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## Abstract

We estimate a model of savings for retired couples and singles who face longevity and medical expense risks, and in which couples can leave bequests both when the first and last spouse dies. We show that saving motives vary by marital status, permanent income, and age. We find that most households save more for medical expenses than for bequests, but that richer households and couples, who hold most of the wealth, save more for bequests. As a result, bequest motives are a key determinant of aggregate retirement wealth.

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# 1 Introduction

This paper studies the saving behavior of retired couples and singles, including the transition of couples to singles due to spousal death. It documents new facts about wealth and medical expenses during retirement, and about bequests distributed to both surviving spouses and other heirs. It then estimates a structural life cycle model of saving and bequeathing that matches many important aspects of the data. Finally, it uses the model to evaluate the determinants of savings during retirement, both at the household and at the aggregate level.

In terms of new facts, we show that current couples decumulate their wealth slowly, but that when the first spouse dies, net worth drops sharply (by \$160,000 on average). Although some of this drop is explained by end-of-life medical expenses, most of it is due to transfers to non-spousal heirs. These “side” bequests are evidence of bequest motives towards recipients other than the surviving spouse. Once single, surviving households continue to run down their wealth slowly, but at a quicker pace than when they were married. By the time the second spouse dies, much of the couples’ wealth has vanished.

Our model of retiree saving incorporates heterogeneity in permanent income, life expectancy, and medical expenses, and accounts for the large jump in medical spending that typically precedes a death. Bequests are potentially left when the first and the last member of a couple dies. In the former case, the estate is optimally split between the surviving spouse and other heirs.

We estimate the model using the Method of Simulated Moments (MSM) and Assets and Health Dynamics of the Oldest Old (AHEAD) data. It matches well both Medicaid reciprocity and wealth holdings (which we target) and changes in out-of-pocket medical expenses and wealth around the time of death (which we do not target).

Our model delivers several novel findings. First, most households (53%) save more to self-insure against medical expenses than to leave bequests. However, because these households hold relatively little wealth, the aggregate effect of eliminating medical expenses is small (mean wealth drops by 3.1%). In contrast, removing bequest motives reduces aggregate wealth by nearly five times as much (mean wealth drops by 14.8%). This is because we estimate bequests to be stronger for couples and richer singles, who hold most of the wealth. Hence, although medical spending is more important than leaving bequests for most households, bequest motives are more important for aggregate saving. We also find that 44% of aggregate bequests are voluntary, again implying a large role for bequest motives at the aggregate level.

Second, the relative importance of bequest motives and medical expenses varies

by marital status. While most singles (62%) save more for medical expenses than for bequests, most couples (69%) save more for bequests. This is because we estimate that bequests are luxury goods, that couples value both side and terminal bequests, and that couples are typically richer than singles.

Third, medical expenses and bequest motives interact in powerful ways. While eliminating bequest motives and medical spending in isolation causes aggregate wealth to fall by 14.8% and 3.1%, respectively, eliminating both motives leads aggregate wealth to fall by 42.5%. This interaction arises because eliminating medical spending still leaves households with bequest motives, while eliminating bequest motives still leaves them needing to save for medical expenses. When both motives are present, wealth can satisfy the two needs simultaneously (Dynan et al., 2002), and when both motives are absent, households have little reason to save. This result is important because much of the previous literature has studied precautionary saving for medical expenses in the absence of a bequest motive. Given that we provide robust evidence that bequest motives are present, the strength of their interaction makes it essential to model the two saving motives together.

The main innovations of our paper are twofold. First, we model both couples and singles. Given that couples make up roughly half of the retiree population and hold substantial wealth, ignoring them would leave us uninformed about many important aspects of retiree saving, including the aggregate response to policy reforms. Second, we better capture household behavior upon the death of the first spouse. Because we find that wealth drops at the time of the first spouse’s death, in large part because they leave “side bequests” to heirs other than their surviving spouse, we model this additional bequest motive and estimate its strength. We also better model household behavior by allowing for the pervasive income- and wealth-based heterogeneity that we estimate.

The rest of the paper is organized as follows. Section 2 summarizes the findings of key related papers and motivates our main modeling choices. Section 3 introduces our data and displays the key facts that we seek to understand. Section 4 presents our model, and Section 5 details our estimation procedure. Section 6 displays important features of the data affecting households’ saving decisions and evaluates our model fit. To build additional trust in our model’s predictions, Section 7 evaluates its performance in terms of important aspects of the data that we do not match at the estimation stage. Section 8 evaluates the saving determinants for singles and couples and in the aggregate, and Section 9 concludes.

## 2 Related literature and modeling choices

The goal of this paper is to document and explain the differences in the saving behavior of couples and singles and their contribution to aggregate retirement savings. Although much of the structural work on retiree saving has focused on singles, a few papers, including Braun et al. (2017) and Nakajima and Telyukova (2020), include couples. De Nardi et al. (2016b) provide a detailed literature review.

Our paper builds on these contributions by considering what happens when a spouse dies. Like Poterba et al. (2011), we find that net worth falls when households lose a spouse. We document that the distribution of wealth to heirs other than the surviving spouse is crucial to explain this drop. These facts motivate a novel feature of our model, which is that we allow households to leave bequests to non-spousal heirs when the first spouse dies.

From a theoretical standpoint, the death of a spouse is a natural time to distribute resources because it resolves uncertainty about the time of death and medical expenses of the deceased. Moreover, in a collective model of the household in which each spouse cares about their own consumption and the bequests they leave to non-spousal heirs when they die, bequests to people other than the surviving spouse arise naturally when the first spouse dies. We highlight this point in Appendix A.1, where we also show that given our data, this collective model is observationally equivalent to our unitary model with side bequests.

In our model, bequests to non-spousal heirs also occur when the final member of a household dies. The desire to leave such bequests has received considerable attention as a potential explanation why households retain high levels of wealth at very old ages, as in Dynan et al. (2002), Ameriks et al. (2011, 2020) and Lockwood (2018). De Nardi et al. (2016a) show that this kind of bequest motive helps their model simultaneously fit the wealth and Medicaid reciprocity profiles of singles.

Besides modeling household demographic transitions and bequest motives toward the surviving spouse and other heirs, we take into account health and medical expense risk, social insurance for couples and singles, and heterogeneity in life expectancy by PI and marital status. These features are important because households face potentially large out-of-pocket medical and nursing home expenses (Braun et al. (2017), French and Jones (2004, 2011), Palumbo (1999), Feenberg and Skinner (1994), and Marshall et al. (2010)), which generate precautionary savings (as in Kopecky and Koreshkova (2014), and Laitner et al. (2018)). But these risks are partially insured by means-tested programs such as Medicaid and Supplemental Security Income, which provide strong saving disincentives (Hubbard et al. (1995), and De Nardi et al. (2010)). Finally, previous work has shown that high-income individ-

uals live longer than low-income individuals (Attanasio and Emmerson (2003) and Hong et al. (2015)) and that married people live longer than single people.

Our analysis abstracts from several factors that other papers study in the context of related questions. For instance, we do not explicitly model housing, which is the focus of Nakajima and Telyukova (2017, 2020), Chang and Ko (2021), Barczyk et al. (2022), and McGee (2022). Likewise, while our model of medical spending indirectly captures the way in which informal care and payments from long-term care insurance reduce out-of-pocket medical spending, we do not model the determinants of either factor; papers addressing these topics include Barczyk and Kredler (2018), Lockwood (2018), Mommaerts (2020) and Ko (2022). Additionally, while we extend the previous literature by introducing side bequests, we do not explicitly model inter-vivos transfers. Inter-vivos transfers are substantially smaller than bequests (Hurd et al. (2011), Barczyk et al. (2022)) and accounting for them would make our model considerably more complex. Barczyk et al. (2022) capture inter-vivos transfers by modeling the strategic interactions between parents and children.

We also abstract from issues of intra-household bargaining (see Chiappori and Mazzocco (2017) for a survey) and use a unitary decision-making framework instead. We do so for four main reasons. First, we want to extend the previous singles-only analysis to the simplest model with both couples and singles. Second, very few members of our sample exercise their “outside option” of divorce, meaning issues of commitment are not very important during retirement. Third, in our regression analyses of wealth growth, we find no evidence that the husband’s share of retirement income (a natural proxy for bargaining weights) is an important determinant of wealth trajectories after retirement; this suggests that most retired households have similar internal decision-making protocols. Fourth, Appendix A.1 shows that in a two-period version of our model with collective decision-making under commitment, imposing equal bargaining weights on husbands and wives is a normalization.

## 3 Savings, medical spending, and Medicaid

### 3.1 The AHEAD dataset

We use the AHEAD dataset, which began in 1993/94 with households of non-institutionalized individuals age 70 or older and has surveyed their survivors every two years since. The unit of analysis in our paper is the household, and all of the financial values that we report are measured at the household level. Appendix B describes the details of our sample selection and data work.

Three important decisions are that (i) to abstract from labor supply decisions,

we only consider retired households; (ii) to be consistent with the transitions in the model, we drop household who either get married or divorced during the sample period; and (iii) due to the well-known under-reporting of assets and medical spending in the initial wave, we drop the 1993/94 data.

Our 1996 data include 4,634 households, of whom 1,388 are initially couples and 3,246 are initially singles. This represents 24,274 household-year observations for which at least one household member was alive.

### 3.2 Permanent Income

A contribution of this paper is distinguishing heterogeneity from risks. During retirement, differences in permanent income (PI) capture a large amount of household ex-ante heterogeneity: households with different PI ranks receive different flows of retirement income and face different processes for health, mortality and medical expenses.

To estimate a household's PI, we first sum all of its annuitized income sources (Social Security benefits, defined benefit pension benefits, veterans benefits and annuities).<sup>1</sup> Because there is a roughly monotonic relationship between lifetime earnings and our annuitized income measure, this measure is also a good indicator of income during the working period. We then construct a PI measure comparable across households of different ages and sizes. To do so, we regress annuitized income on a household fixed effect, dummies for household structure, a polynomial in age, and interactions between these variables. These variables jointly explain 72% of the variation in incomes across all years and households, of which 10% of the variation is explained by age and household structure, with the remainder being explained by fixed effects. Our specification thus captures most of the income variation in our data. The rank order of each household's estimated fixed effect provides our measure of its PI. This is a time-invariant measure that follows the household even after one of its members dies. See Appendix C for details.

### 3.3 Savings patterns and their determinants

Our measure of wealth (or net worth) is the sum of all assets less mortgages and other debts.<sup>2</sup> Figure 1 displays median net worth, conditional on birth cohort and

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<sup>1</sup>Since we model means-tested social insurance from SSI and Medicaid explicitly in our model (through a consumption floor), we do not include SSI transfers.

<sup>2</sup>The AHEAD has information on the value of housing and real estate, autos, liquid assets (which include money market accounts, savings accounts, Treasury bills, etc.), individual retirement

PI tercile, for different configurations of couples and singles. We break the data into 4 cohorts containing people who in 1996 were ages 71-76, 77-82, 83-88, and 89-102. For clarity we display data for two cohorts in this picture (Appendix D presents the data profiles for the remaining cohorts, as well as our model fit). To construct these profiles, we calculate the median for each cohort-PI tercile cell, for those alive in each calendar year. The line for each cohort starts at the cohort’s average age in 1996.

“All singles” include those who are divorced, never married, or widowed when first observed in our sample, and those who become widowed over the sample period. Panel (a) displays their median net worth, including the value of bequests left in the period after death. It highlights that the savings of elderly singles depend on their income (which is predetermined at retirement). Individuals with the lowest lifetime incomes reach retirement with little wealth and then run it down. Elderly singles in the middle and top of the income distribution also run down their wealth as they age, but do so slowly, and carry some wealth into very old ages.

“Initial singles” include only those who were single when they first appear in our sample and exclude those who lose their spouse during our sample period, that is, the “new singles”. Because new singles tend to have more wealth than initial singles, and new singles become a larger share of all singles over time, the trajectories of all singles in Panel (a) slope down slightly less than those of initial singles in Panel (b). However, overall the two sets of trajectories are similar.

“Current couples,” include couples who remain intact (and drops them from the sample when they become single). Panel (c) of Figure 1 plots their net worth and reveals several interesting results. First, relative to singles in the same tercile, couples reach retirement with more wealth. Second, the wealth profiles of the lower- and middle-income surviving couples display no decumulation. Third, couples in the top PI tercile increase their net worth until almost age 90.

“Initial couples,” include those who are initially in a couple, but also retain those who subsequently lose a spouse. In that case, we report the wealth of the surviving spouse. Panel (d) of Figure 1 shows that, relative to current couples, initial couples decumulate their wealth more quickly. Some of this decumulation reflects the higher decumulation rates of new singles. Some is due to the loss of wealth that occurs when one of the spouses dies. The remainder is due to sample composition: high-wealth couples live longer, and comprise an increasing share of current couples over time.

To examine the correlates of wealth growth more closely, we regress wealth growth on a rich set of observables, including age, PI, their interaction, household composition (couples or singles), an indicator for being divorced (by 1994) or never married,

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accounts, Keoghs, other defined contribution plan, wealth, stocks, the value of a farm or business, mutual funds, bonds, and other assets.



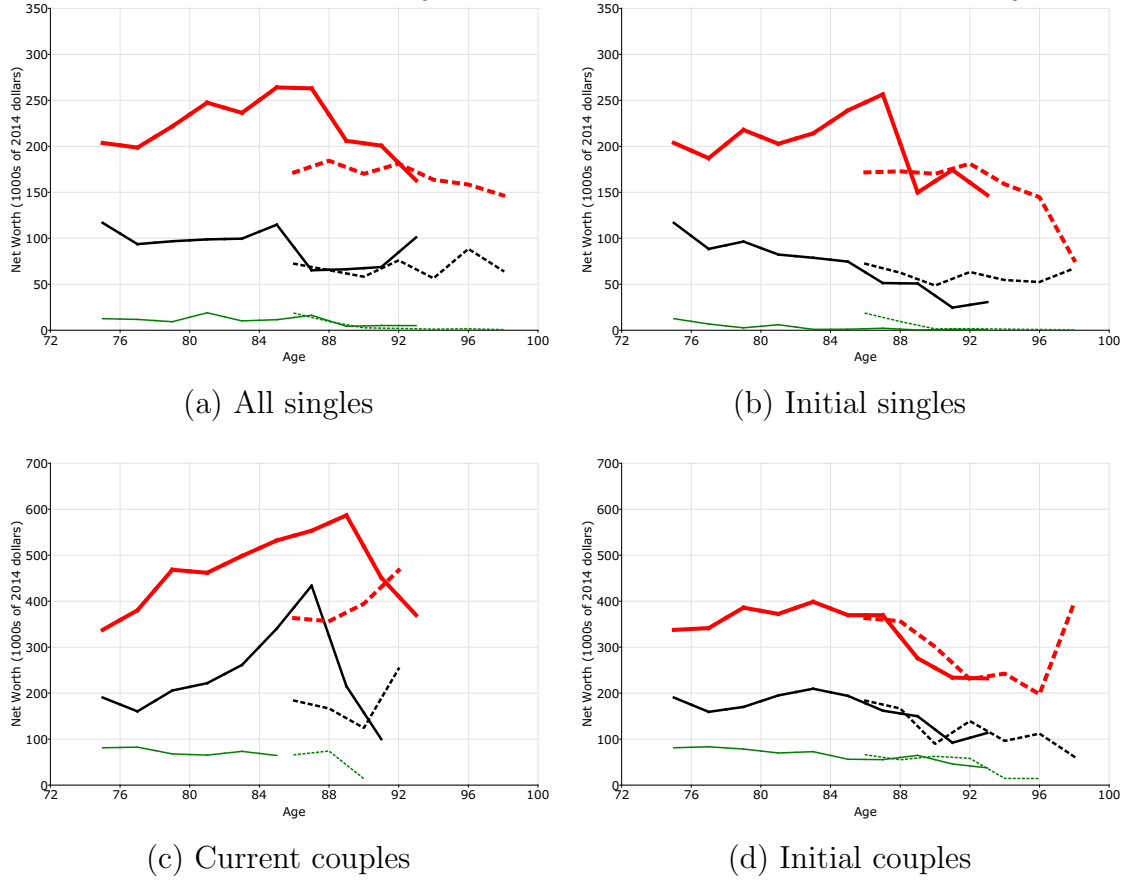


Figure 1: Median wealth by cohort, PI tercile, and age. AHEAD data. Each line represents median wealth for a cohort-PI cell, traced over the time period 1996-2014. Solid lines: cohort ages 71-76 in 1996. Dashed lines: cohort ages 83-88 in 1996. Thicker lines denote higher PI terciles.

the presence and number of children, initial homeownership, the husband's share of total annuitized income for couples, and an indicator for the death of a spouse in a couple. We report both mean and median regression results because theory does not imply that the effects should be constant (or proportional) across the distribution of wealth.

Table 1 reports the most relevant coefficients and their standard errors. It shows that PI and its interaction with age are important determinants of wealth growth. At the mean, couples save more than singles, even after controlling for a rich set of observables.

Table 1: Growth in wealth (in 000s of 2014 dollars) and household characteristics

	Mean	Median
Permanent Income (PI)	260.79*** (106.14)	46.46*** (9.72)
PI $\times$ Age	-3.30*** (1.26)	-0.59*** (0.12)
Couple	13.70* (7.16)	0.74 (1.16)
Divorced or Never Married	4.64 (9.44)	0.05 (0.17)
Any Children	-1.91 (7.29)	0.13 (0.31)
Number of Children	0.71 (1.21)	0.02 (0.03)
Initial Homeowner	-5.83 (5.27)	-2.56*** (0.51)
Husband's Income Share	0.51 (19.21)	2.10 (2.64)
Death of Spouse	-51.06*** (10.82)	-4.89*** (1.74)
Observations	15,502	15,502

*Note:* AHEAD data. Left hand side variable is change in wealth between adjacent waves. All regressions include a second order polynomial in the household head's age and indicator variables for each individual's health status in both waves. Husband's Income Share is the husband's share of Social Security and defined benefit income. Standard errors in parentheses. \*  $p < 0.10$ , \*\*  $p < 0.5$ , \*\*\*  $p < 0.01$ .

In contrast, and consistent with the assumptions that we make in our structural model, those who were divorced when first observed in our data or never married behave similarly to those who were married and then became single. Furthermore, differences in wealth growth between those with and without children, or with different numbers of children, are small and not statistically significant. It is worth noting that this result is consistent with several well-known studies that find little difference in the savings of households with and without children (Hurd, 1989; Kopczuk and Lupton, 2007).

Initial homeownership predicts slower wealth growth (although it is not significant at the mean). We take this surprising result as evidence that the relationship between homeownership and wealth growth is subtle and requires detailed modelling beyond the scope of this paper. Further analysis of homeownership and wealth growth can be found in Nakajima and Telyukova (2017, 2020), Chang and Ko (2021), Barczyk et al. (2022), and McGee (2022).

The husband’s share of annuitized income is commonly used to measure the distribution of bargaining power within a couple (see, for instance, Browning (2000)). The coefficient on this variable is statistically insignificant, which suggests that most retired households have similar internal decision-making protocols.

Finally, wealth drops significantly when a spouse dies. Taking stock, Table 1 suggests there are three important determinants of retiree saving: PI, marital status, and death. These elements will play key roles in our structural model.

### 3.4 Spousal death, wealth, medical spending, and side bequests

Because Table 1 highlights that spousal death is important for saving, we next delve into what happens when couples experience the death of one spouse. To do so, we study the difference in net worth between two sets of couples. The first group consists of couples who lose a spouse. The second group consists of couples who are each similar along multiple dimensions to a couple in the first group (6 years prior to that couple’s spousal death) but do not experience a spousal death around this time period.<sup>3</sup> Our matching analysis accounts for observable initial heterogeneity across couples and thus identifies the impact of death and the declining health that precedes it. Kopczuk (2007) and Kvaerner (2022) use similar methodologies to evaluate the wealth trajectories of those diagnosed with a terminal disease.

We use these data to estimate the following event study specification:

$$a_{i,t} = f_i + \sum_{j=-4}^4 (g_j + d_j D_i) \times 1\{t - T_i = j\} + e_{i,t} \quad (1)$$

where  $a_{i,t}$  denotes the wealth of household  $i$  in calendar year  $t$ , and  $D_i$  indicates whether  $i$  belongs to the group that does not lose a spouse ( $D_i = 0$ ) or to the group that does ( $D_i = 1$ ). We normalize the date of death,  $T_i$ , to occur at year 0 and follow the households for three waves before and two waves after the death. The coefficients

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<sup>3</sup>We match on PI, initial wealth, and age. See Appendix E for details and Jones et al. (2020) for additional outcomes.

of interest are the parameters  $\{d_j\}$ , which show the extent to which wealth rise or fall for households who experience the death of a spouse, relative to households in the matched sample who experience only a placebo death at date  $T_i$ .<sup>4</sup>

Panel (a) of Figure 2 reports our estimated death-related wealth decline (the values of  $d_j$ ). On average, the net worth of households experiencing a death declines by an additional \$160,000 compared to those not experiencing one. While the decline begins up to 6 years in advance of death, a large share of the decline occurs in the final two years. Part of this decline reflects a gradual worsening of health and a related increase in medical expenses. The rest reflects bequests made at the time of death of the first spouse and changes in consumption. The gap between the treatment and control groups continues to widen during the post-death years. This may reflect additional death-related effects, for instance the loss of a spouse’s income.

Some of these wealth declines are explained by high medical expenses prior to death. The AHEAD contains high-quality data on what the household spends out-of-pocket on private insurance premia, drug costs, hospital stays, nursing home care, home health care, doctor visits, dental visits, and outpatient care, including those incurred during the last year of life. To construct our measure of out-of-pocket medical spending, we sum all of these components, along with funeral, other end-of-life expenses, and imputed Medicaid insurance contributions.

Panel (b) of Figure 2 shows that when a member of the household dies, there is a sharp increase in medical expenses: they are \$8,000 larger during each of the two years preceding the death of a spouse, compared with similar couples experiencing no death. Over the 6 years preceding death, the total difference in medical expenses between these two households is about \$22,000. Thus high end-of-life medical expenses can explain  $\frac{22,000}{160,000} = 14\%$  of the average fall in wealth. A similar event study reveals that the spending jump for singles is larger than for couples, totalling almost \$28,000.

If not medical and other end-of-life expenses, what explains the drop in wealth at the time of death of a spouse? When one spouse dies, a family member of the deceased, usually the surviving spouse, is asked how the estate is split between the surviving spouse and other heirs, such as children. The AHEAD data show that most of the wealth is left to the surviving spouse, but that on average \$87,000 is bequeathed to other heirs, transfers which we will refer to as “side bequests”. Hence, the sum of reported non-spousal bequests and medical expenses explains about two-thirds of the observed wealth decrease.

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<sup>4</sup>The coefficients  $g_j$  and  $d_j$  are defined relative to their value 6 years before death (the omitted indicator category). In interpreting the summation, recall that AHEAD interviews occur every other year.

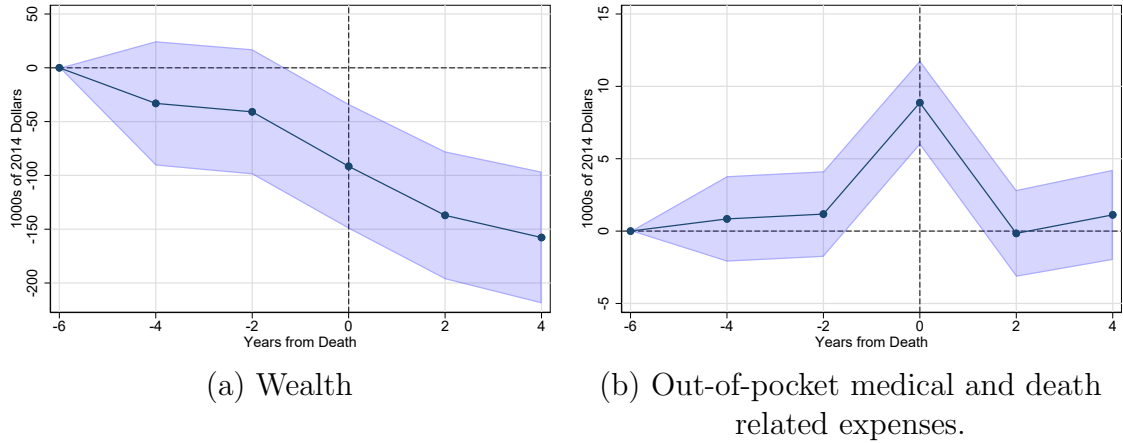


Figure 2: Average changes in wealth (Panel a) and the sum of out-of-pocket medical and death related expenses (Panel b) around the death of a spouse, initial couples. AHEAD/MCBS data. Solid lines: estimates from event study in Equation (1), shaded region: 95% confidence interval. Death dates are centered at year 0.

To the best of our knowledge, these non-spousal side bequests are not well documented, the one exception being Fahle (2023). The top panel of Table 2 shows that side bequests are positive in 30.6% of all spousal deaths, and when positive have a large mean (\$248,300) and make up a large fraction of the estate (42.9%).

Hence, these side bequests are common and large, both in absolute size and as a share of the couples' estates. Given that these transfers are likely intentional, their presence supports the view that bequest motives are important. Although we do not require our estimated structural model to match either the decline in wealth around the death of a spouse or the transfers to other heirs, it does match these aspects of the data well, which helps validate its predictions.

Panel (A) of Table 2 examines whether side bequests differ systematically by the presence or number of children. Contrary to what many expect, those without children are more likely to make non-spousal bequests and there is no strong behavioral relationship with the number of children. This is consistent with many earlier studies (for example, Hurd (1989)) that find no evidence of differences in saving behavior between those who do and do not have children, as well as evidence showing that saving for bequests is important even for those without children (Laitner and Juster (1996)). While Fahle (2023) finds that caregivers are more likely to receive side bequests, he concludes that “a warm-glow motive may be a reasonable characterization of bequest preferences for many decedents.”

Table 2: Bequests at the death of the first spouse by household characteristics

	Share of Sample	Fraction Positive	Distribution when Positive	
			Mean Amount	Share of Estate
All	100%	30.6%	248,300	42.9%
<i>A. By Children</i>				
No Children	6.7%	39.6%	369,700	43.9%
Children	93.3%	30.0%	236,700	42.8%
2+ Children	77.2%	29.8%	231,100	43.2%
<i>B. By Homeownership Status</i>				
Not a Homeowner	22.4%	24.4%	257,900	58.1%
Homeowner	77.6%	32.4%	246,200	39.6%
<i>C. By Age of Death</i>				
Age 72-81	25.9%	26.6%	216,700	37.8%
Age 82-91	56.9%	32.7%	253,200	43.8%
Age 91+	17.2%	29.9%	273,000	46.3%
<i>D. By Permanent Income</i>				
Bottom PI Tercile	18.8%	27.9%	165,500	53.1%
Middle PI Tercile	35.5%	28.8%	211,500	45.5%
Top PI Tercile	45.8%	33.1%	301,600	37.6%

*Note:* AHEAD and exit interview data. Conditional mean calculated by winsorizing values above the 99th percentile of overall sample. Homeownership status is measured in the wave prior to the death of the spouse. “No children” includes observations who are missing information on children (0.3% of sample).

Panel (B) shows that homeowners are somewhat more likely to make side bequests, but that, conditional on a transfer, non-homeowners transfer a larger share.

Panel (C) documents how bequests differ by the age at which the first spouse dies. Both the fraction of the deceased who transfer wealth to other heirs and the amount and share of wealth transferred tend to increase with age. This is consistent with the idea that, all else equal, older surviving spouses need fewer resources because they have shorter lifespans. Finally, Panel (D) reports results by PI tercile. The fraction making non-spousal transfers and the size of these transfers are both increasing in PI, which is consistent with bequests being luxury goods.

