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## **POLICY BRIEF**

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# **EARLY RETIREMENT: THE DAWN OF A NEW ERA?**

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## EXECUTIVE SUMMARY

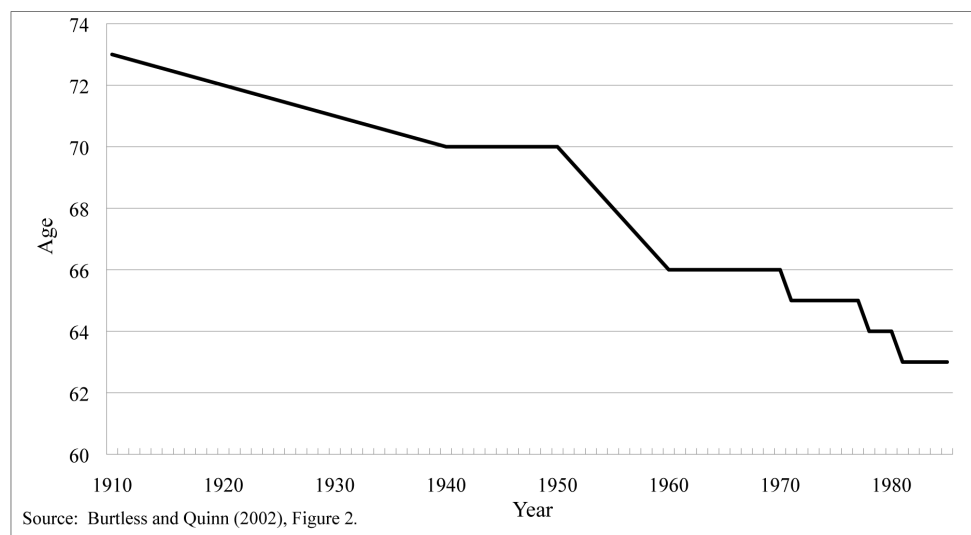
Americans reaching traditional retirement ages during the past two decades and today face a different retirement environment than did prior cohorts. Mandatory retirement has been eliminated for the vast majority of American workers, and important work disincentives (or retirement incentives) in Social Security and in employer pension plans have been eliminated or reduced. Americans are living longer and healthier lives, fewer have physically arduous jobs, and technology has increased the options about where and when people work. In addition, the age of eligibility for ‘full’ Social Security retirement benefits has been increased from 65 to 66 (and will soon increase to 67), which is equivalent to an across-the-board benefit cut, and fewer firms are offering employer-sponsored post-retirement health insurance. There are concerns about the future of Social Security, Medicare and Medicaid. Some of these changes are good news for older workers and some bad, but they all have altered the relative attractiveness of work and leisure late in life in favor of work.

In response to a very different environment, retirement patterns have changed dramatically since the mid 1980s. A century-long trend toward earlier and earlier retirement by American men has come to a halt and has subsequently reversed. Among older women, there was a similar break in trend, and many more older men and women are working today than the pre-1980s trends would have predicted. In addition, the majority of Americans retire not all-at-once, but gradually, in stages, utilizing bridge jobs between full-time career employment and complete labor force withdrawal. Since the structural changes we describe are not about to be reversed, we think that recent trends are a good guide for the near future. We have entered a new era of retirement, which, we argue, is mostly good news – for the individuals themselves, for employers, and for the nation as a whole, facing the challenges of an aging society.

**INTRODUCTION**

The story of retirement among American men during most of the past 130 years has been a simple and straightforward one - men left the labor force at younger and younger ages over time. Dora Costa (1998: 7-8) has estimated that in 1880, nearly 80 percent of men aged 65 and older and 95 percent of men aged 55 to 64 were employed. By 1940, these participation rates had declined to near 40 and 80 percent, respectively, and by 1985, they had dropped further to 16 and 68 percent. Gary Burtless has documented the same phenomenon in a different way, estimating the average age of retirement for American men over time, defined as the earliest age at which 50 percent of that population is out of the labor force.<sup>1</sup> As seen in Figure 1, half of the 73 year-old American men were still working in 1910. This average age of retirement dropped to 70 by 1940, to 66 by 1960, and to 63 by the mid-1980s - a decline of 10 years over a 75-year period.

**FIGURE 1**  
**AVERAGE RETIREMENT AGE OF MEN, 1910 - 1985**



One purpose of this Policy Brief is to show that this century-old trend toward earlier and earlier retirement is over, and, in fact, has been over for more than two decades.<sup>2</sup> American men and women are now leaving the labor force later than their predecessors did, not earlier, and many more older Americans are working today than prior trends would have predicted.

Which of these historical experiences is the better guide for the retirement trends of the future - a century of earlier labor force departure over time, or the subsequent quarter century showing just the opposite? To answer this question, we must ask why this dramatic change in trend occurred. We will argue below that it is a logical response to an equally dramatic change in the retirement environment - important structural changes that have altered the relative attractiveness of work and leisure late in life in favor of work. We will also describe *how* Americans retire - how they leave their career jobs - and show that most do *not* leave career employment and the labor force at the same time; rather, most utilize transitional bridge jobs, often part-time, on the way out. Since the environmental changes we will describe are unlikely to be reversed, we see the more recent retirement experience as the better guide for the future. We have indeed entered a new era of retirement; one that we think is mostly good for the nation, for employers, and for older workers themselves.

**RETIREMENT TRENDS – WHY DID THEY REVERSE?**

Considerable research has focused on the long run decline in elderly labor force participation rates. The simplest explanation is rising per capita income. With more earning power, workers enjoyed additional lifetime consumption, both material goods and hours of leisure (hours one could now afford *not* to work). Over time, Americans entered the labor force later (usually after additional schooling), worked fewer hours per week while in the labor force, and retired earlier (that is, ‘purchased’ more hours of leisure late in life.) Costa (1998: 57) considers rising incomes to be the primary explanation before 1940, after which another important determinant appeared - retirement income.

In the post-war period, Social Security and defined-benefit employer pension plans grew in prominence, and provided a predictable income stream for those who left the labor market. And within these public and private pension plans was another factor - a subtle set of financial incentives that often penalized workers who stayed on the job or in the labor force too long.

Social Security is a defined-benefit plan, as were most employer pensions prior to the 1980s. Several variables are factored into a formula (usually including the number of years of employment and some measure of average earnings; in private plans, often over the last few years on the job) to determine one's annual pension benefit. Changes in these variables change the pension amount.

