One of the largest changes in the U.S. retirement savings landscape during the last decade has been the widespread adoption of automatic enrollment in 401(k) plans. In 2010, 57% of 401(k) plans at companies with over 1,000 employees and more than $10 million in 401(k) assets featured automatic enrollment (Tower Watson, 2010); that is, employees contribute to the plans by default unless they actively opt out. This is in contrast to the situation a decade ago, when almost all 401(k) plans had a default of non-participation. The rapid spread of automatic enrollment has been abetted by research showing that it generates large gains in 401(k) participation (Madrian and Shea, 2001; Choi et al., 2004) and the legislative encouragement provided by the Pension Protection Act of 2006. Ninety-seven percent of individuals surveyed in 2007 whose companies offered automatic enrollment reported being glad that their company did so (Harris Interactive Inc., 2007).

The success of automatic 401(k) enrollment motivates Automatic’s core proposals: extending automatic enrollment to IRAs and annuities. About half the U.S. workforce does not have access to a 401(k), putting them beyond the reach of automatic 401(k) enrollment, and default annuitization of 401(k) balances is practically non-existent. The hope is that savings rates and annuitization (private annuities provide less than 2% of total household income for current retirees) will increase if IRA saving and 401(k) annuitization are made the default. Bills proposing automatic enrollment in IRAs have been introduced on a bipartisan basis in Congress multiple times, and the idea was endorsed by both Barack Obama and John McCain during the 2008 presidential campaign, so this book is essential reading for anybody closely following U.S. savings policy. However, Automatic makes clear that successfully extending automatic enrollment to IRAs and annuities is not straightforward.

Mark Iwry and David John’s chapter describes the automatic IRA proposal in great detail. Employers above a certain size would be required to offer automatic payroll-deduction IRAs if they don’t already sponsor a 401(k). Workers at these firms would have a portion of their pay contributed to the IRA via payroll deduction unless they opted out.

The government has already been encouraging employers to establish payroll-deduction IRAs (without automatic enrollment) for over a decade, but very few have done so. This is probably due to the two primary obstacles to the automatic IRA’s success. First, many small
employers lack the expertise and scale to make establishing a payroll-deduction IRA cost-effective. Second, financial companies are reluctant to service the small accounts that payroll-deduction IRAs would generate unless they could charge fees so high that not only earnings, but principal may also be eroded. Iwry and John propose creating small tax credits for employers to compensate them for the costs of establishing automatic IRAs, and creating a fallback no-frills IRA investment vehicle operated by private companies under a federal government contract in case a private market for servicing payroll-deduction IRAs does not materialize.

William G. Gale, Iwry, John, and Lina Walker’s chapter and Iwry and John A. Turner’s chapter propose approaches to increasing annuitization. A key challenge is that defaults have not to date proven to be very effective at raising annuitization. Annuitization is already required to be the default in cash-balance pension plans, but the vast majority of participants in these plans opt out of the default in order to receive a lump sum. Therefore, the proposals take a “boiling the frog gradually” approach. Gale et al. propose amending regulations to encourage employers to default retirees into a two-year trial-income period where they receive monthly installment payments from their 401(k) before the remaining balances are by default invested in an actual annuity. The hope is that by allowing retirees to experience an annuity-like income stream, they will come to appreciate annuities more and accept the final annuitization default. Iwry and Turner propose that employers make small, continuous acquisitions of deferred annuities from mid-career onwards the default, thus avoiding the need to suddenly and drastically increase one’s annuitization level upon retirement. These are promising ideas that should be studied with pilot experiments in the field once current regulations have been revised to facilitate their implementation.

Some of the challenges for automatic IRAs are laid out in an extremely enlightening chapter by John and Ruth Levine, who survey national retirement savings systems in Australia, Chile, New Zealand and the United Kingdom. For example, Australia’s Superannuation Guarantee (SG) system requiring employers to contribute 9% of employee earnings to individual retirement accounts bears similarities to the automatic IRA proposal. John and Levine report that 20% of SG accounts, each holding an average of $2,000, are “lost accounts” because participants who did not consolidate their accounts upon switching jobs can no longer be found. Perhaps in part due to the small average account sizes, fees on SG assets are high, averaging 1.25% of assets per year. On the annuitization front, John and Levine report that more than half of Chilean
retirees—an impressively high proportion—choose to annuitize their retirement assets. One wonders what factors cause such high annuitization in Chile, and if they could be applied in the U.S.

There are other policy proposals in *Automatic* that aim to increase the quantity of U.S. savings, especially among the economically disadvantaged, and to increase economic security during retirement. Gale, Iwry, and Walters and chapters by Ngina Chiteji, Michael Dworsky, Peter R. Orszag, Leslie E. Papke, Eric Rodriguez, and Lina Walker argue for expanding and reforming the Saver’s Credit, eliminating 401(k) and IRA balances from asset tests for public assistance program eligibility, promoting financial education, and increasing government transfers to those with little to no income because of caregiving responsibilities. While enacting each of these proposals has potential benefits, their costs must be carefully considered in this era of yawning fiscal deficits. The book would have been strengthened if these proposals were accompanied by budgetary analysis such as that found in the chapter by Christopher Geissler and Benjamin H. Harris, who estimate that the fiscal impact of expanding automatic enrollment to all 401(k) plans would be modest and progressive.

**References**


