Congress Should Encourage Workers to Save for Retirement

Proposals to Reduce Incentives Would Hurt Workers With Modest Incomes

- ***The National Commission on Fiscal Responsibility and Reform has recommended reducing the amount that workers can save for retirement.*** The commission suggested limiting contributions to 401(k) plans to the lesser of $20,000 or 20% of income (known as the "20/20 plan").

- ***The Commission's proposal would significantly reduce the creation of new retirement plans.*** Many small businesses do not sponsor retirement plans because they believe that a retirement savings plan will be expensive and the small business owner is too busy with other matters to investigate low cost options. A reduction in the contribution limits as suggested by the Commission will further discourage the creation of new plans by employers as it reduces the amount that can be saved in the plan for retirement.

- ***The proposal would adversely affect the ability of workers to save.*** Life events impact the ability of workers to save uniformly throughout their careers. For example, individuals are often not able to save as much for retirement when they have increased expenses related to caring for small children or elderly parents, paying for college tuition, and unexpectedly home or health care expenses. Under the 20/20 plan, workers wouldn't have the flexibility to save more in the years when they are able to compensate for their more fiscally challenging years.

- ***An analysis by the Employee Benefit Research Institute (EBRI) shows that these reduced limits would result in lower account balances at retirement for all income groups.*** For example, the data shows that the 20/20 plan would result in workers age 36-45 in the lowest income quartile having an expected reduction in account balances at Social Security normal retirement age of over 10% if this proposal became law.

401(k) Plans Are Effective at Helping Workers at All Income Levels Save for Retirement

- ***401(k) plans are primarily a middle class benefit.*** Seventy-eight percent of all full time workers have access to a workplace retirement plan, with 84% of those workers participating. For private-sector workers, 73% of full time workers have access and 80% of those participate. Given these high rates of participation, it's no surprise that the overwhelming majority of participants are far from wealthy. In fact, almost 75% of participants in 401(k) and profit sharing plans make less than $100,000 per year. Thirty-eight percent make less than $50,000.

- ***401(k) and similar plans have been remarkably successful at getting workers to save for retirement.*** In fact, the primary factor in determining whether or not a worker is saving for retirement is whether or not they have a retirement plan at work. Data prepared by the EBRI shows that over 70% of workers earning from $30,000 to $50,000 participated in employer-sponsored plans when a plan was available, whereas less than 5% of those without an employer plan contributed to an IRA.

- ***401(k) tax incentives are more progressive than current marginal income tax rates.*** Another unique feature of the retirement savings tax incentives is the non-discrimination rules that encourage employers to contribute on behalf of non-highly paid employees, and limit the amount of pay that can be counted toward benefits. As a result, the current tax incentive for employer-sponsored defined contribution plans is more progressive than the current income tax system. Based on an analysis by a former JCT economist, taxpayers making less than $50,000 pay only 8% of income taxes, but receive 30% of the tax incentives for defined contribution plans. Households making less than $100,000 pay 26% of income taxes, but get over 60% of the benefit of this tax incentive.