

Challenges and Opportunities of Living and Working Longer

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Abstract

This paper describes the challenges and opportunities that older Americans face, with a focus on retirement income security and the role of continued work later in life. We begin with an overview of the new world of retirement income security in America, including a discussion of how a low return environment (e.g., low interest rates) exacerbates existing retirement income security challenges. We then document how older Americans have responded to the evolving retirement income landscape, especially when and how they exit the labor force, and we explore how continued work later in life can help mitigate some of the anticipated retirement security challenges. We then pose some important outstanding questions. The implications of societal aging depend in large part on how we harness or squander the labor resources of older Americans.

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Older Americans contemplating retirement today are more exposed to market forces and financial insecurity than their predecessors were (Quinn and Cahill 2016). This increased exposure results from a variety of interactions among long-term demographic changes, the evolution of traditional retirement income sources, and macroeconomic volatility. With public sector budgets also strained, many older Americans are faced with a decision to extend their working lives or reduce their standard of living in retirement. This choice presents older Americans, their employers, and our nation with both challenges and opportunities.

In many ways, these three characteristics of the retirement environment create a perfect storm threatening financial security later in life. First, the long-term demographic changes behind societal aging—increases in longevity and declines in fertility—mean that the on-going shift in the age distribution will be permanent (Ortman et al. 2014). The combination of low fertility rates during the Great Depression and high fertility rates following WWII resulted in a pause in societal aging from 1990 to 2010, followed now by a rapid increase that will continue through 2030 (Werner 2011). Second, the retirement income landscape has evolved over the past three decades and continues to do so, altering the retirement incentives and opportunities that older Americans face (Cahill et al. 2015a). The well-documented transition from defined-benefit to defined-contribution pension plans in the private sector is an important example (Copeland 2009; Munnell 2014). Finally, the changing retirement landscape has exposed older Americans to market forces at a time when the macroeconomic environment is volatile. The economic well-being of older Americans could now be more cyclical than in the past, with the outlook for retirement income security being stable or improving in a strong macroeconomic climate but becoming unstable and declining during and following economic downturns.

In response to these changes, some Americans appear to have adapted and prepared for this storm, although the adequacy of their preparations remains to be seen. A century-long trend toward earlier retirement came to a halt in the 1980s and has since reversed, although that reversal may now be slowing down (Quinn et al. 2011; Munnell 2015b). This increase in labor force participation among older Americans is all the more notable because it comes at a time when labor force participation among workers aged 25 to 54 has declined steadily since 2000, for both men and women (Hipple 2016). Older Americans are bucking the broader trend which is good news for them in light of changes in the retirement income landscape.

As important as the changes in labor force participation, the ways in which older Americans exit the labor force reveal a flexible work force that is willing to change employers, occupations and work intensity late in life (Cahill et al. 2015a; Johnson et al. 2009). This flexibility may be an antidote to the expected retirement income security challenges ahead (James et al. 2016; Smyer et al. 2009).

For the foreseeable future, individuals are likely to play a more central role in determining their own financial security at older ages. Policymakers should focus on the incentives that older Americans face and how these incentives can encourage continued work later in life among those who can do so, while protecting those who cannot. Many challenges exist when it comes to living and working longer. Many opportunities do as well.

Societal Aging

The story of societal aging in America has long-term and short-term components. The long-term components are increases in life expectancy and decreases in fertility. Life expectancy at birth for men and women were 46 and 48 years, respectively, in 1900, 66 and 71 years in 1950, 70 and 77 years in 1980, and 76 and 81 years in 2014 (National Center for Health Statistics

2016). The same is true for life expectancy at age 65, available since 1950. Between 1950 and 1980 life expectancy at age 65 increased 1.3 years for men (to 14.1 years) and 3.3 years for women (to 18.3 years), and between 1980 and 2014 it increased another 3.9 years for men (to 18.0 years) and 2.2 years for women (to 20.5 years) (National Center for Health Statistics 2016). These steady gains in life expectancy contribute to the continued increases in societal aging expected over the next several decades.

The second long-term trend is a pronounced decline in fertility rates dating as far back as the early 1800s, when the average number of births per female was approximately seven (Munnell et al. 2004). By the beginning of the 20th century, the number of births per female had dropped nearly in half and the decline persisted through the Great Depression. Fertility jumped temporarily to about 3.5 births per female following World War II (a reversal that has important implications today, some 65 years later) but then the long-term decline resumed and fertility rates eventually stabilized in the 1990s at approximately 2.0 births per female. The decline in fertility means that societal aging is not just a baby boomer phenomenon. If the boomers had had children at the same rate as prior generations did, the shift toward a more rectangular population distribution would not have occurred.

The important short-term component of societal aging has to do with two brief breaks from the long-term fertility trend, one during the Great Depression and the other following World War II. As noted above, fertility rates declined during the economic hardships of the 1930s and these lower rates, decades later, yielded a brief respite from the tide of societal aging. Between 1990 and 2010 the percentage of the population aged 65 and over changed little, from 12.6 to 13.0 percent (Werner 2011). In contrast, the temporary spike in fertility following World War II is now generating a rapid aging of our population. The percentage of the population aged

65 and older, 13.0 percent in 2010 and 14.9 percent in 2015, will increase to nearly 20 percent by 2030—an increase of over 50 percent in just 20 years—and is expected to remain between 20 and 22 percent between 2030 and 2050 (US Census Bureau 2016a, 2016b; Ortman et al. 2014).

The New World of Retirement Income Security in America: Many Causes for Concern

Both the long-term trends in societal aging and the current short-term acceleration will challenge our ability to maintain living standards as we age. Moving from this macro view to the micro—the decisions facing an individual contemplating departure from the labor market—there are legitimate concerns regarding several of the income sources on which retirees will rely.

Figure 1 shows these sources for Americans aged 65 and older in 2014 (US Social Security Administration 2016b).

(Insert Figure 1)

Nearly two-thirds of this income comes from sources about which potential retirees might be concerned: Social Security, pension benefits (including annuities), and asset income. For those aged 65 and older in the lower three income quintiles, the reliance is even higher—85, 91 and 83 percent of total income come from these three sources, with Social Security by far the most important (US Social Security Administration 2016a: table 10.5).

Social Security. As seen in Figure 2, Social Security provides an important and essential safety net for the elderly. The progressive nature of Social Security’s benefit calculation formula disproportionately rewards those with lower lifetime earnings, providing lower absolute benefits but higher replacement rates. On the other hand, there are many concerns ahead. The permanent benefit reduction for claiming at the Earliest Age of Eligibility—still age 62—will increase from 20 to 30 percent as the Full Retirement Age (FRA) rises from 65 to 67 for those born after 1959 (Board of Trustees of OASDI 2016).¹ This higher offset for claiming benefits early

disproportionately affects lower-income workers and those in physically-demanding occupations who may find it difficult to postpone benefit receipt until their FRA or beyond (Rutledge and Coe 2012).

