

## Defined Contribution Plans



This issue features an interview with **Catherine Collinson**, president of Transamerica Institute and Transamerica Center for Retirement Studies, a nonprofit based in the U.S.,



and **Lex Solleveld**, retirement product design leader of Aegon in the Netherlands



Moderated by  
**Stacy L. Schaus, CFP®**  
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## Global Retirement Expectations Gap

In this *PIMCO DC Dialogue*, we speak with **Catherine Collinson** of Transamerica Center for Retirement Studies in the United States and **Lex Solleveld**, retirement product design leader of Aegon in the Netherlands. They share insights and suggestions on how to improve retirement plans globally. Drawing from the 2014 Aegon Retirement Readiness Survey, they compare and contrast differences in workers' retirement confidence and expectations across 15 countries. They also highlight the shift from traditional defined benefit (DB) plans to DC systems and comment on how workers often underestimate the change and their personal retirement planning responsibility. They support automatic enrollment and escalation systems because these systems make retirement saving easier for workers. They encourage the government to offer more support to plan sponsors for offering financial planning and retirement income solutions. Finally, they suggest that employers do more to help workers transition to retirement, including supporting part-time work arrangements and workers' access to DC savings.

**DC Dialogue:** Can you tell us about your organizations and how you work together on global retirement issues?

**Catherine Collinson:** Transamerica Center for Retirement Studies (TCRS) is a division of Transamerica Institute, a nonprofit private foundation that is funded by contributions from Transamerica Corporation. Its mission is to conduct research and help educate the public about the latest issues and trends surrounding saving and planning for a financially secure retirement.

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Aegon is the parent company of Transamerica Corporation and is an international life insurance, pension and asset management company with businesses in more than 25 countries in the Americas, Europe and Asia. Its mission is to help people take greater levels of personal responsibility for their long-term financial security. To this end, it conducts research to support our retirement product development efforts as well as to help inform clients, advisors and the public about retirement sentiments.

TCRS collaborates with Aegon and team members around the world in conducting the global Retirement Readiness Survey, which is in its third year of existence. We have seen tremendous demand and even passion around finding solutions to help workers around the globe retire successfully.

**Lex Solleveld:** In the Netherlands, I lead the Aegon retirement product design team. We value the research conducted by our organizations, as well as the collaboration with the academic community, such as the Dutch group Netspar. We work to understand the needs and preferences of market participants, including plan sponsors and other stakeholders. It's a very active discussion.

**DCD:** Can you tell us more about the 2014 Aegon Retirement Readiness Survey?

**Collinson:** TCRS worked with Aegon representatives to survey 16,000 working or retired people in 15 countries about their retirement ambitions and fears. Countries spanned the globe, including Asia, the Americas and Europe. In each country, we surveyed 1,000 respondents, including 900 employees and 100 retirees. The survey was conducted online, so that presented some challenges and potential sample bias in developing markets such as China, India and Brazil. In such markets, we understand that we reach more urban dwellers than those living in the countryside or rural areas.

**Solleveld:** We have found the study helpful particularly as the Dutch market continues the move from defined benefit (DB) plans to more of a DC structure. We are focused on helping individuals meet needed outcomes. Our study helps identify the retirement income needs and preferences, allowing us to make the connection with the final client – the plan participant. At a product level, we work to set retirement income targets and then manage the products to help make retirement happen.

**DCD:** Catherine, can you tell us more about the survey objective?

**Collinson:** The overall objective of the survey is to understand the attitudes, savings behaviors, perspectives and retirement confidence and preparedness of employees and retirees around the world. Based on our research findings, we prepare recommendations on how to improve the retirement systems. Several years ago when we started this journey, we didn't have any preconceived ideas of what the results might look like. So, it's been exciting and informative for us.

We aim to capture a full picture of how people are thinking about and preparing for retirement. The survey asks a range of questions such as: Are you aware that you need to save? Do you feel like you're saving enough? Are you engaging in various planning-related activities? Do you have a plan or a strategy? Do you have access to employer benefits? What are your dreams and aspirations for retirement?

While we know that retirement systems around the world vary in terms of government benefits, employer benefits and the degree to which people save, we also understand that many systems have been under financial strain because of the financial crisis, low interest rate environment and increasing longevity. These pressures differ in magnitude country by country, so we look at our findings relative to this backdrop.

**DCD:** Can you share both your suggestions on how to improve the retirement system and the survey observations that support your suggestions?

**Collinson:** Our 2014 survey report theme is "making it easy." Workers need a simpler and more flexible retirement system. Our findings support this direction and are presented in four parts. First, while the economic outlook for most countries is improving and workers have more positive retirement aspirations, they continue to report concerns about the reality of living in retirement. Second, the study shows that most workers continue to fall short in retirement planning and preparedness. Third, we find that automatic enrollment and escalation programs are globally attractive and underscore the desire for simplicity. Finally, we identify a need to support retirement transitions, as many workers desire or need to continue working at least part-time as they age.

