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Older Workers: Employment and Retirement Trends

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Congressional Research Service

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Older Workers: Employment and Retirement Trends

Updated October 26, 2001

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Older Workers: Employment and Retirement Trends

Summary

As the members of the "baby boom" generation – people born between 1946 and 1964 – approach retirement, the demographic profile of the U.S. workforce will undergo a substantial shift: a greater number of older workers will be joined by relatively few new entrants to the labor force. According to the U.S. Bureau of the Census, while the number of people between the ages of 25 and 64 will grow by about 18.4 million between 2000 and 2015, an estimated 86% of this increase will occur among people ages 55 to 64.

The *labor force participation rate* (the percentage of people either employed or unemployed but looking for work) among men 55 and older is lower today than it was a half-century ago. Most of the decline, however, occurred over a brief period from about 1970 to the mid-1980s. At the same time, the labor force participation rate among women ages 55 to 64 has risen steadily from 27% in 1950 to 52% in 2000. Data collected by the Census Bureau indicate that during the period from 1995 to 2001, employment remained generally steady among men 55 to 61 years old and rose among women in this age group. Of men ages 55 to 61, 72% were employed in 2001, the same percentage as in 1995. Employment among women ages 55 to 61 rose from 54% in 1995 to 58% in 2001. Among men ages 62 to 64, 46% were employed in 2001, compared with 42% in 1995, while among women ages 62 to 64, employment increased from 31% in 1995 to 37% in 2001.

Labor force participation declines both with increasing age and with the receipt of pension income. Among men ages 55 to 64 who received income from a private pension or retirement savings plan during 2000, 38% were employed either full-time or part-time in March 2001. Among women 55 to 64 years old who received income from a private pension or retirement savings plan in 2000, 33% were employed in March 2001. Among people 65 or older, only 12% of men and 8% of women who had private pension income in 2000 were employed in March 2001.

As millions of workers reach retirement age over the next several years, employers might wish to induce some of those who would otherwise retire to remain on the job, perhaps on a part-time schedule. This is sometimes referred to as "phased retirement." Several approaches to phased retirement – such as job-sharing, reduced work schedules, and rehiring retired workers on a part-time or temporary basis – can be accommodated under current law. Some of these approaches, however, require the individual to separate from the firm before returning under an alternative work arrangement. Under current law, a pension plan cannot pay benefits unless the recipient has either separated from the employer or reached the pension plan's *normal retirement age*. Some employers see the statutory prohibition on *in-service* pension distributions as an obstacle to establishing phased retirement plans. They would prefer that employers be permitted to begin partial pension distributions to workers when they reach the company pension plan's *early retirement age*. In addition, they would like to be able to limit participation to workers in particular occupational categories. However, targeted participation could cause the plan to violate the provisions of the Internal Revenue Code that prohibit pension plans from discriminating in favor of highly-compensated employees in terms of benefits.

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Deciding when to retire is a choice that will affect an individual's economic circumstances for the rest of his or her life. In addition to affecting the lives of individuals, the retirement decisions of older workers have an impact on the nation's economy. The number of people retiring each year affects the size of the labor force, which has a direct impact on the economy's capacity to produce goods and services. Other things being equal, fewer retirements in any given year would result in a greater supply of experienced workers available to employers and fewer people relying on savings, pensions, and Social Security as their main sources of income. Consequently, changes in the age-profile of the population or the average age at which people retire have implications for both national income and the size and composition of the federal budget.

To understand the factors that affect the retirement decision, one must first know what it means to "retire." Retirement is most often defined with reference to two characteristics: nonparticipation in the paid labor force, and receipt of income from pensions, Social Security, and other retirement plans. An individual who does not work for compensation and who receives income only from pensions, Social Security, and financial assets, would meet this definition of retirement. An individual who works for compensation and receives no income from pensions or Social Security would not be retired according to this definition.

Between these two extremes, however, are those who might be considered to have "retired" based on one part of the definition but not the other. For example, individuals who have retired from careers in law-enforcement or the military – both of which typically provide pensions after 20 years of service – often work for many years at other jobs, while also receiving a pension from prior employment. In such cases, having retired from a particular occupation does not necessarily mean that one has retired from the workforce. On the other hand, many people who retire from full-time employment continue to work part-time to supplement the income they receive from pensions and Social Security. If the majority of their income is provided by Social Security, pensions, and savings, economists typically classify them as retired, even though they continue to engage in paid employment. As these examples suggest, not everyone who receives pension income is retired, and some people who work for pay actually are retired.

This report begins by describing the change in the age distribution of the U.S. population that will occur between 2000 and 2015 and summarizing the historical data on the labor force participation of older workers. This discussion is followed by an analysis of data from the Census Bureau's *Current Population Survey* on employment and receipt of pension income in recent years among persons age 55 and older. Employment trends among older workers are then discussed in the context of data from the Social Security Administration on the proportion of workers who claim retired-worker benefits before the full retirement age (currently age 65). The final section of the report discusses recent proposals to promote “phased retirement” through amendments to the sections of the Internal Revenue Code that govern the taxation of pension income.

The Aging of the Labor Force: 2000 to 2015

As the members of the “baby boom” generation – people born between 1946 and 1964 – approach retirement age, the demographic profile of the American population will undergo a profound change. According to the Bureau of the Census, the proportion of the U.S. population age 65 and older will increase from 12.6% in 2000 to 20% by 2030.[1] The age profile of the *working-age* population, however, already is undergoing a substantial shift toward a greater number of older workers and a relative scarcity of new entrants to the labor force. In 2001, the oldest baby boomers will turn 55, while the youngest members of the group will be 37 years old. These 77 million individuals comprise approximately 53% of the U.S. population between the ages of 25 and 64 in 2001. Their sheer numbers suggest that the impact on labor markets could be substantial if this generation chooses to retire earlier – or to remain in the workforce longer – than did previous generations.

The data presented in **Table 1** show how dramatically the age profile of the U.S. population will change between 2000 and 2015. According to estimates prepared by the U.S. Bureau of the Census, there were 178 million Americans age 25 or older in 2000. By 2015, this number will increase by about almost 17% to 208 million. However, the number of people ages 25 to 54 – the ages when labor force participation rates are at their highest levels – is projected to increase by only 2.5 million (2.1%) by 2015. At the same time, the number of people between the ages of 55 and 64 is projected to increase by *15.9 million*, or more than *66%*. In other words, while the number of people between the ages of 25 and 64 is projected to increase by about 18.4 million between 2000 and 2015, an estimated 86% of this increase is expected to occur among people between the ages of 55 and 64.

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[1] U.S. Bureau of the Census, “National Population Projections – Summary Tables,” reproduced in the *Statistical Abstract of the United States: 2000*, table 14, page 17.

