

TASK 3: TRENDS IN PENSION CASH-OUT AT JOB SEPARATION AND THE EFFECTS ON LONG-TERM OUTCOMES

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FINAL REPORT

Trends in Pension Cash-out of Older Workers at Job Separation and the Effects on Long-term Outcomes

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Abstract

Might the financial security of working Americans during retirement be jeopardized by their ability to cash out their pension plans when they leave a job? Federal tax rules discourage such actions, but the limited evidence available suggests the practice is common. This paper takes advantage of long-term longitudinal data in the Health and Retirement Study to update prior findings, investigate cohort differences and study the long-term consequences of pension cash-out at job separation. We find that pension cash-out is more concentrated among workers who experience economic or health shocks around the time of job separation. The most recent cohort of older workers more often cashed out pension balances and more frequently used the balances for spending or to pay off debt. This is likely due to most of the job separations for this cohort occurring during or in the aftermath of the Great Recession, which brought about economic shocks at higher frequency. Long-term outcomes for those who cashed out pension balances are worse than for those who did not cash out, but so were their baseline characteristics. Taking this together with the fact that outcomes are largely similar across populations of workers with or without access to pension cash-out, we conclude that the worse outcomes among workers who cashed out are due to the experience of shocks leading to cash-out behavior rather than due to access to the cash-out option.

Keywords:

Pensions, financial security, retirement resources, economic shocks, health shocks

INTRODUCTION

Promoting financial security in retirement is a major objective of U.S. policies governing employer-provided pensions. To encourage workers and employers to participate, legislation mandates very large tax advantages for private-pension savings. These effectively represent “tax expenditures” to the federal government in the form of forgone tax revenues.

U.S. policymakers have a substantial interest in the results of these large expenditures for promoting financial security in retirement. Is the private-pension system effectively enhancing financial security in retirement? What are the barriers or impediments to achieving economic security for old age among U.S. workers? Which groups of workers are at greatest risk of falling short?

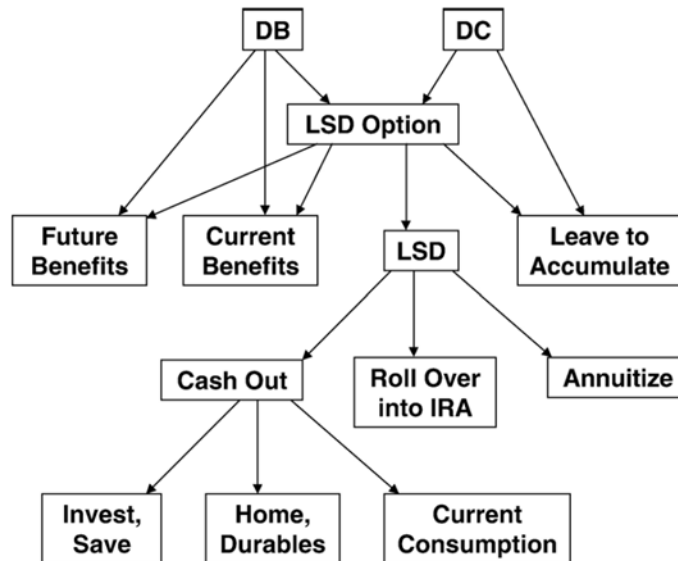
One feature of the U.S. pension system in particular may jeopardize the objective of promoting retirement-income security: the ability of workers to cash out (i.e., withdraw funds from) their private-pension plans upon job separation. Federal rules aim to discourage such pre-retirement cash-outs. For example, the Tax Reform Act of 1986 introduced a 10 percent tax penalty on withdrawals from tax-advantaged accounts prior to the age of 59 ½. Burman et al. (2012) showed that this tax penalty reduced pre-retirement cash-out of pension balances and increased rollovers into individual retirement accounts that preserve the tax-advantaged status of the pension balances. They also found reductions of cash-outs in response to a 1992 reform that imposed 20 percent tax withholding (without affecting the total tax liability). These policy changes have reduced, but not eliminated, early withdrawals. Several studies have investigated the causes of the remaining early pension withdrawals. It appears that a significant portion of these are made by households facing liquidity constraints and experiencing financial shocks (Amromin and Smith, 2003; Scherpf, 2010). Still, according to Butrica et al. (2010), about half of early withdrawals from 401(k) defined-contribution pension accounts and Individual Retirement Accounts (IRAs) could not be attributed to the events observed in the data, possibly indicating “unnecessary loss of retirement savings.”

This paper uses the long panel of data collected in the Health and Retirement Study (HRS), spanning up to 20 years for the earliest cohorts, to add new insights to prior research findings on this topic. Analyses in the current study address trends in pension cash-outs among older workers, cohort differences, and

retirement income security metrics at later years or ages and their relations to earlier job and cash-out choices. We did not restrict ourselves to looking at single cash-out actions but incorporated cumulative measures of pension cash-out decisions. The paper includes analyses of precipitating events that shed light on determinants of cash-out behavior and how it may have changed over time. We were especially interested in how the Great Recession affected cash-out choices. The HRS data permitted an analysis of the relationship between the variation in cash-out choices of older workers to a variety of outcomes observed in panel up to 20 years later, including assets, income and health.

In an antecedent to this paper, Hurd and Panis (2006) analyzed HRS data on cash-outs and other dispositions of pension entitlements among workers over the age of 50 who left their jobs between 1992 and 2000 (five waves of biennial HRS data). Their study highlighted an issue that had been underappreciated in prior research: whether a lump-sum distribution (LSD) harms retirement preparation depends critically on what the worker does with the money. Some LSDs may be rolled into an IRA, some may be annuitized, and some may be cashed out. Although the first and second outcomes carry with them the loss of ERISA protections, only the last of these fully removes savings from retirement investment vehicles, and even then some uses may function as savings. Hurd and Panis used the following graphic to clarify the situation. In the cash-out branch, some of the funds may be invested or saved directly and some may be invested in the home, which is a form of saving. While bringing such funds out of tax-sheltered accounts may not be optimal tax management, it is primarily spending for current consumption among those not facing binding credit constraints that poses the greatest harm to economic preparation for retirement.

Potential options for the disposition of pension entitlements, as illustrated in Hurd and Panis (2006):



Hurd and Panis established several facts that are important for understanding the causes and consequences of LSD decisions. Not all plans allow an LSD on job separation. In fact, the availability of LSDs varies dramatically across types of plans: a little over 80% of DC plan participants report an LSD option, versus just 42% of DB plan participants. This 80% figure may be an underestimate. The HRS question about the availability of an LSD does not distinguish between the employer contribution to a DC plan and an employee contribution (which can always be cashed out), and a worker may be thinking just of the employer contribution. Further the HRS data are recorded prior to job separation, yet worker knowledge of plan details is likely to be greatest when a decision about pension receipt must be made (at job separation). Some workers may misreport plan type with the implication that some of the apparent DC plans are in fact DB plans where the rate of LSD option is, indeed, lower than 80%. See Hurd and Panis (2006) for a further discussion of classification and reporting error with respect to pension types in the HRS.

Besides looking at the fraction of workers who cashed out their pensions, Hurd and Panis examined the implications of cash-outs for aggregate pension balances and net wealth, including non-retirement wealth. They identified two factors that implied a limited overall impact of cash-outs on retirement and total household wealth. First, cashed-out plans had lower average value than other plans, especially

among those holding DC plans. Second, over 75% of cashed-out funds were either invested or used to pay off debt. Hurd and Panis conclude that “among workers that are within roughly 10 years of retirement, only a small fraction of pension plan dollars is consumed immediately after job separation and that the vast majority is preserved for retirement income security.”

While the Hurd and Panis paper provided a useful perspective up through the year 2000, the demographic and pension landscape has changed considerably with the decreasing importance of DB plans, the increasing pension entitlement of women, and changing trends in marriage and divorce. Furthermore, the Great Recession may have led to more cash-outs, harming particular segments of the population. These changes in the landscape warrant revisiting the Hurd and Panis analysis, which is the objective of this paper.

DATA

The HRS is a biennial longitudinal survey of persons at least 50 years of age. Since its launch in 1992, the HRS has gathered data on income, work, assets, pension plans, health insurance, disability, physical health and functioning, cognitive functioning, and health-care expenditures, among other topics. Periodic additions of cohorts ensure the HRS remains representative of the population at least 50 years of age.

The analyses in this paper are focused on several key variables. We analyzed self-reported data on employer-provided pensions for HRS respondents. The HRS asks whether respondents own such a pension, and whether it is a defined-benefit (DB) or a defined-contribution (DC) plan. It also asks respondents whether the pension plan allows for a lump-sum distribution. They are asked about the disposition of the pension plan at job separation or retirement: whether it was left with the former employer to accumulate; whether a full or partial LSD was taken; whether DB holders started drawing benefits on separation or chose to await future, larger benefits; whether the pension plan was lost with separation (likely where there is lack of vesting); or whether some other disposition occurred. For those who took an LSD, the survey asks whether the money was rolled into an IRA, converted to an annuity, or cashed out. For those who cashed out their pension plan, the HRS asks whether the money was saved

or invested, whether it was used to pay off debt¹ or to purchase durable goods or a home, or whether it was used for non-durable consumption.

This research updates and expands that of Hurd and Panis in several directions. First, more waves of the HRS are now available. Hurd and Panis used five waves of HRS data from 1992 through 2000. Since then, six more waves of HRS surveys—from 2002 through 2012—have been conducted and the data made available for analysis, bringing not only an increase in sample size, but also an expansion in the types of analyses that could be conducted. In particular, because additional waves of data became available, differences across cohorts (e.g., those born before World War II and post-war “Baby Boom” cohorts) could be analyzed. A growing number of DC plans is also available for analysis, partly because of the time elapsed since 2000, but perhaps more importantly because DC plans have become increasingly prevalent in the U.S. pension system, so workers in more recent cohorts are more likely to have them.

