MICHIGAN RETIREMENT AND DISABILITY RESEARCH CENTER
UNIVERSITY OF MICHIGAN

Promoting research on retirement, disability, and Social Security policy

Public Pension Design and Household Retirement Decisions: A Comparison of the United States and Germany

*David Knapp, Jinkook Lee, Maciej Lis, and Drystan Phillips**

Social insurance-based public pensions, such as the social security systems in the United States and Germany, were developed to insure financial security for individuals in old age, dependents after death, or disabled individuals. While these plans may be designed to be actuarially fair, differences in generational and gender mortality often mean these public pensions provide financial incentives to continue or stop working. We compare the U.S. and Germany in this paper given the many similarities between the two systems, including basing benefit levels on earnings histories, having survivor benefits, providing incentives to delay the start of benefits, and similar eligibility ages for earliest and full benefits. We use data from the U.S.' Health and Retirement Study (HRS) and the Survey of Health, Ageing and Retirement in Europe (SHARE), the HRS' harmonized sister study, to examine how retirement claiming decisions of married households in the U.S. and Germany are influenced by the existence and structure of auxiliary benefits.

Previous studies have demonstrated that people respond to pension incentives. We affirm these findings and analyze whether individuals also respond to the additional incentives implicitly built into auxiliary benefits, specifically the U.S. Social Security's spousal and survivor benefits. We examine whether our findings are consistent with these benefits being salient for retirement and benefit-claiming decisions.

We find that incentives to alter benefit claiming timing built into U.S. spousal and survivor benefits are unrelated to labor supply decisions. This finding is consistent with recent survey evidence from an online representative panel of American households that suggests that knowledge of eligibility rules for these benefits is low (Carman

* **David Knapp** is an associate economist at the RAND Corporation. **Jinkook Lee** is research professor of economics, as well as a senior economist and program director of the University of Southern California's Center for Economic and Social Research. **Maciej Lis** is an economist for the Organisation for Economic Co-operation and Development. **Drystan Phillips** is a senior programmer for USC's Program on Global Aging, Health and Policy. This research brief is based on working paper WP2021-417, UM19-13.

and Hung 2018). A U.S. worker's benefit payment depends on a complex interaction of own claiming decisions and his or her spouse's claiming decisions. The lack of responsiveness may reflect the complexity of benefit rules or that benefits paid to a worker's spouse are not salient in the worker's decision-making.

To provide a benchmark, we examine Germany where survivor benefits create similar incentives for retirement timing. German survivor benefits are largely independent of the survivor's decision, making the benefit calculation and resulting incentives easier to understand. Given the small sample size, the German analysis is inconclusive. However, the findings are consistent with survivor benefits influencing married, working men's labor supply decisions.

Our findings have implications for Social Security policy. A lack of policy salience may be desirable in old-age insurance if the incentives encourage early labor market exit. The design of U.S. spousal benefits is an example. A spouse cannot collect her spousal benefits until the worker claims his benefit. This design theoretically promotes early claiming for households eligible for this benefit. Early claiming encourages these households to take lower lifetime monthly benefits, placing them at greater risk of financial insecurity in retirement, particularly in widowhood. Alternatively, the design of survivor benefits rewards delayed benefit claiming through increases in the monthly benefit. We find that married workers do not respond to the incentives associated with spousal and survivor benefits even if doing so would enhance their retirement security. Additional education and outreach may increase couples' understanding of how individual claiming decisions influence each person's benefits while alive and in widowhood.

Our findings also have implications for analyses of retirement benefits' potential impact on households' retirement decisions. Recent studies evaluating the potential impact of reducing or eliminating spousal or survivor benefits using structural models of household decision-making assume that potential income sources are treated equally. In the context of own, spousal, and survivor retirement benefits, our findings suggest that this is not true. If spousal and survivor benefits are not salient, then the predictions by many such structural models are unlikely to be valid. Our findings suggest caution when interpreting model predictions of labor supply responses from potential changes to own and auxiliary benefit policy. ❖

Michigan Retirement and Disability Research Center
Institute for Social Research
426 Thompson Street, Room 3026
Ann Arbor, MI 48104-2321
Phone: (734) 615-0422 **Fax:** (734) 615-2180
mrdrcumich@umich.edu www.mrdrc.isr.umich.edu

Sponsor information: The research reported herein was performed pursuant to grant RDR18000002 from the U.S. Social Security Administration (SSA) through the Michigan Retirement and Disability Research Center (MRDRC). The findings and conclusions expressed are solely those of the author(s) and do not represent the views of SSA, any agency of the federal government, or the MRDRC.