the new Presidents of the United States, new Justices of the Supreme Court, and everybody who is on the Federal payroll will be covered. New Members, like new entrants to the civil service of the Government, would be subject to having to pay social security.

It would be a little harder, I think, to change our own system that we now have. I looked at my accounts the other day and seemed to me I paid somewhere around $400 a month into our own retirement program. A lot of people don't realize I think how much we pay into it. It might be a little bit more difficult to come up with an alternative such as we are proposing for the civil service people than it would be in their case.

But may I just say one word about this matter of raising the eligibility age? It looks like a simple solution, but we all recognize the mental effect or the physical reaction that we get, spiritual reaction we get, from certain proposals.

Senator BENTSEN. Let me say to the Congressman that I think it is pretty academic in your case. I can't imagine you retired.

Mr. PEPPER. I didn't hear what you said.

Senator BENTSEN. You just wanted to hear it again. [Laughter.]

Mr. PEPPER. May a wise counsel prevail. [Laughter.]

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Mr. Chairman, I, like most everyone here, would like to compliment the panel, the Commission, on the work you have done. I think it is a great stride forward in trying to find the balanced compromise that all of us know is necessary if we are going to satisfy the concerns of most people in the country with respect to social security.

I wanted to urge this body on this side to pledge, if possible, its constraint in not adding excess baggage because I fear that, as pointed out by Barber Conable, just as restraint on the part of the House in not adding excess baggage will help us on this side exercise the discipline necessary to not add excess baggage, it's important for us on our side to first send a message to the House that we will not either add excess baggage so the House Members also are constrained.

It is true that there is a tendency for members of this body to add on all kinds of amendments. I am one of the offenders, as most everyone else on this panel is. But I would hope that in this situation, because of the importance of social security, that we on this side send a very strong signal to the other body that we, too, exercise a restraint.

I have a second point to make and that's sort of a footnote to the point made by Senator Chafee with respect to the long-term needs. I, too, would like to find a long-term solution, but I don't know if we can at this point find a much longer term solution. I understand that insurance companies—life insurance companies, health insurance companies—revise their estimates, revise their premium schedules, recrank through the actuarial tables as to what is happening in America about every 3 or 4 or 5 years. They don't plan 75 years in advance. They don't plan 50 years in advance. They really don't plan 10 years in advance because times change; circumstances change. It's impossible to predict what the country is going to be like 75 or 50 or 10 years from now. So we have to do the best we can.

I, frankly, have belief and confidence that we will meet those changes when they occur, just as the Commission has come up with a solution to review the changes of the social security system, and just as I think the Congress will by and large enact the Commission's proposal.

However, I do think there are a couple of soft spots in the Commission's recommendations. I think we have to give some guarantees, some certainty to Federal employees. They are worried, legitimately worried. I think the suggestion by you, Congressman Pepper, is a very helpful suggestion to meet that concern.

I also feel that small businessmen are bearing too much of the burden. Perhaps Congressman Archer, perhaps Senator Armstrong would agree in some respect to that point. Perhaps that can be changed slightly.

We can make some adjustments. We should make some adjustments. It is my firm hope that making those adjustments to satisfy the concerns of Federal employees, and perhaps some other concerns, that we do not add unemployment compensation legislation, do not add prospective reimbursement, 10 percent withholding—repeal 10 percent withholding or whatever because I think that would be a disservice to the senior citizens, to the country generally if we were to do so.

The CHAIRMAN. Thank you. I appreciate that signal. I met with Congressman Conable briefly before the session, and I believe that we ought to assure each other—Ways and Means, the Finance Committee and other committees—that it is our purpose to cooperate and not try to load up the bill.

Mr. CONABLE. Mr. Chairman, I have an 11 o'clock appointment with Chairman Rostenkowski to discuss this very matter. I will carry your message, if you will excuse me at this time.

The CHAIRMAN. Could I first recognize Senator Long? He is next. He may have something to say. He has been around to see more horses go through here than——

Senator LONG. Well, I actually wanted to direct this question to Mr. Archer. I would have anticipated that Joe Waggonner, being one of the Presidential appointees, was going to sign onto this Commission proposal and that he was going to be urging me to support it just as it came in. My communications with him prior to the time the Commission made its report led me to believe that he thought the matter was going along pretty well, and that the proposal would be something he could recommend. He is highly regarded up there in that area of Louisiana where I was born. Those are good salt-of-the-earth people.

A lot of people have said, and I think with good justice, that Shreveport is a small-scale Dallas. It has about the same philosophy that you see there. Those are very devoutly religious people, and they work hard. And they believe in the fundamentals that made the country strong.

Mr. Waggonner expressed the same concern that you have expressed here, but he used a somewhat different figure, that does shock me. You are saying here that it is the estimate of independent actuaries that the combined cost of the OASDI and the HI funds will require 32 percent of payroll in the year 2030—just for those items, not to mention the other costs of Government.

I find that shocking. Is that figure generally agreed to by those who served on the Commission, that this is about the kind of cost that we could anticipate at that point?

Mr. ARCHER. I can't say that it was, Senator, because the members of the Commission were basing their judgments on the actuaries' projections over at SSA; not by outside actuaries.

I have a feeling—I can't prove this—that from time to time the premises that are given to the actuaries at SSA are to some degree determined by political judgments. I, personally to be safe with social security, would rather really be eclectic in working at the problem, and look at some of the outside actuaries that are not under any political pressures whatsoever.

Obviously, they are not going to guarantee you that that is what it is going to be. They think that's a potential range for it to fall in. There are uncertainties in all these actuarial projections, but I think we have got to take into account the range. I agree with Senator Chafee that we have got to make decisions on the long term. We've got to strike now, I think, at this moment while we have the opportunity to do so. Otherwise, our options become so limited, if we let them shrink into the short term.

But some people will even say—and I didn't use this bizarre figure—but some of the outside actuaries say it could go to 40 percent of payroll.

But certainly 25 to 30 to 32 percent of payroll seems to be in the ball park for most of the outside actuaries that I have talked to.

Senator LONG. I recall how we got into this fiasco in the first place. As I recall, it all started out at the time when our dear friend Wilbur Mills, whose State borders on your State and mine, undertook to try to become President of the United States. I thought that when he started that he was most cautious in what he was saying and in his pronouncements. He came and made a statement to the Louisiana Legislature against revenue sharing. Later on he was compelled to abandon that position.

Then he got involved with the bill on social security. Right in the midst of a New Hampshire primary, he sent a wire down here instructing the Senate Finance Committee to amend that bill to increase the benefits by 20 percent, to give everybody automatic cost-of-living increases in the future, without any taxes to pay for that, just to finance that on an optimistic assumption.

Mr. Ball and a lot of the people in the department at that time thought that this was a proper thing to do. The proposal failed in the Finance Committee, as I recall, either on a tie vote or by one vote. But when a similar amendment was offered out there on the floor, the whole Senate caved in, including some of those courageous statesmen who had spoken against it within the committee. It was an 82-to-4 vote, to give everybody a 20-percent increase, automatic cost-of-living increases in the future, with no tax increase, just finance the whole thing on optimistic assumptions.

That assumption has proved to be an error. It seems to me that somehow or another we are going to have to find a way to work our way out of the trap we are in. Look what it's done to people who have come along since that time—Pat Moynihan said to me that since he had been on this committee he had not been able to vote to raise benefits. The only thing he has been able to vote for is to raise taxes and cut benefits. That's how far we have gone beyond what we could afford.

One way or the other, it looks to me as though we are going to have to start to move to get this genie back inside the bottle. Mr. Waggonner testified yesterday, and the way I read it, he is not hoping to defeat the bill. He just hopes that by the time we get through amending this bill, that it would be something that he could recommend.

My understanding is that what we really need here is to put something in that the Commission has recommended, and we may need to go beyond that. They recommended a fail-safe provision that says in effect if you don't have the money to pay as much benefits as they anticipate that you may not have as much cost-of-living increase as you would like to have otherwise. If the taxes that we are voting here are not going to pay for all the benefits that we hope we can provide, especially without reducing the benefits those who are now receiving them, and even paying them the cost-of-living increases—if we can't do any better, at least for those coming on in the future we should find a way to compute the benefits so as to somehow keep the costs within what we are able to pay for. I believe you have got a real cause for concern that the people of this country just don't want to keep on and on raising these taxes, especially when you are talking about a possible 32 percent of payroll a year at some time in the future.

Now do you have some suggestions to make as to how we could get the genie back inside the bottle?

Mr. ARCHER. Well, Senator, I think you are certainly accurate in your description of what occurred back in 1972. I was here in my first term at that time.

In 1971 there was a 10 percent across-the-board increase in benefits when inflation was running 4 percent. The Congress came back, in what you adequately described, in 1972 with an additional 20 percent which it compounded was 32 percent across-the-board in 2 years at a time when inflation was running an average of 4 percent per year. They did it without any provision to pay for it except, as you said, the Pollyana projections.

I argued with it then. I voted against that. In 1973, the Congress came back again and wouldn't even let the inflationary escalator take effect that had been provided in 1972 to take effect in 1974 because of this tremendous advance in increase in benefits. They said, well, we have got to do something again in 1973. So they added again another across-the-board. It was either 7 or 11 percent that was on top of what was already done in 1971 and and 1972. Again, inflation was still running 4 to 5 percent per year at that time.

I stood on the floor in 1973 and said, "I can't leave this legacy to my children. We are creating a half trillion dollar deficit in the social security fund." A lot of people said to me "Boy, that's great information. Bill, you have got a lot of courage to get up there and speak out on this issue. Nobody has ever done it before that I can remember. I guess you are right, but, Bill, I can't vote with you because you can't be reelected if you vote against this bill."

Twenty-three of us voted against it out of about 400. It was a big vote. All 23 of us were reelected, by the way. It's the best vote we ever made because it was one-half trillion dollars. When the actuaries finally put the pencil to it a couple of years later, it was $4 trillion in deficit.

That's what we are trying to dig our way out of today. The Senator is absolutely right. That's the main reason—in those 3 years, plus the late 1960's—that we have benefits today that are about 52 percent higher in real purchasing power than they were back 15 years ago.

Now it is always easy to go off on the benefit side. It's very difficult to start hammering out programs that are going to restrain the spending outflow so that it is manageable, is affordable, as I mentioned in my testimony. I think we have got that responsibility. The ultimate solution isn't going to be everything that I want, but I sure would like to see it more in a balanced package that I can tell my children and grandchildren that they will be able to afford. I can't do that with this Commission proposal.

Senator LONG. Mr. Pepper.

Mr. PEPPER. Yes, Senator, if I may attempt to respond to your very interesting and very profound suggestion. In the first place, that 32 percent of payroll figure includes the projected cost of medicare, not just social security cash benefits. Is also assumes no reductions in the skyrocketing cost of medicare, which we are all seeking to achieve now.

In the second place, as to what caused the situation that we now have. I respectfully submit that it is two things that caused it. The first is that in 1972 we provided that the CPI would be the criteria of the COLA, the cost of living adjustment. Up until that time, wages had always exceeded the cost of living increase as measured by the CPI. The whole economic situation deteriorated immediately beginning with the next year and for almost every year since, the CPI has exceeded the wage increase. And even as we tied the cost of living adjustment to the CPI the incoming contributions, based on wages, slowed down relatively. And that tended to bring about the imbalance.

The second thing that contributed to the current shortfall started, a few years ago during the Ford administration when we began to have a heavy rate of unemployment. This trend is much worse now. The unemployment rate was 7.4 percent when the President took office—President Reagan. It is currently above 10 percent. This problem extended through the Carter administration and all the way back to the Ford administration. So we go back quite a number of years until we come to the climax of the present where we have got 12 million people that we count as unemployed; not including 2 million that have quit looking for a job that are out of a job.

Now all of us can easily imagine how much money this staggering level of joblessness cost the trust funds. Even if we just took the difference between 6 percent—euphemistically called full employment—and the present 10.4 or 8 percent, and we considered those people. Look at the billions of dollars that those working people would be pouring into the social security fund and the amount of money that the employer, who, of course, pays the same amount, would be contributing to the fund.

So it isn't, social security so much that needs reform as it is our economy. When we get our economy back on a normal basis and a normal level, the social security structure is adequate to sustain itself the way we provided for it.

My last comment, Senator, is that we affirm to the American people that the Commission had the benefit of sensible, wise, competent people in the economic prediction group, analysts, and the like. They say we do have a sound system with the revenue that we have provided. That if it needs a little implementation out there in distant future 70 or 75, years from now, an increase of less than one-half percent or one-tenth of 1 percent in the payroll tax would bring it up to the required level.

May I add one other reminder. They tell us that wages, actual cash salaries received by working people are going to diminish in years ahead relative to their total compensation. This is because they will get an increasing amount of their total income, their compensation, in things such as in-kind benefits that we so far don't tax. So the prospect, I think, is not quite as dreary as my friend would think it is.

Senator LONG. It does concern me, gentlemen, that I have seen low estimates come out of that department so many times. Abe Ribicoff had a proposal when he was Secretary about social services.

They said that would cost us $40 million a year. The year we managed to finally get some kind of a cap on the program, it was projected to cost over $4 billion that year. That was 100 times the estimate. When they came in here with medicaid, they said it was going to cost about $200 million in the first year. I think everybody will agree that the cost was exceeding the estimate 15 to 1, and then went on up to where the cost now exceeds the original estimate by about 100 to 1. Anybody can see just on the face of it, looking back on it, that it would tend to turn out that way. It does dismay me to see them start programs like that—and then if the program didn't exceed the cost, they would proceed with the benefits in such a way that it did exceed the cost.

