SMALL BUSINESS RETIREMENT PLANS: THE IMPORTANCE OF EMPLOYER PERCEPTIONS OF BENEFITS AND COSTS

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Executive Summary

At any given time, only about half of U.S. private sector workers are covered by an employer-sponsored retirement plan, and few workers save without one. The coverage gap, which undermines the retirement income security of the nation's workers, is driven by a lack of coverage among small employers. But, in fact, about half of firms with less than 100 employees do offer a plan for their employees.

This study presents results from our *2023 Small Business Retirement Survey*, which provides an up-to-date and comprehensive understanding of why some small firms offer retirement plans and the barriers preventing other small firms from offering one. A unique aspect of this survey is the inclusion of 100 firms with 0-4 employees, a group typically ignored in most small business retirement surveys.

Key insights from the survey:

- Firms' perceptions of the value of retirement plans for hiring and retaining workers and of the costs involved are important determinants of whether they offer, or will likely offer, a plan.
- As in previous surveys, firms report that the two main barriers to offering a plan are: 1) revenue stability/size of the firm; and 2) perceived costs or administrative burden of having a plan.
- However, concerns about costs or administrative burdens are driven by misperceptions; many firms are unaware of lower-cost options for employers and tax credits.
- Finally, the recent growth of state-sponsored retirement programs may encourage firms without a plan to offer one.

These results suggest that many firms overestimate the financial and time costs required to offer a plan and that better awareness of lower-cost plan options for employers and tax credits could help move the needle on the coverage gap.

Introduction

At any given time, only about half of U.S. private sector workers are covered by an employer-sponsored retirement plan, and few workers save without one. As a result, many households end up with no retirement savings and are entirely dependent on Social Security, while others move in and out of coverage throughout their careers and end up with only modest balances in a 401(k) account.[1]

Numerous studies have shown that offering a retirement plan is closely related to firm size; firms with less than 100 employees are much less likely to offer a plan than larger firms. As a result, observers tend to dismiss small firms as a source for future growth in coverage. However, a meaningful share of small businesses does offer a retirement plan. The purpose of this study, which is based on a new survey, is to provide an up-to-date and comprehensive understanding of why some small firms offer retirement plans and the barriers preventing other small firms from offering one.

The discussion proceeds as follows. The first section provides an overview of what we know about small business retirement plans so far. Turning to the new survey data, the second section examines what factors make a firm likely to provide coverage. The third section examines the perceived barriers firms face to offering a plan and dives into some of the misperceptions. The fourth section explores what characteristics make a firm without a plan more inclined to adopt one in the near future. The fifth section examines whether the presence of state-sponsored retirement programs – which generally require firms without a plan to enroll their workers in the state program – shifts firm perceptions.

The final section concludes that important drivers to offering a plan – in addition to standard characteristics like industry, firm size, and employee salary – are beliefs about the value of retirement plans for employee retention and a firm's future revenue growth. But employers that do not offer a plan hold many misperceptions about the financial and time costs of offering one. Therefore, better awareness of the many available options for small firms may help close the coverage gap.

What We Know About Small Business Retirement Plans

The coverage gap is a pressing concern for the nation's retirement income security, and the gap is driven by small employers. Small employers (firms with fewer than 100 employees) account for the vast majority of businesses and 35 percent of private sector workers.[2] But only about half of small employers offer a retirement plan for their employees (see Figure 1).

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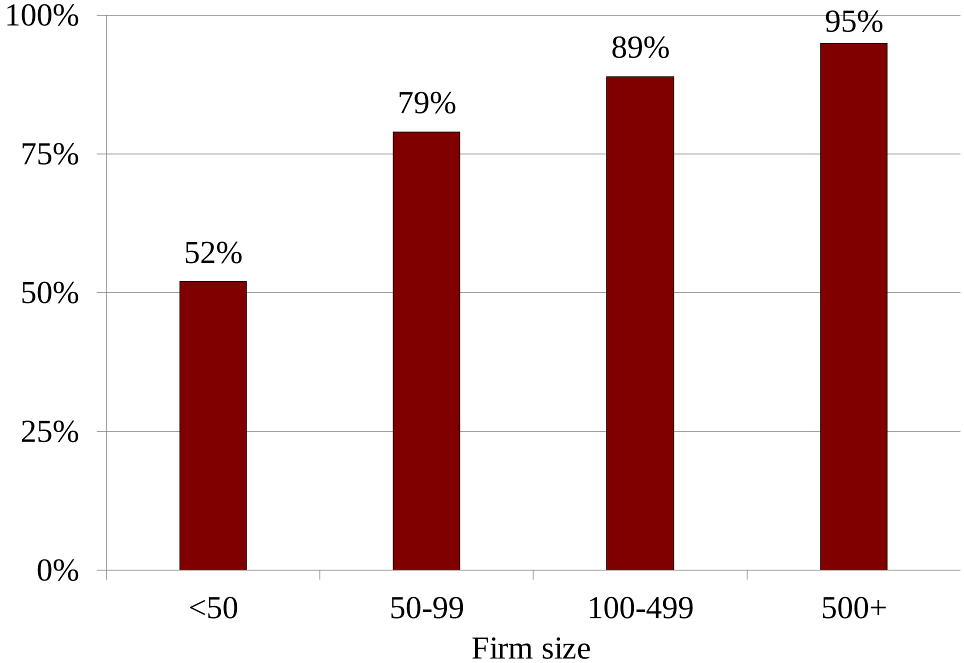
[1] Biggs, Munnell, and Chen (2019).

[2] U.S. Bureau of Labor Statistics, *Business Employment Dynamics* (2022).

