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The Demand for and Supply of Phased Retirement Programs: Opportunities and Barriers

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Abstract:

Phased retirement offers many benefits to employees who wish to maintain a steady income stream later in life and to employers who want to retain their experienced workforce, yet few employers offer formal programs as a variety of barriers hinder widespread implementation. These barriers include regulatory complexities and ambiguities involving federal tax and age discrimination laws. Thus, employers are tasked with overcoming significant barriers to facilitating a phased transition into retirement for their workers. In this report, we addresses the various challenges related to phased retirement from the employee, employer, and legal perspective. Further, we discuss employee interest in working past the traditional retirement age by using 2014 Health and Retirement Study (HRS) data.

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Introduction

Recent retirement trends illustrate that the average American is living and working longer. With greater life expectancy, many individuals choose to delay retirement to maintain a working lifestyle, and a significant share report that they delay retirement because of financial needs. Moreover, the aging U.S. baby boom generation and long-term demographic trends are expected to permanently shift the population's age distribution. In an aging nation, traditional welfare systems are forced to change to adapt to the greater retirement risks faced by individuals, and this is where phased retirement comes in as a solution. Currently, there is no formal legal definition of phased retirement. In 2000, the Advisory Council on Employee Welfare and Pension Plans proposed its legal definition [to the Secretary of Labor]: "a gradual change in a person's work arrangements as a transition toward full retirement, which may involve a change of employers (including self-employment), a career change or a reduction in the number of hours worked." Regardless of the lack of a formal legal definition, more workers between full-time status and complete retirement are choosing partial retirement and are staying longer in that partial retirement state. From 1960 to 2010, the incidence of partial retirement increased from nearly zero to more than 15% for 60–62-year-old workers, while partial retirement among 65–67-year-old workers went from 5% to 10% to almost 20% (Gorodnichenko et al. 2013). According to the 2014 HRS data 40% of 59–64-year-olds are expecting to work past 65 and 33% among this age cohort is likely to work full-time beyond 65. Moreover, as recent generations of retirees are less financially prepared for retirement relative to earlier cohorts (Lusardi, Mitchell, and Oggero 2017a; Lusardi, Mitchell, and Oggero 2018b), more older workers are shifting into self-employment and engaging in entrepreneurial activities later in life (Lusardi, Christelis, and de Bassa Scheresberg 2016).

Employee Demand

From 1970 until 2016, the number of years in retirement increased from 10.4 to 17.2 for men and from 15 to 20.6 for women in the U.S. (OECD 2018). Increased life expectancy and the accompanying longevity risk—the risk of running out of wealth during one's retirement—are among the most commonly cited reasons for the need to work longer in a phased retirement program. Today, non-retired Americans, on average, say they will retire at around age 66 (2014 HRS). Furthermore, in the 2014 HRS[1], 57% of the 65–69-year-olds consider themselves as fully retired, 18% consider their work status as partly retired, and 23% consider themselves as not retired.[2] Along with the rise in working years is the rise in life expectancy:

[1] The Health and Retirement Study (HRS) is an extensive nationally representative longitudinal panel survey on the aging population of the U.S. that started in 1992 at the University of Michigan's Institute for Social Research. It is sponsored by the National Institute on Aging and the Social Security Administration. The study surveys a representative sample of approximately 20,000 Americans of age 50 and older and has conducted 12 waves every two years, from 1992 to 2014. Interviews are conducted every two years, and new interviewees are added in cohorts every six years. Its extensive questionnaire includes information about income and wealth, health, employment, family connections, and biosocial and psychosocial characteristics of individuals to provide social scientists, policy-makers and the like with the most comprehensive study on the retired and soon to retire population. New questions have been added at the beginning of almost every study. For this study we used the 2014 HRS wave.

