Article from

Retirement Section News

February 2018

Issue 94

ERISA Advisory Council

AUGUST 23, 2017

Written Statement On Mandated Disclosure for Retirement Plans—Enhancing Effectiveness for Participants and Sponsors

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Editor's Note: The RSN *has decided to reprint the presentation Carol Bogosian made to the ERISA Advisory Council. This statement aimed at giving observation to the council on some of the research sponsored by the SOA.*

On behalf of the Society of Actuaries (SOA) and myself, I would like to thank you for the opportunity to present observations from research sponsored by the SOA. The following is a summary of the research conducted with pre-retirees and retirees on their perception and management of risks in retirement. The information is presented to inform the ERISA Advisory Council on their review of "Mandated Disclosure for Retirement Plans—Enhancing Effectiveness for Participants and Sponsors."

SOA POST-RETIREMENT NEEDS AND RISKS RESEARCH

The SOA Committee on Post-Retirement Needs and Risks (CPRNR) has been working for nearly 20 years to identify and understand the way Americans manage their finances post-retirement. This work includes eight biennial surveys of the public's knowledge and perceptions about post-retirement needs and risk management. A major finding from this work is that planning often tends to be short term and cash flow focused, and that many people do not focus on risk or plan for shocks.

In 2015, the SOA-sponsored retirement risk research consisted of three components: a Survey of Post-Retirement Risk and the Process of Retirement (surveying U.S. pre-retirees and retirees), focus groups looking at experiences of U.S. and Canadian individuals who had been retired 15 years or more and were resource constrained in the amount of assets and regular income they had in retirement, and in-depth interviews with caregivers of people who need substantial care and would not have generally fit into the focus group population.

In 2013, the SOA sponsored a series of focus groups with people who had retired in the prior 10 years and who self-described they chose to retire (i.e., not forced to retire due to health, disability or job loss) and were resource constrained in the amount of assets and regular income they had in retirement. The study discovered a lack of planning and a general tendency to adjust to events as they occur.

The research of the CPRNR can be obtained from the SOA website at *https://www.soa.org/research/topics/research-post-retirement-needs-and-risks/*. The research findings presented in this article are taken from reports found in the tab for Retirement Risk Survey Series.

FINDINGS FROM THE RESEARCH

When people are planning for retirement, many risks in retirement must be considered. Three key items that are basic to retirement planning are to plan for a long time horizon (i.e., to end of life), to consider daily expenses along with other non-daily expenses that will most likely occur, and to have sufficient assets and income to cover these items. Based on the survey and personal responses in interviews and focus groups, the research documented the following items of concern:

- Planning for retirement is short term and cash-flow focused:
  - Three top concerns consistently appear, namely, inflation, health care expenses and long-term care expenses—although planning for these is not necessarily considered.
  - Retirees retired at a median age 60, but pre-retirees expect to retire at a median age 65—creating a gap in knowledge between the groups.
  - Planning horizons of a median 10 years are short for a retiree's potential longevity.
  - Risk management strategies for retirees are to reduce their spending, increase their savings and pay off debt.
- Financial shocks and unexpected expenses are not fully considered in their planning:
  - Home repairs and major dental expenses are unexpected expenses most mentioned—both of which could be expected.
  - The rising costs of housing, especially taxes and upkeep, are also mentioned.
  - Multiple shocks accumulate to a bigger problem than a single shock—the effect of shocks may take time before they create a crisis in living standards.
  - Due to financial shocks, the research indicates:
    - Assets were significantly reduced for one-third of the retirees.
    - Spending was significantly reduced for one-tenth of the retirees.
  - Very few have emergency funds set aside for unexpected expenses:
    - About one-fifth could not spend more than $1,000 without harming their security.
- Retirees are resilient:
  - At least three-fourths of retirees were able to manage somewhat in their new financial constraints.
  - Long-term care and divorce were shocks that caused the most significant issue.
  - Children needing longer-term support was also a major issue.

