Opening Address: The Transformation of Social Security

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One of the striking things about the U.S. Social Security program is that it required not one but three different starts. If we examine each of these starts, we discover that it took from 1935 until 1950 for the program to be launched. The program, in other words, was not an inevitable triumph. Instead, it needed to overcome a series of political obstacles.

The Origins of Social Security

Perhaps the most surprising thing about Social Security was that it began at all. The notion of legislating a contributory social insurance program in the middle of the worst depression in the nation's history was not a congenial one to most economists. If the object of the program was to alleviate poverty among the nation's elderly, then such a program appeared to be a very inexact tool of social policy. People who were already old stood to gain nothing from the program, since they had not had the chance to contribute to it. People who were nearing retirement age had little opportunity to build up funds in the system and hence earn a decent pension, particularly since pensions were to be based on something called "cumulative creditable wages."

If the object of the program was to build up funds for pensions to be paid in the future to current workers, then problems still remained. For one thing, the workers had to take it on faith that they would ever receive a pension. In the meantime, they faced the prospect of paying into the program without seeing anyone getting anything back, except for lump sum payments in the event of a person's death. As matters stood, tax

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collections were set to begin in 1937, and the first regular pensions were not be paid until 1942. For five years, then, the program was to function simply as a tax, not as a benefit. For another thing, the taxes were themselves dubious forms of fiscal policy. Beginning in 1937, the tax would draw money out of workers' paychecks at a time when many economists believed that the economy required more purchasing power, not less.

Indeed, economists emerged as early critics of the program, particularly those economists who subscribed to the recently articulated theories of John Maynard Keynes. Among Keynes's followers in America was Alvin Hansen who, as a graduate of the University of Wisconsin, knew many of the leaders of the Social Security program personally and who served on the first Social Security advisory council. Hansen engaged in a spirited correspondence with Arthur Altmeyer, the head of the Social Security Board, in which Hansen warned, "Every time we face a tendency toward recession, the impounding of this Old Age Reserve Account will plague us and add to our difficulties in overcoming a recession."

Not only cerebral economists but also practical politicians criticized the program. The Economic Security Bill that Congress received in January 1935 contained many titles. It amounted to a compendium of existing federal social welfare programs, combined with proposals to begin two new social insurance programs: one to cover unemployment and the other to deal with income maintenance during old age. Presented with the proposal for old-age insurance, Congress reacted at best with indifference and at worst with disdain. Congressman Allen Treadway, who was the ranking Republican on the House Ways and Means Committee, called old-age insurance the "worst title in the bill . . . a burdensome tax on industry." Congressman Daniel Reed pointed out that neither old-age insurance nor unemployment compensation were "relief provisions and they are not going to bring any relief to the destitute or needy now nor for many years to come." Nor was the discontent with old-age insurance limited to the Republican side of the aisle. Among those who voted to remove old-age insurance from the omnibus economic security bill was Senator Walter George, a prominent Georgia Democrat who later became the head of the Finance Committee.

Old-age insurance did have influential advocates or it would never have passed. Among those who believed in it were the economists and actuaries on the staff of the Committee on Economic Security who had helped to design it. Probably the most important of these individuals was J. Douglas Brown of Princeton University. He managed to convince others on the staff, such as Edwin Witte of the University of Wisconsin, that an old-age insurance law belonged in the Economic Security Bill. Witte, although not unsympathetic, concentrated most of his energy on unemployment compensation. That was the high-profile item of the moment, and it was one in which Witte, who administered the recently passed Wisconsin unemployment compensation law, was personally invested. Even more surprisingly, Brown sold Witte and the rest of the staff on the notion that old-age insurance should be a federal law. The first staff proposals took traditional forms, with the states or private insurance companies administering old-age insurance programs. In subsequent drafts, the staff worked up to the idea of federal administration. Brown later wrote that the staff deliberately exaggerated the difficulties of establishing separate state old-age insurance systems, writing memos to the other staff members with "awesome descriptions of the complexities."

