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AGING AND AMERICA: DEMOGRAPHIC CHANGE AND ITS CONSEQUENCES FOR WORK AND RETIREMENT

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EXECUTIVE SUMMARY

In 2012, the National Research Council of the National Academy of Sciences issued a comprehensive report documenting the aging of the U.S. population and analyzing the economic effects this phenomenon may trigger over the next 40 years. The report, *Aging and the Macroeconomy: Long-Term Implications of an Older Population,* identified two potential policy strategies for mitigating the economic consequences of population aging: 1) enabling people to increase their savings for retirement; and 2) encouraging people to postpone retirement by working longer. [1]

In November 2013, the TIAA-CREF Institute and the Alfred P. Sloan Foundation sponsored a colloquium of researchers and policy analysts to discuss how to help people save more and work longer.[2] The colloquium, *Towards a Policy Agenda for an Aging America,* began with a panel during which the key findings and implications of the National Academy report were reviewed. A second panel discussion focused on improving the planning and saving behavior of American workers. Senator Tom Harkin, chair of the Senate Health, Education, Pension and Education Committee, then gave a keynote address, presenting his perspectives on enabling people to save more by improving the U.S. public and private pension system for workers. A final panel focused on research and policy initiatives for longer work.

1 National Research Council. (2012). Aging and the Macroeconomy. Long-Term Implications of an Older Population. Committee on the Long-Run Macroeconomic Effects of the Aging U.S. Population. Board on Mathematical Sciences and their Applications, Division on Engineering and Physical Sciences, and Committee on Population, Division of Behavioral and Social Sciences and Education. Washington, D.C.: The National Academies Press. The report is available at: http://www.nap.edu/openbook.php?record_id=13465.

2 The colloquium was sponsored by a generous grant to the TIAA-CREF Institute from the Alfred P. Sloan Foundation. Colloquium presentations are available at: https://www.tiaa-crefinstitute.org/public/institute/convenings/upcoming-past-convenings/jointcolloquium2013.

Financial Services

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Key findings from the colloquium are described below, under the broad themes of saving more and working longer.

SAVING MORE

1. Creating a more holistic and integrated retirement income system requires defining the relative responsibilities of individuals, employers and government for assuming the risks inherent in financing retirement income, such as investment, interest rate and longevity risks. It also entails addressing the challenges posed by changing labor force participation rates, as well as changing job mobility and retirement patterns. Health and long-term care insurance should also be integrated into the system.

2. The objective of saving for retirement should be to provide an adequate and secure income throughout retirement. This implies leveraging annuity products to insure against outliving accumulated savings.

3. Unlike the 403(b) model in higher education, most private sector 401(k) plans do not offer an annuity payout option, primarily due to fiduciary concerns of plan sponsors. Proposals to address this include a safe harbor provision for in-plan lifetime income options, clarity regarding the fiduciary exposure associated with in-plan lifetime income options, classifying products with a lifetime income component as Qualified Default Investment Alternatives (QDIAs), and allowing deferred annuitization through longevity annuities under required minimum distribution rules.

4. Low levels of financial literacy and poor personal financial management practices are barriers to long-term financial security. For example, financial literacy is generally low even among college-educated millennials who are nonetheless confident in their ability to manage day-to-day financial matters. But debt is widespread among this group, as is worry about repaying debt. More fundamentally, their debt is associated with poor financial management, such as expensive credit card practices and tapping into retirement accounts.

5. There are signs of an emerging, bipartisan consensus that pension reform should expand retirement plan coverage across the workforce, maintain or expand tax incentives for retirement savings and plan sponsorship, and promote financial education efforts. In the absence of federal action, various states are proceeding with initiatives to promote retirement income security for the public sector workforce, and private-sector workers as well.

WORKING LONGER

1. Data indicate that labor force participation is already increasing among older workers. But workers with lower education levels remain less likely to continue working due to a combination of health issues and jobs that tend to be more physically demanding.

2. Many workers change jobs after age 50; this may or may not involve a change in occupation. While the new jobs often pay less, they tend to involve less physical labor and less managerial responsibility. Many job changers report increased enjoyment in their work.

3. While there is limited research to date of labor market demand for older workers, existing research indicates significant growth in older worker employment in the service sector, where jobs are characterized by limited physical demands, flexible schedules, opportunities for social interaction and relatively high levels of job satisfaction. In the service sector, an increased demand for older workers has been associated with increased wages, a decreased outflow of older workers, and an increased inflow of older workers from other sectors and out of retirement.

4. Research indicates increased labor force participation among older workers after the passage of state and federal protections against age discrimination in employment. It further indicates that anti-discrimination laws complement the effect of Social Security reforms intended to increase work lives and delay benefit claiming.

5. Strategies to reengineer the workplace for an aging population include flexible work schedules to help individuals balance work with family caregiving responsibilities; continuing education to address changing technology and knowledge requirements; and reorganization of how and where people work to promote knowledge transfer and a new social contract between young and old employees.

6. The federal government has become a leader in the use of phased retirement. Such programs can lengthen work-lives and ease the transition into retirement by allowing older employees to work part-time for pro-rata salary. Beginning in 2014, some 100,000 federal employees are projected to take phased retirement each year, resulting in a $450 million reduction in annual payroll costs. At least 20% of the phased work time will be devoted to mentoring younger workers.

AGING AND THE MACROECONOMY: MAJOR FINDINGS AND IMPLICATIONS OF THE NATIONAL ACADEMY STUDY

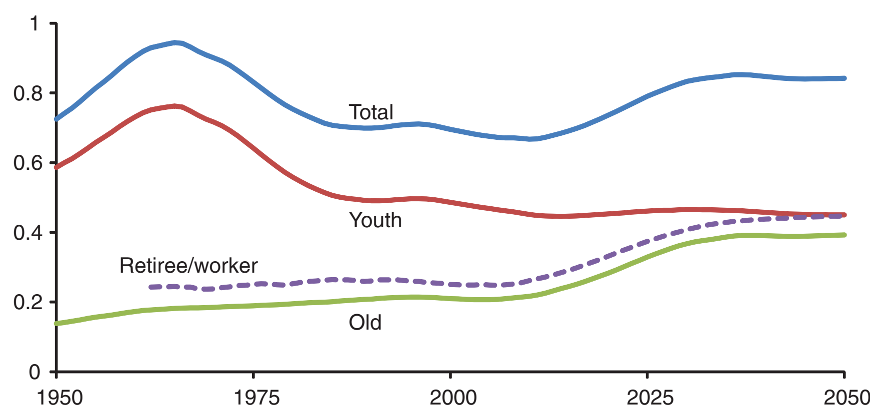
The colloquium, *Towards a Policy Agenda for an Aging America,* opened with a panel discussion moderated by Dr. Paul Joskow, president of the Sloan Foundation, during which the key findings and implications of the National Academy report were reviewed. The panel featured three members of the National Academy study committee: co-chairs Roger Ferguson, president and CEO of TIAA-CREF, and Ronald Lee, professor of demography and economics at the University of California at Berkeley, as well as Charles Lucas of Osprey Point Consulting.

