

Looking Forward... The “Super 401(k)”

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The number of American workers covered by traditional pension plans is in rapid decline, making 401(k) savings plans a primary source of retirement income for private-sector workers in the U.S. Unlike a pension plan, a 401(k) plan requires employees to save and invest wisely in order to accumulate retirement wealth. This has proven to be a challenge for the average American worker.

According to the Vanguard Center for Retirement Research, nearly one-third of eligible workers don't participate in their company 401(k) plans at all, and many that do fail to save enough or make poor investment decisions. To address these concerns, Congress incorporated several 401(k) provisions in the Pension Protection Act of 2006, including automatic enrollment, automatic deferral increases, broadly diversified default investments and investment advice. In essence, these provisions were established to encourage better saving and investment strategies for workers.

Encouraged by these recent regulatory changes that shield employers from lawsuits, more companies are starting to make changes to 401(k) plans, with the goal of taking the decision-making out of employees' hands. A great example to illustrate the new frontier of 401(k) plan design in the post-PPA era is Devon Energy.

For the 2008 plan year, Devon offered its 3,400 employees an unusual choice. They could either stay with the company's traditional pension and 401(k) retirement plans or switch into a new "super 401(k)." Under the new plan, Devon will make annual contributions to employee accounts in line with what it would have spent to provide a traditional pension benefit. Depending on an employee's tenure, the company will put 8% to 16% of annual compensation into the 401(k). And for those who do put money into the plan, the employer will also match it dollar for dollar up to 6% of salary. All in, between employer and employee contributions, a participant in the plan can be saving as much as 28% of pay per year.

In return for Devon's generous contributions, employees who chose the super 401(k) are required to use "target date" funds that have been customized for the Devon Energy plan.

In case you haven't been paying attention to the buzz, target date funds provide participants with a one-stop solution to get them to and through retirement. Employees simply select the fund that most closely matches their expected retirement date, and the fund managers shift into a more conservative mix of stocks, bonds, and other asset classes as retirement approaches.

Ironically, the brave new 401(k) world may start to look more like that of traditional pension plans, in which the company makes decisions about funding and investments. The big difference, of course, is that if the investments lose money, the employee bears all the risk.

It will be interesting to see over time how other employers act on the incentives that Congress and the Department of Labor have given them to help workers achieve greater retirement security. As a nation, we can't afford for the 401(k) to not be successful.

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