Society of Actuaries
Key Findings and Issues: How Americans Understand and Manage their Retirement Risks
2005 Risks and Process of Retirement Survey Report
April 2006

Introduction and Background

The long and widely heralded passage of Baby Boomers to retirement is about to reach fruition. Maturing into senior citizen status, this generation of Americans brings with it to the forefront serious issues of financial security and wellness. Understanding retirement risks is becoming critically important in light of our aging society, volatility in financial markets and growing emphasis on individual responsibility for managing personal assets. Compounding these issues are the changing dynamics of work itself, specifically, how people leave the labor force or partially retire as they get older. The very concept of retirement is also changing, as people ‘reinvent’ their lives.

Traditionally, retirement planning had focused on the years before retirement. Several years ago, the Society of Actuaries, recognizing the need to address management of risks after retirement, instituted a Retirement Needs Framework Project. As part of this project, the Society has had research on public attitudes toward retirement in 2001, 2003 and 2005 conducted on its behalf by Mathew Greenwald & Associates, Inc., and by the Employee Benefit Research Institute (EBRI).

The purpose of this ***2005 Risks and Process of Retirement Survey*** study is to evaluate Americans’ awareness of retirement risk, how their awareness has changed recently, and how it affects the management of their finances. Additional reports cover in more depth the process of retirement, longevity, and retirement issues of special concern to women. The 2001, 2003 and 2005 studies separately analyzed current retirees and those not yet retired, referred to in these reports as ‘pre-retirees’. Another study conducted in 2003, The Retirement Plan Preferences Study, sponsored by the Society of Actuaries and American Academy of Actuaries, focused on the preferences of employees for different benefit plan features and distribution methods.

The ***2005*** survey was conducted through telephone interviews of 602 adults age 45 to 80 (302 retirees, 300 pre-retirees); the 2003 Retirement Plan Preferences survey covered adults of all ages who have or retired with benefits from an employer-sponsored pension plan. A description of methodologies and some discussion about the populations studied follows.

The ***2005 Risks and Process of Retirement Survey*** applies to Americans on average, and does not provide specific insights into behaviors and values of high net worth individuals. Only 2% of the sample reported $1 million or more in savings and investments. Four percent of pre-retirees and 9% of retirees report savings and investments between $500,000 and $1,000,000. Fifteen percent of pre-retirees and 10% of retirees report household incomes of at least $100,000. At the low income end of the spectrum, 15% of pre-retirees and 21% of retirees report incomes below $25,000.

The groups surveyed identified a number of risks relating to retirement. The preponderant emphasis was concern over cost and availability of health care, keeping the value of investments up with inflation, outliving one’s assets and having to rely solely on Social Security, and maintaining a reasonable standard of living. This report provides an overview of these post-retirement risks, how they are perceived, and ways to provide protection against them. It presents key findings from the ***2005 Survey*** on understanding and management of the **health care**, **inflation**, **investment**, and **longevity** risk, and relates these results to other studies. It also includes findings from focus groups conducted in 2005 that examined how Americans manage their assets, and certain results from the 2003 study for some questions not repeated in 2005.

To further the understanding of changes in perception of risk, these studies include some new questions in each iteration, and not all questions are repeated in every study. The report provides additional perspectives on risk from other sources, and concludes with observations on Behavioral Economics and Retirement Risk. The discussion sections in this report include input from all organizations that supported the studies.

Overview of Post-Retirement Risks

Post-retirement risks include those specific to each individual retiree, such as longevity and the risk of outliving assets; declining functional status; ability to pay for health insurance and major out-of-pocket medical expenses; loss of a spouse or other care giver; change in status of other family members providing or needing assistance; and extraneous risks, such as inflation and volatility in financial markets.

Protection against the financial impact of some of these risks may be provided by employee benefit plans, Social Security, private insurance, and other financial products. Many Americans, however, still choose to self-insure against these risks by investing their retirement portfolios independently and changing their spending habits. Following is a summary of risks and the types of insurance and financial products available to protect against them.

Risk	**Potential Range of Risk**	**Products for Risk Transfer**
Outliving Assets	At age 65, average life expectancy is 17 years for American men and 20 for women. This means that half those retiring at 65 will survive longer. Thirty percent of all women and almost 20% of men age 65 can expect to reach 90. [1]	Annuities, including joint and survivor annuities and deferred annuities commencing at higher ages, such as 75 or 80.
Loss of spouse	Because women have traditionally been younger than their spouses, periods of widowhood of 15 years or more are not uncommon. For many women, the death of a spouse is often accompanied by a decline in standard of living.	Joint and survivor life annuities; life insurance
Decline in Functional Status	The cost of care as older people become frail may amount to millions of dollars for a couple over their lifetimes. Nursing home care costs may exceed $70,000 a year per person. [2] Care may be provided at home, in adult day care centers, assisted living facilities or nursing homes.	Long-term care insurance that helps pay for the cost of caring for disabled seniors. Many continuing care retirement communities (CCRCs) cap monthly costs for assisted living and skilled nursing care, but are subject to their own financial risks.
Health care and medical expenses	Medical costs for retirees over 65 not covered by Medicare may exceed $1 million for a couple over their lifetimes.	Medical insurance
Inflation	Over the period 1980–2005, annual inflation in the US for all items has ranged from 1.1% to 8.9%, and has averaged 3.3%. For medical care, the annual average has been 6.4%. [3] Inflation has generally been much higher outside North America.	Annuity products with cost-of-living adjustment

1. US Life Tables, 2002
2. Expressed in 2005 dollars
3. Consumer Price Indices, US Bureau of Labor Statistics, 2005

Key Findings from the 2005 Study

Pre-retirees are more concerned about risk than retirees. Both are highly concerned about health care-related risks.

Finding

Pre-retirees express higher levels of concern about retirement risks than those already retired, and are much more likely than retirees to be *very* or *somewhat* concerned about most of the risks examined in the study, including:

- Inability to afford adequate health care (75% pre-retirees, 46% retirees);
- Keeping the value of their investments up with inflation (65% pre-retirees, 51% retirees);
- Inability to afford long-term care (61% pre-retirees, 52% retirees);
- Inability to maintain a reasonable standard of living for the remainder of their and their spouse's lives (59% pre-retirees; 43% retirees);
- Depleting their savings and having to rely solely on Social Security (55% pre-retirees, 38% retirees);
- Inability to leave money to heirs (37% pre-retirees, 26% retirees); and
- Inability to rely on family members to provide assistance (34% pre-retirees, 26% retirees).

