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Abstract

Social Security is important to all Americans, but, particularly, to low-income workers and their families. Financing the program partly through earmarked deductions from employees' wages is an integral and vital part of Social Security's design, and has been an important reason for Social Security's success and broad public support over the program's seventy-year life. At the same time, these contributions are harder to bear for those with lower wages. Just as the EITC has eased the burden of these contributions without undermining the basic structure and philosophy of Social Security, so the program's long-range deficit, if eliminated properly, can help strengthen Social Security while remaining sensitive to the burdens of the low-wage worker. If that is done, Social Security will continue, in the words of President Franklin Roosevelt, "to provide sound and adequate protection against the vicissitudes of modern life" for all workers and their families, now and in the future.

Keywords

Social Security, Social insurance, Elderly, Low-Income workers

SOCIAL SECURITY AND THE LOW-INCOME WORKER*

NANCY J. ALTMAN**

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I. THE IMPORTANCE OF SOCIAL SECURITY

Social Security is extremely valuable, not just to low-income workers but to all Americans. The program has transformed the nation.[1] It has eradicated what once was a primary anxiety of the vast

* Some parts of this Article also appear in NANCY J. ALTMAN, THE BATTLE FOR SOCIAL SECURITY: FROM FDR'S VISION TO BUSH'S GAMBLE (2005), recounting the political history of Social Security and asserting that recent attempts at reform are part of a long-standing battle between political ideologies. Throughout this Article, "Social Security" refers to the cash benefits programs, Old Age, Survivors, and Disability Insurance ("OASDI"), not to Medicare.

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1. This transformation was not instantaneous. The program developed slowly because Social Security requires that workers achieve insured status in order to receive benefits. *See* 42 U.S.C. § 402(a) (2000) (extending old-age insurance benefits only to fully insured individuals); SOC. SEC. ADMIN., 1948 ADVISORY COUNCIL REPORT, INTRODUCTION—OLD-AGE AND SURVIVORS INSURANCE (1948), http:/www.ssa.gov/ history/reports/48advise4.html (finding that more than a decade after the beginning of the Social Security program, only one out of five elderly were either

majority of workers, the terror of growing old. A writer in 1912 described the attitude people used to have about aging:

> After the age of sixty has been reached, the transition from non-dependence to dependence is an easy stage—property gone, friends passed away or removed, relatives become few, ambition collapsed, only a few short years left to live, with death a final and welcome end to it all—such conclusions inevitably sweep the wage-earners from the class of hopeful independent citizens into that of the helpless poor.[2]

Before Social Security, people worked as long as they could hold jobs. But this was an insecure state of affairs. The fast pace of many jobs "wears out its workers with great rapidity. The young, the vigorous, the adaptable, the supple of limb, the alert of mind, are in demand . . . . Middle age is old age."[3]

Once older workers lost their jobs, they could seldom find new ones.[4] Older people almost never had sufficient savings to last until death. The difficulty of saving for retirement was described in 1937:

> A man's productive, wage-earning period is rarely more than forty-five years. Under present conditions he must earn enough in this period to contribute toward the support of aged parents, rear and educate children, maintain his family at a standard of living more or less consistent with American ideals, and save enough in the form of insurance or absolutely safe investment to provide a modest income until death, if he survives his working period. This last item of his budget is the one least urgent, least stressed by advertising propaganda and most easily disregarded among the many financial demands.[5]

Those unable to work routinely moved in with their children. Those who had no children or whose children were unable or unwilling to support them typically wound up in the poorhouse. The poorhouse was not some Dickensian invention; it was an all-too-real

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insured or receiving any benefits and that the benefits received were inadequate); *see also infra* note 48; NANCY J. ALTMAN, THE BATTLE FOR SOCIAL SECURITY: FROM FDR'S VISION TO BUSH'S GAMBLE 149-50 (John Wiley & Sons, 2005) [hereinafter, Altman] (describing how means-tested welfare payments were more widespread and larger than Social Security throughout the 1940s).

2. ABRAHAM EPSTEIN, FACING OLD AGE 20-21 (1922) (quoting L.W. SQUIER, OLD AGE DEPENDENCY IN THE UNITED STATES 28-29 (1912)).

3. *Id.* at 4 (quoting E.T. DEVINE, MISERY AND ITS CAUSES 125 (1909)).

4. *See* JOANNA N. LAHEY, CTR. FOR RET. RESEARCH AT BOSTON COLL., HOW DO AGE DISCRIMINATION LAWS AFFECT OLDER WORKERS? 1 (2006), http://www.bc.edu/centers/crr/issues/wob_5.pdf (asserting that in the first half of the last century firms specified age limits in their want ads and hiring policies).

5. COMM. ON ECON. SEC., SOC. SEC. ADMIN., U.S. SOCIAL SECURITY IN AMERICA 138 (1937), http://www.ssa.gov/history/reports/ces/cesbookc7.html.

means of subsistence for the elderly in the world immediately preceding the enactment of Social Security.[6]

When Social Security became law, every state but New Mexico had poorhouses, which were also referred to as almshouses or poor farms.[7] The vast majority of the residents were elderly. Most of the "inmates," as they were often labeled,[8] entered the poorhouse late in life, having been independent wage earners until that point. A Massachusetts commission reporting in 1910 found, for example, that only 1% of the residents had entered the almshouse before the age of forty; 92% entered after age sixty.[9]

Fear of the poorhouse was always lurking in the background, haunting people as they aged.[10] The poorhouse was a fate to be dreaded. Even in as progressive a state as New York, the conditions were abysmal. In 1930, the New York State Commission on Old Age Security found that

> [w]orthy people are thrown together . . . with whatever dregs of society happen to need the institution's shelter at the moment; sick people are thrown together with the well, the blind, the deaf, the crippled, the epileptics; the people of culture and refinement, with the crude and ignorant and feeble-minded . . . . Privacy, even in the most intimate affairs of life, is impossible; married couples are quite generally separated; and all the inmates are regimented as

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6. The proximate cause that ended the system of poorhouses was the program of Grants to States for Old Age Assistance, which was enacted in the same legislation as Social Security. *See* Social Security Act of 1935, Pub. L. No. 74-271, tit. I, 49 Stat. 620, 620 (1935) (granting funds to each state, subject to certain requirements, to provide financial assistance for the elderly poor). Social Security today prevents millions of elderly Americans from falling into poverty. *Infra* notes 22-25 and accompanying text. The program was not the main contributor to ending the poorhouses, though, because it was structured to be slow to develop. *See supra* note 1 (regarding requirement that workers achieve insured status to qualify for benefits, and the resulting slow development of the program).

7. *See* ALTMAN, *supra* note 1, at 7.

8. *See* ABRAHAM EPSTEIN, INSECURITY: A CHALLENGE TO AMERICA 501 (Harrison Smith & Robert Haas eds., 1933).

9. A higher percentage of men wound up in the poorhouse, even though a woman's life expectancy was longer on average than a man's, just as they are today. The reason for this surprising result, according to a 1919 Pennsylvania commission, was that women's traditional work around the house was useful even as they aged. Consequently, the commission discovered, "[c]hildren or relatives will make greater sacrifices in order to keep an old mother at home and prevent her going to a poorhouse, than they would for an aged father or other male relative." EPSTEIN, *supra* note 8, at 501.

10. The poorhouse was a powerful, ubiquitous image in the general culture. The early Monopoly boards, patented in 1904 as the Landlord's Game, contained a square labeled "Poorhouse." According to the rules, players were sent there when they couldn't meet their expenses. Today, in a world with Social Security, that same, exact square reads, "Free Parking." *See* Patrick Taylor, The Game Monopoly, http://www.patricktaylor.com/game-monopoly (last visited Apr. 8, 2007) (detailing the history of Monopoly).

