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Delays in claiming social security benefits

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Abstract

This paper focuses on Social Security benefit claiming behavior, a take-up decision that has been ignored in the previous literature. Using financial calculations and simulations based on an expected utility maximization model, we show that delaying benefit claim for a period of time after retirement is optimal in a wide variety of cases and that gains from delay may be significant. We find that approximately 10% of men retiring before their 62nd birthday delay claiming for at least 1 year after eligibility. We estimate hazard and probit models using data from the New Beneficiary Data System to test four cross-sectional predictions. While the data suggest that too few men delay, we find that the pattern of delays by early retirees is generally consistent with the hypotheses generated by our theoretical model.

Keywords: Social security benefit; Claiming behavior; Utility maximization model; New Beneficiary Data System; Cross-sectional predictions

Social Security (SS) is the largest entitlement program in the United States today, providing income support for retired and disabled workers and their families. The concurrent growth in this program and decline in the labor force participation of older men has motivated an extensive literature investigating how SS influences retirement behavior. There is another large literature investigating the transfers induced by SS across and within cohorts.

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One common feature of the work in this area has been the assumption that individuals claim benefits as soon as they are eligible — either upon retirement, or upon turning age 62 if retirement is before that age. However, as with other social insurance programs, there is a *take-up decision* associated with claiming SS benefits. Individuals need not claim their benefits immediately upon retirement, or upon turning age 62. By delaying claiming, workers increase the benefits paid to them and their spouses, through the actuarial adjustment. As we demonstrate below, it is optimal in a wide variety of cases to delay claiming benefits for a period of time after eligibility. Moreover, for at least one group, men retiring before their 62nd birthday (the age of first eligibility for benefits), claiming delays are empirically important: roughly 10% of these retirees delay claiming for at least 1 year.

This *dynamic take-up* consideration suggests that standard computations of both the retirement incentives of SS and the redistribution through SS may be biased. Moreover, we are not aware of any in-depth analysis of this take-up behavior. An examination of the extent to which observed claiming patterns are consistent with rational choice theory may have important implications for aspects of SS design and reform.

The purpose of our paper is to investigate delays in SS benefits claiming and to explore their implications. We do so in five steps. First, in Section 1, we provide relevant institutional background on the SS program. We highlight the fact that retirement provides only a necessary, and not a sufficient, condition for receiving SS benefits.[1] We briefly review the SS literature, emphasizing areas where realistic consideration of claiming behavior can affect analysis.

In Section 2, we turn to a theoretical examination of claiming delays. We begin with a discussion of the benefit rules to explore how worker characteristics such as mortality expectations, wealth, age difference with spouse, and relative earnings of spouses may influence claiming delays. Then we use simulations of financial gains from delay to generate cross-sectional predictions that can be tested in our empirical analysis. We also present simulation results based on an expected utility maximization model with liquidity constraints, as we recognize that financial calculations in general *understate* the incentives to delay relative to the optimization of a risk averse utility function. This is because SS provides a real annuity valued by risk averse individuals with an uncertain date of death; individuals buy more of this annuity by delaying, so delays are more attractive with risk aversion.

Section 3 presents evidence that claiming delays are empirically relevant. We use data from the New Beneficiary Data System (NBDS), a survey of SS claimants in the early 1980s. This survey provides administrative data on work and benefits histories which allows us to form a relatively precise measure of claiming delays. We highlight the differences in delays by early retirees, those retired before their 62nd birthday, and later retirees, those retiring after their 62nd birthday. We

[1] This discussion applies only to those under age 70; at age 70, benefits are paid out regardless of retirement.