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Innovations in Protecting the Old: Mostly Social Insurance and Some Assets

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For the first time in two generations, there's a growing risk of being poor or near poor in old age because the U.S. pension system has failed. The U.S. pension system is based on a three-layered pyramid, with Social Security on the bottom, employment-based retirement plans in the middle, and personal assets at the top. The second layer has collapsed over the last 35 years as employer-based pensions have shifted years to "do-it-yourself" financial-based accounts anchored in individual asset-building.

This chapter describes how the American retirement system has collapsed. There is currently an ideological commitment to individual asset building and emphasis on individual wealth for retirement and superannuation. However, this focus on individual asset building embeds fatal flaws in old age income support programs, which are described in this chapter. As a result of individual asset building, access to government subsidies for retirement savings is varied and has generated new sources of inequality.

The argument presented in this chapter is that eroding pension security for low- and middle-income workers further "commodifies" their labor. "Commodification" and "decommodification" are concepts widely used in the welfare state literature to convey the idea that social welfare spending is an indicator of how much citizens are protected from having to sell their labor in the market to earn a living. Decommodification of a labor occurs when social entitlements pay for all or a portion of basic expenses so a person does not see their labor like a commodity. Eroding the value of pensions commodifies old people's labor.

Social Security benefits have been slowly cut by 10-14 percent since 1983 (Lieberman 2012), and the normal retirement age for Social Security increased from 65 to 67. The wages of the boomers (born between 1946 and 1963) have been suppressed for many reasons—decline in unionization, trade, government policies regarding wage support, and because of the sheer size of their cohort. Over seven million boomers who would have retired under the old type of employment-based pension plans may now have to stay in, enter, or return to the labor market (Ghilarducci, Papadopoulus and Radpour 2015). 401(k) incomes are becoming more insecure and unequally distributed.

The chapter closes by presenting a way forward through an effective system based on Guaranteed Retirement Accounts (GRAs). The authors Teresa Ghilarducci and Blackstone President and Chief Operating Officer Hamilton "Tony" James introduce a GRA proposal that secures the second layer of retirement income by combining elements of social insurance with asset accumulation. GRAs will help mitigate old age poverty as well as unequal access to retirement assets and tax breaks while stabilizing the economy through the ups and downs of the business cycle.

1. The Rise of Assets in Place of Social Insurance

The second tier of the retirement income security system currently fails to deliver three necessary elements that allow lifetime consumption: a method for workers to accumulate assets, strategic investment of assets, and lifelong annuity payouts. Coverage is incomplete, investments underperform, and payments are made as lump sums rather than lifelong payouts. Coverage rates have not increased significantly for half the workforce in the U.S. since the 1980s (Ghilarducci and Saad-Lessler 2015). As a result of these failings, workers are not accumulating enough for retirement.

These liquid accounts mean that long-term savings are not matched to long-term investments and portfolios are not appropriately diversified. The failure to annuitize financial assets leaves seniors at risk of outliving their savings.

The inability to accumulate enough savings is linked to the switch from actuarially-funded defined benefit (DB) plans to commercial, voluntary, and individually directed accounts, or 401(k) and Individual Retirement Accounts (IRAs). This change of pension plan types offered in the workplace shifts the financial, investment, and longevity risk from the employer to the individual. This process of shifting risk to individuals and households without any added return or benefit describes the "Ownership Society."

Profiting from retirement income security is a fatally flawed design. The idea was part of a movement to promote an asset-based welfare state, supported by both the right and left. It gained popularity in the 1980s, pushed by liberal scholars (Sheridan and Midgely 2003) and the ideological right.

The rhetoric of an "Ownership Society" became the motivational framework behind the more recent effort to reform Social Security through private savings accounts. President Bush and Vice President Cheney described the importance of assets:

"Ownership, access to wealth and independence, should not be the privilege of the few. They are the hope of every American, and we must make them the foundation of Social Security."
(Stevenson 2001 quotes President Bush 2001)

"One of the great goals of our administration is to help more Americans find the opportunity to own a home, a small business, a health care plan, or a retirement plan. In all of these areas, ownership is a path to greater opportunity, more freedom, and more control over your own life."
(Rosenbaum 2005 quoting VP Dick Cheney)

The left also supports asset-based social welfare programs. Ed Wolff, a left-leaning economist at New York University, and his coauthor are quoted in a 2005 Russell Sage publication supporting asset-based social welfare policy:

"*Assets for the Poor is the first full-scale investigation into the importance of family wealth and the need for policies to encourage asset-building among the poor*." (Ed Wolff and Tom Shapiro 2005)

Progressive philanthropic organizations such as the Ford Foundation also reinforce the role of individual savings accounts as an important social welfare policy, including individual wealth building in their social welfare projects.

