

MESSAGE from the CHIEF COUNSEL

Social Security Reform and Small Business

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The self-employed make up a significant part of the U.S. economy. According to the most recent data available to the Office of Advocacy, 9.8 percent of the total labor force was self-employed in 2003. This represents over 12.2 million businesses or half of the total small business population. The self-employed are clearly at the heart of the American economy, and their financial health is central to our country's economic progress.

Individual wage and salary workers pay 6.2 percent of their wages in payroll taxes to fund Social Security benefits for current retirees. Their employers pay taxes that match those amounts. The self-employed pay the full 12.4 percent Social Security payroll tax because they are rightly considered both the employer and the employee. When they retire, the self-employed expect that the payroll taxes on future workers and employers will fund their promised benefits.

According to the National Association for the Self Employed (NASE), more than 65 percent of 14- to 19-year-olds want to start a business. Do they realize that the Social Security system will be bankrupt at least nine years before they retire? If that is not a wake-up call for reform, how about explaining to young entrepreneurs that one-eighth of the money they earn goes into Social Security and—despite making decisions that mean survival or death for their own business—they cannot decide what happens to that money once they retire?

This looming Social Security crisis will affect a flood of entrepreneurs because the path of self-employment is being traveled by more and more people anxious to be their own bosses. From 2000 to 2003, total self-employment increased by 6.2 percent. Minority self-employment is also on the rise. Latino entrepreneurs topped 1 million in 2003. The number of self-employed African Americans and Asians has also sharply increased, according to data from the Bureau of Labor Statistics' Current Population Survey program.

President Bush's plan to reform Social Security calls for a portion of payroll taxes to be voluntarily set aside into personal retirement accounts. The concept of personal accounts mirrors the American Dream of owning a business. A personal account, as part of Social Security reform, will allow the self-employed to make decisions about their savings. Personal accounts will allow self-employed individuals to reinvest in their business for growth or to ensure that it passes on to the next generation.

The importance of personal accounts is amplified by the limited retirement savings options for the self-employed. The double payroll tax puts small business

retirement plans out of reach. An increased payroll tax eats up money that could go to IRAs or Keogh accounts. By crowding out the funds needed for retirement savings, the burden of the double out-of-pocket payroll tax reduces the likelihood that small businesses will have a separate retirement plan. According to the Employee Benefit Research Institute, in 2003 over 50 percent of small business owners had either never heard of or had only vague familiarity with small business retirement plans. The only retirement savings vehicle they had a high degree of familiarity with was the 401(k), which is often too costly for the self-employed to administer.

Without reform, perhaps sons and daughters of entrepreneurs will never realize the full benefits of the Social Security system. Or, perhaps the 12.2 million self-employed in the United States and their families will take pride in their enormous contribution to the economy and insist that personal accounts remain a part of Social Security reform.