Insecurity, Austerity, and the American Social Contract

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On August 14, 1935, Franklin Roosevelt signed into law the Social Security Act, the cornerstone of America's distinctive framework of social protection. Seated at a table in the White House's Cabinet Room, he was flanked by Labor Secretary Frances Perkins, the first woman appointed to a presidential cabinet, and Representative David Lewis, a former coal miner and self-taught lawyer who championed the legislation. Standing nearby was Representative John Dingell of Michigan—the child of polish immigrants (his original last name was Dzieglewicz) who introduced the first bill for national health insurance in Congress in 1933. Their presence was fitting, for as Roosevelt declared that day, the law was designed to provide ordinary workers and their families—women as well as men, children as well as adults, coal miners and sons of immigrants alike—with "some measure of protection" against the "hazards and vicissitudes of life." [1]

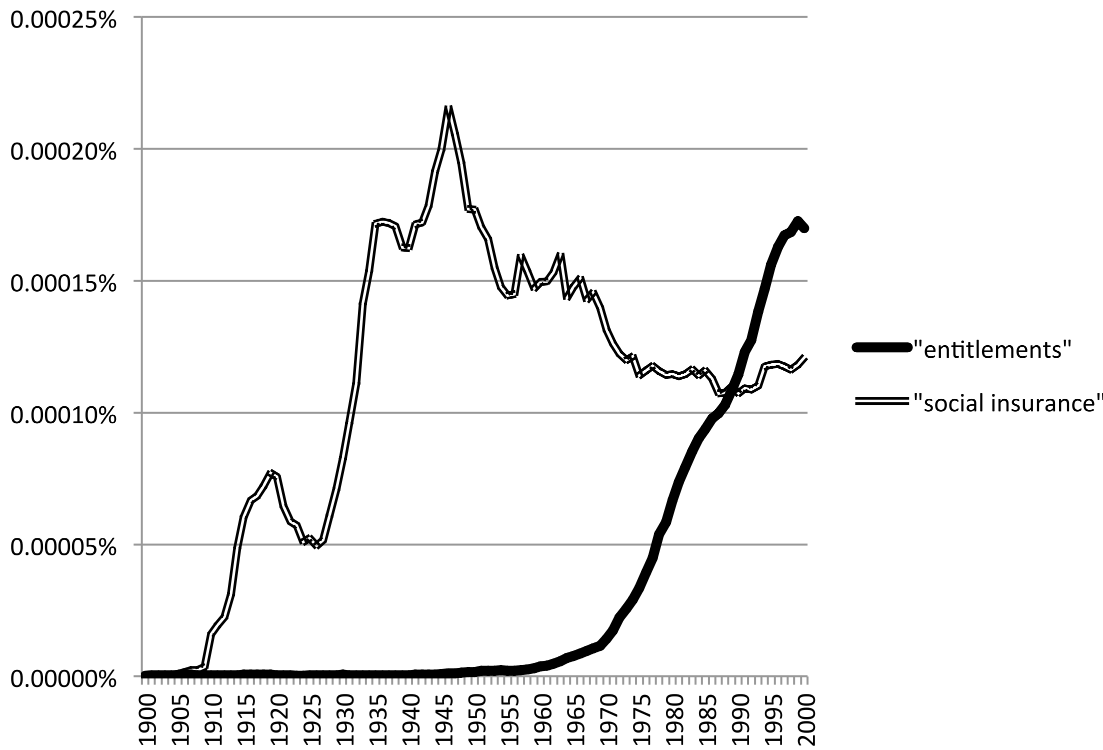
But Roosevelt did not just celebrate the law's safeguarding of "human needs"; in addition, he emphasized that the Act was part of an evolving "structure intended to lessen the force of possible future depressions" and to limit the need for the government to go "deeply into debt to furnish relief to the needy." Henceforth, Roosevelt proclaimed, the law would "provide for the United States an economic structure of vastly greater soundness."

Roosevelt's insistence that public insurance was good not just for those experiencing dislocations but also for the economy as a whole sounds jarring today. The dominant view is that Social Security, Medicare, and other similar programs are inefficient and unaffordable. Defenses of these programs stress their protection of "human needs" rather than their role in supporting a strong economy. Meanwhile, the many and vocal attacks on these programs emphasize their mounting costs, their supposed uncontrollability, and their alleged perverse incentives.

The leading economic spokesperson of the Republican Party, Representative Paul Ryan, suggests that we are transforming "the safety net into a hammock that lulls able-bodied people to lives of dependence and complacency, that drains them of their will and their incentive to make the most of their lives." Spending on this hammock threatens a "debt crisis," Ryan warns, in which "our finances will collapse, our economy will stall." The United States, he insists, must "change course"—and that change should take the form of dramatically cutting back the mandatory programs that D.C. insiders pejoratively refer to as "entitlements."[2]

To get a sense of the change in discourse, glance at Figure 1, which shows the number of references to "entitlements" and "social insurance" in the tens of millions of English-language books scanned by Google. "Social insurance" was once a common term, used to describe programs and policies that provide broad risk protection that is more generous for lower-income and higher-risk groups. In the wake of the Social Security Act, the phrase rose dramatically in prominence. Starting in the 1970s and accelerating in subsequent decades, however, "entitlements" has risen to surpass "social insurance" in English-language books. The notion that many public programs are a form of insurance that is potentially beneficial to the economy has been eclipsed by the idea that these are runaway obligations that threaten our economic future.

