How Have Workers Responded to Oregon’s Auto-IRAs?

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Introduction

Only about half of private sector workers are covered by employer-sponsored retirement savings plans at any given time, and few workers save without them. The net result is that a third of households end up relying almost exclusively on income from Social Security in retirement. In the absence of federal action to close the coverage gap, some states have passed legislation to implement so-called “Auto-IRAs,” which expand coverage by requiring employers who do not offer a retirement plan to automatically enroll their workers into an IRA-based saving program. Workers enrolled in the programs would be able to opt-out, change how much they save and how they invest, and make withdrawals. The recent launch of OregonSaves – Oregon’s Auto-IRA program – is providing data that allow an early glance at how workers respond to these kinds of programs. This brief offers a first look at those data.

Background

The goal of OregonSaves is to provide over 500,000 workers – most of whom work for small employers – with access to a Roth IRA-based saving program. The design of OregonSaves is modeled after the best practices of 401(k)s – a relatively high default contribution rate, automatic escalation, and a low-fee default investment vehicle that ultimately contains some equities. The default deferral – 5 percent of pay with automatic increases by 1 percent per year until reaching 10 percent – would ensure that a 25-year old participating continuously in the program would have enough to retire at age 67 with an 80-percent replacement rate. To make sure people who opt out after 30 days (and therefore made some contributions) can get all of their money back, the first $1,000 in deferrals are invested in a capital preservation fund, with additional deferrals invested in an age-based target date fund.

The question is: how do workers actually respond to these design features? To date, researchers have had to either assume uncovered workers would respond like workers with access to a 401(k) or use surveys to inquire about how they might respond. Yet, the workers being enrolled in Auto-IRAs differ in key ways from workers covered by 401(k)s – they are more mobile, lower income, and more likely to be under financial stress – and surveys can only

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1 For example, see Munnell and Chen (2016).
2 Dushi, Iams, and Trenkamp (2017). Data from the 2013 Survey of Consumer Finances confirm that almost a third of Americans have no retirement savings and are not covered by a defined benefit pension. Among respondents ages 55-64, 19 percent report having no retirement savings or pension outside of Social Security (Miller, Madland, and Weller, 2015).
3 This replacement rate estimate includes Social Security as well as income from the Auto-IRA program and assumes a 4-percent drawdown rate and a 4-percent real return on investments.
go so far. Yet, the degree to which OregonSaves improves retirement security among uncovered workers depends on workers participating and maintaining default contributions and investments. Fortunately, initial OregonSaves data allow a first look at how previously uncovered workers behave when they obtain access to an employer-based plan.

Data

This brief uses OregonSaves administrative data on employees working for employers that registered for the program between July 2017 and June 21, 2018. Specifically, the data available at the time of this brief include employee status at their employer (i.e., active versus inactive), opt-out status, and – for those who have saved through the program – asset balances and allocation as of June 21, 2018. These data are only a first glance at what will eventually be available to researchers – future data will be updated each day allowing a look at longitudinal behavior like whether workers continue participation as they move from job-to-job or how likely they are likely to withdraw money from their accounts. The future data will also include many more variables, like worker age and a measure of earnings. But the existing data provide a valuable first glance at workers’ initial behavior. The sample used for the analysis consists of 35,139 people who were: 1) active employees who had passed the opt-out window; or 2) active employees who had opted out.

Results

Perhaps the most important variable in program success is participation. While a precise opt-out rate is difficult to calculate with the current snapshot of data, the initial look suggests that 32 percent of workers chose to opt out of the program during their initial 30 days and an additional 4 percent changed their contribution rate to 0 later on. This effective opt-out rate of 36 percent is higher than estimates based on the survey responses of uncovered workers mentioned above, which had ranged from 20-30 percent, but still suggests a majority of workers participate. Of workers who have not opted out, 33 percent are actively contributing and 31 percent are ready to make contributions but no money has yet been placed into their accounts (see Figure 1), likely because they have not been paid since they passed their 30-day opt-out window or because payroll is still being set up by their employer. Given the fact that many new employers are enrolling each month, the size of this group is not surprising.
When opting out, participants were asked to give a reason, and workers gave three main explanations. Twenty-seven percent said they could not afford to save, 19 percent said they had their own or other retirement plan, and around 10 percent said they did not want to save through this particular employer, perhaps because they did not expect the relationship to last long.

It is also important for program success that workers stick with the default contribution rate, which is designed to be high enough for significant assets to accrue by retirement. As of June 21, 83 percent of participants had not changed their default deferral rate of 5 percent. Of the remaining 17 percent who had made a change, 16 percent had decreased their deferral rate and 1 percent had increased their rate – usually to 10 percent (see Figure 2). The stickiness of the default mirrors participant behavior in 401(k) plans.
Figure 2. Deferral Rate among Participants who had Not Opted Out

<table>
<thead>
<tr>
<th>Deferral Rate (%)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 percent</td>
<td>3.8%</td>
</tr>
<tr>
<td>1 - 4 percent</td>
<td>11.6%</td>
</tr>
<tr>
<td>5 percent</td>
<td>3.8%</td>
</tr>
<tr>
<td>&gt;5 percent</td>
<td>0%</td>
</tr>
</tbody>
</table>

Source: Authors’ calculations from administrative data.

It is also important for the long-term success of the program that workers keep their assets in a diversified mix of stocks and bonds and do not completely shy away from risk. Ultimately, Oregon defaults workers into a target date fund appropriate for someone their age that would satisfy this requirement, although based on the current data it is too early to say whether workers will maintain this default. The reason is that, so far, ninety percent of assets were invested in the capital preservation fund. Among the remaining 9 percent of assets, only 1 percent were invested outside of a target retirement fund. So while workers seem to be sticking with the program’s defaults, it is too early to say that this pattern will persist once workers have accrued enough assets to be switched to the target date fund.

Conclusion

Early results from OregonSaves answer some questions and suggest avenues for future research. First, the data suggest that the majority of workers will participate in the program, although initial opt out rates appear higher than were found in surveys of uncovered workers prior to program launch. Second, workers appear likely to behave like those in 401(k)s with respect to defaults – by and large they stick with default saving rates and investment options.
Oregon’s data and implementation experience also open up several avenues for further research. In the short term, payroll data and more detailed employer data will allow researchers to assess drivers of opt out at the individual and firm level. As the program matures, the program data will show the extent to which participants accumulate assets over time and whether they treat assets in the plan as a precautionary reserve or a retirement nest-egg. Over the long term, the data made available by the program will allow researchers to investigate the overall impact of auto-IRAs on household finances over a lifecycle. The data will ultimately offer other states a unique perspective on the factors related to the success of their programs, and will make it possible for researchers to investigate the extent to which such programs will actually affect retirement security.

References


