

This article offers a brief summary of the workers' compensation and Social Security Disability Insurance programs. Information highlighted includes the differences between the two programs' types and terms of coverage. It compares the differing patterns in workers' compensation and Social Security disability benefits as a percentage of wages over the past few decades and considers the potential causes for such trends. The article also explains the offset provision included in the 1965 Social Security Amendments, the intention behind the offset, and how and when offsets are applied.

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Workers' Compensation, Social Security Disability Insurance, and the Offset: A Fact Sheet

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This fact sheet provides an overview of workers' compensation, Social Security Disability Insurance, and the interaction of these two programs. The information is based on presentations given at the policy research seminar, *Interaction of Workers' Compensation and Social Security Disability Insurance*, cosponsored by the National Academy of Social Insurance and the Social Security Administration. Coordination of disability benefits is recognized as a desirable public policy to ensure that disability payments come from the appropriate program and that the total amount of disability benefits paid does not become a deterrent to return to work.

Workers' Compensation

Workers' compensation provides benefits to workers who are injured on the job or have a work-related illness. Benefits include medical treatment for work-related conditions and cash payments that partially replace lost wages. Temporary total disability benefits are paid while the worker recuperates away from work. If the condition has lasting consequences after the worker heals, permanent disability benefits may be paid. In the case of a fatality, the worker's dependents receive survivor benefits.

Before workers' compensation laws were enacted, an injured worker's only legal remedy for a work-related injury was to bring a tort suit against the employer and prove that the employer's negligence caused the injury. Under the tort system, workers often did not recover damages; those who did recover damages sometimes experienced delays or high costs in doing so. Although employers generally prevailed in court, they nonetheless were at risk for substantial and unpredictable losses if the workers' suits were successful. Ultimately, both employers and employees favored legislation to ensure that a worker who sustained an occupational injury or disease arising out of and in the course of employment would receive predictable compensation without delay, irrespective of who was at fault. As a *quid pro quo*, the employer's liability was limited. Under the exclusive remedy concept, the worker accepted workers' compensation as payment in full and gave up the right to sue the employer.

Workers' compensation programs are designed and administered by the states. The programs vary across states in terms of who is allowed to provide insurance, which injuries or illnesses are compensable, and the level of benefits. Generally, state laws require employers

to obtain insurance or prove they have the financial ability to carry their own risk (that is, to self-insure).

Workers' compensation is financed almost exclusively by employers, although economists point out that workers pay for a substantial portion of the costs of the program in the form of lower wages (Leigh and others 2000). The premiums paid by employers are based in part on the industry classifications of the employers and the occupational classifications of their workers. Many employers are also experience rated, which results in higher (or lower) premiums for employers whose past experience demonstrates that their workers are paid more (or fewer) benefits than workers for similar employers in the same insurance classification.

In 2002, workers' compensation covered 125.6 million workers (Thompson Williams, Reno, and Burton 2004). Total wages of covered workers were \$4.6 trillion and total workers' compensation benefit payments were \$53.4 billion, which amounted to \$1.16 per \$100 of covered wages. Employers' costs for workers' compensation—defined here as premiums written for policies in the calendar year, payments made under deductible arrangements, and the benefits and administrative costs of self-insurers—were \$72.9 billion. Benefits and costs have declined from a peak in the early 1990s (Chart 1).

The difference between workers' benefits and employers' costs per \$100 of covered wages is accounted for by expenses such as administrative and loss adjustment costs, taxes, and contributions for special funds, which can include the support of workers' compensation agencies, and the insurers' profits or losses.

Social Security Disability Insurance

Workers' compensation in the United States is surpassed in size only by the federal Social Security Disability

Insurance and Medicare programs in providing cash and medical benefits to disabled workers.

