

# **How Persistent Low Returns Will Shape Saving and Retirement**

EDITED BY

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## Chapter 11

# **State-sponsored Retirement Savings Plans: New Approaches to Boost Retirement Plan Coverage**

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*William G. Gale and David C. John*

Many workers need help in building retirement security to supplement their social security benefits. The share of the workforce covered by a retirement saving plan has remained relatively flat in recent decades (Copeland 2014). The current low-return investment environment also makes it more difficult for people to accumulate a target of wealth in retirement, especially if the onset of retirement saving is delayed. As a result, bringing people into the retirement system and having them initiate contributions to retirement accounts as early as possible remains an important priority (see Reilly and Byrne's chapter in this volume).

Recent federal policy has not had a significant effect on coverage rates. The US Pension Protection Act of 2006 encouraged automatic enrollment in defined contribution (DC) plans. While the policy raised participation rates among those workers who were already offered a plan, it did little to expand coverage rates. In 2014, an Obama administration executive order established the MyRA, which is available nationally as a starter retirement saving account, but it has generated only very limited participation and was since cancelled under the Trump administration. Federal legislation creating an automatic Individual Retirement Account (IRA) and open multiple employer plans (MEPs) has been introduced but not enacted.<sup>1</sup>

In the wake of stagnant coverage trends and lacking comprehensive federal legislation, several states have acted on their own. Five states (California, Connecticut, Illinois, Maryland, and Oregon) have enacted Secure Choice plans based on the Automatic IRA (AARP 2017). In these plans, states sponsor a simple, low-cost payroll deduction plan managed by private-sector providers. The structure is similar to Section 529 college savings plans. With some exceptions, employers are required to participate in the plan if they do not offer workers another type of retirement plan. Eligible workers are automatically enrolled. In addition, two states (Washington and New Jersey) are developing retirement savings marketplaces, state-sponsored

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websites that enable small businesses to find retirement plans that are pre-screened to meet certain criteria. Many other states are considering Secure Choice plans, marketplaces, or other options, such as Vermont's decision to start an open MEP. The best plan for a particular state will depend on its economic needs, political constraints, and other factors.

Although federal legislative action has been lacking, federal regulations by the Department of Labor in 2016 temporarily eased the implementation of state actions, by confirming conditions under which state-sponsored retirement savings plans are exempt from federal pension regulation (81 F.R. § 92639).<sup>2</sup> Yet in 2017, Congress used the Congressional Review Act to overturn the relevant regulations and to prohibit agencies from issuing similar rulings in the future without advance congressional approval. While reversing these regulations will hamper state-sponsored plans, it will not necessarily end them.<sup>3</sup>

This chapter evaluates models and features used in state-sponsored retirement saving plans. These plans have the potential to raise the number of Americans with access to payroll-deduction retirement saving plans, and thus to reduce the number of retirees with few financial resources other than social security benefits. They could also improve the sponsoring states' fiscal outlooks, by reducing the extent to which future retirees depend on taxpayer-financed government services.<sup>4</sup>

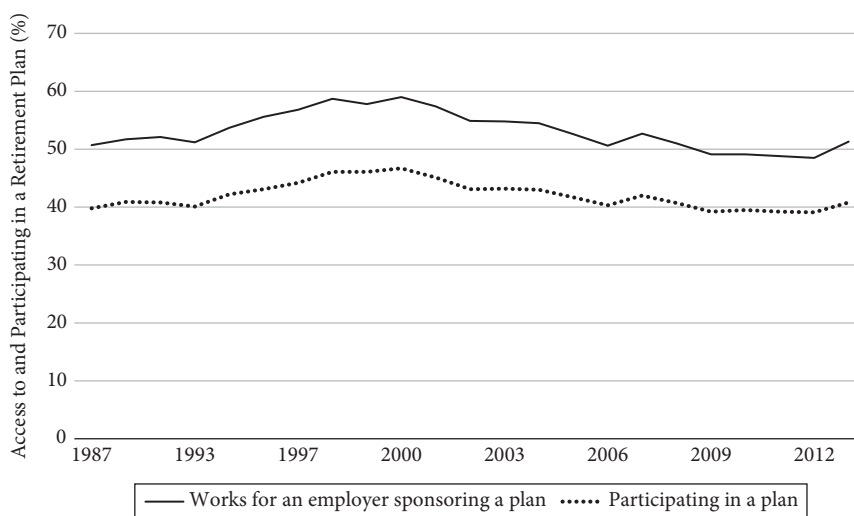
Our main conclusion is that, regardless of which approach—Secure Choice, open MEP, marketplace, or other—is taken, plans that boost coverage most will feature two characteristics: required provision of retirement savings plan by firms, and automatic enrollment of eligible workers. Yet we also note that, under current legal and regulatory conditions, Secure Choice is the only model that enables states to require that employers provide a plan.

This chapter provides background on workers' access to retirement saving plans, describes options that states have taken to date and other actions they could pursue, and evaluates the importance of coverage mandates on firms and automatic enrollment of workers.

### **Workers' Access to Retirement Savings Plans**

The proportion of US private sector workers with access to an employer-sponsored payroll deduction retirement savings plan or pension has remained stagnant for several decades. Figure 11.1 shows the share of private sector workers covered by a retirement savings or pension plan between 1987 and 2013.<sup>5</sup> Both coverage rates and plan participation have remained relatively constant over the 26-year period. Despite a slight uptick in the late 1990s, coverage in 2013 was the same as it was in the 1980s (as shown in Figure 11.1).

