

ICI Webinar

When I'm 64 (or Thereabouts): Changes in Income from Middle Age to Old Age

March 21, 2024

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Introduction

Sarah Holden

Investment Company Institute

Official Statistics Show Less than Half of Elderly Have Non-Social-Security Retirement Income

Percentage of individuals aged 65 or older with own or spouse income from DB plans, DC plans, annuities, or IRAs, 1975–2013



Source: ICI tabulations of Current Population Survey (CPS) Annual Social and Economic Supplement

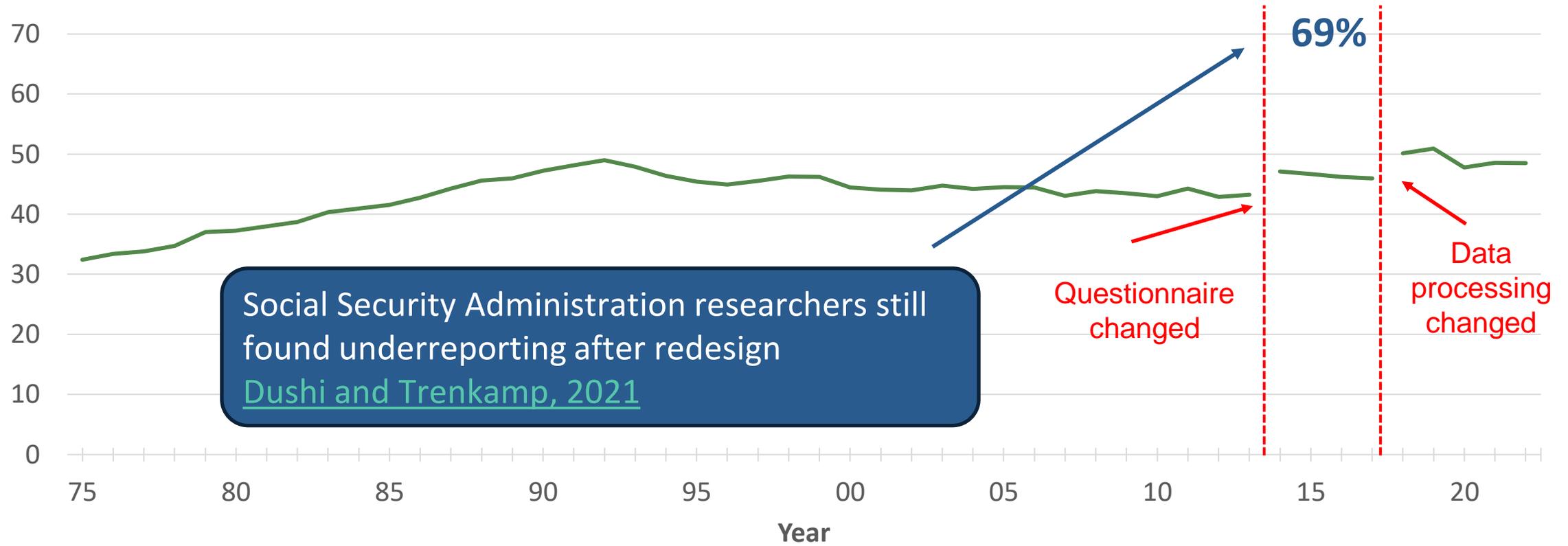
Comparison with Tax Data Shows Retirement Income Underreported in the CPS*

- Census Bureau research ([Bee and Mitchell, 2017](#))
 - Matched CPS survey responses with tax data
 - For individuals 65 or older in 2012, found that the CPS
 - Understated the incidence of retirement income by 25 percentage points
 - Missed more than half of retirement income (pensions, annuities, and IRAs)
 - Understated median income by 23 percent
 - Overstated poverty rate by 32 percent
 - It also found that mismeasurement had gotten worse since 1990

*Current Population Survey

Survey Redesign Did Not “Fix” the CPS

Percentage of individuals aged 65 or older with own or spouse income from DB plans, DC plans, annuities, or IRAs, 1975–2022



Source: ICI tabulations of Current Population Survey (CPS) Annual Social and Economic Supplement



Presentation

Peter Brady

Investment Company Institute

March 21, 2024

When I'm 64 (or Thereabouts): Changes in Income from Middle Age to Old Age

Peter Brady and Steven Bass

This research was conducted as part of the IRS Statistics of Income (SOI) Joint Research Program. Views presented are those of the authors and do not necessarily represent the views of the Internal Revenue Service or the views of the Investment Company Institute or its members. We thank Kevin Pierce for his assistance with this project.

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Goal of Research: Measure Income Changes Near Retirement

- Two questions
 - How does spendable income change from middle age through old age?
 - How does income composition change from middle age through old age?

Motivation for Research: Proposals to Overhaul the US Retirement System

- Components of US retirement system
 - Social Security
 - Employer plans and IRAs
- Proposals typically based on concerns about the current system
 - Adequacy (low “replacement rates”)
 - Overreliance on Social Security
- Provide a baseline assessment of the retirement system to inform the policy debate

Why the Perception that Retirement System is “Broken”?

- “Evidence” on retiree income from household surveys
 - Retirees too reliant on Social Security
 - Few retirees get income from employer plans and IRAs
- “Evidence” on transition into retirement
 - Some early research examining a drop in spending after retirement
 - Research projecting retirement resources will be inadequate

Bloomberg Headlines from Spring 2022

America's Retirement Crisis Is a Financial Crisis Too

"Therein lies the origin of America's retirement crisis. *The U.S. has never properly considered* how people will make up the difference between Social Security and a financially secure old age."

Piecemeal Reform Won't Solve the U.S. Retirement Crisis

"Tweaks, patches and accidents created this mess in the first place. Fixing it *will take more than tinkering around the edges.*"

Saving for Retirement Is Harder Than It Needs to Be

"The U.S. government has long offered myriad contrivances and enticements to get Americans to save enough for a comfortable retirement — *so far with woefully inadequate results.*"

How to Fix the Broken U.S. Retirement-Savings System

"*It's hard to imagine a social program more dysfunctional* than America's morass of retirement-saving accounts."

Unique Data and an Innovative Method Used to Assess the US Retirement System

- Use administrative tax data
 - Accurate measure of retiree income
 - Large representative sample
- Use 18-year panel to track changes in income
 - Follow one birth-year cohort from age 55 to age 72
 - Before age 62 – Social Security early claiming age
 - After age 70 – end of Social Security delayed retirement credits
 - After age 70½ – required minimum distributions (RMDs) from retirement account

Our Findings Are at Odds with the Perception of a Failed System

- Spendable income
 - Typical individual replaces more than 90% of their late 50s spendable income
 - Those with lowest age 55-59 income have the highest replacement rates
- Income composition
 - Most rely on a combination of Social Security and income from retirement plans
 - 75% receive (non-Social-Security) retirement income directly or through a spouse
 - How much income you have in your 50s determines your income composition in your 70s

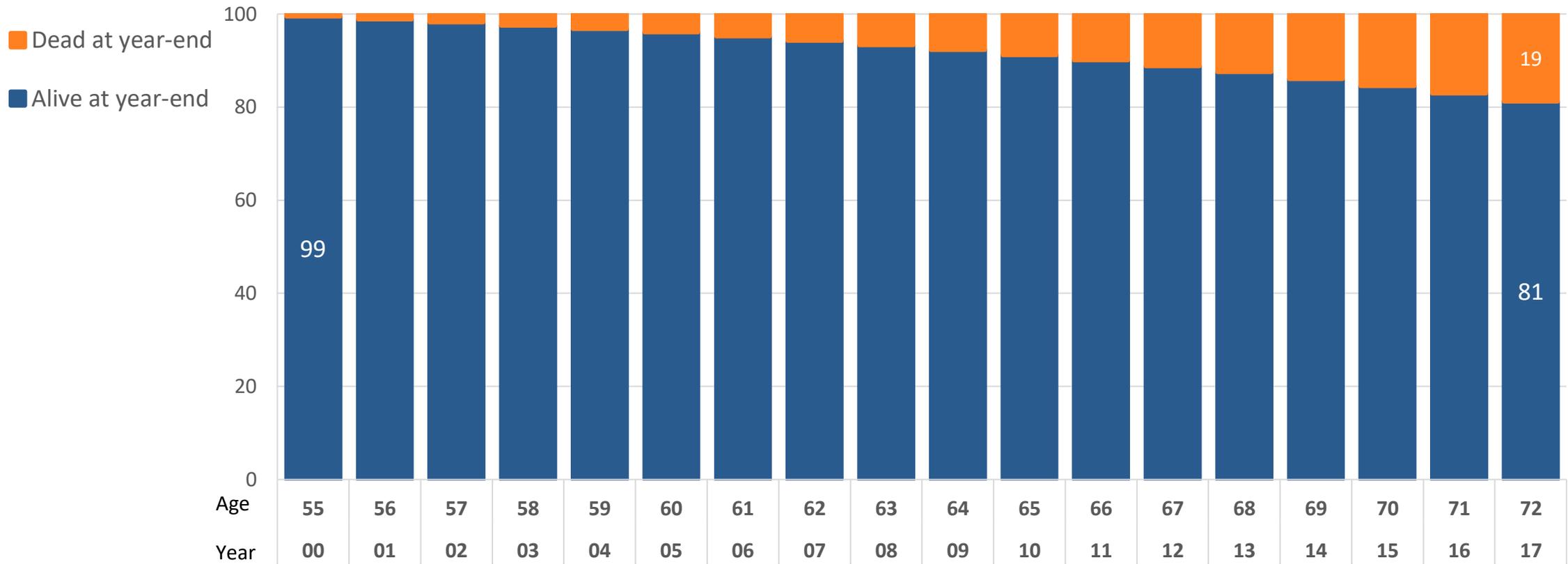
Plan for the Rest of the Talk

- Data and income measure
- Spendable income
- Composition of income

Data and Income Measure

Panel Consists of Individuals Born in 1945 Who Survive to Age 72

Share of population born in 1945 and alive on January 1, 2000 (percentage)



Components of Total Income

Labor+SS+Retire

- Labor
 - Wages, salary, tips, etc.
 - Self-employment
 - Unemployment compensation
- Social Security
- Retirement
 - IRA distributions
 - Pensions and annuities

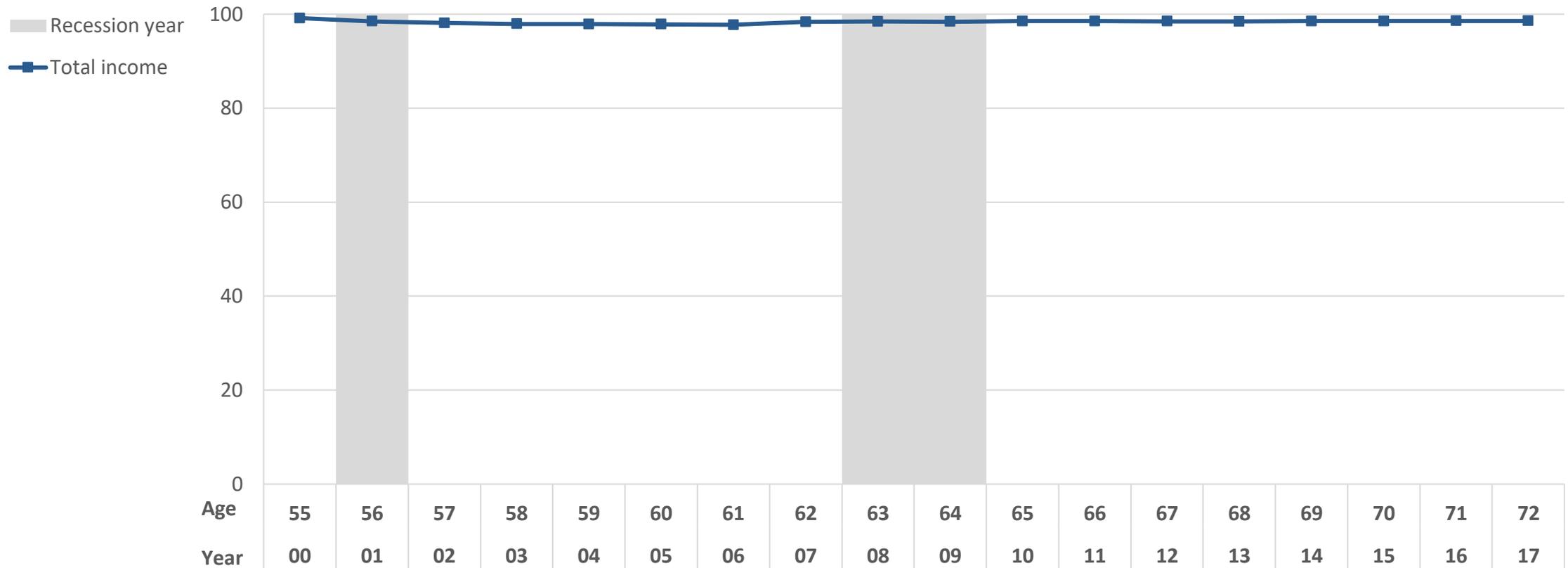
Other Income

- Taxable interest
- Dividends & tax-exempt interest
- Gains/losses
- Business/farm/rents, royalties, etc.
- Net alimony & other

Changes in Spendable Income

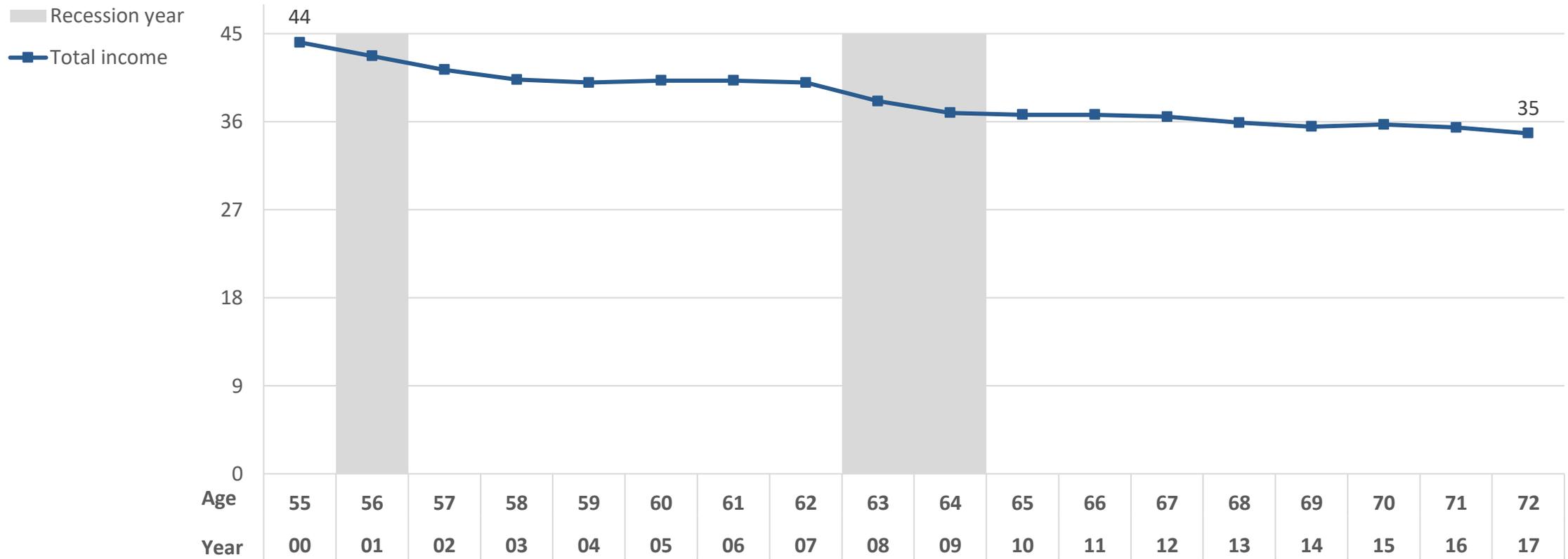
Most Have Income at All Ages

Share of the panel with own or spouse non-zero total income (percentage)



Median Total Income Declines by Nearly \$10,000

Median per capita inflation-indexed total income among those with total income, constant 2017 dollars (thousands)

