Discussion of “Is Uncle Same Inducing the Elderly to Retire?” (by Auerbach, Kotlikoff, Koehler, and Yu)

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1 The Wharton School and NBER

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Summary

Nice paper:

- Many retirees greatly depend on SS (biggest asset to half +)
- High MTR’s for old-age work, especially if benefit recomputation associated with earnings tax not understood
- Big contribution: detailed calculations due to considerable benefit program inter-linkages
- Unclear if paper answers its title, but high MTR’s certainly play a role based on past work

What are the complementary questions for policy applications?

Related future work?
Question #1: Why do so many depend on SS?

Is SS’s role self-fulfilling (rational people)?

- Big literature on how much SSNW reduces private saving (CBO rule is 50%)
- Large related literature on Ricardian equivalence (e.g., Altonji, Hayashi, Kotlikoff [various years])
- Buchanan’s “Samaritan’s Dilemma” (coordination problem?)

Or, is it beta-delta / other behavioral preferences?

- Even here, best policy response depends on specific view (Bernheim, 2015)
Question #1: Why do so many depend on SS? (Cont.)

Why does it matter (in theory)?

- With rational people and progressive PIA, large MTR’s faced by hand-to-mouth could be consistent with ICC’s, if more direct mechanism not available.
  - In contrast, risk reclassification risk likely not be relevant w/o good real private annuities and since SS’s return is tied to population average, not individual longevity.
  - Open issue: current screening models pretty simple with limited intertemporal dynamics.
    - Own guess is that not a big deal (Vickrey tax, not Mirrlees)
  - Even with beta-delta, high MTR’s could be consistent with sophisticated view (Laibson) if additional private saving is efficient and no better direct mechanism exist, but probably not naive version (Rabin)
    - My own guess: high redistribution is efficient with low MTR’s.
Question #2: What is Optimal Consumption Target?

Probably not smooth:
- New retirees (“Needs, Wants, Wishes” paradigm): Needs = 85% preretirement non-mortgage expenses
- Middle-age retirees: OOP medical expenses ($250K EBRI; Fidelity Benefits)
- Older-age retirees: State-dependent utility + skilled nursing

Nonetheless:
- “Old old” age support? (Feldstein)
- Due to absence of private real annuities, an increasing real value of SS replaces second-best precautionary saving in face of longevity uncertainty, with first-best pooling.
- Could be efficient ... unless enhances borrowing constraints early in retirement
- If efficient, likely want to reduce MTR’s until quite old (when it doesn’t really matter)
Question #3: What is “True”? “Perceived”?

“True” (mostly) matters for maintain standard of living:
▶ even if agents rational / informed but unlucky (idiosyncratic shocks)
▶ Positive resource cost to “fix,” if that means increasing benefits

“Perceived” (mostly) matters for labor supply / savings:
▶ Before retirement: not understanding tax-benefit linkage
  ▶ If understood, not distorting for average household when \( r = g \)
▶ After retirement: earnings test is the big one
  ▶ If understood and no borrowing constraints, not distorting either
  ▶ But even financial advisors don’t understand it
▶ Resource cost to fix could be zero or even negative (dynamic score)
Next Steps

Simulate perceived issues, even with geometric discounting (higher hurdle):

- with elastic labor supply, general equilibrium
- with second-best distorting general taxes (e.g., annuities might be inefficient relative to precautionary savings)

If lower MTR’s emerge as efficient (likely), some free lunches available:

- Earnings tax comes from era of belief in “zero sum” economics
  - I.e., old get SS in exchange for freeing up jobs for young
  - Policy: could just eliminate

- Tax-benefit linkage perception issues historically political
  - Trying to hide redistribution (Cohen vs. Friedman)
  - Policy: Could communicate marginal impact easier