Helping Employees Manage Retirement Risks

by Cynthia Levering

Employers may want to review their benefit and financial education offerings to help employees understand risks they face in retirement and make better decisions when they have options.
As employees have become increasingly responsible for their own financial security, it has become more important for plan sponsors to understand what knowledge individuals have and how they make decisions for their retirement security. These key questions may help employers focus on opportunities for change:

- Are we doing enough to help our employees plan for the postretirement as well as the preretirement period?
- Where are there gaps in employee knowledge and action?
- Do our benefits, services and communication programs recognize the reality of employees as they are reaching retirement?
- What improvements can we make in our benefits within our budget constraints?

This article presents highlights of the Society of Actuaries (SOA) 2015 Risks and Process of Retirement Survey, which offers insights into how the public perceives and manages the risks of retirement. Employers may find the information helpful in structuring their benefit plans and offering planning tools and employee education.

For more than 15 years, the SOA Committee on Post-Retirement Needs and Risks has focused on improving retirement outcomes. The 2015 survey, conducted in mid-2015, is the eighth biennial study of public
perceptions related to postretirement risks. It targeted some new, specific aspects of risk such as financial shocks (or dealing with the unexpected) and debt in retirement as well as how the experiences of parents influenced their children’s planning processes. It was preceded by focus groups conducted with both U.S. and Canadian retirees who had been retired 15 years or more.²

**Survey Findings and Commentary**

Employers may be interested to know that basic concerns and strategies for risk management for both retirees and preretirees in this survey series have been consistent over time.

**Risks Viewed as Most Important**

The retirement risk that most concerns both retirees and preretirees is long-term care (69% of preretirees and 58% of retirees are very or somewhat concerned). Rounding out the top three concerns are inflation (69% and 52%) and having enough money to pay for adequate health care (67% and 47%). Approximately two-thirds of preretirees and four in ten retirees also express concern about the possibility of depleting their savings (62% and 43%) and maintaining a reasonable standard of living for the rest of their life (63% and 45%).

This series of postretirement risk surveys consistently has found that the top three concerns are inflation, paying for health care costs and paying for long-term care. Significant changes in economic conditions appear to generate only a temporary change in levels of concern, if any at all.

**Keeping Results in Perspective**

Even though there are many risks Americans face in retirement and retirees are often on their own in dealing with these risks, many people are not too concerned about some of them. A significant number of retirees may not be aware of all of the risks. For example, there seems to be little concern or awareness about the risk of fraud or a scam. However, scams can be devastating. Employers can help employees be aware of good practices and materials such as those from the Consumer Financial Protection Bureau to help them avoid scams.

**Managing Risks**

Among new questions designed to provide more understanding of risk management, the 2015 survey asked what people were most likely to do if they were running out of money. Reducing expenditures significantly was the top result, with 90% of retirees and 88% of preretirees indicating they would do this.

Work was a major area of focus for preretirees, with 74% of them indicating they would either try to return to work or increase the number of hours they were working, compared with only 35% of retirees.

Downsizing housing was also a major area of focus, with 65% of preretirees and 55% of retirees choosing this option. Housing is a major expenditure, but some already may have downsized.

These responses were in sharp contrast to the number who indicated they would get help from family members, friends or communities. Only 20% to 25% expected to get help from either family members or friends and community agencies.

The 2015 survey and focus groups were designed to dig deeper into what events occurred in retirement that could derail or complicate a retiree’s financial status. Overall, these events, considered shocks, had a material impact on many retirees, with more than one in three survey respondents experiencing financial shocks that depleted at least 25% of their assets and more than one in ten retirees stating they needed to reduce their spending by 50% or more as a result of shocks. The types of shocks mentioned most frequently included major home repairs, dental expenses, prescription drug costs and divorce. The research team observed that many retirees were surprised by expenses that can be expected but for which the timing is somewhat unpredictable.

There is a strong preference for maintaining or increasing asset levels in retirement. The most common retirement asset management strategy is maintaining financial assets by withdrawing only earnings and leaving the principal intact. About one-quarter try to grow their assets, but only two in ten plan to spend down their assets. The rest have no plan for how they will manage their assets in retirement. Over 60% of preretirees and 40% of retirees do not have a plan for how much money they will spend each year and where that money will come from. It is encouraging to see that most retirees and retired widows (72%) spend about what they can afford each year.

