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

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Abstract

The risk of being poor or near-poor in old age is growing for the first time in two generations because the American pension system has failed. The American system evolved into a patchwork of loosely connected private-public programs that many people have tried to rationalize by describing the system with various metaphors of stability—a three- layered stool, a multi pillar system, and a layered pyramid. I use the pyramid metaphor describing the relative sizes of the sources of income to middle class elderly—Social Security is the most important so it sits on the bottom, employment-based retirement plans sit in the middle, and personal assets are the least important—that layer sits at the very top. But the system is a crumbling, unstable pyramid that is creating serious sources of inequality in retirement security. A main cause is that employer-based pensions have been transformed over the last 35 years to "do-it-yourself" financial-based accounts and away from a system based on social insurance principles.

This chapter describes how the American retirement system collapsed, in part, because of ideological commitments to individual asset-building. The emphasis on individual wealth to insure the known risks of retirement and superannuation embedded fatal flaws in old-age income support programs. Some of the consequences were new sources of inequality, such as access to retirement and government retirement subsidies.

Eroding pension security for low- and middle-income workers "commodifies" their labor in old age (compels them to work for pay) as the normal retirement age to qualify for Social Security benefits started to increase with the reforms of 1983 from 65 to 67 for people born between 1954 and 1960 and 401(k) income becomes less ample, more insecure, and more unequally distributed. Additionally, the wages of older boomers will be suppressed, as they have over the cohort's experience, as 7 million boomers who would have retired under the former pension plans may now stay in or re-enter the labor market (Ghilarducci, Papadopoulus, and Radpour 2016).

The chapter closes with a way forward to a better designed system, the "Guaranteed Retirement Account (GRA)," which combines social insurance elements and asset accumulation to shore up the crumbing second layer of retirement income (Ghilarducci and James 2016). The GRA will help mitigate the problem of inequality of retirement time, assets, tax breaks, and the coming problem in old age poverty. The GRA will also stabilize the economy over business cycles since 401(k) s and IRAs work as automatic destabilizers—they induce households to save more and work more in downturns, the opposite effects of macro-stabilizers. .

1. The Rise of Assets In Place of Social Insurance

The second tier of the American retirement income security system fails to deliver the three elements of any good pension system. A pension system is designed to smooth consumption over a lifetime in three basic steps: the system helps workers accumulate assets, invest the assets efficiently, and convert them to annuities—pensions for life. The U.S. financial-based system is flawed on all dimensions: coverage is incomplete, the investments underperform, and the payments are in lumps and not lifelong. Spotty coverage and leakages mean people do not accumulate enough for retirement. The liquid account mean long-term savings are not matched to long-term investments and an appropriately diversified portfolio. Furthermore, financial assets are not converted into a payout stream of benefits for life. (Uthoff, this volume, discusses the Chilean pension system has having some of the same problems.)

Most workplace retirement plans are 401(k)-type plans. Most assets in Individual Retirement Accounts (IRAs) (administered not by employers but by financial institutions) is money from a 401(k) plan. The three-decade long decision of employers and policy makers to engineer a switch from actuarially-funded defined benefit plans to commercial, voluntary, and individual directed accounts has shifted financial, investment, and longevity risk to individuals who are the people least able to insure against them. Thus, the "asset ownership society" is a process that shifts risk to individuals and households with no added return or benefit to them. (In Chile, the financial industry benefited greatly (Uthoff, this volume)).

Despite the fatal flaws in the design, the financialization of retirement income security was part of a movement supported by both the right and left to promote an asset-based welfare state. The push for an asset-based social welfare state took off in the 1980s as both the left, liberal scholars (Sherradan 2003 and and Midgely 2003) and the ideological right have promoted an asset-based welfare state.

The rhetoric of "Ownership Society" had become the motivational frame behind the reform of Social Security through private savings account. Here, President Bush and Vice President Cheney describe 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, quoting 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 supported asset-based social welfare programs. Ed Wolff, a left economist at New York University (NYU) and his coauthor are quoted in a publication from a Russell Sage (2005) project 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 institutions, such as, the Ford Foundation, repeated the role of individual savings accounts as an important social welfare policy in their individual wealth building program:

> [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 (2001) dichotomy of social welfare reform divide the welfare state reform into three camps: retrenchment for cost containment sake, recalibration to bring back some benefits into line, and commodification to take away the source of income as a right without selling labor. The changes in the U.S.'s system of retirement income was mostly all commodification. Financializing pensions—supported by the asset movement—resulted in an unravelling of widespread support for the proposition that all workers—not just the well off—are entitled to paid time off at retirement age. The one important source of resistance to commodification of the labor time of the elderly was the labor movement, AARP, and Democratic Party's success in stopping President Bush's push to privatize Social Security in 2005 (Avsar 2008).

