

# Financial Security Research Symposium



## Assessing Financial Preparedness and Retirement Security

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**Financial Security Research Symposium**

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U.S. Treasury Department

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Notes for the slides can be found at the end of the presentation.

# Retirement Security is a Key Policy Priority

The aging of the **baby boom** means more retired households.

**Only half of Americans** polled by Gallup reported being confident that they will have enough money to **live comfortably in retirement**.

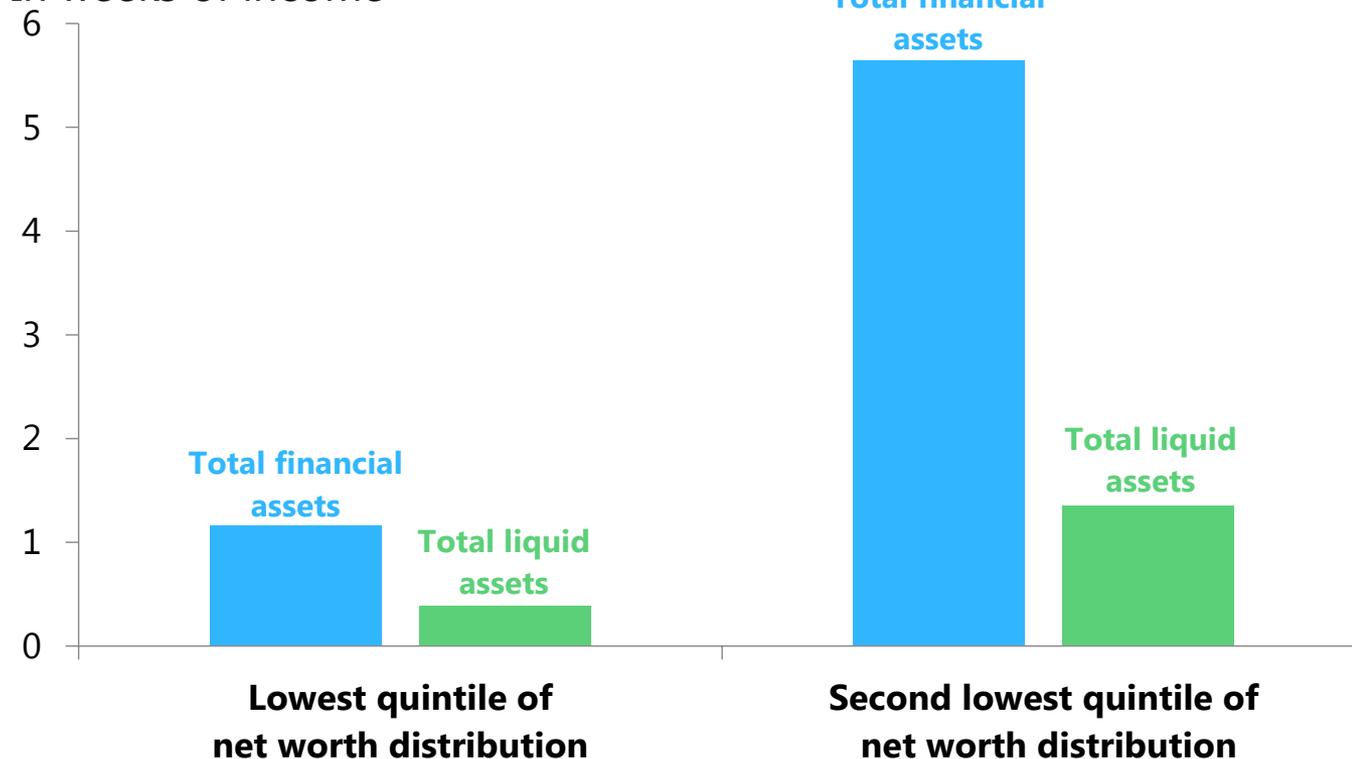
Many households nearing retirement have very **low levels of financial assets**.

There is some evidence that **today's pre-retirees** are **in worse shape** than earlier cohorts.

