Private-Sector Defined Contribution Pension Plans: An Introduction

June 8, 2022

Congressional Research Service
https://crsreports.congress.gov
R47152

CRS REPORT
Prepared for Members and
Committees of Congress

Private-Sector Defined Contribution Pension Plans: An Introduction

SUMMARY

R47152

June 8, 2022

John J. Topoleski
Specialist in Income Security

Elizabeth A. Myers
Analyst in Income Security

The two types of pension plans that private-sector employers can offer are defined contribution (DC) plans, in which participants have individual accounts that can provide a source of income in retirement, and defined benefit (DB) plans, in which participants receive regular monthly benefit payments in retirement (which some refer to as a "traditional" type of pension). Some employers sponsor both types of pension plans for their employees, though most sponsor either one type or the other. In 2021, about 68% of the U.S. private-sector workforce had access to and 51% participated in pension plans through their employers.

A notable trend of the private-sector retirement system is that over the past five decades, employees have become less likely to be covered by a DB pension and more likely to be covered by a DC pension. By 2021, among private-sector workers, 15% had access to and 11% participated in DB plans, while 65% had access to and 51% participated in DC plans. This shift has occurred for a number of reasons. For employers, DC plans may be administratively easier and their costs tend to be both lower and more predictable than DB plans. For employees, the shorter vesting requirements and portability of DC plan balances at job change or retirement are advantageous features. However, because DC plans, unlike DB plans, do not provide a guaranteed benefit for life, this shift has raised concerns about whether households are adequately saving for retirement.

Multiple types of DC plans may be available to employers, including 401(k) plans, profit-sharing plans, money purchase plans, and employee stock ownership plans (ESOPs). DC plans can also be classified based on how many employers sponsor the plan: Single-employer plans are sponsored by one employer, while multiple-employer and multiemployer plans are sponsored by more than one employer. Most DC plans are single-employer plans, though provisions in the the Setting Every Community up for Retirement Enhancement Act of 2019 (SECURE Act, enacted as Division O of the Further Consolidated Appropriations Act of 2020 [P.L. 116-94; December 20, 2019]) were designed to encourage multiple-employer DC plan sponsorship.

Some DC plan policy issues differ from those of DB plans. For example, participants in DC plans are typically responsible for choosing the amount of their contributions, investing their funds, rolling over their account balances at job change, and drawing down assets in retirement. In addition, individuals with DC account balances are at risk of outliving their assets. Some policy analysts note that certain policies toward pensions may need to be reexamined because many were created in the early 1970s—when most workers with pensions participated in DB plans.

This report does not discuss DC plans sponsored by federal, state, or local governments. While there are some similarities between private-sector and public-sector DC plans, many of the laws and regulations that cover private-sector DC plans do not apply to public-sector DC plans.

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Introduction

A pension is a voluntary benefit offered by employers to assist employees in providing for their financial security in retirement.[1] The two types of pension plans that employers can offer are defined contribution (DC) plans, in which participants have individual accounts that can provide a source of income in retirement, and defined benefit (DB) plans, in which participants receive regular monthly benefit payments in retirement (which some refer to as a "traditional" type of pension).[2] Some employers sponsor both types of pension plans for their employees, though most sponsor either one type or the other.[3] Most private-sector employers that sponsor pension plans offer DC plans, of which the 401(k) plan is the most common.

Data on pension plan incidence reports both *access to* and *participation in* benefit plans. Access rates measure the percentage of employees that have benefit plans available for their use. Participation rates indicate the percentage of employees who make contributions (in DC plans) or are earning benefits (in DB plans).[4] Both measures are used to provide a more complete picture of the availability and use of retirement plans. Using only access rates might overstate the retirement security of workers, while using only participation rates would understate the availability of benefits. Among private-sector workers, 68% had access to and 51% participated in retirement plans at work in March 2021.[5]

Nearly all private-sector pension plans are governed by the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406), which is enforced by the Department of the Treasury, the Department of Labor, and the Pension Benefit Guaranty Corporation. Congress enacted ERISA to protect the interests of pension plan participants and beneficiaries. ERISA is codified in the *U.S. Code* in Title 26 (Internal Revenue Code, or IRC) and Title 29 (Labor Code). ERISA sets standards that pension plans must follow with regard to plan participation (who must be covered), minimum vesting requirements (how long an employee must work for an employer to have a legal right to a benefit), and fiduciary duties (how a pension plan is run in the sole interest of participants). ERISA covers only pension plans run by private-sector employers and nonprofit organizations. Pension plans established by the federal, state, and local governments and by churches are exempt from ERISA's coverage.[6] This report does not cover federal, state, and local governmental plans.This report provides an overview of private-sector DC pension plans and provides context for policy issues that affect private-sector DC pension plans.[7] It covers access to

[1] For an overview of pensions, including pensions avalable in the public sector, see CRS Report R47119, *Pensions and Individual Retirement Accounts (IRAs): An Overview*.

