

## **SOCIAL SECURITY REFORM: ISSUES FOR HISPANIC AMERICANS**

SUBMITTED TO:

U.S. HOUSE OF REPRESENTATIVES  
COMMITTEE ON WAYS AND MEANS,  
SUBCOMMITTEE ON SOCIAL SECURITY

Presented by:  
Eric Rodríguez  
Senior Policy Analyst  
on behalf of:

Sonia M. Pérez  
Deputy Vice President  
Office of Research, Advocacy, and Legislation

NATIONAL COUNCIL OF LA RAZA

1111 19th Street, N.W.  
Suite 1000  
Washington, D.C. 20036  
(202) 785-1670

Raúl Yzaguirre  
President

February 10, 1999

## **I. INTRODUCTION**

My name is Eric Rodríguez, and I am a Senior Policy Analyst for the Office of Research, Advocacy, and Legislation, at the National Council of La Raza (NCLR).

NCLR, the largest constituency-based national Hispanic organization, exists to improve life opportunities for the more than 30 million Americans of Hispanic descent. NCLR acts as an umbrella for almost 230 affiliated Hispanic community-based organizations which together serve 37 states, Puerto Rico, and the District of Columbia, and reach more than three million Hispanics annually through a range of services. NCLR appreciates the opportunity to provide for the record this statement of Latino perspective on Social Security reform.

Given that Hispanics are a growing segment of the total U.S. population and an increasing proportion of the total U.S. elderly and working-age populations, they are likely to play a pivotal role in the nation's economic future. For example, in 1990, Hispanics constituted 8% of the total U.S. workforce, compared to 78% for Whites and 10% for Blacks. However, by 2010, 2020, and 2030, Latinos are projected to account for 13.2%, 15.2%, and 17.2%, respectively, of all U.S. workers. Moreover, between 1997 and 2007, the Hispanic elderly population is predicted to increase 50.2%, and from 1997 to 2020 the number of Hispanics 65 years of age and over is projected nearly to double (an increase of 185.1%).

Notwithstanding this, Latinos have not been fully included in policy discussions related to Social Security, pension coverage, and retirement savings – a dialogue that has sharply intensified over the last two years. Without complete information on, and consideration of, Hispanics and Social Security, the likelihood of policymakers' achieving a credible and effective long-term Social Security solution is seriously impaired. For this reason the following statement presents socio-demographic trend data that underscore the importance of the Social Security system for Hispanic retirees and highlight the critical role that Hispanics will play in preserving the nation's pension system. In addition, this statement outlines key public policy areas with regard to Social Security reform and Latinos, and examines specific Social Security reform initiatives, providing a much-needed Hispanic perspective on the relevant reform issues. Finally, the statement offers recommendations on the Social Security reform strategies that are the most promising, and least harmful, for Latinos.

As a point of clarification, the terms "Hispanic" and "Latino" are used interchangeably throughout this statement. In addition, all data presented below are for the Hispanic population in the 50 states, and do not reflect the status of Puerto Rico Island residents.

## **II. THE SOCIAL SECURITY SYSTEM AND HISPANICS**

NCLR agrees that it is wise and prudent for the federal government to bring the Social Security system into long-term fiscal balance. In the absence of reform in the near term, the sheer size of the projected short-fall would likely impose severe economic strains on the federal budget and overall U.S. economy. Such economic pressure would undoubtedly translate into serious financial hardships for most Americans, and would have dire consequences for low-income workers – many of whom are Latino – typically more susceptible to economic downturns than higher wage earners. However, NCLR does not believe that the current system has major structural flaws or is programmatically outdated. Rather, NCLR understands that lawmakers should consider options to improve the system's effectiveness in providing a source of income for retirees and their survivors.

