EXPANDING ACCESS FOR RETIREMENT AND NECESSARY SAVINGS
AN EXECUTIVE SUMMARY

Delaware Office of the State Treasurer
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Summary

Saving for retirement is an increasingly difficult dilemma for American workers. Many states are exploring and creating "Secure Choice" programs to address this challenge. These programs amount to State-facilitated, universally available retirement savings mechanisms, providing a convenient way for all workers to save for retirement, particularly middle and low-income workers who lack access to employer-sponsored plans and small businesses that are unable to provide such a benefit. This report explores options and considerations for creating the Delaware EARNS (**E**xpanding **A**ccess for **R**etirement and **N**ecessary **S**avings) Program, a "Secure Choice" inspired program.

The Office of the State Treasurer and the AARP of Delaware have compiled preliminary research to review the feasibility and potential benefit of Delaware EARNS, a program designed to provide workers and employers access to low-cost retirement savings plans. The review focused on four key areas:

1. **Recent successes in secure choice models in other states**
2. **Behavioral Economics: Why Auto-IRA works**
3. **Closing the Gap: Examining the need for support within Delaware's workforce**
4. **EARNS: A Secure Choice plan Delawareans can trust**

Background: An Urgent Crisis

Recent research reveals a retirement crisis of growing concern. According to research from the National Institute on Retirement Security, 75% of residents agree that America is facing a retirement crisis, with more than half of respondents concerned they won't be financially prepared for retirement.[1] The Center for Retirement Research of Boston College issued a policy brief in January 2018, which indicated that nearly half of all U.S. working age households will be unable to sustain their standard of living in retirement.[2]

The Georgetown University Center for Retirement Initiatives recently found that an estimated 57 million private sector American workers have no access to a retirement program through their employers[3], however according to research from the AARP when a savings program is available at work, employees are 15 times more likely to save.[4] Challenges remain even for individuals with access to an employer-sponsored plan, as these plans may lack "portability," features which facilitate an easy transfer or allow for continued portfolio management when an employee changes jobs.

[1] Diane Oakley and Kelly Kenneally, " Retirement Insecurity 2019: Americans' View of the Retirement Crisis" March 2019 https://www.nirsonline.org/wp-content/uploads/2019/02/OpinionResearch_final-1.pdf

[2] Alicia H. Munnell, Wenliang Hou, and Geoffrey T. Sanzenbacher, "National Retirement Risk Index Shows Modest Improvement in 2016", Center for Retirement Research, Boston College, January 2018.

[3] Antonelli (2020), "What are the Potential Benefits of Universal Access to Retirement Savings?" Georgetown University Center for Retirement Initiatives in conjunction with Econsult Solutions, Inc.

[4] AARP "Work and Save 101" 2014.

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Furthermore, the retirement crisis isn't one that we have decades to solve. While younger generations are on a path towards crisis by missing out on savings opportunities during their prime earnings years, seniors are confronted by challenges today. The number of senior households is growing as life expectancies increase. Many of these individuals are expected to exhaust what little savings they have built through traditional retirement methods and will confront certain poverty without a financial backstop in place.

Since the Great Recession, U.S. households have made only modest wage gains among mid- to low-income earners and these households are expected to see their savings hit the hardest during the next recession.[5] Research also points to a growing divide between the country's highest and lowest earners.[6] As this gap continues to grow so will the retirement savings gap. COVID has only exacerbated this problem, especially among low to modest income individuals.

Secure Choice: An Emerging Solution

The retirement savings gap has many states working to reverse this trend. Over 45 states have introduced legislation, including 20 in 2020 alone, to explore the creation of publicly offered retirement savings programs, also referred to as Secure Choice programs. Since 2012, twelve states have established their own publicly offered retirement programs. Delaware is one of just five states to not have taken any legislative action to explore the feasibility of or establish such a program.

These elements make Secure Choice a fitting introduction for first-time savers – and their employers who may still be considering a more formal private retirement plan offering.

