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Mr. Bill Keller, Executive Editor
The New York Times
620 Eighth Avenue
New York, NY 10018

To the Editor:
The editorial "About Your 401(k) Plan" (August 24) expresses concerns about retirement adequacy based on market declines during the past year, and suggests several ways that 401(k) plans could be improved. The American Society of Pension Professionals & Actuaries (ASPPA) agrees that there is room for improvement. However, the 401(k) system has been remarkably successful at getting working Americans to save for retirement, and changes should enhance the current system, not weaken it. To that end, ASPPA is a strong supporter of expanding the availability of workplace savings through automatic individual retirement accounts (auto-IRAs) such as those proposed by the Obama administration. ASPPA believes payroll deduction auto-IRA arrangements will ultimately encourage more employers to sponsor 401(k) plans, and contribute on the employee's behalf.

However, the editorial repeats a common misconception that changing the tax incentives for 401(k) plans from an income exclusion to a tax credit would strengthen the system. Under a progressive tax system, it may be true that a dollar exclusion is worth more to an upper income taxpayer than a lower income one, but this simple analysis fails to tell the full story. Based on Internal Revenue Service data, 65 percent of the estimated federal tax expenditures for private employer-sponsored defined contribution plans benefit those earning less than $100,000. In addition to providing this direct tax benefit, the exclusion benefits rank-and-file employees by encouraging employers to contribute to 401(k) arrangements. Replacing the current exclusion with a modest tax credit would not even come close to replacing the employer contributions millions of workers receive under the current structure. Although, as you note, some employers have reduced or eliminated matching contributions in the current economic downturn, many of those employers have announced their intention to reinstate matching contributions. Many other employers contribute more than just matching contributions to 401(k) plans, and federal law imposes non-discrimination requirements that assure benefits under these arrangements are being shared by a broad cross-section of workers – not just highly compensated employees.

Participation rates provide clear direction for strengthening the system. According to the Employee Benefit Research Institute, more than 75 percent of moderate-income earners (annual income between $30K and $50K) who have access to employer-sponsored plans participate in those plans. Only 5 percent of individuals without employer-sponsored accounts contribute on their own to an IRA. Changing the tax structure will not expand retirement savings – making workplace retirement savings more widely available through payroll deduction auto-IRAs will.

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ASPPA also believes the suggestion that the government should share the investment risk for retirement savings accounts is misguided. Workers have different investment needs, and making a range of investment alternatives, including equities, available to workers is appropriate for a retirement savings vehicle. Guaranteeing a rate of return in a system with a range of investment options would create a serious moral hazard. If participants could shoot for high returns in equities while being insulated from downturns, the government, and taxpayers, would end up holding the bag. Improved disclosure and access to knowledgeable, independent investment advice are better solutions to concerns about long-term investment performance than government guarantees for retirement savings accounts.

The 401(k) system was intended to supplement Social Security, not replace it. The 401(k) system is worth improving because it has been successful at creating retirement savings for millions of workers. ASPPA believes payroll deduction IRAs will expand coverage, and improved fee disclosure and the availability of independent investment advice will improve the long-term benefits. ASPPA will continue to work with Congress and the administration to incorporate these improvements into the private retirement system.

