

The “Perfect” 401(k) Plan

An actionable strategy informed
by research and focused on results



A white paper prepared by
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TRANSAMERICA CENTER
FOR RETIREMENT STUDIES®

The “Perfect” 401(k) Plan

The Transamerica Center for Retirement Studies® proposes the following definition:

“A ‘perfect’ 401(k) plan helps ensure that workers are participating, contributing and managing investments wisely in order to adequately fund their future retirement and that workers have a strategy for saving, investing and transitioning into retirement.”

Executive Summary

Although 401(k) savings plans are subject to the rules that govern their operation and the annual limits that cap the amounts employees may save, there is a great deal that plan sponsors (and their financial advisors) can do to help create a “perfect” 401(k) plan for the benefit of all participating employees.

This Paper identifies the primary characteristics of an “optimal” 401(k) plan and illustrates survey results that highlight how both employers and workers currently perceive their plans — and identifies where they may not see eye to eye. What’s more, there are several recommendations that plan sponsors, financial advisors and retirement plan providers can put into action now to help improve their 401(k) retirement plans and the overall satisfaction of employees saving in the plans as they travel the path toward retirement readiness.

The “perfect” 401(k) is characterized by the following six key ingredients:

1. *Maximizes employee participation and contribution rates*
2. *Provides and promotes incentives to save (e.g., employer match, tax incentives)*
3. *Educates and empowers employees to make informed decisions about retirement saving, planning and investing*
4. *Underscores the need for workers to have a retirement strategy*
5. *Maximizes plan effectiveness (including investments, education, customer service) and participant satisfaction*
6. *Serves as a highly effective tool for employers to attract and retain employees*

The 12th Annual Transamerica Retirement Survey found a number of opportunities for enhancing the performance of 401(k) plans which, if implemented, could lead to achieving a “perfect” 401(k) plan. For purposes of discussion, survey observations and opportunities are presented in three different sections, including:

- **Saving Enough**
- **Education and Empowerment**
- **Participant Satisfaction**

The good news for plan sponsors is that many of these plan enhancements can be implemented within the context of their existing 401(k) plan infrastructure and do not necessarily need to be costly or require a major investment of human or monetary resources. Plan recordkeeping and service providers often provide an abundance of information, educational tools and other resources — many of which are already included in their standard offering but are often overlooked or underutilized. In addition, much can be done without new legislation or regulatory reform. This gives all plan sponsors the opportunity to implement changes that move their plans closer to the definition of the “perfect” 401(k) plan.

The Elements of Success

Saving Enough

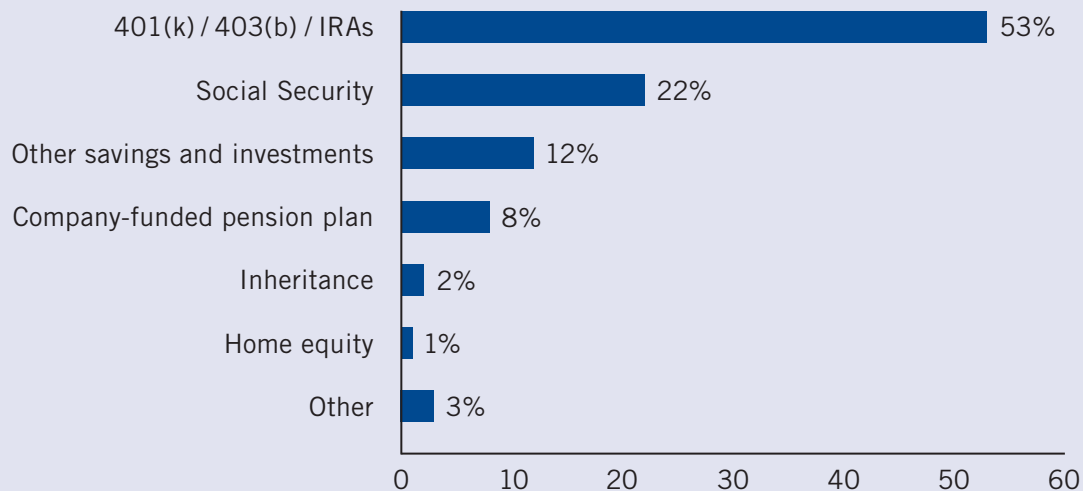
Two elements of the “perfect” 401(k) plan fall into this category:

- Maximizes employee participation and contribution rates, and
- Provides and promotes incentives to save (e.g., employer match, tax incentives).

