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SECURE 2.0 AND THE PAST AND FUTURE OF THE U.S. RETIREMENT SYSTEM

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ABSTRACT

The SECURE 2.0 legislation, passed in December 2022, is the most extensive set of changes to retirement law in the last 15 years. In this paper, we place SECURE 2.0 in the context of the ongoing evolution of the retirement system, summarize its key provisions, and discuss the need for additional reforms. Because 2024 marks the 50th anniversary of the passage of ERISA, assessing the broad arc of retirement policy and behavior is particularly timely. Previous reform efforts, including automatic 401(k)s, Automatic IRAs, and the saver's credit, aimed to make retirement saving easier and more rewarding for rank-and-file workers. More recently, SECURE and SECURE 2.0 improved and expanded the saver's credit (renamed the saver's match), expanded automatic enrollment, and extended plan participation to more part-time employees. They also facilitated multiple-employer plans and took steps to improve account portability and disclosure, reduce pre-retirement leakage, facilitate emergency saving, and promote better options to convert savings into retirement income. However, there are still important avenues for policy to make the retirement system more equitable and effective. Particularly important are eliminating the coverage gap and closing the racial, ethnic, and gender gaps in retirement wealth. Other key goals include helping workers convert savings into reliable lifetime income; encouraging people to work longer; reducing pre-retirement leakage, including by ensuring that retirement savings can follow workers from job to job; and exempting smaller savers from the required minimum distribution rules.

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DISCLOSURES

Iwry periodically provides, in some cases through J. Mark Iwry, PLLC, policy and legal advice to plan sponsors and providers, government officials, academic institutions, other nonprofit organizations, trade associations, fintechs, and other investment firms and financial institutions, regarding retirement and savings policy, pension and retirement plans, and related issues. Iwry is a member of the American Benefits Institute Board of Advisors, the Board of Advisors of the Pension Research Council at the Wharton School, the Council of Scholar Advisors of the Georgetown University Center for Retirement Initiatives, the Panel of Outside Scholars of the Boston College Center for Retirement Research, the CUNA Mutual Safety Net Independent Advisory Board, the Executive Committee of the Improving Taxation Project, and the Aspen Leadership Forum on Retirement Savings Advisory Board. He also periodically serves as an expert witness in federal court litigation relating to retirement plans. The authors did not receive any financial support from any organization or person for any views or positions expressed or advocated in this document. They are currently not an officer, director, or board member of any organization that has compensated or otherwise influenced them to write this paper or to express or advocate any views in this paper. Accordingly, the views expressed here are solely those of the authors and should not be attributed to any other person or organization.

During his service in the U.S. Treasury Department as Benefits Tax Counsel, Deputy Assistant Secretary (Tax Policy), and Senior Advisor to the Secretary with responsibility for national retirement and health care policy (1995-2001, 2009-2017), Iwry was involved in initiating, directing, or overseeing the development, proposal, advocacy for, and/or implementation of many of the legislative, regulatory, and administrative policies provisions, proposals, and guidance discussed in this paper, including payroll deduction IRAs; automatic enrollment and automatic asset-allocated investing; the saver's credit and saver's match; payroll deduction IRAs; the SIMPLE-IRA; automatic rollover of small benefits from plans to IRAs; provisions and guidance expanding portability and rollovers; inclusion and formulation of the Automatic IRA proposal in Obama Administration budgets and in proposed legislation; the QLAC; annuities embedded in QDIA target date funds; rollover of DC plan lump sums to DB plans to purchase lifetime DB pensions; guidance prohibiting corporate plan sponsor buybacks of DB pensions in pay status; emergency savings draft guidance; regulatory safe harbor protection for and permission to use myRAs in state-based auto IRA programs; legislative exemption of all but large plan and IRA balances from required minimum distributions; variable DB and defined ambition plans; multiple employer and pooled employer plans (MEPs/PEPs); long-term part-time employee participation, and other provisions ultimately enacted in the SECURE and SECURE 2.0 legislation.

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Once dominated by employer-sponsored pensions,

the U.S. retirement system has evolved steadily to one where most private sector workers have access to retirement savings accounts. These accounts increasingly embody features rooted in behavioral economics—including automatic enrollment and default investment options. This gradual evolution has been driven by a mix of changing demographics, employers' desire to reduce their risks and pension costs, and incremental policy reforms at the federal and state levels intended to improve retirement security for more people.

The SECURE 2.0 Act of 2022 ("SECURE 2.0"), passed in December 2022, is the most extensive set of changes to retirement law in the last 15 years. In this paper, we place SECURE 2.0 in the context of the ongoing retirement evolution, summarize certain key provisions, and discuss the need for additional reforms. Because 2024 marks the 50th anniversary of the passage of ERISA, assessing the broad arc of retirement policy and behavior is particularly timely.

The paper is organized in several sections. The first section below briefly describes the evolution of the retirement system in the last quarter of the 20th century, from a system where pensions—specifically employer-sponsored defined benefit plans—were predominant to one where 401(k)-type plans and individual retirement arrangements (IRAs) became increasingly important. The ascension of 401(k) plans and IRAs as the main retirement vehicles for rank-and-file workers shifted most of the financial risks onto individuals and created a host of related problems. Addressing these issues has been the principal focus of retirement policy over the past 25 years.

The second section discusses a series of previous reform efforts that aimed to make retirement saving easier and more rewarding for the majority of workers. These policies include the development and promotion of automatic 401(k)'s, Automatic IRAs, and the saver's credit. These changes are gradually moving the retirement system in the right direction, but many more reforms are required.

The third section discusses the more recent evolution of retirement policy, embodied in the SECURE (2019) and SECURE 2.0 (2022) legislation. These changes include improving and expanding the saver's credit (renamed the saver's match), helping savers manage their accounts during their working years by improving portability and disclosure, reducing pre-retirement leakage, and facilitating emergency saving. Importantly, these two bills aim not only to help workers accumulate more resources for retirement, but also to help savers better convert their savings into retirement income.

A concluding section discusses additional steps to create a more equitable and effective defined contribution system that utilizes proven behavioral strategies to achieve better retirement outcomes. Some of these include eliminating the coverage gap so that everyone can supplement their Social Security with retirement savings, increasing focus on closing racial, ethnic and gender gaps in retirement wealth, creating better options to convert savings into lifetime retirement income, introducing policies that encourage people to work longer, taking steps to ensure that retirement savings would follow workers from job to job, and providing reforms to the required minimum distribution rules.

I. The Retirement System in the Late 20th Century

A. DEFINED BENEFIT PLANS

ERISA—the Employee Retirement Income Security Act of 1974—reshaped the laws governing private pensions in the U.S. But even as ERISA began to take effect, the basic nature of the system it was intended to reform—one dominated by defined benefit (DB) pension plans—was changing. The past half century has seen a secular, systemic shift away from a system in which private-sector workers who had retirement coverage often had access to DB plans, which provided meaningful, regular retirement income to millions of middle-income households. However, even in this era, coverage was far from universal.

Traditionally, DB plans were established, funded, and managed by employers for their employees or by unions for their members. Designed mainly to augment Social Security benefits, the funds provided by employers, often pursuant to collective bargaining agreements, were invested collectively and professionally. With benefit formulas based largely on the level of an employee's wages and length of service, the plans aimed mainly to pay a lifetime, guaranteed stream of monthly income (although, typically, the payments were not fully adjusted for inflation). The plans insulated workers against many sources of uncertainty, including risky asset returns, counterparty risk, longevity risk, and the risks associated with poor choices regarding how much to contribute, how to invest the funds, and how much or how quickly to withdraw funds in retirement.

DB plans minimize the need for workers to take initiative or make decisions. Under the DB framework, the employer or union sponsoring the plan makes contribution and investment decisions, and also bears the risk in terms of investment returns and employee longevity. Workers, in effect, swap administrative responsibilities, investment risk, and longevity uncertainty for the risks of pension underfunding (which ERISA mitigated to some extent by creating a federal insurance program), lack of benefit portability, and the significantly larger chance of losing their benefits due to job change, unemployment, or if their employer terminates the plan before a worker can accumulate a significant benefit. At the time, many DB plans required employees to serve for many years before a worker qualified for their benefits. As a result, not only did many workers receive nothing at all, but many others also received only a small benefit.

ERISA did not require employers or unions to offer retirement plans, but if pension promises were made, ERISA generally sought to ensure that they were kept and that plans were structured in a way that generally protected covered workers' reasonable expectations. The law obligates plan sponsors to manage and operate pension plans in the interest of participating employees and retirees and in accordance with the plan's terms and ERISA's fiduciary standards.

