



## Director's Corner

In establishing the two retirement research centers at the University of Michigan and at Boston College, the late Steven Sandell had in mind a network of eminent researchers who would provide a sound scientific basis for Social Security policies now and in the future. That objective remains our overarching goal. The Michigan Retirement Research Center (MRRC) was established two years ago to promote research, training, and dissemination of information related to retirement and Social Security policy with funding from the Social Security Administration. We have been actively engaged in these activities and are making the results of our efforts available via a number of avenues. The focal source of information about our activities is the MRRC website (<http://www.mrrc.isr.umich.edu>). There you can find discussion of our research projects, papers, and research briefs, and biographical information about the researchers who are associated with the Center. The MRRC supports researchers from around the country who are trained in a variety of academic disciplines.

The Center provides other opportunities for you to be involved. There are opportunities described on our website for training workshops, seminars, and conferences. For example, each year, one of the research centers hosts an annual conference that is open to all that brings together Center researchers, policy makers and members of the Social Security Administration. Funded training positions are also available. In addition to information about the Sandell Dissertation Award, a national competition for dissertation support, there is also information on how to apply for pre- or postdoctoral fellowships. And there is much more information on a variety of topics.

These are our first steps towards getting information into the hands of people who can use it to make a difference. We are all grateful for the opportunity to make a contribution and eagerly embrace the work that allows us to do so.

*Lee A. Lillard*  
Center Director

### Visit Our Website!

<http://www.mrrc.isr.umich.edu>

- ◆ *Conferences and Events* are listed that may be of interest to researchers, policymakers, and the general public interested in retirement and social security.
- ◆ *Training and Education* provides information about *pre and post doctoral fellowships* available through MRRC, graduate coursework at the University of Michigan, training workshops and seminars.
- ◆ *Research and Findings* presents an array of materials representing the work of Center researchers including *Issues in Brief*, *Conference Papers*, *Working Papers*, and the *Newsletter*.
- ◆ *Data* directs potential users to valuable sources of data for retirement research.

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*Issue in Brief*

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## How Effective Is Redistribution Under The Social Security Benefit Formula?

by Alan L. Gustman and Thomas L. Steinmeier

### Executive Summary

Conventional wisdom holds that the social security benefit formula is highly redistributive by favoring low over high earners. It certainly is true that the structure of the benefit formula is highly progressive as it replaces a much higher share of earnings for *individuals* with low rather than high earnings. The focus on the *individual* may be misplaced, however. From a public policy perspective, the proper accounting unit for evaluating redistribution is the *household*. This *Issue in Brief* will describe an empirical investigation using data from the University of Michigan Health and Retirement Survey (HRS) linked with social security records for a cohort of individuals nearing retirement. We address only retirement, spouse, and survivor benefits using current social security benefits and formulas.

We provide here a brief overview of the major findings of our investigation. Our aim was to determine the extent of redistribution fostered by the current Social Security System on the basis of each individual's earnings, and then to see how the extent of redistribution changes when we instead look at redistribution on the basis of total household earnings and finally at redistribution on the basis of *potential* household earnings, which is what the household could earn if both partners worked full time.

Our analysis contributes to our understanding of just how much redistribution the current system fosters. This information is required to inform policy makers who are involved in system reform. These calculations also provide a benchmark to help understand the effects of various reforms. Any large change in the system will require an accounting of winners and losers, which in turn depends on the extent of redistribution under the current system.

### How the Social Security Benefit Formula Works

For each individual, the Social Security Administration calculates a measure of lifetime earnings which is an average of the high 35 years of earnings. The earnings measure is typically expressed as a monthly amount, the Average Indexed Monthly Earnings (AIME). A progressive benefit formula is then applied so that those who have low computed lifetime earnings have higher benefits, relative to earnings, than do those with high earnings. Spouses are entitled to roughly half of their partner's benefits, and survivors are entitled to an amount roughly equal to what would have been paid to the deceased.

### The Data

The Health and Retirement Study (HRS) is a longitudinal, nationally representative study of older Americans. The survey began in 1992 with an initial cohort of 12,652 individuals from 7,607 households, with at least one household member born from 1931 to 1941. Social security earnings histories were linked for 9,472 respondents, or about 75 percent of the respondents to the survey. Of the respondents with linked earnings histories, there were 7,370 who were born between 1931 and 1941, for whom the HRS is representative.

### Summary of Major Findings

#### Work and Earnings Patterns

For the purposes of this report, we distinguish individual lifetime earnings from household lifetime earnings. Household lifetime earnings are the combined lifetime earnings of a husband and wife.

Overall, we find that AIME is a poor indicator of lifetime household earnings. Many individuals in the lowest levels of AIME may not be as poor as their individual AIME suggests.

Many workers falling in the lowest AIME categories, mostly women, are there because they worked few years, rather than because they have low earning potential.