More recent cohorts are also likely to consist of more women who have earned pension entitlements at work. Their decisions regarding pension wealth may differ from those of men and merit additional analysis. Indeed, within a household, the behavior of both spouses is important in determining use or disposal of pension assets. The incorporation of more waves of HRS data with more female respondents who hold pension wealth promotes the analysis of pension wealth and its use or disposal from a household perspective.

The analysis has been updated to provide insights on the effects of the Great Recession on pension behavior, particularly on cash-outs. The earlier work by Hurd and Panis studied a period of relatively low unemployment and high stock market and housing returns. The years since then, particularly those surrounding the Great Recession that began in 2008, have not been as favorable. Unemployment in 2009 reached 10 percent, more than two percentage points higher than it was at any point between 1992 and 2000, and more than double what it was in the late 1990s. Though eventually recovering, the U.S. stock market lost about half its value during the Great Recession, and housing values decreased by more than one-third, representing a large shock to wealth that may have led some workers to cash out

¹ Paying off debt is conceptually the same as investing or saving the money when considering net asset levels, but debt reduction may lead to future excessive spending, so we track it separately.

their pensions. Indeed, using tax data on pre-retirement withdrawals, Argento et al. (2014) verified that workers substantially increased withdrawal rates between 2004 and 2010, especially after 2007.

The long HRS panel supports analyses of retirement security outcomes at later years or ages and how they relate to earlier job and cash-out choices. For example, consider a 57-year-old worker who cashed out a pension between 1992 and 1994. We have been able to observe that worker's subsequent economic position at age 75 in 2012, and to compare that worker with otherwise similar workers who did not cash out.

By gaining access to more years of data, we were able to analyze and compare a broader array of events precipitating cash-out, including whether different precipitating events led to differences in subsequent events. We were able, for example, to analyze and compare cash-outs resulting from adverse health changes, unemployment, shocks to household wealth caused by the Great Recession, marital disruption, and extractions to buy real estate during the housing bubble of 2004 to 2008 and the subsequent loss of equity and, possibly, home ownership during the Great Recession.

Changes in the Macroeconomic Environment, 1992-2012

We begin with an overview of the contextual changes occurring over the period 1992-2012. The first half of that period covers the HRS waves available to Hurd and Panis in conducting their analysis, and the second half folds in the years covered by the current work. We specifically focus on labor force participation (LFP) and the recessions that characterized the macroeconomy near the beginning and towards the end of the period of interest.

Labor Force Participation

Using Current Population Survey (CPS) data, we examined trends in LFP by sex. As shown in Figure 1, between the early 1990s and the early 2010s, LFP among males aged 65-69 increased substantially, whereas LFP among males 40-54 decreased slightly. Men of intermediate age (55-64) increased their LFPs modestly if at all. LFPs among older women (Figure 2), aged 55-69, increased at rates matching those of the oldest men in the analysis, although there appears to have been a leveling off following the

start of the Great Recession. LFPs among women in their 40s exhibited a slight increase or stasis until around the turn of the century and a slight downward trend thereafter.

Clearly, the most dramatic trends are the LFP increases among older men and women. These increases reflect trends toward later retirement. In the descriptive analyses which compare cohorts over eight years, we thus expect to see trends toward relatively fewer separations due to retirement, which may alter the frequency of pension cash-outs.

Figure 1: Labor Force Participation, Men

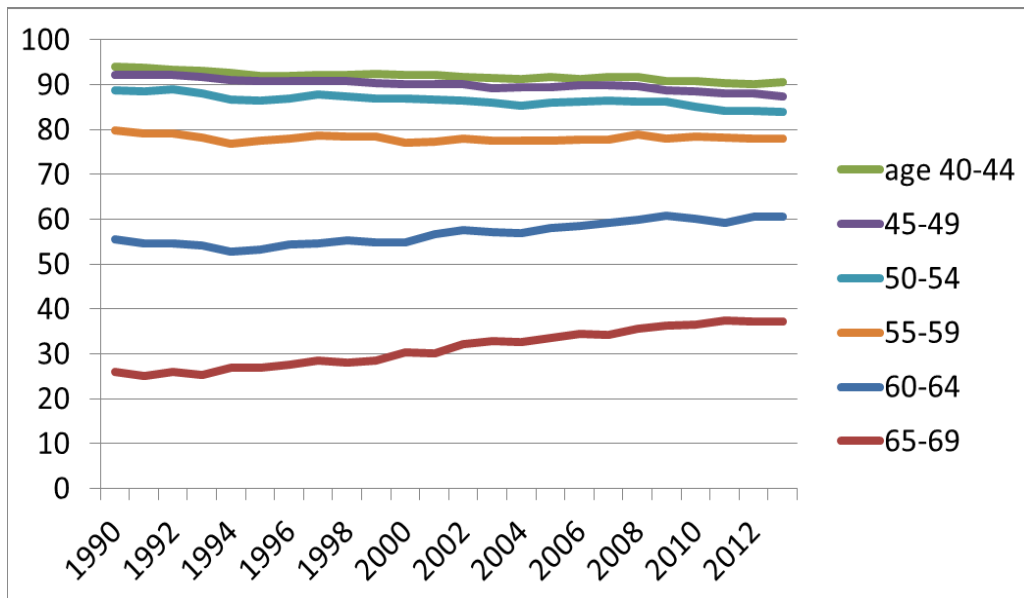
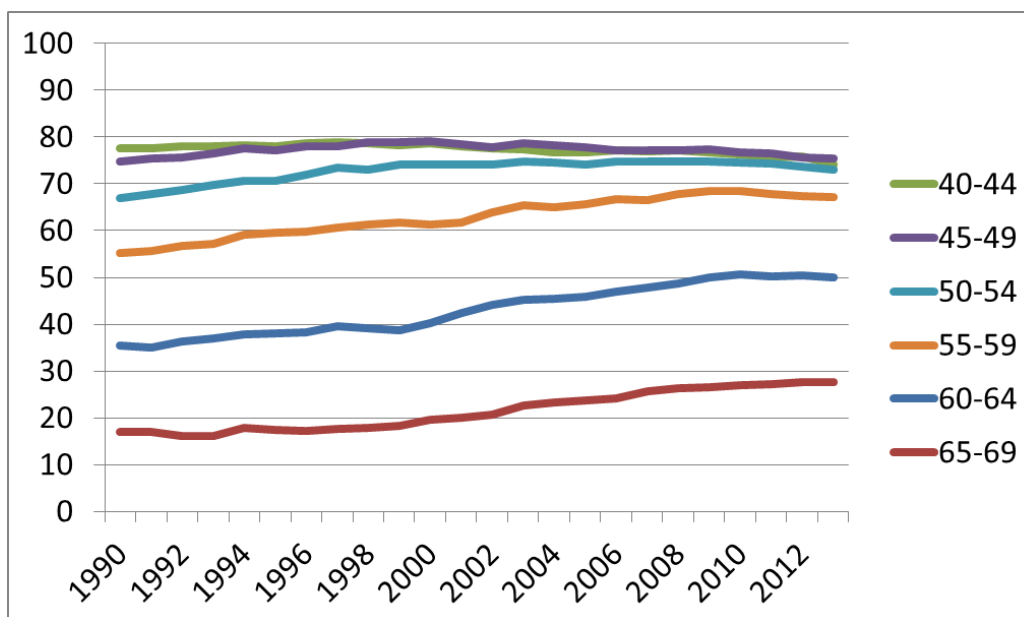


Figure 2: Labor Force Participation, Women



Macroeconomic Conditions

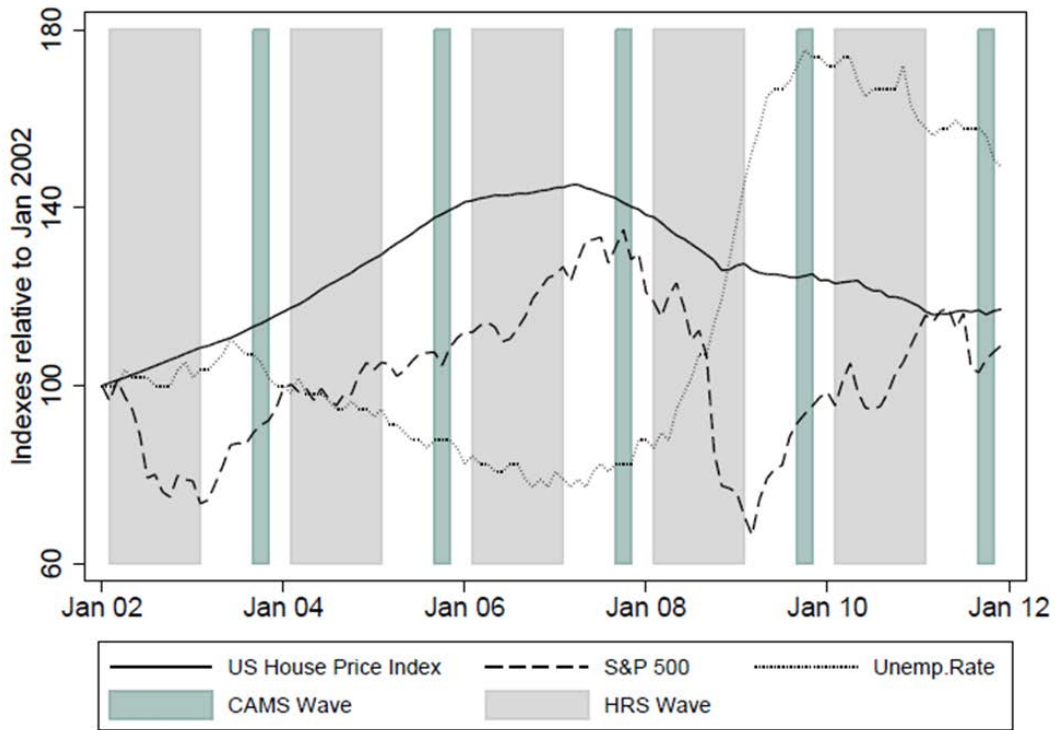
We are here concerned with the recession of 1991 and the Great Recession beginning in 2008. They are of interest because a recession is characterized by unemployment and adverse financial outcomes—loss of income, loss of assets including the value of stocks and real property. Involuntary job losses could trigger pension cash-out particularly when accompanied by wealth losses.