Discussion

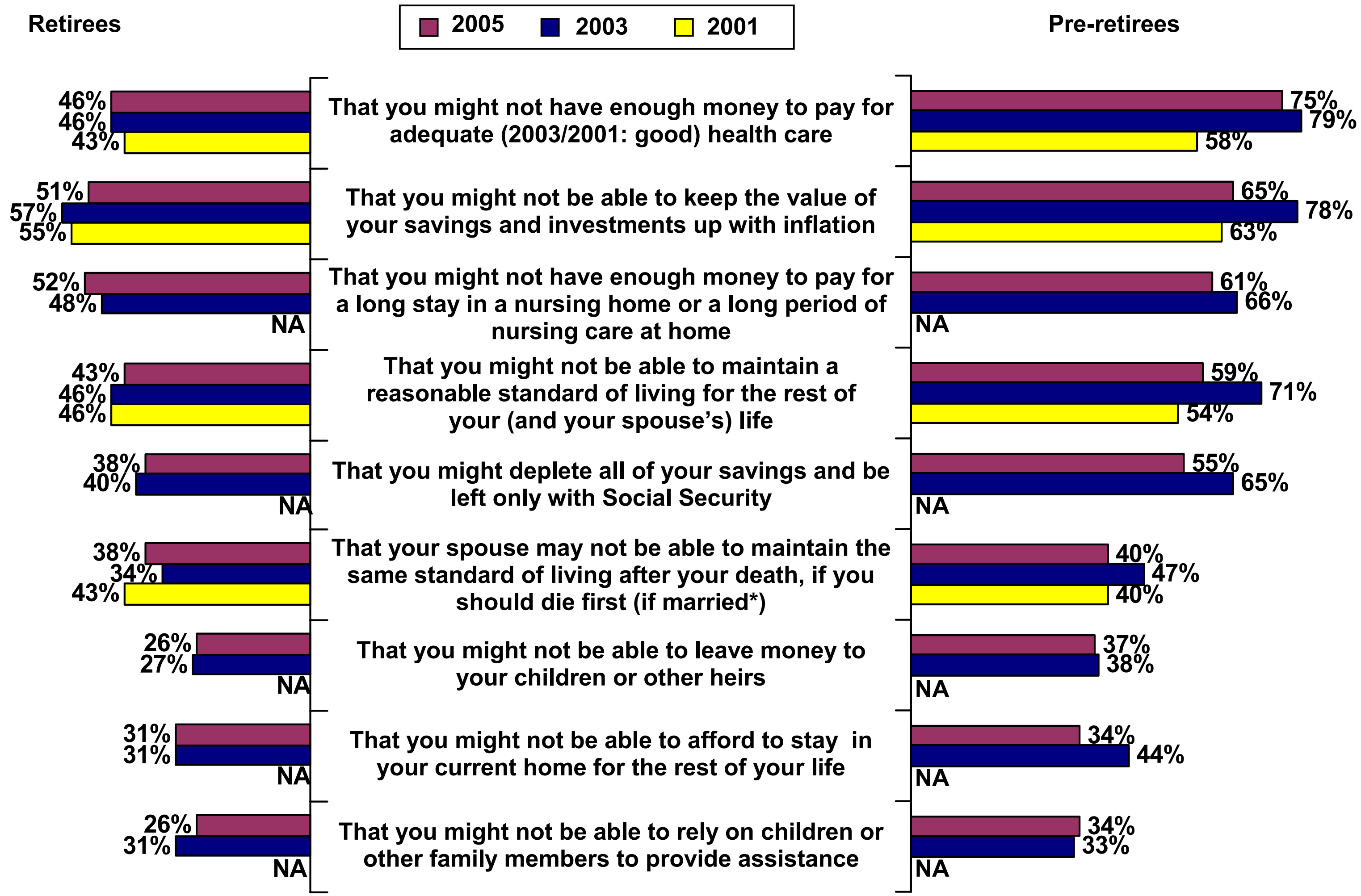
In spite of continued decline in defined benefit plans and retiree health coverage, risk awareness was lower among pre-retirees in 2005 than in 2003, though not quite at the level of 2001. The need for individuals to assume more personal responsibility for their own financial security in retirement does not seem to have been accompanied by greater knowledge in how to manage such risk.

Retirees appear to have fairly constant perceptions about risk, perhaps because they already have plans in place and may feel that there isn't much they can do about them.

Strategies that individuals have been using to adjust to changes in financial circumstances include reducing their spending, working longer, and returning to work. However, many people may not have the option of working longer, and the Retirement Confidence Study indicates that about four people in ten retire earlier than they had planned.

How concerned are you . . ?

(2005: Retirees, n=302; Pre-retirees, n=300)



*Asked only of married respondents (2005: Retirees, n=177; Pre-retirees, n=197)

Source: 2005 Risks and Process of Retirement Survey

Health Care Risk

Among retirement risks, affordability of health care is the one most likely to worry pre-retirees.

Finding

While health care expenses cause significant worry among retirees, pre-retirees are even more likely to express concern about having to pay for health care in retirement. Three-quarters of pre-retirees are *very* or *somewhat* concerned about having enough money to afford adequate health care (75%), and six in ten are concerned about having enough to pay for long-term care (61%). Roughly half of retirees are concerned about each of these costs.