As in previous iterations of the risk survey, both preretirees and retirees tend to focus on strategies of saving and spending to manage the risks associated with retirement. A significant percentage of preretirees (88%) and retirees (86%) report they have already eliminated or plan to
eliminate all of their consumer debt. Nine in ten preretirees (90%) and three-quarters of retirees (74%) say they already have saved or plan to save as much as they can, while similar proportions have already cut back or plan to cut back on spending.

Preretirees and retirees are much less likely to turn to risk pooling strategies to manage retirement risks (other than health insurance). Half of preretirees (50%) and two in ten retirees (20%) indicate they plan to or have already postponed taking Social Security. Only one-third of preretirees and one-quarter of retirees report buying (or expecting to buy) an annuity or choosing an annuity option from an employer plan. There is relatively low interest in financial products for risk management except for health insurance (including Medicare supplements).

Keeping Results in Perspective

Many people do not have enough financial assets at time of retirement and during retirement to effectively use risk pooling strategies such as annuities. An emergency fund is a first priority, but many people do not have adequate emergency funds. Plan sponsors’ educational efforts and tools can help build awareness and knowledge about this topic.

Both prior and recent focus group results indicated that many resource-constrained retirees prefer to hold onto assets, making them available as an emergency fund. They try not to spend down their assets and generally limit withdrawals to the required minimum distribution amounts at the age of 70½ and later. In the focus groups, some participants even expressed that they didn’t like having to take these distributions. Retirees also appear to be surprisingly resilient in their ability to absorb and adapt to shocks. These findings reinforce the value of offering retirees the option to keep funds in the plan and of having a variety of good distribution options.

Death of a Spouse

Few of the respondents expect to experience negative financial consequences from the death of a spouse. Among those who are married, both preretirees and retirees believe the death of a spouse would have little effect on the financial situation of the survivor. However, four in ten married preretirees think their spouse would be better off financially if they were to predecease their spouse. Fewer than two in ten in both groups think the survivor would be worse off.

Keeping Results in Perspective

As it has become increasingly clear there are major gaps in financial literacy and analytical approaches to planning, it becomes much more important and interesting to learn what factors influence how people think about financial risk and longer term decisions. The research shows that many households do not have a good understanding of the impact of the death of a spouse, especially if there was a long period of illness prior to the first death and if the survivor was a caregiver. The research also shows that many people are not doing a careful analysis of their long-term financial situation, and the impact will be very different depending on the family. Plan sponsors can help employees achieve better results with regard to planning for the death of a spouse and for long-term care by the structure of their benefit plans and educational programs.

Overall Results

Overall, there is much consistency in the results of this work, and some main conclusions have emerged:

• Preretiree expectations often do not line up well with the actual experiences of retirees. This is especially true with regard to retirement age and the expectation of working in retirement.

• Long-term care, inflation and having enough money to pay for health care consistently are the top three retirement concerns cited by both preretirees and retirees.

• Many retirees are taken by surprise by shocks—events such as major home repairs, dental expenses, prescription drug costs and divorce that can derail or complicate a retiree’s financial status.

• Over 60% of preretirees and 40% of retirees do not have a plan for how much money they will spend each year and where that money will come from.

• Plan sponsors can help build awareness and knowledge about strategies such as annuities and the importance of having an adequate emergency fund.

• Employers may want to assess what education, tools and advice they are supporting and how effective they are as well as consider offering benefits that help address risks such as long-term care and disability.

• Employers can help employees understand their options as far as timing of retirement and Social Security.

takeaways
• Inflation, health care and long-term care consistently are among the risks retirees and preretirees are most concerned about. There are several risks, like fraud or scams, that seem as though they should be important but retirees show little concern about.

• Preretirees often are more concerned than retirees.

• Reducing spending is the top risk management strategy among those surveyed, followed by increasing savings and paying off debt. The use of risk protection products (other than health insurance) is not very common.

• There are major gaps in retirement planning, and relatively short planning horizons are common.

• Longer term retirees appear to be managing well and are remarkably resilient, demonstrating the ability to absorb and adapt to most shocks. This may indicate the need for future research about traditional measures of retirement adequacy.

Retirement Timing

People actually retire at a much earlier age than those who are still working say they want to retire. In the 2015 study, the median age at which preretirees actually retired was 60 compared with 65 as the median age when people said they plan to retire. This is not surprising when involuntary and “pushed” retirements are considered.

