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Camilla Watson

University of Georgia School of Law, camillaw@uga.edu

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MACHIAVELLI AND THE POLITICS OF WELFARE, NATIONAL HEALTH, AND OLD AGE: A COMPARATIVE PERSPECTIVE OF THE POLICIES OF THE UNITED STATES AND CANADA

*Camilla E. Watson**

All who manage are aware of the needs of the people. You cannot do without them, unfortunately. They must earn sufficient income to satisfy whatever standard of living has been set for them by either circumstances or choice. Within the framework of the marketplace of your organization there are established levels of remuneration within which you must function. If you get beneath the minimum of that marketplace, you jeopardize the longevity of valued people. Should you exceed the norm, you punish the operation. It is within these criteria that you must establish a level of "generosity."¹

I. INTRODUCTION

One of the theories of Niccolo Machiavelli was that rulers should strive for subtle generosity sufficient to avoid the reputation for being generous.² For, once the reputation for being generous is acquired, it becomes a cancer which will lead to impoverishment if that reputation is to be sustained. Even before the impoverishment stage, though, generosity may dissipate the ruler's resources so as to preclude efficient performance of his duties without raising taxes. Once taxes are increased, people come to hate the ruler, causing him to realize that the masses would have considered him to be generous if he initially had been more parsimonious with the few.³

* Associate Professor, University of Georgia School of Law; J.D., University of Mississippi; LL.M. (in taxation), New York University. This Article results from a paper I presented at the University of British Columbia in the Fall of 1992. I wish to thank the UBC law faculty for inviting me to participate in its faculty seminar. I also wish to thank Milner Ball, Robin Malloy, and Alan Watson who commented on an earlier draft of this Article.

1. WILLIAM T. BRAHMSTEDT, MEMO TO: THE BOSS FROM: MACK, A CONTEMPORARY RENDERING OF THE PRINCE BY NICCOLO MACHIAVELLI 61-62 (1986).

2. See NICCOLO MACHIAVELLI, THE PRINCE 55-56 (Quentin Skinner & Russell Price trans., 1988) (1532) [hereinafter THE PRINCE].

3. See *id.* This theme was echoed recently by Robert J. Samuelson:
But while government earns our gratitude, it also stirs our resentment. Dependency creates a backlash. We detest the limitations, the conditions, the paperwork, the hassles and the occasional humiliations that accompany our benefits. We fear that benefits may be cut or modified. Even when they

This Article maintains that the welfare,⁴ retirement security, and national health care policies in the United States are the result of a Machiavellian balance of several factors. These factors include competition between the political parties; competing interests of certain powerful, narrowly focused groups; and public opinion, fueled on the one hand by perceived government generosity, and on the other by the adverse effect of that generosity on the populace. Underlying the Machiavellian balance is the effect of the overall economic climate of the country. Americans, even in the best of times, do not relish paying higher taxes. When any particular group benefits, such as the elderly or the poor, the government is perceived as being too generous.

In general, Americans are inclined to think in terms of how they can increase their personal wealth and possessions, rather than redistributing wealth to the poor and the less fortunate.⁵ In accordance with this philosophy of self-centeredness, Americans are more likely to be politically conservative. During periods of economic hardship, anxiety over personal financial stability and the prospect of suddenly joining the ranks of the needy provokes a realignment in the political spectrum. This shift may favor either liberal or conservative elements depending on which political party presided over the economic downturn. The primary concern arising at this point is change and whether the other political party could improve the economy. When the pendulum swings to the liberal side, it is generally not because of an overall concern for the poor and the less fortunate, but because change for personal financial betterment is of primary importance. This phenomenon of selfishness is reflected in the retirement, welfare, and national health

seem safe, we resist higher taxes to pay for other people's "unworthy" benefits. Paradoxically, government's very generosity helps make it unpopular. Government does so much for so many that anyone can find something that seems wrong or unneeded. My benefit is a public-spirited necessity; yours is ill-conceived waste.

Robert J. Samuelson, *Clinton's Nemesis*, NEWSWEEK, Feb. 1, 1993, at 51.

4. The term *welfare policy*, as it is used here, is intended to mean (1) the federal system of universal old-age pensions; (2) means-tested benefits for the poor; and (3) other programs included under the federal old-age benefits legislation such as Aid to Families with Dependent Children ("AFDC"), Medicare, Medicaid, etc. See *infra* part II.B.2 (discussing various welfare programs under Social Security legislation).

5. As evidence of this inclination, during the period from 1977 to 1989, the after-tax income of the wealthiest 1% of Americans rose by 102% while the after-tax income of the poorest 20% of Americans dropped by 9%. See *Social Security: Higher Taxes on Wealthy Could Pay for SSI Benefits Hike, Project Chairman Suggests*, Daily Tax Rep. (BNA) No. 173, at G-1 (Sept. 4, 1992) [hereinafter *SSI Benefits Hike*]. But see *infra* note 9 (giving examples where it would be advantageous for wealthy to be generous to poor).

policies of the United States.⁶ These policies are established and maintained by the government, but in a democracy, popular opinion often exerts great influence on public policies and legislation.⁷ Thus, in a democracy, “the Prince” is not the single omnipotent ruler envisaged by Machiavelli, because the governed play a greater role in a democracy, taking on a measurable portion of the Prince’s responsibilities for national policy. But the governed who play this greater role are not necessarily the people in general. Instead, the “people” who are most likely to influence policy and legislation are those who are powerful, well organized, and able to speak with a collective voice. These people generally have narrow, self-serving interests, and strive to maintain and expand their wealth and power.⁸ Generosity to the poor figures into this scheme only in a very narrow, self-serving sense.⁹ Otherwise, the poor are perceived as being unproductive and different and, therefore, not worthy of generosity.

While there have been studies indicating that politics and economic development are important to the development of welfare policies and to the redistribution of wealth,¹⁰ this Article charts new ground in attempting to overlay Machiavellian principles to those studies. The relationship is similar to that of macroeconomics

6. The term *selfishness* is used as a pejorative term in this context and is to be distinguished from the term *self-interest* as it is used in the context of law and economics. The latter term, as used by Adam Smith and his followers, has a positive connotation. For example, according to Smith, “[t]he habits of economy, industry, discretion, attention and application of thought, are generally supposed to be cultivated from self-interested motives, and at the same time are apprehended to be very praise-worthy qualities, which deserve the esteem and approbation of every body.” ADAM SMITH, *THE THEORY OF MORAL SENTIMENTS* 464 (New York, Garland Pub. 1971) (1759). Thus, under Smith’s theory, there must be some degree of self-interest in order for generosity to exist.

7. See generally CHARLES M. BRAIN, *SOCIAL SECURITY AT THE CROSSROADS* 5–25 (1991) (discussing theoretical relationship between public opinion and public policy).

8. An example of this is the opposition by the medical establishment to President Clinton’s national health care proposal. See, e.g., Kevin G. Salwen, *Labor Letter: A Special News Report on People and Their Jobs in Offices, Fields and Factories*, WALL ST. J., Sept. 21, 1993, at A1 (“Doctors grumble over the White House plan to revamp health care.”).

9. For instance, there may be circumstances in which it will be economically advantageous to display some generosity toward the poor; e.g., as a means of reducing the incidence of crime. See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 463–64 (1992) (“The criminal sector is in effect the employer of last resort.”). A display of generosity could also be advantageous to appease those who would otherwise rebel against the system that allows well-organized self-servers to amass power and wealth.

10. See KENNETH BRYDEN, *OLD AGE PENSIONS AND POLICY MAKING IN CANADA* 9–10 (1974).

to microeconomics. Underlying the national variables is basic human nature. In addition to being self-interested in the classic economic sense, people also tend to be selfish and self-centered. In the worst sense, we are prone to think of the universe primarily in terms of ourselves and how events affect us personally. Machiavelli used these elements of human nature to devise principles of calculated control.

This Article compares and contrasts the American and Canadian retirement, welfare, and national health care systems in light of Machiavellian principles. Although both countries have comprehensive welfare programs, the Canadian system is, on the whole, a much more humane, benevolent system. This Article maintains that the American systems remain inferior to the Canadian systems because of the force of the basic principles of human nature underlying the Machiavellian balance of political power. This force has not been as pronounced in Canada as it has been in the United States because of Canada's historical development and the dynamics of its political system, both of which have affected the general ideology and the attitude toward the poor.

Some might question the sagacity of using psychological principles to explain a problem that is perceived to be largely one of economics.¹¹ This Article maintains, however, that problems with the retirement, welfare, and national health (or lack thereof) systems stem from the characterization of the systems' problems by those who have something to gain. Thus, the American public is being manipulated in a Machiavellian sense.

This is not to say that these systems lack their share of problems—quite the contrary. The American retirement, welfare, and Medicare systems are appallingly ineffective and overly expensive. But the degree of specific problems may not be as severe as the public often is led to believe,¹² and the cure may not be the bitter pill it is portrayed to be.

This Article maintains that in order to fully comprehend the politics of welfare, retirement security, and national health coverage, it is necessary to examine Machiavellian principles in relation to the variables of economic development and inter-party competition. If the principles of Machiavelli are applied in a slightly differ-

11. For example, it has recently been predicted that the cost of a comprehensive national health care system could exceed \$100 billion a year. See Susan Brink et al., *Top 10 Health Stories to Watch*, U.S. NEWS & WORLD REP., May 10, 1993, at 81, 82.

12. See generally THEODORE MARMOR ET AL., AMERICA'S MISUNDERSTOOD WELFARE STATE: PERSISTENT MYTHS, ENDURING REALITIES 20-21 (1990) (attempting correction of popular misconceptions about social welfare programs).

ent and more constructive manner, they may facilitate reform of the American welfare, retirement, and national health systems.¹³ Now that the political balance in the United States has shifted from the conservative to the liberal, the time is ripe to consider reforming the entire Social Security system and instituting a comprehensive national health system.

Sections II and III provide a basic overview of the American and Canadian systems, respectively, and allow a direct comparison of the retirement, welfare, and national health systems of the two countries. This Article will limit its discussion of welfare policy to those programs which are a part of the public retirement system: Social Security in the United States and Old Age Security in Canada. Section IV examines the differences among the systems and attempts to explain these differences from a Machiavellian perspective. Section V discusses the political implications of the Machiavellian principles and how those principles may be used constructively to reform the American system.

II. RETIREMENT SECURITY IN THE UNITED STATES

A. *The Interconnection of the Policies of Welfare, Retirement Security, and National Health Care*

The American public and private retirement systems, along with private savings, collectively have been referred to as a "three-legged stool" of necessary financial support for the post-retirement years.¹⁴ But the existing legs of the stool are badly flawed, and it is missing the vital fourth leg: a comprehensive national health care system. Without this comprehensive national system, there can be no real retirement security for the majority of Americans. The United States is the only major industrialized nation without a comprehensive national system, yet it spends more than any other nation on health care.¹⁵ As a result of the combined effect of the high cost

13. *But see id.* at 1-21 (criticizing social welfare policy reformist mentality).

14. This term was coined by the President's Commission on Pension Policy appointed by President Carter. *See* FINAL REPORT OF THE PRESIDENT'S COMMISSION ON PENSION POLICY, COMING OF AGE: TOWARD A RETIREMENT INCOME POLICY, reprinted in *The Future of Retirement Programs in America: Hearing Before the House Select Comm. on Aging*, 97th Cong., 1st Sess. 105 (1981).

15. *See, e.g.*, Vincent Amoroso, *Retiree Medical Liabilities: Problems and Solutions*, 16 EMPLOYEE BENEFITS J., Sept. 1991, at 2, 3 (listing health care expenditures of six major countries as percentage of Gross Domestic Product); Sandra Hackman & Robert Howard, *Confronting the Crisis in Health Care: An Interview with Arnold Relman*, 92 TECH. REV., July 1989, at 30, 31 (stating \$550 billion spent on health care in 1989); Joseph S. Mallory, *Strategies for the 1990s*, 90 BEST'S REV., Apr. 1990, at 37, 37 ("Health care costs now account for about 12% of the gross national

of health care¹⁶ and the lack of a comprehensive national system, more than thirty-five million Americans—one-third of them children—have no health insurance coverage.¹⁷ In many cases, lack of health insurance coverage means lack of access to health care. Medicare, the only truly national health system in the United States, exists only for the elderly, and it is not comprehensive.¹⁸

The United States also spends more per capita on social welfare than any other country in the world.¹⁹ Yet the number of American families living in poverty increased last year to its highest level since 1964.²⁰ Many of those living in poverty are elderly women

product and roughly 8% of corporate payrolls.”).

16. For instance, health insurance premium costs rose an average of 15% in 1991. Since 1989 these costs have risen three times faster than inflation. See FOSTER HIGGINS, NATIONAL ASSOCIATION OF MANUFACTURERS, SURVEY ON HEALTH CARE REFORM AND COSTS: SUMMARY OF FINDINGS 23 (1992).

17. See Hackman & Howard, *supra* note 15, at 31, 34; see also EDWARD D. BERKOWITZ, AMERICA'S WELFARE STATE: FROM ROOSEVELT TO REAGAN 153 (1991) (discussing failure of Medicare to provide cost-effective health insurance for elderly citizens). This figure represents nearly 16% of the nonelderly population. See *Current Trends in Health Care Costs and Health Insurance Coverage: Health Care Reform Hearings Before Subcomm. on Health of the House Comm. on Ways and Means*, 103d Cong., 1st Sess. 12 (1993) (remarks of Nancy M. Gordon, Assistant Director, Human Resources and Community Development Division, Congressional Budget Office).

18. More than 70% of the nonpoor elderly purchase “Medigap” insurance policies to cover expenses not covered by Medicare. See Mark V. Pauley, *Medicare and the Health Care Costs of Retirees: Problems in Choosing the Future*, in SOCIAL SECURITY AND PRIVATE PENSIONS: PROVIDING FOR RETIREMENT IN THE TWENTY-FIRST CENTURY 149, 154 (Susan M. Wachter ed., 1988) [hereinafter PRIVATE PENSIONS]. For the poor, there is also Medicaid, but Medicaid is problematic. See *infra* note 75 (discussing limited availability of Medicaid).

19. The United States spends approximately 20% of its GNP on social welfare. See BERKOWITZ, *supra* note 17, at xii. While this figure is comprehensive and does not distinguish among the various welfare programs, this Article will confine its discussion of welfare primarily to those programs under the Social Security system. For a discussion of the distinction between the welfare state and social welfare, see MARMOR et al., *supra* note 12, at 82–127.

20. See Carrie Teegardin, *U.S. Poor Increase by 2 Million*, ATLANTA CONST., Sept. 4, 1992, at A1. The current population reports indicate that there are currently 35.7 million people living below the poverty line. *Id.* Almost half of all black children (46%) live in poverty. *Id.*

These statistics have been criticized, though, as misleading because they do not consider non-cash benefits to the poor. See MARMOR et al., *supra* note 12, at 96–97, 249–50 n.9. But poverty is a relative term, both socially and psychologically. Means-tested benefits are stigmatizing because they spotlight the recipient as being poor. See *infra* text accompanying notes 67–76.

While the methodology employed by the United States Census Bureau may be questioned, the bureau has always used the same indicator (reportable cash income). Thus, trends in the poverty level can be determined with relative accuracy even though on an individual level the poverty threshold can be criticized. Also, while federal expenditures for means-tested benefits increased 3.5 times between 1968 and 1988, most of this growth was in the early part of the period with very little growth

and minorities.²¹ The purpose of the American welfare state is not to eliminate poverty, but rather, to provide basic necessities and to insure against certain risks.²² Given the current cost of medical care, it is astounding that the United States does not provide comprehensive insurance against what has become the greatest of all risks.²³ In terms of efficacy, the problem of poverty in the United

during the late 1970s and 1980s. Moreover, means-tested expenditures account for less than 30% of all welfare spending. See MARMOR et al., *supra* note 12, at 92-94.

As far as cash assistance, there has been a significant decline in government spending under the AFDC program. See *id.* at 85 tbl. 4.2. Marmor gives the following reasons for the decline in government spending for the poor: (1) slow growth of the population of eligible persons; (2) tighter government budgets due to the stagflation, and strained government resources, particularly at the state level; and (3) the lack of federal mandate to provide AFDC benefits as a matter of right. See *id.* at 86-90. The latter reason has several interesting facets to which Marmor alludes. First, the 1960s represented a period of liberalism the likes of which this country has never seen before or since. Many of the federal and state programs for the poor were implemented during that period. See, e.g., Food Stamp Act of 1964, Pub. L. No. 88-525, 78 Stat. 703 (1964) (codified as amended at 7 U.S.C. §§ 2011-2030 (1988 & Supp. IV 1992)); Health Insurance for the Aged Act, Pub. L. No. 89-97, §§ 1901-1905, 79 Stat. 290, 343 (1965) (codified as amended at 42 U.S.C. §§ 1396-1396d (1988 & Supp. III 1991)). Afterward, the political climate of the country began to shift further to the right, profoundly affecting social assistance programs, in particular, and the welfare system in general. Second, cash assistance to the poor has always been problematic. As Marmor describes it: "[Cash assistance is] about the alleviation of suffering, largely without strings attached for those not expected to be in the workforce, but with plenty of strings attached for those who are expected to be self-supporting." MARMOR et al., *supra* note 12, at 90.

AFDC is one of the few cash assistance programs, but it is not intended to provide a new start. Rather, it is intended to insure workers and their families against certain economic risks, to alleviate the suffering of children, and to "maintain and strengthen family life." See 42 U.S.C. § 601 (1988) (authorizing appropriations). Beginning in the early 1970s, public opinion produced a shift in the focus of AFDC away from cash benefits at a time when the political focus of the country as a whole was shifting. See MARMOR et al., *supra* note 12, at 90. The war on poverty has failed because, by establishing welfare programs, the government "[was] not pursuing a political ideal that was particularly attractive to the mass of Americans. Establishing income support as a basic right of citizenship is not for most Americans a high priority." *Id.* The result has been devastating to the poor. See *id.* at 86-90.

For a discussion of cash and "nearcash" benefits and their effectiveness in reducing poverty, see *Sources of the Increases in Poverty, Work Effort, and Income Distribution Data: Hearing Before the Subcomm. on Human Resources of the House Comm. on Ways and Means*, 103d Cong., 1st Sess. 27-97 (1993).

21. See Camilla E. Watson, *The Pension Game: Age- and Gender-Based Inequities in the Retirement System*, 25 GA. L. REV. 1, 5 (1990) (discussing gender bias in coverage and benefits in both public and private retirement systems); see also M. Cindy Hounsell, *Winners and Losers: Pension Policy and Its Effects on Women* 2-3 (1991) (same) (unpublished manuscript, on file with the *Utah Law Review*). If the poverty rate was adjusted to exclude children, the elderly, women, and nonwhites, the overall rate would fall approximately 1.5 percentage points below the current official poverty rate. See MARMOR et al., *supra* note 12, at 112-13.

22. See MARMOR et al., *supra* note 12, at 124-25.

23. The apprehension of Americans over health insurance continues to rise. In a

States can be substantially alleviated with a comprehensive national health system.²⁴

One of the most successful federal programs to date for reducing the incidence of poverty in the United States has been Social Security.²⁵ The Social Security system consists of a variety of programs ranging from welfare to health insurance.²⁶ The success of

recent poll commissioned by the Employee Benefit Research Institute ("EBRI"), 68% of Americans polled indicated that health insurance coverage is the single most important employer-provided benefit. EMPLOYEE BENEFIT RESEARCH INSTITUTE, PUBLIC ATTITUDES ON THE VALUE OF BENEFITS 27 (1992) [hereinafter PUBLIC ATTITUDES]. Fifty-six percent of Americans polled indicated that they would not accept a job that did not provide health insurance coverage. *Id.* at 30; see Albert R. Karr, *Labor Letter: A Special News Report on People and Their Jobs in Offices, Fields and Factories*, WALL ST. J., Nov. 17, 1992, at A1. In another recent poll, 56% of Americans indicated that they would favor higher taxes for a national health system while only 37% would oppose higher taxes for such a system. See Tom Morganthau et al., *Close to Overload*, NEWSWEEK, May 10, 1993, at 32.

The consensus is that the federal government should implement some type of national health system. Beyond that, there is a difference of opinion as to the type of program to be implemented and how it should be financed. More than 200 bills seeking to establish a comprehensive national health system have been proposed. See S. 2817, 102d Cong., 2d Sess. (1992) (proposing comprehensive national health program); H.R. 5502, 102d Cong., 2d Sess. (1992) (proposing universal access to affordable health care and making health insurance available to all children); H.R. 200, 103d Cong., 1st Sess. (1993) (proposing framework for universal access to health care). The basic proposals center around four types of plans: (1) mixed management; (2) personally managed; (3) managed competition; and (4) government managed. See, e.g., H.R. 5936, 102d Cong., 2d Sess. (1992) (proposing system of managed competition). But see *Overview of CBO Scoring for Cost Savings Under Reform Proposals: Health Care Reform: Hearings Before the Subcomm. on Health of the House Comm. on Ways and Means*, 103d Cong., 1st Sess. 150-52 (1993) (statement of Robert D. Reischauer, Director, Congressional Budget Office) (reporting that managed competition may not reduce overall health costs). In addition, there have been some noncomprehensive bills. See, e.g., Universal Health Benefits Employment and Partnership Act, H.R. 30, 103d Cong., 1st Sess. (1993) (proposing universal access to group health benefits and providing incentives to private sector).

24. A comprehensive health system would stem rising medical costs, provide medical coverage for those without, and shift the financial risk in a more equitable manner. Such a system would, of course, involve adjustments to, or coordination with, Medicare, Medicaid, and other federal programs which provide medical benefits.

25. See MARMOR et al., *supra* note 12, at 98-103 (stating Social Security is most effective antipoverty success story); Alan S. Blinder, *Why Is the Government in the Pension Business?*, in PRIVATE PENSIONS, *supra* note 18, at 17-33 (discussing Social Security system from theoretical economic perspective).

26. The Social Security Act of 1935, Pub. L. No. 74-271, 49 Stat. 620 (1935), established the federal-state system of unemployment compensation, *id.* at 626 (codified as amended at 42 U.S.C.A. §§ 501-504 (West 1991 & Supp. 1993)). It also established AFDC, 42 U.S.C.A. §§ 601-617 (West 1991 & Supp. 1993), as well as other social services, e.g., unemployment compensation, *id.* §§ 501-504, and maternal and child welfare services, *id.* §§ 701-709. The act was later amended to include Supplemental Security Income ("SSI"), Pub. L. No. 92-603, 86 Stat. 1329, 1465 (1972) (codified as amended at 42 U.S.C.A. §§ 1381-1383c (West 1992 & Supp. 1993)), to pro-

the system in reducing poverty, however, is primarily attributable to the social insurance component of cash transfers to the elderly, disabled, and survivors of those insured under the system.²⁷ The Social Security system, however, was not designed to provide retirement security in the sense of a post-retirement continuity of living standards and, indeed, it has not. Instead, it provides merely a subsistence level benefit.²⁸ For true retirement security, one also needs investment income, private retirement income (usually from an employer-provided pension plan), and adequate health insurance.

