Reality Testing for Pension Reform

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Abstract

The US private pension system is at a crossroads. Its future direction is now under intense scrutiny by Congress, which has recently considered two very different proposals for change, each containing elements likely to be on the national agenda for some time. One approach embodies a traditional approach to pension reform, with an omnibus statute that tinkers with almost every aspect of the private pension system to make incremental changes. A second seeks to bring radical change and simplification, with sweeping consolidation of the number and types of defined contribution plans. This chapter evaluates these two approaches, one for incremental change, the other for structural reform, and then considers an alternative. Our analysis focuses on the nuts-and-bolts of the private pension system, the plans that comprise it, and the rules that govern them that have accumulated over the past 60 years. Our thesis is that an analysis of the architecture and machinery of the private pension system can teach us a great deal about how to redesign the private pension system to meet retirement income challenges to come.

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> I'm staring at documents that make no sense to me, no matter how many beers I drink ... Apparently I have until Sept. 30 (in most instances) ... to comply with something (but what?) called "GUST" ... [for my Keogh plan and I] ... must adopt EGTRRA prior to the end of the plan year beginning in 2002. I am, frankly, reluctant to adopt anything called "EGTRRA," which sounds like the name of a giant radioactive chicken that destroys Tokyo ... the federal Tax Code is out of control ... It's gigantic and insanely complex, and it gets worse all the time. Nobody has ever read the whole thing. IRS workers are afraid to go into the same ROOM with it. They keep it locked in the baseme nt, and once a day, they open the door, heave in a live taxpayer - some poor slob who failed to adopt EGTRRA in time to comply with GUST (and various other amendments) - then slam the door shut, before the screams start (Barry, 2003).

As humorist Dave Barry has pointed out, the US private pension system *is* fair game for jokes and ridicule. It is absurdly complicated and incomprehensible. Relevant tax rules and regulations include more than 3,000 pages of small, single-spaced, text and weigh more than most laptop computers. The companion labor rules under ERISA, the Employee Retirement Income Security Act of 1974, are smaller, but not by much. There is widespread agreement that the present situation is untenable and something must be done. There is also widespread recognition that the aging of the baby boom generation will place the U.S. private pension system under unprecedented pressure and that a comprehensive review of pension policy is long overdue (Mulvey and Nyce, this volume). As Klein (this volume) notes, reinventing the retirement paradigm requires examining whether the current U.S. private pension system can meet the retirement income challenges to come.

Analyses of the U.S. private pension system typically focus on such issues as how to improve coverage or encourage saving or prevent tax abuse or generate retirement income more equitably. Those issues are important, but this chapter takes the position that reinventing the retirement paradigm will require more fundamental analysis. A critical step in the analysis is to step back and examine closely the architecture of the private pension system today. The thesis of this chapter is that the structure and machinery of the private pension system, that is, the accumulation of plan types and rules over the past 60 years, have much to teach us about directions for reform. Accordingly we focus on the nuts-and-bolts of the private pension system, the plans that comprise it and the rules that govern them.

This is an opportune time for such an analysis. For perhaps the first time, there are two very different types of proposals for change before Congress. The first is reflected in the Pension Preservation and Savings Expansion Act introduced in 2003 by Representatives Portman and Cardin (Portman and Cardin, 2003a, 2003b). PPSEA is the "traditional" type of pension reform, an omnibus bill that tinkers with almost every aspect of the private pension system to make incremental changes. The second proposal is the attempt of the Administration to effect radical change and simplification in the structure of the private pension system. The 2003 proposal, modified in budget submissions in 2004, contemplates a sweeping consolidation in the number and types of defined contribution plans (Purcell, 2003; U.S. Department of the Treasury, 2004). This chapter evaluates these two approaches to change, the first one for incremental change, and the second one involving greater structural reform, and then it considers an alternative.

The Current Structure of the US Pension System

As a starting point, it is helpful to take an overview look at the current structure of the private pension system in the United States. Most people understand that the system is composed of defined benefit and defined contribution plans, but few are aware that, legally speaking, there can be as much diversity within these types of plans as between them. Figure 1 illustrates the extraordinary constellation of plans that will be available when all changes brought about by EGTTRA (Economic Growth and Tax Relief Reconciliation Act of 2001), the most recent major pension reform law, have become fully operational in 2006 (see Glossary for terminology).

Figure 1 here

The US private pension system evolved into its current complicated structure as the result of two primary factors. First, it is a tax-based system that provides tax incentives to promote saving for retirement. Second, it is a voluntary employer-based system: employers are encouraged, but not required, to provide plans for their employees. In this framework, different types of employers are subject to different tax rules. For example, for-profit and non-for-profit employers are subject to completely different sections of the federal tax code, while governmental employers are largely exempt from such rules. The theory has been that, if pension plans are to be sponsored by different types of employers, those plans should be subject to as many different rules as are necessary and appropriate for those employers. This emphasis on the tax attributes of employers largely explains the historical evolution of the private pension system. It began in the 1920s with special tax rules for plans sponsored by corporate employers. Some 20 years later, new types of plans for not-for-profit employers were created. Next, special plans for self-employed individuals were developed, and then rules were imposed on plans for governmental employers. With the passage of ERISA, individual retirement accounts or IRAs were created, almost as an after-thought, to give workers without an employer-sponsored plan a limited opportunity to save for retirement. Finally, special SIMPLE plans have recently been created in hopes of attracting small employers to the private pension system. These are defined contribution plans with safe harbor provisions designed to reduce the regulatory requirements of sponsoring a plan to a minimum.

The historical evolution of the private pension system is reflected in the post-EGTTRA arrangement of plan types composed of three primary families of plans. The largest group consists of qualified defined benefit and defined contribution plans subject to IRC § 401(a) that are subject to the full panoply of tax and ERISA rules. Although these plans were originally developed for corporate employers, now, with a few exceptions, any employer can sponsor these types of plans. The second group consists of tax sheltered annuities that must satisfy IRC § 403(b). These plans continue to be limited to non-profit employers and public educational institutions. As might be expected, these plans are subject to much less regulation than their 401(a) counterparts. The third group consists of IRA-based plans under IRC § 408. Although IRAs were originally intended to be substitute savings plans for individuals without an employer-sponsored plan, employers can now offer group plans using these accounts. These plans are designed to minimize the regulatory burden on employers. Finally, there is a small, special category of plans available largely to governmental employers under IRC § 457(b).

Although each family of plans has its own specific rules, there has been some convergence over time. For example, most of the special rules for plans available to the self-employed have been repealed, and IRA-based plans are now available to employers as well as employees. In addition, some of the rigid barriers between plan families have been relaxed. Both non-profit and corporate employers may sponsor 401(k) plans although governmental employers may not. This convergence, however, has not resulted in much simplification because, in most respects, the plan families retain their historical structures and traditional rules. As the pension system evolves, special rules and exceptions are created when the traditional rules do not fit a new situation. Over time, this process has produced a vast and complex array of rules that are increasingly difficult to navigate, even by the most experienced legal practitioner. These rules, which are illustrated in Table 1, include the EGTTRA changes that became effective in 2004.

Table 1 here.

As the US private pension system has grown more complex, both employers and workers find it more difficult and more expensive to navigate. For example, it is often not readily apparent in any given situation which plan might be the "best" alternative among those available. Numerous consultants and other pension professionals assist in the plan selection and design process, but their services inevitably increase the cost of plan sponsorship and membership. Moreover, as rules grow more complicated, the administrative burden on plan sponsors whose plans must satisfy all relevant rules or lose their tax benefits also increases. The private pension system now includes a plan compliance industry, composed of lawyers, consultants, actuaries, accountants and other pension professionals, dedicated to mastering and implementing plan rules. Their services are often critical to insure that plans satisfy the law, but their costs, which can be significant, must be borne by the employer as an additional business expense or charged to plan participants where they reduce the return to savings.