Recession of 1991. Unemployment, which had been falling in the late 1980s, from around 7.5% to 5%, turned around with the recession to exceed 7% again in 1992 (all figures seasonally adjusted). Stocks simultaneously dropped in value; the Standard & Poor's 500 index lost some 15% of its worth in 1991. Value of housing was not so dramatically affected. The Case-Shiller 20-City Composite Home Price Index, an index measuring residential real estate prices in 20 large American metropolitan areas, had been falling for several years and bottomed out in 1991. (The Federal Housing Finance Agency's house price index showed no movement, but had just been established.)

Great Recession. While changes in macroeconomic indexes were noticeable in 1991, they were much more dramatic for the Great Recession that began in 2008 (see Figure 3). The unemployment rate had been falling for several years, to 4.3%, or down about 20% since 2002. In the second half of 2007 it began rising and continued doing so very rapidly until the end of 2009, when it topped out at more than 10%.

The Standard & Poor's 500 index had been rising since 2003, making up some losses from 2002 and eventually reaching some 35% over the 2002 datum. It then plummeted through 2008, losing more than half its value. The FHFA's U.S. house price index had increased dramatically, by about 40%, between 2002 and the middle of 2007. It then began a long downturn that by early 2011, when it leveled off, had lost almost half of the gain.

Figure 3: Fluctuations in U.S. House Prices, the S&P500 and the Unemployment Rate



RESULTS

Cohort Comparisons

Table 1 defines the cohorts and shows sample sizes. For example, we follow as Group 1 the 5,355 people who entered the HRS with the 1992 wave of data collection. Of these 5,355 persons, 3,871 were working at entry, 2,161 were working with pension coverage, and 1,396 were working and covered by a pension plan allowing a lump sum distribution (LSD). We follow these groups for 8 years, as their participants age from 51-56 up to 59-64. Group 4 only entered in 2010, so insufficient time has elapsed for a longitudinal analysis; we use this group for baseline comparisons only.

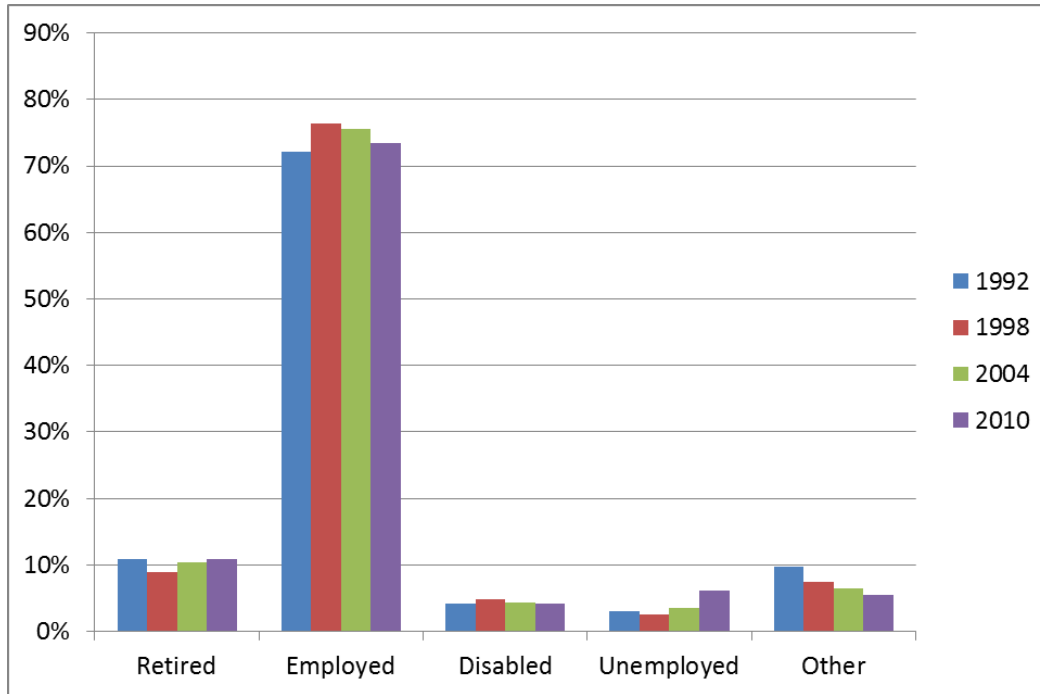
Table 1. Sample sizes of four groups used in analyses

	Initial year observed in HRS	Sample Size			
		Age 51-56	Age 51-56 and Working	Age 51-56 and Working with Pension Coverage	Age 51-56 and Working with Pension Coverage allowing LSD Option
Group 1	1992	5,355	3,871	2,161	1,396
Group 2	1998	3,209	2,402	1,401	878
Group 3	2004	3,322	2,477	1,417	908
Group 4	2010	4,690	3,172	1,688	1,144

Baseline Comparisons

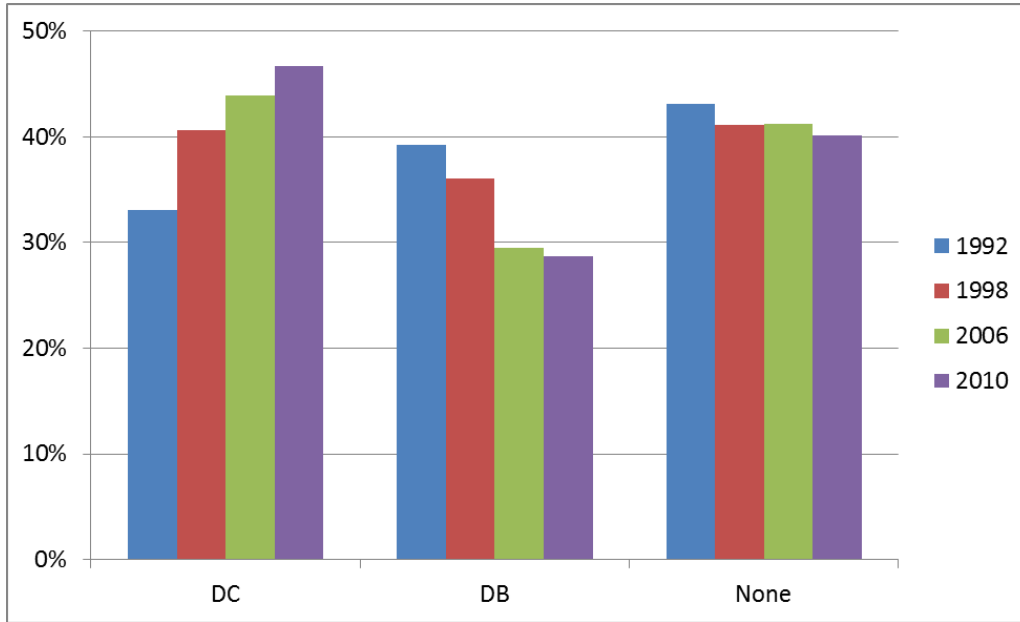
Labor force status. Figure 4 shows labor force status at ages 51-56, as reported by the respondents in each group. Employment was lower in 1992 and 2010, and unemployment higher, particularly in 2010, reflecting the Great Recession.

Figure 4: Labor Force Status at Age 51-56



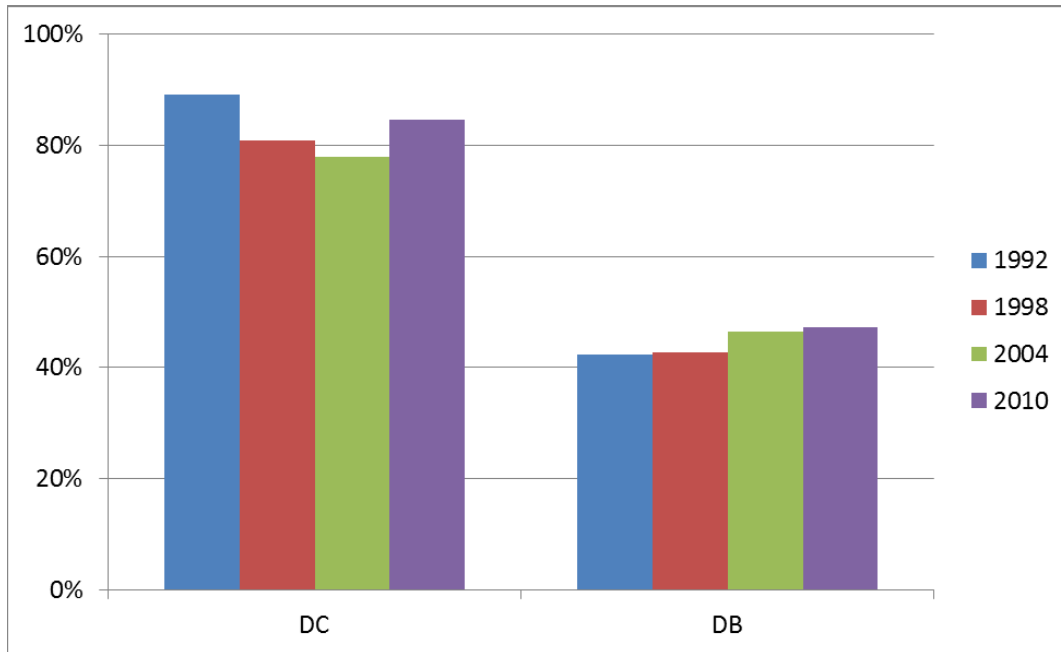
Pension coverage and plan type. Pension coverage improved modestly over the period of interest (see Figure 5), increasing a few percentage points to a 60% coverage rate in 2010. There was a large change in the *type* of coverage, though. Most respondents who had pensions were covered by defined-benefit (DB) plans, versus defined-contribution (DC) plans in 1992. By 1998, that pattern switched around. The trend from DB to DC still continues.