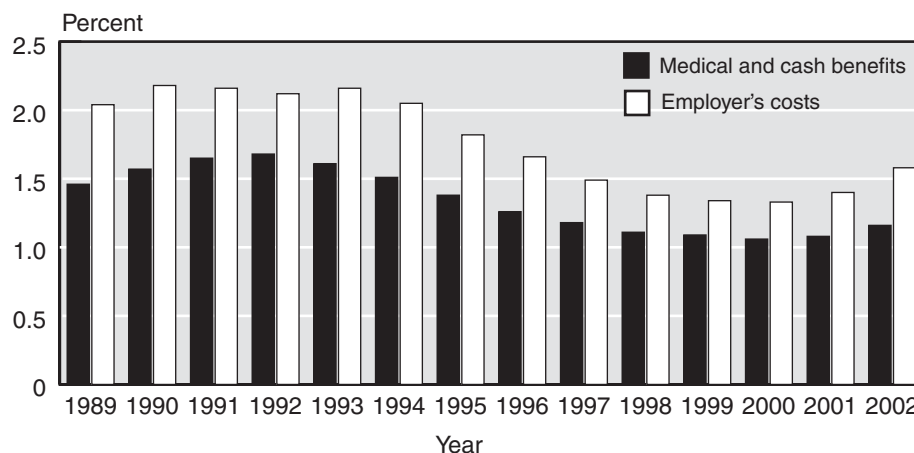
Although Social Security disability benefits and workers' compensation are the nation's two largest disability benefit programs, the two programs are quite different. Workers are eligible for workers' compensation benefits from their first day of employment, but Social Security disability benefits are paid only to workers who have a substantial work history. Workers' compensation provides benefits for both short-term and long-term disabilities and for partial as well as total disabilities. These benefits cover only disabilities arising out of and in the course of employment. In contrast, Social Security disability benefits are paid only to workers who have long-term impairments that preclude any gainful work, regardless of whether the disability arose on or off the job. By law, the benefits are paid only to workers who are unable to engage in any substantial gainful activity by reason of a medically determinable physical or mental impairment that is expected to last at least a year or result in death. The impairment has to be of such severity that the worker is not only unable to do his or her previous work but is also unable to do any other type of substantial gainful work. Social Security disability benefits begin after a 5-month waiting period.

The amount of benefits that Social Security paid in wage-replacement benefits to disabled workers and their dependents in 2002 was nearly twice the amount of cash benefits paid under workers' compensation—\$65.6 billion compared with \$29.2 billion. Employer and employee each pay 5.3 percent of wages for Social Security's Old-Age and Survivors Insurance and 0.9 percent for Disability Insurance. Thus, the total paid for Disability Insurance is 1.8 percent of taxable wages.

Trends in Social Security Disability Benefits and Workers' Compensation

Social Security disability benefits and workers' compensation had different trends in benefits paid relative to covered payroll. Social Security disability benefits grew rapidly in the early 1970s and then declined through the late 1980s, after policy changes in 1977 and 1980 reduced benefits and tightened eligibility rules. From 1989 to 1996, Social Security benefits again rose as claims and allowances increased during the economic recession of 1990–1991

Chart 1. Workers' compensation costs and benefits per \$100 of payroll, 1989–2002



SOURCE: National Academy of Social Insurance estimates.

(Chart 2). Since then, benefits relative to covered wages have been fairly stable (Board of Trustees 2004).

The trend in workers' compensation benefits as a share of covered wages follows a very different pattern. Total workers' compensation benefits (cash and medical combined) were less than Social Security disability benefits during the 1970s but grew steadily throughout the 1970s and surpassed Social Security disability benefits in the mid-1980s. While Social Security disability benefits were flattening out during the mid-1980s, workers' compensation payments continued to grow at a rapid rate. Then, as workers' compensation payments declined as a share of covered wages after 1992, Social Security disability benefits rose.

The opposite trends in workers' compensation and Social Security disability benefits during much of the past 25 years raise the question of whether retrenchments in one program increase demands placed on the other, and vice versa. The substitutability of Social Security disability benefits and workers' compensation for workers who have significant, long-term disabilities that are, at least arguably, work related, or might be exacerbated by the demands of work, has received little attention by researchers and is not well understood (Burton and Spieler 2001).

The Offsets

An offset for concurrent receipt of workers' compensation was contained in the original 1956 Social Security

disability program, eliminated in 1958, and reinstated in 1965. The 1965 Social Security Amendments required that Disability Insurance benefits be reduced when the worker is also eligible for periodic or lump-sum workers' compensation payments, so that the combined amount of workers' compensation and Social Security disability benefits does not exceed 80 percent of the worker's average current earnings. The combined payments after the reduction, however, will never be less than the amount of total Social Security disability benefits before the reduction. Average current earnings are defined as the highest of

- the average monthly wage on which the unindexed disability primary insurance amount is based,
- the average monthly earnings from covered employment and self-employment during the highest 5 consecutive years after 1950, or
- the average monthly earnings in the calendar year of highest earnings from covered employment during the 5 years ending with the year in which disability began.

