Vermont Voluntary Retirement Savings Program

13 June 2006

“Besides the personal implications for individual Americans who are likely to outlive their assets, the increasing national retirement income gap is expected to put heavy stress on state programs.”

- Employee Benefit Research Institute, “Americans' Future Retirement Security,” 2004

“Leveraging their resources and bargaining power, States can assist small businesses in pooling their efforts to help employees save. Vermont can act as a powerful catalyst, partnering with the private sector to expand private pension coverage.”

- Mark Iwry, Nonresident Senior Fellow, The Brookings Institution

The Need for Retirement Savings is Critical!

Half of America's private sector workforce is not covered by any retirement savings plan; their retirement will be anchored only by Social Security and whatever they have managed to save on their own (source: PBS, Frontline).

- **People are living longer.**

- **Social Security is not enough.**

- **People are not saving enough; the U.S. savings rate has steadily declined.**

- **This is an issue that affects all of us: Taxpayers will bear ultimate responsibility for seniors with insufficient savings.**

Retirement Costs Are Up and Will Continue to Rise

- **Longevity**
  - "The driving force behind the growing cost of retirement is the fact that the baby boomers will spend more time in retirement than any previous generation. According to the Center for Disease Control, a 65-year-old can now expect to live another 18 years, on average. American seniors are living 50 percent longer than they were in the 1930s, when Social Security set 65 as the benchmark retirement age."
- **Health Care Costs**
  - Costs are rising.
  - The number of companies offering retiree health care benefits is declining.
  - Long-term Care.
- **Inflation**
  - At current rates, the average retiree can expect the purchasing power of his/her retirement savings to be cut in half during their retirement years.
- **At the same time… Public Systems Safety Nets are facing their own pressures**
  - Medicare
  - Social Security

Source: Catherine Rentz Pernot , PBS, Frontline: Why Does Retirement Cost So Much? 2006

The Retirement Savings Gap

- **If current patterns continue, there will be an annual shortfall of as much as $57 billion by 2030 between the amount retired Americans need to cover basic expenses and what they have.**

-EBRI Issue Brief , “Americans' Future Retirement Security,” 2004

- **“… about a quarter of baby-boomer households have so far failed to accumulate significant savings. They appear likely to depend entirely on government benefits in retirement.”**

  – Congressional Budget Office, “The Retirement prospects of the Baby Boomers,” 2004

