

Disability versus Work

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Entitlement reforms usually focus on changes in Social Security retirement benefits and Medicare. However, the disability component of Social Security is growing faster than retirement benefits and requires substantive reforms. Over the past three years, the number of Americans receiving disability benefits increased by more than 1 million, bringing the total number to 10.8 million. What is behind this surge?



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Social Security Disability Insurance was originally designed for workers over the age of 50 who became physically incapable of performing their current job or any other work compatible with their skills but had not yet reached retirement age. Since the mid-1950s, the program has expanded and now covers workers under the age of 50, disabled spouses of deceased workers and disabled adult children who were never able to work. Disability now includes mental impairments as well as physical ones. But even with better treatments for certain disabling conditions and new laws that require employers to make reasonable accommodations for the disabled, few people ever leave the rolls, except through retirement.

How the Application Process Works. In order to qualify for disability, workers must have enough Social Security disability credits based on their time in the workforce. The minimum number of credits required increases with age. Older workers must have earned most of their credits within the recent past. A nondisabled individual can lose eligibility for the program after 10 years out of the labor market, and must work additional years to regain the necessary number of credits.

A claims examiner investigates each applicant's medical history and can require examination by an independent doctor chosen by the Social Security Administration. Once this process is completed most claims are processed in three to five months, and payments begin the sixth month from the date the disability began.¹ If the initial claim is denied, an applicant can appeal the decision to an administrative law judge.

As shown in Figure I, from 2000 to 2009, on average, 28 percent of initial disability claims were approved and an additional 16 percent were approved on appeal. But more than half of all claims (53 percent) were ultimately denied.

Applications are denied for medical or technical reasons. Medical denials mean that the claimant does not meet the medical criteria for designation as unable to work. Technical denials usually mean that the claimant is earning more from work than is allowed (\$1,010 a month in 2012) or does not have enough work credits. Medical denials have dropped over the years as a percentage of all claims, but technical denials are rising.

Changing Eligibility Criteria for Disability. After disability rolls grew unexpectedly in the 1970s, criteria to qualify for disability benefits

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were tightened in the early 1980s. By the mid-1980s, however, the criteria were relaxed due to concern over the frequency of claim denials. Disability criteria were further broadened and claimants were given more opportunities to appeal. These broader standards have led to an increase in the disability rolls.²

Who Receives Disability Payments? Currently, about 1 in 18 working age, nonretired individuals receives disability payments.³ The prevalence of some disabling conditions has changed relatively little over the decades. But changing eligibility requirements and more effective medical treatments have considerably altered the prevalence of other diagnoses [see Figure II]:⁴

- Neoplasms (benign or malignant tumors), which were the second largest diagnostic category in 1981, fell from 16 percent to 3.1 percent by 2010.
- Mental disorders more than tripled from 10 percent of cases 30 years ago to become the second largest diagnostic category with 32.8 percent. Half of these were considered “mood disorders,” such as depression and anxiety.

The change in diagnoses of neoplasms can be attributed to better cancer treatments and less invasive surgery. The increase in mental disorders is likely due to the wider latitude in the diagnosis of such disorders.

Some conditions, such as back pain, may be difficult to diagnose. Finding an effective treatment through a trial and error process may take many months or even years. As a result, some ailments that are easily treatable with medication may not be treated effectively, putting

some claimants on the disability rolls for years with little likelihood of returning to work.

The age distribution of disabled workers has also changed:

- In 2000, the earliest year for which data by age group are available, 40 percent of beneficiaries were less than 50 years old.
- By 2010, the share of recipients under age 50 fell to 30 percent; nearly 70 percent were over age 50.

The increasingly older composition of the disability rolls can be explained in part by the aging of the population in general. A 2011 study using disability application rates from 1978 to 2008 found that a 1 percent increase in the population of 55 to 64 year olds relative to 25 to 54 year olds was associated with a 2 percent to 3 percent increase in the rate of disability claims.⁵

