Social Security Administration: Health Care Costs, Taxes, and the Retirement Decision

This research simulates how much longer the typical worker aged 65 in the year 2030 would have to work to have the same financial resources in a high tax burden and health cost scenario as in a low tax and health cost scenario.

Lead Agency:
Social Security Administration

Agency Mission:

To advance the economic security of the Nation's people through compassionate and vigilant leadership in shaping and managing America's Social Security programs.

Principal Investigators:

Richard Johnson, Senior Research Associate
Urban Institute, Washington,
2100 M Street, N.W.
Washington, D.C. 20037

General Description:
This research estimates the effects of rising taxes and health care costs on the timing of retirement. Higher tax burdens or health costs may delay retirement, as older people have to work longer to save enough money for retirement. On the other hand, if people anticipate these higher costs, they may work and save more while younger and retire when planned. To answer this question, the researchers consider two possible scenarios—one with high taxes and health costs, and one with low taxes and health costs. The low-cost scenario assumes that the tax burden in 2030 is roughly the same as in 2000 by adjusting exemption amounts and the standard deduction by the change in the average wage index. It also assumes health care costs increase at the same rate as inflation. In the high-cost scenario, there is no change in thresholds used for the alternative minimum tax or for taxing Social Security benefits, so more people would be subject to these taxes, and health costs increase by 3.2 percent each year between 2000 and 2030. Using representative cases for low, moderate, and high earners and single and married individuals, they simulate how much longer the typical worker would have to work to have the same financial resources at age 65 in the high-cost scenario as in the low-cost scenario. In most cases, workers will have to delay retirement by 2.4 to 2.8 years in the high-cost scenario to receive as much annual retirement income as in the low-cost scenario. The only group that would not be affected is low-income single adults, because they would not pay Federal income taxes in either case, and most of their health costs are paid for by Medicaid.

Private individuals face large and growing health care costs. Despite near-universal Medicare coverage, these costs can be particularly burdensome for older Americans, who face out-of-pocket expenses for Medicare premiums, private supplemental premiums, and direct payments to health care providers for deductibles and copayments. Additionally, increasing public costs are likely to boost future tax burdens. Some of this increase will probably fall on older Americans, subjecting them to a double burden. This study is important, because it considers how rising tax burdens and out-of-pocket health care costs will affect the timing of retirement. How well people anticipate future increases in taxes and health care costs, and how they react at younger ages, will crucially affect retirement income. If households are farseeing rational planners, higher health costs and tax burdens will likely induce more saving and harder work while young, muting effects on retirement decisions.

Excellence:	What makes this project exceptional?
Significance:	How is this research relevant to older persons, populations and/or an aging society?
Effectiveness:	What is the impact and/or application of this research to older persons?
Innovativeness:	Why is this research exciting or newsworthy?

Private individuals face large and growing health care costs. Despite near-universal Medicare coverage, these costs can be particularly burdensome for older Americans, who face out-of-pocket expenses for Medicare premiums, private supplemental premiums, and direct payments to health care providers for deductibles and copayments. Additionally, increasing public costs are likely to boost future tax burdens. Some of this increase will probably fall on older Americans, subjecting them to a double burden. This study is important, because it considers how rising tax burdens and out-of-pocket health care costs will affect the timing of retirement. How well people anticipate future increases in taxes and health care costs, and how they react at younger ages, will crucially affect retirement income. If households are farseeing rational planners, higher health costs and tax burdens will likely induce more saving and harder work while young, muting effects on retirement decisions.