DO SPOUSES COORDINATE THEIR RETIREMENT DECISIONS?

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inside

Introduction

The movement of married women into the labor market is transforming retirement behavior. A generation ago, when few married women spent many years in the labor force, it was relatively simple for spouses to coordinate their retirement decisions. Couples typically focused on the generosity of the husband's retirement benefits and the impact of his retirement decision on future benefits. Today, however, retirement decisions are more difficult to coordinate, because many women have accumulated substantial retirement benefits in their own names. As a result, many couples now need to consider how the decision to stop work will affect income and retirement benefits for both spouses. The evidence suggests that couples like to retire together and, since husbands tend to be older than their wives, the increased labor force participation of women may lead to later retirement of men. This *brief* examines retirement behavior and measures the extent to which husbands and wives appear to coordinate their retirement decisions.

What Affects the Retirement Decision?

Economists predict that workers weigh the benefits of increased leisure time against the costs of lost labor market compensation when making retirement decisions. According to standard theory, factors that reduce the cost of retirement, such as health insurance benefits or generous public and private pension benefits that replace pre-retirement income, encourage workers to retire. Factors that raise the cost of employment, such as health problems that make work increasingly difficult, also tend to accelerate retirement. For example, many studies have found that poor health, and especially declining health, are some of the strongest predictors of early retirement.[1]

Lack of health benefits in retirement can discourage workers from leaving the labor force. Most working-age Americans receive health benefits from their employers, and the loss of these benefits can substantially raise the cost of retiring before age 65, when virtually all Americans qualify for Medicare coverage. Those who lose their employer-

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[1] Bazzoli (1985); Bound et al. (1999).

sponsored health benefits before age 65 must turn to the private nongroup market for health insurance coverage, unless they can receive benefits from their spouses' employers. Coverage in the nongroup market can be prohibitively expensive, especially for those with pre-existing medical conditions. Some employers offer their retirees subsidized health benefits, which tend to encourage workers to retire early.[2] But fewer and fewer employers are now offering retiree health benefits.[3] Many workers without access to retiree health benefits wait until they qualify for Medicare benefits at age 65 before retiring.

Social Security and traditional employer-sponsored pension plans also create powerful, yet complex, incentives to retire. Social Security pays lifetime annuities that depend on the amount of earnings people receive throughout most of their worklives.[4] By enabling retirees to live almost as well in retirement as they did while working, generous retirement benefits encourage workers to withdraw from the labor force and enjoy more leisure time. In fact, many workers choose to retire as soon as they can begin collecting Social Security benefits at age 62, and would probably retire even earlier if they had access to retirement income at younger ages.

Similar types of incentives are embedded in traditional employer-sponsored pension plans, which cover about 38 percent of full-time workers now approaching retirement.[5] They provide lifetime annuities that begin at retirement and pay monthly benefits that are typically expressed as a multiple of years of service and earnings received near the end of the career (e.g., 1 percent of average salary received during the final three years on the job times the number of years of service). Although this stream of benefits tends to encourage workers to retire, changes in future retirement benefits resulting from continued employment create other, sometimes conflicting, incentives. For example, working an additional year raises future benefits by increasing the percentage of pay that goes into the benefit calculations. An additional year of work also generally raises earnings, through a combination of real wage growth and inflation, which in turn increases the value of all previous benefit accruals. The incremental growth in future benefits is especially high for more senior employees who have accumulated many years of service, and provides strong incentives for them to remain in the labor force and with the employer.

At some point — usually the age at which workers can begin collecting full retirement benefits — the value of future pension benefits in traditional plans generally declines. The normal retirement age, as it is known, varies across plans but is usually set at ages 62 or 65. Workers forego a year of retirement benefits for every year that they remain on the job past the plan's normal retirement age. And, in many plans, the increase in annual benefits from an additional year of work is insufficient to offset that loss. As a result, the value of future benefits often falls for workers who stay on the job past the normal retirement age.

In addition, many plans subsidize early retirement benefits. Early retirement provisions allow workers to collect reduced benefits before they qualify for full benefits — often as early as age 55. While annual benefits received under these provisions are lower than those received at the normal retirement age, the reduction is often insufficient to offset fully the additional pension installments. These early retirement subsidies can provide workers with strong incentives to drop out of the labor force at relatively young ages, and many workers appear to respond to these incentives by retiring early.[6,7]

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[2] Gruber and Madrian (1995); Johnson, Davidoff, and Perese (2003); Rogowski and Karoly (2000).