More important than the staff were the political principals. Frances Perkins, the U.S. Secretary of Labor who chaired the Committee on Economic Security, had an intellectual predisposition toward social insurance that she had gained as a member of the New York Industrial Commission. In that job, she helped to administer the state's workers' compensation law, which, until 1935, was America's most ubiquitous form of social insurance, with workers' compensation programs in every state except Mississippi. Although it is difficult to reconstruct just how much Franklin Roosevelt knew about social insurance, he, too, appeared to be sympathetic toward the self-help aspects of old-age insurance. He and Perkins may have favored programs administered at the state level, but they acquiesced to the notion of a federal old-age insurance program.

The President, for his part, took the liberty of making the program even more self-supporting than either the committee staff or Secretary Perkins wanted. When he heard that the plan written by Brown depended on general revenue subsidies to keep the program solvent in the future, he objected on the grounds that he could not mandate future government expenditures. At the very last minute, he ordered the staff to rework the tax rates, so that the program would never need to depend on general revenues. That added to the burdensome nature of what already promised to be an unpopular tax. Under the Roosevelt scheme, the tax rate would reach 6 percent of taxable payroll (the first $3,000 of each employee's income) by 1949; by way of contrast, the staff-proposed tax schedule would have reached 5 percent by 1957. It was as if the President deliberately increased his political handicap.

Congress did not delete the old-age insurance section from a law that contained so many other things because, in effect, the President asked them not to do so, and he still had considerable political clout. Hence, the President offered Congress what Carolyn Weaver has called a "tie-in deal." Along with old-age insurance came relatively popular programs such as grants-in-aid to the states that the states could use to supplement their old-age pensions. For every dollar the state contributed, the federal government would match that dollar, up to a total of $30 a month per elderly recipient. To get the program that would be of immediate benefit to the elderly as well as other programs that promised to bring federal funds into many congressional districts, Congress went along with the notion of old-age insurance. Even then, the support was grudging. At the very end of the deliberations, for example, the Senate passed an amendment that would have exempted workers who worked in places with private pension plans from participating in the Social Security program. The amendment had been prepared by a private actuary who wished to preserve the market for private annuities. The Senate refused to retreat on this matter until practically ordered to do so by the President. To gain that concession, the Administration had to promise that the idea of contracting out of Social Security would receive further study.

As a close observer of the progress of the bill through Congress, Edwin Witte, for one, was very worried. He told one of his correspondents at a critical point in the deliberations that "we have been taking it too much for granted that the economic security legislation will be passed in some form just because it is an Administration bill." He worried, as did many others, about the competition of the Townsend plan. This scheme, strongly opposed by the Administration, had a great deal of political appeal because it offered the elderly something for nothing. Anyone over 60 years old would receive a pension of $200 a month on the sole condition that they spend the money that month. Townsend understood that the plan would be popular not only with the elderly but also with the many others who would receive the elderly's money. As he put it, the elderly were only the means for restoring prosperity to everyone. Witte, for his part, noted that "all members of Congress are afraid of the Townsend people," who had a "host of lobbyists" and "letters pouring in, in a greater volume than ever." The Congressmen did not want to "vote on the Townsend plan," but they were also afraid to oppose it.

The Reserve Controversy and the Second Start

Things did not improve for the Social Security program after the law finally passed in August 1935. The Republicans decided to make an issue of Social Security in the 1936 election. When the first payroll deductions began in January 1937, some workers found a note in their pay envelopes that equated the new Social Security taxes with theft. As late as May 1938, Social Security officials met with a group of employers who questioned the point of providing workers with receipts for Social Security deductions. Most workers, the employers said, simply threw the receipts away, and some suspicious workers even wanted to go to Baltimore and make sure that their contributions had been credited to their accounts.

The reserve financing plan attracted the most criticism. Employers and employees paid Social Security taxes; employers sent the money to the U.S. Treasury Department, which used it just as it used any other form of revenue. Until 1939, the money raised was not legally dedicated to Social Security. Instead, Congress needed to appropriate the money into the Social Security account. Once in this account, the money was used to pay benefits, and the money left over, which was a considerable amount, was invested in government securities. The plan was to use the money in the reserve account to keep the program solvent in the future. In 1937, for example, Congress appropriated $511 million into the Social Security account, but only $6 million was needed for current expenses. In 1937, therefore, most of the Social Security money went into the reserve account. At the far end of the actuaries' calculations, in 1980, appropriations would reach more than $2 billion and benefits more than $3.5 billion.

