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How to Get People to Delay Retirement

Longer working lives are crucial to a secure financial retirement. Here's how to encourage older workers to stay on the job, and companies to hire them

One idea under discussion is to scrap the Social Security payroll tax for workers 62 and older. This would give the employees a raise and cut employers' costs. *PHOTO: ISTOCKPHOTO/GETTY IMAGES*

By **ANNE TERGESEN**

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The average American retires relatively early, at 64 for men and 62 for women. But with life expectancy rising by one to three months with every year that passes, economists and policy experts say leaving the workforce at such ages is a luxury most people can no longer afford.

"Retirement was a 20th-century invention, but it's kind of gotten out of control," says John Shoven, an economist at Stanford University. "If you go back to 1900, most men worked until they couldn't work anymore and died a few years later. Now, you can spend

40% of your adult life in retirement."

While the

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solution—working longer—sounds straightforward, older workers face powerful incentives to retire sooner rather than later, says Olivia Mitchell, a professor of business, economics and public policy at the University of Pennsylvania's Wharton School. Those incentives range from age discrimination in the workplace to certain provisions in the tax code and rules for Social Security and Medicare.

Still, extending working lives "is the most powerful lever we have to increase retirement security," says Alicia Munnell, director of Boston College's Center for Retirement Research. "If you delay retirement, it really reduces the percentage of the population at risk" of outliving their money.

What follows are five tax and policy innovations that aim to keep people working longer —by reducing the cost of employing older workers and increasing the financial rewards for workers who stay on the job in later life.

Eliminate the Social Security payroll tax for older people

Employers funnel 6.2 cents of every dollar a worker earns up to $118,500 into a payroll tax that funds Social Security. Employees kick in another 6.2 cents.

But due to the way Social Security benefits are calculated, employees 62 and older who choose to continue working receive only 2.5 cents of extra lifetime benefits on average for every dollar of Social Security payroll tax they pay—a “clear disincentive to work,” says Andrew Biggs, a resident scholar at the American Enterprise Institute.

To induce older workers to stay on the job, Mr. Biggs favors scrapping the Social Security payroll tax for those 62 and older. This would give the employee an immediate 6.2% raise and save his or her employer 6.2%, as well.

Dropping the Social Security payroll tax for older workers would have a “modest negative impact on Social Security’s solvency,” says Mr. Biggs. But the government would offset at least some of the cost by collecting more income tax on older workers’ prolonged earnings.

Require Medicare to cover older workers

If you work for a company with more than 20 employees and are eligible for Medicare, you have the option of sticking with your employer-based coverage, which is typically more generous.

To give companies an incentive to retain older workers, Prof. Shoven proposes transferring the coverage obligation for workers 65 and older to Medicare. “Suddenly, older workers would be the low-cost employees when it comes to health insurance,” he says. If that were the case, employers might even raise older workers’ wages to give them an incentive to stick around, Prof. Shoven adds.

While Medicare spending would rise by about 5%, the government would recoup at least some of that cost by collecting more years of income tax on older workers’ wages, Prof. Shoven says.

Eliminate the Social Security earnings test

The Social Security earnings test temporarily reduces benefits for those who haven’t reached full retirement age and earn more than a certain amount.

Specifically, if you earn more than $15,720 a year and collect Social Security between the age of 62 and your full retirement age—66 for people born between 1943 and 1954, rising gradually to 67 for those born after 1959—you’ll lose $1 of benefits for every $2 you earn over the $15,720 threshold. In the year in which you reach your full retirement age, you can make up to $41,880 without losing any benefits. After that, the earnings test goes away—you can earn as much as you want without giving up any benefits.

Benefits lost to the earnings test are generally restored in the form of higher future monthly Social Security checks.But many people—perhaps due to a belief that their benefits are lost forever—instead cut back on work and prevent cuts to their Social Security payment, says Alexander Gelber, an assistant professor of public policy at the University of California, Berkeley.

In research yet to be published, Prof. Gelber and three other researchers— Damon Jones, an assistant professor at the University of Chicago, Daniel Sacks, an assistant professor at Indiana University, and Jae Song, an economist at the Social Security Administration—found that as people at the ages subject to the earnings test start earning more than $15,720, they become more likely to retire, relative to people earning less than that. Moreover, of those who continue working, the percentage earning just below $15,720 is much higher among the ages subject to the earnings test than among other ages, says Prof. Jones—suggesting that many people are working only as much as they can without triggering a benefit reduction. In sum: “We find strong evidence that the earnings test is discouraging work,” Prof. Jones says.

Because Social Security generally ultimately restores to beneficiaries the money it withholds under the earnings test, actuaries at the Social Security Administration have projected that eliminating the test would have little impact on the program’s solvency. But scrapping the test would increase the fraction of the relevant population that is working by a couple of percentage points, say the researchers.

Provide lump sums for delaying Social Security

Too many people still start collecting their Social Security benefits the first year in which they become eligible, at 62: 42% of men and 48% of women in 2013, according to Boston College’s Center for Retirement Research. By doing so, they forgo a larger monthly payout they would be eligible for if they waited.

Wharton’s Prof. Mitchell and three collaborators think they have found an incentive for some people to delay claiming Social Security, which they believe will encourage people to work longer, and so potentially enjoy a more financially comfortable, albeit shorter, retirement. They recently conducted an experiment in which 2,451 participants were offered the option of a lump sum instead of a higher monthly benefit in return for waiting to claim Social Security.

For instance, someone entitled to $1,500 a month at age 62 who delayed claiming by five years would still receive $1,500 a month starting at age 67—plus an immediate payment of $108,589, based on the additional benefits that person would have received over an average lifespan for waiting five years to claim.

To get the lump sum, the study participants were willing to postpone claiming benefits by an average of up to eight months from the date they had planned—and most said they would work longer, too.

People working longer would bring additional "months or years of Social Security payroll tax" to the government, which "could modestly improve the program's solvency," says Prof. Mitchell. But some retirement experts argue that higher monthly payments are preferable, because they ensure that the extra income paid for postponing benefits will last for the recipient's lifetime.

Impose a new mandatory retirement age

Boston College's Prof. Munnell argues that bringing back a mandatory retirement age—an age at which companies would have the right, but not the obligation, to require an employee to retire—would help raise retirement ages.

Why? Because employers would hire more job seekers in their 50s and 60s whom they might now shun due to a fear of having to keep them on the payroll indefinitely. "It gives everybody a graceful way out," Prof. Munnell says.

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Having a mandatory retirement age limits "the employer's exposure to productivity declines and compensation escalation that typically emerge as workers age," she says.

If the mandatory retirement age were high enough—she suggests tying it to Social Security's full retirement age, which is 67 for people born after 1959—it might also encourage employees to work longer. After all, the average American currently retires by 63, and at least some might interpret a mandatory retirement age of 67 as a standard to aspire to.

Moreover, Prof. Munnell adds, “nothing would prevent employers” from asking high performers to stay past a mandatory retirement age. Under the old system, scrapped in the 1980s, employers had the discretion to retain an older worker on a year-by-year basis, she says. If a mandatory retirement age were reinstated, she says, she would advocate similar flexibility.

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