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WHAT'S INSIDE

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This paper is an update to "Who Gets Retirement Plans and Why," originally published in September 2008 and comprehensively updated in March 2011. Supplemental tables, which provide all the data needed to update the full set of figures included in the original study, also are available.

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Who Gets Retirement Plans and Why, 2013

KEY FINDINGS

- **Most workers who are likely to have the ability to save and to be focused primarily on saving for retirement are covered by an employer-provided retirement plan.** Of those most likely to desire to save for retirement in the current year, three-quarters had access to a pension plan through their own employer or their spouse's employer, and 93 percent of those with access participated.

- **Younger and lower-income households are more likely to report that they save primarily for reasons other than retirement—for example, to pay for education, to buy a house, to fund other purchases, or to have cash on hand in case of an unexpected need.** Economic analysis suggests that these preferences are rational. Older and higher-earning workers are more likely to save primarily for retirement, and thus are more likely to prefer having a portion of their compensation in the form of retirement benefits rather than fully in cash.

- **Access to retirement plans at work is not randomly distributed throughout the workforce.** The probability that an employee works for a firm that sponsors a plan is highly related to the employee's characteristics. In particular, employees who work for firms that sponsor plans are more likely to be older, have higher earnings, and work full-time for a full year.

- **Workers at small employers that sponsor retirement plans are as likely to participate as workers at large employers sponsoring retirement plans.** Although only 17 percent of workers at firms with fewer than 10 employees have an employer that sponsors a plan—compared with 71 percent of workers at firms with 1,000 employees or more—if a firm sponsors a plan, approximately eight in 10 employees participate, regardless of firm size.

- **Differences in workforce composition appear to be a primary cause for the lower rate at which small employers sponsor retirement plans.** As a group, the characteristics of small-firm employees differ substantially from the characteristics of large-firm employees. Nevertheless, workers at small firms that sponsor plans are very similar to workers at large firms that sponsor plans, and workers at small firms that do not sponsor plans are very similar to workers at large firms that do not sponsor plans.

Key findings continued on the next page

- **It is of vital importance to maintain a Social Security system that provides adequate benefits to workers with low lifetime earnings.** Even the best-designed voluntary private-sector retirement system is unlikely to provide adequate resources to fund retirement consumption for workers with inadequate resources to fund consumption in their working years.

Introduction

Increasing the number of employers that sponsor workplace retirement plans, as well as employee participation at firms that currently offer plans, has been a focus of public policy development. As the retirement industry and policymakers try to increase coverage, it is important to understand the motives at play, including why more employers do not currently sponsor plans. To that end, it is necessary to understand which workers currently have access to and participate in employer-sponsored retirement plans, and why certain employees desire, and certain employers offer, compensation in the form of retirement benefits.

Which Workers Want Retirement Benefits?

Workers search for jobs that offer them the most valuable compensation packages. Individuals who wish to save for retirement value pension benefits because the benefits offer favorable tax treatment and other advantages such as the pooling of investments. However, because of the restrictions and tax penalties placed on accessing retirement benefits prior to retirement, some individuals who are not focused on saving for retirement would prefer to have compensation that consists only of cash to an otherwise equivalent compensation package that includes both cash and pension benefits.

Why Do Firms Sponsor Retirement Plans?

Because employers compete with one another to hire workers, they create compensation packages that will help them attract and retain qualified workers. In structuring compensation, employers can compensate their workers with cash or noncash benefits, such as retirement plans. However, the amount of compensation they can offer their employees is limited by the need to keep the products and services that they sell competitively priced. Therefore, an employer is more likely to offer retirement benefits as part of the compensation package if its workforce values such benefits. It is reasonable to predict that the likelihood of a firm offering retirement benefits is greater if a higher proportion of its workforce has the ability to save and is focused on saving for retirement.

This paper is a summarized update to “Who Gets Retirement Plans and Why,” first published in September 2008 (available at www.ici.org/pdf/per14-02.pdf). As with the updates published in October 2011, September 2012, and October 2013, this *ICI Research Perspective* updates the key findings of the original study using the most recently available data. For the most recent detailed analysis, see the March 2011 publication, “Who Gets Retirement Plans and Why: An Update” (available at www.ici.org/pdf/per17-03.pdf).

As part of this update, additional tabulations that provide the detailed data needed to replicate the figures contained in the March 2011 report for the years 1979 to 2013 are available in the supplemental tables (available at www.ici.org/info/per20-06_data.xls).

More formally, a firm sponsors a retirement plan if the associated reduction in the firm's direct compensation costs (cash compensation plus retirement benefits) is sufficient to cover the costs incurred by the firm to set up and administer the plan. A firm would not offer retirement benefits if doing so would increase its total compensation costs. Total compensation costs would increase if the costs incurred by the firm to set up and administer a retirement plan were greater than the associated reduction in the firm's direct compensation costs (cash compensation plus retirement benefits that accrue to employees). This would be the case if a firm's employees valued retirement benefits no more highly than cash compensation. This would also be the case if a firm's employees did value retirement benefits more highly than cash compensation, but the costs the firm would incur to set up and administer a plan would be greater than any associated reduction in direct compensation costs.

How the Terms *Pension Plan* and *Retirement Plan* Are Used in This Report

Often the term *pension plan* is used to refer to a traditional defined benefit (DB) plan, and *retirement plan* is used to refer to a defined contribution (DC) plan. In this *ICI Research Perspective*, the two terms are used interchangeably. Specifically, the term *pension plan* or *retirement plan* refers to both DB plans and DC plans, including 401(k) plans.*

The Department of Labor has stated:

> *"The Employee Retirement Income Security Act (ERISA) covers two types of pension plans: defined benefit plans and defined contribution plans....Examples of defined contribution plans include 401(k) plans, 403(b) plans, employee stock ownership plans, and profit-sharing plans."*†

The Current Population Survey (CPS), the primary source of the data on pension coverage used in this *ICI Research Perspective,* also does not distinguish between DB plans and DC plans when asking whether a worker's employer offers a plan.

