There has been a lot of talk in the media recently about retirement insecurity. For a while now, reporters have been talking about how pensions are “disappearing” and being replaced by 401(k) plans. Then, with the recent economic downturn, many Americans’ retirement savings accounts took a big hit.

You may wonder what this means for your retirement security. The good news is, for those who have earned the guaranteed lifetime benefits provided by group pension plans, you are in a far better position to weather the tough economic storms that come your way.

According to calculations by researchers at Boston College and at NIRS, the retirement savings gap – the difference between what American households will need to save for retirement and what they are on course to save – is almost $7 trillion based on household net wealth, including appreciated housing values. American workers are therefore right to be anxious about their retirement security in the current economic environment. And only a mere 2% of Americans believe that it will be easier to prepare for retirement in the future.¹

Older low- to middle-income workers, in particular, are facing a daunting financial challenge recovering from the Great Recession while preparing for retirement. Indeed, 37 percent of the middle-income workers age 45–54 are projected to be downwardly mobile to lower income status in retirement, based on a study by the Urban Institute.² All told, 9 out of ten workers fall short of target retirement savings.
benchmarks designed to allow older Americans to maintain their standard of living prior to reaching typical retirement ages.³

There are several reasons for this increase in retirement insecurity in America beyond the economic downturn. First, roughly 78 million American workers (both public and private) have no access to any retirement plan at work—the most effective way to save for retirement. Few of these individuals save for retirement on their own, and many will retire, with less than enough money to meet their basic needs.

Moreover, in the private sector, and over the last few decades, many companies who do offer retirement plans have been getting rid of their group pension plans and replacing them with individual savings plans, like 401(k) plans.⁴ Individual savings plans, like 401(k)s, were not originally intended to serve as the primary source of retirement income for individuals. These plans started out as supplements to group pension plans—and are still very effective as such—but are more suited to provide the additional income that may be needed for retirement, or to deal with extraordinary life events—like an unexpected health crisis, the loss of a spouse, etc.

The typical working-age household has only $3,000 saved in retirement accounts, while the typical near-retirement age working household has just $12,000 saved.⁵ To put this amount of retirement savings into context, even the near-retiree savings amount is less than the modest average annual Social Security benefit earned by retired Americans of $15,190.

Due to the above factors, as well as stagnating income, escalating personal debt and rising costs for education and health care, workers today are less likely than their parents or grandparents to enjoy the living standards of their working years when they retire. If these trends continue, Social Security (for those who participate in the program) will be the main source of income for all but retirees in the top one quarter of retiree income levels.

The Best Way to Achieve Retirement Security

Retirement researchers have long acknowledged the importance of Social Security benefits, defined benefit (DB) pension income, and supplemental individual savings—in providing Americans the greatest opportunity to achieve financial security in retirement.⁶

Each leg of this stool fills a specific, unique purpose.

Social Security provides a guaranteed, cost-of-living adjusted income for life in retirement, and has proven to be an effective way to keep older Americans out of poverty.⁷ It is the foundation of retirement security for millions of Americans and their families.

Yet Social Security was never meant to be the sole source of retirement income for American workers. And, in fact, as many as 30% of state and local government employees do not participate in Social Security at all.⁸ The second component—group pension plans—is also extremely important in providing a reliable, steady source of income in
retirement. And for those retirees without Social Security, a pension may represent their only source of guaranteed, inflation-adjusted monthly income, making their pension all the more important.

The final leg of the retirement stool consists of individual savings. You might save for retirement at work in a defined contribution (DC) plan—a 401(k), 403(b), or 457 plan, for example. You might also save in an individual retirement account (IRA), or have other savings. Having individual savings on top of your pension and Social Security is a helpful way to ensure financial security, especially if you experience hardships that may be hard to predict, for example, long-term care costs for yourself or a loved one.

Pensions Provide Guaranteed, Monthly Income for Life

Pensions are fundamentally different from savings because you cannot outlive the guaranteed monthly income provided by your pension. No matter how long you may live, you can be sure that your pension check will continue to come every month. Savings, on the other hand, can run out.

Also, your pension may provide other benefits as well, such as COLAs, disability protections, and benefits for your spouse, should you die first.9 Each of these characteristics is what makes your pension so unique and so different from defined contribution plans.

<table>
<thead>
<tr>
<th>Defined Benefit Plan (Traditional Pension)</th>
<th>Defined Contribution Plan (401(k)s, 403(b)s, 457s)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Contributions</strong></td>
<td>Employees make their own contributions to their savings account at whatever rate they choose. Often, employers will make a certain match—for example, 50 cents on the dollar up to 6% of pay—but they are not required to contribute at all.</td>
</tr>
<tr>
<td><strong>Investments</strong></td>
<td>Employees usually make all investment decisions for themselves. They can choose from a range of investment options offered by the plan.</td>
</tr>
<tr>
<td><strong>Amount of Money in Retirement</strong></td>
<td>The money available in retirement is simply the amount that one has accumulated in the savings plan, through contributions and investment earnings.</td>
</tr>
</tbody>
</table>

9 Each of these characteristics is what makes your pension so unique and so different from defined contribution plans.
Another key feature of group pension plans is their pooled nature—meaning that all of the pension contributions for all workers are put together in the same pot. This pooled nature is important because it makes pension plans a good value for the money. By pooling and professionally managing assets, pensions are able to achieve “economies of scale.” (This is the same reason why shopping at a warehouse club saves consumers money—buying in bulk lowers the price.) Research has found that a group pension can achieve a target retirement benefit at about half the cost of individual retirement accounts.

So not only do group pensions do the retirement job more effectively than individual savings plans, but they’re also a lot less expensive to boot—a fact that policymakers and taxpayers alike can take solace in.
Group pension plans are also likely to benefit local businesses in your town. This is because when you receive your pension check, you probably don’t stuff it under your mattress—you spend it in your local economy. And the business where you make that purchase sees a boost in its profits. This means that they may be able to expand their business or even hire more workers.

This simple act of you spending your pension income has very large economic effects. In 2009, expenditures made out of public pension payments supported more than 6.5 million new American jobs and over $1 trillion in total economic output nationwide. Those are some huge economic impacts!

So, pensions do a great job of providing modest, secure retirement benefits—and they remain quite popular among Americans. Public pensions make sense for taxpayers, too, because they are still a good deal. As if that weren’t enough, pensions also help boost the economy. It’s a classic “win-win” situation for employees, employers, taxpayers, and local business owners.

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4 It is important to remember that, despite the trend to 401(k)s, public sector workers are not the only Americans who have defined benefit pension plans. In fact, there are still about 3.3 million more private sector workers with a pension than public sector workers with a pension.
5 Rhee, op cit.