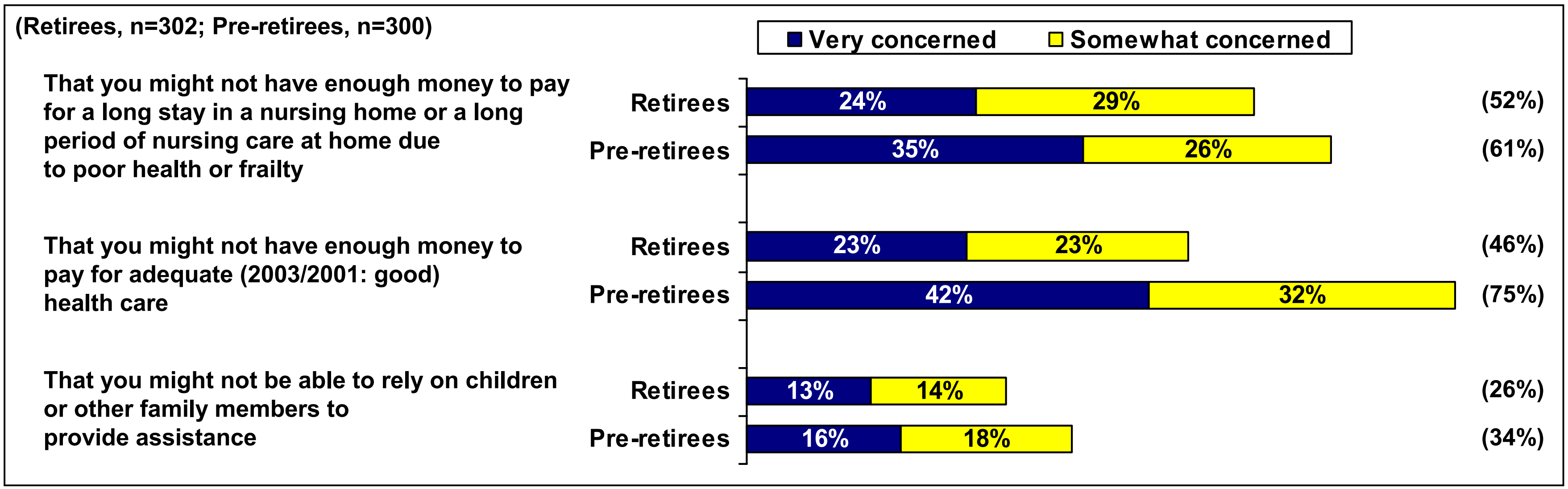
Both retirees and pre-retirees are much less likely to say they are concerned about not being able to rely on family members for assistance. One-third of pre-retirees are *very* or *somewhat* concerned (34%) compared to one-quarter of retirees (26%).

Discussion

High levels of concern about health care risks is not surprising in light of the level of inflation in medical care costs, and the decline in employer-provided health benefits for retirees and, to a lesser extent, for active employees. Even when health coverage is provided, retiree contributions have often risen significantly. Where employer coverage is not provided, it is very difficult for those retirees who are in poor health and not yet eligible for Medicare to buy coverage in many states.

Medicare has just implemented a new prescription drug program as of January 1, 2006, but initial reactions suggest that the program is not well understood, and will require considerable revamping. There also appears to be widespread agreement that major changes will be needed to bring Medicare costs under control, but there is no clear consensus as to how this can be achieved politically.

How concerned are you . . . ?



Source: 2005 Risks and Process of Retirement Survey

Inflation Risk

Inflation ranks among the top three concerns of pre-retirees and retirees; many worry specifically about their ability to maintain their standard of living.

Finding

While pre-retirees seem more concerned than retirees, inflation risk ranks among the top three concerns examined in the study for both groups. Half of the retirees (51%) and two-thirds of pre-retirees (65%) are *very* or *somewhat* concerned about inflation risk.

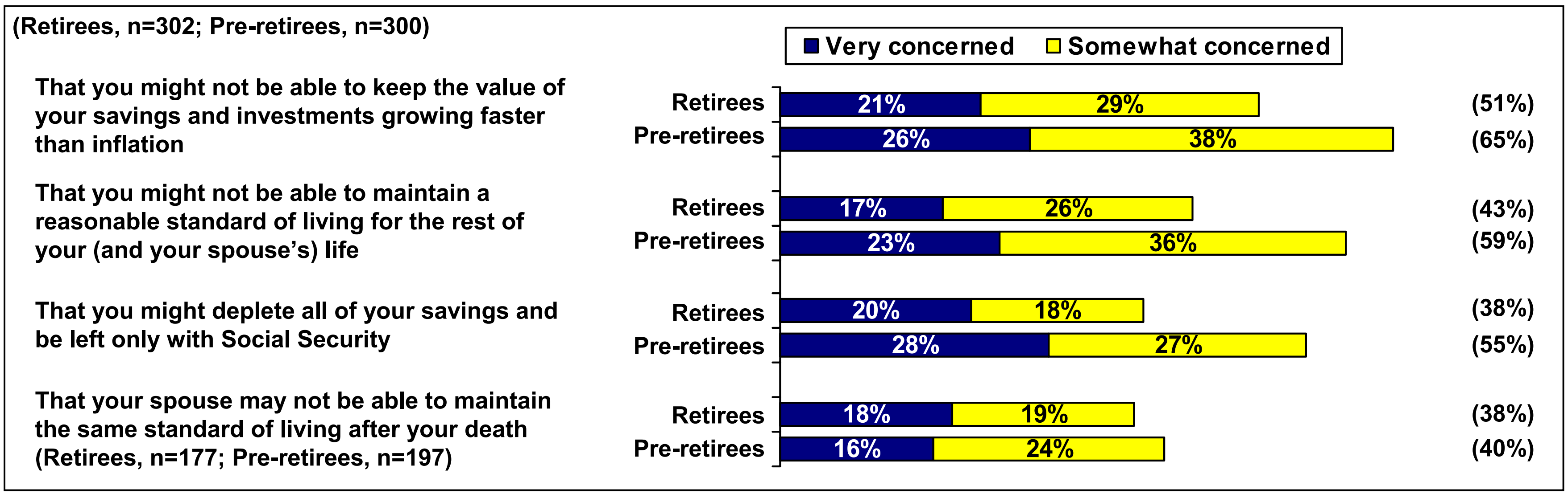
Similarly, pre-retirees are more likely to be concerned that they will deplete their savings and be left with only Social Security (55%) than are retirees (38%). Many are concerned about maintaining their standard of living, with six in ten pre-retirees (59%) and four in ten retirees (43%) concerned that they will not be able to maintain the same lifestyle for the rest of their lives.

Discussion

Although overall inflation has not been as high recently as it was in prior years, medical care costs have been rising at almost twice the rate as for all goods and services. In addition, retirees are often expected to bear a higher share of these rising costs, with Medicare premium increases consuming much of, and in some cases all, their annual increases in Social Security benefits. More recently, the higher cost of energy, especially gas and heating oil, has been an added shock to retirees' budgets.