## State-sponsored Retirement Savings Plans 175



**Figure 11.1.** Access to and participation in US private sector employer-sponsored retirement plans, 1987 to 2013 (workers aged 21–64)

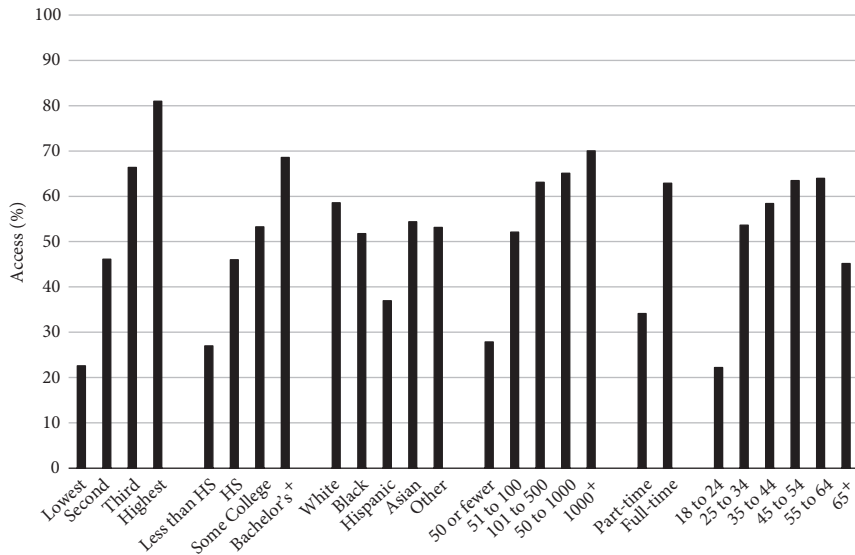
*Source:* Copeland (2014).

Access to a retirement plan varies by workers' demographic characteristics and firm size, as shown in Figure 11.2. Coverage rates in 2012:<sup>6</sup>

- are higher for higher paid employees, from 23 percent in the lowest quartile to 81 percent in the highest quartile;
- are higher for the better educated. Only 27 percent of workers with less than a high school degree were covered, compared to 69 percent of those with a bachelor's degree or more education;
- are fairly constant with respect to age, after workers reach age 25. Coverage rates vary from 54 to 64 percent for workers aged 25 to 64;
- are higher for full-time than for part-time workers;
- are higher for whites than for other groups;
- and rise with firm size. Among firms with 50 or fewer workers, only 28 percent of workers have access to a retirement savings plan. Among firms with 1,000+ employees, 70 percent have access to a plan.

Participation rates, given coverage, are fairly high, as shown in Figure 11.3. Conditional participation rates exceed 72 percent for all worker characteristics and firm sizes, except for three categories—workers aged 18–24, workers in the lowest earnings quartile, or high school dropouts. Even in those categories, conditional participation rates exceed 50 percent. Likewise, Figure 11.3 shows that conditional participation rates have been

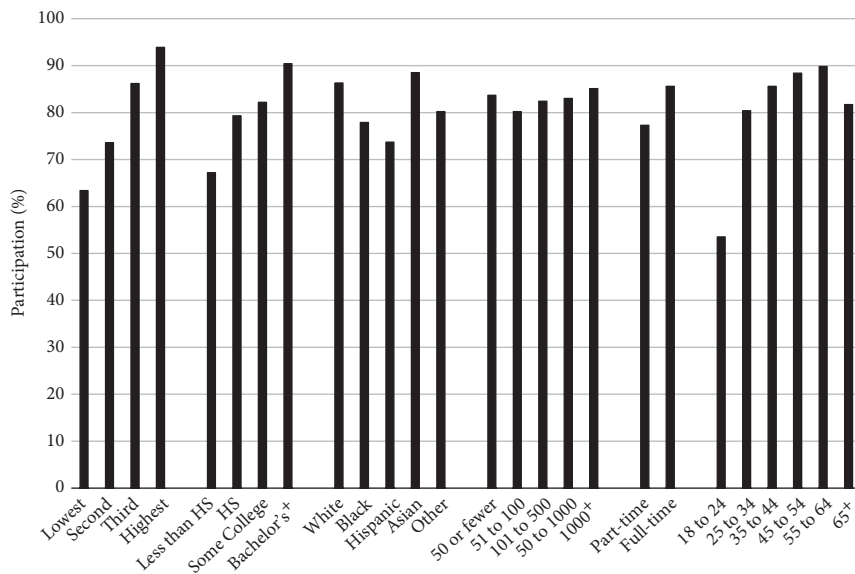
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**Figure 11.2.** US private sector retirement plan access by selected demographics

*Note:* Access is defined as working for an employer who offers a retirement plan and being eligible for that plan.

*Source:* GAO (2015) analysis of 2012 SIPP data.



**Figure 11.3.** Participation in a US private sector retirement plan conditional on access

*Source:* GAO (2015) analysis of 2012 SIPP data.



high and relatively steady—between 79 percent and 81 percent—since 1987. These facts suggest that expanding coverage will expand participation as well.

Lack of access to workplace pensions matters because it impedes the accumulation of retirement wealth. About 61 percent of employees with access to an employer-sponsored plan held more than \$25,000 in overall (non-defined-benefit) saving balances, and 35 percent held \$100,000 or more. By contrast, among those without access to a plan, 87 percent held less than \$25,000 and only 5 percent held \$100,000 or more (Helman et al. 2016).<sup>7</sup>

### **Designing State-sponsored Plans to Meet the Needs of Small Business Employees**

Two principal models for state-approved plans have been used to date, though others may be considered in the future. Table 11.1 describes each of the major approaches and Table 11.2 summarizes several advantages and disadvantages of each option. A successful plan will be practical for small businesses and the state to implement, and will meet the needs of affected employees.