The question for pension coverage in the March CPS is:

> *Other than Social Security, did [any] employer or union that (name/you) worked for in [the past year] have a pension or other type of retirement plan for any of its employees?*

* The Internal Revenue Code makes distinctions among pension, profit-sharing, and stock bonus plans. And, because most 401(k) plans are profit-sharing plans, they would be distinguished from pension plans under tax law. However, the distinction between the plans is not because one type is a DB plan and one is a DC plan. Rather, under tax law, the primary difference between pension plans and profit-sharing plans is that employer contributions to DC pension plans cannot be based on company profits, whereas employer contributions to profit-sharing plans may be based on company profits—although they are not required to be. (See 26 C.F.R. § 1.401-1 "Qualified pension, profit-sharing, and stock bonus plans.") For example, money purchase plans—which are a type of DC plan—are classified as pension plans under tax law. In general, pension, profit-sharing, and stock bonus plans are governed by many of the same sections of the Internal Revenue Code.

† See www.dol.gov/dol/topic/retirement/typesofplans.htm.

Why Do Households Save?

Analysis of survey data shows that younger and lower-income households were less likely to cite retirement as the primary reason they save. These households were more likely to be focused primarily on saving to fund education, to purchase a house, to fund other purchases, or to have cash on hand for an unexpected need (Figure 1).

The tendency of younger workers to focus less on retirement savings is consistent with economic models of life-cycle consumption, which predict that most workers will delay saving for retirement until later in their working careers.

The structure of government transfer programs is consistent with lower-income households focusing less on retirement savings. For example, most government programs aimed at lower-income households attempt to supplement income and increase these households' current consumption; it is unlikely that these same households are able to reduce current consumption to save for retirement. Moreover, Social Security benefits replace a higher percentage of pre-retirement earnings for individuals with low lifetime earnings, making lower earners less likely to desire to save for retirement at any given age.

In addition to age and income, part-time and part-year workers are unlikely to desire to save for retirement in the current year. To some degree, this is because the vast majority of these workers have low earnings and likely will receive a high earnings replacement rate from Social Security. But, in part, this also is because many workers who are currently working part-time or part-year typically may work full-time or for a full year. If earnings in the current year are less than typical earnings, individuals are unlikely to want to reduce current consumption further by saving—for retirement or for any reason.

FIGURE 1

Most Important Reason for Family's Savings

Percentage of households with household head aged 21 to 64 by household income and age of household head, 2013

		Aged 21 to 29	Aged 30 to 44		Aged 45 to 64	
Reason	All	All household income	Below median household income[1]	Above median household income[1]	Below 25th percentile of household income[2]	Above 25th percentile of household income[2]
Retirement	32%	13%	17%	35%	24%	45%
Liquidity	34	38	34	33	39	32
Education, home, or purchases	22	33	33	24	21	14
Education	11	9	17	16	5	7
Buy own home	4	12	5	2	2	1
Purchases	8	11	10	6	13	6
Other	9	14	14	6	9	6
Investments	2	3	2	1	3	1
For the family	6	10	10	5	5	4
No particular reason	1	1	1	1	1	1
Can't/Don't save	3	2	2	2	7	3
Total	100	100	100	100	100	100

[1] Among households with household heads aged 21 to 64, the median 2012 household income was $50,000.

[2] Among households with household heads aged 21 to 64, the 25th percentile of 2012 household income was $27,000.

Note: Components may not add to the totals because of rounding.

Source: Investment Company Institute tabulations of the 2013 Survey of Consumer Finances

Are Certain Types of Workers More Likely to Work for Firms with Retirement Plans?

In 2013, 53 percent of private-sector wage and salary workers aged 21 to 64 reported that their employers sponsored retirement plans (Figure 2). However, access to employer-sponsored retirement plans is not distributed randomly throughout the workforce.

Consistent with the focus of households on saving for retirement, younger workers, lower-earning workers, part-time workers, and part-year workers are less likely to work for firms that sponsor retirement plans. Forty-three percent of workers aged 21 to 29 worked for employers that sponsored retirement plans in 2013, compared with 60 percent of workers aged 55 to 64 (Figure 2, top panel). Twenty-six percent of workers in the lowest quintile of annual earnings ($15,000 or less) worked for employers with retirement plans, compared with 75 percent of workers in the highest quintile ($65,000 or more) (Figure 2, middle panel). Employees also were more likely to report that they worked for an employer that sponsored a plan if they were more fully engaged in the workforce: 60 percent of employees who worked full-time for a full year reported that their employer sponsored a plan in 2013, compared with 26 percent of employees who worked part-time for part of the year (Figure 2, bottom panel).

The fact that worker characteristics are related to the employer's decision to sponsor a plan suggests that worker demand* for retirement benefits plays a key role in determining which employers sponsor retirement plans.

