



# The employment effects of terminating disability benefits<sup>☆</sup>

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## ABSTRACT

Few social security disability insurance (DI) beneficiaries return to the labor force, making it hard to assess their likely employment in the absence of benefits. Using administrative data, I examine the employment of individuals who lost DI eligibility after the 1996 removal of drug and alcohol addictions as qualifying conditions. Approximately 22% started working at levels that would have disqualified them for DI, an employment response that is large relative to their work histories. Those who received DI for 2–3 years had the largest response, suggesting that a period of public assistance may maximize the employment of some disabled individuals.

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## 1. Introduction

Governments in many industrialized countries are trying to reduce the size of their disability insurance programs and increase the employment of disabled individuals. In the United States, where four percent of 18 to 64 year olds receive social security disability insurance (DI) and a further two percent receive federal disability benefits through the supplemental security income (SSI) program, recent efforts include providing beneficiaries with work

incentives and employment support services through the “Ticket to Work” program and mandating funds for medical reassessments of current beneficiaries (Social Security Administration (SSA), 2013a). In the United Kingdom, where the fraction of the working-age population receiving disability benefits is similar to the US, reforms have resulted in reduced benefits, vocational support, and time limits for beneficiaries judged capable of working (Berthoud, 2011). Many other European countries have also recently introduced policies to reduce the number of disability beneficiaries.<sup>1</sup>

A growing literature has estimated how many individuals would work if they were not eligible for disability insurance. Starting with Bound (1989), most of these studies have used the employment of denied applicants to estimate the likely employment of accepted applicants (e.g., Chen and van der Klaauw, 2008; von Wachter et al., 2011; Maestas et al., 2013; French and Song, 2014). The relationship between disability benefits and labor force participation has also been estimated using variation in benefit generosity in the United States (Autor and Duggan, 2003) and Canada (Gruber, 2000), differences in disability insurance rejection rates in the United States (Gruber and Kubik, 1997), and changes in disability eligibility criteria in Austria (Staubli, 2011). All of these studies focus on employment before or at the time of

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<sup>1</sup> Other recent reforms include tightening eligibility criteria in Sweden (Karlström et al., 2008); removing restrictions on work activity in Norway (Kostøl and Mogstad, 2014); and comprehensive reforms in the Netherlands that included stricter eligibility criteria and widespread reassessments of younger beneficiaries (Borghans et al., 2014).

application, and as a result they provide good estimates of how employment might change as a result of limiting entry into these disability programs.

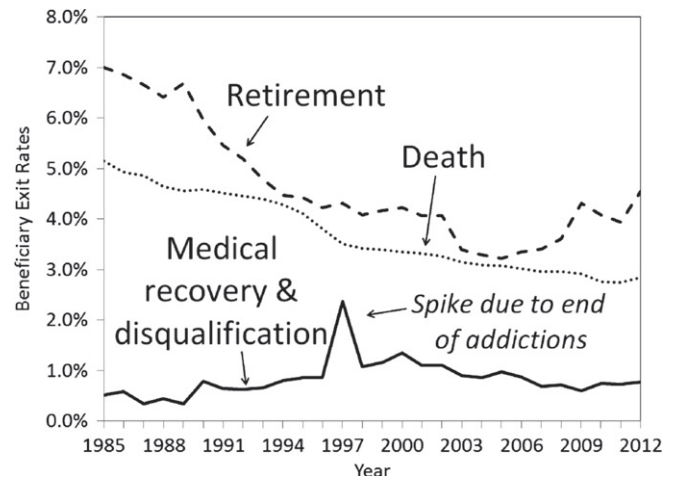
Studies examining policies that affect labor force participation during or after the receipt of disability insurance are far less common. There is recent evidence that beneficiaries do respond to work incentives, such as increasing their labor supply after the reduction of earnings penalties in Norway (Kostøl and Mogstad, 2014), the introduction of higher earning limits in Canada (Campolieti and Riddell, 2012) and decreases in benefit payments in the Netherlands (Borghans et al., 2014). However, research on the employment of individuals after exiting disability insurance is largely limited to documenting the number and characteristics of those who exit (e.g., Hennessey, 1996; Schimmel and Stapleton, 2011).