(*Insert Figure 2*)

According to Munnell (2015a; Figure 3), Social Security replacement rates (the ratio of benefits to prior earnings) for the average earner retiring at age 65 are declining, from 42 percent in 1985 to a projected 36 percent in 2030. In addition, the Medicare Part B premiums that are subtracted from Social Security benefits are rising faster than the cost-of-living and more recipients will find part of their benefits subject to federal income taxation in the future.² When these two factors are considered, the average replacement rate drops further, to 31 percent (*ibid.*). And this all assumes that future Social Security benefits will be paid according to the current benefit formula.

In fact, Social Security faces long-term significant funding issues. Annual expenditures already exceed (non-interest) revenues and without reform on the revenue and/or the expenditure side, the Social Security (OASDI) Trust Fund will be depleted by 2034—just 17 years from now—at which point Social Security would be able to pay out less than 80 percent of promised benefits (Board of Trustees of OASDI 2016: Figure II:D2). One hopes and trusts that reform preceeds this dire outcome. But many reform options spell potential trouble for future retirees, because they include benefit reductions, either explicitly or implicitly, through additional delays in the Full Retirement Age. (Waiting longer for a given benefit implies getting a smaller benefit at any given age, which is an across-the-board benefit cut, although it is rarely described that way.) The last major reform, in 1983, did just that, moving the FRA from 65 to 66, and then to 67, lowering the benefits received at any age.

Many recent reform proposals do the same. For example, the 2010 Simpson-Bowles report, *The Moment of Truth*, proposed (among other changes) lowering benefits for higher income recipients, increasing both the Full Retirement Age and the Early Eligibility Age (which is still 62 for all) in step with future longevity increases, and lowering the annual cost-of-living adjustment, all three of which would lower future Social Security benefits relative to the current provisions (National Commission on Fiscal Responsibility and Reform 2010: 54). The Congressional Budget Office (CBO) (2010) discussed five categories of Social Security reforms, three of which would lower future benefits, via formula changes to reduce initial benefits, additional increases in the FRA, and reductions in cost-of-living adjustments. In fact, the majority of the 30 proposals the CBO analyzed would lower future benefits (CBO 2010: Summary Figure 1). These analyses have not been implemented so far, but they do suggest that reasonable reformers will include benefit cuts in their recommendations.

Employer pensions. Social Security was not designed to provide financial security in retirement on its own. About half of those working in the private sector are covered by an employer pension on their current job and about 44 percent of those aged 65 and over currently receive income from a pension other than Social Security (US Social Security Administration 2016a: table 2.A1). Although pension coverage has remained steady over time at about one-half, the type of pension coverage has changed dramatically, from traditional defined-benefit (DB) to defined-contribution (DC) plans.³ DB pensions typically provide a defined monthly benefit at retirement (as does Social Security, a public DB plan), often based on earnings and tenure with the firm.⁴ In contrast, in a DC plan the employer's only obligation is to make defined contributions to an account designated by the employee. The size of the account at retirement will depend on the amount of

these contributions and how these investments then perform over the years. DC plans transfer financial risk from the employer, who bears it in a DB plan, to the employee and potential retiree.

The percentage of covered workers with a DB plan has plummeted from 88 percent in the early 1980s (including 26% who had both a DB and a DC plan) to only 30 percent in 2013 (including 13% with both). Over the same time, DC coverage only has risen from 12 to 71 percent, or from 38 to 84 percent, including those covered by both (Munnell 2014).

DC plans do have certain advantages. They are portable from employer to employer and the current value of the assets (which can rise or fall) is clear. On the other hand, DC plans often require workers to decide whether or not to enroll (and about 1 in 5 eligible employees do not participate), how much to contribute, how to invest the funds, whether to withdraw assets before retirement, and when and how (via lump-sum and/or annuity?) to withdraw the assets remaining at retirement (Munnell 2014; Munnell and Sundén 2004). DC plans expose workers to both market and longevity risk (living longer than anticipated), two risks assumed by employers in traditional DB plans.

For many, the accumulations in these DC accounts are small. In 2013, for example, workers aged 55-64, at or approaching traditional retirement ages, with a DC plan had median 401(k) and IRA accumulations of about \$110,000, enough to purchase a joint and survivor annuity of only about \$500/month (Munnell 2014; Dushi et al. 2015).⁵ Morrissey (2016: Chart 4) estimates mean retirement account savings in 401(k)s, IRAs and Keogh plans by age, over time. As seen in Figure 3, these assets rise with age, as expected, averaging about \$125,000 for those aged 50-55, and \$164,000 for those 56-61. Both averages have declined since 2007, before the recession and stock market crash. Because nearly half of American families have no retirement account savings at all, the median (50th percentile) value among those aged 32-61 is only \$5,000,

and under \$10,000 for all the ages groups above except the oldest, 56-61, whose median is only \$17,000 (Morrissey 2016: charts 5 and 7).⁶

(Insert Figure 3)

These amounts are modest at best, especially considering the likelihood of financial shocks in retirement. Medicare and Medicaid (see below) do provide very important buffers against catastrophic health events, but for many elderly, health issues will require substantial out-of-pocket expenditures and can force individuals to tap retirement savings, leaving them more vulnerable to financial insecurity at older ages.⁷ In the future, the importance of these often inadequate DC plans will increase among those fortunate who participate in pensions, as the more secure DB coverage continues to decline.

Medicare and Medicaid. Strengthening the fiscal future of Social Security is straightforward compared to the challenges facing Medicare and Medicaid. Social Security (OASDI) just provides checks or bank deposits and analysts can estimate the fiscal impacts of various reform proposals. The reform challenges here are primarily political; understandably, many politicians do not want to be on record supporting increases in Social Security taxes or decreases in benefits, especially when Social Security can meet its full obligations for nearly two decades. But Medicare and Medicaid reforms are much more difficult, because they are intimately connected to the provision of health care in the United States. Because of both aging and increases in health care costs, which have outstripped general inflation, the expected growth rate of federal spending on major health care programs (primarily Medicare and Medicaid) is higher than that of Social Security (Figure 4). Whereas projected Social Security spending, under current rules, will reach about six percent of GDP and stays there, projected federal spending on health care will continue to rise, reaching almost 8 percent by 2040, and heading still higher.

(Insert Figure 4)

Medicare's Hospital Insurance Trust Fund (Medicare Part A) is currently projected to be depleted by 2028—just 11 years from now and six years before the Social Security Trust Fund runs out (Board of Trustees, Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds 2016: table II.E1).⁸ It is difficult to know how Medicare and Medicaid, which is burdening state budgets, will be reformed, particularly under the new administration, but few would predict that they are likely to be expanded, at least in the short run. For those contemplating retirement, the futures of Medicare and Medicaid are addition causes for concern.

Savings. Another leg of the retirement income stool, private savings, is inconsequential for many older Americans. The national savings rate (as a percentage of personal disposable income) was mostly between 10 and 15 percent during the three decades leading up to the mid-1980s (Federal Reserve Bank of St. Louis 2016a). Savings rates then declined steadily and by the mid-2000s they fell below 2 percent, their lowest level since the Great Depression. They have increased slightly since then but still remain near five percent, less than half of the three-decade average prior to the mid-1980s. One result of low savings rates is a low level of accumulated assets. A recent Retirement Confidence Survey found that nearly 60 percent of American workers (and over 40 percent of those aged 45 and older) own less than \$25,000 in financial assets, excluding the value of one's primary residence and defined-benefit pension plans (Helman et al. 2016). Given that life expectancy at 65 is currently about two decades—decades in which out-of-pocket medical expenses will increase for many—these modest assets provide very little financial cushion late in life.

