Universal Retirement Accounts (URAs): Enhancing Income Security by Supplementing Social Security

Executive Summary

While America suffers from a growing partisan divide on many critical issues, views on retirement income security are another matter altogether. Surveys show that 88% of Americans agree the nation faces a retirement savings crisis, a level of concern that is high regardless of gender, income, age and party affiliation. Gallup polls consistently find that retirement security is the nation's number one financial worry. A May 2018 poll reported a rising level of concern, despite the strong economy, "with almost half of those not yet retired – 46% – projecting they won't be financially comfortable when they retire." While down from 55% in 2012, the share of Americans who fear their retirement income will be insufficient has trended steadily upward since Gallup began tracking this measure in 2002.

America's *real* retirement security crisis is not just Social Security solvency or the many big companies freezing or terminating their traditional pension plans. A more systemic problem is that the majority of American workers do not participate in *any* retirement saving plan—whether pension or 401(k) or Individual Retirement Account (IRA). Employer-sponsored plans cover fewer than half of all private sector workers. Coverage and participation rates are strikingly lower among workers who are low-income, young, work part-time, or work at small firms. Pension funds are how America saves, but only half the nation is equipped to do so.

The resulting dependence on Social Security's safety-net level of income is unfortunate and unsustainable. Nearly two-thirds of current beneficiaries rely on Social Security for a majority of their income. More troubling is that more than one-third (36%) rely on the program for 90% or more of their income – a dependency ratio that is far higher for widows (over 45%). This reliance on Social Security is likely to increase further as fewer retirees receive guaranteed income from traditional defined-benefit accounts, relying instead on voluntary, contributory accounts that are not available on an automatic, payroll-deduction basis to half the workforce.

The most promising and potentially bipartisan path to facilitating sufficient retirement saving by *every* American worker is to leverage the existing Social Security system to add an individual, voluntary and supplemental savings account for every American. Today's private pension system works well for workers who have consistent access to a plan and choose to save. But for the majority who do not – or who are between jobs that do – the NRLN proposes creating a Universal Retirement Account (URA). Every working American needs career-long access to both a potent tax incentive to save; and automatic payroll deduction into a portable, professionally-managed retirement account whether or not his or her current employer sponsors a pension plan. This can be done at modest cost to the Treasury and in a manner that takes the burden of pension benefit administration off of small- and medium-sized firms.

The fact that so few workers save regularly in IRAs reinforces research showing that it is not primarily access to a savings account that spurs participation and asset building, but rather what we call the four "I's": Inclusion, Incentives, Infrastructure and Inertia. Universal Retirement Accounts (URAs) – created and tied automatically to each Americans' Social Security number – will best promote saving by incorporating these overall design principles:

- ***Inclusion*:** Enroll every working adult not currently eligible to participate in a qualified employer-sponsored plan – including part-time, contract and contingent workers – as well as the self-employed

and workers who choose to supplement defined-benefit plans, while making contributions voluntary on the part of employees (via opt-out) and employers.

- ***Inertia*:** Although individuals can opt-out, ***default options*** can convert myopia into productive inertia through automatic enrollment and payroll deduction, automatic asset allocation, automatic escalation, automatic rollovers, and automatic annuitization.
- ***Incentives*:** A tax incentive for saving in a URA can be made more inclusive—and targeted toward lower-income earners who find it most difficult to save—by expanding the Savers Credit, making it refundable and more generous matching contribution for low-wage workers, and depositing it directly into the individual's account.
- ***Infrastructure*:** URAs would leverage existing practices to: enable every worker to save by automatic payroll deduction; facilitate career-long portability through a SSA clearinghouse function (to receive and direct contributions); enable choice among certified private pension managers (to professionally invest on a pooled basis); and maintain a low-cost default option for new, small or dormant accounts (managed by, e.g., the federal Thrift Savings Plan).

URAs can promote seamless, career-long accumulation of supplemental saving by combining the following basic elements:

- ***A portable URA account*** is opened for every person, tied to their Social Security number, which facilitates career-long accumulation, tracking and, at retirement, a monthly annuity payment on top of the traditional Social Security benefit.
- ***Automatic Enrollment***: Wage earners who are *not* eligible to participate in their employer's qualified DB or DC plan are automatically enrolled, unless they affirmatively opt out.
- ***A refundable Savers Credit*** as a matching contribution deposited directly into the URA should apply to at least the first $2,000 saved each year; contributions would be from taxable income, but tax-free on withdrawal (Roth tax treatment).
- ***The employers' role*** would be limited to forwarding contributions by automatic payroll deduction along with FICA withholding and, voluntarily, to making contributions on behalf of workers (on either a flat-dollar or flat-percentage basis).
- ***A SSA Clearinghouse*** function would receive, record, and direct all contributions to the selected investment manager; an appointed ***oversight board*** would report back to Congress.
- ***Private institutional pension managers*** (e.g., money managers) will be certified and compete to be selected by individuals initially and during an annual window period; the federal Thrift Savings Plan can serve as the default manager for small, unprofitable accounts.
- ***Other Default Features***: While participation is voluntary, unless a worker opts out, enrollment (at 3% or 4% of pay), investment (a life-cycle fund), escalation (e.g., increasing the contribution rate 1% each year up to 6-8%), rollovers (balances from plans not otherwise directed to an IRA), and annuitization (at or after retirement age) are automatic.

A system of **Universal Retirement Accounts linked to Social Security** can ensure that every worker has at all times a seamless, portable way to save, invest, and enhance their monthly benefit at retirement. Smaller employers can also use URAs as an easy alternative to sponsoring a private plan. URAs with robust inclusion, incentives, infrastructure and inertia would make saving for retirement considerably more universal, automatic, adequate and equitable.

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Universal Retirement Account (URAs):
Enhancing Income Security by Supplementing Social Security

By Michael Calabrese

America's *real* retirement security crisis is not just Social Security solvency or the many big companies freezing or terminating their traditional pension plans. A more systemic problem is that the majority of American adults do not participate in *any* retirement saving plan—whether pension or 401(k) or Individual Retirement Account (IRA). Employer-sponsored plans cover fewer than half of all private sector workers. Coverage and participation rates are strikingly lower among workers who are low-income, young, work part-time, or work at small firms. Pension funds are how America saves, but only half the nation is equipped or adequately incented to do so.

The result of excluding half the nation from an automatic, managed and subsidized private saving plan is that too many individuals are heading toward retirement age with little more than Social Security's safety net. Nearly two-thirds of current beneficiaries rely on Social Security for a majority of their income. More troubling is that more than one-third (36%) rely on the program for 90% or more of their income – a dependency ratio that is far higher for widows (over 45%). The average benefit was $1,400 per month in 2018, not very much more than the federal poverty level. Because retirees with low career earnings, or substantial time out of the workforce, receive minimal Social Security benefits, the Urban Institute estimates that about 36 percent of the elderly received benefits in 2009 that fell below the individual poverty line.[1] This reliance on Social Security is likely to increase as fewer retirees receive guaranteed income from traditional defined-benefit accounts, relying instead on voluntary, contributory accounts that are not available on an automatic, payroll-deduction basis to half the workforce.

The most promising and potentially bipartisan path to facilitating sufficient retirement saving by *every* American worker is to leverage the existing Social Security system to add an individual, voluntary and supplemental savings account for every American. Today's private pension system works well for workers who have consistent access to a plan and choose to save. But for the majority who do not – or who are between jobs that do – the NRLN proposes creating a ***Universal Retirement Account*** that will accumulate saving to supplement the traditional monthly Social Security benefit.

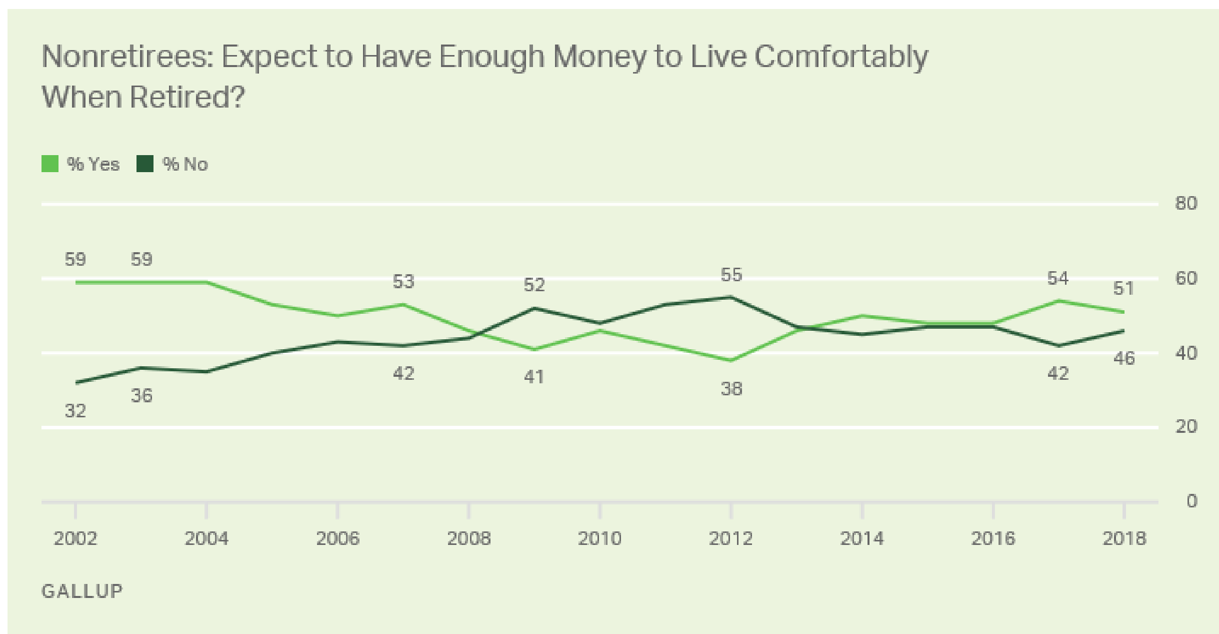
A Universal Retirement Account (URA) would function like a universal 401(k) plan that gives *every working American* access to automatic payroll deduction and a professionally administered retirement savings plan whether or not their employer sponsors a qualified pension plan. In all cases URA accounts would supplement – and not supplant – the existing private pension system and the baseline monthly benefit received through Social Security. A URA system would be voluntary, but with a set of default options that 'nudge' workers to save, invest

