

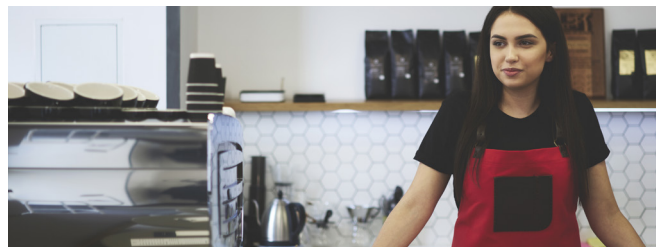
December 1, 2020



# Retirement Security in North Carolina

## Findings and Recommendations

Report to the General Assembly of North Carolina by the Joint  
Legislative Study Committee on Small Business Retirement Options  
Pursuant to NC Session Law 2019-205



This Report is presented to the Speaker of the House of Representatives, the President Pro Tempore of the Senate, and the Fiscal Research Division by the Joint Legislative Study Committee:

President Pro Tempore of the Senate Appointments:

Sen. Jim Perry, Co-Chair

Sen. Sam Searcy

Mr. Robert Cooley (Public Member, Small Business Owner)

Mr. Brian Lewis (Public Member, Labor Advocate)

Speaker of the House of Representatives Appointments:

Rep. Bobby Hanig, Co-Chair

Rep. Becky Carney

Mrs. Lisa D. Riegel (Public Member, Representing Organization for Older Adults)

Hon. Paul N. Tine (Public Member, Representing Private Retirement Services Industry)

Ex-Officio Appointments:

Mr. Sam Watts, representing North Carolina State Treasurer Dale Folwell's Office

Mr. Ronald Penny, North Carolina Secretary of Revenue

As directed under NC Session Law 2019-205.

## EXECUTIVE SUMMARY

In recognition of the retirement savings crisis for small business employees, the North Carolina General Assembly established a Study Committee to explore options to address this savings opportunity gap. The Study Committee met multiple times in early 2020, hearing from experts in the field of retirement security and reviewing alternatives for North Carolina. The Study Committee was provided access to a range of data and analytical information on retirement security in the US and North Carolina, some of which is included here. This report summarizes the information that was presented to the Committee and the options that were considered. It also condenses the future work that is left to be done by a Task Force and Implementing Board as part of program development and implementation should the North Carolina General Assembly decide to proceed.



### Retirement Savings Gaps: Impact to North Carolinians

To carry out its responsibilities, the Committee learned the following:

- ◆ Approximately 53% of the state’s workforce does not have access to a retirement savings plan at work;<sup>1</sup>
  - Currently more than half of the state’s small employers do not offer retirement plans.
  - Many other workers are not covered by an employer’s plan because they work part time, are in an uncovered classification or are independent contractors.
- ◆ Without access to a retirement savings plan at work, most people simply will not save for retirement on their own. In fact, workers with access to a workplace retirement plan are 15 times more likely to save for retirement.<sup>2</sup>
- ◆ Because too many are not saving for retirement, North Carolina’s expenses will increase significantly as those who have not saved will require more social services. In fact, a 2016 study by the University of North Carolina Wilmington forecast a positive fiscal impact of approximately \$468 million to the state with modest increased savings rates of 3% to 5% by workers in low- to middle-income groups, which are over-represented in the uncovered population.<sup>3</sup>

### What Can North Carolina Do to Improve Worker and Taxpayer Outcomes?

If North Carolina is interested in adopting a retirement security approach that will significantly improve coverage of and use by the 1.7 million workers in the state who do not have access to a retirement plan at work, the state has several choices. Of the alternatives available, the simplest and most effective program would be a state-facilitated Auto IRA program using Individual Retirement Accounts, developed and operated in partnership with private sector partners for administration and investments. This model also has the greatest likelihood of helping the state achieve significant savings to rising costs for social services programs.

**We therefore recommend a state-facilitated Auto IRA program as the preferred model to help savers and to help the state achieve savings.**



**Approximately  
53% of the state’s  
workforce does not  
have access to a  
retirement savings  
plan at work.**

### Open Elements and Next Steps

A number of important elements remain open that require further consideration. These include:

- ◆ Development of a program design recommendation
  - Including elements identified in this report, and
  - Taking into account an analysis of North Carolina’s employer and workforce demographic information and key metrics
- ◆ Evaluation of the ability to partner with similar programs established in other jurisdictions
- ◆ Evaluation of the feasibility of establishing either a stand-alone or partnered program
- ◆ Establishment of a general fund loan or other funding source(s) for program startup and early operation — programs are designed to be cost-neutral to the state
- ◆ Determination of optimal oversight for any proposed program

### Recommendation

If the General Assembly proceeds with legislation to address the retirement savings crisis in North Carolina, the preferred model to help workers save and to help the state achieve fiscal savings is an Auto IRA program.

We recommend that if the General Assembly proceeds, the authorizing legislation should include the appointment of a Task Force to oversee the open elements identified above. At the completion of its work, the Task Force should be replaced by an Implementing Board that will be established by the Agency or Authority identified to oversee the program.

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<sup>1</sup> John, David, and Gary Koenig, Fact Sheet: North Carolina - *Workplace Retirement Plans Will Help Workers Build Economic Security*, AARP, August 2015.

<sup>2</sup> Employee Benefit Research Institute. 2006. Unpublished estimates of the 2004 Survey of Income and Program Participation Wave 7 Topical Module (2006 data). Data are for workers earning between \$30,000 and \$50,000.

<sup>3</sup> Galbraith, Craig S., *Fiscal Benefits of Increasing the Savings Rates of North Carolina’s Aging Population: Impact on State Expenditures for Retirees*, University of North Carolina Wilmington, December 31, 2016.

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# CONTENTS

<b>EXECUTIVE SUMMARY</b>	<b>ii</b>
<b>BACKGROUND: WHY RETIREMENT SECURITY IS SO IMPORTANT IN NORTH CAROLINA</b>	<b>1</b>
Introduction	1
Critical Challenge: Retirement Security in North Carolina	2
Fiscal Impact to North Carolina	5
<b>OPPORTUNITIES FOR NORTH CAROLINA</b>	<b>7</b>
Retirement Outcomes in North Carolina – Federal Models	7
Improving Outcomes in North Carolina – State Retirement Models	9
Auto IRA Programs (“Secure Choice”)	9
Multiple Employer Plans	10
Retirement Marketplaces	10
Results of State Models	11
Auto IRA Programs (“Secure Choice”)	11
Multiple Employer Plans	11
Retirement Marketplaces	11
Perspectives: Employers and Workers	12
Employer Perspectives: Impact on Businesses	12
Other Considerations	14
Part-Time, Contract or “Gig” Workers	14
Roth or Traditional IRA Accounts	14
Cost to Employees	14
<b>IMPROVING RETIREMENT SECURITY: RECOMMENDATIONS FOR NORTH CAROLINA</b>	<b>16</b>
Model and Approach	16
Open Elements – Task Force	16
Conclusion	17
<b>APPENDIX</b>	<b>18</b>
A Comparison of Roth and Traditional IRA Features	18

# BACKGROUND: WHY RETIREMENT SECURITY IS SO IMPORTANT IN NORTH CAROLINA

## Introduction

It is widely recognized that Americans, increasingly responsible for their own retirement security, often find themselves not well prepared at all. Many factors lead to this circumstance. The biggest single factor is whether an individual has access to a retirement savings plan at work. “Low and no” levels of retirement savings lead to poor outcomes for individuals and families. They are also a problem for taxpayers, who may find themselves funding billions of dollars in social services rather than investing tax dollars in schools, communities, and businesses. As fewer workers support an aging population, taxes may go up to meet these needs.