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**DCD:** Can you tell us more about worker aspirations and confidence in the ability to retire?

**Collinson:** Our study shows that over a quarter of respondents (28%) expected their domestic national economy to improve in 2014, while nearly a third (31%) expected their personal finances to improve. Both percentages were up relative to expectations in 2013. People continue to hold positive aspirations for retirement, with many associating retirement with leisure (46%) or a sense of freedom (41%). Yet, few people (19%) reported being very/extremely confident that they will enjoy a comfortable retirement. Notably, for the first time, over half of respondents (53%) expect future retirees to be worse off than prior generations.

What's interesting is how significantly the confidence numbers vary by country. Developing markets (China, India and Brazil) showed the highest confidence scores (very/extremely confident), averaging 37%, while Japan, France and Poland reported the weakest scores, at less than 6%. The U.S. came in ahead of the Netherlands, at 28% confidence versus 21%. That's a counterintuitive finding as the Netherlands is viewed worldwide as having one of the best retirement systems in the world – and superior to the U.S. We asked how that could be possible when Dutch people are better cared for in retirement than those in the U.S.

We believe retirement confidence is a function not only of the retirement system, but also of expectations. And for years now in the U.S., the general public has been very aware of the need to plan and save, as well as of retirement savings shortfalls. And we believe that many Americans have simply adjusted their expectations about retirement.

**Solleveid:** That's a good observation. I agree that there is a gap in expectations. Dutch people expect that the government or their employer has planned for their retirement. Within certain industries it's obligatory for all employees to participate in the industrywide pension scheme. Although not obligatory for many other industries, more than 90% of all companies in the Netherlands offer a company pension scheme. It's therefore not surprising that consumers believe their retirement needs are addressed.

Unfortunately, more than 80% of Dutch workers believe that they get a final pay pension, but that is no longer true for the vast majority. This misperception is perhaps culturally fed by observing the current retiree population, who did leave the labor market with a final pay pension. The standing joke is about how these retirees golf four days a week in the Netherlands and the remaining three somewhere else on the planet, plus they have enough money to spend on presents for their grandchildren. Their lifestyles heavily influence the thoughts about retirement in the Netherlands.

What the majority of Dutch workers do not realize is to what extent the pension system has changed over the last five to seven years. While the contribution rate by employees and employers remains high at 15% to 21% of income, the structure has shifted away from a final pay traditional DB plan to more of a DC structure.

Also, the Dutch population's awareness that their retirement and their pension savings depend heavily on interest rate levels and investment income is very low. And this is where the challenge is, because the government is doing some cutbacks on pensions. The need for reform is high, and a first step has been taken toward individual pension savings. This is, however, still outweighed by the attention on gradual changes in company pensions. Without the public noticing, responsibility for retirement is increasingly on the shoulders of consumers and pension providers such as Aegon. And as a pension provider, Aegon is held to a very high level of duty of care by the Dutch regulatory bodies. Our challenge over the coming years is to help individuals have realistic retirement expectations and then help meet those expectations.

**DCD:** What are the challenges in helping people develop realistic retirement expectations?

**Solleveld:** While the Dutch often quip that they work a day a week for their retirement, they generally do not plan for retirement or seek financial advice. They are not aware that they need advice, and there is no willingness to pay for this important service. It will take many years to increase awareness and to help Dutch workers understand the value of financial planning.

**Collinson:** To support Lex's comments, in the second part of our survey on retirement readiness, we asked whether workers have a written retirement plan. Only 10% of Dutch workers said they have a written plan, compared to 18% in the U.S. We also asked how they would rate their level of awareness on the need to plan financially for retirement. Twenty-five percent in the Netherlands are very aware, compared to 41% in the U.S.

Further, we asked to what extent they felt personally responsible for making sure they had sufficient income in retirement. In the Netherlands, 25% said they feel very responsible, compared to 55% in the U.S. That's a significant divide.

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**DCD:** I understand that the Netherlands' shift to DC plans has not been to pure DC, but rather to a collective DC plan. Is that right?

**Solleveld:** Yes, that's right. Collective DC reduces the employer's responsibility to pay the pension premium or contribution and the plan service costs. Employers are off the hook on paying out a pension payment for the retiree's life. Yet, a collective DC (CDC) is presented to the worker as a DB scheme in that an estimated income for life is provided. In reality, the CDC payout is not guaranteed by the employer or any other party. The payout is subject to change, and with the crisis and low interest rate environment, we've seen significant adjustments in some of the CDC payouts. Retirees did not understand or anticipate this change.

