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State Retirement Reform: Lifting Up Best Practices

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Executive Summary

American workers are facing a retirement crisis. Almost half of workers do not have any type of retirement account at work. Those who do have access through their employer are likely to have a 401(k)-type account, which leaves workers vulnerable to leakages when they change jobs, inappropriate portfolios, and high fees. As a result, the current retirement savings system leaves a large portion of the American workforce without a consistent, secure, and efficient way to save for retirement.

At a time when federal support for even modest proposals to increase retirement coverage and savings are being rolled back, states are moving forward – fast. Since 2011, 40 states have either proposed or enacted bipartisan measures to allow private sector workers in their state access to retirement savings accounts.

While the pace of proposals is a reflection of both the need for reform and the political will to act, the short timeframe has yet to deliver outcomes or evidence upon which to evaluate differing reform ideas. As momentum increases at the state level, proposals initiated first have served as models for other legislators eager to tackle the retirement crisis in their own states. For example, out of 40 states active on the issue, current proposals reflect only four major policy vehicles: (1) auto-enrollment individual retirement accounts (auto-IRAs), also known as Secure Choice Plans; (2) small business marketplaces; (3) publicly-administered defined contribution (DC) plans (including open multiple employer plans, MEPs, and prototype plans); and (4) a hybrid model including auto-IRAs and open MEPs.

While heralding the bipartisan effort and innovation of active states and their representatives, this discussion seeks to broaden options for future legislation by raising up best practices from the movement's early leaders. It does so through an analysis of the four major reform models according to their ability to facilitate the principles of effective reform, including universal coverage, mandatory participation, pooled assets, and guaranteed lifetime income.

This analysis, considered in context of the federal Employee Retirement Income Security Act of 1974 (ERISA), finds that of the four current policy vehicles, the hybrid model that combines a marketplace with an open MEP and auto-IRA provides the best option for increasing access to coverage and offers the most potential to support all four principles of reform.

However, this analysis makes clear that none of the current state models are a panacea for the retirement crisis.

For some vehicles, this is due primarily to policy design. Marketplace plans, for example, are not designed to improve retirement plans, but to facilitate employers' access to plan information.

However, the remaining models (some more than others, discussed below), seek to increase coverage as well as plan quality. While coming closer to the goal of comprehensive retirement reform, these fall short due to both ERISA's federal limitations on mandates and participation as well as missed opportunities to build in mechanisms – such as prohibiting hardship withdrawals and including annuitization – that support guaranteed lifetime income.

Ulimately, state innovation, as exhibited here, can pave the road for comprehensive state reform, but is limited by its own borders. The state context leaves policy proposals subject to federal ERISA rules, creates unequal access to retirement savings across the country, and sets up different administrative requirements for multi-state employers.

These limitations make clear that state action is evidence of a bipartisan, grassroots demand for a long-term, comprehensive federal option that can ensure all workers' retirement security.

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1. Introduction

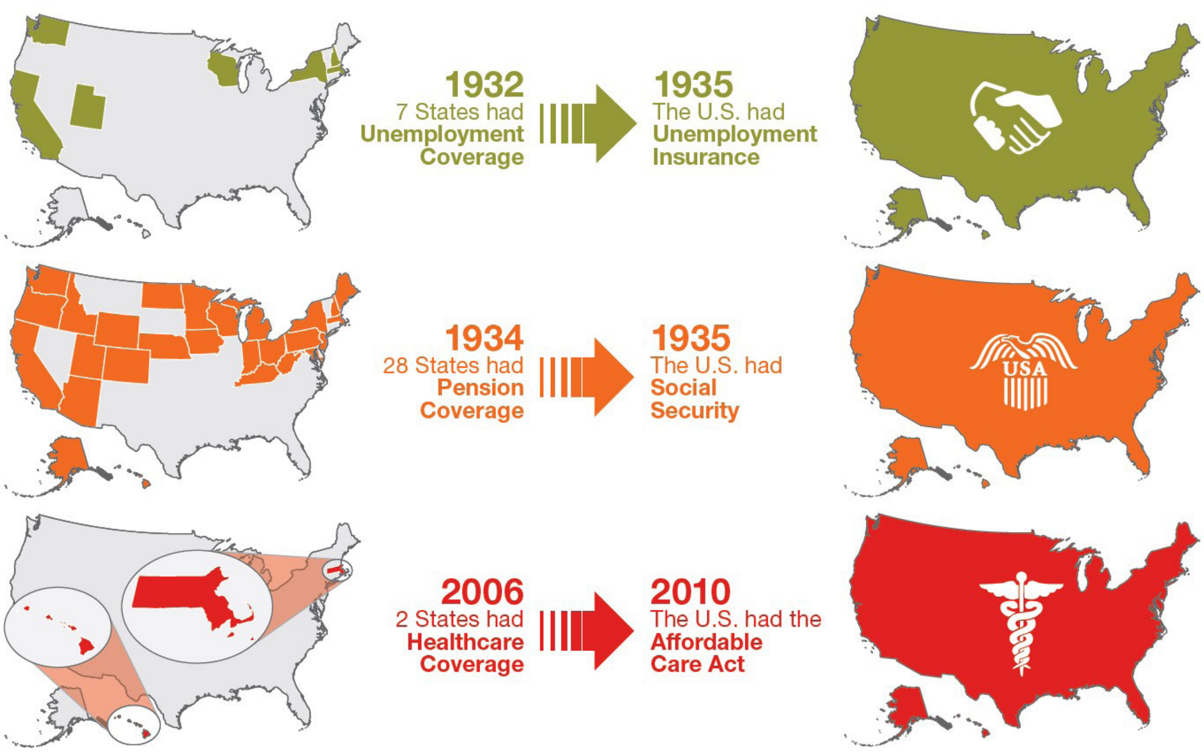
Households have three potential sources of income in retirement: Social Security, employer-sponsored retirement plans, and personal savings. Social Security benefits average $1,300 per month, enough for most seniors to stay out of poverty but not enough to maintain pre-retirement standards of living[1]. Many retirees rely on employer-sponsored plans to make up the shortfall. However, worker access to employer-sponsored retirement savings plans is falling. Approximately 48 percent of American workers did not have access to a workplace plan in 2015, up from 42 percent in 1979.[2] Due in part to households' lack of employer-sponsored plans, the median account balance for workers nearing retirement is $15,000, enough to generate benefits of approximately $60 a month.[3] In the absence of reform, the number of poor or near-poor 65 year olds is projected to more than double within the next decade.[4]

Reform Moves to the States

Despite evidence of a systemic, nation-wide retirement crisis, federal reform efforts have gone from making slow progress under the Obama administration to taking large steps back under the Trump administration. The Obama administration enacted myRA, a small-scale retirement savings program, and issued federal rules to pave the road for state reform and establish protections for retirement investors. President Trump abruptly cancelled the myRA program,[5] eliminated federal support for state reform, and delayed the fiduciary rule.

In the absence of comprehensive federal action under both administrations, state-level retirement reform efforts continue to emerge at a breathtaking pace. In only six years, from 2011 to 2017, 40 states have proposed – and 9 have enacted – bipartisan retirement reform to provide private-sector workers access to retirement savings accounts.[6] Since President Trump's inauguration, 22 states have proposed – and Vermont enacted – retirement reform bills.[7]

Figure 1: State Innovation Leads to National Policy



Source: Department of Labor and the Social Secuity Administration.

The Importance of State Precedent

American social policy has a history of beginning with state-level experiments (see Figure 1). In 1932, Wisconsin had unemployment coverage before it was enacted at the federal level in 1935.[8] That same year, Social Security was created after 30 states had enacted old-age pensions.[9] A 21st century example is the federal Affordable Care Act, known as "Obamacare" and passed in 2010, which was modeled after Massachusetts' 2006 health insurance reform, or "Romneycare."

In this context, state-level retirement reform proposals serve as a bellwether for federal retirement reform. As such, they are invaluable experiments for evaluating how best to ensure all working Americans are enrolled in pre-funded retirement plans.

Of the nine states that have enacted reform, only two programs are up and running (Oregon and Massachusetts), with the rest in various stages of implementation. Hence, the rapid emergence of the bipartisan state retirement reform movement has yet to deliver evidence upon which to evaluate the success or failure of specific policy vehicles.

In the absence of tangible outcomes, state policymakers are modeling legislation on bills moving forward in other states. Thus, the first states to enact reform have had tremendous influence over the shape of reform in subsequent states (see Figure 2). For example, laws passed in Connecticut and Maryland were based on California's 2012 plan, while proposals in Louisiana, Michigan and Ohio were based on Illinois' 2015 law.