[2] The percentages add up to only 98% because for the remaining 2% of respondents the question was irrelevant due to their labor force status.

average life expectancy after age 65 has risen from 14 years in 1950 to 19 years in 2013 (U.S. Department of Health and Human Services, 2015). Since life expectancy keeps rising, recent retiree cohorts (ages 62–65) and pre-retirement cohorts (ages 56–61) have taken on more debt and faced more financial insecurity compared to their predecessor cohorts. The percentage of people age 56–61 approaching retirement with debt rose from 64 percent among those observed in 1992 to 71 percent among the Elderly Boomers in 2010. Moreover, the median debt for these cohorts quintupled from $6,800 in 1992 to $32,700 in 2010 (Lusardi, Mitchell, and Oggero 2018). Furthermore, Munnell et al. (2006) has revealed that the share of households at risk of running out of wealth rose from 35% for the Early Boomers to 44% for the Late Boomers and to 49% for Generation X.

For individuals who find themselves without adequate savings to sustain a full retirement, working longer may be the only path to financial stability. Higher wealth is generally positively associated with leaving the workforce, however, individuals with higher education are likely to work longer and phase into retirement through, for example, part-time consultancy arrangements. Findings from the 2014 HRS data show that near-retirees (59-64-year-olds) who expect to retire beyond 65 have on average lower household net wealth[3] compared to those who do not expect to work longer. The same holds true if we look at 59-64-year-olds who think that they will be working full-time beyond age 65 with a probability of 50% and higher.[4] Their average household net wealth is around $561,000, which is lower compared to $575,000 for those with a probability below 50%. Interestingly, the data show that the self-reported probability of working full-time beyond 65 stays relatively high over all household net wealth levels. Looking at the debt side, we see a link between the total mortgage debt amount that older individuals between ages 65-69 hold and their self-reported retirement status (either fully retired, partly retired, or not retired at all). Those considering themselves as fully retired owe an average total amount of $37,308. However, those who were partly retired have an average amount of $51,559 in mortgage debt, and those considering themselves as not retired owe $61,230. Thus, increasing long-term debt is associated with working longer. Further research needs to be done to analyze the underlying factors and dynamics of wealth accumulation and retirement planning.

Additionally, individuals near retirement who are likely to work full-time after age 65 (with a probability of 50% and higher) have an average annual income of $52,000 compared to $21,000 for those who are less likely to work full-time beyond 65. This higher income is in line with the higher educational attainment of workers who are more likely to work longer. Moreover, those with the higher probability of working beyond 65 are much more likely to be working full-time, i.e., 78% of 59-64-year-olds currently work full-time compared to 23% among those 59-64-year-olds who are less likely to work longer, and also have a spouse who works full-time or part-time. For near-retirees likely to work longer full-time, 63% have a spouse who works either full-time or part-time. This is in contrast to 44% among those less likely to work

[3] The net value of total wealth is calculated as the sum of all wealth components including second homes less debt.
[4] For the age cohort of 59-64-year-olds (near-retirees) we report statistics for two slightly different questions. First, we look at the group who expects to retire beyond 65 and compare them those who expect to retire before or at 65. Second, we group together those near-retirees who report a probability of 50% and higher for working full-time beyond age 65 and compare them to the group of near-retirees who report a probability of less than 50%.

after age 65 (with a probability of less than 50%). Thus, in line with other research, we find that respondents work longer (both full-time and part-time) when their spouses are working either full-time or part-time. Findings from the current work status of older individuals between ages 65-69 reflect the same dependencies. When looking at the age cohort of 65-69, 47% of those who consider themselves as currently not retired have a spouse who works either full-time or part-time. Among those of age 65-69 who consider themselves fully retired, only 18% have a spouse working full-time or part-time, but 66% were living with a fully-retired spouse. Thus, if the spouse is retired, the likelihood of the respondent being completely retired at ages 65-69 increases significantly.

