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It's Not Easy Being Gray: The New Rules of Retirement

The Urban Institute Retirement Policy Program and Health Policy Center

Falling stock prices cut deep into retirement accounts in 2008, dealing yet another blow to our fragile retirement income system. A generation ago, many retirees could count on guaranteed monthly pensions, Social Security, and Medicare for financial and health security. Instead of traditional pensions, many people approaching retirement today have 401(k)-type plans that have been battered by the plunging stock market. Promised benefits from Social Security and Medicare are not sustainable in the long run and will have to be cut unless additional revenues can be found. Declining home equity, rising health care costs, uncertain long-term care needs, low private saving rates, and rising federal deficits further cloud the retirement outlook.

It all adds up to a retirement dilemma that will affect all Americans, not only those nearing retirement. Workers will be expected to finance a large share of the bill for retirees: fixing government retirement programs could require higher tax burdens for everyone. We must think creatively about solutions that consider the whole interconnected cycle of work and retirement. In that spirit, the Urban Institute convened a roundtable of experts in retirement, aging, health, and long-term care policy to discuss the new rules of retirement and explore how public policies might adapt to the diverse needs of aging baby boomers.

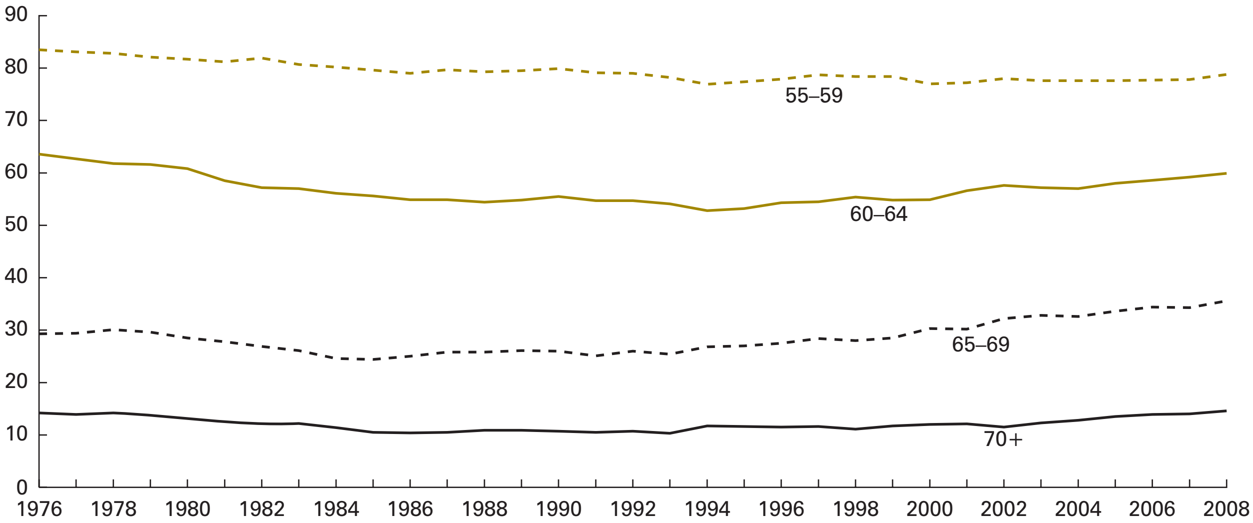
The Nexus of Work, Income, and Health

Recent losses in home equity and the stock market coupled with meager retirement savings and increasing health care costs could force many older adults to delay retirement and work longer—which isn't necessarily bad news. Americans are generally living longer and healthier lives, so for many, postponing retirement makes sense. And continuing to work may have emotional and physical health benefits. Older adults are already working longer than they used to. Between 1998 and 2008, the share of men age 65 to 69 in the labor force jumped from 28 percent to 36 percent (figure 1). The share of women age 65 to 69 in the workforce went up from 18 percent to 26 percent over the same period (figure 2).