Table 1. U.S. Population Age 25 and Older, 2000 and 2015
(Numbers in thousands)

	Age groups					
Year	**25 to 34**	**35 to 44**	**45 to 54**	**55 to 64**	**65 and up**	**Total**
2000						
Male	18,558	22,289	18,174	11,443	14,474	**84,938**
Female	18,882	22,605	18,992	12,558	20,363	**93,400**
Total	**37,440**	**44,894**	**37,166**	**24,001**	**34,837**	**178,338**
2015						
Male	20,500	19,139	20,600	19,205	19,929	**99,373**
Female	20,748	19,649	21,386	20,714	26,030	**108,527**
Total	**41,248**	**38,788**	**41,986**	**39,919**	**45,959**	**207,900**
Change	**3,808**	**-6,106**	**4,820**	**15,918**	**11,122**	**29,562**
% change	*10.2%*	*-13.6%*	*13.0%*	*66.3%*	*31.9%*	*16.6%*

Source: U.S. Department of Commerce, Bureau of the Census, *Current Population Reports*, Series P-25.

Long-term Trends in Labor Force Participation Rates

The *labor force participation rate* – the percentage of the population that is either employed or unemployed and looking for work – varies by age and gender. Moreover, within age and gender categories, labor force participation rates have changed over time as people have responded to economic developments and as the norms and values of society with respect to the employment of women and the retirement of older workers have changed. Also, as the United States has moved from an economy based on "smokestack industries" such as mining and manufacturing to one in which producing and distributing *information* is perhaps the most important industry, there has been an increase in demand for highly-educated workers and relatively less demand for workers who are able to perform physically demanding labor. At the same time that the economy has been producing jobs that can be done by workers of more varied physical abilities, the two-earner couple and the "working mom" have become the rule rather than the exception they were 30 or 40 years ago. With near universal coverage by Social Security and widespread participation in pensions and retirement savings plans, more workers can anticipate retirement as an opportunity for leisure and recreation rather than as a time of financial dependency on their children.

Men aged 55 and older are less likely to participate in the labor force today than were their counterparts a half-century ago.[2] According to data from the *Current Population Survey* (CPS) – a monthly survey conducted by the Bureau of the Census

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[2] For more information, see *Retirement Patterns and Bridge Jobs in the 1990s* by Joseph F. Quinn, Issue Brief 206, Employee Benefit Research Institute, Washington, DC, February 1999.

for the Bureau of labor Statistics – in the 1950s, about 5 in 6 men aged 55 to 64 participated in the labor force – that is, they were either working or actively looking for work.[3] (See **Table 2**). By the 1990s, only 2 in 3 men in that age group participated in the labor force. Most of the historical decline occurred over a relatively brief period, from about 1970 to the mid-1980s. Among men 65 and older, the decline in labor force participation began earlier, but it also appears to have ended around 1985. Between 1950 and 1985, the labor force participation rate among men 65 and older fell from 46% to about 16%. Since the mid-1980s, Labor force participation rates among men aged 55 to 64 years have remained in the range of 66% to 68%, while the rate for those aged 65 and older has remained between 16% and 18%.

From 1950 to the present, women's labor force participation rates have moved steadily upward. Among women aged 55 to 64, the rate rose from 27% in 1950 to 45% in 1990, and 52% in 2000. Among women 65 and older, however, the labor force participation rate has changed very little over the last 50 years, remaining between 8% and 11% over the 1950–2000 period.

The stability of labor force participation rates among men aged 55 and older since the mid-1980s is likely attributable to several factors. First, Social Security coverage has been expanded and now covers virtually all private sector nonfarm employment in the United States.[4] The earliest age of eligibility for Social Security retired worker benefits was set at 62—for women in 1956 and for men in 1961—and has not changed since. Second, in the private sector, the expansion in pension coverage that occurred in the 1950s and 1960s had ended by 1980—about half of all workers were covered by a pension plan in 2000, virtually the same percentage as were covered in 1980. Finally, most traditional defined-benefit pension plans have minimum age and length-of-service requirements that must be met before pension benefits can be paid. These provisions, in effect, establish a minimum age below which retirement is not a viable option for most workers. According to the BLS *Employee Benefits Survey*, more than 90% of employees in medium and large firms who had pension coverage in 1997 were covered by a plan with a minimum age requirement for retirement benefits, and more than 80% of these workers were covered by plans that had a minimum retirement age of 55 years or older.[5]

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[3] Labor force participation rates are annual averages from the monthly CPS data. The CPS, a scientifically designed survey of about 50,000 households, is conducted monthly by the Bureau of the Census on behalf of the Bureau of Labor Statistics. Using data derived from the CPS, the BLS publishes numerous labor force statistics by a variety of economic, social, and demographic characteristics. For more information on the CPS, see the *BLS Handbook of Methods*, Bulletin 2490 (Bureau of Labor Statistics, April 1997), ch. 1, pages 4-14.

[4] Approximately one-quarter of the employees of State and local governments—about 5 million people—work for governments that have elected not to participate in Social Security. This is the only remaining large group of workers not covered by Social Security.

[5] See *Employee Benefits in Medium and Large Private Establishments, 1997*, Bulletin 2517 (September 1999), tables 136 and 137, pages 108 and 109.

Table 2. Labor Force Participation Rates, 1950 to 2008

Men	Age groups		
Year	25 to 54	55 to 64	65 and up
1950	*96.5%*	*86.9%*	*45.8%*
1955	*97.4%*	*87.9%*	*39.6%*
1960	*97.0%*	*86.8%*	*33.1%*
1965	*96.7%*	*84.6%*	*27.9%*
1970	*95.8%*	*83.0%*	*26.8%*
1975	*94.4%*	*75.6%*	*21.6%*
1980	*94.2%*	*72.1%*	*19.0%*
1985	*93.9%*	*67.9%*	*15.8%*
1990	*93.4%*	*67.8%*	*16.3%*
1995	*91.6%*	*66.0%*	*16.8%*
1996	*91.8%*	*67.0%*	*16.9%*
1997	*91.8%*	*67.6%*	*17.1%*
1998	*91.8%*	*68.1%*	*16.5%*
1999	*91.7%*	*67.9%*	*16.9%*
2000	*91.6%*	*67.3%*	*17.5%*
*2008	*91.3%*	*69.4%*	*17.8%*

Women	Age groups		
Year	25 to 54	55 to 64	65 and up
1950	*36.8%*	*27.0%*	*9.7%*
1955	*39.8%*	*32.5%*	*10.6%*
1960	*42.9%*	*37.2%*	*10.8%*
1965	*45.2%*	*41.1%*	*10.0%*
1970	*50.1%*	*43.0%*	*9.7%*
1975	*55.1%*	*40.9%*	*8.2%*
1980	*64.0%*	*41.3%*	*8.1%*
1985	*69.6%*	*42.0%*	*7.3%*
1990	*74.0%*	*45.2%*	*8.6%*
1995	*75.6%*	*49.2%*	*8.8%*
1996	*76.1%*	*49.6%*	*8.6%*
1997	*76.7%*	*50.9%*	*8.6%*
1998	*76.5%*	*51.2%*	*8.6%*
1999	*76.8%*	*51.5%*	*8.9%*
2000	*76.8%*	*51.8%*	*9.4%*
*2008	*79.7%*	*57.7%*	*9.1%*

Source: U.S. Department of Labor, Bureau of Labor Statistics.
*Estimated by the Bureau of Labor Statistics.