Secure Choice programs are distinctly different from more traditional retirement plans such as 401(k)s and pensions. Secure Choice relies on Roth IRAs as the savings vehicle, which means employers are expressly prohibited from contributing to employee accounts in any way, including matching, as they would in conventional retirement plans. As IRAs, participant accounts have lower annual contribution limits, currently $6,000 for individuals under 50.

[5] Michael McCormack and Amanda Novello "The True State of the U.S. Economy" November 2019. https://tcf.org/content/report/true-state-u-s-economy/?session=1
[6] Ibid

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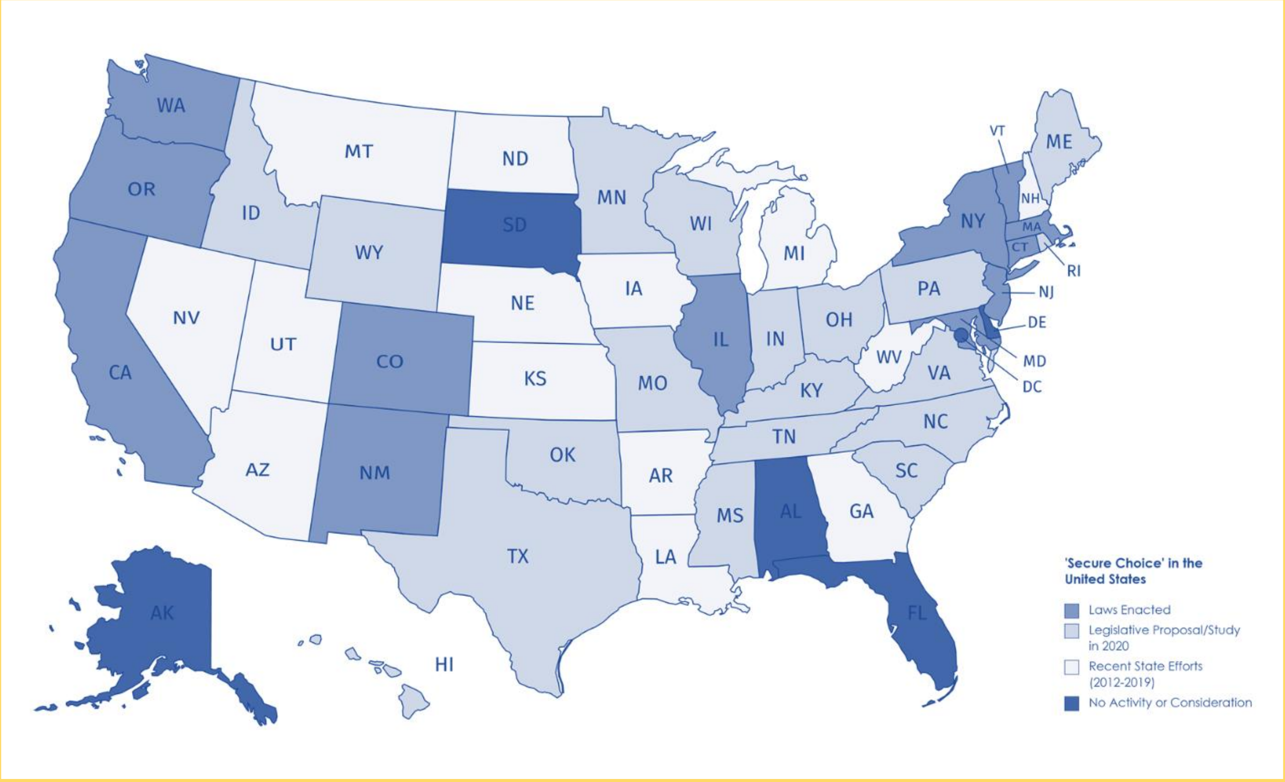
Recent Successes in Secure Choice Models in other States

Currently, there are twelve states and one major U.S. city that offer some form of public retirement plan option for retirement savings, and more have studied or proposed legislation. In all concepts goals typically center around a desire to increase retirement savings among populations that have not traditionally saved. One concept has emerged as the most popular among early adopters – Auto-IRA.



