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RETIREMENT SECURITY IN THE NEW ECONOMY: ACCESS AND GUARANTEES

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PARTICIPANTS:

Welcoming Remarks:

WILLIAM G. GALE
Senior Fellow and Director, Retirement Security Project
The Brookings Institution

Panel One: Retirement Plans for Contingent Workers

Moderator:

DEBRA WHITMAN
Chief Public Policy Officer
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Presenter:

DAVID C. JOHN
Senior Strategic Policy Advisor, AARP Public Policy Institute
Deputy Director, Retirement Security Project

Discussants:

IDA RADEMACHER
Executive Director, Financial Security Program
Aspen Institute

SETH HARRIS
Distinguished Scholar, School of Industrial
and Labor Relations
Cornell University

Panel Two: Guaranteed Returns in Retirement Savings Accounts

Moderator:

JOSHUA GOTBAUM
Guest Scholar, Economic Studies
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Presenter:

WILLIAM G. GALE
Senior Fellow and Director, Retirement Security Project
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Discussants:

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The Wharton School at the University of Pennsylvania

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P R O C E E D I N G S

MR. GALE: One of the most fundamental things about retirement savings that people tell you is that you need to start early. And so we're going to try to actually start on time today. So, I'd like to welcome you to RSP's event on Retirement Security in the New Economy. Thank you very much for attending.

We start from the idea that for many people, the retirement system is working quite well. They're on their way to accumulating sizeable nest eggs. Life will be good for them. They will be able to retire with adequate funds. For many others, though, the system is not working so well, and that's not new, but it's still the case.

What is new is that over the last several years, there have been many relevant changes in the economy, in the workforce, in financial markets, in demographics, retirement savings laws and regulations. These changes have affected some old issues, and they've raised some new ones, as well.

This morning we want to focus on two new issues. The first is how should the retirement system deal with contingent workers. As you all know, the basis of the retirement system is ERISA which envisions an employer and an employee, and the question is, how do you deal with retirement when you don't have a well-defined employer/employee relationship? That's our first paper.

The second paper is, should there be guarantees on rates or returns earned on retirement savings? And that will be the topic of the second session. What ties these topics together is that they've both been raised as issues that are affecting people for whom the retirement system is leaving behind, and we will delve into details on both of these papers. David John and I will present two papers. David is the deputy director of the RSP.

We have been fortunate enough, as RSP to assemble an all-star cast of moderators and discussants. You should have a handout with everybody's bio, so I went go through them in advance. I will say that we thank them in advance, and we look forward to their comments and their input.

One further acknowledgement. The research you'll see today was developed under the auspices of funding from the Laura and John Arnold Foundation. RSP greatly thanks the foundation for its support over the years, but of course, we alone, and by that, I mean David, me and our coauthors, Sarah Holmes, who is here, and Mariah Kim, take all responsibility for errors, omissions, opinions, et cetera.

So in the spirit of keeping things moving and keeping things on time, let me stop there and turn the podium over to Debra Whitman, who is the chief public policy officer for the AARP. Thank you.

MS. WHITMAN: Good morning, everyone.

GROUP: Good morning.

MS. WHITMAN: For many, many years, the traditional way you worked was that you got a salary, maybe some fringe benefits, and if you were lucky, a 401K or a defined benefit pension. But that's not the truth going forward. In recent years, the rise of the so-called gate economy, which allows people to hail cabs or Lyft or Uber, bring household help to TaskRabbit and book lodging Airbnb, has brought the contingent workforce into the spotlight.

But the gig is not new. It's been around for many years, and we see more and more employers substituting independent contractors or going away from the traditional employment model. And we know that very few of these workers get health or treatment benefits, and as a group, they're almost always overlooked by public policy. But not today. That's why we're here.

So, let's start with definitions first. The contingent workforce is diverse and large. It includes full-time workers, part-time or seasonal workers, white collar consultants and independent contractors, some of who are highly paid; some of who don't even make the minimum wage.

It includes blue collar workers such as printers, security guard, maintenance professionals and factory workers, a significant number who used to be in the regular employment sector. And just to make things even more complicated, many traditional jobs use contingent work to add to their earnings.

So, the same person can have both a regular job and drive a cab in their evening. And some people do contingent work because they have to, and some people do it because they want to add additional income. So, with that very clear definition (Laughter), we have a wonderful set of ideas and programs of how to address it, but let me just give you a couple of facts.

We know that there’s about 11 million contingent workers, and that’s about 8 percent of the employee labor force. On average, these employees earned about 13 percent less per year, and that’s even controlling for full or part-time or seasonality. They are 2/3 less likely to have access to a work provided retirement plan than if you had worked in a traditional job, and there’s quite a bit of evidence that suggests these folks are not saving for retirement.

So today, we're going to hear from the wonderful David John who will discuss his paper with Bill Gale about different options that will help these contingent workers save for retirement. I look forward to hearing all of the great ideas and discussing them with our wonderful panel afterwards. David? (Applause)

(Audio dropout)

MR. JOHN: -- the key question here is whether I can figure out the clicker (Laughter). Then we’ll worry about the other things. There it is. Well, thank you, Deb, and welcome.

When we were starting to work on this paper, I walked through my train -- I take a train every day to and from Washington, and I asked several of the people that I know there what was their idea of what a contingent worker was. And a couple of the younger people there immediately said oh, well you know, I've got friends who drive for Uber. Or one of them said I've got someone I know who produces products for Etsy and various and sundry others, and that's what a contingent worker is.

And then I talked to another guy, slightly older in a suit and tie, and he said, oh, well I'm one of them, actually. I'm an independent consultant, and I charge x thousand dollars an hour when I do this, that and the other. And I move from place to place. It's the best career ever. You should consider it. He didn't offer me a job, but that's just as well (Laughter).

Then, I went to a guy that we talked to fairly regularly who is a retired D.C. cop. And he said, well, I'm a contingent worker. I wish I wasn't. And he pointed out that he was -- when he retired his pension wasn't enough for him to just stop working, so he works as a security guard in a couple of different companies over the course of the week, and he works for the same Uber employer, over (sic) employer, but he goes from job to job and they treat him as an independent contractor and take absolutely nothing out of his pay, and he has to pay for everything going forward.

So as Deb said, this is an incredibly diverse heterogeneous group. Some of them are there because they want to be. Some of them because they're not. We have numbers ranging from the 8 percent that Deb used, which is one that comes from a GAO paper, and we have a more recent one which suggests they could be 16 percent. And frankly, depending on the definition, we came across somewhere between five and seven different definitions. One of them is so broad that it actually (Inaudible) as 40 percent. So hypothetically, everyone on this side of the room is a contingent worker. Congratulations.

As Deb mentioned, these workers do tend to be less advantaged. They tend to earn less. They have virtually no job security. Some of them have additional jobs, roughly 3 in 10. We think that this is a second job, the contingent job, et cetera. But we have a very hard time getting a handle. And because we have such a strange lack of definitions, we're not sure that they're actually always counted in the coverage statistics. So it may well be for a full-time contingent worker, that the retirement savings coverage, the pension coverage is actually worse than it appears in the official statistics.

If we have problems defining who our group is, it gets even more confusing when we start to look at retirement savings and the retirement option. We have again, roughly earning 13 percent on average less than a traditional employee, and this controls for the part-time aspect that many of them are there.

Many of them have irregular earnings, and this can include retail workers who hypothetically are employed by a company, but they're on an on-time basis, so basically, they may show up and there's an algorithm that the employer has that says sorry, we don't need you at the moment. And since we don't need you, you know, we won't pay you for this period of time.

We know that they have typically lower access to any sort of a traditional retirement savings plan, and we know -- GAO did some surveys for one of their papers, and we found that for roughly a third of them, this lack of benefits is a very serious concern.

Of course, and people will say, they could save in an IRA. But the simple fact is, if you don't have a payroll deduction, most people don't save in an IRA. We have one set of figures that suggests for people between 30 and $70,000 in income, that maybe 1 out of 20 actually saves regularly in an IRA. And it's one thing to have an IRA, but unless you consistently contribute to it, it's really not doing that much, except maybe as a status symbol.

Now, again, just to clarify here, a word on the data. We don't have decent data sources on this. The ones that we cited, the best ones we could find, the best ones we could develop. But they're estimates, and frankly, this is something that needs to be much more thoroughly explored, especially as the number and percentage of contingent workers continues to rise. So there is a growing need for this type of work.

But given this, with the diversity, we came up with a variety of ideas, solutions, et cetera that -- some of which are less bold than others. But we feel that there is no one solution that’s going to fit everyone here; that because of the diversity, some of these ideas will work for some, some will work for others. For yet others, we still need much more work.

The first one that we're looking at is actually FinTech. And the FinTech model is developing solutions as we go. Already, Lyft drivers have the ability to do a payroll deduction IRA through Honest Dollar. Uber has a new arrangement with Betterment that gives them access to an IRA, and it gives them some level of counseling as to how to save and the like.

But it gets beyond that. If you look at one like Digit, and I use .co means company -- it’s one of the new -- it really isn’t a misspelling. But if you look at Digit, Digit connects to your bank account, and it actually has the ability to determine when you have extra cash based on your usual spending needs, and it will sweep it into a savings account. Now, this is a short-term savings account, typically, because you can access it, and this is very useful for people, for instance, who have variable earnings. But it also could be used for retirement savings plans.

Recognizing the need for some sort of the benefits, we have a couple of platforms that have started to appear, which actually offer people benefits as part of the payment structure. So for instance, if you look at Hyr and Peers, in both cases, the people who are employed by them or through may be sent to various locations. Hyr is aimed, evidently at retail workers in particular, and the benefits, which include payroll taxes and things along that line, are actually deducted from earnings before they are transferred to the individual. So with Hyr, an individual, let's say a retail worker, might work for Store A on Monday and Thursday, Store B on Tuesday and one of the other days, et cetera, et cetera, and receive a paycheck regularly from them.

One of the things that we're seeing, and Honest Dollar has a patent pending for this, is that you could actually set up several different savings goals to be automatically populated through deductions at the time that you're paid.

So with Honest Dollar, they were originally talking about the idea, well, you could save for a new TV or a car, or you know, for a vacation over here or something like that. But you can also set this up very easily so that the initial amount of money goes to your estimated tax quarterly bill, an additional amount of it goes to your retirement savings program, and the rest of it goes into your checking account. So basically, the technology exists now to assist with this, as long as individuals have access to these services. And we'll get to that in just a moment.

