

Gaps in Retirement Savings based on Race, Ethnicity, and Gender

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Good afternoon members of the Department of Labor’s ERISA Advisory Council. My name is Anqi Chen, and I am the Assistant Director of Savings Research at the Center for Retirement Research at Boston College. Thank you for the opportunity to speak to you today about “Gaps in Retirement Savings based on Race, Ethnicity, and Gender.”

This testimony underlines the importance of broader coverage and incentives to encourage savings among low and moderate wage workers and close the gap across race, ethnicity, and gender. Specifically, it argues that expanding the existing state Auto-IRA programs, combined with making the Saver’s Credit refundable, could improve the retirement security of uncovered workers in a meaningful way.

Why Are 401(k)s Falling Short of their Potential

In the United States, most private retirement savings plans are provided through an employer on a voluntary basis. However, only half of private sector workers participate in a plan at any given time, and many with a plan have insufficient balances to maintain their standard of living when they retire.

Moreover, this lack of universal coverage is set against a backdrop where the employer retirement system has shifted decidedly from defined benefit to defined contribution plans (Figure 1).

In theory, 401(k) and other defined contribution plans could generate significant wealth if workers contribute consistently from a young age, keep their money in their accounts, and minimize their investment fees. For example, a 25-year-old median earner in 1984 who contributed regularly would have accumulated about \$425,000 by age 60. However, most workers have 401(k)/IRA balances at retirement that are substantially below their potential. Part of the explanation is that because 401(k) plans are recent, many of today’s near-retirees did not participate in a 401(k) when they were young workers. However, even in a mature system, estimated actual balances are still less than half of the potential. The main reason is inconsistent coverage/contributions (Figure 2).¹

This lack of consistent coverage or contributions can occur for a number of reasons. The most important is that the employer does not offer a plan. But employees can also work for an employer that offers a plan for some of its employees but not be eligible to participate themselves (Figure 3).² Or their employer can offer a plan and they can be eligible to participate but choose not to do so – though this group only accounts for a small minority of all the workers

¹ The conclusion that contributions fall so far short of potential may seem surprising. However, three pieces of evidence support this finding. First, linked administrative tax records show that the typical worker ages 35-44 in 2014 has spent less than half of their working life contributing to a retirement account. Second, aggregate data from the IRS *Statistics of Income* confirm this pattern – only 37 percent of all workers deferred earnings into a retirement account in 2014. Third, data on contributions by age show that the majority of even young workers are not contributing earlier in their career. It is unclear from the tax data whether workers just do not have coverage earlier on in their careers or if other priorities hinder saving for retirement. See Biggs, Munnell, and Chen (2019).

² This includes low tenure workers, part-time workers, and contractors who are not eligible for benefits, among others (see Munnell, Belbase, and Sanzenbacher, 2018).

who do not participate. Overall, inconsistent coverage and contributions results in actual balances being over 30 percent less than potential.

Leakages – due to cash out job changes, in-service withdrawals, or loans – and fees are other factors that can erode 401(k) accumulations, but their role is much smaller (Figure 2). Congress has tried to limit withdrawals by imposing a 10-percent penalty (in addition to federal and state income taxes). Fees have declined noticeably over the last two decades likely due to the rise in passive mutual funds, the Department of Labor’s 2012 requirement that service providers disclose fees, and litigation over 401(k) fees. Therefore, the lack of consistent coverage still represents the biggest barrier to 401(k) accumulations.

Differences by Income, Race/Ethnicity, and Gender

The lack of universal coverage is also a major reason for disparities in retirement asset accumulation across income, race/ethnicity, and gender. Lower-wage workers – who are more likely to be Black, Hispanic, or women – are more likely to work in jobs without a plan (Table 1). They are also more likely to be part-time or contingent workers, who are often not eligible to participate in a plan.

As a result, the typical white worker will spend 58 percent of his career at a job with retirement coverage, compared to 48 percent for Black workers, 37 percent for Hispanic workers, and 54 percent for Asian workers (Figure 4). Workers with a college degree or more spend over two-thirds of their career in covered employment while workers with a high school degree or some college have coverage about half the time and those with less than high school a quarter of the time (Figure 5). Interestingly, the gap between men and women has mostly closed (Figure 6).

These differences in access to retirement savings plan coverage build up and the gaps in 401(k) accumulations across groups have grown over time. In 1989, the average 401(k)/IRA balances for a white worker were 25 percent of their income while the average for Black and Hispanic workers were around 4 percent of income. By 2019, the average balance for white workers had risen to 116 percent of their income while that of Black and Hispanic workers was only 39 percent and 25 percent of their income, respectively (Figure 7). Similar trends can be observed by educational attainment, a proxy for lifetime income (Figure 8). Given that coverage rates are similar across genders; it is not surprising that asset accumulations are also similar (Figure 9). However, it is important to keep in mind that women are much more likely to be in the bottom income tercile, they are more likely to retire early, and are more likely to take time off for childcare and other caregiving duties.

