Signals, Retirement Options, Phased Retirement and Retirement Decisions

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Abstract

Success in retirement depends on building enough resources, not retiring until we have enough and managing assets well after retirement. This paper focuses on when and how we retire. How and when to retire is a complex decision influenced by different kinds of signals. This paper focuses on new knowledge about signals and how they interact with retirement decisions. The paper demonstrates how the age at retirement influences retirement security. The primary focus of the paper is how individuals deal with the system today, and system improvement is a secondary focus. Society of Actuaries (SOA) and other research is used to support the discussion.

Introduction

Many years ago, when I was working to earn an MBA from the University of Chicago, I took labor economics from a very well known labor economist. At the time I had substantial experience working as an actuary including several years of pension consulting. The professor tried to teach me (and the rest of the class) that individuals take jobs early in life by calculating the value of their future wages and benefits including pensions and maximizing this present value. We had repeated disagreements on this topic as I indicated that virtually no one could do this, and that benefits managers at our clients could not do it either. We left at the end of the term without either one of us changing perspectives about how economic analysis affects human behavior. During that period, retirement had become a well established part of the American dream, and middle class Americans generally looked forward to a retirement of leisure. Retirement security for Americans was generally assumed and not a subject in the news very much.

That was more than 20 years ago, and in the last decade, a lot has changed. Retirement is in the news a lot, and there is a great deal of concern about insecurity in retirement. While many people will have a secure retirement, many other Americans will not; and being middle class during working years does not ensure retirement security. In part this is due to the way individuals respond to programs that require individual responsibility and personal savings. Many Americans do not do well with the decisions that are needed. There are emerging insights about that response as a different academic discipline has been applied to understanding human behavior and decisions. This discipline of behavioral finance focuses on how people behave. Richard H. Thaler and Cass R. Sunstein, in “Nudge—Improving Decisions about Health, Wealth and Happiness,”[1] provide a very different analysis of how individuals make decisions. They differentiate between Humans and Econs. They introduced me to the formal idea of choice architecture. In my labor economics class, we learned that all humans can be expected to act like Econs. In Nudge, we learned that it is now accepted that Humans make decisions in very different ways. Behavioral finance tells us that:

- Inertia is a very important factor, and default options are much more likely to be chosen than other options. Defaults are more likely to be chosen whether the decision is trivial or very important.
- Nudges can be very important in driving human behavior.
- Framing matters—the design of the range of options will push people in different directions.
- Where there are two options and combinations are allowed, 50 percent - 50 percent is a likely choice.
- Where there are many choices, people do not choose well. Too many choices are bewildering to the chooser, and often it is difficult to understand the implications of the alternatives.
- Decision framing and choice architecture influence many different types of decisions.

We have learned from the SOA research on post-retirement needs and risks that many people have misperceptions and misunderstandings about retirement risk, and that they tend to think short term.[2] Public confidence about personal retirement security exceeds the reality of the assets being accumulated for many. We have learned from behavioral finance that we need to consider choice architecture and how we define our choices.

I have tried to synthesize the ideas from labor economics, behavioral finance, the SOA and other research on how people perceive retirement and what they do. My conclusions are:

- The word retirement is a “Nudge” or signal. In my view a Nudge is a signal with a push attached to it.
- The words “early retirement” give people permission to move away from work they don’t like, without requiring them to do a detailed analysis of their resources and needs.

[1] Yale University Press, 2008
[2] Society of Actuaries, Public Misperceptions about Retirement Security, 2004 and Public Misperceptions about Retirement Security, Closing the Gaps, 2007 and Spending and Investing in Retirement: Is There a Strategy? 2006.

- If we start an illustration and discussion about Social Security benefits with the age of the largest monthly benefit rather than the earliest benefit, we would probably get different decisions about the age of retirement.
- Planning for retirement, particularly for the later years and longer term, is a complex task and very hard for most people.
- It is not uncommon for people to make decisions that will affect them for 25 or 30 years or more, even though their analysis does not focus on more than the next five years.
- The fact that pension plans set retirement ages at a particular age and that Social Security does not increase retirement ages beyond 67, and has not changed that provision for over 20 years, creates a "fixed retirement age" mindset rather than an expectation that retirement ages will increase with life spans.
- The signals about retirement focus more on leisure and income than on the need for income and lifetime security.
- The signals about retirement focus more on dreams than risks and risk management.

