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The Future of Retirement and the Strengths of the 401(k) System

By Paul Schott Stevens

What is the future of retirement? In remarks today to Town Hall Los Angeles, I made the case that the 401(k) system will play a crucial role in building that future. Surveying the long and quite colorful history of pension systems, I discussed the strengths of the defined contribution (DC) approach of 401(k) plans. In this model, a retiree's ultimate benefits are not determined by a formula set by the employer, but by the savings and investment earnings accumulated during a worker's career. Three critical advantages of this model are portability, ownership, and innovation.

- **Portability**: Americans are a mobile workforce, and it's not unusual for them to move from job to job, even career to career. That puts a premium on portable retirement benefits—benefits that can travel with a worker throughout his or her lifetime, and that treat the first five years on the job the same as years 16 to 20. Eliminating formula-driven benefits also gives workers remarkable flexibility to define their own work schedules and retirement timetables. The notion that everyone has to retire around age 65 is no longer binding, thanks to the defined contribution structure.
- **Ownership**: The holder of a 401(k) account owns actual assets, not a promise of future benefits. 401(k) participants have full rights to their own contributions and the investment earnings on those, subject only to the tax rules that encourage workers to preserve their savings for retirement. Workers also acquire ownership of any employer contributions within no more than six years. Participants control their assets, and the investment manager who oversees them is subject to strict fiduciary and regulatory requirements to safeguard them.
- **Innovation**: The rapid development of 401(k) plans reflects a unique partnership among employers, participants, service providers, and investment providers, working within a framework set by government. Each of these groups has played a critically important role in designing, bolstering, and promoting 401(k) plans—and creating innovative solutions to problems as they've arisen.

I also identified steps that we as a nation must take to create a better retirement future for our nation.

- **We must put Social Security on a sound financial footing.** Social Security provides the foundation of retirement security for almost all American workers, and for the majority of Americans, it may be the largest single income source in retirement. But on its current course, Social Security is not going to be able to meet its future obligations.
- **Workers need a deeper understanding of retirement savings.** ICI worked hard for many years to help the Department of Labor craft comprehensive new disclosure standards for fees, risks, performance, and other vital information. The fruits of that labor are starting to appear this summer as savers receive uniform and enhanced information from their plans for all their 401(k) investment options.

We need to continue to innovate to meet a wide array of needs among America's workers. To increase participation and savings, ICI has called upon Congress to consider requiring all 401(k) plans to use automatic enrollment and automatic savings escalation.

- **We must redouble our efforts to provide financial and investor education to all Americans at every age.** This is a job for educators, for government at all levels, for financial institutions, for all firms that serve the retirement market—and for trade associations such as ours. We must ensure that investors have access to the advice and support they need, whether saving through an employer plan or within an IRA.
- **We must meet the needs of 401(k) savers who are becoming 401(k) retirees by offering innovations to help them manage their assets to produce steady income streams in retirement.** For example, mutual fund sponsors are working on

pairing sophisticated investment models with systematic withdrawal programs to help retirees turn their 401(k) assets into consistent income streams throughout retirement. To meet the challenge of inflation, some providers are including Treasury Inflation Protected Securities (TIPS), in their target date fund portfolios.

- **We must face up to our fiscal challenges.** And we must do so without undermining the tax incentives and other features that successfully encourage millions of Americans to accumulate savings during their working lives and thus generate income in retirement. On this, Americans are solidly in agreement: in our 2011 survey, 85 percent of all U.S. households disagreed when asked whether the tax advantages of DC accounts should be eliminated, and 83 percent opposed any reduction in employee contribution limits.

I invite you to read the full speech and to learn more about 401(k) plans at our 401(k) Resource Center.

Paul Schott Stevens was President and CEO of ICI.