Once eligible for an employer pension, a worker can claim it, or decline it and continue to work. In the latter case, the bad news is that one usually receives no pension benefits during that time; the good news is that one continues to earn a paycheck AND a higher annual pension benefit when it is finally claimed. This option raises an interesting question: which pension stream is worth more, a larger number of smaller checks (from claiming benefits now) or a smaller number of larger checks one would receive by (for example) working another year and claiming benefits a year later? One can calculate the present discounted value (PDV) of both streams - the size of the asset today which, if invested at current interest rates, could provide exactly the income stream under consideration. One can imagine benefit calculation rules in which the PDV of the pension stream increased with delayed receipt and additional work, in which case one would both earn a paycheck AND an increase in lifetime pension benefits by working another year. Alternatively, one could create benefit calculation rules that are actuarially fair, meaning that the PDVs of the two pension streams are the same; the pension increments following an additional year of work are just sufficient to make up over time for that initial year's foregone benefits. Finally, pension rules could be designed to penalize those who work another year, by offering pension increments that are worth less, over the expected lifetime, than the benefits foregone during that initial year's work. In this case, the worker would earn a paycheck (say, \$50,000) but lose lifetime pension benefits (say, -\$8,000) by working another year. Given these hypothetical numbers, this worker's true compensation would be only \$42,000 that year, and s/he would have suffered a surreptitious pay cut of \$8,000 by becoming age-eligible for pension benefits.

Research has established that both Social Security (at age 65) and most defined-benefit employer pensions, often at the earliest age of pension eligibility, followed this third scenario. The PDV of the pension stream *declined* with additional work, and the worker's true annual compensation fell by the loss in lifetime benefits.<sup>3</sup> The combination of lifetime Social Security and employer pension losses could be large, and provided a significant work disincentive or, equivalently, a retirement incentive.<sup>4</sup>

In addition, these financial incentives (a carrot) were often combined with a big stick, mandatory retirement provisions which required many workers (40 to 50 percent of the U.S. work force in the early 1970s) to leave their jobs at a particular age, usually age 65 (von Wachter, 2009). Although employees covered by these provisions were not required to leave the labor force, just that job, few could find another position that matched what they were forced to leave. Not surprisingly, many workers who could afford to retire and who were penalized if they did not, chose to do so when these regulations and/or incentives went into effect.<sup>5</sup>

So, what changed since the mid-1980s? Not the long-run growth in the nation's wealth. In fact, the U.S. enjoyed two decades of strong economic growth, with the exception of modest and short-lived recessions in the early 1990s and in 2001. The unemployment rate dropped from near 10 percent in 1982 and 1983 to near 5 percent by 1989, and to 4 percent by the year 2000. Disposable personal income per capita rose dramatically throughout this period, even during the early 1990s, more than doubling between 1980 and 1990 (from \$2,003 to \$4,250 in constant 2005 dollars), and more than doubling again by 2004 (to \$8,889) and reaching \$10,806 by 2008 - a more than five fold increase in less than three decades.<sup>6</sup> This economic growth generated demand for labor of all types - good news for older workers who wanted to remain employed. For most, the growth in income also increased Social Security and employer pension benefits - good news for older workers who wanted to retire.

In addition to this positive economic news, which, sadly, came to a screeching halt in 2008, there were many other important structural changes. Mandatory retirement was first delayed from age 65 to 70 and then, in 1986, outlawed by Congress for most American workers - good news for those who wanted to stay on their jobs past age 65 or 70. Social Security benefit calculation rules were changed, and became close to actuarially fair after age 65, no longer penalizing workers if they delayed accepting benefits past their normal retirement age - more good news for those who wanted to remain employed.<sup>7</sup> Many defined-benefit (DB) employer pension plans continued to decrease the lifetime benefits of eligible workers who stayed on the job too long, but these plans became less and less important over time. Defined contribution (DC) plans were on the rise. In 1988, only a quarter of those with an employer pension had primary coverage in a DC plan; by 2006, two-thirds did (EBRI 2009, table 5.) DC plans are like savings accounts, and are age-neutral by nature. Employers cannot reduce the value of a DC account if an employee chooses to work for another year, as they can, in essence, in a DB plan. Another strong work disincentive late in life has been reduced, although not completely eliminated.

Older Americans are healthier, on average, than prior cohorts and life expectancies continue to increase.<sup>8</sup> Jobs are becoming less physically demanding and there have been many technological innovations (for example, in computers and hearing aids) that increase the work options of older Americans - all good news for those who want to keep working.<sup>9</sup>

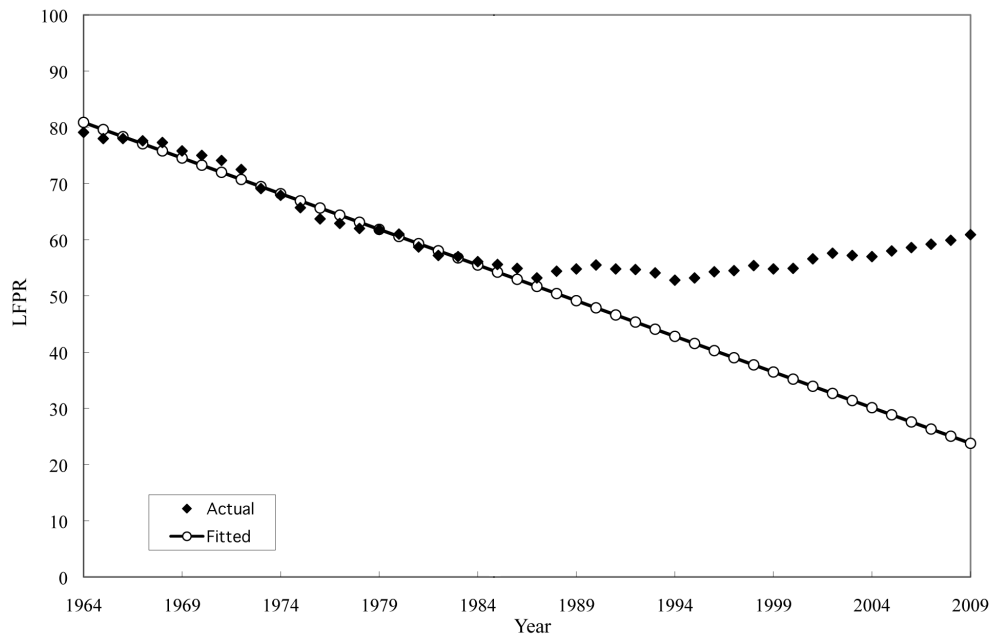
Finally, more women are working now than in prior cohorts. Married women are on average about three years younger than their husbands, and often have fewer years in the labor market. If couples choose to retire simultaneously, this may involve delayed retirement for husbands.

