The relative economic status of the aged

They were gone. They had passed out of his life, and he faced the last bitter hour alone. No. The snow crunched beneath a moccasin; a man stood beside him; upon his head a hand rested gently. His son was good to do this thing. He remembered other old men whose sons had not waited after the tribe.

*The Law of Life*, Jack London¹

*A family must be whole, faithfully keeping the descent line by having sons to feed the old and the dead, who in turn look after the family.*

*The Woman Warrior*, Maxine Hong Kingston²

Among animals the human being is unique in living past his usefulness, and different societies have devised widely different means for dealing with their superannuated members. At one extreme have been the nomadic tribes, who abandoned the old to freeze or starve when they could no longer keep up with the rest of the group. Kookoosh, in the Jack London story, feels that his son has done his filial duty by saying a last goodbye and leaving a pile of firewood to stave off the wolves and cold for a time. At the other extreme were the Chinese families who, at least until recently, put the needs of their most ancient members first. It is hard to say where, on this continuum between abandonment and ancestor worship, the United States stands in its treatment of its older citizens, but researchers at the Institute for Research on Poverty can say this much about their status: the aged are now, on average, no more likely to be poor than the nonaged. This despite the fact that fewer of them work after age 65, despite the fact that medical costs have risen faster than any other item in the Consumer Price Index, and despite the fact that the proportion of the aged in the population has grown and is continuing to grow.

**Measuring the relative well-being of the aged**

Sheldon Danziger, Jacques van der Gaag, Eugene Smolensky, and Michael K. Taussig, in their paper “Implications of the Relative Economic Status of the Elderly” (see box, p. 13), have evaluated the economic status of the aged relative
to the nonaged, taking into account not only money income but a number of other factors that influence relative well-being: their durable assets, the tax laws, the size and composition of their families. The impact of these factors, discussed below, is presented in Table 1.

Money income

Census Bureau data show that the mean money income for all families and unrelated individuals in 1980 was $19,500. The mean money income of households headed by persons 65 and over was $12,226, or about 63 percent of the average. Although in terms of money income, the aged fall far short of the population as a whole, their status is rapidly improving. In 1966 the average money income of the aged was only 49 percent of that for all families. Between 1966 and 1981 the decline in poverty of this group—as measured by their money income—was greater than for all persons, and much greater than that of households headed by women. But money income alone does not accurately reflect economic status.

Durable assets

The aged are more likely than their younger counterparts to own their own homes and other durables. Using data from the Consumer Expenditure Survey of the Department of Labor for 1973, and combining them with data from the Inventory of Consumer Durables, Danziger, van der Gaag, Smolensky, and Taussig estimated the service flows from durables (that is, the contribution the use of a durable made to the Consumer Expenditure Survey of the Department of Labor for 1973, and combining them with data from the Inventory of Consumer Durables, Danziger, van der Gaag, Smolensky, and Taussig estimated the service flows from durables (that is, the contribution the use of a durable made to a family's income in the course of the year—the amount, for example, not spent for rent by a family owning their home). These amounts were added to the reported money incomes of the two groups (aged and nonaged) for 1973, with the result that the mean income of those 65 and older for that year was raised from 48.6 percent of the income of the nonelderly to 52.2 percent.

Tax advantages

The federal personal income tax offers a number of advantages for persons 65 and over. There is no tax at all on Social Security and Railroad Retirement pensions. Personal exemptions for the aged are doubled ($2000 rather than the standard $1000), and a special retirement tax credit reduces the tax of the aged whose total incomes are below a given level. State income and local property taxes also offer advantages to the old. Adjusting for taxes paid increases the mean income of the elderly to 56.2 percent of the mean for the nonelderly.

