Retirement Security in Peril

JOINT ECONOMIC COMMITTEE
DEMOCRATS

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Ranking Member

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American workers are facing a crisis: the inability to retire with dignity after a life of hard work. After years of supporting families and contributing to society, American workers are confronting a nearly empty retirement nest egg. Half of all American families near retirement have $12,000 or less in formal retirement savings.[1] Not only do far too many workers earn too little to adequately save for retirement, but many more also lack access to good retirement saving plans. Many other factors, including the 2007 financial crisis and slow wage growth, have exacerbated the problem.[2]

Congress must now focus on policies that broaden access to low cost, high-yield retirement savings options, strengthen Social Security, secure pension plans, and restore access to a stable and adequate retirement for an aging population.

Challenges to Securing a Stable Retirement

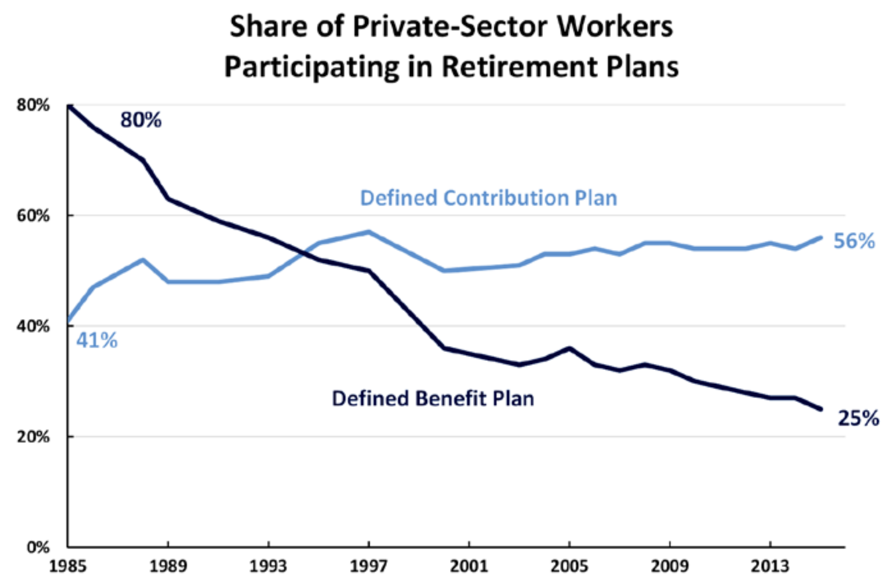
Working Americans face a host of challenges in planning and saving for retirement, including inadequate savings, stagnant wages, limited access to low-cost and high return accounts, among others. These challenges, which all have compounding impacts on later life living standards, are making it more difficult for families and workers to establish a foundation for a secure retirement.

The Shifting and Slimming of Plans

Most employers no longer provide defined benefit plans, such as traditional pension plans that provide a guaranteed source of income into retirement. Instead, they have shifted the responsibility of preparing for retirement onto employees through defined contribution retirement plans, like 401(k)s and IRAs. Only 25 percent of private sector employees in medium and large firms participate in defined benefit plans, a sharp decline from the 1985 high of 80 percent (see next page).[3] The drop in availability and participation in these plans comes as employers attempt to reduce the risk and cost of providing benefits.[4]

Teacher Pensions: Defined Benefit Plans in Action

Teacher pension plans are an example of the key role that defined benefit plans play in providing families a stable retirement. Teacher pensions, much like other defined benefit plans, provide a more secure path to retirement, helping many teachers overcome the multitude of obstacles that prevent saving for retirement.[5] More than 75 percent of teachers participate in defined benefit plan.[6] These pension plans reward longevity with an employer, creating economic incentives for high-quality teachers to stay in the profession. These plans serve as effective recruitment and retention tools for schools, helping attract and maintain the best teachers to ensure student success. Pension plans also afford teachers a more predictable source of income into retirement, which is particularly important for low- and middle-income teachers.[7]



Sources: Employee Benefit Research Institute and the Bureau of Labor Statistics, National Compensation Survey

Notes: Employees at medium and large establishments, 1985 to 2015. "Medium and large establishments" denotes those with 100 or more employees; data are interpolated for the following years: 1987, 1990, 1992, 1994, 1996, 1998, 1999, 2001 and 2002.

