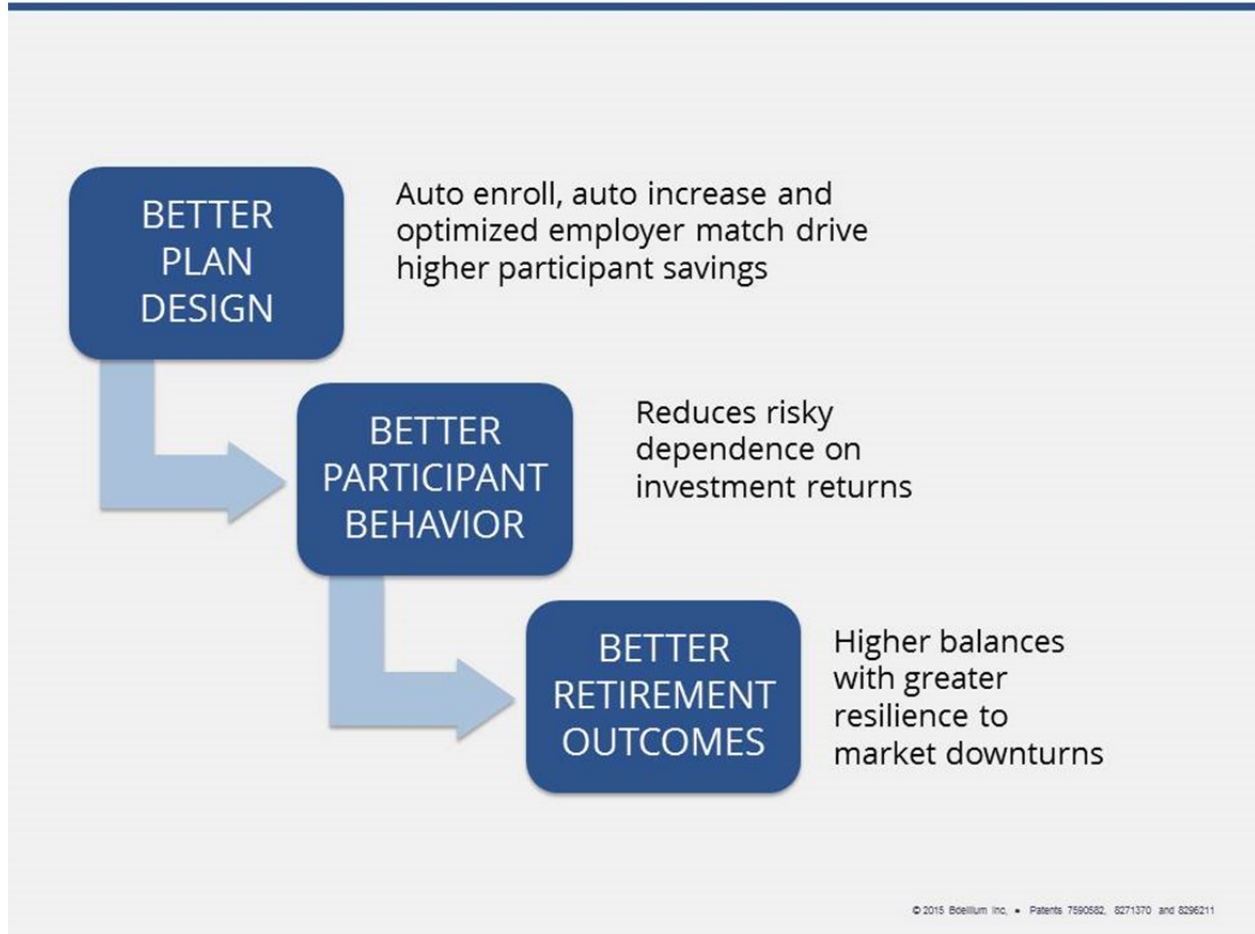


Improving Retirement Outcomes is Not Rocket Science

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Everybody Wins with Better Plan Design

Retirement plan design has an enormous effect on whether employees will be able to retire with some semblance of financial security. Smart plan sponsors recognize that helping their employees prepare better for retirement makes good business sense because it strengthens employee loyalty, reduces financial stress that causes

lower workplace productivity and minimizes additional employer costs due to delayed retirement by older workers. Smart advisors know that one of the best ways to quantify delivered value is to track higher participant savings and better projected outcomes that can be directly linked to improved plan design.