Many employers—not only in the U.S. but also in the UK and other developed economies—have chosen not to sponsor DB pension plans. Increasingly, employers are deterred by what, to them, are the DB's drawbacks: cost, administrative burden, risk of litigation, potential liability, and potential volatility of funding obligations. In particular, fluctuating market values and interest rates can lead to unexpected increases in pension funding obligations that can wreak havoc with corporate financial statements. And in declining industries with shrinking work forces facing stiff global competition (including, at various times, U.S. autos, steel, tire, trucking, airlines, and U.S. manufacturing generally), there is a steadily increasing ratio of (a) pensioners depending on financial support from company-sponsored pension plans to (b) active workers producing revenues that help the company fund those pensions.

Moreover, even in thriving sectors of the economy, as life expectancies have increased markedly over the past century, the ratio of retirement person-years to working person-years has continued to increase. As

a result, pension liabilities have loomed larger than expected on the balance sheets of many corporate DB plan sponsors.

For workers, while DB plans have major advantages, they also have some drawbacks. Although they protect workers from many financial risks and provide regular monthly income guaranteed for life (and often for the lives of both an employee and their spouse), DB benefits for many workers are not payable until the relatively distant future. This makes them harder for many employees to relate to than more tangible, liquid retirement savings account balances that accumulate more visibly in the short term. While many individuals prefer the certainty of pension benefits, many others want more choice, more control, greater liquidity, the possibility of access to more versatile savings before retirement, and flexibility to take more or less than the regular monthly DB payment.

Traditional pension plans also tend to disproportionately reward longer-service, older, and well-paid employees, with vesting schedules and benefit accumulation formulas often reserving the richest benefits for a relatively small fraction of workers who retire from the sponsoring employer. In addition, DB benefits may not be as well suited as retirement savings plans for a mobile workforce or for those moving in and out of the workforce due to family responsibilities or other reasons. Changing jobs can slow the rate of DB benefit accumulation, and the fact that most employers do not sponsor DB plans and the friction involved in moving DB benefits from one employer to another further impede the portability of DB pensions.

Accordingly, with the increase in global competition and changes in the U.S. work force—including the markedly declining market share of organized labor, which traditionally has bargained for DB pensions—the number of DB plans and the number of workers they cover have declined steadily.[1]

B. THE RISE OF 401(K) PLANS

The universe of defined contribution (DC) retirement savings plans—already less protective of individuals than DBs—also shifted. "Classic" DC plans that already existed, such as "profit-sharing: or "money purchase pension" plans[2] typically were funded, invested, and managed mainly by employers. They "defined" the employer's contributions (which could be substantial) rather than the employee's ultimate benefits. Over time, however, the dominant vehicles outside of the DB space became a different type of DC plan—mainly new types of worker-funded retirement saving accounts. These are exemplified by the 401(k), which is mostly funded by employee elections to redirect a portion of their take-home salary or wages to a tax-favored retirement saving account, and the IRA, which is entirely funded by the individual who owns it. Thus, the shift away from pensions was not "just" a shift in the form from DB to DC. Rather, within the DC category, it included a substantial shift from employer-funded and employer-managed pension plans to retirement saving accounts funded and run mainly or largely by workers or individual savers. In doing so, it also placed almost all of the responsibility and risks on the employees.

Starting in the early and mid-1980s and spurred on by the growing availability of mutual funds as a widely accessible means of efficiently diversifying investment risk, 401(k) plans came onto the scene.[3] These retirement saving plans did not define the ultimate benefit, nor—being mostly self-funded by employees—did they define the employer's or employee's contributions. Employees decided how much to contribute on a tax-favored basis, investment earnings accumulated on a tax-deferred basis, and payouts, typically in retirement, would be included in taxable income. Nondiscrimination standards were designed to give employers incentives to encourage broad participation by moderate- and lower-income employees and to limit the disparities in saving and benefits between them and executives or business owners. Partly for this reason, employers often voluntarily matched employee contributions.

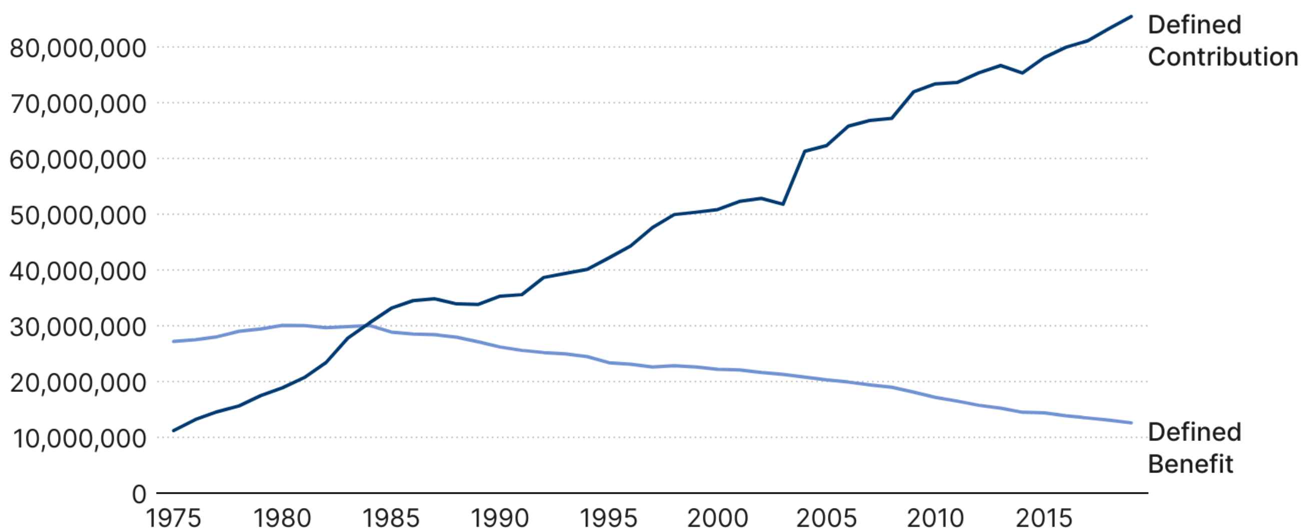
While 401(k)s at first were typically offered mainly as supplements to a mainstay DB pension, they expanded rapidly and gradually became the primary private-sector retirement plan for tens of millions of workers. Between 1980 and 2019, the percentage of private-sector U.S. workers participating in 401(k) and other DC plans increased from 17% to 52%, while the

percentage covered by DB plans dropped from 39% to 8%. Figure 1 shows the change in participation in DC and DB plans from 1975 to 2019.[4] This same period also saw a dramatic expansion of IRAs, which ERISA authorized mainly to offer tax-favored retirement benefits that would help fill the gap for individuals who had no access to an employer plan, and also to give plan participants a tax-favored destination for rollovers of benefits when leaving a job.

In the 1980s and 1990s, the typical 401(k) plan was a "do-it-yourself" vehicle. While this was a popular design, it raised many issues as 401(k)s became the main retirement vehicle for rank-and-file workers. The 401(k) and IRA rules that existed at the time did not require employers to offer a 401(k) or an IRA; and provided little guidance about (a) whether an employee should participate; (b) how much to contribute initially and how much to raise contributions over time; (c) how to invest account balances, and (d) when and in what form to withdraw plan savings. In addition, the 401(k) and the IRA do not naturally protect individuals against their lack of professional investment experience and judgment. Savers also can be exposed to market volatility and sequence-of-returns risk, uncertainty about how much to contribute and at what pace to spend down their account balance, or the risk of outliving their retirement resources. Improving the 401(k) and IRA system to address these issues has been a main focus of retirement plan reform over the past 25 years, as discussed below.

FIGURE 1

Active Participants in Private Pension Plans, 1975-2019



Source: Employee Benefits Security Administration publication "Private Pension Plan Bulletin Historical Tables and Graphs 1975-2020," Table E7. Accessed 1/5/2024: https://www.dol.gov/sites/dolgov/files/EBSA/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf

Note: Active participants are tabulated as of the end of the plan year. EBSA methodology for calculating defined contribution plans changed between 2003 and 2004, leading to a jump in the data.