[3] Kaiser Family Foundation and Health Research and Educational Trust (2003).

[4] Workers with 40 or more quarters of covered employment qualify for Social Security retirement benefits, which are based on earnings received during the 35 years in which the worker had the highest earnings, up to certain limits. Those who retire at the full retirement age, which had been 65 but is now increasing gradually to 67, receive full benefits. Workers can begin collecting reduced retirement benefits at age 62. Current rules reduce benefits below the full amount by 6.67 percent per year for the first three years that retirees collect payments before the full retirement age, and then by 5 percent per year for each additional year of receipt before the full age. The system also rewards those who delay retirement with higher benefits. For those turning 62 in 2005, benefits increase by 8 percent for each year that beneficiaries delay claiming beyond the full retirement age, up to age 70.

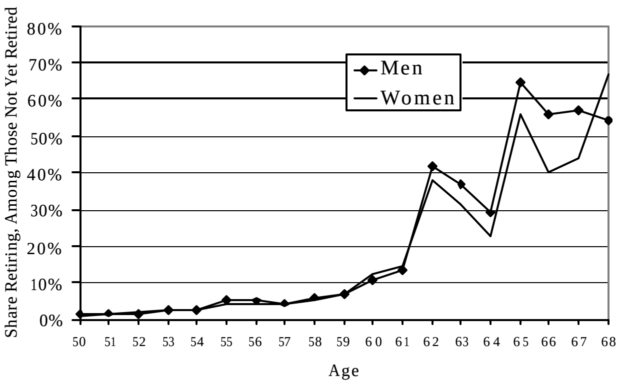
[5] This estimate is based on a nationally representative sample of adults ages 55 to 59 in 2002 from the Health and Retirement Study.

[6] Samwick (1998); Stock and Wise (1990).

[7] Defined contribution retirement plans, which include 401(k) plans, generally do not create incentives for workers to retire early. These plans, which have been growing in popularity and now cover almost twice as many households as traditional employer-sponsored plans (Munnell and Sundén 2004), function essentially as tax-advantaged retirement savings accounts to which both employers and employees generally contribute. Workers receive at retirement the funds that have accumulated in their accounts, generally as lump-sum distributions. Because account balances typically increase steadily over time, participants do not generally forfeit future benefits by delaying retirement. As a result, workers in defined contribution plans appear to work longer than similar workers in traditional retirement plans (Munnell, Cahill, and Jivan 2003).

Actual retirement rates — the share of workers who retire in any given year — rise slowly with age when workers are in their 50s, reaching about 14 percent by age 61 for both men and women (see Figure 1).[8] They then soar at age 62, to 42 percent for men, reflecting the availability of early Social Security benefits and possibly employer-sponsored pension benefits. After dropping at ages 63 and 64, they spike again at age 65, the full retirement age for Social Security for Americans born before 1938 and the age of Medicare eligibility. Nearly two-thirds of men working at age 64 retire the following year. Retirement rates fluctuate at later ages, but they remain high throughout the late 60s.

Figure 1. Share of Men and Women Retiring, by Age

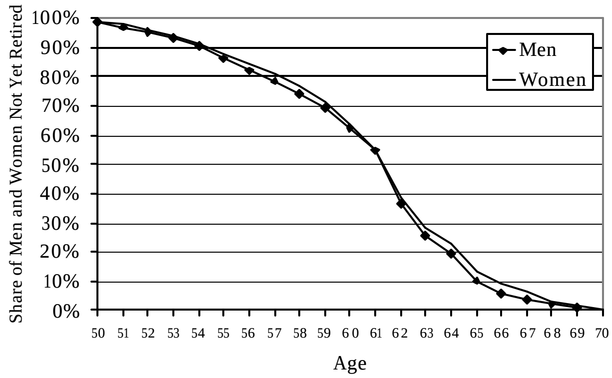


Source: Author's estimates from the 1992-2002 waves of the Health and Retirement Study.

Note: The sample is restricted to men and women born between 1931 and 1941 and employed at age 50. Estimates define retirement based on how respondents classify their own work status.

More than one-half of men and women working at age 50 retire by age 62 (see Figure 2). About one-quarter retire by age 58, and 90 percent retire by age 65, although some find new jobs after leaving the careers they pursued for most of their working lives. There are few differences in retirement patterns between men and women.

Figure 2. Share of Men and Women Not Yet Retired, by Age



Source: Author's estimates from the 1992-2002 waves of the Health and Retirement Study.