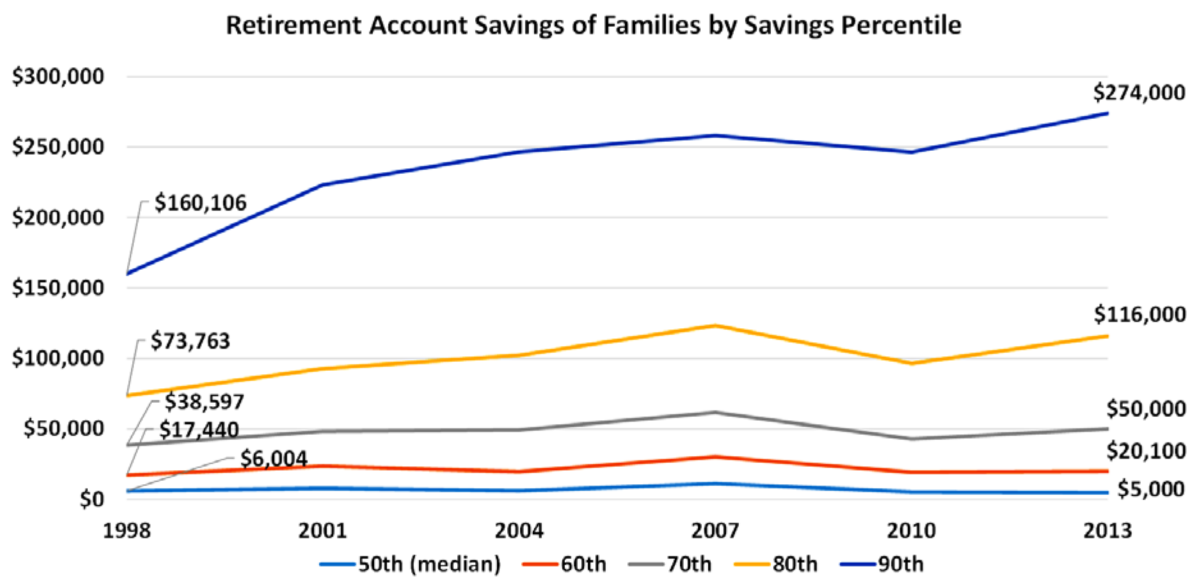
On the other hand, participation in defined contribution plans has steadily increased from 41 percent in 1985 to 56 percent in 2015 for the same workers.[9] Defined contribution plans, such as 401(k)s mentioned above, generally depend on the financial contributions made by the employees themselves. These plans do not commonly guarantee a worker income for life like most pension plans and typically have funds invested in more volatile securities and assets in an attempt to reach higher returns. While defined contribution plans can have higher potential long-term gains, particularly when markets are rising, workers assume investment risk that under defined benefit plans would have been borne by their employers. Modern retirement savers assume the risk associated with investing in the stock market, leaving their savings exposed to management fraud, exorbitant management fees, and market fluctuations exacerbated by Wall Street risk-taking.

Defined Contribution Plans: What are they?

