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OFFICE OF MANAGEMENT AND BUDGET  
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**Remarks by OMB Director Joshua B. Bolten  
U.S. Chamber of Commerce  
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I want to thank Bruce for that introduction, and Tom for hosting this event today. The Chamber, and its members, have played an essential role in supporting the pro-growth policies and spending restraint that keep our economy healthy.

Thanks to the President's pro-growth policies – especially tax relief – our economy is expanding at a strong, sustainable pace. In the last few years, we have faced major challenges – recession, stock market declines, 9/11, corporate scandals, and the onset of war – and each time, our businesses, workers, and economy have responded.

Employment has grown steadily for 16 consecutive months. We've created 2.6 million new jobs. Industrial production is up. Business and consumer confidence are up. Homeownership is at record levels. Business investment is rising, and household wealth has risen \$8.5 trillion since the end of 2001.

This is good news for Americans – and good news for the Federal Budget. Rising economic growth has created rising tax receipts. After three straight years of declines, tax receipts increased by \$98 billion in 2004 – and we expect more growth in receipts in 2005.

These rising tax receipts, combined with spending restraint, are keeping us on the path of deficit reduction. Last year at this time, we forecast a 2004 deficit of 4.5 percent of GDP, or \$521 billion. Mostly because of stronger than expected tax receipts, the final deficit came in at 3.6 percent of GDP, or \$412 billion.

Because of the President's pro-growth economic policies and spending restraint, we're on a path to cut the deficit in half, to well below the 40-year historical average of 2.3 percent of GDP, by 2009.

So in the near-and-medium term, the Federal Budget is on a sound path. What concerns me more as the Budget Director is the long-term fiscal danger posed by mandatory spending programs.

Today, I want to focus on the largest program in the Budget, Social Security. I want to address three questions about the budget implications of Social Security and Social Security reform.

First: What is the long-term fiscal problem with Social Security?

Second: How does this long-term problem affect our fiscal health?

Third: What are the President's principles for fixing the problem, and why would they improve our situation?

#### 1. What is the problem?

The Social Security system operates on a “pay-as-you-go” basis, where the payroll taxes of current workers are used to pay for the benefits of current retirees. The system is 70 years old. It was designed at a time when most people didn't live long enough to receive benefits.

We had far more workers per retiree paying into the system than we do now. In 1950, this worker-to-beneficiary ratio was 16 to 1. Today, it is about 3 to 1. By the time today's young workers retire, it will be 2 to 1.

Until about three decades ago, the Social Security system was no different than most private employer pension systems. These “defined benefit” plans promised retirees and other beneficiaries a certain income level, no matter what. For a variety of reasons, including the growing financial literacy of America's workers, most companies have shifted to “defined contribution” plans like 401(k)s. Meanwhile, Social Security has stood still.

Even as our workforce has changed, our economy has changed, and our private retirement saving system has changed, Social Security has not changed – except in one significant way: It has grown far more expensive, both to workers, and to the Federal Government.

Over the program's lifetime, Social Security taxes have been raised more than 20 times. The government has increased Social Security payroll tax rates by more than six fold since 1949 – from two percent up to today's 12.4 percent. These tax increases have never fixed the fundamental problem with Social Security. In fact, all these tax increases did was to push the problem out to be solved another day. That day has arrived.

If we do nothing to fix Social Security, we will eventually need to raise Social Security payroll taxes on Americans by about 50 percent. Employers know that all Social Security taxes – even if they are split between the employee and the employer – come entirely from the employee in the form of lower wages. A 50 percent payroll tax increase would not only reduce jobs, but, like all big tax increases, would significantly slow economic growth.

In 2018, the Social Security system will begin to pay out more in benefits than it takes in in revenue – and the shortfalls will grow larger with each passing year. And, before today's 20-year-old worker reaches retirement age, the Social Security system will be bankrupt.

Some argue that we don't have to deal with the problem for a few more decades. They say we can patch the problem from year to year. But this notion simply delays the inevitable and forces even harder choices onto our children and grandchildren. Our goal is to fix this problem permanently. And to do that, we need to understand the program's structural problem.

The picture is not pretty. The Social Security Trustees have estimated that the current system owes more than \$10 trillion more than it can afford to pay.

## 2. How does this long-term problem affect our fiscal health?

Carrying an unfunded obligation of more than \$10 trillion is hard enough. According to the Social Security trustees, the cost of delay will add an additional \$600 billion this year to the unfunded obligations, and more in each successive year of inaction. This figure is easy enough to understand. If you owe a debt, and you pay no interest on the debt for a year, the amount you owe grows by the interest you failed to pay.

Such chronic and growing obligations in the Social Security program are properly understood by the American public – including investors – as a sign that the program is out of balance and headed for bankruptcy.

Allowing this condition to persist could have major effects on our economy. A lack of confidence in the Federal Government's resolve in reforming Social Security could undermine confidence in our fiscal policy and the American economy, leading to less business investment in the U.S. and slower overall economic growth.

The fact is the Social Security system is in trouble. If its problems are left unresolved, today's young workers will see their benefits slashed, or see massive tax increases that would threaten the economy.

