

SOCIAL SECURITY AND RACE

Staff Report

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**NATIONAL CENTER FOR POLICY ANALYSIS
7701 N. Stemmons Suite 800
Dallas, Texas 75247
214/951-0306**

EXECUTIVE SUMMARY

Black and white workers earning the same wages pay identical Social Security taxes. Yet because of their higher mortality rates, black workers will receive far less in Social Security benefits than their white cohorts. On the average:

- A white male at birth can expect to live more than six years longer than a black male.
- During his working years, a black male has twice the probability of dying in any given year than his white counterpart.

As a result, fewer blacks than whites will live long enough to become eligible for Social Security retirement benefits, and among those who do, blacks will receive fewer monthly benefit checks than whites. Specifically:

- A white male entering the labor market today can expect to receive 74 percent more in Social Security retirement benefits and 47 percent more in Medicare benefits than a black male.
- A white working couple can expect to receive about 35 percent more in retirement and Medicare benefits than a black working couple.

To the degree that black families succumb to the lure of the federal welfare system, the Social Security system heaps additional penalties upon them. Currently,

- The divorce rate for black women is more than twice the rate for white women, and the percentage of white women who currently are married is about 50 percent higher than for black women.
- Almost 60 percent of all black children are born to unmarried women--more than four times the rate for white children.

These differences help many black women qualify for welfare benefits, but they also result in huge losses of benefits from Social Security. For example,

- Among low-income couples, a married white couple will receive about \$27,000 more in Social Security benefits than an unmarried black couple.
- Among median-income couples, a married white couple will receive about \$36,000 more than Social Security than an unmarried black couple.

The vast majority of blacks of working age would gain financially if the Social Security system were immediately abolished. They would be even better off, if the system had never existed. For example,

- A 50-year-old black couple--each earning only 50 percent more than the minimum wage--would have accumulated \$92,000 today had they been permitted to invest their Social Security taxes in the stock market.
- With no additional savings, this couple could expect to accumulate more than \$184,000 by the time they reach age 62.

INTRODUCTION 1

In no other area of economic life are the interests of black Americans more divergent from the goals of the architects of the modern welfare state than with respect to the Social Security system.² Because Social Security retirement benefits and Medicare benefits are based on age, these programs discriminate against blacks and other minorities who have higher mortality rates and shorter life expectancies. On the average, black Americans are over-represented among those of taxpaying age and under-represented among the elderly population. Although blacks and whites face the same payroll tax rates during their working years, black workers at every age can expect to receive fewer monthly retirement checks from Social Security than their white cohorts.³

The discriminatory nature of Social Security has been a permanent and enduring feature of the system since its beginning:

- In 1940, the first year the Social Security system began paying benefits, the life expectancy of a black male was only 51.5 years.⁴
- As a consequence, only a small fraction of black males born that year had any hope of receiving retirement benefits from a system they would support with their taxes.

¹This report was prepared by John Goodman, Peter Ferrara and the NCPA staff. We would like to thank William T. Rule, III for technical assistance.

²Unless otherwise noted, the term "Social Security system" refers to Social Security retirement benefits, Medicare benefits, survivors and disability benefits and the payroll tax used to finance these benefits.

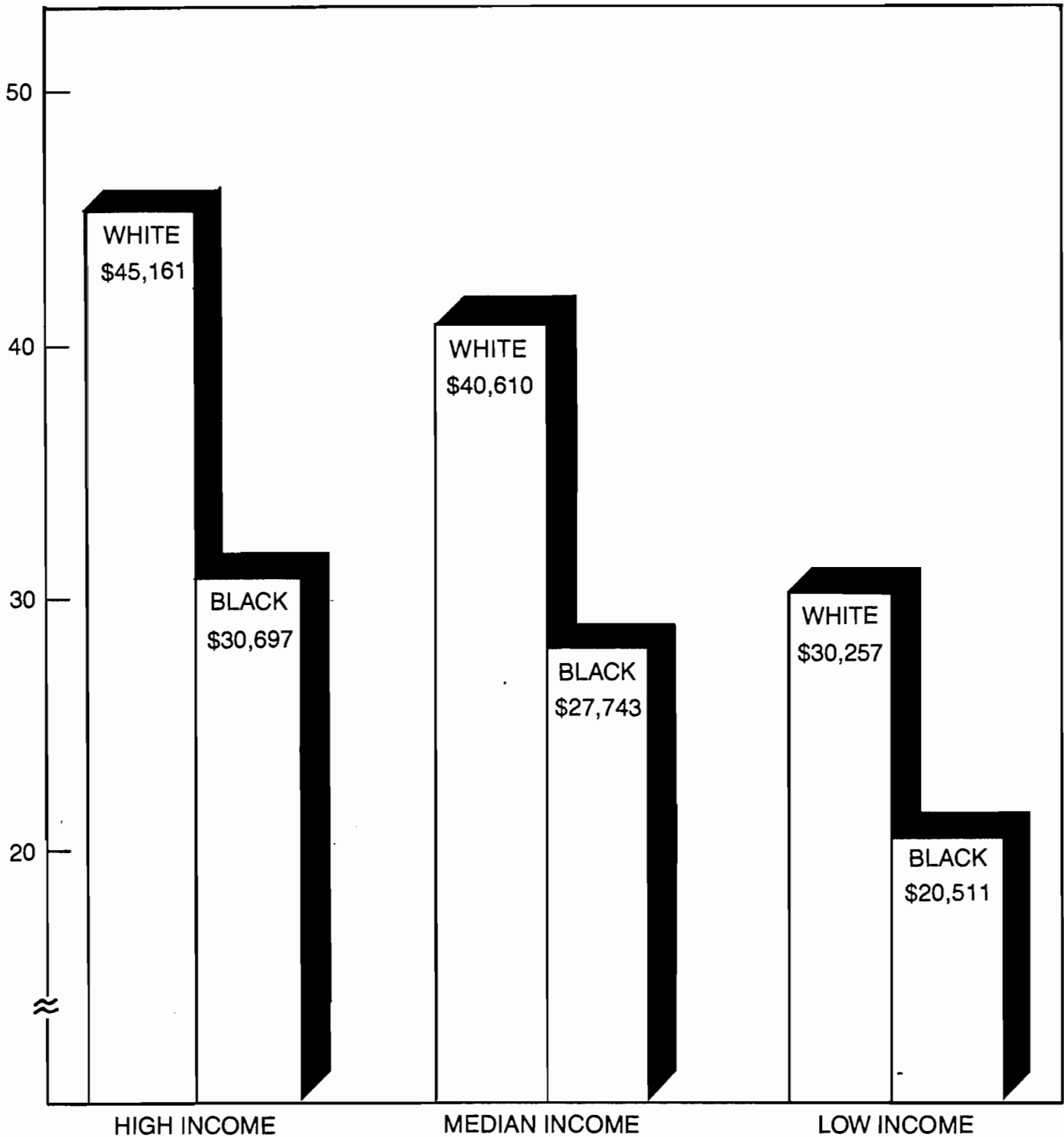
³For an earlier analysis of the different treatment given to blacks and whites under Social Security, see "The Effect of the Social Security Reforms on Black Americans," NCPA Policy Report #104, National Center for Policy Analysis, July, 1983.

⁴Technically, this life expectancy is for "black and other non-white" males. Separate calculations were not made for blacks until 1970 by the U.S. National Center for Health Statistics. Life expectancy for white males in 1940 was 62.1 years. See Statistical Abstract of the United States, 1987, (Washington, D.C.: U.S. Government Printing Office, December, 1986), Table 105, p.69.

EXPECTED SOCIAL SECURITY BENEFITS FOR 20-YEAR-OLD SINGLE MALES

(in 1986 prices)

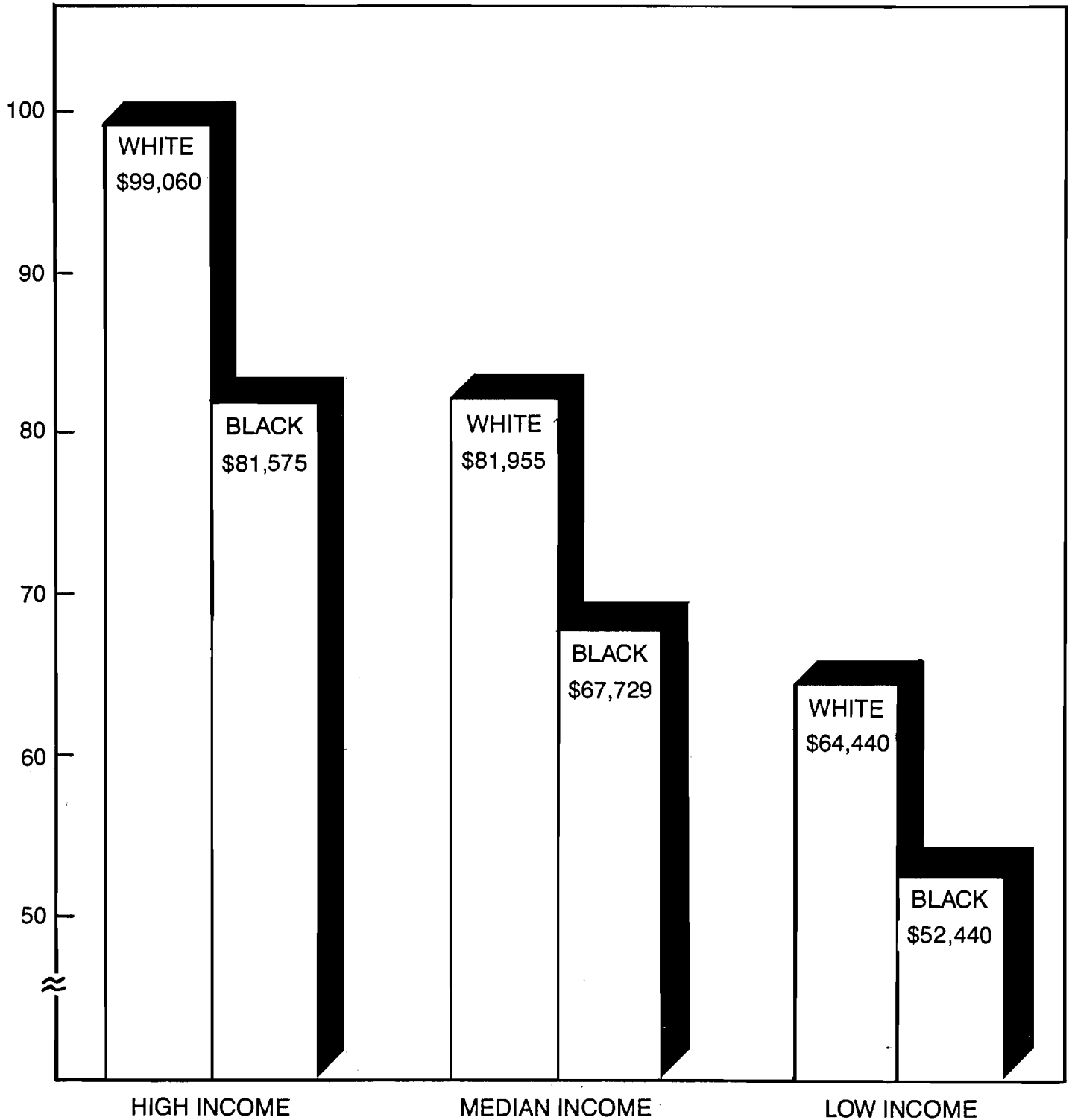
\$
thousands)



EXPECTED SOCIAL SECURITY BENEFITS FOR 20-YEAR-OLD WORKING COUPLES

(in 1986 prices)

\$
ousands)



Source: National Center for Policy Analysis

During the years that followed, life expectancy improved for both blacks and whites. However, by the time life expectancy for a black male at birth had reached 65, Congress raised the official age at which he could retire:⁵

- 1983 marked the first year in which life expectancy for black males reached a point (65.1 years) where the average black male could expect to live long enough to become eligible for full Social Security retirement benefits.
- Yet that same year, Congress eliminated the one-month benefit check the average black could expect by raising the official retirement age to 67.