Figure 1. *Percentage of Private Sector Firms Offering a Retirement Plan, by Firm Size, 2021*

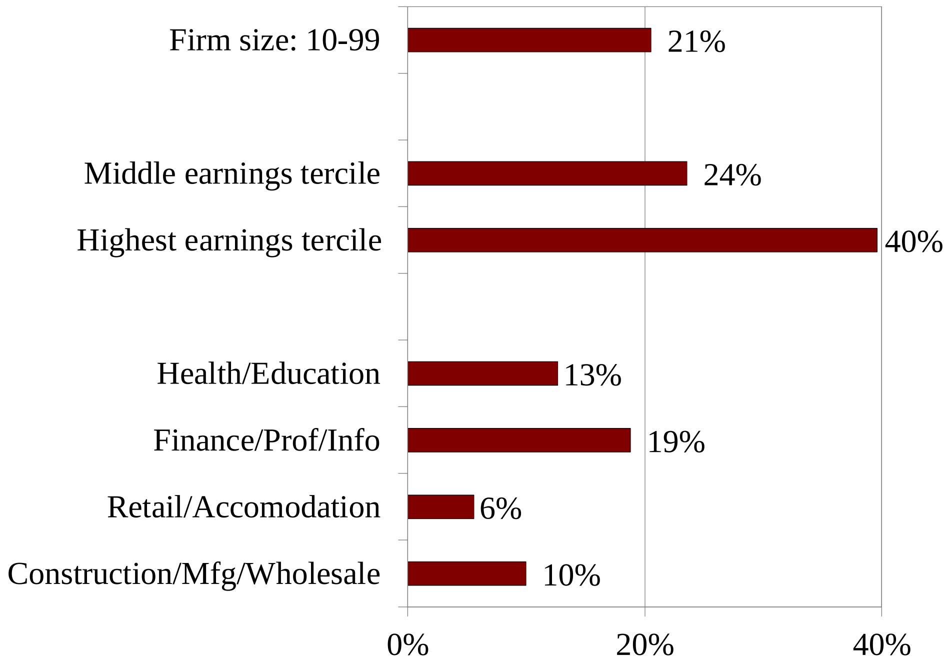


Source: U.S. Bureau of Labor Statistics, *National Compensation Survey* (NCS) (2021).

In order to encourage growth in coverage, we did an initial analysis of the characteristics of firms that do and do not offer a plan in an earlier study (see Figure 2). The results showed that the biggest drivers among small firms are: 1) larger firm size, 2) higher-earning employees, 3) being in finance or other professional services and scientific industries.[3]

[3] Chen and Munnell (2021).

Figure 2. *Employee Characteristics on Likelihood of Small Firm Offering Retirement Plan*



Notes: Base case variables are firm size fewer than 10 employees, bottom earnings tercile, and "other" industries. Other controls include education, hourly vs. salary employee, tenure, age, marital status, gender, and race/ethnicity.
Sources: Chen and Munnell (2021) using the University of Michigan's *Panel Study of Income Dynamics* (PSID) (2019).

The question is, what is preventing other small firms from offering retirement benefits? Historically, small firms have consistently cited the same three major barriers: uncertain revenues that make it hard to commit to a plan; employee preferences for wages and other benefits; and the costs associated with establishing and administering a plan.[4]

It makes sense if small firms do not offer a plan because other business concerns take precedence or their employees would prefer higher cash wages. The less compelling reason is the concern that establishing and maintaining a plan would be too costly or burdensome. Surveys have indicated a substantial lack of knowledge about the various retirement plan options, the costs of the options, and even the need to provide a match in a 401(k) plan.[5] This area seems like fertile ground to make inroads into expanding coverage.

But several important questions remain unanswered, such as: do revenue growth, percentage of full-time employees, or perceptions of the value of retirement plans matter for offering a plan? Most of the information available on small firms is from employee-level data, which lacks key details on firm characteristics. And while recent surveys have touched on the issue of small

[4] Yakoboski and Ostuw (1998), Collinson (2016), and Collinson, Rowey, and Cho (2021).
[5] For a summary, see Chen and Munnell (2021).

businesses and retirement plans, the last comprehensive survey was done over two decades ago.[6] The economy and options for small businesses are very different today. This study updates the survey conducted by the Employee Benefit Research Institute (EBRI) and Greenwald Research in 1998 to answer four main questions: 1) What characteristics – other than firm size, salary, and industry – make a small firm more likely to offer a retirement plan? 2) Have the major barriers to offering a plan changed in the last two decades? 3) What characteristics make a firm without a plan likely to adopt one in the near future? and 4) Have state-sponsored retirement programs changed firm perceptions about offering their own plan? See Box for a brief description of the survey methodology.

Box: 2023 Small Business Retirement Survey

The *2023 Small Business Retirement Survey* is produced in collaboration with EBRI and Greenwald Research. The survey, which addresses why firms do or do not offer a retirement plan, was conducted between February and April 2023 and includes 703 firms with 100 or fewer employees.

Roughly 46 percent of the firms surveyed offered a retirement plan while the other 54 percent did not offer a plan, which is nationally representative of small U.S. firms. What is unique about the 2023 survey is that it includes a sample of 100 firms with 0-4 employees. This group of micro-firms is typically ignored in most small business retirement surveys.

Characteristics of Firms Offering a Plan

To begin, we examine the characteristics of small firms that do provide coverage. Our prior analysis, using worker-level data, found that salary, industry, and firm size were the biggest drivers for whether a small business offered a retirement plan. However, the prior analysis did not include data on other key firm characteristics. With the latest survey results in hand, we can examine whether salary, industry, and firm size are still the biggest drivers or if other factors also influence whether a small employer offers a plan.

