No. 2 in a series of 5

Issue Brief

Retirement Security Challenges: Portability and Retirement Income

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Key Points

- Today's mobile workforce faces challenges in keeping track of retirement savings accumulated from different employers and converting those savings into sustainable retirement income.
- Potential solutions include the creation of a centralized registry for benefits, providing periodic benefit statements, and offering basic education on retirement-related topics at different career stages to help demystify the retirement planning process.
- Secure retirement income can be facilitated by easy access to low-cost investments offering an opportunity for growth while managing risk, and making available at retirement a variety of easy-to-initiate, institutionally priced income options.

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Introduction

In July 2019, the American Academy of Actuaries published an issue brief titled *National Retirement Policy & Principles*. The focus of the paper was the increasing need for the establishment of a comprehensive national retirement policy based on several guiding principles. The Academy's Pension Practice Council plans to issue a series of additional issue briefs to expand the discussion to specific retirement issues that could be addressed in further detail by the national policies and guiding principles.

This initial brief specifically addresses the difficulty that workers in a mobile workforce face as they accumulate retirement benefits at multiple employers over their careers. Two specific risks addressed are 1) the potential for losing track of benefits and 2) the challenge of converting benefits into sustainable retirement income. The elements of a national retirement policy that would be impacted by these risks are: Availability, Adequacy, Allocation of Risks, Cost, and Portability and Leakage (for further discussion of these specific elements of a national retirement policy, see the *National Retirement Policy & Principles* issue brief). These risks are explored in greater detail below, along with ideas as to how they may be mitigated.

Background

Much has changed over the past several decades in how Americans achieve retirement security. In the private sector, the prevalence of the defined benefit (DB) plan as part of employers' ongoing retirement programs has dwindled, while employer-sponsored defined contribution (DC) arrangements have become more prominent. In addition, individual account arrangements and options for investment and retirement income products and solutions have grown. At the same time, life expectancies have increased, and the likelihood of spending one's working lifetime in the service of a single employer has declined.

Many employees of larger employers have access to retirement plans that provide opportunities for retirement planning education, transfer of funds from prior employers' plans, and projections of potential retirement income that the participant account may provide. Some employees may also have access to income options payable from the plan at retirement. With the passage of the Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 discussed in the Appendix, DC plans will be required to provide participants with estimates of the lifetime income their account balance could provide, and the prevalence of lifetime income options in DC plans may increase.

However, not all employees have taken advantage of these services, and many other individuals have not had continuous access to these types of plans through their working careers. It is very common for individuals to have many different jobs during their working years. Individuals may lose track of where the benefits they accumulate over a career reside and may not currently control how those funds are invested, managed, and/or distributed. In addition, they could benefit from access to basic education and cost-efficient, unbiased advice on conversion of their retirement savings into retirement income, as well as access to low-cost investments. Stakeholders have observed that workers would benefit by simplifying the process for transferring funds between retirement vehicles when they change jobs. On occasion, funds that had been set aside for retirement are withdrawn and used prior to retirement. An estimation of these funds

Members of the Retirement System Assessment and Policy Committee, which authored this issue brief, include Eric Keener, MAAA, FSA, FCA, EA—*Chairperson*; Kelly Coffing, MAAA, FSA, EA; David Driscoll, MAAA, FSA, FCA, EA; Lee Gold, MAAA, ASA, EA; Scott Hittner, MAAA, FSA, FCA, EA; Cynthia Levering, MAAA, ASA; Andrea Sellars, MAAA, FSA; Mark Shemtob, MAAA, FSA, FCA, EA; and Claire Wolkoff, MAAA, FSA.

withdrawn could be as much as 2.9% of assets per year based upon tax data.[1] A portion of this leakage occurs when individuals change jobs. More seamless portability to a tax-deferred retirement vehicle could help to lower this leakage rate.

Workers could benefit from easier access to tools and services needed to assist in managing the retirement security challenges they face. Recently, the Department of Labor (DOL) granted approval to an "auto-portability" program to help facilitate the transfer of individuals' small balances earned in prior employers' plans into new employers' plans. However, there continues to be a need for additional and broader services and tools. This issue brief provides an overview of several types of services and tools that could be helpful.

Reasons for Policy Changes to Encourage New Solutions

There are several reasons why the above enhancement in services and tools in our retirement system may be attractive to workers, and why policy changes to encourage those solutions should be considered. Applicable elements of a national retirement policy are highlighted in italics below.

A. **Decline in prevalence of DB plans** (*Availability, Allocation of Risks*): The traditional DB plan providing guaranteed lifetime income has become less prevalent for private-sector employees. According to data from the Employee Benefit Research Institute (EBRI), only 11% of private-sector U.S. workers were covered by a DB plan in 2017.[2] As a result, most employees are assuming the majority of both longevity- and investment-related risks.[3] This is a challenge for many individuals, especially those who lack basic financial literacy and are unable to obtain sufficient financial education and unbiased advice.