Proposals to Increase Retirement Savings

Since very few workers save for retirement unless their employer offers them a retirement plan, the lack of access to an employer-based plan has emerged as a pressing problem.

Prior studies have found two potential levers to improve retirement savings among low and moderate income workers. The first is automatic enrollment. Since people often do not deviate

from default options, studies have shown that this simple change increases participation.³ The second is offering savings incentives, such as matching contributions. Studies have found that higher match rates, in combination with simplified information, encouraged participation.⁴

Initiatives to Improve Coverage

Several initiatives to address the savings gap have been enacted at the federal level over the years (Table 2). However, these programs have relied on the voluntary participation of employers and therefore have had little impact.

Several policy experts have offered other elegant solutions with a mandatory component to the address the coverage gap, but Congress has not enacted any of them.⁵

In the absence of meaningful federal action, states have seized the issue (Figure 10). The inclusion of a mandate for employers is a significant differentiator for state programs. Mandatory auto-IRAs require employers without a retirement plan to auto-enroll their employees in an Individual Retirement Account (IRA). Voluntary programs, which involve “marketplaces,” multiple employer 401(k)s, and voluntary auto-IRAs, allow the employer to choose whether to participate (Table 3).

Not surprisingly, the mandatory programs are showing potential in the early phases. In contrast, voluntary programs have had virtually no impact, with less than a 1-percent take-up rate.

Proposals to Improve Participation and Contributions

These state initiatives could potentially be enhanced by the federal Saver’s Credit, an existing tax incentive that could, in essence, provide a match on contributions to a state plan.⁶ 401(k)s rely on matches by employers, which are not part of the auto-IRA design, but the Saver’s Credit, with some improvements, could serve the same purpose.

³ Nessmith, Utkus, and Young (2007); Madrian and Shea (2001); Choi et al, (2001).

⁴ Duflo et al. (2006); Choi, Laibson and Madrian (2004); Madrian et al (2013).

⁵ Former Senator Tom Harkin (who was chairman of the Health, Education, Labor, and Pensions Committee) proposed the “USA Retirement Funds Act,” which would require employers that do not provide a retirement plan to automatically enroll their employees. However, instead of using payroll deduction IRAs, it would have created a government-mandated, privately-managed defined contribution pension program. The contributions would be invested in a commingled portfolio, thereby spreading the risks among all participants and relieving the individual of the burden of making investment decisions. Payments from the plan would be in the form of an annuity, so that retirees would not have to worry about outliving their savings. Again, workers would be able to opt out. Teresa Ghilarducci has proposed the creation of individual Guaranteed Retirement Accounts, which allow both employee and employer contributions, and would be required for all employers with more than 5 employees. This proposal is akin to a mandatory auto-IRA program, but private contributions would be required by both employee and employer; there would also be a nationwide tax credit to defray the costs of this requirement for low-income households. In 2019 scholars at the Brookings Institution suggested that the Social Security Administration (SSA) could oversee the collection of retirement savings contributions, as it already keeps records of payroll contributions to Social Security. Similar to the Thrift Savings Plan, contributions would be collected and managed by SSA but passed on to private managers.

⁶ See Table 4 for current income limits for receiving the Saver’s Credit.

The current design of the Saver’s Credit limits its effectiveness as a government match program for state retirement initiatives (Table 5). Additionally, because the credit is non-refundable, it provides the least benefit for households with the lowest wages. Proposals to redesign the credit by making it refundable, smoothing the phase-out structure, and expanding eligible income brackets – such as the Encouraging Americans to Save Act of 2021 – could considerably enhance state retirement initiatives by encouraging participation via a lower opt-out rate and increasing the money going into the plans (Table 6).

Conclusion

In summary, the percentage of workers with retirement coverage has remained persistently flat over the last few decades and lower-wage, Black, and Hispanic workers are less likely to have coverage. Over time, these disparities have resulted in large gaps in retirement asset accumulation across income and racial/ethnic groups.

At the same time, a number of factors may also result in the need for more retirement income than in the past. Longer life-expectancies mean people are living longer in retirement. At the same time, increases in the Full Retirement Age from 65 to 67 mean that Social Security will replace less of pre-retirement earnings. Medicare premiums are also projected to take a larger share of their benefits⁷ and more people are slated to pay taxes on a portion of their benefits.⁸

The need for broader coverage and incentives to encourage savings among low and moderate wage workers is crucial. The most realistic option for enhancing coverage is to expand the auto-IRA program. While there are many other proposals that are perhaps more sophisticated and could potentially also bolster retirement savings, the auto-IRA program is already running and increasing the participation of uncovered workers. To further incentivize savings, an expanded auto-IRA program could be combined with a refundable Saver’s Credit to increase the retirement accumulations of uncovered workers.