This looming retirement security crisis will have significant impacts on state and local government budgets and revenue, and on the economic well-being of retirees, their families, and our communities. With this knowledge, the North Carolina House of Representatives and the North Carolina Senate unanimously passed [House Bill 604](#). The bill was signed into Session Law 2019-205 on August 27, 2019, creating the Joint Legislative Study Committee on Small Business Retirement Options Study Committee (the Study Committee).

The bill directed the Study Committee to study:

- ◆ Ways the State can reduce the regulatory and operational burden on small businesses that want to offer payroll deduction retirement savings options to employees;
- ◆ Mechanisms the State could use to assist citizens to be more prepared to retire in a financially secure manner, including the operation of a State-administered Individual Retirement Account or multiple employer plan;
- ◆ The feasibility and benefits of partnering with other similar programs established in other jurisdictions; and
- ◆ Optimal oversight for any proposed retirement program.

The Study Committee met in 2020 on February 12 and March 9, hearing from experts in the field of retirement security:

**Sarah Gill, Senior Legislative Representative, AARP.** Ms. Gill discussed national and state metrics related to household retirement savings and the benefits of access to retirement savings plans at work.

**Angela Antonelli, Research Professor and Executive Director of the Center for Retirement Initiatives (CRI) at Georgetown University’s McCourt School of Public Policy** presented options to address the retirement security crisis. Professor Antonelli discussed the models used by a dozen states and one city to address this issue. The models include: Auto IRA (Secure Choice); 401(k) multiple employer plans (MEPs), and retirement marketplaces. She also highlighted the various cultural and demographic changes that are exacerbating the retirement savings crisis.

**John Scott, Director, Retirement Savings Project, The Pew Charitable Trusts** presented information on March 9th in response to the Study Committee’s questions and discussion during the previous meeting. Mr. Scott described the three types of retirement savings programs - Auto IRA programs, multiple employer plans, and online marketplaces and their use in the states that have enacted these types of programs.

The Study Committee also reviewed and was provided access to a range of data and analytical information on retirement security in the US and North Carolina, some of which is cited here.

This report and recommendations are the result of that activity.



**We believe that increasing the savings rates for North Carolinians is critically important.**

Dr. Craig Galbraith,  
University of North Carolina Wilmington

## Critical Challenge: Retirement Security in North Carolina

North Carolina is facing a retirement security crisis. Many North Carolinians are not preparing themselves for retirement. The US has the broadest range of retirement savings options in the world, with thousands of retirement products offered. However, outside of work, many in North Carolina don't use them.

Since 1983, the risk of financial insecurity in retirement has been increasing. Today, over half of the nation's households are at risk of not having enough money to maintain their standard of living in retirement. This doesn't mean not being able to go on a vacation or buy a new car. This means not being able to afford basic necessities -- things like food, utilities, and health care. As shared in the presentation by Sarah Gill of AARP, according to Boston College's Center for Retirement Research, 52% of households are at risk of not having enough to maintain their living standards in retirement (see Figure 1).

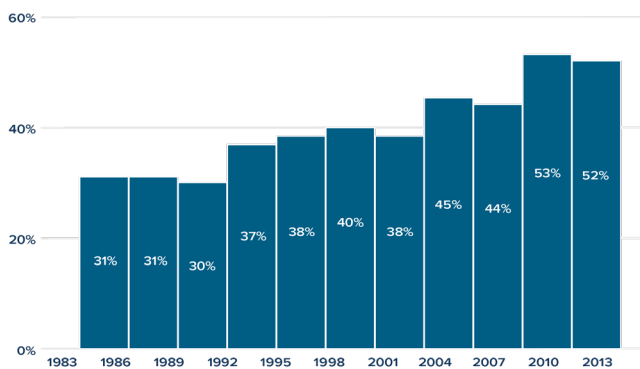
The Baby Boomers are the largest generation in history. They will live longer in retirement than any generation in history, but financially, many are not prepared. Many have virtually no retirement savings. A [report from the National Institute on Retirement Savings](#) shows that **in 2013 across all households, median retirement savings were \$2,500, and only \$14,500 for near-retirement age households.**<sup>4</sup> The number is low because the authors found that almost half of all households have no assets saved for retirement whatsoever (see Figure 2).

In the past, many have relied on defined benefit plans offered by their employers to meet retirement income needs. These defined benefit plans made it easy for workers to have a secure retirement because they offered guaranteed payments at retirement at no risk to the employee. Employees did not have to make any investment decisions. However, recent years have seen a significant shift in how employers approach retirement benefits for their employees.

Now, it is far more common for employers who offer plans to use defined contribution plans. Defined contribution plans give employees the option to choose whether to participate and how much to contribute. Benefits at retirement depend on the amount contributed and how it is invested. Consequently, decisions made by the employee -- like choosing the right investment vehicle, starting to save early, selecting an appropriate rate of contribution, and making sure that fees are low -- play a major role in whether an individual will have enough money to retire.

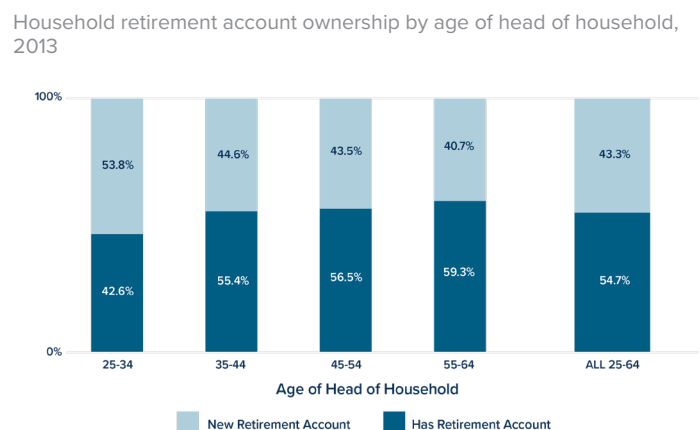
When employers offer these plans, they often provide a fair amount of support for this benefit. Employer contributions help boost saver assets. Employers provide communication and tools related to the plan and make it easy to save by capturing savings on a payroll deduction basis -- increasingly using features like automatic enrollment to get employees participating as soon as they are eligible.

Figure 1: US Households at Risk of Reduced Living Standards



Source: [Boston College's Center for Retirement Research, National Retirement Risk Index](#)

Figure 2: Over 45% of All Working-Age Households Have No Retirement Account Assets



Source: NIRS, *The Continuing Retirement Savings Crisis*, March 2015.

<sup>4</sup> Rhee, Nari PhD and Ilana Boivie, [The Continuing Retirement Savings Crisis](#), March 2015. National Institute of Retirement Security, 2015, p. 12.