[1] *See* Melissa Favrauelt,"Why Do Some Workers Have Low Social Security Benefits?" The Urban Institute (2010).

smart and annuitize their career-long accumulation. This can be done at modest cost to the Treasury and in a manner that takes the burden of pension benefit administration off of small- and medium-sized firms.

I. America's Retirement Saving Crisis

While America suffers from a growing partisan divide on many critical issues, views on retirement income security are far more uniform. Surveys show that 88% of Americans agree the nation faces a retirement savings crisis, a level of concern that is high regardless of gender, income, age and party affiliation. Gallup polls consistently find that retirement security is the nation's number one financial worry. A May 2018 poll reported a rising level of concern, despite the strong economy, "with almost half of those not yet retired – 46% – projecting they won't be financially comfortable when they retire." While down from 55% in 2012, the share of Americans who fear their retirement income will be insufficient has trended steadily upward since Gallup began tracking this measure in 2002.



Gallup polls show a steadily rising concern about the risk of inadequate levels of retirement saving.[2]

Quite simply, pensions are how Americans save. With over $28 trillion in assets, traditional pension trusts and 401(k)-style saving plans account for the vast majority of financial assets accumulated by households – as well as a vital source of patient capital for American business. An analysis of the most recent (2016) Federal Reserve data on household wealth shows that as defined contribution plans have replaced defined benefit plans, assets in individual account plans have become "the predominate source of financial assets for American families holding these assets." The Employee Benefit Research Institute found that individual account (IA) assets represent 68% of total financial assets, at the median, among households with at least one DC, IRA or Keogh account.

Because most household saving accumulates in IAs, the retirement savings crisis is a twofold problem: At any given time, fewer than half of all working people are saving and many of them are not saving enough. While views differ on what income replacement rate is "adequate" (e.g., whether it's closer to 70% or 85%), and how precisely to measure the nation's retirement saving gap, there is no question that tens of millions of working-age

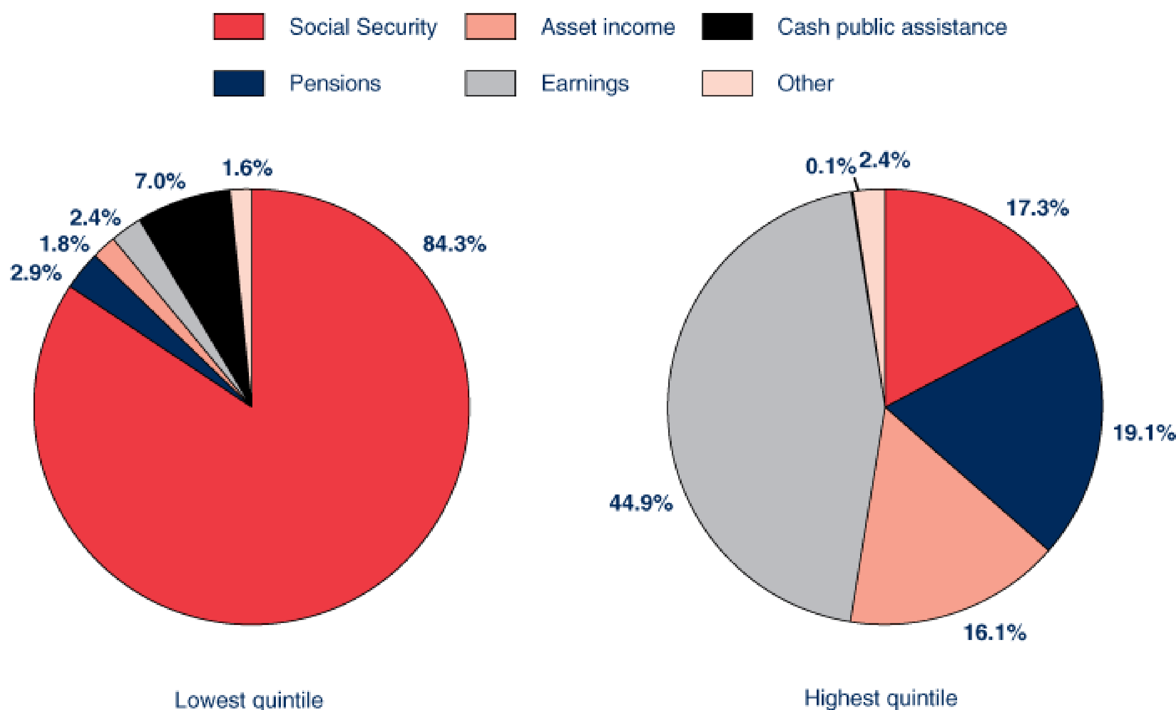
[2] *Source:* Frank Newport, *Gallup News,* "Update: Americans' Concerns About Retirement Persist" (May 9, 2018), available at https://news.gallup.com/poll/233861/update-americans-concerns-retirement-persist.aspx.

adults, including one-third or more of those over age 50, are not accumulating nearly enough financial assets to maintain their standard of living in retirement.

Social Security replaces only 41% of a median worker's pre-retirement – and that's assuming he or she works full time until age 67.[3] Economist Teresa Ghilarducci, relying on Federal Reserve data, calculated that while households with a defined-benefit pension were on track to a 75% replacement rate, on average, those relying only on IAs were on track to 62% replacement rate, and households with no pension saving plan at all were on track to replace only 57% of pre-retirement income.[4] As Ghilarducci notes, middle-income earners are hit hardest by this saving shortfall because Social Security benefits replace a higher share of income for low earners. She observes that just to reach a 70% replacement rate, "career-long earners of $100,000-plus will need to replace about 46% of their pre-retirement earnings" with retirement savings since Social Security only replaces 24% at best.

Not surprisingly, the lowest-earning 40 percent of working adults are accumulating very little in the way of financial assets. Elderly in the lowest income quintile receive on average only about 5 percent of their income from either pension or asset income. And because retirees with low career earnings, or substantial time out of the work force, receive minimal Social Security benefits, the Urban Institute estimates that about 36 percent of the elderly received benefits in 2009 that fell below the individual poverty line.[i] Among those over 65 in the top 20 percent by income, earnings provide the largest (and growing) source of income (45%), while income from pensions and other assets is about 35 percent.

Shares of aggregate income for lowest and highest income quintiles by source, 2010 (SSA)



Overall, the lack of consistent, career-long saving for retirement has left half the nation at risk of outliving their assets. One measure, the National Retirement Risk Index (NRRI), indicates that a majority (51 percent) of working-age households are "at risk" of not having enough retirement income to maintain their pre-retirement level of consumption. As of 2015, this represented a cumulative $7.7 *trillion* "retirement income deficit" for households

[3] Ghilarducci, *Rescuing Retirement*, at p. 26.
[4] Ghilarducci, *Rescuing Retirement*, at p. 27.

in their peak saving years (the 32-64 age range), according to the Center for Retirement Research.[5] The World Economic Forum reported that the U.S. ranks below the international median for retirement income adequacy. WEF estimated the U.S. had a $28 trillion retirement savings gap as of 2015 that will also grow steadily to as much as $137 trillion by 2050 as our population ages and lives longer.[6]

II. Limitations of the Current Employer-Based Pension System

The transformation of the American private pension system over the past 25 years from traditional, employer-paid defined benefit plans (DBs) to predominantly voluntary, contributory plans has widened the nation's retirement saving deficit. As we've turned into more of a do-it-yourself 401(k) nation, several flaws in the employer-based system have been exacerbated. The most salient of these shortcomings is the reality that employer-sponsored plans – DC and DB together – cover only about half the private sector workforce, leaving more than 60 million employed adults without an easy, automatic, incentivized and professionally-managed plan to facilitate saving throughout a career.

The Shift from True Pensions to a 401(k) Nation

Today's retirement saving crisis results from a failure to update our industrial-era pension system. America's postwar pension system has been a great success in many important respects. From 1945 to the late 1970s, the percentage of private-sector workers covered by pension plans grew rapidly from 20 percent to just above 50 percent. The working and middle classes became shareholders and, with Social Security, accumulated the foundation for a secure retirement. Pension funds also steadily became the world's largest pool of "patient capital," boosting U.S. growth and innovation by underpinning the world's most sophisticated, liquid, and dynamic capital market.