Paul Joskow began by observing that the National Academy report provides an excellent analysis of the demographic shifts now under way and the financial and economic challenges they present. The price for increased longevity may be that people will have to, or may want to, expand the time they spend in the labor force.

In the United States, the ratio of older Americans (age 65 and older) to adults (age 20 – 64) is projected to increase by 80% over the next 40 years. Ronald Lee explained that the phenomenon of population aging is related to two demographic trends in recent decades: increased lifespans and decreased fertility rates.

- Fertility rates are falling. In 1957, the U.S. fertility rate was 3.7 births per woman. In 2010, the rate was slightly less than 2.1 children per woman. As a result, the ratio of younger to older age individuals has fallen as well, leaving fewer potential workers to support retirees.

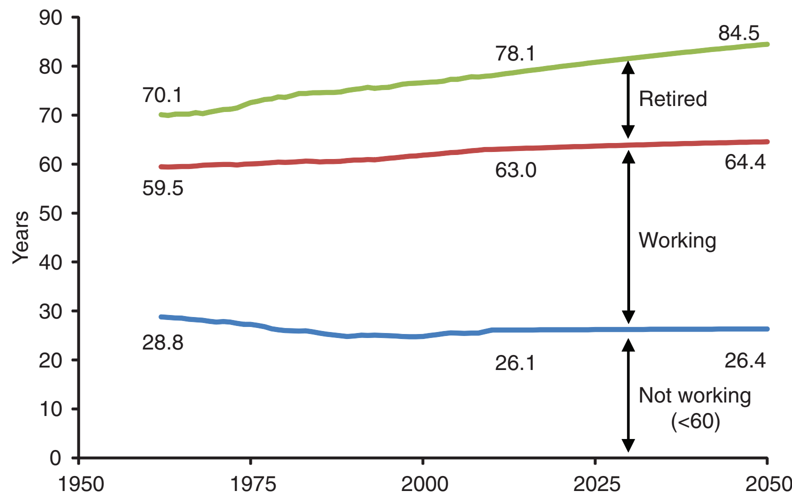
AGE DEPENDENCY RATIOS FROM 1950 TO 2050



Source: Figure 3-13 from the National Academy Study, page 51.

- Longevity is increasing. Due to lower mortality rates and improved health status, life expectancy in the U.S. has risen from 47 years in 1900 to 78 in 2014. By 2050, it is expected to reach 85 years. Disability rates also have declined, although the future trend for disability is not clear.

RETIRED YEARS AS A PROPORTION OF WORKING YEARS AND OF LIFE EXPECTANCY FROM 1962 TO 2050



Source: Figure 3-2 from the National Academy Study, page 37.

The demographic shift to an older population is in many respects good news. People are not only living longer, but they are living more active, healthier lives in retirement. Yet, new policies will be needed to meet the economic and social challenges ahead. For example, as a result of these changes, the normative retirement age of 65 is becoming increasingly obsolete as a social policy. Growing numbers of Americans will be able to work longer than that, while still enjoying many years of retirement in good health. Also, there has been a major shift in consumption patterns by age, with older individuals now consuming much more than younger people. This is largely due to the growth of public-sector support programs for the elderly, particularly pensions, health care and long-term care. This growth has in turn resulted in increased financial pressure on major social programs like Social Security and Medicare.

Roger Ferguson stressed that the demographic shift to an older population documented in the National Academy study is a global phenomenon. While the U.S. population is indeed getting older, more extreme trends can be observed in Southern Europe and Asia. He also noted that population aging will have a disparate effect on different demographic groups. For example, the lives of women and men differ in ways that will affect their ability to save more and work longer. Although the differences have narrowed somewhat, women as a group still earn less on average than men and spend less time in the labor force. Financial literacy is another key issue, as significant numbers of workers are not saving and preparing adequately for retirement.

Charles Lucas observed that the origin of the aging phenomenon is not the baby boom, but the worldwide drop in fertility rates associated with economic development. He also noted that in the U.S., Social Security and Medicare will face increased political pressure to cut benefits. But if benefits are cut, the country will have to decide what social supports should be provided to older Americans with a low capacity to save, low income histories or both.

Ronald Lee noted that population aging presents many economic risks for the future, requiring new forms of financial instruments to manage them. In particular, the rate of inflation poses risks for retirement savings. Although the current inflation rate is very low, it will present a threat to financial security in retirement as it rises in the future. Roger Ferguson said that financial innovation through the development of such instruments as inflation-protected annuities will be helpful. However, the fundamental challenge will be to enable people to save a sufficient portion of their income over time, so that they can replace an adequate share (at least 70% to 80%) of their working income in retirement.

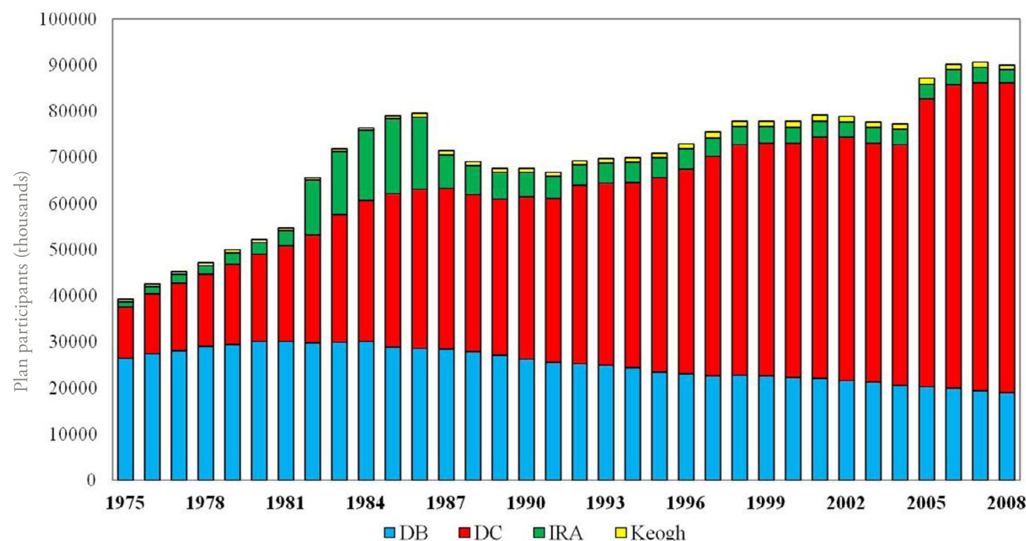
The National Academy study notes that, "while population aging does not pose an insurmountable challenge to the nation, it is imperative that sensible policies are implemented soon to allow companies and households to respond." One major policy initiative suggested in the report is saving more, because "to the extent that people have prepared for [retirement] by starting to save and accumulate assets early in their working lives, the problem is reduced." A second recommended strategy is working longer, because "raising the average age of retirement is one key alternative to…enhancing people's ability to stretch their assets over their lifetimes."[1]

SAVING MORE FOR RETIREMENT: WHAT CAN BE DONE?

