



Strategies to Improve Retirement Readiness

September 2014

Introduction

Retirement experts agree that Americans continue to face a financial retirement crisis – they are not prepared to retire. Workers face an increasing risk of not having enough funds to maintain their lifestyle through retirement.

Many factors contribute to Americans' retirement insecurity. One possible cause is the ongoing shift from defined benefit pension (DB) plans to defined contribution (DC) plans, which puts greater responsibility on individuals to plan for retirement.¹ From 1979 through 2010, the percentage of private sector workers covered by a DB plan decreased dramatically from 62 percent to 7 percent, while the percentage covered by a DC plan increased from 16 percent to 69 percent.² Despite the decline in DB coverage among the private sector, the public sector remains committed to DB plans, providing DB coverage to more than 85 percent of public sector workers in 2010.³

This paper identifies key findings about retirement readiness among workers in the U.S. and strategies to help individuals plan for retirement. It concludes by noting potential opportunities for employers to engage their employees in retirement planning.

Retirement readiness

Retirement confidence among Americans remains low despite the improving economy.

Research indicates 13 percent of Americans are “very confident” and 38 percent are “somewhat confident” about having enough money to live comfortably throughout retirement.

Retirement confidence is low because Americans now realize how much they need to save to retire comfortably. Many Americans are preoccupied by more immediate financial concerns such as high debt, job uncertainty, making ends meet, and paying for health insurance or medical expenses. Half of all Americans do not even have \$2,000 in savings to cover an unexpected need.⁴

Research also shows that Americans are having a harder time preparing for retirement. Issues complicating retirement planning include:

- Bleak economy
- Fewer pensions
- Middle class salaries not keeping up with inflation
- Social Security status (unsure that Social Security will be there when they retire)⁵

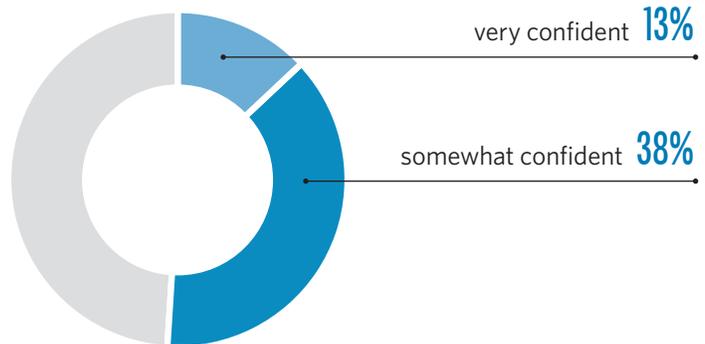
Certain populations are at greater risk than others when preparing for retirement such as individuals under 30 years old (Millennials), women, and low-income families.⁶ Those with higher household incomes and educational levels, however, are more likely to save for retirement.

Retirement planning strategies

To address the lack of retirement readiness, many employers are considering or actively implementing strategies to help employees plan financially for retirement. Strategies include:

- Boosting financial literacy
- Leveraging behavioral economics
- Tailoring retirement education
- Being a key source of information for employees

Retirement confidence among Americans



Boosting financial literacy

Studies show that low financial literacy can lead to inadequate savings. As a result, financial literacy has gained attention from interest groups, policy makers, government agencies, and other organizations.⁷

Findings also indicate that efforts to boost financial literacy, particularly among the newly hired, should:

- Focus on the understanding of key concepts to improve employees' overall financial literacy (e.g., inflation, numeracy, and risk diversification)
- Recognize that debt management and retirement savings go hand in hand – Employees should look at their entire financial picture when planning for retirement
- Provide employees with basic retirement plan information
- Remind employees about investment risk⁸

Some employers have their own financial literacy programs while others are partnering with interested stakeholders to help individuals achieve more secure financial futures. For example, the California State Controller's Office works with governmental and nongovernmental stakeholders to promote and organize financial literacy events for public awareness.⁹

Findings show that it is critical to understand existing legislation that guides the availability and format of financial education. It is also important to recognize what drives saving behavioral changes and to measure the effectiveness of financial literacy programs based on participant savings behavior versus participation.¹⁰

Leveraging behavioral economics

Traditionally, employers left the choice of participating in a DC plan to the employee. Research shows few employees take action to enroll in a DC plan, and when they do participate, they are not saving enough. A potential strategy to address this challenge is for employers to adopt automatic features, requiring employees to opt-out rather than opt-in. Findings from behavioral economic research indicate that many employees typically do not take action to opt-out, thus increasing participation and employees' savings.¹¹

Two effective methods are automatic enrollment and automatic escalation. Automatic enrollment is an essential strategy to overcome workers' procrastination tendencies. Retirement plans with an automatic-enrollment feature have the highest employee participation rates. The enrollment rates average 50 to 80 percent without automatic enrollment compared to over 90 percent of those who have automatic enrollment.¹²