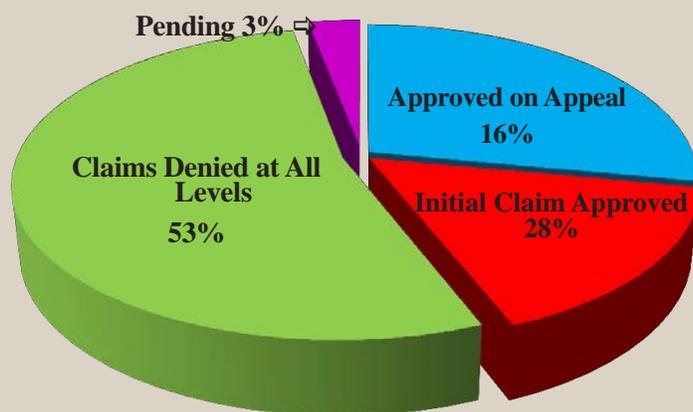
Furthermore, though it has been widely assumed that the disability rate is falling, this is only true for those ages 65 and over (not counted in the working age population) due to better treatments for heart, circulatory and vision problems.⁶ In the working age population, the disability rate for 50 to 64 year olds has increased. A 2010 study examined data from the National Health Interview Survey on reported disability among 50 to 64 year olds. Disability was defined as the inability to perform at least one of nine activities of daily living (ADL), such as getting in and out of bed or a chair, bathing and dressing.⁷ The survey data show that from 1997 to 2007:⁸

- Back or neck problems increased 31 percent and were the top cause of self-reported disability for 50 to 64 year olds.
- Depression, anxiety and emotional problems increased 20 percent and, taken together, constituted the third leading cause of disability.
- Arthritis and rheumatism cases fell 18 percent, but this category was still the second leading cause of disability in 2007.

Researchers say the growth in underlying medical conditions — such as musculoskeletal conditions, diabetes, nervous system disorders and depression — are the primary causes of increased self-reported disability.

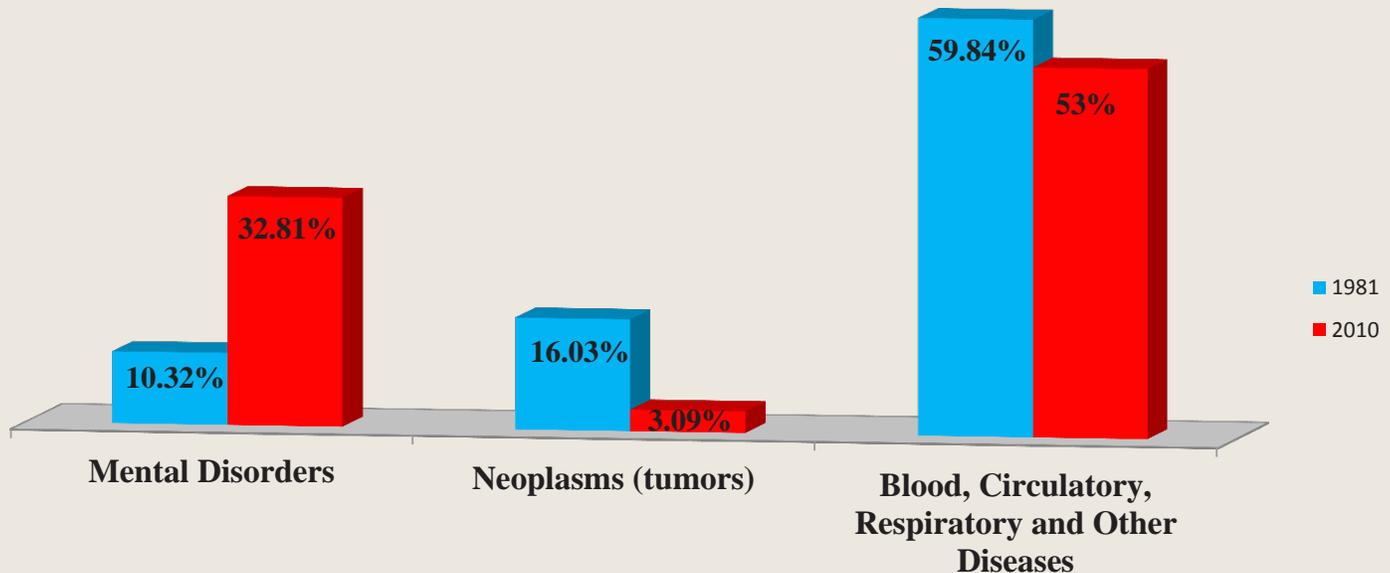
Importantly, Social Security’s disability determinations involve judgments by doctors in addition to self-reported claims. Thus,

Figure I
Disability Claim Outcomes, 2000-2009



Source: *Annual Statistical Report on the Social Security Disability Insurance Program*, Social Security Administration, 2010.