Recent Employment Trends Among People Age 55 and Older

Data collected by the Census Bureau indicate that during the period from 1995 to 2001, employment remained generally steady among men 55 to 61 years old and rose among women in this age group.[6] (See **Table 3** and **Table 4**). Of men ages 55 to 61, 72% were employed in 2001, the same percentage as in 1995. Employment among women ages 55 to 61 rose from 54% in 1995 to 58% in 2001. Among men ages 62 to 64, 46% were employed in 2001, compared with 42% in 1995, while among women ages 62 to 64, employment increased from 31% in 1995 to 37% in 2001.

Much of the increase in employment among persons aged 55 years and older during the mid- to late-1990s probably was due to the strength of the economy during these years. Between 1995 and 2000, for example, the unemployment rate for workers of all ages declined from 5.6% to 4.0%. Over the same period, the Nation's real gross domestic product (GDP) grew at an average annual rate of 4.4%.[7] It is possible, however, that at least part of the increase in employment was due to the trend of workers choosing to remain in the labor force rather than taking early retirement, as well as the effects of long-term trends away from defined-benefit pension plans, which often include early-retirement subsidies, toward defined contribution plans, which are age-neutral in their design. The *Employee Benefits Survey*, for example, indicates that between 1993 and 1997, the proportion of full-time employees in medium and large private establishments who were covered by a defined-benefit pension plan fell from 56% to 50%. At the same time, the proportion of employees in these firms who were covered by defined-contribution plans rose from 49% to 57%.[8]

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[6] The labor force participation rates discussed in the previous section were based on annual averages of monthly data. The employment data analyzed in this section are from the March supplement to the CPS. They show employment in the week prior to the March CPS interview. The March CPS files were used for this analysis because they include detailed data about sources of income in the previous year. CRS used information about current labor force status rather than information about labor force status in the previous year because an individual who reported that he or she both worked and received pension income during the previous year might have worked and received pension income consecutively rather than concurrently.

[7] *Economic Report of the President* (Council of Economic Advisers, January 2001), table B-42 page 324 and table B-2, page 276.

[8] See *Employee Benefits in Medium and Large Private Establishments, 1993,* Bulletin 2456 (Bureau of Labor Statistics, November 1994) table 1, page 8; and *Employee Benefits in Medium and Large Private Establishments, 1997,* Bulletin 2517 (Bureau of Labor Statistics, September 1999) table 1, page 5 .

Table 3. Employment of Men Age 55 and Older, 1995 to 2001

Age in March	Population (000s)	Number employed (000s)	Percent employed	Employment: full-time	Employment: part-time
55 to 61					
1995	6,993	5,035	***72.0%***	*91.5%*	*8.5%*
1996	7,409	5,349	***72.2%***	*91.2%*	*8.8%*
1997	7,523	5,404	***71.8%***	*90.6%*	*9.4%*
1998	7,855	5,664	***72.1%***	*91.4%*	*8.7%*
1999	8,174	5,990	***73.3%***	*91.7%*	*8.3%*
2000	8,204	5,849	***71.3%***	*92.3%*	*7.7%*
2001	8,479	6,138	***72.4%***	*91.6%*	*8.4%*
62 to 64					
1995	2,879	1,206	***41.9%***	*79.0%*	*21.0%*
1996	2,681	1,159	***43.2%***	*77.8%*	*22.2%*
1997	2,733	1,255	***45.9%***	*79.2%*	*20.8%*
1998	2,812	1,283	***45.6%***	*80.9%*	*19.1%*
1999	2,785	1,297	***46.6%***	*78.4%*	*21.6%*
2000	2,927	1,380	***47.2%***	*77.9%*	*22.1%*
2001	2,771	1,284	***46.3%***	*77.2%*	*22.8%*
65 to 69					
1995	4,395	1,169	***26.6%***	*54.7%*	*45.3%*
1996	4,522	1,237	***27.3%***	*56.7%*	*43.3%*
1997	4,321	1,150	***26.6%***	*56.8%*	*43.2%*
1998	4,286	1,085	***25.3%***	*57.0%*	*43.0%*
1999	4,298	1,136	***26.4%***	*55.7%*	*44.3%*
2000	4,376	1,330	***30.4%***	*60.5%*	*39.5%*
2001	4,449	1,328	***29.9%***	*63.2%*	*36.8%*
70 and older					
1995	8,607	970	***11.3%***	*44.9%*	*55.1%*
1996	8,738	989	***11.3%***	*44.2%*	*55.8%*
1997	9,083	1,063	***11.7%***	*45.7%*	*54.3%*
1998	9,238	970	***10.5%***	*48.0%*	*52.0%*
1999	9,429	1,030	***10.9%***	*44.8%*	*55.2%*
2000	9,510	1,169	***12.3%***	*48.5%*	*51.5%*
2001	9,730	1,198	***12.3%***	*48.1%*	*51.9%*

Source: CRS analysis of the annual March demographic supplement to the *Current Population Survey*.

Table 4. Employment of Women Age 55 and Older, 1995 to 2001

Age in March	Population (000s)	Number employed (000s)	Percent employed	Employment: full-time	Employment: part-time
55 to 61					
1995	7,716	4,196	***54.4%***	*74.1%*	*25.9%*
1996	7,947	4,314	***54.3%***	*74.5%*	*25.5%*
1997	8,142	4,582	***56.3%***	*77.1%*	*22.9%*
1998	8,515	4,896	***57.5%***	*77.7%*	*22.9%*
1999	8,743	4,904	***56.1%***	*76.8%*	*23.2%*
2000	9,041	5,250	***58.1%***	*77.2%*	*22.8%*
2001	9,296	5,365	***57.7%***	*77.3%*	*22.7%*
62 to 64					
1995	3,162	975	***30.8%***	*58.3%*	*41.7%*
1996	3,044	968	***31.8%***	*59.3%*	*40.7%*
1997	3,069	1,047	***34.1%***	*62.5%*	*37.5%*
1998	3,065	1,040	***33.9%***	*61.2%*	*38.8%*
1999	3,199	1,102	***34.4%***	*60.1%*	*39.9%*
2000	3,209	1,109	***34.6%***	*61.4%*	*38.6%*
2001	3,236	1,185	***36.6%***	*62.6%*	*37.4%*
65 to 69					
1995	5,263	919	***17.5%***	*36.3%*	*63.7%*
1996	5,224	865	***16.6%***	*40.4%*	*59.6%*
1997	5,180	936	***18.1%***	*42.1%*	*57.9%*
1998	5,075	941	***18.5%***	*44.5%*	*55.5%*
1999	5,022	941	***18.7%***	*40.9%*	*59.1%*
2000	4,976	983	***19.7%***	*44.2%*	*55.8%*
2001	4,933	947	***19.2%***	*42.3%*	*57.7%*
70 and older					
1995	13,001	650	***5.0%***	*30.4%*	*69.6%*
1996	13,174	681	***5.2%***	*30.3%*	*69.7%*
1997	13,294	639	***4.8%***	*32.8%*	*67.2%*
1998	13,484	740	***5.5%***	*31.9%*	*68.1%*
1999	13,646	807	***5.9%***	*35.0%*	*65.0%*
2000	13,759	816	***5.9%***	*36.3%*	*63.7%*
2001	13,866	840	***6.1%***	*39.3%*	*60.7%*

Source: CRS analysis of the annual March demographic supplement to the *Current Population Survey*.

