

Labor Supply and the Pension Contribution-Benefit Link

Cormac O'Dea (with Eric French, Attila Lindner & Tom Zawisza)

Abstract:

We estimate the labor supply response among workers far from retirement age to a reform that switched the Polish pension system from a Defined Benefit (DB) to a Notional Defined Contribution (NDC) scheme. Central to this reform was a change the link between current pension contributions and future pension benefits. Only those born after December 31st 1948 were affected, creating a sharp cohort-based discontinuity in the contribution-benefit link for individuals in their 50s. Using administrative data on the universe of Polish taxpayers, we examine labor supply responses to the reform at ages 51-54, around 11-15 years before the normal retirement age. In line with the change in incentives, we find that the employment rate decreased by 2% in response to the policy change, which is consistent with an extensive margin elasticity of 0.33. These responses are driven by regions where the incentives had changed the most. Our results imply that changing the contribution-benefit link of public pensions can alleviate the labor supply distortions caused by social security contributions.