Thank you again for this opportunity to speak before you.

⁷ The Medicare actuaries project Medicare out-of-pocket costs to increase from about 16 percent of average Social Security benefits in 2017 to over 30 percent of benefits by 2045 (Centers for Medicare & Medicaid Services, 2017)

⁸ Ellis, Munnell, and Eschtruth (2014).

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Table 1. *Percentage of Workers Ages 25-64 in the Bottom Income Tercile, By Race/Ethnicity and Gender*

	Percent
White	31%
Black	38
Hispanic	39
Asian	32
Male	26
Female	41

Source: CRR analysis from U.S. Census Bureau, *Current Population Survey* (2020).

Table 2. *Federal Policies Enacted to Address the Coverage Gap Since 1975*

Year	Policy	Type
1978-	SEP IRA	Simplified plan
1996-	SIMPLE IRA	Simplified plan
2001-	Small business tax credit	Tax credits to start a plan
2014-2017	myRA	Starter account
2019-	SECURE Act	Expanded use of multiple employer plans (MEPs)

Source: CRR analysis.

Table 3. *Types of State Initiatives, by Account Type and Employer Mandate*

Employer participation	Account type	
	IRA	401(k)
Voluntary	Voluntary Auto-IRAs (NM and NY)	Retirement marketplaces (NM, WA) Multiple Employer Plans (MA and VT)
Mandatory	Mandatory Auto-IRAs (CA, CO, CT, IL, ME, MD*, NJ, OR, VA)	--

*Maryland's legislation requires employers without a plan to auto-enroll their employees, but imposes no penalties for failing to do so. Instead, it allows participating employers to avoid the annual \$300 filing fee that ordinarily applies to businesses in Maryland.

Source: CRR analysis.

Table 4. *Adjusted Gross Income Limits for Saver’s Credit, 2021*

Credit	Married couples	Heads of household	Single individuals
50%	\$39,500 or less	\$29,625 or less	\$19,750 or less
20%	39,501-43,000	29,626-32,250	19,751-21,500
10%	43,001-66,000	32,251-49,500	21,500-33,000

Source: IRS Form 8880 (2021).

Table 5. *Saver’s Credits in Theory and Practice for U.S. Workers Not Offered an Employer-Sponsored Pension, 2019*

Income quartile	6% contribution	Average credit rate	Credit rate		Match rate	
			Theory	Practice	Theory	Practice
Lowest	\$611	0.33	219	76	36%	12%
2 nd	1,682	0.14	216	79	13	5
3 rd	2,860	0.02	57	12	2	0
Highest	5,223	0.00	1	0	0	0

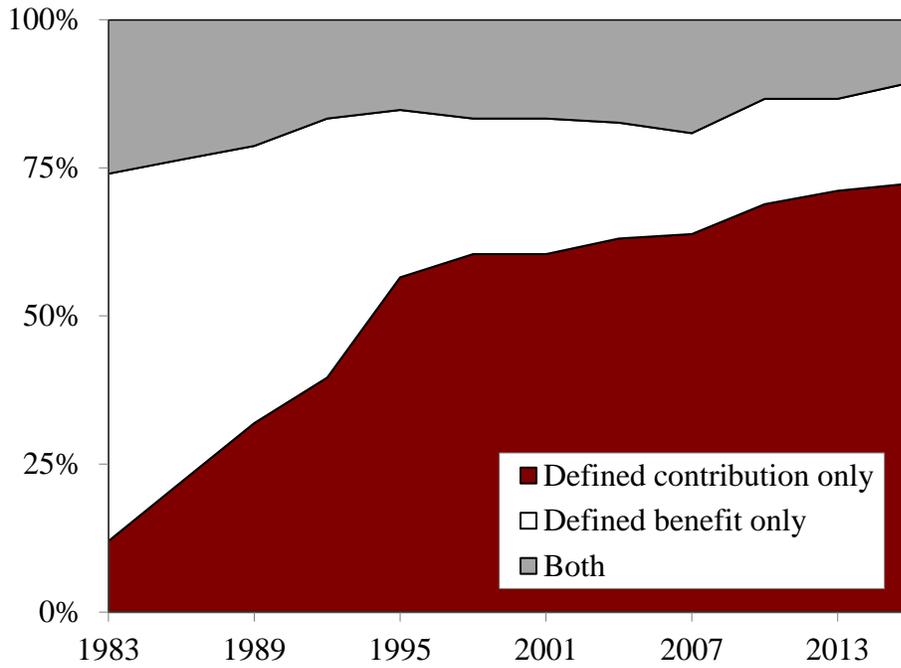
Source: CRR analysis.