Secure Choice in the United States

Under the Auto-IRA concept, the State contracts with private sector providers to manage a state-facilitated retirement program and its corresponding assets. Contributions are deducted directly from an employee's paycheck and deposited into an IRA, over which the employee has full ownership and control. The administrator provides a simplified lineup of investments for individuals to choose from, similar in structure and diversification as the options made available to 401k participants. Should the employee change jobs or move, they have the option to remain in the plan, or rollover their assets into a 401k or other permissible rollover instrument. Of the five launched state-facilitated retirement programs, three have adopted the Auto-IRA model. The attraction to this model, from both an administrative and employer perspective, is that an Auto-IRA is relatively simple to launch and manage. From the employer perspective, there are no IRS filing requirements, nor the responsibility to serve as the fiduciary.

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Oregon was the first in the country to get its Secure Choice program, called 'OregonSaves' fully launched and implemented. The plan offers participants a simple, portable, low cost way to save. Under the program, the State Treasurer's office oversees and manages an Auto-IRA for businesses of all sizes that do not offer an employer-sponsored retirement plan, with a focus on providing a simple facilitation process for employers aided by a team of client service professionals. By the close of 2020, and just three-years after launching, Oregon registered over 16,000 employers, with close to 90,000 total funded accounts and over $80,000,000 in assets under management.

Colorado is the most recent state to adopt an Auto-IRA program for its constituents. In July of 2020, amid the backdrop of COVID-19, the Colorado Governor signed legislation to create the Secure Savings Program and Colorado Secure Savings Plan Board that would implement and launch a program. According to a study performed by the Colorado Board, 'failing to take action to increase access to retirement savings would result in the State facing a combined budget and revenue impact of almost $10 billion between 2021 and 2035. The state could save almost $9 billion over the fifteen-year period if retirees have sufficient savings.'[7] While just beginning its implementation phase, Colorado recognized that COVID-19 exacerbated the barriers towards financial empowerment and retirement readiness and that its citizens would be well-served by a state-facilitated retirement savings program. Other states or cities that have elected to use the Auto-IRA model include California, Illinois, Connecticut, Maryland, New Jersey, and Seattle.

Behavioral Economics: Why Auto-IRA Works

Saving for retirement is universally accepted as beneficial and yet for countless reasons, many individuals do not to do so. In many instances, the decision not to save is not made from choice but financial necessity. However, there are many for whom the decision not to save is driven by innate behavioral biases and preferences, as well as a lack of information.

The field of behavioral economics examines these biases and proposes simple low or no-cost solutions to overcoming them in the form of "nudges." Richard Thaler, a pioneer in the field

[7] https://treasury.colorado.gov/press-release/release-colorado-secure-savings-program-board-appointed

of behavioral economics defines nudges as *"any aspect of the choice architecture that alters people's behavior in a predictable way without forbidding any options or significantly changing their economic incentives. To count as a mere nudge, the intervention must be easy and cheap to avoid."8*

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The incorporation of nudges into retirement and savings program designs has proven to be a very simple and efficient way to boost participation and savings rates. Popular retirement nudges are auto-enrollment into retirement programs (also known as "opt-out" model) and auto-escalation of contribution rates, both of which have been incorporated into existing Secure Choice programs. According to Vanguard, plans that use auto-enrollment have a 92% participant rate compared to 61% for plans with just a voluntary rate.[9]

To address the challenge of choice and complexity surrounding retirement investment, research has indicated that offering retirement plan participants simplified investment choices can further enhance outcomes.[10] California and Oregon have both incorporated these three design elements into their successful Secure Choice program models.

Closing the Gap: Supporting Delaware's Workforce

Secure Choice programs are generally designed to serve small businesses who are unable to offer retirement plans to their employees due to the cost and administrative burden. In Delaware, there are a total of 25,316 non-farm, private business locations ("establishments") as of 2016.[11] Using information from the National Compensation and Benefits Survey, it is estimated that nearly 54% of these establishments (13,653) do not offer any form of retirement benefit, which translates to more than 200,000 Delaware employees lacking access to an employer-sponsored retirement plan option.