It just looks like altogether too often people are either not being conservative, or else they are taking an irresponsible attitude. I just suspect they had to know in their hearts that their proposals were going to cost a great deal more than they were telling us up here on Capitol Hill. That then became our problem—to find a way to pay for a program once it was passed, especially the way the program was administered.

Mr. ARCHER. Senator, I certainly agree with you. And I think the projections now are going to prove to be totally optimistic. I think longevity is going to increase far beyond what the projections are from the actuaries. We are spending $1 billion a year right now in cancer research. And this country wants to find a cure for cancer. We all want to find it. And I think we will find it.

When we do, the average life expectancy could well jump another 10 years in a short period of time. So the actuaries are taking, in my opinion, still very optimistic projections for the long term.

Senator LONG. Thank you very much, gentlemen.

The CHAIRMAN. Thank you. I understand that Senator Pepper has to leave at about 11. He was supposed to leave at 10:30 but he has stayed on. He now has to leave at about 11:15.

I think the problem may be the New Hampshire primary. [Laughter.]

Maybe we can address that easier than we can this. There are five Senators already running, and others willing to run so who knows what will happen.

Senator Bradley?

Senator BRADLEY. Thank you, Mr. Chairman.

Let me ask both of the Commission members who are here to try to deal with the question that we discussed yesterday, which was alluded to a little bit today in a couple of the comments. That is the beef on the part of young people that it is not going to be there when they get to retirement. I find that in the last month I have probably talked with over 150,000 people in a series of very intense meetings that they don't believe it's there. They don't believe it is going to be there. They are more and more suggesting their own voluntary retirement system that fundamentally doesn't understand the nature of social security.

I'm curious how each of you would propose to reassure the generation of workers who are out there under 45 or under 50 who fundamentally don't believe that this system is going to be there when they retire. Now with the senior citizens, who we have also dealt with, you can kind of reassure him or her because their check is going to come. The rhetoric that surrounded the issue with regard to senior citizens was that your check isn't going to come. When they see their checks coming, they are reassured, and they think things are going to come out OK.

For someone who is not going to get their check for 30 years, there is just an enormous reservoir of suspicion and doubt that it is ever going to be there. I see it as a very serious problem. I am curious as to how each of you would respond to that.

Mr. PEPPER. Senator, I mentioned that in my opening statement.

What this package does is that it really comes to grip with this problem. I remarked about this cynical attitude of the young toward the present system, up until this package was proposed with the approval of the President of the United States and the Speaker of the House of Representatives and 12 members of this Commission. This is the first affirmance by the President, and if approved, as I hope it will be, by the Congress of the United States that they are going to get what they are supposed to get when they come to the age of entitlement.

Since the agreement, I have noticed a change in this attitude as I have been around over the country. Shortly after this package was agreed to I went to a football game and I noticed a number of young people who stopped me and said something like, "We appreciate what you are trying to do for us up there. Not just for the old people, but we appreciate what you are trying to do for us up there. You all seem to be concerned about our problem."

We have assured them that this is a good package. We have had competent people advise us, and we are committed—the President is committed and the Congress will be committed if it adopts this package. We are going to keep social security solvent and sound for 75 years.

I think that is very meaningful to the country, and very reassuring to the country.

Senator BRADLEY. So your position is that the short-term package takes care of the long-term problem?

Mr. PEPPER. The position of our Democratic group on the Commission is that the short-term package that we have presented comes within 5 or 4 percent of meeting the anticipated needs way out there in 70 or 75 years, but to be sure, we propose to add .46 percent to payroll tax in the year 2010 in order to be sure that there would be enough revenue to meet whatever demands that we can anticipate at that time.

So we propose that it will be solvent and sound 75 years from now as well as 50 years from now.

Senator BRADLEY. What would the age have to be raised to?

Mr. PEPPER. It would remain the same as it is. Our contemplation does not change the basic structure of social security one iota.

Senator BRADLEY. All right.

Mr. PEPPER. We don't change the age of eligibility. We don't change the benefit formula or the "bend point." We don't change the other fundamental provisions of the social security law. That is what means a lot also to the young as well as middle aged people.

Senator BRADLEY. If I could, I would like to ask Congressman Archer if he wants to say anything.

Mr. ARCHER. Well, I would like to respond to your question, which I think is an excellent one. I think the young people would believe in social security when we have submitted a credible, not politically dictated, answer to the social security problems. That means, in my opinion——

Senator BRADLEY. So what you would have us do is increase the age of retirement and then change the method of indexing benefits, and a number of options designed to relate benefits more closely to the taxes individuals contribute to the system?

Mr. ARCHER. Yes; I think that the young people can have confidence in a system when the benefits relate to the moneys paid in during a work life because then it makes sense.

Senator BRADLEY. So that you would receive no more benefits than what you have paid in?

Mr. ARCHER. Pardon?

Senator BRADLEY. What do you mean?

Mr. ARCHER. That was the last of the alternatives that I mentioned there, which is we may not be able to do it all the way, but the ultimate goal should be, I think, to relate benefits to what you have paid in during your tax life. I don't think it's economically conceivable to put the money aside and retain it for the retirement of that particular beneficiary.

Senator BRADLEY. I don't want to cut you off, but the light is there and I want to get to the last question because I have to go.

Mr. ARCHER. Sure.

Senator BRADLEY. Let's get to the issue of taxing the benefits. One-half of the benefits above nonsocial security income of $25,000.

Two questions. Did you consider not taxing any benefit until the person has received back everything that they put into the system, which would be about 3 years?

Mr. ARCHER. The answer to that is "yes."

Senator BRADLEY. Would you consider indexing that number? If you earned $12,000 in 1972, the equivalent of $12,000 in 1972 is $25,000 today. So if we put a $25,000 threshold and then you are taxed, you could, in real spendable income, have a greater number of people go over the threshold 10 years from now. So those are two questions. Would you consider deferring any tax until after all the tax that has been paid in is paid out? Second, would you consider indexing the amount before you go to any tax?

Mr. PEPPER. Senator, I will attempt to answer the first, if I may. In the first place, if the Commission had made the proposal that you suggest—deferring the beginning of the tax until the recipient and working people receive back what they had paid in—I would have been glad to have supported it. But now we have a package, which is a balanced package. Lots of people have signed the approval of this package based upon other provisions that were in it.

For example, at one time the President said he would not support a package that provided for additional governmental revenues. He has. He one time said he would not approve anymore taxes to sustain the system. He has. Revenue is actually going to be appropriated in order to cover the cost of gratuitous military wage credits.

So we have got a package that is supposed to yield $168 billion. We have been discussing here this morning the possibility of our estimates being low. What do we do then? I don't want to do anything to reduce the size of the package because we have put it all together. The package is sort of like an arch. Each brick helps the others to support the structure above. Each part has its own part to play in the structure. So I couldn't agree to take out so many billions of dollars from the package and reduce it down to a lower figure so there would be a greater likelihood that we wouldn't have enough money. In principle, I don't object to it. As I said a while ago, that tax that we imposed upon half of the revenue of the social security benefits that one receives is the same tax that today people are paying on unemployment compensation. It's the same tax that civil service retirees are paying on their retirement benefits. It's nothing new in principle to require it.

There has been a feeling for a good long while that people like me, for example are receiving a tax-free windfall. When I was a practicing lawyer for a good many years, immediately I became eligible for social security. I hurried to get my contribution in. I paid it. Then finally after I had been here 10 years, one day I came to my desk and there was a check there. A social security check. I called my secretary in and said, "What's this? I'm not retired." She said, "Yes, but you are 72 years old."

It meant that when you got to be 72, regardless of your amount of income, you received it. Now I am in that category of people. I don't mind paying it. I have noticed among my personal, professional, and social friends who are up in higher brackets—lawyers and physcians—think we ought to have been paying it a long time ago. Only 11 percent of the people receiving social security will pay the tax.

So on the whole, I think what we have done is a reasonable thing, a reasonable approach to the problem. We had to get the money from somewhere. These people, generally, will be hurt less than maybe other people would be who had to contribute the same amount.

Your last question was about—what was it?

Senator BRADLEY. Indexing.

Mr. PEPPER. Oh, the indexing. Well, there, again, I am not in favor of the indexing principle. I'm not in favor of continuing the indexing that we are already doing on income. I would favor repeal of that law that we passed in 1981 to index incomes in the future.

If it stood alone without any relationship to indexing generally, I wouldn't have any particular objection to it because as I said before you arrived, last night I was on a talk show program from Boston. One of the questions asked: Are you folks going to lower that $20,000 or $25,000? I said "No, in my opinion." It was proposed that we start that and we opposed it. Finally, the Commission agreed on $20,000 to $25,000. I hope Congress never will go lower than that. I would rather have seen it $40,000 or $50,000 than $20,000 or $25,000. I hope we will pass on the hope to the future Congresses that they won't change that figure below what it is now.

Senator BRADLEY. On the flip side of lowering the $25,000 is not indexing it and having inflation push more people up to the level where they have to pay it.

Mr. PEPPER. If that occurs, it will be a general change that will occur. It won't be just that particular income. It will be a part of the general picture. The whole economy will be moving forward in the same way.

The CHAIRMAN. Senator Pryor.

I understand we have kept you now beyond your second time limit.

Mr. PEPPER. I will stay to see what my distinguished friend has to say.

Senator PRYOR. Mr. Chairman, I will try not to take all of my time.

I would just like to thank Congressman Pepper and Congressman Archer for serving on this Commission. I think that's a bold thing to do these days because that was certainly a very difficult decision that we all had and have to make relative to social security. I applaud both of you for doing it.

I would like to ask one or two questions very briefly about the merger of the two systems. I have a great fear that these have been covered. But if they have not covered them in the record, then certainly you may say so.

Do you feel that the reason the Commission sought to merge the two retirement systems—social security and civil service—into one—was that an economic decision or a philosophical decision?

Mr. PEPPER. Well, I will say to my distinguished friend that it was—you might say it was both. We have got a social security system that affects 95 percent of the people of the country. The Government workers of this country of 2 or 3 million people ought not to be outside that system. If it is good enough for all the rest of the country, it ought to be good enough for participation by the people who are on the Federal payroll.

But at the same time we had to take account of the fact that they have already got a system in which they are very heavily involved and which means a great deal to them. We must safeguard the rights that they already have under that system. Those that are covered by it, been paying into it, and who are drawing benefits. So we had to mesh the past and the future. We thought the best way to do that was to pass as soon as we can a new bill setting up an alternative system, which would resemble a pension, as one of the Senators said. A pension system that a private employer has where an employee will belong to the private pension system of the company, and will also belong to social security. We thought that was the pattern that we should seek to pursue with respect to Government employees. That's the reason I suggested a moment ago that it would be so reassuring to those people if we could enact that alternative system before this takes effect to show them that we really did intend to be fair to them, and see to them they have a two-tier system in the future instead of a one tier system as in the past.

But the two together would give them substantially the same protection that they have had in the past.

Senator PRYOR. Do you feel that the merger concept is necessary not only to the passage but also of the workability and the viability of this entire package?

Mr. PEPPER. Yes, sir, the Government pays a very heavy—I think it's 30-odd percent of payroll contribution into that civil service retirement system that we now have. It may be a little bit too much to expect that they will maintain altogether the new system at the same level when they have also got social security down below. So our concept was to put the two together and give them substantially what they have got now in the coverage of the two. But at the same time not deprive them, as you don't deprive employees from belonging to a private pension system. Don't deprive them from the right that we Members of Congress have—to pay more into our retirement system, far more than we would pay if we were covered by social security. But, of course, we get far more back in the case of retirement than we would receive that way. We want to preserve that option for them.

Senator PRYOR. Mr. Chairman, I won't use all my time. Thank you, sir.

The CHAIRMAN. Senator Heinz.

Senator HEINZ. Mr. Chairman, I just want to welcome my former colleague. We worked together in the House for so many years. We worked on this Commission for what seems like so many years. We both had similar responsibilities on our respective aging committees for a number of years. Not nearly long enough from my point of view.

Mr. PEPPER. These two gentlemen—the Senator from Pennsylvania and the Senator from Arkansas—have worked very hard in their contribution to the elderly people of this country. Senator Pryor started the elderly movement really in the House a long time ahead of any of the rest of us. He didn't get to realize all the fruits of it that some of us later did from his——

Senator HEINZ. If Congressman Pepper will permit me, I think the reason that you were able to become chairman of the Aging Committee is that I was able to steal then Senator Pryor's idea. I stole it quite fair and square. He ran for the Senate; lost; and wasn't around to look after those interests. Bill Archer here, as well.

I want to ask you, Claude, one question. Some people in looking at what the Commission has accomplished over the long term have, frankly, in my judgment either not perceived what we have done or have belittled what we have done, perhaps out of ignorance. They accuse the Commission of kind of having somehow ducked the long-term issue. Not to the extent that we only addressed two-thirds of the 1.82 perçent of taxable payroll. We recognize that we haven't addressed the entire problem. But we have a gentlemen's agreement that we are going to do it through the legislative process, and that while we have a gentlemen's agreement to disagree on how to do it—we know each other's feelings on raising the retirement age—we are united in the fact that we must do it. That's what our report says.

Second, if you look at what we have recommended on how we propose to address the 1.22 percent of taxable payroll that we have addressed, the fact is that we have made some real changes in the program so the program will not live beyond its means. The taxation of social security benefits—I don't want to get into the semantic argument about whether that is a cut in benefits. I think I know Claude's position on it. He would not call that a cut in benefits. I think I know what it is. I think it will reduce the benefits of social security to certain classes of people. But I would agree that it is technically not a cut in benefits. The 6-month delay is technically not a cut in benefits, but reduces the growth in benefits so much that that is worth three-tenths of 1 percent on the benefit side.

