trap the whole country in it: Set up a system where everybody has a stake in expanding the goodies, pretend that contributors get back what they pay in, but distort the tax and benefit schedules so that the poor get more.

As long as the amount of income redistribution in the system remained modest, no one particularly noticed or minded. The far Left actually deplored the Social Security program in the beginning precisely because its welfare feature was modest. What was the point of the program, said 1930s socialists, if it wasn't going to shift massive amounts of wealth from the rich to the poor? Seeing how hard it was going to be to sell a transfer program, New Deal leaders played down the redistribution theme. Edwin Witte, Roosevelt's leading expert on Social Security, explained the program's original thrust: "Only to a very minor degree does it modify the distribution of wealth, and it does not alter at all the fundamentals of our capitalistic and individualistic economy."

As the years passed, the Left reasserted itself, and the result has been a program sliding ever more clearly into the welfare mold. The soak-the-rich thrust is especially noticeable in the relentless rise in the proportion of wages subject to taxation. In 1950, tax was paid on only the first $3,000 of earnings; by 1996 this had soared to $62,700. Thus, a high income worker with a salary of $100,000 would have paid $60 in Social Security tax in 1950, but $10,675 in 1996. Over the same period, the benefit schedule was continually readjusted so that high contributors received a declining share of benefits relative to low contributors.

Other changes moved the system further toward a simple welfare giveaway. In 1966, Congress added some older beneficiaries to the program who had never paid any Social Security taxes. The adoption of the Earned Income Tax Credit (EITC) in 1975 was another critical step. This measure was originally justified as a way to refund the Social Security tax payments of low-income workers; it has now become a multi-billion dollar subsidy that writes checks to households for more than triple the amount of taxes they paid. For millions of low-income workers, the EITC turns Social Security into a (literally) something-for-nothing welfare benefit. Finally, the taxing of Social Security pensions, begun in 1983 and expanded in 1993, introduced a kind of means test into Social Security, and made it more clearly a welfare program.

The Penalties of Overpromise

The scheme to trap trusting middle-class taxpayers in a welfare program now appears to be backfiring, however. Presenting Social Security as a retirement insurance program encouraged workers to treat it as a retirement investment and calculate a "rate of return" for it. But burdened with welfare features and non-investment financing, Social Security gives a dismal payback for the typical worker. The arithmetic actually shows a *negative* yield on every dollar put in now. Younger workers compare this loss to the positive annual returns of six, eight, or ten percent they could expect from ordinary retirement investments, and conclude, not unreasonably, that politicians are selling them down the river on the single biggest deduction from their paychecks.

If Social Security had been set up as a frank welfare program, this opposition would not have arisen. No one would be criticizing it as a bad "investment," because they would not have expected anything from it. The solution to the developing crunch in Social Security finances clearly lies in this direction:

Social Security Imbalances Could Wreck the U.S. Economy

By William Modahl

What will happen if no changes are made in our Social Security program as we approach the retirement of the Baby Boomers? In May 1996, the Congressional Budget Office addressed that question. And for the first time in a major government report, the CBO considered how the economic feedbacks of rising Social Security and Medicare deficits would affect the national economy.

The outlook, even without economic feedbacks, is gloomy. Slowing growth in the labor force as Boomers retire causes economic growth to drop from 2.1 percent in 1995 to only 1.3 percent in 2030. The federal budget deficit climbs from our current level of 2 percent of gross domestic product (GDP) to 15 percent by 2030, a level never before seen.

Adding in economic feedbacks (that is, the effects of Social Security's deepening imbalance on the rest of the economy) makes the picture much worse. Government borrowing to cover Social Security deficits begins to crowd out private investment, causing interest rates to climb rapidly. Federal debt soars as the government issues ever more paper to pay interest charges. The economy goes into a downward spiral.

What would it take to avoid this doomsday scenario? To hold the ratio of debt to income steady at the federal level would require pushing taxes up from their current level of 20 percent of GDP to 29 by 2050. (Actually, because this does not count the negative economic effects of a 50 percent increase in federal taxes, an even greater hike would be needed). Alternatively, government spending would have to be cut in amounts that would exceed the total of *all* discretionary spending.

The CBO report makes clear for the first time that what's at stake in Social Security reform is not merely the health of our retirement program, but the future of the entire economy, and therefore our social fabric. It also shows that delaying action is not feasible.

