

The United States

The unemployment benefit system: a degree of minimal protection, for 'insiders' only

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The American unemployment benefit system is one of a kind. It is, firstly, largely managed by the individual states, albeit under the supervision of the federal government. The system is, moreover, financed exclusively by employers' contributions, the level of which varies according to the company's past record in terms of redundancies, its 'experience rating'. Finally, the benefit payments provided are particularly scant and of short duration. The choice of a low level of benefit was a deliberate one, designed to avoid creating 'disincentives to work' and to limit so-called 'moral hazard' effects, thus reflecting concerns about 'voluntary unemployment' prevalent among US economists¹. These features arose from a particular historical context. The unemployment insurance system came into being in 1935, following a number of related initiatives, such as the setting up of voluntary company and/or trade union schemes in the 1920s, and the adoption, as of 1932, by certain states such as Wisconsin, of their own legislation (Blaustein, 1993).

The system, designed in the 1930s, as along with the setting up of a public Employment Service, has remained virtually unchanged in terms of its structure and underlying principles, although it has undergone legislative changes and financial tensions several times in the course of its history. It was devised at the outset to cater mainly for people with strong links to the labour market, who are victims of seasonal unemployment resulting from economic cycles (typically people laid off temporarily). Today, therefore, it seems largely unsuited to a labour market which has undergone profound changes. As a result, it offers protection to an ever smaller number of the unemployed (around 1/3 of the total), with no coverage for most part-time and low-paid workers, principally women.

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1. Much research has been done in the United States as to the impact of benefit on the duration of unemployment.

The trade unions remained opposed for a long time to the setting up of a compulsory system, although few of them opted to create their own unemployment funds². The unions played only a very minor part, if any, in the design of the system. They are not at all involved in its management, which has been devolved to the states, leaving these a great deal of freedom as to the form and implementation of schemes (eligibility conditions, duration and level of benefit, etc.). Some reforms have taken place at state level. Nevertheless, no successful attempt has been made at federal level to remedy the main shortcomings of the current regime or to bring about a large-scale reform.

The choice of 'experience rating' and of a decentralised system

The compulsory unemployment insurance system was set up by the 1935 Social Security Act, at the same time as the old-age insurance regime and the social welfare programme for widows with children (Aid to Families with Dependent Children, or AFDC). The Act was adopted in the wake of the Great Depression, when in 1933 the unemployment rate peaked at 25% of the active population. From the outset it was designed as a countercyclical mechanism to support consumption and stabilise the economy, rather than one primarily intended to help provide income security; it was designed as an insurance regime rather than a system of social solidarity. There is in fact no welfare regime in the United States for the long-term unemployed. The decision to create a federal programme under the auspices of the Department of Labor, but managed by the states, was a direct result of the discussions and state legislative initiatives on unemployment insurance which had taken place in the 1910s and 1920s. At the time, there were two main schools of thought. On the one hand, there were the views of John Commons, an institutional economist working at the University of Wisconsin, who advocated an unemployment insurance system based on the principle of modulation of contributions by 'experience rating', as well as the constitution of reserves by employers. On the other were the ideas of the Ohio

2. Unlike their counterparts in Europe, few US trade unions have set up unemployment funds. In 1931, three national craft unions and 45 local union sections did so. A few joint employer/trade union funds were established in the 1920s, while about 30 large companies, including Procter & Gamble, General Electric and Eastman Kodak, created their own unemployment insurance regimes, *cf.* Blaustein (1993).

Commission on Unemployment Insurance, led by I. Rubinow, which, on the contrary, were in favour of a single contribution system (employer and employee) based on risk mutualisation at national level and the setting up of a common unemployment fund (Becker, 1972). Ultimately it was the influence of Commons and his team which prevailed in the final design of the system created by the Social Security Act (Baicker *et al.*, 1997).

