Portfolio Management

Employers stand ready to boost buy-in on 401(K) plans

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On the 30th anniversary of the creation of the 401(k) plan, employers are trying to tackle the escalating problem of employees not saving enough for retirement and reducing plan administrative costs.

That's because Americans' retirement savings rate is abysmal. People in their 60s who are retiring today have on average $144,000 in their 401(k) plans, according to the Retirement Confidence Survey published by the Employee Benefit Research Institute. Even with Social Security, the 401(k) funds are barely enough to cover 10 years or so of living expenses for the middle class, at a time when the average American is living 20 to 30 years after retirement.

With a volatile stock market and shaky economy – which directly impacts a 401(k) plan's value – employers' efforts to get more workers to save isn't an easy task. After rising in 2003 and for the next four consecutive years, the average 401(k) retirement account fell 27.8 percent in 2008. The good news is valuations rose 31.9 percent in 2009, which is the most recent data available.

"Many people are still in the frame of mind that someone else will be responsible for their retirement," said **Brian Hanna**, senior relationship manager with Everhart Financial in Columbus. "People are putting far too much weight on Social Security and that's going to be a small percentage of income after retirement."

Recession's impact

When the 401(k) was introduced in the 1980s, it was considered nothing more than a supplement for retirement income. But over the years it has become the primary source of income after retirement.

There are three primary programs Americans use for income after they are done working: pensions, Social Security and 401(k)s. Pension plans are dwindling – they accounted for just 10 percent of workers' retirement plans in 2005, according to the Employee Benefit Research Institute – while many claim Social Security may dissolve within 30 years.

Pension plans – funded by employers by holding back part of an employee's paycheck – had been a favorite of retirees for decades because they provided guaranteed income. The concept was introduced in the 1700s to benefit widows and children of ministers.

Social Security's roots date to 1935 when President Franklin D. Roosevelt signed the Social Security Act to provide guaranteed income for people after they retired.

In the 1980s, 401(k)s started to take hold because they were less expensive for businesses to offer than pensions.

Now that the concept has gained traction with more than 50,000 employer-sponsored 401(k) plans, the next step is for businesses to help workers get the most out of them and convince more people to participate in them.

In 2010, 59 percent of workers said they were saving for retirement, down from 65 percent in 2009, according to the Retirement Confidence Survey. The recession hurt many people who lost jobs and no longer contributed to a retirement plan. Others were faced with severe financial difficulty and had to dip into the plan to make ends meet.

The survey from March 2011 discovered some disturbing trends:

• About 35 percent of workers age 45 or older are not saving for retirement.

• Nearly 29 percent of those older than 55 say they have less than $10,000 in retirement savings.

• About 56 percent of workers have less than $45,000 in savings and investments, including 29 percent with less than $1,000.

• And 58 percent of workers said they have not done a retirement needs calculation.

More than half the people surveyed said they had $25,000 or less saved for retirement. That's far below the necessary $500,000 or more needed to sustain a middle-class lifestyle after retirement.

Scott Everhart of Everhart Financial said 401(k) plans have helped employees. "We would say that as a supplement for someone that has the other two streams of retirement income, they have worked just as intended," he said.

The reason 401k plans have become the dominant plan is really due to challenges with defined benefit plans and the subsequent reduction in their use, Everhart said. Companies can have wildly varying funding requirements annually to defined benefit plans.

"That can cause major problems with cash flow and profitability," he said. "With 401(k) plans, companies can commit to a company match and/or a profit sharing contribution, and they can be quite generous, but most importantly, they can be predictable."

To address the fact that defined benefit plans are less common, Everhart is seeing 401(k) plan providers view participant balances as a funding mechanism to provide retirement income streams. For example, just as defined benefit actuaries have to take into account planned annual deposits, assumed rates of return and planned current balances in order to calculate retirement income streams, 401(k) participants should take the same factors into account in order to estimate their probable retirement income stream. Plan providers are beginning to provide this type of software and communications.

"As these trends continue, 401k plans will do a better job of filling the gap that defined pension plans have left behind," Everhart said.

Buying in

One way to raise participation is through a one-on-one counseling session with an employee, Hanna said. In the past, an employer often would hold a group session for a few hours to explain the retirement plan. He said a little more than half of employees on average would contribute.

Employers now are taking a more aggressive approach. Some businesses are offering free one-on-one consultation with a financial planner to calculate how much employees need to save to sustain their current lifestyle. An employee who has a private meeting is far more likely to contribute more to his 401(k) plan, compared with those who don't have the personal experience, Hanna said.

Another trend is the "opt-out" approach. Since 401(k) plans were introduced, employees had the option of enrolling. Now, many employers are automatically enrolling employees, requiring them to opt out if they don't want to participate.

"The 401(k) plans are really the best vehicle for retirement," said **Grace Schmitt**, vice president of Human Resources at Glimcher Realty Trust in Columbus.

As a property management company, Glimcher has a diverse pool of employees.

For employees on the lower end of the pay scale such as housekeepers and security workers, it has been difficult to convince them to enroll in the plans. They often need to use every dollar they earn for living expenses and savings doesn't seem like a viable option, Schmitt said.

Reducing Fees

For years, providers that managed 401(k) plans handled the administration, investments and consulting.

"It was a one-stop shop," Schmitt said. And that system wasn't always ideal. Often it was difficult for the employer to know how much a plan was charging in fees.

The one-stop shop method of businesses for 401(k) plans is starting to break apart. Employers now have the option to shop for the best administrator or investor rather than be locked into one company doing everything, Schmitt said.

Companies that provide 401(k) services also are starting to be more transparent with fees, said **Julie Kasper**, CFO of Columbus-based Hull Inc., an engineering consultancy. "With this new approach, we know exactly how much in fees is going to each organization," said Kasper. "Before, the vendor fees were hidden and lacked transparency."

With transparency and ability to shop around, Glimcher was able to save about $75,000 a year in fees, Schmitt said.

In the majority of 401(k) plans, the employer will match a percentage of the employee's contribution. Many consider this "free money."

"There is a real disconnect between what employees are doing and what they'll need," Hanna said. "Employers are doing what they can to convince employees to save more."

Troy May is a freelance writer.