# Many Households Nearing Retirement Have Very Low Levels of Financial Assets

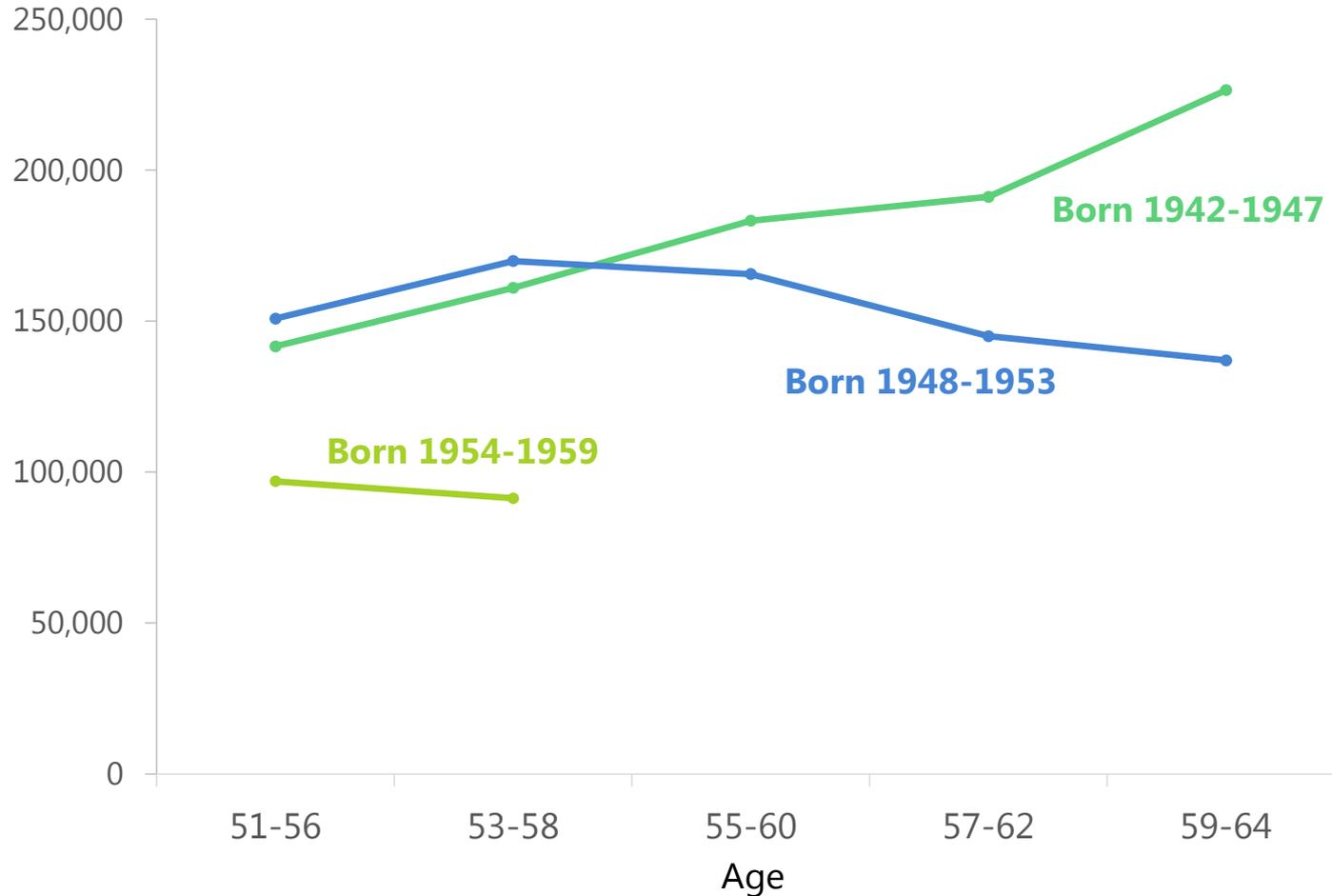
## Accumulated Financial Assets of Households with Heads Age 45-54, 2013

In weeks of income



# Today's Pre-Retirees Appear to Be in Worse Shape than Earlier Cohorts

## Real median household wealth



# Recent Strides Toward Better Retirement Security Policy

Important **research**:

On the limitations of traditional savings incentives

On the **importance of making saving easier and more automatic** for some types of households

**Actual policy developments** that build on this research:

“Auto-IRA” proposal in President’s budget,

State IRA programs

*myRA* program

# But Knowing More Will Help Us Make Better Retirement Policy

**Who** should policy target?

**How big** is the shortfall in savings for the key populations?

Beyond savings, **what else** should we be worrying about?

*Possible long-term care needs? Other uncertain outcomes?*

**Why** are some households more vulnerable?

*Role of different circumstances, preferences, behaviors?*

What are the relevant **policy levers**?

How are the answers to these questions **changing over time**?

*Impact of labor market changes, new technologies, etc.*

# Presenters in this Session will Speak to Many of these Questions

**Carvalho:** What financial tools older people use

**Rohwedder:** Who is at risk and by how much; uncertainty related to long-term care needs and dementia

**Houseman:** How the changing nature of work is affecting retirement security

**Mitchell:** How planning horizons vary across the elderly population and how these differences bear on their decisions

# Endnotes

**Slide 1:** Source - Riffkin, Rebecca (2014), "[More Americans Think They Will Retire Comfortably](#)," Gallup.

**Slide 2:** Source – Treasury calculations based on the 2013 Survey of Consumer Finances.

**Slide 3:** Source – Treasury calculations based on the 1998-2012 waves of the Health and Retirement Study.



LABOR AND POPULATION

***Economic Preparation for Retirement  
and the Risk of  
Out-of-pocket Long-term Care Expenses***

***Susann Rohwedder***

**Financial Security Research Symposium  
September 7, 2016**

*We gratefully acknowledge research support from the Social Security Administration via the Michigan Retirement Research Center, and additional support from the National Institute on Aging and the Department of Labor. All opinions are our own.*

# ***Adequacy of resources in retirement: No absolute standard***

- Lifetime resources vary across households
- Households poor during working life will be poor during retirement

**How to assess adequacy?**

# Assessing adequacy: Three methods

## 1. Income replacement rate:

Ratio of income after retirement to  
income before retirement

**But common implementations ignore**

- Financing consumption out of saving
- Time horizon or survival curve of the *household*
  - Lower survival chances of the poor
- Reduction in spending following widowling
- Consumption path is not flat, declines with age
- Taxes