Note: The sample is restricted to men and women born between 1931 and 1941 and employed at age 50. Estimates define retirement based on how respondents classify their own work status.

How Do Married Couples Decide When to Retire?

Retirement decisions are typically more complex for married couples than single individuals. Because married men and women tend to enjoy spending time with their spouses, married couples often try to retire together. But differences between husbands and wives in their employment and personal circumstances can complicate these efforts. For example, from an employment standpoint, one spouse may hold a fulfilling, challenging job that she wishes to pursue until late in life, while the other faces long hours of repetitive, physically demanding work on a job that he wants to leave as soon as possible. From a personal standpoint, spouses often differ in age, and the older spouse may be ready for retirement before the younger spouse. Married men nearing retirement today are on average almost four years older than their wives, and in 1 out of 10 marriages they are more than 10 years older than their wives.[9] In addition, health problems may prompt one spouse to consider retirement, while the other spouse enjoys robust health and prefers to remain at work.

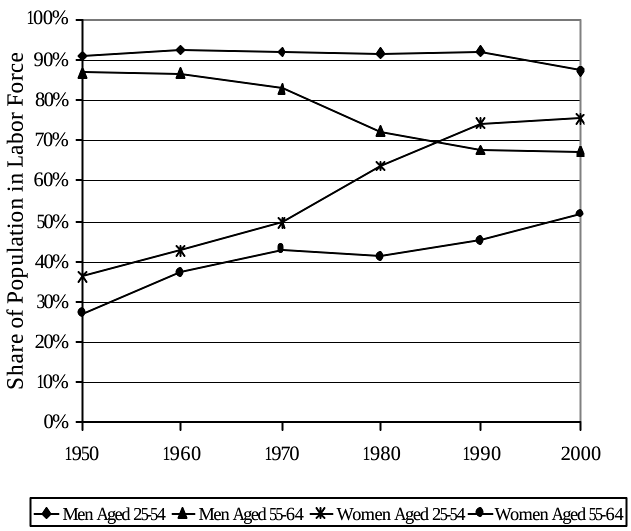
Coordinating retirement decisions is even more difficult when both spouses have strong ties to the labor force. A generation ago, most married

[8] Estimates are based on a sample of men and women born between 1931 and 1941 in the Health and Retirement Study. These estimates classify people based on how they describe their work status. Under this definition, some retirees may be working, because some respondents describe themselves as retired after they leave the jobs they held for most of their working lives even if they subsequently take other jobs.

[9] These estimates are based on data on married men ages 53 to 64 from the 2000 wave of the Health and Retirement Study.

women stopped working when they were raising their children. They generally did not establish the long employment histories necessary to accumulate substantial retirement benefits on their own. Over the past 50 years, however, the employment of women has increased steadily. Between 1950 and 2000, the share of women ages 25 to 54 participating in the labor force more than doubled, while the share of men in that age group participating in the labor force declined slightly (see Figure 3). Almost one-half of women nearing traditional retirement age today are in the labor force, compared with only about one-quarter of women 50 years ago. And working women who are now approaching retirement are almost as likely as men to have employer-sponsored pension coverage, although they have not generally accumulated as many rights to future benefits as men.[10] For many couples, it may not make financial sense for the wife to follow her husband out of the labor force at the time that simply maximizes *his* retirement benefits.

Figure 3. Labor Force Participation Rates by Age and Gender, 1950-2000



Source: Bureau of Labor Statistics (2003).

Because retirement incentives generally differ across pension plans, joint retirement decisions often involve difficult trade-offs between the future pension benefits of husbands and those of their wives when both spouses are covered by retirement plans. Consider the case of a man in a plan with a normal retirement age of 62, whose wife is three years younger than him and in a plan with a normal retirement age of 65. The man may be able to maximize the value of his future pension benefits by retiring at age 62, but the woman could end up with much less generous benefits of her own if she retired with her husband and quit her job at age 59, instead of remaining with her employer until age 65.

Social Security is structured somewhat differently than traditional employer-sponsored pension plans, but it also often creates different retirement incentives for husbands and wives. For example, unlike employer plans, Social Security offers retirement benefits to spouses, adding to the complexity of joint retirement decisions for husbands and wives. Married adults can collect half of the Social Security retirement benefits paid to their spouses, instead of collecting benefits based on their own earnings. As a result, those with spouses who earn considerably more than they do themselves receive the same level of Social Security benefits regardless of how much they work. The availability of spousal benefits reduces the returns to work for these people, and hence lowers work incentives. On the other hand, high-earning spouses — who can receive additional rights to future retirement benefits for both themselves and their spouses by working more — have an incentive to work longer.[11]

Do Married Couples Retire Together?