Individual accounts "*… help community residents develop their own, long-term wealth-generating capacity. They promote education, homeownership and small, local business* *development—critical elements of vibrant, sustainable neighborhoods. By teaching participants key financial skills, they empower people to make informed choices and secure their own financial wellbeing."* (Ford Foundation website 2016)

Epsing-Anderson and Pierson's (Pierson 2001) typography of social welfare reform divides "Ownership Society" into three camps: retrenchment for the sake of cost containment, recalibration to bring back some benefits, and what they call "recommodification," to take away the source of income as a right without selling labor.

The changes to the retirement income system are largely based on commodification. One result of financializing pensions is the new belief among U.S. workers that not all workers are entitled to paid time off at retirement age. However, it could be worse. A decade ago the AARP and the Democratic Party worked together to fight the commodification of old people's labor and time by successfully stopping President Bush's push to privatize Social Security in 2005 (Avsar 2008).

2. The Failure of the Current System

Commercial, liquid accounts that are individually directed underperform for everyone. Low- and middle-income workers pay disproportionately higher fees than high-income earners (Ayers and Quinn 2015). Tax breaks also underperform for low- and middle- income workers, while the highest paid workers get a disproportionate share of the benefits. Under-performing liquid accounts and lopsided tax breaks contribute to the growing retirement inequality, and some workers don't even get to retire at all.

The system's first failure is lack of coverage during working years, which results in insufficient accumulation. Only 53 percent of workers in the U.S. between the ages of 25 and 64 have a retirement plan through their employer, despite indirect subsidies from federal and state governments totaling over $140 billion in 2015.

Those workers who do have 401(k)-type retirement plans or Individual Retirement Accounts (IRAs) have accumulated a median value of only $104,000, which yields $2,500 per year in retirement, for life (Saad-Lessler, Ghilarducci, Bahn 2015).

The median account balance for all households with and without retirement plans is $12,000. Most people in the bottom 90 percent of the income distribution have no plan.

But lack of coverage (both access to a plan and participation) is only one source of inadequate accumulations. Pensions are not mandatory and can be withdrawn before retirement, which means that life events, such as an illness, unemployment, or divorce can disrupt the best intentions. The inequality this structure causes is covered in Section 4.

3. The Rise of Privatized Social Insurance Through Tax Breaks and Behavioral Economics

The rise of the asset ownership ideology abetted the financialization of the American pension system. According to Weller (2016) and Zelinsky (2008) ownership ideology lubricated the passage of laws and regulations that allowed conflicted and expensive IRA and 401(k) brokers (Anderson 2013) to manage workers' assets. In addition, employers eroded (Madland 2007) traditional employee defined benefit pensions as they discovered workers either didn't understand the value of their defined benefit plan or have the means and motivation to fight against it. Madland found that workers whose employers ended their DB system were confused who was responsible for their pensions. They did not see their employer as the chief entity responsible for securing their retirement. Workers expect the government, employers, and themselves to share the responsibility of retirement plans; therefore workers' motivation to fight for DB plans may have been weakened.

It was not always thus. Arrangements, especially in the form of social insurance—paid vacation days, sickness and superannuation—were always income elastic. Demand for paid time off increased with income. The labor movement secured shorter working times for their members, including retirement (Lambert 2005), paid holidays, funeral leave, vacations, and weekends. The song "Too Old To Work: Too Young To Die," (Glazer 1950) written during the 1950 UAW strike against Chrysler, sums up the anger over unequal access to retirement, "Your boss gets a pension when he gets too old. You helped him retire. You're out in the cold."

The demand for retirement time, backed by insurance plans, is also evinced by the democratic acceptance and expansion of Social Security between 1935-1985. During this time, more workers could express their views collectively through membership in a union. They voted to divert some compensation into defined benefit plans, which are mandatory and pay out annuities at retirement. DB plans are not used as loan collateral and can't be withdrawn before retirement. Under previous DB plans, the employer bore three risks that workers now bear under 401(k) plans. First, the employee bears the investment risk of investing in inadequate portfolios. Second, the employee bears the financial risk of retiring when the market is on a down cycle. Third, the employee bears the longevity risk of outliving her or his pension.

