# ПРОГРЕСИВНИЙ ЗАКОРДОННИЙ ДОСВІД РЕГУЛЮВАННЯ ВІДНОСИН ЗАЙНЯТОСТІ

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## AMERICAN REALITIES: BRIEFLY ABOUT MAIN SOURCES OF RETIREMENT INCOME

The article considers typical components, of which the income of modern American retirees is formed. As is in many developed countries, the most important sources of income Americans could count on in retirement include the existing system of social security, employer-sponsored pension plans, which are formed on the basis of contributions of employees and employers. The article also underlines such sources of income support, as part-time employment of retirees as well as individual savings outside employer – sponsored plans.

It is emphasized that under current conditions, the workers have comprehensive responsibility to set up their retirement savings during all active life in order to support their income at old age. It is very important to have a life strategy and use reasonable financial planning. The article provides data from several published surveys in the field of retirement income, that were conducted by leading insurance companies, as well as some public data from governmental agencies including Social Security Administration and Bureau of Labor Statistics.According to the results of these researches, there are several groups of workers with different approach to life strategies of funding retirement. Depending on age, the researchers identify the older group (Baby Boomers), the group, whose active activities begin in the 21st century (Millenials) and the "sandwich" group between them (GenerationX). Information and analysis included in this article will help to understand current developments in field of retirement income in the US.

For many people aging and stepping away from a regular employment with relying on retirement income and own savings definitely would be a difficult transition. The numbers of life expectancy in developed countries might promise another 20-25 years of active life after retirement. It raises questions about sources of income to provide if not habitual lifestyle but support appropriate level of living for remaining years.

From far away seems that American retirees live with worries free and prosperous life. However wellbeing in golden age depends of many factors especially on life-long strategies of preparation for retirement. The existing legislative and financial systems provide favorable environment to make these goals come true for significant part of population.

Let's take a look at separate components that typically are combined in retirement income. As is in many developed countries, there are several main sources of income Americans could count on in retirement.

<u>Number one is for Social Security</u> – social insurance program based on tax law to ensure sources of income for retirees, disabled persons, and families of retired, disabled or deceased workers. Today's workers and employers pay Social Security taxes into this program and money flows back out as monthly income to beneficiaries as soon as they became eligible. Over 8 in 10 Americans aged 65 and older receive Social Security. For over three out of five (61 percent) of them, Social Security is more than half their total income, and for one in three (33 percent), it is all or nearly all of their income. The eligibility and amount of Social Security depends on number worked credits (roughly at least 40 quarters or 10 years), average reported annual earnings and number of years one worked.

The maximum Social Security benefit for a worker retiring in 2017 at the normal retirement age was $2,687 a month equal to $32,244 of annual income. The average monthly Social Security benefit paid in June 2017 was $1,413 a month that is equal to $16,956 of annual income for retired workers. These benefits are capped at a certain dollar amount each year, regardless of how much a person earns because of limit on social security wage base taken in calculations and cost of living adjustments.

<u>Number two is for employee's savings through retirement plans</u> – qualified defined contributions plans and tax deferred annuities provided to them by their employers. In 2016, about 44 % of private industry workers participated in these plans. Defined contribution retirement plans are a component of employer-sponsored benefit packages. These plans accumulate tax-deferred savings in individual employee accounts established by the employer. The government provides tax and savings incentives to

both employers and employees by making it legal to set aside money on a tax-deferred, salary reduction basis for retirement expenses. Businesses have incentives for contributing money to these accounts as deferred salary because it reduces their income and payroll tax liabilities. The portion of deferred salary that workers contribute also may be exempt from income taxes, as well as investment income tax liabilities until the funds are withdrawn at retirement. Annual maximum limits of contributions are set by the Internal Revenue Code.

According to a recent report from Transamerica (*A Compendium of Finding of American Workers, 18th Annual Survey, Transamerica Center For Retirement Studies, June 2018)* , about 39% percent of baby boomers expect their primary source of retirement income to be self-funded from accounts such as 401(k)s, 403(b)s, and IRAs or other personal savings . Understandable, those higher-income retirees possess higher savings. More than half of the wealthiest retirees assume that their retirement savings will provide them with a median annual income of $30,000. However statistics does not support this rosy outlook. Per same Transamerica reports, baby boomers median balance while increased in 2.2 times since 2007 consists of $164,000. With 4% of annual return, this amount will produce only around $6,560 in annual income in first year of retirement.