[2] In some DC plans, plan participants have the option to purchase annuities (a monthly payment for life) with some or all of their account balances. In some DB plans, plan participants have the option to receive a lump-sum payment at retirement in lieu of the annuity.

[3] In March 2021, 12% of private-sector workers had access to both DB and DC plans, 3% had access to DB plans only, and 53% had access to DC plans only. See U.S. Department of Labor (DOL), *National Compensation Survey: Employee Benefits in the United States, March 2021*, September 2021, https://www.bls.gov/ncs/ebs/benefits/2021/employee-benefits-in-the-united-states-march-2021.pdf.

[4] See DOL, "National Compensation Survey: Glossary of Employee Benefit Terms," https://www.bls.gov/ncs/ebs/glossary20152016.htm.

[5] Ibid. Sixty-two percent of full-time, private-sector workers in the United States participated in retirement plans sponsored by their employers in 2021.

[6] Church plans can elect to be covered by ERISA. Governmental plans, such as 403(b) and 457(b) plans that are sponsored by governmental employers, are not subject to ERISA but are tax-qualified.

[7] For more information about DB plans, see CRS Report R46366, *Single-Employer Defined Benefit Pension Plans: Funding Relief and Modifications to Funding Rules*; and CRS Report R43305, *Multiemployer Defined Benefit (DB)*

and participation in pension plans among U.S. workers, the growth of DC plans since 1974, and DC retirement account balances. The focus of this report is on private-sector DC plans for several reasons. First, private-sector employees face issues related to access and participation in pension plans to a greater extent than public-sector employees do.[8] Second, if private-sector employees do have access to workplace retirement plans, they are more likely to have access to DC plans. And third, ERISA applies only to private-sector plans.[9]

Defined Contribution Pension Plans

In DC plans—of which 401(k) plans are the most common in the private sector—workers contribute a percentage of their wages to individual accounts established by the employers. An employer may also contribute a match to the DC plan, which is an additional contribution equal to some or all of the worker's contribution. Workers determine individually how their account contributions are invested among investment options provided by the employer. The account may accrue investment returns and can then be used as a source of income in retirement.

The DC pension plans that employers offer are *tax-qualified*, which means that the retirement savings plan provides tax benefits for both employers and participants.[10] For private-sector employers, contributions are tax deductible. For participants, contributions to DC plans are made to either pre-tax accounts or *designated Roth accounts*. In pre-tax accounts, contributions are excluded from taxable income (in which case, taxation is deferred until funds are distributed). In designated Roth accounts, contributions are not excluded from taxable income (in which case, most distributions in retirement are not taxable). As a condition of being tax-qualified, pension plans must meet certain requirements in the IRC with regard to eligibility and participation. These requirements ensure that a broad range of employees in a company—not just upper management (referred to as *highly-compensated employees*)—benefit from the plan.[11]

Retirement Account Balances

Table 1 provides 2019 data on the percentage of households, by age and net worth quintile, with (1) DC savings from a current or past job and (2) retirement savings more generally, which includes DC savings, Individual Retirement Accounts (IRAs), and Keoghs.[12] **Table 1** includes IRAs because individuals with DC plans often roll their account balances over to IRAs at job change or retirement. In 2019, the percentage of households with retirement account balances

Pension Plans: A Primer.

[8] Nearly all public-sector employees have access to pension plans at work, and the majority of these employees are covered by DB plans.

[9] Certain sections of the tax code apply to private- and/or public-sector plans.

[10] Some employers also offer executives a retirement plan called a nonqualified deferred compensation plan. Compared to a qualified plan, these offer larger benefits but fewer protections. (For example, the assets in the plan are subject to creditor claims in bankruptcy.) Nonqualified plans are not discussed in this report. See U.S. Government Accountability Office (GAO), *Private Pensions: IRS and DOL Should Strengthen Oversight of Executive Retirement Plans*, GAO-20-70, January 2020, https://www.gao.gov/assets/710/704097.pdf.

[11] These are called nondiscrimination rules.