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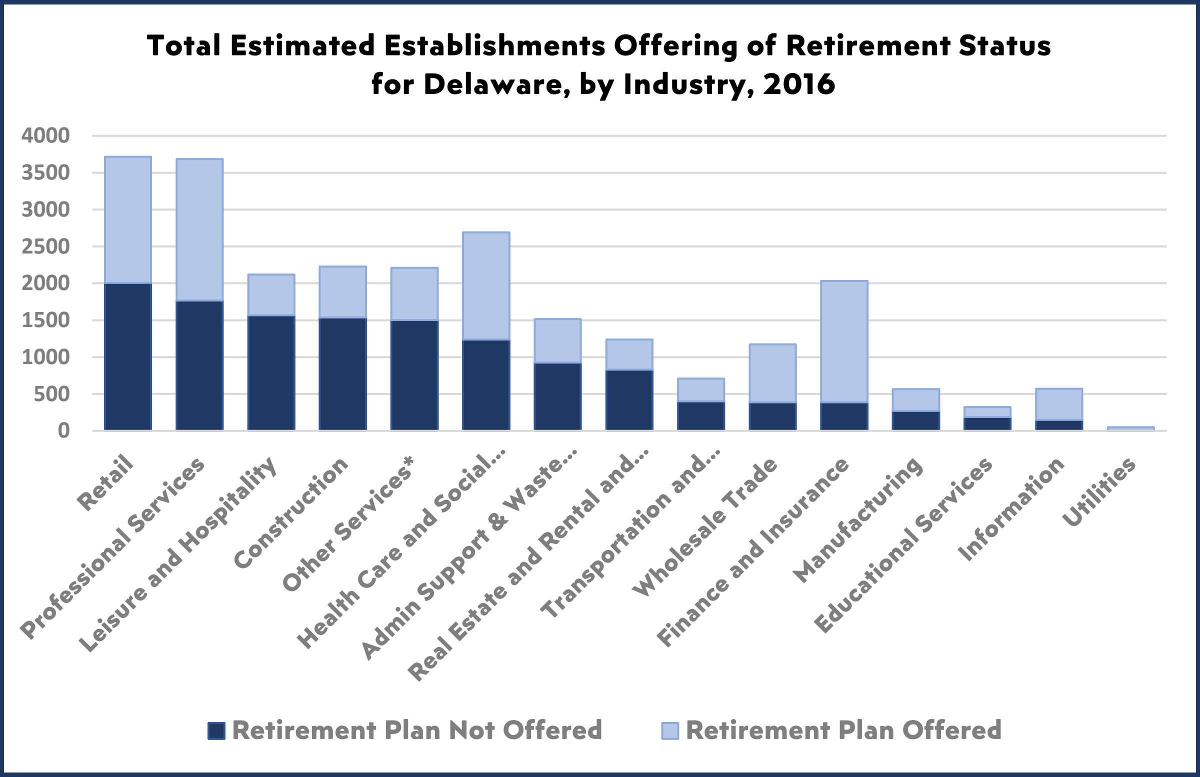
[8] Thaler, R. H., & Sunstein, C. (2008). *Nudge: Improving decisions about health, wealth, and happiness.* New Haven, CT: Yale University Press.

[9] https://static.vgcontent.info/crp/intl/avw/mexico/documents/how-america-saves-insights.pdf

[10] The Pew Charitable Trusts "How States Are Working to Address The Retirement Savings Challenge" 2016 https://www.pewtrusts.org/en/research-and-analysis/reports/2016/06/how-states-are-working-to-address-the-retirement-savings-challenge

[11] Census, "Delaware County Business Patterns, 2016 County Business Patterns,"



Source: BLS, Census[12]

There are documented wealth gaps established in Delaware, disproportionately impacting women, and people of color. In a recent report from Prosperity Now, the data shows that in the city of Wilmington, the median income for African American and Latino households is roughly half that of White households (White $60,772, African American $30,034, Latino $32,976)[13]. The same report shows that 14.2% of African American households in Delaware live in poverty, nearly three times the rate of White households. Demonstrated by a 2019 Federal Reserve's Survey of Consumer Finance revealed that among working-age families that have retirement account balances, the typical black family has two and half times less saved than their white counterparts.[14]