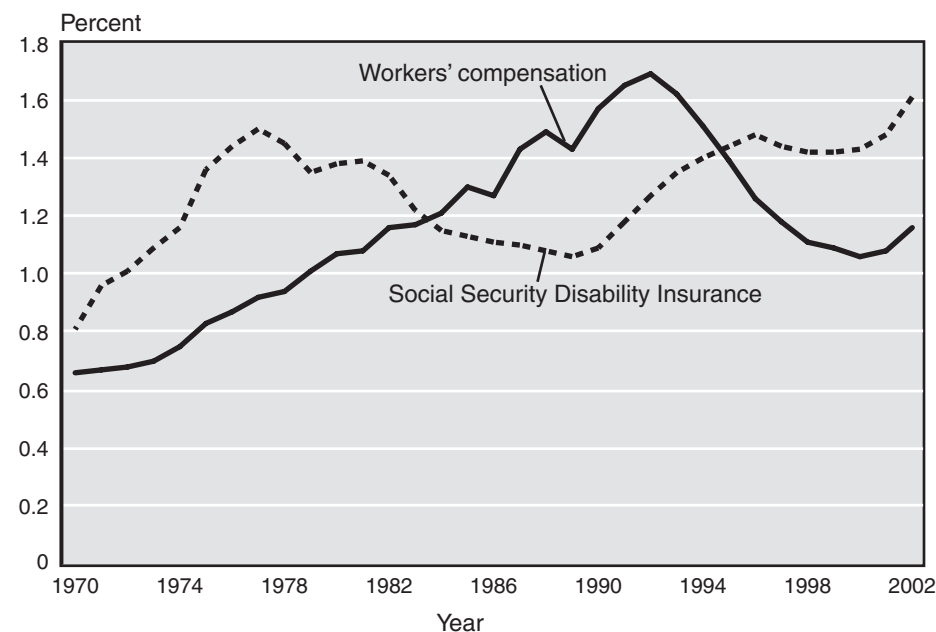
Total earnings, including those above the Social Security taxable maximum, are used to determine average current earnings.

The intent of the offset provision is to ensure that the combined benefits from workers' compensation and Social Security are not excessive. The offset of Disability Insurance benefits applies to disabled workers under the

age of 65 and their families. Benefits for a worker's spouse or dependent children are offset before the offset is applied to the worker's benefit. Under the 1965 law, the Social Security disability benefit will not be reduced if the state workers' compensation law or plan provided for a reverse offset (a reduction of the workers' compensation benefit of a worker also receiving Disability Insurance).

The Omnibus Budget Reconciliation Act of 1981 (Public Law 97-35) ended the option for additional states to adopt reverse offsets. It also extended the Social Security disability offset to apply to certain public disability benefits paid by federal, state, or local governments. In particular, it applies to disability benefits that are earned in employment that is not covered by Social Security—for example, in jobs that

Chart 2.
Social Security Disability Insurance and workers' compensation benefits as a percentage of wages, 1970–2002



SOURCE: National Academy of Social Insurance, *Workers' Compensation: Benefits, Coverage and Costs, 2002* (Washington, DC: NASI, August 2004).

are covered by the California Public Employees' Retirement System and not by Social Security. At the time of the 1981 legislation, 16 states and Puerto Rico had reverse offset statutes, which remain today.

When a workers' compensation law provides for periodic payments but permits a lump-sum settlement that discharges the liability of the insurer or the employer, the settlement is subject to the offset. In this case, the lump sum is prorated to reflect the monthly rate that would have been paid had the lump-sum award not been made. Medical and legal expenses incurred by the worker in connection with workers' compensation may be excluded when computing the offset.

Specifically excluded from these offset provisions are all Department of Veterans Affairs' benefits; needs-based benefits; federal, state, or local disability benefits that are based on employment that was covered by Social Security; and private pension or private insurance benefits.

In December 2003, about 7.6 million beneficiaries (workers and dependents) received Social Security Disability Insurance benefits. Of those beneficiaries, about 1.3 million, or about 17 percent, had some connection to workers' compensation or public disability benefits.¹ That connection includes those who

- received workers' compensation or public disability benefits,
- had received workers' compensation or public disability benefits in the past,
- received a lump-sum settlement in lieu of periodic benefits, or
- had claims pending for workers' compensation or public disability benefits.

Of those with a connection to workers' compensation or public disability benefits,

- about 1 million were disabled workers, and about 240,000 were dependents;
- about three-fourths were connected to workers' compensation and one-fourth to other public disability benefits;² and
- 53 percent of disabled workers had a pending connection or claim, and 47 percent had a prior connection.

The percentage of Social Security Disability Insurance beneficiaries with a connection to workers' compensation or public disability benefits varies by state of residence, in part because workers' compensation programs vary, as do rules for coverage of public employees under Social Security and alternative public disability benefits. Jurisdictions with the highest percentages of workers with a

connection to workers' compensation or public disability benefits are California, Puerto Rico, Rhode Island, and West Virginia.

Jurisdictions with the lowest percentages include the District of Columbia (just 5 percent), Indiana (7 percent), Wisconsin (about 8 percent), and North Carolina (9 percent).

Notes

¹ The 1.3 million includes a small number of beneficiaries (1,851 workers and 6,057 dependents) who are not currently receiving benefits because their entire benefit is being offset.

² Excludes reverse offset, no offset, or pending cases, which can be either workers' compensation or public disability benefits.

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