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AN "ELASTIC" EARLIEST ELIGIBILITY AGE FOR SOCIAL SECURITY

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Introduction

In the early 1980s, Congress responded to the Social Security program's long-term financing shortfall, in part, by raising the Full Retirement Age (FRA) from 65 to 67. When fully phased in, for those who turn 62 in 2022, workers will have to wait an additional two years to get the same monthly benefit. If they do not postpone claiming, the increase in the FRA will cut their benefits by about 13 percent.

Congress did not change the earliest age at which workers can claim. This Earliest Eligibility Age (EEA) remains 62. When the increase in the FRA is fully phased in, workers who claim at 62 will get 70 percent, rather than 80 percent, of their FRA benefit. This has raised concerns that benefits claimed at the EEA will be too low, especially as retirees age and other sources of income decline. One response would be to raise the EEA from 62 to 64, in line with the two-year rise in the FRA.[1]

There are, however, two important objections to an increase in the EEA. The primary concern is that it would create hardship for those unable to work or find employment and who lack the resources to support themselves without working until age 64. A second objection is that raising the EEA is unfair to disadvantaged groups with low life expectancy. This *brief* addresses these concerns by considering an "Elastic" EEA, which gives different workers different earliest eligibility ages.

The EEA Arguments

Raising the EEA would improve income security by increasing each worker's minimum monthly benefit over their retirement years. Given rising longevity, the shift to less strenuous and more rewarding employment, and strains on the retirement income system, it seems reasonable to raise the socially defined notion of when retirement can "normally" begin. The primary objections to raising the EEA are the hardship and unfairness such a change could produce.

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Pro: Improved Retirement Security

Social Security reduces the monthly benefits of workers who claim before the Full Retirement Age (FRA) to offset the longer period of benefit receipt. These reductions are designed to maintain the value of lifetime benefits at their FRA level, no matter when they are claimed. As the FRA rises from 65 to 67, workers who claim at 62 will find it increasingly difficult to maintain living standards on these reduced monthly benefits. The problem is illustrated in Table 1, which shows benefit amounts in 2005 had the FRA been 67. All workers will have a more difficult time maintaining their standard of living as benefits replace a smaller share of pre-retirement earnings. But the problem is most acute for low-wage workers, defined by the Social Security Administration as those who earn 45 percent of the average earner's wage. If the FRA in 2005 had been 67, such workers who claim at 62 would have gotten just $6,780, far below the poverty threshold of $9,570 for a one-person household. Even the benefit of an average earner who claimed at 62 — $11,332 — would be only 18 percent above poverty. If the EEA were raised to 64, benefits for low-wage workers would still fall below the poverty threshold. But the higher minimum monthly benefit would clearly improve retirement income security.

Table 1. Annual Social Security Benefit by Claiming Age if the FRA in 2005 were 67

Earner type	Claimed at 62		Claimed at 64	
	Benefit	% of poverty	Benefit	% of poverty
Low earner	$6,780	71%	$7,748	81%
Average earner	11,332	118	12,951	135
High earner	14,659	153	16,753	175

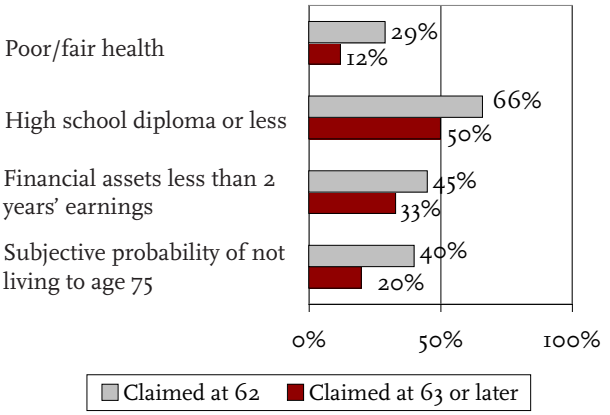
Note: Following the Social Security Administration, a low earner makes 45 percent, an average earner 100 percent, and a high earner 160 percent of the national average wage, which was $36,953 in 2005. The poverty threshold for a one-person household in 2005 was $9,570.
Sources: Authors' calculations based on U.S. Social Security Administration (2006) and U.S. Social Security Administration (2007).

