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Social Security claiming decision of married men and widow poverty

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ABSTRACT

We find that most husbands claim Social Security before the ages that maximize the expected present value of their benefits. Although household benefits are only slightly reduced, the expected present value of widows' benefits reduces by 17.7%, increasing their risk of poverty.

1. Introduction

In the U.S., retired workers can claim Social Security retired worker benefits at any age from 62 to 70. The amount of their benefits depends on their primary insurance amount (PIA) and claim age.[1] Single men generally maximize the expected present value (EPV) of their retired worker benefits if they claim Social Security early.[2] But married couples almost always maximize the EPV of the total of the household's retired worker, spousal, and survivor benefits if the husband delays claiming for several years. Delayed claiming by married men could also greatly increase the amount of widow's survivor benefits—by as much as 60%.[3] Although there are many advantages to delaying claiming, data show that most married men claimed Social Security soon after becoming eligible, leaving Social Security wealth "on the table".

Previous literature finds that early claiming results in only a small reduction in the EPV of household benefits. We re-examine the loss from a new angle. Using Health and Retirement Study (HRS) data matched to Social Security earnings histories and claiming records, which are available to researchers on a restricted basis, we calculate claim ages that maximize the EPV of household benefits for each married couple in our sample. We show that, consistent with previous studies, the average loss of household Social Security wealth resulting from early claiming is only 3.1%. But early claiming has a significant effect on the distribution of resources within the household. The above loss can be decomposed into a 1.5% increase in the EPV of benefits payable during the husband's lifetime, and a 17.7% reduction in the EPV of benefits payable to the surviving widow.

The average woman outlives her husband by six years. Widows rarely have much financial wealth (Zick and Holden, 2000), and widowhood is often associated with large declines in income and assets, resulting in the surviving widow becoming heavily dependent on the Social Security survivor benefits (McGarry and Schoeni, 2005). Thus, the substantial reduction in widow's survivor benefits due to early claiming by married men could significantly increase the risk that their wife will face hardship as a widow.

The remainder of the paper is organized as follows. Section 2 briefly reviews the Social Security claiming literature. Section 3

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[1] The PIA is calculated based on workers' earnings history and is the amount of the retired worker benefits if claimed at the full retirement age (FRA). Benefits will be reduced if claimed before the FRA and increased if claimed after the FRA. For details, see Sass et al. (2008).

[2] As is conventional in the literature, we calculate EPVs using a 3% real interest rate and population average mortality in this paper.

[3] The survivor benefit the wife can receive upon death of the husband is based on his actual benefit, not the PIA.

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presents our new estimates of claim ages that maximize the EPV of household benefits. It also evaluates the losses in household benefits and in widow's survivor benefits due to early claiming. Section 4 concludes.

2. Literature

Two studies, Coile et al. (2001) and Munnell and Soto (2005), have investigated the effect of claim ages on the EPV of a married household's Social Security benefits. Both studies estimate the effect using hypothetical households, population mortality, and a 3% real interest rate. Coile et al. (2001) calculated the value of household Social Security wealth at different husband claim ages. They assumed that the husband has a PIA of $963, that the wife never works, and that claims are made as soon as possible. They also assumed that the husband was born in 1930 and the wife in 1932, so both have a full retirement age (FRA) of 65. The EPV of household benefits was maximized if the husband claimed at age 65 assuming the wife claimed at 63, when her husband claimed. If the husband claimed as early as possible, at age 62, the household lost $6270 in the EPV of household benefits, or 3%, relative to claiming at age 65. Munnell and Soto (2005) calculated the combination of claim ages that maximizes the EPV of household benefits, where both spouses were assumed to be born in 1948 and to have an FRA of 66. They showed how the maximizing claim ages depended on the age difference between the spouses and the relative sizes of their PIAs. The EPV of household benefits was generally greatest when the husband claimed between age 66 and 69. This is later than for the older cohort studied in Coile et al. (2001), reflecting the increase in life expectancy and a more generous delayed retirement credit for later birth cohorts.