Just a couple of quick, other incremental changes, one of which is the state-sponsored retirement savings plans are currently aimed at employees, just as the ERISA plans are. However, in several states, there have been discussions that maybe as a tier II or a tier III, they would open this up to non-employees, contingent workers.

Now, this is actually an approach that's already taken in the MyRA, because when the MyRA first went live, it was available only through payroll deduction. Now, it's available through a web site where anyone can sign up and save through the MyRA through a direct debit vet.

And last but not least, in the incremental areas, we have a couple of areas of tax reform that could be done. We think that the Saver's Credit could be modified to make it essentially a match for savings, which would then build the contingent workers' balances much faster than if it's in the current system, plus the fact that very few workers of any sort know that the Saver's Credit actually exists. And we think that that can be dealt with. Then, we can change the contribution limits so that any married couples can save.

But the more fun one here is an employer-facilitated account. And an employer-facilitated account is universal. It would work for all workers; employees and contingent workers. It's portable, like Social Security, so it would go with you from job to job. And the reasons are very simple. Coverage depends currently on an employer for the most part, if you're going to get a payroll deduction.

With the employer facilitated, that wouldn't be the case. The biggest problem as far as leakage from a retirement savings account comes when people move from job to job. And if you have one account that moves with you, that part of the leakage becomes much harder to come up with.

And last but not least, we have an increasing number of people who through their careers are going to be both regular employees and contingent workers. The value is that for the employee, they have one plan with one investment option that follows them from job to job. And this is true whether they become an employee for 25 years, or whether they are on a contingent thing for 30 days, et cetera.

For the employer, it allows them to offer a plan of any type that they choose, and I'll get to why in a second, and it allows them to decide that as to what type of workforce they want and can retain. The employer account under the proposal that we have would change characteristics. So, if I am an employee and I go to work for someone that offers a 401K, my account becomes a 401K and can receive employer contributions, and has the higher contribution rate.

If I then go to work for someone that doesn't offer one, they would offer me a payroll deduction IRA, and in case you haven't figured this, every employer would be required to offer some form of an account. And at that point, it would have an IRA contribution limit. There wouldn't be an employer contribution, et cetera. We believe that there should be a uniform set of withdrawal rules and various and sundry other activities there.

On employment, the employee would provide the routing number for the retirement plan. And this is exactly the same as providing your Social Security number now and providing your direct deposit for your paycheck. So essentially, this does not include a tremendous amount of additional work.

The employee, as I said, has one account. It has a default investment option. It may change providers at any point. The initial provider would probably be chosen through some form of an automatic revolver assigned choice similar to what New Zealand uses for a kiwi saver. So, I go to work. The account is set up. It is pretty much a commodity, and I would be assigned to a provider, and I would carry that provider, unless I decided always that I wanted to provide -- move to a different provider or a different type of investment with that provider.

For the employer, this has an advantage because it substantially reduces the amount of work that they have to do to provide an account. They still have to provide something for everyone, and because of the anti-discrimination test, they couldn't just say, well if you're at such and such a level, I'm going to give you a 401K with such and such a match. And if you're at a lower level, I'm only going to give you the auto IRA.

So basically, this encourages them to make a decision, much as they do now, as to what type of account they want to offer. And you'll notice that we have a regulatory idea there, which would include the CFPB, which has been known to be a little bit controversial on occasion, but we think makes some sense here.

Two common concerns, as I close here. First is people are concerned, well what about the fees. And the fees would be commoditized, so that an employee would receive a certain type of account, unless they chose something else. We also believe that the fees should be disclosed and that there should be a very strong encouragement to keep the fee level as low as possible.

And the second one is that we always get the question -- we've gotten this with the automatic IRA since the very beginning. Well, won't this encourage companies to close down their 401Ks and move to something that's simple? And the answer is really no. And the UK has got a similar movement here to require all employers to offer some sort of a retirement account, and it has not had that effect.

So, what we have seen is that if you closed your account, or if you closed your plan for your employees, the ones who are going to be most affected are going to be the top level managers that you most especially want to keep. We have discovered through some fairly interesting discussions that most companies like to keep their top managers, because essentially, they're well-paid for a reason.

So, what we have here is an interesting, diverse problem that needs resolution. We have a variety of proposals, because as we say, we don't think any one proposal is going to meet the needs of everyone. The one that we think is the most radical, but probably the most valuable in the long run is one where we move to the idea that everybody has an account. The account moves with them. Again, this is the same model as Social Security. And we believe that this would actually assist workers, especially contingent workers, but also with all employees. So with that, I'm going to stop, and we'll now hear from our various and sundry respondents. (Applause)

MS. WHITMAN: So in keeping with brevity, I'm going to make sure that everybody comes up here.

(Discussion off the record)

MS. WHITMAN: And as I get mics, I will give the very briefest of introductions for people that probably need none whatsoever. Ida Rademacher is the executive director of the financial security program at the Aspen Institute. We also have the wonderful help of Seth Harris who is a distinguished scholar at Cornell's University

School of Industrial and Labor Relations. He was both deputy secretary of labor, and also, acting U.S. secretary of labor.

I'm going to ask my first question from here, and then I'll mike myself while I go. But David provided a whole range of different solutions to this very complex problem. So, FinTech, state-sponsored retirement savings plans, MyRA, tax reform, employer facilitated accounts.

Asking both of you, which of these options do you think could be most successful to address the problem? And which is your favorite? And what are you concerned about of these really interesting ideas that David has put on the table? We'll start with Ida.

MS. RADEMACHER: Yeah, I'll go ahead and start. Thanks, Deb. And I also want to thank Brookings and thank David and Sarah for writing this paper. Essentially, for writing it before you have the solutions, because I think these discussions and landing on the specifics, it's important to have these dialogues to get to that place, versus kind of doing that in the corner, coming out and defending them to one another. So, kudos to starting it there.

And then just a little bit of -- in terms of who we're talking to, my sense is that there is also two different audiences listening to this conversation right now that we should keep in mind. On the one hand, there is a growing set of folks really focused on the future of work, both on the flexibility that it's going to provide workers, but also on the growing precarity and insecurity that some of these implications have.

At the same time, there is a whole audience within the retirement savings and investment ecosystem, and they're looking in some ways, at the disruption to the market that this trend could pretend. And you know, my sense is that again, being mindful that both sets of audiences have valid concerns and that this conversation needs to be happening in tandem is great with that sense.

My main coming away from the paper, and my own main kind of sense of this as I read and we look -- at Aspen, we're looking at both retirement security issues and income volatility and the growing level of kind of precarity in the workplace. My sense is that in terms of having a retirement security conversation ramp up in this country, unless we use inclusion as the overall framework for having that conversation, I don't think we're going to start in the right place.

The adequacy conversations, the de-cumulation conversations are all important, but if we continue to talk about really, only half the country's workforce, it's not going to end up in the right place if we don't start at the right place. And then you know, quickly, in terms of one quick thing on each of your points, and then we'll turn it over --

MR. JOHN: Yes.

MS. RADEMACHER: You know, I think the FinTech piece, and you couldn't have even written that a couple of years ago. Right?

MR. JOHN: No.

MS. RADEMACHER: And the FinTech piece was really started in some ways more on credit, and it's really started to move into retirement. You know, I do think that the conversation we need to be having in that space is, does innovation necessarily and always lead to greater inclusion? And does it -- and how well do we understand the consumer protection issues in that space?

MR. JOHN: Mm-hmm.

MS. RADEMACHER: I also think that while it's terribly exciting to see the innovation and the starting point of inclusion, a lot of business models get to the point where small dollar savers aren't where you can stay focused. And so even though some of these kind of market driven inclusion starting points may not stay there, and I think we need to think hard about you know, how far those -- and include those companies --

MR. JOHN: Yes.

MS. RADEMACHER: -- in that part of that conversation. In terms of states, again, that's where a lot of the legislative innovation is coming from. I think that's great. I also think that in terms of the guidelines and the rules that have come out of the Department of Labor, though, the only time that ERISA carve-out is going to be there is if the size of the employer is written into the legislation.

MR. JOHN: Yes.

MS. RADEMACHER: And in only one state has the size of that employer gone to zero. So, this whole contingent work thing, really, is still -- you know, if you're in Illinois and the work starts at employers with 25 employees or more, you can't really just say that's going to work for contingent workers, because there's a huge risk of legal implications and there's definitely going to be testing the viability of these in legal ways, even though there's an ERISA, you know, rule that's come out of labor. So, that's what I'd say about the state work.

And I think, you know, the only other thing to say in terms of your -- I think it's exactly the right question to look at. Do we continue to couple this as an employer-based account or as a facilitated account?

MR. JOHN: Yeah.

MS. RADEMACHER: And my own sense of that is that really, this longer term change to facilitated, but where this becomes like a phone number that you take with you, or a Social Security number. That portability level is pretty fundamental to the success of the system. So, sorry that's long, but that's my opening response.

MS. WHITMAN: Great. And Seth?

MR. HARRIS: So, thank you, Deb. I think the answer to your question is actually a question. And that is, how do you eat an elephant? And because retirement security and the retirement crisis is an elephant-sized problem. And the answer, of course, is you eat one bite at a time. And so I think this paper did an excellent job of taking a big bite out of one of three big pieces of the retirement crisis.

Of course, the crisis -- this paper focuses on coverage. The other problems, of course, are adequacy, meaning we have a lot of people who don't have enough money to retire; either none or not enough. The second paper will take a big bite out of that issue. And the third, of course, which is reference -- in David's presentation is leakage; and that is that retirement money ends up being used for non-retirement purposes, whether it is people taking money out to pay for a new car or to pay for a medical emergency, or money being funneled to financial institutions for fees or excessive risk or other things.

And all of them are important, but you can't swallow an entire elephant all in one bite. So this paper, I think, does an excellent job of getting us started on coverage, and the answer to your question -- the direct answer to your question, Deb, which of these options should we pick, is all of them and more.

I think the paper does an excellent job of highlighting that coverage actually has two parts to it; at least two parts, but two parts that are addressed in the paper. One is access -- the access to a retirement account. There are many, many, many too many employees putting aside independent contractor and others -- and we're going to talk about that in a minute, who simply don't have access to an easy retirement option.

The IRA market is always there. David, appropriately, sort of dismissed it as an option and sort of a -- I don't know if it's a status symbol, but it really is not a sufficient alternative to employer based. It's simply too hard and too complicated for a lot of folks. So, access is a big issue and resources are a big issues.

