When We All Have Access: The U.S. Retirement Ecosystem of the Future

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On Trend: Workplace Access to Savings

Can you hear it? There's a quiet revolution happening in the U.S. retirement system.

Until quite recently, about 57 million people in the United States didn't have access to retirement savings at work, meaning that they were much less likely to save for retirement. In fact, many have not been saving. It often means that some started so late that they are well behind where they need to be to live independently in retirement.

They're familiar with the traditional retirement system that covers everybody else—the folks who are unionized or who work full-time, generally for a business that is medium sized or larger and often in well-paying salaried positions. This is the system of 401(k), profit-sharing and pension plans of one stripe or another.

They may be less familiar with the way this is changing and the new entrants that are driving paycheck-linked savings for short- and long-term needs.

One new entrant is the states. Seeking to dampen significant expected increases in public safety net spending, states are looking for ways to increase retirement savings sufficiency levels. Many of them are using a promising new model, the automatic individual retirement account, or auto-IRA for short.

It's likely that by the end of 2024, as many as a dozen states will be operating auto-IRA programs. Those states are home to more than 19 million U.S. workers who otherwise do not have workplace access to retirement savings.

This change has the potential to create wide-ranging systemic opportunities for experts and providers.

Auto-IRA, You Say?

If the term *auto-IRA* is new to you, you are not alone.

First proposed at the federal level as a solution to widespread undersaving, the programs got traction in the states in 2012 with the passage of early program-related legisla-

AT A GLANCE

- Seeking to dampen significant expected increases in public safety net spending, many states are using a promising new model, the automatic individual retirement account (auto-IRA).
- As of 2022, the United States has 12 authorized state auto-IRA programs that, when fully implemented, will provide workplace retirement access for more than a third of today's estimated 57 million uncovered workers.
- Despite challenges, auto-IRAs may be adding to the value of the current retirement savings system—both public and private—and providing the opportunity to discern what is needed and tune expertise and offerings in ways that are truly fruitful and fiscally rewarding.

tion in California. Other states followed. In 2017, Oregon launched the first live auto-IRA program in the nation, OregonSaves. Illinois opened its program a year later. California also launched its program in 2018. Today, five states have live programs with an aggregate of $460 million in assets across 521,000[1] participant accounts.

At their most basic, auto-IRA programs enable workers to fund IRAs using payroll deductions. The sidebar describes the basic features of auto-IRAs.

These programs lean heavily on defined contribution (DC) account best practices from the existing retirement system. Chief among them is automatic enrollment. Workers are free to opt out of participation and to increase or decrease their savings, but covered workers have to take an action if they choose not to save. Near-universal access to retirement savings in auto-IRA states is boosted by the state-level requirement for covered employers to facilitate the program if they do not otherwise offer a retirement plan.

Although the programs aren't identical to each other, they tend to have certain common characteristics, including:

- Automatic enrollment—Often at 5% of employee pay
- Automatic escalation—Often to a 10% cap
- Streamlined investment menus
- Roth IRAs as standard account type
- A focus on simplicity and ease of use.

As of 2022, the U.S. had 12 state auto-IRA programs authorized from coast to coast. States include California, Colorado, Connecticut, Delaware, Hawaii, Illinois, Maine, Maryland, New Jersey, New York, Oregon and Virginia. When fully implemented, these programs can provide workplace retirement access for about 19 million workers—more than a third of the 57 million workers who are estimated to be uncovered today (Table I).

Does that mean non-auto-IRA states are inactive, immune to or ignoring the coming ramp-up in costs associated with undersaving? In short, they are not. In the last decade, almost all states have made legislative proposals related to state-facilitated retirement savings.

In addition to the 12 auto-IRA states, four states have enabled other types of programs. Massachusetts and Vermont have authorized multiple employer plans (MEPs)—a state version of the pooled employer plans (PEPs) that are now becoming popular in the private sector. Washington State and New Mexico have authorized retirement savings marketplaces, and New Mexico's legislation includes a companion program, an employer-voluntary payroll deduction IRA.

Where launched, these programs have seen limited usage so far and are not experiencing the widespread penetration that the auto-IRA model provides. At the same time, they are contributing points of access for employers and adding invaluable information to the development of best practices in the public and private sector savings space.

What will the legislative sessions of 2023 bring? It's anyone's guess but, since 2015, an average of one to three state retirement savings bills have passed into law each year. The question is not whether more states will pass legislation but which one will be next.

What Is an Auto-IRA?

Automatic individual retirement account (auto-IRA) programs can make it easier for employees to save for retirement at work because of the following features.

- Automatic enrollment with opt-out
- Contributions by payroll deduction
- IRAs are portable and tax-advantaged
- Simple, inexpensive investments
- Flexibility—Savings, investments, opt-out
- States establish and manage
- Private sector provides services, including administration and investments
- Employers facilitate deductions

How It's Going: Program Usage Experience

Early predictions were that auto-IRA programs would be raging successes or miserable, expensive failures.

