



SOCIAL SECURITY REFORM MUST CONFRONT THE HARD CHOICES

As our leaders in Washington consider the best way to remedy Social Security's long-term funding gap, it is essential for them to confront the hard choices that a meaningful reform plan requires. They should reject both the "do nothing" approach and the "free lunch" plans that rely on substantial long-term borrowing to appear painless. Both offer a false hope.

We, the undersigned, have different views about the best way to reform Social Security. Some of us prefer changes within the current system. Some of us believe that personal accounts, if properly funded, should be part of a comprehensive reform plan. All of us agree, however, that deficit financing is neither a viable nor a responsible way of avoiding the hard choices that must be made on contribution and benefit levels.

Simple arithmetic, not ideology

The basic case for reform is a matter of arithmetic, not ideology. Well within the lifetime of America's baby boomers, the current system faces a growing gap between what it promises in benefits and what we are setting aside to pay for it. Doing nothing to address this problem will eventually result in steep tax hikes, deep spending cuts, or massive borrowing from the public.

Ensuring a more sustainable system will require change, meaning that someone is going to have to give up something—either in the form of higher contributions, lower benefits or a combination of both. No Social Security reform will succeed unless this fact is acknowledged up front.

More debt is not the answer

Responsible reform options must make sense within the context of sound fiscal conditions and the need to raise national savings. Moreover, the fiscal challenges facing Social Security, while substantial, are not as great as the long-term fiscal, moral, and technological challenges we face on Medicare reform. If we can't make the hard choices on Social Security we can never hope to tackle the problems of our health care entitlements.

One reform idea that has received much attention lately is establishing personally owned accounts and "funding" them with borrowed money. Most of the undersigned believe that personal accounts have potential advantages if they are properly funded and adopted as part of a comprehensive reform plan. They are not a free lunch. Simply funding personal accounts with further borrowing, and not with new contributions or contemporaneous benefit cuts, raises many concerns:

- **It would not add to national savings.** A fundamental goal of reform should be to improve national savings. As America ages, the economy will have to transfer a rising share of resources from workers to retirees. This will be easier in a prosperous growing economy. The best way to ensure this is to raise national savings, and ultimately productivity growth. Social Security reform that relies on deficit financing will not boost net national savings, and may even result in lower savings if households respond to the new personal accounts by saving less in other areas. Without additional savings, any gain for the Social Security system must come at the expense of the rest of the budget, the economy, and future generations.
- **It would worsen the already precarious fiscal outlook.** The 10-year cost of roughly \$2 trillion would come on top of the \$5 trillion deficit that appears likely if current fiscal policies are continued. Yet the greater fiscal danger with most such plans is that they require additional borrowing for decades to come. In the most widely discussed plan produced by the 2001 President's Commission to Strengthen Social Security, the magnitude of the borrowing equals or exceeds the cost of the new Medicare drug benefit well into the 2020s. Meanwhile, the increased deficits and debt exceed the promised savings until the 2050s. Official projections already indicate that current fiscal policies are unsustainable long *before* then and the new deficits would only make the problem worse. Savings programmed for the 2050s won't be enough to prevent us from going over the cliff well before that time.
- **It would send a dangerous signal to the markets that we are not taking our fiscal problems seriously.** With our large budget deficit and low domestic savings rate we are borrowing record amounts from abroad. This year's increase in foreign debt is likely to approach \$700 billion. If we "pay for" Social Security reform by running up the debt further, rather than making hard choices, it would signal to increasingly wary financial markets that Washington has no intention of doing what is necessary to get its fiscal house in order. This would increase the risks of a so-called "hard landing" such as a spike in interest rates, rising inflation and a plunging dollar. Promises that all the new debt will be paid back starting in about 50 years are unlikely to satisfy the concerns of those who are watching to see what Washington does now to improve its fiscal position. If markets looked out 50 years, current interest rates would be through the roof.

Because the trade-offs that genuine reform requires can appear painful, many leaders try to find excuses for not confronting the hard choices. Yet the truth is clear. Social Security reform involves real resource trade-offs. It's time to get serious about reform—and face up to the hard choices.

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