The Pew Charitable Trusts

Written Statement of John Scott, Director, Retirement Savings Project
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Thank you, Madam Chairwoman and Ranking Member Casey, for the opportunity to testify on the importance of financial security in retirement. My name is John Scott, and I am the director of the retirement savings project at The Pew Charitable Trusts (Pew). Pew is an independent nonpartisan, non-profit organization that applies a rigorous analytical approach to improve public policy. I want to commend the chair and the ranking member for holding this hearing on a topic of great importance to our country.

For many Americans, saving through a workplace retirement plan is the primary vehicle for ensuring financial security in old age, but coverage is not universal. Overall, one-third of private sector workers lack access to a retirement plan at their jobs, and some workers do not participate even when their employer offers a plan. Only 28 percent of full-time workers without access to employer-sponsored plans report having any other retirement savings through alternative approaches, such as an IRA or a 401(k) from a previous employer.

Gaps in retirement plan coverage affects not just workers' retirement security. Federal, state and local governments—as well as the larger economy—will likely face higher costs and reduced output.

A study by the University of Maine, for example, found that in 2016 spending for Mainers between 65-79 years old receiving social services such as Medicaid, SSI, SNAP and housing assistance reached $164 million, with about $28 million financed by the state. Maine's retirement age population, those persons over 65, was projected to increase 30 percent between 2016 and 2032. The cost of those social services is expected to increase to $362 million in 2032, with the state's share growing to $61 million or 2.2 times greater than in 2016.

A similar Pennsylvania study found that the commonwealth spent an estimated $702 million in public assistance costs and lost about $70 million in tax revenue in 2015 due to insufficient retirement savings by Pennsylvania residents. Net costs for inadequate retirement savings are projected to grow to $1.1 billion by 2030 and total a cumulative $14.3 billion from 2015-2030.

Increasing the number of workers saving for retirement, and boosting their rate of savings, would have a substantial and positive impact on individual financial security as well as on the country's fiscal and economic situation.

Barriers facing workers

To help provide guidance on what encourages or prevents people from saving for retirement, Pew conducted a nationally representative survey of private sector workers at small to midsize businesses with five to 500 employees. Workers at small businesses have especially low levels of access to a retirement plan. According to the Department of Labor, only 49 percent of employees at firms with less than 50 workers have a workplace retirement plan, compared to 83 percent of those at firms with more than 100 workers.