> though in a prison or penal colony. Private possessions, other than the clothes on the back, are almost out of the question, since individual bureaus, closets, tables or other articles of furniture, outside of a bed, are generally not provided.[11]

Poorhouses and destitute senior citizens were a fact of life well before the Great Depression. In 1934, the Committee on Economic Security, the intercabinet group appointed by President Franklin D. Roosevelt to draft a Social Security bill,[12] canvassed the available statistics. No national figures existed, but using available data, the Committee reported, "Connecticut (1932), New York (1929) and Wisconsin (1925) found that nearly 50% of their aged population (65 years of age and over) had less than subsistence income."[13] In contrast, the poverty rate among the elderly in 2005 was 10.1%, about the same as the poverty rate for adults aged eighteen to sixty-four.[14]

The reduction in the poverty rate of the elderly is directly due to Social Security. According to a 2005 report of the Center for Budget and Policy Priorities, a nonprofit, nonpartisan research organization, "Leaving aside Social Security income, nearly one of every two elderly people—46.8%—has income below the poverty line."[15] The percentage is strikingly similar to the poverty rate before the enactment of Social Security.

Today, about one-third of the elderly receive 90% or more of their income from Social Security.[16] Two-thirds receive half or more of

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11. EPSTEIN, *supra* note 8, at 508 (quoting NEW YORK STATE COMM'N ON OLD AGE SEC. REPORT 395-96 (1930)).

12. *See* Exec. Order No. 6757 (June 29, 1934), *available at* http;//www.ssa.gov/history/fdrstmts.html (establishing the Committee on Economic Security, consisting of the Secretary of Labor, the Secretary of the Treasury, the Secretary of Agriculture, the Attorney General, and the Federal Emergency Relief Administrator).

13. COMM. ON ECON. SEC., SOC. SEC. ADMIN., FINAL STAFF REPORT (1935), http://www.ssa.gov/history/reports/ces/ces2armstaff.html.

14. *See* U.S. CENSUS BUREAU, POVERTY: 2005 HIGHLIGHTS (2006), http://www.census.gov/hhes/www/poverty/poverty05/pov05hi.html (listing the overall 2005 poverty rate at 12.6%, the poverty rate for Americans aged eighteen to sixty-four at 11.1%, and the poverty rate for Americans sixty-five or older at 10.1%). Poverty among older Americans falls largely on women. Of the 3,400,000 elderly Americans in poverty, 2,400,000, or 71%, are female. POPULATION RESOURCE CTR., OLDER WOMEN AND POVERTY: A DEMOGRAPHIC PROFILE (2005), http://www.prcdc.org/summaries/AgingSeries05/womenandpoverty.html.

15. ARLOC SHERMAN & ISAAC SHAPIRO, CTR. ON BUDGET AND POLICY PRIORITIES, SOCIAL SECURITY LIFTS 13 MILLION SENIORS ABOVE THE POVERTY LINE: A STATE-BY-STATE ANALYSIS 1 (2005), http://www.cbpp.org/2-24-05socsec-pr.pdf.

16. *See* OFF. OF POL'Y, SOC. SEC. ADMIN., INCOME OF THE AGED CHARTBOOK (2004), http://www.ssa.gov/policy/docs/chartbooks/income_aged/2004/iac04.html (representing that 34% of the aged receive 90% or more of their income from Social Security); *see also* Nancy J. Altman, Facts Every American Should Know, http://thebattleforsocialsecurity.com/facts.php (last visited Apr. 8, 2007) [hereinafter Altman, Facts] (offering statistical support for the notion that Social Security is the nation's most effective anti-poverty program).

their income from Social Security.[17] The benefits are particularly important to women and minorities. Social Security provides 90% or more of the income of almost half of all unmarried (including widowed, divorced, and never-married) women and of all African Americans aged sixty-five or over.[18]

In addition to retirement benefits, Social Security also provides extremely important life insurance and disability insurance protection for workers and their families.[19] In that way, it has also transformed the world with respect to workers who become disabled or who die leaving dependent spouses and children.

As a result of its dependent benefits, Social Security is the nation's largest and most generous children's program. Three million children receive benefits as dependents of workers who have died, become disabled, or retired while an additional 2,000,000 children do not receive benefits as dependents but nevertheless live in families where another member of the household receives Social Security benefits.[20] All together, Social Security supports 5,000,000 American children, between 7% and 8% of all American children.[21] The program is of particular importance to children in low-income families. The 3,000,000 children receiving Social Security dependent benefits live in families whose total income is 25% lower than the average for all American families with children. The benefits are also especially important to African American children. Because African

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17. Altman, Facts, *supra* note 16.

18. *See* SOC. SEC. ADMIN., SOCIAL SECURITY IS IMPORTANT TO WOMEN 1 (2006), http://ssa.gov/pressoffice/factsheets/women-alt.pdf (stating that Social Security provides 90% or more of the income of 46% of elderly unmarried women); NAT'L COMM. TO PRES. SOC. SEC. AND MEDICARE, WHY SOCIAL SECURITY IS IMPORTANT TO AFRICAN AMERICANS (2006), http://www.ncpssm.org/news/archive/vp_africanamericans (asserting that Social Security provides 90% or more of the income of 45% of elderly African Americans).

19. *See* SOC. SEC. ADMIN., DISABILITY BENEFITS 2, 11 (2006), http://www.ssa.gov/pubs/10029.pdf (outlining the general provisions governing Social Security disability benefits and the extension of these benefits to spouses and children).

20. *See* CATHERINE HILL & VIRGINIA RENO, NAT'L ACAD. OF SOC. INS., CHILDREN'S STAKE IN SOCIAL SECURITY 1 (2003), http://www.nasi.org/usr_doc/Social_Security_Brief_No_14.pdf (noting the particular importance of Social Security for children receiving benefits as dependents or living with relatives who receive benefits).

21. In contrast to the 5,000,000 children who benefit from Social Security, around 3,600,000 children get part or all of their family income from the next largest children's program, Temporary Assistance for Needy Families ("TANF"). Under Social Security, children are entitled to benefits every month until they reach age eighteen (or age nineteen, if they are still in high school). Parents caring for children receive monthly benefits until children reach age sixteen. In contrast, families may only receive TANF benefits for a maximum of five years. Social Security provides children an average annual benefit of around $5000. TANF provides no children with benefits in their own right; the average spending per recipient is around $2200. *See id.* (comparing the benefits received by children through Social Security with those received through TANF).

Americans have higher rates of disability and premature death than whites, African American children receive a disproportionate percentage of Social Security's dependent benefits. African American children constitute 15% of all children in the United States under age eighteen, but represent 23% of all children receiving Social Security.[22]

Moreover, Social Security is the nation's largest and most generous disability program. Over 6,000,000 disabled workers receive monthly Social Security benefits. Without that monthly check, 55% of disabled workers and their families would live in poverty.[23] Long-term disability is an uncommon private sector benefit. Seventy-seven percent of the private sector work force is without it.[24]

II. SOCIAL SECURITY'S CONCEPTUAL BASIS

Social Security is frequently described as the nation's most popular domestic program.[25] The popularity is not hard to understand. Studies have shown that most people are risk averse with respect to their economic circumstances.[26] Consistent with these findings, workers dependent on wages historically have sought to protect themselves and their families from the loss of earnings by banding together and pooling their risk. As far back as the Middle Ages in England and Europe, individuals who had a common trade or craft joined together to form mutual aid societies or guilds, which, in addition to regulating the craft, provided a variety of wage-

22. *See id.* at 2 (asserting the particular importance of Social Security to African American children who receive a disproportionate percentage of total Social Security children's benefits).

