SHARED RESPONSIBILITY, SHARED RISK

GOVERNMENT, MARKETS, and SOCIAL POLICY in the TWENTY-FIRST CENTURY

edited by
Jacob S. Hacker
Ann O'Leary

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and

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Contents

Part Three IMPROVING ECONOMIC SECURITY FOR FAMILIES

Part Four INCREASING HEALTH AND RETIREMENT SECURITY

Part Five CONCLUSIONS

Foreword

Shared Responsibility

CRAIG CALHOUN

The financial crisis of 2008 drew attention to the extent to which some private actors could create enormous public risks. Banks engaged in proprietary trading (that is, for their own and not their customer's benefit), hedge fund managers traded credit default swaps, finance companies issued dubious mortgages then bundled them into securities that ostensibly more prudent investors not only bought but used as collateral for leveraged purchases. Ironically, much of this explosion in financial activity was actually done in the name of risk management. Instruments were created for trading risk and for trading on market fluctuations. The marketization of risk actually enhanced vulnerability in certain ways, however, notably by making actors in the financial system highly interdependent, reducing the transparency of trades and asset values, and scaling up demands for liquidity. When this highly leveraged and minimally transparent financial system crashed, governments stepped in, using public funds to shore up the markets and those institutions deemed "too big to fail."

There has been a great deal of attention to how ordinary taxpayers bore the consequences of risk-taking by large firms and wealthy individuals. But it is not only as taxpayers that individual citizens and families are vulnerable to economic upheavals, risks created by highly volatile markets or new technologies, or indeed the frauds of big investors who break the rules. They also bear the consequences through unemployment, lost health care, lost pensions, mortgage foreclosures, and escalating university costs. And, indeed, they are more vulnerable because during the same recent decades when the scale and influence of the finance industry was expanding dramatically and neoliberal governments were reducing regulations, long-standing systems of shared responsibility, mutual support, and social security were being undermined.

Privatization of risk thus has two faces. On the one hand, deregulation and concentrated control over private wealth allow some private actors to create risks that affect their many fellow citizens and also the government, as custodian of the public good. On the other hand, sharp cuts in programs to help ordinary citizens mean that more and more face risks privately, as individuals and families without adequate social support. And of course, the risks they face are not limited to those created by speculators in financial markets. They range from vulnerability to natural disasters to the risks associated with new technologies to the many more or less routine risks of everyday life: traffic accidents, occupational injuries, diseases.

Though not only government programs have been cut, government programs have special significance both because they reach all citizens and because they embody a recognition of shared citizenship. Nonetheless, government programs have been cut, and cut severely around the world. Some of this is part of austerity programs launched in response to fiscal crises associated with the post-2008 financial meltdown. But the rollback of the welfare state started in the 1970s. Under the generals who seized power in Chile, Chicago-trained economists experimented with privatizing government institutions and reducing spending on social welfare (which not surprisingly had increased under the previous socialist government). These experiments informed state policy first in Britain and then the United States as Margaret Thatcher and Ronald Reagan sought to weaken unions, social welfare programs, and government regulation of private capitalism. Such policies, often labeled neoliberal, spread widely through the late twentieth century. They did not always cut total government expenditures, partly because of high military budgets. And they did not always cut deficits, partly because neoliberalism also favored tax cuts, especially for the wealthiest citizens. But they cut deeply into the social safety net that protected ordinary people from risks. In the wake of the financial crisis, cuts have deepened. Citizens are thus deprived of social support precisely at a time when risks have proliferated.

The development of more effective institutions to share the burdens of these risks is among the great achievements of the modern era, especially the twentieth century. The institutions come mostly through private insurance programs that pool risks and government programs that either offer insurance or offer direct support to those in need. These provide both security, so that people may approach the future with more confidence and less worry, and direct material benefits when hazards become harms. In addition, of course, there are efforts to reduce risks—ranging from regulating financial speculation to monitoring the safety of food products. But risks are never eliminated, and so compensating for the fact that only some of those potentially harmed actually are harmed becomes an important social issue.

Responding to risks is in fact one of the basic reasons for the development of social institutions in general, not just government. Through most of history, individuals and families bore the risks of earthquake, fire, flood, famine, plague, and pestilence without effective state action. Providing assistance to neighbors was basic to traditional notions of community, family, and collective responsibility. Members of medieval craft guilds created funds to sustain each other in the face of market crises. Religious charities aided the victims of misfortune.

