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Stuart Butler and Peter Germanis (1983)

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ACHIEVING A “LENINIST” STRATEGY

Stuart Butler and Peter Germanis

Introduction

Marx believed that capitalism was doomed by its inherent contradictions, and that it would inevitably collapse—to be replaced by the next stage on the ladder leading to the socialist Utopia.

Lenin also believed that capitalism was doomed by its inherent contradictions, and would inevitably collapse. But just to be on the safe side, he sought to mobilize the working class, in alliance with other key elements in political society, both to hasten the collapse and to ensure that the result conformed with his interpretation of the proletarian state. Unlike many other socialists at the time, Lenin recognized that fundamental change is contingent both upon a movement’s ability to create a focused political coalition and upon its success in isolating and weakening its opponents.

As we contemplate basic reform of the Social Security system, we would do well to draw a few lessons from the Leninist strategy. Many critics of the present system believe, as Marx and Lenin did of capitalism, that the system’s days are numbered because of its contradictory objectives of attempting to provide both welfare and insurance. All that really needs to be done, they contend, is to point out these inherent flaws to the taxpayers and to show them that Social Security would be vastly improved if it were restructured into a predominantly private system. Convinced by the undeniable facts and logic, individuals supposedly would then rise up and demand that their representatives make the appropriate reforms.

While this may indeed happen, the public’s reaction last year against politicians who simply noted the deep problems of the system, and the absence of even a recognition of the underlying problems during this spring’s Social Security “reform,” suggest that it

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will be a long time before citizen indignation will cause radical change to take place. Therefore, if we are to achieve basic changes in the system, we must first prepare the political ground so that the fiasco of the last 18 months is not repeated.

First, we must recognize that there is a firm coalition behind the present Social Security system, and that this coalition has been very effective in winning political concessions for many years. Before Social Security can be reformed, we must begin to divide this coalition and cast doubt on the picture of reality it presents to the general public.

Second, we must recognize that we need more than a manifesto—even one as cogent and persuasive as that provided by Peter Ferrara.¹ What we must do is construct a coalition around the Ferrara plan, a coalition that will gain directly from its implementation. That coalition should consist of not only those who will reap benefits from the IRA-based private system Ferrara has proposed but also the banks, insurance companies, and other institutions that will gain from providing such plans to the public.

As we construct and consolidate this coalition, we must press for modest changes in the laws and regulations designed to make private pension options more attractive, and we must expose the fundamental flaws and contradictions in the existing system. In so doing, we will strengthen the coalition for privatizing Social Security and we will weaken the coalition for retaining or expanding the current system. By approaching the problem in this way, we may be ready for the next crisis in Social Security—ready with a strong coalition for change, a weakened coalition supporting the current system, and a general public familiar with the private-sector option.

Framework for Reform

Peter Ferrara's "family security plan" provides a sound framework for reform.² The Ferrara plan resolves the contradiction within the existing system and provides a realistic phase-in process for a private pension plan. Recent efforts to publicize and implement the Ferrara plan, however, only confirm the fact that a successful reform strategy must be designed within a framework of well-understood constraints

¹See Peter J. Ferrara, *Social Security: The Inherent Contradiction* (San Francisco: Cato Institute, 1980); *Social Security: Averting the Crisis* (Washington, D.C.: Cato Institute, 1982); and *Social Security Reform: The Family [Security] Plan* (Washington, D.C.: Heritage Foundation, 1982).

²Ferrara, *The Family [Security] Plan*, pp. 49–73.

and opportunities; otherwise we will fall into the same political traps that have discouraged many a would-be reformer.

In an effort to identify a broad framework for Social Security reform, the Heritage Foundation (1982) gathered various experts, who discussed the essential ingredients of reform. The principles and observations that emerged from that gathering can now be summarized.³

Calming Existing Beneficiaries

The sine qua non of any successful Social Security reform strategy must be an assurance to those already retired or nearing retirement that their benefits will be paid in full. It was irresponsible in the first place for the federal government to promise unrealistic benefits. But it would be even more irresponsible now to break faith with the millions of people who have based their retirement plans on these expected benefits. Instead of spreading widespread panic among our elderly, which will only undermine our efforts to reform the system, we should acknowledge the system's liabilities as a total writeoff.

From a purely political standpoint, it should be remembered that the elderly represent a very powerful and vocal interest group. This power was reflected in the recent bailout plan, which made no effort to address the system's underlying structural problems. One congressman, with disarming frankness, implicitly evidenced that considerable power when he explained his position on Social Security reform: "I have no intention of trying to explain what needs to be done, just give me a vote on something that can save the damn thing until I retire."⁴

The political power of the elderly will only increase in the future. The proportion of the population over 65 will rise steadily, from 11.3 percent today to 18.3 percent by 2030. So any proposal aimed at cutting benefits will face increasingly stiff opposition from the elderly, undermining the prospects for genuine reform. Any plan to change the system must therefore be neutral or (better still) clearly advantageous to senior citizens. By accepting this principle, we may succeed in neutralizing the most powerful element of the coalition that opposes structural reform.