23. *See* Nancy J. Altman, What Social Security Means to Disabled Americans, http://thebattleforsocialsecurity.com/important/disabled.php (last visited Mar. 25, 2007).

24. *See id.* (stating that only 23% of American workers have long-term disability insurance protection apart from Social Security).

25. *See, e.g.*, Press Release, Office of Sen. Lindsey Graham, Statement from Sen. Lindsey Graham: Introduction of the Soc. Sec. Solvency and Modernization Act (Nov. 18, 2003), http://www.senate.gov/~lgraham/index.cfm?mode=presspage&id=219419 ("Social Security is the most popular government program in American history.").

26. *See* JACOB S. HACKER, THE GREAT RISK SHIFT 26 (2006) (citing a survey estimating people's tolerance for risk, which asked Americans whether they would prefer (a) their current incomes guaranteed for life or (b) a fifty-fifty chance of either doubling their incomes or having their incomes reduced by a third). Though on pure odds, the chance to gain or lose income is the better bet, 65% preferred the guaranteed income. *Id.* In a 2005 survey, which asked respondents whether they were "more concerned with the opportunity to make money in the future, or the stability of knowing that your present sources of income are protected," 62% answered that they were more concerned with stability. *Id.*

replacement benefits to guild members.[27] Similarly, as early as the sixteenth century, workers in the mining districts of central Europe formed customary funds, which provided benefits for sickness and accidents.[28]

Banding together to share risk, exchanging the possibility of a larger loss for a smaller, certain payment, is the essence of insurance. A group of people, all of whom are exposed to the possibility of a particular loss, can protect against the loss by each member contributing an amount of money related to the average likelihood of its occurrence. This eliminates the possibility of a large, unsustainable loss by any member of the group. Each member of the group trades a larger possible loss for a smaller but certain premium payment.

This is the concept behind Social Security.[29] Like other group insurance, Social Security involves making periodic payments and sharing the risk of loss—in the case of Social Security, loss of wages to support oneself and one's dependents in the event of disability, death, or old age. Because the government is setting the rules, it can compel participation, which in turn creates a very broad risk pool and reduces costs to participants.[30] In a "fireside chat" explaining his plan for Social Security, President Franklin D. Roosevelt conceptualized the program as self-help, where Americans were "to use the agencies of government to assist in the establishment of means to provide sound and adequate protection against the vicissitudes of modern life—in other words, social insurance."[31]

Today, some view Social Security as simply a government spending program, undifferentiated from other federal spending, and the

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27. *See* ROBERT M. BALL, SOCIAL SECURITY: TODAY AND TOMORROW 12 (1978) [hereinafter BALL, SOCIAL SECURITY] (discussing the predecessors of modern Social Security, including the Middle Age guild system and the first government sponsored social insurance plans in Europe).

28. *See id.* at 12-13 (listing the organizational origins of modern social insurance programs).

29. *See generally id.* at 288-305 (discussing in great detail the controversy over whether Social Security should be considered a form of insurance and concluding that it is).

30. Because it is a compulsory, universal program, it is extremely cost efficient, returning more than ninety-nine cents of every dollar collected in old age, survivors, and disability benefits. *See* BD. OF TRS. OF THE FED. OLD-AGE AND SURVIVORS INS. & FED. DISABILITY INS. TR. FUNDS, ANNUAL REPORT 2007, at 4-5 (2007), *available at* http://ssa.gov/OACT/TR/TR07/tr07.pdf [hereinafter 2007 ANNUAL REPORT] (detailing the financial accounting of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance trust funds for the year 2007).

31. Franklin D. Roosevelt, Fireside Chat on the Seventy-third Congress (June 28, 1934), http://www.millercenter.virginia.edu/scripps/digitalarchive/speeches/spe_1934_0628_roosevelt.

deductions from wages that support the program as merely a tax.[32] In keeping with President Roosevelt's vision though, the legal structure is one of direct exchange, consistent with the program's distinctive insurance character. The deductions from workers' wages, matched by equal payments by employers, are placed in trust and held for the sole purpose of paying Social Security benefits and expenses.[33] The surplus of income over outgo is, by law, invested in treasury bonds, at fair market interest rates, that are carefully accounted for and fully repaid with interest.[34]

Those employee deductions are commonly referred to as a payroll tax,[35] but that is a misnomer in two respects. First, workers do not have payrolls; only employers do. More importantly, the deductions are better understood as mandatory premiums or contributions, rather than mere taxes. It is instructive to note that the acronym for the Social Security payment is "FICA," which stands for "Federal Insurance Contributions Act," enacted in 1939,[36] well before the days of paid political public relations consultants and spin doctors.

If viewed simply as a federal tax, the employee deductions raise policy questions. Why, for example, should low-income workers who owe not a single penny of federal income tax[37] nevertheless pay 6.2%

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32. *See, e.g.*, CONG. BUDGET OFFICE, SOCIAL SECURITY AND THE FEDERAL BUDGET: THE NECESSITY OF MAINTAINING A COMPREHENSIVE LONG-RANGE PERSPECTIVE 3 (2002), http://www.cbo.gov/ftpdocs/36xx/doc3650/No3August.pdf ("Social Security and Medicare, by their size, are poised to crowd out other government spending and limit the availability of funding for other government functions.").

33. *See* 42 U.S.C. § 401 (2000) (creating trust funds to receive proceeds from wage deductions and invest such proceeds received beyond those needed to pay the required old-age and disability benefits). Some financing also comes from interest on Treasury bonds held by the trust funds and taxation on the benefits of higher income beneficiaries. *See* 2007 ANNUAL REPORT, *supra* note 30, at 4 (listing "interest" as a form of income for the old-age and disability trust funds).

34. *See* 42 U.S.C. § 401(d) (2000) ("Such investments may be made only in interest-bearing obligations of the United States or in obligations guaranteed as to both principal and interest by the United States.").

35. *See, e.g.*, Memorandum from David C. John, Senior Research Fellow, The Heritage Foundation, Raising the Social Security Payroll Tax Cap Does Not Fix Social Security (Feb. 16, 2005), http://www.heritage.org/Research/SocialSecurity/wm667.cfm ("Currently, workers pay Social Security payroll taxes on only the first $90,000 of their annual income.").

36. Social Security Act Amendments of 1939, Pub. L. No. 76-379, § 1432, 53 Stat. 1360, 1387 (1939) ("This subchapter may be cited as the 'Federal Insurance Contributions Act.'").

37. As a result of expansions in the Earned Income Tax Credit in the 1980's and early 1990's and the enactment and expansion of the Child Tax Credit in 1998 and 2000, increasing numbers of low income taxpayers now have zero or negative federal income tax liability. It has been estimated that, for 2006, approximately 43,400,000 federal tax returns had zero or negative liability. *See* Scott A. Hodge, *Number of Americans Paying Zero Federal Income Tax Grows to 43.4 Million: Fiscal Fact No. 54*, TAX FOUND., Mar. 30, 2006, http://www.taxfoundation.org/files/ff54.pdf (describing the typical profile of the 43,400,000 taxpayers who owe no federal income tax and listing

of their wages to Social Security?[38] Moreover, why should the highest paid workers, the 6% of the workforce earning over the maximum taxable wage base, $97,500 in 2007,[39] pay nothing to Social Security with respect to earnings above the base?[40]

However, when Social Security is understood as the insurance program that it is, the policy questions disappear and the financing makes sense. Social Security's benefits relate to earnings on which FICA deductions are made. The employee earning just at the maximum taxable wage base, $97,500 in 2007, and the employee earning ten times that amount each receive the same Social Security benefits. Consequently, it is rational that they purchase these benefits for the same dollar amount, even though the dollar amount translates to a different percentage of earnings, just as they pay for private insurance, food, cars, or any other economic good or service on the basis of cost, not ability to pay.[41]

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the estimated number of non-payers by state). While federal taxes of low-income workers with children have declined over the past quarter century, those of low-income workers without children have not. *See* NAT'L EITC OUTREACH P'SHIP, CTR. ON BUDGET & POLICY PRIORITIES, EITC FACT SHEET 1 (2006), http://www.cbpp.org/eitc-partnership/eitcfactsheet.pdf (providing information on the Earned Income Tax Credit and Child Tax Credit and how each benefits working low-income taxpayers with children); *see also* KEVIN A. HASSETT & ANNE B. MOORE, NAT'L POVERTY CTR., POLICY BRIEF #5: HOW DO TAX POLICIES AFFECT LOW INCOME WORKERS? 1-2 (2005), http://www.npc.umich.edu/publications/policy_briefs/brief5/brief5.pdf (illustrating the decline in total tax liability, since 1979, for a low-income married couple with two children and a low-income single mother with two children in contrast to a childless, low-income adult who has experienced little change in tax liability since 1979).

