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SSDI Reform

Promoting Gainful Employment while Preserving Economic Security

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EXECUTIVE SUMMARY

The Social Security Disability Insurance (SSDI) program faces imminent insolvency. Annual expenditures totaled \$143 billion in 2013, but program receipts amounted to \$111 billion—a shortfall that is projected to continue indefinitely. According to the Social Security Trustees, the program's trust fund will be fully depleted in 2016, compelling either a large benefit cut or a large tax hike—neither option being politically popular.

Regardless of the program's insolvency, SSDI creates substantial work disincentives, causing many with medical impairments who could work to withdraw from the labor force and apply for SSDI. That undesirable outcome arises from the complicated rules and procedures that SSDI uses to establish benefit eligibility. But rectifying SSDI's processes is a monumental task, unlikely to be accomplished in the short term.

Determining whether medical impairments imply inability to work is becoming more difficult in a growing

number of cases, with the result that many applicants with residual capacities are admitted to SSDI. Many beneficiaries express a desire to return to work but fear of losing benefits and health coverage under SSDI's current benefit rules impedes such a decision. Accordingly, this paper advocates a change in the structure of SSDI's benefit payments to those admitted to the program. Shifting benefits at the margin toward paying beneficiaries to work rather than to remain out of the work force would encourage beneficiaries with residual work capacities to return to work. That shift would serve as a backstop to reduce the economic loss from wrongful allowances of applicants into SSDI. Such a switch in benefit design can be accomplished without compromising benefit eligibility for those who cannot work. The paper explains how to implement such a change to SSDI's benefit structure and the advantages that would accrue from it. Apart from creating better incentives to work, the proposed reform complements other reforms Congress might adopt.

“Social Security Disability Insurance distorts the incentive to work, causing people with substantial work capacity to withdraw from the labor force and seek to enroll.”

INTRODUCTION

Social Security Disability Insurance (SSDI) insures workers against the loss of wage earnings from premature onset of a disabling condition. Annual benefit payments and administrative costs totaled \$143 billion in 2013, and program receipts amounted to \$111 billion—an shortfall that is projected to continue.¹ According to the Social Security Trustees, SSDI’s trust fund will be exhausted in 2016.² Absent changes in the law until then, a benefit cut of 19 percent will become necessary immediately after 2016—an outcome Congress is unlikely to tolerate.³ In response to the shortfall, the Social Security Trustees could redirect payroll taxes from Social Security’s Old-Age and Survivors Insurance (OASI) Trust Fund, but that would merely shift the underfunding elsewhere.⁴

Regardless of solvency concerns, SSDI distorts the incentive to work, causing people with substantial work capacity to withdraw from the labor force and seek to enroll. This is because disability is rarely all or nothing with individuals who are either capable of working or not. Instead, people experience a range of health conditions that reduce work capacity but do not necessarily preclude significant earnings. Thus, to avoid paying SSDI to everyone who claims disability, the Social Security Administration (SSA) must first determine who is “sufficiently” disabled to deserve benefits and then monitor enrollees’ medical status to identify cases where claimant medical conditions no longer meet the program’s eligibility rules.

Today’s disability determination systems involve a peculiar combination of procedures. On the one hand, case officials and administrative law judges (ALJs) must often base decisions on their own or experts’ subjective judgments, because objective medical criteria are not available for measuring the severity of conditions like pain or mental impairment. On the other hand, adjudicators must often apply legal presumptions of disability according to an applicant’s age, education, vocation, and other nonmedical characteristics, irrespec-

tive of work capability. As will be described, a statistical analysis of ALJ benefit allowance patterns suggests persistent inconsistencies across ALJ decisions, implying problems with disability policies, compliance with those policies, or both.

This paper first argues that the environment for adjudicating disability cases has become increasingly challenging and is likely causing unwarranted SSDI allowances. Application and allowance patterns suggest that SSDI is increasingly used as alternative support by those who could work but have exhausted unemployment insurance benefits. The paper also examines micro survey data and Social Security Administration (SSA) data on labor force participation, SSDI’s enrollments, and the outcomes and projections of SSDI’s prevalence rate; those data suggest that the program is encouraging those with medical impairments to leave the work force.

Congress has two possible ways to address looming insolvency and the distortions caused by SSDI: reduce benefit levels or adopt better procedures for determining and monitoring disability status. Lower benefits will cause fewer people to seek SSDI over work, but that would harm deserving disabled persons. Better determination procedures are desirable, but designing and implementing improvements are difficult: any process will require significant time, debate, and judgment, and whether the effect of resulting changes will be beneficial is uncertain.

This paper describes a different kind of reform: one that does not target the disability determination process itself but adds a financial incentive to more effectively encourage SSDI beneficiaries to return to work. The new SSDI benefits system advocated here would protect access to SSDI for those beneficiaries who are unable to work. Moreover, the “post-entitlement” reform proposed here is complementary to all other reform measures, including “pre-entitlement” changes that Congress may implement in the future.⁵ For example, although the reform proposed here appears unlikely to induce many more workers with

medical impairments to drop out of the workforce and apply for SSDI, those that are so induced would be suitable for early-intervention programs to preserve their motivation and ability to continue working.

MOTIVATION FOR SSDI REFORM

Many analysts and observers claim that SSDI is failing individuals with disabilities. But they also believe we must reform the program in fundamental ways because the tax increases necessary to continue benefit payments under current laws may erode political support for the program.⁶ Even sitting ALJs opine that SSDI no longer serves its intended purpose and needs significant structural changes.⁷

Several analysts have asked whether augmenting SSDI with “front-end” initiatives would prevent or delay entry into SSDI by workers who could remain gainfully employed with additional support services.⁸ Those proposals are motivated by the observation that disabling conditions become more serious

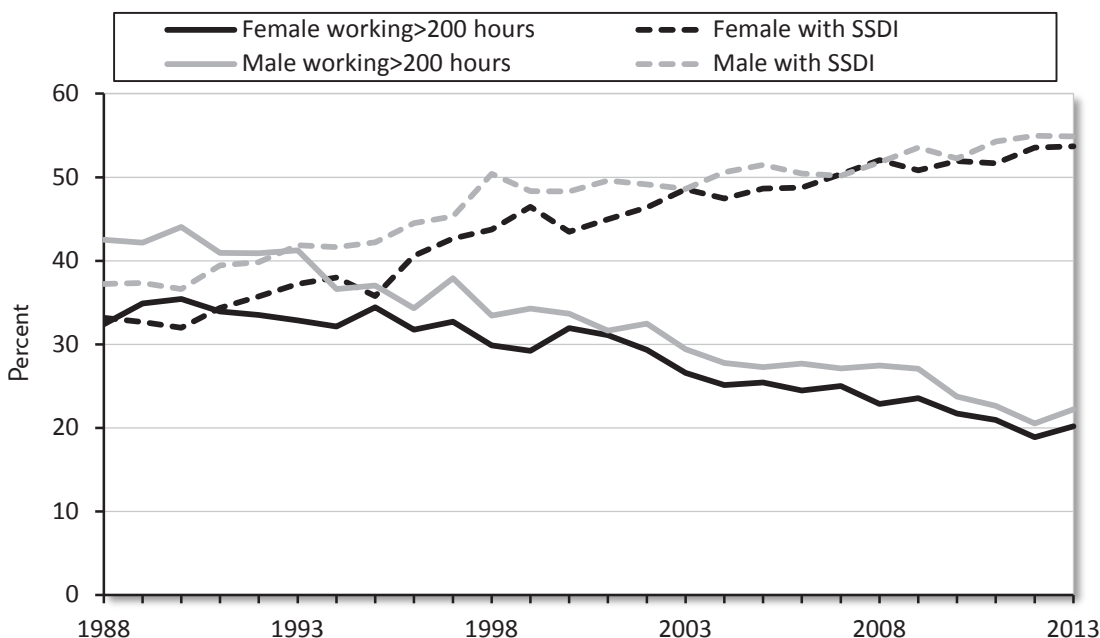
over time, and that the likelihood of sustaining a worker’s ability and motivation to remain employed is greater the earlier remedial interventions can be provided.

That approach, however, has several problems. First, SSDI’s rules provide strong incentives for people with medical impairments to stop working and apply for the program. Figure 1 shows a secular decline in labor force attachments and an increase in SSDI enrollment by those with a work-limiting medical impairment—as if those individuals are investing in not working in order to qualify for SSDI.⁹ So countering SSDI’s incentive to apply for disability benefits by providing early-intervention services and supports may prove difficult as recent research has shown.

Second, identifying workers to target for early-intervention supports and work accommodations will be challenging. Screening almost the entire work force to identify those likely to experience declining health and eroding work capacity will be difficult and costly. Third, like other disability insurance (DI) re-

“Tax increases necessary to continue benefit payments under current laws may erode political support for the program.”

Figure 1
Disability Policy and (Anti-) Work Incentives
Adults 25–59 with a Work-Limiting Disability



Source: Author’s calculations from Census Bureau’s Current Population Survey data.

“Technological advances in assistive devices, and changes in the workplace, social, and legal environments for individuals with disabilities—mean that operationalizing the term ‘medically determinable work disability’ to make disability determinations has become much more difficult.”

form approaches, the early-intervention approach is also not immune from “induced entry” issues.¹⁰

In contrast, few analysts have proposed “post-entitlement” reforms that would provide better work incentives to current SSDI beneficiaries, presumably under the belief that beneficiaries possess little residual work ability and motivation.¹¹ This is consistent with the original disability definition—“of long-continued and indefinite duration”—which is widely recognized as creating strong work disincentives. Although the definition was liberalized during the 1960s, it continues to discourage beneficiaries from rejoining the labor force. As discussed below, a significant minority of beneficiaries appears to possess residual work ability, but most who do work limit their hours and earnings to preserve SSDI eligibility.

As under the original disability definition, the one in force today requires SSDI eligibility to be based on one or more “medically determinable” impairments. It specifies that the worker (a) must be unable to continue work in the current occupation, (b) must be unable to adjust to other work because of a medical condition, and (c) must have a disability that is expected to last for at least one year or to result in death. However, changes in the American economy since that definition was introduced in 1967—the lighter exertional requirements of today’s jobs, improvements in population health, technological advances in assistive devices, and changes in the workplace, social, and legal environments for individuals with disabilities—mean that operationalizing the term “medically determinable work disability” to make disability determinations has become much more difficult. The Social Security Advisory Board recently wrote, “Medical advances and improved rehabilitative knowledge and technology . . . during the last 50 years . . . increasingly call into question the ability of a program to neatly draw a line between those who can and those who cannot work.”¹² Thus, it is likely that many current beneficiaries have residual work capacities and the case for continuing with a disability benefit structure

that discourages working so strongly is much weaker today.

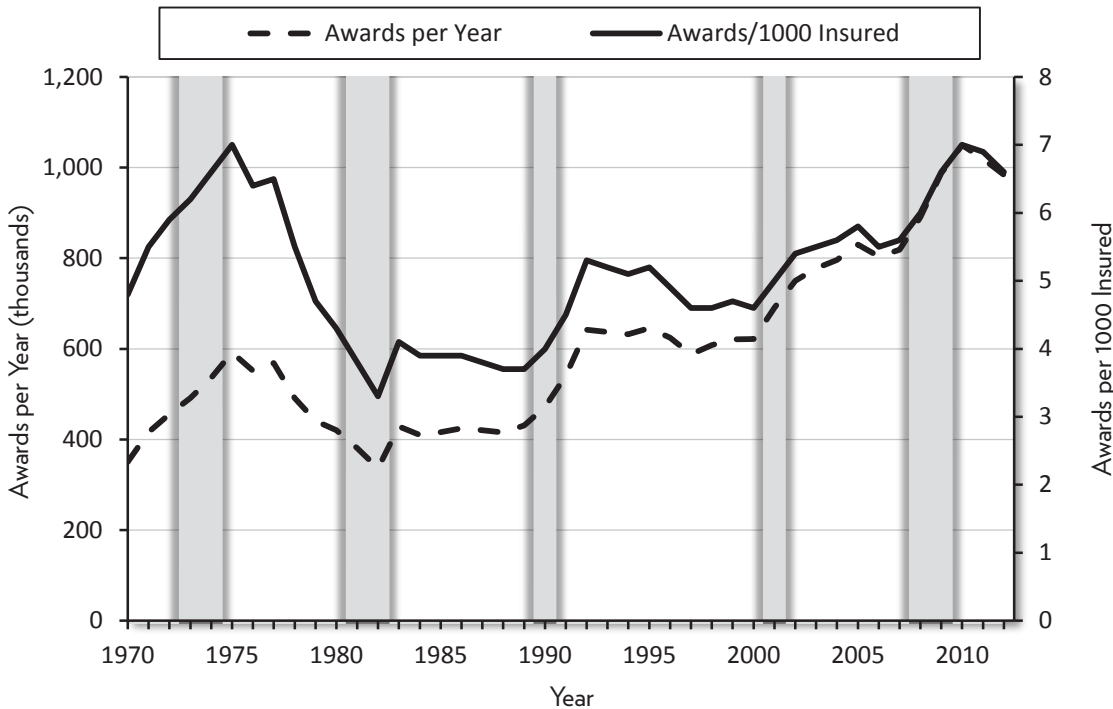
How can we introduce an effective work incentive into SSDI’s benefit structure that preserves the program’s safety net for individuals with disabilities? Many disability analysts believe that goal is infeasible under the current SSDI disability definition and the current benefit eligibility criteria. However, altering SSDI’s benefit structure to substitute, at the margin, “payments to work and earn” instead of “payments to replace lost wages” could achieve that objective.

Such a reform of SSDI’s benefit structure will also have ancillary advantages. It would generate savings for the SSDI trust fund, reduce the program’s administrative costs, and provide a federal disability benefit structure around which state and local public, nonprofit, and charitable organizations could design and build additional support programs. Those agencies could provide saving programs and financial advice, especially to counter employment and earnings risks that beneficiaries will experience when they return to work. Such a change would improve the living standards of individuals with disabilities, allow them greater independence, encourage community participation through employment, and nurture a self-supported and self-determined lifestyle secure in the knowledge that SSDI’s safety net will continue to be available if labor market attachments cease for health or other reasons.