[12] IRAs are tax-advantaged savings accounts that, in most cases, are unconnected to an individual's workplace. For more information on IRAs, see CRS Report RL34397, *Traditional and Roth Individual Retirement Accounts (IRAs): A Primer*. Keogh plans are retirement plans for self-employed people. The Internal Revenue Service (IRS) indicates that this term is seldom used because the law no longer distinguishes between corporate and other plan sponsors. See IRS, *Retirement Plans for Self-Employed People*, https://www.irs.gov/retirement-plans/retirement-plans-for-self-employed-people.

generally increased with age until reaching age 55-65. Households in which the head was older than 65 years (1) were less likely to have DC accounts and more likely to have DB plans during their working years and/or (2) may have already began drawing down their retirement assets.

The percentage of households with savings, as well as the median savings balance, increased by net worth quintile. In the lowest net worth quintile, 21.2% of households had retirement account savings, with a median balance of $4,900. In the highest net worth quintile, 84.1% of households had retirement account savings, with a median balance of $404,000.

Table 1. Household Retirement Savings Balances by Age and Net Worth in 2019

	Percentage with DC Savings	Median Balance of DC Savings (for Households with Savings)	Percentage with Retirement Savings (DC Accounts, IRAs, and Keoghs)	Median Balance of Retirement Savings (for Households with Retirement Savings)
All households	37.5%	$50,000	50.5%	$65,000
Age				
Less than 35	40.4%	$13,000	45.3%	$13,000
35 to under 45	48.2%	$51,000	55.8%	$60,000
45 to under 55	49.9%	$73,000	57.9%	$100,000
55 to under 65	42.3%	$100,000	54.5%	$134,000
65 or older	17.0%	$95,000	43.7%	$125,000
Net worth quintile				
Less than $6,370	18.9%	$5,000	21.2%	$4,900
$6,370 to less than $67,650	29.2%	$13,000	33.4%	$12,500
$67,650 to less than $200,950	41.7%	$31,000	49.3%	$34,000
$200,950 to less than $557,160	45.2%	$76,000	64.5%	$85,000
$557,160 or greater	52.3%	$300,000	84.1%	$404,000

Source: CRS analysis of the 2019 Survey of Consumer Finances.

Notes: The percentage of households with savings refer to those with non-zero balances. Medians are calculated using non-zero balances. Retirement savings include DC accounts, IRAs, and Keogh plans. In some cases, median amounts for retirement savings are less than median amounts for DC plans perhaps because of small-balance accounts, such as IRAs. Households include those in the public and private sectors.

Access to and Participation in DC Plans Among U.S. Private-Sector Workers

Table 2 shows the percentage of private-sector workers in the United States that had access to, and participated in, DC pension plans at work in March 2021. In DC plans, workers traditionally needed to actively choose to participate, though that has changed as more DC plans have adopted *automatic enrollment* provisions in which new employees are enrolled in the plan by default but have the option to decline participation (referred to as *opting out*).[13]

Table 2 shows access and participation data for private-sector workers in March 2021. Key distinctions in the data include the following:

- A greater percentage of full-time workers had access to DC plans compared with part-time workers. Among full-time workers, 74% had access to DC plans. Among part-time workers, 38% had access to DC plans.
- Access and participation rates were higher for workers in higher-paying occupations. As the average wage of a worker's occupation increased from the lowest 25% to the second-lowest 25%, DC plan access rates increased from 42% to 64%, and participation rates increased from 22% to 44%.[14] This increase was larger than that between the other average wage quartiles.
- Access rates increased as the size of workers' firms increased. For example, 51% of private-sector workers in firms with fewer than 50 employees had access to DC plans, whereas 85% of workers in firms with 500 or more employees had access.

Table 2. Access and Participation Rates in Employer-Sponsored Pension Plans Among Private-Sector Workers, March 2021

	Defined Contribution	
	Access	**Participation**
All workers	65%	47%
Full-time	74%	57%
Part-time	38%	18%
Union	61%	53%
Nonunion	66%	47%
Average wage of occupation		
Lowest 25%	42%	22%
Second 25%	64%	44%
Third 25%	75%	58%
Highest 25%	85%	73%
Number of employees at place of employment		
1-49	51%	33%
50-99	68%	48%
100-499	76%	55%

[13] Prior to the widespread adoption of automatic enrollment, about 30% of employees eligible for a DC plan did not choose to participate. See, for example, these reports with data prior to the widespread adoption of automatic enrollment DC plans: Patrick Purcell, *Retirement Plan Participation and Contributions: Trends from 1998 to 2006*, Congressional Research Service, January 2009, https://ecommons.cornell.edu/bitstream/handle/1813/78093/RL33116_20090130.pdf; and Vanguard, *How America Saves 2009: A Report on Vanguard 2008 Defined Contribution Plan Data*, August 2009, p. 20, https://www.pionline.com/assets/docs/CO68397126.PDF.