38. *See* 26 U.S.C. § 3101(a) (2000) (imposing, beginning in 1990, a 6.2% tax on the wages of covered workers for old-age, survivor, and disability insurance); *see also* 26 U.S.C. § 3121(a)(1) (2000) (defining "wages" as "all remuneration for employment," subject to certain exceptions, up to the amount of the maximum taxable wage base. *See infra*, note 40. An additional 1.45% on all covered earnings is paid for hospital insurance. *See* 26 U.S.C. § 3101(b) (2000) (imposing a 1.45% tax on wages for hospital insurance beginning the last day of 1985). Employers pay a matching amount. *See* 26 U.S.C. § 3111(a) (2000) (creating an excise tax on employers linked to the wages paid to an employee and matching the amount of Social Security tax paid by the employee). Self-employed workers pay 12.4% to OASDI and 1.9% to hospital insurance. *See* 26 U.S.C. § 1401(a) (2000) (listing the tax rate imposed for Social Security and hospital insurance on the wages of self-employment income).

39. *See* Cost-of-Living Increase and Other Determinations for 2007, 71 Fed. Reg. 62,636 (Oct. 26, 2006) (announcing the 2007 maximum taxable wage base of $97,500); *see also* SOC. SEC. ADMIN., SOCIAL SECURITY BULLETIN, ANNUAL STATISTICAL SUPPLEMENT tbl.4.B4 (2005), http://www.ssa.gov/policy/docs/statcomps/supplement/2005/4b.html#table4.b4 (showing that 94.5% of all workers had wages under the maximum base for 2003, the most recent available data).

40. *See* 42 U.S.C. § 430(b) (2000) (setting forth the formula for determining the "contribution and benefit base" in any given calendar year).

41. An employee earning $97,500 and an employee earning twice that amount, $195,000, will each pay $6,045 to Social Security in 2007. *Supra* notes 38 and 40. The

Comparing those two employees with the low-income employee, the exchange is progressive, even though the employee deductions, viewed in isolation, are not.[42] All workers pay the same flat-rate contribution. However, lower income workers receive benefits that constitute a higher proportion of wages than the benefits of higher workers.[43]

This outcome results mainly from a progressive benefit formula.[44] A worker's benefit is calculated by indexing and averaging his or her career earnings to determine average indexed monthly earnings ("AIME").[45] The AIME translates into a monthly benefit by plugging it into a benefit formula. The formula for 2007[46] is the sum of:

> (a) 90% of the first $680 of his or her average indexed monthly earnings, plus
>
> (b) 32% of his or her average indexed monthly earnings over $680 and through $4100, plus

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$6,045 equals 6.2% of the salary of the worker earning $97,500, but only 3.1% of the salary of the employee earning $195,000.

42. If only the deduction from wages is considered, without regard to benefits received, the structure is proportional with respect to those earning up to the base amount, regressive with respect to those earning above and below the base. *Supra* note 41.

43. Also, because the formula looks to career earnings, workers who have periods of unemployment receive larger proportionate benefits. *See infra* note 44 and accompanying text.

44. In addition, Social Security benefits are based on covered taxable wages only, not all wages. *Supra* notes 38 and 40; *infra* note 45. Consequently, with every dollar of additional wages a worker earns above the maximum taxable wage base, the percentage of wages replaced by the Social Security benefit declines.

45. The method described in the text is the basic benefit computation method. The special minimum method for low-income workers who have many years of work under covered employment is used if it produces a larger benefit. CONG. BUDGET OFFICE, SOCIAL SECURITY: A PRIMER 13-29 (2001), http://www.cbo.gov/ftpdocs/32xx/doc3213/EntireReport.pdf (describing the special minimum method as based upon number of years worked as opposed to amount of earnings and providing an alternative calculation that benefits those who work for many years but earn little). To calculate the AIME for retirement purposes, a worker's wages (up to the maximum taxable wage base) are indexed to the growth in wages in the overall economy, up through the year in which the worker reaches age sixty. Earnings after that point are used without indexing.

46. *See* Cost-of-Living Increase and Other Determinations for 2007, 71 Fed. Reg. 62,636, 62,640 (Oct. 26, 2006). The percentages in the formula remain constant. However, the dollar amounts of the formula are indexed and change annually. The pertinent formula for an individual is the formula applicable to the year in which he or she reaches age sixty-two, becomes disabled, or dies, whichever occurs first. *See* 42 U.S.C. § 415(a) (2000). The benefit generated by the formula is the benefit received at Normal Retirement Age; adjustments are made for benefits received before or after that age.

(c) 15% of his or her average indexed monthly earnings over $4100.[47]

The formula achieves progressivity in much the same way as the federal income tax. The formula brackets wages and replaces a larger percentage of earnings with respect to the lower brackets, or first dollars of wages earned, than with respect to the subsequent brackets, or last dollars at higher wage levels.

Workers who have earned higher salaries over their careers receive benefits that are larger in absolute dollars, but are proportionally smaller than those received by lower paid workers. In other words, lower income workers pay the same flat percentage amount for a more generous package of benefits.

The flat percentage contributions, through which workers achieve insured status[48] and become eligible for benefits in the event of disability, death, or old age, give Social Security the essential property of an exchange. FICA payments are fundamental to making Social Security insurance, rather than welfare.[49] Although some refer to Social Security as part of the social welfare system,[50] social insurance and welfare developed from separate historical roots and are intrinsically different.[51]

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47. Cost-of-Living Increase and Other Determinations for 2007, 71 Fed. Reg. at 62,640.

48. To achieve "insured status," an individual must obtain the requisite number of quarters of coverage, which he or she earns through employment in service that is covered by Social Security. There are three types of insured status: fully insured, disabled insured, and currently insured. *See* 42 U.S.C. § 414 (2000); *see also supra* note 1.

49. For an excellent essay highlighting the difference between welfare and social insurance, see ROBERT BALL, INSURING THE ESSENTIALS: BOB BALL ON SOCIAL SECURITY 33-51 (Thomas Bethel ed., 2000) [hereinafter BALL, ESSENTIALS].

50. *See, e.g.*, Douglas Lathrop, Entitlements: Social Welfare Policy in the United States, http://www.gwu.edu/~gspm/academics/syllabi/mala/psc224_2.pdf (last visited Apr. 8, 2007).