TABLE 11.1 Comparison of state retirement plan structures

	Auto IRA	Open MEP	Marketplace	MyRA
Account Structure	Payroll deduction IRA (Traditional or Roth)	401(k) or other DC plan	Varies. May include SIMPLE IRAs, Auto IRAs, Roth IRAs, 401(k), MyRA	Roth IRA
Employer Participation Requirement	Yes	No	No	No
Employer Contribution	No	Allowed	Allowed	No
Contribution Limits	\$5,500 annually (\$6,500 if over 50)	Same as for a 401(k): \$18,000 annually (\$24,000 if over 50)	Depends on account type	\$5,500 annually (\$6,500 if over 50). After \$15,000 must roll over into private Roth IRA
ERISA Coverage?	No	Yes	Marketplace itself is not covered but individual plans may be	No

Source: Derived from Pew Charitable Trusts (2017).

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TABLE 11.2 Advantages and disadvantages to retirement plan types

	Secure Choice (Auto-IRA)	Open MEP	Marketplace	MyRA
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• Simple and low cost</li> <li>• Employers have virtually no regulatory burden or fiduciary responsibility</li> <li>• Easy to change contribution amounts</li> <li>• Employees do not need to take action to participate and maintain complete control over their account</li> </ul>	<ul style="list-style-type: none"> <li>• Allows employer contributions</li> <li>• Higher contribution limits</li> <li>• ERISA protection</li> <li>• More likely to have additional investment and financing options</li> <li>• Lower regulatory burden for employers</li> <li>• Streamlined compliance at the state level</li> <li>• Can use auto-enrollment</li> </ul>	<ul style="list-style-type: none"> <li>• Allows the state to pre-screen retirement plans to ensure they meet certain standards</li> <li>• Can provide high quality information about retirement alternatives</li> <li>• Employers can choose their level of involvement</li> <li>• State does not have any involvement with ERISA</li> </ul>	<ul style="list-style-type: none"> <li>• Good way for new savers to get in the habit of saving</li> <li>• Simple and easy to understand</li> <li>• Limited to no risk of loss</li> <li>• No fees</li> <li>• National program is available to everyone</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>• Low contribution limits</li> <li>• No employer matches</li> <li>• Strength of employee protections depends on state law</li> <li>• Plans in different states may have different rules</li> </ul>	<ul style="list-style-type: none"> <li>• May impose higher costs and more responsibilities on employers than IRAs</li> <li>• Employer must ensure fiduciary responsibilities are handled by provider</li> </ul>	<ul style="list-style-type: none"> <li>• No direct incentive for employers to adopt a retirement savings plan (will do little to raise coverage).</li> <li>• Does nothing to simplify retirement saving or reduce regulatory burdens for small employers</li> <li>• Needs an enforcement mechanism to ensure that plans continue to be adequate</li> </ul>	<ul style="list-style-type: none"> <li>• Low maximum size</li> <li>• No real potential for contributions to grow</li> <li>• No mechanism to roll over account to a private provider once maximum size is reached</li> <li>• Uncertain political future</li> </ul>

**Secure choice (Auto IRA).** Five states (California, Connecticut, Illinois, Maryland, and Oregon) have enacted Secure Choice programs based on the Automatic IRA (see Table 11.3; Iwry and John 2009; AARP 2017). Under these plans, states sponsor a simple and low-cost plan using a payroll-deduction IRA. The programs apply to employers who offer no other retirement saving or pension plan. Employers face few regulatory burdens, no fiduciary responsibility, and no contribution responsibilities. Most employers already use either an outside payroll provider or payroll processing software, so the cost of setting up the deduction and forwarding contributions would be minimal. Employees are enrolled automatically and can opt out or adjust their contribution levels. Contributions are invested into a Target Date Fund or similar vehicle, unless employees choose to allocate funds to one of a few other basic investment options. Investment management and record keeping are contracted to a private provider. States handle fiduciary responsibilities and consumer protections.

Secure Choice plans were developed to meet the needs of small businesses and their employees. One criticism of using a payroll deduction IRA is that contribution limits are significantly lower than for 401(k) plans. In 2017, workers under 50 could contribute up to \$18,000 annually to 401(k) plans, but only \$5,500 to an IRA. Small business employees, however, are likely to have lower median earnings than those of larger firms, suggesting lower optimal targets for wealth accumulation.<sup>8</sup> In addition, the significant gap in contribution limits between IRAs and 401(k)s can reduce the extent to which the program might encourage firms to drop their existing 401(k)s in favor of a Secure Choice plan. Secure Choice plans are not covered by the Employee Retirement Income Security Act (ERISA), the major federal law regulating employee benefits. Thus the strength of employee protections in Secure Choice plans depends on state laws and may differ from the extensive protections guaranteed under ERISA.

The Illinois Secure Choice Savings Program was enacted in January 2015 and went into effect in 2018. The plan applies to all employers with at least 25 employees, who have been in business for at least two years, and who do not currently provide a qualifying savings plan. Smaller employers can voluntarily participate (Illinois State Treasurer 2016). Employees will be automatically enrolled in a Roth IRA with a 3 percent default contribution rate.

