Worries and Plans as Individuals Approach Retirement

by Paul J. Yakoboski, Ph.D.

The primary objective of an employment-based retirement plan is to provide a secure and adequate income for workers throughout retirement. In the defined contribution (DC) framework, asset accumulation is a means to the end, but not the end. Drawing retirement income from savings and paying for health care expenses in retirement are the two issues that concern individuals the most as they approach retirement. This article examines the attitudes of near-retirees regarding these risks and their plans for managing them. The author discusses how DC plan design can have a major impact on how individuals convert their retirement savings to retirement income; differences in survey responses between those who have consulted a financial advisor or other financial professional and those who have not; and the role of trust in implementing advice.
ment Medicare, copayments, deductibles and payments for otherwise uncovered services and supplies, but 35% say they do not know how much the typical retiree spends and an additional 34% think it is $5,000 or less. So two-thirds of near-retirees do not have a realistic perception of the health care expenditures they likely face once retired.

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WHAT WORRIES NEAR-RETIREES

While 80% of higher education near-retirees intend to maintain their current standard of living (or enjoy a higher standard) in retirement, 22% are very concerned about outliving their savings; an additional 43% are somewhat concerned. Essentially the same percentages, 20% and 47%, respectively, are very and somewhat concerned about choosing the best way to draw income to live on from their retirement savings. Concern over converting assets to income is understandable. The timing and amounts of withdrawals must be decided in a framework where average life expectancies of a 65-year-old are 17 years for a man and 20 years for a woman. But these are only averages; a 65-year-old man has a 50/50 chance of living to the age of 85, and a 65-year-old woman has a 50/50 chance of living to 88. For a couple both aged 65, there is a 50% chance that one will live to the age of 92. Inflation rates and investment returns over such time spans can not be predicted with certainty, but can have dramatic effects on the real income levels of retirees.

The challenge of meeting health care needs in retirement is even more worrisome to higher education near-retirees—42% are very concerned about being unable to afford good health care in retirement, with an additional 29% somewhat concerned. In fact, near-retirees are more concerned about health care than with any other issue they will face in retirement. Accompanying this concern about affording care, and likely contributing to and reinforcing it, is a great deal of uncertainty among near-retirees regarding the amount typically spent out of pocket during retirement for health care-related expenses. The typical retiree can expect to pay approximately $10,000 annually to cover premiums for insurance to supple-

CONVERTING ASSETS TO INCOME

Forty percent of near-retirees report that they do not have a good understanding of the options available for converting retirement savings into retirement income; 46% understand the options somewhat and 14% feel that they understand available options very well. Not surprisingly, understanding appears related to the level of thought that has been given to the issue—36% have really not considered it, 46% have thought about it some and 17% have thought about it a great deal. Older near-retirees have given more thought to managing their retirement savings for income and report a greater level of understanding regarding available options.

When asked about current intentions for drawing income from their retirement savings, regular periodic withdrawals of a fixed percentage of savings was the most common option chosen (37%). Withdrawing only the minimum amount required by law and annuitizing some or all of their retirement savings were chosen by 29% and 25%, respectively. Nine percent did not know what they will likely do.
Annuitzation is the only means to guarantee a consistent level of income that will last the lifetime of a retiree (and his or her spouse in the case of a joint-and-survivor annuity). In a separate survey of individuals who had retired with significant DC assets but no meaningful defined benefit income, 19% reported that they had annuitized at least some of their savings. The challenge from a retirement income security perspective is creating the intent to annuitize during accumulation and encouraging follow-through on that intent in retirement. In this regard, the survey of retirees highlights the importance of annuities in the design of a DC plan, both in the accumulation and distribution stages. Retirees who have annuitized their retirement savings are more than twice as likely, compared with retirees who have not annuitized, to have saved through an annuity in a DC plan while working. And one-third of annuitants annuitized through a DC plan.

Advice and Annuitzation

Fifty-eight percent of near-retirees rated receiving advice as they near retirement on managing and drawing income from savings in retirement as very important, plus almost 30% considered it somewhat important. But only 30% of near-retirees in higher education have consulted with a financial advisor or other financial professional within the past two years specifically about drawing income from savings during retirement. These individuals appear to be better prepared to address the issue than those who have not received such advice; they were more likely to report that they understood their options very well (29% compared with 15%) and more likely to have thought a great deal about how they will manage their savings and draw income in retirement (34% compared with 19%). In addition, they are less concerned than their peers about outliving their retirement savings. There is little difference, however, in the level of concern about choosing the best way to draw retirement income; two-thirds of each group are concerned in this regard. This could be explained by a higher initial likelihood of concern among those consulting with an advisor, with this interaction then subsequently lowering the level of concern. Twenty-nine percent of those who have consulted with an advisor on drawing income from savings plan to annuitize some or all of their retirement savings compared with 24% of those who have not consulted an advisor. It is somewhat surprising that there is not a greater differential in this regard. From the survey of retirees, it is apparent that the use of an advisor and the advice received matter when deciding how to manage savings during retirement. While only 3% of nonannuitants were advised to buy an annuity, 71% of annuitants worked with a financial advisor in deciding to annuitize and/or implementing the decision.

