



## Peter, Paul and Barry: A Contrast in Economic Policy Visions

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Over the past few months, the Obama White House has taken a beating over its proposed policies, with its ideas on health care reform and the federal budget deficit arousing the most intense opposition. As public understanding of the Administration's economic plans has grown, support for these plans has declined. These concerns have been reflected in the President's steadily declining poll numbers, and sudden electoral shifts in Virginia, New Jersey and Massachusetts have underscored the opposition.

Over the past week, the White House began trying something new: changing the subject from their own proposals to those of Congressional Republicans. This is a marked departure from the past several months, during which the White House alleged repeatedly – and wrongly – that Republicans were obstructing necessary legislation with no alternatives of their own. But now, the White House has decided it is time to acknowledge that Republicans have been offering ideas – and to attack them.

The chief target chosen for White House criticism has been Congressman Paul Ryan (R-WI). He has put forward a vision for resolving the federal government's fiscal crisis, entitled "A Roadmap for America's Future", which was first unveiled in 2008. It includes detailed proposals to restructure the most politically-sensitive programs of all – including Medicare and Social Security – whose reform is essential to repairing the nation's fiscal outlook.

Along Pennsylvania Avenue, the tone of the exchange has been mostly respectful even as the substantive

debate has been vigorous. Both the President and Director Orszag were careful to compliment Mr. Ryan personally even as they attacked his ideas. Ryan, who worked closely with Director Orszag when the latter was director of the Congressional Budget Office, has also focused on substantive differences in his public responses.

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Still, there have been times when the mask of comity has slipped. In at least one interview, Director Orszag described Ryan's proposal as introducing "privatization into Social Security." This is untrue. Although the Ryan proposal would allow workers to save part of their Social Security payroll taxes in personal accounts, there would be no privatization; both the savings component and the pay-as-you-go portion of the program would be publicly administered (just like the personal Thrift Savings Plan accounts that are available to federal employees). "Privatization" is, of course, one of the left's favorite Social Security buzzwords, used to scare seniors without regard for accuracy.

The White House wants the public to believe two things about the Ryan roadmap: first, that it would be implemented if Republicans control Congress and the White House; and second, that the ideas it advances are ill-advised.



Is it fair to hold up Congressman Ryan's personal ideas as a stand-in for a broader Republican alternative agenda? It's roughly as fair as it is to use the OMB Director's policy ideas as a stand-in for the Administration's – at least on any subject that the President has not yet declared a policy. Due to his position and his substantive knowledge, Congressman Ryan's views will carry weight within the Republican caucus. Similarly, due to his position and his substantive knowledge, OMB Director Orszag's views will also carry great weight within the Administration. Neither's views are dispositive; both are influential.

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The parallel, of course, isn't exact. Clearly the views of Congressman Ryan, as an elected official, deserve attention in the way that no unelected individual's ideas can wholly claim. But just as clearly, the views of the Administration's Cabinet-level officials matter greatly. Given this parallel, it seems useful to compare and contrast the competing visions of Congressman Ryan and Director Orszag on Social Security.

The Ryan roadmap relies principally on two changes to shore up Social Security's finances: progressive indexing – first developed by Robert Pozen (a former vice chairman of Fidelity Investments and currently chairman of MFS Investment Management as well as a senior lecturer at Harvard Business School), later embraced both by President Bush and Senator Robert Bennett – as well as indexing the retirement age for changes in longevity. Progressive indexing would essentially entail calculating benefits for high wage earners based on price growth rather than wage growth, which grows slightly faster. This

would result in slightly reduced benefits for high wage earners than currently promised under current law, but would still result in benefits with the same purchasing power as beneficiaries receive today. These two changes are by themselves sufficient to balance Social Security without raising taxes. In fact, they would create a small amount of additional savings to pay for an additional provision in the Ryan plan; to increase the benefit safety net for low-income workers.

The Ryan proposal also contains optional personal accounts. Because the accounts are voluntary, however, and because their guaranteed value is limited, participation is expected to be limited as well. As a result, scorekeepers believe that the plan's financial contours will be shaped primarily by the benefit re-indexing provisions.

