

President's Commission
to Strengthen Social Security

*Monday,
June 11, 2001*

Held at the
Willard Inter-Continental Hotel
Washington, DC

Audio Associates
9537 Elvis Lane
Seabrook, Maryland 20706
301/577-5882

PRESIDENT'S COMMISSION TO STRENGTHEN SOCIAL SECURITY**Commission Members**

Chairman, Richard D. Parsons
Co-Chairman, The Honorable Senator Daniel Patrick Moynihan
Samuel Beard
John Cogan, Ph.D.
William E. Frenzel
Estelle James, Ph.D.
Robert L. Johnson
Gwendolyn S. King
Olivia S. Mitchell, Ph.D.
Gerald L. Parsky
Timothy J. Penny
Robert C. Pozen
Mario Rodriguez
Thomas R. Saving, Ph.D.
Fidel A. Vargas

Commission Staff Members

Charles (Chuck) P. Blahous
Jeff Brown
Steve Goss

DFO, Social Security Administration

Michael Anzick

I N D E X

	<u>Page</u>
Closed Session (Summary of proceedings in meeting minutes):	
Michael Anzick, Federal Advisory Committee Act Briefing	
Randolph Gaines, Ethics Compliance Briefing	
Commission Members Sworn In	
Opening Statements	32
Interim Report Development	66
Motion	106-107
Staff Availability Period for Commissioners to Request Additional Information	107

Keynote: "---" indicates inaudible in transcript.

M O R N I N G S E S S I O N

(10:55 a.m.)

Opening Statements

MR. PARSONS: If we could bring this to some semblance of order. Boy, I tell you, this group came to order so fast I figured it would take me five minutes at least. First of all, my name is Dick Parsons, and along with The Honorable Daniel Patrick Moynihan I am privileged to be one of the co-chairs of this commission. The Senator and I flipped a coin this morning and I lost, so I got to actually chair the first commission meeting. He gets the second, third and fourth. Kind of like draft picks.

(Laughter)

MR. PARSONS: Welcome. We are doing our best to operate in the sunshine. We couldn't actually have it outdoors, but this approximates. So we welcome the members of the public and obviously the press.

In a minute we are going to officially kick off by having each of the commission members introduce themselves to the public and give a short opening statement. We are going to wait before we start that, because I'm told that the folks with C-SPAN have requested that we not get officially launched until 11:00 o'clock, and I wouldn't want to deprive anyone of their hour in the sun. But just so that those of you who are here today know kind of what the order of march is, we will probably spend the

next hour or so hearing from all of the commission members in terms of their preliminary thoughts regarding the responsibilities of this commission and the way we should undertake them and the importance of what we are trying to do. We Obviously, the rest of you are going to have to fend for yourselves.

We will reconvene at 1:00 o'clock where we will begin to discuss the nature and substance and the tone and style of the interim report that we are required to publish under the Executive Order setting up the commission. So that should be interesting, and not only will we talk about the problem but the ways in which this commission is going to be evaluating suggestions, proposals, alternatives for dealing with those problems, including the alternatives that will be proffered up I'm sure over the course of time by the interested public. The sure that everyone has a full sense of both the scope of the problem and the nature of -- their information requests are communicated so we get all that information back. The public is obviously invited to audit that as well.

So having said all that, again, I would reiterate on behalf of Senator Moynihan and the other commission members our welcome to you. We are pleased to formally get started. I thought what I would do is I'm going to forego my opening statement, which was devastating good I must say.

(Laughter)

MR. PARSONS: It will be on the record for any of you

who want to visit the commission's office on Jackson Place and read it. Instead, read to you a letter, and this is more for my fellow commission members, that we received this morning from President Bush:

"To the members of the President's Commission to Strengthen Social Security, today you begin the important work of strengthening and reforming America's social security system. For over 60 years social security has provided a secure retirement for our seniors and the promise of a secure future for young workers. Through the work of this commission, we will develop the reforms necessary to keep these commitments to the American people.

"I am confident that we can restore social security to sound financial footing, protect all the benefits of today's seniors, build wealth for low-income workers, and transform the United States to a nation of owners and savers. Yours is an important task, and I have faith that you will carry it out in a manner that will honor our commitment to today's retirees and strengthen it for future generations of retirees. Signed, George Bush."

So with that as the opening ---, let me turn to my co-chair Senator Moynihan who has a few thoughts, and then we'll go right around the table. I would ask each of the commissioners to speak into the microphone and introduce yourself before you give

your opening statement. Senator.

SENATOR MOYNIHAN: Mr. Chairman. I am Daniel Patrick Moynihan. I am the co-chair of this distinguished group and happy to speak for the first time to it, to speak to our first task, which is an interim report setting forth the situations we have to deal with, the problems we have to solve, because one of the first facts of our situation is that we do have a problem, and that is to say that by the year 2016, as our distinguished actuary will attest to us and the trustees have previously -- have recently confirmed, by 2016 our present system, for the first time ever in any consequential way, begins to run short of cash flow, and that has to be attended to. The question is, who is aware of and concerned about this matter?

I have a short story. In 1994, and Bill and Tim will recognize the setting, I called up on the Senate floor legislation to reestablish the Social Security Administration as a free-standing agency. It had begun as such in the 1930s, then had been shuffled about from one general purpose organization to another and slowly disappeared down into the depths of the Health and Human Services, and had not the visibility that it had once had and which it needed. I had a Bill to do that and some other things.

It was early mid-morning. There was no one else on the floor particularly. I was on my own, and I took the occasion to discuss at length the fact that, you know, social security is a sound system. We have had it in place since 1935. It had never

been a day late or a dollar short, that persons who were now working would have it when they retired, and that we should make what changes might be necessary to ensure that, but those were doable and that we are going to do them.

Then I realized something very strange was going on in the Senate chamber. The clerks at the desk were listening. They never listen. They have other things to do and they have heard it all before, but they were sitting there listening to me, and so I put in a quorum call. I asked them all to come down to the well in the Senate. I said now look, don't deny it. I caught you. You were listening. Well, yes, they were. You were listening because you had never heard anybody say that you would get your social security. We call them clerks, but they are all graduates of Georgetown Law School. Yes, this was a new thought to them. Here these people at the center of American government are little aware of this reality.

One of the things we did with the new independent agency is we began to send out once each year a statement, the social security statement, telling individuals that -- workers that we knew their name, we knew what they'd made, we knew what they contributed, if they continued for another -- until age 65 this is about what they would get. They never heard from the system previously. It was just -- and there was a bureaucratic aspect that the people running knew you were going to get it so it didn't really that much matter to them that you didn't. Well, of course it does matter in a democracy.

I would pick any number of members of our commission -- well, I could ask our three distinguished staffers, you have received now a social security statement, have you not?

(No audible response)

SENATOR MOYNIHAN: Raise your hands.

(Show of hands)

SENATOR MOYNIHAN: Yes. See, you young people. So you know that we know your name, and that I think has begun to change the degree to which the public recognizes that this is a real system, and that if it has real problems, they can and ought to be fixed, and that is the purpose for which our President has given us -- has assigned to us the marvelous idea that we could become a nation, as he put it, "of owners and savers." A large enterprise as noble as the one in the 1930s, and I hope, Mr. Chairman, that we can carry it out.

DR. MITCHELL: Good morning. My name is Olivia Mitchell. I am delighted to be here. Chairmen Moynihan and Parsons, fellow commission members, and ladies and gentlemen, the U.S. social security system faces to my mind what are alarming financial problems that adept action can do much to alleviate.

As Senator Moynihan has noted, by 2016, which is only 15 years away, annual social security payroll tax revenues will not be adequate to cover currently promised benefits, requiring Congress to either alter benefits or come up with more revenue.

I am a baby boomer, and under current benefit rules, by the time I reach 66, social security will need to take in 50

percent more financing than now. By my 100th birthday, which I plan on seeing, either those workers supporting me will have to pay about 80 percent more in current tax revenue, more in tax revenue as compared to now, or my benefits will have to fall by a third or perhaps more. Furthermore, the aging baby boom will have additional demands on tax revenue by Medicare, Medicaid, SSI, DI and perhaps other programs.

I view these prospects with considerable professional and personal alarm. As an economist, I am concerned that last minute changes in the program will have undesirable economic, political and social consequences. As an aging American, I believe that reforming the system now to make benefit promises sustainable in the future is essential to increase economic security.

I believe we have two tasks as members of this commission. First, and perhaps most importantly, we have an educational mission, to do the very best we can to alert the American public about this system's financial challenges and to explain how alternative reform scenarios might work. Second, we have a design mission. We have been charged with the task of formulating a specific plan that will restore financial and fiscal soundness to America's retirement security. Our commission has the duty of proposing a new design element in social security, namely an individually-controlled personal retirement account.

As we begin to evaluate the options, I will urge us to

focus on two issues, at least initially: first of all, how risk and return are valued in social security reform plans, and second, how the individual account design is structured so as to affect administrative cost and retirement security. Important benefits can flow from establishing funded individual accounts invested in real assets. About half of the U.S. population today holds no stock in its retirement portfolio, and many of these people I believe would find appealing increased retirement saving in a diversified social security investment account.

Additionally, the fact that these would be owned by system participants and not counted as part of the federal budget should help, in my mind, should help preserve the funded aspect of the program that emerges.

I believe that the design of the reform plan matters critically. As we begin our work, our group's deliberations regarding social security redesign proposals should therefore keep in mind three points. First, reform plans that permit asset diversification into stocks and bonds will involve risk and return. These should be factored into the evaluation and compared with the risk and return from our current system. Second, reform plans that build assets will require additional revenue and/or reduced benefits. Third, designing an individual account system demands detailed attention to administrative costs and service performance benchmarks.

I am honored to serve as a member of this body, and I look forward to our work. Thank you.

Audio Associates
301-577-5882

SENATOR MOYNIHAN: Well said.

MR. PARSONS: Bill.

MR. FRENZEL: Thank you, Mr. Chairman. I am Bill Frenzel. I am a guest scholar at the Birkings Institution. I am a recovering congressman having gone straight to 1991. There's lots I don't know about social security. There are a few things that I think I know, one of which is: a way we can guarantee to do the system a great deal of harm is not to do anything. The second of them is that the sooner we begin to make whatever repairs we're going to make in the system, the easier it will be on all of the contributors and participants. With that, Mr. Chairman, I am anxious to learn from all of you.

MR. PARSONS: Bob.

MR. JOHNSON: My name is Robert Johnson, and I am delighted to be a member of the commission. I look at this problem from the eyes of a business person. If it were a business problem, you would see it simply. You have less revenue and more costs than you could sustain, and you have to solve that problem. If we put our head in the sand and assume that the problem will go away, we will be faced with a crisis of tremendous proportions that will affect every American.

I also look at it from the standpoint of an African American who understands that African Americans are totally underrepresented in the portion of wealth that's generated in this nation. I see the potential for investment in personal retirement accounts as a way of bringing African Americans into

the mainstream economic benefits of the society while at the same time maintaining the fundamental benefits that social security has promised since its existence.

I also recognize that African Americans have lived -- have a higher mortality rate than the general population, therefore contributing more but receiving less from social security, which also creates an imbalance in their ability to have their heirs and their families benefit from their contribution.

Obviously, these are problems that must be solved in the context of all Americans, but I have a particularly unique perspective on it, and I intend to voice those opinions in the commission. Thank you.

MR. BEARD: My name is Sam Beard. I am honored to be on this commission. I approach it with three principles. One is that social security is the most effective and best government program ever created. It is essential to save it. Part of saving it is to save the guarantees of benefits flowing to retirees. The charge against individual accounts is: don't give up a guarantee for a gamble. It is essential that we save the guarantee. The next charge against the direction is social security is social insurance. It has disability insurance. It has survivors' benefits. Those elements of social security are essential, and no plan can go to undercut those.

On the positive side, my whole background -- I had the privilege of working with Senator Robert Kennedy starting in the

mid-60's, and my whole lifetime has been "economic opportunity."

I sit afraid that we're becoming two separate societies. One of the big dividing points is those with financial assets and those without. Half of our American society has less than two percent of the financial assets. That's unacceptable.