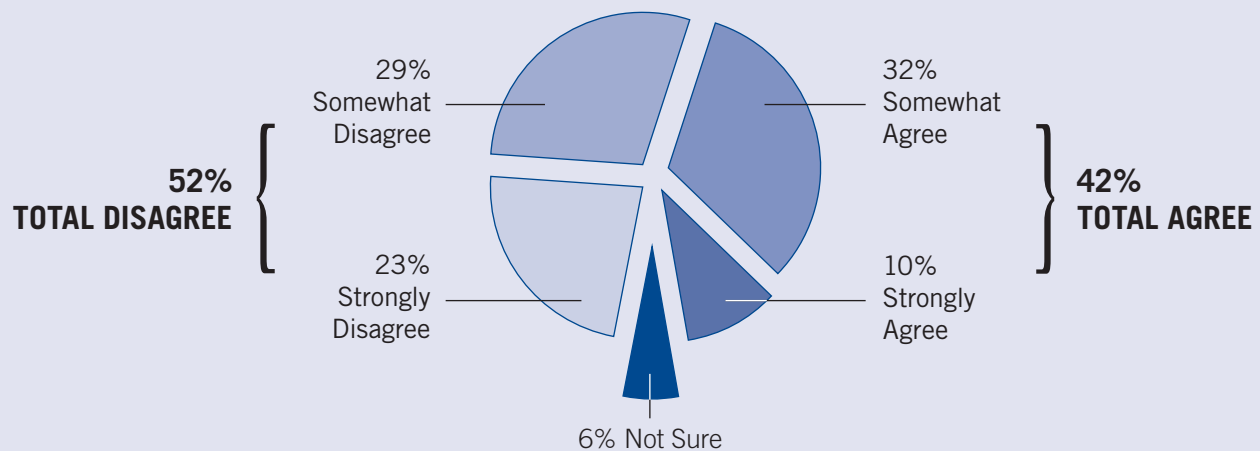
▼ KEY SURVEY FINDINGS

The survey results illustrate why these two elements are so important. While 53% of workers expect to derive the majority of their retirement income from their 401(k), 403(b) and IRA accounts, 52% do not believe they are currently building a large enough nest egg.

Which one of the following do you expect to be your primary source of income to cover your living expenses after you retire?



How much do you agree or disagree that you are currently building a large enough retirement nest egg?



Survey data confirms workers' fears. Using savings-related responses collected in the survey, including a median age of 28 to begin saving, a plan contribution rate of 6% of annual pay, and an expected median retirement age of 65, a worker could likely face a substantial savings shortfall at retirement.

Anatomy of a Savings Shortfall

BASIC ASSUMPTIONS:

- Single
- Current age: 28 years old
- Current savings: \$0
- Annual pay: \$50,000 salary
- Retirement income replacement ratio: 80%
- Annual salary increase: 3%
- Annual inflation rate: 3%
- Participates in 401(k) plan
- 401(k) pre-tax contribution rate: 6% of salary
- Company match: 3%
- Investment growth rate (pre-retirement): 6%
- Investment growth rate (in retirement): 3%
- Retirement age: 65 years old
- Life expectancy: 90 years old

ADDITIONAL ASSUMPTIONS:

- No breaks or gaps in employment
- No early distributions from 401(k)
- No other expected sources of retirement income
- No breaks in savings
- Expectations of receiving Social Security benefits
- No hardship withdrawals

ESTIMATED TARGET RETIREMENT GOAL:

\$ 970,874

LESS: Income from Social Security: **\$ 426,117**

LESS: Projected value of 401(k) savings: **\$ 283,941**

SHORTFALL:

(\$ 260,816)

Workers may mitigate or overcome a potential shortfall by working longer or saving more (or both), but according to the survey, 47% of workers “guessed” at the amount of savings they will need for retirement. Another 26% estimated the amount based on current living expenses. Only 11% used either a worksheet or calculation to determine their retirement savings needs. In addition, just 11% had a written savings strategy.