Con: Hardship for Those at Risk

Increasing the EEA would create hardship for many who find it difficult to work from 62 to 64. Workers with enough assets could live off those resources and collect higher monthly benefits at 64. Workers with a serious health problem could qualify for Social Security disability benefits. But workers with insufficient assets, and with less serious health problems or little demand for their labor, could have considerable difficulty supporting themselves from 62 to 64.

Health problems and weak labor-market prospects are quite common among workers who claim at 62. Nearly 30 percent of all men who claim at 62 report being in poor or fair health, as opposed to about 10 percent of men who claim later (see Figure 1). Two-thirds of these early takers have a high school diploma or less, and older workers with low educational attainment have especially poor job prospects[2] and are disproportionately prone to displacement.[3]

Figure 1. Incidence of Risk Factors for Men by Age of Claiming Social Security Benefits, 1992-2004.



Source: Authors' calculations from University of Michigan, *Health and Retirement Study* (HRS), 1992-2004.

Less educated older workers are also less likely to have adequate private pensions or other financial resources.[4] Raising the EEA would thus require workers with health and labor-market problems to prolong their work lives or have inadequate incomes until age 64.

Con: Unfairness to Groups with Short Life Expectancy

Forcing workers with average life expectancy to claim at 64 rather than 62 does not reduce the value of lifetime benefits. But it does reduce the value of lifetime benefits for workers with below-average life expectancy, such as African American men and low-wage workers. Because such workers receive benefits over a shorter period of time, the lifetime value of benefits claimed at any age is less than the value received by workers with greater life expectancy. But the disparity is greater for benefits claimed at 64 than 62. The reason is that the two-year reduction in benefit receipt represents a greater share of a shorter life expectancy. For example, if the EEA were raised from 62 to 64, the lifetime value of a given monthly benefit claimed at the EEA by African-American men would fall from 89 percent to 87 percent of the value received by whites.[5]

An "Elastic" EEA Based on Lifetime Earnings

The policy objectives for reforming the EEA are to improve retirement income security while minimizing the hardship and unfairness a higher EEA creates. The traditional approach would raise the EEA and address the adverse effects using other public programs or by changing other features of the Social Security program. The alternative is an "Elastic" EEA, which assigns different workers different earliest claiming ages, based on a rule that achieves these policy objectives.

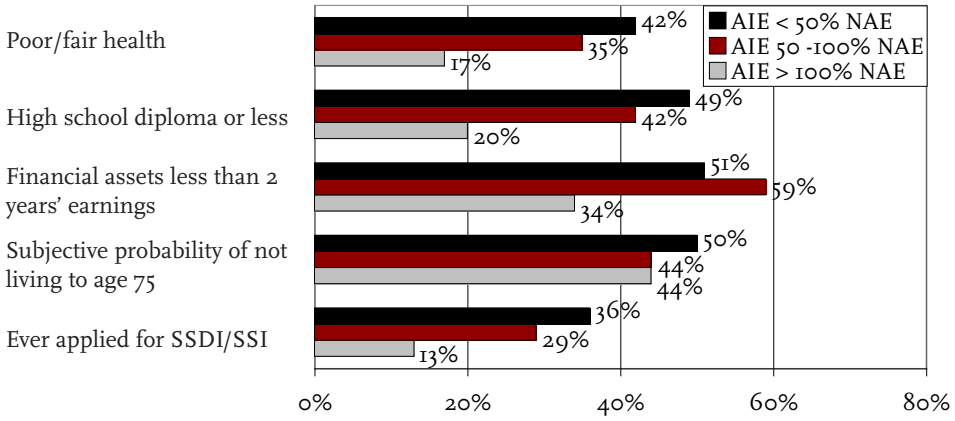
Under the traditional approach, the hardship caused by a higher EEA could be mitigated by expanding Social Security's Disability Insurance (DI) and Supplemental Security Income (SSI) programs or other social welfare programs. The unfairness could be offset within a larger package of reforms that produced a more even distribution of gains and losses.[6] But expanding DI, SSI, or public means-tested programs could prove a difficult sell among policymakers concerned about budgetary pressures.[7] And no large package of Social Security or welfare reforms that includes such offsets to unfairness is working its way through Congress. So while the adverse effects of a higher EEA could be mitigated by changes in other public programs, this approach to raising the EEA has gained little traction.

