Don’t Cut Pensions, Expand Them

By Teresa Ghilarducci Thu, Mar 22, 2012

This economist at the New School argues that, rather than curtailing public and private pensions, New York and other states could save millions of workers from impending poverty by creating public pensions for everyone.

On March 15, the New York State Legislature agreed to a deal limiting pensions for future public employees. The state thus joins 43 others that have recently enacted legislation curtailing public retirement benefits.

Though New York needs to reduce its spending, the cuts come at a particularly bad time: over a third of New York workers, both public and private, approaching retirement age have have less than $10,000 in liquid assets. As a result, those workers are projected to be poor or near poor in retirement, with an average budget of about $7 a day for food and approximately $600 a month for housing.

Fortunately, there’s an easy solution. Rather than curtailing public and private pensions, New York and other states could save millions of workers from impending poverty by creating public pensions for everyone.

While the recession bears some blame for the looming retirement crisis, experts agree that the primary cause is more fundamental: Most workers do not have retirement accounts at work. Over half of the workers in New York State, more than four million people in 2010, do not participate in retirement plans with their current employers, while over half of American workers do not have pension plans at work.

Private-sector pensions have been on the retreat for decades. In fact, in the late 1970s and early ’80s, Congress, worried about the dismal rate of pension coverage, tried to remedy the situation by extending 401(k) plans, originally designed for executives, to everyone, while also passing a law to create individual retirement accounts.

The problem is that these steps set up incentives through the tax code, which means that the biggest benefits go to the highest earners — people who, moreover, would probably have saved anyway. Today 79 percent of such tax breaks go to the top 20 percent of workers.

Meanwhile, despite extensive commercial advertising for retirement planning, coverage for ordinary people stalled. And even many of those who do save for retirement fail to consistently put away the 5 to 10 percent of their pay necessary to adequately supplement their Social Security benefits.

In response, in late February California State Senator Kevin De León and Darrell Steinberg, the Senate president pro tempore, introduced legislation that would allow private-sector workers in California to enroll in a modest, state-operated retirement program financed by the workers and their employers — at virtually no cost to taxpayers.

This would increase coverage because employers would put every worker into a plan, either their own or the California plan. In the California version workers could opt out; some will, but most workers once in a plan will stay in.

Also in February, John Liu, the New York City comptroller, called for a similar plan for New York City residents. His program would pool employee and employer contributions into a professionally managed, citywide retirement fund.

Both plans would use the same professional staff and institutional money managers that invest the state and city pension funds to manage contributions made by participating employers and employees in the private sector.

This is a vital step: public pension plans usually outperform 401(k) plans and individual retirement accounts, because instead of a single worker managing a single account, large institutional plans pool workers of all ages, diversify the portfolio over longer time periods, use the best professional managers that aren't available for retail accounts and have the bargaining power to lower fees and prioritize long-term investment.

By some estimates, costs for public pensions are over 45 percent lower than for individual 401(k) plans. Of course, since these plans would be financed by workers and their employers, there would be no cost to taxpayers.

Saving for retirement is never easy. But finding a safe place to put your money these days is even harder. Opening up public pension options to everyone is a cheap, simple way to help.

Teresa Ghilarducci, a professor of economics at the New School, is the author of When I'm Sixty-Four: The Plot Against Pensions and the Plan to Save Them (*Princeton University Press, 2008).*