Program Growth

As of August 2022, across the three longest running programs (California, Illinois and Oregon), about 521,300 sav-

ers had accumulated more than $460 million in retirement assets. This can seem large or small, fast or slow, depending on your perspective.

The first programs began rolling out statewide to small numbers of savers in 2018. Not until late 2019 and early 2020—into the teeth of the pandemic—did they begin to be available to more than a million potential savers. By comparison, we would have to think hard about the last time the retirement savings system added half a million funded accounts over a similar time frame.

As state programs have progressed, program growth has been solid and steady. Although there is insufficient data to prove it, the growth curve associated with state auto-IRAs so far looks a great deal like the growth curve of new 401(k) plans when they were first gaining adoption in the early to mid-1980s (Table II).

As of late 2022, the CalSavers program was becoming available to the largest single wave of workers covered by an auto-IRA. It's estimated that more than 6 million Californians will soon be able to participate in CalSavers as their employers register and begin to facilitate payroll deductions.

TABLE I

States With Authorized Auto-IRA Programs

Auto-IRA State	Before Auto-IRA Uncovered Workforce	Program Live or Anticipated Live Date
Oregon	759,474	2017
California	6,676,205	2018
Illinois	2,195,023	2018
Connecticut	639,116	2022
Maryland	1,096,394	2022
Colorado	1,122,953	2023
Maine	236,997	2023
Virginia	1,491,537	2023
New Jersey	1,556,081	2023-4
New York	3,230,441	2023-4
Delaware	173,926	2024
Hawaii	215,000	2024-5
In auto-IRA states	19,393,146	34%
National uncovered	56,626,884	

Source: Massena Associates, LLC, computed using public information.

Program Participation

Despite some differences in program timing and levels, it is striking to see how similar employee response has been across the three states with the longest running programs. Retention rates across each of the programs are hovering at around 68%. This means about a third of eligible workers are formally opting out of the savings opportunity when it is presented, but the majority are not.

In traditional 401(k) plans with automatic enrollment, we see higher retention rates—generally 90% or greater. It's worth closer study, but we see several factors that could contribute to lower rates of participation in auto-IRA programs, including:

- Lower compensation rates
- The inclusion in the covered population of workers below the poverty line
- The lack of any form of savings match or equivalent incentive
- Newness of the programs and low initial awareness levels.

Contributions

Auto-IRA programs by their nature cover employees who, as a group, work in higher turnover and lower compensated jobs than their counterparts whose employers offer plans. The median earnings for these workers has been measured at between $29,000 and $36,000 a year in the live auto-IRA states. This compares with wages that are much higher for employees whose employers offer plans.

Because of this, states early on deliberated over the starting savings rates for automatically enrolled employees. While some states have set rates as low as 3%, the most popular current rate is 5%.

Across the three longer-running programs, average savings rates vary from 5.1% in California to 5.6% in Illinois

TABLE II

State Auto-IRA Program Asset Growth

	Rate of Change			Year End		
State Auto IRA Programs[1]	**YTD**	**12/31/2020**	**Most Current**	**12/31/2021**	**12/31/2020**	**12/31/2019**
Total assets	13%	2.6x	**$ 459,502,649**	$ 407,904,516	$ 160,100,055	$ 407,904,516
Funded accounts	21%	1.7x	**521,332**	429,663	263,764	108,945
Average account balance	-7%	1.5x	**$ 881**	$ 949	$ 607	$ 503
Employers registered to facilitate	174%	1.7x	**127,655**	46,636	28,999	19,498
Employers have added employees	194%	1.7x	**100,559**	34,254	22,076	13,350
Employers started payroll[2]	81%	1.6x	**30,567**	16,889	11,439	5,134
Effective opt-out rate[2,3]	5%	-2 points	**34%**	33%	34%	35%
Effective participation rate[2,3]	-2%	+2 points	**66%**	67%	66%	65%

1. OregonSaves, Illinois Secure Choice and CalSavers.
2. Hybrid data as of publication—October 31, 2021 for Oregon and July 31, 2022 for Illinois and California.
3. Computed as a simple average of the three programs.

Source: Massena Associates, LLC, August 2022.

and 6.2% in Oregon. Each of the programs starts with an automatic savings rate of 5% that can be adjusted up or down by savers. All three states auto-escalate savers who have been in the program for six months or more. For these savers, savings rates increase by 1% each January unless the saver opts out of the increase. The programs in Oregon and Illinois cap escalation at 10%. California currently caps automatic escalation at 8%.

These savings rates are translating to current average monthly savings of between $139 and $176.