INCREASING RELIANCE ON SSDI

The evidence to date on burgeoning SSDI incidence rates suggests that the program is acting as a gravitational force, peeling individuals with medical impairments away from the work force and absorbing them into a permanent state of public dependency. Figure 2 shows that since the 1990s, sharp increases in SSDI enrollments have coincided with recessions (periods shown as gray vertical bars) when unemployment rates tend to be high. It suggests that SSDI’s marginal applicants may be work-capable but end up in SSDI as an al-

Figure 2
SSDI Allowances (1970–2012)



Source: Social Security Administration.

ternative source of long-term unemployment support after federal unemployment insurance benefits expire.¹³

Such applicants are admitted into the program because SSDI appears less able today to determine whether medical impairments and associated functional limitations reduce work capacity sufficiently to warrant allowance into the program. Moreover, during recessions, it becomes easier to meet the program's vocational eligibility conditions, as job availability in applicants' occupations are, indeed, scarcer.¹⁴

The curious aspect of Figure 2 is that although allowance rates spike during recessions, they do not fully revert to earlier levels once the economy recovers. Thus, recessionary conditions may be stimulating factors that induce permanent increases in SSDI's allowance frequencies. One such factor is the increased representation of SSDI applicants by attorneys, nonprofit agencies, state welfare workers, and other social organizations, even at the initial application level.¹⁵ The financial

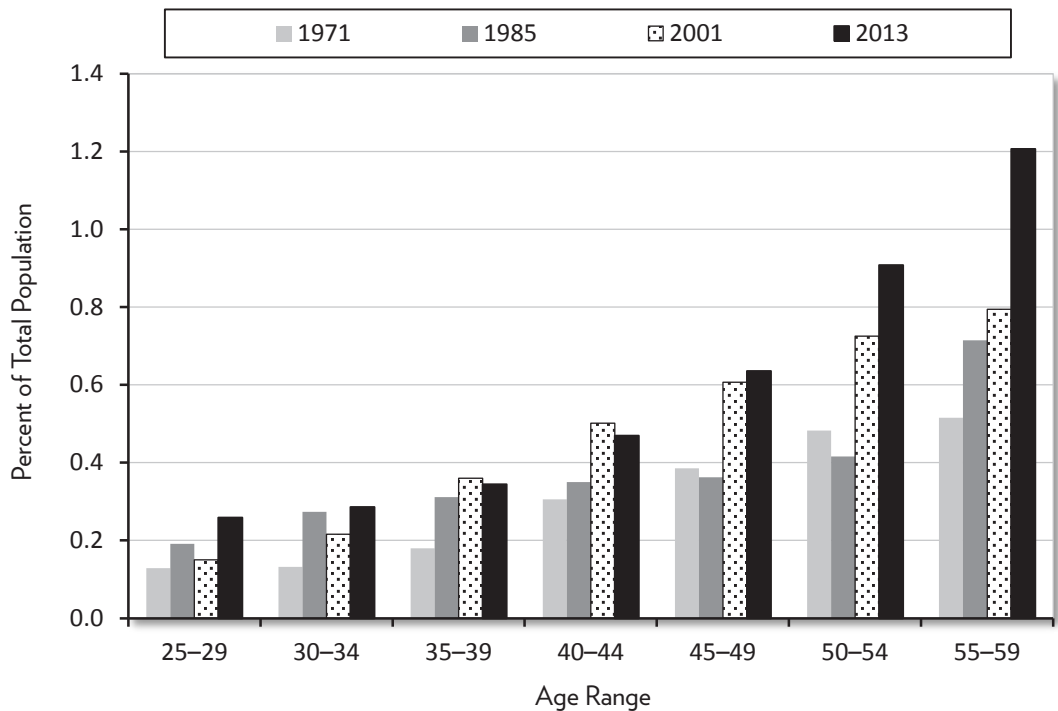
fees paid to such intermediaries under SSDI's current rules justify investing in the ability to prepare applications strategically: the advocates sharpen supporting evidence, target shortcomings in the system's operational procedures, and exploit SSDI's procedural quirks to increase the likelihood of favorable decisions. Recessions spur the irreversible acquisition and broader application of such case management techniques and strategies.

A part of the increased annual incidence of disability (and one of the reasons for non-reversal of SSDI enrollment spikes during recessions as shown in Figure 2) is the movement of baby boomers into older ages and the increased entry of women into the labor force during and after the 1970s. That change increased the share of women insured under SSDI. Had disability prevalence rates remained constant, most of the increase in SSDI enrollments would be potentially attributable to those two factors. However, as Figure 3 shows, SSDI's age-specific prevalence rates

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“Several factors, especially changes in the nature of jobs, technological advances, and increased use of assistive devices, have made it easier for individuals with disabilities to adapt despite medical impairments and to retain the ability to work.”

Figure 3
SSDI Prevalence by Age Groups for Selected Years



Source: Author's calculations from Census Bureau's Current Population Survey data.

have also increased over time, suggesting that the changing age and gender composition of the insured population alone does not account for all of the increase in SSDI's incidence (Figure 2).¹⁶ As suggested below, the increased disability prevalence within age groups may indicate changes in how disability policies have been implemented over time.

Changes in the Economy, Jobs, and Worker Characteristics

Changes in sectoral employment and the work force (e.g., age composition, career longevity, education, gender composition) appear to have eroded SSDI's ability to link medical conditions with (in)ability to work. Several factors, especially changes in the nature of jobs, technological advances, and increased use of assistive devices, have made it easier for individuals with disabilities to adapt despite medical impairments and to retain the ability to work.

Changes in the sectoral composition of the work force have also contributed in that

regard. During the early 1960s, more than 40 percent of employment was in agriculture and manufacturing, where most tasks required significant physical exertion. Today, only about 13 percent of national employment occurs in those sectors, versus 87 percent in the service sector, which involves less physical exertion and greater application of cognitive and light psychomotor activities and skills.¹⁷

Patterns of sectoral employment changes since the mid-1980s show that the service-sector share of medically impaired individuals employed and *not* enrolled in SSDI increased more rapidly than the share of those without medical impairments. Moreover, the service-sector share of medically impaired individuals who work despite being enrolled in SSDI increased at the fastest rate compared with the other two groups. Those patterns are consistent with the conjecture that service-sector jobs place fewer physical demands on workers and are easier to acquire and retain for individuals with disabilities.

Among all SSDI beneficiaries, whether employed or not, the share of those associated with the service sector (currently, if working, or before entering SSDI if not) has increased at roughly the same rate as those without medical impairments. That is, for those on SSDI, the shift in national employment toward the service sector has not skewed the distribution of beneficiaries toward nonservice sectors as might have been expected. Instead, the sectoral distribution of SSDI beneficiaries has shifted in tandem with the overall sectoral composition of the U.S. nondisabled work force.

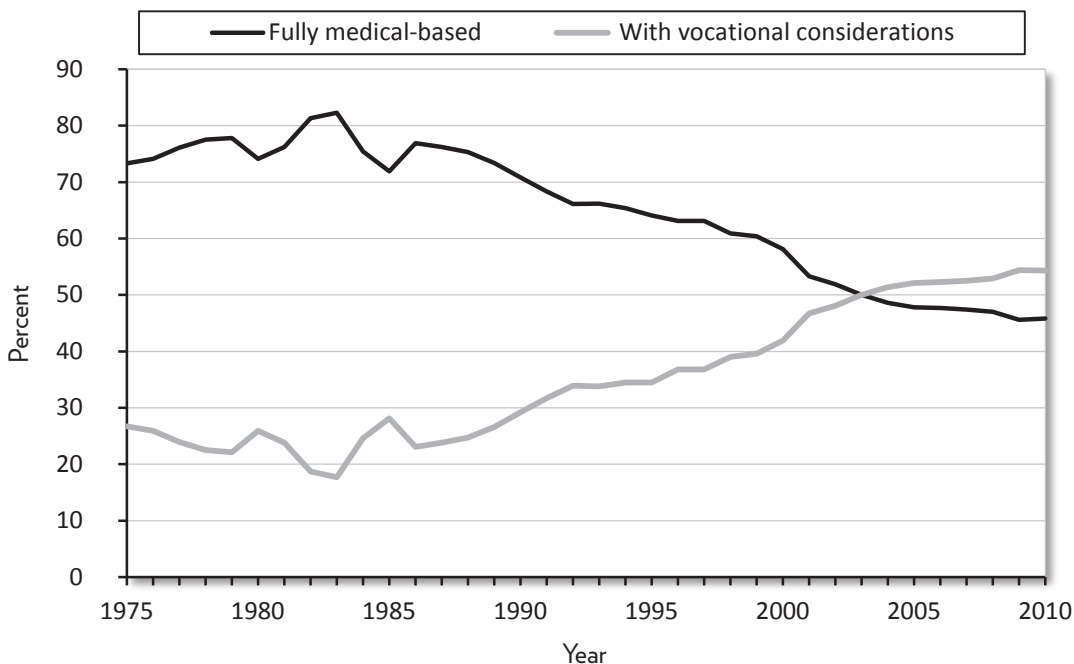
Today, SSDI allowances are based less frequently on strict medical grounds. Allowances based strictly on the applicant's medical condition made up more than 90 percent of total allowances during the program's initial years.¹⁸ In 1988, about one-quarter of allowances were based on nonmedical considerations. In contrast, as Figure 4 shows, more than one-half of today's SSDI allowances are based on non-medical grounds.

That secular change in the basis for disability program allowances is attributable to several factors:

- *Changes in the law specifying who should qualify.* Figure 4 shows that the vocational allowances began to increase soon after the Social Security Disability Benefits Act of 1984 placed greater emphasis on vocational factors, subjective evaluations of pain, and mental conditions.
- *Changes in the nature of American jobs.* A shift toward service-sector jobs, technological changes, faster skill obsolescence, and more rapid worker turnover meant those with medical impairments faced greater difficulties in shifting occupations, causing greater use of vocational criteria in disability determinations over time
- *Changes in the nature of the work force.* Although overall economic growth and labor force participation were both quite

“Today, Social Security Disability Insurance allowances are based less frequently on strict medical grounds.”

Figure 4
DI Awards by Basis for Decision (Fiscal Years 1975–2010)



“Under eligibility determination rules introduced in 1984, older individuals and those with less education and work experience receive more lenient consideration and are allowed to enroll at higher rates on the basis of vocational considerations.”

robust for more than two decades until the recession of 2008–9, there were significant changes in the nature of the work force, especially as baby boomers matured from young adults to middle and older ages. That factor likely accounts for a large part of the secular change in the basis for SSDI allowances because, under eligibility determination rules introduced in 1984, older individuals and those with less education and work experience receive more lenient consideration and are allowed to enroll at higher rates on the basis of vocational considerations.¹⁹

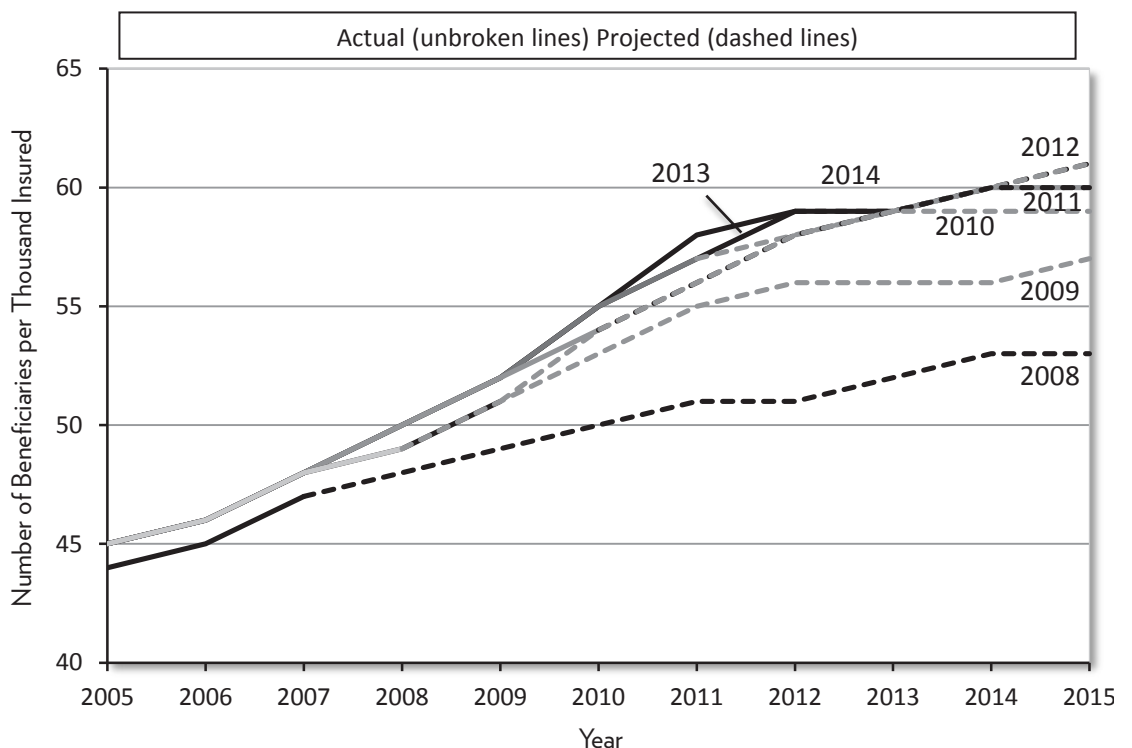
■ **Poor economic prospects and higher medical costs for lower-income workers.** Robust economic growth of the post-1980 economy involving rapid technological changes meant declining employment prospects for low-skilled workers. At the same time, health care became more expensive. Those two factors may have combined to compel lower-income

workers to seek financial support under SSDI.

■ **The SSA’s implementation of disability eligibility rules itself changed toward greater reliance on vocation-based allowances.** The difficulty of establishing functional and work limitations purely on the basis of medical impairments increased over time, resulting in reliance on vocational allowances that, over time, produced an increasingly lower threshold for qualifying for benefits. If that notion is correct, the trend will likely continue in the future.

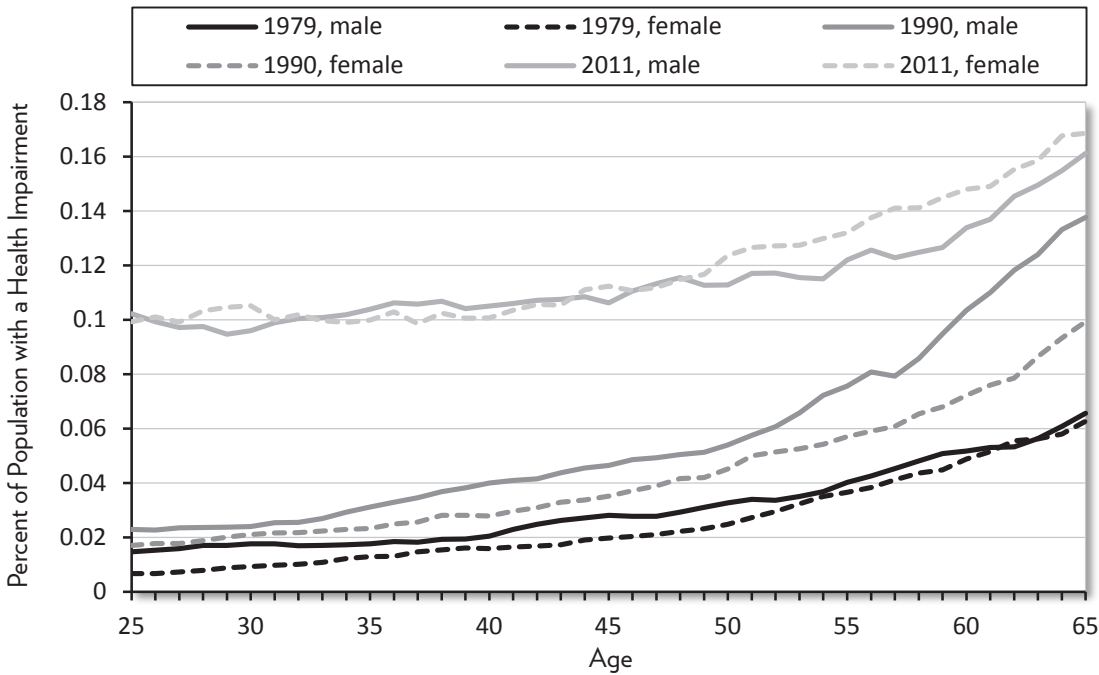
To what extent did each of those explanations contribute to the change in SSDI’s basis for disability determinations? Although demographic changes surely contributed, changes in disability policy following changes in the law in 1984 appear to be the key factor, especially when considered together with Figure 3’s evidence of increased prevalence of disability at older ages.