Another effective method is automatic escalation, particularly when tied to pay raises. Based on a recent study, an employer who implemented automatic escalation saw 78 percent of employees almost quadruple their saving rate in slightly less than four years.¹³

Although automatic enrollment and automatic escalation have proven to be highly effective, there are certain legal restrictions to consider before implementing any automatic features. In addition, these two methods may not be appropriate for all employees. Retirement readiness requires planning for individual lifestyles, basic needs, and expectations of providing or receiving support from family.¹⁴

Tailoring retirement education

Tailoring retirement education to meet employees' specific needs provides a more individualized approach to retirement planning. Research shows that designing employee-centric materials that incorporate an employee's perspective is an effective method of outreach.

Tailored retirement education is not a one-size fits all approach. Tailored retirement education:

- Includes levels of customization based on the employees' needs and learning style
- Considers generational differences in levels of retirement readiness and financial literacy
- Focuses on employees' retirement goals and shows how the plan offered is an important piece of a successful retirement strategy
- Focuses on all aspects of employees' financial life¹⁵

Employers are recognizing the benefits of using technology to tailor retirement education to effectively reach specific audiences. Online tools are becoming more prevalent, allowing customized ways to educate individuals about retirement savings and personal finances.¹⁶ Research shows that online calculators help individuals set more adequate savings targets for retirement. Younger households in particular are predicting savings targets that are more likely to be adequate than their older counterparts.

Mobile applications are also becoming a standard business practice. Many financial service providers are offering mobile applications to allow a member to view their account status via their mobile device. An example includes how a member checks a bank account through a mobile device. Research further indicates mobile applications, virtual planning tools, and live interactive webcasts provide timely and accessible financial information, especially for Millennials.¹⁷ In addition, social media offers a low-cost means to connect with members of all ages and may be an effective way to engage and educate employees. The effectiveness of these tools, however, should be studied further.

Being a key source of information for employees

In addition to tailoring retirement education, it is important to consider the timing of this education. Research indicates that the timing of retirement education is particularly important when encouraging employees to take action and that employers are in the ideal position to provide employees with this information.¹⁸

Regular reminders of the value of retirement planning and providing financial information to employees at “teachable moments” appear to be effective.¹⁹ Examples of “teachable moments” include providing information at the time of hire, when an employee receives a pay increase, or when an employee experiences a life event such as marriage or the birth of a child.

Research shows that organizations are starting to use timelines to provide retirement education at life, decade, and career stages to help employees understand that retirement is an ongoing journey. Receiving information years before actual retirement, advance understanding of the importance of lifetime income, and early action from employees is highly beneficial.²⁰

Conclusion

With the ongoing shift of responsibility from the employer to the employee for retirement planning, it is essential for working individuals to begin planning for retirement early in their careers. There are potential opportunities for employers to help engage their employees in planning for retirement as they are uniquely positioned to provide their employees with timely and accessible retirement education.

To develop an effective strategy that works best for an organization, research shows it is important to assess employees’ retirement readiness and understand their demographics. Findings from the assessment will help shape a strategy that best suits employees’ needs and adopting the right technologies can help support the implementation. It is also important to develop measures to evaluate the effectiveness of the strategy, which is critical to continuous improvement.

Strategies to engage workers to plan for retirement early in their careers can lead to greater retirement readiness and increased retirement security.