Inflation is a serious long-term issue for retirees as, except for Social Security, most retirement income benefits are not indexed for cost-of-living. In recent years, investment markets have disappointed many retirees, and while inflation has been more contained with lower interest rates, the downside for retirees is reduced yields on their fixed-income assets. Adding to these woes, returns on their equities investments have been much lower, sometimes in negative territory, for the first years of the 21st century.

How concerned are you . . . ?



Source: 2005 Risks and Process of Retirement Survey

Inflation Predictions

Half the public think prices will be at least double 10 years from now.

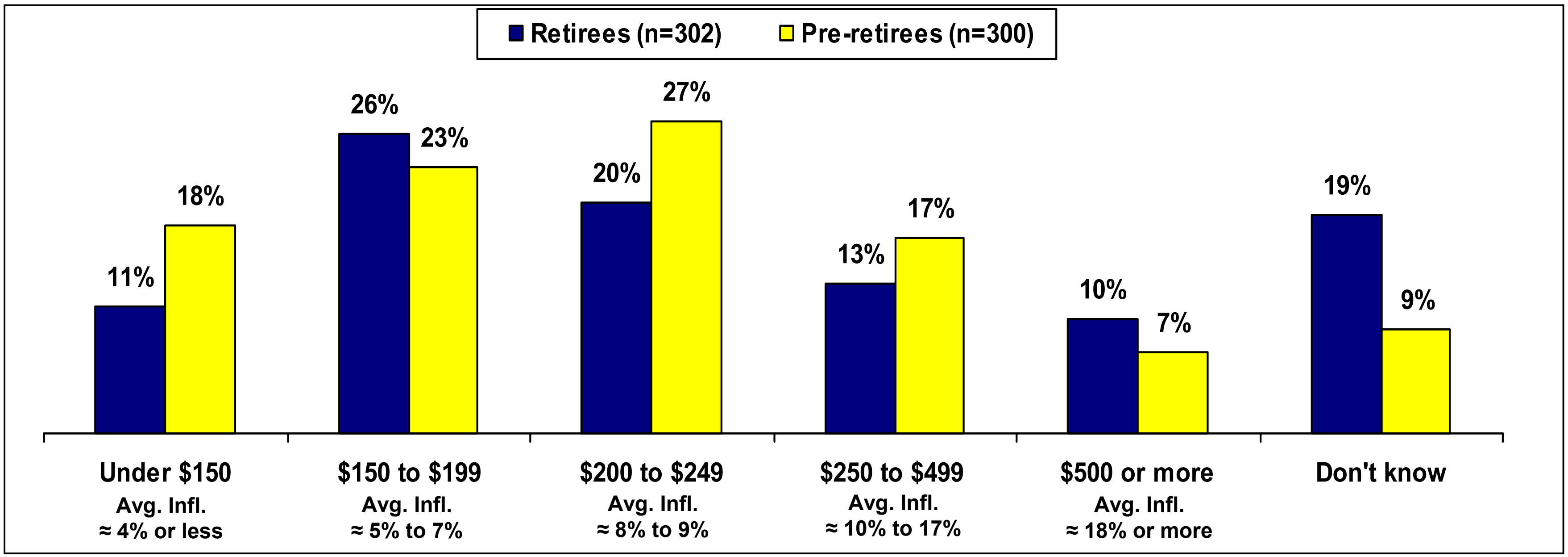
Finding

Pre-retirees and retirees generally offer similar predictions of 10-year inflation, with more than half expecting that prices will at least double in ten years. However, pre-retirees are more likely than retirees to think groceries costing $100 today will cost less than $150 ten years from now (18% pre-retirees, 11% retirees).

Discussion

Public perceptions of inflation are that it will considerably exceed in the near future what it has actually been in the recent past. Between 1995 and 2005, prices for all items in the US rose by an average of 2.5 % a year; for health care the average was 3.4%. [4] Long-term economic predictions depend on countless variables, and are highly speculative, but for prices to double in the next ten years, as a majority of both retirees and pre-retirees expect, the annual rate of inflation would have to average above 7%. This would be more than double the average for the past quarter-of-a-century, and almost three times the average for the past ten years.

Suppose your weekly groceries today cost $100. How much do you think they will cost in 10 years?



4. Consumer Price Indices, US Bureau of Labor Statistics, 2005

Source: 2005 Risks and Process of Retirement Survey

Investment Risk: In 2003, neither workers nor retirees described themselves as *'very confident'* about managing their money in retirement, though more say they are *'somewhat confident'*.

Finding

Neither workers nor retirees express a great deal of confidence in their ability to manage money in retirement; this low level of confidence declines even further as questions become more specific. Only 35% of retirees and 31% of pre-retirees say they are *very* confident in their ability to manage investments during retirement. When questions become more specific, such as allocation of investments, growing savings at least as fast as inflation, and converting a lump sum balance into a lifetime income stream, the proportion of retirees who say they are *very* confident about managing their money falls to one-quarter and of pre-retirees to two in ten.