The decision to work longer is also based on several personal characteristics, such as educational attainment, skills, income levels, health, and family size. Those with specialized skills present specific incentives for employers and are often retained as consultants or mentors to train newer employees. The HRS data show that in 2014 42% of the 59-64-year-olds who will likely work full-time beyond 65 have a college degree or above and 29% attended some college but did not earn a degree. In contrast, among this subgroup, 24% have a high-school or General Education Degree (GED) and only 5% attended some high-school but did not finish it. These numbers are different from the subsample of near-retirees who will not likely work longer, 31% hold a college degree or above, 29% have a high-school or GED degree, and 11% did not finish high-school. Thus, those who are likely to work longer have a higher education, which is in line with research showing that employers tend to offer phased retirement options to highly skilled workers (Hill, 2010). When we look at the age cohort of 65-69-year-olds, we find similar results. 44% of the 65-69-year-olds who consider themselves as not retired have a college degree or above. In contrast, among those who self-report to be fully retired at age 65-69, only 25% hold a college degree or above, but 34% hold a high-school degree or GED and 13% dropped out of high school.

Another study found that those with a higher number of financially dependent children are more likely to look for ways to continue providing for their children, and thus explore ways to delay retirement (Reitzes et. al. 1998). In the 2014 HRS data we do not find a significant difference in household size and number of children living in the same household among the near-retirees who expect to work beyond 65 compared to those who do not expect to work past 65. The average number of children living in the same household is around 2.3 for those planning to work past 65. When looking at the older age cohort of 65-69-year-olds we see again that there are no significant differences between those who consider themselves as fully retired, partly retired, and not retired in terms of marital status, number of children, and household size.

Moreover, higher life expectancy and rising healthcare costs increase the need for health benefits in retirement, which serves as an additional factor for employees to consider when deciding about working longer and in what capacity. The 2014 HRS data show that the self-reported health status has a major effect on workers' likelihood of working longer. We also find that if the spouses have health issues that interfered with their own ability to work, the survey respondents are more likely to work longer full-time. 19% of the 59-64-year-old respondents expect to work full-time past 65 when their spouses have health problems that limit their own ability to work. This figure is 17% for the near-retirees that do not expect to work longer. This also holds true when we look at the older age cohort of 65-69-year-olds and their selfassessed retirement status. Among those who consider themselves as partly retired or not retired, 71% and 75%, respectively, have a spouse with health problems. This percentage is at 66% for 65-69-year-olds who assess their retirement status as fully retired.

Furthermore, in line with other research using previous HRS waves, we see that both men and women in the age group of 59-64 are equally likely to expect to work longer. Interestingly, when focusing on the age cohort of 65-69-year-olds, we find that a higher percentage of women considered themselves as not retired compared to men, i.e., 53% and 47% respectively. Overall, analyzing the link between labor force, health status of the spouse, and retirement decision-making of the respondent clearly shows that spouses have a considerable influence on each other's decision for working longer. Also, work enables people to feel mentally stimulated and challenged, while offering a social support system (Stendardi 2005).

Employer Perspective

Facing a shrinking workforce as the U.S. population ages, employers across industries may need to respond to this trend by offering various forms of transitional retirement programs to attract and retain older workers. Several factors influence the options that employers can make available to their older workers who want to phase into retirement.

Phased retirement options can benefit employers that face potential labor shortfalls as the number of younger people joining the workforce fails to compensate for the number of Baby Boomers reaching retirement age (Stendardi, Edward J. 2005). Moreover, employers that expect rapid company growth, and thus need to attract and retain more workers, are far more likely to create phased retirement opportunities, formally or informally. Retaining older workers is linked to reduced hiring and training costs, and this linkage can result from phased retirement policies stipulating that those in the program spend at least 20% of their time mentoring new employees. Retention of skilled and trained employees serves as a major incentive for employers to offer phased retirement programs. As older employees' jobs get more complicated and as responsibilities increase with years of tenure, finding replacements with comparable work experience is difficult. Thus, employers depending on their workers' industry-specific experience and skills gained over the working years are more likely to provide phased retirement options (Sass et. al. 2009).