New Jersey is also a good example. In early 2016, Governor Chris Christie rejected the Illinois-type plan passed by the state legislature, replacing it with legislation based on the proposal enacted in Washington State a year earlier.[10]

This report seeks to lift up best practices from current state models for legislators interested in pursuing retirement reform by evaluating them against a set of qualities necessary for effective reform. The report proceeds according to the following outline:

1. Qualities of Effective Reform: Identification and description of the qualities of effective reform.

2. State Plans and ERISA: A discussion of the legal context for state proposals as dictated by ERISA.

3. Analysis of State-Level Models: Analysis of the four major state-based reform models, including how the reform vehicle works, how it interacts with ERISA, and how the model reflects the qualities of effective reform.

 a. State Proposals: Each model includes a discussion of state efforts, including the significance, impact, legislative status, how it works, and how the state's reform measure fulfills the qualities of effective reform.

4. Context for State Action: Discussion of the short- and long-term context for state reform efforts, including federal reform efforts and the limitations of state-by-state reform.

5. Conclusion

Figure 2: States Follow Early Retirement Reform Models

State Leader & Year Enacted	Massachusetts 2012	California 2012	Illinois 2015	Oregon 2015	Washington 2015	Massachusetts Pending
Model Type	Public Admin DC (incl Open MEPs)	Auto-IRAs >5 employees	Auto-IRAs >25 employees	Auto-IRAs All Firms	Small Business Marketplace	Hybrid Auto-IRA & Public Admin DC
States to Follow	New Jersey Vermont	Arizona Colorado Connecticut Kentucky Maryland Pennsylvania	Louisiana Michigan Ohio	Indiana Montana* New York North Carolina* Rhode Island	Arkansas Connecticut Maine New Jersey North Dakota Oklahoma	Minnesota Texas

Source: Georgetown Center for Retirement Initiatives
Notes: Montana limits eligible employers to those with no more than 150 employees. North Carolina limits eligible employers to those with no more than 50 employees. States not included are those that proposed legislation to study retirement reform options and Utah, which proposed a voluntary IRA bill. City proposals by New York City and Seattle are also not included.

2. Qualities of Effective Reform

Each of the four major state reform vehicles share in the goal of ensuring residents' access to a retirement plan at work. However, an external measure is needed to clarify the strengths and limitations of state-level policy proposals to lift up best practices for future state and federal legislation.

This report defines effective reform as ensuring seniors have guaranteed retirement income sufficient to maintain their pre-retirement standards of living. Retirement USA, a Washington, DC-based non-profit that advocates on behalf of workers and retirees, put forward 12 principles necessary to fulfill this goal.[11] These can be summarized into the following four qualities, which form the basis of this analysis:

1. Universal Availability:

Every worker should have access to a retirement savings plan to supplement Social Security. This will ensure that seniors do not need to be dependent on the public purse to avoid old-age deprivation after a lifetime of work.

2. Mandatory Participation:

As with Social Security, workers and employers should be required to contribute to accounts that cannot be accessed before retirement, ensuring all workers have adequate retirement income.

3. Pooled and Diversified Portfolios:

Contributions should be pooled and professionally managed to diversify the portfolio, lower costs and earn better investment outcomes. Pooled funds benefit from economies of scale that minimizes fees, especially for smaller accounts under a million dollars.

4. Guaranteed Lifetime Income:

Retirement reform should provide workers with a guaranteed lifetime income in retirement as a supplement to Social Security. Annuities protect workers from the possibility of outliving their savings.

These four qualities not only provide a baseline to evaluate leading state reform vehicles, but also offer policymakers a list of guidelines when choosing the policy options appropriate for their state needs.

3. State Plans and ERISA

This analysis takes place among an ongoing conversation between state, local, and federal actors regarding the legal constraints on non-federal reform as dictated by the federal law known as ERISA, or the Employee Retirement Income Security Act of 1974.

ERISA provides important federal protections for workers participating in most retirement and pension plans sponsored by private business. The law assigns a fiduciary duty to employers offering a workplace plan to ensure plan decisions are made soley in the interest of participants. It also establishes a grievance process for workers to claim benefits and employees' right to take legal action and receive damages.[12]

Because the four reform models used by states (and analyzed here) affect employers—either by creating new opportunities or specifying new responsibilities—policymakers sought clarification from the U.S. Department of Labor (DOL) regarding the application of ERISA. A brief overview of this ongoing legal and legislative dialogue is included in the analysis of each model.

ERISA and the Qualities of Effective Reform

Universal Availability and Mandatory Participation

The state auto-IRA model, which is not expected to be covered by ERISA, seeks to overcome the problem of low retirement savings plan coverage and participation by both requiring employers to participate and automatically enrolling employees, although with an opt-out provision. Models without an auto-IRA mechanism that are covered by ERISA, including marketplaces and publicly-administered DC plans, rely on voluntary employer participation rather than employing mandates.

In 2016, the DOL issued a regulation stating that an employer's choice to participate in a retirement savings plan served as a trigger for ERISA. For example, a plan falls under the federal statute if an employer chooses to offer a 401(k) plan, and/or make contributions on behalf of their employees, or if they choose to automatically enroll their employees in a state-sponsored IRA. However, if an employer is mandated to enroll employees in a state-facilitated auto-IRA (with an opt-out) and does not contribute on behalf of their employees, the plan should not fall under ERISA.

This clarification was rolled back under the Trump administration. However, legal opinion on the application of ERISA to state plans continues to rest on employer involvement, stating that voluntary employer involvement qualifies a plan for ERISA.[13]

ERISA provides valuable protections for workers. However, it's reliance on voluntary participation for both the employer and employee limits the ability of state reform to fulfill the principles of universal availability and mandatory participation. Hence, federal reform is needed.

4. Analysis of State-Level Models

This paper discusses a representative sample of the four main models of current state reform efforts: auto-IRA plans, small business marketplaces, publicly-administered DC plans (prototype and open MEP plans), and hybrid vehicles. It also includes discussion of relevant efforts at the municipal level.

4.1. Auto-IRA Model

Auto-IRAs are the most popular state reform model, used in 18 places, including 17 states and one city. The policy was enacted in five states (California, Connecticut, Illinois, Maryland, and Oregon), proposed in 12 states (Ohio, Arizona, Louisiana, Indiana, Kentucky, Michigan, Rhode Island, New York State, Colorado, Pennsylvania, Montana and North Carolina), and in the ciy of Seattle.

Auto-IRAs are also included as part of hybrid models (discussed in section 4.4) in three states and New York City.

Auto-IRAs are state-level retirement plans designed to provide retirement savings accounts to private-sector workers who do not have access to such a plan at work. Under auto-IRAs, designated private-sector employers are required to automatically deduct a percentage of their workers' pay and forward it to state-facilitated, not-for-profit individual retirement account (IRAs). Such accounts, which are individually owned and professionally managed, would be administered by an independent board headed by state-appointed trustees. Employees would have the right to change their contribution rates or opt-out of the program.

Auto-IRA Plans and ERISA

State and city pension plans for public employees are considered "governmental" plans and, as such, exempt from ERISA. However, a government-facilitated auto-IRA for private sector workers is not considered a governmental plan.[14] To be considered exempt from ERISA coverage, it would have to qualify for a "safe harbor" exemption from DOL.

Since 1975, ERISA has provided "safe harbor" exemptions for employers offering payroll deduction IRAs to their employees when both employers and employees participate voluntarily.[15]

The DOL has historically required ERISA coverage for plans that allow for voluntary participation on behalf of both employers and employees. However, state-facilitated auto-IRA plans are expected to qualify for safe harbor exemption because employers are not choosing to participate, but are mandated to do so (and only as a limited intermediary between employee and state administrator) and employees, while automatically enrolled, have a choice to opt out.[16]

To clarify this distinction for states seeking to implement such plans, the DOL issued a final regulation, "Savings Arrangements Established by States for Non-Governmental Employees," in August of 2016 after a full deliberative legal and legislative process. The regulation addressed the new elements included in state-facilitated auto-IRAs of mandated employer participation and auto enrollment with an employee opt-out and supported the conclusion that such plans would qualify for exemption from ERISA under the original 1975 safe harbor. At the same time, the DOL proposed a new rule, finalized later in 2016, that also allowed certain city-administered IRAs for private-sector workers to qualify for the safe harbor.[17]

In February and May of 2017, the Republican majorities in Congress passed resolutions later signed by President Trump using the Congressional Review Act (CRA) to overturn DOL's regulations regarding cities and states establishing auto-IRAs. In response, states and cities with active reform efforts, including California,[18] Illinois,[19] and Oregon,[20] publicly stated their intent to continue moving forward with their respective programs. Officials noted that DOL's 2016 regulations were not legally necessary due to the original 1975 safe harbor, but were requested for additional clarity only. Experts expect the first plans implemented to be challenged in court.[21]

Auto-IRAs and Qualities of Effective Reform

Universal Availability and Mandatory Participation

Auto-IRAs include mandatory participation for specified employers. However, this mandate is limited to enrolling their employees in a state-facilitated IRA. While this design falls short of the principle of mandated participation, which requires not only participation of both employers and employees, but contributions as well, it is an important first step in acknowledging the inadequacy and lack of efficacy of voluntary participation when it comes to saving for retirement.[22] For this reason, auto-IRAs are considered to offer what we call "near" universal availability in the following pages, but are not considered to satisfy the full principle of mandatory participation.

