Wi$e Up Teleconference Call
Strategies for a Secure Retirement
July 31, 2006
Speaker 2 – Martha Priddy Patterson

Jane Walstedt: Now I’m going to turn the program over to Cornelia Moore, the Women’s Bureau Regional Administrator for our New York and Philadelphia regions to introduce our second speaker. Cornelia--

Cornelia Moore: Thank you, Jane.

It is my pleasure to introduce Martha Priddy Patterson, Director of Deloitte Consulting, LLP’s, Human Capital Practice.

Miss Patterson is a lawyer who has spent almost a quarter of a century working with major employers on retirement and health care benefit plan designs and compliance issues. In that role, she closely follows the work of the U.S. Department of Labor’s Employee Benefits Security Administration.

Miss Patterson considers her most important achievement or significant achievement to be her work done largely outside the workplace in educating women about the importance of saving for retirement, how to do so most effectively, the various rules surrounding retirement savings, and the unique challenges many women face in building retirement savings and benefits.


Miss Patterson is a graduate of the University of Texas [School] of Law and Vanderbilt University. She’s a member of the Bars of the State of Texas and the District of Columbia, the U.S. Supreme Court and the U.S. Court of Appeals for the D.C. Circuit.

She also serves on the Board of the Pension Research Council and is a member of the American College of Employee Benefits Counsel. She is the Contributing Editor of *The 401(k) Handbook*, published by Thompson Publishing Group.

Please join me in welcoming Martha.

**Martha Priddy Patterson:** Thank you, Miss Moore, I really appreciate that introduction.

I’m going to talk a little bit about the role of Social Security and employee benefits in building retirement security. This has got to be a very high level overview, as you can imagine.

But generally speaking, **when we talk or think about retirement savings, we think of the three-legged stool** in building for retirement security, and **those three legs are your own savings**, which will
always be the most important in many ways; Social Security; and employer-provided retirement benefits.

So let’s start with Social Security, because I think it’s important that you remember when you are working and you’re paying your Social Security taxes and your employer is paying Social Security taxes, you’re already covered by two important Social Security benefits, and [those are] disability benefits and survivor benefits.

So if you became disabled while you were still in your working years, you would have some disability income from Social Security. This is very important even for young workers because 20-year olds have about a 30% chance of becoming disabled sometime during their working lives.

Generally, you’re eligible for this benefit if you’ve worked for 40 quarters, and that number is actually reduced for younger employees. So if you’ve been in the work force less than 40 quarters or 10 years, you would still be eligible for disability benefits. That’s, I think, very important. You can find the disability benefit calculators, by the way, on the Social Security Web site, and that’s www.socialsecurity.gov/planners/calculators.htm.

Now you should also be aware of the survivor benefits that Social Security would provide. So, worst case, you or your spouse die before retirement age and you have children who are age 18 or younger. They will receive a benefit from Social Security so that you will have some additional income, and this is extremely important. I can tell you from personal experience because my father died when I was seven, the Social Security benefits were very important.
Then of course, what we always think about in Social Security is retirement age and the benefit you’ll receive while you’re retired. For most of you on this call, whom I suspect were born after 1960, you will need to be about age 67 before you can qualify for full Social Security benefits, but you may retire and start getting benefits as early as age 62. You will just simply have a reduced benefit, and, unfortunately, it will be reduced for as long as you receive Social Security, not just until you reach your full Social Security retirement age.

The value of those benefits will be based on the amount of money that you paid into the system and the number of years that you worked. So generally, you’ll have to work for at least 40 quarters or 10 years to be eligible to get any [Social Security] benefits in retirement. The more quarters you work, the higher your benefit is going to be, and your benefit will also be based on your highest 35 years of compensation. So those early years that you might have worked and earned very little will be dropped out and you’ll just count the 35 highest.

So that’s a 30,000-foot view of Social Security. Let’s move on to employer-provided retirement benefits.

Now, the employer-provided retirement benefits I’m going to be talking about here are those provided by private employers, companies, et cetera. The rules are a little different – or the benefit plans are different for state and local governments and for Federal government employees and for some non-profit [employees].

So these will be general rules that apply to most employers, but not all. And we really talk in broad terms about two different kinds of plans. [One is] what’s called a defined contribution plan. And that [the
defined contribution plan] simply means that there is a pot of money there. It is what it is when you retire. If it is $125,000, that’s what you’ve got to live on for the rest of your life, so to speak, unless you’ve got other benefits, which we hope you have, or other retirement savings.

[Defined contribution plans do not guarantee a specified amount for retirement. The amount you have available in the plan to help fund your retirement will depend on how long you participate in the plan, how much you and possibly your employer contribute to it, and how well the investments the contributions are put into do over the years.]

And the other major type of employer-provided retirement plans [is] what we call defined benefit pension plans, what most people call real “pensions.”

Now, the great thing about a [defined benefit] pension plan is that it is paid out to you once you retire based on your eligibility and your age. The normal form of benefit is a monthly amount you continue to receive for as long as you live and, if you are married, your spouse can continue to receive those benefits until the spouse dies.

