



Reaffirming the Role of Social Insurance

by

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Tuesday, June 3, 2014

at the National Press Club
Washington, DC

winner of

The Robert M. Ball Award **2014**
FOR OUTSTANDING ACHIEVEMENTS IN SOCIAL INSURANCE



About the *Robert M. Ball Award for Outstanding Achievements in Social Insurance*

Each year, the National Academy of Social Insurance presents the Robert M. Ball Award to an individual whose recent work has made a significant impact on the U.S. social insurance system. Selection criteria for the award include: Innovation in changing, educating about or otherwise furthering public understanding and informed policy-making in a specific area of social insurance and Effectiveness in deepening public understanding, fostering collaboration, informing policy, implementing policy, or teaching others about social insurance.

No individual has done more to advance American social insurance program than Robert M. Ball. From his early appointment in a field office to his selection as Commissioner of Social Security by President Kennedy in 1962, to advisory roles in each of the following presidential administrations, Bob Ball sought a balance between political pragmatism and his determination to protect the principles of social insurance. Bob Ball served as Commissioner of Social Security from 1962 to 1973. He also played a crucial role in the origin of Medicare in 1965, and then successfully carried out the ambitious task of implementing the program. Ball founded the Academy in 1986, and continued to advise presidential administrations and policy-makers and to write on Social Security, Medicare, national health insurance and welfare until his death in January 2008 at the age of 93.

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About the National Academy of Social Insurance

The National Academy of Social Insurance is a nonprofit, nonpartisan organization made up of the nation's leading experts on social insurance. Its mission is to advance solutions to challenges facing the nation by increasing public understanding of how social insurance contributes to economic security. Social insurance encompasses broad-based systems that help workers and their families' pool risks to avoid loss of income due to retirement, death, disability, or unemployment and to ensure access to health care. Despite the importance of social insurance in the United States, few people know the programs well. The Academy was established as an independent organization to promote informed discussion and debate on social insurance issues and to stimulate fresh thinking.

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Although there have been a lot of changes in our economy and the status of American households, the basic reasons and rationale for establishing Social Security in the 1930s and Medicare in the 1960s have not changed. We have not outgrown our need for these key programs; they have become a part of the fabric of our financial and social well-being. People may indicate in surveys that they fear these programs may not be there when they retire; nonetheless, they behave as if these programs are there and assume they will form a key part of their well-being as they age. We have seen no movement to indicate that the private sector is ready and able to take over except at the margins.

To some extent I am preaching to the choir tonight, but this choir is one that is heard in Washington and elsewhere. The work we do contributes to the debate about the future and we can help shape it in a more positive way. Good research is needed to remind decision makers about the implications of their proposals and to highlight what has changed over time. Good stewardship of the programs in terms of smooth operations and sharing information on what social insurance does are also important for maintaining support for social insurance. We cannot accept the skepticism and hostility of critics who choose not to fully understand these programs or how they help people. The legacy of Bob Ball—who we remember in this event tonight—is to respond positively and constructively in reaffirming the role of social insurance.

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Rationale for Social Insurance

Consider the basic reasoning behind social insurance programs. First, financial security and health insurance represent insurable events. People need protection against periods of disability or unemployment that can reduce their ability to save for retirement. Indeed, the movement away from defined benefit pensions to a defined contribution pension environment means that individuals today and going forward have less private insurance protection against untoward events than in earlier eras. They are on their own to ensure that there are sufficient resources in their pension plans—rather than having basic guarantees as used to be the case. Failure to save consistently or poor investment choices can lead to inadequate savings at retirement from the private pension portion of an individual’s resources. And in actuality the situation is even worse: the data indicate that only a minority of Americans are saving substantial amounts of resources in this way. And many are unaware of how much they really need in order to sustain a reasonable standard of living in retirement.

Insurance for health expenditures for those over the age of 65 and persons with disabilities represents another liability best served by an insurance program. The need for insurance arises not only from the variability in need for health care but also from the rapid increase in the costs of care that have occurred over the last 40 years.

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The insurance requirements for financial and health security arise not only on an individual level, but society also has a stake in the outcomes. We cannot thrive as a nation without the stability that such insurance assures for a highly vulnerable portion of the population.

While policy makers in the U.S. often defer to the private sector to solve a variety of problems, the private sector has never been able or willing to fully take on these financial and health protections even for those who can pay. The public pooling of risk across the whole population is a much more efficient way to address large challenges such as economic and health security in old age. And private markets have never handled well the notion of redistribution across individuals to bolster those with lower incomes. In fact, this need extends beyond retirement programs.