The Bureau of the Census identifies 15 different racial groups in American society. The only groups for which there are reliable mortality tables, however, are blacks and whites. As more research is done, we may discover that there are striking differences in mortality and life expectancy among the other 13 racial groups. For the moment, what is known about the differences between blacks and whites and the implications for Social Security is shocking.

Programs for the elderly already consume more than 25 percent of the federal budget. Sometime in the next century they are likely to consume more than 50 percent of the federal budget. The payroll tax rate needed to fund these programs may exceed 40 percent of workers' incomes by the middle of the next century.⁶ Yet these programs, which are making an ever-increasing claim on our national resources, are inherently discriminatory with respect to race.

⁵The higher retirement age will be phased in between the years 2003 and 2027. See "The Effect of the Social Security Reforms on Black Americans," p. 6.

⁶Projections of the future of Social Security are made annually by the Social Security Administration. For the latest projections, see the 1987 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Trust Funds. For an analysis of these projections and the assumptions on which they are based, see "Social Security: Who Gains? Who Loses?," NCPA Policy Report No. 127, National Center for Policy Analysis, May, 1987, pp. 6-10; Rita Richardo-Campbell, "Social Security Reform: A Mature System in an Aging Society" in John H. Moore, ed., To Promote Prosperity: U.S. Domestic Policy in the Mid-1980s, (Stanford, California: Hoover Institution, 1984); Peter J. Peterson, "The Coming Crash of Social Security," The New York Review of Books, December 2, 1982; A. Haeworth Robertson, "The National Commission's Failure to Achieve Real Reform" and Paul Craig Roberts, "Social Security: Myths and Realities," in Peter J. Ferrara, ed., Social Security: Prospects for Real Reform, (Washington, D.C.: Cato Institute, 1985); and James R. Capra, Peter D. Skepardas, and Roger B. Kubarych, "Social Security: An Analysis of its Problems," Federal Reserve Bank of New York Quarterly Review, Autumn 1982.

LIFE EXPECTANCY AND RACE

Students of Social Security have long known that, on the average, women live longer than men and whites live longer than blacks. Among full-time workers with identical earning abilities, therefore, Social Security offers a better deal to women than men and a better deal to whites than blacks.

At one time it was widely believed that the life expectancy gap between men and women would narrow as women moved into the labor force and begin working in male-dominated occupations. By and large, that has not happened. Similarly, although the life expectancy gap between blacks and whites has narrowed over the post-World War II period, a substantial gap still remains, and we can have no confidence that it will disappear in the foreseeable future.

Current Life Expectancy Estimates

The most recent life expectancy tables produced by the U.S. National Center for Health Statistics are for the year 1984. On the basis of these estimates,⁷

- A black male, born today, has a life expectancy of 65.5 years.
- By contrast, a white male, born today, has a life expectancy of 71.8 years.

These estimates imply that if there is no change in mortality rates over the next 70 years, black males can expect to receive far fewer Social Security benefits than white males. Specifically,

- Although he will pay Social Security taxes throughout his working life, a black male born today, can expect to die 18 months before he is eligible for full Social Security retirement benefits.⁸
- By contrast, a white male born today can expect to receive 4.8 years of full Social Security retirement benefits.

⁷Statistical Abstract of the United States, 1987, Table 105, p. 69.

⁸As noted earlier, by the time the individual reaches age 65, the Social Security retirement age will have increased to age 67.

Because of their longer life expectancy, black women fare better than black men under Social Security. However, they fare far worse than their white, female cohorts.⁹

- A black female, born today, can expect to receive 6.7 years of Social Security retirement benefits.
- By contrast, a white female, born today, can expect to receive 11.8 years of Social Security retirement benefits.

A widespread notion is that the major reason for the discrepancy in life expectancy between blacks and whites is due to the higher incidence of infant mortality among blacks. This notion is wrong. While it is true that the black infant mortality rate is substantially higher than the white infant mortality rate, it is also true that,¹⁰

- At virtually every age, whites have a higher life expectancy than blacks.
- Among men of working age, black males, on the average, are twice as likely to die in any given year as their white cohorts.

The fact of higher black mortality means that a substantial proportion of black men and women will never receive Social Security or Medicare benefits from a system that imposes an enormous tax burden upon them during their working years. Specifically,

- Black children born today can expect to pay Social Security taxes ranging from the current level of 14.3 percent of income to as much as 38 percent of income by the time they reach the age of retirement.¹¹
- More than 70 percent of black families pay more in Social Security taxes than they do in income taxes, and this percentage undoubtedly will grow.¹²
- Yet despite this enormous tax burden, about 42 percent of all black men and 25 percent of all black women will die before they become eligible for Social Security and Medicare benefits.

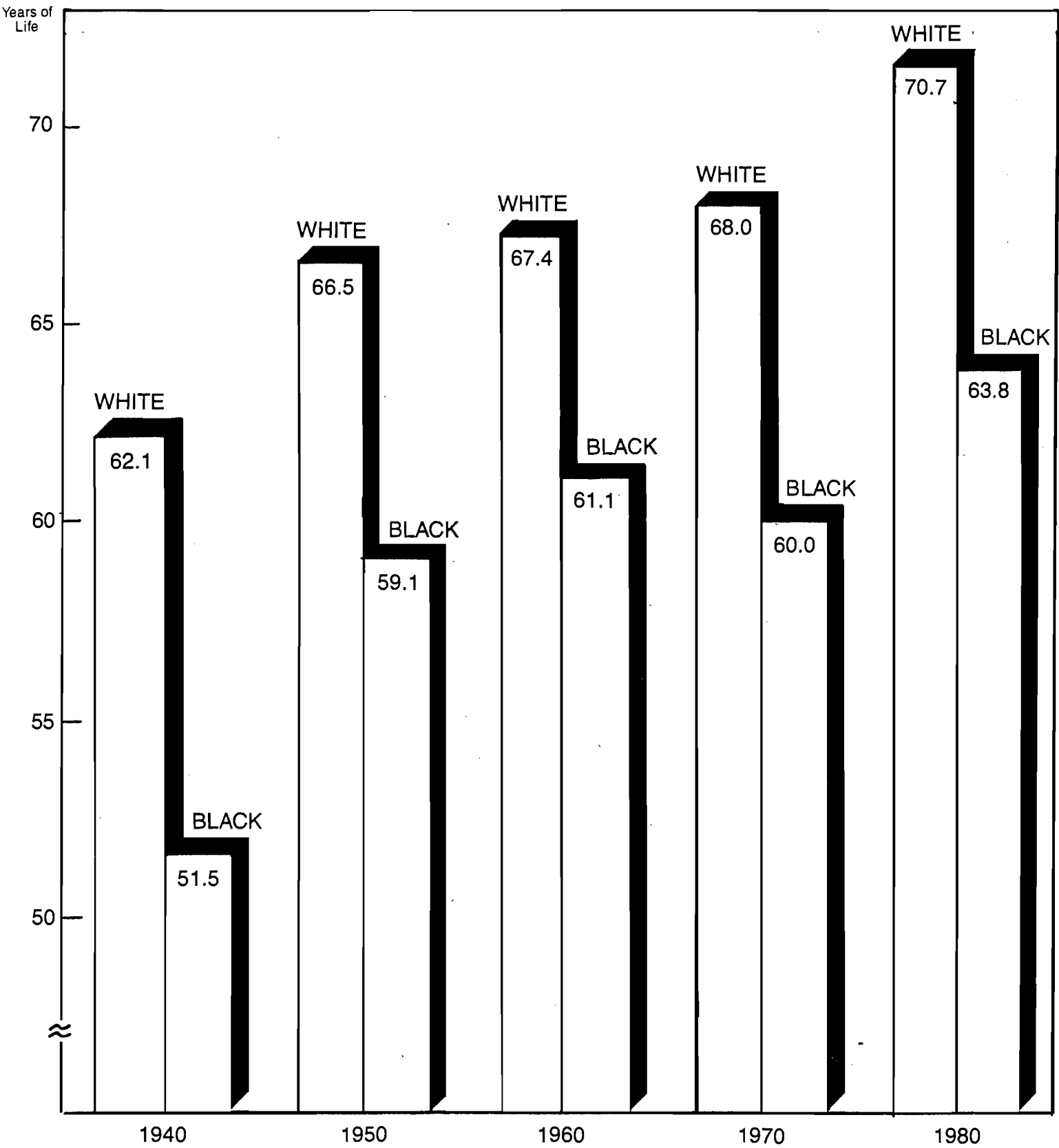
⁹Statistical Abstract of the United States, 1987, Table 105, p. 69.

¹⁰*Ibid*, Table 108, p. 71.

¹¹These are the combined "employer's" and "employee's" share of the payroll tax. For a discussion of future payroll tax rates, see "Social Security: Who Gains? Who Loses?," p. 6.

¹²See "The Effect of the Social Security Reforms on Black Americans," Table III, p. 13.