So that is a very important feature [of a defined benefit pension plan] because you simply can’t outlive it and you don’t have to worry about making your money last. It’s there for you.

To digress for a second here. Let’s look at the real value of “compensation,” including benefits. In terms of looking at your employer’s overall [compensation] package, you need to understand and think about the fact that a $60,000 salary, for example, with no
benefits, may not be as valuable as a $50,000 salary with benefits. There are several reasons for that.

First of all, you generally will not pay any current income tax on most employer-provided benefits, but of course if you were getting salary instead, you would have to pay tax on it [the salary].

Then, if you also consider that, for example, the annual cost of employer-provided health care [premiums] in 2005 was about $4,000, of which your employer paid $3,400, you’ve also got a huge savings there. Then add on the value of any kind of employer contribution to a defined contribution [pension] plan or defined benefit [pension] plan you may receive. You’re not going to pay taxes on that either until you begin receiving those benefits in retirement.

So you can see how say a $60,000 salary that has no benefits could barely be competitive with the $50,000 salary that also has health care benefits and some kind of pension benefits.

So always think in terms of your total compensation package, not just the amount of money that you actually see. And I realize it’s sometimes hard to do that because deferred gratification is an issue for all of us. [Kiplinger’s Personal Finance has a “Job Assessor,” which allows you to rate the importance of various criteria on a scale of 0 to 100. The criteria include cash compensation and benefits, among others. The Job Assessor can be found at http://kiplinger.salary.com/jobassessor/layoutscripts/joel_start.asp.]

Let’s talk first about, specifically, 401(k) plans because they are the most popular kind of defined contribution plan. [For a description of defined contribution plans and defined benefit plans, see page 18 of]
In order to get this benefit, you’re contributing your own money. You have it taken out from your pay each pay cycle, but you’re usually doing this with dollars that are not currently taxable, so you’re going to save on your current taxes.

Once you retire, you begin to take that money [out of the 401(k) account] and you will pay taxes on that amount of money, but you’ve had it in that account to build up on a “tax-deferred” basis [i.e. you don’t pay tax on the money until you withdraw it] for hopefully decades, and it really makes a difference when you’re saving on a tax-deferred versus a taxable basis each month.

It’s also important to know that a lot of employers will also match any contribution that you make to the 401(k). About half of [employers] do [offer a matching contribution]. When they do that, they impose what we call “vesting” rules, and no, that’s not anything to do with a three-piece suit. It is the idea that you must work for them for a certain amount of time—typically three to five years—before you actually own the employer’s portion of the contribution. You always own your own money [contributions]. So that’s another important thing to remember.

Many employers now allow you to choose among investment options. I would say virtually all of them [do]. And when Kevin Huff begins to talk with you, he’ll talk about some of the various options that you might see in an employer plan. You also have the ability in some 401(k) plans or defined contribution plans to actually withdraw the
money from time to time for hardships, or some plans will allow you to borrow against the money at low interest rates.

So that is another important source of your emergency fund, for example, that Miss Martindale was referring to, and another advantage of these 401(k) plans.

You’ll also hear about profit sharing plans. They are very much like 401(k) plans. It’s the employer who’s putting in the money, and the employer may contribute one year and if [the employer] doesn’t have profits, the next year not contribute. So those are much [less predictable] than your own savings, but good plans to be part of at any rate.

When you leave the employer, your 401(k) money can be rolled over [in]to an IRA [Individual Retirement Arrangement] or, if [your new] employer’s plan will accept [401(k) transfers], you could roll it over into that new employer’s plan.

The other sort of defined contribution [plan] you will hear about is something called an employee stock ownership plan or ESOP. Now ESOPs are a good thing as long as the employer is giving you stock in the company [the employer’s company]. There’s no reason to turn that down. I would caution though that if you have an option in your 401(k) plan of buying employer stock, and you’ve also got an employee stock ownership plan, I would be very careful about investing a lot of money in the employer’s plan.

Jane Walstedt: Martha, let me just give you a time check. It’s already 2:30.

Martha Priddy Patterson: Okay.
Jane Walstedt: So we’re running a little over.

Martha Priddy Patterson: All right.

Jane Walstedt: I know you're still going to talk about IRAs.

Martha Priddy Patterson: I think that we’ll just go over those very quickly. You can contribute your own money [to an IRA] as long as you’re earning money. That’s $4,000 this year [the maximum amount you can contribute]. Next year it will be $5,000. If you’re over 50, you can contribute [as much as] another thousand dollars [per year] for what’s called a “catch-up contribution.” And, just briefly, in terms of spousal IRAs, when you’re not working and you’re married, your spouse can contribute for you.

So with that, I will turn it back to Jane and we’ll go from there.

Jane Walstedt: Thank you very much, Martha. I should have said Individual Retirement [Arrangement] instead of IRA. That’s what IRA stands for, for any of you who may not know that.

And a couple of questions or comments came up during your remarks, but I will save them for the question and answer portion so that we can get on to Kevin, but I thank you very much for telling us the different types of pension or retirement plans.