Summary. There are significant causes for concern in the three traditional legs of the retirement income stool. Social Security, by far the most important of these three, providing over 80 percent

of the income of the bottom two income quintiles of the elderly (and about two-thirds and 40 percent for the next two quintiles, respectively), faces a long run financial shortfall and reform proposals are likely to include benefit cuts or delays. Pensions remain very important for some elderly, but many are not covered and among those who are, defined-contribution plans now dominate the landscape. The medical care landscape is unclear. Personal savings have always been small among all but the wealthiest Americans and provide only a modest cushion for the retirement years ahead.

The Current Low-Return Environment

The current low-return environment exacerbates these challenges, though the net impact depends on a variety of factors. Nominal interest rates are correlated with rates of inflation (Federal Reserve Bank of St. Louis 2016b; US Bureau of Labor Statistics 2016). Therefore, while one downside of a low-return environment is lower returns on assets, they are accompanied by lower rates of inflation. This implies little change in economic well-being for those relying primarily on Social Security benefits for the bulk of their retirement income.

In contrast, timing issues are a concern for some. Those who locked into annuities in recent low-return years stand to lose when prices rise, while those who bought annuities during the earlier higher-return environment have gained as the nominal return on their assets, built into their fixed monthly benefits, has been maintained while price increases declined. Such outcomes reflect the risks of decision making in the face of uncertainty. For older workers depending on income flows from assets, annuities purchased in a low-return environment will provide less financial security during high-inflation environments in the future.

The low return environment could also impact some older workers' decisions about when to leave the labor force. Overall, income from assets provides about 10 percent of the income of

Americans aged 65 and over. That percentage rises slightly with age and dramatically by income quintile, from less than three percent for those in the bottom two quintiles to 14 percent for those in the top quintile, many of whom are still working (US Social Security Administration 2016a: tables 10.1 and 10.5). A low-return environment could very well impact the retirement decisions of these workers.

The potential loss of retirement income due to low returns can be substantial. For example, the monthly payment on an annuity with a starting principal of \$250,000, an interest rate of five percent, and a 20-year period is \$1,632. At an interest rate of two percent the monthly payment is only \$1,263—nearly a quarter less. One way to compensate for this loss is work more or longer. Importantly, expectations about future rates can impact these work decisions. If older Americans expect rates to increase soon, then the low rates of return over the past five years could be viewed as temporary and have little or no impact on work decisions. But expectations of persistently-low rates could induce individuals to remain working longer. Other individuals might choose to take on more financial risk to achieve higher average returns, at the cost of higher variation in returns. If so, low returns on assets could further increase older Americans' exposure to market fluctuations. Either way, the low-return environment is likely to impact older Americans' choices about work and retirement, their exposure to market risk, or both.

Finally, another important consideration regarding low rates of return is the impact on incentives to save and to take on debt, especially for younger Americans. The Federal Reserve Bank has kept interest rates at historical lows since the Great Recession in part to induce individual spending and spur economic growth (Board of Governors of the Federal Reserve System 2016). Increased spending implies lower savings, and low interest rates can encourage individuals to incur debt. Such changes in behavior can alter the financial outlook for younger

and older Americans alike, at a time when the financial security of older Americans is already a real concern.

Are Older Americans Prepared for Retirement?

How does the financial future of Americans approaching traditional retirement ages look, within the context of a low-return environment, when these various income streams are combined? What proportion of households are preparing adequately for retirement? Will they be able to maintain their prior standards of living if and when they do leave the labor force?

The Center for Retirement Research at Boston College has created a national retirement risk index which estimates the proportion adequately prepared by comparing the replacement rate (the ratio of income after retirement to that before) that households in the Survey of Consumer Finances (SCF) are likely to face if they retire at age 65 with the rate they would need to maintain their prior standard of living after retirement (Munnell et al. 2014).⁹ Those who fall 10 percent or more below what is required are judged to be at risk and inadequately prepared for retirement. The income available after retirement includes the usual sources, such as Social Security, defined-benefit pension payments and income from assets, plus the imputed rental value of housing for those who own their own homes, and the additional income they could receive through a reverse mortgage, but of course, no earnings (Munnell et al. 2014). The results are not encouraging.

(Insert Figure 5)

One can anticipate trouble in Figure 5, which shows the ratio of wealth to income over time, for age cohorts of respondents in the SCF. Not surprisingly, the ratios increase with age, as respondents approach traditional retirement ages. The ratio was highest at older ages in 2007, prior to the 2008-2009 recession, but then dropped significantly in 2010 and 2013, suggesting that the current elderly are now less well prepared than prior cohorts. This concern is confirmed in the

National Retirement Risk Index (Figure 6), which estimates that in 2010 and 2013, more than half of American households have accumulated less than 90 percent of what they need to maintain their pre-retirement standard of living.¹⁰ The index jumped by 20 percent from pre (2007) to post (2010) recession, but that just continued a long-term trend, up from near 30 percent in the 1980s to the high 30s in the 1990s to the mid 40s just before the recession. The index showed little improvement between 2010 and 2013, and it will be interesting to see the extent of the recovery (a decline of the index) by 2016, when those data become available later this year.

(*Insert Figure 6*)

To explain this discouraging trend in unpreparedness, Munnell (2015a) refers to many of the factors discussed above: declining Social Security replacement rates (partly because of rising deductions for Medicare premiums and a higher proportion of Social Security beneficiaries who will pay federal income tax on their benefits), the shift to defined-contribution pension plans (which tend to *increase* the wealth/income ratios in Figure 5, because DC assets are counted as wealth, while the present discounted value of DB pension payments is not) and declining real interest rates. In addition, life expectancies for men and women continue to increase which imply that additional funds at retirement will be needed.

Schieber (2015: exhibit 1) discusses three sets of estimates of retirement unpreparedness by birth cohort, by researchers using different datasets, different income definitions and annuitization assumptions, and different criteria for being at risk. Munnell et al. are the most pessimistic because, according to Schieber (2015:15), they believe ‘that current workers will have defined contribution balances at retirement that are no larger than that of current retirees.’ One researcher presents two sets of estimates, with and without expected long-term care and home health care expenditures, with much higher risks when these are considered. Schieber (2015: 16) concludes

that ‘it is clear that many low earners face retirement with inadequate resources to provide an income that will allow them to maintain either a socially acceptable standard of living or one that matches that achieved while they were working.’

What Might Concerned Potential Retirees Do?

Later in life, approaching traditional retirement ages, the options are limited. An individual has little or no influence over future Social Security, Medicare or Medicaid reform (write to your congressional representatives!), or over employers’ decisions regarding pension coverage, pension type or post-retirement health insurance (write to your human resources department!). Additional savings later in life can help, but nowhere near as much as savings much earlier, with decades of asset accumulation ahead. If one cannot rewrite one’s savings history and cannot influence important Social Security parameters, trends in employer pensions, or the details of medical insurance coverage, what can one do? The answer for many is simple and very consequential—work longer, either on a career job or on one or more post-career bridge jobs before complete labor force withdrawal.