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II. Making Retirement Saving Easier and More Rewarding

Helping retirement savers to have better outcomes and reduced risk began with regulatory changes by the Treasury Department starting in 1998 that first defined, approved, and began to promote automatic enrollment (paired with automatic diversified investing) in 401(k)s and similar plans. As evidence mounted that automatic features worked and private-sector interest and take-up in the market increased, the regulatory reforms expanded and were eventually complemented by federal legislation. The legislation, especially 2006's Pension Protection Act (PPA06), enabled the private sector to implement the auto features more expansively. In short, despite delays and obstacles, the automatic 401(k) illustrates how innovative policymaking can work—beginning with more limited changes to test the premise, then evaluation in academic and think tank settings, and finally gradual implementation and expansion through governmental and private-sector action.

In 2006, inspired by the success of automatic features in 401(k) plans, the Retirement Security Project proposed a nationwide Automatic IRA program. As described below, while Congress has continued to consider the Auto IRA legislation without acting on it, 15 States (to date) have adopted the concept by enacting Auto IRA programs for their citizens.

A. THE AUTOMATIC 401(K)

As DB plans continued to erode, policymakers in the Office of the Benefits Tax Counsel at the U.S. Treasury Department in the late 1990s formulated a regulatory strategy to reshape the rapidly spreading "do-it-yourself" 401(k) to incorporate certain valuable attributes of DBs and other traditional pensions (Clinton Administration History Project 2001). DBs and traditional pre-401(k) DC plans generally cover employees automatically, without requiring them to take the initiative to enroll. Accordingly, rulings issued by Treasury and IRS in 1998 and 2000 outlined a new 401(k) paradigm. Instead of having to sign up for a 401(k) plan (and too often failing to do so out of inertia, procrastination, or indecision about how much to contribute or how to invest), employees could be automatically enrolled in the plan. The new guidance announced that "auto enrollment" was lawful for 401(k) and similar plans, and that, accordingly, plan sponsors may, but are not required to, automatically enroll employees into the plan if it provides explicit advance written notice. Unless an employee affirmatively opted out of participation, the employer could deduct a portion of the employee's pay and contribute it to the plan on a pre-tax basis.

The implications and power of this strategy have been transformative for the 401(k) system. The default affects not only enrollment; plans automatically enrolling employees must specify the level of contribution and how the funds will be invested among the available options. Employees are free to reject those defaults and make their own affirmative choices, but if they don't, they are enrolled in the plan's choices. The government's rulings made clear that it was not requiring plans to use any particular contribution level (like 3% of pay) or any particular investment as the plan's defaults. But because the rulings used particular facts to illustrate how automatic enrollment and the defaults could work, plans and their legal counsel paid close attention to those examples. Three of those illustrative facts are particularly worth noting: the default contribution level was not the same in all the rulings (3% of pay in several rulings and 4% of pay in another); the plan's use and continuation of employer matching contributions in all the rulings, and a default investment consisting of a balanced fund of diversified stocks and bonds—and explicitly not stock of the employer sponsoring the plan—in all the rulings. (Rev. Rul. 98-30; Rev. Ruls. 2000-8, 2000-33; Rev. Proc. 2000-35; Rev. Rul. 2009-30; IRS Notice 2009-66).

Moreover, Treasury's decision to use the term "automatic enrollment" in 1998 was intended to cue the market to recognize that enrollment was only one phase of the saving cycle that could usefully be made

automatic (Iwry 2020). In addition to automatic investing, beneficial defaults could apply also to distributions, including rollovers. Later, Treasury/IRS made clear—prompted by Thaler and Benartzi's "Save More Tomorrow" proposal—that plan sponsors could also default participants into increasing their contribution rate over time[5] (IRS 2004). Automatic escalation of contributions improves the adequacy of saving. It also helps address the concern that some new employees could passively accept the plan's initial default rate and never increase it even though it would not produce sufficient levels of savings. If forced to make an explicit election, they would otherwise decide to contribute at a higher rate.

The market took up automatic enrollment gradually at first, but before the 2006 Pension Protection Act (PPA 06) took effect in 2007, an estimated 41% of large employer 401(k)s (and a lower but substantial percentage of all 401(k)s) had already adopted it. (Gale, Iwry, and Orszag 2005b; Plan Sponsor Council of America 2008). After the 2006 legislation took effect, removing some of the potential obstacles to auto enrollment, this expansion—already accelerating—continued. Today, it is estimated that roughly 3 out of 4 larger 401(k) plans use auto-enrollment, although take-up in the smaller plan market remains distinctly lower (Dietrich 2022).

Early on, the evidence in the market, including research by Madrian and Shea (2001), Thaler and Benartzi (2004), and others, suggested that auto-enrollment was significantly increasing plan participation, which provided an additional boost to policy efforts. Plans in which two-thirds or three-quarters of eligible employees traditionally participated would see their participation rates rise to 9 out of 10 or even higher when they switched to auto-enrollment. One powerful example: in the mid-2000s, the largest DC plan in the world—the Thrift Savings Plan (TSP), which resembles a 401(k) and covers over 6 million U.S. federal government employees—adopted auto-enrollment despite an already high participation rate. TSP's Executive Director estimated that this step raised the participation rate from about 85% to more than 90% and increased the number of employees participating in the plan by approximately 300,000.[6] Importantly, auto-enrollment tends to raise participation especially by those who otherwise confront the greatest challenges to saving and who are disadvantaged by racial, ethnic, and gender savings, income, and wealth disparities (Madrian and Shea 2001, Francis and Weller 2021).

Because defining auto-enrollment and declaring it lawful was an administrative rather than a legislative initiative, it was able to progress from concept to settled law within a few months without congressional involvement. However, after Treasury and IRS issued their landmark guidance in 1998 and President Clinton then showcased the concept in a speech covered by major media, various Members of Congress began to express both support and interest in promoting the practice. Nonetheless, even without help from Congress, auto-enrollment caught on in the market, first slowly and then rapidly in the years leading up to 2007. That said, the regulators began to hear auto-enrollment issues from plan sponsors that only Congress could address. Therefore, legislation was drafted in 2005 and added to PPA 06 (a bill which was intended mainly to deal with DB pension issues) to help lay to rest three particular concerns with auto-enrollment.

The first concern was that newly auto-enrolled employees who failed to read or understand the advance written notice of auto-enrollment and their opt-out rights might be unpleasantly surprised to find their take-home pay reduced by contributions they had never explicitly authorized. The then-existing 401(k) restrictions preventing active employees from withdrawing from their accounts might also keep them from obtaining a refund of their unintentional contributions. In addition, employees who could get their money back might incur a 10-percent early withdrawal tax. Congress solved this by providing a 90-day grace period in which plans could retroactively "unwind" automatic contributions by refunding them to requesting employees, free of the 10-percent tax.

Second, employers were concerned that their limited relief from fiduciary liability when employees "self-direct" investments by selecting from among plan options did not apply to investments made by auto-enrollment (i.e., without an explicit employee investment election). The Labor Department therefore issued

regulations assuring the market that certain default investments entitle plan fiduciaries to the same relief they enjoy when employees choose their own investments. The regulations extended the limited fiduciary relief for "self-directed" investments to three "qualified default investment alternatives" ("QDIAs"): balanced funds, target-date funds, and professionally managed accounts.

Third, some plan sponsors expressed a concern that state anti-garnishment, worker protection laws might prevent 401(k) auto-enrollment by prohibiting paycheck withholding without an employee's explicit written authorization. PPA 06 solved this by preempting state laws to the extent necessary to permit auto-enrollment.

In addition, industry lobbyists proposed—and Congress agreed to—a new statutory nondiscrimination safe harbor to encourage plans to adopt auto-enrollment. Plans obtained a free pass from nondiscrimination standards if they auto-enrolled employees at 3% of pay, automatically escalating 1% each year up to at least 6%, and offered specified employer matching (or made nonmatching) contributions with two-year vesting. As policy, this raised some concerns, but it did serve to illustrate to the market the auto-escalation feature (Retirement Security Project, 2006).

B. THE AUTOMATIC IRA

The automatic 401(k) helped millions who were eligible to participate in retirement savings plans, but failed to help the large share of the workforce whose employers did not offer such a benefit. To address the needs of this group, Iwry (2006) and Iwry and John (2006, 2021) proposed to extend the power of auto-enrollment to the tens of millions of workers without access to employer plans.