After reviewing the extensive literature on the adequacy of retirement saving, the National Academy study concluded that between one-fifth and two-thirds of the older population has accumulated insufficient financial assets for retirement. The report also noted a significant shift in the relative responsibilities of employers and employees for providing retirement income.

Financial resources for retirement in the U.S. are strongly related to participation in a workplace retirement plan. But plan sponsorship is voluntary on the part of employers and only about 50% of workers have access to a workplace retirement plan. In addition, since the 1980s, the private sector retirement system has evolved from one where the primary plan type was typically a defined benefit (DB) plan to one where defined contribution (DC) plans are now dominant. DB plans remain the dominant primary plan type in the public sector.

PENSION PLAN PARTICIPANTS IN THE PRIVATE SECTOR BY PLAN TYPE, 1975-2008



Source: National Academy Study Summary Report, page 3.

DB plans pay monthly benefits that begin at retirement and continue for the life of the retiree (and maybe the retiree's spouse). Benefit payment amounts are generally determined by the participant's job tenure and end-of-career income level. Employees are automatically enrolled. They are not typically required to make funding contributions in private sector plans; they do typically contribute in public sector plans. The employer is responsible for ensuring adequate funding to support earned benefits.

1 National Research Council. (2012). Aging and the Macroeconomy. Long-Term Implications of an Older Population. Committee on the Long-Run Macroeconomic Effects of the Aging U.S. Population report in brief. Committee on the Long-Run Macroeconomic Effects of the Aging U.S. Population. Board on Mathematical Sciences and their Applications, Division on Engineering and Physical Sciences, and Committee on Population, Division of Behavioral and Social Sciences and Education. Washington, D.C.: The National Academies Press. Available at: http://sites.nationalacademies.org/xpedio/groups/depssite/documents/webpage/deps_072649.pdf.

The retirement benefit in a DC plan is the accumulated balance in a worker's account. The employee and/or his employer make contributions to the account. Those assets are invested at the discretion of the employee given investment options provided by the plan. In the private sector 401(k) model, employee participation is voluntary, the employee contribution rate is discretionary, and any employer contribution is in the form of a match. Employees are responsible for converting their account balance into income during retirement. Worker savings decisions, in particular regarding how much to save, are a major issue of concern with the 401(k) model. Innovations such as auto-enrollment, sometimes combined with automatic contribution rate increases, and target-date investment funds are having a positive impact, however. In other sectors, such as higher education, primary DC participation is mandatory with nondiscretionary levels of employee and employer contributions and the option to annuitize at retirement.

The second colloquium panel—*Saving More for Retirement: What Can be Done?*—focused on improving the planning and saving behavior of American workers. The panel was moderated by David Richardson, senior economist at the TIAA-CREF Institute, and featured remarks by Jeffrey Brown, professor of finance, University of Illinois at Urbana-Champaign, and TIAA-CREF Institute Fellow,; Brigitte Madrian, Aetna Professor of Public Policy and Corporate Management, Harvard University, and TIAA-CREF Institute Fellow; Debra Whitman, executive vice president of policy, strategy and international affairs at AARP; Preston Rutledge, tax and benefits counsel of the Republican Tax Staff of the Senate Finance Committee; and Paul Yakoboski, senior economist at the TIAA-CREF Institute.

Brown opened the panel by arguing that a focus on increasing retirement savings is too narrow. A broader conversation on promoting and improving retirement income security is needed. He noted that the objective in saving for retirement is to maintain a current or desired standard of living once retired, not merely to accumulate a lump sum of wealth that is available in retirement. Adequate savings are necessary for ensuring that living standards are maintained, but achieving lifetime income security requires converting savings into an income stream that the retiree cannot outlive. This means the focus of retirement saving needs to move from wealth accumulation to sustaining retirement income.

Brown maintained that the 401(k) system as currently structured is not focused on lifetime income. In particular, he noted that less than one in five 401(k) plans offer an in-plan annuity or any other lifetime income option. He attributed this, in part, to a history of fiduciary standards that discourage plan sponsors from doing so. From a fiduciary perspective, it's simply safest to not offer an annuity. Brown argued that plan sponsor perceptions about the level of fiduciary risk inherent in offering an in-plan annuity need to change.

Brown cited the absence of lifetime income products as qualified default investment alternatives (QDIAs) under the Pension Protection Act as another example of how the current system discourages a focus on lifetime income. He also explained that minimum distribution rules, which were written from the perspective of tax policy, not retirement income security, tend to encourage account holders into taking distributions at levels that are unlikely to be sustainable over a lifetime.

In other areas, Brown noted that participant communications, such as account statements, tend to focus on account balances rather than retirement income, further contributing to a wealth accumulation mentality. To highlight the impact of communication, he discussed research demonstrating that the framing of information – i.e., how financial products are presented to consumers – can significantly influence relative preferences for retirement savings products. Specifically, when product descriptions emphasize consumption, 72% of those surveyed preferred a life annuity over a savings account. In contrast, when the same products were presented using investment terminology, only 21% of respondents preferred an annuity. When consumers think in terms of consumption, they perceive life annuities as offering valuable insurance against the risk of outliving one's savings. However, when they think in investment terms, they view life annuities as increasing risk without increasing return.

Brown concluded by arguing that the DC system provides a strong foundation upon which to build a better retirement system, noting these strengths:

- Four out of five full-time civilian workers are covered by some form of employment-based plan.
- Participations rates in DC plans generally fall in the 75% to 80% range.
- Median contribution rates to DC plans (employer and employee contributions combined) are often around 10% in certain sectors, which is consistent with the minimum necessary for targeting an adequate retirement income.