The Oregon Saves program, enacted in 2015, went into effect in 2018. The plan requires all Oregon employers either to join the state Oregon Saves plan or offer their own qualified retirement plan (State of Oregon 2017). Employees are to be automatically enrolled in a Roth IRA with a 5 percent default contribution rate.

California's Secure Choice program was enacted in September 2016 and will soon phase in. The program will require employers who have five or

TABLE 11.3 Comparison of state retirement plan actions

	California	Illinois	Oregon	Maryland	Connecticut	Washington	New Jersey
<b>Date Enacted</b>	September 29, 2016	January 5, 2015	June 25, 2015	May 10, 2016	May 27, 2016	May 18, 2015	January 19, 2016
<b>Date Implemented</b>	Bill effective January 1, 2017. Implementation in 2018 or later.	Effective June 1, 2017. Participants must be able to enroll within two years and employers have 9 months after that to set up automatic payroll deposits. Phased enrollment	Individuals were able to begin contributions from July 1, 2017	July 1, 2016	January 1, 2018	January 1, 2017	Not specified
<b>Plan Type</b>	Auto IRA	Roth IRA	Roth IRA	At least one payroll deposit IRA	Roth IRA	Marketplace containing selection of: SIMPLE IRAs, myIRAs, Auto IRAs, and/or 'life insurance plans for retirement purposes'	Marketplace containing selection of: SIMPLE IRAs, myIRAs, Auto IRAs, and/or 'life insurance plans for retirement purposes'
<b>Automatic Enrollment</b>	Yes	Yes	Yes	Yes	Yes	Not required	Not required
<b>Default Contribution Rate</b>	3% (Board can adjust from 2% to 5%), option for auto-escalation at no more than 1% per year until rate reaches 8%.	3%	5% standard rate, 1% minimum and no maximum	Not specified	3%	None Specified	None Specified

Source: Derived from Pew Charitable Trusts (2017).

more employees and who do not otherwise offer a retirement plan to automatically enroll their employees in a state-sponsored IRA overseen by the Secure Choice Retirement Savings Investment Board. The default contribution rate will begin at 3 percent of workers' payroll, with the option for the Board to implement an automatic escalation policy (automatically increasing contributions by 1 percent per year, capped at a rate of 8 percent). Funds will initially be invested in low-risk securities such as Treasury bonds, after which more investment options will be made available (California State Treasury 2017). While the low-risk investments will reduce the chance of loss, they will also make it harder for California savers to build significant retirement balances.

The Connecticut Retirement Security Program, enacted in 2016, is also now in place. The plan requires employers with five or more employees and who do not provide a retirement savings option to join the state plan. Employees will be automatically enrolled in a Roth IRA with an initial 3 percent default contribution rate (Act Creating the Connecticut Retirement Security Program 2016). A public-private oversight board, the Connecticut Retirement Security Authority, was established to oversee the implementation of the program.

The Maryland Small Business Retirement Savings Program and Trust started in 2017. The plan requires private employers who do not currently offer a retirement savings plan and who have been in business for the last two years to enroll their employees in an Auto IRA. The program is required if an employer uses an outside payroll provider or a payroll software program. Businesses that comply with the law will receive a waiver on an annual \$300 business report filing fee (Maryland General Assembly 2016). A Small Business Retirement Savings Board, which oversees the program, selects Auto-IRA plans and contribution rates.

**Marketplaces.** Two states (Washington and New Jersey) are implementing retirement savings marketplaces (see Table 11.3). A marketplace is a state-sponsored website that enables small businesses to find retirement savings or pension plans. The marketplace will display a diverse array of plans—including payroll deduction IRAs, SIMPLE IRAs, open MEPs, MyRA, and perhaps even 401(k) plans and defined benefit (DB) plans—offered by several different providers. The state pre-screens retirement plans, ensuring that the options presented to employers meet certain standards (regarding, for example, fees) and provide unbiased information about retirement plan options. Because the marketplace merely lists plan options, a state has no potential ERISA liability and does not take on any of the employer's legal responsibilities. The marketplace design enables employers to determine which type of plan best meets their and their employees' needs, including whether they prefer an ERISA-covered plan. A marketplace could be

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coupled with a requirement that employers provide coverage, as discussed in the next section. But, by itself, a marketplace does nothing to simplify retirement saving or to reduce the regulatory burdens and fiduciary responsibilities that would be placed on smaller employers.

Washington's Small Business Retirement Marketplace, enacted in 2015, became fully operational in 2017. Employers with fewer than 100 employees are eligible to participate but are not required to do so. The law permits the government to provide incentives for employers to do so. The marketplace is to contain a variety of low-cost savings options provided by financial services firms (SIMPLE IRAs and payroll deduction IRAs, for example) and investment choices, as well as access to the federal MyRA.

New Jersey enacted a marketplace plan in 2016 based on Washington's model, available to companies with fewer than 100 employees; participation is voluntary. The marketplace must offer a similar variety of low-cost savings options, at least two investment choices and access to MyRA (Bernard 2016).

**Open MEPs.** Beyond Secure Choice plans and marketplaces, states can also choose to operate an open MEP.<sup>9</sup> In 2017, Vermont approved legislation establishing an MEP, and the New York City Comptroller's office proposed a variant of an open MEP in 2016 as part of a larger retirement savings plan (Office of the New York City Comptroller 2016). Philadelphia is also considering an open MEP for that city's small businesses (City of Philadelphia Office of the Comptroller 2017). Federal regulations require employers participating in private sector MEPs to have a common bond (such as being in the same industry). By contrast, state-sponsored MEPs do not face this restriction; they may cover workers from firms without a common bond. Under an 'open MEP,' several small businesses may join together to offer a common type of account to each employer's workforce. The common plan structure reduces the compliance burden and places most fiduciary responsibilities on the plan administrator. State-sponsored open MEPs could be open to any small business in the state that wants to offer its employees a retirement plan. As with the Secure Choice model, these open MEPs would use services that are contracted out to private sector providers.