Household size and composition

Household size varies with age. Households in the prime age group (35–54) contain twice as many persons on average as households headed by those 65 and older. Obviously a household consisting of four persons requires more income than a household of two to achieve the same living standard. Furthermore, income required to maintain a given standard of living varies with household composition. Van der Gaag and Smolensky used consumption data to construct constant utility equivalence scales that equate the well-being of households of differing composition and size. They found that aged couples and women need less money to obtain the same standard of living as a household headed by a nonaged man. Why should a man require more money than a woman, or a young couple more than an elderly couple, at an equivalent standard of living? Surely any difference has to do with the austerity and efficiency of those who manage on less, rather than a difference in needs. But the difference does exist in the data. Though one can assume that the difference between men and women will gradually disappear as their domestic and work lives become more similar, that is not the case for the difference between the aged and nonaged. As long as we can expect economic growth, the difference between the aged and nonaged will persist, because the aged will have adapted to smaller incomes.

Danziger, van der Gaag, Smolensky, and Taussig found that using the equivalence scales to account for differences in household size and composition raises the relative well-being of the aged from 56.2 percent of that of the rest of society to 85.3 percent. This is the largest single adjustment to the relative well-being of the aged.

<table>
<thead>
<tr>
<th>Table 1</th>
<th>Relative Economic Status of the Elderly, 1973: Adjustments to Money Income</th>
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</thead>
<tbody>
<tr>
<td>Income Concept/Weighting Concept for Recipient Units</td>
<td>Relative Economic Status of Elderly* (%</td>
</tr>
<tr>
<td>Household Weights</td>
<td>1. Reported money income 48.6%</td>
</tr>
<tr>
<td></td>
<td>2. Adjusted for durables 52.2%</td>
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<td>3. Less direct taxes 56.2</td>
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<td></td>
<td>4. Adjusted for household size and composition 85.3</td>
</tr>
<tr>
<td>Person Weights</td>
<td>5. Each person counted once instead of each household 88.0</td>
</tr>
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<td></td>
<td>6. Adjusted for classification of persons by their own age 90.0</td>
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<tr>
<td></td>
<td>7. Total 90.0</td>
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</tbody>
</table>


*Defined as the mean value of the income concept for the elderly divided by the mean for the nonelderly.

Note: The adjustments are cumulative. For example, the number in line 4 is based on adjusting reported cash income of households for durables, after subtracting taxes paid and dividing by the equivalence scales.
Household income weighted by number of persons in the household

The calculations up to this point have used households as the unit of observation. Thus each household is counted once, regardless of whether it contains one person or ten. To address this problem, they adopt an approach that gives equal weight to each person. This weighting procedure can be applied to any income concept. The authors apply it to income divided by the equivalence scale. This procedure further raises the economic status of the older population, from 85.3 percent of the nonaged to 88.0 percent.

Classification by age of person instead of age of head

Thirteen percent of the aged live in households without any aged members. At the same time, 2.75 percent of the nonaged live in households headed by the aged. When the assumption is maintained that all persons in a household share equally in total household income, the reclassification of persons according to their own age rather than the age of the household head raises the relative well-being of the aged an additional 2 percentage points.

Further adjustments

These adjustments to 1973 data raise the relative income of the aged to 90 percent of that of the rest of the population. Although more recent data for replicating these adjustments are not available, we can infer how this ratio may have changed in the past ten years. In 1973 Social Security benefits were not yet indexed to the cost of living, and the Supplemental Security Income (SSI) program had not yet gone into effect. These two laws—but chiefly the indexing of Social Security—are responsible for most of the increase in the money income of the elderly since 1973, from .53 of that of all families to .64 in 1981. Yet even these additions to cash programs do not give the whole picture. The aged also receive a disproportionate share of certain government in-kind transfers: Medicare, Medicaid, and Food Stamps. The aged have been found to understate the size of their money incomes in response to Census surveys more than do the rest of society. And there are many community subsidies and services for those 65 and over, such as Independent Living, Meals on Wheels, Visiting Nurses, day care programs, and reductions in bus fares and ticket prices. (The number of community services for the elderly keeps growing in an attempt to forestall the much more expensive alternative—nursing homes.) Thus it can be safely said that today the aged are at least as well off economically as the rest of us.