Figure 1: “Entitlements” vs. “Social Insurance” in English-Language Books



Source: Google Ngram Viewer, http://books.google.com/ngrams. Results represent a three-year moving average of occurrence of “entitlements” and “social insurance” in English-language books digitized by Google as a percentage of all one-word and two-word phrases, respectively.

In this chapter, I show that this view has it almost exactly backward. Economic insecurity remains a pressing problem that only effective government policies can address. What’s more, our society can afford to upgrade these policies. Indeed, we cannot afford to *not* upgrade these policies. Like the Great Depression, the financial crisis that began in 2007 has taught us important lessons about the limits of private responses to widespread economic risks. It is these private responses, such as workplace health insurance, that are inefficient and unsustainable. As they decline, more and more risk is shifting onto workers and their families—in ways that likely hurt the economy overall. Far from a comfortable hammock, America’s framework of social protection is becoming more threadbare and less complete.

This transformation is an opportunity as well as a threat. Because the United States relies more on inefficient and eroding private responses than any other rich nation, there is ample room for us to expand social protection while actually saving our society money and improving our economy. The greatest opportunity lies in health care, where we spend vastly more than other affluent nations for less coverage and poorer outcomes. But there is also an enormous amount of “money on the table” in the complex web of subsidies that encourage private employment-based benefits and retirement savings—subsidies that cannot and will not prevent the continuing shift of risk and whose benefits accrue mostly to the least vulnerable workers.

In short, critics are correct that the American social contract needs to be harmonized with a twenty-first-century economy and society. But contrary to their arguments, this means upgrading public social protections so they cover the most significant risks and the most vulnerable Americans. We can increase security for workers and their families even as we make American social protection more efficient and its costs more controllable. The challenges we face are at least as much political as economic, which is why those seeking reform should be thinking at least as much about political realities as about policy alternatives.

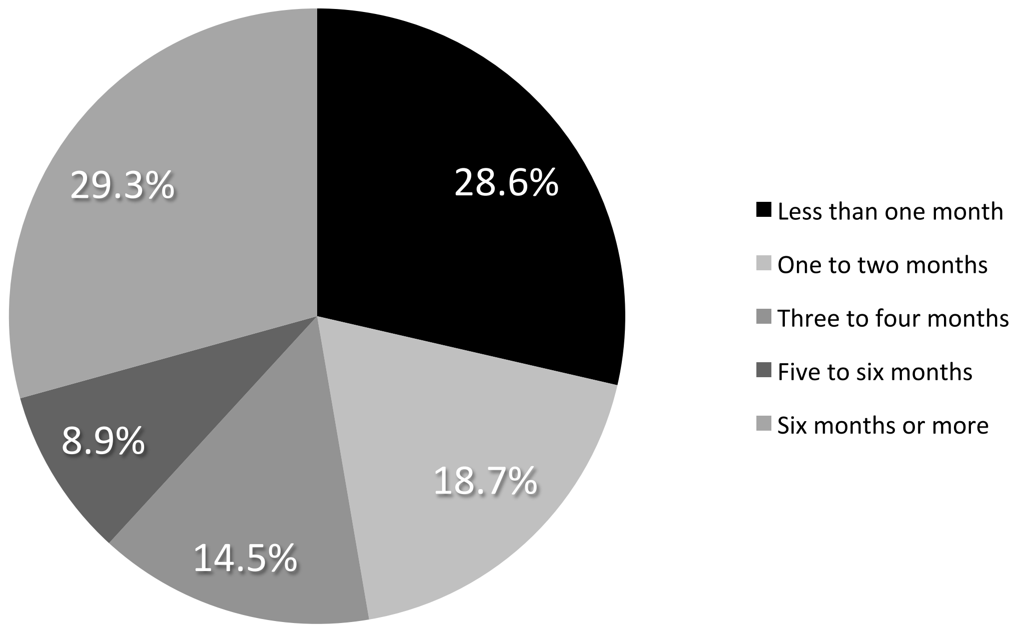
The Insecurity Constellation

The financial crisis that began in 2007 has provided a harsh reminder that economic insecurity is still very much a part of American life. In the 18 months between March 2008 and September 2009—according to a survey that I designed with two fellow researchers—roughly half of Americans experienced at least one major employment dislocation within their family (involuntary unemployment or loss of more than a month of work due to sickness or injury) and more than half experienced at least one major health dislocation (major out-of-pocket expenses, much higher insurance costs, or loss of insurance altogether).[3] At the same time, Americans were, and continue to be, strikingly ill-prepared for major economic risks. Asked how long they could go without their current income before hardship set in, more than 70 percent said less than six months, and nearly half said less than two months (see Figure 2).

These pessimistic expectations are borne out by our evidence. Households that experienced major economic risks between March 2008 and September 2009 reported much higher levels of unmet basic needs: going without food because of the cost, losing one's house or rental, or going without health care because of the expense. Even among families in the third quartile of household income (annual income between $60,000 and $100,000), more than half of families who experienced employment or medical disruptions reported being unable to meet at least one basic economic need.[4]

Though the recent downturn cast insecurity in stark relief, these dislocations represent the culmination of a long-term trend rather than a sudden departure from stable conditions. Over the last generation, there has been a gradual but steady increase in the share of Americans experiencing large economic losses, such as big drops in income or major spikes in out-of-pocket medical costs.[5] The cumulative risk of such losses over a working life is very high. According to a recent examination using data from 1968 to the present, more than two-thirds Americans will experience involuntary job loss by the age of 60, and more than half will spend at least one year in poverty. And these risks have risen: Between 1968 and 1988, roughly 12 percent of 45-55 year old experienced at a least a year in poverty. Between 1988 and 2008 (two decades that overwhelmingly predate the recent downturn), the chance was almost 18 percent.[6]

Figure 2: How Long Can Households Go Without Income Before Hardship Sets In?

