



GROWING PENSION INEQUALITY

Workers who don't participate in a voluntary retirement plan face a significantly higher risk of a financially insecure retirement.

The answer to the question, "Is Pension Inequality Growing?" is an unqualified "Yes," according to research published by Nadia Karamcheva and Geoffrey Sanzenbacher. What they mean by inequality in this context is a wide range in the percentage of retirement income that retired workers receive from a pension (as opposed to other sources of retirement income, such as personal savings and Social Security). It ranges from a high of 31% for some recipients in the population they studied to just 3% for others.

They find this inequality particularly worrisome since, as they remind us, pension income often makes the difference between a comfortable retirement and years of struggling to make ends meet. In fact, the authors conclude, the majority — 60% — of the group receiving the lowest percentage of retirement income from a pension is at risk of having less retirement income than they need overall.

REDUCED PARTICIPATION

In examining the reasons for this disparity in pension income, Karamcheva and Sanzenbacher point to a drop in the rate at which certain workers participate in employer-sponsored retirement plans. (Participation rates are determined by multiplying the percentage of people with access to a pension plan times the percentage of those who enroll.)

Unsurprisingly, those workers who ended up with the smallest pensions after they retired were the ones who elected not to participate.

The main reason for failure to participate, the authors conclude, is the change in the pension landscape since 1979. Specifically, defined contribution pensions that require employee contributions and have optional

→ A QUICK LOOK

- 60% of retired workers are at risk of having less income in retirement than they need to live comfortably
- Many of these now-retired workers didn't participate in an employer-sponsored retirement plan when one was available to them
- Having too little money is the primary reason these non-participants did not contribute to a 403(b) or similar plan.
- Since 1979, there's been a major shift to defined contribution plans from defined benefit plans

enrollment have replaced defined benefit pensions in which participation is mandatory for qualifying workers and the employer makes the entire contribution.

The authors further point out that when enrollment is optional, workers whose income falls below the median income level participate at significantly lower rates. In 2007, for example, 96% of higher-income employees and 78% of lower-income employees participated in a defined benefit plan offered by their employers. In most cases, those who did not participate were either too young to be included or had not been at the job long enough to be enrolled. In contrast, when a defined contribution plan was offered, the participation rate dropped to 83% of higher-income workers and just 41% of lower-income workers.

IDENTIFYING THE CAUSES

The factors that contribute to this lack of participation, in the view of the authors, are too little knowledge about the importance of retirement savings and too little money, especially the latter. Using data from the U.S. Census Bureau *Survey of Income and Program*

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Participation (2007), they found that the primary reason lower-income earners gave for not enrolling in a 403(b) or similar plan was not being able to afford to defer income.

That helps to explain why, although automatic enrollment in salary reduction plans can increase participation by as much as 35% overall, it doesn't increase participation for people who say that money is the reason they don't enroll. This group is more likely to exercise their right to opt out if they are automatically enrolled.

Karamcheva and Sanzenbacher don't offer a solution to the problem of growing pension inequality, despite the fact that participation in a pension plan "could help these most vulnerable individuals achieve an adequate retirement." But they make it clear that the type of

retirement plan that could decrease the disparity in participation rates is one where participation is mandatory and the employer contribution is a substantial portion, if not all, of the funding for the plan.

Unfortunately, the authors do not provide specific income ranges to define the categories such as "higher income" and "lower income" which they use to differentiate groups of workers and retired workers. But to put those descriptors in perspective, the data collected by the US Bureau of Labor Statistics and the US Census Bureau and published in the 2008 Current Population Survey, which is their source, places people over 65 with incomes of \$33,677 in the highest income quartile and those with incomes under \$11,139 in the lowest income quartile.

The study, "Is Pension Inequality Growing?" was written by Nadia Karamcheva and Geoffrey Sanzenberger and published by the Center for Retirement Research at Boston College in January 2010. It examines trends in pension sponsorship and participation rates by income level, using data from the U.S. Bureau of Labor Statistics and the U.S. Census Bureau.