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The Financial Vulnerability of Former Disability Beneficiaries in Retirement

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By their early 60s, one in four workers has experienced the onset of a work-limiting health condition (Johnson et al. 2007), and nearly four in five adults in this age group have experienced the onset of a chronic health condition (Smith 2003). Older workers who develop significant medical conditions or impairments face declines in earnings, income, and consumption and an increase in poverty (Schimmel and Stapleton 2012; Meyer and Mok 2014). In addition to these effects, leaving the labor force during peak earning years may have a lasting impact on financial security after retirement. In this brief, we consider the post-retirement financial well-being of workers based on whether they received Social Security Disability Insurance (DI). We compare their experiences to other workers who did not receive DI but claimed Old Age and Survivors' Insurance (OASI) program.

Background

Benefits administered by the Social Security Administration (SSA) are critical to many adults during retirement and may help mitigate some of the income losses associated with disability onset. Older workers who develop a disability may leave the labor force and seek benefits through the Old Age, Survivors, and Disability Insurance (OASDI) program, either through Social Security Disability Insurance (DI) or, if they are age 62 or older, through the Old Age and Survivors' Insurance (OASI) program. It is not uncommon for older adults to claim DI benefits; in 2014, 68 percent of all DI awards made were to workers aged 50 or older (SSA

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2015). SSA converts DI benefits to OASI when the DI beneficiary reaches the full OASI retirement age (FRA), which is age 66 for those claiming OASI in 2016; the benefit amount stays the same.

For those who do not receive DI benefits first, claiming OASI is another way to mitigate income losses after developing a new work-limiting health condition. Although monthly benefits are higher if people delay claiming OASI until FRA, workers may apply for benefits as early as age 62 (the earliest eligibility age). Claiming benefits early is quite common; nearly three in four OASI claimers begin to receive benefits before FRA (SSA 2015). Yet doing so comes with a reduction in monthly benefits for the remainder of one's life; workers who claimed OASI at age 62 in our study population had benefits that were 25 percent lower than similar workers who delayed claiming OASI until FRA. That percentage has been increasing and is scheduled to increase in the future, as the FRA increases.[1]

We compare the financial well-being after FRA of people who were DI beneficiaries to that of people who claimed OASI without receiving DI benefits. We consider those who claimed OASI before FRA (between ages 62 and 66) and those who claimed OASI at or after FRA. We also consider the experiences of two DI beneficiary groups, based on when they first received DI—before or after age 59.[2] The latter group may be more similar to early OASI claimers than the former because they did not experience a disability during most of their working years. We find that, compared to OASI recipients, DI beneficiaries are more likely to be financially vulnerable before FRA and into retirement.

The information in this brief is based on a longer manuscript by Wu et al. (2016). To conduct our analysis, we used data from the Health and Retirement Study (HRS) linked to SSA administrative data. Using the linked administrative data, we were able to identify benefit receipt status and payment amounts without the measurement error that is common in self-reported survey data. The results reported here control for differences across DI and OASI claimers that might affect the measurement of their financial well-being, while not accounting for characteristics that are correlated with the likelihood of DI or OASI benefit receipt. They pertain to people who turned age 62 between 1994 and 2008.

What are the Characteristics of DI Beneficiaries and OASI Claimers Before FRA?

Among the 4,076 people that were the subject of our analysis, 14 percent received DI benefits before FRA; of these, two-thirds were receiving benefits by age 59 and the rest received benefits later. Of the 86 percent of those who did not receive DI before claiming OASI, 80 percent claimed OASI before FRA, and 20 percent claimed it at or after FRA. These numbers are generally consistent with published statistics about the distribution of beneficiaries (SSA 2015).