In examining the current system of retirement security, it becomes readily apparent that the three-legged stool will probably not support the majority of Americans who reach retirement age in the twenty-first century. A comprehensive national health system is, at present, nonexistent. Moreover, it is debatable whether the Social Security system will remain solvent past the turn of the century.²⁹ It is well documented that Americans do not save enough, and that the United States has the lowest savings rate of any major industrialized country.³⁰ Furthermore, the private retirement system is an

vide means tested assistance to needy elderly people, *see infra* notes 67-76 and accompanying text, and Medicare, Pub. L. No. 89-97, 79 Stat. 290 (1965) (codified as amended at 42 U.S.C.A. §§ 426, 1395-1395ccc (West 1992 & Supp. 1993)). For a discussion of the events and underlying policies behind the various welfare programs under the Social Security system, see generally BERKOWITZ, *supra* note 17 *passim* (discussing events and underlying policies).

27. See MARMOR et al., *supra* note 12, at 101-03.

28. See BRAIN, *supra* note 7, at 31-33.

29. Although the social insurance portion of the system appears to be on fairly solid ground, the Hospital Insurance Trust Fund reportedly will be solvent only until around 1998. See *What's News—World-Wide*, WALL ST. J., Apr. 7, 1993, at A1. Furthermore, the Disability Insurance Trust Fund apparently will be exhausted sometime between 1995 and 1997. See *Projected Depletion of the Social Security Disability Insurance Trust Fund: Hearing Before the Subcomm. on Social Security and Family Policy of the Senate Comm. on Finance*, 102d Cong., 2d Sess. 2 (1992) (statement of Subcommittee Chairman Daniel P. Moynihan). In order to alleviate the fiscal problems of the Hospital Insurance Trust Fund, the Omnibus Budget Reconciliation Act of 1993 ("OBRA '93") has eliminated the wage base cap for hospitalization insurance taxes and has increased from 50% to 85% the maximum amount of Social Security benefits subject to income tax. See OBRA '93, Pub. L. No. 103-66, secs. 13207, 13215, §§ 3121, 86(a), 107 Stat. 312, 467, 475 (1993).

30. For the past eight years, the United States after-tax savings rate has ranged between four and five percent. See, e.g., Henry F. Myers, *Personal Saving Rate May Finally Recover*, WALL ST. J., Nov. 2, 1992, at A1. This Article is cautiously optimistic about the savings rate increasing in the future. Such confidence is based on a perceived future increase in wages, a dawning realization that one can no longer save through the increase in home values, and optimism that soaring health care costs can soon be contained. *Id.*

It is estimated that since 1980 the loss in wages to an average American family due to rising health costs has been \$8398. It is further estimated that the

appallingly ineffective system for its cost.³¹

Critics of the American retirement system have argued cogently from economic, logistic, and moral perspectives that the entire system, both public and private, needs reformation.³² With respect to the Social Security system, the primary obstacle to reform has been the threat of severe political repercussions which historically have quashed any major restructuring of the universal benefit portion of the system.³³ In order to comprehend the strength of this portion of the system and the relative vulnerability of the remainder, it is necessary to examine the various components of the entire system.

B. *The Social Security System*

The Social Security system was established under the Social Security Act of 1935³⁴ as a byproduct of the Great Depression. The system was designed originally as a system of social insurance,

average American family suffered the equivalent of a five percent pay cut in 1992 because of rising medical costs. The excess rise in health care costs since 1980 is estimated to be \$1.2 trillion. See Albert R. Karr, *Labor Letter: A Special News Report on People and Their Jobs in Offices, Fields and Factories*, WALL ST. J., Nov. 3, 1992, at A1.

Some have theorized that the private savings rate has been adversely affected by the Social Security system and by the private retirement system because of a false sense of financial security. See, e.g., Martin Feldstein, *Social Security, Induced Retirement, and Aggregate Capital Accumulation*, 82 J. POL. ECON. 905, 906 (1974). But see Steven F. Venti & David A. Wise, *The Saving Effect of Tax-deferred Retirement Accounts: Evidence from SIPP*, in NATIONAL SAVING AND ECONOMIC PERFORMANCE 103, 124 (B. Douglas Bernheim & John B. Shoven eds., 1991) (showing that IRAs have increased private savings rate).

For discussions of the effect of government borrowing and spending on the private savings rate, see Michael J. Boskin, *Deficits, Public Debt, Interest Rates and Private Saving*, in PRIVATE SAVING AND PUBLIC DEBT 255, 255-86 (Michael J. Boskin et al. eds., 1987) [hereinafter PRIVATE SAVING]; Luigi Paganetto, *Public Debt, Private Savings and Supply-Side Policies*, in PRIVATE SAVING, *supra*, at 298, 298-312; Rudolph G. Penner, *Government Deficits: The Case of the United States*, in PRIVATE SAVINGS, *supra*, at 105, 109-15.

31. See generally *The Illusory Promise of Retirement Security: Hearing Before the Subcomm. on Retirement Income and Employment of the House Select Comm. on Aging*, 102d Cong., 1st Sess. 1-3 (1991) [hereinafter *Illusory Promise Hearing*] (statement of Subcommittee Chairman William J. Hughes).

32. See, e.g., Nancy J. Altman, *Rethinking Retirement Income Policies: Nondiscrimination, Integration, and the Quest for Worker Security*, 42 TAX L. REV. 433, 437-38 (1987); Michael J. Graetz, *The Troubled Marriage of Retirement Security and Tax Policies*, 135 U. PA. L. REV. 851, 853-56 (1987); Deborah M. Weiss, *Paternalistic Pension Policy: Psychological Evidence and Economic Theory*, 58 U. CHI. L. REV. 1275, 1275-77 (1991). But see MARMOR et al., *supra* note 12, at 3-7 (arguing Americans are too reformist oriented).

33. See *infra* part II.C.1.

34. Social Security Act, Pub. L. No. 74-271, 49 Stat. 620 (1935) (codified as amended at 42 U.S.C. §§ 301-1397(f) (1988)).

guaranteeing a minimum benefit in order to rescue from poverty those on the borderline and to provide some assistance to others who needed it.³⁵ But the Social Security guarantees were based on the assumption that few people would derive anything from the system because, when the system was first implemented, the average life expectancy was less than sixty years.³⁶ Now, however, the average life expectancy is seventy-five years and rising.³⁷ Nevertheless, the Social Security system has become instrumental in reducing the incidence of poverty through two of its largest programs: Old-Age, Survivors, and Disability Insurance ("OASDI")³⁸ benefits paid to the elderly and to surviving dependents of insureds as well as to the disabled of all ages; and Supplemental Security Income ("SSI")³⁹ benefits paid to the needy elderly and others.⁴⁰ The success of these programs is such that they are much more efficient in reducing the incidence of poverty than any of the welfare programs targeted specifically at helping the poor.⁴¹ Moreover, the reliance on Social Security benefits continues to increase.⁴²

In addition to OASDI and SSI, the Social Security system encompasses a variety of other programs such as Medicare, Medicaid, and Aid to Families with Dependent Children ("AFDC"). The linchpin of the system, however, is OASDI.

35. President Franklin D. Roosevelt, under whose administration the Social Security Act was enacted, referred to the system as security against the "hazards and vicissitudes of life." See BERKOWITZ, *supra* note 17, at 13.

By all accounts, the 74th Congress understood little about the complex legislation it had passed. In the end, the Social Security Act was enacted because President Roosevelt wanted it. Roosevelt "had won a resounding vote of confidence in the 1934 congressional elections, [making] it possible for the Democrats to consolidate their hold over Congress." See *id.* at 15.

For a discussion of the constitutional basis for Social Security, see Robert M. Cover, *Social Security and Constitutional Entitlement*, in SOCIAL SECURITY: BEYOND THE RHETORIC OF CRISIS 69, 69-87 (Theodore R. Marmor & Jerry L. Mashaw eds., 1988) [hereinafter RHETORIC OF CRISIS].

36. See John Stossel, *Informed Retirees Back Entitlement Cuts*, WALL ST. J., Feb. 5, 1993, at A10.

37. *Id.*

38. See 42 U.S.C.A. §§ 401-433 (West 1991 & Supp. 1993).

39. See *id.* §§ 1381-1383.

40. Such benefits are also paid to the blind and to the disabled who are needy. *Id.* § 1382(a).

41. See MARMOR et al., *supra* note 12, at 154-61.

42. See *id.* at 154-56. At present, the collective entitlements of the Social Security system, excluding Medicare and Medicaid, constitute 21% of the federal budget. See David Wessel, *Want Some Tough Budget Cuts? OK, Pick Up an Ax and Try These*, WALL ST. J., Apr. 8, 1993, at A16. Medicare and Medicaid account for another 16%. *Id.* As of 1990, there were 133.6 million workers covered under the Social Security system. See JOSEPH S. PIACENTINI & JILL D. FOLEY, EMPLOYEE BENEFIT RESEARCH INSTITUTE, EBRI DATABOOK ON EMPLOYEE BENEFITS 161 (1992).

1. OASDI

By far the largest and most popular program under the Social Security system, OASDI consists of three parts: old-age benefits payable to the elderly regardless of need, survivors' benefits, and disability benefits payable regardless of age.⁴³ All citizens and legal residents⁴⁴ of the United States who have paid into the system for the required number of calendar quarters,⁴⁵ and who have reached age sixty-five,⁴⁶ are eligible for OASDI benefits. It is a mandatory system funded under a pay-as-you-go method in which current payments fund current benefits.⁴⁷ Direct funding for the program comes from a payroll tax imposed on wages up to a taxable wage base limit.⁴⁸ Because of the wage base limit, the employment tax system

43. See 42 U.S.C.A §§ 401–433 (West 1991 & Supp. 1993).

44. Note that while citizenship or legal residency is a prerequisite for receiving benefits, there is no residency or citizenship requirement imposed on the taxation of employment income for Social Security purposes. See I.R.C. § 3121(b) (1988 & Supp. IV 1992). This was the issue behind the withdrawal of the nomination of Zoe Baird, a Clinton nominee for U.S. Attorney General.

45. Calendar quarters are defined as three-month periods ending on March 31, June 30, September 30, and December 31. See 42 U.S.C. § 413(a)(1) (1988); see also *id.* § 413(a)(2)(B) (defining quarters that will not be credited).

Fully insured status generally requires a minimum of 40 calendar quarters, although disabled workers may be fully insured with a minimum of six quarters. See *id.* § 414(a). Even though not fully insured, a deceased worker may be considered to be currently insured if a minimum six-quarter coverage and other specified criteria are met. Currently insured status would entitle survivors of a deceased worker to reduced benefits. See *id.* § 414(b).

46. While 65 is currently the age for eligibility for full old-age benefits, see *id.* § 416(l)(1)(A), reduced benefits are available at age 62, see *id.* § 402(a). See also 42 U.S.C.A. § 402(q)(1) (West Supp. 1993) (discussing mechanics of benefit reduction). Special benefits are available at age 72 under very limited conditions for those otherwise unable to obtain coverage, but who have, nevertheless, worked for a relatively short period. See 42 U.S.C. § 428(a) (1988 & Supp. III 1991); 20 C.F.R. § 404.381–.382 (1993). Beginning in the year 2000, the retirement age will increase by increments of two months per year for the next six years so that by the year 2005, the retirement age will be 66. Then, beginning in the year 2017, the retirement age will again rise by two months per year for the next six years so that by the year 2022, the eligibility age will be 67. See 42 U.S.C. § 416(l)(1) (1988).

47. For discussions of the problems with this approach, see PHILLIP LONGMAN, *BORN TO PAY: THE NEW POLITICS OF AGING IN AMERICA* 1–85 (1987); James Tobin, *The Future of Social Security: One Economist's Assessment*, in *RHETORIC OF CRISIS*, *supra* note 35, at 41–68.

48. See I.R.C. § 3401 (1988 & Supp. IV 1992). The current Social Security taxable wage base for 1993 is \$57,600, 42 U.S.C.A. § 430 (West Supp. 1993), which reflects a three percent cost-of-living adjustment over the 1992 taxable wage base. The Medicare taxable wage base for 1993 is \$135,000, although the OBRA '93 repeals the wage base cap for wages and income received after December 31, 1993. Thus, after that date all wages will be subject to the Medicare tax. See I.R.C. §

is regressive, with wealthier individuals taxed on a smaller percentage of their earned income.⁴⁹ This means that there is essentially no vertical redistribution of income.⁵⁰ While an argument may be made that vertical redistribution does exist with respect to greater proportionate benefits directed to the lower class, there are, nevertheless, offsets to redistribution—such as the lack of a comprehensive health care program—which ensure that the lower class does not permanently benefit.⁵¹

There is, on the other hand, some horizontal redistribution because workers who retire before the end of the twentieth century stand to receive greater benefits than their younger counterparts who will retire in the twenty-first century.⁵² This phenomenon is attributable to the past rapid growth of the system, combined with the 1973 enactment of legislation indexing benefits.⁵³

Benefits are not provided at a flat rate, but vary according to the amount paid into the system and the length of time the individual has been insured. There is, however, a ceiling on the benefits an individual may receive annually.⁵⁴ Benefits are indexed according

3121(x)(2) (1988 & Supp. IV 1992). The rate for Social Security and Medicare is 7.65% (6.2% for Old Age, Survivors and Disability Insurance; 1.45% for hospital insurance) for both employers and employees, and 15.3% for self-employed, collected by withholding at the source. *See id.* §§ 1401, 3101, 3111. This duty is imposed on the payor, *see id.* § 3102, although self-employed are also subject to the withholding requirement. Employment income is taxed under either the Federal Income Contributions Act (“FICA”) or the Self-Employment Contributions Act (“SECA”).

49. Unearned income is exempted. For a more thorough discussion of the inequities attending the employment tax realm, see generally Graetz, *supra* note 32, at 864–74 (examining disproportionate tax burdens and effects of payroll tax on fringe benefits).

50. *See id.* at 855–56, 864–74; *see also* BRYDEN, *supra* note 10, at 2–3 (discussing redistribution of income in United States and Canada).

51. For instance, although the lower class may benefit from Medicaid, there are many gaps in its coverage. *See generally* MARILYN P. RYMER ET AL., MEDICAID ELIGIBILITY: PROBLEMS AND SOLUTIONS 33–123 (1979) (discussing inequities in coverage of persons in various social and economic circumstances).

52. For a discussion of the horizontal redistributive aspect of Social Security, see RHETORIC OF CRISIS, *supra* note 35, at 60–65.

53. *See* Act of July 9, 1973, Pub. L. No. 93-66, 87 Stat. 152 (codified as amended at 42 U.S.C. § 415 (1988 & Supp. III 1991)).

54. In calculating these benefits, the starting point is the determination of the primary insurance amount. There are several methods of determining this amount, but all are based on income and years of covered employment. In determining income, for years after 1950, the Social Security Administration looks to compensation, wages, self-employment income, and deemed military wage credits. *See* 20 C.F.R. § 404.211(a)(b) (1993). There is a ceiling on the amount of creditable earnings. *See* 42 U.S.C. § 415(e)(1) (1988). This ceiling corresponds to the maximum taxable wage base for FICA taxes. For a determination of the number of years used to calculate the primary insurance amount, using the average-monthly-wage method, *see* 20 C.F.R. §

to the Consumer Price Index with a stabilizer clause that provides for a lower cost-of-living adjustment based on a wage index in years in which (1) prices rise faster than wages; and (2) assets in the Social Security trust fund fall below a certain percentage of benefits paid during that year.⁵⁵ Up to age seventy, there is a limit imposed on the earnings of beneficiaries.⁵⁶ If this limit is exceeded, it will offset OASDI benefits dollar for dollar.

Dependents' benefits are available upon an insured's death, disability, or retirement. These benefits extend to spouses, minor children, and parents.⁵⁷ Eligibility for divorced spouse benefits, however, is based generally upon the recipient being unmarried, without regard to financial circumstances.⁵⁸ In the case of a surviving spouse without dependent children, there is an automatic disqualification if the survivor and the deceased were married less than nine months.⁵⁹

Although OASDI is the largest and most controversial program under the Social Security system, it is not a true program of social security because a true program would provide for a continuity of

404.221(c) (1993). There are also numerous circumstances in which benefits may be reduced. *See, e.g.*, 42 U.S.C.A. § 402(q) (West Supp. 1993) (listing circumstances in which benefit amounts for certain beneficiaries may be reduced); 20 C.F.R. § 404.290 (1993) (listing instances in which insurance amounts may be either increased or decreased through "recalculation").

55. *See* 42 U.S.C. § 415(i) (1988 & Supp. III 1991).

56. *See id.* § 403(f). *But see* S. 30, 103d Cong., 1st Sess. (1993) (proposing repeal of earnings test for individuals attaining retirement age); H.R. 1413, 103d Cong., 1st Sess. (1993) (same); H.R. 37, 103d Cong., 1st Sess. (1993) (proposing repeal of limitation for those who have attained retirement age with increase in exemption amount for those who have not).

57. *See* 42 U.S.C.A. § 402 (West Supp. 1993). For a discussion of problems of discrimination in spousal benefits, see Watson, *supra* note 21, at 29-30. *See also* S. 2635, 102d Cong., 2d Sess. (1992) (proposing equal division of earnings during marriage to recognize economic contribution of each spouse and ensure each will have Social Security benefits in own right); *Women and Social Security: Families Are Changing, the Workplace is Changing, Should Social Security Change Too: Hearing Before the Subcomm. on Social Security of the House Comm. on Ways and Means*, 102d Cong., 2d Sess. 30 (1992) (testimony of Nancy M. Gordon, Assistant Director, Human Resources and Community Development Division, Congressional Budget Office) (discussing issues of gender discrimination in benefits and coverage under Social Security system).

58. *See* 42 U.S.C.A. § 402 (West Supp. 1993). Note that in order to be eligible to receive spousal benefits, a divorced spouse must have been married to the insured for at least ten years preceding the date of the divorce. *See* 42 U.S.C. § 416(d) (1988).

59. *See* 42 U.S.C. § 416(c)(5) (1988). There are some exceptions to this rule for accidental death, death while on active duty in the military, and in cases in which the survivor had previously been married to the decedent for at least nine months and had subsequently divorced, then remarried. *See id.* § 416(k)(1), (2).

living standards after retirement. OASDI does not do this. Although its benefits are universal, in the vast majority of cases the level of benefits conferred is insufficient to maintain pre-retirement living standards.

2. Welfare Programs

The Social Security system also includes various welfare programs: AFDC,⁶⁰ SSI,⁶¹ disability insurance,⁶² unemployment compensation,⁶³ Medicare,⁶⁴ and Medicaid.⁶⁵ Unlike OASDI, whose benefits are universal, the welfare programs are social assistance programs⁶⁶ with no automatic across-the-board entitlement to protect them from attack. Instead, there is a means test employed.⁶⁷ This test represents a "divide and conquer" tactic that is both punishing and stigmatizing to its recipients. It is also a Machiavellian method of exerting control over the needy by isolating them from any natural support base that would provide them with a strong, united voice.⁶⁸

60. 42 U.S.C.A. §§ 601-617 (West 1991 & Supp. 1993).

61. *Id.* §§ 1381-1383.

62. *See id.* §§ 401-433. For a discussion of the development of disability benefits under the Social Security system, see BERKOWITZ, *supra* note 17, at 158-60.

63. *See* 42 U.S.C.A. §§ 501-504 (West 1991 & Supp. 1993).

64. *See* 42 U.S.C. §§ 426, 1395 (1988 & Supp. III 1991).

65. *See id.* § 1396.

66. While OASDI is not included under the welfare category, it is also a welfare program because most recipients will withdraw more from the system than they will ever pay in. In fact, those who retired more than ten years ago had recovered the entire sum they paid in, plus interest, within three years of retirement. *See* Stossel, *supra* note 36, at A10.

67. *See, e.g.*, 42 U.S.C.A. § 602(a) (West Supp. 1993) (AFDC); 42 U.S.C. § 1382 (1988 & Supp. III 1991) (SSI); *id.* § 1396 (Medicaid).

68. A similar tactic of control was espoused by Machiavelli in recommending the overthrow of the Turkish Kingdom:

It follows that anyone who attacks the Sultan of Turkey must expect to find the enemy united, and will be obliged to trust more in the strength of his own troops than in the disunity of his enemy. But if victory is achieved, and the defeat inflicted is so decisive that the enemy forces cannot regroup, there remains no other obstacle except the ruler's family. If they are wiped out, there is no other focus of resistance to be feared, since no one else enjoys any standing with the inhabitants. And just as the conqueror could expect no help from them before his victory, afterwards he will have no reason to fear them.

THE PRINCE, *supra* note 2, at 16.

Under the Social Security system, the isolation concept works in two ways. First, because there is no universal entitlement, there is no middle-class incorporation principle to protect these benefits. Second, because the poor are given some benefits, they are alienated from much of their natural support base, i.e., those who for moral or political reasons advocate a better life for the less fortunate. Consider,

For instance, the structure of the SSI program virtually ensures that the recipients retain their status as the poorest of the poor. The guaranteed yearly benefit under SSI is an amount which is less than the current federal poverty threshold.⁶⁹ In addition, there are punitive conditions attached to eligibility. For example, in order to be eligible to receive SSI benefits, recipients must have total assets no greater than \$2000 for single individuals, and \$3000 for couples.⁷⁰ A proposal is currently under consideration to increase these limits,⁷¹ but even this proposal is flawed because the suggested benefit increase is paltry and there is no proposed elimination or revision of the punishing means test. Thus, there is no incentive for the poor to better themselves.

Viewed as a Machiavellian tactic, however, the proposal is not as flawed as it first appears. In the best Machiavellian tradition, the limits increase proposal establishes a certain level of government generosity without being overly generous; that is, without improving the plight of the poor in any substantive sense.

Besides facing stigmatizing asset limits, if beneficiaries live with and receive aid from family members or friends, their benefits may be cut by one-third.⁷² Thus, the system operates to ensure

for instance, the difference in quality of federal support for the elderly, with their powerful lobby, versus support for the nonelderly poor. *But see* Douglas Dobson, *The Elderly as a Political Force*, in *AGING AND PUBLIC POLICY: THE POLITICS OF GROWING OLD IN AMERICA* 123, 140-41 (William P. Browne & Laura K. Olson eds., 1983) (espousing view that elderly, while influential in past, are no longer a unified political force and may be losing favored status).

69. *See More Benefits Urged For Poor People Who Are Elderly, Blind or Disabled*, ATLANTA CONST., Sept. 4, 1992, at A6 [hereinafter *More Benefits*]. The current federal poverty guideline annual income level is \$7143 for single individuals. *See* U.S. BUREAU OF THE CENSUS, CURRENT POPULATION REPORT: POVERTY IN THE UNITED STATES, at viii tbl. A (1992). SSI presently guarantees recipients a yearly income of \$5064. *See More Benefits, supra*.