2. The Failure of the Current System

Because individual-directed, commercial liquid accounts underperform for everyone, low- and middle-income workers are especially hit hard because they pay disproportionately higher fees (Ayers and Quinn 2015). The tax breaks also underperform for low- and middle-income workers as the highest paid receive a disproportionate share of the benefits. Because of the inequality of under-performance and lopsided tax breaks, there is a growing inequality to access to retirement.

The first aspect of the failure of the system is lack of coverage and, thus, too little accumulation. Only 53% of American workers between the ages of 25 and 64 have a retirement plan at work, despite the generous indirect subsidies from federal and state governments, which totaled over $140 billion in 2015. Those who do have 401(k)-type retirement plans or IRAs have only accumulated a median value of $104,000 in those accounts. In retirement, this yields only $2,500 per year for life (Ghilarducci, Radpour, Fisher, and Saad-Lessler 2015). Including all households with and without a plan, the median account balance is $12,000. Most people in the bottom 90% of the income distribution have no plan.

But lack of access and participation is only source of inadequate accumulations. Because pensions are not mandatory and can be withdraw before retirement, life events can disrupt the best intentions. The inequality this structure causes is covered in section 4 on inequality.

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

The financialization of American pension plans were abetted by the rise of the ideology of asset ownership because it lubricated a series of Congressional Acts; permissive regulations by the Labor Department and Treasury on 401(k) plans and IRAs (Weller 2016); entrepreneurial activity by 401(k) brokers (Anderson 2013); and employers who discovered their employees did not either understand the value of their defined benefit plan or had the means and motivation to fight against their erosion (Madland 2007) .

It was not always thus. For workplace benefits that pay workers for time off (paid time off for vacation, sickness, and the largest form of paid time off), time off for old age and “superannuation” were benefits that were luxury-type goods and are income elastic—demand for paid time off increased with income. The labor movement always included shorter working times, including retirement, paid holidays, funeral leave, vacations, and weekends, in the list of demands. The song, “Too Old to Work: Too Young to Die” (Glazer 1950), written during the 1950 UAW strike against Chrysler, summed 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 from 1935–1985. When workers were represented by unions and could express their views collectively about their financial future, they voted to divert some compensation into defined benefit plans, which are mandatory and pay out annuities at retirement. They are not used as loan collateral and they cannot be withdrawn before retirement. The employer bears three risks that are placed on workers in 401(k) plans: 1) the investment risk—investing in inadequate portfolios; 2) the financial risk—retiring when the market is on a down cycle; 3) the longevity risk—outliving your pension.

Starting in about 1980, as the labor movement waned, employers embraced 401(k) plans and retrenched their defined benefit plans resulting in an overall decrease in employer contributions towards retirement. Risk was transferred to workers and wealth transferred to employers. The onus of failure was also transferred to the individual with the investment; financial and longevity risk was transferred. When the individual worker was given control, it was seamless to blame the worker when the system failed. Instead of the design coming under scrutiny, individuals were. Behavioral economics explained that the 401(k) system failed because of heuristic mistakes humans make.

With the rise of behavioral economics and asset-based social welfare, policy took a wide swing (Amir et al. 2005) into psychology and behavioral finance in the early 2000s and the “better design” or “choice architecture” became the preferred and professed stronger ways to design social programs (Orenstein 2013; The Economist 2015). The argument was that tweaking human decisions is a cheaper way to solve expensive social problems than through politically difficult mandates. Clever design of options could solve some social problems free. Free, just like fusion. Fusion releases great clean energy with no pollution. All the gains of energy without the cost. In like manner polices designed to nudge humans to make the social optimal choices through “choice architecture” offers up social policy “fusion” solutions. Here are three examples of problems solved cheaply, it seems with little downside.

a. Problem: Dirty toilets. Cass Sunstein (Obama’s chief regulation advisor) explains that the power of “choice architecture” overcomes collective action problems, it makes individuals—in this case men—make slight private “improvements” that will save millions of dollars in janitorial money. 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 house fly 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 with lower costs and encourage second opinions about expensive course of action. For decades, companies paid for wellness programs and second opinions. But, workers did not join up or seek second opinions. By changing the reward into a penalty, many employers saw a surge in wellness program sign-ups 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 workforce not being covered by pensions. Behavioral economics encourage the same voluntary structure, but by making people opt out of their 401(k) rather than opt in, studies show peoples tendency toward inertia raises the participation rate. Therefore, the Obama Administration pushed for auto IRAs, whereby everyone would be auto enrolled in an IRA and individuals could opt out, rather than have to take the affirmative step to decide and actively opt-in (Madrian 2014). But many people eventually opt out. Imagine the failure and the expense if Social Security relied on "inertia" to keep people in the system and not withdrawing from their accounts in recessions and household turmoil. Social Security participation would have to be tax incented.

