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Session 9PD
Public Perceptions Of Post-Retirement Risk

Track: Retirement Systems Practice Area

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Panelists: MATT DRINKWATER†
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ANNA M. RAPPAPORT

Summary: This session discusses the results of recent studies, one sponsored by the Society of Actuaries, conducted by Mathew Greenwald & Associates and the Employee Benefits Research Institute (EBRI); and another conducted by Life Insurance Marketing and Research Association (LIMRA), focusing on public knowledge and attitudes with regard to post-retirement risks.

MS. JUDY F. ANDERSON: Our speakers are Anna Rappaport, Matt Drinkwater and Mathew Greenwald. Anna's a worldwide partner and principal with Mercer Human Resource Consulting where she consults about retirement strategy. She's concerned about employer adaptation and financial security in an aging society and is particularly concerned with the problems of women. She's a frequent writer and speaker, authors a quarterly column on post-employment benefits for compensation and benefits management and has co-edited three books from the Pension Research Council. She served as president of the Society of Actuaries from 1997-98. She was chosen as a delegate to the Saver Summit in 1998 and 2002. She chairs the SOA Committee on Post-Retirement Needs and Risks, and she chaired the SOA's June 2002 Retirement Implications of Demographic and Family Change Symposium and its predecessor, the Retirement 2000 Symposium. She's

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also on the board of the Actuarial Foundation, the Pension Research Council, the National Academy of Social Insurance, the Women's Institute for a Secure Retirement and the Metropolitan Chicago Information Center.

Matt Drinkwater heads the senior markets area within retirement research at Life Insurance Marketing and Research Association (LIMRA). His responsibilities include the deferred annuity owner and annuitization study, the retirement income management study, the in-depth annuity persistency study and the pension rollover study. He's a project director for the quarterly U.S. Annuity Persistency Survey. In addition, he's responsible for industry sales, forecasts and annuitization estimates for individual annuity market sales and asset reports. Matt has also worked on an investigation of retirement planning software in coordination with the Society of Actuaries and the International Foundation for Retirement Education. Matt joined LIMRA in 1999 and has worked on projects in both the retirement research and markets research divisions.

Mathew Greenwald established his research and consulting company, Mathew Greenwald & Associates, in June 1985. Since then he's done strategic planning and marketing research for over 100 of the most prominent financial services companies and numerous other organizations. Dr. Greenwald has a Ph.D. in sociology from Rutgers University. He served as a Congress-appointed delegate to the 1998 and 2002 White House Congressional National Summits on Retirement Savings and has also testified before the U.S. Senate Committees and the SEC. He has published numerous articles in academic journals and trade periodicals and is frequently quoted by national print, radio and television outlets, including national publications like the *New York Times*, *Wall Street Journal* and *Time* magazine. He has spoken at numerous press conferences and life insurance and other professional meetings.

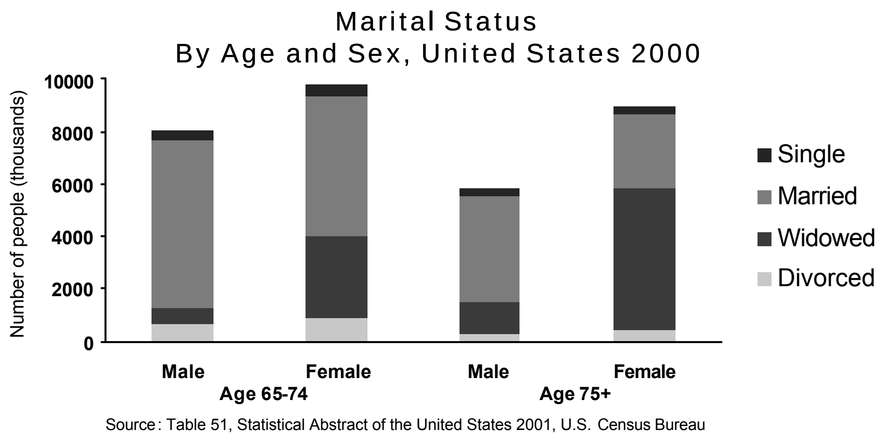
Before starting his business, Dr. Greenwald spent 12 years at the ACLI. From 1977-85 he was ACLI's Director of Social Research and was responsible for programs monitoring public attitudes towards financial issues, demographic research and futures research. He is currently an elected member of the Market Research Council, a group of the country's leading market researchers. Among the companies his firm has served are the American Bankers Association, MetLife, New York Life, Fidelity Investments and Principal Financial Group. Non-financial services and clients included AARP, the Hershey Food Corporation, National Education Association, National Geographic Society and the Smithsonian Institution Press.

ISSUES FOR RETIRMENT PLANNING

MS. ANNA RAPPAPORT: In my portion of the presentation, I am not going to present the research but present some positioning data and talk a little bit about the post-retirement period. Let's start with some key data. Figure 1 is data on U.S. marital status. We have the population by age and sex, male and female, age 65 to 74, and 75 and over. The first thing that we notice here is that there are more females than males in both age groups, and as an actuarial audience, we know that women live longer, but then if we go on and look at marital status, the biggest piece is married, and we notice there are more married males than females, and what's happening is that men frequently marry younger women.

Figure 1

US Marital Status, Age 65+



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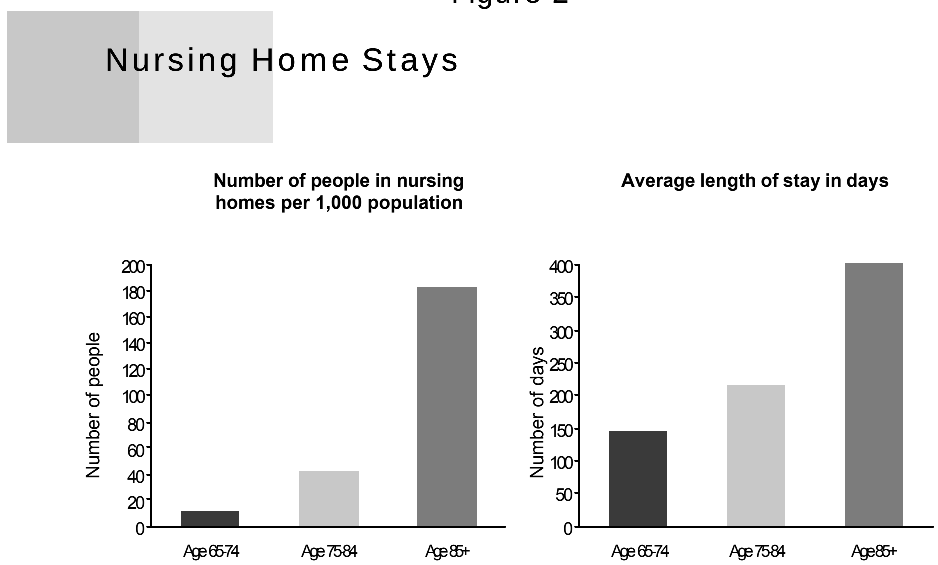
We have a lot more married males than females, and next we have widowed, and then we've got divorced at the bottom and single at the top. You notice that we have a lot more widowed females and a few more divorced females. This becomes important in thinking about the issues of post-retirement risk, which is why I've pointed it out, and particularly when you get to the 75-and-over category, that you've got many more widowed. Widowed females are by far the biggest group among the 75-and-over category. Data also shows that the economic status of the widowed females is significantly less than of married couples, which, for those of you in the life insurance industry, means you've got an opportunity, and also we're not doing a very good job. There's a lot to be done. The poverty rates are still quite high among widowed and divorced females.

We mentioned life expectancies being different, and, at age 65, females have a life expectancy of 19 years compared to 16 years for males. We've also got some data on nursing home stays. In Figure 2, the first set of data is the number of people in nursing homes per 1,000 population, 65 to 74, 75 to 84 and 85 and over, and 85 and over is where there are lots of people. The second part is lengths of stay, and the lengths of stay are much longer for the 85 and over, and this is a risk that you're going to hear data about, how people view it, and it's the females in the old group that are most likely to need the help.

Figure 2



Source: Department of Health and Human Services, Vital and Health Statistics, Series 13, N0. 152, June 2002

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I mentioned being well off. The poverty rate for married couples at age 65 and over is about 4.3 percent according to Figure 3,which is from the Office of Research Evaluation and Statistics. That's part of the Social Security Working Paper Number 87. This paper is a great source of data about the differences in economic status of men and women and their work histories and so forth. It’s a good paper that summarizes data from many sources, and I recommend it. In contrast, for unmarried women, it's over 17 percent; 16 percent for widowed and 20 percent for divorced, and I contend that this is America, and we should be able to do better than these poverty rates. This to me is a very disturbing issue.

Figure 3

Today's Elderly Women

	Poverty Rate (1999)
▪ Married	4.3%
▪ Not married	17.3
– Never married	18.9
– Widowed	15.9
– Divorced	20.4

Source: ORES Working Paper Number 87, Reducing Poverty Among Elderly Women, Table 1, 2001.