So what we have done, to those skeptics who say Congress has not had the courage to really address the question of whether social security will be able to live within its projected income—these changes represent a major and very courageous commitment of Congress to make some adjustments that while not being benefit cuts have an effect on beneficiaries. Anybody who thinks that that was not a major and courageous undertaking by the Commission as a whole, I think, is just plain dead wrong.

I just wanted really, Mr. Chairman, to make that point and to commend my friends and colleagues on the Commission; particularly, Claude Pepper and Bill Archer, for their invaluable assistance in helping us fashion a package. I know Bill had some different feelings about how that package should be shaped. I respect his feelings in that respect. But, frankly, his contributions, had he not stuck by his convictions—what we were able to achieve might have been quite different and from his point of view less good than even now it appears to be to him. So I thank you very much.

Mr. PEPPER. Thank you very much. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Grassley is next, but if you have to leave——

Mr. PEPPER. Here's another distinghished member of our aging committee.

Senator GRASSLEY. Thank you, Congressman Pepper. I appreciated how fairly you treated me the 2 years I was ranking Republican on the House Select Committee on Aging my last 2 years in the House.

I have no question, but I would implore you as a person who I know to be fair and honorable to see what we can do to put together a total package. As Senator Heinz said, this is two-thirds of the problem—what the 12 people voted for. I suppose we ought to accept the view that two-thirds of a loaf of bread is better than no loaf at all. But I think that we have gone through the debate in 1977 and now 2 years waiting to get to the point where we are today, and that when this is all done, the best we can do not only for the senior citizens of America but also the working contributors to the trust fund is to say that this Congress bit the bullet and we came up with a program that is sound for the next 75 years.

I know that you have taken some adamant positions. You are a recognized leader in this area, and you are respected. But also I think from the standpoint of that respect and that power you are a person who can lead the way to finding a solution for the last one-third of the loaf of the bread so that we can announce when the President signs this bill that we have taken care of the problem 100 percent. That as we can see into the future, 75 years as we do each year, this is a solution. I would implore you to do that.

Mr. PEPPER. I heartily agree with the able Senator in what he says. I have tried as best I could in contacts with the public and otherwise to assure them that we have provided stability, soundness for this program for 75 years into the future. The only thing is there is a difference in the recommendations—there are two separate reports. One report approaches the matter by reducing benefits, as I would say, by increasing the age limit, which would no doubt accomplish the result. The other part of the Commission, the group with which I was associated, would do it by increasing the payroll tax. That also, I am assured, will do the same thing. So by either method—I prefer the method of increasing the payroll tax because that leaves no question about not reducing the benefits. I think that is fairer to the people in the future who are not here to speak on this.

I have said everywhere I have spoken that this is a package that is good for 75 years.

Senator GRASSLEY. I guess what I am suggesting, then, is that maybe from your position of leadership in this area, and Senator Dole's, that there is an area of compromise even between these two extremes that we can announce that we have a total package where the 12 of the 15 would even agree on the 100 percent as opposed to two-thirds. That's all I have to say.

Mr. PEPPER. Thank you, Mr. Chairman.

Senator PRYOR. Mr. Chairman, before Senator Pepper leaves—he can go ahead and leave certainly, but I just wanted to make a little statement for the record. Senator Pepper, we claimed him in Arkansas because I think, Claude, it was in the late 1930's or early 1940's when a young Claude Pepper, professor of law, came to the University of Arkansas and taught there for 1 year.

Mr. PEPPER. 1924 and 1925.

Senator PRYOR. In 1924 and 1925. All right, I was wrong on my date.

Mr. PEPPER. Senator Fulbright was one of my students.

Senator PRYOR. That's right. Bill Fulbright was a student to you, as I understand. You were thinking about at that time establishing your political base in the State of Arkansas. I was just sitting here thinking had he done that, I would probably be back home and he would be the Senator from Arkansas.

Mr. PEPPER. My feelings told me you might come along some time and I had to go to Florida. [Laughter.]

The CHAIRMAN. There is still plenty of time, Claude. [Laughter.]

Mr. PEPPER. Thank you, Mr. Chairman.

The CHAIRMAN. Our next witness is the Honorable John Svahn, Commissioner of the Social Security Administration.

We appreciate very much Congressman Pepper, Congressman Archer, and Congressman Conable coming.

STATEMENT OF HON. JOHN A. SVAHN, COMMISSIONER, SOCIAL SECURITY ADMINISTRATION

The CHAIRMAN. Jack, you can proceed in any way you wish. If you want to summarize your statement, the entire statement will be made a part of the record. We do have some questions.

Mr. SVAHN. I appreciate that, Senator, and thank you very much.

In the interest of time, I will, if that is permissible, summarize just briefly. I will make a couple of comments and move right on to the questions that the chairman and members might have.

I appreciate the opportunity to appear before you today to discuss the financial condition of the social security program, and the recommendations of the National Commission on Social Security Reform. I can summarize what this administration believes about the bipartisan proposal for resolving the crisis we face in the social security system. It is simply this: What the Commission has proposed may well not be the best of all worlds for all of the points of view that have focused on this crisis, but—and this is a big but—the Commission's proposal is clearly the best possible solution that we can expect given the real world we find ourselves in.

There is no need for me review with this committee the urgency of the situation or the importance we attach to the restoration of the fiscal integrity of and public confidence in the social security system. After 2 years of intense debate, there is now a much better public understanding of both the nature of the social security program as a pay-as-you-go system, and of the fundamental issue of social security expenditures exceeding social security revenues.

We believe that this Congress has a once in a generation opportunity to do what the people of this Nation demand we do on behalf of their social security system. That is to resolve the financing question, and to get social security out of politics and out of the headlines and back into the confidence of the American people.

None of us likes all of this package. All of us dislike certain parts in this package. But the package is a very fragile one and has to be looked at as a whole. In looking at it as a whole, we find that the President has endorsed the package, that the Speaker of the House has endorsed the package, and that the Majority Leader of the Senate has, as well as three members of this committee who served on the National Commission on Social Security Reform. I certainly endorse it, and hope that we will be able to get social security out of politics and out of the headlines.

With that, Mr. Chairman, I would just say, that basically summarizes our statement. I am here this morning with Mr. Paul Simmons, Deputy Commissioner of Social Security on my left, and Mr. Harry Ballantyne, the Chief Actuary of the Social Security Administration, the man who has been working overtime for the past month or so in order to break out the various estimates on different proposals. I would be glad to answer any questions that you have.

The CHAIRMAN. Thank you very much. That is a good summary. The statement will be made a part of the record.

[The prepared statement of Commissioner Svahn follows:]

STATEMENT ON SOCIAL SECURITY FINANCING BY JOHN A. SVAHN, COMMISSIONER OF SOCIAL SECURITY

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, I APPRECIATE THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY TO DISCUSS THE FINANCIAL CONDITION OF THE SOCIAL SECURITY PROGRAM AND THE RECOMMENDATIONS OF THE NATIONAL COMMISSION ON SOCIAL SECURITY REFORM. I CAN SUMMARIZE WHAT THIS ADMINISTRATION BELIEVES ABOUT THE BIPARTISAN PROPOSAL FOR RESOLVING THE CRISIS WE FACE IN THE SOCIAL SECURITY SYSTEM; IT IS SIMPLY THIS:

> WHAT THE COMMISSION HAS PROPOSED MAY WELL NOT BE THE BEST OF ALL WORLDS FOR ALL OF THE POINTS OF VIEW THAT HAVE FOCUSED ON THIS CRISIS - <u>BUT</u> - AND THIS IS A <u>BIG BUT</u> - THE COMMISSION'S PROPOSAL IS CLEARLY THE BEST POSSIBLE SOLUTION THAT WE CAN EXPECT, GIVEN THE REAL WORLD WE FIND OURSELVES IN.

THERE IS NO NEED FOR ME TO REVIEW WITH THIS COMMITTEE THE URGENCY OF THE SITUATION OR THE IMPORTANCE WE ATTACH TO THE RESTORATION OF THE FISCAL INTEGRITY OF AND PUBLIC CONFIDENCE IN THE SOCIAL SECURITY SYSTEM. AFTER 2 YEARS OF INTENSE DEBATE,

THERE IS NOW MUCH BETTER PUBLIC UNDERSTANDING OF BOTH THE NATURE OF THE SOCIAL SECURITY PROGRAM AS A PAY-AS-YOU-GO SYSTEM AND OF THE FUNDAMENTAL ISSUE OF SOCIAL SECURITY BENEFIT EXPENDITURES EXCEEDING SOCIAL SECURITY REVENUES. WE BELIEVE THAT THIS CONGRESS HAS A ONCE-IN-A-~~DECADE~~ GENERATION OPPORTUNITY TO DO WHAT THE PEOPLE OF THIS NATION DEMAND WE DO ON BEHALF OF THEIR SOCIAL SECURITY SYSTEM, AND THAT IS:

-- TO RESOLVE THE FINANCING QUESTION; AND

-- TO GET SOCIAL SECURITY OUT OF POLITICS AND OUT OF THE HEADLINES - AND BACK INTO THE CONFIDENCE OF THE AMERICAN PEOPLE.

I THINK IT'S FAIR TO SAY THAT THE AMERICAN PEOPLE ARE NOW CONVINCED THAT THE ADMINISTRATION WAS CORRECT IN WARNING OF THE EXHAUSTION OF THE OASI TRUST FUND (WHICH OCCURRED NOVEMBER 5, 1982) AND AGREE WITH THE NEED FOR GETTING ON WITH THE JOB OF RESTORING FINANCIAL SOUNDNESS. MORE THAN THAT, OF COURSE, THE

PEOPLE ARE CONCERNED--EVEN FEARFUL--ABOUT THE FINANCIAL SOUNDNESS OF SOCIAL SECURITY AND IMPATIENT AND FRUSTRATED OVER THE INACTION, INDECISION, AND PARTISAN POSTURING THAT THEY HAVE SEEN UP TO NOW.

THE BIPARTISAN AGREEMENT REACHED BY THE NATIONAL COMMISSION ON SOCIAL SECURITY REFORM GIVES US THE OPPORTUNITY TO DEMONSTRATE TO THE PEOPLE WHOM WE ARE ELECTED AND APPOINTED TO SERVE THAT THE ADMINISTRATION AND THE CONGRESS CAN WORK TOGETHER TO DEAL EFFECTIVELY AND FAIRLY WITH THIS MOST CRITICAL ISSUE. I DON'T THINK IT IS POSSIBLE TO OVERSTATE THE VALUE OF THE WORK OF THE COMMISSION IN REACHING AGREEMENT ON THE KIND OF LEGISLATION THAT IS NEEDED NOW TO RESTORE AND MAINTAIN THE VIABILITY OF OUR SOCIAL SECURITY SYSTEM. DR. GREENSPAN, THE DISTINGUISHED MEMBERS OF THIS COMMITTEE, AND THE OTHERS WHO SERVED ON THE COMMISSION DESERVE BOTH OUR CONGRATULATIONS AND OUR GRATITUDE FOR THEIR EXTREMELY VALUABLE WORK.

ONE OF THE SIGNAL ACHIEVEMENTS OF THE COMMISSION IS THE <u>REAFFIRMATION OF SOCIAL SECURITY'S FUNDAMENTAL ROLE IN PROVIDING A</u>

FOUNDATION OF BASIC INCOME AFTER RETIREMENT, DISABILITY, OR DEATH. IT IS A TRIBUTE TO THE ENDURING VITALITY OF THE PRINCIPLES OF SOCIAL SECURITY THAT NATIONAL LEADERS OF BUSINESS, INDUSTRY, LABOR AND THE CONGRESS REPRESENTING A WIDE SPECTRUM OF VIEWPOINTS COULD ALL AGREE ON THE FUNDAMENTAL SOUNDNESS OF THE SOCIAL SECURITY APPROACH. IT IS A MAJOR STEP TOWARD RESTORING PUBLIC CONFIDENCE IN SOCIAL SECURITY. THIS ADMINISTRATION WHOLEHEARTEDLY CONCURS WITH THIS MOST BASIC CONCLUSION OF THE NATIONAL COMMISSION.

ANOTHER FUNDAMENTAL ACHIEVEMENT OF THE COMMISSION WAS DEFINING THE EXTENT OF THE SOCIAL SECURITY FINANCING PROBLEM. THE COMMISSION REACHED BIPARTISAN AGREEMENT ON THE NEED FOR \$150-TO-\$200 BILLION IN ADDITIONAL REVENUES AND/OR REDUCED EXPENDITURES IN THE SHORT RANGE AND ON THE EXISTENCE OF A LONG-RANGE GAP BETWEEN REVENUES AND EXPENDITURES OF SOME 1.8 PERCENT OF TAXABLE PAYROLL. WHILE THESE NUMBERS ARE, OF COURSE, SENSITIVE TO CHANGES IN THE ECONOMY AND TO LONG-RANGE

ECONOMIC AND DEMOGRAPHIC ASSUMPTIONS, THEY UNDERSCORE THE SERIOUSNESS OF THE SITUATION WE FACE.