Pensions Among Older Workers

An important consideration for an individual who is deciding whether to retire from the workforce is whether the sources of income available in retirement will be adequate to maintain his or her desired standard of living. **Table 5** shows the proportion of men and women aged 55 and older who reported on the CPS that they received pension income of some kind during the calendar year prior to the survey. In this table, "pension income" includes employer-sponsored pensions (including military retirement), veterans' pensions; and periodic payments from annuities, insurance policies, individual retirement accounts, 401(k) accounts, and Keogh plans for the self-employed.

Not surprisingly, the proportion of men and women who receive income from a pension or other retirement plan increases with age. In 2000, only 19% of men aged 55 to 64 received any income from a pension or other retirement plan; among those 65 years and older, however, 43% had income from private pensions or retirement savings plans. The patterns among women are similar: only 12% of 55- to 64-year-old women received income from private pensions or retirement savings plans in 2000, while 29% of those aged 65 years and older received such income.

The proportion of men aged 55 to 64 years who were receiving pension income declined from 23% in 1994 to 19% in 2000. Over the same period, the proportion receiving pension income fell from 47% to 43% among men aged 65 and older. The proportion of women aged 55 to 64 years with pension income was more stable, at 11% to 12% throughout the 1994–2000 period. Among women 65 and older, 29% received income from private pensions and retirement plans in 2000, the same percentage as in 1994.

Table 5. Receipt of Income From Employer Pensions and Retirement Savings Plans

	All individuals age 55 and older (000s)					
	Individuals 55 to 64 years old			Individuals age 65 and older		
Men	Number of people	Number of recipients	*Percentage*	Number of people	Number of recipients	*Percentage*
1995	9,872	2,303	*23.3%*	13,001	6,108	*47.0%*
1996	10,090	2,279	*22.6%*	13,260	6,206	*46.8%*
1997	10,256	2,177	*21.2%*	13,404	6,316	*47.1%*
1998	10,667	2,152	*20.2%*	13,524	6,317	*46.7%*
1999	10,959	2,195	*20.0%*	13,727	6,457	*47.0%*
2000	11,131	2,174	*19.5%*	13,886	6,358	*45.8%*
2001	11,249	2,124	*18.9%*	14,179	6,099	*43.0%*
Women						
1995	10,878	1,316	*12.1%*	18,264	5,252	*28.8%*
1996	10,991	1,164	*10.6%*	18,398	5,025	*27.3%*
1997	11,210	1,287	*11.5%*	18,474	4,933	*26.7%*
1998	11,580	1,253	*10.8%*	18,559	5,114	*27.6%*
1999	11,943	1,403	*11.7%*	18,668	5,186	*27.8%*
2000	12,250	1,439	*11.7%*	18,735	5,513	*29.4%*
2001	12,532	1,475	*11.8%*	18,799	5,426	*28.9%*

Source: CRS analysis of the annual income supplement to the *Current Population Survey*.

Note: Retirement plans may include a traditional pension, a retirement savings plan, or both. The income year is the year prior to the survey.

Work by Pension Recipients. Among men aged 55 to 64 who received income from a private pension or retirement savings plan during 2000, 37.5% were employed either full or part time in March 2001 – the same percentage as in 1995. (See **Table 6**). Relatively few men aged 65 or older who receive income from private pensions and retirement savings plans also engage in paid employment: only 10% to 12% were employed, on average, over the 1995–2001 period. Women who receive pension income are even less likely than men to be employed. Among 55- to 64-year–old women who received income from a private pension or retirement savings plan in 2000, just 33% were employed in March 2001. Among women aged 65 years and older, only 6% to 8%, on average, were employed during the 1995–2001 period.

Table 6. Employment of Recipients of Employer Pensions and Retirement Savings Plans, Age 55 and Older

	Retirement income recipients age 55 and older (000s)					
	Recipients, age 55 to 64			Recipients, age 65 and older		
Men	Number of recipients	Number employed	*Percentage*	Number of recipients	Number employed	*Percentage*
1995	2,303	864	*37.5%*	6,108	727	*11.9%*
1996	2,279	831	*36.5%*	6,206	726	*11.7%*
1997	2,177	832	*38.2%*	6,316	724	*11.5%*
1998	2,152	778	*36.2%*	6,317	648	*10.3%*
1999	2,195	870	*39.7%*	6,457	706	*10.9%*
2000	2,174	799	*36.7%*	6,358	739	*11.6%*
2001	2,124	797	*37.5%*	6,099	721	*11.8%*
Women						
1995	1,316	410	*31.2%*	5,252	326	*6.2%*
1996	1,164	324	*27.9%*	5,025	281	*5.6%*
1997	1,287	416	*32.3%*	4,933	277	*5.6%*
1998	1,253	363	*29.0%*	5,114	404	*7.9%*
1999	1,403	370	*26.3%*	5,186	426	*8.2%*
2000	1,439	442	*30.7%*	5,513	401	*7.3%*
2001	1,475	488	*33.1%*	5,426	436	*8.0%*

Source: CRS analysis of the annual income supplement to the *Current Population Survey*.

Note: Retirement plans may include a traditional pension, a retirement savings plan, or both. The income year is the year prior to the survey. Employment is in current year.

Social Security Retirement Benefits

Age when benefits begin. Currently, the "full retirement age" under Social Security is 65. Social Security retired-worker benefits are first available at age 62, but benefits that begin before the full retirement age are subject to a permanent actuarial reduction equal to 5/9% for each month under age 65. At age 62, this results in a benefit equal to 80% of the amount that the worker would have received without the reduction. As a result of the *Social Security Amendments of 1983* (P.L. 98-21), the Social Security full retirement age is being increased to 67 incrementally over a 22-year period. Reduced benefits will continue to be available as early as age 62, but when the full retirement age reaches 67, the benefit payable at 62 will be just 70% of the amount that would have been paid if not for the early retirement reduction.

