

rate for the stock market as a whole, the percentage of new cash allocated to the stock market under the IA plan will fall gradually, until it hits 0.14 percent in 2010.

Revolutionizing. Proponents of the Personal Security Account—PSA—represent the most radical school of thought on the Social Security spectrum. They would split the program into two parts, a basic benefit equivalent to about 47 percent of the current package and a personal savings account where the rest of the benefit that could be invested by the individual in private securities markets. There still would be strings attached, however. The funds could not be withdrawn before retirement. But at early retirement age, people could use the money in their accounts as they pleased. Because benefits now promised would have to be paid until the new plan kicked in, the PSA plan requires a transition phase that would be financed by a new tax of 1.52 percent of payroll, starting this year.

Longman points out that the recommendations are based on the “best estimate” projections from the Social Security trustee’s report. That report projects a shortfall in the next 75 years of 2.17 percent of taxable payroll.

All three options include adjusting the Consumer Price Index down to rein in the growth of spending on Social Security; and, by extension, further cut the budget deficit. The CPI solution is the most divisive and politically explosive.

That’s why negotiators crafting the budget agreement last year fudged the issue, opting for leaving it to the future. Their bet was that economists at the Bureau of Labor Statistics slowly will make the necessary downward adjustment on the CPI, to which Social Security and other government programs are indexed.

The proposed alteration is predicated on the conclusion that the CPI exaggerates true increases in the cost of living by 0.8 percent to 1.6 percent a year. A revised CPI is anticipated to shave budget deficits by an estimated \$1 trillion in 12 years. The annual cost-of-living adjustment for Social Security benefits would fall slightly, with savings estimated at \$10 billion to \$15 billion from 2000 to 2002. For millions of retirees, this would mean somewhat smaller Social Security checks than they would get if the current law stays in place.

The proposal to trim the CPI as a way of fixing Social Security has been in the air since 1994, when the Bipartisan Commission on Entitlement and Tax Reform

warned of an explosion in Social Security spending when the Baby Boom generation begins to retire. The commission forecast that unless far-reaching reforms were enacted, the Social Security fund, which currently has a surplus, would begin recording a deficit by 2013 and become insolvent by 2029.

The Boskin Commission—named after its chairman, economist Michael Boskin—argued that revising the CPI would pump growth rate measurements significantly.

The bias in the CPI stems from several factors, all related to the way the index measures changes in the cost of living by estimating the increased cost of a fixed basket of consumer goods. This implies that the CPI doesn’t keep up with changes in the consumer basket or with how and where the products are purchased. According to the Boskin Commission, the failure to capture important changes in consumer spending patterns accounts for something like a third (or 0.4 percent) of CPI mismeasurement.

An additional 0.1 percent is attributed to the fact a greater—and growing—number of Americans shop at discount outlets. But by far the biggest effect (0.6 percent) arises from the fact that the CPI underestimates the benefits shoppers gain from product quality improvements and the introduction of new products in the market. The BLS, while supporting the Boskin Commission in principle, has disagreed with some of the findings, describing them as “empirically unsound.” The delayed revision of the CPI has retirees smiling, but for how long is a matter for conjecture.

Phil Smith, the senior lobbyist at Prudential Securities who tracks developments that will affect the securities industry, projected that the IA plan is the most politically viable of the three options. As outlined above, the IA plan combines the concept of personal choice and responsibility that are at the core of the PSA plan with the maintenance of a minimum federal safety net for all. While the IA plan would rely on the “double no-no” of a tax increase and reduced fixed benefits, its proponents favor its built-in nod to the diametrically opposed ideological requirements behind the MB plan and the PSA plans.

C. Eugene Steuerle, a senior fellow at the Urban Institute and one of the principal proponents of the IA plan, noted that this also was the only option that would both balance revenues and payouts and also maintain the original promise of Social Security to guarantee a basic level of

support throughout old age. Because the IA plan would limit the growth of future payouts, it would not prompt periodic funding crises such as the current system experiences. To make up the difference between this capped fixed benefit, recipients would receive an individually administered retirement savings plan, individually funded by an additional 1.6 percent payroll tax. But unlike the PSA plan, retirees would be insulated from risks of poorly performing markets or bad investment choices by the capped fixed benefit.

But the plan has its critics. Thomas W. Jones, president and COO of the national teachers’ retirement fund TIAA-CREF, notes that the IA plan does not represent a “harmless compromise.” He argued that the two-tiered system could prompt a wider gap between poor and wealthy retirees—especially if we assume that wealthy retirees who have access to personal financial planners may reap better results from their personal savings accounts because of a sounder asset mix or market timing decisions or both.

Taking the argument one step further, Jones noted that the wealthy may push for a growing percentage of payroll taxes allocated to the individual accounts, further reducing the guaranteed safety net for all retirees. Such an effort, if successful “could lead to the unraveling of the redistributive provision so integral to Social Security and so crucial to its effectiveness.”

In fact, the debates swirling around proposed changes to Social Security have been dominated by such ideological concerns about the role of government and personal responsibility. But before the debate concludes, someone will have to run the numbers and find out just who bears the burden of funding a new plan, and whether government or individuals bear the risk of privatized Social Security investments. Both factors will play a role in shaping compromise and in determining the future of the wealth gap—between retirees themselves and between the young and the old.

Even as these spreadsheets were kicked out, it appeared financial changes in the 60-year-old program are seriously contemplated. In Wall Street parlance, Social Security is in play. 