Savings of the aged

Further confirmation of the relative well-being of the aged has been found in evidence that casts doubt on the Life-Cycle Hypothesis of Consumption. It has been an assumption of consumption theory that people save during their working years and dissave during retirement in order to maintain, more or less, their previous standard of living. However, in examining microdata on the incomes and consumption levels of the old relative to the not-yet-old, Danziger and his colleagues found that "the elderly not only do not dissave to finance their consumption during retirement, they spend less on consumption goods and services (save significantly more) than the nonelderly at all levels of income. Moreover, the oldest of the elderly save the most at given levels of income." This finding confirms earlier studies by Institute researchers.

A number of hypotheses have been put forward to explain this finding, so at odds with the expectations of some theorists. It may be that those households of the aged that turn up in studies are the unrepresentative survivors of a much larger group, those who failed to save, or failed to save enough, and therefore no longer maintain separate households, living either with relatives or in nursing homes. Another suggested explanation is that the aged are more efficient consumers than other groups: because they have the time, they can shop more carefully. A somewhat contradictory explanation is that they haven't the mobility and health required either to purchase or to enjoy consumer goods and services. Or it may not be the lack of mobility and health that keeps them from purchasing. They may have detached themselves from the material world, such that their wants are few. Or their saving behavior may be the result of a deeply felt insecurity: They have, after all,
Postdoctoral Funding Opportunity

Funds were obligated to the Institute for Research on Poverty in the Omnibus Funding Bill passed by Congress in December 1982. As a result, IRP in association with the Office of the Assistant Secretary for Planning and Evaluation at the Department of Health and Human Services is sponsoring a Small Grants for Visitors Program for social scientists doing empirical research on a variety of poverty-related topics, including trends in economic status and the efficiency and equity effects of income transfer policies for the nonaged. The program will run from July 1, 1983, to December 31, 1984. Further information can be obtained by writing to Elizabeth Evanson, Institute for Research on Poverty, 3412 Social Science Building, University of Wisconsin, Madison, WI 53706.

watched their savings eroded by inflation, they cannot predict how long they will live, and most of them do not relish the prospect of becoming burdens on their families or on the state. Aged couples have an additional anxiety that, should one of them require more care than can be provided by an aged spouse at home, and therefore have to be put in a nursing home, the other spouse will quickly be reduced to penury. (Nursing home costs are very high and long-term stays are not covered by Medicare, Medicaid will cover bills only for those with very low incomes and virtually no assets.) But whatever the explanation of why the aged continue to save—whether because they feel they have more than they need, or because they are insecure—the fact remains that if they didn’t have the money to save, they would not be savers.

Transfers to the aged

To a great extent, the aged owe their relative well-being to government transfers. Based on income measures, their relative mean economic status is raised by about 50 percent by transfers, and transfers reduce inequality among them by 30 percent.6 The transfers that most affect the well-being of the aged are Social Security, Medicare, Medicaid, Supplemental Security Income, and Food Stamps. Each is briefly discussed below.

Social Security

In 1935 there was no OASI. Income support for the aged was provided through their own earnings or those of their families, savings for retirement, limited private and public employee pensions, state-administered old-age assistance programs, and private charities. In that year of deep depression and high unemployment the call for political action to provide an adequate income maintenance program for the aged was overwhelming. . . . The final outcome was a compulsory, contributory insurance program containing both insurance and redistributive features.7

Social Security was enormously popular and grew rapidly. Originally designed to cover only workers who paid into the system, it was expanded in 1939 to pay benefits to dependents and survivors of these workers. Benefits were raised eight times between 1950 and 1971, as the program expanded, bringing more and more workers in until it now covers 88.5 percent of the work force. In 1972 benefits were increased 20 percent and the automatic cost of living adjustment (COLA) was instituted, tying benefits to the Consumer Price Index beginning in 1974. Social Security (including Medicare) is the largest single item in the government budget and comprises 40 percent of all government spending on social welfare.