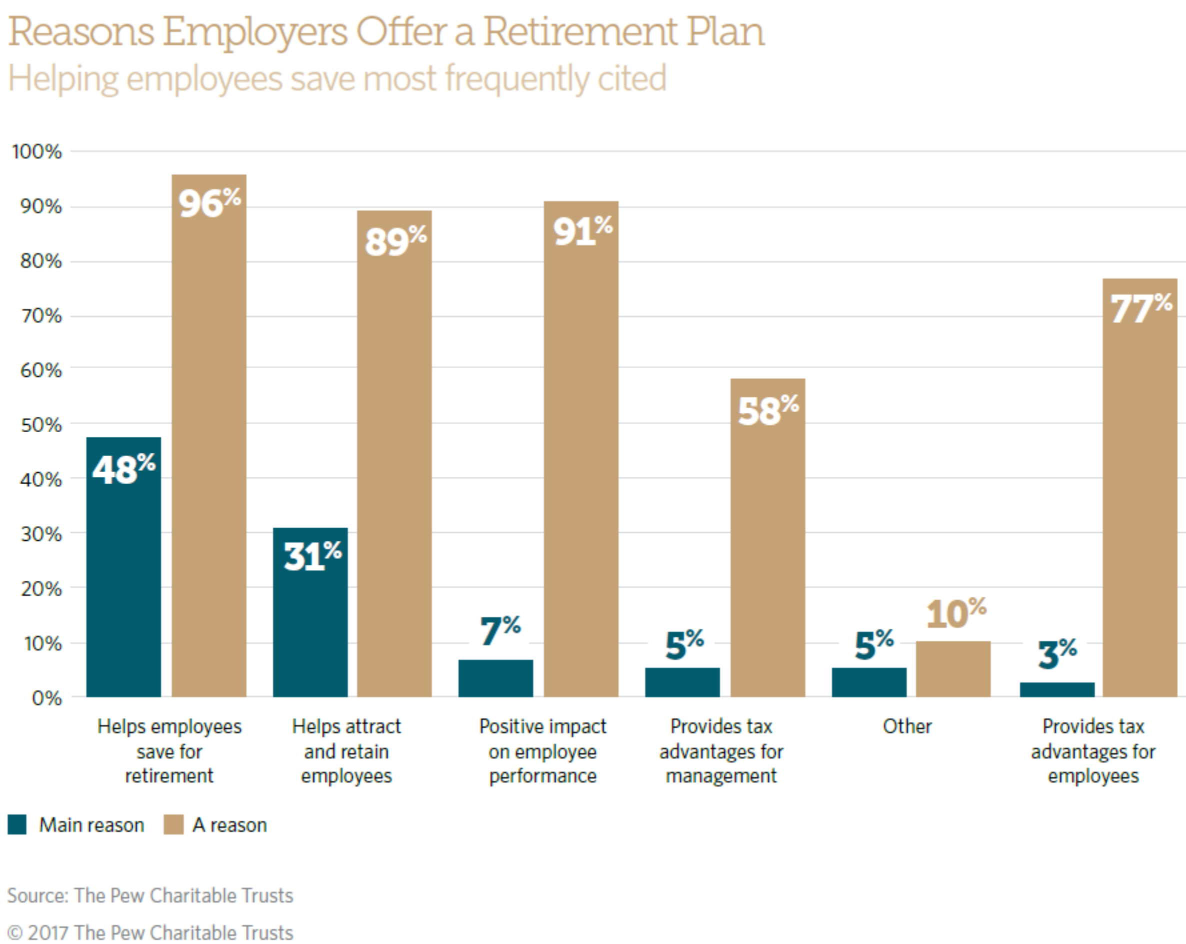
Pew's survey found that whether workers have access to employer-sponsored retirement plans differs by type of work and worker characteristics. Among the key findings:

- Part-time workers, those with lower wages, and those who had experienced unemployment for an extended period are less likely than other employees to have access to a workplace plan.
- Access to a retirement plan also varies by education level. For example, full-time workers with at least a bachelor's degree are more than twice as likely as those with less education to have any retirement plan.
- Race, ethnicity and gender can also affect retirement plan coverage. Hispanic full-time workers have less access to plans than white full-time workers. Specifically, across racial groups, white full-time workers are three times as likely as Hispanics to have any plan (even when controlling for industry in regression models). And women are more likely than men to have any retirement savings.
- Plan access can vary by industry: Workers in wholesale and retail trade businesses, for example, are less likely to have a workplace plan than those in other industries.

Employer characteristics also matter.

To improve retirement security and to reduce future government spending on social services for the elderly, policymakers are looking at ways to increase access to private sector employer-sponsored retirement plans, particularly among small businesses. When crafting their approaches, understanding why some small employers offer plans and others do not may be useful to policymakers. In 2016, Pew conducted a survey of owners, top executives, and human resource managers at more than 1,600 private sector, small and midsize businesses nationwide—one of the first high-quality small business surveys conducted in 10 years. One focus of the survey was to identify the obstacles to, and motivations for, offering plans and to gather data on what plans are currently offered and plan characteristics.

First, the survey found that employers offered various reasons for providing retirement plans. Almost all—96 percent—cited a desire to help employees save for retirement, and 48 percent identified it as the main reason. In Pew focus groups conducted prior to the survey, small to midsize employers repeatedly said that offering a retirement plan helped them to attract quality employees. In the survey, 91 percent said they felt that offering a retirement plan had a positive impact on employee performance, while 89 percent said doing so helped attract and retain employees. Nearly a third—31 percent—said attracting and retaining workers was the main reason they offered a plan. Tax advantages for management and employees were cited much less often as main reasons (5 percent and 3 percent, respectively).



In terms of characteristics associated with plan sponsorship, firm financial stability emerged as a key factor. For example, employers that reported that earnings increased over the past 2 years were 41 percent more likely to offer a plan than if earnings had remained flat.

