Statement of Norman Stein

Before the ERISA Advisory Council

Working Group on

"Gaps in Retirement Savings

Based on Race, Ethnicity and Gender"

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Good afternoon. I am Norman Stein. I am a professor at the Drexel University School of Law, where I teach and write principally in the areas of employee benefits and tax law. I am also Senior Policy Advisor for the Pension Rights Center in Washington, on whose behalf I am testifying today.

The Pension Rights Center is the country's oldest consumer organization dedicated solely to protecting and promoting the retirement security of American workers, retirees, and their families. So on behalf of the Center, thank you for inviting me here today to present our views on gaps in retirement savings based on race, ethnicity and gender. On a personal note, I should also add that it is always a pleasure to appear before the advisory council, of which I am an alumnus, to assist it in its work.

Today's topic is an important and interesting one, in part because it was not a driving consideration in the enactment of ERISA. ERISA was initially crafted not to expand participation or improve the adequacy of benefits in retirement plans, but to improve transparency and fairness for working people participating in those plans. It was primarily consumer protection legislation, not retirement policy legislation. Moreover, in the 1960s and early 1970s—the incubation period for ERISA—issues of race, gender, and ethnicity, and the disparate economic outcomes based on such characteristics, focused more on overt discrimination than on structural characteristics of American economic life that result in less favorable economic outcomes for members of certain groups. Because of the important work of Nari Rhee, your next witness, we have considerable empirical evidence of how these disparities infect our national retirement preparedness as well as the more obvious areas of wage and job opportunities. And we also have an unacknowledged problem: many undocumented workers have off-the-books jobs and are not the beneficiaries of any retirement program.

It should also be said that ERISA was a bill written by men for a regular, full-time workforce composed mostly of men. Women were and continue to be paid less than men, are less likely than men to work at a job with pension coverage, and when they do work in such a job, are less likely to work long enough to vest in their benefit and, if they work long enough to vest, are less likely to accumulate adequate levels of benefits. As a consequence, women are more likely than men to be dependent upon the retirement savings accumulated in employer plans from their spouse's employment. The 1974 version of ERISA, although providing that a plan had to provide the option of a joint and survivor annuity for married participants, did not require spousal consent for the participant's election to be paid a single life annuity. Indeed, it took almost ten years of advocacy before Congress required spousal consent to a participant's election for a benefit form that deprives her of a survivor annuity in a pension plan. But because of quirks in the law, largely explainable by the historical development of profit-sharing and 401(k) plans, a spouse's interest in a participant's retirement savings account is not always adequately protected.

A spouse's right to share in a pension at marital separation or divorce is another issue with which the 1974 ERISA Congress simply failed to engage, which created considerable uncertainty about whether and how and by whom a pension could be divided when a marriage ended. Again, Congress took up the issue in the Retirement Equity Act of 1984, which introduced the QDRO mechanism. The QDRO process, however, is expensive, complex, and can too often result in woman not receiving their equitable share of a pension after a divorce.

I want to make two additional general introductory points—about issue overlaps. Particularly with respect to solutions, there is considerable overlap between the Working Group's topic today and retirement preparation problems experienced by low and moderate income people generally. And second, one of the issues that complicates the discussion about retirement coverage gaps is the overlapping problems of retirement savings and shorter-term savings needs among low and moderate income individuals. It is difficult to address the retirement savings problem without also addressing the aggregate savings problem.

I will turn now to three sets of gender, racial and ethnic "gap" topics about which the Pension Rights Center is particularly concerned. The first topic is retirement issues faced disproportionately by women, the issue I was specifically asked to discuss because of work that the Pension Rights Center initiated two years ago on retirement benefits and divorce. The second topic is incremental reforms that might close some of the system's gaps in coverage and adequacy. And finally, the third topic is an argument for a different national retirement policy to replace the Rube Goldberg system we are now saddled with, in which enormous tax expenditures are used to reward the savings of the people least likely to need government largesse to incentivize them to save for retirement while preparedness problems of lower and moderate individuals are studied over and over again rather than meaningfully addressed. We can do better than this if only we can muster the national will to do so.