<u>Number three is for pension plans sponsored by employer</u>. Before 1990's defined benefits / pension plans sponsored by employers were very common among large private companies. This plan provides employees with guaranteed monthly/annual payments that are based on a benefit formula. A participant's retirement age, length of service and pre-retirement earnings may affect the benefit received. In the private sector, defined benefit plans are typically funded exclusively by employer contributions. The amount of annual contribution has been calculated by actuary based on certain mathematic assumptions. Number of these plans is in decline now as companies discontinue making mandatory contributions. Many pension plans are underfunded; this caused already legal consequences for employers in cases of declared bankruptcies or mergers. Major trend in retirement field is to move toward self-funded voluntary defined contributions plans.

Roughly one-third of current retirees receive public pensions, so this income doesn't apply to the majority of retirees. Pension numbers vary widely, with the median private pension bringing in less than $10,000 per year and federal pensions averaging $22,172 and $24,592 for a railroad pension. In last two years percentage of retirees receiving pensions dropped on 6 points. Even fewer workers (21 %) are expecting a steady stream of payments from their former employer in retirement.

<u>Number four is for Part-time work after retirement</u>. Many Americans are forced to continue working past 65 in order to maintain their desired lifestyle. According to the Bureau of Labor Statistics, among 65- to 74-year-olds, labor force participation is predicted to hit 32 percent by 2022, up from 20 percent in 2002. At age 75 and up, the rate will jump from 5 percent in 2002 to 11 percent in 2022. And, other studies predict work after retirement age to be even more common. Transamerica estimates that two-thirds of all baby boomers plan to or already are working past age 65 and about 8% do not plan to retire at all. According to the AARP, the median retirement income earned by retirees from work is $25,000 a year. New retirement includes employment!

<u>Number five is for personal savings i</u>n forms of bank accounts, brokerage accounts, individual retirements accounts (IRA) and mutual funds, home equity, rental properties and royalties. About 43% retirees consider them as a minor part of retirement income and 23% as a significant source. Some savings have been held on FDIC-insured banking accounts as certificates of deposits, and for 8% it has been seen as a major source. Their value is insured up to certain amount ($100,000-150,000) from losing value. Aware of market volatility, this type of individual savings is still popular despite of relatively low interest rates.

There is a rule that younger workers tend to invest more to risky variable securities and the older moving to most conservative fixed income generating options. Accordingly to Gallup poll (*Gallup poll. Update: Americans' Concerns About Retirement Persist, by Frank Newport, April2-11, 2018. Economy, May 3, 2018*), just 11 % of retirees say a significant part of their income comes from individual stocks or mutual fund investments. About twice as many workers (20 percent) are hoping the stock market will give their retirement income a lift.

Great inspiration is to pay off primary mortgage before retiring, this way value of home including built equity may become a source of income at retirement. House payments are the highest household's expense. Per same Gallup poll, about 18 percent of retirees are using the equity they have built up in their home to help pay for retirement, perhaps using a reverse mortgage or by significantly downsizing and pocketing the extra cash. The advisors usually warn against taking loan to offset home equity as it has to be repaid back. However additional 18% of workers are hoping that home equity will give their retirement finances a boost in near future.

Relatively often some funds are invested into second home that becoming a rental property may produce a significant part of retirement income. Income from a rental property or intellectual property can be used to help pay for retirement by the people who have this option, which includes 6 percent of retirees and another 7 percent of workers.

This is how general breakdown of retirement income looks like, based on several research: 37-39% is coming from social security; 19-21% - from employer-sponsored retirement plans; average 30-32% contributes continued past normal retirement age employment; 10-14% is expected to be covered from personal savings. Remaining 3-5% is coming from undisclosed other income.

Combining all listed sources, how retirement income corresponds with household expenses, how much is actually needed to cover major expenses?

An unspoken rule is that in retirement a person needs to replace from 70% to 90% of income to maintain standard of living. This may vary depending on when one retire, where choose to live, how long to live, when to start taking Social Security and on a list of other factors. However recent survey by T. Rowe Price of new retirees who have 401(k) account balances or rollover IRAs found that you can live comfortably on a lot less. The report suggests that nearly three years into retirement, the majority of retirees are living on just 66% of their pre-retirement income on average, or $58,000 annually (household income). Eighty-five percent of the survey's 1,507 respondents say they don't need to spend as much as they did before retirement to be satisfied. And, 57% report they live as well or better than when they were working. But the figure likely doesn't include special or one-time expenses, such as traveling, house repairs or car replacements or dramatic raise of expenses in case of a disastrous illness or for long-term care.

