TIAA-CREF institute

TRENDS AND ISSUES

Phased Retirement:
Often a Win-Win Situation

Mimi Lord, TIAA-CREF Institute

June 2005

TIAA CREF

FINANCIAL SERVICES
FOR THE GREATER GOOD℠

EXECUTIVE SUMMARY

Older faculty members wanting to reduce their work loads increasingly are interested in phased retirement plans, which allow them to ease into retirement and avoid an abrupt separation from their institutions. The terms of phased retirement plans vary from one institution to another, and it is extremely important for faculty members to understand exactly how their salaries, work responsibilities, current and future benefits will be affected before making a decision. This paper synthesizes some of the findings about phased retirement plans based on several papers written by TIAA-CREF Institute Fellows.

TABLE OF CONTENTS

Evolution of Phased Retirement Plans

As part of the 1986 amendments to the Age Discrimination in Employment Act (ADEA) prohibiting mandatory retirement ages for most workers, Congress permitted colleges and universities to continue requiring tenured faculty members to retire at age 70 until 1994. Beginning in 1994, institutions no longer could require retirement based on age.

Many institutions feared that after the end of mandatory retirement, substantial numbers of older faculty would remain employed beyond age 70, resulting in higher costs and reduced flexibility and resources to hire new faculty in growing fields. At the same time, there was increasing concern that a massive exodus of active faculty might occur once the baby boom generation neared typical retirement ages. Under that scenario, institutions would suffer from a lack of continuity and institutional memory. In short, institutions became faced with increasing uncertainty about the future composition of their faculty.

The Higher Education Amendments of 1998 further amended the ADEA to permit institutions to offer tenured faculty voluntary early retirement incentive plans that are in part age-based, so long as participants receive additional benefits for retiring early. The additional benefits may be reduced based on the age at which the faculty member opts to retire. However, the amendments emphasize that in no case can the faculty member's base retirement package be reduced.

The 1998 amendments provided institutions with clear authorization to implement voluntary early retirement incentives. Some institutions, concerned about the impending end of mandatory retirement, began to offer buyouts to faculty, typically consisting of a lump sum for those in defined contribution (DC) plans and of extra service credits for those in defined benefit (DB) plans. Buyouts generally are offered for a window of time and can be useful when staffing reductions need to occur quickly. Institutions interested in a permanent plan that would allow for more orderly retirement patterns began to implement phased retirement policies that provide administrators with more predictability about the nature and timing of retirements.

Prevalence of Phased Retirement Plans

Phased retirement programs are desirable to institutions by helping them develop better succession plans, minimize unfilled positions, and avoid buyout plans. In addition, many institutions consider them an important benefit to offer to faculty and a way to enhance continuity while encouraging faculty members to begin the transition to full retirement sooner than they would have without the phased program. Such plans also can be an effective incentive for keeping valued and productive faculty members working beyond the date at which they might have retired fully if no phased plan were in place.

The most comprehensive source of information about phased retirement plans is the Survey of Changes in Faculty Retirement Policies (SCFRP), conducted in 2000 by the American Association of University Professors with financial support from the TIAA-CREF Institute.[1] Results of the survey, canvassing nearly 1,500 institutions with 75 or more full-time faculty, indicated that 27% offer a formal phased retirement program. A much larger percentage of private institutions offer phased retirement programs than public institutions, 35% vs. 23%. Institutions conferring doctoral degrees are the most likely to provide phased retirement programs since they need to have orderly replacement of aging faculty to be competitive for graduate students and research contracts. Half of private doctoral institutions and 35% of public doctoral institutions provide them. Those with larger percentages of tenured faculty are more likely to offer phased retirement programs than those with smaller percentages of tenured faculty.

In the SCFRP report, Cornell University Professor and TIAA-CREF Institute Fellow Ronald Ehrenberg noted that institutions with DC retirement plans are twice as likely as those with DB plans to offer a phased retirement program. Reasons include:

- DB plans already have built-in, age-related retirement incentives that typically are offered to those meeting specified age levels and years of service; as a result, there is less need for their institutions to offer additional retirement incentives. The formulas of most DB plans are established so that the present value of the pension annuity is maximized when the individual becomes eligible for full retirement benefits. Depending upon the terms of the plan, choosing to participate in a phased retirement plan could postpone the initiation of the lifetime annuity, thus resulting in fewer years of receiving benefits.

- Since benefits in DB plans typically are linked to average salary levels during the final years of working, they do not easily lend themselves to phased retirement programs with significantly reduced work and salaries in the final years. Phasing individuals could forfeit valuable benefits unless the plan calculates benefits on highest annual salary levels or includes other accommodations for phased retirement.