Figure 5
SSDI Prevalence Rates



Source: Annual Reports of the Social Security Trustees, various years.

Figure 6
Assistive Device Use by Age (1979, 1990, and 2011)



Source: Author's calculations from National Health Information Survey data.

Additional Indicators of Anti-work Incentives

Since 2008, Social Security's Trustees have published the history and projections of SSDI prevalence rates—SSDI beneficiaries as a share of the SSDI insured population.²⁰ Figure 5 compares those projections with actual outcomes over time. It shows that the actual DI prevalence rate (designated by unbroken lines) was higher in each year than the rate that was previously projected (designated by dashed lines) for the same year.

One possible conclusion that can be drawn from Figure 5 is that the Trustees do a poor job of constructing those projections. However, their projection methodology is standard, and they take great care to incorporate all available information when constructing them.²¹ If the prevalence projections consistently undershoot outcomes, then we should conclude that SSDI's rules are incentivizing individuals with medical impairments to apply for and enroll in DI at faster-than-expected rates.

Improvements in Medicine, Assistive Technology, and Rehabilitation Methods

Over the past few decades, changes in medicine have changed how humans experience many illnesses. Newer treatments and techniques are improving patients' mental and physical abilities. Considerable progress is also evident in assistive devices that improve and extend human physical and mental functional capabilities. For example, new and improved adaptive devices and equipment enable significant restoration of physical functionality despite permanent loss of limbs, communication ability (hearing, speech, and vision), mobility, and even sensory and cognitive faculties. Figure 6 shows that the use of assistive devices (excluding eyeglasses) has increased significantly during the past two decades.²² The work-ability-enhancing effects of technological innovations in assistive devices should be incorporated into eligibility standards and case determinations for the nation's disability programs. However, a recent study by the U.S.

“If the prevalence projections consistently undershoot outcomes, then we should conclude that Social Security Disability Insurance's rules are incentivizing individuals with medical impairments to apply for and enroll in disability insurance at faster-than-expected rates.”

“Changes in public amenities during the late 1960s through the 1980s included access to public places, trains, buses, buildings, parking, polling places, and so on, providing greater means for community participation by individuals with disabilities.”

Government Accountability Office reports that SSA “faces constraints in fully modernizing the disability adjudication system in response to technological changes.”²³

Changes in Social Attitudes and the Legal Basis for Benefit Awards

Social views about individuals with disabilities have evolved over several decades in opposing directions: toward associating disabling conditions with “inability to work,” yet also encouraging greater independence, self-determination, and participation by individuals with disabilities in community and public life. But such independence and social participation can happen only if individuals with disabilities “work,” perhaps with assistance services and accommodations.

The demand for improved health, education, and rehabilitation services for individuals with disabilities intensified during the administrations of John F. Kennedy and Lyndon Johnson and led to treatment and housing of the mentally ill within community settings rather than in underfunded and poorly managed institutions. Along with the elimination of the “of long continued and infinite duration” clause in the definition of disability, amendments to expand rehabilitation centers and fund additional vocational rehabilitation programs were enacted during the 1960s. Changes in public amenities during the late 1960s through the 1980s included access to public places, trains, buses, buildings, parking, polling places, and so on, providing greater means for community participation by individuals with disabilities.²⁴

The Supplemental Security Income (SSI) program, introduced in 1972, extended financial support for families caring for children with disabilities. Other advances—Braille on public utilities, closed-captioning in TV programs, educational supports for student with disabilities, and so on—during the 1970s dramatically increased the scope for individuals with disabilities to live, associate, and participate in their communities. Those improvements concomitantly make it easier to adapt

to medical impairments and to increase the productive abilities of individuals with disabilities.

Changes in the Criteria for Allowing Entry into SSDI

Although changed social attitudes enabled greater access to and participation in public and community life for the disabled, SSDI has remained controversial. High disability enrollments and expenditures during the 1970s had spurred beliefs that improper payments had grown considerably. Indeed, a report published by the General Accounting Office in 1979 noted that almost one million beneficiaries received overpayments during the first half of that year, most because they earned more than was allowed under the law.²⁵ In response, Continuing Disability Reviews (CDRs) increased, and benefit terminations accelerated early in the Reagan administration. However, lack of clarity in the standards and procedures for conducting CDRs generated further controversy, and CDR implementations were suspended until proper methods could be developed.²⁶

The new legislation introduced uniform national standards for “medical improvement” criteria to determine when a person’s disability benefits could be ceased. That law—the Social Security Disability Benefits Reform Act of 1984, whose provisions remain in force today—also included changes that increased the likelihood that an applicant would gain benefits. For instance, it allowed disability awards on the basis of subjective medical diagnoses, including applicants’ own assessments of their disability relating to pain and discomfort. The act also replaced the government’s medical assessments with those of the applicant’s doctor (the “treating physician’s rule”) and liberalized the screening criteria for mental illness. Under that law, applicants’ subjective claims of pain or mental incapacity became a sufficient basis for benefit allowances.

That wide latitude in policy likely contributes significantly to the wide variation in allowance rates across SSDI’s case examiners and administrative law judges. A statistical

evaluation of ALJ allowance decisions (discussed below in greater detail) suggests that either (a) case allocation practices and ALJ decision procedures somehow combine to deliver poor SSDI policy compliance, or (b) SSDI's policies for disability determination allow such wide differences of opinion on identical cases that allowances are mostly "luck of the draw" outcomes.

Enhancements in the Legal Rights and Representation of Individuals with Disabilities

Changed social attitudes, improved accommodations for greater community participation, and better assistive technology have changed the meanings of "medical impairment" and "inability to work." The two are less congruent today than when SSDI was introduced in 1956. Those changes have rendered fruitless attempts to map medical conditions into corresponding functional limitations that prevent particular work performance on par with the "average worker."

Expanding functional ability with assistive technology brought forth demands to accommodate individuals with disabilities in the workplace, culminating in the Americans with Disabilities Act of 1990 (ADA). That act requires employers to provide workplace accommodations, at a reasonable cost, for individuals with disabilities and prevents discrimination against them if such accommodations make them as comparably productive as those without medical impairments. Legal developments and case adjudications over time have clarified and expanded the scope of the ADA.²⁷

Despite establishment of legal precedents to expand employment potentials for individuals with disabilities, however, SSDI applications and enrollments as a share of the insured population have continued to grow throughout the 1990s and 2000s. Indeed, disability advocates suggest that the ADA, although effective at ensuring fair consideration of individuals with disabilities for competitive job placements when used, is not used as frequently as might be expected. Those with

medical impairments have increasingly turned to SSDI for support rather than relying on the ADA to acquire employment and pursue an independent and self-determined lifestyle.

One factor contributing to that trend may be increased assistance from legal firms, non-profit institutions, insurance companies, and state and local governments to enroll potentially eligible individuals in SSDI. Many of those institutions are motivated by the opportunity to earn fee income or to reduce state welfare budget expenditures.²⁸ Indeed, public agencies and private law firms proactively seek individuals with physical or mental impairments—those with even moderate likelihoods of being awarded SSDI benefits when their applications are professionally developed and represented before program adjudicators.²⁹ Often the main task that representatives perform is to obtain medical certification from the client's doctors. As detailed below, medical certification appears to skew the SSDI determination process toward undeserved allowances.

ALJ Hearings: Erosion of Decisional Authority and Loopholes That Permit System Abuse

Administrative law judges consider cases that are appealed after being denied SSDI benefits at two administrative decision stages—"initial" and "reconsideration." The ALJs play a multifaceted role in the process of developing and hearing a disability case. Apart from providing a "full and fair hearing," ALJs must also help claimants develop their record and present their case, even when a claimant has representation. And ALJs are supposed to act as guardians of the Social Security trust funds, thereby representing the public and taxpayers. Thus, ALJs represent the opposing interests of disability claimants and taxpayers simultaneously. However, because the latter's interests are not formally represented by a government representative (apart from the ALJs), the hearing is conducted in a nonadversarial setting. That type of SSDI adjudication impedes the determination of SSDI awards based on a comprehensive and fair review of the claimant's record.

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According to some ALJs, SSA's management of the hearings process compromises ALJ independence, subverts due process, and interferes with the expeditious movement of cases. One major complaint is the poor specification and execution of SSDI eligibility criteria, facilitated by the obfuscation permitted under the current disability definition. One example is "double-dipping," claiming to be ready, willing, and able to work to collect unemployment insurance benefits and simultaneously claiming inability to work to remain eligible for SSDI.³⁰

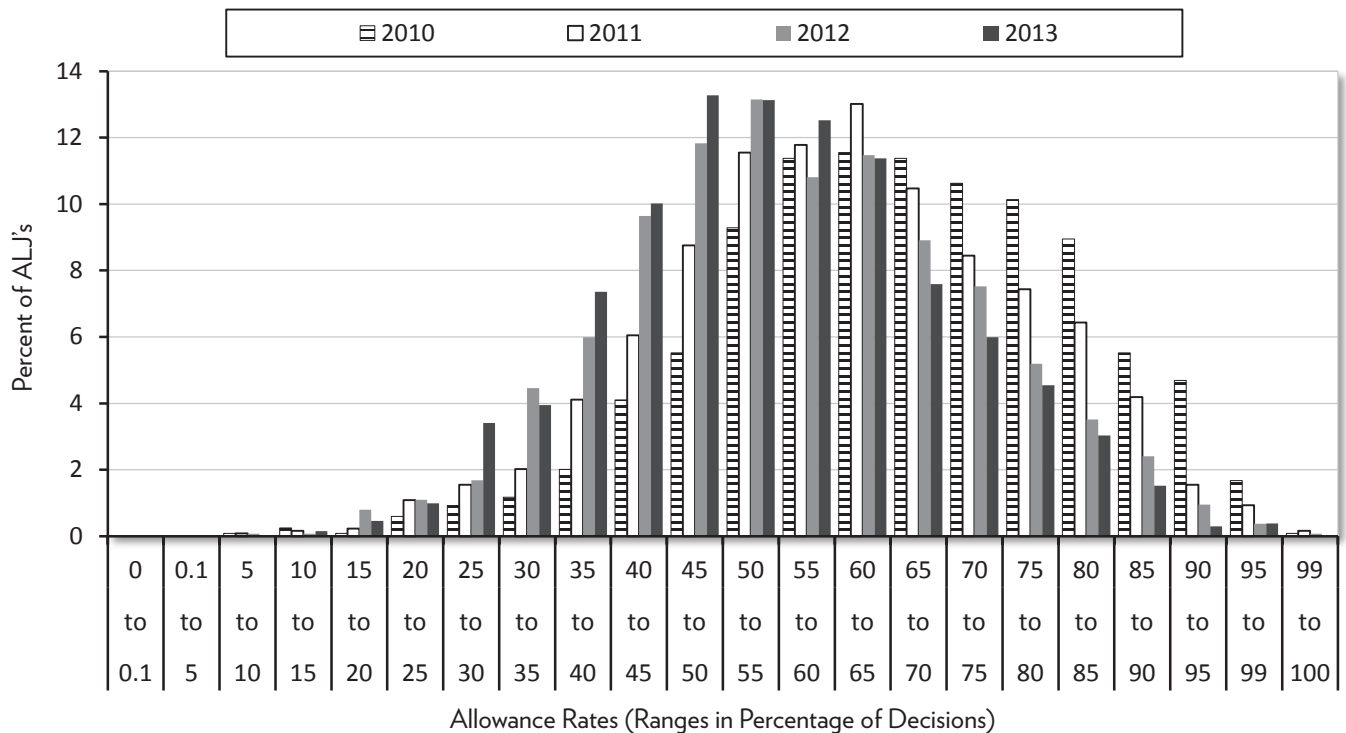
Another example of how the ALJ opinions are neutralized or subverted in contestable cases is best described by quoting the words of a sitting ALJ. According to the ALJ, under current SSDI law,

the opinions of treating physicians (are declared) as controlling. . . . In a tribunal, in which . . . the [Social Security

Administration] is not represented, this permits easy solicitation of favorable reports from treating physicians, who are already naturally in sympathy with their patients. . . . These reports are not sworn under the pains and penalties of perjury. . . . The treating physician is never subjected to cross-examination, let alone prosecution for misrepresentation. . . . Thus an Administrative Law Judge is boxed into a corner, and forced to grant benefits, even when knowing the individual is not truly disabled.³¹

The issue is that under the current nonadversarial ALJ hearing procedure, the "treating physicians rule" confers controlling weight on the medical certification provided by the claimant's doctor(s). The burden of countering that the claimant could perform gainful work is forced onto the ALJ. But ALJs are ill-equipped to "prove" that the claimant is able

Figure 7
ALJ Allowance Rates (Fiscal Years 2011, 2012, and 2013)



Source: Author's calculations from Social Security Administration data.

to work. The medical certification may be suspect, but the ALJ has little ability to deny eligibility. Worse, “too many [ALJs] are bludgeoned . . . by the Administration’s constant push for numbers [high pace of case dispositions].” The acquisition of (potentially suspect) physician opinions is often the only thing claimant representatives do, but it is sufficient to win allowances to SSDI.³²

Persistence in ALJ Decisional Variance: Policy Noncompliance or Noncompliant Policy?

Whatever the merit of such ALJ complaints, statistical analysis of ALJ decisions suggests that ALJs’ decisions largely reflect their individual views and preferences. The key question is how closely SSDI allowance decisions adhere to program rules. That question is difficult to answer directly, especially at the ALJ level, because SSDI decisions involve subjective judgments. Alternatively, those judgments are, at times, overridden by statutory (vocational) requirements.

Moreover, at least at the ALJ hearing level, decisions are considered to be impartial “judgments” rendered by independent ALJs after considering available evidence and in accordance with the program’s rules. Therefore, those judgments are deemed indisputable and irreversible except via appeal to the SSDI Appeals Council and federal courts.³³ Except for those two avenues of reevaluation, no other entity could ever be in a position to validate or challenge individual ALJ decisions.

Nevertheless, ALJ decisions have consequences “in the aggregate” that reveal whether the ALJ system as a whole is “policy compliant.” Data on ALJ case dispositions reveal regularities that appear inconsistent with the system being “policy compliant.” Figure 7 shows the distribution of allowance rates across all ALJs during fiscal years (October of previous year through September of year labeled) 2010, 2011, 2012, and 2013. The statistics underlying the figure show that while 66 percent of the cases decided by ALJs were allowed during fiscal year 2010, the mean allowance rate declined to 54

percent by 2013. Figure 7 also shows that the distribution of SSDI allowances shifted toward the left (toward fewer allowances) between FY10 and FY13.³⁴ It also shows a slight narrowing of the distribution because the black-shaded bars representing the distribution for FY13 are shorter at both ends of the figure compared with the lighter-shaded bars for earlier years.³⁵ Such a leftward shift and narrowing of the distribution is often interpreted as evidence of improved policy compliance by ALJs.