The Social Security system – which provides retired workers age 65 or older with a livable income – is designed, in part, to help alleviate poverty among elderly Americans and meet the retirement needs of workers (especially those who do not have access to, or are unable to participate in, employee pension plans). The program disproportionately benefits Latinos primarily because the overall socioeconomic picture of the Latino community closely resembles that of the nation in 1935 when the program was enacted. Today's Hispanic workers are

concentrated in low-wage jobs typically lacking in pension coverage, experience high poverty and relatively high unemployment, and have less ability to save and invest for retirement than most other Americans. As a result, in 1996, the median income for Hispanics 65 and over was \$8,036, compared to \$12,921 for Whites and \$8,656 for Blacks. Furthermore, that same year, 24.4% of Hispanics 65 and over lived below the poverty level, compared to 9.4% of comparable Whites and 25.3% of comparable Blacks.

Given this profile, Latinos fare better than most other Americans in the Social Security system for several reasons. First, Social Security's benefit formula is progressive, therefore, it ensures that low-wage workers receive a greater share of the resources that they contributed to the system. Second, benefits are based on the length of time worked, as well as on the level of reported wages and salaries earned, during a worker's lifetime. The progressive formula means that while low-wage retired workers receive a smaller amount in Social Security benefits than high-wage retired workers, the system compensates the burdensome nature of the payroll tax by replacing a greater share of a low-wage worker's lifetime earnings. According to the Social Security Administration, the proportion of annual earnings replaced by the system is about 60% for a low-wage earner, 42% for an average-wage earner, and 25% for a high-wage earner. Consequently, since Hispanics have relatively low earnings levels, they are more likely to put a smaller amount in, but receive a greater share of income from, Social Security than either Whites or Blacks. In addition, because Latinos tend to have longer life expectancy rates than other Americans, they are especially likely to receive benefits for a longer period of time, which helps them recover the proportion of income they contributed to the system. In short, the labor force and demographic picture of Hispanic workers and retirees actually results in a higher rate of return on investments for Latinos in the Social Security system.

Nevertheless, because benefit levels are low, the Social Security system has not met its goal of reducing poverty among elderly Latino and Black retirees. To illustrate, the Hispanic elderly population is more likely than Whites, but less likely than Blacks, to be poor; in 1996, about one-quarter of Hispanic (24.4%) and Black (25.3%) persons aged 65 years and over were poor, compared to fewer than one-tenth (9.4%) of their White peers.

### **III. SOCIAL SECURITY REFORM AND LATINOS**

In 2013, soon after the number of retirees starts increasing by more than one million per year, it is projected that Social Security will begin to pay out more in benefits than it collects in payroll tax revenues. In the absence of reform, the federal government will need to borrow from the Social Security trust fund (accumulated reserves) in order to continue to pay necessary benefits. It is projected that in 2032, shortly after the youngest of the baby boomers is of retirement age, the trust fund will be depleted and revenues will support only 75% of guaranteed benefits. Based on these projections, policy intervention is necessary to ensure that neither American workers nor the economy are adversely affected.

Lawmakers have examined and proposed policy options that bring the system into long-term balance and which, in some cases, are designed to improve the financial outcomes for retirees. While some reformers have closely examined the impact of plans and proposals on low-wage workers – lending due consideration to the social insurance mission of the Social Security system – few have examined the impact of reform specifically on Latinos. Instead, policymakers, both progressive and otherwise, have tended to lump Hispanic concerns into the all-encompassing "low-wage/minority issues" category. Yet, Hispanics are, and will continue to be, a significant segment of the American work force, whose productivity, savings, and investments help to ensure the continued economic prosperity of the nation. In this sense, Hispanics are not simply part of the low-wage workforce, but an exponentially growing segment of America that currently experiences serious economic challenges. Therefore, any long-term Social Security "fix" that purports to help the majority of Americans but harms Latinos disproportionately will not be beneficial to the nation over the long run. Moreover, any long-term Social Security

solution that does not address, in some manner, the economic and employment challenges that Latinos currently face will not be fully successful.