THE COMMISSION NOT ONLY CONFIRMED THE UNDENIABLE REALITY OF THE SOCIAL SECURITY FINANCING PROBLEM BUT ALSO SHOWED THAT AT LAST THERE IS A CONSENSUS THAT THE TIME HAS COME TO DEAL WITH THIS PROBLEM. THEY ALSO SET AN EXAMPLE FOR US ALL IN SHOWING THAT, IN THE INTEREST OF THE BROADER OBJECTIVES OF RESTORING THE SOUNDNESS OF THE SYSTEM, WE MAY EACH HAVE TO ACCEPT SOME MEASURES THAT WE ARE LESS THAN ENTHUSIASTIC ABOUT. MR. CHAIRMAN, AS YOU AND THE OTHER MEMBERS OF THE COMMITTEE WHO SERVED ON THE COMMISSION KNOW BETTER THAN I, THE COMMISSION'S BI-PARTISAN FINANCING SOLUTION IS A CAREFULLY BALANCED COMPROMISE, EVERY PIECE OF WHICH WAS CRITICAL TO ACHIEVING AGREEMENT. THE ADMINISTRATION RECOGNIZES THIS, AND THAT IS WHY WE HAVE ENDORSED THE PACKAGE DESPITE THE FACT THAT IT CONTAINS PROVISIONS WE COULD NOT HAVE SUPPORTED INDIVIDUALLY. THE REALITY OF THE SITUATION IS THAT SOMETHING MUST BE DONE, AND IT

HAS BECOME CLEAR THAT WE ALL MUST BE REALISTIC IN COMPROMISING ON A SOLUTION.

MR. CHAIRMAN, BOTH THE PROBLEMS WE FACE AND THE SOLUTIONS WE ARE CONSIDERING ARE THE RESULT OF FORCES THAT HAVE BEEN AT WORK FOR 10 YEARS NOW--10 YEARS OF NEARLY CONTINUOUS CRISIS IN SOCIAL SECURITY FINANCING, AND 10 YEARS OF RISING PUBLIC DOUBTS ABOUT THE SOUNDNESS OF SOCIAL SECURITY. TO PUT OUR CURRENT SITUATION AND THE COMMISSION'S RECOMMENDATIONS IN PERSPECTIVE, LET ME REVIEW FOR THE RECORD THE RECENT HISTORY OF SOCIAL SECURITY FINANCING.

HISTORY OF RECENT FINANCING

IN 1970, THE OASDI TRUST FUNDS HAD MORE THAN 12 MONTHS' WORTH OF BENEFITS ON HAND, AND FINANCING PROJECTIONS SHOWED CONTINUALLY FAVORABLE FINANCIAL CONDITIONS FOR SOCIAL SECURITY.

BY 1973, HOWEVER, THE BOARD OF TRUSTEES OF THE OASDI TRUST FUNDS BEGAN TO PROJECT BOTH SHORT-TERM AND LONG-TERM FINANCING PROBLEMS. THE PROJECTED SITUATION WORSENED ANNUALLY THEREAFTER AS DEVELOPING EXPERIENCE PROVED MORE ADVERSE THAN EXPECTED AND THE

LONG-RANGE ASSUMPTIONS WERE REVISED. BY 1977, THE TRUSTEES REPORTED A CRISIS IN THE SHORT RANGE AND A LONG-RANGE GAP BETWEEN EXPENDITURES AND REVENUES OF NEARLY INCREDIBLE DIMENSIONS-- 8.2 PERCENT OF TAXABLE PAYROLL.

IN RESPONSE TO THESE REPORTS, THE CONGRESS TOOK COURAGEOUS ACTION IN 1977 BY BOTH REDUCING FUTURE BENEFIT GROWTH AND INCREASING SOCIAL SECURITY TAX REVENUES. THE MOST FAR-REACHING BENEFIT REDUCTIONS IN THE 1977 AMENDMENTS CORRECTED A MAJOR FLAW IN THE AUTOMATIC BENEFIT ADJUSTMENT FORMULA AND REDUCED SOME OF THE UNINTENDED INCREASE IN REPLACEMENT RATES WHICH TOOK PLACE IN THE 1970'S. THESE CHANGES REDUCED THE BENEFIT FOR A PERSON WITH AVERAGE EARNINGS RETIRING AT 65 IN 1983 BY UP TO 25 PERCENT COMPARED TO WHAT IT WOULD HAVE BEEN HAD THE FLAWED FORMULA REMAINED IN EFFECT. THE 1977 AMENDMENTS ALSO INCREASED SOCIAL SECURITY TAXES BY OVER $400 BILLION BETWEEN 1979 AND 1990, DUE PRIMARILY TO SIX INCREASES IN THE COMBINED OASDHI TAX RATE.

It is important to bear in mind that rather optimistic intermediate economic assumptions were used to project the results of the 1977 amendments. Those projections showed adequate funds to meet benefit payments in the cash benefits programs until sometime beyond the year 2025. But those economic assumptions did not occur. Beginning with 1979, economic performance has been substantially worse than even the pessimistic assumptions made in 1977. Thus, by 1980 Social Security was once again facing a financing crisis.

This time the Congress responded, in October 1980, with a temporary measure: a reallocation of revenues from the DI program to the OASI program for calendar years 1980 and 1981. However, the Social Security financing crisis worsened, and further action became necessary sooner than expected.

In an effort to obtain more time to consider effective short- and long-term solutions to the system's financing difficulties, the Congress in 1981 authorized interfund borrowing among the

OASI, DI AND HI TRUST FUNDS, WITH ANY SUCH LOANS REPAYABLE WITH INTEREST. BORROWING WAS AUTHORIZED ONLY IN AMOUNTS SUFFICIENT TO ENSURE THAT BENEFITS COULD BE PAID THROUGH THE JUNE 3, 1983 CHECK.

THE INTERFUND BORROWING AUTHORITY HAS BEEN USED THREE TIMES:

-- \$581 MILLION WAS BORROWED BY THE OASI TRUST FUND FROM THE DI TRUST FUND ON NOVEMBER 5, 1982;

-- \$3.4 BILLION WAS BORROWED BY THE OASI TRUST FUND FROM THE HI TRUST FUND ON DECEMBER 7; AND

-- \$13.5 BILLION WAS BORROWED BY THE OASI TRUST FUND FROM THE DI TRUST FUND (\$4.5 BILLION) AND HI TRUST FUND (\$9.0 BILLION) ON DECEMBER 31, 1982.

SINCE THE BORROWING AUTHORITY HAS EXPIRED, <u>THE OASI PROGRAM WILL, IN THE ABSENCE OF FURTHER LEGISLATION, BE UNABLE TO PAY RETIREMENT AND SURVIVOR'S BENEFITS ON TIME BEGINNING IN JULY 1983</u>.

MR. CHAIRMAN, IN REVIEWING THE HISTORY OF THE LAST 10 YEARS IN SOCIAL SECURITY FINANCING, WHAT STANDS OUT CLEARLY IS THE SENSITIVITY OF SOCIAL SECURITY TO ECONOMIC FACTORS, AND THE NEED

TO BETTER GUARANTEE THE SOUNDNESS OF THE PROGRAM IN THE EVENT THAT DEVELOPING EXPERIENCE IS LESS FAVORABLE THAN ALL THE EXPERTS' BEST GUESSES AT THE TIME THE CONGRESS ACTS.

CAUSES OF CURRENT FINANCING PROBLEMS

RECENT HISTORY HAS ALSO VIVIDLY ILLUSTRATED THE BASIC CAUSES OF THE CURRENT SHORT- AND LONG-RANGE FINANCING PROBLEMS FACED BY THE SOCIAL SECURITY PROGRAM. THESE ARE:

-- HAVING BENEFIT EXPENDITURES DETERMINED BY INFLATION RATES WHILE REVENUES ARE DETERMINED BY WAGE GROWTH AND EMPLOYMENT LEVELS; AND

-- LONG-RANGE DEMOGRAPHIC SHIFTS WHICH AFFECT THE RATIO OF WORKING PEOPLE TO BENEFICIARIES.

IN RECENT YEARS, COST-OF-LIVING INCREASES AS MEASURED BY THE CONSUMER PRICE INDEX HAVE EXCEEDED INCREASES IN AVERAGE WAGE LEVELS. AS A RESULT, ANNUAL COLA'S HAVE CAUSED BENEFIT EXPENDITURES TO INCREASE AT A FASTER RATE EACH YEAR SINCE 1978 THAN THE TAX INCOME ON EARNINGS COVERED BY SOCIAL SECURITY.

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IN ADDITION TO ECONOMIC PERFORMANCE, WHICH AFFECTS BOTH SHORT- AND LONG-RANGE SOCIAL SECURITY FINANCING, DEMOGRAPHIC FACTORS STRONGLY INFLUENCE THE LONG-RANGE FINANCING SITUATION. AS YOU KNOW, IT IS EXPECTED THAT SOME 50 YEARS FROM NOW, THE NATION WILL HAVE A RELATIVELY LARGER OLDER POPULATION AS THE POST-WORLD-WAR-II "BABY BOOM" AGES AND AS THE WORK FORCE CONTINUES TO REFLECT THE LOW FERTILITY RATES SINCE THE 1960'S.

AT CURRENT RETIREMENT AGES AND RETIREMENT RATES, THIS WOULD MEAN THAT THERE WOULD BE A LARGE RETIRED POPULATION BEING SUPPORTED BY A SMALLER RELATIVE NUMBER OF WORKERS THAN AT PRESENT. CONTINUING LOW BIRTH RATES AND INCREASES IN LIFE EXPECTANCY MEAN THAT WHILE THE TOTAL POPULATION GROWS BY ABOUT 40 PERCENT OVER THE NEXT 50 YEARS, THE POPULATION AGED 65 AND OLDER WILL INCREASE BY ABOUT 150 PERCENT. GROWTH IN THE VERY OLDEST PORTION OF THE POPULATION WILL BE GREATER STILL--IT IS ESTIMATED THAT THE NUMBER OF PEOPLE 85 AND OLDER WILL TRIPLE. THUS, NOT ONLY WILL THERE BE MORE RETIREES COLLECTING BENEFITS IN THE NEXT CENTURY, THEY WILL BE COLLECTING THEM FOR LONGER PERIODS THAN EVER BEFORE.

SCOPE OF PROBLEM

AS THE NATIONAL COMMISSION ON SOCIAL SECURITY REFORM HAS SHOWN IN ITS WORK, MR. CHAIRMAN, ANY EFFORT TO RESTORE THE FINANCIAL SOUNDNESS OF SOCIAL SECURITY MUST BEGIN WITH AGREEMENT ON THE SCOPE OF THE FINANCING PROBLEMS. I WILL FIRST LOOK AT THE SHORT-RANGE FINANCING NEED, WHICH IS, OF COURSE, THE MOST PRESSING CONCERN TODAY.

IN ADDRESSING THE SHORT-RANGE SITUATION, IT IS IMPORTANT TO CONSIDER NOT ONLY MEETING THE IMMEDIATE BENEFIT OBLIGATIONS BUT ALSO PROVIDING FOR A MEASURE OF PUBLIC CONFIDENCE BY MAINTAINING SOME OPERATING AND CONTINGENCY RESERVE LEVELS IN THE TRUST FUNDS.

TWO PRIMARY FACTORS DETERMINE THE AMOUNT OF ADDITIONAL FINANCING NEEDED BY THE SYSTEM IN THE SHORT RUN: THE APPROPRIATE RESERVE RATIOS TO BE MAINTAINED BY THE SYSTEM AND THE ECONOMIC ASSUMPTIONS USED. THE QUESTION OF THE APPROPRIATE RESERVE RATIOS TO BE MAINTAINED BY THE SYSTEM IS, TO SOME DEGREE, A MATTER OF JUDGMENT. FIFTEEN PERCENT SHOULD BE THE LOWEST ANNUAL RESERVE

LEVEL FOR THE OASDI TRUST FUNDS. IN VIEW OF RECENT EXPERIENCE, EVEN THE 15-PERCENT LEVEL COULD INVOLVE SOME RISK. BUILDING UP TO A 25- TO 30-PERCENT LEVEL OVER THE NEXT FEW YEARS WOULD BE MORE PRUDENT.

THE 8-9 PERCENT THAT NOW IS THE ABSOLUTE MINIMUM RESERVE RATIO NEEDED TO PAY EACH MONTH'S BENEFITS ON TIME COULD BE REDUCED BY AUTHORIZING THE SECRETARY OF THE TREASURY TO ADJUST THE MANNER IN WHICH TAXES ARE CREDITED TO THE TRUST FUNDS. UNDER SUCH PROCEDURES, TREASURY WOULD BE AUTHORIZED TO ESTIMATE AMOUNTS TO BE COLLECTED IN A GIVEN MONTH AND TRANSFER SUCH SUMS TO THE TRUST FUNDS ON THE FIRST OR SECOND DAY OF THE MONTH. THIS TECHNICAL PROCEDURE WOULD SMOOTH OUT THE INCOME AND OUTGO IN THE OASDI TRUST FUNDS AND ALLEVIATE THE POTENTIAL FOR CASH FLOW PROBLEMS.