Delay and inaction are not an option. We must fix Social Security permanently. The sooner we take action, the less costly and less difficult our actions will have to be.

The President's critics call this "hyping" the problem. But in 1998, a prominent Democrat spoke about the need to address the Social Security problem. He spoke not far from here, at Georgetown University, and here is what he said:

"This fiscal crisis in Social Security affects every generation. We now know that the Social Security trust fund is fine for another few decades. But if it gets in trouble and we don't deal with it, then it not only affects the generation of the baby boomers and whether they'll have enough to live on when they retire, it raises the question of whether they will have enough to live on by unfairly burdening their children and, therefore, unfairly burdening their children's ability to raise their grandchildren."

That Democrat was President Clinton, and he was right. He was not hyping the problem. The fiscal crisis in Social Security affects every generation. We may disagree about the solutions, but at least we agree on the problem. And so if we are to be serious about the issue, let's treat the facts seriously. It is a serious problem. This is a crisis.

Real Social Security reform requires us to recognize the problem and move beyond quick fixes and short term schemes. Social Security's problems do not lie out in the distant future and solutions cannot responsibly be postponed.

3. What are the President's principles for fixing the problem, and how would these reforms help the fiscal situation?

The President wants to fix Social Security permanently, erasing that more than \$10 trillion debt now facing our children and grandchildren. And, he has outlined several broad principles to guide reform efforts.

First, nothing will change for those who are receiving Social Security now and for those who are near retirement. In short, this is a debate about how we save Social Security for today's younger workers, their children, and their grandchildren.

Second, we must not increase payroll taxes, because taxes are already high enough on America's workers, and higher taxes would slow job growth, and our entire economy. And third, we should give younger workers the option to save some of their payroll taxes in a personal account, a nest egg they own and control and can pass on to their children, which the government cannot take away. Let me emphasize here, this would be an option, it would be voluntary. Workers who prefer to continue with the current system should and will be allowed to do so.

Setting up personal accounts as part of a reform package is needed to modernize the system. Workers should have the option of investing more of their own retirement money and earning a reasonable rate of return, rather than the less than 2 percent real return they can expect with the current system.

And so what would it take to introduce personal accounts? Setting up these accounts is likely to require transition financing. I said "transition financing", and not "transition costs", because we are financing the transition to a stronger pension system. We are not creating new costs. By allowing people to keep some of their payroll taxes in personal accounts, we would be pre-funding benefits that would otherwise have to be paid in the future – from the payroll taxes of workers not yet born.

Some opponents of fixing the system have suggested that transition financing would hurt our economy. They're wrong. It is true that the Treasury would have to borrow funds to pay for current retirees as young worker payroll taxes stay in their own accounts. But because of the new saving that would occur in these new accounts, the economy would see no net loss in saving.

In fact, it is likely that these reforms would help the overall economy. In 2001, the President appointed a Social Security Commission to study the issue. According to the Congressional Budget Office, one of the reform models presented by the commission would lead to a three to four percent increase in cumulative GDP, and a 10 to 12 percent increase in national wealth by 2080.

Perhaps even more notably, the Congressional Budget Office found that under this plan, economic growth would have accelerated somewhat by 2025 – well within the so-called “transition period” for funding personal accounts. So even during the transition period when personal accounts would be established, economic growth would be better than it otherwise would be.

Some opponents of personal accounts also say they are too expensive. Smart reforms of Social Security should be considered against the cost of doing nothing, which is more than \$10 trillion. Putting off saving Social Security increases the size of the problem by \$600 billion a year and counting – and puts us on a path where a long-term fiscal imbalance will soon begin to cause serious budget and economic problems. Inaction would produce the greatest and most difficult costs and the longer we wait, the greater the burden we pass on to future generations.

As Budget Director, I have a special interest in making sure we understand what things cost. And in the debate over Social Security reform, the cost of inaction is clear: more than \$10 trillion and counting.

Some of these same opponents assert personal accounts are too risky. There is a concern that people would use their personal accounts at the horse track, or on lottery tickets. Any plan with personal accounts would have guidelines that would set basic standards of safety and soundness when it comes to investment choices. And when it comes to risk, there is no riskier investment than paying into a system we know will go bankrupt unless it is fixed.

The President is committed to solving the problem permanently; assuring today’s young workers and all investors that America’s fiscal challenges will be met with reform. And solving the Social Security challenge with a comprehensive solution involving voluntary personal accounts would have other positive economic effects. It would promote private savings in America, helping to build a culture of saving and a society of ownership. And it would give younger workers the opportunity to receive a greater rate of return on a portion of their payroll taxes than Social Security has historically paid.

The President was clear about the need to reform this program during his campaign. Fixing Social Security will require bipartisan cooperation and the courage of leaders in both parties. And, we will need the support of the business community and entrepreneurs who are concerned about the retirement of their employees.

Social Security continues to give seniors the dignity, security, and peace of mind that Franklin Roosevelt promised. Our job is to keep the promise of Social Security for our own children and grandchildren.

Thank you very much.