## ***Assessing adequacy: Three methods (cont.)***

**2. Compare actual wealth at retirement with  
“optimal wealth”** (e.g., Scholz, Seshadri, Khitatrakun, 2006)

**Theoretically sound**

**But simplifying assumptions needed to be tractable.**

## ***Assessing adequacy: Three methods (cont.)***

**3. Can household finance predicted consumption path during retirement, given its resources?**  
(Hurd and Rohwedder, 2012)

- ***Predict consumption path from beginning of retirement to end of life***
- ***Calculate economic resources necessary to finance that consumption path***
- ***Compare with actual resources at household level***
- ***Account for uncertainty through simulation.***

# *Rich Data from the Health & Retirement Study*

- Representative sample of U.S. population age 51+
- Follows households over time: core survey every two years
- Refreshes with new group age 51 to 56 every six years
- Complete inventory of household economic resources
- Household spending → spending paths over time
- Sample of 65-69 year-olds at respective baseline
- Survey years used: 2000 – 2008, plus checked effects of recession years

## *Simulations account for*

- Returns to scale in spending, and widowling
- Spending paths decline with age, consistent with theory and empirical observation
- Future earnings
- Housing wealth
- Taxes
- Mortality risk and differential mortality
- Risk of out-of-pocket medical expenditures
- Heterogeneity by marital status, sex and education taken into account throughout

# *Individual-level Metric with Respect to Wealth*

## Ask:

What are the chances that individuals will die with positive wealth with high probability?

Allow for some margin of error so that small short-falls ok.

# Percent Adequately Prepared: 71%

Married persons better prepared, single females most vulnerable.

	Singles			Couples		
	All	Male	Female	All	Male	Female
Less than high-school	36.0	63.6	29.0	70.1	70.2	69.9
High-school	62.1	66.7	60.5	79.5	77.2	80.8
Some college	53.8	62.5	51.0	80.7	77.2	82.6
College and above	68.5	65.0	69.6	88.5	86.5	90.2
All	54.5	64.9	51.3	79.9	77.9	81.1

Source: Hurd and Rohwedder (2012)

# *One Important Threat to Economic Preparation*

## **Risk of large out-of-pocket (OOP) medical expenditures**

- Even though Medicare (including Part D) insures a large fraction of medical expenditure risk of those age 65+.

## *Some Statistics on Out-of-pocket Medical Expenses*

# *High SES individuals healthier, but spend more on health care.*

HRS 2014, individuals' out-of-pocket medical expenditures last 2 years, weighted, thousands of 2014 dollars

Wealth quartile	70-79 year olds		80-89 year olds	
	Mean	95th %ile	Mean	95th %ile
Lowest	2.7	9.9	2.4	9.2
2 <sup>nd</sup>	3.0	9.6	3.3	11.6
3 <sup>rd</sup>	3.6	10.6	3.4	11.7
Highest	3.9	12.5	4.4	16.1
Total	3.3	10.9	3.5	12.2

Source: Hudomiet, Hurd and Rohwedder (in progress)

# ***Relevant metric for financial planning: Remaining LIFETIME risk of OOP expenditures***

- HRS data
- cumulated OOP starting from age 70 until death
- adjusted for right-censoring
- weighted by baseline weight
- thousands of 2014 year dollars

# *Average financial lifetime exposure moderate, but non-trivial risk of very large OOP*

HRS data, cumulated OOP starting from age 70 until death, adjusted for right-censoring, weighted by baseline weight, thousands of 2014 year dollars

Wealth quartile at age 70	Mean wealth in quartile	Lifetime OOP	
		Mean	95th %ile
Lowest	21.7	40.8	147.2
2 <sup>nd</sup>	147.8	54.0	182.4
3 <sup>rd</sup>	391.6	61.7	208.0
Highest	1,724.5	66.6	214.0
Total	596.9	56.1	191.1

# ***Largest uninsured risk among elderly: Nursing home***

- Medicare only pays for nursing home stays following hospital admission and only up to 100 days, large co-pays after 21 days.
- Annual cost of nursing home stay: about \$84k
- Medicaid pays if household depletes financial resources  
→ well-to-do will pay substantially more

# Mostly large OOP spending on Nursing Home

But cannot spend more than resources available.  
Medicaid will step in if resources depleted.

Wealth quartile at age 70	Lifetime OOP mean	Lifetime NH nights mean	Lifetime OOP, NH mean	Lifetime OOP, NH 95th %ile
Lowest	40.8	312.7	17.5	102.5
2 <sup>nd</sup>	54.0	272.7	21.3	117.5
3 <sup>rd</sup>	61.7	293.2	22.3	131.1
Highest	66.6	261.7	22.3	112.1
Total	56.1	284.6	20.9	117.5

Source: Hudomiet, Hurd and Rohwedder (in progress)

# *Nursing Home stay often due to dementia*

- High SES similar LIFETIME likelihood of dementia
- survive longer and dementia risk doubles every 5 years after age 70

Wealth quartile, age 70	Years alive after age 70	Prob ever dement	Lifetime NH nights	
			Never dement	Ever dement
Lowest	11.7	0.40	116	564
2 <sup>nd</sup>	13.6	0.40	81	524
3 <sup>rd</sup>	14.2	0.41	90	545
Highest	15.1	0.38	89	514
Total	13.7	0.40	94	537

# ***Future Trends in OOP Med Expenditures: depends critically on trends in dementia***

- **Will longevity increases continue?**
  - Most recent cohorts in HRS have worse health; implications for mortality?
- **Trends in mortality and trends in dementia interact (competing risk)**
- Some recent studies have found declines in age-adjusted rates of dementia (Europe and U.S. Framingham)
- **Need to study future trends for U.S.**
  - Any trend—up or down—will have huge impact on long-term care costs.