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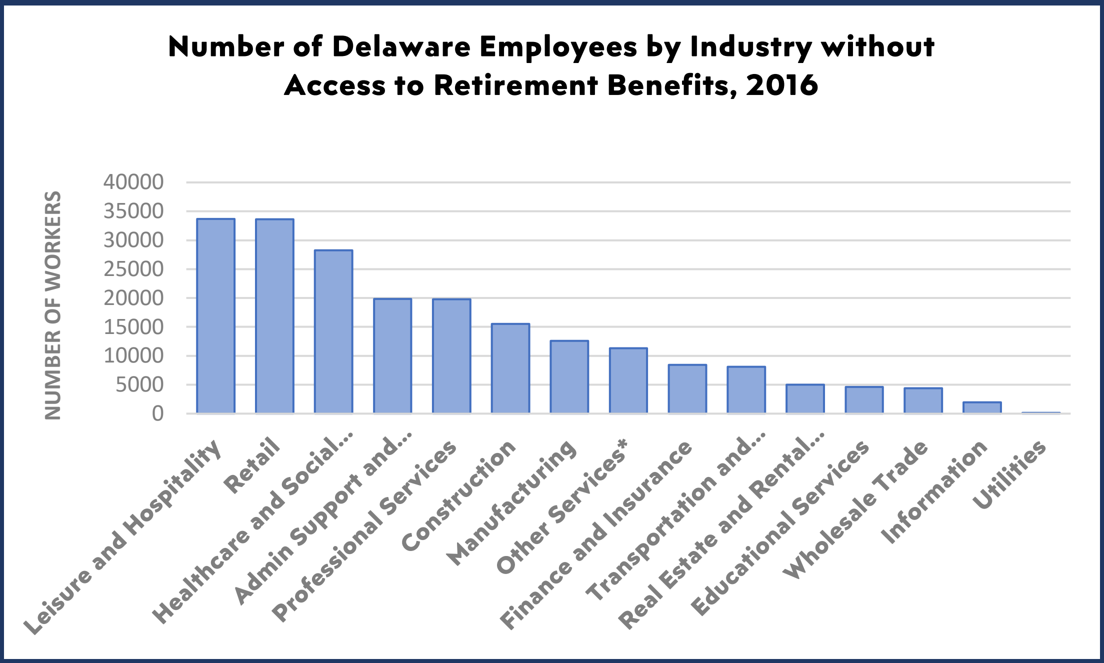
[12] "Other Services" generally includes equipment and machinery repairing, promoting or administering religious activities, grantmaking, advocacy, and providing dry cleaning and laundry services, personal care services, death care services, pet care services, photofinishing services, temporary parking services, and dating services. https://www.bls.gov/iag/

[13] Prosperity Now "Racial Wealth Divide in Wilmington" March 2019 https://prosperitynow.org/resources/racial-wealth-divide-wilmington

[14] Bhutta, Neil, Andrew C. Chang, Lisa J. Dettling, and Joanne W. Hsu (2020). "Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances," FEDS Notes. Washington: Board of Governors of the Federal Reserve System, September 28, 2020, https://doi.org/10.17016/2380-7172.2797

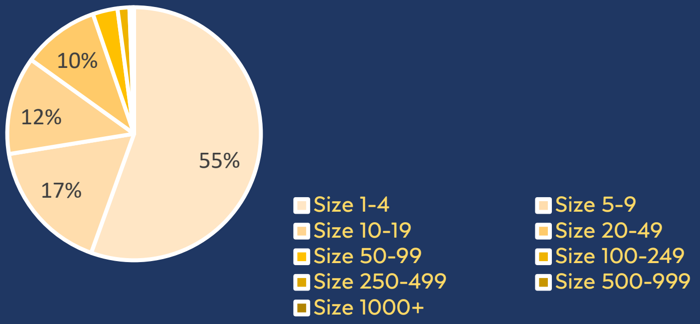


Source: BLS, Census

Introducing a state-facilitated benefit plan in Delaware could alleviate barriers small employers face in offering options and keep Delaware competitive with its regional neighbors when attracting talented workers to the region.