On the negative side of the ledger, the prevalence of employer-sponsored health insurance after retirement is declining, with the percentage of private-sector workers employed by firms with such coverage for new retirees dropping from 31 to 21 percent between 1997 and 2004.<sup>10</sup> In addition, Social Security benefits have been decreased across the board, as the Normal Retirement Age increased from 65 to 66, and eventually will increase to 67.<sup>11</sup>

Most of these changes, such as the demise of mandatory retirement and Social Security work disincentives and improvements in health and life expectancy, are good news for older Americans. Others, like the decline in employer-sponsored post-retirement health coverage and the delays in the Normal Retirement Age, are bad news. But they all have altered the relative attractiveness of work and leisure late in life in the same direction - in favor of work. The retirement environment has been fundamentally altered, and one might expect retirement behavior to change as well. And so it has.

Figure 2 shows the labor force participation rates (LFPRs) for American men aged 60 to 64 from 1964 to 2009. From 1964 to the mid-1980s, these LFPRs were declining steadily and rapidly, by more than one percentage point per year. In Figure 2, that very strong linear time trend (from 1964 to 1985) has been extrapolated to the present, and compared to what actually happened. One can easily see the dramatic break in trend. Not only did a century-old trend come to a halt, it actually turned around, and these male LFPRs began to increase, although modestly. A LFPR that dropped by 23 percentage points (nearly 30 percent) from 1964 to 1985 rose by 5 points by 2009 (a 10 percent increase). This same break in trend can be seen among younger men (55 to 59) and older (65 to 69, where the post-1985 increase is much larger, and men aged 70+).<sup>12</sup>

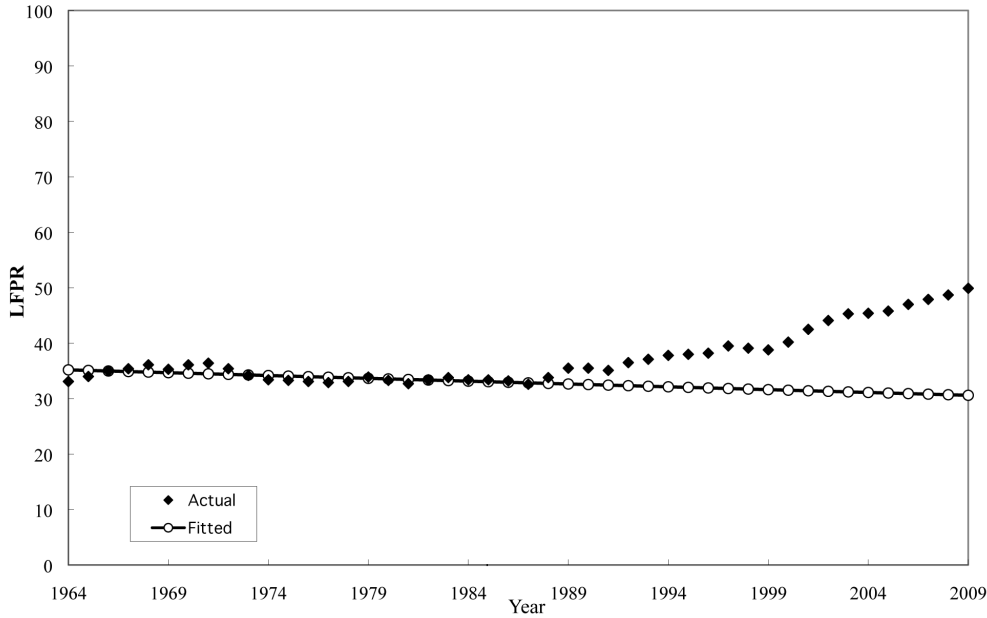
**FIGURE 2**  
**LABOR FORCE PARTICIPATION RATES**  
**ACTUAL AND FITTED VALUES**  
**MALES, AGED 60 - 64**  
**1964 - 2009**



Source: U.S. Bureau of Labor Statistics and regression by authors.

The experiences of women aged 60 to 64 (in Figure 3) are initially very different from those of men, but then very similar. The trend between the mid-1960s and mid-1980s is very different - almost flat rather than the sharp decline seen in Figure 2.<sup>13</sup> But the break from trend is equally stark. A participation rate that was almost unchanged over 2 decades rose by nearly 50 percent since 1985 (from 33 to 50 percent). The graphs are similar and equally dramatic for younger (55 to 59) and older women (65 to 69 and 70+). It is clear, as mentioned above, that many more older American men and women are working today than prior trends would have predicted.

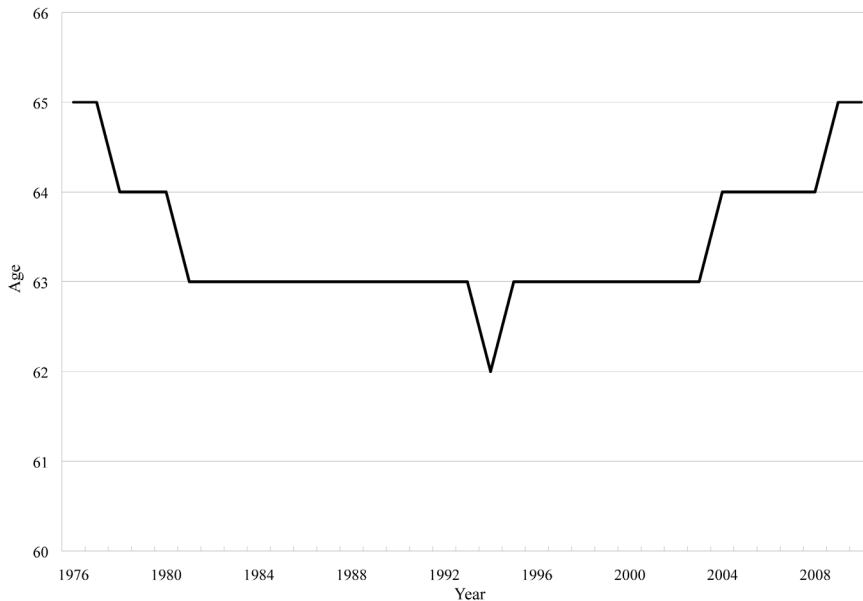
**FIGURE 3**  
**LABOR FORCE PARTICIPATION RATES**  
**ACTUAL AND FITTED VALUES**  
**FEMALES, AGED 60 - 64**  
**1964 - 2009**



Source: U.S. Bureau of Labor Statistics and regression by authors.