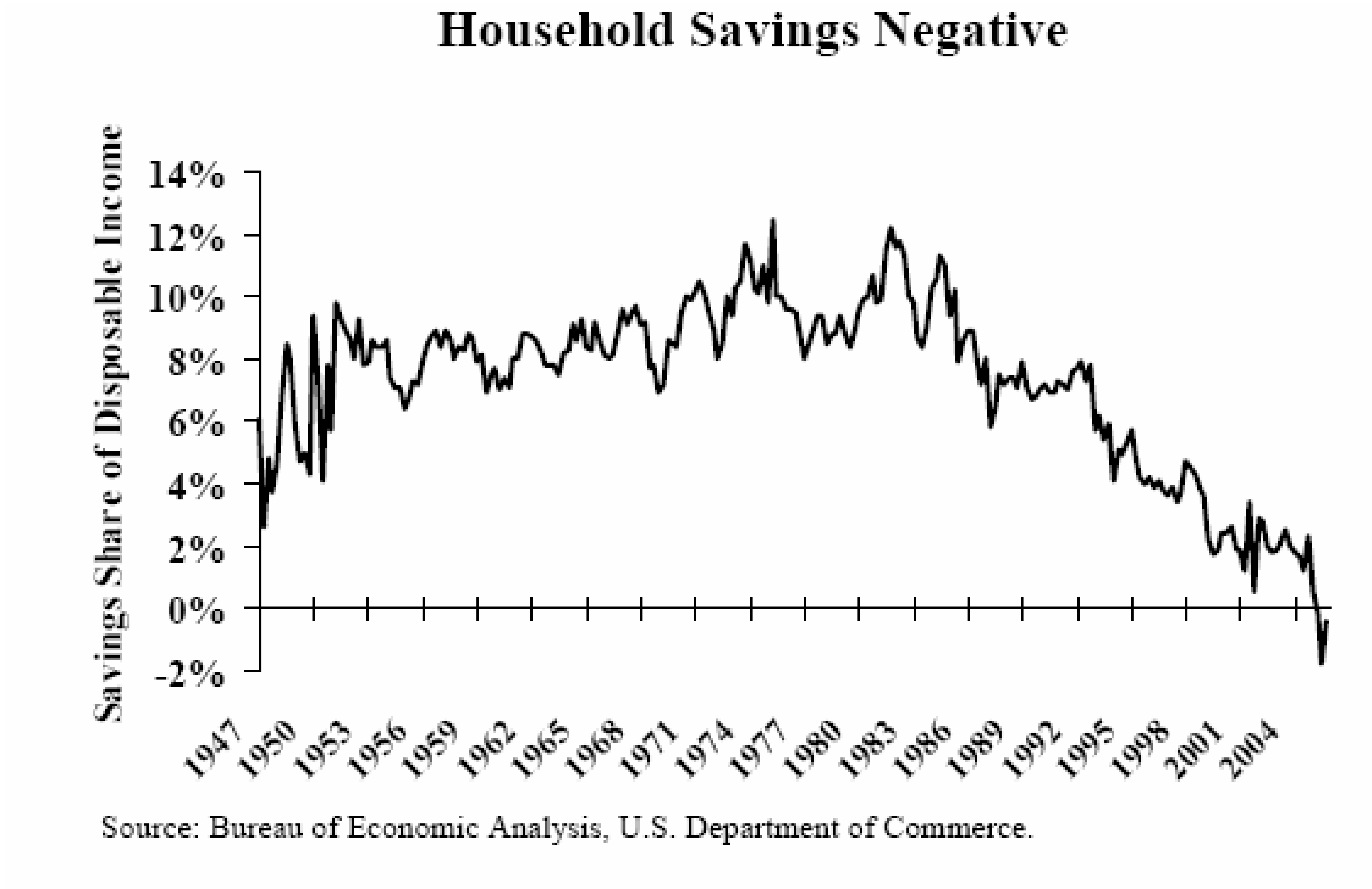
Inadequate Retirement Savings

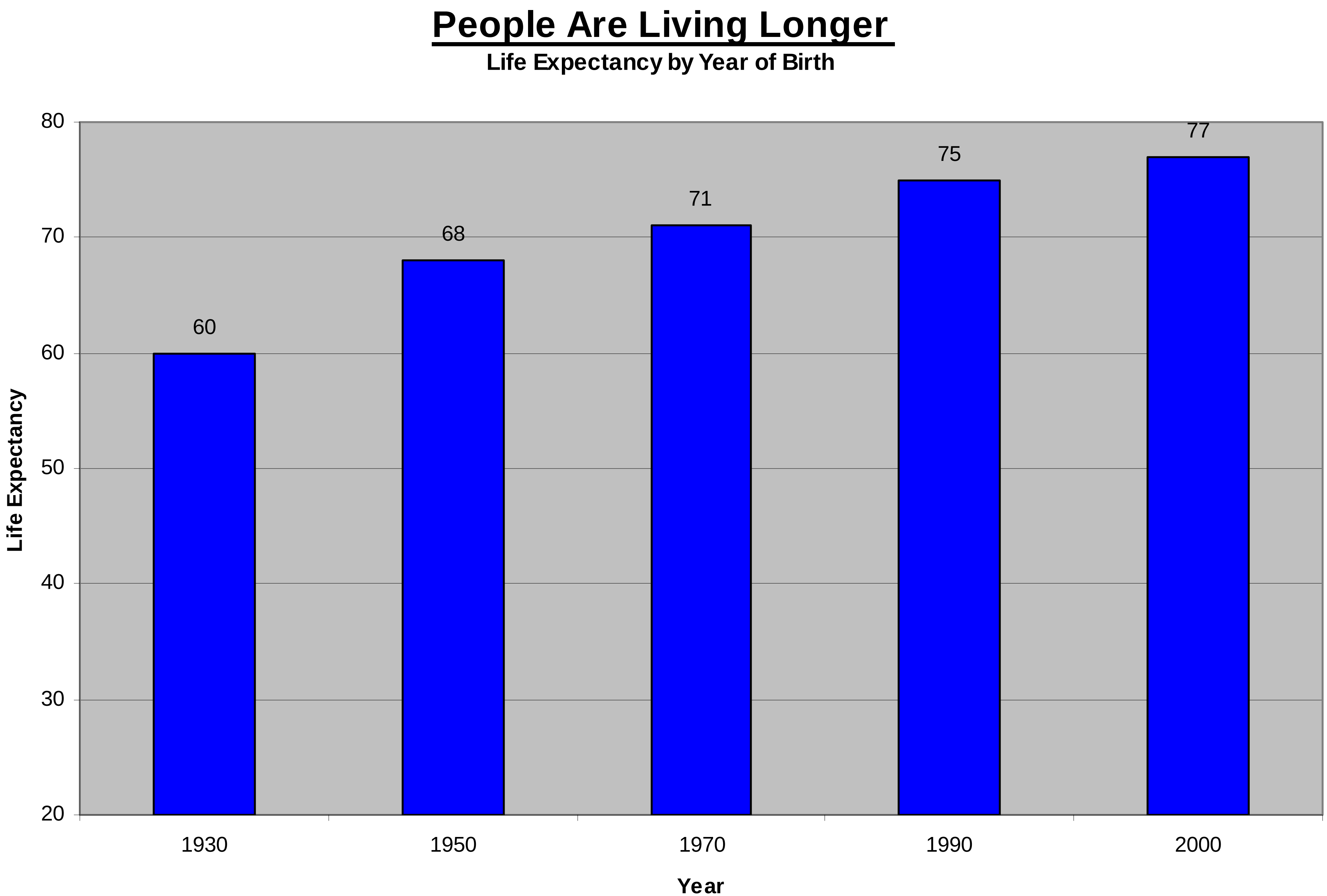
- The Commerce Department reported in January 2006 that the U.S. savings rate is now the lowest since the Great Depression. Americans' personal savings fell into negative territory at -0.5% in 2005, the first time since 1933.

- This means they had to dip into previous savings or have run up higher levels of debt.

- One-quarter of current retirees rely totally on Social Security for their income, and have no outside resources. Two-thirds rely primarily on Social Security for the income.

- Roughly one-third of the elderly (those age 65 or older) received a work-related pension in 2004.