Table 6. *Saver’s Credit and Match Rates under Current Law and Encouraging Americans to Save Act for U.S. Workers Not Offered an Employer-Sponsored Pension, 2019*

Income quartile	Credit amount		Match rate	
	Current law	Encouraging Americans to Save Act	Current law	Encouraging Americans to Save Act
Lowest	\$76	\$274	12%	45%
2 nd	79	682	5	41
3 rd	12	302	0	11
Highest	0	40	0	1

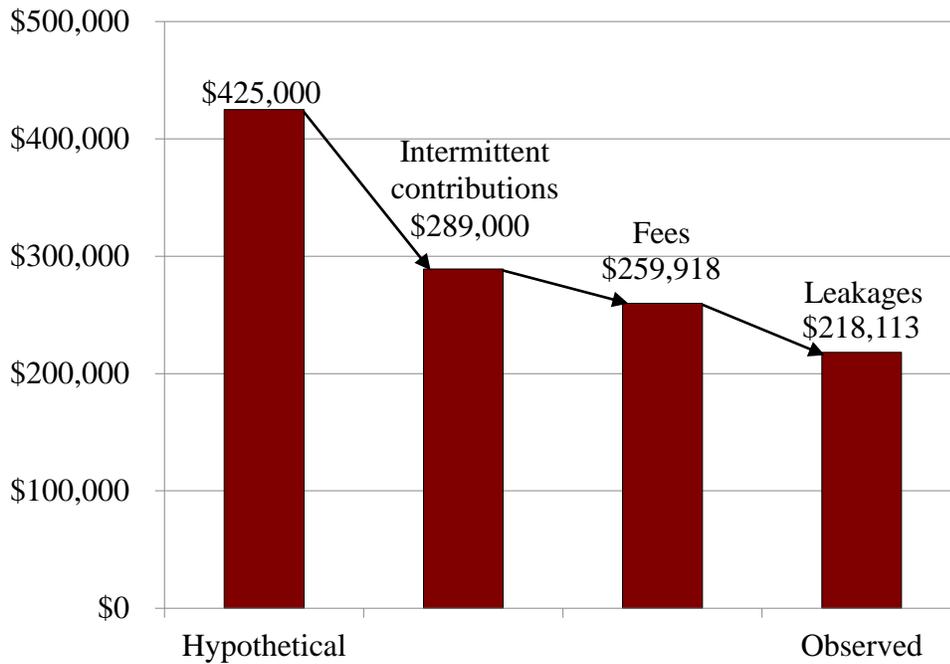
Source: CRR analysis.

Figure 1. *Workers with Pension Coverage by Type of Plan, 1983-2019*



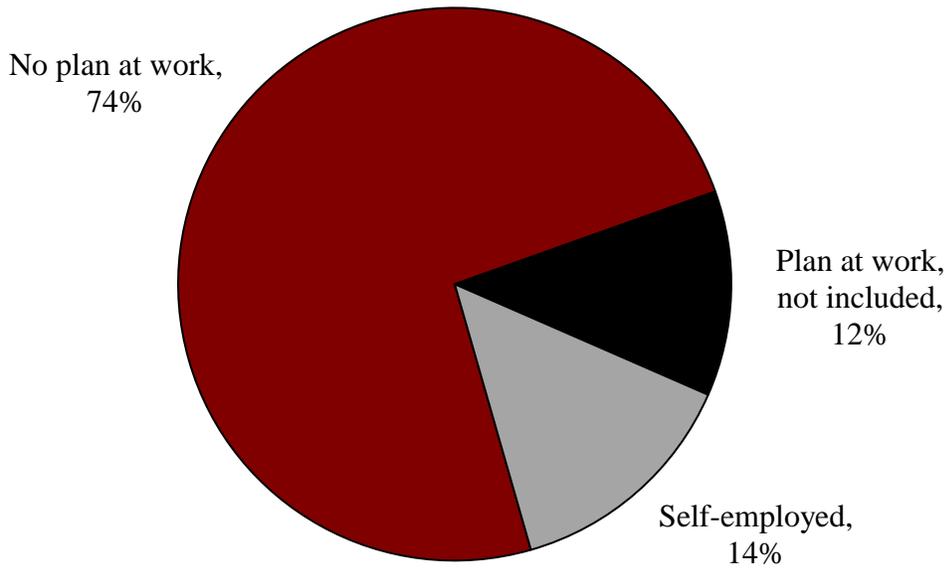
Sources: Authors' calculations based on U.S. Board of Governors of the Federal Reserve System, *Survey of Consumer Finances* (1983-2019).