An Elastic EEA could potentially raise the earliest claiming age for most workers while shielding those for whom a higher EEA would result in hardship or an unfair loss. A key concern is how to assign EEAs to accomplish this objective. In an earlier research project, several authors of this *brief* investigated an Elastic EEA based on the length of a worker's employment history.[8] The intuition is that less educated workers, who enter the labor force at relatively young ages, are most at risk from a rise in the EEA. They disproportionately have physically demanding jobs, which increases the incidence of health problems and makes work difficult at older ages; they have relatively poor employment prospects at older ages; and they have relatively low life expectancy. But while less educated workers enter the labor market early, it turns out that they do not have relatively long employment histories. Health impairments and lackluster demand for their labor, which would put such workers at risk if the EEA were raised, also result in less time spent in employment by age 62 than for workers not at risk. So an Elastic EEA based on employment history would not produce the desired result.

In the course of this research, a different marker — average lifetime earnings — emerged as a more promising basis for an Elastic EEA. Assigning EEAs based on average lifetime earnings could raise the earliest age most workers could claim while protecting most who would be hurt by such a change. Such an Elastic EEA would be effective because workers at risk of hardship and with low life expectancy tend to have low lifetime earnings. Protecting such workers from a general increase in the EEA would mitigate the hardship and unfairness while improving retirement income security for the majority.

Using data from the *Health and Retirement Study* (HRS) and the Social Security Administration, Figure 2 on the next page shows the relationship between estimated average lifetime earnings at age 55, as measured by Average Indexed Earnings (AIE) relative to the national average wage and various worker characteristics at age 63 that could create hardship or unfairness should the EEA be raised. The method used to estimate average lifetime earnings is biased downward for certain workers. As the AIE calculation

Figure 2. Incidence of Risk Factors for Men Age 63, by Ratio of Average Indexed Earnings (AIE) to National Average Earnings (NAE), 1992-2004

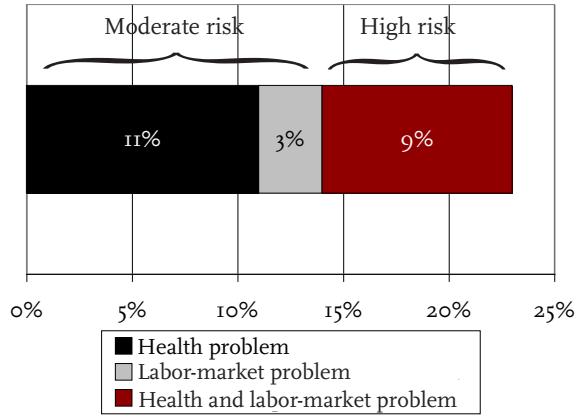


Note: The ratio of Average Indexed Earnings to National Average Earnings is calculated when the worker is age 55.
Source: Authors' calculations from 1992-2004 HRS.

includes only earnings covered by the Social Security program, it does not count wages earned abroad (either by immigrants or U.S. workers employed outside the United States) or while employed by a state or local government not covered by Social Security.[9] Nevertheless, low average lifetime earnings, as given by this measure, are clearly associated with a lack of financial assets, fair or poor health, low educational attainment, low subjective life expectancy (which has been shown to be a reasonably good indicator of actual life expectancy), and having applied for Social Security DI or SSI benefits.

To get a sense of the relationship between average lifetime earnings and the overall risk of hardship from an increase in the EEA, workers can be grouped into three risk categories. Those at 'high risk' of hardship have both a health problem and a labor-market problem and lack the resources needed to support themselves to age 64 without working. Those at 'moderate risk' have either a health problem or a labor-market problem, but not both, and cannot support themselves to age 64 without working. Workers 'not at risk' either can support themselves to age 64 without working or have neither a health nor a labor-market problem. To assign workers in the HRS to these risk categories, non-housing financial assets at 63 of less than two years' lifetime average earnings indicates inadequate resources to bridge the gap from 62 to 64 without working. A self-report of fair or poor health or a work-limiting health condition indicates a health problem. A labor-market problem is indicated by peak earnings from age 55 to 60 of less than 80 percent of national average earnings at 55. This categorization results in 9 percent of men in the HRS in the 'high risk' group and 14 percent in the 'moderate risk' group (see Figure 3).

