

## INCENTIVIZING WORK AT OLDER AGES: THE NEED FOR SOCIAL SECURITY REFORM

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*The Social Security benefit structure discourages older individuals from working, leading to strain on the nation's economy and entitlement programs. In this Note, Mr. Zimmerman continues the debate on how Social Security should be reformed to encourage individuals to continue working. Mr. Zimmerman analyzes the history of Social Security and scrutinizes the various disincentives put on older individuals that prevent them from continuing to work as they age. Ultimately, Mr. Zimmerman offers solutions to reform Social Security and provides suggestions on incentivizing older individuals to work.*

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## I. Introduction

Imagine you are a sixty-five-year-old worker who just became eligible for Social Security. You can begin collecting benefits, but if you earn over \$4,000 in income, your entire Social Security benefit is eliminated.<sup>1</sup> One would think twice about risking Social Security benefits for a minor gain. This onerous penalty was once the law for initial beneficiaries of Social Security.<sup>2</sup> Although some of the disincentives to continue work have been removed from the Social Security program, many arguably remain. Workers are increasingly willing and able to work at older ages; however, certain laws discourage continued work by seniors. Specifically, Social Security has inherent disincentives toward work by seniors. Social Security laws should be reformed to incentivize, rather than discourage, work at older ages.

Incentivizing work at older ages should be an important policy goal for the United States. With a rapidly aging population, the economic and social well-being of the country depends on a high labor force participation rate among all citizens. The looming retirement of the baby boom generation further strains the nation's economic output and entitlement programs.<sup>3</sup> Based on the aging of the baby boomers, current analysis predicts that the number of retirees will double over the next thirty years.<sup>4</sup> Fewer individuals working as a percentage of the overall population reduces the labor force participation rate, and the rate is expected to decrease in the coming decades.<sup>5</sup> A lower labor force participation rate has negative effects on the U.S. economy because it results in fewer taxpayers and more dependent

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1. See Larry DeWitt, *Research Note #7: Brief History of the Retirement Earnings Test*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/ret.html> (last visited Nov. 2, 2011). The initial Social Security retirement earnings test subjected benefit recipients who continued to work to an extremely onerous penalty. *Id.* Workers earning over twenty-five percent of the minimum wage lost their Social Security benefit until they retired. *Id.* The \$4,000 calculation is twenty-five percent of the full-time minimum wage. *Id.*

2. *Id.*

3. Mitra Toossi, *Labor Force Projections to 2018: Older Workers Staying More Active*, 132 MONTHLY LAB. REV. 30, 30 (2009). The baby boom generation is defined as those born between 1946 and 1964. *Id.*

4. Liqun Liu & Andrew J. Rettenmaier, *Work and Retirement*, NAT'L CTR. FOR POL'Y ANALYSIS, Nov. 3, 2006, at 1, available at <http://www.ncpa.org/pdfs/bg162.pdf>.

5. Toossi, *supra* note 3, at 34.

individuals.<sup>6</sup> Besides impacting the economy, the aging of the boomers has important consequences for the public sector, especially the Social Security program.

The status of the government's largest program, Social Security, reflects America's demographic shift. For the first time since 1983, Social Security is expected to pay out more than it collects in payroll taxes in 2010.<sup>7</sup> Although the current economic recession affects the short term outlook for Social Security, the long term prognosis was problematic even before the financial crisis.

Social Security's prospects appear dire, but the government has discussed the possibility of reform. In February 2010, President Obama authorized the creation of a deficit reduction commission that would make recommendations for deficit reduction, including changes to Social Security.<sup>8</sup> Although no one can predict the sincerity of the proposals, the commission considered proposals and brought attention to Social Security reform.<sup>9</sup> The fiscal commission's final proposal did not gather the necessary support to receive a vote in Congress.<sup>10</sup> It did gain more support than anticipated, however, given the commission's recommendation for a future increase to the Social Security retirement age.<sup>11</sup>

Encouraging later retirement through Social Security reform improves the program's solvency.<sup>12</sup> Keeping individuals in the workforce has a number of other advantages: it increases income tax revenues, improves Medicare's finances, boosts economic output, and

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6. *See id.*

7. THE 2010 ANNUAL REPORT OF THE BOARD OF TRUSTEES OF THE FEDERAL OLD-AGE AND SURVIVORS INSURANCE AND FEDERAL DISABILITY INSURANCE TRUST FUNDS 2 (2010) [hereinafter 2010 ANNUAL REPORT], available at <http://www.ssa.gov/OACT/TR/2010/tr2010.pdf>.

8. *See Charter for the National Commission on Fiscal Responsibility and Reform*, NAT'L COMM'N ON FISCAL RESP. & REFORM, <http://www.fiscalcommission.gov/charter> (last visited Nov. 2, 2011).

9. *National Commission on Fiscal Responsibility and Reform*, N.Y. TIMES, Dec. 3, 2010, [http://topics.nytimes.com/top/reference/timestopics/organizations/n/national\\_commission\\_on\\_fiscal\\_responsibility\\_and\\_reform/index.html](http://topics.nytimes.com/top/reference/timestopics/organizations/n/national_commission_on_fiscal_responsibility_and_reform/index.html).

10. Brady Dennis & Lori Montgomery, *Deficit Plan Wins 11 of 18 Votes; More Than Expected, but Not Enough to Force Action*, WASH. POST, Dec. 3, 2010, <http://www.washingtonpost.com/wp-dyn/content/article/2010/12/02/AR2010120205913.html>.

11. *Id.* Senator Durbin, an influential Democratic Senator, surprised some by "explicitly endorsing a gradual increase in the retirement age from 67 to 69." *Id.*

12. Liu & Rettenmaier, *supra* note 4, at 18.

keeps the most experienced employees in the workplace.<sup>13</sup> A 2008 report found that “increasing the median retirement age from 62.1 to 64.1 by 2015 would add \$13 trillion to the economy over the next 30 years.”<sup>14</sup> Working longer also benefits the individual. “Delayed retirement gives people more time to earn, save, accumulate Social Security credits, and build more wealth in employer sponsored pension plans.”<sup>15</sup> Currently, the average retirement age is approximately sixty-three for men and sixty-two for women.<sup>16</sup> Boosting the average retirement age by a year or even several months would increase Social Security’s solvency and improve the economy.<sup>17</sup>

This Note examines the possibility of incentivizing work at older ages. Part II discusses the history of Social Security and the potential for employment by the elderly. Part III analyzes the specific Social Security disincentives towards work. Finally, Part IV recommends possible solutions to reform Social Security and incentivize work at older ages.

## II. Background

Social Security currently has aspects that discourage work at older ages. From the program’s inception it has included certain provisions that either legally discourage work or imply that work is not appropriate for seniors.<sup>18</sup>

### A. History of Social Security’s Disincentives Toward Work

The comprehensive 1937 book, *Social Security in America*, chronicles the creation of Social Security.<sup>19</sup> The book states some of the pri-

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13. *Id.* at 1.

14. David C. John, *Time to Raise Social Security’s Retirement Age*, BACKGROUND (Heritage Found., D.C.), Nov. 22, 2010, at 6, available at <http://heritage.org/Research/Reports/2010/11/Time-to-Raise-Social-Securitys-Retirement-Age>.

15. RICHARD W. JOHNSON ET AL., URB. INSTITUTE, WORK IMPEDIMENTS AT OLDER AGES 5 (2006), available at [http://urban.org/UploadedPDF/311313\\_work\\_impediments.pdf](http://urban.org/UploadedPDF/311313_work_impediments.pdf).

16. JOHN A. TURNER, CTR. FOR RET. RESEARCH, PROMOTING WORK: IMPLICATIONS OF RAISING SOCIAL SECURITY’S EARLY RETIREMENT AGE 1 (2007), available at [http://crr.bc.edu/images/stories/Briefs/wob\\_12.pdf](http://crr.bc.edu/images/stories/Briefs/wob_12.pdf).