Yet state action is still at least as ancient as Joseph's advice to Pharaoh to set aside grain against a coming dearth—a wise policy that saved people throughout the region.

Modern governments have gone well beyond opening their storehouses in times of extreme need. They have built public institutions to promote the prosperity of whole nations and to ensure that all citizens share the benefits. Public schools, for example, have been seen not just as charity for poor children or training programs for private industry but as investments in the future of the country. Like health care, clean water supplies, transport networks, rural electrification, and safe food, education has been seen as a shared responsibility—partly on ethical grounds of shared obligation but largely on more instrumental bases of shared benefits. Yet the enormous achievements made by building institutions to provide public goods are not merely threatened; they are being reversed. The privatization of risk, moreover, involves not only reductions in programs explicitly designed to share risk, but also a result of weakness in the provision of other public goods. Higher education is a ready example. In recent years, there has been a growing tendency to treat university education not as a public good to be shared widely, but as a private good available to those with money to pay for it.

Moreover, cuts in state "safety nets" are not being matched by more effective private or civil society action. On the contrary, pensions and health care benefits have been curtailed or eliminated in a host of private firms; some corporations have used bankruptcy provisions to avoid providing health care and other benefits to retirees who previously thought such support was guaranteed. Indeed, employment itself has become increasingly precarious. Even large corporations have become commodities to be bought and sold, with reductions in employee benefits usually part of the deals. Many of the stable organizations within which employees once made relatively secure careers have vanished.

This is an issue not only in the developed world but also in many rapidly developing countries. There are many new opportunities in China, for example, and the society is getting richer (though also more unequal). But with high rates of labor migration and a host of new employers, older institutions that provided securely for members' basic needs—notably the *danwei* or work unit—no longer function in the same way. Families still provide support to their members, but the development of new larger-scale institutions is lagging behind need. In China, as in many other developing countries, some employers provide health care and other benefits to workers, often in factory towns. As during the nineteenth-century industrial revolution in Europe and America, some do this more generously and more effectively than others. But these are extensions of employment compensation, available only to some, not to all citizens, and often part of a disciplinary as well as a charitable regime.

Charities do important work in many settings, providing safety nets and sometimes helping to create new institutions for the longer term. But they are not able to expand their services to meet the new needs. There is also a loss of dignity for workers and citizens to feel they are dependent on charitable gifts—rather than on protections rightly available to them.

Risks come, of course, not just from financial upheavals, nor indeed from "normal" market processes that do include ups and downs in different industries and shifts in the balance of trade among different countries. They come also from technological innovation—which produces technological obsolescence in competing sectors and which creates new risks even while it may also offer enhanced productivity or direct consumer benefits. Overall, the spread of electronic communications brings benefits, but it also concentrates losses, for example costing postal workers their jobs. Programs like unemployment insurance serve to smooth such processes, sustaining workers who through no fault of their own find themselves out of work due to changes that may in the larger picture bring progress. But technological innovation also brings other risks, as for example new drugs bring unanticipated side effects. The issue is not just determining whether benefits outweigh costs. It is that benefits are often spread widely among consumers and concentrated somewhat among those with property rights, while costs are concentrated severely among those unlucky enough to suffer the side effects in the form of illness, injury, or death.

Frank Knight's distinction between "known unknowns" and "unknown unknowns" has become famous as investors have realized that some risks bring opportunities for trading and profit. Looking at a population, or a period of time, or a pool of transactions, some risks are calculable: death rates from cancer, mortgage defaults, or bankruptcies. This is the basis for most insurance—and for a host of derivative investments based on estimating chances where at least many relevant variables are known. Of course, it is also possible to buy insurance for less calculable losses—the remote possibility that lightning will strike while one is playing golf, for example, or that a ship will be sunk in an as yet undeclared war. But there are also dangerous events that should not really be considered risk in this sense because there is no basis at all for calculation. The insight that some risks are predictable makes it possible to price insurance (though not perfectly) and to plan social responses.