When the landmark Employee Retirement Security Act (ERISA) became law in 1974, its fiduciary, funding, vesting and other provisions were designed to perfect what was then a system of employer-sponsored defined-benefit plans. These were true pensions: Employers made the contributions and shouldered the investment risk, managing pooled trusts subject to government oversight at relatively low cost. Workers—at least those who clocked more than 20 hours per week—were automatically covered and received, at retirement, guaranteed monthly income for life. Combined with Social Security, workers who remained at a firm with a DB plan for 30 or more years replaced well over half of their pre-retirement income.

This industrial-era system was based on assumptions of career-long job tenure, stable corporate structures, pressure from strong unions, and large doses of employer paternalism—conditions, like traditional DB plans themselves, that have been rapidly disappearing over the past two decades. Since the first 401(k) plan emerged out of an unintended tax loophole in 1981, the share of private sector workers participating in defined benefit pension plans fell from 38% to 15%, according to the U.S. Bureau of Labor Statistics. Today the U.S. is a 401(k) nation. More than two-thirds of private-sector workers lucky enough to have any pension benefit work at firms that sponsor only a 401(k)-type contribution plan.

Four Problems with Sole Reliance on Today's Employer-Based System

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[5] NRRI represents the present value of the saving and investment shortfall needed to ensure, on average, retirement security for every American. *National Retirement Risk Index*, Center for Retirement Research at Boston College, available at http://crr.bc.edu/special-projects/national-retirement-risk-index/.

[6] "We'll Live to 100 – How Can we Afford it?" World Economic Forum, White Paper (May 2017), available at http://www3.weforum.org/docs/WEF_White_Paper_We_Will_Live_to_100.pdf.

Even as 401(k)s and other DC plans emerged as the dominant plan type, the nation's fundamental approach to promoting retirement saving has not changed. It continues to rely entirely on voluntary plan sponsorship by employers who are offered tax carrots in the form of deductions that disproportionately benefit high-wage earners and are subject to regulatory sticks—ERISA antidiscrimination, fiduciary, and reporting requirements—that, however well-meaning, discourage small employers in particular from helping their employees save. And even if the overall share of workers participating in an employer-sponsored plan had not declined so substantially, the shift from DBs to a do-it-yourself 401(k) nation has served to exacerbate flaws inherent in relying on private employers to ensure retirement security.

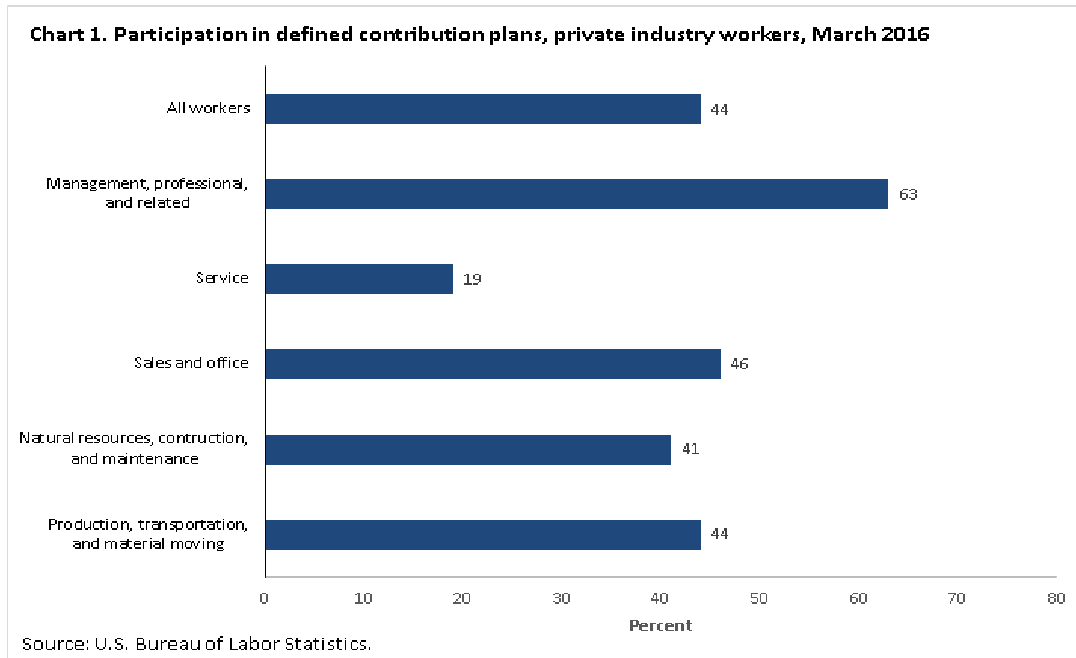
1. ***Inclusion: Coverage is partial and excludes non-traditional workers***

The most glaring gap in the private pension system is inclusion. Employer-sponsored plans cover only half of all private sector workers, leaving more than 60 million workers—including a disproportionate share of young, low-income, part-time and small business employees, as well as the self-employed—without an easy, automatic, incentivized and professionally-managed infrastructure to facilitate saving throughout a career.

Only about 44% of all private-sector workers age 25-to-64 participated in an employer-sponsored 401(k) or other defined contribution retirement plan in 2016,[7] a striking decline from the 50.3 percent participation rate in 2000.[8] (See Chart 1 below.) Only 55.4% of workers in their prime saving years (age 45 to 64) participate in any workplace retirement plan. The percentage of private sector workers whose employer even sponsors a plan (whether or not they are eligible or participate) fell to 53.2% in 2008. One result is that roughly one-third of all households accumulate no pension plan saving during their entire work life and end up relying almost exclusively on Social Security.[9]

While participation is somewhat higher among full-time workers (51%), participation rates are also strikingly lower among workers who are low-income, young, work part-time, or work at small firms. Approximately 85 percent of Americans without a pension benefit at work shared one or more of these four characteristics, according to a General Accounting Office study. Minorities also participate at substantially lower rates, primarily because they are less likely to work at a firm that sponsors a pension or 401(k)-type plan.[10]

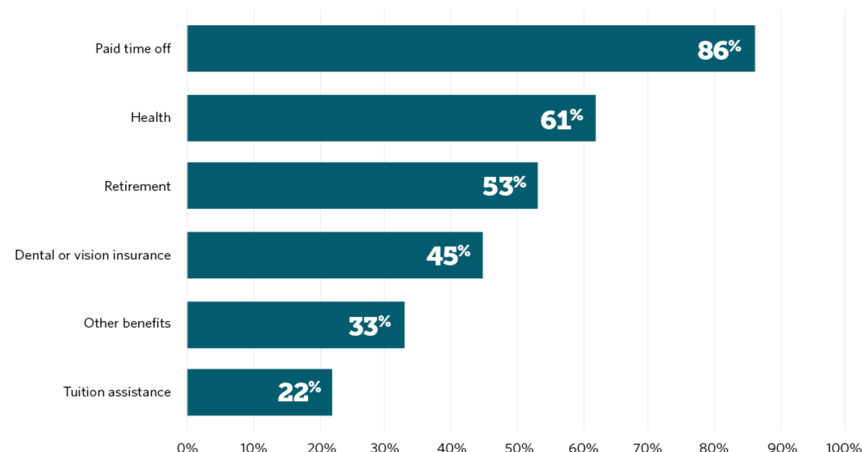
[7] Bureau of Labor Statistics, U.S. Dept. of Labor, "Beyond the Numbers," Vol. 5, No. 17 (Dec. 2016).
[8] *See* Patrick Purcell, "Pension Sponsorship and Participation: Summary of Recent Trends," Congressional Research Service (Sept. 2009). CRS estimates are based on the U.S. Census Bureau's *Current Population Survey* (CPS). Largely because of the decline of defined-benefit plans, which automatically covered employees averaging more than 1,000 hours per year, participation rates are substantially lower than at the late 1970s peak; in 1979, 51 percent of wage and salary workers age 25-64 participated in a plan. *See* Alicia Munnell and Laura Quinby, "Pension Coverage and Retirement Security," Center for Retirement Research, Issue in Brief No. 9-26 (Dec. 2009).
[9] Alicia Munnell and Laura Quinby, "Pension Coverage and Retirement Security," Center for Retirement Research, Issue in Brief No. 9-26 (Dec. 2009).
[10] *See* Alicia Munnell and Christopher Sullivan, "401(k) Plans and Race," Center for Retirement Research, Issue in Brief No. 9-24 (Nov. 2009), at p. 11.