17. See Liu & Rettenmaier, *supra* note 4, at 18.

18. See generally DeWitt, *supra* note 1.

19. Comm. on Econ. Sec., *Social Security in America*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/reports/ces/cesbook.html> (last visited Nov. 6,

mary purposes for enacting the legislation, such as: “[the retiree’s] advanced age or invalidity renders him incapable of an effective part in productive enterprise” and “his continuance at work prevents a younger man from filling his place and gaining occupational skill, experience, and promotion.”<sup>20</sup> Essentially, Social Security is based upon the premise that the elderly are incapable of work and take jobs from younger workers, thus decreasing the productivity of the economy.<sup>21</sup> Both of these rationales highly discourage work at older ages.

#### 1. INITIAL PURPOSE OF SOCIAL SECURITY WAS TO REMOVE SENIORS FROM THE WORKFORCE

Social Security was originally designed to eliminate seniors from the workforce.<sup>22</sup> During the drafting stages of the legislation, the Committee on Economic Security<sup>23</sup> initially proposed a retirement earnings test that would remove an individual’s benefits if he or she continued to work.<sup>24</sup> “The Economic Security Bill President Roosevelt transmitted to Congress in January 1935 contained the following language: ‘No person shall receive such old-age annuity unless . . . He is not employed by another in a gainful occupation.’”<sup>25</sup> During a public statement following the passage of the bill in the House of Representatives, President Roosevelt “included an item to the effect that retirement, of

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2011). The Social Security Administration states “[t]he full work of the CES was contained in 10 large volumes of reports and studies, which were never published. In 1937, two years after passage of the Social Security Act, the new Social Security Board published a summary of the Committee’s work. This summary was in the form of a book entitled, ‘Social Security In America.’ This book, therefore, represents the only published work documenting the study and analysis that underlay the creation of the Social Security program.” *Id.*

20. Comm. on Econ. Sec., *Old-Age Security*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/reports/ces/cesbookc7.html> (last visited Nov. 6, 2011).

21. *See id.*

22. Fernando M. Torres-Gil, *The Politics of Work and Aging: Public Policy for the New Elders*, in *AGING AND WORK: ISSUES AND IMPLICATIONS IN A CHANGING LANDSCAPE* 77, 81 (Sara J. Czaja & Joseph Sharit eds., 2009) (“[A] major political rationale for the passage of the Social Security Act was to move the elderly out of the workforce and make room for others.”).

23. *In Depth Research: Reports & Studies*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/repstud.html> (last visited Nov. 3, 2011). Description of the Economic Security Committee: “[t]he Committee on Economic Security (CES) was commissioned by President Roosevelt and its research formed the basis of the legislative proposal the President sent to Congress in January 1935. The material produced by the CES was thus the blueprint for what would become the Social Security Act. Indeed, it was the intellectual and academic case for Social Security in America.” *Id.*

24. *Id.*

25. DeWitt, *supra* note 1.

course, should be a condition of granting of any annuity."<sup>26</sup> Thus, Social Security was designed as an extreme disincentive to continue work, because one could not work and receive Social Security. The government emphasized that receipt of benefits and continuing employment were mutually exclusive:

The checks will come to you as a right. You will get them regardless of the amount of property or income you may have. They are what the law calls "Old-Age Benefits" under the Social Security Act. *If you prefer to keep on working after you are 65, the monthly checks from the Government will begin coming to you whenever you decide to retire.*<sup>27</sup>

This provision forced workers to choose between receiving promised benefits or continued employment.<sup>28</sup> Although reforms have eliminated the full retirement requirement, the original purpose of the legislation was not to allow seniors to continue working and receive benefits.

## 2. RETIREMENT EARNINGS TEST

Although the final version of the Social Security Act did not require complete retirement to receive benefits, the law did include other extreme disincentives to continued work.<sup>29</sup> The original legislation included a retirement earnings test that greatly reduced benefit payouts if seniors continued to work.<sup>30</sup> The retirement earnings test in the Social Security law "prohibited any Social Security payment when income was earned in 'regular employment.'"<sup>31</sup> The specifics of regular employment were not defined until Congress amended the law in 1939 to define retirement as "the receipt of less than \$15 of earnings in a month from jobs covered under the Social Security program."<sup>32</sup> At

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26. *Id.* (internal citations omitted).

27. *The 1936 Government Pamphlet on Social Security*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/ssb36.html> (last visited Nov. 3, 2011) (emphasis added).

28. *See id.*

29. DeWitt, *supra* note 1.

30. *Id.* The final version of the Social Security Act of 1935 contained the following language on the retirement earnings test:

Whenever the Board finds that any qualified individual has received wages with respect to regular employment after he attained the age of sixty-five, the old-age benefit payable to such individual shall be reduced, for each calendar month in any part of which such regular employment occurred, by an amount equal to one month's benefit.

*Id.*

31. *Id.* (internal citations omitted).

32. *Id.*

the time, this figure represented roughly twenty-five percent of the minimum wage.<sup>33</sup> Earning over twenty-five percent of the minimum wage effectively resulted in disqualification from Social Security benefits, and thus did not allow meaningful employment and the collection of benefits.

### 3. SOCIAL SECURITY CLAIMED SENIORS WERE INCAPABLE OF WORK

Social Security's disincentives toward work by seniors extends beyond the text of the law. In a booklet published by the Social Security Board, the government attempted to educate citizens about the reasoning for Social Security.<sup>34</sup> The booklet claims: "[o]ld people, like children, have lost much of their economic value to a household."<sup>35</sup> The comparison to children implies dependency and the inability to work. The booklet eventually stops implying dependency; it clearly states that the elderly are "helpless."<sup>36</sup>

Old people were not "dependent" upon their relatives when there was need in a household for work they could do. They have become dependent since their room and their board cost money, while they have little to give in return. Now they need money of their own to keep the dignity and independence<sup>37</sup> they had when their share in work was the equivalent in money.

These statements made by the government discourage work by the elderly. The booklet further asserts that payments to the elderly are necessary because of "the inability of the old to work for their living."<sup>38</sup> While promoting Social Security, the government regularly asserted that the elderly should not, and are not able to, work.<sup>39</sup> These assertions are relevant because they influence the behavior and mindset of workers. Although it may be true that when Social Security was enacted some older citizens could not continue to work, many were likely able to continue earning a living. The government's justification

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33. *Id.*

34. *Why Social Security?*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/whybook.html> (last visited Nov. 3, 2011). The Social Security Administration states that the booklet "was published in 1937 as part of the Board's efforts to educate the American public about the rationale underlying the new Social Security program." *Id.*

35. *Id.*

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.*

and actions regarding Social Security can impact the behavior and expectations of seniors.

#### 4. INITIAL SOCIAL SECURITY PAYMENT LEVELS

The initial payment levels of Social Security were much lower, and subsequent changes have discouraged work at older ages.<sup>40</sup> Throughout the history of Social Security, the average monthly payment has varied.<sup>41</sup> In the 1950s and 1960s, the average Social Security benefit was approximately twenty percent of the average full-time worker's wage.<sup>42</sup> During the 1970s and 1980s, average benefits rose to approximately thirty-five percent of the average wage, and the percentage has remained relatively stable since that time.<sup>43</sup> Notably, the percentage of workers above age sixty-five in the workforce fell as greater Social Security benefits replaced their wages.<sup>44</sup> As the average Social Security payment increased, workers had less motivation to continue working.<sup>45</sup> Larger payments are appropriate if the Social Security Administration has a significant surplus; however, current projections for Social Security indicate that this is not likely to occur.<sup>46</sup>

#### 5. INITIAL RETIREMENT AGE

When the Social Security Act became law in 1935, the initial retirement age was sixty-five years old.<sup>47</sup> The retirement age was not selected based on life expectancy or cost, but rather it was determined based on political compromise: "[a]ge sixty-five was not selected as the result of some scientific process; nor did it have some social or gerontological basis. Rather, there was simply general consensus that sixty-five was the most acceptable age."<sup>48</sup> Early retirement did not ex-

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40. Liu & Rettenmaier, *supra* note 4, at 2-3.

41. *Id.*

42. *Id.* at 2.

43. *Id.* at 3.