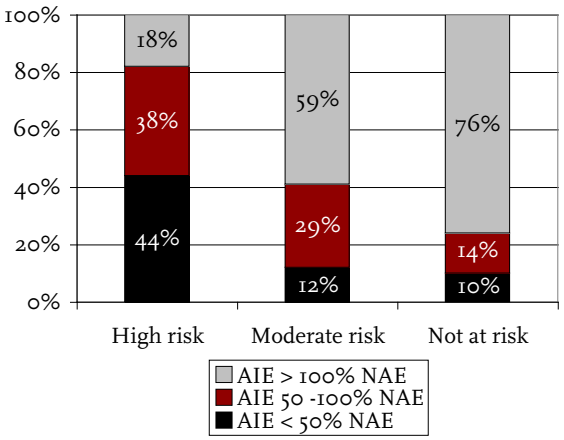
Figure 3. Percent of Men 'At Risk' of Hardship from a Rise in the EEA, 1992-2004



Note: All men reported in this figure lack the resources to support themselves without working from age 62 to 64 based on their level of financial assets.
Source: Authors' calculations from 1992-2004 HRS.

As shown in Figure 4, our measure of average lifetime earnings (AIE) is a powerful predictor of risk as specified above. In the 'high risk' group, over 80 percent had average lifetime earnings below the national average and 44 percent had earnings less than half the national average. In the 'moderate risk' group, more than 40 percent had earnings below the national average and 12 percent had earnings less than half the national average.

Figure 4. Hardship Risk for Men, by Ratio of Average Indexed Earnings (AIE) to National Average Earnings (NAE), 1992-2004



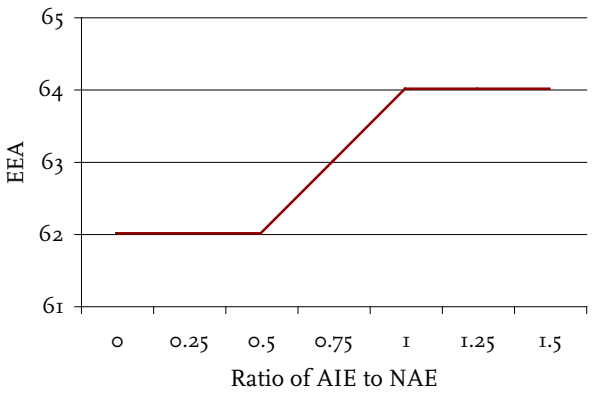
Note: The ratio of AIE to NAE is calculated when the worker is age 55. Those at 'high risk' of hardship have both a health problem and a labor-market problem and lack the resources needed to support themselves to age 64 without working. Those at 'moderate risk' have either a health problem or a labor-market problem, but not both, and cannot support themselves to age 64 without working. Workers 'not at risk' either can support themselves to age 64 without working or have neither a health nor a labor-market problem.
Source: Authors' calculations from 1992-2004 HRS.

An Elastic EEA based on average lifetime earnings thus seems capable of addressing the issue of hardship. It could also address the issue of fairness, as low-wage workers have low life expectancy. The Social Security Administration already calculates average indexed earnings for each worker. So an Elastic EEA based on average indexed earnings would be reasonably easy to implement.

An Elastic EEA

A simple example of an EEA based on average indexed earnings (AIE) is shown in Figure 5. For workers with AIE of 50 percent of national average earnings or less, the earliest claiming age would remain 62. For workers with AIE equal to or greater than the national average wage, the earliest age of claiming would rise to 64. For workers with AIE between 50 and 100 percent of national average earnings, the earliest age of claiming would rise by a month for each .48 percentage point increase in AIE above 50 percent of national average earnings. For example, a worker with an AIE equal to 75 percent of national average earnings could claim at 63 (25 x .48 = 12 months).[10]

Figure 5. Example of an Elastic EEA based on Ratio of Average Indexed Earnings (AIE) to National Average Earnings (NAE)



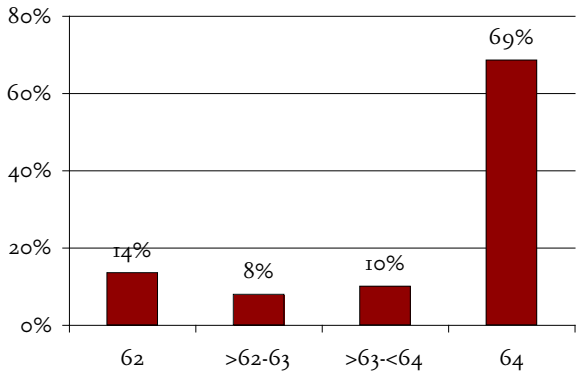
Source: Authors' illustration.