Withdrawals

The state programs have made account withdrawals deliberately easy. Roth IRAs allow this to be done on a minimally impactful basis, and the states' rationale for easy access is multifaceted.

- Savers have access to their money for emergencies.
- Enrollees will have confidence that savings are accessible if needed or desired.
- The accounts offer the chance to "try as you buy"—because workers can have their savings returned if desired.
- Workers who find themselves unintentionally enrolled can have their money returned.

In practice, a portion of savers do withdraw funds. More than half of withdrawals are full cashouts, while the balance are partial withdrawals for savers who continue to contribute. A chunk of these withdrawals are clearly for workers who find themselves enrolled but don't currently want to save through the program. The reasons for other withdrawals are mixed. Anecdotally, some savers report that they wanted to try the program but find they are not currently able to save. Along a separate pathway, states report that they see spikes in withdrawals every time quarterly statements land in mailboxes.

As of mid-2022, Oregon program data shows that about 25% of all funds ever contributed have been withdrawn. California's cumulative withdrawal rate is lower—at about 12.6%—possibly reflecting the newness of the program relative to Oregon's or other reasons.

Participation, contributions and withdrawals are expected to be areas of close focus as the programs accumulate more time and data.

State Auto-IRA Programs and the Private Sector

Before they launched and in their early days, state auto-IRA programs caused a small ruckus from those in the private sector community who were watching the space.

Concerns included the potential for state programs to cannibalize the existing retirement system, causing employers to drop their current plans like hot potatoes in favor of something easier and much less expensive. In reality, employers offer retirement plans for many reasons, and those plans provide employees with distinct and important benefits that IRAs—and, therefore, auto-IRA programs—can't replicate.

Experience indicates that employers are not terminating their Employee Retirement Income Security Act of 1974 (ERISA) plans in response to auto-IRA plans. (As a preventive measure to discourage this, most states have lengthy cooling-off periods in case this is contemplated.) Instead, a Pew Charitable Trusts multiyear study of Form 5500 data seems to show that in states with active auto-IRA deadlines, new plan formation has risen significantly.

Generally speaking, state auto-IRAs seem to be settling into and becoming a normal part of the existing landscape in the states where they are authorized. Opposition to the programs has softened and declined. Provider activity seems to show that many firms understand the private sector opportunity created by these programs. With new plan formation up, providers are concentrating on simple, low-cost and entry-level retirement plans and products, and some are intentionally focusing sales activity on auto-IRA states.

Program Challenges: It's Not All a Cakewalk

As with any statewide effort, states' activities to date have largely centered on organizing, funding and launching their new programs. They have and do face a plethora of challenges along the way. Some of these are large and obvious and apply to any new initiative a state undertakes, including:

- Developing program awareness for users and affected parties
- Establishing a program "persona"—Friendly, authoritative, both, other
- Determining whether and how to enforce employer compliance
- Keeping key stakeholders informed and satisfied with results
- Procuring program providers that can provide quality, public-facing services at favorable rates
- Managing program financials and funding sources—Public, user, private, other
- Ensuring that programs comply with applicable laws, regulations and statutes.

It may or may not be intuitive, but creating awareness is a top challenge for all programs. Most have stringent budgets that don't allow for heavy advertising. For this reason, states use a mix of methods to communicate—including some advertising—but they use larger amounts of earned media, cost-effective social media, cultivation of associations and organizations serving businesses and workers, and direct communication by mail and email to tranches of employers as their program deadlines approach.

Program growth rates also present challenges. With low levels of state financial commitment and a dependence on savers to fund program costs, states find themselves in a balancing act with providers to keep costs low while the programs slowly move toward the size and scale that allow providers to offset their own operating costs. Some programs are beginning to add account-level fees to flatten this curve for providers and achieve breakeven faster.

Finally, states have been the subject of a number of legal challenges. These tend to intersect with ERISA and follow two streams: (1) whether in the act of requiring exempt employers to indicate their status, the programs are placing an undue burden on ERISA plan sponsors and (2) whether the programs themselves are preempted by ERISA.

These challenges have been resolved to date, most recently with the February 2022 decision by the U.S. Supreme Court not to review the Ninth Circuit Court of Appeals 2021 ruling in favor of the CalSavers Retirement Savings Program. The Ninth Circuit ruling stated: "We hold that the preemption challenge fails. CalSavers is not an ERISA plan because it is established and maintained by the State, not employers; it does not require employers to operate

their own ERISA plans; and it does not have an impermissible reference to or connection with ERISA. Nor does CalSavers interfere with ERISA's core purposes. Accordingly, ERISA does not preempt the California law."

Implications for the Future of Retirement Savings

The entrance of state auto-IRA programs is changing the retirement savings ecosystem in ways that deserve thoughtful consideration. Here are a few worth a closer look.