[14] The corresponding take-up rates (which measures the percentage of individuals with access who participate) increased from 52% to 69%.

	Defined Contribution	
	Access	Participation
500 or more	85%	71%

Source: Bureau of Labor Statistics (BLS), March 2021 National Compensation Survey (NCS), https://www.bls.gov/ncs/ebs/benefits/2021/employee-benefits-in-the-united-states-march-2021.pdf.

Notes: Private-sector workers exclude agricultural workers and private households. Definitions are from the NCS's Glossary of Employee Benefit Terms, available at http://www.bls.gov/ncs/ebs/glossary20152016.htm, and BLS, "Information Glossary," http://www.bls.gov/bls/glossary.htm#C.

One of the notable trends in the U.S. retirement system is that over the past five decades, private-sector employees have become less likely to be covered by DB pensions and more likely to be covered by DC pensions. This shift occurred for a number of reasons, such as lower and more predictable costs and fewer administrative burdens.[15] For more information on this, see CRS In Focus IF12007, *A Visual Depiction of the Shift from Defined Benefit (DB) to Defined Contribution (DC) Pension Plans in the Private Sector*.

DC Plans: Types of Plans

The types of DC plans available to private-sector employers include 401(k) plans, profit sharing and stock bonus plans, money purchase plans, and Employee Stock Ownership Plans (ESOPs). Tax-exempt 501(c)(3) organizations can offer 403(b) and 457(b) plans. While these plans share many similarities, they differ along several dimensions, such as whether employee and/or employer contributions are required or allowed, which investment options are permitted, and if and when withdrawals can be made.

401(k) Plan. A 401(k) plan allows employees to contribute a portion of their wages to their individual accounts. Employers can also contribute to the accounts as a match of the employee's contributions or as a profit-sharing contribution. Employers must demonstrate that their 401(k) plans benefit a wide variety of employees (and not just well-paid employees) through a process called *nondiscrimination testing*.[16]

Additionally, there are several types of 401(k) plans available to certain employers:

- *Safe Harbor 401(k)* plans are available to employers of any size. These plans are exempt from nondiscrimination testing, provided they follow certain contribution rules.
- *SIMPLE 401(k)* plans are available to employers with 100 or fewer employees and are exempt from nondiscrimination requirements. Employers are required to make either (1) matching contributions up to 3% of each employee's pay or (2) a nonelective contribution of 2% of each employee's pay.
- *Solo 401(k)* plans cover a business owner with no employees (or the owner and spouse, if applicable).

[15] See U.S. Bureau of Labor Statistics, *Retirement Costs for Defined Benefit Plans Higher Than for Defined Contribution Plans*, December 2012, https://www.bls.gov/opub/btn/volume-1/pdf/retirement-costs-for-defined-benefit-plans-higher-than-for-defined-contribution-plans.pdf. DB plan actuaries determine the value of benefits earned by participants in a year and how much the plan must set aside to fund those benefits.

[16] Plan sponsors of SIMPLE 401(k) and Safe Harbor 401(k) plans are not required to demonstrate that the plans are being used by both highly compensated employees and rank-and-file employees.

Profit-Sharing Plans and Stock Bonus Plans. In a profit-sharing plan, an employer makes a contribution to each eligible participant's account based on a formula established by the employer.[17] Employee contributions are not permitted. Profit-sharing plans provide flexibility to employers because they can choose whether to contribute to employees' accounts each year. Profit-sharing contributions do not need to be tied to a company's profits, if any. A stock bonus plan is a type of profit-sharing plan in which employer contributions are paid in employer stock rather than cash. Profit-sharing plans and stock bonus plans may have a 401(k) component, in which case employee contributions are allowed.

Money Purchase Plan. In a money purchase plan, the employer contributes an amount to each eligible employee's account as a percentage of compensation. Employees are not permitted to contribute to the plan.

Employee Stock Ownership Plan (ESOP). An ESOP is a type of DC plan in which the investments are primarily in stock of the plan sponsor. ESOPs allow employees to own shares of the company's stock. ESOPs differ from stock bonus plans in several ways, such as the percentage of assets required to be invested in company stock, tax benefits, and the ability to borrow money to buy employer stock.[18]

403(b) Plan. A 403(b) plan (or tax-sheltered annuity plan) is a pension plan offered by 501(c)(3) tax-exempt organizations and churches. Originally, 403(b) plan investments were restricted to annuity contracts until 1974, after which investments in mutual funds were also permitted.

