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# **Social Security Disability Insurance (SSDI): Becoming Insured, Calculating Benefit Payments, and the Effect of Dropout Year Provisions**

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## Summary

Eligibility for Social Security Disability Insurance (SSDI) benefits are based on a worker's insured status, and payment levels are associated with the individual's career earnings under covered employment. Monthly payments are calculated using a formula that takes into account the period of employment, a worker's average earnings over that period, and the application of "dropout years."

To be insured for SSDI benefits, a claimant must have worked a minimum amount of time in covered employment. First, a worker must be "fully insured," which requires one quarter of coverage for each calendar year after the age of 21, with a minimum of six quarters and a maximum of 40 quarters. In 2014, each quarter of coverage requires \$1,200 in earnings. Second, a recency of work test requires 20 quarters of coverage in the 40 quarters preceding the onset of a disability; that is generally five years of work in the last 10, although fewer quarters are required for younger workers.

In calculating the SSDI benefit level, up to five years of a worker's lowest years of earnings are eliminated or "dropped" to minimize the effect of lower years of earnings on monthly payments. An eligible worker who becomes disabled has one year of earnings dropped (via the disability dropout year provision) for every five years of earnings, known as the one-for-five rule. A separate childcare dropout year (CDY) provision also disregards from benefit calculations up to two years in which a beneficiary received no income during periods when he or she was caring for a young child. The number of CDYs applied to a benefit calculation may be offset by the number of disability dropout years applied and vice versa. The CDY provision largely benefits a small subset of SSDI recipients with lower career earnings.

This report provides (1) an overview of the SSDI program and how workers become insured for SSDI benefits, (2) an explanation of how benefit payments are calculated, and (3) a description of how the dropout year provisions affect the calculation of disability benefit payments. The report concludes with a brief analysis of the earnings of disabled workers that have been credited with CDYs.

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## Introduction

The disability insurance portion of the Old-Age, Survivors and Disability Insurance (OASDI) program was enacted in 1956 and provides benefits to disabled workers under the full retirement age (FRA) in amounts based on an individual's career-average earnings in covered employment.<sup>1</sup> A statutory formula determines monthly payment levels for Social Security Disability Insurance (SSDI).<sup>2</sup> In addition, the law also eliminates from benefit calculations one year of a SSDI beneficiary's lowest earnings for every five years of earnings (also known as the one-for-five rule), which equates to a maximum of five "disability dropout years" for an individual with 25 or more years of earnings. By statute, SSA also applies "childcare dropout years" (CDYs) for years in which a beneficiary has zero earnings due to leaving the workforce to care for an infant child. The application of CDYs is not common, affecting approximately 0.16% of SSDI beneficiaries between 2000 and 2013. This report describes how workers become insured for SSDI benefits, how SSDI benefits are calculated, and the use of dropout years in benefit calculations.

## Social Security Disability Insurance Benefits

### Eligibility Requirements

SSDI benefits, like those of the Old-Age and Survivors Insurance (OASI) program, are meant to replace income from work that is lost by incurring one of the risks the social program insures against. The SSDI program is financed primarily through a payroll tax levied on workers, their employers, and self-employed individuals in jobs covered by Social Security.<sup>3</sup> To be eligible for SSDI benefits, a worker must be (1) disability insured, and (2) unable to engage in substantial gainful activity (SGA) by reason of a medically determinable physical or mental impairment expected to result in death or last at least 12 months. Generally, the worker must be unable to do any kind of work that exists in the national economy, taking into account age, education, and work experience.<sup>4</sup> Special rules for disability insured status apply to individuals under the age of 31.

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<sup>1</sup> The FRA is the age at which an individual can receive their full retirement benefit. Under the Social Security Amendments of 1983 (P.L. 98-21), the FRA is increasing gradually from 65 to 67. The FRA will reach 67 for persons born in 1960 or later, i.e., persons who become eligible for benefits at the age of 62 in 2022. See CRS Report R41962, *The Social Security Retirement Age: In Brief*, by Gary Sidor.