Here are three tips to help plan sponsors and advisors achieve their common goal of helping employees to maximize savings and minimize retirement risk.

More Insights, not More Data

Today we deliver an ocean of data to plan sponsors including participation rates, average deferral rates, percentage of participants maximizing the employer match, retirement readiness ratios, participant investment selections – to name just a few common data points.

Unfortunately, data alone will not help improve outcomes, particularly if we rely on average plan data or blindly use measurements without understanding their limitations. For example a high average participant deferral rate might compare well to an industry index but it can be very misleading if it is really a barbell of those saving a lot and those not saving at all. Segmenting by age and income might provide a more accurate picture but not if we are using flawed measurements. For example, it is becoming more common to report retirement readiness ratios for plan participants but too often these calculations reflect assumptions about future investment returns that are unreasonably high. This encourages participants to save less and cause them to fall further and further behind while they hope that returns catch up with the projections (which often never happens). Furthermore, typical retirement readiness ratios are not a good indicator of the risk that somebody will not be able to retire because they do not reflect whether the participant has 4 or 40 years to make up any projected funding deficit.

Overloading fiduciaries with even more data is not the way to achieve better outcomes! We need to change our approach from delivering data to delivering actionable insights that address the real issues. For example, the more a participant relies on investment returns to fund their retirement income, the higher the risk of not retiring comfortably. Therefore, instead of making assumptions about what we think they might earn on their investments we should be calculating the Minimum

Required Rate of Return (MR3™) they implicitly would need to earn to achieve a comfortable retirement, given their current saving behavior and social security entitlements. Showing a plan sponsor that 70% of their participants would need to earn more than 15% per annum on their investments for each of the next 20+ years is a real wakeup call that quickly focuses action on how to increase savings.

Safe Outcomes, not Safe Harbor

A safe harbor plan design is the default choice for many plan sponsors. Typically safe harbor designs have a 2-tiered match structure in which the first tier has a dollar-for-dollar match and the second tier matches 50 cents on the dollar. If we think about everything we have learned from behavioral psychology, we know that telling participants “the more you save the less you will get from your employer” is not a good way to encourage higher savings rates.

In addition, for years the industry has been telling participants that they should maximize the employer match and, unfortunately, this message has often been interpreted as “if I maximize the employer match, I will be saving enough for a safe retirement”. Typically a participant needs to be saving 15% of earnings to be on track for a low-risk, secure retirement but safe harbor plans maximize the employer match at deferral rates as low as 5% or 6%. Using a safe harbor plan is therefore most likely to ensure that participants are saving only a fraction of what the need to retire securely – exactly the opposite of improving retirement outcomes.

If plan sponsors really want to help their employees improve retirement outcomes they need to stretch the employer match and ideally use a two-tiered structure with a higher match rate for higher deferrals. As a suggestion, consider matching 30 cents on the dollar for the first 10% of deferrals and a 50 cents match on the next 2% of deferrals. In many cases, highly compensated employees will reach their dollar deferral limit on the first tier but to further help the plan pass its annual testing, the plan rules could restrict the second tier match to the non-highly compensated employees.

Lower Risk not Lower Cost

The fiduciary action of identifying an investment as suitable for a plan should mean that the specific investment has undergone a comprehensive analysis of why it was

the most appropriate for that specific plan. In many cases this will require that advisors [help plan fiduciaries to evaluate and improve their decision making process](#), to ensure that they properly consider all appropriate risk factors and reflect the relative importance of each factor to the specific plan.

For example, lowering the cost of investments is an admirable goal but selecting the lowest cost investment is not always the best choice, particularly if it comes with lower expected returns or higher risk.

It is also important to remember that while investment returns impact participant retirement outcome we cannot invest our way to a safe retirement. The more a participant depends on investment returns to fund their future retirement income needs, the greater their potential risk of not achieving their goal. The most certain way to reduce the risk of not retiring safely is to save more. Automating participant deferrals and optimizing employer contributions to maximize retirement savings are prudent steps that relieve pressure to roll the dice on higher risk investments.

More Common Sense, Less Rocket Science

Financial service providers often try to differentiate themselves through the volume of data and complexity of analysis that they provide. Hopefully this article shows that this is not rocket science and that a little common sense, creativity and flexibility can go a long way to improving retirement outcomes for all employees, all within the employer's existing budget.