# ***Research Needs to Make Further Progress***

- **To estimate lifetime risk longitudinal data like HRS must continue to follow cohorts over time AND**
  - **careful follow-up (albeit costly) determines reliability of results**
  - **Maintain sample size (if not increase)**
  - **Data innovations to incorporate new methods**  
(like Harmonized Cognitive Assessment Protocols that's under way)
- **Assessments of financial security need high-quality, detailed measures of economic behavior and economic status.**  
**Including spending data.**

***Thank you!***

**... and to my co-authors**

**Péter Hudomiet**

**and**

**Michael Hurd**

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# The Changing Nature of Employment Arrangements and Potential Implications for Retirement Security

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Susan Houseman

Upjohn Institute for Employment Research

Presentation prepared for the Financial Security Research Symposium, U.S. Treasury Department, Washington, D.C., September 7, 2016

# Overview

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- **Emerging forms of employment and what is known about**
  - Growth
  - Reasons for growth
  - Implications for retirement security
- **What is not known and the need for better data to document implications for retirement security**

# Changing nature of employment arrangements

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Many terms used to express new/growing forms of “nontraditional” employment arrangements

- e.g., nonstandard, alternative, contingent, gig arrangements, fissured employment
- No consistent terminology

Important types:

- Contract company workers—firms outsource or subcontract work to companies that hire employees; some are contingent (e.g., agency temps), some work at client’s worksite
- Independent contractors—firms outsource or subcontract work to individuals, who are self-employed. May or may not be contingent/gig workers, small subset acquire work through websites, mobile apps (e.g., Upwork, Uber)
- Flexible scheduling—Employees typically work part-time; schedule varies from week to week, some are “on-call”

# Evidence of growth

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- Evidence is piecemeal and some measures biased
- **Recent Rand American Life panel survey (Katz & Krueger 2016) suggests substantial growth over last decade in several categories:**
  - Independent contractors, contract company workers, agency temps, on-call workers—combined 4 to 5 percentage point increase
  - 16% self-identify in these categories, likely an underestimate
- **Large growth in number of 1099s – suggests growth of independent contractors**
- **Growth in sectors providing contract services, e.g.**
  - Business services, Logistics
- **Growth certain arrangements enabled by new technologies**
  - Flexible scheduling practices—now common in retail & hospitality
  - On-demand “gig” work enabled by mobile apps (e.g. Uber, Lyft) & web-based micro jobs (e.g. Mechanical Turk, Upwork)

# Reasons for growth

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- **Changes in business strategies dating back to 1980s**
  - Focus on core competencies, high value-added components of business
  - Vertical disintegration of firms, fissuring of workplace—partly in response to financial market pressures to increase short-term net revenue growth
  - Emphasis cost savings, including labor cost savings
  - Growth domestic (and foreign) outsourcing
- **Staffing flexibility—hire workers only when need them, increase productivity, lower costs**
- **Lower wage and benefits costs**
  - Some outsourcing motivated by savings on benefit costs
  - Trends coincide with shift from DB to DC retirement plans

# Implications for retirement security

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- **Likely some causal link between changing employment arrangements and decline in retirement security**
  - Workers in contract, other alternative arrangements often receive lower earnings, few if any benefits, less job stability—all factors that undermine retirement security
  - Wage inequality mostly explained by growth in inequality across firms (Bloom et al., 2016)—one hypothesis: related to growth in outsourcing
    - ▣ Likely similar relationship to inequality in benefits
  - Independent contractors are self-employed, can't receive employer-sponsored benefits
- **Some new forms of work may offer employment opportunities for older Americans, relieve financial pressures**