The proposal would apply automatic enrollment to payroll deduction IRAs. This enables an employer to facilitate tax-favored saving by its employees easily without the employer decisions, tasks, and responsibilities involved in sponsoring an ERISA-covered plan and overseeing investments in the plan's trust (Gale et al. 2009). Starting in 1997, the Treasury Department had encouraged small employers that did not wish to sponsor a retirement plan to simply let their employees use the employer's existing payroll system to save a portion of their wages in an IRA. Treasury deliberately made this entirely voluntary for employers in the hope of expanding coverage without subjecting firms to even the most minimal requirements. Moreover, in the conference report to the Taxpayer Relief Act of 1997 (Pub. L. 105-34, which also included other important retirement provisions), Congress made a point of weighing in to support Treasury's efforts, stating that "employers that choose not to sponsor a retirement plan should be encouraged to set up a payroll deduction [IRA] system to help employees save for retirement by making payroll-deduction contributions to their IRAs," and accordingly encouraged the Treasury Secretary to "continue his efforts to publicize the availability of these payroll deduction IRAs" (H. Rept. 220, 105 Cong. 1 sess. (1997)). But despite those efforts, over the ensuing quarter century the take-up of voluntary payroll deduction IRAs has consistently been close to zero. Therefore, responding to both the failure of the voluntary payroll deduction IRA and the success of automatic enrollment in 401(k) plans, the Automatic IRA proposal would require employers that chose not to sponsor a retirement plan to simply serve as a conduit, automatically enrolling employees into contributing a portion of their own wages to payroll deduction IRAs provided and managed by the private sector.

This combined three key building blocks of the current retirement system. First, payroll deduction saving at the workplace, which continues automatically on a "set it and forget it" basis; second, federally tax-favored individual retirement accounts—the most portable and simplest vehicle in the private pension system (and which do not require employers to select or oversee investments or plan administration); and third, automatic enrollment, borrowed from the 401(k) market, to maximize participation while preserving individuals' freedom of choice regarding participation and investment.

Taken as a whole, these features make it easy for workers to save in a rudimentary structure without threatening to compete with or crowd out actual employer-sponsored retirement plans. In fact, Auto-

matic IRAs can act much like a benign “gateway drug” making it easier to persuade employers to sponsor plans because they have had some experience with a simplified version of a payroll deduction retirement benefit.

The Auto IRA proposal (like the state Auto IRAs discussed below) was designed to make the default type of IRA a Roth—which is often better suited for lower-income taxpayers, who face low (or zero) current income tax rates, and which permits tax-free withdrawals to meet emergencies or other immediate needs. The default investment generally is a low-cost target date fund offered by private-sector firms. Employees can opt out at any time or override the defaults regarding the type of IRA, rate of contributions, or type of investment. To mesh with and support the private pension system, savings accumulated in Auto IRAs can—and in many cases eventually will—be rolled over to most regular private-sector IRAs or plans.[7]

The smallest and newest employers are exempted from the requirement, and covered employers are not required—or even permitted—to contribute. The absence of employer contributions to Auto IRAs and the major difference between their $7,000/$8,000 IRA 2024 contribution limits and the $23,000/$30,500 401(k) 2024 employee contribution limits (and $69,000/$76,500 total DC plan 2024 contribution limits) help ensure that Auto IRAs are not as attractive as, and likely will not crowd out or compete with employer-sponsored retirement plans. In fact, an important secondary purpose of the Auto IRA is to facilitate marketing of 401(k) plans (as well as other tax-qualified and SIMPLE-IRA plans) by amplifying the messaging about the importance of saving and demonstrating to employers the popularity and value of tax-favored saving in the workplace. In addition, many Auto IRA contributors would also qualify to receive the saver’s credit (discussed below), and small employers facilitating these Automatic IRAs would receive a small federal tax credit to help defray any administrative costs.

The Auto IRA proposal promptly received a favorable reception from across the political and policy spectrum, including endorsement by Martin Feldstein, the Chair of the Council of Economic Advisors in the Reagan Administration, Laura Tyson, his counterpart in the Clinton Administration, and ultimately by both 2008 Presidential candidates, then-Senators Obama and McCain (Retirement Security Project 2008). Congressional offices on both sides of the aisle requested briefings and, later, potential legislative drafts. According to an editorial in The New York Times, “The best idea yet developed for making savings universal is an IRA that is funded with automatic direct deposits from a paycheck. The brainchild of researchers from the Heritage Foundation and the Brookings Institution, the automatic IRA would use a no-frills design and economies of scale to overcome the problem of high fees on small accounts. Congress should pass legislation to establish auto-IRAs, and the President should sign it” (New York Times, 2006).

The federal Auto IRA proposal was introduced as legislation by Republican and Democratic co-sponsors in both the House and Senate tax-writing committees. But despite its auspicious beginnings, the prospects of passage suffered from the widening partisanship exacerbated by the 2010 party-line passage of the Affordable Care Act. Republican leadership identified the bill as another Obama administration proposal that, if enacted, would give the President a victory. Meanwhile the bill’s Republican lead cosponsors failed to win reelection. President Obama included the proposal in each of his eight annual budgets, while Democrats—including Rep. Neal (D-MA) and others in the House and Senators Bingaman (D-NM), Kerry (D-MA), and Whitehouse (D-RI)—continued to introduce the bill in each Congress, hoping for renewed bipartisan support (S. 1141; H.R. 5376).

In 2002, one of the co-authors began exploring whether state governments might be able to play a supporting role assisting the private sector and the federal government in expanding retirement coverage—not for state and local government employees, most of whom are already covered by retirement plans, but for private citizens. With outreach to state treasurers and legislators, including conferences bringing interested parties together from around the country, this state-based initiative began to take shape and pick up momentum in a half dozen states by 2005 (Iwry 2003b; Iwry 2006).

By 2008, it was becoming clear that the preferred approach for the states would be a state-based version of the federal Auto IRA model; and by the end of 2023, 15 states—California, Colorado, Connecticut, Delaware, Hawaii, Illinois, Maine, Maryland, Minnesota, Nevada, New Jersey, New York, Oregon, Vermont, and Virginia—had adopted Auto IRA legislation, and other states have bills pending. With only a few variations, the state Auto IRA programs are very similar.[8]

Implementation thus far in roughly half of these states provides proof of concept and has enabled almost a million lower- and moderate-income individuals to begin saving conveniently at work on a tax-favored basis. Importantly, federal courts have rejected a challenge arguing that the state Auto IRAs should be preempted by ERISA (Iwry 2020). Moreover, evidence suggests that the state Auto IRAs are also beginning to promote wider adoption of 401(k) and similar plans in the private sector (Chalmers et al. 2021, 2022; Guzoto et al. 2023; Tergesen 2023b; Samuels 2023).

Most state Auto IRAs are run by a state board that has fiduciary responsibility for overseeing the program and contracts with private sector recordkeepers and asset managers to administer it. The boards, often chaired by the State Treasurer, generally consist of both state government officials and private sector representatives. Employers that do not sponsor a 401(k) or other retirement plan are required only to facilitate auto-enrollment of their employees into the state program's private-sector-managed IRAs. State Auto IRA programs generally use a target date fund as the default investment and offer a handful of other investment alternatives. Providers are chosen by competitive bidding. Employers' responsibilities are quite limited: first, registering on a state web site and uploading their employee roster and related contact information to the private sector Auto IRA program manager/recordkeeper firm which will contact employees and administer contribution elections. The program manager then notifies employers of each employee's election so employers can withhold the appropriate amounts from pay and remit them to the program manager for investment in the IRAs. Survey data from the Pew Charitable Trusts suggest that only a small fraction of employers incur any out-of-pocket administrative costs or are not satisfied with the programs (Guzoto et al. 2023).

Proponents of state Auto IRAs have proposed that state programs join in partnerships to realize economics of scale and to help states with smaller populations start their own programs faster and at a lower cost (Correia 2023). Colorado has entered into a partnership with Maine and Delaware and is working on similar arrangements with other states.

C. SAVER'S CREDIT

Tax benefits for retirement saving tend to be weighted heavily toward high-income households even after taking into account the indirect "trickle down" benefits for rank-and-file participants in qualified plans (Congressional Budget Office 2021). The Saver's Credit, enacted by Congress in 2001, provides a very partial amelioration of that pattern. The U.S. Treasury Department had developed and proposed it as a 50-percent refundable tax credit for lower- and moderate-income savers, to be deposited in their retirement accounts. The proposal was designed to reduce the disparity in tax incentives for those in lower tax brackets, and to encourage them to contribute to an employer plan or IRA. At the time, the retirement industry was developing the extensive Portman-Cardin legislative package, which was largely focused on increasing saving incentives for more affluent individuals and encouraging employers to sponsor plans by raising the maximum limits on tax-favored contributions and benefits in employer plans and IRAs. Accordingly, Treasury proposed that the saver's credit be added to Portman-Cardin in order to include at least one significant provision targeted explicitly to benefit the majority of U.S. workers instead of benefiting mainly affluent savers (Gale, Iwry, and Orszag 2004a, 2004b).