So here we have a chance to save the best federal program ever created. We all agree coming from the actuaries, the degree of seriousness of the financial imbalance, which totals in excess of \$25 trillion. Something has to be done, but out of a problem we have an opportunity.

MR. VARGAS: Good morning. My name is Fidel Vargas. Contrary to what many people want to believe, I'm actually glad to be back and serving on this commission, as I was a member on the previous advisory council on social security back in 1994.

As a former mayor of the City of Baldwin Park, a resident of Baldwin Park community, that of working class people where social security is an integral component of their retirement, this issue is very personal and something that I see on a daily basis.

My context that I will bring to this commission also includes other personal aspects. My parents, for example, both union members, both less than 10 years away from retirement, and both making sure that they told me yesterday at our barbecue where we were watching the Laker game to make sure that I took care of them. Seven brothers and sisters, five sisters and two brothers, youngest just completed her sophomore year at Berkeley,

the rest teachers, accountants, financial analysts, and also very concerned about their and their children's financial security and social security retirement. Then there's my wife and our friends, the young generation or the Generation X, as we've been known, who are very concerned, as the Senator pointed out, about the viability of the system and trying to make sure that we do something to fix it now. Finally, my children and their friends and all the children in this country. When I started in 1994, I had two children ages 5 and 2. Now I have three children ages 11, 8 and 6, and nothing has been done since then.

As has been said earlier, the sooner that we are able to find a solution or to come up with some ideas that can be implemented, the quicker that we'll be able to deal with this problem. So I am glad to be a member and looking forward to contributing as well as learning from each and every one of you. Thank you.

DR. SAVING: Good morning. My name is Thomas Saving. This is a problem that I've been addressing for the last decade or more. I think the problem is best summarized by looking at the debt that's implied by -- among all those who are currently eligible to receive social security or are now receiving it.

If we look at the value of that debt, it's some \$14 trillion, and that's compared to a publicly held debt of only \$3.5 trillion. If we add to that the other two elderly entitlement programs that we have, and that's part A of Medicare and part B of Medicare, the total of that debt is \$39 trillion.

This is a number that we are going to have to pay. This is not like the regularly publically held debt that we never actually have to pay. This actually is going to come due. These elderly people are going to retire. They are going to use -- to drive real cars. They are going to live in real houses. They are going to eat real food. They are going to use -- and all that has to be produced by the United States by the gross domestic product. That's all we have to work with.

If the elderly consume more, the workers have to consume less. There isn't any other way to do it. The only solution to this problem is to find a way to change the capital stock of the country, to increase the gross domestic product, because otherwise the children, Fidel's children, are going to have to eat a lot less than we do, because the old people are going to be eating a lot more.

We can solve this problem, and we have to try to solve it. If we leave the problem unsolved and the federal government stays the same size it is now, which is one-fifth the gross domestic product, by 2070 these three programs will be 100 percent of the federal budget. That obviously cannot happen. It will not happen, and that means either these programs will be gone or the federal government is going to be an awful lot bigger. We can do something about it, and the time to do something about it is now. Thank you.

MR. RODRIGUEZ: Good morning. My name is Mario Rodriguez --- round table, and I commend President Bush for

taking the task of putting this commission together, because it's so important to all Americans and in particular the Hispanic community. The Hispanic community has -- a small percentage of the Hispanic community puts money into savings, and I feel that this is a way to really open up their eyes and hopefully have something for the future.

My daughter Ashley asked me when I was coming up to -- out here, "Dad, what are you coming out here for?" And I said, Ashley, I'm coming out here to -- hopefully we can come with some recommendations so there will be social security there for when you are ready to retire. So I commend President Bush for putting this commission together, and I'm honored to be here. Thank you.

DR. JAMES: Yes. You're not speaking? I'd like to hear what you guys have to say. I'm Estelle James and I'm also very pleased to be on this commission. After working on social security reform in other countries, it's nice to be doing it in my own country.

I think everyone in this room, both the commissioners and members of the press and public, all agree that social security is in a state of financial imbalance. By the time my children retire, social security will only be able to afford 70 percent of the benefits that have been promised to them. So the system has to change. I mean everyone agrees that there has to be some kind of change in the system, and the question is what kind.

As I think one of the other commissioners mentioned,

this problem really presents us with an opportunity to improve the system. After all, we've had this system now for 65 years. We've learned something about how social security systems function. We've learned from the experience of other countries.

So in the process of changing the system, we should be able to put in place mechanisms that actually work better. That's going to be one of my goals on this commission.

Let me just mention four criteria that I think are important in terms of evaluating whether a system is better or not. First of all, it must be sustainable, obviously, because it's not going to provide security for people if it is not sustainable. Usually sustainability has been measured in terms of the 75-year time horizon that the Social Security Administration uses, but I think we should also be thinking beyond there in terms of automatic stabilizing devices that maintain the sustainability even beyond the 75-year time horizon.

One problem with the 75-year time horizon approach is that when you move one year into the future, things that seem to be sustainable a year ago turn out not to be sustainable. Conditions change in unexpected ways, and it would be nice to have some mechanisms that enabled the system to respond in automatic ways. So that's one of the things I think we should be thinking about.

Now, a second criterion that I think is important is what is the impact of the system on the broader economy.

Ultimately, the best security for workers and for older people

comes from a growing economy. If you are going to have more and more older workers, many of whom are not working, this is going to have a negative impact on the standard of living of everyone in the economy, workers and older people, unless we have economic growth, unless we improve the productivity of labor. So I think we should be looking at systemic changes that will have a beneficial effect on the broader economy and on economic growth.

Here we have to look at things like the impact on national saving and capital accumulation, the allocation of that saving, the impact on the labor supply of older workers and the work effort of younger workers. So I think that's a key criterion that we should keep in mind.

A third criterion has to do with equity, with the distribution of the benefits and costs, and we always have to keep in mind that different groups benefit differentially from our current system and from changes that we might make. So I think we should look carefully at who is going to be paying the price and who is going to be getting the benefits, and in particular, I think we should be concerned about the bottom half of the population and make sure that they are protected by a social safety net. That is the group that we should be redistributing to, and that is the group whose lifetime benefits from social security should exceed their contributions. So that's something I am going to keep my eye on, and I'm sure that the staff will be giving us data on the impact of high and low earners, of men and women, and distinguished by marital status as

well. I think it's very important to look at how each of these groups might be changing -- might be affected by any changes that we contemplate.

Fourth, the final point that we should keep in mind, is we should try to avoid the excesses of political risk and financial market risk. Now, under the present system people are subject to very great political risk, so the very fact that we know the current system is not sustainable, so people are either going to be hit by cuts in benefits or increases in contributions. So that's a very risky position that workers today face.

Now, if we invest money in the financial market through individual accounts, people will then be subject to financial market risk, and I think we have to design the system in such a way that the extremes of that financial market risk are avoided.

The key to avoiding risk, whether it's political risk or financial market risk, is diversification, diversifying retirement income sources, and if you have savings, diversifying your asset mix. So those are some of the criteria that I'll be keeping in mind and I hope the whole commission will be.

MR. PARSKY: Thank you. My name is Gerry Parksy. I was former assistant secretary of the Treasury in 1974, and I'm in a private investment area now.

First of all, I want to thank the President and the co-chairmen for allowing me to participate in this important effort.

I think that, as someone has said, the social security system is

our most important government policy and program touching all American lives.

I step back and just look at a couple of points I think I would make, not to repeat what is already said. I think as we engage in this effort, I think it's important that we try to come forward with something that will constitute real reform. Too often a part of government policy making and to some extent the way the private sector participates, we wait for a crisis to be on us before we act. Those of us in California understand that in the context of energy right now.

Now is the time when we can anticipate there are real problems with respect to our social security system. Therefore, now is the time when we should embark on putting in place real reform, not wait until whether it's 2015 or 2038. In this town that we're in, often people will say well, why do we have to deal with this issue now, it's going to be okay until 2038. I think one of the jobs hopefully of this commission is to alert people, the public and those that are involved in the political world, of the importance of putting real reform into place now.

Second, I think that solvency of the system should not be our focus. Our focus should be on real reform, because just allocating a certain number of dollars that will in effect prop up the system for a period of time I think would be the wrong focus for us now. We have an opportunity to create real reform and reform that will not be just focused on whether the system is solvent or not.

The third point I'd make is that having spent a lot of time in the market place, both in the government and the private sector, debt markets and equity markets are not to be feared. There is a risk reward associated with any form of investing, but I think it's important to properly assess that risk and not automatically look at one moment in time when the stock market may have gone dramatically down or dramatically up. This is a system that needs to be reformed for the long-term, and as we look at personal savings accounts and we look at the prospects for defining what ground rule should be established, I think we should bear in mind historically what happens in both the debt and equity markets.

Finally, I would just say I hope we don't shy away now both from recommending real reform and convincing the political establishment, one, that now is the time for reform. I think our President has been quite courageous in addressing an issue that most people would say don't address at this point in time or don't address at all. I think we have an opportunity to change that focus and bring about real reform.

MR. PENNY: My name is Tim Penny. I'm a senior fellow at the University of Minnesota Humphrey Institute. Like my friend Bill Frenzel, I too am a recovering politician, and like him, I represented in Congress the State of Minnesota, I in the Democratic Party, he in the Republican Party.

I am going to state the obvious, but there are three criteria that typically apply when public policy makers are asked

to address difficult issues like social security reform. The first is that there has to be a general sense of urgency about the need for reform. Our co-chairman Senator Moynihan played a key role in developing the 1983 social security reforms, but we were in a period of crisis at that point, and very often we wait until the crisis hits. This time we do have the advantage of a growing public consensus that reform is needed. When the Social Security Administration and other sources articulate time and again that by the year 2016 we will face a cash flow crisis in the social security system, that begins to sink in with the public, and there's a growing awareness that it's best to act sooner rather than later.

There's also a sense of urgency upon the part of younger Americans. Most opinion surveys demonstrate that younger Americans have little if any confidence in the current social security system, and I can say from own experience having been named to this commission that invariably when I encounter those under 50 years old, they say be bold, because they understand that the current system is not a system that will return for them the kind of benefit levels that it is providing for their parents and grandparents.

The second key factor in accomplishing reform on an issue of this magnitude is presidential leadership. In this instance, we need to recognize and acknowledge the leadership that President Bush has afforded us on this matter. He made this a central element of discussion during the campaign and then

since tried to bring the American public along on this issue. He laid forth several valuable principles that should undergird the work of this commission as we develop recommendations for reform, and he put a six-month or less time limit on the work of this commission as a way of indicating that he believes that there is some urgency to act sooner rather than later.

The third factor is bipartisanship. You cannot tackle an issue of this nature, of this sensitivity, without some degree of bipartisanship. Ultimately we need that. We need a degree of bipartisan support within the Congress. The President has moved in the right direction by establishing a commission evenly numbered between those who identify themselves as Republicans and those who identify themselves as Democrats, and yet there's diversity of opinion within this group. We are all comfortable with the principles the President has laid forth, but there's a certain degree of diversity.

For my own part, I come from a family in which my mother lives on social security and nothing else. I come from a family in which my youngest brother is totally disabled and relies on a disability check. So I understand the insurance nature and safety net nature of the current program, but I also understand as the father of four children, three of whom are in college and one who just finished ninth grade, that this younger generation is not well served by the current structure of the system, that they will get an increasingly unfair deal under the current system, and for that reason intergenerational equity is

best served if we can address this system now and enact changes that provide a better guarantee for future retirees.

Our recommendations to President Bush must ultimately result in a report that assures the sustainability of and confidence in the social security system for the longer term. That is a tall order, but it is the order of the day and I am honored to have been asked by President Bush to play a role in this endeavor.

DR. COGAN: My name is John Cogan. I'm a senior fellow at the Hoover Institution at Stanford University. Social security is the most important social invention of modern times.

For over 65 years it has alleviated poverty among millions of Americans. It is in good financial condition right now. It is able to pay all of the benefits to current retirees. But it is facing enormous financial problems a short time down the road. The problems don't start in 2038; they start early in the next decade. The commission's job, which is to develop a reform plan that's consistent with the President's principles, is an awesome responsibility. The time we have to do the work is short, but the time to address the problem is now.