The design of asset-based, voluntary, individual-directed pension systems coincided with its failure to perform and behavioral economics focused on blaming individual behavior rather than innovate for a better design. The design of asset-based, voluntary, individual-directed pension system also caused inequality to grow in two ways.

4. The Rise of Inequality because of the Financialization of Pensions

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

Unequal Distribution of Exposure to Life-Course Shocks

The first pathway to inequality is shocks. The design of the system and the facts of life make the saving process much more onerous for those at the bottom 90% of the income distribution. Lower income people suffer more shocks that interfere with their saving than wealthy people. The second pathway is that the government subsidizes higher-income workers more than lower-income workers.

First, shocks. One study followed a special group of workers who were aged 51-65 and who did not lose their jobs in the years after the recession 2009-2012 (Ghilarducci, Saad-Lessler, Fisher 2016). This study found clear inequality in not only the life events that cause retirement account leakages, 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% of the income distribution reduced account balances in their 401(k) during the recession, compared to 39% in the other income groups. Lower-income people had more income shocks in their lifetime, 7.37 compared to fewer in the middle- and top-income groups. The top 10% had many fewer lifetime weeks unemployed than the bottom 90%: 1.4 total weeks unemployed (See Table 1).

Table 1: The Unequal Distribution of Life time Shocks That Affect Accumulation

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

Another study (Ghilarducci, Webb, and Radpour 2016) found that in just two years, 2009–2011, one fifth of low income 401(k) participants were likely to experience job loss, divorce, health problems, or a job change. In contrast, middle-income workers experienced a 17% risk and high earners had an 11% risk. Shocks trigger 401(k) and IRA withdrawals and that low- and moderate-income households are more likely to withdraw, conditional on experiencing a shock. Furthermore, since workers in low-income households were more likely than those in middle- and upper-income households to respond to an economic shock by withdrawing money from their retirement savings, the ordinary conduct of economic life 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 the structure of the government subsidy for retirement saving, called tax expenditures. Tax expenditures are revenue losses to federal or state treasuries from tax exclusions and deferrals.[i] Aimed at promoting a social goal, tax expenditures are designed to obtain a positive externality. In 2014, federal retirement plan tax expenditures were $94.6 billion. Spending on defined contribution (DC) plans, such as 401(k) plans, made up the largest share of this total. The costs of these tax subsidies are projected to increase to $222.1 billion in 2018, for a total of $805.1 billion over five years (U.S. Treasury 2015).

Those with the highest balances garner the most in tax expenditures--70% of the tax benefit go to the top 20% of taxpayers. The top 10% have a vast majority of all the retirement assets, the experience of the top 25% is very different than the lower 75%. Therefore, the tax expenditures are highly skewed to the highest income savers.[ii] And the tax expenditures are clearly ineffective. In 1980, the tax expenditure per worker was $406 in 2016 dollars and the retirement plan coverage rate was 46%. By 2015, the coverage rate had fallen slightly to 45% of all workers having a retirement plan at work but the tax expenditure per worker more than doubled to $997 (See Table 2).

Table 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
Sources: EPI Retirement Inequality Chartbook, BLS, JCT, EBRI					

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 who live in states with an income tax, for a total of $804.

Unequal Access to Retirement Legitimacy

The third avenue of inequality is the unequal distribution of legitimacy, the social approval of 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 S 2012).

More people ages 55 and older are working than ever before in America because most of the population growth since the mid-eighties has been among older Americans and because the labor force participation rate among men and women aged 55-plus is higher than ever before, mainly due to women's increasing 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 emphasize two overlapping reasons more people are working at older ages: the love of work and money. First, there is love of work, of being productive in the marketplace, of developing new skills and meeting new challenges. The second reason is money.

The good news about older workers is that they are more educated, and since more educated people work more, it is estimated that the increase in education accounts for almost half of the increase in 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. In 2013, 35 years later, over 36 percent did. Enfranchising older women into mainstream economic life is part of the trend. Labor income gives women some independence and more equal footing with men, and that was good news for men and women.

But many older people are working because of their reservation wage, or the minimum wage required to lure one into the work force. The amount of income from non-wage sources is a key factor in determining a person's reservation wage. As non-labor income to the elderly erodes the reservation wage as Social Security replaces less retirement income—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 and most older workers have no traditional pension and only little over half have a 401(k) or IRA. As mentioned above, almost half of older workers have nothing besides Social Security, and the half who do have a median amount of $111,000 (2013), which would yield about $400 per month. A part-time, minimum-wage job will get you almost twice that.