# Proposed reforms for workers in non-traditional employment arrangements

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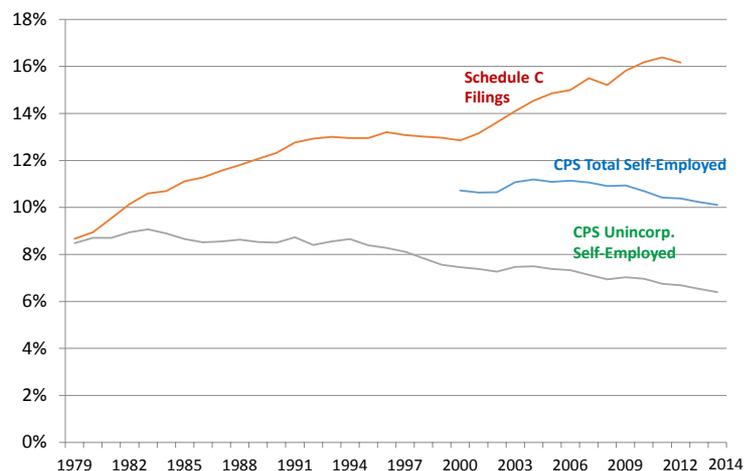
- **Principle of universality**
  - Cover workers who generally don't receive workplace retirement and other benefits—-independent contractors and part-time employees (Aspen Institute 2016)
  - Remove perverse incentives for employers to use alternative work arrangements to sidestep regulations governing benefits
  - Remove some barriers to utilizing flexible staffing arrangements
- **Benefits portability—move with the worker, not the job**
- **Contributions from employer or business/customer in case of independent contractors**
- **Experimentation at state or local level**
  - Proposed \$100 in state grants from DOL
  - Could involve exempting 3<sup>rd</sup> party payers from independent contractor misclassification suits.

# Data issues

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- **Official statistics for most part not designed to capture emerging forms of work**
- **Consensus on need to revamp surveys**
  - Impetus for new data initiatives (e.g., CPS Supplement on Contingent and Alternative Work Arrangements, module on Annual Survey of Entrepreneurs)
  - But many holes remain
- **Evidence indicates information on work arrangements that is collected often inaccurate (especially from household surveys)**

## Disturbing divergence between IRS and CPS data on self-employment (Katz and Krueger 2016)



- Abraham et al. (2016) confirm problem in linked CPS Annual Social and Economic Supplement and IRS data: 65% of self-employed in IRS data do not report themselves as self-employed in CPS ASE; 51% who do report themselves as self-employed in CPS are not self-employed in IRS data.
- CPS similarly missed growth temporary help employment in 1990s
- Undercount of temporary help, self-employment in CPS & CWS raises concerns about accuracy of figures on other employment arrangements

# Need for better data

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- **To understand implications of changing nature of employment relationships will require better data**
  - Characteristics of workers in these arrangements and savings behavior
  - Career paths of workers in these arrangements—whether employment in certain arrangements transitory or long-lasting
- **Developing better data will require**
  - Revamping existing surveys
  - Use of administrative data, linking to survey data

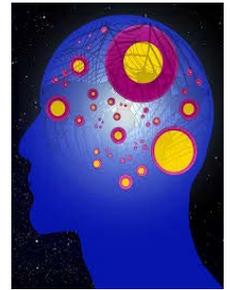
# Time Discounting & Economic Decision-making in the Older Population



MRRC Financial Security Research Symposium  
U.S. Department of the Treasury  
Sept. 2016

© David Huffman, Raimond Maurer,  
& Olivia S. Mitchell

# Motivation:



- ✓ Much research on inter-temporal decision-making for prime-age/youth; little on older adults.
- ✓ Yet older folks make many key decisions with major LR impacts:
  - Save/spend
  - Claim/defer Soc Sec
  - Exercise/health care/insurance
  - LTC/annuity, sell home, etc.
- ✓ Our goal: investigate impatience among the elderly & link to observed behavior.

# Our Study:

- Exp'tl module (*HRS 2014*) to evaluate levels & heterogeneity in time discounting;
- Age 70+ sample (& compare to younger people);
- Correlate impatience with other SES information on respondents;
- Link economic & health behavior with time discounting.

N=591



# Module Q's:



- Suppose you were given the choice between receiving a payment today or a payment in 12 months. We will now present to you 5 situations. The payment today is the same in each of these situations. The payment in 12 months differs in every situation. For each of these situations, we would like to know which you would choose.