As the labor movement waned in the early 1980s, employers embraced 401(k) plans and retrenched their defined benefit plans, resulting in an overall decrease in employer contributions towards retirement (Ghilarducci 1998). This change transferred risk to workers and wealth to employers. The onus of failure was transferred to the individual, along with the investment, financial, and longevity risks. With the individual worker now in control, it was easy to blame the worker when the system failed. Instead of the new system coming under scrutiny, individuals were. Behavioral economics explains the failure of the 401(k) system through the heuristic mistakes made by humans.

With the rise of behavioral economics and asset-based social welfare, U.S. policy took a deep dive (Amir et. al. 2005) in to psychology and behavioral finance in the early 2000s. The "better design" or "choice architecture" became the preferred way to design social programs (Orenstein 2013, The Economist 2015), which prevails today. The argument was that tweaking human decisions was a cheaper way to solve expensive social problems as opposed to passing politically difficult mandates. A clever design of options could solve some social problems for free, like "fusion" for example.

Fusion releases clean energy with no pollution, providing all the energy gains without the cost. Policies designed to nudge humans towards making the optimal choices through "choice architecture” provide social policy “fusion” solutions. The following three examples are problems that were solved inexpensively and with little downside.

a. Problem: dirty toilets. Cass Sunstein (President Obama’s chief regulation advisor) believed that “choice architecture” could be used to overcome problems of collective action. It the case of dirty airport toilets, its application encourages men to make slight “improvements” to save millions of dollars in janitorial fees. Sunstein explains, “In a busy airport restroom used by throngs of travelers each day, the unpleasant effects of bad aim can add up rather quickly. Enter an ingenious economist who worked for Schiphol International Airport in Amsterdam. His idea was to etch an image of a black housefly onto the bowls of the airport’s urinals, just to the left of the drain. The result: spillage declined 80 percent. It turns out that if you give men a target, they can’t help but aim at it,” (Thaler and Sunstein 2008).

b. Problem: expensive and unnecessary surgeries. Wellness programs aim to make people healthier, lower costs, and encourage second opinions for expensive procedures. U.S. companies have paid for wellness programs and second opinions for decades, but workers did not join them or seek second opinions. However, by changing the reward for such behaviors into a penalty, many employers saw a surge in wellness program participation and second opinions. “Employers that used penalties or surcharges for not participating boosted their median employee participation rates to 73 percent,” (Zabawa 2015).

c. Problem: half of the U.S. workforce lacks retirement plan coverage through their employer. Behavioral economics encourages a voluntary structure. Changing the structure that requires workers to opt-out of a retirement plan at work rather than opt-in increases employee participation rates. As a result, the Obama Administration pushed for auto IRAs, whereby everyone would be automatically enrolled in an IRA with an option to opt-out (Madrian 2014). However, many people eventually do opt-out.

Imagine if Social Security were voluntary. There would be continual tax incentives to keep people enrolled, not to mention behavioral and design tricks such as "inertia" to keep people from withdrawing from their accounts during recessions and periods of household turmoil.

Consistent contributions require that people are required to contribute. The cutting edge design now is for employers to auto-enroll workers into a DB plan with the opportunity to opt-out. It may be the next best option, but unfortunately the latest research (GAO, 2010; Beeferman and Becker, 2010) suggests that auto-enrollment with an opt-out option will not yield high enough participation rates to fund an adequate pension for most low- and middle-income workers. A large portion of workers opt-out of their automatically enrolled employer-sponsored 401(k) plans at some point and never restart their contributions.

The current asset-based, voluntary, individually directed pension system coincided with a failure to perform. Behavioral economics blamed the individual's behavior rather than acknowledge that the system failed individuals, therefore resisting the need to innovate and design a better pension system.

4. **The Rise In Inequality Because of the Financialization of Pensions**

Rising inequality in retirement time is occurring for three reasons: savings shocks are unequally distributed, tax breaks are unequally distributed, and the legitimacy of being a retired person is unequally distributed.

