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Building Effective Retirement Savings Programs for Uncovered Workers: Lessons from the UK Experience

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Imagine workers with access to retirement savings programs that will help provide a secure retirement income at affordable contribution rates. Imagine those contributions managed at low-cost with a long-term, wealth creation focus that will help those workers manage their savings to last their lifetime. If we could achieve that vision, we would provide for a more sustainable retirement system supplementing Social Security for millions of Americans. In doing so, we also can create a stronger retirement income system for American individuals and families, less vulnerable to future financial bubbles and crises similar to what we experienced during the past decade.

STATES AND THE LOOMING RETIREMENT SAVINGS CHALLENGE

The majority of private sector workers in the United States do not participate in a workplace retirement savings program today. A growing body of studies suggests that, as a result, a significant proportion of these workers and their families face the prospect of material declines in living standards in their post-work years in the coming decades. These projections have raised a profound public policy question. What, if anything, can and should government do about this looming challenge? There is a growing consensus that doing nothing is no longer a defensible option. But what to do?

In the United States, at least 30 states have taken, or are contemplating taking, some kind of action on private sector retirement security. For example, California was among the first to pass legislation in 2012 to establish a mandatory state-sponsored payroll deduction IRA for employees who currently lack coverage through their workplace and Illinois and Oregon followed with similar programs in 2015. Washington and New Jersey passed voluntary marketplace models to make available via a website access to low cost, simple retirement savings plan options.

While this momentum is impressive, the greater challenge for a state is to successfully make its program operational. Creating an expert, cost-effective retirement savings program is a significant undertaking. The states would do well to look to the experiences of some other nations and some lessons learned that can be helpful to make sure state efforts move from well-intentioned ideas to successful implementation.

THE UK NEST PROGRAM

In 2003, the United Kingdom (UK) government established an independent Pensions Commission, chaired by Lord Turner, charged with considering the case for the introduction of Australian-style compulsory retirement saving. It produced its first report – a comprehensive analysis of the likely future state of the UK retirement system – in 2004, with a follow-up containing policy recommendations in 2005. The Commission's key finding was that up to 9 million UK workers were under-saving for retirement. If the UK was to avoid a precipitous decline in retirement incomes in the future it faced some unavoidable choices: higher taxes to pay for more generous national pensions; increased private pension saving to deliver higher private pension incomes; longer and later working lives and later entitlement to national benefits; or some combination thereof.

To deliver on the second of these the Commission recommended a new program that relied on the automatic enrollment of employees either into a new national savings program or into existing company retirement savings plans, but with the right to opt out, and with a requirement for employers to make matching contributions. In 2007, the UK government established an agency with an independent Board of Directors to "provide expert advice to the Government to develop the practical implementation of the new pension policy." In 2010 this agency morphed into the National Employment Savings Trust (NEST) Corporation – the body responsible for operating the NEST pension plan on an ongoing basis. UK legislation requiring employers to enroll their employees with certain minimum features went into effect in 2012. Under that legislation, NEST began enrolling workers from 2011 on a beta-test basis and had workers from 100 different employers participating in the plan by the end of March 2012.

NEST has auto-enrolled some 2.8 million UK uncovered workers, and has some £725 million under management. Under the same legislation, several million more have been auto-enrolled into other qualifying plans offered by commercial providers chosen by the employers of these workers. Around 8 percent of those workers enrolled into NEST exercised their option to dis-enroll themselves, with similar numbers experienced in other plans. Perhaps not surprisingly, most were workers close to retirement. Looking ahead, NEST will auto-enroll millions of additional UK workers over the course of the next few years. On the financial side, the program startup was made possible by a multi-year loan agreement provided by the UK Government. On the revenue side, NEST is charging its participants a 0.3 percent per annum management fee on assets under management, as well as a 1.8 percent one-off charge on contributions to recover the start-up costs. Together, the two charges are, for the average member, equivalent to about 0.5 percent of assets per year.

LESSONS FOR THE STATES

The unfolding UK pension reform story provides the state governments in the U.S. with critically important insights in how they should proceed down the retirement savings reform path from here. For example:

- Are they prepared to embrace basic design features, such as expanded coverage, employer participation, default contribution levels, a strong governance structure, transparency and citizen engagement, lifetime income options, consumer protections, portability and ensuring the program supplements and not supplants already existing retirement programs? A well designed program will have features that combine the best elements of traditional DC and DB plans (e.g., a target pension, clear property rights, no intergenerational wealth shifting, lifetime income, opt-out option).

- Will they require employers not already offering a qualifying retirement savings program to enroll their employees in a qualifying arrangement? In the UK, any eligible employee who was not already in a qualifying plan *had to* be enrolled, either to the employer's existing plan or to a new one.

- Are they prepared to invest the resources – both money and talent –in a Board or Task Force to design and create effective implementation strategies that would finalize the design of and administer a state retirement savings program? The Personal Accounts Delivery Authority – PADA – which was the forerunner to NEST advised government on design and implementation and was then responsible for the initial procurement and build of the NEST system. PADA was set up as an agency of Government but staffed with people from commercial, financial services, investment and IT backgrounds and with considerable operating freedom.

- Will they find acceptable ways for commercial vendors to participate in these newly created markets for retirement savings? The UK experience suggests a prominent role can be found both for existing providers alongside any state-sponsored plan, and within the delivery of the state plan itself through the use of outsourcing.

If the answer to these questions is yes, there are three success drivers that should be kept in mind: first, a viable, explainable vision to address the retirement coverage gap; second, the political will to see it through; and third, a properly resourced, effectively led effort to implement it.

In this context, the NEST story is instructive for three reasons:

1. **It Confirms Three Success Drivers:** The Turner Commission defined the problem and a solution for fixing it. The UK Government committed to transforming the "on paper" solution into an actual solution, and the UK Government created a properly resourced, effectively led effort that successfully managed the transformation.

2. **Getting It Right Takes a Long Time:** The Turner recommendations were accepted by the UK Government in 2006 and NEST became operational in 2011. The last employers to fall under the legal duty to enroll their workers will not do so until 2018.

3. **Good Governance Is Key**: The NEST organization continues to demonstrate that a collective mix of skill, experience, and "greater good" mindsets has been essential to overcoming the many landmines and roadblocks the organization has experienced on the road to turning vision into reality. NEST's board was given significant flexibility over key areas of plan design such as the investment strategy and fund choices for participants, design of the key business processes and user interfaces, and overall approach to communication with members. NEST's corporate culture reflects this level of independence and as a Trustee, the focus of the organization is to work in the interests of participants.

So are efforts to close the coverage gap among private sector workers a good idea or a pipe dream? In the end, it all depends on the power and clarity of the political vision, and on the will and the resources required to successfully implement it. The UK NEST program offers some reason for optimism.

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