So, here is the disturbing part of the new work reality for older workers. Nonexistent and too-small 401(k) account balances reduce bargaining power for older workers, limiting their power to quit a job or find a job they want. Older people will have to take low-wage jobs with poorer working conditions than they want, and what would be worse than having a poor-quality, low-wage job--not having one at all when you don't have an adequate income.

Also, the quality of jobs older people hold have stopped improving. The share of older workers who say they have very physically demanding jobs is increasing and the share of jobs reported as easy is falling. The incidence of requirements for stooping, bending, and using keen eyesight and intense concentration is increasing.

In addition, some workers are coming into retirement with poor health because of their lifetime jobs; continuing to work may degrade their health. Lauren Schmitz's (2015) National Science Foundation-funded research found that older workers who have less control on their jobs suffer worse health outcomes and continuing 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 get the control they need and to get away from stress is to retire with a decent pension so they can control how they spend their time.

Consider this: Americans already work more years and more weeks per year than most people in many other 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 more hours per year, at 1,790 hours per year. The OECD average is almost a week less, and the United States ranks 8th out of 33 nations in the percentage of adults working long hours: 11.8 percent versus the average of 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 jobs in the United States pay less than $23,000 per year. Older people face this labor market reality as many find work in the service and retail sectors.

Further evidence that 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 nations (with detailed health and retirement status data (Heiland and Yin 2015)). American older people have more severe health problems, but are less likely to say they are severely restricted to work (See Table 2).

The correlation between self-reported work ability and the objective condition of diabetes is negative, but more negative when the U.S. is not included in the correlations. For all countries reported above, the correlation is -38%. But without the U.S., the negative correlation is stronger, -52%. Further evidence that American workers are more likely to say they are ready to work even with worse health is found in the correlation between self-reported severe work limitations and having many ADLS is negative, but more negative when the U.S. is not included in the correlations. For all countries reported above, the correlation is -7%. But without the U.S., the negative correlation is stronger, -17% (See Table 3).

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

	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	Self-reported limitations of work none	Self-reported limitations of work: Extreme severe and severe
US	64.6	24.5	31.6	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
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
Europe	64.1	8.6	12.4	9.6	0.09	0.13	0.48	0.09
Italy	63.7	6.4	8.4	7.2	0.09	0.17	0.47	0.1
France	64.9	2.1	5.9	8	0.09	0.16	0.51	0.08
Belgium	63.9	2.9	4.7	10.2	0.08	0.17	0.38	0.09
Spain	64.8	3.9	4.6	7.1	0.12	0.13	0.45	0.13
Sources: Heiland and Yin. 2015 and OECD Stats								

Many may not consider American elderly and impaired workers willing to work a problem to be solved. The National Academy of Science (2013) views getting older workers to work as one of the key drivers to long-term growth (more in Section 6). Older workers choosing to work because work provides hours, wages, and opportunities for skill enhancement in comparison to an adequate retirement is likely to have the effect on productivity that the added worker effect has. Attracting workers—what Henry Aaron at the Brookings Institution calls “bribing” older workers will have a better effect on productivity than “mugging,” or forcing people without pensions to work.

The next section assumes that public policy makers prefer employers to boost older labor force participation by tackling age discrimination (Neumark 2015) and encouraging employers to make work more inviting. The policy solution below constructs policies that aims to boost the reservation wage of older people by securing their pensions.

5. Solutions: 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. Innovations are a combination of previous good ideas: the comprehensive policy recommendation is to prop up Social Security and implement Guaranteed Retirement Accounts (GRAs). In sum, the problems to solve are not just inadequate retirement assets for many, but an unequal distribution of retirement readiness and access to retirement that results in downward mobility of middle-class workers and poverty and chronic deprivation among the old. Other problems are the ineffective use of tax expenditures and the unintended consequences of lowering the reservation wage of older Americans. The causes of these problems are badly designed retirement plans and policies, not badly-designed humans.

An optimal pension system (Barr and Diamond 2009) embeds key design features of social insurance. A pension system should also help stabilize and grow the economy, which is described in a small section of the chapter before the conclusion.