Wealth accumulation can be higher in an MEP because the plans contain higher contribution limits and employers can make contributions. MEPs are also more likely to offer loan provisions and more diverse investment choices. Both MEPs and Secure Choice plans reduce administrative costs for small employers, compared to offering a comparable retirement plan on their own. But MEPs may impose higher administrative costs and greater responsibilities on employers than IRA-based plans, since MEPs would typically offer more services and employers must meet certain fiduciary and regulatory responsibilities under ERISA. As discussed below, participation in a state-sponsored MEP would be voluntary, as states are not allowed to require employers to offer ERISA-regulated plans.

**MyRA.** Another option states could pursue would be to encourage workers to sign up for MyRA accounts, though this is now unlikely with the cancellation of the MyRA product.

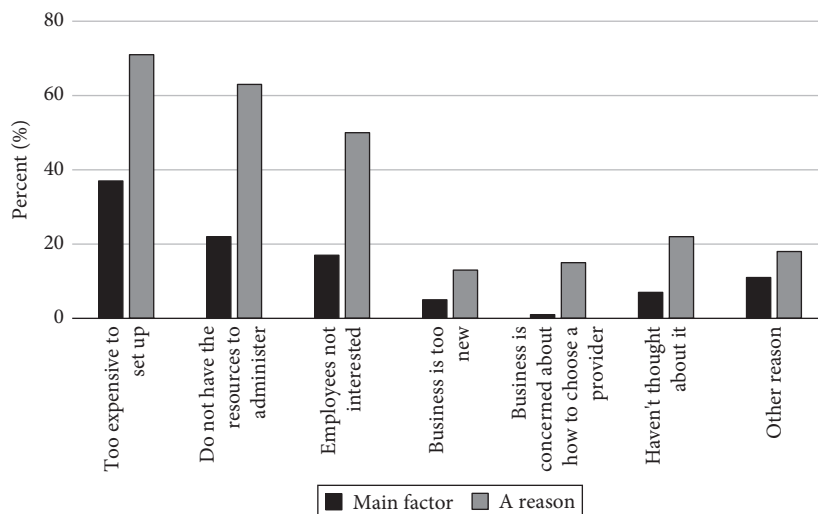
**Other state and local actions.** Over the past few years, legislation has been introduced in more than half of the remaining states (beyond those listed above) to either establish state-sponsored retirement programs, or to create a commission to study them (Georgetown University Center for Retirement Initiatives 2017). In 2017 alone, legislators in over ten states proposed legislation to enact state-sponsored retirement savings plans or create a feasibility study. In 2012, Massachusetts enacted the Connecting Organizations to Retirement Program (CORE), a voluntary 401(k) plan for non-profit firms having fewer than 20 employees, where the state controls administrative costs. States are also experimenting with different plan features. For example, West Virginia and Utah have proposed Auto IRA plans without a mandate that employers participate.

In addition, cities such as New York City, Seattle, and Philadelphia have expressed interest in creating retirement plans for local private-sector workers. New York City proposed creating a voluntary marketplace to access easy-to-use 401(k) plans, including a newly created publicly funded Empire City 401(k) MEP, SEP-IRAs, and SIMPLE IRAs. Employers who do not offer a plan on their own or through the marketplace would be mandated to enroll employees in a new NYC Roth IRA in which the first \$15,000 is invested in a MyRA account and anything above that would be put in more conventional investment vehicles (Office of the New York City Comptroller 2016). The overturning of Department of Labor (DOL) regulations that would have enabled cities to establish Auto IRAs complicates the implementation of much of this plan. Philadelphia created a working group to develop a plan, as well as a series of outreach efforts with the local community (City of Philadelphia Office of the Controller 2016). As mentioned, these efforts resulted in the recommendation that the city establish an open MEP (City of Philadelphia Office of the Controller 2017).

**Small business needs.** A key factor in designing a successful state-sponsored plan is understanding why small businesses currently do not offer plans and what reform features they support. In order for these plans to attract sufficient political support, it is imperative to have small businesses believe that a state proposal is feasible and designed to meet the needs of their workers. At the same time, each state must understand how small businesses will react to the proposal, and what proportion of employers required to offer a plan will use the state plan.

The expense and complexity of small business retirement plans are major reasons why employers fail to offer them. On an asset-weighted basis, the smallest existing private sector retirement savings plans can cost up to four

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**Figure 11.4.** Reasons small and medium-sized businesses do not offer retirement plans

*Note:* Survey data is directly from source attributed below. The study authors surveyed owners of small and medium-sized business without retirement plans in place about their views on implementing such a plan.

*Source:* Pew Charitable Trusts (2017, Figure 1).

times as much as larger plans (Steverman 2017). In a recent survey, 37 percent of small businesses that did not offer plans said that the main reason was because they were too expensive to set up. About 71 percent cited it as one of the factors contributing to their decision, as shown in Figure 11.4. Another 22 percent said the main reason was that the company did not have the resources to administer a retirement plan, with a total of 63 percent mentioning this as a reason. The focus on cost was reinforced later in the survey when small- and medium-sized business owners were asked what would motivate them to offer a retirement plan, and the answer that drew the largest support was an increase in profits, followed by the provision of a business tax credit for starting a plan (Pew Charitable Trusts 2017: 3). Interestingly, the survey found that the creation of a retirement plan with reduced administrative requirements and the availability of easy-to-understand information would have almost no effect on plan offerings, with over half of those responding saying that those factors would make them no more likely to offer a plan.