Working longer helps in many important ways. It provides additional lifetime earnings and the opportunity for incremental saving, augments the size of eventual pension and Social Security benefits (especially if receipt of Social Security benefits, which rise by about eight percent per year of delay, are postponed while one continues to work), and reduces the number of years of retirement over which these augmented assets will be consumed. The numerator (retirement resources) increases while the denominator (years of retirement) declines.

Is working more a likely response to the financial challenges older individuals face? Yes it is, and in fact a trend toward delayed labor force withdrawal has been underway for three decades.

Retirement Trends and Patterns in the Modern Era

Retirement trends. As mentioned above, the road to continued work later in life among older Americans has been well paved as a century-old trend toward earlier and earlier retirement came to a halt in the 1980s (Quinn et al. 2011). Since 1910, the average age of retirement for men, defined here as the age at which the labor force participation rate drops to 50 percent, declined steadily from age 73 to age 65 in the mid-1970s and to age 63 in 1985 (Burtless and Quinn 2002: Figure 2). Dora Costa (1998: Figure 2.1) documents similar dramatic declines in the employment rates of men aged 55 – 64 and 65+ going back to 1880. But since the mid-1980s, these trends have all reversed. As seen in Table 1, between 1985 and 2014, after a century of decline, the labor force participation rate of men aged 62, increased by over 20 percent (from 51 to 62 percent). For men aged 65, 68 and 70, the changes are even more dramatic—increases of approximately 40, 60 and 70 percent over these past three decades.¹¹ For older women, the increases are even higher. Since 1985, the labor force participation rate of women aged 62 has increased by over 50 percent (from 32 to 48 percent), and for those aged 65, 68 and 70, the rates have approximately doubled. Older Americans are already working longer than they did a short time ago.

These increased participation rates among older Americans are all the more remarkable because they come at a time when participation among younger and middle-aged workers has been declining (Hipple 2016). Among Americans aged 25 to 54, labor force participation rates declined about four percent between 2000 and 2015 (from 92 to 88 percent for men and from 77 to 74 percent for women), in stark contrast to the significant increases among older Americans.

The reversing of the early retirement trend is consistent with important changes in retirement incentives noted above. In addition, the Social Security earnings test has been eliminated for those above their FRA and the delayed retirement credit (DRC) has increased to

become actuarially fair for the average worker (Cahill et al. 2015b; Gruber and Orszag 2003). This increase in the DRC (from 3 to 8 percent for each year of delay beyond the FRA) removed a significant work disincentive (an implicit pay cut for those who worked beyond their FRA) by making expected lifetime benefits approximately the same for the average worker regardless of when they are first claimed between the FRA and age 70. With this incentive removed, Munnell (2013) points out that the ‘true’ Social Security retirement age is really age 70, as the FRA has little meaning in terms of one’s expected lifetime Social Security benefits before then. On the employer pension side, the move from DB to DC plans also removed strong retirement incentives for many workers, since many DB pensions lose present discounted value after the earliest age of eligibility—an implicit pay cut that does not occur in a DC plan.

Retirement patterns: The road to continued work later in life is also well paved because for most older Americans retirement is a process rather than a single one-time event. Indeed, the term ‘retirement’ can be confusing because of its many definitions, some of which require labor force withdrawal, others are based on receipt of Social Security or employer pension benefits or on a decline of hours or earnings, but not necessarily to zero, and sometimes are based on the self-description of survey respondents who are far from consistent in their definitions of what constitutes retirement.

Three common pathways from career employment to complete retirement (out of the labor force) have been identified: phased retirement (a reduction in hours with one’s current employer), bridge employment (a job change following career employment, with or without a change in hours), and job reentry (a subsequent return to the labor force following ‘retirement’—sometimes known as ‘unretirement’) (Cahill et al. 2015b, 2016; Kantarci and van Soest 2008; Maestas 2010). These pathways to retirement are often studied as follow-ups to career

employment (full time work for a significant duration), but jobs changes later in life are also common among those who have not had career jobs (Cahill et al. 2012).

Bridge employment is the most prevalent form of gradual retirement among those with career jobs (Cahill et al. 2006, 2015b; Quinn 1999). An analysis of three cohorts of older Americans from the Health and Retirement Survey over a 20-year period shows that between 50 and 60 percent of older career workers move to a bridge job following career employment. The majority of career workers do not follow the ‘traditional’ pathway to retirement, directly out of the labor force from career employment. Reentry is the next most common form of gradual retirement. About 15 percent of career workers who leave the labor force for at least two survey waves years later return to paid work (Cahill et al. 2011). The least prevalent form of gradual departure is phased retirement, with only 10 percent of workers reducing their hours on a career job by 20 percent or more (Cahill et al. 2015b).

Phased retirement, the last option, would seem to be a preferable exit route since the worker could continue to capitalize on accumulated specific human capital in a familiar environment, but factors on both the supply and demand sides of the labor market help explain its low prevalence. On the labor supply side, individuals might choose to change employers to alter the type or intensity of the work they do, or prefer to move to warmer climes or closer to (or farther away from!) grandchildren. Lower hours on a career job might decrease subsequent pension benefits if they are based on the last few years of earnings. The concept of ‘encore jobs’—those with a social impact—are attractive to many (Alboher 2012; Quinn 2010; Johnson et al. 2009), and surveys by AARP show that older Americans care about the non-financial aspects of their work (AARP 2014).

On the demand side legal and regulatory requirements, often implemented for good reasons, can present obstacles for some employers. Regulations designed to protect employees from policies favoring tax-deferred benefits for highly compensated individuals seem have to limited the possibility of phased retirement for older workers. Rules regarding pension distributions can also complicate a phased retirement offering (Johnson 2011). The supply-side and demand-side challenges to phased retirement on the career job could explain why bridge employment remains by far the most common option and might also explain the importance of retirement and later reentry. When faced with the choice between full-time work or changing employers, some workers might first decide to leave the labor force and save the prospect of reentry as a contingency plan, if later needed or desired.

Another important barrier to continued work later in life on a career job or elsewhere is physical or mental health. For a sizable minority of the population, continued work later in life is difficult or impossible. Increases in longevity and improvements in overall health have reduced the percentage of workers for whom physical health presents a barrier to continued work and a shift away from physically-demanding jobs over time has also expanded work options for older Americans (Munnell et al. 2004; Penner et al. 2002; Steuerle et al. 1999). Nonetheless, it is important to keep in mind that continued work later in life is not a viable option for a sizable minority of the labor force.

Future Retirement Trends: One question is whether the retirement patterns of older Americans observed in the 1990s and 2000s will hold among future cohorts of retirees, who live in a world in which important changes in the retirement income landscape that began in the 1980s are now well established. Examples are changes to the Social Security earnings test and the delayed retirement

credit and the dramatic transition from defined-benefit to defined-contribution pension plans in the private sector.

We might also expect the retirement patterns of future retirees to differ from those of the past for at least two other reasons—the impacts of the Great Recession during 2008 and 2009 and the subsequent sluggish recovery (Desilver 2014), and the current low-return environment. Older Americans who planned on higher asset returns might have altered their retirement plans. As noted above, just as older Americans are more exposed to market forces through defined-contribution pension plans, older Americans might be further exposed to market fluctuations by seeking riskier assets with rates of returns more like historical averages. In the near term, this strategy has worked as equity returns since 2010 have been strong (Wall Street Journal 2016). The downside of this strategy, however, is that older Americans are further exposed to financial losses in the event of another market downturn.