## Workers that have a way to save for retirement via payroll deduction are 15 times more likely to save for retirement.



Workers that have a way to save via payroll deduction are 15 times more likely to save for retirement.<sup>5</sup>

Although access through the workplace is critical in helping people save for retirement, many businesses do not offer this option to their employees. Across the nation, only 55% of private sector workers have access to a retirement plan at work.<sup>6</sup> (See Figure 3)

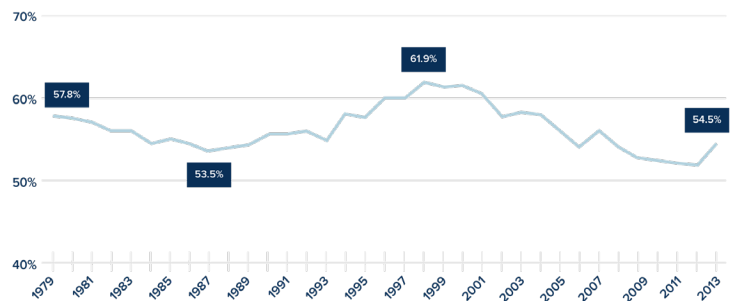
Access is lower in North Carolina, where it is estimated that only 47% of workers in the private sector work for businesses that offer a retirement plan; thus roughly 1,716,000 workers do not have a way to save for retirement at work.<sup>7</sup> The resulting impacts are disproportionately felt by people of color, women, and lower-income workers.

While additional study work needs to be completed, North Carolina's workforce is very likely to have characteristics similar to those observed in other states. Those states have identified that uncovered workers are more likely to be employed in services jobs (restaurant, food service and hospitality; craftspeople, plumbers, electricians, and installers), in construction, and in the raw materials industries (agriculture, mining, forestry). They are also more likely to earn less, are somewhat more likely to work part time, and tend to have less financial experience. These characteristics make having some savings even more important as a source of resilience against natural volatility in income and circumstances.<sup>8</sup>

One might logically ask, can't uncovered employees simply save outside of work into Individual Retirement Accounts? The short answer is "yes, they can," but they rarely do. If these employees want to save for retirement, they are unlikely to do so without access to payroll deduction at their workplace.

Figure 3: Access to Workplace Savings Plans Over Time

Private sector wage and salary workers age 25-64 whose employers sponsor a retirement plan, 1979-2013



Source - NIRS, The Continuing Retirement Savings Crisis

<sup>5</sup> Employee Benefit Research Institute. 2006. Unpublished estimates of the 2004 Survey of Income and Program Participation Wave 7 Topical Module (2006 data). Data are for workers earning between \$30,000 and \$50,000.

<sup>6</sup> Rhee, Nari PhD and Ilana Boivie, *The Continuing Retirement Savings Crisis*, National Institute of Retirement Security, 2015. Page 4.

<sup>7</sup> John, David, and Gary Koenig, *Fact Sheet: North Carolina - Workplace Retirement Plans Will Help Workers Build Economic Security*, AARP, August 2015.

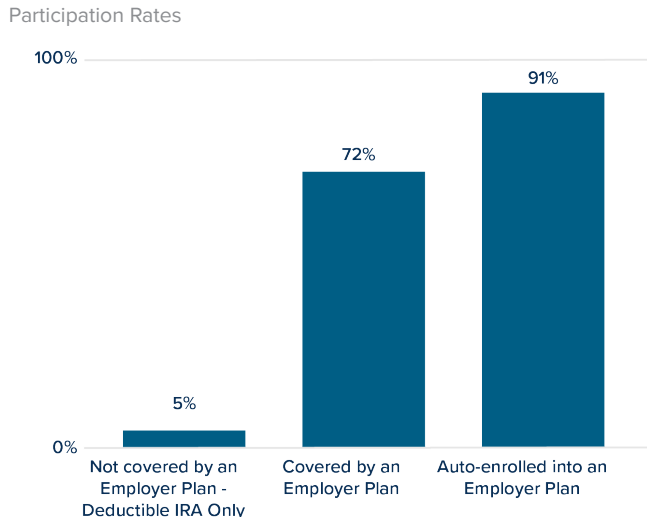
<sup>8</sup> Colorado Secure Savings Plan Board, *Recommendations to Increase Retirement Savings in Colorado*, February 2020 and Center for Retirement Research at Boston College, *Oregon Market Research Report*, July 2016.



AARP's Public Policy Institute working with the Employee Benefits Research Institute found that only 5% of people save in an IRA if they're not covered by an employer plan.<sup>9</sup> According to a 2018 study by Vanguard, participation jumps to 72% when people are covered by an employer plan, and 91% when they're automatically enrolled into an employer plan.<sup>10</sup> This shows that people are 15 times more likely to save when they can do so out of their regular paycheck at work, and 20 times more likely when they are automatically enrolled. (See Figure 4)

With little retirement savings, a growing number are relying on Social Security. Over half of retirees rely on Social Security for 50% or more of their income. More alarming is that for a third of North Carolinians over the age of 65, Social Security is the only source of income. North Carolina residents' average benefit is only about \$1,405 per month, or less than \$17,000 per year.<sup>11</sup> This average income may not even cover basic costs for housing and food. North Carolina, like most states across the nation taking or considering such action, is working to address this retirement saving crisis.

Figure 4: Rates of Participation in Retirement Savings Plans and Accounts



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<sup>9</sup> Employee Benefit Research Institute. 2006. As referenced earlier in this report.

<sup>10</sup> Clark, Jeffrey W., and Jean A. Young, *Automatic enrollment: The power of the default*, Vanguard, 2018.

<sup>11</sup> AARP's Sarah Gill as presented in refreshed form on February 12, 2020, and as originally published in *NC Work and \$ave: A Plan Putting the Financial Security of North Carolina's Workers First!*, AARP, 2015.

## Fiscal Impact to North Carolina

Does retirement insecurity impact taxpayers? A 2016 study by Dr. Craig Galbraith, Professor, Cameron School of Business at the University of North Carolina Wilmington finds that it does.<sup>12</sup>

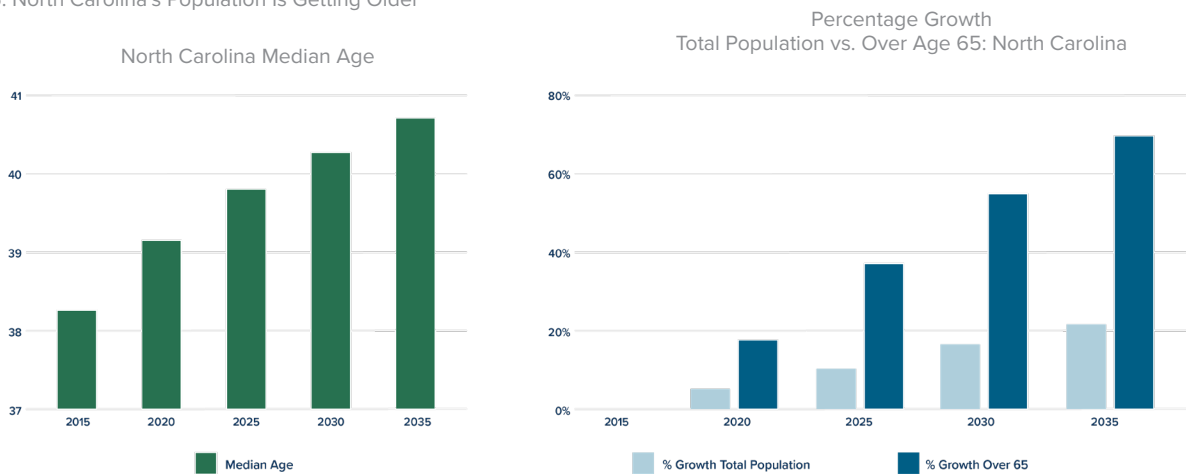
This analysis specifically examines the potential savings to the state of North Carolina if the saving rates of North Carolinians in low- to middle-income groups could be raised by 3% to 5% of current income. The work estimates future state expenditures for select government programs for older adults, and the related financial impact of an increase in savings.