<sup>2</sup> 42 U.S.C. §415.

<sup>3</sup> See CRS Report RL32279, *Primer on Disability Benefits: Social Security Disability Insurance (SSDI) and Supplemental Security Income (SSI)*, by Umar Moulta-Ali.

<sup>4</sup> This report focuses on benefit payments to disabled workers, however additional benefits may also be provided to a worker's spouse, and qualified children. See CRS Report RS22294, *Social Security Survivors Benefits*, by Scott D. Szymendera.

## Becoming Fully Insured for SSDI

### *Quarters of Coverage*

To be fully insured, a worker must have worked a minimum amount of time in employment covered by Social Security.<sup>5</sup> Generally, an individual must have one quarter of coverage (also referred to as “credits”) for each calendar year after the age of 21 up to the year before the individual (1) reaches the age of 62, (2) dies, or (3) becomes disabled.<sup>6</sup> A minimum of six quarters is required to become fully insured. In 2014, each quarter of coverage requires \$1,200 in earnings, which is indexed annually to average wage growth.<sup>7</sup> Workers under the age of 31 need to have credit in one-half of the quarters during the period between when they attained age 21 and when they became disabled.

### *Recency of Work*

In addition, a recency of work test requires the worker to have 20 quarters of coverage in the 40 quarters preceding the onset of disability (generally five years of work in the last 10).<sup>8</sup> An exception applies to disabled workers under the age of 31; these individuals can meet the recency of work test by having credit in at least one-half of the calendar quarters during the period beginning with the quarter after the quarter the individual turned 21 and ending with the quarter that they became disabled. The recency of work test does not apply to individuals who are blind.

### **Inability to Engage in Substantial Gainful Activity**

To qualify for benefits, a disabled worker must also be unable to engage in “substantial gainful activity” (SGA).<sup>9</sup> In 2014, SGA is the ability to earn \$1,070 in a month.<sup>10</sup> Since July 1999, the SGA amount has been adjusted annually to reflect the growth in average wages.

## Calculating Average Indexed Monthly Earnings

The SSDI benefit payment is based on a disabled worker’s average indexed monthly earnings (AIME), which is used in the computation of the individual’s Primary Insurance Amount (PIA). For SSDI beneficiaries, the initial monthly benefit payment equals the PIA.

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<sup>5</sup> Similar eligibility rules exist for retirement and survivors benefits; see CRS Report R42035, *Social Security Primer*, by Dawn Nuschler.

<sup>6</sup> 42 U.S.C. §414; 20 C.F.R. §404.110. Also see *Online Social Security Handbook, Chapter 2: Becoming Insured*, available at [http://www.ssa.gov/OP\\_Home/handbook/handbook.02/handbook-toc02.html](http://www.ssa.gov/OP_Home/handbook/handbook.02/handbook-toc02.html).

<sup>7</sup> An individual can earn up to four quarters per year, but quarters do not equate to actual calendar quarters.

<sup>8</sup> 20 C.F.R. §404.130.

<sup>9</sup> SSA uses the term SGA to describe a level of work activity and earnings. According to SSA, substantial entails doing “significant physical or mental activities or a combination of both,” while gainful work activity involves work performed or intended for profit.

<sup>10</sup> By statute, a higher SGA amount is set for individuals who are blind, which is \$1,800 in 2014. For more information, see SSA, *Substantial Gainful Activity*, at <http://www.ssa.gov/oact/cola/sga.html> and CRS Report RS20479, *Social Security: Substantial Gainful Activity for the Blind*, by William R. Morton.

The AIME is calculated as the sum of indexed earnings over the computation period, divided by the number of “computation years” (in months).<sup>11</sup> The AIME is calculated based on an individual’s earnings record by indexing—to national average wage growth—the worker’s earnings during full calendar years after 1950 and up to the second year prior to the year (the “indexing year”) of SSDI eligibility.<sup>12</sup> Earnings in years after the indexing year are not indexed and are counted at their nominal value.<sup>13</sup> This adjusts a beneficiary’s earnings to be comparable to the earnings level in the year he or she became disabled.