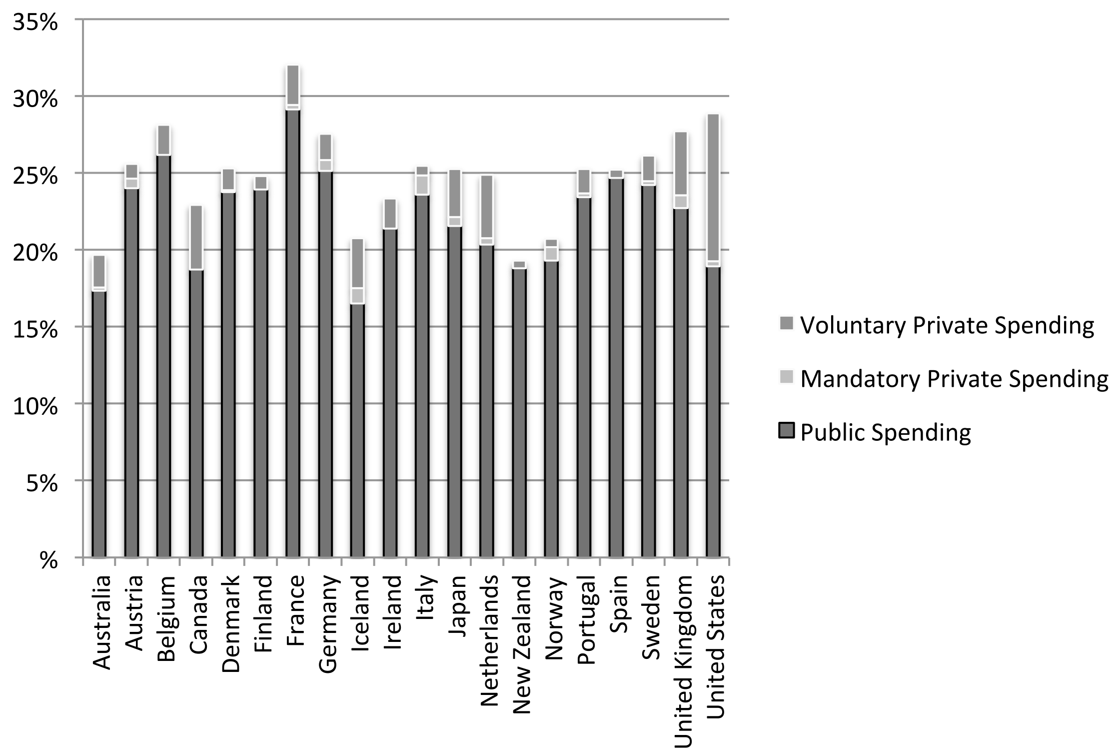


Source: Survey of Economic Risk Perceptions and Insecurity (SERPI). The SERPI was incorporated as a part of the 2008-2009 Panel Survey of the American National Election Studies (ANES), an online survey of a nationally representative sample of Americans who agreed to be interviewed monthly between January 2008 and October 2009. With financial support from the Rockefeller Foundation, the SERPI was fielded as the sole questions for the ANES panel in March (Wave 15) and September (Wave 21) of 2009; 2,084 respondents completed both waves of the survey. Results are weighted to replicate a nationally representative distribution of respondents. The question asked how long a respondents' household could go without income before "hardship" set in.

We often neglect rising insecurity, for at least two reasons. First, the gap between the most affluent Americans and the rest of society has grown dramatically.[7] These fortunate families have not experienced the same rise in economic insecurity as the less affluent and their divergent experience looms large in media portrayals of the economy. Second, and more important, the changes of the last generation have yet to work fully through the age pyramid of American society. Changes in social benefits, especially those that affect retirement, often take decades to reach full effect. Shifts in labor markets usually have their greatest impact on less established workers. Thus, in many areas of social policy, older Americans reflect the economic order of forty or more years ago. Like a distant constellation whose light takes years to reach us, their much higher levels of economic security provide an image of the past: a world of widespread economic security in which a substantial amount of risk was pooled across workers and generations. Their children and especially their grandchildren are coming of age in a fundamentally different world—one that promises much greater insecurity and much more unequal prospects during their working lives and in retirement.

I have called this transformation the "Great Risk Shift," the long-term transfer of economic risk from broad structures of insurance, whether sponsored by the corporate sector or by government, onto the balance sheets of American families.[8] Unique among rich democracies, the United States fostered a social contract based on widespread provision of private workplace benefits. As Figure 3 shows, our *government* framework of social protection is indeed smaller than those found in other rich countries. Yet when we take into account private health and retirement benefits—mostly voluntary, but highly subsidized through the tax code—we have an overall system similar in size to that of other rich countries. The difference is that our system is distinctively private.

Figure 2: Public and Private Social Spending in Affluent Democracies, 2009



Source: OECD, "Social Spending During the Crisis: Social Expenditure (SOCX) Data Update 2012," http://www.oecd.org/els/soc/OECD(2012)_Social%20spending%20after%20the%20crisis_Data.zip. All figures reflect net spending after taxes. In order to avoid double counting, the value of tax breaks that subsidize private social benefits has been ignored for the calculation of net public social expenditure.