LIFE EXPECTANCY FOR MALES AT BIRTH



Note: Black life expectancy for 1940, 1950 and 1960 includes black and other non-whites

MALE DEATH RATES AT DIFFERENT AGES, 1983

(Deaths per 1,000 population)

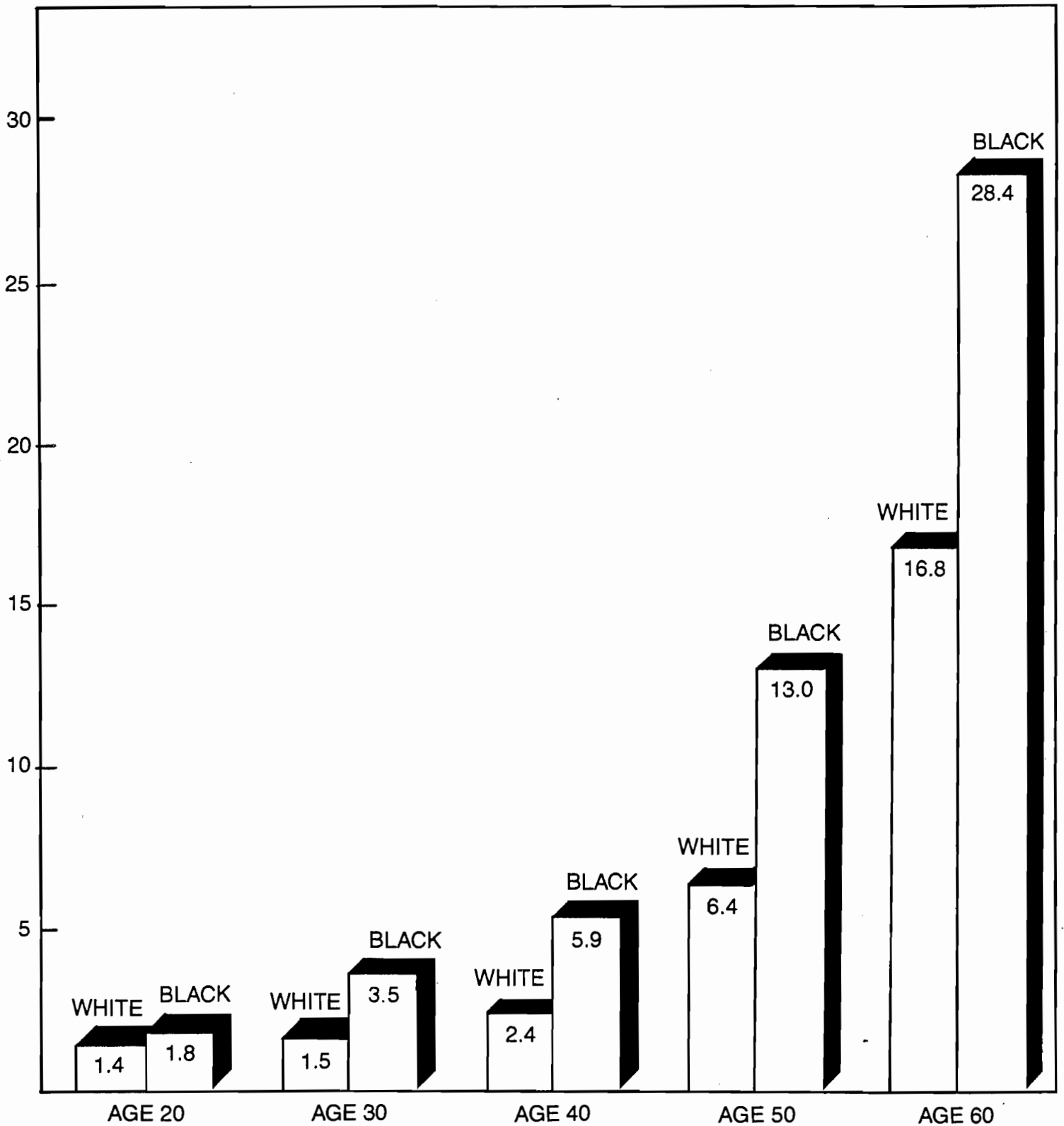


TABLE I
PERCENTAGE OF THE POPULATION
EXPECTED TO REACH AGE 65

	<u>White</u>	<u>Black</u>
Men	74.1 %	57.9 %
Women	85.3 %	74.5 %

Source: Statistical Abstract of the United States, 1987,
Table 106, p. 70.

Causes of Death

One of the difficulties in predicting future mortality is that little is known about the causes of the differences in mortality between blacks and whites. As Table II shows, the mortality rate for black males is substantially higher than the mortality rate for white males for virtually every leading cause of death. What is not known is to what extent these differences can be explained by genetic factors, environmental factors, lifestyle choices or other factors.

As an example of the complexity involved in explaining mortality rates, consider deaths due to accidents and violence. On the average, whites have a higher probability of dying in an automobile accident than blacks. On the other hand, blacks have a substantially higher probability of dying in other types of accidents.¹³

The disparities between the races with respect to suicide and homicide approach the bizarre, considering the degree of racial integration our society is perceived to have achieved. For example,¹⁴

- A white male is more than twice as likely to commit suicide as a black male.
- A white female is about three times more likely to commit suicide as a black female.

¹³Statistical Abstract of the United States, 1987, (Washington, D.C.: U.S. Government Printing Office, 1986), Table 119, p. 79.

¹⁴Ibid.

On the other hand, blacks are far more likely than whites to die a violent death at the hands of someone else.¹⁵

- A black male is about six times more likely to die from a homicide than a white male.
- A black female is about four times more likely to die from a homicide than a white female.

TABLE II
DEATH RATES, 1983
(Age-Adjusted Deaths per 100,000 Population)

<u>Cause of Death</u>	<u>Black Males</u>	<u>White Males</u>
Diseases of the Heart	308.2	257.8
Cancer	232.2	158.9
Accidents and Violence	66.2	51.8
Cerebrovascular Diseases	64.2	35.2
Pulmonary Diseases	22.2	27.6
Pneumonia, Flu	24.3	15.3
Suicide	10.5	19.3
Diseases of the Liver	22.8	13.4
Diabetes	17.7	9.2
All Causes of Death	1,019.6	698.4

Source: Statistical Abstract of the United States, 1987, Table 115, p. 76.

¹⁵Ibid.

Taxpayers and Beneficiaries
Under the Current System

Partly because of a higher mortality rate, and partly for other reasons (such as a higher fertility rate), there is a significant difference in the age structure of the black and white populations. As Table III shows,¹⁶

- About 37 percent of the black population is under 20 years of age, compared with only 28 percent of the white population.
- At the other end of the age spectrum, more than 12 percent of the white population is 65 years of age or older, compared to only eight percent of the black population.

As a result, the white population is over-represented among the elderly, who are eligible for Social Security and Medicare benefits. By contrast, the black population is over-represented among the population of tax-paying age (or soon to be of taxpaying age). For example,¹⁷

- Blacks currently represent about 11.9 percent of the total population.
- Yet only 8.7 percent of elderly females are black, and only 7.7 percent of elderly males are black.
- As a result, the percentage of individuals of taxpaying age who are black is about 50 percent higher than the percentage of those of retirement age who are black.

Even more striking is the fact that among elderly blacks and whites, blacks are significantly less likely to qualify for Social Security benefits:¹⁸

- Among families with a head of household over 65, 93 percent of whites, but only 89 percent of blacks, receive Social Security retirement benefits.
- Among unrelated individuals over 65 (about 30 percent of the elderly), 92 percent of whites, but only 82 percent of blacks, receive Social Security retirement benefits.

¹⁶Statistical Abstract of the United States, 1984, Table 37, p. 33.

¹⁷Ibid., Table 36, p. 35.

¹⁸Statistical Abstract of the United States, 1981, page 451. -

Exact statistics are not available, but it is probably true that considerably more is being taken from the black population in Social Security taxes than is being paid back to them in the form of benefits. To a large extent, Social Security appears to be transferring income out of the pockets of black workers and into the pockets of white retirees.

TABLE III

AGE STRUCTURE OF
THE POPULATION, 1985

Percentage in Each Age Group

	<u>Under 20</u>	<u>65 and Over</u>
White	28.2 %	12.7 %
Black	37.2 %	8.1 %
Hispanic*	39.6 %	4.8 %

Median Age

	<u>Male</u>	<u>Female</u>
White	31.2	33.6
Black	25.2	27.8

* Persons of Hispanic origin may be of any race.

Source: Statistical Abstract of the United States, 1987, Table 20, p. 18.

ESTIMATES OF THE VALUE OF PARTICIPATING IN SOCIAL SECURITY FOR BLACK AND WHITE FAMILIES

Social Security confronts workers entering the labor market with a stream of potential costs and a stream of potential benefits. The potential costs are the payroll taxes imposed on their incomes during the years they work. The potential benefits are disability benefits, survivors benefits, retirement pensions and Medicare benefits. Each of these categories of benefits depends upon a contingency -- death, disability, old age, illness, etc.

To measure the value of participating in this system to an individual worker, we used the same computer program we used in our study in "Social Security: Who Gains? Who Loses?"¹⁹ Based on an individual's probability of living to all possible ages (up to 105 years of age) the program calculates the costs and benefits to an individual for each possible life span. The program also calculates the probability that an individual will become disabled and begin receiving disability benefits in any given year, as well as the probability that a disabled individual will re-enter the labor force in some future year. The program then evaluates the expected value of participating in a system with all of these possible outcomes, using a four percent real rate of interest.

The calculations presented in this study differ from our previous study in that we have taken explicit account of different mortality tables for blacks and whites. Since whites have lower-than-average mortality rates and higher-than-average life expectancies, they can expect to receive lower-than-average survivors benefits and higher-than-average retirement and Medicare benefits. By contrast, black families can expect to receive higher-than-average survivors benefits and lower-than-average retirement and Medicare benefits.

The mortality tables used are 1984 Tables (the latest year for which estimates are available) prepared by the U.S. National Center for Health Statistics. These numbers are predicted to change in future years according to the projections of the Social Security Financing Alternative II B assumptions (the "intermediate" projection). We have assumed that any future increase in life expectancy will affect blacks and whites in the same way. We also assumed that disability rates will be the same for black white workers. Finally, we have assumed that in all cases promised future benefits will be paid and the payroll tax will be raised (whenever necessary) to pay these benefits.²⁰

¹⁹The program was developed by William T. Rule III of Peat, Marwick, Main & Co. An earlier version of this program was developed under a grant from the National Chamber Foundation.

²⁰For a more complete description of the assumptions, see Appendix A and Appendix B.

The results of these calculations for single male workers and working couples are presented in Tables IV, V and VI. A summary of the present value of Social Security for other cases is presented in Appendix B.

Racial Differences: Social Security Benefits and Income

One of the most striking facts about the Social Security system is that it has evolved into a system in which those who have less pay taxes to support benefits for those who have more. In our previous study, we reported that,²¹

- The, after-tax, per capita income of the elderly is greater than the after-tax income of individuals under 65 years old.
- The elderly also have more assets than the non-elderly.
- Among the elderly, those with the highest incomes receive the largest Social Security benefits.

Even more remarkable is the fact that these benefits are funded by a regressive payroll tax. On the average, low-income workers pay a higher percentage of their income in Social Security taxes than high-income workers.²²

This system might be defensible if Social Security operated like a private pension system in which workers' contributions were funding their own retirement pensions. Yet, as is well known, Social Security does not operate like a private pension system. It is instead a pay-as-you-go system in which taxes paid by today's workers are immediately paid out in benefits to today's retirees. Current retirees no more paid for their own benefits than food stamp recipients or Aid to Families With Dependant Children (AFDC) recipients paid for their benefits.

Social Security, then, is an income transfer program -- no different in principle than the food stamp program, the AFDC program or any other income transfer program. It differs from other income transfer programs only in one important respect: Rather than distributing benefits based on need, it distributes its greatest benefits to those least in need.

²¹See "Social Security: Who Gains? Who Loses?," pp. 4-5.