To be fair, it must be acknowledged that EGTTRA has resulted in some long overdue and welcome changes. For example, it rationalized the contribution limits on most employee savings plans today, 401(k), 403(b) and 457(b) plans, and the employer deduction limits on most plan types. It also eliminated some anomalies, such as the exclusion allowance for 403(b) arrangements and the coordinated contribution limit for 457(b) plans. It will result in one less plan type to worry about; by increasing the deduction limits for profit-sharing plans to those of money purchase plans; the latter (which are slightly less flexible) will become extinct. But, of course, most plan types continue to operate and the private pension system must now absorb and digest the changes EGTTRA has made in pension law.

The type of reform represented by EGTTRA and its predecessors have generally left the private pension system with more rules, not fewer; more plan types, not fewer; and more choices, even though many are not meaningful or worthwhile if and when understood. Only in a very few cases, such as the repeal of special contribution limits for 403(b) arrangements, did some rules actually disappear. In most cases, new rules are just placed on top of old rules, and new regulations must be written to harmonize and integrate them with existing law. Moreover, the private pension system has not yet felt the full brunt of EGTTRA. Rules permitting IRA contributions to employer-based plans recently became effective, and in 2006, some plans will be allowed to provide eternal tax forgiveness of future returns as long as no up-front deduction is taken, essentially by permitting the Roth-type contributions available already for Roth IRAs.

Given this background, not all of EGTTRA's changes are as benign as they might first appear. Allowing IRA contributions to be made to employer-based plans (thereby letting employees make these contributions directly to their employer's plan rather than to a separately-maintained IRA) might be viewed as a good idea. Dodging the budgetary implications of back-loading the cost of tax preferences to future years, allowing Roth-type contributions to employee savings plans (e.g., Roth 401(k)'s in 2006) might also be viewed as worthwhile in isolation as a pension policy. From a legal perspective, however, these additions compound the complexity now found in the private pension system. IRA contributions to qualified plans ("deemed IRAs") bring with them their special rules that will be added to plans already overwhelmed with their own rules. A plan that fails to observe the IRA rules will jeopardize the tax-qualified status of the entire plan while a plan that violates tax-qualification requirements will cost its IRAs their tax benefits too.[1] Roth-contributions too make employer-plans more complicated. Employees have traditionally made contributions on a pre-tax basis through which contributions (and their earnings) are taxed only when distributed from the plan or on an after-tax basis in which contributions are made from already-taxed income and only earnings are taxed when distributed. Roth-contributions are based on a completely different tax system in which contributions are made from after-tax income but are completely exempt from taxation thereafter. Adding Roth-contributions therefore means layering a third tax system on top of the traditional pre-tax and after-tax regimes. Employers will have to observe all the separate vesting rules, separate distribution rules, and separate record keeping, tax reporting and accounting requirements that apply to these different types of contributions and tax regimes in their plans. The ultimate effect of even the best-intentioned changes brought about by EGTTRA is more, not less, legal complexity in the private pension system and more, not less, of a compliance burden for employers.

Maintaining the Status Quo: The Pension Preservation and Savings Expansion Act of 2003

According to its sponsors, the Pension Preservation and Savings Expansion Act of 2003, or PPSEA, makes “the next generation of improvements to our nation’s savings and pension systems” by providing “a number of important new savings tools,” strengthening and expanding the employer-sponsored retirement system, offering “new protections to participants” and “assisting retirees in managing and preserving retirement assets and income”(Portman and Cardin, 2003a). It is a massive bill, with more than 200 pages and 16 lengthy sections of highly-technical changes to employee benefits law.[2]

PPSEA follows in the footsteps of EGTTRA and was crafted as a follow-on bill by EGTTRA's primary drafters, U.S. Representatives Rob Portman of Ohio and Benjamin Cardin of Maryland. Its initial thrust was to accelerate and make permanent the changes in EGTTRA that would have expired in 2010 unless extended by Congress. Its immediate effect would be to increase the amounts individuals could contribute to 401k-type plans and IRAs. The bill then winds its way through almost every aspect of the private pension system, proposing changes, additions, and deletions to current rules along the way. If PPSEA were to be enacted, major legal rules throughout the pension system will be changed. These include rules on when employees are vested in plan benefits, when plans become tax-qualified, how defined benefit formulas can calculate pension, and when employees must begin receiving benefits.

In addition to rule changes, there are, as always, changes to plan types. This time, the focus is on the SIMPLE plans created in 1996 that were based on plan designs intended to minimize the regulatory burden of sponsoring a plan for small employers. When SIMPLE plans were enacted, employers were no longer permitted to create new SARSEPs, plans that could be restricted to employee, 401(k)-type contributions. SIMPLE plans required employers instead to make at least a minimal plan contribution in exchange for fewer rules and less liability. PPSEA proposes to weaken the effect of these reforms by bringing back SARSEP-type plans and permitting a smaller employer contribution. Employers would have more choices but the design of SIMPLE plans would become more complicated and, in the end, not very different from their traditional counterparts.

No one of these changes, standing alone, is particularly problematic, and many are in fact improvements in current rules. But perhaps this is not the appropriate standard for evaluating PPSEA. The important question is not whether it does some good for some people, but rather whether it helps move the private pension system toward the systematic improvement it needs to meet the retirement income challenges to come and whether it makes the best use of the resources that are spent. A more general question is why the private pension system seems to need major reconstructive surgery every year or so. After every extensive legal revision, it usually takes about five years before the necessary regulatory guidance to implement the new rules is available. Too frequent changes leave plans in legal limbo and the system in regulatory gridlock.

PPSEA tinkers with many current rules and adds new ones but does little to change the basic architecture of the private pension system. For example, there will still be eight different ways for employees to save their own money, depending on what type of employer they have and the plan it chooses to sponsor, if any: a 401(k) plan for corporate and non-profit employers, a 403(b) arrangement for non-profit and public employers, a 457(b) plan for non-profit and public employers, a SIMPLE plan based on a 401(k) model, a SIMPLE plan based on an IRA, a traditional IRA, a Roth IRA, or a SARSEP. For employers, distinguishing 401(k) plans from 403(b) arrangements from 457(b) plans from SIMPLE plans will be difficult, because they will outwardly look so much alike. Employees, too, often find the intricate rules for saving perplexing. When navigating the private pension system, employers and employees are confronted with choices that appear similar but can have very different legal consequences, and this, as lawyers often say, can and will be a trap for the unwary.

EGTTRA and PPSEA exemplify the customary approach to reform in the US private pension system. For the most part, they maintain the status quo and preserve the historically-distinct plan types based on employer tax attributes and their rules. At the same time, they create new plan types and tax regimes that do not fit neatly into the traditional structure. Over time, the traditional structure makes less sense and becomes less capable of supporting such changes; systemic reform is warranted but never achieved. Instead, plan types continue to be haphazardly combined, and their rules are layered on top of each other, along with the many special rules and exceptions and transition rules and historical legal quirks required to maintain the legal integrity of the system. The consequence is an all too complex and intricate private pension system.

One consequence of this approach is too frequent mutations of pension law that increase the compliance burden of employers as well as the costs of sponsoring a plan. On the positive side, it may provide employers and employees with more choices. Then again, while more choice is usually good, too many unnecessary choices may not be desirable especially if, over time, they are not sustainable. For example, adding Roth-contributions will increase the complexity and cost of plan administration for employers and be a likely source of confusion for employees (Vanguard Center for Retirement Research, 2001). Not only do Roth-contributions require employees to project future earnings, tax rates, and statutory changes to tax law when deciding about contributing, but the tax consequences of their choice will determine pension and budget policy in part for decades to come. There is no guarantee, moreover, that Roth-contributions will always have the favorable tax treatment they now enjoy. Employees, even assuming they can make a perfectly rational choice between the alternative tax regimes, may find that new tax laws (e.g., higher rates, lower rates, adoption of a consumption tax) means that the government reneged on what it once offered. It is one thing to change the law; it is another to give people choices, and then change the rules under which those past choices were made. And when eligibility for future Medicare, Medicaid, and other income-related benefits are determined, "income" from Roth IRAs and 401(k)s probably will be counted, meaning that employees will have to maintain little mini-accounting systems just for Roth-contributions, even though they do not need to be reported for income tax purposes.

