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It Is Time for Employees to Set Their Retirement GPS

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Abstract
Employees are confused by all the retirement issues facing them, as they are now responsible for managing their retirement future. Employers, however, are not off the hook as they have a fiduciary responsibility to manage the operations of the plan offered to their employees. This article explores how employees can create a retirement GPS to help them sift through the maze of retirement information and follow a planning path to a successful retirement destination, and why it is important for employers to play a role in helping them during this process.

Keywords
retirement counseling, baby boomers, pension, retirement planning, employer fiduciary responsibility

Most new employees seeking to enroll in their company's retirement plan have the same initial question, "Where do I put my money and how much of my earnings should I put aside for retirement savings?" For those employees who are in the midlife of their career, as well as those close to retirement, the issues are even more daunting. Midcareer employees are facing questions about balancing retirement contributions while paying off debt, and pre-retirees are concerned about having enough money to live on after they retire. Recently, as legislation has raised the awareness of plan fees, employees are starting to inquire about those fees they are paying to their employer's retirement provider. As employees are contemplating these issues, employers have started to take a second look at how responsible they should be in helping their employees sort through these issues. Many of them have hired consulting firms to assist them with conducting analysis on plan utilization, evaluate plan fees, review the services offered by their vendors and guide the process to make sure that the plan is in compliance with ERISA regulations.

Some employers believe these are simple steps and not such a big deal. However, it is a very big deal! If a plan is audited by the Internal Revenue Service and an employer is not monitoring fees, or following plan provisions in a plan document, or tracking investment performance, they run the risk of being out of compliance and facing potential fines. Employers will be able to sleep better at night knowing they have conducted their due diligence as they continue to look for ways to assist employees to have a more secure retirement.

Almost any paper, magazine or blog on a weekly basis carries a story in the financial section on how people are not saving enough for retirement. You can look almost anywhere and find data on retirement issues. Experts say we are in a "retirement crisis" as Americans cannot afford to retire, and employers are reluctant to hire older workers in fear of the rising cost of health care. However, to employees, it is all so confusing. Some employees complain that retirement plans offer too many investment choices and they have no help (nor any clue) on how they should be investing money over the long term. There are also concerns that Social Security is going to run out of money by 2033. Then, there is the issue of the stock market and concerns that a correction will occur causing people to lose money—and their minds. What is one to do?

First, everyone should take a deep breath. The good news is that all these factors are making people more attentive to their retirement plans and statistics are starting to look better. Additionally, we are seeing employers creating more "outcome-based solutions" to help employees sort through these issues.

According to the Employee Benefits Research Institute, only half of private sector workers were covered by an employer-sponsored retirement plan of any kind in 2011. In 2013, a report from the Center for Retirement Research's National Risk Index indicated that half of U.S. households were at risk of being unable to maintain their preretirement standard of living. However, in the

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August 2014 release of Transamerica's 15th Annual Retirement Survey of over 4,000 workers, 64% of respondents revealed that they were somewhat or very confident that they would be able to retire with a comfortable lifestyle. In essence, as the economy recovers from the recession, retirement confidence has also started to rise.

One reason there is so much information available on retirement is that employers have three distinct generations of future retirees: Baby Boomers (born between 1946 and 1964), Generation X (born between 1965 and 1978), and Millennials (born between 1979 and 1996). According to the Transamerica survey, Baby Boomers continue to be the generation who place retirement savings as their number-one priority (38%). Generation X employees entered the workforce in the late 1980s, just as 401(k) plans were starting to become commonplace. This generation was the first one to have access to 401(k) plans for most of their working careers, and accordingly, they value the 401(k) plan as an important benefit. Millennials and Generation X respondents listed "just getting by in covering daily expenses" and "paying off debt" as their top financial priorities, respectively. Of the three generations of surveyed respondents, results specify that Millennials are the least likely to participate in a retirement plan (71% indicated they participate in their employers plan) compared to Baby Boomers (81%) and, surprisingly, Generation X (84%). For those not participating in their employer's plan, 26% identified "being financially strapped" as the number one reason for not participating, followed by 14% indicating that they save for retirement in other ways.

