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Forget the 401(k). Let's Invent a New Retirement Plan.

Ideas include allowing your savings to follow you wherever you go or however you work

By Jason Zweig

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If we could reinvent retirement-saving plans from scratch, how would they differ from the rigid and often paltry 401(k)s that workers have today?

In all sorts of ways.

The reimagined plan, for one thing, would blend the stable income for life of old-fashioned defined-benefit pension plans with the favorable tax treatment of the contemporary 401(k). But unlike those plans, this one would follow participants wherever they work and be universally available, while accommodating the needs of different kinds of savers and protecting participants from their own worst impulses.

None of this is impossible to accomplish, although many of the best ideas for improvement will require new laws, regulations or technological innovations. But there's little question that the 401(k) as we know it just isn't getting the job done. With lifespans lengthening, health-care costs rising, and stocks and bonds alike expected to deliver lower future returns, the need to augment retirement savings is greater than ever.

Consider: One-quarter of working Americans say they have no pension or retirement savings at all, according to a 2017 survey by the Federal Reserve; among those who are 60 or older, 13% say they have nothing saved for retirement, leaving them to rely largely on Social Security, which often won't pay enough to sustain their standards of living.

So now is the time to imagine a new future—one that offers retirees the best chance at avoiding the hardships that threaten so many of them today. Here are the suggestions of retirement-industry leaders and academic researchers on how to get there.

Savings plans for retirement should be universally available

Ted Benna, the benefits consultant who in 1981 implemented the first practical 401(k) savings plan, remains frustrated by the glacial pace at which access to retirement plans has widened.

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In 1999, private employers offered retirement-plan coverage to 63% of workers. As of 2017, nearly two decades later, that number had ticked up only to 66%, according to the Bureau of Labor Statistics.

"Education only goes so far," says Mr. Benna. "Design is what actually changes behavior. Unless you have a mandate, it's going to take a very long time to close this gap of so much of the workforce not having access to a retirement plan."

So, he says, all businesses with 10 or more employees should have to offer a retirement plan. Employers should also be required to enroll their employees in the plan automatically, he says, and to increase workers' contributions on a predetermined schedule over time until they are saving at least 6% of pay. Mr. Benna says employers could satisfy that requirement by offering a payroll-deduction IRA program with minimal administrative costs.

Workers would still be free to opt out of saving entirely or to reduce their contribution rate, but they would have to make an active choice to do so. Inertia is as powerful a force in finance as it is in physics: People will rarely reverse a decision they have already made, so most who are prodded into saving won't choose to stop.

Make it easier to convert savings into regular income

To convert preretirement savings into regular retirement income, Mr. Benna suggests that the first $1,000 of withdrawals each month should be tax-free. Extending a tax break to retirement-annuity income, he says, would encourage retirees to take advantage of the opportunity to lock in a lifelong stream of monthly payments. That, he says, would incentivize retirees to demand—and insurance companies to offer—a wider selection of low-cost annuities that would offer guaranteed income for life.

70%

Civilian workers who have access to retirement-benefit plans

55%

Civilian workers who participate in retirement-benefit plans

79%

Civilian workers who have access to retirement-benefit plans and participate in them

Source: Bureau of Labor Statistics, 2017 data

Supplementing the 401(k) with the regular-income feature of defined-benefit plans, while skipping the shoddier aspects of their history, is long overdue.

Often romanticized today as representing a golden age of retirement, defined-benefit plans were, in fact, sporadic, arbitrary and unfair: In 1950, only about 25% of workers were covered, most had to work for at least 15 years at the same company to earn the right to receive any pension, and many employers that had promised to pay regular retirement income ended up going bust and leaving their pensioners holding the bag.

Thus, the most alluring feature of a defined-benefit plan—the promise of a stable, monthly, lifelong income—was never attained by most workers.

Retirement income should last well past the age of 65

New proposals seek to make the often-chimerical promises of the past a widespread reality today by securing regular income for retirees for the rest of their lives.

As of now, such longevity income annuities are rare, say Tom Totten, chairman of Nyhart Co., a benefits-consulting firm in Indianapolis, and Laurence Siegel of the Research Foundation of CFA Institute, a nonprofit that studies investments.

That's largely because many people don't like the incremental payments generated by annuities. They prefer instead to receive payouts in a seductively large lump sum—even when the annuity would have greater cumulative value.

To make sequential monthly payouts more appealing, about three years ago Nyhart began designating its contributions in the amount of 0.5% of salary to the company's profit-sharing plan as a "longevity account." Those contributions immediately belong to the firm's roughly 150 employees. Nyhart assures employees that when they turn 65, they will have the option of using those contributions to purchase a deferred longevity annuity. That form of insurance will begin paying regular monthly income when they reach the age of 85, so long as they live.