Figure 5: Pension Coverage and Plan Type, Conditional on Working



The great majority—over 80%—of persons having a DC pension plan report being allowed by the plan to cash out via an LSD (see Figure 6). The like percentage for DB plans is 47% in 2010, which represents a steady but modest increase since 1992. In reality the fraction having a DC plan that allows cashing out is likely to be higher, because virtually all DC plans allow cashing out at least part of the plan balance. The discrepancy with respondents’ reports shows that there is reporting error in the data in plan type, and in the information about cash-out options.

Figure 6: Pension Plan Allows LSD, Conditional on Work & Pension on Job



Longitudinal Comparisons

Job separations. Table 2 lists the number of job separations within HRS cohorts between their entry year (1992, 1998, or 2004, when they were 51-56 years old) and 8 years later (when they were 59-64). These can be separations to another job, to unemployment, to retirement, or to any other employment status category. They also include separations by individuals not having a job at entry into the HRS who later take a job and then separate from that job, and they count multiple separations per individual where those occur.

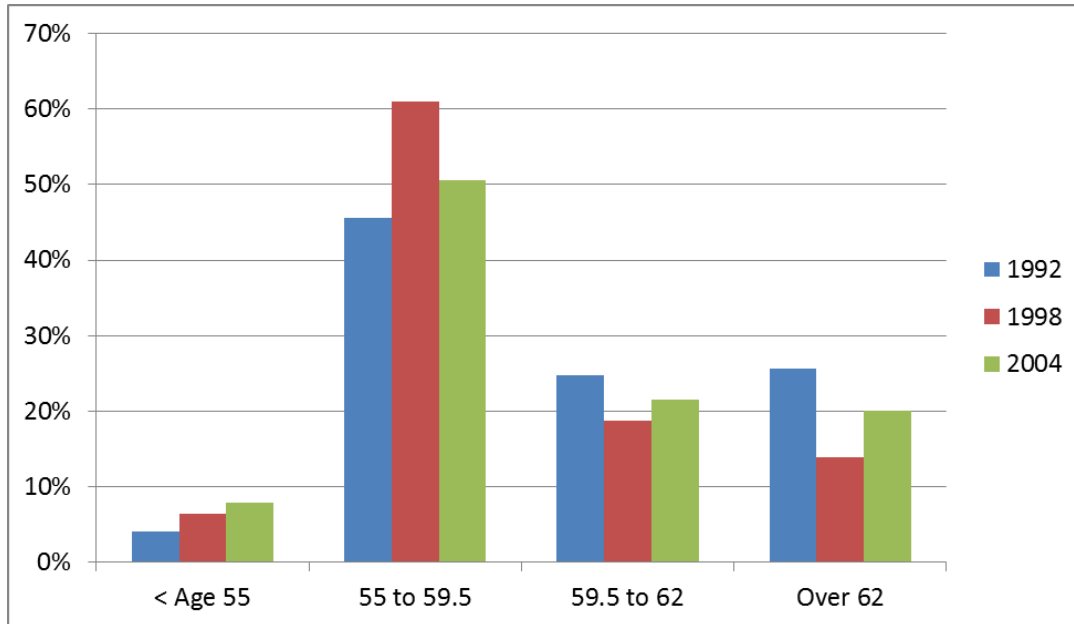
Table 2. Number of persons with job separations over eight years

Cohort	ALL # individuals with one or more job separations	# individuals with any separations from a job with a pension plan	# individuals with any separations from a job with a pension and cash-out option
1992	2,067	1,204	731
1998	1,386	901	567
2004	1,319	738	528

Separation counts are larger for 1992 because the HRS cohort was larger.

We sought trends in age at separation and in labor force status following job separation among respondents with pensions. Figure 7 shows the age at which cash-outs occur, where each cash-out that occurred is counted equally; if an individual cashed out multiple times, each time in a different age group, each cash-out would add to its respective age group. The plurality of cash-outs appear to happen around ages 59/60, the age at which tax penalties for early withdrawals end.²

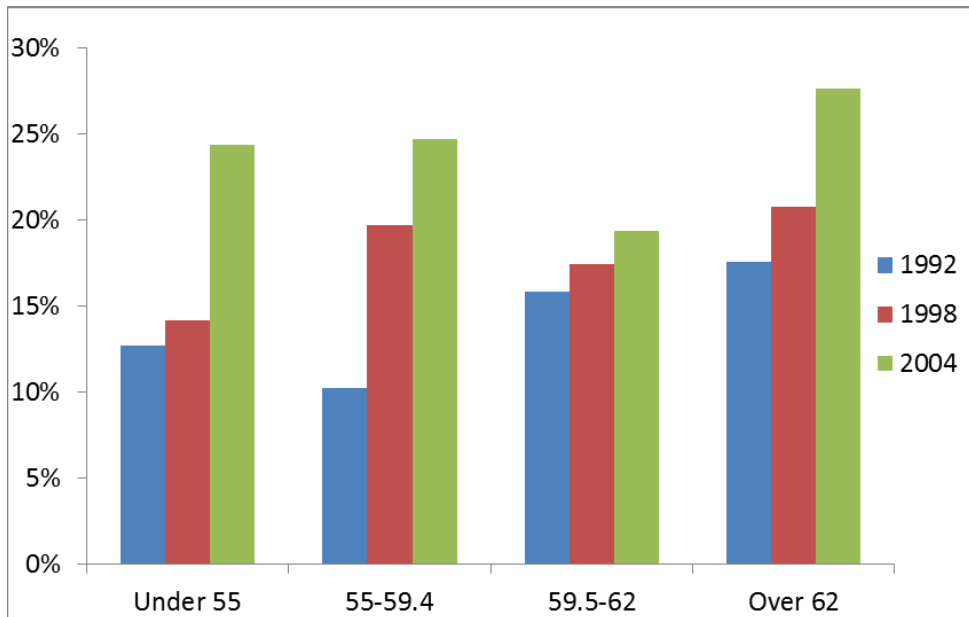
Figure 7: Age Distribution of Individuals at Time of Cash-Out, Both DB and DC



However, the apparent concentration of cash-outs for those around age 59/60 stems from the greater frequency of job separations at this age. Figure 7a, on the other hand, shows the likelihood of cashing out a DC plan within age groups, given separation from a job with DC pension entitlement. This comparison shows little evidence of any differences in the propensity of cash-out across ages, and also demonstrates that the greater propensity to cash out among later cohorts holds across the age groups studied.

² Although employer-provided DC plans such as 401(k)'s allow for a penalty-free withdrawal at age 55 if a worker is separating from their employment, Figure 7a does not show any observable increase in the propensity to cash-out a DC plan when comparing workers separating at age 54 versus age 55.

Figure 7a: Among Separations from DC Plans, Fraction that Includes a Cash-Out, by Age Group



There were substantial differences by cohort in labor force status after job separation (see Figure 8).

The 2004 cohort (group 3) was more likely to be unemployed than the other two cohorts, whereas the 1992 cohort was much more likely to retire after a job separation.

Figure 8: Labor Force Status After Job Separation

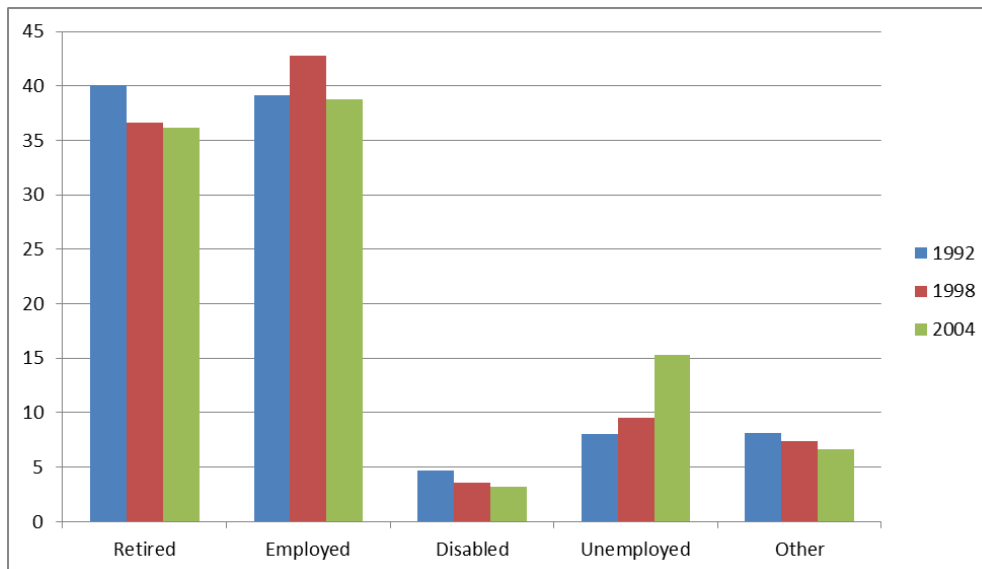


Table 3 shows the number of job separations over 8 years among respondents covered by a pension plan, classified by whether the individual had a DC or DB plan. For example, there were 637 job separations among persons with DC plans, and those amounted to 44.8% of all job separations involving a pension plan. The table documents sharp increases in the percentage of respondents with pension plan coverage who have a DC plan, and sharp decreases in the percentage with a DB plan. (Note, some persons have both types of plan, so the row totals exceed 100%.)