A version of the saver's credit was included in the Portman-Cardin bill before it was enacted as part of the larger 2001 EGTRRA tax legislation. However, to divert revenues to fund other provisions, the managers of the bill cut back drastically on the structure and magnitude of the proposed credit. As enacted, it became a temporary and nonrefundable credit, therefore of use only to savers who have federal income tax liability (cutting

out a large majority of the savers who would otherwise be eligible). The simple 50-percent credit rate was converted to three tiers: a 10% credit for most eligible savers, 20% for some others, and 50% for only a very small number of the lowest-income savers. In addition, the credit would not be deposited to a retirement account and therefore has typically been consumed or applied to reduce debt. These changes made the credit difficult to understand and to use; in fact, some simpler experimental efforts obtained higher take-up rates despite being less financially rewarding (Duflo et al. 2006, 2007).

III. SECURE and SECURE 2.0

While the basic changes to automatic saving structures and enactment of the Saver's Credit more than two decades ago have shown promise, the intended breakthroughs in expanding coverage, closing the racial, ethnic, and gender gaps in retirement saving and security, providing reliable and adequate retirement income, and achieving sufficient portability of benefits have yet to be achieved. In recent years, Congress has taken a few limited additional steps by enacting the SECURE Act and the SECURE 2.0 Act, signed into law in 2019 and 2022, respectively.

These Acts include further efforts to expand retirement plan coverage and automatic saving; expand and reform the Saver's Credit; improve options to provide lifetime retirement income (and thus eliminate longevity risk); and require plans to offer participation to a wider group of part-time employees. They also enhance portability; expand tax credits for small employers to adopt new plans, contribute, and auto-enroll employees; improve disclosures; reduce pre-retirement leakage; allow plans to offer small immediate taxable payments to induce participation by nonparticipating employees (Tergesen 2023a); facilitate multiple employer plans; and make emergency saving easier and more accessible. At the same time, SECURE and SECURE 2.0 include various other provisions, not discussed here, that misallocate resources, exacerbate inequalities, and miss opportunities to improve the system.[9] For a list of specific provisions and their revenue estimates, see JCT (2019) and JCT (2022).

A. AUTO FEATURES IN SECURE/SECURE 2.0

Building on the spread of auto-enrollment and related auto features in the 401(k) market and of state-facilitated Auto IRAs, efforts were made in Congress in 2021 to enact the nationwide Automatic IRA, including recognition and support for state-based Auto IRAs, while also providing further incentives for adoption of 401(k)s and other employer-sponsored plans (Ebeling 2021). When this legislative proposal failed to garner sufficient bipartisan support, the proponents resigned themselves to a far less ambitious and thoroughly bipartisan legislative package that at least would include a requirement that 401(k) plans incorporate auto-enrollment and other automatic features and would expand the saver's credit. A version of this, combined with numerous other retirement provisions, became SECURE 2.0. The legislative compromise reflected in SECURE 2.0 requires new 401(k)s and similar plans to adopt auto-enrollment and auto-escalation of employee contributions (but beginning at 3% of pay, which is now considered a relatively modest initial default rate). The requirement is also rather weak because nearly all plans in existence before 2023 are exempted.

An unsuccessful attempt was made to require employers to periodically re-auto-enroll existing employees who are not participating, so that practice remains voluntary for plans. (Treasury has been asked to provide guidance on whether the auto-enrollment and auto-escalation required of new plans extends beyond new hires to other employees.) SECURE 2.0 also codifies and makes permanent an existing IRS administrative safe harbor that encourages 401(k) auto-enrollment and auto-escalation in plans that are not subject to the new SECURE 2.0 auto features requirement by facilitating and reducing the cost of correcting plan errors in administering auto-enrollment and auto-escalation.

B. SAVER'S CREDIT/SAVER'S MATCH

Shortly after the Saver's Credit was enacted in 2001, an effort began to persuade Congress to restore the credit to its originally proposed form: a permanent, refundable, 50-percent credit deposited in the saver's retirement account like a matching contribution. (Gale, Iwry, and Orszag 2004a, 2004b, 2005). Just as auto 401(k) features help make retirement saving easier for moderate- and lower-income workers, the reformed saver's credit would help make saving more remunerative for them. Redesigning the credit as a government matching contribution was intended to further stimulate saving.

In SECURE 2.0, Congress made major structural improvements along these lines. The redesigned saver's match under SECURE 2.0 provides for a single 50%

match rate and is effectively "refundable"—available to all savers with modified AGI below $71,000 if married ($35,500 if unmarried) regardless of whether the saver has a federal tax liability. This "refundability" will expand the number of workers who will be eligible if they save by tens of millions .

The form of the credit will be changed to a government matching contribution (and hence the credit is renamed the "saver's match") of up to $1,000 (50% of up to $2,000 of the saver's retirement contributions) into a retirement plan account or IRA designated by the saver. Because the match will be automatically deposited into a retirement savings account rather than paid directly to the saver, it is more likely to be saved than spent. The 50% match is fully available to married savers with modified AGI not exceeding $41,000 ($20,500 for those who are unmarried), with the percentage phasing down gradually to zero if their modified AGI is between $41,000 and $71,000 (half these amounts for unmarried).

Converting the saver's credit to the saver's match entailed substantial revenue cost and was controversial in Congress. SECURE 2.0 therefore restricted it in six significant ways. First, although the match rate was increased to 50%, the income eligibility limits were set lower than current-law limits; accordingly, while refundability dramatically increases the total number of eligible savers, not everyone eligible for the current credit will be eligible for the expanded match.

Second, to reduce the 10-year revenue cost under current budget scoring rules and to provide plans, their recordkeepers, and the IRS more time to prepare for the new matching deposits, the saver's match will not take effect until 2027, and the existing, smaller credit will remain in effect until then. Third, also to limit revenue cost, the match, while excludable from the saver's income when earned and deposited to the plan or IRA, will be taxable when ultimately distributed, much like employer contributions to DC plans (instead of more generous Roth treatment upon distribution, which would cost more revenue).

Fourth, owing to apparent concerns about the difficulty of enforcing this distinct, non-Roth tax treatment if the match was deposited in a Roth IRA or Roth 401(k) account, SECURE 2.0 prohibits deposit of the match into those Roth vehicles. Fifth, to accommodate the possible preferences or concerns of some plan sponsors, recordkeepers, and IRA trustees about taking in the new matching deposits, no plan or IRA will be required to accept them, even if it is the saver's only retirement account and hence the one to which the saver contributed to earn the match. Sixth, if a saver makes taxable early withdrawals from a retirement savings account during a specified lookback period, they will reduce the match amount.

C. RETIREMENT INCOME

As noted, the shift away from pensions, DB and other, has largely transformed our private pension system to an account-based retirement saving system. DB pensions are traditionally designed to supplement Social Security and protect retirees from the risk of outliving their savings by providing regular (typically monthly) income for life, replacing the paychecks they once received. In contrast, 401(k)s and IRAs provide account balances instead of income, and usually do not assist households to determine how and how much to spend month by month in retirement.

Accordingly, recent years have seen efforts to restore the "pension" to our private retirement system. For example, from 2010 through 2016, an Executive Branch initiative promoted a national dialogue on lifetime retirement income and public-private efforts to foster it in DC plans. This initiative included Treasury/IRS guidance creating a new income vehicle—the Qualified Longevity Annuity Contract (QLAC)—that protects against the risk of outliving 401(k) or IRA savings. A QLAC simplifies the challenge of managing those assets over an uncertain period by establishing a fixed time horizon and is exempt from the required minimum distribution requirements discussed below (U.S. Treasury 2014a). Treasury/IRS guidance also permitted fixed income annuities to be embedded in target date fund qualified default investment alternatives (QDIAs) in DC plans (as proposed in Gale et al. 2008 and Iwry and Turner 2009), accumulating gradually as deferred annuity units that can reduce interest rate risk and help accustom participants to receiving

monthly annuity payments when they retire (U.S. Treasury 2014b). Other Treasury/IRS initiatives encouraged DB and DC plan sponsors to allow employees to roll DC plan lump sums into the employer's DB plan to purchase a DB pension; clarified the rules governing annuities in 401(k) plans; and prohibited plan sponsors conducting pension risk transfers from cutting off ongoing DB pensions by offering to buy them back from retirees for cash (IRS Notice 2015-49).