Workers need specific, personalized tools to determine their savings needs that are easy to access, easy to understand and allow real-time modeling of various saving scenarios. Further, they need a way to document their savings strategies and update them as their personal situations change.

ACTION OPPORTUNITIES

With a better understanding of the challenges that workers face in saving enough for retirement and their potential for a shortfall, action can be taken by plan sponsors, retirement plan providers and by workers themselves to move toward a more “perfect” 401(k) plan.

For Plan Sponsors

Prompt workers to calculate and forecast their retirement savings needs. Emphasize that this exercise should be undertaken periodically as financial and lifestyle factors, as well as retirement plans change over time.

For Retirement Plan Providers

Enhance retirement plan websites to present participants' retirement forecast to them when they log on — and enable them to model and implement changes to improve their forecast. Provide retirement income projections, at least annually, on 401(k) account statements.

For Workers

Create a retirement strategy and begin saving and investing consistently. Incorporate retirement income planning into that strategy.

Education & Empowerment

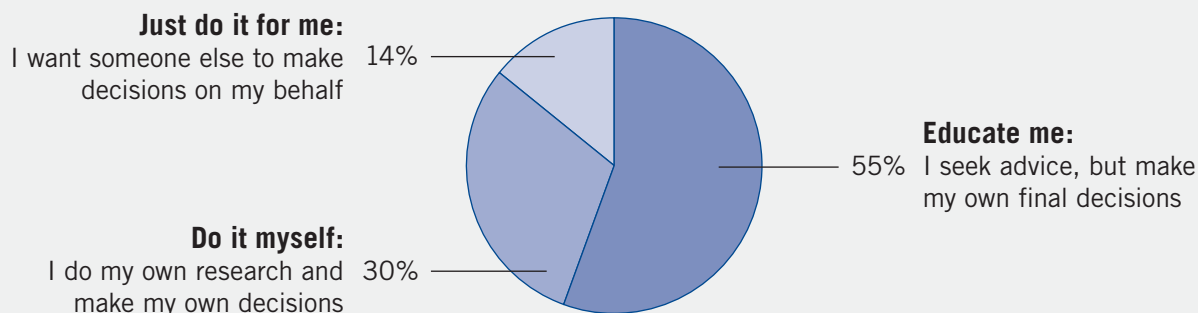
The “perfect” 401(k) plan incorporates the following two elements related to employee education:

- Educates and empowers employees to make informed decisions about retirement saving, planning and investing, and
- Underscores the need for workers to have a retirement strategy.

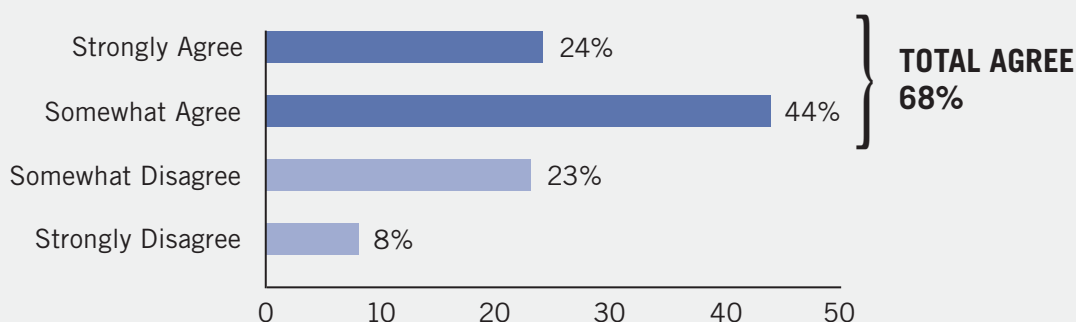
▼ KEY SURVEY FINDINGS

Most workers prefer to make decisions regarding their retirement savings, and the majority seeks advice. However, two-thirds of workers agree that they don't know as much as they should about retirement investing.