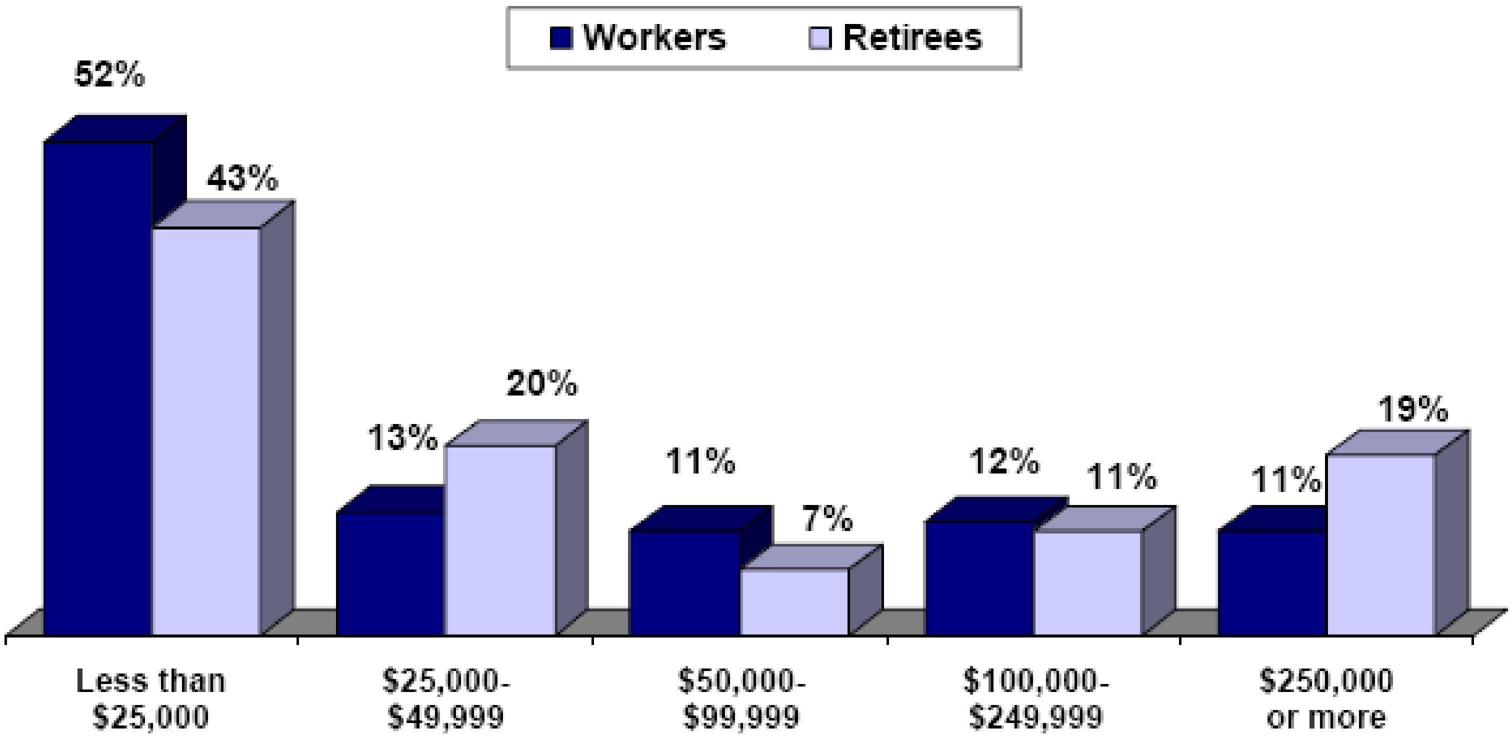

Household Savings Negative
Savings Share of Disposable Income
14%
12%
10%
8%
6%
4%
2%
0%
-2%
1947
1950
1953
1956
1959
1962
1965
1968
1971
1974
1977
1980
1983
1986
1989
1992
1995
1998
2001
2004
Source: Bureau of Economic Analysis, U.S. Department of Commerce.


People Are Living Longer
Life Expectancy by Year of Birth
Life Expectancy
Year
80
70
60
50
40
30
20
60
68
71
75
77
1930
1950
1970
1990
2000

Survey Results:

Most Workers and Retirees Have Little in Savings

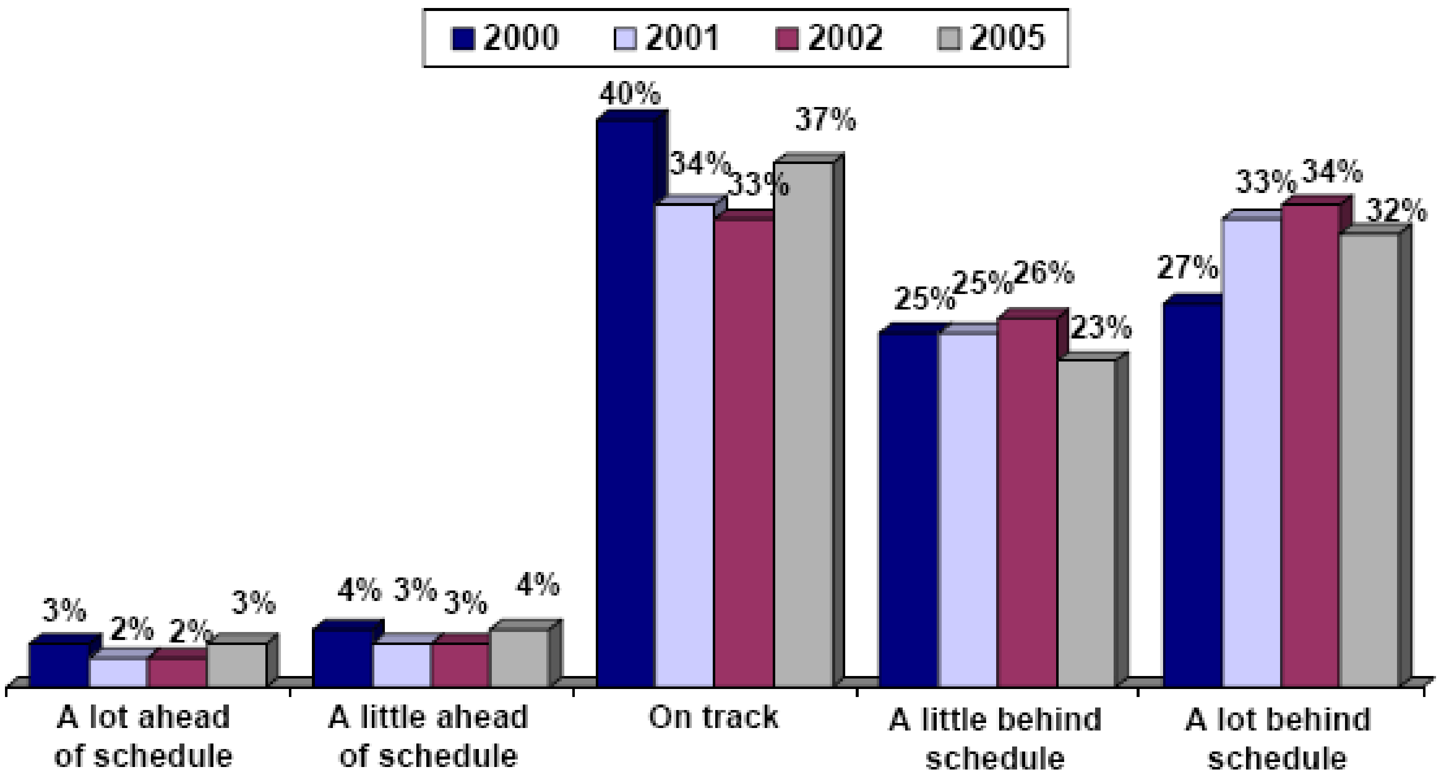
In total, about how much money would you say you currently have in savings and investments, not including the value of your primary residence? Please include savings, certificates of deposit, stocks, bonds, mutual funds, workplace retirement plans, and other investments (Workers responding n=818; Retirees responding n=190)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