In large part, Social Security was popular because all participants received more in benefits than they paid in payroll taxes or could have earned by investing the amount of the taxes in the private market. A major reason for the discrepancy between benefits and contributions was that there were many more people paying into the system than drawing benefits. According to Richard Burkhauser and Jennifer Warlick:

In 1972 retired individuals and couples received approximately $27.1 billion in OASI benefits. Had their benefits equaled the fair annuity value of their lifetime contributions this sum would have been reduced to $7.4 billion. The remaining $19.7 billion, or 73 percent of reported benefits, represents a large intergenerational transfer from workers to the retired population. . . . The tradition of large intergenerational transfers helps explain the strong support of the system by previous generations of taxpayers. Similarly, the fact that the relative size of the transfers is diminishing may explain the growing lack of confidence in and discontent with OASI voiced by current taxpayers.8

A maturing system, longer life spans, the fall in the birth-rate, and shorter work lives require that we either reduce benefits in the Social Security system or be willing to spend a much higher proportion of the GNP on the aged than we have in the past. In 1960 the equivalent of 2 percent of the GNP was distributed to the retired via Social Security; in 1970 it was nearly 4 percent; by 1980 it was 6 percent.9

Medicare

Medicare was enacted in 1965 to provide hospital insurance and supplementary medical insurance to all aged persons entitled to Social Security benefits, as well as to some other groups, such as the disabled. Obviously everyone receiving Social Security in 1965 received windfall benefits from this program, since they had not contributed to it through payroll taxes. Participants do pay a certain amount in deductibles, coinsurance, and premiums. Over 26 million people

(continued on p. II)
tive to those from above-median-income families varied with race and sex. The ratios went down among whites and men, but went up for blacks and women. Because the first two groups are larger than the second two, the overall ratios went down by a small amount. The decline again leads to a somewhat gloomy conclusion, namely, that educational aspirations have not changed to any significant extent for youths from lower-income families.

These findings have proved controversial. Critics have pointed out that college enrollment figures for the early 1970s are inflated because young men in those years chose college rather than military service in Vietnam, whereas the figures for the late 1970s may be depressed because deteriorating economic conditions discouraged college attendance. Moreover, the author himself offers two qualifications to the pessimism of his conclusion. First, he speculates that student aid may not have been sufficiently generous to attract into college additional young people from lower-income groups. The implication that could be drawn from that point (Hansen does not explicitly do so) is that the programs deserve to be expanded, not abandoned. Second, Hansen states that perhaps, if no financial aid had been available, enrollment rates would have declined more than they did. If so, the programs could be regarded as a success in the sense that without them fewer low-income students would have attended college. Finally, since they did provide aid to low-income students, Hansen concludes that they operated as transfers rather than as human investment programs.

The two studies that have been described here share the quality of going against what many have accepted as common knowledge: that rates of return to education have gone down; that federal student aid programs have expanded post-secondary educational opportunities for young people from poorer families. And they both call for economists to refine their tools of analysis, especially their measures of the effects of education—on the country's economic growth, on personal well-being, and on the well-being of the nation.

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1Robert Mare, "Sources of Educational Growth in America," Focus, 3:2 (Winter 1978–79), 5–6, 12.

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are now enrolled in the program, and the cost continues to mount, not only because of the increasing number of aged, but because the cost of medical care has risen so fast. In 1967 Medicare expenditures were $3 billion a year; in 1981 they were over $37 billion. According to Karen Davis, the program has greatly increased the care available to the elderly and has been a major source of relief of the burden of excessive bills.10

**Medicaid**

At the same time that Medicare was enacted for Social Security beneficiaries, Medicaid, an income-tested program, was established for the needy. Because the aged are the group most likely to be in need of prolonged and expensive medical care, this program aids them more than other groups. About 70 percent of all Medicaid expenditures go for hospital and nursing-home care. In 1981 the expenses for this program, shared by the federal government and the states, came to $27.6 billion, and it served 22.1 million people.