Defined contribution plans are a type of retirement plan in which the employee, the employer, or both agree to make regular contributions to a retirement account. Contributions are normally invested on the employee's behalf and can return gains or losses. Employer contributions are not always fixed, since they are often contingent on voluntary employee contributions, and do not normally promise a specific amount of benefits in retirement. Some of the most common defined contribution plans are employer sponsored 401(k) and 403(b)s.[8]

Further, while workers who start saving early in their careers have time to withstand market downturns, a financial crisis or economic downturn can profoundly diminish savings for those closer to retirement in defined contribution plans.[10] Older Americans closer to retirement with deflated accounts may have less time to make up financial loses, forcing many to continue working into older age—a stark reality for many Americans following the financial crisis and economic downturn of the last decade. In fact, nearly 19 percent of

Americans 65 years or older continue to work at least part-time, with future generations expecting to work past 65 at a much higher rate.[11]



Source: Economic Policy Institute analysis of Federal Reserve Survey of Consumer Finance data, 2013.
Note: Retirement account savings include 401(k)s, IRAs, and Keogh plans for families age 32-61, 2013 dollars.

While those with defined contribution plans must weather swings in the stock market, defined benefit plans have also faced scrutiny and have seen significant cuts to promised benefits. Since 2009, local and state pension plans, which now represent a majority of defined benefit plans, have seen benefit cuts and other changes.[12] These cuts are in part a response to the sharp decline of state and local pension fund assets following the market crash, and shift the risk and burden onto plan participants.[13]

Many of the changes to defined benefit plans are aimed at both current and new employees. From 2009 to 2014, over 55 percent of local plans and nearly 75 percent of state plans made cuts to benefits affecting both new and current employees.[14] The result is usually an increase in employee-required contributions, a decrease in overall benefits promised, and longer service requirements to be eligible to receive similar benefits.[15] Similar benefit cuts and reforms are affecting other defined benefit plans as well.[16]

Multiemployer plans, which are defined benefit plans created through collective bargaining agreements and funded in collaboration with multiple employers typically in the same or related industry, cover about 10 million American workers and are found in many industries.[17] Many of these plans have struggled in recent years due to a number of factors, including asset losses from the financial crisis, declining ratios of active workers to retirees within the plans, and a low interest rate environment which raises the value of their future liabilities relative to current assets.[18] These problems are exacerbated when individual employers leave the plan without contributing enough to cover their pension commitments. This now leaves about a million participants in underfunded plans.

The Gig Economy, Workers, and Access to Retirement Plans

As the importance of the gig economy keeps growing, the work-force relationship grows more complex. The rise of the gig economy—which allows people to work from remote locations to complete short-term projects and contracts—has grown the size of contingent workers.

Independent contractors, better known as contingent workers or freelance workers that have a contracted relationship with a company, now make up about 16 percent of the American labor force, up over 50 percent since 2005.[19] The nonpermanent status of contingent workers creates new complexities that reshape how individuals are compensated, limiting access to employer sponsored retirement plans, among other benefits. Contingent workers were two-thirds less likely to have access to employer provided retirement plans than their traditional employee counterparts.[20] Limited access to benefits and the growing prevalence of contingent work present new challenges to ensure adequate retirement plans for a growing share of Americans.