The study uses in-state and national sources for its analysis. This includes the *2015 American Community Survey (ACS)*, the *Survey of Income and Program Participation (SIPP)*, the *2013 Survey of Consumer Finances (SCF)*, population forecasts from the North Carolina Budget and Management Office, and various scholarly articles and research regarding savings rates in the United States. Key factors evaluated include:

- ◆ Forecasts related to North Carolina’s population turning aged 65
- ◆ The number of benefit-years for individuals turning 65, from 2017 to 2030
- ◆ The North Carolina ratio of income to federal poverty levels
- ◆ Available retirement resources for lower-income individuals in North Carolina
- ◆ Future expenditure forecast of North Carolina for the aged (Medicaid and others)
- ◆ Estimated retirement income impact of increased savings, at 3% and 5%
- ◆ Impact of additional saving on eligibility for safety net programs
- ◆ Impact of additional saving on program cost

The study identified that between 2020 and 2035, North Carolina’s 65+ population is expected to grow three times faster than the total population. (See Figure 5).

Figure 5: North Carolina’s Population Is Getting Older



<sup>12</sup> Galbraith, Craig S., *Fiscal Benefits of Increasing the Savings Rates of North Carolina’s Aging Population: Impact on State Expenditures for Retirees*, University of North Carolina Wilmington, December 31, 2016.

This study forecast that boosting retirement savings in the shortfall group by 3 percent could result in a total savings of **\$448 million** in state expenditures between 2018 and 2030, a savings of 8.25 percent of Medicaid spending on residents reaching age 65 during that time period. See Figure 6 for an illustration of the gradual improvement in the number of seniors requiring benefits.

Figure 7 illustrates the annual capture of savings at the state level in North Carolina.

The study found that an **additional \$20 million** could be saved at the combined county and state level in reduced costs for special assistance for adults.

In aggregate, the study forecast nearly a **\$468 million** fiscal impact based on the programs analyzed.

The study did not consider two elements that have been noted in other states. One of these is the impact of lower savings on tax revenue to the state. Retirees with less income spend less and pay less in taxes. In Colorado, this figure was estimated to be about 10% of the overall negative fiscal impact identified.<sup>13</sup>

A second impact is the squeeze on working taxpayers, who are projected to shrink in proportion to the number of retirees as North Carolina’s population ages.

For reference, the states of Colorado and Pennsylvania conducted similar work using different but very thorough methodologies and identified 15-year fiscal impacts to their states of \$10 billion and \$14 billion, respectively.<sup>14</sup>

Figure 6: Reduction in Newly Age 65 Entering NC Medicaid

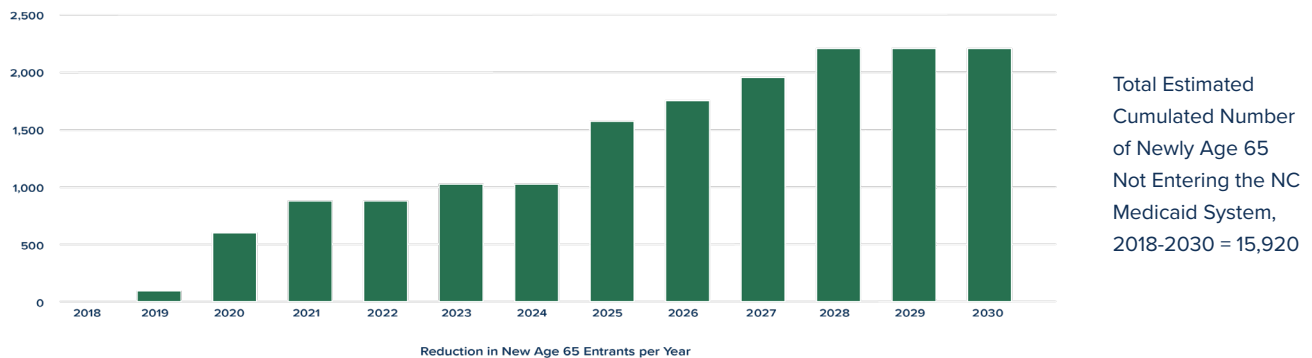
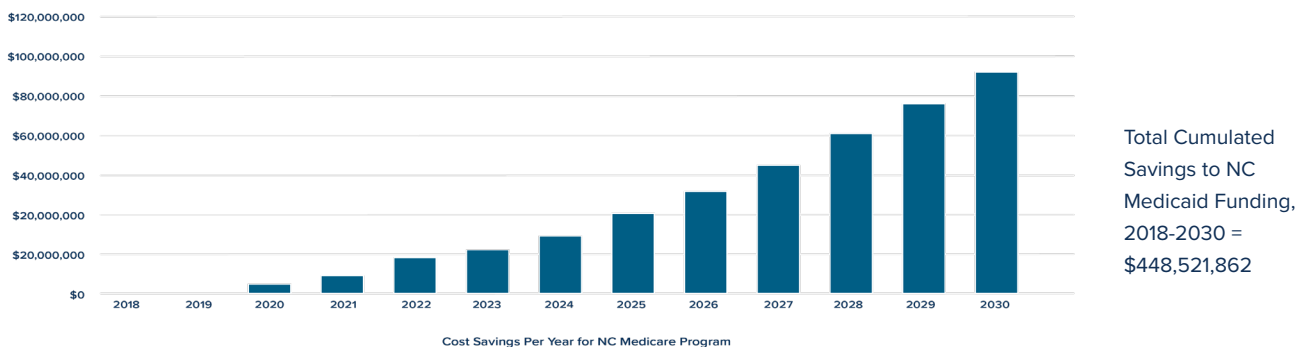


Figure 7: NC Medicaid Participant Yearly Savings and Total Cost Savings



<sup>13</sup> Econsult Solutions Inc., *The Fiscal Impacts of Insufficient Retirement Savings in Colorado: a report to the Colorado Secure Savings Plan Board*, February 2020.

<sup>14</sup> Ibid, and Econsult Solutions Inc., *The Impact of Insufficient Retirement Savings on the Commonwealth of Pennsylvania*, January 2018.

## OPPORTUNITIES FOR NORTH CAROLINA



### Retirement Outcomes in North Carolina – Federal Models

As referenced earlier in this report, for private sector workers there are a variety of ways to save for retirement today. These include workplace-based plans like defined benefit and defined contribution plans. They also include options for individuals choosing to save outside the workplace, such as Individual Retirement Accounts.

The upside of **defined benefit plans (DB)** is that they can be very easy from a worker perspective – you’re either covered, or you are not. If you are covered by a DB plan, you can expect to receive a steady income stream in retirement as a part of your employer’s commitment to you. You don’t have to do anything except work long enough to become fully vested in this benefit.

Defined benefit plans also have some downsides. For one thing, they are not particularly portable. When you leave an employer, you stop earning benefits through that employer. The benefits you have earned remain as a future commitment from that employer to you, but you cannot generally cash them in or transition them to a new employer or retirement account. You also run the risk that the employer’s plan could become underfunded and the employer could have a tough time paying your benefits in the future. In July 2017, Bloomberg reported on the top underfunded corporate pension plans in the US, citing reductions in benefits and other impacts to workers.<sup>15</sup> The list included a number of highly respected “household name” US employers.