Using data from the Health and Retirement Study (HRS), an ongoing nationally-representative survey of older Americans that began in 1992, we studied the retirement patterns of the Early Boomers, aged 51 to 56 in 2004, and the Mid-Boomers, aged 51 to 56 in 2010, and compared their behavior to that of two older HRS cohorts, the HRS Core (aged 51 to 61 in 1992) and the War Babies (aged 51 to 56 in 1998). For each of the HRS cohorts we selected individuals who were on a full-time career (FTC) job at the time of the first interview.¹² We followed individuals over time and used each respondent's work history to identify their pathway to retirement (directly, or via phased retirement, bridge job, or job reentry).

Bridge employment continues to be the most common gradual retirement pathway among the Early Boomers and the Mid-Boomers for those who have left career employment (Table 2). Few of the Early Boomers reduced hours in career employment by 20 percent or more.

Retirement and then reentry rates are only slightly lower than those of the HRS Core and HRS War Babies, an interesting finding given the very different macroeconomic landscape following the Great Recession. It is too soon to consider reentry among the Mid-Boomers as just four years of follow-up data are available.

The latest data available from the HRS suggest that this recent cohort of retirees is following the same pathways to retirement as their predecessors did, despite their exposure to market fluctuations and the low return environment since 2008. Bridge jobs remain much more important than job reentry, and both are more common than gradual retirement on the career job. The concept of retirement as a one-time, permanent event does not apply for most older Americans today and has not for decades.¹³ This flexibility of older workers is good news and offers opportunities to address the challenges of societal aging.

Key Outstanding Questions

As noted throughout this paper, current and future cohorts of older Americans are exposed to market forces more than previous cohorts were and this exposure exacerbates the risk of financial insecurity later in life. Continued work later in life is one way to address these challenges and those associated with a low-return environment, but more work needs to be done to understand the potential impacts of extended working lives. In this section we discuss some key outstanding questions.

To what extent does prolonged labor force participation translate into more work hours over the retirement transition period? A priori, the impact of extending working lives on total hours worked over the retirement transition period is ambiguous. Policies that promote continued work later in life might simply alter how older individuals allocate their work hours rather than increase the total number of hours worked. Employment decisions, retirement timing, and total

hours worked are all jointly determined. This is a potentially fruitful area of research and some preliminary work on this topic suggests that voluntary job changes later in life increase the likelihood of remaining in the labor force to age 65 (Sanzenbacher et al. 2017).

To what extent does bridge employment increase labor supply over the retirement transition period? For many, bridge employment is a way to extend labor force participation later in life; for example, for those who move from a physically-demanding career job they can no longer handle to a less strenuous one. But others may leave a career job that they could have continued. Since about one half of bridge jobs are part time, it may be the case that the total number of hours worked over the retirement transition period would have been higher with continued career employment than with bridge employment. Studies of the impact of bridge employment on total hours worked would be worthwhile.

How do bridge jobs compare with the career jobs that older workers leave behind? Bridge employment has the potential to offer older workers a variety of benefits, including flexible work arrangements and re-careering opportunities (reirement!). Indeed, job transitions later in life are mostly voluntary (Cahill et al. 2015b; Maestas 2010), suggesting that older workers expect to be better off after changing jobs. A deeper understanding of the trade-offs that older workers face when changing jobs later in life could improve policymaking around the impacts of pro-work incentives. For example, how does bridge employment compare with career employment in terms of wages, fringe benefits, job security and other considerations? Further, how do these compare for those leaving career employment voluntarily versus involuntarily?

How can society address some of the challenges associated with hiring and retaining older workers (e.g., age discrimination and the cost of fringe benefits)? To this point we have focused on the labor supply decisions of older workers under the implicit assumption that jobs

will be available to those who want them. This is a reasonable assumption when economic conditions are favorable, such as now when the unemployment rate among workers aged 55 or older is just 3.5 percent (US Bureau of Labor Statistics 2017). The sudden onset of the Great Recession between 2007 and 2009, however, with large increases in the extent and duration of unemployment, reminds us that the labor demand side can be critical. Rather than wait until the next downturn, we should address the persistent challenges in hiring older workers, including age discrimination and extra costs that might be associated with older employees. Doing so might help avoid or reduce a spike in long-term unemployment similar to the one recently observed (Rix 2014).

To what extent are low interest rates masking the financial instability of older Americans with substantial debt and suppressing the urgency of continued work later in life? As noted above, the current low-return environment could influence older individuals' decisions to hold debt or take on additional debt. Citing work at Iowa State University, the Center for Retirement Research at Boston College reports that 11 percent of middle boomers are in debt; i.e., have negative net worth (The Center for Retirement Research at Boston College 2017). The current low interest rate environment (bad news for those relying on income from assets for income, but good news for those in debt) could be shielding these individuals from the true precariousness of their financial situation and obscuring the need for continued work. More needs to be done to understand the degree to which older Americans with sizable debt are vulnerable to a rise in interest rates.

For savers, is the low-return environment altering appetites for risk in order to achieve higher returns? For those with financial assets, the low-return environment introduces incentives for behavioral change regarding risk. As noted above, older Americans facing lower

returns on their assets might decide to continue working later in life in order to supplement their retirement savings. To the extent that they are physically able to do so, such a decision is nearly universally beneficial to the individual, employers, and society as a whole as more goods and services are produced to be distributed over an aging population. Alternatively, savers might desire to increase asset returns by accepting more risk. The downside to this response is even more exposure to market forces, compounding the negative repercussions of the next market downturn. Research on the riskiness of assets held older American in low- and high-return environments might be useful to policymakers.

Conclusion

Older Americans are living longer and working longer. While societal aging is a given, its implications will depend in large part on how we respond to the challenges and the opportunities presented by these trends. The new world of retirement income security in America suggests many causes for concern. Social Security, the bedrock of financial stability for most older Americans, is now experiencing annual shortfalls as expenditures exceed (non-interest) revenues. The Social Security Trust Fund is projected to be depleted in just 17 years. The financial outlooks for Medicare and Medicaid are precarious. The shift to DC plans in the private sector, for the approximately one half of workers covered by an employer-provided pension, and low personal savings suggest that for many older Americans these two legs of the traditional retirement income stool are unlikely to fill any void created by changes to Social Security, Medicare, and Medicaid.

On the other hand, many older Americans are responding to these changes by staying in the labor force later in life. A nearly 100-year trend toward earlier retirement ended in the mid-1980s and has since reversed. The change is even more notable because the labor force

participation rates of older Americans have increased even as those among younger workers have declined. Older Americans have also shown a remarkable ability to adjust the ways in which they work, by changing employers, re-careering, switching between wage-and-salary and self-employment, and altering the number of hours that they work. The flexibility of older workers is one of the true (and few?) bright spots in the financial outlook for older Americans. Policymakers would be wise to consider additional ways to support continued work later in life to help mitigate the many challenges that our aging society will face in the decades ahead.