The rise in benefit costs reflected the simple fact that, whatever else happened, a greater percentage of the elderly would be eligible for Social Security benefits in 1980 than in 1937. Furthermore, the actuaries seriously underestimated the population in 1980, failing to foresee the postwar baby boom. That meant that the actuaries understated the amount of revenue that would be paid into the system. Although the actuaries foresaw a substantial shortfall, they expected the problem to be handled through the reserve fund. By 1980 the balance on the reserve would have reached over $46 billion, and the interest would be enough to make up the difference between income and expenditures.

The problem with this scheme was that the size of the projected reserve attracted people's attention. That figure represented eight times the amount of money then in circulation in the United States. It amounted to nearly five times the amount of money in savings banks. It was enough money to buy all the farms in the United States and still have $14 billion to spare.

The idea of building up such a large reserve at a time when the need for current income was so dire grated against depression-era sensibilities. The Republicans sensed a winning issue. In the 1936 platform, the Republicans charged that the 1935 act was unworkable. "The so-called reserve fund," the party charged, "is no reserve at all, because the fund will contain nothing but the government's promise to pay, while the taxes collected in the guise of premiums will be wasted in reckless and extravagant political schemes." On September 26, 1936, Republican nominee and Kansas governor Alfred Landon elaborated on this theme. In a Milwaukee speech, he blasted Social Security as "unjust, unworkable, stupidly drafted and wastefully financed." Landon reserved the brunt of his attack for the reserve financing plan. "We have some good spenders in Washington," he said. "With this Social Security money alone running into billions of dollars, all restraints on Congress will be off."

Alfred Landon was certainly not alone in his condemnation of Social Security. The Brookings Institution, the American Federation of Labor, the Chamber of Commerce, and *The New York Times* all agreed that the reserve financing plan was a bad idea. Hence, even though the Republicans lost the 1936 election in a landslide, they refused to let go of the Social Security issue. Arthur Vandenberg, a prominent Republican Senator from Michigan, offered a Senate resolution in January 1937 to his colleagues in which he called the reserve method of financing "a perpetual invitation to the maintenance of an extravagant public debt." That led to a Senate Finance Committee hearing at which Vandenberg suggested, and Arthur Altmeyer agreed, that a congressional commission should be created to inquire into the matter.

This congressional commission became the first Social Security advisory council. Meeting for the first time in November 1937, it drew up a plan for what became Social Security's second start. Over the course of the next 13 months, the advisory council devised a means to reduce the reserve fund through two major methods: beginning Social Security payments earlier and expanding the types of benefits the system offered. Although the group contained a number of prominent economists such as Alvin Hansen, who was then serving as president of the American Economic Association, Paul Douglas, Edwin Witte, J. Douglas Brown, and William Haber, it was not economics so much as politics that dominated the discussions. The participants were inventing a new Social Security system according to the accepted notions of the day.

The group freely indulged in racial and sexual stereotypes. In a discussion about domestic workers, one advisory council member spoke of how difficult it would be to collect contributions from the "colored woman . . . who goes from house to house for a day's work here and a day's work there." In February 1938, the council first explored the idea of giving married workers a greater return on their Social Security investments than single workers. "I don't mind taxing the bachelors," said Professor Theresa McMahon. "I think they ought to take on the responsibility of sharing their income with somebody else."

On that same date, the group discussed the rationale for making a widow's benefit equal to three-quarters of the value of a single man's benefit. An actuary for the Social Security Board defended the decision on the grounds that a "widow could look out for herself better than the man could." J. Douglas Brown speculated that a single woman could adjust to a lower budget "on account of the fact that she is used to doing her own housework whereas the single man has to go to a restaurant." In a discussion about eliminating the lump-sum death benefits in favor of survivors' benefits, Walter D. Fuller, president of the company that published the *Saturday Evening Post*, told a cautionary tale of a "colored man in our employ who died. He was a widower and he had two minor children and he left $2,000 insurance. It was turned over to the family, and they immediately tried to run it up in a numbers game and lost it in two weeks."