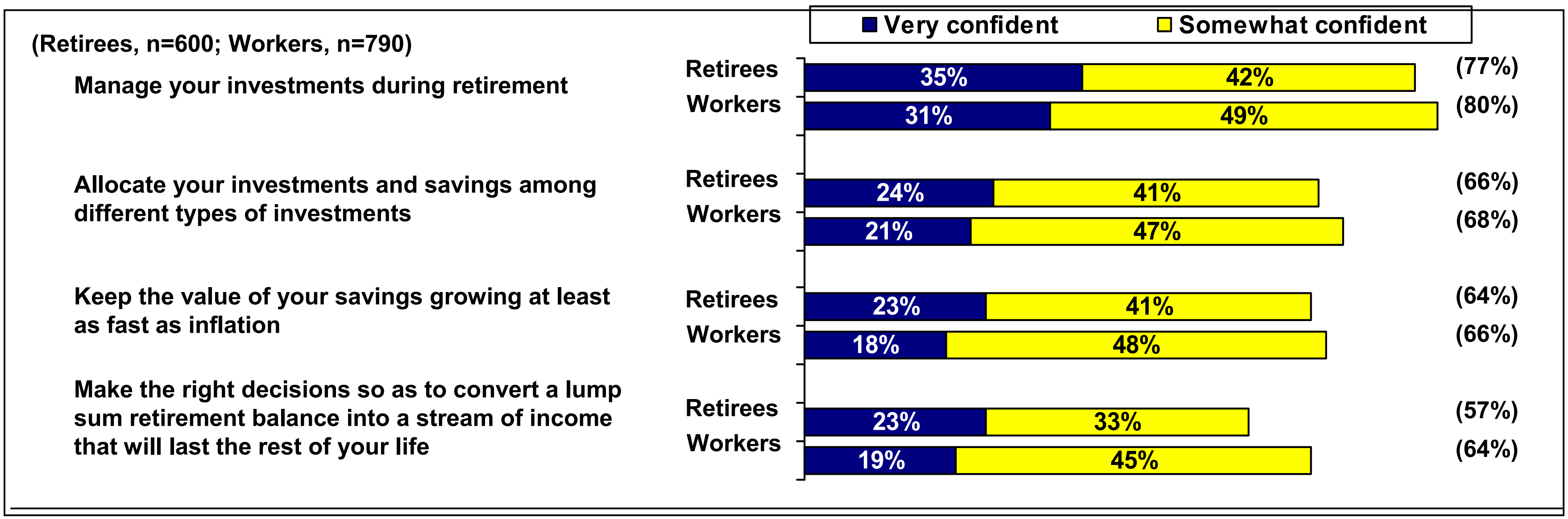
Discussion

The lack of confidence that retirees express in their ability to manage retirement assets may not be surprising, as many of the retirees surveyed have participated primarily in traditional defined benefit plans. They may not have many investments to manage nor had the expectation that they would need to manage investments in retirement.

However, a majority of those surveyed who are still working participate in defined contribution plans, and might be expected to be more comfortable managing such funds. As noted, they lack knowledge of investment basics, which clearly translates into lack of confidence. This lack of knowledge and confidence may increase their financial risk once they retire.

Major gaps clearly exist in the public's understanding of investments. Extensive financial education is needed with workers increasingly dependent for retirement security on the assets in their defined contribution plans, which they will have to assume more personal responsibility in managing.

Please indicate how confident you are in your ability to do each of the following during retirement.



Source: 2003 Retirement Plan Preferences Survey

The role of housing as an investment in managing post-retirement risk

In 2005, the ***Risk and Process of Retirement Survey*** included for the first time questions as to whether housing was important in financial planning for retirement. Not surprisingly, for many families, housing is an extremely important asset. Even for families with significant pensions and assets in retirement savings programs, equity in their home is often their next largest asset. And for families without such retirement savings or pensions, housing is often their only significant asset.

Housing can be used to help finance retirement in various ways:

- By paying off the mortgage, families can reduce their current spending in retirement.
- By taking a reverse annuity mortgage, families can gradually use the value of a house to generate additional income in retirement. Although they currently lack in popularity among retirees, such mortgages can offer a lifetime guarantee, so that payments will continue regardless of how long the person lives. Hence, they can provide longevity insurance.
- The house can be sold in an emergency, generating cash to pay for other needs, but the family will still need housing after the sale.
- The house, if owned, can be viewed as a part of life income during retirement and then be used as a bequest at time of death.

Only a small minority of homeowners plan to tap their equity to help fund retirement.

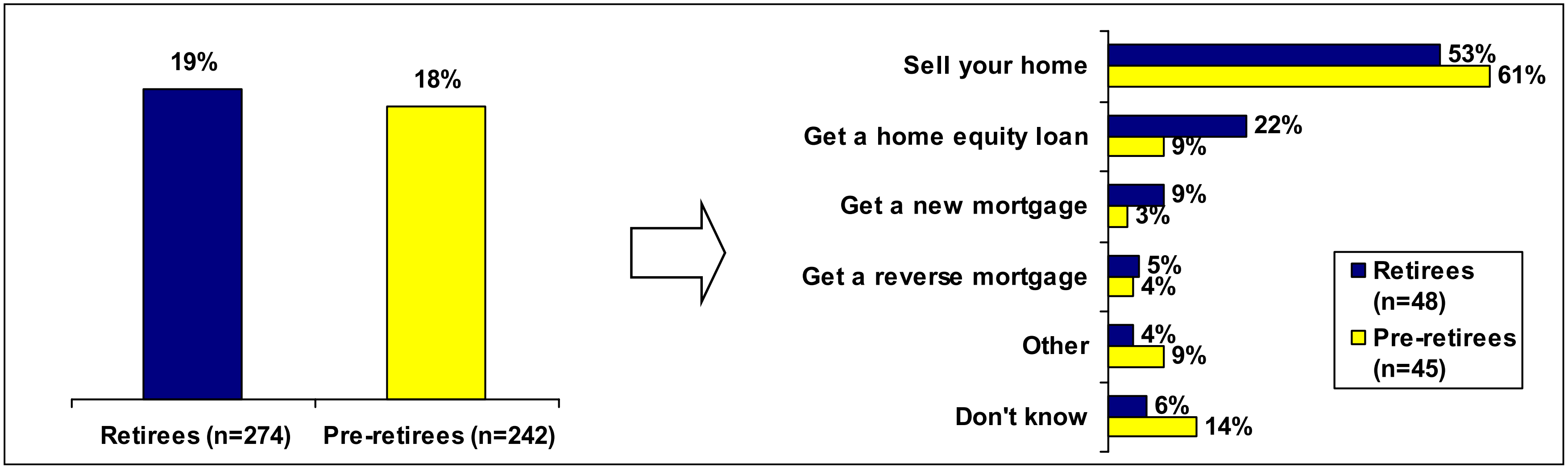
Finding

Only two in ten retirees (19%) and pre-retirees (18%) plan to use equity in their home to help finance their retirement. More than half of those who do plan to use home equity say they will tap into it by selling their home (53% of retirees, 61% of pre-retirees). They are less likely to indicate their plans include getting a home equity loan (22% and 9%), a new mortgage (9% and 3%), or a reverse mortgage (5% and 4%).