44. *Id.*

45. *See id.*

46. *See* 2010 ANNUAL REPORT, *supra* note 7, at 2.

47. Social Security Act of 1935, Pub. L. No. 74-271, § 202(a), 49 Stat. 620, 623 (1935).

48. Kathryn L. Moore, *Raising the Social Security Retirement Ages: Weighing the Costs and Benefits*, 33 ARIZ. ST. L.J. 543, 547 (2001). Further, "Dr. Eveline Burns, who served on the staff of the Committee on Economic Security, testified before Congress that '[65] was chosen because there was nothing very much better. Honestly, a great deal of those decisions in those days were not based on statistics.'" *Id.* (internal citations omitted).

ist until nearly twenty years after seniors began collecting benefits.<sup>49</sup> Women could elect to retire at age sixty-two beginning in 1956<sup>50</sup> and men could retire at age sixty-two beginning in 1961.<sup>51</sup> Individuals who had, on average, more physically demanding jobs, shorter lives, and worse health were required by law to work until age sixty-five, while the current generation of seniors can choose to retire at age sixty-two.<sup>52</sup> Based on the experience of individuals working seventy-five years ago, it appears that current workers could likely survive working with a higher early retirement age.<sup>53</sup>

## 6. FISCAL STATUS OF SOCIAL SECURITY

The current fiscal status of Social Security highlights the need for reform. In 2010, Social Security expenditures were expected to exceed tax receipts for the first time since 1983.<sup>54</sup> The Social Security Administration estimates that “[a]fter 2014 deficits are expected to grow rapidly as the number of beneficiaries continues to grow at a substantially faster rate than the number of covered workers.”<sup>55</sup> Thus, the government projects permanent deficits for Social Security after 2014.<sup>56</sup> Further, the fact that program deficits are not anticipated for 2011–2014 is based on a relatively quick economic recovery, which may need rethinking.<sup>57</sup> Although permanent deficits will occur after 2014, the Social Security Administration claims the trust fund can cover full payments until the reserves are exhausted, which the government predicts will occur in 2037.<sup>58</sup> Given the fact that an actual “trust fund”

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49. See generally Social Security Amendments of 1956, Pub. L. No. 84-880, § 102(a), 70 Stat. 809, 942.

50. *Id.*

51. Social Security Amendments of 1961, Pub. L. No. 87-64, § 202(a), 75 Stat. 131 (1961); *Special Collections: Chronology*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/1960.html> (last visited Nov. 3, 2011) (listing a detailed chronology of Social Security developments during the period).

52. See generally TURNER, *supra* note 16, at 2–4 (describing how general changes in health, life expectancy, and physically demanding jobs are more conducive to older workers).

53. See generally Peter H. Schuck, *The Golden Age of Aging, and Its Discontents*, 18 ELDER L.J. 25 (2010) (describing better conditions for older workers and older people in general).

54. 2010 ANNUAL REPORT, *supra* note 7, at 2.

55. *A Summary of the 2011 Annual Reports*, SOC. SEC. ADMIN., <http://www.ssa.gov/oact/trsum/index.html> (last visited Nov. 3, 2011).

56. *Id.*

57. *Id.*

58. *Id.*

does not exist, however, the current Social Security shortfall will likely have to be paid by adding to the national debt.<sup>59</sup> Following the exhaustion of the “trust fund” in 2037, the government projects that Social Security can pay roughly seventy-five percent of promised benefits until 2084.<sup>60</sup> Based on the Social Security Administration’s arguably optimistic projections, Social Security will likely be unable to pay promised benefits within approximately twenty-five years.<sup>61</sup> In light of this serious development, reforms are necessary to encourage work at older ages.

## B. Elderly in the Workforce

Even if Social Security was reformed to encourage continued work, seniors must be capable of longer work lives. To examine whether individuals are able to work longer, several questions must be addressed. Issues with life expectancy, health care, education, the nature of jobs, and fairness are all components to determining the appropriate length of work. Current employment data for the elderly provides insight into the ability of today’s seniors to work at older ages.<sup>62</sup> The statistics indicate that increased work by the elderly may be possible.<sup>63</sup> Obviously, personal choice is a major component when determining retirement; however, because government programs such as Social Security and Medicare are significant factors in the decision, public policy should influence work length and retirement.

### 1. TRENDS IN WORK AMONG THE ELDERLY

Work patterns among older Americans changed throughout the twentieth century.<sup>64</sup> In 1950, nearly fifty percent of men worked past

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59. See Richard Kaplan, *Top Ten Myths of Social Security*, 3 *ELDER L.J.* 191, 192–93 (1995). Over the years the Social Security payroll surplus has been spent by the federal government. *Id.* at 193. The government has obligated itself to repay the surplus; however, considering the increasingly massive budget deficits, the repayment will come from further debt. *Id.* at 193–94.

60. *A Summary of the 2011 Annual Reports*, *supra* note 55.

61. *See id.*

62. See Toossi, *supra* note 3, at 39. The American labor force is growing older and individuals are working at older ages. *Id.*

63. *Id.*

64. See Nicole Maestas & Julie Zissimopoulos, *How Longer Work Lives Ease the Crunch of Population Aging*, 24 *J. ECON. PERSP.* 139, 144 (2010); *see also* Richard V. Burkhauser & Ludmila Rovba, *Institutional and Individual Responses to Structural Lag: The Changing Patterns of Work at Older Ages*, in *AGING AND WORK: ISSUES AND*

the age of sixty-five.<sup>65</sup> By 1990, the number of men working past sixty-five dropped to nineteen percent.<sup>66</sup> Workers now retire earlier than previous generations, even though they are healthier and have less physical jobs.<sup>67</sup> As the baby-boom generation approaches retirement, the next decade's retirees could substantially alter the labor force. Projections indicate that between 2008 and 2018, the percentage of baby boomers in the workforce will drop from eighty-three percent to thirty-nine percent.<sup>68</sup> This decrease will have significant effects on the economy and the Social Security system's ability to pay promised benefits.

Although the number of individuals working at older ages decreased during the twentieth century, recent trends may show that seniors are beginning to work longer.<sup>69</sup> The percentage of seniors working has increased in the past ten years.<sup>70</sup> The labor force participation rate of individuals fifty-five and older has risen from approximately thirty percent in the early 1990s to nearly forty percent in 2008.<sup>71</sup> The number of workers aged sixty-five to seventy-four is expected to grow even faster, increasing nearly eighty percent by 2016.<sup>72</sup> The number of workers fifty-five and older will be forty million in 2018, a forty-three percent increase over the previous decade.<sup>73</sup> Additionally, the recent economic crisis and subsequent recession appear to have influenced the decision of some individuals to work longer.<sup>74</sup>

Some of the increase can be attributed to the general aging of the baby-boom generation, but the attitude toward working longer also appears to be changing. Workers themselves are increasingly anti-

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IMPLICATIONS IN A CHANGING LANDSCAPE, *supra* note 22, at 9, 17. Table I.I. lists detailed statistics for the labor force participation rate between 1950 and 2005. *Id.*

65. Maestas & Zissimopoulos, *supra* note 64, at 144 fig.1.

66. *Id.*

67. JOHNSON ET AL., *supra* note 15, at 1.

68. Toossi, *supra* note 3, at 38.

69. Liu & Rettenmaier, *supra* note 4, at 3.

70. Toossi, *supra* note 3, at 39.

71. *Id.*

72. Howard Eglit, *Age Bias in the American Workplace—An Overview*, 3 J. INT'L AGING L. & POL'Y 99, 106 (2009).

73. Toossi, *supra* note 3, at 31.

74. Schuck, *supra* note 53, at 37–38 (noting that the recent trend in delaying retirement, caused partially by the decrease in home value and personal investments, may or may not continue depending on several factors).

pating delayed retirement.<sup>75</sup> A recent survey found that more than one-third of current workers plan on retiring after the age of sixty-five, up from only twelve percent in 1995.<sup>76</sup> This was the first time in Gallup's fifteen years of asking retirement age questions that more Americans planned to retire after the age of sixty-five than before it.<sup>77</sup> Although these statistics are a positive development, serious Social Security reforms could significantly increase the labor force participation rates of seniors.