Table 3. Job separations among those with a pension: number and % by plan type

Cohort	Any DC		Any DB	
	% with DC	N with DC	% with DB	N with DB
1992	44.8%	637	67.9%	956
1998	57.4%	614	62.5%	642
2004	70.1%	591	46.6%	400

As the prevalence of DC plans was changing over the period of interest, so was the means of disposition of these plans at job separation (see Table 4). Cash-outs increased sharply from less than 14% to 24% (not conditioned on LSD availability), while rates of rolling plan assets into IRAs remained high, at around 30 to 40%. While cash-outs may be the principal worry from the retirement security point of view, IRAs do not necessarily protect savings well. These funds are no longer under the protection of the Employee Retirement Income Security Act (ERISA), and transfers to IRAs may presage spending.

Table 4. Cohort comparison: pension disposition of DC plans at job separation (over 8 years)

	Cohort		
	1992	1998	2004
Cashed Out	13.6%	19.0%	24.0%
Rolled over into IRA	35.1%	31.6%	40.8%
Annuitized	2.4%	2.5%	2.6%
Left with Employer	41.5%	45.6%	32.7%
Transferred to New Employer	0.0%	2.4%	2.8%
Lost	0.3%	1.3%	3.9%
Other	9.3%	5.6%	3.2%

Note: All Percentages are weighted, categories are not mutually exclusive. Conditioned on cash-out option being available.

If the analysis is altered to include only those respondents who had DC plans with LSD options, some differences are observed (see Table 4a). Cash-outs are higher in levels when the LSD option is available, but increase at about the same rate across cohorts. Rollover prevalence does not exhibit consistent trends across cohorts and is higher, but variably so, when the sample is restricted to those having the LSD option. The LSD-available group also shows reduced probabilities of leaving savings with the employer in the most recent cohort (21.9%, in comparison to 26% in the 1992 cohort and 29.3% in the 1998 cohort).

Table 4a. Cohort comparison: pension disposition of DC plans at job separation (over 8 years), conditioned on availability of lump-sum distribution option

	Cohort		
	1992	1998	2004
Cashed Out	18.9%	26.7%	29.1%
Rolled over into IRA	49.0%	44.5%	49.5%
Annuitized	3.3%	3.5%	3.2%
Left with Employer	26.0%	29.3%	21.9%
Transferred to New Employer	0.0%	2.2%	2.0%
Lost	0.0%	0.2%	3.2%
Other	5.7%	4.3%	2.3%

Note: All Percentages are weighted, categories are not mutually exclusive. Conditioned on cash-out option being available.

Finally, for DC plans, Table 4b shows DC disposition for DC plans valued over \$5,000 nominally. Because employers can compel former employees to cash out plans with balances under \$5,000, the increase in cash-out may be confounded by greater prevalence of low-value plans. However, as Table 4b indicates, although the level of cash-out is lower for these higher-valued plans, there is still a substantial increase in cash-out likelihood for later cohorts.

Table 4b. Cohort comparison: pension disposition of DC plans at job separation (over 8 years), conditioned on DC plan having nominal value greater than \$5,000

	Cohort		
	1992	1998	2004
Cashed Out	10.9%	14.4%	20.3%
Rolled over into IRA	38.5%	33.3%	36.9%
Annuitized	1.3%	2.9%	3.2%
Left with Employer	43.7%	49.5%	44.5%
Transferred to New Employer	0.0%	1.8%	2.9%
Lost	0.0%	1.2%	1.4%
Other	8.4%	6.0%	2.9%

Note: All Percentages are weighted, categories are not mutually exclusive. Conditioned on cash-out option being available.

A like analysis was conducted for respondents with DB plans at job separations. As shown in Table 5, the prevalence of cash-outs increased with cohort from 12% to 18%. There was a much smaller rate of rollover to IRAs than there was for the DC people, but IRA rollover rates did increase across cohorts, from 8% to 21%. Over half the respondents with DB plans at job separation were drawing benefits from it for the 1992 and 1998 cohorts—an important annuity feature of DB plans—but this had fallen to 36% by the 2004 cohort.

Table 5. Cohort comparison: pension disposition of DB plans at job separation (over 8 years)

	Cohort		
	1992	1998	2004
Cashed Out	12.5%	12.0%	18.0%
Rolled over into IRA	8.1%	11.2%	20.6%
Annuitized	0.0%	0.0%	0.0%
Expecting Benefits	29.3%	28.8%	28.7%
Drawing Benefits	57.3%	52.6%	36.4%
Lost	2.7%	1.9%	2.9%
Other	2.2%	3.8%	3.2%

Note: All percentages are weighted, categories are not mutually exclusive. Conditioned on cash-out option being available.

If we restrict the sample to those having DB plans with an LSD option (Table 5a), cash-out rates are higher and there continues to be an increase in the likelihood of cash-out, albeit a smaller increase. IRA

rollover rates are higher and they markedly increased across cohorts, and fewer individuals are drawing benefits in the 2004 cohort, similar to the results in Table 5.

Table 5a. Cohort comparison: pension disposition of DB plans at job separation (over 8 years), conditioned on availability of Lump-Sum Distribution Option

	Cohort		
	1992	1998	2004
Cashed Out	17.1%	15.3%	20.0%
Rolled over into IRA	15.5%	14.6%	27.9%
Annuitized	0.0%	0.0%	0.0%
Expecting Benefits	24.2%	22.0%	26.5%
Drawing Benefits	57.7%	57.4%	29.8%
Lost	0.7%	0.6%	3.9%
Other	2.3%	5.6%	3.8%

Note: All percentages are weighted, categories are not mutually exclusive. Conditioned on cash-out option being available.

The prior work by Hurd and Panis established that among respondents who cash out their pension plan upon job separation, whether it was DB and DC, these pension plans were disproportionately likely to be of low average value. We find similar patterns across all cohorts in our analysis. Table 5b shows the likelihood of cash-out of DC plans upon separation, conditional on plan value. For example, of DC plans valued under \$5,000 for the 1992 cohort from jobs being separated from, 34.5% were cashed-out. As is clear, the lowest value plans have a much higher likelihood of cash-out across all cohorts. Additionally, although the increase in cash-out for the 1998 cohort occurs across the entire value distribution, the cash-out increase for the 2004 cohort is driven by the middle value plans alone.

Table 5b. Percentage of DC Plans in Value Range that were Cashed-Out at Job Separation, by Cohort

Plan Value (2000 \$'s)	Cohort		
	1992	1998	2004
0-5,000	34.50%	42.10%	41.20%
5,001-50,000	15.30%	18.30%	27.40%
Over 50,000	6.00%	11.20%	12.10%

Although we would prefer to conduct a similar analysis with workers separating from jobs with DB entitlement, valuation of DB plans requires pooling answers from multiple parts of the HRS

questionnaire with varying reliability (e.g., the age at which an individual plans to start collecting pension benefits, the frequency and amount of such benefits in the future) and relies on assumptions as to mortality and personal discount rates. Additionally, later cohorts are asked these questions in systematically different ways, rendering cross-cohort comparisons difficult. Hurd and Panis (2006) conduct such an analysis for the 1992 cohort and show that cashed-out DB plans are of much lower value on average than those rolled over into IRAs, kept with one's employer in expectation of future benefits, or those from which individuals are currently drawing benefits. In Table 5c, we instead compare the value distribution of DB plans cashed out, since individuals report the value of the cash-out they received, allowing for clean cross-cohort comparisons. Each column therefore sums to 100%, with each row showing the percentage of cashed-out DB plans in that value bin. Although the likelihood of DB cash-out has increased in the 2004 cohort, Table 5c shows that the share of high-value DB plans cashed out is much lower (17%) than in previous cohorts (40% and 36% for the 1992 and 1998 cohorts).

Table 5c. Distribution of DB Plan Value *Conditional on Being Cashed Out*, by Value Category and Cohort

Plan Value (2000 \$'s)	Cohort		
	1992	1998	2004
0-5,000	22.83%	33.93%	36.43%
5,001-50,000	36.96%	30.36%	46.47%
Over 50,000	40.22%	35.71%	17.10%
All	100.00%	100.00%	100.00%

If people have been cashing out retirement savings more often and at younger ages, what have they been doing with the money? Patterns of use of cashed-out retirement funds among persons with a DB plan are shown in Table 6. Use patterns were similar for the 1992 and 1998 cohorts. Somewhat more than half was put into some other form of savings, and the remainder divided between spending and paying off debt. The 2004 cohort (data for 2004 to 2012) cut the percentage of cash-out funds going to other savings by half, doubling the percentage spent on debt and increasing spending by half. These patterns are consistent with a greater rate of negative shocks generated by the Great Recession and experienced by this cohort: they were more likely to spend and pay down debt.

Table 6. Uses of cash-out funds by those with a DB plan

	Cohort		
	1992	1998	2004
Spent	24.8%	21.9%	31.0%
Saved	55.9%	55.7%	29.2%
Debt	19.3%	18.6%	38.3%
Durables	0.0%	3.7%	1.5%

Note: All percentages are weighted.

Precipitating events of pension cash-outs

Closely related to the question of what cash-out recipients do with the money is why they sought the cash-out. A respondent's use of funds from a cash-out could reflect a specific event that precipitated the transfer. We have a window into this through HRS questions on reasons for job separations. Potential reasons include health shocks, unemployment, other wealth shocks (such as the Great Recession's effects on retirement savings), and family needs such as the effects of divorce or widowhood or the need to support children financially. Answers to the HRS question on reasons for job separations are given for those cashing out DC plans in Figure 9, and for those cashing out DB plans in Figure 10, with Figures 9a and 10a showing these reasons for all individuals separating from jobs with the corresponding pension eligibility, regardless of pension disposition.

