THIRD WAY

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Capitalize Workers!


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Raising the minimum wage has justifiably captured policy makers' attention, but if the goal is to materially raise living standards for every American worker, we should also be calling for a minimum pension. Done right, this would not only create real wealth for the middle and working classes, it would use the power of financial markets to reduce wealth disparity instead of widening it.

There is a vast difference in the way the wealthy and the rest of Americans earn their money. In 2010, 60 cents of every dollar earned by those in the top 1 percent came from investments and businesses they owned. For the middle class, it was 6 cents.

For decades, the returns to capital have far outstripped the returns to labor. Before the mid-1980s, worker salaries constituted 65 percent of national income. In 2012, they were 58 percent. Economists rightly fret over how this contributes to wealth inequality. Well, if you can't beat 'em, join 'em. If all working people, whatever their wage, could get a piece of these gains, it would improve their financial well-being exponentially. This is where the minimum pension comes in.

We are proposing a Savings Plan for Universal Retirement account, the centerpiece of which is a 50-cent-per-hour minimum retirement contribution from all employers to virtually all employees. This is not what President George W. Bush proposed when he sought to privatize Social Security in 2005. Under our plan, Social Security remains as is, but every worker would also have his or her own private Individual Retirement Account, the way many white-collar workers do now.

Contributions placed in this account would automatically go into a privately run low-fee life-cycle fund. (Life-cycle funds comprise a mix of stock and bond investments tailored to how far the owner is from retirement.) Recipients could switch investment options to say, an S&P 500 index fund. A government board like the one that now manages the retirement accounts of federal employees would sanction the investment options.

This policy isn't meant to replace current pension plans; employers that still provide retirement benefits would satisfy the new requirement. It is geared to individuals who are not saving in the existing system. And it would be completely portable, like a cellphone number.

A 50-cent minimum pension (adjusted for inflation) would amount to a minimum yearly employer contribution of roughly $1,000 for each full-time worker. It would improve retirement security for the 47 percent of these workers who are not currently contributing to any employer-sponsored retirement plan. Contributions would begin early on so even small amounts would have decades to grow.

How much? If stocks and bonds enjoy the same average rates of return as they did over the last 45 years, someone who begins earning income at age 22, receives only the minimum contribution each year, and retires at age 67 would have a balance of approximately $160,000, in 2013 dollars. By contrast, the median couple — not individual — approaching retirement today has only $42,000 in private retirement accounts. Of course, past gains are no guarantee, but over the long term investments in diversified stock and bond funds have usually paid off. And since this is on top of Social Security, a certain amount of risk is acceptable.

The biggest winners would be minorities, who have high labor participation rates but lag far behind whites in retirement savings. Only 34 percent of working-age Latinos and 51 percent of African-Americans with full-time jobs participate in employer-sponsored retirement plans, compared with 59 percent for whites, who also contribute more to these plans.

Individuals would be able to match or exceed employer contributions (and employers could contribute additional amounts, as some do now). For those at the lower end of the income spectrum, up to half of their contributions could be reimbursed by the Savers Credit, an underused government savings incentive that became law in 2001. Simply matching the contribution yourself would increase your expected account balance at retirement to more than $300,000. This nest egg could not be raided or borrowed against, and in retirement would automatically convert to an annuity, unless you chose otherwise. So we would never outlive our savings. A $160,000 account would amount to a $790 monthly annuity.

How would this affect businesses? The 50-cent minimum contribution is only one-sixth of the proposed increase to the minimum wage. And Congress could make a number of small changes in the tax code to make this palatable to employers.

Being dependent only on wages is, unfortunately, no longer enough. A minimum pension would create a chain of wealth for everyone who works and it would allow ordinary Americans to benefit from the expansion of the world economy rather than being at the mercy of it.

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