Figure 2. *Impact of Contributions, Fees, and Leakages on 401(k)/IRA Balances, 2019*



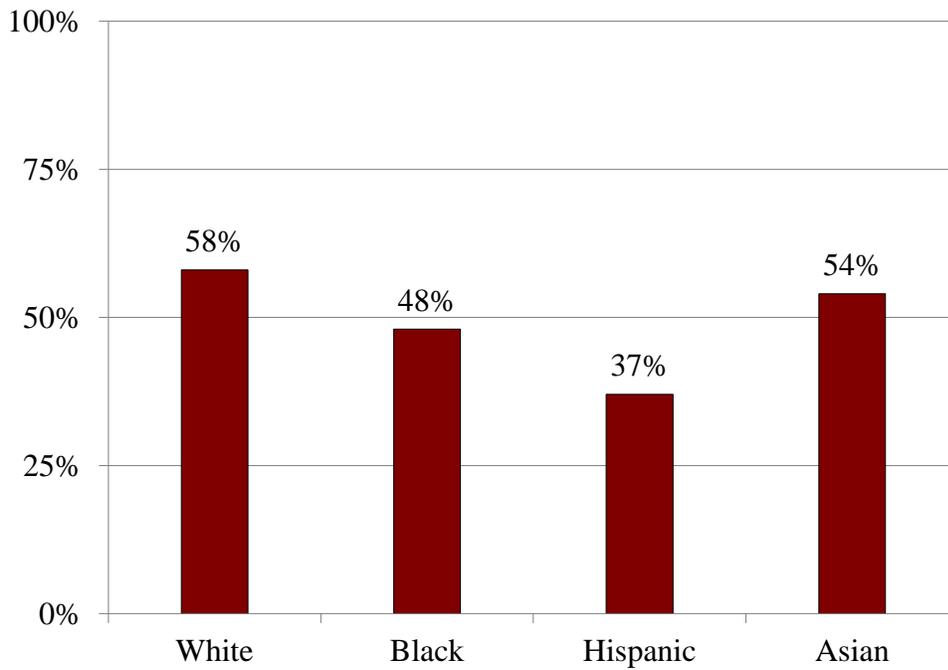
Source: Authors' estimates based on Biggs, Munnell, and Chen (2019).

Figure 3. *Uncovered Workers by Reason Uncovered, 2018*



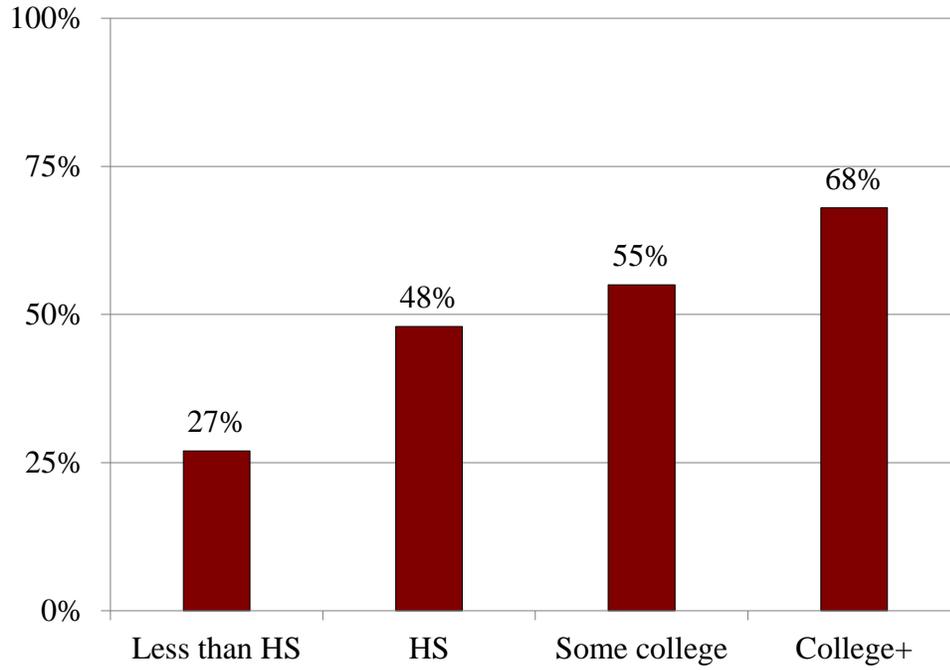
Source: CRR calculations from U.S. Census Bureau, *Current Population Survey* (2019).