At the time, a few standards were set at federal level, but a great deal of freedom was left to individual states in working out the details of their own programmes. One of the federal standards was that the system should be based on a set-rate contribution from employers only. A tax credit would be granted to employers, providing that the state laws respected a certain number of minimum rules set out at federal level. Some measures were included in the legislation to provide particular protection for beneficiaries, allowing an individual, notably, to turn down a job offer if the conditions relating to it were particularly disadvantageous for him/her, or for his/her trade union³. This provision was included to reassure the unions, who might worry that the unemployment benefit system would be used to erode standards of employment and pay. It was for this reason that the AFL finally gave its support to the act, having been opposed until 1932 to the setting up of a compulsory system.

The public employment service was created in 1933 by the Wagner-Peyser Act. This Act established a central administration, as well as public employment agencies at state level to provide job search assistance, although these, at the time, provided no training for job-seekers. It sets out the general framework for the unemployment compensation system, granting a key role to the states, which are entitled to determine the eligibility criteria for unemployment benefits, their level, etc. This decentralised form of organisation was chosen by Congress at a time when it was dominated by local interests⁴. President Roosevelt did not dare to

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3. An unemployed person who turned down a job offer could not be refused benefit, or have benefit stopped, if the offer was for a post left vacant by a striking worker during a labour conflict, if the working and pay conditions were markedly less favourable than in his/her previous employment, or if this offer would oblige the person to join a trade union or call into question his/her right to join a union.
 4. The Southern Democrats, wishing to maintain their racist ways of managing the workforce and to keep labour costs at the lowest levels, were particularly well represented in Congress at this time and chaired some key parliamentary committees.

oppose these groups on this point, for fear of jeopardising the other programmes contained in the Act (the pension regime and assistance to poor children). The characteristics of the system, and the principles underlying it, have scarcely evolved since its beginnings in the 1930s.

Minimal wage replacement and strong incentives to return to work

The unemployment insurance system was created to meet two objectives: to provide temporary and partial compensation for the loss of wage due to an 'involuntary' loss of employment, and to stabilise the economy during periods of recession. The system was thus designed to limit supposed 'disincentives to work', while remaining anchored in the structural characteristics of the US labour market, i.e. considerable employment flexibility and, apart from during periods of economic recession, a relatively low unemployment rate compared to a number of industrialised countries.

The financing of unemployment insurance by contributions

The 1935 Social Security Act (SSA) defined the administrative framework and the rules governing the granting of federal subsidies to the states. The 1939 Federal Unemployment Tax Act (FUTA) then set the level of the employer contribution, or tax, (currently 6.2%) and the minimum wage base subject to this tax (\$7,000 since 1973). The possibility for employers to qualify for a tax credit has brought down the real rate of the employer contribution to 0.8% in those states which meet the requirements set by the federal government. The taxable wage base actually chosen, however, varies from state to state. The employer contribution to unemployment insurance also depends on the number of people made redundant by the company over the previous three to five working years. Newly created businesses are subject to a standard rate for between one and three years. For other employers, the state calculates a rate for each company, based on its past number of redundancies. This rate is then compared with a reference scale, which varies according to the overall solvency of the state unemployment insurance fund, in order to ascertain the contribution rate to be paid by the employer. This rate may vary within a range of 0 to 10%, depending on the company's redundancy record and the state in which it is based, hence the term 'experience rating'.

Generally speaking, these unemployment insurance contributions, or taxes, paid by employers are not very high: from the 1960s to the 1990s, the effective national tax rate averaged about 1% of overall payroll (OECD, 1999) ; over the last decade, it fell to 0,65%. They are collected by the states, paid into a Treasury fund (the Unemployment Trust Fund) which in turn feeds into the federal budget. The money is then reallocated between states according to various criteria (population size, estimated number of job-seekers receiving benefits, etc.). It is used to finance the Employment Service and the unemployment benefit regime, both of which are now, since the 1998 Workforce Investment Act, part of a one-stop delivery system, which also includes further benefit programmes and a federal loan account to states in deficit.

Broad coverage but restrictive eligibility criteria

The tax must be paid by all employers who have at least one employee over a twenty week period, or have paid wages to employees totalling \$1,500 in any quarter of a calendar year. These conditions apply to those working in all sectors, except for certain agricultural labourers, those in domestic service, employees of religious associations and self-employed workers. There are special regimes, set up at the end of the 1930s and in the 1950s, for railway workers, former servicemen and women, and federal civil servants.