**Figure II
Disability Recipients by Diagnosis**



Source: “Distribution, by diagnostic group, selected years 1960–2010,” *Annual Statistical Report on the Social Security Disability Insurance Program*, Social Security Administration, 2010.

disability rates based on surveys differ from disability claims rates.

Do Disability Recipients Ever Return to Work?

Social Security reports that less than one-half of 1 percent of disabled individuals return to work.⁹ However, a longitudinal study from the Center for Studying Disability Policy found that up to 2.8 percent of beneficiaries return to work within 10 years of receiving benefits.¹⁰ Either way, the likelihood of returning to work is small, even though the health status of many disability recipients improves over time.

The disability system is designed to provide incentives to work for those who are eventually able to do so. First, individuals are allowed a “trial work period,” where they are given nine months to work without income limits and continue to receive disability payments. After the trial period, individuals can work an additional 36 months and still receive benefits, provided their monthly income does not exceed \$1,010. After the 36-month period, if an individual continues working but receives more than \$1,010 a month, disability payments will stop. If the individual is unable to continue working, he can reclaim disability within a five-year period without having to requalify.

There are considerable disincentives for individuals on

disability to return to work. Consider:

- Lack of accountability in the system allows beneficiaries who could eventually return to work to continue receiving payments.¹¹
- Recipients who are able to supplement their disability payments with part-time work are discouraged from doing so out of fear of losing their disability benefits.
- Finally, Social Security disability status makes recipients eligible for various other benefits, such as Medicaid, food stamps, Section 8 housing and student loan forgiveness.

Does High Unemployment Increase Disability Claims? Much attention has been focused recently on the relationship between rising unemployment and an increase in disability applications or awards in countries with generous social insurance systems. For example:

- A 2010 study from the research organization IZA found that among Norwegian workers, job displacement (unemployment) accounts for about 28 percent of new disability claims among men and 13 percent among women.¹²
- An Organization for Economic Cooperation and Development study of U.S. data spanning 22 years found that a 1 percentage point increase in the

unemployment rate increased the disability claims application rate more than 10 percent and the new awards rate 7 percent overall.¹³

- A 1995 U.S. study from the Social Security Administration found that from 1988 to 1992, the rate of actual disability awards increased 1.8 percent for men, but there was no statistically significant change for women.¹⁴

Long-term unemployment and the receipt of extended unemployment benefits increase the likelihood that an individual will never return to work. It appears that increasing numbers of older workers permanently exit the labor force for early retirement or disability pensions.

The Cost of Disability. Disability is the fastest-growing component of U.S. Social Security:

- Between 2008 and 2011, disability expenditures increased 22 percent to \$132 billion, compared to 19 percent for Social Security retirement benefits.
- By 2016, disability expenditures are expected to increase an additional 30 percent to \$170 billion, but the payroll taxes that fund disability will cover only 79 percent of benefits.¹⁵
- By 2018, it is expected that nearly 1 in 14 working-age individuals will be receiving disability payments.¹⁶

Just as there will be fewer working age adults to pay for the benefits of Social Security retirees, there will be fewer workers in the future to pay for the benefits of disabled workers.

Designing a Better Disability System. Evidence across many countries suggests that those with generous disability systems have more applicants and higher costs. Chile, however, reversed this trend when it implemented a new retirement and disability benefits system in 1981. Workers prefund their retirement by

putting a portion of their pay into individual accounts. The accounts are invested by private pension companies and earn market rates of return. Fully disabled workers are guaranteed 70 percent of their salary while partially disabled workers are guaranteed 50 percent. As a result of these and other characteristics of the system, the disability rate among Chilean workers fell significantly after 1981 and is now less than half that in the United States, after controlling for age:¹⁷

- Workers in the Chilean system are only 21 percent to 35 percent as likely to start a disability pension as they were in the old system, after controlling for age and gender.
- In 1999, among 45 to 54 year olds, 2.9 per thousand covered workers under the new system in Chile were accepted to newly disabled status, compared to 7.8 per thousand in the United States.
- For 55 to 59 year olds, 7.2 per thousand workers in Chile gained disability status, compared to 13.9 per thousand in the United States.

While Chile implemented this process in a funded defined contribution context, it could be adapted for other countries that have more traditional pay-as-you-go disability schemes, including the United States.

Conclusion. The current Social Security disability system is fraught with poor incentives, high costs and an unsustainable future. Prefunded personal disability accounts, as an integral part of overall entitlement reform, would reduce costs and promote a more efficient system that encourages individuals to work to the extent they are able.

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References and sources can be found in the online version at www.ncpa.org/pub/ib109.

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