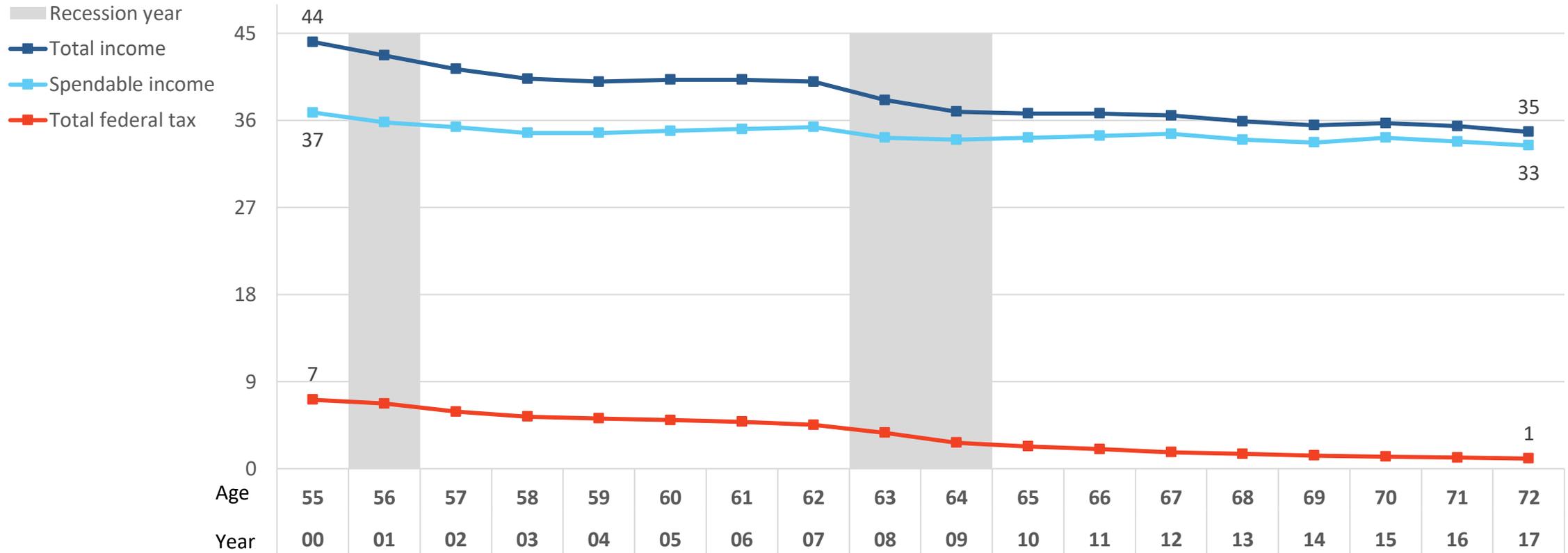


Spendable Income Is a Better Measure of Well-Being

- Spendable income is akin to “take-home pay”
 - Income available to spend after savings and taxes
- Total income measure already excludes retirement contributions
- Spendable income = total income – payroll taxes – federal income taxes

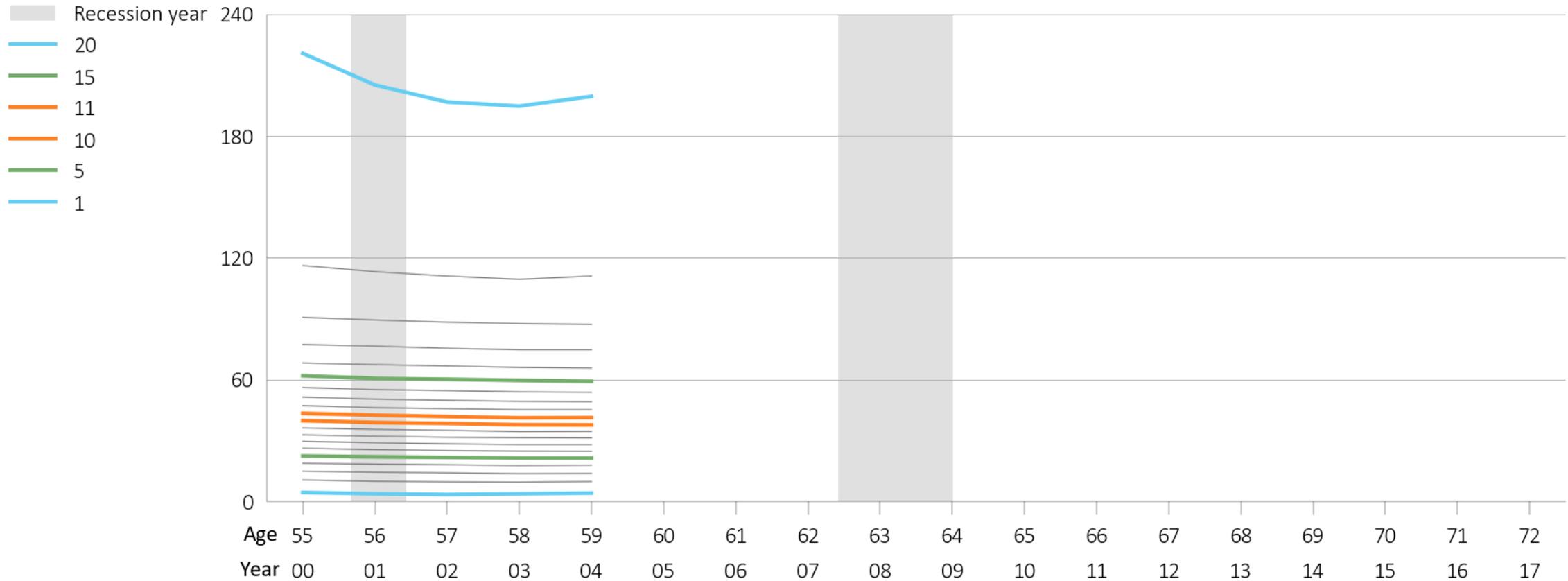
Median Spendable Income Declines by Less than \$4,000

Median per capita inflation-indexed income among those with total income, constant 2017 dollars (thousands)



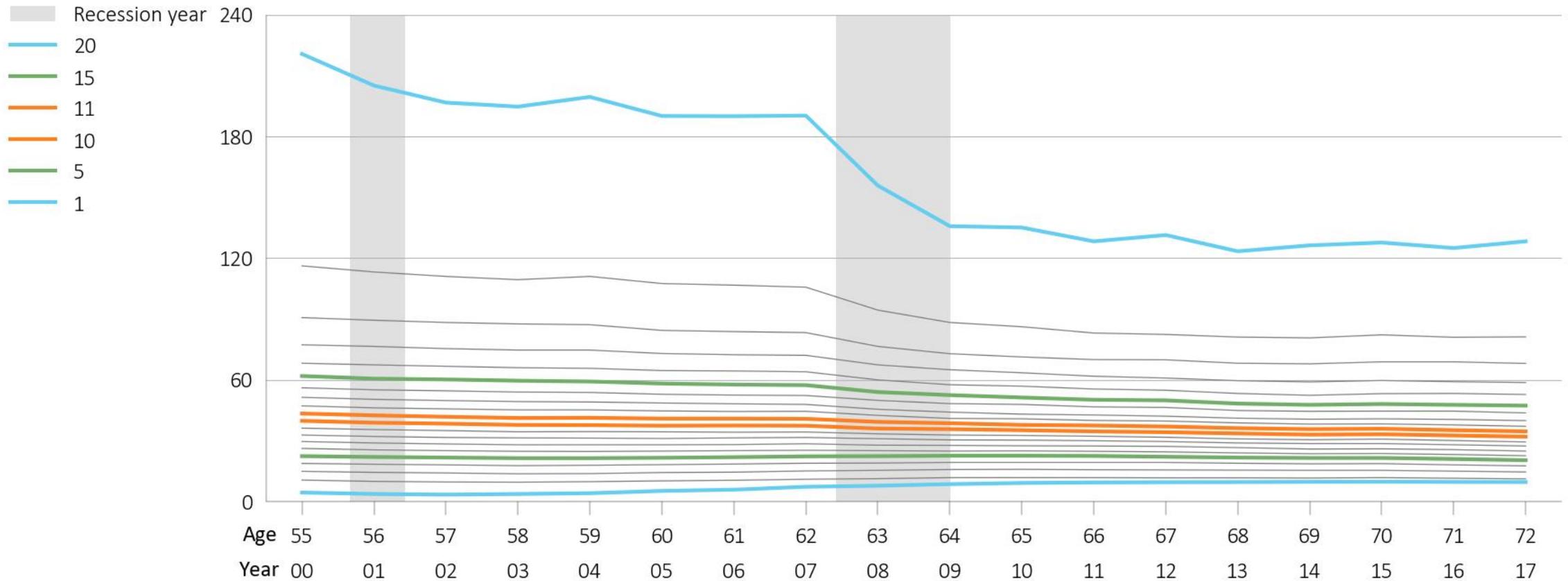
We Rank Individuals by Average Age 55–59 Total Income

Median per capita inflation-indexed total income by ventile of age 55–59 income, constant 2017 dollars (thousands)



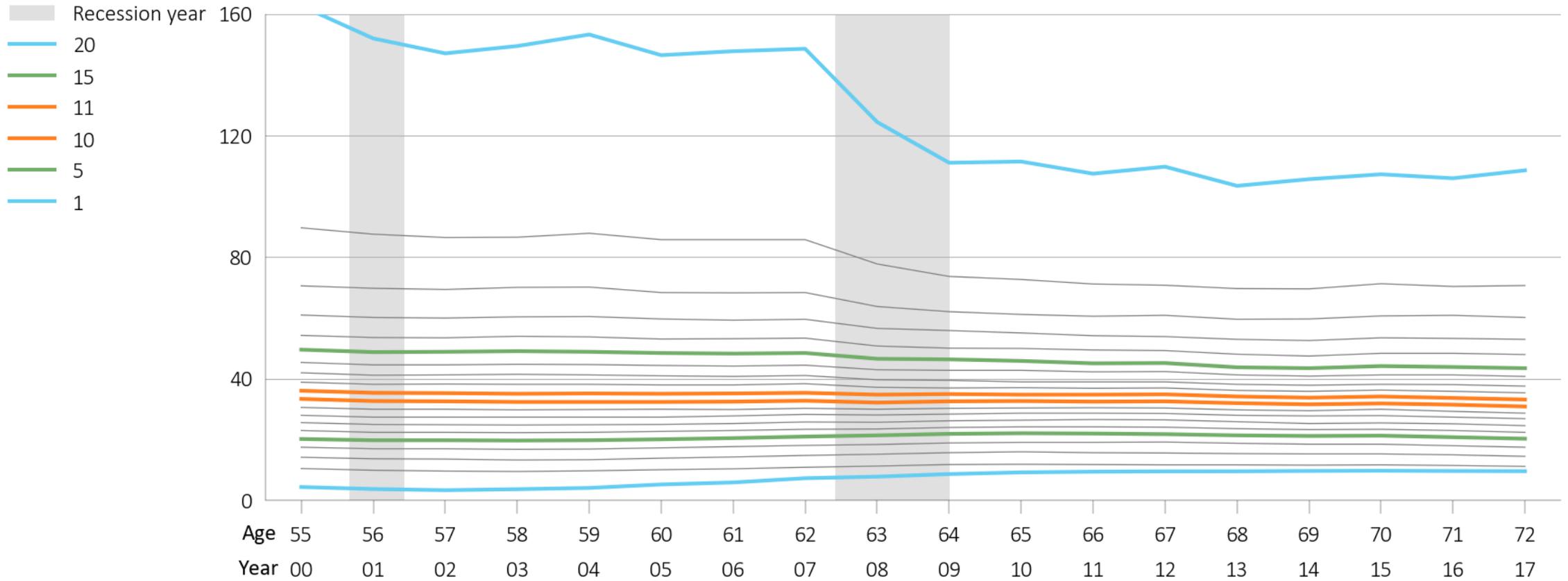
Total Income Falls the Most For Highest Income Ventiles

Median per capita inflation-indexed total income by ventile of age 55–59 income, constant 2017 dollars (thousands)



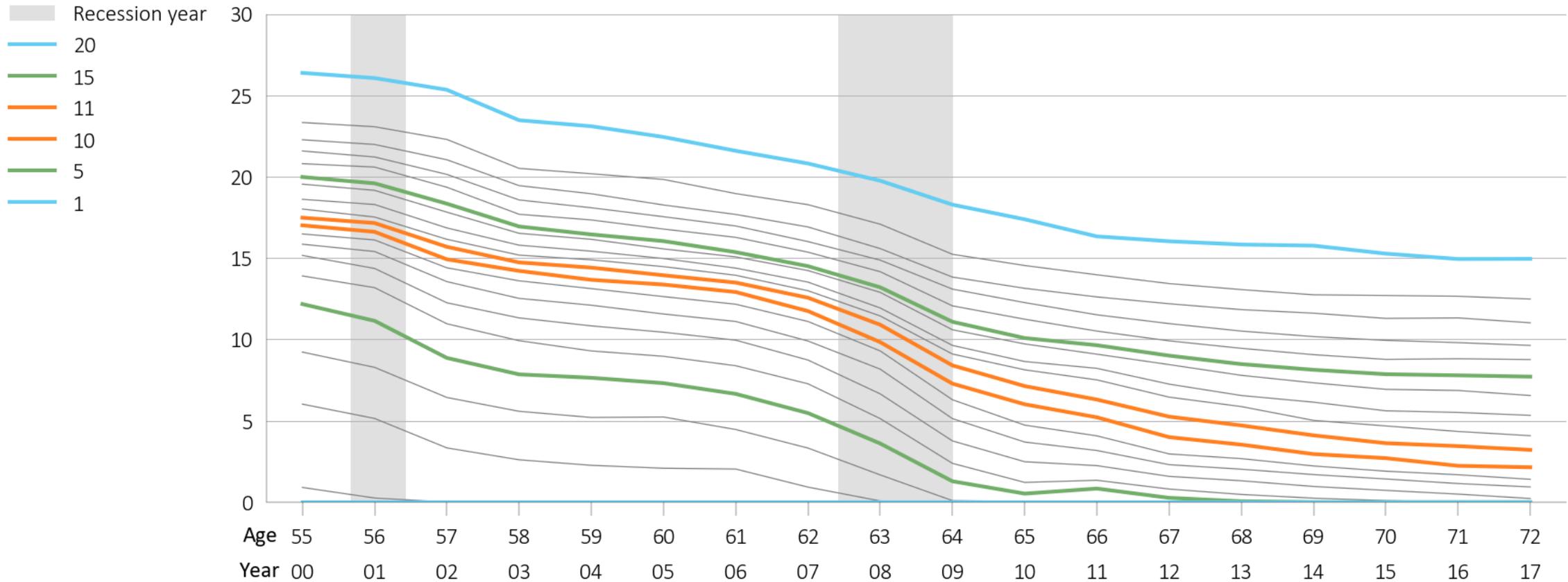
Spendable Income Flatter, but Still Declines the Most at the Top

Median per capita inflation-indexed spendable income by ventile of age 55–59 income, constant 2017 dollars (thousands)