Accumulation

The GRA aims to strengthen retirement security by increasing accumulation. Low- and moderate-income families are especially helped by mandatory contributions into private asset-based accounts. GRAs apply to all 1099 workers and full-time and part-time workers. Senator Elizabeth Warren (2016) called for all employee benefits and protections to be delinked from employers—this plan does that—although savings and contributions occur at the point of wage and salary payment. The contributions to the GRAs would be 3% of wages, with half paid by employer and half paid by employee. To ease the burden on low-wage earners, all workers would receive a tax credit equal to their annual contribution up to $600 per year so that the after-tax cost to workers earning $40,000 or less would be zero. For high-income workers, the obligation to contribute is capped—the 1.5% 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 are required to offer a defined benefit pension or contribute to a GRA. The proposal assumes that most employers would choose the GRAs because the costs would be lower. The benefit to who provide pensions are not penalized by having to compete with firms that do not. This protection functions all labor regulation—some aspects of pay and protection is taken out of competition.

Accumulation is further enhanced by current tax breaks for 401(k) plans and IRAs repurposed into a retirement tax credit. The plan would be revenue-neutral and deficit-neutral. The costs 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 the new GRAs.

Investment

Investment of the accumulated assets is improved through competition and 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 the GRAs would earn a 6-7% rate of return. In order to reduce workers' risk, the government would guarantee a minimum return of 2%, on average, on the accounts over the long term. The government could charge for this guarantee.

Deaccumulation

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, adding them on to 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 individuals and employers and repurposed tax deductions from federal (and presumably state) governments. Also, annual distributions withheld from affluent retirees would be used to fund annuities topping up accounts of low-wage or part-time workers if need be, offsetting administrative costs of the GRAs and the guarantee.

6. Asset-Based Programs Make Recessions Worse Risk

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. In the Great Recession of 2008–2009, the gap between real gross domestic product (GDP) and potential output fell precipitously in 2009 by

$504 billion. Additionally, because of the decline in household and business spending between December 2007 and December 2009, employment fell by 5.7%—a loss of 8.3 million jobs—and the unemployment rate peaked at 10%.

To counter the recession, the U.S. federal government spent $700 billion for stimulus programs. But, the largest source of recession mitigation—built-in automatic stabilizers—quietly did their thing by injecting 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 simulative effect as the average marginal tax rate shrinks as more people fall into the lower brackets)—all helped mitigate the effects of the downturn.

Nontraditional automatic stabilizers: Social Security's Old-Age and Survivors Insurance; Social Security Disability Insurance (SSDI), and Medicare, and DB and 401(k)'s also had an effect. People use these programs in recessions as income and life-style support and the taxes used to finance those programs reduce spending in expansions. Five government automatic stabilizers—progressive income taxes, UI, OASI, SSDI, and Medicare—reduced the number of jobs lost in 2009 by a low of 81,456 and a high 967,506—the range depends on which marginal propensity to consume is used.

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

Because 401(k) plans work in the opposite, destabilizing direction, 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 because 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—whose values fluctuate with the business cycle—made the last recession deeper and caused slightly more unemployment than would have happened otherwise if 401(k) plans did not exist (Ghilarducci and Saad-Lessler 2015). Annuity-based retirement accounts backed by government programs also 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 individual directed, commercial liquid 401(k) and IRA accounts may boost participation but the investment and distribution aspects of the system is doomed to be ineffective and very expensive and create more inequality. The system relies on tax breaks to encourage participation. The tax breaks are extend to people with the smallest risk of not having enough retirement assets. Although pension systems with automatic enrollment, automatic investing in safe instruments, and auto annuitization depend on most people not opting out in order to preserve a libertarian paternalism philosophy doesn't work because it is still a voluntary system.

The Obama administration spent 8 years trying to implement the Auto-IRA in keeping with a libertarian paternalism philosophy (White House 2015). But like many large problems, the solutions to most our social problems will take real money. We can get real money from progressive taxation—or in the case of comprehensive pension reform—by 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 sector are deficit spenders.

The 401(k) structure is not suited for pensions and the government subsidies are perversely-incented. The problem is not bad human decisions or financial illiteracy. Life events happen to people over their life course that disrupts best-laid plans. The consequences are an unequal distribution of work at older ages; work for old people *can be* bad, choice about retirement is good; employers are using old people as substitutes because old labor is being recommodified, lump sum cause depression, and annuities make old people happy. Asset ownership induces shame, blame the victim narratives, and lack of political will.

A pension system does three simple things to smooth life-course consumption. One, it accumulates sufficient assets over the life course; two, investments those assets well; and three, it distributes the assets in a lifelong stream of income. Ghilarducci and James (2016) Guaranteed Retirement Account plan below satisfies all three functions. Sufficient accumulation is achieved through mandatory participation and banning all leakages before retirement; investments are low fee, pooled and invested to match the long term liabilities; and the payouts are in the form on an annuity.

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ENDNOTES

[i] 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)

[ii] 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.