One of the reasons people don't save money is because they don't have money. For 35 years in the United States, we've had stagnant and declining wages for a very sizeable percentage of the American workforce. We all just saw census release data that showed that family incomes have increased in the -- by the largest amount. Median family incomes have increased by the largest amount. They've increased in the life of that data series, decades and decades and decades, and yet, still, median family income is below where it was before the great recession.

So, if people don't have enough money to save, the question is, how do we get money into a savings entity, a savings enterprise for their retirement that's not called Social Security, because Social Security is intended only to replace about a third of people's pre-retirement wage, a tremendous problem.

And if the elephant weren't big enough, David went out -- David and Sarah and Bill, and I want to congratulate all three of you on this paper -- they went out and made it even harder by picking this very difficult to define group of workers who are especially vulnerable to the retirement crisis. This is sort of substantiating my argument that we need all of these solutions, and more.

And David is right. There is not good data, or let me just say there is a lot of data, most of which doesn't agree with one another. I like to think of this group of folks being in three buckets, and the bucket in which you put them is very important for what solution you end up delivering to them. So there are traditional independent contractors who don't have an employment relationship. That's the definition, in a sense. They're independent businesses.

Then, there are traditional employees. And let me say the overwhelming majority of Americans are still in some kind of a traditional employment relationship with someone. And then, there's lots of folks in the middle who are in some kind of a hybrid economic status. They may have an employment relationship. They may also drive for Uber or Lyft. They may be a part-time worker. They may be a temporary staffing agency worker.

Some of the folks, my friends Alan Kruger and Larry Katz captured in their very valuable paper. So we have to figure out who it is that we're trying to help, because the solution is partly driven, or the vehicle for the solution is partly driven by their relationship to an employer. If you have a relationship with an employer, the employer can be part of the solution.

They may not want to be, but they can be part of the solution. For independent contractors and others who don't really have an employment relationship of any kind, whether it's an unstable one, a changing one, serial, contemporaneous, multiple employment relationships, then it's a very different discussion. Right? You may need some kind of a government solution or a market-based solution when you're dealing directly with those kinds of folks. So, here the focus, it seems to me, is on that middle group.

MR. JOHN: Mm-hmm.

MR. HARRIS: Less on independent contractors and more on that middle group, which is important, because lots of people are going in and out of these statuses, and it's very, very, very, very complicated. If you spend as much time talking to Uber drivers as I do, you'll find that -- you know, I actually got a lift to the airport from a guy who was driving me on his lunch hour from his job. Right?

So what are we doing with that guy? I mean, that's a complicated thing. He's trying to supplement his income. He gets up at 3:00 in the morning to drive before work. He drives at lunch. He drives after work. He's just trying to accumulate lots and lots and lots of money, some of which comes through his employer, some of which comes from other -- what are we doing with that guy? All right?

And that's where this paper, I think, is most valuable, is that group needs a diverse set of very complicated solutions that they can understand and access. And I think you did an excellent job. So Deb, I think that's a long-winded way of getting back to my original answer, which is, all of it and more.

MS. WHITMAN: So, I'm actually going to push back a little bit, because all of it and more, we already have a very complicated retirement system; very hard to navigate for employers, let alone individuals. There's you know, 401Ks, there's 403Bs, there's all kinds of letters out there that I'm sure David could rile off in his sleep.

But you know, Social Security is Social Security and it fits everybody. Do we need a hundred different retirement programs? And so, I push back a little bit on you, Seth, to answer, but I'll ask David. These in some ways were distinct options, and in some ways, I think your meta-solution of the employer-facilitated account could replace all of the letters of alphabet soup that we have.

Where do you see the future? Are we going to add more Rube Goldberg type plans and opportunities, or do you think we should really look more comprehensively and simplify, but try to simplify into a system that could help everybody?

MR. JOHN: Well, I think simplify is definitely the way to go, but the solutions we put forward actually can fit together. So, hypothetically, if we have an account that moves with the employee, it would be possible for that employee in certain employment situations to actually connect that through a FinTech provider, and have money that goes to retirement savings and other savings, actually, simply through that FinTech application, in addition to any money that might come from, say, an employer or a traditional system. So, I think it fits together in a number of different ways.

But it's true; we don't need 827 or however many it is, different types of accounts and situations. So, some level of simplification is in order, but at the same time, we want to have a system in the end, because this is such a complicated issue, one size is never going to fit all. So we want something so that an employer can decide what they want to offer to get and retain the type of workforce that they have. So it's going to be an interesting tug of war between simplicity, on one hand, and flexibility on the other.

MS. RADEMACHER: And if I can bridge back over to you with a couple of -- just to put them in perspective, you know, I think this unpacking of the portability and the coverage question. All right? So we know right now that the average millennial switches jobs four times in the first 10 years of the workplace. That's double what Generation X was. It's more than that for prior generations.

We also know that people who do have accounts, a third of them have three or more, and one in six have five or more accounts. So this issue of simplicity, you know, and this issue of portability, I think it's already front and center and part of that elephant that we have the technology to address sooner versus later.

MR. HARRIS: So I don't want to be elected a spokesperson for the complexity caucus (Laughter). I'd rather be the voice of the diversity caucus, because -- and maybe this is the meta thing with my comments on the paper, this is a diverse population. I think that the paper actually acknowledges that.

And going beyond this population to the broader set of employees, even within the employment status, there are different populations who need different things. The fact that we have a diverse set of solutions doesn't mean that it has to be complex to the worker. One of the things that I really liked about the paper -- I don't want to spend too much time praising the authors, because they're going to get big heads.

But one of the things I really liked about it is it looked at the problem from the perspective of the worker. And that is how we should try to address it. How do we have a diverse and maybe complex solutions that are simple and accessible to the individual worker/retiree? So, without pointing out flaws in the paper, because I'm a big fan of it, allowing portable accounts among employers doesn't solve the problem of my getting up at 3 a.m. Uber driver who is earning income in an independent -- what is now an independent contractor relationship with an online platform.

That money doesn't flow and wouldn't flow into this system. What do we do with that guy and the extra earnings he's bringing in? Right? Should we be tax protecting some of those earnings? As an independent contractor, those earnings are not tax protected. Maybe we should, not just the growth, but the actual -- the initial income.

So I'm not for complexity. It's already complex enough, particularly -- let me just say, if you break into a conversation about retirement products, that's a sure way to make everybody's eyes glaze over. And if you pile that on top of vehicles, it becomes much too hard. So part of the challenge, and the paper takes this on, I think in a very smart way is, how do we make it easily accessible to the worker?

The idea of one number, like the Social Security number, I think is brilliant, and that's where we need to go. Ease, simplicity so that the worker or the independent contractor doesn't have so many choices that they're frozen. They end up in analysis paralysis, and that they are guided by an expert in making the decisions.

Let me make one more point. I apologize for filibustering. And that is, one of the concerns that I have about the system and many systems is who is responsible for growth in this system? Who is responsible for the responsible stewardship of the money? Who is responsible for making sure that the retiree gets out what they need to get from their system; helps them to figure it out.

My friends at the labor department just issued a rule that deals with a slice of that, but in this context, it's not entirely clear. And I worry that we may lose some of the advantages of pooling, when we look more at individual accounts than when we look at group accounts in some form. Now, this system doesn't exclude the possibility of group accounts. I would have liked for you to say a little bit more clearly, pooling is critically important. We've got to find a way to keep people's money together with other people's money to get the maximum advantage for the worker.

MR. JOHN: Let me say explicitly that pooling is essential, and one of the things that we are looking at and probably will be looking at in the future is the idea of moving beyond the retail investment of accounts into a more pooled structure that allows for lower costs and the benefits that you're talking about.

MS. RADEMACHER: Good.

MR. JOHN: In the case of the Uber driver, what I'd love to see, and we need to explore this more, is whether or not the employer is already going to be hypothetically connected to this one number, but whether the Uber account would also be connected to that number, so that the money that this individual earns during his lunch hour also can go into this savings mechanism.

MS. WHITMAN: So, question for Ida. You talked about the volatility of household incomes, I think you even used for KSD. And I think it’s not just for this population, but your research has shown that that’s rising for the entire population. And as we think about saving for retirement many, many years ago, and people are seeing their incomes bounce around so much on a given week or month, this isn’t just a gig thing anymore. What have you guys found, and how is that changing your thinking about this problem?

MS. RADEMACHER: Yeah, I think you’ve made a great point with your Uber driver on lunchtime, that multiple income streams from multiple classifications are the new normal for a growing percentage of the workforce. Aspen hasn’t done so much -- a lot of new research in this space, has tried in the last year to gather the knowledge that different people are publishing around the growing incidence of volatility and the implications of that for worker well-being and for both short and long-term security.

Because what we know from a lot of behavioral economics is that one of the first things that happens when you're balancing so many short-term issues about short-term financial security is that your ability to think about long-term and more complex problems gets greatly diminished. So you know, I think the first thing you would probably do maybe in the next questions, you start asking Uber drivers --

You know, and I think what we'll find is that most people, regardless of income, want the opportunity to save. They want the opportunity to make those decisions for themselves, have some agency in their futures. So it's really important to not just decide that Social Security is the solution for them.

And by the way, in terms of worker classification, unless you're making that conscious decision that you're actually a self-employed (Inaudible) worker, you're not actually thinking about quarterly taxes. There's actually a pretty large percentage of people who don't know that they should be putting away taxes.

MR. JOHN: Right.

MS. RADEMACHER: So, we actually are potentially exacerbating the kind of income shocks that households are going to be dealing with when it comes tax time. So that's one implication. And the other implication is, they're not actually going to be paying into a Social Security system that is supposed to be the bedrock for a lower income worker, because they are not actually actively engaged in that system.

So again, there are technology solutions, but unless there's a regulatory and I think a societal discussion about the values we have or about long-term security, that's going to be the case. You know, the volatility issues, I'll say, you know, a couple of different data points that really drew us to that issue.

JPMorgan Chase Institute put out a look at all of its -- you know, over a hundred-thousand-person sample from its data. They saw across income brackets, 55 percent of their customers were experiencing -- saw income swings month to month of 30 percent or more. That's a very similar number to the financial diaries which will be putting out a book next year, that they saw that the families in their study, which was a much more intensive kind of study, that five months out of the year, the families in that study were experiencing monthly volatility of 25 percent or more.

And there's another research paper out yesterday of a set of 900 workers

-- shift workers mainly from retail stores, experiencing month to month volatility of 30 percent or more. So this calls into question both the direct deposit mechanisms of some amount every month that gets taken in. But I think the other thing to point out is not --

And then we also then built a panel of folks to weigh in on what they thought about this research. Did we actually feel like they were confident that the -- kind of that the research was you know, valid; that the evidence base was solid, and what was the future? You know, 86 percent of the people we surveyed in that expert panel thought that income volatility was a real and growing phenomenon on a month to basis.