Coverage: The Pie Is Getting Bigger

At a minimum, state auto-IRAs are going to expand coverage to at least a third of the 57 million previously uncovered U.S. workers. Some might expect more expansion—perhaps to half of the uncovered workforce—but the two biggest states without programs, Texas and Florida, are at the moment also the least likely to legislate in favor of state-facilitated retirement savings. A number of states that follow them by size could legislate, and some of them (Pennsylvania) are currently very active.

As state programs spread, they may become a catalyst for the federal government to act to create a national standard for more universal workplace access to retirement savings. There is likely to be a federal requirement for employers to facilitate payroll-based saving before 50 states adopt an auto-IRA program.

That said, consider what could happen when 80% of the workforce has access to workplace savings, and perhaps more than half are being automatically enrolled and auto-escalated.

- More savers with assets will need more services—At both the institutional and the individual levels.
- The U.S. system will have a new class of savers with lower account balances, especially initially and for a time. This has interesting implications for the use of smartphone-based services and the use of automated, event-based support (nudges).
- The norm may shift (is shifting) in the direction of savings as a more expected, more universal behavior among workers of all ages.
- Slowly, required commitments to social services such as Medicaid could level off and perhaps even decline.

Innovation: Emergency Savings, Lifetime Income, Nudges and More

State retirement savings programs are springing to life in an environment that has become rich with innovation over the last eight to ten years.

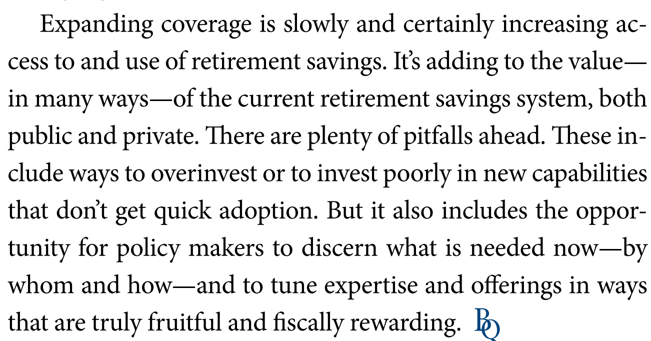
Many of these advances are synergistic and include the following.

- **Pooled employer plans (PEPs)—**PEPs may turn out to have many uses beyond the original legislative intention. They are expected to provide for professionalization and simplification of retirement plans at the small end of the market and should make a perfect "step-up" plan for employers graduating out of the state auto-IRA system.
- **Lifetime income—**Plan sponsors wrestle with whether and how to provide integrated annuities and other lifetime income strategies for retirees. SECURE Act 2.0 could reduce some of the fiduciary risk and expand the solution set but, candidly, employers have moved at a glacial pace in this space. Many of the state programs are deeply interested in providing these sorts of transition-to-retirement options. States in some ways have more flexibility to innovate and may be early adopters with useful proof-of-concept results that support private sector plan sponsor decision making.
- **Emergency savings—**A hot topic in the private sector, emergency savings has been a theme among auto-IRAs since their initiation. For lower income savers, emergency access to savings may be an essential part of the ability to save in the first place. Now, states are beginning to think about whether retirement-adjacent emergency savings accounts should be an explicit part of their programs rather than an implicit capability of a retirement-oriented Roth account. Some 401(k) plan sponsors are beginning to experiment here as well.
- **Artificial intelligence (AI) and nudges—**Except for the built-in features of automatic enrollment and escalation, states are not using many other AI and "nudge" elements in their programs. However, as public and private services to small-balance savers expand, these features only make sense. They're an efficient and effective way to help savers help themselves.

How does this matter to experts and providers? The expanded group of savers, larger asset pools and use cases associated with serving savers from this point forward are good reasons to innovate—to develop and price useful capabilities that people and organizations need, will benefit from and will pay for.

Bringing It Home

Expanding coverage is slowly and certainly increasing access to and use of retirement savings. It's adding to the value—in many ways—of the current retirement savings system, both public and private. There are plenty of pitfalls ahead. These include ways to overinvest or to invest poorly in new capabilities that don't get quick adoption. But it also includes the opportunity for policy makers to discern what is needed now—by whom and how—and to tune expertise and offerings in ways that are truly fruitful and fiscally rewarding. BQ



Endnote

1. Blended data from June 30, 2022 and July 31, 2022.

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International Society of Certified Employee Benefit Specialists

Reprinted from the First Quarter 2023 issue of *BENEFITS QUARTERLY*, published by the International Society of Certified Employee Benefit Specialists. With the exception of official Society announcements, the opinions given in articles are those of the authors. The International Society of Certified Employee Benefit Specialists disclaims responsibility for views expressed and statements made in articles published. No further transmission or electronic distribution of this material is permitted without permission. Subscription information can be found at iscebs.org.

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