### 3.5 Medicaid reciprocity

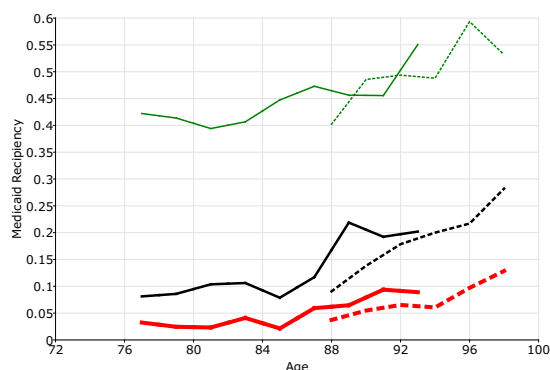


Figure 3: Medicaid reciprocity by age, PI, and cohort, AHEAD data, 1996-2014. Singles and couples pooled. Solid lines: cohort ages 71-76 in 1996. Dashed lines: cohort ages 83-88 in 1996. Thicker lines denote higher PI terciles.

Because previous work has shown that means-tested social insurance programs affect saving, it is important to match the extent to which retirees use such programs. The AHEAD has reliable measures of Medicaid reciprocity, although not spending. Figure 3 plots Medicaid reciprocity rates conditional on age, PI tercile, and cohort for all households in our sample. It shows that the lowest-income retirees are most likely to end up on Medicaid and that Medicaid reciprocity rises with age. This is consistent with the asset-tested nature of these programs (high-asset households are not eligible) and the wealth rundown shown in Figure 1.

## 4 The model

A retired household maximizes its expected discounted lifetime utility by choosing savings, consumption, and, upon death of the first spouse, the split of wealth between

the survivor and other heirs. These choices also determine final bequests upon the death of the last household member.

Households make these choices at household head age  $t$ ,  $t = t_r, t_r + 1, \dots, T + 1$ , where  $t_r$  is the initial period that we consider (corresponding to age 70) and  $T$  is the maximum potential lifespan (corresponding to age 102). Consistent with the AHEAD data frequency, our time period is two years long. For tractability, we assume that wives are always two years younger than their husbands (a single model period), so that one age is sufficient to characterize a household.

The household begins the period as either a couple, a newly widowed man or woman, or a single man or woman. It uses beginning-of-period cash on hand to consume and save. After that, mortality, health and medical expense shocks occur, income net of taxes is received, and government transfers take place. At this point, the amount of cash-on-hand that is carried into the next period is known, and the household enters next period.

People who are newly widowed have an additional decision, which is how to divide their estate between themselves and bequests to others.<sup>5</sup> Once that decision is made, they become single men or women, with wealth equal to the remainder of their estates.

When the final member of a household dies, all remaining net worth goes to its heirs. Consistent with reality, our timing implies that medical costs associated with death are collected before any bequests can be made and that Medicaid pays bills that are incurred even when a patient dies.

## 4.1 Preferences

The per-period utility functions for singles and couples are given by

$$u^S(c) = \frac{c^{1-\nu}}{1-\nu}, \quad u^C(c) = 2 \frac{(c/\eta)^{1-\nu}}{1-\nu}, \quad 1 < \eta \leq 2, \quad \nu \geq 0, \quad (2)$$

respectively, where  $c$  is total consumption and the parameter  $\eta$  determines the extent to which couples enjoy economies of scale in the transformation of consumption goods to consumption services. The household weighs future utility with the factor  $\beta$ .

Our choice of how we model bequest motives is driven by both tractability and flexibility. This is because of the computational demands of solving our model and the lack of consensus in the literature about why households leave bequests. Our

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<sup>5</sup>Because we have time-consistent preferences and a unitary model of the couple, there is no inconsistency between what the couple wants in terms of bequests and how the surviving spouse distributes bequests.



flexible but parsimonious functional form for bequests, is consistent with several bequest motives, including dynastic, “warm glow,” and strategic considerations.<sup>6</sup>

We thus assume that the household derives utility  $\theta_j(b)$  from leaving bequest  $b$ , where  $\theta_0(b)$  is the utility from bequests when there are no surviving members in the household, while  $\theta_1(b)$  is the utility from bequests when there is a surviving spouse. It takes the form

$$\theta_j(b) = \phi_j \frac{(b + \kappa_j)^{1-\nu}}{1-\nu}, \quad (3)$$

where  $\kappa_j$  determines the curvature of the bequest function, and  $\phi_j$  determines its intensity. De Nardi (2004) shows that when  $\kappa_j > 0$ , bequests are luxuries and many households leave zero bequests, matching a key feature of the data.

## 4.2 Sources of uncertainty and budget constraints

### 4.2.1 Income

Because there is less income uncertainty during retirement than during the working period, we simplify the model by assuming that the household’s non-asset income at time  $t$ ,  $y_t(\cdot)$ , is a deterministic function of the household’s permanent income,  $I$ , age, and family structure  $f_t$  (single man, single woman, couple, all dead).

$$y_t(\cdot) = y(I, t, f_t). \quad (4)$$

We do not include received bequests as a source of income, because very few households age 70 and older receive them.

### 4.2.2 Health and survival uncertainty:

Health and survival are individual, rather than household-level, variables, and we use gender,  $g \in \{h, w\}$ , to differentiate between men and women. A person’s health status,  $hs^g$ , indicates whether he or she is in a nursing home, in bad health, or in good health. The transition probabilities for a person’s future health status depend on that person’s current health status, permanent income, age, gender and marital status

$$\pi_t(\cdot) = \Pr(hs_{t+1} | hs_t, I, t, g, f_t). \quad (5)$$

Survival depends on the same variables. Let  $s_t(I, g, hs_t, f_t)$  denote the probability that an individual alive at age  $t$  survives to age  $t + 1$ .

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<sup>6</sup>See, for instance Abel and Warshawsky (1988), Carroll (1998), and Andreoni (1989) for “warm glow” formulations, and Barczyk and Kredler (2018), Barczyk et al. (2022), Bernheim et al. (1985) and Brown (2003) for strategic motives.

### 4.2.3 Medical expense uncertainty

We use  $m_{t+1}$  to denote the sum of medical spending that is either paid out-of-pocket by the household or covered by Medicaid between periods  $t$  and  $t + 1$ . While we treat this total as exogenous, the division of expenses between the household and Medicaid depends on the household's financial resources, the total expenses that must be covered, and the level of the consumption floor. In other words,  $m_{t+1}$  gives the household's maximum possible medical spending obligation, but because of social insurance the amount paid by poorer households may be much smaller.

We allow  $m_{t+1}$  to depend on the health status of each family member at both the beginning and end of the period, permanent income, age, household's family structure (also differentiating single men and single women) at the beginning and end of each period, and an idiosyncratic component,  $\psi_{t+1}$ .

$$\begin{aligned} \ln m_{t+1} = & m(hs_t^h, hs_t^w, hs_{t+1}^h, hs_{t+1}^w, I, t + 1, f_t, f_{t+1}) \\ & + \sigma(hs_t^h, hs_t^w, hs_{t+1}^h, hs_{t+1}^w, I, t + 1, f_t, f_{t+1}) \times \psi_{t+1}. \end{aligned} \quad (6)$$

We normalize the variance of  $\psi_{t+1}$  to be 1.

Allowing medical expenses to depend on the household's composition and health status at both the beginning of a period (which was realized at the very end of the previous period) and the period's end (which will be carried over into the subsequent period) allows us to capture the jump in medical spending that occurs when a family member dies – that is  $f_t$  changes – and to incorporate the impact of two subsequent health realizations on medical spending. The latter better helps us account for the cost of prolonged periods of bad health or nursing home stays. Our timing implies that the value of  $m_{t+1}$  is not known to the household when it decides how much to consume between periods  $t$  and  $t + 1$ .

Following Feenberg and Skinner (1994) and French and Jones (2004), we assume that  $\psi_{t+1}$  can be decomposed as

$$\psi_{t+1} = \zeta_{t+1} + \xi_{t+1}, \quad \xi_{t+1} \sim N(0, \sigma_\xi^2), \quad (7)$$

$$\zeta_{t+1} = \rho_m \zeta_t + \epsilon_{t+1}, \quad \epsilon_{t+1} \sim N(0, \sigma_\epsilon^2), \quad (8)$$

where  $\xi_{t+1}$  and  $\epsilon_{t+1}$  are serially and mutually independent. We discretize  $\xi$  and  $\zeta$ , using the methods described in Tauchen (1986).

### 4.2.4 Budget constraints

Let  $a_t$  denote net worth at the beginning of period  $t$  and  $r$  denote its constant pre-tax rate of return. Total post-tax income is given by  $\Upsilon(r a_t + y_t(\cdot), \tau_{ft})$ , with the

vector  $\tau_{f_t}$  summarizing the tax code, which depends on family structure. Define the resources available *before* government transfers as

$$\tilde{x}_t = a_t + \Upsilon(r a_t + y_t(\cdot), \tau_{f_t}) - m_t, \quad (9)$$

To capture Medicaid and SSI, we assume that government transfers bridge the gap between a minimum consumption floor and the household's financial resources,

$$tr_t(\tilde{x}_t, f_t) = \max \left\{ 0, c_{min}(f_t) - \tilde{x}_t \right\}, \quad (10)$$

where we allow the guaranteed consumption level  $c_{min}$  to vary with family structure. As defined in equation (9), the resource measure used to determine transfer eligibility accounts for medical expenses, along with income and wealth.

To save on state variables we follow Deaton (1991) and sum the household's financial resources *after* government transfers into cash-on-hand:

$$x_t = a_t + \Upsilon(r a_t + y_t(\cdot), \tau_{f_t}) - m_t + tr_t(\tilde{x}_t, f_t). \quad (11)$$

Households divide their cash-on-hand between consumption and savings:

$$a_{t+1} = x_t - c_t, \quad (12)$$

$$c_t \in [c_{min}(f_t), x_t], \quad \forall t. \quad (13)$$

Equation (13) ensures that consumption is at least as high as the consumption floor and that savings are non-negative.

Next period's resources before transfers and next period's cash-on-hand can then be expressed in terms of this period's cash-on-hand and are, respectively,

$$\tilde{x}_{t+1} = (x_t - c_t) + \Upsilon(r(x_t - c_t) + y_{t+1}(\cdot), \tau_{f_{t+1}}) - m_{t+1}, \quad (14)$$

$$x_{t+1} = \tilde{x}_{t+1} + tr_{t+1}(\tilde{x}_{t+1}, f_{t+1}). \quad (15)$$

### 4.3 Recursive formulation

Let  $f_t = S$  indicate a single-person household. The value function for a single person of age  $t$  and gender  $g$  is

$$\begin{aligned} V_t^g(x_t, h s_t, I, \zeta_t) = \max_{c_t} & \left\{ u^S(c_t) + \beta s_t(I, g, h s_t, S) \right. \\ & \times E_t \left( V_{t+1}^g(x_{t+1}, h s_{t+1}, I, \zeta_{t+1}) \right) \\ & \left. + \beta [1 - s_t(I, g, h s_t, S)] E_t \theta_0(x_{t+1}) \right\}, \end{aligned} \quad (16)$$

subject to Equations (4)-(8), and (13)-(15).

A newly-single person – one who was part of a couple in the previous period and single now – distributes bequests towards other heirs before making savings and consumption decisions as a single person:

$$V_t^{ng}(x_t, hs_t, I, \zeta_t) = \max_{b_t} \left\{ \theta_1(b_t) + V_t^g(x_t - b_t, hs_t, I, \zeta_t) \right\}, \quad (17)$$

subject to equation

$$b_t \in [0, x_t - c_{min}(f_t)], \quad (18)$$

which prohibits the surviving spouse from using bequests to become eligible for government transfers.

The value function for couples ( $f_t = C$ ) can be written as

$$\begin{aligned} V_t^C(x_t, hs_t^h, hs_t^w, I, \zeta_t) = \max_{c_t} \left\{ u^C(c_t) \right. \\ + \beta s_t(I, w, hs_t^w, C) s_t(I, h, hs_t^h, C) E_t \left( V_{t+1}^C(x_{t+1}, hs_{t+1}^h, hs_{t+1}^w, I, \zeta_{t+1}) \right) \\ + \beta s_t(I, w, hs_t^w, C) [1 - s_t(I, h, hs_t^h, C)] E_t \left( V_t^{nw}(x_{t+1}^w, hs_{t+1}^w, I, \zeta_{t+1}) \right) \\ + \beta [1 - s_t(I, w, hs_t^w, C)] s_t(I, h, hs_t^h, C) E_t \left( V_{t+1}^{nh}(x_{t+1}^h, hs_{t+1}^h, I, \zeta_{t+1}) \right) \\ \left. + \beta [1 - s_t(I, w, hs_t^w, C)] [1 - s_t(I, h, hs_t^h, C)] E_t \theta_0(x_{t+1}) \right\}, \quad (19) \end{aligned}$$

subject to Equations (4)-(8) and (13)-(15). The dating of the continuation value for new widows,  $V_t^{nw}(\cdot)$ , reflects that wives are one model period (two years) younger than their husbands. We solve our model numerically: see Appendix F for more details.

## 5 Estimation

We adopt a two-step strategy to estimate the model. In the first step, we estimate or calibrate those parameters that, given our assumptions, can be cleanly identified outside our model. These include health transitions, out-of-pocket medical expenses, and mortality rates from raw demographic data. In addition, we fix the discount factor  $\beta$  at an annual value of 0.97, and we set the consumption floor for couples to be 150% of the consumption floor for singles in accordance with the statutory rules for Medicaid and Supplemental Social Insurance.<sup>7</sup>

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<sup>7</sup>See <https://www.ssa.gov/oact/cola/SSI.html> for more on SSI spousal benefits.

In the second step, we estimate the rest of the model’s parameters, which include risk aversion, the consumption equivalence scale, bequest parameters, and the consumption floor for singles,

$$\Delta = (\nu, \eta, \phi_0, \phi_1, \kappa_0, \kappa_1, c_{min}(f_t = S)),$$

with the method of simulated moments (MSM), taking as given the parameters that were estimated in the first step. In particular, we find the parameter values that allow the simulated life-cycle decision profiles to “best match” (as measured by a GMM criterion function) those from the data. These profiles are calculated using a large number of simulated life histories. Each simulated history begins with a draw of age, PI, and wealth from the initial joint distribution of the data, and uses the observed history of health and survival shocks for each household member. Consequently, we generate attrition in our simulations that exactly matches the attrition in the data (including its variation by initial wealth and mortality). Appendix F provides more details on the mechanics of our MSM procedure.

Because our goal is to explain why retirees save so much and at rates that differ by income, we match moments of the distribution of wealth by cohort, age, and PI tercile. Because we wish to study differences in savings patterns of couples and singles, we match wealth profiles for the singles and couples separately. Finally, because Medicaid is an important program insuring the medical expenses and consumption of the poor we also match Medicaid reciprocity. More specifically, the moment conditions that comprise our estimator are given by

1. The 25th percentile, median, and 75th percentile of wealth holdings by cohort-PI tercile-year for all singles (including bequests).
2. The 25th percentile, median, and 75th percentile of wealth holdings by cohort-PI tercile-year for those who are currently couples with both members currently alive.<sup>8</sup>
3. Medicaid reciprocity by cohort-PI tercile-year for all households currently alive.

Appendix G contains a detailed description of our moment conditions, the weighting matrix in our GMM criterion function, and the asymptotic distribution of our parameter estimates.

When there is a death in a couple, we drop the household from the current couples’ moments and add the surviving spouse to the moments for all singles. The

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<sup>8</sup>We also include bequests for the small number of couples where both spouses die between adjacent waves.

moments for all singles thus combine new singles and initial singles. We do so because the number of new singles is small, especially earlier in our sample. This grouping also aligns with our model’s assumption that, conditional on our state variables, new singles behave like initial singles. Such an assumption is consistent with the regression evidence in Table 1. Moreover, we show in Section 7 that our model matches the jumps in wealth and medical expenses occurring at death of the first spouse (which are not moments we target). This implies that our model also captures well the starting wealth of new singles.

When estimating our model, we face two well-known problems. First, in a cross-section, older households were born in earlier years than younger households and, due to secular income growth, have lower lifetime incomes. Because of this, the wealth levels of households in older cohorts will likely be lower as well. As a result, comparing older households born in earlier years to younger households born in later years leads to understated wealth growth. Second, lower-income households and singles tend to die at younger ages than higher-income households and couples. The average survivor in a cohort thus has higher lifetime income, and thus more wealth, than the average deceased member of the same cohort. This “mortality bias” is more severe at older ages, when a greater share of the cohort members are dead. As a result, not accounting for mortality bias leads to overstated wealth growth. We address both problems by starting our simulations with initial conditions that come from the data, by explicitly modeling heterogeneity in mortality, and by giving simulated households the same mortality histories as in the data.

## 6 Estimation results

This section reports some of the most relevant features of our first-step estimates and discusses our second-step estimates and their identification.

### 6.1 First-step estimation results

Because they are key elements affecting saving behavior, the most important features of our first-step estimates pertain to life expectancy and nursing home risk, income and its drop when one of the spouses dies, and medical spending. Appendix H describes our first-step estimation procedures in detail.

### 6.1.1 Life expectancy and nursing home risk

We estimate health transitions and mortality rates simultaneously by fitting the transitions observed in the AHEAD to a multinomial logit model. We allow the transition probabilities to depend on age, sex, marital status, current health status, PI, and interactions of these variables.

Table 3 shows life expectancies at age 70 for single and married people, respectively, which we obtain by using our estimated transition probabilities to simulate demographic histories, beginning at age 70, for different gender-PI-health-family structure combinations. It shows that rich people, women, married people, and healthy people live much longer than their poor, male, single, and sick counterparts. For instance, a single man at the 10th permanent income percentile and in a nursing home expects to live only 3.0 more years, while a single woman at the 90th percentile and in good health expects to live 15.4 more years. The far right column of the top two panels shows average life expectancy conditional on PI, averaging over both genders and health states. Singles at the 10th percentile of the PI distribution live on average 10.2 years, while singles at the 90th percentile live on average 12.0 years.

People in couples at age 70 live about 2 years longer than singles: single women live on average 13.9 years versus 15.8 for married women but, conditional on PI and health, the differences in longevity are much smaller. Thus, married people live longer than singles, but a significant part of the difference is explained by the fact that married people tend to have higher PI and to be in better health. The bottom part of Table 3 shows the expected years of remaining life for the oldest survivor in a household when both the man and the woman are 70. On average the last survivor lives 17.9 more years. The woman is the oldest survivor 63.7% of the time.

Table 3: Life expectancy in years, conditional on reaching age 70

Income Percentile	Nursing Home	<u>Men</u>	Good Health	Nursing Home	<u>Women</u>	Good Health	All
		Bad Health			Bad Health		
Singles							
10	3.0	6.9	8.7	4.1	11.3	13.2	10.2
50	3.0	7.8	10.3	4.1	12.3	14.9	11.5
90	2.9	8.1	10.9	3.8	12.5	15.4	12.0
Couples							
10	2.7	7.8	9.8	4.0	12.1	14.1	11.3
50	2.8	9.4	12.2	4.0	13.7	16.3	13.4
90	2.7	10.4	13.5	3.9	14.6	17.3	14.5
Single Men							9.0
Married Men							11.5
Single Women							13.9
Married Women							15.8
Oldest Survivor*							17.9
Probability that Oldest Survivor is Woman							63.7%

*Note:* Life expectancies calculated through simulations using estimated health transition and survivor functions. \*Oldest survivor among households who were couples at age 70.

Table 4 shows that single men and women face on average a 26% and 37% chance of being in a nursing home for an extended stay (at least 60 days in a year), respectively, while married men and women face on average a 20% and 36% chance of being in a nursing home for an extended stay. Married people are much less likely to transition into a nursing home at any age, but married people, especially women, often become single as their partner dies. Furthermore, married people tend to live longer than singles and thus have more years of life to potentially enter a nursing home. Compared to gender or marital status, PI and age-70 health have smaller effects on ever being in a nursing home. This is because those with high PI, or in



good health, are less likely to be in a nursing home at any given age, but they tend to live longer.

Table 4: Probability of ever entering a nursing home, conditional on being alive at age 70

Income Percentile	<u>Men</u>		<u>Women</u>		All
	Bad Health	Good Health	Bad Health	Good Health	
<b>Singles</b>					
10	23.6	25.3	35.8	37.9	32.8
50	22.8	24.8	35.5	38.2	32.5
90	20.3	22.8	32.2	35.8	30.1
<b>Couples</b>					
10	17.3	19.2	34.4	37.0	28.7
50	16.6	18.8	34.1	37.3	28.7
90	14.6	16.8	31.4	34.5	26.3
Single Men					26.4
Married Men					19.5
Single Women					37.2
Married Women					36.3

### 6.1.2 Income

As discussed above and in Appendix C, we model non-asset income as a function of PI, age, and family structure. Figure 4 presents predicted income profiles for those at the 20<sup>th</sup> and 80<sup>th</sup> percentiles of the PI distribution. The average income of couples ranges from about \$14,000 at the 20<sup>th</sup> percentile to over \$30,000 at the 80<sup>th</sup>. As a point of comparison, median wealth holdings for these two groups at age 74 are \$70,000 and \$330,000, respectively.

To illustrate how household income drops when one of the spouses dies, Figure 4 displays three income scenarios for each PI level, all commencing with the income

of a couple. Under the first scenario, the household remains a couple until age 100. Under the second one, the man dies at age 80, while under the third, the woman dies at age 80. Our estimates imply that couples in which the husband dies at age 80 suffer a 40% decline in income, while couples in which the wife dies at age 80 suffer a decline of 30%. The income losses that occur at the death of a spouse reflect the fact that even though Social Security and private defined benefit pensions have survivors' benefits, these benefits replace only a fraction of the deceased spouse's income.

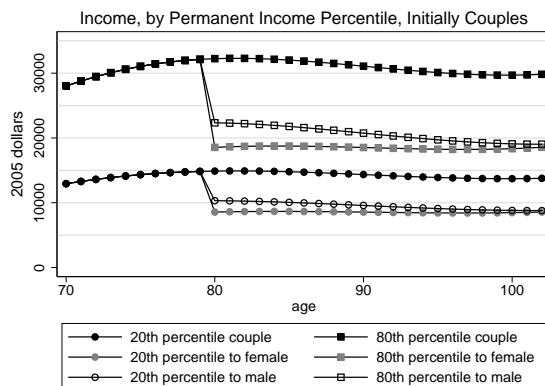


Figure 4: Income, conditional on permanent income and family structure. All households begin as couples, then either stay in a couple or switch to being a single man or single woman at age 80. Estimates of Equation 4 using AHEAD data, see Appendix C for details.

### 6.1.3 Medical spending

Because our model explicitly accounts for Medicaid payments, which depend on a household's savings, the measure of medical expenses that we need is the sum of out-of-pocket spending by the household and Medicaid payments.<sup>9</sup> Although the AHEAD contains detailed data on out-of-pocket medical spending, it does not contain Medicaid payments. A key empirical contribution of this paper is to construct the sum of these two components by combining out-of-pocket medical spending information in the AHEAD with Medicaid payment data from the Medicare Current Beneficiary Survey (MCBS).

<sup>9</sup>A large share of the elderly's medical spending is covered by Medicare co-pays, which are not means-tested. Our measure is net of those co-pays.

The MCBS contains extremely high quality administrative and survey information on both Medicaid payments and out-of-pocket medical spending (De Nardi et al. (2016c)). Like the HRS, it tracks household members as they enter nursing homes. Its main limitation for our purposes is that the data are collected at the individual, rather than the household level: although the MCBS contains marital status, it lacks information on the medical spending or health of the spouse. To exploit the strengths of each dataset, we use the conditional mean matching procedure described in Appendix H.2 to impute a Medicaid payment for each individual in each period in the AHEAD. The procedure preserves both the mean and the distribution of combined medical spending, conditional on Medicaid reciprocity, age, income, out-of-pocket spending and other health and medical utilization variables. The regression of Medicaid payments on these variables has an  $R^2$  statistic of 0.67, suggesting that our predictions are accurate.

We model medical spending as a function of a polynomial in age, a polynomial in PI, marital status, health of each spouse (at the beginning and the end of the period), interactions of these variables, and persistent and transitory spending shocks (see Equation (6)). To estimate these profiles, we use fixed effects rather than ordinary least squares for two reasons. First, differential mortality causes the composition of our sample to vary with age, whereas we are interested in how medical expenses vary for the same individuals as they grow older. Second, by controlling for fixed effects we control for all time-invariant characteristics, including cohort effects.

We estimate the medical spending persistence parameter  $\rho_m$  and the variance of the transitory and persistent medical spending shocks using a standard error components model. Our estimates imply that approximately 40% of the cross-sectional variation in log medical spending is explained by observables. Of the remaining cross-sectional variation, 40% comes from the persistent shock and 60% from the transitory shock. Our estimated value of  $\rho_m$  is 0.85. See Appendix H.3 for details.

The top row of Figure 5 shows model-predicted mean medical spending for the AHEAD cohort aged 71-76 in 1996, where we simulate the households through age 101.<sup>10</sup> Three general trends are apparent. First, medical expenses rise rapidly with age, in part because older individuals are more likely to reside in nursing homes or die.<sup>11</sup> Second, spending rises only modestly with PI, if at all. Although our underlying coefficients show that medical expenses rise with PI when health is held constant, lower-income households are often in worse health. Finally, the spending of couples (right panel) is roughly twice that of singles (left panel). Given that we

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<sup>10</sup>Because of the structure of our medical spending model, which requires two periods of health realizations, the simulation results start at age 77.

<sup>11</sup>Our simulations include end-of-life spending.

measure spending at the household level, this suggests that there are some economies of scale in the consumption of medical goods and services.

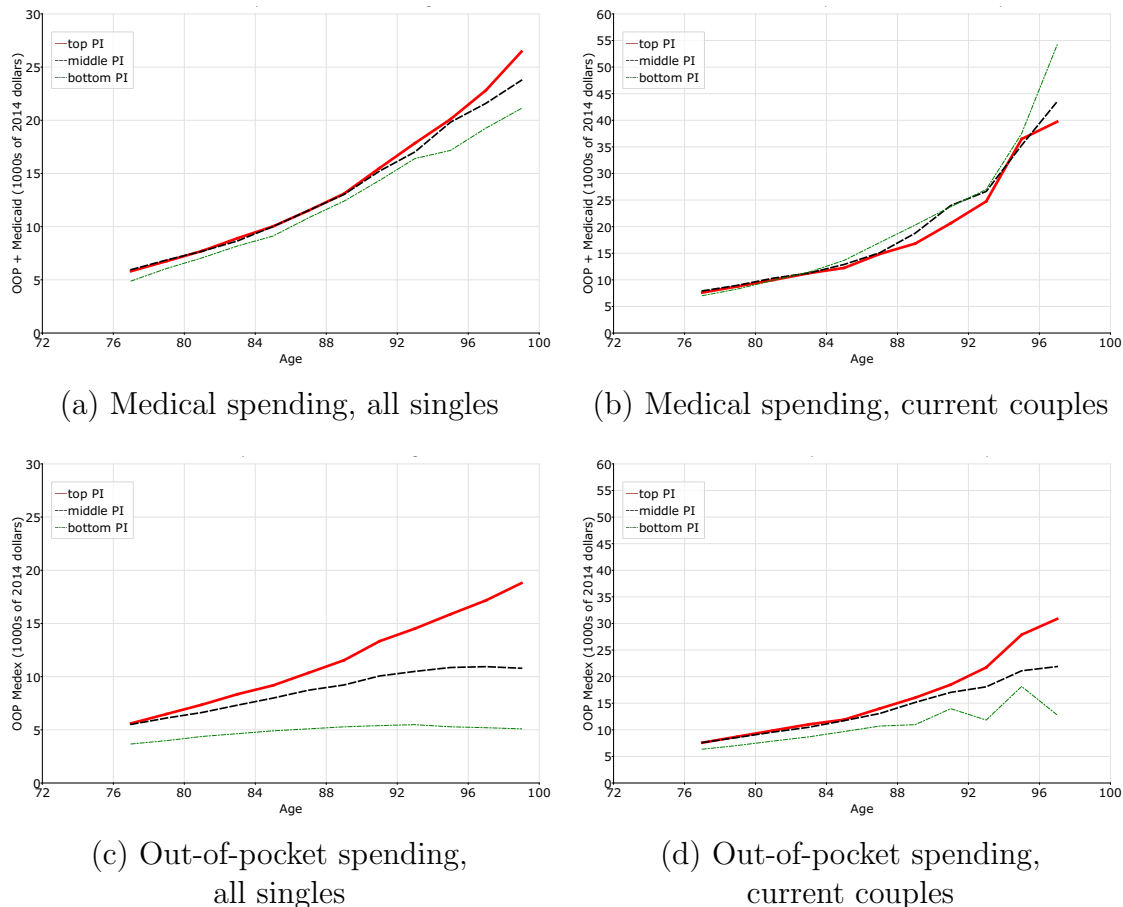


Figure 5: Household-level mean medical (top row) and out-of-pocket spending (bottom row) for all singles and current couples by PI tercile.