The key element of the President's reform plan is personal accounts. These accounts will enable individuals for the first time within social security the opportunity to build real wealth and financial security. But this key ingredient is not the only ingredient to reform. Other steps have to be taken.

I am flattered to be part of this group. I've worked

with some of you in the past on policy issues inside the government. I have learned much from the work that others of you have done in researching social security, and so I look forward to this chance to move the ball to the next stage and develop a plan that the Congress will regard as an acceptable plan, but more importantly, develop a plan that the American people will regard as sensible reform. Thank you, Mr. Chairman.

MS. KING: Good morning. My name is Gwen King. I am the president of Podium Pros, the Speakers' Bureau here in Washington, D.C., and in a prior incarnation I was privileged to serve as the eleventh commissioner of the Social Security Administration. One of the things I learned at Social Security was that there are a lot of good, smart people working on this problem, not the least of whom of course is our current co-chairman Senator Moynihan, who was wise enough way back in those days to insist that Social Security devise a way to notify people regularly, every year, about their status at Social Security. He was modest in telling you that you receive an accounting; he was responsible for that. And what we learned is that people can pick up that accounting and read about their own history with Social Security. Everyone who works has a history. They feel an ownership for that program, so you can imagine how devastating it is when people are actually sitting here fearful that their benefits will never come to them.

So I, too, thank the President for putting this commission together, and I really am appreciative of his asking

me to serve on it. Co-chairman Parsons at one point commended the President on his courage in facing this issue, and I think we all learned a lesson from the President when he said, you know, it really takes more determination than courage. I think the determination that we bring to this task will ultimately decide how effective we are in preserving this critical program.

I would simply like to urge my colleagues to keep in mind several things that you may not think about when we start to look at all the actuarial tables and all of the issues surrounding the economics of social security.

The first thing is that we have to speak plainly. We have to be very clear. The report we produce simply has to be readable and understandable, so that we do not run the risk of having everyone who does not support this approach begin to interpret the report for us. In government we have a tendency to speak in jargon. We assume that everybody knows what PIAs are. We assume that everybody knows what FICA means. I think it's time for us to be very clear that when we talk about Old Age Survivors and Disability Insurance, we make it clear that we're not talking about O-A-S-D-I, or when we want to talk about the various --- income, we shouldn't revert to jargon and talk about "AIM." We should be clear about what we're saying. I think if we do that, if we take the time to put definitions to the terms we use, nobody can misinterpret what we say. We can be very clear.

The second thing I think is important is that for the

vast majority of people who might be receiving these personal savings accounts for the first time in their lives, it would be very, very important for us to take the time to counsel them, to let them know what this whole program is all about, to spend the money if necessary to make sure that they understand what their own risk tolerance is. After all, if we go to some organization to invest our money for us, that's the first thing they sit down and try to tell us about. So we need to make sure that people aren't feeling uncertain about what it is that might be offered.

In fact, if there are options, we ought to be clear that they are not required to take any step but that these are options for them.

I think it's going to be very important for us to look at the most vulnerable people in our community, people who stand to lose a lot, as Estelle talked about, winners and losers. There are some clear winners and losers with regard to this program, and we need to make sure that we protect women as a group who rely so heavily on social security, minorities, who, as Bob Johnson pointed out, may not live to get the maximum benefit from the Old Age Program but who very often are blessed to have social security as survivors and cover their families and their children when they meet an early demise.

I think we need to be very clear on what this commission's responsibilities are, that we, when we say that the commission will take an action, that we have decided to do that.

And for all of us, that's going to mean a real commitment of

time. We should make that commitment, we should dedicate ourselves to this task and not leave it in the hands of the very, very competent and able staff, but if we're going to step up to this task, we ought to understand everything that we put into a report so that we will feel comfortable standing behind it.

So, readability, be clear on definitions, protect people who are vulnerable, protect people who rely on the system, spend the time making sure that we counsel the people who for them some of these things that we're talking about may be foreign terms, but we need to take the time to make sure they understand it, to make sure that we try to avoid any adverse impact on families and people who are vulnerable. Then finally, I think we need to screw up our courage and move forward. We cannot be deterred by all the people out there who are going to be critical, who are just waiting to lob in incoming missiles on whatever it is we produce.

We have a task. We have a 15-year lead time before we begin drawing down trust funds, and we have about a 37-year lead time before social security falls off the precipitous cliff. I think, Mr. Chairman, we have our task before us. The time we take over the next 6 months will be important time, and I am absolutely delighted to be a part of this effort to make sure that we continue this critical program that has supported my family, all of our families, for the last 60-odd years. Thank you.

MR. POZEN: My name is Bob Pozen. I'm currently vice
Audio Associates
301-577-5882

chairman of Fidelity Investments, so I've publicly announced I'll be retiring at the end of the year and teaching at Harvard next year. I, like the others here, am honored to be chosen to serve on this commission. I believe strongly, as Sam stated, that social security is one of the most successful, if not the most successful, government program in the history of the United States, and that's exactly why we need to strengthen this program and make sure that it's sustainable.

I believe that the commission's initial task has to be to educate the public on the long-term issues involved with the financing of social security. Since I was appointed to the commission, many people have come up to me, and I'm amazed by the lack of understanding and the confusion that surrounds this subject. I think we have a great opportunity in the initial report and in other documents to educate people.

Now, the fact that social security is a long-term problem, that's the good news. The good news is because we do not have to touch retirement benefits of anyone who's in retirement or near retirement. I should emphasize that in the President's Executive Order he states specifically that modernization must not change social security benefits for retirees or near retirees, so that those people who fear that this is somehow going to be a problem for them if they are in retirement or close to retirement, that's just not an issue. Instead, as a number of people have said here, since this is a long-term issue, we can make small changes soon that will have a

great effect over a long term. This is the beauty of having a 30-year problem, that if you can make small changes, that over a period of 20 or 30 years it can help the next generation.

On the other hand, there are no easy solutions. I think that when you look at private accounts, you have to look at them relative to the other solutions. I don't think that there's probably a lot of people who want to raise payroll taxes, and there aren't a lot of people who want to cut benefits dramatically, and there aren't a lot of people who want to create a huge budget deficit. So we have to realize that there is no free lunch here. There are no easy solutions, and when we look at private accounts, we have to look at them relative to other approaches that could be taken. And when we look at private accounts, I think that it's important, as Olivia mentioned, that we look at how they are designed, whether they are practical. I would add to Estelle's criteria, practicability or workability, since I think those are very important considerations.

So in the end I think we come back to education. We come back to some of the things that Gwen is saying. We have to have a report here that will explain the problem so that most Americans can say yes, I understand this is a problem, and then can also explain whatever solutions we come up with in simple language that everybody can say well, I can see there aren't a lot of easy solutions but this is a quite reasonable one given the circumstances, and I can understand that these are the sorts of things that are going to be done and these seem reasonable to

me. If we can convey that in simple terms and have people understand that, then we can build the consensus that we will need to actually put this reform program into place. Thank you.

MR. PARSONS: Thank you, Bob. Yes, I think everyone spoke both from the heart and from the head at the same time. I want to introduce also, because I was remiss at the outset in not doing so, our Executive Director Chuck Blahous. I do that for two reasons. Number one, he is really going to be the work horse supporting this commission in pulling together all of the analyses and data and options that we're going to be evaluating over the course of time, and number two, so that any of you who have real bones to pick can go to Chuck and leave the rest of us alone. So Chuck, on behalf of the commission, we're grateful to you and the staff that you're putting together and look forward to working with you over the course of the next several months.

Everything has been said around this table about both the importance and the determination of attacking this problem. I would just like to before we take a break echo one thought which Bob expressed at the end and others of you along the way.

It's easy to think when you get into the hothouse of the Beltway that, well, everybody knows social security needs to be reformed and it's just a question of when and how. Those of us who live outside the Beltway don't necessarily share that view. I am not even sure it rises to the level of confusion about social security. Many people just draw a blank. It's

something that my grandmother gets or something, but they don't know what FICA is. It's just another thing on their payroll slip that means they don't get their money.

One of our real challenges is going to be to shine some light on the nature not only of the system, the benefits that it promises to present Americans who are retired and future generations that will retire, but why the system is structurally broken, why it cannot work anymore in the way in which it's set up, and to have people gain an understanding of what the problem is before we get bogged down in what the solution is going to be.

There are a number of people who have already begun to attack the work of this commission even though this is our first meeting, and they're out sort of rattling their sabres and threatening -- or charging us with committing all sorts of mayhem upon retired Americans or disabled Americans or future generations of Americans, when we haven't proposed any approach to the problem yet.

I think the first thing we need to do is help develop around the country and not just inside the Beltway, an understanding of the system, its structural infirmities, and get some discussion around that before we then tackle construction of solutions to those structural infirmities. And that, ladies and gentlemen, is what we're going to start talking about after the lunch break.

As we've thought about our work, we're going to divide it in two parts. First part will be an interim report which

really does come out and talk about the problem, what is the problem and why is it important to Mr. and Mr. (sic) Joe Citizen, in language hopefully, Gwendolyn, that will be understandable to Mr. and Mrs. Joe Citizen and that the press can convey in fair and balanced terms, so that we don't cause fear, we don't cause concern on the part of people who are currently retired, but we do cause awareness on the part of people who will retire some day. That interim report will be the subject of our discussion when we return from lunch.

After the interim report is out and later on in the fall, we hope to open the process to those members of the public who have been thinking about working on this problem to share some of their ideas and thoughts with us and to have some deliberations around this table about our own ideas and thoughts, but --

SENATOR MOYNIHAN: Mr. Chairman, could I ask, did you suggest that we would have a public hearing at one point?

MR. PARSONS: Again, as a commission we haven't formally addressed that issue, but I think the two co-chairs are of the view that this is a process that needs to be characterized by a number of things, but certainly one of them is openness and accessibility and availability to hear what people who have been working on this problem for years have to say, and to take their input as well as develop our own thoughts and ideas. So my disposition, Mr. Chairman, is yes, we should, but we need to as a commission sort of wrestle with that.

DR. JAMES: Yes. I think it would be a good idea for us to talk about it perhaps in the afternoon or the next meeting about the best way to get input from the public. A public hearing is one way, and then there are other ways, such as taking written submissions. I thought a little bit about what I think might be helpful to me; that is, I think it might be useful if we posed specific questions and requested people and organizations to submit their answers, so that we could actually get ideas that could be constructive that would help us grapple with specific issues that we're thinking about. And that might also be more expeditious than simply a series of public hearings. It's not an either-all situation, but it's another way --

MR. PARSONS: Yes.

DR. JAMES: -- to get constructive input.

MR. PARSONS: I think it's a good idea because --

DR. JAMES: I hope we have time to talk about that.

MR. PARSONS: -- as several of you pointed out, we're on a fast track.

DR. JAMES: Uh-hm.

MR. PARSONS: Which means we cannot have sort of endless hearings. We've got a very --

DR. JAMES: That's right. And we all have limited time, but on the other hand, I think we'd like -- it's important to be open to ideas from the outside.

MR. PARSONS: I agree with you, but I do think all of this proceeds from a common understanding at least of what the

problem is.

DR. JAMES: Uh-hm.

MR. PARSONS: And so hopefully we can make some progress on that when we reconvene. Unless any of my fellow commissioners have further contributions, we are going to take a luncheon recess. We'll be back at 1:00 o'clock.

(Luncheon recess)

A F T E R N O O N S E S S I O N

(1:04 p.m.)

Interim Report Development

MR. PARSONS: May we come to order. I'm going to tell you, this is not like New York, where approximately 15 minutes after the first call to come to order people begin to quiet down. Very --- quiet here. Okay. I hope everyone had a at least nourishing repast. We certainly did.

What we are going to do for the next hour or so now is talk a little bit about this interim report that under the President's commission, by charter the commission is required to prepare and which we mentioned a little bit this morning. Chuck, I think what I would do by the way of just putting everybody on the same footing is ask you to kind of walk us through the requirements of the charter and tell us where the staff is at this point in time and what you need by way of commission input to take the next steps.