Not surprisingly, pension coverage is lowest among workers whose savings would truly *add to* net national saving: workers who earn less than the median wage. Even if a lower-wage worker is inclined to save, fewer than 40 percent of private sector workers in the bottom income quartile work for a firm that sponsors a retirement plan, while 72 percent of top quartile earners work at firms offering qualified plan coverage, typically a 401(k) with employer matching contributions.[11] Not surprisingly, occupation makes an enormous difference in whether a worker has a retirement saving plan at work. According to BLS data in Chart 1 just above, "In 2016, 63 percent of management, professional, and related workers (relatively high-paying jobs) participated in defined contribution plans, compared with 19 percent of service workers (relatively low-paying jobs) who participated."[12]

Overall, the largest groups of workers without access to a payroll-deduction savings plan at work are the tens of millions not considered to be full-time payroll employees. At least one in four U.S. workers are in non-standard work arrangements (part-time, temporary and contract workers) that rarely include pension coverage. The two largest categories are part-time workers (25 million) and the self-employed (15 million in 2016).[13] Another 5.9 million workers are classified as temporary or otherwise "contingent," making them ineligible for pension plan participation (which is often a reason they are contingent). While these categories overlap somewhat, roughly 40 million workers in these categories are excluded by definition (and under ERISA) from the private pension system. Another 15 million Americans are self-employed. Many are doing quite well and fund Keogh accounts. But most are lower-income or less sophisticated and save little or sporadically. While the "gig economy" may be good for business productivity and flexibility, it makes the current payroll-based pension system increasingly inadequate.

[11] *Id.*, at p. 13. CPS data show that 73 percent of private sector workers in the highest earning quartile worked for an employer sponsoring a qualified plan, compared to only 59 percent among third quartile earners and 38 percent among workers in the lowest earning quartile.
[12] Bureau of Labor Statistics, "Beyond the Numbers," *supra*, at 2.
[13] https://www.bls.gov/news.release/empsit.t08.htm While ERISA requires that some part-time workers are eligible to participate in qualified plans because they have averaged more than 1,000 hours (roughly 20 hours per week) for more than one year, the majority are typically excluded.



2. ***Portability: Saving and accumulation is not continuous and subject to leakage***

A second, related problem is the lack of pension ***portability***. Labor market mobility is increasing and job tenure is steadily decreasing. The typical worker will change jobs seven or more times after age 25. Even if a worker has coverage today, he or she may not have access to a plan next year in a new job. And even if the worker's new employer sponsors a plan, in most plans new hires are not eligible to participate (or at least not receive contributions) for at least one year. Although a majority of private sector workers are at firms that sponsor a plan, at any given time millions of other employees at firms sponsoring plans are not eligible to participate. The most common reason is the one-year waiting period that most plans impose on new hires.

Over a career the combination of changing jobs, one-year waiting periods, and jobs without a pension plan results in many gaps in coverage and incentives for saving. And although a long-tenured worker in a traditional pension plan will vest in monthly income for life (or a lump sum), those who terminate in less than five years can end up with no retirement accumulation at all for that period.[14] The matching contributions offered in many 401(k) plans similarly vest over a period of years.

Trends in job tenure exacerbate these saving gaps. Although saving early in one's career has the biggest impact on adequacy (because investment returns compound over time), workers under 45 change jobs far more often than older workers. A longitudinal study by the Bureau of Labor Statistics (BLS) found that workers changed jobs 11 times on average between age 18 and 44.[15] BLS concluded that although the length of employment

[14] ERISA allows employers sponsoring DB plans to deny short-tenured employees any benefit accrual at all by choosing between "cliff" vesting and "graded" vesting. Under cliff vesting the participant must become 100% vested in their benefit earned to date after no more than five years. Under graded vesting after two years of service a participant must become vested in 20% of benefits earned to date for each additional year (e.g., 20% after three years, 40% after four years) until reaching 100% after seven years.

[15] Even between the ages of 28 and 44, the typical worker had an average job tenure of just four years. Bureau of Labor Statistics, "Number of Jobs Held, Labor Market Activity, and Earnings Growth Among the Youngest Baby Boomers: Results from a Longitudinal Survey," News Release (Sept. 10, 2010). *See also* "Employee Tenure in 2008," U.S. Bureau of Labor Statistics, News Release, USDL 08-11344, Sept. 26, 2008 (suggesting a typical 25-year-old will work for seven or more employers by age 65).

increases with age, "these baby boomers continued to have large numbers of short-duration jobs even at middle age."[16] Indeed, since 1980, the largest drop in median job tenure has been among males in their prime saving years. According to BLS data compiled by EBRI, median tenure for males 55 to 64 years old dropped from 15.3 years in 1983 to 10.4 years last year.[17]

3. *Tax Incentives: Deductions are neither targeted nor equitable*

The tax break for retirement saving is one of Washington's most expensive programs. The net cost of uncollected federal tax revenue due to the tax deduction for contributions to DC and DB retirement saving plans will exceed $250 billion in fiscal year 2019, according to the Congressional Joint Committee on Taxation.[18] (See Chart below.) Cost aside, the problem is that tax incentives for saving are not targeted to stimulate net new saving by the lower half of the income distribution who save far too little.

Quite simply, the incentives for retirement saving are upside down. More than two-thirds of the tax subsidies for retirement saving flow to the most affluent 20 percent of taxpayers— and more than one-third of those subsidies to the top 5 percent of earners—but extremely little (7 percent) goes to encourage saving by the lowest-earning 40 percent of households.[19] (See the second Chart below). The reason is simple but too often overlooked: a program subsidized by tax deductions, rather than by refundable tax credits, offers little incentive for the lower-earning half of the workforce.

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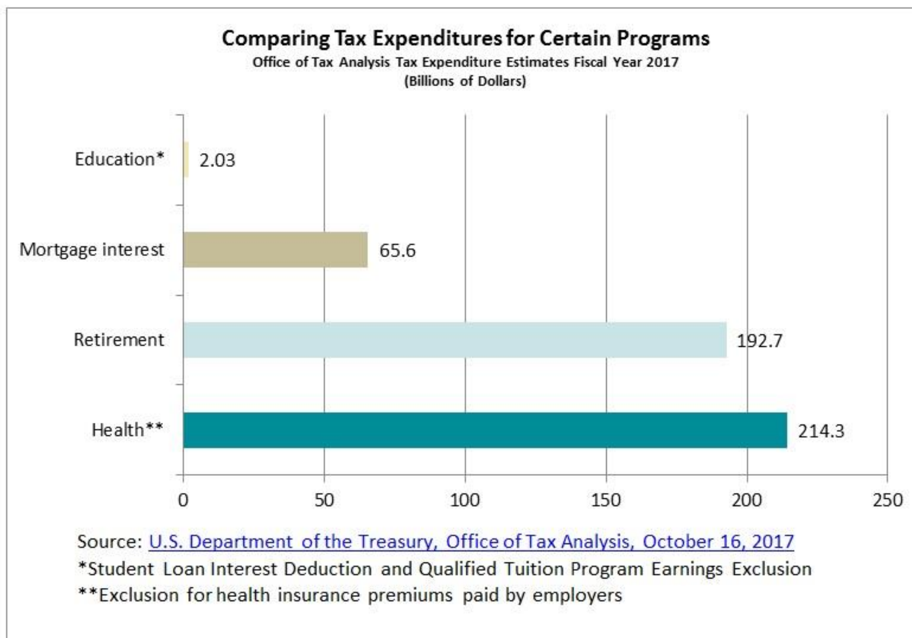
[16] Bureau of Labor Statistics, 2008. The second largest shortening in median job tenure was among males age 45 to 54 (from 12.8 to 8.5 years over the same period).

[17] Craig Copeland, "Employee Tenure Trend Lines: 1983-2010," Employee Benefits Research Institute, *Notes*, Vol. 31, No. 12 (2010), at p. 3. EBRI's longitudinal study of a large sample of 401(k) plan participants has also shown that consistent participation in a plan yields far larger average account balances than the norm. *See* Jack VanDerhei, "What Does Consistent Participation in 401(k) Plans Generate?" Employee Benefits Research Institute, Issue Brief No. 349 (2009).

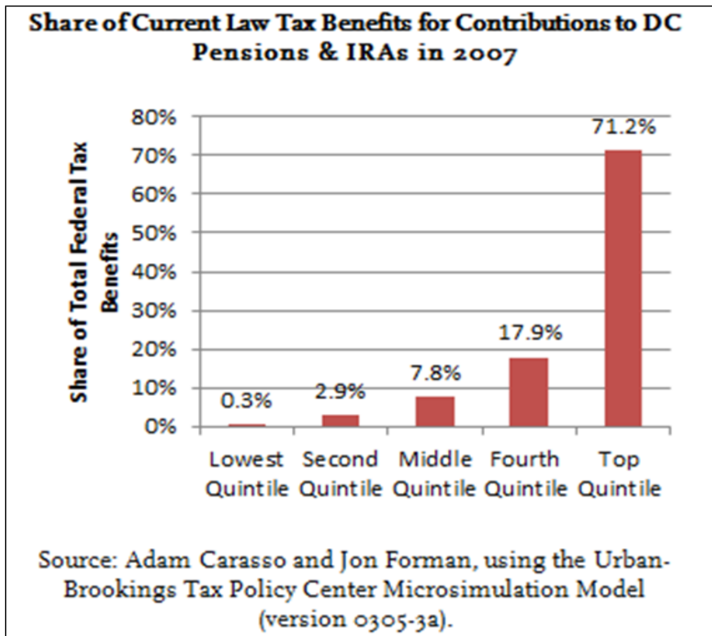
[18] Joint Committee on Taxation (JCT), U.S. Congress, "Estimates of Federal Tax Expenditures for Fiscal Years 2017-2021" (May 25, 2018), available at https://www.jct.gov/publications.html?func=startdown&id=5095. Estimates by the U.S. Treasury are somewhat lower due to a difference in methodology, as the chart just below indicates. For 2017, Treasury estimated net pension tax expenditures cost $192.7 billion, while the JCT estimated the cost at $206.6 billion. *See* U.S. Dept. of the Treasury, Office of Tax Analysis, "Tax Expenditures" (Oct. 16, 2017), available at https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2019.pdf.

