A Government Match for Private Pension Saving?

C. Eugene Steuerle

Document date: February 08, 1999
Released online: February 08, 1999

As part of his package of budget and social security proposals, the president has proposed to "spend" about 12 percent of the surplus over the next 15 years to subsidize a new "USA" retirement account. Although given modest attention so far, in point of fact this proposal is by far the largest of any real changes the president has put forward. If one puts aside the accounting transfers from one part of government (Treasury) to others (social security and Medicare), which have no direct real effect on anything other than the government's ledgers, the USA proposal could use up as much as half of the net sum of spending increases and tax cuts put forward by the president.

Like so many retirement proposals today, controversy centers on how USA accounts would be financed. Forget for the moment, however, whether additional private retirement should be subsidized with existing social security taxes, new social security taxes, or, like the president's proposal, with income tax subsidies. Also ignore the lively debate over the meaning of all the accounting transfers suggested by the administration. Instead, focus on what is relatively unique about USA accounts: they would provide a government match for retirement saving. This type of match is not unlike those offered by employers to employees who contribute to their 401(k) and related plans.

The suggestion of a government match as a possible alternative to a mandate was first made, I believe, over two years ago in this column. (See Tax Notes, Dec. 9, 1996, p. 1235 and Dec. 16, 1996, p. 1357.) When I talked over the possibility with various officials in the administration and Congress, the reaction was generally mixed, in no small part because a government match is more complex than the simple notion of a mandate. But simplicity has its costs too. A straightforward mandate generally results in accounts no larger than the size of the mandate itself, as it may not leverage up any additional private retirement saving. It's also easier, even if incorrect, to discuss a mandate only within the context of social security rather than the broader retirement system.

Interestingly enough, up until now the public has not been engaged in any effort to stretch the social security debate into the private pension arena. There have been a few broaches: the National Commission on Retirement Policy, on which I served as a commissioner, made some recommendations along those lines, as have a few others. But they have received very little attention in the midst of the more visible debate between those who talk almost solely of "privatizing" social security and those who talk almost solely of "maintaining" the current system. Clearly, however, it is not much of step to consider the president's USA account proposal—and, in truth, many other proposals for the establishment of mandated individual retirement accounts—much more broadly as a first step toward redefining the private pension universe.

Were it not for the larger social security issue hanging over the budget, integration of a well-developed USA account proposal into private pensions might easily stand on its own merits. The difficulty is that in a world where the government is already on a path to increase its spending on retirement and health from around 40 percent to around 80 percent of expected revenues, it is hard to believe that new subsidies are the only things that are needed. Another difficulty is that almost every Congress for the past 30 years has tried to patch on yet more saving or retirement incentives, so that the system as a whole is already messy and very inefficient at the objective of increasing retirement saving. Dodging these larger issues of integration into the existing universe of public and private plans weakens the proposal.

The discussion so far, however, reflects policy rather than political analysis. The president's budget plan was also developed to meet a number of political objectives. After promising last year to tackle social security at the beginning of this year, the president had to say something in his State of the Union address. By the time work began on that address, no real plan had been developed, and the elaborate estimation and analysis required to put together a complete package—as well as to see how the parts interrelated—was simply not possible. Meanwhile, the administration feared that Congress and the Republican opposition, in particular, were starting to set their own priorities for the use of the surplus, especially for tax cuts.

Accounting transfers were proposed to suggest that something was being done about social security. Whatever their merit, they did give the administration an excuse for limiting the amount of unified budget surplus that could be spent.

But our focus here is on the USA accounts. They fit into the picture in three different ways. First, they are at least a partial gesture to those in Congress who are trying to increase saving as a way of dealing with upcoming retirement needs. Second, by using general revenues rather than social security taxes, they appeal to those who really don't want to reduce any promised benefit in social security or use existing social security taxes to subsidize private saving. Third, the administration recognizes that there very likely will be a tax bill this year. The USA accounts give it some chits to play in that game.

Whatever the Republicans might suggest in the way of tax cuts, the president can now fight on two fronts. First, he can say he wants less of a cut in order to save more of the surplus for social security. Or, to the extent there is a tax cut, he will argue that a large proportion should go to meet future retirement needs through USA accounts.

This strategy does not go very far toward meeting the long-term problems of our retirement and health systems, unless Congress wants to make the hard choices that the administration has avoided. Even the logical cutbacks in other promised government benefits equal to the size of the new USA subsidy are left to Congress to propose.

The president's proposal is also confusing because of the subtle way it blends policy, politics, and accounting systems. But give it credit on one count: it is likely to deter Congress from reducing the projected surplus by much—which seems to be its primary purpose. Unfortunately, at least as it now stands, it also deters Congress from enacting significant reform as well. Indeed, failure to enact anything would save even more of the surplus than the president's proposal itself. That could be unfortunate for those who see USA accounts and individual retirement accounts as reflecting a bipartisan desire to try to expand private pension wealth throughout the income distribution.

The president's proposal for a match is one way to try to encourage greater saving, especially among the middle class. To be effective, however, requires a much more delicate crafting of legislation that simultaneously tries to address the excessive promises of social security along with the inadequacies of the existing private pension system. It's not an easy task, but neither is it one that should be neglected.

Other Publications by the Authors

- C. Eugene Steuerle