The list of challenges for employers wanting to implement phased retirement programs is led by legal issues that influence employer's decisions on the structure of the retirement benefits they provide (Hutchens and Grace-Martin 2006a; GAO 2017). Noncompliance with federal laws has serious consequences, including loss of an employer's tax qualification status. From an employer's perspective, health care coverage becomes one of the most crucial issues impacting phased retirement, as eligibility can involve minimum working-hour requirements and this has cost implications (GAO 2017). The legal barriers are discussed in detail in the second part of this report. Additional challenges relate to older workers being seen as costly due to reduced productivity, high salaries, and high health care costs. These challenges of reduced productivity are more common in industries such as mining, agriculture, construction, and manufacturing since the nature of the work is more manual labor-intensive, i.e., physically demanding. Thus, those companies might have higher incentives to provide early retirement options to those aging workers whose productivity levels have decreased, and to negotiate phased retirement options with certain workers with specific skills on a case-by-case basis.

Further, even if legal barriers were not an issue, employers might be reluctant to implement formal phased retirement plans because those programs do not suit their business model, job and organization structure, and company goals (Hill 2010). Jobs that require working with a team, that are manual labor-heavy, or that need intensive supervision are less suitable for phased retirement arrangements where employees work on a part-time schedule. Similarly, occupations which fit a relatively young workforce and do not typically offer part-time employment are likely to face challenges in implementing formal phased retirement programs. Moreover, workers who perform unskilled tasks are less likely to be offered phased retirement arrangements as their company could replace them with younger, less expensive workers. Thus, formal programs are mostly offered by employers with larger and more technical and professional workforces. Industries with workers that are hard to replace because of the need for a specific skill set or industries with labor shortages are more motivated to offer phased retirement programs (GAO 2017). In 2017, GAO released a study providing insights from a series of interviews with nine employers that use, will soon use, have thought of using, and do not want to use phased retirement programs. They identified consulting, education, and high-tech industries as the ones that are more willing to offer formal phased retirement programs. Another study conducted by the Society for Human Resource Management (2016) added to this list of industries government and utilities. In contrast, the industries that are the least likely to offer formal phased retirement programs are real estate, rental leasing, and retail (SHRM 2016). Lastly, employees covered by unions are the least likely to receive the option of phased retirement because of the often informal and customized nature of this arrangement as opposed to the preference of unions for rigid contract-like terms (Hutchens and Grace-Martin 2006b). This shows that for certain industries a holistic legal approach for phased retirement programs to ease employers' barriers is not likely to be feasible since different businesses have very different structures.

It is important to note the distinction between formal and informal phased retirement programs and the way in which so-called "ad-hoc programs" are implemented. The informal program refers to an "arrangement in which a worker remains with the same employer but eases into retirement through an informal channel rather than a structured program" (GAO 2017), i.e. as retirement gets closer, full-time workers switch to part-time status without any formal policy implementation. The formal program is a "formal, employer-based program in which older workers can reduce their working hours in order to transition into retirement" (GAO 2017), i.e., laws and regulations regarding health coverage, retirement benefits, and age discrimination have to be followed by the company and the employee. Another critical aspect of this distinction is the meaning of "ad-hoc programs." The term is mostly used in reference to the informal programs and refers to rules that accommodate the process of phasing into retirement on a case-by-case basis (Hill 2010).

Legal Perspective

Despite the fact that an increasing number of employees demand phased retirement or options that enable them to work longer, the number of employers who provide such programs is relatively small. Additionally, informal phased retirement arrangements are more common than formal programs, and even for employers who do have formal programs, it is often flexible and customized to individual cases (AARP 2006). This is driven by the regulatory complexities and ambiguities involving federal tax and age discrimination laws. Moreover, different phased retirement programs raise different legal issues. Sheaks et al. (2006) describe two situations: In one situation, an employee fully retires and returns to work as a full-time employee, part-time employee, independent contractor, or consultant for either a previous or new employer. In another situation, an employee partially retires and works on a reduced work schedule with different access to benefit plans (either full, partial or no distribution). The legal issues vary depending on how individuals may access retirement funds to supplement their reduced income. In the following discussion, we will focus primarily on the second situation described above, in which an employee continues to work with the same private employer on a reduced schedule.

