Testimony of The Pew Charitable Trusts

John Scott, Project Director, Retirement Savings

Before the House Committee on Labor

April 18, 2024

Good morning. Thank you, Chair Haadsma, Vice Chairs Mentzer and Wozniak, and members of the Committee for the opportunity to testify on retirement security issues and policy options. My name is John Scott, and I direct the retirement savings project at The Pew Charitable Trusts (Pew). Pew is a nonpartisan, non-profit organization that applies a rigorous analytical approach to solving public policy problems.

Retirement savings levels are low. According to data from government surveys and financial service providers, many Americans are struggling to save for retirement. For example, the investment manager Vanguard reports that the average amount saved for retirement among its 30 million clients is $112,572. The average is skewed, however, by high income savers. The median amount saved for retirement is $27,376, which means that half of all retirement accounts at Vanguard have less than that amount. The same median for those between the ages of 55-64, who are on the cusp of retirement, is just $71,168.[1] In other words, half of near-retiree account owners have less than $71,168, which most are expecting to last them 20 years or more. The Vanguard data covers only their participants with retirement accounts. But according to the Federal Reserve, about 1 in 4 non-retired Americans have no retirement savings at all.[2]

Lack of workplace retirement benefits is a driver of retirement insecurity. Workers not having enough retirement savings largely stems from not having workplace retirement benefits. Specifically, according to AARP:[3]

- Approximately 42% of Michigan workers in the private sector ages 18 to 64 – over 1.5 million in total – do not have access to a retirement plan at their job.
- Employees of small businesses are less likely to have access to a retirement plan. Among Michigan firms with under 10 employees, 73% of workers lack access to a retirement plan, and about 65% of such workers at firms with between 10 and 24 employees lack access to a plan.
- Retirement plan access also differs by race and ethnicity. In Michigan, 54% of Hispanic workers, 48% of Black workers, 37% of Asian American workers, and 40% of White workers lack access to a workplace retirement plan.

---

[1] Vanguard, 2023, "*How America Saves 2023*", Figure 55, https://institutional.vanguard.com/content/dam/inst/iig-transformation/has/2023/pdf/has-insights/how-america-saves-report-2023.pdf

[2] Board of Governors of the Federal Reserve System, May 2023, "*Report on the Economic Well-Being of US Households in 2022*", Figure 32, https://www.federalreserve.gov/publications/2023-economic-well-being-of-us-households-in-2022-retirement-investments.htm

[3] AARP, 2022, *Fact Sheet: Michigan*, https://www.aarp.org/content/dam/aarp/ppi/2022/state-fact-sheets/michigan.doi.10.26419-2Fppi.00164.024.pdf

Lack of access to retirement benefits is the result of a voluntary, employer-based system of employee benefits. If workers have retirement benefits, they receive them largely through employers. Of course, people can save on their own, but research from AARP shows that people are 15 times more likely to save through payroll deductions.[4] And for those working at a business with retirement benefits, the system can work well. However, many employers, and particularly small firms, find it difficult to offer retirement benefits due to high startup costs and a lack of administrative capacity.

In 2023, AARP surveyed businesses in Michigan with fewer than 150 employees.[5] All surveyed businesses were local firms as opposed to franchises. The survey found that employers offer retirement benefits primarily because doing so benefits their workers:

- A major reason was that a plan has a positive impact on employee attitude or performance (22%).
- Employers also said plans help attract and retain quality employees (29%).
- And offering a plan was the right thing to do (34%).

For employers without plans, the survey asked if they ever plan to offer a retirement savings plan, and 51% said they would not offer a plan at any point in the future. When asked why they did not provide retirement benefits, the top reason identified by respondents was that they were concerned about the cost to administer such a plan (72%) followed by the complexity of operating a plan (46%).

An aging population with insufficient retirement savings affects all Michigan taxpayers. As states face budgeting challenges, insufficient retirement savings will increase pressure on public assistance programs, reduce tax revenue, and decrease household spending by retirees. This will shift increasing fiscal costs onto a population of working-age taxpayers that is not growing.

Pew commissioned Econsult Solutions, an economic consulting firm, to quantify the fiscal costs of insufficient retirement savings nationally and in Michigan. The results indicate that the number of Michigan households with residents aged 65 and older is expected to increase by 36%, going from 1.1 million in 2020 to just over 1.5 million by 2040.[6] The working-age population will not keep up with this growth in the older population, resulting in an expected 45% increase in the ratio of retirement-age households to those of working age from 2021 to 2040.