The bottom row of Figure 5 shows out-of-pocket medical spending. We find out-of-pocket expenses by simulating our estimated structural model and calculating Medicaid payments. Subtracting these payments from total medical spending (shown in the top row) yields out-of-pocket spending. Because Medicaid covers a larger share of medical expenses in poorer households, out-of-pocket spending has a strong income gradient. Likewise, as medical expenses rise with age, the share covered by Medicaid rises as well. This leads out-of-pocket medical spending to rise more slowly with age than total spending, especially among the low-income. For instance, among singles

in the bottom PI tercile, out-of-pocket medical spending stays between \$3,700 and \$5,400; among those at the top, spending rises by a factor of 3, from \$5,600 to \$18,000. Because couples tend to be wealthier, their Medicaid reciprocity rates are lower and thus Medicaid covers a smaller share of their costs.

## 6.2 Second step parameters: estimates and identification

We require our model to match the observed variation in savings and Medicaid reciprocity by cohort, income, age, and wealth rank. More specifically, we target the 25th percentile, the median, and the 75th percentile of wealth, conditional on cohort, PI tercile, and age, for both couples and singles. We also target average Medicaid reciprocity by cohort, PI tercile, and age. As we will see below, these targets help separately identify households' precautionary saving motives, the strength of their bequest motives, and the degree to which bequests are luxury goods.

Table 5 reports our estimated preference parameters. Our estimate of the consumption equivalence scale  $\eta$  (1.53) is almost identical to the “modified” OECD scale. It also lies within the confidence interval estimated by Hong and Ríos-Rull (2012), who estimate it using data on life insurance holdings and a structural life-cycle model of consumption and saving decisions. After reviewing a variety of estimates, Fernández-Villaverde and Krueger (2007) argue in favor of similar economies of scale. In combination with our estimated value of  $\nu$ , our estimate of  $\eta$  implies that in order to have the same marginal utility of consumption as a single the consumption of a couple must be 1.64 times as large.<sup>12</sup>

Intuitively,  $\eta$  is identified by the extent to which couples save, relative to singles, to self-insure future risks. To better illustrate this intuition, Appendix I evaluates the sensitivity of our model-generated profiles to changes in parameter values. It shows that when we reduce the household consumption equivalence scale  $\eta$ , the savings of initial singles remain unchanged while those of couples increase. This is because, holding consumption constant, a lower value of  $\eta$  reduces the marginal utility of consumption for a couple relative to that of a single. Couples respond by deferring consumption to the future, when they might be singles who value consumption more highly at the margin. Setting  $\eta$  below its estimated value thus raises the savings of couples relative to singles in a counterfactual way.

The parameters  $\phi_0$  and  $\kappa_0$  govern terminal bequest motives. The left hand side of Figure 6 shows, using the estimated values of  $\phi_0$  and  $\kappa_0$ , the share of resources that

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<sup>12</sup>To see this note that the marginal utilities of singles and couples are  $\frac{\partial u^S(c^S)}{\partial c} = (c^S)^{-\nu}$  and  $\frac{\partial u^C(c^C)}{\partial c} = (\frac{2}{\eta^{1-\nu}})(c^C)^{-\nu}$ . Equating these marginal utilities yields  $\frac{c^C}{c^S} = (\frac{2}{\eta^{1-\nu}})^{1/\nu}$ .

Table 5: Estimated second-step parameters

$\eta$ : consumption equivalence scale	1.528 (0.195)
$\phi_0$ : bequest intensity, single (in 000s)	6,826 (1,208)
$\kappa_0$ : bequest curvature, single (in 000s)	3,517 (352)
$\phi_1$ : bequest intensity, surviving spouse	4,447 (656)
$\kappa_1$ : bequest curvature, surviving spouse (in 000s)	211.2 (23.3)
$\nu$ : coefficient of RRA	3.701 (0.096)
$c_{min}(f = 1)$ : annual consumption floor, singles	4,101 (124)

*Note:* Standard errors in parentheses. We set  $c_{min}(f = 2) = 1.5 \cdot c_{min}(f = 1)$ .

would be bequeathed by single households who know that they will die next period for sure. In that scenario, single households with less than \$29,600 in resources will leave no bequests,<sup>13</sup> while those having \$100,000 will leave over 75% of their resources in bequests. Repeating the exercise for couples (with both spouses dying for sure), reveals that couples require almost \$50,000 in resources before they choose to leave bequests to other heirs. These differences in behavior for singles and couples do not come from differences in the bequest parameters, which we constrain to be the same when there are no survivors. Rather, they are due to differences in household size and the presence of the equivalence scale. The left hand side of Figure 6 shows that bequests are a luxury good for singles and even more of a luxury good for couples. Panel (b) of Figure 6 compares our estimated bequest motives for singles with those from several previous papers. Our estimated bequest motive for singles is of similar strength and slightly more of a luxury good than those estimated by Lockwood (2018) and Lee and Tan (2019).

To provide insights on the identification of  $\phi_0$  and  $\kappa_0$ , Appendix I evaluates the sensitivity of our model-generated profiles to changes in their values. The two key

<sup>13</sup>This is an annual value. In our two-year framework, the threshold will (approximately) double. See Appendix A.2.

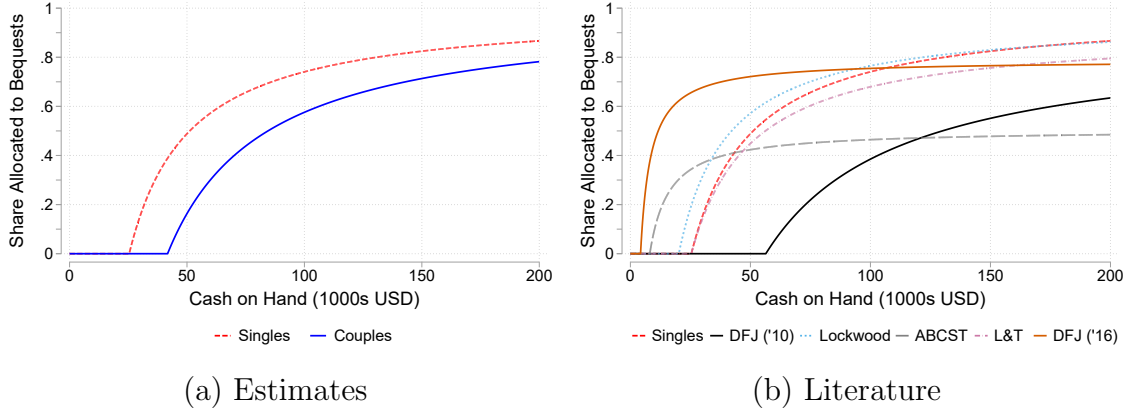


Figure 6: Estimated Bequest Motives. Panel (a): expenditure share allocated to bequests for couples (solid) and singles (dashed) facing certain death in the next period. Panel (b): comparing our results for singles (dashed red) with those in De Nardi et al. (2010) (DFJ '10), De Nardi et al. (2016a) (DFJ '16). Lockwood (2018), Ameriks et al. (2020) (ABCST), and Lee and Tan (2019) (L&T).

findings are the following. First, increasing the marginal propensity to leave final bequests (MPB) by increasing  $\phi_0$ , affects the savings of rich singles more than those of rich couples because singles have a shorter (effective) life expectancy and because couples also care about the side bequests made when one spouse dies, lowering the relative importance of terminal bequests. Second, raising  $\kappa_0$ , which raises the extent to which final bequests are a luxury good, increases the resource level beyond which people actively save to leave these bequests. In contrast to changes to  $\phi_0$ , which primarily affect rich households, changes to  $\kappa_0$  affect households across much of the PI and wealth distribution.

Appendix I also discusses the sensitivity of our model-generated profiles to changes in  $\phi_1$  and  $\kappa_1$ , which govern the utility from bequests to non-spousal heirs at the death of the first spouse. Similarly to final bequests, decreasing the MPB of side bequests affects richer couples who are likely to leave a bequest, leading them to hold less wealth. Changing the threshold  $\kappa_1$ , in contrast, affects saving rates further down the PI and wealth distributions. The effects of changing  $\phi_1$  and  $\kappa_1$  are also mediated, however, by the fact that when the desire to leave side bequests is reduced, couples leave a larger share of their wealth to surviving spouses. This raises the savings of all singles and lowers Medicaid reciprocity rates, because surviving spouses have more wealth to self-insure high medical expenses. Appendix A.2 provides additional intuition on the side bequest decision.

A related issue is whether the data allow us to differentiate the parameters governing the terminal and side bequests. Appendix J reports a specification where we constrain the two sets of parameters to be equal, showing that this constraint substantially worsens the model’s fit and generates different bequest behavior.

Our estimate of  $\nu$ , the coefficient of relative risk aversion, is 3.7, a value similar to that estimated for retired singles in De Nardi et al. (2010), and to those typically used in the life-cycle literature. Appendix I shows that reducing our risk aversion parameter reduces the wealth holdings of couples and singles and raises Medicaid reciprocity.

Our estimate of the consumption floor  $c_{min}$  implies that the consumption of a single household is bounded below at \$4,101 per year. The floor for couples is set to 150% of this value. Our estimated floor is best interpreted as an “effective” consumption floor that accounts for transactions costs, stigma, and other determinants of Medicaid and SSI usage. Appendix I shows that raising the consumption floor reduces saving and raises Medicaid reciprocity.

Appendix I also shows that even though  $\nu$  and  $c_{min}$  have similar effects on savings, they have different effects on Medicaid reciprocity. Decreasing the level of risk aversion and increasing the consumption floor both decrease saving, which in turn leads to higher Medicaid reciprocity rates. This increase in Medicaid reciprocity is concentrated at older ages, when households are most likely to face large medical expenses. Moreover, the effect is similar across the PI distribution. Raising the consumption floor, however, increases Medicaid reciprocity even if savings are unchanged. This additional effect is largest for low-PI households, who are more likely to rely on Medicaid, and more likely to receive Medicaid at younger ages. In sum, relative to lowering risk aversion, raising the consumption floor is more likely to increase Medicaid reciprocity at younger ages and lower PI ranks.

Consequently, even if a decrease in relative risk aversion and simultaneous decrease in the consumption floor had no effect on the savings moments that we target, it would change the profile of Medicaid reciprocity. More specifically, it would decrease the average Medicaid reciprocity rate of low PI households and would generate a steeper increase in their reciprocity rate with age. It would likewise decrease the average Medicaid reciprocity rate of higher PI households, particularly at older ages. These changes in the model’s fit of the Medicaid reciprocity moments help us identify the level of risk aversion separately from the value of the consumption floor.

Finally, to evaluate our assumption that couples and singles have the same preferences, we estimate our model for singles only. Appendix K shows that estimated parameters from this alternative specification are in line with those from our baseline specification.



### 6.3 Model fit

Figure 7 plots median net worth by age, PI, and birth cohort for current couples (Panel (a)) and all singles (Panel (b)), in the data (solid line) and from our model (dashed line).<sup>14</sup> It shows that our model matches the key features of retirement savings well. First, higher-PI households dissave more slowly than lower-PI households throughout retirement. Second, these patterns are more pronounced for couples, as long as both members of the couple stay alive. More specifically, singles in the lowest PI tercile have almost no wealth, while couples in the same PI tercile hold onto their retirement savings until age 90. Singles in the middle PI tercile start decumulating their wealth from the time that we start tracking them (age 75), while couples of the same age and PI tercile display flat wealth trajectories over much of the period that we observe them. Finally, households in the highest PI tercile, and especially current couples, have highest savings during their retirement years.

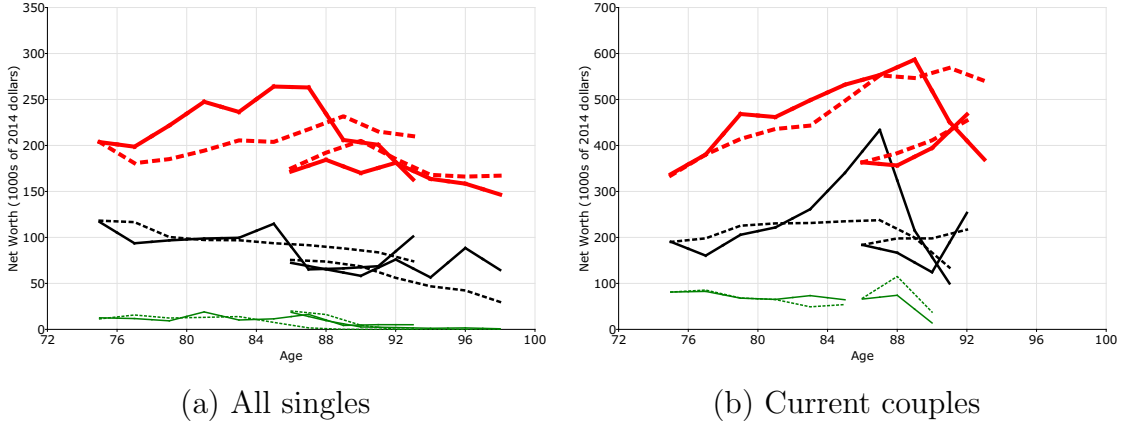


Figure 7: Median wealth by cohort and PI tercile, AHEAD data for 1996-2014. Solid lines: AHEAD data for cohorts ages 71-76 and 83-88 in 1996. Dashed lines: model simulations. Thicker lines denote higher PI terciles.

Figure 8 compares the Medicaid reciprocity profiles generated by our model (dashed line) to those in the data (solid line). While the model matches the general patterns of Medicaid usage across age and household PI, it does overstate the rate of increase of Medicaid reciprocity among households in the bottom PI tercile. De Nardi et al. (2016a) experience similar issues with matching Medicaid reciprocity trajectories, despite having separate asset tests and Medicaid rules that distinguish between the

<sup>14</sup>For clarity, we only show targeted moments for two of our birth cohorts in each panel of these set of graphs, but the model fit is similarly good across cohorts (See Appendix D).

categorically and medically needy eligibility provisions. We are not able to capture all of the heterogeneity in Medicaid savings incentives, including that the Medicaid housing exemption depends on one’s state of residence.

Appendix D shows all the moments that we match and our model’s fit. Matching multiple wealth percentiles across multiple PI terciles requires the model to reproduce saving behavior across households with different incomes, household structures, and initial wealth holdings. High-PI households and couples save at higher rates than their low-PI and single counterparts, and this is especially evident at the 25th and 75th wealth percentiles, as shown in Appendix Figures A3 and A4. Among couples at the top of the PI distribution, wealth rises with age at the 75th percentile of wealth, but is constant at the 25th percentile. Among singles at the bottom of the PI distribution, wealth is constant at the 75th percentile, while it falls rapidly, or is 0 throughout, at the 25th percentile. This variation helps disentangle the saving motives operating within our model.

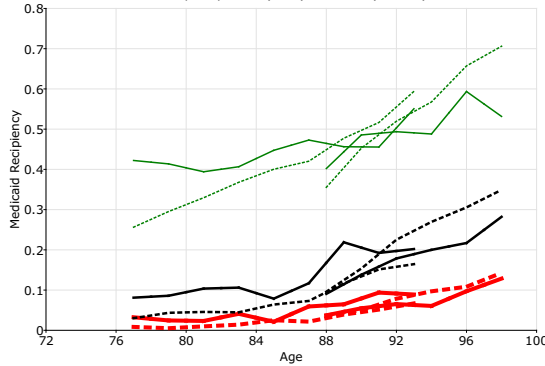


Figure 8: Medicaid Reciprocity by cohort and PI tercile. AHEAD data for 1996-2014. Solid lines: AHEAD data for cohorts ages 71-76 and 83-88 in 1996. Dashed lines: model simulations. Thicker lines denote higher PI terciles.

## 7 Model validation

To build additional trust in the predictions of our estimated model, we now turn to comparing its implications with aspects of the data that are important given our questions but are not targeted in our estimation procedure.

Our first validation exercise focuses on the rise in out-of-pocket medical spending around the death of a spouse and uses the same event study approach used for

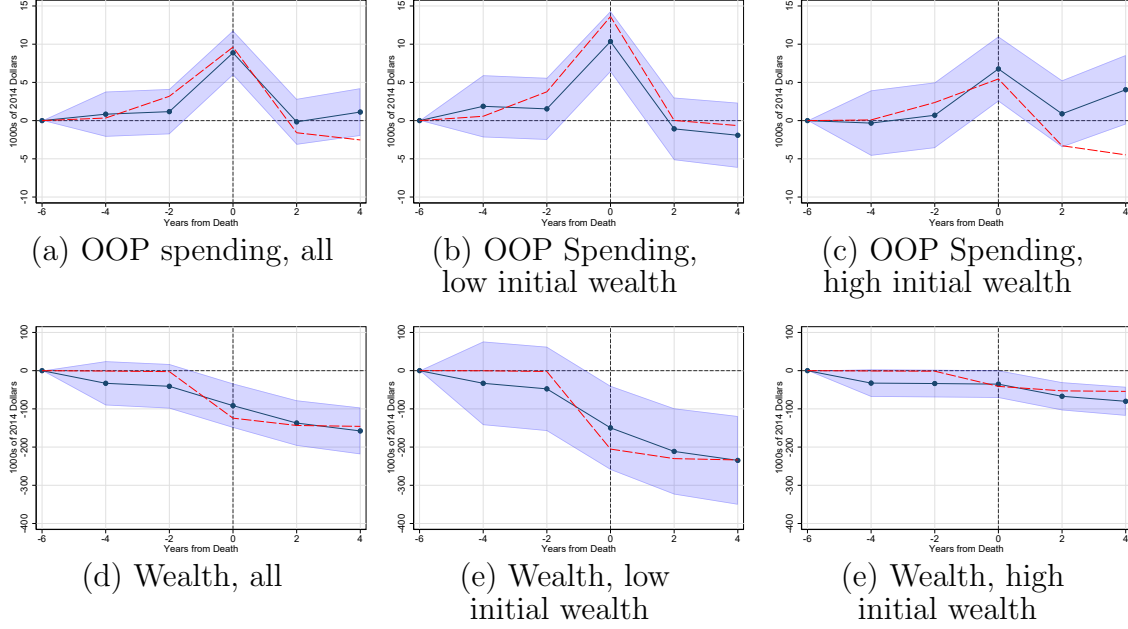


Figure 9: Average changes in the sum of out-of-pocket medical and death-related expenses and in wealth. AHEAD data (solid blue line) and their 95% confidence interval (shaded region) and differences-in-differences estimates (dashed red line) from model-simulated data. Death dates are centered at year 0.

Figure 2. The top panel of Figure 9 shows that our model generates a trajectory of out-of-pocket medical expenses around the time of death that matches the one observed in the data. This is notable because we are not requiring the model to match it by construction. Although the sum of out-of-pocket and Medicaid payments is exogenous in our model, the out-of-pocket component is partly a function of household wealth, which determines Medicaid eligibility and thus the share of expenses paid by Medicaid. Hence, the fact that our model replicates the dynamics of out-of-pocket medical spending through the dynamics of saving and means-tested transfers implies that it endogenously generates the correct exposure of wealth to medical expense risk. The figure further shows that the model matches well the jump in out-of-pocket spending by initial wealth. In both model and data, low wealth households spend less out-of-pocket because their low wealth makes them Medicaid-eligible in the event of high medical spending.

Our second validation exercise pertains to the wealth dynamics of couples when one of their spouses dies. The bottom panel of Figure 9 displays results from our

event study analyses for the samples of all initial couples (left hand side graph), those with initial wealth above the median (center), and those with initial wealth below the median (right hand side). It shows that the net worth dynamics around a spousal death generated by our model lie well within the 95% confidence interval of their AHEAD data counterpart, even when we condition on household wealth. For the full sample of initial couples, both the data and the simulations predict a decline of \$160,000, while for the sample of wealthier households we replicate the decline of \$255,000 around death. Matching well the wealth dynamics for households around the time of death, including by initial wealth, means that our luxury good specification of bequest motives generates realistic saving behavior across the wealth distribution.

Our model thus captures well the dynamics of both medical spending and net worth around the time of a spousal death, across the wealth distribution. This implies that the model also matches well the extent to which the decline in wealth at death is due to out-of-pocket medical expenses, as opposed to non-spousal bequests. These features of the data, in turn, have important implications about the relative importance of the precautionary savings and bequest motives, which help identify the risk aversion and bequest motive parameters (given the consumption floor, which is pinned down by Medicaid reciprocity).

Appendix L shows the model’s fit of additional untargeted moments. These include: the effect of mortality bias on wealth trajectories; Medicaid reciprocity rates for singles and couples; differences in wealth accumulation across genders (among singles); the 90th percentile of the wealth distribution for different age, cohort, PI and household structure cells; and additional disaggregated plots of how wealth and medical spending trajectories around the time of a spousal death. By and large, our model fits these additional untargeted moments well.

## 8 What drives savings?

To quantify the determinants of retiree savings, we perform several decomposition exercises and calculate the changes in retiree wealth that occur when we switch off bequest motives and/or medical spending. In doing so, we assume that household wealth accumulation prior to retirement is unchanged. Hence, our approach focuses on the drivers of post-retirement savings and helps us understand policy reforms that are not announced far in advance. Because our model generates smaller wealth changes than one in which people can re-optimize their savings at younger ages, our results provide a lower bound of their impacts on retiree saving.

As a cohort ages, its wealth holdings change both because of household saving

decisions and because of changes in household composition. In particular, as individuals die, single households exit the simulations and married households become widows/ers (or “new singles”). The set of initial singles and current couples thus shrinks over time, while the set of all singles both loses and adds members. In addition, the financial position of new singles is affected by the amount of side bequests given to other heirs upon the death of the first spouse. In such a complex environment, examining each type of household separately allows us to better understand the mechanisms that drive savings. To make our analysis clearer, we focus on our youngest cohort, aged 71-76 in 1996. Starting at this point, we simulate households through age 99, using the processes for health and mortality estimated from the AHEAD. Our simulations thus reflect the same mortality bias that is in the data.

In Section 8.1 we document how savings motives vary across different groups of households, which is important for understanding distributional implications. However, because wealth is unequally distributed, a change affecting the wealth of many poor households may have little effect on aggregate savings. In contrast, a change affecting a small number of rich households may have substantial aggregate effects. Hence, we finish our analysis by collecting all households alive at each age in our simulations into a pooled sample, containing both singles and couples, and describing (in Section 8.2) how various saving motives affect summary statistics for the distribution of wealth. We then perform the same analysis for the pooled sample of side and terminal bequests.

## 8.1 Heterogeneity in retiree savings motives

To understand heterogeneity in saving motives, we focus on four groups of households – initial singles, new singles, all singles, and current couples – and examine the effects of eliminating one or more saving motives on their savings. Each row in Figure 10 compares baseline savings with savings under a counterfactual described below, and each column refers to a particular group of households.

**Eliminating terminal bequest motives** has little to no effect on the savings of initially single households in the lower two PI terciles, who are too poor to save for bequests (Panel (a)). In contrast, it reduces the savings of initial singles in the top PI tercile, especially at older ages. Among new singles (Panel (b)), the wealth of high-PI households is lower at all ages. This occurs because in the absence of a terminal bequest motive, high-PI couples both reduce their savings (Panel (d)) and tend to give more away as side bequests. Hence, new singles are left with less wealth upon the death of their spouse. The savings of all singles (Panel (c)) initially resemble those of initial singles because few people lose their spouse in their early

70s. As the sample ages, however, new singles become increasingly common and dominate the wealth profiles of the all singles group.

**Eliminating side bequests** has no effect on the savings of initial singles (Panel (e)), as they only have a terminal bequest motive. In contrast, it increases substantially the wealth of new singles in the top two PI terciles (Panel (f)). As we eliminate side bequests, richer couples save less (Panel (h)) but also give less to others when the spouse dies. Because the second effect dominates, new singles in the top two PI terciles start out richer.

**Eliminating medical expenses** can have either positive or negative effects on the savings of initial singles (Panel (i)). Those in the lowest two PI terciles save less because they no longer need to self-insure against future medical expenses. For the poorest singles, who have little wealth to begin with, the magnitude of these reductions is small.<sup>15</sup> The impact in the middle PI tercile is more substantial.

In contrast, initial singles in the highest PI tercile save substantially more after age 81. This seemingly counterintuitive result occurs because medical expenses reduce household wealth. Removing these expenses thus generates a positive wealth effect. Because we estimate bequest motives to be luxury goods, the richest initial singles choose to spend much of their windfall on bequests, and this wealth effect dominates the reduction in precautionary savings. To confirm this explanation, Appendix M eliminates the variation in medical expenses generated by health and medical expense shocks, but holds constant their average (conditional on household structure, age and PI). This exercise reduces savings at all PI levels and thus shows that, in the absence of wealth effects, high-PI households save against medical spending risk.

In the absence of medical expenses, new singles start out with much less wealth (Panel (j)). This is because couples barely change their savings (Panel (l)) but distribute larger side bequests, which leaves less resources for their surviving spouses, who no longer have medical expenses to finance.

**Eliminating both bequest motives and medical expenses** lowers the wealth profiles of initial singles in the bottom and middle PI terciles (Panel (m)) only slightly more than eliminating medical expenses in isolation (Panel (i)). This happens because households in these groups are too poor to prioritize leaving bequests. In contrast, the savings of initial singles in the top PI tercile drop markedly. To avoid repetition, we will explain the reasons for this result in the next subsection.

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<sup>15</sup>As we show below, however, the proportional effects are large.