## 2. LIFE EXPECTANCY

Life expectancy is an important aspect of any Social Security program.<sup>78</sup> As American life expectancy continues to increase, workers receive Social Security benefits for longer periods. This demographic change impacts retirement and Social Security. "[W]orkers may not only want to work longer, but they may *need* to work longer in order to support consumption over a longer lifespan."<sup>79</sup>

The increase in life expectancy over the past 150 years has not yet shown signs of deceleration.<sup>80</sup> Not only are individuals living longer, but the abnormally large baby-boom generation raises the number of retirees.<sup>81</sup> The percentage of elderly individuals in the overall population is growing, and this trend will continue over the next fifty years as the baby-boom generation ages.<sup>82</sup> The Census Bureau projects that over twenty percent of the adult population will be sixty-five or older by 2050.<sup>83</sup> This is an increase from seventeen percent in 2000.<sup>84</sup> Although a significant factor in the increased life expectancy is the reduction of the infant mortality rate,<sup>85</sup> individual life span length has also increased.<sup>86</sup> In 1940, life expectancy for an indi-

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75. Frank Newport, *Americans' Projected Retirement Age Continues to Creep Up*, GALLUP (Apr. 26, 2010), <http://www.gallup.com/poll/127514/americans-projected-retirement-age-continues-creep-up.aspx>.

76. *Id.*

77. *Id.*

78. See Moore, *supra* note 48, at 559.

79. Maestas & Zissimopoulos, *supra* note 64, at 150.

80. *Id.* But see S. Jay Olshansky et al., *A Potential Decline in Life Expectancy in the United States in the 21st Century*, 352 NEW ENG. J. MED. 1138 (2005).

81. Toossi, *supra* note 3, at 39.

82. JOHNSON ET AL., *supra* note 15, at 6.

83. *Id.*

84. *Id.*

85. Schuck, *supra* note 53, at 28–29.

86. See Liu & Rettenmaier, *supra* note 4, at 8–9.

vidual after reaching the age of sixty-five was thirteen years, while the current life expectancy after reaching age sixty-five is eighteen years and is continuing to increase.<sup>87</sup> The increased life expectancy for individuals at the age of sixty-five indicates seniors will collect more Social Security payments as they are living longer, but it also opens up the possibility of increased work at older ages.

### 3. HEALTH IMPROVEMENTS

Work at older ages not only requires longer life spans, but also improved health.<sup>88</sup> Generally, an individual's health affects his or her ability and desire to work.<sup>89</sup> The number of seniors with disabilities has decreased,<sup>90</sup> which indicates better health at older ages.<sup>91</sup> "The incidence of chronic disability (lasting at least three months) declined substantially for the population over age 65 for the period 1982–1999."<sup>92</sup> Additionally, since the early 1980s, fewer seniors are reporting that they are in poor health.<sup>93</sup> Although some workers do claim Social Security early as a result of health-related issues, a 1990s study by the Congressional Budget Office found that only six percent of individuals claimed early benefits because of poor health.<sup>94</sup> Overall, the Government Accountability Office, in a 2005 report, found that "the majority of workers aged 62 to 67 do not appear to have health limita-

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87. *Id.*; Burkhauser & Rovba, *supra* note 64, at 15. Other research indicates even greater increases in life expectancy at age sixty-five: "life expectancy rose from 11.7 years in 1900 to 21.2 years in 2000, with most of this change occurring after 1950." *Id.*

88. Moore, *supra* note 48, at 575–79.

89. Alicia H. Munnell et al., *Will People Be Healthy Enough to Work Longer?* 2 (Ctr. for Ret. Research at B.C., Working Paper No. 2008-11, 2008).

90. *Id.* at 5–7.

91. *See id.* at 3–7.

92. TURNER, *supra* note 16, at 3.

93. *Id.* at 2; Andrew G. Biggs, *The Case for Raising Social Security's Early Retirement Age*, AM. ENTER. INST. FOR PUB. POLICY RESEARCH, Oct. 2010, at 6, available at <http://www.aei.org/docLib/10-RPO-2010-g.pdf>. ("Among individuals aged fifty-five to sixty-four, those with fair or poor health dropped from 25.1 percent in 1983 to 18.5 percent in 2007; among those aged sixty-five to seventy-four, the percentage dropped from 32.5 to 22.4; and for those aged seventy-five to eighty-four, it dropped from 34.6 to 25.5.")

94. CONG. BUDGET OFFICE, *RAISING THE EARLIEST ELIGIBILITY AGE FOR SOCIAL SECURITY BENEFITS* 13 (1999), available at <http://www.cbo.gov/ftpdocs/10xx/doc1058/ssage.pdf>.

tions that would prevent them from extending their careers.”<sup>95</sup> Along with a longer life span, increased health allows for work at older ages.

#### 4. ABILITY OF OLDER WORKERS TO FIND EMPLOYMENT

Even if more seniors anticipate delayed retirement, jobs must exist for older individuals. In determining reforms to increase work at older ages, an important consideration is the availability of work and the workforce skills of the elderly.<sup>96</sup> In particular, the improved education of the elderly and the availability of less physically demanding jobs will help older workers find employment.

*a. Increasing Education Levels of the Elderly* Seniors are becoming more highly skilled and educated, therefore increasing the possibility of working longer. Research indicates that “completed schooling (by age 30) among those in the 65–74 age group will rise from 10.4 years in 1990 to 13.3 years in 2030.”<sup>97</sup> This will likely lengthen the work life of seniors: “[e]ducated people work more at least in part because they are paid more, have more fulfilling jobs, and face fewer physical demands.”<sup>98</sup> The education gap between elderly and young workers appears to be decreasing over time as the baby-boom generation had greater access to higher education and younger workers are not increasing their level of education as quickly as the previous generations.<sup>99</sup> Thus, the competition older workers face from younger and more educated workers is on the decline.

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95. *Redefining Retirement: Options for Older Americans: Hearing Before the S. Special Comm. on Aging*, 109th Cong. 10 (2005) (statement of Barbara D. Bovbjerg, Director of Education, Workforce, and Income Security), available at [www.gao.gov/new.items/d05620t.pdf](http://www.gao.gov/new.items/d05620t.pdf).

96. *See id.*

97. Maestas & Zissimopoulos, *supra* note 64, at 146.

98. *Id.*

99. *Id.* at 151. Research indicates that the education gap between young workers and the elderly is decreasing:

[D]ata from Goldin and Katz (2007) show that in 1990 a retiring 65 year-old had on average 10.9 years of schooling, while an entering 25 year-old in that year had 13.5 years of schooling, a gap of 2.6 years. In 2010, a retiring 65 year-old will have on average 12.6 years of schooling, while an entering 25 year-old will have about 13.9 years, dramatically narrowing the education gap to just 1.3 years. By 2030, a retiring 65 year-old will have 13.5 years of schooling, while, if current trends continue, an entering 25 year-old might have around 14.0 years, further closing the education gap to just half a year.

*Id.*

*b. Fewer Physically Demanding Jobs* Another important issue with work at older ages is the ability of seniors to meet the physical challenges of employment. Generally, physical strength and endurance decrease with age.<sup>100</sup> Seniors are unable to work in certain physically demanding jobs; however, the number of physically demanding jobs continues to decrease.<sup>101</sup> “Between 1950 and 1996, the percentage of the workforce in jobs that required frequent lifting or carrying of objects weighing 25 pounds or more declined from 20 percent to 8 percent.”<sup>102</sup> During the past fifty years, technological advancement has favored cognitive and analytic skills over manual and routine skills.<sup>103</sup> As technology has made work less physical, the ability to work in spite of health limitations has increased.<sup>104</sup> While the movement toward less physically demanding work has somewhat slowed since the 1990s, the overall trend has nevertheless continued.<sup>105</sup> Less physically demanding jobs increase the availability of work for seniors. In sum, the elderly are ready and able to stay in or reenter the workforce after the age of sixty-five. Social Security reform may provide the necessary incentive to encourage work at older ages.