In addition to limits on mandates, the auto-IRA's ability to expand coverage is also constricted by the inclusion of exemptions.

In 2012, California became the first state to enact auto-IRAs, followed by Illinois in 2015. Illinois' plan follows California's model but for a few details. While both include a 3 percent employee contribution and opt-out provisions for employees, Illinois provides less coverage by providing exemptions for business.

California requires participation from employers with five or more employees, whereas Illinois sets the bar for participation at a firm size of 25 or more employees. This difference has become significant as states following in California and Illinois' footsteps choose between these two auto-IRA models. The California model requiring more coverage is reflected in proposals in six states, including Arizona, Colorado, Connecticut, Kentucky, Maryland and Pennsylvania. The Illinois auto-IRA model that provides less coverage is the basis of proposals in Louisiana, Michigan and Ohio.

Mandatory Participation: Pre-Retirement Withdrawals

Most of the existing auto-IRA bills were drafted under DOL's November 2015 proposed guidelines for state auto-IRA programs that prohibited states from limiting withdrawals. The department's final rule, however, evolved to recognize the need to limit retirement savings withdrawals, to both preserve funds for their intended purpose and allow for less-liquid investment options.[23]

While the DOL rule was voided by President Trump's rollback of federal support for state reform, it serves as a recognition of the need for a prohibition on withdrawals in subsequent reform efforts.

Pooled Assets

Commercial IRA and 401(k) accounts are individually owned and directed. Under this structure, each account holder is responsible for selecting their investments, with the overwhelming choice being liquid investments.

A pooled fund of diverse assets is a legal entity managed by a third-party administrator that pools together savers' contributions for investment in a mixed portfolio of assets, similar to defined benefit plans or endowments. Each saver owns "units," or a piece, of the fund. The fund itself owns the underlying assets. But, unlike mutual funds, pooled and diversified portfolios include illiquid asset classes in addition to public stocks and bonds.

Auto-IRA legislation (including those both proposed and enacted) requires workers' savings be invested in pooled funds. However, as state auto-IRAs move from the statehouse to their respective implementing agencies, the requirement for pooled accounts has been widely interpreted. For example, in California's process, which required two enabling laws, the first law called for an investment strategy based on pooled assets. The legislation directs the newly created board to, "arrange for collective, common, and pooled investment of assets of the retirement savings program or arrangements, including investments in conjunction with other funds with which those assets are permitted to be collectively invested, with a view to saving costs through efficiencies and economies of scale."[24]

The board recommended the program invest in U.S. Treasuries for the first three years while it continues to investigate the investment options. The final law signed by Governor Brown incorporated this recommendation. The language was updated to state, "The board may also develop investment option recommendations that address risk-sharing and smoothing of market losses and gains. Investment option recommendations may include, but are not limited to, the creation of a reserve fund or the establishment of customized investment products."[25]

Other states, including Illinois, Oregon, and Connecticut, are also considering various investment options. Illinois' law[26] designates one of the board's duties as providing, "an efficient product to enrollees by pooling investment funds." As part of the implementation process, the State Treasurer, as chair of the board, issued a statement of the program's investment principles.[27] This includes a provision requiring the board to provide, "practical investment options, such as retirement target date portfolios that automatically rebalance based on their retirement time-horizon (i.e. a life-cycle fund), risk-based portfolios (i.e. aggressive, moderate, or conservative risk profiles) with varying target allocations, or a choice-based portfolio of stand-alone investment funds that track broad market segments."

Pooled Assets: Limits on Fees

The retirement savings landscape struggles with high fees that reduce returns[28] and a lack of transparency. Demos, a public policy research center, estimates that 401(k) fees decreased individual investors' wealth at retirement by nearly $155,000.[29]

Pooled funds with diversified assets allow for lower ees and better investments results. They offer more iversification and professional management than separate, individually-managed accounts. Because they are larger, they benefit from economies of scale.

However, state reform provides an additional opportunity to promote transparency and prohibit predation by capping fees.

While some state auto-IRAs limit fees under the general category of administrative fees, Connecticut specifically defines fees as "investment management charges, administrative charges, investment advice charges, trading fees, marketing and sales fees, revenue sharing, broker fees, and other costs necessary to administer the program."[30]

Of the state auto-IRAs that specify fee limits, plans include a range between a low of 0.5% of assets under management in Maryland to a high of 1% in California. A middle range between these two - 0.75% - is the most popular, included in Connecticut, Illinois and New York.

However, while limiting fees to 75 basis points will prevent the worst abuses, this cap is unlikely to provide employees with relief from high fees that erode savings.

Guaranteed Lifetime Income: Annuities

Vital to retirement security but with limited availability in the private market, state reform provides an opportunity to redefine payout standards for retirement savings by including annuities computed at smoothed interest rates in state-facilitated savings programs.

While payout remains an open question in many states' implementation processes (Illinois, Maryland and Oregon allow for the option of annuities), Connecticut has taken the lead by enacting a requirement that participants receive 50% of their payout in the form of an annuity.

States Using Auto-IRA Plans

Auto-IRA plans enacted or proposed in California, Connecticut, Illinois, Maryland, New York State, and Oregon are discussed in the following section, including their significance, impact, legislative status, and how they work.

a) California

Significance

In 2012, California was the first state to pass a law creating an auto-IRA.[31] As such, it provided the first model for other states.

Impact

When implemented, the California Secure Choice Retirement Savings Program could provide approximately 1.9 million people with access to a retirement plan at work.[32]

Legislative Status

California's Secure Choice law is the result of a two-step implementation process. First, the law created the California Secure Choice Retirement Savings Investment Board to complete a market and legal analysis on the program's feasibility and structure. The law required passage of a second bill incorporating the board's recommendations. In fulfillment of these requirements, the board reported their recommendations to the legislature in March 2016. California Governor Brown signed the second bill authorizing implementation on September 29, 2016.[33] California State Treasurer John Chiang estimates that employers will be required to particpate beginning in 2019.[34]

How it Works

California's auto-IRA requires employers with more than five employees who do not offer a retirement plan to automatically enroll their employees in state-sponsored IRAs. Employer participation will be phased in over three years based on employer size, however non-compliant employers will face penalties (as of yet undetermined). While employees have the choice both to opt-out and adjust their contribution rate, the default contribution rate is set at 3 percent of each paycheck with auto-escalation of up to 8 percent of salary with increases limited to no more than 1 percent of salary per year.[35] The California Secure Choice Retirement Investment Board will oversee the program and choose a private firm to manage workers' savings. The board recommended participants' savings be invested in U.S. Treasury securities for the first three years of the program's operation while further research is conducted regarding a long-term investment strategy based on either custom target date funds or a pooled IRA coupled with a reserve fund.

California's Current Retirement Coverage	
Working Age Population	21 million
Proportion of the Working Age Population in Labor Force	76%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	41%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	34%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of California's Auto-IRA (enacted)	
Year Enacted	2012
Default Employee Contribution	3%
Contribution Auto-Escalation	max 1% per year, up to 8% total
Subject to ERISA	No
Withdrawals	Yes
Account Type	Traditional IRA or Roth
Employee opt-in or opt-out	opt-out
Firm Size	>5
Portable	Yes
Fee limits	1%
Appoximate Impact on Coverage	+12 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by California's Secure Choice Retirement Savings Program	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	Payout undetermined

b) Connecticut

Significance

Connecticut's auto-IRA provides a model for the inclusion of annuities, moving the auto-IRA model closer to the principle of providing guaranteed lifetime income in retirement.[36]

Impact

When implemented, the Connecticut Retirement Security Exchange will provide approximately 200,000 people with access to a retirement plan at work.[37]

Legislative Status

In May 2016, Connecticut enacted an auto-IRA through the 2016 budget implementation bill. The program, administered by the Connecticut Retirement Security Authority, has an unspecified start date. The Authority must revisit the implementation deadline by March 1, 2018.

How it Works

The act requires all employers with five or more employees who do not offer a retirement plan to automatically enroll their employees in a state-facilitated Roth IRA. The employee default contribution rate will be 3 percent, but workers will be able to opt-out or change their contribution rate. While the board is tasked with investing savings in target date funds offered by multiple vendors, the plan is designed to provide lifetime retirement income by automatically converting half of each participant's savings to an annuity when they reach retirement age. The authority is also tasked with studying the possibility of offering a traditional IRA. Accounts would be pooled, professionally managed and portable.

Connecticut's Current Retirement Coverage	
Working Age Population	1.9 million
Proportion of the Working Age Population in Labor Force	83%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	51%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	43%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Connecticut's Auto-IRA (enacted)	
Year Enacted	2016
Default Employee Contribution	3%
Contribution Auto-Escalation	Yes, max 10% total
Subject to ERISA	No
Withdrawals	Yes
Account Type	Traditional IRA
Employee opt-in or opt-out	opt-out
Firm Size	>5
Portable	Yes
Fee limits	0.75%
Approximate Impact on Coverage	+12 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Connecticut's Secure Choice Retirement Savings Program	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	Yes (annuities required)

c) Illinois

Significance

In 2015, Illinois was the second state to pass legislation creating an auto-IRA.[38] Exempting those with under 25 employees rather than California's five, the Illinois auto-IRA serves as a model for those seeking broader business exemptions. However, in doing so, this model provides less coverage.