The additional characteristics we explore are:

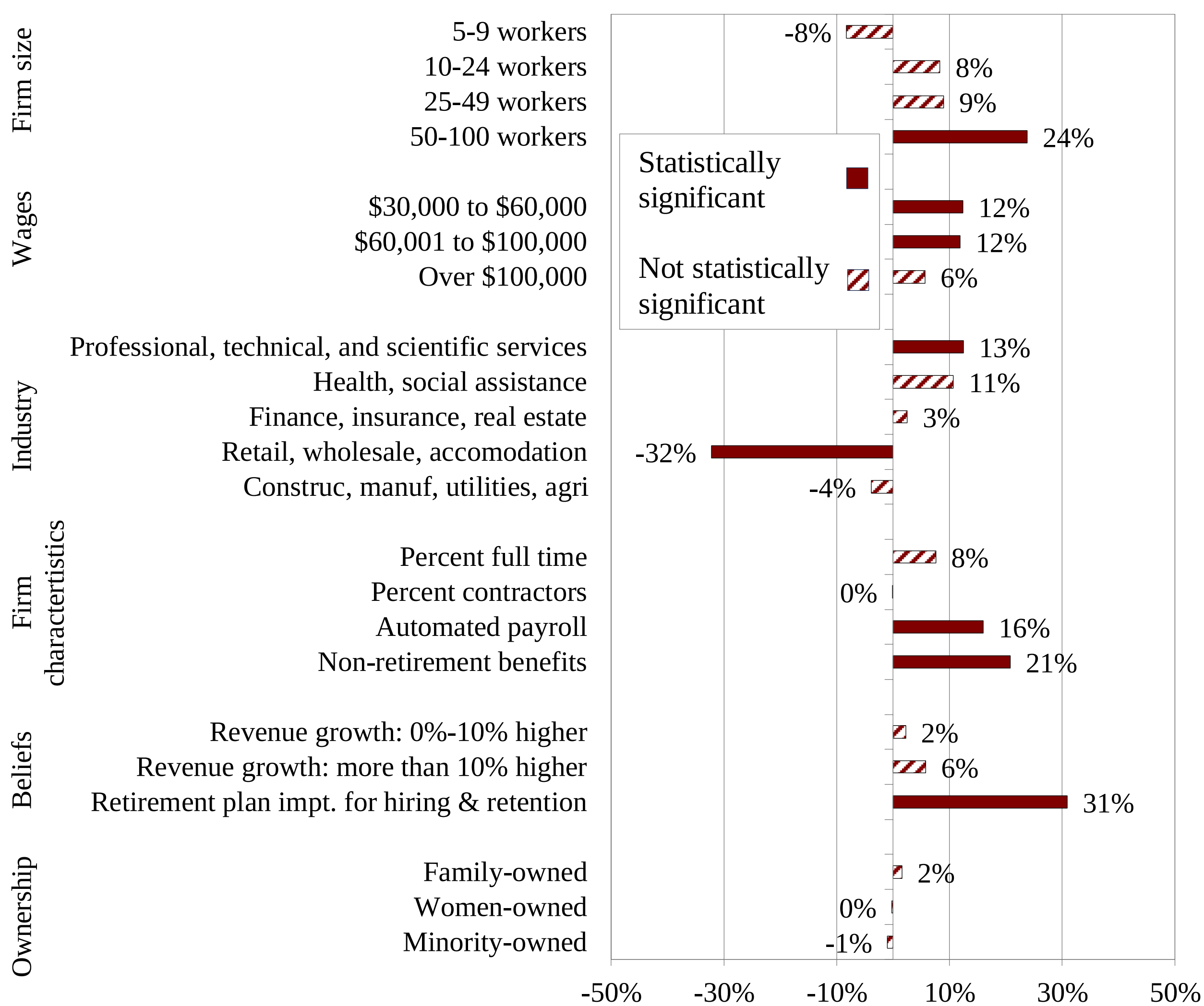
- Percentage of employees who are full-time – small firms that hire mostly part-time workers or contractors are unlikely to offer a retirement plan.
- Revenue expectations – firms with booming business are more likely to offer a retirement plan than those that are unsure whether they will stay open next year.
- Employee retention – beliefs about whether offering a retirement plan is important for hiring, retention, and employee performance could impact whether firms offer a plan.
- Automated payroll systems – retirement plans require payroll deductions, so setting up a plan may be easier for firms with automated payroll.

[6] For summaries of the survey results; see Yakoboski and Ostuw (1998) and Employee Benefit Research Institute (EBRI) (1998). EBRI also surveyed small employers in 1999, 2000 and 2002, but the 1998 survey is our reference point because it asked a more comprehensive set of questions.

- Health or other benefits – firms that offer health insurance or other benefits may be more likely to also offer a retirement plan.
- Ownership – perhaps family-, women-, or minority-owned businesses are more likely to offer a plan.

Many of these characteristics are highly correlated. In order to disentangle their relative importance, we estimate a simple linear regression relating various factors to the likelihood of a firm offering a plan (see Figure 3).

Figure 3. *Effect of Firm Characteristics on Likelihood of Offering a Plan, 2023*



Note: Solid bars are statistically different from zero at least at the 10-percent level.
Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

After controlling for all these characteristics, firm size, employee wages, and industry are still important predictors of whether a small firm offers a retirement plan. As expected, firms with 50-100 employees, those with higher average salaries, and firms in professional, technical, and scientific services industries are much more likely to offer a retirement plan. Meanwhile, firms in retail or wholesale sales, and in accommodations (hospitality and food services) are much less likely to offer a plan.

But other factors also mattered. Beliefs about whether having a retirement plan is important for hiring and retaining good employees is also an important driver. In fact, it is the strongest indicator of whether small firms offer a plan; firms that believe having a retirement plan is important for hiring, retention, and performance are 31 percent more likely to have a plan than those that do not consider it important. Notably, a firm's beliefs about revenue growth had little to no effect on having a retirement plan.

Other characteristics that are important predictors of offering a plan are having an automated payroll system and providing other fringe benefits. Interestingly, though, the percentage of full-time employees did not matter, nor did the type of people who owned the business.

Have the Barriers to Offering a Plan Changed Between 1998-2023?