70. *See* 42 U.S.C. § 1382(a)(3) (1988). In addition, the current limit on excess earned income is \$65 per month. *See id.* § 1382a (1988 & Supp. III 1991). A recent government report sponsored by the Social Security Administration suggests raising this limit to \$200 per month. *See SSI Benefits Hike, supra* note 5, at G-1 to G-2.

71. *See* H.R. 5991, 102d Cong., 2d Sess. (1992). A recent government report on the SSI program recommends raising this limit to \$7000 for individuals and \$10,500 for couples. This report also suggests increasing the earned income exclusion from \$65 to \$200 as a work incentive. *See SSI Benefits Hike, supra* note 5, at G-1 to G-5. There are also other bills under consideration. *See, e.g.*, H.R. 5695, 102d Cong., 2d Sess. (1992) (proposing to increase asset limit to \$10,000 for individuals and \$15,000 for couples); H.R. 899, 103d Cong., 1st Sess. (1993) (proposing increase in minimum assessed wage limit of domestic employees to \$200).

72. *See* 42 U.S.C. § 1382a(a)(2)(A) (1988); *see also* Kathy H. Trumbull, *Social Security Needs Overhaul, Says Panel*, ATHENS DAILY NEWS, Sept. 4, 1992, at 1A. A bill to eliminate this reduction in benefits was introduced in the House by Rep. Wayne Owens and as of this writing is under consideration by the House Ways and

that the poor remain poor and isolated as a group. It is analogous to a life support system rather than to a treatment for the disease.⁷³

This is consistent with Machiavelli's principles. To be considered overly generous would undermine the government, thus leading to its defeat, because those who must "foot the bill" for this generosity (i.e., the majority of the voters) would eventually resent the poor and despise the government.⁷⁴

Another Machiavellian tactic designed to isolate the poor from any effective support base is to structure welfare programs under the Social Security system so that they are the joint responsibility of the state and federal governments. Two problems are raised by this arrangement: difficulty in organizing strong support for the programs when the constituencies are broken up among the states, and difficulty in finding adequate funding at the state level.⁷⁵ The result has been a dramatic reduction in support for welfare programs during the last fifteen years.⁷⁶

Means Committee. See H.R. 5991, 102d Cong., 2d Sess. (1992).

73. Another problem is that the Social Security Administration is overworked and understaffed. This shortage results in a significant backlog in benefits applications. According to Arthur S. Fleming, chair of a panel recently appointed by the Social Security commissioner to study reform of the system, "[t]he 1993 budget would result in a backlog of disability cases of 1.4 million." Trumbull, *supra* note 72, at 1A.

74. According to Machiavelli, "[a] ruler must above all guard against being despised and hated; and being generous will lead to both. Therefore, it is shrewder to cultivate a reputation for meanness, which will lead to notoriety but not to hatred." THE PRINCE, *supra* note 2, at 57-58.

The issue of government generosity to the poor raises two issues: (1) cash assistance versus in-kind benefits, and (2) dependency. Cash benefits have long been controversial and regarded as a handout rather than an incentive. But, while cash transfers are only a small part of the welfare system, they have been more effective in reducing poverty than in-kind benefits. See MARMOR et al., *supra* note 12, at 96-104.

Another complaint about the welfare system is that it encourages dependency, whether the benefits are primarily in-kind or in cash. But as Marmor documents, the facts are otherwise. Amounts of cash assistance to the poor vary widely from state to state, but the facts do not indicate a migration of the poor into those states with higher cash assistance amounts. Similarly, when AFDC benefits increased, the unemployment level of young black men fell, and correspondingly, the level increased when the benefits declined. See *id.* at 104-14.

75. See MARMOR et al., *supra* note 12, at 80. For instance, Medicaid, which provides medical care to the indigent, is an optional program for the states. As of July 1991, only 36 states, plus the District of Columbia, had Medicaid programs. See PIACENTINI & FOLEY, *supra* note 42, at 319-20. Furthermore, the existing programs vary widely in eligibility requirements. As a general rule, persons qualifying for benefits under AFDC and SSI are automatically eligible for Medicaid, although coverage may be extended to others within limits of the federal guidelines. See *id.* at 319.

76. See MARMOR et al., *supra* note 12, at 53-81.

3. *Medicare*

The Medicare program was enacted as part of the Social Security system in 1965 under President Lyndon Johnson.⁷⁷ The enactment of Medicare represented the culmination of a battle that had been going on for nearly half a century.⁷⁸ Initially, a national health program had been proposed under the Social Security Act of 1935, but the program was not enacted at that time. The reason for this failure was two-fold. First, there was no adequate national health care structure that could be commandeered to support the system. In many rural areas, for example, there were few or no hospitals and a shortage of doctors.⁷⁹ Second, the medical community was suspicious of proposals to alter the health care system. Physicians felt reforms would harm their income, limit professional freedom, and cause a decline in the quality of health care.⁸⁰

After 1935, various efforts were made in support of a national health care system,⁸¹ but none were initially successful. By 1940, however, the New Deal policies had produced an upturn in the economy and the country had begun to enter a period of prosperity. Again, however, Machiavellian principles came into play. Because the majority of Americans were in better financial shape than in the previous five years, there was less Depression-era panic over personal financial stability, and thus less interest in altruistic social policies. In keeping with this theme, Congress, usually a barometer of public opinion, was reluctant to increase Social Security benefits.⁸²

Instead of a public health care system in which costs would be spread on an average basis across the population—providing accessible health care for everyone, as well as greater cost containment—the nation chose to retain a *laissez-faire*, private, com-

77. See Health Insurance for the Aged Act, Pub. L. No. 98-97, 79 Stat. 290 (1965) (codified as amended at 42 U.S.C.A. §§ 426, 1395-1395ccc (West 1992 & Supp. 1993)).

78. The early history of this battle is related in DANIEL S. HIRSHFIELD, *THE LOST REFORM: THE CAMPAIGN FOR COMPULSORY HEALTH INSURANCE IN THE UNITED STATES FROM 1932-1943*, at 15-41 (1970). See also BERKOWITZ, *supra* note 17, at 153-76.

79. "As late as 1945, a Senate subcommittee found that 40% of the counties in the United States lacked hospital facilities, and many of these also suffered from a shortage of physicians." BERKOWITZ, *supra* note 17, at 156.

80. See HIRSHFIELD, *supra* note 78, at 34-37.

81. See *id.* at 135-65 (discussing proposals such as Wagner Health Bill of 1939 and Lodge Proposal of 1940).

82. See BERKOWITZ, *supra* note 17, at 153-71; RHETORIC OF CRISIS, *supra* note 35, at 178-84.

munity-based approach.⁸³ Under this approach, those who could afford neither the cost of health care nor the cost of private insurance remained at the mercy of rising health care costs.

Finally, in 1965, after much political wrangling, Congress enacted Medicare and Medicaid as a part of the Social Security system.⁸⁴ The victory was short-lived, however, because it was not long before rapidly escalating costs began to get the better of the system. Other imperfections began to surface as well,⁸⁵ emphasizing the need for reform. In this regard, the history of Medicare reform converges with that of welfare reform because, although in both instances there appeared to be a public consensus on the need for reform, no serious efforts were made toward that goal.

There are two probable reasons for this lack of effort. The first is public apathy. The sentiment of average Americans is that welfare will have no direct effect on them because they never expect to be welfare recipients. Although people generally believe that something should be done for the poor and down-trodden, they are only willing to support programs accomplished with relatively little direct cost to the individual taxpayer.⁸⁶

In the case of national health coverage, however, there is an added dimension because medical care is perceived as highly personal. Given a choice between containing costs or having a choice of doctors and hospitals, the latter is frequently considered to be more important than the former.⁸⁷ Also, there has been strong, well-organized opposition to a national health care system by the insurance industry and the medical community, and this opposition has fed on the apprehensions of the public.⁸⁸

Second, the enactment of the Social Security system, with all its component parts, such as OASDI, AFDC, and Medicare, under-

83. For a discussion of the historical development of Medicare see BERKOWITZ, *supra* note 17, at 153-66.

84. See Health Insurance for the Aged Act, Pub. L. No. 98-97, 79 Stat. 290 (1965) (codified as amended at 42 U.S.C.A. §§ 1395-1395ccc (West 1992 & Supp. 1993)).

85. These faults were primarily attributable to the complexities of governmental regulation of the system and the lack of comprehensive coverage. See BERKOWITZ, *supra* note 17, at 180-86.

86. I believe that there is also probably some racism involved since many of the poor are ethnic minorities. Part of the apathy toward welfare generally, is that the poor are perceived as being different.

87. See, e.g., Memorandum from Fabrizio, McLaughlin & Assoc. to the United Seniors Ass'n, Inc. 7 (Jan. 25, 1993) [hereinafter Fabrizio Memorandum] (regarding the national survey of senior Americans' health care concerns).

88. See, e.g., *Health-Lobby Mania*, NEWSWEEK, July 5, 1993, at 38 (discussing opposition to health care reform by variety of groups). Note that these same groups also opposed both Disability and Medicare. See BERKOWITZ, *supra* note 17, at 164-68.

cut the moral argument of benefits for the needy. The needy *did* have benefits under the Social Security system even though the system itself was flawed. More important, however, was the fact that instead of real-life hardship cases to which the public could relate, the issues now involved statistical abstracts about which it was difficult to become impassioned.⁸⁹ Thus, like its welfare counterpart, Medicare reform died a quiet death.

C. *The Welfare State*

Edward Berkowitz, in his book *America's Welfare State*, described the developing welfare system as being "based in large part on indirect government subsidies—through tax policy—of private social benefits."⁹⁰ He goes on to say that "[t]his strategy fit the more general American model for social policy: the use of tax policy to manage the economy and encourage socially beneficial, yet privately controlled behavior."⁹¹

This strategy also fit the Machiavellian mold because the use of tax policy to encourage socially responsible behavior benefits the wealthy and powerful by maintaining their control. Tax benefits are of no use to the poor, although the poor may indirectly benefit from the use by the rich of some tax incentive devices, such as the deduction for charitable contributions.⁹² However, the rich retain control over the poor.

An example of this type of control is the use of tax benefits to encourage employers to dole out perquisites, such as health insurance, which may be used as an incentive device for recruiting and retaining employees. These benefits are not guaranteed, however, by the employer or by the insurer. If a worker changes jobs, as many workers are prone to do, there might be a decrease in, or an elimination of, health care coverage. Because there is no national pooling of medical costs or any other type of governmental restraint on costs, there is no protection against these rising medical expenses. Thus, a decrease in, or elimination of, health care benefits could be devastating if a worker or a member of her family becomes seriously ill.⁹³

From the employer's perspective, however, the provision of

89. See BERKOWITZ, *supra* note 17, at 179–80.

90. *Id.* at 160.

91. *Id.*

92. See I.R.C. § 170 (1988 & Supp. IV 1992).

93. This example does not address the situation of the unemployed, most of whom lack health insurance coverage and cannot qualify for Medicaid. See *supra* note 70 (discussing Medicaid eligibility).

health care coverage as an employee benefit is a significant competitive edge in the business world.⁹⁴ From a Machiavellian perspective, the absence of a national health care system could be regarded both as a necessary means of controlling the masses and as an efficient means of concentrating wealth and power in the hands of a few powerful lobbyists such as big business, the American Medical Association, and the insurance industry.

The Machiavellian strategy by which this concentration of power has been accomplished underscores the point. For instance, there are a variety of means employed to redistribute the cost of Medicare among the elderly.⁹⁵ The redistribution does not take into account, however, the ability of each individual recipient to pay.⁹⁶ As a result, the financial burdens are unequally distributed among the elderly.⁹⁷

In addition, Medicare does not cover many major expenses.⁹⁸ As a result, the majority of elderly Americans purchase "Medigap" insurance policies to cover these costs.⁹⁹ These policies are tax deductible,¹⁰⁰ thus subsidized by the taxpayers, resulting in a windfall to the insurance industry and further widening the disparity of financial burdens among the elderly population.

Such examples indicate that the United States has never been

94. For example, in a survey conducted by the EBRI, 68% of respondents regarded health benefits as the single most important employee benefit. The next most important benefit was pension coverage, trailing health benefits in importance by 55 percentage points. See PUBLIC ATTITUDES, *supra* note 23, at 27; see also Morganthau et al., *supra* note 23, at 32 (reporting that people would pay higher taxes to have comprehensive health coverage).

95. Medicare generally does not cover such costs as outpatient prescription drugs, homemaker services, custodial services, hearing aids, routine physicals, eye exams for glasses, and routine immunizations. See generally SUSAN HELLMAN & LEONARD H. HELLMAN, MEDICARE AND MEDIGAPS: A GUIDE TO RETIREMENT HEALTH INSURANCE 15-22 (1991) (discussing outpatient claims under Medicare).

96. For example, only 50-60% of health care costs are covered. Medicare does not begin to adequately cover the costs of long-term nursing home care or home health care. See *id.* at 23.

97. See RHETORIC OF CRISIS, *supra* note 35, at 183-84.

98. See 42 U.S.C. §§ 1395d-1395f (1988 & Supp. III 1991); see also HELLMAN & HELLMAN, *supra* note 95, at 15-22.

99. For a more in-depth discussion of options for covering Medicare gaps, see HELLMAN & HELLMAN, *supra* note 95, at 23-36.

100. See I.R.C. § 213(d)(1)(C) (1988 & Supp. IV 1992). The deduction is allowed to the extent that total allowable medical expenses exceed 7.5% of the taxpayer's adjusted gross income. *Id.* § 213(a). Obviously, the people who benefit the most from this provision are the elderly who are on fixed incomes. Note that higher income taxpayers are subject to the limitation on itemized deductions. *Id.* § 68. President Clinton earlier considered a scheme to tax employer-paid health insurance, but he has since backed away from this plan. See Susan Dentzer, *Clinton's Taxing Health Reform*, U.S. NEWS & WORLD REP., Jan. 18, 1993, at 66.

serious about a comprehensive national health care system. Another indication of this phenomenon is the fact that Medicare was enacted under the Social Security Act, a tax legislation. This means that it is under the auspices of the House Ways and Means Committee and the Senate Finance Committee. Thus, Medicare is susceptible to what has been termed a "double exposure" of budget deficit woes, "once from program reduction pressures and second, from revenue pressures."¹⁰¹ Because these committees are subject to revenue generating pressures, "they cannot be as strongly focused on protecting 'their' programs as other committees are."¹⁰²

1. *The Vulnerability of the Welfare State*

The United States was among the last of the major industrialized countries to establish a public Social Security system. The underlying post-Depression social and economic policies behind the American system were perhaps less altruistic than those of most other countries because the American system was implemented during the Great Depression, a time when most Americans considered themselves to be needy.¹⁰³ Thus, they perceived no discernible difference between themselves and the poor. The term *social security* is commonly used to refer to the OASDI program. For instance, the Social Security system has been called the "third rail" of American politics: "touch it and die."¹⁰⁴ In reality, this only refers to OASDI, because all other programs under the Social Security system are vulnerable.¹⁰⁵

Ronald Reagan was the first president to test the irony of the vulnerability and the invincibility of the Social Security system.

101. Katherine A. Hinckley & Bette S. Hill, *Biting the Bullet? Post-1980 Congressional Processes and Medicare Decisions*, in HEALTH INSURANCE AND PUBLIC POLICY: RISK, ALLOCATION, AND EQUITY 31 (Miriam K. Mills & Robert H. Blank eds., 1992).

102. *Id.* As proof of this point, during the early 1980's, these tax committees were responsible for between one-fourth and one-half of all cuts to domestic programs. *Id.*

103. Although it is the position of the neo-pluralists that welfare policy is largely determined by interest groups whose initial influence is generally to hinder the development of the welfare state, each group is more interested in securing benefits for themselves than in creating "a more centralized public program that distributes benefits to a larger part of the population." JOHN WILLIAMSON & FRED PAMPEL, OLD AGE SECURITY IN COMPARATIVE PERSPECTIVE 15 (1993). Because of this phenomenon, "national public pension systems have often been adopted earlier in less democratic countries." *Id.* at 15-16.

104. BRAIN, *supra* note 7, at 91.

105. Although OASDI, to this point, has been relatively invincible, only the Old Age benefit payments are protected under the middle-class incorporation theory. Survivors and disability benefits may well be cut at some future point.

One of his first acts as president was to push for the enactment of the Omnibus Budget Reconciliation Act of 1981 ("OBRA '81").¹⁰⁶ This legislation reversed the trend toward creation of a stronger welfare state by cutting benefits in many welfare programs.¹⁰⁷ There were cuts under other Social Security programs as well, but these cuts focused primarily on the politically vulnerable.¹⁰⁸

OBRA '81 also implemented a "clawback" system in which half of all OASDI benefits are subject to taxation.¹⁰⁹ What is more, President Reagan was successful in obtaining the enactment of this legislation in a Democratically-controlled Congress. But when the President proposed cutting middle class entitlements under OASDI, his public approval rating dropped sixteen points in a matter of days.¹¹⁰

Why such resounding initial success followed by such sudden and dramatic failure? One commentator theorizes that the reason for the relative invincibility of OASDI lies in the concept of "middle class incorporation," a solid alliance based on entitlement of the masses to benefits as a matter of right.¹¹¹ This concept rests on the theory that the working class has or will have contributed to the Social Security system throughout their careers. They have fulfilled their end of the bargain and upon meeting the other eligibility requirements,¹¹² they feel they have an absolute right to their promised benefits and no politician can take them away.¹¹³ This is ex-

106. Pub. L. No. 97-35, 95 Stat. 357 (1981).

107. For instance, benefits were cut or eliminated under such social assistance programs as the school lunch and child nutrition programs, *id.* § 801, Medicaid, *id.* § 2100, and the public-service jobs program, *id.* § 701.

108. *See id.* § 2201, at 830 (repealing minimum benefit provisions for low income workers); *id.* § 2210, at 841 (eliminating "child's insurance benefits in the case of children aged 18 through 22").

109. I.R.C. § 86 (1988). There is a minimum threshold amount so that lower income beneficiaries may escape tax liability. *Id.*

110. Jill Quadagno, *Interest-Group Politics and the Future of United States Social Security*, in STATES, LABOR MARKETS, AND THE FUTURE OF OLD-AGE POLICY 36, 36 (John Myles & Jill Quadagno eds., 1991) [hereinafter OLD AGE POLICY]. Such was the depth of public feeling and criticism by the elderly community that the Republican National Committee went to great lengths to influence the conduct and outcome of the 1981 White House Conference on Aging. For a discussion of the events leading up to and surrounding this conference, see HOUSE SELECT COMM. ON AGING, THE POLITICIZATION OF THE 1981 WHITE HOUSE CONFERENCE ON AGING, 98TH CONG., 2D SESS. (Comm. Print 1984).

111. *See* Quadagno, *supra* note 110, at 36-58 (citing PAUL LIGHT, ARTFUL WORK: THE POLITICS OF SOCIAL SECURITY REFORM 124 (1985)).

112. *See supra* notes 44-46 and accompanying text (discussing various eligibility requirements).

113. Many people consider social security to be an "insurance policy." Consider the statement of a 75-year old man interviewed by ABC's 20/20 for a program on

actly what President Roosevelt had counted on when he advocated universal benefits funded through payroll and self-employment tax deductions.¹¹⁴

The middle-class incorporation principle employed by President Roosevelt to protect the Social Security system also fits the Machiavellian model. He correctly surmised that casting the program solely as a welfare program would render it vulnerable to attack. As Dennis Guest states in discussing the Canadian counterpart to the American Social Security system: "It is virtually an axiom of social services experience that where social welfare programs are designed exclusively for 'the poor' they become second-rate services—often punitive and grudging in administration, invariably meager in benefit, and, above all, stigmatizing to the citizen who uses them."¹¹⁵

As a necessary measure to protect the new system, Roosevelt gave all citizens a stake in it so that any future critics would be faced with united resistance. This strategy proved successful. Although the system (often viewed as a program of unwarranted largesse) has been subject to constant attacks—the strongest occurring during the Reagan years—it has, nevertheless, withstood these attacks. Interestingly, the attacks themselves have been Machiavellian in nature, with most following the same two-part theme. The first part consists of portraying the elderly as "greedy geezers" who have no need of financial assistance, yet derive a steady income for life from the government (funded, of course, by the hard-working middle class), while also draining government resources through

entitlement cuts: "I'll never forget when it started . . . the first week they took 60 cents out of my salary. And I've been paying ever since. And I am never going . . . to give any of it back!" Stossel, *supra* note 36, at A10.

Another building block in the middle class incorporation concept is the bolstering of widows and widowers benefits under the 1972 amendments to the Social Security Act. *See* Social Security Amendments of 1972, Pub. L. No. 92-603, sec. 102, § 202, 86 Stat. 1329, 1335-39 (1972). These amendments, among other things, increased the old age benefits by 20%, and provided for a cost of living inflation index. Pub. L. No. 92-336, Sec. 201, § 215, 86 Stat. 406, 411-16 (1972).

One factor which evidently does not contribute to the middle class incorporation concept is the prospect of deriving more benefits than contributions. According to a recent Gallup poll published by the EBRI, 65% of workers expect to pay more into the system than they will receive. Another 21% expect to receive the same amount upon retirement that they contributed into the system. *See* EMPLOYEE BENEFIT RESEARCH INSTITUTE, PUBLIC ATTITUDES ON TAXATION OF EMPLOYEE BENEFITS, 1992, at 13, 18 (1993).

114. *See* BRAIN, *supra* note 7, at 1. However, current and future retirees will probably receive less in benefits than the amount they paid into the system. When this happens, there is likely to be serious dissatisfaction with the system because taxpayers could receive a better return investing their tax dollars on their own.

115. DENNIS GUEST, THE EMERGENCE OF SOCIAL SECURITY IN CANADA 159 (1985).

Medicare and, at the same time, contributing very little in return to the government, society, and the local community.¹¹⁶ The underlying message of this attack is that the ruler is too generous. In order to “package” this message to appeal to the masses, the elderly are portrayed as being “different” from the rest of the populace.¹¹⁷ This non-elderly populace is described as hardworking, productive, and middle-class.¹¹⁸ Its members could use some financial assistance as well, but their youth precludes governmental benefits.

This leads to the second part of the theme, the intergenerational equity argument, which is based on a moral hazard: younger workers will soon be forced to bear more than their fair share of tax burden to pay for the retirement of the elderly population, many of whom, ostensibly, are financially secure and do not need Social Security benefits.¹¹⁹ One commentator has noted that “[t]he old have come to insist that the young not only hold them harmless for their past profligacy, but sacrifice their own prosperity to pay for it.”¹²⁰

Current retirement policy is likely to exacerbate the intergenerational equity problem because it produces a tendency toward early retirement.¹²¹ There are a number of commentators

116. Carroll L. Estes, *The Reagan Legacy: Privatization, the Welfare State, and Aging in the 1990s*, in OLD AGE POLICY, *supra* note 110, at 59, 59–77. A recent study has shown, however, that while the elderly pay less federal income taxes than other groups, their federal tax burden has risen by 10% since 1977 because of the effect of other federal taxes. Also, the effect of state sales and property taxes on the elderly is disproportionate to that of the wealthiest citizens. See BRUCE FISHER & ART LYONS, NATIONAL COUNCIL OF SENIOR CITIZENS, A MATTER OF EQUITY: A STUDY OF TAXES AND INCOMES OF THE ELDERLY, at v–vi (1993).