This framework, however, is coming undone. The unions that once negotiated and defended private benefits have lost tremendous ground. Partly for this reason, employers no longer wish to shoulder the burdens they took on during more stable economic times. Employers also no longer highly value the long-term commitments to workers that these arrangements reflected and fostered. The resulting shifts are larger than any retrenchment program pursued by conservative critics of public social programs. Health insurance has become much less common in the workplace, even for college-educated workers. In the early 1980s, 80 percent of recent college graduate had health insurance through their job;

by the late 2000s, the share had fallen to around 60 percent.[9] And, of course, the drop has been far greater for less educated workers.

Meanwhile, employers have restructured retirement benefits to eliminate guaranteed payouts (so-called defined-benefit plans) and replace them with individual savings accounts sponsored by employers (so-called defined-contribution plans).[10] 401(k)s and other defined-contribution plans do not pool the risk of inadequate income in retirement, nor do they ensure participation or adequate contributions in the way that traditional plans did. As a result, retirement security is declining, with most younger workers holding retirement savings that are far too limited to provide them with a secure retirement even with Social Security. We are moving back toward a world in which only the well off can expect to retire comfortably in old age.

Debate over the American social contract is badly dated. A period of greater insecurity is already upon us, embedded in the limited savings and less secure benefits of younger workers. Still, the choices we as a society make today will help shape how the costs and benefits of our current framework are distributed. More important, they could usher in a new era of broad security—if we move to redirect resources that are currently used to underwrite a costly, unequal, and eroding private system.

The Health Care Rent is Too Damn High!

In one of the 2012 Republican presidential debates, there was an unexpected contestant named Jimmy McMillan, running under the banner of the Rent Is Too Damn High Party. (Perhaps recognizing how few Republican voters are renters, the candidate known for his odd facial hair changed the slogan for the campaign to "The Deficit is Too Damn High!") Given that McMillan hales from New York City, it is understandable why he chose to focus on housing costs. But if there is one form of rent that really is too damn high, it is the exorbitant amount that Americans pay for health care. In the lingo of economics, a "rent" is excess payment made to market actors because of their political or economic power. The rents in health care consist of enormously wasteful levels of spending that result from policies tilted toward the health care industry within a market marked by vast imbalances of information and influence between patients and providers.

The good news is that getting control of these costs would vastly increase economic security both directly and indirectly—directly because health costs are a major threat to economic security in themselves, and indirectly because they are the biggest threat to America's long-term budget. Without "rent control" in health care, any larger reform goals will be crushed under the ever-growing burden of medical costs.

Tempers flare whenever international comparisons of health care are made. Yet certain basic facts cannot be ignored. The United States spends vastly more than other rich nations—almost twice as much per person as the next most profligate nation, Switzerland, and about $700 billion more overall in 2006 than you would predict based on our per capita income.[11] Furthermore, the main reason for this higher spending is not greater utilization of care: Americans visit doctors less often and spend less time in the hospital after treatment, they are younger on average, and there are fewer doctors and hospital beds per capita than is the norm among rich nations.[12]

Instead, the main reason we spend so much more is that our health care *prices* are so much higher than those found in other rich nations (see Figure 4). High prices equal high incomes for providers, drug companies, medical device manufacturers, and other industry players. They do not, alas, equal better health outcomes. Despite all the excess spending, Americans live shorter lives and are in poorer overall health than citizens of most other rich nations, and rates of preventable deaths are higher.[13] The quality of American health care is not the sole, or even the primary, reason for this poor performance. But at the very least, we are not getting very good value for our money.

These cost differences add up. If American expenditures had risen at the rate of Swiss expenditures between 1980 and 2010, we would have spent $15 trillion less on health care overall. Even in the jaded world of health costs, that is a lot of money (enough, for example, to send more than 175,000 kids to a four-year college).[14] Looking forward, America's long-term deficit problem is a health care spending problem. Take out Medicare and Medicaid, and the federal budget is more or less balanced as far as the eye (or at least the Congressional Budget Office) can see.[15] Over the long term, demographic shifts, while real, pale in their effects to the pressures created by rising medical costs. Ever-escalating health spending means not just less disposable income for workers and their families, but also less budgetary scope to upgrade benefits or invest in education, infrastructure, technology, and other critical sources of future growth. No health care cost-containment, no improved social contract.

Fortunately, this is an area where effective public and private efforts could make an enormous difference. Other countries control costs better than us for a simple reason: they create countervailing power to push back against all the industry players seeking higher incomes. These strategies do not require a "single payer," where the government acts as a public insurer for basic services. In Switzerland, insurance is private, though highly regulated; yet the government effectively sets prices. In other nations, the state oversees negotiations between providers and insurance funds. But in no rich nation besides the United States is cost control left to decentralized negotiations between private insurers and providers—negotiations in which increasingly consolidated and politically mobilized providers almost invariably hold the upper hand.

We do not need international experience to demonstrate this point. Medicare, the federal insurance program for the elderly and disabled, has controlled costs better than private insurers, pioneering new payment methods, such as prospective payment for hospitals, precisely because it has some measure of countervailing power.[16] Yet Medicare's power is limited. Not only does it covers the elderly and disabled alone, but the medical-industrial complex has managed to limit Medicare's countervailing power in myriad ways. In 2006, for example, drug companies successfully insisted that a prescription drug benefit not allow direct insurance through Medicare (instead, private supplemental plans offer the benefit), nor involve any price negotiation by the federal government. As a result, companies have been able to charge exorbitant prices. Lipitor, a cholesterol drug used by many beneficiaries, costs on average $124 a month in the United States—and $6 in New Zealand. The nasal medication Nasonex runs $108 a month on average—and $29 in Canada.[17] On most dimensions, Canada and New Zealand are as market-oriented as the United States. They just don't allow manufacturers with limited-duration monopolies thanks to patent protections charge whatever a distorted market will bear.