Slow Wage Growth Limits Retirement Savings

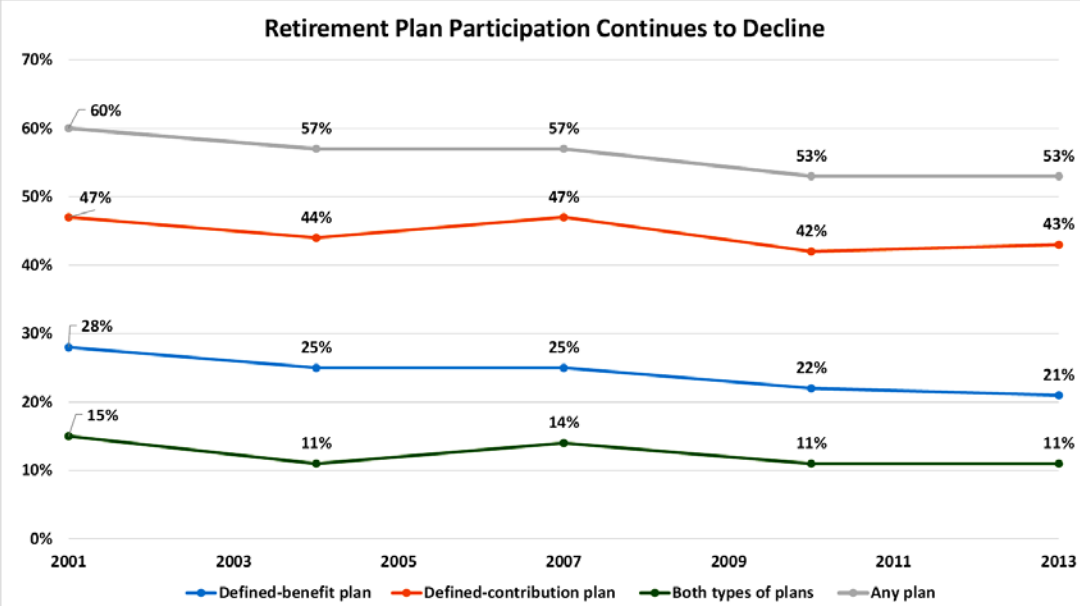
While wage growth has picked up over the last few years, it has not been enough to ensure adequate savings for many families.[21] When adjusted for inflation, many low-wage workers have actually seen their wages stagnate or fall over the past few decades, leaving little for many working families to put away for retirement.[22]

The problem is more pronounced for bottom income quintile families and single parent households. Compared to high-income earners, low-income families have less in retirement savings accounts; in fact, high-income families are eleven times more likely to have a retirement account than families in the bottom income quintile.[23]

As the chart on the prior page indicates, retirement account savings for the bottom 50 percent of families remain very small and have actually declined by 17 percent since 1998, while those in the top 90 percent have made substantial gains of more than 70 percent over the same period. Additionally, as of 2013, the median family's retirement account had only $5,000.[24]

Insufficient Access to, and Participation in, Workplace Retirement Savings Plans

Access to workplace retirement savings plans is key to establishing workers' future economic security, but many workers are still unable to access low-cost, high-quality plans. This is particularly true for gig economy employees, who have grown as a share of the economy over the last decade (see box above).[25] While access and participation rates vary by state, well over 30 percent of full-time private sector workers do not have access to either defined benefit or defined contribution plans through their employer, with part-time workers having even less access.[26] If non-participants were given access to affordable retirement savings plans and adequate workplace matching contributions, most say they would be more willing to take advantage of the opportunity to save for later life.[27]



Source: Economic Policy Institute analysis of Federal Reserve Survey of Consumers Financial data, 2013.
Note: Shares indicate whether the respondent or her or his spouse participated in a plan (s) at a current job (individual participation rates are lower).

Education, age, employer size, industry, and income play a significant role in determining access to, and participation in, retirement savings plans.[28] Families headed by someone with a college degree or more, for example, have a higher likelihood of a worker participating in a retirement plan.[29] This also true when comparing total balances of retirement savings accounts.[30] The underlying trend over the last decade, though, is an across-the-board decline in retirement plan participation rates. This is in large part due to the lack of access to low-cost, high-quality savings plans.[31] The figure below highlights this ongoing declining trend, particularly as workers approach retirement, though older cohorts as a group save more than younger workers.[32]

Millennials' Impact on their Parents' Retirement Savings

The rising cost of education has also made retirement readiness more difficult for all aging Americans. Recent data show that the number of older Americans with student loan debt quadrupled from 2005 to 2015.[33]

Older Americans now own an estimated $247 billion in outstanding student loan debt, an amount that has grown substantially since the beginning of the 21st century, even after accounting for inflation.[34] These older borrowers are parents who finance their children's education and individuals seeking to further their own education later in life. Unfortunately, those with student debt are more likely to have lower retirement account balances, and, if they default on the loan, often have to surrender about 15 percent of their Social Security benefits to pay their loans.[35] To make matters worse, many defined contribution plans often do not allow participants to draw against their savings to supplement a child's tuition without a penalty.

