

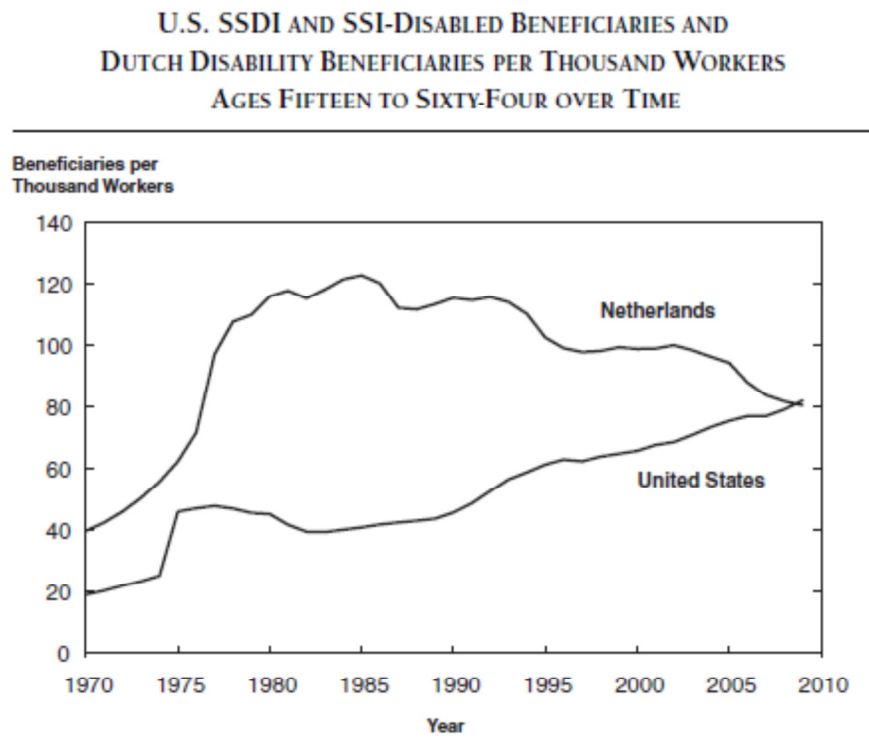
Testimony before the U.S. Senate Budget Committee

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Disability benefit schemes are often used as a provision to accommodate social change, and cyclical ups and downs. In the Netherlands, the DI scheme supported structural change towards a service-oriented economy and it mollified the transition of Dutch households from a traditional single breadwinner type to a modern dual earner family. Similar uses of disability benefit schemes could be seen in Eastern Europe to soften the pains of transition to a market economy in the 90s. In the U.S., too, the pronounced positive relationship between the national unemployment rate and the SSDI application rate shows that SSDI works as an alternative, and more generous, unemployment scheme. It is one of the factors that caused secular growth in the U.S. number of disability benefits.

Figure 1

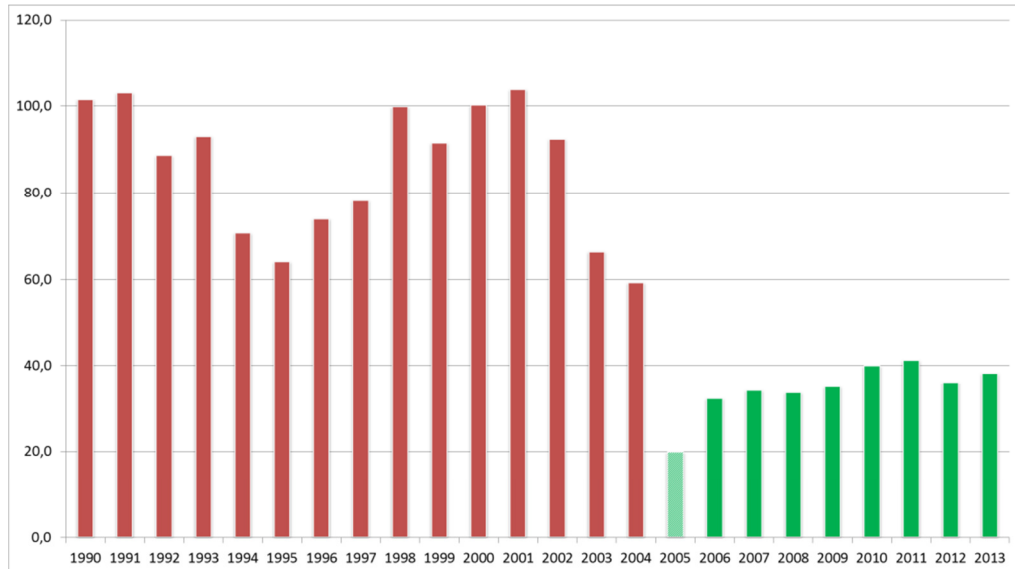


Source: Richard V. Burkhauser and Mary C. Daly, *The Declining Work and Welfare of People with Disabilities*. The AEI Press, 2011.

The drawback of using disability benefits as a 'soft' unemployment scheme is that it hides the lack of targeted, more cost-effective, provisions, and postpones their introduction. Meanwhile, huge unfunded financial liabilities are created given the

long average duration of disability benefit dependency. The Dutch case is a good illustration both of the size of such liabilities and of the long political road it took to change an entitlement oriented disability policy into an employment oriented one.

Figure 2: Number of Dutch DI awards, 1990-2013



Under pressure of an ageing workforce the Dutch government took a series of steps from 2002 onwards. These were successful in bringing down DI awards by 60% between 2002 and 2012 (see Figure 2).

Financial incentives for firms

The major element causing the drop in DI-inflow is early intervention (before DI application), fuelled by strong financial incentives for firms. All Dutch firms are obliged to pay for sickness benefits, rehabilitation, accommodation, job mediation during the first two years of disablement (before DI application). Moreover, DI benefits are financed by contributions that are experience rated at the level of the firm. This means that Dutch firms pay substantially higher rates if one or more of their employees enter the DI scheme.

Financial incentives for workers

Dutch workers also face stronger incentives. Although sickness benefits replace about 85% of wages, the DI benefits are lower and such that they make work pay if someone has a residual earning capacity that is more than 20% of his previous earnings. If such partially disabled workers do not use their residual capacity they get a much lower benefit.

From 2004 more stringent eligibility standards apply, and these standards are strictly administered by the DI program administrators. The denial rate is about 45%, and proves robust against cyclical variations in applications. Denied applicants can rely on UI benefits for a limited period. About 10% of those denied a benefit re-apply later.

Reforming a benefit program creates the issue of what to do with the current beneficiary population. Between October 2004 and December 2007 all (300,000) WAO beneficiaries younger than 45 were re-assessed using the stricter standards. 39% of the benefits were terminated or reduced, and among this group about 60% were working three years after their benefit status was reviewed.

The reformed Dutch DI scheme purports to cover only those that have hardly any productive capacity left, and to provide other workers with disabilities with strong incentives to remain active. The results for the first nine years of the operation of the new scheme show that inflow rates have dropped substantially to levels that are reasonable by international standards, and showed to be robust against the deep recession of 2008-2013. The incentive structure that steers the behaviour of employers and long-term sick workers proves to work.