As these comments show, the group clung to a model in which men joined the labor force and women stayed at home and did the housework. The group members suggested that the Social Security system be changed to reflect a worker's marital situation and to protect the family against the death of the wage earner. That meant that the system would pay benefits to the survivors of a deceased worker. In order for the system to do that, it was necessary to change the manner of benefit computation from "credited wages"—a number related to the amount of money a person had contributed—to "average" wages—a number related to the amount of money a worker was currently earning. Equity gave way to adequacy. A worker who died and left behind dependent children would get back more on his Social Security investment than would the worker who lived until old age, never married, and never had children.

The advisory council did try to balance the concept of adequacy against the constraint of cost. If the system were to offer life insurance, then it also made sense to explore other contingencies that might interrupt a worker's income, such as disability. The council members decided, however, that it would simply be too costly to begin a disability program during the depression. As one Social Security actuary put it, "It seems almost inevitable that when men are laid off and cannot work, with nothing in sight, no earning power whatever, they will be judged disabled."

The report of the advisory council formed the basis for the 1939 Social Security Amendments. As a result of this legislation, regular benefits became payable in 1940, rather than in 1942 as originally intended. The legislation transformed old-age insurance into old-age and survivors insurance. The great controversy over the reserve funds receded, in part because the 1939 amendments pointed the way to a reasonable contingency reserve, in part because the financing of the Second World War made large government expenditures seem less remarkable, and in part because Congress refused to raise the tax rate throughout the 1940s.

The Race with Welfare and the Third Start

Although the controversy over the reserve funds abated, the second start failed to transform Social Security into a popular or enduring program. In 1940 the nation spent far more on veterans' payments and workers' compensation than it did on old-age and survivors insurance. Even in the area of old-age security, social insurance played a distinctly secondary role to welfare. By the end of the 1940s, just over one-fifth of the elderly received old-age assistance (welfare) payments, and in a few states over half received such payments. The average monthly welfare benefit was $42 in 1949, compared with an average Social Security benefit of $25. As late as 1950, more than twice as many people were on state welfare rolls receiving old-age assistance as were receiving retirement benefits from the federal government under Social Security.

In agricultural states, the disparity between old-age insurance and relief was extreme. In 1947, for example, Oklahoma had 575 elderly people on relief for every 1,000 elderly residents, compared with a Social Security beneficiary rate of 50 per 1,000. The situation was similar in other rural states. Four times as many welfare recipients as Social Security recipients lived in the states of North Carolina, South Carolina, Mississippi, Tennessee, Alabama, and Georgia. The reason was that the Social Security program limited its coverage to industrial and commercial workers and excluded agricultural workers and self-employed businessmen.

It was no wonder, then, that more Congressmen paid attention to old-age assistance than concentrated on old-age insurance. In the fourth congressional district of Texas, where the ratio of expenditures between welfare and social insurance was on the order of 36 to 1, the local Congressman could honestly say, "old-age and survivors insurance means practically nothing to us." In 1949, J. Douglas Brown pleaded with Congress to rescue Social Security, noting that although "relief" was more popular and easier to administer, unless it was promptly replaced by social insurance it would send the United States "down the primrose path of state paternalism." Brown compared the situation to a fairy tale with an unhappy ending. Unless Congress strengthened and enlarged social insurance, "it may become a Cinderella displaced by its more demanding stepsisters, assistance and relief." Since public assistance was "fast winning the race," it looked as though Cinderella might never go to the ball.

Once the war ended and the Republican Eightieth Congress had departed Washington, Social Security administrators devised a third start for Social Security that rescued the program. Once again, an advisory council was summoned to Washington and once again it came up with a plan to save Social Security. The plan contained two basic elements. The first element involved bringing new groups into Social Security and keeping them there. That meant extending Social Security coverage and making sure that elderly individuals in these groups qualified quickly for benefits. The second element consisted of boosting benefits for everyone, to make Social Security more attractive financially than welfare. The advisory council plan of 1948 led directly to the Social Security amendments of 1950.