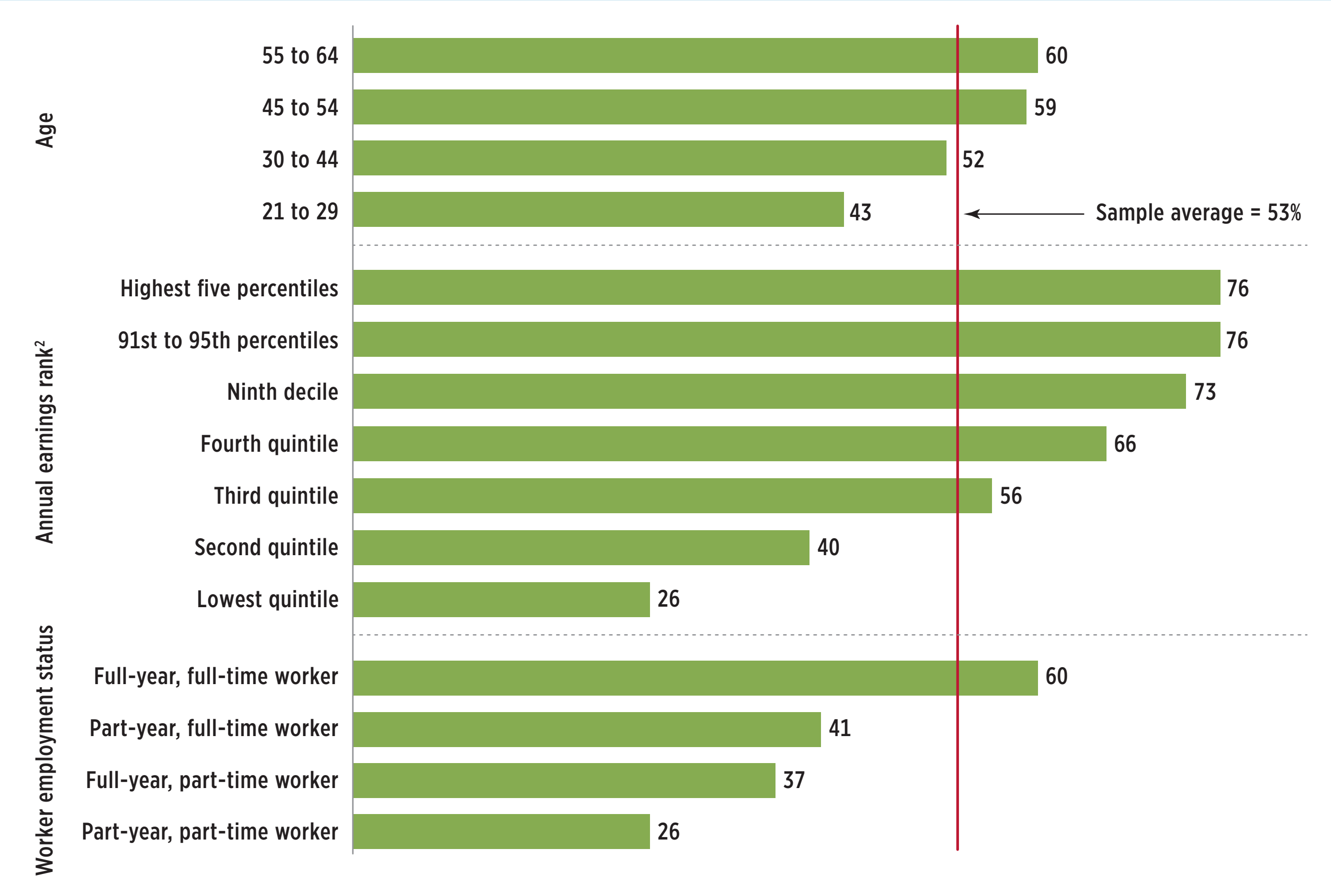
The starkest difference in sponsorship across groups of workers, however, is not related to a worker characteristic, but rather to a characteristic of the employer—namely, employer size as measured by the number of employees. Only 17 percent of workers at firms with fewer than 10 employees reported that their employer sponsored a retirement plan in 2013, compared with 71 percent at firms with 1,000 or more workers (Figure 3, left panel). Why sponsorship rates vary so markedly by firm size is examined below.

* In this paper, the term *demand* is used in accordance with its meaning in economic theory. An individual worker is said to demand pension benefits if he or she would prefer a compensation package that combines cash and pension benefits to a package with an equal amount of total compensation but consisting of cash alone. If an individual demands a pension, it in no way implies that the worker communicates this preference in any direct manner to his or her employer or that the individual will be offered a pension by an employer.

FIGURE 2

Probability That Employers Sponsor Retirement Plans by Various Employee Characteristics

Percentage of private-sector wage and salary workers aged 21 to 64 whose employers sponsor plans,[1] 2013



[1] Survey respondents are asked whether any worker at their employer is eligible to participate in a retirement plan. The figure plots the percentage of employees answering affirmatively.

[2] The lowest earnings quintile includes individuals with $15,000 of earnings or less; the second quintile includes those with earnings from $15,000 to $27,000; the middle quintile includes those with earnings from $27,000 to $40,000; the fourth quintile includes those with earnings from $40,000 to $65,000; the ninth decile includes those with earnings from $65,000 to $90,000; the 91st to 95th percentiles include those with earnings from $90,000 to $120,000; the highest five percentiles include those with earnings of $120,000 or more. For more detailed information on the earnings rank calculations, see the notes page in the supplemental tables (available at www.ici.org/info/per20-06_data.xls).

Source: Investment Company Institute tabulations of March 2014 Current Population Survey