Ultimately, the question arises: who really benefits from PPSEA and the type of change it represents? It certainly means more work for the lawyers, actuaries, consultants, and accountants in the plan compliance industry. New regulations must be drafted, plans must be re-written and re-qualified, and administrative procedures must be re-programmed. PPSEA also means more assets of higher-income individuals will need to flow through an extra layer of retirement plan management, thus increasing the fees paid to financial services, mutual fund, and insurance companies relative to other saving. It means that wealthier Americans can get more tax benefits from savings plans sooner because of higher contribution limits and liberalized withdrawal rules. Further, there are many special rules and provisions for almost every large group with an interest in pensions. But it is difficult to argue that it does much constructive for the ordinary pension consumer – the not-so-large employer and the not-so-wealthy employee – from whom the higher costs of management attributable to the added complexity will take a much larger share of savings. For many of them, net rates of return will likely decline. Neither have its economic benefits been demonstrated; there is no evidence (and no one has attempted to estimate) that PPSEA would result in any increase in the percent of low- and middle-income workers who reach retirement with perhaps more than $100,000 in assets.

An Alternative Direction for Private Pensions? Simplified Savings Accounts

In 2003, the Bush Administration stunned the employee benefits community by proposing a radical pruning of employer-sponsored savings plans. It advocated replacing the panoply of 401(k) plans, 457(b) plans, SIMPLE 401(k) plans, 403(b) arrangements, SEPs and

SIMPLE IRAs with a new, standard plan type called *Employer Retirement Savings Account* or ERSA. Although ERSAs look similar to today's 401(k) plan, contributions would not be made from pre-tax income. Instead, all contributions would be Roth-contributions, made from after-tax income and exempt from taxation thereafter. Traditional and Roth IRAs would also be combined into a type of plan called a Retirement Savings Account or RSAs, modeled on today's Roth IRAs, would replace individual IRAs, and a new savings arrangement called a Lifetime Savings Account or LSAs would be created for general purpose saving.[3] LSAs are also modeled on Roth IRAs, but would have fewer rules and restrictions than either ERSAs or RSAs. In 2004, the proposal was expanded to include a fourth type of savings plan, individual development accounts or IDAs, intended for low-income workers.

The Administration's proposals were widely criticized; many felt that RSAs and LSAs were too generous to higher-income taxpayers who could arbitrage the tax system and generate tax saving with little or no increase in personal saving (Steuerle, 2003). Others felt that these would destabilize the private pension system, because employers, particularly small business owners, would trade in their broad-based plans for personal RSAs and LSAs for themselves and their families. Some suggested that employees also might abandon their employer-based plans and worried that (Profit-Sharing/401k Council of America, 2003):

> Some moderate and lower income employees will make smaller, or no, contributions to LSAs and RSAs than they and their employers would have made to their qualified plans. Many employees will redirect their retirement savings to LSAs and use their accumulations for non-retirement purposes. To the extent that some employers continue to offer 401(k) plans, it may be more difficult for these plans to pass the nondiscrimination tests, even as changed in the proposal. Many

employees offered a 401(k) will choose instead to save in LSAs, where they will have immediate and unrestricted access to their savings.

The plan compliance industry was distressed that it had not been consulted and the proposals were developed without their knowledge or cooperation. As a result, the proposals failed to find supporters or receive serious consideration.

Yet the following year, ERSAs, RSAs, and LSAs again returned to the policy arena, and this time, the Administration actively worked with the plan compliance industry. The most recent proposals retained some of the beneficial simplification features of the 2003 design but there were also some significant differences. Table 2 illustrates the major design features of each plan as currently proposed and indicates important rule changes from the 2003 proposals.

Table 2 here

One change was that RSAs and LSAs were made modestly less attractive by reducing annual contribution limits by one-third, from $7,500 to $5,000 annually. Otherwise, the accounts were little changed: RSAs and LSAs are still essentially Roth-IRAs, funded with after-tax contributions and largely exempt from tax thereafter. In an effort to provide a balance for RSAs and LSAs that would benefit those at the high end of the income scale, the Administration added something for those at the low end – an expansion of the still-experimental individual development accounts known as IDAs (Individual Development Accounts). Low-income savers could contribute to an IDA and receive a 100 percent match of up to $500 annually. Matching contributions would come indirectly from the government through private financial institutions (not employers) that would receive a 100 percent tax credit in return for providing the match initially. Account assets would be available to pay for higher education, first-time home purchases, and small business capitalization.

ERSAs too were changed in the 2004 round. Figure 2 illustrates how ERSAs would reduce the current hodgepodge of savings plans - the 401(k) plans, the 403(b) arrangements, the 457(b) plans, the SIMPLE IRAs, the SARSEPs and the SIMPLE 401(k)s - that now clutter the private pension system, to a single, standard plan. All 401(k) plans would become ERSAs, and all other plans could become ERSAs; those that did not would be frozen as of 2005. ERSAs could also include RSAs, subject to RSA rules.

Figure 2 here

This new direction proposed for the US private pension system, based on simplified savings accounts, has some significant merits that have largely been lost in the controversy over RSAs and LSAs. First, ERSAs would help rationalize and modernize the private pension system by eliminating some archaic, duplicate plan types. Second, they would simplify and standardize further the rules for employee saving and thereby reduce the burden and costs of plan administration. Nevertheless, although a single plan for employee saving makes sense, the new proposal does not go as far as it could from a design perspective. It preserves the anachronism that some separate rules are required for different type of employers, even though ERSAs are primarily designed for employee saving. There are drawbacks from a tax perspective as well, notably the Roth-style accounts. They push all costs into the future, often for decades; they add significant complication for both planning and administration when withdrawals from traditional defined benefit plans receive more traditional tax treatment; they disfavor middle-income employees who are likely to retire and move into lower tax brackets (for whom the traditional tax treatment is better); and, as noted above, other government programs are inevitably going to require income accounting for supposedly-nontaxable Roth-contribution income anyway.

In addition, while the 2004 ERSAs look much like the 2003 version, they lack many of the features with the most promise for simplifying pension law. Most plans currently must perform complicated tests against the non-discrimination rules, to prove that they are not providing high-paid employees with excessive benefits. Last year's proposal greatly simplified those rules by providing standard definitions of key concepts and less-complicated testing procedures. It minimized the special non-discrimination rules that 401(k) plans must pass every year to maintain a balance between contributions by high-paid and low-paid employees. It also dispensed with the top-heavy rules that come into play when plan benefits favor company owners and executives and the procedures employers can now use to shift a higher proportion of plan benefits to the high-paid such as Social Security integration and cross-testing.

The 2003 proposal promised to take the US pension system in a new direction. Through a radical pruning of plan types and their anachronistic rules, it seemed to herald a turning point in design that would reduce the administrative burden on employers and the cost of sponsoring plans. The 2004 proposal had a more limited vision. For example, the 2003 proposal retained the current non-discrimination standard that qualified plans could not be designed or operated to favor high-paid employees but suggested simplified tests for measuring discrimination. The simplification it proposed seemed even-handed for both low- and high-paid employees. Each won and lost a little relative to the current rules but, on balance, neither seemed particularly disadvantaged by the proposed changes. By contrast, the 2004 proposal kept alive today's version of the non-discrimination rules, that massive tangle of pseudo-mathematical rules, regulations, testing procedures, and special exceptions, that most qualified plans must satisfy every year. By doing so, it retained such rules as Social Security integration and cross-testing that enable employers to shift more contributions and benefits to high-paid employees. At the same time, ERSAs in 2004 offered nothing new for low-paid employees but were likely to enable high-paid employees to contribute even more than they could under current law.