CHOOSING WHICH ECONOMIC ASSUMPTIONS TO USE TO DETERMINE THE SYSTEM'S SHORT-RANGE FINANCING NEEDS IS MUCH MORE DIFFICULT AND FRAUGHT WITH UNCERTAINTY THAN CHOOSING A RESERVE RATIO TARGET. ALTHOUGH WE ARE HOPEFUL THAT ECONOMIC PERFORMANCE IMPROVES IN THE COMING MONTHS AND YEARS, PROJECTIONS ASSUMING RAPID IMPROVEMENT

SHOULD NOT, AS A PRACTICAL MATTER, INFLUENCE DECISIONS REGARDING THE SOCIAL SECURITY PROGRAM. WE HAVE BEEN STUNG TOO OFTEN BY THE USE OF ESTIMATES THAT LATER PROVED TOO OPTIMISTIC. WE CANNOT BASE THE FINANCING OF SOCIAL SECURITY ON HOPES (OR EVEN ON REASONABLY FAVORABLE EXPECTATIONS). IF OUR EXPECTATIONS FOR IMPROVED ECONOMIC PERFORMANCE ARE REALIZED, WHATEVER MEASURES WE HAVE TAKEN WILL RESULT IN AN EVEN STRONGER SOCIAL SECURITY SYSTEM.

BASED PRIMARILY ON THE 1982 TRUSTEES ALTERNATIVE III ASSUMPTIONS, THE NATIONAL COMMISSION REPORT ESTIMATED THE 1983-89 DEFICIT TO BE BETWEEN $150 AND $200 BILLION. THE BIPARTISAN REPORT RECOMMENDED CHANGES INITIALLY ESTIMATED BY THE COMMISSION TO PRODUCE $168 BILLION IN SAVINGS AND INCREASED REVENUES OVER THE PERIOD. OUR ACTUARIES HAVE REFINED THESE ESTIMATES AND HAVE DETERMINED THAT THE BIPARTISAN AGREEMENT WILL YIELD $165 BILLION UNDER THE 1983 ALTERNATIVE II-B ASSUMPTIONS. THE DEFICIT FOR THE 1983-89 PERIOD UNDER THE 1983 TRUSTEES REPORT II-B ASSUMPTIONS IS $117 BILLION.

ALL ESTIMATES HAVE NOT BEEN COMPLETED ON THE MORE PESSIMISTIC ALTERNATIVE III ASSUMPTIONS FOR 1983, BUT I BELIEVE IT IS SAFE TO SAY THAT ENACTMENT OF THE BIPARTISAN AGREEMENT WILL GENERATE SAVINGS SUFFICIENT TO ACCOMMODATE ECONOMIC ASSUMPTIONS SOMEWHERE BETWEEN II-B AND III OF THE 1983 TRUSTEES REPORT. ADOPTION OF THE TAX TRANSFER PROCEDURE DESCRIBED A MOMENT AGO COULD, AS I MENTIONED, ALLEVIATE POTENTIAL CASH FLOW PROBLEMS.

THE QUESTION OF HOW CLOSE AN ACTUARIAL BALANCE SHOULD BE MAINTAINED IN THE SOCIAL SECURITY PROGRAM OVER THE 75-YEAR VALUATION PERIOD IS ONE THAT HAS RECEIVED CONSIDERABLE ATTENTION OVER THE PAST FEW YEARS. I SHOULD EMPHASIZE, PARTICULARLY IN LIGHT OF RECENT ECONOMIC EXPERIENCE, THAT ESTIMATES MADE FOR A DYNAMIC SYSTEM WITH AUTOMATIC COST-OF-LIVING FEATURES OVER A PERIOD OF AS LONG AS 75 YEARS MUST NECESSARILY BE CONSIDERED RATHER TENTATIVE PROJECTIONS INSTEAD OF PRECISE PREDICTIONS.

WE BELIEVE THAT THE CONGRESS SHOULD TAKE INTO ACCOUNT THE GREAT EROSION IN PUBLIC CONFIDENCE IN THE FINANCIAL CONDITION OF

THE SOCIAL SECURITY PROGRAM THAT HAS OCCURRED IN RECENT YEARS. IT MAY WELL BE ADVISABLE AT THIS TIME TO STRIVE FOR SOMETHING CLOSE TO A 75-YEAR ACTUARIAL BALANCE.

SOLUTION RECOMMENDED BY NATIONAL COMMISSION

THE BI-PARTISAN SOLUTION TO THE SOCIAL SECURITY FINANCING PROBLEM RECOMMENDED BY THE NATIONAL COMMISSION AND ACCEPTED BY THE PRESIDENT AND LEADERS OF BOTH THE SENATE AND HOUSE PROVIDES THE COMPROMISE THAT IS NEEDED FOR QUICK ACTION. AS PRESIDENT REAGAN NOTED IN HIS JANUARY 15 STATEMENT, THE NATIONAL COMMISSION PLAN "INCLUDES ELEMENTS WHICH EACH OF US COULD NOT SUPPORT IF THEY WERE NOT PART OF A BI-PARTISAN COMPROMISE."

I AM SURE THAT NONE OF US LIKES EVERY PROPOSAL IN THE NATIONAL COMMISSION PACKAGE; NONE OF US WOULD SUPPORT EVERY ONE ON AN INDIVIDUAL BASIS. THE DIFFICULTY IS THAT THERE IS NO SOLUTION TO THE PROBLEM THAT EVERYONE WOULD LIKE. THE PACKAGE DEVELOPED AFTER INTENSE NEGOTIATION BY THE NATIONAL COMMISSION REPRESENTS A

CAREFULLY BALANCED EFFORT TO ACHIEVE A SOLUTION THAT CAN BE ACCEPTED BY THE AMERICAN PEOPLE AS A FAIR METHOD OF PUTTING SOCIAL SECURITY ON A SOUND FINANCIAL BASIS.

THE COMMISSION'S PACKAGE ADEQUATELY ADDRESSES THE SHORT-RANGE PROBLEM AND GOES A LONG WAY TOWARD ERASING THE LONG-RANGE PROBLEM. THE OVERWHELMING NEED TO REINSTILL CONFIDENCE IN SOCIAL SECURITY'S ABILITY TO MEET ITS COMMITMENTS TO FUTURE GENERATIONS OF RETIREES MAKES IT IMPERATIVE THAT WE COMPLETE THE WORK OF ELIMINATING THE PROJECTED LONG-RUN DEFICIT. THE NATIONAL COMMISSION SUGGESTED TWO MEANS OF ACCOMPLISHING THIS:

- -- BEGINNING IN 2003, GRADUALLY RAISE THE CURRENT AGE OF 65 FOR FULL RETIREMENT BENEFITS TO 66 BEGINNING IN 2014 ~~2015~~; OR
- -- BEGINNING IN 2010, INCREASE THE OASDI TAX RATE ON EMPLOYEES AND EMPLOYERS EACH BY 0.46 PERCENT.

A MAJORITY OF THE COMMISSION RECOMMENDED THE FIRST APPROACH, GRADUALLY RAISING THE CURRENT AGE OF RETIREMENT.

THERE ARE IMPORTANT CONSIDERATIONS REGARDING EACH OF THESE SUGGESTIONS. RAISING THE RETIREMENT AGE HAS BEEN DISCUSSED FOR ALMOST A DECADE AS A WAY OF OFFSETTING THE PROJECTED GROWTH IN THE RATIO OF RETIREES TO WORKERS. AFTER THE TURN OF THE CENTURY, RAISING THE RETIREMENT AGE COULD BE JUSTIFIED, IN PART, BY THE FACT THAT PEOPLE TEND TO LIVE LONGER TODAY THAN WHEN 65 WAS SELECTED AS THE RETIREMENT AGE IN 1935 AND LIFE EXPECTANCY IS EXPECTED TO INCREASE FURTHER IN THE FUTURE. THUS, EVEN IF THE RETIREMENT AGE WERE INCREASED 1 YEAR 30 YEARS FROM NOW, THE AVERAGE RETIREE COULD STILL EXPECT TO HAVE MORE LEISURE YEARS THAN EARLIER GENERATIONS.

THE ONLY ADVANTAGE OF INCREASING SOCIAL SECURITY TAXES IN 2010 TO ERASE THE LONG-TERM SHORTFALL IS THAT IT WOULD MAKE UNNECESSARY ANY MODIFICATION OF BENEFIT AMOUNTS OR ELIGIBILITY. IT WOULD, HOWEVER, FURTHER BURDEN TODAY'S YOUNG WORKERS AND FUTURE GENERATIONS OF WORKERS FOR WHOM SOCIAL SECURITY WILL NOT BE THE BONANZA IT IS FOR TODAY'S RETIREES.

NEED TO RESTORE FINANCIAL STABILITY

MR. CHAIRMAN, I BELIEVE WE ALL AGREE THAT THERE IS NO MORE TIME FOR RHETORIC OR DELAY. FEAR ON THE PART OF BOTH RETIREES AND YOUNGER PEOPLE THAT SOCIAL SECURITY IS TOTTERING ON THE BRINK OF COLLAPSE HAS BEEN ALLOWED TO CONTINUE TOO LONG. THERE HAS BEEN TOO MUCH FRUSTRATION OVER THE INACTION AND DISAGREEMENT THAT HAS PREVAILED EVER SINCE THE ADMINISTRATION POINTED OUT THE EXTENT OF THE FINANCING PROBLEM IN 1981. NOW, HOWEVER, THERE IS A NEW SENSE OF URGENCY, A NEW AGREEMENT ON THE NEED TO ACT AND A NEW READINESS TO DO SO.

WE PLEDGE TO YOU OUR COOPERATION AS WORK PROGRESSES ON BOTH THE COMMISSION'S BIPARTISAN FINANCING PACKAGE AND THE BEST WAY TO ERASE THE REMAINING LONG-TERM DEFICIT. THE INTERESTS OF 36 MILLION BENEFICIARIES AND 116 MILLION TAXPAYERS CANNOT BE ALLOWED TO FALL VICTIM TO NARROW VIEWPOINTS NOW WHEN WE ARE SO CLOSE TO RESTORING SOCIAL SECURITY'S ABILITY TO MEET ITS COMMITMENTS TODAY AND FOR THE FUTURE.

I WILL BE HAPPY TO ANSWER ANY QUESTIONS.

The CHAIRMAN. I want to thank you for your assistance to members of the Commission and your patience in dealing with members of the Commission for a period of over 1 year. I believe, as you have indicated, that this is certainly not the package that any one of us would have proposed, but it is a compromise. Recently, I find more and more support for the compromise. We will hear as many as 60 witnesses next week who may have different views, but I doubt that any of them have different plans. It's easy to come up and say I don't agree with this, but difficult to develop a better plan. When we see a better plan, then obviously we will take a look at it. But I haven't yet seen such a substitute plan. I keep hearing that there will be one. I hear there is a lot of support building up out there for something, but, again, I haven't had an opportunity to know what that might be.

Obviously, one group is very concerned and has a great deal of political influence—your Federal employees. Some Federal workers seem to believe that being covered by social security is all bad, as if it would involve a new tax with no benefits down the road.

Would you elaborate on the ways that social security coverage may actually improve the protection employees have? For example, disability protection and others. I really believe that we are seeing a lot of well-intentioned Federal employees justifiably concerned because of misinformation or a lack of understanding. First of all, there are some current employees that believe they will be affected and don't understand that it only applies to new hires. Anything that you could furnish for the record or state at this time would be very helpful.

Mr. SVAHN. Well, I have to say, Mr. Chairman, that I have heard a lot of that misinformation. Most of it seems to be coming over the media in the form of advertisements in the morning and in the evening. It is misinformation. I think that it is unfortunate that it is being discussed in the way that it is. It seems to me that there are some people who have, basically, a scare campaign going on for Federal employees.

In the first place, Mr. Chairman, you are absolutely correct that the bipartisan compromise proposal deals only with new Federal employees. As you know, Mr. Chairman, there was discussion about whether it should be all Federal employees, whether it should be Federal employees who do not have a vested Federal pension, and the decision was made in the compromise to make it only new Federal employees. So that's the only group that we are talking about.

A second thing that I think is being said to Federal employees which is incorrect is that they are going to be hurt by being covered by social security. I just don't think that's the case. Now the outcome of the legislative process will be that the Federal pension system that is enacted for new Federal employees will be one which takes into consideration the fact that these Federal employees will also be covered by social security. And I don't see any loss to Federal employees by being covered by social security.

Assuming that in putting together the legislative language we take into consideration the fact that certain Federal employees currently receive a windfall in many instances because of social security—that would, in fact, be eliminated and they would receive, basically, what they had paid for from social security.

In terms of protection and coverage, the social security system for these new Federal employees would actually provide them with better coverage early in their careers as Federal employees than does the civil service retirement system, in terms of disability protection through the disability insurance program. So, from that standpoint, until an employee had been in the Federal Government for a long period of time, the protection that he would receive from disability insurance under social security actually would exceed the protection he now gets under the civil service retirement system.

I think it's unfortunate, and it's another instance of where we are seeing the social security system portrayed in a manner in which it shouldn't be. I hope through hearings such as this and through discussions in the Federal community we can allay the fears of a lot of Federal employees. I really think it is unfortunate.

The CHAIRMAN. Well, obviously, they will be heard. We certainly want to address any just concerns that they have. They have indicated that covering Federal workers would not only worsen the condition of the civil service retirement system, but also eventually worsen the condition of the social security system. That's the big charge. You are going to make both systems sick where you only have one sick now.

Could you respond to that charge?

Mr. SVAHN. Well, Mr. Chairman, I have heard from a lot of Federal employees myself. I have got 87,000 of them working for me right now. It seems that there is this belief that the Federal civil service retirement system right now is a well-funded operation without any unfunded liability, and, in fact, has this huge surplus in its trust fund right now; it is just waiting for every Federal employee to retire.

I tell my employees that that is just not the case. I'm not an expert on the civil service retirement system. I understand that there is a substantial unfunded liability. It is backed by the Government of the United States, of course, and presumably would be met at such time as it comes due. But there is a very substantial unfunded liability in the civil service retirement system now.