When we looked at the kind of data that other people are putting out, as well, on the drivers of volatility, to your point, it's not all just even in the contingent worker space. A lot of this is actually worker schedule within job volatility for workers who experience a lot of changes in hours and shift work. And so you know, a lot of this is part-time workers that don't have access to retirement and any other kind of savings.

And unless we actually, to your point, figure out a way to link short-term savings opportunities, emergency savings, financial cushions, and I also think that people shouldn't -- we should really rethink as a society, how many things should be self-insuring for versus how much is a benefit for the social insurances system not serving people well anymore. Right? The unemployment system serves one in nine people that are dealing with that phenomenon in certain states.

So, emergency savings, yes, but how much of that is actually incumbent on the individual for that risk-shifting point? And I think the final piece on that part of it is just you know, thinking about this volatility issue in the long run. It's not something that a lot of workers are going to grow out of. Right? It's not a problem that's like, oh, it's just the first part of the work time, and then they're going to get into a steady job.

The fundamental nature of work is changing. We can have labor market reforms that address that, but I think also dealing with the pragmatic relationship of people will have many different classifications at the same time and over their lifetime. And unless these mechanisms are automated and in some way universally -- you know, I know we hate mandates, but I think that there's some real need to kind of look at this from a cost perspective.

If people aren't just helping save for their own futures, what are the costs going to be for the different states and those different you know, insurances when some people get older? So, I don't think it's trade-off of we do nothing or we do everything. I think we have to look at this holistically.

MS. WHITMAN: Thanks, Ida. I want to give the audience a chance to ask questions in a second. Do we have some time for that? But first, I have a quick question for each of you. We're in Washington. We talked a lot about the ideas. What are the chances that any of the wonderful ideas that this program put together will actually see their way into law and into action within the next five years?

MR. HARRIS: Pschew. I'm hesitant to even project how the election is going to come out. And projecting five years in politics is a challenge. I think there are solutions to this particular problem and others that don't cost money and don't require a mandate that are achievable, and I think actually, the odds are pretty good that they will be achieved, not in five years, but in the next 18 months; maybe a little bit longer than that.

Once you start talking about employer mandates and spending money, the politics become fantastically complicated on Capitol Hill. The Republican party is split on this stuff. The Democratic party, just understand, is also split with those who want not a public option, but a public solution, you know, and a dramatic expansion of Social Security to try to address this problem.

And there are others who see the private retirement system in some form as a solution, although they recognize the desperate need for reform. So, I am optimistic in one respect that we can chip away at aspects of this problem; take bites out of aspects of this problem, but getting to a global solution that's as sophisticated as this one, I think is going to be a very, very big challenge.

MS. WHITMAN: Ida, are you more hopeful?

MS. RADEMACHER: Well, I think I'm hopeful. I'm in agreement that I think there's some short-term places where there's already a lot of movement on both sides to come to consensus and to implement some solutions. So, the pooling area, the part of open maps happening, the idea of that -- the market both -- I would say the market in two dimensions.

We can expect to see change in some of that enabled by new legislation that could come through that really lets some of the existing market players help to pull the risk. But honestly, a lot of that is pooling the risk with small employers, and it's going to be a question whether that also will expand to pooling the risk for contingent workers.

MR. HARRIS: Right, right.

MS. RADEMACHER: And I think the other part of the market is, really again, I think you've nailed that in terms of the financial technology. And really, what's capable of being done right now -- there's a lot of market uncertainty in terms of what people can and can't do. I think that part of that speaks to other kinds of policy change that we could do.

We should look at some of the things like red tech sandboxes. We should look at how do we get regulators and legislators really smart about the kinds of changes going on. I would love to see that happen in the context of growing a plan that is an inclusive plan that solves the problem for all workers. But I think the short-term piece, there's a lot of parts in motion. The longer-term piece, I actually think we need a broader set of people at the table to have the conversation about what actually needs to get solved and for him.

MR. JOHN: I agree with what's been said. I mean, luckily, certain of the solutions don't require Congress, and I think one of the things that we may see, if we continue to have essentially a dysfunction legislature is that we will continue to find ways to go around it; whether that's through the states, whether that's through FinTech or various other things.

But let me just take a quick second for one other purpose. Bill and are the ones who are standing up here today, but this paper would not exist without Sarah Holmes, who actually did a tremendous amount of the work. (Applause)

MS. WHITMAN: I'm going to turn it over to the audience. We do have people watching online, so wait for the microphone. Also, please introduce yourself and keep your question to a question.

(Audio dropout)

MS. WHITMAN: -- person in the back.

(Audio dropout)

(Simultaneous discussion)

MR. GOTBAUM: You all had made -- Josh Gotbaum, Brookings. You've made the point that this needs -- in order that -- you need a new kind of retirement system in order to solve this, and that it needs to be universal and it needs to follow the worker.

One consequence of that is that (Inaudible) oversight, it's not clear who actually provides oversight. Who actually -- since it has to be simple, and since workers -- most of us don't understand our retirement systems, anyway. The question is, who oversees the store? Who watches? As we all know, at the moment, the financial services committee is overseen by more federal agencies than any of us can count. And to your credit, David, in your paper, you said I think this should be regulated by some combination of the Department of Labor and the Department of Treasury and the

Consumer Financial Protection Bureau.

Would you all at least talk a little bit about how we can have something that is universal and simple and effectively overseen --

(Audio dropout)

MS. WHITMAN: Do you want to take that, or Seth?

MR. HARRIS: Let's have David start.

MR. JOHN: Okay. One of the things that I've learned over the years in Washington is that jurisdiction and control over certain issues is jealously gardened and is basically taken out of a regulator's cold, dead fingers, at best (Laughter). So, I would love to say if we were starting over, this would be unified in one area. I don't necessarily think that reality is going to be with that.

But given the fact that this is a consumer oriented account, it is a financial service, it is one that the individual will have and needs a tremendous amount of structuring, shall we say, I think it makes perfect sense to turn a significant portion of this over to the CFPB.

MS. WHITMAN: Seth?

MR. HARRIS: That's so not going to happen (Laughter). That's a great -- oh my god, is that not going to happen. Joshua had been in the meetings where the struggle over jurisdiction in this space has played out as a slow rolling feud, I guess it is. I think feud might overstate it slightly.

So going back to my three buckets; different regulators have responsibility for different buckets. And CFPB is not really in this space in a meaningful way, but they could be added in. And it may be that there's a bucket for them, as well, or that they are the bucket masters, or in support of the work of the others, because the work with CFPB is really quite substantively different from the work of the Labor Department and the Treasury Department.

So the employee bucket is pretty clearly the Labor Department. The non-employee market is very much the Treasury Department. It's that middle space in which you are operating where it becomes a lot more complicated, and they're going to have to work together.

When you said, David -- just to give you an illustration of the complexity here, when you said that you would love to have a single number where my Uber driver could put his employment earnings and his Uber earnings, a bunch of regulators' heads all over Washington exploded, (Laughter) because you crossed territorial and legal lines in doing that.

MR. JOHN: Right.

MR. HARRIS: So that's going to be a very, very hard thing to do. But I like that the (Inaudible) didn't have to solve that problem. You know, let's let the regulation follow the solution.

MS. RADEMACHER: Well, I think the only thing I'd add to that is, you know, what I think is ultimately coming to play in the retirement space, and maybe more than any other is that you know, people have been navigating increasingly complex labor markets, and we're adding to that in an explicit conversation about navigating increasingly complex financial markets and financial decisions.

Unfortunately, there has never been an over-arching bureau until the last couple of years, so that it's still in some ways, going through the punch list of what it's mandated to do, and in other ways, trying to figure out how it plays in this system over time. I do love that you see this happening in the marketplace, that human center design is driving innovation, is driving companies to put you know, a friendly skin on the types of products and services that are out there.

I think that part of getting to a solution, given the tensions that you're talking about is, again, really needing to understand what kinds of technology that regulators don't really understand yet can help to facilitate a solution where everybody's jurisdictions come into some kind of a place where they can look together at it through the lens of consumer financial well-being. And I do think that that's going to be -- I would love to hear more of that be part of the leadership that takes this conversation forward.

MS. WHITMAN: Sorry. We have less than five minutes left. I want to make sure that I get two questions, and then our answers will be brief. So, there's a hand up right there.

MS. WHITE: My name is Elizabeth White, and my question is what do we do in the meantime? I saw a GAO study that said for Americans 55 to 54, 29 percent have not saved a dime, and that the median value of retirement accounts was something like a hundred thousand dollars, which generated an annuity protected -- inflation protected annuity of 300. So that point, because we have a lot of people who are in trouble now.

And then I think many people saw Neal Gabler's piece in *The Atlantic* in April, which said that 47 percent of Americans cannot pull together $400 for an emergency. So, we keep talking about workers, like they're all minimum wage people. But I think this problem also impacts people who have had career choice privilege and significant incomes and have not put away nearly the 10 to 15 times their income that they needed to retire. So it's the meantime question, and then broadening who workers are, because it's also people in this room.

MS. WHITMAN: Ida, I'll let you take that briefly.

MS. RADEMACHER: Yeah, I think it's exactly the right question, and I take heart that more and more people are asking the question about from a place of deep insecurity that goes well into the middle class. What do we do now?

You know, I wish I was -- I mean, obviously, there's no magic bullet. These changes that we're talking about our multiple year changes in the cultural norms and the political will to solve a problem that's almost like a global climate change problem. Right? The problem is out there. The tsunami is out there, but it's not hurting me today, and I have really big problems today that I have to solve first.

The fact that we're actually -- the way that our markets are set up right now, driving people to make a choice between their short-term well-being and their long-term well-being and putting that risk as well on the individual isn't going to serve us well as a society. So, I would love to see multiple marketplace and regulators and elected officials and public advocacy groups really join together to think hard about how we're going to pool risk differently in the short-term and the long-term.

It's not meant to be a punt of an answer, but I think that you know, solving the great retirement crisis, and we've been talking about this quite a bit --

MR. JOHN: Mm-hmm.

MS. RADEMACHER: The first leg of retirement savings has got to be emergency savings, because honestly, with this increasing volatility and 25 percent of people pulling money out -- I'm not going to call it leaking anymore. It's for usage. It's for every day usage to get through, and they have a choice with that money.