Impact

When implemented, the Illinois Secure Choice Savings Program will provide over 300,000 people with access to a retirement plan at work.[39]

Legislative Status

While Illinois was the second state to pass an Auto-IRA law, it was the first to go into effect on June 1, 2015, with the creation of the program's administrative entity, the Illinois Secure Choice Savings Board. In July 2016, the Treasurer's office issued an RFP to conduct a market analysis for the program. Implementation will be phased in with a pilot program beginning in 2018.[40]

How it Works

Illinois' auto-IRA requires employers with more than 25 employees who do not offer a retirement account to automatically enroll their employees in state-facilitated target date Roth IRA. The law further exempts employers who have been in business for fewer than two years and employers who have offered a retirement plan within the previous two years. Employers who do not comply will be fined $250 per employee for the first year and $500 per employee each year thereafter. Employees' default contribution will be 3 percent of each paycheck, although they will be able to adjust their contribution rate or opt-out. The Illinois Secure Choice Savings Board will oversee the program, choose a private firm to manage workers' savings, and determine how to invest workers' savings. While the legislation states that the board has the option to invest in annuity funds, the investment guidelines issued by the board chair and state treasurer do not include annuities.[41]

Illinois' Current Retirement Coverage	
Working Age Population	6.7 million
Proportion of the Working Age Population in Labor Force	81%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	47%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	40%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Illinois' Auto-IRA (enacted)	
Year Enacted	2015
Default Employee Contribution	3%
Contribution Auto-Escalation	No
Subject to ERISA	No
Withdrawals	Yes
Account Type	Roth IRA
Employee opt-in or opt-out	opt-out
Firm Size	>25
Portable	Yes
Fee limits	0.75%
Approximate Impact on Coverage	+6 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Illinois' Secure Choice Retirement Savings Program	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	TBD (annuity option)

d) Maryland

Significance

Maryland's auto-IRA is unique in providing an incentive to participating employers, who will receive a waiver of the state's $300 annual corporate filing fee.[42]

Impact

When implemented, the Maryland Small Business Retirement Savings Program and Trust will provide approximately 300,000 people with access to a retirement plan at work. [43]

Legislative Status

In May 2016, Maryland enacted an auto-IRA based on recommendations from the state's Task Force to Ensure Retirement Security for all Marylanders created by former Governor Martin O'Malley and chaired by retirement security expert Kathleen Kennedy Townsend. In July 2016, Maryland authorized the Maryland Small Business Savings Board to study and administer the trust and the program. In October 2017, the Board approved bylaws and received approval from the Attorney General to operate as a non-profit corporation that will still be subject to state oversight.

How it Works

Maryland's auto-IRA requires all employers who do not offer a retirement plan to automatically enroll their employees in a state-facilitated IRA. New businesses are allowed a two-year deferral, while participating businesses are given a waiver on the state's $300 annual corporate filing fee. Employees are allowed to opt-out, but the board will determine an automatic default contribution rate. The board will oversee the program and establish a range of investment options, including possible options to invest in annuities.

Maryland's Current Retirement Coverage	
Working Age Population	3.2 million
Proportion of the Working Age Population in Labor Force	81%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	52%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	43%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Maryland's Auto-IRA (enacted)	
Year Enacted	2016
Default Employee Contribution	Not specified
Contribution Auto-Escalation	No
Subject to ERISA	No
Withdrawals	Yes
Account Type	Traditional IRA
Employee opt-in or opt-out	opt-out
Firm Size	>5
Portable	Yes
Fee limits	0.5%
Approximate Impact on Coverage	+11 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Maryland's Small Business Retirement Savings Program and Trust	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	TBD (annuity option)

e) New York State

Significance

New York State's proposed Auto-IRA requires all firms to participate, but has a lower contribution rate than Oregon's model.[44]

Impact

If implemented, the New York State Secure Choice Savings Program and Trust will provide over 4.3 million people with access to a retirement plan at work.[45]

Legislative Status

In February 2017, lawmakers in New York State's Senate and Assembly introduced legislation to create a New York State Secure Choice Savings Board to study an auto-IRA program and guide its implementation. The bill was originally introduced in 2015, followed in 2016 by the creation of Governor Cuomo's SMART Commission, "Saving More to Achieve Richer Tomorrows," to work with stakeholders on how to implement an auto-IRA in the state.[46]

How it Works

Like the Oregon SCP, New York's proposed plan would require employers who do not offer a retirement account to automatically enroll their employees in state-facilitated IRAs. Employees' default contribution would be 3 percent of each paycheck, although they will be able to adjust their contribution rate or opt-out. Accounts would be pooled, professionally managed and portable.

New York's Current Retirement Coverage	
Working Age Population	10.4 million
Proportion of the Working Age Population in Labor Force	77%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	46%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	39%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of New York's Auto-IRA (proposed)	
Year Enacted	Not enacted
Default Employee Contribution	3%
Contribution Auto-Escalation	No
Subject to ERISA	No
Withdrawals	Yes
Account Type	Roth IRA
Employee opt-in or opt-out	opt-out
Firm Size	All
Portable	Yes
Fee limits	0.75%
Approximate Impact on Coverage	+54 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by New York's Secure Choice Savings Program	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	No

f) Oregon

Significance

The Oregon auto-IRA is significant for three reasons. First, it is the only state auto-IRA that is up and running. Second, it was the leader in requiring all firms to participate, regardless of their size.[47] Therefore, within the auto-IRA model, it comes closest to the principle of providing universal coverage. Third, Oregon also has the highest default employee contribution rate within the auto-IRA model, at 5 percent rather than the more commonly used 3 percent.

Impact

When fully implemented, the Oregon Retirement Savings Program will provide over 800,000 people with access to a retirement plan at work.[48]

Legislative Status

Oregon enacted an auto-IRA in June 2015. The law established the Oregon Retirement Savings Board to guide implementation of the "OregonSaves" program. In July of 2017, the program began enrolling interested employers as a part of a pilot program and went statewide in October, phasing in employers based on firm size.

How it Works

Oregon's auto-IRA, overseen by the Oregon Retirement Savings Board, requires all employers who do not offer a qualified retirement plan to automatically enroll their employees in state-facilitated Roth IRAs. However, it will phase in employers based on size, beginning with the state's largest employers and giving small businesses the longest time to make the transition.[49] The board has determined a default contribution rate of 5% with auto-escalation of 1% per year and a limit of 10% of pay. Employees will be able to adjust their contribution and escalation rate or opt-out of the program. Accounts will be pooled and portable. The first $1,000 is invested in a capital preservation fund, with additional contributions invested in a target date fund.

Oregon's Current Retirement Coverage	
Working Age Population	2.1 million
Proportion of the Working Age Population in Labor Force	78%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	48%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	38%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Oregon's Auto-IRA (enacted)	
Year Enacted	2015
Default Employee Contribution	5%
Contribution Auto-Escalation	Yes
Subject to ERISA	No
Withdrawals	Yes
Account Type	Roth IRA
Employee opt-in or opt-out	opt-out
Firm Size	All
Portable	Yes
Fee limits	Not specified
Approximate Impact on Coverage	+52 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Oregon's Retirement Savings Program	
Universal Availability	Yes (near)
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	TBD (annuity option)

4.2. Small Business Marketplace Model

The marketplace model is second to auto-IRAs in popularity among states. It is the vehicle used by seven out of 40 states, including Arkansas, Connecticut, Maine, New Jersey, North Dakota, Oklahoma and Washington.

Marketplace plans are online exchanges set up and managed by the state to connect small businesses with providers of retirement savings plans. According to the Retirement Equity Lab (ReLab) report, "Are U.S. Workers Ready for Retirement?," employees at small businesses are less likely than those at medium and large businesses to have access to an employer-sponsored retirement account.[50] Employers have suggested this is due to high administrative costs, including the burden of finding and choosing a plan and exposure to liability. In response, marketplace plans propose to mitigate small employers' barriers to entry by offering a screening mechanism to identify quality plans.[51]

Marketplace Plans and ERISA

Because the role of the state in a retirement savings plan marketplace is to facilitate a connection between employers and private-sector vendors, the plans offered through the marketplace can be either ERISA or non-ERISA plans.

Marketplaces and Qualities of Effective Reform

Universal Availability and Mandatory Participation

Marketplace plans face two significant hurdles in the effort to promote employer provision of retirement savings plans. First, the program leaves the potentially disabling issues of cost and liability unaddressed. Second, employer participation is voluntary. If employers find the marketplace insufficient in addressing transaction costs, they are unlikely to change prior behavior and offer plans through the marketplace.

