Working To Make Retirement Plans Better For The Poor

Commentary

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When the U.S. Congress reconvenes later this month, the Senate will consider its version of the Comprehensive Retirement Security and Pension Reform Act. This bill, a variant of the Taxpayer Refund and Relief Act of 1999 that President Clinton vetoed, passed the House in July by a whopping 401 to 25 vote.

But the bill represents a second-rate solution to a first-order problem—an out of touch and outmoded private pension system that leaves millions of Americans without adequate retirement incomes.

This new bill would substantially increase the amount that American workers could contribute to tax-deferred retirement plans. Participants in 401(k) plans would be able to contribute $15,000 rather than today's $10,500 limit—a 43 percent jump.

Plans could count $200,000 as a base for calculating compensation for benefits, rather than today's $170,000 limit. That would be an 18 percent increase. One cap on combined employer and employee contributions to so- called defined contribution plans (whose benefits come from annual contributions and investment earnings) would go by the wayside.

The other, an annual $30,000 limit on tax-deferred savings, would rise to $40,000. Each of these proposals sounds sensible because Americans will need to save more for retirement no matter what happens to Social Security.

But how good are these incentives when put to the test? To find out, I compared how much Americans with Individual Retirement Accounts and other plans that let them decide how much to save every year get now, to what they would get under the proposed changes.

The calculations showed that higher-income individuals who can already afford extremely high rates of saving get a reward of more federal tax dollars.

The new proposals don't offer new incentives to less avid savers who can currently afford to put more away or to those who can afford to save little or nothing.

Just as troubling, huge amounts of time and money will be needed to retool the private pension system to accommodate these changes. Every plan will have to be rewritten and resubmitted for IRS approval, and required plan info for participants must be redrafted.

Plan administration, testing and operating procedures must be changed too. The plan-compliance industry, consisting of lawyers, accountants firms and consultants, will have a field day.

And all would-be savers will foot the bill because these compliance costs will either be charged to the plan and deducted from their accounts or paid by their employers who will cut their contributions to compensate.

An even greater waste is that of a golden opportunity to reform the private pension system. On a scale of one to 10, raising contribution limits rates at most a three for overall impact. Among the more important issues that Congress should consider are three that rate at least a nine.

First is coverage. The private pension system does very well by better-educated, higher-income, longer-tenured workers in larger corporations.

But what about those millions of working Americans left out and behind by the private pension system? The pension reform bill increases the contribution limits for IRAs, a long-overdue step. But instead of the consolation prize of an IRA, why not open the richer benefits of an employer-sponsored plan to the majority of employees who have none?

Second is confusion. The pension reform act tinkers with some of the pension law's more obscure provisions, all in the name of reducing complexity and encouraging more employer participation. But this pruning isn't enough to fix an irrational and inefficient maze of plans and rules.

Do we really need six different ways for Americans to save, depending on whether they have no plan, are self-employed (two options here!) or save through a corporate, nonprofit or government plan? Why not have a single, simple employee savings plan?

Third is assistance. Tax incentives and subsidies can do only so much to help Americans take more responsibility for their retirement savings. Low-income workers earn too little to contribute enough to build substantial retirement funds, and those in the lowest tax bracket get the smallest tax subsidy.

Both the administration's "USA Accounts" proposal and reform bills proposed by Rep. Jim Kolbe and Rep. Charles Stenholm and Sen. John Breaux and Sen. Bob Kerrey offer federal matching dollars to low-income savers. Adding such federal assistance and combining it with employer matching dollars would truly be comprehensive and bipartisan pension reform.

Passing the Comprehensive Retirement Security and Pension Reform Act wouldn't be a terrible mistake provided Congress also passes other measures to make savings plans simple and give the poorest workers a leg up.

But as the sole response by Congress to a looming retirement savings crisis, this backdoor tax cut for the wealthy would poorly serve an aging America.

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