We've got to solve this problem so that these people can think about their entire life in a long-term horizon way. And I honestly think that in some ways, the unfortunate piece is going to be that it will be the crisis that is going to happen, because people don't have the preparation. It will be the awful stories we're going to hear about people losing their dignity and people really struggling in poverty as retirees that are going to drive us to say shame on us as a society and decide to come together and solve the problem.

MR. JOHN: And let me just point out that some of us who work on these issues divide them very neatly into retirement savings and other savings. And the bottom line is that this is one problem with a number of different aspects.

MS. WHITMAN: And that's -- I'll take license just to say, while on the federal level I may agree with Seth that it will be a time. We now have 26 states that are looking at creating their own retirement based system. So, places like California, Illinois, Oregon, Connecticut, my home state of Maryland are all moving forward into the one solution that David talked very briefly about.

So, things are changing, because I think we, as Americans can't wait 10, 20 years for this problem to be solved. So thank you for that question, and thank you to my amazing panel, and also, to the authors for this really thoughtful paper that answers the question that most of the time, we don't talk about in public policy. How do you deal with the really complicated folks?

Usually, solutions come that are for the easy problems. And so I applaud the Retirement Security Project for pulling this together. I'm going to briefly introduce Josh, who introduced himself as formerly of the PBGC and ask him to come up with the next panel, and now of the Brookings Economic Studies. (Applause)

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MR. GOTBAUM: We're now going to switch to a topic which is much less complicated (Laughter) and much easier than the one that we just discussed. But in the world of pensions and retirement, that means it's simply really complicated and really difficult.

The Employee Retirement Income Security Act, ERISA, was enacted to preserve traditional pensions. Ironically, it instead began their decline. Companies that were judged by quarterly earnings decided they didn't want to guarantee their employees' retirement income 40 years into the future. And as this paper notes, guarantees are not free, and thousands of businesses decided not to pay their price.

As a result, market risk and longevity risk have been transferred to employers to millions of individual employees; employees who are almost without exception, woefully unprepared to assess these risks and make choices about them. This transition from guaranteed retirement income proceeded on many fronts. We've already noted the switched from defined benefit plans to defined contribution plans, but even for the 40 million people who are still covered by private defined benefit plans, more than 10 million of them are in hybrid plans whose benefits are not fully guaranteed. They vary to some extent with the markets.

And within 401Ks, the use of annuity options, i.e., guaranteed income options has declined. Indeed, the word annuity has been banished by marketing mavens in favor of lifetime income. And yet, if you ask people whether they want their retirement to be protected from market drops, a very large portion of them would say yes and do say yes.

This pension nostalgia has not gone unnoticed. David John, in addition to the co-author of the previous paper, a co-author of this paper, has worked with virtually all of the states that are considering legislating auto IRAs. A surprising number of those bills include a provision directing the board that designs the program to try and provide some sort of guarantee.

California, which passed the first such bill and Maryland, which passed the most recent one; both originally included a guarantee provision. So interest and guarantees were widespread, and yet, none of the states that have thus far enacted an actual secure choice program includes a guarantee. That conundrum is the reason for this paper and this panel.

After Bill Gale presents the paper, he'll be followed by two discussants, each of whom has too many distinctions for me to list them all. Fortunately, we do have their full bios. First, Olivia Mitchell, distinguished professor as Wharton, director of the Pension Research Council. And then she'll be followed by Andrew Biggs, resident scholar at our new growth, AEI -- welcome to the nabe -- and also, former deputy commissioner of the Social Security Administration.

We'll follow that with a discussion first among ourselves, and then take questions from the audience. Bill, David and Brian Kim, to whom I should give credit, as well, titled this paper "You Get What You Pay For." They could have just as well titled it "There's No Such Thing as a Free Lunch." This menu has a price list.

And so, without further ado, to take us through the menu, the director of the Retirement Security, Bill Gale. (Applause)

MR. GALE: Josh just got himself a new job as the person who's going to introduce me all the time (Laughter). So as he mentioned, the title is "You Get What You Pay For." In this paper, as Josh mentioned and hinted at earlier, is a response to the efforts at various state levels to -- the discussions that have been going on about guarantees, about the state requiring that pension plans provide guaranteed rates of return.

No state has done this yet, as far as I know. California and Connecticut studied it. Maryland discussed it. But this issue is not going to go away. It's been around. Olivia may well talk about Social Security and guarantee -- the discussion of guaranteed returns there and the privatization episodes 10, 15 years ago.

In any case, our goal in the paper is to highlight some key issues related to this point. And the one that just jumps out after looking at the literature and the policy discussion is this notion that guarantee -- costs resources. It costs money. It's not a free good. And I'll talk through that in some detail.

So, we conclude -- let's start with our conclusions. We conclude you could have guarantees. The guarantees do exist in pension plans around the world and some plans in the United States, but relative to the popular discussion, the benefits do not seem, in our estimation to be as big one might infer from the popular discussion, and the costs are considerably higher than one might infer from the popular discussion.

So let me give some background on guarantees, first, and then talk about these issues. The notion of a guaranteed minimum return sounds simple, but as we learned in the earlier session, simple concepts can get very complicated in implementation very quickly. So, you can -- the actual minimum can vary. You could have a zero nominal return, a zero real return, you could have a fixed -- you could try to have a fixed real or nominal return as an aside.

If you have a guaranteed return that's higher than the risk-free return, finance tells you you can't ensure that risk, but some guarantees are listed in terms of real or nominal returns. Some guarantees are listed as reference to some other asset. So the S&P 500 or the 10-year treasury rate or something like that.

So the actual guarantee can vary. It can apply to returns on contributions -- on all the contributions you've made in a given year, or it can reply -- sorry -- it can apply to contributions you've made in a given year going forward, or it can apply to all your past contributions and the return in the given year.

All right? You can design this lots of different ways. It can be constant. It can vary. It can be checked or enforced annually or upon retirement or upon job change. There are -- every variation you can think of, someone has tried somewhere.

What all these guaranteed minimum returns have in common is the following: That if the investment earns less than the return, then -- less than the minimum return, the insurer tops off the amount. It pays up. So, the saver gets whatever that minimum return is. If the actual return is higher than the minimum return, then nothing happens. The saver keeps the money. The insurer doesn't make a payment. So from a finance positive, the saver obtains a put option from the insurer. All right?

Now one of the benefits of these things -- the first thing to notice for people, the core retirement package is Social Security and Medicare. And that provides a base, and we can argue about whether that base is adequate, but for purposes of the discussion, the important point is that the importance of risk in returns declines as the base increases.

For those who have the base, plus a large amount of retirement savings, the guarantee does not seem to be that important, precisely because they have a large amount of savings. For those who have very little retirement savings, retirement savings makes up a small portion of that overall portfolio of Social Security, Medicare and owned retirement savings. So again, there are questions about how valuable the guarantee is.

Now, you can do all this formally, but we're doing it very intuitively at this level. And then those are the gross benefits. The net benefits have to take into account that someone has to pay for this, and unless it’s taxpayers, it’s going to be savers. The insurance companies, the provider of the guarantee is not going to bear the burden of the guarantee. Either the saver is going to buy it or taxpayers are going to be left holding the bag. Okay?

In terms of the cost, this is where the public discussion really gets lost. The cost typically is recorded as the inflows and outflows to the government budget. That is a problem for two reasons. One, typically you're discounting at the government’s borrowing rate, but second, you're focusing on cash flows. You're not focusing on the opportunity cost, the resource cost of giving that guarantee.

And the economic costs -- the resource costs, the opportunity costs should not depend on whether the government or private sector is issuing the guarantee. So using government borrowing rates and using government cash flow is going to systematically understate the resource cost. But that’s the easily comparable thing to do, so that’s what often gets done.

All right. So let’s talk about who pays for this. Obviously, if there’s no charge -- if a state government were to tell -- to require that employers provide guarantees, one option is that the state could pay for it. Taxpayers could pay for it. The more likely option is that savers will end up paying for it in some form or another, some explicit or implicit form.

The most obvious way savers would pay for it is if they paid a premium, just like an insurance premium. Now you might say, well, the firm might -- you know, maybe we could require it for -- so that the firm pays the premium, but most of the evidence suggests that workers bear the burden of those costs, just like they bear the burden of the employer’s share of the payroll tax, and most economists, myself included, feel that workers end up bearing the burden, regardless of whether the burden is placed on the -- the explicit burden is placed on the firm or the worker.

All right. The second option is what’s called rate of return collars. And the idea here is sure, the saver gets a minimum guarantee, but the insurer then caps them at a maximum return. So a collar might be, we're going to guarantee you a minimum of 2 percent and then anything above 6 percent, we're going to claim as the insurance company.

And the saver then, is paying for that, in that they are foregoing the chance to get returns higher than 6 percent in the example. So in the few years when it returns 10 or 12 or 15 percent, the difference between that and 6 goes to the insurer. And then in the other years, the insurer is making sure they get at least 2 percent, say. I’m making up the numbers, but that’s the type of range that people often talk about.

So, just as an aside, if you have a plan with a fixed rate of return where the minimum return is the maximum return, all right, that’s a collar. It’s just a very compressed collar. It’s a very, very tight collar.

A third option is portfolio constraints. That is, the insurer can tell the saver, all right, we will guarantee a return, but in exchange, you have to do the following. And this is where the real mischief comes in, because if you want to guarantee somebody a T-bill return, they could do that themselves. All they have to do is stick their portfolio in T-bills. If they want to guarantee of an S&P 500 return, they could do that themselves. They just put their portfolio in an S&P 500 index.

And so this guarantee is virtually costless to the insurer. There's always administrative costs. But in terms of the economic risk being born, it's costless to the insurer. But at the same time, it's worthless to the saver, because they can do it themselves.

The fun and games come in when savers decide that they want the T-bill guarantee, but they also want the option to invest in the stock market. All right? Then you have mismatched risks. You have mismatched assets and liabilities, and that's -- this is the sense in which in popular discussions, people think they can get something for nothing. They can invest in the stock market, but hey, if the stock market has a really bad year, they're guaranteed the T-bill will return.

Well, those types of guarantees are very expensive in terms of the resource costs, the opportunity costs that is created. So this is sort of the prototypical poster child for high cost guarantees where the costs are not accurately reflected in the budget.

The last option is to have a reserve fund. So in this scenario, the pension firm provider or the insurer would say we're going to give you a guaranteed return of say, 3 percent, but we're going to manage -- we're not going to give you all of the returns. We're going to manage the returns to build up a reserve fund, so that in years when the actual return is less than 3 percent, we have some resources that we can add in there. And the TIA, a traditional annuity, actually works this way. And Theresa Ghilarducci had a well-known proposal a couple years ago that also would work this way.