Most people choose to begin receiving Social Security retirement benefits before age 65. The data presented in **Table 7** show that approximately 75% of men and 80% of women who began receiving Social Security retired worker benefits between 1990 and 1999 applied for benefits before age 65. Among women, this percentage has remained steady over the past 10 years,[9] while among men, there was a slight increase in the proportion of applicants younger than 65 years.

The data presented in **Table 3** and **Table 4** indicate that the proportion of 55 to 64 year-olds engaged in paid employment rose during the mid- to late- 1990s. The data also show, however, that a much smaller proportion of 62- to 64-year-olds were employed than were among those aged 55 to 61. One reason for the sharp decline is that age 62 is the earliest age of eligibility for Social Security retirement benefits.[10] The availability of (actuarially reduced) Social Security benefits at 62 allows many people who otherwise would have continued working to retire from the labor force.

The Social Security system also affects labor force participation through the *delayed retirement credit* and the *earnings test*. The delayed retirement credit provides a permanent increase in benefits for workers who delay their receipt of Social Security benefits until after age 65 – thus creating an incentive for older workers to remain in the labor force. The earnings test reduces the Social Security benefits of recipients under the normal retirement age (currently 65) whose earnings exceed specific thresholds.[11] In 2001 a Social Security recipient under age 65 can earn up to $10,680 without having his or her benefit reduced, but benefits are cut by $1.00 for each $2.00 earned in excess of that amount. This creates a financial incentive for these individuals to reduce their earnings below the threshold. Congress has at times altered both the delayed retirement credit and the earnings test to encourage workers to stay in the labor force.

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[9] The percentage of awards to women age 65 and older increased temporarily in 1997 and 1998 due to an outreach effort by the Social Security Administration to convert non-disabled widow beneficiaries to the higher benefits to which they were entitled as retired workers.

[10] Sixty-two also is the *normal retirement age* in about one-quarter of private pension plans.

[11] The *Senior Citizens' Freedom to Work Act* (P.L. 106-182, April 7, 2000) eliminated the earnings test for people at the "full retirement age" (currently age 65) or older, effective January 1, 2000. See CRS Report 98-789, *Social Security: Proposed Changes in the Earnings Test*, by Geoffrey Kollmann.

Table 7. Social Security Retired Worker Benefit Awards by Age and Gender

	Age in year when retired worker benefits began					
	62 to 64		**65**		**Over 65**	
Men	Awards	*Percentage of all awards*	Awards	*Percentage of all awards*	Awards	*Percentage of all awards*
1990	618,900	*73.8%*	160,300	*19.1%*	58,900	*7.0%*
1991	639,800	*73.3%*	172,200	*19.7%*	61,300	*7.0%*
1992	641,800	*74.2%*	166,100	*19.2%*	57,600	*6.7%*
1993	646,100	*75.3%*	159,400	*18.6%*	52,100	*6.1%*
1994	607,600	*76.1%*	145,500	*18.2%*	45,600	*5.7%*
1995	596,500	*75.6%*	145,900	*18.5%*	47,000	*6.0%*
1996	581,900	*76.0%*	135,200	*17.7%*	48,300	*6.3%*
1997	586,300	*75.4%*	137,300	*17.7%*	53,800	*6.9%*
1998	586,800	*75.7%*	136,300	*17.6%*	52,100	*6.7%*
1999	606,100	*75.6%*	140,500	*17.5%*	55,000	*6.9%*

	62 to 64		**65**		**Over 65**	
Women	Awards	*Percentage of all awards*	Awards	*Percentage of all awards*	Awards	*Percentage of all awards*
1990	487,800	*79.6%*	86,900	*14.2%*	38,200	*6.2%*
1991	489,100	*79.0%*	95,400	*15.4%*	34,400	*5.6%*
1992	510,600	*80.1%*	89,900	*14.1%*	36,600	*5.7%*
1993	502,800	*79.5%*	97,100	*15.4%*	32,200	*5.1%*
1994	504,600	*81.5%*	82,600	*13.3%*	31,600	*5.1%*
1995	486,200	*79.5%*	88,900	*14.5%*	36,300	*5.9%*
1996	488,100	*80.4%*	86,500	*14.3%*	32,200	*5.3%*
*1997	486,500	*66.7%*	86,500	*11.9%*	156,600	*21.5%*
*1998	497,500	*75.9%*	92,500	*14.1%*	65,800	*10.0%*
1999	514,300	*78.6%*	93,300	*14.3%*	46,400	*7.1%*

Source: *Annual Statistical Supplement to the Social Security Bulletin*, various years.

*__Note:__ Special outreach programs by the Social Security Administration resulted in an above-average number of conversions of non-disabled widows to retired worker benefits in 1997 and 1998. Initial awards exclude conversions from disabled worker benefits to retired worker benefits.

Retired worked beneficiaries as a percentage of each age category. If more workers chose to delay receipt of Social Security benefits until age 65, this delay would eventually show up as a declining percentage of 62- to 64-year-olds who are receiving such benefits. The data presented in **Table 8** show that there was a decline of about two percentage points between 1995 and 1999 in the proportion of men aged 62 to 64 who were receiving benefits. This coincided with the rising employment–population ratio among men in this age group. The lower rate among 62- to 64-year-old men during this period may have been caused by robust economic growth, or it may reflect a trend toward later retirement, independent of economic conditions. More time will be needed before firm conclusions can be drawn. Among women aged 62 to 64, the proportion who were receiving Social Security benefits rose slightly from 1990 to 1999, which is reflected in the 5-year averages for the first half and second half of the decade. From 1990 through 1994, an annual average of 34% of women aged 62 to 64 years received Social Security retired worker benefits. For the 5 years from 1995 through 1999, the annual average was 35.3%.

Table 8. Social Security Retired Worker Beneficiaries by Age and Gender

(Retired worker beneficiaries, in thousands)

	62 to 64		65 to 69		70 and over	
Men	Number	*Percentage of age group*	Number	*Percentage of age group*	Number	*Percentage of age group*
1990	1,336	*43.7%*	3,898	*83.8%*	7,751	*91.7%*
1991	1,345	*43.7%*	3,896	*84.0%*	7,985	*91.8%*
1992	1,351	*43.9%*	3,937	*84.5%*	8,186	*91.9%*
1993	1,350	*44.5%*	3,946	*84.5%*	8,354	*91.7%*
1994	1,353	*44.8%*	3,906	*83.6%*	8,536	*91.3%*
1995	1,320	*44.7%*	3,900	*83.4%*	8,694	*91.2%*
1996	1,293	*44.6%*	3,871	*83.1%*	8,848	*90.6%*
1997	1,278	*43.0%*	3,836	*83.8%*	9,012	*90.6%*
1998	1,286	*42.6%*	3,783	*83.5%*	9,138	*90.2%*
1999	1,302	*42.5%*	3,790	*84.3%*	9,238	*89.9%*

	62 to 64		65 to 69		70 and over	
Women	Number	*Percentage of age group*	Number	*Percentage of age group*	Number	*Percentage of age group*
1990	1,167	*34.2%*	3,067	*55.6%*	7,607	*55.9%*
1991	1,150	*33.7%*	3,062	*55.7%*	7,836	*56.4%*
1992	1,137	*33.7%*	3,098	*56.4%*	8,037	*56.7%*
1993	1,126	*33.9%*	3,104	*56.7%*	8,218	*57.1%*
1994	1,139	*34.5%*	3,065	*56.5%*	8,404	*57.4%*
1995	1,128	*35.0%*	3,058	*56.7%*	8,570	*57.7%*
1996	1,126	*35.6%*	3,046	*57.0%*	8,715	*57.8%*
1997	1,131	*35.1%*	3,053	*58.1%*	8,972	*58.9%*
1998	1,156	*35.3%*	3,036	*58.8%*	9,112	*59.3%*
1999	1,180	*35.6%*	3,070	*60.1%*	9,203	*59.4%*

Source: *Annual Statistical Supplement to the Social Security Bulletin*, various years.