457(b) Plan. Tax-exempt 501(c)(3) employers may establish 457(b) plans.[19] While 457(b) plans share many features with 401(k) plans, they differ in some respects—for example, investments in 457(b) plans are limited to annuities and mutual funds, and some withdrawal rules differ.

Single, Multiple, Multiemployer Plans

Pension plans are also classified by whether one or more than one employer sponsors the plan. Pension plans sponsored by one employer are called *single employer* plans. Plans established by more than one employer and whose workers are covered by collective bargaining agreements are called *multiemployer* plans. Plans established by more than one employer and whose workers are not covered by a collective bargaining agreement are called *multiple employer* plans.

Historically, multiple employers could participate in a common plan only if there was a business connection among them.[20] However, as of 2021, unrelated employers are able to join together in a common 401(k) plan known as a pooled employer plan (PEP).[21] Though any size 401(k) plan can

[17] For more information, see Human Interest, "How a Profit-Sharing Plan Is Different from a Traditional 401(k)," https://humaninterest.com/learn/articles/profit-sharing-plan-how-is-it-different-from-a-401k/; and IRS, "Choosing a Retirement Plan: Profit-Sharing Plan," https://www.irs.gov/retirement-plans/choosing-a-retirement-plan-profit-sharing-plan.

[18] See National Center for Employee Ownership, "How ESOPs, Profit Sharing Plans, and Stock Bonus Plans Differ as Employee Ownership Vehicles," June 4, 2014, https://www.nceo.org/articles/esops-profit-sharing-stock-bonus-plans.

[19] See IRS, "Non-Governmental 457(b) Deferred Compensation Plans," https://www.irs.gov/retirement-plans/non-governmental-457b-deferred-compensation-plans.

[20] See DOL, Employee Benefits Security Administration (EBSA), *Advisory Opinion 2012-04A*, May 25, 2012, https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/advisory-opinions/2012-04a.

[21] The SECURE Act (enacted as Division O of the Further Consolidated Appropriations Act of 2020 [P.L. 116-94; December 20, 2019]) authorized PEPs for 401(k) plans. Unrelated employers that sponsor 403(b) plans cannot join PEPs. Multiple bills in the 117th Congress would permit 403(b) plans to join PEPs. See, for example, H.R. 2954.

participate in a PEP, small plans might find them advantageous due to their reduced administrative burdens and costs as compared to establishing a single employer plan.[22]

In 2018, there were 675,007 private-sector DC pension plans, of which 669,400 (covering 90.7% of DC participants) were single-employer plans; 4,523 (covering 5.3% of DC participants) were multiple-employer plans; and 1,084 (covering 4.0% of DC participants) were multiemployer plans.[23]

DC Plans: Overview of Policy Issues

Some policy analysts note that certain policies toward pensions may need to be reexamined because they were created in the early days of ERISA—when most people with pensions were receiving DB pension plans and DC plans were supplemental.[24] Since the expansion of DC plans over the past few decades, policymakers and policy analysts have identified a number of issues faced by DC plans and participants in these plans.[25] These policy issues include the following:

Access to and Participation in Plans

Many policymakers have an interest in increasing access to and participation in DC plans among U.S. workers.[26] While 74% of full-time, private-sector workers had access to DC plans at work in March 2021, access rates were much lower among some groups, such as part-time workers (38% of part-time workers had access to DC plans at work), workers in smaller firms (49% of workers in firms with fewer than 50 employees had access to DC plans at work) and workers in lower wage occupations (42% of workers in occupations with the *lowest 25% of average wages* had access to DC plans at work).[27]

Not all workers with access to DC plans participate in these plans. To increase participation rates, an increasing number of DC plans have adopted *automatic enrollment* policies, in which eligible

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[22] See EBSA, "Registration Requirements for Pooled Plan Providers," 85 *Federal Register* 54288, September 1, 2020, https://www.federalregister.gov/documents/2020/09/01/2020-18504/registration-requirements-for-pooled-plan-providers.

[23] See EBSA, *Abstract of 2018 Form 5500 Annual Reports*, January 2021, Table A6, https://www.dol.gov/sites/dolgov/files/EBSA/researchers/statistics/retirement-bulletins/private-pension-plan-bulletins-abstract-2018.pdf.