That way, employees need only to plan for their retirement savings to last 20 years, from age 65 to 85. If they are lucky enough to live longer than that —as few people expect to, but as about 50% do—then the annuity will kick in.

Someone who worked 30 years and earned $50,000 annually should receive roughly 1% of those cumulative earnings, beginning at age 85, for life. Such an annuity would pay about $15,000 a year, or $1,250 in regular monthly income. That's meant to supplement Social Security and other savings, much as a traditional pension would, says Mr. Totten.

"That's a better way of looking at retirement, instead of saying, 'I don't know how long my money has to last,' " he says. "It's breaking it up into two pieces, instead of one unknown number. It's a hedge against living too long."

The cost to employers of 0.5% of salary is fairly low, says Mr. Totten, and could simply be redirected from conventional contributions to a retirement plan. A few of Nyhart's outside clients are discussing whether to adopt such a program, says Mr. Totten, although most people continue to underestimate how long they will live and to overestimate how long their money will last.

Your retirement savings should follow you wherever you go or however you work

Phyllis Borzi, a consultant who headed the employee-benefits division of the U.S. Department of Labor from 2009 to 2017, would like to see "fully portable" retirement plans, in which "every hour you work, no matter where or for whom you work, would count toward an ultimate benefit."

Regardless of whether you were self-employed, a full-time employee, an independent contractor or a leased employee, a professionally managed not-for-profit company with an independent board of directors would collect and invest retirement contributions from you and your employers.

> **With "fully portable" retirement plans, "every hour you work, no matter where or for whom you work, would count toward an ultimate benefit."**
>
> —Phyllis Borzi

Ms. Borzi envisions such companies operating large regional pools of capital. The resulting balances would automatically move with you as you changed jobs.

Contributions from employers would be voluntary, as they are now, but individuals for whom employers do contribute would be required to set aside a portion of their pay.

That could help prevent retirement savers from being separated from their money. From 2004 through 2013, workers leaving their jobs also left behind at least 16 million retirement accounts with balances of $5,000 or less, according to the U.S. Government Accountability Office. That money belongs to retirees, but such small balances can easily be devoured by fees or lost track of by their owners.

All told, such orphan accounts totaled $8.5 billion in retirement savings whose owners may barely remember them.

Finally, retirement savings should be made much harder for savers to raid

A team of researchers including Brigitte Madrian, dean of the Marriott School of Business at Brigham Young University in Provo, Utah, thinks retirement savers should have at least two nest eggs, including one that's hard to access and one they can break open almost at will.

So many Americans live paycheck to paycheck that they often feel they have no choice but to raid their retirement accounts to fund current spending needs. More than four in 10 adults say they couldn't easily meet an unexpected $400 expense, according to the 2017 Federal Reserve survey.

The U.S., unlike such other major countries as Germany, Singapore and the U.K., makes it fairly easy for workers to make early withdrawals (often with a 10% tax penalty) from retirement accounts.

No wonder about 14% of taxpayers under the age of 55 made taxable withdrawals from retirement plans in any given year from 2004 to 2010. Over the same period, according to research from the Federal Reserve and the Internal Revenue Service, taxpayers under the age of 55 yanked out an average of 29 to 41 cents of every dollar that went into their retirement accounts.

"It's too easy for people to access their money right now, and lots and lots of people are doing it," says Ms. Madrian. What she and her colleagues call a rainy-day account could change that.

"If you only have one account, then it de facto becomes the 'everything' account, so people no longer think of it as a retirement account because it's serving multiple purposes," says Ms. Madrian. "And it's got a lot of money in there, so you take a lot of money out of there—the same way you eat more out of a big bag of potato chips."

To mitigate that problem, she and her colleagues have proposed permitting employers to set up rainy-day accounts from which workers could withdraw limited amounts of money to meet emergencies.

The less an employee has in rainy-day savings, the more of the early contributions would go there. As those savings build, more of the total contributions would automatically be shunted into the retirement bucket.

A young or struggling saver might have 50% of contributions allocated to the emergency account at first, to create a cushion against short-term critical expenses, says Ms. Madrian. Independent contractors and other gig-economy workers could even have their contributions adjusted dynamically depending on the fluctuations in their monthly income.

As a result, employees would be more likely to tap the emergency account than the retirement fund—leaving more and more of their savings, over time, to grow undisturbed in the long-term account.

Ms. Madrian and her colleagues are already designing a pilot program to test the idea of rainy-day accounts in the U.K., she says.

Combining old and new ideas in creative ways could eventually improve retirement security for millions of workers. With luck, more employers and workers alike will start demanding features like these. When the marketplace evolves, regulators and policy makers eventually follow.

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