Despite the difficulty of coordinating spousal retirement decisions, a substantial share of married adults now retire at about the same time as their spouses. In nearly one in five married couples, husbands and wives retired in the same year (see Table 1).[12] Another 30 percent of these husbands retired either one or two years before their wives, or one or two years after their wives. Overall, then, in about one-half of these retired couples, husbands and wives left the labor force within two years of each other. The share of husbands and wives who

[10] Johnson (1999).

[11] The rise in employment and earnings by married women will likely increase the share receiving benefits based solely on their own earnings records.

[12] These data come from a sample drawn from the Health and Retirement Study. The sample was restricted to couples in which at least one spouse was between the ages of 61 and 71 in 2002, both spouses were retired by 2002, and both worked at some point after age 49 or in 1992. These estimates define retirement based on how respondents classify their own work status.

Table 1. Percentage Distribution of the Difference in Retirement Timing of Husbands and Wives

Husband Retires	All	Husband and Wife Differ in Age by No More than 2 Years	Husband Is at least 3 Years Older than Wife	Husband Is at least 3 Years Younger than Wife
10 or more years earlier	8.7%	2.9%	12.9%	1.2%
5 - 9 years earlier	15.2	8.1	20.8	3.9
3 - 4 years earlier	11.5	7.5	14.9	3.9
1 - 2 years earlier	18.2	21.7	15.9	19.8
Same year	18.7	24.0	16.6	8.2
1-2 years later	12.0	16.7	9.1	11.9
3-4 years later	6.0	9.9	3.1	10.9
5-9 years later	7.0	6.8	5.4	22.2
10 or more years later	2.7	2.2	1.2	18.0
Share of retired couples	100.0	35.1	58.2	6.7

Source: Author's estimates from the 1992-2002 waves of the Health and Retirement Study.

Note: Estimates are based on a sample of 784 married couples who were first interviewed in 1992. The sample was restricted to couples in which at least one spouse was born between 1931 and 1941, both spouses worked after age 49 or in 1992, and both spouses retired by 2002.

retire at about the same time rises when age differences between spouses diminish. For example, among couples in which spouses differ in age by no more than two years, 62 percent of retired husbands left the labor force within two years of their wives' retirements.

Extreme differences between husbands and wives in the timing of retirement exist, but they are rare. In 9 percent of couples, the husband retired more than 10 years before the wife, and in 3 percent of couples the wife retired more than 10 years before the husband. Husbands retired first in slightly more than one-half of the retired couples, and wives retired first in about one-quarter of the retired couples.

Does Spouse's Employment Affect Retirement?

Workers appear to be more likely to retire when their spouses have already retired. One strand of research compares retirement patterns by the relative age of the spouse. If spouses coordinate their retirement decisions, workers with younger spouses will likely retire later than those with older spouses. In fact, married men more than five years older than their wives tend to remain at work longer than men who are younger than or the same age as their wives (see Figure 4).

Figure 4. Share of Married Men Not Yet Retired, by Relative Age of Wife

Source: Author's estimates from the 1992-2002 waves of the Health and Retirement Study.

Note: Estimates are based on a sample of 784 married couples who were first interviewed in 1992. The sample was restricted to couples in which at least one spouse was born between 1931 and 1941, both spouses worked after age 50 or in 1992, and both spouses retired by 2002.

Another study has found that married men respond to the financial incentives that their wives face in Social Security and employer-sponsored pension plans.[13] For example, an increase of $1,000 in the return to work for the wife reduces the husband's relative retirement probability by 0.8 percent, holding all else constant. Because it is hard to imagine how retirement incentives for women could directly affect their husbands' work decisions, this statistical relationship suggests that these men are staying in the labor force because their wives are delaying retirement. Interestingly, women do not appear to respond to their husbands' work incentives, perhaps because men value spending time in retirement with their spouses more than women do. Women may have more activities than men to occupy their time in retirement if their spouses are working.