MR. BLAHOUS: Thank you, Mr. Chairman. The President's Executive Order specifies that the commission shall submit an interim report that will describe the challenges facing the current social security system, as well as the criteria by which the commission will evaluate reform proposals.

What we have done for all of you in your briefing materials is to assemble material that speaks to both of these objectives. Chapter one in your briefing book attempts to describe the state of the current social security system, and

chapter two presents possible criteria of analysis and evaluation for reform proposals.

Let me just say a few words very briefly about the contents of chapter one of your briefing book. One of the difficulties that faces you or anyone else who is trying to describe the current social security system is that the current system is out of actuarial balance. In other words, there is a mismatch between the outlays that are promised from the system and the revenues that are committed to it.

This provides not only an actuarial problem, but an analytical one as well. It's impossible to describe who is being affected in what way if you don't know from where the revenues are coming to pay the benefits that the system would provide. What we have attempted to do is to show you various ways that the current system could play out if no action were taken and no reform were adopted.

The first baseline we've presented to you is reproduced on the chart in the corner over there. That is our best effort to describe the literal consequences of current law. This is what would take place if no legislative changes were made. As you can see on that chart and as has been alluded to by some of the commission members already, in 2016 the system's annual cash payment obligations will exceed its annual revenues coming in from payroll and benefit taxation.

What that means is that beginning in 2016, the federal government would face a series of choices. Lacking dedicated

program revenues that are sufficient to pay full benefits, it would have to find another means of closing the gap. It would either have to raise additional tax revenue, reduce spending either on social security benefits or some other area of the federal government, or increase public debt, borrow the money.

Now, at that time the social security trust fund would still have a positive balance. That means that the Social Security Administration would still have the full legal authority to continue to send out benefit checks, but that authority would expire in 2038, because in the period from 2016 to 2038, the entirety of Social Security's trust fund balance would be drawn down, and at the point where there is no more positive balance in the social security trust fund, the Social Security Administration would lack the authority to write checks. It does not have borrowing authority, and it would simply have to wait until sufficient revenues came in to pay benefits.

SENATOR MOYNIHAN: Mr. Chairman, may I --

MR. BLAHOUS: The effect of such change --

SENATOR MOYNIHAN: Sir, can I just say, when you say the trust fund would be drawn down, there is no stored value as such in the trust fund. These are government undertakings defined revenue, so it would have to come from --

MR. PARSONS: Someplace.

SENATOR MOYNIHAN: -- taxes or borrowing of another kind. There is no "starting in 2016 we are out of money."

MR. BLAHOUS: That is correct, sir. That is absolutely

correct. And while that problem begins in a very gradual way in 2016, as you can see on that chart, the size of those financing gaps becomes extremely large well before the projected insolvency date of 2038. So the --

SENATOR MOYNIHAN: Well, if I just may say, it somewhat misleads the public to talk about an insolvency date that simply means a date on which there are no longer these bonds in the Treasury, which the Treasury has to go out and find revenue for in any event. The insolvency date, sir, is surely 2016. If I'm -- please correct me. I know --- assisting.

MR. BLAHOUS: You are absolutely correct, sir. Whether or not there is a positive balance in the social security trust fund, the government has exactly the same problem. And that problem begins in 2016, which is that annual program revenues are insufficient to pay full benefits.

DR. JAMES: Could I just follow up on this question, because it sounds like there is a distinction between 2016 and 2038. Now, 2016 there's a government undertaking to find the money, there's an obligation; 2038, I think the current law, from what you said, I think the current law says that there is no such government legal obligation. There may be a moral commitment or a political need, but legally at that point, benefits would simply be cut. So that's a kind of distinction between what happens in 2016 and what happens --

MR. BLAHOUS: That's correct.

DR. JAMES: -- in 2038.

MR. BLAHOUS: That's correct. Now, what we have attempted to do in your briefing book is to provide you with various alternative views that could show how the system might evolve under other circumstances.

MR. PARSONS: It might be well just to sort of tarry on this point for a minute, because it's all part of I think one of the big challenges this commission has, which is explaining first --- and then the American people what actually is going on here. As I understand it -- so let me take a cut at that and then invite other members of the commission to add if need be.

Currently, we collect enough under FICA to actually -- enough money comes into Social Security to pay out the benefit obligations that Social Security pays to current retirees, and in fact, we take in a little bit more than we actually need to pay out. That little bit more, which is called a surplus, one of several things could happen to it. Actually, the money could be taken by the system or by the government and put somewhere, what Senator Moynihan calls a stored value. It could be invested somewhere or just put in a bank. But what's actually happening is the government takes the money, uses that money for other non-social security-related purposes and gives a piece of paper back to the social security system saying I owe you X dollars, and in 2016 the amount of money that comes in under those taxes to pay for social security obligations is less than, starting in 2016, is less than the amount of money that has to go out and the system has to now redeem those government IOUs. But since the

government spent the money, in order to redeem the IOUs, the government has to go out and either raise taxes or increase public borrowings, because the money is gone.

So I think Senator Moynihan is right when he says that the real crunch time comes in the middle of the next decade, because we're either going to have to reduce benefits because we don't have the cash flow to make that and nobody anticipates that, or all suffer either a higher tax burden or greater public debt in order to pay out those IOUs. Then we run out of IOUs sometime in the middle of 2035, 6, 7, sometime in that time frame, and at that point in time, the problem compounds itself because we don't even have the IOUs. Now the government has to go out and raise not only the money they borrowed to spend on earlier programs but --

DR. JAMES: Or cut back.

MR. PARSONS: --- new money.

DR. SAVINGS: Mr. Chairman, I think that's exactly why we should try to avoid focusing on insolvency, because insolvency is equated I think too often with this period from 2038 forward, when our problems moves (sic) toward insolvency starting in 2016. So that's why the insolvency issue is not really the real focus.

MR. PARSONS: But I think people need to understand that sooner rather than later --

DR. SAVINGS: Right.

MR. PARSONS: -- something has to give. Either benefits get cut or the government raises taxes --

DR. SAVINGS: Right.

MR. PARSONS: -- in one form or another because the incoming cash won't meet the outgoing requirement.

DR. JAMES: Could I add one point to that, that even before 2016 something else happens, which is the amount of money that's coming from social security to support government programs gets smaller and smaller. I mean, it becomes zero in 2016, but it becomes smaller every year before then. So even before then, if the government wants to maintain that same flow of money to its other programs, it has to find the money from somewhere else through increased borrowing --

MR. PARSONS: Uh-hm.

DR. JAMES: -- or taxation. So the problem really starts considerably before 2016.

DR. COGAN: I would only add one thing to your discussion, Mr. Chairman, and that is besides raising taxes, besides borrowing, the option that the government has, as unpleasant as it is, is cutting non-social security spending. Some attention in the report, in the interim report, to the amount of reductions in non-social security spending might be very instructive for our readers.

DR. SAVINGS: Mr. Chairman, I think an issue that's related to this issue is that if we, and we could do this, Congress could simply do this by running the printing press and printing up more of these bonds, if there was a googol trillion dollars in the trust fund, and that's 10 to the 100 trillion in

the trust fund, or if there's zero, the implications for the federal budget are identical after 2016. It makes absolutely no difference what's in the trust fund, and because of that, we would argue in economics there's nothing in the trust fund, it's simply a promise, and as it impinges, as I pointed out earlier, both with Medicare, Medicaid and this, by 2070 100 percent of the federal budget will be used for these programs. And that's assuming the federal budget grows with gross domestic product and stays a fifth of the gross domestic product.

The point is that the trust fund is irrelevant except in this legal sense, that when the trustees come to the Secretary of Treasury and hand them these certificates, they are required to give us cash and that's only required if Congress requires them to do that, and if it's impinging on the other aspects of the federal budget that are more important at the time, then clearly hard decisions have to be made. But it doesn't change the actual federal revenues in any way. So it impinges on those revenues, and it's important for I think the public to understand what the trust fund really means and changing those numbers, because they can easily be changed and the system can be made solvent in that sense of the word. We can make that trust fund anything we want to. If we want to change the interest payments, which is a suggestion that's been made, change the rate of interest, make it 100 percent a year, we can make this last forever, but we can never actually find the real resources because retired people, as I say, drive real cars, eat real food,

and live in real apartments and use real medical care, and that's real output in the country and that's the only thing we have. We can't change it with writing numbers on a sheet of paper.

MR. PARSONS: Okay. I just thought, and I appreciate your provoking conversation, Senator Moynihan, it would be helpful to talk about that a little, because there's a great source of confusion as to what all these concepts mean, and also from an urgency point of view, there's a big difference between the middle of the next decade and 2038 or whatever. Carry on.

MR. BLAHOUS: Well, as has been indicated here, that fiscal problem develops in 2016 and is not something that materializes only in 2038. Dr. Saving in his remarks said that the only real difference is that -- is really sort of a legal definition of what is happening in 2038, that legally in 2038 the Social Security Administration no longer even has a claim on sufficient revenues. And at that point, as you can see in the chart, the effect on beneficiaries in that year would be a sudden reduction in benefits of approximately 27 percent. From that point forward, if benefits were to be funded from projected revenues, those benefit reductions would gradually increase from 27 percent in 2038 and would gradually become 33 percent in 2075. So even if you assume that the federal government has done something to produce these extra revenues between 2016 and 2038, this would be the consequence for beneficiaries of inaction.

Now --

MR. PENNY: Mr. Chairman, if I could follow on that

**Audio Associates
301-577-5882**

point. Just to clarify, you said that the legal standing of the system at that point would be such that they have no other recourse.

MR. BLAHOUS: There --

MR. PENNY: In law what is anticipated that the Administration, the Social Security Administration will do if we allow ourselves to hit that point?

MR. BLAHOUS: This is an area that is often speculated about.

MR. PENNY: And can we look back on the 1982-83 experience for any enlightenment here?

MR. BLAHOUS: Well --

MR. PENNY: No. I see Steve --

MR. BLAHOUS: -- there were things that were done to carry the Social Security Administration over so it didn't reach the point where they couldn't send the checks out, on a very emergency basis. Now --

SENATOR MOYNIHAN: There were benefit cuts.

MS. : That's right.

MR. PENNY: As part of law.

SENATOR MOYNIHAN: I'm sorry, Tim.

MR. PENNY: As part of law.

SENATOR MOYNIHAN: Yes, sir.

MR. PARSONS: That's right.

SENATOR MOYNIHAN: The --

MR. PENNY: But what I'm asking is, did the

Administration, the Social Security Administration under its own authority --

MR. BLAHOUS: No.

MR. PENNY: -- do anything in the '82 to '83 time frame?

MR. BLAHOUS: No. And in fact, the Social Security Administration does not have borrowing authority. It does not have the authority to write checks without dedicated financing.

MR. PENNY: I just wanted to get that on the record.

MR. GOSS: But Chuck, if I might just add, at that time there was a temporary borrowing authority that was made available.

MR. BLAHOUS: That's right.

MR. GOSS: Amongst the --

MR. PENNY: Under law.

MR. GOSS: Under law. Only under a law can this occur, and amongst the OASDI and HI trust fund, borrowing --

MR. PENNY: So the bottom line is that --

MR. GOSS: -- was temporarily ---.

MR. BLAHOUS: -- that there are no options available to the Social Security Administration unless under law we make those options available.

MR. BLAHOUS: And as a technical sense, the Administration, neither do they have the authority to make the arbitrary benefit reductions that would result on that chart either. They cannot do that. Those projections arise from the

finding that lacking financing, SSA would simply have to delay when checks were issued and the effect of those delays would be to reduce levels by 27 percent.

MR. PARSONS: Bob.

MR. JOHNSON: I have a question. In listening to all of this then, I think the public can conclude that social security is not a right, that there's no -- nothing in the Constitution that says you are entitled to life, liberty and social security. You are only entitled to it so long as the Congress decides that there should be a plan called social security benefits for people where no matter how much you put in, you are not guaranteed a certain amount that you would take out.

MR. BLAHOUS: That is correct.

MR. JOHNSON: Thank you.

DR. JAMES: And there's nothing that's contractually enforceable in court.