An additional strength noted by Brown is the DC system's tendency to evolve when policymakers and plan sponsors agree that it's important. For example, auto enrollment has dramatically increased participation rates, particularly among lower-income workers. Auto escalation provides an effective means to increase individual savings rates over time. Investment diversification has improved due to both qualified default investment alternatives (QDIAs) and the declining role of employer stock in sponsored plans. And a majority of plans now allow for immediate participation, which is particularly valuable given worker mobility patterns.

Brown argued that the system needs to evolve further to address low coverage rates among workers at small employers and among part-time, low-wage workers. He maintained that this would entail reducing barriers that small employers face in sponsoring retirement plans, and possibly increased incentives for sponsoring plans.

More fundamentally, Brown emphasized the imperative for changing the focus of public policy conversations from retirement savings to retirement income security. To this end, he suggested that the Department of Labor provide a safe harbor provision for in-plan lifetime income options and in the interim provide additional clarity regarding the fiduciary exposure of offering such options. He also called for expanding QDIAs to include products with lifetime income components, enhancing disclosure rules so that plans report both account balances and retirement income projections, and revisiting required minimum distributions.

Brigitte Madrian discussed the need to base retirement income policy on a holistic, integrated view of the U.S. system. The current system, in contrast, was built piecemeal over many decades to address various needs. For instance:

- Social Security was created in the 1930s to help provide financial security to workers and their families.
- Wage and price controls during World War II led employers to compensate workers with non-wage benefits, such as health insurance and pensions.
- Medicare was implemented in the 1960s to address retiree health care needs.
- ERISA was passed in 1974 to regulate retirement plans.
- The Revenue Act of 1978 added Sec. 401(k) to the internal revenue code.
- Medicare part D was created in the mid-2000s to subsidize the costs of prescription drugs for Medicare beneficiaries.

Madrian noted that a holistic, integrated view of the retirement income system would consider elements typically overlooked by piecemeal thinking, such as:

- The effects of changing labor force participation, job mobility and retirement patterns.
- Individuals who are physically unable to work until prescribed retirement ages.
- The integration of health and long-term-care insurance into a retirement income system.
- Adequate longevity insurance.
- Access to retirement savings before retirement.

Madrian also discussed several big-picture issues, the first being the relative responsibilities of individuals, employers and government for financing retirement income security. She noted that Social Security replaces as much as 85% of income for workers in the lowest income quartile, but overall replaces about 40% to 50%. What replacement rates should be provided under Social Security? At the same time, how large a role should employers be expected to play and what should they be expected to provide? As for individuals, what's the expectation for deferring consumption while working to finance consumption once retired?

An issue closely related to financing retirement is risk bearing. Risk is inherent in any retirement system; the question is how much should each party (individuals, employers, government) bear of the various types of risk, including investment, interest rate, health care, and individual and cohort longevity? Madrian argued that one party should not bear all the risk, or even all of one type of risk, calling instead for risk diversification across broad groups of individuals and institutions. How can we design a system that manages risks across individuals and institutions in the most sensible way?

These questions have no obvious or agreed-upon answers, but they influence plan type and design decisions. For example, what are appropriate deferral rates in a DC plan, both for the participant and the sponsor? Should DC participation be mandatory with nondiscretionary levels of contributions specified for participant and sponsor, as some public sector plans are designed? Some public employee retirement systems allow workers to choose between participating in a primary DB or a primary DC plan, or a hybrid arrangement. Should participants generally have such discretion over plan type?

In working through these questions, Madrian explained that it's important to recognize and understand that what is optimal for the individual may not be optimal for society, and vice versa. This point is often lost in public discourse. She maintained that disagreements about system design and reform can result from one party advocating what would be socially optimal while another advocates what would be optimal for the individual, with a significant gap between the two. Without recognizing and acknowledging the underlying premises of each side's argument, it's inevitable that the two will disagree. What's individually optimal will drive individual behavior in any system, but the system's first focus needs to be on what's socially optimal. Still, both issues need to be considered and understood.

Madrian explained this phenomenon in the context of a social safety net. Moral hazard will lead individuals to save less because a backstop exists in the event that they don't have enough. This implies that a minimum level of mandatory savings or mandatory annuitization might be socially optimal, even if it is not individually optimal.

Debra Whitman discussed several problems she sees with the current U.S. retirement system:

- Lack of employment-based retirement savings plans for too many workers.
- Weak tax incentives for encouraging low-income workers to save.
- The need for better products for creating retirement income.
- Lack of financial education and understanding concerning the importance of saving.
- Fears among workers that they will outlive their savings in retirement.
- The absence of a strong political consensus to address retirement income security.

Whitman also noted several strategies to address these issues:

- Ensure all workers have access to a retirement savings plan that incorporates auto-enrollment and auto-escalation of worker contributions.
- Protect and expand tax incentives for retirement savings across all income levels, particularly for people of low and moderate income.
- Maintain and expand existing tax credits for retirement savings.

- Improve public education on the importance of saving for retirement, the amount of income Social Security can provide, and savings needed to fund a retirement lasting 40 years or more.
- Focus attention on the importance of lifetime income and lifetime income products.
- Encourage later retirement among those who can work longer, both to maximize benefits from Social Security – which is the main source of annuitized, inflation-adjusted retirement income for most retirees – and to help people save more.

Whitman optimistically noted discussions among federal policymakers, often on a bipartisan basis, focused on retirement income security that can lead to important changes. She explained that support is emerging from a wide range of groups that often have different political predispositions, such as AARP and the U.S. Chamber of Commerce, at least on the need to address retirement income security if not yet on the specifics of how to do so. Consensus priorities include:

- Expanding retirement plan coverage.
- Maintaining or expanding tax incentives.
- Providing education to enhance financial decision-making.

Whitman concluded by mentioning that various states are moving forward with their own initiatives to promote retirement income security for private- and public-sector workers. But much remains to be done before private sector reforms are realized through state action.

Paul Yakoboski described how millennials are well positioned to adjust retirement expectations and behaviors as recommended in the National Academy study, simply because of their age. But will they? And what will it take to get them to do so? Yakoboski believes that understanding millennials' current financial behavior is a prerequisite for strategies to engage them in their personal finances and help them build long-term financial security.

Basing his comments on research that he and Annamaria Lusardi, professor of economics and accountancy at The George Washington University, and a TIAA-CREF Institute Fellow, conducted using FINRA's *2012 National Financial Capability Study*, Yakoboski outlined the personal financial practices of college-educated millennials, noting several apparent disconnects between perception and reality. On one hand, there is widespread asset ownership among millennials, and the vast majority of them rate themselves highly in terms of financial literacy and day-to-day financial management. However, actual financial literacy levels, as measured through tests of basic knowledge, are low; the majority of millennials have received no financial education; and evidence of stress abounds in millennials' personal finances.

