

# Pension Reform and Return to Work Policies

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## Summary

Rules regarding post-retirement work (defined as work after beginning benefit collection) have the potential to greatly affect decisions about benefit collection and post-retirement labor supply. This is because when people make decisions about retirement they must consider how they will replace their wage income and continued work is one way to supplement retirement benefit income. In turn, these decisions will affect the health of pension systems, like public employee pensions and Social Security, by determining the number of years of benefit collection and, sometimes, the annual amount of benefits collected.

Existing research has shown that retirees are sensitive to the Social Security earnings test, which restricts the amount of earnings some beneficiaries can receive (e.g., Friedberg 1998, Friedberg 2000, Engelhardt and Kumar 2009, Gelber et al. 2013, Gelber et al. 2017). However, little is known about the effects of other types of return-to-work policies on post-retirement employment. Instead of restricting earnings, many public pension plans restrict the number of hours beneficiaries can work. In 2018, for example, 18 states placed restrictions solely on the time worked by retirees, another 11 restrict both hours and earnings, and just 10 set limits on earnings only. In Illinois (the setting of this study), the rules regarding limitations on hours for those returning to work after retirement have changed 4 times in the past twenty years. This is evidence that the rules are binding enough for policymakers to change them over time in order to affect changes in retiree labor supply. The most recent rule change increased the maximum number of hours allowed to 600 in 2018, which is evidence of how timely this issue is and how important it is that we understand these policies' effects.

In this study, I aim to provide some of the first evidence on how restrictions on the number of hours worked after retirement affect labor supply decisions. First, I document the post-retirement work patterns of public sector retirees. Using data covering employees in the Illinois school system (outside of Chicago) over a period of over 20 years, I describe the patterns of post-retirement work and how they have changed over time for this population. In doing so, I pay particular attention to how the patterns of post-retirement work vary by employee gender, race, age, occupation, and earnings level.

Several patterns emerge from this descriptive analysis. First, the annuitants with the highest levels of service at retirement are the most likely to return to work after retirement. These are probably the employees with the highest labor market attachment. Since incentives inherent in the pension system encourage employees to retire immediately upon eligibility (Stock and Wise 1990, Costrell and Podurksy 2009, Koedel and Podursky 2016, Ni and Podgursky 2016), these may be employees who retire early for financial reasons rather than based on their preferences for work. They are also the youngest annuitants and post-retirement employment decreases with age. Although there is little difference in post-retirement employment patterns by race or earnings, there are marked differences by gender and occupation (position last held). Instructional staff (teachers) are much less likely to return to work after retirement than administrative (principals, superintendents) and support (librarians, counselors) staff. At the same time, men are more likely to return to work after beginning benefit collection than are women. The differences in employment by gender are partly related to differences in the occupations across genders (men are much more likely to be in non-

instructional positions, where retirees are more likely to return to work than in instructional positions) and partly related to differences in labor supply within occupation (male instructional staff retirees are more likely to be employed than their female counterparts). Finally, there is clear variation over time in patterns of labor supply among annuitants. Post-retirement work rises sharply for annuitants after an early retirement incentive program in the 1990s; this is likely driven by the compositional shift in retirees towards those who had been less likely to want to retire than retirees in previous cohorts. Employment of annuitants begins to rise again in 2000, peaks just after the increase in the maximum number of allowable hours of work in 2001, and declines thereafter, but what drives the decline is unclear.

Second, I analyze how rules restricting the number of hours that beneficiaries can work affect retirement decisions and post-retirement employment. To accomplish this, I make use of two sources of variation: (i) changes to the rules regarding post-retirement work and (ii) the fact that these rules applied to some employees and not others. Although the rules regarding the maximum number of hours of post-retirement employment in Illinois Public Schools (IPS) have changed multiple times, because of data limitations, I use the variation driven by the policy change in 2001.<sup>1</sup>

To identify how rules restricting the number of hours employees can work post-retirement affect retirement decisions, I use difference-in-difference techniques. This methodology makes use of the fact that, although most employees are restricted in the

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<sup>1</sup> I focus on the change in 2001 because it was the only policy change for which I have enough pre- and post-treatment data to identify the effect.

number of hours they can work in IPS schools after collecting their retirement benefit, employees in certified subject shortage areas in a given district are not. As such, the retirement decisions of those in certified subject shortage areas in a district should not be affected by rules limiting the number of hours that can be worked post-retirement. Therefore, I compare the retirement decisions of employees likely to be affected by the rules (those not in certified subject shortage areas within a district) to those unlikely to be affected by the rules (those in certified subject shortage areas within a district) before and after the state alters the hours restrictions. Doing so will allow me to identify the effects of the hours restrictions under the assumption that there was nothing else that changed concurrently to the rules changes that also differed across these groups. As described in more detail later, I also make use of the fact that it is only the labor supply of those closest to retirement eligibility that should be affected. This further allows me to control for potential confounding factors differentially affecting the labor supply of those nearing retirement eligibility.

I find that the increase in the maximum number of allowable hours of post-retirement work had little effect on retirement annuitant benefit collection. However, it increased the probability of working part-time for retirees, as would be expected given the incentives. As such, these policies appear to be binding on the labor supply decisions of some employees. These results are relevant for designing policies aimed at extending work-lives or improving the health of pension systems.

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