Figure 4: U.S. Medical Prices in Cross-National Perspective

Source: "The High Cost of Medical Procedures in the U.S.," *Washington Post*, March 2, 2012, accessed July 8, 2014, http://www.washingtonpost.com/wp-srv/special/business/high-cost-of-medical-procedures-in-the-us/. Data from International Federation of Health Plans.

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Faced with the reality of runaway prices, many critics of economic protections have argued that the problem is that patients don't have enough "skin in the game."[20] The solution, they insist, is to shift more risk and costs onto patients—especially Medicare beneficiaries—to increase their incentive to shop around and bargain for better prices. But health care is not a normal market. The asymmetry of information between providers and patients is huge. Shopping around, especially at the time of treatment, is often prohibitively difficult ("Wait, don't pull out my rupturing appendix; I want to see what the place down the street charges!"). And insurance creates its own Catch-22. High-tech care is simply too costly to finance without insurance. Yet insurance rightly protects the most costly patients whose expenses account for the vast bulk of our overall spending. (The costliest 10 percent of Medicare beneficiaries account for more than 60 percent of spending.)[21] They cannot have skin in the game unless we allow them to lose all their skin.

Transforming Medicare's guaranteed benefits into a voucher that covers only a fixed amount of the cost of care, with the growing remainder falling onto older and disabled Americans, makes sense only if we pretend that health costs borne by individuals are fundamentally different from health care costs borne by the federal government. Because such a shift will not control costs for all the reasons just mentioned—and may even cause costs to rise by reducing the pressure on federal policymakers to improve Medicare's efficiency—then reducing the federal government's commitment simply means shifting more costs and risks onto patients and their families. That is a poor bargain for today's older Americans. It is an even worse bargain for younger generations who are facing greater insecurity in the workforce today and will now be required to face greater insecurity in retirement, too.

Health care cost control would be good for economic security in itself, and very good for economic security when we consider the larger opportunity costs of ever-rising spending. In principle, such cost control is within our grasp. Extending Medicare to younger Americans, for instance, would give the program much greater leverage to hold down costs. It would also eliminate the current tension between Medicare and the Affordable Care Act (ACA) that has been created by the ACA's heavy reliance on slowing Medicare spending to finance new coverage for the nonelderly. Systemic cost-containment could be achieved through a variety of strategies, from an expanded Medicare program to a "public option" insurance plan for younger Americans without secure workplace coverage to so-called all-payer rate setting at the state or federal level to create standard prices across all insurers.[22] All of these would involve breaking open the demographic silos of our present inefficient system and fostering countervailing power on the purchasing side of health care.

The problem, of course, is the politics—a topic to which I will return. But the politics of increased cost control is arguably no less fraught than the politics of shifting ever more expenses onto Medicare beneficiaries, a constituency not exactly known for its quiescence. Instead of moving Medicare toward the private model of multiple plans and limited coverage, we should be doing the opposite: increasing the public bargaining power embodied in Medicare and extending its reach to younger Americans. This would not only allow the public sector to better control costs, but create pressures on private insurers to adopt public innovations in cost control and care management as well.

A New Social Contract

The road to reform runs through health care cost-containment. But where does it lead? Whole books are devoted to this question. But in the more limited space available here, let me lay out some of the main goals.

The overarching goal, of course, is an affordable framework of security that provides adequate protection against the most pressing risks of our era. Yet achieving that goal requires a measure of pragmatism often lacking among advocates who compare the shining beauty of policy ideals to the messy reality of actual arrangements. To use a social-science term, our public-private system of social protection is "path-dependent."[23] The road already traveled makes some future routes very unlikely (the Swedish cradle-to-grave model of social services, for instance). Central aspects of our system, such as our heavy reliance on workplace benefits, are likely to remain with us for some time to come. Reformers will need to work with what they have.

Yet they should also recognize that times have changed. When FDR signed the Social Security Act, economic insecurity was largely seen as a problem of drops or interruptions in male earnings, whether due to unemployment, retirement, or other costly events. Even as working women became the norm, America's social programs mostly failed to address the special economic strains that two-earner and single-parent families face. Whole categories of social protection that are nearly universal in other rich nations—from paid sick days to subsidized child care to early childhood education that enriches children's capacities even when their parents are working—are largely absent in the United States.

Nor do existing programs adequately address the distinctive unemployment patterns that became increasingly prevalent as industrial employment gave way to service work, such as the rising problem of long-term unemployment. And the shift of workers from one economic sector to another that is characteristic of our current era often leads to large cuts in pay and the need for specialized retraining, not just short-term income losses.

In short, U.S. social policy has become less capable of cushioning the biggest risks that workers and their families face. Our framework of social protection is overwhelmingly focused on the aged, even though young adults and families with children face the greatest economic strains. It emphasizes short-term exits from the workforce, even though long-term job losses and the displacement and obsolescence of skills have become more severe. In many places, it embodies the antiquated notion that family strains can be dealt with by a second earner—usually a woman—who can easily enter or leave the workforce as necessary. Above all, it is based on the idea that job-based private insurance can easily fill the gaps left by public programs, even though it is ever clearer that job-based private insurance is not enough.

These shortcomings suggest that an improved social contract should emphasize portable insurance to help families deal with major interruptions to income and big blows to wealth. They also mean that these promises should be mostly separate from work for a particular employer; social benefits should move from job to job. If this sometimes means corporations are off the hook, so be it. In time, they will pay their workers more to compensate for fewer benefits, and there are plenty of ways to encourage their contributions without having them decide who gets benefits and who does not.