Goals and Context for the Paper

My purpose is to think about successful retirement for individuals and for society as a whole. Success in retirement depends on:

- Building enough resources.
- Not retiring until we have enough—since work is often part of retirement, the when is really "when and how."
- Managing assets well after retirement.

This paper focuses on when and how we retire, a complex set of decisions influenced by different kinds of signals. New knowledge about signals and how they interact with retirement decisions is examined. The paper demonstrates how the age at retirement influences retirement security. The primary focus of the paper is how individuals deal with the system today, and system improvement is a secondary focus. The paper is organized in several sections:

- The signals about retirement.
- Decisions about retirement.
- Creating a better future.

Why this Paper

I see a world in which life spans are increasing gradually, and the retirement system is changing a lot. We can think about the retirement system as having both spectacular successes and definite weaknesses. From an individual point of view, it can be seen as a success or failure depending on circumstances. This work is provided within the idea that we can improve the system and the result for many people.

My personal goals are societal and focus on several different outcomes:

- More individuals thinking long term and doing better personal planning for retirement, with more analysis as part of that planning.
- Financial systems, public and private, to support retirement that works without too much individual decision making. Systems that support better work options, later retirement and retirement security for as many Americans as possible. Systems designed to recognize that many individuals will not do good long-term planning.
- Better work options for third age Americans as they move toward full exit from the labor force.
- Later retirement and full exit from the labor force that gradually adjusts to changing life spans, and helps make the idea of retirement more affordable for more people.

This paper on retirement ages and options is part of a broader effort to look at signals and how they affect the retirement system. Understanding and modifying the signals about retirement ages will not bring about change directly, but it can help us to meet these goals by helping to change expectations and Nudge us toward somewhat different systems.

Signals are important in thinking about the goals because:

- They create expectations about personal choices and drive the options we consider, and sometimes override analytical planning.
- They motivate individuals and employers to consider certain types of work options, provide ideas about what is possible, and they create expectations about what a good employer should do.
- They have encouraged us not to think about the gradual increase in life spans as we move forward.
- They influence the structure of financial systems used to support retirement.

The Signals about Retirement

We can think about the signals surrounding retirement in several different ways:

- The words describing retirement.
- The provisions of the Social Security system and common pension plans.
- The advertisements and literature that are in the common press.
- Role models, peers and family.
- What is not said.

Words Describing Different Aspects of Retirement

There are many different ways to describe retirement and retirement ages. How many people are considered to have the "status of retirement" will be different if one measures receipt of benefits, labor force activity or self-definition. We can think of retirement as reflecting our sources of income, our state of mind, our activity pattern or some combination of these. We can think of retirement also as being the transition point between accumulation of assets versus use of them to supplement or replace income.

These are some of the definitions from the reports on the 2007 Risks and Process of Retirement Survey. They reflect careful crafting and show some of the issues surrounding the meaning of retirement and retirement ages:

<u>Retirement</u>—*This is generally defined as exiting from one's job or occupation, typically at an age at which the individual has no expectations of returning full-time to the labor force. For the purposes of the 2007 Survey, retirement is based on exit from a primary occupation or the self-definition of respondents.*

<u>Retiree</u>—*Traditionally, a person who, having attained a certain age—often, but not necessarily, normal retirement age—has left the labor force, with no expectation of returning. Today, many retirees leave full-time work, but continue with some work. As retirement is changing, there is no clear definition of retirement, and self-declaration of status produces varying definitions when based on labor force participation criteria. Others tend to consider themselves retired if they are collecting retirement benefits. For the purposes of the 2007 Survey, respondents were considered retirees if they classified themselves as retired in an employment status question or were employed, but responded that they had retired from a primary occupation.*

Full Retirement Age—Defined by Social Security as the age at which monthly retirement benefits are available in full without reduction for early retirement. For birth cohorts through 1937, this has been established at 65. For those born in 1938, full retirement age for Social Security is currently set at 65 years and two months, increasing an additional two months for each subsequent birth year, reaching age 66 for those born from 1943 through 1954. It increases again by two months for each subsequent birth year after 1954, reaching age 67 for those born in 1960 and after.