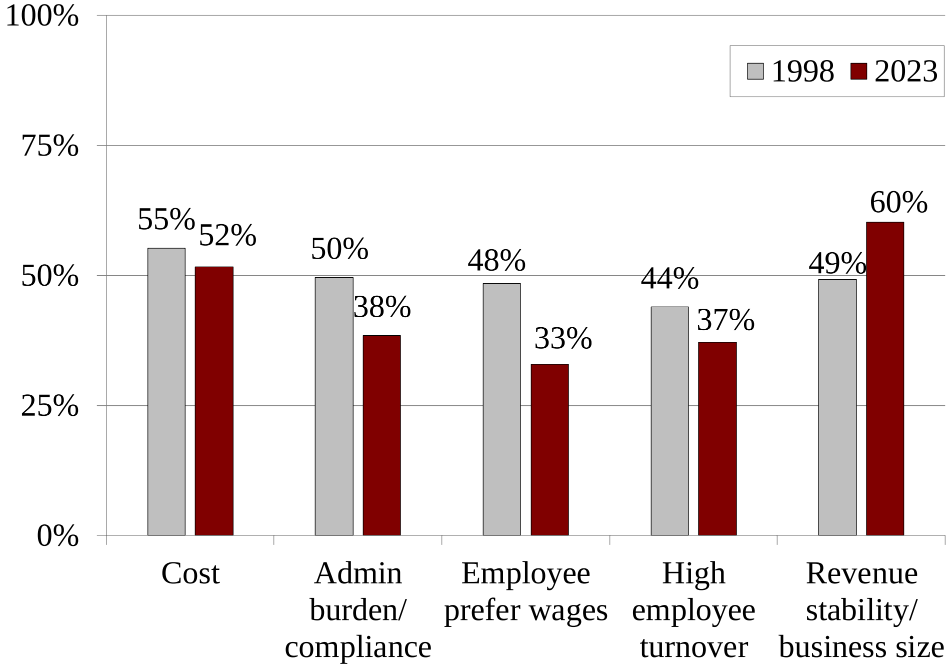
Historically, as noted, small firms that do not offer a plan have cited uncertain revenues, employee preferences for wages; and administrative costs. Have the barriers to plan adoption changed since 1998?

Figure 4 compares the responses of small businesses in 1998 and 2023. The top two barriers that prevent small firms from offering a retirement plan – revenue concerns/business size and costs or administrative burden – have remained the same. Today, however, employers are far less likely to cite "employee prefers wages" as a major reason for not offering a plan. But revenue/size has grown to become the biggest barrier.[7] This finding suggests that many small firms do not feel firmly enough established to introduce a workplace retirement plan.[8]

[7] The 1998 survey did not include firms with fewer than five employees. If we compared the share of firms with 5-100 employers, the main takeaway remains the same; a rise in the share of firms – from 49 percent to 56 percent – that cite revenue stability or being too small as a major barrier for offering a retirement plan.

[8] It is important to note that revenue predictions are not the same as citing a concern for revenue stability. Figure 3 shows that revenue expectations do not influence the likelihood of offering a retirement plan, all else equal. But firms can expect higher revenue growth next year and still feel uneasy about revenue stability. For example, over half of the firms that believe revenue growth will be more than 10 percent higher next year still cite revenue stability as a major barrier to offering a plan.

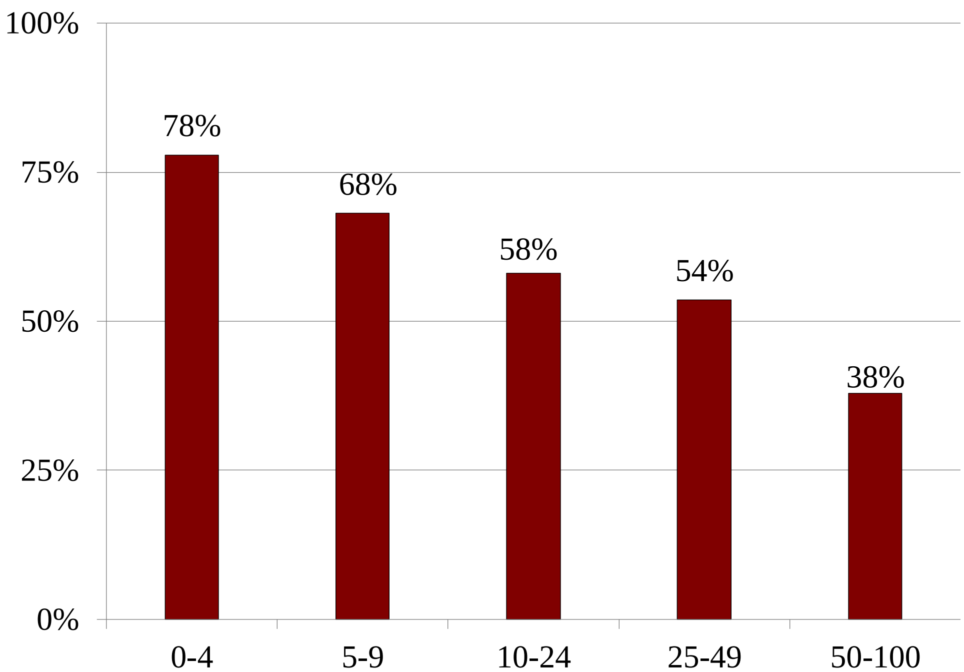
Figure 4. *Major Reasons for Not Planning to Offer a Plan, 1998 and 2023*



Sources: Yakoboski and Ostuw (1998); and author's calculations from the *2023 Small Employer Retirement Survey*.

Indeed, close to 80 percent of firms with 0-4 employees cited revenue and size as a major barrier to offering a plan. This share decreases to 54 percent for firms with 25-49 employees and 38 percent for firms with 50-100 employees (see Figure 5).

Figure 5. *Percentage of Firms that Cited Revenue/Size as a Major Reason for Not Offering a Retirement Plan, by Firm Size, 2023*



Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

The smallest of these small firms may simply have too much on their plate to add an additional benefit.[9] For more established firms, costs and administrative burden/compliance become more important drivers for not offering a plan.