---

[1] Ronald G. Ehrenberg, 2000, "Survey of Changes in Faculty Retirement Policies," The American Association of University Professors, http://www.aaup.org/Issues/retirement/retrpt.htm. Note that a new report with updated survey results, produced with funding from the TIAA-CREF Institute, will be available in late 2005.

- Phased retirement plans with DC plans are easier to implement because there is no link to salary levels. The value of the DC account is tied to investment performance, contributions, and length of investment horizon. Most institutions continue contributing to faculty DC accounts during phased retirement.

- DC plans generally offer greater flexibility for distributions than DB plans. Whereas some DB plans may not allow distributions until full retirement, DC plans allow phasing faculty to take retirement plan distributions to supplement their reduced salaries. Distributions before age 59 ½, however, may incur an IRS penalty of 10%.

Components of Phased Retirement Programs

Most phased retirement programs contain similar elements, although the specific terms and conditions vary. Institute Fellow David Leslie, chancellor professor of education at The College of William and Mary, lists 10 elements in a recent report, "Phasing Away: How Phased Retirement Works for College Faculty and Their Institutions."[2] The elements are listed below, along with data from Leslie's research and the SCFRP.

1. **Eligibility Requirements.** Most phased retirement programs require faculty to attain a certain age and number of service years to be eligible. The most common minimum age is 55, followed by 60, 50, and 52. The majority of programs have a minimum service requirement of 10 years, although significant numbers also require 15 and 20 years of service. Approximately 20% of programs have a *maximum* age of eligibility, most commonly 65 or 70.
2. **Tenure Status.** The majority of plans do not require faculty to relinquish tenure before they enter phased retirement, but faculty generally must lose their tenured status after three or five years of phased retirement.
3. **Notice.** Faculty planning to phase usually must provide notice of intent to retire at a certain time or a formal declaration of retirement.
4. **Participation Period.** The most common periods are three or five years, after which employment is terminated. However, the SCFRP indicates that 16.5% of institutions with phased retirement allow tenured faculty to remain in part-time status for as long as they want.
5. **Work Load.** Most commonly, the work load is reduced by a stated 50% in phased retirement programs. Frequently, the teaching load is cut in half and administrative duties are reduced by more than half. Often, the professor has the choice of working part-

[2] David W. Leslie and Natasha Janson, March 2005, "Phasing Away: How Phased Retirement Works for College Faculty and Their Institutions," a report funded by the Sloan Foundation, http://www.wm.edu/education/Faculty/Leslie/PhasingAwayBooklet.pdf.

time for the entire academic year, or working full-time for one semester and having the other semester off.

6. **Salary.** Salary is normally pro-rated according to work level, such as 50% pay for 50% work load. However, about 35% of institutions provide a premium, such as 60% pay for 50% work or balloon payments or bonuses upon completion of the phased period.
7. **Raises.** Some plans allow for merit increases during the phased period while others do not.
8. **Insurance.** The majority of institutions offering phased retirement continue to pay premiums for health, life, and disability insurance at the same rate as for the full-time faculty, according to Leslie's study. Looking specifically at health coverage, the SCFRP indicates that 80% of institutions with phased retirement programs continue to make full employer contributions to the health insurance program during the phased period. To qualify, a minimum level of work, such as half-time, may be required. For those retiring before the age of 65 when Medicare is available, the continuation of employer-provided health care coverage is a critical issue.
9. **Mutuality.** Most policies require that the institution and the individual mutually agree to the terms and conditions of the assignment.
10. **Pensions.** While most phased retirement plans prorate retirement contributions/credits during the phased period, the SCFRP found that 20% of the phased retirement programs provide additional retirement payments or credits. For those in DC systems, the institution may make contributions to the professor's retirement account based on more than his or her pro rata salary. For those in DB systems, the institution may add a full year of service credit toward retirement even though the faculty member is working only part-time.

Attractiveness of Phased Retirement Programs to Faculty

Faculty members in general are very dedicated to their work and derive high satisfaction from teaching, research, and interactions with colleagues. A recent survey of faculty aged 50 and above[3] revealed the following:

- Avg years in higher ed: 26
- Avg years at current institution: 20
- 84% tenured

[3] Jerry Berberet, Carole J. Bland, Betsy E. Brown, and Kelly R. Risbey, 2005, "Late Career Faculty Perceptions: Implications for Retirement Planning and Policymaking," TIAA-CREF Institute Research Dialogue 84, http://www.tiaa-crefinstitute.org/Publications/resdiags/latestiss.htm.