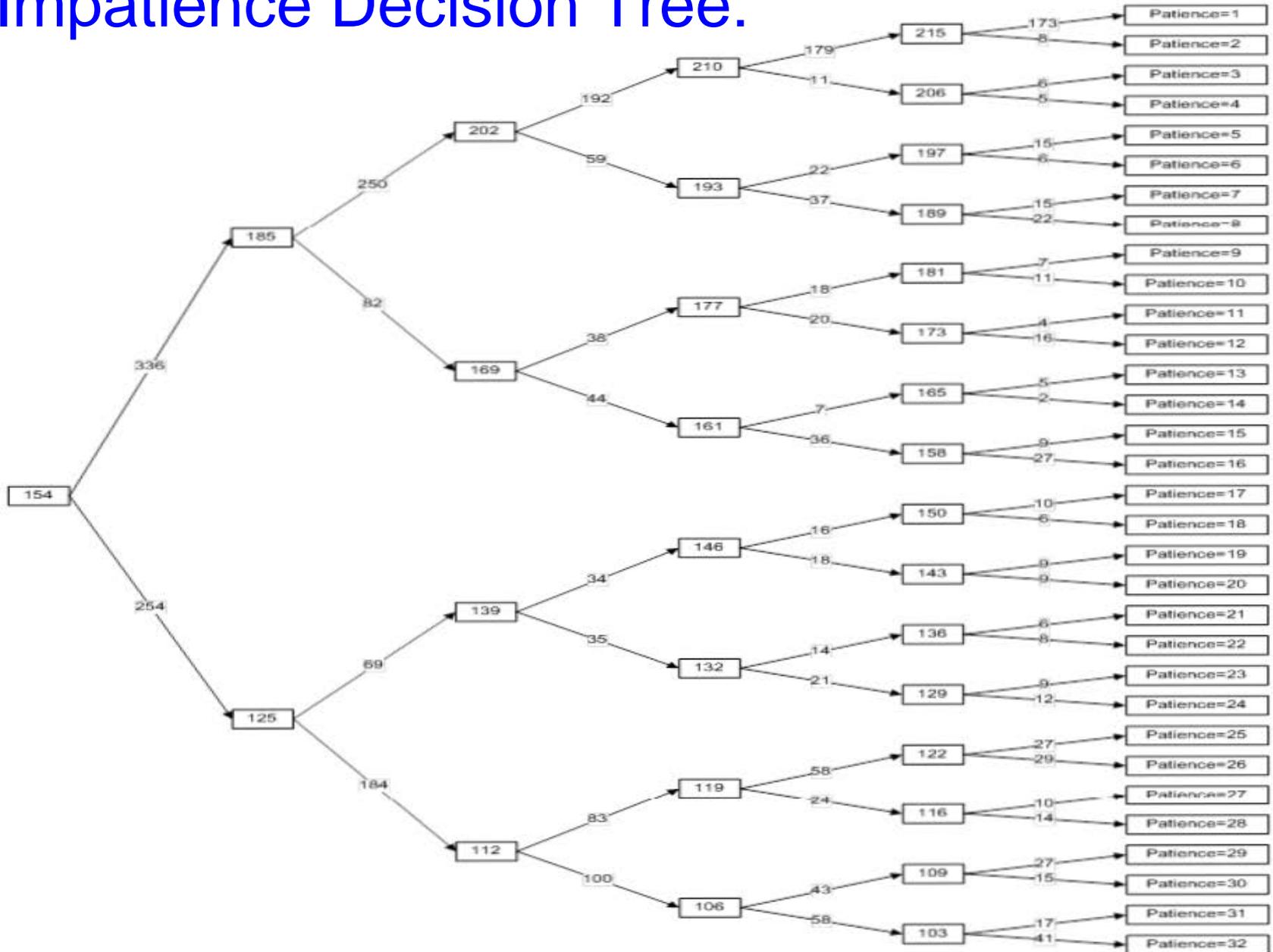
Would you rather receive \$100 today or \$154 in 12 months?

1. Today → *go to [step up]* → \$100 today or \$185 in 12 mos ... And so forth

2. In 12 mos → *go to [step down]* → \$100 today or \$125 in 12 mos ... And so forth

# Impatience Decision Tree:

Least patient



Most patient

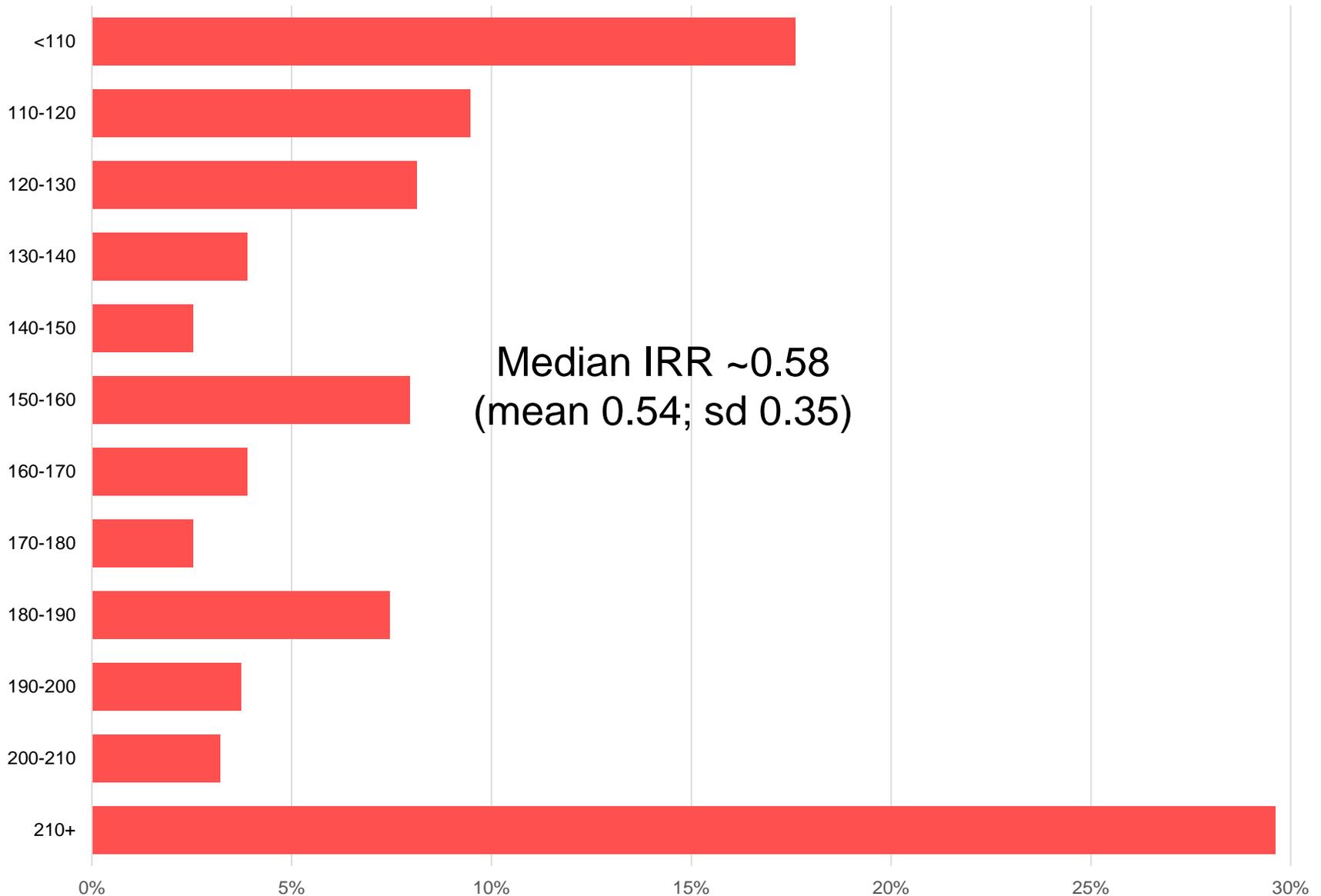
Convert to IRR (the interest rate setting NPV  
future money = money amount today):