Figure 4. *Percent of Working Years with Workplace Retirement Plan Coverage for Workers 25-64, by Race*



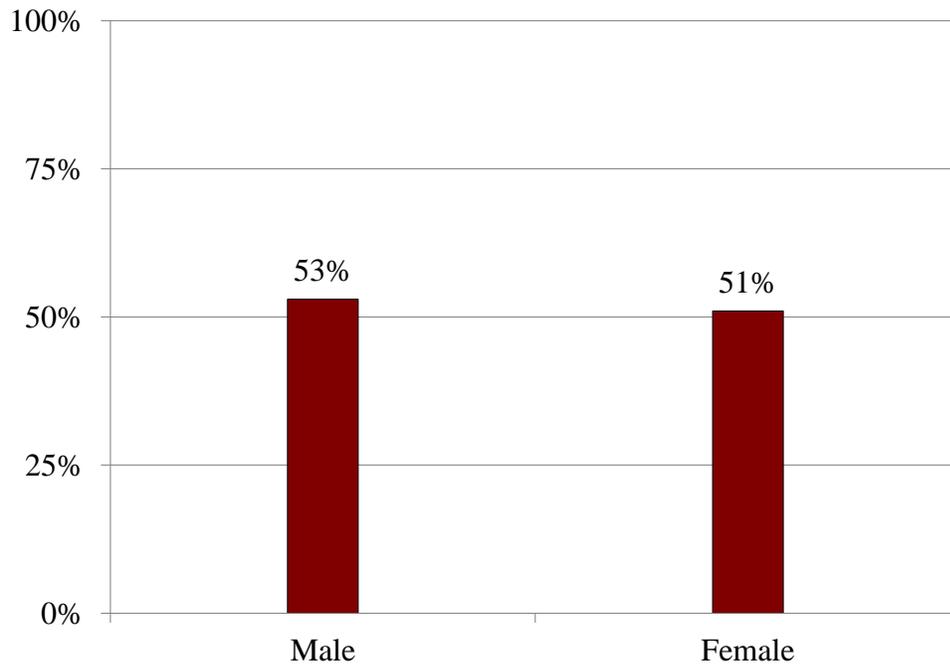
Source: CRR calculations from the *Panel Study of Income Dynamics* (2019).

Figure 5. *Percent of Working Years with Workplace Retirement Plan Coverage for Workers 25-64, by Education*



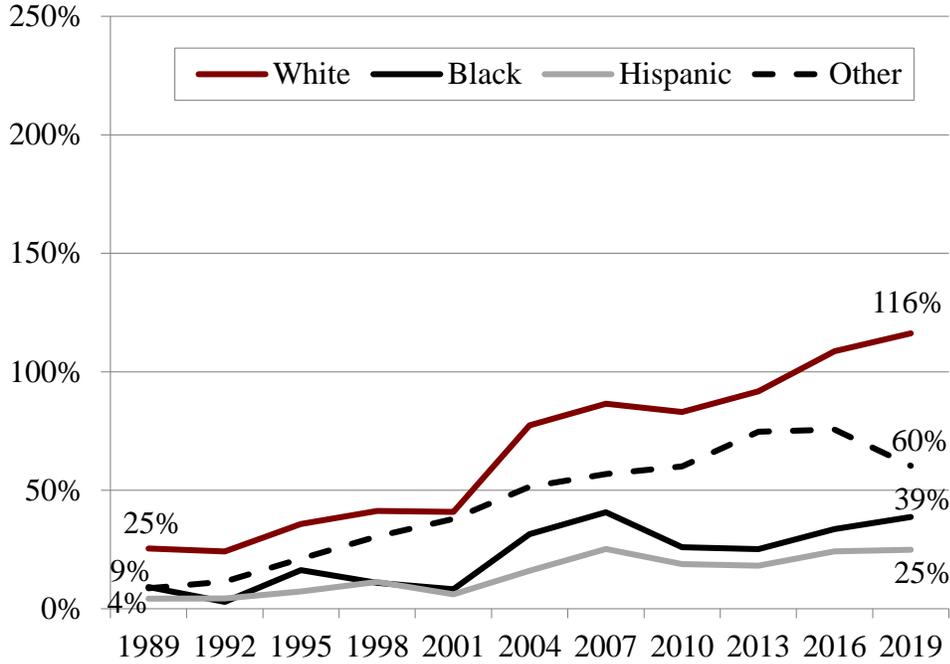
Source: CRR calculations from the *Panel Study of Income Dynamics* (2019).

