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From the Editor

ERISA 2.0

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ERISA, the nation's comprehensive retirement law, is showing its age. The Employee Retirement Income Security Act of 1974 added crucial fiduciary protections, ironclad vesting standards, funding requirements, investment rules and a uniform regulatory system. Since then, both Congress and generations of regulators have adjusted the rules, mostly in reaction to discovered abuses and perceived unfairness, and most recently with the so-called SECURE 1.0 and 2.0 Acts.

Yet, during ERISA's five-decade reign, we have experienced declining levels of employee participation and savings, near extinction of private sector defined benefit pension plans and growing worker retirement unpreparedness. The disconnect between good intentions and results is due, in large part, to a lack of a legislative post-mortem review for effectiveness and unintended consequences. It is (past) time for an ERISA reboot.

Here are six big ideas for ERISA 2.0.

UNIVERSAL COVERAGE

Employees do most of their retirement savings at work. Sure, folks can save through an individual retirement account (IRA) or a regular investment account. But saving is hard without the nudge, guidance and convenience of a workplace plan and most people do not save on their own. This relegates workers whose company does not offer any type of plan, gig workers, the self-employed and frequent job-hoppers, together representing over 50% of the private sector workforce, in a savings desert.

ERISA 2.0 should give everyone access to some sort of savings program. I am not suggesting a utopian European style deluxe retirement, just a bare minimum opportunity for folks to save a portion of their own earnings via payroll withholding. Whether through an employer 401(k) (even without a match), a state-run auto-IRA, opening the federal thrift plan to all or a new national savings vehicle, at the very least everyone should be covered by some sort of retirement plan.

BRING BACK PENSIONS AND LIFETIME INCOME

In many respects, the post-ERISA single employer pension is the ideal retirement vehicle, offering lifetime income and professional management, with little decision-making or expertise required of workers. However, employers are steadily eliminating their pensions. Why? Constant "fixes" to ERISA made pensions toxic to employers. Examples include rules that punish underfunding without allowing employers to take advantage of overfunding, cash flow/financial unpredictability caused by fluctuating investment markets and interest rates, benefit limits disproportionately affecting executive decision makers and a slew of regulations adding complexity with little consumer protection.

ERISA 2.0 should enable employers to adopt a pension-like plan where workers receive lifetime income but employers only are responsible for the annual contribution. These retirement plans would still be an effective, low-cost vehicle for paying lifetime income, in part by enabling participants to pool their mortality risks at a lower cost than possible with individual annuities or life insurance. For this to work, benefits would be adjusted (up or down) based on long-term investment and mortality experience.

Importantly, ERISA 2.0 should be flexible so that the pension-like plans can develop organically as the workforce and market evolve.

EMBRACE DEFAULTS

Humans have difficulty making long-term decisions. Procrastination, present-day bias, loss aversion and other built-in wiring make most people poor retirement preparers. Choice architecture and default elections (with easy opt-outs) allow for smart plan design, nudging participants into escalating saving levels, diversified investment and secure lifetime payment elections. In effect, defaults enable most participants to make prudent decisions by doing nothing.

Yet, some politicians and regulators on both the left and right incorrectly see defaults as a big brother conspiracy ignoring the reality that robust communications and opt-outs give participants complete freedom of choice, if they wish. The ERISA rules were recently tweaked to allow greater use of defaults, but regulators are consistently several steps behind best practices. ERISA 2.0 should embrace choice architecture, including requiring all 401(k)s to have automatic enrolment, escalation and periodic reenrollment of non-savers.

CARROTS & STICKS

ERISA uses numerous incentives (tax-deductible contributions and tax deferred investment income) and rules/penalties (requiring broad-based employee coverage, benefit caps and limits on includible compensation) to make retirement plans "fair." Do these well-intended rules succeed? I suspect not and believe a complete and open-minded review and overhaul is needed.