U.S. employers face an array of complex legal issues around the implementation of formal phased retirement programs, with some of the regulations significantly influencing workers' retirement income strategies and age. The most relevant laws are the Employment Retirement Income Security Act of 1974 (ERISA), the Internal Revenue Code (IRC or "Tax Code"), the Social Security Act, and the Age Discrimination in Employment Act of 1967 (ADEA). The ERISA and the IRC are two important federal laws that govern private employer benefit programs. The ERISA sets minimum standards to protect the rights of participants in and beneficiaries of private pension and health plans. The Internal Revenue Service (IRS) enforces the IRC under the ERISA Title II, which sets out requirements that plans must meet to benefit from federal income tax deferrals and deductions, and they include "nondiscrimination rules" that prohibit qualified plans from favoring highly compensated employees. ERISA and the IRC have been amended several times; a major amendment that can significantly impact participants' retirement income strategies is the Pension Protection Act (PPA) of 2006. Moreover, the U.S. Social Security program, created in 1935 and governed by the Social Security Act, provides the largest retirement income source in the U.S., comprising about 52% of household income in retirement (GAO 2017). This program therefore plays a major role in influencing workers' retirement age (Lumsdaine et al. 1996). Lastly, the Equal Employment Opportunity Commissions (EEOC) enforce the ADEA, which protects workers age 40 and older from age-related employment discrimination. These laws and regulations can be seen as barriers to the establishment of formal phased retirement programs.

Prior to the mid-1980s, retirement ages were decreasing. This trend was well-documented and was frequently attributed to a strong economy and high demand for labor. According to Burtless and Quinn (2002), average male retirement age fell from 74 in 1910 to 63 in 1983, and this was mainly due to workers' increased wealth in the form of higher home prices and generous Social Security and Medicare benefits. As a result, from 1983 to 1987, the retirement rate was 17% for 62-year-olds in the workforce and 14% for 65-year-olds in the workforce (Friedberg 2007). Furthermore, traditional defined benefit (DB) pensions, the most prevalent form of retirement plans in the U.S. until the mid-1980s, were often designed to provide substantial incentive for retirement before 65, the traditional full retirement age (FRA) and the age at which a worker is eligible to receive full Social Security benefits (Stock and Wise 1990).

However, several policy shifts have helped reverse this trend of retirement before age 65 and incentivize individuals to continue work until they reach their FRA, at least on a part-time basis. First, over the recent decades, private sector employers have shifted from providing DB plans to offering defined contribution (DC) plans[5] (Department of Labor 2018), which encouraged more workers to delay their retirement. This has been influenced by specific features of the two plan types and several policy changes. The benefit formula of DB plans factors in salary and years of service (i.e., last five years of wages or average of the workers' highest five years of wages). As a result, the increase in pension benefits resulting from continued work may not be sufficient to compensate workers for benefits foregone while continuing to work (Burtless and Quinn 2002). Additionally, a reduced schedule might reduce benefit payments for individuals whose benefits are set based on earnings during the years closest to retirement. Unlike DB plans, retirement benefit payments from DC plans depend on employee contributions made throughout their career. This means that continued work does not result in any reduction in benefit payments. In fact, wealth accrual patterns in DC plans are more age-neutral, and hence do not encourage early retirement (Johnson 2011). Furthermore, the Revenue Act of 1978 enabled both employers and employees to make tax-deferred contributions to 401(k) plans, the most common form of DC plans, which made them much less costly for employers than DB plans, which are subject to stronger funding requirements under the ERISA (Purcell and Staman 2008). Additionally, under the ERISA, employees who have completed 1,000 hours of service for 12 months consecutively can participate in any company pension or profit-sharing plans offered to other employees, and this can help phased retirees continue to save for retirement. Thus, providing retirement savings options for workers on a reduced work schedule may positively affect their decision about working until the normal retirement age (NRA).[6] Second, the Social Security Amendments of 1961 allowed workers to start claiming Social Security benefits beginning at age 62, known as the early retirement age (EEA), and the ability to claim benefits may be a significant factor in retiring no earlier than age 62 (Burtless and Quinn 2002). Thus, more people have started claiming benefits at age 62, while fewer people have waited to claiming at or after their FRA (Annual Statistical Supplement to the Social Security Bulletin). However, claiming between age 62 and the FRA results in permanently lower benefits, because it results in a longer period over which the same total benefit amount will be paid, which in turn might increase the age at which an individual decides to retire (Mitchell and Phillips 2000). Third, the PPA of 2006 allowed DB plans to make in-service distributions to participants without penalty at age 62 or at the