[24] For example, this was the policy rationale for DOL's update of the definition of *investment advice* in 2016. See EBSA, *Fiduciary Investment Advice: Regulatory Impact Analysis*, April 14, 2015, https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB32-2/ria.pdf, and Rebecca Miller et al., "ERISA: 40 Years Later," *Journal of Accountancy*, September 1, 2014, https://www.journalofaccountancy.com/issues/2014/sep/erisa-20149881.html.

[25] See, for example, Joint Economic Committee, *Retirement Insecurity*, August 2020, https://www.jec.senate.gov/public/_cache/files/98e919eb-87e6-4a5a-b286-ccb9283bd40b/retirement-insecurity-2020-final.pdf; Sen. Susan Collins, "Addressing the Looming Retirement Security Crisis," press release, February 27, 2019, https://www.collins.senate.gov/newsroom/addressing-looming-retirement-security-crisis; and Andrew G. Biggs, *The Real Retirement Crisis: It's Not Where You Think*, Statement before the Committee on Ways and Means, February 6, 2019, https://www.congress.gov/116/meeting/house/108921/witnesses/HHRG-116-WM00-Wstate-BiggsA-20190206.pdf.

[26] See, for example, House Ways and Means Committee, "Neal and Brady Reintroduce Bipartisan Legislation to Strengthen Retirement Security," press release, May 3, 2021, https://waysandmeans.house.gov/media-center/press-releases/neal-and-brady-reintroduce-bipartisan-legislation-strengthen-retirement; and U.S. Congress, Senate Committee on Finance, *Building on Bipartisan Retirement Legislation: How Can Congress Help?*, 117th Cong., 1st sess., July 28, 2021.

[27] See CRS Report R43439, *Worker Participation in Employer-Sponsored Pensions: Data in Brief*.

participants are enrolled in the plan, by default, but may opt out. Policymakers have expressed interest in further increasing plan participation rates.

Adequacy of Contributions

Although workers might have access to, and participate in, DC plans at work, it is possible that they are still not contributing as much as they need to in order to have sufficient retirement assets in retirement. In 2019, among taxpayers who contributed to DC plans, the average contribution was $5,510.[28] Some plans automatically increase a worker's contribution over time to increase employees' savings (referred to as *auto escalation*). Policymakers have also considered expanding the *Saver's Credit*, which is a tax credit for retirement plan contributions that is available to individuals with wages under specified thresholds.[29]

Protection of Plan Participants

Private-sector pension plans are intended to be operated in the sole interest of plan participants for the purpose of providing benefits.[30] As such, a number of issues have the attention of policymakers, such as how to protect participants' personal information online;[31] whether to expand investment options for plan participants to include funds that incorporate Environmental, Social, and Governance (ESG) factors and other non-financial goals,[32] cryptocurrency,[33] and private equity;[34] and whether to expand the definition of *investment advice* that plan participants receive.[35]

Leakages and Short-Term Savings

While many plans allow access to retirement savings prior to retirement via hardship withdrawals and loans and at job change, policymakers are concerned that these provisions might make participants less financially prepared for retirement.[36] Some policymakers have proposed creating

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[28] See CRS Insight IN11721, *Data on Retirement Contributions to Defined Contribution (DC) Plans*.

[29] For more on the Saver's Credit see CRS In Focus IF11159, *The Retirement Savings Contribution Credit*.

[30] See Section 404 of ERISA (29 U.S.C. §1104).

[31] GAO, *Defined Contribution Plans: Federal Guidance Could Help Mitigate Cybersecurity Risks in 401(k) and Other Retirement Plans*, GAO-21-25, March 15, 2021, https://www.gao.gov/assets/gao-21-25.pdf.

[32] See DOL, "US Department of Labor Proposes Rule to Remove Barriers to Considering Environmental, Social, Governance Factors in Plan Management," press release, October 13, 2021, https://www.dol.gov/newsroom/releases/ebsa/ebsa20211013; and the discussion of the Religious Freedom Restoration Act in EBSA, "Financial Factors in Selecting Plan Investments," 85 *Federal Register* 72869, November 13, 2020, https://www.govinfo.gov/content/pkg/FR-2020-11-13/pdf/2020-24515.pdf#page=24.

[33] See Anne Tergesen, "Fidelity to Allow Retirement Savers to Put Bitcoin in 401(k) Accounts," *Wall Street Journal*, April 26, 2022, https://www.wsj.com/articles/fidelity-to-allow-retirement-savers-to-put-bitcoin-in-401-k-accounts-11650945661.