With the additional burden of loans, older borrowers often struggle to repay and become delinquent. In addition, older Americans with outstanding student loans are also more likely to neglect their important health care needs, including dental care and regular doctors' visits.[36]

The Significant Role of Social Security

As individual earnings and incomes decline with age and more workers are pushed into more volatile defined contribution plans, the role of Social Security grows. Social Security is the largest federal anti-poverty program, providing 62 million beneficiaries—retirees who have worked for 35 years or more, disabled workers and their family members, and family members of deceased workers—monthly financial benefits.[37] By ensuring income and economic security into old age, Social Security lifts more than 15 million elderly Americans out of poverty.[38] Without it, the poverty rate for individuals age 65 or older would more than triple, leaving four in ten older Americans living in poverty.[39] Average monthly benefits at the end of 2015 ranged from $1,166 to $1,342 for beneficiaries, but were considerably less for women and those with low incomes during their working lives.[40]

With half of all American households near retirement holding less than $12,000 in formal retirement savings and more Americans working into older age, Social Security is playing an increasingly important role for retirees, particularly low-income seniors.[41] Currently, nearly nine out of ten of people over the age of 65 receive Social Security benefits.[42]

Unfortunately, Republican proposals would cut Social Security benefits and the Social Security Administration's budget to address budgetary shortfalls.[43] Administrative cuts squeeze the agency's ability to provide necessary services to an aging population. These actions can be disastrous to the millions of people who rely on the program, undermining their economic security and stability. Suggested reforms to Social Security, many of which propose deep cuts to benefits and changes to existing requirements, would wreak havoc on family finances and could push many into poverty.

Next Steps for Congress

Without improved access to retirement benefits, Americans will continue to struggle to provide a safe and secure retirement for themselves and their families. There are several steps that policymakers can take to address the retirement crisis and ensure that older Americans can age with dignity.

First, Congress needs to modernize Social Security, which remains the primary and most reliable source of income for retirees. Changes should focus on expanding benefits for hard-working Americans, and ensuring long-term viability and security. Policymakers have discussed raising the current payroll tax cap of $128,400 so that a larger share of wealthier Americans' earnings would go into the Social Security trust fund and increasing the payroll tax rate marginally if real wage growth accelerates.[44]

Workers should also have better access to employer-based retirement plans. Given that employers are now more likely to offer defined contribution plans than pensions, employers should be more engaged in assuring retirement readiness. There are several policy proposals that expand access to defined contribution plans, while reducing administrative costs. These proposals include establishing "startup" tax credits for small businesses that offer retirement plans for the first time, allowing businesses to pool their defined contribution plans, opening up retirement plans to part-time workers, and ensuring that financial advisors protect seniors' hard-earned investment by putting their clients first.[45]

It is also important that policymakers secure the long-term stability of the Pension Benefit Guaranty Corporation (PBGC), a critical backstop for private sector pension plans that ensures timely and uninterrupted payments should a plan become insolvent. With the pension benefits of nearly 40 million Americans insured through the corporation, PBGC's financial future remains uncertain.[46] This is in part due to the financial risk of the countless underfunded pension plans that PBGC insures and the declining number of private defined benefit plans.[47] Congress has taken the approach of issuing short-term fixes for the program, and it should work to create a long-term solution to ensure that the PBGC's protections continue to cover workers' retirement benefits.[48] This includes addressing the multiemployer pension crisis with innovative solutions, like the Joint Select Committee to Solve the Multiemployer Pension Crisis or the Butch Lewis Act of 2017 that strengthen these plans covering millions of Americans.

Finally, there needs to be new ways to entice employers and state and local governments to provide access to high benefit, low cost retirement plans. Proposals like the Preserve Rights of States and Political Subdivisions to Encourage Retirement Savings (PROSPERS) Act that allow for more flexibility and better access to retirement accounts are good options.[49] These measures all work towards a retirement system that is inclusive, portable, and enhances long-term security for workers from many economic backgrounds.