Unequal Distribution of Exposure to Life Course Shocks

The first pathway to inequality is life's unexpected shocks. Low-income people suffer more shocks that interfere with their savings than wealthy people, making the savings process more onerous for those at the bottom 90 percent of the income distribution. (Martinez 2016) One study followed a group of workers aged 51 to 65, who did not lose their jobs in the years after the recession 2009 – 2012 (Ghilarducci, Saad-Lessler, Fisher 2015) but experienced unexpected life events. Inequality was found, not only as a result of the life events causing early withdraws from retirement accounts, but also in the intensity of the responses to those life events. Low earners were more likely to have reduced their asset balances during the recession and economic recovery. Forty-four percent of the bottom 50 percent of the income distribution had reduced account balances in their 401(k) during the recession compared to 39 percent in other income groups. Low-income people have 7.37 percent more income shocks than middle and high-income groups in their lifetime. The top 10 percent had fewer lifetime weeks unemployed—1.4 total weeks—than the bottom 90 percent (See Figure 1).

The government also subsidizes high-income workers more than low-income workers by conferring many more tax benefits to high-income savers than low-income savers. The growing gap between those who have retirement security and those who do not is partially a consequence of the inefficient and inequitable savings incentives embedded in the U.S. tax code.

Households that need the most help saving for retirement receive the least assistance from the federal and state governments. The tax code is used as an incentive for people to save via tax advantages that vary by type of savings, such as individual retirement accounts, IRAs, 401(k) plans, or Roth IRAs. These savings incentives are complex; information about tax breaks and the confidence to override them bar some workers from participating.

Savings incentives benefit high-income earners more than middle- and low-income earners because high-income earners face higher tax rates and thus enjoy greater tax breaks from existing savings incentives. High-income earners are likely to contribute more because they have substantial income and are not liquidity constrained. They are also more likely than low-income earners to have a retirement plan through their employer.

Even if a high- and low-income earner save the exact same amount of money, the high-earner will accumulate more retirement assets because the high-income earner earns a higher net of tax rate of return and pays lower fees.

These costly savings incentives fail to prepare households adequately for retirement and the public loses out on increasingly large amounts of tax revenue that would otherwise have been collected without these tax breaks. Federal and state governments forgo a substantial amount of tax revenue to create incentives meant to help people save for retirement, but in reality produce little additional savings. The federal government alone annually forgoes more than $100 billion in personal income tax revenue due to retirement savings incentives. (Weller and Ghilarducci 2015) State governments with income taxes lose substantial tax revenue—about $20 billion. (Ghilarducci and Martinez 2016)

Figure 1: The Unequal Distribution of Lifetime Shocks That Affect Retirement Savings				
	balances 2012	shocks	weeks un-employed	percent who lost money in recession
Bottom 50 percent of income distribution	$ 65,006	7.37	2.86	44 percent
Middle 40 percent of income distribution	$ 132,510	5.86	2.44	39 percent
Top 10 percent of income distribution average	$ 218,556	6.06	1.40	39 percent
Source: Ghilarducci, Sadd-Lesser, and Fisher (2015)				

Another study (Ghilarducci, Webb, Radpour 2016) found that between 2009 and 2011, one fifth of low-income 401(k) participants were likely to experience a shock, including job loss, divorce, health problems, or a job change. Middle-income workers experienced a 17 percent risk and high-earners an 11 percent risk of a life shock. Life shocks that trigger 401(k) and IRA withdrawals are more likely to happen with low- and middle-income households. Furthermore, since workers in low-income households are more likely than those in middle- and high-income households to respond to an economic shock by withdrawing money from retirement savings, the ordinary conduct in the American economy results in an unequal distribution of retirement wealth and access to retirement.

Unequal Access to Government Retirement Subsidies

The second pathway to inequality is through tax expenditures, government subsidies for retirement savings accessed through the tax code. Tax expenditures are revenue losses to federal or state treasuries from tax exclusions and deferrals.[1] Aimed at promoting a social goal, tax

[1] Tax expenditures are entitlement spending: the size determined by the number of taxpayers who participate in the preferred activity and claim the benefit on their taxes. As part of the tax code, tax breaks are immune from "sunset provisions" that automatically terminate unless extended through a process of legislative oversight and action. Experts criticize entitlements as that allow the growth of government spending without appropriate scrutiny and evaluation and, in part because of the lack of scrutiny, retirement savings tax expenditures have been widely criticized as ineffective and regressive (Government Accountability Office 2005)

expenditures are designed to create a positive externality. In 2014, federal retirement plan tax expenditures were $94.6 billion. Spending on defined contribution plans, such as 401(k)s, made up the largest share of this total. The costs of these tax subsidies are projected to increase to $222.1 billion in 2018, a total of $805.1 billion over five years (U.S. Treasury 2015).