Those most impacted by these changes will range from food service personnel to office administrative personnel across varying industries. Given the limited household income of these professions, it will be incumbent in early adoption to consider the cost of living prior to enaction.

Share of Delaware Establishments Estimated to Not Offer Retirement Benefits, by Number of Employees, 2016



Source: BLS, Census

Share of Delaware Employees by Establishment Size that are Impacted by Lack of Access to Retirement Benefits, 2016

Source: BLS, Census

A state-sponsored savings plan, funded by employees, empowered by employers, and overseen by the State, could offer a solution to the quickly emerging crises stemming from generations of workers without adequate savings.

EARNS: A Plan Delawareans Can Trust

The Office of the State Treasurer has been studying Secure Choice programs for over a year—before the COVID-19 crisis and throughout. Having met with many industry experts, peer states, and stakeholders across Delaware, the Office of the State Treasurer is proposing the establishment of the Delaware Expanding Access for Retirement and Necessary Savings program ("EARNS"), a Secure Choice program, tailored to meet the needs of hardworking Delawareans at every socio-economic level. Delaware EARNS is a public-private partnership, designed to be collaborative and inclusive of the needs of businesses and employees alike.

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Under this proposal, the Office of the State Treasurer envisions a collaborative and complementary relationship with the existing wealth management industry in Delaware, currently offering private retirement plans for businesses. One prominent feature guaranteed under this proposal would offer support and educational resources to businesses ready to progress from EARNS and into a more robust retirement plan offering.

Additional highlights of the proposed Delaware EARNS program include—

- ✓ ***Only for Businesses Without a Plan:*** Eligible employers who are already or intending to offer their employees some other form of defined benefit or defined contribution retirement option for employees would not be required to participate

- ✓ ***A Phased in Approach for Business Participation:*** Businesses with more than five employees will be required to participate in Delaware EARNS. The initial deadline for employer participation in Delaware EARNS would be phased according to the size of the employer — employers with the smallest number of employees would have the most time to establish participation

- ✓ ***Resources for Growing Businesses:*** The program will provide informational resources for employers looking to transition out of the publicly offered plan by establishing their own privately-sponsored plan

- ✓ ***Auto-Enrollment:*** Employees will be automatically enrolled into Delaware EARNS, unless they elect to opt-out. The option to opt-out may be exercised at any time and there are no penalties for doing so. An employee who has opted out may elect to re-enroll at a later date

- ✓ ***Auto-Escalation:*** The default contribution rate would begin at 3% and automatically escalate annually 1 to 2% every year, until a 15% contribution rate is achieved. Employees have the freedom to change their contribution rate at any time, to any amount

- ✓ ***Simplified Investment Line-up:*** The program will endeavor to keep the investment options simple and easy for participants to understand

- ✓ ***Portability:*** Participants benefit from being able to take their accounts with them when they switch jobs. Participants may also continue contributing to their accounts when they are self-employed or not otherwise working for an eligible employer. Savers are also able to rollover their accounts into privately sponsored retirement plans

- ✓ ***Promote and Create a Culture of Personal Savings:*** The program will promote awareness through financial literacy education on of the benefits of all forms of personal savings, including emergency savings funds and savings for major expenses associated with life events

Delaware EARNS would be supported by an independent board tasked with overseeing all administrative aspects of the program including but not limited to marketing and promotional responsibility, vendor management, and investment oversight.

Other Board responsibilities shall include—

- **Investment and Contribution Oversight:** The board would select age-based investment options for participants as well as a simplified menu of alternative investment options. The board will also be tasked with establishing default investment options and contribution rates for participants
- **Vendor Selection:** The board would be responsible for procuring and managing relationships with a third-party program administrator, investment managers, private financial institutions, other financial and service providers, consultants, actuaries, counsel, auditors, and other professionals when necessary
- **Strategic Partnerships:** The board may seek to form or join consortiums or alliances for the purpose creating economies of scale and generating cost savings
- **Trust Oversight:** The board shall establish a program trust for the purpose of protecting participant contributions. Each participant fully owns their contributions to and earnings on their program account. Neither the State nor any employer shall have any proprietary interest in the participant's account

Proposed Governance Model