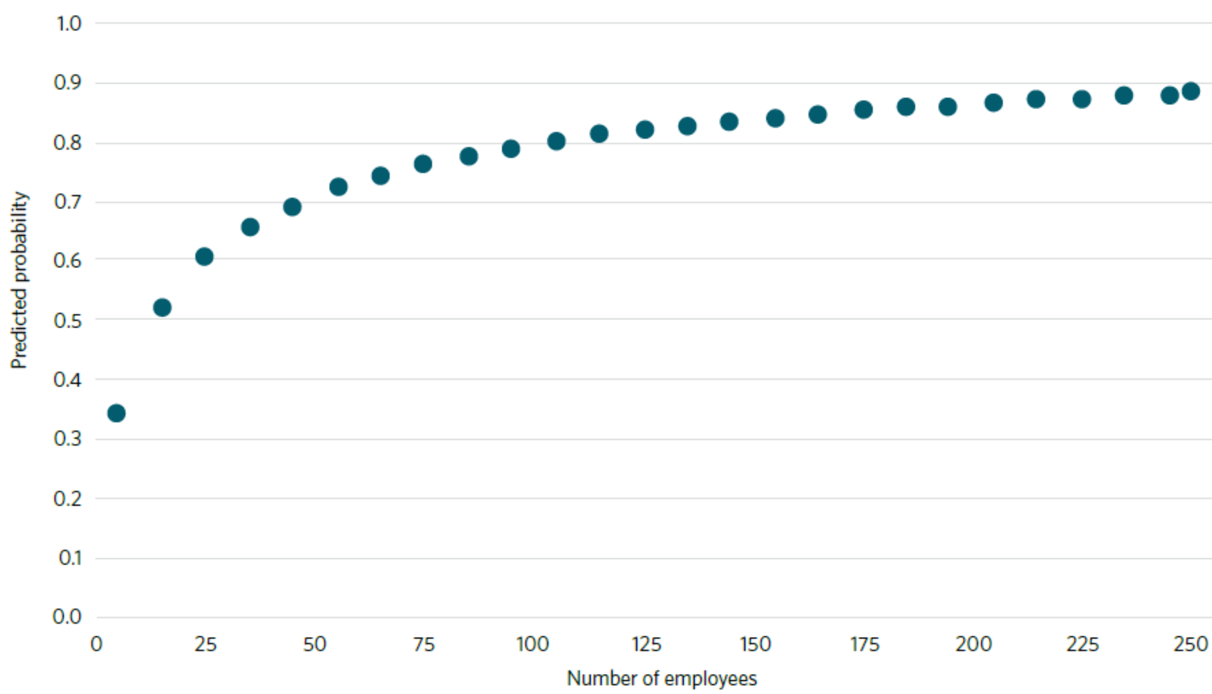
The type of business matters, too. Incorporated businesses are 1.8 times more likely to offer a plan than nonincorporated businesses, even when controlling for the number of employees.

Corporate status may signal that a firm is growing or stable enough to support offering more benefits.

Not surprisingly, larger, older businesses are more likely to offer plans, but the relationship is not linear. Businesses are more likely to adopt plans in the early stages of growth, but that likelihood tapers off after a certain point. For example, the probability that the average business with five employees offers a retirement plan is just 34 percent, while the probability for the average business with 55 employees to do so is a little more than twice that—72 percent. The probability continues to grow as staffing increases, but at a much lower rate.

Probability of Offering a Retirement Plan by Number of Employees

The likelihood increases most rapidly among smaller businesses



Note: In the left-hand column, a probability of 1 represents a 100 percent likelihood that a business offers a retirement plan. The probability rises fastest as a business's staffing grows to about 75 and then levels off as the number of employees increases.

Source: The Pew Charitable Trusts

Businesses with a higher percentage of full-time workers also are more likely to offer a plan that those with more part-time employees. On average, there is a 66 percent likelihood that a firm that employs all full-time workers will offer a plan compared with a 44 percent chance for a company with a workforce divided evenly between full- and part-time workers.