Now we're seeking ways to offer retirees more certainty. We're looking at guarantee solutions to add to DC schemes. The first generation of DC was seen as much too simplistic. We're working together with research and the academic community to improve outcomes for workers. As a nation, we're not ready to simply shut down DB schemes and start up brand-new DC schemes. Workers are not ready to take full responsibility for risk and planning. So the Dutch market is taking gradual steps toward DC and looking for ways to help manage risk for consumers.

**DCD:** Certainly there are DC-oriented systems that imbed guarantees, such as in Germany. Do workers show a higher retirement confidence level when such systems are available?

**Collinson:** Despite the availability of the guarantee, only 11% of German respondents said they felt confident in their ability to retire comfortably. This is well below both the U.S. and the Netherlands. Understand, though, that the guarantee within the plan is simply a return of nominal principal invested, so this may be insufficient to build confidence.

It's also common to see lower confidence in the European countries, given government cutbacks to the pension system and worries about the stability of public pension systems. Or other factors may influence confidence, such as mandatory retirement dates and unemployment. For instance, in France, respondents report anxiety about their need to work longer and the fact that they may be precluded from doing so. Spain offers an example of how high unemployment rates harm the worker's ability to save for retirement.

Retirement confidence is a function of the economy and overall retirement system – the government benefits – as well as guarantees people may receive. Around the globe, workers desire more stable and lower-risk investments.

**DCD:** Another country that jumps out in your study is Japan, where the confidence level is extremely low.

**Collinson:** Yes, Japan is a good example of low confidence correlating to long-term, lackluster economic growth. Plus, Japan has one of the most rapidly aging populations in the world, thus shouldering workers with more weight to carry for their elders.

**Solleveld:** In the Netherlands, we often cite Japan as a picture of what could happen to us if we do not alter our pension system. We recognize that with our aging population, increasing longevity, and continued low interest rate environment, we face the risk of looking like Japan.

**DCD:** Catherine, you mentioned that respondents desire low risk. Does your study support that people globally have the same appetite for risk taking? Or do you believe people may vary by country or culture in their risk preferences?

**Collinson:** Our study shows that people in faster-growing economies, such as China, India and Brazil, are more bullish on the markets, and this may make them more willing to accept market risk. However, by and large, workers report a desire for low-risk or relatively risk-free investments. I'd venture to say that everyday people are everyday people everywhere. They have similar aspirations for retirement. They are looking for retirement solutions that enable them to make informed and good decisions without taking on excessive risk or requiring them to be technical experts.

**DCD:** What types of risk protection, insurance or guarantees may be attractive in the future?

**Solleveld:** In the Netherlands, insurance in the form of immediate annuities is very expensive at present. And you may know, in our DC scheme, it's mandatory at the retirement date that all accumulated capital be invested in an annuity. The regulators realize that with the current low interest rate environment, immediate annuities are expensive. Or, to say it another way, given low rates, the annuity payout may be meager. Because of this reality, we anticipate legislation this year that will open the door for variable annuities, which may offer market-risk and longevity protection. We may also see other ways to manage market risk in DC schemes, such as using option-hedging strategies. It will take time to develop the right solutions.

**Collinson:** From a U.S. perspective, DC plan sponsors and providers are considering similar risk-mitigating solutions. It's fantastic to see the amount of innovation. The real challenge will be for the industry to translate these ideas into products and services that can deliver both the returns investors need and the risk management they seek.

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Unfortunately, our research identifies possible barriers to delivering insured solutions within the U.S. DC marketplace. Namely, from a plan sponsor perspective, there is a concern with potential fiduciary liability in the event something goes wrong with a selected provider or with delivery of the solution. We believe the government can help overcome this barrier by providing more fiduciary relief and safe harbors to support the plan sponsor community.

**DCD:** Catherine, you mentioned that the third part of your study encourages plan sponsors to make it easy to invest for retirement. Can you elaborate?

**Collinson:** We asked the survey respondents what would encourage them to save more for retirement or what would make it easier to save. And I guess it should not be surprising that in all countries, many respondents said a pay raise. Having more money available to save, of course, would make it easier for them to save.

But we also found in the survey responses that by simplifying the process and making it more convenient to save, people would be more likely to save. Nearly two-thirds of employees reported finding the concept of being automatically enrolled into a retirement plan appealing. They also identified the savings rate they believe appropriate, suggesting, on average, a 14% contribution, with 8% from the employer and 6% from the employee. Employers have a vital role to play in making retirement programs available, easy to access and understandable.