Figure 9: Reason for Job Separation Among DC Cash-Outs

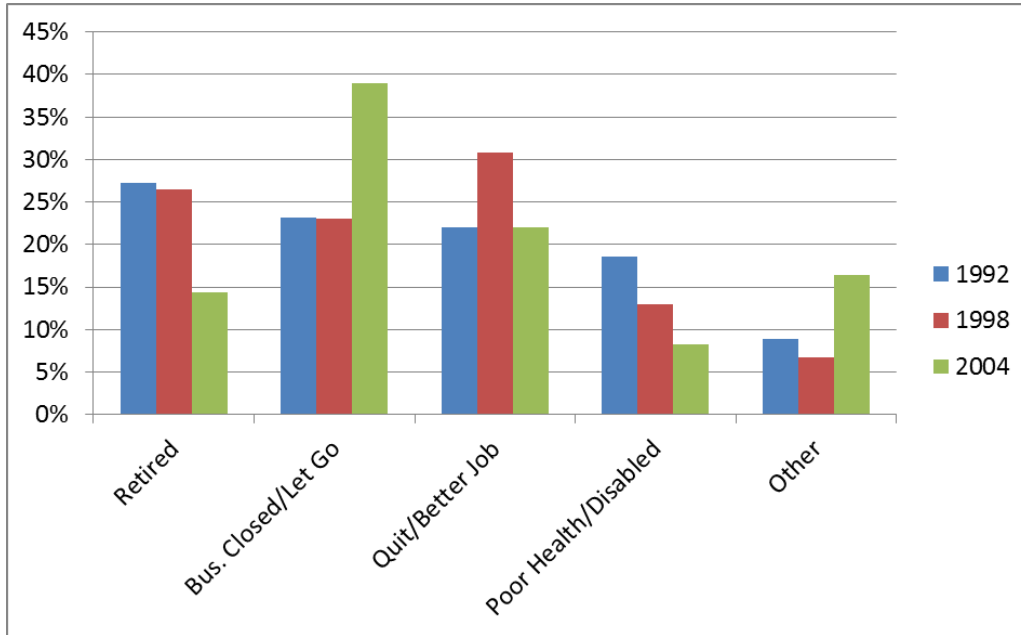


Figure 9a: Reason for Job Separation Among All Separations from All Jobs with DC Plans

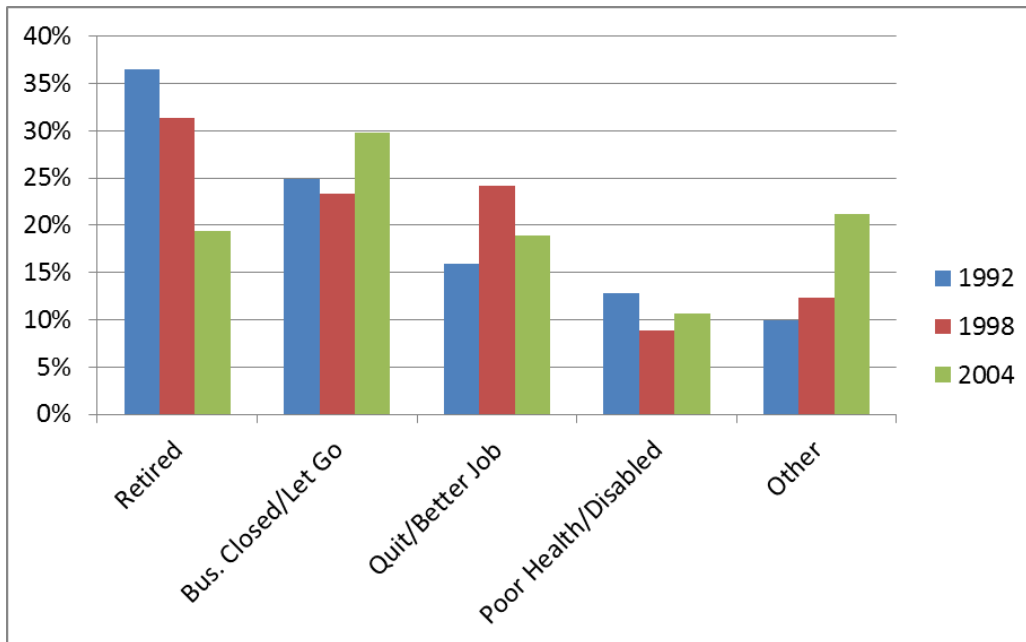


Figure 10: Reason for Job Separation Among DB Cash-Outs

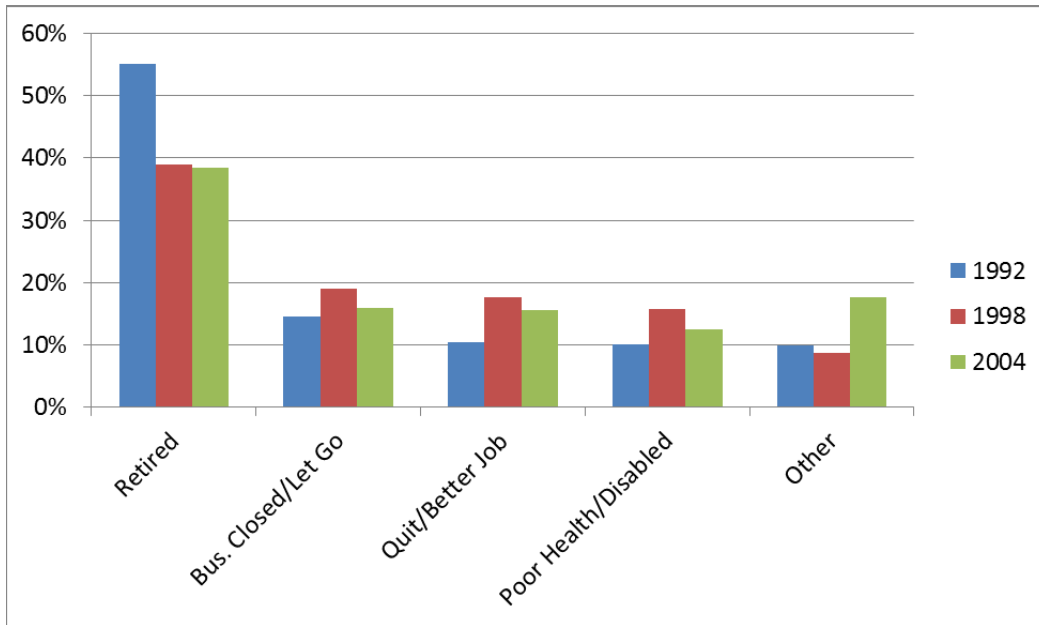
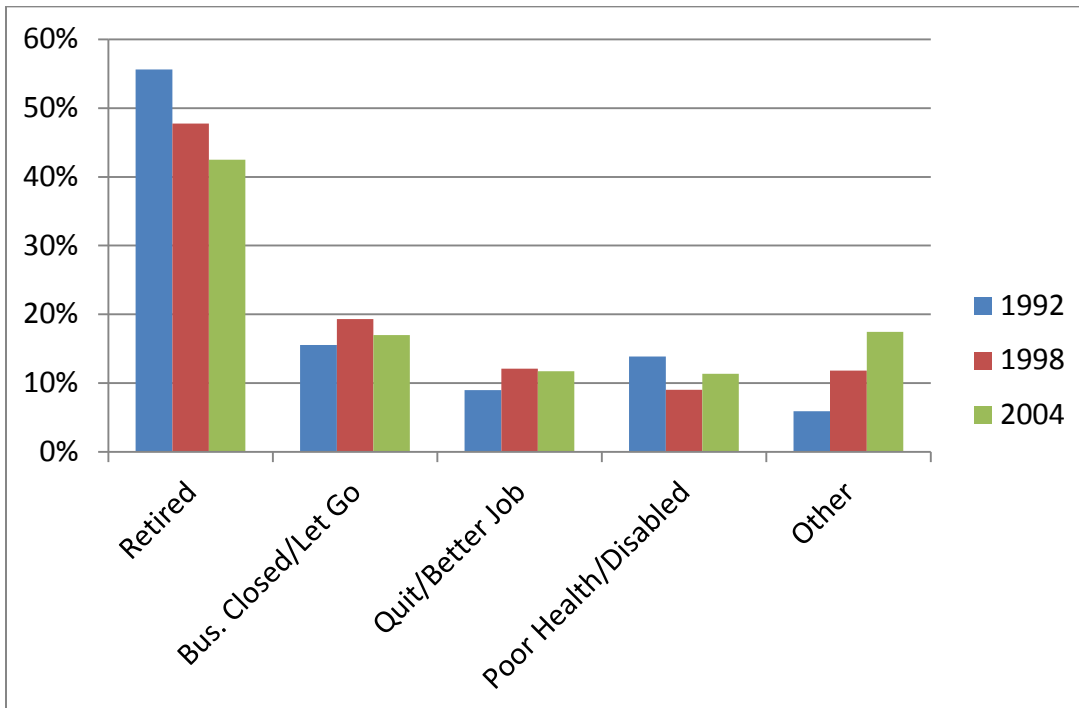


Figure 10a: Reason for Job Separation Among All Separations from All Jobs with DB Plans



Among individuals separating from a job with a DC plan (Figure 9), the first three reasons shown—retirement, job loss, or voluntary separation—were all important reasons for separating from a job. However, retirement was less often the reason in the 2004 cohort and job loss—“let go” or “business closed”—was more often the reason for those cashing out DC plans, especially in comparison to all individuals separating from DC plans. Poor health or disability is less often cited by each cohort than by the preceding one.

Among those separating from a job with a DB plan, retirement was given as the reason by 40% to 55% of the respondents, whereas fewer than 20% gave any other reason (Figure 10). Fewer retired in the 1998 and 2004 cohorts, but there was no increase in those responding “business closed/let go” for the 2004 cohort.