More Than Half of Workers Feel They Are Behind Schedule

When it comes to planning and saving for retirement, would you say you are on track, ahead of schedule, or behind schedule? (Workers n=1,001)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

Some Workers Who Are *Very Confident* About Their Retirement Security May Be *Over*confident

- On average, it appears that confidence about retirement security is related to financial preparation.
- However, even among *very* confident workers, some may be overconfident:
  - 20% of very confident workers are not currently saving for retirement.
  - 38% have less than $50,000 in savings.
  - 52% do not have an IRA opened with money saved outside of an employer's retirement plan.
  - 37% have not done a retirement needs calculation.
  - 35% say their current level of debt is a problem.

Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

In response to inadequate accumulation of savings, many workers plan to retire later in life than they originally planned. Others plan to supplement their income during retirement. The facts indicate this is often an unrealistic plan.

- **Four out of 10 retired workers left their jobs <u>sooner than they had planned</u>, usually because of health problems or the loss of employment, according to the report by McKinsey & Co.**

- **The survey also found that 45% of people who are currently employed planned to keep working past age 65. But among the retirees polled, only 13% said they had done so.**

- **According to study, among those who were forced to retire early:**
  - **47% - Health reasons**
  - **44% - Job loss**
  - **9% - To care for an ailing family member.**

- **"Our research clearly shows that many people — and more than a few public policymakers — who are betting on simply working longer to compensate for a lack of current savings are setting themselves up for a rude awakening and a significantly poorer standard of living in retirement than they had expected."**
  - David Hunt, senior partner, McKinsey & Co.

Source : Los Angeles Times, May 15, 2006

As Baby Boomers Retire, the Problem Will Get Worse

- I think this is a crisis in the making… I think 10 or 15 years from now, people who approach their early sixties are simply not going to have enough money to retire on.“
  - Professor Alicia Munnell, director of the Boston College Center for Retirement Research

- "I would say, unless you're fortunate to be in the upper-income quartiles, that you're probably going to be in for a very rough ride, … You're not going to have sufficient monies to pay the predictable expenses -- your housing, your utilities, your food -- plus the potential catastrophic medical care costs.“
  - Jack VanDerhei , Temple University and the Employee Benefit Research Institute

Retirement Crisis Has Larger Economic Consequences….

- As retirees make up a greater percentage of the population, their personal economic situations will have long-term impacts on the larger economy.

- Could adversely impact investment, productivity, and wages for continued economic growth.

- “What holds up our economy ... is consumer spending. When retirees are 20 percent of the economy and run out of money, then -- poof -- there goes the economy.”

- Brooks Hamilton, Benefits Consultant, Brooks Hamilton & Partners in PBS, BABY BOOMERS FACE RETIREMENT CRISIS AS LIFETIME PENSIONS WITHER AND 401(k)s FALTER, May 16, 2006.

….**Resulting in Increased Pressure on Social Security and Medicare**

- Just by their numbers, the retirement of boomers will place additional burdens on the Social Security and Medicare systems.

- To the extent that savings and other retirement plans are not available, many retirees will need to rely on other forms of government assistance, creating more tax burdens at the federal and state level.

- As a matter of good public policy, it makes sense to develop alternatives that encourage savings for retirement.

- Saving through the workplace assists future retirees in meeting their future income needs.

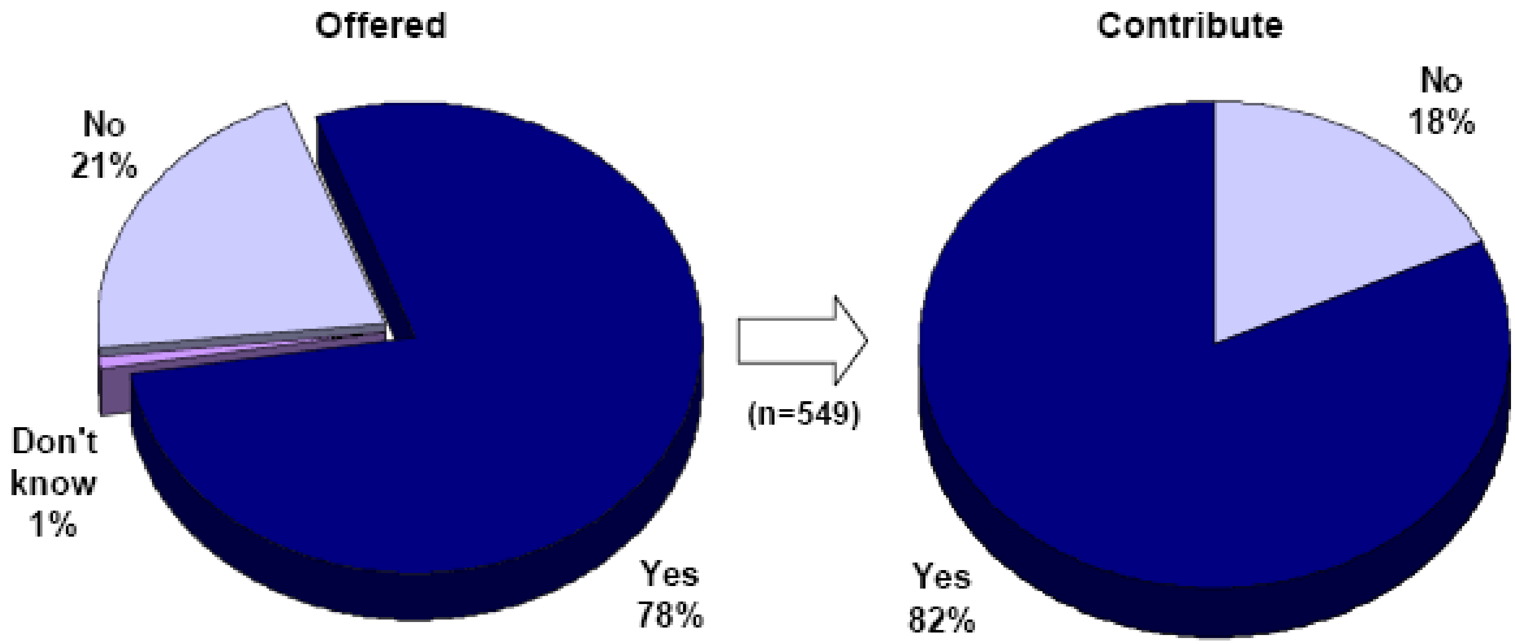
Employees are more likely to save through the workplace than on their own.