Meanwhile, a 3-year-old firm is 25 percent more likely to offer a retirement plan than a 1-year-old firm. That increase in probability diminishes as companies age. For example, one in business for 13 years is only 3 percent more likely than one in business for 11 years to offer one.

These results suggest that businesses tend to adopt plans during a “middle” phase in their development, after startup and during a period of expansion and growth. At such a time, retirement benefits may be an attractive tool for hiring and retaining talented employees when an employer already has provided other benefits to workers, such as health insurance. When addressing barriers, such as limited knowledge and startup costs, state policies could specifically target younger, less established businesses.

Several plan features such as employer contributions can improve workers’ financial security. Employers in the Pew survey were likely to contribute to workers’ plans. Among those with defined contribution plans, 89 percent contributed to their plans, and 82 percent of those that contributed said they match worker contributions.

Automatic enrollment is another feature that can affect participation. When a worker is automatically enrolled in a plan, contributions are set at a default rate, such as 3 percent of his or her wages or salary, with the employee able to opt out of the plan or change the contribution level. Auto-enrollment serves to overcome a worker’s inaction, since many workers are stymied by the complex or overwhelming information retirement plans provide. The Pension Protection Act of 2006 authorized employers to automatically enroll workers and, increasingly, private sector employers are automatically enrolling new hires into 401(k) plans.

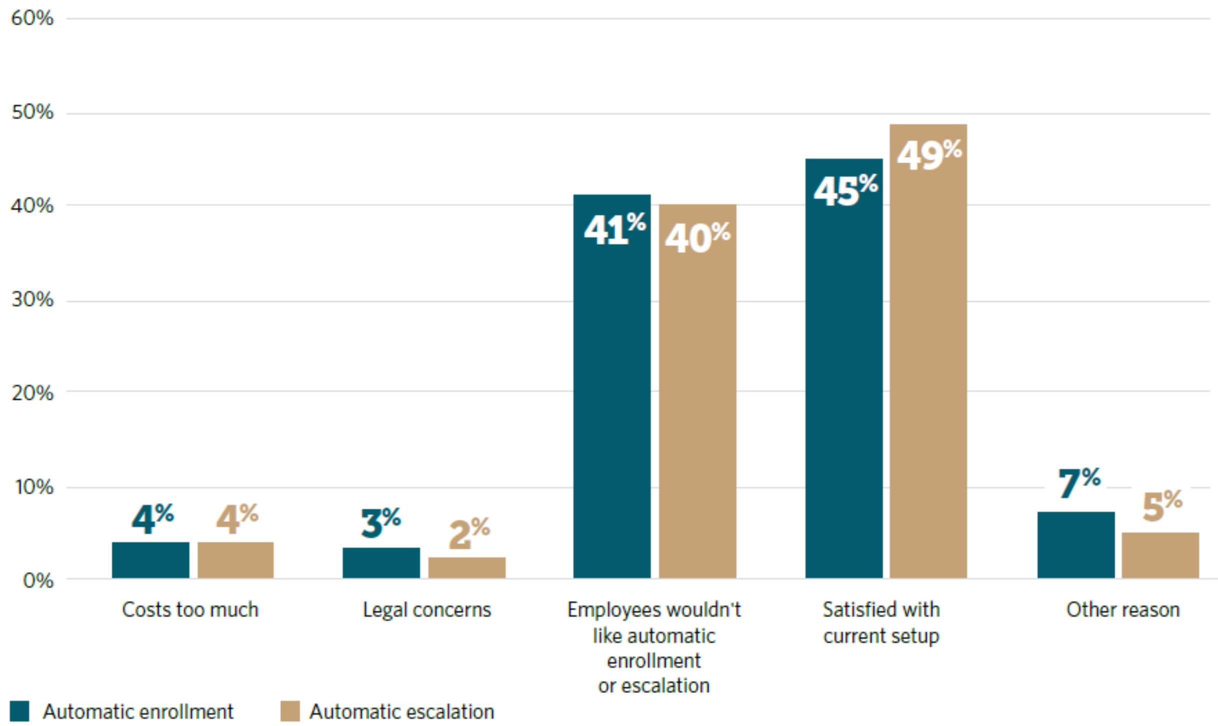
According to client data from the mutual fund company Vanguard about the plans it manages, 46 percent of retirement plans use automatic enrollment, up from 20 percent in 2008, with the percentage varying greatly by company size: 65 percent of plans with 5,000 or more participants use auto-enrollment, but only 30 percent of plans with 500 or fewer participants do so. The effect is dramatic: Looking again at Vanguard’s database, 92 percent of employees participated in auto-enrollment plans, with only a small percentage opting out, while 57 percent enrolled in voluntary plans.