Normal Retirement Age—For most traditional defined benefit pension plans, this has been established as 65, the same age at which full Social Security benefits were available for birth cohorts through 1937. See also, 'Full Retirement Age.'

Phased Retirement—There is no standard agreed upon definition of phased retirement. It is used to describe such arrangements as working part-time before retirement or retiring and then taking a new job, becoming self-employed or working on a limited basis for a former employer. Viewed broadly, it may include reducing one's work schedule before retirement, changing duties at normal retirement age, working part-time in retirement or some combination of approaches to gradually phase out of the labor force. The definition of phased retirement is typically limited to situations where a partial pension payment is available or to a situation where the individual is working for the same employer as before.

The author does not totally agree with this definition of phased retirement and would include situations where the individual is working for a new employer, or phasing down without partial pension payments. This disagreement serves to illustrate that there are many nuances in these definitions and there is no consensus among experts about exactly what they mean.

Not defined in the survey reports is early retirement, a term used in many pension plans to define benefit eligibility prior to normal retirement age. Usually there is a benefit reduction to reflect the longer period of payment, but this is not true in all situations.

Note that except for the Social Security definition, which called for a gradual increase in retirement ages, ages are generally defined as a "fixed age" and they do not build in any expectation that they will gradually increase as life spans increase.

Signals from Social Security, Employers and Employer Pension Plans

Social Security tells us that people are expected to retire between 62 and 70. Age 62 is the earliest retirement age for Social Security, and there are no further benefit increases or reasons to delay claiming after age 70. If people evaluated the differences in benefits carefully, they might conclude that Social Security benefits send a signal that there is an advantage in waiting, but it appears that many do not do this. The monthly worker benefit in 2008 for a worker with maximum earnings in all years based on claiming age in 2008 is as follows:

Maximum 2008 Social Security Benefits for a Worker Initially Claiming Benefits in 2008

Claiming age	Monthly benefit
62	$1682
65	$2030
70	$2794

Social Security also tells us that work is an acceptable part of retirement. In the calendar years prior to full Social Security retirement age (about 66 now and increasing to 67), it is possible to work while receiving benefits with earnings of up to the earnings test, $13,560 in 2008, without any adjustment in benefits, and above that amount benefits are reduced $2 for every $1 earned. After the full benefit age, Social Security benefits can be claimed without any requirement with regard to future work. There is no adjustment in benefits for continued work. Note that the level of the Social Security monthly benefit is very important to the economic security of retired middle and lower income Americans. For four out of 10 older women who live alone, their Social Security benefit is virtually all that they have.

Many people feel that employers expect them to leave as they reach their early 60s. Provisions of retirement plans as well as buyouts reinforce this expectation. A recent survey tells us that if they want people to stay longer, "***Employers may just need to ask*****:** *Many retirees report they would have been open to an approach from their employer asking them to stay longer with the company. Sixty-one percent say they would have viewed the experience positively. Just 10 percent indicate they would have reacted negatively to an approach asking them to delay their retirement.*"[3]

[3] EBRI 2008 Recent Retirees Survey, Washington, D.C. This study looked at what would have encouraged recent retirees in the aerospace industry to say longer.

Employer defined benefit (DB) plans tell us that we are "expected" to retire by normal retirement age. Unlike Social Security, employer DB plans are designed to signal all or nothing retirement, and they generally do not formally support phased retirement. Most phased retirement comes either by working part-time before retirement or returning to work after retirement, either at the same employer or another employer. Early retirement age also signals that it is time to think about retirement. The normal form of payment, life income with survivor benefits for married participants, signals us about thinking about the pension plan as income replacement. Even plans with lump sums provide these signals since they communicate benefits as income.

Employer defined contribution (DC) plans tell us much less about when or whether we are expected to retire. Many of them pay benefits primarily (and in some cases only) as a lump sum. They provide a signal about retirement savings and resources, but leave much more open expectations about when to retire and about how to use funds. They make planning far more important.

Advertisements and Literature: The New Retirement

Common advertisements for financial services, retirement homes, vacations and other products are full of signals and show retirement as a continuous vacation, fishing trip or golf game. They focus on leisure and show happy, healthy people. They tend to create signals and impressions about leisure. They forget that vacation is a break from what we normally do, and that we can not be on vacation all of the time. People who retire dreaming of a permanent vacation often find they are unprepared to deal with a new set of daily realities. What was exciting as a break from work can easily become boring if it is a daily activity. Recently, experts focused on successful planning are increasing thinking about three dimensions of planning—financial, health and activities. The focus on activities considers not just leisure, but work, volunteerism, hobbies, family and building a satisfying life in the third age and beyond.

