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Commentary

BUFFIN PARTNERS INC. ECONOMIC INVESTMENT AND ACTUARIAL RESEARCH

Appeal for a National Retirement Income Policy

The current arrangements for the provision of retirement income in the United States are not expected to be adequate for today's working population. Significant increases in financial resources will be necessary if reasonable standards of living are to be maintained after retirement. The main sources of retirement income are: Social Security; employer-sponsored defined benefit plans; employer-sponsored defined contribution plans; Individual Retirement Accounts; and personal savings and investments. Many individuals spend too much income on current consumption and do not plan ahead to ensure adequate levels of retirement income. Some workers are not covered by an employer-sponsored retirement plan. Longevity, inflation, and investment risks all impact retirement income and need to be properly managed. Social Security provides a basic safety net and a foundation for retirement income; it protects beneficiaries against these types of risk. Employer-sponsored defined benefit plans typically make no provision for inflation protection. There has been a significant decrease in the number of defined benefit plans in recent years as employers terminate or freeze plans and switch to defined contribution arrangements. Employer-sponsored defined contribution plans transfer all longevity, inflation and investment risks to the individual participants. Individual Retirement Accounts may enjoy certain tax advantages, but do not protect the holder from these risks. The adequacy of funding arrangements for defined benefit plans has become controversial as employers seek to reduce their financial obligations for maintaining expected benefits; plans have been terminated with inadequate assets, resulting in the transfer of unfunded obligations to the Pension Benefit Guaranty Corporation (PBGC); this often leads to reductions in participants' expected benefits due to the coverage limits imposed by PBGC regulations. Companies claim that benefit costs, including health care and retirement income, are adversely affecting their competitiveness in global markets; this situation has been used to justify cuts in future benefit promises. Pension fund governance and investment management practices need to be improved; financial turmoil and equity market declines have created significant risks for pension funds; investment strategies have frequently resulted in large losses that necessitate increases in future funding requirements.

A Presidential Commission should be established to investigate and report on the current state of provision for retirement income in the United States. The Commission's mandate would be to develop a National Retirement Income Policy. Its objective would be to correct the deficiencies in the present arrangements and to recommend ways and means to provide adequate retirement income for the US population. The Commission should include members selected from among the nation's leading academic and technical experts, as well as representatives of labor and business. The Commission should be empowered to collect data, authorize research studies, and obtain testimony from expert witnesses. The Commission should study the relevant practices in the United States and other countries, particularly those in the Organization for Economic Cooperation and Development (OECD). The Commission could also benefit from the expertise and global perspective of the International Labour Organization and the World Bank.

Some of the major issues to be examined by the Commission would be: adequacy and shortfalls in existing arrangements; financial resources required to provide adequate old-age income security; affordability of adequate retirement income relative to other national priorities; roles and responsibilities of government, employers, and individuals; assessment of social transfers policy; viability of employer-financed retirement plans; tax treatment of various retirement income sources; rationalization of tax policy; regulatory framework for pension arrangements; strengthening the funding of defined benefit plans; reducing the potential exposure of the PBGC for under-funded pension obligations; expansion of the Social Security system to offset the decline in employer-sponsored defined benefit pension plans; projected solvency and sustainability of Social Security with due consideration of the potential need for future revenue increases; and the government's responsibility for the ongoing timely payment of principal and interest on its holdings of special-issue treasury bonds that are held in the Social Security Trust Fund.

There are many important issues to be addressed in developing a rational, affordable and integrated national retirement income policy. These critical issues require attention from a broad social and economic perspective. Simply reacting to problems with stop-gap measures and tinkering with the tax code and regulations will no longer suffice as a substitute for an acceptable national retirement income policy. A Presidential Commission that succeeds in developing a coherent national retirement income policy with a focus on the social, economic, and demographic challenges will be providing a valuable service to current and future generations. The success of the Commission can be judged by what it achieves by educating the general population on retirement planning issues, influencing the balance between spending and saving, identifying risks, providing the means for protection against these risks, emphasizing the responsibilities of government, employers and individuals, and encouraging greater focus on ways and means for achieving adequate levels of retirement income.

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