Each worker's earliest claiming age should be set early enough so that workers could adjust their retirement plans. In the example presented below, EEAs are based on a worker's AIE relative to the national average wage at age 55. There is not much change in men's AIE (relative to national average earnings) between 55 and 62. So their EEA would generally be much the same whether set at 55 or 62. Notifying workers of their EEA in their mid-50s would also function as a "wake-up call" to plan for retirement.[11]

This simple specification would be reasonably successful in achieving policy objectives for reforming

the EEA. As shown in Figure 6, the earliest claiming age would rise to 64 for close to 70 percent of men, with less than 15 percent eligible at 62. But the EEA would remain unchanged, or rise by less than a year, for two-thirds of the men classified above as having a 'high risk' of hardship and a quarter of those classified as having a 'moderate risk' of hardship (see Figure 7).

Figure 6. Distribution of Earliest Claiming Ages for Men under an Elastic EEA, 1992-2004

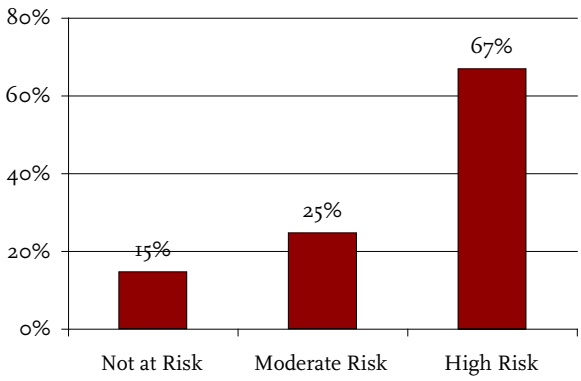


Source: Authors' calculations from 1992-2004 HRS.

If this Elastic EEA were applied to men in the HRS who claimed benefits before age 64, two-thirds would be required to delay by more than one year. Those allowed to claim at 62, or to wait no more than one year, are less healthy, less wealthy, less educated, and less likely to live past 75.

While this approach has significant promise for protecting high-risk men, its effect on those classified as 'not at risk' suggests the need for further research and refinement. Under this simple specification, 31 percent of men would have an EEA of less than 64. This could be too many. More troubling, over half of this group is classified as 'not at risk' (i.e., healthy and doing reasonably well in the labor market or with sufficient resources to support themselves for two years without working). Ideally, such workers should have to wait until 64 to claim.[12] These results could be due, in part, to the downward bias in estimates of some worker's average lifetime earnings (a bias that could largely be corrected in practice). A more accurate measure of risk might also show greater target efficiency.

Figure 7. Percent of Men with an EEA Less Than 63, by Hardship Group, 1992-2004



Note: This figure is based on the Elastic EEA described in the text.
Source: Authors' calculations from 1992-2004 HRS.

Fiscal Impact and Policy Objectives

The purpose of raising the EEA is to assure retirees a more adequate guaranteed monthly income. Because Social Security benefits are actuarially adjusted, raising the EEA would achieve that objective with little direct increase in program costs.[13] To the extent that a higher EEA resulted in later retirements, the finances of the federal government would actually benefit from higher income and payroll tax receipts with little or no increase in government obligations.[14]

An Elastic EEA would result in a modest increase in the cost of providing Social Security retirement benefits.[15] It is important to note, however, that an across-the-board increase in the EEA can be expected to increase other government expenditures. As shown in Figure 2, a significant share of low earning men have applied for DI or SSI benefits at some point in their lives.[16] Requiring such workers to wait until 64 to access Social Security retirement benefits can be expected to result in increased government expenditures on such programs. It is far from clear whether these increased expenditures, over the long-term, would be greater or less than the increased expenditures on an Elastic EEA.[17]

Conclusion

As the Full Retirement Age rises to 67, raising the Earliest Eligibility Age becomes an attractive option for assuring adequate retirement incomes. Raising the EEA, however, creates hardship for those unable to work or find employment and who lack the resources needed to support themselves from 62 to 64 without working. An Elastic EEA that sets a worker's earliest claiming age based on average lifetime earnings can capture many of the benefits of a higher EEA while avoiding many of the pitfalls. It should also be reasonably easy to implement.