Figure 6. *Percent of Working Years with Workplace Retirement Plan Coverage for Workers 25-64, by Gender*



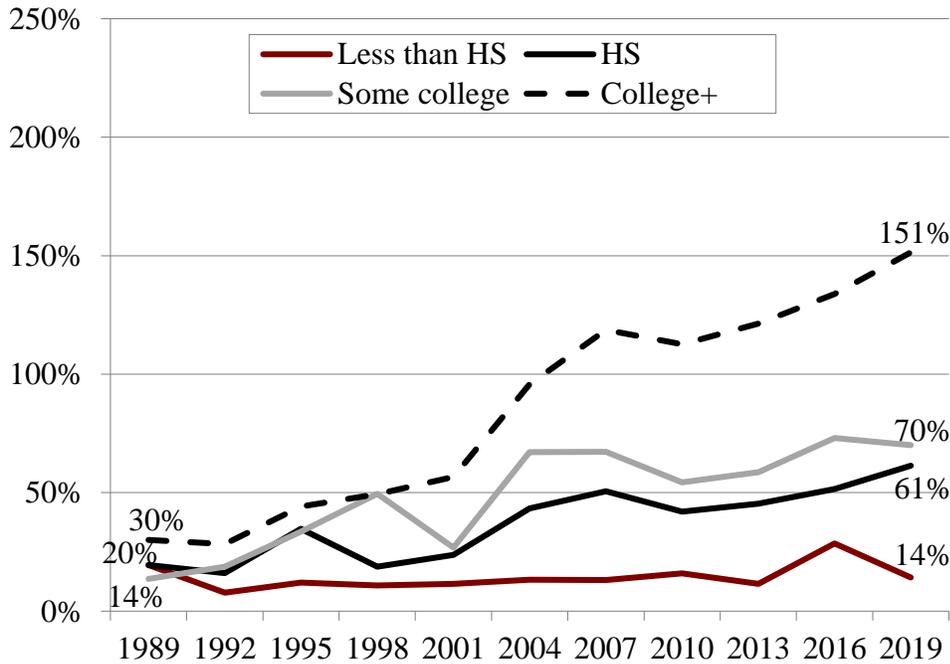
Source: CRR calculations from the *Panel Study of Income Dynamics* (2019).

Figure 7. 401(k)/IRA Assets as a Percent of Income for Workers Ages 25-64, by Race/Ethnicity, 1989-2019



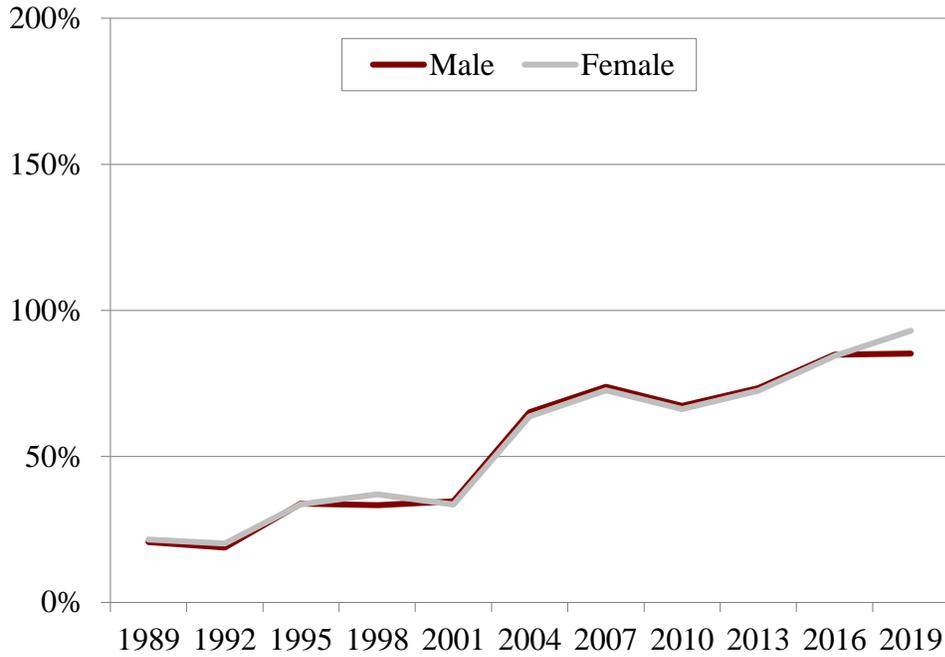
Source: CRR calculations from the Survey of Consumer Finances (1989-2019).