[5] From 1975 to 2015, number of defined benefit plans have more than halved from 103,000 to 46,000 while the number of defined contribution plans have more than tripled from 208,000 to 650,000 (Department of Labor 2018).

[6] Retirement plan's "normal retirement age (NRA)" is specified by each plan, and this may differ from Social Security Benefit's FRA (sometimes also called the NRA, but to avoid confusion, will use FRA). While a plan may choose an NRA to determine when a participant's benefits vest, ERISA requires that this age be (1) the earlier of the time a participant attains NRA or (2) the later of the time the participant attains age 65 or the fifth anniversary of the time the participant began participating in the plan (Purcell and Staman 2008).

plan's NRA, enabling participants to receive distributions without formally retiring. This allows workers to continue work (or phase into retirement) through the plan's NRA while supplementing their reduced wage with DB benefits during phased retirement. Fourth and finally, the share of large firms offering retiree health benefits to their pre-65 retirees has declined over the past two decades (Kaiser Family Foundation 2017; Johnson 2007). This decline is due to rising health care costs and the introduction of an accounting rule in 1993 which required that employers disclose health insurance plan offerings (Johnson 2011). This discourages workers from retiring before they become eligible for Medicare at 65, because individual health insurance plans are expensive (Nice et al. 2013). Overall, these policies, together with the economic recovery from the 2007-09 Great Recession, lead older individuals to stay longer in the workforce. As a result, the labor force participation rate of older men has grown since mid-1990s and more than two-thirds of men ages 60 to 64 are in the labor force today (Coile 2017).

But as Americans are living longer with improved health, several policies have supported their desires to stay in the workforce beyond the traditional FRA. First, the 1983 Social Security Amendments made Social Security benefits less generous (sufficiency of Social Security funds had become a policy concern) by gradually increasing the FRA from 65 for all workers to 67 by year of birth. Raising the FRA increased the number of people working past age 65 and up to age 70 as well as the labor force participation rate of workers even younger than 65 (Gustman and Steinmeier 2013; Pingle 2006). Second, the 1972 amendment to the Social Security Act instituted the Delayed Retirement Credit (DRC) for those claiming Social Security benefits after the FRA and up to age 70, to compensate for the shorter period of benefits received. The 1984 amendment increased the credit amount from 1 percent to 8 percent per year. This means that the maximum DRC for an individual whose FRA is set at 65 would be 40 percent (five years times 8 percent). Thus, by waiting to collect benefits until 70, one would receive a benefit worth 40 percent more than the amount received at 65. This change made the benefit receipt more actuarially fair, or age-neutral, and resulted in increased employment among workers over age 65 as shown by Pingle (2006). Third, the Senior Citizen's Freedom to Work Act 2000 eliminated the earnings test, which withheld partial Social Security benefits for workers between the FRA and age 70 who received distributions while working and simultaneously earned above a threshold amount. As a result of this change, individuals over age 65 receive the full benefit amount while working, regardless of how much they earn. Although the amount withheld was returned after one became fully retired, some researchers argued that the earnings limit could be a disincentive to working past the FRA. There is little agreement on its effect on labor supply as some have argued that the elimination of the earnings test increased the labor supply of older workers (Engelhardt and Kumar 2007; Haider and Loughran 2008), but others have argued that it had little meaningful effect on the labor supply decisions of men (Gruber and Orszag 2003). Fourth and finally, the legal mandatory retirement age, which was 70 until 1978, was outlawed in 1986 with an amendment to the ADEA. This not only increased retirement age options for older employees but also conveyed a message that "there is no single appropriate age at which to retire (Burtless and Quinn 2002)." Currently the EEA for Social Security benefits is 62, the eligibility age for in-service distribution is 62 for DB plans and 59.5 for most DC plans under the IRC. However, these ages have become outdated because of increased longevity, so raising the EEA for Social Security benefits and the eligibility age for in-service distribution for DB and DC plans along with the FRA would significantly impact workers' retirement decision (Burtless and Quinn 2002; Manoli and Weber 2016).