- **Eight in 10 eligible employees participate in a workplace savings plan.**

- **Just 4 in 10 have an IRA.**

8 in 10 of Those Offered a Retirement Savings Plan at Work Say They Participate

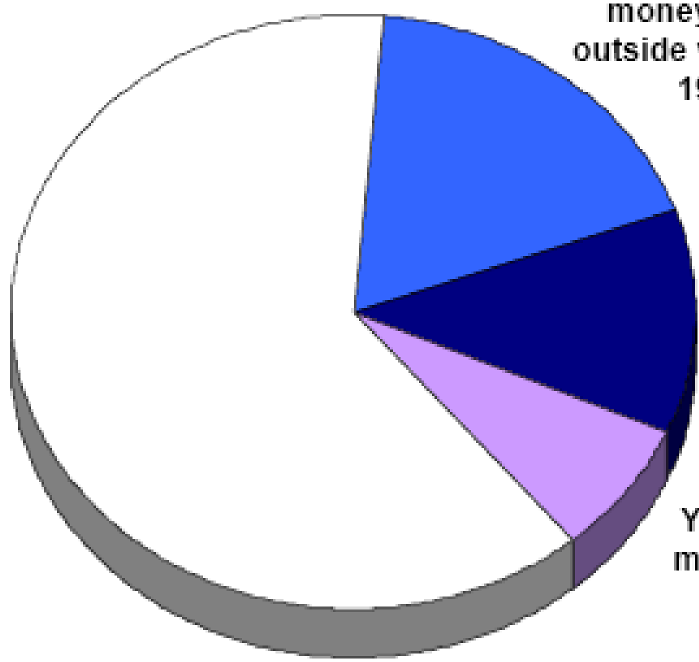
Does your current employer offer you a retirement savings plan that allows you to make contributions from your salary to an individual account set up in your name, such as a 401(k), 403(b), or 457 plan? If yes, do you contribute to the plan? (Workers employed full or part time, n=683)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

Less Than 4 in 10 Workers Have an IRA; Just 3 in 10 Have One Opened With Money Saved Outside a Work Plan

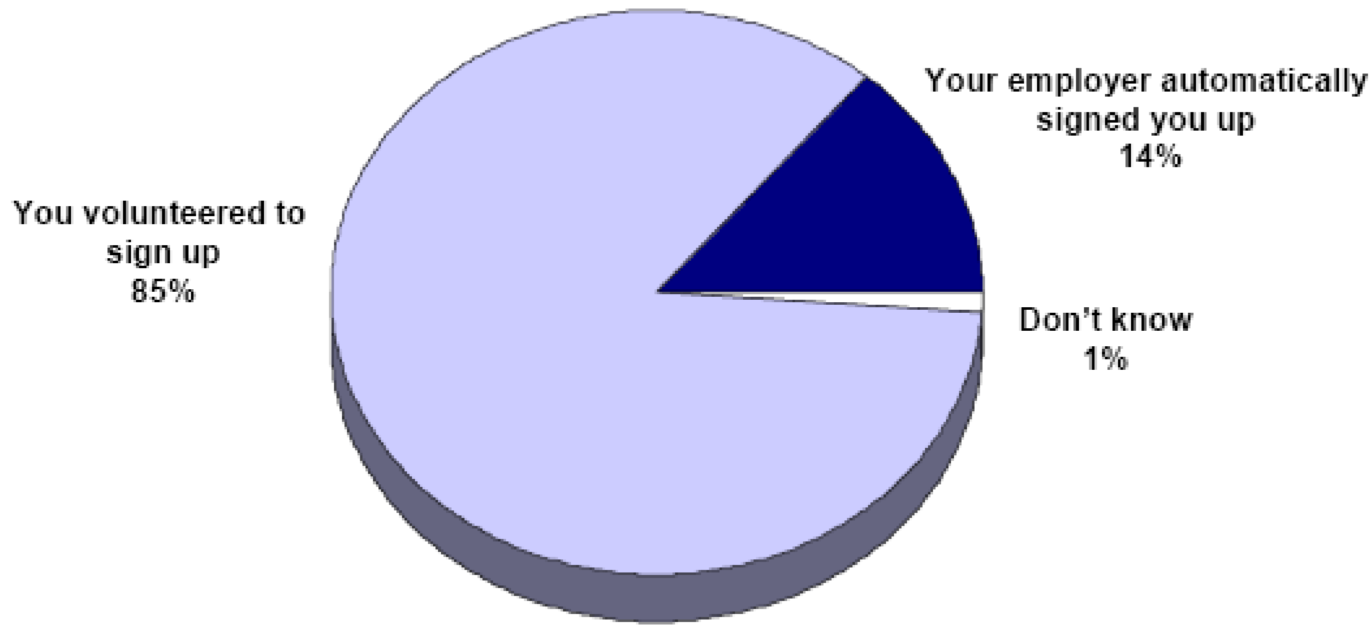
Do you (and/or your spouse) currently have an IRA that you (opened with money rolled over from an employer's retirement plan/opened with money saved outside of an employer's retirement plan)? (Workers n=1.001)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