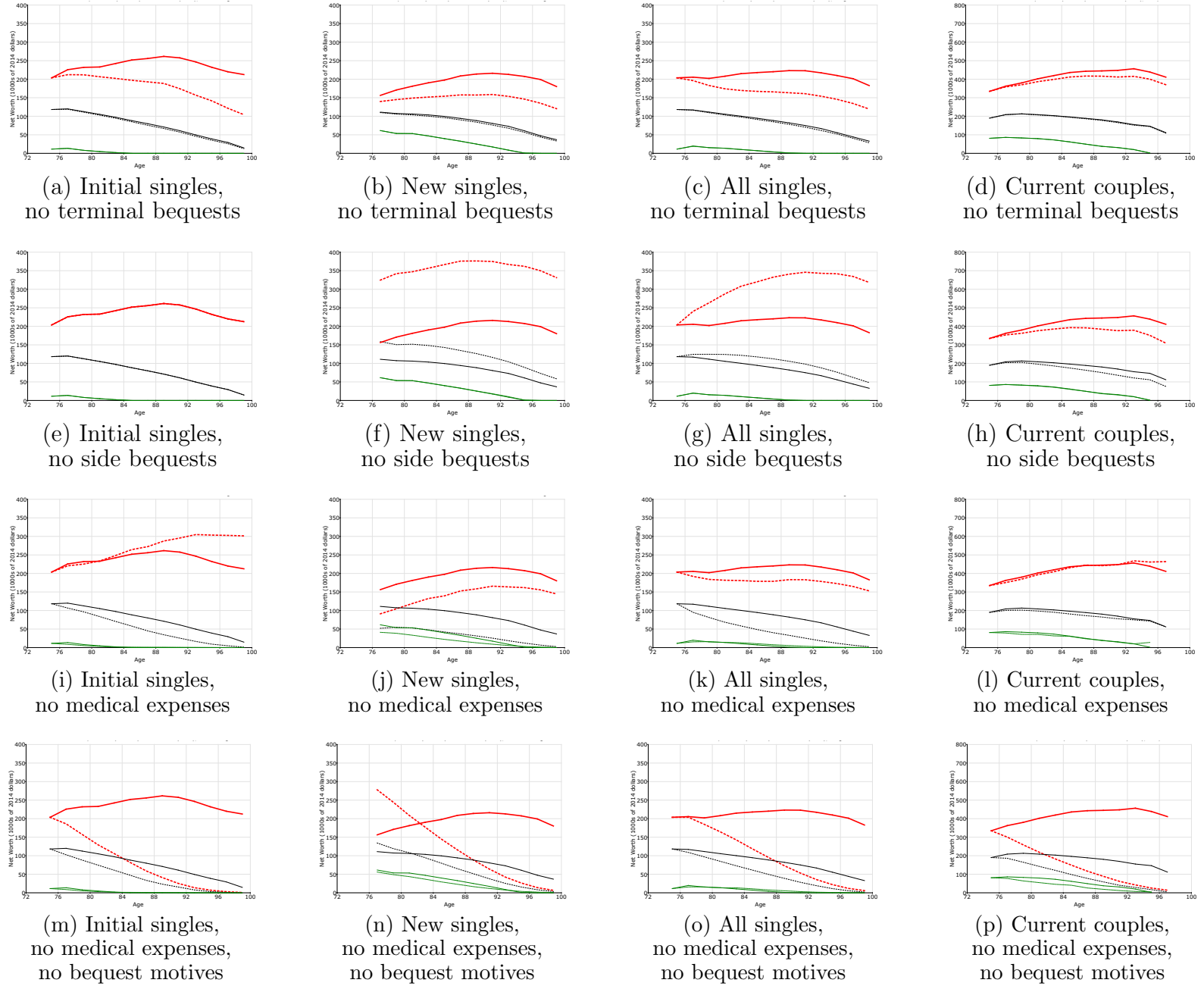


Figure 10: Median wealth for initial singles (left column), new singles (center left), all singles (center right) and current couples (right column) by PI tercile. Baseline (solid lines) and experiment (dashed lines). The thick red lines denote the top PI tercile, the medium black lines denote the middle PI tercile; and the thin green lines the bottom.

Eliminating side bequests implies that many new singles start off with more resources (Panel (n)). However, eliminating terminal bequest motives and medical expenses leads them to consume more, and any increases in their initial wealth soon evaporate. This fast decumulation is also present for current couples (Panel (p)). As all singles include initial and new singles, their wealth is a composite of the wealth of these two groups (Panel (o)).

## 8.2 What drives the aggregate distributions of savings and bequests?

As we have just seen, the drivers of retirement savings differ substantially across household types, permanent income ranks, and age. Given this heterogeneity, which drivers are most important for understanding aggregate retirement savings and bequests? And which drivers are most important for the largest number of households? To answer these questions, we compare the cross-sectional distributions of savings and bequests in our baseline model to counterfactuals where we eliminate one or more saving motives from our model.

Table 6: Implications of retiree saving motives on the distribution of wealth

Experiment	25th Percentile	Median	75th Percentile	Mean
Baseline wealth (1000s of 2014 dollars)	50.3	149.3	387.8	360.8
(1) No terminal bequest motive	-4.0%	-8.7%	-17.3%	-23.0%
(2) No side bequest motive	11.0%	16.6%	12.2%	12.2%
(3) No bequest motives	7.5%	7.4%	-7.5%	-14.8%
(4) No medical expenses	-60.0%	-21.1%	-0.4%	-3.1%
(5) No medical expenses or bequest motives	-62.5%	-45.4%	-42.3%	-42.5%

*Note:* The first row reports baseline wealth. The subsequent rows refer to percentage changes in wealth resulting from the counterfactual experiments.

We start with retirement savings. Table 6 includes every household in our age-74 simulated cohort for as long as they live, which amounts to computing the cross-sectional distribution of retirement wealth under a demographic steady state. Ex-



periment 1 generates the expected result that eliminating terminal bequest motives causes people to consume more and save less. Savings drop at all wealth levels, especially among the rich (4.0% at the 25th percentile and 17.3% at the 75th), consistent with these bequests being luxury goods. In contrast, eliminating side bequest motives (Experiment 2) increases wealth at all wealth levels by roughly similar percentages (11.0% at the 25th percentile and 12.2% at the 75th). This is because, as we discussed in the previous section, in the absence of side bequests, new singles start out with more wealth.

Eliminating all bequest motives (Experiment 3) increases the wealth of poorer retirees (7.5% at the 25th percentile). This is because at lower wealth levels, the effect of eliminating side bequests dominates. In contrast, wealth holdings drop at the upper end of the wealth distribution (7.5% at the 75th percentile), where terminal bequest motives are stronger. While the effect at the top of the wealth distribution is similar to that in many models with only terminal bequest motives, the one at the bottom is more unexpected. It showcases that ignoring the side bequest decision biases our understanding of retiree saving.

Eliminating medical expenses (Experiment 4) drastically reduces savings at the lower end of the wealth distribution (60.0% at the 25th wealth percentile) because it reduces precautionary savings. The reduction at the upper end of the wealth distribution (0.4% at the 75th) is much smaller. This is because eliminating medical expenses makes households wealthier, and households with an active bequest motive save some of this additional wealth for bequests.

When we compare the elimination of all bequest motives with the elimination of medical expenses (Experiment 3 vs. Experiment 4) on a household-by-household basis, we find that most households (53%) save more to self-insure against medical expenses than to leave bequests. However, because these households hold relatively little wealth, the aggregate effect of eliminating medical expenses is small. Mean wealth drops by only 3.1%. In contrast, removing bequest motives reduces aggregate wealth by nearly five times as much (the mean drops by 14.8%), because it has its largest effects on the richest households, who hold most of the wealth. Hence, although medical spending is more important than leaving bequests for the majority of households, bequest motives drive aggregate saving.

The same household-by-household comparison also reveals that most singles (62%) save more for medical expenses rather than to leave bequests, while most couples (69%) save more for bequests. This is because couples value both side and terminal bequests and are also typically richer than singles.

Simultaneously removing medical expenses and all bequest motives (Experiment 5) has a very large effect that exceeds the sum of the individual effects. Mean wealth

drops by 14.8% when we remove bequest motives, by 3.1% when we remove medical expenses, and by a whopping 42.5% when we remove both.

This interaction arises because eliminating medical spending still leaves households with bequest motives, while eliminating bequest motives still leaves them needing to save for medical expenses. When both motives are present, wealth can satisfy the two needs simultaneously (Dynan et al., 2002). When both motives are absent, households have little reason to save. Not surprisingly, these interactions are weakest at the 25th percentile, where bequest motives are weak. This interaction constitutes an important finding because much of the previous literature has focused on precautionary saving for medical expenses in the absence of a bequest motive.

We next turn to determining the drivers of the cross-sectional distribution of all bequests, including both side and terminal bequest motives. Table 7 has the same structure as Table 6; but because the 25th percentile of the bequest distribution is approximately zero, we replace it with the 90th percentile. This allows us to focus on its upper tail. The first row of Table 7 shows that, as in the data, the mean bequest (\$251,800) is significantly larger than the median one (\$77,900).

Table 7: Implications of retiree saving motives on the cross-sectional distribution of bequests

Experiment	Median	75th Percentile	90th Percentile	Mean
Baseline value (1000s of 2014 dollars)	77.9	256.7	614.5	251.8
(1) No terminal bequest motive	-11.8%	-16.9%	-22.4%	-28.6%
(2) No side bequest motive	-100.0%	-29.1%	14.7%	-2.2%
(3) No bequest motives	-100.0%	-45.2%	-33.3%	-44.0%
(4) No medical expenses	28.3%	19.2%	15.6%	14.3%
(5) No medical expenses or bequest motives	-97.9%	-77.8%	-67.5%	-69.6%

*Note:* The first row reports baseline bequests left. The subsequent rows refer to percentage changes in bequests resulting from the counterfactual experiments. This includes all side and terminal bequests, including zeros, left during a period.

Eliminating terminal bequest motives (Experiment 1) decreases bequests across their entire distribution. This effect is strongest at the upper tail (22.4% at the 90th

percentile compared to 11.8% at the median) because large bequests are less likely to be accidental.

Eliminating side bequest motives (Experiment 2) changes the distribution of bequests but leaves the average bequest virtually unchanged. Because every side bequest would be zero in this case, the observation that the median bequest is now zero indicates that many smaller bequests are side bequests and thus intentional. In contrast, bequests at the 90th percentile increase by 14.7%. This reveals substitution between side bequests and terminal bequests: when side bequest motives are eliminated and terminal bequest motives remain, some households leave larger terminal bequests.

Experiments 1 and 2 thus reveal that side bequests dominate the lower end of the bequest distribution and that terminal bequests dominate the upper end.

Eliminating all bequest motives (Experiment 3) causes the median bequest to become zero, the 90th percentile to decrease by 33.3%, and the mean to fall by 44%. The large fall in mean bequests is especially important, because it implies that 44% of aggregate bequests are voluntary.

Because eliminating medical expenses (Experiment 4) generates a positive wealth effect, bequests tend to increase in their absence. The proportional increase is larger for smaller bequests (28.3% at the median, as opposed to 15.6% at the 90th percentile). This is because the positive wealth effect from removing medical expenses is proportionally larger for poorer households.

Eliminating both medical expenses and all bequest motives (Experiment 5) generates large declines across the entire bequest distribution, especially at the lower end. The drop is 97.9% at the median and 67.5% at the 90th percentile. The observation that the mean bequest drops by 69.6% implies that roughly 70% of bequests are due to either bequest motives or saving for medical expenses.

## 9 Conclusions

This paper documents new facts about the retirement savings and risks of couples and singles. It then develops and estimates a rich structural model that includes these risks and explains their savings.

In terms of new facts, we compare the saving behavior of couples and singles. Households with high PI, and especially couples, tend to accumulate wealth, whereas those with low PI, and especially singles, tend to decumulate it. Furthermore, when the first spouse dies, net worth drops sharply. Although some of this drop is explained by end-of-life medical expenses, most of it is due to transfers to non-spousal heirs.

To understand the role of risks it is crucial to properly measure them for both couples and singles. While medical expenses for couples and singles are not very different on a per capita basis until someone dies, medical spending jumps at the time of a spouse’s death. At the same time, household income falls, exposing households to a substantial loss in financial resources upon a spouse’s death.

We embed these risks in a rich structural model of savings that incorporates heterogeneity in financial resources, life expectancy, and medical expense risks, including the large jump in end-of-life medical expenses. It accounts for means-tested social insurance, which helps insulate households against those risks. It also allows households to derive utility from leaving bequests, both upon the death of a spouse (when present), and upon death of the last survivor. In addition, and importantly, households choose how to split the estate between the surviving spouse and other heirs.

We estimate our model using MSM and targeting the savings of both couples and singles, and Medicaid reciprocity rates by cohort, PI, and wealth levels. It fits these key features of the data well. In addition, although we do not require our model to match the dynamics of out-of-pocket medical spending and wealth around the time of a spouse’s death, it matches those as well. This helps build confidence in its predictions. Finally, we use our estimated model to measure the extent to which the savings of retirees are driven by medical expenses, bequest motives, and their interaction.

We find that medical expenses are more important for singles, whereas bequest motives are more important for couples. This is due to two main reasons. First, couples not only receive direct utility from leaving bequests at the time of the first and last spouse’s death. Second, bequests are a luxury good, and couples are wealthier.

We also find that introducing bequest motives reduces the effects of medical expenses on savings. This is because savings intended for medical spending that go unspent due to early death are still valued when bequest motives are present. This finding implies that we need to model both medical spending and bequests.

Lastly, these forces imply that, while the savings of most households is driven more by medical expenses than by bequest motives, aggregate retirement savings are driven by the bequest motives of a small fraction of richer households.

Hence, to understand the drivers of retirement savings, it is essential to model the bequest motives and medical spending of both couples and singles. Our findings have important policy implications. They suggest that couples and high-PI singles can easily self-insure against medical spending risk because they save to leave bequests. Low-PI singles are well insured through Medicaid and do not need to save for medical expenses. In contrast, middle-PI singles set aside significant amounts of wealth for

precautionary purposes because they are not rich enough to want to leave bequests but are too rich to qualify for Medicaid. It is thus the middle-PI singles who would respond most to changes in public health insurance.

We leave many interesting issues for future research. They include modeling the household in a collective rather than in a unitary fashion, explicitly modeling marriage and divorce after age 70, allowing for heterogenous preferences, and evaluating government policies such as the relative generosity of Medicaid for couples and singles.

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# Appendices for Online Publication

## Appendix A: Theoretical background

This appendix uses stylized models to provide intuition for the workings of our rich quantitative model. In its first part, we set out a two-period model that allows for collective household decision making and use it to derive two new results. First, that side bequests upon the death of the first spouse naturally arise in the context of a collective decision model in which each spouse cares about their own consumption and about the bequests left to non-spousal heirs when they die. Second, while this model nests that of a unitary household, its collective parameters, that is the spousal weights, cannot be separately identified from other preference parameters, given our model structure and the consumption data available in the HRS. In the second part of this appendix, we illustrate the economic forces that give rise to side and terminal bequests (and influence their size) in our unitary model.

### A.1 A collective model of retired couples

Consider the following simplified collective model of retired couples. Each spouse derives utility from consumption while they are alive and, after death, from the bequests that they leave to children and other non-spousal heirs.

In the first period, both members are alive and consumption,  $c_0$ , is a public good with equivalence scale  $\eta$ . The husband ( $h$ ) dies after the first period. His discounted lifetime utility is thus given by

$$\frac{(c_0/\eta)^{1-\nu}}{1-\nu} + \beta\phi_1 \frac{(b_1 + \kappa_1)^{1-\nu}}{1-\nu},$$

where  $b_1$  are his bequests,  $\nu$  is the coefficient of relative risk aversion,  $\beta$  is the discount factor, and  $\phi_1$  and  $\kappa_1$  govern the strength and curvature of his utility function for bequests.

The wife ( $w$ ) lives for two periods and derives utility from consumption during each period and from bequests upon her death. Her lifetime utility is given by

$$\frac{(c_0/\eta)^{1-\nu}}{1-\nu} + \beta \frac{c_1^{1-\nu}}{1-\nu} + \beta^2\phi_2 \frac{(b_2 + \kappa_2)^{1-\nu}}{1-\nu},$$

where  $b_2$  are her bequests and  $\phi_2$  and  $\kappa_2$  govern the strength and curvature of her utility function for bequests (and need not coincide with  $\phi_1$  and  $\kappa_1$ ).

There is no uncertainty and full commitment. At the beginning of period 0, the collective household thus solves

$$\begin{aligned} \max_{c_0, c_1, b_1 \geq 0, b_2 \geq 0} & \left\{ \mu_h \left( \frac{(c_0/\eta)^{1-\nu}}{1-\nu} + \beta \phi_1 \frac{(b_1 + \kappa_1)^{1-\nu}}{1-\nu} \right) + \right. \\ & \left. \left( \frac{(c_0/\eta)^{1-\nu}}{1-\nu} + \beta \frac{c_1^{1-\nu}}{1-\nu} + \beta^2 \phi_2 \frac{(b_2 + \kappa_2)^{1-\nu}}{1-\nu} \right) \right\}, \\ \text{s.t. } & c_0 + \frac{1}{1+r}(b_1 + c_1) + \frac{1}{(1+r)^2}b_2 = W, \end{aligned} \quad (\text{A1})$$

where  $\mu_h$  is the Pareto weight on the husband's utility,  $r$  is the rate of return, and

$$W = a_0 + \sum_{t=0}^2 \frac{1}{(1+r)^t} (y_t - m_t) \quad (\text{A2})$$

is the net present value of the household's financial resources, where  $a_0$  is initial assets and  $y_t$  and  $m_t$  are time- $t$  income and medical spending. In the absence of a consumption floor, the household's problem is meaningful only if  $W > 0$ , but, in contrast to our full model, the household can borrow subject to repayment upon the wife's death.

Two remarks are worth making.

**Remark 1:** A collective model of the household in which each spouse cares about their own consumption and bequests to non-spousal heirs can generate both side and terminal bequests.

**Remark 2:** Data on average wealth growth and Medicaid reciprocity do not allow us to distinguish the collective model from the unitary one. That is, the weight  $\mu_h$  is not identified independently of the preference parameters  $\nu$ ,  $\phi_1$  and  $\phi_2$ .

To better understand these remarks, note that a simple rearrangement of terms allows us to rewrite the household's objective function as

$$2 \frac{(c_0/\tilde{\eta})^{1-\nu}}{1-\nu} + \beta \frac{c_1^{1-\nu}}{1-\nu} + \beta \tilde{\phi}_1 \frac{(b_1 + \kappa_1)^{1-\nu}}{1-\nu} + \beta^2 \tilde{\phi}_2 \frac{(b_2 + \kappa_2)^{1-\nu}}{1-\nu}, \quad (\text{A3})$$

with

$$\begin{aligned} \tilde{\eta} &= \eta (0.5(\mu_h + 1))^{1/(\nu-1)}, \\ \tilde{\phi}_1 &= \mu_h \phi_1, \\ \tilde{\phi}_2 &= \phi_2. \end{aligned}$$

Because the function in equation (A3) equals the original objective function multiplied by  $(\mu_h + 1)^{-1}$ , it will induce the same pattern of wealth holdings and bequests as equation (A1). Hong and Ríos-Rull (2012) make a similar point. Moreover, the collective decision problem given by equation (A1) is equivalent to the problem of a unitary household whose preferences follow equation (A3). The latter problem is a simplified version of our unitary model.

A key assumption behind these results, which we also impose in our main model, is that consumption in a married household is a public good. This enhances tractability and, importantly, accomodates HRS data limitations. That is, the HRS consumption module is small, unavailable in certain years, and contains no information on the private consumption of each person in a couple.

## A.2 The decisions to consume and bequeath

Here, we highlight the drivers of terminal and side bequests.

**Terminal bequests.** Consider a single individual facing no uncertainty and one period to live. This individual solves

$$\max_{c \leq W} \frac{1}{1-\nu} c^{1-\nu} + \beta \phi_2 \frac{1}{1-\nu} ((1+r)(W-c) + \kappa_2)^{1-\nu},$$

where  $c$  denotes consumption and  $W > 0$  is the net present value of the individual's financial resources.

The first-order condition for an interior solution is

$$c^{-\nu} = \beta \phi_2 (1+r) ((1+r)(W-c) + \kappa_2)^{-\nu},$$

Define

$$\varphi = [\beta \phi_2 (1+r)]^{1/\nu}. \quad (\text{A4})$$

We can then solve for bequests,  $b = (1+r)(W-c)$  :

$$\varphi \left( W - \frac{b}{1+r} \right) = b + \kappa_2 \Rightarrow b = \frac{1+r}{1+r+\varphi} (\varphi W - \kappa_2). \quad (\text{A5})$$

It immediately follows that for intentional bequests, the marginal propensity to bequeath out of wealth,  $\frac{\partial}{\partial W} \left( \frac{b}{1+r} \right)$ , is

$$MPB = \frac{\varphi}{1+r+\varphi}. \quad (\text{A6})$$

With bequests required to be non-negative, however, it follows from Equation (A5) that the propensity to bequeath is identically zero unless

$$W > \underline{W} = \frac{\kappa_2}{\varphi}. \quad (\text{A7})$$

It is widely accepted that  $MPB$  (or  $MPC = 1 - MPB$ ) and  $\underline{W}$  provide a better characterization of the bequest motive than  $\phi_2$  and  $\kappa_2$  (see, e.g., De Nardi et al., 2010 or Lockwood, 2018).

Because the mapping between the vectors  $(MPB, \underline{W})$  and  $(\phi_2, \kappa_2)$  is one-to-one, we can reverse the preceding derivations. Using equation (A7), we know  $\kappa_2 = \varphi \underline{W}$ , and it follows from equations (A4) and (A6) that:

$$\begin{aligned} \varphi &= (1+r) \frac{MPB}{1-MPB} \\ \Rightarrow \phi_2 &= \frac{\varphi^\nu}{\beta(1+r)} = \left[ (1+r) \frac{MPB}{1-MPB} \right]^\nu \frac{1}{\beta(1+r)}. \end{aligned}$$

Given that the full model operates at a two-year frequency, it is useful to map its bequest parameters into those of a models with an annual frequency. An important intermediate step in this mapping is to consider the sequence of 1-year problems where the individual lives two periods and then dies. We will use hats to designate parameters for this one-year model, and unmarked parameters for the two-year framework. To simplify the algebra, suppose that  $\hat{\beta}(1+\hat{r}) = 1$ , so that  $\hat{c}$  is the same in the two periods of life. The present value budget constraint is

$$W = \hat{c} \left( \frac{2+\hat{r}}{1+\hat{r}} \right) + \frac{\hat{b}}{(1+\hat{r})^2},$$

which can be rewritten as

$$\hat{c} = \left( \frac{1+\hat{r}}{2+\hat{r}} \right) \left( W - \frac{\hat{b}}{(1+\hat{r})^2} \right). \quad (\text{A8})$$

If the marginal propensity to bequeath out of starting wealth is  $\widehat{MPB} = \frac{\partial}{\partial W} \left( \frac{\hat{b}}{(1+\hat{r})^2} \right)$ , the marginal propensity to consume on a **annual** basis, found by differentiating equation (A8), is:

$$\widehat{MPC} = \frac{\partial \hat{c}}{\partial W} = \frac{1+\hat{r}}{2+\hat{r}} \left[ 1 - \widehat{MPB} \right]. \quad (\text{A9})$$

Next, consider the wealth threshold  $\widehat{\underline{W}}$ . Recall that in the final period of life, all wealth below  $\widehat{\underline{W}}$  is consumed. Let  $\widetilde{\underline{W}}$  denote the wealth threshold **two** periods prior

to death. By definition, when wealth two periods prior to death equals  $\widetilde{W}$ ,  $\hat{b} = 0$ . Equation (A8) then implies that the wealth threshold **one** period prior to death is

$$\widehat{W} = (1 + \hat{r}) \left( \widetilde{W} - \frac{1 + \hat{r}}{2 + \hat{r}} \widetilde{W} \right) = \frac{1 + \hat{r}}{2 + \hat{r}} \widetilde{W}. \quad (\text{A10})$$

To complete the mapping, suppose that  $1 + r = (1 + \hat{r})^2$ ,  $MPB = \widehat{MPB}$ , and  $\underline{W} = \widetilde{W}$ . Equations (A9) and (A10) then imply that

$$\begin{aligned} \widehat{MPC} &= \frac{1 + \hat{r}}{2 + \hat{r}} MPC, \\ \widehat{W} &= \frac{1 + \hat{r}}{2 + \hat{r}} \underline{W}. \end{aligned}$$

In other words, when we operate at a one-year frequency, the marginal propensity to consume and the wealth threshold are (more or less) half their two-year counterparts. Conversely, when an individual expects to live more than one period, the threshold where the bequest motive becomes operative will be higher.

**Side bequests.** In our model, when the first member of the household dies, the surviving spouse decides how much of the household's wealth should be passed on immediately to other heirs. This decision depends on both the parameters of the side bequest motive and the opportunity cost to the surviving spouse of foregone resources. The opportunity cost is in turn governed by the value function for single retirees, a complex model object that can be difficult to interpret.

To provide intuition for the optimal side bequest, consider a newly widowed individual who faces no further uncertainty and remaining lifespan of  $T$  periods. The individual's problem is given by

$$\max_{\{c_t\}_{t=0}^T, b_0 \geq 0, b_{T+1} \geq 0} \phi_1 \frac{(\kappa_1 + b_0)^{1-\nu}}{1-\nu} + \sum_{t=1}^T \beta^t \frac{c_t^{1-\nu}}{1-\nu} + \beta^{T+1} \phi_2 \frac{(\kappa_2 + b_{T+1})^{1-\nu}}{1-\nu}, \quad (\text{A11})$$

where  $c_t$  denotes consumption at period  $t$ , and  $b_1$  and  $b_{T+1}$  denote the side and terminal bequests, respectively. They face a (remaining) lifetime budget constraint given by

$$\sum_{t=0}^T \frac{1}{(1+r)^t} c_t + b_0 + \frac{1}{(1+r)^{T+1}} b_{T+1} = W := a_0 + \sum_{t=0}^{T+1} \frac{1}{(1+r)^t} (y_t - m_t), \quad (\text{A12})$$

The decision problem in equation (A11) corresponds to the value function for surviving spouses given by equation (17) in the main text. Moreover, the second two



terms in equation (A11) – the utility from lifetime consumption and the utility from the bequests made at the death of the final household member – together correspond to the value function for singles given by equation (16) of the main text.

This simpler formulation makes it easy to express the optimal side bequest as a closed-form function of the individual’s remaining lifespan ( $T$ ) and financial resources ( $W$ ). In Figure A1 we plot the optimal allocations for different values of  $W$  and  $T$  using our baseline parameter estimates. Holding  $W$  fixed, newly-widowed individuals with shorter planning horizons, including those who are older or in worse health, have less need to retain resources for their own use and thus transfer more to non-spousal heirs. In contrast, those who face higher expected out-of-pocket medical spending effectively have fewer resources. Holding  $T$  fixed, this decreases the probability they make positive transfers and decreases the amounts transferred.

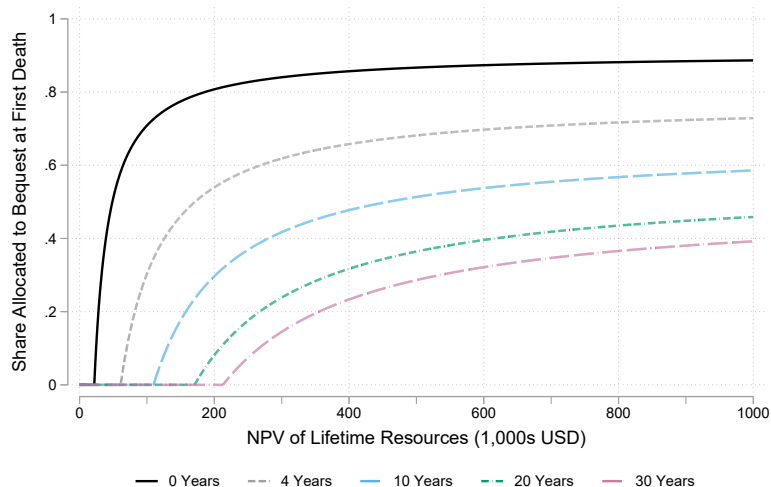


Figure A1: Analytic Solution for Optimal Side Bequests as a Function of Expected Lifespan and Financial Resources

In our full model, the trade-off between retaining wealth as a new widow(er) and transferring it to non-spousal heirs is complicated by the presence of uncertainty and the desire for self-insurance. Furthermore, the interaction between the precautionary and bequest motives raises the implicit value of retained wealth, which lowers the average, and marginal, propensity of new widow(er)s to make to make immediate bequests.

## Appendix B: Data and sample selection

Our main dataset is the AHEAD data, which is a cohort within the Health and Retirement Study (HRS).

To keep the dynamic programming problem manageable, we assume a fixed difference in age between spouses, and we take the average age difference from our data. In our sample, husbands are on average 3 years older than their wives; in the model we assume the difference is one period, or 2 years. To keep the data consistent with this assumption, we drop all households where the wife is more than 4 years older or 10 years younger than her husband.