(Continued on page 5)



## ***Winner of the 2000 Sandell Dissertation Award*** ***Purvi H. Sevak***

The Sandell Dissertation Award was created to honor the late Steven H. Sandell. Dr. Sandell was a distinguished researcher, leader, and public servant. He created and then served as Director of the Division of Policy Evaluation at the Social Security Administration. In spearheading the creation of the Retirement Research Centers, Dr. Sandell hoped that they would serve to cultivate a new generation of social scientists whose work would shape the future direction of policy research. As a tribute to his scholarship, leadership, and vision, a dissertation grant program was established in his name. Each year, one grant is awarded to a doctoral candidate pursuing work in a priority research area. Following competitive review by a National panel of experts in the area of retirement research, this year's award was granted to Purvi Sevak.



Purvi is a Ph.D. candidate in the department of economics, and a research associate at the Survey Research Center, both at the University of Michigan. She has also been a pre-doctoral trainee, funded by the National Institute on Aging, at the Populations Studies Center at the University of Michigan, since 1997. Her fields of specialization are labor economics and public finance. Her specific areas of interest include disability, aging, and income security. Purvi's work with the MRRC examines the impact of widowhood on the economic prospects of women. Her other recent work includes: estimating the effect of welfare reform on SSI-disabled caseloads; estimating the potential long-term earnings costs of care giving for elderly parents, and the importance of these costs in the decision to provide informal care; and examining the importance of offspring gender composition on nursing home placement. Before attending graduate school, she was a research assistant with the Lewin Group, a health policy consulting group. Purvi received her Bachelor's degree from Cornell University in 1995 and her Master's degree from the University of Michigan in 1998.

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### **Instructions For Sandell Dissertation Grant Applicants**

#### **Prerequisites:**

1. Admission to Candidacy (completion of all dissertation requirements except research and writing)
2. An approved dissertation proposal for research in the general area of retirement and Social Security policy issues.

#### **Application Information Required:**

1. Cover sheet – The cover sheet should include the title of proposed research, applicant's name and contact information, proposal date, institutional affiliation with full address; names of committee chairperson and members
2. Abstract – one page maximum length
3. Proposal – 10 page maximum length. Reviewers will look for the following major sections within the proposal: hypothesis, background, research significance, research methods and data, bibliography.
4. Budget – A budget should be submitted for a maximum total cost of \$25,000.
5. Other Funding Sources – Show other funding available as well as funding requested from other sources.
6. Letters of reference – Three letters of recommendation are required; one must be from the dissertation chair.
7. Resume

#### **Deadline for submission of proposal**

Applications must be received by February 1, 2001. Award decisions will be announced by April 2, 2001

#### **Proposal Submission:**

Applications must be submitted in two hard copies and one electronic copy (which may be via file transfer, IBM disk, or zip disk).

Sandell Dissertation Grant  
Michigan Retirement Research Center  
University of Michigan  
426 Thompson Street  
Ann Arbor, MI 48106-1248

## *F* *or* *Y* *our* *I*nformation

### How Social Security Figures Your Retirement Benefits

To figure your benefits, the Social Security Administration begins by calculating the amount you earned over your working life in the average year. Your earnings are first adjusted to account for changes in the value of the dollar over your lifetime. Then they calculate your average monthly earnings during the 35 years you worked the most.

Next, they apply the following formula to figure your monthly benefit, or "Primary Insurance Amount (PIA)" that you can receive at retirement age (currently 65):

- ◆ 90 percent of the first \$531 of your average monthly earnings
- ◆ 32 percent of the next \$3,202 of your average monthly earnings, and
- ◆ 15 percent of remaining earnings.

### Who Gets Retirement Benefits?

You will need at least 10 years of work to qualify for retirement benefits from social security. Your spouse is entitled to roughly half the amount of your PIA, regardless of his or her work history. If your spouse has worked and paid in to the system, he or she will first receive the amount that would be due based on his or her own earning record. If the spouse benefits would be more, additional payments are made to bring the spouse up to the amount of the spousal benefit.

A worksheet is available on the SSA Web Site that allows you to calculate your own benefits.

<http://www.ssa.gov/pubs/10070.html>

Source: Social Security Administration Web Site, 2000 (<http://www.ssa.gov>).

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## Training Opportunities

The Michigan Retirement Research Center offers *Post-Doctoral Fellowships* to citizens and non-citizens of the United States. The Center is now accepting applications for the summer or fall of 2001. The one-year stipend is \$30,000 plus benefits with the potential to renew for a second year.

Fellows will conduct research in collaboration with one or more of the Center's Research Associates. Fellows are encouraged to participate in Center activities such as coursework, conferences, and seminars. The National Academy of Social Insurance, one of the Center's affiliated institutions, will provide Fellows with a Washington, D.C. base during their period of study.

To apply, submit a curriculum vita, a transcript, letters of support, and a brief research proposal that outlines activities for the year. Applications will be evaluated for how well the proposed research fits with the Center's priority research areas and how well the applicants' expertise complements that of the Center-affiliated faculty and researchers.