The number of computation years used in the AIME determination is equal to the number of “elapsed years,” minus any dropout years as discussed below. By statute, the number of elapsed years equals the calendar years after an individual turns age 21 through the year before the individual first becomes eligible for SSDI benefits.<sup>14</sup> The minimum number of computation years used is two. The individual’s highest (indexed) earnings years are used as computation years for the AIME calculation. Computation years may include years of zero earnings when the number of computation years is greater than the number of years of earnings; it is these computation years of zero earnings for which CDYs may be applied for eligible individuals.

### Disability Dropout Years in AIME Calculations

Under current law, SSA will remove up to five of a disabled worker’s elapsed years with the lowest earnings in calculating the AIME.<sup>15</sup> Also known as the *one-for-five* (or one-fifth) rule, for every five elapsed years of earnings, the lowest year(s) of earnings will be dropped, up to a maximum of five total *disability dropout years* for a worker with 25 or more years of earnings.<sup>16</sup> This provision reduces the effects of years of lower earnings on a disabled worker’s benefit amount. For example, for a worker who becomes disabled with seven years of work history in covered employment, only the highest six years of earnings will be used for the purposes of AIME calculation (i.e., applying one disability dropout year). If the worker had 10 years in covered employment, SSA would use the highest eight years of earnings (i.e., applying two disability dropout years).

### Childcare Dropout Years in AIME Calculations

In addition, in calculating the AIME, disabled workers who receive fewer than three disability dropout years under the one-for-five rule (as described above) may be credited with up to two additional dropout years based on the care of a child, for up to a total of three dropout years.<sup>17</sup> Specifically, these “childcare dropout years” (CDYs; also referred to as caregiving years) may be

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<sup>11</sup> 20 C.F.R. §404.211.

<sup>12</sup> 20 C.F.R. §404.211. Language in this section is adapted from “Benefit Calculations” in the Social Security Administration’s *2012 Annual Statistical Report on the Social Security Disability Insurance Program*.

<sup>13</sup> 20 C.F.R. §404.211(d)(ii).

<sup>14</sup> Online Social Security Handbook §704.1, available at [http://www.ssa.gov/OP\\_Home/handbook/handbook.07/handbook-0704.html](http://www.ssa.gov/OP_Home/handbook/handbook.07/handbook-0704.html).

<sup>15</sup> 42 U.S.C. §415(b)(2)(A)(ii); 20 C.F.R. §404.211(e)(3).

<sup>16</sup> Any elapsed year can count as a dropout year (e.g., a person with 10 years of earnings could have years 1 and 2 as dropout years).

<sup>17</sup> 20 C.F.R. §404.211(e)(4). A total of three dropout years is based on a combination of disability dropout years and childcare dropout years.

credited under two conditions: (1) the SSDI claimant had a child (or the child of a spouse) under the age of three in his or her care for at least nine months throughout a given year, and (2) the SSDI claimant had no earnings in that year.<sup>18</sup>

In addition, the year selected as a CDY must also be a year that could be selected as a benefit computation year. The claimant must have a minimum of two computation years.<sup>19</sup> Authorized by the Social Security Disability Amendments of 1980 (P.L. 96-265), the CDY provision became effective July 1981.

### Example of AIME Calculation Using Disability and Childcare Dropout Years<sup>20</sup>

Ms. M. was born August 4, 1983, and turned 21 on August 4, 2004. She became entitled to SSDI benefits beginning in December 2013 based on a disability which began July 15, 2013. In computing the AIME, SSA determines that the elapsed years is eight (2005 through 2012), the number of disability dropout years is one (based on the one-for-five rule), setting the number of benefit computation years at seven (eight elapsed years minus one disability dropout year). Since Ms. M. had no earnings in 2005, SSA drops out 2005 and uses her earnings for the years 2006 through 2012. Ms. M. lived with her child, who was born in 2006, in all months of 2006 and did not have any earnings during that year. SSA therefore reduces the seven computation years by one childcare dropout year (in addition to the year 2005 which was dropped initially) to get six computation years.