We do not use 1993/94 wealth, nor medical expenses, due to underreporting issues (Rohwedder et al. (2006)) and thus begin with 6,047 households. Because we only allow for household composition changes through death, we drop households where an individual enters a household or an individual leaves the household for reasons other than death. Fortunately, attrition for reasons other than death is a minor concern in our data. We drop 401 households who get married, divorced, were same sex couples, or who report making other transitions not consistent with the model (of whom 257 are dropped due to marriage), 753 households who report earning at least \$3,000 in any period, 171 households with a large difference in the age of husband and wife, and 87 households with no information on the spouse in a household. As a result, we are left with 4,634 households, of whom 1,388 are couples and 3,246 are singles. This represents 24,274 household-year observations where at least one household member was alive.

An advantage of the AHEAD relative to other datasets is that it provides panel data on health status and nursing home stays. We assign individuals a health status of “good” if self-reported health is excellent, very good or good, and a health status of “bad” if self-reported health is fair or poor. We assign individuals to the nursing home state if they were in a nursing home at least 120 days since the last interview (on average 60 days per year) or if they spent at least 60 days in a nursing home before the next scheduled interview and died before that scheduled interview.

The AHEAD has information on the value of housing and real estate, autos, liquid assets (which include money market accounts, savings accounts, T-bills, etc.), IRAs, Keoghs, other defined contribution plan wealth, stocks, the value of a farm or business, mutual funds, bonds, “other” assets and investment trusts less mortgages and other debts. One problem with asset data is that the wealthy tend to underreport their wealth in virtually all household surveys (Davies and Shorrocks (2000)). This could lead us to understate wealth levels at all ages. However, Juster et al. (1998) show that the wealth distribution of the AHEAD matches up well with aggregate

Table A1: Summary Statistics

	Restricted AHEAD Sample		Unrestricted AHEAD Sample	
	Mean	S.D.	Mean	S.D.
Head's Age	84.9	6.5	84.6	6.5
Wife's age	82.1	6.7	81.7	6.7
OOP Medical Expenses	6,600	12,480	6,740	12,600
Medicaid Payments	1,910	9,130	1,830	9,020
Net Worth	302,000	659,600	322,000	702,000
Nights in a Nursing Home	30.8	100.3	29.3	98.2
Income	21,300	31,900	22,800	31,800

*Note:* All variables refer to household level aggregates for couples.

values for all but the richest 1 % of households. Given that we match the quantiles (conditional on permanent income) rather than means, underreporting at the very top of the wealth distribution should not affect our results.

Social Security and pension benefits are included in our measure of annual income, hence differences in Social Security and pension wealth appear in our model as differences in the permanent income measure we use to predict annual income (and other state variables).

## Appendix C: Income and Permanent Income

We describe our procedure for estimating the income profiles in Section 6.1.2 of the main text. We assume that log income evolves as following

$$\ln y_{it} = \kappa(t, f_{it}) + h(I_i) + \omega_{it}, \quad (\text{A13})$$

where  $\kappa(t, f_{it})$  is a flexible function of age  $t$  and family structure  $f_{it}$  (i.e., couple, single man or single woman) and  $\omega_{it}$  represents measurement error. The variable  $I_i$  is the household's percentile rank in the permanent income (PI) distribution. Since it is a summary measure of lifetime income at retirement, it should not change during retirement and is thus a fixed effect over our sample period. However, income could change as households age and potentially lose a family member.

To estimate Equation (A13) we first estimate the fixed effects model

$$\ln y_{it} = \kappa(t, f_{it}) + \alpha_i + \omega_{it}, \quad (\text{A14})$$

which allows us to obtain a consistent estimate of the function  $\kappa(t, f_{it})$ . Next, note that as the number of time periods over which individual  $i$  is observed (denoted  $T_i$ ) becomes large,

$$\text{plim}_{T_i \rightarrow \infty} \frac{1}{T_i} \sum_{t=1}^{T_i} [\ln y_{it} - \kappa(t, f_{it}) - \omega_{it}] = \frac{1}{T_i} \sum_{t=1}^{T_i} [\ln y_{it} - \kappa(t, f_{it})] = \alpha_i = h(I_i). \quad (\text{A15})$$

We thus calculate the PI ranking  $I_i$  for every household in our sample by taking the percentile ranking of  $\frac{1}{T_i} \sum_{t=1}^{T_i} [\ln y_{it} - \hat{\kappa}(t, f_{it})]$ , where  $\hat{\kappa}(t, f_{it})$  is the estimated value of  $\kappa(t, f_{it})$  from Equation (A14). Put differently, we take the mean residual per person from the fixed effects regression (where the residual includes the estimated fixed effect), then take the percentile rank of the mean residual per person to construct  $I_i$ .

However, we also need to estimate the function  $h(I_i)$ , which converts the estimated index  $I_i$  back to a predicted level of income that can be used in the dynamic programming model. To do this we estimate the function

$$[\ln y_{it} - \kappa(t, f_{it})] = h(I_i) + \omega_{it} \quad (\text{A16})$$

where the function  $h(I_i)$  is a flexible functional form. In practice we model  $\kappa(t, f_{it})$  as a third order polynomial in age, dummies for family structure, and family structure interacted with an age trend. When estimating Equation (A16), we replace the function  $\kappa(t, f_{it})$  with its estimated value. We model  $h(I_i)$  as a fifth order polynomial in our measure of permanent income percentile.

Given that we have, for every member of our sample,  $t$ ,  $f_{it}$ , and estimates of  $I_i$  and the functions  $\kappa(\cdot, \cdot)$ ,  $h(\cdot)$ , we can calculate the predicted value  $\ln \hat{y}_{it} = \hat{\kappa}(t, f_{it}) + \hat{h}(\hat{I}_i)$ . It is  $\ln \hat{y}_{it}$  that we use when simulating the model for each household. A regression of  $\ln y_{it}$  on  $\ln \hat{y}_{it}$  yields an  $R^2$  statistic of .72, showing that our specification captures most of the income variation in our data. We interpret the remaining variation as being measurement error. Consistent with this interpretation, we find no evidence of positive serial correlation of the residuals from this regression, which is what we would expect to find if the remaining variation came from persistent income shocks. For example, across any two waves, the correlation is -.06.

## Appendix D: Additional data profiles and model fits

Figure A2 compares the Median wealth profiles generated by the model (dashed line) to those in the data (solid line) for all of the birth cohorts and permanent income terciles that we match in estimation. We reproduce profiles for the cohorts reported in the main text, but also show profiles for the cohorts that were omitted. In all cohorts, the model matches differences in the level and trajectory of wealth by age and household permanent income.

Figure A3 plots the corresponding data for the 75th percentile of the wealth distribution. Comparing the 75th wealth percentiles to the median ones towards the beginning of the retirement period, when we start tracking our sample, shows that the 75th percentiles of wealth are about twice the medians for the two highest PI groups and much larger than twice the median for the lowest PI tercile. In addition, the 75th percentiles of wealth show even more evidence of wealth accumulation during retirement than do median wealth, both for couples and singles. Finally, the 75th percentiles suggest that current couples tend to save more during their retirement than singles, even given similar initial wealth. As with the medians, the model does a good job of matching the 75th percentile of wealth holdings across PI groups and ages, both for singles and couples. For example, it reproduces the flatter profiles of lower PI groups, while still generating eventual wealth holdings of more than \$1,000,000 for the top terciles.

Figure A4 plots the corresponding data for the 25th percentile of the wealth distribution. Comparing the 25th wealth percentiles to the medians towards the beginning of the retirement period, when we start tracking our sample, shows that the 25th wealth percentiles are about half the median ones for the two highest PI groups, with the exception of the lowest PI tercile for singles, where it is almost always 0. In addition, the 25th wealth percentiles show even more evidence that couples and singles' wealth evolves differently as the wealth holdings of singles decline. As with

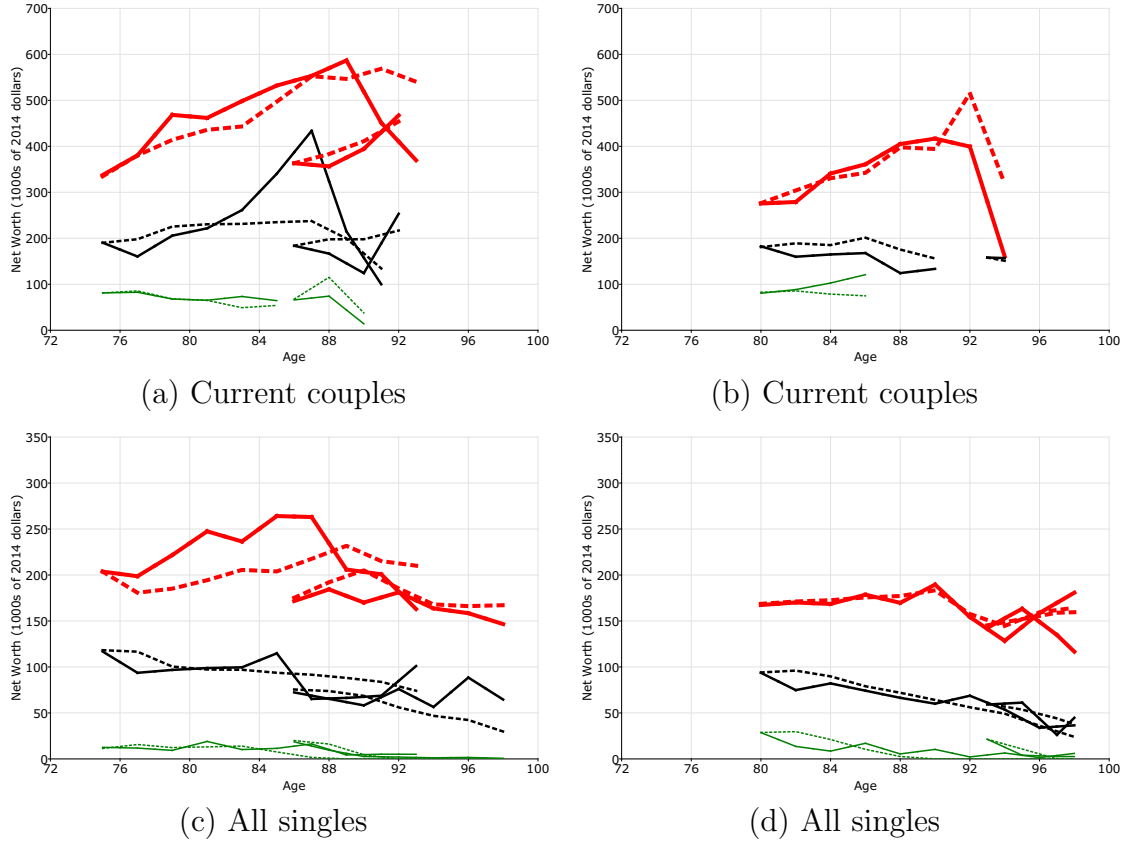


Figure A2: Median wealth. Solid lines: AHEAD cohorts ages 71-76, 83-88 in 1996 (left-hand side panels) and ages 77-82 and 89+ in 1996 (right-hand side panels). Dashed lines: model simulations.

the 75th percentile, it seems that current couples tend to save more during their retirement than singles, even given similar initial wealth. Our model, in addition to matching the median and the 75th percentile of wealth holdings by age, PI, and cohort, also does a good job of generating the differential decumulation we see for the 25th percentile.

Finally, Figure A5 compares the Medicaid reciprocity profiles generated by the model (dashed line) to those in the data (solid line) for the same birth cohorts and permanent income terciles and shows that our model matches important patterns of Medicaid usage. We reproduce the cohorts reported in the main text and add the cohorts not shown there. The model matches difference in the level of usage by age and household permanent income for all cohorts. It does especially well in capturing

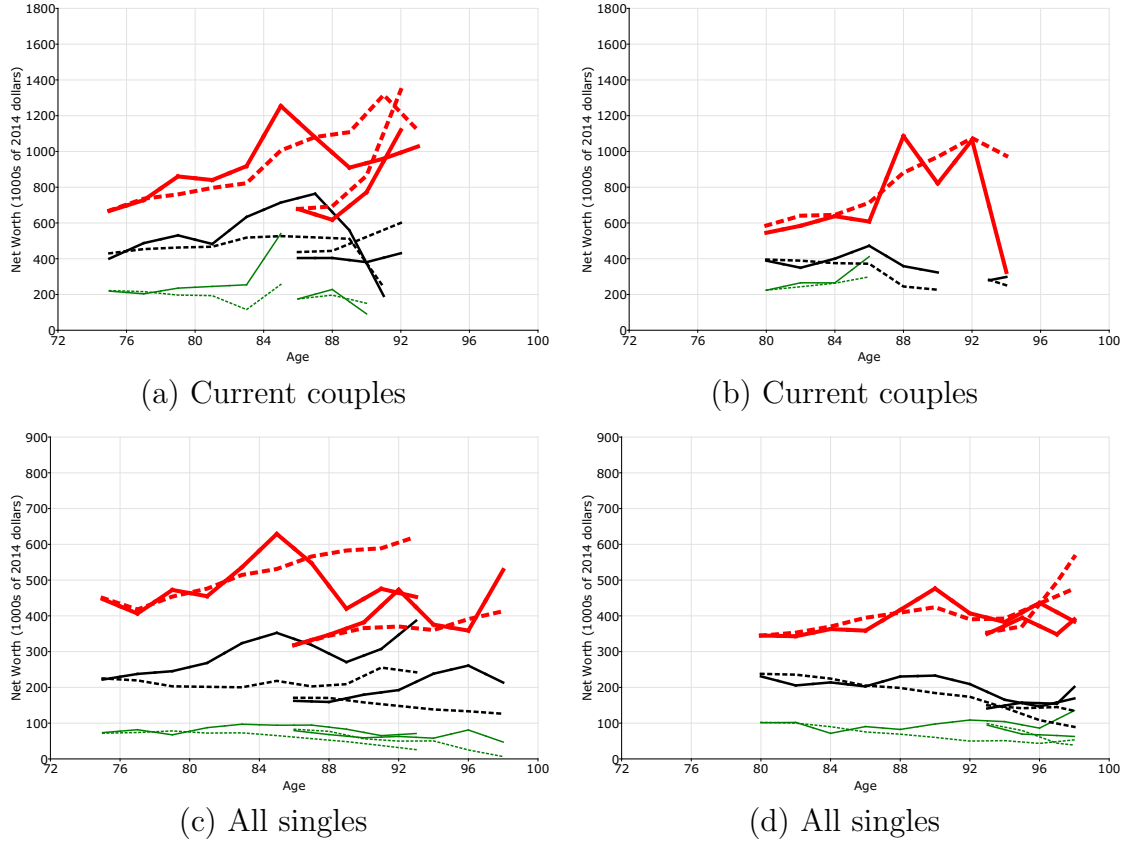


Figure A3: 75th wealth percentile. Solid lines: AHEAD cohorts ages 71-76, 83-88 in 1996 (left-hand side panels) and ages 77-82 and 89+ in 1996 (right-hand side panels). Dashed lines: model simulations.

the run-up in Medicaid use by wealthier households at very old ages.

## Appendix E: Matching methodology

We match each household that suffers a death to a household that did *not* experience a death at the same date or within the window shown in our graphs, but did experience a death within 6-10 years. (Fadlon and Nielsen (2019) impose a similar restriction in their analysis of health shocks.) More specifically, for each household we take a matched control household from the set of households who have the same initial (1996) household composition, have a PI percentile within 15 percentage points and where their 1996 wealth differs by no more than 2.5% (or \$5,000 in levels). We

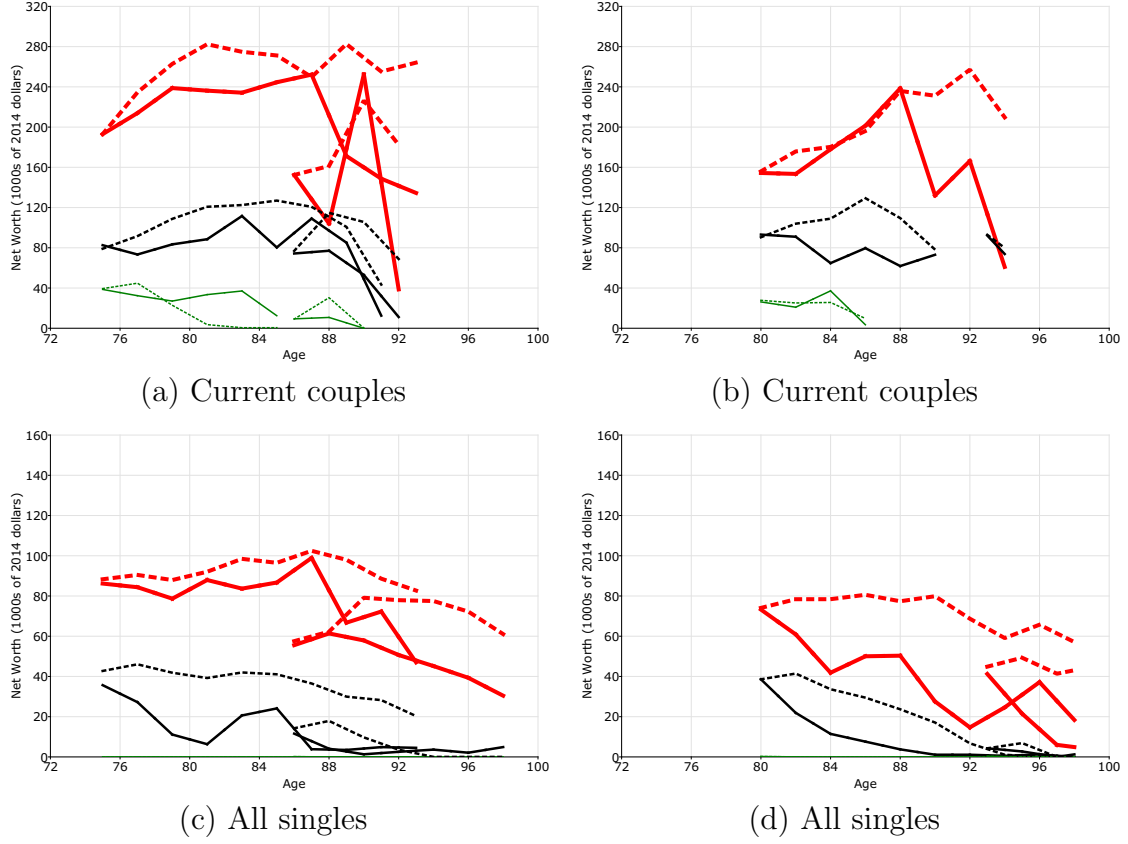


Figure A4: 25th wealth percentile. Solid lines: AHEAD cohorts ages 71-76, 83-88 in 1996 (left-hand side panels) and ages 77-82 and 89+ in 1996 (right-hand side panels). Dashed lines: model simulations.

then use a random number generator to select a single control household from this set giving each household an equal probability of being selected. Our event study specification then uses a sample of 476 households who experience the death of a spouse (2,383 household-year observations) matched to 476 households who do not experience a death in the sample window (2,624 household-year observations). Jones et al. (2020) present more results on this.

## Appendix F: Decision rules and MSM estimates

We compute the value functions by backward induction. We start with singles. At time- $T$ , we find the value function and decision rules by maximizing Equation (16),



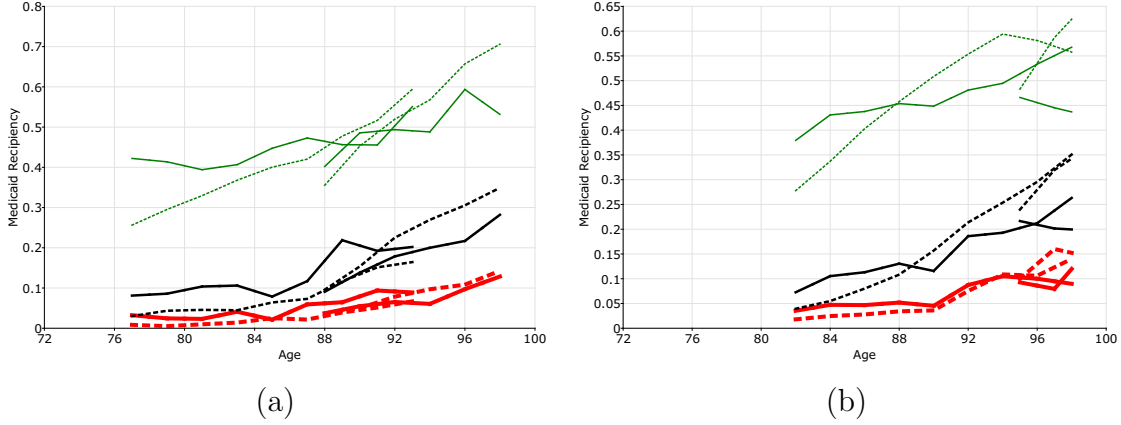


Figure A5: Medicaid Reciprocity. Solid lines: AHEAD cohorts aged 72-77, 84-89 in 1996 (Panel (a)) and ages 78-83 and 90+ in 1996 (Panel (b)). Dashed lines: model simulations.

subject to the relevant constraints, using  $V_{T+1}^g = \theta_0(x_t - c_t)$ ,  $g = h, w$ . This yields the value function  $V_T^g$ . We then find the value function and decision rules at time  $T - 1$  by solving Equation (16) with  $V_T^g$ . Continuing this backward induction yields decision rules for periods  $T - 2, T - 3, \dots, t_r$ .

We find the value function for new widows and widowers,  $V_t^{ng}$ , and the split of the estate between spousal and non-spousal heirs, by solving Equation (17), subject to the relevant constraints. These calculations utilize the value function for singles,  $V_t^g$ , described immediately above.

We find the time- $T$  value function for couples,  $V_T^c$  by maximizing Equation (19), subject to the relevant constraints and the value function for the singles, and setting the time- $T + 1$  continuation value to  $\theta_0(x_t - c_t)$ . This yields the value function  $V_T^c$  and the decision rules for time  $T$ . We then find the decision rules at time  $T - 1$  by solving Equation (19) using  $V_T^c$  and  $V_T^{ng}$ ,  $g = h, w$ . Continuing this backward induction yields decision rules for time  $T - 2, T - 3, \dots, 1$ .

More specifically, to solve our value functions, we discretize the persistent component and the transitory components of the health shock,  $\xi$  and  $\zeta$ , using the methods described in Tauchen (1986). We assume a finite number of permanent income categories and we break the space of cash-on-hand into a finite number of grid points. We use linear interpolation within the grid and linear extrapolation outside of the grid to evaluate the value function at cash-on-hand values that we do not directly compute. The end result is a set of decision rules for each possible combination of cash-on-hand, PI, health status, and persistent health shock ( $\zeta$ ).

The mechanics of our MSM approach are as follows. We compute life-cycle histories for a large number of artificial households. Each of these households is endowed with an initial value of the state vector  $(t, f_t, x_t, I, hs_t^h, hs_t^w)$  that is drawn from the data for 1996. In addition, each household is assigned the entire health and mortality history that is recorded for this same household in the AHEAD data. This way we generate attrition in our simulations that exactly follows the attrition in the data (including by initial wealth and mortality). The simulated medical expenditure shocks  $\zeta$  and  $\xi$  are Monte Carlo draws from discretized versions of our estimated shock processes. Our decision rules, combined with the initial conditions and simulated shocks, allows us to simulate a household’s wealth, medical expenses, health, and mortality.

We construct life-cycle profiles from the artificial histories in the same way that we compute them from the real data. We use these profiles to construct moment conditions and evaluate the match using our GMM criterion. As done when constructing the figures from the AHEAD data, we drop cells with fewer than 10 observations from the moment conditions. We search over the parameter space for the values that minimize the criterion. Appendix G details our moment conditions, the weighting matrix in our GMM criterion function, and the asymptotic distribution of our parameter estimates.

## Appendix G: Moment conditions and asymptotic distribution of parameter estimates

We estimate the parameters of our model in two steps. In the first step, we estimate the vector  $\chi$ , the set of parameters that can be estimated without explicitly using our model. In the second step, we use the method of simulated moments (MSM) to estimate the remaining parameters, which are contained in the  $M \times 1$  vector  $\Delta = (\nu, \eta, \phi_0, \phi_1, \kappa_0, \kappa_1, c_{min}(f_t = S))$ .

Our estimate,  $\hat{\Delta}$ , of the “true” preference vector  $\Delta_0$  is the value of  $\Delta$  that minimizes the (weighted) distance between the estimated life cycle profiles for wealth and Medicaid reciprocity in the data and those generated by the model.

For each calendar year  $t \in \{t_0, \dots, t_T\} = \{1996, 1998, \dots, 2014\}$ ,<sup>1</sup> we match the 25th, 50th and 75th percentile of wealth for 3 permanent income terciles in 4 birth-year cohorts, both for singles and couples. Because the 1996 (period- $t_0$ ) distribution of simulated wealth is bootstrapped from the 1996 data distribution, we match wealth

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<sup>1</sup>Because we do not allow for macro shocks, in any given cohort,  $t$  is used only to identify the individual’s age.

for the period 1998 to 2014, hence 9 waves. In addition, we require each cohort-income-age cell have at least 15 observations to be included in the GMM criterion. As a result, we end up with 414 wealth targets.

We construct the moment conditions for wealth by building on French and Jones (2011) (useful references include Buchinsky (1998) and Powell (1994)). Suppose that household  $i$  of family type  $f$  belongs to birth cohort  $c$  and permanent income tercile  $p$ . Let  $a_{fcqt}^q(\Delta, \chi)$  denote the model-predicted  $q$ th wealth quantile for households in household  $i$ 's group at time  $t$ .<sup>2</sup> Assuming that observed wealth has a continuous conditional density,  $a_{fcqt}$  will satisfy

$$\Pr \left( a_{it} \leq a_{fcqt}^q(\Delta_0, \chi_0) \mid f, c, p, t, \text{household } i \text{ observed at } t \right) = \pi_q,$$

where  $\pi_q$  is the probability value associated with quantile  $q$  – when  $q$  denotes a median,  $\pi_q$  would equal  $1/2$ . The preceding equation can be rewritten as a moment condition. In particular, applying the indicator function produces

$$E(1\{a_{it} \leq a_{fcqt}^q(\Delta_0, \chi_0)\} - \pi_q \mid f, c, p, t, \text{household } i \text{ observed at } t) = 0.$$

Letting  $\mathcal{J}_p$  denote the values contained in the  $p$ th permanent income tercile, we can convert this conditional moment equation into an unconditional one (e.g., Chamberlain (1992)):

$$E \left( [1\{a_{it} \leq a_{fcqt}^q(\Delta_0, \chi_0)\} - \pi_q] \times 1\{f_{it} = f\} \times 1\{c_i = c\} \times 1\{I_i \in \mathcal{J}_p\} \times 1\{\text{household } i \text{ observed at } t\} \mid t \right) = 0, \quad (\text{A17})$$

for  $q \in \{.25, .5, .75\}$ ,  $f \in \{\text{single, couple}\}$ ,  $c \in \{1, 2, 3, 4\}$ ,  $p \in \{1, 2, 3\}$ , and  $t \in \{t_1, t_2, \dots, t_T\}$ .

We also match Medicaid reciprocity rates. We divide individuals into 4 cohorts, match data from 9 waves, and stratify the data by permanent income, but combine couples and singles. Let  $\bar{u}_{cpt}(\Delta, \chi)$  denote the model-predicted reciprocity rate for households in cohort  $c$  and permanent income tercile  $p$  at time  $t$ . Let  $u_{it}$  be the  $\{0, 1\}$  indicator that equals 1 when household  $i$  receives Medicaid. The associated moment condition is

$$E \left( [u_{it} - \bar{u}_{cpt}(\Delta_0, \chi_0)] \times 1\{c_i = c\} \times 1\{I_i \in \mathcal{J}_p\} \times 1\{\text{individual } i \text{ observed at } t\} \mid t \right) = 0 \quad (\text{A18})$$

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<sup>2</sup>The elements of  $\chi$  include the permanent income boundaries.

for  $c \in \{1, 2, 3, 4\}$ ,  $p \in \{1, 2, 3\}$ , and  $t \in \{t_1, t_2, \dots, t_T\}$ .