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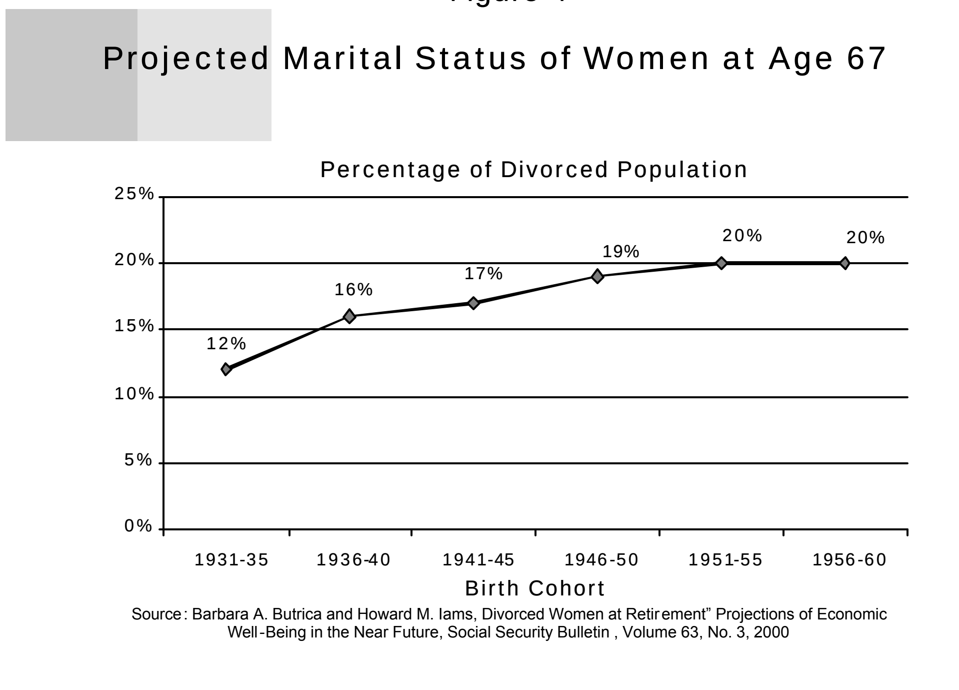
Divorce is an issue that's going to get to be a bigger issue. The problem is getting worse. In Figure 4, for people born in 1931-35, 12 percent of them are divorced at age 67, and it's projected to increase to 20 percent for people born in 1956-60. If you ask, is the issue of economic status among divorced people going away? No, it's getting worse. This data is also from work done by the Social Security Administration, and it's very good, solid work. I recommend this paper as well.

Figure 4



The second part of my introduction focuses on some of the things we need to be concerned about in the post-retirement period. For those of you that want to hear more about this, I encourage you to follow the work of the Committee on Post-Retirement Needs and Risks. We have an active multidisciplinary group working on these issues. One of the things we know about the environment is that overall it's a big issue in this country. The elderly today are much better off than they were if we look back to the past. Many more people can plan to retire. Poverty rates are lower. Health and functional status are key. As we're living longer, we are also healthy longer. The period of chronic illness is about the same. But we're paying out more benefits as lump sums, and that's true in employer plans, whether they're defined-benefit (DB) plans or defined-contribution (DC) plans.

If we were to privatize Social Security, that gets to the issue of who needs to manage post-retirement risk? We have pretty long periods of widowhood, and single women, as we saw, are less well off. We have a lot less retiree health coverage. Studies show it's dropping every year, and fewer and fewer people have retiree health, particularly after Medicare eligibility, but also before. We've changed the way we're retiring as a society, and more people are retiring and then working at least part-time after retirement, and pensions and individual savings make a big difference in how well off people will be.

Figure 5 is an overview of post-retirement risk, and you might ask how we got these numbers. We got these numbers by consensus of the Committee on Post-Retirement Needs and Risks. I can't go and point to the specific data sources. These are really based on the consensus of a group of actuaries.

The risk of outliving assets—we said the range for that risk at age 65 or the range for life spans at 65 is from zero to about 40 years, and we talk about products for risk transfer, annuities, including joint and survivor annuities. Loss of a spouse, periods of widowhood, 15 years or more are not uncommon, often accompanied by a reduction in standard of living. There may be a decline in functional status, and we had much discussion about these numbers in the committee. The cost of care on account of frailty can range from zero to over $2 million for a couple over their lifetimes. Nursing home costs may run $70,000 or more per person per year. Care can be provided at home, and, in fact, the majority of care for people who need it is provided at home by family members and adult day care, assisted living facilities or nursing homes.

Figure 5

Overview of Post-Retirement Risks

Risk	Potential Range for Risk	Products for Risk Transfer
▪ Outliving assets	▪ Life spans at age 65 range from 0 years to over 40 years.	▪ Annuities, including joint and survivor annuities
▪ Loss of a spouse	▪ Periods of widowhood of 15 years or more are not uncommon. These are often accompanied by a reduction in standard of living.	▪ Joint and survivor annuities; life insurance
▪ Decline in functional status	▪ Cost of care on account of frailty can range from $0 to over $2,000,000 for a couple over their lifetimes. Nursing home care costs may run $70,000 or more per person per year today. Care can be provided at home, in adult day care, assisted living facilities, or nursing homes.	▪ Long-term care insurance helps pay for the cost of care for the disabled. Continuing care retirement communities that provide caps on monthly costs for assisted living and skilled nursing care offer some risk protection as well.
▪ Out-of-pocket medical expenses	▪ Medical costs not covered by Medicare for retirees over age 65 can range from $0 to over $1,000,000 for a couple over their lives.	▪ Medical insurance
▪ Inflation	▪ Inflation can range from 0% in any year to 10% or more; inflation has been much higher in other countries.	▪ Products with cost-of-living adjustments ▪ Better education on investing lump sums

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Long-term-care (LTC) insurance helps pay for the cost of care for the disabled. Continuing care retirement communities that provide caps on monthly costs are another way to cover it. Continuing care retirement communities can help pay for some of the cost in assisted living and skilled nursing. This is an issue of how will we finance it? Some people can finance this from savings, and for people that have no money it's financed heavily out of Medicaid, and for the people in the middle it's a very big issue, and we're going to hear data on what people know about that.

Out-of-pocket medical expenses are another risk. Medical care not covered by Medicare could range from nothing to a whole lot, particularly for people that need a lot of prescription drugs. We've established a limit of about a $1 million for a couple over 65 over their lives, and again the committee is comfortable with this. It was a consensus. Inflation is the last risk that we've identified in Figure 5. Presently in my committee we're doing a much larger identification of post-retirement risks, and if you watch for that, it'll be out on the Web site, I think, by the end of the year.

We need retirement assets for: basic retirement income, acute medical care (beyond what's covered by Medicare), LTC or insurance to cover it and helping other family members in their retirement years. In many cases, the couple is not only caring for themselves. Many have parents to care for as they enter those years. There is also an increasing number of grandparents caring for grandchildren. Finally, retirement assets are also needed for travel, hobbies and meeting retirement dreams.

POST-RETIREMENT RISKS: HOW THEY ARE VIEWED AND MANAGED?

MR. MATT DRINKWATER: I'm going to talk with you about a study that LIMRA completed and published this year on how retirees and those people approaching and nearing retirement view post-retirement risks and some of the things they try to do to manage those risks. We'll also highlight some areas in which we feel that their perceptions of these risks depart from the actual reality of the risks and where education is probably most needed.

We looked at retirees and pre-retirees with this study. Retirees were self-defined. They just said, "Yes, I am retired." We did that rather than give a standard employment status question because it's our belief that retirement is not the same as employment status. You can be retired but still working. Retirees were between the ages of 55 and 78, and our pre-retirees were between the ages of 50 and 70, and these were people self-defined as not retired, but were going to retire within the next two years.

MS. RAPPAPORT: I just wanted to point out that as you listen to this, keep these definitions in mind because the two studies use different definitions of how the populations were drawn.

MR. DRINKWATER: We screened for those individuals in July and August of last year, and we mailed our survey in October. We waited a little bit between August and October because September 11 occurred when we were just about to send out the survey. In fact, we found that nine percent of our pre-retirees were actually planning to retire later than they originally anticipated due to the economic fallout from September 11.

We ended up receiving usable surveys for about 2,800-or-so retirees and over 500 pre-retirees. The information I'm going to be covering is only one piece of this larger survey. We have called it the Retirement Income Management Project or Retirement Issues Project. There are several reports that we're going to be working on, including retirement planning, managing retirement income, expenses and then finally post-retirement risks, which is, again, what I'll be focusing on.

There are some methodological differences between the LIMRA study and the study that Mathew Greenwald will be discussing. Our study was done through the mail. Theirs was a telephone survey. Our pre-retirees are within two years of retirement, whereas the SOA study, theirs are nonretired but age 45 or older. We had a similar set of risks that we looked at with some slight definition differences, and ours actually had a somewhat longer set of risks, though by no means as long as the list that the SOA Committee on Post-Retirement Risks and Needs is working on. And, as I just said, ours covers other issues besides post-retirement risks.

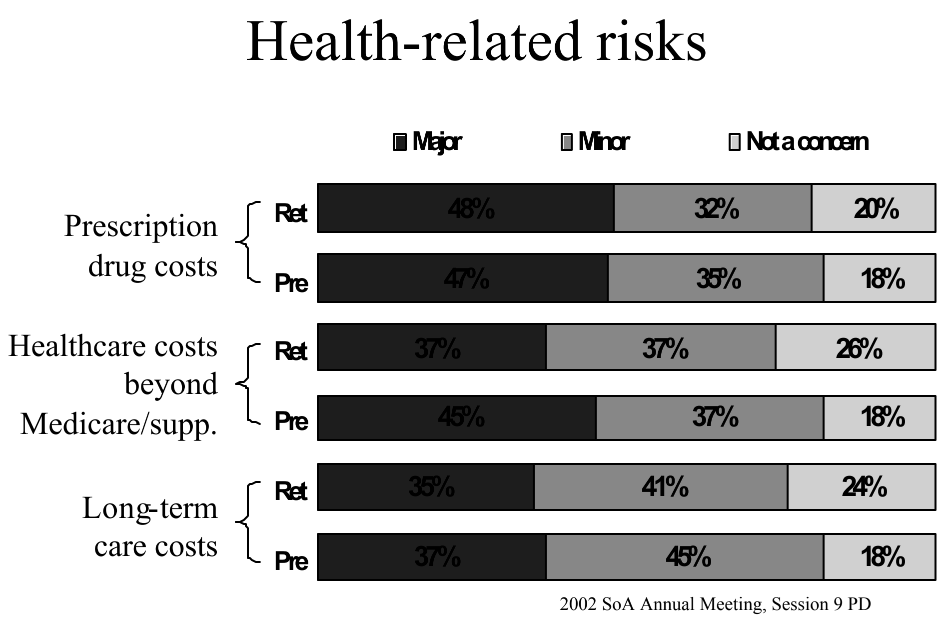
Now our questionnaire included a list of 11 items dealing with postretirement risks, and we asked our participants to "indicate their level of concern about the impact these items could have on their standard of living in retirement." That's the way we phrased it to our respondents. When we looked at that question with this list of 11 items, the results that we got back initially surprised us. We found a clear pattern in the results where we had certain groups of risks as rated most important, of lesser importance, and then not very important.

