

less burden is involved for individuals in a collective sense when the full cost of benefits is recognized currently and the excess of future over current costs is funded according to a systematic program. The reasoning runs as follows:

1. The excess of current contributions over current benefit payment; that is, pension saving, finances capital formation. As a result, productivity gains are greater than would otherwise be the case.

2. As the pension system matures, or comes closer to maturity, the increasing transfers of output to beneficiaries are made from a larger total output. The fraction of the current output transferred from active to retired workers is, therefore, a smaller and less burdensome one.

3. If a cohort of workers over their active working years saves the capital accumulation and the earnings on it to enlarge total output sufficiently to generate the goods and services which will satisfy their claims in retirement, it has placed minimal burdens on other workers.

However, this line of reasoning is based on a series of assumptions which are probably not equally valid. In the first place, it is assumed that investment will expand to absorb the full addition to savings at full-employment levels of output. A study by Simon Kuznets supports this assumption.¹¹

Second, it is assumed that benefits are in a fixed relationship to past savings. This is surely not entirely valid. In fact, we know that economic growth and rising living standards will be accompanied by improvements in the level of benefits, involving a supplemental transfer of current output from the working to the retired group. However, if inflation erodes the real value of money claims, the price rise will partially offset this supplemental transfer process.

In summary, the maturing process never ends in a growing economy. There is a rising level of aspirations which results in transfers to retired workers in excess of what they have contributed through pension saving. Our reasoning, therefore, is that the burden of pension benefits is lessened when they are provided at least in part from additions to saving which has been employed in incremental capital formation to expand real output. This should be true on the average for individual burdens and for the burden on productivity of the economy as a whole. One of the conditions promoting this result is a minimal effect on the incentives of those engaged in production.

Pay-as-you-go arrangements and those which use the taxing power of Government to make transfers of income are, in this sense, the most burdensome pension program since they entail no contribution to capital formation.¹² We should be cautious about reaching fixed conclusions on these matters. Within broad limits, the tolerance levels of individuals to accepting burdens and limitations of their expenditure decisions are not fixed for all time. We know that people can and do adjust to all kinds of circumstances, including burdens. This process takes

¹¹ *Capital in the American Economy: Its Formation and Financing*, Princeton University Press for NBER, 1961.

¹² Pay-as-you-go plans of industrial organizations or of Government, of course, need not be more burdensome in every case. Contributions not made to fund future costs may be directly invested to produce future productivity gains from which rising benefit payments can be met. The after-tax return from these direct investments must be persistently high relative to the cost of capital from other sources to make pay-as-you-go programs less burdensome than those which are systematically funded.