Middle Income Have Largest Declines in Tax Rates

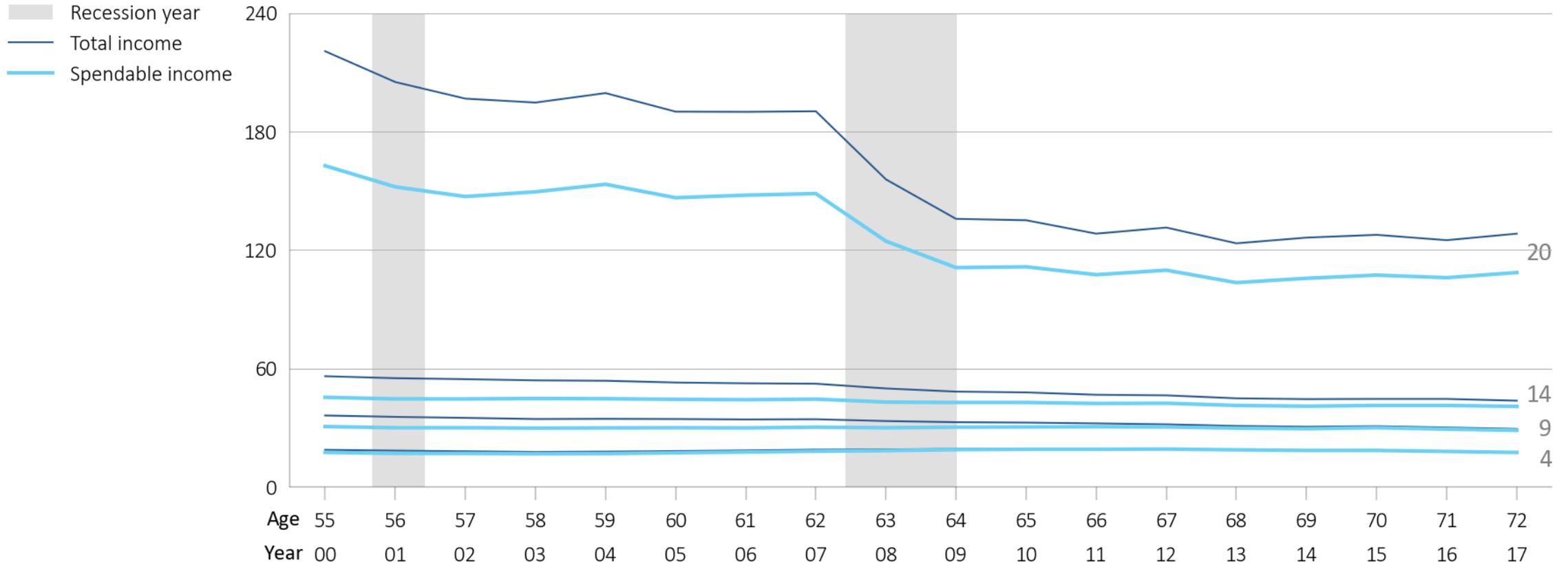
Median effective total federal tax rates (total federal taxes divided by total income) by ventile of age 55–59 income (percentage)



Illustrations:

Impact of Taxes Varies with Age 55–59 Income

Median per capita inflation-indexed total and spendable income, selected ventiles of age 55–59 income, constant 2017 dollars (thousands)



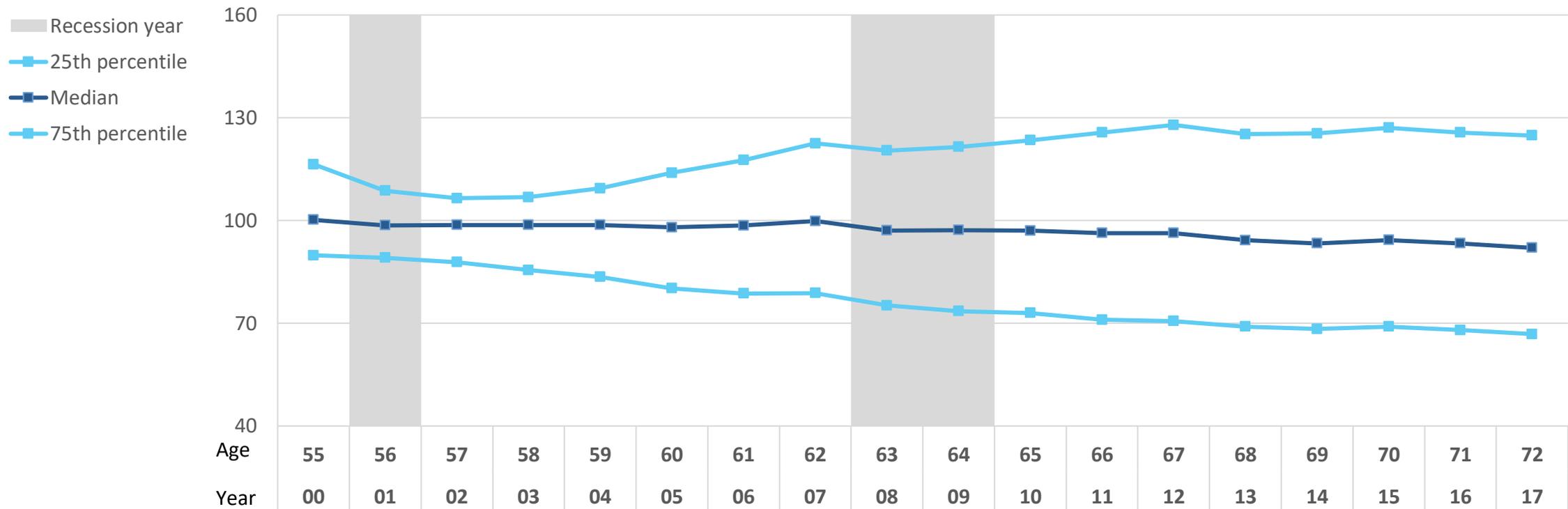
Calculate Replacement Rates of Spendable Income

- Calculate for each individual
- Replacement Rate =

$$\frac{\text{Spendable income at age } t \text{ (from 55 through 72)}}{\text{Average spendable income from age 55 through age 59}}$$

Typical Replacement Rate More Than 90 Percent

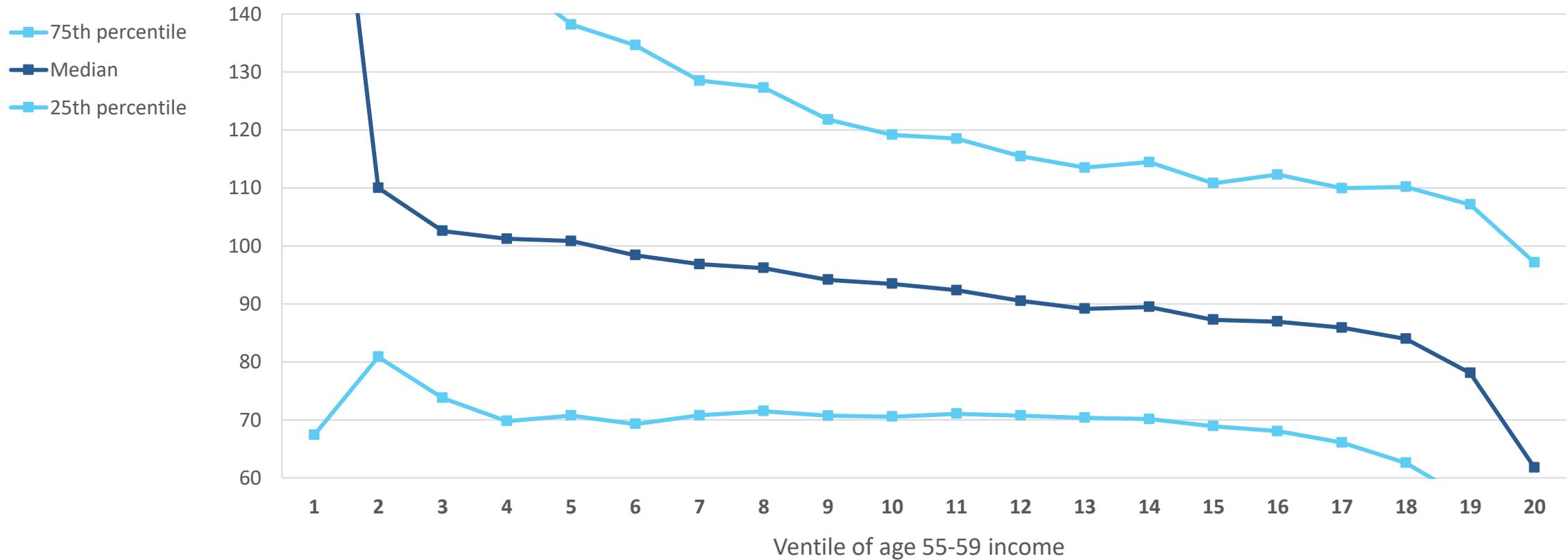
Spendable income replacement rates* (percentage)



*Per capita inflation-indexed spendable income divided by per capita inflation-indexed spendable income averaged from age 55 to age 59

Distribution of Replacement Rates at Age 72

Median spendable income replacement rates* at age 72 (percentage)



*Per capita inflation-indexed spendable income divided by per capita inflation-indexed spendable income averaged from age 55 to age 59

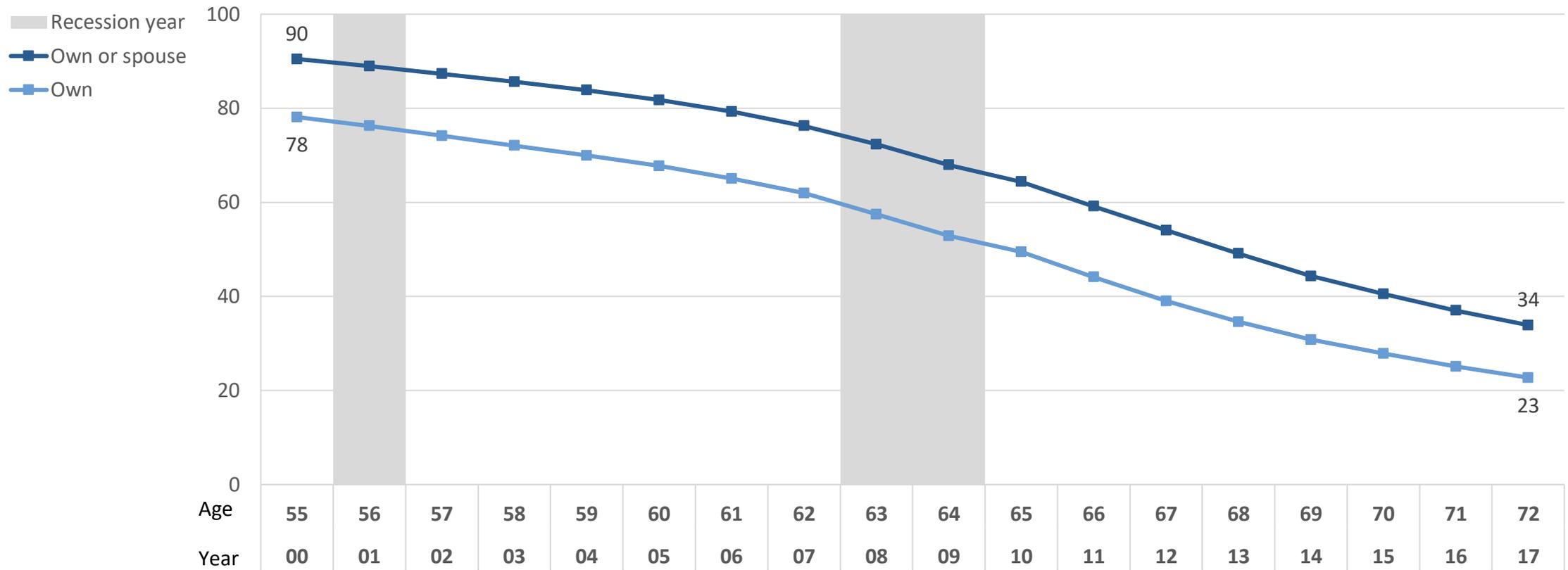
Summary: Changes in Spendable Income

- Spendable income falls by less than total income from age 55 to age 72
- Typical individual replaces more than 90 percent of their late 50s spendable income
- Those with lowest age 55-59 income have the highest replacement rates

Composition of Income

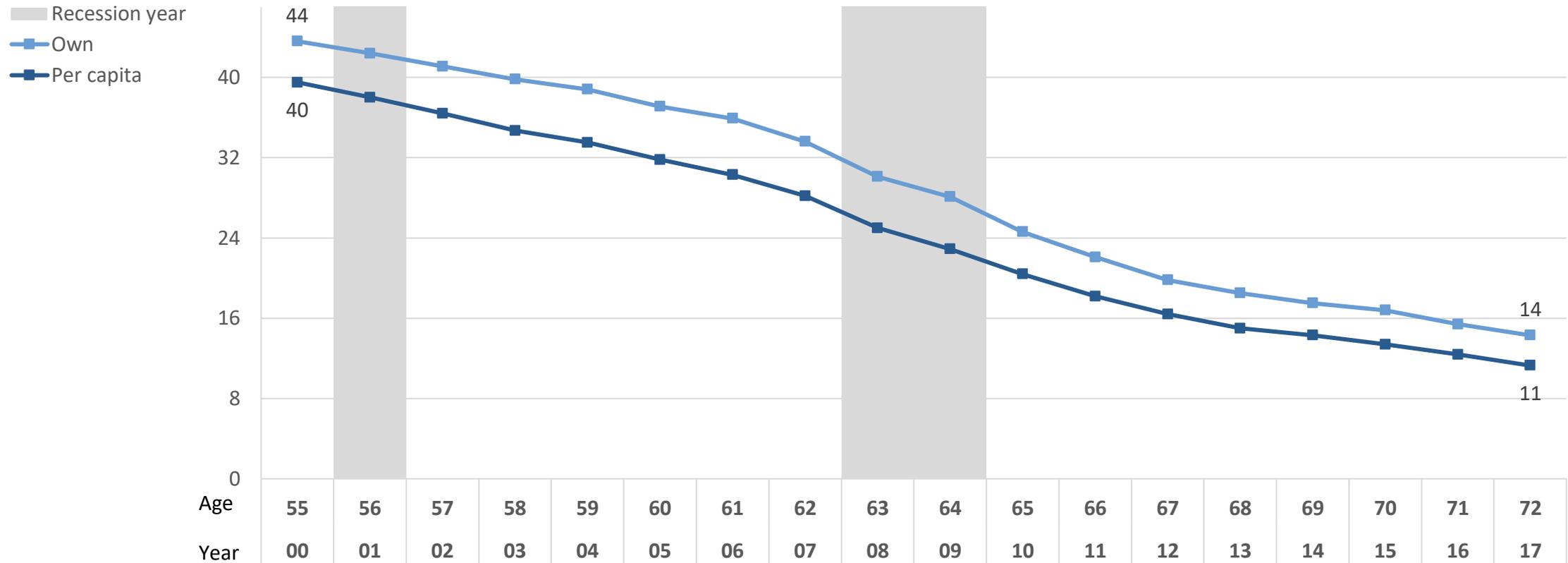
The Share Working Declines Slowly with Age ...

Share of the panel with labor income (percentage)



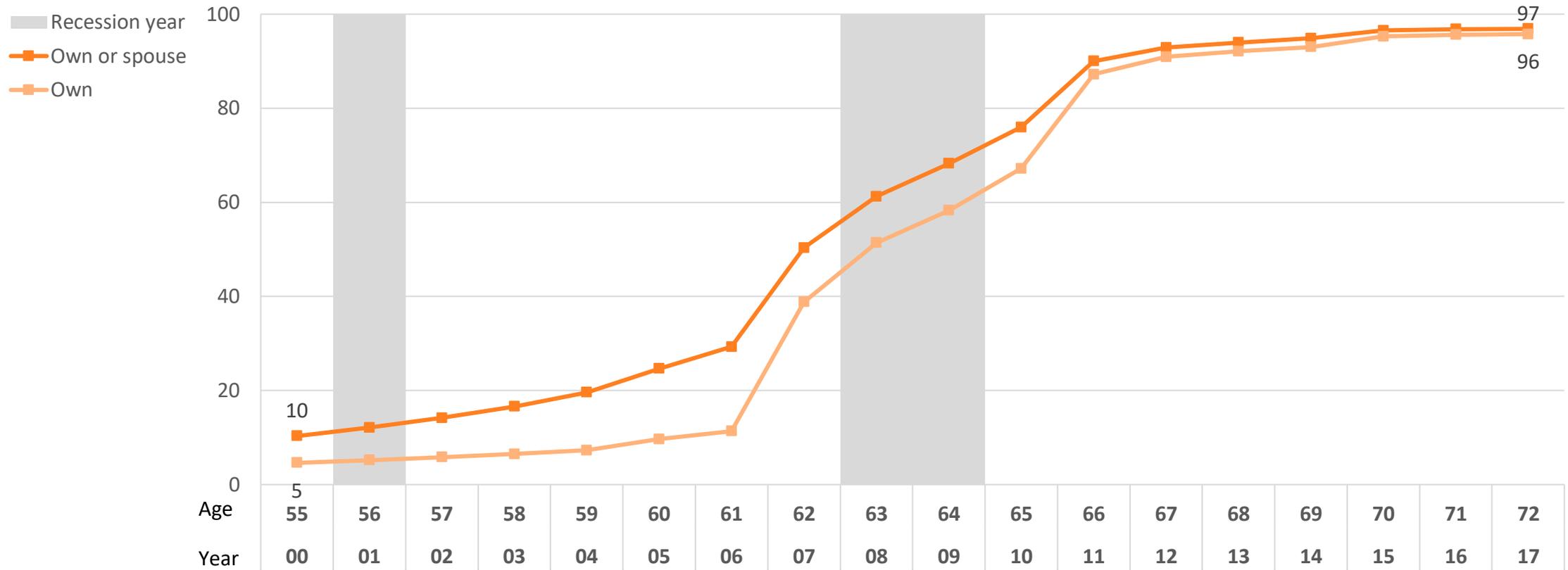
... And Those Who Continue Working Typically Earn Less