Recently, there has been a lot of focus on the literature on how retirement is changing, and on work as a part of retirement. Several books provide terminology and focus on the new retirement designed to create signals about retirement. The author notes that much of this work focuses on the early years of retirement. Some of this literature ignores the need for risk management and planning for limitations

Here are some examples:

Don't Retire, Rewire! by Jeri Sedlar and Rick Miners. The cover promises us "five steps to fulfilling work that fuels your passion, suits your personality or fills your pockets."

Portfolio Life, by David Corbett. The cover promises us "The new path to work, purpose and passion after 50."

Encore, by Marc Freedman. Freedman discusses work that matters in the second half of life, and tells stories of people in encore careers, who work both for money and the promise of work that matters.

Other books provide a longer term and more balanced approach looking at challenges and risks as well as next steps.

Project Renewment, by Bernice Bratter and Helen Dennis. This work offers a trailblazing retirement model for the generation of women just now leaving the workforce. These women were the pre-boomers and baby boomers who pioneered the new territory of women in the workplace and work-life balance. The authors emphasize the possibility of positive change, enlightenment and adventure. They also discuss challenges and more difficult-to-discuss topics such as caregiving, loss of a spouse and what to do when you no longer have your identity.

Smart Women Don't Retire, They Break Free, by Gail Rentsch. This book describes how women are reinventing their lives and careers in the second half of life.

The Quest, from Steve Vernon. This material is a retirement planning program in the form of a DVD.

There is a different twist on this topic in a paper from the Australian Institute of Actuaries titled "***It's time to abolish retirement (and here's how you do it)***" by Darren Wickman.[4] This paper focuses on the replacement of retirement by a "Lifetime Income" system that focuses on disability, not retirement, and also supports cycling in and out of work, training and leisure. Government funds

[4] Paper presented to the Institute of Actuaries of Australia Biennial Convention, September 2007.

would not be used for income replacement for people who are able to work in this approach.

The typical life cycle pattern is evolving, but retirement certainly remains part of the life cycle in the United States, Canada, Europe and many other countries. A number of people have suggested looking for a new term for the evolving pattern, and some have suggested replacing the system with a very different one. It is the author's opinion that we will never reach agreement about terminology to replace the word retirement and that further, most people won't really be able to work after age 75, so that while we might retire later, retirement is unlikely to go away.

Role Models, Peers and Family

A set of signals and expectations is created by what others do. We are particularly influenced by family, peers and publicly defined role models. An extreme example of this will serve to illustrate. During a recent trip to the Dominican Republic, a tour guide explained how the success of Sammy Sosa, a major league U.S. baseball player originally from that country, had changed the aspirations of many young people. For many of them, Sosa's success had led them to think beyond the world around them and to dream about and reach for far greater goals in life.

The impact of peers on decisions was a focus at the 2008 Retirement Research Centers Conference. One of the presenters said that this influenced his personal research agenda when he asked his mother how she decided about when to retire, and she replied that she had started out by talking with her friends. Some of the research presented was structured to explore how peers influenced individuals as they make retirement decisions. The paper "Who Determines When You Retire: Peer Effects and Retirement" finds "*Indeed, our main finding is that individual decisions about when to retire strongly correlated with the retirement timing decisions of their peers, who we defined to be retirement eligible coworkers within the same employer.*" The authors point out that this is economically logical in some situations where the circumstances are the same, but illogical in others where the circumstances are not the same.[5] They suggest further research on peer effects and their upsides and downsides.

[5] Chalmers, John M.R., University of Oregon, Johnson, Woodrow T. U.S. Securities and Exchange Commission, and Reuter, Jonathon, Boston College, "Who Determines When You Retire? Peer Effects and Retirement, presented at the 2008 Center for Retirement Research Conference.

Pictures of what we can do and be are important as we think about emerging patterns of third age activity. This is the first time in history that so many people are living to higher ages, and that people are healthy and active at these ages. For many people, family patterns before them provide no help in shaping their own third age. We need to find more role models to help us think about how to build our new lives. Several of the books referenced above are about looking at personal role models and individual stories.