Older adults' ability to work longer or return to work, though, depends on whether they are healthy enough to work, whether they can connect to the right jobs, and whether employers are willing to hire and retain them. Surveys show that employers value older workers' experience and long-held client networks (Pitt-Catsouphes et al. 2007), but some—especially those that view older workers as costly or those in slow-growth industries—are lukewarm about retaining older workers (Eschtruth, Sass, and Aubry 2007).

Finding the right job or keeping a job can be challenging. The unemployment rate, 7.2 percent at the end of 2008, is on the rise, limiting opportunities for older adults. Historically, unemployment rates have not been particularly high for older workers, partly because many choose to retire early when work is hard to find (Black and Liang 2005). But older adults' unemployment rates are beginning to go up, as fewer can now afford to retire early. Today's labor market places a high value on technical skills that many older adults lack, potentially reducing the number of jobs available to them. The consequences of job loss are also more serious for older workers than for younger workers, because seniors have more difficulty finding new positions.

FIGURE 1. Male Labor Force Participation, Age 55 and Older, 1976–2008 (percent)



Source: Urban Institute estimates from the Bureau of Labor Statistics (2008).

Note: The labor force participation rate is the portion of the noninstutionalized population that is employed or looking for work.

What about older adults who aren't healthy enough to work? Four in 10 workers in their fifties have jobs with some physical demands (Johnson, Mermin, and Resseger 2007), which they might not be able to meet as they grow older. Even for workers in jobs that aren't strenuous, health problems can keep many from working. More than a quarter of adults age 65 to 69 have a health problem that limits the work they can do. And about one-third of all Americans develop a health-related limitation in their fifties and sixties (Johnson, Mermin, and Murphy 2007).

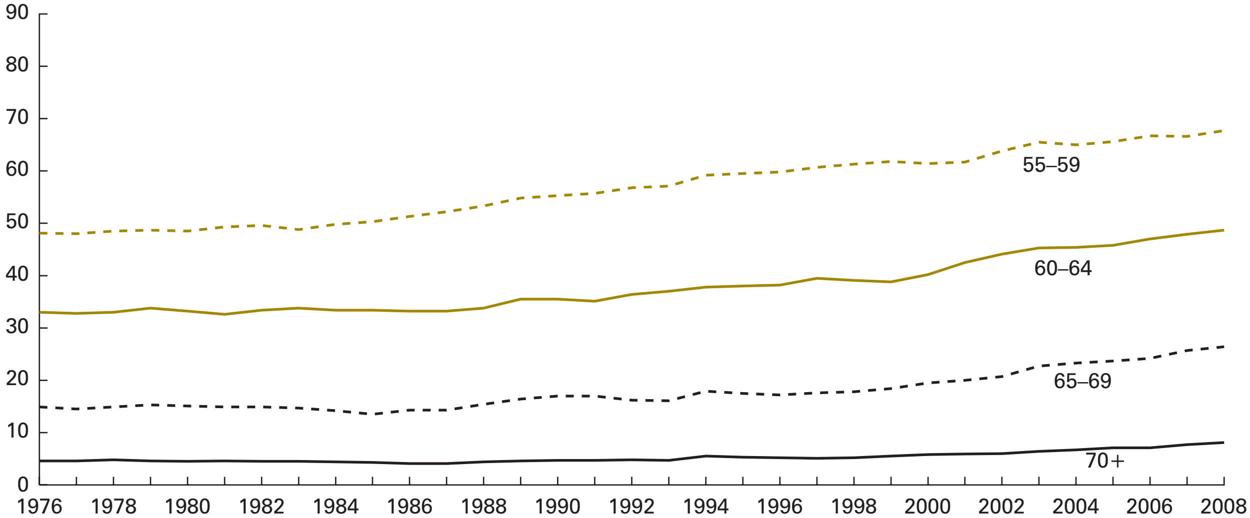
Social Security Disability Insurance (DI) is supposed to serve as a safety net program for these workers, but relatively few qualify for benefits. DI imposes a strict disability test that requires workers to prove that they are unable to work at any job. Applicants also contend with long waits as underfunding has led to a growing backlog. Compounding the problem, disability applications have been soaring, partly because the increase in Social Security's full retirement age to 66 makes DI benefits more attractive.[1] As a result, applicants often spend two or more years negotiating the process, usually with the help of professional legal assistance (Social Security Advisory Board 2008). The scheduled 2022 increase of the full retirement age to 67 will exert further pressure on the system, as would any additional increases in the retirement age to improve solvency. There's no consensus on whether we should update the method for determining DI eligibility now or wait until the system's administrative problems are fixed and the backlogs are cleared.