Median inflation-indexed labor income among those with labor income, constant 2017 dollars (thousands)



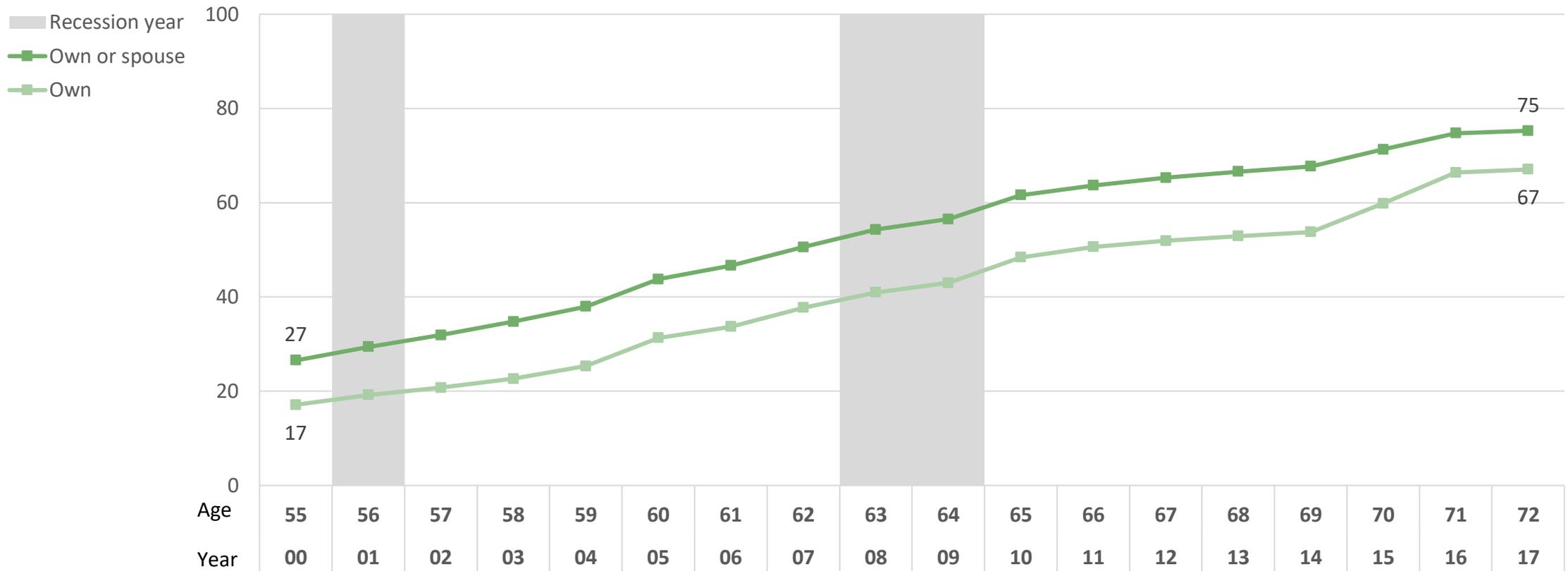
Claiming of Social Security Increases Rapidly After Age 61

Share of the panel with Social Security income (percentage)



By Age 72, Three-Quarters Have Income from Employer Plans and IRAs

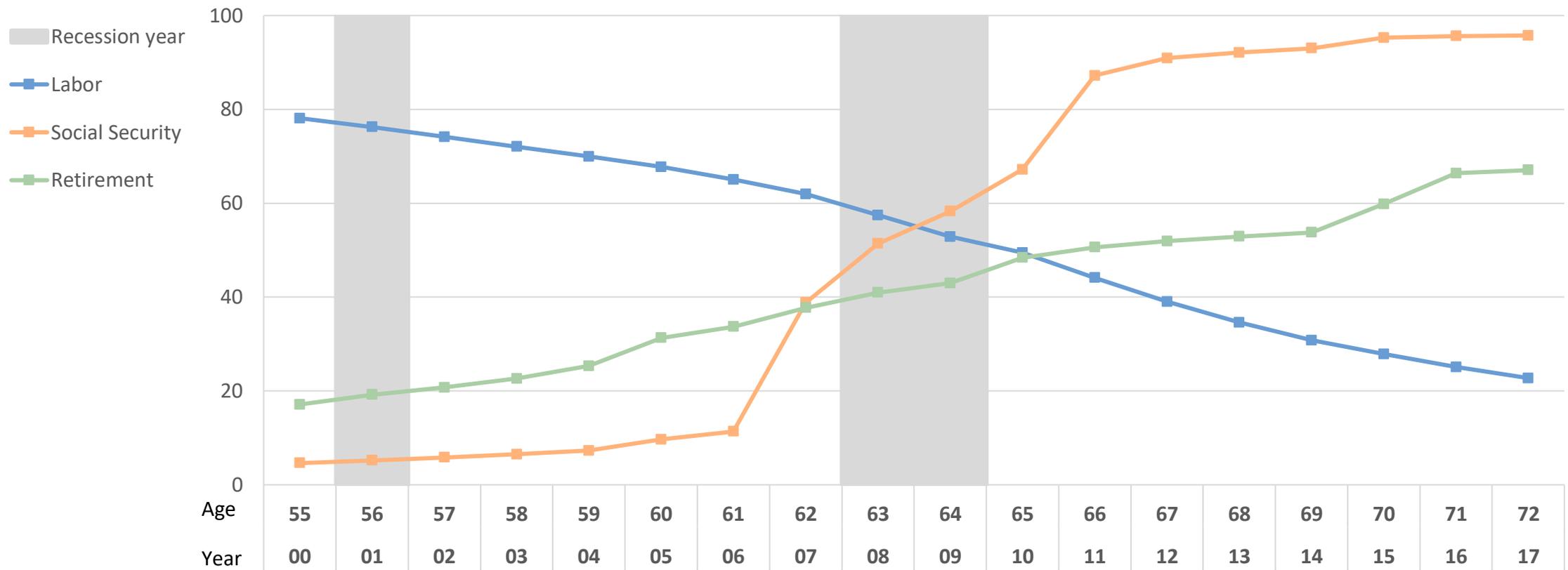
Share of the panel with retirement income* (percentage)



*Income from pensions, annuities, and IRAs

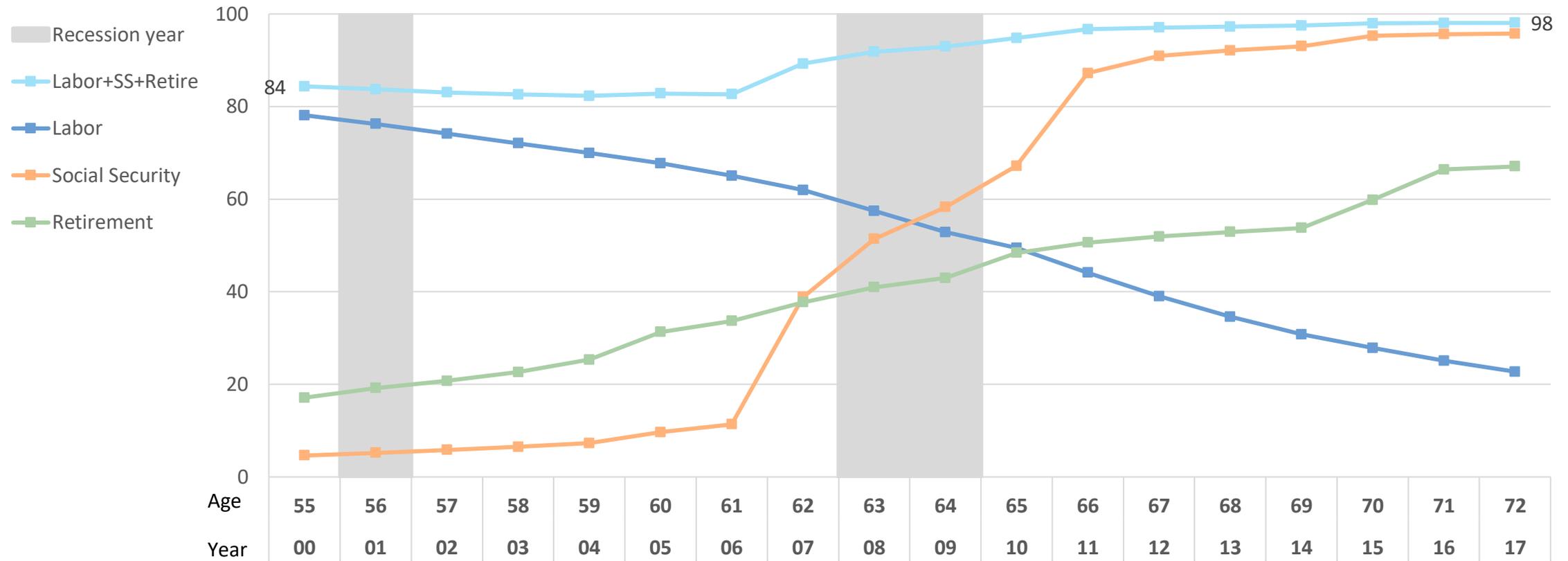
It Is Hard to Pinpoint When Retirement Occurs

Share of the panel with own income (percentage)



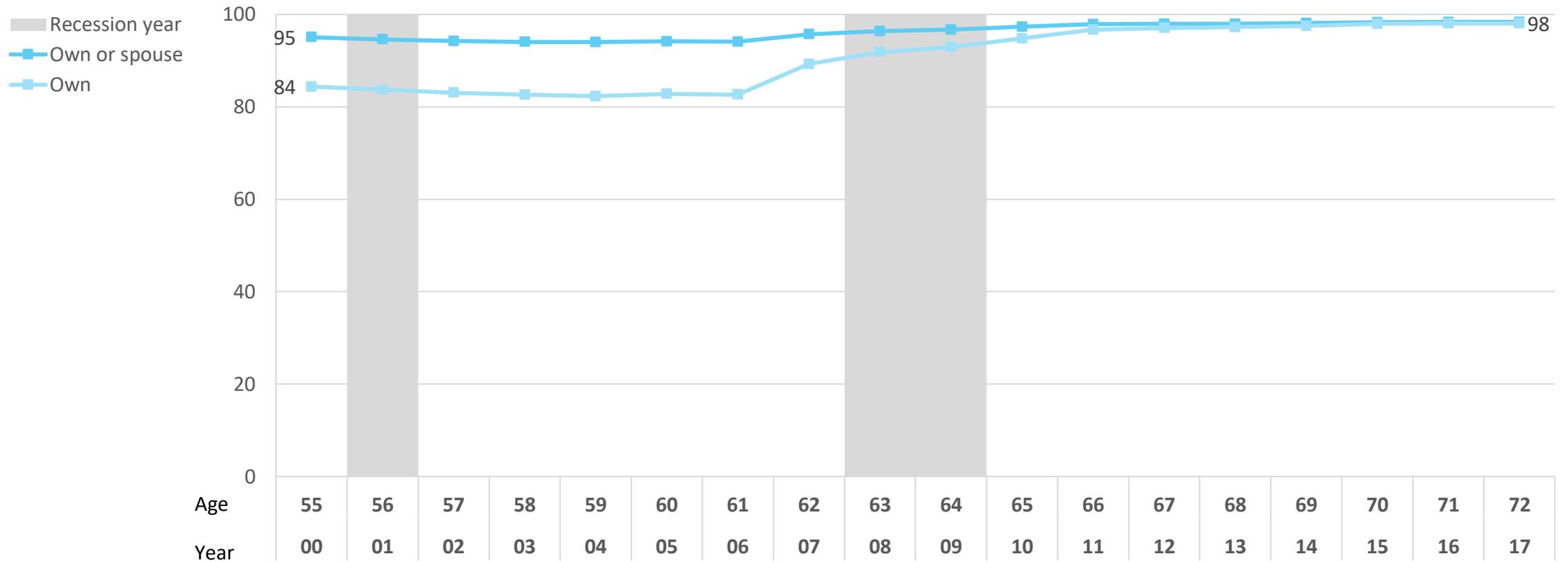
A More Coherent Picture Emerges Looking at Incidence of Labor+SS+Retire Income

Share of the panel with own income (percentage)



Most Have Labor+SS+Retire Income Throughout

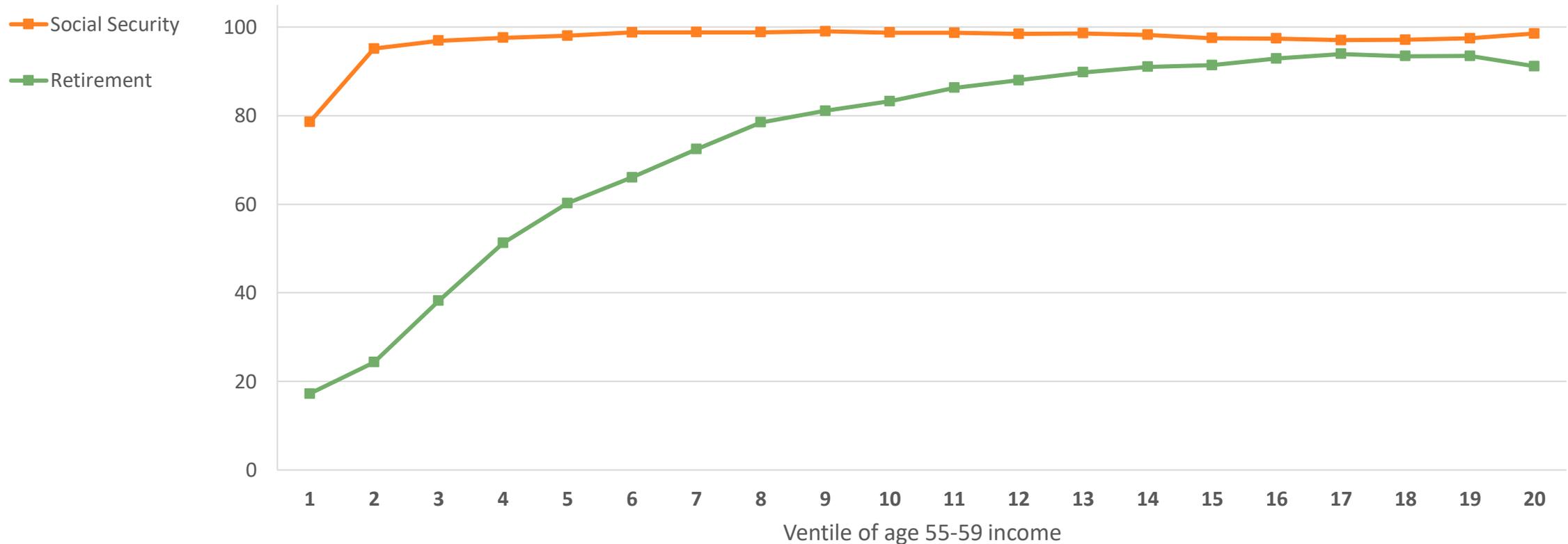
Share of the panel with Labor+SS+Retire income (percentage)



Income Composition at Age 72 by Age 55-59 Income ...