As it turns out, health-related risks were rated as causing the greatest concern about their impact on one's standard of living in retirement, followed by a set of financial risks, and the least concerning set of risks were those involving mortality and longevity. We originally felt that the mortality risks would be rated as the most important, but, as we've discovered, there are gaps between the perceptions of retirees and people approaching retirement and the realities that they face.

The more concrete risks we found were rated as more worrisome than the more abstract ones. I should also point out the fact that the risks shouldn't necessarily be seen as independent of one another. The risk of outliving one's assets, you could say, is related to the risk of inflation, for example.

The health-related risks were prescription drug costs, providing for health care costs beyond what Medicare and supplement will provide, and LTC costs. Prescription drug costs were seen as the most important risk for both retirees and pre-retirees. In Figure 6, the left-hand-most bars indicate 48 percent of retirees and, just below that, 47 percent of pre-retirees, said this is of major concern to them. Health care costs really are important to people. They're front-of-mind issues because they're current costs that people are facing. They're not abstract future events. The cost of prescription drugs in particular has been receiving a lot of attention lately. We've seen that in the ads on TV, particularly this election year; we've been inundated with these ads, and a lot of them mention prescription drug coverage.

Figure 6

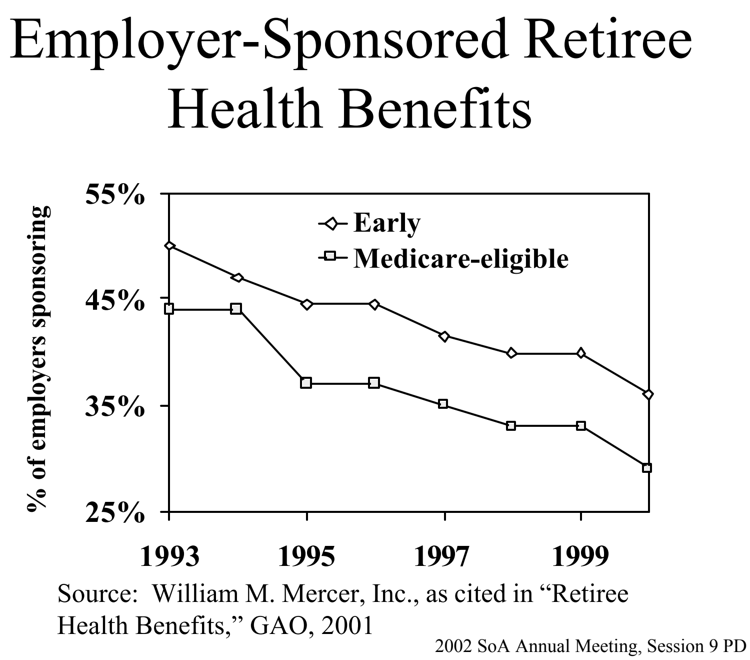


Health care costs beyond Medicare, Medicare Supplement, were also a major cause for concern, more so for pre-retirees than retirees; 45 percent to 37 percent. Long-term-care costs were seen as a cause for concern about equally by pre-retirees and retirees. They are concerning the people, but, as we'll see, most people aren't taking the step to address the LTC risk by purchasing LTC insurance. So perhaps they're not concerned enough.

We asked our respondents to indicate their current sources of health insurance. Most retirees in our survey, of course, were eligible for Medicare, and the 80 percent eligible for Medicare becomes 93 percent when we eliminate respondents under the age of 65. Forty-three percent also had some type of supplemental coverage, and half of all retirees in our survey currently receive some form of health insurance from their former employer, either paid in whole or in part by their former employer. Despite this level of coverage, they're still concerned about health care and drug costs. Not everything is taken care of with their current coverage. It's immediately clear to retirees what's lacking. It's not an abstract future situation.

With regard to that future situation, I just want to point out Figure 7, which is actually from a Mercer study originally, but was published in a government accounting office report last year. This looks at the percentage of employers sponsoring retiree health benefits, and, as you can see, there's been a steady decline in the percentage of retirees who can expect to receive employer-sponsored health benefits. That's true for Medicare-eligible individuals and people retiring before that. Employers have tended to reduce coverage for future rather than the current retirees, but they haven't reduced the benefits among current retirees by increasing the share of the premiums that retirees have to pay, increasing the co-payments and deductibles and capping employers' expenditures for coverage.

Figure 7



Why is this happening? Premiums are rising very fast, faster than inflation, and that's due to a variety of reasons: medical technology, a decrease in the tightly managed care that we had over the past few years and a developing nursing shortage. We have a shaky economic situation. A lot of companies are being hard hit. And, of course, we've got the baby boomers ready to retire. This promises to continue in the future, and it seems that our pre-retirees recognize that, and they're very concerned about that.

Moving on to LTC, we asked our retirees and pre-retirees if they owned LTC, and, if not, did they at least look into it? A quarter of our retirees and about a sixth of our pre-retirees say they own it. We don't believe these numbers. It's probably in the single digits according to other sources, as well as some LIMRA research. A large proportion said they didn't own it, but had looked into it, and they, for some reason, rejected it. We asked them why they don't own LTC insurance. It's too expensive, was the key reason. Perhaps it might be too expensive if you're an older retiree, but really what's going on is people tend to confuse the cost of LTC with the cost of LTC premiums. There's a difference here.

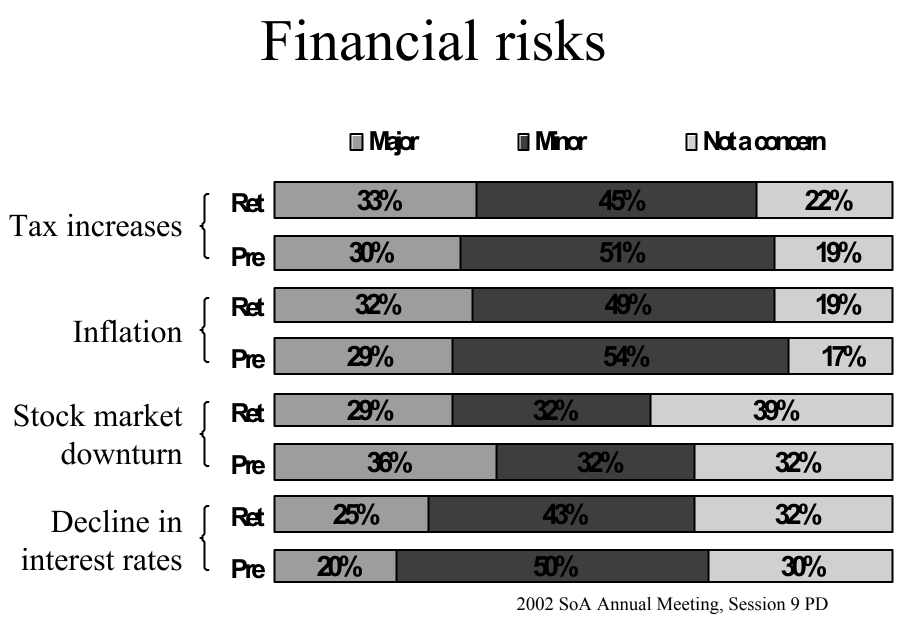
A LIMRA focus group, for example, showed that people grossly overestimate LTC insurance premiums on the magnitude of five to 10 times what the actual premium would be for a hypothetical 65-year-old male. Another reason is: "I don't need it." This is sort of the "well-it-won't-happen-to-me" group. It might not happen to you. You might not need LTC insurance, but is it really worth the risk? I could cite all sorts of statistics here. The U.S. Department of Health & Human Services says that once you reach the age of 65, you're looking at about a 40 percent lifetime risk at that point of entering a nursing home, and it's proportionally more likely for women to face that possibility.

Some people thought Medicare would pay for their LTC costs. Yes and no. It will cover skilled at-home care for short-term, unstable, medical conditions for 100 days or less. So, relying on Medicare is not going to cut it either. We asked our retirees if they thought Medicaid would pay, and 14 percent said they don't own it because Medicaid will pick it up. Medicaid will pick up the nursing home coverage, not home care, and won't pick up adult day care. You don't get to choose your own type of care, and also there are the asset requirements. You might have to spend down your assets to a certain degree.

The bottom line with these results is there's a perceived need for LTC insurance, but there's a lot of misunderstanding about these products. People don't seem to realize that they can address the risk of facing LTC costs by purchasing LTC insurance, especially in those years when it is affordable.

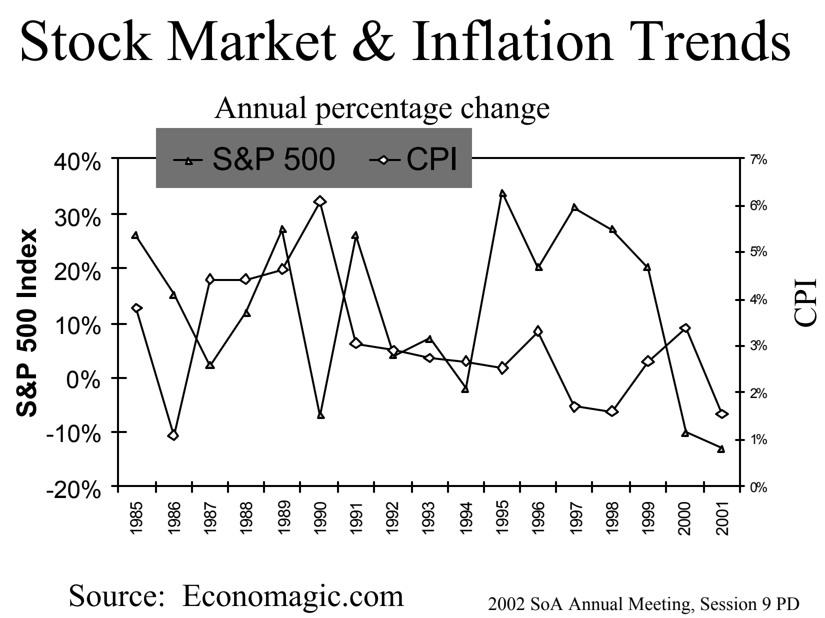
Moving on to the next group of risks, these are what we call the financial risks. The financial risks were tax increases, inflation, the risk of a prolonged stock market downturn, and a decline in interest rates. The results in Figure 8 show that generally both samples, the retirees and the pre-retirees, were worried about these risks, but, as you get down to the stock market downturn, the decline in interest rates, the level of non-concern, the right-hand-most bars, those are starting to creep up a little bit.