For another, there’s generally a built-in delay in the securing of retirement benefits. DB plans are subject to vesting schedules that may allow for a percent of benefits to be earned gradually over a time period not exceeding seven years, or immediately at a point in time not exceeding five years.<sup>16</sup> Workers who leave employers before their benefits are fully vested forfeit a chunk of potential retirement income. In addition, because they were covered by a DB plan there is a good chance they were not independently contributing to an employer 401(k) plan, which would offer some portability. For a mobile workforce, this can lead to a serial forfeiture of retirement benefits.

Finally, well less than 20% of the workforce was covered by a defined benefit plan as of 2018,<sup>17</sup> leaving the balance of workers covered by other types of plans, or not covered.

**Defined contribution (DC)** plans work differently. Compared to DB plans, savings are far more portable. DC plans offer the ability for workers to save on a payroll-deduction basis into a tax advantaged account, typically as part of a 401(k) plan.

<sup>15</sup> Kochkodin, Brandon and Laurie Meisler, *S&P 500’s Biggest Pension Plans Face \$382 Billion Funding Gap*, Bloomberg, July 20, 2017.

<sup>16</sup> U.S. Department of Labor Employee Benefits Security Administration, *FAQs about Retirement Plans and ERISA*, Page.4. Accessed October 2020.

<sup>17</sup> US Bureau of Labor Statistics, *TED: The Economics Daily*, October 12, 2018. Accessed October 2020.

Employers often match contributions at rates ranging from 50% to 100% of the first 2% to 8% of pay set aside by an employee. Limits on annual contributions are relatively high, \$19,500-\$26,000 for employees in 2020, depending on age. Employers are allowed to contribute an additional amount with a total cap of 100% of employee compensation (or \$57,000-\$63,500 in 2020).<sup>18</sup> While employer matches and contributions may be subject to vesting, amounts contributed by an employee are always their own.

DC plans have additional advantages. Employers often cover the costs of administration of the plan, relieving employee savers of this burden. Plans generally offer investment menus that are set and monitored by the employer. The employer is a fiduciary to the plan, required to operate the plan “solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses.”<sup>19</sup> Increasingly, DC plans are deploying automatic features, like automatic enrollment and automatic annual escalation of savings. Not only do these features get workers into plans much faster, they also simplify the process by establishing a standard starting saving rate and investment choice – two decisions that confuse the average worker when they are trying to figure out how to get started saving.

Defined contribution plans also have some downsides. Like DB plans, they are only offered to a subset of the workforce: typically, those working full time, and who are in fairly stable, often higher-compensated employment. Even for those workers, DC plans come with some wrinkles. First, not all DC plans offer automatic enrollment. A wide-ranging survey by Vanguard showed that by the end of 2017, a little less than half of their client plans were offering this feature.<sup>20</sup> When automatic enrollment is not used, plan participation tends to languish at levels below 60%.<sup>21</sup> One reason for lower participation rates may be the decisions workers have to make in order to get started: is it a priority for me today; how do I sign up; how much should I be saving; what investments should I choose. These decisions can be daunting.

For plans that offer automatic enrollment, the automatic features of savings rate and investment tend to be very sticky. Participants tend to make few adjustments to their savings rates and investments. If you have a high starting savings rate, with annual escalation and an age-based investment with some market exposure, you may be just fine. If your plan has a low starting savings rate, no escalation, and a low-risk, low-return standard investment, you run a real risk of not saving enough.

Finally, as with defined benefit plans, DC plans are offered voluntarily by employers who choose to include them in their benefits packages. In North Carolina, this means that 53% of the workforce doesn’t have the option to save for retirement at work. Workers in this group are among the many who must save for retirement outside of the workplace.

For uncovered workers, IRA accounts are the most widely available tax-advantaged retirement vehicle. IRAs have lower annual savings limits than 401(k) plans. Income-based factors apply, but generally the contribution limits for IRAs are \$6,000-\$7,000 in 2020, depending on whether you are under or over age 50.<sup>22</sup> While IRA accounts are available through thousands of financial institutions, the sheer number of institutions and investments create a conundrum: where should I save; what will it cost; can I be confident I’m making good decisions. Add to this the basic decisions of ‘how much should I save’ and ‘which investments should I use’ and you find that a small percentage of workers successfully establish and fund their own retirement accounts. Estimates put this figure between 5% and 15%.<sup>23</sup>

Altogether, the availability and use of employer-sponsored plans and independent IRAs provides only a partial solution to the need in North Carolina for retirement savings and retirement income security.



**Altogether, the availability and use of employer-sponsored plans and independent IRAs provides only a partial solution to the need in North Carolina for retirement savings and retirement income security.**

<sup>18</sup> IRS, [Retirement Topics - Contributions](#), accessed October 2020.

<sup>19</sup> US Department of Labor, [Fiduciary Responsibilities](#), accessed October 2020.

<sup>20</sup> [How America Saves 2018](#), Vanguard, June 2018. Page 5.

<sup>21</sup> Ibid, Page 11.

<sup>22</sup> IRS, [Retirement Topics - IRA Contribution Limits](#), accessed October 2020.

<sup>23</sup> 5% - AARP presentation to the Study Committee on February 12, 2020; 15% - Scott, John, [3 Ways People May Save for Retirement in the Future](#), Pew, March 14, 2019.

## Improving Outcomes in North Carolina – State Retirement Models

With the looming retirement savings crisis and significant impact to state revenue and budgets, states are driving change. Most states are considering or taking action to expand access and improve long-term retirement income outcomes. States’ goals are to improve the availability of simple, low-cost, easily accessible and effective savings options. Figure 8 provides a current view of the US.

There are now 12 states that have enacted retirement savings programs for private-sector workers whose employers do not offer plans. The state programs can be divided into three groups:

- ◆ Retirement marketplaces
- ◆ Multiple employer plans (MEPs), and
- ◆ Auto IRA Programs

Figure 9 provides a view of programs enacted by states, with first contribution dates where programs are live.

A description of the three models and their primary characteristics follows. Where available, usage information is provided.

### Auto IRA Programs (“Secure Choice”)

These programs are designed to be simple, low cost and easily accessible for employers and employees. They use IRA accounts and features like automatic enrollment, payroll deduction, and automatic, gradual savings increases. Features like these are increasingly used by today’s employer sponsored retirement plans because they are effective in boosting participation and savings. With Auto IRAs, workers have the flexibility to change investments, and to save more, or less. They can opt out of saving altogether or withdraw their savings at any time.

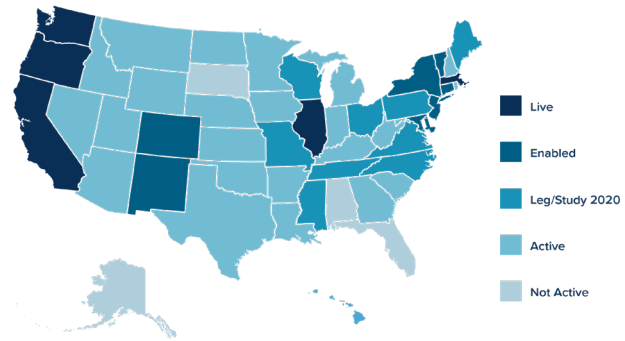
Auto IRA programs come in two forms. In one form, employers are not required to facilitate the program. Two states have passed legislation enabling these types of programs: New York in 2017, and New Mexico in February of 2020. New York has not launched their program or established their governing board. Proposed language would make their program mandatory for employers, but this change has not yet been adopted.<sup>24</sup>

In the more commonly used form of Auto IRA and the only form that has been implemented to date, covered employers are required to facilitate the program. Some parts of the below comments apply specifically to employer-required Auto IRA programs.