### III. Analysis

Even though more jobs are increasingly available and older workers want employment, significant disincentives exist toward work at older ages. One of the government’s most influential programs,<sup>106</sup> Social Security, has aspects that discourage continued employment amongst seniors. Social Security’s formula for determining benefits, taxes on benefits, early retirement age, and retirement earnings test all discourage continued work by beneficiaries.

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100. TURNER, *supra* note 16, at 3.

101. *Id.*

102. *Id.*

103. Maestas & Zissimopoulos, *supra* note 64, at 147.

104. *Id.*

105. See TURNER, *supra* note 16, at 3–4.

106. Torres-Gil, *supra* note 22, at 80. Social Security is the most important government program affecting retirement: “[A]lthough Social Security may not have been intended as the overarching policy approach to work and aging, it has become the primary policy tool influencing how and when older workers elect to work or retire.” *Id.*

**A. Social Security's Benefit Structure Discourages Work**

Like all wage earners, seniors who continue to work must pay a 12.4% Social Security payroll tax split between the employer and employee.<sup>107</sup> Social Security discourages work at older ages by not rewarding continued employment for workers who have spent more than thirty-five years in the labor market.<sup>108</sup> Social Security recipients who remain employed continue to pay Social Security payroll taxes, without receiving any gain in benefits.<sup>109</sup> Additionally, seniors with over thirty-five years of employment "gain relatively few additional Social Security benefits by continuing to work and pay taxes."<sup>110</sup> Social Security "[b]enefits are based on average indexed monthly earnings, computed over the 35 years with the highest indexed earnings. For workers with fewer than 35 years of employment, an additional year of work . . . eliminates a year of zero earnings . . . generally raising future benefits substantially."<sup>111</sup> For those workers that already have a thirty-five year work history, however, the additional work generally does not significantly increase benefits.<sup>112</sup> Based on the reality that continued work does not increase benefits for most workers, Social Security's thirty-five year cap does not incentivize continued work by seniors.

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107. JOHNSON ET AL., *supra* note 15, at 2.

108. *Id.*

109. *Id.* at 20.

Although employers nominally pay half of the payroll tax, almost all economists believe that employers completely offset their share of the tax bill by reducing wages below the amount they would have paid in the absence of the tax. Workers effectively pay the entire payroll tax themselves, especially over time as employers adjust to the cost of labor.

*Id.* (internal citations omitted); ALICIA H. MUNNELL & STEVEN A. SASS, WORKING LONGER: THE SOLUTION TO THE RETIREMENT INCOME CHALLENGE 130 (2008). By requiring that beneficiaries continue Social Security payroll taxes, the "contributions essentially become a tax, a levy without a compensating benefit." *Id.*

110. JOHNSON ET AL., *supra* note 15, at 20.

111. *Id.* at 20–21.

112. *See id.*

## B. Taxes on Social Security Benefits Discourage Work at Older Ages

Generally, low income seniors do not pay income taxes on Social Security benefits.<sup>113</sup> Seniors with modest incomes above \$34,000 for individuals or \$44,000 for couples, however, can have up to eighty-five percent of Social Security income subject to taxation.<sup>114</sup> Additionally, these numbers are not indexed to inflation, which enhances the problem further.<sup>115</sup> “As wages and Social Security benefits increase over time with prices and productivity, a growing share of beneficiaries will pay taxes on their Social Security benefits.”<sup>116</sup>

For those seniors who claim benefits early, the Social Security taxes paid on wages prior to the normal retirement age do not create any additional benefits.<sup>117</sup> Considering most workers claim benefits prior to the normal retirement age,<sup>118</sup> this is a relevant issue. Current law requires elderly workers to pay substantial payroll taxes: “[t]he average 64-year-old worker is expected to earn \$26,662 and pay an additional \$2,826 in Old Age and Survivors Insurance (OASI) taxes.”<sup>119</sup> Cumulatively, an individual who takes Social Security at age sixty-two will pay over \$9,000 for average earners and \$15,000 for high earners in OASI taxes between the ages of sixty-two and sixty-four, without likely increasing Social Security payouts.<sup>120</sup> These taxes on Social Security benefits provide disincentives to work at older ages.

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113. Barbara A. Butrica et al., *The Implicit Tax on Work at Older Ages*, 59 NAT'L TAX J. 211, 214 (2006).

114. *See id.* Demonstrating the potentially high tax rate faced by Social Security recipients with moderate incomes:

If adjusted gross income (AGI) plus tax-exempt interest income and one-half of Social Security benefits (“modified AGI”) fall below \$25,000 for single taxpayers or \$32,000 for couples, beneficiaries pay no federal income taxes on their Social Security. However, up to 50 percent of Social Security income is taxable for single taxpayers with modified AGI between \$25,000 and \$34,000 (or between \$32,000 and \$44,000 for couples). Up to 85 percent of Social Security income is taxable for single taxpayers with modified AGI over \$34,000 (or \$44,000 for couples).

*Id.*

115. *Id.*

116. *Id.*

117. Liu & Rettenmaier, *supra* note 4, at 8.

118. *Id.* at 3–4. “Most workers begin claiming Social Security benefits before they reach normal retirement age. In 2004 . . . two-thirds of men who started claiming benefits had not reached normal retirement age.” *Id.*

119. *Id.* at 8.

120. *See id.*

### C. Social Security Early Retirement Age Discourages Continued Work

For workers born in 1960 or after, the normal Social Security retirement age is sixty-seven.<sup>121</sup> Reforms passed in 1983 increased the normal retirement age but left the early retirement age unchanged at sixty-two.<sup>122</sup> “[M]any analysts believe that the availability of early Social Security benefits at age 62 induces many workers to leave the labor force at or near that time.”<sup>123</sup> Additionally, the largest recorded declines in labor force participation among men occurred in 1961, the year that early retirement was first made available.<sup>124</sup> The guarantee of benefits at a predetermined age likely distorts worker decision making, further incentivizing retirement as opposed to continued work.<sup>125</sup> Although having an early retirement age is a benefit to many, for lower earners who have not considered the ramifications of reduced benefits, an early retirement age encourages them to retire when they can likely continue working and increases the number of seniors in poverty.<sup>126</sup> Also, the reduction in benefits for receiving Social Security before one’s normal retirement age likely discourages some from claiming; however, decisions appear to be influenced more by “the availability of benefits than to benefit amounts.”<sup>127</sup>

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121. *Id.*

122. *Id.* at 10.

123. TURNER, *supra* note 16, at 1.

124. Jill Quadagno & Joseph Quinn, *Does Social Security Discourage Work?*, in SOCIAL SECURITY IN THE 21ST CENTURY 127, 135 (Eric R. Kingson & James H. Schulz eds., 1997). These researchers found a correlation between increasing early retirement by men and the availability of Social Security benefits. *Id.* “It is true that the largest declines in the labor force participation rates of American men aged 60–64 occurred after the age of earliest Social Security eligibility was reduced from age 65 to age 62 (in 1961), and after very large increases in real benefits were legislated (1969–1972).” *Id.*

125. June E. O’Neill, *Assuring the Future of Social Security: Privatization and Other Reforms: Why Social Security Needs Fundamental Reform*, 65 OHIO ST. L.J. 79, 91 (2004) (It is “likely that by promising a relatively generous benefit at a politically determined age of retirement, Social Security has distorted the decision about when to retire and has contributed to the sharp decline in work participation over time among men age sixty-two and older.”).

126. Andrew G. Biggs, Op-Ed., *Raise the Early Retirement Age*, L.A. TIMES, Nov. 9, 2010, <http://articles.latimes.com/2010/nov/09/opinion/la-oe-biggs-social-security-20101109> (claiming that if early retirement were eliminated “poverty among retirees over the age of 65 would be about one-fifth lower”).