Role models and examples are important for individuals but also for employers as they think about phased retirement and new job options. Employers seek out case studies:

A case study that bridges the organizational and individual perspectives is Bon Secours Health System, which uses three different approaches to phased retirement.[6]

- Employees may "retire" at age 65 but continue working part-time (not more than 24 hours per week) while collecting their full pension.
- Employees who work past age 70.5 begin receiving a pension check in April of the following year, regardless of whether they continue to work for Bon Secours.
- Employees who prefer to retire altogether may come back to work after an absence of at least three months. They continue to receive retirement benefits after they are rehired, regardless of how much they work.

Employees who choose any of the options continue to earn pension credit if they work over 1,000 hours in a year. Their benefit is then recalculated when they stop working.

Dawn Malone from Bon Secours Health System described some case studies of employees and how they had moved from job to job. Here is one example:

> *"In this next scenario, we'll look at Nettie's career. She began nursing in 1957. She worked on three units. She was one of the first "working mothers" to request flex scheduling to accommodate child care issues. Her husband was in the military and was gone for months at a time. She was originally hired to work 3 p.m. to 11 p.m. However, with small children at home and child-care issues*

[6] Rappaport, Anna and Young, Mary, Phased Retirement After the Pension Protection Act, The Conference Board, New York, 2007.

interfering with her work schedule, Nettie lobbied the Nursing Director to allow her to flex her schedule. She worked 7 a.m. to 7 p.m. for many years.

In 1975, she transferred to Employee Health. During this time, she also worked PRN evenings, and weekends on the units. This made her the first employee allowed to work in more than one cost center—another flex scheduling milestone. In 1999, she retired. Then in January 2000, she returned to work for Employee Wellness. Among other duties, she performs TB skin tests on employees. She has gradually reduced her hours since retirement. She currently works two days per week."[7]

This and several other examples made phased retirement much more understandable and demonstrated how individuals use a range of options to apply skills in different roles.

Hidden Signals—Things That Are Not Said

Since there is a lot of information provided about retirement in many different ways, there are also hidden signals that we can find in what is not said. The big gaps in the messages that I hear most often are the failure to stress the importance of making money last a lifetime, the uncertainty of life span, the fact that some people will live to age 100 and the need to think about risk protection. There is quite a lot of focus on how much one can "safely" withdraw from investments, but much less on the chance that investments will decline in value and that they will run out, or be used up for long-term care expenses, leaving the couple or, more often, the widow, with nothing but Social Security or Social Security and a house.

The gaps are aggravated because there is quite a lot of negative publicity about annuities, much of it referring to deferred variable annuities as an investment. However, the distinction between immediate and deferred annuities is often missing, as is the distinction between buying individual annuities and selecting income options in employer-sponsored plans.

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[7] Several examples are published in *Pension Section News*, the Society of Actuaries, January 2008, "Some Interesting Information About Phased Retirement," by Anna M. Rappaport. Stories based on comments made during Webcast sponsored by The Conference Board in June 2007.

Decisions about Retirement

Some of the Most Important Decisions We Will Ever Make

The decisions about when to retire and how to organize the distribution of our retirement assets are among the most important life decisions we will ever make. A related set of decisions includes whether we will continue to work on some basis as part of the retirement period.

New insights reinforce how important signals are to vital decisions. We are still learning about the balance between inertia, intuition, signals, economic analysis and risk preferences in decision making. SOA Research, Spending and Investing in Retirement concluded *"It can be argued that the decision of whether and when to retire is one of the most important financial decisions a person makes. It can easily impact a person's financial security for a period of 25 years or more. But relatively few focus group participants retired with the benefit of having undertaken a careful analysis to determine whether their funds would sustain them throughout the retirement period. And none reported that they retired after achieving a calculated (dollar) target level indicating that they could afford to retire."*[8]

These focus groups with retirees help us understand more about the decisions people make at time of retirement.[9]

> *"I thought you were supposed to retire when you were 65 and I thought I would try it."*

> *"I didn't consider how long retirement would be."*

The series of SOA surveys on Post Retirement Risk regularly has shown, as has other work, that people expect to work to older ages than the retirement ages of current retirees. Twenty-eight percent of the pre-retirees in the current survey indicate that retirement does not apply to them, and they do not seem to expect to retire.[10] Many people tell me that they will not retire, and then when I ask them if they plan to work beyond age 75, they usually say no. My impression is

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[8] LIMRA and the Society of Actuaries, Spending and Investing in Retirement: Is There a Strategy? 2006, page 6.