The 1950 amendments passed in part because labor and management leaders had signed collective bargaining agreements in the late 1940s that included retirement pensions. The agreements were written in such a way as to permit part of the pension to be paid through company funds and part through the Social Security system. That gave both management and labor a new incentive to favor increased Social Security benefits. Because the 1950 amendments also expanded coverage to such groups as the self-employed and made it relatively easy for the new groups to begin to qualify for benefits, the number of Congressmen with a stake in the program increased. As a result of these two developments, support for

Social Security increased and the long period of inactivity that marked the years after 1939 ended.

In the history of Social Security, the advisory council report that produced the 1950 amendments was important in both a personal and an institutional sense. On a personal level, the report represented the debut of Robert Ball, who served as the staff director for the advisory council, into the higher levels of policymaking. In a more fundamental sense, the 1950 amendments marked the start of Social Security's golden age, in which rising wage levels and expanding employment levels made possible the continued rise of Social Security benefits without substantial tax increases. The 1952 amendments set the postwar pattern. Both Democrats and Republicans backed a substantial rise in benefits, and the Social Security actuaries ruled that no new taxes would be necessary to fund the increase. The third start, unlike the first two, stuck.

Conclusion

In this manner, Social Security was transformed between 1935 and 1950. The original law followed the social policy logic of the era, in which it was simply assumed that Social Security applied to industrial and commercial workers. The image policymakers held was of a worker in an industrial plant with a steady attachment to the labor force. Everyone agreed that agricultural workers had at least as much need for Social Security, yet people thought it appropriate for such workers to have their own sets of policies. Hence, the early New Deal featured the National Industrial Recovery Act for industrial workers and the Agricultural Adjustment Act for farmers. The Social Security Acts of 1935 and 1939 continued that pattern.

The 1950 Social Security Amendments broke the mold. For the first time, they were aimed at workers in both the industrial and the agricultural sectors: the man who worked for General Motors and the man who sold farm implements in Moline. Almost alone among social welfare programs, Social Security came to enjoy a universal following, free of the occupational and class divisions that had plagued previous efforts at social policy. That meant that Social Security, with its dedicated source of tax funds and its direct relationship to the nation's payrolls, could harvest the postwar bonanza of economic productivity and become the most popular social welfare program in the nation's history.

As with any historical process, however, the triumph of Social Security was not inevitable. Before Social Security could triumph, it needed to work its way through the complicated logistics that came with starting a fully funded social insurance program in the middle of the Great Depression. First, the program needed to overcome the substantial obstacles to the expansion of the American state, in order to make it past the Congress in 1935. Second, the balance between adequacy and equity needed to be adjusted in socially acceptable ways, such as raising benefit levels for married workers and initiating survivors' benefits. Third, the program was changed to make it more attractive than its policy rivals. That necessitated raising benefit levels and expanding coverage in 1950. So Social Security did triumph, but the program required three starts before it could grow into the huge program of old-age, disability, and health insurance that it is today.

It might be, too, that the struggle to create an effective Social Security program made policymakers all the more resistant to fundamental reform of that program. Policymakers discovered in the 1950s and 1960s that Social Security was the one social policy vehicle that could be relied on to advance social goals. The same model that was used for old-age insurance was applied to disability policy in 1956. As a result, policymakers equated disability with retirement from the labor force, an association that would become problematic as society discovered that people with functional limitations could indeed work. In 1965, Social Security was extended to cover medical care, meaning that Social Security beneficiaries would benefit from an expensive form of health insurance but also making it increasingly difficult to extend that coverage to other groups in the population. Even the basic old-age insurance program would run into financial difficulties in the 1970s and 1980s, in part because the economy no longer performed so reliably as it had in the 1950s and in part because the nature of labor force participation was changing in a postindustrial age.

None of that diminished the hard-won triumph of Social Security between 1935 and 1950. In effect, Franklin Roosevelt cashed in some of his considerable political popularity in return for congressional passage of the Social Security Act of 1935. Although it was difficult, even impossible, to start a self-financed social insurance program in the middle of the Great Depression, the political process allowed the original Social Security program to be transformed into a near-universal program that paid relatively generous benefits. As a result of its third and final start, Social Security was, in a sense, as much a program of the prosperous fifties as of the depressed thirties.