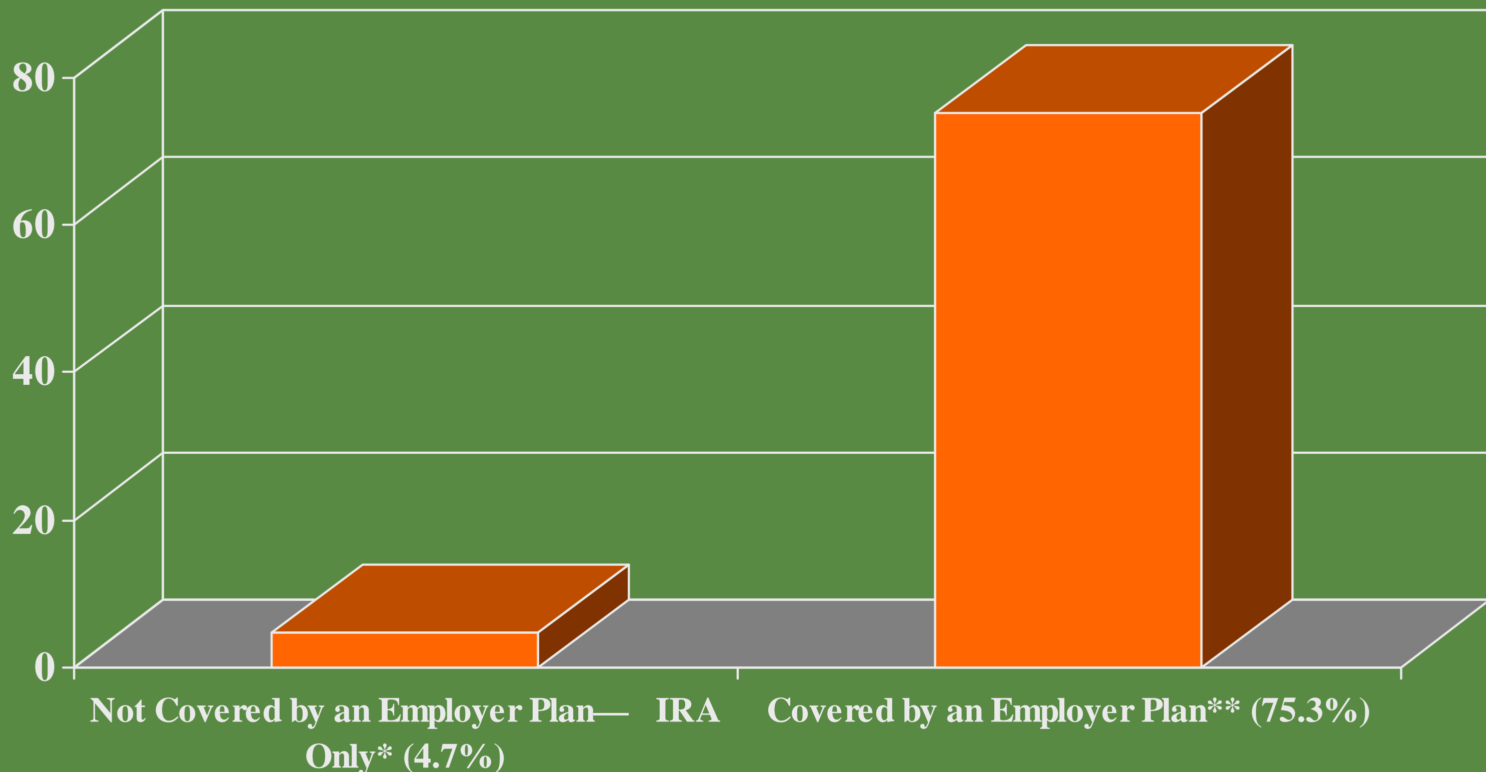
Sincerely,

Stephen L. Dobrow, CPC, QPA, QKA, QPFC
President

Effectiveness of Employer Plans

ASPPA
WORKING FOR AMERICA'S RETIREMENT

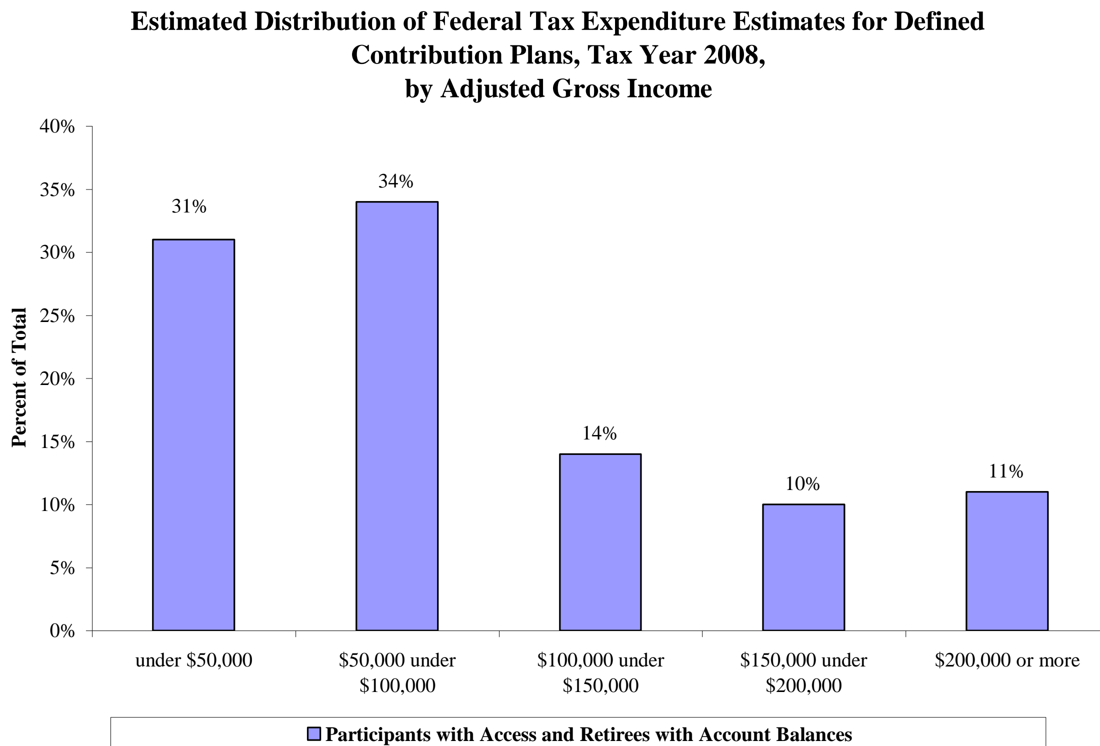
Participation Rates by Moderate Income ($30,000–$50,000) Workers Not Covered by a Workplace Retirement Plan Versus Covered by a Plan



Source: Employee Benefits Research Institute (2008).

Estimated Benefits of Tax Expenditure Estimates for Defined Contribution Plan Participants and Retirees with Account Balances

The following graph displays the estimated tax expenditure benefits by income class. As displayed in this graph, the distribution of benefits for defined contribution plans shows that approximately 65 percent of the benefits are attributable to taxpayers with less than $100,000 of adjusted gross income (AGI).



The distribution includes active participants in all defined contribution plans, including public plan participants (Federal, State, and Local). In addition to the active participants, the estimated benefits includes those retirees with account balances.

Estimating the Distribution Benefits of the Tax Expenditure Estimates –

1. The estimated number of taxpayers relies on primary data from the Internal Revenue Service (IRS) Statistics of Income Division (SOI). This data source matched Form 1040 with the corresponding Form W-2 to determine pension participation in a defined contribution plan.[1] This analysis identifies active participants for the given tax year, in this case tax year 2004. The base numbers for 2004 were extrapolated to reflect the 2006 return data (the most current data).[2]

   The active participants include any:

   - Qualified pension, profit-sharing, or stock-bonus plan (including 401(k) plans) described in section 401(b)
   - Annuity plan described in section 403(a)
   - Annuity contract or custodial account described in section 403(b)
   - Simplified employee pension (SEP) plan described in section 408(k)
   - SIMPLE retirement account described in section 408(p)
   - Trusts described in 501(c)(18)
   - Plans for Federal, State and Local governments

   In addition to these active participants, retirees with account balances were included to reflect the benefit of the tax deferral for inside buildup.

2. Average deferrals and associated inside buildup were estimated by income class and applied to the distribution of participants. Data from the PSCA's Annual Survey provided the foundation for estimating the average elective deferrals and the corresponding employer matching contributions. Based on the average deferral rates for (lower- and higher-paid) workers, the percent of elective deferrals was determined. The estimated employer matching or profit-sharing contributions relied on PSCA's statistics and overall contribution rates.

3. Average account balances were estimated to reflect the inside buildup attributable to retirees.

4. Aggregate deferrals and inside buildup were estimated by income class and the corresponding income tax rates were applied to each income class to create the final distribution of benefits.

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[1] The number of taxpayers with pension coverage is determined from Form W-2 box 13, which indicates participation in a retirement plan.
[2] The change in the number of returns was estimated by detailed income classes to remain consistent with the 2006 return data.