The Large Majority of Participants Volunteered to Sign Up for Their Employer's Retirement Plan

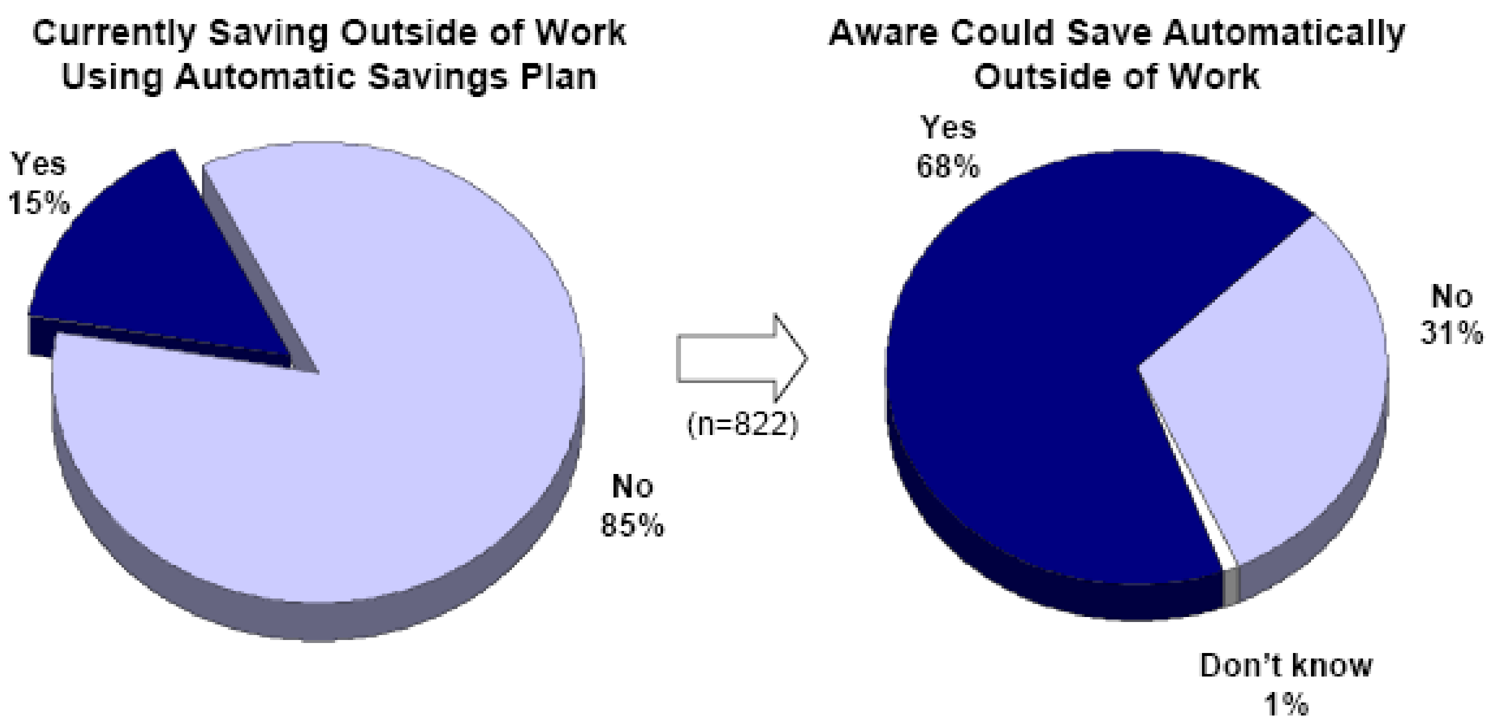
When you were enrolled in your employer's retirement plan, did your employer automatically sign you up, allowing you to discontinue participation, or did you volunteer to sign up? (Workers participating in a workplace savings plan, n=461)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

Very Few Workers Participate in Automatic Savings Arrangements Outside of Work, but Most Know of Them

Are you currently saving for retirement outside of work using an automatic arrangement like this? (Workers n=1,001) Before today, were you aware that you could save automatically for retirement in this way? (Workers not using an automatic savings plan, n=822)



Source: Employee Benefit Research Institute and Mathew Greenwald & Associates, 2005 Retirement Confidence Survey, Chart Book

Many small businesses don’t provide plans.

