

contributions. This situation is common at the beginning of a system, since full benefits are frequently awarded to workers who have contributed to the retirement plan for only a fraction of their working lives. This practice gives rise to "past service credits," the liability which future beneficiaries (or the employer) must bear. Past service credits are also generated when a mature retirement system is liberalized, to the extent that those near retirement age partake of liberalized benefits without having had to make commensurate contributions.

The similarities between past service credits in group insurance and the aspect of OASDI make equating of the two types of programs tempting. Despite this similarity, the analogy between group insurance and social security is just as tenuous and misleading as the more general analogy between individual insurance and social security. One obvious difference is that failure of a firm to pay premiums for a group insurance plan terminates the insurance for all members of the group, whereas employees covered by OASDI are credited with quarters of coverage even if the firm does not pay the tax due.

The key distinction between the two approaches—private insurance and social security—turns on whether an individual currently in the labor force and paying taxes into the social security trust funds is paying for the benefits of current retired workers and survivors or for his own or his family's future benefits. In individual insurance, each person's premiums are contractually tied to his own and his family's future benefits. No insurance company knows how many new policies it will sell, and, therefore, does not know the amount of its future cash inflow from premiums. Consequently, it must charge its present customers enough to create a reserve fund sufficiently large to meet its future financial obligations.

In social security, on the other hand, the level of payroll taxation is set to defray costs of benefits for the *currently* retired. The social security program (for very good reasons discussed in chapter 7) has been financed on a virtual cash or pay-as-you-go basis in recent years. The accumulated reserves are sufficient to cover only approximately 1 year of benefit payments at present benefit levels. Moreover, on balance, the reserves have not increased in the last decade. It is true that most social security bills project surpluses in the distant future, but these are quickly eliminated by later legislation. Each new law contains benefits and taxes that provide a rough balance in the trust funds for the first couple of years, with surpluses projected thereafter. Before the surpluses are realized, however, benefits are liberalized, new tax rate increases are scheduled for future dates, and the cycle is repeated. In other words, the money which workers currently pay into the funds is not stored up or invested, but, is paid out concurrently as benefits to the various categories of current beneficiaries. Workers pay for benefits to eligible nonworkers. The future benefits of present workers, their dependents, or their dependent survivors will be paid in similar fashion out of the contributions of the working population as of some future date.

The fact that a fund is not accumulated at some explicit interest rate does not imply that an individual in the OASDI retirement program fails to share in the growth of the economy. Economic and population growth assures to the average individual covered by the