As our focus in this report is on facilitating the transition for workers past the FRA from full-time to part-time to retirement through implementation of formal phased retirement programs, we will discuss some major challenges for employers below.

Health

Even if employees want to phase into retirement up to or past age 65, some provisions on health plans under the ERISA Title I pose challenges for employers. Under the Consolidated Omnibus Budget Reconciliation Act (COBRA) of 1985, private sector employers with 20 or more employees are required to provide 18 months of continued health coverage to employees who either ended their employment (for reasons other than gross misconduct) or reduced their number of work hours. However, this coverage might not last until one reaches 65 if an individual retires too soon. Nevertheless, the Affordable Care Act (ACA) of 2010 required health insurance exchanges, online marketplaces where consumers can purchase individual coverage, to be established in all states and to offer multi-state exchanges starting in 2014. Although the ACA's impact on the cost of individual health insurance is subject to debate (Moffit and Meredith 2015), some have expected that it will reduce the cost substantially (Blumberg 2011) and will provide a possible solution to fill the gap in health coverage between the end of COBRA and the start of Medicare. Moreover, for phased retirees older than 65 working at companies with more than 20 employees, the Medicare Secondary Payer Act of 1980 made Medicare a secondary payer, requiring it cover only the costs the employer does not cover. As employers are not required by federal law to provide health insurance for part-time employees,[7] they may be reluctant to cover high health care costs of part-time older workers. Furthermore, as many employers do not provide health benefits to part-time employees, making exceptions for older workers could violate age discrimination rules.

Age Discrimination

ADEA forbids employers with at least 20 employees to discriminate against workers over age 40 with employment opportunities based on age. The ADEA applies to all the terms, conditions, or privileges of employment, including hiring, firing, promotion, lay-off, compensation, benefits, job assignments, and training. Workplace Flexibility (2010) discusses a number of cases in which the ADEA can adversely impact employers from establishing a formal phased retirement program. Employers may choose to provide phased retirement only to employees with desired skills, but doing so may expose the employer to ADEA claims, if it denies enrollment to relatively older employees. But employers can refute ADEA claims by showing legitimate and nondiscriminatory reasons—such as skills and performance—for their decisions.

[7] The Fair Labor Standards Act (FLSA) has no definition for part-time or full-time employment, and employers may determine their own definitions. A minimum of 20 hours per week is common although it may vary depending on federal laws or individual state law. The U.S. Department of Labor uses a definition of 34 or fewer hours a week; the Affordable Care Act uses a definition of less than 30 hours per week.

Although ADEA protects workers age 40 or older, employers who offer phased retirement only to workers in their 50s or 60s may be exposed to ADEA claims for discriminating against workers in their 40s. The 2007 amendment clarified that the law only prohibits discrimination based on old age, and does not prohibit employers from favoring any relatively older worker above 40, thus protecting employers from ADEA claims (ADEA Final Rule 2007). Generally, the current law makes it difficult for employees to successfully prove that formal phased retirement programs violate the ADEA (Workplace Flexibility 2010). But ADEA is ambiguous compared to the IRC and ERISA, and court cases rather than provisions typically have shaped the evolution of the ADEA (Penner et al 2002). Moreover, even if employers prevail, legal exposure is expensive and this can discourage employers from providing phased retirement programs, no matter how small the risk (Johnson 2011).