Diversity Matters

Effective policy to address these problems—to help older workers find and retain jobs and to strengthen our work and retirement safety nets—must recognize the diversity of both employers and older adults. Some industries whose skills are in short supply are eager to hold onto older workers. The oil industry, for example, wants to retain its older, more experienced engineers but not necessarily the 70-year-old dock worker on the oil rig. According to one participant, employers are concerned that policymakers will ignore these distinctions and treat all jobs and workers the same.

While this demand for particular skills boosts opportunities for well-educated workers, where does it leave low-skilled workers who can be more easily replaced by new technology or

FIGURE 2. Female Labor Force Participation, Age 55 and Older, 1976–2008 (percent)



Source: Urban Institute estimates from the Bureau of Labor Statistics (2008).

Note: The labor force participation rate is the portion of the noninstutionalized population that is employed or looking for work.

younger workers? Where does it leave workers in physically demanding jobs? A small minority of older adults gets job training through the Workforce Investment Act (WIA), a federal program that funds state-run job centers. A few states are focusing on older adults as a priority group, but most are not (Eyster, Johnson, and Toder 2008). The federal government also funds the Senior Community Service Employment Program to help low-income adults age 55 and older find community service jobs and other training. But this program serves fewer than 100,000 older adults annually and most clients are women living in poverty (Sum and Khatiwada 2008).

The number of older low-income adults who could benefit from employment and training services already far exceeds their capacity. WIA funding for employment and training services, for example, has declined by nearly 70 percent since the late 1970s (Holzer and Martinson 2008). More funding is needed, especially as the population ages.

Keeping Older Workers Engaged

In the past, when young workers were streaming into the labor force, policymakers and employers came up with innovative ways to encourage retirement. Now, as the pool of younger workers stagnates, we need to channel that creativity into keeping older people engaged with paid work, volunteering, or some combination of both.

Older workers may be more willing and able to stay employed if they could work flexible schedules. Employers in a slow economy, however, may not embrace such options as job sharing, extended leave, and phased retirement. This is where the public sector could step in and take the lead. More service providers will be needed as the nation grows older. For example, seniors age 80 and older, the fastest-growing demographic group, will need home care and other services that help them remain in their communities. Younger seniors in good health and with free time could be part of the solution, helping staff the jobs that serve the oldest old. The public sector could facilitate the match between new service demands and seniors wanting to help fulfill this demand.

Many seniors volunteer formally, and more would likely contribute if opportunities were more apparent. Some seniors, for example, help in low-income schools through programs like Experience Corps, which provides seniors with meaningful activities and a small stipend to cover some of their out-of-pocket costs. Others may want to move into paid positions in public-interest fields. About 9.5 percent of Americans age 44 to 70 (8.4 million people) are pursuing encore careers in the public sector, according to a survey by Civic Ventures (2008). This survey also indicates that roughly half of those age 44 to 70 who are not in an encore career want to be in one. Colleges and universities can tap into these aspirations by finding innovative ways to educate older adults who may lack the skills or experience to move into service work.

With creative ideas, one participant said, we can satisfy older Americans' need to work and desire to be engaged and turn it into an individual and public good. Diversity matters here, too, and should be reflected in policy. Low-income seniors are less connected to networks that open doors to volunteer work and encore careers. One participant mentioned the importance of recognizing informal volunteer contributions, especially by low-income minority seniors.