The example of an Elastic EEA presented in this *brief* also demonstrates potential shortcomings. A non-trivial portion of the population classified as 'at-risk,' especially those classified as 'moderate risk,' was not protected or only partially protected. In addition, most men who qualified for an early EEA were classified 'not at risk.' This, in part, is due to the downward bias in our measure of average lifetime earnings.

If an Elastic EEA were put in place, the Social Security Administration should be able to produce far more accurate measures of average lifetime earnings for assigning EEAs. That calculation would also need to counteract the downward bias created by women's more interrupted employment histories, perhaps by omitting care-giving years.

Endnotes

1 Other responses include a minimum benefit, which would assure low-wage workers who retire early a basic income, but would do little to combat myopia on the part of other workers (Favreault, Mermin, and Steuerle, 2006); an educational campaign that would alert all workers of the benefits of claiming later; and fixing the minimum survivor benefit at the spouse's FRA benefit, paid for by further reducing early retirement benefits, which would combat myopia and assure widows and widowers higher monthly incomes (Sass, Sun, and Webb, 2008 forthcoming).

2 Mosisa and Hipple (2006).

3 Munnell et al. (2006).

4 Lundberg and Ward-Batts (2000).

5 The lifetime value of a given monthly benefit is calculated using a 3 percent real interest rate. Life expectancy for 60 year-old men is 18 years for African-Americans and 21 years for whites (U.S. Centers for Disease Control and Prevention, 2003). Life expectancy for 60-year-old men is 20 years for workers in the bottom half of the earnings distribution and 25 years for workers in the top half of the distribution (Waldron, 2007).

6 Munnell et al. (2004); and Mermin and Steuerle (2007).

7 Autor and Duggan (2006).

8 Haverstick et al. (2007).

9 We do exclude workers whose longest job, as recorded by the HRS, is employment in state or local government.

10 Gradually raising the EEA avoids abrupt changes in eligibility in response to minor changes in earnings, dampening the moral hazard that workers would reduce earnings to qualify for benefits earlier.

11 Workers would receive the information at age 56 after the Social Security Administration recorded their age 55 earnings and calculated their EEA. Setting the EEA much earlier might not be useful, as most men in their mid-fifties have a financial planning horizon of less than 5 years (Haverstick et al. 2007).

12 The 31 percent of men who would have an EEA of less than 64 breaks down as follows: 'high risk' — 8 percent, 'moderate risk' — 6 percent, and 'not at risk' — 18 percent. The 14 percent of men who could claim upon turning 62 breaks down as follows: 'high risk' — 4 percent, 'moderate risk' — 2 percent, and 'not at risk' — 7 percent. (The numbers in both of these cases do not sum to the totals due to rounding).

13 Raising the EEA would increase program costs to the extent that it increased survivor benefits, which are not factored into the actuarial adjustment. On the other hand, raising the EEA would improve Social Security's cash flow by postponing benefit payments.

14 Butrica, Smith, and Steuerle (2006).

15 Costs would rise under an Elastic EEA because low earners, with relatively low life expectancy, would not have their lifetime benefits reduced via a shortened period of benefit receipt, while the lifetime benefits of high earners would rise, due to their relatively long life expectancy, as their higher monthly benefits more than offset the shortened period of benefit receipt. The increase would be modest because the change in the value of lifetime benefits for low earners relative to high earners resulting from an increase in the EEA, as noted above, is small.

16 Twenty-one percent of men with average lifetime earnings at age 55 of less than 75 percent of the national average wage have applied for such benefits.

17 While an Elastic EEA could protect at-risk workers from hardships associated with delayed eligibility, it would not protect such workers from the meager benefits paid to low-wage workers at age 62. An option that would address this concern is to fix the EEA benefit at 80 percent of the FRA benefit. This would clearly increase program costs and worsen Social Security's long-term financing shortfall. On the other hand, it would reduce the incentive to claim DI benefits. The monthly DI benefit is the worker's monthly FRA benefit. When the FRA is 67, the DI benefit will be 43 percent higher than the age-62 retirement benefit. But it would be only 25 percent higher if the EEA benefit were fixed at 80 percent of the FRA benefit. Fixing the EEA benefit would also "flatten" the Social Security program, making benefits claimed prior to the FRA less sensitive to average lifetime earnings. This could be valuable as policymakers seek ways to close Social Security's financing shortfall by cutting benefits while preserving a minimum level of benefit adequacy.

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