

# *7.65% Solution*

a Social Security reform proposal

*Answers to the Most Important Questions*

*Regarding Social Security Reform*

### 1. What is Social Security?

Social Security provides retirement, disability, and survivor's insurance to American workers, who pay for this out of a specific tax on their wages—6.2% of the first \$94,200 in earnings. But remember, we're only talking about the retirement portion. In addition, the Medicare system requires each worker to pay an additional 1.45% of their earnings, with no cap, to fund their medical insurance during retirement. The combined amount of these taxes is 7.65%. The employer matches the employee's contribution for a total of 15.3% of earnings.

It is the largest government program in the world. Nearly a quarter of every dollar collected by the taxman goes to pay Social Security.

### 2. How does Social Security work?

It is a pay-as-you-go system. This means that taxes from today's workers pay benefits for today's retirees.

Your payroll taxes aren't saved in an account for the future. Each generation must support the generation that came before it.

### 3. So what is the problem?

Today there are fewer workers supporting each retiree. When Social Security was created, having more workers than retirees wasn't a problem. For example, in 1945 there were more than 40 workers for every retired person. But, people are living longer and having fewer children, meaning that there will be fewer workers. So today there are three workers for each person receiving Social Security, and when people born in the 1960s retire, there will be just two workers to support their retirement.

### 4. So there are fewer workers to pay for current retirees. What does this mean for the system?

Today Social Security is collecting more money than it needs to pay benefits, but by 2017 it will begin running a deficit—collecting less in taxes than it pays in benefits.

### 5. Won't the trust fund help pay benefits and put off the need for tax increases or benefit cuts?

Not really. The trust fund consists of nothing but IOUs that the government has written to itself. And when Uncle Sam goes to repay those IOUs, you know who pays the bill: we do. In order to repay those IOUs, the government will have to either raise taxes or cut benefits.

### 6. Is there more to the problem?

Yes, Social Security is unfair to certain workers. It's unfair to single workers and families where both spouses work; they receive little from Social Security's spousal benefits. It's also unfair to those with short life expectancies who don't live long enough to collect the retirement benefits they've paid for. It's unfair to younger workers, who will pay more than an eighth of their wages all their lives into a program that won't be able to pay them back.

### 7. I'm 35 years old. If nothing is done to improve Social Security, what can I expect to receive in retirement benefits from the program?

Under current Social Security law, at age 69 in 2040 your scheduled benefits will be reduced by 26 percent and will continue to be reduced every year thereafter from presently scheduled levels. (See the 2006 Trustees Report from The Social Security Administration website.)

### 8. So what can we do to fix Social Security for the future?

- A. We could raise taxes. But we've done that 20 times before and Social Security is still going broke. Social Security is already the biggest tax that most workers pay, but to keep the system afloat payroll taxes will have to rise even higher—to 20 percent of each worker's wages. And that's before income taxes, or Medicare taxes, or state and local taxes. Is this what we want for our kids and grandkids?
- B. We could cut benefits. We've tried that, too. But Social Security already leaves millions of seniors in poverty. Do we want to make that even worse?
- C. We could give every worker a personal retirement account that could protect their payroll taxes in an account similar to an IRA or 401(k).

### 9. How would personal accounts work?

As a worker, you would deposit your Social Security taxes in a personal retirement account.

These accounts would hold simple, broadly diversified investments: bond and stock funds.

Personal accounts would build value over time. At retirement, your account would pay your monthly Social Security benefit.

Personal accounts are similar to the federal government's Thrift Savings Plan (TSP). This very popular plan for federal employees and members of Congress allows a choice of five highly diversified, low-cost mutual funds. In the TSP, no direct investments in individual stocks are allowed.

### 10. But how would Personal Retirement Accounts help Social Security?

It's simple: every dollar of retirement benefits paid from a personal account is a dollar the traditional system doesn't have to pay.

Accounts cost more in the short term since we have to build up account balances while still paying benefits to current retirees, but when workers with accounts begin to retire, the pressure on Social Security is reduced.

### 11. Is there a comprehensive plan to solve the Social Security crisis?

Yes, there is a plan and it is called the 7.65% Solution. You see, America has always been a country that respects individualism and self-sufficiency. The 7.65% Solution was created to inject these ideas into the retirement system in order to create a sense of pride and worthiness in each individual that they are personally taking care of their own retirement and health care while eliminating the unfunded liabilities of the current Social Security system.

### 12. Why 7.65 percent?

7.65% is the amount currently withheld from the paycheck of every working American to pay for the government run retirement system. Because the full amount the worker pays would go into their personal account, a tax has been effectively converted into an individual savings account. Once these funds are in the hands of individual Americans they are protected from government takings by the Constitution.