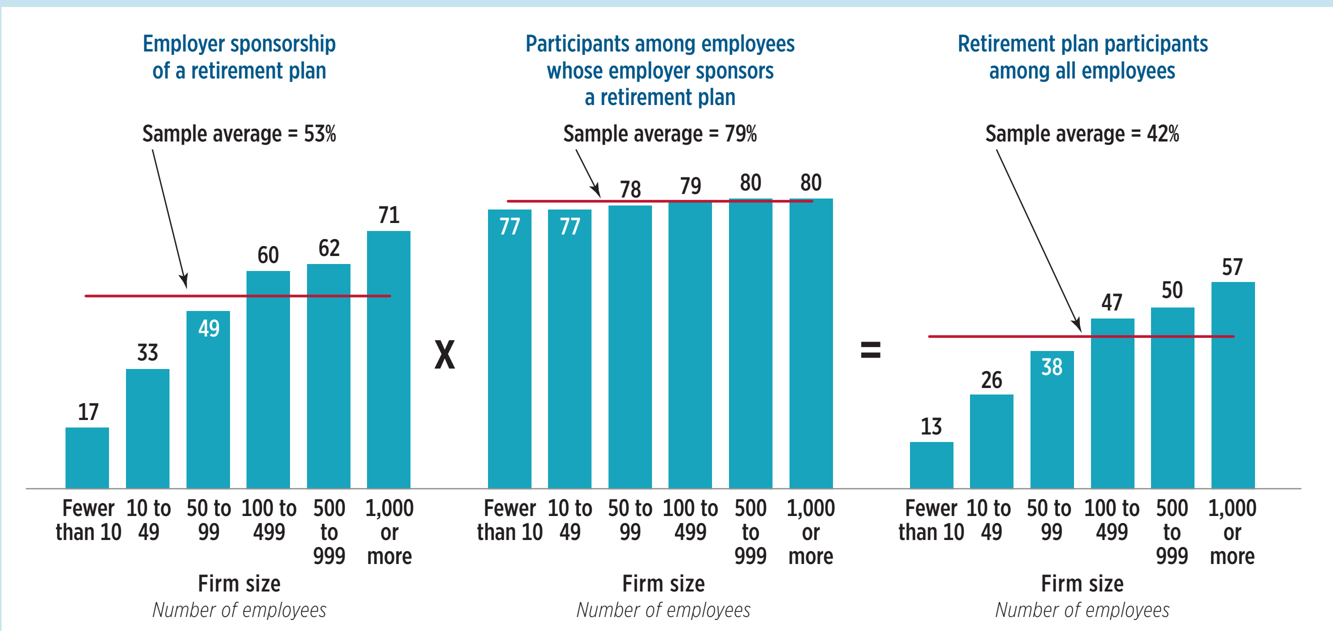
Are Certain Types of Workers More Likely to Participate in Retirement Plans?

As with employer sponsorship, there are significant differences between groups of workers in the proportion that participate in a retirement plan. For most characteristics used to classify workers, these differences are primarily driven not by the employee's decision to participate in a plan if one was offered, but by his or her employer's decision to offer a plan. For example, the percentage of workers participating in a plan ranged from 13 percent for workers at firms with fewer than 10 employees to 57 percent for workers at firms with 1,000 or more employees (Figure 3, right panel). However, this pattern primarily is driven by differences in sponsorship rates. Of those working for a firm that sponsored a plan, participation rates averaged 79 percent and varied little by firm size, ranging from 77 percent to 80 percent (Figure 3, middle panel).

FIGURE 3

Retirement Plan Sponsorship and Participation Rates by Firm Size

Percentage of private-sector wage and salary workers aged 21 to 64 by firm size (number of employees), 2013



Note: Survey respondents are asked whether any worker at their employer is eligible to participate in a retirement plan. The first panel plots the percentage of employees answering affirmatively. Survey respondents who say their employer offers a plan are then asked if they participate in the plan. The second panel plots the percentage of individuals whose employer sponsors a plan and who answer the second question affirmatively. The third panel reports the percentage of all respondents who participate in a plan, including those who said that their employer does not sponsor a plan.

Source: Investment Company Institute tabulations of March 2014 Current Population Survey

Alternative Explanations for Why Retirement Plan Sponsorship Rates Differ by Firm Size

Given the importance of the employer's decision to sponsor a plan and the focus of public policy on increasing sponsorship by small firms, this section examines differences in sponsorship rates by firm size in more detail. There are two potential explanations for why small firms are less likely to sponsor retirement plans: (1) small firms incur higher per-employee administrative costs than large firms and (2) small-firm employees do not value retirement benefits as highly as large-firm employees do.

If the costs of setting up and administering a plan have a significant fixed component that does not vary with the number of employees covered, then small firms will have much higher per-employee costs associated with a plan than large firms. In this case, even if employees at small firms value retirement benefits as much as employees at larger firms that sponsor plans, smaller firms will be less likely to sponsor a plan because of higher per-employee administrative expenses.

Alternatively, small firms may have lower sponsorship rates because small-firm employees are systematically different from large-firm employees. Specifically, they are less likely to desire to save for retirement in the current year and thus place less value on employer-provided retirement benefits. In fact, many may prefer cash wages to retirement benefits. On net, if total compensation costs, including administrative costs, are higher with retirement benefits, employers will choose not to offer plans.

In particular, for firms with few employees who desire to save for retirement, complying with nondiscrimination rules—rather than administrative costs—may be the largest barrier to adopting a plan. Nondiscrimination rules are designed to ensure that pension benefits do not disproportionately accrue to highly compensated employees. This is accomplished by linking the benefits received by high-paid workers to the benefits received by low-paid workers within a given firm. However, if few of a firm's low-paid workers choose to contribute to a 401(k) plan, the consequence of this linkage is that the amount high-paid employees at that firm can contribute is severely restricted. For these firms, the end result is that offering a 401(k) plan would provide little benefit to any employee.

Although both high fixed costs and differences in workforce composition could explain the observation that smaller firms are less likely to sponsor a retirement plan, the two alternative explanations generate other predictions that differ. If the fixed costs associated with starting up and administering retirement plans are the primary barrier to small firms adopting a plan, then noticeable differences should exist in sponsorship rates by firm size even if firms are similar in other observable characteristics. In contrast, if the primary reason small firms are less likely to sponsor a plan is that small-firm employees place a lower value on benefits relative to cash compensation compared to large-firm employees, the workforce composition of small firms should be noticeably different from that of large firms, and these differences should be consistent with small-firm employees having less desire to save for retirement in the current year.

