PLAN SPONSOR FACT SHEET

Early or Phased Retirement Incentive Programs for Higher Education

This fact sheet discusses the purposes of early or phased retirement incentive programs and the issues that may arise with these programs. The information provided is based on TIAA-CREF's understanding of the law but does not constitute legal advice. You should consult with labor law and employee benefits counsel regarding the legal ramifications of these programs before taking action.[1]

Purposes of Early or Phased Retirement Incentive Programs

The purpose of an early or phased retirement incentive program is to assist an institution in managing its workforce in light of future needs.

In most cases the programs are designed to encourage certain employees to retire early in order to:

- Provide openings for new hires
- Reallocate staffing to better satisfy changing student needs
- Reduce payroll expenses, or
- Provide them with suitable work-life balance solutions.

Phased retirement programs may also be used to encourage certain older employees whose continued services are needed over the next few years to continue their employment. Through these programs, such employees can ease into retirement by gradually reducing their workloads instead of fully retiring immediately.

Early and phased retirement programs are particularly attractive to colleges and universities with tenured faculty, many of whom, in the absence of early retirement incentives, may be inclined to postpone their retirement well past the Social Security retirement age.

The Difference

The difference between an early retirement incentive program and phased retirement incentive program is that:

- An early retirement incentive program provides benefits to employees only when they retire fully whereas,
- A phased retirement incentive program provides benefits to employees when they commence a program of gradually reducing their workloads over a specified period.

The Incentives

Early and phased retirement incentive programs achieve their goals by providing targeted employees who agree to retire (or enter phased retirement) before normal retirement age with incentives in form of:

- Cash benefits,
- Early access to distributions from retirement plans (generally permissible only if fully retiring unless the plan document allows in-service distributions), and/or
- Additional contributions to retirement or deferred compensation plans.

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Primary Considerations for Employers

Before embarking upon the task of designing an early or phased retirement incentive program, an employer needs to:

- Identify the target group of employees,
- Decide whether the program will be long-term or a one-time “window” program to satisfy an immediate need to reduce the workforce, and
- Identify cost-effective incentives that will encourage the target group to retire early without triggering the exodus of employees whose continued services are needed.

Special Considerations

Beyond the basic considerations identified above, the employer must also determine whether target employees will be too young to qualify for:

- Full or even early Social Security benefits
- Medicare benefits

If the employer does not generally provide retirees with medical benefits, the incentives may need to include both additional income and retiree medical benefits to bridge the period until the early retirees qualify for government benefits.

If the incentive program is to be made available to employees who are too young even for early retirement, it might be useful to include outplacement benefits and perhaps extended medical benefits to cover a reasonable amount of time for a job search.

If the program is intended to be offered to only a limited number of employees, the employer might want to consider offering part-time or post-retirement consulting arrangements tailored to the specific wants/needs of those employees rather than implementing an incentive plan. Note, however, that an employee who elects to go to part-time status will not be able to supplement his or her reduced salary for part-time work by taking early distributions from a retirement plan unless the plan document permits in-service distributions.

Legal Hurdles

Like other employee benefit plans, early and phased retirement incentive programs are subject to a variety of legal requirements including:

- The Age Discrimination in Employment Act of 1967 (ADEA) which prohibits employers from discriminating against employees over age 40,
- The Older Worker Benefit Protection Act of 1996 (OWBPA) which requires benefits be offered under a voluntary bona fide employee benefit plan with benefit payments or costs for older workers at least as high as those for younger workers,
- The Faculty Retirement Incentive Act of 1998 which provides a “safe harbor” from ADEA requirements for qualifying early retirement incentive plans of colleges and universities (see below),
- The Employee Retirement Income Security Act of 1974 (ERISA), and
- The Internal Revenue Code, which imposes a variety of benefit limits and nondiscrimination requirements on contributions to qualified and 403(b) retirement plans used as an incentive to retire early by private employers.

Safe Harbor Faculty Retirement Incentive Plans

A college or university’s early retirement incentive program satisfies the ADEA’s nondiscrimination requirements if it qualifies as a Safe Harbor Program under Section 4(m) of the ADEA:

- Participation in the program is voluntary,
- Benefits are provided only to tenured faculty,
- Benefits are supplemental and in addition to (not replacements for) benefits currently offered to faculty under other, non-early retirement incentive programs.

For newly adopted safe harbor early retirement incentive programs, special rules apply to faculty members who satisfy all of the program’s eligibility requirements but do not qualify for maximum benefits under the program because they are already too old. Such an employee must be given 180 days to elect to retire and receive the maximum benefit that the program would provide to an employee with his or her salary and years of service at any age.

Permissible Incentive Plans

Generally, an early or phased retirement incentive may be offered under a retirement plan such as:

- A severance pay program,
- A Section 401(a) plan,
- A Section 403(b) plan,
- A Section 457(b) plan, or
- A Section 457(f) plan.

Permissible Benefits

Incentive benefits under an early or phased retirement incentive program may be:

- Flat dollar cash payments for any eligible faculty member opting for the benefit,
- Service-based benefits (e.g., $1,000 x years of service),
- Percentage of salary benefits,
- Percentage of salary x years of service (e.g., 1% of salary x years of service),
- Flat dollar or percentage increases in benefits from defined benefit plans,
- Post-retirement contributions to 403(b) retirement plans.

Examples of Permissible Benefit Structures

Here are a few ways that the benefits offered under an early or phased incentive program may be structured:

- Plan A provides tenured faculty who retire between the ages of 65 and 70 with monthly bridge payments equal to 50% of final monthly salary until retirement benefits commence at age 70.
- Plan B provides bridge benefits of 50% of final monthly salary for tenured faculty who retire at age 65, 40% for those who retire at 66, 30% for those who retire at 67, 20% for those who retire at 68, and 10% for those retiring at 69.
- Plan C provides bridge payments for retirement only to tenured faculty who meet minimum service requirements and/or who work in specified schools, departments, or employee classifications.
- Plan D provides lump-sum payments calculated on the basis of salary and age, i.e., 50% of final annual salary for tenured faculty who retire between 62 and 65, 40% for those who retire at 66, 30% for those who retire at 67, 20% for those who retire at 68, and 10% for those retiring at 69. No incentives are provided for those retiring at later ages.
- Plan E provides subsidized pay for tenured faculty who move from full-time to part-time status between ages of 62 and 70. The size of the subsidy depends upon the age at which the transition to part-time status is made.

For assistance

- Contact your TIAA-CREF Relationship Manager for information on the retirement plans that might be used as a retirement incentive under your early or phased retirement program.
- Call our Administrator Telephone Center at **888-842-7782** Monday through Friday, 8 a.m. to 8 p.m. (ET)

[1] All interpretations in this Factsheet reflect our current understanding of the application of the rules. The information is presented with the understanding that TIAA-CREF (or its affiliates, distributors, employees, representatives and/or insurance agents) is not engaged in rendering legal or tax advice. Clients should consult their independent legal advisor for legal advice to determine what best suits their individual needs. Investment, insurance and annuity products are not FDIC insured, are not bank guaranteed, are not deposits, are not insured by any federal government agency, are not a condition to any banking service or activity, and may lose value.