Health Care Costs Loom Large

Although Medicare provides near-universal health coverage to older Americans, many still struggle to cover their medical expenses. For one thing, Medicare excludes certain services, such as long-term care and dental care. Costs to beneficiaries can rack up quickly with Medicare's high premiums, deductibles, and cost sharing. In 2004, Medicare beneficiaries age 65 and older paid, on average, almost $4,000 out of their own pockets.[2] The median beneficiary spent about 11 percent of his income on health care. The largest share of spending went to premiums (for Medicare, Medigap, and employer health plans), followed by long-term care and prescription drugs. These estimates predate Medicare Part D, which began covering drug costs in 2006. However, early estimates for 2006 show that prescription drugs still consume a large share of senior health care spending, because Part D benefits are incomplete.

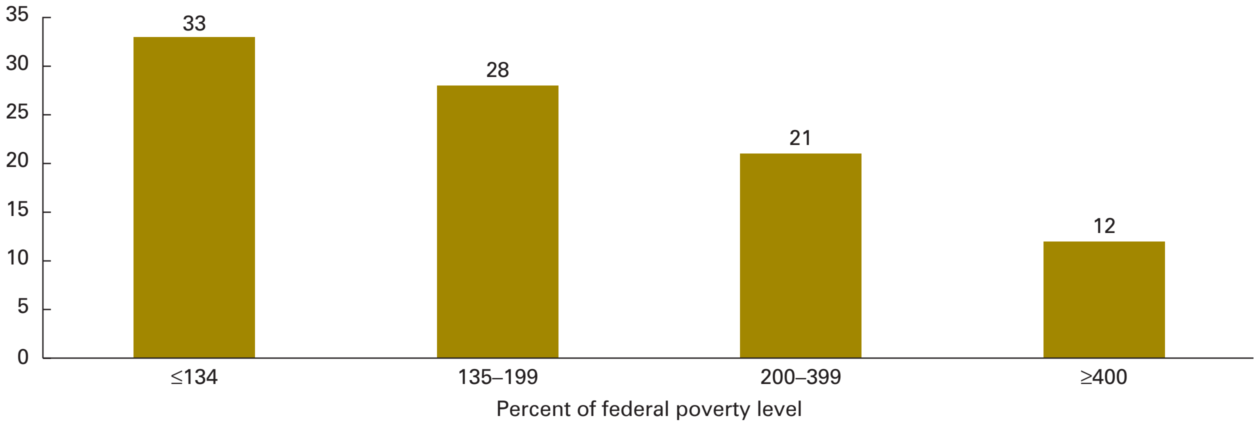
The health care cost burden on low-income people is large and growing. In 1997, about 43 percent of Medicare beneficiaries with incomes below 135 percent of the federal poverty level spent one-fifth or more of their incomes on health care. In 2004, 54 percent of these beneficiaries spent that much of their incomes on health care. Other data from the Consumer Expenditure Survey show how the share of income devoted to health care for seniors on Medicare generally declines as income rises (figure 3).

Medicare subsidizes outpatient services and prescription drugs, but these subsidies are out of sync with low-income needs. Medicare charges the same premium to people with incomes between roughly 135 and 800 percent of the federal poverty level. One participant maintained that a more sensible approach might be to tilt the premium schedule, charging lower rates for low- and moderate-income beneficiaries and higher rates beginning at about 400 percent of the poverty level, with premiums continuing to rise gradually at higher incomes. Another warned that, while making Medicare more progressive may be the reasonable choice, it's important to keep track of the cumulative effect of benefit reductions across retirement programs to avoid creating disincentives to work among higher-income beneficiaries.

Retirement Income Adequacy

So, have baby boomers saved enough for retirement? The short answer is no, according to one participant. But reaching a *definitive* answer is complicated because how much an individual needs to save is partly a question of taste. Most evaluations of retirement well-being compare retirement income to earnings received at younger ages, but well-being really comes down to how much retirees want to consume. Big-ticket items, such as college tuition and home purchases, are often paid off by the time people retire, so many retirees can maintain their standard of living with less money than simple earnings-replacement measures might suggest.