I. Gender Issues.

As earlier noted, Congress was not focused on expanding coverage or increasing benefit adequacy when it enacted ERISA. Its concerns were ensuring that contractual pension expectations were satisfied—that plan participants vested in their benefits, that defined benefits were properly funded, that plan assets were competently and honestly managed, that defined benefits were insured, and that there was some control over the magnitude of the tax subsidy. Little in ERISA changed the underlying scope of plan coverage or benefit adequacy. Plans could continue to exclude part-time and seasonal workers and independent contractors; the 1974 vesting rules enshrined what was then the commonly used 10-year cliff vesting provision; and even apart from vesting, the benefit structure of most defined benefit plans favored employees with long job tenures. Pension plans were also permitted to fully integrate with Social Security, which further diminished retirement security for the many woman whose wages were at, below, or not much higher than the Social Security wage base. In short, ERISA was not a statute designed to assist people with the type of work histories and compensation levels that many women, in and out of the workforce and often in part-time positions, experienced. It should be said, however, that there were in 1974 some advocates for pension reform that would have been responsive to some of the considerations relating to the participation of women in the workforce, including Congresswoman Liz Holtzman, law professor Merton Bernstein, and Karen Ferguson, the president of the Pension Rights Center. But despite these Cassandra-like voices, woman today are, according to the Census bureau, to have only 55% of the retirement income of men and are almost twice as likely as men to face poverty in old age.

This means that the retirement security for many married women was and continues to be tied partly or entirely to the workplace savings accumulated by their spouse. But ERISA, as enacted in 1974, did not adequately protect the interests of a woman in her spouse's pension. There are three separate inflection points at which a spouse's interest in a retirement plan was (and as we will discuss, still is) inadequately protected: at divorce; at the time a pension benefit form is selected, for this when a spouse's survivor annuity is either selected or forgone; and during pre-retirement moments of discretionary control of a plan's assets. Although there have been positive changes to ERISA in its protections for spouses, particularly with the enactment of the Retirement Equity Act of 1984, there remain significant statutory shortcomings in the protection of a woman's interest in her spouse's pension.

A. QDROs and Divorce

Prior to ERISA, judges in appropriate state courts had the power to divide a pension at divorce, at least in some states in some circumstances. ERISA, as enacted, introduced two elements of uncertainty with respect to the jurisdiction of state courts to divide pensions among a divorcing couple: ERISA's provisions preempting state laws that relate to employee plans and ERISA's provision prohibiting alienation of retirement benefits. And it was unclear under the statute whether federal courts themselves had jurisdiction over such matters.

In 1984, Congress addressed the confused state of the law by introducing the QDRO mechanism, which divides responsibility of pension divisions among state courts, plans, and federal courts.

But the 1984 legislation has not worked nearly as well as it should have, at least if the goal was to ensure that pensions were equitably and effectively divided on marital disunion. Here it should be noted that retirement plan savings, where they exist, are typically the most valuable marital asset outside a family residence.

The QDRO process is complex and often requires expert legal advice. A lawyer dividing a pension must know the terms of the relevant retirement plan, must know the options for division under state law, and must know the complicated federal requirements for turning a state court order into a qualified domestic relations order. Expert legal help is in short supply and can be expensive. Many legal aid organizations are not equipped to prepare QDROs and neither participants nor non-legal advocacy organizations are educated about the need to divide retirement benefits at divorce and how to navigate the QDRO process. These problems are compounded for spouses who are not fluent English speakers.

While some plans provide model QDRO forms and extraordinarily helpful guidance to lawyers and participants, many plans do not and some plans, generally inadvertently, create create obstacles to the creation of a QDRO. In addition, many individual account plans and plan record keepers charge fees for processing a QDRO. And in divorce cases involving spousal abuse, the QDRO process's complexities sometimes allow the participant spouse to prolong or leverage the process to continue exerting coercion and control over their former partner.

Because the QDRO process is not well understood, many spouses, particularly in moderate and lower income households, are not in position to divide a pension at all. Somewhat incredibly, a spouse of a plan participant does not possess a clear legal right to request information directly from a plan, information that is generally required in order to prepare a QDRO, an ERISA Catch 22. And sometimes a participant empties out a retirement plan before the QDRO process even gets underway. Moreover, it is often difficult to modify a domestic relations order, which at the least requires a new court appearance, and time and resources, even when the parties are in agreement about the modification.

The Pension Rights Center typically fields approximately 2,000 inquiries each year from individuals around the country seeking help with earned retirement benefits. One in five of these calls is about the division of retirement benefits at divorce. In 2018, the Center's website had 120,000 unique visits to a single page covering the division of retirement benefits at divorce. And six federally funded pension counseling projects providing services to individuals in thirty states, also receive thousands of inquiries over the course of a year.

It is for these reasons that the Pension Rights Center convened a common-ground initiative on women and divorce, in which family lawyers, family court judges, legal aid attorneys, large plans, women's and other advocacy groups, and organizations as diverse as AARP and the Chamber of Commerce, have joined forces to make the QDRO process simpler, more transparent, and more accessible.