Discussion

The home is an important asset—if not the most significant—for many families, yet fewer than one homeowner in five said they plan to tap this source of equity to help fund retirement. Sentimental value and the psychic rewards of maintaining a home are significant considerations for many retirees, and may lead to decisions that are not necessarily to their greatest advantage from a purely financial perspective.

(Retirees:) Up until now, have you used any of the equity you built up in your current home or a previous home to help fund your retirement? (Retirees and pre-retirees:) Do you have any plans to use the equity in your home to help finance your retirement in the future? If yes to either question: Did you/Do you think you will . . . ?



Source: 2005 Risks and Process of Retirement Survey

Understanding of Investment Risk and Vehicles

From their responses to basic questions as to how investment vehicles work, the public appears poorly prepared to assume the management of retirement assets.

A useful perspective of the public's knowledge of investments is given in the John Hancock Life Insurance Company's 2004 study in the series, *The Insight into Participant Investment Knowledge and Behavior Study.* Respondents to that survey all participated in 401(k) or similar plans that gave them investment choice, but many show significant gaps in their knowledge of investments, and confusion about how investment vehicles work, their relative risk and what they include.

Survey respondents were unclear about the features and risk profiles of many investment vehicles common to employer-sponsored plans. For example, when asked what types of instruments are found in a money market fund, 48% said short-term investments, 47% said bonds, and 43% said stocks. Participants were asked to include all that applied, so multiple responses are possible. Only 9% knew that money market funds contain only short-term investments. Similarly, most participants do not understand how bonds function and perform in changing investment markets. Specifically, they do not understand that the market value of a bond moves inversely with changes in external interest rates. In the Hancock's 2004 survey, more than three-quarters, 77% of respondents, did not know that the best to time to invest in bonds is prior to a decrease in interest rates. In addition, significantly more respondents believed there is a direct relationship between bond prices and interest rates than believed there is an inverse relationship. This level of misunderstanding has been consistent since these questions were first posed in 1992.

Participants are confused about the relative risk of company stock. When asked to rank the risk of various investment options within their employer-sponsored plans, in all nine surveys, respondents ranked their company's stock as less risky than diversified domestic stock funds or diversified global stock funds. Unfortunately, familiarity with the employer, combined with the loyalty of the employee may lull the participant into a false sense of security regarding employer stock as an investment. Recent revelations of corporate fraud and mismanagement, leading to the impoverishment of retirees who had a majority of their defined contribution plans invested in company stock, serve to heighten the importance of education in financial risk.

The lack of investment knowledge of the average American is probably even worse than that suggested by the results to this series of surveys. All respondents to these surveys were required to participate in their employer-sponsored defined contribution plan, and therefore had some investment experience. Not all Americans do.

Longevity Risk: Lifetime income is the dominant concern among retirees when choosing a payout option from a retirement plan.

Finding

Almost nine in ten retirees say lifetime income is a *very* important consideration when choosing a payout option from a retirement plan. Almost as important for retirees are not outliving one's assets and keeping up with inflation. Workers consider the same set of factors *very* important, but also add control of savings to the list of considerations they are most likely to think *very* important. At the same time, both retirees and workers express concern about dying early and losing annuity value.

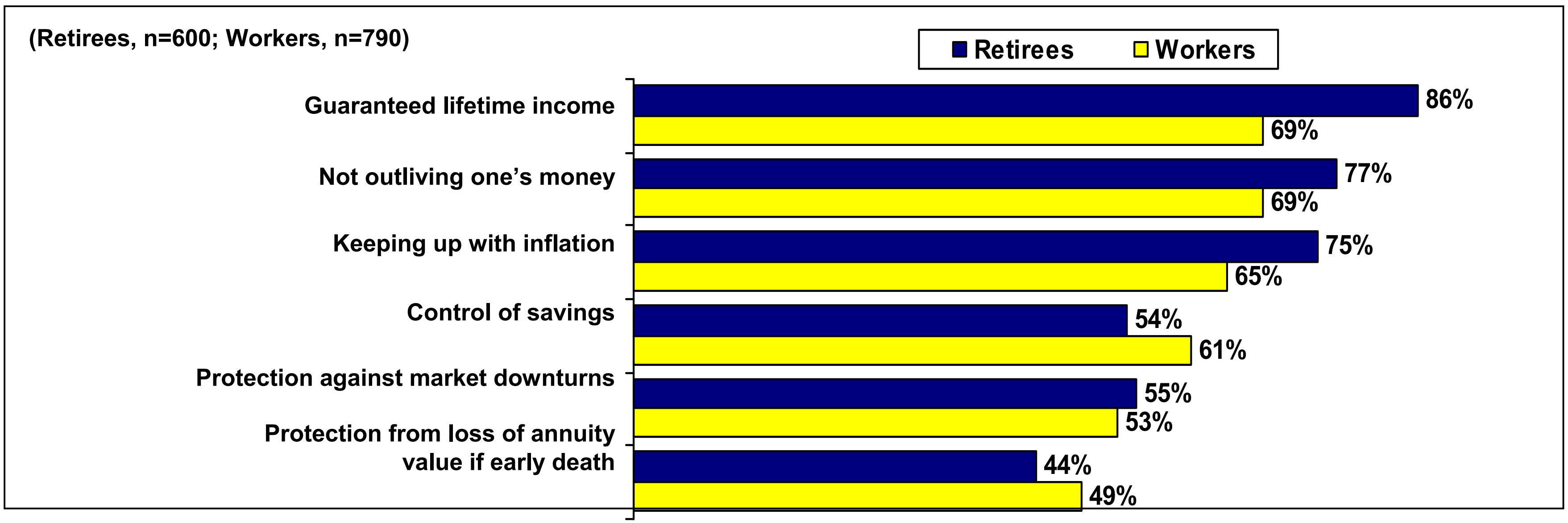
Discussion

These findings tend to contradict anecdotal evidence from private pension plan sponsors, who report high rates of lump sum elections. There is a need to understand in more detail what is meant by lifetime income and how decisions about choosing lifetime income, other regular non-guaranteed income, and other methods of asset management are chosen.

Rejection of annuity options may lie partly with concerns of perceived loss of value on early death. These concerns might be partly alleviated by product design, but may also require attention from public policy makers for a complete solution.