How would you describe yourself when it comes to saving and investing for retirement?



I do not know as much as I should about retirement investing:

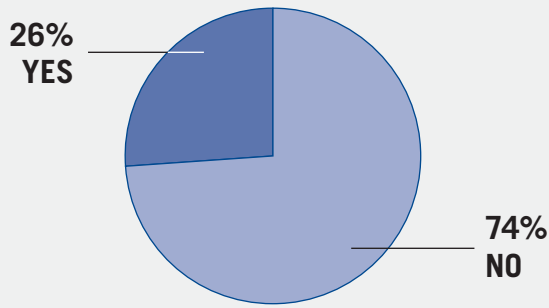


When asked what would help motivate them to learn more about retirement saving and investing, the three items topping the list were:

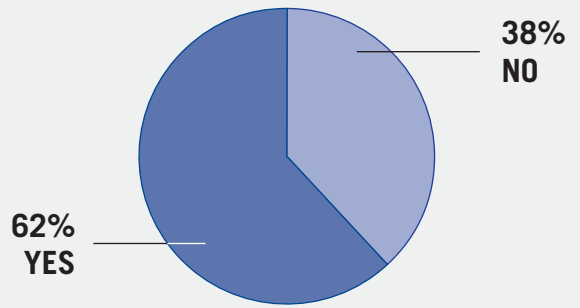
- Tax breaks and other savings incentives (47%)
- Easy-to-understand educational materials (37%)
- Easy-to-understand starting point (36%)

Interestingly enough, while “tax breaks and other savings incentives” was the number one response, the survey also showed that many workers were unaware of two common tax incentives available to every 401(k) plan participant who qualifies — The Saver’s Credit and Catch-Up Contributions.

Are you aware of a tax credit called a "Saver's Credit"?



Are you aware that people age 50 and older may be allowed to make Catch-Up Contributions to their 401(k)/403(b)/457(b) plan or IRA?



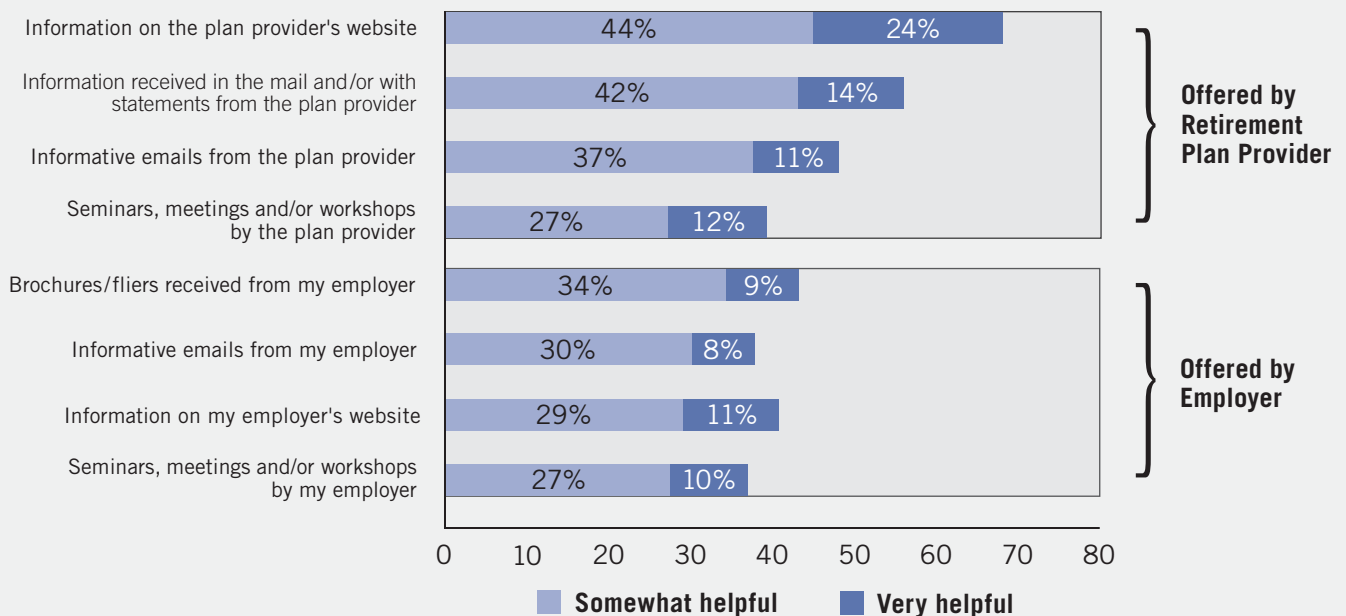
Furthermore, while most workers (69%) knew about the Roth 401(k) option, more than half (52%) indicated it was not available to them in their plans. Of workers who did not currently have a Roth component in their plans, 41% indicated they would like to have this feature available to them.