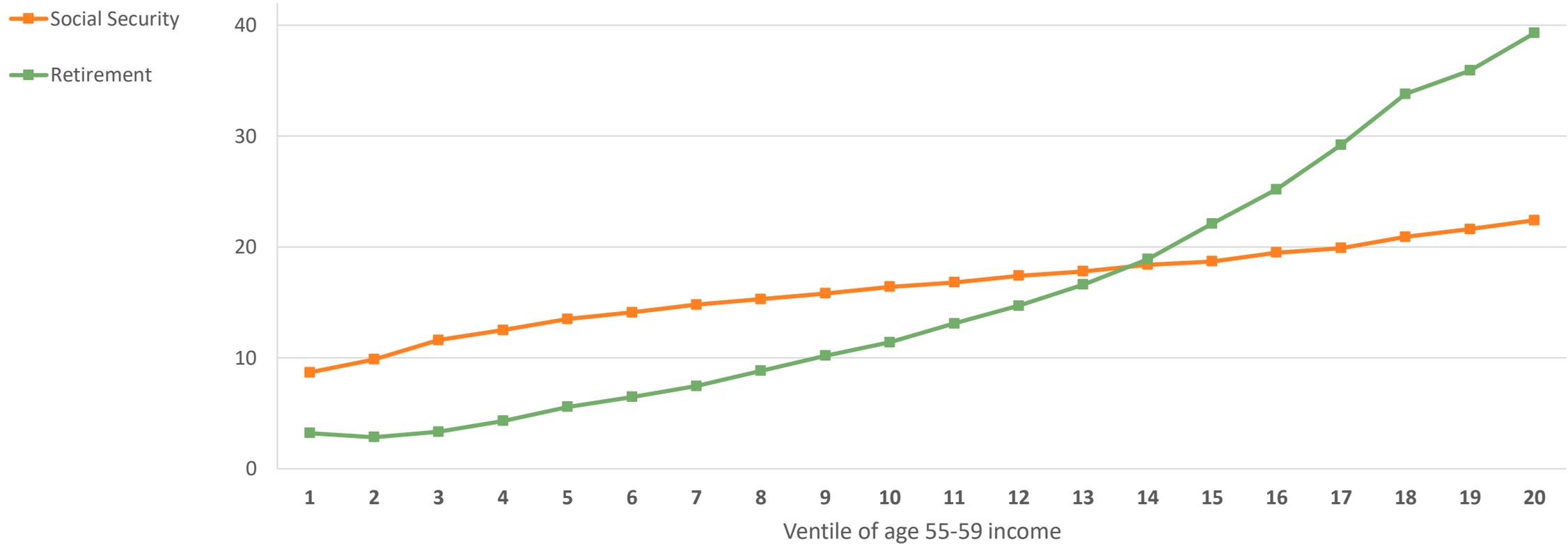
Incidence of Retirement Income at Age 72 Increases Sharply with Age 55-59 Income

Share of the panel with income (own or spouse) at age 72 by ventile of age 55–59 income (percentage)



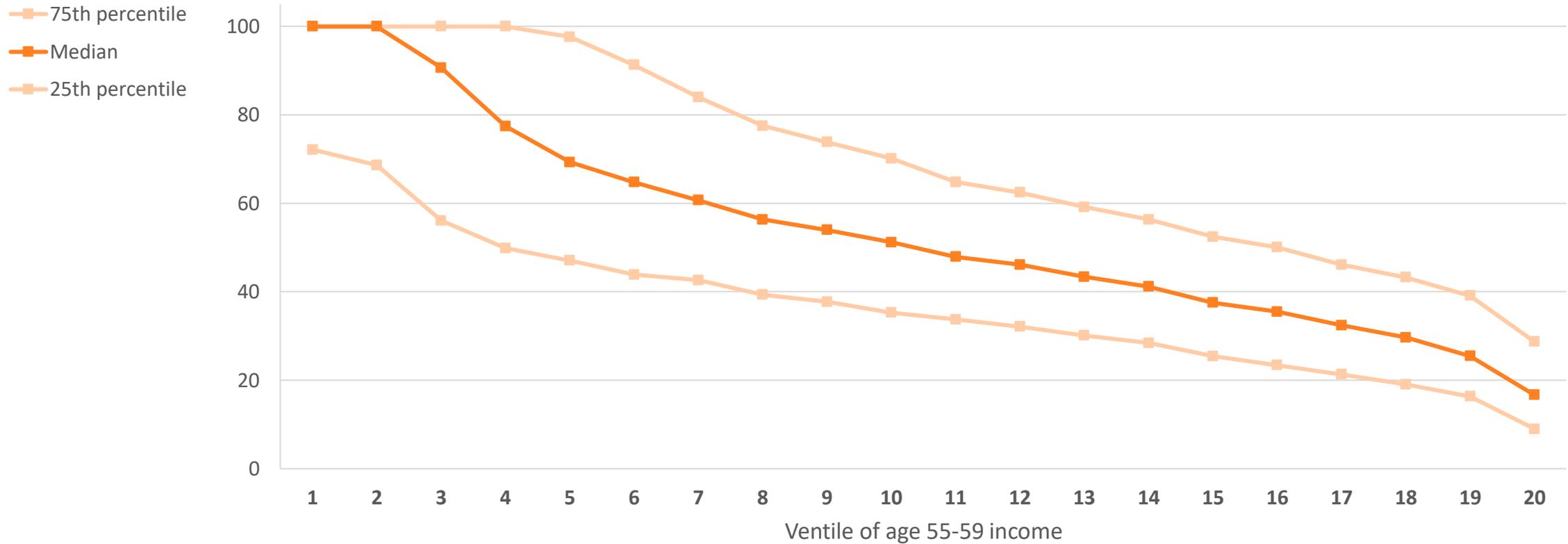
At Age 72, Retirement Income Varies More with Age 55-59 Income than Social Security Income

Median per capita income from source at age 72, 2017 dollars (thousands)



Share of Total Income From Social Security at Age 72

Social Security share of total income at age 72 (percentage)



Summary: Composition of Income

- Retirement is transitional period rather than a point in time
- Composition of income at age 72 varies with age 55–59 income

Our Findings at Odds with Perception of a Failed System

- Income composition
 - Most rely on a combination of Social Security and income from retirement plans
 - 75 percent receive (non-Social-Security) retirement income directly or through a spouse
- Spendable income
 - Typical individual replaces more than 90 percent of their late 50s spendable income
 - Despite relying more on Social Security, lowest income have the highest replacement rates

**Please use the Q&A feature on
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Discussion

Gary Burtless

Brookings Institution

Michael Hurd

RAND and NBER

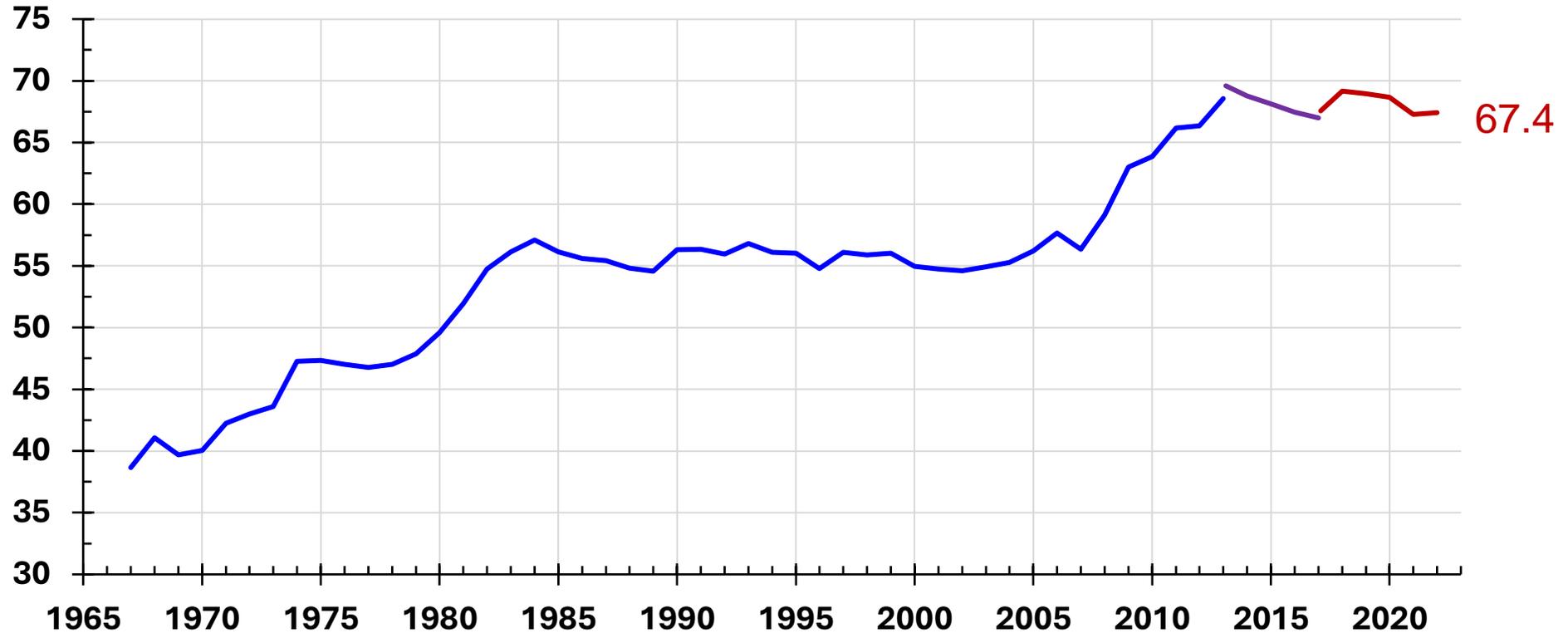
Comments by Gary Burtless (BROOKINGS INSTITUTION) on

**When I'm 64 (or Thereabouts):
Changes in Income from Middle Age to Old Age**

BY PETER J. BRADY AND STEVEN BASS

MARCH 21, 2024

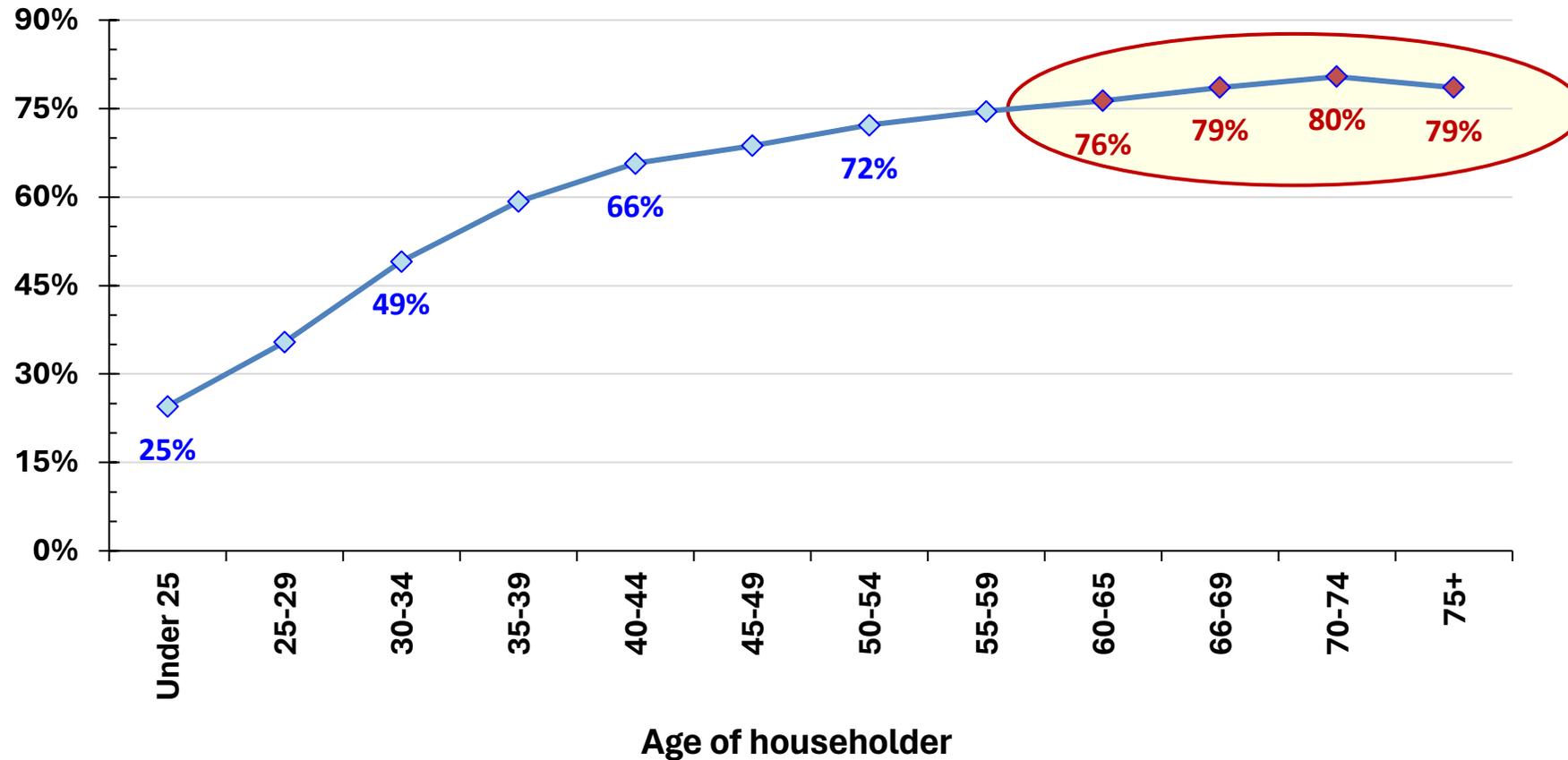
Chart 1. Median income of households headed by adults 65 and older as percent of all-household median income, 1967-2022



Source: U.S. Census Bureau (2023) annual tabulations of CPS ASEC files.

Chart 2. America's aged tend to be home owners

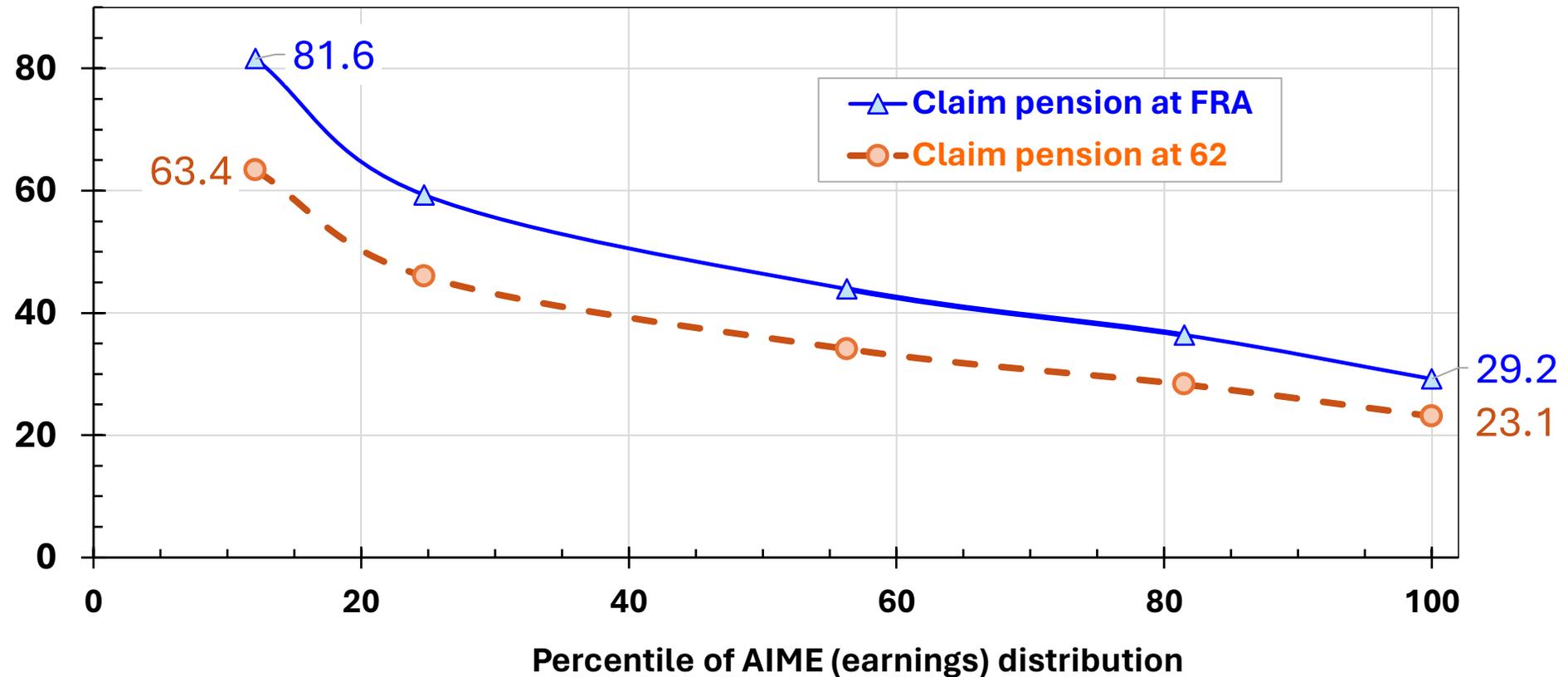
Home ownership rate by age of householder, 2022-2023



Source: U.S. Census Bureau, Current Population Survey/Housing Vacancy Survey, March 12, 2024.