SSA will use six computation years to find Ms. M.'s AIME. SSA excludes 2005 and 2006 and totals her indexed earnings for the remaining years, i.e., the benefit computation years (including her unindexed earnings in 2010 and 2012) and gets \$115,200. SSA then divides that amount by the 72 months in her six benefit computation years and finds her AIME to be \$1,600.

### *The Interaction of Disability Dropout Years and Childcare Dropout Years*

CDYs are offset by disability dropout years and can only be credited to eligible SSDI beneficiaries when the number of disability dropout years is less than three. As presented in **Table A-1**, an eligible individual may be credited with one CDY at three elapsed years. Two CDYs may be credited at four elapsed years. At five elapsed years, a disability dropout year may be credited (in addition to the two CDYs) for three total dropout years. CDYs begin to phase out at 10 elapsed years, as one CDY is replaced with one disability dropout year. CDYs completely phase out at 15 elapsed years as both CDYs are replaced with disability dropout years.

### Calculating the Primary Insurance Amount

A disabled worker's PIA is determined by applying a formula to the AIME as shown in **Table 1**.<sup>21</sup> First, the AIME is sectioned into three brackets (or segments) of earnings, which are divided by dollar amounts known as bend points. For 2014, the bend points are \$816 and \$4,917.<sup>22</sup> Three

<sup>18</sup> 42 U.S.C. §415(b)(2) Clause (ii); 20 C.F.R. §404.211(e)(4). This may also include the calendar year in which the child attained the age of three, see SSA Program Operations Manual (POMS) RS 00605.235.A.2.b at <http://policy.ssa.gov/poms.nsf/lnx/0300605235>. CDYs were initially introduced in the Social Security Disability Amendments of 1980 as an anti-poverty measure in an effort to reduce the effects of lower Social Security benefits for women who forgo potential earnings and perform unpaid work while caring for young children. However, both women and men are eligible for CDYs in the calculation of their benefits.

<sup>19</sup> For more information, see SSA POMS §RS 00605.235 *Childcare Dropout Years*, at <http://policy.ssa.gov/poms.nsf/lnx/0300605235>.

<sup>20</sup> This example is adapted from 20 C.F.R. §404.211(e)(4).

<sup>21</sup> The PIA calculation similarly applies to OASI beneficiaries.

<sup>22</sup> The bend points are indexed to average wage growth under current law.

replacement factors—90%, 32%, and 15%—are applied to the three brackets of AIME.<sup>23</sup> The three products derived from multiplying each replacement factor and bracket of AIME are added together. For a worker who becomes disabled in 2014, the PIA is determined as shown in the example in **Table 1**. A disabled worker’s benefit is equal to his or her PIA. In addition, a beneficiary’s payment increases each year from the year of eligibility to the year of benefit receipt based on the Social Security cost-of-living adjustment (COLA).<sup>24</sup>

**Table 1. Computation of “Ms. M.’s” Primary Insurance Amount (PIA) in 2014 Based on Her AIME of \$1,600**

Factors	Three Brackets of AIME	PIA
90%	first \$816 of AIME, plus	\$734.40
32%	AIME over \$816 and through \$4,917, plus	\$250.88
15%	AIME over \$4,917	\$0.00
<b>Total PIA (rounded down)</b>		<b>\$985.00</b>

**Source:** CRS table based on *Computation of Primary Insurance Amount* at 42 U.S.C. Section 415.

**Note:** The PIA is rounded down to the next whole dollar.

## Analysis of PIA for SSDI Beneficiaries Credited with CDYs

Some 861,396 disabled workers aged 25 to 36 at the time of disability-onset were awarded SSDI benefits between January 2000 and May 2013.<sup>25</sup> CDYs were applied to 1,336 (0.16%) of these recipients. During this period, most of these individuals (991 or 74.2%) were credited with one CDY, whereas 339 (25.4%) were credited with two CDYs.<sup>26</sup> As shown in **Figure A-1**, the distribution of CDY credits is skewed toward beneficiaries with lower earnings. During this period, 84.5% of beneficiaries (1,129) who were credited with CDYs had a PIA of less than \$1,000.

