Should Women Support the Privatization of Social Security?

John Williamson

Women have been forgotten in the current debate over the privatization of U.S. social security. Almost every current proposal would put retired women at a disadvantage to men.

Five years ago very few people took proposals to privatize social security seriously. Today such proposals are being given very serious consideration. Attention to this issue has increased with the recent release of three alternative proposals for reform by the Advisory Council on Social Security, two of which call for partial privatization.¹ In view of this, it is time to remedy the near silence with respect to the implications for women. Many privatization proposals, including those recently made by the Advisory Council, would have bad economic consequences for women.

The Maintenance of Benefits plan, the least controversial of the three proposals by the Advisory Council, suggests that 40 percent of the Social Security Trust Fund be invested in the stock market. It calls for a number of other less controversial changes that translate into modest benefit cuts and tax increases, but it

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Williamson does not call for the partial privatization of social security. The most radical of the two privatization proposals is the Personal Security Accounts plan, which would transform social security into a two-tier scheme. The first tier would be a flat-rate benefit of $410 (in 1995 dollars), which is 65 percent of the poverty level for a single person living alone. The second tier would be mandatory personal savings accounts, similar to IRAs, financed by diverting the lion's share (5 percentage points) of the employee payroll contribution into these accounts. The second privatization proposal is the Individual Accounts plan calling for the creation of mandatory individual savings accounts managed by the federal government. These accounts would be financed by a 1.6 percentage point increase in payroll contributions paid entirely by employees. Both of the partial privatization schemes call for a number of other changes that translate into increased taxes and benefit reductions.

Although many women have reason to be concerned about these proposed changes, this is not true for all women, notably women with high-wage jobs. Such women would be less likely to be adversely affected by proposed cuts in spouse benefits and more likely to benefit from proposed changes in the formula used to compute survivor benefits. Affluent women would face some new risks, but overall most would come out ahead as a result of privatization, despite the risks to the well-being of women more generally. An important difference between these women and those in low- and middle-income households is that affluent women can better afford to invest a substantial portion of their social security assets in the stock market. The risk to women referred to here means the risk to the majority of women—those presently living in low- and middle-income households and those who, due to business reversals, divorce, disability, or the death of a spouse, will unexpectedly end up in such households.
Also, affluent women are not highly dependent on social security for retirement income, but middle- and low-income women are much more dependent on this source of income. More affluent women can more easily delay retirement a few years if need be in response to a dramatic drop in stock or bond markets. They tend to be in better health and have jobs that are physically less demanding than those held by others.

The partial privatization provisions of the Individual Accounts proposal and particularly the more radical Personal Security Accounts proposal put all low-wage workers at risk. One of the largest of these risks is investing in the stock market. If we could count on the stock market to continue to perform as it did between 1982 and 1996 there would be few complaints. But if the stock market declines just before retirement, low-wage workers would be particularly vulnerable. The stock market did not return to its pre-crash 1929 level until 1954. More recently it took almost a decade to return to the 1972 market high following the 48 percent decline between 1973 and 1974.

Because women are more likely to be low-wage workers, a greater proportion of women live on the margins of poverty in old age. This is true despite the trend toward higher wages and full-time careers for women. It is particularly true for elderly women who are divorced or widowed. Because of their lower pre-retirement wages, they enter old age with less financial assets. As a result, they are less able to tolerate the risk of a substantial drop in retirement income of the sort that could accompany a sharp drop in the stock market just before retirement.

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vestment advice. Many invest too conservatively during their early working years due in part to low income and in part to the tendency for women to be more risk-averse investors. There are also some women who take too much risk during the years just before retirement. Many workers, particularly more risk-averse female workers, are going to experience investment gains that are far below the long-term rate of return for the overall stock market, the rate so frequently promised by advocates of privatization.

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In the more radical privatization plan, yet another kind of risk arises because assets accumulated in the mandatory personal savings accounts would belong to the workers who contributed to these accounts. This would put many married women at a disadvantage relative to their often higher-earning husbands. As Advisory Council member Edith Fierst points out, upon retirement the husband could quickly spend this money, leaving his wife and himself with little to live on over a potentially long retirement.\(^3\) When a husband dies, the funds in his account become part of his estate. Often the money goes to his widow, but some men elect to give a substantial portion of these funds to other beneficiaries.

The three proposals for social security reform differ on many issues, but a majority of the Advisory Council members agree
on a number of points, all of which will have a more disadvantageous impact on women than on men. These include the need to increase the number of years of a worker’s earnings history used to compute the size of a worker’s benefit (from 35 to 38 years), to change the date by when the age of eligibility will be increased to 67 from the year 2022 to 2011, to reduce the spouse benefit from 50 to 33 percent of the covered worker’s basic benefit, and to shift to a less generous consumer price index (CPI) when adjusting pension benefits for inflation.