Also, 7.65% of a worker's income is large enough not only to accomplish the goals of Social Security (a bare minimum of food, shelter and health care), but to actually provide a substantially better retirement. Anyone who works consistently can expect their personal account to take care of all their retirement needs including income and health care needs.

### 13. Why does the 7.65% Solution work?

The 7.65% Solution is built on the bedrock solid principle that savings grow at an exponential rate because of the power of compounding interest. As personal account funds are invested the earnings from those investments are added to the personal account and those earnings now become invested assets that earn even more earnings. The principle of compounding never fails.

#### 14. Why is the 7.65% Solution better for individual Americans?

Because 7.65% of wages is paid by both the worker and the worker's company both of these costs become part of the imbedded cost of producing goods and services and are ultimately passed on to consumers. Because the 7.65% payment by the worker alone, if saved and invested in personal accounts, is more than sufficient, over time the requirement for the worker's company to match this payment will disappear. When that occurs all goods and services will be less costly to produce, which will ultimately reduce the price of goods and services to consumers.

#### 15. Why is the 7.65% Solution better for the economy?

Under the 7.65% Solution, personal account assets will be invested in the U.S. economy. These accounts will pump \$400 billion each year into the most productive part of our society—the private sector. This investment represents a large increase in national savings. This national savings will be used by the private sector to expand and improve operations, which will lead to new jobs and increased productivity. Increased productivity will in turn lead to greater wages. 7.65% of these greater wages will be invested in personal accounts, which provides yet more investment.

#### 16. Why is the 7.65% Solution better for widows/widowers and dependents?

The nature of today's Social Security law may deprive a family of much, if not all, of the worker's potential benefits if the worker dies before normal retirement. This unfair situation is remedied by the 7.65% Solution because the entire amount of the worker's personal account can be passed on to the family (or any other assignee).

#### 17. Why is the 7.65% Solution better for young workers?

Current Social Security law taxes all workers at 7.65% of wages regardless of age. Yet, the system does not give workers under the age of 23 any credit for Social Security payments when calculating eligibility for benefits at retirement. This is not fair and the 7.65% Solution corrects this unfairness because every cent deducted from a worker, whether young or old, goes straight into an account that they own and control.

#### 18. Why is the 7.65% Solution better for the poor?

Anyone living paycheck to paycheck knows that it is nearly impossible to build any real savings. One reason nothing is left to save at the end of the month is the fact that the government has been taking 7.65% out of each paycheck. For the working poor the Social Security tax is the largest tax they pay. If, as under the 7.65% Solution, the money withheld from the worker's paycheck went straight to a savings account anyone could build a substantial nest egg for retirement.

#### 19. Why is the 7.65% Solution better for tax payers?

Congress has been raiding every cent from the Social Security Trust Fund and replacing the money with IOUs. Taxpayers are the only source available to provide the money to repay these IOUs. Today, every taxpayer faces a tremendous tax burden if the Social Security system is not fixed. The 7.65% Solution relieves the tax payer of this burden by creating a long-term financially solvent system.

Also, Social Security taxes are not allowed as a deduction against income. Therefore, the money going into the system is taxed. When you begin to receive benefits the amount received in benefits is counted as income and taxed accordingly. You can see that Social Security money is taxed twice. This isn't fair, and this problem is corrected under the 7.65% Solution where your retirement funds are taxed only once.

#### 20. What about my grandparents?

The first rule of Social Security reform: we cannot take away grandma or grandpa's check. Seniors deserve the benefits they have been promised and so we must guarantee full benefits to those who are currently retired and to those near retirement.

The 7.65% Solution doesn't change the benefits of today's retired individuals. In fact, it offers a great new benefit. With today's system anyone working past retirement age is still subject to having their paycheck taxed. Under the 7.65% Solution, post retirement contributions are optional. This gives everyone over 65 an immediate raise should they choose not to continue contributing.

#### 21. Every year I get a "Social Security Statement." Doesn't that mean we already have personal accounts?

No, your money is not saved in an account to pay for your retirement. Under law, the taxes you pay to Social Security go right out again to pay benefits to today's

seniors. The annual "Social Security Statement" you receive in the mail gives you an estimate of the benefits you'll receive at retirement if you keep paying into the program, and if Social Security doesn't go broke or reduce benefits. Those are big if's.

#### 22. If the government can raid the Social Security trust fund, can't they take away my account, too?

Well, nothing's certain but death and taxes. However, personal accounts are a lot safer than the current system, where the government spends every spare penny it can find on other programs.

Where do you think your money is safer: Social Security or your own bank account? Neither is totally safe, but a personal account is your best bet. Possession is nine-tenths of the law and it's easier for the government to refuse to pay the benefits it owes you than to take back the savings you've already got.

