MANAGING YOUR MONEY

It May Be Time To Design Your Own Pension Plan

(NAPSA)—Your mom or dad may have had a company pension, but chances are you do not.

Since 1985, the number of defined benefit plans has shrunk from more than 112,000 to less than 30,000, according to the U.S. Pension Benefit Guaranty Corp.

It's no longer the struggling companies that are cutting pensions. Even "healthy" companies are deciding to cut or freeze pensions due to a variety of factors, including a desire to cut compensation, growing health care costs, and the increasing risk inherent in funding defined benefit plans.

Citigroup, for example, announced a few months ago that it will freeze pension contributions beginning in 2008 and will instead raise matching contributions in 401(k) plans.

What 401(k)s Mean To Your Retirement

What does the movement from defined benefit plans (pensions) to defined contribution plans like 401(k)s mean for retirement in America?

Simply put, 401(k)s were designed to provide supplemental retirement income to be used in conjunction with company pensions and Social Security, the main sources of retirement income. Unlike pensions, they provide retirement savings, but do not provide retirement income. This means workers may have to move their savings to another retirement vehicle in order to receive distributions once they retire.

Remember that with a 401(k) plan, it is up to the employee to decide whether to participate. The passing of the Pension Protection Act of 2006 prompted making enrollment in 401(k)s automatic, requiring employees to "opt out" instead of "opt in."

Unfortunately, most employees who do participate do not contribute enough to accumulate enough retirement savings. According to research from the Center for Retirement Research at Boston College, only 1 percent of workers earning under $60,000 made the maximum annual contribution to their defined contribution plan in 2004.

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Families that are stretched with rising health care and housing costs simply cannot afford to contribute. In addition, many employees are not properly educated and prepared to make financial retirement decisions required with 401(k) plans.

Many fail to diversify (e.g., holding too much company stock or other single-equity investments), which puts their portfolio at risk. With the increasing frequency of workers changing jobs, many cash out their 401(k), unaware of the detrimental effect that can have on retirement income.

"In summary, 401(k) plans require the employee to decide whether or not to join the plan, how much to contribute, how to invest the contributions and when to rebalance, what to do about company stock, whether to roll over accumulations when changing jobs and how to use the money in retirement" ("401(k) Plans Are Still Coming Up Short," by Alicia H. Munnell and Annika Sunden, Center for Retirement Research at Boston College).

So what can Americans do in light of the changes in retirement-income funding? There are a number of choices. They can create a comprehensive retirement income plan consisting of a managed portfolio, such as a 401(k), and an annuity that produces a guaranteed income stream.

Variable Annuities

Variable annuities are gaining popularity as a source of guaranteed retirement income within a diverse retirement income plan. "Today's variable annuities are usually designed as income contracts as well as savings vehicles," said Mike Buchholz, whose company, ING U.S. Financial Services, offers consumers several annuity products through brokers and financial advisors.

How popular is this? The first quarter of 2006 showed record variable annuity sales. Reasons for their popularity include:

- Variable annuities offer tax-deferred asset accumulation, like 401(k)s, but also come with "risk insurance," protecting retirement assets from market downturns.
- Variable annuities offer a variety of other insurance benefits that can help create a sense of security for retirees. Like traditional pensions, annuities can provide a steady stream of income—a retirement "paycheck."

Companies have spoken—it is no longer their responsibility to fund their employees' retirement income. The sooner Americans understand the implications this change can have on their retirement security, the better chance they'll have of taking over the reins and creating a comprehensive retirement income plan that will meet the demands of modern retirement. To learn more, visit www.navanet.org.