Sketching A Compromise

Although it did not pass in 2003, PPSEA seems more destined for legislative passage, since it represents a traditional approach to reform and is therefore less controversial as it makes no fundamental change to the *status quo*. Moreover, almost every special interest group in the retirement benefit field has a desired provision in it, and the muscle of employee benefits and financial service trade associations is behind it. Budgetary constraints, however, may prevent or slow its passage. PPSEA, like EGTTRA, was designed in the unique 1997-2003 budget period, where almost every major tax or expenditure bill included give-aways but little or no attention was paid to financing the changes.

At the same time, however, the Bush Administration's ERSA/RSA/LSA type of proposal has a support base. Although its design was initially viewed as too radical, the 2004 changes brought the plan closer to the mainstream and increased its appeal, though this may have eroded its potential for real change. In reality, the Administration's proposal was never as radical as it first appeared, but the new changes made it even less so. For example, the design of ERSAs seemed appealing for its simplicity, but it could have been improved without adding too much complexity. The 2004 changes not only failed to simplify coverage and non-discrimination standards that keep low-paid workers from being left behind or left out, they generally were in the opposite direction.

The 2004 proposal also retained several other design flaws. For example, the Administration proposed to create different ERSAs for different types of employers. Keeping special rules for tax-exempt and governmental employers is an anachronism; the tax attributes of employers have no relevance for plans designed for employee savings, especially now that employee-funded plans are the primary, and often the only, source of retirement income for millions of workers. An employee who works for a corporation should have the same opportunity to save as an employee at a state government. A high-paid employee of a tax-exempt hospital should have no greater or lesser chance to save than a corporate employee with the same income. A related issue was the failure to design ERSAs with more incentives for savings by low-paid employees. Today's 401(k) plans, for example, have special provisions designed to increase retirement saving by low-paid employees that seem to have succeeded, so there is a argument for applying them to plans of tax-exempt and state government employers too. Another crucial reform to the ERSA proposal is to eliminate all opportunities for Roth-like contributions. As noted, they represent substantial complexity in figuring out what type of account to open, they are all back-loaded in costs and represent poor budget policy, and they add to complexity, with only one piece of that complexity related to the potential for conversions over time.

In Figure 3 we present a compromise proposal for revising ERSAs, one we first broached when ERISA turned 25. At that time it did not seem feasible in the near term, but, thanks to EGTRRA and the Administration's proposal, it no longer seems out of the realm of possibility. Like the Administration's proposal, it calls for a single, simple defined contribution plan for employee saving, to replace the many varieties available today. It also calls for uniform contribution and deduction limits and rules on portability that have largely been achieved - thanks to EGTRRA. It provides further simplification by proposing uniform Social Security treatment for contributions, and, it ignores the tax attributes of employers when designing rules to promote employee saving.

Figure 3 here

This design also avoids the issue over which the Administration's proposal stumbled, namely overly-generous individual saving vehicles which compete with employer plans, by having an individual, coordinated limit on saving between individual and employer-sponsored vehicles. This will not solve the coverage problem by itself; that is, there will still be many smaller employers who will find the current IRA limits an attractive alternative to sponsoring a plan. But, unlike the Administration's RSA proposal, the coordinated limit will keep this plan from becoming the Trojan horse of the private pension system.

Finally, this model recognizes that more needs to be done to make a tax-based system an effective saving tool for low-paid workers. It is unclear why major reform should be enacted, unless it promises to expand participation in the private pension system, so this alternative plan recommends government matching contributions for low- and moderate-income workers just for that purpose. The fiscal realities facing the federal government today are very different today, but three years ago EGTRRA created a tax credit for low-income savers that PPSEA now proposes to make available to higher-paid workers. It makes more sense to make EGTTRA's credits refundable, which would help the majority of low-income savers who have no tax liability and provide an incentive to save that is similar to matching contributions. This issue involves more than fairness. Those with little saving currently are the ones least likely to be able merely to transfer money out of one account into a subsidized retirement account. Thus government subsidies might be more likely to increase national saving as well, if they were less directed to those able to obtain the benefits of the private pension system without contributing any additional net saving.

Conclusions

The challenges facing the US pension system are well-recognized. Despite large budgetary costs, the current structure does not provide substantial benefits for a very large portion of new retirees, particularly those who have had average or below-average earnings. Accordingly, Congress, and the country, is at a crossroads. Legislators can either decide to maintain the *status quo,* or they can strike out in a new direction.

Maintaining the *status quo* may seem the safer choice and may be the path chosen. Yet bolder action may be warranted. One approach, represented by the Administration's 2003 and 2004 proposals for ERSAs, LSAs, and RSAs, moves the private pension system toward a more efficient structure. The effectiveness of this design for increasing saving and plan participation, as well its effect on the long-term budgetary situation, is open to question. An alternative model for restructuring the U.S. private pension system takes some good ideas, along with the best elements of EGTRRA, PPSEA and the Administration's proposals, and repackages them. At the same time, the appeal of a simple, standard, universal savings plan is that it avoids both the mind-numbing complexity of PPSEA and the budgetary costs and distributional effects of the Administration's proposal. In sum, the private pension system does not necessarily need *more* saving tools, but rather it needs to put them to work more effectively. This is the critical first step towards reinventing the pension component of the new retirement paradigm.

Glossary

401(a). IRC § 401(a), the federal tax statute containing the basic requirements for qualified defined benefit and defined contribution pension plans under U.S. law.

401(k). IRC § 401(k), the federal tax statute containing the special requirements for a "cash-or-deferred" savings arrangement that enables employees to save for retirement on a pre-tax basis when contributing to their employer's defined contribution plan.

401(k) plan. A component of a qualified defined contribution plan based on IRC § 401(k) that permits pre-tax contributions by employees. A 401(k) plan is a qualified plan.

403(b). IRC § 403(b), the federal tax statute containing the primary requirements for tax-deferred defined contribution arrangements available to employees of educational institutions and certain non-profit organizations defined in IRC § 501(c)(3). 403(b) arrangements may also permit 401(k)-type, pre-tax contributions.

403(b) arrangements. A savings arrangement, also called a tax sheltered annuity, based on IRC § 403(b) that can permit pre-tax contributions by employees. A 403(b) arrangement is not a qualified plan.

408. IRC § 408, the federal tax statute containing the basic requirements for IRAs and SIMPLE plans based on IRAs.

408A. IRC § 408A, the federal tax statute containing the basic requirements for IRAs permitting Roth-contributions.

457(b). IRC § 457(b), the federal tax statute containing the basic requirements for tax-deferred defined contribution plans sponsored by state and local governments and tax-exempt employers that permit 401(k)-type, pre-tax contributions by employees.

457(b) plan. An employer-sponsored arrangement based on IRC § 457(b) that permits pre-tax contributions by employees. A 457(b) plan is not a qualified plan.

ACP. Average Contribution Percentage Test, one of the two primary tests for 401(k) plans that impose a ceiling on benefits for high-paid employees relative to the benefits received by low-paid employees in order to encourage their participation. The ACP test measures whether the difference between the amount of employer matching contributions and employee after-tax contributions, measured as a percentage of pay, made by NHCEs, on average, and by HCEs, on average, is within the spread permitted by IRC § 401(m).

ADP. Average Deferral Percentage Test, one of the two primary tests for 401(k) plans that imposes a ceiling on benefits for high-paid employees relative to the benefits received by low-paid employees in order to encourage their participation. The ADP test measures whether the difference between the amount of pre-tax contributions, measured as a percentage of pay, made by NHCEs, on average, and by HCEs, on average, is within the spread permitted by IRC § 401(k).

After-tax contributions. Employee contributions to an employer-based plan or IRA that are made from after-tax income so that only earnings are taxed when distributions are made from the plan.