²²Ostensibly, the payroll tax is a proportional tax levied on income up to the maximum income subject to the tax (\$42,000 in 1986). However, most fringe benefits escape the payroll tax, even though fringe benefits clearly are a substitute for money wages. Since the proportion of income that workers receive in the form of fringe benefits tends to rise as income rises, as a percentage of the total compensation package, the effective payroll tax rate tends to fall as income rises.

Tables IV and V show that this pattern of distribution will continue when today's young people reach retirement. On the average,

- Median-income workers can expect to receive about one-third more in Social Security benefits than low-income workers.
- High-income workers can expect to receive about 50 percent more in Social Security benefits than low-income workers.

If anything, Tables IV and V probably understate the regressivity of Social Security's benefit structure. Because the National Center for Health Statistics does not produce separate mortality tables for individuals at different income levels, these tables were constructed on the assumption that life expectancy is independent of income. Yet it is well known that mortality from leading causes of death is higher among low-income families than among high-income families.

Much has been made of the fact that young, black professional couples (with a college education) now earn more than their white cohorts. Yet it is still true that, on the average, adult, black male workers earn only 73 percent of the income of their white cohorts. Intact black families earn only 82 percent of the income of intact white families.²³ Although much progress has been made since 1940, most of it occurred before the Civil Rights Act of 1964, and there is no convincing evidence that affirmative action programs have done anything to close the income gap.

The upshot is that during their working years blacks are likely to pay a higher percentage of their income in payroll taxes to support a disproportionately large white population of retirees. Among those who survive to collect Social Security retirement benefits, the monthly payment received by black retirees is likely to be smaller than the monthly payment received by whites.

Racial Differences: Single Males and Working Couples

In our previous study we reported that virtually all young workers can expect to pay more in Social Security taxes than they will receive in Social Security benefits. Yet, as Tables IV and V show blacks can expect to lose considerably more from participation in Social Security than white workers who earn identical wages and face the same payroll tax rates.

Single Male Workers. As Table IV shows, single male workers who are black can expect considerably less in Social Security benefits than their white cohorts. Specifically,

²³James P. Smith and Finis R. Welch, Closing the Gap: Forty Years of Economic Progress for Blacks, (Santa Monica: Rand Corporation, August 1986).

- Among low-income workers, black males can expect to receive \$9,746 less in Social Security benefits than white males.
- Among median-income workers, black workers can expect to receive \$12,257 less in benefits.
- Among high-income workers, black workers can expect to receive \$14,464 less in benefits.
- At every income level, white workers are promised about 50 percent more in Social Security benefits than their black cohorts.

Table VI shows that the major difference in expected benefits stems from retirement benefits and Medicare benefits -- benefits for which eligibility is partly determined by age. For example, among median-income, single males, whites can expect 74 percent more in retirement benefits and 47 percent more in Medicare benefits than their black cohorts.

Although the gap between expected benefits for black and white workers rises with income, the "penalty" for being black is more severe the lower the worker's income. In other words, relative to their incomes, low-income blacks are penalized more severely than high-income blacks. Specifically,

- Among low-income blacks, lost benefits due to having a lower life expectancy are equal to almost one year's annual income.
- Among median-income blacks, the "penalty" is equal to almost one-half the worker's annual income.
- Among high-income blacks, the "penalty" is equal to about one-third of the worker's annual income.

Since black workers have a higher probability of dying than their white cohorts in any given year, the expected future taxes of blacks also are lower than for whites with the same incomes. The combined effect of lower expected taxes and lower expected benefits still leaves young black workers significantly worse off than white workers, however.

- For low-income white workers, Social Security taxes are about 50 percent higher than Social Security benefits (when evaluated at a four percent rate of interest).
- Among low-income black workers, however, Social Security taxes are more than twice the size of Social Security benefits.
- Among median-income workers, Social Security taxes are more than twice the amount of promised benefits for whites; but they are more than three times the amount of promised benefits for blacks.
- Among high-income workers, taxes are about three times greater than benefits for whites, but about 4.5 times greater than benefits for blacks.

Compared to the alternatives offered in the private capital market, Social Security is a bad "investment" for all young workers. But it is a worse investment for blacks than for whites. This is because the amount of taxes paid, relative to benefits received, is substantially greater for blacks than whites at every income level.

Translated into the language of financial analysis, these disparities mean that the "rate of return" that black workers can expect to earn on their "investment" in Social Security is significantly lower than the rate of return white workers can expect to earn. For example,

- Among median-income workers, the rate of return Social Security promises to black workers is -0.6 percent, compared with a positive 1.1 percent rate of return for white workers.
- Thus, Social Security promises single, white male workers almost twice the rate of return that it promises to their black cohorts.

Working Couples. Just as black males have lower life expectancies than white males, so black females have lower life expectancies than white females. As a consequence, the gap between expected benefits for black and white working couples is even greater than the gap between black and white single males. Specifically,

- Among low-income working couples, black couples can expect to receive \$11,915 less in Social Security benefits than low-income white working couples.
- Among median-income working couples, black families can expect to receive \$14,226 less in Social Security benefits.
- Among high-income working couples, black families can expect to receive \$17,485 less in Social Security benefits.

As in the case of single, male workers, the loss of benefits among black working couples relative to their annual income is more severe the lower their income. Moreover, the total package of benefits and taxes is far less favorable for black working couples than for white working couples.

- Among low-income working couples, Social Security promises white families a rate of return which is 50 percent higher than the rate of return promised to black families.
- Among median-income working couples, the rate of return Social Security promises to white families is more than twice the rate of return promised to black families.

TABLE IV

VALUE OF PARTICIPATION IN SOCIAL SECURITY
FOR SINGLE MALES, AGE 20 IN 1986
(in 1986 prices)

Low-Income Workers

	<u>White</u>	<u>Black</u>
Expected Benefits	\$30,257	\$20,511
Expected Taxes	45,564	44,060
Past Taxes	<u>3,202</u>	<u>3,202</u>
Net Present Value	- \$18,508	- \$26,751
Rate of Return	2.5 %	1.1 %

Median-Income Workers

	<u>White</u>	<u>Black</u>
Expected Benefits	\$40,610	\$27,743
Expected Taxes	95,968	92,560
Past Taxes	<u>0</u>	<u>0</u>
Net Present Value	- \$55,358	- \$64,817
Rate of Return	1.1 %	- 0.6 %

High-Income Workers

	<u>White</u>	<u>Black</u>
Expected Benefits	\$45,161	\$30,697
Expected Taxes	143,041	137,587
Past Taxes	<u>0</u>	<u>0</u>
Net Present Value	- \$97,880	- \$106,891
Rate of Return	- 0.0 %	*

* = Very Negative

TABLE V
VALUE OF PARTICIPATION IN SOCIAL SECURITY
FOR WORKING COUPLES, AGE 20 IN 1986
(in 1986 prices)

<u>Low-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Expected Benefits	\$64,355	\$52,440
Expected Taxes	92,181	89,916
Past Taxes	<u>6,404</u>	<u>6,404</u>
Net Present Value	- \$34,230	- \$43,880
Rate of Return	2.5 %	1.7 %
 <u>Median-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Expected Benefits	\$81,955	\$67,729
Expected Taxes	159,239	154,720
Past Taxes	<u>0</u>	<u>0</u>
Net Present Value	- \$77,284	- \$86,992
Rate of Return	1.6 %	0.7 %
 <u>High-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Expected Benefits	\$99,060	\$81,575
Expected Taxes	289,892	281,672
Past Taxes	<u>0</u>	<u>0</u>
Net Present Value	- \$190,832	- \$200,097
Rate of Return	0.1 %	- 7.4 %

TABLE VI

BREAKDOWN OF SOCIAL SECURITY BENEFITS
FOR 20-YEAR-OLDS
(in 1986 prices)

Median-Income, Single Males

<u>Type of Benefit</u>	<u>White</u>	<u>Black</u>	<u>Ratio of White to Black</u>
Retirement ^a	\$22,396	\$12,822	1.74
Medicare	9,853	6,714	1.47
Disability ^b	<u>8,361</u>	<u>8,176</u>	<u>1.02</u>
TOTAL	\$40,610	\$27,712	1.47

Median-Income, Working Couples

<u>Type of Benefit</u>	<u>White</u>	<u>Black</u>	<u>Ratio of White to Black</u>
Retirement ^a	\$34,989	\$26,055	1.34
Medicare	22,527	16,659	1.35
Disability ^b	14,757	14,508	1.02
Survivors ^b	<u>9,682</u>	<u>10,507</u>	<u>.92</u>
TOTAL	\$81,955	\$67,729	1.21

^a All cash benefits received after age 67, including pension benefits, disability benefits and (if applicable) survivors benefits.

^b Benefits received prior to age 67.

Racial Differences: Social Security and the Traditional Family

In a previous National Center for Policy Analysis study²⁴ we reported that although Social Security penalizes all young families, it penalizes traditional families less than those with non-traditional lifestyles.

Although there are some differences in the expected benefits for black and white families under the current benefit formulas, these differences are small compared to the total burden of participation in Social Security. The reason why these benefit formulas are so important is that there are striking differences between the black and white populations with respect to family structure.

In recent years conservatives and liberals alike have become alarmed over the dissolution of the black family. For example,

- Among adult, black females, only 43 percent are currently married, compared with 63 percent of adult, white females.²⁵
- The divorce rate for black women is more than twice the divorce rate for white women.²⁶

Moreover, since 1960, the differences in family structure between blacks and whites has been steadily widening, creating an increasing cultural gap between the two races. For example, in the 1940s the percentage of black children born out of wedlock was not that much different from the percentage in the white population. Today, the differences are staggering.²⁷

- Almost 60 percent of all black children born today are born to an unmarried woman.
- By contrast, only 13.4 percent of white children are born to an unmarried woman.

²⁴"Social Security: Who Gains? Who Loses?" pp. 14-15.

²⁵Statistical Abstract of the United States, 1987, Table 655, p. 383.

²⁶Ibid, Table 52, p. 41.

²⁷Ibid, Table 86, p. 61.