In this paper, I partly address that gap by examining the employment effects resulting from a reform in the United States that resulted in a large number of individuals losing their eligibility for DI. In March 1996, the congress removed alcohol and drug addictions as eligible conditions, including for those who did not have it as their primary disability. At the time, approximately two percent of DI beneficiaries had an alcohol or drug addiction that had contributed to their eligibility. Affected individuals could apply for continued eligibility on the basis of their other disabilities, and approximately 90% did so. Around half were judged to be re-eligible for DI, and continued to receive benefits. The remaining 65,000 individuals had their DI cash payments and benefits terminated in January 1997 (Stapleton et al., 1998).<sup>2</sup>

This is the only large-scale termination of DI eligibility since major reforms to the program in 1984. Fig. 1 shows the annual DI exit rates between 1985 and 2012. Approximately one percent of beneficiaries exit annually due to no longer being disabled. The sole exception is in 1997, when the rate more than doubled due to the terminations examined here. Fig. 1 also shows that the rate at which beneficiaries return to labor force has remained relatively constant, even as exit rates due to death or reaching normal retirement age have been declining, as beneficiaries have become younger and more likely to have low-mortality conditions (Autor and Duggan, 2003).

Using SSA administrative data that cover most of the DI beneficiaries affected by the policy change, I first show that there was a large employment response after the removal of disability benefits. This is estimated using difference-in-differences models with affected beneficiaries who remained on DI as the comparison group, as they have similar pre-treatment employment histories to terminated beneficiaries. Employment is primarily measured in terms of having wage income above the 1996 “substantial gainful activity” (SGA) threshold (\$8602 per annum in 2013 dollars),<sup>3</sup> which is the level at which capacity for work is assessed. I find the fraction of terminated DI beneficiaries with annual earnings above this threshold increased by 22 percentage points following the termination of disability benefits, which is large relative to these individuals’ work histories. It is also far higher than the base SGA employment of the control group, which is typically one percent per annum. The employment effects decline after four years, primarily because some individuals regain eligibility for disability benefits. Varying the earnings thresholds at which employment is assessed suggests that terminated beneficiaries who started working generally earned more than annualized SGA levels, although not much more.

There is considerable heterogeneity in the employment response. There are large and statistically significant differences related to an



Source: Annual Statistical Supplement to the Social Security Bulletin [various years].

Fig. 1. Social Security disability insurance termination rates by reason, 1985–2012.

individual's age at termination, with the employment effects among 30–39 year olds of 25 percentage points being much higher than the estimate of 16 percentage points for 50–61 year olds. Terminated beneficiaries also had a higher employment response if they had higher wage earnings prior to getting onto DI or if they applied for DI when the unemployment rate was lower. There are not large differences by type of addiction, and the employment effects are similar for individuals whose primary disability had been an addiction, a mental disorder, or a musculoskeletal condition.

Individuals had received DI for different lengths of time prior to the terminations. After showing that cohorts of beneficiaries had similar employment and health characteristics prior to receiving DI, I examine how the employment effects vary as a function of time receiving disability benefits. I find that there is an inverted-U shaped relationship between the size of the employment effects and time spent on DI. The employment response is highest among those who received benefits for approximately 2.7 years prior to termination, and is 50% larger than the employment response of individuals who received benefits for nine months (the shortest period of receipt for anyone in the sample) and 31% higher than those who received benefits for six years. This inverted-U relationship is strongest among younger individuals.

It is surprising that the employment effects do not monotonically decline with time on DI, given the widespread evidence that healthy individuals become less able to work the longer they are out of the labor force (e.g., Mincer and Opek, 1982; Kroft, Lange and Notowidigdo, 2013). To better understand the role of initial health, I compare the employment effects for those immediately awarded DI to those awarded DI after successfully appealing an initial denial. Hu et al. (2001) and von Wachter et al. (2011) find that beneficiaries who were initially denied DI are healthier and more able to work than other beneficiaries. Among those who had spent less than 1.5 years on DI, the employment response for immediately-accepted beneficiaries is lower than for initially-denied beneficiaries, which is consistent with this prior evidence. However, the employment response for the immediately-awarded group increases sharply with time on DI, so much so that those who had received DI for between two and four years had a larger employment response than the initially-denied group. These results suggest that assessments of health and work capacity made at the time of application do not necessarily hold over time. They also indicate that health changes while on DI may have affected terminated beneficiaries’ ability to work, although it is not possible to quantify that effect. It is also not possible to attribute any changes to the cash and medical

<sup>2</sup> These changes also affected beneficiaries on the means-tested disability benefit program, supplemental security income (SSI). I focus on DI because they have much higher labor force participation than SSI recipients, and Campbell et al. (2003) and Chatterji and Meara (2010) have previously examined the employment of SSI recipients.

<sup>3</sup> All dollars are in 2013 values, unless otherwise noted. Conversions are based on the CPI-U.

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