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Endnotes

¹ Johnson et al. (2013) report that Social Security claiming rates at age 62 have declined over the past decade. Among men born in 1943 and 1944, 45 percent claimed benefits at age 62 compared with 55 percent of those born between 1935 and 1937. Approximately one half of women born in 1943 and 1944 claimed Social Security benefits at age 62, down from 60 percent among those born between 1935 and 1937.

² Couples with “combined income” of over \$32,000 and individuals over \$25,000 pay income tax on 50 percent of their Social Security benefits. At combined incomes of \$44,000 and \$34,000, respectively, 85 percent of Social Security benefits are taxable. These thresholds are not indexed for inflation, so the percentage of recipients paying taxes on Social Security benefits will rise over time, from about 10 percent in 1985 to about 40 percent today, and an estimated half of recipient households by 2030 (Munnell 2015a).

³ Some analysts disagree with this 50 percent estimate. Munnell (2014), using the 2013 Survey of Consumer Finances (SCF), argues that among prime-age private sector workers, the percent participating in an employer pension on the current job has drifted from 50 percent to the low 40s. Morrissey (2016), also using the 2013 SCF, estimates that participation by respondents or their spouses declined from 60 percent in 2001 to 53 percent in 2013. In contrast, Dushi et al. (2015) estimate that participation rates increased slightly from 58 percent in 2006 to 61 percent in 2012. While these participation rate estimates differ, there is unanimous agreement about the precipitous decline in traditional DB plans in the private sector.

⁴ Schieber (2015: 13) points out that many defined-benefit plans no longer automatically pay monthly benefits, but rather “have restructured their plans so they also pay benefits at termination in the form of lump sums; most terminating workers...choose lump-sum payments

over annuities.” Those who do claim lump-sums then face the longevity risk facing defined contribution recipients, living beyond one’s assets.

⁵ Ownership of DC assets is highly correlated with income. According to Munnell (2014), two thirds of those aged 55-64 in the fourth and fifth income quintiles had DC accounts, averaging \$132,000 and \$450,000 respectively. DC participation fell to 22 percent and 48 percent in the lowest two quintiles, and they averaged only \$13,000 and \$53,000 as they approached retirement (Munnell 2014: table 2). And of course many have no DC coverage at all.

⁶ Not surprisingly, retirement saving accounts are much more prevalent among high-income families. In 2013, only 8 and 30 percent of those in the lowest two quintiles had any such accounts, compared about half of those in the middle quintile, and nearly 70 and 90 percent of those in the highest two quintiles. While over 60 percent of (non-Hispanic) white families had retirement accounts, only 26 and 40 percent of Hispanics and blacks did (Morrissey 2016, Charts 9 and 10). Schieber (2015) makes this same point, that utilization of retirement savings plans is highly correlated with income, and therefore that high income workers are more likely to be well prepared to meet retirement needs.

⁷ In 2012, Medicare-eligible households spent nearly 14 percent of their income on health care expenses (9.1% on additional health insurance, 2.6% on medical services, and the remaining 2.2% on prescription drugs and medical supplies) (Cubanski et al. 2014).

⁸ Medicare Part A is the only component of Medicare that is funded by the FICA tax and that has a Trust Fund. Parts B (supplementary medical insurance) and D (prescription drug benefit) are funded annually from a variety of other sources.

⁹ The Survey of Consumer Finances is conducted every three years. The data reported here are from the 2013 survey. The 2016 survey results are likely to be available in late 2017.

¹⁰ Munnell et al. (2017) compare their estimates of preparedness with the self-assessments of preparedness by the individual households in the 2013 SCF. In aggregate, the news is about the same: the authors find that 52 percent are inadequately prepared compared to 57 percent of the household themselves. But they are not always the same households. A majority, 57 percent of the households, agree with the authors' assessment. Others are confident when they should not be (19 percent; often with a DC plan whose income generating potential they may overestimate) or concerned when the authors forecast they can generate 90 percent of their pre-retirement income (24 percent; including some who underestimate the income-producing potential of owning a home).

¹¹ The average age of retirement for men, as defined by Burtless and Quinn (2002) also reversed. It declined from 65 in 1976 to 63 in 1980, and then increased, in almost symmetric fashion, back to 65 by 2009.

¹² A full-time career job is defined as one with 1,600 or more hours per year and 10 or more years of job tenure.

¹³ Data from the old Retirement History Survey (RHS), which was conducted among older men from 1969 to 1979 suggest that gradual retirement has been the norm since then (Ruhm 1990).

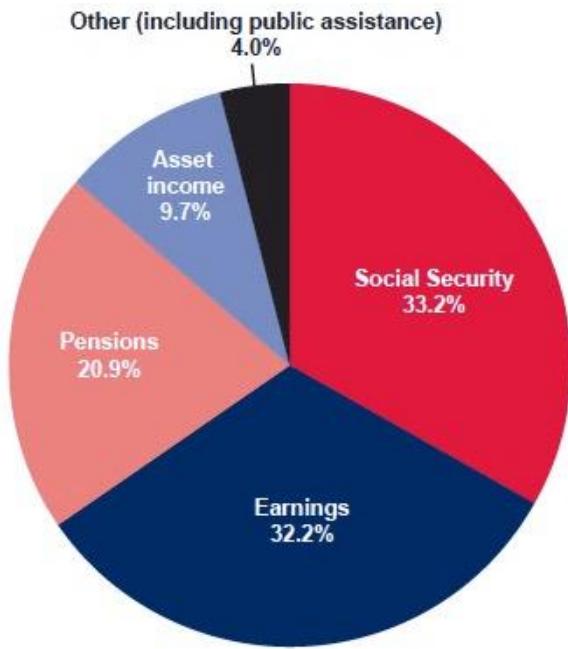


Figure 1: Shares of aggregate income for aged units 65 or older, by source, 2014.

Note: Totals do not necessarily equal the sum of the rounded components. Aged units include married couples with a least one person aged 65 or older and nonmarried persons aged 65 or older.

Source: US Social Security Administration (2016b).

