Readings

Pensions Under Siege

Pensions in a Changing Economy
edited by Richard Burkhauser and Dallas L. Salisbury
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Reviewed by Kathleen Utgoff

Anyone who believes our private pension system faces a crisis should read this volume. A careful reading of these 12 diverse papers reveals considerable cause for optimism, despite some worrisome trends. Pension funds continue to grow, they are better funded, and the percent of older families receiving a pension (now about 50 percent) is expected to grow to more than 90 percent by 2030. Private pensions could relieve some of the pressures on the Social Security system.

One of the worrisome trends that receives a great deal of attention in this volume is a shift away from traditional plans that pay a monthly benefit to asset-accumulation vehicles such as 401(k) plans that pay lump sums. In addition, the proportion of workers covered by a pension appears to be stagnating at about half the workforce, after growing continuously from the end of World War II to the beginning of the 1980s. The projected growth in families receiving pensions is due to the earlier growth in coverage and new rules that require earlier vesting. Of particular concern to some of the authors is the evidence that workers most likely to be left out of the pension system are women, minorities, and low-wage workers.

Not every author shares all those concerns. As the excellent introduction by Richard Burkhauser points out, there are two distinct justifications for the tax breaks that have created our private pension system. According to one school of thought, pension savings should be exempt from the double taxation of our income tax in order to encourage private savings for retirement. Not surprisingly, that view is prevalent among supporters of a consumption tax.

Another view is that the tax breaks that go to pensions should be used as a tool to redistribute income and that pensions for high-wage workers should be available only to the extent that low-wage workers end up with more income in retirement. That view has produced a stream of burdensome pension regulations. The so-called "non-discrimination" rules are just one example. In order to demonstrate that a pension plan does not favor higher income groups, employers must spend billions of dollars a year on complex calculations. Fairness in the availability of benefits is not enough; the outcome must also pass muster. Those rules have become the kudzu of the pension system despite a total absence of any evidence that the required contortions actually benefit low-wage workers.

Given the diversity of authors, including two Chicago economists, the head of the Pension Rights Center (a consumer advocacy group), and a liberal congressional staffer, the wide range of views expressed in this volume is not surprising. It is an excellent sampling of the conflicts that have made our national pension policy so schizophrenic over the years. What is surprising to me is the general agreement that additional restrictions on our pension system would be helpful. Many of the authors appear to support restrictions on the availability of lump-sum pension systems or a requirement that benefits be provided in the form of an annuity. I suspect that those pension experts have concluded that pension tax breaks cannot survive unless

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they clearly lead to improvements in income throughout retirement. If workers withdraw pension accumulations when they change jobs or if they buy a fancy car at the beginning of retirement, the tax breaks could be harder to justify.

That view is misguided. The real source of the worrisome trends that are discussed in this volume is government regulation. Traditional (defined benefit) plans are out of favor, but not because of changes in the economy. They have been made unattractive by a host of new laws and regulations. The tax benefits for traditional plans have been reduced through limits on deductible contributions. It is now more expensive to pay a dollar of benefits through a defined benefit plans than through an asset accumulation (defined contribution) plan. In addition, employers are increasingly prevented from using defined benefit plans to manage quits and retirements because plans that are designed with features such as delayed vesting or reduced accruals for older workers are considered unfair, even when those features are the result of collective bargaining. Small wonder that traditional plans are waning in popularity; they cost more and have fewer advantages to employers. Unfortunately, the end result is that workers are more likely to be covered by a pension plan where they bear investment risk and longevity risk. The employer absorbs those risks in a traditional plan.

The lump-sum trend is also the product of our pension laws. The taxation of a lump sum is more favorable than the taxation of an equivalent annuity. In addition, when a plan offers both options, the government requires the calculation of the lump sum at a below-market rate that "protects" the worker by making lump sums more attractive than the annuity alternative.

Although I think this volume should be retitled *Pensions in a Hostile Regulatory Environment*, the sponsors should not be criticized for the misnomer. The papers and the title accurately reflect the state of current thinking in the pension world. Another important contribution of this volume is that it combines the work of academics and policymakers in a field where interactions between those groups are far too few and far too late. Just one example is the assumption behind many pension regulations that a pension is a gift. Surprisingly, that assumption has not been challenged by economists, even though most are convinced that pensions are paid for by workers through lower wages.

One of the sponsors of this volume, the Employee Benefit Research Institute, has long played a valuable role in Washington by bringing important facts to the policy arena in a timely and unbiased way. But that is not enough. Our national pension policy needs the kind of rational framework that is best produced outside the Beltway, in an academic environment. The most valuable contribution of this volume may be that it begins to fill that need.