We next seek to learn what fraction of respondents cashed out their retirement plans when facing a shock around the time of job separation. The results of this analysis are shown in Table 7. Among those separating with a pension, the overall fraction that cashed out for any reason was 18.6%. Rates were much higher among those affected by some specific shock. In particular, among those who were separating from a job with a pension and falling behind on their mortgage, 55% cashed out, as did 36% of those losing their health insurance at job separation and 26% of those whose health became poor, with 54% cashing out if they lost their health insurance and reported being in poor health (including both those newly in poor health, and those currently and previously in poor health).

Table 7. Among those separating with a pension, the percent that cashed out, by precipitating events

Shock at (or around time of) job separation (N)	Percent cashed out (%)
Got Divorced (23)	20.7
Became Widowed (21)	19.5
Became Work-Limited (242)	22.1
Health Worsens (389)	19.4
Became Poor Health (66)	26.5
Lost Health Insurance (193)	36.2
Lost Health Insurance and In Poor Health (28)	54.7
Fell Behind on Mortgage (30)	54.6
Any Mortgage Issues (41)	47.2
None of the Above Shocks (834)	16.9

Predictors of pension cash-out: DB and DC plans with lump-sum option

To control for a number of covariates, we estimated several regression models of the relationship between cash-out of pension plans among those separating from jobs and 26 right-hand (explanatory) variables, including shocks. Probit estimation was employed on three models. In one model (designated “0”) the dependent variable was cash-out of a DB or DC pension. The other two models pertained to cash-out of a DC plan. Model 2 contains all the variables used in Model 1 and also includes the real value of the DC plan in question or whether this value was missing. .

The analysis identified numerous variables predictive of cash-outs at a statistically significant level (see Table 8). Being older, living in an area with a higher unemployment rate, and being African-American were associated with a higher probability of a pension cash-out. Being wealthier or more educated or having a longer planning horizon, better health (self-reported), health insurance, or a higher DC plan value was associated with lower pension cash-out probability. Generally, these were similarly predictive across models.

Table 8. Probit Coefficients Predicting Cash-out of Pension Plan among Separations from Jobs with Pension Coverage with Lump-Sum Option

	Dependent variable		
	DB or DC Cash-out	DC Cash-out	
	(0)	(1)	(2)
Age (continuous)	0.0102* (0.00546)	0.0218*** (0.00682)	0.0214*** (0.00702)
1998 Cohort	0.0101 (0.0661)	0.0721 (0.0839)	0.0615 (0.0877)
2004 Cohort	0.0575 (0.0712)	0.122 (0.0896)	0.102 (0.0918)
Unemployment Rate (1-100)	0.0619*** (0.0143)	0.0374** (0.0184)	0.0454** (0.0187)
Male	-0.0309 (0.0474)	-0.0521 (0.0604)	0.00166 (0.0618)
Black	0.226*** (0.0705)	0.245*** (0.0881)	0.275*** (0.0888)
Less than High School	0.0995 (0.0821)	0.200** (0.0971)	0.190* (0.0993)
More than High School	-0.119**	-0.191***	-0.159**

	(0.0520)	(0.0661)	(0.0672)
Log(Total HH Wealth ^a)	-0.0477*** (0.0157)	-0.131*** (0.0217)	-0.101*** (0.0217)
Subjective Prob(Survive to 85)=0	-0.0951 (0.114)	-0.119 (0.140)	-0.148 (0.136)
Few Months Planning Horizon	0.0589 (0.0789)	0.165* (0.0949)	0.124 (0.0968)
Five Years or More Planning Horizon	-0.0191 (0.0498)	-0.0407 (0.0648)	-0.0513 (0.0659)
Health (increasing in healthiness, 1-5 scale)	-0.0392 (0.0240)	-0.0713** (0.0299)	-0.0662** (0.0304)
Any Health Insurance	-0.271*** (0.0875)	-0.376*** (0.104)	-0.331*** (0.106)
Disabled	-0.319* (0.192)	-0.0814 (0.228)	-0.0414 (0.234)
Working	-0.0193 (0.0513)	0.0981 (0.0654)	0.0429 (0.0672)
DC Plan Value			-0.136*** (0.0224)
Missing DC Plan Value			-1.445*** (0.237)
Observations	4,910	3,802	3,802

Robust standard errors in parentheses, *** p<0.01, ** p<0.05, * p<0.1

^a Wealth includes net values of primary residence, secondary residence, other real estate, business, stocks and investment funds, bonds, bank accounts, and other savings.

Several variables were not predictive of pension cash-out at statistically significant levels; these included gender, subjective probability of survival, and disability.

Longitudinal Analyses: consequences of cash-outs

By taking advantage of the HRS's longstanding longitudinal panel, we can track respondents who cashed out and compare outcomes (economic status, personal characteristics, survival) with those of participants who did not cash out. Specifically, we focus on the 1992 cohort and follow it for 20 years.

As shown in Table 9, 25% of those who had never separated from a job died by 2012, compared with only 16% of those who had ever separated. This difference is at least partially due to the time window over which a job separation could occur: those who died early had fewer chances for job separation. Among those who had ever separated with a cash-out, over 19% died compared with 16% among those who separated without a cash-out. Most likely this difference is a reflection of a positive correlation between cash-out and economic shocks, and a negative correlation between cash-out and 1992 socio-economic status: as will be shown below, those who cashed out were initially less wealthy, had lower incomes and were in worse health, all of which predict greater mortality.

Table 9. Mortality among 1992 workers

	% Dead by 2012
Never Separated	24.9%
Ever Separated without Cash-out	15.9%
Ever Separated with Cash-out	19.3%

Table 10 shows the labor force states in 2012 among those who survived and who worked with pension coverage over the 20 years between 1992 and 2012. Although, of course, most had retired, a non-negligible fraction was still working.

Table 10. Labor force status in 2012

Alive in 2012 and Had Ever Worked with Pension Coverage	
Retired	2,443
Working	855
Disabled	2
Unemployed	44
Other	17

Table 11 shows several measures of health and economic status in 1992 and in 2012, by employment and cash-out status.

Table 11. Economic measures in 1992 and 2012 conditional on survival to 2012

Retirees in 2012				
1992 Averages for those Retired in 2012	Log(Wealth^a)	Household Income^b	Health^c	Pension Income
Never Separated	11.43	70314	3.83	603
Ever Separated without Cash-out	11.24	69277	3.84	413
Ever Separated with Cash-out	10.78	53130	3.47	245
2012 Averages for those Retired in 2012	Log(Wealth)	Household Income	Health	Pension Income
Never Separated	11.43	32665	3.16	3374
Ever Separated without Cash-out	11.38	33853	3.11	2410
Ever Separated with Cash-out	9.94	23617	2.87	339
Workers in 2012				
1992 Averages for those Working in 2012	Log(Wealth)	Household Income	Health	Pension Income
Never Separated	11.14	72399	3.83	718
Ever Separated without Cash-out	11.49	72376	3.88	504
Ever Separated with Cash-out	10.98	59600	3.73	655
2012 Averages for those Working in 2012	Log(Wealth)	Household Income	Health	Pension Income
Never Separated	11.65	78795	3.64	1438
Ever Separated without Cash-out	11.76	55236	3.63	3339
Ever Separated with Cash-out	10.94	45022	3.49	1339

^aFor components of wealth, see note to Table 8.

^bIncludes income from individual earnings, household capital, employer pension or annuity, public pension (including Social Security), Supplemental Security Income, unemployment or workers compensation benefits, and other government transfers.

^cSelf-reported health status, on a scale from 1 to 5, with 5 corresponding to “Excellent Health” and 1 “Poor Health.”

Considering wealth, health, household income, and pension income among those who survived to 2012, those who cashed out do look worse off in 2012 compared to those who never separated or separated without cash-out, for either retirees or those still working. However, these individuals were also worse off in 1992, *before they cashed out*. Whether cashing out affects individuals negatively is therefore conflated with the types of people who choose to cash out: selection plays a role in attempts to isolate the effects of cashing out on these well-being measures. Further, as we have seen, cash-out is

accompanied by shocks such as losing health insurance and falling behind on mortgages. Those events by themselves would lead to relatively worse outcomes in 2012, even were the individual not to cash out.

To separate the causal effect of cash-out from initial conditions that are correlated with cash-out and from precipitating shocks, we used as a classifying variable the availability of an LSD option in the pension plan when we first observe individuals in 1992.³ Under the assumption that the availability of an LSD at baseline was orthogonal to initial characteristics and to the probability of a shock during the 20 years of observation,⁴ the variation by availability shows whether giving an LSD option results in worse outcomes, and when properly used as an instrumental variable, how large the negative effects of cash-out are. Additionally, we limit our sample to DB plan holders, since the vast majority of DC plan holders report having an LSD option, providing little useful variation in availability of such an option. We therefore have a measure of access to the option of cashing out one's DB pension which appears statistically unrelated to the selection issues that arise from directly comparing those who cash out from those who did not, which can be driven by both the experience of shocks around job separation as well as vulnerability to these shocks before the cash-out decision itself. As Table 12 indicates, the presence of this option in 1992, regardless of whether individuals subsequently gain or lose this option, leads to a substantially and highly statistically significant difference in the likelihood of an individual actually cashing out a DB plan in the subsequent 20 years.

We also note that about 10.5 percent of workers who apparently did not have an LSD option in their DB plan reported a DB cash-out. However, the classification is by DB LSD status on the 1992 job. Due to subsequent job changes (prior to 2012), a respondent who did not have an LSD option in 1992 could have shifted into a job that had one and on switching out of that job cashed out that pension; individuals may have misreported the availability of such an option, perhaps unaware of this option until job separation; or individuals' DB plans may have changed in the interim to include a cash-out option.

³ Due to issues surrounding sample attrition, identification of specific pension plans with pension characteristics across waves, and the ease and reliability of comparing control and treatment groups in a single wave, this analysis focuses on baseline availability of LSD options. However, we have also conducted analyses as to whether an individual reported having an LSD option in his/her most recently described DB plan at the time of separation, and we find neither significantly nor substantially different results.