117. See, e.g., Quadagno, *supra* note 110, at 44–49 (discussing the generational equity debate).

118. See Lee Smith, *The War Between the Generations*, FORTUNE, July 20, 1987, at 78–82.

119. See LONGMAN, *supra* note 47, at 27–35, 258–62; Quadagno, *supra* note 110, at 44–49. Because of the baby boom phenomenon, the ratio of elderly to nonelderly persons around the year 2040 will be approximately one to three. See OFFICE OF THE ACTUARY, SOCIAL SEC. ADMIN., SOCIAL SECURITY AREA POPULATIONS PROJECTIONS, ACTUARIAL STUDY No. 57 tbl. 18f (1983).

120. See Quadagno, *supra* note 110, at 45 (quoting Phillip Longman, *Taking America to the Cleaners*, WASH. MONTHLY, Nov., 1982, at 24). The logic behind the concept of intergenerational equity is that the system is funded on a pay-as-you-go basis rather than by advance funding. This means that current benefits are funded through current contributions. Because of the baby boom phenomenon and the increasing life expectancy of the elderly, the portion of the population over age 65 is likely to increase significantly by the middle of the next century. This, in turn, is likely to produce a tension as younger workers are expected to support the elderly retired workers through contributions to the Social Security system.

121. For a discussion of this trend, see LAURENCE J. KOTLIKOFF & DANIEL E. SMITH, PENSIONS IN THE AMERICAN ECONOMY 16–19 (1983). See also Harold L.

who do not believe that the system will be readily able to support such a glut of retirees.¹²²

But while the most vociferous critics decry the Social Security system as a welfare program for the rich,¹²³ they also regard it largely as politically invincible. Even so, politicians continue to cast benefit reductions as a panacea for federal deficit problems.¹²⁴ To date, however, efforts to reduce benefits under the OASDI have met with united and adamant opposition.

So why was President Reagan initially successful in attacking the Social Security system? There were several reasons. First, the attack focused on the poor, a politically vulnerable group. There was

Sheppard, *The "New" Early Retirement: Europe and the United States*, in *THE AGING OF THE AMERICAN WORKFORCE* 158, 158-78 (Irving Bluestone et al. eds., 1990) [hereinafter *AMERICAN WORKFORCE*] (noting trend toward early retirement).

122. See, e.g., John D. Owen, *An Aging Work Force? The Dog That Didn't Bark*, in *AMERICAN WORKFORCE*, *supra* note 121, at 57, 57-68 (analyzing why work force has not aged); John R. Stepp, *Older Workers: New Problems, New Opportunities*, in *AMERICAN WORKFORCE*, *supra* note 121, at 31, 31-36 (proposing early retirement trend be reversed by adapting the workplace to accommodate older workers).

To alleviate some of the concern over the intergenerational equity problem, House Ways and Means Committee member Rep. William Thomas has introduced legislation that would reduce Social Security taxes and allow workers to use their Social Security contributions to create individual retirement accounts. See H.R. 5159, 102d Cong., 2d Sess. (1992). The employer's portion of the contribution would go into Social Security individual retirement accounts. *Id.* Thus, workers would have more psychological security since they would have a greater degree of control over the funds, and they would know, with certainty, how much they had available in their accounts.

123. See LONGMAN, *supra* note 47, at 240. But see JOHN GIST, *AMERICAN ASS'N OF RETIRED PERSONS, ENTITLEMENTS AND THE FEDERAL BUDGET DEFICIT: SETTING THE RECORD STRAIGHT* 1, 9-10 (1993) [hereinafter *AARP REPORT*]. According to the AARP, the argument that Social Security disproportionately benefits the wealthy is misplaced. The AARP's theory is twofold: (1) "[n]early 75 percent of Social Security and Medicare benefits are received by households with pre-transfer incomes below \$20,000. On the other hand, less than 2 percent of Social Security and Medicare benefits go to households with incomes over \$100,000"; and (2) the middle and upper income non-elderly taxpayers disproportionately benefit from tax breaks, particularly from the three largest tax expenditures: the exclusion of pension contributions from gross income, deductibility of home mortgage interest, and the exclusion of employer contributions for medical insurance. *Id.* at 10. Tax incentives essentially amount to entitlements because "they are available automatically to anyone who qualifies and applies for them, and because they confer benefits just as spending programs do." *Id.* at 1.

124. See James Tobin, *The Future of Social Security: One Economist's Assessment*, in *RHETORIC OF CRISIS*, *supra* note 35, at 42, 44-47. Indeed, the recurring theme is that the federal budget deficit can be controlled through the use of funds accumulating in the Social Security trust fund. The fact is, however, that although the budget deficit has grown as a percentage of the gross domestic product from less than 1% in the 1960s to 4.2% in the 1980s, entitlements have not grown. *AARP REPORT*, *supra* note 123, at 3.

no middle class incorporation principle to protect the welfare programs. The second reason was much more complex. From the inception of the Social Security program in 1935, until the late 1960s and early 1970s, there was a "constructive period" of establishing and fine-tuning the welfare state. OASDI, the universal retirement benefit portion of the system, was relatively stable during this time.¹²⁵ In the late 1960s and early 1970s, however, several factors coalesced to bring about a prevailing change in attitude toward the American welfare state. One was the fact that although the period from 1935 through the late 1960s represented a period of post-war economic boom, Americans nevertheless remained concerned about financial security in the aftermath of the Great Depression.¹²⁶ In the late 1960s and early 1970s, the economic climate began to change for the worse and the United States entered a period of stagflation, and then inflation.¹²⁷

These changes in the economy effected a change in the political climate with a shift from liberal to conservative. It has never been part of the conservative ideology to encourage the welfare state and, in keeping with that theme, the conservatives and neoconservatives have made the destruction of the welfare state a distinct part of their agenda.¹²⁸ Because a large portion of this attack has centered on the Social Security system, it has had a profound effect on retirement policy.

The most successful attack on the system has been based on its financial instability.¹²⁹ This attack has been successful because it was based initially on fact.¹³⁰ Prior to the early 1980s, there was a shortfall in the Social Security trust fund, due primarily to the federal government borrowing from that fund.¹³¹ This deficit was expunged by legislation enacted in early 1983.¹³² The 1983 legis-

125. See RHETORIC OF CRISIS, *supra* note 35, at 55-58.

126. For a discussion of the historical development of Social Security, see BERKOWITZ, *supra* note 17, at 13-65.

127. For a discussion of the effect of the economic climate on the Social Security system, see *id.* at 66-81; MARMOR et al., *supra* note 12, at 48-55.

128. See, e.g., Quadagno, *supra* note 110, at 44-49.

129. *Id.*

130. See *supra* note 29 (discussing solvency concerns with Hospital Insurance Trust Fund).

131. For a discussion of the economic effect, see MARMOR et al., *supra* note 12, at 128-74.

132. See Social Security Amendments of 1983, Pub. L. No. 98-21, 97 Stat. 65. However, this legislation addressed the foreseeable financial problems of the system. There are other problems which have arisen since that may not have been foreseeable. For example, the Treasury Department has credited more than \$9 billion to the Social Security trust fund, yet this amount is not supported by the records of the Social Security Administration. See Scott R. Schmedel, *A Special Summary and Fore-*

lation alleviated the funding deficiency, however, by cutting benefits rather than by spreading the shortfall evenly across the middle and upper income groups.¹³³

A major fault of the Social Security system is that the heaviest burden for the funding responsibility is borne by the middle class.¹³⁴ While the tax rates have increased steadily and will continue to do so,¹³⁵ benefits have been cut. Thus, insureds are paying more and receiving less. Perhaps, this could have been avoided if higher income individuals assumed a fairer share of the Social Security tax burden. By at least one account, however, the system is now in strong financial shape and is likely to remain that way.¹³⁶ The neoconservatives would have us believe otherwise, but there is no indication that their ideology has prevailed. President Reagan's contribution to the Machiavellian development of the welfare state was the Medicare Catastrophic Coverage Act of 1988.¹³⁷ This Act significantly expanded medical benefits for the disabled, the elderly poor, and poor women and children.¹³⁸ The problem was that funding for these benefits was to be primarily the responsibility of the

cast of Federal and State Tax Developments, WALL ST. J., Oct. 21, 1992, at 1; see also *infra* note 143 (discussing government borrowing against Social Security surplus).

133. See *supra* note 46 (discussing reduction of benefits due to gradual increase in retirement age); see also Graetz, *supra* note 32, at 861-74 (discussing inequities in Social Security payroll tax).

134. See Graetz, *supra* note 32, at 868-74. Although there is a ceiling on the amount of wages subject to the FICA tax, there is no floor. Thus, the employment tax places the heaviest burden on the working poor. See *id.* at 864-68.

135. For a discussion of the structure and growth of the payroll taxes, see *id.* at 861-64.

136. See, e.g., TREAS. DEPT., REPORT ON THE TAXATION OF SOCIAL SECURITY AND RAILROAD RETIREMENT BENEFITS IN CALENDAR YEAR 1990, at 2 (1993); David M. Walker, *The Financial Status of the Social Security and Medicare Programs (1990)*, 16 EMPLOYEE BENEFITS J. 36, 38 (1991) ("Based on current law and last year's projections, this program is well financed for many years into the future."). But see Schmedel, *supra* note 132, at 1 (discussing unrecorded nine billion dollar credit to Social Security trust fund).

Also, while the system is fiscally strong for the time being, it is feared that a shortfall might arise around the year 2020 when the bulk of the baby boomers retire. See BRAIN, *supra* note 7, at 86-90.

137. Pub. L. No. 100-360, 102 Stat. 683, amended by Pub. L. No. 100-485, 102 Stat. 2343, 2413-25 (1988) (codified at scattered sections of 42 U.S.C. 1395a-1395zz (Supp. III 1991)).

138. For example, the Act extended nursing home coverage from 100 days to 150 days, provided "long-term hospital care, . . . prescription drug benefit for medication not covered by preexisting Medicare policies, mammography screening, hospice care, and caregiver support for anyone caring for a sick relative; and the extension of Medicaid benefits to poor pregnant women and infants." Quadagno, *supra* note 110, at 49.

middle class elderly, those to whom the Act was directed.¹³⁹ This lowered the benefit-to-cost ratio because the costs would be concentrated among a smaller portion of the population. It also created a sore spot with the elderly population, worsened by the fact that most of the middle class elderly did not benefit significantly from the legislation.¹⁴⁰ Just sixteen months after the enactment, in response to tremendous lobbying efforts by the middle class elderly, the House voted to repeal much of the legislation and the Senate quickly followed suit, repealing the surtax and all benefits under the Act except the long-term hospital care.¹⁴¹

Not only was the repeal of this legislation devastating to the poor and the disabled, who are most in need of the benefits, it was also devastating to the American public because this Act had represented the "deferred agenda in health care."¹⁴² Thus, President Reagan was successful not only in undermining support for the largest expansion of the Medicare program since its inception in 1965, but he also was successful in providing fuel for the neoconservatives' fire against comprehensive national health coverage.

D. The Economics of Reform

The Social Security system is funded under a pay-as-you-go method in which those who are currently employed fund benefits for

139. In 1990, the elderly were to have paid a \$37.50 surtax for every \$150 in income tax up to a ceiling of \$800. By 1993, this surtax was scheduled to increase to \$42 with a ceiling of \$1050. Pub. L. No. 100-360, § 111, 102 Stat. 683, 689-91 (1988). This was a substantial cost for middle-income elderly taxpayers, many of whom were on fixed incomes.

140. Because of previous gaps in Medicare coverage, a large portion of older people either purchased or received from their employers "Medigap" policies from private insurance companies. These policies pay benefits similar to those the Catastrophic Coverage Act would have covered. Additionally, these medigap policies fill many of the holes in health care coverage that the new legislation would not have filled.

The new legislation also offered no protection against the astronomical costs of extended nursing home care. The only present source of public funding for such care is through Medicaid, a means and asset tested social assistance program in which eligibility depends on impoverishment. Thus, the elderly must spend down their income and assets to the poverty level in order to qualify. Under the new legislation, the middle and upper income elderly taxpayers would have had to pay increased taxes for insurance coverage that they did not need, while not receiving any major benefit that they did need.

141. See Medicare Catastrophic Coverage Act of 1989, Pub. L. No. 101-234, 103 Stat. 1979, 1979-86 (codified in scattered sections of 42 U.S.C. §§ 1395a-1395zz (Supp. III 1991)).

142. See Quadagno, *supra* note 110, at 49.

those who are currently retired.¹⁴³ From an economic perspective, there are advantages to such a funding method but there are also disadvantages.¹⁴⁴ For instance, such a method requires close monitoring of demographic factors in order to regulate the contribution rate.¹⁴⁵ An obvious factor leading to such an adjustment is a declining birth rate. While the pay-as-you-go funding method may have been appropriate in the late 1930s when the Social Security system was first conceived, it ceased to be appropriate in the late 1960s and early 1970s, and possibly prior to that time when the effect of the baby boom phenomenon became documented.¹⁴⁶ At that time, the system should have switched to a capital reserve system, a nonredistributional funding method in which contributions are accumulated to fund benefits for those paying into the reserve.¹⁴⁷ If that had happened, the system probably would be in a stronger financial position today. Now, it is virtually impossible to switch funding methods, although perhaps it may be done in the future after the baby boomers have passed on.

As it is, the economics of the system are vulnerable to attack in several respects. First, consider the intergenerational equity argument where taxes are disproportionately levied in order to maintain the system. This argument focuses on long-term inequities. Second, because of legislation enacted in 1983 to alleviate the deficit under the Social Security trust fund, there is currently a surplus in Social Security assets. But this is a short-term dilemma. To those sea-

143. For a discussion of this method see CONGRESSIONAL QUARTERLY, INC., SOCIAL SECURITY AND RETIREMENT: PRIVATE GOALS, PUBLIC POLICY 7-42 (1983). *But see supra* notes 50-53 and accompanying text (discussing redistributional aspect of Social Security system). There is some build-up of funds in order to pay benefits to the retiring baby boomers in the twenty-first century but the system remains predominately a pay-as-you-go system because current tax payments are used to pay current benefits. Because of the 1983 legislation, the system is currently running a surplus. The government has been using this money in its operating budget and has been issuing IOUs to the Social Security trust fund. *See* Kenneth L. Heaton, *Social Security Reserves Need to Be Invested Wisely*, ST. PETERSBURG TIMES, Aug. 18, 1989, at 2. The problem is that the IOUs are only as good as the financial condition of the government which, to date, has not been good. The surplus is not in a marketable security that can be sold when funds are needed in the future. Nor is there an investment that would stimulate capital formation and productivity gains. *See id.*; *see also* Paul C. Roberts, *Social Security Fairy Tale*, WASH. TIMES, Sept. 13, 1989, at F3.

144. *See* H.A.A. Verbon, *Conversion Policies for Public Pension Plans in a Small Open Economy*, in THE POLITICAL ECONOMY OF SOCIAL SECURITY 83, 93-95 (Bjorn Gustafsson & N. Anders Klevmarken eds., 1989).

145. *Id.* at 83-85.

146. *Id.*

147. Although this was no simple matter, some have speculated that it could have been done. *See, e.g.*, H.A.A. Verbon, *The Rise and Evolution of Public Pension Systems*, 52 PUB. CHOICE 75, 75-100 (1987).

soned advocates of the "quick fix," the surplus has been a very tempting source of funds with which to halt the alarming growth in the federal budget deficit.¹⁴⁸ The question is how to avoid the political hurdles erected nearly sixty years ago by President Roosevelt.

The argument goes like this: because debt service on the federal budget deficit and entitlement payments under Social Security and other federal entitlement programs are growing by leaps and bounds each year,¹⁴⁹ there will soon be little left over in the budget for maintenance and expansion of infrastructure, including education. The issue is often phrased in terms of a crossroads for Americans: higher taxes to support growing entitlements, or cuts in those entitlements.¹⁵⁰

There are, however, alternative considerations, such as the elimination of the mandatory retirement age under the Age Discrimination In Employment Act of 1967.¹⁵¹ As a result of this legislation, employers cannot force employees to retire solely on the basis of age.¹⁵² While it is yet too early to determine what effect this will have on the workforce, there are some predictions that can be made. With advancements in medical technology, better nutrition, and general health habits, people are living longer and their quality of life has improved. Those workers who are more highly paid and generally have more marketable skills are likely to retire from their primary career somewhere between the ages of sixty and seventy.¹⁵³ Nevertheless, they are likely to continue working part-time or in some advisory capacity, particularly if their jobs are not physically demanding.¹⁵⁴

148. In order to provide some protection to the system, Social Security trust funds are now "off budget," and must be accounted for separately. They are exempted from general budgetary spending limitations and are not available for net lending. See Social Security Amendments of 1983, Pub. L. No. 98-21, secs. 710, 347, § 203(F)(3), 97 Stat. 65, 137-38.

149. Entitlement spending currently constitutes half of the federal budget and is predicted to consume 14.2% of the economic output of the United States by the turn of the century. See *Target the Sacred Cow of Entitlements*, BUS. WK., Sept. 7, 1992, at 106. However, most of the increase in entitlement spending is attributable to health costs. See AARP REPORT, *supra* note 123, at 7-8. But see *supra* note 124 (discussing fact that entitlement spending has not increased as percentage of gross domestic product).

150. See Mike McNamee & Susan B. Garland, *Can't Live With 'Em, Can't Live Without 'Em*, BUS. WK., Sept. 7, 1992, at 74.

151. Pub. L. No. 90-202, § 4, 81 Stat. 602, 603-04 (codified as amended at 29 U.S.C. § 623 (1988 & Supp. IV 1992)).

152. 29 U.S.C. § 623 (1988 & Supp. IV 1992).

153. At least, this has been the trend. See JAMES H. SCHULZ, *THE ECONOMICS OF AGING* 69 (1988).

154. Note, though, that this theory is contrary to the 1987 findings of the

This post-retirement employment will alleviate any potential financial problems they might encounter in their post-retirement years. On the other hand, those who are paid less usually have less marketable skills, and likely will have fewer opportunities available to them in later life to continue working.

These factors indicate that post-retirement employment compensation will be an increasingly important source of income for the elderly because most of the elderly probably will remain in the workforce in some capacity.¹⁵⁵ Those who are likely to retire completely from the workforce will be those who are ill or disabled and those who perform arduous tasks for menial wages. In other words, those for whom the differential between current wages and Social Security benefits is slight.

1. *The Poverty Underclass*

An exception to the latter group is the underclass of workers not covered under the Social Security system. Over ninety percent of American workers are covered under the Social Security system.¹⁵⁶ The original legislation, however, excluded certain categories of workers from coverage for a variety of reasons.¹⁵⁷ Among those excluded were agricultural workers and domestics. The reason articulated for the exclusions was the administrative burden of collecting the tax.¹⁵⁸ Eventually, mandatory coverage was extended to these workers under the 1950 Social Security Amendments.¹⁵⁹

Spencer Report which concluded that the early retirement trend has continued relatively unabated despite the illegality of mandatory retirement. *Id.* at 83-84.

155. According to the Bureau of Labor Statistics, there has already been an increase in the number of employed people aged 65 and older. In 1985, 10.4% of the elderly were employed, while in 1990 the percentage of elderly workers had increased to 11.5%. See Aurora M. Armstrong, *Workable Solutions; Labor: Many Senior Citizens Are Returning to the Job Market, Often For Personal Satisfaction—And Employers Are Finding Them A Valuable Resource*, L.A. TIMES (Ventura County ed.), Aug. 16, 1990, at J10.

One frequently raised issue is the effect on the job market for younger workers if the elderly remain in the workforce. It is difficult at this point to predict what impact this will have because there will be relatively fewer younger people and technology may make many advancements. Thus, some jobs may be eliminated and others may be created.

156. See BRAIN, *supra* note 7, at 37 (stating 93% of workers were covered during 1989).

157. *Id.* at 48.

158. *Id.* A less articulated reason is that southern Congressmen insisted on the exclusion of agricultural workers and domestic servants in order to maintain control over tenant labor. See WILLIAMSON & PAMPEL, *supra* note 103, at 95-96 (1993).

159. Pub. L. No. 81-734, 64 Stat. 477 (1950) (codified at I.R.C. § 3121(a)(7)(B))

For many of these workers, however, such coverage exists in name only. By law, an employer must withhold Social Security taxes on income paid to an "employee" who receives compensation of at least fifty dollars in a calendar quarter.¹⁶⁰ The term "employee," however, is a slippery slope for employers as well as employees because it is nebulous and somewhat malleable.¹⁶¹ In many cases, there may be a fine line between an employee and an independent contractor, particularly with casual employees such as babysitters, gardeners, and maids. Where ostensible employers hire only one or a few people, those employers might not consider themselves to be in a trade or business.

In many cases, however, the Internal Revenue Service may consider those workers to be employees, thus subjecting the employer to liability for tax under the Federal Insurance Contributions Act ("FICA").¹⁶² Since abuse in this area is great,¹⁶³ employees will probably be able to find work with an employer who does not take the withholding obligation seriously, who is afraid of losing the employee, who feels incompetent to deal with the administration of withholding, or who is not fully aware of the law.

If an employer does take the obligation seriously, the employee may threaten to quit work if the employer reports the income because many of the ostensible employees in this category are poor and view the withholding obligation as depriving them of much-needed current income. In addition, reporting the income may cause other problems for the employees such as revealing the fact that they are illegal aliens or causing them to be disqualified for welfare,

(1988 & Supp. IV 1992)).

160. See I.R.C. § 3121(a)(7)(B) (1988 & Supp. IV 1992). If an employer pays wages to a domestic employee of \$1000 or more during a calendar quarter, the employer may also be liable for federal and state unemployment contributions tax. *Id.* § 3306(a)(3).

161. See James H. Ditkoff, *Withholding and Employment Taxes: Practices, Penalties, and Questions of Policy*, 37 N.Y.U. INST. FED. TAX'N §§ 30-1, 30-11 to -15 (1979) (discussing complexities and inequities in classification and administration). The IRS has attempted to resolve some of the ambiguities in this area with its 20-factor analysis. See Rev. Rul. 87-41, 1987-1 C.B. 298-300; see also Dave N. Stewart & John L. Kramer, *An Empirical Answer to the Problem of Determining "Employee" or "Independent Contractor" Status*, 58 TAXES 747, 747-57 (1980) (discussing history of IRS factors for determining "employee" status).