Relatively small percentages of small business plan providers, however, use plan options such as automatic enrollment. In Pew’s survey of small employers, about a third automatically enroll their workers, while about a sixth use automatic escalation, which increases employee contributions annually until a certain maximum percentage is met. About 48 percent of employers said they offered retirement benefits primarily to help their workers save. Still, those who said this was a reason were no more likely to use these pro-savings features than those who did not cite this as a reason they offer benefits.

When asked why they do not offer features that encourage participation and savings such as automatic enrollment or automatic escalation, executives were most likely to say their businesses were satisfied with their current setup (45 percent in response to automatic enrollment and 49 percent in response to automatic escalation). In addition, about 4 in 10 said that employees would not like automatic enrollment (41 percent) or automatic escalation (40 percent). Few cited legal or cost concerns.

Reasons Employers Do Not Offer Automatic Enrollment or Automatic Escalation

Many unsure that employees would like either approach



Source: The Pew Charitable Trusts

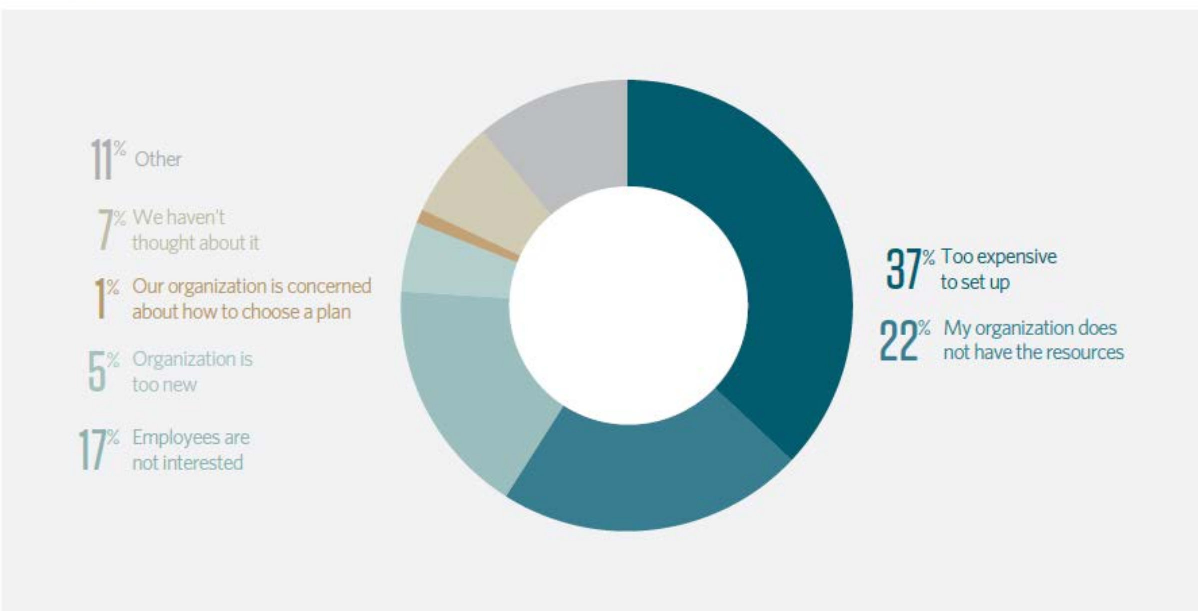
Smaller business owners and their workers may not be as familiar with the workings and benefits of auto-enrollment and auto-escalation. Even if familiar with them, however, small employers may have concerns about how their employees would react to these features. Unlike larger corporations, these employers have more direct involvement with employees and are more aware of their attitudes and specific preferences.