Older Workers and "Phased Retirement"

In the traditional view of retirement, a worker moves from full-time employment to complete withdrawal from the labor force in a single step. In fact, however, some workers choose to continue working after they have retired from their "career" jobs. The data in **Table 6**, for example, show that 38% of men and 33% of women aged 55 to 64 who received income from private pension plans in 2000 were employed in March 2001. The process of retiring often occurs gradually over a number of years, with many workers retiring from year-round, full-time employment and moving to part-time or part-year work at another firm, often in a different occupation.

As members of the baby-boom generation begin retiring in the coming decades, millions of skilled and experienced workers will exit the labor force. As this occurs, employers may find it necessary to alter their employment practices and pension plans to induce some of those who would otherwise retire completely to remain on the job, perhaps on a part-time or part-year schedule. This process is sometimes referred to as *phased retirement*. No statutory definition of phased retirement exists, but one analyst has described it as "the situation in which an older individual is actively working for an employer part time or [on] an otherwise reduced schedule as a transition into full retirement. [It] may also include situations in which older employees receive some or all of their retirement benefits while still employed."[12]

Advocates of phased retirement contend that more pension-eligible individuals would choose to continue working if employers could offer them the opportunity to collect pension benefits while still on the employer's payroll. Under current law, this option can be offered only to employees who have reached a pension plan's *normal retirement age*. Some employers have suggested phased retirement would be embraced by more firms if this option could be offered to employees at the plan's *early retirement age*. Employers generally would prefer to offer the option of receiving these "in-service" distributions only to selected categories or classifications of plan participants.[13] In order for either of these actions to be taken, however, the Internal Revenue Code and the Employee Retirement Income Security Act (ERISA) would need to be amended.[14]

Current approaches to phased retirement. A study conducted by the benefits consulting firm Watson Wyatt Worldwide found that 16% of the 586 firms participating in the survey offered some form of phased retirement to their employees.[15] The firms surveyed by Watson Wyatt described a number of strategies that employers can use to retain the services of valued employees who are eligible for

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[12] Testimony of Wilma K. Schopp on behalf of the Association of Private Pension and Welfare Plans before the U.S. Senate Special Committee on Aging, April 3, 2000.

[13] This discussion refers to in-service distributions under *defined benefit* pension plans. In-service distributions under *defined contribution* plans are discussed later in this report.

[14] See, for example, *New Opportunities for Older Workers,* issued by the Committee for Economic Development, Washington, DC, 1999.

[15] Laurene A. Graig and Valerie Paganelli, "Phased Retirement: Reshaping the End of Work," *Compensation and Benefits Management*, vol. 16 no. 2 (Spring 2000).

retirement and who might be lost to the firm if the only options available are full-time employment or full-time retirement. Although the firms participating in the survey may not be representative of all employers, their practices with respect to phased retirement offer some insights into the strategies that firms have been able to employ under current law and regulations to promote phased retirement among their employees.[16]

According to the data collected by Watson Wyatt, many firms rehire retired employees on a part-time or temporary basis: 75% of the firms that reported having a phased retirement arrangement said that they rehire employees after they retire, usually as part-time or temporary workers. In addition, 42% of firms with phased retirement said they contracted with retired employees to be consultants. (Some firms had both kinds of arrangements with retired employees). Of the firms with phased retirement, 60% said that their approach included allowing retirement-eligible employees to work fewer days per week or fewer hours per day. Other policies include allowing employees who are not ready to retire fully to transfer to other jobs within the firm (32% of firms had such policies), extended leaves of absence (23%), and job sharing (19%).

As the variety of these arrangements indicates, several approaches to phased retirement can be accommodated under current law. It is important to note, however, that two of the most popular arrangements—hiring retired former employees on a part-time or temporary basis and hiring retirees as contractors—require the individual to separate from the firm before returning under an alternative work arrangement. This introduces considerable uncertainty into the process for both the retiree and the employer, because once the employment relationship is severed, neither party is legally bound to renew it.

Another popular approach to phased retirement is to allow employees to reduce the number of days per week or hours per day that they work for a period of months or years before they cease employment altogether. Unless the employee has reached the pension plan's normal retirement age, however, the plan cannot pay retirement benefits to the individual while he or she remains employed by the firm, even if only on a part-time basis. A plan that pays benefits to an employee that has not yet reached the plan's normal retirement age could lose its tax-qualified status.[17] In order to qualify for the favorable tax status granted to tax-qualified pension plans, the plan must pay benefits only on condition of death, disability, termination of employment, plan termination, or at the normal retirement age.[18]

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[16] The 586 firms that participated in the survey represent only about 6% of the 9,500 employers to whom the survey materials were sent. Thus, caution should be used when interpreting the results of the survey.

[17] In a "tax-qualified" plan, employer contributions to the plan are deductible business expenses for the firm and neither the employer contributions nor investment earnings on those contributions are counted as income to the employee in the years that they occur; instead, pensions are taxed as income when the benefits are paid to plan participants in retirement. Usually, retirees are taxed at a lower marginal tax rate than when they worked.

[18] *Code of Federal Regulations*, § 1.401-1(b)(1)(i).

An employee who has reached the pension plan's normal retirement age can begin to receive distributions from the plan, even if he or she continues to be employed by the firm.[19] Likewise, an employee who has reached the plan's early retirement age can begin to receive distributions from the plan upon separation from the firm, provided that he or she has met the required number of years of service stipulated by the plan. If a participant has separated from the employer and has begun to receive distributions from the plan at the early retirement age, he or she can continue to receive these distributions, even if at some future date the participant becomes re-employed by the plan sponsor.