- Avg work hours per week: 57
- Overall high work satisfaction
- Avg planned retirement age: 66

The survey, led by TIAA-CREF Institute Fellow Jerry Berberet and supported by the Institute, found that older faculty members greatly appreciate the intellectual stimulation from their work as well the opportunities to make contributions to their institutions. They typically have been employed at their institution for many years and value the relationship highly. Their dissatisfactions generally relate to insufficient time for work, difficulty balancing teaching and research, and institutional "red tape." Rather than stopping work altogether, phased retirement allows them to continue the intellectual and social engagement with their institution but with significantly less time and administrative demands. Without a phased retirement program, an older faculty member's only option to reduce work load at his/her institution might be to retire and then become re-hired on a part-time basis, often at very unattractive pay. Alternatively, he/she might retire from the institution and accept part-time work elsewhere, a potential loss of talent and experience to his/her former employer.

Health care coverage is often cited as a critical aspect of the retirement decision. As health care costs have continued to out-pace inflation by a significant margin, more and more institutions, and particularly private institutions, are dropping their retiree health care plans.[4] Some institutions with retiree health coverage provide it only to pre-65 retirees and some provide it only to those aged 65 and older. Individuals working at institutions without retiree health coverage may need to keep working until age 65 when Medicare becomes available. If a phased retirement program that maintains health coverage is available, that can be a very attractive option for those wanting to scale back their work loads but needing to maintain health care insurance. In short, a phased retirement program that reduces work loads but maintains valuable benefits can be a win-win situation for employees.

Faculty Experience with Phased Retirement

In a study of the phased retirement program at the University of North Carolina (UNC), responses to the question about being "pleased with my participation in the Phased Retirement Program and would make the same decision again" were as follows:

[4] Sylvester J. Schieber, 2004, "The Outlook of Retiree Health Benefits in Higher Education in the United States," TIAA-CREF Institute's "Recruitment, Retention and Retirement" conference in NYC, April 2004, http://www.tiaa-crefinstitute.org/Publications/wkpapers/wp_pdfs/wp04-2004d.pdf.

Strongly agree:	60%
Agree:	33%
Disagree:	6%
Strongly disagree:	1%

Steven Allen, Professor of Business Management at North Carolina State University and a TIAA-CREF Institute Fellow, analyzed some of the study findings of the phased retirement program at UNC in a paper, "The Value of Phased Retirement."[5] For example, phasing faculty members at UNC are able to achieve income levels-- including salary, pension income, and Social Security-- at about 90% of their pre-phasing income. Forty-two percent indicated they had replaced 100% or more of their prior income level. Faculty members nearly always begin receiving pension benefits upon entering phased retirement at UNC.

Eighty-four percent of UNC phasing faculty reported that, without the phased program, they would have continued to work full-time for an average of 3.6 more years. Larger percentages of faculty chose phased retirement on campuses where the main mission is teaching than where the mission also includes research; this likely reflects the fact that phased retirement buys more free time on teaching campuses.

Phasing faculty at UNC were asked how they reallocate their time that previously was spent working. The following table indicates what percentage of phasing faculty report spending more time on certain specified activities:

More time in activities with friends, family and community:	67.7%
More time in research or other creative/scholarly activities:	42.7%
More time on volunteer activities and family assistance:	33.3%
More time working for pay off campus:	22.0%

Negative comments of participants in UNC's phased retirement program referred to the loss of on-campus amenities such as a private office, the inability to teach summer school, and the limited number of years for phasing.

[5] Steven G. Allen, 2004, "The Value of Phased Retirement," presented at the TIAA-CREF Institute's "Recruitment, Retention and Retirement" conference in NYC, April 2004, NBER Working No. 10531, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=552894. Note that a volume of papers presented at the conference will be published in Summer, 2005: Recruitment, Retention, and Retirement in Higher Education: Building and Managing the Faculty of the Future, 2005, edited by Robert L. Clark and Jennifer Ma, Edward Elgar Publishing, Cheltenham, UK and Northampton, MA, USA.

TIAA-CREF institute

06/05

TRENDS AND ISSUES

www.tiaa-crefinstitute.org

Summary

Many colleges and universities have developed phased retirement programs and other early retirement incentives as tools to help manage employment and retirement patterns following the end of mandatory retirement policies in 1994. Despite fears that substantial percentages of faculty might decide to keep working after age 70, most faculty continue to retire in the 65-66-year-old range. Those who keep working longer tend to be research-oriented faculty in doctoral/research institutions. From the faculty perspective, phased retirement programs provide them with an opportunity to reduce work loads while maintaining their intellectual pursuits and collegial affiliation with their institutions. Faculty choosing to phase often enjoy increases in salary and other benefits that are beyond the pro rata levels of their reduced work load. Before making a decision to phase, however, faculty need to fully understand and agree to the components of their particular institution's program.

Additional Information

http://www.wm.edu/education/Faculty/Leslie/PhasingAwayBooklet.pdf

www.aaup.org/Issues/retirement/retrpt.htm

http://www.tiaa-crefinstitute.org/Grants/pdfs/wp01-01.pdf

http://www.tiaa-crefinstitute.org/Publications/resdiags/latestiss.htm

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=552894