[19] Congressional Budget Office, *The Distribution of Major Tax Expenditures in the Individual Income Tax System*, Pub. No. 4308, at p. 15 tbl. 2 (2013), *available at* http://www.cbo.gov/sites/default/files/cbofiles/attachments/43768_DistributionTaxExpenditures.pdf. *See also* Carasso, A., Forman, J. 2007. A more recent estimate of the distributional effects of ending tax incentives for retirement saving concluded that the highest-earning quintile receives 79.6 percent of the total net benefit and that the overall revenue saved could fund a refundable tax credit for equal to $781 for every taxpaying adult and $391 for every dependent child under age 17. *See* Eric Toder, et al., "Distributional Effects of Tax Expenditures," Tax Policy Center (2010), available at https://sites.lsa.umich.edu/katherinelim/wp-content/uploads/sites/287/2015/08/411922_expenditures.pdf.



Under current law, qualified retirement saving reduces taxable income, a deduction that reduces the tax liability of a top-bracket taxpayer by 37 cents for each dollar saved. In contrast, a tax deduction for saving is worth zero to the more than 45 million low-earning taxpayers who have payroll tax liability but who don't have any income tax liability to offset. Even median-income families in the 10 and 15 percent income tax brackets receive a weak subsidy compared to the 35 or 37 percent subsidy rate that applies to individual earning over $200,000 a year. In contrast, the effect on higher-income workers—who would likely save anyway—is primarily a shifting of assets from taxable to tax-deferred accounts.

The lack of a substantial tax benefit for middle- to low-income earners also impacts the inclination of firms to sponsor a plan. Even very large companies with a predominantly low-wage workforce – the Walmarts and McDonalds among employers – have little incentive to sponsor a plan for workers who (a) receive little or no financial benefit from a tax deduction, and who (b) without a strong incentive would prefer a higher wage now to an employer contribution for retirement. In contrast, large high-wage employers use retirement plans to steer tens of billions of dollars in pension tax subsidies to their employees every year. If, instead, contributions by both workers and firms were matched by a refundable tax, workers would be far greater, rather than less so.



4. ***Adequacy and Longevity: DC plans typically lack features to 'nudge' robust saving***

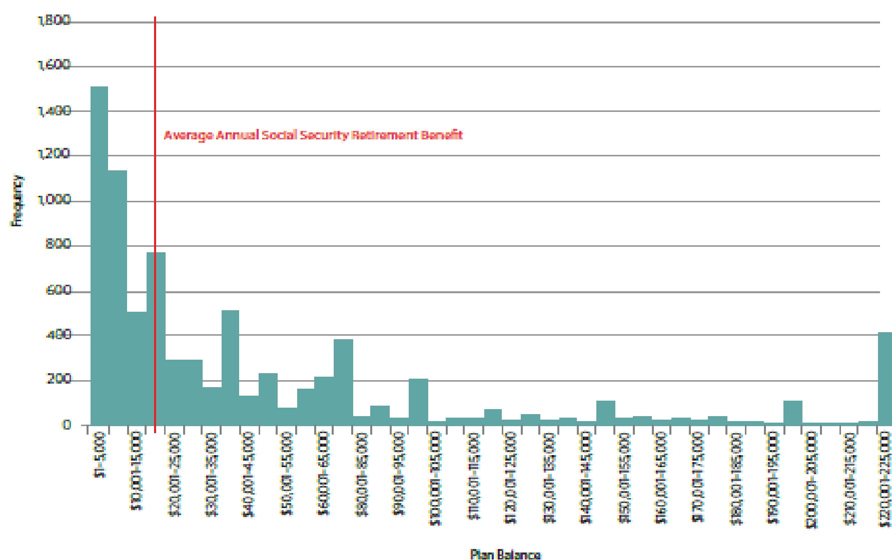
Even among those workers who are currently participating in a 401(k) or other defined contribution plans, saving is not continuous enough, accumulations are not large enough, and lump-sum withdrawals in retirement are often depleted too quickly, exacerbating the risk of outliving assets. Even an essentially voluntary saving system like the Auto-IRA needs to design in a set of "nudges" strong enough to push the typical middle- to lower-income worker toward a higher contribution rate (6 to 12 percent or more), reinforced by the incentive of additional matching contributions (from both tax credits and employer contributions), and converted as a default into a secure stream of income for life.

We might expect the workers lucky enough to participate in 401(k)-type plans to be accumulating significant savings. Sadly, that is not the case except among the subset of high earners with steady access to a 401(k). As the Chart below illustrates, the median plan balance for all workers is just $22,000; and 40% of workers with a defined contribution plan have saved less than the average annual Social Security retirement benefit ($16,146).[20] More worrisome, workers approaching retirement age are not accumulating enough saving to generate adequate income throughout retirement. According to a Congressional Research Service analysis of Federal Reserve survey data, the median value in 2007 of all retirement accounts owned by households headed by persons 55 to 64 was $100,000. For a 65-year-old man, $100,000 would be sufficient to purchase a level, single-life annuity paying out $700 per month for life (based on interest rates in 2009). Because women have longer average life expectancies, a 65-year-old woman could generate annuity income of only $650 per month.[21]

Not surprisingly, 401(k) participation and accumulation rates among workers in the bottom 60% of the earning distribution are far lower. Even among longer-tenured 401(k) participants in their 50s and 60s who are

[20] The Pew Charitable Trusts, "Employer-Sponsored Retirement Plan Access, Uptake, and Savings," Chartbook (Sept. 2016), at p. 10.
[21] Patrick Purcell, Congressional Research Service, "Retirement Savings and Household Wealth in 2007," Report for Congress 7-5700 (April 8, 2009).

earning between $40,000 and $60,000 the median account balance was just over $81,000 in 2009, according to the EBRI/ICI 401(k) database.[22]



Source: Pew analysis of U.S. Census Survey of Income and Program Participation, 2016
© 2016 The Pew Charitable Trusts

Another reason that participation rates have declined, particularly among lower-income earners, is the simple fact that 401(k) plans are voluntary and typically require workers to make investment decisions they may feel unprepared to make. Unlike traditional DB pensions, with 401(k)-type plans individuals must *choose* to save. Unfortunately, the incentives are often not nearly compelling enough, particularly for low-income workers who, unlike high-income earners, receive little if any tax subsidy for saving.

In sum, for workers with access to either a DB or DC plan, America's employer-based private pension system provides powerful saving incentives—both tax breaks and employer contributions—as well as the convenience and discipline of automatic payroll deduction. Too many are still not saving enough, but at least they have a vehicle. The NRLN believes the greatest need is for a type of Universal 401(k) that can provide a similar set of infrastructure, incentives and positive saving inertia for those who lack access, including the growing numbers (more than 40 million currently) who are part-time, contract, contingent or self-employed workers.

III. Universal Retirement Accounts: Portable, Career-Long Saving for All

The fact that so few workers save regularly in IRAs reinforces research showing that it is not primarily access to a savings account that spurs participation and asset building, but rather what we call the four "I's": Inclusion, Incentives, Infrastructure and Inertia. Universal Retirement Accounts (URAs) – created and tied automatically to each Americans' Social Security number – can most effectively promote sufficient saving among *all* workers by incorporating these overall design principles:

[22] Jack VanDerhei, Sarah Holden and Luis Alonso, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2009," Employee Benefits Research Institute, Issue Brief No. 350 (Nov. 2010), at pp. 20-21.

- ***Inclusion*:** Enroll every working adult not currently eligible to participate in a qualified employer-sponsored plan – including part-time, contract and contingent workers – as well as the self-employed and workers who choose to supplement defined-benefit plans, while making contributions voluntary on the part of employees (via affirmative opt-out) and employers.

- ***Inertia*:** Although individuals can opt-out, ***default options*** can convert myopia into productive inertia through automatic enrollment and payroll deduction, automatic asset allocation, automatic escalation, automatic rollovers, and automatic annuitization.

- ***Incentives*:** A tax incentive for saving in a URA can be made more inclusive—and targeted toward lower-income earners who find it most difficult to save—by expanding the Savers Credit, making it refundable and more generous matching contribution for low-wage workers, and depositing it directly into the individual's account.

- ***Infrastructure*:** URAs would leverage existing practices to: enable every worker to save by automatic payroll deduction; facilitate career-long portability through a SSA clearinghouse function (to receive and direct contributions); enable choice among certified private pension managers (to professionally invest on a pooled basis); and maintain a low-cost default option for new, small or dormant accounts (managed by, e.g., the federal Thrift Savings Plan).

