Retirement saving in the United States has come a long way since the Internal Revenue Service adopted regulations ushering in defined contribution vehicles such as 401(k) plans. But we still have a lot of work ahead. By adopting the best features from other leading nations, we can move closer to a structure where U.S. workers put aside enough to fund their golden years.

A number of shortfalls in the American retirement structure need addressing. These are especially evident when you compare the U.S. system to other countries’ retirement programs. The U.S. retirement system could vastly improve retirement outcomes for millions of contributors if we implemented a few key changes.

1. Make retirement saving or auto enrollment compulsory for U.S. workers.
2. Embed an annuitization process as a mandatory feature of these plans.
3. Work toward simplification of regulations governing retirement savings plans so employers more easily understand them and are less concerned about potential litigation that may arise from forcing participants to save and invest.
4. Implement federally sponsored educational efforts so that current and future workers understand retirement savings, investment and distribution choices.
5. Severely limit pre-retirement withdrawals and loans to staunch the “leaks” we typically see in retirement savings accounts that can significantly erode their ending values.

STILL NOT SAVING ENOUGH

The three-legged stool that underpins the U.S. worker’s retirement savings doesn’t provide the same level of support, financially or education-wise, as the multi-legged models other countries employ. With the continued decline of defined benefit (DB) plans, Americans typically rely on employer-based defined contribution (DC) programs such as 401(k) plans, as well as Social Security and their own personal savings.

Of those people with some retirement savings, the median amount saved is $104,000 for households age 55 – 64 and $148,000 for those ages 65 – 74. That’s equivalent to an inflation-protected lifetime annuity of just $310 and $649 per month, respectively.
Astonishingly few U.S. workers nearing retirement have saved enough (or any) money for their retirement years. In fact, about half of U.S. households aged 55 and older have no retirement savings at all, according to the U.S. Government Accountability Office Retirement Security report issued in May 2015. And that figure includes any 401(k) or IRA savings. Of those people with some retirement savings, the median amount saved is $104,000 for households age 55 – 64 and $148,000 for those ages 65 – 74. That’s equivalent to an inflation-protected lifetime annuity of just $310 and $649 per month, respectively. It’s not much money to supplement Social Security – assuming the program survives the next decades – and any personal savings, which often include home equity.

That means too many U.S. workers are relying almost exclusively on the government to provide funds during retirement rather than saving on their own. Many others must continue working part-time after their “official” retirement just to get by. The reasons for this are legion, but foremost among them is the fact that the United States does not require its workers to save for retirement. In a heterogeneous, melting-pot culture where self-reliance and bold decision-making are held up as virtues, we do not hold our retirement funding structure up to that same social scrutiny. Many workers can and would save, if only we required it.

**HOW OTHERS DO IT**

That situation contrasts markedly in other developed countries with well-regarded retirement structures. One huge difference is that the United States does not make contributions to pension savings plans mandatory. Nor do we require workers to understand the financial investment they are making in their own futures.

In Denmark, for example, employees contribute one-third and employers contribute two-thirds to the mandatory DC program, which incentivizes annuities by removing the limit on contributions paid into it. The Danish program provides greater protection against fraud, mismanagement or provider insolvency of members’ accrued benefits, and it uses investment professionals to handle the DC funds’ asset allocation. Norway has offered a national public insurance program since 1997 and implemented an updated pension plan in 2011. It includes a mandatory occupational pension arranged by employers for employees. And in the Netherlands, there are a number of “hybrid” DB-DC plans where the employee also contributes to the DB-type employer-sponsored program.