[9] Quotations from **Spending and Investing in Retirement,** LIMRA and Society of Actuaries, 2006. Focus groups of individuals from 2 to 10 years after retirement designed to understand decisions made about when to retire, its affordability and how money was invested in retirement. Participants had significant assets in 401(k) or similar plans.

[10] 2007 Survey of Risks and the Process of the Retirement, Society of Actuaries

that when people say they do not plan to retire, that means they plan to retire later.

Some of the things that we know about this decision are:

- People with only DC plans retire later than those who have DB plans.
- The majority of people claim Social Security benefits at the earliest possible age. Those who live to higher ages—certainly over age 90—would have been better off to wait as long as possible to claim benefits.
- In recent years, common advice provided by many financial planners and employees of Social Security was to claim benefits as early as possible.
- The majority of respondents (54%) in a recent survey in the aerospace industry considered their retirement timing for 18 months or less before they retired, and 72% considered the timing for 2 years or less. [11]
- Most of the retirees in the study of the aerospace industry did not have a good discussion about plans with their employers before they retired, and they would have been willing to stay longer if asked and if made to feel that they were valued.
- Four out of 10 older women who live alone, the majority of whom are widows, have virtually no income other than Social Security.
- It is not uncommon for people to retire without doing a longer-term financial analysis.

However, not all individuals choose when they will retire. Historically about four out of 10 people retired earlier than they chose to, and, in 2008, this had increased to five out of 10.[12] Many of the participants in the focus groups discussed above also did not choose when they would retire from their long-term jobs.

The Timing of Retirement and Why it is Important

When one decides to retire is extremely important in retirement security. There are several reasons for this:

- Medicare starts at age 65, and employer coverage often is not continued to retirees before age 65. For people in poor health, it is extremely difficult to get individual health coverage and very expensive if it is available at all.
- Social Security benefits increase with claiming age. The monthly benefit at age 70 will be about 75% larger than the benefit at age 62. While the

[11] EBRI Issue Brief No. 319, EBRI Recent Retirees Survey: Report of Findings, July 2008, page 4.
[12] EBRI Retirement Confidence Study series.

shorter period of payout offsets the higher benefit, the present value may still increase, particularly when widow's benefits are considered.

- For four out of 10 widows over age 65, Social Security is essentially the only income that they have.
- When one starts to use savings at a later age, there is a shorter period during which they need to be used. It becomes much more cost effective to buy an annuity at a higher age as well.
- When one starts to use savings at a later age, you have more years to save and more years to earn investment income.
- Added years of work usually mean more years of employer-provided health insurance coverage, which is particularly important for people who are not yet Medicare eligible.
- Added years of work for individuals who are covered by pension plans usually mean more years of pension credit. If traditional pension benefits are paid before "normal retirement age," the monthly benefits are often adjusted to reflect the fact that benefits will be paid for more years.

Research on Financial Impact of Delaying Retirement

These factors all interact. Here is an example considering several of the factors together. A Congressional Budget Office (CBO) Study, *Retirement Age and the Need for Saving*, May 2004, illustrates the impact of choosing retirement at ages 62, 66 and 70 for single persons and married couples. The age 62 couple needs 8 to 11 times annual income in assets in addition to Social Security if they are to retire and replace 80 percent of income. At age 70, the amount needed is ½ to 2 times income. Much of the difference stems from higher Social Security benefits, immediate access to Medicare, fewer years of retirement, and more time to save. This reinforces the benefit of considering both timing and needs for planning purposes.

The CBO study emphasizes the fact that the gap between what is provided by Social Security and what is needed for a reasonable level of retirement income is very large at age 62, and it gradually decreases over time as Social Security benefits provide more of what is needed.