We have largely chosen to think of social insurance as protection at the end of life, in part because of a recognition that hardships arise that are beyond the control or responsibility of individuals but reflect broad based societal challenges. It is simply not practical to decide who is worthy or not after a lifetime of experience and hence it has been easy to justify broad-based programs. The case for those of working age has been more difficult to make. But, over time, we have moved into new areas such as earned income credits; unemployment compensation, and most recently health insurance for the young —reflecting the need for protections across the lifespan. None of these have the same level of support as yet as Social Security and Medicare, but that may well come in time.

Key Aspects of Social Insurance

Linking social insurance programs to direct contribution has strengthened people’s loyalty and acceptance. Polls continue to indicate that even in an era of great resistance to new taxes, raising funds to support these programs would be acceptable to most Americans. The linking of funding and benefits is a characteristic that we have largely ignored for other programs such as health insurance for the young—perhaps at the cost of acceptance over time.

One of the real benefits and advantages of Social Security and Medicare as compared for example to SSI and Medicaid is that we have established a very un-American approach that focuses more on inclusion than exclusion. That is, these programs are largely universal, extending coverage to almost all Americans; the eligibility rules are simple and straightforward—and linked to the contributions that people are required to make. Unlike the so-called welfare programs that focus on strict eligibility standards and often onerous application processes, Social Security and Medicare are accepted as part of the basic structure of our economy.

Social insurance emphasizes inclusion and assuring universal coverage. Ironically, it is probably one of the reasons why these programs are so popular; people believe that they have a right to participate and receive benefits.

In practice, much of our public policy focuses on setting the eligibility criteria and tests very high so that ineligible people are not admitted. The United States operates many of its programs on the principle of preventing ineligible persons (“welfare cheats”) from getting through the screening process. Consider, for example, the very stringent process of getting on welfare or Medicaid. Or, in the case of unemployment compensation, the reluctance to extend long term benefits based on the concern that some who are not “worthy” or looking hard enough for jobs would get benefits. Welfare programs tend to be predicated on the principle that it is most important to keep out those who do not “deserve” benefits even if that means discouraging those who do qualify.

Social insurance, in contrast, emphasizes inclusion and assuring universal coverage. Ironically, it is probably one of the reasons why these programs are so popular; people believe that they have a right to participate and receive benefits. The near universal nature of these programs means that we have implicitly chosen to emphasize inclusion. It is not quite clear why these programs have thrived in an environment with so much emphasis in the other direction.

Another key aspect of social insurance is its progressive nature. The formula for Social Security benefits results in lower replacement of wages for those with the highest earnings. And the fact that everyone pays a standard percentage in payroll taxes for Part A of Medicare and receives essentially the same benefit also makes it progressive. Although the rules are clear and available to anyone who wishes to examine them, most Americans are not knowledgeable about the Social Security benefit formula, for example, and likely do not focus on this progressivity. Nonetheless, this element was very much a consciously designed feature of both Social Security and Medicare. These programs balance universality with progressivity.

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Over time these basic tenets of social insurance have proven to be both stable and popular. Even politicians who are most anxious to limit the role of government concede that Social Security and Medicare should be there—although with additional limitations.

Adjusting to Change

A large number of aspects of our economy have changed over the years, requiring a careful reconsideration of whether our social insurance programs are still appropriate and if so, what adjustments or modifications may be needed. Adjustments are inevitable as the economic and social situations we face change over time. But it is important to make sure that the adjustments to these programs actually fit the new situations. Ironically, some of the very issues that increase the need for social insurance are sometimes used as rationales for cutbacks. For example, the rising costs of health care over time explain much of the growth in the Medicare program. This is an issue that individuals did not cause; it reflects much more systemic change in our health care system. It also increases the pressures on older and disabled Americans. Why then do people use that as the reason to argue that Medicare must be cut as a response?

To think about what adjustments are needed over time, it is important to consider how our socio-economic environment is changing and what that may mean for social insurance in the future.

1. Inequality issues

Perhaps the most significant area where adjustments may be called for arises with respect to the increased inequality in wages and income that have been taking place since the 1970s. This has been occurring across the income spectrum. Large numbers of people remain in poverty, and wages for middle class families are stagnant, while shares of income attributable to the very top of the income distribution have skyrocketed. In addition, if we had better data on lifetime incomes and wealth, we would see a similar pattern, reflecting issues such as problems with unemployment, health problems that take people out of the labor force and other factors that affect not only annual earnings but the consistency and certainty of earnings over time.

This inequality relates directly to our social insurance programs, particularly Social Security. When wages rise more slowly for middle income and lower income workers over time, Social Security benefits will also be lower for those individuals when they retire. Periods of extremely low or no earnings reduce the formula as well. And to the extent that a greater share of wages go to those with very high incomes, Social Security contributions which are subject to an upper bound, grow more slowly. And finally, if more of our GDP goes to capital than to labor, Social Security benefits are also going to be smaller as a share of GDP. Inequality over Americans' worklives translate into a smaller overall role for Social Security and less progressivity in Social Security benefits.