In an Auto IRA program, employees are automatically enrolled to begin saving into an individual retirement account (IRA). Automatic enrollment includes the use of standard savings rates and investments. Typical standard contributions are 5% of pay, although that level is set by each state individually. Workers can opt out or change their contribution level at any time. Covered employers facilitate the state’s retirement savings program if they do not otherwise offer a plan. The state establishes the definition of covered employer, often based on employer size (for example, California excludes employers with fewer than five employees). Employers may exempt themselves from facilitating at any time by offering a qualified plan of their own.

Figure 8: States Studying, Introducing Legislation, and Launching Retirement Savings Programs

State Facilitated Retirement Savings



Information as presented to the Study Committee by the Pew Charitable Trusts, brought current to October 2020 by Massena Associates LLC.

Figure 9: State Retirement Savings Programs (first contributions)

RETIREMENT MARKETPLACE	MULTIPLE EMPLOYER PLAN	AUTO IRA PROGRAM
Washington State (2018)	Massachusetts (2017)	Oregon (2017)
New Mexico	Vermont	Illinois (2018)
		California (2019)
		Maryland
		Connecticut
		New Jersey
		New York
		New Mexico
		Colorado

<sup>24</sup> New York State Assembly, [Bill A05978B](#), accessed October 2020.

Employers may not contribute, and their primary responsibility is to provide a limited set of employee data to the program and to process regular payroll contributions for employees who elect to save. Employers are not fiduciaries and are not responsible or liable for investments or program administration.

To date, programs have used Roth IRAs as the standard account type. Roth IRA contributions are made on an after tax basis and can be withdrawn by employees at any time and without penalty or taxes. Traditional IRAs may also be offered as a participant choice. Because Roth contributions are made on an after tax basis, contributions do not impact current year state revenue in states with income taxes. Saver IRA accounts are subject to the federal limits on annual contributions, which are lower than the limits for 401(k) plans. Because the populations served typically have a lower average income, very few savers (well less than 1%) ever hit the federal savings cap every year.

Programs are often operated in partnership with private sector firms, who manage investments and provide services like record keeping and administration. To date, these firms have also borne some of the financial burden of program startup and operation in the early years.



#### WHAT IS AN AUTO IRA?

- ◆ Account type: IRA
- ◆ Automatic enrollment, with opt out
- ◆ Contributions by payroll deduction
- ◆ Simple investment menu
- ◆ Employers: execute regular payroll deductions for workers who choose to save

## Multiple Employer Plans

A multiple employer plan, or MEP, is a single retirement plan that is adopted by two or more unrelated businesses. MEPs are 401(k) plans and are therefore covered by ERISA and subject to its requirements and regulatory structure.

For workers, MEPs offer all the advantages of 401(k) plans described earlier. For employers, the availability of a MEP can simplify some of the decisions associated with establishing a retirement plan, and parts of the fiduciary burden may be lightened where they are shared with others, for example in the selection and monitoring of investment managers.

Under the MEP model, states sponsor multiple employer plans which employers may decide voluntarily to join. MEPs are generally run by a private plan administrator and offer mutual funds and other private sector investment options. If an employer does join the state-facilitated MEP, the employer can auto-enroll workers and make employer contributions in addition to workers' contributions.

Massachusetts and Vermont have chosen to offer MEPs. The Massachusetts CORE program, launched in October 2017, is available to non-profit organizations with 20 or fewer employees. When launched, Vermont's MEP will be available to businesses with 100 or fewer employees.

Pursuant to the 2019 Federal [SECURE Act](#), it is now easier for businesses to act on their own to join together to offer MEPs and benefit from the economies of scale. It is anticipated that private sector MEPs will become more common starting in 2021. Because employer participation is voluntary, MEPs are not expected to significantly close the workplace retirement access gap.

## Retirement Marketplaces

Under the retirement marketplace model, the state provides a website for financial service providers to offer retirement products to small employers. The only marketplace launched to date is the Washington Small Business Retirement Marketplace, enacted in 2017. In Washington State, the program is limited to small employers and individual employees, and the state reviews and approves the product offerings from financial service providers before they are offered on the marketplace. Financial firms are not required to offer products, and employers and employees are under no obligation to go to the website or select a plan.

## Results of State Models

### Auto IRA Programs (“Secure Choice”)

OregonSaves was the first Auto IRA to go live, in July of 2017. The program launched statewide in a series of waves to increasingly smaller employers starting in January 2018. As of November 2020, over 83,000 Oregonians have funded accounts and contribute about \$130 a month, and assets in the program have grown to over \$77 million.<sup>25</sup> The average account balance in the Oregon program is more than \$950, while early savers have account balances averaging more than \$3,000.

Auto IRAs in other states have increased coverage and savings relatively quickly because of their simplicity for both employers and employees.

Across the three programs as of November 2020, more than 216,000 workers had established funded accounts, saving a combined \$136 million (see Figure 10).<sup>26</sup>

Figure 10: State Auto IRA Programs as of November 2020

State Auto IRA Programs*	Year to Date Increase**	Most Current***	9/30/2020	6/30/2020	12/31/2019
Total Assets	149%	\$136,273,359	\$115,382,510	\$89,851,932	\$54,823,423
Funded Accounts	99%	216,505	173,445	151,107	108,945
Employers Registered to Facilitate	37%	26,753	23,578	21,492	19,498
Employers Started Payroll	97%	10,090	9,420	8,735	5,134

\* OregonSaves, Illinois Secure Choice, and CalSavers

\*\* Year to Date percentage increase, December 31, 2019 to Most Current.

\*\*\* Hybrid data as of publication - October 16 and November 17, 2020

Source: Massena Associates, November 2020



### Multiple Employer Plans

Launched in October 2017, the Massachusetts CORE program is available to non-profits with 20 or fewer employees. As of November 2019 after two years in operation, 63 employers and 460 employees are currently registered in the program, accounting for less than one-half of 1% of Massachusetts employees working at small non-profits.<sup>27</sup>

### Retirement Marketplaces

Launched in March of 2018, [Washington’s Small Business Retirement Marketplace](#) now offers nine types of retirement plan and account choices from three providers. In 2017 the state identified that about 2 million workers are not covered by a plan at work.<sup>28</sup> The state of Washington estimates that about 131,000 of its businesses do not offer plans. As of the end of 2019, this program had added fewer than 200 savers. In contrast, neighboring state Oregon’s Auto IRA program [OregonSaves](#) currently has over 83,000 savers whose aggregated account balances are more than \$77 million. Based on this experience, in 2019 and 2020, Washington legislators [introduced a bill](#) to enact an Auto IRA program for the state.

<sup>25</sup> Figures provided by OregonSaves, November 2020.

<sup>26</sup> Massena Associates LLC, November 2020, provided as an update to the results shared with the Study Committee by the Pew Charitable Trusts in March 2020.

<sup>27</sup> John Scott, Director, Retirement Security Project, the Pew Charitable Trusts, October 2020.

<sup>28</sup> [Retirement Readiness: Washington State Retirement Preparedness Study](#), Washington State Department of Commerce, November 2017.



## Perspectives: Employers and Workers

### Employer Perspectives: Impact on Business

During its tenure, this Committee did not have time to survey North Carolina employers directly. However, the Committee directed a number of employer-related questions to Pew and was referred to Pew's studies of employer experience in Auto IRA implementing states.