Those with the highest balances receive the most benefit from retirement tax expenditures. Seventy percent of the tax benefits go to taxpayers in the top 20 percent of the income distribution. Those in the top 10 percent hold a vast majority of retirement assets. Because tax expenditures are skewed to those with the highest incomes, the experience of the top 25 percent is drastically different from the lower 75 percent.[2]

In addition to promoting inequality, tax expenditures are ineffective. In 1980, the tax expenditure per worker was $406 (in 2016 dollars) and the retirement plan coverage rate was 46 percent. By 2015, the coverage rate had fallen slightly to 45 percent of all workers having a retirement plan at work, but the tax expenditure per worker more than doubled to $997 (See Figure 2).

Replacing ineffective tax deductions with refundable tax credits would provide 88 million workers with $607 to save for retirement. An additional $197 would go to 70 million people living in states with an income tax for a total of $804.

Figure 2: Increasing Tax Expenditures Did Not improve Coverage

2016 Dollars					
Year	Coverage	Tax Expenditures	Workforce	Tax Exp per Person Covered	Tax Exp per Worker
1980	0.46	$43,550,000,000	107,352,000	$882	$406
1990	0.47	$111,670,000,000	126,142,000	$1,884	$885
2000	0.52	$129,220,000,000	143,248,000	$1,735	$902
Present	0.45	$157,400,000,000	157,833,000	$2,216	$997

[2] For example, a worker earning $2,000 a month has a marginal tax rate of 10 percent, pays a $200 tax bill, and has $1,800 remaining in after-tax income. But if this worker contributes $200 to a 401(k), her taxable income is $1,800 and she owes only $180 in taxes. She will have less after-tax income - $1,620 versus $1,800 - but she now has $200 in a retirement account and has saved $20 on her tax bill. Tax is not paid on the investment gains in the account during accrual. When she withdraws the savings – presumably when retired and paying a lower tax rate 4 – she will pay less in taxes.

Unequal Access to Retirement Legitimacy

The third avenue of inequality is the unequal distribution of legitimacy, or the collective social belief that retirement before ill health is increasingly only available for the wealthy (Estes, 2001). The legitimacy of retirement, a form of paid time off, is under challenge for working class people (Moulaert and Biggs 2012).

There are more working people ages 55 and older than ever before in the United States. Most of the population growth since the mid-1980s has been among older Americans. The labor force participation rate among men and women aged 55+ is at an all-time high, primarily due to women's increased participation. Between 1985 and 2013, the labor force participation rate for women ages 55 and older increased from 22 percent to just over 35 percent. Men's participation rate rose from 41 percent to nearly 47 percent. Expert opinion emphasizes two overlapping reasons more people are working at older ages: the love of work and money.

It's estimated that the increased levels of education among older workers accounts for almost half of the increased older worker labor force participation (Burtless 2013). In 1985, less than 20 percent of workers between the ages of 60 and 64 had college degrees. Thirty-five years later in 2013, over 36 percent had college degrees. Enfranchising older women into mainstream economic life accounts for part of the trend.

However, many older people are working because their "reservation wage" has fallen. A reservation wage is the lowest wage someone would accept to enter or stay in the labor force. Everyone's reservation wage falls—and the need to work increases—when the income one gets from a family member, a pension, or some other source erodes and becomes more insecure. Older people will remain in or reenter the labor market if their pensions erode, whether it's from the payouts or income from retirement benefits or Social Security.

The amount of income an individual receives from non-wage sources is a key factor in determining their reservation wage. As the elderly person's non-labor income erodes and Social Security replaces waning retirement income, the reservation wage falls. The average replacement rate will fall as the full benefit age increases to 67, and real benefits are reduced for beneficiaries between ages 62 and 67.

Most older workers have no traditional pension and little more than half have a 401(k) or IRA. This leaves almost half of older U.S. workers with nothing besides Social Security. Those who do have access to a retirement savings plan have a median balance of $111,000 (2013). This sum would provide a retiree with only about $400 per month.

Nonexistent and inadequate 401(k) account balances reduce bargaining power for older workers, the power to quit a job or find a desirable job. Older people will have to take low-wage jobs with poor working conditions. And what's worse than having a poor-quality, low-wage job? Faced with inadequate retirement income, having no job at all.