---

[4] AARP, 2023, "State Programs, Federal Incentives Spur Rise in 401(k)s," https://www.aarp.org/retirement/planning-for-retirement/info-2023/rise-in-401k-benefits.html.

[5] AARP, 2023, "Michigan Small Business Owners Support a State Retirement Savings Option for Workers," https://www.aarp.org/pri/topics/work-finances-retirement/employers-workforce/michigan-saves-retirement-survey.html.

[6] EConsult Solutions, May 2023, *"The Cost of Doing Nothing: Federal and State Impacts of Insufficient Retirement Savings"*. https://econsultsolutions.com/wp-content/uploads/2023/05/Impacts_of_Insufficient_Retirement_Savings_May2023.pdf

To maintain the living standards enjoyed by households during their working years, financial advisors recommend an "income replacement" target of 75% of the household's average income between ages 45 to 64. Looking at households that receive less than $75,000 in income, who are considered economically vulnerable, the study estimates that by 2040, the shortfall in annual retirement income for these vulnerable households relative to that target will be $9,030. As these individuals age, inadequate retirement savings will further reduce their retirement income and hence the quality of life for many.

This shortfall in retirement income means that some Michigan households will need help in the form of Medicaid and other assistance programs. Over the 20-year period of 2021 through 2040, the cumulative costs to Michigan of additional state social assistance program spending due to insufficient retirement savings will reach <u>$11.15 billion.</u>

But there's good news: Even small savings now could help offset the effects of this shortfall. If all Michigan households saved, on average, just an additional $2,155 a year—$180 a month—over 30 years, they could erase the additional $11.15 billion taxpayer cost and ensure retiring households can maintain the living standards they enjoyed during their working years. Even if all households do not save this full amount, a modest increase in savings will reduce the fiscal cost of insufficient savings.

<u>States are implementing solutions to boost retirement savings and reduce taxpayer burdens.</u> States have taken multiple approaches to expand access to retirement savings opportunities to more workers and their families. The most popular state-facilitated program is the automated savings program, also called work & save, secure choice, or auto-IRA. These programs combine payroll deductions, in which wages are deducted and sent directly to an employee's personal IRA, with the same automatic enrollment often used in 401(k) plans. In practice, the state requires that private-sector employees without an employer-sponsored plan at their job be automatically enrolled, with the ability to opt out at any time. Only employers who do not offer plans are required to participate, and their only role is to enroll workers and facilitate payroll deductions.

An automated state savings program can use either a traditional or Roth IRA, but in practice all active states use a Roth IRA, which is funded with post-tax contributions. Investments usually include a range of low-cost mutual funds and other fund options managed by an outside investment firm. Employees can withdraw their contributions tax- and penalty-free for any reason and own their IRAs; neither the state nor employers can control their savings. Participant fees are kept low through the economies of scale in a statewide program with hundreds of thousands of savers. Like the 529 college savings plans, these programs are a public-private partnership with investments professionally managed by a third-party financial firm overseen by the state.

<u>Data and research show the success of state automated savings programs.</u> Sixteen states have already adopted state automated savings programs, and in the last seven years, eight of those programs became active (California, Colorado, Connecticut, Illinois, Maine, Maryland, Oregon, Virginia). The remaining states (Delaware, Hawaii, Minnesota, Nevada, New Jersey, New York, Vermont, and Washington) have passed legislation and are working on implementation.

Recent data from the established programs in California, Colorado, Connecticut, Illinois, Maryland, and Oregon show:[7]

- Over 845,000 savers have funded accounts.
- Savers have already amassed over $1.3 billion in assets.
- Over 212,000 employers have registered for these programs.
- Two-thirds of workers chose to participate and save with average savings ranging from $107 to $280 per month.

Because of their wide adoption, Pew has spent considerable time and effort looking at automated savings programs in terms of how they affect employers, employees, taxpayers, and the private market for retirement plan products and services.

Research shows automated savings plans are well received by employers and workers. In 2020, Pew surveyed participating employers in Oregon—the first state to launch an auto-IRA program, OregonSaves—to assess their views, and nearly three in four (73%) said they were either satisfied or neutral about the program. OregonSaves doesn't charge businesses any fees, and 79% said that they haven't experienced any related out-of-pocket costs. Employees also are having positive experiences. Four out of five (80%) surveyed employers said that they're fielding few or no questions from their employees about the program.[8]

Employers in other states have also eagerly responded to automated savings programs with a no-cost retirement benefit. In California in 2022, nearly 33,000 businesses had enrolled in the state's program more than three months before the scheduled deadline.[9] In Oregon, 27% of eligible businesses joined the program at least 90 days before they were required to do so.[10]