If the number of years of a worker’s earnings used to compute benefits is increased from 35 to 38, benefit levels will generally fall. Because women are more likely to be out of the labor force or in part-time jobs for more years than men, this change will force more women than men to include in the formula years during which their wages were low. Of women who will retire in 1999, approximately 15 percent will have 38 years of covered employment. The corresponding estimate for men is 57 percent. In short, this change will reduce benefits for both men and women, but the adverse impact will be greater for women.

The call in both privatization proposals to advance the date of normal retirement to age 67 will reduce pension benefits for both men and women between 2011 and 2022. This might affect women more adversely than men, but only if they are less responsive than men to the increased penalty for early retirement, which could happen given that their income is typically a smaller share of the total family income. Married women are more likely than their husbands to retire early. While early retirement is generally assumed to be voluntary, for many women it is in part a response to pressure from husbands. Some husbands have health-related personal-care needs. Some want their wives to make a retirement-related residential relocation, and others want them to share in travel or other leisure activities. Increasing the normal retirement age will yield a modest increase in the aver-
age of retirement, but at the same time it will produce an increase in the number who take early retirement and the associated reduction in pension benefits.

In both privatization proposals there is a provision that would further increase the normal retirement age after 2011 as life expectancy increases. This provision would tend to further depress pension benefits for both men and women, but for the reasons just mentioned it could have a more adverse affect on women than on men.

A majority of the Advisory Council members support a proposal to reduce the spouse benefit from 50 to 33 percent of the covered worker’s benefit albeit with a corresponding improvement in the surviving spouse benefit. This change would reduce benefits for married couples who are rarely poor and the money saved would be used to finance a more generous benefit for many surviving spouses who are often poor. Instead of the current aged survivor’s benefit, which is equal to 66 percent of the combined husband–wife benefit, the new benefit would increase to 75 percent of the combined benefits. For many surviving widows this would yield a higher benefit than under the current scheme. Thus, while this change would represent a benefit cut for many married couples, it would be compensated for with a benefit increase for many widows who tend to be more needy. However, while benefits would be higher for widows who had worked, they would not be higher for widows who had been non-working wives.

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women would not do as well as they do with social security as currently structured. Today a divorced woman can benefit from that part of a former husband’s earnings record which is based on earnings during the years after the divorce. This would not continue. Currently at the death of the former husband many divorced women become eligible for his full-pension benefit. Under the Personal Security Accounts plan the extent to which a divorced woman could share the assets in her former husband’s personal savings account would depend on the divorce settlement because these assets would be defined as his property. While this would be a less-favorable option for most divorced women than current policy, it would at least give these women an opportunity to share their husband’s assets, an opportunity that not all married women would have under the Personal Security Accounts plan. Under the Individual Accounts plan a divorced woman would have no claim on her former husband’s individual account so long as he was alive. At his death she would become eligible for only half of his benefit from his mandatory individual account.

If the formula used to make annual cost of living adjustments (COLAs) in pension benefits were modified to reduce the size of those adjustments, the impact would not amount to much in the short run; however, in the long run it would be very substantial. The impact of the 0.21 percent reduction suggested by the Bureau of Labor Statistics and the Advisory Council would be much less dramatic than the 1.1 percent reduction recently proposed by economist Michael Boskin. But even a 0.21 percent

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reduction would have a substantial impact over the long run. The risk of a serious cut in pension benefits would be greatest for those who live longest after retirement. Given the gender difference in life expectancy, the adverse impact of any downward adjustment of the CPI would be greater for women than for men.

The decrease in pension benefits relative to the present scheme is only one aspect of the problem for women. Because of longer life expectancy, women are more likely to live long enough to deplete other supplemental sources of income. Thus, not only would pension benefits be lower, the impact would be compounded by less income from other sources.

The argument is often made that the proposed change in the CPI (whether a 0.21 or a 1.1 percent COLA reduction) is merely an effort to shift to a more accurate measure that does not overcompensate the elderly during their retirement years. If it were possible to come up with a measure of the cost of living that fairly measured changes in the cost of living for all population subgroups, it would be easy to defend the proposed cuts. But there is a great deal of controversy about how to measure changes in the cost of living.6

Even if we agree that a new CPI would give a more accurate measure of changes in the cost of living for the overall population, this does not mean that it would give a more accurate measure for the elderly, particularly the very elderly. There are a number of ways in which consumption patterns for the very elderly differ from the rest of the population—for example, spending on health care. Since the very old are disproportionately low-income women, the adjusted index will hurt women more than men. It is difficult to defend this gender inequity until there has been more discussion about how accurately the new index measures changes in the cost of living for the very elderly. The evidence suggests that the current CPI underestimates increases in the cost of living for the elderly, a problem that gets
worse for the very elderly with obvious implications for women.⁷

Given that the COLAs after retirement do not make any effort to adjust for increases in the standard of living (the increase in real wages) and given that women on average depend upon their social security pensions for many more years than do men, there is reason to question the claims of those who assert that elderly women, particularly very elderly single women, are presently being overcompensated by social security. In light of the evidence that 40 percent of elderly widows live below the poverty line, can a case be made that a shift to a less generous CPI is called for to avoid overcompensating them? While it would be unfair to suggest that this proposed change is targeted at elderly widows, it is relevant to ask why provisions have not been made to protect this segment of the elderly population. Very elderly single women are not making major advances in the standard of living relative to the general population.