MR. BLAHOUS: That is correct. Now, the problem that many might find with this particular projection is the quite reasonable prediction that the political process would react to avert that circumstance, that we would not tolerate a sudden reduction of benefits of 27 percent. So even though this is a literal projection of current law, some might find fault with it and say this is not our best guess of what would happen under the current system.

Towards that end we have provided you with various

alternative projections in your briefing book that show different adjusted baselines, to give you a sense of the range of possibilities. There are really only two sets under the current system. One is to cut benefits, the other is to raise taxes. Now, this chart shows the consequence of benefit reductions delayed to their last possible moment in 2038, if we did nothing and then we would have the maximum amount of required benefit reductions all of a sudden in 2038.

For purposes of illustration, we provided in your briefing books the opposite side of the spectrum which is shown in chart two and baseline two in your briefing books, which is to also assume what level of benefits can the current system actually fund but what if those benefit changes occurred at the earliest possible moment rather than the latest, and the projection is that if they occurred next year and were averaged over 75 years, the changes would be roughly 12 percent less than current law, although -- or excuse me, current promises, although after 2075, just as in this chart, benefit changes would be 33 percent less.

Now, no one can say for certain what exactly would happen within the current revenue stream that is projected, but what we can say is that the likely larger boundary on how large they would be would be 27 percent, the smallest they could possibly be would be 12 percent if they occurred next year, and somewhere in between that 12 and 27 percent benefit reduction, depending on the timing that they occurred, would be the benefit

reductions that are implicit in the current system.

Now, charts three and four show the other alternative, which is to raise taxes. Similarly, as with charts one and two, there are shown two possible scenarios. One is that the nation waits until the last possible moment and enacts its tax increases in 2038. Again, after all the measures are undertaken to fill in the cash gaps from 2016 to 2038, then there would have to be an additional explicit raising of the payroll tax or whatever other taxes the nation would need to raise in 2038, in order to meet full benefit promises. Then finally, in baseline four we show what would happen if revenues were increased in a short term, immediately, beginning next year and again averaged over 75 years.

Now, there are faults and problems with all four of these possible baselines. One is the most literal application of current law, but people would say the nation would never permit that to happen. Baselines two, three and four in various respects violate the instructions that have been given to this commission and also violate I think much of the political consensus regarding how social security should be treated. Baseline two, for example, assumes that there would be changes in benefits next year, which is clearly in violation of the commission's instructions and I think in violation of the political consensus. Moreover, baselines three and four assume increases in taxes, which, if they were payroll taxes, would also be off the table as far as this commission were concerned.

MS. : Mr. Chairman --

DR. JAMES: I have a question about baselines three and four, the additional revenue commitment.

MS. : Could you talk into the mike.

DR. JAMES: Yes. Baselines three and four, additional revenue commitments. You assume that all of that temporary surplus is used to buy government bonds, I mean, is given to the government. What rate of return are you assuming?

MR. BLAHOUS: Well, under both of these assumptions, these are simply attributions of revenue to the trust fund --

DR. JAMES: Uh-hm.

MR. BLAHOUS: -- and I treated them exactly the same way.

DR. JAMES: There's no investment --

MR. BLAHOUS: That's correct.

DR. JAMES: -- of those funds.

MR. BLAHOUS: And that actually points out some additional problems with these baseline projections. For example, one might regard it as politically unlikely that any nation would raise taxes in the midst of enjoying a surplus, as baseline four assumes. But if that did happen, then the nation would be on a path of far more rapid redemption of the public debt than it even currently is.

DR. JAMES: Uh-hm.

MR. BLAHOUS: One could look at baseline four and say that ultimately well before current projections, this scenario

would envision the government having to buy up private securities, because it will have brought in additional revenue when it's already buying down public debt at its maximum possible pace.

DR. JAMES: But you haven't computed any such rate of return.

MR. BLAHOUS: No. They are assumed treated as under current law.

DR. JAMES: Right.

MR. PARSONS: Yes, Olivia.

DR. MITCHELL: If I could just interject. It seems to me that in proposing or in outlining some of these different baselines, what's very clear is that you cannot use current law regarding benefits and current law regarding taxes as a baseline, because that is not a system which works. So I think that it's very important for all of us to remember going forward that you could hypothetically imagine a system where current law taxes go forward and make the benefits fit, or conversely where current benefits go forward and make the taxes fit, but not both. So that's really the place we need to start from in moving forward.

MR. PARSONS: Gwendolyn.

MS. KING: Yes. Another question, Chuck, I had, it seems to me that the four selected baselines could have been tripled or quadrupled with any number, and I think it would be important for you to mention to the group why you chose the 75-

year period for the baseline number two and what that portends for the trust -- for the social security program itself.

MR. BLAHOUS: Well, this actually was an issue that we struggled with at the staff level for a very long time. I think the conclusion was reached fairly early that we had to have at least one presentation of the consequences of pure inaction. In other words, the trust fund balance goes down to zero and benefit reductions occur as a consequence of that.

We did consider various alternative ways of looking at this. We finally in the end came to the conclusion that it would be most symmetric and organized in our presentation to the commission if there was a consistency between the total of levels of benefits provided under both baselines one and two and the total level of revenues made available in baselines three and four. For example, what happens under baseline one is that the trust fund balance goes down to zero and remains there. Now, under baseline two we could have said that benefits would be changed by the level that would be required to bring the system into what the trustees define as actuarial balance.

DR. MITCHELL: And that's really what I want you to speak to.

MR. BLAHOUS: That means that the trust fund ratio would be maintained at 100. For those of you who don't understand what that means, that means that there is always enough money in the trust fund at a particular time in order to pay one full year's of benefits. The reason we did not do it

that way is that that meant that baseline two would assume a different total level of benefits than under baseline one, where we allowed the trust fund to go all the way down to zero.

Now, we could have chosen to do both the other way, but we were -- we felt that baseline one was important to include simply because that was a literal portrayal of inaction, and then baseline two we felt we needed to show a level of benefits that was consistent except that the timing was different with respect to when they were paid.

DR. MITCHELL: So if memory serves me right, the trust funds have not been in actuarial balance for some time. Do you recall the last time the trust funds were in actuarial balance, Steve?

MR. GOSS: Yes. Precise actuarial balance last time was 1983, right after the amendment.

DR. MITCHELL: 1983.

MR. GOSS: Yes.

MR. : For one year?

MR. GOSS: Yes. Yes. The year after, a very, very small imbalance.

MS. KING: So for about three months. That's right. So we've been going along now for a period of some 18 years without the trust fund being in actuarial balance, which means that my grandchildren when they begin working at 21 -- they are now 1 and 4 and 6 years old, when they begin working, the assumption is that by the time they get ready to retire, there

will be funds sufficient to pay their benefits. My sense is that if we were do a whole series of baselines, we could really ratchet in 30 years, 40 years, 20 years, and it would give us a different picture but it still would say to us that we're not going to be in a situation where we take in the money sufficient to pay out benefits going forward, that there will be a shortfall, and that sooner or later we are going to have to reconcile ourselves to a sharp drop in benefits or some sort of revenue increase in order to keep the system going on the current path. Is that correct?

MR. BLAHOUS: That's correct. And just to elaborate on this question of how many baselines to present and how we arrived at these, one of the things we wanted to steer clear of was presenting anything that looked like a prediction or a recommendation or an attempt to mold these things consistent with someone's preferences as to how this would go forward.

We presented these baselines because they basically show boundaries. Baseline one shows the size of benefit changes that would be required if you wait to the last possible moment. Baseline two assumed they would occur at the earliest possible moment. The truth is somewhere there in the middle, and we felt it would be presumptuous to try to predict or suggest what the reality would be.

MR. PARSONS: Can I --

DR. JAMES: Just further on this question of baselines.

If you look at baseline two where you --

MR. PARSONS: Estelle doesn't know the rule.

DR. JAMES: -- are averaging over the 75-year period, I have the impression, and maybe you could comment on this, that if we were to do that, to adopt a benefit reduction sooner rather than later, and if we were then to run a projection for another 75-year period five years from now, we would find we still had a problem. Even though we thought we had solved it today, tomorrow it's no longer a solution, because we're substituting a bad year out there for a good year.

MR. BLAHOUS: That's it. That's absolutely correct, and we know that with some certainty. One year beyond the 75-year period, and I think Ms. King's comments may touch on this as well --

DR. JAMES: Uh-hm.

MR. BLAHOUS: -- this baseline assumes a change of 12 percent averaged over 75 years. In the 76th year, the change that is needed is 33 percent.

DR. JAMES: Right.

MR. BLAHOUS: So if this happened under current law --

DR. JAMES: Right.

MR. BLAHOUS: -- the next year's trustees's report would say you're out of balance again and you are not on a sustainable path.

DR. JAMES: Right. Those are my grandchildren who are going to be retired at that time, so I am concerned about that.

DR. COGAN: Chuck, as I understand it, the baselines

that you are using, the purpose of that discussion is to help us arrive at some common understanding of the problem and draft an interim report that provides that common understanding of the problem. It does seem to me that, although these baselines are useful, I'm not sure that they are necessary. I mean, it does seem to me that what we want to do in this interim report is state very clearly and very simply what the magnitude, the timing, and the scope of the problem is, and what the consequences of failing to act are.

What I worry about is that the presentation of specific ways of solving the problems are going to be misconstrued, incorrectly construed by individuals as our proposed solutions, and since I don't think that these baselines are necessary for an interim report and I do worry that they are going to be misconstrued, seems to me that we might be better off trying to structure an interim report that focuses on the timing, the scope, the magnitude of the problem, and hold off on the selection of a specific baseline until we get to the point where we have several proposals, several proposed solutions and we need a baseline against which those proposals can be compared.

MR. POZEN: I'd like (coughing) to, excuse me, reinforce what Jack (sic) Cogan just said, because I think what's the purpose of these baselines, is just to help educate people as to what's the nature of the problem, and I think when you come down to it, ultimately you see, if we do nothing, in the year 2038, we're going to either -- that we'll have a shortfall of

benefits or we'll have to raise more revenue, and you can raise revenue through specific payroll taxes or through general revenue. I think that's really all you need to say. You don't have to say we're proposing to, even the theoretical, hypothetical we're going to propose to reduce benefits et cetera.

It's just a way of explaining to people how big the shortfall will be, and I think that if we can get that through, to have people understand that there's a year-to-year deficit in 2016 and then in 2038 there is this shortfall, that can be described in a number of different ways, and I would stay with what -- just benefit and revenue, and not try to get in these gradual things which really make it extremely complex. Then people have a sense of what the magnitude of it will be.

MR. PARSONS: I wonder also, Chuck, I know the chair is supposed to not comment substantively, but just listening to the discussion, it does strike me that it's fairly easy to say we have an obligation to pay out \$500 trillion and we're only taking in \$400 trillion, so there's a shortfall. I think people need to understand why that is so, why you can't fix it in the current system for all time, namely the point that Estelle was making, that if you just move it out a year it falls out of balance again, and it has to do with the nature of, the structural nature of the social security system.

In a pay-as-you-go system, if when you started out, let's say that there were 8 people working for every person who was retired and the average age of a retiree was -- lived in

retirement for 10 years, and if those ratios stayed in balance for all time, then probably the pay-as-you-go system would work.

But those are changing. We now have 3 people, moving down to 2 and a half people, working for every person who's retired. Instead of living an average of whatever it was 30 years ago, it's now 2 times that length. So that we're always going to be falling behind, given the structural nature of the social security system, unless we change the structural nature of the system. You can't ever get -- all you can do is sort of catch up for the moment, and with the next click of the second hand you're out of balance again because the demographics and the structure of the system are working against you. So I think that people can begin to understand why there's a problem, not just that there is a problem --

MS. : Uh-hm. Right.

MR. PARSONS: -- and what it's current magnitude is, but why there's a problem. That then leads you to a whole different way of thinking about what possible solutions might be. Yes, Sam.

MR. BEARD: I completely agree with that comment, because as I've gone around the country just talking about social security, what everybody understands is once the baby boomers retire there are going to be less than two workers asked to finance one senior. Everybody understands that. It's not trillions of math this and some curve that no one knows what it is. It's that there's 1.8 workers asked to finance 1 senior who

increasingly is going to live to late 80's, early 90's, and then go over 100. Your wording was perfect.