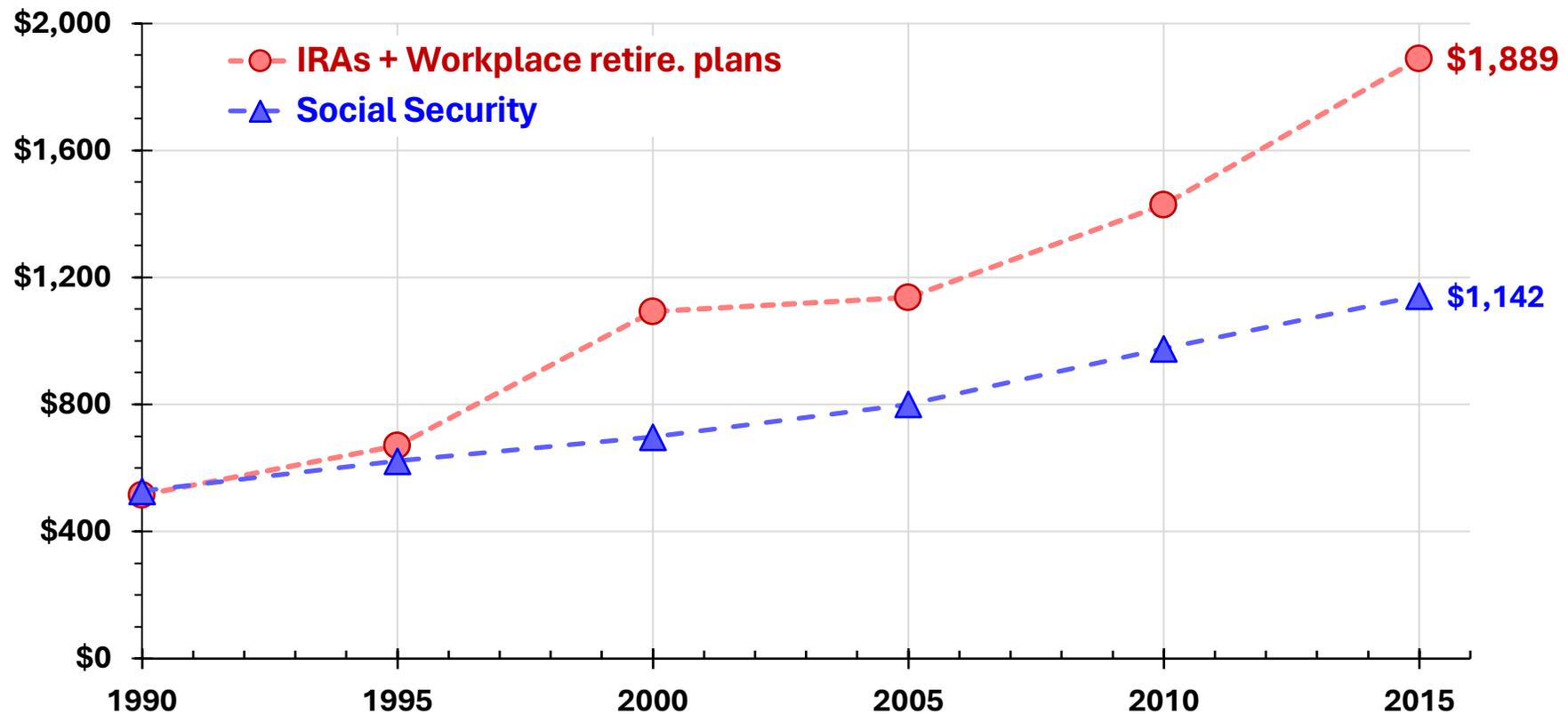
Chart 3. Gross Social Security Replacement Rates for Workers Born in 1948, by Lifetime Earnings Percentile and Age at Benefit Claiming

Percent of worker's annual wage-indexed earnings in highest 35 years of earned income



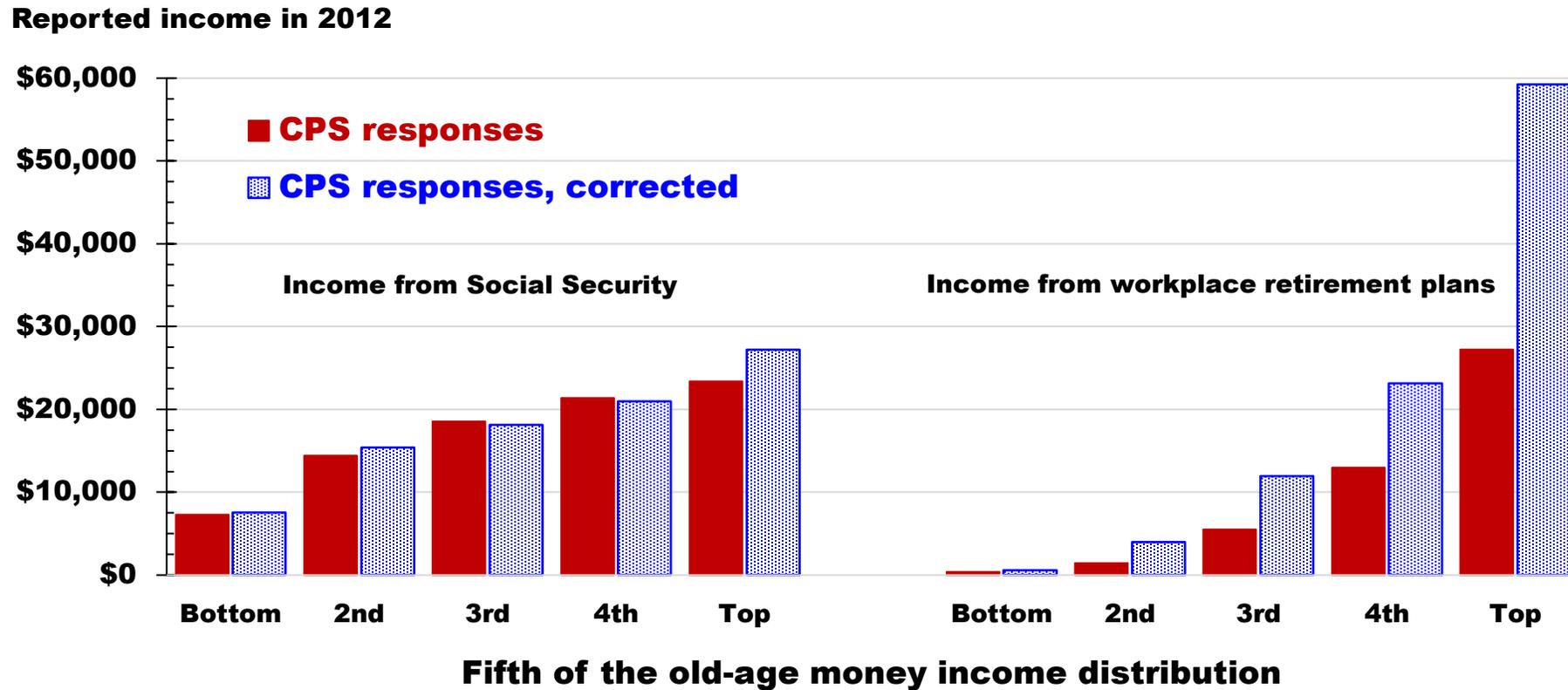
Source: Michael Clingman, Kyle Burkhalter, and Chris Chaplain. 2014. "Replacement Rates of Hypothetical Retired Workers." Actuarial Note 2014.9. (Baltimore, MD: Office of the Chief Actuary, Social Security)

Chart 4. Annual payouts of Social Security and IRAs plus workplace retirement plans, selected years 1990-2015 (Billions of 2023 dollars)



Sources: NIPA statistics, Dept. of Treasury *Statistics of Income*, and author's estimates.

Chart 5. Social Security and Retirement Income Reported in CPS and in Administrative Records for Americans 65 and Older, 2012

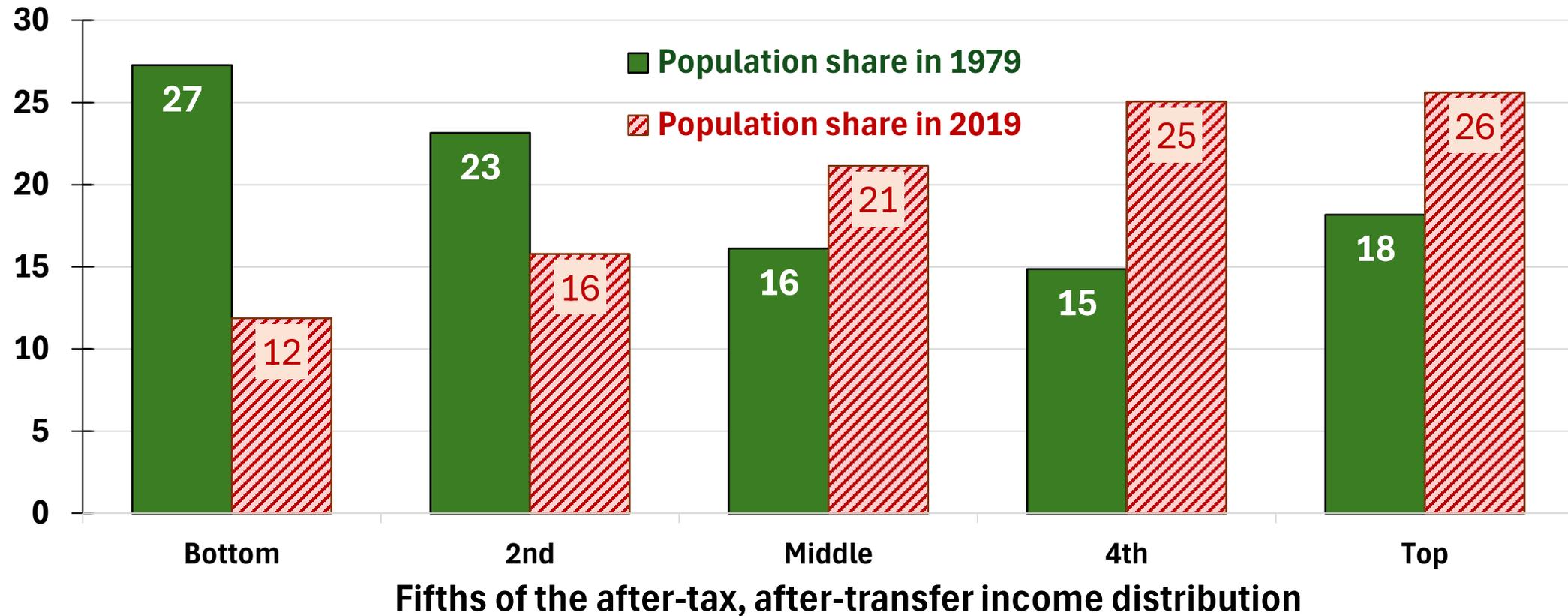


Note: Workplace retirement plans include employer pensions and taxable withdrawals from retirement plans, including IRAs

Source: Bee and Mitchell (2017) and author's calculations.

Chart 6. Percent of aged population in each one-fifth of the overall distribution of after-tax, after-transfer income, 1979 and 2019

Percent of the population past 65



Source: CBO (2023). Households are ranked by their after-tax, after-transfer (household-size-adjusted) incomes. The rank of each elderly adult is determined by the rank of the household of which it is a member.

When I'm 64 (or Thereabouts): Changes in Income from Middle Age to Old age

Discussion by
Michael D. Hurd
RAND, NBER, NETSPAR



Social and Behavioral Policy Program



Overall

- Terrific paper!
- Typical replacement rate recommendations range from 65% to 95%
- Most people in Brady & Bass 90% or over
- Less well-to-do have even higher rates
 - Role of Social Security
- More well-to-do have lower rates but spend assets
 - Couples age 65-69 have assets of **\$800,000** (2017\$) (Hurd and Rohwedder)

Shows value of close attention to detail!

Suggestions for additions

- Follow cohorts to older ages
- Estimate population trajectories accounting for mortality
 - Drop balanced panel
 - Survivors to age 72 may have different trajectories than decedents
 - Calculate one-year panel rate of change of income using all one-year survivors
 - E.g. percent change in income at age t among those who survive from t to $t+1$
 - Apply rates of change beginning with baseline income to yield income trajectory for population alive at each single year of age

But why Replacement Rates?

(A) Difficult to quantify In Today's Multi-pillar Retirement Financing System

- **What income pre- and post-retirement?**
 - Pre- or post-tax?
 - Dedicated contributions to retirement accounts
 - Take out work-related expenses?
- **Whose retirement?**
 - He is retired; she is not
 - Unretirement
 - Problem solved by tracing out age path
 - B&B used age as an instrumental variable

Replacement Rates (cont.)

(B) Life-cycle theory: household spending path not flat

- Spend more when children are in the house
- Survival
 - Most begin retirement married
 - About 56% of household's life expectancy spent as couple, 15% as widower and 29% widow
 - Rest-of-lifetime consumption about 17% lower on this basis alone
 - Differential survival by sex, SES, and marital status
 - Shift more spending to when more persons in household and shift depends on SES

Large Differences in Survival Chances

By sex, education & marital status:

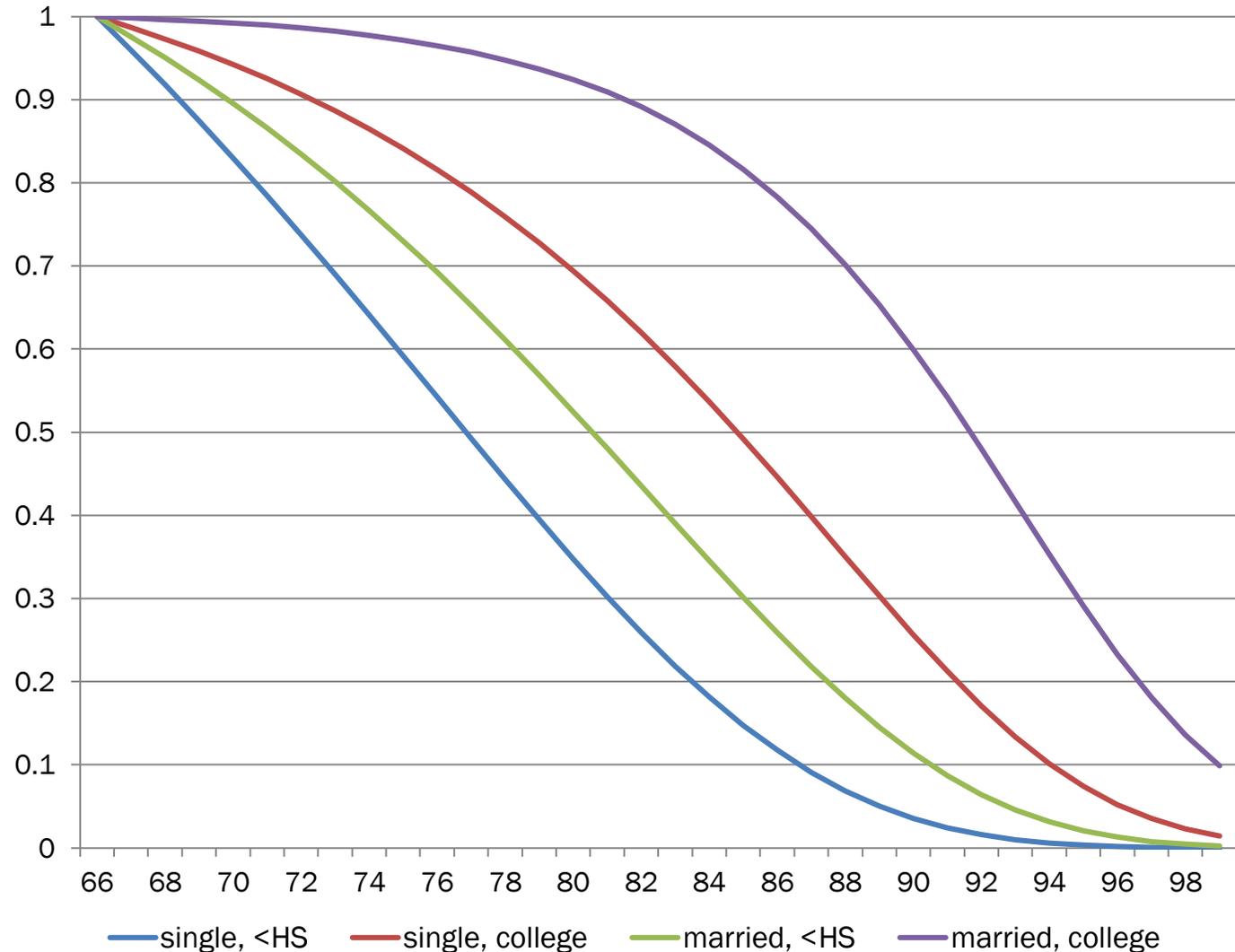
Single males lacking a high school degree

- 50% chance of survival to age 77

Married males with college degree

- 50% chance of survival to age 92

Differential Survival:
Men aged 66, by education and marital status



Source: Hurd and Rohwedder, 2012

Replacement Rates (cont.)