The tax advantages, supposedly costing the U.S. Treasury $200 billion a year in lost revenue, according to the Congressional Budget Office (CBO) are miscalculated and perhaps misguided. The value/cost of the deferral depends in part on the participant's tax bracket during retirement that in turn depends on the participant's investment success, total retirement income and the future state of ever-changing tax laws.

Also, plan distributions (ignoring Roth 401(k) and IRAs) are taxed at less favorable ordinary rates, while non-plan investment income can benefit from favorable capital gains and dividends rates and availability of tax free municipal bonds. Thus, the calculations also must consider whether and how much the participant would save outside of the plan, future rates and investment income. The lost revenue also should be estimated over the entire expected life of the saver, not the artificial period used by the Congressional Budget Office.

With a realistic cost estimate, we then can take a serious look at the effectiveness of the tax advantages of retirement savings and consider whether alternatives, such as tax credits for contributions, would be more effective. I will not try to predict the outcome of a reasoned analysis, but am absolutely sure that the current estimates of revenue loss and effectiveness of incentives are off base.

On the stick side, the benefit and compensation limits – designed to both keep plans from being a windfall for top-earners and to encourage coverage of the lower-paid – have the exact opposite effect. The proof, hiding in plain sight, is the decline in coverage and the near extinction of pensions. These limits affect the decision makers and their direct reports who, when it is time to decide if, what type and how generous a plan to offer, ask "what's in it for me." If the answer is not that much, it discourages plan adoption and decreases benefits levels. Greed may be good or bad, but it definitely affects decision-making.

Everyone should have a workplace retirement plan, but to promote generous benefits in a voluntary system, the top-paid should have the same relative benefits as the rest of the workforce.

TECHNOLOGY

Existing technology could help solve a number of problems – if we let it.

First, we should harness the information stored by the Internal Revenue Service and Social Security into a database to unite "lost" participants with their benefits. This would solve a vexing problem of retirees and their families and employers.

A related concern is the extreme difficulty of combining scattered IRA and retirement accounts into a single easier to manage fund. Anyone who has rolled over an IRA or 401(k) knows how cumbersome, slow and frustrating the process is. Triple that for people who are less literate or financially sophisticated. Several companies have designed software to make rollovers simple. All providers should be required to facilitate frictionless account transfers using their own or another vendor's system.

Technology also has made communicating with participants faster and less expensive. While existing rules encourage e-disclosure, regulators have stymied full adoption, attempting to protect the miniscule minority who cannot (or prefer not to) use smart phones, tablets or whatever, an example of the perfect being the enemy of the good.

Then there is generative AI and other tools that could be employed in financial literacy, investment education and advice, encouraging savings and preventing leakage. ERISA and its regulators cannot (and should not) lead the charge. However, the rules should be flexible and allow experimentation and adoption of these fast-developing technologies.

DISCLOSURE

ERISA always has required that plan summaries and the like be in "plain" English. Anyone who has read a summary plan description, tax notice or other participant explanation knows that every plan in the country is in violation of the plain English rule. These communications (including those prepared by the regulators themselves) are written by lawyers for lawyers, completely ignoring the intended human audience. The communications conundrum is exacerbated by the explosion in class action litigation against employers and providers claiming participants were misled by inadequate disclosure. The resulting "kitchen sink" communications cover all eventualities and say nothing. Granted, it is hard (expensive) to write clearly.

ERISA 2.0 should allow a Russian doll disclosure stacked from a paragraph or two of the key elements (you have a plan), to a page or so of the basics (here is what you get), to lengthier explanations for the concerned and focused.

Crucially, ERISA should protect employers and providers from liability for truthful but brief notices. Perhaps the federal government could hire a few writers to prepare canned plan summaries for providers to crib.

CONCLUSION

The information and tools needed to upgrade our retirement system already exist. We just have to use them.

The views set forth herein are the personal views of the author and do not necessarily reflect those of the law firm with which he is associated.

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