

## Chapter 9 Review: Social Insurance 1

### Social Security and Unemployment Insurance: John

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**Readings:** Rosen: Chapter 9, all

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#### Outline

- I. Characteristics of Social Insurance Programs**
  - II. Justification for Social Insurance**
  - III. Overview of Social Security**
    - A. Fully Funded (pre-funded) vs. Pay as You Go.
    - B. A brief history of SS funding
    - C. Defined Benefits vs Defined Contributions
  - IV. Major issues regarding Social Security**
    1. equity: Who gains? Who loses? Is this fair?
    2. financing SS
    3. incentives to work
    4. incentives to save privately
    5. SS's effect on poverty amongst the elderly
  - V. Benefits under Social Security**
  - VI. Distributional Issues regarding SS**
  - VII. SS's Effect on Incentives Among Retirees**
  - VIII. Financing SS**
    - A. Financial Viability of current system
    - B. Proposals for "Saving SS"
  - IX. Cautions about proposals to transition SS to fully funded**
    - A. Transitional funding problems
    - B. This changes the nature of Social Security
  - X. SS's Effect on Incentives to Save**
    - A. SS may crowd out private savings
    - B. Govt. may just spend SS savings, thereby depleting national savings and hurting growth
    - C. What is national savings and why is it important?
  - XI. SS's Effect on Poverty Amongst the Elderly**
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## Problems<sup>1</sup>

1. Chapter 9 Discussion Question (pp 198 – 199) # 2
2. Chapter 9 Discussion Question (pp 198 – 199) # 3. While you will not be able to come up with exact \$ (or £) figures, you should be able to come up with % changes.
3. Chapter 9 Discussion Question (pp 198 – 199) # 4
4. Chapter 9 Discussion Question (pp 198 – 199) # 5
5. Ahhh! The semester is over and you are on vacation. You, of course, go to Ozark, Missouri to visit your favorite Uncle, Duane. Duane is getting near retirement. He states; *“You know young-un, I’m not the spring chicken I used to be. I’ll be retiring soon and I ‘m mighty worried. I saved all my pay vouchers and have figured out that I haven’t paid much into my social security account. I might not be able to live very well in retirement.”*

At this time Aunt Shana, Duane’s wife, says; *“Duane, I’ve stayed home and raised your kids for you instead of working. Now you tell me you haven’t paid much into Social security! You better have a plan to feed us during our old age!”*

Help Duane out. In particular, answer the following:

- a. Explain how current (and those in the near future) Social Security benefits are funded.
  - b. How are Duane’s benefits tied to the amount of payroll tax money he sees on his pay stubs? Hint: There are two parts to this question. 1) Was/is Duane the only one paying payroll taxes on his behalf? 2) How are past payments tied to benefits?
  - c. What kind of deal do you think Duane and Shana are getting out of Social Security? Explain your answer.
6. Cousin/Uncle Steve is 32 years old.<sup>2</sup> He expects to retire sometime around 2035. He states; *“I’ve read the numbers. I know Social Security will be bankrupt and won’t be able to pay one red cent by the time I retire. If the current system continues without changes, I won’t get any Social Security Retirement benefits.”*<sup>3</sup>

Is Steve correct? Will Social Security not be able to pay anything, if there are no changes to the current system, after about 2035? If not, clearly explain why.
  7. Cousin/Aunt Wren is a bit more optimistic than the rest of the family.<sup>4</sup> She states; *“I have more faith in our government and the American people than the rest of you. We will figure out a way to save Social Security.”* You have always been partial to Wren (in a perfectly respectable and

<sup>1</sup> The names have been changed to protect the innocent. Any resemblance to people, real fictional, or those in the Lovett family is purely coincidence.

<sup>2</sup> Steve is Shana’s brother.

<sup>3</sup> Feel free to hum Merle Haggard’s song “Big City” while you answer this question. ... *“You can keep your retirement and your so called social security ...”* Hey, I know you are all closet Merle Haggard fans. Myself, I really was a fan of his later stuff. It just doesn’t have the soul of his earlier stuff.

<sup>4</sup> also Shana’s sister.

legal way of course). You want to help her out. Do this by discussing several methods by which Social Security can be saved.

This question is a pretty long one. If you saw one like this one the exam, it will either constitute a major portion of the exam or will be narrowed down a bit.

8. Paul (no one is quite sure how he is related to the family ... but he hangs around anyway) is a survivalist and is generally not terribly keen on government. He states; *“Heck! I don’t even think the government should be in the business of Social Security. Why don’t we just rely on people’s own private, individual initiative to provide for people’s age retirement?”*

Answer Paul. Explain the basic arguments for social insurance programs, in particular Social Security. Hint: 1) Make your movements real slow, avoid eye contact, and make your explanations really good. Paul is armed and a bit agitated. 2) I didn’t discuss economizing on decision making. You will have to get this argument from the text.

9. **Find this out on your own.** Grampa Bob has recently gotten hooked on phonics. He is practicing on your Public Finance textbook. He says: “Okay smarty-pants, let’s see if you know everything in Chapter 9 of this book. Tell me how unemployment insurance is financed. In particular, answer the following questions for me: Who directly pays for unemployment benefits? Is the system funded or pay as you go? Do all payers pay at the same rate?”

Wow! Phonics really works.<sup>5</sup> Answer Grampa Bob’s questions.

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<sup>5</sup> And it is the only segway I could think of to this question.