In the report in this series on the longevity risk, while a majority of those surveyed had a reasonable perception of average longevity at age 65, few understood the significant probabilities—30% of women and almost 20% of men—of surviving to age 90. This suggests that even greater attention be given to the importance of considering lifetime income options when choosing the form of payout from a retirement plan.

When deciding on what payout option to choose from your retirement plan, how important are each of the following? (percentage saying *very* important)



Source: 2003 Retirement Plan Preferences Survey

Managing Retirement: Assets and other Issues

Focus groups conducted in the fall of 2005 looked at how retirees manage assets, and probed their understanding of post-retirement risk. The results can be found in the the SOA/LIMRA study entitled “**Spending and Investing in Retirement—Is There a Strategy?**” The findings included the observation that retirees did not focus on long-term issues well. When asked to rank a variety of risks, the composite ranking of the groups from most to least risky was:

1. Inability to afford health care;
2. Inability to afford long term care;
3. Inflation;
4. Investment;
5. Inability to maintain lifestyle;
6. Outliving Assets

This ranking of concerns expressed by retirees may reflect the degree of control they feel they have—little or none over health care costs and inflation, and not much over their own needs for long term care. While they have no control over financial markets, they feel they can modulate their own investment risk to some degree through changing asset allocation or exiting the market. They feel less concern over maintaining lifestyle because they do have some control over their expenses and, to the extent that they manage them, some control over outliving their assets.

The following advice offered by retirees to the next generation on how to achieve a financially secure retirement reflects both what they have done themselves, and steps they wish they had taken:

- Pay off all debt before retirement.
- Begin to save for retirement as soon as possible.
- Invest in real estate.
- Have extra money for cares and emergencies.
- Get health insurance coverage.
- Make a list of the things you really want to do in retirement.

Comparisons of 2005, 2003 and 2001 Results; Relationship to Focus Group Findings

Finding

Among retirees, the levels of concern regarding the retirement risks examined in this study have remained relatively consistent since 2001. Among pre-retirees, however, concern about many of these risks returned to 2001 levels after an increase in 2003. For example, four in ten pre-retirees in 2003 said they were *very* concerned about their ability to keep the value of their investments up with inflation. Yet, in 2005, just one-quarter of pre-retirees express this level of concern (26%), comparable to the 24% who said *very* concerned in 2001. Pre-retirees also showed decreased levels of concern about:

- having to deplete all of their savings and being left with only Social Security (36% *very* concerned in 2003, 28% *very* concerned in 2005);
- their ability to maintain a reasonable standard of living for the rest of their life and their spouse's (20% *very* concerned in 2001, 34% *very* concerned in 2003, 23% *very* concerned in 2005); and
- their spouse's ability to maintain the same standard of living if they should die first (17% *very* concerned in 2001, 25% *very* concerned in 2003, 16% *very* concerned in 2005).
- On the other hand, pre-retirees were more likely in 2005 (75%) and in 2003 (79%) than in 2001 (58%) to indicate they are concerned about their ability to afford adequate (2005) or good (2003/2001) health care.

Discussion

The findings of the focus groups detailed in the SOA/LIMRA study entitled "**Spending and Investing in Retirement—Is There a Strategy?**" tend to reinforce the results of the risk surveys. Retirees are not as focused on longer term issues as they are on the shorter term. The longevity risk in particular**—**outliving one's assets**—**is seen as a relatively lower risk than the inability to afford health care and long term care. Retirees had various degrees of awareness of annuities and long-term care insurance, but generally did not buy such risk management products. Their evaluations of whether they should retire or could afford to retire were somewhat intuitive and based more on near-term evaluations of spending. Their focus on discontinuities and major possible changes to their retirement plans was limited, and few had made long-term estimates of retirement risk.

Note: In comparing the results of the three studies, major events and conditions during the period from 2001 to 2005 should be reflected. The 2001 study field work was done in August, 2001, about a month before the events of September 11, 2001. Investment market conditions were more volatile between the 2001 and 2003 studies but somewhat more stable between 2003 and 2005. Neither period had the good investment results of the 1990s, but 2003–2005 was further away in time from that period. It appears that risk awareness was generally higher in 2003, but had receded somewhat by 2005.

Retirement security for much of the population has traditionally depended on having programs that work without individuals having to make decisions or take action. Currently, Social Security and defined benefit plans are such systems, and they are extremely important. Defined contribution plans, by contrast, vary in the extent to which they operate without individual action. Decisions to opt in and decisions to opt out of such plans are not symmetric, because many employees accept defaults. Increasing focus is now placed on using default options that produce consistent savings patterns including:

- Automatic enrollment
- Automatic increases in savings
- Balanced funds as default investment options

More focus is needed on default distribution options. Even when people say that they are going to take action, they often do not. Mitchell and Utkus report on a study in which, after education, 100% of employees not participating said they planned to enroll in the 401(k) plan, but over the following six months, only 14% did enroll. 28% of the attendees said that they planned to increase their contribution rates, but only 8% did so within six months. 47% said that they planned to change their fund selection, but only 15% did so within six months. **[7]**

7. Mitchell and Utkus, Pension Design and Structure, p. 11

Research reveals major gaps in the public's understanding of risk. In spite of the need for individuals to assume more responsibility for financing their retirement, these gaps are not closing. Defined contribution 401(k) plans have been in existence since 1980, and many employers have been trying to educate employees about investing their plans and saving for retirement. While financial education helps some people, there is also evidence that many are not interested in advancing their financial awareness, and that it has little influence over their decisions.

An emerging body of knowledge provides new insights into how people understand and deal with risk and uncertainty. One financial planning group segments society according to interest in, knowledge of, and ability to manage retirement risk. This kind of information should be considered together with the surveys and research presented in this report. Readers interested in learning more about economic behavior as it applies to pensions may wish to consult *Pension Design and Structure: New Lessons from Behavioral Finance*.[5] This work contains a discussion of some of the following considerations that make retirement savings difficult:

- The payoff for behavioral change is quite uncertain;
- Workers do not easily buy into the idea of payoffs in the distant future;
- The promise of pleasure tomorrow is perceived as meaning pain today;
- Wrong decisions may yield instantaneous gains;
- There is no immediate tangible reward for saving now;
- Savings decisions can be postponed without immediate penalty; and
- There are no specific functional deadlines for action.