Basic Elements of a Universal Retirement Account System

A URA system can promote seamless, career-long accumulation of supplemental saving by combining the following basic elements:

- ***A portable URA account*** is opened for every American, tied to their Social Security number, which facilitates career-long accumulation, tracking and, at retirement, a monthly annuity payment on top of the traditional Social Security benefit.

- ***URA accounts are owned by each individual:*** Although coordinated with Social Security, the financing of the two programs would be kept separate. Like an IRA, URA accounts are owned by the individual who contributes and is available throughout the person's lifetime.

- ***Automatic Enrollment***: Wage earners who are *not* eligible to participate in their employer's qualified DB or DC plan are automatically enrolled, unless they affirmatively opt out.

- ***A refundable Savers Credit*** as a matching contribution deposited directly into the URA should apply to at least the first $2,000 saved each year; contributions would be from taxable income, but tax-free on withdrawal (Roth tax treatment). Like the current Savers Credit, the credit could be made available only to low-to-median earner households, or could be available to everyone but with a lower match for higher earners (for example, 25% or 50%).

- ***The employers' role*** would be limited to forwarding contributions by automatic payroll deduction along with FICA withholding and, voluntarily, to making contributions on behalf of workers (either a flat-dollar or flat-percentage amount for each worker up to a maximum, such as 5% of pay).

- ***A Clearinghouse*** function within the Social Security Administration (or IRS) would receive, record, and direct all contributions to the selected investment manager.

- ***Private institutional pension managers*** (e.g., money managers) will be certified and compete to be selected by individuals initially and during an annual window period; the federal Thrift Savings Plan can serve as the default manager for small, unprofitable accounts.

- ***Other Default Features***: While participation is voluntary, unless a worker opts out, enrollment (at 3% or 4% of pay), investment (a life-cycle fund), escalation (e.g., increasing the contribution rate 1% each year up to 6-8%), rollovers (balances from plans not otherwise directed to an IRA), and annuitization (at or after retirement age) are automatic.

- ***An appointed Board of Trustees*** would oversee the program, certify pooled investment managers, and report back to Congress as directed in the authorizing legislation.

It is important to acknowledge that there will be substantial trade-offs and budget implications depending on the details of the components listed above. Eligibility for the refundable tax credit match and contribution limits are examples. Making those choices is best left to Congress, but in the interest of clarity, a few of the most critical elements of the framework deserve further explanation.

1. *A Clearinghouse to Enable Portability and Lower Costs for Employers and Investment Managers*

A great benefit of 401(k) plans is the convenience, discipline and protections provided by automatic payroll deduction and professional asset management. Employers typically contract with an investment firm and, through automatic payroll deduction, forward all contributions each pay period to that entity. Similarly, the Social Security Administration can house a critical piece of the "plumbing" needed to achieve universal saving, while also minimizing costs for employers, by serving as a Clearinghouse that initially receives, records, tracks and ultimately directs contributions on behalf of each worker to the investment manager of his or her choice. Every employer (except possibly those with fewer than five employees) can readily include URA contributions along with the income taxes, payroll taxes (FICA), and unemployment taxes (FUTA) that are withheld each pay period and forwarded to the U.S. Treasury either monthly or semi-weekly.[23]

A Clearinghouse function within SSA (or, if not, IRS) is also well positioned to receive deposits directly from individuals not able to contribute through an employer by automatic payroll deduction. This could include the self-employed, contract workers and others who are not subject to income tax and payroll tax withholding. This could also be the conduit for workers at very small employers (e.g., under five employees) to the extent they are exempted from the program.

One way to facilitate saving from workers without payroll deduction is the sort of automatic monthly bank draft authorization (ACH) that tens of millions of Americans use to automatically pay utility bills and even to make installment payments on overdue taxes. IRS can use the annual Form 1040 tax form to ask taxpayers if they would like to designate a bank account for an automatic monthly debit into their URA. To further encourage contributions, Congress should include provisions that make it easy for the self-employed and others not subject to withholding to add saving deposits to their quarterly income tax payment and filing. In addition, all taxpayers should be able to direct all or a portion of an IRS tax refund into their URA.

[23] *See* Internal Revenue Service, Depositing and Reporting Employment Taxes, available at https://www.irs.gov/businesses/small-businesses-self-employed/depositing-and-reporting-employment-taxes.

Another set of reasons for a clearinghouse involve continuity, leakage and lost accounts. The leading Automatic IRA proposals all envision the employer establishing an account for each new employee at a financial institution of the *employer's* choice. While this is familiar as the way firms administer 401(k) plans, it creates a number of long-term problems as employees change jobs multiple times. Median job tenure has varied between 4.1 and 4.4 years in recent years. And even among older workers, average job tenure is nearly 50 percent less than it was before 1990 (8.5 years among workers 45 to 54, and 10.4 years for age 55 to 64).[24]

Finally, because the SSA Clearinghouse is tracking the contributions and balances associated with every URA, it could readily add an account summary to the annual Social Security benefit statements available to all workers (although only mailed currently to those over 60, since SSA discontinued mailing statements to all workers in 2017). Integrating the statements – and projecting the combined benefit based on a worker's age, income, URA balance and current level of saving – would be another helpful way to make sure every American knows whether they are on track to meet their retirement income goals. And when a worker decides to claim Social Security, the Clearinghouse is also in the best position to calculate the supplemental annuity payment, based on the retiree's URA balance, and deposit it along with the individual's standard benefit each month, as noted above.

2. *Pooled, Low-Cost Investment Funds Managed by Private Institutional Money Managers*

One great advantage of URAs is the potential to achieve higher investment returns at lower costs than the typical IRA or small-firm 401(k) can achieve. The URA model can offer workers a choice among competing institutional money managers, but do so in a way that achieves the economies of scale and long-term investment horizon that allows low costs and higher investment returns more comparable to those achieved by defined-benefit pension plans. Since URAs will collectively accumulate total assets comparable to the very largest public and private pension plans, the system can select and regulate a choice of private institutional[25] money managers who, like DB pension managers, will have the scale and long-term time horizons needed to achieve the highest average returns at the lowest costs. Investments would be pooled (similar to a pension plan or diversified mutual fund), with the default allocation between equity and fixed-income products determined by age and proximity to retirement (a life-cycle fund, as noted above).

Workers who lack access to an employer-sponsored plan typically rely on Individual Retirement Accounts set up through their local bank or a mutual fund company. Even if they pay substantial fees for professional investment advice, individuals rarely have accounts large enough to achieve the lowest fees or access to top-flight expertise and less-liquid investments, such as private equity. As pension economist Teresa Ghilarducci and Blackstone Group President Tony James detail in their book *Rescuing Retirement*, "IRAs and 401(k)s simply do not perform well enough. Fees are too high and typical portfolios poorly diversified.

Ghilarducci and James propose a similar universal saving plan, which they call a Guaranteed Retirement Account. In making the case for a requiring pooled investment funds offered by competing and regulated institutional money managers who would have a fiduciary duty solely to account holders. They cite three advantages. First, lower fees: As benefits consultancy Aon Hewitt concluded, "[t]he annual savings from transitioning from retail to institutional shares may be as high as 65 basis points (0.65 percent) per year."[26] This

[24] Employee Benefit Research Institute, "Employee Tenure Trend Lines, 1983-2010," Notes, Dec. 2010, at p. 3.
[25] Teresa Ghilarducci and Tony James, *Rescuing Retirement: A Plan to Guarantee Retirement Security for All Americans*, Columbia University Press (2018), at p. 61.
[26] Aon Hewitt Investment Consulting Inc., "Customize DC Investments for Participant Success" (July 2015), available at http://www.aon.com/attachments/human-capital-consulting/custom-dc-investments-for-participant-success-wp-july2015.pdf.

may not sound like much, but over 30 or 40 years the average individual investor could save and retire with tens of thousands more dollars in assets if they paid the low fees paid by big pension funds.

Second, Ghilarducci and James note that large institutional funds gain access to top-tier portfolio managers who compete to generate returns 3% or more higher than those achieved by individual investors.[27]

Third and they say most significantly, because pension managers know the most of the fund's assets will not be withdrawn for decades, unlike the mutual funds that fill most IRA and most 401(k) accounts, they are free to diversify into less-liquid, higher-return asset classes reserved for investors with long-term investment horizons. "These include high-yielding and risk-reducing alternatives such as real estate, private equity, venture capital, and hedge funds."[28] For example, the National Association of State Retirement Administrators found that over a 25-year period through 2017, public pension funds (which manage over $4.2 *trillion* in assets) delivered an 8.1% annual median rate of return, far higher than the 2-to-4% return characteristic of IRAs and 401(k)s.[29]

Another important piece of the 'plumbing' for the URA system is a default administrator for small, unprofitable accounts, as well as for savers who do not select a specific private investment manager. The Federal Thrift Savings Plan (TSP), which manages very low-cost 401(k)-style saving accounts for five million current or former federal military and civilian personnel, could take this on at very low cost.[30] The TSP currently oversees the investment of $500 billion in saving by current and retired federal employees, which it contracts out to private investment firms. Congress should task the TSP to coordinate with the SSA Clearinghouse to likewise manage new, very small and unprofitable URAs until such time as the owner selects a private pension fund manager.