Catch-up. Additional contributions permitted to defined contribution plans by employees who have attained age 50.

Coverage. One of the two primary non-discrimination tests for qualified plans that are intended to insure that a plan does not disproportionately favor high-paid employees. In general, this test measures whether the plan includes a sufficient number of participants who are NHCEs relative to the number of HCEs that participate and is defined IRC § 410(b).

Cross-testing. A method of testing a qualified plan for non-discrimination under IRC § 401(a)(4) that permits a defined benefit plan to be tested as if it were a defined contribution plan and a defined contribution plan as if it were a defined benefit plan.

Deemed IRAs. An IRA that is included within a qualified plan, a 403(b) arrangement or a 457(b) plan.

Defined benefit plan. A type of plan that pays retirement benefits, usually for life. Employees earn benefits under a plan formula usually based upon their pay and years of employment.

Defined contribution plan. A type of plan that provides an account for each participant and bases benefits on contributions to that account and its earnings.

EGTTRA. The Economic Growth and Tax Relief Reconciliation Act of 2001, the most recently-enacted tax legislation to amend employee benefits law significantly.

Employee stock ownership plan. A qualified plan that is a defined contribution plan designed to invest primarily in employer stock, defined in IRC §§ 409 and 4975(e)(7).

ERISA. The Employee Retirement Income Security Act of 1974, the primary modern law, including both labor and tax laws that governs most U.S. employee benefit plans.

ERSA. Employer Retirement Savings Account, proposed by the Administration in 2003 and 2004 as a simplified, uniform replacement plan for 401(k), SIMPLE and 457(b) plans as well as 403(b) arrangements.

HCE. Highly-compensated employee, defined in IRC § 414(q), one of the major concepts in the non-discrimination tests that qualified plans must satisfy. In 2004, an employee who earns at least $90,000 is an HCE.

IDA. Individual Development Account, proposed by the Administration in 2004 as a savings account for low-income individuals.

IRA. Individual retirement account governed by IRC § 408 and originally enacted as part of ERISA as a defined contribution savings plan for individuals without an employer-based plan. IRAs now can be found in employer-based plans such as SIMPLE IRAs and SEPs, and, if the plan permits it, employees may also make contributions to an IRA through a traditional defined contribution plan. An IRA is not a qualified plan.

IRC. Internal Revenue Code, the body of federal U.S. tax law statutes.

LSA. Lifetime Savings Account, proposed by the Administration in 2003 and 2004 as a new defined contribution account for general purpose saving.

Money purchase plan. A qualified plan that is a defined contribution plan with a fixed contribution formula.

NHCE. A non-highly compensated employee, defined in IRC § 414(q), one of the major concepts in the non-discrimination tests that qualified plans must satisfy. In 2004, an employee who earns less than $90,000 is a NHCE.

Non-discrimination rules. The body of rules under 401(a)(4) designed to insure that qualified plans do not discriminate in favor of highly-compensated employees in their plan benefits or contributions. These rules, coordinated with the coverage rules, implement the non-discrimination standard that prohibits a qualified plan from being designed or operated in favor of HCEs.

Non-qualified deferred compensation plan. A retirement plan, usually for executives, that is not a qualified plan but is often used as a supplement to one. Plan participants are not taxed on contributions to the plan or accrued benefits until they are received or available for distribution, at which time employers receive a deduction for their contributions to the plan.

PBGC. Pension Benefit Guaranty Corporation, the federal insurer of defined benefit plans.

PPSEA. The Pension Preservation and Savings Expansion Act of 2003, H. R. 1776, major pension reform legislation proposed in 2003 by Representatives Rob Portman and Benjamin L. Cardin, the primary sponsors of EGTTRA.

Pre-tax contributions. Employee contributions to an employer-based 401(k) plan, 403(b) arrangement, 457(b) plan or to an IRA that are made from pre-tax income and are not taxed until they (plus earnings) are subsequently distributed from the plan.

Profit sharing plan. A qualified plan that is a defined contribution plan with a discretionary contribution formula.

Qualified plan. A defined benefit or defined contribution plan that satisfies the requirements of IRC § 401(a), and other relevant legal provisions. Under the special tax treatment available to qualified plans, employers may take an immediate deduction for contributions to their plans but plan participants are not taxed until they receive benefits from the plan.

Roth 401(k). A 401(k) plan funded with Roth-contributions, rather than with pre-tax contributions, enacted in EGTTRA and scheduled to begin in 2006.

Roth IRA. An IRA funded through Roth-contributions.

Roth-contributions. A type of contribution to an IRA, created under IRC § 408A and named for former Senator William Roth, that is made from after-tax income and is generally not subject to tax thereafter. Beginning in 2006, 401(k) and 457(b) plans and 403(b) arrangements may permit Roth-contributions.

RSA. Retirement Savings Account, proposed by the Administration in 2003 and 2004 as a uniform replacement plan for IRAs and Roth IRAs.

SARSEP. A form of SEP, established before 1997, permitting employees to make 401(k)-type contributions to their employer's SEP. A SARSEP is not a qualified plan.

SEP. Simplified Employee Pension Plan, a simplified employer-sponsored plan based upon IRAs created under IRC § 408(k). A SEP is not a qualified plan.

SIMPLE. Savings Match Incentive Plans for Employees, a simplified employer-based plan created under either IRC § 401(k) or IRC § 408(k) that has individual savings accounts to which both employers and employees contribute. A SIMPLE 401(k) is a qualified plan but a SIMPLE IRA is not.

Social Security integration. A safe-harbor exception to the non-discrimination rules that permits employers to take Social Security into account when determining benefits or contributions in a qualified plan, as described in IRC § 401(l).

Stock bonus plan. A qualified plan that is a defined contribution plan with a discretionary contribution formula whose benefits are distributable in company stock.

Tax sheltered annuity. Another name for a 403(b) arrangement.

Thrift plan. A form of profit sharing plan that predates 401(k) plans and permits employee after-tax contributions.

Top-heavy rules. Tests found in IRC § 416 that requires qualified plans to provide minimum contributions or benefits if high-paid company officers and owners receive more than 60% of plan benefits or contributions.