To address this problem, the model allows for the provision of incentives to employers through either public or private funds.

As a model, marketplaces provide an alternative to requiring employer participation. However, the resulting trade-off is significantly diminished coverage for workers. This is dramatically illustrated by the legislative history behind New Jersey's implementation of a marketplace plan. The state's legislature passed legislation to create an auto-IRA. When it reached Governor Chris Christie's desk, he supplanted the auto-IRA with a replica of Washington's marketplace, which was subsequently passed into law. The original auto-IRA would have required employers with 25 or more employees to participate, providing 27 percent of New Jersey's workforce with coverage.[52] However, the voluntary nature of the enacted marketplace plan makes it impossible to determine if these workers will indeed receive coverage as a result of the new policy.

Pooled Assets

Unlike auto-IRA proposals, marketplace plans do not specify that assets should be pooled. The only specifications for asset investment include a provision that firms participating on the exchange must provide a minimum of two product options, either target date funds or balanced funds.

Pooled Assets: Limits on Fees

The marketplace model focuses on sparing employers both time and expense. However, current exchange proposals miss the opportunity to protect employees from undue costs. For example, both Washington and New Jersey prohibit firms participating in the exchange from charging employers a fee, but cap fees charged to employees at 1% of total assets (100 basis points), a cap unlikely to provide employees with relief from high fees that erode their savings.[53]

States Using Marketplaces[54]

Because these plans exhibit little variation, the first state to implement the proposal, Washington, is analyzed in the following section, including its significance, impact, legislative status, and how it works.

a) Washington

Significance

Washington was the first state to create a marketplace for small businesses to connect with certified retirement savings vendors.[55] Subsequently, the marketplace model was adopted by New Jersey and proposed in Maine, Arkansas, Connecticut, North Dakota, and Oklahoma.

Impact

Because the Washington Small Business Retirement Marketplace is based on voluntary participation on behalf of employers, the impact on worker coverage cannot be determined.

Legislative Status

In May 2015, Washington became the first state to enact a small business marketplace. Housed within the state's Department of Commerce, the program established a pre-launch website and is working to establish participation protocols for financial service firms.[56] The marketplace's kickoff, set for 2017, was delayed by the cancellation of the federal myRA program, a plan the state law required to be featured on the marketplace.[57] The marketplace's initial launch is now expected in early 2018.

How it Works

Washington's Small Business Retirement Marketplace is open to employers who are self-employed, sole proprietors of their business, and those with 100 or fewer employees. The marketplace director is charged with approving private-sector financial firms for participation and the retirement plans offered. While there is no limit to how many financial firms can participate, there must be at least two for the exchange to operate. Participating firms must offer at least two types of plans, including a SIMPLE IRA-type plan that allows for employer contributions and a payroll deduction IRA-type plan for employee contributions only. Firms are required to provide two investment options, including a target-date fund and a balanced mutual fund.

Employees must be allowed to roll over pre-tax funds from a marketplace to an unaffiliated IRA or qualified account. Qualified plans cannot charge employers an administrative fee and enrollees cannot be charged more than 100 basis points in total annual fees.

Washington's Current Retirement Coverage	
Working Age Population	3.8 million
Proportion of the Working Age Population in Labor Force	80%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	50%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	41%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Washington's Marketplace Plan (enacted)	
Year Enacted	2015
Default Employee Contribution	No
Contribution Auto-Escalation	No
Subject to ERISA	Marketplace, no. Plans offered, yes.
Withdrawals	Yes
Account Type	Traditional and Roth IRAs, 401(k) and other ERISA retirement plans
Employee opt-in or opt-out	NA
Firm Size	<100
Portable	Yes
Fee limits	1% to investor, no fee to employer

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Washington's Small Business Retirement Marketplace	
Universal Availability	No
Mandatory Participation	No
Pooled Assets	No
Lifetime Income	No

Due to its primary function as a portal between small employers and qualified plans, the marketplace does not define contribution rates.

4.3. Publicly-Administered DC Model

Three states have enacted or proposed publicly-administered DC models, including Massachusetts, New Jersey and Vermont.

In fact, this vehicle spans the reform movement. Massachusetts was the first state to take action on state reform and Vermont was the latest to act.

In November of 2015, the DOL issued Interpretive Bulletin (IB) 2015-02 to provide guidance to states regarding creation of publicly-administered DC plans, including prototype plans (Massachusetts) and state-facilitated open MEPs (New Jersey and Vermont).

While MEPs have been in existence since the 1950s, previous DOL regulations required participants in multiple employer plans to have a "common nexus," interpreted to mean that participating employers operated in the same market. The IB expanded this definition, stating that in a state-facilitiated MEP, the state served as the nexus between employers and employees through the state's need to support retirement coverage. These vehicles are known as open MEPs.

The IB also clarified rules on prototype plans, such as Massachusetts' 2012 law establishing a state-facilitated 401(k) for non-profit workers and allowed for city-administered open MEPs (included in New York City's proposed hybrid plan, discussed in section 4.4).[58]

This IB was unaffected by the Congressional CRA effort signed into law by President Trump that rolled back a separate DOL regulation on safe harbors for state auto-IRAs. As such, these regulations remain in effect.

Publicly-Administered DC Plans & ERISA

For both prototype plans and open MEPs, employers must voluntarily choose to participate and enroll their employees, qualifying the plans for ERISA coverage.[59]

However, under protoype plans, each individual employer is considered to sponsor the ERISA plan and serve as a fiduciary. Under an open MEP, the state acts as the plan sponsor of a signle ERISA plan covering all participating employers. As such, the state is responsible for the regulation of the plan and bears the fiduciary duty to the employee.[60]

Publicly-Administered DC Model and Qualities of Effective Reform

Universal Availability and Mandatory Participation

Current stand-alone models for publicly-sponsored DC models face two limitations to increasing coverage.

First, current proposals in Massachusetts and Vermont target small employers by relieving them of the administrative and legal burdens associated with offering ERISA plans. As such, these plans cover a vital need but limit their potential to increase coverage. Fortunately, this limitation is not a requirement of the model, allowing other states to use this model to cover all firms.

Second, publicly-sponsored DC plans do not mandate employer participation due to ERISA's limitation that employers must participate voluntarily.

These limitations motivated the creation of hybrid vehicles (discussed in the next section) that pair publicly-administered DC plans with auto-IRAs. Under this combined policy vehicle, states can offer plans that suit different employers and be assured coverage will increase coverage; if employers choose not to participate in a prototype or open MEP plan, they will be required to provide coverage through an auto-IRA program.

Pooled Assets

Assets in an open MEP would be pooled for investment purposes and professionally directed and managed. The resulting scale would generate lower fees and a greater universe of available investment alternatives, leading to a higher risk-adjusted rate of return.

Pooled Assets: Limits on Fees

Massachusetts is also a leader in using state reform as an opportunity to limit fees charged to plan participants. Among the states that have included fee limits, Massachusetts' range of 40-86 basis points is the lowest. As such, it is likely to be most effective in the effort to reign in the common problem of high fees eroding employees' savings.

States Using Publicly-Administered DC Plans

Massachusetts and Vermont, profiled here, are leaders in pursuing this reform vehicle. Both states' efforts are analyzed in the following section, including their significance, impact, legislative status, and how they works.

a) Massachusetts

Significance

In March 2012, Massachusetts was the first state to act on behalf of residents' need for retirement savings plan coverage.[61] Since then, it has set a high bar for reform. It was the first state to create and open a public alternative to commercial 401(k)s and IRAs for private-sector workers by creating a state-administered defined contribution plan. It is a leader in the effort to reign in high fees by setting the most stringent limit on fees vendors can charge to plan participants. It also has the highest initial default contribution rate of any vehicle at 6%, which helps employees build up retirement savings.

While Massachusetts' plan for non-profit employees covers only a small number of people, it was an early model for ERISA-protected savings accounts at no extra cost to the taxpayer.[62]

Impact

Because employer participation in the Massachusetts Defined Contribution CORE plan is voluntary, the impact on worker coverage cannot be determined.

Legislative Status

In 2012, Massachusetts enacted a law creating the Connecting Organizations to Retirement (CORE) 401(k) plan. Administered by the state treasurer, the law created a 5-member, not-for-profit defined contribution committee with experience in non-profits to serve as an advisory board to the Treasurer. The ERISA-covered plan was approved by the IRS in 2014. In October 2017, the state's Treasurer announced the program's official launch.[63]

How it Works

The plan would allow non-profit employers with fewer than 20 employees to deduct pre-tax dollars from employee paychecks and invest them in tax-deferred, state-administered 401(k)s. Employer participation is voluntary and employer contributions permitted, but not required. Employees are automatically enrolled, but can choose to opt-out. The default contribution rate is 6 percent, although employers can choose to set employee contributions at a 4 percent contribution with auto-escalation up to 10 percent.