3. *A Voluntary System with Strong Default Features*

Central to the Auto-IRA is the concept of converting myopia into positive inertia by making participation the default option for everyone. Studies have shown that automatic enrollment boost 401(k) participation rates as high as 95 percent—when there is also an employer match—and to 80 percent among low-income workers. However, as we know from today's inadequate saving in 401(k)s, participation alone does not result in the saving and investment behaviors associated with achieving an adequate and guaranteed stream of retirement income for life.

Although URAs would be voluntary, additional default policies should be designed in, including a significant initial contribution (4-to-6% range), automatic escalation (up to 8-to-10% over a period of years), an age-appropriate investment allocation, rollover deposits (from former employer plans), and automatic annuitization up to at least a certain multiple of Social Security (to insure against outliving other assets). Taken together, these robust default features will make it far more likely the typical workers retire with guaranteed monthly income as large and secure as it should be.

Automatic Enrollment: Surveys show that in large 401(k) plans adopting automatic enrollment, participation rates have increased by about 30 percentage points compared to pre-automatic enrollment levels.[31] For URAs, employers would withhold and submit to SSA the default contribution (e.g., 3 or 4% initially) unless an individual worker affirmatively opts out. An additional way to boost the impact of automatic enrollment is to renew

[27] *Ibid*.
[28] Ghilarducci and James, *supra*, at 62.
[29] National Association of State Retirement Administrators, "NASRA Issue Brief: Public Pension Plan Investment Return Assumptions," Issue Brief (Feb. 2018), at p. 2. Public plans returned a median 5.9% annually over the 10-year period ending Dec. 31, 2017 – due to the great recession that began in 2008 – and 8.7% over the 30-year period beginning in 1988.
[30] *See* Thrift Savings Plan, TSP: 30 Years of Service, available at https://www.tsp.gov/thirty/.
[31] Lucas, L., Hess, P., Peterson, C. 2011.

it every two years. A worker who opts out when first hired may have a different perspective after being on the job for two years. At a minimum, this sends a reminder and a message that they should be saving – and prompts them to consciously reassess whether to participate.

In contrast, there is considerable disagreement concerning the initial default contribution rate. Among defined-contribution plan sponsors that have adopted automatic enrollment, most use a default contribution rate of 3 percent and some even less. This is most likely because the Pension Protection Act 2006, when it authorized automatic enrollment for DC plans, cited a range of 2 to 4 percent when it authorized. There is also concern that a new hire may be more likely to opt out if the rate is high. However, as the *Wall Street Journal* opined in a page one report on automatic enrollment, for workers without savings vehicle, 3% is far too low to achieve even basic retirement income adequacy.[32]

Automatic Escalation: Automatic enrollment at low initial rate (3% or 4%) is a good example of how default features must work together to reinforce participation and adequate saving. If Congress authorizes a low initial rate, then it should also ensure a robust automatic escalation feature that automatically increases an individual's contribution, over a number of years, up to a rate likely to achieve retirement income adequacy. Absent automatic escalation, inertia works against adequate saving rates since too many workers leave that low default rate in place indefinitely. They may even mistakenly believe that their employer is defaulting them to the "appropriate" saving rate.

The right balance between encouraging participation and adequacy is a tricky one. Nonetheless, if we intend the "default" rate to be interpreted by participants as expert advice about smart savings behavior, then a 6% default rate would seem minimal. A 2010 study by EBRI and the Defined Contribution Institutional Investment Association found that, depending on income level, between 54% to 73% of employees would fall short of saving enough money to replace at least 80 percent of their pre-retirement income level if they enrolled in their companies' 401(k) plans at the default-contribution rate and were auto-escalated by 1% a year to a maximum of 6%.[33] EBRI concluded that among the various factors, increasing the limit on employee contributions has the greatest impact on overall saving.

Although there is a legitimate fear that new hires may opt out, the extra accumulation from a 6 percent contribution rate would be worth what appears to be a very small risk for two reasons. First, 6 percent is the average self-selected contribution by a 401(k) participant even at lower income levels.[34] Second, if a participant takes affirmative action to change their default status, they can simply reduce the contribution rate (to 3 percent or whatever they wish) rather than opt out entirely. Even with escalation of 1% or 2% per year, it would take years to push the contribution rate up to the 10-to-12 percent level that is considered minimally adequate, creating a savings deficit in the meantime.

Automatic Asset Allocation: Ideally, as explained further below, contributors to URAs will select among competing investment managers based on their performance in managing a pool of assets rather than presented with a menu of stock and bond funds, as most 401(k)s and IRA participants experience today. If the private institutional investors managing URA assets are given the benefit of the scale and long-time horizons that characterize defined-

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[32] Ann Tergesen, "401(k) Law Suppresses Saving for Retirement," *The Wall Street Journal* (2011).

[33] Jack VanDerhei and Lori Lucas, "The Impact of Auto-enrollment and Automatic Contribution Escalation on Retirement Income Adequacy," Employee Benefit Research Institute, Issue Brief No. 349 (2010).

[34] In large part this reflects the impact of employer matching contributions, which most commonly match 50% of the first 6% of pay contributed by the employee. In the context of an Auto-IRA, a worker earning $33,000 would need to save 6% of pay ($2,000) in order to receive the full benefit of a refundable Savers Credit match set at a rate of 1:1. This effort would add a total of $4,000 (12% of pay) to the worker's account.

benefit investment management, fees will be substantially lower and rates of return substantially higher. This is explained further below.

If individuals are allowed to choose firms offering a menu of stock and bond funds, as most do today in workplace DC plans, in URAs, workers who do not affirmatively choose how to allocate their assets among different investment options should be defaulted to a life-cycle fund, sometimes called a target-date fund, that diversifies and allocates among equity and fixed-income investments based on age (and hence proximity to retirement). A default allocation is important since too often employees – or workers on their behalf – are prone to choose overly conservative investments with little risk of capital loss, such as money market funds and stable value funds, to minimize the risk of losses.[35] Financial analysts uniformly agree that retirement assets should be invested with a long time horizon—and that money market or stable value funds that barely offset inflation sacrifice the compounding of interest and earnings on saving that is critical to achieving an adequate accumulation over the life course.

Automatic Rollovers: Millions of workers who participate in employer-sponsored plans for a portion of their career retire without any pension income or assets. The reason is that roughly half of all lump-sum distributions to workers changing jobs or otherwise terminating their employment are not rolled over into an IRA or another retirement plan. Census survey data on lump sum distributions between 2000 and 2006 indicated that only 46% rolled over the entire amount, accounting for 73% of the dollars distributed since larger accumulations were far more likely to be rolled over. The opportunity cost of this leakage is substantial. The Congressional Research Service estimates that due to compounding and the young age of most workers not rolling over distributions, cash-outs between 1980 and 2006 could have paid those who did not roll them over $220 in monthly income for life by age 65 (assuming an average return equal to AAA-rated corporate bonds).[36]

With a central clearinghouse and notional "career accounts" established for every worker, the default for all non-directed distributions from an employer-sponsored plan—including those of less than $1,000—can be deposit into the worker's URA. To help staunch this leakage, ERISA requires employers to deposit distributions between $1,000 and $5,000 into an IRA on the worker's behalf, unless the employee directs otherwise. Employers would thereby avoid the burden of opening IRAs for ex-employees; and even uninformed or disinterested workers would at some point learn that this automatic rollover is being invested on their behalf in one consolidated and consistent account.

Automatic Annuitization: At retirement age, the default payout option should be in the form of an annuity—guaranteed monthly payments—to ensure that retirees do not outlive their assets. For example, currently a 65-year-old male will live 18 more years on average, but also has a roughly 20% chance of living to age 90 or older. In a 401(k) nation, too many older workers share a natural inclination to underestimate the level of assets they must maintain to avoid outliving their assets.

URAs should include a default and incentives to encourage and facilitate annuitization, which is one of the great (and disappearing) advantages of a defined-benefit plan. If an account holder has substantial assets, the default might apply only to the assets necessary – when combined with Social Security – to pay a monthly benefit

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[35] The Pension Protection Act of 2006 amended ERISA Section 404(c) to give plan sponsors that choose to adopt automatic enrollment and default investment allocation the same insulation from fiduciary liability for investment losses that generally apply to participant-directed investments in qualified DC plans. However, just as employers are not required to adopt default enrollment, they can also choose an overly conservative default investment allocation.

[36] Patrick Purcell, "Pension Sponsorship and Participation: Summary of Recent Trends," Congressional Research Service (2009).

for life equal to an adequate share of pre-retirement income (e.g., 80%). Another role for a central clearinghouse could be to aggregate demand for purchasing lifetime income contracts. Annuity contracts could be bid out to one or several private insurers or other financial institutions, as DB plan sponsors do when they purchase Guaranteed Investment Contracts.