Figure 8



Pre-retirees are somewhat more concerned than retirees about a prolonged stock market downturn, and I'll mention one clear reason for this difference in just a moment. Figure 9 shows the year-to-year percentage change in the S&P 500 Index, and I've also put down the consumer price index (CPI), as a measure of inflation. The stock market currently, of course, is receiving a lot of attention, but we were experiencing double-digit increases from year to year for a while in the general market. It's becoming more of an issue for people, for retirees and those approaching retirement, but a lot of them have ended up overexposing themselves to the equities market. It's now a front-of-mind issue, but a few years ago they wouldn't have seen it as a risk.

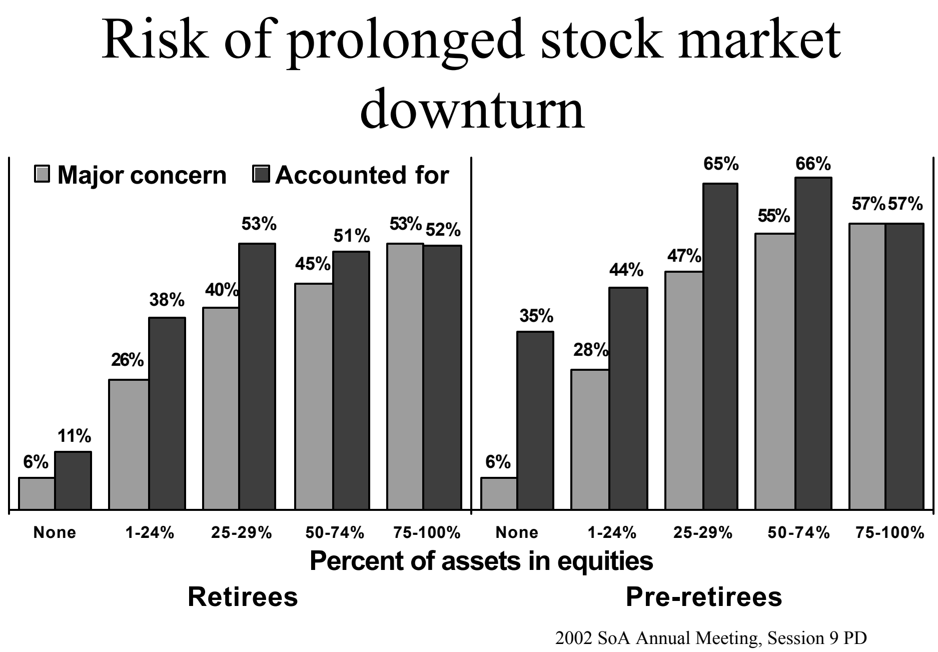
Figure 9



The inflation rate has remained fairly reasonable, but, again, there's the risk of that turning around at some point. This may have served to lull people into thinking that things will always be okay, we'll only have two or three percent inflation, but if they don't have a cost-of-living adjustment (COLA) or an inflation-indexed feature in their retirement income, they could be hurting in later years.

In Figure 10, looking at that one risk, the risk of a prolonged stock market downturn, we generally found that as the percentage of their assets invested in equities increases, we see an increase in the level of concern, which is fairly rational. Pre-retirees have more in equities, and they are more concerned, but a higher proportion of assets in equities—as the right-hand bars show—also is associated with respondents saying that they've taken it into account.

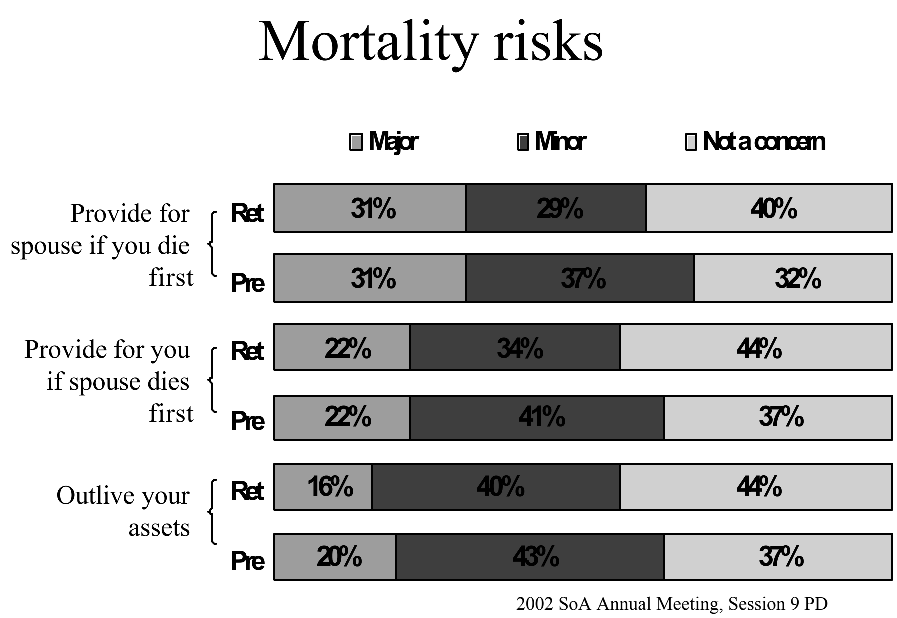
Figure 10



How can people take market risk into account to a greater degree by exposing themselves to that risk to a greater and greater degree? This might be explained in terms of demographics. There is a correlation between having a large amount of investable assets and a high percentage of those assets invested in equities. Presumably these wealthier people do have the wherewithal to deal with a market downturn, if it occurs, due to other income sources. So the riskiness of the market has been underplayed to people until very recently, and they've been left overexposed.

The mortality risks were rated as the least important to people. The three items in our survey dealing with mortality risks were a couple of spousal mortality risks, providing for your spouse if you should die first, and then the flip side, providing for you if your spouse should die first. The third mortality risk was the possibility that you or your spouse will outlive your assets. I would say that these are future events. They're more abstract to people than spending money on prescription drugs. Again, it's subject to the "it-won't-happen-to-me" phenomenon with people. You can see the results on Figure 11. Retirees and pre-retirees were more concerned for their spouses should they die first, which is interesting, and this is especially true for men.

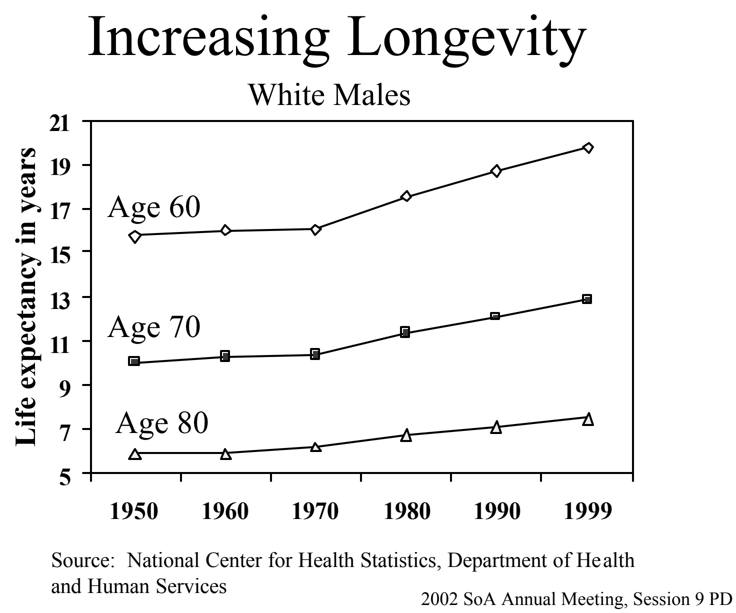
Figure 11



Traditionally, and in particular among the generations we're looking at here, men have more and greater sources of income in retirement than women. If they were to die first, the widow's standard of living could drop much more severely than if the reverse situation had occurred. I would also urge you to keep in mind the nonfinancial risks of widowhood. If the husband is the one that, for example, deals with the finances, he's the money manager, and he dies, how does the widow then go ahead and pick up all of these tasks that he was taking care of, dealing with investments, insurance policies and so on?

People are living longer than they did 50 to 100 years ago. As you can see in Figure 12, there have been more recent gains in longevity in those older ages. You can see that the slope of the lines increases somewhat after 1970. White males now live for an average of 20 years or so after they hit age 60. Women live a few years longer than that. Another thing to keep in mind is couples' longevity. If you have a couple where both are the same age, 65, there's about a one-in-three chance that one of them will survive to age 95.

