The DC plan proposition: Retirement readiness

Greater responsibility for funding retirement is shifting to the individual worker as U.S. employers continue to close or freeze their traditional defined benefit (DB) plans and replace them with defined contribution (DC) programs. Companies have plans in place that enable employees to build up tax-advantaged savings. But competing financial demands are leaving many workers far behind in preparing for retirement, prompting many employees to plan to delay, or actually delay, leaving the workforce. Workers who delay retirement are at financial risk, bring stress to the workplace and are more costly to employers.

DC plans have evolved so that they offer workers many options for saving and investing, and provide sponsors with a range of tools to help employees get started and to encourage them along the way. But many sponsors evaluate their employees' progress by relying on snapshots of plan-wide aggregate data. This offers little insight to help understand and improve their workers' retirement readiness, or to measure sponsors' return on the considerable capital they devote to their plans.

Sponsors can strengthen their plan governance and improve their plans' return on investment by using detailed analytics that evaluate specific segments of their employee population based on age, job category, tenure and benefit structure. The right analytics highlight those employees and groups most at risk, and allow sponsors to determine which participant tools and strategies best prepare employees for retirement.

A shared retirement savings problem

Even though many workers are now responsible for funding much of their own retirement through employer-sponsored 401(k) programs, many are also not saving enough. The savings shortage is epidemic: Irrespective of age or income level, employees' savings rates and the accumulation of retirement assets simply are not adequate to fulfill income needs during retirement.

In 2015, the median 401(k) balance for participants in their 60s earning $60,000 to $80,000 was approximately $150,000.[1] Many employees may have other sources of retirement income, but as a sole funding source, such low 401(k) balances are unlikely to take employees very far in retirement, even at spending levels sharply reduced from their working years. Accordingly, the Center for Retirement Research at Boston College estimates that as of 2016, 51% of U.S. households (and even 41% of high-income households) covered only by DC plans will be at risk of not being able to maintain their standard of living in retirement.[2]

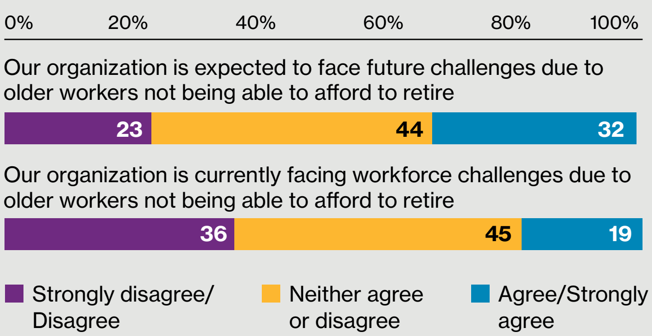
The problem is not a lack of awareness: In Willis Towers Watson's 2017 Global Benefits Attitudes Survey, 68% of workers reported that retirement security is a top-of-mind issue, up sharply from 46% in 2013. Rather, they are just not saving enough – despite their own good intentions, and the efforts and investment of employers in plan design features such as automatic enrollment, automatic escalation and matching contributions.

[1]Jack VanDerhei et al., "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2015," *Employee Benefit Research Institute Issue Brief*, August 3, 2017, page 20, Figure 17

[2]Alicia Munnell, Wenliang Hou, and Geoffrey Sanzenbacher, "National Retirement Risk Index Shows Modest Improvement in 2016," Center for Retirement Research at Boston College, *Working Paper 18-1,* January 2018

The financial stress workers face is forcing many to postpone retirement: About half of those age 50 and older plan to continue to work past typical retirement age.[3] Granted, some employers may benefit from retaining older workers' experience and skill levels, but adverse selection often prevails, so that over half of those expecting to delay retirement come to the workplace with a burden of fair-to-poor health, are highly stressed and disengaged. This, in turn, creates substantial risks for employers. In Willis Towers Watson's 2017 U.S. Defined Contribution Plan Sponsor Survey of 349 large plan sponsors, 32% anticipate future workforce challenges from workers' inability to a take a timely retirement *(Figure 1).*