The Ryan plan represents a value choice to solve the Social Security problem on the cost-containment side rather than by raising taxes. Even under this choice, future Social Security beneficiaries will still have higher benefits, in real terms, than those paid today.

Mr. Orszag has also co-authored a Social Security plan. It represents the opposite value choice: to solve the Social Security problem almost entirely by raising taxes. The Orszag plan, which he co-authored in 2003 with MIT professor Peter Diamond, contains a number of modest benefit changes, but over the next 50 years – during which the entirety of the Social Security cost explosion takes place – cost reductions are so limited that, when combined with other provisions to increase costs, the plan as a whole would not contain programmatic cost growth at all.

What Social Security taxes would increase under the Diamond-Orszag plan? Pretty much everything



you can think of. Start with the payroll tax; the 12.4% rate would begin to gradually rise, topping 13% in the 2030s, 14% in the 2050s, and 15% in the 2070s. These tax hikes would hit the lowest-income workers as well as the highest-income workers.

In addition, the Diamond-Orszag plan would apply an additional 3% surcharge on all income above the Social Security tax base cap (currently \$106,800, though raised under the plan.) This additional 3% surcharge would not be considered in benefit calculations, permanently ending Social Security's historical practice of earning benefits whenever contributions are made. And, starting in 2023, this 3% tax rate would also begin to rise gradually over time.

But wait – there's more. The plan would also raise the cap on taxable wages. An updated estimate for the effect of this tax increase is not available, but data from the Social Security Administration's website suggest that the full 12.4% tax would ultimately need to be extended from today's \$106,800 up to the equivalent of at least \$140,000. The plan would also raise substantial Social Security revenue by requiring state and local workers to join, to which many are unalterably opposed.

The Diamond-Orszag plan also contains a number of other complex changes to the Social Security benefit formula, some of which decrease benefit growth for high-earners while creating additional protections for low-income workers, widows and the disabled. The overall fiscal effects of these provisions are slight, however, in comparison with the tax increases.

Because the plan relies so heavily on tax increases, the Congressional Budget Office found in 2004 (before Orszag became CBO Director) that the plan would reduce economic growth and personal savings. As CBO wrote, "Calculations based on

a life-cycle growth model suggest that, under the proposal, real (inflation-adjusted) GNP could be between 0.7 percent and 0.8 percent lower in 2025 – and between 1.5 percent and 1.7 percent lower in 2080 – than it would be under the 'trust-fund-financed benefits' baseline scenario." CBO explained, "The macroeconomic effects of the proposal stem largely from the fact that it would raise payroll tax rates" and further that, "CBO's simulations suggest that under the Diamond-Orszag proposal, the capital stock would be 0.8 percent lower in 2025 and between 0.8 percent and 1.4 percent lower in 2080."

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Both Director Orszag and Congressman Ryan deserve credit for placing fully fleshed out Social Security plans on the table. But as the White House directs public attention to the Ryan Social Security proposal, the public should remain aware of the alternative vision advanced by senior Obama Administration officials. It is a vision of higher taxes and slower economic growth.

The Ryan and Orszag proposals represent competing visions of how the United States deals with our fiscal dilemma. Under Congressman Ryan's vision, we try to live within our projected revenues, leave our children with tax burdens comparable to our own, and constrain our spending appetites accordingly. On the Social Security side, this means slowing the growth of benefits -- which would still grow faster than inflation.

Under the alternative vision espoused by Orszag, we would impose on younger generations higher payroll



tax rates, tax a higher fraction of national wages, and levy an additional 3% benefit-less surcharge, thereby reducing economic growth and individual saving.

The contest between the Ryan and Orszag visions for Social Security is the fundamental contest between constraining our spending appetites and raising taxes to fuel persistently higher costs. It mirrors the gap between the Obama Administration's larger fiscal policies, and the views of American voters on the political center and on the right.

Let the debate begin.