But from the point of view of individuals, the risks that may be calculable in the aggregate become very concrete, particular, and personal suffering. A 10 percent unemployment rate is complete unemployment for some individuals. A 0.2 percent cancer rate is death for some individuals and very specific suffering for their children. A hailstorm destroys some crops completely and exposes some farmers to bankruptcy and loss of their land.

Issues of risk, disease, and disasters should be central concerns for social science. So should the availability and viability of social institutions to minimize risk where possible, to share costs, and mitigate harm. And not least of all, social science should address inequalities in how well people are served by such institutions, whether they are government funded and operated or independent. The question is not simply public versus private. Indeed, as the public importance of nominally private pension funds reveals, the two are inextricably intertwined. The issue is what makes institutions effective, and what makes them responsive to public needs. Social science should be part of the answer.

To live up to its full potential, social science cannot be merely a source of technical expertise, or advice to those with power. Social science must also inform public communication, bringing not only capacity to manage but also understanding and insight to inform public choices. Public understanding, like public policy, needs to be informed by serious, empirically grounded, social science analyses. This is a pressing concern not only with regard to natural disasters and "homeland security" but also with regard to pensions and social security, the availability of health insurance and health care, and the stability of financial institutions and markets.

To investigate these issues and to provide information to inform public debate and public policy, the Social Science Research Council (SSRC) launched a project on the privatization of risk in 2006. This project began with working group discussions and a forum of essays posted on our web site. A grant from the John D. and Catherine T. MacArthur Foundation enabled us to expand the inquiry, and we are grateful to a very helpful program officer, Michael Stedman. We were fortunate to recruit Jacob Hacker to play a leading role. Jacob's voice has been central to bringing a concern for the issue of privatization of risk—and the need for shared responsibility—to public discussion. In addition to undertaking his own research, he helped to build a network of colleagues with related interests. Crucially, this brought together academic researchers, policy analysts, and policymakers. A series of six shorter books reflect this interdisciplinary engagement as they address different dimensions of the issue.[1] Jacob also recruited Ann O'Leary as an important collaborator in organizing two major conferences, one directly linked to the preparation of this book. I am pleased that the SSRC has been able to play a role in this important work.

In this book Hacker and O'Leary have brought together an impressive range of scholars. They take up enduring issues that have been made urgent in the current context. Immediate economic crisis is entwined with enduring structural changes. Governments face macroeconomic challenges at the same time that citizens doubt their capacity to deliver public goods efficiently. Broad ideological changes dovetail with concrete transformations of policy. Yet the concrete implications of different policy proposals are often poorly understood. Creativity in finding new approaches to basic needs is stifled by debates stuck in old oppositions.

This book brings clarity to the often confused and ideological debates. It brings research-based knowledge to analysis of the choices before us. It makes a crucial contribution both to understanding and to addressing an issue that is urgent in the United States and around the world.

Notes

1. Jacob Hacker, ed., *Health at Risk: America's Ailing Health System—and How to Heal It* (New York: Columbia University Press, 2008); Andrew Lakoff, ed., *Disaster and the Politics of Intervention* (New York: Columbia University Press, 2009); Donald Light, ed., *The Risks of Prescription Drugs* (New York: Columbia University Press, 2009); Katherine Newman, ed., *Laid Off, Laid Low: Political and Economic Consequences of Employment Insecurity* (New York: Columbia University Press, 2008); Mitchell Orenstein, ed., *Pensions, Social Security, and the Privatization of Risk* (New York: Columbia University Press, 2009); Robert E. Wright, ed., *Bailouts: Public Money, Private Property* (New York: Columbia University Press, 2009).

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In May 2009, we brought together these authors in Berkeley, California to present their working ideas to a peer group of academics and policy practitioners in order to receive feedback. Authors then revised their work and made final presentations in October 2009 to a larger audience of policy thinkers and practitioners in Washington, DC. We thank all those who provided invaluable feedback at these conferences, including: Maeve Elise Brown, Karen Davenport, Will Dow, Maurice Emsellem, Michael Ettlinger, Netsy Firestein, Mark Greenberg, Lief Haase, Alexander Hertel-Fernandez, Ken Jacobs, David Kirp, Gillian Lester, Goodwin Liu, Mary Ann Mason, Paul Nathanson, Mark Paul, John Quigley, Robert Reich, Eric Stein, Jamie Studley, Anne Stuhldreher, Siovahn Walker, Sarah Rosen Wartell, and Micah Weinberg. We thank the Center for American Progress, particularly Sarah Rosen Wartell and Michael Ettlinger, for providing a platform to present this work in Washington and Luke Reidenbach at CAP for his administrative assistance.