That interpretation does not seem accurate, however. A part of the explanation for those changes may be that the appeals of people who applied during and after the recession of 2008–9 reached the ALJ stage during FY10 to FY13. Many of those cases may have been of work-capable individuals who lost their jobs during the recession. The smaller allowance rates during FY12 and FY13 may reflect a greater proportion of only marginally health-impaired individuals in the applicant pool following the recession. Moreover, ALJ decisions may have shifted toward lower allowance rates following prominent news reports and investigations into fraud committed by ALJs in specific locations. Indeed, further analysis of the ALJ-specific allowance rate information published by SSA is inconsistent with a high degree of ALJ policy compliance:

Imagine that all ALJs are identical individuals. That is, each approaches every case identically and in the manner prescribed by SSDI eligibility rules. Assume, in addition, that disability applications are randomly distributed across ALJs. Under these assumptions, individual ALJ positions within the annual allowance-rate distribution would vary from year to year in a manner consistent with random case assignment. That is, although a particular ALJ may allow a high percentage of cases in one year because of the mix of cases that the ALJ happened to receive in that year, the same (or a similarly high) allowance rate is not likely for the same ALJ in the following year. Under the hypothesis of identical ALJs who strictly follow the law and random distribution of cases across ALJs each year, the cross-year correla-

“Administrative law judge decisions have consequences ‘in the aggregate’ that reveal whether the administrative law judge system as a whole is ‘policy compliant.’”

“The cross-year correlation of allowance rate positions across administrative law judges should be zero — something that can be tested directly.”

Table 1
ALJ Allowance Rate Statistics

Fiscal Year	SSA Region ^a	Mean Allowance Rate (%)	Standard Deviation	Number of ALJs	Cross-Year Correlation
2010–11	1	68.4	14.9	41	0.90
	2	70.3	15.7	85	0.86
	3	64.9	15.3	107	0.91
	4	66.9	15.7	236	0.92
	5	66.4	15.5	139	0.86
	6	59.3	17.1	118	0.89
	7	61.5	14.4	37	0.80
	8	64.8	11.4	23	0.84
	9	68.6	15.6	103	0.91
	10	67.6	15.5	30	0.90
	11	67.7	15.8	37	0.86
2011–12	1	64.1	16.0	36	0.92
	2	67.3	14.7	84	0.89
	3	59.5	16.5	106	0.92
	4	63.7	15.9	263	0.91
	5	57.6	15.3	159	0.87
	6	54.1	16.5	125	0.87
	7	57.4	16.9	41	0.75
	8	61.1	12.4	22	0.88
	9	64.2	14.5	111	0.88
	10	61.8	16.1	32	0.91
	11	56.9	12.2	45	0.69
2012–13	1	58.4	13.7	38	0.94
	2	65.4	14.1	89	0.90
	3	56.1	15.0	104	0.91
	4	58.3	15.2	276	0.90
	5	54.6	14.7	178	0.89
	6	50.1	15.0	117	0.88
	7	49.6	16.2	44	0.90
	8	59.1	10.6	25	0.81
	9	58.4	15.3	117	0.92
	10	55.6	15.8	35	0.91
	11	52.6	12.7	39	0.84

Source: Author's calculations from SSA-published ALJ disposition data, <http://www.socialsecurity.gov/open/data/>.

Note: The calculations exclude the top and bottom 5 percent of the distribution of ALJs according to the number of cases disposed each year.

^a Social Security operations are divided into 10 regions across the United States. The four National Hearing Centers are collectively indicated as Region 11.

tion of allowance rate positions across ALJs should be zero—something that can be tested directly. The last column of Table 1 shows those correlations for three pairs of fiscal years: 2010–11, 2011–12, and 2012–13—separately for each of SSA’s 11 regions to control for region-specific differences in the types of cases that ALJs adjudicate.³⁶

Table 1 shows that in most instances, cross-year correlations in ALJ allowance rate ranks vary between 0.8 and 0.9 across SSA regions. The correlations are also far from zero at the National Hearing Centers (Region 11) where cases from across the nation are adjudicated via videoconferencing. These allowance-rate rank correlations are far higher than is consistent with a random distribution of cases across identical ALJs who consistently “follow the law” in applying SSDI’s rules.³⁷ The correlation differences across regions are quite small, indicating that the high-correlation result is robust to differences in the types of applicants across regions.

Thus, an alternative hypothesis is that case allocations across ALJs are nonrandom. But in that case, one would have to believe that the nonrandom distribution is somehow controlled before ALJ hearings—to consistently allocate cases with high- and low-allowance likelihoods to the same judges each year. Conversations with and testimony by ALJs indi-

cate, however, that cases are not distributed according to any rules involving applicant or ALJ characteristics.³⁸

Another possibility is that ALJ decisions reflect nonuniform applications of SSDI eligibility laws, policies, and procedures by different ALJs. Yet another possibility is that SSDI eligibility laws, policies, and procedures provide a very wide latitude for deciding cases—so wide as to permit ALJs to provide a reasonable, defensible, and legally justifiable basis to allow or disallow any given case.

More recently, ALJs have complained that SSA managers pressure them to process a high caseload, which is suggested as one reason for high allowance rates. Judges who fail to adhere to the workflow and timeliness guidelines set by SSA managers are subject to disciplinary action.³⁹ Some ALJs argue that such pressure for haste makes granting an allowance the easier choice: allowed cases will not be appealed for further review, which could remand the case to the ALJ. As a result, the pressure to dispose of several hundred cases each year results in unwarranted allowances.

To examine that hypothesis, Table 2 shows the correlation between case disposition rates and allowance rates across ALJs for FY10 through FY13. Correlations are calculated for ALJs within the 25th and 75th percentiles and below the 25th percentile of the case-disposi-

“These allowance-rate rank correlations are far higher than is consistent with a random distribution of cases across administrative law judges who consistently ‘follow the law’ in applying Social Security Disability Insurance rules.”

Table 2
ALJ Correlations between Award Rates and Annual Case Dispositions

Fiscal Year	25th and 75th Percentiles of the Case-Dispositions Distribution	Correlation: Award Rate x Annual Case Dispositions (lower, upper 95 percent confidence limits) ^a	
		ALJs above 25th Percentile of Case-Dispositions Distribution	ALJs at or below 25th Percentile of Case-Dispositions Distribution
2010	397, 596	0.326 (0.258, 0.391)	-0.116 (-0.219, -0.012)
2011	403, 596	0.310 (0.244, 0.374)	0.014 (-0.087, 0.114)
2012	415, 601	0.335 (0.271, 0.395)	0.008 (-0.090, 0.106)
2013	434, 579	0.219 (0.151, 0.285)	0.024 (-0.074, 0.123)

Source: Author’s calculations from SSA-published ALJ disposition data, <http://www.socialsecurity.gov/open/data/>.

^a The likelihood that the true correlation lies between the upper and lower limits shown is 95 percent.

“The positive correlations across administrative law judges within the 25th and 75th percentiles of the case-dispositions distributions support the view that caseload disposition pressure may be inducing higher disability award rates.”

tions distribution. That separation was done because ALJs at the lower and upper ends of the distribution either hold positions with managerial responsibilities and, therefore, are expected to conduct fewer disability hearings or are very efficient—that is, they do not feel pressure to achieve high case dispositions each year.

The positive correlations across ALJs within the 25th and 75th percentiles of the case-dispositions distributions support the view that caseload disposition pressure may be inducing higher disability award rates. That view is reinforced by the near-zero correlations for ALJs in the lower 25 percent of the annual case-dispositions distributions.

Those results, and the fact that denied applicants receive multiple opportunities to appeal, including finally appealing to federal district courts, suggest that SSDI is biased toward paying benefits to work-capable individuals.

MOTIVATION FOR A DIFFERENT SSDI BENEFIT STRUCTURE

In an era where American liberals seem inclined to assume an unwavering “hold the line” policy stance against any changes to entitlement programs, while conservatives follow the same strategy when it comes to increasing taxes, is there any middle ground on SSDI reform that the two political parties could conceivably agree to? For a decent chance to succeed, any reform must provide something to both sides. The good news is that one particular approach to reforming SSDI’s benefit structure could appeal to both sides.

SSDI’s current definition of disability and its disability determination procedures introduce strong work disincentives for beneficiaries. That fact is confirmed by the general failure to date of SSA’s initiatives to induce beneficiaries to rejoin the labor force. For example, the Ticket to Work program aims to provide access to employment, vocational, and other support services. Unfortunately, the take-up rate has been extremely low, and the program has had little effect on the rate

at which beneficiaries leave SSDI for work.⁴⁰ Furthermore, the Benefit Offset Pilot Demonstration and the Benefit Offset National Demonstration projects that tested the effect of a gradual reduction in disability benefits—by \$1 for every \$2 earned above the substantial gainful activity (SGA) level, thereby removing the “cash cliff” of full benefit loss upon working beyond the SGA earnings level—have generated poor and unreliable results.⁴¹

Those outcomes notwithstanding, several studies indicate considerable residual work capacity among SSDI beneficiaries. According to one study, which compared cohorts of identical SSDI applicants, some of whom were allowed but others denied SSDI benefits, the work activity of rejected applicants suggests that more than one-quarter of SSDI beneficiaries are likely to have additional, unused work capacity.⁴² Another study using cases at the ALJ hearings stage finds that the likelihood of working if rejected is as high as 35 percent.⁴³ Yet another study finds that as many as 40 percent of disability beneficiaries may be work-oriented (report having work goals and expectations) and work-capable (those with current or recent work activity and those looking for work).⁴⁴ In the future, more beneficiaries are likely to be work-capable if past SSDI decisional trends persist.⁴⁵ Under that outlook, the time seems ripe to introduce a benefit system that allows SSDI beneficiaries to contribute to economic productivity—if they can. Fortunately, even within the existing definition of disability, it is possible to redesign the benefit structure to accommodate more robust work incentives for individuals with disabilities.

A BETTER DISABILITY INSURANCE BENEFIT STRUCTURE

This section outlines how such an incentive-compatible benefit structure could be introduced. Note that eligibility to full benefits when a person cannot work can be preserved even if benefits are not paid (or are reduced) in periods when the beneficiary chooses to work

and earn well above the SGA level. The benefit amount could be adjusted (reduced or temporarily suspended) when a beneficiary works. But current benefit-offset pilot programs implement that separation of eligibility and payments inflexibly by reducing benefits by \$1 for every \$2 that a beneficiary earns above the SGA level. That reduction is a 50 percent marginal tax rate on earnings, which cannot be considered to be a robust “work incentive.”

A better labor-market incentive would combine benefit offsets with variable wage subsidies. Under this “generalized benefit offset” (GBO), beneficiaries would choose when and how much to work according to their health conditions, labor market opportunities, and work abilities. If a beneficiary has sufficiently high earnings in any period, he or she would receive a smaller benefit out of SSDI’s trust fund but would also receive a wage subsidy (from a different federal funding source) that increases with earnings up to a certain level well beyond SGA. Over that range, the earnings subsidy would increase the beneficiary’s income faster

than the increase in earnings. Such a subsidy would provide a more robust work incentive.

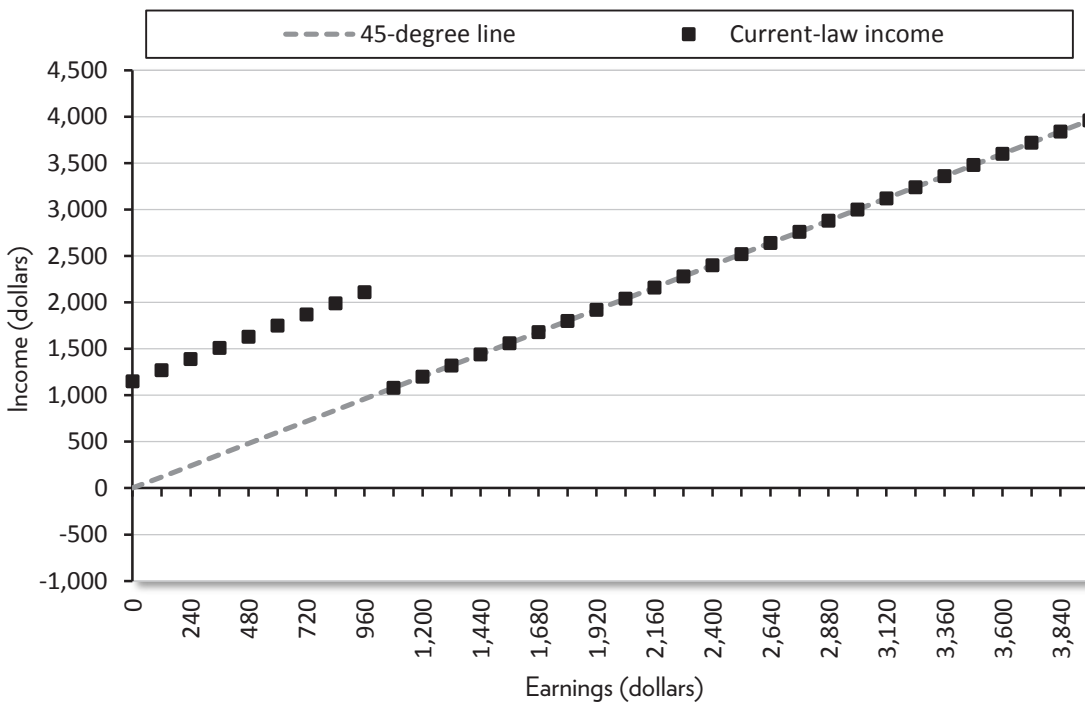
That payment structure should induce labor force reentry by beneficiaries who retain work abilities. However, it is likely to be effective only if SSDI benefits are restored when earnings decline, for whatever reason. In essence, GBO would provide a flexible, pro-work system of payments to those who have been admitted onto SSDI. A key advantage of GBO’s benefit structure is that it would incentivize SSDI beneficiaries who can work to self-select into working rather than remaining out of the labor force, thereby inducing voluntary labor market choices that would better reveal beneficiaries’ work capabilities and are better suited to their economic preferences and opportunities.

**HOW GBO WOULD WORK:
AN EXAMPLE**

The GBO approach involves switching disability payments at the margin from one that

“Under this ‘generalized benefit offset,’ beneficiaries would choose when and how much to work according to their health conditions, labor market opportunities, and work abilities.”

Figure 8
Current-Law SSDI Income Schedule (SSDI Primary Insurance Amount=\$1150)



Source: Author’s calculations based on Social Security Disability Insurance Benefit Laws.

“Disability payments should be switched at the margin from one that pays workers to remain idle to one that pays them to work, if they can.”

pays workers to remain idle to one that pays them to work, if they can. As I argue in *Regulation*, that switch in the benefit structure makes sense because, under SSDI’s current benefit structure, most beneficiaries do not work despite strong, albeit indirect, indications that they possess residual work abilities.⁴⁶ And those who do work limit their earnings because, as Figure 8 shows, they face a steep cash cliff of losing SSDI benefits if earnings exceed the SGA threshold.