The following comments from *Pension Design and Structure* are of a study of how people make decisions:

- Long-term thinking is foreign to many people;
- More choices are not necessarily better than fewer choices; for many people, too much choice is confusing;
- There is no time for trial and error in making decisions; however, since bad results are likely to emerge after a period of years rather than immediately, it will be a while before results are recognized.
- Many Americans are not skilled in the mathematics of finance and do not understand compound interest. That makes it very challenging for them to understand long term savings and the impact of inflation.
- In influencing how people act and think, personal experiences make for a much more powerful message than statistics and probabilities.[6]

5. *Pension Design and Structure: New Lessons from Behavioral Finance* Olivia Mitchell and Stephen Utkus, Oxford, 2004
6. *Pension Design and Structure,* Gary Selnow p.45

Conclusions

Retirees face a range of risks during the post-retirement period, **health care**, **inflation**, **investments** and **longevity** leading, in that order, the list of their concerns.

Some retirement benefits such as Social Security, Medicare, and traditional defined benefit pension plans, are paid either as regular monthly income or provide ongoing benefits with built-in protection against specific risks. Defined contribution plans and personal savings offer no such protection, and retirees depending on them are responsible for managing many post-retirement risks on their own. This series of reports provides insights about what those nearing retirement and those already retired say about these risks and the use of various strategies for managing them. It reveals major gaps in their understanding of these risks and in the techniques for dealing with them. Examples of the challenges are:

- Longevity risk is poorly understood and not planned for. This is a particularly serious issue for women since they live longer. Also, since women have traditionally tended to be younger than their spouses or male partners, their greater longevity exposes them to the risk of lengthy widowhood.
- Premature retirement risk is greater than generally recognized. About 40% of Americans end up retiring earlier than they planned to retire, usually as a result of job loss, family needs, including health issues, or personal poor health.
- Many people do not understand investments or how to make the financial management decisions necessary for a secure retirement. For example, many do not even understand what a money market fund is.
- A substantial number of people believe that the common stock of their employer is less risky than a diversified portfolio of common stocks.
- Many people do not save enough, do not estimate their needs well, fail to consider the impact of future inflation, and some have changed jobs so frequently that they have accrued no pension benefits if these are not vested when they change jobs

These challenges are all the greater because many people are not focused on the long term, significant numbers of retirees and pre-retirees are not sufficiently aware of the financial risks inherent in retirement, or of the techniques for managing their impact. Even among those aware of the risks and the means to insure against them, too few are moved to take action. Often, awareness does not seem to translate into action and changed behavior.

Other risks that for all practical purposes are beyond the retiree's control, and for which little protection currently exists, have only been vaguely alluded to in the report. These are corporate fraud and mismanagement leading to the impoverishment of pre-retirees and retirees with a majority of their defined contribution plans invested in company stock, and the risk of a continuing care retirement community going bankrupt. Added to this list for consideration in future reports of this nature is the still limited, but growing practice of companies declaring bankruptcy as a corporate strategy to relieve themselves of employee benefit obligations. It can only be hoped that issues of this degree of seriousness will eventually be addressed at the Congressional level.

This report should serve as a call to action by employers and employees, and by all groups advocating for employees and retirees, to accelerate the enormous task of preparing the Baby Boom generation for the challenges it faces as retirement looms.

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To Obtain a Copy of the Complete Survey Report

The 2005 Risks and Process of Retirement & Survey report may be obtained from the web site of the Society of Actuaries at www.soa.org.

Glossary

ADEA—The Age Discrimination in Employment Act, 1967 and as subsequently amended.

Baby Boomers; Baby Boom Generation—Those born in the US from 1946 through 1964.

Defined Benefit—A retirement plan in which the pension benefit is expressed as a monthly or other periodic amount based on a formula typically reflecting earnings and years of service.

Defined Contribution—A retirement plan in which contributions to each participant's account are typically a percentage of earnings, subject to certain statutory limits in the case of qualified plans. Many of these plans allow employees to save on a pre-tax basis with an employer match.

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.

High Income—An arbitrary amount of income or earnings which, for the purpose of these reports, is assumed to be in excess of $100,000 annually for a family of two.

High Net Worth—An arbitrary amount of retirement savings, including defined contribution pension account balances, aggregating $1million or more for a family of two.

Inflation—Annual increase in the Consumer Price Index as measured by the US Bureau of Labor Statistics; it may be for all consumer items, or for specific subsets such as medical care.

Joint and Survivor Annuity—An annuity issued on two individuals under which payments continue in whole or in part until the second of the two dies (also called joint life annuity).

Life Expectancy—The average future remaining lifetime for a cohort of people at a specific age. For all Americans, life expectancy at birth in 2005 was 78; for females 80, and for males, 75. At age 65, life expectancy for males is 17 years, and for females, 20 years. Source: US Bureau of Census Tables.

Maximum Life Span—The maximum possible extent of human longevity, generally taken by gerontologists and actuaries as 120 years. Two thoroughly documented cases are of the Japanese, Shigechiyo Izumi, who died in 1986 at the age of 120, and of Jeanne Calment, who was born in Arles, France in February, 1875, and died there also in August, 1997 eight days short of 122½ .

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.

Pre-retiree—Anyone still in the work force who has reached an arbitrary age—typically set around 50—at which planning for retirement begins to become a serious prospect. For the purposes of the 2005 Risk and Process of Retirement Survey, pre-retirees are at least age 45.

Qualified Plan—A pension plan under which contributions meet certain standards set by the IRS to be tax deductible for the plan sponsor and are tax-deferred to the participant. These plans are subject to numerous rules in order to maintain the favorable tax status.

Retiree—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 2005 Risk and Process of Retirement Survey, respondents have been classified as retired either through self-definition or if they have retired from their primary occupation.

Retirement—Exit from one's job or occupation, typically at an age at which the individual has no expectation of returning full-time to the labor force.

Risk—Exposure to the probability of an event that will occur with certainty, but with unknown timing—death—or that may or may not occur, such as accident, sickness, becoming disabled, or outliving one's assets.

SIPP—The Census Bureau's Survey of Income and Program Participation.