162. See I.R.C. §§ 3101-3128 (1988 & Supp. IV 1992).

163. It is estimated that only about 25% of employers of domestics report their employee's wages and pay the tax liability. See *Proposals to Simplify and Streamline the Payment of Employment Taxes for Domestic Workers: Hearing Before the Subcomm. on Social Security and Subcomm. on Human Resources of the House Comm. on Ways and Means*, 103d Cong., 1st Sess. 29, 32 (1993) [hereinafter *Domestic Worker Hearing*] (statement of Louis D. Enoff, Acting Commissioner of Social Security).

unemployment, or disability benefits. In many cases, employers may be inclined to comply with the wishes of the workers, particularly in the case of domestic workers, where employers, having hired someone they know and trust, are reluctant to alter that established relationship.

Many employers also wish to avoid the cost and administrative inconvenience of compliance with the employment tax withholding laws.¹⁶⁴ The result is that the worker is not covered under the Social Security system upon retirement. Furthermore, an employer who fails to withhold is forever liable for the taxes, interest, and penalties, even though the failure to pay the tax may be attributable to an innocent mistake.¹⁶⁵

The solution to this problem is first to identify it and then to publicize it, sunshine being the best disinfectant. The issue received considerable attention during the nomination hearings for the confirmation of Zoe Baird as Attorney General. It has been widely acknowledged that there is general noncompliance with the FICA laws with respect to domestic workers and farm laborers.¹⁶⁶ Because there is a special problem of noncompliance with these two groups, Congress should narrowly define the term "employee" with regard to FICA. The appropriate remedy is to delete these classes from the common-law definition of employee and to define an employee in these groups as any worker who is in continued service within a calendar quarter, to whom more than a certain minimum amount is paid in wages, and who is not otherwise employed by an agency or firm. In order to avoid further problems with semantics and to ensure coverage, any ostensible employee who falls into a grey area should be allowed to opt out of the withholding system and into a system currently being used for self-employed.¹⁶⁷

164. There is significant paperwork involved in complying with the FICA. For instance, the employer must file quarterly returns (Form 941) with the IRS, and there may also be various state forms required, as well as six copies of the Form W-2 which must be sent out each January to the Social Security Administration, the Internal Revenue Service, and the employee. See INTERNAL REVENUE SERV., 1993 INSTRUCTIONS FOR FORM W-2, at 1, 3 (1993).

Jennie S. Stathis, Director of Tax Policy, General Accounting Office, has stated that her agency has repeatedly urged simplifying the withholding of payroll and Social Security taxes. See John H. Cushman, Jr., *I.R.S. Tries Honey but Still has Vinegar on Hand*, N.Y. TIMES, Apr. 15, 1992, § D, at 23; see also *Domestic Worker Hearing*, *supra* note 163 *passim*.

165. See, e.g., *Ginter v. United States*, 93-1 T.C.M. (CCH) ¶ 87,293, 87,295-96 (1993). In *Ginter*, the court held liable a taxpayer who had mistakenly classified employees as independent contractors and filed form 1099 rather than W-2s and 941s. The filing of the 1099s did not trigger the statute of limitations. *Id.*

166. See David E. Rosenbaum, *Usually, the Illegality in Domestic Work Is Benefits Denied*, N.Y. TIMES, Jan. 31, 1993, at E5.

167. Canada, for instance, permits this arrangement. See *infra* part III.A.4 (dis-

In addition to the employee-definition dilemma, the fifty-dollar threshold amount has been criticized as being too low.¹⁶⁸ This amount was set in 1954 and by today's standards, a person who "hir[es] a babysitter every three weeks" should not be subject to liability.¹⁶⁹

A backup to compliance with the FICA is to provide a box on the income tax return to be checked if the taxpayer employed a domestic or farm worker during the taxable year. If this box is checked, the return itself should direct the taxpayer to file the appropriate withholding returns.¹⁷⁰

At present, the ambiguity of the law may produce severe consequences for both workers and employers. Uninsured workers constitute an underclass who ultimately may be in dire need of retirement income but may not be insured under the Social Security system.¹⁷¹ Employers, if found liable, will be subject to severe penalties for failure to withhold,¹⁷² although many may have inno-

cussing more flexible Canadian withholding system). Under my proposal, an employee who falls into a grey area may either elect to withhold as a self-employed individual or allow the employer to withhold. The obligation would be on the employer to ensure that adequate arrangements are made but the employer and employee could agree which of them would assume the withholding obligation. Note that in the United States, the obligation currently cannot be shifted to the employee by agreement.

168. Recently, there have been several bills introduced proposing that the threshold be raised. *See, e.g.*, S. 1231, 103d Cong., 2d Sess. (1993) (proposing significant increase in wage limit, exempting employees under 18, and providing for single annual return); S. 402, 103d Cong., 1st Sess. (1993) (proposing to raise limit to \$250 per year and index it for inflation); H.R. 899, 103d Cong., 1st Sess. (1993) (proposing raising threshold and providing for annual adjustments).

169. *See Social Security: Trigger Level for Withholding Taxes Should Be Examined*, Stephanopolous Says, Daily Tax Rep. (BNA) No. 25, at G-12 (Feb. 9, 1993). According to Dave Durenberger, sponsor of Senate Bill No. 402, the proposed threshold is "reasonable by current standards and fair to those who need occasional help in their daily lives." 139 Cong. Rec. S1898-99 (daily ed. Feb. 18, 1993).

170. This is currently done with respect to foreign bank accounts and trusts. *See* I.R.S. Sched. B, Form 1040 (1992).

171. Even if the employers are forced to pay the back taxes they should have withheld, it is often difficult to determine how long the employee worked for that employer or how much the employee received in wages. Frequently, employers will pay these workers in cash, particularly in the case of itinerant farm workers who may have no bank account, and the employee will not file an income tax return.

172. *See, e.g.*, I.R.C. § 7202 (1988) (willful failure to collect and pay taxes punishable by fine of up to \$10,000 and/or five years in prison); *id.* § 7204 (failure to supply information to employee punishable by up to \$1000 fine and/or one year in prison); *id.* § 7215 (willful failure to deposit taxes in trust fund punishable by up to \$5000 fine and/or one year in prison).

There are also penalties applicable to employees who furnish false withholding certificates. *See id.* § 7205 (1988 & Supp. IV 1992). There may also be other penalties applicable to employees who willfully fail to furnish information when required to do so or who willfully furnish false information. *See id.*; *see also* MICHAEL I.

cently failed to do so. Many domestics, in particular, are hired by laypersons who have little knowledge of the tax laws.

Many employers of domestics may feel pressured by employees, particularly poor working mothers, not to withhold. Because Congress does not take a firm stand on the issue of withholding from the wages of casual workers, there is an incentive not to withhold because employees who wish to avoid having their wages reduced by the withholding taxes will simply threaten to quit. Thus, in order to comply with the law, the employer will be forced to pay higher wages.¹⁷³ The fact that many employers do not withhold on wages paid to these employees undermines the integrity of the federal tax system.

Although it would be relatively simple to call attention to the problem of withholding on casual workers, the government has not addressed this problem in a constructive manner.¹⁷⁴ Perhaps one reason for this is because the underclass consists primarily of the politically vulnerable (i.e., lower paid) workers who are predominantly black, hispanic, or female, and who historically have had no organized voice or political strength.¹⁷⁵ Thus, there has been no interest in updating and reforming the withholding laws to take these workers into account.

For these workers, however, the effect of congressional inaction

SALTZMAN, IRS PRACTICE AND PROCEDURE ¶ 7A.05 n.3 (1991) (discussing other potential penalties).

173. One method of dealing with this problem is to increase the employee's wages to an amount where the employee's take-home pay will not be reduced by the withholding. Many employers will simply remit the entire amount of the withholding tax (employer and employee's portion) without actually withholding this amount from the employee's wages. This creates a problem because the amount of the FICA tax remitted by the employer represents two amounts: (1) the amount of the employer's obligation (currently 7.65%), and (2) the amount of the employee's obligation (currently the same percentage) which the employer withholds from the employee's wages. See I.R.C. §§ 3101, 3102, 3111, 3121 (1988 & Supp. IV 1992). If the employer assumes the employee's portion of the FICA tax liability obligation, the relief of the employee's obligation technically constitutes additional income to the employee on which the employer should also withhold. See *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716, 731 (1929); *Safe Harbor Water Power Corp. v. United States*, 303 F.2d 928, 938 (Ct. Cl. 1962). Since there are important public policy concerns in assuring that the underclass is covered, Congress should allow employers to pay this tax without risking pyramiding liability for further taxes and penalties.

174. Perhaps this is because enforcement of this provision is left to the Internal Revenue Service, an agency historically more intent upon punitive measures (penalties) rather than positive incentives.

175. See Rosenbaum, *supra* note 166, at E5. A former congressman, James C. Corman, described an example of this lack of governmental concern by observing that, "[c]rimes committed by well-off people against poor people do not get as much attention as crimes committed by poor people against well-off people." *Id.*

will be devastating when they reach retirement age, become disabled, or die leaving dependent survivors, because the workers and their beneficiaries will not be entitled to a social insurance benefit. Instead, they will be dependent upon social assistance (welfare) benefits.

From a Machiavellian perspective, as the lower class becomes larger, the need for control becomes greater. Thus, there is likely to be less, rather than more, concern for the underprivileged. This may not be readily apparent at times because some benefits will have to be given to the underprivileged in order to prevent anarchy. Nevertheless, if the underclass expands, the middle class may feel that the cost of the welfare state is too great because they will have to pay much more in order to maintain the current level of benefits.

E. The Private Retirement System

Because the OASDI benefits are insufficient to allow most workers to leave the workforce without a significant drop in income, private or occupational pensions assume great importance in the retirement security scheme. The American private retirement system, however, is a grand scheme of control in the truest Machiavellian sense.¹⁷⁶

The system is encouraged through the use of tax incentives regulated by an inordinately complex piece of legislation, the Employee Retirement Income Security Act of 1974 ("ERISA"),¹⁷⁷ and jointly administered by the Internal Revenue Service and the Department of Labor. ERISA was originally enacted to ensure that promised benefits would be available when the workers became entitled to them, that plans would be fairly administered, and that sufficient numbers of lower paid employees would be covered in order to justify the significant loss of tax dollars.¹⁷⁸

ERISA, however, has failed in its missions. Instead, it repre-

176. For a discussion of the elements of control inherent in this system, see generally TOM SCHULLER, *AGE, CAPITAL AND DEMOCRACY: MEMBER PARTICIPATION IN PENSION SCHEME MANAGEMENT passim* (1986) (explaining different levels of decision-making power involved in pension participation in Britain and United States).

177. Pub. L. No. 93-406, 88 Stat. 829 (1974).

178. For fiscal year 1991, tax incentives for employer-sponsored pension plans amounted to \$46.9 billion. For Individual Retirement Accounts, they totaled \$6.2 billion, and for Keoghs, they reached \$1.6 billion. The total of all these was \$54.7 billion. See *Illusory Promise Hearing*, *supra* note 31, at 4. But see Edward A. Zelinsky, *The Tax Treatment of Qualified Plans: A Classic Defense of the Status Quo*, 66 N.C. L. REV. 315, 315 (1988) (espousing view that tax incentives for qualified plans are part of normative income tax expense and do not represent tax expenditures).

sents one of the best known examples of Machiavellian principles at work. For instance, on the corporate and management side, the private retirement system is a winner. It is a voluntary system. Therefore, management is not forced to provide for the workers. If it does, there are significant advantages. First, there are tax incentives¹⁷⁹ which means that private retirement plans are subsidized by the taxpayers.¹⁸⁰ Second, the plan represents a significant recruiting and retention device for employers.¹⁸¹ Third, the plan places significant assets under the control of management. All of this adds up to big money for lawyers, accountants, and actuaries who are involved in implementing and maintaining plans for management.

From the perspective of the rank and file employees, however, ERISA is a loser. It is true that employees are better off with a plan than without. But ERISA's employee protection is illusory. Although ERISA is under the auspices of the Departments of Labor and Treasury, neither has any power to assist the employees with grievances. Nor is there any type of administrative process available to the employees. Instead, they must proceed directly to federal court.

Very few cases get to court, however, because there are numerous hurdles to clear. First, there is the problem of representation. Although representing management is lucrative for attorneys, representing ERISA plaintiffs is not. For instance, "plaintiffs' lawyers complain that ERISA, which preempts state law and leaves the award of attorneys' fees up to the judge's discretion, offers too little in the way of incentives: no multipliers, no punitive damages, no compensatory damages."¹⁸² Further, most retirees are living on a fixed income and cannot afford the cost of going to court. Second, if the employee gets to court, there is no right to a jury trial.¹⁸³ Despite the 1989 United States Supreme Court decision in *Firestone*

179. The tax incentives are threefold. First, employer contributions, to the extent that they represent "reasonable" compensation, are deductible. I.R.C. § 162 (1988 & Supp. IV 1992); see *id.* § 404 (providing for employer deduction for plan contributions under § 162). Second, the investment income on trust assets is tax-exempt, so the assets accumulate much faster than they would if they were subject to tax. *Id.* § 501(c)(17). Third, the employee is not taxed on the amount of the contribution until there is a distribution. *Id.* §§ 72, 402.

180. This subsidy is significant. See *supra* note 178 (discussing various tax incentive totals for fiscal year 1991).

181. See *supra* note 94 and accompanying text (noting importance of pension plans to potential employees).

182. Fred Stasser, *ERISA: A Law With No Teeth?*, NAT'L J., July 16, 1990, at 1, 27.

183. The problem is one of classification. Many ERISA claims may be classified as legal or equitable. If legal, the plaintiff has a right to a jury trial. If equitable, she does not. See MICHAEL J. CANAN, QUALIFIED RETIREMENT AND OTHER EMPLOYEE BENEFIT PLANS 978-84 (1993).

Tire & Rubber Co. v. Bruch,¹⁸⁴ changing the standard of review for ERISA claims from arbitrary and capricious to *de novo*, ERISA cases are very difficult for plaintiffs to win because the courts will continue to defer, in most instances, to the decision of the plan administrators absent a showing of arbitrariness and a clear breach of fiduciary duty.¹⁸⁵

ERISA also has failed to adequately protect employees within the plan itself. For instance, despite complicated funding rules requiring plans to be fully funded, these rules can be avoided via authorized exceptions. An employer may, for example, obtain a waiver of funding requirements for business hardship.¹⁸⁶ Because a substantial number of these underfunded plans are insured by the Pension Benefit Guaranty Corporation ("PBGC"), a federal agency similar in function to the FDIC and FSLIC, there is a current potential for a crisis similar to that recently experienced in the Savings and Loan industry.¹⁸⁷ Thus, benefits may not necessarily be available to the participants when they retire.

At the other end of the spectrum, there is the problem of overfunded plans, exemplified by the failure of the Executive Life Insurance Company.¹⁸⁸ Executive Life's problems, in this case, be-

184. 489 U.S. 101, 115 (1989). For a criticism of this opinion, see John H. Langbein, *The Supreme Court Flunks Trusts*, 1990 SUP. CT. REV. 207, 207-29.

185. See, e.g., *Morales v. Pan Am. Life Ins. Co.*, 914 F.2d 83, 88 (5th Cir. 1990) ("Where the administrator of the plan has discretion to determine the form of benefits, the exercise of that authority in a nonabusive manner should not be overturned."); Langbein, *supra* note 184, at 213.

186. See I.R.C. § 412(d) (1988 & Supp. IV 1992).

187. Kirk Victor, *Crying Wolf?*, NAT'L J., Oct. 28, 1989, at 2630, 2630-31. The Pension Benefit Guarantee Corporation ("PBGC") insures certain types of tax qualified plans through employer premiums. The PBGC had a deficit of \$1.9 billion at the end of 1990 and this figure likely will continue to rise. The premiums paid by employers have not covered the losses. The problem is that many plans are underfunded and use actuarial assumptions to value plan liabilities that are different from those used by the PBGC. See *Pension Benefit Guaranty Corporation's Premium Program: Hearing Before the Subcomm. on Oversight of the House Comm. on Ways and Means*, 102d Congress, 1st Sess. 16-29 (1991) [hereinafter *PBGC Hearing*].

There is some objection to the characterization of the PBGC situation as another S&L crisis. See Victor, *supra*, at 2630-31. It is generally acknowledged, however, that the long-term financial future of the PBGC is questionable and that reform is needed. Among the suggestions for reform are a revised premium structure which corresponds to the risk the plan poses to the PBGC, as well as stronger funding legislation. It has been stated that the present premium rate structure, coupled with the PBGC's inability to restrict claims, amounts to a moral hazard in which large underfunded plans are grossly undercharged but still protected. *PBGC Hearing, supra*, at 32-56.

188. See *Pension Annuity Protection In Light of the Executive Life Insurance Company Failure: Hearing Before the Subcomm. on Retirement Income and Employment of the House Select Comm. on Aging*, 102d Cong., 1st Sess. 1, 19-105 (1991) [hereinafter

gan with the Pacific Lumber Company, a corporation located in northwestern California. For many years Pacific Lumber had sponsored a defined benefit pension plan¹⁸⁹ for its employees. This plan paid monthly benefits to the retired workers and their beneficiaries. Because it was a fully funded, defined benefit plan, its benefits were insured by the PBGC in case of plan termination. The Pacific Lumber plan was overfunded by design in order to provide a margin of safety and to provide cost-of-living increases for inflation.¹⁹⁰

In 1985, Pacific Lumber was taken over in a leveraged buy-out by corporate raider Charles Hurwitz and his Maxxam group of companies. Pacific Lumber was an attractive target for Hurwitz because of the surplusage in the pension fund. Under the ERISA legislation, an employer may terminate a defined benefit plan and use the remaining assets for its own use provided that the plan document provides for a reversion of plan assets and that annuities are purchased as replacement benefits.¹⁹¹ There are virtually no other safeguards protecting the beneficiaries.

Executive Life Hearing]; see also *Kayes v. Pacific Lumber Co.*, No. C-91-1812-SBA, 1993 WL 187730, at *1 (N.D. Cal. May 14, 1993).

189. A defined benefit plan is the classic pension plan, as opposed to a profit sharing plan:

A pension plan within the meaning of section 401(a) is a plan established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to his employees over a period of years, usually for life, after retirement. Retirement benefits generally are measured by, and based on, such factors as years of service and compensation received by the employees. The determination of the amount of retirement benefits and the contributions to provide such benefits are not dependent upon profits A plan designed to provide benefits for employees or their beneficiaries to be paid upon retirement or over a period of years after retirement will, for the purposes of section 401(a), be considered a pension plan if the employer contributions under the plan can be determined actuarially on the basis of definitely determinable benefits, or, as in the case of money purchase pension plans, such contributions are fixed without being geared to profits.

Treas. Reg. § 1.401-1(b)(1)(i) (1993).

190. See *Executive Life Hearing*, *supra* note 188, at 34 (statement of Jeffrey Lewis, attorney for annuitants of Pacific Lumber Co.). There are several reasons why plans may be overfunded. One is that actuarial assumptions are usually conservative. In the 1980s, when the stock market did better than expected, the result was an overfunding of many defined benefit plans. Note that it is only defined benefit plans which may be overfunded because defined contribution plans promise only the account balance to the employee rather than a set benefit. Other reasons for overfunding a plan involve actuarial miscalculations in employee turnover rates, higher annuity interest rates than the plan used, and various funding formulae such as level funding. See Barbara J. McGeoch, Note, *The American Voluntary Pension System: Can It Thrive Under a No-Reversion Rule?*, 43 *TAX LAW* 773, 778-80 (1990).

191. See 29 U.S.C. § 1342(c) (1988 & Supp. IV 1992).

Shortly after the takeover by Hurwitz and the Maxxam group, the Pacific Lumber plan was terminated and Hurwitz and Maxxam walked off with \$55 million in surplus assets from the plan. These surplus assets were then used to buy down some of the debt from the leveraged buy-out.¹⁹²

In soliciting bids for the required annuities, Pacific Lumber and Maxxam hired an independent consultant who recommended several insurance companies, but did not include Executive Life. Maxxam officials, however, ordered Pacific Lumber officials to include Executive Life in the bidding process. At this point, the treasurer of Pacific Lumber wrote a memo to the Maxxam officials pointing out numerous problems with Executive Life, including its questionable investments in high-risk, high-yield junk bonds.

After Executive Life returned the lowest bid, Maxxam officials insisted that the annuities be purchased from Executive Life, while insisting that the Executive Life investment was safe. When Executive Life failed, it left the financial futures of many retirees in jeopardy. If the plan had terminated with insufficient assets, the beneficiaries would have been entitled to PBGC coverage. But because the plan had sufficient assets at the time of the termination, and the annuities were purchased as required, the PBGC took the position that it did not cover the termination.¹⁹³ In general, the courts have not been helpful in preventing such risky termination.¹⁹⁴

The Executive Life case exemplifies the machinations of the Machiavellian principle of control. The private pension system is generally a voluntary system and Congress has an interest in maintaining it as such to appease powerful constituents. Consequently,

192. See *Executive Life Hearing*, *supra* note 188, at 34.

193. Annuities are subject to state guaranty laws which may not provide the protection of the PBGC. For instance, most state guaranty laws do not provide protection in the event of an insolvency by an insurance company. In addition, there are three states, plus the District of Columbia, which provide no guaranties for insurance annuities. See *Executive Life Hearing*, *supra* note 188, at 61 (statement of Joseph F. Delfico, Director, Income Security Issues, Human Resources Division, General Accounting Office).

194. See, e.g., *Mead Corp. v. Tilley*, 490 U.S. 714, 721 (1989) (ERISA's allocation scheme does not create benefit entitlements); see also Richard A. Ippolito, *Issues Surrounding Pension Terminations for Reversion*, 5 AM. J. TAX POL'Y 81, 82 (1986) (noting terminations generally effected as means of borrowing funds from pension plan); Norman P. Stein, *Raiders of the Corporate Pension Plan: The Reversion of Excess Plan Assets to the Employer*, 5 AM. J. TAX POL'Y 117, 119 (1986) (arguing law should not countenance reversion of plan assets upon termination). Instead, courts have taken the position that such terminations are a matter of corporate, rather than fiduciary, responsibility. See *Executive Life Hearing*, *supra* note 188, at 37 (statement of Jeffrey Lewis).

there is a reluctance on the part of the government to adequately police reversions of assets in terminations of noncontributory plans (those funded entirely by the employer).¹⁹⁵ Instead, such loopholes in the ERISA law are defended by management as being necessary to prevent further governmental intrusion in the private pension industry.¹⁹⁶ Thus, big business, with its more powerful lobby, prevails over the workers who have been led to believe that the ERISA legislation prevents the looting of their pension assets. From a Machiavellian perspective, the explanation is that, as long as management is funding the plan, regardless of what representations have been made to the workers, management is entitled to maintain its control over both its funds and the workers.

A perplexing problem in the Executive Life case is that the DOL waited three years after the failure of Executive Life to sue Pacific Lumber for breach of fiduciary duty in its selection of the insurer.¹⁹⁷ Such inaction is curious in light of the possibility that the Executive Life debacle was just the tip of the iceberg with respect to unsound insurance companies insuring the futures of America's pensioners.¹⁹⁸ The DOL's own Inspector General has expressed concern that the nation's pension assets are ripe for looting through "a combination of 'permissive regulations and lax enforcement' of ERISA."¹⁹⁹ This speculation has sparked an uproar from government officials who deny that the problem is of such magnitude.²⁰⁰ In response to the Inspector General's speculation, the Justice Department, along with the DOL, forced the suspension of about 1200 criminal investigations under the Inspector General's office.²⁰¹ Such action helps to illustrate the theory that, contrary to Marxist philosophy, elements of control have not just evolved through economic principles, but have been carefully orchestrated through Machiavellian tactics.