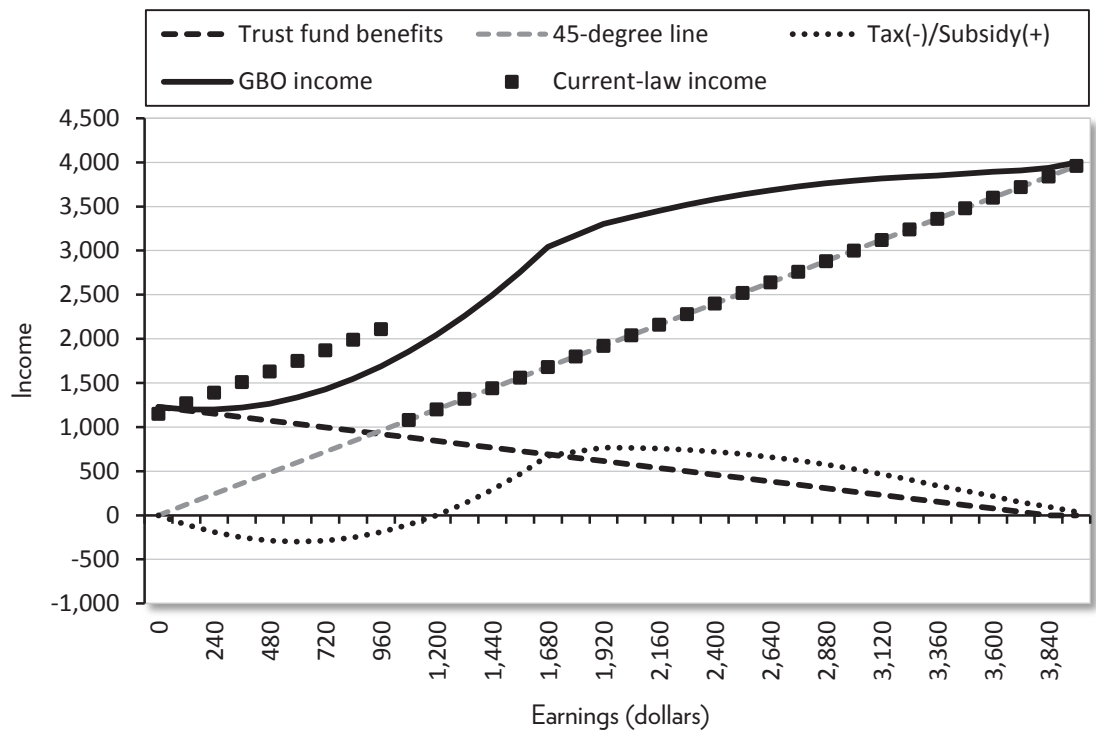
Figure 8 considers a beneficiary with a primary insurance amount (PIA) of \$1,150 per month. The 45-degree line in the figure (line in dashes) translates earnings (shown on the x-axis) into income (y-axis) dollar for dollar. With zero earnings, income is \$1,150 per month. The line with black squares in Figure 8 shows how income increases as the beneficiary’s earnings increase. The sharp income decline is the “cash cliff” work disincentive, which induces many beneficiaries to remain out of the

work force or to limit earnings to below the threshold that causes accruals of trial work period (TWP) months. They also fear triggering a Continuing Disability Review and ultimately losing SSDI benefits.⁴⁷

Instead of a benefit structure that incorporates the cash cliff, SSDI benefits should be the sum of two components: a trust fund-financed “safety-net benefit” and a general fund-financed “work-incentive benefit.” The two components of such a GBO system would be determined by the beneficiary’s past observed earnings. Figure 9 shows how that benefit structure would work.

At zero earnings, the safety-net benefit under GBO (line with dark dashes) is slightly increased above the PIA—an initial benefit enhancement. Marginal earnings are initially subject to a high wage-tax rate, resulting in a negative subsidy to earnings when earnings are low (line with small dots).⁴⁸ As earnings increase (moving rightward along the x-axis),

Figure 9
GBO and Current-Law SSDI Income Schedules
 (SSDI Primary Insurance Amount=\$1150)



Source: Author’s GBO benefit design.

the safety-net benefit and the wage tax rate are both reduced. Although the dollar amount of wage taxes paid (negative subsidy accrued) increases over an initial range of low earnings, GBO (total) income (unbroken line)—which is the sum of earnings (45-degree line), safety-net benefits (line with dark dashes), and the earnings tax or subsidy (line with small dots)—increases as earnings increase. At a yet higher earnings level, while safety-net benefits continue to decline, the wage tax changes into a wage subsidy to eventually boost income at a faster rate than earnings. In Figure 9, the slope of the total GBO income (unbroken) line is steeper than that of the 45-degree line for earnings just above the SGA level. As earnings increase still further, the wage subsidy is gradually withdrawn. It is completely withdrawn in Figure 9 where the total GBO income line joins the 45-degree line at the highest earnings level shown. The parameters and calculations that generate the GBO schedule described here are detailed in Appendix A.

Figure 9 also shows income under current law (black-square markers) that induces beneficiaries not to work or to limit earnings for fear of triggering a CDR or accruing TWP months toward eventual loss of SSDI benefits. In contrast, introducing a GBO reform of the benefit structure would encourage those beneficiaries to work and increase their earnings well above the SGA level of earnings. The reason is that under a GBO, working would never result in complete cessation of eligibility to safety-net benefits, even when beneficiaries earn well above the highest earnings shown in Figure 9 for any length of time. Job separations would result in a leftward slide along the total GBO income schedule, with the wage subsidy eliminated but safety-net benefits restored to their enhanced level at zero earnings.⁴⁹

A concern may arise about why GBO's two-element benefit structure would work better than work incentives attempted by SSA to date. The fact is that it is impossible to directly observe how many of today's beneficiaries could and would work under a different system. The work incentive systems

attempted by SSA thus far are inflexible and of questionable efficiency simply on the basis of economic principles. GBO's system, on the other hand, is based on a more careful consideration of the principles of contract design under imperfect information. That is, it is designed with the objective of incentivizing beneficiaries themselves to reveal their work abilities through labor market choices by acting in their own interest to improve their incomes and living standards through work and earnings under a system that continues to protect them. GBO protects those who cannot work by providing more generous benefits, protects SSDI benefit eligibility for those who can and do choose to work, and provides continuously increasing financial incentives to remain employed over a sizable earnings range beyond the SGA level. Such a system is likely to be more effective than the work incentive programs attempted thus far for the reasons described below. Appendix B discusses administrative issues involved in implementing a GBO reform of SSDI's benefit structure.

In Figure 9, a vertical point-by-point comparison between current-law income (black-square markers) and the total GBO income schedule (black unbroken line) suggests that although GBO provides higher income than under current law for earnings beyond SGA, a segment of the GBO schedule remains below the current-law income level when earnings are below the SGA level. Thus, although work-capable individuals would be able to shift to a better point on the GBO schedule (making a vertical point-by-point comparison of current law with the GBO schedule inappropriate for them), those who cannot increase their work effort may be made worse off. That criticism of the GBO schedule, as calibrated in Figure 9, appears to be valid. It should be noted, however, that the wage tax/subsidy design of GBO is intended to induce those beneficiaries who are "parked" at or below SGA to shift upward along the GBO schedule. Providing a strong work incentive requires reduced income at current work and earnings levels and the pros-

“At a yet higher earnings level, while safety-net benefits continue to decline, the wage tax changes into a wage subsidy to eventually boost income at a faster rate than earnings.”

“Because the current system discourages work by Social Security Disability Insurance beneficiaries, the generalized benefit offset reform is designed to elicit a positive labor market response.”

pect of a substantial boost to income from working and earning more. The SSDI benefit enhancement at the zero (and low) earnings levels is intended to compensate those who cannot shift to a higher earnings level under GBO and, therefore, could become worse off. Indeed, not imposing a small cost on those earning at moderate levels under current law would dilute the wage incentive for beneficiaries to move to a higher working and earning level. As currently calibrated, the GBO schedule involves trading off SSDI trust fund benefits for wage subsidy expenditures on a roughly even basis. Of course, the initial benefit enhancement could be made even more generous, but only at a higher taxpayer cost.

UNCERTAINTY ABOUT HOW MUCH GBO WOULD COST THE FEDERAL GOVERNMENT

The most widely recognized cost estimates of Social Security reform proposals are those prepared by the Office of the Chief Actuary of the Social Security Administration and the Congressional Budget Office. Those agencies estimate the costs of proposed legislation on the basis of information about how the private sector would respond to new initiatives and incentives provided under proposed laws. In the case of SSDI, however, although there are several sources of information on the work capability of SSDI beneficiaries, those sources are based on indirect evidence from self-reports on earnings and work intentions and the work activity of denied applicants.

Although the studies cited earlier suggest considerable work potential among SSDI beneficiaries, little reliable evidence exists on the extent to which DI beneficiaries might expand their labor force participation under a new system of work incentives and credible protection against loss of beneficiary status upon working under a GBO-type reform. The fear of losing SSDI benefits prevents many beneficiaries from joining the labor force and induces many to restrict their work hours and earnings to remain below the SGA level. Reli-

able information on the potential increase in beneficiary earnings can be obtained only by actually introducing a GBO-type work incentive program, permanently and irrevocably, to convince beneficiaries that working under GBO for any length of time will not result in the cessation of SSDI eligibility upon job separations.⁵⁰

Because the current system discourages work by SSDI beneficiaries, the GBO reform for SSDI is designed to elicit a positive labor market response. A key question concerns how such a reform should be financially scored. In the case of GBO, there are three distinct reference points and two alternative scoring baselines to consider. The reference points are:

1. Current SSDI law and the existing distribution of labor force participation by beneficiaries. Most would remain out of the labor force, many would be “parked” at earnings below SGA, and very few would exit SSDI by earning more than SGA.
2. GBO with zero behavioral labor market response by beneficiaries who sustain their labor market choices as under current SSDI law.
3. GBO with a significant positive labor-market response by beneficiaries to generate more work hours per year.

Of course, the relevant comparison is between the alternatives 1 and 3 because alternative 2, it is expected, will not be realized.⁵¹

The two scoring alternatives are “current law” and “current benefits.” Under the former, government expenditures under GBO (the sum of post-adjustment trust fund benefits and the wage tax or subsidy) would be compared with current-law benefits. But because benefits are terminated under current law when earnings exceed SGA (beyond the nine-month TWP), GBO would be scored to show a large additional cost for the federal government on account of those who begin working and earning above SGA once GBO is introduced.

Because the increase in work effort would not materialize if GBO were not introduced, beneficiaries whose labor market response crosses the SGA threshold after GBO is introduced should be evaluated on a “current benefits” base-line: their base-line SSDI benefits should not be scored at zero (as they would be under current law), but at their pre-GBO benefit level—the federal cost that would be realized if GBO is not introduced.

One noteworthy item is that even if GBO’s net federal cost is positive (it would smaller under the “current benefit” scoring alternative), any increase in labor force participation and earnings that GBO generates would have positive effect on national productivity and output each year after GBO is introduced. But budget-agency evaluations of policy proposals usually take no account of such wider economic effects.⁵² Finally, criticisms based on program cost that some analysts levy against the Earned Income Credit program do not apply to GBO as explained in Appendix C.

A final point concerns the federal financing structure for GBO. GBO’s benefit reductions triggered by beneficiaries who work would generate direct saving for the SSDI trust fund. However, if many beneficiaries choose to work and earn just enough to take full advantage of GBO’s wage subsidy, additional expenditures would be required from the federal government’s general budget account. To avoid duplicating payment infrastructure, both payments—net SSDI trust fund benefits (after adjustment for past earnings) and the wage tax or subsidy—could be provided to all SSDI beneficiaries by one agency: the Social Security Administration. Congress should mandate the annual provision of general funds to SSA as needed to finance net wage subsidy expenditures. Thus, the general fund expenditure on net wage subsidy should be a “mandatory” (not “discretionary”) item in the federal budget, similar to the funding of non-premium-covered expenditures on the Supplementary Medical Insurance and prescription drug program (Medicare Parts B and D). General fund transfers for prospective GBO subsidy pay-

ments would be based on estimates and reconciled later with actual wage subsidy expenditures (net of wage taxes levied) at the end of each fiscal year.

GBO’S ADDITIONAL ADVANTAGES

The GBO adjustments to SSDI benefits represent a marginal change in SSDI’s payment structure. The question arises whether GBO would induce an increase in the SSDI rolls, as workers who previously chose to continue working would now choose to work *and* receive GBO’s protection and wage subsidies. Such “induced entry” is possible but seems unlikely to be large for a number of reasons. GBO generates a countervailing incentive: The level of the total GBO income schedule depends on the worker’s SSDI PIA, which in turn depends on pre-SSDI earnings. It means that for those who can continue to work despite their medical impairments, there would be an advantage to delaying the application for SSDI in order to accrue a larger PIA and eventually be placed on a higher total GBO income schedule once they apply and are admitted into SSDI.

Furthermore, potential applicants with medical impairments who wish and are able to remain employed, would have to weigh the financial costs and time gap in employment and earnings that would be involved if they decided to apply for SSDI benefits under the program’s current laws and adjudication procedures. The process can take anywhere from six months to more than a year, and the outcome of eventually being awarded beneficiary status is uncertain. Moreover, the process would likely take more time for people with less severe impairments. The gap in employment involved in applying to SSDI, including the concomitant depletion of skills, work abilities, and employment prospects, may make applying for SSDI just to benefit from GBO’s insurance protection unattractive. Additionally, for workers who are strongly oriented toward self-reliance through work, the social stigma of reliance on government benefits that SSDI and GBO involve may be unacceptable.

“Even if the generalized benefit offset net federal cost is positive, any increase in labor force participation and earnings that it generates would have positive effect on national productivity and output each year after it is introduced.”

“Individuals allowed into the program under the general benefit offset could not be removed unless their medical condition improves and no longer satisfies the program’s medical criteria.”

Introducing GBO would enable working beneficiaries to accrue a higher PIA for their eventual shift into Old-Age and Survivors Insurance upon attaining the normal Social Security retirement age. But for workers committed to remaining employed, such accrual of a higher PIA is already feasible by continuing current employment rather than by applying for SSDI to obtain coverage under GBO. Indeed, the accrual of a higher PIA would be impeded by time spent out of work during SSDI’s application and adjudication processes.

GBO is likely to make the SSDI’s vocational criteria less relevant, certainly for conducting CDRs. Under GBO, once individuals are on SSDI, beneficiaries who wish to work would seek jobs to exploit the earnings incentive in GBO. Some will find appropriate placements while others will not; some may work at regular jobs, and others may work intermittently—but all who are admitted and remain on the program would be supported under GBO with appropriate adjustments to their benefits and earnings, depending on their labor market outcomes. Note that provisions of the Americans with Disabilities Act provide an extensive legal framework to support SSDI beneficiaries (and others with medical impairments) by requiring employers to offer reasonable work accommodations.

Over time, GBO would facilitate refining the medical criteria for awarding SSDI benefits to applicants. Individuals allowed into the program under GBO could not be removed unless their medical condition improves and no longer satisfies the program’s medical criteria.⁵³ However, the work activity of the current pool of beneficiaries would inform policymakers and program adjudicators of how medical criteria for admitting individuals to the program should be revised for the future. Those revisions should take into account the work activity of beneficiaries with specific medical impairments. That system could dynamically adjust SSDI medical criteria according to objective, market-based information on the changing linkage between medical impairments and the likelihood of productive work.

That approach would be preferable to today’s vocational decision making that relies on a decades-old compendium of the types of jobs available in the U.S. economy.⁵⁴

COMPLEMENTARITY BETWEEN GBO AND PRE-ENTITLEMENT SSDI REFORMS

Under a low growth and tight federal budget environment, which appears likely to persist, some analysts have proposed policies intended to prevent or delay program entry by workers experiencing the onset of disabling impairments but who nevertheless retain some capacity to work.⁵⁵ Pre-entitlement reforms to provide such employment supports would work well only if workers are appropriately targeted. But targeting the right group of workers requires identifying those more likely to apply for SSDI—a difficult task when the base population encompasses almost the entire U.S. work force.⁵⁶ Mission creep to provide unneeded benefits and behavioral responses by workers to be included in the targeted worker group could escalate costs, subverting the goal of efficiently providing pre-SSDI support for individuals to delay or prevent their entry into SSDI. Recent research suggests that early-intervention initiatives may extend labor force participation by those with medical impairments but seem unlikely to delay or prevent applications to SSDI.⁵⁷

These considerations mean that GBO’s combination of safety-net protection with earnings subsidies would induce additional SSDI applications by those who are still able to work despite their medical impairments but who also perceive a high risk of worsening health and need for safety-net support. Such induced entry from the introduction of GBO could provide the correct “screening mechanism” for targeting pre-entitlement early-intervention programs.⁵⁸

CONCLUSION

A multitude of changes—labor market competition and globalization, the changing nature

of work, demographics, worker skills, improvements in technology, the legal environment, and others—have made it increasingly difficult to distinguish between medically impaired individuals who are able to work at a substantial earnings level from those who are not. The current disability allowance process takes a long time to complete and is susceptible to errors. Statistical evidence on disability allowances at the administrative law judge level suggests either poor disability policy compliance or policies with such excessive latitude as to allow large decision errors. Because applicants can appeal denials several times, including to the federal courts, the Social Security Disability Insurance’s systematic errors appear biased toward allowing work-capable individuals onto SSDI rolls.