FIGURE 3. Average Out-of-Pocket Health Care Spending as a Percentage of Income in 2003, for Poor and Middle-Income Individuals Age 65 and Older



Source: Fishman, Tamang, and Shea (2008).

Note: Data are from the Consumer Expenditure Survey.

The slump in stock values has intensified concerns over retirement income as retirement assets have plummeted, but the repercussions will be limited primarily to higher-income adults. Older low-income adults rely mostly on Social Security, which replaces a large portion of their income in retirement. Social Security is especially important for older adults with limited education and for minorities (figure 4). Home equity is a potential source of retirement income, but tapping into it can be difficult. Reverse-annuity mortgages are expensive and home values have declined in recent years.

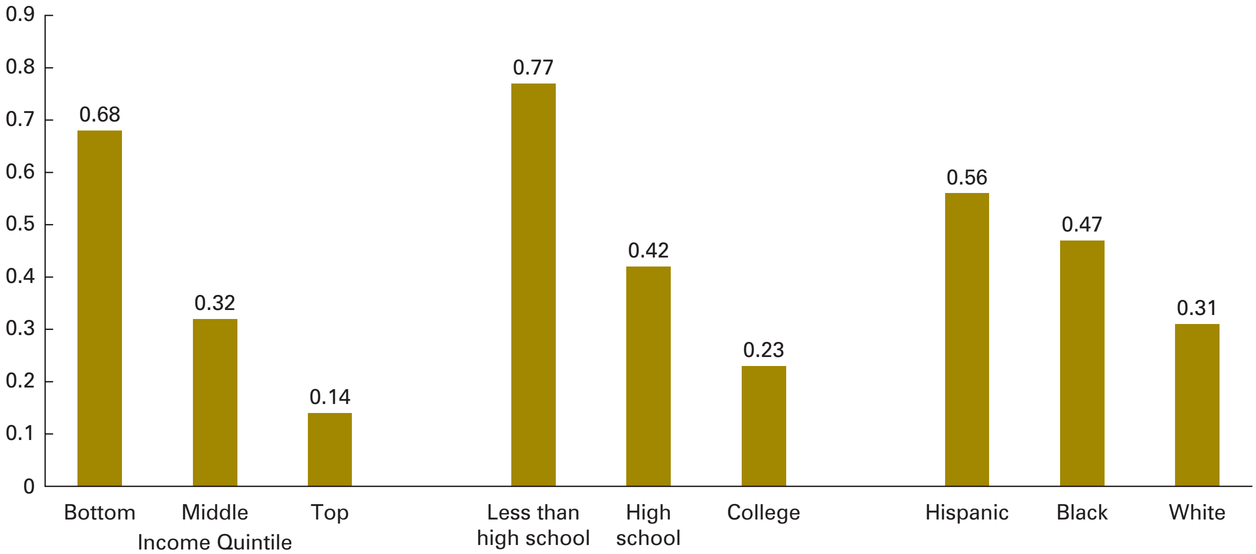
It's hard to say if baby boomers have saved enough because the cost of retirement is dependent on some unknown, potentially hefty, expenses. Retirement income needs to go further now than it did a generation ago because health care is more expensive and people are retiring earlier and living longer. Health care cost inflation is the largest uncertainty overshadowing retirement. Older Americans, especially those with few resources, already devote a significant share of their income to health care and could end up spending much more in the future if health costs continue to rise.

Long-term care is another wild card. Nursing homes are prohibitively expensive, Medicare covers only short-term post-hospitalization care, and Medicaid doesn't help until people have already depleted nearly all their resources. Private long-term care insurance is a possible solution, but few Americans purchase such insurance, partly because premiums are high and some mistakenly expect that Medicare or Medicaid will cover their needs. One participant suggested that the current system works for most Americans, while another argued for mandating long-term care insurance with income-related subsidies for premiums. Before we get to that point, another participant warned, insurance must be standardized and those who have already purchased insurance should be guaranteed that they will not have to pay twice. Decisionmakers should also remember that much long-term care is provided for free by family and friends. This informal care doesn't appear as an expense in government ledgers, but it creates tremendous burdens for many families.