#### 23. I know I could handle my own investments, but what about people who've never invested before?

Making accounts safe and easy for new investors is probably the biggest Social Security reform concern. But, over 25 countries around the world have personal accounts, and reformers have learned a great deal about how to do it and how not to do it. In other words, we will not be the guinea pigs in a personal account experiment. It's already been done—successfully. Here's what reformers have learned:

- A. Accounts would be voluntary—anyone who didn't feel comfortable with an account could, at retirement, choose whether to accept their personal account or all of the benefits promised under the current Social Security system.
- B. Account investments would be made simple. There would be five simple funds of bonds and stocks. You could not invest in single companies or in anything exotic.
- C. For workers who don't want to, or forget to make a choice, a safe and diversified default plan would be set up. Even if they never looked at their investments, the default mix of stocks and bonds would pay decent returns without taking on too much risk. A worker could do absolutely nothing and they'd still get a good deal.

## Questions & Answers

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We know this model works. The Federal government's Thrift Savings Plan gives government workers a few simple, low-cost investment choices. Government workers have successfully invested; all Americans should be given the same opportunity.

### 24. You make it sound too good to be true.

Sure, there are a lot of good things about personal accounts. But no one's pretending that Social Security reform will be easy.

Fixing a Social Security system that's trillions of dollars in the hole will be tough, with or without personal accounts. But accounts make those tough choices just a whole lot easier.

Since accounts can pay higher benefits than the current system, they make the other steps needed to balance Social Security's books easier to bear.

### 25. Right now, Congress spends the surplus Social Security taxes. If, instead that money goes into individual retirement accounts, what will the government do to make up the shortfall?

The government's choices are tax or cut or borrow. And right now, the government is hiding some of its borrowing, by taking from the Social Security trust fund. Individual retirement accounts would take that option away and force the true costs out into the open. If the government wants to keep on borrowing, that's its business; but it shouldn't be borrowing our Social Security money.

### 26. These accounts sound ok, but won't they be expensive? Will Wall Street fees eat up my account balance?

No, all personal account investment options will be approved by an appointed board of experts established to ensure that the accounts are diversified, have a strong track record and reasonable fees. Fees will be kept low by this board and by intense competition among investment providers.

### 27. How exactly will individual retirement accounts be managed? By a government agency? By private business, with oversight by government? What sort of regulatory body?

Many of us don't trust our institutions. We don't trust government, we don't trust business, and we don't trust the regulators. So what works? 401(k) and IRA accounts are owned by the individuals, but managed by companies with governmental regulation and oversight. This is a winning combination.

The 7.65% Solution proposes that account oversight be handled by an independent advisory board, similar to the Federal Reserve. So your Social Security Protected Account investments will be approved neither by a government bureaucrat nor a stockbroker, but by an independent regulator who is looking to provide you with the safest, best performing investments possible.

### 28. What about the market crash? How can you even suggest investing in the stock market in a time like this?

Let's be honest, the stock market crash hurt a lot of people, and shook American's faith in investing.

But retirement investing is about the long term, and over the long term the stock market's day-to-day ups and downs even out. Over 20 years or more, the stock market has never lost money—even including the Great Depression.

And personal accounts aren't just about stocks. Workers could own AAA corporate bonds.

Ask yourself this: would you rather own a bond that's never been defaulted on or pay your money into Social Security, which the government can cut if it chooses?

### 29. I am receiving disability benefits from Social Security. Should I be worried that my monthly check will be cut?

This plan does not reduce the benefits of currently disabled beneficiaries.

### 30. Why don't the unions support Social Security reform?

The unions have a vested interest in the current retirement system and they spend millions of dollars each year influencing elections to protect their power base. If workers were given a personal retirement account they could secure their own retirement instead of relying on union pension programs. This would make union membership unnecessary for a secure retirement and would take away a big union money maker—managing pension funds.

### 31. Why doesn't the AARP support Social Security reform?

The AARP also has a vested interest in the current system because they make big money helping seniors invest their savings. If workers were given personal accounts there would be less need for AARP investment services which would mean lost revenue from investment fees as well as less incentive to join the association.

### 32. Why is it that some legislators, Republican and Democrat alike, don't support Social Security reform?

Some legislators fear that groups like the unions and the AARP that support their campaigns will withhold their campaign contributions. Other legislators are stuck in the past and fear that Social Security reform is the "third rail" of politics. What it really boils down to is the fear that they will not get reelected.

What those legislators who fail to support Social Security reform do not realize is that Americans know Social Security must be fixed and they are looking for leaders who will stand up and do the right thing.

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