Yakoboski explained further that college-educated millennials have financial assets – almost all have a checking account and 85% have a savings account. Moreover, 55% own a self-directed retirement account, 49% own a home and 40% have some other form of financial investments. In addition, 85% feel competent dealing with day-to-day financial matters, such as managing checking accounts, credit and debit cards, and expenses.

But focusing on the asset side of the balance sheet without considering liabilities provides a distorted view of millennials' financial profile, as other evidence suggests financial stress and vulnerability. For instance, half of college-educated millennials find it difficult to cover their expenses and pay all their bills in a typical month. Less than 50% are certain they could come up with $2,000 if an unexpected need arose within the next month. Almost 30% have used alternative high-cost borrowing options, such as auto title loans, payday loans, tax-refund advances, pawnshops and rent-to-own stores. Among those with a credit card, almost half carry a balance and incur interest charges, and over 40% engage in other expensive credit card behavior, such as making minimum required payments, incurring late or over-limit fees, and using their card for cash advances.

Underlying young people's financial decision-making is a generally low level of financial literacy. This is not surprising given that only 30% have received some form of financial education. But this knowledge gap stands in sharp contrast with millennials' self-reported financial literacy.

Yakoboski went on to note that debt is widespread among college-educated millennials, as is worry about having too much debt and being able to repay it. Eighty-one percent of college-educated millennials have at least one form of longer-term debt – such as a student loan, home mortgage or car loan – and 44% have more than one. Additionally, 22% have unpaid medical bills. Yakoboski believes that this debt could be having a negative impact on millennials' financial decision-making. For instance, those with longer-term debt are more likely than those without it to:

- Have difficulty covering expenses and paying bills.
- Carry credit card balances and incur interest charges.
- Use their credit card for cash advances.
- Use alternative high-cost borrowing.
- Have overdrawn their checking account.
- Have taken a loan or hardship withdrawal from their retirement account.

COLLEGE-EDUCATED MILLENNIALS REPORT ON LONG-TERM DEBT AND OTHER FINANCIAL BEHAVIOR

	Has longer-term debt	No longer-term debt
Has difficulty covering expenses and paying bills	53%	40%
Carries credit card balances and incurs interest charges	53%	24%
Engages in other expensive credit card behavior	46%	29%
Has used alternative high-cost borrowing	30%	22%
Overdraws checking account	25%	15%
Has taken a loan or hardship withdrawal from retirement account	21%	10%

Source: *College-Educated Millennials: An Overview of Their Personal Finances,* TIAA-CREF Institute and the Global Financial Literacy Excellence Center at The George Washington University.

While it may seem rational to use other sources of credit to make ends meet while paying off longer-term debt, doing so is not viable in the long run without a change in financial circumstances, such as an increase in earnings. Yakoboski further noted that something is different for Gen Y with regards to student loans—there appears to be more of a negative effect associated with student loan debt than with car loans and home mortgages on millennials' finances.

Given the current circumstances, Yakoboski concludes this about college-educated millennials:

1. They would benefit from help with debt management.
2. Engaging them may be difficult as they are unaware of their lack of financial knowledge and they feel good about their day-to-day financial management decisions.
3. Financial literacy cannot be taken for granted, even among highly educated individuals.

Preston Rutledge concluded the panel discussion by reiterating that policy conversations about retirement income security can be misleading, since they tend to be incomplete. These conversations typically involve issues related to accumulation, but too often omit the decumulation phase where the security element lies. He lamented that much has been done to effectively remove the "security" from the Employee Retirement Income Security Act (ERISA). He cited the

example of floor offset plans that received a favorable revenue ruling post-ERISA after having been previously denied pre-ERISA. He also cited the ability to take lump-sum distributions from DB plans as another example.

Rutledge identified three particular challenges to retirement income security:

- Current low interest rates create an incentive for greater risk taking in investment decisions.
- The politics of deficit reduction which continually view the tax preferences afforded employment-based retirement savings plans as a potential revenue source, in particular, reductions in the amount that can be saved on a tax-deferred basis. Rutledge worries specifically about proposals to eliminate catch-up contributions for participants age 50 and older.
- Significant increases in life expectancy will create substantial longevity risk. Rutledge questioned whether DB and DC plans could realistically function in an environment where significant numbers of individuals lived past age 100.

The issue of increasing life expectancies motivated a set of proposals on which Rutledge has worked. The proposals sought to meet the challenges above by leveraging the financial structure of a life insurance company. Rutledge noted that life insurers sell traditional life insurance that protects against the event of premature death when insufficient assets have been accumulated to meet the needs of surviving family members. Life insurers also sell annuities that insure against the event of outliving retirement assets. He noted the former is sometimes referred to as "short life insurance," while the latter is referred to as "long life insurance."

Turning this model to retirement plans, Rutledge noted that they too accumulate assets, invest those assets, and eventually make payments contingent on some event. But life insurers are unique in that they sell both "short life" and "long life" insurance, which implicitly hedges the insurer against the financial consequences of changes in life expectancies. Rutledge maintained that policymakers need to consider leveraging a comparable structure for retirement plans, since providing retirement income security is essentially a life insurance issue.

Rutledge highlighted three proposals emerging from this line of thinking:

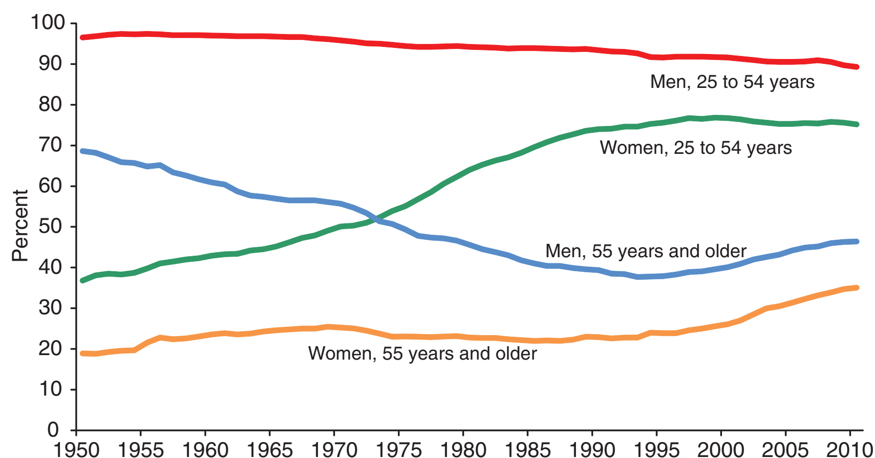
- Provide safe harbor protections from fiduciary duty provisions for employers that choose a life insurer to provide the types of annuity contracts covered by the life insurance guaranty associations. This would provide fiduciary cover for providing a lifetime fixed annuity.
- Change the required minimum distribution rules to allow DC participants to convert up to 25% of account balances into a longevity annuity, such as an annuity that commences payments when the individual reaches age 80.
- Enable state and local governments to sponsor "annuity accumulation plans" for their employees. Each year the employer would purchase a single life annuity contract for each worker. Annual purchases would serve to even out the effect of interest-rate fluctuations on the ultimate annuity payout, i.e., the individual would not risk annuitizing assets at a time of relatively low interest rates. Rutledge explained that annuity purchases equal to 10% of salary each year over a 40-year career would replace two-thirds of final salary under reasonable interest-rate assumptions.