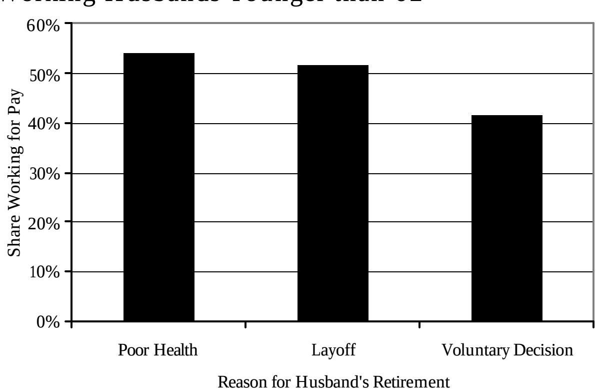
[13] Coile (2003).

In fact, a study of married couples in New York State found that newly retired men were least satisfied with retirement when their wives continued to work.[14]

Another recent study also found that having a retired spouse increased the likelihood of retiring, and that the effects were larger for men than for women.[15] For men, the impact on retirement of a retired wife is equivalent to the effect of being one year older. For women, the impact of a retired husband is equivalent to the effect of being about three-quarters of a year older. Joint retirement is especially prevalent among those who report that being with their spouse is a "very important" benefit of retirement.

Husbands and wives are less likely to retire together, however, when one spouse is forced into retirement by health problems or the loss of a job.[16] For example, among married women ages 51 to 61 whose spouses were not yet age 62 and thus did not qualify for Social Security retirement benefits, only 42 percent of those whose husbands had voluntarily retired were working in 1992 (see Figure 5). By contrast, 54 percent of those whose husbands were forced to retire because of health problems remained at work. Only about 1 in 10 married men are forced out of the labor market at relatively young ages. But when they are, their wives may be compelled to remain at work (or enter the labor force if not currently employed) to compensate for the loss in family income. Few wives (or husbands) appear to drop out of the labor force to provide care to their frail spouses.

Figure 5. Share of Married Women Ages 51-61 Working for Pay in 1992, among those with Non-Working Husbands Younger than 62



Source: Johnson and Favreault (2001).

Does Joint Decisionmaking Have Policy Implications?

Interdependencies in spousal retirement decisions have important implications for policy choices. Failing to recognize the tendency for husbands and wives to coordinate their retirement decisions can distort the predicted labor supply impact of policy initiatives.

Consider proposals to reform Social Security to increase work incentives at older ages and encourage workers to delay retirement. This issue is becoming increasingly important as the aging of society raises the burden of supporting the older population. Recent proposals include increasing the full retirement age (to as high as 70 in some cases and tying future increases to changes in life expectancy), raising the early entitlement age from 62 to 65, and eliminating the earnings test before the full retirement age (which reduces benefits by one dollar for every two dollars of earnings). These proposals could induce workers to delay retirement, by increasing the returns to work at older ages and, indirectly, by inducing their spouses to remain at work.[17] Ignoring the indirect effect of spousal work decisions could lead analysts to underestimate the impact of these proposed initiatives. For example, failing to account for the effect of wives' work decisions on their husbands' retirement behavior can understate the estimated impact of delaying the full retirement age on men's labor supply by 13 percent.[18]

Conclusion

Choosing when to retire is a complex family decision. Careful planning requires families to weigh the generosity of future retirement benefits and other sources of wealth against uncertain future income needs. They must predict what their future earnings and retirement benefits would be if they delayed their retirement. They must evaluate current and future health status. And they need to balance the social benefits of employment — engaging in fulfilling work and maintaining meaningful social ties at the workplace, for example — against the benefits of engaging in rewarding leisure activities and volunteer work in retirement.

[14] Moen, Kim, and Hofmeister (2001).

[15] Gustman and Steinmeier (2004 forthcoming).

[16] Johnson and Favreault (2001).

[17] Increasing the returns to work can affect labor supply in opposite ways. On one hand, by raising the relative price of leisure time, higher returns discourage people from spending time on leisure activities and induce them to work more. On the other hand, higher returns raise incomes, which can lead workers to devote more time to leisure and work less. The empirical evidence indicates that, on balance, workers tend to increase labor supply when the returns to work rise (Killingsworth 1983).

[18] Coile (2003).

These decisions are especially complex for married couples when both spouses work, an increasingly common situation. Spouses often face conflicting incentives to retire. Many husbands and wives differ in age and health status, and they often belong to separate employer-sponsored pension plans that provide financial incentives to retire at different ages. Despite these coordination problems, however, many husbands and wives continue to retire together. Because more married women are working now than in the past and men are typically a few years older than their wives, the tendency for joint retirement may contribute to the recent increase in the average retirement age for men. Therefore, failing to recognize the general preference of husbands and wives to coordinate their retirement decisions can understate estimates of the potential impact of proposed policy initiatives on labor supply.

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