To summarize, the moment conditions used to estimate our model consist of: the moments for wealth quantiles described by Equation (A17) and the moments for the Medicaid reciprocity rates described by Equation (A18). We have a total of  $J = 505$  moment conditions.

Suppose we have a dataset of  $I$  independent individuals that are each observed at up to  $T$  separate calendar years. Let  $\varphi(\Delta; \chi_0)$  denote the  $J$ -element vector of moment conditions described immediately above, and let  $\hat{\varphi}_I(\cdot)$  denote its sample analog. Letting  $\widehat{\mathbf{W}}_I$  denote a  $J \times J$  weighting matrix, the MSM estimator  $\hat{\Delta}$  is given by

$$\underset{\Delta}{\operatorname{argmin}} \frac{I}{1 + \tau} \hat{\varphi}_I(\Delta; \chi_0)' \widehat{\mathbf{W}}_I \hat{\varphi}_I(\Delta; \chi_0),$$

where  $\tau$  is the ratio of the number of observations to the number of simulated observations.

In practice, we estimate  $\chi_0$  using the approach described in the main text. Computational concerns, however, compel us to treat  $\chi_0$  as known in the analysis that follows.

Under the regularity conditions stated in Pakes and Pollard (1989) and Duffie and Singleton (1993), the MSM estimator  $\hat{\Delta}$  is both consistent and asymptotically normally distributed:

$$\sqrt{I} \left( \hat{\Delta} - \Delta_0 \right) \rightsquigarrow N(0, \mathbf{V}),$$

with the variance-covariance matrix  $\mathbf{V}$  given by

$$\mathbf{V} = (1 + \tau)(\mathbf{D}'\mathbf{W}\mathbf{D})^{-1}\mathbf{D}'\mathbf{W}\mathbf{S}\mathbf{W}\mathbf{D}(\mathbf{D}'\mathbf{W}\mathbf{D})^{-1},$$

where  $\mathbf{S}$  is the variance-covariance matrix of the data;

$$\mathbf{D} = \left. \frac{\partial \varphi(\Delta; \chi_0)}{\partial \Delta'} \right|_{\Delta = \Delta_0} \quad (\text{A19})$$

is the  $J \times M$  gradient matrix of the population moment vector; and  $\mathbf{W} = \operatorname{plim}_{I \rightarrow \infty} \{\widehat{\mathbf{W}}_I\}$ . Moreover, Newey (1985) shows that if the model is properly specified,

$$\frac{I}{1 + \tau} \hat{\varphi}_I(\hat{\Delta}; \chi_0)' \mathbf{R}^{-1} \hat{\varphi}_I(\hat{\Delta}; \chi_0) \rightsquigarrow \chi_{J-M}^2,$$

where  $\mathbf{R}^{-1}$  is the generalized inverse of

$$\begin{aligned} \mathbf{R} &= \mathbf{P}\mathbf{S}\mathbf{P}, \\ \mathbf{P} &= \mathbf{I} - \mathbf{D}(\mathbf{D}'\mathbf{W}\mathbf{D})^{-1}\mathbf{D}'\mathbf{W}. \end{aligned}$$

The asymptotically efficient weighting matrix arises when  $\widehat{\mathbf{W}}_I$  converges to  $\mathbf{S}^{-1}$ , the inverse of the variance-covariance matrix of the data. When  $\mathbf{W} = \mathbf{S}^{-1}$ ,  $\mathbf{V}$  simplifies to  $(1 + \tau)(\mathbf{D}'\mathbf{S}^{-1}\mathbf{D})^{-1}$ , and  $\mathbf{R}$  is replaced with  $\mathbf{S}$ .

Even though the optimal weighting matrix is asymptotically efficient, it can be biased in small samples. (See, for example, Altonji and Segal (1996).) Hence, we use a “diagonal” weighting matrix, as suggested by Pischke (1995). This diagonal weighting scheme uses the inverse of the matrix that is the same as  $\mathbf{S}$  along the diagonal and has zeros off the diagonal of the matrix.

We estimate  $\mathbf{D}$ ,  $\mathbf{S}$ , and  $\mathbf{W}$  with their sample analogs. For example, our estimate of  $\mathbf{S}$  is the  $J \times J$  estimated variance-covariance matrix of the sample data. When estimating this matrix, we use sample statistics, so that  $a_{pqt}(\Delta, \chi)$  is replaced with the sample median for group  $pqt$ .

One complication in estimating the gradient matrix  $\mathbf{D}$  is that the functions inside the moment condition  $\varphi(\Delta; \chi)$  are non-differentiable at certain data points; see equation (A17). This means that we cannot consistently estimate  $\mathbf{D}$  as the numerical derivative of  $\hat{\varphi}_I(\cdot)$ . Our asymptotic results therefore do not follow from the standard GMM approach, but rather the approach for non-smooth functions described in Pakes and Pollard (1989), (Newey and McFadden, 1994, section 7), and Powell (1994).

To find  $\mathbf{D}$ , it is helpful to rewrite equation (A17), for the case of medians, as:

$$\Pr \left( f_{it} = f \ \& \ c_i = c \ \& \ I_i \in \mathcal{J}_p \ \& \ \text{individual } i \text{ observed at } t \right) \times \left[ \int_{-\infty}^{a_{fcpt}^{\text{median}}(\Delta_0, \chi_0)} f(a_{it} \mid f, c, I_i \in \mathcal{J}_p, t) \, da_{it} - \frac{1}{2} \right] = 0. \quad (\text{A20})$$

It follows that the rows of  $\mathbf{D}$  for the median wealth moments are given by

$$\Pr \left( f_{it} = f \ \& \ c_i = c \ \& \ I_i \in \mathcal{J}_q \ \& \ \text{individual } i \text{ observed at } t \right) \times f \left( a_{fcpt}^{\text{median}} \mid f, c, I_i \in \mathcal{J}_p, t \right) \times \frac{\partial a_{fcpt}^{\text{median}}(\Delta_0; \chi_0)}{\partial \Delta'}. \quad (\text{A21})$$

In practice, we find  $f(a_{fcpt}^{\text{median}} \mid f, c, p, t)$ , the conditional p.d.f. of wealth evaluated at the median  $a_{fcpt}^{\text{median}}$ , with a kernel density estimator written by Koning (1996). The derivatives for the 25th and 75th percentiles are found in analogous fashion.

## Appendix H: First stage estimates

In the first-step estimation procedure, we estimate or calibrate those parameters that, given our assumptions, can be cleanly identified outside our model. In particular, we estimate health transitions and mortality rates from raw demographic data, estimate income profiles from the AHEAD, and calibrate the returns to saving and income taxes using external sources. We use our measure of total medical expenses (which combines data from the AHEAD and the MCBS) to estimate the process for medical expenses as a function of exogenous household-level state variables which are observed in the AHEAD.

We set the annual rate of return on saving to 4% and outline the estimation and calibration of the rest of these objects next.

### H.1 Health and mortality

Each person’s health status,  $hs^g$ , has four possible values: dead; in a nursing home; in bad health; or in good health. We allow transition probabilities for an individual’s health depend on his or her current health, age, household composition  $f$ , permanent income  $I$ , and gender  $g$ .<sup>3</sup> It follows that the elements of the health transition matrix are given by

$$\pi_{i,j,k}(t, f_{it}, I_i, g) = \Pr(hs_{i,t+2}^g = k \mid hs_{i,t}^g = j; t, f_{i,t}, I_i, g), \quad (\text{A22})$$

with the transitions covering a two-year interval, as the AHEAD interviews every other year.<sup>4</sup> We estimate health/mortality transition probabilities by fitting the transitions observed in the AHEAD to a multinomial logit model.<sup>5</sup>

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<sup>3</sup>We do not allow health transitions to depend on medical spending. The empirical evidence on whether medical spending improves health, especially at older ages, is surprisingly mixed; see, for example, the discussion in De Nardi et al. (2016a). Likely culprits include reverse causality – sick people have higher expenditures – and a lack of insurance variation – almost every retiree gets Medicare.

<sup>4</sup>As discussed in De Nardi et al. (2016a), one can fit annual models of health and medical spending to the AHEAD data. The process becomes significantly more involved, however, especially when accounting for the dynamics of two-person households.

<sup>5</sup>We do not control for cohort effects. Instead, our estimates are a combination of period (cross-sectional) and cohort probabilities. While our AHEAD sample covers 18 years, it is still too short to track a single cohort over its entire post-retirement lifespan. This may lead us to underestimate the lifespans expected by younger cohorts as they age. Nevertheless, lifespans have increased only modestly over the sample period. Accounting for cohort effects would have at most a modest effect on our estimates.

We enumerate each possible health status as follows

$$hs = \begin{cases} 0 & \text{Dead} \\ 1 & \text{Nursing Home} \\ 2 & \text{Bad Health} \\ 3 & \text{Good Health.} \end{cases} \quad (\text{A23})$$

Our multinomial logit assumption gives the following expression for health and mortality transitions

$$\pi_{i,j,k}(t, f_{it}, I_i, g) = \frac{e^{x_{it}\beta_k}}{\sum_{h=0}^3 e^{x_{it}\beta_h}} , \quad (\text{A24})$$

with  $\beta_k$  denoting the coefficient vector for future outcome  $k$ . The coefficient for death,  $\beta_0$ , is normalized to zero. We jointly estimate health transitions and survival probabilities at the individual level using a maximum likelihood estimator. We allow the transition probabilities to depend on  $x_{it}$  which includes age, sex, current health status, marital status, and permanent income. In particular we include a third order age polynomial, indicators for gender and marital status (interacted with an age quadratic), single woman (interacted with a first order age polynomial), contemporaneous indicators for health (interacted with age), and a quadratic in permanent income (interacted with a first order polynomial in age and marital status).

Using the estimated transition probabilities, we simulate demographic histories, beginning at age 70, for different gender-PI-health combinations. We report moments of these histories in Section 6.1.1.

## H.2 Imputing Medicaid payments

Our goal is to estimate the data generating process for the sum of Medicaid payments and out-of-pocket expenses: this is the variable  $\ln(m)$  in Equation (6) of the main text. The AHEAD data contain information on out-of-pocket medical spending, but not on Medicaid payments. Fortunately, the Medicare Current Beneficiary Survey (MCBS) has extremely high quality information on both Medicaid payments and out-of-pocket medical spending. One drawback of the MCBS, however, is that although it has information on marital status and household income, it does not include information on the medical spending or health of the spouse.

We use a two-step imputation procedure to exploit the strenghts of both datasets.

### **First step of imputation procedure**

We use the MCBS to infer Medicaid payments for recipients, conditional on observable variables that exist in both the MCBS and the AHEAD datasets. Let

$oop_{it}$  denote out-of-pocket medical expenses for AHEAD person  $i$  at time  $t$ , and let  $Mcd_{it}$  denote the dollar value of Medicaid payments.

To impute  $Mcd_{it}$ , we follow David et al. (1986) and French and Jones (2011) and use the following predictive mean matching regression approach. First, using every member of the MCBS sample with a positive Medicaid indicator (i.e., a Medicaid recipient), we regress the variable of interest  $Mcd$  on the vector of observable variables  $z$ , yielding  $Mcd = z\beta + \varepsilon$ . Second, for each individual  $j$  in the MCBS we calculate the predicted value  $\widehat{Mcd}_{jt} = z_{jt}\hat{\beta}$ , and for each member of the sample we calculate the residual  $\hat{\varepsilon}_{jt} = Mcd_{jt} - \widehat{Mcd}_{jt}$ . Third, we sort the predicted value  $\widehat{Mcd}_{jt}$  into deciles and keep track of all values of  $\hat{\varepsilon}_{jt}$  within each decile.

The variables  $z_{jt}$  include nursing home status, number of nights spent in a nursing home, an age polynomial, total household income, marital status, self-reported health, race, visiting a medical practitioner (doctor, hospital or dentist), out-of-pocket medical spending, education and death of an individual. Because the measure of medical spending in the AHEAD is medical spending over two years, we take two-year averages of the MCBS data to be consistent with the structure of the AHEAD. The regression of  $Mcd_{jt}$  on  $z_{jt}$  yields an  $R^2$  statistic of .67, suggesting that our predictions are accurate.

#### **Second step of imputation procedure:**

Next, for every individual  $i$  in the AHEAD sample with a positive Medicaid indicator, we impute  $\widehat{Mcd}_{it} = z_{it}\hat{\beta}$  using the value of  $\hat{\beta}$  estimated using the MCBS. Then we impute  $\varepsilon_{ic}$  for each member of the AHEAD sample by finding a random individual  $j$  in the MCBS with a value of  $\widehat{Mcd}_{jt}$  in the same decile as  $\widehat{Mcd}_{it}$  in the AHEAD, and set  $\varepsilon_{it} = \hat{\varepsilon}_{jt}$ . The imputed value of  $Mcd_{it}$  is  $\widetilde{Mcd}_{it} = \widehat{Mcd}_{it} + \varepsilon_{it}$ , and the imputed value of the sum  $m_{it}$  is  $\widetilde{m}_{it} = oop_{it} + \widetilde{Mcd}_{it}$ .

As David et al. (1986) point out, our imputation approach is equivalent to hot-decking when the “ $z$ ” variables are discretized and include a full set of interactions. The advantages of our approach over hot-decking are two-fold. First, many of the “ $z$ ” variables are continuous, and it seems unwise to discretize them. Second, we use a large number of observable variables “ $z$ ” because we find that adding extra variables greatly improving goodness of fit when imputing Medicaid payments. Even a small number of variables generates a large number of hot-decking cells because hot-decking uses a full set of interactions. Thus, in this context, hot decking is too data intensive.

We predict Medicaid payments for 3,756 household-wave observations with Medicaid reciprocity in the AHEAD and report the results of this imputation exercise in Table A2. Households where the last surviving member died between the previous and current waves of the sample have the largest imputed Medicaid payments. In



Table A2: Imputed Medicaid payments for Medicaid beneficiaries in AHEAD

Family Structure	Number of Medicaid-Eligible Households	Mean	Standard Deviation
Dead	1,040	21,800	31,500
Couples	287	15,300	25,700
Single Men	351	11,600	21,500
Single Women	2,078	12,300	21,800

contrast, couples have the smallest Medicaid payments per individual, but Medicaid payments at the household level are larger than for either single men or women. The imputed Medicaid payments for each spouse in a couple are approximately equal and the results for couples are not driven by the expenditures of only the husband or wife. In Table A2, new widows and widowers (those whose spouse has died between the current and preceding waves of the AHEAD sample) are included in the rows for single men and single women – on average the Medicaid payments of dead spouses are less than 20% of the single households’ Medicaid payments.

The distribution of imputed Medicaid expenditures in the AHEAD is close to that in the MCBS. The mean imputed Medicaid expenditure,  $Mcd_{it}$ , for Medicaid recipients in the AHEAD is \$14,050. This is lower than the corresponding value of \$16,000 in the MCBS. This difference is due to the distribution of observable variables,  $z$ , in both the MCBS and AHEAD. In particular, the number of nights in a nursing home is 20% lower in the AHEAD than in the MCBS, which is in part due to the fact that AHEAD respondents were not in a nursing home when they answered the survey for the first time.

### H.3 Medical spending

Our medical spending measure is the sum of expenditures paid out-of-pocket plus those paid by Medicaid (see Appendix H.2 for its construction). The AHEAD’s measure of medical spending is backward-looking: in each wave, the household is asked about the expenses it incurred since the previous interview.

Let  $m_{i,t}$  denote the expenses incurred by household  $i$  between ages  $t - 1$  and  $t$ . We observe household’s health at the beginning and the end of this interval, that is, at the time of the interview conducted at age  $t - 1$  and at the time of the interview

conducted at age  $t$ . We assume that medical expenses depend upon a household's PI, its family structure at both  $t - 1$  and  $t$ , the health of its members at both dates, and an idiosyncratic component  $\psi_{i,t}$ :

$$\ln m_{i,t} = m(hs_{i,t-1}^h, hs_{i,t-1}^w, hs_{i,t}^h, hs_{i,t}^w, f_{i,t-1}, f_{i,t}, I_i, t) + v_{i,t}, \quad (\text{A25})$$

$$v_{i,t} = \sigma(hs_{i,t-1}^h, hs_{i,t-1}^w, hs_{i,t}^h, hs_{i,t}^w, f_{i,t-1}, f_{i,t}, I_i, t) \times \psi_{i,t}. \quad (\text{A26})$$

We normalize the variance of  $\psi$  to 1, hence  $\sigma^2(\cdot)$  gives the conditional variance of  $v$ .

Including current and lagged family structure indicators allows us to account for the jump in medical spending that occurs in the period a family member dies. Likewise, including health indicators for both periods allows us to distinguish persistent health episodes from transitory ones.

To see how we estimate  $m(\cdot)$  and  $\sigma(\cdot)$ , write Equation (A25) as

$$\ln m_{it} = x_{1i}\beta_1 + x_{2it}\beta_2 + \vartheta_i + \varsigma_{it}, \quad (\text{A27})$$

where  $x_{1i}$  denotes a vector of time-invariant variables,  $x_{2it}$  denotes a vector of time-varying variables,  $\vartheta_i$  is an unobserved person-specific term, and  $\varsigma_{it}$  captures any remaining variation. We assume that  $E(\varsigma_{it} | \vartheta_i) = 0$ .

We estimate Equation (A27) in three steps. First, we regress log medical spending on the time-varying factors in Equation (A25), namely age, household structure, and health, and interaction terms (such as gender and PI interacted with the time varying variables) using a fixed effects estimator. In particular we regress log medical spending on a fourth order age polynomial, indicators for single man (interacted with an age quadratic), single woman (interacted with an age polynomial), the contemporaneous and lagged values of indicators for {man in bad health, married man in a nursing home, single man in a nursing home, woman in bad health, married woman in a nursing home, single woman in a nursing home}, whether the man died (interacted with age and permanent income), whether the woman died (interacted with age, and permanent income).

Because fixed effects regression cannot identify the effects of time-invariant factors, which are combined into the estimated fixed effects, in the second step we collect the residuals from the first regression, inclusive of the estimated fixed effects, and regress them on the time-invariant factors, namely a quadratic in permanent income and a set of cohort dummies. The level of  $m(\cdot)$  is set to be consistent with the outcomes of the cohort aged 71-76 in 1996.

A key feature of our spending model is that the conditional variance and the conditional mean of medical spending depends on demographic and socioeconomic factors, through the function  $\sigma(\cdot)$  shown in Equation (A26). In the third step of our

estimation procedure, we use the coefficients for  $m(\cdot)$  in hand, found in the previous two steps, to back out the residual  $v$  from Equation (A25). To find  $\widehat{\sigma^2(\cdot)}$ , we square the residuals and regress  $v^2$  on the demographic and socioeconomic variables in Equation (A26).

We assume that  $\psi_{i,t}$  can be decomposed as

$$\psi_{i,t} = \zeta_{i,t} + \xi_{i,t}, \quad \xi_{i,t} \sim N(0, \sigma_\xi^2), \quad (\text{A28})$$

$$\zeta_{i,t} = \rho_m \zeta_{i,t-2} + \epsilon_{i,t}, \quad \epsilon_{i,t} \sim N(0, \sigma_\epsilon^2), \quad (\text{A29})$$

where  $\xi_{i,t}$  and  $\epsilon_{i,t}$  are serially and mutually independent. With the variance of  $\psi_{i,t}$  normalized to 1,  $\sigma_\xi^2$  can be interpreted as the fraction of idiosyncratic variance due to transitory shocks.

We estimate the parameters of Equations (A28) and (A29) using a standard error components method. Although the estimation procedure makes no assumptions on the distribution of the error terms  $\psi_{i,t}$ , we assume normality in the simulations. French and Jones (2004) show that if the data are carefully constructed, normality captures well the far right tail of the medical spending distribution.<sup>6</sup>

Approximately 40% of the cross-sectional variation in log medical spending is explained by observables, which are quite persistent. Of the remaining cross-sectional variation, 40% comes from the persistent shock  $\zeta$  and 60% from the transitory shock  $\xi$ . In keeping with the results in Feenberg and Skinner (1994), French and Jones (2004) and De Nardi et al. (2010), we estimate substantial persistence in the persistent component, with  $\rho_m = 0.85$ .

## H.4 The tax system

We parameterize the tax system using the functional form developed by Gouveia and Strauss (1994). Average tax rates for total pre-tax income,  $y$ , are given by

$$t(y, \tau_{f_t}) = b_{f_t} [1 - (s_{f_t} y^{p_{f_t}} + 1)^{\frac{-1}{p_{f_t}}}], \quad (\text{A30})$$

where  $b_{f_t}$ ,  $s_{f_t}$  and  $p_{f_t}$  are parameters of the tax system that can differ between couples and singles, and  $\tau_{f_t} = (b_{f_t}, s_{f_t}, p_{f_t})$  is their union. We use the estimates of  $\tau$

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<sup>6</sup>To help us match the distribution of medical spending, we bottom code medical spending at 10% of average medical spending. French and Jones (2004) also bottom code the data to match the far right tail of medical spending. Because we include Medicare B payments in our medical spending measure, which most elderly households pay, for the vast majority of households these bottom coding decisions are not important.

for married and singles households with no children provided by Guner et al. (2014). After-tax income  $\Upsilon(y, \tau_{f_t})$  is then

$$\Upsilon(y, f_t) = (1 - t(y, \tau_{f_t})) \times y. \quad (\text{A31})$$

To reflect differences in the generosity of Medicaid, and other means tested social insurance programs available to the elderly, between couples and singles we impose that the consumption floor for couples is 150% of the value we estimate for singles.

## Appendix I: Identification and sensitivity

In this appendix, we document how changes in our seven second-step estimated parameters affect our model's implications for the savings of couples and singles and for Medicaid reciprocity. To do this, we change each of our estimated parameters while holding all other parameters fixed at their baseline estimated values. Figures A6 - A12 show how changing each parameter affects the life-cycle profiles of couples' and singles' savings, Medicaid reciprocity, and non-medical consumption.

The first row of Table A3 decomposes the GMM criterion for our baseline estimates between the moments related to singles' wealth, couples' wealth and Medicaid reciprocity. Because we use a diagonal weighting matrix, the GMM criterion function is the sum of the squared moment conditions multiplied by their respective weights, making the decomposition trivial. (The weight for each moment is the inverse of the variance of that moment condition.) We simply assign each moment to the proper category and calculate weighted squared sums. The other rows of this table display how the GMM criterion and its components change as we vary one parameter at a time.

Figure A6 shows the effects of reducing the equivalence scale  $\eta$  by 10 percent. (In this and all other Figures in the current section, solid lines denote profiles from the baseline model and dashed lines denote profiles from the model with modified parameters.) This parameter change implies that couples become more efficient in transforming household consumption expenditures into the consumption goods and services from which they derive utility; in other words, there are larger economies of scale from being in a couple. Because  $\eta$  does not enter the utility function of initial singles, their savings are unaffected by this change. But for couples, a lower value of  $\eta$  implies that, holding household consumption expenditures constant, effective consumption rises and the marginal utility of consumption falls. Hence, consumption expenditures made when married become less valuable relative to expenditures made when single. This in turn raises the savings of couples, because they expect to

Table A3: Effect of Parameter Changes on GMM Criteria.

	Singles' Wealth	Couples' Wealth	Medicaid Reciprocity	Total
Baseline	1059	154	421	1634
$\eta$ decreased 10%	1077	177	423	1676
Final Bequest Motive				
· MPB Decreased 10%	1301	161	431	1893
· Threshold Halved	2244	229	407	2880
Bequest Motive at Death of First Spouse				
· MPB decreased by 10%	1198	157	415	1770
· Threshold halved	1158	213	443	1814
$\nu$ decreased 10%	1140	155	447	1742
$c_{min}(\cdot)$ increased by 10%	1139	156	442	1736

become single in the future, and thus the savings held by the newly single. The second row of Table A3 shows that these changes worsen the model’s fit along all moment categories.

Figures A7 and A8 show the effects of changing the terminal bequest motive that applies when there is no surviving spouse. In particular, we change the corresponding marginal propensity to bequeath, rather than consume, out of wealth in the final period before certain death (MPB), as defined in equation (A6), and the threshold at which the bequest motive becomes operative, defined in equation A7. Both of these objects are functions of the bequest parameters  $\phi_0$  and  $\kappa_0$ . To ease interpretation, we scale both the MPB and the threshold to an annual frequency. (See Appendix A.2.)

Table A3 and the figures show that the final bequest parameters impact the savings of singles more than those of couples. This makes sense for two reasons. First, a married household containing two members is more likely to survive to future periods (in some form) than a single individual. Second, couples attach value to the “side bequests” made when one spouse dies, a transfer not relevant to singles. Both of these alternatives make couples more willing to save for reasons not related to final bequests.

Figure A7 shows that the effects of lowering the MPB depend on the household’s PI: only households who are rich enough to have an operative bequest motive are affected. In contrast, Figure A8 shows that lowering the threshold where the

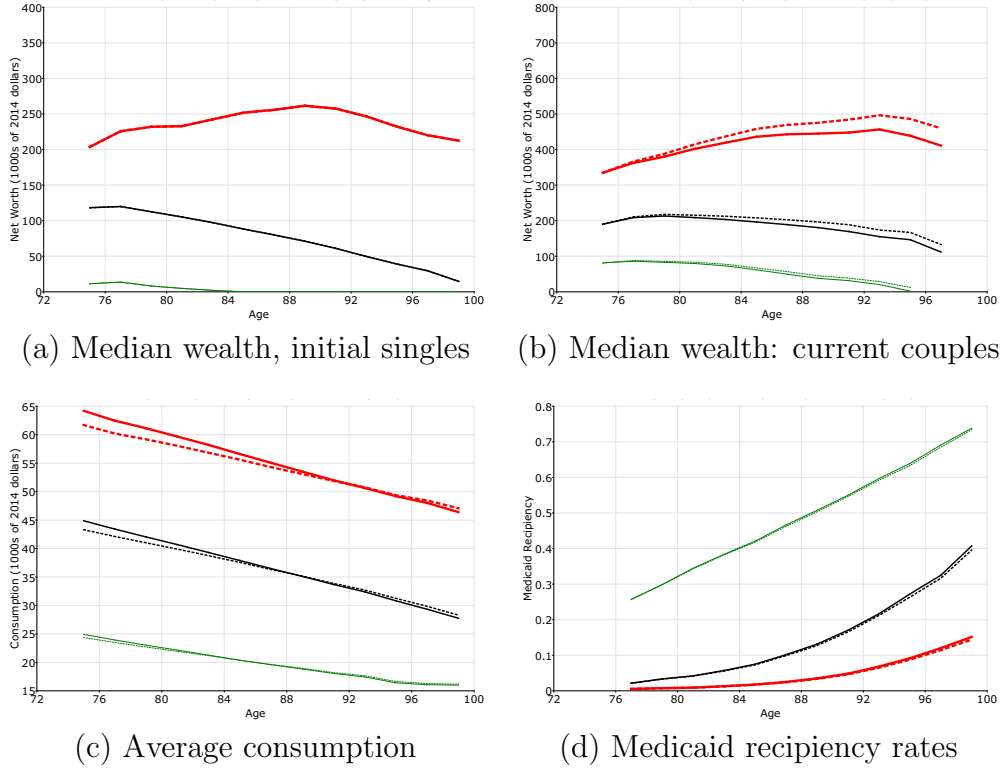
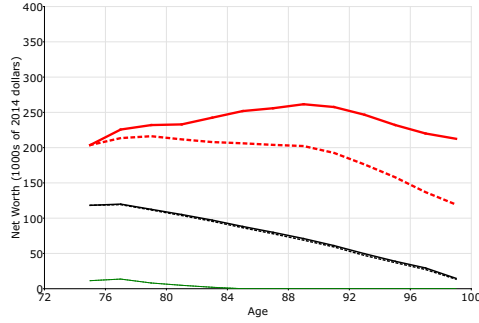


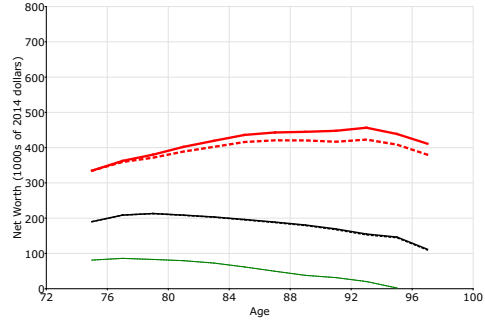
Figure A6: Effects of Decreasing  $\eta$  by 10 Percent

bequest motive becomes operative affects households across much of the PI and wealth distribution.