By contrast, small businesses responded positively in the survey to a mandatory retirement savings plan with features like those found in the Auto IRA, as shown below in Table 11.4. About 92 percent of small- to



TABLE 11.4 Individual features of an Auto IRA that business owners support

	‘Somewhat Support’ or ‘Strongly Support’ (%) <sup>a</sup>
Businesses’ only responsibility would be to withhold money from participating employees’ paychecks and send it to the retirement account on their behalf.	79
Businesses would not be required to contribute to the plan.	83
Businesses would not have any legal responsibility for their employees’ retirement accounts.	86
Employees who don’t have access to a retirement savings plan at their work would be offered the chance to participate in one.	92
By default, workers would contribute to the retirement savings account unless they took action to opt out of the program.	72
Employees could stop or change their contributions at any time.	92
As a starting point, participating employees would contribute a set amount of 3 percent of their paychecks to the retirement account.	79
As a starting point, participating employees would contribute a set amount of 6 percent of their paychecks to the retirement account.	69
Employees could withdraw their own contributions to the account at any point without a penalty.	82

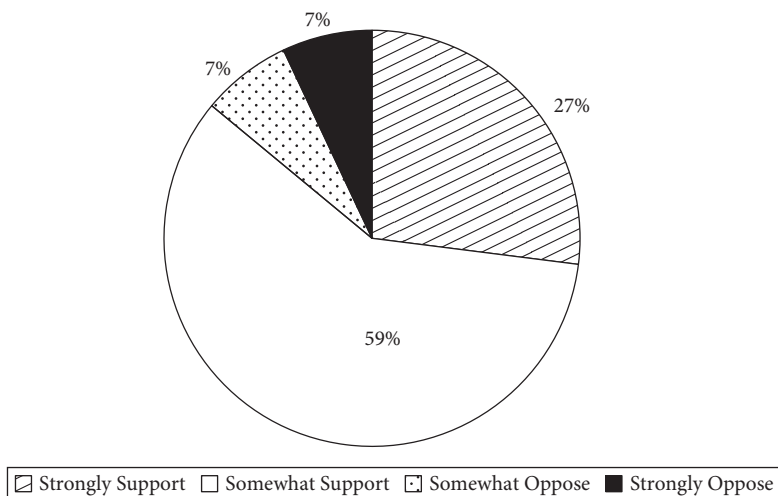
<sup>a</sup> The study authors surveyed owners of small and medium sized business without retirement plans in place about their views on implementing such a plan. For this question, employers were asked to indicate their support for features of a hypothetical retirement plan similar to an Auto IRA that would be sponsored by an outside organization and not a business like theirs.

Source: Survey data from Pew Charitable Trusts (2017).

medium-sized employers expressed some level of support for enabling employees who lacked a workplace retirement plan to participate. Further, 79 percent supported the idea that employers would only have the responsibility to withhold money from an employee’s pay and send it to the retirement account, and 83 percent supported employers not being required to contribute. Overall, 86 percent of surveyed employers expressed some level of support for an Auto IRA-based program. Yet that support was less than enthusiastic, with 59 percent ‘somewhat’ supporting, as shown in Figure 11.5.

Features of an open MEP are also popular with small- to medium-sized employers, with 88 percent of employers supporting allowing both employers and employees to contribute, and 84 percent favoring the reduced legal liability found in an open MEP (see Table 11.5).<sup>10</sup> Employers also supported a marketplace, with almost 86 percent saying that it would be helpful to improve retirement savings. Yet, this contrasted with earlier answers stating

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**Figure 11.5.** Employer attitudes toward Auto IRA plans: US firms

*Note:* Survey data is directly from source attributed below. The study authors surveyed owners of small- and medium-sized business without retirement plans in place about their views on implementing such a plan.

*Source:* Pew Charitable Trusts (2017, Figure 3).

**TABLE 11.5** Individual features of a multiple employer plan (MEP) that business owners support

	'Somewhat Support' or 'Strongly Support' (%) <sup>a</sup>
Several businesses could adopt a group retirement savings plan run by their state treasurer's office	55
Both employers and employees could make contributions	88
Employers and employees have some choice in how to invest their contributions	92
The state would handle record keeping, financial reporting, and communication for the plan	57
Employers would have reduced legal liability compared with operating their own plan	85

*Notes:*

<sup>a</sup> The study authors surveyed owners of small- and medium-sized business without retirement plans in place about their views on implementing such a plan. For this question, employers were asked to indicate their support for features of a hypothetical retirement plan similar to an MEP that would be sponsored by an outside organization and not a business like theirs.

*Source:* Survey data from Pew Charitable Trusts (2017).

that easy-to-understand information and a plan with reduced administrative requirements would make employers no more likely to start a plan.

### **Evaluating State-sponsored Plans**

The two features essential to the success of state-sponsored retirement savings plans are, first, requiring an employer to offer a retirement saving option, and, second, automatic enrollment of workers into that plan.

An effective state-sponsored plan will generate several results. In addition to raising coverage and generating high participation rates among the newly covered workers, it should also induce significant contributions, provide safe and rewarding investments, impose low fees, and induce responsible withdrawal patterns. Notably, the states that have enacted Secure Choice plans have already included provisions that address fees and initial investment choices. Several of them recognize the need for an appropriate level of contributions and have taken steps in that direction. Others have discussed responsible withdrawal options, but have recognized that this discussion must come after the plan is established.