WORKING LONGER: WHAT CAN BE DONE?

As the National Academy report notes, creating policies that encourage longer work lives, and thus postpone the average age of retirement, is one strategy for minimizing the negative economic consequences of an aging America. By working longer, people will have more years to save for retirement, and greater ability to stretch their financial assets in retirement. At the same time, working longer can provide more public resources for major social programs – e.g., Social Security, Medicare and Medicaid – which serve as the predominant support systems for an aging population.

Recent trends in labor force participation suggest that longer work lives are already becoming more common. For most of the second half of the 20th century, the average retirement age among men declined substantially. In 1950, about 70% of men age 55 and older were in the labor force, while only about 40% of men this age were still working by the mid-1990s. Labor force participation by women exhibited very different patterns during this period, as women expanded their presence in the labor force. The participation rate of women aged 24-54 essentially doubled between 1950 and 2000, while that of similar age men declined slightly. For both older men and women, however, the mid-1990s exhibited a pronounced uptick in labor force participation. Increases for men largely occurred among men in their 60s, while all age groups among women increased their labor force participation.[2]

LABOR FORCE PARTICIPATION RATES FOR FOUR BROAD AGE-SEX GROUPS, 1950-2011



Source: Figure 5-2 of the National Academy Study, Page 77.

Projections of labor force participation through 2050 anticipate that the role of older workers will increase substantially as the supply of young (age 16-24) and prime age (age 25-54) workers declines for most of this period. Older workers are expected to offset this decline, and their rate of participation is expected to increase from about 12% in 1990 to 24% by around 2020. The rate will then continue to grow to more than 27% by 2050.[3]

Economists and policy analysts have argued for some time that longer work lives are both feasible and desirable. Yet, while the recent trend in increased labor force participation at older ages has been recognized, little is understood about it. The colloquium's final panel, moderated by Kathleen Christensen, program officer at the Sloan Foundation, focused on research and policy initiatives for longer work. Presenters included Richard Johnson, senior fellow and director of the program on retirement policy at the Urban Institute; Nicole Maestas, senior economist at the Rand Corporation; David Neumark, professor of economics and director of the Center for Economics and Public Policy at the University of California – Irvine; Joseph Coughlin, director of the MIT AgeLab; and Michele Varnhagen, chief policy advisor and labor policy director, Democratic Staff of the Committee on Education and the Workforce of the House of Representatives. Their presentations provided insights into the supply of workers for longer work, the demand by employers for older workers, the design of the future workplace to encourage longer work, and policy initiatives to support it.

2 *Aging and the Macroeconomy. Long-Term Implications of an Older Population*, Page 78.

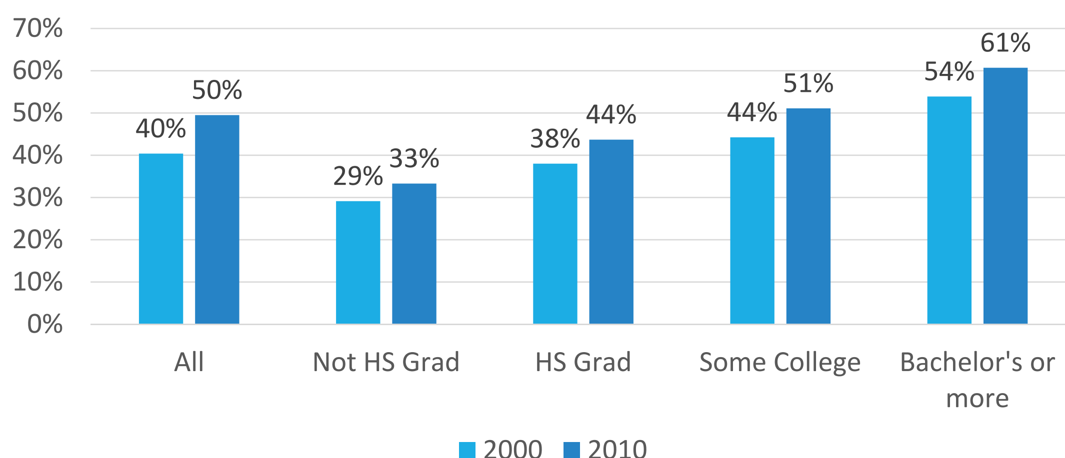
3 *Aging and the Macroeconomy. Long-Term Implications of an Older Population*, Page 80.

A View from the Supply Side: Which Workers Can and Will Work Longer

Creating effective social policies that encourage workers to work longer requires better information about the type of workers for whom this is feasible. Richard Johnson presented results of recent research into key variables that influence people to work longer.[4]

Johnson measured labor force participation of both men and women at ages 62-64 by level of education in both 2000 and 2010. He noted a dramatic increase – from 40% to 50% - for groups at all education levels during this period. Less-educated workers, however, were less likely to continue to work. For example, workers with a bachelor's degree were 50% more likely to work than those with only a high school diploma and were twice as likely to work as those who did not finish high school.[5]

LABOR FORCE PARTICIPATION RATES AT AGES 62-64 BY EDUCATION, 2000 AND 2010



Source: The Urban Institute Program on Retirement Policy, www.retirementpolicy.org.

Johnson also found that workers with less education were more likely to have chronic health issues. While 55% of college-educated adults aged 55-70 in 2008 reported that their health status was "excellent" or "very good," only 33% of those without a college degree did so. Those without a college degree also reported a higher incidence of chronic health conditions such as diabetes (23% vs. 15%), lung disease (12% vs. 6%), heart problems (20% vs. 16%), arthritis (59% vs. 47%) and high blood pressure (57% vs. 46%). The one exception was cancer, which was slightly more common among better-educated workers.