SSDI’s single-minded focus on providing benefits to only those who cannot work above SGA earnings saps medically impaired workers’ motivation to continue working (or seeking work) and induces them to seek SSDI enrollment. That growing trend is assisted by the professionalization and commercialization of disability case representations. It is time to augment SSDI’s goal of providing wage-replacement support to the disabled by a second and opposing objective: preserving the incentive to work for individuals with medical impairments.

Two tasks are involved in achieving the second objective: (a) preserving the labor force attachments of medically impaired workers (pre-entitlement reforms) and (b) providing wage-replacement support on the basis of beneficiaries’ observed labor market attachments under a system that provides effective incentives to work (post-entitlement reforms). This paper describes the role that a generalized benefit offset reform could play in achieving the second task and argues that its introduction would help toward achieving the first task as well.

The GBO changes the nature of SSDI benefits at the margin, shifting from paying benefi-

ciaries a “wage-replacement benefit” to remain disengaged from the work force to paying them an “earnings subsidy” to rejoin the work force if they can. Although the adjustments would be delivered with a time lag, relief from the current “cash cliff” of benefit loss if earnings exceed the SGA level would be eliminated. That change would free work-capable beneficiaries to improve their living standards by pursuing gainful employment.

SSA actuaries have not yet officially scored the GBO reform proposal. However, this approach is likely to be better than the work-incentive programs being tested by SSA. Economic analysis clearly shows that GBO would provide a stronger work incentive at a potentially low cost to the federal budget when GBO is scored appropriately. For example, GBO will be less costly than the existing Earned Income Tax Credit program under the federal income tax, because it offsets the cost of wage subsidies by reducing the trust fund–financed benefits of those who choose to return to work. It permanently preserves SSDI’s safety net for working beneficiaries if and when they experience job separations, either because of poorer health or because of labor market downturns. GBO’s chief appeal is that it would allow beneficiaries to self-reveal their work capabilities—a better approach than relying on bureaucratic rules. GBO permits the buildup of earnings records for attaining higher Old Age and Survivors Insurance primary amounts and benefits during beneficiaries’ retirement phase.

Finally, the introduction of GBO may generate “induced entry” into SSDI. People who seek to enroll in order to benefit from SSDI’s new earnings incentive and safety-net protection under GBO would be appropriate targets for pre-entitlement early-intervention programs that some analysts have proposed. Overall, the introduction of GBO is likely to improve the welfare of individuals with disabilities, reduce the SSDI’s trust fund expenditures, and boost national output.

“Economic analysis clearly shows that general benefit offset would provide a stronger work incentive at a potentially low cost to the federal budget when it is scored appropriately.”

“The calibration of the general benefit offset income schedule is designed to continually increase the beneficiary’s income when earnings increase.”

APPENDIX A: DERIVATION OF THE GBO SCHEDULE IN FIGURE 9

The generalized benefit offset (GBO) schedule is based on the beneficiary’s primary insurance amount (PIA) calculated under current Social Security Disability Insurance (SSDI) rules.⁵⁹ Under GBO, the PIA of a disabled beneficiary is first rounded to the nearest \$100 and the result divided by 5 to determine the *earnings step* (ES). Next, the PIA is rounded to the nearest \$10 and divided by 15 to provide the *benefit step* (BS). For example, a PIA of \$1,072.40 rounded to the nearest \$100 yields \$1,100, and dividing by 5 yields ES = \$220. And rounding the same PIA to the nearest \$10 yields \$1,070, and dividing by 15 yields BS = \$71.33.

All adjustments are made beginning with the PIA rounded to the nearest \$10—\$1,070 in this example—and values are shown to the nearest \$0.1. If this beneficiary has no earnings under GBO, the SSDI benefit would be \$1,070.00 + \$71.3 = \$1,141.3, reflecting the benefit enhancement at zero earnings, because it is larger than the beneficiary’s PIA.

Under GBO, SSDI beneficiaries are permitted to work as much or as little as they wish, with no waiting period and no threat of benefit and health coverage cessation, no matter the size of earnings or duration of labor force attachment. Larger earnings lead to a larger negative adjustment to benefits funded out of the SSDI trust fund. The adjustment is applied linearly to benefits at the rate of $-BS \div ES$. In the example above, the rate of benefit adjustment would be $-\$71.33 \div \$220 = -0.32423$. Thus, if the beneficiary earned \$1,650 in a particular month, SSDI trust fund benefits would be $\$1,141.3 - (0.32423 \times \$1,650) = \$606.3$. Column (2) of Table A.1 shows how SSDI trust fund benefits decline under GBO as earnings shown in column (1) increase.⁶⁰

Under GBO, low earners are subject to an

earnings tax that gradually transforms into an earnings subsidy as earnings increase. The average GBO rate of tax or subsidy on earnings is 100 percent at zero earnings (implying a zero tax liability for those who do not work) and declines continuously, anchored to values shown in column (3) of Table A.1. Note that the average GBO earnings tax or subsidy rate declines with earnings through the first eight earning steps, to reach -40 percent. The earnings subsidy is gradually withdrawn for yet higher earnings, and it is withdrawn fully after the 17th earnings step. Column (4) of Table A.1 shows that earnings of \$1,650 would generate an earnings subsidy of \$660. Adding together earnings and adjusted trust fund benefits and subtracting the earnings tax (if negative, the subtraction operation would add the subsidy value)—[column (1) plus column (2) and minus column (4)]—yields total GBO income shown in column (5).

The calibration of the GBO income schedule shown in column (5) is designed to continually increase the beneficiary’s income when earnings increase. It is intended to deliver a faster increase in income than the increase in earnings over a segment of earnings beyond SGA (as shown in Figure 9 in the text). The calibration of the GBO income schedule is conditional on the tax or subsidy rates, the earnings step, and the benefit step calculations as described above. Given those fixed parameters, the beneficiary’s PIA, which is calculated based on the beneficiary’s pre-SSDI earnings history, would determine the level and range of the GBO income schedule that would apply for determining the two adjustments described above. Thus, because beneficiaries with a higher PIA are likely to have higher earnings potentials even after enrolling into SSDI, they would be placed on a GBO schedule with a similar pro-work incentive structure, but one that extends over a broader earnings range.

Table A.1
GBO Schedule Calculation Example (SSDI PIA = \$1,070 per month)

Step	Earnings	SSDI Trust Fund Benefits	Average Tax or Subsidy Rate	Tax (+) or Subsidy (-) (Federal General Fund)	GBO Income
	(1)	(2)	(3)	(4) = - (1)x(3)	(5)=(1)+(2)+(4)
1	110.0	1,105.7	0.900	99.0	1,116.7
2	330.0	1,034.3	0.700	231.0	1,133.3
3	550.0	963.0	0.500	275.0	1,238.0
4	770.0	891.7	0.300	231.0	1,430.7
5	990.0	820.3	0.100	99.0	1,711.3
6	1,210.0	749.0	-0.100	-121.0	2,080.0
7	1,430.0	677.7	-0.300	-429.0	2,536.7
8	1,650.0	606.3	-0.400	-660.0	2,916.3
9	1,870.0	535.0	-0.375	-701.3	3,106.3
10	2,090.0	463.7	-0.325	-679.3	3,232.9
11	2,310.0	392.3	-0.275	-635.3	3,337.6
12	2,530.0	321.0	-0.225	-569.3	3,420.3
13	2,750.0	249.7	-0.175	-481.3	3,480.9
14	2,970.0	178.3	-0.125	-371.3	3,519.6
15	3,190.0	107.0	-0.080	-255.2	3,552.2
16	3,410.0	35.7	-0.040	-136.4	3,582.1
17	3,630.0	0.0	-0.010	-36.3	3,666.3

Source: Author's calibration of the Generalized Benefit Offset reform.

“The calibration of the generalized benefit offset income schedule is conditional on the tax or subsidy rates, the earnings step, and the benefit step calculations.”

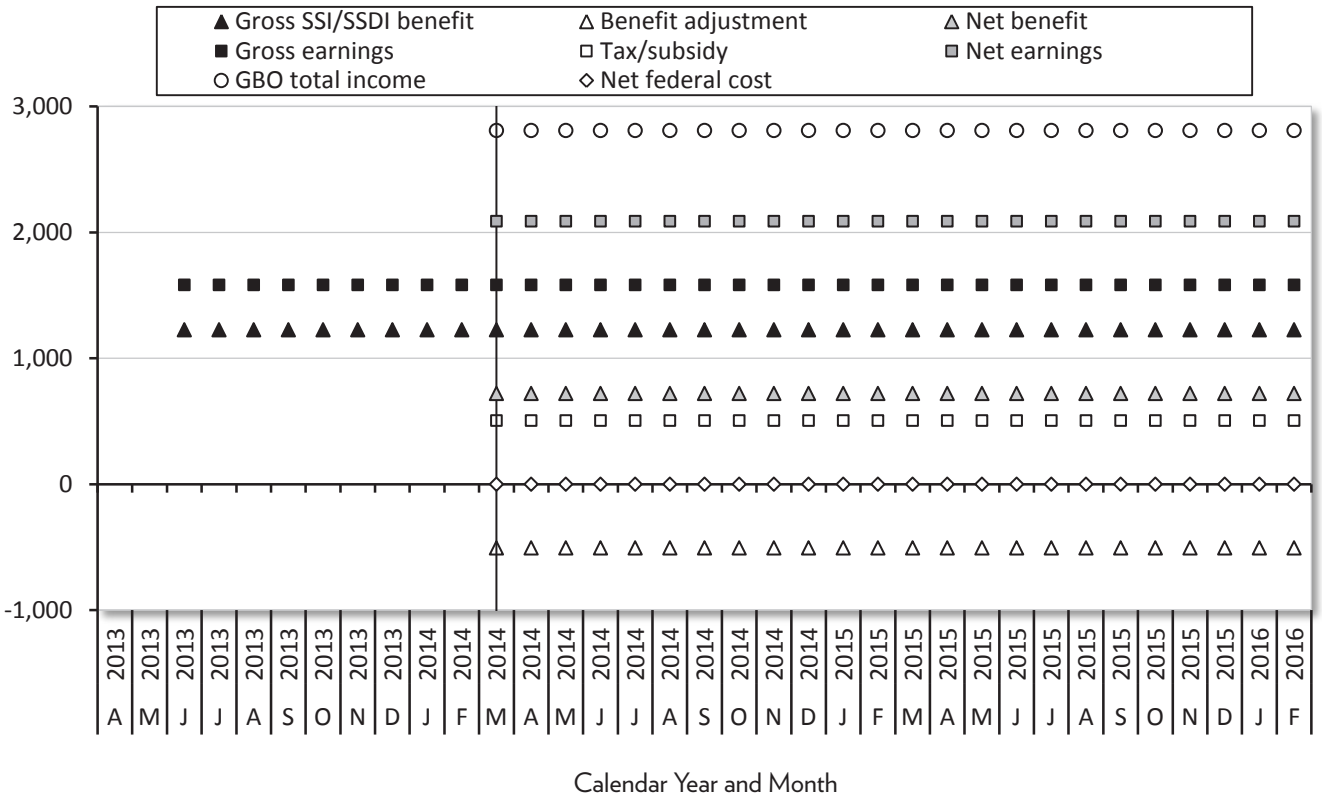
APPENDIX B: ADMINISTRATIVE AND ANCILLARY CONSIDERATIONS OF GBO IMPLEMENTATION

The generalized benefit offset approach involves a change in the structure of Social Security Disability Insurance benefits, one that at the margin substitutes payments for working in place of payments for remaining off the labor force. GBO’s wage tax or subsidy and adjustments to SSDI benefits for each beneficiary would be simplest to administer if they are based on quarterly state unemployment agency reports on individual worker earnings. Employers in each of the 50 states and the District of Columbia, Puerto Rico, and the U.S. Virgin Islands report wage and employment information for each person employed in their establishments during each calendar quarter. Those reports cover more than 97 percent of

employees in nonfarm payroll employment. The quarterly wage reports can be the basis for implementing GBO’s benefit and tax or subsidy adjustments.

Because employers submit their quarterly wage reports only after a time lag following each calendar quarter, a working SSDI beneficiary’s benefit and wage-tax or subsidy adjustments cannot be based on earnings from the immediately preceding quarter—to provide time for gathering and reporting the relevant earnings information. Thus, for a month in quarter 4 (say December), GBO adjustments could be based on average monthly earnings (AME) during the six months covering quarters 1 and 2 of the current year (January through June). Earnings during quarter 3 (July through September) of the current year would not be included for calculating AME on which December’s GBO adjustments would be based. For this case, quarters 1 and 2 of the current year are “GBO quarters.”

Figure B.1
Gross and Net Benefits, Adjustments, Earnings, and Income under GBO Constant Earnings



Source: Author’s calculations based on GBO benefit design (see Appendix A).

Of the six GBO quarter months used for calculating AME for determining December's GBO adjustments, only the months after the month of first eligibility to SSDI would be included in the AME calculation. For example, a person who becomes eligible for SSDI benefits in February and begins working immediately would receive the first GBO adjustments in December of the same year (March through November being the nine minimum necessary intervening months after the month of first SSDI eligibility). However, out of the six GBO quarter months, January and February would not be AME-eligible, because SSDI beneficiary status commenced in February. Thus, in that case, AME during GBO quarters (quarters 1 and 2 of the year) would be based on earnings during March through June. During January of the following year, GBO adjustments would be based on AME computed over the six months during the second and third quarters of the previous year (April through September), all of which are AME-eligible months because SSDI eligibility was acquired before April.

Such an implementation of GBO's benefit structure for SSDI would be administratively simple because GBO's benefit and tax or subsidy adjustments would not be based on beneficiaries' self-reported earnings. To examine how GBO would operate under this administrative setup, consider Figure B.1. The figure shows the case of a beneficiary who is allowed into SSDI in May 2013 and becomes eligible for GBO adjustments during March 2014—after nine full intervening months have elapsed. The SSDI benefit adjustment and tax or subsidy that would be levied or paid during March 2014 would be based on average earnings during four AME-eligible months (June through September) of GBO quarters in 2013 (quarters 2 and 3).