What about working women who receive spouse or widow benefits based entirely on the work histories of their husbands? Jonathan Forman, a University of Oklahoma law professor, argues that these women would do better under privatization than under current law.⁸ It seems simple. Currently they are receiving nothing back for their social security taxes, and they would at least receive some return for their contributions under either of the proposed privatization schemes. Many of these women will have held high-paying jobs and will have had long work histories. Typically they would be better off. But a majority would do worse than under the current scheme. Some will have earnings that are sufficiently low that they will still find it to their economic advantage to take even the dramatically reduced spouse benefit. While many of these same women would subsequently benefit from the change in the formula used to compute widow benefits, not all would do better with 75 percent of the couple's combined benefit. For working women with lower
incomes, it is likely that the most significant adverse consequences would be the market risk the couple’s combined retirement savings would be subject to. The wife would suffer along with her husband in the event of an unexpected and prolonged stock market decline in the years just before retirement. They would also both suffer the consequences of bad investment decisions over the pre-retirement years and the consequences of the less-generous COLA adjustments that are part of all three Advisory Council proposals.

The defense for many of the cuts that adversely affect women is that cuts must be made to reduce the projected long-term increase in social security spending levels. While some cuts will have to be made, we should insist that proposed changes (either individually or taken together) impact women to the same degree as men. We need to find ways to close the projected gap between revenues and expenditures that do not increase the relative burden on women, particularly on the most vulnerable categories of women.

One alternative would be to increase or remove the cap on the level of wage income that is subjected to the social security payroll tax. A related alternative would be to remove the cap on the employer’s portion of the social security tax, as has already been done for the Medicare tax. Yet another alternative would be to tax all compensation, not just wage compensation. If all or a portion of fringe benefits were taxed as ordinary income, much of the increase in the tax burden would fall on those with higher incomes who tend to be men. While a policy shift that increases the tax burden on men relative to women would be hard to justify in the name of gender equity, it might be appropriate as part of a package that includes one or more of the policies being considered, which would contribute to an increase in the burden on women. In the event it proves difficult to come up with individual policy changes that do not affect men and women equally,
it might make sense to consider a package of changes that taken together do not burden one gender more than the other.

Despite the high level of current interest, there is a good chance that both of the Advisory Council’s proposals calling for the partial privatization of social security will be rejected at least in their current forms. A major reason may turn out to be opposition from women. Due in large part to the near total absence of media discussion of the implications for women, there is no evidence of a gender gap on the issue today. Once the implications for women become clear, however, a substantial gap may emerge. If either of these proposals gets close to enactment, the media will begin to pay closer attention to the issue of who stands to gain and who stands to lose. At that point the implications for women will be widely discussed. For most women the potential gains from privatization are much less than advocates of privatization suggest and the potential risks much greater.

Notes


Erratum

We regret the error in the equations in note 9 in the article by Wynne Godley and George McCarthy, “The Boskin Commission’s Trillion-Dollar Fantasy” (May–June 1997). Following is the correct note text:

9. These figures may, however, have some interest insofar as they shed light on how we made the calculations. Note that our figure for the effect on the deficit in 2008, which includes feedback, is the same as the Boskin Commission’s, which does not. The reason for this is that the lower inflation in our simulation reduces entitlements measured in nominal terms below what the commission recommends, and this counteracts the “multiplier” and other secondary effects. Is it mysterious that our estimate of the effect on debt in 2008 is so much lower than the commission’s? The reason for this is that our method, which uses proportions of GDP, will only “score” changes to debt measured at one price level. Formally, the problem resembles that used for the calculation of the inventory valuation adjustment. Thus, by identity, \( \Delta d_p = \Delta D - \Delta p \cdot d_0 \) where \( d_0 \) is the debt (in 2008) measured at pre-cut prices, \( \Delta p \) is the difference to prices made by the cut and \( D_1 = d_1 \cdot p_1 \), \( D_0 = d_0 \cdot p_0 \). Our contention is that the terms \( \Delta p \cdot d_0 \) and hence \( \Delta D \), have no relevant meaning.