Employees with Retirement Plans at Firms of All Sizes Have Similar Characteristics

This section will refer to firms with fewer than 100 employees as *small firms* and firms with 100 employees or more as *large firms*.*

Despite substantial differences in worker characteristics by firm size in the aggregate, small firms that sponsor retirement plans have workers who are similar to workers at large firms that sponsor plans. Similarly, large firms that do not sponsor plans have workers who are similar to workers at small firms that do not sponsor plans.

For example, controlling for whether or not employers sponsor retirement plans, there is very little difference in the age distribution of employees between small firms and large firms (Figure 4, top panel). However, across all firm sizes, workers at firms that do not sponsor plans are younger: 29 percent of workers at firms without plans are 21 to 29 years of age, compared with 20 percent of workers at firms that offer plans.

Twenty-seven percent of employees at small firms that sponsor plans are in the lowest two quintiles of annual earnings ($27,000 or less), compared with 25 percent of employees at large firms that sponsor plans (Figure 4, middle panel). Regardless of firm size, employees at firms that do not sponsor plans earn substantially less: 59 percent of employees at small firms that do not sponsor plans and 53 percent of employees at large firms that do not sponsor plans are in the lowest two quintiles of annual earnings.

Firms that do not sponsor retirement plans also have higher proportions of part-time or part-year employees (Figure 4, bottom panel). Of firms that sponsor plans, 76 percent of employees at firms with fewer than 50 employees are full-time, full-year workers, compared with around eight in 10 workers at other firms. Regardless of firm size, firms that do not offer plans have fewer full-time, full-year workers. Of firms that do not sponsor plans, the smallest and largest firms have the lowest percentages of full-time, full-year workers: 59 percent of workers at firms with fewer than 50 employees; 66 percent of workers at firms with 50 to 99 employees; 65 percent of workers at firms with 100 to 999 employees; and 60 percent of workers at firms with 1,000 employees or more.

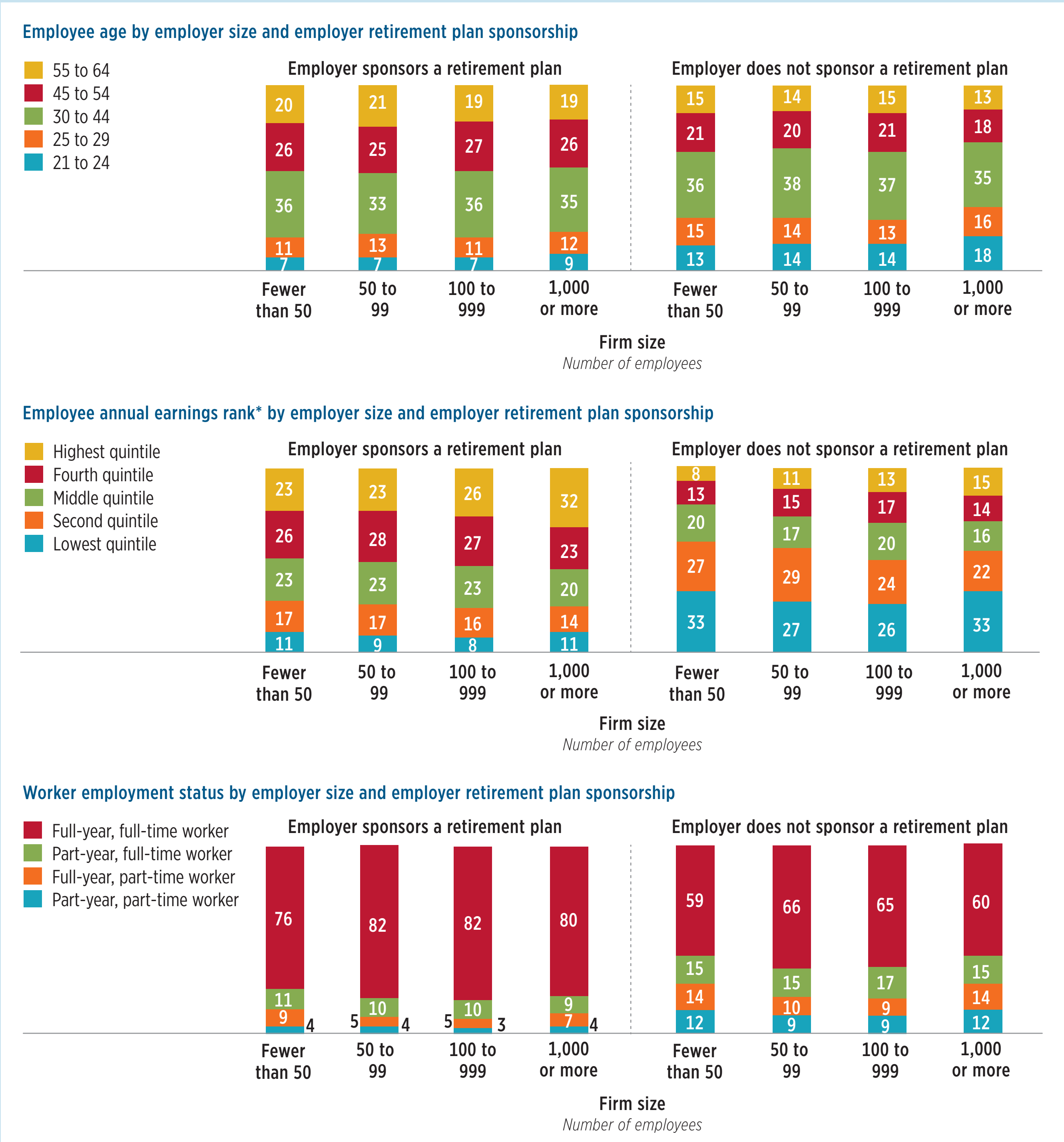
Although both administrative costs and workforce composition are likely to influence an employer's decision to sponsor a retirement plan, the data suggest that the low sponsorship rate at small firms is more likely due to differences in demand for retirement benefits by the firms' employees than to the fixed costs associated with starting up and administering a plan.