A large majority of those who are allowed onto SSDI are unlikely to begin working immediately. But since GBO would allow working and earning to begin at the beneficiary's discretion, with full guarantee of adjustments to gradually restore SSDI benefits upon exit

from the work force, some beneficiaries who are work-capable may begin working soon after receiving their benefit eligibility notice from the Social Security Administration. In Figure B.1, it is assumed that the beneficiary begins working in June 2013, the month immediately succeeding May 2013, when SSDI eligibility was acquired. The beneficiary's SSDI primary insurance amount is assumed to be \$1,150 per month, post-entitlement earnings are constant at \$1,583 per month (dark squares), and the unreduced SSDI benefit (which would be retained by the beneficiary if AME were zero) equals \$1,227 per month (dark triangles). That makes the beneficiary's monthly gross income equal to \$2,810 (white circles). However, the AME of \$1,583 per month during GBO quarters for March 2014 (quarters 2 and 3 of 2013) triggers a benefit reduction of \$506 per month (white triangles). Those benefit adjustments are shown during the months in which they would be levied, beginning in March 2014. That makes net SSDI benefits in March 2014 equal to \$721 (gray triangles). Moreover, AME of \$1,583 during GBO quarters also trigger a wage subsidy of \$506 per month (white squares), resulting in net earnings (earnings plus subsidy) of \$2,089 (gray squares) during March 2014. In this particular case, the benefit adjustment and the wage subsidy fully offset each other, implying zero net cost to the government (white diamonds on the x-axis), while the beneficiary's total income is \$2,810 per month (white circles).⁶¹

Under GBO, the benefit adjustment and the wage tax or subsidy would be administered by SSA. Total post-adjustments GBO income would be subject to normal income and payroll taxes. And the beneficiary's pre-adjustment earnings (employer gross wages) would count toward calculating average indexed monthly earnings for calculating future Social Security PIA and retirement, survivor, child, and other benefits—an added incentive for work-capable beneficiaries to return to work.

GBO's benefit structure reform relieves the "cash cliff" constraint under current law that prevents SSDI beneficiaries from work-

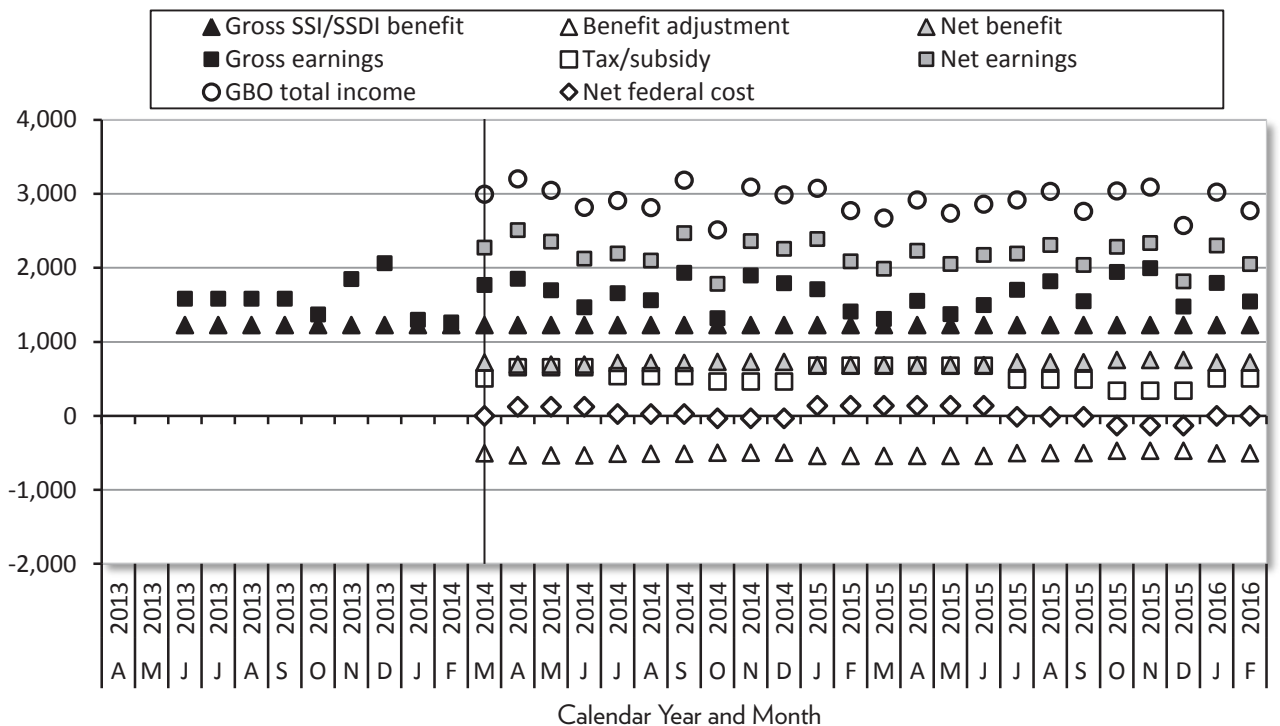
“Implementing the general benefit offset benefit structure for Social Security Disability Insurance would be administratively simple because the benefit and tax or subsidy adjustments would not be based on beneficiaries' self-reported earnings.”

ing beyond the substantial gainful activity earnings. By allowing work and earnings at a higher rate, GBO allows and incentivizes beneficiaries to earn and sustain a higher living standard than would be possible under current SSDI laws (SSDI PIA of \$1,150 + earning at SGA of \$1,170 = \$2,320). In the case of Figure B.1, post-entitlement earnings are assumed to remain constant, making all of the other items—including AME, benefit and wage-subsidy adjustments, income after adjustments, and net federal cost—also constant.

Some disabled individuals may obtain steady employment and enjoy constant earnings. However, others may experience greater volatility in job attachments and earnings. Figure B.2 shows the case of a beneficiary with earnings that are initially steady at \$1,583 per month but are randomized around that level beginning in October 2013 (black squares). In this case, as earnings vary, AME calculated over rolling GBO quarters also change over time, triggering change in benefit adjustments and the wage

subsidy.⁶² However, because AME are calculated by averaging earnings over six-month periods of rolling GBO quarters, changes in AME and in adjustments to benefits (white triangles) and to earnings (white squares) are much less volatile than earnings. When earnings during GBO quarters and AME are low, the wage subsidy is reduced, but SSDI net benefits (after adjustment) increase—both changes occurring after a one-to-three quarter time lag. When earnings are high, the opposite changes occur, again after a time lag. In this case, as before, the net federal cost of the two adjustments is quite close to zero (white diamonds). But the beneficiary is freed from the current law’s cash-cliff constraint against working and earning at more than the SGA level. Note that total GBO income (income after adjustments, shown as white circles) is just as volatile as gross (pre-adjustment) earnings (dark squares), implying the potential need for developing savings plans to smooth working beneficiaries’ living standards over time.⁶³

Figure B.2
Gross and Net Benefits, Adjustments, Earnings, and Income under GBO Randomized Earnings



Source: Author’s calculations based on GBO benefit design (see Appendix A).

APPENDIX C: CRITICISMS OF FEDERAL EARNED INCOME CREDIT PROGRAM ARE NOT APPLICABLE TO GBO

It is worth noting that although generalized benefit offset introduces an earnings incentive similar to the federal Earned Income Tax Credit program, the two main criticisms usually leveled against the EITC program are not applicable to GBO. The first criticism of the EITC is that providing an earning incentive by way of a wage subsidy to low-wage workers also introduces a disincentive to work at a higher earnings level as the EITC is withdrawn. That disincentive means workers depress their work activity and earnings to avoid the high marginal wage tax that EITC withdrawal creates. In the case of Social Security Disability Insurance, however, no one (or only a very few SSDI beneficiaries) currently work and earn in the range where withdrawal of GBO's wage subsidy would create a work disincentive. Indeed, GBO is intended to induce beneficiaries' earnings to a higher level than substantial gainful activity. Any wage disincentive at higher earnings levels would come into play only if and when SSDI beneficiaries begin to earn at higher levels.

Second, the EITC's wage subsidy must be tax financed, which creates additional dead-

weight economic losses from the higher taxes required to finance the low-earner wage subsidy. However, GBO's wage subsidy expenditures would be accompanied by reductions in SSDI's trust fund benefits, potentially fully offsetting and possibly even reducing overall federal expenditures. In overall economic terms, it means any net expenditure increases from the enactment of GBO would be more than counterbalanced by SSDI beneficiaries' positive labor market response and boost to national economic output.

GBO's alternative benefit structure is consistent with maintaining current rules for medical coverage (Medicare after 24 months, continued for 93 months after benefit cessation before age 65, and Medicare buy-in post 93 months). Moreover, GBO could be introduced for current as well as new SSDI beneficiaries without any changes to auxiliary benefits of dependents and survivors whose benefits would continue to be based on the worker's primary insurance amount as under current law. Thus, considerations of medical coverage and auxiliary benefits need not be sources of work disincentives under GBO's benefit structure. Indeed, as noted earlier, GBO could offer opportunities for nongovernment entities to build support programs to assist beneficiaries to leverage GBO to maximum advantage by returning to work.

“The general benefit offset’s alternative benefit structure is consistent with maintaining current rules for medical coverage.”

NOTES

The author thanks Erin Partin and Nathan Pritchard for excellent research assistance and Jackie Chapin, Gabrielle D'Adamo Singer, Claire Green, Jeffrey Miron, Amy Shuart, Peter Van Doren, and others for very helpful comments. Any and all errors are attributable to the author.

1. The 2014 annual report of the Social Security Trustees places SSDI's 75-year noninterest revenues at 1.85 percent of total 75-year payrolls, whereas program benefit expenditures are projected to be 2.18 percent of 75-year payrolls. "The 2014 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds," May 31, 2013, Table IV.B4, <http://www.ssa.gov/OACT/TR/2013/tr2013.pdf>.
2. See *ibid.*, Table IV.A2.
3. Monthly benefits averaged \$1,204 for disabled workers, \$466 for dependent spouses, and \$314 for dependent children. See *Social Security Bulletin, Annual Statistical Supplement*, 2013, Table 6.A3, <http://www.ssa.gov/policy/docs/statcomps/supplement/2013/6a.pdf>. SSDI's financial projections (see note 1) show a 75-year resource shortfall averaging 15.1 percent of current-law benefits.
4. The OASI Trust Fund is projected to remain solvent through the early 2030s. The Social Security Amendments of 1981 facilitated limited interfund borrowing among (a) Social Security's Old-Age and Survivors Insurance, (b) Disability Insurance, and (c) Health Insurance (Medicare) Trust Funds. Despite those amendments, however, a reallocation of tax revenues from OASI to Disability Insurance may be resisted by retiree political lobby groups in order to prevent the OASI Trust Fund exhaustion date from being moved closer to the present.
5. For examples of SSDI reform proposals by other analysts, see Richard V. Burkhauser and Mary C. Daly, *The Declining Work and Welfare of People with Disabilities: What Went Wrong and a Strategy for Change* (Washington: AEI Press, 2011); David H. Autor and Mark Duggan, "Supporting Work: A Proposal for Modernizing the U.S. Disability Insurance System," Center for American Progress and Brookings Institution, December 2010; and David Mann and David Stapleton, "A Roadmap to a 21st-Century Disability Policy," Issue Brief no. 12-01, Center for Studying Disability Policy, Mathematica Policy Research, January 2012. The "generalized benefit offset" (GBO) reform was proposed in Jagadeesh Gokhale, "A New Approach to SSDI Reform," *Regulation* 36, no. 3 (Fall 2013): 44-51.
6. For example, see "How Some Legal, Medical, and Judicial Professionals Abused Social Security Disability Programs for the Country's Most Vulnerable: A Case Study of the Conn Law Firm," report requested by Sen. Tom Coburn (R-OK) and released by the U.S. Senate Committee on Homeland Security and Government Affairs, October 2013. Also see Jeffrey B. Liebman and Jack A. Smalligan, "Proposal 4: An Evidence-Based Path to Disability Insurance Reform," Hamilton Project, Brookings Institution, February 2013, page 1, available at http://www.brookings.edu/media/research/files/papers/2013/02/thp%20budget%20papers/thp_15waysfedbudget_prop4.pdf. Liebman and Smalligan opine that "while a consensus is emerging that changes are needed to the U.S. disability insurance system, there is no agreement around any specific reforms, nor does there appear to be a path in place that will lead to such agreement."
7. See Jeffrey S. Wolfe and David W. Engle, "Restoring Social Security Disability's Purpose," *Regulation* 36, no. 1 (Spring 2013): 46-54.
8. One example is Autor and Duggan, "Supporting Work." The authors recommend a private disability insurance system (purchased by employers from private insurance companies) to fund the provision of disability supports to workers remaining on the job but facing declining work ability from health impairments. That system would include a two-year delay in applying for SSDI benefits. Another is Liebman and Smalligan, "Proposal 4."

9. That view is suggested by Burkhauser and Daly in *The Declining Work and Welfare of People with Disabilities: What Went Wrong and a Strategy for Change* (Washington: AEI Press, 2011).

10. The term “induced entry” refers to the phenomenon whereby public benefit provisions or benefit enhancements induce people to behave in ways that make benefit receipt more likely. Thus, provision of early-intervention disability supports and services may induce workers to adopt lifestyles and behaviors to make qualifying for those benefits more likely.

11. Exceptions are the Ticket to Work program, the Benefit Offset Pilot, and national demonstration projects that SSA is currently operating.

12. See “The Social Security Definition of Disability,” Social Security Advisory Board, October 2003, p. 20.

13. The vertical shaded areas in Figure 2 indicate recession periods. Application rates from those insured under SSDI also surge during recessions. When measuring “core” SSDI incidence rates, standard practice is to filter out the effect of population aging, increases in women’s labor force participation after the 1970s, and the state of the economy—normal times versus recessions when job availability is low. Among those factors, removing the effects of changes in the state of the economy is inappropriate, because SSDI’s vocational eligibility rules are designed specifically to provide benefits if applicants are unable to find jobs in their occupations.

14. The increase in applications during recessions could be the result of state and county program requirements that make *applying* for SSDI (and Social Security’s Title XVI Supplemental Security Income program) a prerequisite for receiving state or county assistance. The fact remains, however, that SSDI enrollments spike during periods of high unemployment because of SSDI’s vocational eligibility criteria, no matter the reason for the initial application. Once enrolled, such work-capable individuals become trapped in no or low

labor force participation.

15. Recent evidence suggests that an increasing number of SSDI claims are represented by either attorneys or nonattorney representatives from nonprofit organizations or claimants’ relatives. The evidence also suggests that represented claims have a higher allowance rate than nonrepresented claims. See “What Impact Does Professional Representation Have at the Initial Application Level?” Report of the Social Security Advisory Board, September 2012.

16. According to one widely cited study (that uses different data sources from the ones used to construct Figures 2 and 3 in the text), only up to one-fifth of the increase in SSDI enrollment is explained by changes in the age and gender composition of the U.S. population. See Mark Duggan and Scott Imberman, “Why Are the Disability Rolls Skyrocketing?” in *Health at Older Ages: The Causes and Consequences of Declining Disability among the Elderly*, ed. David Wise and David Cutler (Cambridge, MA: National Bureau of Economic Research, 2009), pp. 337–79.

17. The figures cited are based on the author’s calculations using information provided by the U.S. Bureau of Labor Statistics.

18. See “The Social Security Definition of Disability,” p. 7.

19. For example, SSA’s guidance on SSDI’s disability determination process states: “SSA’s regulations provide for disability evaluation under a procedure known as the ‘sequential evaluation process.’ For adults, this process requires sequential review of the claimant’s current work activity, the severity of his or her impairment(s), a determination of whether his or her impairment(s) meets or medically equals a listing (see Part III of this guide), the claimant’s residual functional capacity, his or her past work, *and bis or her age, education, and work experience*” (emphasis added). See “Disability Evaluation under Social Security,” Social Security website, <http://www.socialsecurity.gov/disability/professionals/bluebook/general-info.htm>. These

rules are favorable to those approaching ages 50–54 if they are limited to sedentary activity and do not have skills transferable to other jobs. The rules are most favorable to those low-skilled workers who are 55 and older who are limited to light work or intermittent medium work even if they have a high school education.