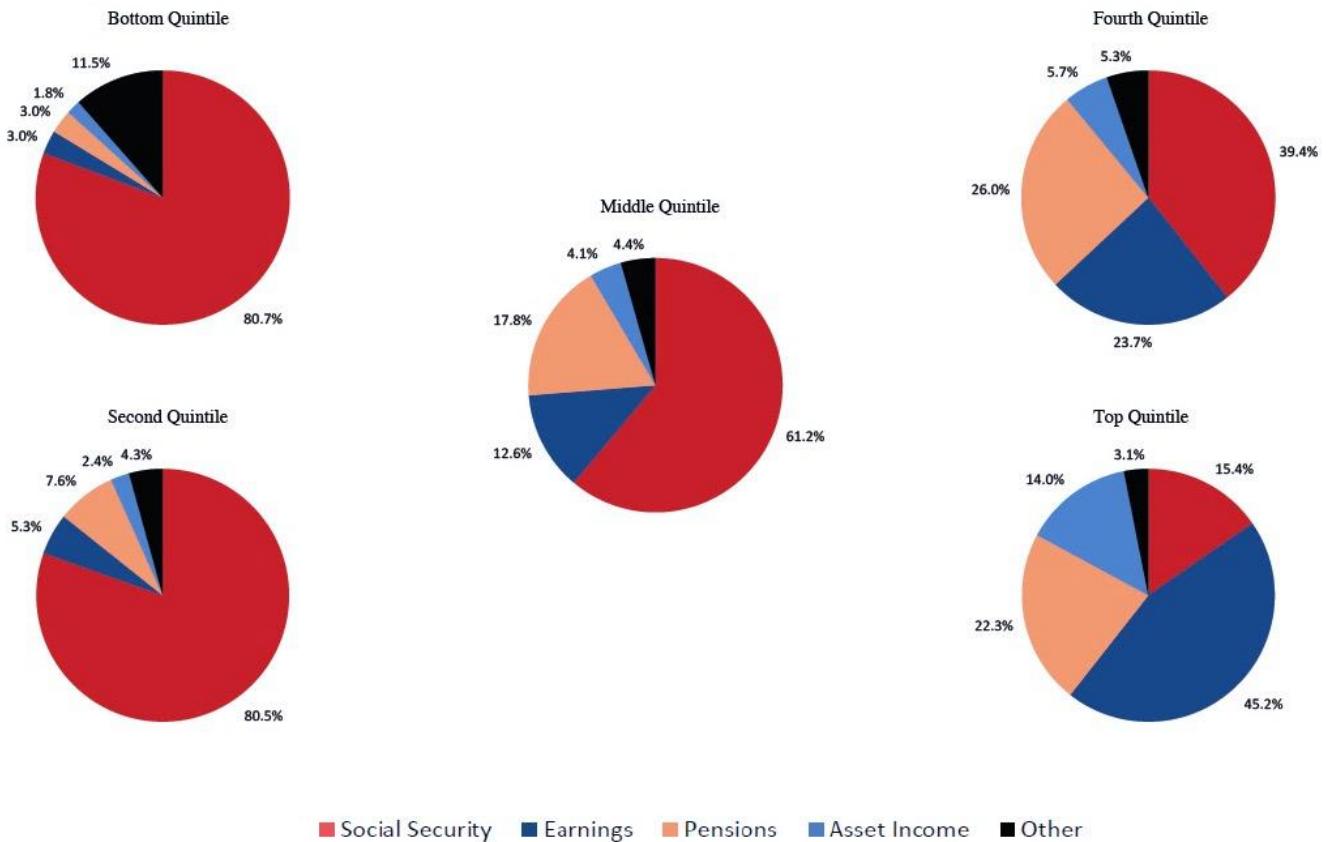


Figure 2: Shares of aggregate income, by source and quintile of total money income, 2014.

Source: US Social Security Administration (2016a).



Figure 3: Mean retirement account savings of families by age, 1989–2013.

Note: 2013 dollars. Retirement account savings include 401(k)s, IRAs, and Keogh plans.

Source: Morrissey (2016).

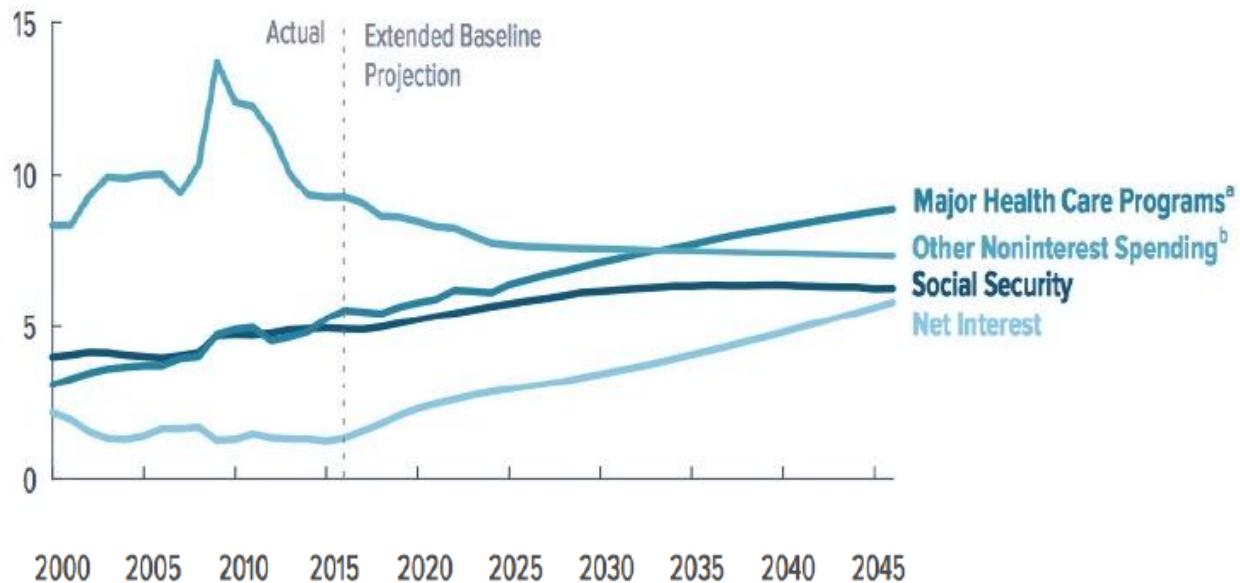


Figure 4: Federal spending as a percentage of GDP, by component, 2000 to 2045.

Notes:

- ^a Consists of spending on Medicare (net of offsetting receipts), Medicaid, and the Children's Health Insurance Program, as well as outlays to subsidize health insurance purchased through the marketplaces established under the Affordable Care Act and related spending.
- ^b Consists of all federal spending other than that for Social Security, the major health care programs, and net interest.

Source: Congressional Budget Office (2016), Figure 1-2.

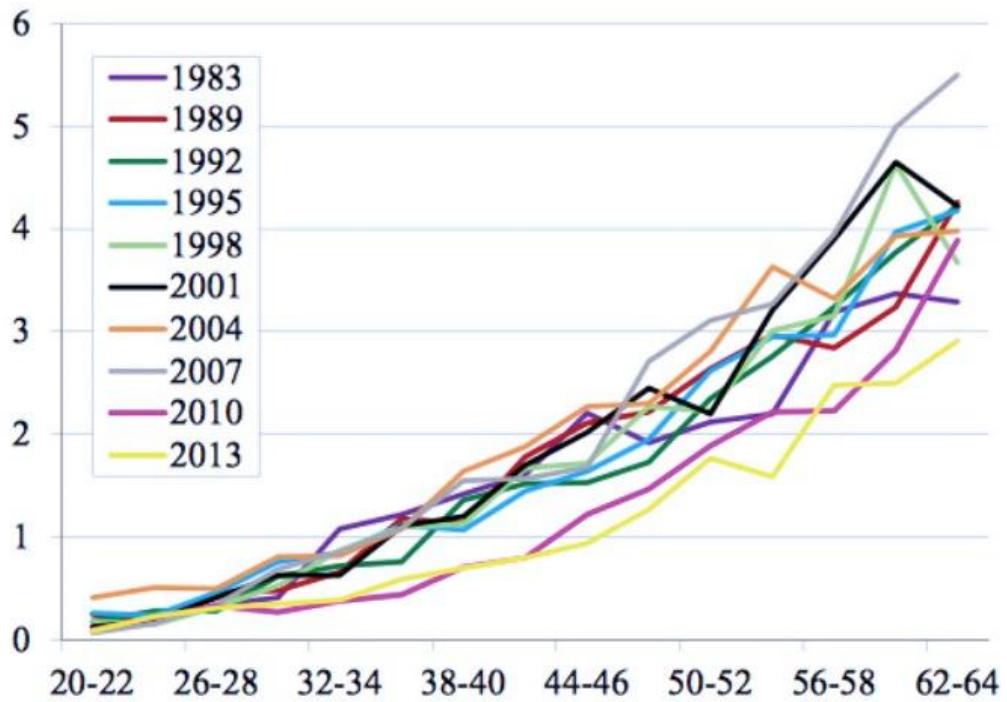


Figure 5: Ratio of wealth to income by age, 1982–2013.

