

LEGAL ADVICE

We must encourage our employees to save

By now you have read about the crisis involving defined benefit pension plans that at one time formed the backbone of American middle class retirement. Such plans are going the way of the Edsel.

According to a recent study by the Pension Benefit Guarantee Corporation (the PBGC), the federally created entity that takes over underfunded plans, the number of private sector defined benefit plans reached a peak of 112,000 in the mid 1980s, but has since declined to a little over 30,000 at the end of 2005, and continues to dwindle. The PBGC estimates that from 1986 to 2004 approximately 7.5 million participants in defined benefit plans were terminated. Even public pensions, such as those earned by policemen and firemen and once considered sacrosanct, have recently come under attack. State and local governments, suffering from a declining tax base, particularly in hard hit areas like the Rust Belt, simply have not been able to sock away enough money to cover these obligations.

Defined benefit plans are those plans that guarantee a retiree a fixed monthly income based on a formula, usually taking into account salary and years of service. Such plans are for the life of the retiree and usually have a cost of living adjustment on an annual basis. These defined benefit plans are quickly being replaced by so-called defined contribution plans such as 401(k) plans, in which an employee may contribute to a fund which the employee manages at his or her own risk.

Responding to rising concerns about the state of pensions in America, Congress recently enacted the Pension Protection Act of 2006, which was signed into law in August by President Bush. The primary purpose of the law is to protect employees from under-funded plans managed by their employers and requires most pension plans to become fully funded over a seven-year period starting in 2008. One recent study showed that a little over 80 percent of corporate pension plans are underfunded.

Critics of the plan suggest that this will merely hasten the number



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of companies who freeze their pension plans and switch new employees over to defined contribution plans such as a 401(k). Freezing of defined benefit plans means that participants will not lose the benefits they have already accrued, but no further benefits will accrue to them. The money that would have accrued has to be made up by individual contributions by these workers.

The concern among many is that the average American worker has historically been a very poor saver. A majority of workers, when given an option to enroll in a defined contribution plan, either choose not to, or fail to properly invest their contributions to achieve a respectable level of return.

The Employee Benefit Research

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Group estimates that a majority of workers age 45 and older have less than \$50,000 in retirement savings. By even the most optimistic estimates, those counting on Social Security to make up the difference in retirement will be sorely disappointed.

Though moderate steps were taken under the Pension Protection Act to encourage more participation in 401(k) plans, more must be done to encourage every American worker to take personal responsibility for retirement. Workers must be reminded that it is never too late to start saving, and tax laws now allow those over 50 to contribute a little extra to

defined contribution plans to catch up for past years. Even if you can only afford to set aside a little at the beginning, getting into the habit of saving is critical. Most companies will allow automatic payroll deductions, which makes contributing even easier. If you get a raise, contribute the extra money from each paycheck to your retirement. And by all means, if your company provides a match contribution, make the minimum amount necessary to earn it. Otherwise, you are just leaving free money on the table.

Simple steps such as these will get more workers into the habit of saving. The costs to the country by not encouraging responsible economic behavior — and to each individual retiree — is simply too great to ignore. ■