The initiative is focusing on educational efforts directed at participants and advocacy organizations, the preparation of model forms for creation of QDROs, and training programs for domestic relations lawyers, legal aid organizations, ERISA lawyers, and family court judges. The initiative also has a work group that is focusing on regulatory and legislative steps that might be taken to improve the division of retirement assets at divorce. One possible idea that is interesting and worth at least some thought is the benefits of an automatic statutory default division of pensions at divorce, which would apply unless a couple elected out.

B. Survivor Benefits

When ERISA was enacted in 1974, it was common for pension plans to offer married participants an annuity benefit with a spousal survivor annuity. ERISA made it mandatory for a plan to offer such a benefit form but the choice of whether to take this form of benefit or a larger straight life annuity was the participant's alone; spousal consent was not required. And ERISA did not include a pre-retirement survivor annuity feature. The Retirement Equity Act of 1984 added these critical spousal protections.

But these protections apply to "pension" plans, whether defined benefit or defined contribution in form (for example, a money purchase pension plan), but not to other individual account plans unless the plan offers an annuity benefit option. This means that the typical profit-sharing plan, including most 401(k) plans, offers only a limited spousal survivor protections: the spouse is the default beneficiary of the plan unless the spouse waives this beneficiary status in a notarized writing. But there are no constraints on the participant in such plans until death: the participant can withdraw all or part of his account balance, or take a loan, without spousal consent. And for IRAs, federal law does not even mandate that the spouse be the default beneficiary, although under some state property regimes the spouse is automatically entitled to all or a part of the IRA. IRAs, which receive rollovers from employer plans, today hold more assets than in all ERISA-covered plans. It is a major defect in our retirement system that IRAs and most individual account plans provide so little recognition of the reality that retirement plans of married couples were, in effect, created by both parties to the marriage, not simply the participant.

C. Pre-Retirement Control of Plan Assets

We have already noted that in profit-sharing plans and IRAs, a participant can to the extent a plan permits, take withdrawals (often during active employment) and loans, without spousal consent. To this we can add the fact that the participant has control over the investment of plan assets in self-directed plans and the spouse has no right to plan disclosures or information until the participant’s death. I note that Senator Patty Murray has just introduced legislation, the Women’s Retirement Protection Act, which would create spousal consent requirements for certain distributions to a participant from individual account plans.

I want to close this section of my comments with a pet peeve: catch-up contributions, which were added to the Internal Revenue Code supposedly as a means of helping woman who have inadequate retirement savings because of time they spend outside the workforce. Our tax laws were thus amended to permit people over 50 to make an additional contribution to a 401(k) plan, now $6,500 a year above the normal limit. If one is drawn to irony, one might speculate that this provision is designed to help those lower and moderate income women who are already contributing the maximum $19,500 to their 401(k) plan and want to contribute even more. Of course, the only people who make this contribution are those well paid enough to contribute an aggregate $26,000 per year, a pretty small slice of the population. And the General Accounting Office has indicated that this provision is used far more often by men, who have not been out of the workforce, than by woman who have. It is a costly and unnecessary provision that has almost nothing to do with retirement issues faced by women.

II. Incremental Measures to Address Coverage and Adequacy Gaps

Ideas that would mandate or at least incentivize coverage and employer contributions to Americans who currently do not benefit from the current system (note that there is overlap between the proposals):

A. A mandatory universal pension system, in which employers would contribute to a retirement savings vehicle. Jimmy Carter's Commission on Retirement Policy proposed such a system in its 1979 report, recommending a program in which employers would contribute 3% of payroll for all workers. There have been several similar proposals over the years, most recently "The Savings for the Future Act," introduced by Senators Chris Coons and Amy Klobuchar and Representatives Scott Peers, Lucy McBath and Lisa Blunt Rochester, which would generally require employers to contribute 50 cents per hour to an employer plan or an UP Account, which would be modeled on the Federal Thrift Savings Plan.

B. Replace matching safe harbors, where employers match a percentage of employee contributions with reverse matches, where employees can match a percentage of employer contributions. This ensures that all plan participants will receive an employer contribution.

C. Provide immediate vesting in employer matching contributions and do not permit pre-retirement withdrawals for such contributions.

D. Require coverage of part-time and seasonal workers. The Women's Retirement Protection Act would take modest first steps in this direction.

E. Bright letter rules that treat most gig-economy workers as employees for purposes of retirement plans. The master-servant doctrine is an irrational arbiter of employee status for a national retirement policy—it has nothing to tell us about retirement policy or whether the person or entity that engages labor should bear responsibility for contributing to that person's retirement security.