The expenses after retirement due to paying off mortgage debts go down, however real income for retirees is still much lower than desired and comfortable $58,000. According to data provided in T. Rowe Price survey *(First Look: Assessing the New Retiree Experience. Survey Highlights. Retiree Spending Study. Brightwork Partners LLC),* the median income of married retired couples in 2016 was $39,823, which means half of all such households received less than that amount, and half received more. Basically it means that this family income consists of two about average social security payments and some other income. The income drop significantly for households age 75 and up, to a median of $30,635. This number reflects a higher number of retired people, since relatively few individuals of age 75 and up are working.

A way to adjust spending to income for many retirees is to move to less expensive areas. Rural areas with same level of service and comfort are usually cheaper than urban areas. For example, average cost of living for people of 65 + years old in rural areas of state of Colorado, is $19,785. Many retirees take this option and move out to towns and even countries where their savings will last longer.

Whether retirement income can keep pace with longer life spans is a source of concern for many retirees. Key findings from a 2016 brief provided by Boston College's Center for Retirement Research (*National retirement Risk Index shows modest improvement in 2016, by Alicia H. Munnell, Wenliang Hou, and Geoffrey T. Sanzenbacher. a 2018.)* - retirement security remains a major challenge that requires today's workers to save more and/or work longer. Roughly half of all retirees are at risk of falling short when it comes to retirement income.

According to the "New Generations Ahead Study" from Allianz Life , 63% of respondents are more afraid of running out of money in retirement than they are of death. The survey shows some discrepancy between actually saved funds and preparedness for retirement how workers self-estimate it. Over 70% of baby boomers say that they consider that they are financially ready for retirement, this number rose from 58% in 2010. The millennials (younger group) also seem overconfident about their long-term finances. About 74% of them feel prepared for retirement and 76% are confident their income will last a lifetime. In fact, Allianz found the median retirement savings for millennials was $35,000 only. With uncertain future of Social Security this does not look very promising but they have another 30 years to build an investment nest.

The surveys found that a half of respondents who feels it's impossible to determine retirement expense tend to have a financial advisor. Retirement planning becomes a real helping tool. In addition to certified planners, majority of providers create electronic online tools to determine different versions of and scenarios of life "after" including setting goals, social security calculations, savings rates, and investment models, up to creating virtual accounts. It is important for advisers to understand and account the unique financial challenges workers face including longevity risk of running out of money, predicting healthcare costs and developing a sound strategy around Social Security income.

So generally, even if many workers still rely exclusively on Social Security and have a little or no personal savings, a key to an optimistic outlook at retirement is advance planning. By smart saving and acquiring all possible sources there is a possibility of entering retirement with considerable assets to make golden years long and comfortable.

Common Definitions:

In order to retire a person must attain of Normal Retirement Age (Full Retirement Age) – the age one becomes entitles for full amount of retirement benefit under Social Security. It depends of date of birth and currently varies from 65 to 67. For people born before 1937 normal retirement age is 65, for others up to born in 1954 it gradually increases from 65 to 66, then increased again and will be 67 for those born in 1960 and later. The earliest age a person can retire is 62, but at 62 he/she will be entitled for about 75% of full Social Security benefit.

Three groups the workforce the researchers operate with are as following: millennials - youngest group born in 1982-2000; baby boomers – oldest group born in 1946-1964; and generation X – sandwich group between two already named.

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**Американскі реалії: стисло про основні джерела доходів пенсіонерів у США**

*У статті розглядаються окремі складові доходу сучасних американських пенсіонерів. Головними ресурсами є: наявна система соціального забезпечення (social security), спонсоровані работодавцями пенсійні внески, що формуються на основі поєднання внесків працівників і роботодавців (defined contribution and defined benefits plans). Застосовуються і такі джерела підтримки доходу як часткова зайнятість осіб пенсійного віку (part time employment) та індивідуальні накопичувальні пенсійні рахунки, які відкривають самі працівники незалежно від роботодавця (individual retirement accounts). Підкреслюється, що в сучасних умовах багато залежить від самого працівника, який протягом активного життя повинен відповідально ставитися до формування свого доходу в старості, мати життєву стратегію та спиратися на інструменти фінансового планування. У роботі використані проведені на замовлення провідних страхових компаній дослідження у сфері отримання доходів, а також дані адміністративних органів (Social Security Administration). За результатами досліджень виділені різні вікові групи працівників із притаманними їм особливостями в підходах до формування доходів – літня група (Baby Boomers), група, початок активної діяльності якої припадає на XXI століття (Millenials), та середня (GenerationX). Інформація й аналіз, включені в статтю, можуть бути корисні для кращого розуміння сучасної Американської системи формування доходів осіб старшого віку.*