Note: Based on data from the Survey of Consumer Finances.

Source: Munnell (2015a), Figure 1.

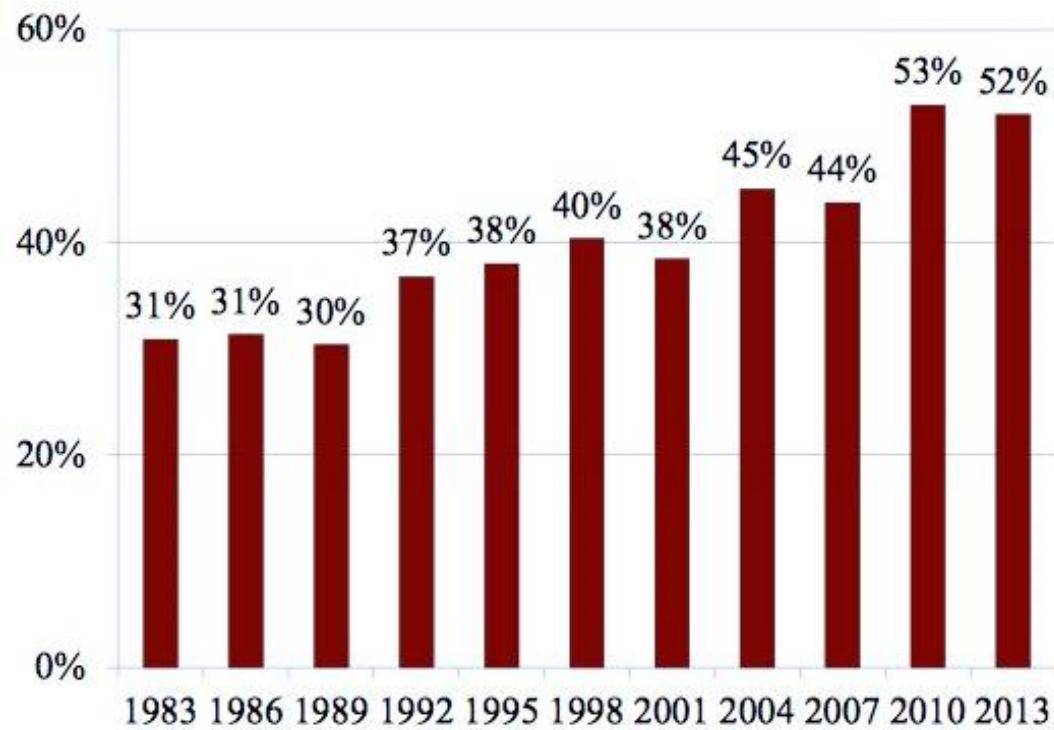


Figure 6: The National Retirement Risk Index, 1983–2013.

Source: Munnell (2015a), Figure 2.

Table 1: Labor force participation rates, by age and gender, 1985 to 2014

	Men						
	55	60	62	65	68	70	72
1985	83.7	71.0	50.9	30.5	20.5	15.9	14.9
1990	85.3	70.5	52.6	31.9	23.4	17.1	16.4
1995	81.1	68.9	51.3	33.5	22.4	20.6	16.0
2000	79.8	66.2	53.0	35.9	28.1	20.2	18.5
2005	80.6	67.7	57.7	39.7	32.2	23.8	21.6
2010	82.2	69.0	59.0	42.7	33.4	24.7	23.9
2014	80.1	72.1	61.7	42.7	33.1	26.8	23.0
% Change							
1985-2014	-4%	2%	21%	40%	61%	69%	54%

	Women						
	55	60	62	65	68	70	72
1985	55.5	41.9	31.5	16.2	12.1	9.0	8.2
1990	59.8	44.8	34.9	20.6	15.2	11.7	8.0
1995	64.6	49.2	36.3	22.3	15.2	10.7	9.8
2000	65.2	51.5	38.7	23.2	16.6	10.9	10.8
2005	69.8	55.7	44.6	28.3	20.6	16.7	11.8
2010	72.8	61.0	49.7	33.7	23.7	17.3	14.6
2014	69.9	58.7	48.4	33.7	23.3	17.6	15.4
% Change							
1985-2014	26%	40%	53%	108%	93%	96%	87%

Source: US Bureau of Labor Statistics (2015).

Table 2: Prevalence and part-time status of bridge employment, phased retirement, and reentry, by gender and HRS cohort (horizontal percentages)

	n ^a	Still on or last observed on career job	Moved to bridge job ^b	Moved to no job	Don't know	Bridge job/ (bridge job + no job)	PT bridge job (%) ^c	SE bridge job (%) ^d	Reduced FTC job hours >= 20% (%)	On FTC	Moved	Reentered (%) ^e
Men												
HRS Core	1,417	36%	33%	27%	4%	56%	40%	17%	12%	7%	7%	
War Babies	586	39%	34%	23%	4%	60%	40%	16%	10%	8%	8%	
Early Boomers	656	38%	32%	26%	3%	55%	26%	14%	10%	5%	6%	
Mid Boomers	759	77%	7%	9%	8%	46%	60%	-----	-----	-----	-----	
Women												
HRS Core	1,145	35%	34%	28%	4%	55%	55%	11%	10%	10%	10%	
War Babies	406	35%	38%	22%	5%	64%	47%	9%	8%	7%	7%	
Early Boomers	558	37%	37%	24%	3%	61%	39%	10%	9%	2%	5%	
Mid Boomers	718	71%	12%	10%	8%	55%	83%	-----	-----	-----	-----	

Notes:

^a Includes respondents aged 51-56 on a wage-and-salary FTC job at the time of the first interview. Transitions are measured within 10 years of the first interview, with the exception of the Mid Boomers for whom transitions are measured within four years of the first interview (i.e., by 2014).

^b Does not include respondents who were not working for two consecutive waves following FTC employment and who later reentered.

^c Percentage of respondents working part-time in bridge employment as a percentage of all individuals who transitioned to a bridge job; part-time employment is defined as working fewer than 1,600 hours per year.

^d Percentage of respondents who were self-employed in bridge employment as a percentage of all individuals who transitioned to a bridge job.

^e Percentage of respondents who returned to paid work after not having worked for at least two consecutive waves at some point following career employment.

Source: Authors' calculations based on the Health and Retirement Study.