The same reversal in trend can be seen in the continuation of the data on the average age of retirement (the earliest age at which fewer than half of the people that age are in the labor force) shown in Figure 1. Figure 4 illustrates the average retirement age from the mid-1970s through the 1980s, and then through 2010, courtesy of Gary Burtless. The symmetry is remarkable, as the average retirement age rises from 63 to 64, and, in 2009, returns to age 65.

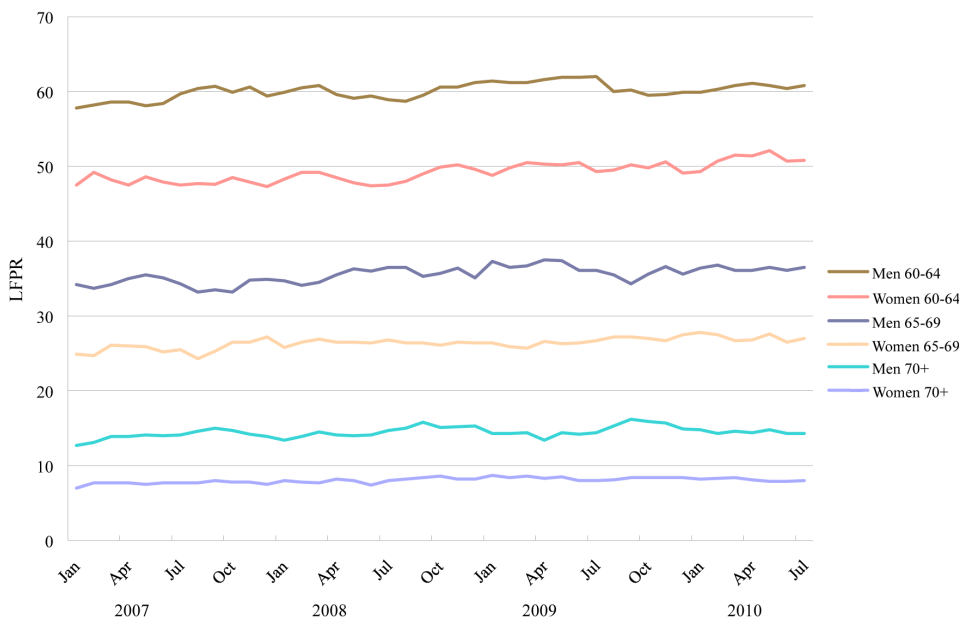
**FIGURE 4**  
**AVERAGE RETIREMENT AGE OF MEN, 1976 - 2010**



Source: Burtless and Quinn (2002), Figure 2, updated by Gary Burtless.  
 Note: 2010 Data through June.

How might the current recession affect these trends? The demand for labor by employers is down and slow to recover, but the labor supply by older workers is undoubtedly up. Those still working are less likely to leave a job in this economic environment, and some who have retired and seen their retirement assets decline in value would like to return. The data thus far suggest that the increases in the participation rates of older men and women since the mid-1980s have not reversed, though they may have flattened out. Figure 5 shows monthly participation rate data from January of 2007 (18 months before the stock market crash in October 2008) through July 2010, for men and women aged 60 to 64, 65 to 69, and 70 and older. In every case, the July 2010 rate is at least as high as the January 2007 rate, as are the January 2010 rates, if one is worried about seasonal factors. So far, these new participation rate trends have survived the worst job market recession since the 1930s.

**FIGURE 5**  
**MONTHLY LABOR FORCE PARTICIPATION RATES**  
**BY GENDER AND AGE**  
**JANUARY 2007 - JULY 2010**



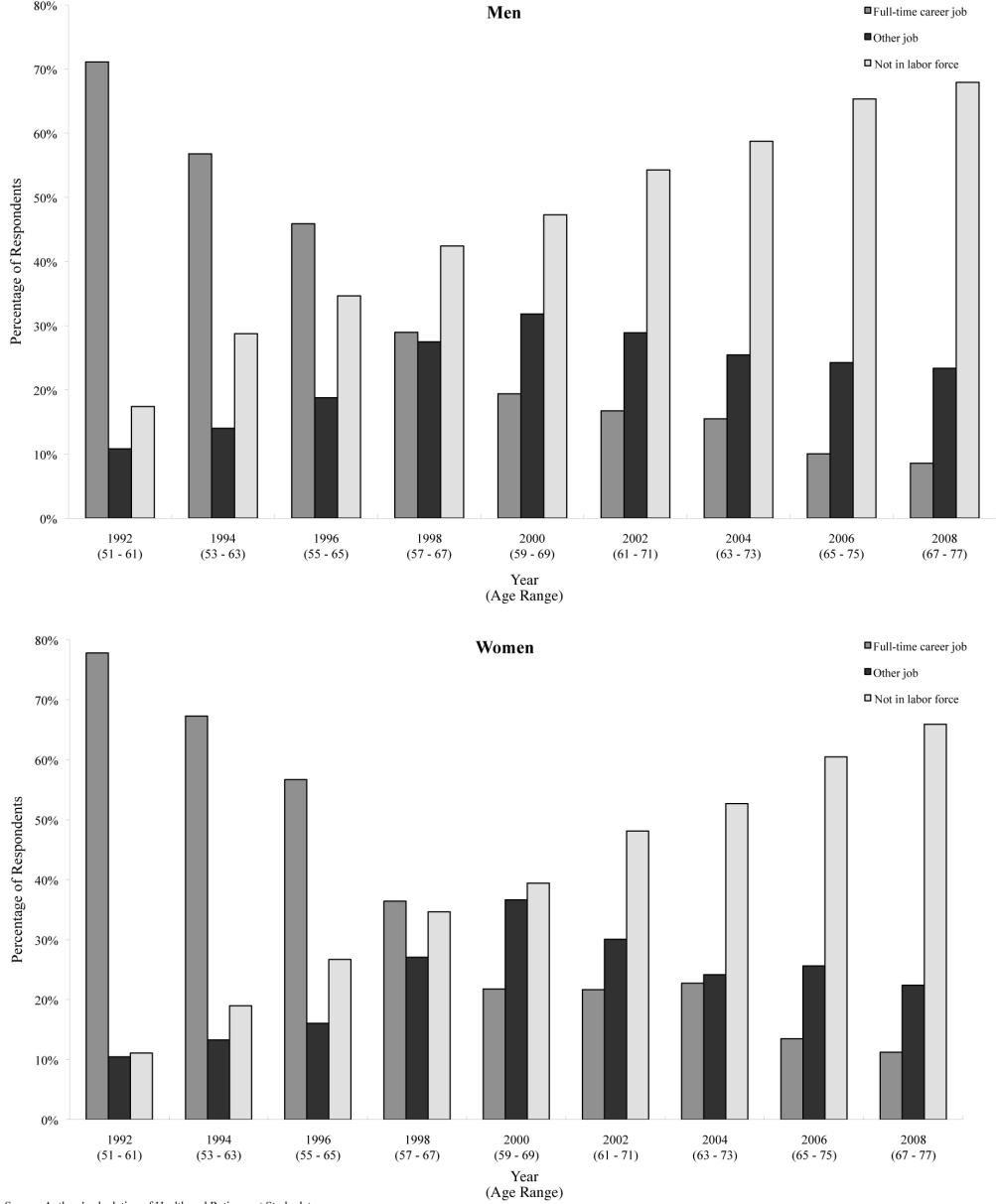
Source: U.S. Bureau of Labor Statistics.

