

Removing the Disincentives in Social Security for Long Careers

Gopi Shah Goda
John B. Shoven
Sita Nataraj Slavov

National Bureau of Economic Research
December 2006

Policy Abstract

Since Social Security was instituted in 1935, life expectancy at age 20 has increased from 66 to 76 for men; and from 69 to 80 for women. Health at older ages has also improved. Such dramatic advances in health and longevity mean that people have the physical and mental capability to work until older ages. Yet people are retiring younger, even as they live longer and healthier lives. Indeed the duration of retirement has grown by even more than the increase in life expectancy at retirement. This study considers the role of Social Security policy in influencing – or more precisely distorting – the work and retirement decisions of older workers. It highlights the features of Social Security that discourage long careers, discourage work at older ages, and increase the number of years in retirement. The main finding of the paper is that Social Security imposes high implicit tax rates on workers late in their careers. As a result of this distortion, the duration of retirement is suboptimally long, compounding the financial stress on public and private retirement support systems. The study also illustrates how some specific policy reforms could level the implicit tax rates associated with the Social Security benefit formula, and eliminate the disincentives for long careers.