Coping with Government Programs and Other Financial Choices

Social Security, DI, Medicare, and Medicaid all serve older Americans, but some roundtable participants raised concerns about how well they can meet the needs of a growing senior

FIGURE 4. Median Ratio of Social Security Wealth to Total Wealth for Households Age 55–64 by Income, Education, and Race in 2001 and 2004



Source: Mermin, Zedlewski, and Toohey (2008).

population. Because these government programs are so complex and difficult to understand, few older adults use them to their maximum benefit. Increases in Social Security's full retirement age have reduced the benefit for early retirement. Older workers must understand the consequences of retiring early and the benefits of working longer. With both members of a couple typically working now and able to qualify for Social Security benefits on their own earnings records, spousal benefits have become more complex and should be clarified. For example, couples may get a better deal if the lower earner retires first on his or her own record and then converts to a higher spousal benefit later on.

As already discussed, DI presents a particularly difficult challenge because assessing eligibility can take two years or longer and the backlog is growing as more boomers apply. Deciphering health benefits can be equally taxing for retirees. Understanding coverage under the different parts of Medicare and figuring out how it intersects with benefits from a current or former employer requires intensive study. Benefits for long-term care are not well understood.

Policy Implications

Older Americans face an uncertain retirement future if nothing is done to shore up Social Security and Medicare, get health care spending under control, and make staying in the labor force at older ages easier, while still protecting disabled workers. The following policy implications, which summarize the roundtable discussion, address these urgent needs.

- Older adults will likely have to postpone retirement and work longer to supplement pensions battered by the stock market collapse and to ensure against soaring health care costs. We need to rethink public policies that encourage early retirement, like the Medicare secondary-payer rule that requires employers—not Medicare—to cover most health care costs for workers age 65 and older. Older workers, especially low-income seniors, could also benefit from employment services focused on connecting them to jobs and training.

- Volunteer opportunities offer a way to connect older adults to meaningful activities while meeting the growing demand for social services. Volunteer work can also connect older adults to paid work in nonprofits and the public sector.
- How much adults need to save for retirement should be based on consumption, not income replacement. Savings requirements vary by income, health care needs, and the share of preretirement income replaced by Social Security benefits.
- Health care cost inflation is the biggest uncertainty facing older Americans. National health care reform must consider the needs of older adults, especially the high out-of-pocket costs for low-income seniors.
- Government should do more to help seniors best use the benefits that programs offer. Social Security DI must cut through its backlog and provide quicker disability assessments. Older adults also need clarity on Social Security, especially on how spousal benefits and the timing of retirement affect lifetime benefits. They need simpler information on Medicare premiums and out-of-pocket spending requirements.
- Public policy should recognize the diversity of the older population. Rather than provide new entitlements to everyone, assistance should be tailored to the needs of different income groups. Decisionmakers must consider this diversity when shaping Social Security and Medicare reform and policies that affect employment.

Notes

This brief summarizes an invitation-only roundtable discussion at the Urban Institute on December 2, 2008. Experts in income security, health, work, and volunteerism participated in a wide-ranging discussion of retirement and aging to explore how public policies might adapt to the aging population. The organizers of the roundtable, Richard Johnson, Eric Toder, Stephen Zuckerman, and Sheila Zedlewski, wish to thank Ruthie Cabelli, Jam Tashi, and Corina Mommaerts for their assistance in preparing for the roundtable. Also, we would like to thank Serena Lei for her assistance in preparing this policy brief. We also would like to thank the Rockefeller Foundation for their support of this roundtable and the Retirement Policy Program at the Institute.

1. Benefits are reduced for those who retire before the normal retirement age, currently age 66. These benefit reductions do not apply to DI beneficiaries.

2. The out-of-pocket health care spending costs covering the period 1994–2004 were tabulated by the Urban Institute using the Medicare Current Beneficiary Survey.

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