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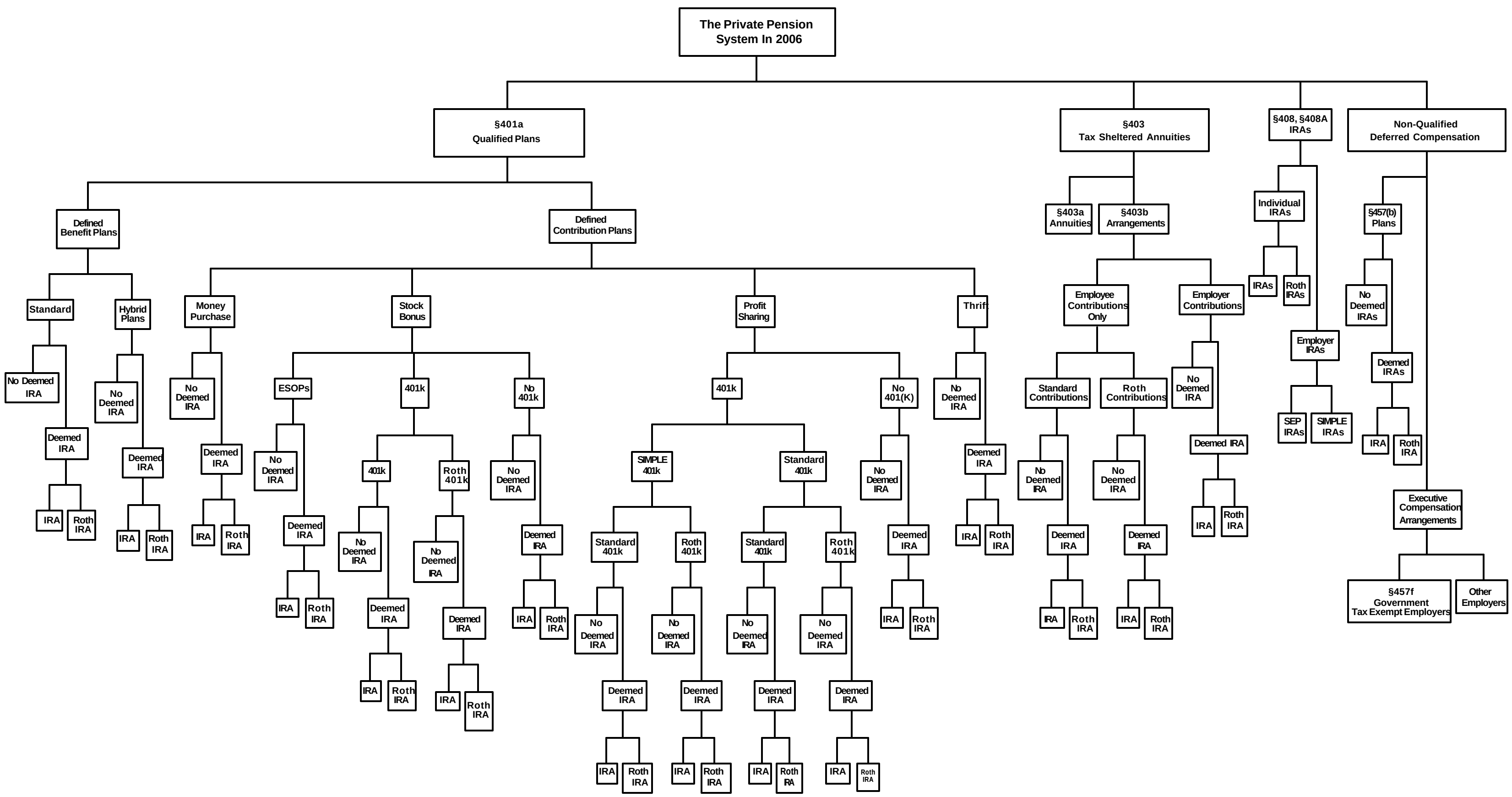
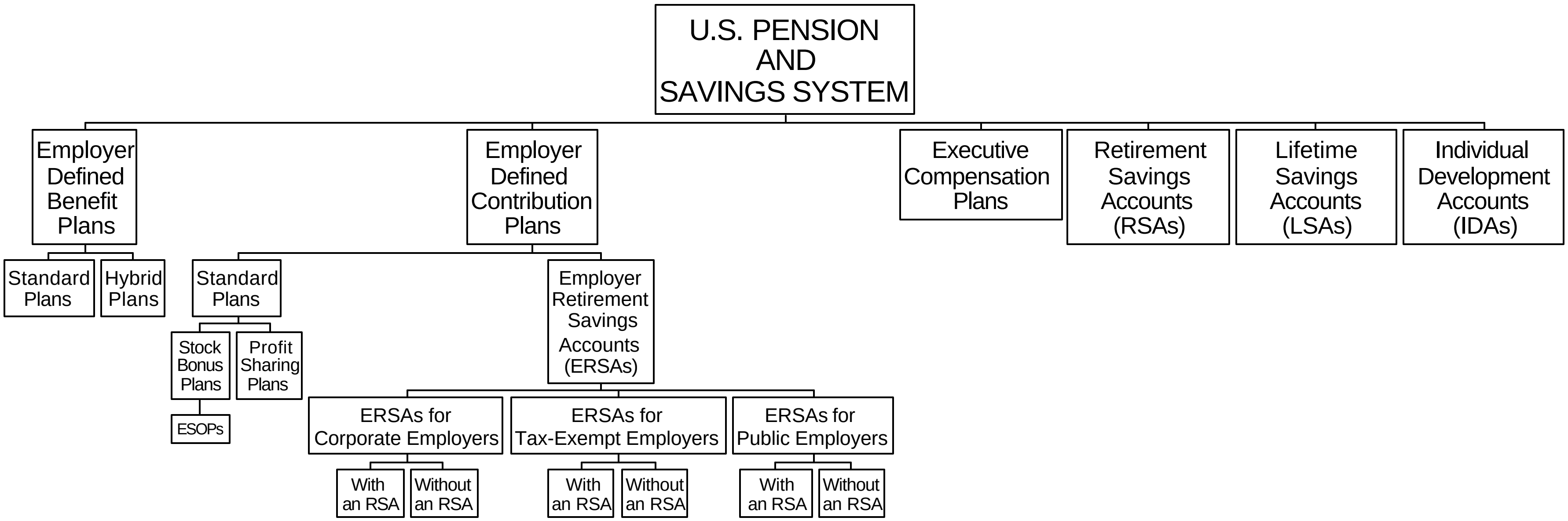
Figure 1. Plan Types Available in 2006 in the U.S. Private Pension System



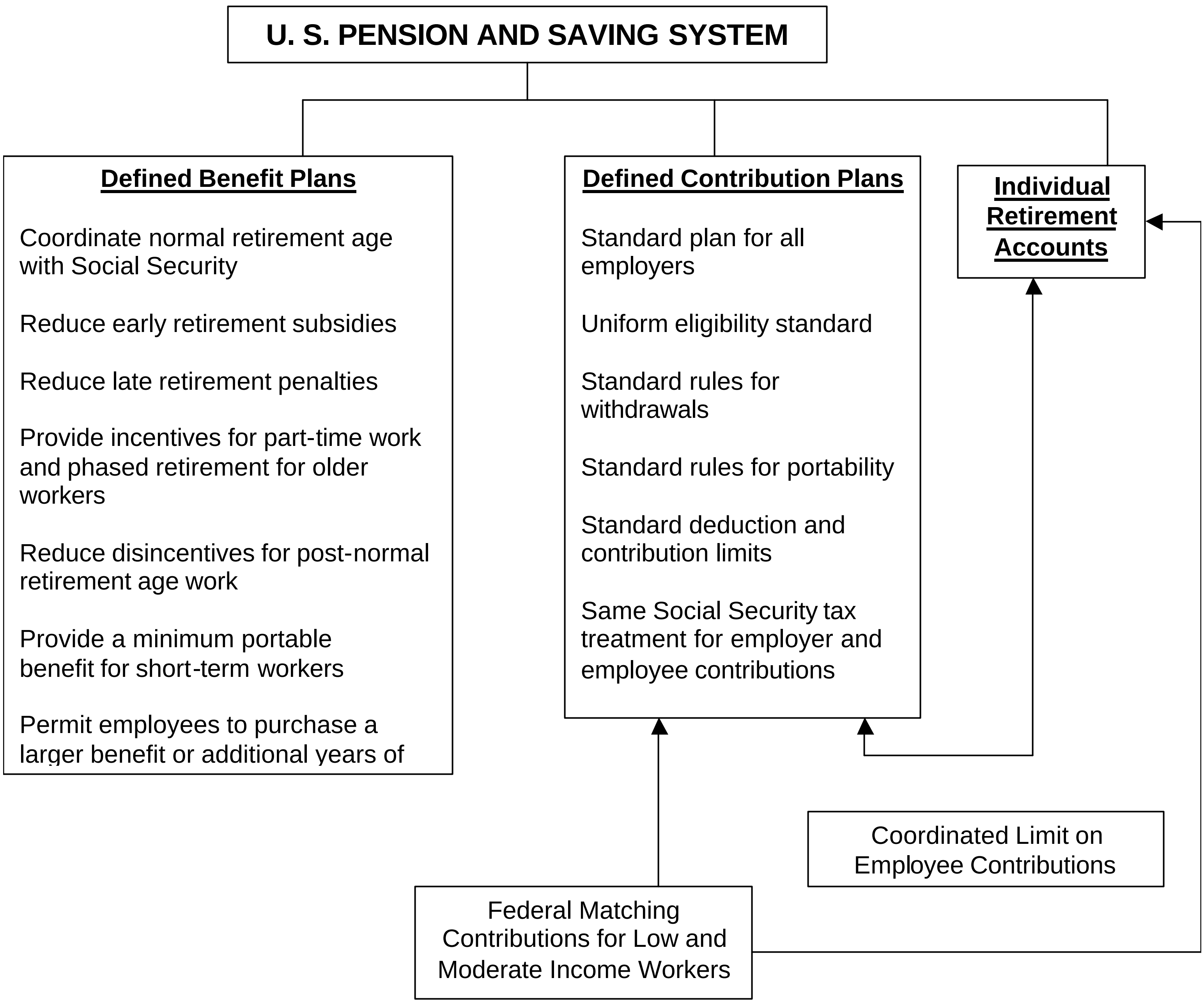
Source: Perun and Steuerle (2000) (revised for EGTTRA)