**RETIREMENT PATTERNS – THE IMPORTANCE OF BRIDGE JOBS**

Researchers have investigated not only *when* workers leave the labor force (later than they did two decades ago) but also *how* they do so. Do Americans tend to retire all at once, or gradually, in stages? We have used the longitudinal Health and Retirement Study (HRS) to analyze workers on full-time career jobs, and followed them through time - from 1992 to 2008, with detailed surveys every other year.<sup>14</sup> As seen in the subsequent HRS cross-sections in Figure 6, as the respondents age (from ages 51 to 61 in 1992 to ages 67 to 77 in 2008), the percentage of the sample still on a full-time career job declines (from 71 to 9 percent for men, and from 78 to 11 percent for women), while the percentage out of the labor force increases (from 17 to 68 percent of the men and from 11 to 66 percent of the women). Note, however, the importance of “other jobs” - continued employment in something other than the career job. It rises to a maximum of 32 percent of the men and 37 percent of the women when the HRS respondents are aged 59 to 69, but still remains significant (more than 20 percent of the sample) even among those aged 67 to 77.



**FIGURE 6**  
**LABOR FORCE STATUS, BY YEAR AND GENDER**  
**HRS RESPONDENTS WITH A FULL-TIME CAREER JOB SINCE AGE 50**  
**1992 - 2008**



Source: Authors' calculation of Health and Retirement Study data.

To see how Americans leave the labor force, we analyzed the HRS respondents who were employed in full-time career (FTC) jobs after age 50 and observed them through 2008. By then, as seen in Figure 6, nearly all (91 percent of the FTC men and 89 percent of the FTC women) had left these career jobs. What had they done upon departure? Some left the labor force but others moved to another job - a bridge job - either part-time or full-time but of less than “career job” duration. As seen in Table 1, 32 percent of these men were still working in 2008, with 9 percent still on their FTC job and 23 percent on a subsequent job. The other two-thirds (65 percent) were out of the labor force. Of those, 34 percent left directly from a FTC job, while 31 percent went first to a bridge job, which they then left.<sup>15</sup> When we combine all the men who had left their full-time career jobs by 2008 (noted in **bold** in Table 1), we see that 61 percent of them [54/88] moved to a bridge job. Among the women with a FTC job since age 50, we find almost identical results - 60 percent [51/85] left the career job not for complete retirement, but for another job. Slightly more than half of these bridge jobs were part-time positions.

**TABLE 1**  
**EMPLOYMENT STATUS IN 2008, BY GENDER**  
**SAMPLE: HRS INDIVIDUALS WITH A FULL-TIME CAREER JOB SINCE AGE 50**

	Sample size	Full-time career job	Bridge job	<i>percent part time</i>	Don't know	% with bridge job
Men, Working	834	9%	<b>23%</b>	54%	1%	
Men, Nonworking, Last job was	<u>1,766</u>	<b>34%</b>	<b>31%</b>	50%	<u>3%</u>	
Total	2,600	43%	54%		3%	61%
Women, Working	778	11%	<b>22%</b>	56%	1%	
Women, Nonworking, Last job was	<u>1,508</u>	<b>34%</b>	<b>29%</b>	56%	<u>3%</u>	
Total	2,286	45%	51%		4%	60%

Source: Authors’ calculations from the Health and Retirement Study.

In recent research, we compared the retirement experiences of a subset of the original HRS respondents (those aged 59 to 64 in 2000) with a younger cohort subsequently added to the HRS (aged 59 to 64 six years later, in 2006) (Giandrea, Cahill and Quinn, 2009). We found a small increase in bridge job behavior over time. About 64 percent of the younger group who had left their FTC jobs moved first to a bridge job (63 percent of the men and 65 percent of the women), compared to 60 percent of the older cohort (58 percent of the men and 62 percent of the women).<sup>16</sup> Six years is a small time difference, but the data do suggest that the prevalence of bridge jobs and gradual retirement may be increasing over time. In any case, there is no evidence that it is declining in importance among older American workers.

Who is more likely to utilize a bridge job on the way out of the labor force? In Tables 2 through 4, we show some correlates of bridge job activity among the older HRS sample. It is not surprising that the younger people are when leaving career jobs, the more likely they are to move to a bridge job rather than directly out of the labor market (Table 2). The decline is monotonic for women, from 78 percent of those aged 55 or younger at the time of transition down to 49 percent of those aged 65 or older. For men, the percentage utilizing a bridge job drops from 76 percent of those aged 55 or younger to 59 percent for those 56 to 64 and then a slight rise to 62 percent among those 65 and older.