⁴ We directly test differences for these cohorts in 1992, and find no statistically significant differences by race, gender, marital status, earnings, health insurance coverage, health, or work-limitation, and only marginally significant differences in 1992 wealth and household income, although these differences are driven by the top 1% of the respective distributions.

Hurd and Panis (2006) also noted this. Nonetheless, the rates of DB cash-out are over 60% higher among the 893 reporting the option, showing that respondent reporting about DB LSD availability does have discriminatory power.

Table 12. Long-Term Outcomes based on 1992 Availability of LSD Option in DB Plans, Pairwise T-tests of Means, Among 1992 DB Plan Holders

	DB LSD Option in 1992		Statistically Significant
	No	Yes	
Counts	1,548	893	
Fraction Alive in 2012	80.22%	82.54%	No
Conditional on being Alive in 2012			
Counts	1,242	737	
Any Non-Retirement Separation by 2012	26.63%	31.15%	Yes, at 10% Level
Any Retirement Separation by 2012	93.80%	90.88%	Yes, at 5% Level
Both Non-Retirement and Retirement separations	23.75%	25.15%	No
Any DB Cash-out	10.50%	17.00%	Yes, at 0.1% Level
Wealth in 2012	511,031	556,601	No
Pension and Annuity Income in 2012	5,654	4,700	No
Household Income in 2012	47,897	51,070	No
ADLs			
Number of ADLs	0.20	0.18	No
Number of iADLs	0.09	0.09	No
Healthy Behaviors			
Smoke Now?	6.55%	6.57%	No
Cigarettes/Day	15.48	12.45	No
Ever Drink?	56.53%	55.68%	No
Drinks/Day	1.75	1.67	No
Vigorous Exercise more than Once a Week?	23.33%	24.36%	No
Other Income Measures			
Pension Income	4,343	4,109	No
Annuity Income	1,311	591	No
SSI/SSDI Income	53	4	No
OASI Income	13,798	13,777	No
UI Income	28	1	No
Other Gov Income	1,331	957	No

Other Wealth Measures

IRA Wealth in HH	102,521	120,715	No
Net Primary HH Wealth	156,985	173,305	Yes, at 10% Level
Net Secondary HH Wealth	24,436	22,083	No
Net Non-Housing HH Wealth	352,784	383,087	No

Consumption (N=304)

Consumption, Durable	369	273	Not significant
Consumption, Non-Durable	30,113	28,449	No
Consumption, Transportation	8,831	8,275	No

Subjective Well-Being Scores (N=553)

Purpose in Life	36.54	38.18	Yes, at 5% Level
Life Satisfaction	5.06	5.13	No
Positive Affect	2.62	2.75	Yes, at 0.1% Level
Negative Affect	2.80	2.82	No
Chronic Stressors	1.42	1.45	No
Financial Satisfaction	2.25	2.28	No
Difficulty Making Monthly Payments	1.69	1.75	No
Quality of Life	5.59	5.59	No

Sample: 51-61 1992 HRS Cohort, Working in a Job with DB Pension Coverage in 1992, All Dollar Figures in 2012 Dollars. Consumption measures and Subjective Well-Being Scores derive from additional survey instruments given to HRS respondents, leading to lower sample sizes. For more information on subjective well-being measures, see <http://hrsonline.isr.umich.edu/sitedocs/userg/HRS2006-2010SAQdoc.pdf>

There are several results of interest. First, there is little apparent difference in the survival rates. Second, availability of a DB LSD option does appear to be linked with a greater propensity to separate from a job pre-retirement (marginally significant at the 10% level) and a lower propensity to have retired (significant at the 5% level). Possible explanations for these differences include having a DB LSD option allowing for more pre-retirement job switching, greater knowledge of LSD options among individuals considering switching jobs, those employers and positions at those employers that offer LSD options being linked to higher turnover rates, or a combination of these. However, there appear to be no resulting statistically significant differences in household wealth or household income among those with a cash-out option; if anything, the averages for these outcomes are slightly higher for those with a DB LSD option. Although average pension income is lower for those with the DB LSD option, this difference is not statistically significant. We go on to measure a wide range of income variables, split by source, and wealth variables, broken down by IRA, housing, and non-housing stocks, none of which are

statistically significant at the 5% level. Thus, this table does not support the view that a cash-out option has led to pension holders being less economically prepared for retirement.

Additionally, we compare a lengthy list of impairments (those that affect Activities of Daily Living and Instrumental Activities of Daily Living), unhealthy and healthy behaviors, consumption by category, and subjective well-being metrics.⁵ We find no systematic or statistically significant differences, with the only exceptions being “positive affect” and “purpose in life,” but these differences are small compared to the means. Even across these disparate measures, there again appears to be little difference in economic, physical, or mental well-being across availability of cash-out options. Although our statistical power is limited given our sample size, the lack of significant differences allows us to rule out very large effects of the availability of cash-out options on well-being.

CONCLUSIONS

Among policymakers concerned about retirement economic security, the practice of cashing out retirement plans at the time of job separation has been a worry. Changes to the tax code have been enacted to discourage such transfers, but the limited evidence previously available suggests that cash-outs continue to pull substantial amounts out of retirement plans, even when households are not facing imminent liquidity challenges. In this paper we have attempted to add to the literature on pension cash-out practices. Specifically, we draw on long-duration panel data from the Health and Retirement Study to learn what shocks can trigger cash-outs, whether and how cash-out practices are changing, and what might be their long-term consequences.

Health was an important event associated with cash-out: more than a third of those losing their health insurance at job separation engaged in cash-outs, and only a quarter of those whose health turned bad did so. Although only observed in the most recent cohort, mortgage-related issues also were related to higher rates of pension cash-out.

Trends are of particular interest. To identify them, we took advantage of the HRS entering cohorts in 1992, 1998, and 2004. Most of these analyses showed that cashing out became more frequent. Also, fewer job separations in the 2004 cohort were followed by retirement; among those with DC plans, more separations were due to employer closures and layoffs.

⁵ See Appendix Table A1 for means of these metrics by type of pension coverage among workers and by pension disposition after job separation over the entire HRS sample.

Ultimately, the concerns about retirement economic security rest on the long-term welfare of the nation's senior citizens. How are these affected by cash-outs? The 1992 HRS cohort has been running for over 20 years, so some inferences can be drawn. At first glance, those who cashed out do look worse off in 2012 compared to those who never separated or separated without cash-out. However, these individuals were also worse off in 1992, *before they cashed out*. This suggests some confounding of genuine cashing-out effects with participants' prior attitudes and behaviors. Further work to isolate these relationships suggests that respondents having access to cashing out have more non-retirement job separations and less retirement than those without this access, but 20 years after reporting the availability of such an option, there are no statistically significant differences in wealth and income between these two groups. This is not necessarily the outcome we would have expected, but it is not inconsistent with the conclusions of Hurd and Panis (2006). Further attention to this topic is warranted.

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Appendix Table A1

	Among Workers with Pension Coverage			Among those Separating with DB Plans		Among those Separating with DC Plans	
	No Pension Coverage	DB Coverage	DC Coverage	Didn't Cash Out	Cashed Out	Didn't Cash Out	Cashed Out
Expected Retirement Age	64.62	62.32	63.13	62.96	64.28	63.84	65.28
ADLs							
Number of ADLs	0.09	0.05	0.05	0.13	0.14	0.11	0.22
Number of iADLS	0.06	0.05	0.04	0.04	0.05	0.04	0.06
Healthy Behaviors							
Smoke Now?	0.19	0.15	0.15	0.16	0.17	0.16	0.23
Cigarettes/Day if smokes	17.09	17.21	16.72	17.65	15.89	15.00	16.06
Ever Drink?	0.62	0.68	0.70	0.61	0.64	0.68	0.57
Drinks/Day if drinks	2.03	1.84	1.96	2.02	2.21	2.01	2.39
Vigorous Exercise>Once a Week?	0.37	0.38	0.37	0.42	0.39	0.40	0.32
Income Measures							
Pension Income	2,331	881	861	5,773	2,307	2,810	1,522
Annuity Income	246	117	125	179	382	176	44
SSI/SSDI Income	84	15	17	152	188	89	207
OASI Income	2,660	582	735	2,785	2,758	2,619	3,029
UI Income	176	81	86	291	567	521	483
Other Gov Income	379	334	414	568	528	657	369
Wealth Measures							
IRA Wealth in HH	53,338	52,942	60,976	77,733	146,152	116,072	52,031
Net Primary HH Wealth	117,689	118,950	123,585	120,520	109,582	140,856	72,552
Net Secondary HH Wealth	18,035	20,301	24,093	18,058	21,846	24,299	11,536
Net Non-Housing HH Wealth	302,520	238,172	284,966	270,924	342,843	370,550	160,963
Consumption							
Consumption, Durable	348	469	464	433	366	462	266
Consumption, Non-Durable	21,643	24,381	25,010	25,345	22,266	25,176	17,330
Consumption, Transportation	9,115	10,976	11,060	10,506	8,479	9,523	6,839
Subjective Well-Being Scores							
Purpose in Life	37.69	38.62	38.61	37.74	37.97	38.12	37.46
Life Satisfaction	4.86	4.99	4.98	5.12	4.73	4.91	4.46
Positive Affect	2.74	2.76	2.77	2.71	2.75	2.75	2.72
Negative Affect	2.80	2.83	2.83	2.81	2.79	2.80	2.75

Chronic Stressors	1.53	1.50	1.52	1.46	1.52	1.50	1.61
Financial Satisfaction	2.68	2.48	2.51	2.37	2.68	2.52	3.01
Difficulty Making Monthly Payments	2.04	1.81	1.84	1.73	1.95	1.84	2.29
Quality of Life	5.50	5.47	5.48	5.49	5.39	5.50	5.45