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Shared Responsibility,
Shared Risk

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Part One

INSPIRATIONS AND CHALLENGES FOR SHARED RESPONSIBILITY, SHARED RISK

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1

Sharing Risk and Responsibility in a New Economic Era

JACOB S. HACKER

The roughly twenty months between President Barack Obama's inauguration in January 2009 and the midterm elections of 2010 witnessed the passage of a number of reforms designed to improve economic security. The biggest by far was the Patient Protection and Affordable Care Act, passed in March 2010—a landmark health care bill with a federal price tag of roughly $1 trillion over ten years that is predicted to newly insure more than 30 million Americans by 2019.[1] But the health care bill was only one of several major steps taken to improve economic security amid the deepest economic downturn since the Great Depression. In addition, Congress passed a financial reform bill that will provide greater consumer protections for home buyers and borrowers; enacted (as part of the health care bill) a new long-term care insurance program and a substantial expansion of direct government student lending; and passed an economic stimulus package that included a major modernization of unemployment insurance.[2]

The chapters to come will examine these measures, their foci, and their effects. This initial chapter provides the broader context. The policy battles of 2009 and 2010 did not emerge fully formed out of the recent economic downturn. Rather, they were rooted in a deeper and longer-term transformation of our economy and our society that has increased the economic insecurity of American workers and their families. Five years ago, in a book that attempted to draw attention to this sea change and map out a new economic path, I called this transformation the "Great Risk Shift."[3] My argument was that economic risk had increasingly shifted from the broad shoulders of government and corporations onto the backs of American workers and their families. This sea change, I argued, had occurred in nearly every area of Americans' finances, from jobs, health care, and retirement pensions to homes, personal savings, and strategies for balancing work and family. With the economic collapse that began at the end of 2007, this shift no longer seems debatable. But how to deal with this transformation given the political and budgetary constraints that our leaders face remains very much an open question.

The purpose of this volume is to provide an answer—or rather, a series of answers—to that question. In my book *The Great Risk Shift*, I sought to begin a conversation about how to adapt America's ailing economic security infrastructure to our nation's new economic and social realities. By bringing together some of the best thinkers about economic and social policy in the United States today, this book is designed to move that conversation toward concrete ideas for reform. Each of the contributors to this volume examines how economic security has changed in specific crucial areas of Americans' lives and then outlines realistic yet farsighted measures to ensure that workers and their families have the tools and policies they need to deal with unexpected shocks and to invest in their futures.

This chapter lays out the big picture that should guide these efforts. It begins by documenting and explaining the Great Risk Shift, which is rooted in the erosion of America's distinctive framework of economic security. This framework differs from the frameworks found in other nations less in terms of total *size* and more in the *form* that social protections take. Responsibilities that in other nations were handled by government, perhaps with the cooperation of nonprofit mutual insurers, became the responsibility of employers and for-profit providers. Government policies that encouraged and regulated these private benefits to promote their broad distribution and stability were once at the core of America's uniquely "divided welfare state."[4] Yet this distinctive framework has crumbed over the last generation in the face of growing economic pressures on employers, as well as increasing political resistance to the ideal of economic security itself.

The chapter then turns to the question of what can be done in response to the Great Risk Shift. The legislative landmarks of 2009 and 2010 represent a major step forward. Even after their passage, however, the United States still badly needs a twenty-first-century social contract that protects families against the most severe risks they face, without clamping down on the potentially beneficial processes of change and adjustment that produce some of these risks. This will require recognizing and responding to the most fundamental source of American economic insecurity: the deep mismatch between today's economic and social realities and America's strained framework for providing economic security. It will also require recognizing that economic security and economic opportunity are not antithetical, but go hand in hand. Just as investors and entrepreneurs need basic protections to encourage them to take economic risks, so ordinary workers and their families require a foundation of economic security to confidently invest in their futures and seize the risky opportunities before them.