51. The antecedents to modern welfare programs can be traced from biblical prescriptions, such as "thou shalt not wholly reap the corners of thy field, neither shalt thou gather the gleanings of thy harvest. And thou shalt not glean thy vineyard . . . ; thou shalt leave them for the poor . . . ." *Leviticus* 19:9-10 (King James). In England, the practice of voluntary tithing to the church to help the poor evolved into compulsory tithing and then into the English poor laws. These laws were in turn transplanted by the colonists from England to form the basis for America's welfare laws. *See* William P. Quigley, *Five Hundred Years of English Poor Laws, 1349-1834: Regulating the Working and Nonworking Poor*, 30 AKRON L. REV. 73, 74 n.4, 74-82 (1996). In contrast, a second equally rich but fundamentally different tradition of providing economic security came in the form of pooling of resources and risk among equals. *See* discussion *supra* notes 25-31 and accompanying text.

Welfare, by definition, provides a benefit based on need.[52] It generally involves an arrangement between financially unequal parties—those materially better off providing assistance to those less advantaged, the poor. The benefit is generally an amount designed to provide the recipient with just enough to get by, as judged by the provider. An examination of the potential recipient's income and assets ensures that he or she is really in need and thus determines eligibility. Past earnings are irrelevant as long as the person has no accumulated assets.[53] Obviously, if the potential recipient earns income above the subsistence level, he or she is not in need of the community's help. Moreover, if the person has savings upon which to draw, he or she is, again, not in need of the assistance of others.[54]

In contrast, insurance is a matter of right for those who are eligible. Eligibility derives from achieving insured status, irrespective of need.[55] Welfare programs are designed for people who are already poor. Social insurance prevents workers from becoming poor in the first place. Welfare programs are essential as long as there is poverty, but they have inescapable, inherent weaknesses.

For those people who can earn no more than the community-determined subsistence level, means-tested welfare removes financial incentives to work. Wages reduce the means-tested assistance, leaving recipients where they began. In that situation, work is like running on a treadmill. The work effort gets people no further along financially. Further, welfare discourages savings. If potential recipients must exhaust their savings before they are eligible to receive welfare, the system penalizes them for their thrift.[56]

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52. For example, one definition of welfare in the Merriam-Webster Collegiate Dictionary is "aid in the form of money or necessities for those in need." MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 1342 (10th ed. 1998).

53. *See* KATHLEEN MCGARRY & BRIAN KASKIE, CAL. POLICY RESEARCH CTR., THE ECONOMIC WELL-BEING OF OLDER CALIFORNIANS 2 (2001), http://www.ucop.edu/cprc/sb910econ3.pdf ("[Supplemental security income ('SSI')] recipients cannot earn income that exceeds their SSI benefit without reducing their payment amount, and accumulated assets must fall below certain limits. Consequently, many impoverished older adults are not eligible for SSI benefits because their assets (such as home equity) exceed the maximum allowed.").

54. As people grow older they tend to gradually "spend down" their assets. According to a 2001 paper by the California Policy Research Center at the University of California, the average net worth of individuals between the ages of seventy-one and seventy-five was $201,227, whereas that of people aged eighty-one to eighty-five decreased to $126,085. Given the increase in the general population's life expectancy, some have expressed concern over the elderly outliving their assets, opening them to financial insecurity late in life. *See id.* at 3.

55. *See supra* text accompanying notes 45-47 (discussing benefit eligibility requirements).

56. Rourke O'Brien, *Mixed Messages Inhibit Escape from Welfare*, WASGHINGTONPOST.COM, Aug. 31, 2006, http://www.washingtonpost.com/wpdyn/

Insurance has none of these shortcomings. If the insurance is designed to replace wages, as Social Security is, work is encouraged. Under Social Security and other wage-replacement pensions, the higher one's prior earnings, the higher the benefit received.[57] Moreover, social insurance encourages savings. Unlike welfare, savings do not disqualify a person from receiving benefits. Rather, savings permit an additional source of income from which to draw when one no longer receives a paycheck.

By definition, then, welfare discourages work; wage-related insurance encourages it. Welfare discourages savings; social insurance providing a floor of protection encourages workers to save. To qualify for welfare, recipients must prove something negative about themselves—that they do not have enough to get along on their own. In contrast, beneficiaries of social insurance must prove something positive—that they have worked long enough to qualify for benefits.

President Franklin Roosevelt believed in structuring Social Security as social insurance, not welfare. However, the belief did not emerge simply as the result of an intellectual analysis of the objective advantages of insurance over welfare. Rather, Roosevelt preferred insurance because he understood what it meant to be dependent.

Frances Perkins, President Roosevelt's Secretary of Labor and long-time associate, witnessed Roosevelt undergo "a spiritual transformation during the years of his illness . . . . The man emerged completely warmhearted, with humility of spirit and with a deeper philosophy. Having been in the depths of trouble, he understood the problems of people in trouble."[58] Roosevelt understood clearly that people would be uplifted in spirit if they worked hard and joined together to provide a common pool of funds from which to draw when their working days were over. He understood how demeaning it was for people to have to prove to someone else that they could not support themselves without help, and how crippling in spirit to feel oneself to be helpless and a failure.

The President held a long-standing view that benefits for the elderly should be structured as insurance, not welfare. In 1931, in his annual message to the legislature, then-Governor Roosevelt stated that the welfare bill enacted in the prior session "may be justified only as a means intended to replace to a large extent the existing methods

content/article/2006/08/30/AR2006083002684.html.

57. *See supra* note 47 and accompanying text (explaining the calculation of Social Security benefits).

58. FRANCES PERKINS, THE ROOSEVELT I KNEW 29 (1946).

of poor-house and poor-farm relief," but it should not be expanded, for to do so would "smack of the . . . dole."[59] Rather, he continued, "our American aged do not want charity, but rather old age comforts to which they are rightfully entitled by their own thrift and foresight in the form of insurance."[60] He believed that,

> the next step to be taken should be based on the theory of insurance by a system of contributions commencing at an early age. In this way men and women will, on arriving at a period when work is no longer practicable, be assured not merely of a roof over head and enough food to keep body and soul together, but also enough income to maintain life during the balance of their days in accordance with the American standard of living.[61]

President Roosevelt recognized that in order to get immediate assistance to people in need—to alleviate the immediate suffering caused by the Depression—there was no alternative to welfare. But for the long term—once the Depression was history and the economic health of the country restored—the President wanted a system of insurance in place to guarantee for posterity that people would have a reliable, stable source of income from which they could draw in old-age. Acutely conscious of the debilitating quality of fear, he wanted all workers to have the peace of mind and security that they would be insured against their dependency on wages.

Consistent with being a form of insurance premium, FICA contributions promote the security of the program. Social Security, as its name suggests, is intended to provide not only tangible cash benefits, but also the intangible benefit of security during a future beneficiary's working years. For Social Security to accomplish its goal of providing security, people must be able to depend on its long-term continuation. Otherwise, the program ceases to function as intended, providing only income replacement, not security.

No Congress can bind its successor to maintain statutory entitlements.[62] Nevertheless, to the extent that people have made specific monetary payments to ensure receipt of their own benefit, the moral obligation of government to honor the promises made is

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59. COMM. ON ECON. SEC., SOC. SEC. ADMIN., BRIEF IN DEFENSE OF OLD-AGE BENEFITS AS PROVIDED IN THE SOCIAL SECURITY BILL (1937), http://www.ssa.gov/history/reports/ces/ces2harrisbrief.html (discussing President Roosevelt's 1931 Annual Message to the Legislature).

60. *Id.*

61. *Id.*

62. The Supreme Court has clarified that the promise of Social Security benefits is not a binding, contractual right. *See* Flemming v. Nestor, 363 U.S. 603, 608-11 (1960) (upholding the termination of the benefits of an alien deported for having been a member of the Communist party).

much stronger than it would be otherwise. Americans appropriately have a sense of contributing toward their own retirement and feel good about receiving those benefits. This sense of entitlement contributes to the program's success. As long as political support for Social Security remains strong, benefits will continue to be paid, in full and on time, as they have since the program began.[63] As long as these important benefits are paid, support will remain strong.