20. Those projections are based on the Social Security Trustees' 2008–14 intermediate demographic and economic assumptions used for projecting Social Security's finances (including for the SSDI program).

21. The Social Security Trustees follow a standard methodology in making the program's future demographic and financial outcomes. For example, to obtain next year's projection of the DI prevalence rate, the insured and beneficiary populations are aged by one year; those who become newly insured by acquiring an adequate work history are added to the insured population; those who leave the insured and beneficiary pools either through death or by achieving the normal retirement age (to be shifted to the OASI insured population) are subtracted from their respective groups; and finally, the existing DI beneficiary population is updated by applying age- and gender-specific probabilities of acquiring a disabling health condition to the updated insured population. That method provides next year's DI incidence rate, and next year's projected new DI beneficiaries are added to next year's beneficiary population update as described above. Those calculations are performed after making second-order changes to underlying demographic, morbidity, labor force participation, and other parameters, taking into account the most recent information that is available.

22. National Health Information Survey questions solicited information about assistive devices, such as hearing aids, mobility assistive equipment, canes or walking sticks, walkers, Zimmer frames, crutches, wheelchairs or scooters, prosthetic devices, other equipment, and sign language.

23. The report states: "SSA officials maintain that other modern concepts of disability cannot be

fully incorporated into SSA's disability decisions. Specifically, SSA faces constraints considering the extent to which assistive devices and workplace accommodations can mitigate work disability, because these are not universally available and SSA lacks the resources to conduct individualized assessments." See "Modernizing SSA Disability Programs: Progress Made, but Key Efforts Warrant More Management Focus," GAO Report 12-420, Government Accountability Office, June 2012, <http://gao.gov/assets/600/591701.pdf>.

24. See "Disability Rights Movement Timeline," U.S. Department of Transportation, http://www.fta.dot.gov/12325_4064.html.

25. Historical data show that the award rate out of applications peaked in 1975 at 46 percent, declining subsequently to 33 percent by 1980. However, the earlier high allowance rate may have spurred the belief that many among disability beneficiaries did not deserve to be on the rolls. In a September 1981 speech, President Ronald Reagan affirmed, "No one will deny our obligation to those with legitimate claims, but there's widespread abuse of the system, which should not be allowed to continue." See SSA's website on presidential statements, <http://www.ssa.gov/history/reaganstmts.html#09241981>.

26. See the section on "State, Judicial, and Congressional Reactions to Accelerated Continuing Disability Reviews" in John R. Kearney, "Social Security and the 'D' in OASDI: The History of a Federal Program Insuring Earners against Disability," *Social Security Bulletin*, vol. 66, no. 3, 2005–6, <http://www.ssa.gov/policy/docs/ssb/v66n3/v66n3p1.html>.

27. For example, *US Airways vs. Barnet* (2002) clarified that the right of a worker with a disabling impairment who seeks a particular position as a "reasonable accommodation" may, under special circumstances, take precedence over other workers' rights to apply for that position under the employer's current seniority system. *Cleveland vs. Policy Management Systems Corporation* (1999) identified five rationales for SSDI claimants (implying

total disability) to pursue ADA claims against an employer. Other court cases expanded the range of services for individuals with disabilities along many dimensions, including the criminal justice system's provision of effective accommodations and communication to disabled individuals during arrest and detention to compatibility of state laws with the ADA, the provision of service animals to disabled students in school, and so on.

28. See Channa Joffe-Walt, "Unfit for Work: The Startling Rise in Disability in America," National Public Radio, March 28, 2013, <http://apps.npr.org/unfit-for-work/>. Note: representatives of successful SSDI applicants are allowed to deduct a percentage of initial benefits—up to \$5,300 per claimant—as a service fee. Some observers, including some sitting ALJs, have noted that the average allowance rate of ALJ hearings, which exceeds 50 percent, results in poor incentives for attorneys and nonattorney representatives to perform their tasks properly. Instead, many representatives operate in the manner of a fast-food restaurant: conducting a high-volume business without conscientiously developing complete records for their clients and, instead, simply depending on the favorable ALJ allowance rate to collect fees amounting to thousands of dollars each month for simply "holding their clients' hands" and accompanying them to ALJ hearing sites.

29. See "What Impact Does Professional Representation Have on the Process at the Initial Application Level," Social Security Advisory Board, September 2012. The report suggests that represented cases take longer to adjudicate and result in slightly higher benefit allowance rates.

30. Recently, Rep. Sam Johnson (R-TX), chair of the Social Security Subcommittee of the House Committee on Ways and Means, introduced the Insurance and Unemployment Benefits Double Dip Elimination Act of 2013. That act would end the ability to double-dip by receiving Social Security disability benefits and unemployment benefits simultaneously.

31. See letter to E. Clay Shaw Jr., chair of the Sub-

committee on Social Security of the House Committee on Ways and Means, Hearing on Management of the Social Security Administration Office of Hearings and Appeals, September 30, 2003. Supporting reference is to 20 CFR §§404.1527(d)(2), 416.927(d)(2).

32. For more detailed information on policy compliance issues at the ALJ level, see "Systemic Waste and Abuse at the Social Security Administration: How Rubber-Stamping Disability Judges Cost Hundreds of Billions of Taxpayer Dollars," staff report, U.S. House of Representatives, 113th Cong., 1st sess., June 10, 2014.

33. It is noteworthy that about one-half of ALJ (and SSA Appeals Council) denials that are further appealed to federal courts are affirmed. That means, despite multiple reviews by SSDI case officials and ALJs, one-half of appealed denials are remanded, reversed, or dismissed.

34. That is, the black bars showing the distribution for 2013 are generally taller on the left-hand side and shorter on the right-hand side compared with those for earlier years.

35. The standard deviation of the distributions declined from 15.9 percentage points in 2010 to 14.9 percentage points by 2013.

36. SSA has 10 regions across the United States, with the National Hearing Centers in Albuquerque, New Mexico, Falls Church, Virginia, Chicago, Illinois, and St. Louis, Kansas, being designated as the 11th region in Table 1. The data underlying Table 1's calculations are from SSA's ALJ Disability Case Dispositions, http://www.ssa.gov/appeals/DataSets/03_ALJ_Disposition_Data.html.

37. Across all SSA districts, the cross-year ALJ allowance-rate correlations were 89.7 for 2010–11, 88.6 for 2011–12 and 89.9 for 2012–13.

38. Conversations with ALJs and visits to state Offices of Disability Adjudication and Review suggest that applications are distributed among

ALJs on a rotational (“first come, first served”) basis. Indeed, several ALJs confirmed that they are not allowed to influence the case distribution function, which is controlled only by technicians at Office of Disability Adjudication and Review locations.

39. According to Chief ALJ Debra Bice, “Generally, this process works. The vast majority of issues are resolved informally by hearing office management. When they are not, management has the authority to order an ALJ to take a certain action or explain his or her actions. ALJs rarely fail to comply with these orders. In those rare cases where the ALJ does not comply, we pursue disciplinary action.” See her testimony before the Permanent Subcommittee on Investigations of the Senate Committee on Homeland Security and Governmental Affairs, 112th Cong., 2nd sess., September 13, 2012, <http://www.hsgac.senate.gov/subcommittees/investigations/hearings/social-security-administrations-disability-programs>.

40. See David Stapleton, Arif Mamun, and Jeremy Page, “Initial Impacts of the Ticket to Work Program for Young New Social Security Disability Awardees: Estimates Based on Randomly Assigned Mail Months,” final report, Mathematica Policy Research, July 30, 2013, <http://socialsecurity.gov/disabilityresearch/documents/Ticket%20Impact%20Report.pdf>.

41. For additional detail and analysis of the Benefit Offset Pilot Demonstration and the Benefit Offset National Demonstration projects, see Jagadeesh Gokhale, “A New Approach to SSDI Reform.”

42. See “Does Disability Insurance Receipt Discourage Work? Using Examiner Assignment to Estimate Causal Effects of SSDI Receipt” by Nicole Maestas, Kathleen J. Mullen, and Alexander Strand, *American Economic Review* 103, no. 5 (2013): p. 1797–1829. Their study finds that “among the estimated 23 percent of applicants on the margin of program entry, employment would have been 28 percentage points higher had they not received benefits. The effect is heterogeneous, ranging

from no effect for those with more severe impairments to 50 percentage points for entrants with relatively less severe impairments.”

43. See Eric French and Jae Song, “The Effect of Disability Insurance Receipt on Labor Supply: A Dynamic Analysis,” Federal Reserve Bank of Chicago, Working Paper no. 2012-12, 2012. This paper predicts the labor supply response to benefit denial when there is no option to appeal. It finds that if there were no option to appeal the benefit-denial decision, denied applicants would be 35 percentage points more likely to work.

44. See Gina Livermore, “Social Security Disability Beneficiaries with Work-Related Goals and Expectations,” *Social Security Bulletin*, vol. 71, no. 3, 2011.

45. Between 1980 and 2010, increases in age- and sex-specific disability prevalence rates account for 42 percent of the nearly doubled disability prevalence. That could have occurred because more individuals within each age and sex group are disabled today, or because those with increasingly less severe medical impairments are being allowed into the program. However, micro-data survey evidence suggests that workers’ health status has not worsened and incidence of work-disabling impairments by age and sex has not increased since 1980. See “The Financing Challenges Facing the Social Security Disability Insurance Program,” Stephen C. Goss, chief actuary, SSA, Testimony before the Subcommittee on Social Security of the House Committee on Ways and Means, 113th Cong., 1st sess., March 14, 2013, http://www.ssa.gov/oact/testimony/HouseWM_20130314.pdf.

46. See Jagadeesh Gokhale, “A New Approach to SSDI Reform.”

47. Under SSDI, working and earning is allowed without loss of benefits for nine TWP months. TWP months need not be continuous but must occur within the past 60 months. A TWP month accrues if earnings exceed a particular threshold that varies each year. It is \$770 per month dur-

ing 2014. Once nine TWP months have accrued within the 60-month look-back period, the beneficiary is placed on “probation”: SSDI benefits are eliminated, and the worker’s income drops steeply to equal earnings. That “probationary” period is called the “extended trial work period” (ETWP). During the ETWP, benefits are automatically reinstated if earnings decline below SGA. However, once the 36-month ETWP has elapsed, benefits are permanently eliminated. The ex-SSDI beneficiary retains the option of continuing Medicare coverage by paying discounted premiums.

48. However, at low earnings, the dollar amount of the tax does not exceed the trust fund benefit amount, and no “out-of-pocket” tax payment is required from beneficiaries.

49. GBO legislation should include the proviso that benefit enhancement at zero earnings should become effective only after the beneficiary begins working and should be removed if there is no work activity during the past four quarters. That feature will prevent beneficiaries from working for just a few quarters to enroll into GBO and permanently obtain a benefit enhancement.

50. Under GBO, benefits would be ceased only under evidence of medical improvement discovered through a CDR.

51. Even if alternative 2 is realized, it would provide information about the status of SSDI beneficiaries, who would reveal by their labor market choice of zero additional work effort that they are already working to the maximum of their abilities. Introducing GBO into the law would be worthwhile regardless of the size of the behavioral response. It would reveal better information about beneficiaries’ work potential, no matter whether beneficiaries increase their labor force participation by a little or a lot.

52. Estimating GBO’s likely cost by comparing it with the Earned Income Tax Credit program under the federal income tax seems inappropriate, as discussed in Appendix C.

53. To be consistent with what follows, the medical improvement should be judged relative to the medical criteria that were in place at the time of acquiring eligibility for SSDI.

54. Currently, SSA uses the 1991 edition of the *Dictionary of Occupational Titles* to guide decisions based on vocational criteria.

55. Proposals to accomplish early disability interventions include, among others, (a) providing employers with better incentives to retain disabled workers, (b) providing tax credits for employer provision of work supports and accommodations, (c) adopting universal insurance programs for providing assistive equipment at the workplace, (d) revising occupational placements or tailoring job requirements to suit disabled workers, and (e) providing better access to specific health care and rehabilitative services under employer-sponsored disability “case management” services.

56. For example, see Jeffrey B. Liebman and Jack A. Smalligan, “Proposal 4,” page 2. The authors propose to “screen disability applicants and target those who appear likely to be determined eligible for benefits but who also have the potential for significant work activity if provided with a proper range of services.”

57. See “Employer Accommodation and Labor Supply of Disabled Workers” by Matthew Hill, Nicole Maestas, and Kathleen J. Mullen, RAND Working Paper Series WR-1047, March, 2014.

58. Post-entitlement SSDI reforms fail to receive sufficient support because of the possibility that induced entry into SSDI would make them too costly. However, the pre-entitlement early-intervention programs being proposed are also susceptible to the same possibility. Those reforms would actively seek out high-risk workers—those most likely to become disabled and eventually to apply for SSDI benefits—and preemptively provide them with disability supports in the hope of preventing or delaying applications to SSDI. But such reforms could also induce behaviors that signal a need for pre-entitlement supports.

That is, induced entry is likely to be a problem for both pre- and post-entitlement SSDI reforms. The GBO's post-entitlement reform, however, includes a countervailing incentive to delay application to SSDI: waiting to apply for SSDI while acquiring a longer work history and a higher PIA would qualify the applicant for a more attractive GBO schedule. Any induced entrants into SSDI as a result of adopting GBO would thus be "naturally screened" and would provide appropriate targets for early-intervention initiatives.

59. The requirements for acquiring insured status under SSDI are provided in the Social Security Code of Federal Regulations, http://www.ssa.gov/OP_Home/cfr20/404/404-0130.htm. The computation of average monthly indexed earnings is described at http://www.ssa.gov/OP_Home/cfr20/404/404-0211.htm. The procedure for computing the primary insurance amount is available at http://www.ssa.gov/OP_Home/cfr20/404/404-0222.htm.

60. Earnings in column (1) of Table A.1 are shown at the midpoint of each earnings step.

61. The monthly earnings level of \$1,583 is a break-even point for government net cost under the GBO schedule shown in Table A.1 that is used as the basis for Figures B.1 and B.2. Earnings higher than that amount would result in a positive net cost for the government as the subsidy's

cost begins to exceed saving from lower trust fund benefits. As earnings become still higher, however, the wage subsidy is gradually withdrawn, and a second break-even point is reached when the beneficiary's monthly earnings are \$2,307. For earnings beyond that level, the government would have negative net costs as both trust fund benefits and the wage subsidy are reduced.

62. A Windows application for exploring the net benefit and income implications alternative SSDI beneficiary earnings patterns, including temporary and permanent unemployment, rising and declining earnings, alternative GBO calibrations, and so on is available from the author upon request.

63. Relieving the constraint against earning at more than the SGA level would also expose SSDI beneficiaries to labor market risks of reduced earnings and job losses. Beneficiaries whose earnings were substantial before job loss may be exposed to GBO adjustments to benefits just when earnings decline. In general, those adjustments will be larger for people with large pre-job-loss earnings. Hence, some beneficiaries would need assistance in developing savings plans to counter the risks of job separations and earnings declines. Such programs could be built around GBO by state and local nonprofit organizations and other social services organizations that cater to the needs of individuals with disabilities.