127. MUNNELL & SASS, *supra* note 109, at 58.

#### D. The Social Security Retirement Earnings Test Discourages Work

The Social Security retirement earnings test (earnings test) applies to workers who receive Social Security prior to the normal retirement age and continue to work.<sup>128</sup> For these individuals, some Social Security benefits are withheld if the worker earns a certain amount: "Social Security withholds one dollar of an early retiree's benefits for every two dollars earned above \$12,480."<sup>129</sup> This reduction in benefits, however, is gradually restored after the individual reaches normal retirement age.<sup>130</sup> The recalculated benefit gives the individual a higher payment for the rest of his or her life.<sup>131</sup>

Although the most serious deterrents toward work were removed by previous changes in the earnings test,<sup>132</sup> reform is still necessary. The earnings test remains in effect for those who have claimed benefits before their normal retirement age.<sup>133</sup> The earnings test does not apply to individuals past the normal retirement age, but the test still impacts a large number of Social Security recipients because most workers claim benefits early.<sup>134</sup> The mere fact that the government reduces benefit payments for individuals who continue to work could cause seniors to think that they should completely retire before claiming benefits: "the retirement earnings test may send a signal to older people that they should not work, discouraging employment more than the financial incentives alone suggest."<sup>135</sup> Also, even though the benefits removed by the earnings test are eventually restored, certain

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128. Liu & Rettenmaier, *supra* note 4, at 4.

129. *See id.* Statistics are based on 2006 numbers. *Id.*

130. *Id.*

131. *Id.*

[B]enefits withheld by the earnings test are gradually restored over time after the retiree reaches the normal retirement age. The Social Security benefit is recalculated and the individual receives a higher payment for the rest of his or her life. The adjustments used to restore benefits account for the time value of money (the fact that a dollar of benefits today is more valuable than a dollar of future benefits) and for the fewer remaining expected years of life as one delays receiving benefits.

*Id.*

132. *See id.* at 6–7. The Senior Citizens Freedom to Work Act was passed in 2000 and eliminated the earnings test for workers above the normal retirement age. *Id.* at 6.

133. JOHNSON ET AL., *supra* note 15, at 22–23.

134. Liu & Rettenmaier, *supra* note 4, at 3.

135. JOHNSON ET AL., *supra* note 15, at 23.

individuals with lower life expectancies or risk aversion may not value the recalculated benefits and thus choose not to work while receiving benefits.<sup>136</sup> One economic analysis demonstrated that the earnings test reduced the number of men working full time between age sixty-two and the normal retirement age by four percentage points.<sup>137</sup> Overall, the Social Security earnings test likely discourages continued work by seniors.

#### IV. Resolution

Based on the increased health and ability of older workers, Social Security can be reformed to encourage continued work. Most proposals to reform Social Security focus solely on the program's finances. Prolonging work lives not only improves Social Security's finances, but it also enhances the personal finances of the elderly, enabling a higher standard of living for retirees and shielding them from potential future benefit reductions.<sup>138</sup> The following suggestions focus mainly on feasible proposals, as there are various ways to increase the working lives of seniors. For example, cutting Social Security benefits in half would increase the labor force participation rate of the elderly, but such a plan is not appealing or politically feasible.<sup>139</sup> Any plan to increase the retirement age of seniors should include changes to the benefit formula, tax incentives, earnings test, and the retirement age.

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136. See Liu & Rettenmaier, *supra* note 4, at 4–5. While the earnings tax benefits are later restored, the value is often not equal: “[D]epending on an individual’s own subjective discount rate, mortality expectations and risk preferences, claiming benefits early may be a natural response to the scheduled adjustments for early retirement.” *Id.* at 5.

137. Alan L. Gustman & Thomas L. Steinmeier, *The Social Security Retirement Earnings Test, Retirement and Benefit Claiming* 18 (Nat’l Bureau of Econ. Research, Working Paper No. 10905, 2004), available at <http://www.nber.org/papers/w10905>.

138. See Liu & Rettenmaier, *supra* note 4, at 1.

139. SELAHATTIN İMROHOROĞLU & SAGIRI KITAO, FED. RES. BANK OF N.Y., BENEFIT CLAIMING AND LABOR FORCE PARTICIPATION: A QUANTITATIVE GENERAL EQUILIBRIUM APPROACH 33 (2010), available at [http://www.newyorkfed.org/research/staff\\_reports/sr436.pdf](http://www.newyorkfed.org/research/staff_reports/sr436.pdf). The study finds that a fifty percent reduction in Social Security payroll taxes and benefits has a noticeable impact on the number of seniors in the workforce. *Id.* “A 50% reduction of the payroll tax rate and benefits is shown to have a significant effect on both saving and labor supply. The participation among older workers in their 60s rises from 50% to 62%. More individuals choose to postpone the benefit take-up and the claim rate at age 62 plummets from 50% to less than 30%.” *Id.*

### A. Factoring Additional Years of Work into Social Security's Benefit Formula

One Social Security reform that would incentivize work at older ages requires changing aspects of the benefit formula. Currently, the benefit formula does not reward workers for additional work beyond thirty-five years.<sup>140</sup> The present benefit structure discourages continued work: “[s]omeone who works 45 years at \$35,000 gets substantially fewer benefits than someone who works 35 years at \$45,000.”<sup>141</sup> Social Security should be reformed to include time in excess of thirty-five years in the beneficiary’s payout. This approach would encourage work past thirty-five years, as each additional year can have a tangible effect on future benefits.<sup>142</sup>

One straightforward solution is to calculate benefits based on forty years of work rather than thirty-five.<sup>143</sup> This would remove the disincentive for workers who have already reached thirty-five years of work.<sup>144</sup> Analysis of this proposal shows a reduction in the effective tax rate at older ages.<sup>145</sup> The increase to forty years could be combined with tax incentives to enhance the overall bonus.<sup>146</sup> Additionally, factoring forty years into the formula would decrease Social Security’s projected budget deficit by twenty-nine percent.<sup>147</sup> A second possibility is to increase the Social Security payout for those who work longer than thirty-five years, giving workers a predetermined percentage increase in future Social Security benefits. Third, instead of averaging the worker’s benefit based on thirty-five years of work, the benefit can be computed using the total wages paid into the system.<sup>148</sup> Although

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140. JOHNSON ET AL., *supra* note 15, at 2.

141. JED GRAHAM, A WELL-TAILORED SAFETY NET 102 (2010) (internal citations omitted).

142. *Id.* (internal citations omitted).

143. Gopi Shah Goda et al., *Removing the Disincentives in Social Security for Long Careers* 7 (Nat’l Bureau of Econ. Research, Working Paper No. 13110, 2007), available at <http://www.nber.org/papers/w13110.pdf>.

144. *Id.*

145. John Sabelhaus, *What is the Effective Social Security Tax on Additional Years of Work?*, 60 NAT’L TAX J. 502, 505 (2007).

146. Goda et al., *supra* note 143, at 9.

147. *Increasing the Number of Work Years Used to Compute Benefits*, URBAN INST., [http://www.urban.org/retirement\\_policy/ssraiseworkyears.cfm](http://www.urban.org/retirement_policy/ssraiseworkyears.cfm) (last visited Nov. 4, 2011) (“Increasing to 40 computation years (phased in from 2009 through 2017, again excluding disabled workers) would reduce the long-term deficit by about 29 percent.”).

148. Eugene Steuerle & Christopher Spiro, *Should the Social Security Benefit Formula Include Every Year Worked?*, STRAIGHT TALK ON SOC. SEC. & RET. POLICY

the approaches may vary, reforms to the Social Security benefit formula will encourage additional years of work. However, increasing the number of years worked within the benefit calculation would reduce benefits for individuals with fewer work years. Hopefully the possibility of reduced benefits would encourage slightly longer work lives.