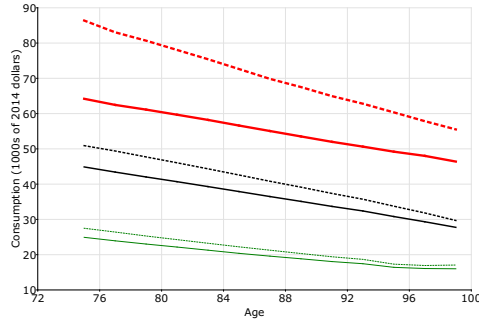
More generally, decreasing the MPB leads to counterfactually low savings rates, especially for singles (who have shorter life spans) and for those with high income (for whom the bequest motive is more likely to be operative). The GMM criterion worsens across all moment categories. Lowering the threshold, and thus making the bequest motive operative for more households, leads to counterfactually high savings rates across the PI distribution. This, too, worsens the model's fit of the wealth moments. At the same time, however, the higher savings rates of middle and high-PI households reduces their Medicaid reciprocity, improving the match along this dimension. These differences help us differentiate the two bequest-related parameters during estimation.



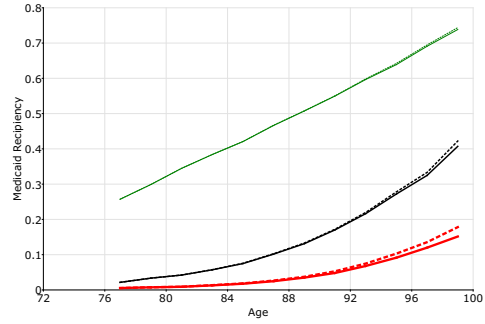
(a) Median wealth, initial singles



(b) Median wealth: current couples

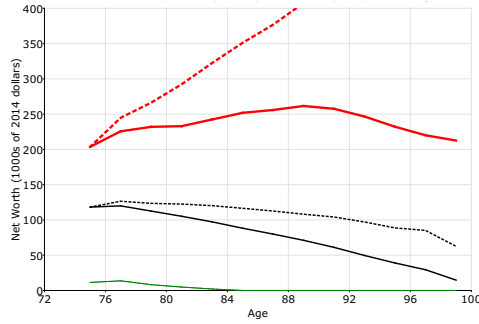


(c) Average consumption

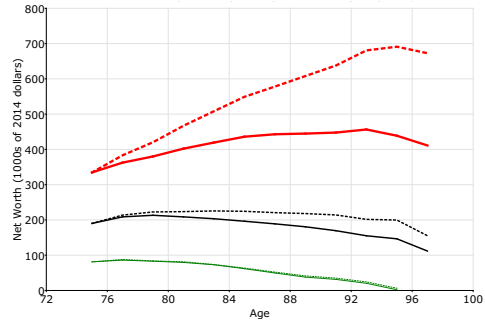


(d) Medicaid reciprocity rates

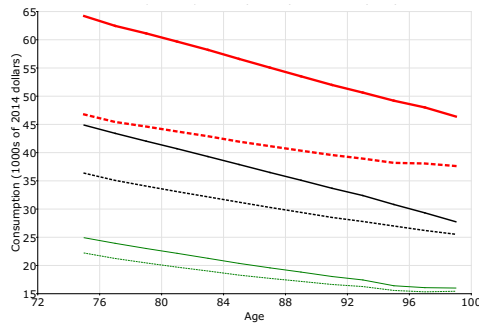
Figure A7: Effects of Decreasing MPB for Final Bequests by 10 Percent



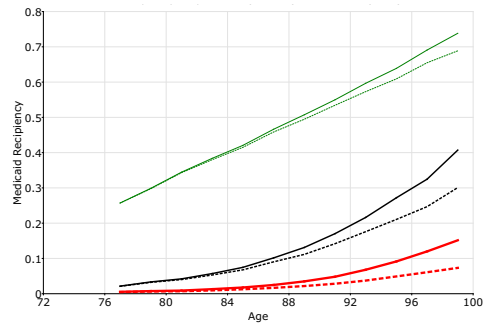
(a) Median wealth, initial singles



(b) Median wealth: current couples



(c) Average consumption



(d) Medicaid reciprocity rates

Figure A8: Effects of Halving Bequest Threshold for Final Bequests

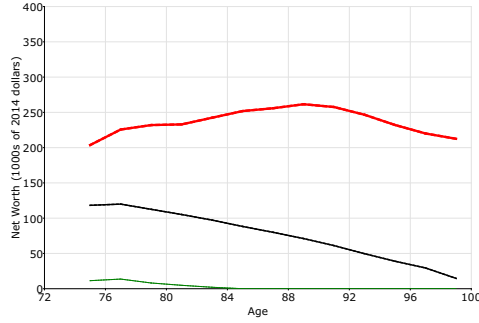
Next, we repeat the exercise of lowering the MPB and the bequest threshold with the bequest parameters that apply at the death of the first spouse ( $\phi_1$  and  $\kappa_1$ ). These changes worsen the overall fit of the model substantially. Similarly to final bequests, decreasing the MPB affects the households who are most likely to leave side bequests, leading these couples to hold less wealth (see Figure A9). Likewise, lowering the threshold affects saving rates further down the PI and wealth distributions (Figure A10).

Changing the bequest parameters in effect when the first spouse dies has no effect on the behavior of initial singles. However, the effect of decreasing the MPB is transmitted to people who become widowers or widows, as couples leave a larger share of their wealth to their surviving spouses. Even though couples hold less wealth in total, the increased share raises the amount transferred to survivors and thus raises the savings of singles as a whole. Their Medicaid reciprocity rates fall, albeit modestly, as well. Decreasing the threshold at which the bequest motive becomes operative has the opposite effect. Couples accumulate more wealth but bequeath a larger share of their wealth to non-spousal heirs. This lowers the wealth of singles as a whole and raises Medicaid reciprocity rates, because surviving spouses have less wealth with which to self-insure against high medical expenses.

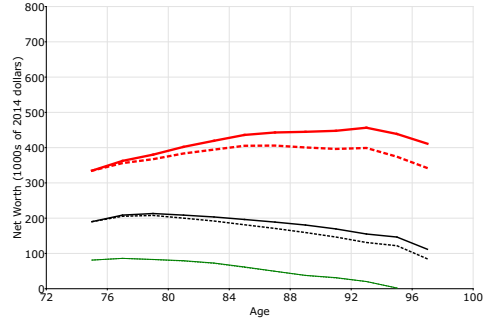
Figure A11 shows that reducing the coefficient of relative risk aversion ( $\nu$ ) by 10% reduces the wealth holdings of both couples and singles and raises Medicaid reciprocity. Lower risk aversion implies less precautionary saving and consequently less wealth overall. It also implies a smaller utility loss from receiving the consumption floor, as opposed to higher levels of consumption, thus encouraging higher Medicaid reciprocity. The penultimate row of Table A3 shows that these changes worsen the model's fit across all moment categories.

Figure A12 presents the effects of increasing the consumption floor  $c_{min}$  by 10%. This change gives households more insurance against high medical expenses, and lowers their desire for precautionary savings. The effect is strongest at the 25th percentile of the conditional wealth distribution, where households are more exposed to medical expense risk and more likely to receive Medicaid in the future. This change also worsens the model's fit.

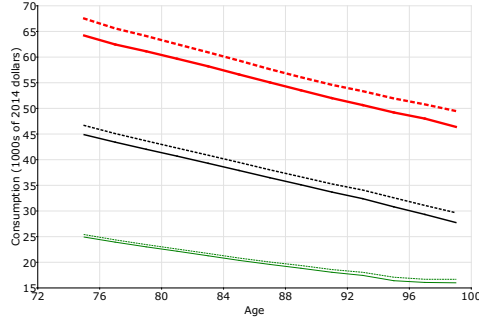




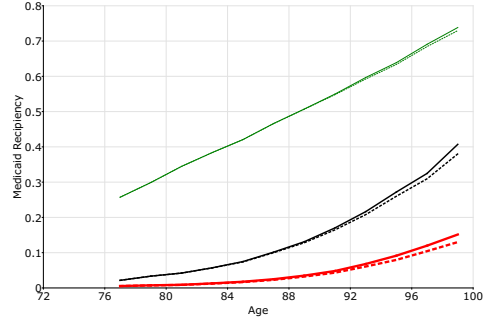
(a) Median wealth, initial singles



(b) Median wealth: current couples

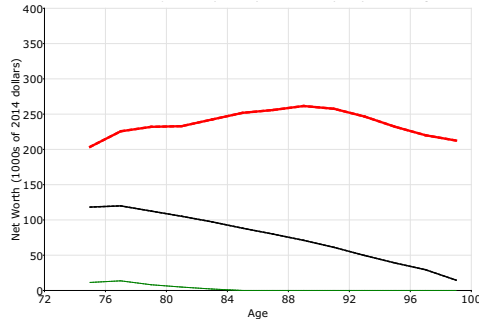


(c) Average consumption

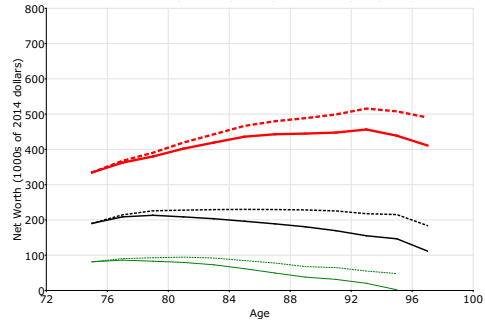


(d) Medicaid reciprocity rates

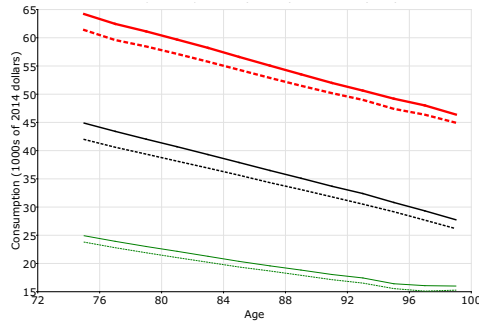
Figure A9: Effects of Decreasing MPB for Side Bequests by 10 Percent



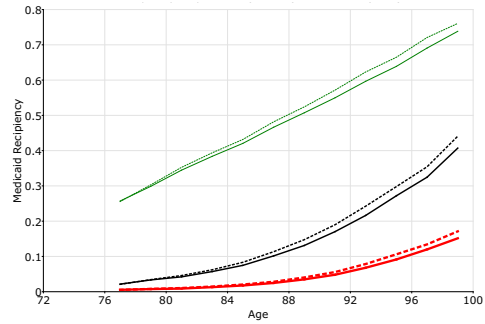
(a) Median wealth, initial singles



(b) Median wealth: current couples

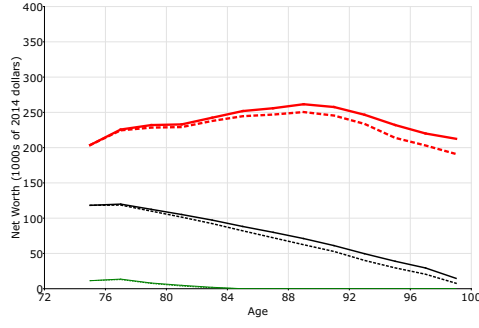


(c) Average consumption

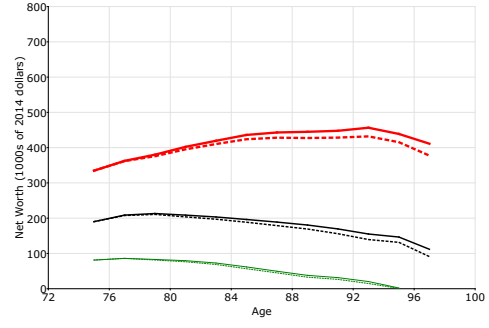


(d) Medicaid reciprocity rates

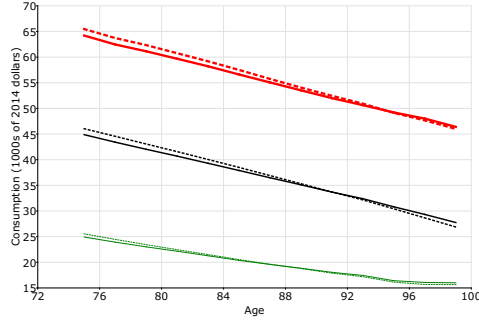
Figure A10: Effects of Halving Bequest Threshold for Side Bequests



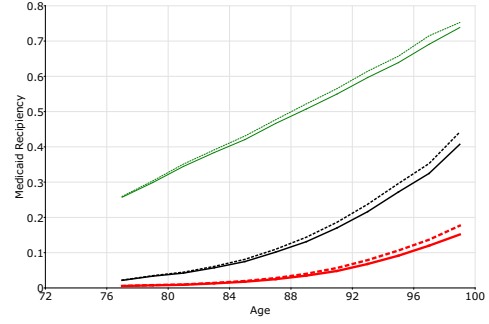
(a) Median wealth, initial singles



(b) Median wealth: current couples

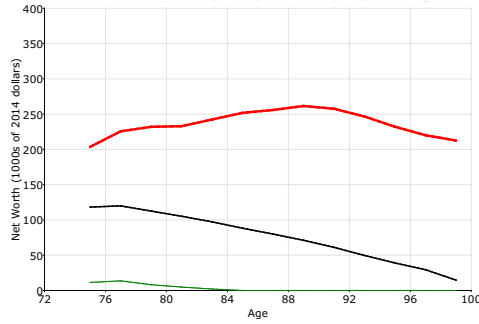


(c) Average consumption

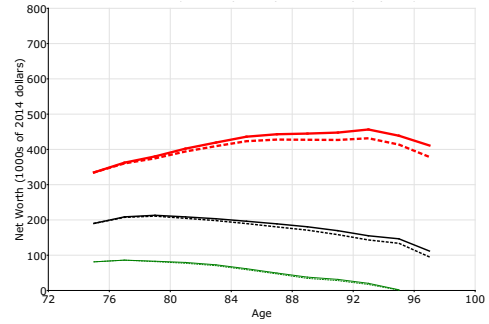


(d) Medicaid reciprocity rates

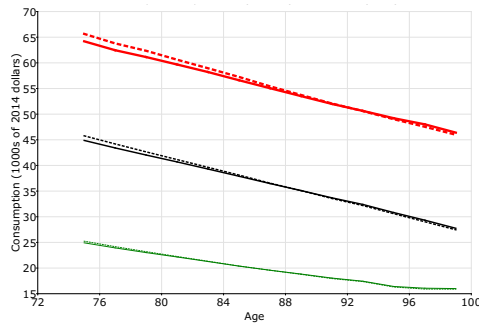
Figure A11: Effects of Decreasing  $\nu$  by 10 Percent



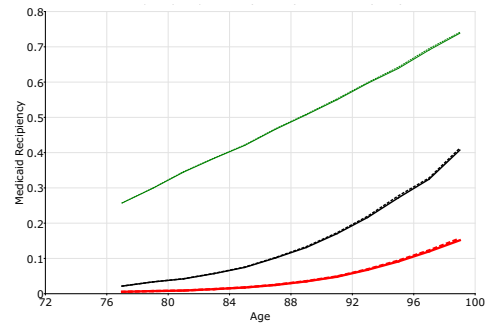
(a) Median wealth, initial singles



(b) Median wealth: current couples



(c) Average consumption



(d) Medicaid reciprocity rates

Figure A12: Effects of Increasing  $c_{min}(\cdot)$  by 10 Percent

Figures A11 and Figure A12 show that decreasing risk aversion and lowering the consumption floor can generate similar changes in savings. This highlights that it can be difficult to separately identify these model parameters only using data on household wealth.

Importantly, however, these two parameters have different implications for Medicaid reciprocity rates. Decreasing risk aversion raises Medicaid reciprocity rates by reducing wealth accumulation. As Figure A11 shows, this effect is concentrated at older ages, when households face large remaining medical spending risk and the decreases in wealth are the largest. Moreover, the effect is similar across the PI distribution. In contrast, increasing the generosity of the consumption floor raises Medicaid reciprocity even if saving is unchanged. Figure A12 shows that this effect is largest for low PI households, who are both more likely to rely on Medicaid and more likely to receive Medicaid at younger ages. Thus Medicaid reciprocity rates rise for low-PI households at all ages when the generosity of the consumption floor is increased, and by more than for high-PI households. In sum, relative to lowering risk aversion, raising the consumption floor is more likely to increase Medicaid usage at younger ages and lower PI ranks. Medicaid reciprocity rates are thus essential to identifying the level of risk aversion separately from the value of the consumption floor.

## Appendix J: Are side bequests and terminal bequests different?

To consider whether side bequests and terminal bequests are different, this appendix reports a specification where we restrict the two sets of parameters governing bequests to be equal. To sum, this restriction worsens the model's ability to fit the data and generates different bequest behavior. The details are as follows.

Table A4 reports an alternative specification of the bequest motive where we restrict both the weight ( $\phi_1 = \phi_0$ ) and curvature ( $\kappa_1 = \kappa_0$ ) of the bequest utility function to be the same when any member of the household dies ( $\theta_1 = \theta_0$ ). Column (2) of the table provides the parameter estimates for this alternative specification, while column (1) reports our baseline parameter estimates for comparison. While all parameters in our model are jointly identified, it is reassuring that only the estimated bequest motives change by large amounts in the alternative specification. The fit of our model, as measured by the GMM criterion function, declines when we impose this equality constraint in estimation.

Figure A13 shows that the common-bequest specification also worsens the model's prediction of the asset decline at the death of the first spouse. Panel (a) of the figure

Table A4: Estimated second-step parameters

	Baseline (1)	One Bequest (2)
$\eta$ : consumption equivalence scale	1.528 (0.195)	1.526 (0.190)
$\phi_0$ : bequest intensity, single (in 000s)	6,826 (1,208)	104 (18)
$\kappa_0$ : bequest curvature, single (in 000s)	3,517 (352)	1,152 (150)
$\phi_1$ : bequest intensity, surviving spouse	4,447 (656.1)	104
$\kappa_1$ : bequest curvature, surviving spouse (in 000s)	211.2 (23.28)	1,152
$\nu$ : coefficient of RRA	3.701 (0.096)	3.641 (0.169)
$c_{min}(f = 1)$ : annual consumption floor, singles	4,101 (124)	4,118 (156)

*Note:* Standard errors in parentheses. We set  $c_{min}(f = 2) = 1.5 \cdot c_{min}(f = 1)$ .

shows results for our baseline specification, while Panel (b) shows results for the alternative specification. Comparing the panels indicates that model estimates that do not allow for marital state dependence generate a smaller decline in wealth relative to the data.

## Appendix K: Relaxing common preferences for couples and singles

We assume that couples and singles have common preferences and differ only because couples derive utility from side bequests at the death of the first spouse and enjoy economies of scale in consumption. To assess the robustness of our results to these assumptions, we estimate the model only for singles (and hence only estimate the parameters for singles) on data for those who were single when first observed. Overall, we find that the parameters estimated for singles only (which are not constrained to be the same as those for couples) are close to our the estimates from our

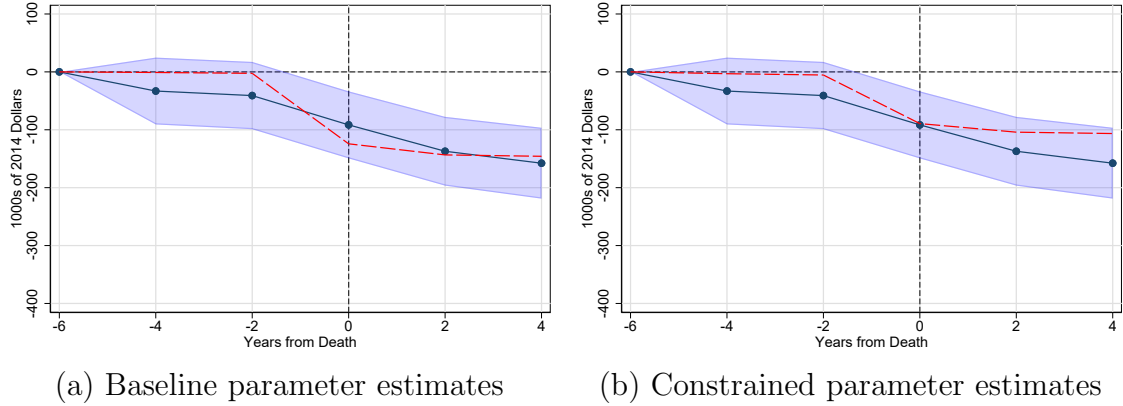


Figure A13: Average change in wealth around death of a spouse for initial couples using our baseline estimates and constrained estimates. Differences-in-differences estimates (solid blue line) and their 95% confidence interval (shaded region) from the AHEAD data and differences-in-differences estimates (dashed red line) from model-simulated data. Death dates are centered at year 0.

baseline model (that is, the one with couples and singles).

More specifically, Table A5 shows that the coefficient of relative risk aversion and consumption floor estimated for the singles-only model differ modestly from the baseline model. The estimated coefficient of relative risk aversion from our singles-only model is 12% smaller than the one from our baseline model. Likewise, the estimated consumption floor from our singles-only model is 9% smaller than the one from our baseline model. These gaps are small compared to the wide range of estimates from the literature.

Table A5: Estimated second-step parameters.

	Baseline	Initial Singles Only
$\nu$ : coefficient of RRA	3.701	3.275
$c_{min}(f = 1)$ : annual cons. floor, singles	4,101	3,734

Similarly, we show that our estimated bequest motives for the singles only and the baseline model are comparable. Because the bequest parameters are difficult to interpret, Figure A14 reports what the estimated parameters imply in terms of the share of expenditures that goes to bequests, rather than own consumption, for a person who dies with certainty next period. The left-hand-side panel compares

the implied shares for the singles only and the baseline model and shows that the differences are small compared to the range of estimates for singles in the literature, which we report in the right-hand-side panel.

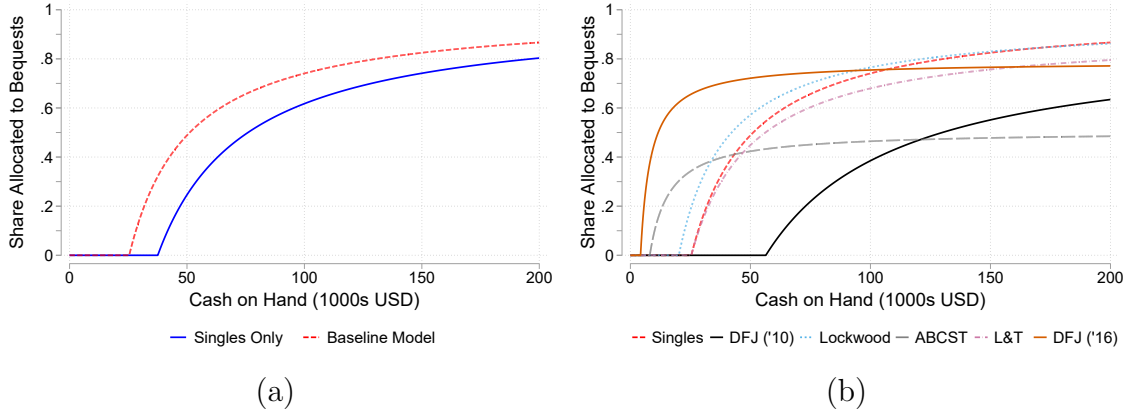


Figure A14: Estimated Bequest Motives. Panel (a): expenditure share allocated to bequests for singles facing certain death in the next period in the baseline (solid) and initial singles subsample (dashed) estimations. Panel (b): comparing our baseline results for singles (dashed red) with those in De Nardi et al. (2010) (DFJ '10), De Nardi et al. (2016a) (DFJ '16), Lockwood (2018), Ameriks et al. (2020) (ABCST), and Lee and Tan (2019) (L&T).

## Appendix L: Untargeted model fits and implications

Because individuals who are single, poor or sick die at younger ages, in an unbalanced panel the sample composition changes over time, introducing mortality bias. Figure A15 compares the mortality bias found in the AHEAD data (left panel) with that predicted by the model (right panel). The solid lines show median wealth for all households (both singles and couples) observed at a given point in time, even if all members died in a subsequent wave, that is, the unbalanced panel. The dashed lines show median wealth for the subsample of households with at least one member still alive in the final wave, that is, the balanced panel. They show that the wealth profiles for households who survived to the final wave (the balanced panel) have much more of a downward slope. The difference between the two sets of profiles confirms that people who died during our sample period tended to have lower wealth than the survivors.

Our model matches the extent of the mortality bias found in the data, without being required to do so by construction. As in the data, restricting the profiles to long-term survivors reveals much more wealth decumulation.

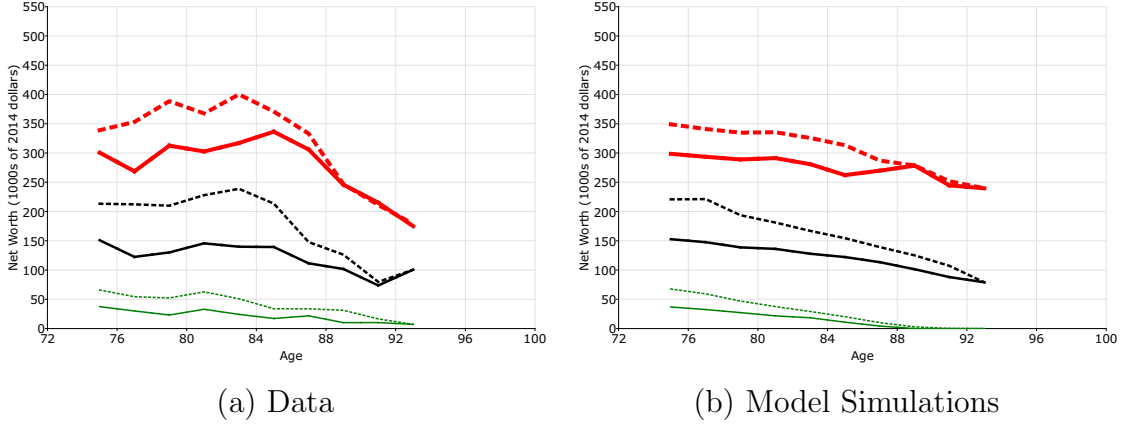


Figure A15: Mortality Bias. Solid lines: all household in the data at a given point in time. Dashed lines: households with at least one member surviving to 2014.

Figure A16 Reports the fit of Medicaid reciprocity by marital status that is implied by our estimates. It shows that the goodness of fit is similar for these two groups.

Our estimation matches multiple wealth quantiles by PI tercile for single men and women combined. One might wonder, given the difference in life expectancy for men and women, to what extent our model matches wealth trajectories for each gender. Figure A17 shows median wealth by gender from the AHEAD data and the model simulations for two cohorts of initial singles. In the interest of space, we do not report the graphs for all of the other wealth moments (namely the 25th and 75th wealth percentiles and the other two cohorts), as they convey the same message in terms of fit by gender.