Do these programs work for employees? Pew recently conducted a survey of workers in the Illinois program, and almost two-thirds—62%--were satisfied with their program experience versus only 5% who expressed dissatisfaction. More importantly, 38% said the program made them feel more financially secure versus only 14% who felt that the program made them feel less financially secure.[11]

State savings program also complement the existing private market for retirement plan products and services. As currently operated in other states, the automated savings model should not replace existing retirement plans and should not compete with private retirement plan service providers and financial firms. For example, 401(k) plans offer significantly higher

---

[7] Georgetown University Center for Retirement Initiatives, 2023, State Program Performance Data, https://cri.georgetown.edu/states/state-data/current-year/

[8] The Pew Charitable Trusts, 2020, "Employers Express Satisfaction with New Oregon Retirement Savings Program," https://www.pewtrusts.org/en/research-and-analysis/articles/2020/07/30/employers-express-satisfaction-with-new-oregon-retirement-savings-program

[9] CalSavers, 2022, "Participation & Funding Snapshot as of 3/31/2022," https://www.treasurer.ca.gov/calsavers/reports/participation/march-2022.pdf

[10] The Pew Charitable Trusts, 2020, "Employers Express Satisfaction with New Oregon Retirement Savings Program," footnote 7.

[11] The Pew Charitable Trusts, 2022, "Many in Illinois Retirement Savings Program Feel Their Financial Security Is Improving," https://www.pewtrusts.org/en/research-and-analysis/articles/2022/04/18/many-in-illinois-retirement-savings-program-feel-their-financial-security-is-improving

annual contribution limits than the state programs, usually provide a wide range of investment alternatives, and allow employers to make their own contributions to employees' accounts.

Pew examined federal data on employer-sponsored retirement plans to compare new plan adoption rates in states with automated savings programs relative to states without such programs. While the existing state programs are still new, Pew's analysis found evidence that employers are still adopting their own retirement plans. California, Illinois, and Oregon show a higher rate of increase in new plans adopted by employers following the adoption of a statewide automated savings program relative to states without such programs. In other words, rather than competing with the private market for retirement products, state programs complement the private market.[12] These results make sense because many employers don't offer retirement benefits until they've reached a point of financial stability. Thus, the advent of a state automated savings program may be nudging those employers who have been contemplating whether they should adopt their own plan to move forward.

<u>The Retirement Savings Program Act (H.B. 5461) would address retirement insecurity in Michigan</u>. H.B. 5461 would create an automated savings program for private-sector workers in Michigan who work for an employer that does not offer a private retirement plan. The following summarizes the program created in this legislation:

<u>Employers:</u> Michigan employers with one or more employees, that have been in business for at least 730 days since their first payroll, and do not offer a federally qualified retirement plan to their employees, will be required to facilitate the program, at no cost to the employer. The only requirement on the employer is to register with the program, upload an employee census, and process payroll deductions. Employers are not plan sponsors or fiduciaries and cannot make contributions to employee accounts; all reporting requirements are undertaken by the state program.

- According to the AARP's survey of Michigan small business, noted above, most (73%) of small business owners would support legislation to establish a privately managed, state retirement savings program – as provided for in H.B. 5461 – for their workers.[13]

<u>Employees</u>: Employees are automatically enrolled to begin saving via payroll deduction into their own post-tax Roth IRA but may change their contributions or opt-out at any time. Savers can access their contributions at any time, including for unexpected financial emergencies. The accounts are fully portable and remain with the individual, even if they change jobs or leave the state.

<u>Governance</u>: The program is governed by a seven-member board, which determines the program defaults (i.e., the contribution rate, investment type, and escalation of contributions), and contracts with private, third-party entities for program administration and investment management.

---

[12] The Pew Charitable Trusts, 2023, "State Retirement Programs Continue to Complement Private Market Plans," https://www.pewtrusts.org/en/research-and-analysis/articles/2023/04/14/state-automated-retirement-savings-programs-continue-to-complement-private-market-plans.

[13] AARP, "Michigan Small Business Owners Support a State Retirement Savings Option For Workers," footnote 4.

Pew has evaluated this legislation, and the act aligns with best practices and incorporates programmatic lessons learned from existing state programs. Pew has performed significant research on these programs and views this policy as successful in addressing the retirement savings access gap for the private-sector workforce. For the reasons stated above, Pew supports this legislation.

* * *

In conclusion, Pew commends the Committee for its work on these critical issues and respectfully requests the Committee support the Retirement Savings Program Act (H.B. 5461). Thank you again for this opportunity to provide our views, and I would be pleased to answer questions.