[34] DOL, "US Department of Labor Releases Supplemental Statement on Private Equity Investments in Participant-Directed Retirement Savings Plans," press release, December 21, 2021, https://www.dol.gov/newsroom/releases/ebsa/ebsa20211221.

[35] See DOL, "New Fiduciary Advice Exemption: PTE 2020-02 Improving Investment Advice for Workers and Retirees Frequently Asked Questions," press release, April 2021, https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/faqs/new-fiduciary-advice-exemption.

[36] See Joint Committee on Taxation, *Estimating Leakage from Retirement Savings Accounts*, April 26, 2021, https://www.jct.gov/CMSPages/GetFile.aspx?guid=ed1c9da4-f180-41cd-b3f9-b8afb9531d18; and GAO, *Retirement Savings: Additional Data and Analysis Could Provide Insight into Early Withdrawals*, GAO-19-179, March 28, 2019,

short-term savings accounts within DC plans to assist workers with financial emergencies while keeping retirement balances intact.[37]

Missing Participants

In some cases, plans are unable to connect participants with benefits that they are owed. Examples of such *missing participants* include, for example, a participant who left a company and did not realize he or she was automatically enrolled in the company's DC plan, a former participant who moved but did not provide the plan with a new address, or beneficiaries of a deceased participant whom the plan is unable to contact.[38]

Asset Drawdown and Longevity Risk

Unlike DB plan participants, who most often receive monthly benefit payments throughout retirement, DC plan participants at retirement face the prospect of withdrawing their funds too quickly and outliving their retirement assets.[39] Examples of federal action intended to prevent participants from outliving their assets include a recent Employee Benefits Security Administration rule requiring DC plan sponsors to provide disclosures that illustrate the amount of regular income participants would receive from their account balances[40] and plan sponsors offering annuity options to participants.[41]

DC Plans: The Influence of Behavioral Economics

Over the past 20 years, a branch of economics called *behavioral economics* has significantly influenced pensions and retirement policy.[42] Behavioral economics is rooted in the study of

https://www.gao.gov/products/gao-19-179.

[37] See, for example, U.S. Senate Committee on Health, Education, Labor, and Pensions, "At HELP Hearing on Retirement and Emergency Savings, Murray Discusses Ideas for Bipartisan Package to Strengthen Families' Financial Security," press release, March 29, 2022, https://www.help.senate.gov/chair/newsroom/press/at-help-hearing-on-retirement-and-emergency-savings-murray-discusses-ideas-for-bipartisan-package-to-strengthen-families-financial-security; and Lee Barney, "How to Prevent Retirement Plan Leakage," *Plan Advisor*, May 24, 2021, https://www.planadviser.com/prevent-retirement-plan-leakage/.

[38] See, for example, EBSA, *Missing Participants—Best Practices for Pension Plans*, January 12, 2021, https://www.dol.gov/agencies/ebsa/employers-and-advisers/plan-administration-and-compliance/retirement/missing-participants-guidance/best-practices-for-pension-plans; and Pension Benefit Guaranty Corporation, "Missing Participant," 82 *Federal Register* 60800-60833, December 22, 2017, https://www.govinfo.gov/content/pkg/FR-2017-12-22/pdf/2017-27515.pdf.

[39] See, for example, Angela M. Antonelli, *Generating and Protecting Retirement Income in Defined in Defined Contribution Plans*, Center for Retirement Initiatives at Georgetown University, June 2019, https://cri.georgetown.edu/wp-content/uploads/2019/06/policy-report-19-02.pdf. Note that some policy analysts do not believe that there is a widespread need for individuals to convert their retirement assets into income streams at retirement. See, for example, Investment Company Institute, *The Myth of Under-Annuitization: Managing Income and Assets in Retirement*, April 2020, https://www.ici.org/doc-server/pdf%3A20_ppr_annuitization.pdf.

[40] See EBSA, *Temporary Implementing FAQs: Pension Benefit Statements—Lifetime Income Illustrations Interim Final Rule*, July 21, 2021, https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/faqs/temporary-implementing-faqs-lifetime-income-interim-final-rule.pdf.

[41] See, for example, TIAA/CREF, "Introducing Income Test Drive," https://www.tiaa.org/public/retire/financial-products/annuities/retirement-plan-annuities/income-test-drive/.