MR. PARSONS: And if it's me the senior, I've got expensive tastes.

(Laughter)

MR. BEARD: The next thing I'd like to --

MR. POZEN: You're going to live a long time, too.

MR. BEARD: The next thing I'd like to talk about in defining the problem is not just the social security problem, it's the wealth problem.

MR. PARSONS: Yes.

MR. BEARD: I'm not sure that that's in these materials, in terms of if you don't define a problem then you can't come up with a solution. If you start with the problem that, going forward for retirement security, unless you have adequate finances you're going to be in a real difficulty, then you go to the whole wealth issue that half the country has less than two percent of the wealth. I think that needs some real definition, which then sets the stage, and I like your wording, which is it's the reason for major structural change. We have new problems in the year 2001 which they weren't facing in 1935, and one of them is the wealth issue. If we don't define it as a problem, then we're never going to get a solution to it.

MR. PARSONS: Gerry.

MR. PARSKY: I would really concur with the comments about the baselines. My added comment, though, is that the

baselines as presented try to anticipate what might be done, as opposed to, say, real structural change needs to happen, let's propose a solution. I do think, though, that it is important as we lay out the problem that we set the stage for comparisons. There will be comparisons made to the solutions that we come up with against other solutions, and I think we need to be able to anticipate that as we lay out the problem, but I would really concur that trying to pick one of these baselines -- to lay out the problem around the baseline as opposed to basically getting on with the structural problem is not the right way to go, because people will just say well, you're anticipating certain behavior, that's not going to happen that way, and it can go on endlessly.

MR. PARSONS: Tom.

DR. SAVING: Mr. Chairman, there's another issue I think that the interim report or a way of describing the state of the system that would be instructive for people is the question as you look at the deficits that are forecast, you would wonder why is that a problem, why can't we just raise the money. And the question that's there is, what's the share, if we assume the federal government is going to continue to raise 20 percent of the gross domestic product, what share of that budget is going to be taken up with a program like this one and with other elderly entitlement programs? That is what's going to tell you the pressure that's going to be on the federal government, because all its other programs are going to have to get smaller. It's

very important for everyone to see that if this program were to go on, and if we were to fund it in any one of these scenarios, that it has implications for the entire rest of the budget. As I've said before, in 2070 it means the rest of the budget is zero. The federal government is no longer doing anything.

The point really is to see --- those implications. We've raised that issue, and that comes back to this trust fund issue that says there's nothing in the trust fund because the trust fund has nothing to do with that share of the federal budget. It doesn't impact on it in any way. It's exactly the same no matter what the trust fund is. And it really gets right to that point and says what's the share of the federal budget that these programs have to take in order to continue, and you can see that that share of the federal budget is not going to be tolerated. The public is not going to give up those federal expenditures that they now have, and if they're not going to give them up, then they are going to have to give up this program or those programs or do something, and I think that's important.

MR. PARSONS: Olivia.

DR. MITCHELL: Just to follow along that tack, I think one of the things that's really important in this area is to recognize that most folks don't really relate on a daily basis to GDPs and trillions of dollars and percentages even, and so what I would like to propose is to try to go back to the baseline but maybe cast it in terms of something concrete that people can really understand. For example, if you're talking about a

benefit cut of 33 percent, cast it in terms of, well, average benefits for the average family are on the order of \$16,000 a year for a retired worker and spouse, so this is maybe a \$5000-a-year cut, on that order. Make it very concrete so that people understand, it's not abstract, it's not something that will happen in the future that we can't get a handle on. This is going to be very important to retirement consumption.

Similarly, I would say take the tax changes that would be required, if you take that approach, and convert it into actual dollars per payroll per worker that a worker is going to have to pay on his or her payroll. Or a different way to put it is if you're talking about the unfunded liability of the current system, that number is maybe \$9-10 trillion. I don't relate to trillions. I know some of you people with bigger budgets than professors do, but you know, if you convert it to an annual -- I'm sorry, a per capita amount on a per worker basis, it's on the order of \$68,000 per worker in today's America.

So this is the way we have to I think convert these graphs and scenarios to a very concrete way of talking that people can really understand and get the notion that instead of retiring on \$16,500 a year for an average retired working family, maybe it's more like 10 grand, and that's going to be a big change and we need to do something in order to make it look better.

MR. PARSONS: If you don't deal well with trillions --

DR. JAMES: Can I --

MR. PARSONS: -- imagine the rest of us with
googols. ---

DR. JAMES: Can I add one other thought, and maybe
you're planning to get to this when we let you move on, but until
now we've only been talking about financial flows, and I think at
some point we have to talk about the real goods and services that
we're really concerned about.

One thing that happens when you have fewer workers
supporting each retiree is it becomes very important to raise the
productivity of those workers, otherwise there's just going to be
less to go around for everyone. I mean, it's really not the
paper money that we care about, it's really the goods and
services that go behind it and one problem that I think we have
to raise. but it is difficult to discuss and it's going to be a
challenge for you to write this, is that the current system
doesn't really include any components designed to address this
issue of enhanced productivity.

Now, you could say that this problem could be taken
care of somewhere else, but if you want a program that really
provides security for old age, then as the retiree-to-worker
ratio increases, I think you really have to worry about taking
specific measures to increase worker productivity so you have a
larger pie to go around so that both the workers and the retirees
can be supported, and the current system doesn't do that. I see
that as really the big problem that lies behind the financial
flow problem.

MR. PARSONS: ---

SENATOR MOYNIHAN: Mr. Chairman, just to correct the record about our colleague Olivia Martin (sic), she may not deal with trillions, but people who have trillions deal with her. She is the recipient of the TIAA CREF Paul A. Samuelson Award for Outstanding Scholarly Writings on Lifelong Financial Security. We were mentioning this earlier because of something that Tim Penny said, that the -- I think most of us here will know, any professor will know, that in 1915 or thereabout Andrew Carnegie set up a system that provided teachers insurance and annuities that you could purchase directly, as it were. It had a huge -- hugely important, because it meant that academics could move around in the system, weren't stuck with the first job they had --- for them. Then in the 1960s or thereabout, they added for a fixed income system, they added portfolio choices, and that's what the CREF is. I mentioned to you, I have some --- of that that they recently commented that their benefits had gone down because the market had gone down, they had gone up so very much earlier but you know how all things considered, they're all better off. I asked was that automatic, and you said well, yes, if you have that open arrangement. A mutual fund system can reduce benefits if incomes or prices are reduced and raise them, and they have indeed raised them, but as Tim Penny said and it seems to me absolutely essential, nothing can be changed in social security save by statute, by law. Those immensely able people, I see Steve Goss agreeing, for all the willingness in the

world and all their knowledge, it has to take statute to reduce benefits or to increase taxes.

MR. : --- missed that point.

SENATOR MOYNIHAN: Doesn't hang around with trillions, you know, lots of guys have trillions.

MR. PARSONS: Are there other thoughts about the report?

(No audible response)

MR. PARSONS: I had one just in sort of reading the outline that you sent to us, Chuck. It does strike me that there is learning that can be captured. In other words, Estelle, you --- on to this, there are other models we can look at that have gone down the road we're going down and have reached the point of judgement or reckoning that we all agree is still some number of years off here, but those systems didn't act in appropriate and timely fashion, and then you end up with very different sort of options I think that face you, if you put off kind of correcting structural imbalances. I wonder if in trying to illuminate the problem, we shouldn't reach out to some of those examples.

MR. BLAHOUS: Are you referring to international examples?

MR. PARSONS: Yes, well, there's certainly -- well, you can actually refer not only to international examples in terms of some of the European countries, but as I was listening to Senator Moynihan talk about TIAA CREF, on whose board I served many years

ago, and it's been one of the sort of exemplars of responsible retirement planning, because it's always been on a funded basis.

My father worked for Pan American Airways for 35 years, --- company, great -- and once upon a time it was the great airline.

He retired, and some number of years after he retired, the pension fund ran out because it was never funded.

MR. : Yes.

MR. PARSONS: It wasn't done on a fully funded basis. The assumption always was that Pan Am will be there, and I suppose the assumption here is that the United States government will always be here, but will we have the will and the means to do the kinds of things that Tom Saving was talking about or will we be effectively precluded from meeting our future obligations because we don't -- we simply can't go into that bag and pay up?

In other words, I think there's something very fundamental here about the way in which we have funded this system, the promises we've made.

Bob Johnson pointed out that those promises are just that. They're not enforceable. There's no contractual obligation. People have been lead to believe something that at some future date is not -- they're not going to be able to cover that debt. They're not going to be able to cover that promise going the way we're going. I think that somehow we need to illuminate that for people, because there will certainly be numbers of folks, in fact they already are kind of rattling their sabres about the nefarious work that we're up to here and we're

trying to take people's benefits away. I think it's quite the opposite actually, trying to create or revise the system so that it can fulfill the promises that are being made today, tomorrow.

DR. MITCHELL: I'm not quite sure how you would like to proceed. I know one of the things that it was intended that would be included in the interim report would be some discussion of where the problem is, where it came from, how big it is. At an earlier point there was also the suggestion by some commission members that there would also be criteria for evaluation. Are we going to discuss that today, or should we come back to that a different time?

MR. PARSONS: No. I think we need to discuss that, because we need to give the staff some guidance so that they can be working on drafts which they can then get to us between now and our next meeting and we can give feedback. So if you have some thoughts on that --.

DR. MITCHELL: Well, I did have a couple of thoughts I think mostly coming from my experience on the technical panel for "Trends and Issues in Retirement Saving." These were criteria that we developed around a lot of different discussions with people from a whole variety of different persuasions.

I think that in terms of the briefing material, there were some excellent suggestions that were identified in terms of solvency, sustainability and so on. Economic impact, there was a good discussion of that also. Some of the things that I would

hope could be added, at least based on my experience with the technical panel, our first criterion was adequacy of retirement income relative to poverty thresholds and to the household's preretirement income. There's a little bit of that there, but I would like to see some more.

Also, down the road when we get to looking at various different suggestions and plan designs, I would hope very much that we could examine some of those plan designs in terms of the distributional consequences. So to the extent that anybody around can help devise models of that sort, that would be useful.

We also talked about avoidance of market inefficiencies, and there's a little bit of that there, but again, to try to emphasize avoiding inefficiencies. Encouragement of private and aggregate national saving, I think that ought to be a criterion, and perhaps we can come to some agreement around the table on that.

Then also strengthening the financial integrity of the nation's retirement income system as a whole. In other words, not just focusing on social security alone, but also looking at the spillover effects on --

SENATOR MOYNIHAN: ---

DR. MITCHELL: -- other pieces of the system, like employer pensions, other private savings, IRAs and so on. So I will be happy to make available to you the statement of criteria from the technical panel, if that would be useful, but at least I hope to get some of those on the table.

MR. PARSONS: ---, Gwen.

MS. KING: I would just urge everybody to remember that in this discussion about social security benefits, it was never intended that social security benefits would be the only benefits retirees would enjoy. That, of course, has turned out to be the case in a number of instances, and many of us probably have situations like that in our own immediate families. I know I certainly did, but the thinking has always been that social security -- and I always hate this expression. I've looked for another one. I haven't found it yet -- would be one leg of a three-legged stool. You all know that expression. The other two legs of the stool being a pension and savings. Well, we all know what the savings rate is in the United States. It's pitifully low, and people have no extra money.

SENATOR MOYNIHAN: It is now just negative.

MS. KING: It's negative, as far as -- and I may be wrong, Steve. I defer to you and Chuck again. But the savings rate, and you can break it out into different groups of people, but it's pitifully small compared to other countries.

Pensions we like to think are working, but a lot of people are not working long enough to get pensions, and of course, the chairman has just given his own example about how some companies go away and with them, pensions. So social security does have that importance. And I raise that because, while the program was never intended to be the sole retirement income for people, in many, many instances it has turned out to

be that. So it again underscores the importance of the work that we are called on to do.

MR. PARSONS: Bob.