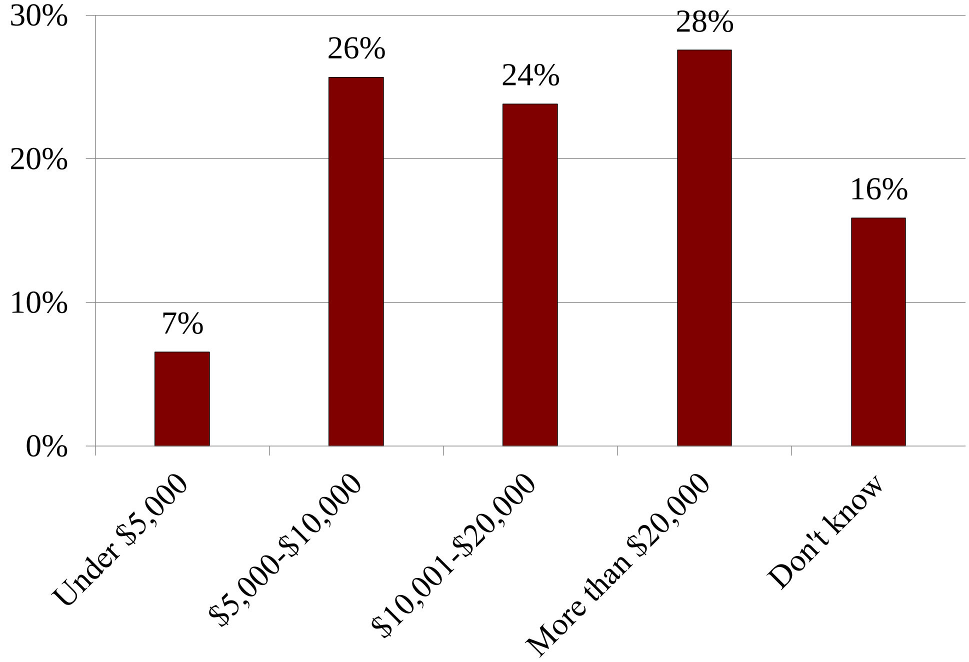
Financial and Time Costs of Offering a Plan

Interestingly, most small firms that cite costs and administrative burden/compliance as a barrier do not have a good sense of how much money or time is actually required for setting up a plan. A quick Google search yielded several 401(k) options where annual employer costs would only be about $2,500 for a firm with 10 employees and $5,000 for a firm with 50 employees.[10] But, over half of small firms believe providing a retirement plan would cost more than $10,000 per year; and nearly 30 percent think it would cost more than $20,000 per year (see Figure 6).

[9] Some respondents provided explanations of why they did not offer a retirement plan. Many firms with 0-4 employees were self-employed or worked with part-time employees or contractors on an as-needed basis. They may not be aware of options such as solo-401(k)s and SEP IRAs or they may not consider having a retirement plan for themselves as "offering" a retirement plan.

[10] The mid-tier plan offered by Guideline costs $79 a month and $8 a month per participant. The mid-tier plans from Betterment and Human Interest cost $150 a month and $6 a month per participant. Fidelity offers a small business retirement plan that charges a $500 start-up fee and a $300 per-quarter administration fee. However, it also requires employers to match employee contributions, which can increase costs.

Figure 6. *Perceived Annual Costs of Offering a Retirement Plan, 2023*



Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

Not only do small firms overestimate the cost of offering a plan, the vast majority – particularly those with fewer than 50 workers – are not aware that they can claim a tax credit of up to $5,000, for three years, to help offset the costs of starting a plan (see Table 1). And, interestingly, about 80 percent of employers say that such a credit would make offering a plan more attractive.

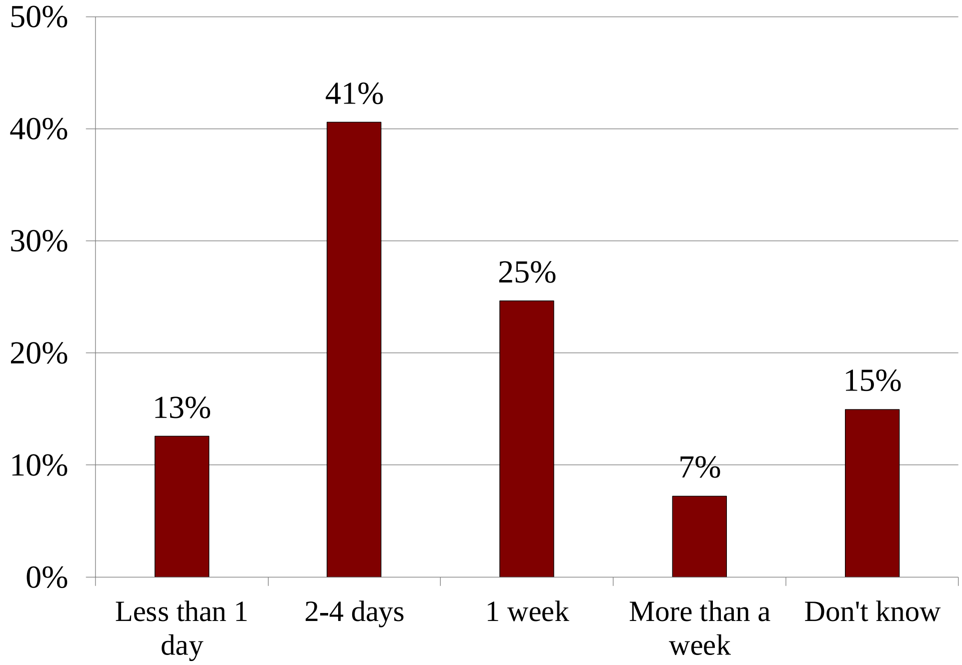
Table 1. *Awareness of Retirement Plan Tax Credit and Impact on Attractiveness of Offering a Plan, by Firm Size*