The second point is whether or not this is going to cost the social security system money or hasten the social security system's financial problems. In fact, as the chairman knows, in estimating what the coverage of new Federal employees would do and including nonprofit employees, the Commission estimated that the short-term savings would be approximately $20 billion for 1984 through 1989. Over the long-term, there is about 0.3 percent of payroll of the long-term social security deficit that is eliminated by the inclusion of Federal and nonprofit employees.

The CHAIRMAN. As I understand, if we are going to have the 6-month COLA delay we should have this bill passed, what, by early May? Is that the absolute deadline?

Mr. SVAHN. Well, our absolute deadline for delaying the COLA is May 7, Mr. Chairman.

The CHAIRMAN. Why do you pick that date? What makes that absolute?

Mr. SVAHN. Well, that backs off from July 3. Under present law, the COLA, the cost-of-living adjustment, is paid in the July 3 check, which is the June benefit. If you back off from July 3, the Post Office needs to get the checks from the Treasury 3 days before the delivery date. Just keep walking back from there the amount of time that is required to print the checks and the amount of time that is required to make up the tape with the check amounts. It all works back and May 7 is the last date. If it is delayed past that we either will have to delay the check that normally goes out on July 3, or we would go ahead and pay the COLA and then try to recoup that amount at some later time. So May 7 is the last date.

The CHAIRMAN. Senator Long.

Senator LONG. How important does the Administration feel it is to completely eliminate the long range deficit? What are the administration's recommendations for accomplishing that goal?

Mr. SVAHN. Well, Senator, the administration is very much in favor of eliminating the long-term deficit and putting the system back into actuarial balance or somewhere near actuarial balance. I think that as Senator Heinz and Congressman Pepper were indicating earlier, the Commission's bipartisan agreement recommends doing that and provides two options as ways to put the system back, basically, into actuarial balance.

I think, Senator, none of what is to be done is going to be extremely popular. I think that if we are engaged in doing something unpopular that we ought to go ahead and take care of the entire problem. Now we have not taken a position as to whether or not we would favor one over the other of the Commission's recommendations. One, of course, relies on increasing taxes out in the future. The other relies on a gradual long-range raising of the retirement age by 1 year.

I think the administration will be working with the Congress to work out some sort of an agreement. The bipartisan package that has been agreed to by the majority of the National Commission is a balance of both of those. It's a balance of raising taxes and reducing benefits. I think that that makes for a pretty good position for compromise in the long term.

But we do endorse putting the system back in actuarial balance.

Senator LONG. The proposal to tax benefits accounts for half of the long range savings of the Commission package. The Commission said that we are proposing to tax only "higher income persons." But the income threshold to which it would tax benefits—$20,000 for individuals and $25,000 for couples—remains the same on into the future. As time goes by, more and more middle-income and eventually lower-income people with income other than social security will be taxed. Does the administration believe it appropriate eventually to tax most beneficiaries with other income?

Mr. SVAHN. Well, Senator, the administration supports this bipartisan package. The bipartisan package has in it one piece, as you said, that taxes social security benefits for person with incomes of $20,000 for single persons, and $25,000 for couples.

I was not privy to the meetings of the Commission when they decided that first, they were going to include taxation of benefits, and second, how they picked $20,000 and $25,000. I think it is probably a number that was just picked and they said, OK, that sounds pretty good, and everybody agreed on it.

I do know that the members of the Commission in discussing that matter discussed whether or not to index the $20,000 and $25,000 or to raise it at any given interval other than by statute or by individual legislative action. The members of the Commission decided not to do that. The savings that result from that package from taxing benefits—0.6 percent of payroll—are predicated on those numbers remaining the same. Now as to whether or not we would support changing the numbers or indexing them, our position is that we support that package. That package includes $20,000 and $25,000, and it's a fixed number.

Senator LONG. The Commission report indicates that the Commission favored coverage of State and local employees under social security, but did not recommend it because of a majority of the Commission thought that it would not be constitutional to mandate such coverage. Yet the Commission did recommend mandatory coverage for those State and local governments which previously opted for voluntary coverage. Has the administration asked the Justice Department's advice on whether it would be constitutional to impose mandatory coverage on some but not all State and local governments?

Mr. SVAHN. I know of no such request to the Justice Department, Senator. We at Social Security have looked at that issue on a number of occasions both with regard to State and locals and nonprofits as to whether or not you can constitutionally require those entities to pay social security taxes. I have to honestly say, while not being a constitutional lawyer myself, that there are arguments on both sides. There are some who would argue that you could include State and local employees, make mandatory universal coverage. There are others who argue, of course, that you can't under the Constitution.

I guess we have ways of determining that in our judicial system. I am sure that should the Congress decide to require coverage or should the package pass which prevents withdrawal, I am sure there will be a constitutional challenge and we will just have to wait for the courts to decide how it comes out.

Senator LONG. It seems to me, Mr. Svahn, that this is not going to be something that is any great joy for Senators to vote for. What we are doing here, generally speaking, in some respects raises taxes, and in some respects it trims benefits. So when we are voting for this, there is no real joy in it, but at least we can go back and tell our constituents that we voted to make the program sound, and we voted to finance it over a long period of time. If we do what I think we ought to do, we should meet the long-term problem as well as the short-term problem. But it would seem to me that while we are at it, we ought to be sufficiently conservative in our estimates and see what it takes in order to achieve those results. We don't want to have to come back here in 2 or 3 years and do the same thing all over again. I don't know of anything that would undermine our credibility and yours more than for us to have to keep going back to the public and say, well, you know we put that big tax on, and then we put another big tax on, and we did this, that, and the other thing—and we regret to say that we were still too optimistic, we have got to do something again.

I just think that if that is the kind of thing that we do, we will encourage people to think that when their time comes, the young people paying the tax, that there won't be anything there.

In 1977 I was one who refused to go along with the general revenue approach. I took the view that I would support the 1977 bill and fight for it and raise the money to pay for it. The only reason that this program is running short, as far as I am concerned, is that they gave us a bad estimate. They should have taken into account the fact that you might have a recession. They should have been sufficiently conservative in those estimates that this program would have been solvent even in spite of that.

I would hope that when this bill gets to the Senate, if it needs to be amended that we will amend it to see that we are not going to have to come back and do this again 5 years later. I hope that you and your people would help us to bring about that kind of protection, or at least not stand in the way if the Congress has the guts to go ahead and vote to do what it takes to make this program solvent for the people.

It's hard to make a reliable estimate 75 years off. But we ought to be able to be sufficiently conservative in what we are doing so that the estimate would stand up for at least 20 years. I would hope that you share my view that we ought to do at least that much, so that we shouldn't have to be back here in 5 years or even 10, the way it is now, having to pass another bill to increase taxes and trim benefits.

Mr. SVAHN. Well, Senator, I fully agree with you in virtually everything that you have just said. I think that we have tried over the past 2 years, and I think the Commission in its deliberations tried to look at fairly pessimistic economic scenarios in order to come up with a reasonable financing package. You are correct, it is increasing taxes, and cuttng benefits. There are only two options in this system.

Just last week I wrote to the Senator and to the chairman, under our intermediate assumptions for our 1983 trustees' report we estimate the short-term deficit between now and 1989 to be approximately $117 billion. The package that the National Commission has recommended we costed out under those same economic assumptions as being just about $165 billion. As I said in that letter, I feel fairly confident that the revenues and reduced expenditures that are in the National Commission's Bipartisan Agreement will provide sufficient funding for economic circumstances somewhere between what we consider the intermediate and the pessimistic economic assumptions of this year's trustees' report, not last year's.

So while the margin is fairly thin, there is a margin there. We think that it will be enough to get us through 1990 when we anticipate beginning to build fairly substantial surpluses in the trust funds.

The CHAIRMAN. Senator Pryor.

Senator LONG. I have one more comment.

The CHAIRMAN. Oh, excuse me.

Senator LONG. What is the name of that gentlemen on your left there?

Mr. SVAHN. Paul Simmons.

Senator LONG. Well, I think Mr. Simmons took on a tough job the other night in defending the cutback in the disability insurance program. I think that you did a courageous and worthy job in trying to explain what the Congress had in mind, what we thought about the reduction in disability. I think that your people ought to point out when they discuss this on television again, that when they bring out those horror cases of somebody who appears to be totally disabled and perhaps should never have been taken off those rolls, we have plenty of horror cases on our side, too, literally hundreds of thousands of cases of people who never did have any basis for being on those rolls. It looks like we have about three times as many people on those rolls as we planned to put on when we passed that disability program. When the program is administered in such a way that we wind up with three times as many people on the roll as we thought we were voting to put on there, including literally hundreds of them where when you look at and can't see anything wrong with them, and when you take them off the rolls, they proceed to go back and join the labor force that shows there are a lot of horror stories on our side too. There are a tremendous number of people who have convinced themselves they are disabled because they had difficulty getting a job somewhere, and they wind up on those disability rolls. But that's not what that program is for.

Mr. SIMMONS. As you know, Senator, that is our top program priority. In terms of operating all of our programs we are trying to get this program to the point that the only kinds of horror stories would be cases where the person is on the benefit rolls erroneously and not cases where people are being taken off the rolls wrongly. We think we have correct procedures in place and, with the help of the 1982 amendments, we are going to make some progress on that.

Senator LONG. The Department, I think, is doing a job today working with the States in trying to make fathers support their children. They are raising a lot of money now. They are raising well over $1 billion—but for years they told us nothing could be done, yet they are raising about $1½ billion a year now. In my State just this last year they increased their collections by about 38 percent. My thought is that they could probably raise twice that if they keep working at it, so we wouldn't have to be taxing the taxpayers to support children when a father is able to support those children and just doesn't want to do so, when he wants to duck out on his responsibility.

If we just administer all the programs the way that they were intended when we passed them, then some of these tax increases wouldn't be necessary. I think you understand that as well as I do. You have got some well-intentioned people who want to do something for their neighbors and their friends, and often times it is really not necessary, where people could handle their situation on their own if they were required to do so. We really intend that where they can, they do it.

I'm not talking about social security retirement benefits. I am talking about some of the other parts of the program.

Mr. SVAHN. Fine, I understand. I can appreciate that, Senator. Having been with the Federal Government once before in 1974 and

1975 when title IV D was passed and having had the opportunity to start that program, I think the Senator is absolutely correct. It has come an awful long way, and we are collecting a substantial amount of child support that is owed. There is much more out there to be done so I would agree with the Senator wholeheartedly.

Senator LONG. But if you have been responsible for the child support program, I think that you understand some of what has to be done if we are going to make these programs work. I'm sorry that it's not fun. I imagine sometimes you might be taking your life in your hands to go out there and track some fellow down. But if you are going to be fair to the taxpayer, he is entitled to expect us to make fathers support their families.

Mr. SVAHN. Yes, sir.

Senator LONG. Thank you.

The CHAIRMAN. Mr. Pryor.

Senator PRYOR. Thank you, Mr. Chairman.

The Commission has recommended, Mr. Svahn, a reallocation of the tax rate between the old age and survivors fund and disability fund. Senator Long made reference to that. That it be changed. I wonder how those changes are going to affect the disability fund, which is now in, let's say, pretty healthy financial shape.

Mr. SVAHN. Well, perhaps, Senator, I should let Mr. Ballantyne answer that question. Mr. Ballantyne is the Chief Actuary of the Social Security Administration. In general I would say that our best estimates are that the change should not endanger the financial viability of the disability insurance trust fund. The trust fund ratio should remain above minimal levels. With that I will turn the mike over to Harry.

Mr. BALLANTYNE. Senator Pryor, in answer to the question, the National Commission proposed that the reallocation be done in such a way that, I believe, both the trust funds would have about the same ratio of assets to outgo. That is, the assets of the funds at the beginning of each year as a percentage ~~of out-go~~ during the year would be about the same for both OASI and DI.

The reallocation could be done this way or it could be done so that a little bit more is left in the disability fund to make it a little stronger because it's a more volatile program than the OASI program, as we have seen from the increase in the disability incidence rates during the 1970's, and more recently some drop in those incidence rates.

Senator PRYOR. How many individuals have been taken off social security disability payments, let's say, in the last 12 months?

Mr. SVAHN. In what period of time, Senator?

Senator PRYOR. In the last 12 months.

Mr. SVAHN. About 200,000 initial CDI terminations in calendar year 1982—that is, before any appeals—for the title II program.

Senator PRYOR. Do you feel that the system itself—and I certainly don't want to take issue with Senator Long. I did not see the television show that Senator Long had referred to. But do you feel that that system is an equitable system? Is it fair?

Mr. SVAHN. Well, no. I said all along, Senator, that when I first came into social security I looked at the disability insurance program, and it was a program that denied about 70 percent of the beneficiaries on the front end; a program that had somewhere be-

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tween 25 and 30 percent of the people who were on the disability roll not meeting the statutory criteria for disability, and yet at the appellate level we had about a 58-percent reversal rate. And I knew then that there were some problems with that program.

I think we worked very closely with the chairman and with Senator Long and other members of this committee, in the Senate and in the House last year, to try and smooth out the disability adjudicative process with the disability amendments of 1982.

We still have a ways to go, but I think that we are moving in the right direction. As Mr. Simmons said to Senator Long, it's my goal, anyway, to make the disability insurance adjudicative process a stable and objective process. It has been subject to tremendous amounts of subjectivity in the past. And there have been a lot of mistakes made in that program. But it's our goal to administer the program the way the Congress enacted the law. And that's where we are going.

Senator PRYOR. Do you have a quota of a number of people who should be taken off?

Mr. SVAHN. Absolutely not.