Figure 2. Proposed New Structure for the U.S. Private Pension System



Source: U.S. Treasury Department (2004); IRC §§ 401(a), 409, 4975(e)(7)

Figure 3. An Alternative Structure for the U.S. Private Pension System



Source: Perun and Steuerle (2002)

Table 1. Rules of the U.S. Private Pension System in 2004

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	Money Purchase	Profit Sharing, Stock Bonus, Standard 401(k)	Profit Sharing, Stock Bonus, SIMPLE 401(k)	Other Profit Sharing or Stock Bonus with no 401(k)	Employee Stock Ownership Plan	IRC § 403(b)
Eligible Employer	any employer		any employer except state & local governments	401(k) eligible employer with <100 employees and no other plan	any employer	corporate employer	tax-exempt organizations and public schools
Overall Annual Limits	annual benefit limit, per person, is the lesser of $165,000* or 100% x the highest 3 years' pay	annual contribution limit, per person, is the lesser of $41,000[4]* or 100% of pay	per person, same as money purchase + 401(k) contributions up to a maximum of $13,000*	annual contribution limit, per person, is a 401(k) contribution up to a maximum of $9,000* + the employer contribution	same as money purchase		
Pay Limit	$205,000*						

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	**Money Purchase**	**Profit Sharing, Stock Bonus, Standard 401(k)**	**Profit Sharing, Stock Bonus, SIMPLE 401(k)**	**Other Profit Sharing or Stock Bonus with no 401(k)**	**Employee Stock Ownership Plan**	**IRC § 403(b)**
Required Employer Contribution	amount for funding current + past service costs for each employee over future service OR the normal costs of the plan + past service liability amortized over 10 years	amount required by plan formula	none	employer matching contribution up to 3% of pay OR fixed 2% of pay contribution	none, usually		

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	**Money Purchase**	**Profit Sharing, Stock Bonus, Standard 401(k)**	**Profit Sharing, Stock Bonus, SIMPLE 401(k)**	**Other Profit Sharing or Stock Bonus with no 401(k)**	**Employee Stock Ownership Plan**	**IRC § 403(b)**
Employee Contribution Limits	amount required by plan formula, if any	not permitted	maximum contribution of $13,000* + $3,000* catch-up contribution if or age 50+	maximum contribution of $9,000* + $1,500* catch-up contribution if age 50+	not permitted	none, usually	same as standard 401(k)
Employer Deduction Limits	lesser of 165% of current liability or accrued liability minus lesser of value of plan assets or their actuarial value	25% of aggregate employee pay	25% of aggregate employee pay (excluding 401(k) contributions)	greater of contributions (excluding 401(k) contributions) up to 25% of aggregate employee pay or required contribution	same as money purchase	same as money purchase + certain dividends and interest on any loan	not applicable

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	**Money Purchase**	**Profit Sharing, Stock Bonus, Standard 401(k)**	**Profit Sharing, Stock Bonus, SIMPLE 401(k)**	**Other Profit Sharing or Stock Bonus with no 401(k)**	**Employee Stock Ownership Plan**	**IRC § 403(b)**
Exclusions from Social Security tax	both contributions and distributions		not for 401(k) contributions but other contributions and all distributions qualify		yes	yes	not for employee contributions but employer contributions and all distributions qualify
10% Early Withdrawal Tax	yes						
In-Service Withdrawals	not permitted		financial hardship[5], minimum 2 year holding period for employer contributions, loans		minimum 2 year holding period, loans		financial hardship, loans
Non-discrimination rules (not governmental plans)	top-heavy, coverage and non-discrimination rules		ADP, ACP, top-heavy, coverage and non-discrimination rules[6]	can be exempt from top-heavy rules; no ADP, ACP or non-discrimination rules	top-heavy, coverage and non-discrimination rules		ACP for matching contributions, availability test for deferrals and non-discrimination rules

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	**Money Purchase**	**Profit Sharing, Stock Bonus, Standard 401(k)**	**Profit Sharing, Stock Bonus, SIMPLE 401(k)**	**Other Profit Sharing or Stock Bonus with no 401(k)**	**Employee Stock Ownership Plan**	**IRC § 403(b)**
Integrated with Social Security	may be		may be (not 401(k) contributions or matching contributions)	no	may be	no	may be
Spousal Protection	survivor annuity, consent and death benefit rights		only death benefit usually[7]				
Vesting	deferred		immediate for 401(k) contributions; all others deferred	immediate	deferred		immediate for deferrals; others deferred

	IRC § 401(a) Plans						IRC § 403(b) Arrangements
	Defined Benefit	**Money Purchase**	**Profit Sharing, Stock Bonus, Standard 401(k)**	**Profit Sharing, Stock Bonus, SIMPLE 401(k)**	**Other Profit Sharing or Stock Bonus with no 401(k)**	**Employee Stock Ownership Plan**	**IRC § 403(b)**
Special requirements	PBGC guarantee and premium of $19 per participant	minimum funding required in full each year	special vesting rules for matching contributions		none	forfeitures/interest payments raise annual contribution limit if ?1/3 of contributions are for HCEs; 100% employer securities allowed; diversification optional at 55; put option/voting rights.	special catch-up contributions permitted with 15+ years of service

	IRC §408, 408A IRAs				Non-qualified Deferred Compensation Plans	
	Traditional IRA	**Roth IRA**	**SEP-IRA**	**SIMPLE IRA**	**Eligible 457(b) plans**	**Executive Arrangements**
Eligibility	anyone	anyone with earnings less than $110,000 for individuals and $160,000 for couples[8]	any employer	employees of employers with no other plan and <100 employees	employees of state and local government and tax-exempt organizations	select group of officers or highly-compensated employees
Dollar Limit on Contributions	$3,000* for all IRAs+ $500* catch-up contributions; contributions are fully deductible if there is no employer plan or income is less than $45,000 for individuals and $65,000 for couples [9]	$3,000* for all IRAs + $500* catch-up contributions	lesser of $41,000* or 25% of pay	amount of employee and employer contributions	$13,000* + $3,000* catch-up contributions	none
Maximum Per Cent of Pay Limit on Contributions	100%	100%	25%	not applicable	100%	none
Employer Contribution Limits	not applicable		lesser of $41,000* or 25% of pay	matching contribution of up to 3% of pay or fixed contribution of 2% of pay	none	

	IRC §408, 408A IRAs				Non-qualified Deferred Compensation Plans	
	Traditional IRA	Roth IRA	SEP-IRA	SIMPLE IRA	Eligible 457(b) plans	Executive Arrangements
Employee Contribution Limits	\$3,000* + \$500* catch-up contributions	\$3,000* + \$500* catch-up contributions	not applicable	\$9,000* + \$1,500* catch- up contributions	lesser of \$13,000* + \$3,000* catch-up contributions or 100% of pay	none
Employer Deduction Limits	not applicable		25% of aggregate pay	amount of contributions	not applicable	none
Exclusion from SS Tax	not for contributions but distributions qualify		both contributions and distributions	not for employee contributions but employer contributions and distributions qualify	not for employee contributions but distributions qualify	depends on vesting
10% Early Withdrawal Tax	yes	usually not	yes	yes, increased to 25% in 1st 2 years	not applicable	no (unless annuity purchased)
Early Withdrawal Tax Exceptions	medical, 1st home purchase, higher education expenses, health insurance payments for unemployed	age 59 ½, death, disability, 1st home purchase	same as traditional IRA	same as traditional IRA	not applicable	none (unless annuity purchased)
Withdrawals Permitted	yes, may be subject to excise tax	5-year waiting period	yes		unforeseeable emergency only while employed	yes