In Pew's survey of employers participating in the OregonSaves Auto IRA program, respondents commented on positive aspects of the program (and separately on the challenges). Several employers noted that OregonSaves gave them the ability to offer retirement benefits when they could not afford their own plan:<sup>29</sup>



**Having an option for employees to save for retirement in the absence of an employee plan.**



**Glad our team has access to a retirement plan, as we can't afford a traditional retirement plan.**



**I appreciate that it is free and it allows our employees to start saving for their retirement, a benefit that we wouldn't have implemented otherwise, because of the cost.**



**I do appreciate the program overall. It helps younger staff start saving early. From a small business that can't afford to have a retirement plan, it is a nice option for our team.**

In addition to the ability to facilitate retirement savings in a low-cost manner, at least one employer appreciated the reduced fiduciary responsibility:



**I appreciate that I am absolved from telling the employees whether to invest and how much.**

The Study Committee requested information on the return on investment to employers from these state-facilitated retirement savings programs, and on payroll-related costs. The team from Pew provided the following information during discussions with the Committee on March 9, 2020 and committed to provide access to ongoing information as available.

Regarding return on investment to employers, benefits could include:

- ◆ the ability to offer access to retirement benefits to attract and retain workers;
- ◆ the no-cost aspect of Auto IRA programs; and
- ◆ the reduced legal or fiduciary liability with Auto IRAs compared to adopting a traditional retirement plan.

In Pew's survey of small employers,<sup>30</sup> a primary motivation for offering retirement benefits is helping workers save for retirement and attracting and retaining talented employees. However, retirement benefits are usually offered after health insurance and paid time off are provided, which makes sense as those latter benefits deal with more immediate needs. The survey also found that employers offer retirement benefits after some growth in size and development, indicating a need to reach financial stability before taking on plan sponsorship. Employers that did not offer retirement benefits stated that startup costs and lack of administrative capacity were the main obstacles to offering retirement benefits.

Subsequent study activity on the OregonSaves program has identified the following results. To help inform policymakers considering an Auto IRA program, The Pew Charitable Trusts from 2019 to 2020 surveyed nearly 2,400 private sector businesses that are currently participating in OregonSaves. The survey was designed to help better understand how employers experience the program in terms of their satisfaction with different program elements and whether OregonSaves imposes any costs or burdens.<sup>31</sup>

<sup>29</sup> Pew, pre-publication results of 2019-2020 OregonSaves Employer Survey, October 2020.

<sup>30</sup> Pew, [Employer barriers to and motivations for offering retirement benefits](#), June 21, 2017.

<sup>31</sup> Pew, pre-publication results of 2019-2020 OregonSaves Employer Survey, October 2020.



**The responses generally show strong levels of satisfaction with OregonSaves. Among the key findings:**

- ◆ Overall, 73% of participating employers are satisfied or neutral (neither satisfied nor dissatisfied) with their experience in the program.
- ◆ Expressed satisfaction is two-and-a-half times higher among employers who have begun to process payroll contributions into funded accounts for their employees compared with those that have not yet started.
- ◆ This survey was carried out in three waves, the last of which coincided with the onset of the COVID-19 pandemic. However, the stay-at-home order in Oregon does not seem to have had an effect on satisfaction levels.
- ◆ Higher satisfaction is associated with firms that register with the program well in advance of their registration deadlines, which suggests a demand for Auto IRA programs like OregonSaves among a significant number of businesses. Time spent in the OregonSaves program is also linked to higher satisfaction, which implies that growing familiarity with OregonSaves may lead to increased satisfaction.

**The survey did not find that OregonSaves was costly to employers:**

- ◆ About four-fifths of OregonSaves employers did not report any out-of-pocket (OOP) costs associated with the program.
- ◆ Among the roughly 20 percent that did report OOP costs, some employers cited fees for outsourcing program contributions to external payroll firms or bookkeepers, or wages for additional staff time. Others counted time spent registering employees with OregonSaves as OOP costs; this may partly explain why employers who handled payroll internally were about equally likely to report OOP costs as employers who outsourced their payroll management.

**In terms of burdens on employers, employers did not find a lot of questions or concerns from workers:**

- ◆ Four-fifths of employers (79.8%) reported that their employees had few or no questions.
- ◆ About four percent of all employers reported that their workers had a lot, or a great deal, of questions about the program.
- ◆ Different forms of outreach and communication had varying effects on employee concerns. A visit from an OregonSaves representative minimized questions directed to an employer. Employers also reported that the OregonSaves website was helpful to their employees. Giving employees the OregonSaves handout was less helpful. Not notifying workers at all did not shield employers from questions about the program.

## Other Considerations

The following includes additional areas of interest that should be considered further as part of overall program design for North Carolina.

### Part-Time, Contract or “Gig” Workers

In her report to the Study Committee, Professor Antonelli of Georgetown highlighted the ability of state-facilitated programs to serve the independent workforce, citing “the potential to assist gig workers” as one of the key ways state programs transform the retirement landscape.<sup>32</sup>

In its discussions, the Committee asked about the process for enrolling independent workers or self-employed persons into state-facilitated retirement savings program, and how other states have handled 1099 and part-time workers in their programs.

John Scott of Pew’s Retirement Savings Project advised that contract workers are able to self-enroll in any of the existing state programs. Further, current implementing states do not have explicit exclusions on “commission-paid” workers like Realtors or independent salespeople. Those who are classified as employees because they fall under the state guidelines of receiving a W-2 or of contributing to unemployment insurance are treated just like salaried workers and provided with automatic enrollment.

While the independent workforce is difficult to measure, a recent analysis by a joint research team of the US Department of the Treasury and the Internal Revenue Service indicates that the percentage of 1099 and independent contractors in North Carolina is among the fastest-growing in the nation.<sup>33</sup>

### Roth or Traditional IRA Accounts

A program that uses automatic enrollment will need to establish standard features – such as the type of account an individual will be enrolled into if they don’t make a specific election. In the US, traditional and Roth IRAs offer different types of contribution deductibility, tax treatments, and penalties for early withdrawal of contributions and earnings. The Committee requested an overview of the different account types (e.g., Roth IRA, traditional IRA) with comparative information. That analysis can be found in the Appendix.

Current implementing Auto IRA programs, following analysis, have elected to use Roth IRAs as the standard for their automatically enrolled savers. Rationales cited include the ability for savers to access contributions in an emergency or for other reasons without incurring financial penalties. Programs also offer traditional IRAs as an available choice.

This is an area for further exploration in North Carolina.

### Cost to Employees

The Committee requested information on program costs for employees. The following provides a summary of information provided to date. Program costs overall are an important element and should be evaluated further, depending on the final form of program recommended.

In addition to investment fees, retirement plans, including the Auto IRA programs, often charge fees for administration and record keeping. Oregon charges 85 basis points for the external plan administrator and another 5 basis points for internal administrative costs, or \$9 for every \$1,000. Similarly, California charges 75 basis points for the external plan administrator and 5 basis points for its own administrative costs, however, these fees could fall to as low as 12 basis points for the administrator as assets under management grow. Total fees (investment and administrative fees) in Oregon cannot exceed 105 basis points while the cap in California is 100 basis points. Illinois charges 75 basis points all in, or \$7.50 for every \$1,000.