Small employers without retirement plans

Many employers said they would like to offer retirement savings options but feel they face numerous barriers to doing so. Some business representatives in focus groups held as part of the survey cited limited demand for retirement benefits because their workers earned low wages or were working short term, in addition to the costs and resources required to start and maintain a plan. The survey data generally support all these focus group findings regarding barriers. Policies that take a multipronged approach can help to address the range of possible barriers.

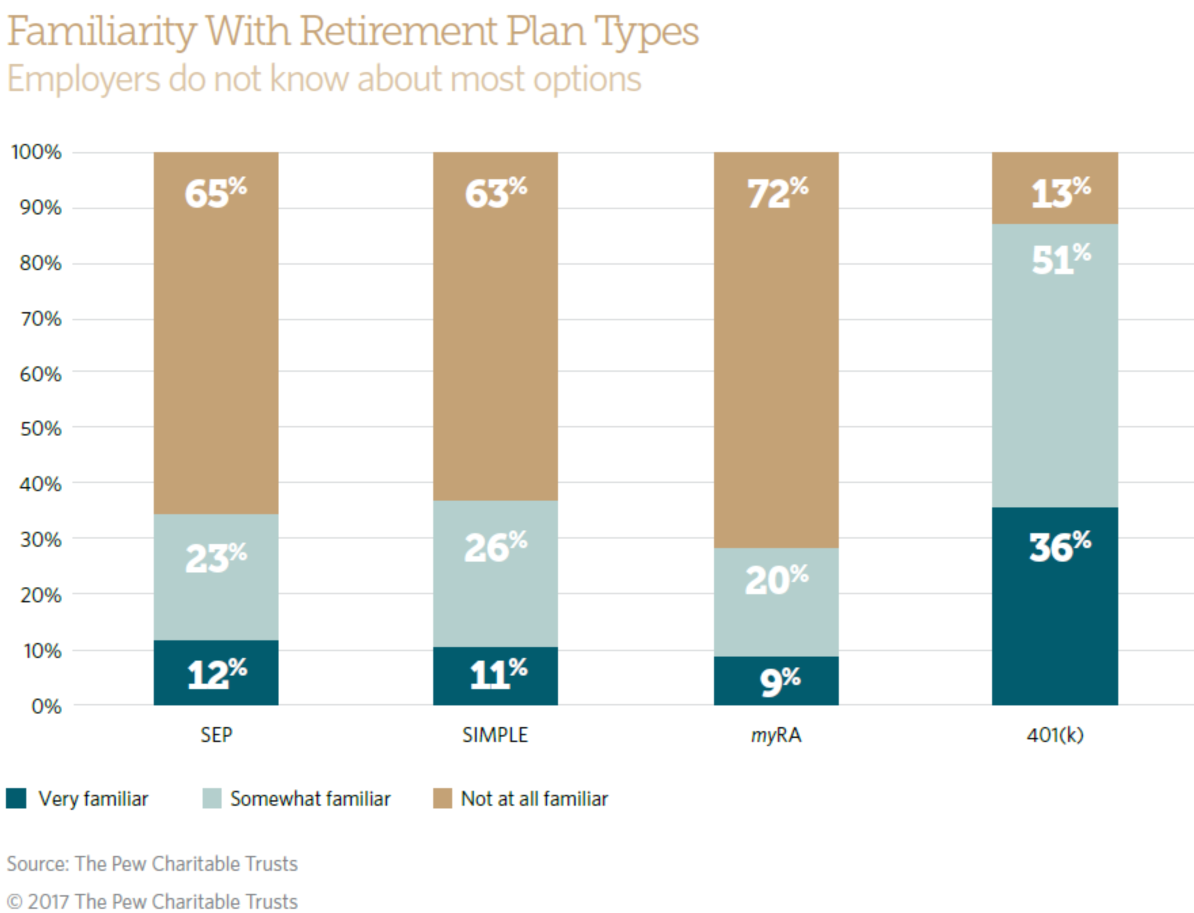
Most commonly, employers without plans said that starting a retirement plan is too expensive to set up (37 percent). Another 22 percent cited a lack of administrative resources. In focus groups, some business representatives said their mix of workers—especially if they included low-wage or short-term employees—translated into limited employee interest in or demand for retirement benefits. But in the survey, only 17 percent cited lack of employee interest as the main reason they did not offer a plan.

