AUTO-IRA MAY BE JUST THE TICKET

Minnesota’s saving program should become available next year for those workers without an employer retirement plan.

Minnesota’s auto-IRA program would mean employers without a retirement savings plan must auto-enroll employees in one.

By CHRIS FARRELL • For the Minnesota Star Tribune

RETIREMENT

The standard advice when saving for retirement is: “Start early and save regularly” to harness the power of compound interest.

Yet many Americans have saved little for retirement, and that’s not because they’re financially illiterate. Instead, about half of the private-sector workforce works for companies that don’t offer a retirement savings plan. Few workers save without one, and that’s a major reason why about 30% of retired households solely rely on Social Security for income. The lack of access to an employer-sponsored retirement plan is concentrated among lower-wage workers without college degrees.

Several administrations of both parties have proposed initiatives to expand coverage nationally, but the efforts have gone nowhere. Frustrated at the lack of progress, eight states stepped into the breach and created auto-IRAs, and at least eight more states are in the wings, including Minnesota. The Secure Choice Retirement Program — Minnesota’s auto-IRA — should become effective next year.

The state auto-IRA plans share a similar model, although the details can differ. Employers without a retirement savings plan must auto-enroll employees in an IRA (often a Roth-IRA). Workers can opt out of it.

There is no company match. The default after-tax contribution rate is 5%. The first $1,000 goes into a moneymarket fund. Contributions above that threshold invest into an age-based target date fund.

Will these state-sponsored plans make a difference? Yes, at least according to a paper presented at a recent retirement conference in Washington, D.C., by two economists from Boston College. They took the basic auto-IRA blueprint, made some assumptions and peered into the future. One baseline number: Median household assets in 401(k)s and the like at ages 51-56 are zero on average among employees with high school or less education. (The study offers projections for workers by education. I’m focusing on less-educated employees.)

They assume about one-third of this group will optout. Participants who cycle in and out of the program and use the money for emergencies will accumulate a median balance at ages 51-56 of more than $25,000.

The same group would have almost $44,000 with no withdrawals. These modest sums are better than zero. Workers from this cohort who are continuously enrolled throughout their careers in the program accumulate sizable balances. Making sure all workers have access to a retirement savings plan at work matters, especially early in their career so they can take advantage of compound interest.

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