SECURE and SECURE 2.0 built on these prior initiatives in several ways. The SECURE Act introduced a long-awaited fiduciary safe harbor designed to help protect plan sponsors from ERISA fiduciary liability if a private-sector insurance company prudently selected by the plan sponsor to provide annuities for plan participants ultimately fails to meet its decades-long obligations. However, the safe harbor was designed by the insurance industry in a way that includes at any given moment nearly every annuity provider in the market—an overbreadth that defeated the purpose of giving plan sponsors confidence that they need not incur the cost of engaging expert consultants as independent fiduciaries to select truly dependable annuity providers. Other SECURE and SECURE 2.0 provisions promoted lifetime income by requiring DC plan benefit statements to provide regular projections of the retirement income equivalent of the saver's account balance (as proposed in Gale, Iwry, John, and Walker 2008). Other provisions facilitated, in certain circumstances, the portability of annuity contracts in DC plans and IRAs; raised the maximum QLAC dollar amount that can be purchased, eliminated the restriction on purchasing QLACs with more than 25% of the purchaser's plan or IRA balance; and relaxed some of the other restrictions on the offering of annuity contracts in DC plans.

D. MANAGING RETIREMENT ACCOUNTS

The U.S. private pension system has yet to achieve adequate "portability" of benefits—either in the sense of tracking and moving benefits or of continuing to save an adequate amount—as workers change jobs or exit and reenter the workforce. DB plans are less portable than DC, as noted earlier, but DC plans are not portable enough, even with the ability to move retirement savings into IRAs.

The Portman-Cardin legislation included in EGTRRA (2001) expanded the ability to transfer assets tax-free ("roll over") between the various types of tax-qualified plans and accounts. It also dramatically improved portability and put an end to many years of unnecessary leakage by enabling plan sponsors to automatically roll over terminating employees' small balances (up to $5,000) into IRAs established for them. These default rollovers preserved the savings of millions of people, who otherwise would have had their small accounts cashed out when they left a job unless they affirmatively asked to have the money sent to their new employer's plan or to an IRA.

But despite these auto rollovers of terminating employees' small balances, and the 20-percent mandatory withholding imposed on departing participants' benefits if the savings are not directly rolled over to another plan or IRA, considerable leakage continues to impair retirement security. Small plan and IRA accounts are more likely than larger accounts to be abandoned, lost, or cashed out. This especially hurts the retirement security of Black and Hispanic savers (John et al. 2021a).

One reason for continued leakage is that Labor Department ERISA fiduciary "safe harbor" guidance caused the auto rollover IRAs to be invested in principal preservation assets like money market or stable value funds, which tend to have very low interest rates. This led these "safe harbor" IRA balances to dwindle as investment earnings during the era of low interest rates failed to keep up with the cost of maintaining IRAs. And more generally, savers requesting one plan to roll over their benefits to another commonly encounter foot-dragging, delays, and unnecessary red tape, leading too many of them to eventually give up on rolling over and instead simply take a cash lump sum and spend it.

SECURE 2.0 contains four important and potentially far-reaching provisions that could help alleviate these problems: arrangements for auto-portability; establishment of a lost and found facility; steps toward standardization of data and procedures to facilitate rollovers; and special authorization for emergency savings (John et al. 2021a).

1. Auto-Portability for Small Balances

Expanding on previous Labor Department guidance, SECURE 2.0 codifies and elaborates on an "auto-portability" agreement among major recordkeeper firms called the Portability Services Network. The agreement requires firms to automatically roll over savers' small account balances (initially up to $5,000, increasing to $7,000 starting in 2024) from their former employer's retirement plan to a new employer's plan, unless the participant objects. This should improve portability and reduce leakage in cases where a terminating employee has a new employer with a plan willing to accept the rollover. At the same time, though, SECURE 2.0 also threatens to ultimately lead to greater leakage insofar as it allows employers that don't agree to use auto-portability to eject more small accounts (up to $7,000 instead of the previous $5,000 limit) from their plans.

2. Lost & Found

In a separate provision which should also reduce leakage and enhance participant control over their financial future, SECURE 2.0 requires the Labor Department to set up a new online data base to help individuals locate and keep track of their various retirement benefits. Although authority to provide more enhanced features might have made the facility function as a still more useful "dashboard" of retirement benefits (John et al. 2021a), collecting the necessary participant data from plan sponsors and recordkeepers for even a basic registry of benefits will likely be challenging.

3. Standardization to Facilitate Rollovers

Those provisions require Treasury and IRS to consult with private-sector stakeholders and, with their input, develop proposed standard data sets, forms, and procedures to serve as models for use by plans and recordkeeper firms in administering rollovers (as proposed in John et al. 2021b, Appendix C). The hope is that a consultative process and the eventual availability of standard forms, data sets, and procedures—reflecting extensive input and possibly broad consensus from the recordkeeping industry and plan sponsors—would lead to their uniform and universal (or near universal) adoption.

4. Emergency Saving

A continuing problem for retirement savers—especially lower- but also many middle-income households—is the effect of inevitable unexpected expenses on household finances. All too often, households lack emergency savings and deal with financial emergencies by withdrawing money from their retirement accounts, selling other assets, or taking on high-cost debt such as payday loans or credit card debt. Inflation has made this problem even worse, and in response, a growing number of employers are offering some form of emergency savings benefit.

There are various types of emergency savings benefits. Some are funded by employee payroll deductions and are set up as separate emergency accounts that could be connected to a 401(k) or similar tax-favored retirement plan. Alternatively, these accounts could be freestanding and entirely separate from any plan. Whether part of a plan or not, these accounts can also be funded by some form of employer contributions. Freestanding emergency savings accounts are not tax-favored. A third form of this benefit is a single company fund that could include contributions from either employers or employees or both and is available to advance money to a worker who faces a serious financial problem.

Emergency savings accounts should be separate from general savings, so they are less likely to be used for other purposes. They can be designed to have smaller balances for unexpected short-term needs or larger balances that might, for example, replace a household's wages during periods of unemployment. The accounts are intended to be used when an unexpected expense strikes, and then be replenished. A continuing problem is that while employees say they want such a benefit, the process of opening an account can be complex and discourage participation. The obvious solution would be automatic enrollment, but this presents legal questions for out-of-plan accounts in the U.S.[10]

SECURE 2.0 dealt with the need for emergency savings in two ways. First, it allowed 401(k)s and similar plans to automatically enroll non-highly compensated employees into tax-favored, "pension-linked emergency savings accounts" with balances up to $2,500 as part of the plan. They are subject to ERISA, but separate from other accounts, and withdrawals are tax-free and penalty-free. Plans that otherwise offer employer matching contributions must match employees' emergency saving contributions (but the employer match must not exceed $2,500). Auto enrolled accounts may have a contribution rate of up to 3% of pay. Savers must be permitted to make withdrawals at least monthly and may make up to four withdrawals a year without having to pay fees.

The second provision in SECURE 2.0 does not use a separate emergency savings account; instead, it allows retirement savers to withdraw up to $1,000 penalty free once a year from their retirement savings account in a plan or IRA to meet an emergency. The withdrawal is taxable, but that can be reversed if it is repaid within three years, at which point further annual $1,000 withdrawals may resume.

E. MEPS AND PEPS

The 2019 SECURE Act promoted the spread of multiple employer plans (MEPs). To make it easier and less costly for small businesses to sponsor plans, Congress was lobbied heavily to relax ERISA restrictions that allowed only related employers to co-sponsor a single retirement plan. SECURE therefore amended the law to allow multiple employer plans to be sponsored by unrelated employers. These can be either "open" MEPs or "pooled employer plans" (PEPs), which must satisfy special statutory conditions.[11] The stated goal was to achieve economies of scale that reduce the traditionally higher per capita costs of plan sponsorship by small employers, in order to extend coverage to many small business employees who previously lacked access to a plan at work. For further discussion of SECURE's MEP provisions, see Baily, Harris, and Iwry (2019).

In the wake of SECURE, numerous recordkeepers, asset managers, plan advisors, third-party administrators, and consultancies are now offering PEPs and other open MEPs. Their marketing is targeted not only to small employers without plans but also (more than Congress might have expected) to encouraging existing single-plan sponsors, including larger employers, to participate in a MEP or PEP instead. The ultimate impact of this activity remains to be seen, in part because the pandemic has slowed implementation.