Educating the Public

A second prerequisite for reform is to improve the public's understanding of the current program. During the recent financing crisis,

³For an edited transcript of that conference, see Peter Germanis and John Palffy, eds., *Rebuilding Social Security*, Heritage Lectures 18 (Washington, D.C.: Heritage Foundation, 1982).

⁴Rep. Marvin Leath (D-Tex.) quoting one of his colleagues in "Social Security Expediency," *Washington Times*, March 23, 1983.

there was only a vague awareness among the general population that the system was in serious trouble; the true nature of the problem and the proposed reforms were understood by very few Americans.

A comprehensive program of economic education must confront people with the facts about Social Security and the problems it faces. The many myths surrounding the system must be dispelled, especially the popular belief that Social Security is an "insurance" program financed by "contributions" that provide an "earned annuity." That many have come to rely on Social Security as their major or sole means of support, not realizing that it was originally intended only to supplement other sources of retirement income, is apparent from a reading of the popular press. Over the years, the program has become surrounded by a cloak of demagoguery and misinformation, woven by political leaders and interest groups seeking to further their own ends. If the public is ever to support real Social Security reform, this cloak must be removed.

Recognizing Successful Alternatives

Despite the unwillingness of Congress to undertake or even consider real reform, the public has shown a great deal of interest in private alternatives to Social Security. In a poll conducted by the Sindlinger Company for the Heritage Foundation, for instance, a majority of people surveyed said that they would favor a voluntary system. Even more people expressed the view that the private sector would be a more efficient vehicle than Social Security for providing pension benefits. The recent upsurge in savings put into Individual Retirement Accounts (IRAs) is further testimony to the public's enthusiasm for private pension plans. A *New York Times*/CBS News poll suggested that Americans had invested about \$30 billion in tax-free IRAs for the 1982 tax year, which is much higher than the Treasury Department had estimated. According to the poll, nearly one out of every five employed adults had opened an account by early April.⁵ Extending this option as an alternative to Social Security could both increase savings and provide funds for long-term capital investments.

A restricted private option is now being tried in Great Britain. Britain has a two-tier retirement benefit system made up of a mandatory basic pension plan and an earnings-related pension. It is possible, however, to opt out of the earnings-related pension (but not the basic pension). The employer has the legal responsibility of

⁵Robert A. Bennett, "I.R.A.s a Hit With Taxpayer," *New York Times*, April 15, 1983, p. D1.

making the decision to allow the employees to contract out of the plan. If an employer does decide on the contracting-out option, he is required to provide private pension benefits at least equal to those in the government program. This contracting-out scheme for the second tier has enjoyed a great deal of success. Since 1978, when it was fully initiated, nearly 45 percent of all British workers have enrolled in private pension programs.

The British system indicates that many employees are willing to choose a private retirement option in preference to a government-guaranteed plan. It also indicates that workers are willing to pay a price to leave Social Security. British workers who opt out of the earnings-related element of Social Security do not obtain a reduction in payroll taxes that is equal to the benefits they forgo. In other words, those who opt out still pay some tax to support existing and future beneficiaries of the government system.

According to John Goodman, the payroll-tax reduction available to those who contract out is carefully designed to be just large enough to encourage enough workers to opt out (thereby reducing future liabilities), while ensuring that these workers still provide considerable tax revenue to subsidize existing beneficiaries.⁶ It does seem that the price people are willing to pay to leave Social Security is substantial. Perhaps in the United States it is large enough that those wishing to leave the system can cover a large part of its current obligations to beneficiaries while it still enables a high proportion of workers to opt out, thus reducing the system's future obligations.

A Plan of Action

The background issues discussed above suggest a political strategy to achieve basic reform of the Social Security system in the fashion suggested by Peter Ferrara. There are two main elements to this strategy.

The first element consists of a campaign to achieve small legislative changes that embellish the present IRA system, making it in practice a small-scale private Social Security system that can supplement the federal system. As part of this campaign, the natural constituency for an enlarged IRA system must be identified and welded into a coalition for political change. If these objectives are achieved, we will meet the next financial crisis in Social Security with a private alternative ready in the wings—an alternative with which the public is familiar and comfortable, and one that has the backing of a powerful political force.