State-sponsored plans may also reduce the amount that states and the federal government must spend in the future to support retirees with inadequate resources (Trostel 2017). For states, these savings would predominantly be due to reductions in Medicaid costs and certain housing programs. The amount of saving per state would depend on the size of the low-income population and the scope of assistance provided through public programs. Federal savings would come from reductions in demand for other means-tested programs (such as Supplemental Security Income [SSI]), as well as from the federal share of Medicaid funding.<sup>11</sup> It is also possible that state-sponsored retirement savings programs will increase state revenues. If states tax retirement income, then any increased retirement savings will eventually lead to higher revenue. In addition, higher retirement income may lead retirees to spend more money, which can result in higher sales and corporate tax revenue.

**Boosting coverage through mandatory provision.** Requiring employers to offer a plan would be the most effective way to increase coverage.<sup>12</sup> Most mandatory provision rules require that all companies offer some type of retirement savings or pension plan to their workers. Firms that offer 401(k)s or DB pension plans already meet this requirement. Those who do not would have to either establish such a plan or offer their employees access to a state-sponsored retirement savings plan. Under federal law, required coverage can only apply to an IRA-based retirement plan; states are forbidden from requiring employers to establish an ERISA-regulated retirement plan.

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There is some evidence that a state-sponsored plan without mandatory provision is unlikely to significantly increase coverage rates. For example, at the end of 2016, only about 20,000 people had enrolled in the nationwide MyRA program (Lobosco 2016). Even with much more promotion, a voluntary program is unlikely to encourage employers who are mainly concerned with running a business to open a retirement plan for their employees.

Small businesses do have concerns about state government involvement in retirement saving, expressing much stronger support for a plan sponsored and administered by a private sector provider, such as an insurance company or mutual fund, than for a plan administered by the federal or state government. As a result, employers are split almost 50–50 between those who would participate in the state-sponsored plan and those who would start their own retirement plan (Pew Charitable Trusts 2017: 8).

Nevertheless, it may be counterproductive for states to require small-to-medium businesses to offer a payroll deduction IRA or their own plan and then to leave it to the private sector to provide the plans from its usual offerings.<sup>13</sup> Such plans would initially have high prices, undermining support for the program early on, although the entry of competition in the later years could reduce prices to some extent. Therefore, pairing a low-cost state-sponsored payroll deduction plan with a mandatory provision requirement is most likely to both increase coverage and provide employees with low-cost savings vehicles.

**Boosting participation rates through automatic enrollment.** In a traditional DC plan or IRA, individuals must specifically sign up to participate, designate a contribution level, and allocate contributions to investment vehicles before they can begin saving. Under automatic enrollment, eligible workers are placed in the plan and save a pre-determined amount in a pre-set investment option unless he or she decides otherwise. Savers always have complete control and can choose at any point to opt out or change their contribution levels or investment allocations. Automatic enrollment is key to boost participation among newly covered employees. While studies in the United States and other countries show the value of automatic enrollment, adoption of the feature is currently voluntary for employers, and it is predominantly offered by larger companies.<sup>14</sup> A new United Kingdom retirement savings program offers evidence on the potential effects of a universal automatic enrollment system.<sup>15</sup> Under the UK reforms, all employers will eventually be required to offer a retirement plan that automatically enrolls workers and meets minimum contribution levels. These reforms are being phased in over several years ending in 2019, and experience with them will be valuable for understanding the potential effects of state-sponsored retirement plans. Specifically, an early evaluation of these reforms shows a substantial increase in both retirement plan coverage and

participation at all incomes, ages, genders, employer sizes, and among both full-time and part-time workers (Department for Work and Pensions 2016). Almost seven million UK workers have been automatically enrolled in retirement plans, at almost 300,000 different employers. Some 265,000 employees who opted out the first time have been re-enrolled. Participation has been very high in the UK plan, but it varies by age, working hours, and employer size (James 2017). Opt-out rates range from about 8 percent at the largest employers, to roughly 11 percent at firms with 50–99 employees; the proportion climbs to 17 percent for the smallest firms having 19 employees or fewer. About 90 percent of full-time employees participate, compared with the average of 82 percent for part-time workers. About 93 percent of employees under age 30 participate, compared to 91 percent of those aged 30–49, and only 77 percent of workers over age 50. Controlling for other factors, automatic enrollment may be responsible for a 37-percentage-point increase in overall participation (Cribb and Emmerson 2016). Automatic enrollment has been especially effective in increasing participation among younger workers, with a 52-percentage-point increase in workers aged 22–29, and 37 percent in workers aged 30–39. It also has a major effect on low-to-moderate income workers, with an increase in participation of 54 percentage points among those with earnings in the lowest earnings quartile and 46 percentage points among those in the second quartile.

These findings, combined with surveys of automatically enrolled workers in the United States, imply wide support for the mechanism even among those who have opted out. This makes a compelling case for including the mechanism in state-sponsored retirement savings plans (Retirement Made Simpler 2009).