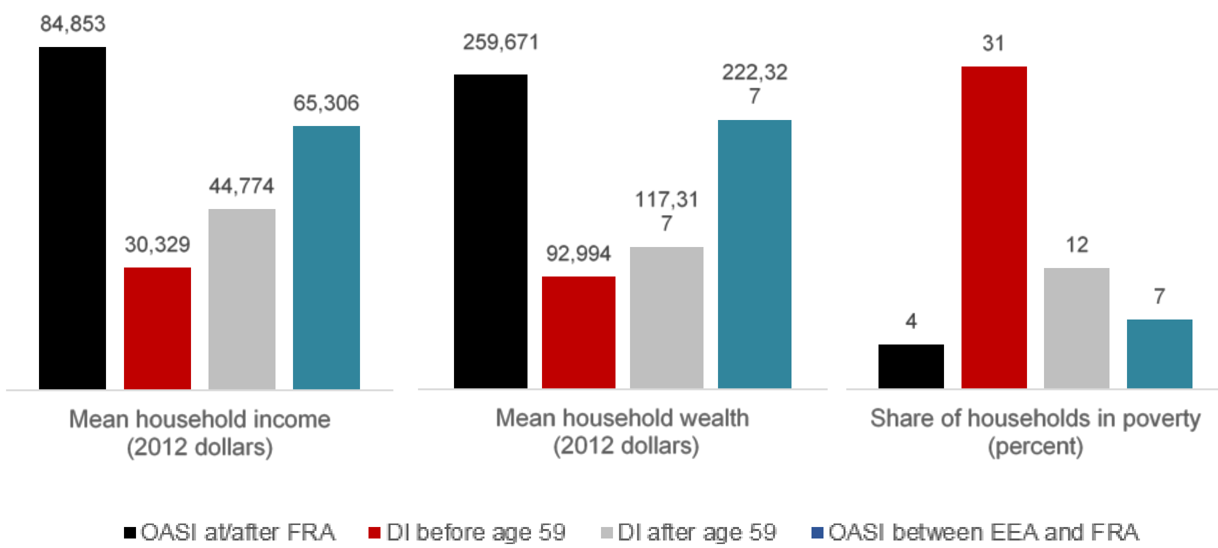
[1] If workers apply for OASI before FRA, SSA asks whether they have any work-limiting conditions that could make them eligible for DI. If so, they are considered for DI while receiving OASI, and their benefits are retroactively adjusted if they subsequently receive DI benefits.

[2] We selected this age because it is before the earliest eligibility age for OASI, and to ensure that all age-eligible members of our sample had at least one HRS interview. The HRS interviews occur every two years, so age 59 is a simplication of the true age of respondents at this point, which ranges from 58 to 60.

Compared to OASI claimers, DI beneficiaries are more likely to be members of minorities, are less educated, and are less likely to be married or veterans. Those who claim OASI before FRA are more likely to be white, female, and married, and less likely to be college graduates or veterans than later OASI claimers.

Compared to OASI claimers, at about age 59 DI beneficiaries have significantly lower household income and wealth, and a significantly higher likelihood of being in poverty (Figure 1). This is true both for those who receive DI before age 59 and those who receive DI after that age but before FRA. Members of the latter group might have been waiting for a disability determination at the time of their age-59 interview, their health and functioning might have already been interfering with their work, or they might have been working in lower-wage jobs than OASI claimers. The financial well-being of DI beneficiaries is also likely to be affected by medical and other expenses related to their impairment that healthier workers may not face. After a two-year waiting period, DI beneficiaries begin to receive Medicare, which may mitigate their financial vulnerability.

Figure 1. Financial well-being at age 59, DI beneficiaries and OASI claimers



Source:Wu et al. (2016).

Notes: We measured financial well-being around the time respondents were age 59. Household income and wealth are per-capita measures, adjusted for whether the HRS household was composed only of the respondent or also included the spouse; see Wu et al. (2016) for details. Each mean for the OASI at/after FRA group is significantly higher for the corresponding mean for every other group.

How Does Financial Well-Being Evolve After FRA?

At FRA and again two and four years later, DI beneficiaries and early OASI claimers had substantially lower income and wealth than those who claimed OASI at or after FRA (not shown). The sheer magnitude of this difference is notable; two years after FRA, the incomes of DI beneficiaries were about half as large as incomes of those who claimed OASI at or after FRA (Figure 2). The difference in per-person wealth at that time was even larger than at age 59 (not shown); \$116,628 among those who received DI before age 59 compared with \$404,001 among those who claimed OASI at or after FRA. Early OASI claimers had incomes that were significantly better than those of DI beneficiaries, though worse than for those who delayed claiming OASI; their per-capita wealth was also in between that of the other two groups ($282,725). Relative differences across the groups are fairly constant over time; the gaps do not change appreciably with age.