By the same token, however, we should not force massive social risks onto institutions incapable of effectively carrying them. Bankruptcy—which afflicts roughly 1.5 million mostly middle-class families each year—should not be a backdoor social insurance system.[24] Private charity care should not be our main medical safety net. And credit cards should not be supplemental income for families when times are tight. To be sure, when nothing better is possible, we may need to preserve even incomplete and inadequate safety nets. But the ultimate goal should be a framework of social insurance that revitalizes the best elements of the present system, while replacing those parts that work less effectively with stronger alternatives geared toward today's economy and society.

Which brings us to the final principle: measures to enhance security should be designed to enhance opportunity. Most of us think of these measures a way of helping those who have had bad fortune or have fallen on hard times. Yet, as FDR recognized, providing economic security has far broader benefits for our economy and our society. Corporate law has long recognized the need to limit the downside of economic risk taking as a way of encouraging entrepreneurs and investors to make the risky investments necessary to advance in a capitalist economy. The law of bankruptcy and the principle of limited liability allow entrepreneurs to innovate with the security of knowing that they will not be financially destroyed if their risky bets fail.

The experience of major economic shocks is among the most unsettling events that families go through, leaving psychological, economic, and social traces—from reduced happiness to decreased labor-force attachment to family dissolution—for years and even decades to come. Workers who come of age during a recession experience poorer earnings and employment outcomes for at least twenty years.[25] Workers who lose a job face a significantly heightened risk of death compared with their continuously employed counterparts—even two decades after unemployment.[26] Although some degree of economic insecurity is part and parcel of a dynamic capitalist economy, families torn apart by economic risks are not in a position to adequately plan for or invest in the future.

Just as entrepreneurs need basic protections to foster risk taking, families also need a basic foundation of financial security if they are to feel confident in making the investments required to advance in a dynamic economy. All of the major wellsprings of opportunity in the United States—assets, workplace skills, education, investments in children—are costly and risky for families to cultivate. Providing security can encourage families to make these investments, aiding not just their own advancement but improving the economy as a whole.

Rebuilding the Three-Legged Stool of Retirement Security

To see what such a framework might look like, let us return to one of the most glaring examples of the Great Risk Shift: the movement away from secure pension benefits in the private sector. America's framework for providing retirement security was historically referred to as a "three-legged stool," with Social Security, private pensions, and personal savings each carrying an important part of the weight of securing workers' retirement. As private defined-benefit pensions have disappeared, we have moved from the traditional three-legged stool of retirement security to a two-legged stool—Social Security and private savings (inside and outside of 401(k)s). Needless to say, this stool is much less stable than the last.

Today, Social Security is basically the only guaranteed pension left. Yet the role of Social Security has declined in the last twenty years as well, mainly due to cutbacks that occurred in the late 1970s and early 1980s. Looking forward, Social Security is expected to replace a smaller share of pre-retirement income than it did in the past. That is true even if Social Security pays promised benefits—an assumption that is safer than Social Security's doomsayers believe but still hinges on favorable economic and demographic trends and some adjustments in the program.

But if Social Security has grown modestly less generous, private pensions have essentially ceased to provide any risk protection to a large chunk of less-affluent workers. This is not a coincidence. The incentives for higher-income Americans to save have ballooned with the expansion of tax-favored investment vehicles like 401(k)s. Yet, because the tax breaks for these benefits are skewed toward higher-income Americans, most Americans receive modest benefits from these costly tax breaks. (In 2011, tax breaks for retirement pensions and accounts cost the federal government over $140 billion in forgone tax revenue). Roughly eighty percent of these tax subsidies for retirement saving accrue to the top twenty percent of the population. Only seven percent accrue to the bottom sixty percent of the population.[27]

The reasons for this stark disparity are threefold—and they largely hold true with other tax-subsidized workplace benefits. First, lower-income Americans face lower marginal tax rates, making tax breaks for private benefis worth much less to them. Second, lower-income Americans are least likely to have access to tax-favored benefits. And third, lower-income Americans have the least discretionary income to contribute to tax-favored accounts (or pay for their rising portion of employment-based health premiums). Living paycheck to paycheck, they need the greatest incentive and assistance to save. Instead, the tax benefits for retirement are structured so that they provide the greatest rewards to higher-income workers. Not surprisingly, account balances in 401(k)s are highly tilted toward the rich. The typical account-holder has less than $20,000 saved, and this counts only those who *have* 401(k)s. Overall, around seventy percent of defined-contribution pension and IRA assets are held by the richest fifth of Americans.[28]

All this strongly argues for preserving and even expanding the one guaranteed source of retirement security for most workers that we have left: Social Security. Though Social Security has a long-term deficit, dealing with it does not require abandoning the core elements of the program: guaranteed lifetime benefits paid on retirement, provided as a right, and linked to lifetime earnings. The shortfall can be relatively easily closed by making benefits and the payroll taxes that fund them more progressive and by tying benefits to future longevity so that fortunate generations that live longer than the last receive slightly less from the program than now promised. Because most of the gains in life expectancy over the last generation have been enjoyed only by higher-wage workers, increased progressivity should take precedence over longevity-based adjustments.[29]

In particular, the so-called wage cap on Social Security payroll taxes should be eliminated or at least substantially raised, and applied to capital income as well as wages. As income has grown more unequal over the last generation, more and more of the highest wages are exempt from the Social Security payroll tax—which is capped at around $115,000 in annual earnings. Because high-income workers receive the lowest rate of return from Social Security, raising the cap results in far more revenue flowing into the program than new spending on benefits. In fact, eliminating the payroll-tax cap would by itself close the long-term funding shortfall.