**TABLE 2**  
**FIRST TRANSITIONS FROM CAREER JOBS BY 2008**  
**THOSE WITH FULL-TIME CAREER JOBS IN 1992, BY GENDER AND AGE**  
**(HORIZONTAL PERCENTAGE AND RATIO)**

Age	Sample Size	Still on Career Job	Moved to Bridge Job	Moved to No Job	Ratio of Bridge Job/ (Bridge Job + No Job)
<b>Men</b>					
<= 55	419	0%	76%	24%	76%
56-61	1016	1%	59%	40%	59%
62-64	405	2%	58%	41%	59%
65+	468	37%	39%	24%	62%
<b>Women</b>					
<= 55	673	3%	75%	21%	78%
56-61	885	7%	54%	40%	57%
62-64	297	11%	45%	44%	51%
65+	208	43%	28%	29%	49%

Note: Percentages are based on 2,308 men and 2,063 women who were on a full-time career (FTC) job in 1992 and either (1) were still on their FTC job in 2008 or (2) had an observed transition prior to 2008. For individuals who made a transition by 2008, age is measured as of the survey wave prior to the transition; for individuals still on a FTC job in 2008, age is measured as of the 2008 survey date.  
 Source: Authors' calculations from the Health and Retirement Study.

Table 3 illustrates the importance of health (subjective, self-defined) at the time of transition. The better the person's health at the time of departure from a FTC job, the more likely a move to a bridge job - from nearly 70 percent of those in "excellent or very good" health, to 60 percent of those in "good" health and only about half of those in "fair or poor" health.

**TABLE 3**  
**FIRST TRANSITIONS FROM CAREER JOBS BY 2008**  
**THOSE WITH FULL-TIME CAREER JOBS IN 1992, BY GENDER AND HEALTH STATUS**  
**(HORIZONTAL PERCENTAGE AND RATIO)**

Subjective Health Assessment	Sample Size	Still on Career Job	Moved to Bridge Job	Moved to No Job	Ratio of Bridge Job/ (Bridge Job + No Job)
<b>Men</b>					
Excellent or very good	1,244	7%	62%	30%	67%
Good	729	9%	55%	36%	60%
Fair or poor	335	9%	47%	44%	51%
<b>Women</b>					
Excellent or very good	1,134	9%	63%	29%	69%
Good	643	12%	54%	35%	61%
Fair or poor	286	10%	42%	48%	47%

Note: See note on Table 2.  
 Source: Authors' calculations from the Health and Retirement Study.

Perhaps the most interesting finding concerns socio-economic status, measured here by the wage rate on the career job. Men and women at both ends of the wage distribution were more likely to utilize bridge jobs on the way out than those in the middle - more than 70 percent of those making either less than \$10 per hour or more than \$50 per hour moved to a bridge job, compared to 60 percent of those making between \$20 and \$50 per hour. Answers to questions about why these people were still working suggest that those at the upper end were working because they wanted to (it was a life style choice) while those at the bottom were doing so because they had to (for the pay and/or the medical coverage.)

**TABLE 4**  
**FIRST TRANSITIONS FROM CAREER JOBS BY 2008**  
**THOSE WITH FULL-TIME CAREER JOBS IN 1992, BY GENDER AND WAGE RATE**  
**(HORIZONTAL PERCENTAGE AND RATIO)**

Wage Rate	Sample Size	Still on Career Job	Moved to Bridge Job	Moved to No Job	Ratio of Bridge Job/ (Bridge Job + No Job)
<b>Men</b>					
< \$6/hour	114	16%	63%	21%	75%
\$6 - \$10/hour	220	11%	65%	24%	73%
\$10 - \$20/hour	798	8%	56%	36%	61%
\$20 - \$50/hour	1011	6%	56%	38%	59%
> \$50/hour	147	14%	61%	26%	70%
<b>Women</b>					
< \$6/hour	131	8%	66%	27%	71%
\$6 - \$10/hour	402	13%	60%	27%	69%
\$10 - \$20/hour	966	10%	54%	36%	60%
\$20 - \$50/hour	505	8%	55%	37%	60%
> \$50/hour	40	8%	75%	18%	81%

Note: See note on Table 2. Wage rate could not be determined for 18 men and 19 women.

Source: Authors' calculations from the Health and Retirement Study.

In summary, Americans approaching traditional retirement ages are making decisions in a very different environment than prior cohorts did. Today's older workers do not face mandatory retirement provisions, or a Social Security system that discourages work after age 65. Those with employer pension coverage live in a world of primarily defined-contribution plans, which, unlike defined-benefit plans, have no age-specific work or retirement incentives. They are healthier and living longer than prior generations, are less likely to hold physically-demanding jobs, and they enjoy the benefits of technological innovations that broaden their work options. As a result, today's older Americans are, on average, working longer than their predecessors, with the majority moving to a bridge job after they leave career employment.

### A LOOK AHEAD

We do not anticipate that these important structural changes will be reversed. Mandatory retirement and Social Security work disincentives are gone, and are unlikely to return. We do not foresee a resurgence of defined-benefit pension plans or employer-sponsored retiree health plans or an increase in the number of physically arduous jobs. Improvements in life expectancy and age-adjusted health are likely to continue, although some have warned that the obesity epidemic may threaten these trends.<sup>17</sup> Because of the permanency of these changes, we think that recent retirement trends are a good guide for the near future. Surveys of current workers support this view. In the 2010 EBRI Retirement Confidence Survey, 70 percent of the workers surveyed said that they planned to work for pay in retirement. In a 2010 MetLife survey, nearly 60 percent of workers said they plan to work beyond age 65.<sup>18</sup> Although these responses (60 to 70 percent) are not credible predictions for the near future (the actual labor force participation rate for those aged 65 to 69 in 2009 was only 31 percent), they do suggest a new attitude toward the appropriate mix of work and leisure late in life. We have indeed entered a new era of retirement in the United States.<sup>19</sup>

These labor supply patterns of older Americans - later and gradual retirement - are generally good news for the individuals making these decisions, for their employers, and for the nation as a whole. For individuals, these patterns show flexibility - the ability to respond to a changing environment.<sup>20</sup> There are legitimate concerns on the horizon. Social Security benefits might well be reduced (from what they would be under current regulations) or delayed (either further delays in the normal retirement age - equivalent to an across-the-board benefit cut - or a much more controversial delay in the age of earliest eligibility). Defined-contribution plans, although much more portable than traditional defined-benefit plans, can subject employees to significant market risk if they do not appropriately adjust their investment

portfolios as they age. Employer-sponsored retiree health insurance plans are in decline and Medicare and Medicaid are under increasing financial pressure. Individuals have little or no control over Social Security or Medicare legislation, or the employee benefit decisions of their employers. For older workers it is too late to have a significant impact on asset accumulation - the important savings decisions were made decades ago. The one thing that older workers can control late in life is their labor supply - the timing and manner of their withdrawal from the labor market.