Some of the most intriguing findings in the study related to employee education. While plan sponsors and retirement plan service providers continually strive to provide educational information on a range of topics and in a variety of formats (in-person meetings, print brochures, website content), and try to make the information easy to understand, 401(k) education materials are not as effective as they could or should be with the intended audience. The biggest reason?

Employee education needs to be easier to understand and offer workers a simple starting point to begin learning about the plan.

Despite the need for more easily understandable information, the survey shows that workers have distinct preferences regarding the sources and methods for accessing information. Across the board, workers found information from their retirement plan providers to be more helpful than what is offered by their employers. Workers also found many items to be "somewhat helpful," but few to be "very helpful." With respect to the method of delivering education, workers overwhelmingly named the retirement plan provider's website as the most helpful in assisting with planning, saving and investing for retirement.

How helpful do you find the following in assisting you to plan, save and invest for retirement?



ACTION OPPORTUNITIES

Armed with this information, plan sponsors and retirement plan providers can take immediate, concrete action to make employee education more understandable for employees and to capitalize on demonstrated worker preferences for certain education sources and delivery methods.

For Plan Sponsors and Retirement Plan Providers

- Reevaluate educational offerings to ensure that they are reaching the widest possible audience and that they are both easy to understand and helpful.
- Promote and increase worker awareness of existing tax incentives including The Saver’s Credit and Catch-Up Contributions.
- For those offering the Roth 401(k) feature, promote and increase awareness. For those not offering the Roth 401(k) feature, consider adopting it.