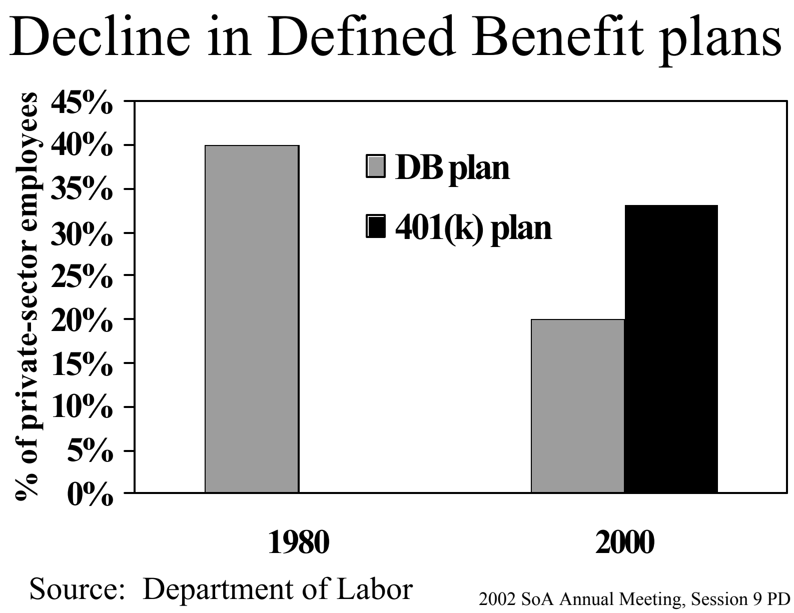
Figure 12



So, people are living longer, but, despite that fact, our retirees and pre-retirees tended to underestimate their own longevity when it was compared to an actuarial standard, in this case the Annuity 2000 Basic Table. We could use other mortality tables, but the general result is still there. They're underestimating their own life expectancy. Women, in fact, tend to be less accurate than men, and that inaccuracy has greater consequences for them than it would for men.

Given that people underestimate their life expectancy, how can the risk of outliving their savings be addressed? In the past, traditionally one way is done through the DB pension plan which offers lifetime income and sometimes with a COLA, but as you can see in Figure 13, we've seen a decline in the DB plan over the past 20 years, and we've seen just an explosion of money flowing into DC plans, such as the 401(k), which went from almost nothing—it was originated in 1980—to having more employees involved in one than DB plans. What does this mean? This creates a greater opportunity for lump-sum distributions from these plans. You're not taking the money in a form of annuitized income. Then you have rollovers into IRAs, and when you do that, the spousal guarantees are lost. The spousal guarantees are usually built into the DB plans, though, of course, the money from those IRAs can be inherited.

Figure 13



With the DB plans on the decline, another important way to address the mortality and longevity risks is through individual annuities. Figure 14 shows some data from LIMRA sales surveys, and when you look at the annuitization rate you find that there's a bit of variability, but the trend is not promising. It went from 0.9 percent of all individual annuity assets annuitized in 1997 to .7 percent in 2001. The sale of immediate annuities has been mostly flat, although within that the variable immediate annuity market has picked up, but in total we're seeing $14 billion annuitized—that's very small potatoes when you consider that there's about $1.4 trillion in annuity assets, and we have sales of about $200 billion or so each year.

Figure 14

Using annuities for income

	1997	1998	1999	2000	2001
Annuitization rate	**0.9%**	**0.8%**	**0.7%**	**1.0%**	**0.7%**
Annuitizations ($ bil)	**$ 9.2**	**$ 9.4**	**$ 9.8**	**$13.9**	**$9.6**
Immediate annuities ($ bil)	**3.0**	**2.4**	**2.9**	**3.8**	**4.3**
Total	**$12.2**	**$11.8**	**$12.7**	**$17.7**	**$13.9**

Source: LIMRA International

2002 SoA Annual Meeting, Session 9 PD

Even when people buy an annuity and they annuitize, they're not always addressing these postretirement risks when they do so. LIMRA is in the process of doing an annuitization study that looks at both annuitizations and newly bought, immediate annuities in the years 2000 and 2001. These are somewhat preliminary results, but we're finding that fewer than half of these people are choosing a lifetime income payout. Most are choosing the period-certain only. That, of course, leaves most people without the guaranteed income that's such a crucial feature to an annuity. Why is this happening?

There are all sorts of reasons I won't get into for the reticence to annuitize, but one reason is that people are thinking in terms of return on the dollar. Am I going to get that money back? Throw in a period-certain feature. That gives them that piece of mind, but I'm not sure if that really adequately addresses the longevity risk, the postretirement risk that we're focusing on here. The joint and last survivor option or type of annuity is not very popular. Our annuitization study shows that just over 20 percent chose this income option in 2000 and 2001. It's a relatively small percentage.

The bottom line here is that the products out there that address these risks exist, but they're not being utilized to the extent that they could or really should be, and, as with LTC insurance, there's a real need to educate them about the need for the products as well as the products themselves. LIMRA focus gro ups showed that once the concept of annuitization of lifetime income was adequately explained to the members of the focus group, retirees were interested and receptive. There is hope. They're initially hostile to the idea, but a little explanation goes a long way.

Finally, there are some other information sources to consider. The LIMRA research is available on LIMRA online for those of you who work at LIMRA member companies. The Opportunities in the Pension Rollover Market study discusses what people do with their lump-sum eligible set of money that they have with their employer-sponsored plans, whether DC or DB. What do they end up doing with that? In a nutshell, they're not taking annuitized income from it. Also, the MetLife crossroads study that just came out this year looks at guaranteed sources of income and how that relates to people's perceptions of retirement. It's a very interesting study. The EBRI retirement confidence survey and health confidence survey is very good. And the SOA Retirement Needs Framework (2000) is an extremely good source of information for many of these risks we're covering today.

SOCIETY OF ACTUARIES 2001 RETIREMENT RISK SURVEY

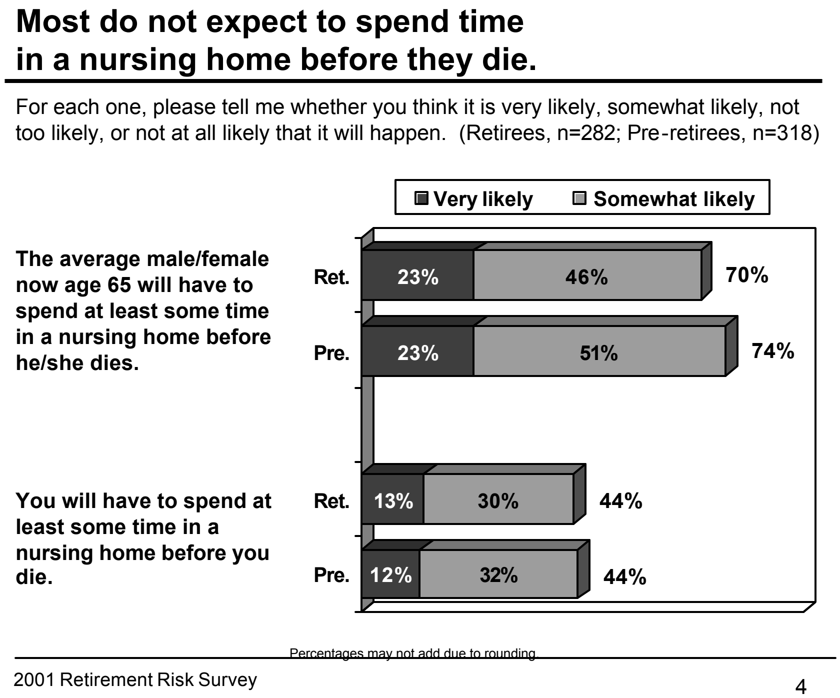
MR. MATHEW GREENWALD: I'm here to talk about a survey that was supervised by the Committee on Post-Retirement Needs and Risks of the Society of Actuaries and funded by the Society of Actuaries, and it is similar in a lot of ways to the LIMRA work, but it is also different in some ways, and I think it gives us some added insights.

Our survey was conducted by telephone. We surveyed 600 people who were born after 1956, who were ages 45 and above in August 2001 when we conducted the survey, and we partnered with EBRI in working on it under the supervision of the committee of the SOA. There are three goals I have in presenting this information to you. The first one is to try to quantify the low awareness of risk, the low skills the people have in this group, ages 45 and above, in dealing with the risk. Second, we have some insights into why people are doing what they're doing. And, third, this study represents, I believe, a benchmark to measure change because we hope that change will come, and it seems to me some of the work of the Society will lead to change in a more positive adaptation to longer life and greater exposure to the risks of a longer retirement.

MS. RAPPAPORT: We are planning to repeat the study next year and are hoping to do it on a regular two-year cycle so we will have some trend data.

MR. GREENWALD: In Figure 15, an important point is illustrated by the question: If the person is male/female, now age 65, how likely is it that the average male/female (not themselves) will have to spend at least some time in a nursing home before he or she dies. You see that about seven in 10 people think that's at least somewhat likely. By the way, we took our population of age 45 and above, and we asked people if they're retired or working, and that's how we got to retirees, and, if they were working, hopefully pre-retirees.

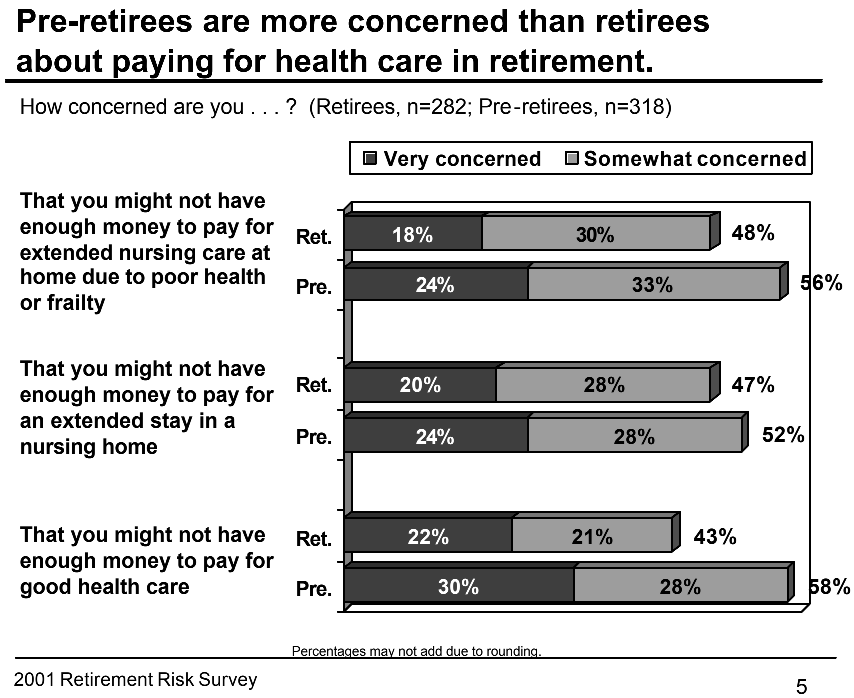
Figure 15



Then we asked these same people: What about you? How likely is it that you will have to spend at least some time in a nursing home before you die? You see that the percentage is far less. One way of putting it is most people think they're above average, and there's a certain element of denial that illustrates why people can look at what the risks are in general for the population overall but are resistant to the fact that it will happen to them, whether it's wishful thinking, denial or whatever. This is an important point that explains some of the behavior that's now going on.