Policy issues. Some employers see the statutory prohibition on making in-service pension distributions to employees who have not yet reached normal retirement age as an obstacle to establishing phased retirement plans because some older workers would find it financially impractical to cut back to a part-time or part-year work schedule if they were unable to supplement their earnings with pension income. One way for a firm to offer phased retirement to these workers under current law, without jeopardizing the tax-qualified status of its pension plan, would be to lower the normal retirement age. For example, if the normal retirement age under the plan is 62 years and the early retirement age is 55 years, the firm could reduce the normal retirement age to some age between 55 and 61. From the an employer's point of view, there would be at least two potential drawbacks to such an approach. It could result in an unintended exodus of workers into retirement, because all eligible plan participants would be able to receive full pension benefits at an earlier age than previously, and it could result in a dramatic increase in the cost of funding the plan, because full benefits would be payable at a younger age.

Rather than reduce the normal retirement age in their pension plans, some employers would prefer that Congress amend the Internal Revenue Code to allow in-service pension distributions to employees who have reached the plan's early retirement age (or some age between the early and normal retirement ages).[20] Some observers believe, however, that such a policy would be contrary to the main purpose of pension plans, which is to replace wage income during retirement. These critics say that if employers were permitted to pay pension benefits to individuals still engaged in gainful employment, the benefits would become a tax-subsidized supplement to wages, paid to individuals who are still able to work. They argue that pension benefits are intended to be a substitute for wages and should be paid only to retired workers. Permitting in-service distributions to current employees who have not reached the plan's normal retirement age might allow employers to compensate current employees with pension funds, effectively reducing their operating expenses by shifting some costs that would otherwise be paid as wages to the pension fund.

In 2000, about 2.4 million workers in the United States received pension payments from a former employer. More than a million of these workers were under age 65. (See **Table 6**.) Current law allows an individual who has separated from a

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[19] If a plan participant continues to work for an employer beyond the plan's normal retirement age, the plan must meet the statutory requirements for continued benefit accruals; see 26 U.S.C. § 411(b)(1)(H).

[20] Requirements for qualification of pension plans are defined at 26 U.S.C. § 401(a).

firm and is receiving pension distributions under an early retirement provision of the plan to become re-employed by that firm, while continuing to receive those benefits. Some employers have argued that it should be permissible to allow eligible employees to receive partial distributions under an early retirement provision without first having to separate from the employer and then be rehired. Such an option would require an amendment to the tax code. However, plan sponsors currently have the option of setting the normal retirement age at any age not greater than 65, and the early retirement age at any age under the normal retirement age, provided that the plan complies with the statutory requirements with respect to benefit accrual, vesting of benefits, nondiscrimination on the basis of age, and other plan characteristics.

An amendment to the tax code permitting in-service distributions at the early retirement age would alter incentives to work or retire, as well as how much to work and for whom to work. Consequently, it would affect both labor force participation and hours worked among affected employees. The net effect of these changes in labor force participation and hours worked would be almost impossible to predict. Some workers who would otherwise have fully retired before the plan's normal retirement age would choose instead to continue working for their current employer on a reduced schedule, because they would be able to take partial pension distributions while still employed. This would tend to increase labor force participation. Other workers who would have taken early retirement and then sought other employment might choose instead to remain with their current employer on a reduced schedule. The effect of this change in behavior on hours worked might be close to neutral, depending on the wages available from alternative employment and the income received from pension distributions. Finally, some employees who otherwise would have chosen to continue working until reaching the plan's normal retirement age might instead reduce their work schedule and supplement their earnings with partial distributions from the retirement plan. This would tend to reduce total hours worked.

Distributions from 401(k) plans. Coverage under defined contribution plans, such as those authorized under section 401(k) of the Internal Revenue Code, grew rapidly during the 1990s. Between 1991 and 1997, the proportion of workers in medium and large private-sector establishments (those with 100 or more employees) who participated in defined contribution retirement plans increased from 49% to 57%.[21] The trend among small establishments (those with fewer than 100 employees) was similar. In 1996, 38% of employees in small private establishments participated in defined contribution retirement plans, compared with 28% in 1990.[22]

In-service distributions from defined contribution plans that occur before the participant reaches age 59½ are subject to a 10% excise tax in addition to ordinary income taxes. Distributions may begin as early as age 55, however, if the employee separates from his employer under an early retirement plan. Distributions in the form

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[21] *Employee Benefits in Medium and Large Private Establishments*, Bulletin 2422 (Bureau of Labor Statistics, May 1993) and *Employee Benefits in Medium and Large Private Establishments*, Bulletin 2517 (Bureau of Labor Statistics, September 1999).

[22] *Employee Benefits in Small Private Establishments*, Bulletin 2388 (Bureau of Labor Statistics, September 1991) table 1, page 5; and *Employee Benefits in Small Private Establishments*, Bulletin 2507 (Bureau of Labor Statistics, April 1999), table 1, page 5.

of a lifelong annuity are permissible at any age. Some advocates of phased retirement arrangements have suggested that the minimum age for in-service distributions from defined contribution plans should be lowered to age 55.[23] The effect on labor force participation of such a change in tax policy would likely be very similar to the effect of allowing in-service distributions from a defined benefit plan at the plan's early retirement age. Some workers who might have fully retired from the labor force earlier than age 59½, so that they could begin taking distributions from the plan, would be induced to work longer. Others who would have taken early retirement and then sought work elsewhere would remain with their current employers, because they would be able to combine wages from part-time work with distributions from the retirement plan. Finally, some employees who otherwise would have chosen to continue working until age 59½ or later would reduce their work schedules and supplement their earnings with distributions from the retirement plan.

H.R. 4837 and S. 2853 of the 106th Congress, both titled the *Phased Retirement Liberalization Act* would have amended the Internal Revenue Code to permit in-service (preretirement) distributions from a defined benefit or defined contribution plan when the participant has either reached the plan's normal retirement age, reached age 59½, or has completed 30 years of service, whichever comes first. Currently, such distributions cannot be made from a defined benefit plan before the participant has reached the plan's normal retirement age or from a defined contribution plan before age 59½.

Flexibility versus nondiscrimination. Pension plans that provide benefits mainly to the owners of a firm or to highly paid employees do not qualify for favorable tax treatment under the Internal Revenue Code.[24] The tax code defines specific tests that must be applied to a pension plan to determine whether or not it meets these requirements for nondiscrimination in favor of highly compensated employees.[25] These tests consist mainly of mathematical computations of the percentage of plan participants who are highly compensated employees and the

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[23] It might also seem reasonable that if legislation were passed to allow in-service distributions from an employer's defined benefit plan at the plan's early retirement age, then distributions from the employer's defined contribution plan should be permitted at the same age (perhaps with a lower limit of 55). However, such a policy would suffer from at least two drawbacks. First, the minimum age for in-service distributions from defined contribution plans, which is now the same for all such plans, would differ from firm to firm, thus making the retirement planning process even more confusing for workers and their families. Second, it would be administratively difficult—and in some cases, perhaps, impossible—to tie the minimum age for in-service distributions in the defined contribution plan to the early retirement age specified in the employer's defined benefit plan.