<sup>23</sup> The replacement factors in the benefit formula are fixed under current law.

<sup>24</sup> Annual COLA increases are indexed to inflation using the CPI-W (Consumer Price Index for Urban Wage Earners and Clerical Workers). See CRS Report 94-803, *Social Security: Cost-of-Living Adjustments*, by Gary Sidor.

<sup>25</sup> These tabulations were provided by SSA from the Master Beneficiary Record upon request from CRS. A worker could initially become eligible for a CDY at age 25, which would phase-out after 14 elapsed years (age 37+). See **Table A-1**.

<sup>26</sup> SSA reported 96 individuals being credited with three CDYs, which is attributed to a coding error. These individuals, while included in disabled worker totals, are excluded from the analysis of beneficiaries credited with CDYs.

## Appendix A. CDY Computation Chart and Graph

**Table A-1. Disability and Childcare Dropout Year (CDY) Computation Chart for SSDI Benefits**

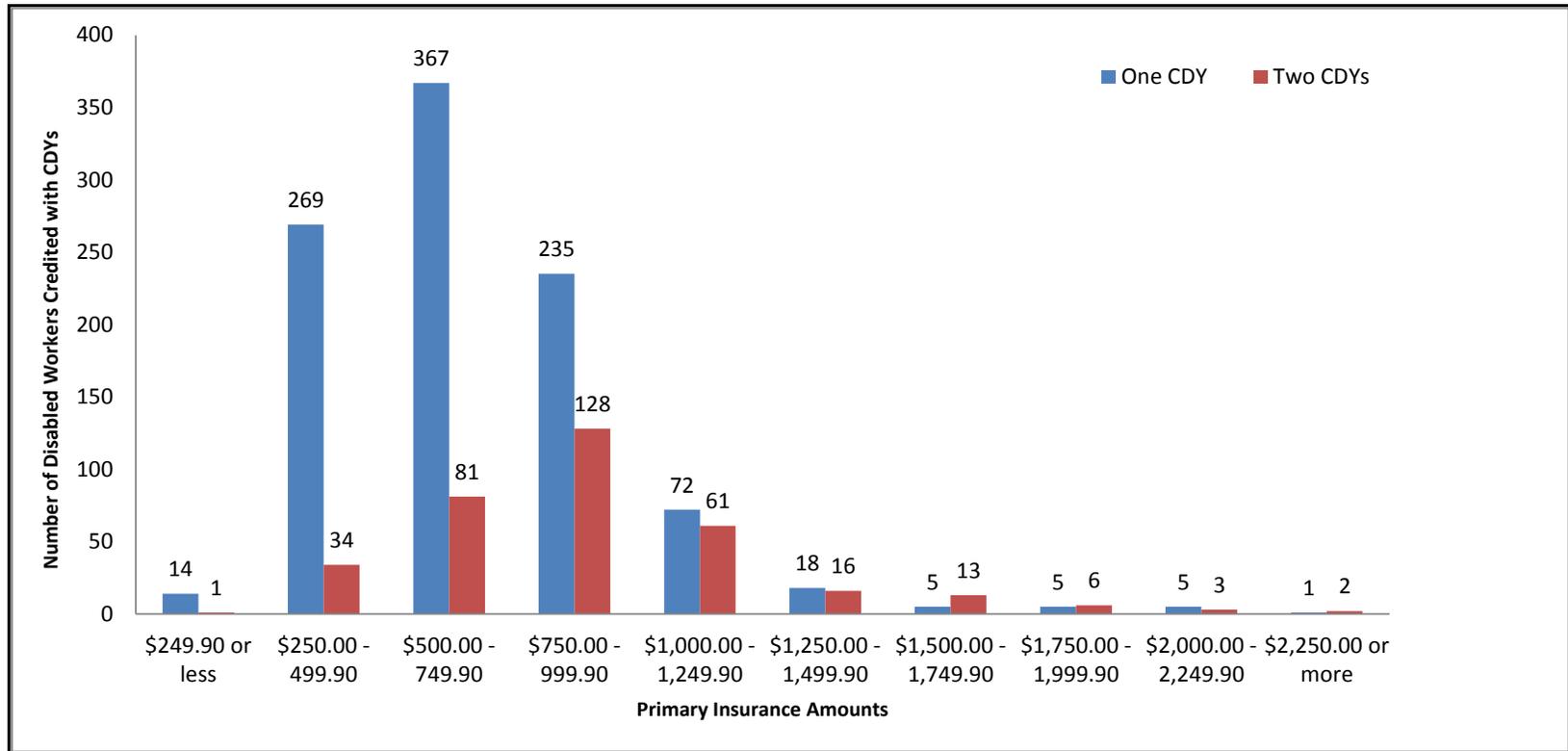
	A	B	C	D	
Age of Disabled Worker (years)	Number of Elapsed Years in Covered Employment	Number of Disability Dropout Years (one-for-five rule)	Maximum Number of Childcare Dropout Years	Total Dropout Years (B+C)	Total Benefit Computation Years (A-D)
22	0	0	0	0	N/A
23	1	0	0	0	N/A
24	2	0	0	0	2
25	3	0	1	1	2
26	4	0	2	2	2
27	5	1	2	3	2
28	6	1	2	3	3
29	7	1	2	3	4
30	8	1	2	3	5
31	9	1	2	3	6
32	10	2	1	3	7
33	11	2	1	3	8
34	12	2	1	3	9
35	13	2	1	3	10
36	14	2	1	3	11
37+	15 or more	3 or more (five maximum)	0 (phased-out after 14 elapsed years)	3 or more (five maximum)	12 or more (depending on the total number of disability dropout years)