F. Household worker SEPs. Permit a person who engages household labor on a regular basis to establish a SEP for such worker, with the employer eligible to deduct such contributions.

G. Bring back the MyRa. Allow it to be used for small rollover contributions. Do not require conversion to an IRA. And provide federal annuity conversion of MyRa amounts.

H. Increase the saver's credit and make it refundable. To extent of the credit, lock in assets until retirement age.

Eliminate the IRC § 72(t) 10% tax on early withdrawals.

Section 72(t) of the Internal Revenue Code imposes a 10% penalty tax on withdrawals from a retirement plan unless one of several exceptions apply. There are two conceivable justifications for this tax: it recovers a tax subsidy which was intended to incentivize retirement savings; and/or it discourages people from withdrawing retirement assets before retirement.

While I am not aware of empirical work showing the incidence of the tax by income, race, gender or ethnicity, my impression is that it is primarily a tax on lower and moderate income participants in employer plans or IRA owners. For these individuals, the tax is purely punitive—lower income retirement savers receive small if any tax subsidies for their savings and a 10% add-on tax is far in excess of any tax subsidy they received. And many such individuals withdraw money from an employer plan when they lose a job and often desperately need the money. A 10% tax is not likely to deter a withdrawal in such a situation.

Moreover, most of the exceptions from section 72(t) are designed to address the needs of middle income rather than lower-income taxpayers. The section 72(t) tax, when assessed against lower and moderate income individuals is a mean-spirited, unjustified punitive tax. There should be an exception from the tax for taxpayers whose income is below some amount, such as 200% of the poverty level.

Study of Undocumented Workers Access to Retirement Plan Benefits.

It has been estimated that undocumented workers contribute upwards of $12 billion to Social Security, even though they are not eligible to draw Social Security benefits. There are also questions about whether an undocumented worker is eligible to participate in an employer retirement plan and if so, whether they are able to access their plan benefits. These issues merit study.

Default Electronic Notice.

The retirement industry, aware of the power of defaults, has been pushing the Departments of Labor and Treasury to permit plans to use electronic delivery as the default method of providing required disclosures. There is, however, considerable disparity in internet and computer access based on race. The Census Bureau tells us that 36.4% of African Americans and 30.3% of Hispanics lack broadband or computer access, compared to only 21.2% of non-Hispanic whites and 11.1% of Asians. This issue should be studied before allowing plans to default participants into electronic forms of disclosure.

III. A New System

Our national retirement policy is essentially built on two pillars: Social Security, which alone is inadequate to provide for retirement, and the employer-based retirement system, which is heavily tax-subsidized—the subsidy is estimated at almost $1.5 trillion dollars over the next five years. The value to an individual of the tax subsidy in the private system is a function of the individual's marginal tax rate on investment income, the amount sheltered in a retirement plan, and the length of time retirement assets stay in plan solution. Since high-income individuals are subject to high marginal tax rates and have the greatest ability to defer income into retirement plans and park it there indefinitely, the cost to the government of maintaining the tax-subsidized retirement system disproportionately benefits the upper quintile of income earners, who by definition do not need to be incentivized to save for retirement or, for that matter, for any purpose. They can, and should, and will save without such incentives.

The incentives are sometimes justified by resort to the Internal Revenue Code's nondiscrimination rules. The idea, which John Langbein has referred to as brining the whale, is this: highly paid employees will demand that their employer establish a retirement plan so that they may enjoy the resulting tax reduction. But once the employer establishes the plan, the so-called non-discrimination rules force the employer to provide benefits for lower and moderate income employees, who otherwise would not save. If that sounds like a ridiculous justification for spending $1.5 trillion dollars over the next five year it is because it is. And it is an idea that not only fails to work in theory, but not surprisingly also fails to work in the real world. In any given year, only a fraction more than 50% of the workforce participates in private employer retirement plans. The median 401(k) balance in Vanguard accounts last year was $25,885 and that is the median of people who have 401(k) balances. And the median for people age 65 and older is only $65,588. If we want to spend government resources to increase the retirement resources of low and moderate income individuals, we should direct that money at the intended beneficiaries and not engage in a shadow play of bribing the wealthy to get plans established and then depending on the “non-discrimination” rules to provide benefits for those who would otherwise be under-saved for retirement.

A MUPs plan, a plan such as that advanced in the Savings for the Future Act, an expanded Social Security system, mandatory contributions to something similar to the Netherlands collective defined contribution plans, Professor Ghilarducci’s Guaranteed Retirement Account—there are many good ideas out there, ideas that might actually help all Americans prepare for retirement. And helping all Americans, by definition, means no gaps in coverage related to race, ethnicity, or gender.