3. New estimates of the effect of claim ages on Social Security wealth

In this section, we present calculations of our measure of Social Security wealth for a sample of married couples at different combinations of claim ages. Munnell et al. (2009a,b,c) identify several "unusual" Social Security claiming strategies, such as claiming and then repaying benefits, claiming spousal benefit now and retired worker benefit later, and claiming and then suspending benefits. In some circumstances, these strategies can increase the EPV of households' benefits. However, these strategies are rarely used, and the first has been prohibited. We therefore do not analyze them further.

Our calculations extend previous research in two ways: first, by looking at actual rather than prototypical households, we capture the effects of the joint distribution of the various determinants of Social Security wealth – for example any correlation between the relative PIAs of the husband and the wife and their age difference, which both affect the EPV of their benefits – that researchers using prototypical households either address with assumptions or ignore. Second, we calculate the EPV of household benefits for every possible combination of the husband's and wife's claim ages. This approach gives the maximum EPV, the EPV based on the ages at which the husband and wife actually claimed, and the amount (if any) each household left "on the table". In addition, actual claim ages, based on linked administrative records, are more accurate and often quite different from the self-reported claim ages found in the HRS. While the overall pattern of early claiming is quite similar to that found in the self-reported data, the discrepancies display the importance of using administrative data in analyses of claiming behaviors.

We use data from the HRS, a national representative panel of older individuals first interviewed in 1992. The HRS originally includes individuals born between 1931 and 1941 and their spouses at any age. They have been re-interviewed every two years, and younger cohorts were added to the survey in 1998 and 2004. The dataset contains considerable details on household demographic and socio-economic characteristics. In 1992, 1998, and 2004, individuals were asked for consent to use their earnings histories and Social Security claiming records. The administrative data are available to researchers on a restricted basis.

As is conventional in studying Social Security claiming decisions, such as Coile et al. (2001) and Hurd et al. (2004), we limit our sample to households in which the individuals had retired before age 62.[4] The age of claiming can thus be viewed as a purely financial decision, separate from their labor supply decisions.

The restricted dataset contains 3427 men who can be identified as married at age 62.[5] 2357 of them have their wife's earnings histories available in the dataset. We drop individuals who were still working at age 62 and were therefore not eligible to claim Social Security at 62. We define an individual as retired before 62 if his earnings in the year he turned 62 and the following year were both less than the Social Security retirement earning test (RET) threshold.[6] This reduces our sample to 694 married couples. We further drop men who claimed disabled worker benefits and individuals who have undocumented claim type codes, leaving 473 married couples in the final sample.

Our results for the claim ages that maximize the EPV of household benefits are similar to those found by previous studies. Households, on average, maximize their household Social Security wealth when the husband claims at age 66 and the wife claims as soon as possible. Most of the husbands in our sample claimed much earlier than their maximizing claim age. This is seen in Fig. 1, which compares the pattern of actual claim ages of married men with the ages that maximize their household Social Security wealth.[7] 85.8% of married men should postpone claiming to age 65 and over in order to maximize the EPV of their household benefits. However, 86.4% of them claimed Social Security within one year of turning 62.

While most married men claimed several years earlier than their maximizing claim age, this generally results in a small loss of household Social Security wealth. On average, the maximum EPV of household benefits is $331,077.[8] At the actual claim ages, the average EPV reduces to $320,884. The average loss resulting from early claiming is just $10,193, 3.1% of the maximum. So, at least at the household level, they are not leaving enormous amounts of wealth on the table.

The generally small loss in household benefits, however, hides a substantial loss of widow's survivor benefits. Fig. 2 decomposes the total loss into the change in the EPV of benefits payable over the husband's lifetime, and the change in the EPV of benefits payable to the surviving widow. Claiming at the actual claim ages increases the EPV of benefits payable while the husband is alive from $251,654 to $255,545, a gain of $3891 (1.5%). But the EPV of widow's survivor benefits falls by 17.7%, from $79,422

4 This sample represents the worst group of widows. If the husband retires later and hence claims Social Security later, the loss of widow's survivor benefits will be smaller.

5 To be identified as married at age 62, the man has to be born in or after 1930, so they turned 62 on or after the first wave interview in 1992.

6 The last year for which earnings records are available is 2007, which limits our sample to individuals born before 1945.

7 As we include only those men who earned less than the RET threshold, men who delay claiming beyond the maximizing age are not doing so as a result of the earnings test.

8 In 2008 dollars.