It's not just income

In HRS we observe spend-down of assets to support consumption

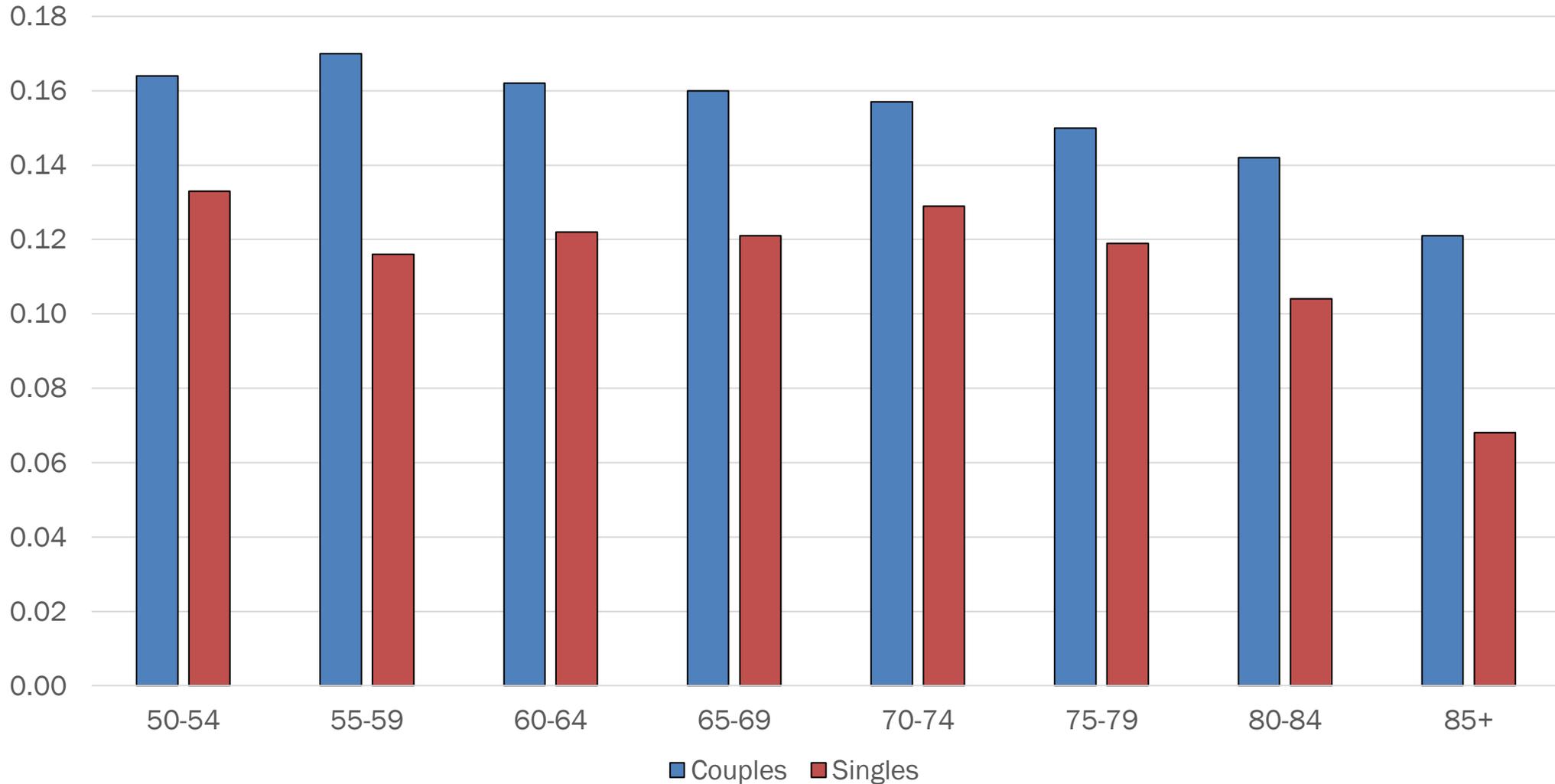
- Single persons: about 1.9% per year decline in assets
- Married persons: about 1.1% per year

Spending Following Retirement

- After retirement more time available for **home production**
→ can spend less to achieve same consumption bundle
- **Marginal utility of some types of spending depends on health**
 - Health-care spending is a substitute for health
 - Spend less when in good health
 - Many types of spending are complements to health
 - Spend more in good health
 - Some neutral

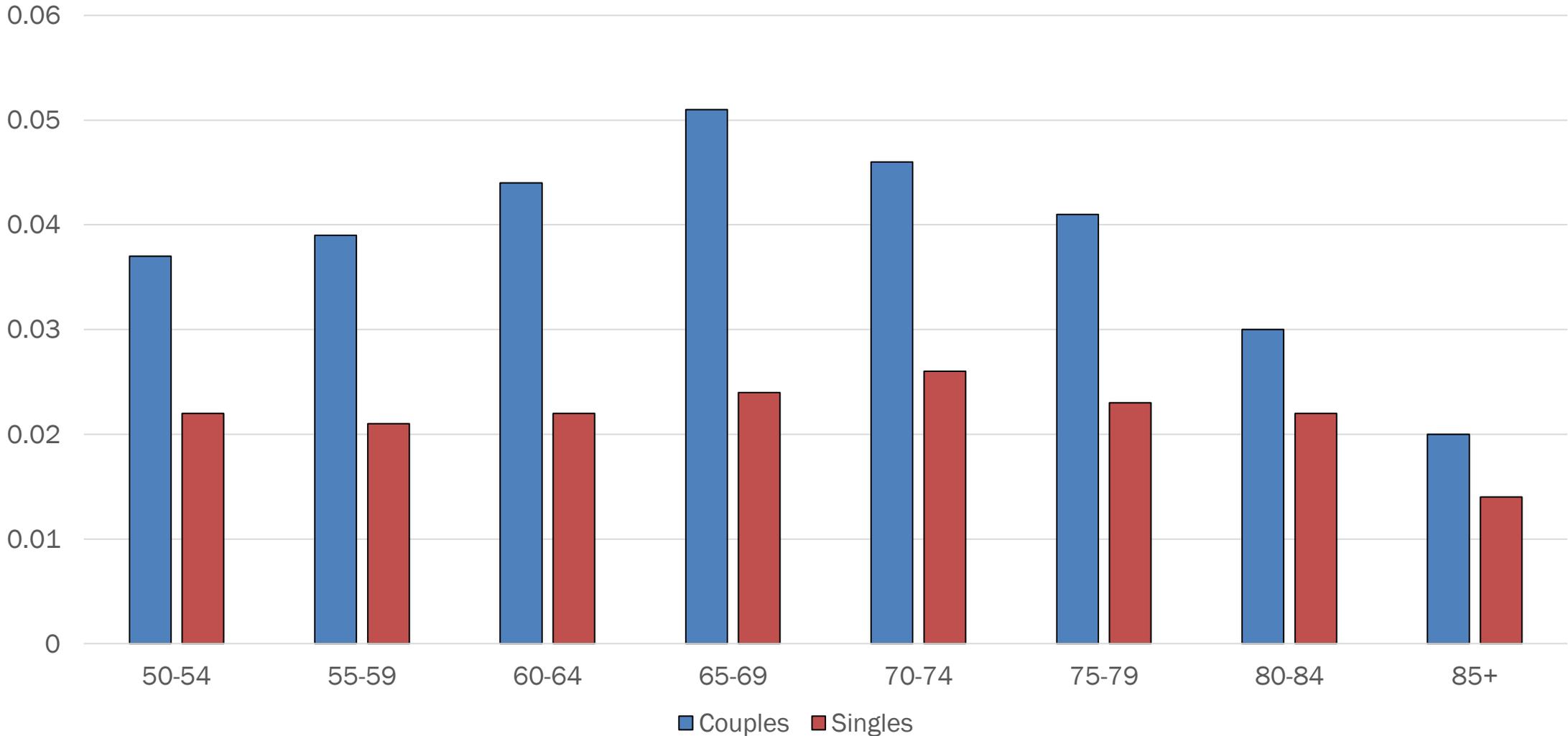
Budget Shares: Transportation

Complement to health - spend more when healthy



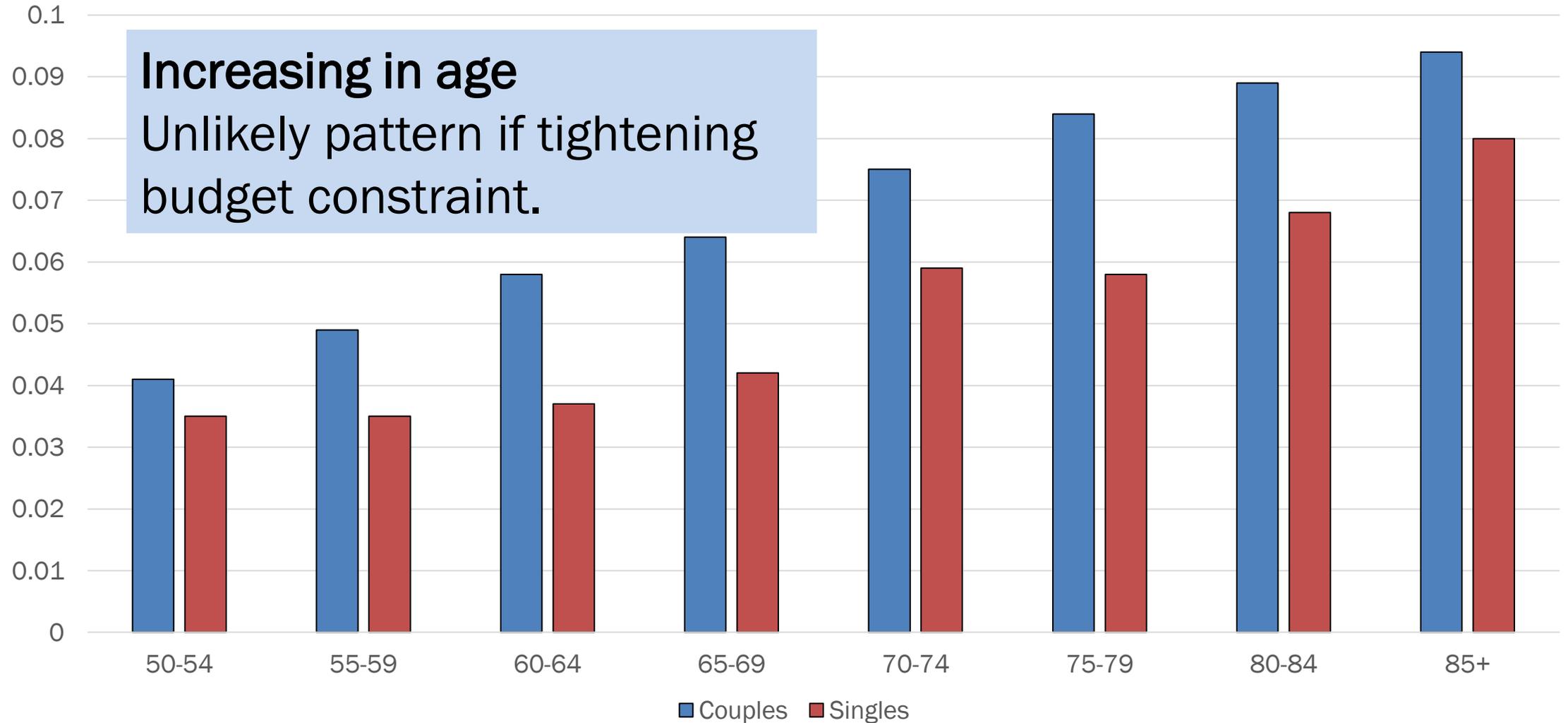
Budget Shares: Trips and Vacations

Complementary to health. Time input & social situation.



Budget Shares: Gifts and Donations

Neutral to health?

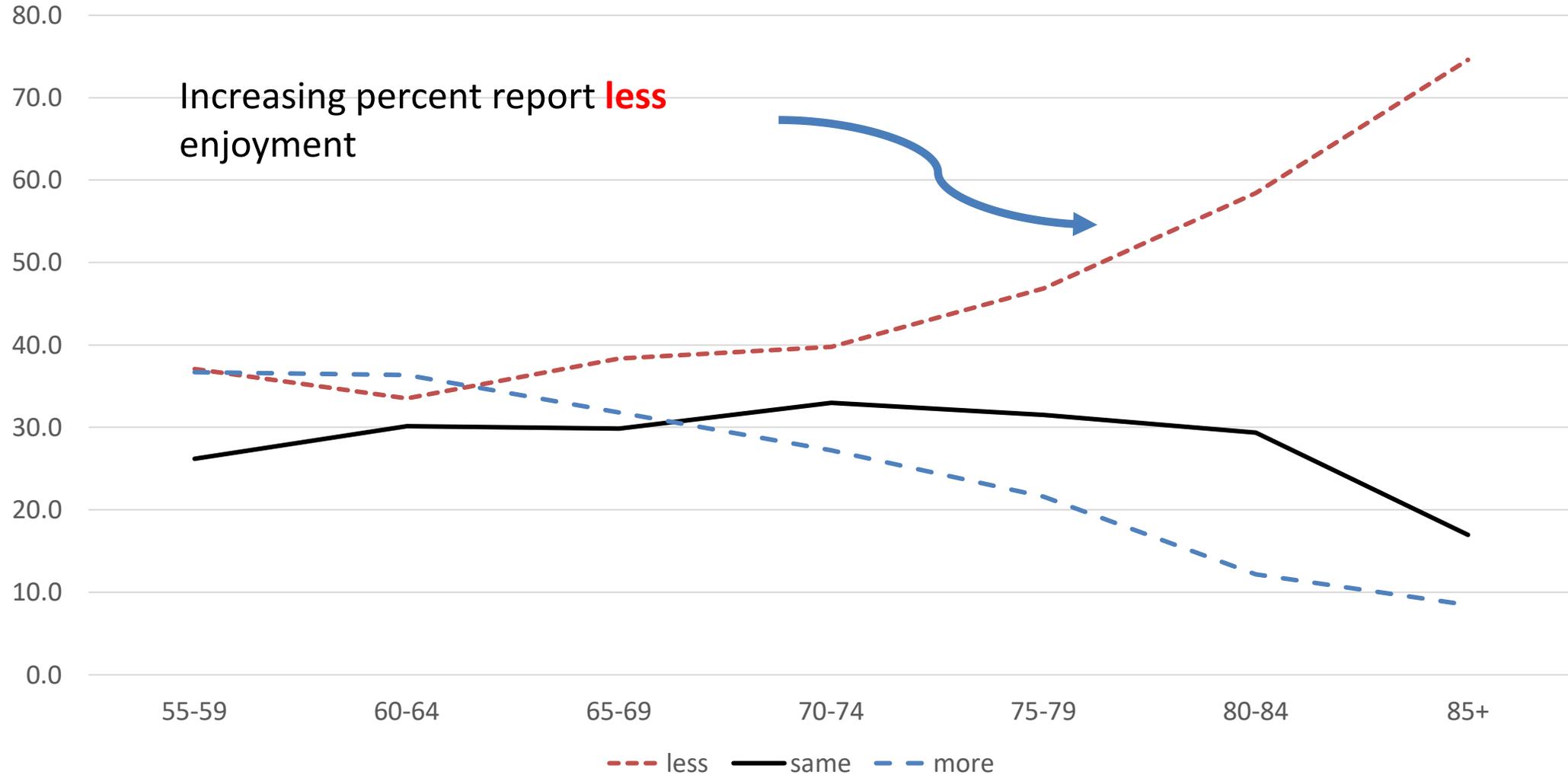


Why these declines in budget shares?