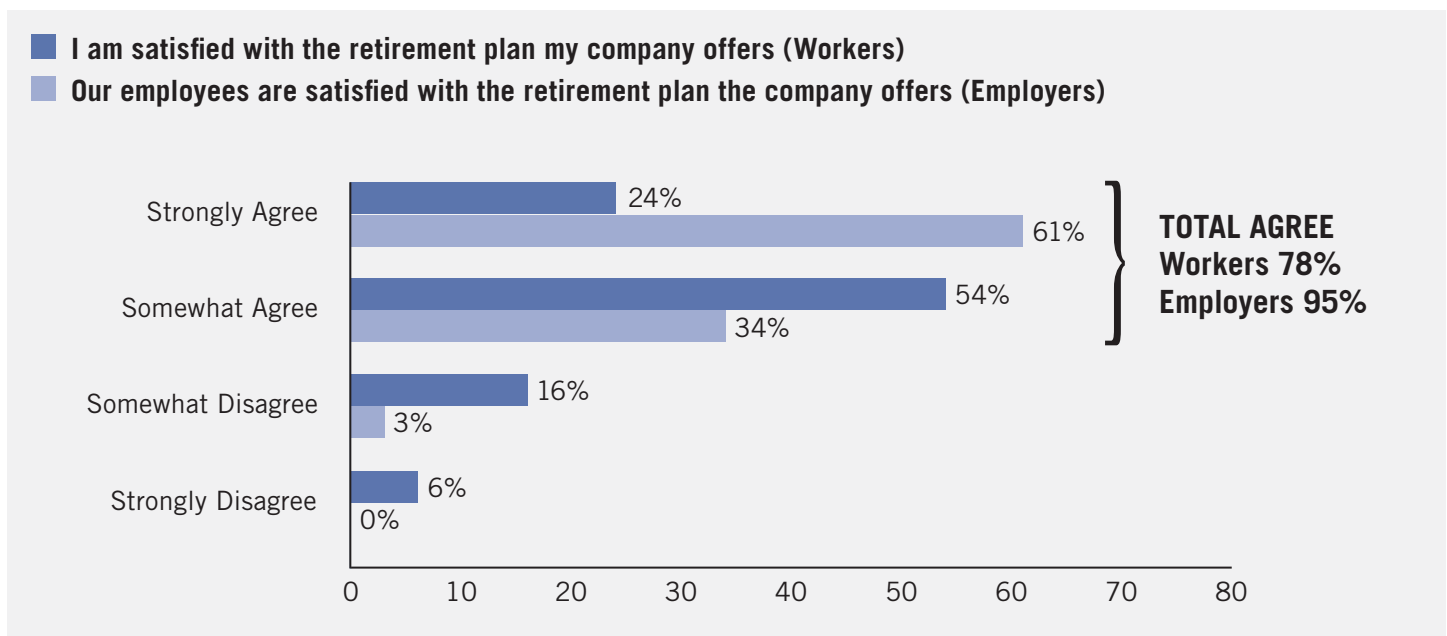
Participant Satisfaction

The final two elements of the “perfect” 401(k) plan are:

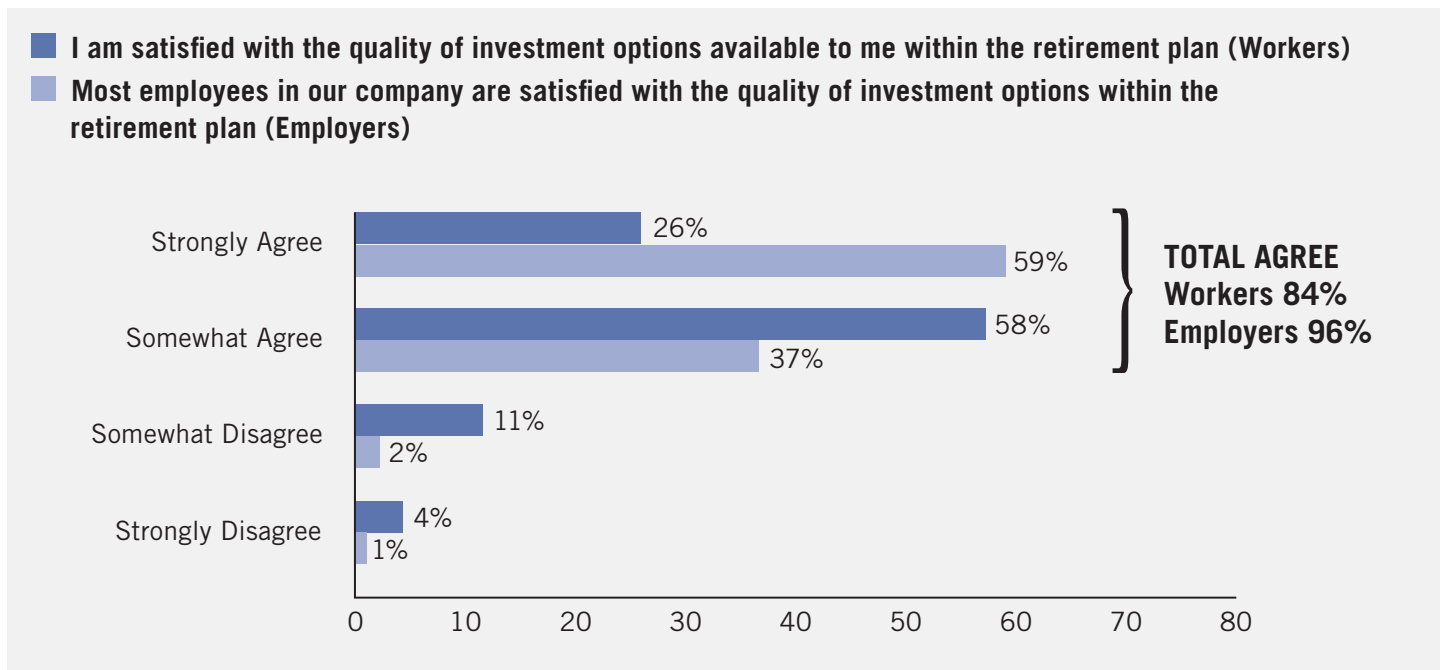
- Maximizes plan effectiveness (including investments, education, customer service) and participant satisfaction, and
- Serves as a highly effective tool for employers to attract and retain employees.