Planning as One Nears or Enters Retirement

Planning tends to be cash flow-based and short-term—People make decisions based on what they are currently spending for routine expenses compared with the income they expect to receive. Most do not think about setting aside an emergency fund for things like major home repairs that can be anticipated (such as replacing a roof). Planning horizons for both retirees and preretirees consistently are only about ten years, which is inadequate to cover the period of retirement. Almost three in ten report they have not thought about their planning horizon (28% of preretirees and 29% of retirees), and one in ten says he or she does not plan ahead (10% of preretirees and 11% of retirees).

Working During Retirement

Working longer is an important strategy, but many more people say they want to do this than actually do work in retirement. Employers can support longer work with employment options and phased retirement programs.

Long-Term Care

The survey and in-depth interviews with caregivers found that when significant paid long-term care is needed, it is a major problem—across all of the economic ranges covered by the focus groups and the interviews.

Keeping Results in Perspective

Many people are reaching retirement age today without adequate preparation for what faces them. There are two different paths for dealing with this: Help people make better decisions and be better prepared, or structure systems to be less dependent on individual decisions. It seems unlikely that there will be much improvement in decision making, so default options and plans that work without individual action (like so-called autofeatures) continue to be very important.
fined contribution plan sponsors should also consider adding features such as lifetime income options to help individuals plan for the postretirement as well as the preretirement period.

Opportunities for Plan Sponsors

To improve programs, plan sponsors may want to consider:

- **Understanding postretirement needs and how programs fit in.** Employers may wish to review current programs to see what planning and postretirement risk issues are addressed well and to identify gaps in programs and information.

- **Aligning expectations and reality.** The research shows several areas where preretiree expectations do not fit with actual retiree experiences. Employers can help by providing information and also by modifying programs.

- **Addressing gaps in planning.** Can we communicate more effectively to our various constituencies by considering the different ways they perceive and approach planning? Employers may want to assess what education, tools and advice they are supporting and how effective they are. There are major opportunities in the area of offering better tools to support planning. The market includes a great deal of software, but much of it is focused on asset management. The average employee faces substantial issues different from and beyond asset management. The tools may not address those issues, and they may not focus on the specific situation at hand. Employees often respond well to employer-offered support systems.

- **Helping employees manage assets postretirement.** What products or plan features can organizations offer that better meet retiree needs? Employers will want to review whether defined contribution plans permit retirees to keep their assets in the plan and the payout options available. Both education about payout alternatives and employer-supported options are important. Lifetime income options are one way to help employees manage their postretirement income.

- **Improving risk protection.** The research shows important knowledge and action gaps with regard to planning for widowhood and long-term care. In both of these areas, employers can offer provisions in their benefit plans including company-supported benefits, products for voluntary purchase and education. Another risk often forgotten is disability risk and its impact on retirement.

- **Supporting desired retirement timing.** What happens to employees if they can’t afford to retire, and what happens to an organization when its employees can’t retire? A focus on adequacy is important to both employers and employees. For many employees, the timing of retirement and Social Security are critical issues, and employers can help them understand all of their options.

**Endnotes**

1. The complete survey report is available at www.soa.org/Research /Research-Projects/Pension/2015-risk-process-retirement-survey.aspx. Special reports focusing on the areas of emphasis will be released throughout 2016 and be made available on the website.

2. The focus group report can be found at www.soa.org/Research /Research-Projects/Pension/2016-post-retirement-experience-15-years .aspx. Results demonstrate that many members of the public need help in managing the postretirement period and show the value of employers offering support in that regard. They also demonstrate the need for more planning and better use of planning tools. (They do not demonstrate whether planning tools are adequate to handle the postretirement period.)

**Bio**

Cynthia Levering retired as a senior vice president and consulting actuary at Aon Consulting, where she regularly consulted with corporate and not-for-profit clients on the design, funding and administration of their qualified and nonqualified defined benefit, defined contribution and other postretirement benefit plans. Levering currently serves on the SOA Committee on Post-Retirement Needs and Risks (as both a member and part of the steering committee) and the Pension Section Research Team. She also is a member of the American Academy of Actuaries Lifetime Income Risk Joint Task Force. Levering received her B.A. degree in mathematics from Thiel College in Greenville, Pennsylvania and her M.S. degree in applied mathematics from the University of Maryland, Baltimore County. She is an associate of the Society of Actuaries and member of the American Academy of Actuaries. Levering recently was appointed to a three-year term on the Department of Labor ERISA Advisory Council.