So what does all of this mean? For one, 401(k) and similar type plans have become the primary retirement vehicle, placing more responsibility on all employees. This is a shift from many years ago when *employers* were responsible for managing retirement plans when defined benefit plans were the popular retirement vehicle. Historically, the burden fell to the employer under the traditional defined benefit arrangement to take on the investment risk of the plan and make all the decisions to ensure a benefit is available at retirement for each employee. Not anymore. The burden has shifted to the employee under the defined contribution approach (i.e., 401(k) plans, 403(b) plans, etc.) to manage their accounts.

With employees more responsible for managing their retirement arrangements, it has become challenging, to say the least, to understand and make the best decisions for their long-term future. For example, an employee who meets their employer's retirement plan eligibility typically faces the following decisions, among others:

- How much can I afford to contribute from my paycheck?
- How much will my take home pay be reduced?
- How much will I need to retire?
- Where do I go to learn more about the plans offered by my employer?
- What are the fees if I decide to enroll?
- How do I actually enroll in the plan?
- Which investment option(s) should I select?
- How have the funds performed historically?
- Are there any restrictions on the investment options?
- What distribution options are available?

In addition to addressing these questions, employees offered multiple investment providers for their retirement plans have additional confusing choices as they also have to figure out which firm is the best choice to receive their contributions.

There are major concerns expressed by workers about their retirement. In the Transamerica survey, 82% of all respondents believe their generation will have a much harder time achieving financial security compared with their parent's generation. Even more alarming, nearly 70% indicated that they do not know as much as they should about retirement investing—that is 70%! If most employees do not know as much as they should about retirement, how are they supposed to answer all the questions we just posed as a new employee seeking to enroll in the retirement plan? This is one reason why we have a retirement crisis. People do not understand what they have, and they do not know what to do about it.

Taking it one step further, 75% of respondents indicated that they had "none or just some" understanding of asset allocation. With little understanding of asset choices—arguably, the most important issue in retirement investing—did they choose an allocation by throwing darts at a screen? Did they ask what their colleagues did, or randomly choose based on what sounded good? Did they come to their employer and say, "Tell me what to do?" Houston, we have a problem.

These statistics are alarming and consistent with other data. In an April 4, 2012, Washington Post article titled: "Rise of the 401(k): More Americans Are Managing Their Own Retirement Savings. For Many, That Means Trouble," a 2011 Gallup poll was noted indicating that 75% of Americans stated that not having enough money for retirement was their top financial worry. Not enough money for retirement? Not surprising, since current data suggest little understanding of allocation choices and how employer retirement plans work. Similarly, in the Transamerica report, 46% of respondents feared that they will outlive their savings or not be able to meet basic financial needs for their families.

Saving for retirement is difficult if you do not understand how much you need to retire or how to get there. How can you drive to a destination if you do not know how to get there? Use a GPS? Well, actually, yeah.

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The Answer?

The answer is first knowing the question, and the question is, "Where are you going and how do you get there?" Today, almost everyone has a GPS or Global Positioning System in their car. If not, they can pull up GPS on their phone, use Google Maps (or for the Baby Boomers, they can still use Map Quest). That provides an individual's current location and helps set the course for where they need to go. Is that not the retirement planning process? People need to know where they are currently in the retirement process, and how to get to their desired retirement destination. If employees use *Great Planning Strategies* (retirement GPS), they can reach their destination. Accordingly, employers need to hire financial service firms that offer planning tools for employees.

An employee's ideal retirement destination goal should be to have a lifetime retirement income that replaces about 80% of their preretirement income, including Social Security, employer-sponsored plans, IRAs, voluntary contributions to tax-deferred or Roth-type vehicles (Roth vehicles are after-tax monies) and any other personal savings dedicated to retirement. Depending on their lifestyle, they may need more, but for most Americans, 80% is appropriate based on the latest financial planning data.

Now that a destination is determined, how do employees get there? Here is where the retirement GPS tools come in handy. Financial services firms have created all types of retirement GPS services. For example, new employees who are not investment savvy in selecting an investment option can now choose lifecycle or target-based funds on enrollment. These arrangements are designed to track the year closest to when an employee plans to retire, and provide a diverse allocation mix that automatically changes as they get older, becoming less risky the closer employees are to retirement. These arrangements are considered a "set-it-and-forget-it" vehicle and are becoming very popular for new employees. Research by an investment company, The Vanguard Group, indicates that 80% of new enrollees will select these investments by 2018. Several institutions also use lifecycle funds as a default option for new employees enrolling in a plan. As a best practice, institutions also use "auto increase" and "auto escalator" as additional tools. Financial services firms have all types of other helpful online vehicles like income projections and paycheck tax-calculators that can also assist with long-term planning.