* For this reason, the numbers reported in the text are not reported directly on the figures (because they are an average of the categories presented).

FIGURE 4

Many Employee Characteristics Are More Associated with Employer Retirement Plan Sponsorship Than Firm Size

Percentage of private-sector wage and salary workers aged 21 to 64 by various characteristics, 2013



*The lowest earnings quintile includes individuals with $15,000 of earnings or less; the second quintile includes those with earnings from $15,000 to $27,000; the middle quintile includes those with earnings from $27,000 to $40,000; the fourth quintile includes those with earnings from $40,000 to $65,000; the highest quintile includes those with earnings of $65,000 or more. For more detailed information on the earnings rank calculations, see the notes page in the supplemental tables (available at www.ici.org/info/per20-06_data.xls).

Note: Components may not add to 100 percent because of rounding.

Source: Investment Company Institute tabulations of March 2014 Current Population Survey

Reexamining Workers at Firms That Do Not Sponsor Retirement Plans

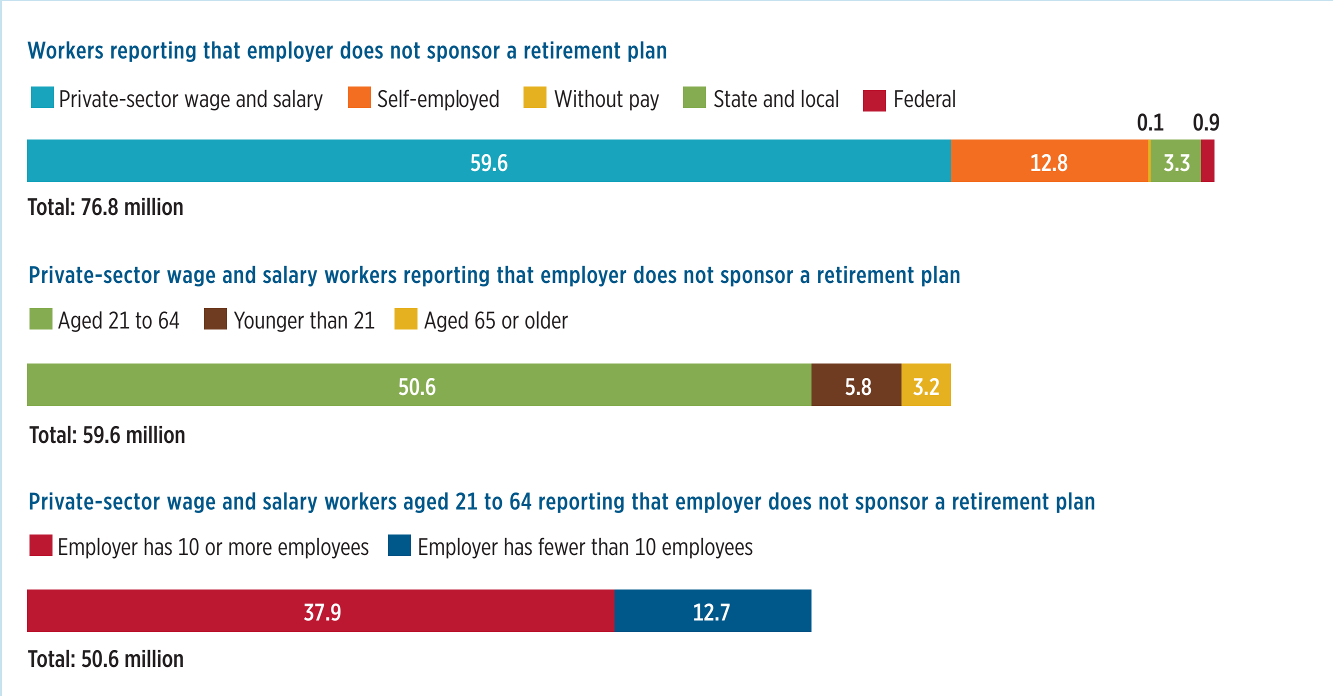
As illustrated above, employees who work for firms that do not sponsor retirement plans are more likely to be younger, have lower earnings, and have less attachment to the workforce—all characteristics associated with being less focused on saving for retirement. Younger workers typically invest in other ways, such as funding education, purchasing a home, and raising children. Retirement savings typically ramps up as workers get older, both because earnings typically increase with age and because other expenses, such as childcare and education, decline. Workers with lower earnings are less likely to be focused on retirement savings at any given age because Social Security provides a higher replacement rate for workers with low lifetime earnings. To maintain their standard of living in retirement, these workers have less of a need to supplement Social Security benefits and can begin saving later in life. Similarly, those who typically work part-time or part-year will have less need to supplement Social Security benefits in retirement because the vast majority have low earnings. Those who are temporarily working part-time or part-year are likely to suspend savings of any kind until they resume full-time work.

In light of this analysis, Figure 5 examines the data underlying the often-cited statistic that more than 70 million American workers do not have access to employer-sponsored retirement plans. In 2013, 76.8 million workers reported that their employers did not sponsor retirement plans. However, not all of these workers were private-sector wage and salary workers. Among government workers, 0.9 million federal government workers and 3.3 million state and local government workers reported that their employers did not sponsor retirement plans (and therefore possibly gave an inaccurate response to the survey). Another 12.8 million workers without an employer-sponsored retirement plan were self-employed and had the ability to establish a plan for themselves. Approximately 118,000 reported that they worked without compensation of any type, and thus had no compensation that could be deferred through an employer plan. Of the 76.8 million without a work-based retirement plan, 59.6 million were private-sector wage and salary workers. This study focuses on private-sector wage and salary workers between the ages of 21 to 64. Within this group, 50.6 million reported that they worked for employers that did not sponsor retirement plans.