Another aspect of this is the lower level of concern about all aspects of LTC versus health. It's interesting that people are more protected against health costs by Medicare at age 65 and over than they are against LTC costs, but if you look at the lowest group of bars in Figure 16, concern that they might not have enough money to pay for good health care is higher than concern that they might not have enough money to pay for extended nursing care at home or extended stay in a nursing home. So, concern is higher about health care. It's also interesting that concern is higher for the pre-retired and younger population than it is for the retired population, and that indicates concern about the future viability of the Medicare system, which underlies some of this.

Figure 16



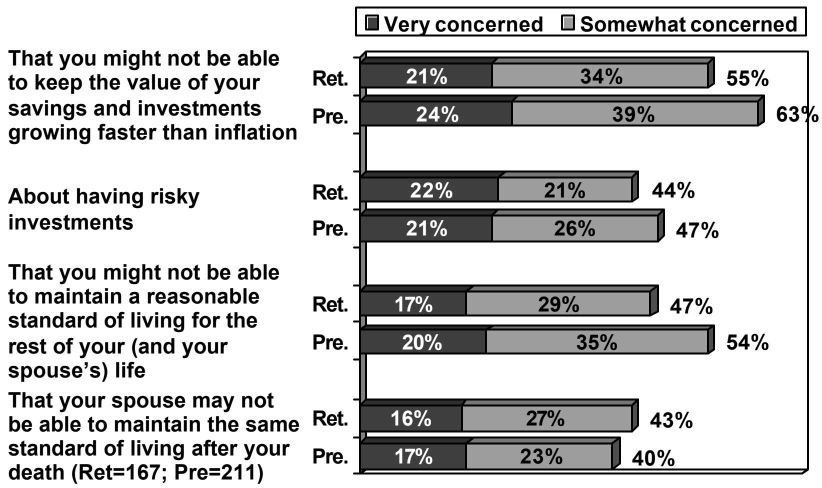
We also asked how much thought people have put into these different issues. The thing they can prepare for and put thought into is protecting financially against the risk of needing LTC because you could buy LTC insurance at an earlier age, but they're less likely to think about that than to think about something where there's less need for premature action. These are retirees. A substantial amount of thought has been put into the possible impact of large medical expenses that are not covered by Medicare. Forty-five percent have thought about it a great deal. Health and the cost of health care is what they're worried about.

In the area of financial risks we find an interesting counterplay of two findings. The first one I'd like to point you to is in Figure 17. How concerned are you that you might not be able to keep the value of your savings and investments growing faster than inflation? Of pre-retirees, 63 percent are at least somewhat concerned about that. With retirees, it's 55 percent. It's higher for that than the related thing on the third subject, that you might not be able to maintain a reasonable standard of living for the rest of your and your spouse's life. There's lower concern about that than inflation. For people who were around during the 1970s, inflation continues to be a scary word, even though we're in a fairly longstanding era of rather low inflation, and this also indicates that people feel the ability to reduce their standard of living if inflation and other things injure them. That is the primary financial planning tool of the retired, and in some ways, what the pre-retired have in mind.

Figure 17

The biggest financial concern is keeping savings growing faster than inflation.

How concerned are you . . . ? (Retirees, n=282; Pre-retirees, n=318)



Percentages may not add due to rounding.

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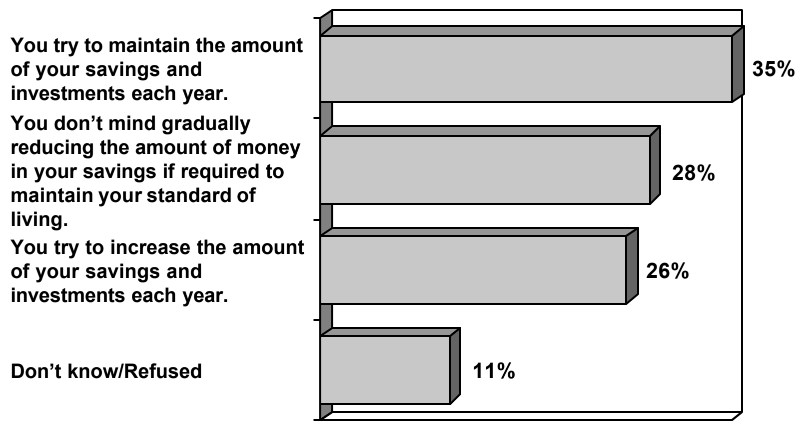
They're more concerned about inflation than they are about being able to maintain a reasonable standard of living because that can vary to some extent, although when the next generation of workers gets to retirement they're going to be a lot more uncomfortable about varying and reducing their standard of living than the current generation of the very old who grew up during the Depression, World War II, and found it a lot easier to reduce their standard of living.

Figure 18 is very important in that it shows the extent to which people haven't adapted to the realities of a long retirement. We asked retirees which of these three statements best describes the way they've managed their finances for the past three years or, if they were retired less than three years, since they've been retired, and we see that 35 percent try to maintain the amount of their savings and investments each year. They try to keep the amount the same in current dollars; 28 percent say they don't mind gradually reducing the amount of money in their savings if it's required to maintain their standard of living. Only one in four, 26 percent, try to increase the amount of their savings and investments each year. My firm just completed a study for the National Association for Variable Annuities, and we asked this of people who were working, about the strategies they expected to use, and the results were similar to this.

Figure 18

Only one in four retirees tries to increase his or her savings each year.

Which one statement best describes you over the past three years of your retirement, or since you retired if you have been retired for less than three years?
(Retirees, n=282)



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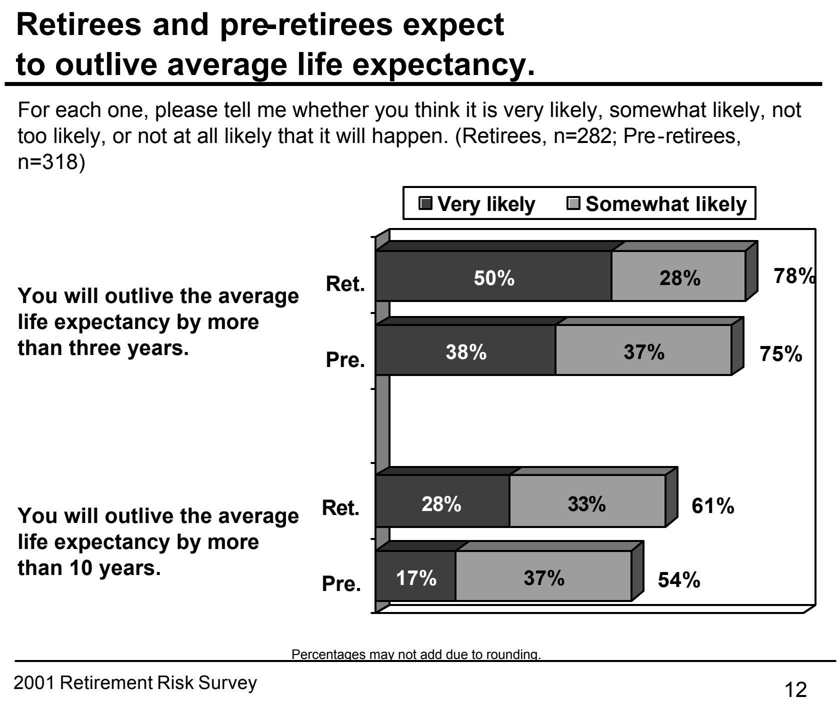
About half the people who retired will live for over 20 years. Let's take the 20-year point. Let's take inflation at three-and-a-half percent. People have the strategy of maintaining their current dollars. In 20 years, three-and-a-half percent, half the principal will be eroded to inflation, and –if the law stays in place where people have to start taking money out of their qualified accounts at age 70½, and most retirement savings right now is in 401(k) plans, then by that 20-year period another 20 percent or so is gone. So with this strategy for the half or so who live more than 20 years at this point, 70 percent or so of their income will be gone. This current approach to matching money in retirement is broken and has not kept pace with increases in life expectancy.

We also find that females who were not trained as actuaries are not as good at understanding how long life expectancy is. Most people, especially women, underestimate life expectancy. The LIMRA study asked people about how long they, themselves, expected to live. We asked people a somewhat different question, and the results are interesting. We asked how likely is it that they will outlive the average life expectancy by more than three years?

In Figure 19, you see that three-quarters of people think it's at least somewhat likely that they will outlive average life expectancy by at least three years. More interesting is that over half feel it's at least somewhat likely that they'll outlive the average life expectancy by more than 10 years. Again, most people think they're better than average. The interesting thing to me about this is why don't they act as if this were so? If this is somewhat likely, why don't they organize their finances to take this into account? Anna uses the word disconnect, and I think this is a disconnect. In some ways it's promising that people understand the risk of a longer life to themselves personally. It's the lack of action based on this that's the interesting thing.

