NRTA PENSION EDUCATION TOOLKIT

The Importance of Your Pension

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.

The Current State of Retirement Security in America

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

Your pension plan is important because…

- The traditional three-legged stool—of a pension, Social Security, and individual savings—is still the best way to achieve retirement security. Social Security provides a basic benefit, but your pension helps you to maintain your standard of living in retirement, and savings provides important supplemental income for unforeseen expenses.
- Group pension plans provide guaranteed, monthly income for life, which makes financial security in retirement much more achievable for those who have them.
- Not surprisingly, almost all Americans still want pensions.
- Pensions are an economically efficient way to fund retirement, which means they are a prudent use of taxpayer money.
- Pensions also help to boost local economies, especially in tough economic times.

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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.

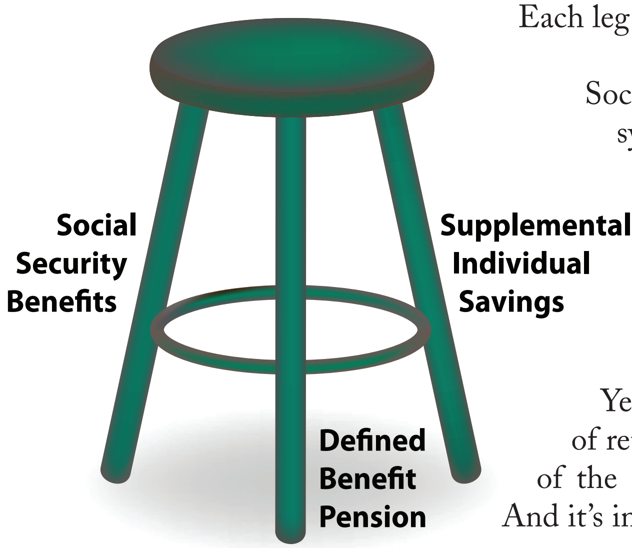
Moreover, in the private sector, and over the last few decades, many companies who do offer retirement plans have been getting rid of their group pension plans and replacing them with individual savings plans, like 401(k) plans.[4] Individual savings plans, like 401(k)s, were not originally intended 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 the so-called "three-legged" stool—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 is our (near) universal social insurance system, administered by the Federal government. It provides a guaranteed, cost-of-living adjusted income for life in retirement and is the foundation of retirement security for millions of Americans and their families. Social Security has also been a very effective way to keep older Americans out of poverty.[7]

Yet Social Security was never meant to be the sole source of retirement income for American workers. The second leg of the stool—group pension plans—are also very important. And it's important to remember that about 30% of state and local government employees do not participate in the Social Security system.[8] So a pension may represent that retired household's only source of guaranteed, inflation-adjusted monthly income.

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.

	Defined Benefit Plan (Traditional Pension)	**Defined Contribution Plan** (401(k)s, 403(b)s, 457s)
Contributions	In the public and private sectors, contributions are made on behalf of each employee by the employer. In the public sector, many pensions are "contributory," meaning that employees also contribute to the plan out of their own paychecks.	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.
Investments	Contributions for all employees are pooled, and invested by professional asset managers in a range of assets—stocks, bonds, real estate, etc.	Employees usually make all investment decisions themselves. They can choose from a range of investment options offered by the plan.
Amount of Money in Retirement	The monthly benefit is determined by a set calculation—usually based on years of service and pay at the end of one's career.	The money available in retirement is simply the amount that one has accumulated in the savings plan, through contributions and investment earnings.

Payout in Retirement	Payouts are typically provided as a monthly income stream that is guaranteed for the remainder of the retiree's life.	Plans are not required to offer a lifetime income payout. Payout is often a one-time, lump sum payment.
Supplemental Benefits	Spousal protections, disability benefits, and cost of living adjustments are common.	Supplemental benefits are not applicable.

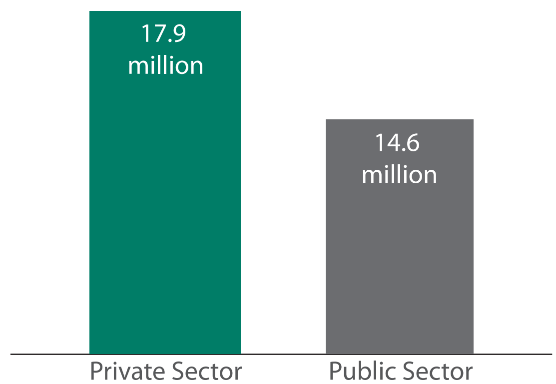
Americans Want Pensions

It is important to note that many Americans do realize just how important pensions are. With the trend away from pensions in the private sector, it seems more and more Americans are anxious about retirement—and are in favor of having a pension.

Recent public opinion research has found…
• More than eight out of ten Americans are worried about their ability to retire.
• 80% believe that the decline of pensions has made it more difficult to achieve the American Dream.
• More than eight in ten Americans would participate in a "new" pension system, if offered.
• 82% of Americans believe that all workers should have a pension plan.[9]

So, it's not just that middle-class Americans *need* pensions. It seems most Americans *want* pensions, too.[11]

Active U.S. Workers with a Group Pension Plan, in millions 2009[10]



Pensions Are an Efficient Use of Taxpayer Funds

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.[12]

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.

Pensions Boost Local Economies

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.[13] 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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[1] Oakley, D., and K. Kenneally. Pensions and Retirement Security 2013: A Roadmap for Policy Makers. Washington, DC: National Institute on Retirement Security.

[2] Butrica, B., and M.Waid. 2013. What Are the Retirement Prospects of Middle-Class Americans? AARP Public Policy Institute Research Report. Washington, DC: AARP.

[3] Rhee, N. 2013. The Retirement Savings Crisis: Is It Worse Than We Think? Washington, DC: National Institute on Retirement Security.

[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.

[6] Munnell, A.H., Soto, M., Webb, A., Golub-Sass, F., and Muldoon, D. 2008. *Health Care Costs Drive up the National Retirement Risk Index.* Issue in Brief No. 8-3. Chestnut Hill, MA: Center for Retirement Research at Boston College. and Munnell, A.H., Webb, A., and Golub-Sass, F. 2007. *Is There Really a Retirement Savings Crisis? An NRRI Analysis*. Issue in Brief No. 7-11 Chestnut Hill, MA: Center for Retirement Research at Boston College.

[7] Engelhardt, C.F., and Gruber, J. 2004. *Social Security and the Evolution of Elderly Poverty*. Working Paper 10466. Cambridge, MA: National Bureau of Economic Research.

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[9] Almeida, B. 2008. *Retirement Readiness: What Difference Does a Pension Make?* Washington, DC: National Institute on Retirement Security.

[10] Pension Benefit Guaranty Corporation. 2012. *PBGC 2010 Databook*. Washington, DC: PBGC. and U.S. Census Bureau. 2013. State and Local Government Employee-Retirement Systems. Washington, DC: U.S. Census Bureau.

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[12] Almeida, B., and Fornia, W. 2008. A Better Bang for the Buck: The Economic Efficiencies of Defined Benefit Pension Plans. Washington, DC: The National Institute on Retirement Security.

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