FIGURE 5

Distribution of Workers Without Retirement Plan Coverage

Workers reporting that employer does not sponsor a retirement plan, millions of workers, 2013



Note: Components may not add to the totals because of rounding.

Source: Investment Company Institute tabulations of March 2014 Current Population Survey

Figure 6 categorizes these 50.6 million workers based on the likelihood that they would be focused on saving for retirement. Among this group, 19.9 million (or 39 percent) were part-time or part-year workers. As noted, this group is unlikely to be focused on saving for retirement in the current year, particularly if they typically work full-time or for a full year. Another 7.2 million (or 14 percent) were full-time, full-year workers aged 21 to 29. Few in this age group save primarily for retirement; this group saves primarily for education, the purchase of a home, or for precautionary reasons.

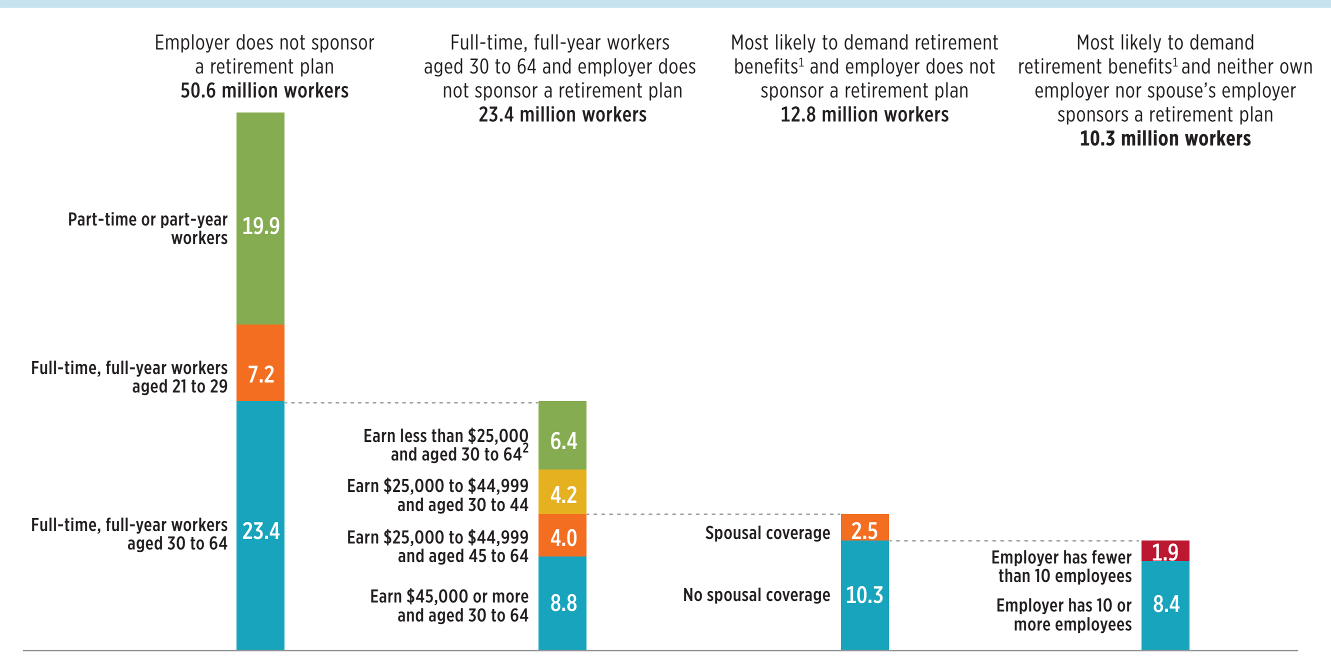
Among the 23.4 million full-time, full-year employees aged 30 to 64, 6.4 million earned less than $25,000 a year (Figure 6). These workers are unlikely to have the capacity or desire to save for retirement. Another 4.2 million earned $25,000 to $44,999 in 2013 and were aged 30 to 44. Full-year, full-time workers earning $25,000 to $44,999 may have the ability to save, but because they have other saving priorities, they are likely to delay saving for retirement until after age 44. This leaves 12.8 million workers—or 25 percent of all 21- to 64-year-old private-sector wage and salary workers at firms that did not sponsor plans—who were the most likely to be focused on saving for retirement: 4.0 million who earned $25,000 to $44,999 in 2013 and were aged 45 to 64, and 8.8 million who earned $45,000 a year or more and were aged 30 to 64.

To some extent, the percentage of workers at firms that sponsor retirement plans underestimates access of individuals to employer-sponsored retirement benefits. Some individuals who do not have access to plans through their own employers have spouses who work for firms that sponsor plans. On net, of the 50.6 million employees who worked for firms that did not sponsor retirement plans, 10.3 million, or 20 percent, were both likely to demand retirement benefits from their employer and were without access to an employer plan through a spouse (Figure 6).

FIGURE 6

A Closer Look at Workers Whose Employers Do Not Sponsor a Retirement Plan

Millions of private-sector wage and salary workers aged 21 to 64, 2013



[1] Full-time, full-year workers who earn $45,000 or more and are aged 30 to 64, or who earn $25,000 to $44,999 and are aged 45 to 64.

[2] Among full-time, full-year workers aged 35 to 44, $25,000 represents the top earnings for the 20th percentile of annual earnings and $45,000 represents the top earnings for the 50th percentile of annual earnings.

Note: Components may not add to the total because of rounding.