- Take a respondent with patience score of 25:  
so  $\$125 \geq \$Z \geq \$122$ .
- This bounds  $\$Z$ : at least \$122, at most \$125.
- Solve for IRR s.t.  $(1+\text{IRR}) * \$100 = \$Z$   
 $\rightarrow \text{IRR} = [\$X / \$100] - 1$

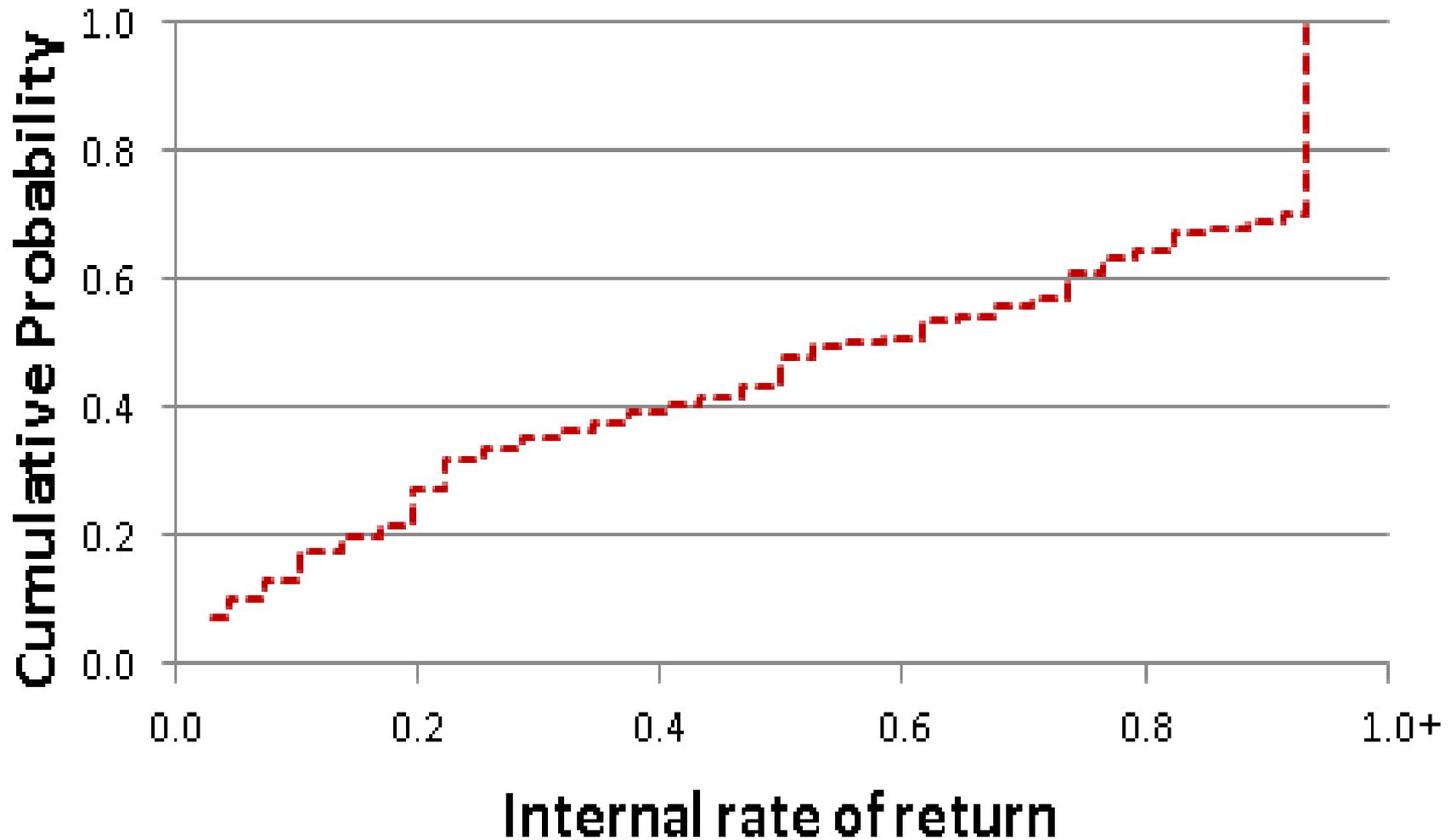
$\rightarrow$  Do for upper & lower bounds and average.