Although the relative financial position of the groups remained roughly constant after FRA, there is an important difference between the groups during this period. Around FRA, those claiming OASI for the first time are making a planned decision to leave the labor force. As a result, they experience lower incomes and higher poverty (during this time, incomes declined for all of the subgroups we considered). But OASI claimers who waited until at least FRA to claim benefits likely expected and planned for these changes. For later OASI claimers, falling incomes and an increased likelihood of poverty in the years after FRA mask the financial stability offered by substantially higher levels of wealth held by households claiming OASI at or after the FRA. Two years after FRA, the per-capita wealth of later OASI claimers is nearly four times as large as that of early DI beneficiaries (not shown). In addition to the ability to draw upon financial wealth to offset any income declines, households in this group are more likely to own their home than other groups, so they also have more implicit income in the form of the rental value of their home.

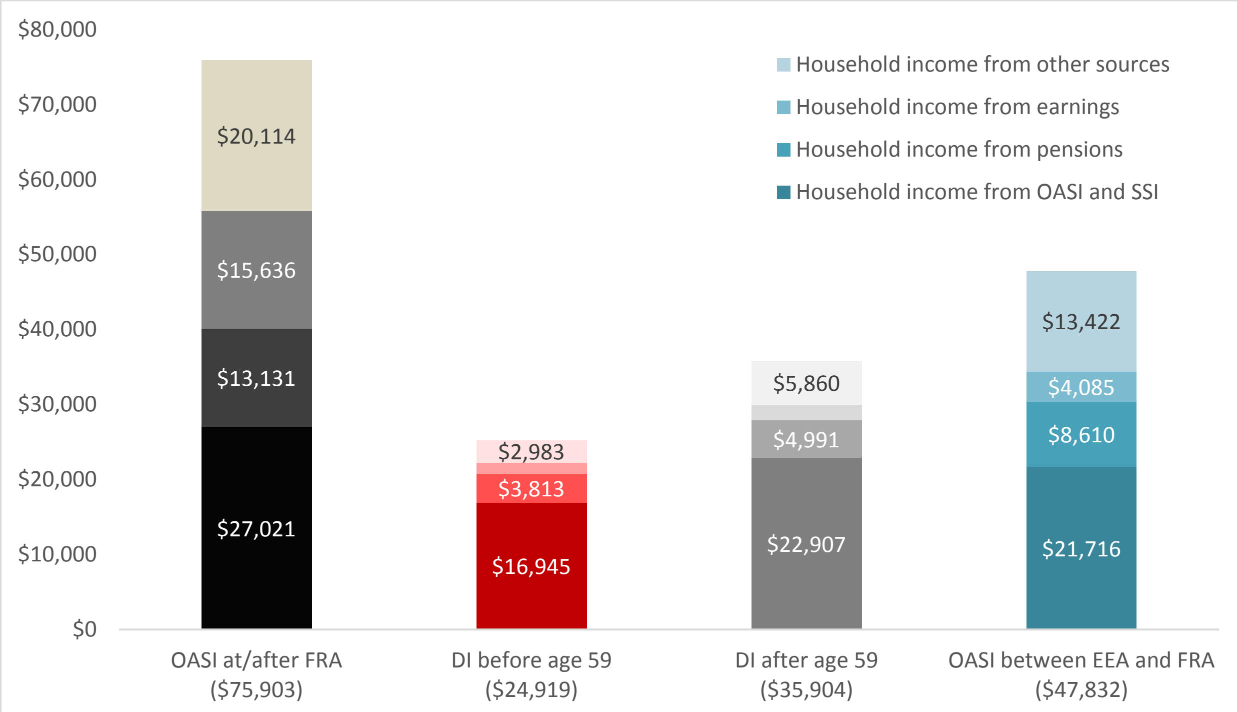
How Important Are OASI benefits For Financial Well-Being After FRA?