America's Unique—and Endangered—Framework of Economic Security

We often assume that the United States does little to provide economic security compared with other rich capitalist democracies. This is only partly true. The United States does spend less on government benefits as a share of its economy, but it also relies far more on private workplace benefits, such as health care and retirement pensions. Indeed, when these private benefits are factored into the mix, the U.S. framework of economic security is not smaller than the average system in other rich democracies—it is actually slightly larger.[5] With the help of hundreds of billions of dollars in tax breaks, American employers serve as the first line of defense for millions of workers buffeted by the winds of economic change.

The problem is that this unique employment-based system is coming undone, and, in the process, risk is shifting back onto workers and their families. Employers want out of the social contract forged in the more stable economy of the past. And with labor unions weakened and workers just worried about holding onto their jobs, employers are largely getting what they want. Meanwhile, America's framework of government support is also strained. Social Security is declining in generosity even as guaranteed private pensions evaporate. Medicare, while ever more costly, has not kept pace with skyrocketing health expenses and changing medical practices. And although the share of unemployed workers receiving unemployment benefits has risen in recent years, the long-term trend is one of declining support for Americans out of work, even as unemployment has shifted from cyclical job losses to permanent job displacements.

The history of American health insurance tells the story in miniature. After the passage of Medicare and Medicaid in 1965, health coverage peaked at roughly 90 percent of the population, with approximately 80 percent of all Americans covered by private insurance.[6] Since the late 1970s, however, employers and insurers have steadily retreated from broad-risk pooling, and the number of Americans who lack health coverage has increased with little interruption. Private health coverage now reaches just over half the American population.[7]

Employment-based health insurance has not been the only casualty. Companies have also raced away from the promise of guaranteed retirement benefits. Twenty-five years ago, 83 percent of medium and large firms offered traditional "defined-benefit" pensions that provided a fixed benefit for life; today, the share is below one-third.[8] Instead, companies that provide pensions mostly offer "defined-contribution" plans like the 401(k), in which returns are neither predictable nor assured. Moreover, despite the expansion of 401(k) plans, the share of workers with access to a pension at their current job—either a defined benefit plan or a 401(k) plan—has fallen from just over half in 1979 to under 43 percent in 2009.[9]

Defined-contribution plans are not properly seen as pensions, at least as that term has been traditionally understood. They are essentially private investment accounts sponsored by employers that can be used for building up a tax-free estate, as well as for retirement savings. As a result, they greatly increase the degree of risk and responsibility placed on individual workers in retirement planning. Traditional defined-benefit plans are generally mandatory and paid for largely by employers (in lieu of cash wages). They thus represent a form of forced savings. Defined-benefit plans are also insured by the federal government and are heavily regulated to protect participants against mismanagement. Perhaps most important, their fixed benefits protect workers against the risk of stock market downturns and the possibility of living longer than expected.

None of this is true of defined-contribution plans. Participation is voluntary, and due to the lack of generous employer contributions, many workers choose not to participate, or if they do, to contribute inadequate sums.[10] Plans are not adequately regulated to protect against poor asset allocations or corporate or personal mismanagement. The federal government does not insure defined-contribution plans. And defined-contribution accounts provide no inherent protection against asset or longevity risks. Indeed, some features of defined-contribution plans—namely, the ability to borrow against their assets, and the distribution of their accumulated savings as lump-sum payments that must be rolled over into new accounts when workers change jobs—exacerbate the risk that workers will prematurely use retirement savings, leaving inadequate income upon retirement. And, perversely, this risk falls most heavily on younger and less highly paid workers, the very workers most in need of secure retirement protection.[11]

We do not yet know how severely the market crisis that began in 2008 will reduce private pension wealth, but the signs are deeply worrisome. Just between mid-2007 and October 2008, an estimated $2 trillion in retirement wealth was lost in 401(k)s and individual retirement accounts.[12] A 2009 survey found that two-thirds of adults aged 50 to 64 years lost money during this period in mutual funds, individual stocks, or 401(k) accounts, with the vast majority losing more than 20 percent of their investments.[13] (Most who had no losses had no investments.)