⁶John Goodman, "Lessons From Abroad," in Germanis and Palffy, pp. 23–31.

guerrilla warfare

The second main element in our reform strategy involves what one might crudely call guerrilla warfare against both the current Social Security system and the coalition that supports it. An economic education campaign, assisted by modest changes in the law, must be undertaken to demonstrate the weaknesses of the existing system and to allow it to be compared accurately (and therefore unfavorably) with the private alternative. In addition, methods of neutralizing, buying out, or winning over key segments of the Social Security coalition must be explored and formulated into legislative initiatives. The objective of this element of the strategy complements the first. The aim is to weaken political support for the present system when the next financial crisis appears. This two-pronged strategy will now be considered in more detail.

Creating a Private Model

Expanding IRAs

IRAs are a powerful vehicle for introducing a private Social Security system. They are extremely popular with the public. No politician wishing to be reelected would even suggest that the tax deduction for IRAs should be eliminated. Building on this strong political support, proponents of a private Social Security system should press for an extension of the deduction. No doubt Congress would find it difficult to reject proposals designed to allow workers to provide a more secure retirement for themselves.

The aim should be to secure legislation that not only indexes the basic IRA deduction and makes it available to all (including non-working spouses) but also allows people to take a much larger IRA deduction if it is used to purchase old-age health insurance, disability insurance, or other benefits now available through Social Security. Ideally, this “super IRA” would be close to that of the Social Security system in both size and structure. As the payroll-tax rate increases, the maximum tax-deductible contribution to an IRA should increase to the same cash level. Similarly, the prescribed allocation of an IRA among retirement income, health insurance, and other uses should reflect the equivalent allocation of the Social Security tax.

The reason for designing a “super IRA” law with these restrictions is purely political. Expanding the IRA system in this way would make it a private prototype of Social Security. People could then compare the two alternatives. The public would gradually become more familiar with the private option, and would no doubt view it as a parallel system. If that did happen, it would be far easier than it is

now to persuade people to adopt the private plan as their principal source of old-age insurance and retirement income.

Coalition Building

Building a constituency for Social Security reform requires mobilizing the various coalitions that stand to benefit from the change. Such a constituency is already extensive, but mobilizing it could become a self-generating process. If an extension in the IRA system is achieved, for instance, it will expand the natural self-interest constituency by making IRAs more attractive to more people. This wider constituency will then be better able to achieve further extensions that in turn will further expand the constituency. This self-generating process in the private sector is identical to the political process that has forced programs in the public sector to grow and serve ever larger constituencies.

The business community, and financial institutions in particular, would be an obvious element in the constituency. Not only does business have a great deal to gain from a reform effort designed to stimulate private savings, but it also has the power to be politically influential and to be instrumental in mounting a public education campaign. This influence was clearly demonstrated in the fight to repeal withholding on interest and dividend income. The banking industry's ability to lobby and garner support for the repeal effort led many in Congress to reverse their earlier votes. Financial institutions, likewise, have been extremely effective in marketing various types of savings plans, such as All-Savers Certificates and IRAs, thereby building up public acceptance of these innovations.

Interest groups concerned with Social Security reform can be divided into the young, the middle-aged working population, and the retired or those nearing retirement. Of these, the young are the most obvious constituency for reform and a natural ally for the private alternative. The overwhelming majority of people in this group have stated repeatedly that they have little or no confidence in the present Social Security system. Discontentment will only grow as the taxes needed to support the system continue to rise, and as the prospects for a reasonable return on one's "contribution" continue to fade.

Despite misgivings about Social Security, however, the young have yet to have a significant impact on the political process as it relates to reform measures. It is imperative, therefore, that they be informed about the problems inherent in the current system and that they be organized behind the private alternative.

Clearly, an important thread running through the entire strategy is education. An education campaign is needed to gain the support of

key individuals in the media as well as to win over vital constituencies for political reform. The banking industry and other business groups that can benefit from expanded IRAs must be encouraged to play a central role in educating the public about the benefits of the private plan. They can do this both through their commercial advertising and through public relations.

Weakening the Opposition

Individual Accounts

To emphasize how unfavorably Social Security compares with the private alternative, the Social Security Administration should be required to establish an individual account for each person participating in the program. Furthermore, each person should be provided with an annual statement showing how much he has paid into the system and what benefits he can expect to receive. Individuals could then compare their returns from private investment with their returns under Social Security. Such a scheme would illustrate in cold numbers just what the program means for different individuals, and would help reveal the inter- and intragenerational distribution that occurs under the current system. The retired population might then come to realize that they have not purchased an earned annuity but instead are receiving a tremendous welfare subsidy. Younger workers, on the other hand, would see just how much of a loss they are taking by participating in the program. This mechanism for demonstrating the individual gains and losses that occur under Social Security is a key step in weakening public support for the present system.⁷

The technology for creating a reporting system already exists. Using it simply requires an improvement in the computer system of the Social Security Administration. The SSA, however, undoubtedly would claim that the enormous cost and complexity of such a system would prevent it from providing what would be highly embarrassing information. Fortunately, there are private-sector companies, such as Accucomp Financial Services, that are willing to compile the necessary information from an employee's tax returns for a very modest fee. (Accucomp does it for \$35.)⁸ The SSA could be required to contract out the service to such companies, or taxpayers could receive a tax credit for arranging it themselves.