As we move further into the 21st century, it is imperative that Congress initiates reforms that allow American workers to live fruitful lives into retirement. This includes having access to multiple income streams as seniors ease into retirement.

[1] http://www.nirsonline.org/index.php?option=content&task=view&id=768; Note: figures are for 2010.
[2] http://www.epi.org/publication/retirement-in-america/; and https://www.jec.senate.gov/public/_cache/files/4bc4e022-4bc8-476c-a91a-268852d8ff0e/pensions-report---fact-checked-12-21-2-.pdf
[3] Employee Benefit Research Institute and the Bureau of Labor Statistics, National Compensation Survey; https://www.jec.senate.gov/public/index.cfm/democrats/press-releases?ID=A6E01566-5EBA-42EB-8BA7-F1BB6D32707A; http://www.ebri.org/pdf/publications/books/databook/DB.Chapter%2005.pdf; and https://www.bls.gov/ncs/ebs/benefits/2017/ownership/private/table01a.pdf
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[11] https://www.bloomberg.com/news/articles/2017-07-10/working-past-70-americans-can-t-seem-to-retire; Note: Bloomberg analysis based on U.S. Department of Labor data 2017-Q2. Also, this cohort's employment to population ratio is the highest it has been since 1961.
[12] http://crr.bc.edu/wp-content/uploads/2016/12/slp_54.pdf
[13] *Ibid*.
[14] *Ibid*.
[15] http://www.nasra.org/files/Spotlight/Significant%20Reforms.pdf
[16] https://www.washingtonpost.com/news/get-there/wp/2017/01/27/in-unprecedented-move-pension-plan-approves-benefit-cuts-for-retired-iron-workers/?utm_term=.a7f80dde7a6e; and https://www.ebri.org/pdf/notespdf/0704notes.pdf
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[22] http://www.hamiltonproject.org/assets/files/thirteen_facts_wage_growth.pdf; and http://www.pewtrusts.org/~/media/assets/2015/01/fsm_balance_sheet_report.pdf
[23] http://www.epi.org/publication/retirement-in-america/ Note: See charts 7 and 9. Families are for individuals age 32-61.
[24] *Ibid*.
[25] https://www.brookings.edu/research/retirement-plans-for-contingent-workers-issues-and-options/
[26] http://www.pewtrusts.org/~/media/assets/2016/09/employersponsoredretirementplanaccessuptakeandsavings.pdf
[27] http://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/12/workers-open-to-retirement-plan-features-intended-to-boost-savings .
[28] http://www.pewtrusts.org/~/media/assets/2016/01/retirement_savings_report_jan16.pdf
[29] http://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/02/retirement-plan-access-and-participation-across-generations; and http://www.epi.org/publication/retirement-in-america/#chart12
[30] *Ibid*.
[31] http://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/02/retirement-plan-access-and-participation-across-generations; and EPI analysis of Survey of Consumer Finance data, 2013.

[32] http://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2017/02/retirement-plan-access-and-participation-across-generations
[33] http://files.consumerfinance.gov/f/documents/201701_cfpb_OA-Student-Loan-Snapshot.pdf
[34] https://www.urban.org/urban-wire/complexity-education-debt-among-older-americans. Note: In estimating outstanding student loan debt, older Americans are defined as over 50 years old.
[35] https://www.gao.gov/products/GAO-17-45; and http://files.consumerfinance.gov/f/documents/201701_cfpb_OA-Student-Loan-Snapshot.pdf. Note: Analysis is for Americans between the ages of 50 to 59.
[36] http://files.consumerfinance.gov/f/documents/201701_cfpb_OA-Student-Loan-Snapshot.pdf
[37] http://www.crs.gov/Reports/IF10426?source=search&guid=c644d06e1c314880a7afa79af5414099&index=3
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[39] *Ibid*.
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