III. PROGRESSIVITY AND SOCIAL SECURITY'S LONG RANGE DEFICIT

Retaining the fundamental design feature of an employee contribution to Social Security is important to the stability, popularity, and success of the program. At the same time, concerns about the retirement income system should not override other equally important public policy goals, such as increasing the returns that low-income workers receive from their work effort by reducing the costs of working, including the financial burden of the Social Security contributions, federal and state income taxes, and other work expenses. For these reasons, in 1975 Congress enacted the Earned Income Tax Credit ("EITC"),[64] which provides eligible low income taxpayers a refundable tax credit to apply against their income tax liability.

The EITC indirectly adds progressivity to the overall structure of Social Security. The current projected long-range deficit in Social Security presents an additional opportunity to increase the program's progressivity. The current projected seventy-five-year shortfall is around 2% of taxable payroll.[65] In other words, increasing the 6.2%

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63. Social Security is affordable, notwithstanding fears to the contrary. The total dependency ratio in the United States, which is the number of all nonworkers (elderly and children) to all workers, is projected to be lower over the next seventy-five years than what it was from 1960 to 1975, even considering the aging of the population. *See* Richard B. Du Boff, Samuel & Etta Wexler Professor of Econ. Emeritus, Social Security is not in "Crisis," Bryn Mawr Emeritus Gatherings (Feb. 1999), http://www.brynmawr.edu/emeritus/gather/Duboff.html. For one way to solve Social Security's current projected long-range deficit, see *infra* notes 66-92 and accompanying text.

64. *See* Tax Reduction Act of 1975, Pub. L. No. 94-12, § 43, 89 Stat. 26, 30 (codified as amended at I.R.C. § 32 (1975)).

65. More precisely, the long-range deficit is projected to be 1,95% of taxable payroll. 2007 ANNUAL REPORT, *supra* note 30, at 2. The long run deficit and the estimates of savings derived from various reform proposals are routinely expressed in terms of percentage of taxable payroll. "Taxable payroll" is the payroll that is under the maximum taxable wage base. The "percentage" is the tax rate. Since 1965, Social Security actuaries have consistently employed a seventy-five-year valuation period for the program. *See* LARRY DEWITT, SSA HISTORIAN'S OFFICE, RESEARCH NOTE #14: KEY DATA FROM THE ANNUAL TRUSTEES REPORTS (2001), http://www.ssa.gov/history/trustchart.html#%7B17%7D. For a public program of social insurance, the trustees of the program have concluded that seventy-five years is the proper length of

FICA rate to 7.2% on employees and employers, for a combined increase of 2%, could eliminate the projected deficit. However, raising the FICA rate would needlessly increase the burden of low-income taxpayers. A preferable way of closing the deficit is through three reforms, all of which are sound policy and increase Social Security's progressivity while retaining its distinctive character.[66] These three reforms would bring the program into "close actuarial balance" over the next seventy-five years. (Social Security's trustees have long recognized the impossibility of making exact projections for as long as seventy-five years into the future. First employed in 1957, "close actuarial balance" is a test that Social Security's trustees use to determine whether to recommend legislative changes in Social Security's financing).[67]

First, the practice of subjecting 90% of all covered earnings nationwide to FICA should be restored. (The 90% mark is achieved when 90% of the sum of all wages covered by Social Security are under the maximum taxable wage base and only 10% are above.[68]) In 1977, Congress intended to make the 90% practice permanent and automatic, without need for further legislative action, by having the maximum taxable wage base increase annually by the same

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time to forecast the long-term financial operations of the trust funds. Workers who are age twenty and just starting their working lives this year will be age ninety-five (if still alive) in the last year of the valuation period. *Id.*; *see also* ALTMAN, *supra* note 1, at 298. (distinguishing Social Security's valuation period of seventy-five years as a longer than is generally employed by the private sector with respect to private pension plans).

66. Former Commissioner Robert M. Ball developed the three proposals. *See generally* Robert M. Ball, *Meeting Social Security's Long-Range Shortfall: A Golden Opportunity for the New Congress*, Apr. 15, 2007, http://robertmball.org/ (suggesting three reforms to ensure Social Security's funding and long-range financial balance); *see also* ALTMAN, *supra* note 1, at 297-309 (describing in greater detail Ball's three proposals for Social Security reform). For another perspective on the proposals, see Kathryn L. Moore, *Social Security Reform: Fundamental Restructuring or Incremental Change*, 11 LEWIS & CLARK L. REV. (forthcoming 2007), and Kathryn L. Moore, The Battle for Social Security: From FDR's Vision to Bush's Gamble, 40 J. MARSHALL L. REV. (forthcoming 2007) (book review).

67. Close actuarial balance is satisfied if income falls within plus-or-minus 5% of outgo over the next seventy-five years, an amount that is calculated today at about 0.80% of taxable payroll. 2007 ANNUAL REPORT, *supra* note 30, at 61.

68. When Congress enacted Social Security in 1935, all covered wages below a maximum level of $3000 were subject to withholding for Social Security. *See* Social Security Act of 1935, Pub. L. No. 74-271, § 811, 49 Stat. 620, 639 (1935). The $3000 limit covered 92.4% of all wages paid to workers covered under Social Security in 1940. SOC. SEC. ADMIN., SOCIAL SECURITY BULLETIN, ANNUAL STATISTICAL SUPPLEMENT tbl.4.B1 (2005), http://www.ssa.gov/policy/docs/statcomps/supplement/2005/4b.html#table4.b1. Before automatic indexing, Congress raised the base on an ad hoc basis as part of legislative increases in benefit levels. *See, e.g.*, Social Security Amendments of 1954, Pub. L. No. 83-761, 68 Stat. 1052 (1954).

percentage as the increase in average wages nationwide.[69] Unfortunately, this adjustment mechanism has not worked as planned because the earnings of high income workers have increased much more rapidly than the average in the last several decades.[70] As a result, the 90% target has declined steadily as an increasing amount of the earnings of the highest paid have risen above the base. Today, only about 83% of wages in covered employment are within today's maximum taxable wage base.[71]

The switch from coverage of 90% of wages to 83% was not a conscious policy decision, but a byproduct of whose wages grew the fastest over the last few decades. Indeed, the last two times it acted on Social Security financing (in 1977 and 1983), Congress endorsed the 90% benchmark.[72] That seemingly small slippage from 90% to 83% translates into billions of dollars in lost revenues each year.

Restoring that 90% practice is a highly progressive way to close about a third of the long range deficit.[73] That restoration can and should be extremely gradual—over a number of decades—so that the the impact on the 6% of workers earning above the maximum taxable wage base would be close to trivial. The restoration can and should be done so gradually that, in any particular year, the highest-paid, 6% of the workforce affected by the change would be subject to no more than one additional week of FICA withholding, about $121 in 2007.[74] Those workers paying increased FICA contributions would

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69. *See* REPORT OF THE COMM. ON WAYS AND MEANS TO ACCOMPANY H.R. 9346, H.R. REP. NO. 95-702(I), pt. 1, at 18, *reprinted in* 1977 U.S.C.C.A.N. 4155, 4175. Because the wages covered by the maximum taxable wage base represented only 85% of total wages in 1977, Congress also enacted several ad hoc increases to the wage base, over and above the automatic adjustments, so that the base would be restored to covering 90% of all wages. *See* Social Security Financing Amendments of 1977, Pub. L. No. 95-216, 91 Stat. 1509 (1977). The 90% level was reached in 1982.

70. *See* U.S. CENSUS BUREAU, INCOME IN THE UNITED STATES: 2002, CURRENT POPULATION REPORTS 25, tbl.A-3 (Sept. 2003), http://www.census.gov/prod/2003pubs/p60-221.pdf.