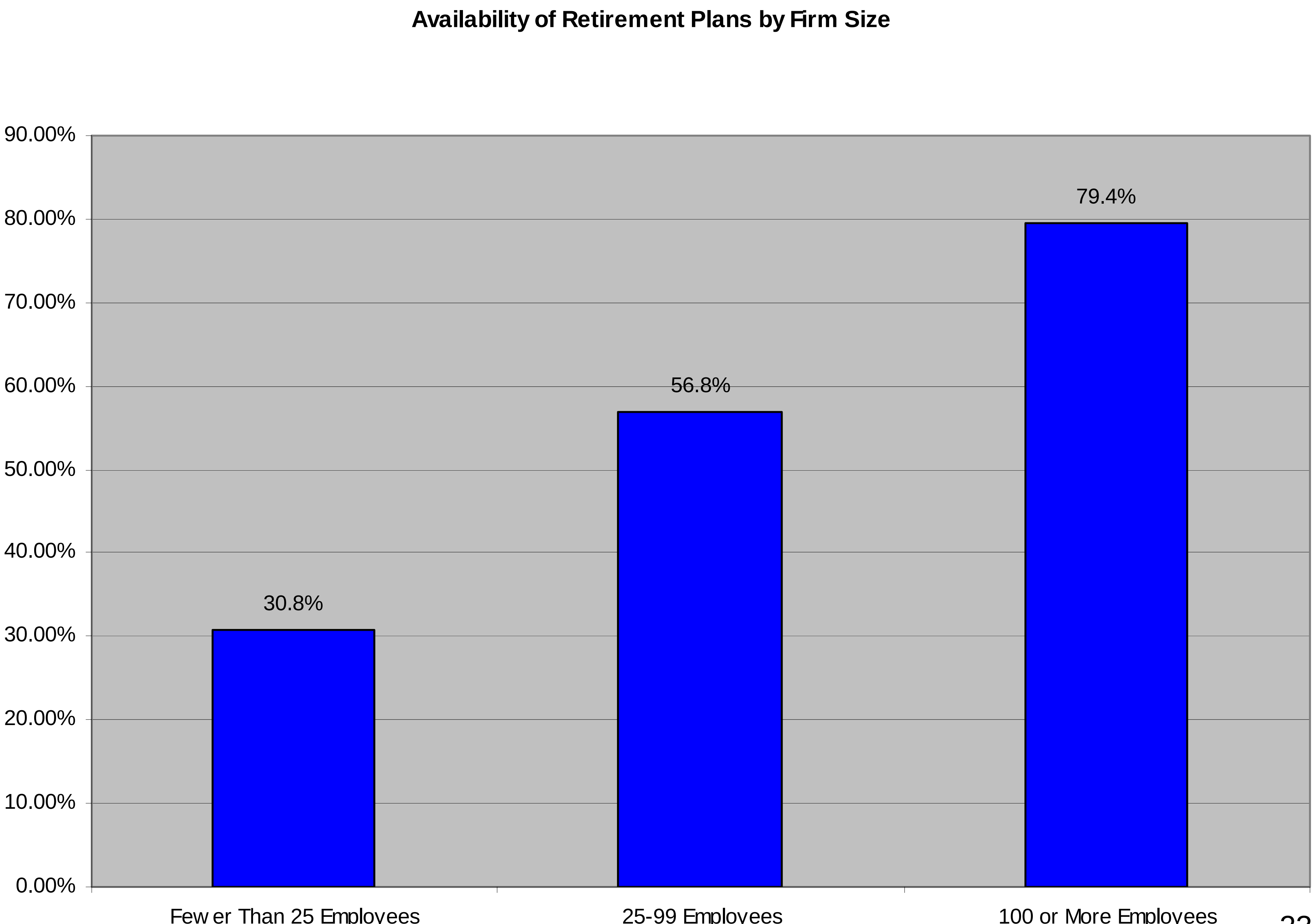
Many employees do not have access to employment based plans.

“A growing body of evidence suggests that low-income families will contribute to retirement accounts if they are presented with effective and transparent incentives to do so and have easy access to a savings vehicle.”

- Center on Budget and Policy Priorities, “Protecting Low-Income Families’ Savings,” June 2005

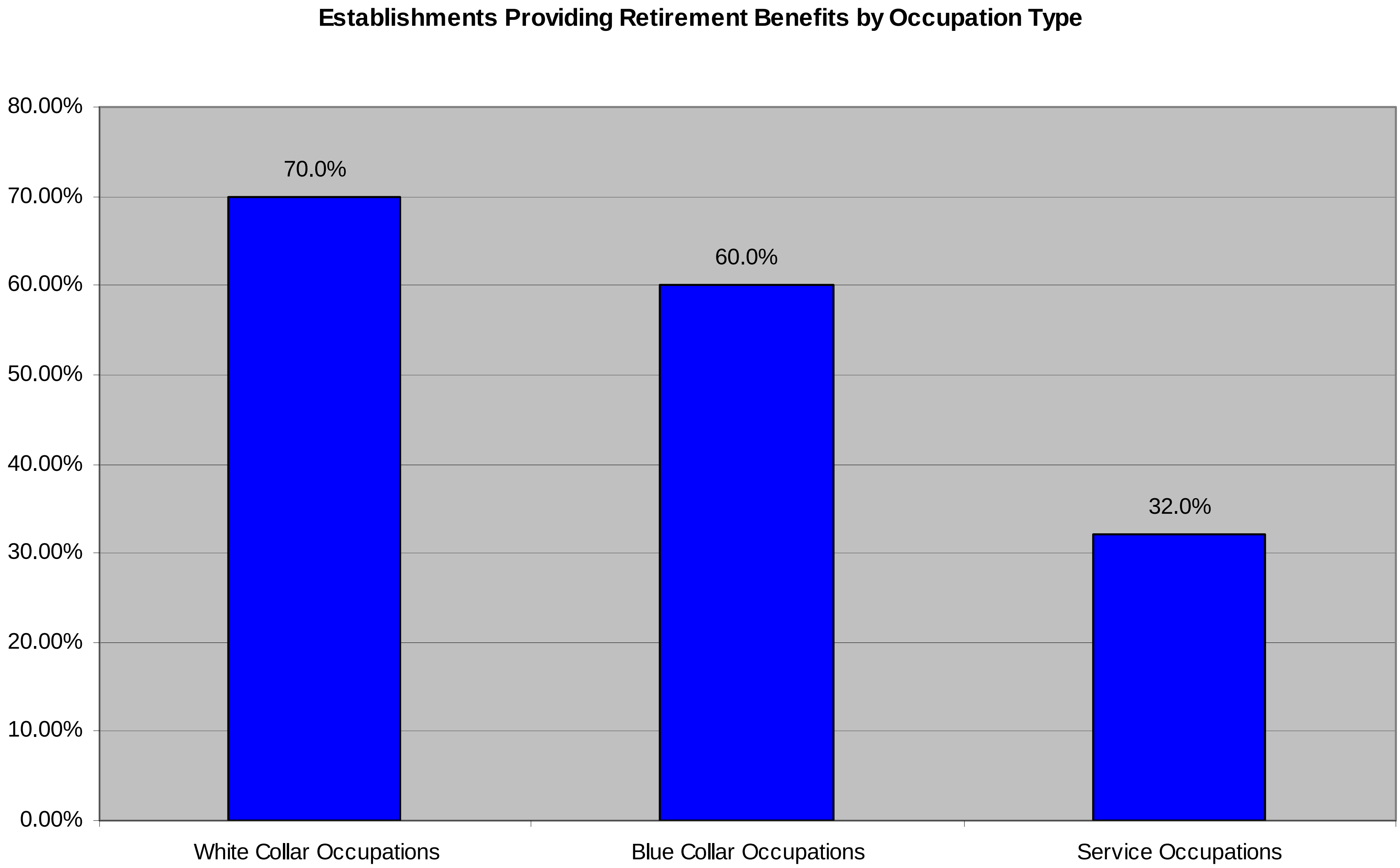
- **Approximately half of the workforce in the United States is not covered by an employer-sponsored retirement plan.**
- **82% of workers with annual incomes of less than $20,000 lack pension coverage.**
- **79% of part-time or seasonal workers do not have a pension.**

