
DC Plans and Deficit Reduction

By David Wray *Thu, Jun 16, 2011*

"A big bulls-eye has been painted on the employer-sponsored defined contribution system," writes the president of the Profit Sharing Council of America.

Currently one-third of Federal spending is financed by new borrowing. This is unsustainable. However, with the two parties locked in mortal combat in preparation for the 2012 election it is likely that the changes made as part of the debt limit extension in August will be only a down payment.

More will have to be done in 2013 and our political leaders will have to cut more spending and raise revenue. Due to the unpopularity of raising tax rates this means eliminating or reducing the tax breaks and deductions that are termed "tax expenditures."

According to the Joint Committee on Taxation these tax expenditures reduce Federal revenue by \$1.1 trillion annually. The favorable tax treatment of contributions to retirement savings plans accounts for about 10% of this and is among the biggest of these expenditures.

In a June 8 appearance before The Economic Club of Washington, D.C., Sen. Mark Warner, D-Va., said that the so-called Group of Six, a group of senators trying to convert last year's presidential deficit commission recommendations into legislation, is embracing the deficit commission's idea of eliminating or reducing these tax expenditures, nearly all of which are popular with the public.

The Debt Commission proposed two scenarios which affect DC plans. One would reduce the combined DC contribution limit to \$20,000 or 20%, whichever is less. The other would eliminate it altogether. A big bulls-eye has been painted on the employer-sponsored defined contribution system.

The 2013 tax debate will be a barroom brawl with supporters of each tax preference engaged in a no holds barred effort to preserve as much of their program as possible. Mix in consideration of the tax rate for of capital gains, dividends and corporations and you may have a situation where virtually everyone will be willing to throw the employer-sponsored defined contribution system under the bus.

It gets worse. Many see this situation as an opportunity to replace the current system with one run by the government and if that doesn't fly they will propose changes that would alter the current system significantly.

For example, some would replace the current tax deferral with a refundable tax credit. And at the other end of the political spectrum some advocates see any tax preference as a social manipulation preferring no tax preferences whatsoever, including those for retirement savings.

If we are going to preserve the current system in anything resembling its current form with anything close to its current contribution limits, we must begin preparing now. Check back for more information on this subject coming soon.