Accordingly, NCLR has outlined below several essential considerations, from a Latino perspective, that should be central to Social Security reform:

® Financial Security. Social Security invests a worker's payroll taxes in government securities. There is virtually no risk associated with these investments. Under the current system, benefits are guaranteed to be paid upon retirement and the amount is tied closely to wages earned over a worker's life. Several reform options inject a measure of risk by proposing to invest part of an individual worker's contribution into the stock market in the hope of generating greater returns on their investments. Under such models, benefit levels are not guaranteed and the value of one's retirement package is at considerably greater risk than with the current Social Security system. Because Latinos tend to be the least likely of all Americans to receive private pension coverage, the guarantee of a benefit upon retirement is critically important. In 1996, Hispanics 65 years of age and over received only 13.5% of their income from pensions, compared to 18.3% for Whites and 18.1% for Blacks. Moreover, according to Department of Labor (DOL) employee pension coverage data, while there were about 12.3 million Hispanic Americans in the workplace in 1997, only about one-third (32%) participated in employee pension plans, compared to more than two-fifths (44%) of other minorities and one-half (51%) of Whites. In fact, DOL reported that between 1979 and 1993 the rate of pension participation for Hispanics declined five percentage points, compared to a one percentage point increase for Whites. Therefore, a guaranteed and defined benefit is an essential component of any reform plan that considers the interests of Hispanic workers.

® Retirement Income and Rate of Return. Many reformists have focused on Social Security's rate of return as a key issue. As previously mentioned, NCLR believes Latinos – due to their low wages and high life expectancy, coupled with the Social Security system's progressive benefits formula and guarantee of life-long benefits (with cost of living adjustments) – receive a higher rate of return on Social Security benefits than other Americans. Moreover, because the benefit formula is tied to earnings during working years, Hispanics maintain high-income replacement rates; thus, a Latino retiree is likely to receive a substantial proportion of the earnings s/he made the year prior to retirement. Such an approach helps to maintain a worker/retiree's standard of living. However, it is precisely because the formula is based on wages over a lifetime that Social Security does not effectively prevent poor workers from becoming poor retirees. But disproportionate poverty among retirees who earned low wages as workers is not necessarily a result of Social Security's rate of return on payroll taxes. Rather, high poverty among elderly Hispanic Americans is due more to the fact that Hispanic and other low-wage workers lack access to private pensions and have little opportunity to save and invest for their retirement; two important sources of supplemental retirement income. As a result, Latinos tend to rely heavily on Social Security as the sole source of retirement income. Efforts to improve access to private pensions and increase personal savings and investment by low-wage workers, including many Hispanics, should be distinct from, but closely parallel, Social Security reform efforts.

® Equity. Overall, the current system is very progressive because low-earners – and Hispanics in particular – fare better than high-earners in terms of rate of return on investments and income-replacement rates. Yet several reform proposals, most notably "privatization" or "private individual saving account" plans, include provisions that would alter the progressive nature of the current system. These plans would create an exponentially more favorable structure for high-earners than low-earners by providing substantially higher returns for high-earners (largely because the benefit level of a defined contribution plan is principally dependent on the amount of contributions made over a lifetime). This transformation may have serious implications for the distribution of wealth in the nation. No policy option under consideration should seek to re-distribute benefits unevenly, widen the wealth gap between upper and lower-income Americans, or increase elderly poverty.

® Hispanic Women. While Social Security reform has serious implications for the overall Hispanic community, Hispanic women may be the most severely affected by reform efforts. Hispanic women are more likely than other women to work inside the home and are less likely than other women to have saved for retirement. Moreover, Hispanic women are less likely than other workers to have access to private pension coverage, they tend to rely heavily on Social Security benefits, and they tend to receive the lowest wages of any group of workers. As a result, changes in marital status or loss of a family member who is a principal wage-earner places Latinas in a particularly vulnerable economic position. In 1997, more than one-quarter of Hispanic women 65 years of age and older lived below poverty -- while in households with a female householder over 65 years of age and no husband present, the poverty rate was 50%. Consequently, reform plans that threaten the economic status of retirees by making direct changes to the structure of the Social Security system -- and also the survivors benefits system -- will have a disproportionately harmful affect on Hispanic women.