TABLE VII
MARITAL STATUS OF THE POPULATION
18 YEARS OF AGE AND OLDER, 1985

	<u>Percent Married</u>	
	<u>White</u>	<u>Black</u>
Males	67.6 %	50.7 %
Female	62.7 %	42.7 %

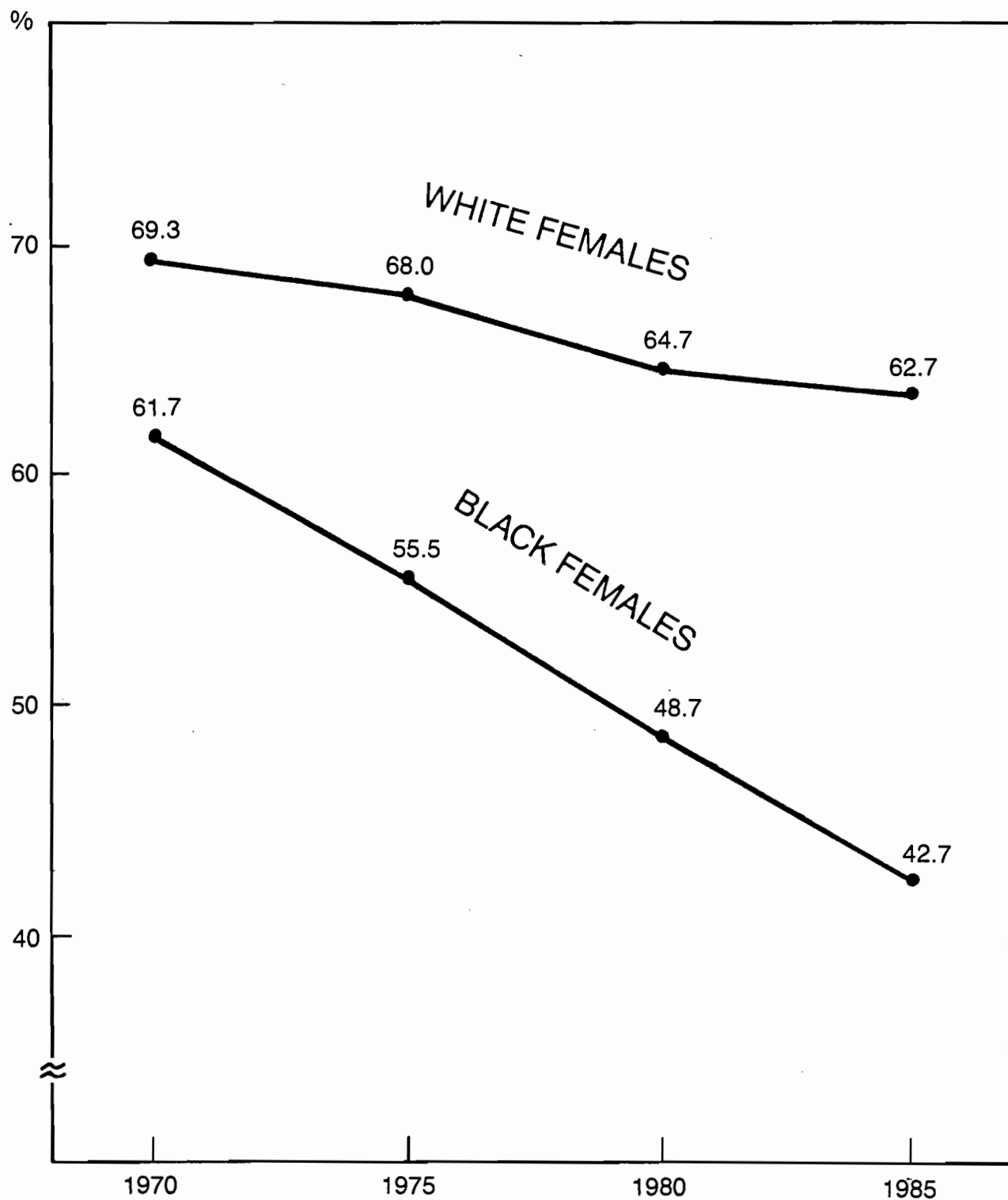
	<u>Divorce Rate</u> (Divorced persons per 1,000 married persons)	
	<u>White</u>	<u>Black</u>
Males	98	179
Females	142	326

Source: Statistical Abstract of the United States, 1987, Table 45, p. 38 and Table 52, p. 41.

Although it continues to be a matter of considerable debate, virtually all scholars agree that the welfare state is in some measure responsible for the dissolution of the black family.²⁸ As a result, our two largest federal bureaucracies offer contradictory incentives to young families. While Social Security provides favorable treatment to intact families, our federal welfare programs encourage the family's dissolution.

²⁸See Martin Anderson, Welfare, (Stanford: Hoover Institution Press, 1978); Chap. 2; George Gilder, Wealth and Poverty, (New York: Basic Books, 1981); John C. Goodman, "Welfare and Poverty," NCPA Policy Report #107, National Center for Policy Analysis, 1985; Charles Murray, Losing Ground: American Social Policy 1950-1980, (New York: Basic Books, 1984); Lowell Gallaway and Richard Vedder, "Paying People to be Poor," NCPA Policy Report #121, National Center for Policy Analysis, 1986; and John Goodman and Michael Stroup, "Privatizing the Welfare State," NCPA Policy Report #123, National Center for Policy Analysis, June, 1986.

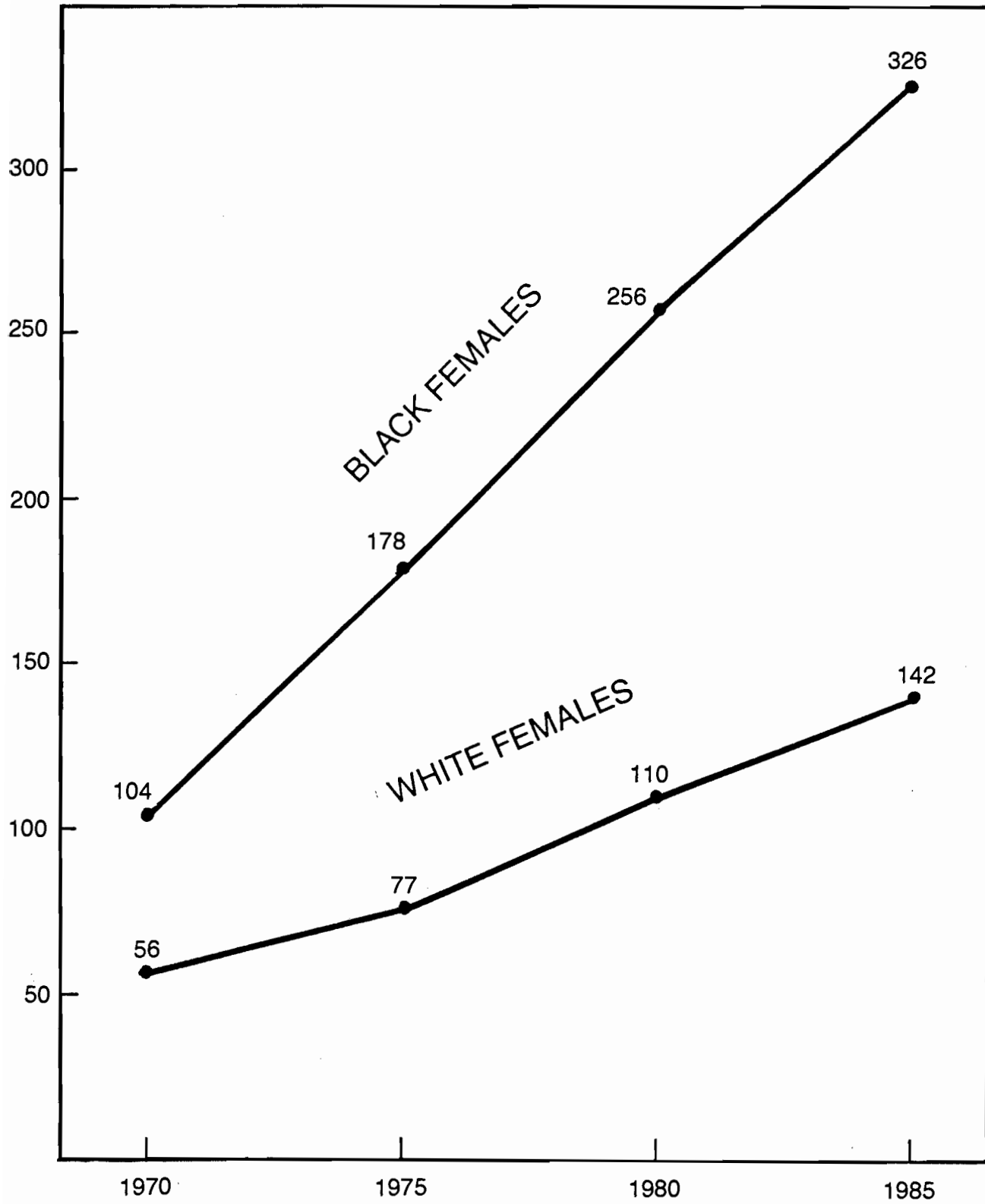
PERCENT OF ADULT WOMEN WHO ARE MARRIED



Source: *Statistical Abstract of the United States*
1987, p. 45

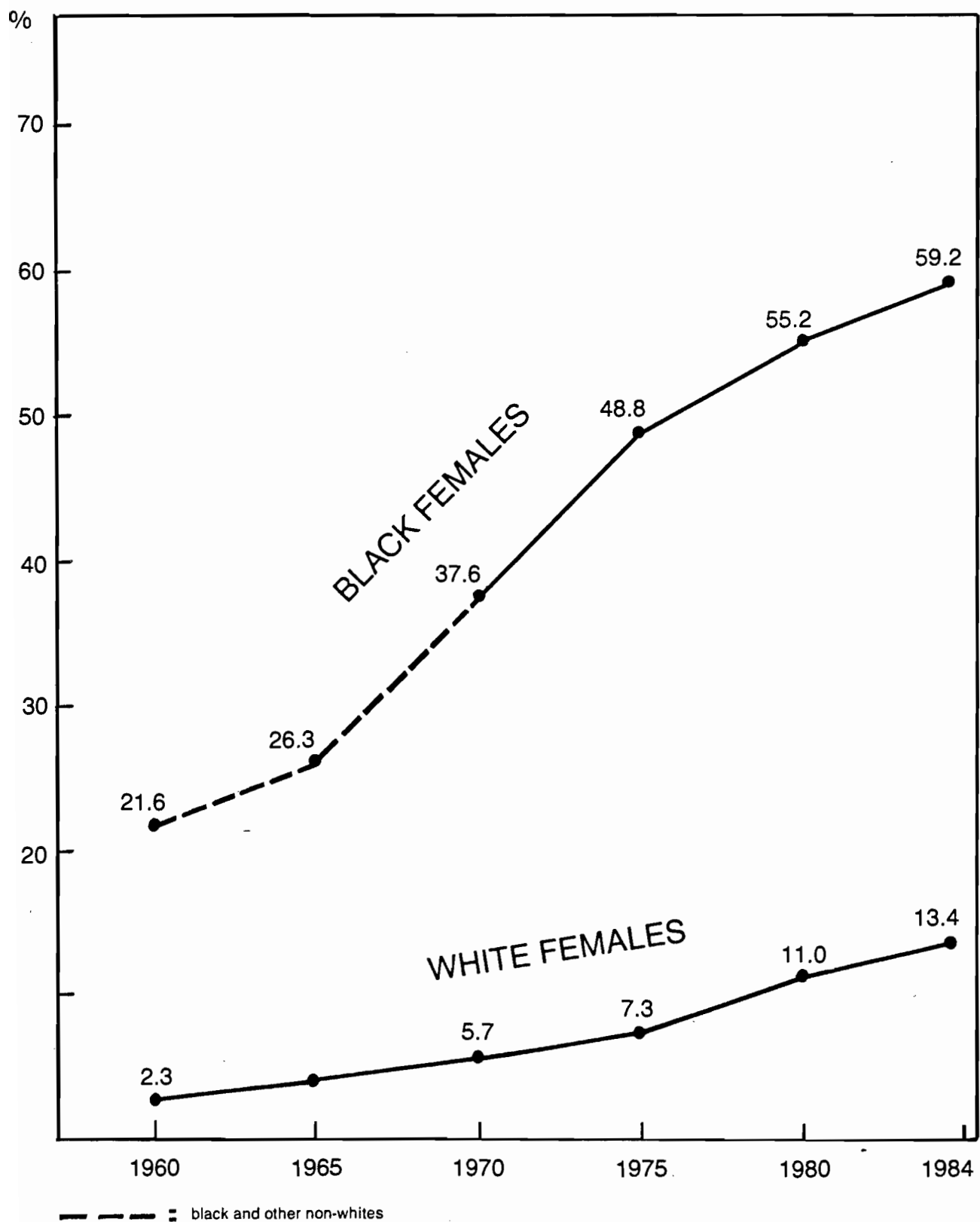
DIVORCE RATE

Divorced persons per 1,000 married persons



Source: *Statistical Abstract of the United States*
1987, p. 41

PERCENT OF BIRTHS TO UNMARRIED WOMEN



Source: *Statistical Abstract of the United States*
1987, p. 61

The benefits that the welfare state promises to the non-traditional family, however, are current and immediate. The benefits Social Security promises to the traditional family are distant and probabilistic. Ironically, to the degree that the welfare state succeeds in dissolving the black family, the Social Security system heaps additional penalties upon those families.