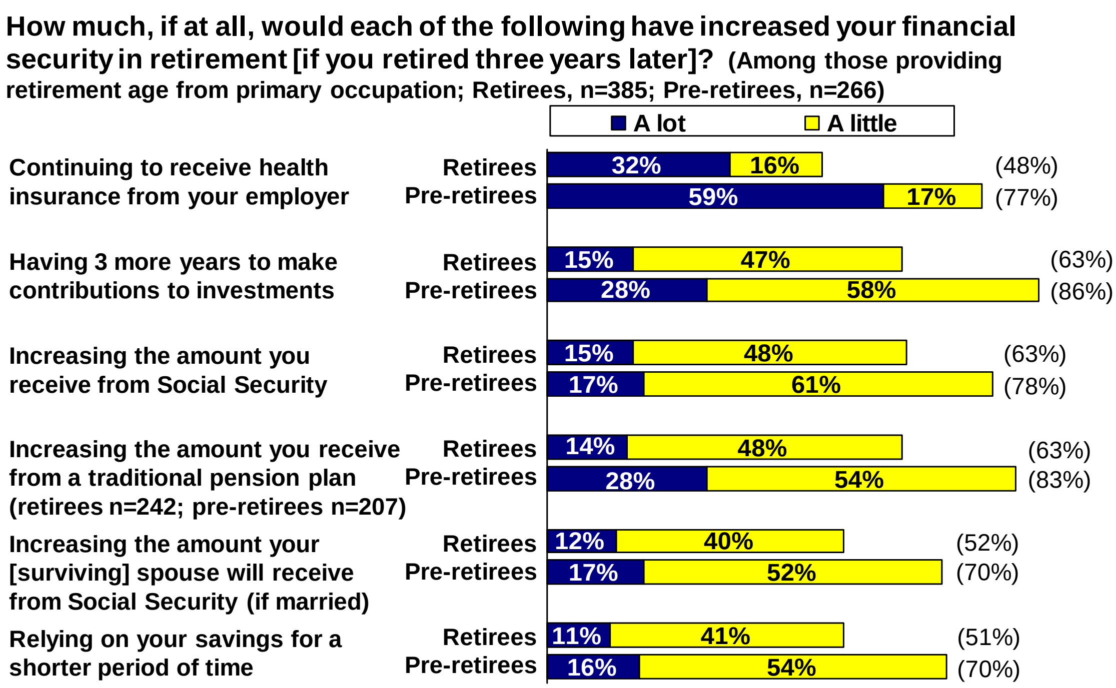
This issue is being recognized in various circles. Alicia Munnell and Steven A. Sass tell us: "Americans will need to work two to four years longer than they do at present to ensure a reasonably comfortable old age. As the average retirement age for men has been 63 for the past quarter century, they must now remain employed until their mid- to late 60s."[13]

Research on Public Knowledge about Delaying Retirement

The Society of Actuaries 2007 Risks and Process of Retirement Survey explored what the public knows about the implications of delaying retirement. In response to the question "Suppose you had retired/you were to retire three years later than you actually did/are currently planning. Do you think this would make your retirement financially….?"

	Retirees	Pre-retirees
A lot more secure	15%	14%
A little more secure	30%	54%
No more secure	51%	30%
Don't know	4%	3%

The survey went on to ask respondents how various elements of change would make them more secure if they retired three years later. Results are as shown in the following exhibit.



Source: Society of Actuaries, 2007 Risks and Process of Retirement Survey

[13]Munnell, Alicia H. and Sass, Steven A., "Working Longer: The Solution to the Retirement Income Challenge," , Brookings, 2008, page 117.

The responses indicated that the biggest expected impact among pre-retirees is continuing to receive health insurance from your employer, with 59 percent saying it would increase security a lot and 17 percent a little. The other responses that got the most attention were having three more years to make contributions to investments, with 28 percent of pre-retirees saying it would increase their security a lot and 58 percent a little; and increasing the amount you will receive from a traditional pension plan, with 28 percent saying it will increase it a lot, and 54 percent saying it will increase it a little. Pre-retirees focused on the importance of maintaining employer health insurance, but they did not place a lot of importance or differentiate very much between the impact of needing retirement assets for a shorter time and getting more Social Security or pensions at a later age.

The focus on health care coverage is very realistic since it is very difficult, expensive and sometimes impossible to buy coverage as an individual on the open market. Other research has repeatedly shown that access to health insurance is a very important factor in many individuals' decisions about when they will retire and whether to seek new work.