Figure 19



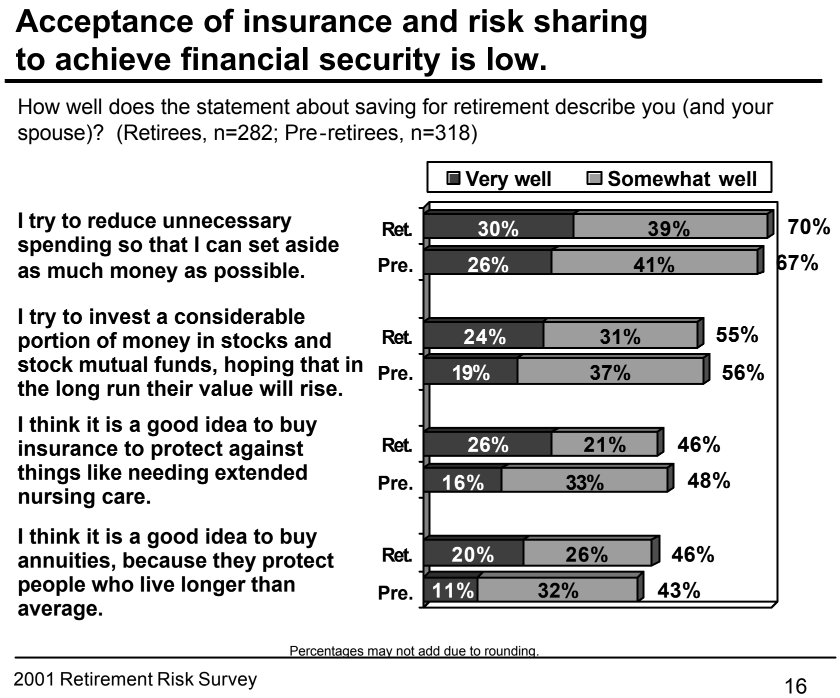
A couple of positive things emerge, however. How much thought have you put into preparing financially for retirement? Retirees, half of them said they didn't put a great deal of thought into this, and their savings indicates that that's true, and, of course, many of them started work and lived mainly in a DB world rather than in a DC world where retirement planning was less important. In a DC world, putting thought into retirement planning is a lot more important, and it's optimistic that the pre-retireds, not even close to two years before retirement, are already putting more thought into that than the current population of retireds is, and I expect that the retirement planning is going to occur younger and younger. So people are already showing signs of putting more thought into this.

On the other hand, these are pre-retirees. Have you or your spouse tried to figure out how much money you will need to have saved by the time you retire so you can live comfortably in retirement? That seems like a reasonable thing to do to me. In fact, when we've asked at what age do you expect to retire, almost everyone has a number in mind. Trying to figure out how much they need to have accumulated by that time seems essential to make decisions about how much to save and how much to spend, but a third—and this is people age 45 and above—have overlooked that point. In fact, it's fair to say that most people spend more time planning a two-week summer vacation than a 22-year retirement.

The bad news in some ways is, of the people who've thought about it and did try to calculate the amount, only one-third are confident that they'll be able to accumulate the amount of money that they will need by that time. Again, it's striking in some ways that this is a tolerable situation. Having decided how much they need for a comfortable retirement, a lot of people are tolerating not being on track to get there, and we've done other surveys that indicate that most people think they could save more for retirement.

Figure 20 discusses how well each of these statements describe you and your spouse, if you're married. The one that wins is, "I try to reduce unnecessary spending so that I can set aside as much money as possible." It's trying to reduce unnecessary spending that's the leading financial planning tool, more than the bottom two on this figure. I think it's a good idea to buy insurance to protect against things like needing extended nursing care or a good idea to buy annuities because they protect people who live longer than average. We're not even talking about doing something the LIMRA studies talked about. We're talking about it being a good idea to cover these risks with insurance, and for LTC insurance, 26 percent of retirees and 16 percent of pre-retirees think that this is even a good idea. So it's interesting to have the nonacceptance of insurance to protect against these risks. At this particular point in time, reducing expenses is a more likely tool.

Figure 20



Why do people retire? We asked retirees which of the factors were important in their decision to retire when they did, and we asked pre-retirees what they anticipated would guide them in their retirement, and the main thing is health. Among the retirees, 50 percent said keeping health insurance available through their employer was a very important aspect of their decision to retire when they did. Slightly less said the amount of money they had. What did the pre-retirees expect? Ninety-one percent think their health will be a somewhat important aspect to consider at the time they're planning to retire. Health is the first factor and then the amount of money is the second factor. But the key thing is health, and having access to health insurance is a key driver, and factors least considered when pondering retirement are age of eligibility for pension plans or for Social Security. So, setting these policies is going to have less of an impact.

One of the things that the Society was interested in was phased retirement, and, of course, to make phased retirement more feasible, some laws will have to be changed, but some phased retirement seems to be happening informally right now. We asked people who retired if they stopped working all at once or did they gradually reduce their working hours? Most people stopped all at once, but about one in five gradually reduced working hours. How interested would you be in being able to gradually cut back on the hours you work at your current job rather than stopping work all at once? We asked this of working people, and without mention of a pension supplement—it really didn't matter if we mentioned the idea of a pension supplement or not—about 40 percent are very interested in this idea, and another quarter are somewhat interested. Only about a third are not interested in the idea of a phased retirement.

Let me conclude with this. I think we see people who have some weak understanding of the risks in retirement, have some level of denial and have strategies for planning their retirement that just don't work. One of the goals is to help people from a system that works well for the half that are lucky enough to die early, to a system that works well for everybody.

MS. RAPPAPORT: I'd like to focus now on addressing the issues, because the purpose of the Committee on Post-Retirement Needs and Risks is to understand the issues, figure out where to get data and figure out how to model, but really that's just a little bit of the purpose. The real purpose is to make the retirement security system work better, and I personally feel like we have a long way to go and that we're in a time of opportunity. I'm excited to be involved with this activity. In talking about the issues we're going to talk about sources of security, about the family, issues affecting women, issues around annuitization and lump sums, the role of work during retirement and implications for education.

Sources of security are diverse. We didn't really talk about Social Security this morning, but for many Americans, and certainly for 40 percent, Social Security is basically the money they have in retirement, and people think Social Security is not that important. It is critically important for many people. We need to remember that, and that's really not very likely to change. Other sources of security are pensions, personal savings, assets and continued work. Many people are, in fact, phasing out not because their employers offer programs to do that, but they figure it out themselves. Housing is a source of retirement assets and security, for some people a very important source of security, as well as LTC insurance and life insurance. We've got a whole portfolio of things, and one of the challenges in thinking about this is being able to think about it as a portfolio rather than one thing at a time.

Family structure and old age security are important when considering retirement and risks. Family members are extremely important. If you go to some countries, they are virtually the total source of old age security. What is the system? The family takes care of people. In some of those countries birth rates have been declining, and where birth rates decline a lot, and the family was the source of old age security, that's a very big change and big issue. Family members can provide for and arrange for care. They can help with tasks and provide economic security and decision-making help.

How many people here have had a family member that they've been helping to care for or oversee in some way? Lots of us. We learn a lot of stuff from the actuarial exams, but there's a lot of stuff you learn from your family members. Family members are extremely important in this, and the availability of family to help is important. In fact, many people have moved to be near family members in order to help. Many younger people I know have made decisions to go back to the area where they grew up. So as we're thinking about this retirement planning picture, we need to not forget about the family.

The issues affecting women, which you all heard earlier, is one of my favorite subjects. There are differences in life spans, and many elderly women are alone for part of that time, and they're not as well off as families in many cases. We do have this decline in economic status at widowhood. Another way of saying that is that the financial security systems weren't working very well, and it's not a problem if they're still well off, but many of them are not well off. Work history affects old age security, and the paper I mentioned earlier from Social Security documents that there are still very big differences in the number of years on average that women and men are working in this country, and that's for people recently reaching retirement age. They're less likely to have a family caregiver available, and there are issues around how Social Security works. So it works better for some than others, and that's another issue I'm interested in.

Issues around annuitization need to be considered. Outliving assets is a serious issue, but it's often brushed aside. At the same time, level annuities without indexation don't do a good job. For the people here that are in the insurance industry, I have a challenge for you to think about product development, and, as we mentioned earlier, the issue could become more important. I want to point out to you another resource because we thought pointing out resources would be a valuable thing. The Actuarial Foundation Consumer Education Committee working with WISR, the Women's Institute for a Secure Retirement, has produced a booklet called "Making Your Money Last For A Lifetime: What You Need To Know About Annuities," and this is a booklet, and there's a background paper. The background paper is on the Foundation Web site. The booklet is available through WISR.

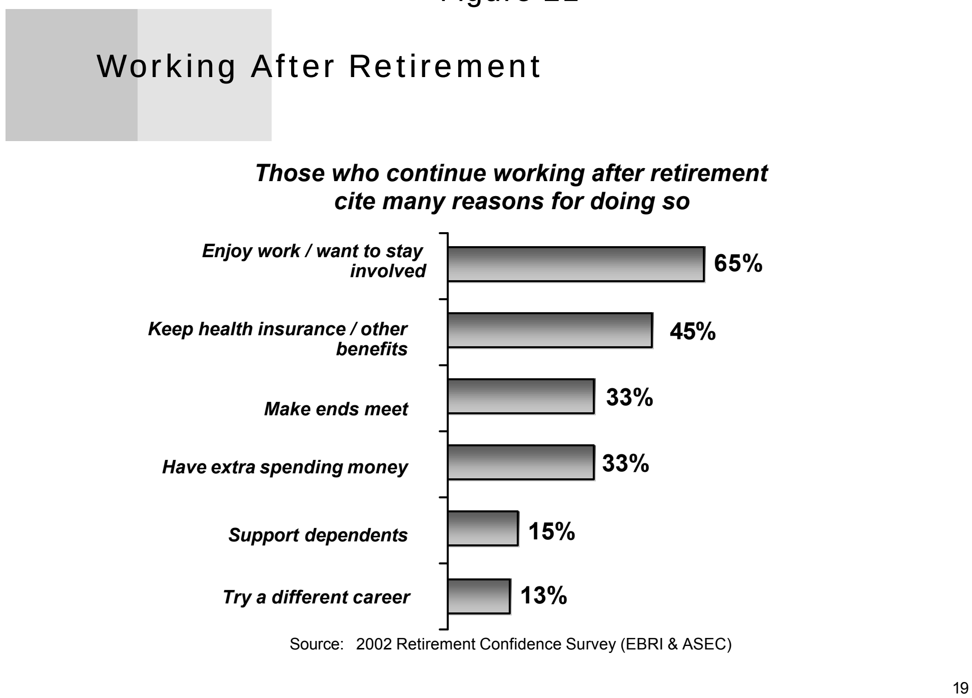
The booklet attempts to set forth the question: What are the issues and the tradeoffs? While we said people don't do things about this, these are not easy decisions, and there are tradeoffs involved in all of them. This tries to set out for people the tradeoffs, but I've given it to many people who aren't professionals, and they say this really helps put the issues in focus. So I recommend that.