Many Employees Do Not Have Access to Employment-Based Plans



source: EBRI, January 2006

Many Employees Do Not Have Access to Employment-Based Plans



Plan Sponsorship Among Small Employers

Likelihood of Starting a Plan in the Next Two Years

	1998	1999	2000	2001	2002	2003
Very likely	17%	15%	16%	13%	10%	7%
Somewhat likely	25	24	23	25	22	22
Not too likely	24	24	29	28	25	25
Not at all likely	32	36	31	34	43	43

Just 7 percent of nonsponsors say it is *very* likely that their business will start a retirement plan for employees in the next two years. This percentage has experienced a slow decline since 2000, when 16 percent reported they were very likely to start a plan within the next two years.

Another 22 percent say they are *somewhat* likely to start a plan, but 43 percent say they are *not at all* likely to start a plan in the next two years (up from 32 percent in 1998 to 43 percent in 2002).

Source: EBRI, The 2003 Small Employer Retirement Survey (SERS) Summary of Findings

Characteristics of Employers Not Providing Retirement Benefits

- Small employers that do not offer retirement plans tend to have revenues of less than $2 million (70 percent).
- They tend to be family-owned businesses (61 percent), even among those with 21 to 100 full-time employees.
- Two-thirds have been in business for at least 10 years (66 percent).
- Nonsponsors tend to employ workers who have a high school degree or less. Their workers also tend to earn between $20,000 and $40,000, to be between the ages of 30 and 39, and to stay three to nine years with the business.

Source: EBRI, The 2003 Small Employer Retirement Survey (SERS) Summary of Findings

Employee Characteristics of Nonsponsors, by Size of Business

Characteristics of Most Full-time Employees	Total	5-20 Workers	21-100 Workers
Age			
Under age 30	25%	23%	39%
Ages 30–39	40	40	42
Age 40 or older	31	33	19
Annual Salary			
Less than $20,000	30	30	27
$20,000–$40,000	59	58	68
Over $40,000	8	8	5
Educational Level			
High school or less	56	55	63
Some college	30	31	25
College degree or more	13	13	10
Length of Time with Company			
Less than 3 years	36	35	43
3–9 years	42	41	44
10 years or more	20	21	12

Source: EBRI, The 2003 Small Employer Retirement Survey (SERS) Summary of Findings

More than ¾ of Vermont's businesses establishments have nine or fewer employees, but these 17,000 establishments employ 21% of the state's workers.

Source: Vermont Economy Newsletter, March, 2006

Why Small Businesses Don't Offer Plans

- **Administrative complexity**
- **Cost**
  - **Start-up is expensive in terms of time and money. Initial start-up fees often fixed, regardless of firm size.**
  - **Recurring administrative costs, including preparation of tax forms and record keeping, may be burdensome.**
- **Difficulty comparing options**
- **May not be profitable for investment firms to offer services to smallest businesses**

Source: Steve Idemoto, Washington Voluntary Accounts: A proposal for Universal Pension Access, Economic Opportunity Institute, October 2002

How Can We Help?

- **Make voluntary, portable retirement savings available to all workers in the state.**
- **Allow workers to make tax-deferred contributions to a 401(K)-style retirement account.**
- **Provide an easy and inexpensive mechanics for small business to offer the benefit of a retirement plan to workers.**

Vermont Voluntary Retirement Savings Program

- **What:** A voluntary retirement savings plan option for employers and employees, or self-employed Vermonters, sponsored by the State of Vermont at no cost to taxpayers.

- **Why:** A healthy retirement system to augment Social Security is needed. A very large percentage of Vermonters are not currently saving for retirement and do not have retirement plans offered through their employers. Taxpayers will bear the ultimate responsibility for seniors with insufficient savings. By providing a simplified, inexpensive, high-quality, and safe retirement plan option for small employers and self-employed Vermonters, we can increase critical savings for retirement. People will save if simple retirement plans are available.

- **How:** The Vermont State Treasurer will piggyback on the State's existing defined contribution and/or deferred compensation plans to offer businesses the option of providing a 401(K) retirement plan for their employees. Administrative and investment expenses will be covered in the fee for plan participants.

Vermont Voluntary Retirement Savings Program

- **Advantages for Employees:** Payroll deductions, pre-tax savings contributions (not the case for most private IRAs), portability, low cost, simplicity, pre-screened investment options, safety, credibility.

- **Advantages for Employers:** Optional participation and employer match. Easy administration and low cost. Safety.