And of course, the key here is this minimum return that's being guaranteed, and can it aptly be guaranteed? TIA, I think, has a pretty good record over the years, but the return on that account still is significantly lower than what you would get in the stock market, for example, precisely for the risk reasons I mentioned.

And so here again, the saver is paying for this, but the way they're paying for this is they're foregoing the big up side of the return. They're allowing the insurer to take the big up side and stick it in the reserve fund. So there’s no mystery here. It’s sort of like if you don't see these last four ways I’ve discussed, the premiums, the collar, the portfolio constraints and the reserve fund -- it’s sort of like if you don't see the way that the saver is actually paying for this, then you don't get the idea. Okay?

So, let me just summarize real quickly. It’s definitely possible to provide guarantees. I didn’t go into this, but other countries do offer some guarantees. Some of them are in public plans, so it’s cheating in the sense that the public sector is the back stop there. But some plans in the U.S. also provide these.

But there’s no way around the fact that they have to be paid for. If savers don't pay it, then taxpayers will be left footing the bill. And so without commenting on each and every detailed specific case, this is our thinking about guaranteed rates of return in pensions. Thank you. (Applause)

(Break in recording)

MS. MITCHELL: Good morning, ladies and gentlemen. It’s a great pleasure to be here. This has been quite a week for retirement topics. I came in on Monday. There were three days at the World Bank on retirement pension reform around the world. There was a thing here yesterday at Brookings. There were, I think, two sets of testimony hearings on retirement. So, I’m very delighted, because you know, it’s been quiet in our neck of the woods for quite a long time (Laughter). So thanks to Brookings and Bill Gale and Josh Gotbaum for including me in the proceedings.

So, I just wanted to elaborate a little bit more on some of the topics that were touched on. And as was noted, there have been a number of pension guarantees tried around the world. Japan actually put in place a 401K plan and suggested or insisted that one of the 401K elements on the retirement menu had to be a principle guarantee option. You didn't have to pick it, but it was there if you wanted, the argument being that a lot of people weren't used to investing on their own in the 401K marketplace or the equivalent in Japan. And so this would be a way for people to get their feet wet.

In Chile, for many years, they've had since 1981, the defined contribution mandatory scheme. Ten percent of pay must go in to the scheme. And the idea there was they said all the money managers had to earn a rate of return on their investments that were within a plus or minus 2 percent tunnel of the average across all the investment managers. So the notion was, if somebody ended up making a lot more money than average, they put it into one of these reserve funds. If somebody ended up losing money below that 2 percent, they had to dip into the reserve funds.

And if one of the money managers couldn't make it, then they were absorbed by the other money managers. So that's only one piece of the regulation. There are a lot of other regulations about you can't hold assets that are too risky. They make sure they can hit this target. But so there has been a lot of experimentation. And as was pointed out, there's a lot of interest in state pension options that are being discussed now, and it has applied to cash balance accounts in the U.S., as well. So it's not a strange beast that we've never seen before.

When I served on the Bipartisan President's Commission to strengthen Social Security back 15 years ago, of course I was reminded how long it was, because it was the year of 9/11, as well, unfortunately. But so the commission was asked to think about guaranteeing returns in the private piece that would be the optional opt-out if people wanted to do that. And the commission did not go the guarantee path, basically saying as Bill Gale so cogently pointed out, you get what you pay for. It's not a free lunch.

So basically, what we've done is -- and there have been other people that have looked at some of these models, too, but to notice that the way -- this doesn't work on this screen, does it? (Laughter) We have one of these, too, where the lines mess everything up.

So the way the guarantee works is that if your individual account, your investment account is high enough, the guarantee is not in the money. But if your return or your assets fall below a certain floor, then the guarantee starts to pay out. But you basically need to have a model of how you think capital markets work, and returns and stochastic volatility, to be able to estimate what the value of that protection is. The retiree gets the maximum of a guarantee payment, which is zero if you're doing well, or the floor, minus how much is actually in your individual account. So that's the quick approach to it.

It's very important to understand, and the paper does a great job pointing this out, that depending on a whole host of assumptions, you're going to get very different cost outcomes. So for example, our analysis for the commission assumed that you put your money in from the moment you started working, and the guarantee would only kick in at retirement. So you were not allowed to take money in and put it out every single year. If you do that, that's a lot more expensive.

The guarantees, as we've said, could be various. We assume annual contributions, but again, this is all simply modeling. You do have to be very careful and very up front about what kind of a model you have for investment returns and correlations across the returns. Because as we know, capital market outcomes are stochastic, and you have to decide how you're going to model that. And so that's what we did in our model. I just wanted to illustrate, to give you a sense of magnitude, how big these costs can actually be.

So the base case was an investment horizon of 40 years. You start at 25. You end up pulling your money out at 65, for example. Let's say you were holding an investment portfolio of half stocks, half bonds, and you wanted to set up a design such that you could earn the rate of return on bonds at the end of 40 years. And that was what was being guaranteed. We costed that, and it's basically 16.1 percent of every contribution, every year over the 40 years. This is a pretty big number.

And so then, I asked you would you be willing to pay 16 cents out of every dollar for a guarantee payable in 40 years? And the guarantee is only the bottom of your return? Some people would, but I guarantee you, a lot of people wouldn't. Then if you also look at some of the different assumptions, the impacts on them, if you ended up guaranteeing only a 10-year period instead of a 40-year period, the cost would be a little bit less, 8.1 percent of each contribution.

This comes as a bit of a surprise to some people, because some people think, well, if I hold stocks in the long run, aren't I going to get more money than otherwise? And the reality is that the volatility of stocks increases over a longer holding period, and that's the way the cost is double over 40 years versus 8 percent for a 10 year holding period.

We also said, well, what if we let folks hold a hundred percent stocks, but then let -- you know, gave them only a bond return? That's really expansive. So a third of every payroll dollar contributed would go into the account, meaning you only have 67 cents left to invest. And a principle guarantee, that is you get your money back, nothing more, nothing less after 40 years is virtually free, because as was pointed out, you could invest in treasury bills and end up fully protected.

The financing issue really is where the rubber meets the road. Some folks, some countries have self financing. By that, I mean the participants in the system have to pay premiums to cover their eventual guarantees. The problem is, if it's an optional program, some people wouldn't be able to afford it, and so then you have to decide what to do if they're not going to be able to afford it.

In a pay as you go system, you're going to have -- excuse me, you're going to have the fact that the positive is it will be a universal system, but then the negative might be that you'd have to go rely on taxes or other government debt to try to keep it going over time.

So, just really by way of conclusion, I just wanted to emphasize and underscore the notion that guarantees are not free. There was an ancient Chinese proverb quoted to me one time -- I think it's accurate. They said the couple that goes to bed early to save on candles ends up with twins (Laughter). The notion is, you cannot avoid risk. It just transforms itself.

And so ultimately, the policy question is, are the guarantee costs really worth the benefits? And if so, to whom? These are just some references; some of the work that we've done in this area. But I congratulate this team on having brought this question back to bear in this context, where it's very much an active consideration, especially in the state plans. So, thanks very much, and let me turn it over without further ado to my co-commenter (Applause).

(Discussion off the record)

MR. BIGGS: Okay, I'll go from here, then. I thought I was going to be sitting down. I don't want to violate the schedule. Well, thank you very much. It's nice to be here today. I had prepared some written comments, and then when we were sitting there this morning, I rewrote them all, so I'm just working from notes, instead.

The idea of guarantees on retirement accounts has gotten increasing prominence in recent years. I'm glad we're having this event today to talk about it. But when I think about guarantees -- I've done a fair bit of work on them in the past in connection with the idea of Social Security personal accounts, they strike me as a little bit like you know, the ideas of eat more while losing weight or pay less for cable (Laughter).

They're things that sound really good, but you know, at the end of the day, don't come out very often. There is the president of Black Rock Investments who is involved with the Theresa Ghilarducci plan that Bill Gale mentioned -- you know, he's written the guarantees for retirement accounts are, I think his phrase was, essentially costless.

And yet, if you actually go to Black Rock Investments, I will guarantee you they will not -- Blackstone, sorry -- they will not give you a guarantee for nothing. And I think one of the nice things about the paper is it illustrates you know, the types of guarantees that can be offered. I don't deny that financial engineering can give you the type of guarantee that you're looking for, but it's also really helpful in thinking about the costs that are involved with doing that.

You know, one example in the paper is the TIAA/CREF annuities with collared returns on them, that you have protection against the down side, but then you give up some of the up side in order to pay for it. I'll give a quick example of how that will work, and Bill even mentioned, you know, a very tightly collared return.

If you think about it, imagine that you had some money. You put in stocks with an expected return of 8 percent. But you don't want the expected return. You want a guaranteed return. So, you can buy a put option with a strike price equal to you know, your initial investment compound at 8 percent. That put option is an insurance policy to guarantee you that you will get no less than 8 percent. Now, that's going to cost you some money. So, you can partially finance that by selling a call option that would give away any returns that you got in excess of 8 percent.

So you've got this portfolio. You're invested 100 percent in stocks, but you have a guaranteed return for 8 percent. But of course, you've got these upfront costs. And the insight of thinking about how markets price this is that the protection against the down side costs a lot more than giving away the up side.

So if you take your initial investment of $100, plus the costs, the net costs, these put and call options, which is around 89 or $90. You say okay, what sort of return am I going to get on that? You know, the total investment. The return is exactly equal to what the riskless rate of return is on treasury bonds. So if you're getting a riskless return, you're paying for a riskless return. Right? I think that's the kind of insight to think about of you know, why these sort of things are expensive; why they're not offered very much.

You know, it's important to pay attention to the cost here. If you look at state and local government pensions, you know, what they are doing, if you look at the math a little bit, is essentially, they are guaranteeing participants of 7 to 8 percent annual return on both the participant's contributions, but also, the government's contribution to it.

And the problem with state and local governments is that they're not putting any price on this. And anybody who thinks these guarantees are essentially costless should look at state and local budgets these days. I mean, they are now paying the cost of that guarantee, and the problem they had is they did not acknowledge the cost up front.

So, I think one of the real benefits of what we have here today is saying yes, there are benefits to the guarantees, but there are also costs to it. When I think about what role these can play in retirement saving, you know, I like the economist's idea of revealed preferences. You know, as Josh said, if you ask people in an opinion poll or just informally, would you like a guaranteed return or some guaranteed floor for your 401K account, everybody is going to say sure, I'd like it.