Older people's job quality has not improved over time. The share of older workers who describe their jobs as physically demanding is increasing and those who report their jobs as easy is decreasing. The incidence of requirements for stooping, bending, using keen eyesight and intense concentration is increasing.[3]

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[3]

Some workers are coming into retirement with poor health after working jobs that degraded their health. Research by Lauren Schmitz funded by the National Science Foundation found that older workers who have less control over their jobs suffer worse health outcomes. Continuing this work may foreshorten their lives. A simple characteristic of a good job—less stressful and more healthful—is one that allows workers to control the pace and content of their time and work. For many people, the only way to remove stress from their lives is to retire with a decent pension, enabling them to control how they spend their time.

Workers in the U.S. already work longer than most people in advanced industrialized countries. The OECD reports that the United States ranks in the bottom third in achieving a balance between work and life (OECD 2015). Americans work 1,790 hours per year; the OECD average is nearly a week less. The U.S. ranks 8th out of 33 nations in the percentage of adults working long hours, 11.8 percent versus the average of just under 8 percent. For example, less than 1 percent of Dutch workers work more than 50 hours a week. The United States leads rich countries in low-wage jobs, paying two-thirds of the median wage. Over 22 percent of the jobs in the U.S. pay less than $23,000 per year. This is the reality of the labor market for older job seekers. As such, many find work in the service and retail sectors.

Further evidence that older American workers have lost bargaining power is that they are more likely to say they are ready to work, even with worse health compared to older people in a select group of European nations (see Table 2) Heiland and Yin (2015) report that if workers in the U.S. assessed their health the same way Swedes did, they would report twice as many work limiting disabilities than they do now. While Americans report they are ready to work at older ages, they are objectively sicker. Older people in America have more severe health problems but are less likely than workers in European nations to say they are severely disabled and can’t work (See Figure 3).

In addition to Heiland and Yin’s important work, it’s evident via statistics using data in Figure 3 that the relative generosity of a nation’s disability system impacts a worker’s willingness to admit if they are limited in their ability to work.

The correlation between self-reported work limitations and the objective condition of diabetes is negative, meaning if a worker is sick, they likely say they can’t work. The correlations in different countries between being sick and a worker reporting they can’t work confirm Heiland and Yih’s conclusion. The relationship between being sick and perceiving a limitation from work depends on the generosity of the country’s disability program.

The number of needs for assistance with daily living (ADL) is a standard measure of disability. The correlation between having a ADLs and a worker reporting they can't work is expected to be near 100 percent. Without including the United States, the correspondence between having ADLs and reporting the inability to work is 66 percent. But when the U.S. is included in calculating the correlation between ADL and work limitations the correspondence between having a lot of ADLs and reporting an inability to work drops to 25 percent.

Figure 3: Older Americans are Sicker But Work More and are Less Likely to Report Work Limitations

	Average age	Labor force participation of 65-69 year olds: 2000 (OECD)	Labor force participation of 65-69 year olds: 2014 (OECD)	Education	Diabetes	ADL limitations	No Self-reported limitations of work	Extreme severe and severe: Self-reported limitations of work:
Netherlands	62.8	6.0	15.7	11.5	0.07	0.09	0.54	0.06
Germany	63.8	5.1	14	13.1	0.11	0.09	0.42	0.08
France	64.9	2.1	5.9	8	0.09	0.16	0.51	0.08
Europe	64.1	8.6	12.4	9.6	0.09	0.13	0.48	0.09
Belgium	63.9	2.9	4.7	10.2	0.08	0.17	0.38	0.09
Italy	63.7	6.4	8.4	7.2	0.09	0.17	0.47	0.1
Spain	64.8	3.9	4.6	7.1	0.12	0.13	0.45	0.13
US	64.6	24.5	31.60	12.7	0.18	0.22	0.45	0.14
Sweden	64.1	14.5	21.8	10.4	0.07	0.09	0.56	0.15
Correlations with all nations with severe limitations of work					0.45	0.25		1
Correlations with all nations with severe limitations of work without the US					0.97	0.66		1

The rate of diabetes and rate of self-reporting among older workers in the U.S. ages 65-69 that they can't work, is higher than the rates of other countries. The relationship between the rate of sickness with diabetes and being severely limited in work is expected to be near a one to one correspondence. Not including the U.S. the correspondence between having diabetes and reporting an inability to work is 97 percent. But when the United States is included in calculating the correlation between ADL and work limitations the correspondence between having a lot of ADLs and reporting an inability to work, it drops considerably to 45 percent.