[24] 26 U.S.C. § 401(a)(4) states that a qualified pension trust is one in which "the contributions or benefits provided under the plan do not discriminate in favor of highly compensated employees (within the meaning of section 414(q))." The term "highly-compensated employee" is defined at 26 U.S.C. § 414(q) as a person who is at least a 5-percent owner of the firm or is paid compensation of at least $85,000 and is among the top 20 percent of employees in the firm with respect to compensation.

[25] 26 U.S.C. § 410(b).

percentage of contributions to the plan or benefits paid by the plan that are made on behalf of highly compensated employees.

It is a relatively common practice for firms to establish separate nonqualified retirement plans for the company owners or senior executives. However, if a plan that was originally established as a tax-qualified plan is subsequently found to discriminate in terms of coverage or benefits in favor of highly compensated employees, it could lose its tax-qualified status. In most of these cases, the only viable options available to the plan sponsor would be to remove the discriminatory provisions of the plan or terminate the plan. Covering rank-and-file employees under a nonqualified plan usually would not be practical because of the substantial tax liability that would result for both the plan sponsor and plan participants.

In general, employers would prefer the flexibility to offer phased retirement to some—but not all—pension plan participants. Some analysts have suggested that, even if Congress were to amend the Internal Revenue Code to allow in-service distributions from pension plans before the normal retirement age, it would do little to spur the growth of phased retirement unless employers also were permitted to limit eligibility for this benefit to employees with particular skills or abilities. However, a phased retirement option that offered in-service distributions only to managerial or professional employees could result in the plan failing to meet the nondiscrimination requirements of the Internal Revenue Code by altering the distribution of benefits among plan participants in a way that favored the highly compensated group.[26] In contrast, a phased retirement option that offered in-service distributions to all participants meeting specified age and length-of-service requirements would not conflict with the IRC anti-discrimination requirements.

Section 410(b) of the Internal Revenue Code prescribes specific tests for determining if a pension plan's coverage or benefits discriminate in favor of highly compensated employees. These tests are mathematical calculations that reveal the proportion of plan participants who are highly compensated employees and the proportion of contributions or benefits that are made on behalf of highly compensated employees. Some plan sponsors who would like to implement phased retirement programs would prefer to have these tests for nondiscrimination replaced by the more subjective method of testing that was in effect until 1994, which was based on the "facts and circumstances" surrounding the operation of the plan. In some cases, a phased retirement option that fails the mathematical tests for nondiscrimination that are required under current law might not fail if it could be tested under the earlier (pre-1994) approach.

On May 2, 2001, the House of Representatives passed H.R. 10, the *Comprehensive Retirement Security and Pension Reform Act of 2001.* Among many other pension reforms, this bill would have authorized the Secretary of the Treasury

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[26] Employers whose approach to phased retirement does not affect eligibility for pension distributions are less likely to violate the IRC nondiscrimination provisions. Examples would be phased retirement plans that involve only reductions in hours of work, job sharing, transfers to other duties, or that are based on rehiring retired former employees. These are conditions of employment rather than characteristics of the pension plan.

in some cases to employ a test based on facts and circumstances in testing for nondiscrimination. A similar provision was included in S. 742, the *Retirement Security and Savings Act of 2001*. While many provisions of these two bills were incorporated in H.R. 1836, the *Economic Growth and Tax Relief Act of 2001* (P.L. 107-16), the sections dealing with flexibility in nondiscrimination testing were not included in the final version.

Policy Responses to an Aging Population

In a free market economy, individual employers decide how much compensation to offer and whether that compensation will include benefits like pensions and health insurance. Employees decide whether they will work, where they will work, and how much they will work at least in part on the basis of the compensation offered by prospective employers. The terms of these labor market transactions can be influenced through direct regulation—such as ERISA, the Age Discrimination in Employment Act, and minimum wage legislation—through social insurance programs—such as Social Security and Medicare—and through the financial incentives created for both employers and employees by the Internal Revenue Code. Social insurance programs and the tax code differ from direct regulation in that their primary objectives are, respectively, to provide benefits to individuals and to collect revenue for government operations. Nevertheless, both Social Security and the tax code affect the labor market behavior of employers and workers by establishing financial rewards or sanctions for certain actions. Given that the aging of the population and the impending retirement of the baby-boom generation are likely to affect the supply of labor and the productive capacity of the economy, both the Social Security Act and the tax code may be amended to provide incentives for people to work longer.

The rules that govern eligibility for Social Security benefits can have a substantial influence on workers' decisions about when to retire. Empirical evidence indicates that more retirements occur at age 62—the earliest age at which reduced retired worker benefits are available—and age 65—the earliest age at which full retired worker benefits are available—than at other ages. The "earnings test," which reduces benefits for some Social Security beneficiaries who work, and the "delayed retirement credit," which increases benefits for workers who defer their benefits until after age 65, also may influence one's decision to work (and how much to work) after becoming eligible for Social Security. At times, each of these provisions has been amended to provide greater incentives for individuals who are eligible for Social Security to continue working.

The *Social Security Amendments of 1983* mandated a gradual increase in the age at which individuals are eligible for full retirement benefits from its current level of 65 years to 67 years in 2022. As a result, the actuarial reduction in Social Security benefits for those who retire at 62 will increase from 20% to 30%, creating a financial incentive to delay receipt of Social Security and continue working. The 1983 amendments also provided for an increase in the delayed retirement credit for workers who defer their application for Social Security benefits until after age 65. In 1977, Congress set the DRC at 3 percent, meaning that benefits were permanently increased by 3% for each year that a worker delayed receipt of Social Security beyond age 65. The 1983 amendments provided for a gradual increase in the DRC beginning in 1990.

When fully phased-in, the DRC will be 8% per year for people who turn age 65 in 2008 or later, which will result in a DRC that is close to being "actuarially fair" for the average worker.

In April of 2000, the Social Security Act was amended to repeal the earnings test for beneficiaries who are 65 or older. As a result of Public Law 106–182, the earnings test has been eliminated for people at the full retirement age (currently 65 years) or older, effective January 1, 2000. The earnings test remains in effect, however, for beneficiaries who are under the full retirement age. In 2001, Social Security recipients under age 65 have their benefits reduced by $1 for each $2 of earnings in excess of $10,680.

Some employers are calling on Congress to amend the tax code to allow employers greater flexibility in designing phased retirement programs for their employees. One proposed amendment would permit pension in-service distributions to employees who have not reached the pension plan's normal retirement age. This, employers say, would allow them to offer older employees the chance to cut back their work schedules to part time, while supplementing their reduced salaries with pension income. Under current law, such an arrangement would be permissible only for plan participants who have reached the plan's normal retirement age.

Allowing in-service pension distributions to begin when a participant has reached the earliest of a plan's normal retirement age, age 59½ , or the completion of 30 years of service might promote continued employment among older workers who—if given the choice between working full time and taking early retirement—would otherwise have chosen to retire. A more complicated issue is whether employers should be permitted to offer such an option only to specific categories of workers.

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