	0-4	5-9	10-24	25-29	50-100	Total
Aware of tax credit	16%	15%	20%	23%	50%	24%
Existence of credit makes offering plan more attractive	76	80	82	74	77	78

Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

Additionally, small firms also do not have a good sense of how much time it would take to administer a retirement plan (see Figure 7). Most firms believe that it would require several days to a whole week every month. But in reality, after the initial set-up is complete, operating a retirement plan should only take a few hours a year.[11]

Figure 7. *Perceived Monthly Time Required to Administer a Retirement Plan, 2023*

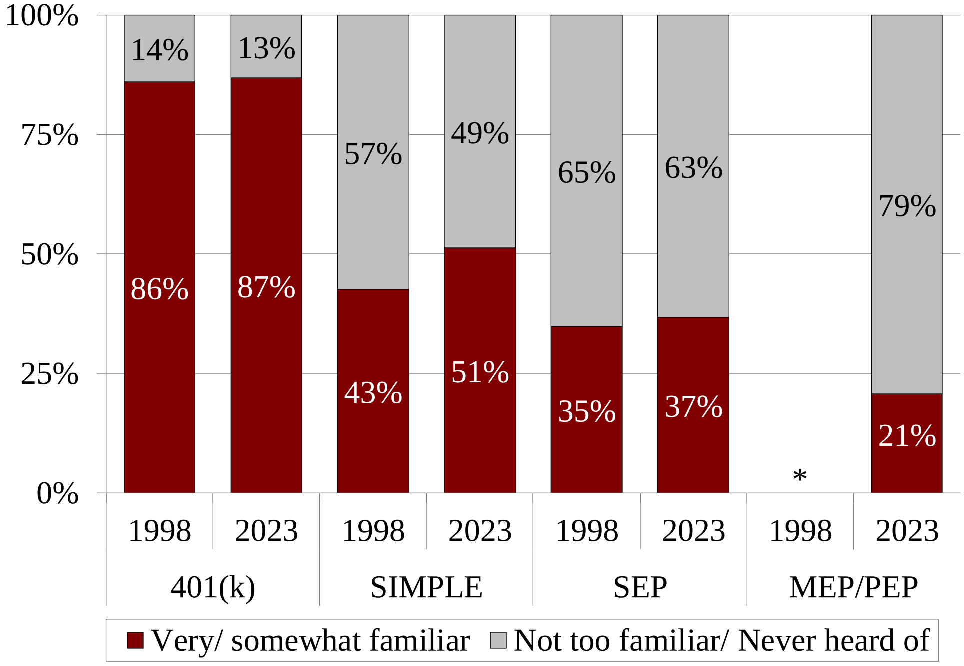


Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

Many small firms are also unfamiliar with the various retirement plan options that are designed to help ease the cost and administrative burden on the employer of offering a plan. While most small firms are at least somewhat familiar with 401(k) plans, the vast majority are not familiar with SIMPLE and SEP plans (see Figure 8). And this percentage has barely budged since 1998.

[11] Drobleyn (2023).

Figure 8. *Familiarity with Different Retirement Plans, 1998 and 2023*



* Firms were not asked about their familiarity with MEP/PEP plans in 1998.
Sources: Yakoboski and Ostuw (1998); and author's calculations from the *2023 Small Employer Retirement Survey*.

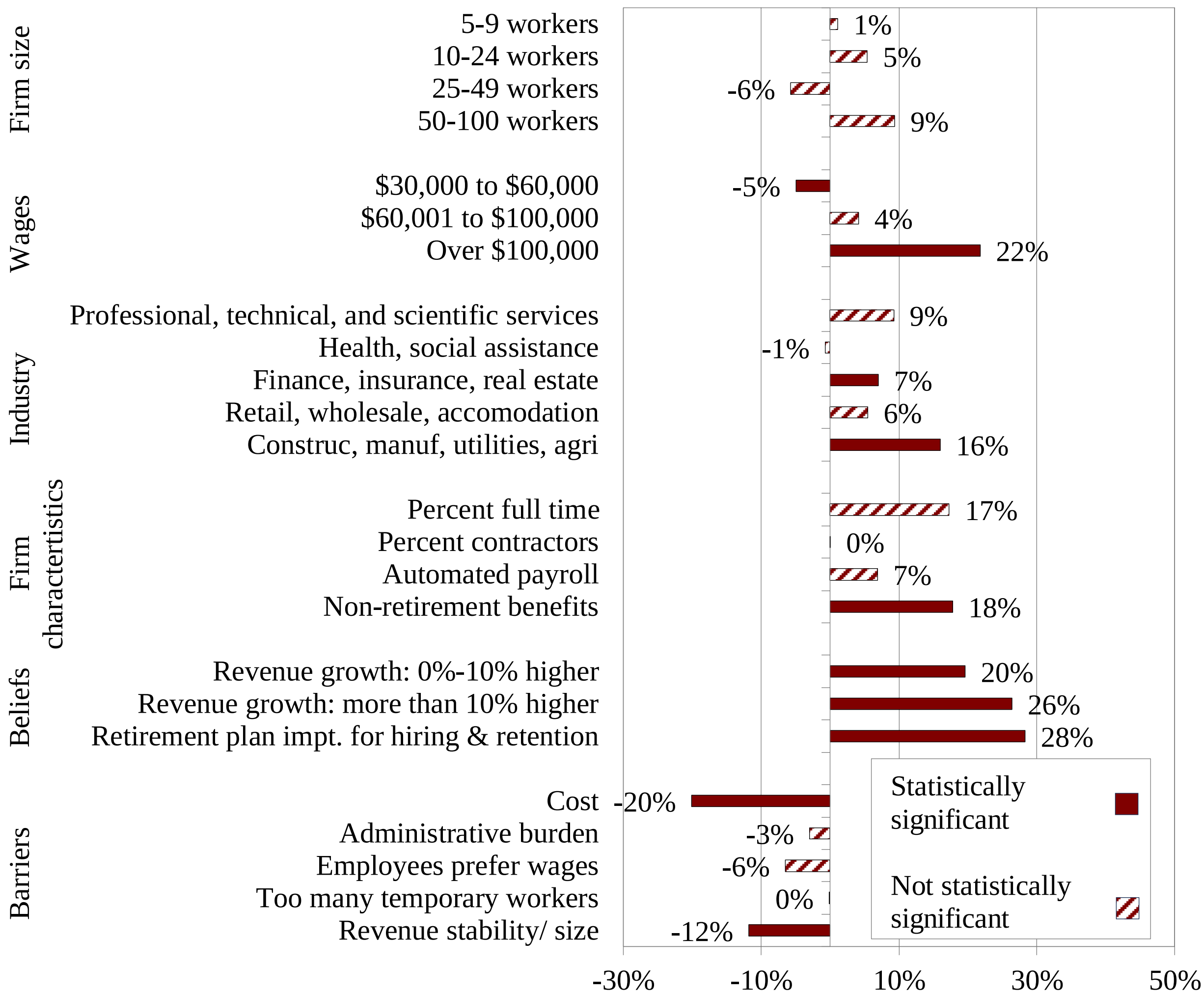
These results suggest that many firms overestimate the financial and time costs required to offer a plan, so better awareness of actual costs, as well as available options, could help reduce the barriers that small firms perceive.