## B. Tax Incentives

### 1. PAYROLL TAX REDUCTIONS

The government could use tax incentives to encourage extending work lives. One important tax to reduce is the Social Security payroll tax. About three-quarters of American households pay more in payroll taxes than in federal income taxes.<sup>149</sup> Once workers begin claiming benefits, their Social Security payroll taxes do not generate any additional payout, even though they continue to pay their half of the 12.4% payroll tax.<sup>150</sup> Research indicates that eliminating the tax on older individuals would increase the number of workers.<sup>151</sup> By eliminating the employee's portion of the payroll tax, the worker would immediately gain a 6.2% income boost. Eliminating the payroll tax could be an incentive for workers who have attained a certain number of years in the workforce to continue working.<sup>152</sup>

Additionally, eliminating the payroll tax on employers would increase the number of working seniors: "those who are willing to work beyond their normal retirement age should be exempt from paying any further payroll taxes, as should their employer. The combination will provide additional employment opportunities for older Americans."<sup>153</sup> Moreover, payroll tax reductions are a political possi-

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(Urban Inst., D.C.), Dec. 15, 1999, at 1, available at <http://www.urban.org/UploadedPDF/Straight13.pdf>.

149. David Leonhardt, *Yes, 47% of Households Owe No Taxes. Look Closer.*, N.Y. TIMES, Aug. 13, 2010, <http://www.nytimes.com/2010/04/14/business/economy/14leonhardt.html>.

150. Liu & Rettenmaier, *supra* note 4, at 8.

151. *Id.*

152. Goda et al., *supra* note 143, at 8–9 (proposing that the Social Security benefit formula factor in forty years of work and that individuals continuing to work after forty years be exempt from the 6.2% payroll tax).

153. John, *supra* note 14, at 3.

bility, given the two percent Social Security Payroll tax cut in 2011.<sup>154</sup> While lower payroll taxes could affect Social Security's budget, the reduction would likely be coupled with other reforms to make the cuts deficit-neutral.

## 2. INCOME TAX REDUCTIONS

Besides payroll tax reductions, lowered income tax rates would encourage extended work lives by the elderly. Although they may seem difficult to implement, recent proposals have suggested lower taxes for seniors.<sup>155</sup> During the 2008 presidential campaign, President Obama proposed a major tax incentive for the elderly.<sup>156</sup> The plan included eliminating income taxes for seniors making less than \$50,000.

Barack Obama will eliminate all income taxation of seniors making less than \$50,000 per year. This will eliminate taxes for 7 million seniors—saving them an average of \$1,400 a year—and will also mean that 2.7 million seniors will not need to file an income tax return at all.<sup>157</sup>

Experts criticized the proposal for its alleged political pandering and lack of depth.<sup>158</sup> Although the plan received negative publicity and was never proposed as a law, the concept has been considered by the President and may be included in upcoming legislation. Regardless of the specific proposal, tax incentives can encourage continued work by individuals at older ages.

### C. Eliminating the Social Security Retirement Earnings Test

Eliminating the earnings test would encourage longer work lives. Individuals claiming Social Security before their normal retirement age currently face substantial penalties on their benefits if they are still working.<sup>159</sup> To increase the number of beneficiaries who continue to work, the earnings test could be reduced or even eliminated.

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154. *2011 Benefit Fact Sheet*, SOC. SEC. ADMIN., <http://www.ssa.gov/pubs/10003.html> (last visited Nov. 4, 2011).

155. See, e.g., *Barack Obama's Comprehensive Tax Plan*, BARACKOBAMA.COM (original on file with author).

156. *Id.*

157. *Id.*

158. See *Obama's 'No Income Tax on Seniors' Draws Critics*, USA TODAY, Aug. 12, 2008, [http://www.usatoday.com/news/politics/election2008/2008-08-12-obama-seniors\\_N.htm](http://www.usatoday.com/news/politics/election2008/2008-08-12-obama-seniors_N.htm); see also Mark Robyn, *Obama's Income Tax Cliff for Senior Citizens*, TAX FOUNDATION (Aug. 22, 2008), <http://www.taxfoundation.org/news/show/23525.html>.

159. Liu & Rettenmaier, *supra* note 4, at 4.

Analysis has shown that labor force participation rates of individuals over the age of sixty-two are “substantially higher” without the earnings test.<sup>160</sup> Although statistical analyses vary, it appears as though eliminating the earnings test would induce some seniors to continue working while collecting benefits.

Perhaps the best example of the effect of removing the earnings test is the elimination of the earnings test for workers over the normal retirement age that occurred in 2000.<sup>161</sup> In 2000, Congress repealed the earnings test for Social Security beneficiaries that work past the normal retirement age.<sup>162</sup> The bill received substantial bipartisan support and was quickly signed into law by President Clinton.<sup>163</sup> Studies found a noticeable increase in the number of workers age sixty-five to sixty-seven once the earnings test was removed.<sup>164</sup> Another study by the Social Security Administration found a smaller initial impact on increased work by seniors but that the “effect appears to increase over time, suggesting that the removal has long-lasting effects on work participation.”<sup>165</sup> Overall, current analysis and the success of prior reform indicate that removal of the earnings test can incentivize work at older ages.

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160. Hugo Benítez-Silva & Frank Heiland, *The Social Security Earnings Test and Work Incentives*, 26 J. POL'Y ANALYSIS & MGMT. 527, 548 (2007) (“[I]ndividuals with low earning power work less due to the Earnings Test under the current system but are likely to work more, on average, if the Earnings Test was removed.”).

161. See Jae G. Song & Joyce Manchester, *How Have People Responded to Changes in the Retirement Earnings Test in 2000?*, 67 SOC. SEC. BULL. 1 (2007), available at <http://www.ssa.gov/policy/docs/ssb/v67n1/v67n1p1.pdf>.

162. Senior Citizens' Freedom to Work Act of 2000, Pub. L. No. 106-182, 114 Stat. 198 (2000) (codified as amended at 42 U.S.C. § 403 (2006)).

163. *SSA History: History of SSA 1993–2000, Chapter 3: Program Solvency*, SOC. SEC. ADMIN., <http://www.ssa.gov/history/ssa/ssa2000chapter3.html> (last visited Nov. 4, 2011). The legislation passed the house with a vote of 422-0 and the Senate with a vote of 100-0. *Id.* The bill was signed into law by the President slightly over a month after it was brought to the floor of the house. *Id.*

164. Benítez-Silva & Heiland, *supra* note 160, at 549 (citing a study that found “the rate of full-time work increased 11 percentage points more for 65–67-year-olds than for 62–64-year-olds in the HRS when the Earnings Test for those after age 65 (NRA) was removed in 2000”); Liu & Rettenmaier, *supra* note 4, at 6–7. In addition to an increase in labor force participation rates, the analysis also found an increase in workers earning above the previous level that was taxed by the earnings test. *Id.*

165. Song & Manchester, *supra* note 161, at 1.

## D. Increasing the Retirement Age

### 1. INCREASING THE NORMAL RETIREMENT AGE

Increasing the retirement age is another way to encourage work at older ages. The previous proposals provided incentives to encourage continued work. Increases in the retirement age, however, are often less optimal for the average worker.<sup>166</sup> Although raising the normal retirement age is a controversial issue, it must be considered with any serious proposal to remove the work disincentives from Social Security.

The deficit reduction commission proposed raising the normal retirement age to sixty-eight in 2050 and sixty-nine by 2075.<sup>167</sup> Although a good suggestion, increases likely need to occur sooner. Increasing the normal retirement age from sixty-six to sixty-eight would immediately increase the labor force participation rate of seniors and the finances of Social Security.<sup>168</sup> Specifically, this action would lower the number of workers taking Social Security at age sixty-two and increase labor force participation rates between ages sixty and sixty-nine.<sup>169</sup> Under current law, the retirement age will increase to sixty-seven, so this is only one extra year of work.<sup>170</sup> Other proposals have suggested similar increases; however, any reforms to encourage work must address the normal retirement age.

An immediate increase of the normal retirement age is unlikely.<sup>171</sup> The last time the normal retirement age was raised in the 1980s, the change did not impact retirees for approximately seventeen

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166. CONG. BUDGET OFFICE, *supra* note 94, at 2.

167. THE NATIONAL COMM'N ON FISCAL RESPONSIBILITY & REFORM, THE MOMENT OF TRUTH 50 (2010), available at [http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12\\_1\\_2010.pdf](http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12_1_2010.pdf).