Because of situations such as that in the Executive Life case, many employees perceive that their plans are not always fairly

195. There is instead a 20% excise tax imposed on assets that revert to the employer upon termination of a defined benefit plan. See I.R.C. § 4980 (1988 & Supp. IV 1992). This tax, however, is evidently not enough of a deterrent to prevent abusive situations and consequent deprivations of pension benefits.

196. See, e.g., *Executive Life Hearing*, *supra* note 188, at 39 (prohibiting asset reversions would limit extent to which annuities will replace pensions).

197. See *Martin v. Pacific Lumber Co.*, No. C-91-18125BA, 1993 U.S. Dist. LEXIS 660, at *4 (N.D. Calif. Jan. 15, 1993) (unpublished opinion).

198. See *Executive Life Hearing*, *supra* note 188, at 54 (statement of Sherwood L. Boehlert, Select Committee on Aging).

199. Victor, *supra* note 187, at 2630 (quoting Inspector General Raymond Mario).

200. *Id.*

201. *Id.* at 2631.

administered.²⁰² Statistics clearly show that the number of covered workers has steadily declined in the past ten years.²⁰³ Despite the decline in coverage, however, the tax cost of these plans has continued to rise.²⁰⁴

One problem is that the private pension system is voluntary, rather than mandatory. The result is that it is by no means universal. In fact, less than half of all workers are covered under this system²⁰⁵ although all taxpayers support it indirectly.²⁰⁶ Furthermore, the public must also foot the bill for those who are not covered, who have no other means of support, and who must resort to welfare. On the other hand, retirement funds are the largest source of investment capital in the United States.²⁰⁷ They, of course, are controlled by big business, the same group who lobbied against mandatory benefits.²⁰⁸

But even for those who are covered, retirement security is far from certain. Most private plans are not indexed for inflation, are

202. See, e.g., *Executive Life Hearing*, *supra* note 188, at 19–22, 26–28 (relating criticisms of pension plan participant).

203. Nearly half of all workers were covered by an employer-provided pension a little over ten years ago. Today, less than 44% of all workers are covered. See *Illusory Promise Hearing*, *supra* note 31, at 4 (statement of William J. Hughes).

204. See J. Robert Suffoletta, Jr., Note, *Who Should Pay When Federally Insured Pension Funds Go Broke?: A Strategy for Recovering from the Wrongdoers*, 65 NOTRE DAME L. REV. 308, 312 (1990) (discussing growth in pension assets).

205. See EMPLOYEE BENEFIT RESEARCH INST., PENSION POLICY AND SMALL EMPLOYERS: AT WHAT PRICE COVERAGE? 14 (1989) (approximately 49.5% of nonagricultural workforce is currently covered under an employer-provided plan).

206. There are two bills currently pending which purport to alleviate some of the participation problem, the Pension Coverage and Portability Improvement Act of 1991, H.R. 2390, 102d Cong., 1st Sess. (1991), and the Pension Access and Simplification Act of 1991, H.R. 2730, 102d Cong., 1st Sess. (1991). H.R. 2390 requires all employers that do not sponsor a pension or other retirement savings plan to offer voluntary salary reduction plans for their employees. Under H.R. 2730, employers with 100 or less employees would be allowed to establish a qualified retirement plan without having to pass the nondiscrimination tests, provided that certain minimum contribution standards are met. *But see Illusory Promise Hearing*, *supra* note 31, at 86–89 (statement of Karen W. Ferguson criticizing H.R. 2730).

207. The value of pension assets in 1987 was \$1.6 trillion. See Suffoletta, *supra* note 204, at 312 (citing UNITED STATES GEN. ACCOUNTING OFFICE, PUB. NO. HRD-88-21, EFFECT OF THE 1987 STOCK MARKET DECLINE ON SELECTED LARGE PENSION PLANS 1 (1988)). It is predicted that by the year 2000 these assets will grow to \$4 trillion. See *id.* For a discussion of the concerns of concentrating this wealth in the hands of a few, see SCHULLER, *supra* note 176, at 1–22, 30–36, 80–106.

208. See, e.g., COMM. FOR ECONOMIC DEV., REFORMING RETIREMENT POLICIES 43 (1981) (opposition of business leaders to mandatory system). Under a mandatory system each worker would have an account which would either be managed by the government or by an independent investment advisor of the taxpayer's choosing, similar to an individual retirement account. For a discussion of this concept see EMILY ANDREWS, THE CHANGING PROFILE OF PENSIONS IN AMERICA 174–75 (1985).

not easily transferrable when workers change jobs, and although the vesting provisions are less restrictive due to reform legislation enacted in 1986,²⁰⁹ it still takes between three and seven years, and sometimes even longer,²¹⁰ before the worker is completely vested.²¹¹ Furthermore, plans may legally deny coverage to lower paid workers through "integration" with the Social Security system.²¹² Statistics show that the 1986 provisions are not sufficient to make the private retirement system more equitable for women and others with short term job tenure.²¹³ Congress has been holding hearings to determine what can be done to alleviate this problem.²¹⁴

In the meantime, the lower paid workers will continue to depend upon Social Security as their sole or "important" source of post-retirement income.²¹⁵ For the more highly compensated elderly workers, Social Security will not have much significance. For these workers, private pensions and savings will assume a more important role. But considering the tremendous tax cost of private plans for which the taxpaying public foots the bill, the system remains highly inefficient and inequitable.²¹⁶ Because it is a voluntary system, the employees have little direct influence on whether the employer implements a retirement plan for their benefit. Moreover, if an employer implements a plan, the employees have little

209. Tax Reform Act of 1986, Pub. L. No. 99-514, sec. 1101, § 214, 100 Stat. 2085, 2411-2414 (1986).

210. See I.R.C. § 411(a)(2)(B) (1988 & Supp. IV 1992); 29 U.S.C. § 1053(a)(2)(B) (1988 & Supp. IV 1992).

211. For instance, in the case of a multi-employer plan, the minimum vesting schedule is 10 years for employees covered pursuant to a collective bargaining agreement. See I.R.C. § 411(a)(2)(C) (1988 & Supp. IV 1992).

212. *Id.* § 401(a)(5). Integration involves a reduction in employer-provided pension benefits by a portion of the employee's Social Security benefits. For a discussion of integration and its inherent problems, see Watson, *supra* note 21, at 24-26.

213. See Watson, *supra* note 21, at 20-24.

214. See, e.g., *Women in Retirement: Are They Losing Out?: Hearing Before the Subcomm. on Retirement Income and Employment of the House Select Comm. on Aging*, 101st Cong., 2d Sess. 19-136 (1990) (discussing unique problems facing women under private retirement system).

215. During the latter half of the 1980s, half of all retirees had less than \$10,000 in savings when they retired. (This figure does not include a house and car.) Furthermore, the national savings rate has fallen from around 8% to a current rate of around 1.7%. See *Illusory Promise Hearing*, *supra* note 31, at 4 (statement of William J. Hughes).

216. For instance, the revenue loss attributable to employee plans for 1993 is estimated to be \$57.6 billion with \$61.1 billion in revenue losses predicated for 1994. See JOHN H. LANGBEIN & BRUCE A. WOLK, *PENSION AND EMPLOYEE BENEFIT LAW* 133 (1990) (citing JOINT COMM. ON TAXATION, *ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 1990-1994* (1989)).

voice in what type of plan is implemented.²¹⁷ Additionally, if the employer does implement a plan, thirty percent or more of the workforce may be legally excluded under the current ERISA rules.²¹⁸

Over the past several years there has been a steady decline in the number of defined benefit plans.²¹⁹ Since defined benefit plans pay a pre-determined benefit after retirement or disability, the employer assumes the risk of investment loss. Thus, defined benefit plans provide greater retirement security than defined contribution plans.²²⁰ Under the defined contribution plan, the employee receives a benefit determined solely by the account balance.²²¹ Thus, the employee assumes the investment risk. This means that it is not as secure a retirement vehicle as the defined benefit plan. Another consideration is that defined benefit plans are insured by the PBGC, whereas defined contribution plans are not.²²²

217. If more elderly workers remain in the workforce, employers theoretically will be more inclined to establish true pension plans or defined benefit plans, in which the worker is promised a definite benefit upon retirement, because the benefits will be funded over a longer period of time for a shorter retirement period. While this does provide security to the worker, it gives the worker no choice as to whether it would be preferable to individually assume the investment risk for a potentially higher return. As a practical matter, the onerous reporting and disclosure requirements combined with the anti-discrimination in coverage provisions have all but destroyed defined benefit plans. *See supra* note 206. A more practically feasible plan that would allow the worker to assume the investment risk is a profit-sharing plan or a defined contribution plan. Under this arrangement, the worker is promised only her account balance upon retirement. For a general discussion of the various types of plans, see CANAN, *supra* note 183, at 98-182 (1990).

218. *See* I.R.C. § 410(b)(1)(A) (1988 & Supp. IV 1992) (at least 70% of non-highly compensated employees must be covered).

219. This decline is attributable to plan terminations. For instance, there were more than 42,000 terminations of defined benefit plans between 1989 and 1991. AM. ACADEMY OF ACTUARIES, PRELIMINARY REPORT: RESULTS OF THE AMERICAN ACADEMY OF ACTUARIES SURVEY OF DEFINED BENEFIT PLAN TERMINATIONS 1 (1992) [hereinafter PRELIMINARY REPORT]. The growth of new defined benefit plans has also slowed. IRS statistics show that in fiscal year 1990, 86% of the new plans implemented were defined contribution plans. *See Illusory Promise Hearing, supra* note 31, at 5 (statement of William J. Hughes). According to a recent study by the EBRI, defined contribution plans account for 78% of all private plans. *See id.* at 7 (Statement of Rep. Sherwood L. Boehlert).

220. A recent survey has shown that there is a significant difference in the amount of benefits received under defined contribution versus defined benefit plans. For a retiree earning \$15,000 per year, the average defined contribution pension was around 19% of salary. The average pension for the same retiree under a defined benefit plan was around 28% of salary. *See Illusory Promise Hearing, supra* note 31, at 5.

221. *See* CANAN, *supra* note 183, at 96-98.

222. *See* 29 U.S.C. § 1321(a) (1988 & Supp. IV 1992) (PBGC coverage applies to any "employee pension benefit plan"); *id.* § 1321(b) (exception to PBGC coverage is

One reason for the decline in the number of defined benefit plans has been poor marketing efforts by financial advisors because such plans are more complex and, therefore, more difficult to administer.²²³ Another problem is that in one-third of the terminations, the employer did not implement a replacement plan, and where replacement plans were implemented, half were less generous than the terminated plan.²²⁴

A related difficulty is employee "cash-out" when a plan is terminated or the employee changes jobs.²²⁵ The problem is that very few employees invest their plan proceeds in deferred savings arrangements.²²⁶ Instead, most spend the cashed-out amount, paying the back taxes and a penalty, thus dissipating their retirement savings.²²⁷

Also worrisome is the popularity and growth of 401(k)

"individual account plan").

223. See *Employee Benefits: Actuaries May Be Partly Responsible for Defined Benefit Plan Decline, Meeting Told*, Daily Tax Rep. (BNA) No. 208, at G-7 (Oct. 27, 1992) (remarks of Harlan Weller, actuary for Office of Tax Policy, Treasury Department). Actuaries and accountants blame, in part, complex government regulations. Small, growing companies rarely turn to defined contribution plans instead of defined benefit plans. *Id.* In a survey conducted by the American Academy of Actuaries, it was found that the primary reason given for termination of a defined benefit plan was excessive and complex government regulation. See PRELIMINARY REPORT, *supra* note 219, at 3-6.

Note that the decrease in the number of defined benefit plans may also be due, at least in part, to the current trend toward early retirement. For a discussion of this trend, see SCHULZ, *supra* note 153, at 68-70. This accelerates the number of retirements anticipated under the plan and greatly increases its costs. This reason, however, would not be as readily articulated by actuaries and accountants.

Several pension simplification bills have been introduced recently in Congress. See, e.g., Pension Simplification Act, S. 762, 103d Cong., 1st Sess. (1993); H.R. 13, 103d Cong., 1st Sess. (1993).

For small businesses, there is a type of plan available which can be established with relative ease and little expense. This type of plan is a Simplified Employee Pension Plan ("SEP"), introduced in 1979, which is similar to an IRA with larger employer contribution limits. See I.R.C. §§ 219(b), 402(h), 408(k) (1988 & Supp. IV 1992). However, SEPs have been greatly underused. See *Illusory Promise Hearing*, *supra* note 31, at 6 (statement of William J. Hughes). This, also, is probably due to marketing deficiencies.

224. See PRELIMINARY REPORT, *supra* note 219, at 14-16.

225. A cash-out occurs when a distribution of the employee's vested benefit is made because of the employee's termination of participation in the plan. The distribution does not necessarily have to be made in cash. The term *cash-out* is a term of art under the ERISA rules and carries specific tax treatment. For a discussion of the cash-out rules, see CANAN, *supra* note 183, at 367-70.

226. See *Illusory Promise Hearing*, *supra* note 31, at 5 (statement of William J. Hughes); ANDREWS, *supra* note 208, at 58, 162.

227. See ANDREWS, *supra* note 208, at 163 tbl. 8.6 (although percentage spent varies with amount of cash-out).

plans.²²⁸ Under a 401(k) plan, an employee may defer income tax on contributions up to \$7000.²²⁹ The employer then matches this contribution.²³⁰ These types of plans raise two problems. First, they represent a shift away from defined benefit plans; and second, only more highly compensated employees can afford them. It has been argued that frequently, these more highly compensated employees are merely shifting income to the 401(k) plan that they would have saved anyway, so the assets in the 401(k) plans do not represent new retirement savings.²³¹ As Karen Ferguson, director of the Pension Rights Center in Washington, D.C. states: "This cost is not justified if 401(k)s are merely providing tax breaks for people who do not need incentives to save for themselves."²³²

Because the concept of retirement plans as a system of deferred compensation rather than a gratuity from the employer is now pervasive,²³³ one might wonder why Congress stopped short of legislating mandatory retirement benefits since, under the Tax Reform Act of 1986, it did significantly cut the minimum vesting period.²³⁴ The reason behind this is the powerful lobbying efforts by big business, who do not want to lose control over either the workers or its single most important source of investment capital. Thus, although big business initially opposed the enactment of ERISA because of the increased costs it would entail,²³⁵ business managers have now come to realize that it is a substantial means of recruitment, incentive, and retention, as well as a significant means of control over employees.²³⁶ If the private retirement system were mandatory, management would lose control of these assets whereas the workers or the government would gain control. Moreover, when workers change jobs, they would always be able to take their accumulated

228. So called because the tax consequences are determined under I.R.C. § 401(k) (1988 & Supp. IV 1992).

229. See *id.* § 402(g)(1). This amount is indexed for cost-of-living adjustments under § 402(g)(5).

230. See *id.* § 401(k)(2).

231. See *Illusory Promises Hearing, supra* note 31, at 80.

232. See *id.* at 85 (statement of Karen Ferguson).

233. See, e.g., BERNARD BENJAMIN ET AL., PENSIONS, THE PROBLEMS OF TODAY AND TOMORROW 49 (1987) ("The concept of the pension as deferred pay has become universally accepted partly because it is an apparently simple concept to understand."); SCHULLER, *supra* note 176, at 23-36 (discussing historical development of pensions and changing attitudes toward them).

234. See I.R.C. § 411(a)(2) (1988 & Supp. IV 1992).

235. These efforts are noted in Camilla E. Watson, *Broken Promises Revisited: The Window of Vulnerability for Surviving Spouses Under ERISA*, 76 IOWA L. REV. 442-49 (1991).

236. See DAN M. MCGILL & DONALD S. GRUBBS, JR., FUNDAMENTALS OF PRIVATE PENSIONS 21-24 (1989).

retirement benefits with them.

III. THE CANADIAN RETIREMENT AND WELFARE SYSTEM

The Canadian retirement system, like the American system, is dualistic, consisting of both a public and a private segment. Although the Canadian system is not perfect, it is generally better organized than the American system. More importantly, the proper national health care infrastructure exists in Canada, and this infrastructure has been instrumental in controlling medical costs.

A. *The Canadian Public Retirement System*

The Canadian public retirement system consists of two portions: Old Age Security²³⁷ and the Canada/Quebec Pension Plan ("C/QPP").²³⁸ Both programs have some attributes of the American Social Security system. In order to properly compare and contrast the Canadian system with the American system, it is necessary to examine the development of the Canadian system.

1. *Old Age Pensions Act of 1927*

The development of the Canadian public retirement system had its origins in the pioneer experience. The first Canadian settlers did not find an easy life. For the most part, they lived an isolated existence of hard work and self-reliance. The nuclear family assumed a very important role, with all members of the family doing their share of the work. Those unable to work were cared for by their families.

Against this backdrop, the market ethos of hard work and productivity became firmly engrained.²³⁹ An early form of social welfare legislation, the Elizabethan poor law, was adopted only in New Brunswick and Nova Scotia where it was indifferently applied.²⁴⁰ The economy was based on barter and subsistence farming. Later, however, came urbanization and industrialization, and this produced a change to a cash economy. The nuclear family began to assume less importance.

Other factors also contributed to a different way of thinking.

237. Old Age Security Act, ch. 18, 1951 S.C. 181 (1951) (codified as amended at R.S.C., Ch. O-3 (1985) (Can.)).

238. Canada Pension Plan, ch. 51, 1964-65 S.C. 605 (1965) (Can.); Quebec Pension Plan, ch. 24, 1965 S.Q. (1965) (Can.).

239. For a more in-depth discussion of this phenomenon, see BRYDEN, *supra* note 10, at 19-43.

240. *See id.* at 22.

For example, increases in life expectancy resulted in a larger population of elderly people.²⁴¹ As they became more numerous, their problems became more visible. Furthermore, other countries, including England, had already implemented old age pension systems.²⁴²

The Old Age Pensions Act of 1927 ("Pensions Act"),²⁴³ a social assistance program funded jointly by the federal government and the provinces,²⁴⁴ was enacted after an arduous battle. The primary objection to the Pensions Act was that it "represented an unwarranted intrusion into the provincial field."²⁴⁵ Critics of the legislation also objected on the ground that it would penalize thrift and would not differentiate between the deserving and the nondeserving.²⁴⁶ They further believed that there was no public demand for government-provided pensions, and that such pensions invaded the purview of the family, whose responsibility it was to care for the old and the disabled.²⁴⁷

In the end, however, changing social conditions and attitudes toward the elderly prevailed over more traditional views, and the Pensions Act was passed.²⁴⁸ The Act was significant because it heralded the involvement of the Canadian government in the retirement arena.

Because the system was designed to be noncontributory, benefits were based on an income-measured means test. This led to problems because standards in applying the test varied among the provinces.²⁴⁹ In fact, there was neither general uniformity in nor speed of implementation of the plan among the provinces. It was nearly ten years before the plan was fully implemented on a national level.²⁵⁰ In the meantime, living costs increased and pensions under the plan could not keep pace.²⁵¹

In addition to these problems, economics also influenced the

241. *See id.* at 61-101.

242. *See id.* at 45-48.

243. Old Age Pensions Act, ch. 35, 1926-27 S.C. 165 (1927) (Can.).

244. *Id.* at 165-66. The system was to be administered by the provinces subject to advance federal approval. *See id.*

245. BRYDEN, *supra* note 10, at 70. The real impetus behind this objection, however, was not a concern for provincial rights but rather a belief that the provinces would fail to act and thus destroy the system. *Id.* at 76. For their part, the provinces were concerned about affordability. *Id.* at 70.

246. *See id.* at 24.

247. *See id.*

248. One of the arguments in favor of the legislation was that the war had robbed many families of able-bodied men who, in turn, could have provided for family members unable to support themselves. *See* GUEST, *supra* note 115, at 76.

249. *See* BRYDEN, *supra* note 10, at 61-62.

250. *Id.* at 81-101.

251. *See id.*

development of the public system. Most Canadians had prospered during and immediately after World War II. This period of financial security, following on the heels of the Depression, created a powerful stimulus in favor of Keynesian economics with stronger paternalistic government involvement in the retirement realm.²⁵²

2. *Old Age Security*

The 1950s and 1960s saw major changes in the public retirement system. The Pensions Act was replaced with the Old Age Security Act ("OAS"),²⁵³ enacted in 1951. The OAS is a universal, noncontributory system of assistance to the elderly with benefits intended as a supplement to the pensioner's own resources.²⁵⁴ Beneficiaries under OAS receive a flat rate, not based upon need.²⁵⁵ The benefits are indexed quarterly according to increases in the Consumer Price Index ("CPI").²⁵⁶ As with the American OASDI benefits, there is a clawback provision in which taxpayers with incomes above a certain level are taxed on their OAS benefits.²⁵⁷ The effect of the clawback provision in Canada, as in the United States, is to reduce the importance of the government retirement system and to shift the focus to private pensions.

There is no earnings test applied to reduce the amount of the basic OAS benefit as there is with the American OASDI program.²⁵⁸ Thus, Canadian old age pensioners may work without

252. For a general discussion of the effect of the Depression and World War II on the Canadian economy and retirement policy, see GUEST, *supra* note 115, at 83-141.

253. Old Age Security Act, ch. 18, 1951 S.C. 181 (1951) (codified as amended at R.S.C., ch. O-9 (1985 & 1st Supp. 1988) (Can.) ("OAS"). The federal role in retirement security has resulted in old age expenditures constituting a significant portion of the federal budget. See BRYDEN, *supra* note 10, at 8-9. At the outset, the expenditures amounted to 7.8% of the budget, and by 1974 had risen to 13.3%. *Id.*

254. See GUEST, *supra* note 115, at 151. A spouse's benefit is also available. See Old Age Security Act, R.S.C., ch. O-9, § 19 (1985) (Can.).

255. See Old Age Security Act, R.S.C., ch. O-9, § 7(1) (1985) (Can.). The 1993 rate for the quarter beginning July 1, 1993 is \$383.51 per month, which represents an increase of \$1.91 per month over the previous quarter. See 1 Canadian Empl. Benefits & Pens. Guide Rep. (CCH) ¶ 933 (1993) [hereinafter Canadian Pension Guide].

256. Old Age Security Act, R.S.C., ch. O-9, § 7(2) (1985) (Can.). The OAS was amended in 1977 to allow partial benefits for those failing to meet the residence requirement. Act of Mar. 29, 1977, ch. 9, 1976-1977 S.C. 284 (Can.) (codified as amended at R.S.C., ch. O-9, §3(2) (1985) (Can.)).