Marriage. Although almost all young people can expect substantial losses as a result of participation in Social Security, the mere act of marriage can reduce these losses significantly. Consider a white, working male and a white, non-working female. The mere act of marriage will reduce the couple's expected loss from Social Security by \$23,648 for a high-income male, by \$20,156 for a median-income male, and by \$15,457 for a low-income male.

The reduction in Social Security losses as a result of marriage are about \$1,000 less for similarly situated black couples. Yet, although these amounts are substantial for blacks as well as whites,

- The benefits from marriage are about 50 percent greater for high-income earners than for low-income earners.
- Thus, the benefits from marriage are least attractive for those who are the most likely candidates for public welfare.

Children. Once married, the couple can further reduce their expected losses from Social Security by having children. For example,

- Among white married couples, the additional expected benefits of having two children range from \$3,051 for low-income earners to \$7,215 for high-income earners.
- Among black married couples, the additional benefits are slightly higher, ranging from \$4,325 for low-income earners to \$8,095 for high-income earners.

Here again, however, the benefits of having children increase with income. High-income couples are promised twice as much as low-income couples. To put this in perspective, consider that a woman with two children who is unmarried and who is not working is entitled to the maximum benefits under the Aid to Families With Dependent Children (AFDC) program. At the same time, a woman so situated is entitled to nothing from Social Security.

The Traditional Family. One way to appreciate the impact of Social Security's benefit formulas is to consider the numbers presented in Table VIII. Consider a "family" consisting of a working male, a non-working female and two children.

- If the couple is white and married, they can expect a small gain from Social Security (\$803) if the husband earns a low income.
- A similarly situated black couple will lose \$26,751 from Social Security if they choose not to marry.

- Among median-income families, a black unmarried couple will lose about \$36,000 more from Social Security than a married white couple.
- Among high-income families, a black unmarried couple will lose almost \$40,000 more from Social Security than a married white couple.

TABLE VIII
SOCIAL SECURITY'S TREATMENT OF
TRADITIONAL AND NON-TRADITIONAL FAMILIES *

<u>Present Value of Social Security</u> <u>At Age 20</u>		
<u>Case</u>	<u>Traditional</u> <u>Family</u>	<u>Non-Traditional</u> <u>Family</u>
<u>High-Income Workers:</u>		
White	- \$67,017	- \$97,880
Black	-76,400	- 106,891
<u>Median-Income Workers:</u>		
White	- 28,893	-55,358
Black	- 38,556	- 64,817
<u>Low-Income Workers:</u>		
White	+ 803	- 18,508
Black	- 8,054	-26,751

- * The male is assumed to be a full-time member of the labor force. The female does not work. The couple has two children. In the traditional family the couple is married. In the non-traditional family the couple is not married.

Source: Data taken from Appendix B.

Racial Differences: Treatment of Working Wives

Social Security imposes its severest penalties on wives who enter the labor market. This is partly because the wife who never works is entitled to a retirement pension equal to 50 percent of her husband's benefit. If the woman earns enough to claim a retirement pension in her own right, she forfeits the 50 percent of her husband's pension that she would have received had she chosen not to work. As a result,

- If the wife of a high-income worker enters the labor market and earns a high income, the couple's expected loss from Social Security increases by more than \$123,000.
- If the wife of a median-income worker enters the labor market and earns the median wage paid to adult female workers, the couple's loss from Social Security increases by more than \$48,000.
- If the wife of a low-income worker enters the labor market and earns a low income, the couple's loss from Social Security increases by more than \$35,000.
- In all three cases, the wife's decision to work cost the couple about three years of her wages in terms of lost Social Security benefits.

The loss of Social Security benefits is about the same for similarly situated black and white couples. However, the incidence of working wives is not similar for the two races. Although a black woman is less likely to be married than a white woman, among women who are married the black woman is more likely to be in the labor market.²⁹

- Among married women, 64.2 percent of blacks and only 53.4 percent of whites are in the labor force.
- Among married women with small children, the difference is even greater: 69.3 percent of black women and only 52.3 percent of white women are in the labor force.

²⁹Statistical Abstract of the United States, 1987, Table 655, p. 383.

SOCIAL SECURITY REFORM

Almost everyone is aware that the Social Security system faces periodic short-term crises. Every time one of the trust funds depletes its reserves, Congress is forced to act hastily to insure the fund's solvency -- by raising taxes, cutting benefits, or enacting some combination of the two.³⁰

Scholars who study the Social Security system, however, have long been aware that the system faces a long-term crisis -- far more serious than the short-term funding problems of the last 20 years. By almost any realistic prediction, sometime in the next century we will be faced with the prospect of drastic tax increases or drastic cuts in benefits unless something is done in the near future to avert the crisis.

Given projected tax revenues and projected benefit payments, Social Security faces a long-term actuarial deficit that, by any estimate, is huge. For example,³¹

- According to the Social Security Administration's "intermediate" projections, the actuarial deficit in Social Security is between \$3 and \$4 trillion -- measured in current dollars.
- According to the "pessimistic" projection, the actuarial deficit is between \$14 and \$15 trillion -- measured in current dollars.

Interestingly, virtually every reform that has been proposed by those who desire to maintain the basic structure of Social Security would be detrimental to blacks.

Raising the Eligibility Age

We already have noted that under the 1983 Amendments to the Social Security Act, Congress raised the Social Security retirement age from 65 to 67, beginning in the next century. Similar recommendations have been made for Medicare. Some are calling for an increase in the eligibility age for both programs to age 70. Most who propose to raise the eligibility age also propose to index it so that it automatically increases with any general improvement in life expectancy for the population as a whole. All such changes would be devastating for blacks.

³⁰Currently there are three funds. One fund is maintained for pension benefits and survivors benefits, one for disability benefits, and one for Medicare.

³¹See the discussion in Michael Boskin, Too Many Promises: The Uncertain Future of Social Security, A Twentieth Century Fund Report, (Homewood, Illinois: Dow Jones-Irwin, 1986), pp. 15-18.

In an NCPA report on the effects of the 1983 reforms, we estimated that these reforms would result in massive transfer of wealth from blacks to whites.³² For example, consider the effect of these reforms on 25-year-old male workers. Prior to the reforms, a 25-year-old black male could expect to receive about two years worth of Social Security benefits, based on life expectancy tables available when the reforms were enacted. After the increase in the retirement age, he could expect to receive only about five months of benefits. By contrast, for a 25-year-old white male the period of expected benefits fell from nearly eight years to six years.

The raising of the retirement age penalized all young workers by reducing their expected Social Security benefits. But the effect on black workers relative to white workers was devastating. As a result of the increase in retirement age:

- A black male, age 25, lost more than 80 percent of his expected benefits. A white male, age 25, lost less than 22 percent of his.
- Prior to the reforms, the 25-year-old white male could expect about four times more monthly benefit checks as his black cohort. Afterwards, he could expect about 15 times more than his black cohort.

Cutting Social Security Benefits

Our previously reported calculations of the present value of expected benefits and expected taxes under Social Security have assumed that promised benefits will be paid and that Congress will insure these promises by raising the payroll taxes. These payroll tax increases may be huge, and it is not clear whether workers in the year 2050 will be willing to pay as much as 38 percent of their income to support the Social Security system. An obvious alternative to raising taxes is to cut benefits. Interestingly, this option turns out to be better for most young blacks than increasing taxes. And, solving the financial crisis of Social Security by cutting benefits would be better for blacks than for whites at every income level.

The Social Security payroll tax rate is scheduled to increase to 15.3 percent by the year 1990. We used our computer program to calculate the present value of expected benefits and taxes under the assumption that the payroll tax rate remains at 15.3 percent indefinitely, and that each of Social Security's three trust funds would remain solvent by cutting benefits (whenever necessary) in future years. The impact of this reform on single males and working couples is reported in Tables IX and X.

³²"The Effect of the Social Security Reforms on Black Americans," p.6.

As the tables show, cutting future Social Security benefits reduces the present value of expected benefits for all young workers, regardless of income. Yet these benefit cuts make it possible to avoid increases in the payroll tax beyond the level of 15.3 percent of income. As a result, future benefit cuts also reduce expected Social Security taxes for all young workers, regardless of income.

In general, the combined effect of these two changes is a better deal for blacks than for whites. For example,

- For single black males, the loss of expected benefits is only about 60 percent as great as the loss for their white cohorts.
- For black working couples, the loss of expected benefits is only about 72 percent of the loss experienced by white couples.
- On the other hand, the gain in reduced taxes is much more similar--about 92 percent of the white worker's gain for single black males, and about 94 percent for black working couples.

Under the changes, then, black workers do better relative to white workers at every level of income.

- Although all low-income workers lose as a result of this change, the loss among white workers is about twice the amount of the loss among blacks.
- Among median-income workers, single black males and black working couples experience a positive gain, while their white cohorts post a loss.
- All high-income workers gain substantially as a result of this change, but the gain for a single black male is more than twice the gain for a single white male. A black working couple gains 25 percent more than a white working couple..

These results have dramatic implications for future political coalitions that are likely to form as the issue of Social Security reform heats up. In the past, black political leaders have tended to side with those who prefer tax increases over benefit cuts -- whatever the costs. It appears that the economic interest of black voters lies elsewhere.