Massachusetts' Current Retirement Coverage	
Working Age Population	3.7 million
Proportion of the Working Age Population in Labor Force	80%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	44%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	36%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Massachusetts' Publicly-Administered Defined Contribution Plan (enacted)	
Year Enacted	2012
Default Employee Contribution	6%
Contribution Auto-Escalation	Yes, up to 10%
Subject to ERISA	Yes
Withdrawals	Yes
Account Type	401(k)
Employee opt-in or opt-out	opt-out
Firm Size	<20
Portable	Yes
Fee limits	40-86 bps, depending on fund

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Massachusetts Defined Contribution CORE Plan	
Universal Availability	No
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	No

The law requires the plan to offer participants investment choices including target date funds, objective base funds, growth funds, income funds, capital preservation funds, and an inflation protection fund. Fees are capped for each fund, ranging from 86 bps for target date and inflation-protected funds to 40 bps for income and capital preservation funds.

b) Vermont

Significance

Vermont's retirement reform is significant for both its design and the timing of its passage.[64]

First, it is the first state to pass a state-facilitated open MEP under the expanded definition set in DOL's 2015 Interpretive Bulletin. It also is unique in targeting its efforts to help small businesses offer coverage, employers who are specifically exempted from some auto-IRA proposals.

Second, it was the first state to enact retirement reform after President Trump and Congressional Republicans rolled back Obama-era DOL rules supporting state-run plans. Vermont's passage of its plan on the heels of the Congressional vote illustrated states' political will for reform.[65]

Impact

Because employer participation in the Green Mountain Secure Retirement plan is voluntary, the impact on worker coverage cannot be determined.

Legislative Status

In May 2017, the Vermont House and Senate passed legislation creating the Green Mountain Secure Retirement Plan. It was signed by the Governor in June. Legislation was based on recommendations issued by the Public Retirement Study Committee led by Vermont Treasurer Beth Pearce.[66] The plan is set to be implemented on or before January 2019.

How it Works

The plan would allow employers with fewer than 50 employees to deduct pre-tax dollars from employee paychecks and invest them in a state-sponsored open MEP, or a tax-deferred, state-administered defined contribution plan. Vermont's design hopes to appeal to small businesses by relieving them of the legal and administrative requirements of ERISA, as the open MEP assigns the role of plan sponsor to the state.

Employer participation is voluntary and employer contributions permitted, but not required. Employees are automatically enrolled, but can choose to opt-out. The default contribution rate is not yet defined.

Vermont's Current Retirement Coverage	
Working Age Population	334,000
Proportion of the Working Age Population in Labor Force	84%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	48%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	40%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Vermont's Publicly-Administered Defined Contribution Plan (enacted)	
Year Enacted	2017
Default Employee Contribution	Not yet determined
Contribution Auto-Escalation	No
Subject to ERISA	Yes
Withdrawals	Yes
Account Type	401(k)
Employee opt-in or opt-out	opt-out
Firm Size	<50
Portable	Yes
Fee limits	Not specified

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Vermont's Green Mountain Secure Retirement Plan	
Universal Availability	No
Mandatory Participation	No
Pooled Assets	Yes
Lifetime Income	No

4.4. Hybrid Plan Model

Three states and one city proposed hybrid retirement reform models, including Massachusetts, Minnesota, New York City and Texas.

As reform efforts matured, officials seeking to maximize coverage options innovated to combine previous stand-alone vehicles to offer diverse products for diverse employers - and increase coverage.

For example, Massachusetts proposed pairing an auto-IRA, which mandates employer participation but does not include employer contributions, with an open MEP for employers who wish to offer ERISA-protected plans that allow for employer contributions. New York City's Comptroller went one step farther to include a marketplace in addition to an auto-IRA and an open MEP. Most recently, in 2017, New Jersey introduced a proposal to establish an open MEP that could participate in the state's (already enacted) marketplace.

The design flexibility of hybrid plans allows for maximum coverage. First, it allows employers to choose the quality of ERISA-based plans by relieving them of the responsibilities of serving as a plan sponsor (a role that moves to the state). Second, it works around the coverage limitation inherent in ERISA's requirement that employers participate voluntarily. By defaulting employers who choose not to join an open MEP into a requirement to offer non-ERISA auto-IRAs, increased coverage of some kind is assured.

For these reasons, this report seeks to recommend a comprehensive hybrid model to future legislators seeking to increase retirement coverage for their state's workers.

Hybrid Plans and ERISA

Because hybrid plans represent a second wave of innovation in state retirement policy options, they are designed to both take advantage of recent DOL guidance on ERISA application and to work around its limitations, as discussed above.

Hybrids and Qualities of Effective Reform

Universal Availability and Mandatory Participation

Hybrid plans are structured to offer the broadest possibilities for both increasing the quantity and quality of coverage.

Mandatory Participation: Pre-Retirement Withdrawals

As plans have evolved during the seven years of the state reform movement, Texas, one of the most recent states to introduce reform legislation in March of 2017, is the first state to prohibit withdrawals.

Pooled Assets

Assets in hybrid plans would be pooled for investment purposes and professionally directed and managed. The resulting scale would generate lower fees and a greater universe of available investment alternatives, leading to a higher risk-adjusted rate of return.

Pooled Assets: Limits on Fees

Current hybrid proposals include fee limitations between 0.5% and 1% of total assets, but include these caps for administrative fees, rather than specifying fee caps for investment management.

Guaranteed Lifetime Income: Annuities

Vital to retirement security but with limited availability in the private market, state reform provides an opportunity to redefine payout standards for retirement savings by including annuity payments in state-facilitated savings programs. By requiring annuities for everyone, states could overcome the adverse selection problem of annuities in the private market, resulting in more favorable rates. Namely, buyers are typically those who expect to live longer lives, which increases costs to insurers and leaves buyers facing higher prices.

States using hybrid models are among those taking the strongest stand for the need to include annuities as part of their state-facilitated plans. New York City includes lifetime income as a minimum policy requirement across all platforms, including the marketplace, open MEP and auto-IRA. Texas also includes a strong provision that at least 50% of employees' savings be paid out as an annuity.

States and Cities Using Hybrid Plans

Hybrid plans in Massachusetts, Minnesota, New York City and Texas are analyzed in the following section, including each proposal's significance, impact, legislative status, and how they work.

a) Massachusetts

Significance

Massachusetts' hybrid proposal is an innovative pairing of the mandated coverage required by auto-IRAs combined with the option for employer contributions through a voluntary open MEP.[67]

Impact

If implemented, the Massachusetts Secure Choice Retirement Savings Plan would provide approximately 1.6 million people with access to a retirement plan at work.[68]

Legislative Status

After it's original introduction in 2015, the bill was re-introduced in January 2017.

How it Works

The hybrid proposal would create the Secure Choice Retirement Savings Board to oversee two new trusts. The Secure Choice Multiple-Employer Retirement (MERP) Trust would be an open MEP, or a profit-sharing defined contribution plan based on individual accounts. The Secure Choice Individual Retirement Account (IRAP) Trust would be an auto-IRA, accepting employee contributions through employer-provided paycheck deductions.

Employers would be required to participate in the IRAP if they don't provide employees access to a qualified retirement plan, either in the form of a privately-sponsored 401(k) or IRA vehicle or through voluntary participation in the state-facilitated open MEP, or MERP.

The Board will establish default contribution and escalation rates as well as determine if the payout of accrued benefits will be in the form of annuities or lump sums. The Board is also charged with keeping fees low, but specifies that "in no event shall they exceed one percent of the total trust balance."[69]

Massachusetts' Current Retirement Coverage	
Working Age Population	3.7 million
Proportion of the Working Age Population in Labor Force	80%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	44%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	36%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Massachusetts' Hybrid Plan (proposed)	
Year Enacted	NA
Default Employee Contribution	Yes, unspecified
Contribution Auto-Escalation	Yes, unspecified
Subject to ERISA	Yes, open MEP No, IRA
Withdrawals	Yes
Account Type	Traditional IRA and 401(k)
Employee opt-in or opt-out	opt-out
Firm Size	All
Portable	Yes
Fee limits	1%
Approximate Impact on Coverage	+56 percentage points

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Massachusetts Secure Choice Retirement Savings Plan	
Universal Availability	Yes (near)
Mandatory Participation	Yes
Pooled Assets	Yes
Lifetime Income	No (unspecified)

b) Minnesota

Significance

Minnesota's proposed hybrid plan is an example of the Massachusetts hybrid model.[70] Its significance lays partly in timing. Minnesota and Texas introduced similar hybrid retierment reform proposals during the same month, a testimony to the bipartisan need and call for reform.

Impact

If implemented, the Minnesota Secure Choice Retirement Program will provide approximately 1.1 million workers with access to a retirement plan at work.[71]

Legislative Status

The proposal was introduced in March 2017.

How it Works

The Minnesota proposal would create what the legisaltion calls "a public-private partnership model for privately employed workers to save for retirement."[72]

The proposal would create a board to establish a program that includes both a multiple employer retirement plan (MERP) and an auto-IRA (IRAP). Employers in the state have the option to voluntarily join the MERP, where the state serves as plan sponsor and fiduciary and employers can make contributions to their employees accounts. If they do not choose the MERP, they will be required to participate in the IRAP.