71. *See* SOCIAL SECURITY BULLETIN, *supra* note 68, at tbl.4B1, col. 6.

72. In 1977, Congress explicitly explained its actions in terms of the 90% benchmark. *Supra* note 69. In 1983, Congress implicitly endorsed the 90% mark by taking no contrary action. Social Security Amendments of 1983, Pub. L. No. 98-21, 97 Stat. 65 (1983).

73. *Infra* note 83 and accompanying table.

74. This reform would slowly raise the maximum taxable wage base above the increases automatically scheduled in the law, so that the base once again covers 90% of wages in covered employment. The adjustment is so gradual that the base would not reach the 90% mark for a number of decades. Specifically, on top of the annual percentage increase in the maximum taxable wage base to match the growth in average wages, this proposal would impose an additional 2% increase in the base, until the base once again covers 90% of all wages paid to covered workers. For example, in 2007, the maximum taxable wage base is $97,500. If the reform had been in effect this year, the base would increase an additional 2% on top the current annual percentage growth in wages, or $1950 (i.e., 2% of $97,500). The additional

receive higher benefits in the event of disability or reaching retirement age, and their families would receive higher survivors benefits.[75] Ninety-four percent of the workforce would be completely unaffected.

Second, the federal estate tax, as structured in 2009, should be maintained thereafter and converted into a dedicated Social Security tax, beginning in 2010.[76] In 2001, Congress enacted legislation that gradually phases out the federal estate tax, by increasing the exempt

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tax paid for workers at or above the base in 2007 would be $120.90 (i.e., 6.2% of $1950). FICA is generally withheld at equal rates from workers' paychecks until wages meet the maximum taxable base. At most, this proposal would require workers to have one additional week of FICA withholding. The 94% of workers earning under the maximum taxable wage base would continue to have FICA withheld for the entire year. Those earning exactly at the maximum taxable wage base would continue to have FICA withheld for one additional week than they would experience without the change. Those earning over the wage base would reach the 2% increase in less than a week. The timetable could be expedited in order to reach the 90% level sooner. If the 90% mark were reached in ten years, rather than thirty-six, as this proposal would do, the deficit would reduce even more, to about 1.3% of payroll. However, because this would require adding 8% rather than 2% per year to the automatic adjustment, it would substantially increase the burden of taxation on workers who earn not much above the present maximum. For example, someone earning only $7500 above the cap next year would pay an additional tax of $465. The slower timetable accomplishes nearly as much deficit reduction without imposing sharp tax increases.

75. Because of the progressive benefit formula and the timing of receipts and disbursements, the proposal would generate income for the trust funds, despite the somewhat increased benefit levels.

76. Some have expressed concern about the impact of the estate tax on family farms and small, family-owned businesses. *See, e.g.*, 152 CONG. REC. S5580 (daily ed. June 7, 2006) (statement of Sen. Isakson), *available at* http://isakson.senate.gov/floor/2006/060706estatetax.htm (supporting of a repeal of the estate tax). But the vast majority of these enterprises would be completely exempt from payment of a tax under the proposal. Leonard E. Burman, William G. Gale & Jeffrey Rohaly, *Options for Reforming the Estate Tax*, 107 TAX NOTES 379, 383 (2005), *available at* http://www.taxpolicycenter.org/UploadedPDF/1000780_Tax_Break_4-18-05.pdf (explaining that based on estate tax returns filed in 2004, with a $3,500,000 exemption, "[o]nly about 30 small businesses and farms would continue to pay the tax, contributing 0.2% of total estate tax revenues."). Through estate planning, even those thirty small businesses and farms could reduce their liabilities substantially. Family farms and small, family-owned businesses receive favorable estate tax treatment under current law. For example, farmers and small business owners may use a special formula to reduce the value of their real estate, so long as their heirs continue to use it as a family-owned farm or business and do not sell it to a nonrelative for ten years or more. The formula can result in reductions of the value of the real estate of between 40% and 70%. In addition, if more than 35% of an estate's assets consist of farms and business assets, the estate may pay any owed estate tax in installments payable over fourteen years at reduced interest rates. With careful estate and gift planning, the tax liability could be reduced or eliminated completely. *Id.* at 379. *See generally* CONG. BUDGET OFFICE, EFFECTS OF THE FEDERAL ESTATE TAX ON FARMS AND SMALL BUSINESSES (2005), http://www.cbo.gov/ftpdocs/65xx/doc6512/07-06-EstateTax.pdf (explaining the impact of the estate tax on small businesses and farmers, particularly in relation to transfer of property to heirs). This proposal would leave all of that unchanged.

amount and reducing the rate.[77] The 2001 law provides that in 2009, the exclusion is scheduled to rise to $3,500,000 ($7,000,000 for a married couple).[78] In 2010, the estate tax is scheduled to be zero on all estates, no matter the size.[79] Then, so that future federal budget deficits would not appear so large, Congress had the 2001 legislation sunset, effective in 2011.[80] In that year, if no new legislation is enacted, the estate tax will revert to its 2000 form—i.e., assets in excess of $1,000,000 not left to spouses would be taxed at a 50% rate.[81] President George W. Bush has urged Congress to repeal the estate tax permanently.[82]

Instead of repealing the estate tax, maintaining it at its 2009 level and earmarking its proceeds for Social Security would provide a progressive way of paying down a portion of the costs incurred at the inception of the program. During the start up of Social Security, policymakers decided that the then-current generation of retirees should receive a meaningful benefit from Social Security, even though they did not have enough years under the system to contribute anywhere close to the equivalent value of those benefits. Providing meaningful benefits to older workers at the plan's start is analogous to the practice of many private pensions, which grandfather in older employees by granting them past service credits.[83] Social Security's startup costs have never been amortized.[84] Rather than being met solely by the contributions of future workers

77. *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38 (2001) [hereinafter EGTRRA].

78. In 2009, the tax rate is scheduled to decline to 45%. Id. §§ 501-521, 115 Stat. at 69-72.

79. *Id.*, 115 Stat. at 69-72.

80. Under EGTRRA's sunset clause, the Act is scheduled to expire in 2011. Pub. L. No. 107-16, § 901(b), 115 Stat. 38, 150 (2001).

81. *Id.* § 901(b), 115 Stat. at 150.

82. *See* OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, H.R. 5638–PERMANENT ESTATE TAX RELIEF ACT 1 (2006), http://www.whitehouse.gov/omb/legislative/sap/109-2/hr5638sap-h.pdf.

83. BALL, SOCIAL SECURITY, *supra* note 27, at 210.

84. From the beginning of the deliberations on Social Security, a number of experts have believed that, while the major part of Social Security's financing should come from contributions from wages, some funding should eventually come from general revenue. *See, e.g.*, COMM. ON ECON. SEC., SOC. SEC. ADMIN., REPORT OF THE COMMITTEE ON ECONOMIC SECURITY (1935), http://www.ssa.gov/history/reports/ces5.html (proposing general revenue contributions to begin in 1965); *see also* Altman, *supra* note 1, at 60-61 (describing Roosevelt's reaction in opposition to the plan for taking any payments from general revenue, a position shared by, and by some attributed to, his Secretary of the Treasury, Henry Morgenthau); BALL, ESSENTIALS, *supra* note 49, at 226 (noting the popularity of the proposal for a "system of flat payments paid for from general revenues" from the inception of the Social Security program on).

and their employers, these costs should be paid, at least in part, from a progressive tax that includes capital as well as labor.

