ICI VIEWPOINTS

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Building on the Success of the Private-Sector Retirement System Is the Real "Secure Choice"

Retirement assets in the United States totaled $24 trillion at the end of 2015, bolstered by investments through employer-sponsored plans and individual retirement accounts (IRAs). Nevertheless, there are still millions of American workers who lack access to retirement plans through their employers. This gap has spawned a public policy debate in Washington and in state capitals about how best to expand access to retirement saving opportunities.

We can, and should, do more to expand access to retirement savings for individuals who have the means and desire to save. That is why ICI and the fund industry are working to advance sensible reforms at the national level that build on the successes of the private retirement system.

One bipartisan proposal—endorsed by President Obama, House Speaker Paul Ryan (R-WI), and Senate Finance Committee Chairman Orin Hatch (R-UT)—would enable unrelated small businesses to join together to form open multiple employer plans, or MEPs. Allowing companies to band together to offer those plans reduces costs for employers that otherwise might not be able to afford the plans. This is a sensible way to help workers build their retirement nest eggs. Yet current law restricts MEPs to employers sharing a so-called commonality of interest—a requirement that dramatically limits their use.

Another idea, similar to Hatch's "Starter 401(k)" proposal, is to create a "Simpler" plan. Like the SIMPLE IRA and SIMPLE 401(k), a Simpler plan would have less red tape for employers to deal with than full 401(k) plans. The Simpler plan also would not require employer contributions, making it less expensive for small employers, and thus easier to offer.

An Uncertain Approach

Regrettably, a very different approach fraught with uncertainty is currently taking hold in several states. A handful of state governments have enacted "Secure Choice" laws to establish state-run retirement accounts for private-sector workers whose employers do not offer retirement plans.

At the behest of the White House, the Department of Labor (DOL) is trying to enable a "crazy quilt" approach that is inevitable if these states get their way. Labor Secretary Thomas Perez and National Economic Council Director Jeffrey Zients argued in a recent blog post that “these state savings programs offer American families a simple, consistent method to put away money each month that will grow toward what they need for a comfortable and well-deserved retirement.” In reality, however, these programs are far from consistent, they fall short when measured against existing private-sector options, and they ultimately could create financial burdens for workers and state taxpayers.

California’s Secure Choice proposal is the most prominent example. The scheme would automatically enroll workers in a new savings plan, regardless of the individual’s ability to save. Workers could opt out of the new government-run plan, but those who remain could find that their investment options are severely limited and less competitive than options offered in the private sector. Participants also could be expected to pay a total fee of up to 100 basis points (1 percent of assets) to cover operating expenses and recoup the program’s start-up costs. By contrast, more than 90 percent of equity mutual fund assets in private-sector IRAs are in funds that charge less than 100 basis points in operating expenses, and private-sector IRA investors have more investment choices than the state-run plan contemplates. Compared to what is already available in the private sector, California’s government-run plan is hardly a platform for a secure retirement.

Lacking Legal Protections

Californians automatically enrolled in Secure Choice also would be denied legal protections that apply to private-sector plans. The DOL has proposed a rule exempting state-run retirement programs—such as the program being considered by the California legislature—from the federal Employee Retirement Income Security Act of 1974 (ERISA) and its accompanying consumer protections and rights of action. Given the lack of ERISA protections and the possibility that state immunity laws would shield California officials responsible for operating the program from being held accountable for mistakes or misconduct, plan participants could have no legal recourse if management of the programs proved faulty. When you consider the track record of mismanagement and deficits associated with state pension programs for their own employees, one has to wonder if exempting Secure Choice plans from vital ERISA protections makes sense or would make investors feel secure.

California’s taxpayers should worry, too, because they also face risks with Secure Choice. ICI’s analysis of the feasibility study associated with California’s plan found discrepancies that raise questions about the financial health of the government-run plan. Specifically, the study makes hasty, unrealistic assumptions about how many workers would participate and how much they would contribute—raising the possibility that funding for the program would come up short. If it does, California taxpayers would be left to pay the outstanding costs, adding to the state’s fiscal burden.

Though specifics surrounding Secure Choice retirement proposals differ by state, many of the state-based programs seem likely to bring similar restrictions in investment options, high fees, and fiscal risks for taxpayers. And if the trend toward such plans continues, the country could soon be facing a complicated 50-state regulatory maze that will make the U.S. retirement system more fractured—and less effective—for the growing number of workers trying to save for their golden years.

Rather than gamble on new state-run alternatives that are unproven at best and deeply flawed at worst, we should work to create nationwide solutions that build upon the private-sector system that is already working well for the majority of America’s retirement savers. Clear policy proposals with bipartisan support are already on the table. It’s time for Congress to act on them.

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