Our parsimonious model (seven estimated parameters and about 500 target moments) not only matches the key features of the data unconditional on gender, but also does not generate systematic discrepancies in fit between men and women. Looking more closely reveals that our model produces a slightly closer match of the moments of initially single women. However, this is a natural consequence of our estimation procedure, which targets the moments for all surviving singles and the fact that women make for a much larger share of the older population than men. Nevertheless, our model matches the key patterns of saving by gender, permanent income, age and cohort for singles.

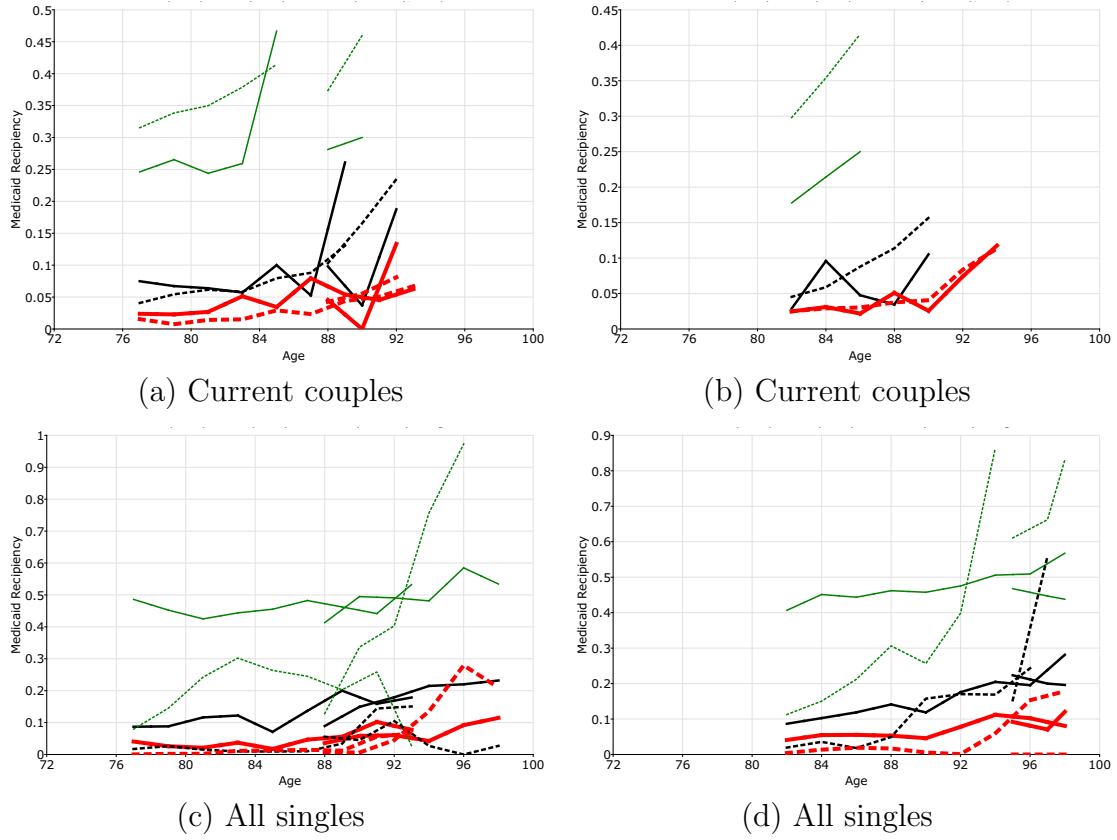


Figure A16: Medicaid Reciprocity. Solid lines: AHEAD cohorts ages 71-76, 83-88 in 1996 (left-hand side panels) and ages 77-82 and 89+ in 1996 (right-hand side panels). Dashed lines: model simulations.

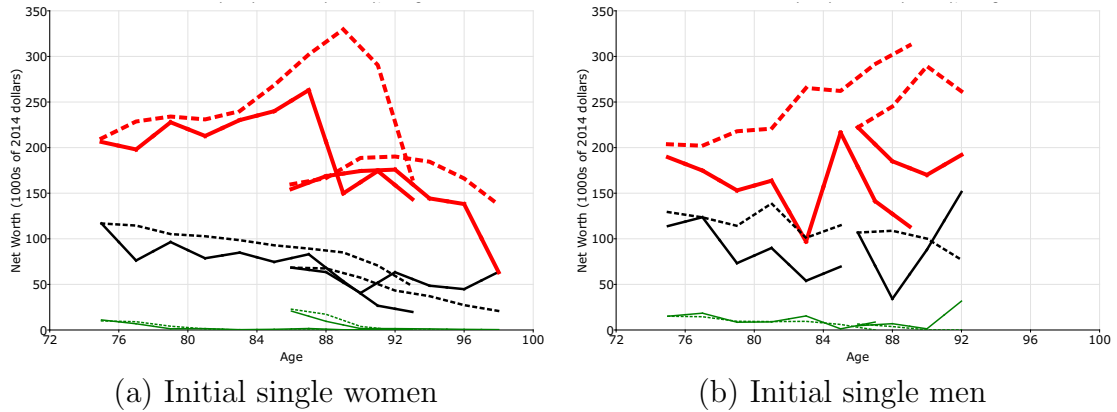


Figure A17: Median wealth of initial singles by gender. Solid lines: AHEAD cohorts aged 71-76, 83-88 in 1996. Dashed lines: model simulations.



Figure A18 compares the 90th percentile of the wealth distribution generated by the model (dashed line) to those in the data (solid line) for all of the birth cohorts and permanent income terciles that we match in estimation, including the cohorts not reported in the main text.

As with our targeted moments, the model does a good job of matching the 90th percentile of wealth holdings across PI groups and ages, both for singles and couples. For couples in the top PI-tercile, we produce too much saving relative to the data moments, however, we closely match the equivalent untargted moments for singles in the top PI-tercile.

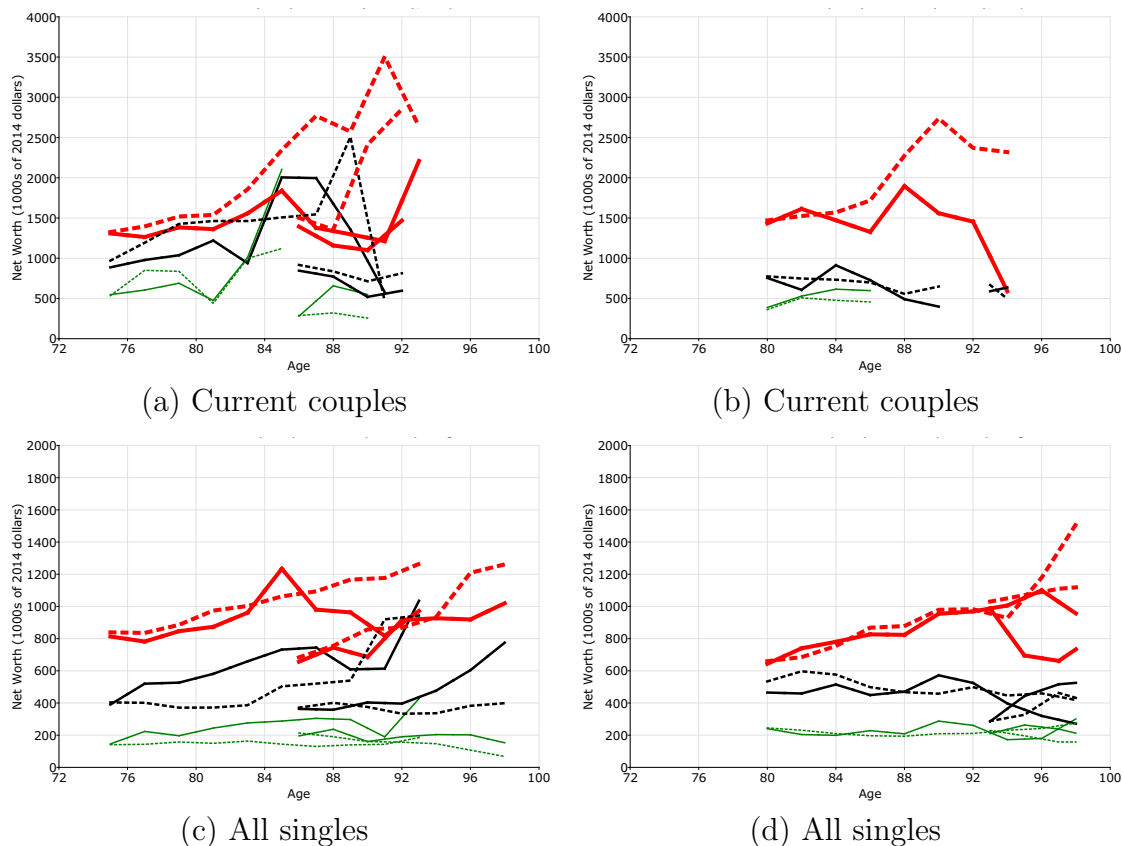


Figure A18: 90th wealth percentiles. Solid lines: AHEAD cohorts ages 71-76, 83-88 in 1996 (left-hand side panels) and ages 77-82 and 89+ in 1996 (right-hand side panels). Dashed lines: model simulations.

Figures A19 and A20 extend the event study comparisons shown in Figure 9 by assessing the model's fit of the medical spending and wealth dynamics around the death of the first spouse for each PI tercile and three age groups. In general the model fits well.

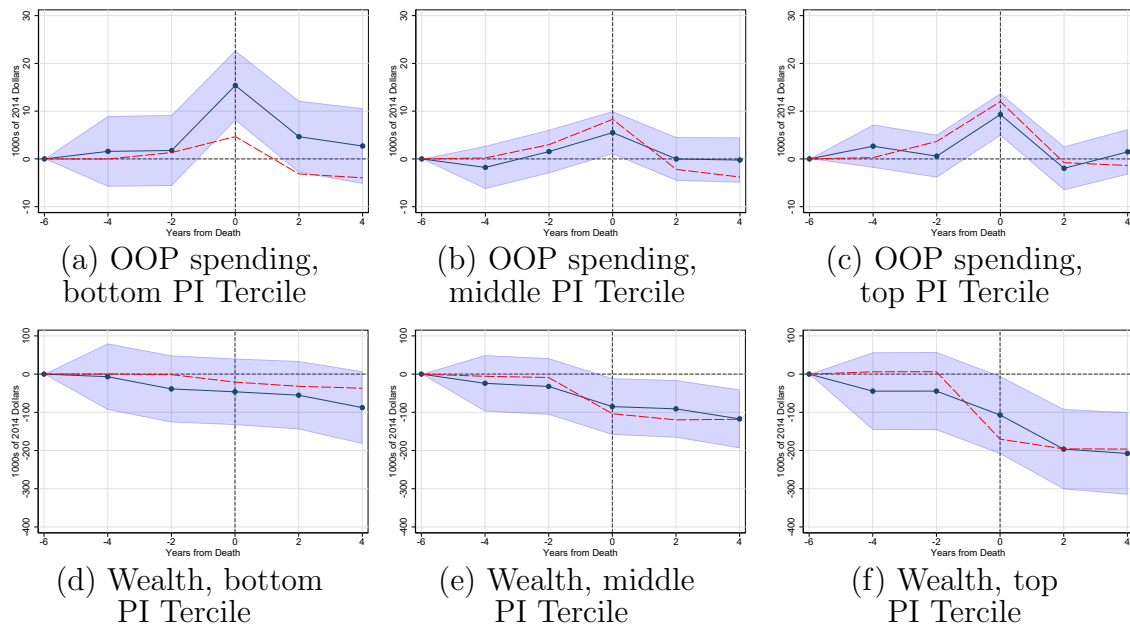


Figure A19: Average change in out-of-pocket medical spending and wealth around death of a spouse for initial couples, by PI tercile. Differences-in-differences estimates (solid blue line) and their 95% confidence interval (shaded region) from the AHEAD data and differences-in-differences estimates (dashed red line) from model-simulated data. Death dates are centered at year 0.

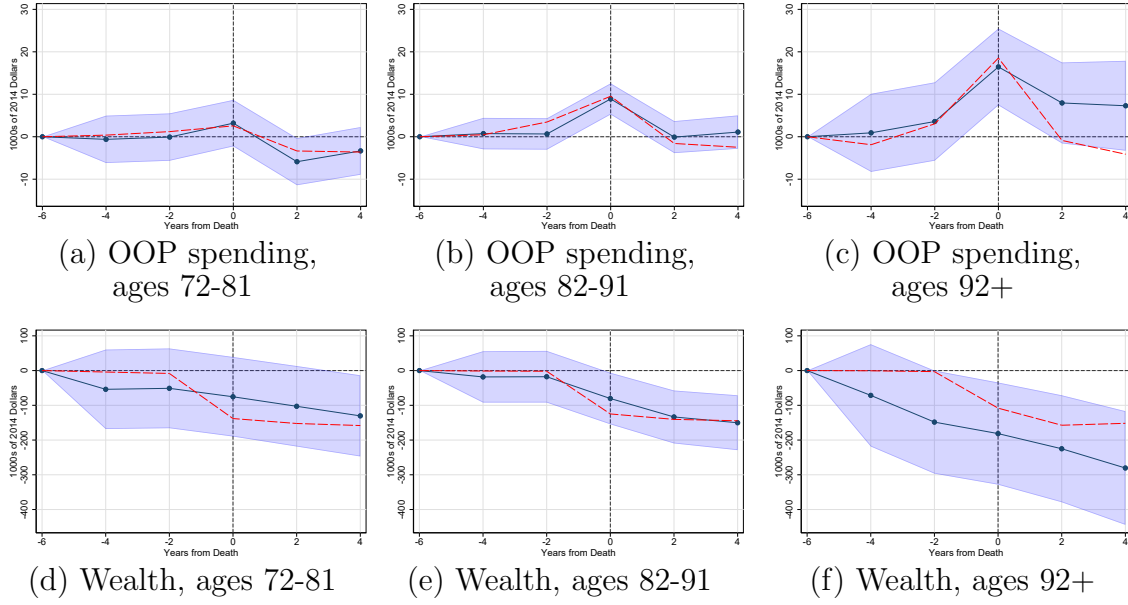


Figure A20: Average change in out-of-pocket medical spending and wealth around death of a spouse for initial couples, by age group. Differences-in-differences estimates (solid blue line) and their 95% confidence interval (shaded region) from the AHEAD data and differences-in-differences estimates (dashed red line) from model-simulated data. Death dates are centered at year 0.

The implications of our estimated spending process for lifetime medical spending are shown in Figure A21, where we use the medical spending simulations shown in Figure 5 to calculate discounted sums for the households still alive (or just deceased) at each age. Panel (a) of the figure shows that at age 77, single households will on average incur \$72,000 of medical expenses over the remainders of their lives, and that nearly 10% of them will incur medical expenses in excess of \$152,000. The corresponding values for initial couples are \$134,000 for the mean and \$250,000 for the 90th percentile. The spending statistics for singles rise with age until age 91. This is not merely an artifact of mortality bias. Although older people have less time to live, Figure 5 shows that medical expenses rise with age. In other words, at any point in time, most survivors have yet to incur the bulk of their lifetime expenses. As De Nardi et al. (2010) and others have pointed out, this “backloading” of medical expenses gives it the potential to be an important driver of saving. In contrast, as couples become singles their medical expenses fall.

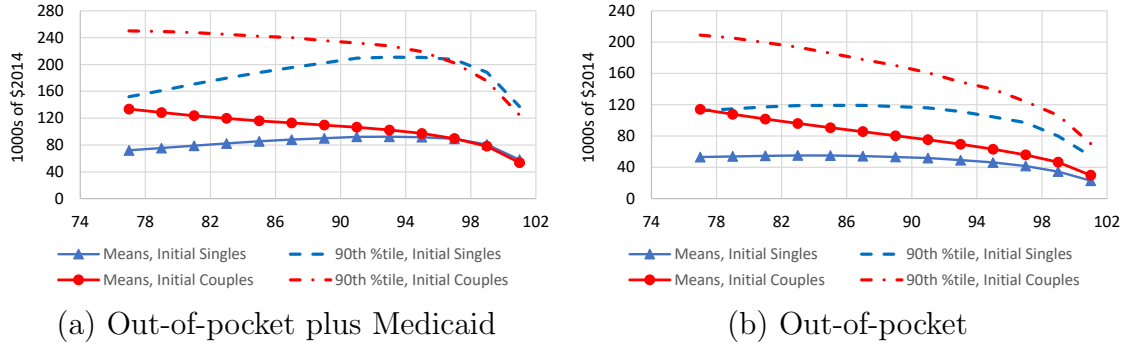


Figure A21: Mean and 90th percentile of remaining lifetime medical spending for surviving households, initial singles and initial couples.

Panel (b) shows the same profiles for out-of-pocket spending, with Medicaid removed. Comparing panels (a) and (b) shows that Medicaid is more prevalent at older ages and among singles. Given that older households are more likely to face high medical expenses, and single households are more likely to be poor, both patterns follow from with Medicaid’s means-tested structure.

Figures A22 and A23 report the same information disaggregated by PI tercile.

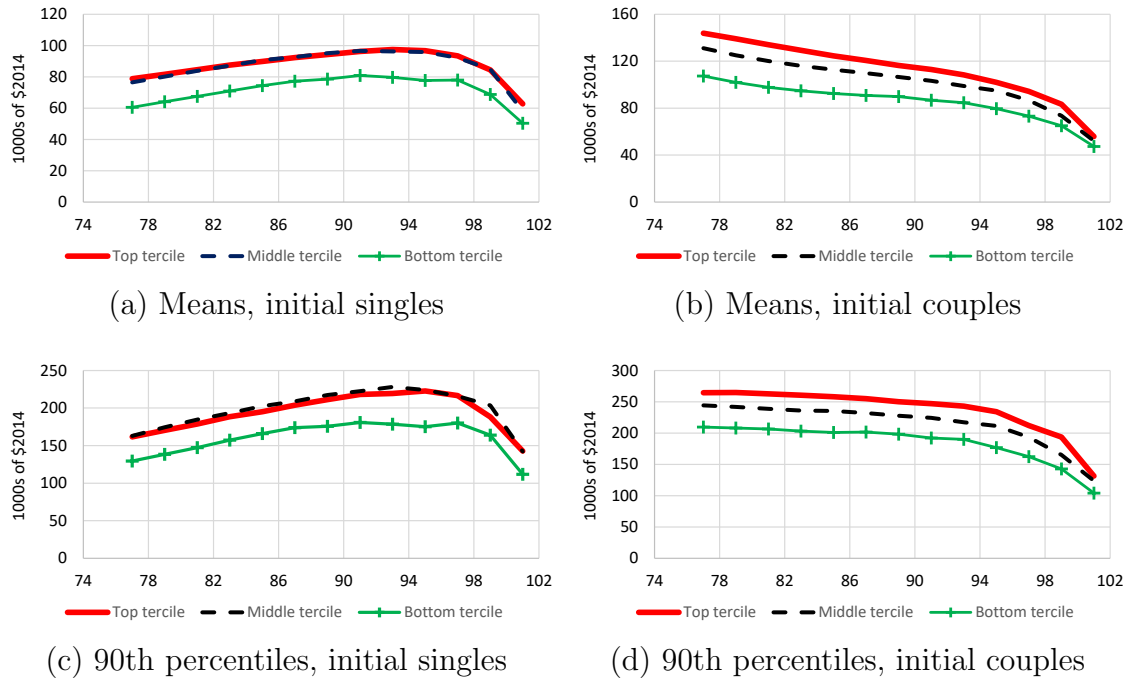
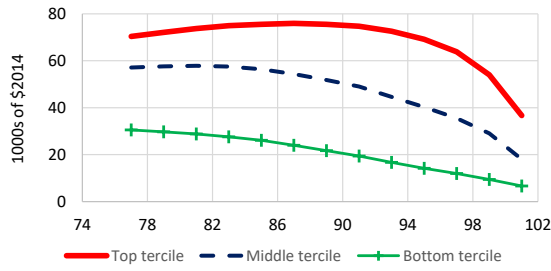
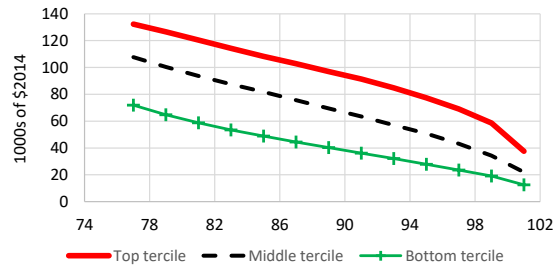


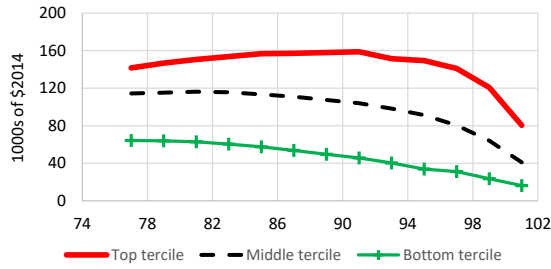
Figure A22: Mean and 90th percentile of remaining lifetime medical spending for surviving households, sum of out-of-pocket and Medicaid spending, by PI tercile.



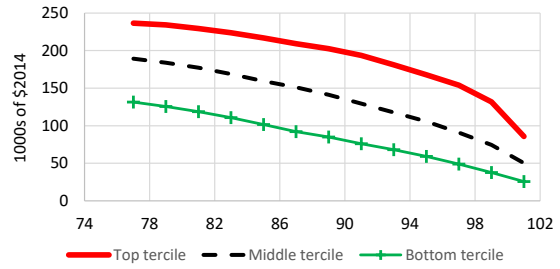
(a) Means, initial singles



(b) Means, initial couples



(c) 90th percentiles, initial singles



(d) 90th percentiles, initial couples

Figure A23: Mean and 90th percentile of remaining lifetime medical spending for surviving households, out-of-pocket spending, by PI tercile.

## Appendix M: No medical expense risk, model counterfactuals

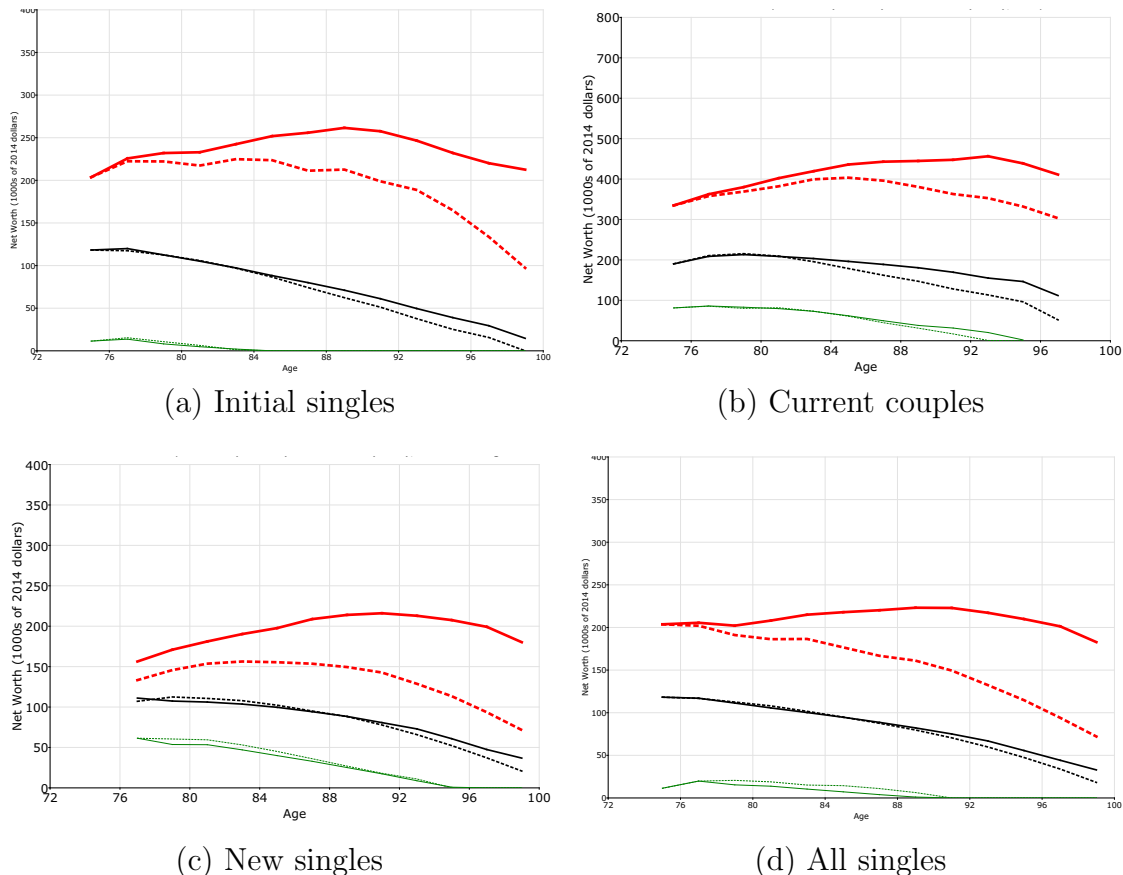


Figure A24: Median wealth for initial singles by PI tercile. Baseline model (solid lines) and model with no medical expense risk (dashed lines). Thicker lines denote higher PI terciles.

We replace the baseline medical spending process, where spending depends in part on health and the idiosyncratic shocks  $\zeta$  and  $\xi$ , with a process where medical spending varies only with age, PI and family structure. This eliminates much of the uncertainty regarding medical expenses and amounts to a mean preserving anti-spread.

This exercise differs from the similar exercise in De Nardi et al. (2010) in four important ways. First, the baseline estimated model in this paper incorporates

bequest motives. Second, we now eliminate medical spending risk due to changes in health. Third, households in our current simulations die off according to their estimated mortality risk, rather than live to the end of the simulation sample. Fourth, our current exercise calibrates total medical spending risk so that average out-of-pocket payments *net* of Medicaid, conditional on household structure, age and PI, are unchanged between the baseline and no medical expense risk experiment.

Panels (a) and (b) in Figure A24 show that for intact households, both singles and couples, the effects of eliminating medical expense risk have a magnitude and pattern similar to the effects of eliminating bequests. Both changes have the largest effects at the top of the PI distribution, either because richer households rely less on the consumption floor (in the case of medical spending uncertainty) or because richer households place more value on luxury goods such as bequests. Initial singles are somewhat more sensitive to medical expense risk than couples, perhaps because they are less sensitive to bequests. For example, at the top PI tercile, wealth at age 95 falls by 24% (from \$439,000 to \$332,000) for couples and by 29% (from \$232,000 to \$165,000) for singles.

Panel (c) shows that eliminating medical expense risk also lowers wealth among the high-PI new singles. Initially, most of the decrease is due to larger side bequests, but the effect also grows over time as the surviving spouses reduce their saving. Panel (d) combines new singles with initial singles to show results for all singles.

Figure A25 shows the extent to which intact couple's savings are driven by the medical expense risk of the last survivor in the couple.

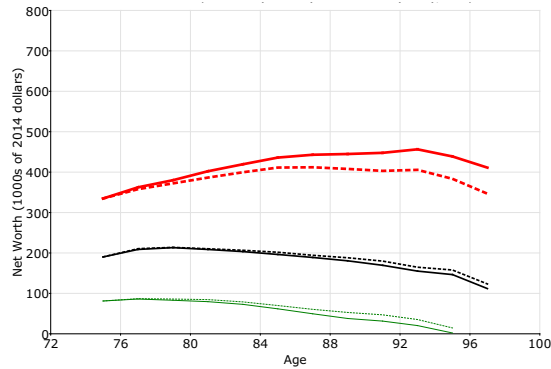


Figure A25: Median wealth for current couples by PI tercile: baseline model (solid lines) and model with no medical expense risk for the surviving spouse (dashed lines). Thicker lines denote higher PI terciles.