B. **Multiple jobs throughout an individual's working lifetime** (*Availability, Portability and Leakage*): The Bureau of Labor Statistics' news release dated Aug. 22, 2019, noted, "Individuals born in the latter years of the baby boom (1957–64) held an average of 12.3 jobs from ages 18 to 52."[4] Many will also have periods when they will be self-employed. Retirement savings through these different employment periods are often spread across a variety of institutions with no coordination among the various plans or accounts. In

1 *Why Are 401(k)/IRA Balances Substantially Below Potential?*; Center for Retirement Research at Boston College; November 2019.
2 "*Tracking the Shift in Private-Sector, Employment-Based Retirement Plan Participation From Defined Benefit to Defined Contribution Plans, 1979–2017*"; EBRI; June 6, 2019.
3 Social Security being an exception for nearly all retirees.
4 "*Number of Jobs, Labor Market Experience, and Earnings Growth: Results from A National Longitudinal Survey*"; Bureau of Labor Statistics economic news release; Aug. 22, 2019.

addition, funds accumulated for retirement may be spent prior to retirement. There is a need to enable individuals to more easily centralize their holdings, either in a single place or through a portal that keeps track of all retirement funds, to facilitate the coordination of investment and decumulation decisions.

C. **Challenges in accessing lifetime income options under employer retirement plans** (*Availability, Cost*): Over the past decade, there has been increasing interest in encouraging employers to provide employees with financial education and advice, as well as to offer alternative retirement income strategies and options for benefits to be paid by employer-based plans. However, the number of employers offering lifetime income solutions within qualified DC plans remains relatively low due to a number of factors, including cost, complexity, and perceived fiduciary liability. This is especially true among smaller employers.[5] If retirees cannot get access through their employers, where can they turn?

D. **Lack of access to low-cost, unbiased advice** (*Availability, Cost*): Individuals without meaningful levels of retirement savings may be unable to obtain quality, unbiased financial advice at a reasonable cost upon retirement. In addition, those who do obtain advice may not be provided with a broad enough array of options or in some cases may even be subject to large per-account fees and what may be considered elder abuse.

Improvements in these areas could help close the gap between retirement income needs and resources, positively impacting the element of *Adequacy*. Greater efficiencies in the accumulation phase can lead to larger accumulations, and greater efficiency in converting accumulations to lifetime income can lead to higher and more stable income.

Description of Desirable Services and Tools

One key objective would be to facilitate workers' ability to track and manage retirement savings they have accumulated from multiple sources, such as qualified retirement plans (e.g., 401(k) plans) offered by prior employers or individual tax-advantaged savings (e.g., Individual Retirement Accounts, or IRAs). There are currently challenges associated with direct transfers between qualified plans, which create the potential for leakage (for additional detail on these challenges, see the 2016 report of the ERISA Advisory Council mentioned in the Appendix). Even if leakage doesn't occur, it often results in workers' savings being spread across multiple institutions and vehicles with a lack of coordination among their investments. The ability to easily consolidate or manage such savings could

5 This could change with the recent passage of the SECURE Act, described in the Appendix.

reduce the likelihood that there will be workers who will lose track of their savings or use it for non-retirement purposes. Consolidation would also provide an opportunity for greater efficiency in areas such as recordkeeping and investment management.

A secondary goal should be to provide assistance to retirees in converting retirement savings into stable retirement income. There are a variety of approaches to convert retirement savings into retirement income, each with pros and cons. Unfortunately, there are retirees who may not be aware of the options they may have.

Specific services and tools that could address these issues include:

- Facilitating transfers and rollovers between IRAs and qualified retirement plans with the goal of having all retirement savings either under one "roof" or, if spread out, easy to track and manage.
- Offering a centralized registry for all qualified retirement funds associated with a given Social Security Number. Such a registry would allow for an easy process for locating "forgotten" IRA and qualified plan accounts.[6]
- Facilitating on a default basis (when other options are not elected) investments in low-cost passive funds (similar to those offered by the Federal Government Thrift Savings Plan), including target date funds, which offer an opportunity for growth while managing risk.
- Providing periodic statements and basic education on retirement-related issues that would help demystify the retirement planning process during both the accumulation and decumulation phases. Statements could include projections of potential retirement income available from workers' savings, such as those required by the SECURE Act for qualified DC plans.

Offering unbiased and reasonably priced personalized retirement income advice.

Upon retirement, making available a variety of easy-to-initiate, institutionally priced lifetime income options that include managed payout funds, structured withdrawals from investment accounts, insured annuities (both immediate and deferred), and life insurance company variable annuities with guaranteed minimum benefits.