To put those fees in context, in the 401(k) space, small employers with private sector plans generally face somewhat higher fees: According to a 2019 Investment Company Institute study,<sup>34</sup> the total fees for 401(k) plans

<sup>32</sup> Antonelli, Angela. *Addressing the Retirement Savings Crisis: What Can North Carolina Do?* Presentation to the Joint Legislative Study Committee, February 12, 2020.

<sup>33</sup> Lim, Katherine, et al, *Independent Contractors in the U.S.: New Trends from 15 years of Administrative Tax Data*, as authorized under the IRS Joint Statistical Research Program, July 2019.

<sup>34</sup> Investment Company Institute, *The BrightScope/ICI Defined Contribution Plan Profile: A Close Look at 401(k) Plans*, 2016, June 2019.

with less than \$1 million in assets ranged from 257 basis points near the top of the scale at the 90th percentile to 54 basis points near the bottom at the 10th percentile. The median was 126 basis points, or \$12.60 for every \$1,000 in the account.

In summary, Auto IRA programs can keep costs low for employers and employees, and can be cost effective for states to implement.

# IMPROVING RETIREMENT SECURITY: RECOMMENDATIONS FOR NORTH CAROLINA

After careful consideration of the information provided in its meetings and summarized here, the Study Committee makes the following recommendations for North Carolina.

## Development of this recommendation:

To carry out its responsibilities, the Committee learned the following:

- ◆ Approximately 53% of the state’s workforce does not have access to a retirement savings plan at work;<sup>35</sup>
  - Currently more than half of the state’s small employers do not offer retirement plans.
  - Many other workers are not covered by an employer’s plan because they work part time, are in an uncovered classification or are independent contractors.
- ◆ Without access to a retirement savings plan at work, most people simply will not save for retirement on their own. In fact, workers with access to a workplace retirement plan are 15 times more likely to save for retirement.<sup>36</sup>
- ◆ Because too many are not saving for retirement, North Carolina’s expenses will increase significantly as those who have not saved will require more social services. In fact, a 2016 study by the University of North Carolina Wilmington forecast a positive fiscal impact of approximately \$468 million to the state with modest increased savings rates of 3% to 5% by workers in low- to middle-income groups, which are over-represented in the uncovered population.<sup>37</sup>

## Model and Approach

If North Carolina is interested in adopting a retirement security approach that will significantly improve coverage of and use by the 1.7 million workers in the state who do not have access to a retirement plan at work, a state-facilitated Auto IRA program is the model which has shown itself to be significantly more effective than the alternatives. As shown here, this model also has the greatest likelihood of helping the state achieve significant savings to rising costs for social services programs.

We therefore recommend a state-facilitated Auto IRA program as the preferred model to help savers and to help the state achieve savings.

## Open Elements – Task Force

A number of important elements remain open that require further consideration. These include:

- ◆ Development of a program design recommendation:
  - Including elements identified in this report, and
  - Taking into account an analysis of North Carolina’s employer and workforce demographic information and key metrics
- ◆ Evaluation of the ability to partner with similar programs established in other jurisdictions
- ◆ Evaluation of the feasibility of establishing either a stand-alone or partnered program
- ◆ Establishment of a general fund loan or other funding source(s) for program startup and early operation — programs are designed to be cost-neutral to the state
- ◆ Determination of optimal oversight for any proposed program

If the General Assembly proceeds with legislation to address the retirement savings crisis in North Carolina, the preferred model to help workers save and to help the state achieve fiscal savings is an Auto IRA program.

We recommend that if the General Assembly proceeds, the authorizing legislation should include the appointment of a Task Force to oversee the open elements identified above. At the completion of its work, the Task Force should be replaced by an Implementing Board that will be established by the Agency or Authority identified to oversee the program.

<sup>35</sup> John, David, and Gary Koenig, [Fact Sheet: North Carolina - Workplace Retirement Plans Will Help Workers Build Economic Security](#), AARP, August 2015.

<sup>36</sup> Employee Benefit Research Institute. 2006. As referenced earlier in this report.

<sup>37</sup> Galbraith, Craig S., [Fiscal Benefits of Increasing the Savings Rates of North Carolina’s Aging Population: Impact on State Expenditures for Retirees](#), University of North Carolina Wilmington, December 31, 2016.

## Conclusion

It is clear there is a need for better and broader work-based retirement savings coverage for North Carolina's workforce. The cost of doing nothing is significant for North Carolina's taxpayers. At the same time, a fairly simple intervention has the ability to change that future dramatically.

Programs such as the one recommended here have been proven to work in other states. In a short period of time they have helped uncovered workers save meaningful amounts toward retirement, while serving as emergency savings for a small number of workers who occasionally need some of that cushion. This year's pandemic, hurricanes and other unexpected circumstances have reinforced the importance and usefulness of having access to some emergency savings.

These programs are designed to be very light touch for small business. Employers are able to facilitate retirement savings for workers into the worker's own IRA accounts without the financial responsibility and liability associated with starting a full retirement plan.

And finally, Auto IRAs are designed to be very cost effective for the states that implement them. Following a startup period accompanied by modest funding, the aim of these programs is to be cost-neutral to the state while reducing the likelihood of expanded future taxes associated with social safety net programs.

## APPENDIX

### A Comparison of Roth and Traditional IRA Features

An IRA, or individual retirement account, is an investment vehicle designed for building retirement savings. IRAs offer tax benefits, although those benefits will differ depending on the type of IRA (Traditional or Roth). IRAs are governed by federal tax rules. The following table compares the two types of IRAs, Roth and Traditional, because these are the vehicles used in the state-facilitated Auto IRA programs.<sup>38</sup>

	Roth IRA	Traditional IRA
<b>Contributions</b>	Up to \$6,000 (\$7,000 for those 50+) in 2020.	Up to \$6,000 (\$7,000 for those 50+) in 2020.
<b>Tax Benefits</b>	Contributions are made from after-tax income; earnings grow tax-free.	Contributions are tax-deductible, earnings grow tax-free. Deductibility is dependent on income and whether you (or your spouse, if any) are covered by an employer-sponsored retirement plan.
<b>Withdrawals</b>	Contributions can be withdrawn at any time, tax-free and without penalty; withdrawals of earnings are taxable and subject to a penalty unless certain conditions are met such as reaching age 59 and 1/2.	If you take out money from a traditional IRA before age 59 and 1/2, there is a 10% penalty (there are exceptions to the penalty) Withdrawals are taxable at the income tax rate when you make the withdrawal.
<b>Required Minimum Distributions</b>	None for the IRA owner.	Distributions must begin at age 72 for the IRA owner.
<b>Who Can Contribute; Income Limits</b>	For 2020, individuals must have a modified adjusted gross income of \$139,000 with contribution being phased out starting at a MAGI of \$124,000; married households must have a MAGI of less than \$206,000 to contribute and contributions are phased out starting at \$196,000	
<b>Miscellaneous</b>	After 5 years, up to \$10,000 of earnings can be withdrawn penalty-free to cover first-time home-buyer expenses. Qualified education and hardship withdrawals may be available without penalty before the age limit and five-year waiting period.	Up to \$10,000 penalty-free withdrawals to cover first-time home-buyer expenses. Qualified education and hardship withdrawals are also available.

<sup>38</sup> The Pew Charitable Trusts, as presented to the Study Committee on March 9, 2020.

**Report to the General Assembly of North Carolina by the Joint  
Legislative Study Committee on Small Business Retirement Options  
Pursuant to NC Session Law 2019-205**

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December 1, 2020