*\*If compound twice/yr  $\text{IRR} = 2 * [ [(\$X / \$100) ^ (.5)] - 1 ]$*

# Amounts Americans age 70+ would take in a year instead of \$100 now



# Cumulative Distribution of IRRs for Older Americans



# Heterogeneity

- +15-years of age 70 -85 associated w/ a standard deviation higher IRR.
- Whites & more educated have lower IRRs (-0.9 and -0.01)
- Serious health problems & dementia associated with much higher IRRs.
- *Not significant:* sex, marital, optimistic life expectancy, risk aversion, procrastinator, income, religion, Nkids



# IRR and economic outcomes:

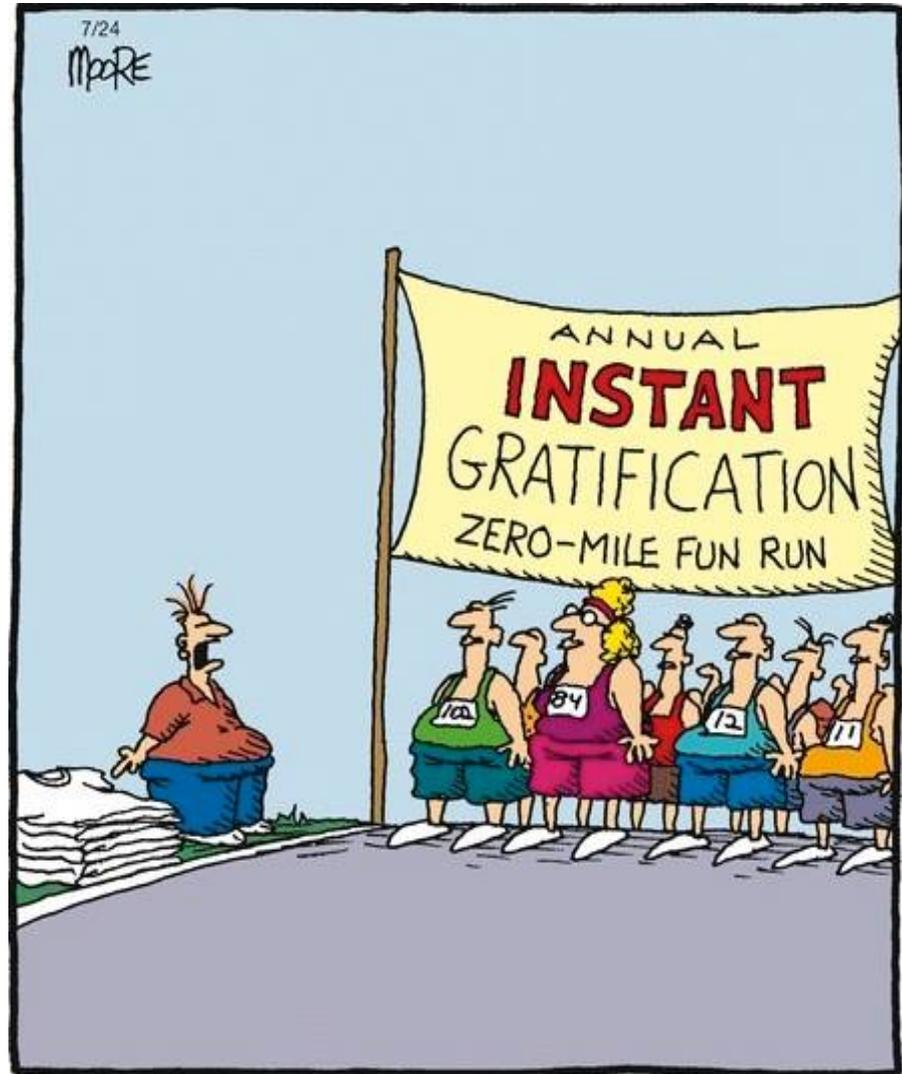
- ✓ Those with higher IRR have significantly **less total wealth and less financial wealth**
  - (1 sd higher IRR or +0.35 → 69% less).
- ✓ High IRR signif'ly **less healthy** (BMI + rel to IRR)
- ✓ High IRR do much **less end of life planning** (living will, will, talk to atty, etc)
- ✓ No link between IRR and Social Security claiming age, or retirement planning.

# Conclusions & Implications

- Reversing present bias could result in more retirement wealth & better economic security.
  - Challenge: how to do this?
- Unlikely to have much direct impact on claiming, and need larger sample sizes to evaluate insurance results.

Thank you!

[www.pensionresearchcouncil.org/](http://www.pensionresearchcouncil.org/)



“Runners to your mark. Get set. Go! ... OK, come get your T-shirts.”