Far from being unduly gloomy, the CBO report is probably too optimistic, since it is based on the Social Security Administration's mid-range assumptions—which have consistently been too positive over the years. Only a privatized system of personal retirement savings holds out hope of meeting the pension needs of future retirees without doing enormous damage to the U.S. economy.

William Modahl follows tax policy for Digital Equipment.

make it only a safety net program for the aged poor, and let everyone else take care of their own retirement by saving money currently withheld as Social Security tax in personal investment accounts instead.

Political economist James L. Payne is a Bradley Fellow at the Heritage Foundation. His books include Costly Returns: The Burdens of the U.S. Tax System, *and* The Culture of Spending: Why Congress Spends Beyond Our Means.

Entitlements Are Corroding Personal Responsibility

By Blake Hurst

"Is the house in her name?" One of the delights of living in a small town is eavesdropping. I overheard the preceding query while getting a tire patched, and what followed was a well-informed discussion of that whole field of legal legerdemain known as "elder law." The proprietor of the tire shop and a couple of customers were chatting about a neighbor entering the nursing home, and the ownership of the neighbor's property was crucial to playing one of America's favorite sports: gaming the entitlement system.

The program in question in this case was Medicaid. In 1995, some $32 billion was spent by the federal government and the states for long-term nursing-home care under Medicaid. States set income and asset levels that qualify a nursing home resident for Medicaid. In order to be eligible in my home state of Missouri, an applicant may possess a home and $1,000 or less in savings. Seventy percent of all of our nursing home patients receive Medicaid.

More than a few families make special efforts to tuck their inheritance away and get Mom or Dad qualified for Medicaid before the nursing home bills start coming in. In 1993, the Congressional Budget Office projected that nearly $2 billion would be lost between 1994 and 1998 due to illegal transfers of personal assets made in order to qualify for Medicaid-financed long-term care. Changes in the law in 1993 tried to institute a 36-month wait after the transfer of assets before Medicaid can be received. But it is questionable how effective this has been. In Missouri, the number of people receiving long-term care courtesy of Medicaid actually increased in the year after the eligibility requirements were stiffened. Only 115 of the over 30,000 Missourians applying for Medicaid-financed long-term care in fiscal 1995 were denied benefits because of recent asset transfers.

People are downright brazen about their Medicaid fiddles. Local bankers report that depositors regularly change names on bank accounts and certificates of deposit in order to hide assets from the Medicaid audit. With barely disguised disgust, a loan officer in a nearby town tells of a new house built by a local couple after appropriating the assets of a parent. Her life savings having disappeared, her children then qualified her for nursing home residence courtesy of Medicaid.

A small-town lawyer "often" has clients who want to hide assets from a nursing home and the state of Missouri. He tells them, and me, that present rules don't allow that. But he goes on to describe how a land-owner in his dotage can sell his farm to his children with a long-term mortgage, cancelable by the passing of the seller, which results in Medicaid-induced penury for the original land-owner.

Corrupted by Cash

These are not exotic measures carried out infrequently by con men. They are becoming part of the everyday landscape of old age and estate planning. When American heartlanders in casual conversation with the guy who fixes their tires are discussing ways of hiding assets, then most moral hesitation about taking advantage of Uncle Sam has been lost.

And the Medicaid hustles I've discussed here are only one example of uneconomic or unethical behavior fostered by entitlements. The earnings tests on Social Security likewise encourage oldsters to hide income. And there are softer but even more widespread ways in which Social Security invites undesirable behavior: It discourages people from saving as much as they know they ought to. It feeds today's rush to early retirement (only 15 percent of men over 64 now work, compared to 46 percent in 1950, despite the fact that the average person who reaches 65 now has 18 years of life left). The disability-protection portions of Social Security have been notoriously gamed and abused. And so forth.

The cavalier attitude toward taxpayer beneficence that entitlement programs encourage is quite familiar to farmers like me. After long experience with government agricultural subsidies I know that people quickly come to think of money made available to them by the government as a "right," and that recipients will use all means available to continue receiving any such payments. If the energy my fellow farmers and I spent squeezing the last dollar from farm programs had gone into increasing our efficiency in more productive ways, both we and the taxpayer would be better off today.

Government farm programs have been riddled with hustles like the "PIK-and-roll" and the "Mississippi Christmas Tree," in which various legal and accounting maneuvers are used to qualify for subsidies, circumvent limits on payments, and so forth. Any time government—acting in the name of compassion, without strict limits—hangs a big slab of bacon out in front of the public, human nature will invariably lead many people into the sorts of dodges and abuses that have long riddled welfare programs, and