[42] A number of economists (for example, Daniel Kahneman in 2002, Finn E. Kydland and Edward C. Prescott in 2004, and Richard H. Thaler in 2017) have been awarded the Nobel Prize for their work related to behavioral economics. See Nobel Foundation, "All Prizes in Economic Sciences," https://www.nobelprize.org/prizes/lists/all-prizes-in-economic-

psychology and considers how individuals' beliefs and consistent errors in judgment (*cognitive biases*) affect decisionmaking. Behavioral economics offers a perspective that differs from more traditional economic thinking, which assumes that individuals are fully informed and make consistently optimal, rational decisions. For example, researchers have found that when presented with alternatives, the option provided when an individual does not make a choice (the *default option*) is influential, perhaps because of procrastination or a belief that the default is somehow good (*anchoring*). More traditional economists might suggest that the default choice does not matter because individuals always choose their best option when presented with alternatives.

Examples of the application of behavioral economics in retirement policy include the use of automatic features in DC retirement plans, such as during the enrollment process, in the savings rate for enrolled participants, and the allocation of investments.[43] Prior to the Pension Protection Act of 2006 (PPA), a newly hired worker typically needed to make an active choice to participate in an employer-sponsored DC plan (*opting in*). PPA made it easier for a plan sponsor to enroll a new employee in a plan without his or her active decision to opt in, provided newly enrolled participants have the option to choose not to participate (*opting out*). This enrollment process is commonly called *automatic enrollment*. Researchers also realized that participants in DC plans do not adjust the amount of their contributions very often—especially participants who were automatically enrolled—which may result in individuals saving less for retirement than what could be considered optimal. An increasing number of DC plans gradually increase an individual's contribution rate over time to some maximum percentage (referred to as *automatic escalation*). Another plan design feature influenced by behavioral economics is the use of target date funds (TDFs). In a TDF, the investment portfolio of a DC participant becomes more conservative as the individual ages. TDFs address a problem of *inertia*, where individuals do not adjust (or *rebalance*) their investment portfolios from high-risk/high-return options to low-risk/low-return options frequently enough as they approach retirement.

It appears that applying behavioral economics concepts to retirement plan design may be affecting retirement outcomes, such as participation rates and portfolio rebalancing. For example, participation rates are higher in DC plans with automatic enrollment. In DC plans in which an individual must make an active decision to participate, about 70% of eligible individuals participate. In DC plans with automatic enrollment, about 90% of eligible individuals participate.[44]

In addition, participants who invest in TDFs do not have to rebalance those portions of their portfolios as they age (and thus, might be less susceptible to seeing large DC plan asset decreases as they near retirement). The number of participants holding TDFs as part of their 401(k)

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sciences/.

[43] See, for example, B. Douglas Bernheim, Andrey Fradkin, and Igor Popov, "The Welfare Economics of Default Options in 401(k) Plans," National Bureau of Economic Research, Working Paper no. 17587, November 2011 (revised March 2015), https://www.nber.org/papers/w17587. However, there may be some downsides to automatic enrollment. For example, some individuals automatically enrolled in DC plans who might otherwise have opted in may save less because the default savings rate is lower than what they might have chosen. See, for example, Joshua Dietch and Taha Choukhmane, *Auto-Enrollment's Long-Term Effect on Retirement Saving*, T. Rowe Price, November 2019, https://www.troweprice.com/content/dam/retirement-plan-services/pdfs/insights/CCON0020242_C8.pdf.

[44] In 2020, data from Vanguard indicated that in plans for which Vanguard provided recordkeeping services, the participation rate in plans with voluntary enrollment was 61% and in automatic enrollment plans was 92%. See Vanguard, *How America Saves 2020*, https://institutional.vanguard.com/ngiam/assets/pdf/has/how-america-saves-report-2020.pdf. Prior to the widespread adoption of automatic enrollment, about 30% of employees eligible for DC plans did not choose to participate. See Purcell, *Retirement Plan Participation and Contributions*; and Vanguard, *How America Saves 2009*, Figure 12.

investment portfolios has increased over time. In 2018, over half (56%) of 401(k) participants held TDFs compared to 19% in 2006.[45]

Author Information

John J. Topoleski
Specialist in Income Security

Elizabeth A. Myers
Analyst in Income Security

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[45] See Sarah Holden, Jack VanDerhei, and Steven Bass, "Target Date Funds: Evidence Points to Growing Popularity and Appropriate Use by 401(k) Plan Participants," Employee Benefit Research Institute, September 9, 2021, https://www.ebri.org/docs/default-source/ebri-issue-brief/ebri_ib_537_401ktdfs-9sep21.pdf.