But although we cannot yet know how sustained these losses will be, we do know they come after a generation of decline in the retirement-preparedness of Americans. According to researchers at Boston College, the share of working-age households that are at risk of being financially unprepared for retirement at age 65 has risen from 31 percent in 1983 to 43 percent in 2004 and a projected 51 percent in 2009.[14] Younger Americans are far more likely to be at risk than older Americans: roughly half of those born from the mid-1960s through the early 1970s are at risk of being financially unprepared, compared with 35 percent of those born in the decade after World War II.[15] In every age group, low-income Americans are the least financially prepared.[16]

In sum, as private and public support has eroded, workers and their families have been forced to bear a greater burden. This is the essence of the Great Risk

Shift. Rather than enjoying the protections of insurance that pools risk broadly, Americans are increasingly facing economic risks on their own—and often at their peril.

The New World of Work and Family

The erosion of America's distinctive framework of economic protections might be less worrisome if work and family were stable sources of security themselves. Unfortunately, they are not. The job market has grown more uncertain and risky, especially for those who were once best protected from its vagaries. Workers and their families now invest more in education to earn a middle-class living, and yet in today's postindustrial economy, these costly investments are no guarantee of a high, stable, or upward-sloping career path. For displaced workers, the prospect of gaining new jobs with relatively similar pay and benefits has fallen, and the ranks of the long-term unemployed and "shadow unemployed" (workers who have given up looking for jobs altogether) have grown.[17]

Meanwhile, the family, a sphere that was once viewed as a refuge from economic risk, has increasingly become a source of risk of its own. At first glance, this seems counterintuitive. Families are much more likely to have two earners than in the past, and a two-income family is the ultimate form of private risk sharing. To most families, however, a second income is not a luxury but a necessity in a context in which wages are relatively flat and the primary costs of raising a family (health care, education, and housing) are high and rising. According to calculations by Jared Bernstein and Karen Kornbluh, more than three-quarters of the modest 24 percent rise in real income between 1979 and 2000 experienced by families in the middle of the income spectrum was due to increased work hours (primarily the addition of a second earner) rather than rising wages.[18] In time-use surveys, both men and women who work long hours indicate they would like to work fewer hours and spend more time with their families[19]—which strongly suggests that they are not able to choose the exact mix of work and family they would prefer.

With families needing two earners to maintain a middle-class standard of living, their economic calculus has changed in ways that accentuate many of the risks they face. Precisely because it now takes more work and more income to maintain a middle-class standard of living, the questions that face families when financially threatening events occur are suddenly starker. What happens when a woman leaves the workforce to have children, when a child is chronically ill, when one spouse loses a job, or when an older parent needs assistance? In short, events within two-earner families that require the care and time of family members create special demands and strains that traditional one-earner families generally did not face.

The Rising Instability of Family Incomes

The new world of work and family has ushered in a new crop of highly leveraged investors—middle-class families. One sign of this change is the rising instability of family incomes. Although the precise magnitude of the increase depends on how income variance is measured, my own research using the Panel Study of Income Dynamics (PSID) suggests that short-term family income variance essentially doubled from 1969 to 2004.[20] Much of the rise in income volatility occurred prior to 1985, and volatility dropped substantially in the late 1990s.[21] In recent years, however, income volatility has risen to exceed its 1980s peak.[22] The proportion of working-age individuals experiencing a 50 percent or greater drop in their family income over a two-year period has climbed from less than 4 percent in the early 1970s to nearly 10 percent in the early 2000s.[23] And although less-educated and poorer Americans have less-stable family incomes than their better-educated and wealthier peers, the increase in family income volatility affects all major demographic and economic groups.[24] Indeed, over the past generation, Americans with at least four years of college experienced a larger increase in family income instability than those with only a high school education, with most of the rise occurring in the last 15 years.[25]

Understanding the causes of increased family income instability is essential if we are to reduce Americans' growing economic insecurity. Along with a team of researchers (and with funding from the Rockefeller Foundation), I have developed the "Economic Security Index," or ESI.[26] The ESI adds to research on income volatility by looking at economic instability caused by out-of-pocket medical spending as well as by income fluctuations. It also considers whether families have adequate financial safety nets to cushion these economic shocks. In a nutshell, the ESI represents the share of Americans who experience at least a 25 percent decline in their inflation-adjusted "available household income" from one year to the next and who lack an adequate financial safety net to replace this lost income until it has returned to its original level. "Available household income" is income that is reduced by nondiscretionary spending, including, most substantially, the amount of a household's out-of-pocket medical spending. (The other main form of nondiscretionary spending considered by the ESI is the cost of servicing debt.). Thus the ESI captures Americans who experience income losses of 25 percent or greater due to a decline in income, an increase in medical spending, or a combination of the two.