In addition, the industry narrative has evolved from using economies of scale to cover millions of previously uncovered small business employees in lower-cost MEPs to making plan sponsorship more efficient and somewhat cheaper for both small and larger employers. This is possible because MEPs might include larger employers and would provide professional expertise (and hence less fiduciary exposure) in selecting and monitoring investment options and in plan management.

However, SECURE also affirmed that employers participating in open MEPs/PEPs retain their ERISA fiduciary responsibilities, including the decision whether to join a particular MEP or PEP and the selection and monitoring of investment managers and plan administrators. This reflected concerns about protecting workers when their small employers are encouraged by MEP/PEP promoters and providers to delegate to them plan management decisions and responsibilities. And the open MEP developments (including SECURE's failure to provide for any certification of MEP promoters or organizers by regulators) also speak to a broader need to fundamentally revise ERISA's employer-centric structure to facilitate appropriate non-employer-based plan sponsorship and coverage while extending to non-employer providers worker protection responsibilities that are neither excessive nor inadequate.[12]

IV. Where Do We Go from Here?

A. FOUR OVERARCHING CHALLENGES TO THE U.S. RETIREMENT SYSTEM

The future of retirement in the U.S. will be affected by at least four overarching demographic and program changes. First, the gradual aging of the American population will have significant effects on both retirement security and macroeconomic growth more broadly. Addressing this trend will almost certainly require a combination of policies ranging from possible automatic enrollment in or other means of promoting 401(k) annuities or similar retirement income products (Horneff et al. 2019) to increasing labor force participation among Americans over 65 (Harris 2020).

Second, long-term fiscal imbalances in the U.S. will eventually affect retirement policy. Given the outsized role of major entitlement programs for retirement in the federal budget—Social Security and Medicare alone comprise roughly one-third of total spending—programmatic changes to Social Security and Medicare may well be unavoidable.

Third, the shift toward defined contribution plans has closely linked issues in preparing for retirement and personal finance. Trends in financial metrics like household debt, wealth accumulation, credit delinquency rates, foreclosures, and access to retirement savings accounts have important implications for retirement as well as overall financial wellbeing.

Fourth, retirement savings issues will feature prominently in efforts to reduce or close the racial wealth gap. In 2016, the typical Black household had just 46% of the retirement wealth of the typical white household, while typical Hispanic households had just 49% (Hou and Sanzenbacher 2020). But because most Black and Hispanic retirement wealth comes from Social Security, gaps in personal retirement savings are even bigger: Black households had just 14% of the non-Social Security retirement wealth of white households, and Hispanic households had just 20% (Hou and Sanzenbacher 2020). Dynan and Elmendorf (2023) find similarly stark racial gaps in wealth and retirement savings; in particular, they estimate that the median white-headed family had eight times as much wealth as the median Black-headed family. These racial gaps have barely budged in the past 50 years (McKay 2022). Current U.S. retirement tax subsidies and the uneven effects of employer matching contributions to DC plans that go disproportionately to better compensated whites—allocate literally hundreds of billions of dollars per year in ways that exacerbate the racial wealth gap (Choukhmane, et al. 2022).

Overall, differences in retirement wealth are larger than can be explained just by racial differences in age profiles, lifetime income, or retirement plan participation. Systematic differences in the receipt of gifts and inheritances (McKernan et al. 2014) and lower rates of return for Black investors, primarily because of differences in asset classes held (Aliprantis and Carrol 2019, Hanna et al. 2010, Sabelhaus and Thompson 2022) also play at least some role. It is also likely that racial and ethnic savers use retirement assets and account features differently.

While retirement policy alone cannot eliminate the persistent racial income and wealth gaps, some of the policy changes suggested here may help. Only 47% of Black employees and 36% of Latino employees work for an employer that sponsors a retirement plan, compared to 58% of white employees (Sabelhaus 2022). Adopting Auto IRAs on a nationwide basis through federal legislation or the expansion of state-level Auto IRAs, expanding automatic enrollment and escalation in employer plans, and implementing the saver's match for lower- and moderate-income workers may play a role in addressing the significant racial, ethnic, and gender disparities in non-Social Security retirement saving and wealth. In addition, further broadening coverage for and participation by part-time and other workers is likely to have a similar effect as would having more small employers sponsor plans.

With these issues looming, SECURE and SECURE 2.0 are the latest legislative efforts to improve the U.S. retirement system. They include provisions that will take steps to raise coverage and participation, make

saving more rewarding for low- and moderate-income households, and begin to help savers manage their investments and assets during both the working years and retirement. However, both Acts were a mixed bag, as enactment required achieving bipartisan congressional agreement and the support of a range of stakeholders with largely competing commercial and policy interests. Accordingly, even though the legislation includes a number of reforms, it does not reflect a broad or comprehensive vision of needed changes to the private retirement system. As a result, there is still much more work to do.

B. FOUR SPECIFIC AREAS FOR REFORM IN THE DC PLAN SYSTEM

1. Coverage

First, far too many Americans still lack the ability to build financial security by saving through payroll deduction. While reforms in both SECURE laws will help to some extent, this problem will not be solved without requiring those employers that choose not to offer their employees some form of pension or retirement savings plan to at least support efforts to help workers save a portion of their own wages at work. As state-facilitated Auto IRA programs have proven, moderate- and lower-income employees want to save and can do so when given a behaviorally realistic opportunity.

2. Retirement Income

Second is the ability of retirees to convert their savings into income. Today, far too many people receive their savings as a lump sum when they retire and are told that only they can decide how to use them. This leaves many at the mercy of well meaning, but mistaken advice from family and friends as well as internet scams that sound promising. More widespread use of annuities can help address this issue, although too many existing annuities are unpopular, nontransparent, confusing, and expensive.

As an alternative to annuity contracts, John, Gale, Iwry and Krupkin (2021) proposed a three-stage lifetime income approach for DC plans. Most of a retiree's retirement savings would go into a pooled, professionally managed payout investment fund that targets a specified payout but does not guarantee an exact dollar amount. Monthly checks would be adjusted annually based on the pool's performance. Without contractual guarantees, these managed payout or systematic withdrawal funds avoid the regulatory and insurance costs of commercial annuities. The second component would include an emergency savings account to deal with the inevitable unexpected expenses.[13] Finally, a QLAC would provide longevity insurance covering the "tail risk" of outliving one's savings. The cost of the QLAC would be paid on retirement and consume only a relatively limited portion of an individual's savings.

As a fundamental preliminary step, the proposal also recommends that plans alert participants approaching age 60 to Social Security Administration disclosures about the increased monthly amount of guaranteed, lifetime, inflation-adjusted Social Security income payable to those who start their retirement benefits at a later age. Plan disclosures could note that it offers benefits that participants delaying the start of Social Security could rely on temporarily for income instead of using other resources.[14]

A different promising variation on this Social Security bridge concept is a proposal for workers, employers, and government to fund mandatory add-on "supplemental transition accounts for retirement" that would be integrated into the Social Security program and would make payments to individuals aged 62 to 69 for a fixed period of time (Fichtner, Gale, and Koenig 2021). This bridge also allows people to receive larger monthly Social Security benefits.

Other retirement income alternatives include trial annuities, which enroll retiring participants into two years of regular monthly payments so they can sample the annuity experience before making final decisions on how to use their retirement savings, as in Gale et al. (2008), automatic investment of employer contributions to fund accumulation income annuities (Iwry and Turner 2009), and tontine-like longevity risk pooling (Iwry et al. 2020).

Most of these retirement income alternatives could be incorporated in 401(k) or other DC plans, including col-

lective DC plans that provide professional, pooled investment management, yet these particular approaches have seen only limited or no meaningful take-up in the U.S. market to date. That said, the market is increasingly focused on the challenge of converting 401(k) account balances into regular retirement income, and a few initiatives have shown some signs of catching on. One is to embed gradually growing annuities into a plan's default QDIA target-date fund. This takes advantage of the wide acceptance of target date funds and the need for those funds to include some fixed income exposure, while accumulating deferred annuity units that enable dollar-cost-averaging of interest-rate annuity purchase timing risk (Iwry and Turner 2009; IRS Notice 2014-66).