Figure 8. 401(k)/IRA Assets as a Percent of Income for Workers Ages 25-64, by Education, 1989-2019



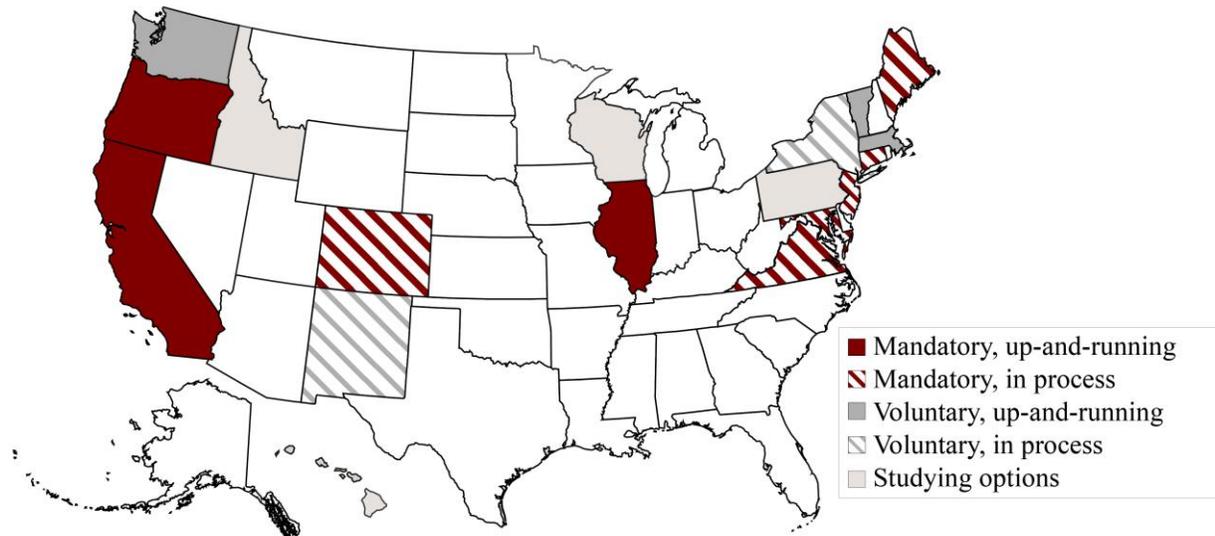
Source: CRR calculations from the Survey of Consumer Finances (1989-2019).

Figure 9. 401(k)/IRA Assets as a Percent of Income for Workers Ages 25-64, by Gender, 1989-2019



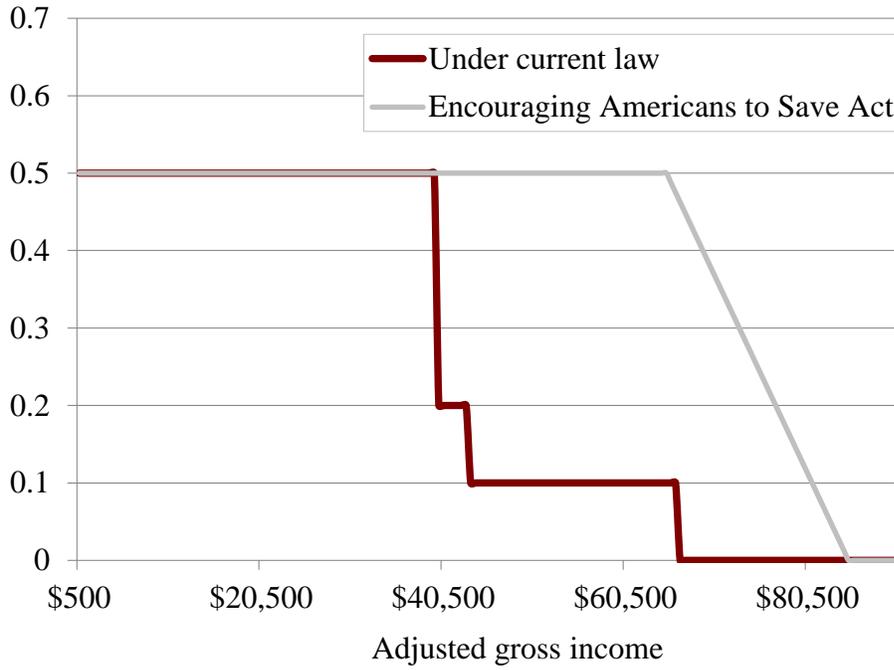
Source: CRR calculations from the Survey of Consumer Finances (1989-2019).

Figure 10. State Initiatives to Address the Coverage Gap, as of July 2021



Source: CRR analysis.

Figure 11. *Saver's Credit Rate under Current Law, Encouraging Americans to Save Act, and Retirement Security and Savings Act, for those Married Filing Jointly, 2019*



Source: Authors' calculations.