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UNIVERSITY OF CALIFORNIA, BERKELEY
CENTER FOR LABOR RESEARCH AND EDUCATION
INSTITUTE OF INDUSTRIAL RELATIONS
BERKELEY, CA 94720
(415) 642-0323

OPTING OUT OF SOCIAL SECURITY--THE BERKELEY VOTE

by Bruce Poyer

Berkeley city employees will soon vote on a proposal to withdraw from Social Security coverage. The city is offering an alternative plan which requires careful analysis, because it is not in the best interests of the city's employees. Social Security will continue to provide the best available protection against the inflationary erosion of promised retirement benefits. And Social Security's combination of survivors' and disability coverage will continue to provide better family protection than any California city or governmental unit can manage to finance through private insurance alternatives.

The choice being offered to Berkeley's employees involves typical cost/benefit questions which arise in most opting-out situations. The decision they make will have considerable impact on their future security, on the security of their families, and on future costs of the city. Their decision may also influence other local governments proposing withdrawal options. It should be of special concern to the wide variety of unions and associations representing city employees--especially SEIU, AFSCME, and the building trades, as well as those representing school and emergency service employees.

The City's Proposal. The present annual Social Security payroll tax is 13.4% on earnings up to the maximum taxable wage of $32,400. 6.7% of the tax, up to a maximum of $2,170.80, is paid by the employee, and an equal amount is paid by the city. Instead of continuing these payments, the city of Berkeley proposes (a) that the employees should retain their 6.7% portion of the tax for use as they desire; (b) that the city should discontinue its 6.7% portion of the tax payment, allocating 5.7% to a new supplementary retirement account, and 1.0% to a disability insurance plan; and (c) that the maximum city contribution to support both retirement and disability protection should be fixed at the total of 6.7%, not to exceed a maximum contribution of $2,170.80.

For retirement, the city's maximum rate would be 5.7%, and its maximum contribution would be $1846.80. If salaries increase by 8% annually, the median salary for Berkeley city employees will be $34,556 by 1988. In a period of only six years, the city would then be contributing less than 5.7% of payroll for fully half of its employees. The city's primary cost interest in its proposal is therefore in the tax rates and maximum contributions which are fixed for the future, for both retirement and disability.

Retirement Benefits Under the City's Plan. What could employees expect from the city's new Supplementary Retirement Account plan? The city assumes that its contributions will have earnings of 10% annually, for all projected time periods. But the past experience of employee benefit plans in the U.S.--especially public employee plans--cannot justify that kind of projection, even for the next ten years, let alone the next 30. In addition, the city proposes to make only fixed income investments, which are extremely vulnerable to inflation.

Even with an unrealistic earnings assumption of 10% for all future years, compounded annually, the city's proposal still loses to inflation. The following data is based on an employee earning $26,315 this year, with contributions to the city's Supplemental Retirement Account of $1500 per year. In column (5), the adjustment to 1982 dollars is made by using the 8.9 national inflation rate of 1981:

(1) years	(2) cumulative deposits	(3) cumulative earnings	(4) total unadjusted value	(5) total value adjusted for inflation (1982 dollars)	(6) total adjusted value as % of total unadjusted value
5	7500	2565	10065	6542	65%
10	15000	11295	26795	11542	43%
20	30000	64500	94500	17010	18%
30	45000	226410	271410	21713	8%

After 30 years, inflation has reduced the real value of the contributions and earnings to only 8% of the unadjusted value. In the meantime, the employees have assumed all the risks of unknown inflation and of uncertain earnings, because the city's financial obligation has been limited and fixed.

Retirement Benefits: the City's Plan Compared to Social Security. The employee in the above example, earning $26,315 in 1982, could contribute an additional $1500 per year to a Voluntary Deferred Compensation Account set up by the city. Under the same assumptions, there would be another $21,713 in 1982 dollars after 30 years --or a total amount of $43,426 in 1982 dollars. If used by someone 65 years old to purchase annunities this year, that amount would buy about $400 per month for life, not subject to cost of living adjustments. By comparison, an employee with $26,315 in 1982 income, now retiring at age 65 under Social Security after 30 years of service, would have a benefit of about $643, subject to cost of living adjustments for further inflation.

Cost of living adjustments in Social Security benefits averaged 9% a year between 1975 and 1981--a period when private plans made very few adjustments in retiree benefits. In addition, Social Security tax rates are periodically adjusted to inflation (and to a host of other variables) by legislation, and the taxable wage base is automatically adjusted annually to a national index of wage rates.

National proposals may be made to weaken or even to eliminate the current indexing provisions which protect Social Security beneficiaries against inflation. But actual legislation will confront enormous political opposition, not only from organized labor and the nation's senior citizen groups, but also from a broad spectrum of middle class Americans. Such a political battle may be coming. But Berkeley city employees who vote to withdraw from Social Security in favor of the City's plan will simply be losing the same battle in advance.

Conclusion: In terms of retirement benefits alone, the option proposed by the city of Berkeley is not equal to Social Security protection. Also, the city's proposed disability coverage is not equal to Social Security protection. And there is nothing in the city's plan to give its employees the kind of survivor's protection which their families have under Social Security.

Many variations of the Berkeley proposal, designed primarily to reduce costs, are being presented to other units of state and local government employees in California. When they are carefully compared, Social Security turns out to be the best bet. The system today keeps more than 15 million Americans above the proverty line. They are people who would otherwise be reduced to proverty because of death in the family, disability, unemployment, old age, or some combination thereof--and not because of the taxes necessary to support an adequate system.

-- Bruce Poyer