▼ KEY SURVEY FINDINGS

When it comes to participant satisfaction, there is a substantial difference between what plan sponsors perceive and what workers actually believe. Plan sponsors tend to overestimate worker satisfaction with the overall plan, the quality of the investment menu, and the availability of the “right” information to make decisions about the plan. Conversely, sponsors underestimate their employees’ desire to receive more information and advice on how to achieve their retirement goals.



A full 96% of employers believe their employees are satisfied with the quality of the plan investments offered. Only 84% of workers agree.



The majority of employers (95%) believe they “give the right information to help their employees make decisions about the retirement plan.” Just 26% of workers “strongly agreed.” Another 53% “somewhat agreed.” When asked whether they would like to receive more information and advice from their companies on how

to reach their retirement goals, three out of five (61%) workers agreed. Just 43% of employers perceived this as a worker need.

While the perceived differences may be somewhat surprising, they also present opportunities for improvement.

ACTION OPPORTUNITIES

The main take-away from the survey results in this section is that more communication is needed between employers and workers on retirement plan issues. Specific action steps need not be costly or onerous and will likely prove extremely valuable and worthwhile.

For Plan Sponsors and Retirement Plan Providers

- Create an ongoing dialogue with workers regarding their retirement benefits.
- Conduct a survey of eligible employees (including plan participants and non-participants) on their levels of satisfaction with all aspects of the plan (e.g., overall satisfaction, investments, education, disclosures, etc.) to identify strengths and areas for improvement.
- Use your employee survey findings and dialogue feedback to evaluate the plan’s performance and implement improvements.

Conclusion and Recommendations

The 12th Annual Transamerica Retirement Survey found a number of opportunities for enhancing the performance of 401(k) plans, thereby leading plan sponsors closer to the definition of a “perfect” 401(k) plan. It is important to note, especially for employers with limited resources, that most of these opportunities are not costly, nor do they require legislative or regulatory reform. Specific recommendations suggested by the Survey include:

Saving Enough

- Motivate employees to calculate a savings goal, conduct a gap analysis, and formulate and document a retirement savings strategy.

Education and Empowerment

- Evaluate educational offerings to provide employees with a good, manageable starting point from which to begin educating themselves and actively managing their accounts.
- Provide educational materials that are easy to understand.
- Take advantage of the sources of information and the delivery methods that resonate most with employees and that they use the most, like Web-based information from retirement plan providers.
- Focus on promoting existing tax incentives such as The Saver’s Credit and Catch-Up Contributions that the Survey showed to be motivators for employees to learn more about retirement savings and investing.

Participant Satisfaction

- Consider adopting additional plan features that are available and meaningful to employees (e.g., Roth 401(k)).
- Survey employees (including plan participants and non-participants) to gauge levels of satisfaction on all aspects of the plan (e.g., plan features, investments, education, etc.) and identify strengths and opportunities for improvement.

Anyone with retirement plan experience knows that the “perfect” 401(k) may not be attainable in an absolute sense. But in a very real sense, the “perfect” 401(k) is achievable through a combination of plan features, effective employee education, and ongoing employer/employee communication that focuses on six key ingredients that characterize the perfect plan and results in increased participant savings rates, education and empowerment, and plan satisfaction.

