May 5, 2009

DOES AMERICA NEED A NEW RETIREMENT SYSTEM?
WE MAY NEED HELP, BUT DON'T NECESSARILY TRUST SOMEONE ELSE TO SAVE US

By Katrina Brown Hunt

No good deed goes unpunished.

That's what unemployed Boston salesman Paul Escobar could be thinking. He'd been paying dutifully into his job's 401(k) plan, and was hands-on with his allocation, putting a lot of his money in equities.

As of today, no surprise, he's lost 45 percent of his balance — and he's lost his job, too. In hopes of recovering losses, "I've definitely been rebalancing my allocations," says the 42-year-old. He also says that he's not opposed to using some other savings vehicles, like a variable life insurance policy.

At the same time, Escobar doesn't think the 401(k) system is inherently flawed, nor does he welcome any reform to the way Americans save for retirement — especially one that would involve government intervention.

"I don't want to be forced to save with anyone other than myself as the 'decider,'" Escobar says. "I'll choose where to get my personal guarantee on benefits."

It's a dilemma: We may need help, but we don't necessarily trust someone else to save us. A rash of recent surveys shows many people are sending out distress calls regarding their retirement savings, especially when it comes to 401(k)s.

The Employee Benefit Research Institute, a research group supported by both business and labor, recently released its annual Retirement Confidence Survey, which found that only 13 percent of respondents said they felt they have enough money for a comfortable retirement — down from 27 percent in 2007. Transamerica's recent retirement survey found that 37 percent of respondents now plan to work past age 70 and perhaps never retire. A Barclays Global Investors study found that 90 percent said they wanted a 401(k) to offer a guaranteed retirement income.

Dallas Salisbury, president of the EBRI, isn't surprised — but he's still skeptical.

"People now put a high priority on a guaranteed retirement income," he says, "but surveys say they want to get it as long as they don't give up anything — as in access to that money and power over it."

Indeed, put the words "401(k)" and "guaranteed income" in the same sentence, and you quickly get a hot debate going among any number of retirement experts and lawmakers along the political spectrum. Some says 401(k)s are being criticized unfairly in this unprecedented economic crisis, while others say the downturn proves that 401(k)s were never meant to be anyone's primary source of retirement savings.

Should we be rethinking our retirement savings system?

“It’s time to have a campaign like we’ve had in health care in this country,” says Karen Friedman, policy director of the consumer advocacy group the Pension Rights Center, “We need to recognize a basic American ideal that everybody should be able to retire and make ends meet.”

Here are some ideas circulating from those who hope to strengthen — or completely rebuild — the way we approach retirement:

• Make 401(k) plans automatic. Most people agree that, given enough time, 401(k) accounts can recover from market losses. What’s impossible, however, is building more savings if you don’t save enough to begin with.

In his 2010 budget blueprint, President Barack Obama called for requiring existing 401(k) programs to be automatic — as in, once you start working for a company that has a 401(k) or similar program, you’ll be enrolled, unless you make it a point to opt out. Meanwhile, companies that don’t offer a 401(k) plan (and have at least 25 employees) would have to set aside funds for employees in individual retirement accounts. On top of that, the government would offer a roughly $500 tax credit for many middle-income workers.

What critics say: While everyone agrees that people should save more, forcing them to do so pushes political buttons. “Mandating participation is a high hurdle,” says Salisbury of the EBRI.

• Make 401(k)s more user-friendly. If you think you’re dense when it comes to reading the specifics of your company’s 401(k) plan — well, it’s not just you. For one thing, there’s information missing.

Reps. George Miller, D-Calif., and Rep. Rob Andrews, D-N.J., introduced a bill last week that would require financial service providers to disclose all fees associated with 401(k) plans. Such “little” fees can add up big, according to the Government Accountability Office: A report found that even one percentage point in excessive fees can bring down a 401(k) account balance by about 20 percent over the course of a worker’s career.

What critics say: Miller has been accused of being anti-401(k). House Republicans have introduced their own proposal to help strapped 401(k) holders — and, they say, protect 401(k)s from being weakened or abolished.

Within days of Miller’s bill, House Minority Leader John Boehner, R-Ohio, and fellow House Republicans introduced the Savings Recovery Act, which seeks to mitigate lost savings through several measures. Among them is a batch of tax breaks: increasing the amount that employees can kick into 401(k)s; giving savers’ credits for college savings plans; raising the limit for Social Security income before the earnings penalty kicks in; and suspending the capital gains tax on newly acquired assets for two years.

• Forget 401(k)s and create a supplement to Social Security. Teresa Ghilarducci, an economic policy professor at the New School for Social Research in New York, spoke to a congressional panel last fall about "Guaranteed Retirement Accounts," which she proposed in her book “When I’m Sixty-Four: The Plot Against Pensions and the Plan to Save Them.”

In her proposal, employers and employees would be required to invest a combined 5 percent of a worker’s income into a program administered by Social Security and would also get an annual $600 government tax credit, adjusted for inflation. Contributions would be invested in a special breed of government bonds, offering a roughly 3 percent annual return. Ghilarducci proposed paying for those subsidies by cutting most tax breaks related to 401(k)s and IRAs.

What critics say: 401(k) advocates blast this plan over the loss of tax breaks, while dismissing the subsidy and 3 percent returns as chump change. Ed Ferrigno, vice president of Washington Affairs for the Profit Sharing/401(k) Council of America, says Americans won't go for the mandated contribution. "It's saying a worker should be forced to donate another 5 percent of wages," he says. "I think that's a profound issue — how does that affect people's ability to pay into other benefits like health care?"

• More cash-balance plans. These hybrids of pensions and 401(k)s have the employer contributing to accounts in the worker's name, but the employer controlling (and assuming risk for) the pooled accounts' investments. As years pass, you can see your account total growing, and when you retire, you often have the option to take the balance in a lump sum. The Pension Protection Act of 2006 clarified the rules for these plans, and more companies are now adopting them — Coca-Cola Co. being one of them.

"We want to learn from the past," says Alan Glickstein, a senior consultant at Watson Wyatt, a firm that helps design such plans, "and try to take the best features of 401(k)s and pensions and blend them. I think it's the next big thing in retirement design."

What critics say: Some have complained about how these plans were created out of otherwise failing pension plans and have questioned whether their formulas put older workers at a disadvantage. They can get complicated, too, as well as expensive. "As the employer, you've got to hire an actuary," says Salisbury, "and you end up with the potential that the investment portfolio loses value. The employer may have to kick in a lot more money than they originally planned."

• Create a new program where the government, an employer and employee share responsibility. A new initiative called Retirement USA — including public policy, union and consumer advocacy groups — is working on a proposal that would create a program that is "universal, adequate and secure." Its working paper points to various models as worth exploring, including Ghilarducci's proposal, TIAA-CREF's retirement plans for doctors and academics, and a few programs outside the U.S.

Even though the group hasn't articulated its plan yet, Retirement USA is already getting buzz (and flack) from both sides of the debate — mostly for implying that the government should have a greater role and that individuals shouldn't be asked to manage their retirement money themselves. "This do-it-yourself system isn't working," says Friedman, of the Pension Rights Center, who is also a principal in Retirement USA. "It's time to have a version with shared responsibility."

What critics say: The "shared" element makes critics think socialism. Plus, "they're really saying that in addition to Social Security, we should have second mandatory government retirement system," says Ferrigno.

Friedman, meanwhile, says their plan won't exclude 401(k)s altogether.

"There will always be a mechanism so that people can save on their own," she says, "but we need a system that is more reliable. I think the people who understand this are the ones who have lost out."