- Interactions with age and presumably with health?
 - Asked HRS respondents about how enjoyment from activities today compares with six year ago

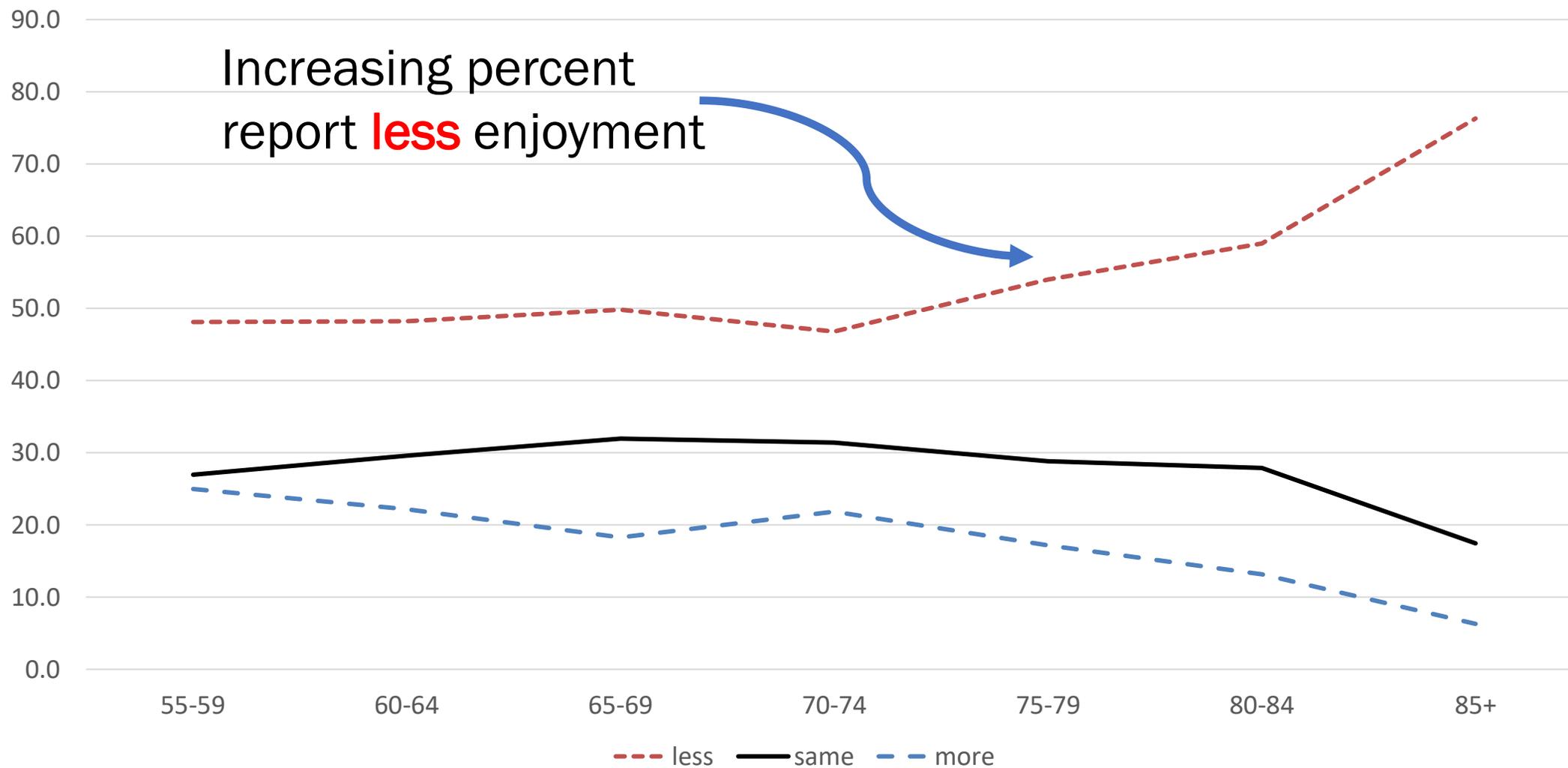
Enjoyment today compared with 6 years ago:

Traveling



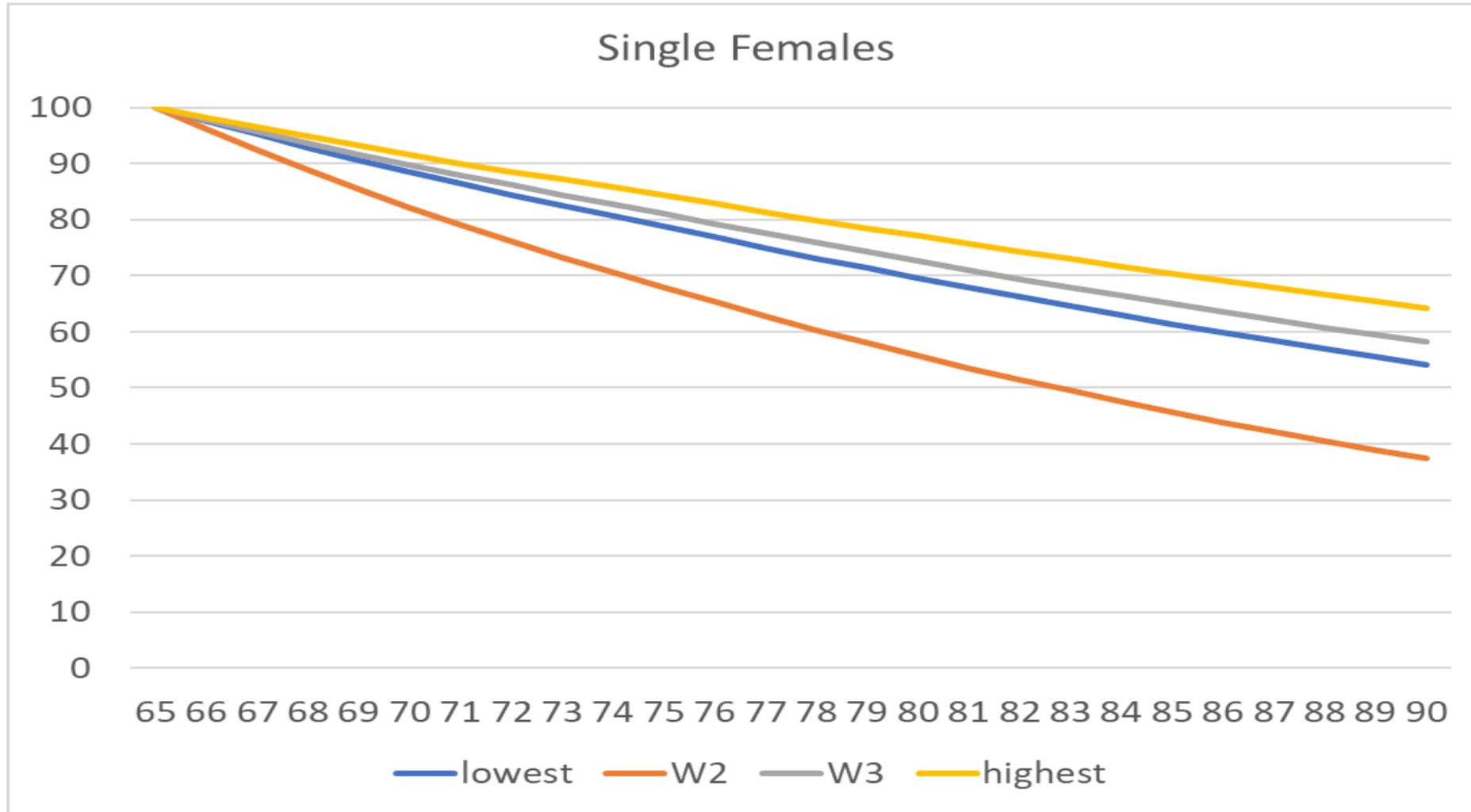
Enjoyment today compared with 6 years ago:

Having a new car



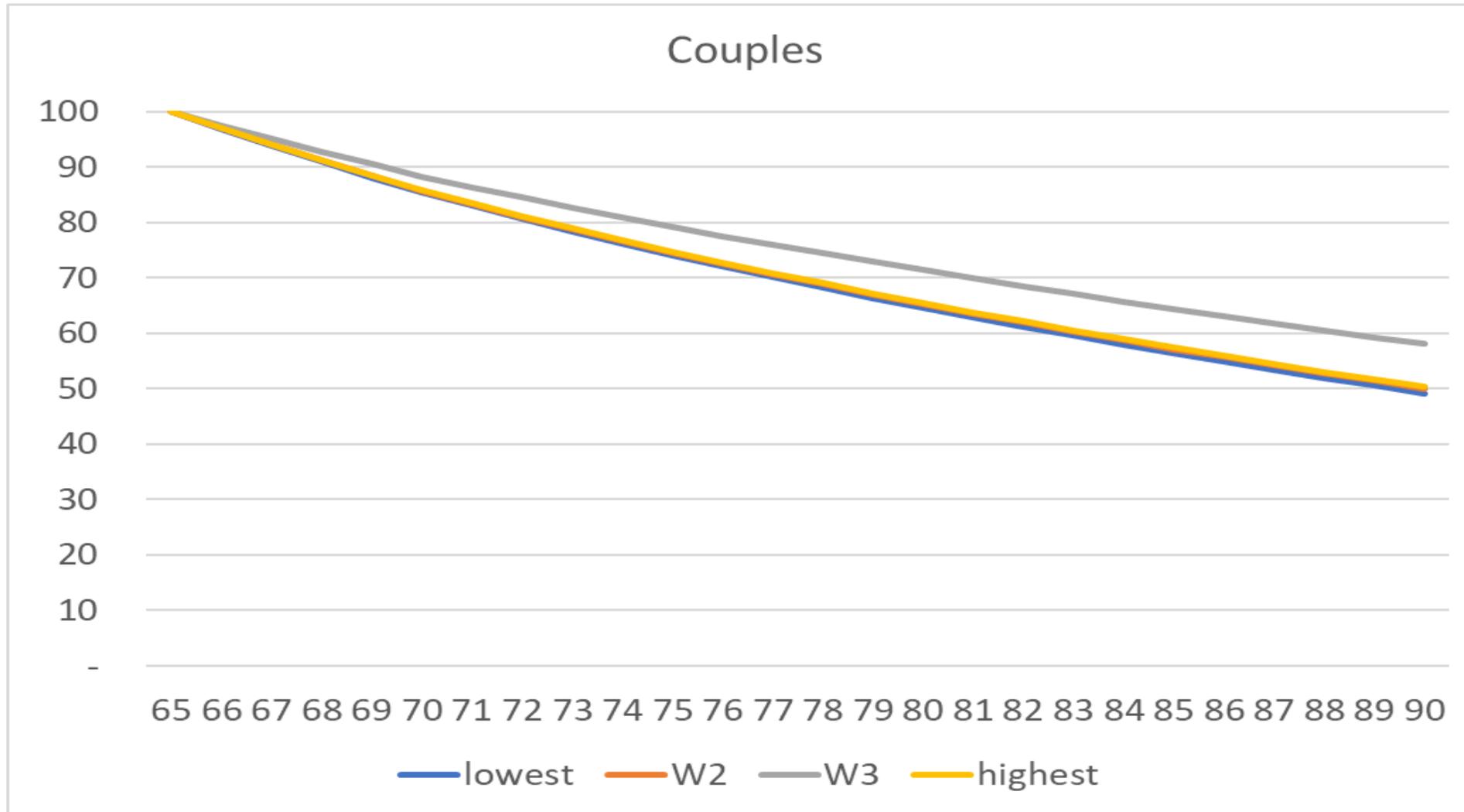
What about total spending?

Estimated Spending Paths: Single Females by Initial Wealth Quartile



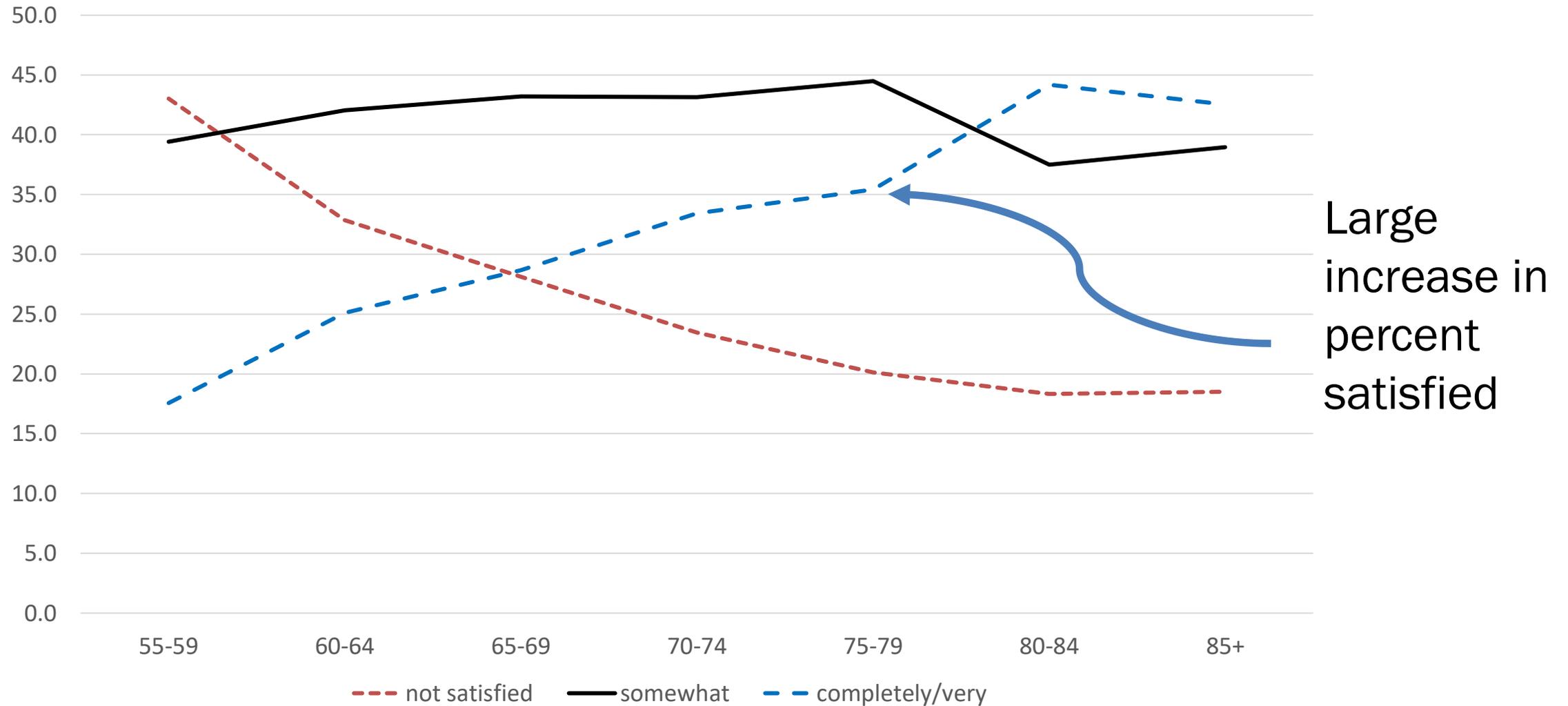
Declining
total
spending in
all wealth
quartiles

Estimated Spending Paths: Couples by Initial Wealth Quartile



Declining
total
spending in
all wealth
quartiles

Satisfaction with Financial Situation



Our Interpretation

- Most enter retirement adequately prepared
- According to our metric about 75% (Hurd and Rohwedder, 2023)
 - Single: 62%
 - Married: 86%
- Our conclusion complementary to Brady and Bass

We don't see widespread retirement-saving crisis

- Except for some subpopulations such as single females lacking a high school degree

But importance of Social Security

- Dependence on Social Security very high among low income persons
 - Single persons lacking high school
 - About 61% of total economic resources from age 65-69 to end of life
 - Including housing and other assets.
- Critical to solve Social Security funding crisis

**Thanks for your
attention!**



Social and Behavioral Policy Program

mhurd@rand.org

Panel Discussion

Shelly Antoniewicz (Moderator)

Investment Company Institute