Main Reason Cited by Employers for Not Offering a Retirement Plan
Setup cost chosen most often



Source: The Pew Charitable Trusts

Lack of familiarity with retirement plan options also can prove to be a barrier to providing one. In the survey, 11 percent of employers said they were not familiar with 401(k) plans, SEPs, and SIMPLE plans. Just 13 percent said they were at least somewhat familiar with all options, while 34 percent said they were only familiar with the 401(k). Leaders of small and midsize businesses were much less familiar with the other three alternatives, even though SEPs and SIMPLE programs are specifically intended to appeal to smaller employers because they are cheaper to establish and administer.



When businesses without a retirement plan were asked which circumstances were most likely to motivate them to begin one, the most common responses were a change in their financial situation or government incentives. Some 67 percent said increased business profits would make them somewhat or much more likely to start a retirement plan. Similarly, 60 percent said they would be somewhat or much more likely to start a plan if there were increased business tax credits for doing so. On the other hand, majorities said that availability of easy-to-understand information (58 percent), tax advantages for key executives (55 percent), or reduced administrative requirements (53 percent) would make them no more likely to offer plans.

Policy innovations

The research has several implications for policy, and there are many promising ideas and initiatives being worked on today. Let me note that Pew does not endorse or oppose any particular initiative.

However, I want to commend Chairwoman Collins for her leadership in introducing legislation, such as the Retirement Security Act (S. 1383 in the 115th Congress), that emphasize key areas for action such as encouraging auto-enrollment, opening up multiple employer plans, improving SIMPLE IRA plans, and increasing tax credits for startup costs.

As noted above, many small business owners are not familiar with plan options that are designed for small firms. In addition, the perceived high cost of starting a plan is deterring small employers from offering retirement benefits. Policy initiatives that reduce plan startup costs and improving awareness of SIMPLE and SEP plans could be useful in encouraging new plans.

And our research has found that executives of small to midsize businesses also saw benefits to the idea of a multiple employer plan (MEP), which allows employers to combine to offer a single plan that achieves economies of scale and lower costs. Despite covering multiple businesses, MEPs are structured similarly to a traditional plan, meaning employers can make matching contributions. Under a MEP, service providers take on much of the fiduciary responsibility, which reduces, but does not eliminate, an employer's own fiduciary duties. Because employers take a more active role in a MEP, states cannot require participation—unlike a state-sponsored auto-IRA where employer responsibilities are more limited.

Pew's survey of small business executives found that 85 percent of employers said they would find a MEP somewhat or very helpful. Most businesses without a plan strongly or somewhat supported each of the individual elements of the MEP. Ninety-two percent liked the idea that the plan would allow employees to have choices in how their contributions are invested. But although employers said they would find such a plan helpful, it is unclear how many would voluntarily adopt one if offered. Some 61 percent of employers without plans said they would definitely be or might be interested in participating in such a program.

Expanding the use of auto-enrollment in particular could boost participation, as noted above. At the state level, several states–California, Connecticut, Illinois, Maryland and Oregon–are in various stages of implementing an automatic enrollment payroll deduction IRA program for private sector state residents who do not have a retirement plan at their work. To date, the use of auto-enrollment at the state level is encouraging: For example, in the State of Oregon, 2,899 employers have registered to facilitate OregonSaves for their employees. In total, 62,888 employees (72 percent of those eligible) have enrolled in the program. On average, employees contribute about $100 per month, and assets in the program now exceed $12.5 million. The average savings rate is currently 5.6 percent.

In summary, while improving retirement plan coverage among small employers remains difficult, we have a better sense from research of what improvements could be effective in increasing coverage and participation. But as you know, more work needs to be done, and in that regard I would commend the 2017 GAO report that calls for a comprehensive examination of the retirement system.

Thank you again for the opportunity to testify, and I would be pleased to answer your questions.