Continued work late in life, especially if full time on a career job, has significant financial advantages. The most obvious is the additional earnings, which can translate into increased assets if some of the income is saved. Annual Social Security benefits will be higher the later they are claimed. In addition, the number of years over which assets will be drawn down in retirement is smaller the later they begin. Munnell and Sass (2008) consider an individual who works from age 20 to age 60, and then is retired until age 80, working two years (40 in all) for each year of retirement (20). With 5 additional years of work, to age 65, the ratio of work years to retirement years rises by 50 percent, from 2:1 to 3:1. A study by the Congressional Budget Office (2004) on retirement age and the need for savings compares retirement income needs (estimated to be 80 percent of pre-retirement income) and Social Security benefits for couples and single persons at the 25<sup>th</sup>, 50<sup>th</sup> and 75<sup>th</sup> percentile of their income distribution. The authors calculate the difference between income needs and Social Security benefits if the benefits are claimed at age 62, 66 or 70, as well as the assets needed at age 62 to fill that income gap between the retirement age and life expectancy. The differences are dramatic because of the increase in Social Security benefits during those years of continued work and delayed benefit receipt. For example, a median-income couple, needing approximately \$47,000 (all in 2004 dollars) in annual after-tax income, has a gap of about \$27,000 if Social Security is claimed at age 62, \$19,000 at age 66 and less than \$9,000 if claimed at age 70. The assets needed at age 62 to fill these income gaps at retirement drop from over \$500,000 (for retirement at age 62) to less than \$250,000 (for retirement at age 66) to only about \$50,000 (for retirement at age 70).

In addition to the obvious financial benefits, there is evidence that continued work can also positively affect one's health and life satisfaction. Wang et al. (2009), summarizing the existing literature on health and retirement, report that those who moved to bridge jobs were healthier than those who did not, even after controlling for pre-retirement health status. In addition, those who continued to work, even with reduced hours, had better mental health outcomes than those who withdrew from the labor force completely. Dave et al. (2008), using the HRS sample, found that complete labor force withdrawal was associated with a deterioration in mental and physical health, beyond that of similar individuals who continued to work full time, but that these effects were mitigated if the individual continued to work part time.<sup>21</sup>

Given the uncertainties and concerns about the retirement environment ahead, an individual who can work longer is wise to contemplate doing so. The evidence discussed above shows that older Americans are already making these choices. Since successful retirement requires appropriate coping skills, gradual withdrawal from the labor market may be a better strategy than the stereotypical all-at-once departure, directly from a full-time career job to complete retirement. Phased withdrawal offers an opportunity to develop the personal interests that can make retirement a rewarding experience, and provides supplementary income during the transition.

Continued work is not the answer for all, however. Some older workers have health problems that prevent or limit the type or amount of work that they can do, or have outmoded skills or live in an area of depressed labor market demand. Census data from 2008 reported in AARP (2009) suggest that about 11 percent of Americans aged 21 to 64 have a work disability, and the prevalence rises dramatically with age, from only 5 percent of those aged 21 to 29, to 16 percent at ages 50 to 59 and 26 percent at 60 to 64, and presumably higher for those 65 and above.

These issues are central to a very important policy debate - whether the earliest age of eligibility for Social Security retirement benefits, which has been age 62 since 1956 for women and since 1961 for men, should be increased. As the normal retirement age (NRA) is raised, to 66 and soon to 67, the actuarial reduction for those claiming early retirement benefits also increases (from 20 percent when the NRA was 65 to 30 percent when it reaches 67), and early recipients are permanently locked into lower annual benefits. As Americans live longer and healthier lives, on average, one is tempted

to encourage later retirement, for the reasons noted above. But on average does not mean all, and some older Americans, currently waiting to turn age 62 to collect Social Security benefits, would be hard pressed to wait another 1 to 3 years. Changes in Social Security disability definitions could soften this blow for those in poor health, but would not for those with outmoded skills or in the wrong labor market. Changing the early retirement age would be a significant change in the retirement environment, more dramatic than delaying the normal retirement age, and one that would certainly encourage more of the later retirements that we have already observed.

For employers, older Americans (especially those in this large baby-boom cohort) provide a pool of experienced workers, many of whom would like to remain active in the labor force, although perhaps not on a career job, perhaps only part-time, perhaps self-employed, and perhaps in a new location or in varied locations during different parts of the year. Some analysts anticipate labor market shortages on the horizon, as a large retiring population is replaced by a smaller cohort of labor market entrants. In particular occupations, these shortages may be acute.<sup>22</sup> Firms that offer appropriate flexibility regarding hours and levels of responsibility may find that older workers meet their needs.

Finally, delayed retirement is good for the nation as a whole. People do not consume Social Security checks, pension benefits or accumulated savings; rather, they consume the goods and services that are currently being produced by the working population. One challenge in an aging society is to produce sufficient output as an increasing proportion of the population moves out of the labor force.<sup>23</sup> That proportion depends on the age distribution, over which we have little control, but also on the labor supply decisions that older Americans make. As we have seen, these decisions are not set in stone, but rather are very much a function of the retirement environment in which these choices are made. Active older workers continue to produce goods and services, increasing the amount to be allocated among the working and non-working populations, and thereby easing the burdens faced by an aging society.