Antidiscrimination (Tax)

The Revenue Act of 1942 tightened the requirement under which employer-sponsored pension plans must meet the IRC provisions under the ERISA Title II for receiving federal income tax advantages. The IRC requires that tax-qualified plans not favor highly compensated employees (HCE) at the expense of non-highly compensated employees (NHCE) with regard to coverage, benefit amount, or benefit availability. The IRC defines an HCE as an employee who owns 5% or more of the company or whose compensation in 2018 exceeds $120,000.[8] Through subsequent amendments to the IRC, these rules have been changed to become more uniform and standardized. One of the tax code's nondiscrimination tests stipulates that a qualified plan must either benefit at least 70 percent of NHCEs, or benefit a share of NHCEs that is at least 70 percent of HCEs benefitting under the plan, or to ensure that the average benefit percentage[9] of NHCEs is at least 70 percent of the average benefit percentage of HCEs. However, these tests can discourage employers from implementing formal phased retirement programs because a lot of employers do so in order to retain highly skilled and experienced workers, who are usually highly compensated workers. Penner et al. (2002) proposed defining a "safe harbor" in the statute, permitting employers to exempt phased retirees when testing their plans for nondiscrimination. An alternative option is to relax the 70 percent rule, but this may reduce NHCE's access to phased retirement (Johnson 2011).

Others

Most DB plans are insured by the Pension Benefit Guaranty Corporation (PBGC), which was created as part of the ERISA, assuring employees that their retirement benefits are guaranteed. However, DC plans are not insured by the PBGC, and this puts more investment risk on employees because they are not protected from the possibility that an employer might terminate a plan. This risk will make employees reluctant to hold DC accounts for fear of losing retirement funds, which will in turn deter the transition to more age-neutral DC plans, thus reducing incentives to work longer. Furthermore, informal phased retirement programs have provided a way for employers to retain workers with desired skills and

[8] IRC §414(q)

[9] Average benefit percentage is determined by first calculating individual employee benefit percentages, then calculating averages of these percentages for the NHCE group and HCE group, and finally dividing the average determined for the NHCE group by the average determined for the HCE group.

expertise on a flexible work schedule, by avoiding legal challenges imposed by the ERISA, the tax code, and the ADEA since these rules only apply to employee benefit programs. But as Penner et al. (2002) describes, they are "stopgap measures at best." To provide phased retirement programs to a broader group over the long run without facing hassles of being sued by some employees, employers will at some point need to implement a formal phased retirement program with written guidelines clearly describing the eligibility criteria, how employee benefits are provided, and how employers are protected from such claims as the ADEA. However, currently there is no legal rule that dictates when a series of informal arrangements become a plan. Such a determination is often made by the courts, and uncertainty about any determination may discourage employers from seeking formal plans, which may serve as an obstacle to meeting employees demands for phased retirement.

Conclusion

To this end, we have tried to understand why people work longer and what barriers to phased retirement the current workforce faces by conducting a literature review and an empirical analysis of the data from the 2014 HRS. To build on this effort, we are currently conducting in-depth interviews with employers, legal experts, and policymakers to have a deeper understanding of various obstacles to the creation of fully integrated retirement programs. Interviews will gather information on employer attitudes towards phased retirement, perceptions of older workers and impediments to developing part-time roles within formal phased retirement programs. Legal experts and policymakers are also being interviewed to improve our understanding of the complex barriers in implementing flexible working arrangements in old age for both employers and employees. Findings from these interviews will be discussed in a future report. Subsequently, we will create separate factsheets for employers and employees that offer a range of viable solutions tailored to the specific needs of each respective population. Additionally, a policy brief will summarize the legal issues that hinder formal phased retirement programs to be implemented and will provide policymakers the information to put forward regulatory changes that will reform the current retirement system and support longer working lives.

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