168. See İMROHOROĞLU & KITAO, *supra* note 139, at 23.

169. *Id.* The study's authors found a significant impact when the normal retirement age increases to age sixty-eight. *Id.*

More individuals postpone early claiming and only 39.3% of retirees take up the benefit at age 62, compared to 49.9% in the benchmark economy. The old age participation at ages 60–69 rises by 2.4 percentage points and aggregate labor supply slightly rises by 0.7%. There is a significant improvement in the Social Security budget and the surplus increases to 1.32% of GDP. Not only does the benefit spending decline, but the revenues from the Social Security tax rises also, since both the wage and labor supply increase.

*Id.*

170. 42 U.S.C. § 416 (2006).

171. Moore, *supra* note 48, at 558.

years.<sup>172</sup> Additionally, if the normal retirement age was increased, the workers impacted would likely be years away from retirement, so they could prepare for the changes. The issue then becomes how to appropriately determine future increases or age levels. Sixty-five was originally selected on a somewhat random basis,<sup>173</sup> and the normal retirement age has not been adjusted since 1983.<sup>174</sup> A better solution than waiting for periodic congressional action is to adjust the normal retirement age based on increased life expectancy.

One solution is to index the normal retirement ages to increases in life expectancy. The normal retirement age could be indexed to equalize the number of years in retirement or indexed to a ratio of potential work years to retirement years.<sup>175</sup> This would increase the normal retirement age to sixty-eight for workers born in 1970 and then index future increases on life expectancy gains.<sup>176</sup> Indexing the normal retirement age was explicitly endorsed by the deficit reduction commission, which suggested "adjusting the retirement ages by one month every two years after the NRA [normal retirement age] reaches age 67."<sup>177</sup> There are various ways to index the retirement age, and the appropriate reforms should adopt an index that accounts for increases in life expectancy.

## 2. INCREASING THE EARLY RETIREMENT AGE

One of the most obvious ways to increase work at older ages is to increase the Social Security early retirement age. Although seemingly simple, this is likely the most difficult and politically controversial Social Security reform. It may be difficult to implement, but increasing the Social Security retirement age would encourage longer work lives. The average worker claimed Social Security retirement benefits at age 68.5 in 1950, while the current average worker claims benefits around the age of sixty-three.<sup>178</sup> The early retirement age was

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172. *Id.*

173. *Id.* at 547.

174. *Id.* at 557.

175. Liu & Rettenmaier, *supra* note 4, at 9–10.

176. *Id.* at 9.

177. THE NATIONAL COMM'N ON FISCAL RESPONSIBILITY & REFORM, *supra* note 167, at 50. The proposed index also included a ratio of work to retirement. *Id.* "This approach would also maintain a constant ratio of years in retirement to years in adulthood; as life expectancy grows by one year, individuals will still be able to spend an additional 4 months in retirement, as compared to today." *Id.*

178. GRAHAM, *supra* note 141, at 74.

not even available until 1961, roughly twenty-five years after Social Security was created.<sup>179</sup> In 1983, Social Security was reformed to gradually increase the normal retirement age from sixty-five to sixty-seven; however, the early retirement age remained unchanged at age sixty-two.<sup>180</sup>

The early retirement age should be increased to correct the past error of leaving the early retirement age at sixty-two when increases to the normal retirement age were implemented.<sup>181</sup> Such a change would encourage extended work lives and reflect increases in health and longevity of workers in their sixties.<sup>182</sup> An increase in the early retirement age makes the most sense because it is the most likely plan to “keep workers on the job longer and produce a higher level of retirement income.”<sup>183</sup> Research indicates that the age requirement and availability of benefits at an early age affects the labor force participation rate of seniors.<sup>184</sup> Further, economists Gustman and Steinmeier estimate that raising the early retirement age to sixty-four would reduce the percentage of fully retired people ages sixty-two and sixty-three by seven percent.<sup>185</sup>

#### E. Shifting the Early Retirement Penalty

Social Security should be reformed by removing incentives to claim benefits at an early age, and retiring before the normal retirement age reduces the benefits for workers who are more likely to need protection.<sup>186</sup> Changes in the early retirement penalty may be more

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179. Quadagno & Quinn, *supra* note 124, at 135–36.

180. Liu & Rettenmaier, *supra* note 4, at 10.

181. John, *supra* note 14, at 3 (commenting that any future changes should not make the same mistake and neglect to increase the early retirement age: “[h]owever, unlike 1983, when only the normal retirement age (NRA) was increased, this time the early eligibility age (EEA) needs to be increased as well.”).

182. See GRAHAM, *supra* note 141, at 95. A retirement age of sixty-two no longer makes sense with increased longevity, benefit cuts, and an early retirement penalty of thirty percent. *Id.* at 94–95.

183. *Id.*

184. See Quadagno & Quinn, *supra* note 124, at 135–36 (citing research that supports the conclusion of Social Security encouraging premature retirement by the elderly). “Some researchers (e.g. Hurd and Boskin, 1984) have attributed most of the decline in elderly labor force participation to increased Social Security generosity.” *Id.*

185. Gustman & Steinmeier, *supra* note 137, at 18.

186. GRAHAM, *supra* note 141, at 75 (finding that “36 percent of retirement benefits are paid to people 69 and younger—retirees who perhaps shouldn’t be considered old”).

appealing than an outright increase in the early retirement age. Currently, individuals who claim Social Security benefits before their normal retirement age face permanently reduced benefits.<sup>187</sup> Individuals who retire early at age sixty-two face a permanent twenty-five percent reduction in benefits, which will increase to a thirty percent reduction when the normal retirement age is sixty-seven.<sup>188</sup> One way to encourage longer work lives and still allow early retirement is to shift the early retirement penalty. This is possibly the best way to incentivize continued work at older ages and protect the very elderly from poverty.

One proposed solution to incentivize work at older ages is to place most of the early retirement penalty at the onset of benefits.<sup>189</sup> A permanent twenty-five percent reduction does not do enough to discourage claiming early benefits and results in low benefits when individuals are old and truly unable to support themselves.<sup>190</sup> Having a large initial benefit cut for early retirees (or smaller initial benefit) that later returned to a full benefit would incentivize continued work and protect the most vulnerable seniors.<sup>191</sup> Although workers currently face a permanent twenty-five percent reduction for claiming benefits at the earliest age, a better solution is to increase the initial reduction to fifty percent or greater.<sup>192</sup> In addition to the substantial initial benefit cut, the penalty would be slowly reduced over a period of years until the individual received a full benefit.<sup>193</sup> This reform would reduce the incentive to retire early and still retain the program's safety net function.<sup>194</sup>

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187. 42 U.S.C. § 402(q)(1) (2000).

188. GRAHAM, *supra* note 141, at 57.

189. *Id.* at 125–26.

190. *See id.* at 104.

191. *See id.* at 95–96.

192. *See id.* at 127. For example, Graham places the initial cut at fifty percent and then slowly reduces the penalty until the beneficiary has full benefits at age sixty-eight. *Id.*

193. *Id.*

194. *Id.* at 94. “Frontloading benefit cuts could shift Social Security’s incentives towards more delayed retirement, making it less likely that individuals would retire too early thinking their savings and benefits would be sufficient, only to realize too late that they had misjudged their needs.” *Id.*

## V. Conclusion

Incentivizing work at older ages should be an important public policy goal of the United States. One of the government's largest programs, Social Security, has inherent disincentives towards longer work lives by older citizens. This Note is not designed as a way to cure all of Social Security's projected revenue shortfalls. Working longer will likely improve the looming deficit, but it is not a total solution. Unfortunately, even with these proposed changes, benefit reductions or substantial tax increases may be necessary for Social Security's solvency. By incentivizing longer work lives, individuals will be better prepared for their retirement.

Reforming the Social Security benefit calculation, providing tax incentives, eliminating the Social Security retirement earnings test, and adapting the retirement age will all reduce the disincentives toward continued work. A complete Social Security reform plan will also incorporate other aspects of increased revenues and decreased benefits. Unfortunately, no policy that adequately improves Social Security's budget will be pain-free. Encouraging longer work lives must be included in any reform as it reflects the changing nature of life expectancy, health, skills, and overall ability of workers at older ages.