Figure 1. **Current workforce challenges are an issue, but future worries loom**



Source: 2017 U.S. Willis Towers Watson Defined Contribution Plan Sponsor Survey

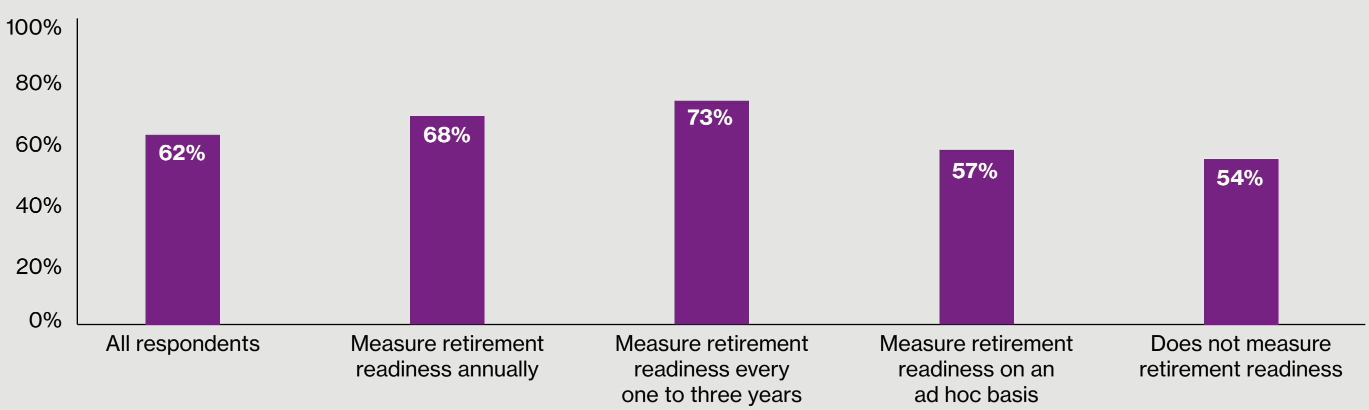
The role of DC plan sponsors

As DC plans increasingly become the primary source of retirement income for many U.S. workers, plan sponsors need to ensure that their DC plans align with the organization's philosophy toward retirement readiness – that is, encouraging employees to save enough during their working years and ensuring an orderly succession in the workforce.

Despite the shift to a more DC-centric world, we have found investment governance structures and processes slow to adapt. As the first generation of workers to rely heavily on retirement savings from DC plans reaches retirement age, it's increasingly clear that committees' current approaches to plan governance may not yield the best outcomes for participants. With more employees falling short of their retirement goals, there is a growing realization among plan sponsors that they need a more proactive and forward-looking approach to managing their DC plans.

Although 83% of plan sponsors in Willis Towers Watson's 2017 DC sponsor survey cited retirement readiness as a top priority, their efforts don't yet reflect that concern: Only 17% allocate time to discussing retirement readiness during committee meetings, noting that greater attention still goes to evaluation of investment managers and monitoring fund performance. Only a third of DC plan committees analyze retirement readiness annually, and fewer than half assess readiness at least every three years. However, most plan to expand their efforts in the near future *(Figure 2).*

Figure 2. **Most plan to step up efforts to measure retirement readiness**



Source: 2017 U.S. Willis Towers Watson Defined Contribution Plan Sponsor Survey

[3]Willis Towers Watson, 2013/2014 Global Benefits Attitudes Survey

To adequately address these challenges, DC plan committees must evolve. Increasingly, we see either separate investment and administrative committees or existing charters expanding beyond a narrow fiduciary role to include plan design and other settlor decisions. Correspondingly, the composition of DC plan committees is starting to change. In Willis Towers Watson's 2016 governance survey, a majority of respondents indicated that their chief human resources officer, chief financial officer and treasurer sit on their committees. In addition, about 50% of respondents indicated that committee members' responsibilities extend beyond investments.

Replacing assumptions with analytics

Insufficient attention to retirement readiness may be compounded by a lack of information useful in setting objectives for improvement. We believe plan-wide statistics on mean or median participation rates, balances or contribution rates measure aggregate data on all participants but offer little in the way of insight into retirement adequacy and meaningful benchmarks for individuals or segments of the population. For example, an average balance measured across a plan at a point in time offers little insight on an individual who waited until age 45 to start saving. Unfortunately, 88% of the sponsors in our 2017 survey said they rely on such aggregates. But without properly informed analysis, sponsors may not have accurate insight into the retirement readiness of their employees or the associated workforce risk.