Once an allocation has been selected, the next question is how much money should an employee put away? Funding of the plan is the fuel that drives the engine of the retirement destination. According to financial services firm Charles Schwab, if a participant starts saving in their 20s, the savings rate should be 10% to 15% or more going into the employer plan. In the 2014 PRM Management Compensation Survey of over 360 institutions, the average employer contribution rate was 7.6%. That means that employees should be putting in at least another 7% to 8% on their own to reach the 15% goal, as long as the annual Internal Revenue Service limits are not exceeded. This number includes employer *and* employee contributions. The range rises to 23% to 35% if the employee delays starting until their 40s. Obviously, the sooner an employee enrolls in a plan the better off they will be. Ten to 15% for most employees is a challenge, and 23% to 35% is almost impossible. These numbers take historical returns into account. Following this course of reaching the 10% to 15% number, an employee's retirement GPS should start bringing their destination into focus.

Deciding how much money to put away is probably the most important first step to understand the design of the employer's retirement plan. The majority of plans contain a matching feature, and employees are sometimes challenged by how much they need to contribute to receive the match by their employer. While it may not always be possible based on individual circumstances, employees should strive to put away the maximum amount of money needed to maximize the employer match. For example, if the employer provides a 50% match on the first 6% that the employee contributes, the initial goal of the employee should be to contribute at least 6% in order to receive the full 3% employer match.

What happens to your car GPS when you make a wrong turn? It recalculates and takes you on a different route to reach the same destination. The same is true with retirement planning. Along the way, employees may have to recalculate as life gets in the way; maybe they had to reduce their contributions due to financial issues, or they had to use the loan feature to borrow funds (which we do not suggest unless absolutely necessary) from their plan. There are times when the employer may also have to reduce the employer contribution, placing more stress on the employee to stay within the noted ranges. These examples represent wrong turns and necessitate the need to recalculate an employee's retirement goals. So if there are years where the employee is under the 15% number, they will need to have years where they are over the 15% to make up the loss. An employee may also have to review their strategy if the market has a significant drop (or gain).

Recalculating *Great Planning Strategies* should occur when employees make that wrong turn or have one of life's challenges knock them off course. An employee may have to increase contributions, make more aggressive allocation choices or delay a purchase to enhance their retirement savings. Alternatively, they may have to

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delay retirement because they have not saved enough, causing stress on the employer as the workforce gets older and employees cannot leave because they do not have enough money. Employers are then forced to offer retirement incentives to persuade older workers to leave, potentially costing the employer more money. That is why it makes good business sense for employers to help employees utilize their retirement GPS.

One reason why Millennials and Generation X employees listed "just getting by and paying off debt" as their top financial priorities in the survey is because they lack a retirement GPS. They tend to live in the now.

> Forego the latest iPhone to fund my retirement plan? Are you kidding? Who cares that I only contribute 5% of my pay to retirement plan and am drowning in student loan debt. Retirement can wait; I want the newest item on the market, be it Jimmy Choo shoes, the new 745i BMW, or season tickets to the local professional team.

All very nice things if one can afford them, but these are wants not needs, and they can deter an employee from following their retirement GPS.

No matter where someone is right now in terms of retirement, and no matter what generation they are in, one can still start their retirement GPS. For Baby Boomers close to their ideal retirement age, they may have to be more aggressive with their investment choices, or consider working longer. For Generation X, data show this group is not saving enough. Fortunately, time is on their side and they should evaluate how they can get to that 10% to 15% range by cutting down on debt. For Millennials, considered a do-it yourself generation of retirement savers, this GPS approach may make the most sense. Millennials have many years to plan, hit some bumps along the way and recalibrate their course as needed. The key, however, is will they learn from the mistakes of other generations?

Conclusion

Even though the burden of managing the pension program has shifted from the employer to the employee, the employer still plays a major role. Some employers create personal counseling days for employees to meet one-on-one with financial planners, others conduct ongoing group education sessions, while others seek providers that have retirement apps that can be downloaded to employees phones. Otherwise, like the survey respondents, employees will continue to be confused about retirement, not knowing what to do and having little confidence that they will have enough for retirement, and will be looking to their employer for help. With no retirement GPS, employees will continue to have a series of retirement questions and a lot of data with no clear plan as to what to do. For others, setting their GPS can align them on the right path to a retirement destination.

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