In Hong Kong, the government set up a mandatory savings scheme in 2000 under which workers and employers each contribute 5% of their salaries. Now, some 85% of employees are covered by a pension plan, far above the roughly 30% of workers who had voluntary coverage before the government stepped in. Hong Kong also is implementing a default fund option for investments if the participant fails to choose a specific fund for his contribution. The default option has a cap on the fee charges as well as an investment strategy that is to be standardized across all MPF schemes. And although Hong Kong doesn’t encourage individual savings by offering a tax advantage, it differs culturally in that there is much more family support for retired workers than in the United States.
Beginning in the mid-1960’s, Canada has operated a federal pension plan, the Canada Pension Plan (CPP), funded by employee and employer contributions. The CPP forms one of the two major components of Canada’s public retirement income system, the other component being the Old Age Security (OAS). Canada’s retirement system is further supported by private pensions (defined benefit or defined contribution plans), either employer-sponsored or from tax-deferred individual savings (known in Canada as a Registered Retirement Savings Plan). To provide additional retirement income, Canada culturally has always encouraged individuals to take personal responsibility for saving enough to retire. That voluntary approach, however, is slowly changing as provincial governments realize that the current retirement savings program may not be sufficient to support its growing and aging population. While some provinces (Ontario and British Columbia in particular) explored the setting up of supplementary provincial pension plans, an enhanced federal program through the CPP has been proposed that will see increases to benefits and contributions to help close the gap.

Among the most forward-looking and aggressive government retirement schemes is in Australia, where the government requires employer minimum superannuation guarantee contributions of 9.5% into a superannuation fund. That money is invested in the employer’s fund or the employee’s fund of choice. One key difference between the Australian and U.S. systems is that contributions to Australian superannuation funds are taxed at entry and are tax-free when transferred out of superannuation into retirement accounts. However, the recent 2016–17 Federal Budget introduced a AUD 1.6 million cap on the amount that can be transferred tax-free at retirement.

UNIVERSAL CONCERNS

Other retirement funding issues cross all geographic borders. Foremost among them are concerns about increasing amounts of regulations and paperwork around pension plans and schemes. The lack of clarity about the rules governing the plans, as well as opacity around the rule-making process, hamstrings those who must abide by the rules. As some pension sponsors note, it’s hard to play by the rules if you don’t understand them!

Also universal among complaints is the recognition of a dearth of solid education aimed at making employees and students – the future workers – savvier financial consumers. Although some nations, including Australia, are addressing this with government-sponsored efforts, others have little in the way of national programs.

In the United States, we face a woeful lack of education to help workers understand and evaluate their retirement income on an annual basis. And too much of the material that does exist comes from financial companies with a vested interest (i.e., commissions) in guiding those monies into their own branded funds and investments when white-labeled funds might perform better.

1 The Canada Pension Plan is for all provinces in Canada except Quebec, which has the Quebec Pension Plan.
We also foster the impression that 401(k) plans are the worker’s total end-all, be-all savings, so many do not squirrel away much money in addition to those DC contributions. And given the annual contribution caps in place, a 401(k) plan alone likely will not provide enough income in retirement for many employees. So there must be other money set aside for retirement.

The focus should be not only on calculating likely budgets during retirement but also on figuring how much money a worker will have each month or year during retirement. Instead of honing in on the total nest egg he or she has accumulated, we should look at annuitizing that amount to compare to the worker’s expected monthly retirement budget.

One way to better acclimate future workers into this holistic mindset would have the U.S. Department of Education implement widespread educational programs starting in elementary school. These could indoctrinate young students into the habit of thinking about saving for retirement as a natural part of the transition process when they graduate from an academic setting into the working world. And they would help erase the fear factor that can grow up around the math needed to figure out future finances.

Another key change that U.S. plans should make would be to severely curtail the ability of U.S. 401(k) plans contributors to take money out entirely or take loans before age 59-1/2. Many employees like the idea of a flexible retirement account that they can access if they deem it necessary. But this practice causes “leaky” plans, where it’s estimated that some 40% of money contributed flows out long before the employee retires.

This contrasts starkly with policies in Australia, Germany, Hong Kong, the United Kingdom and Canada, all of which limit withdrawals to hardships. But the catch is that some U.S. employers and plan sponsors fear the accusations and potential litigation from employees if you take away their ability to access their own money.

MORE WORK AHEAD

Many of the countries with the strongest retirement systems also have much less federal debt to service and much higher taxes overall that fund their healthcare and pension programs. It’s clear that the United States would be hard-pressed politically and socially to suddenly raise taxes to the levels seen in France or Denmark in efforts to strengthen our social safety nets.

But we can take other smaller steps – closing some of the loopholes that allow for early withdrawals, making some level of pension contributions mandatory and stepping up our educational efforts. All these are less angst-causing moves that are doable across a broader swath of the current work force. And all are clearly aimed at making the financial possibility of a less-stressful retirement achievable for more American workers.