With targeted analytics, we feel sponsors can construct a baseline assessment of their plans with views of the population on age, occupation, location, union membership and compensation to identify individuals or groups that might not be adequately prepared. A similar detailed analysis can be carried out to measure the effectiveness of plan design across the participant base from insights on use of features such as automatic enrollment, automatic escalation, Roth 401(k) and loans. Understanding overall retirement readiness is also enhanced by a look at participation in health care savings accounts.

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Armed with well-informed analytics, we believe sponsors can develop objectives and an overall plan strategy that foster retirement readiness in two key ways. The first considers those steps the sponsors take on their own through plan design to establish participation, saving and investment. The second looks at the tactics used to motivate participants to take meaningful financial action, including improving behaviors to increase savings, tax efficiency, investing and spending. Plan sponsors can develop tangible goals and scorecards, and track progress going forward, developing more effective governance and achieving retirement readiness.

For example, a detailed and informed assessment may point to the effectiveness of several different tactics: (1) initiating a reenrollment to capture those employees not participating, (2) moving those enrolled but not saving enough to a new default level, (3) implementing a higher automatic enrollment default rate, (4) stretching the company match to encourage participants to defer more, or (5) reenrolling all participants into target date funds to improve asset allocation.

Further potential benefits of advanced analytics

With the proper analytics, plan sponsors gain not only better-informed answers to retirement questions, but also a better understanding of the broader financial wellbeing for all segments of the participant audience. They can then target employees' needs and develop customized plans and communication strategies to engage employees in positive behaviors. Solutions to most effectively improve the financial wellbeing of a 30-year-old cohort, for instance, will likely differ from those to best motivate workers in their 50s.

Detailed analytics can be paired with plan technology to drive positive employee behavior. In one large hospital system, embedding Willis Towers Watson's myFiTage portal within communication campaigns increased employees' use of other financial wellness tools and sessions with financial counselors, and realized greater retirement savings and improved financial behavior. Five years after its introduction, one-third of the group's participants access the myFiTage portal. And among those at financial risk, FiT Age scores (financial independence target age) improved by an average of two years.

At a large telecommunications company, low- and mid-level salaried workers were not deferring enough in 401(k) contributions to receive the full employer match. The employer offered an incentive for using the portal. Among users who hadn't maximized the employer match, 23% responded with the necessary increase in saving. And in just over a year, users reduced their FiT Age scores, on average, by a full year.*

"We've frozen our DB plan. Is our DC plan keeping up?"

This question, posed by a company's CEO or board of directors, is one that plan sponsors should be prepared to answer: In retirement, most U.S. workers will rely increasingly – for some, exclusively – on their DC plan savings, but statistics suggest that savings levels are significantly below what many people need to adequately fund retirement. A fortunate few among retiring workers may fall back on legacy DB benefits, but in the bigger picture many will still experience a shortfall.

We believe adding an analytics component is essential to DC plan governance. Without detailed information on retirement income gaps and engagement with the plan for participant segments, sponsors lack a full perspective on retirement readiness and broader financial wellbeing. The alternative, relying on rule-of-thumb aggregate plan statistics, leads to uninformed readings on the effectiveness of sponsors' actions, and will not provide solid guidance for management into the future.

Willis Towers Watson's FiT Age[SM]

Financial independence target age (FiT Age) is the projected date when a participant's retirement resources meet retirement lifestyle needs.

FiT Age is a single number calculated with a personal meaning that reflects taxes, active and retiree health care costs, and longevity needs. Its power is in its simplicity and ability to motivate positive employee behavior change.

For employees, the myFiTage portal goes beyond generic messaging, applying analytics to each individual's situation to coach and nudge. It accounts for employee behavior, and progress toward retirement readiness and broader financial wellness.

For employers, FiT Age analytics aggregate individual profiles into a concise view of financial wellbeing and retirement readiness for the workforce as a whole – revealing which employees are on track, which are at risk for a delayed retirement and how the plan is prepared to support them.

Organizations make significant investments in their retirement programs and need to ensure that the money is well spent – for the sake of both their shareholders and employees. Analytics can help define the issues and identify those tactics that make a meaningful difference. Retirement readiness may depend on adequate savings over the long run, but even for today's youngest workers, the future is closer than it seems.

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