6 Participants of DB or DC retirement plans who terminate with vested benefits left in the plan are "reminded" of benefits from prior plans by a notification from the Social Security Administration when applying for benefits. Plan sponsors provide the information as part of the annual IRS Form 8955-SSA reporting. However, this notification comes at retirement age, while most workers should address their retirement savings much earlier than this.

Considerations for Policymakers

It is easy to articulate in a general manner the types of tools and services as outlined above that could help enhance retirement security for workers and retirees. It is more challenging to determine how to make them a reality. An argument can be made that the services and tools can be implemented currently without any further legislation or regulation. This may be true. However, the services and tools can often be complicated and beyond the reach of many workers and retirees —and those workers and retirees are the ones who are most vulnerable to being unable to secure a dignified retirement.

Another argument may be made that the employer plan is the best place to provide these tools and services. However, most of these services are not required by law, and many employers do not wish to take on the additional responsibility voluntarily. In addition, many workers are self-employed or work for employers without retirement plans. Where do they get the help they need? The employer plan is not the answer for everyone, even with government mandates.

The DOL, Securities and Exchange Commission (SEC), Consumer Financial Projection Bureau (CFPB), Pension Benefit Guaranty Corporation (PBGC), and other regulatory organizations have mandates to support the retirement system. It may be prudent to investigate whether they can help facilitate some of these services without hampering what works well in the private sector.

Conclusion

The improvements suggested in this issue brief could help close the gap between retirement income needs and resources. There have been recent efforts in a number of related areas (see the Appendix for more detail), but more can be done. A portion of the workforce (especially those who are more mobile in their jobs) is vulnerable to being unprepared for retirement. This paper does not propose a specific solution but proposes that system stakeholders consider regulation and legislation that could help advance the goal of enabling American workers to accumulate and enjoy dignified retirements.

Appendix —Related Efforts and Issues

Below is a summary of some related topics and current initiatives that are underway that address elements of the subject of this issue brief:

A. The Retirement Clearinghouse: As mentioned earlier in this issue brief, a recent DOL advisory letter addresses a request for "auto-portability" between retirement plans.

B. 2016 ERISA Advisory Council Report: The challenges to efficient portability are highlighted in this report.

C. Thrift Savings Plan: Millions of Americans who work for the federal government have access to a retirement plan that encompasses many of the features outlined above with respect to investments and decumulation options.

D. DOL Safe Harbor IRAs: In 2004, the department published a safe harbor regulation, at 29 C.F.R. § 2550.404a-2, allowing mandatory IRA rollover distributions of amounts of $5,000 or less for terminated participants. These auto-IRAs must be invested in a product that meets the requirements for preservation of principal and provide a reasonable rate of return, the fees and expenses must not exceed those charged by the provider for a comparable, non-automatic rollover IRA, and the participant must have the right to enforce the contractual terms of the IRA. The summary plan description must describe the plan's automatic rollover provisions.

E. Recent legislation and legislative proposals: The Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act), which was enacted as part of the 2019 year-end budget legislation, aims to increase access to tax-advantaged accounts and prevent older Americans from outliving their assets. Other legislative proposals such as The Retirement Enhancement and Savings Act (RESA) would also provide enhanced portability.

F. PBGC's Expanded Missing Participant Program: This program allows plan sponsors to transfer accounts for missing participants from terminated DC plans to the PBGC for retention and investment. Accounts are free from fees, held in perpetuity, and retain ERISA rights and protections. There has been some discussion of extending the program to other voluntary transfers, though there is currently no statutory authority to do so.

G. Auto-Portability Proposals—EBRI Research: *The Impact of Auto Portability on Preserving Retirement Savings Currently Lost to 401(k) Cashout Leakage* examines the possibility of automatically taking participants' accounts from former employers' retirement plans and combining them with their active accounts in new employers' plans with the intention of keeping the DC assets in the retirement system and—in theory—reducing leakage from cash-outs upon employment termination.

In July 2019, the American Academy of Actuaries Retirement System Assessment and Policy Committee published an issue brief titled *National Retirement Policy & Principles*, which discussed the increasing need for a comprehensive national retirement policy based on certain guiding principles. This initial issue brief has been followed up by four additional papers in the series:

- *Retirement Security Challenges: Portability and Retirement Income* (April 2020)
- *New Retirement Plan Designs: Degrees of Risk Sharing* (October 2021)
- *Retirement Policy: Potential for Changing Roles of Employers in Retirement Programs* (October 2021)
- *Retirement Policy: Aligning Plan Design With Effective Employee Engagement* (March 2022)

Taken together, these issue briefs lay out guiding principles that policymakers can look to as they consider the establishment of a comprehensive national retirement policy.