Senator PRYOR. If you don't have a quota, then how do you factor in some sort of a long range projection as to how many will or will not go on social security disability?

Mr. SVAHN. You are talking about estimates? How do we estimate how many?

Senator PRYOR. What are you estimating that the number of individuals to be cut off—you have got to have some figure in order to make the projections that we have just been given.

Mr. SVAHN. The original estimate was made by the GAO. We don't have any quotas. I know there is a lot of talk going around saying that so many people should be taken off or something like that. No, we don't have any quotas. We make estimates. And I think our estimate for last year was about 145,000. But those are just estimates.

Senator PRYOR. Well, back on a more general type of question—let's say if we lessen the tax or the infusion of revenues into the disability fund, will not that increase the possibility of taking even more individuals off of disability?

Now I agree with Senator Long that there are a lot of people drawing disability who should not. But would not this bring pressure on the system with fewer dollars to take more people off of disability?

Mr. SVAHN. No, I don't believe it will, Senator. Again, our estimates are that even with the reallocation—which by the way was also done in 1980 for 1980 and 1981—that the disability insurance program will remain fully funded. There is no connection between the financial status of the disability insurance trust fund, and the adjudicative process of determining whether or not a person is disabled. There is no connection between those two. So, no, it shouldn't have any impact at all.

Senator PRYOR. I think, Mr. Chairman, those are all the questions I have.

The CHAIRMAN. Thank you. Senator Bradley.

Senator BRADLEY. Commissioner, in the Washington Post about a week ago there was a new bureaucratic term coined that I hadn't heard before. And it is called "normalized tax transfers." It deals with the transfer of money from the general fund to the social security system each month. So my question is, Does this transfer apply just to the tax on benefits or does it apply to the existing payroll tax?

Mr. SVAHN. Well, Senator, one morning last week I came upon the same term myself. What it relates to is in the statute at the present time—the statute requires the Managing Trustee to make estimates and to transfer from time to time to the trust funds the taxes that are collected for social security. And while we would all like to think that Government is highly efficient, and is able to know on a daily basis or a weekly basis or a monthly basis how much money was collected, and where that money goes, we just don't have that. So what happens now is that the Treasury Department estimates, usually daily, how much social security tax they might have collected around the country, and then transfers that amount of money from the Treasury general fund into the social security trust fund. Under our benefit payment schedule we have a regular payment on the 3d of the month. On the 3d of the month, about 34 percent of all social security payments are cashed because they are direct deposits. They go right into a bank, and they are immediately credited to someone else's account. A couple of days later, Treasury says, "Well, beneficiaries must have cashed the checks they received by mail on the 3d and they transfer on the 5th, on the 7th more or a little later if the 3d is on a weekend, money out of the trust funds"?

It's all done on estimates right now. The National Commission's Bipartisan Agreement has a slight cash flow dip in it, if you will—we drop down to a reserve ratio of about 13 percent in 1985 under 1983 alternative II-B assumptions. The total amount of money that is saved by this package is sufficient to accomdate economic assumptions somewhere between our alternative II-B intermediate assumptions, and our alternative III assumptions. So the total amount of money is sufficient but because of the way it comes in, we find that in 1985 the trust fund reserves drop to where there is very little margin for error.

And what we proposed was rather than the Treasury estimating every day how much money they collect for social security tax, that they estimate each month how much money they will collect for social security tax during that month, and deposit that to the credit of social security at the start of the month when the demand is there for the checks to be cashed.

Now we didn't propose that it be mandated that this be done every month. We wanted the flexibility that's in the statute today for the Managing Trustee to make estimates and to transfer the money from time to time. But we wanted the Congress to know that we thought there was a way to make sure that in any given month we have at least that 8½ percent in the trust fund that is necessary to cover the checks for that month.

Senator BRADLEY. Thank you for the explanation. Is there any worry here that this could become a subterfuge for general fund borrowing and an infusion of the general fund into the trust fund?

Mr. SVAHN. Well, I guess there is always the worry.

Senator BRADLEY. Can you be sure that it hasn't happened to this point?

Mr. SVAHN. No. I can't be certain that it hasn't happened to this point. In fact, if I looked at the management over the years of the social security trust funds versus the general fund, if anything, there has been a reverse cash management. In other words, prior Secretaries of the Treasury, on back to the start of social security, have always managed the general fund and the trust funds to the general fund's advantage. What this does perhaps is manage the trust funds to the trust funds' advantage, protecting them against cash flow problems. But I really don't see any threat of being able to slide in great amounts of general revenue dollars through this process. And I don't really anticipate that it would be used very much, if at all.

But the point, I guess, is that it does provide a considerable amount of protection to have it there.

Senator BRADLEY. Thank you, Commissioner.

Mr. Chairman, I am done.

The CHAIRMAN. Senator Long.

Senator LONG. I want to touch for just a moment if I could on the disability matter.

We probably should have started out with some kind of employment program where we put enough incentive in there for employers to put handicapped people to work so that, hopefully, we would try to provide a job opportunity for all those people who might be available for employment. That, I think, should be a part of what we are trying to do. We ought to first try to look after the handicapped to put them in employment, and then try to look at the totally disabled.

I was here when we passed that disability program. It only passed by one vote in the U.S. Senate, so that if I had voted against it it wouldn't have passed. The same is true of every other Senator who voted for it.

Senator Walter George made the concluding speech, and he provided the information on how many people were expected to be put on the rolls, the kind of people we had in mind, and what that was going to cost. Now since that time, we have had this type of situation: you can go to my home town of Baton Rouge and talk to the average young mother who finally can afford to hire some help to look after her children while she does some other work. They advertise that they are willing to pay the going market rate. People show up interested in that job and generally speaking they are willing to take the job and do the work with one big condition—they want to be paid in cash with no records kept. Now that's a problem for people who want to obey the law, such as a mother seeking to find someone to help her look after her children or look after her home or do some other kind of work of a relatively unskilled nature.

I have had an experience recently I want to tell you about. I would rather not identify the person; I don't want to embarrass the person. A fellow came to talk to me, and I discussed his problem with him. He went down to apply to the Social Security Administration for his retirement benefits. They told him that they didn't have the earnings records that he thought they should have, so they couldn't justify the kind of retirement benefit that he was confident he was entitled to. Then someone down there in the Department said, "Well, maybe we can put you on the rolls as disabled." They proceeded to put that man on the roll as disabled. It wasn't his idea that he was disabled. It was their idea that he was disabled, because they couldn't find the records to give him what he thought he was entitled to as a retirement benefit.

There are all kinds of people who come to me talking about being disabled even though I can't see anything the matter with them. Nevertheless, I take their word for it that they have arthritis and there is no telling what they might have and might not have, and then I find out later on that their neighbors don't think there is anything the matter with them. With those people out playing golf and fishing everyday and having a good time while their friends work for a living or their neighbors work for a living, it is hard to justify having to put people on the disability rolls when their neighbors don't think there is anything the matter with them.

Are some of you familiar with that aspect of this problem?

Mr. SVAHN. Definitely, Senator. I would just say that in light of the one individual you are talking about, we need the same records, plus more records to put them on disability insurance than to put them on retirement benefits. But I'm willing to just venture a guess that I know what may have happened in that instance.

The individual you are talking about was probably between the ages of 62 and 65. And up until the present time—we are now changing our forms—we had what we called a leading question on the form. We would ask the person who came in to retire whether or not they felt all right. And if they said, no, they were kind of tired and they had a problem then we would work that up to see if they were eligible for disability insurance.

And once people find out that if you become entitled to disability insurance benefits at age 62 you get 100 percent of the benefits you would get if you retired at age 65, but if you just retire at age 62 you only get 80 percent of your age 65 benefit amount, you would be surprised how many people feel they have become disabled at that time. Now we are changing that.

But I understand what it is that you are referring to entirely.

Senator LONG. I think you ought to point out that it wasn't President Reagan that started tightening up on this disability. It was started back under President Carter's administration, a Democratic administration. I would say he would tend to qualify as a liberal Democrat. With Jimmy Carter's administration they came down here recommending to us that we pass legislation requiring that the States and the Federal Government tighten up on the disability program because there were hordes of people on those rolls that didn't belong there.

When we are talking about raising social security taxes, if some of these things weren't costing a great deal more than they were supposed to be costing, we wouldn't have to raise the taxes, would we?

Mr. SVAHN. That's true.

Senator LONG. Some of us who in all good conscience have tried to be good to people and help people with their problems feel that to some extent we have been victimized when doctors certify hosts of people who are not disabled as being disabled. When we have large numbers of people going out and seeking jobs. which they are not supposed to be physically able to hold and keeping it a secret that they are on the disability rolls, some of us have a right to feel like we have been victimized. We were persuaded to vote for a program and then we have to try to defend it.

I see people on television from time to time who refer to themselves as being disabled where I can't see anything the matter with those people. I'm not talking about a horror case that you might have seen on an educational TV program, but just other people who are up there on some other cause. You want to ask the question: Disabled? Why is that person disabled? I can't see anything the matter with that person.

The fact is that when we voted for the program we felt we were voting for a tight program, with very severe limitations on who could be on the program. It has disappointed a lot of people to go down there to apply and then find out they couldn't get on the rolls. I can understand their reaction, it is human nature to be disappointed in that kind of situation, but these people who have a handicap were never intended to be on the disability program. We didn't think we could afford having them all on the rolls, and still don't think we can afford it. That's part of our problem.

Every one of you has known some of the people I am talking about, sweet little people who love their fellow man, but take the view that if you can just get a program started, don't worry that it is only going to cost $100 million the first year. The cost will grow. And after a while, we will have that up to about $2 billion or $3 billion a year, and at that point we will be taking care of most of the people that we wanted to take care of in the first place.

You have known some of those people in that department in years gone by. And I don't want to identify them, but you and I know what has happened. I can see by the smile on your face that you know it just as well as I do. And that's the reason those social security taxes have to be raised.

While we are talking about wanting to help people—and I am willing to vote for these taxes here; if that is what it takes. I am willing to do it—but I do think that we ought to try to tighten up on the program, especially where it is running out of balance.

Thank you very much, gentlemen.

The CHAIRMAN. Thank you, Senator Long. Mr. Svahn, have you had a chance to review S. 1? I think you helped to put some of the language together, is that right?

Mr. SVAHN. Yes, sir.

The CHAIRMAN. The Commission recommended that windfalls be eliminated for people who receive social security plus other Government pensions and suggested two possible ways to accomplish this. I understand that there may be some administrative problems with one of the options. I also understand that you feel that the one that is in S. 1 can be implemented. Is that correct?

Mr. SVAHN. Well, yes, Mr. Chairman. The two options that were presented by the National Commission both present certain problems. The one that takes into account noncovered earnings presents some serious administrative problems for the Social Security

Administration in that we would wind up having to set up an entirely new system to maintain detailed records on a worker's noncovered earnings in a manner comparable to the current covered earnings operation—a massive new project. Also, the benefit computation would be extremely complex. Of the two options, however, it is probably the more appropriate approach from a conceptual standpoint.

The other option, the one that is contained in S. 1, would modify the benefit formula by just making the second percentage factor in the benefit formula—32 percent—apply to the lowest band of average indexed monthly earnings—instead of the first factor, which is 90 percent. It would be the simplist one for us to administer.

There would be some problems in terms of enforcement—that is, making sure that the person was, in fact, covered by a Government pension plan or retirement system in some of the smaller Government entities—water districts, things like that. We would have to establish at the time the person got ready to retire that they were, in fact, eligible for the Government retirement program and that sort of thing. But it will be much easier for us to administer than would the other option.

The CHAIRMAN. What about the COLA stabilizer? Is that going to be difficult to implement?

Mr. SVAHN. Well, that presents us with an awful lot of administrative problems, but because it wouldn't take effect until 1988, we could start planning for those problems right now. It could be taken into account in our systems modernization plan.

If there were a catchup it would require us to keep track of those affected by the stabilizer when it went into effect, and then keep track of those records until such time as the trust fund reserves would reach the 32-percent level. We would then pay the catchup. A catchup is administratively complex, but because of the leadtime that we would have, we could probably do it.

The CHAIRMAN. Next Tuesday, Wednesday, and Thursday we will be having hearings throughout the day and throughout the evening, if necessary, to wind up the witnesses so that we can go to markup shortly thereafter. The one area that we want to be certain that we address—and I think Senator Long and others have commented on it—is that we don't make the same mistake again that was made in 1977. It was not the fault of this committee, but of the assumptions that were given. We are looking to restore confidence in the system for both the young and old. If, in fact, we pass legislation that develops a problem in the next 2 or 3 years then I don't think the American people would believe Congress or the administration or your agency for a long, long time.

I hope that in our effort to pass a compromise we are going to be realistic enough to face up to any problem that may develop. I'm certain that is your attitude.

Mr. SVAHN. It certainly is, Senator. And I would indicate that you will have the full cooperation of the Social Security Administration, our Office of the Actuary, and that we will accurately, without any change in assumptions or anything else, cost out anything that the chairman would like.

The CHAIRMAN. Some of us feel strongly that we should extend the retirement age. In S. 1, it would begin in the year 2000, increasing the age by 1 month a year to age 66 in the year 2012. That doesn't seem to be a very sharp difference in present law, but I know Congressman Pepper and others object to that strenuously. It seems to me it would have more credibility if it were coming from a younger member of Congress. [Laughter.]

To me, he is the best witness we have for extending the retirement age. I can't think of a better person to have testify that we ought to extend the retirement age than Claude Pepper. The fact that he appears makes our case for us. [Laughter.]