Which Firms Are Likely to Start Offering a Plan in the Next Two Years?

New small firms may need a few years to get their business off the ground before they can entertain offering a retirement plan. So, an important question is which firms may just need time to become more stable before adopting a plan and which firms have no interest in offering one.

We once again estimate a simple linear regression to disentangle the relative importance of various factors on whether a firm is planning to offer a retirement plan in the next two years. Interestingly, perceptions matter a lot more, and firm characteristics matter a lot less (see Figure 9).

Figure 9. *Effect of Firm Characteristics and Perceptions on Likelihood of Offering a Retirement Plan in the Next Two Years, 2023*



Note: Solid bars are statistically different from zero at least at the 10-percent level.
Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

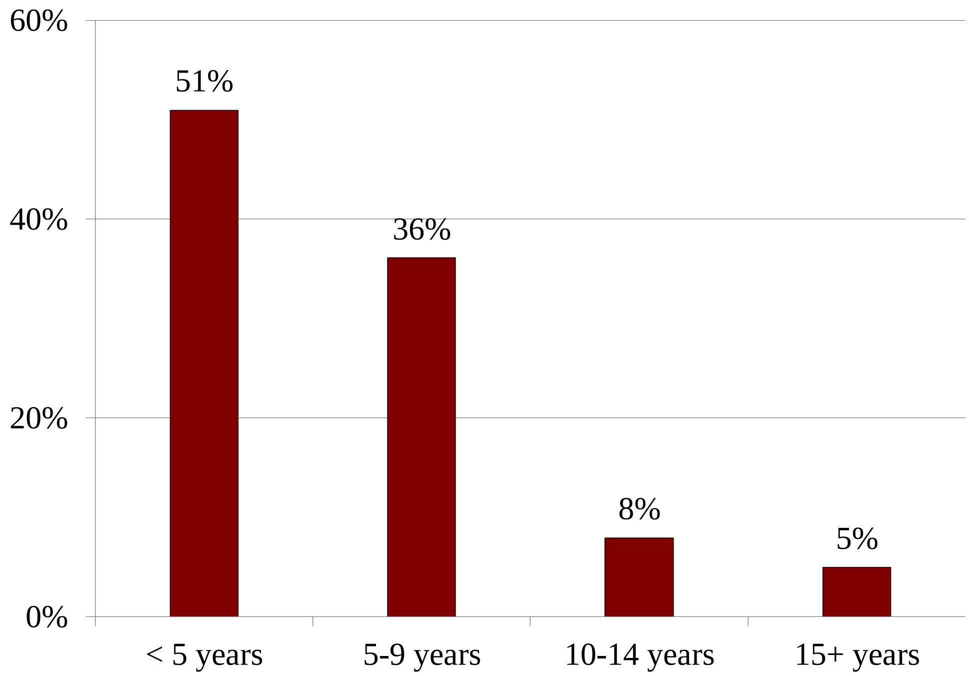
Not surprisingly, firms where the average salary is over $100,000 and those that offer other benefits say they are likely to start offering a retirement plan in the next two years. Firms in the construction, manufacturing, utilities, and agriculture industries are also more likely to say they will offer a plan in the near future. This result is driven mainly by firms in construction – perhaps due to labor shortages associated with the booming housing market and high building demands in recent years.[12] This finding is particularly striking because, as noted earlier, firms in this industry are less likely to currently offer a plan.

[12] Data from the *National Compensation Survey* show that the share of firms with fewer than 50 employees offering retirement plans grew from 48 percent in 2019 to 52 percent in 2021. This 4-percentage-point growth is the largest increase in coverage in over a decade, likely driven by labor shortages and increased competition for workers.

The biggest drivers of the likelihood of adopting a plan in the near future are whether firms believe their revenue growth will be higher next year and whether they believe offering a retirement plan is important for hiring, retention, or performance. Pushing in the other direction, firms that cite the costs of adopting a retirement plan or revenue stability/size as major concerns are much less likely to offer a plan in the near future.

The vast majority of firms that do offer a plan began offering one within 10 years of being in business (see Figure 10). About half begin offering a plan within the first five years and another third begin offering a plan in years 5-10.[13] This pattern suggests that firms that have been established for more than 10 years and still do not offer a retirement plan may be unlikely to offer one in the future.

Figure 10. *Years Since Establishment for Firms to Begin Offering a Retirement Plan, 2023*



Source: Author's calculations from the *2023 Small Employer Retirement Survey*.

Will State-sponsored Retirement Programs Impact Firm Behavior?