Ask that same person how much of their 401K they have invested in stocks. It'll probably be 60 percent or so. What that tells me is sure, they like the guarantee. They're not willing to pay for the guarantee. And that is the key part of if you want the guarantee, you're going to pay for it.

Again, these guarantees can structure returns, you know, and the pattern of outcomes differently than what a normal portfolio will give you. But at the end of the day, if people really wanted to be -- had a safe retirement income and they're willing to pay for it, they would not be holding the kinds of investment portfolios that they do today.

One last thing I'll touch in. These sort of very explicit financial guarantees, they're sort of easily priced, and I think that explains why the state run retirement plans have not gone in that direction. I know Connecticut -- and they had a commission that looked into this idea of offering a guarantee as part of the retirement plan, is they just said look, it's very, very expensive to do, and most people wouldn't be willing to pay the cost for it.

What you're having now, though, is more of a shift into things. Like in the multi-employer pension world you have things called composite plans, where it's sort of not a financial guarantee. It's sort of like an actuarial guarantee where they're trying to spread the cost of this guarantee among the participants of the plan. It may not be a strict, rock solid guarantee, but it's smoothing of returns over time.

But I think the key thing here is just because you're not pricing the guarantee doesn't mean the cost doesn't exist. And so you want to think about -- essentially, the participants in the plans are offering these guarantees to each other, and they need to know how much they're going to pay for it, in terms of both their contributions and the volatility of the benefits they'll get at retirement.

I tend to think that once people really understand that, they're going to be a little bit more wary of things. So you know, the experience I have working in the state and local pensions, which are you know, in disastrous shape because they've ignored the cost of investment risk is they were thinking about options for individuals going forward. We want to make the cost of those guarantees very explicit, and ideally, you want to have the people who are getting the guarantee bear that cost, so that we don't get this mismatch that's created such a problem for state and local government. Thank you very much. (Applause)

(Discussion off the record)

MR. GOTBAUM: Part of what I would like to do now is to make this a little bit harder. I don't think there's anybody on this panel who doesn't think that the notion of guarantees has a cost, and that the costs are real and substantial. But we also know that consumers of retirement products, financial products are not what Simms used to call educated consumers.

MR. BIGGS: (Laughter) Your best customer.

MR. GOTBAUM: Yes. And so part of the challenge, if you will, is that you're not going to be able to have that informed discussion. You're not going to be able to say, would you accept an 8 percent -- a cap of 8 percent on returns in order to get a 2 percent floor, or a principle floor.

In the world of retirement policymaking now, what has happened is, as we all know, the decision making has moved within the 401K choices as 401Ks have tried to emulate some of the benefits of defined benefit plans, to designing a qualified default investment alternative, which I managed to mispronounce already once today -- thank you, Olivia.

As it happens, United Technologies, a couple of years ago developed an unusual innovative one. They said our default is going to be a target date plan, but beginning at age 50, if you do nothing at all, part of that money -- of your money is going to buy an annuity that starts paying when you hit 65.

So the question is, recognizing that these are costs, is that a good idea? Is that a bad idea? What's your view? I'm trying to get you to find there's a trade-off. How would you judge that trade-off?

MR. BIGGS: For the standard --

(Audio dropout)

MR. BIGGS: -- plan like that has people putting in 2/3 stocks, 1/3 bonds and the target date hitting -- you know, they accumulate those proportions until a target date. Mark Avery had John Turner had a proposal, a RSP proposal, actually, probably six or eight years ago that said that you should take that 1/3 that you're putting that you're putting in bonds and just start buying annuities with it.

And the idea there was to move out the interest rate risk that occurs over time. You don't want to save your whole life, and then annuitize things that everything in one fell swoop at 65, if interest rates happen to be really low that year, because you'll get a lousy annuity. And so they had that proposal as a way to smooth out interest rate risk, which I thought made sense.

MR. GOTBAUM: Olivia?

MS. MITCHELL: So this is, I think, part of a broader move that the current administration has been pushing, and Mark Avery's name has already been mentioned. I think he spearheaded this effort to try to "put the pension back in the pension plan." In other words, put the payout stream back into the menu of alternatives that people can select from their 401K plans, either before they retire or after they retire.

And I think that it's a very good idea, but not for everyone. Some people are already over annuitized. That is, they have a Social Security, especially relative to their lifetime wages. If they had been a low wage worker their whole lifetime, they're going to have a very high Social Security replacement rate. If they also have a house, in a sense, that's an annuitized consumption stream, as well. And so those folks probably don't want to be annuitized any further.

Also, we know that people who are low wage and less educated tend to have higher mortality rates. And so using a population life table to price annuities for them is going to be very unattractive. So I think we have to be a little bit sophisticated about who is going to be annuitized and who won't.

On the other hand, if you're a medium or a high wage worker, so Social

Security isn't replacing all that much of your pre-retirement wage and you'd like to have a lifetime income stream, I think that's brilliant. The other point I would note, though, is that the best form of an annuity is a deferred annuity.

Instead of like UTC, where the payouts begin at 65, you can really buy yourself a lot of lifetime income protection if, when you're 50 or 60, you buy yourself a payout annuity that begins at 85. It's really cheap, because not everybody lives that long. But the appeal is that if you're still on God's green earth consuming and spending, the deferred annuity will be there to support you.

And a final point, since I'm a big fan of deferred annuities, is that we had a conference this year at Penn on cognitive aging and financial decision making. And at some point, lots of folks, maybe half, are going to get dementia of one form or another. They're not going to be able to make their asset allocation and payout decisions. So, I started thinking about this when my own mother, who is 94, stopped being able to handle her own finances. And guess who had to do it? You know who. If she had had an annuity, it would have been a whole lot easier for me to manage her end of life affairs.

MR. GOTBAUM: All right. Let me push back for a second on that.

MS. MITCHELL: Sure.

MR. GOTBAUM: While I agree with everything you said, we know that when people are asked the question, do you want to buy an annuity -- in other words, when they're asked the full question, do you want to buy this, and here's what it costs, they tend not to do it. When they're offered deferred annuities, they are even less likely to do so.

So the question is, knowing what you know, both, about rational choice and about behavioral economics, would you be in favor of essentially putting a deferred annuity into a qualified investment default option?

MS. MITCHELL: There are a couple of points --

MR. GOTBAUM: Or do you think that's taking away too much discretion?

MS. MITCHELL: There are a couple of points to be aware of. One is that the people who are most financially literate are also those who understand annuities the best. And I think we have a huge task ahead of us to try to educate the American people, ideally from high school forward more about retirement saving, investments, diversification, inflation and so on. So more financial literacy would enhance the demand for annuity.

The other point that I would make, and this is no surprise to you, I know, that many employers had been reluctant to pay out annuities into their plan menu. Why? Because they fear the insurance company that will be doing the payouts for the next 30, 40 years might go bust. And then the participants may turn around and sue the employer for fiduciary liability.

So, I think that's a huge topic that we really do need to try to figure out; either figure out a safe harbor or maybe through a platform where various different insurance companies can provide products, but that's a big stumbling block, to date.

MR. BIGGS: I mean, just again, going back to the idea of revealed preferences, I mean, it's -- I would be a little bit -- I understand the case, you know, for annuities in the theoretical sense, the longevity risk. But you know, we simultaneously have you know, the claim that Americans are excessively reliant on Social Security, while also saying they're under annuitized.

But it gets back to the point you made and you thought about the guarantees, that the people you know, who don't have annuities generally have a lot more wealth. And I just don't think it's a practical problem for them. But there may be rational reasons why people would not want to -- I don't want to say forced into annuity, but defaulted into an annuity.

I mean, the mortality risk issue for lower income people, they may not realize it, but once they do realize it, that's going to be a real problem, if they feel they're being pushed in that direction. But maybe they want liquidity. Maybe they want to be able to control you know, their consumption patterns over their retirement.

I mean, the idea that everybody is going to consume the same amount each year doesn't hold up in the data very well. People do tend to consume more in the beginning of retirement, less at the end of retirement. So there might be actual reasons that they have for not wanting this. So I definitely agree that it should be made available, and you know, it's a problem. We don't have them very much in 401Ks now.

But you know, I'm a little reluctant. If people are already -- most of their retirement income from Social Security, where we've told them how much they're going to save and how it's going to be invested and so on, you know, there's some window for individual discretion.

MR. GOTBAUM: So I'm not trying to put words in your mouth, but I am trying to understand where you are on this divide from requiring it to merely offering it, to making it the default. Would you --

MR. BIGGS: I would not make it a default.

MR. GOTBAUM: You would not make it a default.

(Simultaneous discussion)

MR. BIGGS: You can't default people into annuities. I mean, automatic enrollment and automatic escalation of contributions are great, both because they get people in the system. They raise contributions. But they also have a feature which is, if they got their contribution rate wrong, or if the person really shouldn't be contributing, it's relatively costless to get out of it.

Somebody puts in 6 percent for 6 months, and then they realize oh, you know, I really shouldn't be doing this for whatever reason. It's no big deal to stop it and get the money out. If you automatically annuitize someone into the wrong annuity, there's a lifetime commitment, and Olivia just gave all the reasons why annuity demand is going to vary dramatically.

And so you don't want to just kind of have somebody stumble, and you wake up one day and say, oh, I've been automatically enrolled, and here's my lifetime you know, income profile. But this is not suitable for me. So David and I and Mark Avery and a woman named Lena Walker, also an AARP employee (Laughter), several years ago, came up with an idea -- just addressed this question.

How do you deal with annuitization if you want to harness the power of automatic saving, but you don't want to commit people to the wrong lifetime annuity? And what we came up with was the idea that when people left their 401K -- left their job and were ready to take their 401K, they would be defaulted into two years' worth of monthly payments, because they couldn't take the whole thing out. They would have a test drive, basically, of the notion of monthly payments. And that would be automatic.

But then at the end, they could choose not to do that. They could choose to take the lump sum. They could choose to extend their -- whatever. So it was sort of an automatic but temporary annuity. I know that's kind of abusing language (Laughter), but that was the notion, this test drive. And that was the best we could come up with for a way to make it automatic but not commit people to the wrong path.

MR. GOTBAUM: So you would be okay with defaulting people into the test drive annuity?

MR. BIGGS: Yeah.