Even with a secure Social Security system, today's workers will need other sources of income in retirement. 401(k)s as they are presently constituted are not the solution. Too few workers are offered them, enroll in them, or put adequate sums in them, and they place too much of the risk of retirement planning onto individuals, with too little information and insurance to help them build a secure retirement. Though many supporters of the present system argue that 401(k)s can be fixed with minor tweaks, such as requiring that companies automatically enroll their workers, these sorts of adjustments will not address the major problems: skewed tax subsidies, low contribution rates, leakage from the system when workers change jobs, and, most fundamental of all, the fact that many employers do not offer a 401(k) at all.

On the other side, some pension experts have proposed mandatory, government managed accounts with a guaranteed rate of return that would supplement Social Security, forming a "second tier" of compulsory retirement savings that would largely replace 401(k)s.[30] For all their merits, these proposals face serious political and logistical obstacles. Instead, I propose a middle way: a more robust version of plans for "universal 401(k)s" that have received notice in recent years. Universal 401(k)s should be available to all workers. Employers would be encouraged to match employer contributions to these plans, and indeed, the federal government could provide special tax breaks to employers that offered better matches to lower-wage workers Automatic enrollment would be required, and the default contribution rate would be set at a level that would finance an adequate retirement along with Social Security. Moreover, the default investment option under 401(k)s should be a low-cost index fund with a mix of stocks and bonds that automatically shifts over time as workers age to limit market risk as workers approach retirement. Existing tax breaks for 401(k)s would be replaced with a retirement savings credit that would be placed in the accounts of all workers. Such a credit would be the same for all workers and, hence, a much larger share of the income of low-wage workers.

After my criticism of 401(k)s, it may come as a surprise that I think universal 401(k)s are the best route forward. Yet the difference between universal 401(k)s with strong incentives for contributions and the present system is profound. What is more, I recommend one additional change: requiring that 401(k) accounts be converted into a lifetime guaranteed income at retirement unless workers could show they had sufficient assets to weather market risk. These new annuities could be provided by private firms under strict federal rules or directly by the federal government. To help workers' plan ahead, 401(k) balances should be reported to account holders not as a cash sum, but as their expected monthly benefit amount—just as Social Security benefits are reported. In essence, universal 401(k)s along these lines would bring back something close to a guaranteed private pension, with government, rather than employers, pooling the risk.

Getting from Here to There

With apologies to the 1992 Clinton campaign, whose campaign handbook *Putting People First* summed up their appeal to the middle class, those seeking to upgrade the American social contract should be "Putting Politics First." By this, I mean that reformers must think not just about what policies would be better than our current crumbling framework, but also about how our polarized and gridlocked political system could realistically take us from here to there. In this final section, I present five strategic maxims and suggest how they link to necessary changes.

Demography Isn't Destiny but It's Powerful. American society is changing fundamentally. Hispanics are becoming the largest minority group, and whites will represent a minority of the U.S. population within a generation. Single and single-parent women—who strongly lean toward progressive policies such as those outlined in this chapter—are growing part of the electorate. And the shifts in the workforce discussed in this chapter have meant that more and more workers, white as well as non-white, face the kinds of insecurity and financial strains once limited to the working poor.

In the short term, these changes have very mixed effects. In presidential election years, when turnout is high, they have resulted in a more progressive electorate, but they have also activated political forces concerned about the transformations underway—forces willing to limit access to the ballot box, gerrymander districts, and sink enormous sums of money into elections to hold back the tide. Yet he arc of history bends toward a greater voice for less advantaged Americans who will see value in greater security. Whether politicians will hear them depends on whether advocates create the ongoing pressure to develop viable options and keep them on the agenda.

Turning the Tables. To create that pressure requires that progressives take a page out of the conservative playbook. In the early 1980s, two advocates of Social Security privatization presented what they called a "Leninist strategy" (yes, that was actually the title of their piece).[31] At its center was the idea that conservatives had to work diligently behind the scenes to shift policy toward their preferred outcome of private retirement accounts, which, they hoped, would eventually become the basis of privatization. Though the idea did not pan out—in part because those accounts were so much less attractive than they thought they would be—the strategy was sound. In American politics, big reforms are hard and rare. Many of the adjustments that are needed will come not through major legislative changes, but through persistent improvement of present arrangements.

Nowhere is this more true than with regard to health care. The passage of the ACA was the biggest change in our framework of social protection since the creation of Medicare and Medicaid in 1965. But the law is a "starter home," as one backer called it—complex, sometimes contradictory, and on the whole insufficient to either provide universal insurance or seriously rein in costs.[32] This is not to argue that much more could have been achieved; given how close the law came to passage and how contested it remains today, the notion that single payer could have passed if only President Obama had fought for it is fanciful. But advocates of the law will have to push it forward on multiple fronts—state and federal—if the ACA is to have anything close to its promised effects, much less go beyond them to provide universal affordable coverage.

I have already suggested that these changes should seek to bring the successful international approach to cost control to bear on America's out-of-line prices. Another goal should be to allow a gradual movement away from employment-based coverage by creating the option for all employers to finance coverage through the new insurance exchanges set up to provide private options (these exchanges should also add a public option). In practice, this means shifting toward payroll-based contributions for coverage through the exchange—the Social Security model and the common way of financing coverage in other systems based on multiple private plans. If these payroll contributions were lower than the cost of private insurance, as they should be, the burden on employers would actually be lower than in the current system. At the same time, workers would be guaranteed portable coverage that moved from job to job.