Lump sums are much more common in the retirement system, and we asked are they good or are they bad? They're good, and they're bad. When people have a choice of lump sums, they elect lump sums, and that seems to be pretty universal, I believe, across countries as well if there's not something like indexing if you get the income. Some of the benefits of lump sums are they allow you flexibility in planning. You can control your assets. You can leave the money to your heirs. If you want to buy a retirement home or save for future frailty, you can do that. You can think, I can invest the money better and get a better return. On the other hand, the money might be spent for nonretirement purposes, and people might outlive their assets, and in some cases the retiree's afraid to use the money and spend it.

I would say in terms of these issues, also in bracketing these issues, we're really talking about the middle here. If we think about the 40 percent of the population that basically has Social Security and doesn't have any financial assets, there's not too much they can do about most of what we're talking about here. They've got to do the best they can. If we think about the very top—and we might argue it's the top five percent, or is it 10 percent?—their concerns really are not so much about the managing of these risks, even though they do have to do risk management, but they're also around things like estate planning, and the risk of outliving assets is not that much of an issue for them, but there's a big piece in the middle, and these issues are really about the middle.

Working after retirement, we didn't really talk about that so much as a strategy, but it's certainly a strategy that people are using today, and one of the ways that they're managing is that they go back to work. If they need health insurance, they go back to work if they need more money. Figure 21 is data from the retirement confidence study. . Why do people continue to work after retirement? If you look at this, the top and the bottom reason are, "it's about what I want to do. It's what I would like to do." Enjoy work and stay involved, 65 percent. Thirteen percent try a different career. All the middle stuff is it's about benefits and money, the top one being health insurance. Now, Joe Quinn, who has done work on what's going on with retirement patterns, says that the people that are most likely to get bridge jobs and work after retirement are the top and the bottom more than the middle, and for the top it's about what I want to do, and for the bottom it's more about money.

Figure 21



We also know people that say my regular retirement income covers my basic living expenses. I want to travel. I want to play. So that's what they do. The whole idea of the definition of retirement is changing. There's also a paper in the most recent Social Security bulletin that looks at health resource services data and asks people if they're retired and then looks at how many hours they're working, and so they cite to what extent there are issues around that, and one of the things my committee is doing is looking at the definition of retirement.

In planning for retirement we need to think about how much money do we need, both currently and over time? How things will change, and if we think about our parents as well as ourselves, things do change, and there are changes that are pretty predictable, but there are also changes that are very unpredictable, and discontinuity certainly. There's a lot of uncertainty. There are also issues surrounding taxes and estate planning, and that's not what my committee does. We do not talk about that.

The need to eliminate and reduce debt is a retirement planning issue. One of the issues that is surprising to me as we've been working on this research in connection with the software, and talking about scenarios and situations that apply for people, is hearing from the financial planners that one of the big issues is that people don't only go to retirement without enough assets, they go with a lot of debt sometimes. Another issue is, how do I get advice? I said I'd give you a couple of disconnects, and we want to work on a paper on disconnects.

What do we mean by disconnects? Research shows what the public believes, and we have some data that shows it's: a poor understanding of life expectancy; the chances of living to 80, 90, 100, or more; a lack of focus on mortality risk and underestimation of the financial consequences of a long life; expectation that only other people will need LTC; denial—they say I'm better than everybody else; failure to plan for the survivor after one dies; underestimating retirement needs; and overvaluing a lump sum over a life income. This has been shown in many things, and actually in some other research we're working on now we want to try to quantify this, but one of the reasons lump sums are so popular is people can't make a translation between income and lump sums, and they think $100,000 or $200,000 is a lot of money. Maybe they'd have more money in terms of an income, but it doesn't seem like it.

Retirees overspend and overestimate how long their lump sums might last, not considering increases in needs and not thinking about how much they need. People overestimate how long they will work, and that's documented in the retirement confidence study. Many people think they're going to work a certain period of time; they retire earlier, and overestimate future investment returns. Hopefully by next year we'll have a paper with data documenting these disconnects. So where are we today?

We've got two studies with compatible results, different samples and methodology, large improvement long term in the economic status of the elderly, disconnects common, inadequate risks, protection and savings. The population will age dramatically as the baby boomers age in this country. There is still too much poverty, and more people are working after retirement. We have a little bit of time for questions, and I was going to start, though, by asking, if any of our visitors from Europe wanted to comment.

MR. TOM ROSS: Yes, a lot of what I've heard, and I'm sure that others from the European end would agree that much of what we heard was quite familiar, except perhaps in the U.K. You certainly wouldn't have quite the same emphasis on the cost of Medicare and so on because of a different system. Maybe they should be worried about it, but it's not so obviously there. I think I was particularly interested in the study of those who are not yet retired that said that of the proportion who had thought carefully about it and were making plans, thought they would struggle to accumulate enough to meet their needs.

There was an earlier question in that that would have been interesting and certainly what is asked in the U.K., which is what are their perceptions about the amounts that they're saving, whether they're capable of saving them or not, and certainly the evidence in the U.K. is people don't have a clue how much it takes. Whether they're able to save it or not is the second question. I think if they got the right answer to the first one, the proportion who would say they wouldn't be able to do it would be vastly higher than you'd find, probably 100 percent or not far off it. I don't know if you've done the work, but there is an earlier question there that I think is very important in all of this, and that would be the answer in the U.K., disturbingly.

I have a few more fairly random comments. Certainly the concept of paid work forming part of retirement income is something that is coming up in debate in the U.K. I haven't seen any surveys that suggest that the people would want to do it. I mean I've gotten a few nasty letters and e-mails saying how dare you suggest I work longer as part of providing for my old age. And certainly there does need to be a very big debate on the nature of that, the education, retraining, and so on needed, because for many people, extending working life in the sort of occupations they have—it's all right for people like us, but for many, many people the concept of continuing in paid work in their occupation is not a very attractive thing, given the nature of the occupation, and they may not be in the 40 percent who are just relying on Social Security anyway.

There's a big investment needed to make this a reality, and to win the hearts and minds of people would be a good thing, including employers. I don't know about you over here, but certainly in Europe there is a need, for example, for anti-ageism-type regulation. This is going to be the next thing that's going to happen, I think, now that the sex discrimination stuff has been supposedly dealt with, and I think that's going to be a big issue for us.

Another issue that is very much in the psyche over there from what I've seen is a desire to pass on assets to the family. Again, I'm not sure quite what you found out, but people have this naive notion that it's a good thing and a very important thing to pass on assets to their kids, when in reality they're not saving enough to look after themselves. I think another very important manifestation of this is home ownership. You mentioned housing, but I think it was more in terms of meeting needs. More and more I suspect the same is true in the United States, people do own their own homes, but are very reluctant to convert them into some sort of an asset or an income that they can live on. There's some sort of desire to want to pass them onto their kids.

A well-known U.K. member of Parliament, who's a member for a rather impoverished constituency up near Liverpool, was telling me once how when he visited constituents in the hospital, and he was talking to them, the big issue there is, do you have to sell your home to pay for care? It's quite controversial. When you ask them what they think about having to use their home to pay for their care, to get it down to the maximum level of capital you can have before the state kicks in, the people concerned don't seem to be too bothered about it. It's their kids who take exception to it. The reality is that it's a large asset there, which counters the issue of whether people are saving enough, but is the prospect of using it damaged by this perception that people would like to leave it to their kids.

I would like to mention a final couple of things on LTC. I haven't mentioned health, although it could be an important thing. On perceptions: Why do people underestimate how long they're going to live? And why do people underestimate the chances that they might need LTC? I think to some extent this is conditioned by their own experience with their own parents. I've sat in a number of surveys where people say, "I know I'm not going to look beyond when I'm 70 because my dad died when he was 63." People's parents grew up in an age in which they tended to die of something where the need for care certainly for any length of time was probably rather less than it is now. I don't think we should underestimate how conditioned people are in their perceptions by what happened to their own families.

Long-term-care insurance is in its infancy in the U.K., and the skeptics look across the pond and say, "Well, it's not going to be a success because not even the Americans can sell it to their people." I've just got one tip. You're meant to be the marketing champions of the world, and I think that long-term care, the name itself, might be one of the reasons why people think it's usually expensive because it's not really long-term care. It's short-term care that's not needed until after a long period elapses. We heard an average this morning, but the typical length of time that LTC payments are needed is really quite short. So I think that before you're going to change the perception of its expenses, some bright person should think of a better name that more accurately describes it.

MS. RAPPAPORT: There also potentially may be a combination product, annuities and LTC, and there's a task force in the Treasury Department to look at changing the tax laws to accommodate combinations.

FROM THE FLOOR: With respect to annuitization I'd like to suggest that the issue has a different dimension for a 62-year-old male versus an 80-year-old female. Are we making a mistake here by treating this as a single-dimension yes-or-no decision?

MS. RAPPAPORT: I think you're absolutely right. Maybe we should think about in our research whether there's anything that we can do to differentiate a little bit. But, of course, we're not focusing here directly on individual planning, and if you were, then you certainly should be differentiating.

MR. GREENWALD: It seems to me that one thing that's worth thinking about, and who better than actuaries, is at what point people should annuitize. The later, clearly the better because that's when the payout is higher, and there's a strategy there in terms of when people start to have their standard of living impinged and try to hold out as long as possible and then annuitize. One impediment, of course, is the desire to leave money behind, but I think there are a lot of studies in the United States that indicate that leaving money behind is only important to about 15 percent or 16 percent of the population who tend to be the most affluent. With some others, their main concern is not being a burden on their children. They really don't want that. Leaving money behind is nice if there's anything left over, but most people who are not affluent think their primary responsibility is to themselves. But the key issue is to give people advice about the ideal time to annuitize, just as there's a common thought that the ideal time to buy LTC insurance is earlier rather than later.