257. See Income Tax Act, R.S.C., ch. 1, § 56(1)(a) (5th Supp. 1992) (Can.).

258. Compare 42 U.S.C. § 403(f) (1988 & Supp. III 1991) (earnings test applied) with Income Tax Act, R.S.C., ch. 1, § 56(1)(a) (5th Supp. 1992) (no earnings test applied).

fear of their OAS benefits being affected by the amount of their earned income.

The age for eligibility to receive OAS benefits was originally set at seventy, but was reduced each year²⁵⁹ until in 1970 it stood at age sixty-five where it currently remains.²⁶⁰ Benefits under the OAS are payable when the recipient files an application after meeting the age and residency requirements.²⁶¹ The amount of annual entitlement under the OAS is paltry, barely reaching subsistence levels.²⁶² For those truly in need, however, there is a monthly guaranteed income-tested supplement ("GIS").²⁶³

Although the GIS is similar to the SSI benefit of the American system, the GIS is more humane. Under the American system, SSI eligibility is based on a potential recipient's total assets after certain exemptions are deducted.²⁶⁴ However, the GIS, as an income-tested system, allows recipients to retain their other assets.²⁶⁵

When the Canadian public pension system was first implemented, benefits had been subject to an income-based means test, but under the regulations, assets were also considered under a formula by which assets were converted to income.²⁶⁶ This test was later abandoned in favor of universal pensions.²⁶⁷ Although a means test was retained for GIS benefits, the asset portion was discarded in favor of a pure income test because the close scrutiny of a recipient's assets was perceived as too humiliating and self-defeat-

259. See BRYDEN, *supra* note 10, at 130.

260. See Old Age Security Act, R.S.C., ch. O-9, § 3(1)(b) (1985) (Can.).

261. See *id.* §§ 3(1), 8(1).

262. See *supra* note 255 (discussing amounts payable under Act).

263. See Old Age Security Act, R.S.C., ch. O-9, §§ 10-18 (1985) (Can.). Under the 1951 legislation, there was established in addition to OAS, another system, Old Age Assistance ("OAA"), which provided means-tested benefits to those between the ages of 65 and 69. This system was a shared cost system with the maximum benefit equal to that under the OAS. The OAA was phased out in 1969 and has now been replaced by the guaranteed income-tested supplement ("GIS"). See BRYDEN, *supra* note 10, at 7-8; Guest, *supra* note 115, at 155.

The GIS was originally proposed in 1966 as an interim measure until the Canadian/Quebec Pension Plan ("C/QPP") became fully operational, but Canadians soon realized that the Pension Plan alone would not alleviate the problem of poverty. See *infra* part III.B (discussing C/QPP).

264. See *supra* notes 69-70, 72 and accompanying text (discussing eligibility requirements to receive SSI benefits). Note that even though some exemptions are permitted under the means test, see 42 U.S.C. § 1382b(a) (1988 & Supp. III 1991), the states vary in the imposition of monetary limits on these exemptions. See PIACENTINI & FOLEY, *supra* note 42, at 436.

265. See Old Age Security Act, R.S.C., ch. O-9, § 3 (1985) (Can.).

266. See III Statutory Orders & Regs. §§ 10-12 (1949) (Can.); see also Old Age Pensions Act of 1927, R.S.C., ch. 156 (Can.).

267. See Old Age Security Act, R.S.C., ch. O-9, § 3 (1985) (Can.).

ing under the remaining vestiges of the market ethos.²⁶⁸

The goal of the Canadian public retirement system is the same as that of the American system—to ensure a minimum standard of living for all Canadians. It is acknowledged that the current Canadian system goes beyond that goal and that a need-based system would be more efficient.²⁶⁹ Some have estimated that the current system may well be unable to bear the burden of an aging population and other tax pressures.²⁷⁰

An interesting facet of the Canadian public retirement system is that the universal component (OAS) is predicted to produce relatively modest future public expenditures attributable to population aging because its importance will decline so long as there is real wage growth in the economy.²⁷¹ The significance of this design is that OAS benefits are less likely to be targeted for budget cuts since (1) they will assume less importance in a booming economy because of the relatively slight budgetary drain, and (2) in a slack economy, the benefits may assume more importance for a greater proportion of the population due to the middle class incorporation principle.²⁷² GIS benefits are also linked to the CPI, but in contrast to OAS benefits, they have been increased several times through ad hoc legislation.²⁷³ GIS recipients have benefitted from “both real and relative growth in GIS benefit levels.”²⁷⁴ Therefore, there will be intense resistance to any benefit cuts.

268. See BRYDEN, *supra* note 10, at 103–28. The current income test considers not only the income of the recipient, but also the income of the spouse. Any change in marital status may result in an adjustment of GIS benefits. See Canadian Pension Guide, *supra* note 255, ¶ 926. There is a spousal benefit under the GIS which is also income-based. See Old Age Security Act, R.S.C., ch. O-9, §§ 13, 19 (1985) (Can.).

269. Jonathan Ferguson, *Great Expectations: Your Dream of a Golden Retirement Could Turn into a Nightmare*, TORONTO STAR, May 10, 1992, at B1.

270. *Id.*

271. John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in OLD AGE POLICY, *supra* note 110, at 84, 89–91. Since 1972, OAS benefits have remained generally constant because there has been no real wage growth. However, it is predicted that productivity gains will trigger such a growth in the future. When that happens, it is further predicted that the universal component of the Canadian retirement system will “wither away with the slack to be taken up by GIS . . . and an expanded ‘semiprivate’ welfare state.” *Id.* at 91.

272. See *supra* notes 111–15 and accompanying text (discussing middle class incorporation principle).

273. See, e.g., Act of June 28, 1984, ch. 27, 1984 S.C. 841 (Can.) (raising GIS by \$50 per month in two stages, \$25 in July and another \$25 in December); amended by Act of June 5, 1980, ch. 4, 1980–1983 S.C. 43, 44 (Can.) (codified as amended at R.S.C., ch. O-9, § 12 (1985) (Can.)) (\$35 per month increase).

274. See John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in OLD AGE POLICY, *supra* note 110, at 84, 89.

3. *The Canada/Quebec Pension Plan*

Because benefits under the OAS were paltry, there was a growing concern in the early 1960s with sharply reduced living standards among retirees,²⁷⁵ although retirees were not the only concern. There also was a growing consensus in favor of an expanded retirement system that would provide benefits to survivors and to the disabled.²⁷⁶ It was strongly felt that a second tier of public benefits was needed. In keeping with the market ethos, public opinion favored a contributory plan. For budgetary reasons, the government mandated a self-financing, contributory plan in order to provide increased public retirement benefits.²⁷⁷ In 1965, the Canada Pension Plan ("CPP")²⁷⁸ became effective. The CPP is a contributory plan funded, like Social Security, by a regressive employment tax in which only those who have contributed for the requisite time period are eligible to receive benefits.²⁷⁹ The CPP also offers survivors' and dependents' benefits, disability benefits, and a death benefit. Contributions to the system have been commingled with general revenues and benefits are currently funded under a pay-as-you-go system as are the OASDI benefits under the Social Security system. Like the American system, CPP contributions are based on wages with an equal obligation imposed on the employee and the

275. See BRYDEN, *supra* note 10, at 129.

276. *Id.* at 142-43.

277. See *id.* The battle in this instance was not as great as in 1927 because the private retirement system had not proven to be very satisfactory and public consensus favored increased benefits, even though it meant higher taxes. Also, Great Britain had implemented a contributory system four years before the C/QPP was enacted. See *id.* at 129-37.

278. Canada Pension Plan, ch. 51, 1964-1965 S.C. 605 (1965) (codified as amended at R.S.C., ch. C-8 (1985 & Supps.) (Can.)). This plan was the government's response to public opinion in favor of a public contributory retirement system with an automatic cost-of-living adjustment. The province of Quebec adopted its own pension plan, the Quebec Pension Plan ("QPP"). While the Canada Pension Plan ("CPP") and the QPP are comparable plans—having become effective within a few months of each other—their development has not always been simultaneous. For background of these plans, see GUEST, *supra* note 115, at 150-59. See also 1 Canadian Pension Guide, *supra* note 255, ¶ 505.

279. This time period is generally 10 years, as it is with Social Security, although in some cases there may be a reduced period for eligibility. See Canada Pension Plan, R.S.C., ch. C-8, § 42(1) (1985); R.S.C., ch. 30, § 12 (2d Supp. 1988) (Can.). At maximum, the combined sums of OAS and the C/QPP are around \$11,000 or 40% of the average industrial wage. See Donald A. McGrath, *Human Resources: A Comparative Look at the Legal and Tax Environment for Motivating and Compensating People in the United States and Canada (ESOPS, Profit Sharing, Pensions and other Fringe Benefits, etc.)—Balance Sheet and Profit/Loss Sheet Effects of Same; Current Status and Future Trends*, 16 CAN.-U.S. L.J. 125, 125 (1990).

employer.²⁸⁰ Benefits under the CPP are indexed for annual adjustments²⁸¹ and are payable in addition to the OAS benefits. Both OAS and CPP benefits are fully portable so that a worker does not lose any benefits upon changing jobs.²⁸²

The age of eligibility for benefits under the Canadian Pension Plan ("CPP") is sixty-five in most instances, with no earnings test imposed.²⁸³ This is consistent with the OAS system. Further, under the public system, recipients age sixty-five or over do not have to retire in order to receive benefits.²⁸⁴ Under the CPP, once eligibility is established, a worker may subsequently become "re-employed" without losing benefits.²⁸⁵

This is a "no lose" policy which encourages the elderly to remain in the workforce. It is in stark contrast to the punitive American OASDI system, in which the elderly are forced to retire and to remain permanently out of the workforce. The American policy, in contradistinction to the Canadian policy, sends the message that the elderly are dependents and are no longer productive members of the workforce.

The survivor's benefit provisions under the CPP are also more humane in that they do not require an automatic disqualification for short-term marriages, although there is the same concern with sham marriages under the Canadian system as there is under the Social Security system. Under the CPP, if a contributor dies within one year of the marriage, the survivor may present evidence to show that at the time of the marriage, the contributor was in a state of health that would justify a reasonable expectation that the contributor would survive beyond a year.²⁸⁶ This is more equitable

280. The total contribution rate for 1993 is 5%, 2.5% for both employer and employee on earnings above the exempt amount, currently \$3200, spread evenly over the 12 month pay period. There is a ceiling of \$33,400 for 1993 on taxable earnings. See 1 Canadian Pension Guide, *supra* note 255, ¶ 535. As in the United States, self-employed persons pay the combined rate. *Id.* ¶ 15-795.

281. Canada Pension Plan, R.S.C., ch. C-8, § 45(2) (1985) (Can.).

282. See *id.* § 6.

283. See *id.* § 44(1); R.S.C., ch. 30, § 13 (2d Supp. 1988), amended by Act of Feb. 28, 1992, ch. 2, 1992 S.C. 123 (Can.).

284. See Canada Pension Plan, R.S.C., ch. C-8, § 67 (1985); R.S.C., ch. 30, § 36 (2d Supp. 1988) (Can.); 2 Canadian Empl. Benefits & Pens. Guide Rep.; Quebec Pens. Plan (CCH) ¶ 35-580, § 157.1(d) (1992) [hereinafter Pension Guide-QPP].

285. 2 Canadian Pension Guide, *supra* note 255, ¶ 724. So long as the worker initially qualified with an annual salary less than the maximum annual pension payable at age 65 that worker may subsequently resume employment which pays out amounts exceeding the qualifying limit. *Id.*

286. "Where a contributor dies within one year after his marriage, no survivor's pension is payable to his surviving spouse if the Minister is not satisfied that the contributor was at the time of his marriage in such a condition of health as to justi-

than the Social Security system, which irrebuttably limits circumstances under which the survivor of a short-term marriage may collect benefits.²⁸⁷

4. *Treatment of Casual Workers*

The problem of casual workers is recognized under the Canadian system, but it is treated in a more intelligent and less punitive manner than under the American system. The Canadian system exempts employers of casual workers from having to make contributions to the public retirement system.²⁸⁸ Thus, the Canadian system does not have the compliance problems of the American system.

One problem which does arise under the Canadian system is the creation of an underclass that is not covered under the public system. This is not as serious a problem as it is in the United States, however, because Canadian workers are entitled by right to OAS benefits which are universal and not tied to contributions. Also, these workers are permitted to make their own contributions to the C/QPP as self employed individuals.

B. *The Canadian Private Retirement System*

1. *Occupational Pensions*

In Canada, as in the United States, the benefits under the public system are insufficient to allow most elderly persons to leave the labor force without a significant drop in living standard. Therefore, a dualistic system is required. As in the United States, the second tier of this system consists of employer-provided private pensions, Registered Pension Plans ("RPPs").²⁸⁹ In both Canada and the United States there is a problem of coverage because less than half of each nation's workers are covered by private pension

fy him in having an expectation of surviving for at least one year thereafter." Canada Pension Plan, R.S.C., ch. C-8, § 63(7) (1985) (Can.). The QPP contains essentially the same provision. 2 Pension Guide-QPP, *supra* note 284, ¶ 35-453, § 114.

287. See 42 U.S.C. § 416(c)(5) (1988); see also *supra* note 59 (discussing circumstances in which surviving spouse may collect benefits in marriages lasting less than nine months).

288. See Canada Pension Plan, R.S.C., ch. C-8, § 6(2)(b) (1985) (Can.). Other categories of employers are also exempted such as employers of migratory workers, some governmental employees, members of the judicature covered under a special plan, certain types of miscellaneous employment such as members of a religious order who have taken a vow of poverty, those who are dependents of the employer who do not receive cash remuneration, and employment as an exchange teacher from a foreign country. *Id.*

289. See Pension Benefits Standards Act, 1985, R.S.C., ch. 32, § 2 (2d Supp. 1988) (Can.).

plans.²⁹⁰ This makes the private system expensive and inefficient because the taxpaying public must support the system through tax subsidies.²⁹¹ For those not covered under the private system and who are in need, the government must provide extra benefits for which the taxpayers must pay.

In both countries, it has been suggested that the private retirement system would be much improved with a mandatory system under which all workers are covered.²⁹² In both countries, however, such a proposal has been opposed by management on two grounds. The first, and most frequently articulated objection, is that such a program would be expensive. The second objection is that management would lose control of the considerable assets currently held under the private retirement system. In both Canada and the United States, these assets represent the single largest source of new investment capital.²⁹³ Thus, the business community is reluctant to lose control over this important source of capital.

In both countries, the private pension system was strengthened by federal legislation enacted in the mid-1980s.²⁹⁴ The Canadian reform, however, was much stronger than the U.S. attempt. Under

290. The percentage of covered workers in Canada is less than in the United States. In 1985, 41.8% of American workers were covered, while in 1984, 36.8% of Canadian workers were covered. See RICHARD L. DEATON, *THE POLITICAL ECONOMY OF PENSIONS* 74-85 (1989). Non-covered workers are typically in "poorly paid, non-unionized, labor intensive industries characterized by either a competitive product market or a high proportion of women workers." *Id.* at 85. This is true for both Canada, the United States, and Britain. *Id.*

291. See Income Tax Act, R.S.C., ch. 1, §§ 144(2), 145(2), 146(4)-(5.1), 146.1(5), 146.3(3), 147(7), 147.2(4), 149(1) (5th Supp. 1992) (Can.).

292. See, e.g., FINAL REPORT OF THE PRESIDENT'S COMMISSION ON PENSION POLICY, *COMING OF AGE: TOWARD A NATIONAL RETIREMENT INCOME POLICY*, reprinted in *The Future of Retirement Programs in America: Hearing Before the House Select Comm. on Aging*, 97th Cong., 1st Sess. 160-64 (1981) (proposing mandatory minimum universal pension system in U.S.); John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy In Canada*, in OLD AGE POLICY, *supra* note 110, at 92-94.

293. See John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy In Canada*, in OLD AGE POLICY, *supra* note 110, at 84, 93; see also *supra* part II.E (discussing value of pension assets in the United States).

294. See Pension Benefits Standards Act, 1985, R.S.C., ch. 32 (2d Supp. 1985) (Can.); Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085 (1986) (codified as amended in scattered sections of 26 U.S.C.). In order to qualify for tax incentives under the Canadian system, the plan must be registered either with the province, in the case of a provincial plan, or with the federal government, in the case of plans for government workers or federally controlled industries. Registered plans must then comply with the Canadian federal law for tax benefits. See Income Tax Act, R.S.C., ch. 1, §§ 146(1), 147.1(2) (5th Supp. 1992) (Can.).

Although the private pension laws were strengthened, nothing was done in either country for those whose retirement security depends almost exclusively on the public sector.

the Canadian system, all federally regulated industries must provide vesting of employer contributions after two years,²⁹⁵ as opposed to three- to seven and five-year vesting under the American system.²⁹⁶ The Canadian system also provides for portability of vested benefits, for voluntary inclusion of part-time employees, and for a minimum survivor benefit equal to sixty percent of the retirement pension payable on the death of a spouse.²⁹⁷ This stands in contrast to the fifty percent payable under the American system.²⁹⁸

Survivors who have been married only a short time are also treated differently under the two systems. Under U.S. law, plan sponsors may treat short-term marriages (less than a year in duration) as irrebuttably void for purposes of survivor benefits.²⁹⁹ Thus, the survivor is treated as having contributed nothing of value to the marriage if the survivor and the decedent have not been married for the requisite time period.³⁰⁰ Accordingly, the survivor may be denied benefits solely on the basis of an arbitrarily imposed time period with no consideration of other factors.³⁰¹

This difference in the treatment of survivors of short-term marriages under the two systems is significant because it highlights the difference in ideology behind the Canadian and American private retirement systems. The Canadian system comes closer to a realization that retirement benefits are earned by the worker and should belong to that worker as a matter of right. The American system still retains a vestige of the theory that retirement benefits are a gratuity from the employer and the worker has no inherent right to these benefits.³⁰²

295. See Pension Benefits Standards Act, 1985, R.S.C., ch. 32, § 17(1) (2d Supp. 1988) (Can.).

296. See I.R.C. § 411(a) (1988 & Supp. IV 1992). *But cf. supra* note 211 (discussing ten year vesting under multi-employer plans).

297. See Pension Benefits Standards Act, 1985, R.S.C., ch. 32, §§ 15, 22(3), 26 (2d Supp. 1985) (Can.).

298. See I.R.C. § 417(b) (1988 & Supp. IV 1992). These are minimum provisions. A plan may be more lenient, but it may not be more restrictive.

299. See *id.* § 417(d). This too is a minimum statutory requirement. A plan sponsor may choose to provide more liberal provisions. *Id.* § 417(d)(1).

300. The survivor and the decedent must have been married throughout the one-year period ending on the earlier of the annuity starting date or the date of the decedent's death. *Id.* § 417(d).

301. For a discussion of the historical background and inequities of this provision, see Watson, *supra* note 235, at 493.

302. See *id.* at 491-92.

2. Registered Retirement Savings Plans ("RRSPs")

RRSPs are individual savings plans similar to IRAs,³⁰³ but with higher tax deductible contribution limits.³⁰⁴ For 1993, an individual may contribute up to the lesser of eighteen percent of earned income or \$13,500,³⁰⁵ minus a "pension adjustment," of the deemed value of any benefits accruing under an employer-sponsored registered pension or deferred profit sharing plan.³⁰⁶ Such a system allows contributions by homemakers and others without earned income who have historically been excluded from the private pension system.

The spousal RRSP rules are much more progressive than their American counterparts. The Canadian system allows for income splitting of the amount of the RRSP contribution³⁰⁷ and, until 1995, for the transfer of annuity income up to a limit of \$6000 per year from an employer-provided pension plan into the spousal RRSP.³⁰⁸

IV. CANADIAN AND AMERICAN NATIONAL HEALTH SYSTEMS

In contrast to the American national health system (i.e., Medicare), which exists only for the elderly and which is an expensive and inefficient system due to the many gaps in coverage, Canadians have a universal, comprehensive national health system of which they are justifiably proud. Although the Canadian national health system, called Medicare, has been criticized as expensive, inefficient, and outdated,³⁰⁹ the facts are otherwise.³¹⁰ Before the

303. For example, investment earnings accumulate tax free and contributions, to a point, are tax-deductible. See *Income Tax Act*, R.S.C., ch. 1, § 146(4)-(5) (5th Supp. 1992) (Can.).

304. The maximum tax-deductible contribution for an IRA is currently \$2000. See *I.R.C.* § 219(b)(1)(A) (1988 & Supp. IV 1992).

305. See *Income Tax Act*, R.S.C., ch. 1, § 146(1) (5th Supp. 1992) (Can.); 1 Canadian Pension Guide, *supra* note 255, ¶ 4584.

306. See 1 Canadian Pension Guide, *supra* note 255, ¶ 4584.

307. Establishment of a spousal registered retirement savings plan ("RRSP") does not raise the deductible contribution limit, but it does allow any amount up to the deductible limit to be contributed to a spousal RRSP. Thus, when the contributions are later withdrawn, they may be taxed at a lower marginal rate. See *Income Tax Act*, R.S.C., ch. 1, § 146(5.1) (5th Supp. 1992) (Can.); 1 Canadian Pension Guide, *supra* note 255, ¶ 4650. Under the U.S. system, the contribution amount may be increased by only \$250 for a spousal IRA. See *I.R.C.* § 219(c)(2) (1988 & Supp. IV 1992).

308. See 1 Canadian Pension Guide, *supra* note 255, ¶ 4654.

309. See, e.g., Ian R. Munro, *How Not to Improve Health Care*, *READER'S DIG.*, Sept. 1992, at 49 (arguing Canadian Health Care System results in long waits for

Medicare system was enacted, Canada and the United States spent about the same percentage of their national income for medical care.³¹¹ Today, Canada spends a significantly smaller percentage than the United States while providing comprehensive health care for everyone.³¹² Moreover, drugs in Canada are much cheaper than in the United States.³¹³ Canadians are not assigned a particular doctor, but have free choice, and most Canadians are pleased with the medicare system.³¹⁴

Most of the criticism of the system focuses on long waits for treatment and lack of advanced technology.³¹⁵ However, Canadian government statistics reveal that ninety-six percent of Canadians over age fifteen receive care within seven days of making a request.³¹⁶ Furthermore, Canada does not lack modern medical technology. Rather, the question has been raised whether the United States has a surplus of high technology equipment that is overpriced, and in many cases, only marginally effective.³¹⁷

There is little doubt that the Canadian poor generally have a better quality of life than their American counterparts. This variance cannot be attributed to economics, because, on a proportional basis, Canada's federal budget deficit is comparable to that of the United States.³¹⁸ Nor is it attributable to a stronger system of government, because Canada's system of federalism is threatened by Quebec separatism.³¹⁹ The Canadian Medicare system is administered by the provinces, although the federal government shares half of the cost as long as the provincial plan conforms to federal standards.³²⁰ In this regard, it is much like the American system.

surgical care, abuse of emergency services, overuse, and demoralized physicians).