**Source:** Congressional Research Service (CRS) table, adapted from the SSA Program Operations Manual System (POMS) § RS 00605.235 *Childcare Dropout Years*, at <http://policy.ssa.gov/poms.nsf/lnx/0300605235>.

**Notes:** At least two benefit computation years after age 21 must be used in SSDI payment calculations; therefore a worker could initially become eligible for a CDY at age 25. CDYs are phased-out after 14 elapsed years as they are offset by disability dropout years. Therefore CDYs would not be applied to the benefit calculations of SSDI recipients aged 37+.

**Figure A-1. Primary Insurance Amounts of Disabled Workers Credited with Childcare Dropout Years (CDYs), 2000-2013**

For SSDI Beneficiaries Aged 25 to 36 at Disability-Onset (n=1,336)



Source: SSA, Master Beneficiary Record.

Note: Data from January 2000 through May 2013.

## **Appendix B. Acronyms used in this CRS Report**

<b>AIME</b>	Average Indexed Monthly Earnings
<b>CDY</b>	Childcare Dropout Year
<b>COLA</b>	Cost-of-Living Adjustment
<b>CPI-W</b>	Consumer Price Index for Urban Wage Earners and Clerical Workers
<b>SSDI</b>	Social Security Disability Insurance
<b>FRA</b>	Full Retirement Age
<b>OASDI</b>	Old-Age, Survivors, and Disability Insurance
<b>OASI</b>	Old-Age and Survivors Insurance
<b>PIA</b>	Primary Insurance Amount
<b>SGA</b>	Substantial Gainful Activity
<b>SSA</b>	Social Security Administration
<b>SSI</b>	Supplemental Security Income