The ESI, available from 1985 through 2007 (with projections for 2008 and 2009) shows that economic insecurity has increased substantially over the last quarter century (see Figure 1.1). In 1985, 12 percent of Americans experienced a major economic loss sufficient to classify them as insecure in the ESI. During the recession of the early 2000s, this figure had risen to 17 percent, and projections suggest that in 2009, the level of economic insecurity experienced by Americans was greater than at any time over the past quarter century.

These stark numbers are not just a reflection of the steep economic downturn of recent years. Rather, economic security has been gradually declining since the

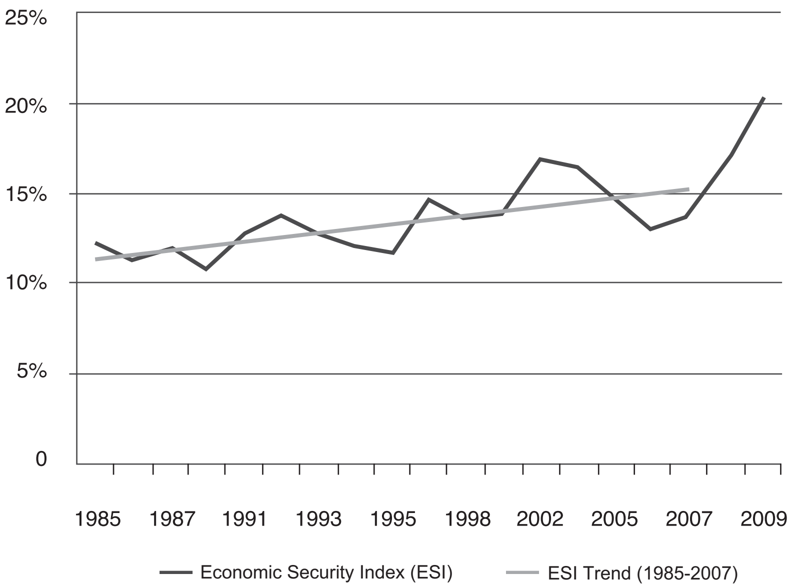

Figure 1.1: Share of Americans Who Are Insecure, 1985–2007 (with 2008–2009 Projections). Source: Jacob S. Hacker et al., *Economic Security at Risk: Findings from the Rockefeller Economic Security Index* (New York: Rockefeller Foundation, 2010), http://economicsecurityindex.org/assets/Economic%20Security%20Index%20Full%20Report.pdf

early 1980s. To see beyond short-term economic fluctuations requires calculating the longer term statistical trend in the ESI, which is shown in Figure 1.1. Based on this analysis, the ESI has increased by approximately one-third from 1985 to 2007. If the projections up to 2009 are included, the ESI has increased by almost half since 1985. To state this trend in terms of population, approximately 46 million Americans were counted as insecure in 2007, up from 28 million in 1985. Moreover, the share of Americans experiencing large drops in available household income has increased even more since the 1960s. A less complete form of the ESI available back to the late 1960s shows that large (25 percent or greater) income losses—the core component of the complete ESI—had already risen by about one-third from the 1960s to the 1980s, making subsequent increases over the past quarter century even more noteworthy.

The Indebted American Family

The rising instability of family incomes would be less troubling if families had substantial liquid savings to tide them over during periods with reduced income. Yet the ESI suggests that very few families have even modest holdings of wealth besides their home. Instead, Americans are often deeply indebted, especially families with children. As a share of income in 2004, total debt—including mortgages, credit cards, car loans, and other liabilities—was more than 125 percent of income for the median married couple with children.[27] According to a recent analysis of families with incomes between two and six times the federal poverty level and headed by working-age adults, more than half of these middle-class families have no net financial assets (excluding home equity), and nearly four in five of these families do not have sufficient assets to cover three-quarters of essential living expenses for even three months, should their income disappear.[28] And, of course, the recent economic crisis has only exacerbated the problem, causing a loss of $15 trillion in private family assets and wealth between June 2007 and December 2008.[29]