310. Eric B. Moch, *Canadian Health Care Isn't Perfect, But It Works*, ST. PETERSBURG TIMES, Oct. 25, 1992, at 2 (criticizing comments on Canadian System by George Bush, Paul Tsongas, and Newt Gingrich as wrong and misleading).

311. See Theodore R. Marmor & John Godfrey, *Canada's Medical System is a Model. That's a Fact*, N.Y. TIMES, July 23, 1992, at 23A (comparing American and Canadian figures in 1971 when Canadian Medicare became effective).

312. See *id.* (stating United States spent 12.3% of GNP while Canada spent 9.2% of its GNP for medical care in 1991).

313. See Philip J. Hilts, *Canada is Found to Lead U.S. in Holding Drug Prices Down*, N.Y. TIMES, Feb. 22, 1993, at 11A (finding drug prices in Canada to be more than 40% lower than in United States according to GAO report).

314. See Marmor & Godfrey, *supra* note 311, at 23A.

315. *Id.*

316. *Id.*

317. See *id.*

318. Anne Swardson, *Owe Canada: Debts Mount North of Border*, WASH. POST, Mar. 17, 1993, at C1.

319. See Marmor & Godfrey, *supra* note 311, at 23A.

320. See Medical Care Act, ch. 64, 1966-1967 S.C. 563, 564-66 (1966) (current

There are two probable reasons why Canada offers its citizens a better health care system than the United States offers its citizens. The first, and most important reason, is that there is a tremendous difference in ideology between the two nations, even though both have been under conservative political regimes for approximately the same amount of time. The Canadian premise is that health care is a right of citizenship.³²¹ The United States, on the other hand, views it as a political issue. Second, Canada has been serious in acting on its premise.

The ideological contrast between the two countries is most striking in the role of federalism in the welfare and national health systems. In the United States, federalism has been a destructive force for both welfare programs and the Medicare system.³²² Pervasive federal benefit cuts combined with simultaneous cuts in federal funding to the states have stifled the effective operation of both systems. Not only have the federal cuts created a funding problem for the states, but the extent of federal cuts in the welfare and medicare programs sends the message that these programs are not worthwhile. In Canada, however, the provinces have had much more control over the welfare and national health systems. The result has been a more progressive and popular system than in the United States, where Congress has sought to appease the maximum number of constituents by exerting the minimum possible effort.

Machiavellian principles could explain why the United States does not have a universal comprehensive health care system. The interests and needs of the politically vulnerable are ignored in order to accommodate the interests of the politically powerful, in this case the American Medical Association and the insurance industry. Why? Because, according to Machiavelli, "men are inclined to think that they cannot hold securely what they possess unless they get more at others' expense."³²³

Another problem under the American Medicare system is that

version codified at R.S.C., ch. C-6 (1985) (Can.)).

321. See, e.g., Canada Health Act, ch. 6, 1984 S.C. 5 (codified at R.S.C., ch., C-6, § 3 (1985) (Can.)) ("It is hereby declared that the primary objective of Canadian health care policy is to protect, promote and restore the physical and mental well-being of the residents of Canada and to facilitate reasonable access to health services without financial or other barriers.").

322. See *supra* part II.C.1 (discussing lack of consistency among various medicaid programs in states and weakening of social welfare system); see also *supra* notes 75-76 (noting lack of organization in administration).

323. NICCOLO MACHIAVELLI, THE DISCOURSES 118 (Leslie J. Walker trans., Bernard Crick ed., Penguin Books 1987) (1531). Machiavelli goes on to state: "Furthermore, those who have great possessions can bring about changes with greater effect and greater speed." *Id.*

the system has not progressed since its inception. For instance, there is no emphasis on preventive medicine. The system also lacks the proper focus on mental health and long-term care. This lack of progressive thinking has been termed by one observer as "penny wise and pound foolish."³²⁴

V. POLITICAL IMPLICATIONS OF REFORM AND LESSONS FROM THE CANADIAN EXPERIENCE

A. *The Social Security System*

The first question here is whether the Social Security system should be reformed, and if so, how? In order to answer this question, the main components of the system must be examined: OASDI, the welfare programs, and Medicare.

The Omnibus Reconciliation Act of 1993 increases the amount of Social Security benefits subject to taxation.³²⁵ The tax increase on Social Security benefits amounts to a benefit cut for most taxpayers. The question is whether this tax increase is wise from a policy perspective.³²⁶

There is no question that entitlements constitute a drain on the federal budget and detrimentally affect the federal budget deficit. However, OASDI and welfare benefits have only a marginal effect.³²⁷ The majority of the growth in entitlement spending has come from Medicare and Medicaid, which have been affected by the growth in health care costs.³²⁸

Drawing from the Canadian experience and lessons of the history of attempted Social Security reform in the United States, it will be very difficult, from a practical perspective, to reform the OASDI. This is due to the same political implications that have made it difficult for Canadians to reform their system. For instance, during both the 1988 and 1992 presidential campaigns, President Bush

324. *Older Women's Health: Hearing Before the House Task Force on Social Security and Women of the Subcomm. on Retirement Income and Employment and the Select Comm. on Aging*, 99th Cong., 2d Sess. 3 (1986) (statement of Rep. Mary Rose Oakar, Chairwoman). Representative Oakar went on to say: "If we dealt more with comprehensive care, in the long run we would save everyone a lot of money, including the Government." *Id.*

325. *See supra* note 29 (discussing increase in Social Security benefits subject to taxation).

326. *See* John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in *OLD AGE POLICY*, *supra* note 110, at 93.

327. Since 1975, old-age pensions and other social welfare programs have grown by an average of 1.1% per year in inflation-adjusted dollars. *See* AARP REPORT, *supra* note 123, at 2, 6.

328. *See id.* at 7-8.

said he would oppose any changes in the Social Security system³²⁹ and, indeed, there were no changes during his administration. This is attributable to the immense popularity of OASDI.³³⁰

The Canadian experience, on the other hand, has been strikingly different from the American experience. In the mid-1980s, while the Reagan administration was busy trying to dismantle the Social Security system, the political climate in Canada was also conservative, but the effort was directed toward expanding the welfare state. In 1984, when newly elected Prime Minister Brian Mulroney launched an attack on the universal demogrant program for children and the elderly in order to "better target social expenditures on those most in need,"³³¹ the attack met broad-based opposition.³³² The Prime Minister's Progressive Conservative government then suffered what has been termed "its single most important political setback to date" when it was forced to withdraw its proposals.³³³

In 1989, the Progressive Conservatives did achieve a victory over the welfare state, although not on as large a scale as their 1984 proposal. The victory involved a clawback of benefits provided under the universal old-age benefit program from elderly persons with incomes greater than \$50,000 per year.³³⁴ The reason this attack was successful was because it was couched not as an attack on the welfare state, as such, but in terms of "mak[ing] the welfare state more efficient by targeting scarce transfer dollars to those most in need."³³⁵

Compared to the American system, however, the Canadian welfare state has been relatively immune from attack. This is primarily due to the concept of middle class incorporation, which is probably stronger in Canada than in the United States because of the important comprehensive Canadian national health system. In

329. See Paul Blustein, *Nominees' Economic Goals Seen as Lacking Realism*, WASH. POST, Oct. 20, 1988, at A1; Douglas Frantz, *Elections '92: Budget Watchers Check Off Reactions to Bush's Tax Plan*, L.A. TIMES, Aug. 22, 1992, at A14.

330. See *supra* notes 111-15 and accompanying text (discussing middle class incorporation).

331. John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in OLD AGE POLICY, *supra* note 110, at 85. Specifically, Prime Minister Mulroney proposed to pay for the changes by de-indexing universal old age benefits. *Id.*

332. Opposition came from organized labor, women's groups, antipoverty lobbies, and the general public. See *id.*

333. *Id.*

334. See Ferguson, *supra* note 269, at B1.

335. John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in OLD AGE POLICY, *supra* note 110, at 85.

contrast, American Social Security benefits assume less and less importance each year as a percentage of medical costs, which continue to uncontrollably skyrocket.

B. *Private Retirement System*

In both countries, it has been suggested that the private retirement system be made mandatory for all employers, as well as for self-employed.³³⁶ While the lobby against such a mandatory system has been powerful in both countries, the Canadian private retirement system is closer to a mandatory system than is its American counterpart. In the early 1980s, Canadians engaged in an interesting debate involving expansion of the public retirement system (OAS) over the private system of occupational pensions and RRSPs. The impetus behind this debate was a realization that the public system was far superior to the private system because of its more lenient vesting provisions, its portability, and the fact that its benefits were indexed for inflation.³³⁷

While such an expansion was favored by organized labor, it was opposed by business leaders who were loath to lose the single most important source of new investment capital in the Canadian economy.³³⁸ The result of this debate was a strengthening of the private retirement system under the Pension Benefits Standard Act of 1985³³⁹ and a strengthening of the public assistance program, but with very little available for those caught in between, many of whom are women.³⁴⁰ It is unlikely that anything will be done for those who were left out of the 1985 legislation because the probable result of the reform is that the liberal element has now been appeased with a system of fortified guaranteed income supplements to the poor.

Both countries allow the practice of integrating the public system with the private system.³⁴¹ This has the effect of reducing private retirement benefits for the lower paid employees because they

336. See *supra* note 292.

337. See John Myles & Les Teichroew, *The Politics of Dualism: Pension Policy in Canada*, in OLD AGE POLICY, *supra* note 110, at 92-93.

338. See *id.* at 92-94. Further, not only would business leaders lose control over this capital, but it would be shifted to government control. *Id.* at 93-94.

339. See Pension Benefits Standards Act, 1985, R.S.C., ch. 32, § 17(1) (2d Supp. 1988) (Can.); see also *supra* text accompanying notes 294-98 (discussing strengthening of Canadian retirement system).

340. For a general discussion of the limitations of the private pension system see DEATON, *supra* note 290, at 74-117.

341. See I.R.C. § 401(a)(5) (1988 & Supp. IV 1992); 1 Canadian Pension Guide, *supra* note 255, § 2322.

receive greater proportionate benefits under the public system. In the United States, it has been strenuously argued that eliminating integration would raise the cost of an employer-provided plan, and that many employers would simply discontinue their plans or reduce benefits.³⁴² Opponents argue that the number of integrated plans increased from forty-five percent of covered employees participating in these plans in 1980, to sixty-three percent in 1989.³⁴³ This is a worrisome statistic considering that the structure of OASDI benefits is weighted toward the poor in order to help alleviate poverty, and that private retirement plans receive considerable tax subsidies as an incentive.³⁴⁴

C. National Health System

The bulk of Americans with health insurance coverage are employed by large businesses.³⁴⁵ While there are some innovative programs that have been implemented on the state level to insure that employees of small businesses have health insurance, these programs are voluntary, and only a small number of businesses currently participate.³⁴⁶

A recent poll indicated that most Americans are more con-

342. See, e.g., *Pensions: Congressional Study Panel Presents Findings on Equalizing Benefits For Women*, DAILY TAX REP. (BNA) No. 187, at G-S (Sept. 25, 1992) [hereinafter *Equalizing Benefits Study*] (statement of Anna M. Rappaport, managing director, William M. Mercer, Inc.). The theory behind this argument is that employers pay half of the workers' Social Security benefits so they should be able to reclaim this amount from their pension payments. Moreover, the more highly paid employees are "discriminated against" under the Social Security system and should therefore be compensated under the retirement plan. See *How Well Do Women Fare Under the Nation's Retirement Policies?: Hearing Before the House Select Comm. on Aging*, 102d Cong., 2d Sess. 21 (1992).

343. See *Equalizing Benefits Study*, *supra* note 342, at G-6.

344. *Id.* (statement of Nancy Altman). Furthermore, Social Security benefits are intended to be a supplement to other income, and the size of the benefits proves this. The current maximum benefit for a married couple where both have worked and are entitled to maximum benefits is \$26,112 per year. See Georgette Jasen, *A Secure Retirement Takes Long Years of Sound Planning, Even After It Begins*, WALL ST. J., May 29, 1992, at C1. For a computation of Social Security benefits see U.S. DEPT. OF HEALTH AND HUMAN SERV., SOCIAL SEC. ADMIN., ANNUAL STATISTICAL SUPPLEMENT 130-44 (1993).

345. See PIACENTINI & FOLEY, *supra* note 42, at 181 tbl. 6.18.

346. See, e.g., Eugene Carlson, *Florida Tries Remedy for Health-Insurance Ailments*, WALL ST. J., Oct. 21, 1992, at B2 (discussing program for small businesses in Florida). Florida officials are optimistic about the response to the program, however, because of the time and expense involved in reaching small businesses, the experimental nature of the program, and the fact that approximately a quarter of the small businesses signing up have not offered health insurance coverage in the past ten years. *Id.*

cerned with Medicare benefits than with Social Security benefits, and would be willing to accept less Social Security in return for more Medicare.³⁴⁷ The concern over health care coverage is apparently growing.³⁴⁸

Another related concern is fairness in health coverage and benefits. Consider, for example, the case of *McGann v. H & H Music Co.*,³⁴⁹ in which an employer altered the terms of a health plan to reduce lifetime benefits from \$1 million to \$5000 for an employee with an AIDS-related illness. The employer's right to reduce benefits after claims were filed was upheld on appeal.³⁵⁰ The inequities in this case have prompted Congressional hearings.³⁵¹

A problem which contributes to the spiraling cost of health care is the high cost of drugs. A recent study shows that the United States drug price inflation from the manufacturer between 1980 and 1992 was 128%, approximately six times the overall rate of inflation during that period.³⁵² Drug manufacturers defend their high prices by blaming research and development costs.³⁵³ It has been shown,

347. See Christopher Conte, *Labor Letter: A Special News Report on People and Their Jobs in Offices, Fields and Factories*, WALL ST. J., Sept. 22, 1992, at 1A; see also, Hillary Stout, *Seeking a Cure: Most Americans Pledge Sacrifice to Help Fix the Health System*, WALL ST. J., Mar. 12, 1993, at 1A (finding 66% of those polled willing to pay higher taxes; 52% willing to accept limits on right to choose doctors; 46% willing to accept higher insurance deductibles and co-payments). However, some polls indicate that the support for health-care reform falls dramatically when the trade-offs are fully explained. These trade-offs include higher taxes, restricted physician visits, and limited ability to sue a health care provider under the system. See *Health Care: Next President Will Be Hampered in Health Care Reform, Pollsters Say*, Daily Tax Rep. (BNA) No. 199, at G-5 (Oct. 14, 1992) (remarks of Greg Schneiders, President, Frederick/Schneiders Inc., Democratic polling firm, Washington, D.C.).

A recent survey of senior citizens indicated that the elderly are not willing to pay higher taxes for reform. See Fabrizio Memorandum, *supra* note 87, at 12. However, many of the elderly are living on fixed incomes with no inflation protection, and they may have a general distrust of government reform efforts having been "burned" under the Medical Catastrophic Coverage Act of 1988. See *supra* notes 137-42 and accompanying text.

348. See, e.g., Cathy Trost, *A Special News Report on People and Their Jobs in Offices, Fields and Factories*, WALL ST. J., Oct. 13, 1992, at 1 (stating recent William M. Mercer survey shows that "quality health care is more of a concern now than it was three years ago").

349. 946 F.2d 401 (5th Cir. 1991), *cert. denied sub nom.* Greenberg v. H & H Music Co., 113 S. Ct. 482 (1992).

350. *McGann*, 946 F.2d at 403.

351. See *Oversight Hearing on ERISA and Cutbacks in Health Benefits: Hearing Before the Subcomm. on Labor-Management Relations of the House Comm. on Education and Labor*, 102d Cong., 2d Sess. *passim* (1992).

352. See STAFF REPORT OF SENATE SPECIAL COMM. ON AGING, 103D CONG., 1ST SESS., EARNING A FAILING GRADE: A REPORT CARD ON 1992 DRUG MANUFACTURER PRICE INFLATION 1 (Comm. Print 1993).

353. *Id.* at 2.

however, that thirty-five percent of the cost of the average prescription goes to pay for marketing and advertising, while only sixteen percent of this cost is used for research and development.³⁵⁴

Although drug companies are posting record-breaking profits, they are being subsidized by the taxpayers through the federal government.³⁵⁵ Drug companies are permitted various tax credits,³⁵⁶ including one for operating in Puerto Rico and other qualifying Caribbean Basin countries if they employ local workers.³⁵⁷ This credit amounts to a significant loss of tax revenue.³⁵⁸ Legislation has been introduced in the past to eliminate this credit,³⁵⁹ but to date, it remains.

One solution under consideration to control the high cost of health care and to provide a possible means of financing health care reform is the taxation of employee health benefits. Such a proposal has been opposed by the AFL-CIO on the ground that it would constitute a regressive tax on the middle class. According to the AFL-CIO, such a tax would be "an unfair burden on workers who are already sacrificing income to maintain health coverage,"³⁶⁰ and the tax would "force[] people to use the health care plan with the lowest cost."³⁶¹

VI. CONCLUSION

The Canadian retirement, welfare, and national health systems offer many examples for reform of the American systems. The Cana-

354. *Id.*

355. *Id.* at 1.

356. *See* I.R.C. § 28 (1988 & Supp. IV 1992) (tax credits for orphan drug research); *id.* § 41 (tax credits for research and experimentation).

357. *See id.* § 936.

358. It is estimated that the elimination of this credit alone would save \$3 billion in the first year and up to \$20 billion over 5 years. *See Tax Credits: Senators Say Drug Company Tax Breaks Need to Be Re-examined*, Daily Tax Rep. (BNA) No. 22, at G-1 (Feb. 4, 1993) (statement of Sen. David Pryor).

359. *See* S. 876, 103d Cong., 1st Sess. (1993); H.R. 1960, 103d Cong., 1st Sess. (1993). For a discussion of the effect of the elimination or reduction of the credit on the Puerto Rican economy, see GEN. ACCOUNTING OFFICE, REPORT TO SEN. FINANCE COMM., 103D CONG., 1ST SESS., PUERTO RICO AND THE SECTION 936 TAX CREDIT (1993).

360. *Health Care: Taxing Health Benefits is Regressive AFL-CIO Poly Analyst Tells Briefing*, Daily Tax Rep. (BNA) No. 27, at G-3 (Feb. 11, 1993) (quoting AFL-CIO's goals statement). The AFL-CIO Health Care Reform Bulletin states that workers, in the past, have bargained for health care benefits instead of higher pay in order to protect their families. Taxing health care benefits in the future, would penalize those workers. *Id.*

361. *Id.* (quoting Claudia Bradbury, Policy Associate, AFL-CIO Employee Benefits department).

dians have shown that a universal, comprehensive, national health-care system can be accomplished with much more cost-effective results than the present American system of Medicare and Medicaid. In many other ways, the Canadian retirement and welfare system is designed better than the American system.

The American retirement system should be revamped. There can be no retirement security in the United States without a comprehensive national health system. Such a system can be accomplished, in part, by changing Social Security from a system of social insurance to a system of social assistance,³⁶² and redirecting the remaining resources toward a comprehensive national health system. While there may still be a minimum threshold of OASDI benefits, the social assistance system should be changed from a means-tested system to an income-tested system for the truly needy. The advantage of eliminating the OASDI system as a system of social insurance and instead implementing a national health system is that true retirement security is offered, not just an empty promise, because there will be a cap on the rising health care costs.

Currently, where medical costs rise faster than the cost-of-living, OASDI benefits decline in importance every year. The needs of society have changed since 1935. With improved nutrition and medical advancements, life expectancy has increased and quality of life is better, although medical care currently remains the greatest expense for the elderly. Cutting OASDI benefits will not be a popular political move, but it is a rationally feasible move because benefits which are declining in importance may be redirected for the benefit of the entire populace, not just the elderly, although the elderly will also benefit.³⁶³

A more Keynesian approach to national health policy is needed because the American medical establishment and insurance industry have been more concerned with their own narrow, self-serving interests than with the greater good of society—particularly with respect to those who lack the basic health care necessities. In this regard, Machiavellian principles may play a beneficial role. With health costs spiralling out of control, there may be an opportunity (similar to that presented to President Roosevelt when he established the Social Security system) to “incorporate” the middle class

362. Note that the middle class incorporation principle discussed above, *see supra* notes 111–24 and accompanying text, may not hold true much longer because of the erosion of Social Security benefits under OBRA '93. *See supra* note 29 (discussing tax increase of Social Security benefits).

363. The cut will have to be phased in because too many of the elderly currently depend on OASDI benefits. I propose no cut to SSI. In fact, SSI may have to be expanded, although the national health system will help in the war against poverty.

into a national health care system. If such a national system is perceived as the only means of facing the uncertainty of those costs, self-interest will convince the middle-class to throw their support behind it. Once incorporated, their reliance on its benefits will defeat attempts to repeal or roll back health benefits.

The question may be raised why Canada offers its citizens a better society. Why is there such a difference in national ideology? This difference cannot be explained by political ideology alone because Canada also has had conservative administrations that have been intent upon dismantling the welfare state. However, Canadian conservatives have not had the same success with restraining the welfare state as American conservatives.

Perhaps one explanation for this phenomenon is that Canadian government economists are more Keynesian in their approach than American government economists. This Article has offered another explanation, although not necessarily mutually exclusive, in the application of Machiavellian principles. The United States is a wealthier nation than Canada and the prevailing attitude in this country has been "me first." In a wealthier society, there is less interest in the well-being of one's fellow man. In a less wealthy society, there is more of a general inclination to pull together for the greater good.³⁶⁴ While this is a simplistic explanation, nevertheless, it is a well-known principle that the strong will generally overrun the weak.

The United States badly needs a Keynesian expanded government program of welfare and national health but less government intervention in the private retirement realm. The private retirement system should be a mandatory system, covering all workers, with minimal tax benefits afforded to employers. Mandatory coverage will compensate for loss of OASDI benefits and cutting the tax benefits of private plans will provide further funding for a national health system.³⁶⁵ Additionally, the complexity in the present system will be alleviated.

However, such an expansion of the welfare system and the implementation of a universal national health system will involve a substantial level of redistribution and a very organized public effort to defeat private lobbying efforts by powerful special interest groups who do not have the welfare of the American public in mind. It is critical that action be taken soon because the American system, unlike the Canadian system, lacks the proper infrastructure of an

364. See, e.g., BRYDEN, *supra* note 10, at 19-43 (discussing Canadian experience).

365. Current revenue lost to tax benefits for private retirement plans amounted to \$54 billion in fiscal year 1992. See AARP REPORT, *supra* note 123, at 1.

adequate retirement security system. When the baby boomers begin to retire shortly after the turn of the century, it will be too late to consider reform. The clock is ticking now. Such drastic reform will not be popular because of middle class incorporation on the one hand and neoconservative ideology on the other. Nevertheless, a final lesson may be learned from Machiavelli:

No government should ever believe that it is always possible to follow safe policies. Rather, it should be realised that all courses of action involve risks: for it is in the nature of things that when one tries to avoid one danger another is always encountered. But prudence consists in knowing how to assess the dangers, and to choose the least bad course of action as being the right one to follow.³⁶⁶

366. THE PRINCE, *supra* note 2, at 79.

