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**SOCIAL SECURITY AND RETIREMENT DECISION:
A POSITIVE AND NORMATIVE APPROACH**

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Abstract

Social insurance for the elderly is judged responsible for the widely observed trend towards early retirement. In a world of laissez-faire or in a first-best setting, there would be no such trend. However, when first-best instruments are not available, because health and productivity are not observable, the optimal social insurance policy may imply a distortion on the retirement decision. The main point we make is that while there is no doubt that retirement systems induce an excessive bias towards early in many countries, a complete elimination of this bias (i.e., a switch to an actuarially fair system) is not the right answer. This is so and for two reasons. First, some distortions are second-best optimal. This is the normative argument. Second, and on the positive side, the elimination of the bias might be problematic from a political perspective. Depending on the political process, it may either not be feasible or alternatively it may tend to undermine the political support for the pension system itself.

Keywords: social security, early retirement, optimal income taxation, majority voting.

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