MR. GOTBAUM: Why don't we open it up to the audience? The basic rules in Brookings are, I have learned, one, you have to say who you are and if you have an affiliation. Two: Your speech has to end with a question mark (Laughter) and should be shorter than the time it takes us to answer. (Laughter) The lady in the last row.

MS. SIGNORELLI: Mary Ellen Signorelli , AARP Foundation. When I was on the ERISA advisory council, UT came to talk to us. And one of the problems they had is that when people went to retire, they would cash out the annuity. And so my question is, is if you're going to do some sort of default, how do you prevent that from happening?

MR. BIGGS: Well, this is exactly what the test drive was aimed at. People don't have a lot of experience with taking a large sum of money and converting it to a monthly payment. And this is what we used to call the big/small problem.

If you go to your Thanksgiving table and tell people -- tell your family members, you give me a hundred thousand dollars and I'll give you $500 a month for the rest of your life, they'll look at you like you're nuts. (Laughter) Right? And so the test drive idea was to get people used to this idea, to see if they were okay with it. If they weren't, then after two years, they could cash out.

I mean, at some point, it's their money. If they really insist on cashing out, you know, there's only so much you can do. But you can at least show them the benefits of monthly income.

MS. MITCHELL: I guess the point I would make about annuities is that they're a different asset than stocks and bonds. So the deal with an annuity is that you put your money in, and everybody in the risk pool puts their money in. And then based on survival curves or mortality curves, he or she who survives gets to benefit from the assets of the person that passed away.

And in this sense, it's totally different than a stock or a bond. When you buy a stock or a bond, you get the capital market return. But the real benefit from the survival curve or the place where the mortality really starts to kick in is around 80, 85, 90, 95. And so if you think about cashing in an annuity right away at 60 or 65, it's not that appealing.

The real benefit comes if you buy a deferred annuity where the mortality curve starts to really play a key role, and then you could earn a lot more than a typical capital market asset in expectation. Of course, only if you live. So that's the name of the game that you're playing.

MR. GOTBAUM: So does that mean that since it's a different asset class, that an appropriately diversified portfolio ought to include some form of deferred annuity (Laughter)?

MS. MITCHELL: Absolutely. Depending on your other wealth, if you're already rich enough that you don't care about longevity, or the other issue is if you're really poor, and if the annuity payouts would be held against you for all our means tested programs -- right? Medicare means tested. Medicaid means tested, SSI. So, if those payments would be held against you for those other poverty type programs, then maybe it wouldn't be a good idea.

(Audio dropout)

SPEAKER: Hi, I'm (Inaudible portion) and I was a consultant to the California Secure Choice Board, and I testified in Connecticut to try to kill the guaranteed return. I wonder whether in all these discussions, we're going down the wrong path. Because what we're trying to get out of these systems is a lifetime income stream of some kind where everybody can choose their target.

But sadly, the focus has gone onto portfolio choice, guaranteed return. So I wonder whether we need to change the dialogue to say what's the objective. And then these are all mechanisms to help you achieve that.

(Discussion off the record)

MR. GOTBAUM: You want to react?

MR. BIGGS: Well, it's easy in all these debates to lose track of what the objective is. And as Seth was saying earlier, you know, you take one bite at a time. And it's definitely helpful to think about what it is you're eating (Laughter) as you're taking a bite of it. Yeah. So, I agree.

MR. GOTBAUM: I'm going to step out of the moderator's role. The reason that I started mentioning that this all began with the Employee Retirement Income Security Act is because that notion, I believe, underlies all of this; that the reason why people talk about guarantees is because they want stable income. But we've gotten ourselves into a place where the dominant form of retirement savings products don't guarantee retirement income.

And so the question is, is it worth it? The reason this panel raised the question is, is it worth it going back to that, bringing it back? And as you can see, there's a range of views.

MR. BIGGS: I mean, I think the reference to ERISA is helpful, in the sense of you know, broadly speaking, ERISA said if you're promising people a benefit, you know, you have -- with investing requirements, you actually have to pay them the benefit, and you actually have to fund the benefit. And it became evident that employers were willing to offer these benefits, as long as they didn't have to pay them or fund them (Laughter).

Once you cash (Inaudible) -- they said it's not -- we don't want to offer it anymore. Or you know, the offset to the workers' wages is not enough. You know, they're not willing to bear it. And the same with state and local pensions now. They're happy to offer the pensions, as long as they don't have to fully fund them.

So, I think that that raises the issue of the guarantee, because in essence with the defined benefit pension, you're guaranteeing against the market risk. And I think it illustrates the issue of, are people willing to pay the price to get rid of the market risk. And the fact that so few people invest heavily in bonds tells me no. So it's just -- you know, it's a trade-off they're not willing to make.

MR. GOTBAUM: And yet, TIAA, the Teacher's Insurance and Annuity Association, still covers you know, some of hundreds of billions of dollars, et cetera. So, I think the challenge we have is, there are some people who clearly will pay there. A lot of people who clearly won't.

MR. BIGGS: Oh yeah, very risk averse crowd (Laughter).

MR. GOTBAUM: Yes, yes.

MS. MITCHELL: So I have a comment on that, because I've studied the TIAA. It's called a participating annuity. It's unique in the U.S. This type of model does exist in Europe, but because of special dispensation under federal law, TIAA is the only annuity provider in the country that can do this.

And what they do is they -- when participants buy in, they share in some capital market risk. But the other thing that's unique is they also share in mortality risk of the pool as a whole. And so other annuities don't -- they have capital market risk, but they don't have participation in the mortality risk.

So what this means is if there's a shock, not to an individual, but to mortality for the group as a whole, then the participants who are going to be receiving benefits under that scheme will either benefit -- if everybody dies all of the sudden leaving you, you're going to get a ton of money, or have their benefit reduced. That is, if everybody lives another three years, you're going to end up having your benefit cut.

But this is a unique product which nobody else can offer under the law. I think actually it would be useful if they did. The benefit to the insurer, which then passes through to the participant, is the insurer need not hold a reserve for mortality shocks. Every other annuity provider in the country must hold a reserve. Therefore, the annuity is much cheaper.

Now you can say, well maybe participants wouldn't like it, because their benefits will be fluctuating in some unknown way. But what we've shown is that for reasonable risk aversion parameters, that actually, participants are much better off pooling the mortality risk and taking the capital market risk from this participating annuity. So, I don't work for TIAA. I just think it's a very clever product. Europeans do it. Why don't we have more of it?

MR. BIGGS: I think it's helpful that you mentioned the two things together. You have the pooling of an annuity risk, and then you have the market risk collar there. And I think it's important to recognize that these are different things. You know, some of these ideas -- the composite pension plans and these guarantees, people will talk, but oh, we just need to pool all our risks together.

Mortality risk is something that you can pool. I mean, the risk that your house is going to burn down in a given year, that's something you can pool. Investment risk over time, I mean, is not something you can easily pool. You can pool it over short periods, but it really does next to nothing for you. If you try to pool it over long periods, you either need to build up the fund first, or you're going to sort of give a freebie to the first generation which may kind of lead to an under-funded plan later on. And so I think people -- there's this misapplication of risk pooling to investment risk which just doesn't work in the same kind of way.

MS. MITCHELL: Yeah, the only thing I would say is that the TIAA product pools mortality risk within the cohort, but if there's a shock to mortality for the cohort as a whole, that's what the participants bear.

MR. BIGGS: Mm-hmm. Yeah.

MS. MITCHELL: So we also have to understand that all mortality is not the same. (Laughter) You can quote me on that (Laughter).

(Simultaneous discussion)

(Audio dropout)

MR. GOTBAUM: I'm going to engage in self-dealing and let the pension advisor of the Brookings Institution ask a question.

SPEAKER: (Laughter) Thank you. But I'm totally financially unaffiliated. The question is transparency. Unlike other asset classes, you know what it's going to cost you for the investments. Have you thought about the impact? You don't know if you're buying a well-priced annuity or not. Have you thought about the impact of that? You don't know.

And I think it impacts each one of the conversations you have on a variety of different levels; is that, will that be helpful? Have you thought about it? What does transparency do? There is no way to find out. When I bought an annuity for my mother, I sat down with an actuary who specializes in this kind of thing, and we worked it through. But not everybody can do that. Josh, thank you.

MR. BIGGS: I don't know annuity markets well enough in a practical sense to say how much are you -- for the same product, how much variation is there? You would think with Internet pricing, that would have squeezed it down, but you know I'm not -- and maybe so few people buy annuities that it's just an inefficient market.

MS. MITCHELL: Or you could go to annuityprice.com, or you know a number of them. The issue, though, because we regulate insurance at the state level, is that every state is going to charge a different amount. So they tell you that you're in Pennsylvania and this is how much you pay. But I highly encourage you to do it, because you can learn a lot by seeing how much annuity and deferred annuities cost.

MR. GOTBAUM: Mm-hmm. Yes. One last question. The gentleman in the back?

MR. BARTHOLOMEW: Hello. Thank you very much. My name is Ed Bartholomew, independent consultant. Very interesting what you just said on the TIAA, which I understand is not available to everybody. It's just available to people that are participating. I love the concept of the deferred annuity, but what I worry about is the following. You're buying something 20 to 30 years in the future. You don't -- they're typically nominal annuities. You don't know what a dollar buys in 20 to 30 years.

And to your point about a mortality shock, it could hit all insurance companies. So you may be faced with a situation at 85 when you're demented -- you know, your insurance company goes bankrupt or it buys much less. So, who takes that risk, and is it really reasonable to put that risk on people? And why is the participating annuity not being pursued as a more robust alternative that's available to everybody?

MS. MITCHELL: Great questions. Most states, because we have state insurance regulations, which by the way, I think we shouldn't have. I think it should be federal, but that's a separate issue. Most states have solvency guarantee funds. So any insurance company operating in the state, selling in that market, would have to kick in to try to bail you out, if you had bought an annuity.

I talked to one of my colleagues who is another annuity guru, or at least junkie (Laughter), and he owns 14 different annuities, bought from different states, to benefit from the insurance guarantee fund (Laughter). So maybe that's the story.

MR. BIGGS: Wow.

MR. GOTBAUM: This is a market which is far from transparent. I want to thank the panel. I want to give the last word to the director of the Retirement Security Project, Bill Gale.

MR. GALE: Thank you. I want to thank you all for attending, and in particular thank Rebecca Sunden for all her work organizing this conference. Thank you. (Applause)

MR. GOTBAUM: One ministerial request. In order to help the support staff of Brookings, please, if there are cups, plates, newspapers, whatever, by your seat, please bring them to the back and deposit them in the appropriate recycling container. Thank you.

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