Many people might not consider the elderly and impaired workers in the U.S. who are willing to work a problem to be solved. The National Academy of Science (2013) views older workers in the labor market as a key driver for long-term growth (more in Section 6). Attracting older workers—what Henry Aaron at the Brookings Institution calls "bribing"—will have a better effect on productivity than "mugging," forcing people without pensions to work. If people are forced to work because they have no pensions their skill levels will likely be lower than average (Burtless 2013).

The next section assumes that policy makers prefer employers boost the labor force participation of older workers by tackling age discrimination (Neumark 2015) and encouraging employers to make work more inviting. The proposals below include policies aiming to boost the reservation wage of older people through secure pensions.

5. Solutions: Despite My Criticisms, Innovations will have to be in Hybrids

I recommend a new pension system that is a hybrid design of asset-based accounts with insurance-like features. This innovation is a combination of the comprehensive policy recommendations calling for the preservation and expansion of Social Security and the implementation of Guaranteed Retirement Accounts (GRAs). Rather than just solve the problem of inadequate retirement assets, we must also combat unequal distribution of retirement readiness, access to retirement that results in downward mobility of middle class workers, poverty, and chronic deprivation among the old. Additional problems include the ineffective use of tax expenditures and the unintended consequences of lowering the reservation wage of older Americans. These problems are the result of flawed retirement plans and policies, rather than flawed humans, hampered by a variety of heuristic problems identified by behavioral economists (Thaler and Sustein 2008 cited above)

Social welfare policy took a wide swing into psychology and behavioral finance in the early 2000s. The "better design" or choice architecture" approach prevails today. Tweaking human decisions is cheaper and more effective than traditional policy tools like social insurance or welfare in order to solve large social problems.

An optimal pension system (Barr and Diamond 2009) includes social insurance as a key design feature. A pension system should also help stabilize and grow the economy, a function described in a later chapter.

Accumulation

The Guaranteed Retirement Account (GRA) aims to strengthen retirement security by increasing accumulation. Low- and middle-income families are especially helped by mandatory contributions into private asset-based accounts. GRAs apply to all full-time, part-time and 1099 workers. Senator Elizabeth Warren (Warren 2016) called for all employee benefits and protections to be delinked from employers. Indeed this plan does delink benefits and protections, although savings and contributions occur at the point of wage and salary payment. GRA contributions would be 3 percent of wages, with half paid by the employer and half paid by the employee. To ease the burden on low-earners, all workers would receive a tax credit up to $600 per year, making the after-tax cost to workers earning $40,000 or less zero. For high-income workers, the obligation to contribute is capped, the 1.5 percent mandate for employees and employers would apply only to the first $250,000 of income. Workers would be encouraged to contribute additional funds to their GRAs.

Employers would be required to offer a defined benefit pension or contribute to a GRA. The proposal assumes that most employers would choose GRAs due to lower costs. The benefit to those who provide pensions are not penalized by having to compete with firms that do not.

Accumulation is further enhanced by repurposing current 401(k) and IRA tax breaks into retirement tax credits. The plan would be revenue-neutral and deficit-neutral. The cost of the new tax credit would be offset by the savings from eliminating existing tax deductions for 401(k) plans and IRAs. Existing 401(k)-type savings accounts would be rolled over into GRAs.

Investment

Investment of the accumulated assets is improved through competition, regulation, and ending the requirement that long-term retirement savings be invested in short-term assets. At the beginning of each year, individuals could choose or change their own money managers from a national exchange of managers administered by the federal government. Money managers would be federally licensed and regulated. The key feature is that GRAs would be pooled, which would reduce administrative fees and could be invested in less liquid, higher-yielding, higher-return asset classes including real estate, managed futures, and commodities.

The proposal assumes that GRAs would earn a 6-7 percent rate of return. To reduce workers' risk, the government would guarantee a minimum return of 2 percent on average over the long term. The government could charge for this guarantee.

De-accumulation

To solve the problem of individuals bearing too much longevity risk upon retirement, each worker's account would be automatically annuitized to provide a source of lifetime income. The Social Security Administration would administer the annuity payments, including them in Social Security benefit disbursements. Workers could chose to annuitize their GRA at any age from 62 to 70, with or without collecting Social Security benefits. Each worker's annuity would take into account their age and marital status. Before annuitization, GRA balances would be inheritable. But once the account had been annuitized, it would not be inheritable. Affluent retirees with annual income of $250,000 or more from sources other than the GRA would not be eligible to receive any annuity income from their accounts, though they could deduct the value of the annuity not received from their taxable income.

The accounts are paid for by individuals, employers, and repurposed tax deductions from federal (and presumably state) governments.