A Politics of "Rent Control." Perhaps the most lamentable feature of America's eroding framework of economic security is the degree to which it wastes resources that could be better applied to improve security or achieve other ends. Massive subsidies to encourage high-income taxpayers to save are mostly wasted resources, since these are the Americans most likely to save on their own. Paying two to three times as much for the very same health services delivered in other countries is wasteful—a transfer from taxpayers and cash-strapped patients to highly profitable and highly paid sectors of the economy. Yes, there is plenty of inefficiency and waste in government. But much of it involves excessive deference to and support for private-sector players that benefit from distorted markets that allow them to provide weak guarantees of security at exorbitant costs.

A politics of "rent control" would have two benefits. First, it would free up resources. If medical costs were restrained as effectively as they have been in other nations, many of our long-term budget problems would simply disappear. Second, a concerted campaign to pare back rents that are borne by citizens and consumers would dispel some of the widespread doubts about the capacity of the public sector to address social problems—perhaps the greatest political barrier to a more secure future.

Reviving Faith in Government. As the journalist George Packer notes, we have lost our faith in "collective self-betterment."[33] Americans value and laud Social Security and Medicare, but mostly see them as one-off successes, rather than as a demonstration that social insurance is actually the best way to deal with insecurity. Trust in public officials has plummeted since the 1960s, reaching basement levels in recent years. A foundation of economic security cannot be built on the soft sands of public cynicism.

Our increasing spending on private social benefits—itself partly a reflection of this lack of faith—only makes the situation worse. The political scientist Suzanne Mettler has found that Americans do not see tax breaks, public loans, and other indirect forms of public aid as governmental, even if they cost the government billions.[34] Those who rely the most on these hidden benefits are also most skeptical of the state. Mistrust breeds mistrust, encouraging our leaders to rely on hidden forms of aid that fail to move the needle of public disillusionment. Mistrust also breed mistrust because leaders are encouraged to avoid at all costs the rhetoric of public problem-solving. Silence about what government can do thus further reinforces the vicious cycle.

Yet vicious cycles can become virtuous cycles when the dynamic is reversed. Reforms that demonstrate the value of public action, such as those outlined in this chapter, feed the reservoir of goodwill on which additional initiatives may draw. This was perhaps FDR's greatest insight. When he declared "the only thing we have to fear is fear itself," he did not mean our nation was safe from threat. Far from it: His point was that even well-grounded fears should not prevent us from finding solutions. The same holds true today. The growing sense of insecurity is paralyzing. It corrodes our faith in collective institutions and pushes our focus inward. To reverse this dangerous drift, we need to remember—and fight for—the basic ideal that FDR's Social Security Act embodied: that some economic risks cannot be addressed through individual or private action, but require the faith in collective self-betterment that made our nation great.

Notes

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[6] Mark Robert Rank, Thomas A. Hirschl, and Kirk A. Foster, *Chasing the American Dream: Understanding What Shapes Our Fortunes* (New York: Oxford University Press, 2014), 36.
[7] Facundo Alvaredo, Anthony B. Atkinson, Thomas Piketty, and Emmanuel Saez, "The Top 1 Percent in International and Historical Perspective," *Journal of Economic Perspectives* 27(2013): 3-20.
[8] Jacob S. Hacker, *The Great Risk Shift: The New Economic Insecurity and the Decline of the American Dream* (New York: Oxford University Press, 2008).
[9] Based on analyses of the March Current Population Survey by Liana Fox and Elise Gould, "Employer-Provided Health Coverage Declining for College Grads in Entry-Level Jobs," Economic Policy Institute, July 18, 2007, accessed July 8, 2014, http://www.epi.org/publication/webfeatures_snapshots_20070718/.
[10] Twenty-five years ago, 83 percent of medium and large firms offered traditional "defined-benefit" pensions that provided a fixed benefit for life; today, the share is below one-third. Instead, companies that provide pensions mostly offer "defined-contribution" plans like the 401(k), in which returns are neither predictable nor assured. Moreover, despite the expansion of 401(k) plans, the share of workers with access to a pension at their current job—either a defined benefit plan or a 401(k) plan—has fallen from just over half in 1979 to under 43 percent in 2009. See Hacker, *The Great Risk Shift*, Ch. 5.
[11] Carlos Angrisano, Diana Farrell, Bob Kocher, Martha Laboissiere, and Sara Parker, "Accounting for the Cost of Health Care in the United States," McKinsey Global Institute, January 2007, accessed July 8, 2014, http://www.mckinsey.com/insights/health_systems_and_services/accounting_for_the_cost_of_health_care_in_the_united_states.
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[22] For more on the public option and its promise, see Jacob S. Hacker, "Health-Care Reform, 2015," *Democracy* 18 (Fall 2010), accessed July 8, 2014, http://www.democracyjournal.org/18/6772.php.

[23] This is the argument elaborated in Jacob S. Hacker, *The Divided Welfare State: The Battle over Public and Private Social Benefits in the United States* (New York: Cambridge University Press, 2002).

[24] Katherine M. Porter, ed., *Broke: How Debt Bankrupts the Middle Class* (Palo Alto: Stanford University Press, 2012).

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[27] Jacob S. Hacker, "Introduction: The Coming Age of Retirement Insecurity," *Meeting California's Retirement Security Challenge*, ed. Nari Rhee (Berkeley: UC Berkeley Center for Labor Research and Education, 2011), 7.

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[32] That backer was Senator Tom Harkin, quoted in Hacker, "Health Care 2015."

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[34] Suzanne Mettler, *The Submerged State: How Invisible Government Policies Undermine American Democracy* (Chicago: University of Chicago Press, 2011).