## **Conclusion**

There is near universal agreement that pension coverage rates for American workers are lower than they could be, yet state-sponsored retirement savings plans are only just starting. Five states are implementing Secure Choice plans, one is starting an MEP, and two are implementing marketplaces, with the programs set to be fully phased in over the next few years. These numbers are expected to grow in the near future as other states consider establishing a state-sponsored plan. The most important determinants of the programs' ability to reach their full potential are straightforward: requiring firms to offer either the state plan or their own plan, and automatically enrolling workers. In principle, these two features matter more than whether the underlying account is an IRA or a 401(k). As a practical matter, however, federal regulations forbid states from requiring employers to offer

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ERISA-regulated plans, making an IRA-based state program the only option consistent with mandatory provision.

Enabling all Americans to save for retirement from the day they begin work until the day they fully retire is an idea that has been discussed for decades. The new plans being implemented offer great potential to raise coverage, participation, and retirement wealth accumulation among a broad swath of the American workforce.

### Notes

1. For example, the Obama administration included an Automatic IRA proposal in every proposed budget. The most recent Automatic IRA proposal by that administration would have required employers with more than ten employees in operation for over two years to enroll employees in a Roth IRA with a 3 percent default contribution rate. Employers with fewer than 100 employees who did so would receive a temporary tax credit of \$1,000 for up to three years in addition to an annual credit of \$25 per employee (up to \$250) for six years (Office of Management and Budget 2017). Members of Congress also proposed bills mandating employers to offer an Automatic IRA in each of the preceding six years. More recently, the American Savings Account Act of 2017 would have automatically enrolled private sector workers lacking access to a retirement savings plan into a newly created American Savings Account, similar to the Thrift Savings Plan currently offered to federal government employees. During 2017, Members of Congress also proposed legislation to decrease barriers to Open MEPs in the private sector (Retirement Security for American Workers Act 2016; Retirement Security for American Workers Act 2017) and to authorize the creation of state-sponsored MEPs (State Retirement Savings Act 2016).
2. Additional Department of Labor (DOL) regulations gave certain cities similar powers. Seattle, Philadelphia, and New York City wrote letters of interest to the DOL asking whether their 2015 ruling that cleared the way for states to enact state-sponsored retirement plans also applied to cities. DOL responded by clarifying that a political subdivision qualifies if they meet three criteria: (1) state law gives them the authority to require employers' participation in payroll deduction savings programs; (2) the political subdivision has a population that is at least the size of the least populous state (currently Wyoming, with 600,000 residents); and (3) the state in which the subdivision is located cannot already have a statewide retirement program for private-sector employees. These additional regulations were final in January 2017, but were overturned by a Congressional Review Act resolution that was passed by Congress and signed by President Trump later that year.
3. The regulations clarify that if states offer an Auto IRA under certain conditions, the plans do not fall under the Employee Retirement Income Security Act (ERISA). Although states now working on such a plan believe that the regulations

are helpful in avoiding a legal challenge, they also believe that they have legal authority under earlier, less explicit laws and regulations.

4. A study by Segal Consulting estimated that if all states sponsored a retirement savings program, taxpayers would save \$5 billion over the first decade in Medicaid costs and that these savings would continue to increase over time. Fifteen states have the potential to save over \$100 million each over the first decade (Segal Consulting 2017).
5. The Current Population Survey measured coverage between 1987 and 2013. After 2013, the survey was redesigned and the accuracy of its later results has been questioned. For this reason, we do not include data after 2013.
6. Participation and coverage information presented in this section is adapted from a Government Accountability Office (GAO) (2015) analysis of data from the Census Bureau's Survey of Income and Program Participation (SIPP). We define retirement plan coverage (synonymous with access) as being an employee aged 18 or older who works for an employer who provides a retirement plan and is eligible for that plan. Since the GAO does not report trends in coverage, we use data from Copeland (2014). This Employee Benefit Research Institute (EBRI) report presents Current Population Survey data on retirement plan participation and coverage over time for workers aged 21 to 64.
7. EBRI defines 'having a retirement plan' as having an IRA, DB, or DC plan. The value of assets reported contains all investments except for the value of the respondent's primary residence and DB plan assets. Although workers without an employer-based plan can contribute to IRAs, very few do.
8. In California, research shows that employees without access to a retirement plan have a median income of \$23,000 (Overture Financial 2016).
9. MEPs can be either open or closed. Under a closed MEP, all businesses that enter the plan must have some common interests (such as being in the same industry). An open MEP has greater flexibility in the types of business that it includes. All MEPs considered by the states are open MEPs because they allow any business that employs residents of that state to join.
10. While the employers like the ability to contribute if they so choose, they also do not want to be required to do so. This is reflected in the Auto IRA question.
11. These estimates assume that the retirement plans being examined increase the retirement income of low-income workers such that they would not qualify for public assistance programs. It also assumes that the individual does not need those supports before retirement and that retirement savings do not fall under the program's maximum allowed asset level. This last assumption is especially questionable as, under current federal law, the only program that completely exempts retirement assets from its asset test is the Supplemental Nutritional Assistance Program (SNAP).
12. Whether this requirement applies to all employers in the state or only to employers with more than a certain number of employees is a political decision.
13. Similarly, the United Kingdom found that relying on competition alone to reduce fees and create effective retirement products would not be effective as

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- many employers would not have enough information to choose a provider that offered good value. See Office of Fair Trading (2013).
14. See, for example, Madrian and Shea (2001) and Chetty et al. (2013).
  15. A key difference is that the United Kingdom is phasing in the contribution level. Initially, employers and employees only contribute 1 percent of earnings each. This 2 percent total initial contribution is close to the usual 3 percent initial contribution in the United States. By April 2019, that will climb to a total of 8 percent of earnings. Also, the UK system exempts lowest income workers and does not collect contributions on the first £113 of weekly earnings.

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