URAs could also make lifetime income options more appealing. Currently relatively few retirees choose to purchase annuities, but that could change considerably through the combination of a default option and innovative lifetime income options. Annuity options that could be made available include partial annuities, trial annuities and longevity annuities. A longevity (or deferred) annuity is a type of partial annuity that begins to distribute payments only after the retiree reaches an advanced age, such as 80 or 85. Allocating a portion of accumulated assets for this form of longevity insurance is particularly useful in preparing for potentially catastrophic long-term health care costs late in life.[37]

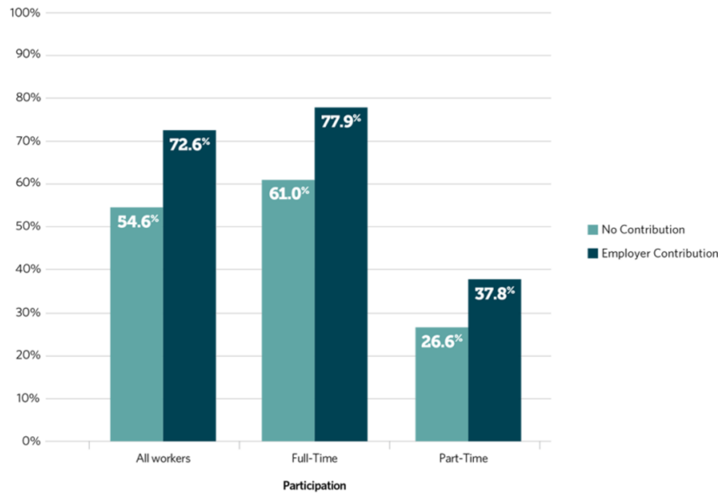
As a default option, the combination of a trial annuity and partial annuitization appears promising since it would give any retiree who does not opt out a familiarity with fixed monthly income payments without locking them in. For example, the Retirement Security Project at Brookings has proposed that a substantial portion of assets in 401(k)-type plans "be automatically directed (defaulted) into a two-year trial income product when retirees take distributions from their plan, unless they affirmatively choose not to participate."[38] At the end of the trial period, retirees could choose among several options—including opting for a lump sum, or annuitization of all or just a portion of their nest egg. If they made no choice they'd default into a life annuity. "This would put inertia to work on behalf of the income stream rather than on behalf of the lump sum," according to the Brookings proposal.[39] A trial annuity could be the default option for URAs, giving individuals who did not opt out the longevity insurance traditionally associated with a DB plan.

4. *Refundable Tax Credit Matching Contributions*

While automatic enrollment will boost participation, in a voluntary system the overall rates of contribution and accumulation will not come close to reducing the retirement saving gap without a tax incentive that is strong and relevant to lower-income earners. As explained earlier, a tax deduction is at best a weak incentive to the lower-earning half of the workforce – that is, to those families who struggle hardest to save. A refundable tax credit would operate just like an employer match in a company 401(k) plan, especially if it is deposited into the account (and not refunded, as the current Savers Credit is).

Just as most employers match contributions to 401(k) accounts, the government should match voluntary saving by providing a refundable tax credit that would be deposited directly into the worker's account. Studies show that workers are far more likely to save if given generous matching credits (see Figure below) – and once they develop the habit of saving by payroll deduction, most continue even when the match rate is reduced. For example, Census data indicates that 60 percent of eligible low-income workers choose to participate in their employer's 401(k) plan.[40] Although these workers receive little if any tax subsidy from an income tax deduction, the employer's matching deposit itself is a powerful inducement since they would be forfeiting compensation by not participating.

[37] Youngkyun, P. 2011.
[38] William Gale, Mark Iwry, et al., "Increasing Annuitization in 401(k) Plans with Automatic Trial Income," The Retirement Security Project, Brookings Institution (2008).
[39] Ibid.
[40] Nadia Karamcheva and Geoffrey Sanzenbacher, "Pension Participation and Uncovered Workers," Center for Retirement Research, Issue Brief No. 10-13 (2010).



Eligibility for the matching credit could be defined a number of ways. One option would be to limit the credit to individuals or married couples below an earnings threshold, as the Savers Credit does currently. For example, individuals earning below $30,000 might receive a 100% matching credit, while those earning up to $60,000 receive a 50% credit. An alternative approach would be to make the same total tax credit available as a direct deposit to *all* savers (including potentially savings in workplace DC plans), but require a greater saving effort by higher income earners.

An example of a sliding-scale credit that targets a stronger saving incentive at those less likely and less able to save could be structured as follows:[41]

Income Range (AGI)	Match Ratio	Matched Limit	Maximum Credit	Credit Rate	Tax Treatment
$5,000-$30,000	1:1	$2,000	$2,000	100%	Roth IRA
$30,001-$60,000	1:2	$4,000	$2,000	50%	Roth IRA
$60,001+	1:4	$8,000	$2,000	25%	Roth IRA

At left, an individual earning less than $30,000 could receive a $1 per $1 (1:1) matching credit on her first $2,000 in savings; in contrast, workers in families earning above that level (up to $60,000) could receive a $0.50 per $1 (1:2) matching credit on their first $4,000 in savings; and taxpayers with even higher incomes (above $60,000) could receive a $0.25 per $1 credit (1:4). This is also equitable, as it gives every taxpayer an opportunity to receive the maximum credit.

5. *Boosting Adequacy with Employer Contributions and Higher Limits*

As noted above, the employer's role in facilitating URAs would be limited to withholding and remitting contributions by payroll employees who are not eligible to participate in the employer's own qualified DB or DC retirement benefit plan. This would be a marginal cost, since virtually every firm today uses an automated payroll

[41] The author initially made this proposal in testimony to the House Committee on Education and the Workforce. Calabrese, M. 2000. p. 6. There should ideally be a phase-out range at each income level, as there is currently for the Savers Credit (which phases down to a 10% credit).

withholding application or service (such as ADP). The employer would forward those contributions by automatic payroll deduction along with FICA withholding and, voluntarily, to making contributions on behalf of workers (either a flat-dollar or flat-percentage amount for each worker up to a maximum, such as 5% of pay). Employer contributions should be taxable as income, but tax free when withdrawn at retirement age, receiving the same Roth IRA treatment as employee contributions.

Subject to certain conditions, allowing employers to contribute on behalf of their employees is a win-win for firms and employees alike. It would grow workers' savings more rapidly while giving employers the option to provide a pension benefit without the burden of administering an ERISA-regulated pension plan. Employers should have the flexibility to decide from year to year whether to contribute to their workers' accounts. Some firms would choose to do so as a type of year-end, profit-sharing bonus depending on performance. Many would offer a matching contribution, as firms typically do in a 401(k), which would also be subject to a limit (such as 5% of pay).

The sort of nondiscrimination testing that complicate 401(k)-type plans would be unnecessary if employer contributions are limited to a flat percentage of wage income, or a flat dollar amount, and made on behalf of *all* payroll employees, including part-time workers. Without such a requirement, employer contributions might undermine ERISA nondiscrimination rules aimed at ensuring that employers are not using the tax subsidies to favor only their higher-wage employees.

A related and final design issue relates to contribution limits. Auto-IRA proposals, such as the one proposed by the Obama administration, fall short by restricting contributions to today's meager IRA limits ($5,500 or $6,500 for workers over age 50). While this may be as much as we can realistically expect, low-income workers to save in a year, most middle-income workers—of whom there are tens of millions who lack access to a 401(k), SIMPLE or other employer-sponsored plan—simply cannot hope to achieve retirement adequacy with their saving restricted at this level. Moreover, higher-income earners can contribute $18,500 of their own wages to a 401(k) or similar DC plan (and $6,000 more if they are age 50 or older). Including the employer's contribution, the limit is $55,000 in 2018. For a worker in the top income tax bracket (37%), this translates into a tax subsidy of $6,845 at the lowest limit up to as much as $20, 350 (for those able to contribute to the combined limit).

There has been a concern that IRAs and other non-workplace plans will undermine the incentives for business owners to sponsor a qualified 401(k) or SIMPLE plan. There is, of course, an entire industry that has developed around managing and investing employer-sponsored DCs. To the extent that Congress wants to favor employer-plan sponsorship, one way to balance these concerns is with a contribution limit that is between today's IRA and SIMPLE limit (which is $10,500). An individual limit in the neighborhood of $8,500 would still leave business owners with the incentive to "graduate" up to the higher SIMPLE or 401(k) limits if they personally wish to save more. The reality, however, is that for a variety of reasons, a very substantial number of new, small and even medium-sized employers will not sponsor a qualified plan and may welcome the ability to facilitate an adequate level of saving by their employees—and even to contribute to those accounts if it could be done at their discretion and with minimum regulation.

CONCLUSION

America's *real* retirement security crisis is that the majority of American workers do not participate in *any* retirement saving plan—whether pension or 401(k) or Individual Retirement Account (IRA). The resulting dependence on Social Security's safety-net level of income is unfortunate and unsustainable. A system of **Universal Retirement Accounts (URA Accounts) linked to Social Security** can ensure that every worker has at all times a seamless, portable way to save, invest, and enhance their monthly benefit at retirement. Smaller employers can also use URAs as an easy alternative to sponsoring a private plan. URAs with robust inclusion, incentives, infrastructure and inertia would make saving for retirement considerably more universal, automatic, adequate and equitable. This can be done at modest cost to the Treasury and in a manner that takes the burden of pension benefit administration off of small- and medium-sized firms.

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[i] Melissa M. Favreault, "Why Do Some Workers Have Low Social Security Benefits?" The Urban Institute (2010); see also Melissa M. Favreault, "Workers with Low Social Security Benefits: Implications for Reform," The Urban Institute, Retirement Policy Program, Brief Series No. 29 (2010).