Application materials and/or questions about the Post-Doctoral Fellowship program should be directed to Becky Bahlibi, (734) 615-4587 or [mrrc@umich.edu](mailto:mrrc@umich.edu).



————— *Issue in Brief Continued from page 2* —————

The majority of women in this study fall into the lowest AIME brackets and have low *individual* lifetime earnings; however these same women have relatively high lifetime *household* earnings. The same is not true for men. Men in the lowest AIME brackets also tend to have very low lifetime household earnings.

*Redistribution at the level of the Individual and the Household*

There is less redistribution among all individuals when individual *and* spouse benefits are taken into account, suggesting that those with high AIMEs benefit disproportionately from spouse and survivor benefits.

When households are categorized according to lifetime household earnings, and spouse and survivor benefits are accounted for, the extent of redistribution from households with high lifetime earnings to those with low earnings is reduced by half.

*Redistribution when Households are Classified by Earning Capacity*

When households are grouped according to the potential household income, or earnings during years when both spouses were engaged in substantial work, there is *very little* redistribution from families with high to low earnings capacity. The remaining redistribution, however, goes primarily to families in the lowest decile and contributes significantly to their benefits.

Most of the redistribution based upon potential household income occurs within AIME groupings. The likely transfer is from families with two earners to families with about the same combined earning power but in which only one spouse is a lifetime worker.

**Conclusion**

In this cohort of individuals nearing retirement, the current Social Security benefit formula clearly redistributes individual benefits from individual taxes when examined at the level of the individual. Much of the redistribution at the individual level is from men to women. The extent of redistribution is halved, however, when benefits and taxes for both spouses are analyzed at the level of the household. When households are grouped by their potential earnings, there is very little redistribution from high earning to low earning households. The current policy effectively subsidizes households with a spouse who, although working at least ten years to qualify for benefits, remains home for many years rather than working in the market.

It is important to remember that the results presented in this paper pertain only to a single cohort, those born from 1931 to 1941. Further investigation of more recent cohorts is needed to see if these findings are generalizable. Nonetheless, it is clear that the common perception that a great deal of redistribution from the rich to the poor is accomplished by the progressive social security benefit formula is inaccurate.

It is often argued that privatization would undermine the redistribution fostered by the progressive social security benefit formula. Our findings suggest that for the cohort of Americans nearing retirement, there is actually very little redistribution of social security benefits from the rich to the poor. Thus, introduction of a system of privatized accounts that ignores issues of redistribution would have no major effect on the distribution of social security benefits among households with different earnings capacities.

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## 2nd Annual Retirement Research Consortium Conference May 17-18, 2000 Washington, DC

The second annual conference of the Social Security Retirement Research Consortium was held at the National Press Club in Washington, D.C. on May 17 and 18, 2000. The one and a half day conference, entitled "The Outlook for Retirement Income," was planned and arranged this year by the Michigan Retirement Research Center (MRRC) in conjunction with the Social Security Administration (SSA) and the other consortium center, the Retirement Research Center at Boston College (CRR).

With over 150 researchers, policy makers, and federal officials in attendance, researchers from each of the two consortium centers presented papers on current projects, all of which are fully funded by SSA. The paper sessions were chaired by Gary Burtless of the Brookings Institution, Angela O'Rand of Duke University, Cori E. Uccello of The Urban Institute, Peter Orszag of Sebago Associates, Paul Van de Water of SSA, Gene Steuerle of The Urban Institute, Mike Hurd of RAND, and Sylvester Schieber of Watson Wyatt & Associates. The topics covered in the paper sessions included the effects of spousal factors on retirement decisions, women's outcomes in retirement, responses to social security and pension retirement incentives, the extent of progressivity of social security now and in the future, an examination of the evidence that 401(k) plans are used for retirement savings, the retirement behavior and income of younger retirees, and the future of pension systems.

Introductory remarks were made by Lee Lillard, Director of the MRRC, Alicia Munnell, Director of the CRR, and Jane L. Ross, Deputy Commissioner for Policy at SSA. William A. Halter, Deputy Commissioner of SSA and Kenneth Apfel, Commissioner of the SSA, offered closing remarks. Papers presented at the conference are available on the MRRC website <http://www.mrrc.isr.umich.edu>.

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## Mark your Calendars for the 3rd Annual Retirement Research Consortium Conference

May 17-18, 2001  
National Press Club  
Washington, DC



Information about this conference can  
be obtained by contacting

Center for Retirement Research  
Boston College  
Fulton Hall 550  
140 Commonwealth Avenue  
Chestnut Hill, MA 02467-3808  
(617) 552-1762  
(617) 552-1750 Fax  
[ccr@bc.edu](mailto:ccr@bc.edu)

The 3rd Annual Conference is being sponsored by the  
Center for Retirement Research at Boston College



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