In addition to health issues, workers with less education also reported that their jobs were more physically challenging than those held by better-educated workers. For example, comparing workers without a college degree to those who have one, more reported that their jobs required lots of physical effort (46% vs. 24%), lifting heavy loads (22% vs. 10%), and stooping, crouching or kneeling (24% vs. 12%). On the other hand, fewer workers with less education reported that their jobs involved a lot of stress (54% vs. 64%). Despite the physical or psychological challenges of their jobs, equal numbers (89% vs. 90%) reported that they really enjoyed their work.

In general, nearly 50% of the difference in continued labor force participation between those who did and did not attend college can be explained by health status and chronic health conditions. Among workers who continue to work, many change jobs to another line of work or to another employer. Johnson reported that among people in their early 50s in 1992,

4 This study analyzed data on job characteristics compiled from the U.S. Department of Labor's Occupational Information Network as well as household survey data from the Health and Retirement Survey, the American Community Survey, and the 1980, 1990 and 2000 decennial censuses.

5 Johnson noted that, as a baseline measure, among people aged 55-70 in 2010, less than 44% did not attend college and about 14% did not finish high school. Although the gap in educational attainment has decreased between older and younger generations in the past 30 years, a sizable proportion of the work force will not have a college degree for decades to come.

who were followed through their mid- to late-sixties only 14% remained in their original job. While 43% left the work force entirely, 27% changed careers and 15% moved to another employer. Even among workers with a high school diploma or less, some 40% moved to a new job after leaving their primary employer. These new jobs often pay less but require less physical effort and managerial responsibility, and people frequently report enjoying their work more than they did before.

Johnson concluded that, although the recent recession had an adverse effect on the employment prospects of older workers, some 25% of aged 55+ workers were able to move to new jobs between 2008 and 2010. Going forward, the economy will continue to present challenges for older workers but the observed trend toward longer work lives will continue.

Views from the Demand Side: Employer Demand for Older Workers and Age Discrimination in Employment

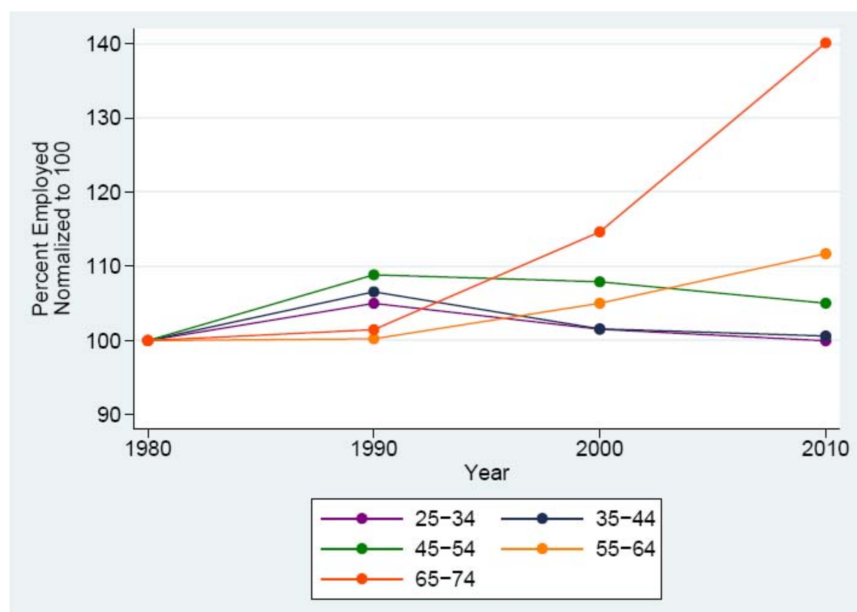
As the pool of younger workers declines over time, labor economists project that older workers will become a valuable resource for employers. To date, however, there has been little research into key questions concerning the interest of employers in hiring and retaining older workers.

1. Where can employer demand for older workers be observed and how do older workers respond to such demand?
2. Do laws to prohibit age discrimination in employment have a positive effect on labor force participation by older workers?

Nicole Maestas, senior economist at the Rand Corporation, discussed employer demand for older workers and its effects on such labor supply outcomes as employment rates, retirement and re-entry into the work force, and claiming Social Security benefits. Her focus was on the service industry, which comprises about one-third of the U.S. employment base. This industry encompasses a wide variety of occupations, from highly paid professions in science, engineering and medicine, to low-wage jobs in food service, personal service, and business and repair services.

Maestas noted that service industry employment of older workers in two categories (age 55-64 and 65–74) increased substantially from 2000 – 2010.[6]

GAINS IN OLDER WORKER PARTICIPATION IN SERVICE SECTOR FROM 1980-2010



Source: Census and American Community Survey.

6 In this study, Maestas analyzed four decades of census data from large metropolitan areas as well as data from the American Community Survey and the Health and Retirement Study.

Maestas measured the effect of a one-percentage point gain in labor demand in the service industry, noting that each age group experienced at least a one-percentage point gain in employer demand over this period. Taking into account the base employment rates for each age group, the gain for workers age 65-74 translates into a roughly 30% increase in employer demand.

In terms of other labor market outcomes, Maestas found that a 1% increase in demand-driven employment translates into almost a 1% increase in staying on the job; about a 7% increase in returning to the labor force; and a 3% decrease in retirement. There is also evidence that this increase in employer demand leads to higher wages—a 4% increase for workers who stay on the job and an 11% increase for those returning to the labor force. Moreover, there is evidence that this increase leads to a 14% reduction in claiming Social Security benefits at age 62, 7% at age 63 and 11% at 64.

Maestas observed that older workers seem to respond to increased employer demand, particularly in industries that offer jobs with less physically demanding work, flexible hours and greater social interaction. If this trend continues, the effects on later Social Security benefit claiming and higher wages for older workers will help offset the detrimental consequences of population aging.

An understudied issue related to employer demand is discrimination against older workers. Beginning in the 1960s, many states enacted statutes against age discrimination in employment, followed by the federal government's passage of the Age Discrimination in Employment Act of 1967. However, age discrimination in the workplace is difficult to examine empirically, as only the most visible instances are litigated on a case-by-case basis and no current estimates exist about its prevalence.

David Neumark discussed his recent research on the topic. He explained that age discrimination laws were passed in part because statistics indicated that older workers stayed unemployed longer than all other age groups except for the very young. Despite the subsequent increased employment of older workers, Neumark observed that it is reasonable to conclude that age discrimination remains important in labor markets.

