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Why the Archer–Shaw Proposal Is Not the Way to Reform Social Security

Stuart M. Butler, Ph.D., and David C. John

The Social Security "add-on" retirement accounts contained in a new reform proposal by House Ways and Means Committee Chairman Bill Archer (R–TX) and Social Security Subcommittee Chairman Clay Shaw (R–FL) would be the wrong way to achieve Social Security reform. This plan would (1) not allow workers to place a portion of their current payroll taxes into personal accounts they control to build a retirement "nest egg"; (2) provide most Americans, especially low-income workers, with the same low benefits they currently can expect from Social Security; (3) encourage workers to seek risky investment options for their accounts because their risk would be protected entirely by the government and only high-yield investments would lead to higher retirement income; and (4) channel general tax revenue into the trust fund, rather than address the underlying problems.

Under the Archer–Shaw proposal, the government would deposit into each worker's personal retirement account an amount equal to 2 percent of his or her income. The money would come from general tax revenues collected by the federal government and go to a private funds manager chosen by the worker from a list approved by a new federal agency. At least initially, the money would be invested in a portfolio made up of 60 percent stocks and 40 percent corporate bonds.

Workers would not receive the money in these accounts on retirement. Instead, the entire account would be taken over by Social Security, which then would pay the worker a monthly annuity based on funds in the account. This amount, in effect, would be deducted, dollar for dollar, from the check the retiree would receive from today's Social Security system. Only if the account were large enough to pay a monthly benefit that is *greater than* the current Social Security benefit would the worker receive a larger check than under today's system.

On the death of a retired married worker, any money left in the account would go into the spouse's account, where it could increase retirement income. On that spouse's death, the money in the account would revert to the Social Security trust fund, not to the worker's heirs. Only if a worker died before retiring would the entire account become part of the worker's estate.

Eventually, the Archer–Shaw plan might allow some workers to increase their retirement income. It also would create an infrastructure of individual

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accounts for lower-income workers and familiarize voters with long-term investing. But these benefits would be more than offset by serious flaws:

- **The Archer–Shaw plan would not reform Social Security and it would keep taxes high.** Workers would pay more in taxes for essentially the same benefits. The plan would create a new tax-financed savings program that would pay all or part of the benefits retirees currently can expect from Social Security. The actual total amount in benefits virtually all workers receive would remain the same. Under this plan, workers would pay both their existing Social Security payroll taxes and the income taxes going into their new accounts. The total tax burden for Social Security retirement benefits would climb from 10.6 percent of income today to an average of 12.6 percent.

- **The plan would make Social Security an even worse deal.** Currently, workers receive a very poor rate of return on Social Security taxes. If an average family with two earners were allowed to invest their Social Security retirement taxes in stocks and government bonds, they could expect to have $525,000 more for retirement than the current system promises. But their situation would be worse under the Archer–Shaw plan. Although most workers' actual monthly Social Security retirement benefits would not change, workers would pay more in total taxes for those same low benefits.

- **The plan would make "personal" retirement accounts the property of the government, estate planning more uncertain, and the "moral hazard" risk to the government greater.** Under this plan, a worker would surrender the entire personal retirement account to Social Security on retirement. Any money remaining after both worker and spouse die would benefit the government, not their estates. But if the worker died before retirement, his or her heirs would receive the funds in the account. Thus, a worker who lived barely to retirement would leave a smaller estate than a worker who died just before retirement, making estate planning more difficult.

  The plan would assure that all workers receive at least their current projected Social Security benefits, no matter how poorly their personal accounts fared. This assurance would encourage workers to seek the highest potential return, regardless of risk—sharply increasing risk to the government and future taxpayers. Such a perverse incentive, like that in the savings and loan debacle of the 1980s, is what economists call a "moral hazard."

Despite these extremely serious flaws, changing some aspects of the Archer–Shaw plan could advance the Social Security debate. These include:

- **Funding the accounts by allowing workers to redirect some of the existing Social Security taxes.** Doing this as a refundable tax credit would be a more effective and permanent way to fund personal retirement accounts. It also would give workers a better rate of return on their payroll taxes.

- **Making the program voluntary and tying personal accounts to benefit changes.** Workers should be able to choose to participate in the program. If they did, they should keep all the earnings from their accounts and give up a portion of their existing Social Security benefits.

- **Allowing workers to benefit from their own accounts.** Instead of requiring workers to give their entire accounts to Social Security or turn it all into an annuity, the plan should allow them to use the accounts in retirement for such purposes as starting a small business; helping a grandchild with college expenses; giving money to their families, churches, or communities; or building their estate.

Although the Archer–Shaw plan is a serious attempt to avoid Social Security's impending financial collapse, it would neither improve the returns workers can expect nor address Social Security's severe financial problems. No action this year would be better than passing this flawed plan.

—Stuart M. Butler, Ph.D., is Vice President of Domestic and Economic Policy Studies and David C. John is Senior Policy Analyst for Social Security at The Heritage Foundation.

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