6. Asset-Based Programs Make Recessions Worse

This section briefly sets out the case that a guaranteed pension system provides automatic stabilizers to the economy. Unlike 401(k) plans and IRAs that destabilize the economy, defined benefit plans and social insurance plans do not. During the Great Recession of 2008–2009, the gap between actual real gross domestic product (GDP) and potential output fell by $504 billion. Because of the decline in household and business spending between December 2007 and December 2009, employment fell by 5.7 percent—a loss of 8.3 million jobs—and the unemployment rate peaked at 10 percent in 2009.

To counter the recession, the federal government spent $700 billion on stimulus programs.[3] But the largest source of recession mitigation, built-in automatic stabilizers, quietly injected billions of dollars into the spending stream of the economy. Traditional automatic stabilizers such as unemployment insurance, means-tested programs and the progressive tax system (which has the largest stimulative effect as the average marginal tax rate shrinks as more people fall into the lower brackets) helped mitigate the effects of the downturn.

Nontraditional automatic stabilizers, Social Security's Old-Age and Survivors Insurance, Social Security Disability Insurance (SSDI), Medicare, DB and 401(k)s, also had an effect. People have used these programs in recessions as income and life-style support; taxes used to finance those programs reduce spending in expansions. Depending on which measurement used for the marginal propensity to consume, progressive income taxes, UI, OASI, SSDI, and Medicare combined reduced the number of jobs lost in 2009 between 81,456 and 967,506.

Over half of U.S. households own Individual Retirement Accounts (IRAs), 401(k)s, and 401(k)-type accounts; the values of those accounts fell by an average of 14 percent in 2008. Middle-income and low-income households, whose current and future retirement income wealth derives primarily from OASI, SSDI, defined benefit pension plans, and Medicare, lost almost nothing in 2008–2009.

OASI, SSDI, UI, Medicare, and federal taxes temper the output gap's effect on unemployment by injecting more net household spending in recessions, and dampening spending in expansions. Those programs are automatic stabilizers. In contrast, 401(k) plans and other financial market–based retirement accounts have a destabilizing effect; the reductions in wealth and income in recessions cause less spending and more induced labor supply than would otherwise be.

Bottom line: the existence of 401(k) plans and other financial market–based retirement wealth, with values that fluctuate with the business cycles, made the last recession deeper and caused slightly more unemployment than if 401(k) plans did not exist (Ghilarducci and Sadd-Lessler 2015). Annuity-based retirement accounts backed by government programs helped the economy while financial market–based retirement programs such as 401(k) type programs hurt the economy.

7. Conclusion

Extending large tax breaks and encouraging more voluntary participation in individually directed commercial liquid 401(k) and IRA accounts may boost participation. But the investment and distribution aspects make the system ineffective, very expensive, and a catalyst for more inequality. The system relies on tax breaks to encourage participation, which are only extended to people with the smallest risk of not having enough retirement assets. In addition, a pension system with automatic enrollment, automatic investing in safe instruments, and auto annuitization, doesn't work either. It's still a voluntary system and depends on people not opting out, preserving a libertarian paternalism philosophy

The Obama administration (White House 2015) spent eight years trying to implement the Auto-IRA, keeping with this libertarian paternalism philosophy. However, as with many monumental social problems, solutions take real money, which Obama didn't spend. It is possible to get real money for comprehensive pension reform from progressive taxation and reducing the regressivity of our current tax system.

A well-designed system has important macroeconomic features. It restores and maintains sources of net wealth for households. A well-designed pension system allows the household sector to be the savers, while the business and government sectors are deficit spenders.

The 401(k) structure is not suited for pensions and the government subsidies are perversely incentivized. The problem is not bad human decision-making or financial illiteracy, but rather bad policy. Life events can and do happen to workers over their lifetime, disrupting their best-laid plans to save for retirement. Lump sum distributions cause depression, while annuities make old people happy. Asset ownership induces shame, blame-the-victim narratives, and demonstrates a lack of political will.

A pension system should provide three simple elements to enable life-course consumption. One, accumulate sufficient assets over a lifetime, two, invest those assets well, and three, distribute the assets in a lifelong stream of income (Ghilarducci and James 2016). The Guaranteed Retirement Account plan satisfies all three functions. Sufficient accumulation is achieved through mandatory participation and banning all withdrawals before retirement. Investments are low fee, pooled, and invested to match the long-term liabilities; payouts are in the form on an annuity.

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