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DID THE PRESIDENT MISLEAD ON SOCIAL SECURITY IN HIS APRIL 29 PRESS CONFERENCE?

by Robert Greenstein

A series of statements by President Bush in his press conference on April 29 is likely to have left millions of viewers with misimpressions about his private-accounts proposal and about the Social Security system. Many of these statements had a common element — they created misleading impressions about how the private accounts would work, because of the President's failure to explain in the press conference that people who elect the accounts would have their Social Security benefits reduced in return. For each dollar that a worker placed in a private account, the worker's Social Security benefits would be reduced by one dollar *plus* an interest charge equal to 3 percent.

The President's statements were problematic in at least five respects.

1. Obscuring the fact that those electing private accounts would have to pay back Social Security through reductions in their Social Security benefits.

In his opening statement, the President declared that "The money from a voluntary personal account would supplement the check one receives from Social Security." He did not explain that those electing the accounts would have their Social Security benefits reduced in return and would come out ahead only if (and to the extent that) their account earned more than 3 percent above inflation.

Few Americans are likely to have understood that the private accounts would not be pure supplements to Social Security; viewers are unlikely to have realized that their Social Security benefits not only would be reduced by the "progressive price indexing" changes the President described but would then be reduced further if they elected a private account. And very few likely understood they would lose money if their account did not make at least 3 percent above inflation. (Yale economist and financial market expert Robert Shiller, author of *Irrational Exuberance*, estimates that between 32 percent and 71 percent of people who elect the President's private accounts would lose money as a consequence.[1])

2. Not explaining that under the option he touted to allow workers to invest their private accounts entirely in Treasury bonds, workers would be guaranteed to lose money.

A particularly misleading aspect of the press conference came when the President said that he knows some people have reservations about the stock market and that he is addressing their concerns by proposing "that one investment option consist entirely of Treasury bonds, which are backed by the full faith and credit of the United States government."

[1] Robert J. Shiller, "The Life-Cycle Personal Accounts Proposal for Social Security: An Evaluation," March 2005.

The President was not very transparent here. He did not explain that under his plan, Americans who chose this investment option would be virtually guaranteed to lose money.

- Workers who elected this investment option would have their Social Security benefits cut by the amount that they placed in their accounts plus an interest charge equal to 3 percent above the inflation rate. But three percent above inflation is what the Social Security actuaries project that Treasury bonds will earn. (A number of financial market experts believe Treasury bonds are likely to earn less than this.) Thus, if a worker chose this investment option, his or her Social Security benefits would be reduced by *the same amount* that the Treasury bonds in the worker's account would earn, if the actuaries' estimate is accurate..

- The worker also would have to pay management fees out of the funds in his or her account. (The Administration estimates that the annual management fee will equal 0.3 percent of the amount in the account, which over a typical career, would consume about 7 percent of the proceeds in an account). Consequently, the worker would be left with a net return that is *lower* than the Treasury bond rate.

- As a result, people who elected this option would lose money because of their private account. One would not know that from the President's discussion of this matter in the press conference.

Adding to the misleading impression that the President created in this area, he also failed to explain that under his plan, a worker who elected a private account at any time — even in his or her early 20s — *would never be allowed to reverse that choice.* The worker would be required to have funds diverted from Social Security to a private account for the rest of his or her career. Hence, if a worker initially elected a private account but then grew fearful of the stock market and did not want to be subject to any investment risk, the worker's only choice would be to invest his or her account in Treasury bonds — and to be assured of losing money.

3. Portraying Treasury bonds in personal accounts as rock-solid, but Treasury bonds in the Social Security Trust Fund as shaky IOUs.

Compounding the problems regarding his treatment of the Treasury bond option, the President denigrated the Social Security Trust Fund later in his press conference, portraying it as nothing more than "file cabinets of IOUs." He failed to tell viewers that these "IOUs" are Treasury bonds, the very investment he lauded as providing a rock-solid investment option for people who elect private accounts and want to avoid risk. When discussing this option for people who elect a private account, the President spoke reassuringly of providing people the option of having accounts that "consist entirely of Treasury bonds, which are backed by the full faith and credit of the United States government." When he spoke of the Social Security Trust fund, however, somehow Treasury bonds transmuted into meaningless IOUs locked up in file cabinets in West Virginia.

4. Misrepresenting how people who die before retirement fare under Social Security and how they would fare under his proposal.

Perhaps the President's most serious misrepresentation involved his discussion of how the families of workers who die before retirement fare under Social Security today and how they would fare under his proposals. The President implied that such families receive nothing today but a burial benefit. "Somebody has worked all their life, the money they pay into the system just goes away," he said.

By contrast, he asserted "If you have a personal savings account, a voluntary personal savings account, and your - - you die early, that's an asset you can leave to your spouse or to your children. That's an important thing for our fellow citizens to understand. The system today is not fair, particularly if the spouse has died early, and this will help remedy that."

Unfortunately, the President misrepresented both how the Social Security system works if a worker dies before reaching retirement and how his private accounts would function in such an event. Under the current system, if a worker with children dies before retirement, the children receive substantial Social Security survivor benefits every year until they reach 18 (or until age 19 if the children are enrolled in high school, and until age 22 if they are disabled). A deceased worker's spouse also receives Social Security survivor benefits for herself every year until her youngest child reaches 16 (and for some years after that if the child is disabled). If there are no children who are under 16 or disabled, the spouse is eligible to receive survivor benefits every year starting when she is 60.