What about Medicare? Medicare has been tinkered with more than Social Security. Here, interestingly, some of the changes made to reduce spending have increased progressivity; eliminating the cap on contributions and adding high income premiums have reduced the level of benefits received by those with higher incomes. And while this improves progressivity, it also raises concerns about retaining public support for Medicare and maintaining the sense of a universal program as higher income persons see their benefits erode. The balance between progressivity and inclusion is at issue. And, it also raises the issue of complicating the program.

2. The Period of Retirement

Toward the end of the 20th century, one of the biggest issues raised around the challenges facing social insurance was the issue of age of retirement. The relentless downward march of retirement age led to concerns that Social Security and Medicare would have to suffice over longer and longer periods as people retired earlier. In addition, one of the successes of our society (and perhaps of the contribution of Social Security and Medicare) is the increase in life expectancy. But it has been treated as a “problem” that needs to be attended to, particularly when linked to lower ages of retirement, and lower rates of birth and immigration.

This issue may be self correcting, however. Age of retirement is showing a steady increase, although not at a very rapid pace. And longer life expectancies seem to have also slowed somewhat—certainly in comparison to other countries.

Nonetheless, there are still many calls for increasing the age of eligibility for social insurance programs to address this “problem.” Foremost, we need to ask whether this is a reasonable strategy for all Americans. Early retirees tend to be of two types: those who can afford to retire and for whom it is fully voluntary, and those who face significant challenges in obtaining or retaining employment and for whom retirement becomes the least undesirable option. Minorities, persons with health problems, those with low skill levels will all be disproportionately disadvantaged by raising the age of retirement.

Moreover, many of those who call for such changes often fail to recognize that Social Security benefits are scaled by age of retirement already. And raising Medicare's eligibility age saves very little and creates a number of unexpected results.

3. Cost of health care

The rapid increase in the cost of health care is essentially a “blame the victim” issue. The benefit package in 2014 is remarkably similar to that offered in 1966 to new enrollees in Medicare—with the exception of the prescription drug benefit. Certainly the quality of care and its effectiveness has improved over the years and we can now safely perform services on older and frailer individuals, so use of care has also risen. Nonetheless, much of the cost increase reflects the much higher rise in prices for health care than for other

goods and services—and much higher growth in the costs of care relative to the incomes of Medicare beneficiaries. Consequently, Medicare beneficiaries pay a greater share of their incomes than in 1966 for those services and treatments that Medicare does not cover. Just as the federal government has experienced higher costs—so have beneficiaries.

We also know that Medicare does at least as well and often better than the private insurance sector in holding down these costs. And recent experience with private health insurance underscores the fact that private companies cannot and will not take on all the risks of health care without assurances for a stable risk pool. Nonetheless, the response by many policy makers is to cut the program.

4. How the private sector has stepped up (or not)

Not many years ago, there was a short lived attempt to privatize Social Security with a lot of people arguing they could go it alone and do better for themselves if they did not have to contribute to Social Security. Recession under President Bush—and I would like to think good analysis by people in this room and our colleagues-- helped short circuit this movement. The reductions in private pension generosity and the shift toward defined contributions also underscored that Social Security was the source of stability and certainty for individuals. But perhaps even more importantly, politicians also underestimated that Social Security has become part of the fabric of our financial well-being.

Medicare is now under a similar claim that private approaches would do a better job of meeting needs for health insurance for the aged and disabled. This is a policy initiative that does not want to die. Perhaps this is because health care is complicated and many politicians either cannot resist interfering or do not know how to organize change, they are skeptical about the ability to see Medicare succeed in the future. There is, however, no evidence that the private sector is ready or able to handle this issue without enormous oversight by the federal government. Recent experience with the private health insurance market offers key lessons; those who did not have some type of group access either faced prohibitively expensive premiums or exclusions as companies denied coverage or limited protection with extensive pre-existing condition exclusions. The Affordable Care Act (ACA) is moving to improve this, but the complexity of the ACA's rollout, the confusion on the part of consumers, and uncertainty about premium growth in the future suggest that private sector efforts under the auspices of a strong regulatory system is not a panacea.

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Responses to the changes

What then are policy options that make sense in the context of the changes and the continuing need for a strong social insurance framework?