MR. POZEN: I'd like to -- we're getting close to 2:00 o'clock, just to sort of formally propose that the staff present us with a draft of an interim report as soon as reasonable, so that the next meeting that we have we can review that, but I'd also like to emphasize that this -- I think everything you've heard here is that we believe that the key to this report is the educational function, the sort of almost investor relations functions or that sort of thing. So that on the one hand, I think we would all like to get the interim report out as soon as possible. On the other hand, unless we can combine this with a strategy, an educational strategy, then I think we will have missed something. So I guess I'd like to encourage you to sort of put them both together. On the one hand, we'd like to have it out quickly; on the other hand, if we have a document out but we have no way to disseminate it, it's like one hand clapping in a forest, you know.

MR. PARSONS: Let me say also for the benefit of the public, as we said, we're going to approach our task in two bites, an interim report and a final report. The interim report will focus more on the nature, cause and nature of the problem and the criteria we will use to evaluate solutions to the problem. Then the second and final report would be a recommendation for dealing with these structural problems.

Nevertheless, we'd like input from the public on both of these reports. Because we are on a fast track with respect to the interim report, we do have a web site that went live today. Chuck is going to shortly tell you what the web site is, and I would encourage those who want to share their wisdom with the commission on fund and nature, origins, antecedents, scope, dimension, size of the problem, and on what the appropriate criteria for evaluating solutions might be to do so by making access to that web site and sharing yourselves with us with respect to the second half of the -- or second part of the report. We have tentatively decided to have some public hearings. I can't tell you at this point in time how many around the country, probably in early September. The commission will probably divide itself up into either two or four groups that will hold hearings around the country to take input from folks who want to respond to some specific questions we'll propound after we've done our preliminary work, so that there's plenty of opportunity for the public and interest groups to have an opportunity to interact with the commission. Chuck, what is that web site?

MR. BLAHOUS: The web site is W-W-W dot comm, C-O-M-M, to, T-O, strengthen, S-T-R-E-N-G-T-H-E-N, soc, S-O-C, S-E-C, dot gov. So it's an abbreviation of our rather illustrious name.

SENATOR MOYNIHAN: Maybe you could repeat that.

MS. : Why don't you just write it on the flip chart.

MR. : Yes.

MR. BLAHOUS: Mike is closer to it. Perhaps he can do it.

MR. PARSONS: Put it up there. Bob.

MR. JOHNSON: I want to charge the staff as they develop this interim report to make sure that they educate the public on how we got here, and it's not one where you can sit back and point fingers at individuals whether they're from the party from the left or the party from the right, whether they're young or they're old. I think it's just the sheer fact of life, once you design a system where you're trying to both level out everyone's opportunity to participate in benefits and engage in a progressive redistribution of wealth for the benefit of everyone, you end up with a system where if just the sheer fact of demography, people living longer and consuming longer than anyone perhaps anticipated, you find a system out of balance under the current structure. So I don't think it would help any of us here if we engage in -- when I was in graduate school a professor at Princeton had this saying about statistics, is that most people will use statistics like a drunk uses a street lamp, to hold them up rather than for illumination.

(Laughter)

MR. JOHNSON: So if you focus on the facts as they are, and clearly we understand there are more people living longer than there are people working and contributing, we have a problem. It's not fair to the older people, who assumed in good

faith when the social security system was instituted that their funds would be there for them, to snatch them away, nor is it fair to young people who work very hard to build up their own nest egg for their own family to see that nest egg given away to someone else and they have no claim on it. So somewhere in all of this, the good intentions ought to be how do we solve a problem that would benefit everybody. I think if we draft our interim report to the point that that is the problem, trying to make sure that young and old are in accord on this, I think we're a long way towards coming up with a solution.

MR. PARSONS: Okay. All right.

DR. JAMES: Could I add something else that I'd like the staff --

MR. PARSONS: Only because you put your hand up this time, Estelle, yes.

DR. JAMES: Okay. I'm just so small that you don't see it.

MR. PARSONS: I have to reward that. Estelle.

DR. JAMES: I'd also like to see something about the distributional effect of the current system included in the interim report, and the reason I'd like to see that is, those effects are somewhat different from what many people think they are. I mean, many people think that one of the good things about our current system is that it's progressive. If you look at the annual benefit formula, it looks progressive, but, as you know, when you actually do studies on lifetime redistributions, it

turns out that our current system really is not progressive and does not redistribute to low-income groups. I think it's very important for people to know that, because I think we ought to be able to do better than that, so we ought to know what the starting point is.

MR. PARSONS: Okay. Mario and then Fidel.

MR. RODRIGUEZ: Chuck, also, I know we're dealing with a lot of complex issues here, but I think when we're giving the information out, I think commissioner King and Olivia both have alluded to is, I think if we can give the information out as simple -- and make it as simple as possible so a general public can really understand and you understand what we're dealing with and real numbers that they can understand, I think it will be very helpful.

MR. PARSONS: Fidel.

MR. VARGAS: As a former mayor, I heard a motion and I was actually just trying to get a clarification. Are we going to -- any of the things that have been recommended, I'm assuming that for the record under Robert's Rules of Order we're going to vote as a commission.

MR. PARSONS: The chair is embarrassed, because you're correct. We did have a -- it sounded like a proposal, but it was a motion to ask the staff to take these thoughts and pull together between now and our next meeting, which is scheduled for the 24th, a draft. So I am going to suggest --

MR. VARGAS: I would second that.

MR. PARSONS: -- if you could ---

MR. VARGAS: I would second that motion ---.

MR. PARSONS: -- 24th of July. So I'm going to suggest that if you could get that draft -- we'll assume that that would say at least two weeks before our next meeting, so the 10th of July.

MR. BLAHOUS: We'll do that.

MR. PARSONS: It has been moved and seconded. Is there any objection?

MR. PENNY: I just want a clarification. We're not committing ourselves to finalizing the report on the 24th.

MR. PARSONS: Not at this point.

MR. PENNY: But we will review --

MR. PARSONS: We're directing that the staff pull something together, that it hand it to us at least two weeks before that so we know where we are.

MR. : Yes.

MR. POZEN: I think we're also asking the staff to have an educational strategy as part of that.

MR. BLAHOUS: Right. Yes.

MS. : Uh-hm. Right.

MR. PARSONS: Okay. With that exception, staff is so directed. We're going to take a break now until 2:30 I think. For the press, Senator Moynihan and I will be taking questions from the press in 10 minutes at 2:15 in the Garfield Room, which is just 2 doors down this way (indicating), and then we're going

to reconvene at 2:30 for the purpose of allowing the dialogue between the commission and staff to continue, and obviously the public is invited to participate in that if they so choose. We'll be back at 2:30.

(Brief recess)

MR. PARSONS: If we could get commissioners back to the table. All right. Because the initial meeting of the commission when we first sent out notice was going to be from 10:00 to 2:00, several of our members have commitments early in the afternoon and are taking off, including Jack Cogan and indeed our illustrious co-chair Senator Moynihan, but we thought for those who could stay there would be an opportunity to have some further interaction with the staff and with Steve Goss, the actuary, in terms of questions and directions or further instruction. As Chuck and I just said, this can go as for short a period a time or as long a period of time up to 4:00 o'clock as is necessary. But are there any further requests of staff or directions to staff or input for staff?

MR. BLAHOUS: I know that at least two of our commission members who had interests are not at the table right now, so even if none of the sitting members have none, we shouldn't break up just yet, because I know there are a few more with interests.

MR. POZEN: One thing that would be helpful I think is, there's been a lot of, you know, a lot of different people who have come up with a lot of different proposals for social

security reform, including private accounts, including government invest, including these things. Is there a readily available summary for the commission members so that -- I mean, many of us have been receiving -- people have been sending stuff and we have a lot of material. If there was a well-organized summary of what's out there in terms of literature and what people have, that would be I think very helpful, categorized as to non-private accounts, private accounts, various other solutions.

MR. BLAHOUS: We can certainly get you summaries of that nature. We have already begun at the staff level to develop some such summaries. Working with Jeff and Steve, we've put together short, one/two page summaries on several of the plans that have been introduced within Congress. You should also know that we still have actuarial estimates that Steve and the Actuary's Office have put together when proposals were introduced in prior Congresses.

One caveat that should be issued is that many of these analyses and estimations were done under the assumptions and previous versions of the trustees' report. Those assumptions have since been updated, and often plans are updated at the same time as people seek to fit the new numbers better. We've tried to be in touch with some of the sponsors of these proposals to ask them what versions of their proposals, how they should be summarized, if there are any changes that should be made to reflect the updated estimates, but we have varying levels of detail that we can provide to you or the entirety of the

commission.

MR. PARSONS: Sam and then Fidel.

MR. BEARD: --- Bob said, one of the really interesting things that occurred in the whole social security debate while I've been in it is, President Clinton's social security advisory panel, because they were addressing the issue of solvency, and the two old ways to do it was you either raise taxes or cut benefits, and they said there's a third way, which is the extra rate of return from the private sector. And that ended up being a breakthrough thing. Then within that, it broke down into those that said the federal government should invest many billions of dollars a year, the extra rate of return of which helps to bail out the system and then two-thirds of the members said go to individual accounts. But just the fact that consistently was what Bob was saying, the fact that that -- there was a Presidential advisory commission which took many hours of Mr. Johnson's time, the fact that it was the first time that it was agreed to at the level that you could address social security without putting the extra rate of return to the private sector to work, it was a breakthrough thing, and then you can discuss and here are the two ways to do it, the individual accounts or the federal government invest the money.

MR. BLAHOUS: Well, we can certainly reproduce and circulate to you, and Fidel is as familiar with this as anybody here but, what those findings were. It's often remarked that that advisory council did split into three camps as to the

proposals that they backed, but there were sections of the report that did reflect the unanimous opinion of the council. They put out findings saying that the system should incorporate some partial advance funding, and that was agreed to across all 13 members of the council. We could reproduce either the separate recommendations of the advisory council and circulate them, or just the unanimous ones, depending on what your needs were.

MR. BEARD: It's just that the important building block was that you unanimously said you needed the extra rate of return from the private sector.

MR. BLAHOUS: That's right.

MR. BEARD: That was the important building block.

MR. GOSS: Sam, just to point out, I think Chuck had it exactly right. The one thing that was true of all three of the major proposals that the council put forth was that they would move towards having increased advance funding over and above what the actual current system was working forward to at that point in time. Two of the three plans did in fact absolutely include investment in private assets to try to get a higher return. One of the three plans came a little bit short of that and simply suggested there should be a study about moving towards investing in the stock market but did not explicitly suggest that that should be done under its plan. That's the so-called, I think it was called the --

MR. BLAHOUS: Maintain benefits.

MR. GOSS: -- the Maintain Benefits Plan, that did not

quite go that far.

MR. POZEN: I just wanted to say, it would not be that useful to get full copies of many, many studies. I think the better is sort of good synthesis and summary categorized in useful ways.

MR. BLAHOUS: That would --

MR. POZEN: And then anyone who wants to read the full 200/300 page setting of each of these studies will be free to do it.

MR. BLAHOUS: The report does contain some short summary pages, and we can just reproduce those.

MR. PARSONS: Let me suggest by the way -- Fidel in a second, but when you speak, it would be helpful, because there are some who are --- us and some who are listening through other means that you speak into the microphone.

MR. VARGAS: I was just going to say that from an educational perspective, one of the issues that eventually we're going to be discussing down the road is the transition, --- up with something that was to some degree addressed and it's obviously a huge issue, so it might be a good idea to start to get some background on that issue.

Second, I was just going to recommend to the chair that since a few people came in, you might want to reiterate your comments in terms of what this session would be for and how long we need to be here or not be here.

MR. PARSONS: Fidel's ready to go.

MR. VARGAS: No, I'm not ready to go. I just want to make sure that --

MR. PARSONS: ---

MR. VARGAS: -- everybody is clear what the deal is.

MR. PARSONS: -- said, because several of our fellow commissioners had earlier -- or had made appointments when we earlier had planned to meet between 10:00 and 2:00, and so they had to move on. This session is intended to really be a little bit more informal and to allow commission members to share any insights they might have with staff or more particularly to task the staff to go and make certain kinds of inquiries or do certain kinds of analyses that will help us down the road, but just to give us an opportunity to make sure that this process is moving in a direction that is both appropriate and comprehensive, and that when we run out of direction to staff we can adjourn the meeting. Bob.