Those who claimed OASI at or after FRA had an average monthly benefit amount 33 percent higher than early DI beneficiaries, 16 percent higher than later DI beneficiaries, and 32 percent higher than earlier OASI claimers (not shown). These differences reflect differences in average earnings during their working years, the additional years in which FRA claimers work and accumulate higher earnings, and the SSA benefit calculation formula.

Monthly OASI benefit amounts are lower for DI beneficiaries than for those who delay claiming OASI until FRA, yet those benefits are a substantially more important component of their post-FRA incomes.[3] Figure 2 shows household income (adjusted for household size, described in Wu et al., 2016) two years after FRA, broken down by key sources. Among DI beneficiaries, regardless of the age of claiming, OASI benefits represent two-thirds of total household income in post-FRA years, with the remaining portion coming from pensions, earnings, and other sources combined. Among those who claim OASI at or after FRA, post-FRA income comes from a combination of SSA benefits, pensions, earnings, and other sources including other investments. Early OASI claimers receive a larger share of their incomes from OASI, but still less than half of household income on average comes from SSA benefits and a substantial share comes from other sources.

[3] We include Supplemental Security Income payments in the measure of SSA benefits, which are about $200 a month on average for those who receive it (about 5 to 6 percent of DI beneficiaries but less than 2 percent of OASI claimers).

Figure 2. Household income from key sources two years after the FRA, DI beneficiaries and OASI claimers



Source: Wu et al. (2016).

Notes: Total household income (adjusted for household size) is shown in parentheses under each group label on the x-axis. Values are reported two years after FRA. We adjusted all values to 2012 dollars.

In addition to DI beneficiaries, a subset of OASI claimers may be particularly financially vulnerable in retirement. Previous research has shown that many early OASI claimers have characteristics and health similar to DI beneficiaries (Bound and Waidmann 2010; Burkhauser et al. 1996). In our sample, 6 percent of all OASI claimers applied for DI but did not receive it and 17 percent reported that they had significant limitations in health or functioning at age 59; within this group, 9 in 10 claimers received OASI before FRA. We find that rejected DI applicants fare worse than DI beneficiaries on most measures after FRA, and that workers with health limitations fare slightly better than DI beneficiaries, but worse than other early OASI claimers. For both groups, SSA benefits represent at least half of their post-FRA household incomes.

Implications for Policy

DI and OASI benefit structures have drawn the attention of policymakers grappling with the depletion of the OASI and DI trust funds. Proposals to ensure the solvency of the trust funds, combined, have included changing the benefit structure for those who claim OASI before FRA (by modifying the earliest age of eligibility or implementing larger benefit reductions for those who claim early) and changing the interplay between DI and OASI at FRA (Pineles-Mark 2015). In each case, policymakers have expressed concern about the effect on beneficiaries' well-being, both at the time of claiming and in the years following FRA.

A small but growing literature highlights how individuals who experience disability during their working years fare in retirement (Johnson et al. 2007; McGarry and Skinner 2009; Meyer and Mok 2016; Khan et al. 2016). Together with our work, this body of evidence indicates that DI beneficiaries remain vulnerable in the years after FRA and that SSA benefits are a critical part of their income. Although the large differences observed between DI beneficiaries and OASI claimers remain do not increase as after the FRA, very large differences in wealth imply that the relative financial security of DI beneficiaries declines, because they have little wealth from which to draw income in later years.

Our work shows that even small reductions in benefits could have lasting impacts on workers with disabilities, even those who did not receive DI benefits. SSA benefits are a significant share of income for these households. In addition, members of this vulnerable group have modest wealth, meaning that it is likely that many of them would not be able to offset benefit reductions with accumulated assets or other income sources. Moreover, workers with significant limitations in health and functioning may have high medical expenses that would consume a larger share of their incomes than for relatively healthier retirees, even with Medicare coverage. Our study highlights the importance of considering the short- and longer-term consequences of potential policy changes for DI beneficiaries as they transition into retirement.

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