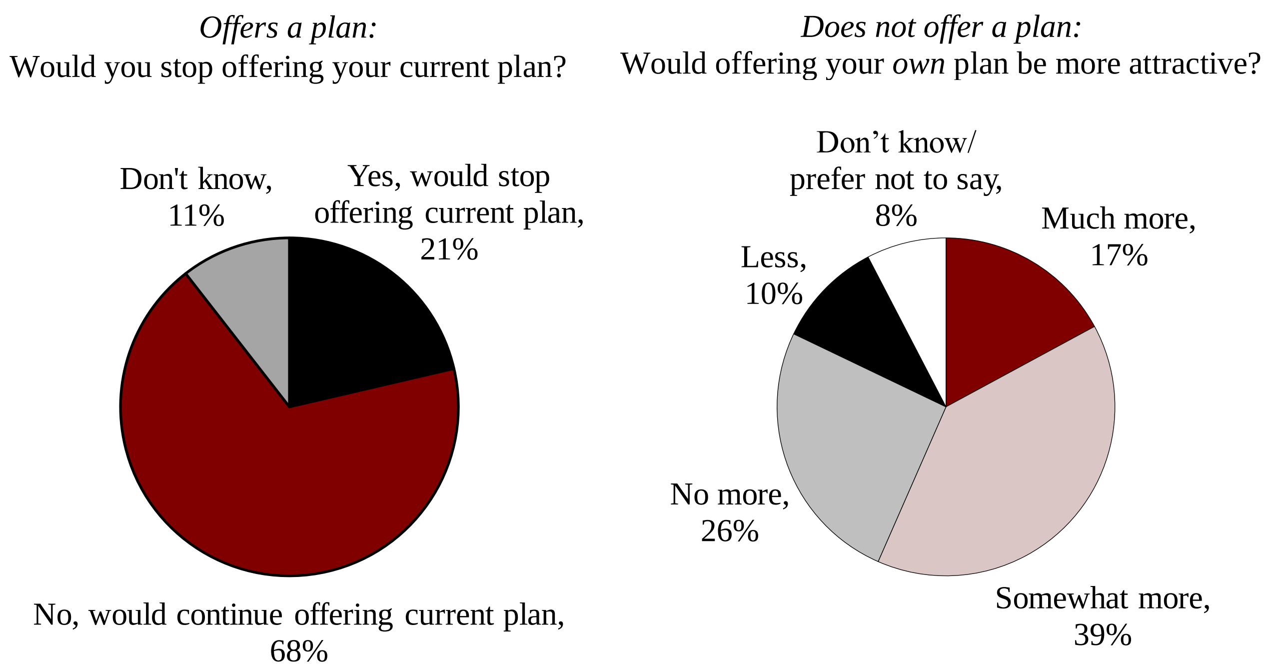
In recent years, a number of states have moved to offer retirement programs in an effort to move the needle on the coverage gap. Currently, 14 states have launched or are preparing to launch programs requiring employers without a plan to automatically enroll their employees in an Individual Retirement Account ("Auto-IRAs"). This move could shift small firms' perspectives

[13] The average salary of employees is the best predictor of whether a small firm will offer a plan in the first five years of establishment. Firms where the average salary is above $30,000 are much more likely to begin offering a plan in the first five years. Not much difference exists across salary bands at higher salary ranges.

on offering retirement plans, though the direction of the shift is not clear, so the survey asked whether employers would be less or more likely to have their own plan.[14]

The results show that the presence of state-sponsored programs does not seem to make firms less likely to offer their own retirement plan (see Figure 11). Among firms that already offer a plan, about 70 percent say they would continue to offer their own if their state introduced a mandate. Among firms that did not offer a plan, almost 60 percent said a mandate would actually make offering their *own* retirement plan more attractive. Perhaps, then, in addition to ensuring all employees have access to some retirement savings vehicle, these state programs may also encourage firms to offer their own plan.[15]

Figure 11. *Firm Response to Mandates in State-sponsored Retirement Programs*



Source: Author’s calculations from the *2023 Small Employer Retirement Survey*.

[14] Theoretically, it is unclear how firms might respond to mandates for state-sponsored retirement programs. Firms could stop offering their own plan and treat state-sponsored plans as an alternative to offering a retirement plan. Alternatively, a state mandate could be the catalyst needed to encourage firms to offer their own plans and change business or industry norms.

[15] A recent study, linking Form 5500 data and individual-level Census data, found that auto-IRA mandates increase the probability of firms offering a retirement plan by 3 percent and the probability that a worker participates in an employer plan by 33 percent (Bloomfield et al. 2023). A similar study by Guzoto et al. (2022) also found that state auto-IRAs complement the private market for retirement plans.

Conclusion

The coverage gap is a pressing concern for the nation's retirement income security, and the gap is driven by small employers. But, in fact, about half of firms with less than 100 employees do offer a plan for their employees. In order to encourage growth in coverage, it is important to understand the characteristics of small firms that do and do not offer a plan.

For firms that offer or are considering offering a retirement plan in the near future, their beliefs are important – such as whether they think retirement plans matter for employee hiring and retention and what their expectations are about revenue growth.

For firms that do not offer a plan, two major barriers – revenue stability/size and costs or administrative burden of having a plan – remain a top concern among small firms today.

Revenue concerns are highly associated with firm size, particularly firms with fewer than 10 employees. It is understandable that firms may need to become established before setting up a workplace retirement plan is seen as a viable option.

The second barrier, cost or administrative burden, however, seems to be driven by misperceptions about the financial costs and the time it would take to operate a plan. Many small firms are also not aware of the many options designed to help ease the burden on the employer of offering a retirement plan, such as tax credits or SEP, SIMPLE, and MEP plans. These results suggest that many firms overestimate the financial and time costs required to offer a plan and better awareness of the actual costs as well as plan options could help reduce the barriers that small firms perceive.

Finally, the growth of state-sponsored retirement programs does not seem to deter firms without a plan from offering one and it may actually encourage them to do so.

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