I have the highest regard for Senator Pepper. I just don't think he is correct in this one area. But he has made a great contribution. Without his assistance, we probably wouldn't be here today.

It's my understanding, as one of the five Commission member working group, that we submitted the long-term difference to Congress, and however it comes out, that's it. No one is going to have a veto. I have a strong feeling, just listening to members of this committee, that we have a lot of support for extending the retirement age to age 66, and then indexing it to longevity, as we provide in S. 1. That may not be the prevailing view on the House side. Though again, I think we have had members—Democrats and Republicans—make some very good points on why we should make some extension. We are talking about 25 years or more in the future so we are not going to interfere with anyone's retirement plans. It won't be an abrupt departure from the present system and I think it also helps restore some confidence in the system. There have been a number of young people in the audience in the last couple of days. I'm not certain whether they ever believe they will have an opportunity to receive social security benefits, but if we would extend the retirement age then that is one way that we might restore some of that confidence.

I was asked by Senator Armstrong, who had to leave, to ask if this testimony reflects your views or views of others.

Mr. SVAHN. Well, it's my testimony, Mr. Chairman.

The CHAIRMAN. I don't say he doubted that, but has anybody else had any input into it. Did anybody read your testimony and make changes?

Mr. SVAHN. Well, obviously, all testimony that is presented as official testimony is the administration's testimony. There is a very involved process and I'm not even sure of the mechanics for getting testimony cleared. You get comments from various people. It's written, rewritten. I did not personally write all of my words in that testimony. But then I have to say, Mr. Chairman, I rarely ever do write all the words in the testimony. So it reflects the administration's position.

The CHAIRMAN. But you are confident, yourself, of all the statements made? You back up everything in the statement?

Mr. SVAHN. Yes, sir.

The CHAIRMAN. I also want to concur with Senator Long. There are now about 4 million DI beneficiaries. The disability program is costing about $19 billion a year so it is a substantial program. We believe that last year we worked out a very fair compromise that would address the concerns of many members of this committee and many nonmembers of the committee.

Anything else that you would like to state at this time?

Mr. SVAHN. No; nothing, Mr. Chairman.

The CHAIRMAN. When do you change hats?

Mr. SVAHN. Well, I'm not too sure. I don't think the nomination has come up yet, but it should come up shortly. Then I will welcome the opportunity to appear before the committee again.

The CHAIRMAN. Right. Well, as soon as that nomination comes up, we will be scheduling your confirmation hearings. But in the meantime, we will be looking to your colleagues on your right and left for their figures and estimates of your systems capabilities on this measure before us. I would also hope that you can help us keep the social security compromise from being cluttered up with other programs or amendments. Perhaps you could make that point on the House side as well as this side. No doubt about it. It's a very attractive target for a lot of amendments because it has the endorsement of the President, the Speaker, the majority leader. It's must legislation. It must be passed by May. It seems to me that if people insist on offering amendments, we might not want to bring this up until about the deadline.

Mr. SVAHN. I will work very diligently on the other side, Mr. Chairman.

The CHAIRMAN. I would like to present it before Easter, but if we are going to be faced with 30, 40, or 50 amendments maybe we will have to rethink our strategy. Sometimes when there is a deadline, a lot of things are not quite as important as they might otherwise be. The lameduck session is the most recent example.

We would appreciate your help in that area. I'm not suggesting that every amendment that is being considered now is not meritorious. But, it is my hope that we would just take care of social security and then move onto the rest of the business in other legislation. Thank you very much.

Mr. SVAHN. Thank you.

[Whereupon, at 12:31 p.m., the hearing was concluded.]

[The letters to Senator Dole from Commissioner Svahn follow:]

THE COMMISSIONER OF SOCIAL SECURITY
BALTIMORE, MARYLAND 21235

February 19, 1983

The Honorable Robert Dole
Chairman
Finance Committee
United States Senate
Washington, D.C 20510

Dear Mr. Chairman:

As requested, attached are the long range estimates of the Old Age, Survivors and Disability Insurance (OASDI) and Hospital Insurance (HI) trust funds under Alternative II-B assumptions which will be used in the 1983 Trustees report. Also enclosed are short-range estimates of the OASDI and HI Trust Fund operations under both the Bi-Partisan agreement of the National Commission on Social Security reform and that agreement plus selected additional proposals under the 1983 Alternative II-B assumptions requested by the Ways and Means Committee.

Some general points on these estimates:

1. You will note on Table 1 (change in estimated OASDI Long-range Cost Rate, and Reason for Change) that the estimates in the 1983 Trustees Reports differ somewhat from the 1982 reports. Specifically, the OASDI deficit is now projected to be -2.09 per cent of payroll, up from the -1.82 per cent projected by the Trustees a year ago. The primary reasons for this change include:

   A. A change in the assumed ultimate fertility rate from 2.1 to 2.0 children per woman;

   B. A change in the assumed long-term unemployment rate from 5.0 to 5.5 per cent; and,

   C. The introduction of a wholly new assumed element in the 1983 estimates -- the effect of potential withdrawals of state, local and voluntary organization employees from the system -- which by itself adds .13 per cent of payroll to the estimated deficit.

2. Assuming the state/local/voluntary withdrawal problem is eliminated as proposed by the National Commission on Social Security Reform, the comparable bottom-line OASDI deficit in the 1983 Trustees Reports will be -1.96 per cent of taxable payroll, or only -.14 more than the deficit estimated in the 1982 reports, an increase of 7.7 per cent.

3. You will note on Table 3 (Preliminary Estimated Long-Range OASDI Cost Effect of the National Commission Bipartisan Agreement) that the Office of the Actuary estimates that enactment of those proposals agreed to by 12 members of the Commission will yield +1.41 per cent of taxable payroll rather than the +1.22 per cent estimated by the Commission at the time the agreement was reached. This increase results primarily from the use of the new Alternative II-B assumptions to be used in the 1983 reports and from the fact that the 1983 reports will project the status of the system one additional year, to 2060.

4. In comparing Table 1 and Table 3, note that the remaining long-term deficit which the Commission proposed be addressed by the Congress is now estimated to be -.68 per cent of payroll, or -.10 more than originally estimated by the Commission.

We will continue to work on other estimates requested by you and your staff and will forward them shortly.

Sincerely,

John A. Svahn
Commissioner

Enclosure

Table 1

Change in Estimated OASDI Long-Range Cost Rate,
and Reason for Change
Alternative II-B

	OASI	DI	Total
1982 Report:			
Actuarial Balance	-2.48	+ .66	-1.82
Average tax rate	10.11	2.16	12.27
Average cost rate	12.59	1.50	14.09
Change in cost rate:			
1982 benefit increase of 7.4%	- .00	- .00	- .00
1982 Legislation	- .01	- .00	- .01
Valuation date	+ .06	+ .00	+ .07
Demographic Assumptions 1/	+ .15	+ .01	+ .16
Economic Assumptions 2/	+ .08	+ .02	+ .10
Disability Assumptions	- .00	- .20	- .20
Opting Out Assumptions	+ .12	+ .01	+ .13
All other factors	+ .04	.00	+ .04
Total all changes	+ .45	- .16	+ .29
1983 Report:			
Average cost rate	13.04	1.34	14.38
Average tax rate	10.13	2.17	12.29
Actuarial Balance	-2.91	+ .83	-2.09

1/ Includes effect of change in the assumed ultimate fertility rate from 2.1 to 2.0 children per woman.

2/ Includes effect of change in the assumed ultimate unemployment rate from 5.0 to 5.5 percent.

NOTE: Prior to the 1983 Trustees Report no recognition was given in the long-range cost estimates to the possibility that some of the covered nonprofit employees and some of the covered State and local government employees could opt out of the OASDI system. The new procedures that are being used to prepare for the 1983 Report recognize this possibility and result in an estimate that this change in methods will increase the long-range deficit by about 0.13 percent of taxable payroll. If the above cost projection had been prepared on the basis of the same procedures that were being used before 1983, the long-range deficit would have been shown as 1.96 percent of taxable payroll. This increase in the estimated cost rate of 0.13 percent of taxable payroll would be fully offset by additional savings in the National Commission on Social Security reform proposals related to the coverage of nonprofit employees and State and local government employees.

Social Security Administration
Office of the Actuary
February 18, 1983

Table 2

Tax Rate and Estimated Cost Rate of the
OASDI System Under Alternative II-B,
Calendar Years 1983-2060

YEAR	COST AS PERCENT OF TAXABLE PAYROLL: OASI	DI	OASDI	OASDI TAX RATE	SURPLUS OR DEFICIT
1983	10.94	1.28	12.22	10.80	-1.42
1984	10.80	1.19	11.98	10.80	-1.18
1985	10.83	1.14	11.96	11.40	-.56
1986	10.93	1.11	12.04	11.40	-.64
1987	10.95	1.09	12.04	11.40	-.64
1988	10.97	1.07	12.05	11.40	-.65
1989	10.97	1.06	12.04	11.40	-.64
1990	11.00	1.06	12.06	12.40	.34
1991	10.96	1.06	12.02	12.40	.38
1992	10.91	1.07	11.98	12.40	.42
1993	10.73	1.06	11.78	12.40	.62
1994	10.58	1.05	11.64	12.40	.76
1995	10.47	1.05	11.52	12.40	.88
1996	10.34	1.04	11.38	12.40	1.02
1997	10.18	1.04	11.22	12.40	1.18
1998	10.05	1.06	11.10	12.40	1.30
1999	9.92	1.08	11.00	12.40	1.40
2000	9.82	1.10	10.92	12.40	1.48
2001	9.76	1.13	10.89	12.40	1.51
2002	9.69	1.16	10.85	12.40	1.55
2003	9.64	1.19	10.84	12.40	1.56
2004	9.62	1.22	10.84	12.40	1.56
2005	9.62	1.26	10.87	12.40	1.53
2006	9.65	1.29	10.94	12.40	1.46
2007	9.71	1.32	11.03	12.40	1.37
2010	10.08	1.40	11.48	12.40	.92
2015	11.28	1.49	12.76	12.40	-.36
2020	12.86	1.52	14.38	12.40	-1.98
2025	14.46	1.48	15.94	12.40	-3.54
2030	15.51	1.41	16.93	12.40	-4.53
2035	15.93	1.40	17.33	12.40	-4.93
2040	15.87	1.42	17.29	12.40	-4.89
2045	15.83	1.45	17.29	12.40	-4.89
2050	15.96	1.45	17.41	12.40	-5.01
2055	16.09	1.42	17.51	12.40	-5.11
2060	16.13	1.42	17.55	12.40	-5.15
25-YEAR AVERAGES:					
1983-2007	10.36	1.13	11.49	12.07	.58
2008-2032	12.84	1.46	14.29	12.40	-1.89
2033-2057	15.93	1.43	17.36	12.40	-4.96
75-YEAR AVERAGE:					
1983-2057	13.04	1.34	14.38	12.29	-2.09

Table 3

Preliminary Estimated Long-Range OASDI Cost
Effect of the National Commission Bipartisan Agreement,
Based on 1983 Trustees Report Alternative II-B Assumptions

(in percent of taxable payroll)

	Effect
Present Law:	
Average cost rate	14.38%
Average tax rate	12.29
Actuarial Balance	- 2.09
Proposed Changes:	
Cover new Federal employees	+ .29%
Cover all non-profit employees	+ .10
Prohibit State and local terminations	+ .08
Delay benefit increases 6 months	+ .30
Eliminate "Windfall" benefits	+ .02
Continue benefits on remarriage	- .00
Modify indexing of deferred survivors benefits	- .05
Pay divorced spouses benefits whether or not worker has retired	- .01
Raise disabled widow(er)'s benefits to 71.5 percent of PIA	- .01
Raise delayed retirement credits to 8 percent per year	- .11
Tax one-half of benefits for high income beneficiaries	+ .63
Accelerate tax rate increases	+ .03
Increase tax rate on self-employment income	+ .19
Modify general fund transfers for military service credits	+ .01
Total for above changes	+ 1.41
After above changes 1/:	
Actuarial Balance	- .68%
Average income	12.92
Average cost rate	13.60

1/ The National Commission Bipartisan Agreement was based on the 1982 Trustees Report Alternative II-B assumptions which projected a 1.80 percent deficit. The agreed upon changes shown above were estimated at that time to leave a remaining deficit of 0.58 percent of taxable payroll. There was bipartisan agreement to eliminate this remaining deficit of 0.58.

Social Security Administration
Office of the Actuary
February 18, 1983

THE COMMISSIONER OF SOCIAL SECURITY
BALTIMORE, MARYLAND 21235

February 22, 1983

The Honorable Robert J. Dole
Chairman
Senate Finance Committee
Washington, D.C. 20510

Dear Mr. Chairman:

Enclosed are the remaining short-range estimates based on Alternative III assumptions to be used in the 1983 Trustees Report. The estimates show the OASDI and HI Trust Fund operations under both the Bi-Partisan agreement of the National Commission on Social Security Reform (NCSSR) and that agreement plus selected additional proposals, as requested by the Ways and Means Committee.

As shown by the tables, the OASDI and Trust Funds would be able to pay benefits on time throughout the short-range projection period only if, in addition to the NCSSR proposal, there is authority for normalized tax transfers. However, even with these changes, there is virtually no margin of safety under the pessimistic Alternative III assumptions. Also, the OASI Trust Fund would not be able to repay the $12.4 billion loan that was transferred from the HI Trust Fund in 1982 before the estimated depletion of the HI fund in the latter half of this decade.

Sincerely,

John A. Svahn
Commissioner

Enclosure