MR. JOHNSON: I just have a question to see if this thinking is consistent. When we approached this problem, none of us anticipated the longevity of the American population and therefore we're sort of in imbalance in the number of workers who are contributing to the workers who are living longer. Are we also facing the issue that we might not anticipate the fact that the majority of workers 2038 to 2075 would be minority workers who are historically paid less, therefore less productive in terms of generating revenue/taxes to support the older workers, and so that there will be even a greater claim on those workers

who are more productive? Because if you continue to have a society that tends to discriminate in terms of wage and opportunities for the majority of workers, the problem could be even worse than anticipated. Has anyone focused on that issue at all?

MR. BLAHOUS: Well, let me -- there are a couple different parts to your question I'd like to address in sequence. We do have some information in your current briefing materials, and we can supplement it with such additional requests as you might have, talking about the changing composition of the elderly population, 20, 30, 40 years out, and those figures do bear out the portrait that you have put out there, which is that there will be an increase in the proportion of people from minority groups that historically, and I'll project it to continue to, have less access to non-social security, private pension income, individual savings, and also historically will have lower wages. These trends also show up in differential longevity data. Now, what we have not produced, at least -- and Steve can take the opportunity to comment here if he wishes, we have not produced, at least not through the Social Security Administration's Actuary Office, breakdowns of the population by ethnic or demographic status to give a read on how such groups are going to fare under the social security system. There has been a number of studies of this in the academic literature, and what we could try to do for you is to try to reproduce some of those and get them to you.

I think Estelle made an allusion earlier that the redistribution that occurs in the current system is really very chaotic and does not really add up to a systematic redistribution of income from people who have more to people who need more. The reasons for this, there are a lot of offsetting trends. For example, there is redistribution in the current system from single earners and two-earner couples to the traditional one-earner couple with a nonworking spouse, and if you break those groups down in turn, you will see a greater proportion of lower income groups among the people who are being redistributed away from according to marital status.

Similarly, we are seeing troubling projections 20, 30 years hence with regard to the beneficiary population and how it's distributed. For example, there's about 23, 24 percent of the current female beneficiary population over the age of 65 are widows. That is projected to decline over the next 20, 30 years down to 12, 13 percent. Well, at the same time, today female beneficiaries age 65 and older, only about 37 percent of them are earning benefits based on their own wage histories alone, and that proportion is going to increase dramatically and be over 50 percent 20, 30 years out. So you have a very different picture in terms of who is at risk of poverty 20, 30 years from now than is the case today.

We have certain things that are built into this system to take care of certain groups. There's a widows benefit, and you can alter the widows benefit and target those resources. But

for divorced women, never married women, the increasing share of the elderly who are from demographic groups with lower life expectancy and lower incomes, for all of the attempts at progressive redistribution within the current system, we could actually be facing enhanced poverty rather than reduced poverty as a consequence of the system 30 years out.

DR. JAMES: I think, though, that your question actually raises another interesting point, which is we know that if we look at the wage gains over the past 20 years, they haven't cut evenly across the population and the polarization has increased. The lower half hasn't really gained very much, and the upper half -- the upper 20 percent or the upper 10 percent, have gained a disproportion -- have taken a disproportionate share of the wage gains.

Now, we also know that there is a ceiling on taxable earnings in social security. So it seems to me this means that a decreasing proportion of the total wage bill has been subject to social security tax, at least it seems to me that's what the logic would be, and it also suggests that the rate of growth in social security covered earnings in the recent past and maybe projected for the future is less than the rate of growth of the total wage bill. So that's another aspect. Of course, it's many of the minorities who are clustered in that lower group that haven't been gaining from the recent wage growth. So in the assumptions that you make in social security projections, are you taking into account the overall rate of wage growth, or are you

projecting what might happen to the distribution of that wage growth that would cause social security wages to be increasing at a slower rate than total wages?

MR. GOSS: Well, Estelle, you are exactly right. I forget exactly how many years ago it was. At one point we were at the point where, of all the earnings covered under social security, we reached a peak of about 90 percent of those earnings being subject to tax under the taxable maximum.

DR. JAMES: Uh-hm.

MR. GOSS: And although the taxable maximum amount is indexed by the average wage growth over time, that has been resulting because of what was known as this dispersion of earnings --

DR. JAMES: Of organization, right.

MR. GOSS: -- more of it showing up moving toward the very highest earnings levels. We've resulted in having somewhat of a decline. We're actually now down at the point of being around 85 percent of covered earnings being subject to tax.

DR. JAMES: Uh-hm.

MR. GOSS: The question is how exactly do we move forward, does this continue to a strong degree in the future. Our current projections assume that we will continue to have some of this dispersion going on for about another 10 years in the future, but only that far.

DR. JAMES: Uh-hm.

MR. GOSS: Might this dispersion continue on beyond the

10 years? It certainly might. The current assumptions are that we'll have dispersion, and Tom Saving isn't here, one of our public trustees who with his different hat needs to speak to this directly, but at this point in time, we're assuming that only about a 10-year period will we be having this occurring.

DR. JAMES: But basically that's an assumption and if in fact this continued, then you would find that the covered wage bill would even be smaller, it would be getting smaller and smaller relative to the total wage bill, and therefore the total social security revenues may be smaller than you anticipate.

MR. GOSS: That's correct. Absolutely. Yes. If I might just add, on the point about the very, very difficult issue of trying to make the projections in a way that it pays attention to the changing nature of our population. As Chuck mentioned, we very carefully make projections in our population on our underlying beneficiary structure and our worker structure going into the future, paying attention to the age, sex and the marital status of individuals. All of these things very directly play into the nature of the benefits that you have.

We've had some great difficulties in trying to make projections by race, partly because a lot of the data that is available that would allow us to look at the level of benefits, the level of earnings, on a race/ethnic basis is not of very good quality, and this appears as though the nature of data reporting in the future is going to make it of even lesser quality. It's not as though -- it's not that it isn't an important feature,

it's that if you can't get a good handle on what is out there, then it becomes very difficult to deal with it very directly. But larger African American, larger Asian components, and it does change in very many ways towards the future, the assumptions that our trustees put together are really designed to try to take that into account as well as they can, without really trying to break up the population into these separate pieces and look at how they'll operate, but more to look at it from the point of view, what do we think the overall economy will be moving forward as, for instance, in our average wage assumption, which is to assume that wages will grow at about an average 4.3 percent per year in the future. You could argue, for example, that if the population were going to be constituted differently in the future, that perhaps that would be faster or it would be slower, but I think our trustees have consistently, even across Administrations, taken the attitude that the economy will be such that the work force that comes to bear in this country will be up to the challenge and will provide the kind of talent or the kind of labor that is needed.

MR. JOHNSON: Well, I think the thing for me that sort of crystallizes for me at least the need for the individual private accounts is because it seems to me that a minority worker has a catch-22 problem, and during the most productive years is when they'll be contributing most to the social security system.

They don't have the same mortality rate as the others, so they'll die off faster and therefore not receive it. If you've

got more of them coming into the work force, they become the primary contributors to the wealth retention, at least while they're alive, of the other population. So in order to equal it out, you have to do something either about increasing the mortality rate of African Americans or allow them some other access to the money that they've earned while they can live off of it. Unless you can do that prior, you will create a situation where the people who are most in need of the wealth transfer are the least likely to get it, even though they are --- for the other ---.

MR. GOSS: But I might suggest one of the good things in some of the academic studies that have been performed so far have not really been in a position to take advantage of all of the aspects of the program that are there. If you look solely just at the retirement benefits, you are absolutely right. Groups that have higher than average mortality, like men, African Americans, either of those groups, would in a retirement sense under a contributory plan like this appeared not to do as well. Both of those groups, however, the evidence is, have higher disability rates, for example, and so both of those groups, both African Americans and men, tend to receive more benefits from that portion of the program which provides disability benefits.

It becomes much more difficult in the analyses to try to incorporate all of these items. We do in some of the estimates that we'll probably be looking at in the coming months, try to incorporate all aspects of the program benefits,

retirement, disability, aged survivor and young survivor. The difficulty is really to do that on a comprehensive basis by race and ethnicity. To do that, you'd have to not only have good knowledge of what the difference in mortality is by group, and there is some knowledge on that, but you'd have to have that also by income level, and also you'd have to have good knowledge about all of those crossed with the disability rates by the different groups, which is very difficult to come by.

MR. BLAHOUS: I just want to wrap this up so we can be responsive. We're talking a lot about some of the difficulties here, but I'd like to end this by talking about what we can do. There is a very extensive academic literature on this, and we can certainly reproduce a lot of that and get that to you that speaks to this. We also are able to break down the treatment of people under the OASI program versus the disability program, and we can do that as well. There are, even though SSA doesn't do them, projections, Census Bureau, others, on the composition of the elderly that would have to be reconciled with SSA's in some respects, but which should be able to give us a handle on the differential mortality expectations. So we should be able to give you a fair amount of that data.

MR. PARSONS: And I do think that the overarching theme ought to be, understanding that there's lots of little moving pieces underneath of this, could we figure out a way to say structurally balance the system so that the benefits that are promised to people now in terms of security and availability can

be secured for the future, and then some of the wealth transfer issues, which as you say cut all kinds of ways, as a secondary level we can kind of look at that and see if all that makes sense. But I think that the big theme is how do you realign, restructure the system so that it can work in today's demographic environment. Okay. Are there other questions? Olivia.

DR. MITCHELL: Let's see, a couple things. One, I think a number of us have been talking amongst ourselves, and I would really appreciate it if we could try to get a meeting schedule through Thanksgiving, at least have some meetings scheduled and then cancel them if we can't hold the meetings, but schedules are good in my business.

Couple other points. One, we talked a lot about educating the public, educating other groups, but I think we also need to do some more to educate ourselves in this next few months. We don't have a lot of time. I think between now and July the interim report is going to be very much on the front burner, but I wanted to get some things going that maybe we could talk about in August if we're able to have a meeting then or at least in the beginning of September.

I'm not a D.C. insider, unlike other people, some other people on this group, and I think one of the areas that I would very much appreciate some education on has to do with the range of individual account options that have been produced and discussed around Washington and other places in the last few years. What I would really like to ask the staff to produce is

some sort of a summary of the range of, I don't know, six or eight recent proposals for individual accounts outlining the key financing, the key benefit issues, the key individual account structures, maybe something such as was prepared for the testimony back in the late 1990's around those proposals. Really the purpose would not be to limit the commission's range of options but to start giving up a better framework for looking at the types of -- the moving parts, the bells and whistles, the tradeoffs. So that's one issue that I would like to ask the staff to start getting going on, maybe for an August meeting if we can do that or early September.

The other issue is that, quite frankly, we just don't have a lot of time. If we're going to produce a report by Thanksgiving, say, we better have most of the work done by October. So the second really big set of issues has to do in my mind with the administrative design and structure, and I would like to start beginning to get some sense of investment options, costs, annuitization problems, some of those things that I haven't thought about as clearly but we need to build those into the framework in order to be able to say something in October, September. So those two issues it seems to me would be very useful to have the staff charged with getting going, a briefing, background material on that.

MR. PARSONS: We certainly will, and I think the staff is working on that, but also we'll be taking -- those are the kinds of things that we're going to be taking some counsel, shall

I say, from public commentators as well. Bill.

MR. FRENZEL: She suggested perhaps sending them after our next meeting. In the case of proposals that are lying around either in Bill form, in press release form or whatever, I would think you could put those together quite promptly and send them to us right away. I don't see any reason to wait.

MR. PARSONS: I think we actually have covered that, and the staff is going to go to work on that as soon as they get back. Sam.

MR. BEARD: I think we're all getting tired. It would be wonderful to quit.

(Laughter)

MR. PARSONS: Bill will entertain a motion to adjourn.

(A chorus of seconds)

MR. PARSONS: Second. Without objection we stand adjourned. Thank you, ladies and gentlemen, for your patience.

(Whereupon, the meeting was adjourned at 3:04 p.m.)