He then addressed whether stronger age discrimination laws would enhance the effect of Social Security incentives – such as increasing the age for full retirement benefits – designed to encourage longer work lives.

Neumark reported that protections in state laws which are stronger than those in federal law enhanced the effect of Social Security incentives for longer work. In states where stronger remedies are available to plaintiffs, he found evidence of postponed claiming of benefits at age 62 and increased employment among workers age 62 and older. He also found that more workers postponed retirement from the traditional age of 65 to their increased full retirement age under Social Security.

Neumark concluded that reducing demand-side barriers to employment of older workers, such as age discrimination, increases the effect of supply-side incentives for longer work. Even though the prevalence of age discrimination in the workplace is unknown, his research indicates that the presence of strong protective statutes can induce longer work lives.

Views on the Future of Work and Retirement

Keeping older individuals in the workforce longer will require rethinking the organization of the workplace and the nature of work and retirement. Joseph Coughlin observed that population aging necessitates creating a better workplace for all generations, not just a better older person's workplace. According to Coughlin, the process of rethinking both work and retirement is underway. Due in part to the recent financial crisis and recession, the future of old age may involve work for many people. Coughlin pointed to AARP data from 2010 showing that 29% of older baby boomers expect to work into their 70s and 40% expect to work forever.

While some older people work primarily for financial reasons, others work for more personal rewards. The AARP survey found that 35% of older baby boomers returned to work "to do something different." Data from the OECD show that 64% of people continued to work for money, 54% for a challenge, 33% for a sense of personal meaning, and 29% for a social setting.

Changing the workplace to accommodate longer work lives will require substantial changes, including greater flexibility. Creating a balance between work and family, acknowledging the demands of family caregiving, and adapting to part-time schedules are features that support continued employment by older – as well as younger – workers. The future workplace will also need to address worker health and wellbeing. Coughlin noted that costs related to aging begin to climb around age 40 due to increases in chronic diseases as well as increases in work-related injuries and disabilities.

In addition, workers will need to recreate themselves through continuing education as the workplace changes through new technologies and knowledge. The notion of a single, lifelong career is now obsolete. Coughlin noted that younger workers today may have as many as six different careers and workers over age 50 are the largest group seeking additional education today. Online continuing education, certificate learning and career-changing education will be common features of the future workplace.

Coughlin concluded by observing that reengineering the workplace for longer work will require re-thinking how, where and when people retire, especially for those performing physical labor. One key element will be the transfer between generations of skills and knowledge gained at work.

The largest U.S. employer – the federal government – has recently taken significant steps towards reengineering its workforce, including instituting a phased retirement program to encourage longer work through more flexible schedules. Michele Varnhagen explained that Congress is interested in helping employers to provide workers with more options for longer work. For example, the Pension Protection Act (2006) gave private employers some flexibility to enable workers age 62 and older to draw a partial pension while working part-time. But phased retirement programs are still uncommon in the private sector.

Facing the impending retirement of large numbers of federal workers, Congress passed a phased retirement program in 2012. Varnhagen explained that federal employees will have a one-time opportunity to apply for phased retirement, provided they have worked full-time for at least three years at any federal agency and are eligible to retire.

Those accepted into the program will work 50% of their regular hours and begin to draw the equivalent amount of pension. As the program matures, employees will be able to choose reduced work schedules of between 20% and 80% of their hours. For benefit purposes, phased retirees will retain full government contributions for healthcare and life insurance. And they will accrue pension benefits in proportion to their time commitment. Phased retirees will spend 20% of their work time mentoring younger workers.

Varnhagen reported that the Congressional Budget Office has projected that 100,000 federal employees will enter this program each year, decreasing government payroll costs by approximately $450 million annually. Congress hopes that its program will serve as a model for similar programs in the private sector.

THE KEYNOTE ADDRESS: POLICIES FOR SAVING MORE AND WORKING LONGER

In the colloquium's keynote address, Senator Tom Harkin, chair of the Senate Health, Education, Labor and Pension Committee, spoke of the progress during his lifetime in reducing infant mortality and extending life expectancies. He noted, however, that these advances have not been shared equally by Americans across all income levels. He also stressed the consequences that longer lives have for health care costs.

Senator Harkin also pointed out that demographic changes involve long-term trends, so developing and adapting policies in response can also happen over time. In terms of working longer, he cautioned that while phased retirement programs and expanded training opportunities for older workers are important, they will not necessarily benefit workers who have

had physically demanding jobs. He also observed that when workers in their 50s and 60s lose their jobs, many never become reemployed.

In terms of saving more, Harkin stressed the need to improve the public and private pension systems as a means of responding to future economic challenges. He discussed the need to improve the elements of those systems that work, like Social Security. He argued that a move to cut Social Security benefits would be grossly misguided. He has introduced a bill that would increase Social Security benefits by $65 a month, adjust benefits for inflation by changing to the CPI-E index, and remove the wage cap for FICA taxes over a period of years. He explained that these steps would protect the long-run solvency of the Social Security trust fund while strengthening the system for those needing it the most. He noted that it was also important to educate younger workers about the importance of Social Security, not just for themselves, but for their parents and grandparents as well.

Senator Harkin has also proposed a new private saving system called the Universal, Secure and Adaptable Retirement Funds (USA Retirement Funds). This system would require employers without a retirement plan to enroll workers automatically into this program with an opt-out provision. The private sector would operate the USA Retirement Funds through a board of trustees that would act as fiduciaries. Contributions would be held and invested until retirement and then converted into monthly annuities. Benefits would be adjusted, when necessary, for economic conditions. Senator Harkin closed by noting that rebuilding and upgrading the country's infrastructure should be an important priority and that the assets held in USA Retirement Funds could provide some of the long-term funding that such projects will require.

CONCLUSION

As the National Academy study observes,

> An aging society need not have lower living standards, lower growth in innovation and productivity, or inefficiently high tax rates. But delaying decisions on how to adapt to our aging demographic structure will make the transition more difficult and costly. Many adjustments will have to be made, and no single feasible policy change is likely to be either an acceptable or a sufficient response to the dynamic challenge and opportunity of population aging.[7]

Given the National Academy study's call for policies to increase saving for retirement and to promote longer work, the colloquium sponsored by the TIAA-CREF Institute and the Alfred P. Sloan Foundation, *Towards a Policy Agenda for an Aging America*, presented multi-disciplinary and in-depth research findings and explored expert opinions designed to lead to the formulation of such policies. This report summarizes and synthesizes the expertise and thinking shared at the event, with the goal of providing a resource for addressing issues related to the future of work and retirement in response to the needs of an aging U.S. population.

7 See footnote 3 on page 5.