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Should Undersaved Americans Work Longer?

By Teresa Ghilarducci *Thu, Jan 22, 2015*

Alicia Munnell, the nation's leading retirement policy economist, and colleagues (Charles D. Ellis, a financial planner and Andrew Eschtruth, a research economist) at the Center for Retirement Research at Boston College, which Munnell directs, have written an elegant, short, and nearly definitive book on the retirement crisis facing Americans today.

Their ambitious goals are to describe the problem of retirement unpreparedness, to explain how we reached this crisis, and to suggest ways for individuals and the government to solve it. They mostly succeed—but after delivering sharp, accurate blows to the system's weaknesses, I think they misfire on some of the policy recommendations.

For instance, they encourage workers to keep working into their late 60s and 70s and call for government action to raise the Social Security early retirement age from 62 to 64. This set of policy recommendations ignores three major facts: involuntary retirement, inadequate labor demand, and older workers' falling bargaining power.

Involuntary retirement is a very real phenomenon. First, most workers retire before they want to. They are fired or laid off or have to quit because of poor health. Second, the labor market doesn't fully employ prime age adults. Third, the incidence of long-term unemployment increasingly singles out older workers, who are also losing pensions. These latter two facts together weaken the bargaining power of older workers, and create conditions for low-quality jobs and low wages. Ultimately, these low-quality, low-wage jobs hasten death and worsen inequality in rates of illness, injury and reduced longevity.

The challenge and its solutions

The problem, as Munnell, Ellis and Eschtruth describe it, is that the financial crisis, along with the erosion of traditional pensions, rising Medicare premium costs, and the slow decline in Social Security benefits (as a share of career average preretirement earnings) placed half of near-retirees (over age 55) in 2013 at high risk of having inadequate old-age income. "Inadequate," in this case, is defined as having too little savings to generate an income that replaces 70% of their annual pre-retirement earnings.

They go on to explain, accurately, that the biggest cause for retirement unpreparedness is the drop-off in employer-based sources of retirement income. Less than half of employers offer a 401(k) or any other type of tax-deferred savings plan. The workers near retirement who are lucky enough to have 401(k)s and IRAs have saved a median amount of just $111,000 (2013), which would yield only about $400 per month.

While I agree with these authors on the problem and its causes, I agree with only some of their solutions. Munnell, Ellis, and Eschtruth recommend shoring up Social Security by using general revenues instead of payroll taxes. Given the lack of retirement readiness, they say that we should fix the Social Security deficit by raising revenues progressively, not by cutting benefits. They also want all 401(k) plans to use auto-enrollment (though studies show that firms adopting auto-enrollment tend to reduce contributions). The authors recommend improving the tax expenditures for retirement plans by replacing the current deduction for retirement saving with a credit. Those recommendations make a lot of sense.

But the authors also want the early retirement age to increase from 62 to 64, and, as I said earlier, I don't agree with that. They call for the government to “vigorously promote work at older age” because even a part time, minimum wage job yielding $800 per month is likely to prevent severely low incomes. You might advise a healthy working older person to work longer if he or she doesn’t have a pension; but advice to individuals doesn't necessarily serve as good public policy. Working longer may solve the retirement income problem for some people, but promoting new ways to save for retirement will have a much broader impact.

A lack of bargaining power

Tens of millions of older workers will have an average real annual Social Security benefit of only $15,000 per year and an income of just $2,400 from IRAs and 401(k) plans—amounts that barely meet the federal poverty standard (a standard that ensures a chronic state of want and deprivation). Because having low retirement benefits weakens older workers’ bargaining power, they will find it more difficult to quit a job or garner decent pay or working conditions. Increasing numbers of older people will have to take low wage jobs with poorer working conditions than they want.

I’m not against the idea of older people working. Some people derive their identities from their jobs and welcome the society and structure of paid work. Laudably, the United States is among the few rich countries that ban mandatory retirement. But policies that promote work should be paired with public policies that protect older workers. Raising the minimum wage, extending the protections in the Americans with Disabilities Act (I credit Sara Rix at the AARP for her efforts in that direction), and pro-union policies in service and retail jobs would all help older workers

I also worry that the authors have not acknowledged the growing inequality of mortality. Brookings Institution economists Barry Bosworth and Kathleen Burke have confirmed Social Security economist Hilary Waldron’s findings that class-based longevity gaps are growing.

The average life expectancy today for 55-year-old men in the lowest income decile is 79.2 years. For those in the top decile (both men and women), it is 89.3 years. Men in the bottom decile who were born in 1920 can expect to collect benefits for 16.6 years, while men in the top 10% are expected to collect for 20.7 years.

For men born in 1940, the gap is even greater. Those near the bottom of the income spectrum will collect benefits for 18.2 years, on average; those at the top for 26.4 years. Cutting benefits for those who now retire before age 64 would disproportionately adversely affect those with shorter life spans.

A valuable book

That said, I think *Falling Short* is an important book. It succinctly identifies the retirement readiness crisis, pinpoints its causes and suggests comprehensive and imaginative solutions. (I read it in just two sittings.) The writing reflects Munnell’s, pithy, inimitable style, as in sequences like this on page 16: “That’s it: work longer, fix Social Security, save more through 401(k)s, and consider using home equity. These steps are all doable, and they should all seem familiar.”

And I agree with many of the authors’ positions: that most people need prearranged savings mechanisms in order to save successfully; that retirees need both longevity insurance and private savings; and that if we are going to give out over $120 billion in tax incentives for retirement savings, the 401(k) system has to work better.

In the next-to-last sentence of the book, the authors mention that incremental change may not solve America’s retirement crisis. I agree with that too, but instead of raising the retirement age, I recommend (in my books and academic papers) increasing private wealth through a system of universal retirement savings accounts—guaranteed, privately managed, cash balance-type accounts on top of Social Security.

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