As the estate tax will be structured in 2009, the estates of the top 5% of all Americans will pay 99.6% of the tax, and the top 1% will pay 97.4% of the tax.[85] The accumulation of large estates is not the result exclusively of the effort of the owner of the estate, but depends also on the general productivity of the American economy and on its infrastructure. Thus, requiring the very wealthiest estates to contribute a portion of their fortune to the common good, while still passing more than half of their assets to heirs, seems a reasonable minimum to ask of those who have benefited so greatly from the commonwealth (i.e., the common wealth). As with the restoration of the maximum taxable wage base, this reform would have no effect on the vast majority of taxpayers.

Finally, just as virtually every other pension plan, Social Security should be permitted to diversify its portfolio and invest in stock funds, as well as Treasury bonds. (Social Security is restricted, by current law, to investment in United States' obligations or in entities whose principal and interest are guaranteed by the United States.[86]) There is ample precedent for responsible investment in equities by today's public pension plans. Assets of the Railroad Retirement Plan,[87] the Federal Reserve Board Plan,[88] and Canada's Social Security pension plan,[89] to name just a few, are invested in equities. Proper investment of our nation's Social Security assets can offset investment lost by the termination of private-sector defined benefit plans or assets invested too conservatively by participants in 401(k) plans.

The idea was first mentioned in the 1930's, but was not pursued because conservatives at the time were concerned about government interference in the stock market.[90] Many of today's conservatives embrace President Bush's proposal for Social Security private accounts, which suggests that the historical concern should no longer

85. *See* Leonard E. Burman, William G. Gale, & Jeffrey Rohaly, *The Distribution of the Estate Tax and Reform Options*, *in* NATIONAL TAX ASSOCIATION PROCEEDINGS 7 tbl.3 (2004), *available at* http://www.urban.org/uploadedPDF/411135_EstateTax.pdf.

86. *Supra* note 34.

87. Railroad Retirement and Survivors' Improvement Act of 2001, Pub. L. No. 107-90, § 105, 115 Stat. 878, 882-87 (2001).

88. *See generally* GOV. EDWARD W. KELLEY, JR., SERVICE CREDIT UNDER THE FEDERAL EMPLOYEES RETIREMENT SYSTEM (1999), http://www.federalreserve.gov/boarddocs/Testimony/1999/19990225.htm (describing the operation of the Federal Reserve retirement system).

89. *See* General Information about the Canada Pension Plan, ¶¶ 26 & 27, http://www.hrsdc.gc.ca/en/isp/cpp/cppinfo.shtml#26 (last visited Apr. 20, 2007).

90. Altman, *supra* note 1, at 122; *see also* ARTHUR J. ALTMEYER, THE FORMATIVE YEARS OF SOCIAL SECURITY 89 (1966).

be there if proponents of private accounts are to be consistent. Under both the President's proposal and the one advocated here, the government selects a limited number of indexed stock funds in which the monies could be invested. Government involvement in the stock market is no different in practical effect if individual workers decide what percentage of Social Security contributions go to each fund, as under the President's proposal, or if an independent board of experts makes the same decision, as would be the case if the assets remained pooled.[91]

Although the extent of government involvement in the stock market is the same under both proposals, the difference with respect to individuals is substantial. Under this proposal, benefits remain guaranteed. Retirement income would continue to be based on earnings records, not the vagaries of the stock market.[92] Diversifying Social Security's portfolio would permit the benefit of higher market returns without individual risk.

As the following table shows, taken together, the three proposals restore Social Security to long-range close actuarial balance. They do so without putting additional burdens on low-income taxpayers—or

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91. A number of safeguards could help ensure against interference with the stock market. First, the investments could be limited to very broad, indexed funds that reflect virtually the entire American economy, and not individual stocks. Further, the amount invested could be limited to, for example, no more than 20% of assets, not to exceed 15% of the total market value of all stocks. This amount could be gradually phased in to ensure against market dislocations. Further, a Federal Reserve-type board with long and staggered terms could be created and assigned the limited functions of selecting the indexed funds; selecting the portfolio managers by bid from among experienced managers of indexed funds; and monitoring and reporting to the trustees and public on Social Security's investments. Finally, Social Security could be prohibited by law from voting any stock or otherwise influencing the policies or practices of any company or industry whose stock is held by the indexed fund.

92. Unlike investments by individuals, this proposal spreads the risk across the entire population over an unlimited time horizon. In contrast, individuals investing retirement funds in the stock market bear the entire risk of poor investment performance. In addition, they ordinarily will have to cash in their investments at or near the time of retirement, and if they are to protect themselves from running out of money before they die, will need to purchase annuities. They may also have to sell stocks and buy an annuity during a market downturn. A variation of even a few months in the time of buying an annuity can make a huge difference in its value. *See generally* GARY BURTLESS, CTR. ON SOC. AND ECON. DYNAMICS, SOCIAL SECURITY PRIVATIZATION AND FINANCIAL MARKET RISK 23 (2000), http://www.brookings.edu/ES/dynamics/papers/sspriv/sspriv.pdf (demonstrating that workers with identical forty-year careers and wages, all retiring at the same age of sixty-two and all purchasing level annuities for retirement, can receive dramatically different benefits based on nothing other than market timing). In contrast, an adequately funded Social Security fund would not have to reduce net assets at any particular time and as such could ride out market fluctuations. Investment risks would be spread over the entire population and be independent of the time a worker filed for benefits.

for that matter on the vast majority of taxpayers and without reducing the benefits that are so vital to virtually every American.

Bringing Social Security into Long-Range Balance[93]	
	Percent of Payroll
The seventy-five-year deficit as projected by the Trustees' 2006 middle-range estimate:	- 2.0
Reforms:	
1. Gradually restore the maximum taxable earnings base to 90 percent of covered earnings.	+ 0.7
2. Maintain the residual estate tax at its current-law 2009 level, and convert it into a dedicated Social Security tax, effective in 2010.	+ 0.5
3. Diversify the trust funds' portfolio by investing some of the assets in broad-based, indexed stock funds.	+ 0.4
Total for 1 through 3	+ 1.5[94]
Deficit well within close actuarial balance[95]	- 0.5[96]

93. The estimates in this table have been made by the Office of the Actuary, Social Security Administration, based on the assumptions underlying the middle-range estimates of the 2006 Trustees Report and reflect a 75-year valuation period. It will take some time for the Social Security actuaries to shift to using the 2007 report, which was released on April 23, 2007, and the differences are very small (e.g., 1.95% of payroll projected deficit in 2007 report, instead of 2.02% projected deficit in 2006 report). 2007 Annual Report, *supra* note 30; BD. OF TRS. OF THE FED. OLD-AGE AND SURVIVORS INS. & FED. DISABILITY INS. TR. FUNDS, ANNUAL REPORT 2006, at 2 (2006), *available at* http://www.ssa.gov/OACT/TR/TR06/tr06.pdf.

94. Because of rounding, the numbers do not add.

95. *Supra* note 67 and accompanying text.

96. For those interested in bringing Social Security to surplus, the author discusses elsewhere several other small, incremental reforms which bring the program to surplus. ALTMAN, *supra* note 1, at 306-08.

Social Security is important to all Americans, but, particularly, to low-income workers and their families. Financing the program partly through earmarked deductions from employees' wages is an integral and vital part of Social Security's design, and has been an important reason for Social Security's success and broad public support over the program's seventy-year life. At the same time, these contributions are harder to bear for those with lower wages. Just as the EITC has eased the burden of these contributions without undermining the basic structure and philosophy of Social Security, so the program's long-range deficit, if eliminated properly, can help strengthen Social Security while remaining sensitive to the burdens of the low-wage worker. If that is done, Social Security will continue, in the words of President Franklin Roosevelt, "to provide sound and adequate protection against the vicissitudes of modern life"[97] for all workers and their families, now and in the future.

97. *Supra* note 31.