Another promising approach is the QLAC (recently expanded in SECURE 2.0, as noted, and mainly offered to date through IRAs). In addition, as an alternative to basic income annuities, the insurance industry has been selling plans somewhat more complex guaranteed "living benefits" (lifetime or minimum withdrawal benefits as contingent annuities), fixed indexed annuities, and other products that represent variations on straightforward income annuities. Plans are also beginning to give more serious consideration to platforms offering retiring plan participants a choice of annuity options. However, it is essential that potential users of these more complex annuities understand in advance how they operate, their drawbacks as well as their advantages, and how their features and costs compare to simpler options.

3. Portability

A third problem for retirement savers is the continuing difficulty of moving their accounts when they change employers. All rollovers, regardless of size, should be made easier, faster, and more user-friendly by requiring standardization of the process and data for sending plans, receiving plans (in both cases including IRAs), and participants. In addition, the process should be made far more efficient and transparent by including the standard set of data points on documents that are regularly required to be provided to terminating participants (John et al. 2021a). Plans would be given added protections from losing their qualification for accepting rollovers that proved to be invalid, and acceptance of rollovers would then become mandatory. Congress was unwilling to impose requirements of this sort and instead adopted a weaker version in SECURE 2.0.

One other proposal would be to move from employer-sponsored retirement plans to employer-facilitated accounts that could move with the worker from job to job and could receive contributions regardless of the type of employment. In this arrangement (which might or might not be different from IRAs), an individual would receive a retirement account when they start work and unless they decided to change providers or investments, it would remain with them until retirement. When they joined a new employer, they would provide their Social Security number, bank account information for direct deposit, and retirement account number. The account could receive employee payroll deduction contributions regardless of whether the worker was considered a full time, part time, or contingent worker. If the account owner has two or more jobs at the same time, he or she would be able to contribute payments from them to the same account. In addition, employers would be allowed to make matching or other deposits if they chose to do so (Gale et al. 2020).

4. Required Minimum Distributions Reform

On a final issue, required minimum distributions, Congress, in both SECURE and SECURE 2.0, passed on the opportunity to make major reforms (Iwry et al. 2021). The RMD rules require the taxation of previously tax-deferred retirement savings gradually during retirement. They do so mainly to prevent affluent savers from repurposing those savings for estate planning by leaving them in plans and IRAs to defer tax for generations. For many seniors, these requirements—enforced by stiff penalties—are not easy to comply with, and deferring tax to or beyond future generations is not their objective. The RMD rules therefore should exempt ordinary retirees with small or moderate retirement balances, because they generally need to spend those savings during retirement in any event and will then be taxed on them.

So far, Congress has reduced the penalties for failure to comply with the RMD rules, but it has not targeted them to affect only the most affluent. Instead, SECURE and SECURE 2.0 delayed the age at which RMDs apply from 70 ½ to 72, then to 73, and ultimately to 75 while also exempting Roth 401(k) accounts from RMDs before death. Although these RMD cutbacks lose substantial future revenues without helping most ordinary retirees, they maximize profitable assets under management for the investment industry.

Far more remains to be done to improve the ability of Americans to build financial security in retirement that supplements their Social Security benefits. But federal retirement and savings legislation and regulatory initiatives over the past quarter century, combined with recent progress at the state level, suggest that, even in an era when partisanship and other obstacles impede cooperation on so many issues, further progress is still achievable.

Notes

1 Federal legislative and regulatory initiatives in the 1980s and 1990s seemed unable to reverse the decline of DB plans. In part this was because some policy measures were intended to limit companies' use of DB plans as tax-sheltered corporate savings accounts accumulating surplus dollars that companies could take back (in what were called "reversions") and use for general corporate purposes. Some of the DB decline reflected elimination of abusive plans that served the interests of relatively affluent business owners and executives to the exclusion of the rank-and-file employees who are the main intended beneficiaries of the large annual retirement tax subsidies (Iwry 2003). In the 1990s and early 2000s, many traditional DB plans were converted to "cash balance" plans, a hybrid plan design with DC-type individual accounts. Cash balance plans are more portable but typically pay fewer pensions and more lump sums. The conversions aroused intense opposition and litigation—mainly for derailing the benefit expectations of older, long-service employees caught in the transition—until legislation in 2006 required transition relief and other protections. Cash balance plans have remained a fixture in the U.S. pension market, and their proponents contend that millions of workers have retained DB coverage because their employer converted to a more appealing form of DB (cash balance) instead of dropping the DB altogether in favor of a 401(k).

2 The money purchase pension plan, a traditional and once-common form of collective DC plan in the U.S., features professional investment, restrictions on leakage, and lifetime income. Unfortunately, money purchase pensions were largely wiped out when the Portman-Cardin legislation (incorporated into the 2001 EGTRRA) expanded tax advantages for 401(k) and profit-sharing plans, a change from the longstanding policy to provide greater tax incentives for employers adopting plans with these pension-like features. See Iwry et al. (2021).

3 Improvements in financial technology also facilitated the change to DC plans operated by increasingly large financial services and recordkeeper firms.

4 One issue with the form 5500 data on which the figure is based is that a single person can "actively participate" in more than one plan (in this case, in both a DB and a DC plan) at the same time.

5 For example, by starting with a 3-percent-of-pay automatic contribution and increasing automatically by 1 percentage point per year unless the employee opted otherwise at any time. See Thaler and Benartzi (2004).

6 These estimates come from an email exchange between one of the authors and Greg Long, former Executive Director of the Thrift Savings Plan, in June 2017. The relevant portion of Long's email reads: "The TSP had plateaued at a participation rate of around 85% for about a decade. The TSP Enhancement Act of 2009, which included auto-enrollment, changed the status quo. We slowly but steadily ticked-up participation every year since and just crossed 90% in May of this year. The 300,000 figure is the approximate number of people that would not be participating if the TSP were still at an 85% rate." Full text of the exchange is available on request.

7 However, current law does not allow a Roth IRA to be rolled into a Roth 401(k).

8 In addition, Massachusetts and Missouri have adopted multiple-employer plans, New Mexico has passed a bill providing for a voluntary payroll deduction IRA, and Washington has a "marketplace" intended to help small businesses find a retirement plan.

9 While arguments can be made in defense of such provisions (e.g., increased catch-up contributions, the complicating catch-up Rothification for participants earning over $145,000, the deferrals of required minimum distributions (RMDs) while failing to exempt small savers from RMDs, the increase from $5,000 to $7,000 in the plan auto rollover threshold, some of the changes to the IRS Employee Plans Compliance Resolution System, or the significant increases to the SIMPLE-IRA contribution limits), the policy concerns they raise generally outweigh, in our view, their potential justifications. SECURE 2.0 also includes different kinds of changes that we do not have space to address or mention elsewhere in the paper, but are novel or otherwise noteworthy

and could well have meaningful positive effects even though some also raise potentially significant concerns, such as employer matching contributions for student loan repayment, the starter 401(k) safe harbor which has no employer contributions or nondiscrimination standards, $1,000 penalty-free emergency personal expense distributions, and some of the other changes to the IRS Employee Plans Compliance Resolution System .

10 Experiments in the UK showed that automatic enrollment into emergency saving increased participation by up to 50 percent of the eligible workforce and sharply increased the amount of emergency savings in the accounts. They also showed no change in retirement account savings (Phillips and Stockdale 2023). Along similar lines, actual experience with emergency saving using after-tax employee contributions in a US 401(k) plan initially shows an increase in participation from about 5 percent to about 35 percent of the eligible workforce before versus after automatic enrollment, also without any material reduction in retirement saving. (Plan Sponsor 2023).

11 In practice, a PEP operates much like a MEP, with a plan organizer and multiple participating employers. However, PEPs allow any unrelated employer to join and must be sponsored by a “pooled plan provider” that has registered with the DOL and the IRS. This plan provider will be responsible for ensuring the PEP meets all disclosure requirements and complies with both ERISA and the tax code, along with other requirements. See the discussion in https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/fact-sheets/secure-act-and-related-revisions-to-employee-benefit-plan-annual-reporting-on-the-form-5500.pdf for more details.

12 Australia’s superannuation funds and the UK’s group trusts are among the examples of somewhat analogous non-employer structures in other countries’ private pension systems (Australian Taxation Office 2023; Smith 2023).

13 The Maryland state Auto IRA program defaults savers into an emergency savings fund within the IRA account and is providing or will be providing many of the benefits listed above.

14 Working longer and continuing to save for retirement is generally preferable, but the bridge is important if an employee must stop work due to health or family situations or is laid off and unable to find another job.

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