With debt levels rising, personal bankruptcy has gone from a rare occurrence to a relatively common one, with the number of households filing for bankruptcy rising from less than 300,000 in 1980 to more than two million in 2005.[30] During that period, the financial characteristics of the bankrupt have grown worse and worse (contrary to the claim that bankruptcy is increasingly being used by people with only mild financial difficulties). Strikingly, married couples with children are much more likely to file for bankruptcy than are couples without children or single individuals.[31] Otherwise, the bankrupt are much like other Americans before they file, though slightly better educated, roughly as likely to have had a good job, and modestly less likely to own a home. They are not the persistently poor or the downtrodden looking for relief: they are refugees of the middle class, frequently wondering how they fell so far so fast.[32]

Americans are also losing their homes at record rates. Even before the housing market collapsed in 2008, there had been a fivefold increase since the 1970s in the share of households that fall into foreclosure[33]—a process that begins when home owners default on their mortgages and can end with homes being auctioned to the highest bidder in local courthouses. The run-up of housing prices before the economic downturn had much less of a positive effect on Americans' net worth than might be supposed. Even as home prices rose, Americans held less and less equity in their homes. As recently as the early 1980s, home equity was around 70 percent of home values on average; in 2007, it was 43 percent—the lowest level on record.[34] In the recent downturn, approximately 20 percent of home owners have negative equity, owing more on their home than it is worth.[35] For scores of ordinary home owners—roughly one in twenty-five mortgage-owning households in the past few years, a level not seen since the Great Depression—the American Dream has mutated into the American Nightmare.

The Endangered American Dream

As these examples suggest, economic insecurity is not just a problem of the poor and uneducated. It affects even educated, middle-class Americans—men and women who thought they had bought the ticket to upward mobility and economic stability by staying in school, buying a home, and investing in their 401(k)s.

Insecurity today reaches across the income spectrum, the racial divide, and lines of geography and gender. Increasingly, all Americans are riding the economic roller coaster once reserved for the working poor and, thus, are at risk of losing the secure financial foundation they need to reach for and achieve the American Dream.

Economic security matters deeply to people. When most of us contemplate the financial risks in our lives, we do not concern ourselves all that much with the upside risks—the chance that we will receive an unexpected bonus, for example. We worry about the downside risks, and worry about them intensely. In the 1970s, psychologists Daniel Kahneman and Amos Tversky gave a name to this cognitive bias: "loss aversion."[36] Most people, it turns out, are not just highly risk-averse—they prefer a bird in the hand to even a very good chance of two in the bush. They are also far more cautious when it comes to bad outcomes than when it comes to good outcomes of exactly the same magnitude. The search for economic security is, in large part, a reflection of a basic human desire for protection against losing what one already has.

This desire is surprisingly strong. Americans are famously opportunity-loving, but when asked in 2005 whether they were "more concerned with the opportunity to make money in the future, or the stability of knowing that your present sources of income are protected," 62 percent favored stability and just 29 percent favored opportunity.[37]

It should not be surprising, therefore, that recent polling shows extremely high levels of economic anxiety among all but the richest Americans. In a September 2010 poll, only half of Americans agreed that "the American Dream—that if you work hard you'll get ahead—still holds true;" more than four in ten said it no longer did.[38] In April 2009, two in three adults said that the current economy presented them with more risks than their parents confronted—six times as many as the 11 percent of those polled who said they faced fewer risks than their parents.[39] A comprehensive poll concerning economic risk that I helped design—fielded as part of the American National Election Studies with the support of the Rockefeller Foundation—asked Americans about 15 different sources of economic risk in employment, medical care, wealth, and family relations (see Figure 1.2). More than three-quarters of all Americans reported that they were very or fairly worried about at least one of these economic risks. Worries about wealth were the most frequent cause of economic unease, though concerns about medical costs were a close second.[40]

These are not idle worries. Households that experienced these economic risks between March 2008 and September 2009—especially risks that persisted for six months or more—reported much higher levels of unmet basic needs (going without food because of the cost, losing one's home or rental, or going without health care because of the expense). This was particularly true of employment and medical risks: households experiencing employment and medical spending risks were three times as likely as unaffected households to report any unmet needs and seven times as likely to report multiple unmet needs. Strikingly, even among families in the third quartile of household income (annual income between