<table>
<tr><th rowspan="2"></th><th colspan="4">IRC §408, 408A IRAs</th><th colspan="2">Non-qualified Deferred Compensation Plans</th></tr>
<tr><th>Traditional IRA</th><th>Roth IRA</th><th>SEP-IRA</th><th>SIMPLE IRA</th><th>Eligible 457(b) plans</th><th>Executive Arrangements</th></tr>
<tr><td>Loans Available</td><td colspan="4">no</td><td>unclear</td><td>yes</td></tr>
<tr><td>Non-discrimination rules</td><td>none</td><td>none</td><td>uniform percent of pay contribution; top-heavy rules</td><td>required employer contribution only</td><td>none</td><td>none</td></tr>
<tr><td>Pay Limit</td><td colspan="2">see above</td><td>$205,000*</td><td>$205,000* for 2% of pay contribution</td><td>$205,000*</td><td>not applicable</td></tr>
<tr><td>Integrated with Social Security</td><td colspan="2">no</td><td>may be</td><td>no</td><td colspan="2">not applicable</td></tr>
<tr><td>Spousal Protection</td><td colspan="6">none under federal law, may be available under state law</td></tr>
<tr><td>Vesting</td><td colspan="5">immediate</td><td>usually deferred</td></tr>
<tr><td>Special Restrictions and Benefits</td><td>none</td><td>after-tax contributions; no tax on distributions</td><td>employer does not have to contribute every year</td><td>employees are generally responsible for investments</td><td>special double catch-up contributions available during the 3 years before retirement; plans are technically unfunded but contributions to public sector plans must be held in trust</td><td>employee taxed when benefits are paid or made available (or when vested for tax-exempts); may be a defined contribution or defined benefit plan</td></tr>
</table>

* means the amount is subject to adjustment for inflation or through a scheduled increase

Source: IRC §§ 219, 401(a), 401(k), 401(m), 402, 403, 404, 408, 408A, 409, 410, 411, 412, 414, 415 and 416 and their regulations.

Table 2. Proposed Rules for ERSAs, RSAs, LSAs and IDAs, 2003 and 2004

	EMPLOYER PLAN	EMPLOYER OR INDIVIDUAL PLAN	INDIVIDUAL PLAN	
	Employer Retirement Savings Accounts (ERSAs)	**Retirement Savings Accounts (RSAs)**	**Lifetime Savings Accounts (LSAs)**	**Individual Development Accounts (IDAs)**
Sponsor/Contributor	any employer	not applicable		
Eligibility	not applicable	**2004:** no income limits; no age limits	**2004:** no income limits; no age limits	single: <$20,000* income married:<$40,000* income
Annual funding	Optional; pre- and post-tax employee contributions; pre-tax employer contributions (broad-based and match)	optional; post-tax only	Optional; post-tax only	individual contributions + 100% match up to $500
Contribution Limits	employee: $30,000 + $3,000 catch-up* maximum: $41,000* or 100% pay	**2003**: $7,500* or pay **2004**: $5,000* or pay	**2003:** $7,500or pay* **2004:** $5,000* or pay	?
Exclusion from SS Tax	no, employee contribution; yes, other contributions and distributions	not applicable		?

	EMPLOYER PLAN	EMPLOYER OR INDIVIDUAL PLAN	INDIVIDUAL PLAN	
	Employer Retirement Savings Accounts (ERSAs)	**Retirement Savings Accounts (RSAs)**	**Lifetime Savings Accounts (LSAs)**	**Individual Development Accounts (IDAs)**
Early Withdrawal Tax	probably, same as today	**2003:** non-qualified withdrawals subject to income+ penalty tax **2004:** non-qualified withdrawals in excess of contributions subject to income + penalty tax; 5 year holding period for conversions from ERSAs or traditional IRAs to avoid 10% penalty	no	?
In-service or qualified withdrawals	probably, same as today	after age 58, death, disability	any amount, any time	higher education, 1st time home purchase, small business capitalization

Non-discrimination rules	**2003:** no top-heavy rules, must have 70% coverage of NHCEs in plan, no integration or cross-testing rules. **2004:** current minimum coverage, top-heavy, integration, cross-testing rules apply; no ACP or ADP; if NHCEs' contributions (employer and employee) average <6% of pay, HCE contributions limited to 200% of NCHE contribution, otherwise no limit; design safe harbors if NHCEs get vested contributions of 3% of pay. **2004:** if 50% vested match up to 6% of pay, no testing; special rules for government and non-profit employers.	not applicable		
Integrated with Social Security	**2003:** no **2004:** yes			
Spousal Protection	?	?	?	?
Vesting	immediate for employee contributions; deferred for others?	not applicable		

Special features	consolidates 401(k), SIMPLE 401(k), 403(b), governmental 457(b)s, SARSEPs, SIMPLE IRAs. **2003:** uniform definition of HCE and compensation: HCE = pay > taxable wage base; compensation = W-2 pay + elective deferrals. **2004:** no uniform definition of HCE or compensation; Roth treatment for after-tax contributions and distributions; current rules for employee and employer contributions	existing IRAs frozen but taxable IRAs could be converted (no income limits); Roth treatment for contributions and distributions. **2004:** no withdrawals for 1st home purchase, education, health expenses or unemployment; no minimum distribution rules; marital rollovers permitted; no income cap on Roth conversions	Roth treatment for contributions and distributions; no minimum distribution rules; can convert Coverdell accounts and 529 plans but not health savings accounts or medical savings accounts	sponsoring financial institutions get a 100% tax credit for matching contributions plus a $50 per account credit for administrative expenses.

* indicates an amount indexed for inflation

Source: Portman and Cardin (2003a, 2003b); U.S. Department of the Treasury (2004)

Endnotes

[1] This rule can be found in Proposed Treasury Regulation § 1.408(q)-1(g).

[2] The provisions of the Pension Preservation and Protection Act of 2003, H.R. 1776, can be found at: http://thomas.loc.gov, last accessed July 5, 2004.

[3] Legislation to create Retirement Savings Accounts was introduced into the House of Representatives on June 25, 2004 as H.R. 4714, and legislation to create Lifetime Savings Accounts was introduced on March 31, 2004 into the House of Representatives as H.R. 4078 and the Senate as S. 2263.

[4]The $41,000 overall dollar limit is a cumulative limit for an employee across all defined contribution plans of the same employer.

[5] Financial hardship is an immediate and heavy financial need, even if foreseeable or voluntarily incurred, not able to be satisfied by other resources.

[6]Both the Actual Deferral Percentage (ADP) test for 401k contributions and the Average Contribution Percentage (ACP) test for matching and after-tax contributions are designed to limit contributions made by HCEs to a proportion based on the average contributions made by NHCEs.

[7] The surviving spouse receives the account balance as a death benefit unless he/she has consented to another beneficiary being named.

[8] The income phase-out schedule for Roth IRAs is $95,000-110,000 for individuals and $150,000-160,000 for married couples filing jointly.

[9] IRA income phase-out schedule in 2004: $45,000-$55,000 for individuals and $65,000-$75,000 for married couples filing together. These phase-outs are scheduled to increase to $50,000-$60,000 for individuals and $80,000-$100,000 for joint filers by 2007. There are also special limits for non-working spouse.