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**ENDNOTES**

- 1 This graph first appeared in Burtless and Quinn (2002), with data through 2001. Gary Burtless has updated it with data through 2010, which appear later in this Policy Brief.
- 2 This Policy Brief draws upon and updates material that appears in Cahill, Giandrea and Quinn (2006, 2007), Giandrea, Cahill and Quinn (2009) and Quinn (2010).
- 3 Quinn and Burkhauser (1983: Tables 1 and 2) showed that in the mid-1970s, Social Security and many employer defined-benefit pension plans imposed significant financial penalties on those who kept working and delayed retirement benefits at age 65. Kotlikoff and Wise (1989: 59) studied the pension accrual patterns of over 1,000 defined-benefit plans, and concluded that “for a large proportion of the plans, the accrual rate after (the earliest age of pension eligibility) is a sizable negative number. (I)t would not be unusual for the reduction in pension benefit accrual after the age of early retirement to be equivalent to a 30 percent reduction in wage earnings.” Olivia Mitchell (1992) reported that about two-thirds of workers in the late 1980s whose employer benefits were reduced for early retirement faced rules that were less than actuarially fair, thereby encouraging workers to claim benefits, and leave the firm, as soon as they were eligible.
- 4 Burkhauser and Quinn (1983: Table 2) showed that the larger the Social Security or employer pension wealth loss associated with continued work (the larger the decline in the present discounted value of the income stream following an additional year of work), the higher the probability of withdrawal from the job. Workers behaved as though they understood and responded to these subtle work disincentives – or retirement incentives.
- 5 Burkhauser and Quinn (1983: 351) also showed that much of what looked like a mandatory retirement effect on retirement at age 65 was actually the effect of these strong age-specific retirement incentives that often went into effect at the same age, and which did not disappear when mandatory retirement was outlawed.
- 6 The unemployment rate and per capita disposable (after tax) personal income data are drawn from the *Economic Report of the President, 2010*, tables B-42 and B-31.
- 7 Those eligible for Social Security who declined receipt and worked another year earned higher annual benefits when they later claimed them for two reasons: their average indexed monthly earnings, on which benefits are based, generally rose, and Social Security offered an additional delayed retirement credit - a reward for declining benefits for a year. Over a 20 year period, this credit for those aged 65 to 70 increased from 3 to 8 percent per year of delay. The 8 percent is about actuarially fair for someone who lives his or her life expectancy, meaning the future increments just about compensate for the benefits initially forgone. The present discounted values of the benefit streams are now about the same, so a potentially strong work disincentive (or retirement incentive) is gone. Between ages 62 and 65, the delayed retirement credit was always close to actuarially fair; it was only at 65 that this financial work disincentive appeared.
- 8 Manton (2008: 106) finds considerable evidence of improvements in the health of the elderly population in America and suggests that rate of improvement is increasing. He estimates that 81 percent of the U. S. population was not disabled in 2004, compared to 73.5 percent in 1982 (*ibid.*, table 1). Life expectancy at age 65 has increased by more than 5 years since 1940 and is predicted to rise by another 4 years over the next 70 years (Board of Trustees, 2010, table V.A4, intermediate estimates).
- 9 Bartel and Sicherman (1993) found that workers in industries with high levels of technological change retired later than similar workers in other industries, because of higher levels of on-the-job training in these industries. Conversely, they found that workers in industries that experienced unexpected technology advances retired earlier than similar workers in other industries. The technology shock resulted in a faster depreciation of workers’ human capital. Friedberg (2003) found that workers approaching retirement were less likely to use computers than similar younger workers, but that those older workers who did use computers at work were more likely to continue working than similar workers who were not computer users.
- 10 See Employee Benefit Research Institute (2008, figure 8). These numbers exaggerate the percentage of the employees who would actually receive these benefits, because eligibility requirements have become more restrictive over time (*ibid.*, p. 14). In addition, when firms still do provide this coverage, the retirees generally pay more of the premium than in the past.
- 11 The Normal Retirement Age (the age at which one is eligible for “full benefits” that are not actuarially reduced) is now 66 for those born during 1943 to 1954. Between 2017 and 2022, it will rise again, becoming 67 for all born in 1960 or later (Social Security Administration, 2009, tables 2.A17.1 and 2.A20.) Delayed receipt of “full benefits” is identical to an across-the-board benefit cut, because waiting longer for a given amount (“full benefits”) means getting less at any given age.
- 12 Between 1964 and 1985, the labor force participation rate for men aged 65 to 69 dropped from 42.6 to 24.4 percent, a decrease of 18.2 points, or 43 percent. From 1985 to 2009, that rate increased to 36.6 percent, which is 11.9 points or nearly 50 percent higher, although on a lower base.
- 13 This lack of trend reflects the net impact of two offsetting trends: older Americans leaving the labor force earlier, but women, especially married women, entering the labor market in increasing numbers during this time.
- 14 The Retirement History Survey initially interviewed about 12,600 Americans aged 51 to 61 in 1992, and has re-interviewed them and their spouses every two years since then (Karp 2007). We define a full-time career job as one held for 10 years or more, on which one works at least 1,600 hours per year. We also experimented with a requirement of 5 or 8 years tenure for a “career” job, and the qualitative results are very similar. Our sample includes those respondents who had held a full-time career job since age 50: 4,288 men and 3,144 women, in 1992. With attrition, these sample sizes declined over time, to 2,600 men and 2,286 women in 2008.

- 15 For a small number of men and women (about 3 percent of each), data deficiencies prevent us from determining the details of their labor market exit.
- 16 These percentages are slightly different from those reported above (61 and 60 percent for men and women) because here we are considering only a 6-year age span of the original HRS respondents, to be comparable to age span of the new respondents.
- 17 Manton (2008: 100-104, 106) notes that some experts question whether the trends of improving health and life expectancy will continue because of increases in obesity, especially among young adults.
- 18 See Employee Benefit Research Institute (2010) and MetLife (2010).
- 19 Bureau of Labor Statistics projections agree, at least in the medium run. Toossi (2009) predicts that the labor force participation rates of Americans aged 60 to 64, 65 to 74 and 75 and older will all increase significantly between 2008 and 2018, by 5.6 percentage points (from 54.1 to 59.7 percent), 5.4 percentage points (from 25.1 to 30.5 percent) and 3.0 percentage points (from 7.3 to 10.3 percent), respectively.
- 20 Maestas and Zissimopolous (2010: 157) make the same point, noting that "...the economic response is typically more adaptive than demographic determinism would suggest. Indeed, in the United States, a variety of economic forces - including changes in pensions, longer life expectancy, delay in disability onset and rising labor force attachment of women - are likely to push labor force participation at older ages higher even if there are no further changes in policy."
- 21 Given the difficulty of establishing the direction (or directions) of causation between health status and retirement decisions, it is not surprising that there are contrary results. Neuman (2008), using the HRS, studied changes in health after retiring or reducing hours of work, and found no evidence that self-perceived health deteriorated as a result.
- 22 Bluestone and Melnick (2010) argue that when the economy recovers, if baby boomers retire at the same ages as older workers before them have, there may not enough workers for the jobs available, especially in some service industries like health care, social assistance, and education.
- 23 The Bureau of Labor Statistics estimates and forecasts an economic dependency ratio, the ratio of those who are not in the labor force to those who are; in other words, how many non-workers are being supported by each worker. Between 2008 and 2018, this ratio is estimated to increase from .96 to 1.03 (Toossi (2009), Table 7).

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