Source: Investment Company Institute tabulations of March 2014 Current Population Survey

Reexamining Retirement Plan Coverage

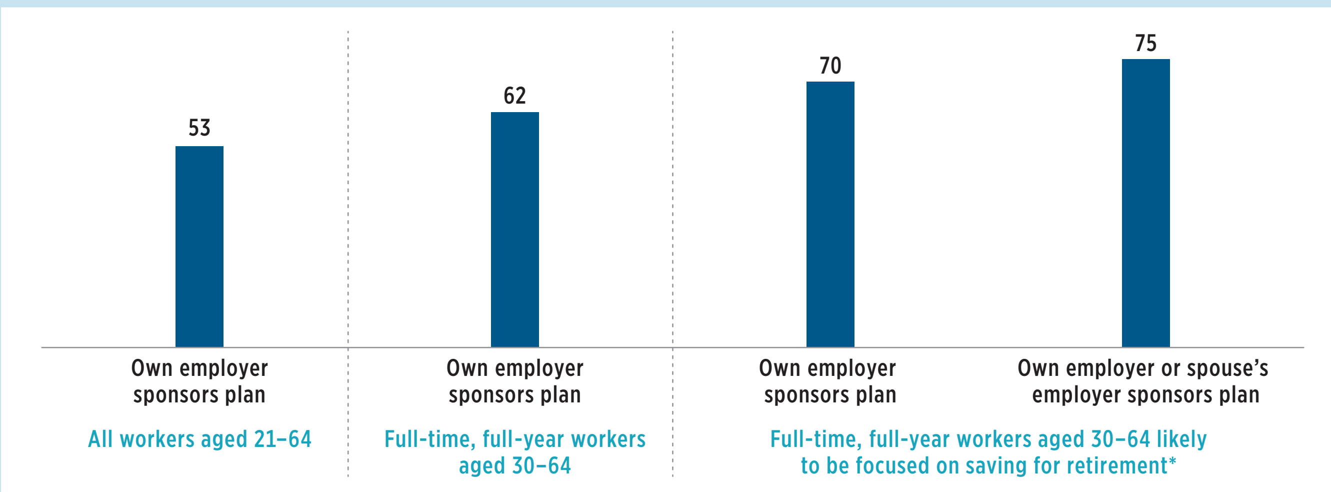
Using these same insights, Figure 7 examines the data underlying the commonly cited statistic that about half of private-sector workers work for an employer who sponsors a retirement plan. Among all private-sector wage and salary workers aged 21 to 64, 53 percent report retirement plan coverage at work. However, if very young workers (aged 21 to 29) and part-time, part-year workers are excluded from the analysis, coverage rates are higher: 62 percent of full-time, full-year private-sector wage and salary workers aged 30 to 64 work for an employer who sponsors a plan. Removing workers with lower earnings—those aged 30 to 44 with earnings less than $45,000 and those aged 45 to 64 with earnings less than $25,000—retirement plan coverage rises to 70 percent. Accounting for access to an employer plan through a spouse, coverage increases to 75 percent.

Thus, limiting the sample to those workers likely to demand retirement benefits—full-time, full-year, private-sector wage and salary workers likely to be focused on saving for retirement—70 percent worked for a firm that sponsored a plan, and 75 percent had access to a plan either through their own employer or through their spouse's employer (Figure 7). Additionally, of those workers with access to a plan—either through their own employer or through their spouse's employer—93 percent participated in the offered plan.

FIGURE 7

Most Workers Focused on Saving for Retirement Have Coverage

Percentage of private-sector wage and salary workers with access to an employer-sponsored retirement plan, 2013



*Full-time, full-year workers who earn $45,000 or more and are aged 30 to 64, or who earn $25,000 to $44,999 and are aged 45 to 64. Among full-time, full-year workers aged 35 to 44, $25,000 represents the top earnings for the 20th percentile of annual earnings and $45,000 represents the top earnings for the 50th percentile of annual earnings.

Source: ICI tabulations of March 2014 Current Population Survey

Conclusion

The private-sector pension system often is criticized because it is said that too few private-sector employees have access to employer-provided retirement plans. However, employer-sponsored retirement plans should not be analyzed in a vacuum; the U.S. retirement system includes both tax incentives to encourage employers to offer pension benefits and a social safety net of programs to help the elderly. Social Security is structured so that the portion of earnings replaced is much higher for workers with lower lifetime earnings; those with higher lifetime earnings rely more heavily on employer-sponsored retirement plans and private savings. This is not unintentional; from the inception of Social Security, policymakers understood that Social Security alone would be insufficient for those with higher lifetime earnings and intended for Social Security and employer-provided pensions to work together.*

The success of private-sector plans should be judged in light of these factors. Of those most likely to need to supplement Social Security benefits in retirement and to desire to save for retirement in the current year, three-quarters have access to a plan through their own employer or their spouse's employer, and 93 percent of those with access participate.

The analysis in this paper supports the proposition that the private-sector pension system can and should be improved. However, the analysis also suggests caution when proposing reforms to a system that already provides retirement benefits to most of the workers who are likely to value retirement benefits more highly than cash compensation. The incentives faced by both employees and employers should be taken into account when crafting pension reforms, and realistic goals should be set for increasing employer-based retirement plan coverage.

Some workers do not have the resources to fund current consumption, much less the ability to set aside resources to fund consumption in retirement. Other workers may have the ability to save and will likely desire to save for retirement at some point in their careers, but have more immediate savings priorities in the current year. It is unlikely that either group of these workers will seek to work for a firm that offers a pension plan, or choose to participate in such a plan if offered.

More significantly, some households face a lifetime of low earnings. Even the best-designed voluntary private-sector retirement system is unlikely to provide adequate resources to fund retirement consumption for workers who have inadequate resources to fund consumption in their working years. Because of this, it is vitally important to maintain a Social Security system that provides adequate benefits to workers with low lifetime earnings.

* Since the enactment of Social Security, Congress has allowed private-sector employers to account for Social Security in their pension plans. This process—known as integration—permits a higher benefit formula or a higher employer contribution rate on earnings not covered by Social Security. Permitted disparity—the provision in the tax code that allows Social Security integration—is defined in Section 401(l) of the Internal Revenue Code.

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