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Working To Fix Our Fiscal Woes

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Work may be a four-letter word to some citizens in slow-growing Western European economies, but Americans know better. So do Frenchmen ranging from de Tocqueville to France's current interior minister, who have both touted the U.S. work ethic.

Ironically, projections about how much Americans will work are now at the heart of worries about emerging crises in U.S. public finances -- whether government deficits or imbalances in Social Security's bankbook. The latter, for instance, are largely a work-related fiscal woe, as the number of workers supporting each retiree falls by an estimated one-third over the next 30 years.

What makes our work habits suddenly so important? For starters, a postwar boom in the U.S. labor force is just now ending. Since around 1950, the percentage of adults who worked rose almost every year except in recessions. But now the great swell of working boomers is starting to retire, and most of the gain in female labor force participation is over. If Americans keep retiring at the same ages they do today, the share of adults who are working will fall markedly. The effect on the economy will be roughly equivalent to increasing the unemployment rate by 3/10 of 1 percent every year for 20 years straight starting in 2008. That means a lower rate of growth for workers, goods, services, and government revenues.

But what if we played to our strength -- a strong and flexible labor market -- by working a little longer? For workers who hang in there, their lifetime income obviously would increase, but their greater reward would be bigger nest eggs to spend down over fewer years of retirement. Even an extra year or two of work reduces the risk that too few Americans face up to when they retire -- that rising costs, especially for health care, make what appears adequate near retirement seem paltry in later years. Since a typical 62-year-old couple today is likely to have at least one spouse who lives another 25 years, most couples need to line up resources for 30 years or more to play it safe.

In short, the most important financial decision facing most people in their 60s is when to retire. Which stocks or bonds to buy -- a typical focus of financial magazines -- is usually far less consequential.

Working longer helps the nation, too. Additional time on the job increases national income, while boosting the revenues needed to float government programs, including those serving the elderly.

Now let's look ahead. Research that Barbara Butrica, Karen Smith, and I did on the effects of working longer show that annual household retirement income, including Social Security, would typically increase by about 6 to 10 percent for each additional year of work. Workers on average would have

an annual income 55 percent higher if they retired for five fewer years, saved some of their additional earnings, and delayed receipt of Social Security benefits.

The percentage increases in annual income for additional work would usually be higher for households with lower lifetime earnings. After five additional years of work, the bottom three-fifths of retirees -- which include seniors well into the middle class -- would see gains ranging from 61 to almost 100 percent.

From a national perspective, it's useful to look out about four decades, when fiscal and Social Security problems are projected to be the most severe. One additional year of work would generate additional earnings to individuals about equal to the entire shortfall between benefits and taxes in the old age insurance portion of Social Security. Five more years of work would generate more in additional taxes to the government (including Social Security and income taxes) than the amount of the shortfall. That same five years would produce enough additional Social Security taxes alone to cover half of the shortfall, if benefits were kept constant.

Obviously just working longer won't solve the nation's fiscal mess or the tangle of old age issues. Not all are well enough to work to later ages, even though life expectancy is increasing and ever fewer jobs are physically demanding. But extra years of work would allow most Americans to live better in retirement and government to provide higher levels of both Social Security and non-elderly program benefits at any given tax rate.

The United States is lucky. It has a flexible and vigorous labor market to which many Western Europeans turn as an example of how to deal with their stagnant employment and economies. Let's not turn in the opposite direction by ignoring work's potential role in solving our own fiscal problems.

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