Chile model ahead for Social Security?

by Leif Johnson

When Congress reconvened Sept. 9, the Senate Finance Committee sat looking at a welter of Social Security cuts and borrowing schemes amid a silly debate between the short-term "patch it up" advocates and the holders of the "long view" who are trying to jangle the public with the doom of the entire Social Security System some time after the year 2020.

Two significant cuts have already been made. In the Aug. 13 budget bill, Social Security benefits to students whose parents are deceased and the minimum $122 a monthly benefit were eliminated. Beyond these specific actions—whose results can only be less schooling and more welfare cases—chaos reigns.

Health and Human Services Secretary Richard Schweiker's May 12 package of draconian cuts is still the Reagan administration's official program. House Ways and Means Social Security Subcommittee Chairman Jake Pickle (D-Tex.), advised by the American Enterprise Institute financial oligarchs, has offered a detailed cure for short- and long-term problems that means cuts now and more cuts in the future. Sen. Patrick Moynihan (D-N.Y.), an advocate of depopulation, is pretending to defend the elderly. House Majority Leader Dan Rostenkowski (D-Ill.), who seems genuinely confused, is waiting for House Speaker Tip O'Neill to pass along a program drafted by the Boston Brahmins who help O'Neill tie his shoes.

The confusion is quite intentional. As the press has been chiming for six months, the public is finally aware of the problem, and the taboo of tampering with the hard-won system of security for our retired workforce has been broken. The purpose of this deliberate confusion is therefore to soften the public for the shock of the bottom line: junking the Social Security System entirely and replacing it with a "private system" run by banks and insurance companies. The model is the private social-security system recently implemented by the military dictatorship in Chile (see box).

In the April/May 1980 issue of *Council Review*, the magazine of the American Council of Life Insurance, Stanford G. Ross, a former U.S. Social Security commissioner and chairman of the Advisory Council on Social Security to the Carter administration, raised the issue of "privatizing" Social Security:

"I would like to see reform take place in the entire context of income security for this country. We should look at all the myriad government programs dealing with income security. We should compare what we are doing through the government with what we are fostering in the private sector through private plans and individual savings."

Ross advocated a double-decker system in which the employee would make payments both to the government system for a minimum benefit and also to a private system for supplemental income. "We need to put tighter boundaries around the federal program so the individual is encouraged to exercise personal responsibility for financial management of his or her affairs," Ross wrote. In other words, hand the contributions over to the insurance companies and banks and reduce the government system to a minimum. Like the private pension system, this would give the private companies a pool of several hundred billion dollars. This is called stimulating personal savings.

'Junk Social Security'

This proposal was made more explicit by Peter Ferrara of the elite New York City corporate law firm Cravath, Swaine and Moore. In a study he wrote for the Cato Institute, a think tank for the Aquarian Age Libertarian Party, he proposed that all workers under 40 place their social security in private plans while workers between 40 and 65 would pay into both private and government funds. Since the government plan could not meet payments, it would then take money from general tax revenues. Ferrara does not say so, but under this kind of "reform" workers would be paying twice, once to the private plan and once again through federal taxes.

In responding to one of the typical confusion stories, this one appearing in a *Wall Street Journal* editorial, David Boaz of the Cato Institute praised the *Journal* for the confusion: "In your April 3 editorial about Social Security you correctly pointed out that more and more working people are beginning to chafe at the system's rising taxes and to realize that the system is in grave financial trouble. . . . The Social Security is near bankruptcy. Its own trustees warn that it will run out of money in 1982 or 1983."

The *Journal*, David Boaz, and other doomsayers are willfully mistaken. Even under the worst-case assumptions of high unemployment and high inflation, the fund comes only a few percent short of matching income with payments. For example, the Social Security trustees projected that in 1981, assuming an 8.3-percent unemployment rate and a 12.8-percent inflation rate, the Social Security fund will receive $140 billion and will pay out $145 billion, a deficit of $5 billion in a government budget of more than $600 billion—less than 1 percent of the federal budget. Even by 1985 the trustees, who assume 9.7-percent inflation and 8.0-per-

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cent unemployment rates in that year, project an income of $228 billion and a payment of $246 billion, which by that time will represent an even smaller percent of the federal budget.

The "bankruptcy" referred to by the panic mongers is that without a small additional funding the system's reserve will drop below the 12 or 13 percent margin, currently about $25 billion, required to maintain payment flow under the current bookkeeping system of the Social Security system.

The "confusion over what to do with Social Security" is intended to cover a "private-enterprise" grab of the cash flows associated with the current system. If there is anything wrong with Social Security, it is that the same people who want to grab the Social Security cash flows are currently ruining the American economy.

How the Friedmanites rigged Chile's system

The Chilean system for social security, which went into effect May 1, 1981, is very simple. As of that date, the government no longer extends old age and health benefits to new labor force entrants and allows present workers to "opt out" of their government coverage into private insurance programs run by Pension Administration Companies (AFPs) set up by banks and insurance companies. Of the 13 such companies set up to solicit pension insurance, half have minority control by foreign companies, including Insurance Company of North America, Aetna Life Insurance, and Lazard Brothers Co., Ltd. of London. These companies solicit workers through a massive advertising campaign that misleadingly promises they will actually receive higher income from the private plans.

If a worker choses a private insurance plan, he must pay his 17 percent pension and health tax to that company, which then invests the proceeds. The employee's former payments to the government system are given over to the private plan at the date the employee chooses to retire.

When the worker retires—and he is free to choose the year—he will then go to his private insurer and, using the accumulated savings in his accord, buy an annuity from the company. If the "market" accepts his bid for an annuity, he will receive it. If not he must either reduce his terms or continue working until he can get a better annuity or the "market" changes in his favor.

There are two immediate consequences of the new Chilean system. First, the government loses between $1.5 and $2 billion in revenue annually that is given over to insurance companies and banks. In the case of Chile that money will be used for speculation on raw materials and the government debt. Second, since about half of the work force, mostly younger workers, went into the private system, the government is left with the obligation of paying pensions and health benefits to the older workers who are retiring relatively soon. Without the income from the other half of the work force, the government will immediately face an enormous cash crisis, which will force it to sell treasury bills to the private insurance funds. As owners of a great deal of government debt, the private insurance funds will then force the government to curtail social expenses, including the promised social security payments. In Chile, whose eight-year-old military dictatorship run by General Pinochet has murdered thousands in a nation of 11 million, budget cutting does not occasion organized resistance.

A banker affiliated with Empresas BHC, Chile's second largest economic group, and a sponsor of the Administradora San Cristobal AFP, claimed, "This new system has a great advantage. Some unions like the copper workers used to lobby Congress for pension benefits. Now they can't do that because the system is private and now they will only get back in proportion to what they put in."

The banker was asked if he sees any application to the United States. "Definitely I do," he said, "you are now learning that government can't afford all the social welfare benefits that it has promised and you will have to turn to private enterprise. That is what our economy is all about. Of course even the idea for this new system came from the United States.

"For 10 years the Católica University in Santiago had an exchange program with the University of Chicago, with the Milton Friedman people. Many of us were trained by the Chicago people, like Sergio De Castro, the present finance minister, Miguel Kast, the former planning minister who is now the labor minister, and Piñera, the former labor minister. These people are referred to as the 'Chicago boys' and they were responsible for the economic reforms including social security.

"We had these plans formulated back in 1973, but we had to get the old [Allende] government out of the way in order to implement them."