**SSI**

Supplemental Security Income is an inflation-indexed negative income tax for the aged, blind, and disabled, which in 1974 replaced state-run Old Age Assistance and programs for the aged, blind, and disabled. It provides a national uniform cash benefit to all the aged whose income and assets are below a certain amount, with benefits reduced as income rises. States have the option to supplement the benefit level. In 1981 expenditures for SSI were estimated at $8.5 billion.

Oddly enough it has been estimated that only 50 percent of those eligible for SSI are enrolled. Jennifer Warlick found that although the amount of the benefit is positively related to the decision to participate in SSI, many people eligible for large benefits do not participate. The reasons why they do not apply are not easy to pinpoint, and therefore will not be easy to rectify.11

**Food Stamps**

Food Stamps is an inflation-indexed negative income tax which provides benefits in kind for low-income households. Forty-one percent of food stamp recipients are either receiving OASDI or SSI. This includes the elderly, survivors, and the disabled. The budgetary cost of Food Stamps was estimated to be $9.7 billion in 1981.

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**Comparing the aged poor to the nonaged poor**

Mean incomes include both extremes, the very wealthy and the very poor. No category of citizens is more diverse than the aged, who have in common primarily their longevity.
They include the couple in their sixties playing tennis outside their retirement condominium in the Sunbelt as well as the senile nonagenarian barricaded in an unheated tenement in the Snowbelt. Those who are both old and poor have been thought to be much worse off than those who are merely poor, since they cannot work and are more likely to need medical care. But since all the aged poor are now eligible for SSI and Medicaid, they have the means—if not to live luxuriously—at least to scrape along. Not so the nonaged poor. According to Danziger and Robert Plotnick, "The aged, who constituted 48 percent of all pretransfer poor households [in 1978] received 62 percent of the pre-transfer poor's total cash transfers. . . . Almost all the elderly [poor] received enough to escape poverty." By comparison, all categories of the nonaged (white, black, Hispanic, male, and female) were less likely to receive transfers, and if they received them, were less likely to be removed from poverty by them. With SSI nationally available, and Medicaid available—though at differing levels of generosity—in all states except Arizona, what is surprising to these researchers is not that the aged are so well off, but that there should be any aged poor at all.

The size of the aged population

In the United States in 1980 there were 24,928,000 persons aged 65 and older. In 2000 there will be 31,822,000 persons in that age group. The number of extremely old persons (80 years and older) will increase 56.1 percent, and will constitute 24.4 percent of the aged. The reasons for this dramatic increase are simple enough. More and more people live to old age, and the life span has been extended by medical technology and health care. The World War II baby boom that created ripples in the education system and waves in the job market will create a tidal wave when it hits retirement age after 2010. No wonder there is worry that the working population will be overburdened by taxes to support the aged.

The working population is already being called upon to increase traditional types of support. Middle-aged couples are now likely to have not one or two but four aged parents to look after. Furthermore the fact that aged parents are better off financially than ever before means that they are less likely than in the past to share a household with their middle-aged children. This is a mixed blessing. The services they require when living alone, the shopping, laundry, meals, transportation, and occasional nursing care, make their financial independence costly to their families at a time when "housewives," who used to do these domestic chores for the aged, are increasingly scarce. And the inevitable crises in their lives, brought on by illness and death, mean that more than one household is disrupted.

Irwin Garfinkel and Karen Holden are more sanguine about the future. In their examination of the Social Security system, they point out that although the aged in the United States are increasing in number, there are fewer children, with the result that the ratio of dependents (those under 20 and over 65) to the rest of the population is unlikely to change over the next fifty years. According to them, "there will be more grandparents but fewer children, more dollars spent on retirement benefits and nursing homes but fewer dollars spent on schools and day care."