HOW RETIREES MAKE DECISIONS

As mentioned previously, retirees are resilient and attempt to manage within their financial constraints. Some of the ways they manage are:

- They carefully manage regular expenses—many considered themselves to be thrifty and frugal and manage to their "needs" more than their "wants."
- They attempt to live from regular income (annuities, Social Security and investment income) and spend their Required Minimum Distributions.
- They do not want to spend down their assets—spending their Required Minimum Distributions was not considered spending down their assets.
- They adjust to events as they occur and reduce spending if needed to preserve assets.

DEFICIENCIES RETIREES ARE FACING

Retirees may hold some misperceptions about retirement security. A decline in their cognitive abilities as they age may serve to complicate these misperceptions and the issue of retirement security more. The SOA-sponsored research on this topic indicates there are gaps in knowledge and is summarized as follows:

- Retirees may save too little before retiring and create the need to rely more on Social Security.
- Retirees may underestimate how much money is needed for retirement. Often retirees conduct very little or ineffective analysis of their finances before deciding to retire.
- Retirees may underestimate their longevity and plan for a shorter time horizon than their expected lifetime. Thus they risk living longer than they planned and a potential crisis in their living standard later in life.
- Most retirees are self-insuring for a long life. They do not purchase annuities to protect their income, or insure, or consider the costs of living assistance and long-term care.
- Many retirees do not fully plan for income and expenses throughout their retirement in one or more of the following ways:
  - Only basic living costs are fully considered and inflation may not be included in their planning.
  - Emergency funds are lacking and unexpected expenses may not be included in their planning.
  - Reliance on Social Security plus Minimum Required Distributions becomes their default income plan.
  - While they desire to preserve their assets, they do not have a real plan in place to do so.
  - Some are spending retirement assets on children and grandchildren without considering their own long-term needs.
- Many do not have the financial literacy to handle managing finances over the long term:
  - Many lack an understanding of investing for income over long periods of time, and many retirees lack basic math skills to understand investing concepts.
  - Many lack understanding of asset allocation and investment risks.
  - Many lack a basic understanding of annuity products and the annuity marketplace.

EFFECT ON EMPLOYEE COMMUNICATIONS AND DISCLOSURES

The views and opinions expressed in this section are based on my own perspective only and are not statements of nor endorsed by the SOA as a whole.

Based on my experience, the following are some ideas that I personally have to aid employers and regulators in designing employee communication programs and plan disclosures.

- The material needs to be part of a broader approach to financial wellness. In designing and positioning the material, employers could:
  - Position the SPD and other employee communication as part of financial wellness education
  - Improve the financial analysis of people before they choose to retire, to allow for them to better plan and prepare for retirement
  - Consider the level of knowledge and misperceptions of the intended audience—documents written in a manner that alludes their level of knowledge are ineffective and similar to reading in a foreign language
- Plan material should emphasize the benefits claiming decisions with the intentions of making people think more about how and when they are choosing their benefits:
  - Consider education on Social Security and benefit claiming options
  - Educate on need for reliable income in retirement and annuities as an option
- Communications should encourage long-term planning:
  - Emphasize the need to start saving early and increasing saving over time
  - Integrate other monies held by participants into the planning process
  - Discuss longevity and planning for a longer horizon
- Communication should encourage people to set aside emergency funds beyond saving for retirement:
  - Educate on the effects on retirement income of borrowing from their retirement assets
  - Educate on the effects on retirement income of withdrawing and spending their retirement assets

I encourage you to review this research and am available to discuss this information and to assist you in locating other information from the CPRNR research. ■

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The ERISA Advisory Council on Employee Welfare and Pension Benefit Plans is an advisory council to the Secretary of the U.S. Department of Labor (DOL). The council provides recommendations with regard to the Secretary's functions under ERISA, the major U.S. federal legislation governing employee benefit plans. Council members are selected from the public and they seek input from a wide variety of stakeholders on issues of importance to the Department.