The responses with regard to waiting and other factors are not surprising when considered with other things that we know about public knowledge including the lack of longer-term planning, and the failure of many people to do a careful analysis of the situation. However, for most people (all but those with major health expenses), the economic impact of not needing to use retirement resources for three more years will be much greater than the value of three more years of employer-sponsored health insurance. If the respondents had done a careful analysis of the impact of the alternative factors, we would expect different responses to the survey.

Pre-retirees tend to underestimate the importance of Social Security, and the same thing shows up here. The author notes that there is no particular focus here on the surviving spouse benefit from Social Security even though four out of 10 widows have virtually nothing other than Social Security. Another question in the survey focused on the awareness of financial change on loss of a spouse. The results indicated relatively low awareness of the likely decline in economic status on widowhood.

Work Plans and the Decision Making Process

Research has repeatedly shown that many more people (often seven out of 10) say they plan to work in retirement than actually work in retirement. Therefore, work expectations are likely to be overvalued in the decision making process.

Retirement Timing and Expectations

Research also shows that people are retiring earlier than they expect to. The 2007 Risks and Process of Retirement Survey showed that once again pre-retirees expect to work longer than retirees actually did, with the results illustrating dramatic differences between the two groups for certain responses. Half of retirees retired before age 60 (52 percent), while only one in 10 pre-retirees currently in the workforce expects to retire prior to age 60 (10 percent). The largest share of pre-retirees in the workforce report they plan to retire at or after age 65 (36 percent), compared to 17 percent of the retirees who retired at 65 or older. Among those in the workforce, nearly three in 10 pre-retirees say retirement does not apply to them—in other words, they expect to never retire (28 percent).

These results show that some pre-retirees have expectations about work that will not be realized. Some will be forced to retire earlier than they expect due to poor health, lay-offs or caregiving responsibilities. Historical findings from the Retirement Confidence Survey illustrate that four to five in 10 workers retire before they had expected, while results from a 2006 LIMRA International survey indicate that six in 10 retirees had retired earlier than planned.[14]

Changing the Signals: Directions for a Better Future

So what might we do to change signals in a way that will support our goals?

- Index Social Security and private plan retirement ages or at least increase them—retirement ages that change gradually with changes in life spans would create very different expectations. Note that the American Academy of Actuaries issued a statement on Aug. 4, 2008 calling for an increase in Social Security retirement ages.

[14] Society of Actuaries, Key Findings and Issues: The Phases of Retirement and Planning for the Unexpected, 2007 Risks and Process of Retirement Survey.

- Show information about Social Security benefits by starting with the age where the monthly benefit is the largest rather than the earliest age at retirement.
- Discuss retirement as a time when wages and earnings are replaced by Social Security, pensions if any and the use of retirement assets—focus thought about retirement in terms of sources of financial support.
- Try to build a culture of analysis and improve financial literacy—encourage individuals to do more analytical work in retirement planning. Create situations where peers talk about this and where peer groups encourage it. Many tools are already available, and more are coming on the market regularly.
- Balance messages about leisure, working in retirement, new retirement with messages about risk, long life and the need for retirement income.
- Build and formalize new and creative work options for the third age—while many people work in the third age and many find new ways to work, there are relatively few formal employer programs for phased retirement or formal programs for creative work options.
- Remove and reduce barriers to phased retirement—in the United States, there are a range of barriers to phased retirement. They include complexities in pension laws and uncertainties about and barriers to the rehire of retirees. These barriers should be addressed so that phased retirement can become an accepted option.
- Change the terminology about retirement ages—while it does not seem practical to get an entirely new term, it is suggested that the terms "normal" and "early" retirement are not helpful in working toward a different world.
- Build expectations about emerging patterns of "retirement and work" in the third age—build information and case studies about what both employers and individuals are doing.
- Improve communications between employers and potential retirees so that both are aware of situations where it would be helpful for people to retire later.
- Recognize the limitations surrounding financial literacy and include appropriate defaults in programs.

Postscript

Although this paper deals primarily with the period around retirement age, the choices and resources available at that time are very influenced by what was done to save and build resources from entry into the labor force to time of retirement. The importance of saving and planning early are very important and should not be forgotten. The more that is done early, the better the options will be that are available as we reach retirement age.