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By Paul Schott Stevens

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“Will we be fair to future generations?” That is the question posed recently by Federal Reserve Chairman Ben Bernanke in a speech to the Washington Economic Club on the retiring Baby Boom generation. The more specific question is: “Are we moving forward fast enough to provide a secure retirement for all generations?”

A look back at the past 25 years of retirement savings shows just how much America has accomplished.

A quarter century ago, on Nov. 10, 1981, the Internal Revenue Service proposed regulations that gave employers the potential to use Section 401(k) of the tax code to establish broad-based, tax-favored savings plans for all workers. In the years since, 401(k) plans have become a mainstay of America’s retirement security. With 47 million active participants in 2005, 401(k) plans cover twice as many current workers as private defined benefit pension plans.

Yet the growth in 401(k) plans – $2.4 trillion in savings in 2005 – is even more impressive when you consider the headwinds they faced out of Washington almost from their birth. Until a few years ago, America’s tax and retirement policies sought to limit the growth of 401(k) plans. For example, in 1983, Congress reduced and then froze the total employer plus employee contribution limit at $30,000, where it stayed for 17 years. In 1986, lawmakers also imposed a $7,000 limit on the employee’s contribution and further complicated the rules.

Despite these limitations, 401(k) plans have proven to be popular with both employers and employees, sending a clear message that Americans value greater opportunities to save for retirement. In 1996, Congress took steps to help them make the most of those opportunities, when lawmakers reduced the burden on small employers and simplified plan rules. In 2001, Congress loosened restrictions on participants’ contributions, created catch-up contributions for older workers, and increased rollover opportunities.

This year, lawmakers passed the Pension Protection Act, making the 2001 changes permanent and encouraging businesses to automatically enroll eligible workers. The PPA also makes it easier for employers to choose better default investments and to provide sound investment advice for participants. These changes have cemented the 401(k) as a pillar of solid retirement policy.

We've come a long way in 25 years. However, we must expand savings opportunities at a much faster clip if we are to increase retirement security for all generations. Congress, employers, and the financial services industry each have a role to play. We need to give the 22 million employees who are not participating in their employers' 401(k)s greater incentives to participate. We need to expand the number of employers who offer such plans. And we must find ways to cover those who are not eligible for an employer-sponsored plan.

These are not easy tasks, but solutions are out there. Reducing the complexity and cost of administration encourages many businesses, especially small and medium-sized companies, to offer retirement benefits. Simplicity also can help bolster IRAs, both for workers who lack an employer-sponsored plan and for covered workers who want to save more. Universal tax deductions for IRA contributions in the 1980s generated a great influx of savings dedicated to retirement, but that impetus was lost when IRA rules became restrictive and complex.

Congress also should consider tax incentives for savings outside of retirement plans. The Generate Retirement Ownership Through Long-Term Holding (GROWTH) Act would defer taxation of automatically reinvested long-term capital gains until mutual fund shares are sold, rather than taxing the gains every year. This important piece of legislation provides a sensible way for tens of millions of Americans – most of them middle class – to create a more secure financial future for themselves and their families.

Now is the ideal time to discuss all solutions that promise a more secure retirement future. At 25 years young, 401(k) is entering its prime. Individual Americans have helped it grow and succeed thus far. It's up to us to help it reach its full potential.

Paul Schott Stevens is President of the Investment Company Institute, the national trade association of the mutual fund industry. Mutual funds hold half of the $2.4 trillion in assets invested in 401(k) plans and have pioneered many of the innovations in investing, service, and administration that have made 401(k) plans so successful today.