**DCD:** What else can employers do to help their workers enter retirement?

**Collinson:** The fourth part of our study considered the retirement transition. Employers can offer flexibility at the transition stage. Around the world, we see many workers envisioning a phased transition into retirement versus a gold watch, where you get an office party and stop working for the rest of your life. Our survey showed that less than a third (32%) of current employees, down from 34% in 2013, envision that they will immediately stop working altogether when they enter retirement. Only in Spain (52%) and France (51%) is the “cliff-edge” retirement seen as the norm.

Most people want to stay active and involved, and this means more want to continue working – ideally, with fewer work hours or with work that’s more satisfying and less stressful. People share that vision around the world. It’s a very optimistic and hopeful vision about the promises that retirement might be able to offer, assuming they can achieve their income needs. We encourage employers to allow those who remain working after retirement age to draw part of their retirement benefits while still at work.



Another variable for employers to consider is the risk of unforeseen events that workers face. While the majority may plan to continue working into their golden years, whether full- or part-time, illness or unemployment may thwart their plans. Among the retirees we surveyed, 45% reported they retired sooner than they planned. Ill health topped the chart of reasons for unplanned early retirement. Employers may consider offering disability insurance, long-term care insurance or other programs, such as elder care for family members and setting up personal emergency funds to help workers protect their nest eggs. Catastrophic expenses can destroy a nest egg overnight.

**DCD:** Do you have any other suggestions on how to improve retirement security?

**Collinson:** We need to encourage governments to continue making it easier for employers to offer retirement plans to their workers. Plan sponsors need more support to offer plans, retirement options, advice and more without the risk of liability. Employers have made great strides in helping millions of participants through auto-enrollment and auto-escalation programs. The plan sponsor oversight of investments and risks is also helping employees improve their financial security and well-being.

**Solleveld:** I agree with Catherine. In the Netherlands, as I mentioned, pension programs are standard for most organizations and their workers. Automatic enrollment is a nonissue – everybody agrees retirement saving should somehow be mandatory. We’ve seen all the behavioral finance evidence outside of the Netherlands which shows that if you lift automatic enrollment systems, there will be a lack of funding. And in the Netherlands, everybody agrees that it’s unacceptable to allow people to retire poor, so the Dutch are likely to keep up an auto-enrollment system. It’s part of the culture.

With that said, our plan sponsors and the government can learn a lot by studying retirement programs outside of the Netherlands, especially about how to encourage people to take responsibility for financial planning. How do we get consumers to take responsibility for their financial planning? That’s a real big challenge.

I also believe the industry shoulders responsibility for improving retirement outcomes. We must come up with product innovations that make it as simple as possible for participants to reach their income goals. The products may be highly sophisticated within, yet should be simple to use. I like to make the comparison to an iPhone. You don’t need to know exactly how it works; you simply need to understand what it does and have the confidence to use it. That’s what people need in retirement solutions. For the Dutch market, that will place us somewhere in the middle between DB schemes and pure DC programs when it comes to company pensions. Just as interesting though, expected further government cutbacks will put more emphasis on private investments specifically designed for retirement.

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**Collinson:** We've seen success in the U.S. with automatic enrollment and escalation adoption rates, so we should consider automatic features as the default plan design, and plan sponsors can opt out if they choose not to offer them to their participants.

We should also address other plan design issues, such as plan leakage, especially as it relates to plan loans. Most plans offer a loan feature and even allow multiple loans. Is more than one loan at a time really necessary? Many participants who have taken a loan are at risk of not being able to pay it back within a relatively short timeframe if they are separated from service from their employer. Extending the allowable time period and offering other alternatives to participants may help them avoid defaulting on the loan and having it treated as an early withdrawal subject to taxes and penalties.

On a different note, we live in such an exciting time of globalization, technology and innovation. While the retirement systems are facing strains and challenges, we're also facing tremendous opportunities to work together around the world to learn from each other's retirement systems so that we can innovate new solutions.

**DCD:** Thank you both for your global insights.

**Solleveld:** Absolutely. Thank you.



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As of 31 December 2014 our:

- Clients include more than two-thirds the Fortune 100
- Investment professionals on staff exceed 700
- Global presence includes offices in 13 locations
- Total assets under management exceed \$1.68 trillion
- DC assets under management over \$153.3 billion

Our PIMCO DC Practice is dedicated to promoting effective DC plan design and innovative retirement solutions. We are among the largest managers of assets in defined contribution plans, offering investment management for stable value, fixed-income, inflation protection, equity and asset allocation strategies such as target-date solutions. We also provide analytic modeling, plus can help plan sponsors identify DC consultant resources. Our team is pleased to support our clients and the broader retirement community by sharing ideas and developments for DC plans in the hopes of fostering a more secure financial future for workers. If you have any questions about the PIMCO DC Practice, please contact your PIMCO representative or email us at [pimcodcpractice@pimco.com](mailto:pimcodcpractice@pimco.com).

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