Both options feature auto-enrollment of employees and default contribution rates, with opt-out provisions for workers. Contribution and auto-escalation rates as well as investement strategies and funds will be set by the board. Payout mechanisms will also be established by the board, but must include an option to transfer account savings to purchase an annuity.

The Minnesota proposal does not specify a fee cap for investment management, but does require that administrative costs are kept below 1% of the trust balance.

Minnesota's Current Retirement Coverage	
Working Age Population	2.9 million
Proportion of the Working Age Population in Labor Force	86%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	55%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	46%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Minnesota's Hybrid Plan (proposed)	
Year Enacted	NA
Default Employee Contribution	TBD
Contribution Auto-Escalation	TBD
Subject to ERISA	Yes, open MEP No, IRA
Withdrawals	Not specified
Account Type	Traditional IRA & 401(k)
Employee opt-in or opt-out	opt-out
Firm Size	All employers
Portable	No
Fee limits	1%

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Minnesota's Secure Choice Retirement Program	
Universal Availability	Yes (near)
Mandatory Participation	Yes
Pooled Assets	Yes
Lifetime Income	Yes (optional)

c) New York City

Significance

New York City's proposal is the most comprehensive and innovative proposal to date.[73] The plan puts forward three options for employers: a marketplace, an open MEP, and an auto IRA. These options allow for maximum flexibility for diverse employers as well as providing maximum coverage for employees while operating within the requirements of ERISA. The proposal matches this flexibility with an assertion that each vehicle should fulfill the minimum criteria requiring automatic enrollment, default contribution and escalation rates, pooled funds in passive lifecycle funds, fee limitations, and guaranteed lifetime income through annuities.

Impact

If implemented, New York City's Nest Egg Retirement Savings plan will provide approximately 2.3 million workers with access to a retirement plan at work.[74]

Legislative Status

In September 2016, New York City Comptroller Scott Stringer released his retirement security proposal, "New York City's Nest Egg: A Plan for Addressing Retirement Security in New York City." The Nest Egg plan was informed by the Comptroller's New York City Retirement Security Study Group.[75]

The plan was designed for New York City residents, but the report stresses its applicability to state implementation. The Wall Street Journal reports the Comptroller's staff shared the plan with New York State Governor Cuomo's SMART Commission, of which Comptroller Stringer is a member.[76]

How it Works

The New York City Nest Egg offers employers three options to sponsor retirement plans for their employees:

1. NYC 401(k) Marketplace – A voluntary exchange overseen by an independent board offering employers a choice of screened 401(k)s, IRAs, and 401(k)-type plans from private and public providers, including the Empire City 401(k) MEP.

2. Empire City 401(k) MEP – A publicly-sponsored multiple employer plan. Offered on the marketplace along with a variety of other retirement accounts, the open MEP provides employers a voluntary option that lessens the administrative and legal burden of ERISA while allowing for employer contributions.

3. NYC Roth IRA – employers who choose not to participate in the marketplace or MEP would be defaulted into an auto IRA, which requires employers to automatically enroll workers into a publicly-facilitated Roth IRA (with an employee opt-out).

The Nest Egg plan would be overseen by an independent board charged with protecting the interests of plan participants. The board would have freedom to select administrative, educational and investment management providers.

New York City's Current Retirement Coverage[68]	
Working Age Population	3.3 million
Proportion of the Working Age Population in Labor Force	68%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	43%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	37%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of New York City's Hybrid Plan (proposed)	
Year Enacted	NA
Default Employee Contribution	Yes, based on age & earnings
Contribution Auto-Escalation	Yes, based on earnings
Subject to ERISA	Yes, MEP & certain plans offered through Marketplace. No, Roth IRA
Withdrawals	"Limited"
Account Type	IRA, Roth IRA & 401(k)
Employee opt-in or opt-out	opt-out
Firm Size	All employers
Portable	Yes
Fee limits	Not specified

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by New York City's Nest Egg Retirement Savings	
Universal Availability	Yes (near)
Mandatory Participation	Yes
Pooled Assets	Yes
Lifetime Income	Yes

d) Texas

Significance

The hybrid proosal introduced in Texas is significant for two reasons.

First, Texas and Minnesota introduced their hybrid retirement reform proposals during the same month, a testimony to the bipartisan need and call for reform.

Second, the state's proposal is uniquely designed to protect workers' retirement savings. It is the only bill to prohibit early withdrawals, which is essential to preserve savings for retirement,[77] and is the only proposal to require creation of a reserve fund to guarantee workers' contributions.

Impact

If implemented, the Secure Retirement Plan for Texans will provide approximately 6.5 million workers with access to a retirement plan at work.[78]

Legislative Status

The proposal was introduced in March 2017.

How it Works

Texas' proposal would create a board to establish both a default, mandatory auto-IRA program with an opt-out for employees and an open MEP for employers who choose an ERISA-based plan that allows for employer contributions. The plan will also allow for direct contributions from those who are self-employed or from account holders who move out of state. Employees would be able to select their contribution rates above a floor of 2% of their wages, with the possibility of auto-escalation not to exceed 5%.

Regarding investment, the proposal does not specify fund types other than to require common funds that allow for pooled assets. It requires the board to create a reserve fund "to guarantee participants do not lose the principal amount of their contributions."[79] While the proposal does not specify limits on investment fees, it does limit administrative fees to 0.5% of the total plan fund.

Regarding payout, the proposal preserves saved funds for retirement by prohibiting pre-retirement withdrawal of funds unless a participant becomes disabled.
Upon payout, the bill requires at least half of workers' savings to be paid out in annuities.

Texas' Current Retirement Coverage	
Working Age Population	14 million
Proportion of the Working Age Population in Labor Force	78%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account	40%
Proportion of Workers with Access to an Employer-Sponsored Retirement Account who are Participating	32%

Note: Authors' calculations from CPS ASEC 2015-2017.

Attributes of Texas' Hybrid Plan (proposed)	
Year Enacted	NA
Default Employee Contribution	At least 2%
Contribution Auto-Escalation	Yes, not to exceed 5%
Subject to ERISA	Yes, open MEP No, IRA
Withdrawals	No
Account Type	Traditional IRA & 401(k)
Employee opt-in or opt-out	opt-out
Firm Size	All employers
Portable	Yes
Fee limits	0.5%

Note: Authors' calculations from CPS ASEC 2015-2017.

Qualities Supported by Texas' Secure Retirement Plan for Texans	
Universal Availability	Yes (near)
Mandatory Participation	Yes
Pooled Assets	Yes
Lifetime Income	Yes

5. Context for State Action

Stalled Federal Support

Federal reform efforts have gone from making slow progress under the Obama administration to taking large steps back under the Trump administration.

In Congress, members in the House and Senate introduced comprehensive reform proposals modeled after the Thrift Savings Plan for federal employees.

In 2016, Congress Member and Vice Chair of the House Democratic Caucus Joe Crowley (D-NY) introduced legislation to create federal SAVE UP accounts. Employers with more than 10 employees who do not already offer a retirement savings plan would be required to automatically enroll their workers. While workers could opt-out, employers would be required to contribute on behalf of each worker.

Also in 2016, Senator Jeff Merkley (D-OR) introduced the American Savings Act, which would automatically enroll workers in an individually-controlled federal savings accounts, but would not require employer contributions.[80]

This proposal is similar to former Senator Tom Harkins' USA Retirement Funds Act, which would set up pooled, auto-enroll 401(k) accounts for small employers and the self-employed.[81]

From 2010 to 2016, the Obama Administration included the auto-IRA proposal in its annual budget proposals to Congress, but the proposal was never enacted. In 2015, Obama launched the myRA program, which offers individuals access to government-sponsored retirement savings accounts similar to Roth IRAs. myRAs were designed as starter retirement savings accounts for workers who lack access to a retirement plan at work.[82]

In 2015 and 2016, Obama's DOL issued federal rules to pave the road for state reform by clarifying ERISA safe harbor exceptions for state and city auto-IRAs, establishing an employer nexis for state-facilitated open MEPS, and issuing a rule requiring advisors to act as fiduciaries regarding retirement investments.

These efforts came to an abrupt end in 2017. President Trump cancelled the myRA program,[83] rolled back federal support for state reform through the Congressional Review Act (CRA), and delayed implementation of the fiduciary rule.[84]

Limitations of State-by-State Reform

While state-level innovation has identified the need for a solution, state and municipal programs are not a long-term solution to the retirement crisis. First and foremost, state and local actors are creating a patchwork of regulations that will complicate the administration of plans across borders. Second, every worker should have access to a quality retirement savings plan. Policy reform that leaves out certain cities and states deny those residents equal access to provide for their own retirement and leave them subject to downward mobility in old age. Ten states and Washington, D.C., have not taken steps toward reform, which would leave over 9.5 million workers - 57% of the population in these states - without access to coverage.