1. Taxes vs. benefits

One aspect of social insurance that has not kept up with the changes described above is the need to appropriately finance these programs. Early writings about Social Security and Medicare recognized that tax rates would need to be increased over time in response to various changes. For example, in 1970, Robert Myers wrote about the need to deal with medical costs that would rise faster than other prices by increasing what we ask workers to contribute into the system. But, while the costs of basic Medicare (Parts A and B)

on a per capita basis have risen by over 350 percent since 1987, the rate of taxes on workers for Part A of the program has remained unchanged. The cap on wages subject to tax was eliminated, but this has not been sufficient to make up for the health care cost growth and increases in the number of beneficiaries. If we are unwilling as a society to raise taxes, we face two choices: cut benefits or allow the system to increasingly be financed by deficit spending. If you listen to political promises, Americans are being promised that they can have it all: “protecting” Medicare without having to pay higher taxes. No serious analysts, however, have ever discovered any reasonable way to achieve that slight of hand. And in the case of Social Security, most don’t even try to argue something for nothing. Thus, we continue to simply delay the inevitable.

An unwillingness to pay for the services we want as a society is certainly not unique to social insurance. Just look at the underfunding of our transportation systems and other infrastructure needs. And from this week’s headlines, long waits at the Veterans Administration reflect budget limitations as much as inefficiencies in management processes—yet the majority of articles castigating the Obama administration failed to talk about sufficiency of financing. We would rather engage in wishful thinking that greater efficiencies in government can resolve all problems.

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Many politicians prefer benefit cuts to tax increases but this flies in the face of the crucial role of social insurance and the need to appropriately respond to change such as increased inequality. The biggest change needed in these programs is a willingness to realistically address the need for greater financing. Finding any politician of any stripe willing to honestly take this on is a difficult search, however.

2. Increasing progressivity

In addition to the overarching issue of the size of these programs is the question of targeting within them. Do we want our major social insurance programs to play a greater role in reducing inequality? Here again is a political opportunity to address this issue head on. But even if there is no political will, analysis should focus on the extent to which some changes could make benefits more progressive, even if we do not yet have consensus on what that balance should be. I would argue that at the least, we should not move in the other direction.

Consider how Social Security might change to offset at least some of the increase in inequality. For example, the formula that translates wages into a primary insurance amount could be made more progressive. Alternatively, we could think about reinstating a minimum Social Security benefit. On the revenue side, raising the tax limit to capture a more consistent share of GDP could certainly be justified based on the economic trends. The share of total wages subject to Social Security contributions has declined to just over 83 percent in 2012. If 90 percent of wages—the share originally captured by FICA contributions—were included, the revenue base for Social Security would rise by nearly \$500 billion.

Other options that are sometimes suggested would likely *reduce* Social Security’s progressivity: raising the normal retirement age or restricting when early benefits could begin would likely harm lower and moderate income persons to a greater extent. Similarly, given the Great Recession and the likelihood of workers with a number of years of low or no earnings, any increase in the number of years needed to qualify for benefits could be counterproductive.

Raising the Medicare retirement age is also a problematic option and despite the availability of the ACA, postponing eligibility for Medicare would likely harm moderate income families. It would also have adverse consequences on older beneficiaries who would face higher premiums as the “inexpensive” beneficiaries are taken out of the program. And these “inexpensive” beneficiaries could raise the costs of insurance to those who are in their early 60s if they are added to ACA risk pools. These unintended consequences are under-examined but very important. And since Medicare has already had a number of adjustments to it to increase its targeting of benefits, the need here is to consider whether the balance is appropriate; are high income beneficiaries feeling increasingly disenfranchised? Will that undermine the strength of our social insurance programs? We need to step back and re-examine how Medicare functions in meeting the needs of older Americans and persons with disabilities before moving further in this direction

3. Dealing with health care delivery

Medicare has done a better job of becoming a more progressive program, but it faces a different but still difficult challenge from the rapid increase in the costs of health care. As a program that does not go directly to beneficiaries but instead funds the services that they need, the complexities and opportunities for change are greater than with Social Security. If greater efficiencies can be achieved, then benefits can rise without an increase in funding—and this will also help to hold down the out of pocket costs that beneficiaries face. But that “promise” is also subject to a lot of exploitation. Wishing for greater efficiency does not make it so. And one person’s wasteful benefit is another’s vital service—as well as a provider’s income.

Care is also needed in the enthusiasm sometimes expressed for “empowering” consumers. Too often this is a euphemism for “impoverishing” consumers by making them more responsible for the costs of their care. Without the tools to judge what services are necessary, many of us will get it wrong and in the long run raise the costs of the program when needed care is delayed. And we know from research that you get the biggest bang for your buck in reducing use from those with low incomes; they simply do without care whether necessary or not because they cannot afford it. That is not an appropriate goal for Medicare reform.

Conclusion

The increased skepticism about government and negative attitudes about any increase in taxation can be readily exploited by those who would argue that we have outgrown our need for these programs or that we can no longer afford them. The key role that social insurance plays in the lives of all Americans is something that needs to be reinforced to a greater extent than even its political supporters seem willing to do at present. The policy community must redouble its efforts to ensure that good analysis forms the basis for future change. Bob Ball would expect no less.

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