About the 12th Annual Retirement Savings Surveys

Since 1999, the Transamerica Center for Retirement Studies® has conducted a national survey of U.S. business employers and workers regarding their attitudes toward retirement. The overall goals for the study are to illuminate emerging trends, promote awareness, and help educate the public.

Harris Interactive was commissioned to conduct the 12th Annual Retirement Surveys for Transamerica Center for Retirement Studies®. Transamerica Center for Retirement Studies® is not affiliated with Harris Interactive.

Worker

A 25-minute, online survey was conducted between January 31, 2011 and March 10, 2011 among a nationally representative sample of 4,080 for-profit workers using the Harris Interactive online panel. Respondents met the following criteria:

- All U.S. residents, age 18 or older, and
- Full-time workers or part-time workers in a for-profit company employing 10 or more people.

Data were weighted:

- To account for differences between the population available via the Internet versus by telephone,
- To ensure that each quota group had a representative sample based on the number of employees at companies in each employee size range, and
- Percentages were rounded to the nearest whole percent; differences in the sums of combined categories/answers are due to rounding.

All results presented here are for the 2,973 workers surveyed whose employers offer an employee-funded retirement plan (e.g., 401(k) SIMPLE or SEP).

Employer

A 17-minute telephone survey was conducted among a nationally representative sample of 743 employers between January 28, 2011 and February 25, 2011. Potential respondents were targeted based on job title at for-profit companies and met the following criteria:

- Business executives who make decisions about employee benefits at his or her company, and
- Businesses that employ 10 employees or more across all locations.

Quotas were set for large and small companies and results were weighted as needed on employee size using weighting targets from the Dun & Bradstreet database to ensure each quota group had a representative sample based on the number of companies in each employee size range.

About the Center

The Transamerica Center for Retirement Studies® (The Center) is a non-profit, private foundation dedicated to educating the public on emerging trends surrounding retirement security in the United States. The Center's research emphasizes employer-sponsored retirement plans, issues faced by small to mid-sized companies and their employees, and the implications of legislative and regulatory changes.

The Center is funded by contributions from Transamerica Life Insurance Company and its affiliates and may receive funds from unaffiliated third-parties. For more information about The Center, please refer to www.transamericacenter.org.

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About the Author

Catherine Collinson serves as President of the Transamerica Center for Retirement Studies® and is a retirement and market trends expert. She directs the Transamerica Annual Retirement Survey, which has been referenced in publications such as The Wall Street Journal, USA Today and Money magazine.



With over a decade of experience in retirement services, Ms. Collinson has become a recognized voice on retirement trends for the industry and in Washington, D.C. She is quoted regularly in the media and her commentary appears in top outlets such as The New York Times, Dallas Morning News, The Baltimore Sun, CNN Radio, Employee Benefits News and National Underwriter.

In addition to serving as President of the not-for-profit Transamerica Center for Retirement Studies®, Collinson is Senior Vice President of Strategic Planning at Transamerica Retirement Services Corporation. In this post, she is responsible for developing and implementing short- and long-term strategic business plans. She has been instrumental in developing business plans and building infrastructure to support the company's high-growth 401(k) market strategy. Collinson joined Transamerica Retirement Services Corporation in 1995, and has since held a variety of positions on both the marketing and operations sides of the company.

Prior to joining Transamerica, Collinson spent nearly a decade at The Walt Disney Company, serving in a number of information services and business planning positions with the corporate office, Euro Disney and Disneyland.

Collinson earned her bachelor's degree in British and American literature at Scripps College, Claremont, CA and her master's of business administration from the University of California, Irvine. She volunteers at a number of community organizations and is a member of the Board of Trustees for the California Science Center Foundation. She is also a member of the Scripps College Alumni Association.

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The 12th Annual Transamerica Retirement Survey,
plus a wide variety of additional retirement plan research information, can be found on
The Transamerica Center for Retirement Studies® website at www.transamericacenter.org.