Focus on Workplace Flexibility
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EXECUTIVE SUMMARY

Phased Retirement and Workplace Flexibility for Older Adults: Opportunities and Challenges

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Providing older employees with flexible work options could encourage them to work longer and delay retirement. As workers approach traditional retirement ages, they often prefer to reduce their hours, shift into less demanding positions, and work flexible schedules, especially if they have accumulated substantial savings or can access retirement benefits so they can afford the pay reductions that usually accompany downshifting. The inclination toward workplace flexibility is often driven by emerging personal obligations (such as the need to care for frail parents, disabled spouses, or young grandchildren), worsening health, declining physical energy, or a growing preference for more leisure after a lifetime of work.

Retaining older workers provides important benefits to employers. The organization loses valuable skills, experience, and accumulated knowledge when seasoned workers and managers retire, attributes that are often difficult to replace from within and sometimes impossible to bring in from the outside. The retention of senior talent is becoming increasingly critical as the population ages. Unless older adults work more, the slow growth in the size of the younger population will lead to a stagnant labor force, making it increasingly difficult for employers to meet their staffing needs and limiting economic growth.

Phased retirement programs that allow older workers to reduce their hours and responsibilities and pursue more flexible work schedules could satisfy both the employee's desire for flexibility and the employer's need to maintain an experienced workforce. However, few employers have established formal programs, because they often complicate the provision of other benefits and might violate anti-discrimination rules.

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- Federal laws and regulations limit retirement plan distributions to employees who are still working for the plan provider, which discourages phased retirement because few older workers can afford to reduce their work hours unless they can receive at least some retirement benefits. Participants in defined contribution retirement plans (such as 401(k)s) are not allowed to access their retirement accounts while still working for the employer until age 59 and one-half. Workers in defined benefit (DB) pension plans — the traditional plans that typically pay retirement benefits based on earnings and years of service — are generally forbidden from receiving in-service distributions before age 62. Before 2007, they could not receive in-service distributions before the plan's normal retirement age, which varies across plans but is often 65.
- Phased retirees in DB pension plans who are not collecting pension benefits often lose significant pension wealth when they move to part-time employment, because benefits are typically tied to earnings near the end of the career (such as the last three or five years). These losses discourage phased retirement.
- Instead of phasing from full-time employment to part-time work, retirees can leave the employer and return as independent contractors or consultants, allowing them to collect pension or retirement benefits. However, they might have to wait several months before returning to the original employer.
- Phased retirement can also jeopardize health and other benefits, because many employers do not provide fringe benefits to part-time employees. Making exceptions for older workers could violate anti-discrimination rules.

- Federal rules require that benefits provided through tax-qualified plans be fairly evenly distributed between highly compensated and lower-paid employees. It is difficult for many formal phased retirement programs to meet these standards because most employers gear them toward well-paid workers, who tend to have the specialized skills and knowledge that employers value and who can generally afford to reduce their work schedules.
- Federal law forbids employment discrimination on the basis of age against workers 40 and older. Employers tend to be selective about the employees to which they offer phased retirement, and those denied enrollment in the program may sue on grounds of age discrimination. Even if these claims would be difficult to prove, the threat of expensive litigation may discourage many employers from implementing phased retirement programs.

Several policy reforms could promote phased retirement, but many of these changes would conflict with other policy objectives. For example, pension law could be changed to allow employers to grant in-service DB plan distributions to employees younger than 62, but that would undermine the notion that pension benefits go only to retirees. Such a change could also encourage some workers to collect benefits early, permanently reducing their annual benefits for the rest of their lives. Congress could weaken or eliminate the so-called benefits, rights, and features test for phased retirement plans mandating that enrollees include both highly compensated and non-highly compensated employees. This change, however, could leave relatively few lower-paid older workers with access to flexible work arrangements. Congress could state that the age discrimination law does not apply to phased retirement programs, but that would weaken employment protections and could expose some older workers to discriminatory behavior.