MEETING HEALTH CARE EXPENSES

Relatively few near-retirees have given a great deal of thought to how they will pay for medical expenses in retirement not covered by Medicare or insurance, including premiums, copayments and deductibles. This does not differ by whether they are expecting health insurance through their employer. Sixteen percent of those with employer coverage and 23% of those without or who are uncertain have given a great deal of thought to how they will pay for uncovered expenses; 46% of those with employer coverage and 37% of those without or who are uncertain have given little if any thought to the issue. Planning for such expenses appears limited at best among near-retirees.

Survey respondents were informed that the typical person retiring today at the age of 65 will need at least $100,000, and possibly more than $200,000, to pay for health care expenses during retirement. Respondents were then asked how well-prepared they felt to meet such expenses. Twenty-three percent feel very well-prepared, 43% somewhat prepared and 32% do not feel well-prepared. However, given the lack of thought focused on addressing the need, many individuals may not be as well-prepared as they seem to think.

In addition, there appears to be a fair amount of uncertainty regarding how employer-sponsored insurance coordinates with Medicare. One-third of those expecting retiree health insurance do not know if that insurance covers individuals who retire before Medicare eligibility at the age of 65 and 37% do not know whether it covers expenses that Medicare does not after the age of 65.

A savings vehicle specifically earmarked to pay health-related expenses during retirement appeals to most near-retirees. Twenty-one percent say they would be very likely to contribute to such a savings plan, with an additional 42% somewhat likely to contribute.

Advice and Retiree Health Care

Analogous to managing assets for income in retirement, 58% of near-retirees rated receiving advice as they near retirement on paying for health care expenses in retirement as being very important, plus
almost 30% considered it somewhat important. But even less—17% of near-retirees—have consulted with a financial advisor or other financial professional within the past two years specifically about retirement health care expenses. Those receiving advice on paying for health care expenses in retirement were more likely to have thought a great deal about how they will manage premiums, deductibles, copayments and other expenses not covered by insurance or Medicare (32% versus 18% for those who have not received such advice) and more likely to consider themselves very well-prepared to meet such expenses (49% versus 32%).

**FINAL THOUGHT ON ADVICE . . . TRUST**

A crucial issue in the advice process appears to be the trust factor as receiving advice does not automatically translate into implementing the advice. Among higher education near-retirees who have consulted with a financial advisor within the past two years, 17% reported always implementing the recommendations of their advisor(s) and an additional 52% implemented their advisor’s recommendations most of the time; 28% followed through on the advice some of the time and 3% hardly ever followed the advice received. A likely reason for nonimplementation among some is trust. Advice received is viewed as always being independent and objective by only 25% of those who typically do not implement an advisor’s recommendations compared with 55% of those who typically implement. Addressing the trust issue is important given that concern over various aspects of retirement planning is lower for those implementing advice received compared to those who receive but do not implement advice.

**Endnotes**

1. 1,002 individuals were surveyed by telephone during April and May 2009 regarding their financial preparations for retirement and their views regarding those preparations. PublicMind of Farleigh Dickinson University fielded the survey and collaborated with the TIAA-CREF Institute on development of the questionnaire. Survey results were weighted to be representative of the population of interest. Individuals who did not envision themselves as ever retiring or leaving the workforce for any reason were excluded from the survey.


4. Sixty percent report consulting with a financial advisor regarding their retirement preparations in general and 50% of these covered how to draw income from savings in retirement. The investment allocation of their savings is the most common issue covered in near-retiree consultations with an advisor; 89% reported receiving advice on how to invest their retirement savings.

5. One-half of higher education near-retirees report that their institution provides health insurance to its retirees, 32% report that it does not and 18% do not know.


7. Sixty percent report consulting with a financial advisor regarding their retirement preparations in general and 28% of these covered meeting retirement health care expenses in retirement.


**THE AUTHOR**

Paul Yakoboski, Ph.D., is a principal research fellow with the TIAA-CREF Institute. He conducts, manages and communicates research on issues such as DC plan design, income and asset management in retirement, individual decision making and preparation for retirement, options for funding retiree health care, managing faculty retirement patterns, and topics relevant to strategic management in higher education. He is responsible for the development and execution of Institute symposiums on such issues. Yakoboski serves as director of the Institute’s Fellows Program and editor of the Institute’s *Trends and Issues* and *Advancing Higher Education* publication series. Previously, he held positions as director of research for the American Council of Life Insurers, senior research associate with the U.S. Government Accountability Office. Yakoboski also served as director of research for the American Savings Education Institute and adjunct faculty member at Nazareth College in Rochester, New York. Yakoboski is a member of the American Economic Association and the National Academy of Social Insurance, and serves on the editorial advisory board of *Benefits Quarterly*. He earned his Ph.D. and M.A. degrees in economics from the University of Rochester and his B.S. degree in economics from Virginia Tech.