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Sam Johnson
Chairman
Subcommittee on Social Security
Committee on Ways and Means

Dear Mr. Johnson:

Thank you again for inviting me to testify before the Committee on Ways and Means Subcommittee on Social Security on June 19, 2013. I am writing in response to your letter of July 17, 2013 that posed four questions to me. I have pasted and italicized those questions below and include my answers in the text that follows.

1. On page eight of your testimony, you contrast the Disability Insurance (DI) program with the welfare program. What can the Subcommittee learn from the reforms made to welfare? Is it possible for similar reforms to be implemented in the DI program to help beneficiaries return to work? What would those reforms look like?

During the 1990s, changes to the AFDC / TANF program substantially increased the incentive to work among current and potential future recipients of program benefits. Each state was given greater latitude to reform their programs and stronger financial incentives to reduce program enrollment through a change in the federal match. Recipients were also given much stronger incentives to work and limits were placed on the total duration of program enrollment. These changes at the time were very controversial – with many opponents predicting they would harm millions of the nation's most vulnerable citizens by reducing their transfer income while doing little to increase their earnings. The reforms to welfare programs coincided with an expansion in the federal earned income tax credit, which further increased the incentive to work among lower-income adults with children.

In the years following these reforms, there were significant reductions in program enrollment and similarly large increases in employment among the groups most affected by the reforms (single parents with children). While other factors including strong economic growth contributed to these changes, a large body of literature persuasively demonstrates that reforms to the AFDC / TANF programs played a central role (Blank, 2002). There was no simple one-size-fits-all reform that worked in all states for all recipients. But the combination of reducing the effective tax rate on working, limits on the duration of benefits, and related changes induced an unprecedented decline in program enrollment and a similarly large increase in labor force participation. These changes coincided with an improvement in the average economic well-being among the groups most affected by the reforms (Meyer and Sullivan, 2004).

The success of AFDC / TANF reforms at reducing program enrollment, increasing employment, and improving economic well-being stand in sharp contrast to the results from the limited efforts to do the same in the federal SSDI program. While the beneficiaries of the two programs differ in many ways and thus the effect of a specific reform may not be the same for the two groups, the results from AFDC / TANF show that simultaneously improving the financial incentive to work while reducing the incentive to remain enrolled can produce substantial changes in behavior that increase employment and improve economic well-being while reducing government expenditures and increasing tax revenues. Reforms to SSDI that incorporate these features and are tailored to the characteristics of program beneficiaries could improve the economic well-being of many individuals with disabilities while reducing program expenditures.

2. Some argue against time limiting benefits since beneficiaries are required to have a review of eligibility every few years, yet it was presented in your testimony as an option to improve the functioning of the DI program. How could time limiting benefits be beneficial? Would you recommend time limiting all benefit or focus on certain categories of impairments?

Each SSDI award decision is all-or-nothing – either the person is awarded benefits or not. However, there are many individuals who are close to the margin of qualifying for benefits, with for example more than 40 percent of SSDI awards now being made on appeal. While it is true that many of those awards made on appeal are to individuals who are unable to work, recent evidence strongly suggests that a large fraction of applicants close to the margin of qualifying can work (French and Song, 2013) and even that many awarded benefits at the initial stage can work as well (Maestas et al, 2013).

Given the low rate at which medical continuing disability reviews (CDRs) are performed (only about 1 percent of SSDI recipients received one each year from 2007-9) and some limitations with the CDR process, one possible reform would be to time-limit benefits for those receiving an SSDI award who are very close to the margin of qualifying. It would not be desirable to apply a time limit to all SSDI recipients, as many on the SSDI program are unambiguously unable to work and almost certainly will be for many years. Additionally, rather than applying this to certain diagnoses but not others, such a time limit could take account of the severity of the person’s condition and/or whether temporary labor market conditions played a role in the decision. Of course any such reform would have to be carefully crafted to protect those SSDI recipients who are unable to work while improving incentives for those who can or might be able to in the near future.

One potentially important benefit of such a change is that SSDI awardees who “just qualified” would have an incentive to further their skills and remain connected to the labor market while on SSDI so that they could make the transition back to work if possible given the evolving nature of their health.

3. You discussed in your testimony that Norway has tried programs similar to the Benefit Offset National Demonstration that replaces the “cash cliff” where workers lose all benefits if they earn just $1 above the substantial gainful activity cap ($1,040 per month this year), with a gradual benefit offset. Please discuss he results in Norway. Did the reforms encourage more people to apply for benefits?

Recent research has demonstrated that reforms in Norway that increased the incentive to work among beneficiaries of their disability insurance program led to a significant increase in labor force participation (Kostol and Mogstad, 2013). More specifically, by allowing disability insurance recipients to keep just 40 percent (as opposed to 0 percent) of any earnings beyond the substantial gainful activity threshold, the reform caused an 8.5 percentage point increase in labor force participation among program recipients between the ages of 18 and 49. The success of this reform suggests that similar changes to the SSDI program could increase return-to-work among existing recipients. While the authors are unable to estimate the effect on program applications, they persuasively argue that applications are unlikely to respond enough to offset much of the budgetary savings stemming from lower disability insurance expenditures and higher tax revenues.

4. In their recent paper, authors Jeffrey Liebeman and Jack Smalligan, found the DI program "is in significant need of reform" because a number of beneficiaries would be better off with a different from of assistance, the actors in the disability program have misaligned incentives, and the disability determination system remains a problem despite recent progress. They proposed several new ideas to test ways to improve the disability program's return to work efforts. These include screening applications and offering some individuals targeted services instead of cash benefits, creating incentives for employers to keep people at work, and allowing States to test alternate approaches. What is your opinion of these ideas to encourage people to stay at work, defer filing, and allow State to innovate to reduce program costs? Should Congress restore Social Security's demonstration authority to test these ideas?

While the Norway evidence suggests that improving incentives to work among existing recipients can have a large payoff, intervening sooner with individuals who may or will soon apply for the program could produce even larger returns (Autor and Duggan, 2010). Thus I agree with the authors' point that targeting services at certain potential applicants and changing employer incentives could stem the flow of individuals onto the SSDI program. The financial payoff to reducing this flow is substantial given that the present value of the average SSDI award is approximately $270,000.

There could also be significant gains from allowing states and the Social Security Administration to experiment – much like they did during the 1990s with AFDC and TANF - to reduce program enrollment and increase employment among current or potential future SSDI recipients. One concern, however, is that pilots could take a long time to roll out and be evaluated if they are not implemented efficiently. Thus an important consideration is the likely delay in the results from any such pilots. Given the fiscal issues facing the SSDI program, it is not clear that policymakers have the luxury to wait for a decade or more before implementing reforms that will get the program on a stronger financial footing. Furthermore, the limited success of pilot programs in the Medicare program suggests that experimentation does not always lead to substantial improvements in large-scale federal programs (CBO, 2012).

I sincerely hope that these comments are helpful to you and other members of the Subcommittee on Social Security. Thank you again for the opportunity to testify last month and please don't hesitate to contact me if I can ever be helpful to you and your colleagues on this important issue.

Sincerely,

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