States Without Retirement Reform Efforts

State	# of People Uncovered	% of People Uncovered
Alabama	966,418	54%
Alaska	150,002	50%
Delaware	186,036	47%
District of Columbia	151,301	46%
Florida	5,037,311	64%
Idaho	353,627	54%
Kansas	594,463	50%
Mississippi	651,911	61%
Missouri	1,175,560	47%
South Dakota	178,631	49%
Wyoming	127,786	51%
TOTAL	9,573,045	57%

Source: ASEC 2015-2017 average.
Notes: Non-self-employed private sector workers age 25-54 whose employers do not sponsor a retirement plan.

6. Conclusion

Raising Up the Hybrid Model

While heralding the bipartisan effort and innovation of active states and their representatives, this report seeks to broaden options for future legislation by raising up best practices from the movement's early leaders.

We find that of the four current policy vehicles, the comprehensive hybrid model that combines marketplaces, open MEPs, and auto-IRAs provides the best option to increase access to coverage and offers the most potential to support all four principles of reform. This framework is exemplified in the New York City proposal put forward by City Comptroller Scott Stringer.

The strength of the full hybrid model is that it allows employers the choice of how to offer their employees a retirement savings plan, but does require they offer, at minimum, auto-IRAs.

For example, an employer can choose to provide a qualified, vetted plan on the marketplace or offer an ERISA-based plan through an open MEP where the state serves as plan sponsor and fiduciary. Both of these options support employers' ability to make contributions to their employees' savings plans. However, If employers choose not to participate in one of these two options, the hybrid model requires they offer coverage through auto-IRAs. While auto-IRA plans do not allow for employers contributions due to ERISA limitations, they use auto-enrollment and (in some plans) auto-escalation to support workers' need to accumulate retirement savings.

Raising Up Prohibitions on Withdrawals, Fee Limits & Annuities

In addition to choosing a state policy vehicle, state reform also provides an opportunity to raise up policies that support workers' needs throughout the retirement savings lifecycle of accumulation, investment and payout.

This includes a prohibition on pre-retirement withdrawals to allow employees to accumulate an adequate level of savings, setting limits on investment fees to preserve employee contributions for savings, and payouts in the form of annuities rather than lump sums to ensure lifetime income.

These policies can be a part of all state reform packages, regardless of reform vehicle. State leaders regarding these policies include Texas, the only state to propose a plan that does not allow for withdrawals before reitrement, Massachusetts' plan for non-profits that puts an effective cap on high investment fees, and Connecticut and Texas for requiring that at least half of workers savings be paid out in annuities to ensure retirees don't out live their savings.

Grassroots Demand for Federal Public Option

Ulimately, state innovation, as exhibited here, can pave the road for comprehensive state reform, but is limited by its own borders. Yet, the willingness of state and city officials to actively pursue reform measures demonstrates both the systemic policy failure of our national retirement system and the political will to provide solutions.

In that sense, state action is evidence of a bipartisan, grassroots demand for a long-term, comprehensive federal option that can ensure all workers' retirement security.

The nature of the retirement crisis and our analysis of current federal and state level programs point toward what comprehensive reform might look like.

The optimal policy solution is Guaranteed Retirement Accounts (GRAs): mandatory, professionally managed accounts that supplement Social Security.

These accounts should be managed by the federal government so they will available to all American workers, and so it is not necessary for companies to navigate different policies in different states.

Workers and their employers whould split annual contributions of at least 3 percent of employee salaries to adequately close the gap between income from Social Security and the expert recommended income necessary for a secure and comfortable retirement.

To be effective, these accounts must be mandatory and early withdrawals prohibited. Reform should guarantee all workers the return of their principal plus an appropriate rate-of-return.

7. Tables

Table 1: States Taking Action on Retirement Reform

	Reform Legislation Status and Type			Potential to Provide Coverage	
State	Proposed	Enacted	Model Type	# of People Uncovered	% of People Uncovered
Arizona	1/22/2014		Auto-IRA	1,584,068	61%
Arkansas	1/26/2017		Marketplace	630,617	58%
California	2/23/2012	9/9/2016	Auto-IRA	9,300,934	59%
Colorado	3/24/2017		Auto-IRA	1,260,182	52%
Connecticut	5/13/2016	5/27/2016	Auto-IRA	801,632	49%
	1/23/2017		Marketplace		
Georgia	2/10/2017		Research	2,450,987	59%
Hawaii	2/7/2017		Research	240,322	42%
Illinois	1/1/2014	1/4/2015	Auto-IRA	2,833,769	53%
Indiana	1/13/2015		Auto-IRA	1,397,600	53%
Iowa	1/23/2017		Research	600,071	44%
Kentucky	2/3/2015		Auto-IRA	910,875	55%
Louisiana	3/10/2014		Auto-IRA	1,023,414	57%
Maine	4/9/2015		Marketplace	289,930	51%
Maryland	2/9/2015	5/10/2016	Auto-IRA	1,251,978	48%
Massachusetts	10/17/2011	3/22/2012	Public Admin DC (prototype)	1,638,608	56%
	1/23/2017		Hybrid		
Michigan	7/13/2016		Auto-IRA	2,060,746	52%
Minnesota	5/15/2017		Hybrid	1,112,013	45%
Montana	3/10/2017		Auto-IRA	211,722	50%
Nebraska	1/5/2017		Research	419,378	51%
Nevada	3/27/2017		Research	654,823	57%
New Hampshire	1/8/2015		Research	284,973	48%
New Jersey	1/11/2016	1/11/2016	Marketplace	1,984,216	53%
	5/18/2017		Public Admin DC (open MEP)		
New Mexico	1/20/2017		Research	423,176	58%
New York State	2/6/2017		Auto-IRA	4,322,137	54%
North Carolina	4/6/2017		Auto-IRA	2,226,003	56%
North Dakota	1/12/2015		Marketplace	174,289	51%
Ohio	10/2/2013		Auto-IRA	2,139,404	46%
Oklahoma	2/6/2017		Marketplace	855,373	57%
Oregon	2/10/2015	6/25/2015	Auto-IRA	870,355	52%
Pennsylvania	2/13/2017		Auto-IRA	2,562,505	50%
Rhode Island	4/14/2017		Auto-IRA	226,949	50%
South Carolina	3/9/2016		Research	1,071,828	57%
Tennessee	3/27/2017		Research	1,439,552	55%
Texas	3/9/2017		Hybrid	6,542,442	60%
Utah	1/25/2017		Voluntary IRA	625,892	53%
Vermont	3/21/2017	6/8/2017	Public Admin DC (open MEP)	145,488	52%
Virginia	1/6/2017		Research	1,721,596	49%
Washington	2/4/2015	5/18/2015	Marketplace	1,514,825	50%
West Virginia	3/6/2015		Research	316,821	50%
Wisconsin	6/21/2017		Research	1,154,332	46%
TOTAL	40			70,848,870	54%

Notes (Coverage): Non-self-employed private sector workers age 25-64 whose employers do not sponsor a retirement plan. Source (Coverage): ASEC 2015-2017 average.
Sources (Timeline): Pension Rights Center www.pensionrights.org/issues/legislation/state-based-retirement-plans-private-sector; Georgetown Center for Retirement Initiatives http://cri.georgetown.edu/

Table 2: Featured State Plan Attributes

		Guaranteed Retirement Accounts	Auto-IRA						Marketplace	Publicly-Administered DC		Hybrid			
	Location	USA	CA	CT	IL	MD	NY	OR	WA	MA	VT	MA	NYC	MN	TX
Characteristics	Account Type	Guaranteed Benefit	IRA	IRA	IRA	IRA	IRA	IRA	any	401(k)	401(k)	401(k), IRA	401(k), IRA	401(k), IRA	401(k), IRA
	Firm Size	All	>5	>5	>25	>5	All	All	<100	<20	<50	All	All	All	All
	Employee Contribution	1.5%	3%	3%	3%	3%	3%	5%	n/a	6%	TBD	TBD	Earnings & age-based	TBD	2 - 5%
	Employer Contribution	1.5%													
Strengths	Pooled Assets	✓	✓	✓	✓	✓	✓	✓		✓		✓	✓	✓	✓
	Employer and Employee Mandate	✓													
	Annuities	✓		✓	✓ (optional)	✓ (optional)		✓ (optional)					✓	✓ (optional)	✓
	Guaranteed Rate of Return	✓													
	Auto Enroll	✓	✓	✓	✓	✓	✓	✓			✓	✓	✓	✓	✓
	Portable	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓		✓
	Fee Limits	✓	✓	✓	✓	✓	✓		✓	✓		✓		✓	✓
	Universal Coverage (near)	✓	✓	✓	✓	✓	✓	✓				✓	✓	✓	✓
	Subject to ERISA	✓							Partial	✓	✓	Partial	Partial	Partial	Partial
Weaknesses	Hardship Withdrawals		✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	Limited		
	Opt-out		✓	✓	✓	✓	✓	✓		✓	✓	✓	✓	✓	✓
	Opt-in														

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