Finally, for Hispanics overall, there is one additional issue related to Social Security reform that policymakers must consider. Specifically, it is generally accepted that raising worker productivity -- thereby increasing payroll tax contributions -- would go a long way toward reducing the projected long-term Social Security imbalance. Because Hispanics will play a crucial role in supporting and promoting the nation's overall economic growth, Social Security reformers should seek to increase the productivity of current and future Latino workers. The data reveal that about three in five (59.9%) Hispanics between the ages of 18 and 34 had graduated from high school in 1996, compared to four in five Whites (83.6%) and Blacks (79.0%). Similarly, while 9.3% of Latinos had graduated from college in 1996, by contrast, 24.3% of Whites and 13.6% of Blacks had completed college that year. Given the direct link between educational attainment and income, earnings, wages, and disposable income for savings, increasing the educational attainment of Hispanic workers will directly enhance the solvency of the Social Security system.

#### **IV. SPECIFIC SOCIAL SECURITY REFORM OPTIONS: IMPLICATIONS FOR HISPANICS**

Experts suggest, there are only three legitimate ways to reform the Social Security program and bring it into long-term actuarial balance: increase revenues (i.e., payroll taxes, etc.), cut benefits, or utilize federal budgetary surpluses to strengthen the Social Security Trust Fund. Keeping in mind the aforementioned concerns for Hispanics, NCLR examined three broad policy options that are likely to be included in a final package of Social Security reform initiatives. In addition, we reviewed an alternative reform proposal to restructure the Social Security system to increase rates of return on worker investments.

##### **Payroll Tax Increases**

Perhaps the most rudimentary Social Security reform policy option, a payroll tax increase, is politically unpalatable to most lawmakers. Nevertheless, because of its simplicity, a modest payroll tax increase may be included in any serious Social Security reform package. As detailed in a 1997 NCLR report, *Burden or Relief? The Impact of Tax Policy on Hispanic Working Families*, federal payroll taxes already extract a disproportionately large share of income from Latino families because they are levied at a flat rate. For example, in 1995, Hispanic families in the lowest income bracket (quintile) had their incomes reduced by 6.6% by the payroll tax. NCLR is inclined to oppose payroll tax increases. We believe that without a corresponding payroll tax relief package for low-wage workers, a significant tax increase would seriously and unfairly diminish the economic status of Latino workers and low-income families.

## **Benefit Cuts**

There are a host of proposals and strategies to reduce the amount of benefits Social Security pays out to retirees. These include increasing the retirement age, modifying the cost of living adjustment, and altering the benefit formula. Because Latinos disproportionately rely on Social Security as the sole source of retirement income, and often receive lower benefits than other Americans, reductions in benefits would have serious negative implications for Latino retirees. NCLR is inclined to oppose benefit cuts. If any such cuts occur, reformers must strike the right balance between fairly distributing the impact and burden of reform efforts, and harming vulnerable retirees. We expect that policymakers will apply any benefit cut initiatives progressively, to avoid imposing disproportionate economic harm on poor elderly retirees.

## **Unified Federal Budget Surplus**

The Clinton Administration has proposed, and several Congressional leaders have agreed, to carve-out 62% of the unified federal budget surplus to fortify the Social Security Trust Fund. The Administration's plan would use projected budget surpluses to pay down the national debt. Most experts agree that reducing public debt enhances the prospects of sustaining long-term economic growth. While the proposal does not bring the Social Security system into 75-year fiscal balance, it moves close to long-term balance without imposing deep benefit cuts or steep payroll tax increases. In addition, the proposal does not significantly modify the structure of the Social Security program; a move that could have far-reaching negative effects on workers and retirees. NCLR believes that reserving a significant portion of the budget surplus to build up the Social Security Trust Fund, and using resources to pay down the national debt, is a sound and prudent plan that should be supported by Congress.