Fiscal retrenchment and the aged

Data show that the aged are no worse off economically than the rest of the population and that they are disproportionately aided by social programs. They will suffer less from reductions in programs directed at them than will some other groups—such as women who head households and nonaged minorities. Furthermore, the aged are increasing, both in number and in age, raising doubts about the extent to which they should be supported by increasing transfers from the working population. Should their share of the GNP be reduced? The answer to that question is not readily apparent. In a paper attempting to evaluate some of the benefits (such as increased security and reduced poverty) and costs (such as collection, administration, compliance costs, and the loss of work time) of our retirement policy, Robert Lampman writes:

"The aged, who constituted 48 percent of all pretransfer poor households [in 1978] received 62 percent of the pre-transfer poor's total cash transfers. . . . Almost all the elderly [poor] received enough to escape poverty." By comparison, all categories of the nonaged (white, black, Hispanic, male, and female) were less likely to receive transfers, and if they received them, were less likely to be removed from poverty by them. With SSI nationally available, and Medicaid available—though at differing levels of generosity—in all states except Arizona, what is surprising to these researchers is not that the aged are so well off, but that there should be any aged poor at all.

There are, of course, enormous difficulties in measuring the several social benefits that may have been achieved by the recent expansion of organized cash transfers [retirement transfers]. To do so requires that we perform the mental experiment of imagining what the world would have been like without that expansion. In any event there have been few attempts to quantify these benefits. But there is also the problem of weighting the achievement of the several goals. Here we find considerable disagreement even among experts in evaluation of retirement programs, who tend to start from conflicting value sets or mentalities. A similar procedure is called for in evaluating the social costs that may have been incurred by the expansion of cash transfers.

Implications for Social Security reform

In one respect the Greenspan Commission reached a consensus: "The National Commission has agreed that there is a financing problem for the OASDI program for both the short-run, 1983–89. . . . and the long range, 1983–2056. . . . and that action should be taken to strengthen the financial status of the program." Social Security will be expected to continue to operate on insurance principles, i.e., to pay its own way. Disagreement seems to have arisen in deciding whether to make the reductions in benefits or increases in taxes: whom to hurt and how much.

In an attempt to compare the financial and equity effect of two widely discussed Social Security reforms, Danziger and his colleagues have simulated the effects of two changes, holding the savings for the first year constant: (i) subjecting
one-half of benefits to the federal income tax, and (2) reducing the cost-of-living adjustment (COLA). They found that the financial effects of the two changes would vary greatly as time went on. The reduction in COLA would have cumulative effects each subsequent year's cost-of-living adjustment would be applied to a permanently lower base. This would escalate savings relative to a tax on benefits. In terms of equity, however, the tax on benefits would be superior. An income tax applied to half of benefits would apply only to the top half of all consumer units receiving Social Security. It would be progressive with respect to Social Security benefits (but not with respect to total income). The cutback in COLA, on the other hand, would be a proportional tax on benefits, and hence would be regressive with respect to income.

Other proposals supported by the Greenspan Commission include expanding the tax base by covering all new federal civil service employees and raising the taxes current workers pay to support the aged. Their recommended solution is a compromise: reducing the growth in benefits while increasing taxes.

Gray power

The aged are a potent political force. Not only are their numbers great in proportion to the rest of the population, they also vote. To a great extent their self-interest is also ours, since most of us, though we may escape the hardship of belonging to some other minority, do anticipate, barring unforeseen circumstances, to be aged one day. It will not be an easy matter to redistribute shrinking government transfers in such a way that the aged get less while those in greater need receive a larger share. It may not even be wise. Other nations—such as West Germany—contribute a greater proportion of their GNP to the aged via cash transfers than we do (12 percent as opposed to 7.6 in 1978). The extent to which we shall continue to provide for the economic well-being of our older citizens will depend upon the relative prosperity of the nation as a whole and upon the political process.

Selected papers


3 Jacques van der Gaag and Eugene Smolensky, "True Household Equivalence Scales and Characteristics of the Poor in the United States" (see box).
4 Danziger, van der Gaag, Smolensky, and Taussig, "Life-Cycle Hypothesis" (see box), pp. 2-3.
5 See Focus 6:1, "From Person to Person: Studies of Nongovernmental Transfers."
6 Danziger, van der Gaag, Smolensky, and Taussig, "Income Transfers and the Economic Status of the Elderly" (see box), pp. 21-23.