⁷Anthony Pellechio and Gordon Goodfellow have calculated these in "Individual Gains and Losses from Social Security before and after the 1983 Amendments," *Cato Journal* 3 (Fall 1983): 417-42.

⁸See Accucomp's ad in the 1983 edition of *Money Guide* (published by the editors of *Money*), p. 61.

Detaching Supporters of Social Security

The final element of the strategy must be to propose moving to a private Social Security system in such a way as to detach, or at least neutralize, segments of the coalition that supports the existing system. A necessary step toward this objective is to honor all outstanding claims on the current system. Without such a commitment, we can never overcome the political opposition to reform, because the retired (or nearly retired) population will continue to strongly oppose any package that threatens to significantly reduce their benefits. Retaining the obligation to fund existing liabilities, however, will necessarily place constraints on the mechanisms that can be used to move the country towards a private system.

The problem of implementing a private system makes the British model particularly attractive. It is clear, in Britain at least, that workers are quite prepared to make some payments into Social Security (even though they will not receive benefits), provided they acquire the right to escape from a governmentally operated retirement system in which they have little confidence. We should consider, therefore, modifying Peter Ferrara's phase-in plan.⁹

Under Ferrara's plan, workers would be allowed to invest part, and eventually all, of the money they now pay into Social Security in expanded IRAs, in return for a corresponding reduction in their future Social Security benefits. Under our proposed modification, workers who choose to opt out of the system would not only lose their corresponding future benefits but would even have them reduced somewhat further for the privilege of getting out of Social Security. This added reduction in benefits could be viewed as a tax that would be used to pay off the system's remaining obligations.

An interim "opting-out tax" hardly conforms with the principles of fairness; yet it makes good political sense. If the support for leaving Social Security is as great as it seems, then it is unlikely that the level of contracting out will be significantly reduced by requiring workers to make some payment into the system while they withdraw and lose benefits (assuming, for the sake of argument, that they ever would have received those benefits!). But the opting-out tax would have important political advantages. It would serve to calm the fears of the elderly, because the net phase-out losses to the Social Security fund would be smaller under opting out than under the Ferrara plan, for virtually the same reduction in future liabilities. Hence, under

⁹We refer specifically to Ferrara's "family security plan," as discussed in *The Family [Security] Plan*, pp. 49-73.

an opting-out plan the support needed from general revenues would be smaller, and the threat to the trust funds would be reduced.

This modification would slightly dampen the enthusiasm of young workers, who are a strong segment of the coalition for change. But on the other hand, this modification would help to meet the concerns of the elderly and of the taxpayers and beneficiaries of federal programs who might resist the use of general revenues to cover the phase-in period.

Detaching workers who have made substantial tax payments into Social Security may not prove to be too difficult. A number of proposals have been put forward in which the worker's accumulated "contributions," plus interest, would be given to him in form of an interest-bearing bond, payable at retirement.¹⁰ This bond would have a market value and could be sold, with the proceeds to be invested in a tax-deductible IRA. Using an appropriate version of this proposal should make it possible to gain some support even from those who have a substantial stake in the current system.

Conclusion

The last two years have demonstrated beyond a doubt that Social Security can be reformed only by treating the issue primarily as a political problem. There is little point in arguing over the nuances of theoretical plans if the political dynamics are not altered; no amount of logic will overcome an unfavorable coalition of interest groups.

It is also clear that the strategy we adopt must be flexible. It would be self-defeating to lay down a rigid blueprint and blindly adhere to it. Indeed, we must be prepared to refine segments of the plan, such as the opting-out mechanism or the design of the "super IRA," to meet the changing political circumstances.

Finally, we must be prepared for a long campaign. The next Social Security crisis may be further away than many people believe. Or perhaps it will occur before the reform coalition is strong enough to achieve a political breakthrough. In either case, it could be many years before the conditions are such that a radical reform of Social Security is possible. **But then, as Lenin well knew, to be a successful revolutionary, one must also be patient and consistently plan for real reform.**

¹⁰See Ferrara, *The Inherent Contradiction*, pp. 340–50.