TABLE IX
SOLVING THE SOCIAL SECURITY FINANCIAL CRISIS
BY CUTTING BENEFITS RATHER THAN BY INCREASING TAXES

Effects on 20-Year-Old, Single Male Workers
(in 1986 prices)

Low-Income Workers

	<u>White</u>	<u>Black</u>
Change in Expected Benefits	- \$7,785	- \$4,773
Change in Expected Taxes	<u>- 2,648</u>	<u>- 2,434</u>
Change in Net Present Value	- \$5,139	- \$2,339
Change in Rate of Return *	- 0.8 %	- 0.9 %

Median-Income Workers

	<u>White</u>	<u>Black</u>
Change in Expected Benefits	- \$7,871	- \$4,828
Change in Expected Taxes	<u>- 6,020</u>	<u>- 5,534</u>
Change in Net Present Value	- \$1,851	+ \$706
Change in Rate of Return *	- 0.6 %	**

High-Income Workers

	<u>White</u>	<u>Black</u>
Change in Expected Benefits	- \$7,922	- \$4,858
Change in Expected Taxes	<u>- 9,696</u>	<u>- 8,913</u>
Change in Net Present Value	+ \$1,774	+ \$4,055
Change in Rate of Return *	+ 0.5 %	**

* = Percentage point increase or decrease.

** = Not calculated.

TABLE X
SOLVING THE SOCIAL SECURITY FINANCIAL CRISIS
BY CUTTING BENEFITS RATHER THAN BY INCREASING TAXES

Effects on 20-Year-Old Working Couples
(In 1986 prices)

<u>Low-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Change in Expected Benefits	- \$12,432	- \$8,920
Change in Expected Taxes	- <u>5,414</u>	- <u>5,086</u>
Change in Net Present Value	- \$7,018	- \$3,834
Change in Rate of Return *	- 0.5 %	- 0.5 %
<u>Median-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Change in Expected Benefit	- \$11,824	- \$8,506
Change in Expected Taxes	- <u>10,068</u>	- <u>\$9,414</u>
Change in Net Present Value	- \$1,756	+ \$ 908
Change in Rate of Return *	- 0.3 %	- 0.2 %
<u>High-Income Working Couples</u>		
	<u>White</u>	<u>Black</u>
Change in Expected Benefits	- \$11,648	- \$8,380
Change in Expected Taxes	- <u>\$19,830</u>	- <u>18,629</u>
Change in Net Present Value	+ \$8,182	+ \$10,249
Change in Rate of Return *	- 0.2 %	- 9.7 %

* = Percentage point increase or decrease.

BLACK POLITICAL SUPPORT FOR SOCIAL SECURITY

Black political support for the current structure of Social Security may rapidly erode for yet another reason: The vast majority of adult blacks would be better off if the system were immediately abolished.

Table XI shows the gains and losses that median-income black workers at different age levels would realize if we abolished all future Social Security taxes and all future Social Security benefits. The calculations for two real rates of interest are shown: four percent (the rate of return historically paid by the bond market) and six percent (the rate of interest historically paid by the stock market).³³ Thus, the columns show how much it would be worth to workers to be able to invest their future Social Security taxes in the bond market or the stock market and forgo all future Social Security benefits. An average of the two columns would give a rough indication of the value of being able to opt out of Social Security and invest in a mixed portfolio, consisting of half stocks and half bonds.

As the table shows,

- Virtually all (median-income) single, black male workers under the age of 50 would gain substantially if they could opt out of Social Security and invest instead in a conservative portfolio in the private capital market.
- The gains from being able to opt out range from about \$20,000 for black men age 45 to as much as \$60,000 for black men in their 20s.
- For black working couples, the gains range from about \$23,000 for 45-year-olds to more than \$80,000 for couples in their 20s.
- Black families with a working husband and a dependent spouse gain from opting out as late as their early 40s; and the gains range from about \$11,000 for 40-year-olds to \$40,000 for 20-year-olds.

Table XII shows what black workers at different age and income levels would have accumulated by 1986 had they been given the option of investing their past Social Security taxes in the private capital market. The results are staggering:

- If a 50-year-old black male earning only 150 percent of the minimum wage had been given the opportunity to invest his Social Security taxes in the stock market (say, through an IRA account) by today he would have accumulated more than \$92,000.

³³See the discussion in Peter Ferrara, *Social Security Rates of Return for Today's Young Workers*, (Washington, D.C.: National Chamber Foundation, 1986), pp. 14-16.

- If this worker made no additional contributions in the future, his IRA wealth would exceed \$184,000 (in 1986 dollars) by the time he reached age 62.
- Similarly, had a 50-year-old black working couple -- each earning only 150 percent of the minimum wage -- been given the opportunity to invest their Social Security taxes in the stock market they would have accumulated \$184,000.
- With no additional saving, this couple's IRA wealth would exceed \$368,000 (in 1986 dollars) by the time they reached age 62.

It is hard to escape the conclusion that the problem of black, elderly poverty would be virtually nonexistent today had we given workers a private alternative to participation in Social Security.

TABLE XI

GAIN/LOSS FROM ABOLISHING SOCIAL SECURITY
FOR BLACK WORKERS(Future Taxes Minus Future Benefits)
(in 1986 prices)Median-Income, Single Male

<u>Worker's Age</u>	<u>4 % Real Rate of Interest</u>	<u>6 % Real Rate of Interest</u>
20	\$64,817	\$53,552
25	64,274	\$56,058
30	56,644	51,474
35	46,636	45,106
40	33,492	36,206
45	17,010	24,207
50	- 1,878	9,188

Median-Income Male With a Dependent Spouse and Two Children

<u>Worker's Age</u>	<u>4 % Real Rate of Interest</u>	<u>6 % Real Rate of Interest</u>
20	\$38,556	\$42,028
25	35,389	42,322
30	27,358	37,475
35	16,708	30,660
40	1,882	20,440
45	- 18,169	5,382
50	- 42,291	- 14,630

Median-Income Working Couple With Two Children

<u>Workers' Age</u>	<u>4 % Real Rate of Interest</u>	<u>6 % Real Rate of Interest</u>
20	\$86,992	\$77,475
25	83,857	79,659
30	72,935	73,508
35	58,845	64,965
40	39,669	52,284
45	13,822	33,459
50	- 17,684	8,039

TABLE XII

HOW MUCH WOULD BLACK FAMILIES HAVE ACCUMULATED TODAY IF
PAST TAXES PAID TO SOCIAL SECURITY
HAD BEEN INVESTED IN OTHER ASSETS?

Low-Income Families

Worker's Age	<u>Single Male/Husband</u>		<u>Working Couple</u>	
	<u>4 %</u>	<u>6 %</u>	<u>4 %</u>	<u>6 %</u>
35	\$37,129	\$44,857	\$74,258	\$89,713
40	49,497	62,933	98,994	125,865
45	59,416	78,862	118,832	157,723
50	66,869	92,034	133,739	184,068

Median-Income Families

Workers' Age	<u>Single Male/Husband</u>		<u>Working Couple</u>	
	<u>4 %</u>	<u>6 %</u>	<u>4 %</u>	<u>6 %</u>
35	\$54,591	\$63,025	\$89,831	\$103,724
40	75,372	91,238	125,936	152,718
45	92,134	116,167	156,402	198,072
50	105,362	138,835	180,326	237,251

High-Income Families

Workers' Age	<u>Single Male/Husband</u>		<u>Working Couple</u>	
	<u>4 %</u>	<u>6 %</u>	<u>4 %</u>	<u>6 %</u>
35	\$60,136	\$67,285	\$120,272	\$134,569
40	82,849	96,843	165,697	193,686
45	102,352	124,766	204,704	249,531
50	116,807	147,602	233,615	295,205

PRIVATIZING SOCIAL SECURITY

There are governments in the world today, Great Britain and Chile for example, which have taken major steps to reduce the long-term problem of funding their pension systems.³⁴ Interestingly enough, the reforms which they adopted not only reduce the funding problem but also reduce any built-in inequities between races.

How did they do it? By instituting either partial or complete voluntary participation in Social Security. Britain, for example, has a two-tier system, with participation in the first tier mandatory, while participation in the second tier is voluntary. Companies are encouraged to opt out of the second tier and set up private pension plans for their employees.

Chile has a government-run pension plan that is entirely voluntary. A majority of Chilean workers have discovered that it is in their financial self-interest to opt out of the government plan and set up the Chilean equivalent of an IRA.

In both instances the long-term problem of solvency has been reduced because the number of participants (and therefore the number of retirees drawing benefits) has been reduced. Similarly, any discrepancy in the return-of-benefits ratio between various races has been reduced by virtue of more citizens having direct control over their own individual pensions.

Until recently it was commonly believed that merely discussing radical reform of Social Security was political suicide for aspiring politicians. Times have apparently changed. Pete DuPont, Newt Gingrich and Bruce Babbitt all have made proposals for fairly sweeping reforms.³⁵

Several years ago Peter Ferrara proposed a very attractive way of privatizing the Social Security system in the U.S. It is called the "Super IRA." Under the plan, workers would receive 100 percent income tax credits for contributions to an expanded IRA account. Roughly speaking, for each dollar contributed to the account, a worker forgoes up to a dollar of promised Social Security benefits. As more contributions were made over time, workers would build up private capital to fund their own retirement needs and would rely less and less on Social Security.

³⁴For a description of the British social security system, see John Goodman, Social Security in the United Kingdom: Contracting Out of the System, (Washington, D.C.: American Enterprise Institute, 1981). For a brief description of the social security systems of Britain and Chile, see John Goodman, "Lessons from Abroad," The Heritage Lectures; Rebuilding Social Security, Volume 18, 1982, pp. 23-31; and John Goodman, "Private Alternatives to Social Security: The Experience of Other Countries," Cato Journal, Vol. 3, No.2, Fall 1983, pp. 563-573.

³⁵See "Addressing the Unassailable in U.S. Politics," Wall Street Journal, December 15, 1986.

In the short-run, the Social Security payroll tax would remain in place, as a necessary source of revenue to fund current Social Security obligations. But with the passage of time, workers' claims against Social Security would diminish. And with fewer Social Security promises to keep, Social Security payroll taxes gradually could be reduced.³⁶

Such a plan would move us away from the chain-letter program we now have -- in which each generation must depend upon the next generation to pay for its retirement benefits. It would substitute a program under which each generation pays its own way. And it would create a program in which people who die at an early age would be able to pass along their savings to their heirs as part of their estate, rather than have those savings disappear into the federal treasury.

This is a proposal that all black Americans should immediately consider.

Note: Nothing written here should be construed as necessarily reflecting the views of the National Center for Policy Analysis or as an attempt to aid or hinder the passage of any bill before Congress.

³⁶See Peter J. Ferrara, ed., Social Security: Prospects for Real Returns, (Washington, D.C.: Cato Institute, 1985); Ferrara, "The Social Security System" in Stuart Butler, Michael Sanera and W. Bruce Weinrod, eds., Mandate for Leadership II: Continuing the Conservative Revolution, (Washington, D.C.: The Heritage Foundation, 1984); and Ferrara, "Rebuilding Social Security, Part 2," Heritage Foundation Backgrounder, No. 346, April 1984.