Endnotes

- ¹ Benartzi, Shlomo, and Richard H. Thaler. “Behavioral Economics and the Retirement Savings Crisis.” *Science Magazine*. Volume 339. American Association for the Advancement of Science, 8 March 2013. Web. 20 December 2013.
- ² Employee Benefit Research Institute (EBRI). “FAQs about Benefits – Retirement Issues.” EBRI, n.d. Web. 20 June 2014.
- ³ Brainard, Keith. *Public Fund Survey Summary of Findings for FY 2010*. National Association of State Retirement Administrators (NASRA), December 2011. Web. 16 June 2014.
- ⁴ Helman, Ruth, et al. “The 2013 Retirement Confidence Survey: Perceived Savings Needs Outpace Reality for Many.” *EBRI Issue Brief*. No. 384. EBRI, March 2013. Web. 4 February 2014.
- ⁵ Oakley, Diane, and Kelly Kenneally. *Pensions and Retirement Security 2013: A Roadmap for Policy Makers*. National Institute on Retirement Security, February 2013. Web. 10 December 2013.
- ⁶ Financial Finesse Inc. “State of U.S. Employee Retirement Preparedness.” *Financial Finesse Reports: Research on Financial Trends*. Financial Finesse Inc., 3 October 2013. Web. 30 January 2014.
- ⁷ Braunstein, Sandra, and Carolyn Welch. *Financial Literacy: An Overview of Practice, Research, and Policy*. National Bureau of Economic Research (NBER), November 2002. Web. 14 January 2014.
- ⁸ Clark, Robert, and Annamaria Lusardi. “How Employers Can Help New Hires Save for Retirement: Best Practices that Build Long-Term Financial Security.” *Insights: American Financial Capability*. Financial Industry Regulatory Authority, September 2012. Web. 10 November 2013.
- ⁹ California State Controller’s Office. <http://www.sco.ca.gov/>. 20 June 2014.
- ¹⁰ Agnew, Julie, and Joshua Hurwitz. *Financial Education and Choice in State Public Pension Systems*. NBER, March 2013. Web. 7 November 2013.
- ¹¹ Benartzi, Shlomo, and Richard H. Thaler.
- ¹² Robinson, Mark. “EBRI’s Spring Policy Forum: Retirement Income Adequacy – How Big Is the Gap and How Might the Market Respond?” *EBRI Notes*. Vol 31. No. 8. EBRI, August 2010. Web. 20 June 2014.
- ¹³ Benartzi, Shlomo, and Richard H. Thaler.
- ¹⁴ AEGON. *The Changing Face of Retirement: The Aegon Retirement Readiness Survey 2013*. AEGON, n.d. Web. 13 February 2013.
- ¹⁵ Davidson, Liz. *The Impact Financial Education Has on Plan Participant Saving and Investing*. Financial Finesse Inc., 18 November 2013. Web. 27 February 2014.
- ¹⁶ accenture. *Public Retirement Systems: Invest in Change to Reap Long-Term Dividends*. accenture, 20 March 2013. Web. 19 May 2014.

- ¹⁷ Prudential. *Younger Workers and Retirement: A 2012 Study by Prudential Retirement*. Prudential, December 2012. Web. 10 December 2013.
- ¹⁸ Lifetime Income Risk Joint Task Force. *Risky Business: Living Longer Without Income for Life*. American Academy of Actuaries, 2013. Web. 10 December 2013.

- ¹⁹ Clark, Robert L., and Melinda Morrill. “What Influences New Hires to Save for Retirement?” *Insight: Emerging Research from the Study of Financial Literacy*. Financial Literacy Center, November 2010. Web. 19 December 2013.
- ²⁰ Lifetime Income Risk Joint Task Force.

Glossary

Auto Enrollment: An automatic feature in a defined contribution plan that allows employers to enroll eligible employees in the plan unless the employee affirmatively elects otherwise.

Auto Escalation: An automatic feature in a defined contribution plan that allows employers to increase employee contributions incrementally every year or upon pay raises or promotions unless the employee affirmatively elects otherwise.

Behavioral Economics: A method of economic analysis that applies psychological insights into human behavior to explain economic decision-making.

Career Stages: Stages that employees experience throughout their career, starting when newly hired and ending when they leave or retire from the organization.

Defined Benefit Plan: Retirement plan that provides a guaranteed benefit, generally paid in the form of a life annuity and based on a predetermined formula. Benefits are generally calculated based on age at retirement, years of service and final compensation. Employer contributions are actuarially determined and may vary annually. The plan may require employee contributions.

Defined Contribution Plan: Retirement plan that provides a non-guaranteed benefit based solely on the value of a participant’s individual retirement account. Benefits depend on the value of the individual’s account upon retirement, which varies depending on contributions and investment earnings and losses. Benefits cease when the account balance is depleted, regardless of the retiree’s age or circumstances. Contributions depend on the plan terms and can include both employer and employee contributions.

Demographics: Assessment of population factors such as age, race, gender, economic status, level of education, income level, and employment, etc.

Financial Literacy: Combination of financial awareness, knowledge, skills, attitudes, and behaviors necessary to make sound financial decisions and ultimately achieve individual financial well-being.

Generations: A group of individuals born and living during the same time, such as:

- Baby Boomers (born between 1946 and 1964)
- Generation X (born between 1965 and 1979)
- Millennials (born between 1980 and 2000)

Life Events: Events that individuals experience throughout their life that changes their status or circumstances, such as the birth of a child/children, marriage, divorce, death of spouse, or job loss.

Online Tools: Tools available online and mobile applications that provide users with readily accessible information, such as account information, a retirement calculator or virtual planning tools. Other examples include social media where users interact or exchange information in virtual communities and networks.

Lead Researcher

Milly Romero-Salas

Contributors

Kimberly Calija, Gina Crawford,
Gentian Droboniku, Kyle Harris,
Michelle Mitchell, Vickie Montosa,
Veronica Sanchez, Stacie Walker,
Valerie Wong

*The Retirement Research and Planning
Division would like to thank Joseph Caffrey
and Michael Ugenti for their valuable
comments.*