## **Mandatory Private Individual Accounts**

There are a host of proposals that create mandatory private individual accounts that would be de-facto retirement savings accounts that could be invested in common stocks and bonds. Proponents of these plans suggest that such accounts would increase the rate of return on investments for retirees, increase national savings, and boost U.S. economic growth. However, there are several factors that suggest that such an option may not proportionately benefit Hispanic workers; specifically:

® Investment Expertise. While it is unclear what investment choices Hispanics will make (which determine their final benefit amount and rate of return), research shows that Hispanics have limited experience with, and exposure to, private investments and financial institutions in general. For instance, data from the Employee Benefits Research Institute's 1998 Retirement Confidence Survey show that only one in five Hispanics has tried to figure out how much they will need to save for retirement. A similar proportion indicated that they are not comfortable dealing with banks, insurance companies, or mutual funds. Given this, it is likely that under such a system Latinos would seek investments in the most risk-averse portfolios – which also happen to maintain the smallest long-term yields.

® Administrative Costs. These accounts would be subject to administrative costs that would further erode the rate of return; and most analysts agree that such costs are reasonably higher in private market investments than under the current system. These costs would have a disproportionately greater adverse effect on the relatively smaller account that Hispanics, due to their relatively lower contributions, would have.

® Economic Status. There are several issues that will affect the ability of Latinos to save and invest in such accounts. As a group, Hispanic workers have variable work histories, due to high levels of unemployment, displacement from jobs, and work in unstable industries. Mandatory private accounts require consistent, stable employment to ensure steady contributions; for Hispanics, such changes over a lifetime would vary and ultimately hinder long-term returns. In addition, Hispanic workers are less likely to have health insurance than any other

group of Americans, which means that at least one in three Latinos has to use a significant amount of earnings for out-of-pocket health care costs. Similarly, almost one in five Latinos spends almost half of his/her income on housing. The lack of health insurance, coupled with high housing costs, seriously diminishes disposable income available to Hispanics for saving and investing.

Furthermore, any major structural change in the Social Security program would impose serious economic burdens on current workers. The transformation of a system from one that uses current contributions to pay the benefits of current retirees to one that builds accounts for current workers would have to be financed. In addition, private individual accounts are likely to alter significantly the progressive nature of the system; specifically, high-wage earners will fare much better than low-wage earners in a defined-contribution system, which would exacerbate the wealth gap, with nation-wide social and political implications. As a result, NCLR is inclined to oppose the creation of mandatory private individual accounts within the Social Security system.

## **V. SOCIAL SECURITY REFORM RECOMMENDATIONS**

Overall, given that the final Social Security reform package may contain measures that directly reduce benefits exiting the system and increase revenues entering the system, NCLR will support the most progressive means of bringing the system into long-term fiscal balance. Of utmost importance to Latinos is maintaining the social insurance nature of the current system. Therefore, the best Social Security reform package for Latinos would retain the equity and progressivity of the current system and maintain a guaranteed benefit upon retirement.

Nevertheless, NCLR supports the goals of the majority of Social Security reform proposals that attempt to improve the economic status of elderly retirees and increase the retirement savings rate of Americans. However, we are not convinced that a dramatic change in the Social Security program is the only, much less the most appropriate, course to achieve these goals; on balance, we believe this would do more harm than good. From NCLR's perspective, the most successful Social Security reform plan should include separate proposals that: reduce poverty levels among Hispanic elderly retirees, increase the retirement savings rate of Hispanic and other low-income Americans, and increase the productivity of Latino workers. Such steps are critical not just to ensure a decent source of income for Hispanic retirees, but also to help sustain the economic growth of the nation as a whole.

Bearing this in mind, we applaud President Clinton's proposal to use a large portion of projected federal budget surpluses to preserve Social Security while investing a modest portion in programs designed to promote the future productivity of the workforce. We believe it is an important first step, and should go a long way toward moderating the potentially harmful economic effects of bringing the Social Security system into long-term fiscal balance. In addition, while we have some questions regarding the details of his plan, we support the general thrust of President Clinton's proposal to create Universal Savings Accounts to increase the personal savings among all Americans.

As the nation's demographics change, the Latino population will be an increasingly significant driving force behind America's social, economic, and public policy agendas. With this in mind, NCLR appreciates the opportunity to submit this statement, and strongly encourages Congress to consider and include the perspectives and concerns of the 30 million Hispanic Americans in the unfolding national debate on retirement issues. We also welcome you to call on NCLR to provide additional information about the economic well-being of Latino workers and future retirees. Thank you.