Some 18 percent of all Social Security benefits — or $88 billion in 2004 — consist of survivor benefits. From the President's remarks, one would not know that Social Security provides such substantial survivor benefits. Nor would one know that the "progressive price indexing" proposal he endorsed would *cut* survivors benefits (except for the survivors of workers who had very low earnings). Survivor benefits would be reduced fully as much as Social Security retirement benefits.

Indeed, from listening to the President, one might have thought that the only people whose Social Security benefits would be reduced are affluent retirees. One would not know that the minor children and widows of modest-income wage earners who died prematurely also would be subject to benefit reductions.

Most significantly, the President created a highly misleading impression about what would happen to a worker's private account if the worker died early. He portrayed the private account as simply being bequeathed to the deceased worker's family. *But that is not how the President's proposal works.* Under his proposal, the surviving spouse would inherit *both* the deceased spouse's private account *and the debt that the deceased spouse owes to the Social Security system* to pay for having diverting money into a private account.

What this means is that if the deceased worker's account earned less than 3 percent above inflation, *the surviving spouse would lose money; the debt she owed to Social Security would be larger than the account she inherited, and she would be made worse off by inheriting the account.* This loss would be on top of the Social Security benefit losses that she and her children would suffer as a result of the application of progressive price indexing to survivors benefits.

What Happens if No Action is Taken on Social Security: Did the President Shade Reality?

As he has done in the past, the President made several misleading statements in his press conference on two aspects of Social Security's finances.

- The President said "the system goes broke in 2041"and "by 2041, Social Security will be bankrupt." Most people would probably think this means that Social Security would have no money to pay any benefits after 2041; after all, "going broke" is commonly understood to mean having no money. In fact, the Social Security actuaries' have projected that Social Security will continue to bring in sufficient revenues to pay 74 percent of promised benefits in 2041. (The percentage drops to 66 percent by 2079.) The Congressional Budget Office projects that Social Security will be able to pay full benefits until 2052 and to pay 78 percent of promised benefits after that.

  The President has made such assertions before. What made his repeating them in his press conference particularly egregious is that he opened the press conference by pledging: "As a matter of fairness, I propose that future generations receive benefits equal to or greater than the benefits today's seniors get." The President was proposing that benefits for future retirees be no lower than benefits for today's retirees, adjusted for inflation. *But if nothing is done and Social Security goes insolvent — or goes "bankrupt" or "broke" in the President's words — it still will be able to pay benefits greater than today's benefits in inflation-adjusted terms*. In other words, the standard that the President promised to protect for future generations, as though this entailed action on his part to shore up the system for the nation's workers, is a standard that Social Security would meet even if it went "broke." It is doubtful anyone watching the press conference would understand this, unless they were a Social Security expert.

  Furthermore, in a speech on May 3, the President declared that if Congress does nothing, "you're either going to have to raise your payroll tax...or cut benefits dramatically by 30 percent." The President is using a double standard here. When speaking of his own proposal, future benefit levels are compared to today's benefits adjusted only for inflation, *not* to the benefits that are scheduled under current law. But when speaking of the current Social Security system, the standard shifts; suddenly, the comparison *is* to scheduled benefits. Use of this double standard obscures the fact that many future workers would be subject to a *larger* percentage benefit reduction under the President's plan than under a "do nothing" scenario.

- The President also asserted that "the Social Security trustees have estimated that every year we wait to solve the problem…costs about $600 billion." This is a distortion of what the Trustees reported. It is true that the dollar figure that this year's Trustees' report shows as being the size of the Social Security shortfall when the shortfall is measured into eternity (i.e., over an "infinite horizon") is over $600 billion larger than the figure shown in last year's Trustees' report. *But that is largely because this year's figure is expressed in 2005 dollars and last year's figure was expressed in 2004 dollars.* The dollar declined in value over the last year.

  That the President's intimation that the shortfall grows dramatically larger each year we wait is a distortion can be seen by examining a more relevant piece of data from the Trustees' reports — the size of the shortfall when measured as a share of the economy. For the cost of addressing the Social Security shortfall to be growing significantly larger with each passing year, that cost must be increasing as a share of the economy. It isn't. The Trustees' report shows that the size of the shortfall, measured as a share of the economy, is *the same* this year as it was last year. The $600 billion figure is largely a reflection of expressing the shortfall in less valuable 2005 dollars than in more valuable 2004 dollars. In other words, the President's $600 billion assertion is a bit of statistical legerdemain.

5. Portraying the private accounts he is proposing are merely what Congress has already provided for itself.

The President declared that "Congress felt so strongly that people ought to be able to own and manage their own accounts, they set one up for themselves. You've heard me say, I like to say this, if it's good enough for the Congress it is - - it ought to be good enough for the workers, to give them that option."

What the President is proposing, however, is not what Congress has. The investment option that Members of Congress and other federal employees have, under which they can put money for retirement into investment accounts through the "Thrift Savings Plan," is *in addition* to Social Security, not in place of part of it. Members of Congress who take this option do not have their Social Security benefits reduced in return.

This Congressional option is akin to the 401(k) plans that many private employers offer, not to the private accounts the President is proposing, under which Social Security benefits are reduced substantially for those who elect the accounts.