APPENDIX A

ASSUMPTIONS BEHIND THE PROJECTIONS

Labor Market Participation. Workers are assumed to enter the labor market at age 18 (for low-income workers), age 22 (for median-income workers), and age 24 (for high-income workers). They are assumed to work continuously until they reach age 65, unless disabled. The computer program calculates the probability that a worker will become disabled at some time in the future. It also calculates the probability that a worker once disabled will later re-enter the labor market. These probabilities were assumed to be identical for blacks and whites.

In each calculation of expected taxes and expected benefits, it is assumed that the worker has worked continuously from the time of entry into the labor market until the time the calculation is made. However, the calculation includes the probability of future disability.

Future Wages. Workers enter the labor market at a certain wage. From that point forward, the worker's real income is expected to grow at the same rate as the rate of growth of real wages in the economy as a whole. This rate is 1.5 percent under the Social Security Administration's "intermediate" projection.

Future Taxes. Unless otherwise noted, all projections are based on the assumption that promises made under Social Security will be kept and will be financed by increases in the payroll tax, whenever necessary, in order to pay promised benefits.

In Tables IX and X the payroll tax rate is assumed to be capped at 15.3 percent, and benefits are cut in future years in order to keep each of the three trust funds solvent.

Future Benefits. The amount of future benefits varies according to assumptions about life expectancy, the rate of inflation, the rate of growth of real wages, etc. The assumptions used are those of the Social Security Administration's intermediate projection. For retirement, disability and survivors benefits, it assumed that the benefit formulas currently written into law will remain in effect indefinitely into the future. For Medicare, no particular assumption is made about benefit formulas. Instead, it is assumed that the future amount spent per beneficiary will increase according to the intermediate assumptions.

Since Social Security benefits now are partly subject to federal income taxes, expected benefits are calculated net of these taxes. In general, one-half of Social Security income is subject to federal income taxes to the extent that total income exceeds \$25,000 for an individual and \$32,000 for a couple. Future marginal tax rates for families at different income levels were estimated, using the assumptions of the Social Security Administration.

Mortality Rates. Mortality tables for blacks and whites have been produced by the U.S. National Center for Health Statistics. The increase in future life expectancy was assumed to be identical for blacks and whites, based on the Social Security Administration's intermediate assumptions.

Expected Values. The computer program calculates the probability that an individual will live to all possible ages up to 105. For each possible lifespan, it calculates the costs and benefits associated with that lifespan using a four percent real rate of discount. Expected value is the sum of all possible outcomes, each weighted by its probability of occurring. These calculations include the probability of disability, as well as the probability of death, at each age.

APPENDIX B

PRESENT VALUE OF SOCIAL SECURITY FOR WORKERS WHO WERE AGE 20 IN 1986

Low-Income Workers

<u>Case</u>	<u>White</u>	<u>Black</u>
1. Single male worker earning 150 percent of the minimum wage.	- \$18,508	- \$26,751
2. Male Worker earning 150 percent of the minimum wage. Dependent spouse. Two children.	803	- 8,054
3. Male worker earning 150 percent of the minimum wage. Dependent spouse. No children.	- 3,051	- 12,325
4. Working couple. Both earn 150 percent of the minimum wage. Two children.	- 34,230	- 43,880

Assumptions:

1. Workers' average lifetime earnings equal 150 percent of the minimum wage (\$10,050 per year in 1986).
2. Workers enter the labor market at age 18.
3. Social Security Financing Alternative II B assumptions apply.
4. The real rate of interest is four percent.

Median-Income Workers

<u>Case</u>	<u>White</u>	<u>Black</u>
1. Single male worker earning the median income for male workers.	- \$55,358	- \$64,817
2. Male worker earning the median income for male workers. Dependent spouse. Two children.	- 28,893	- 38,556
3. Male worker earning the median income for male workers. Dependent spouse. No children.	- 35,202	- 45,580
4. Working couple. Male earns the median income for male workers. Female earns the median income for female workers. Two children.	- 77,284	- 86,992

Assumptions:

1. Male's average lifetime earnings equal the median income paid to adult male workers (\$26,605 in 1986). Female's average lifetime earnings equal the median income paid to adult female workers (\$16,472 in 1986).
2. Both workers enter the labor market at age 22.
3. Social Security Financing Alternative II B assumptions apply.
4. The real rate of interest is four percent.

High-Income Workers

<u>Case</u>	<u>White</u>	<u>Black</u>
1. Single male worker earning the maximum wage subject to the Social Security payroll tax.	-\$97,880	- \$106,891
2. Male worker earning the maximum wage subject to the Social Security payroll tax. Dependent spouse, two children.	- 67,017	- 76,400
3. Male worker earning the maximum wage subject to the Social Security tax. Dependent spouse. No children.	- 74,232	- 84,495
4. Working couple. Both earning the maximum wage subject to the Social Security payroll tax. Two children.	- 190,832	- 200,097

Assumptions:

1. Workers' average lifetime earnings are equal to, or greater than, the maximum taxable Social Security wage (\$42,000 in 1986).
2. Workers enter the labor market at age 24.
3. Social Security Financing Alternative II B assumptions apply.
4. The real rate of interest is four percent.

APPENDIX C

REAL RATES OF RETURN UNDER SOCIAL SECURITY FOR BLACKS AND WHITES

Low-Income Workers

<u>Case/Age</u>	<u>20</u>	<u>25</u>	<u>30</u>	<u>35</u>	<u>40</u>	<u>45</u>	<u>50</u>
Single male worker earning 150 percent of the minimum wage.	1.1 % 2.5 %	0.7 % 2.4 %	0.4 % 2.4 %	0.3 % 2.3 %	0.5 % 2.3 %	0.8 % 2.3 %	1.3 % 2.4 %
Male worker earning 150 percent of the minimum wage. Dependent spouse. Two children.	3.4 % 4.1 %	3.2 % 4.0 %	2.9 % 3.8 %	2.7 % 3.7 %	2.7 % 3.7 %	3.0 % 3.8 %	3.4 % 4.1 %
Male worker earning 150 percent of the minimum wage. Dependent spouse. No children.	3.1 % 3.8 %	2.9 % 3.8 %	2.7 % 3.7 %	2.6 % 3.6 %	2.7 % 3.7 %	3.0 % 3.8 %	3.4 % 4.1 %
Working couple. Both earn 150 percent of the minimum wage. Two children.	1.7 % 2.5 %	1.5 % 2.4 %	1.2 % 2.3 %	1.0 % 2.2 %	1.0 % 2.2 %	1.3 % 2.3 %	1.6 % 2.5 %

Assumptions:

1. Workers' average lifetime earnings equal 150 percent of the minimum wage (\$10,050 per year in 1986).
2. Workers enter the labor market at age 18.
3. At every age, workers are assumed to have worked continuously since entering the labor market.

First estimate is for blacks. Second estimate is for whites.

**REAL RATES OF RETURN UNDER SOCIAL SECURITY
FOR BLACKS AND WHITES**

Median-Income Workers

<u>Case/Age</u>	<u>20</u>	<u>25</u>	<u>30</u>	<u>35</u>	<u>40</u>	<u>45</u>	<u>50</u>
Single male worker earning the median income for male workers.	- 0.6 % 1.1 %	- 0.9 % 1.1 %	- 1.2 % 1.1 %	- 1.4 % 1.0 %	- 1.2 % 1.0 %	- 0.8 % 1.1 %	- 0.2 % 1.2 %
Male worker earning the median wage for male workers. Dependent spouse. Two children.	2.0 % 2.8 %	1.9 % 2.8 %	1.7 % 2.7 %	1.5 % 2.6 %	1.6 % 2.7 %	1.9 % 2.8 %	2.3 % 3.1 %
Male worker earning the median wage for male workers. Dependent spouse. No children.	1.8 % 2.6 %	1.7 % 2.6 %	1.5 % 2.6 %	1.5 % 2.6 %	1.6 % 2.6 %	1.9 % 2.8 %	2.3 % 3.1 %
Working couple. Male earns the median income for male workers. Female earns the median income for female workers. Two children.	0.7 % 1.6 %	0.5 % 1.6 %	0.3 % 1.5 %	0.1 % 1.4 %	0.2 % 1.4 %	0.4 % 1.5 %	0.7 % 1.7 %

Assumptions:

1. Male's average lifetime earnings equal the median income paid to adult male workers (\$26,605 in 1986). Female's average lifetime earnings equal the median income paid to adult female workers (\$16,472 in 1986).
2. Both workers enter the labor market at age 22.
3. At every age, workers are assumed to have worked continuously since entering the labor market.

First estimate is for blacks. Second estimate is for whites.

**REAL RATES OF RETURN UNDER SOCIAL SECURITY
FOR BLACKS AND WHITES**

High-Income Workers

<u>Case/Age</u>	<u>20</u>	<u>25</u>	<u>30</u>	<u>35</u>	<u>40</u>	<u>45</u>	<u>50</u>
Single male worker earning the maximum wage subject to the Social Security payroll tax.	*	*	*	- 2.6 %	- 2.4 %	- 2.0 %	- 1.3 %
	0.0 %	0.0 %	0.0 %	0.1 %	0.1 %	0.2 %	0.4 %
Male worker earning the maximum wage subject to the Social Security payroll tax. Dependent spouse. Two children.	1.1 %	0.9 %	0.8 %	0.7 %	0.8 %	1.1 %	1.6 %
	1.9 %	1.9 %	1.9 %	1.9 %	2.1 %	2.3 %	2.6 %
Male worker earning the maximum wage subject to the Social Security tax. Dependent spouse. No children.	0.9 %	0.8 %	0.6 %	0.7 %	0.8 %	1.1 %	1.6 %
	1.7 %	1.8 %	1.8 %	1.9 %	2.0 %	2.3 %	2.6 %
Working couple. Both earning the maximum wage subject to the Social Security payroll tax. Two children.	- 7.4 %	- 1.1 %	- 1.3 %	- 1.4 %	- 1.3 %	- 1.1 %	- 0.7 %
	- 0.1 %	0.1 %	0.1 %	0.2 %	0.2 %	0.4 %	0.6 %

Assumptions:

1. Worker's average lifetime earnings are equal to, or greater than, the maximum taxable Social Security wage (\$42,000 in 1986).
2. Workers enter the labor market at age 24.
3. At every age, workers are assumed to have worked continuously since entering the labor market.

First estimate is for blacks. Second estimate is for whites.

* = Very negative.

- Note 1. It should be noted that rate of return estimates for workers at different age levels are not exactly comparable. This is because at every age level workers are assumed to have worked continuously since entering the labor market. Thus, a worker age 50 has paid taxes to support disability and survivors insurance, but has never received any benefits from these programs. On the other hand, the calculation of expected benefits for a worker age 20 includes the probability of death or disability prior to age 50, in which cases the worker would cease paying Social Security taxes and his family would begin receiving survivors or disability benefits.
- Note 2. These rates of return differ somewhat from the numbers presented in Ferrara, Social Security Rates of Return for Today's Young Workers because in that study it was assumed that benefits would be cut when the trust funds ran out of money. In the current study we assume taxes will be raised to pay promised benefits.

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