The eligibility conditions for receiving unemployment benefit are set by the states. To be entitled to benefit, the claimant must be registered as a job-seeker with a public employment agency, must have worked for a defined period before becoming unemployed (generally for the first four of the last five quarters prior to his/her benefit claim), and must have received a minimum level of earnings during that reference period. The claimant must also prove to the relevant services that he/she is able to work, available for work (registered as a job-seeker) and determined to actively seek work (providing job-seeking reports). Generally speaking, a person may not turn down a job offer or 'suitable work' without a 'good reason'⁵. Most states impose financial penalties if the claimant turns

5. The criteria used to define "suitable work" also vary from one type of job to another, taking account of effects on the health of the claimant, his/her educational background, experience, previous earnings, the distance between the potential place of work and the claimant's home, etc.

down 'suitable work', and some even go so far as to stop unemployment benefit. Over and above the standards for 'suitable work' set out by the FUTA, the states are free to add other criteria, thus rendering eligibility conditions more restrictive. Several, for example, require claimants to seek full-time employment. Job-seekers may also be excluded permanently or temporarily from access to unemployment benefit by intervention of their previous employer, in particular in the case of a voluntary cessation of employment without 'good cause'.

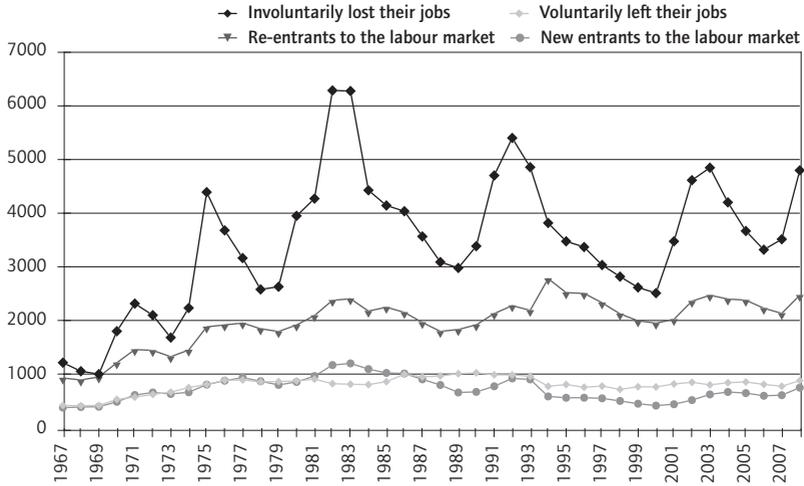
A steady decline in the number of unemployed receiving benefit

Whilst more than 50% of unemployed persons were receiving benefit in the 1950s, the rate has been declining ever since, reaching its lowest point in the middle of the 1980s (28.5% in 1984). At the end of 2007, only 34% of job-seekers were being paid unemployment benefit (Blank & Kerr, 2008). This rate in fact varies over the economic cycle. It increases during periods of recession, such as the present crisis⁶, because of an increase in the number of lay-offs, and goes down during periods of growth, as companies take on workers again. It also varies a great deal depending on the eligibility criteria used by individual states. Two surveys carried out, one at the end of the 1980s and one at the beginning of the 1990s, confirmed that fewer than 50% of unemployed persons actually claimed benefit (Wander & Stettner, 2000). Those who did so had mainly lost their job through no choice of their own: these make up on average a slight majority, just over half, of the number of people becoming unemployed, as is shown in Table 1.

However, those who have voluntarily left their last job, or are seeking to re-enter the labour market after a period away, as well as new entrants just joining the labour force, are far less inclined to register to receive unemployment benefit. The former believe that they will soon be able to find a job, the latter two groups that they are not eligible, which is generally the case. As a result, most unemployed people do not claim unemployment benefit, and those who do so are mainly adults who have lost their job through no choice of their own, in particular those belonging to a trade union.

6. During the first quarter of 2009, the rate had increased to 45% on average, cf. US Department of Labor, *Unemployment Insurance Data Summary*, 1st Quarter 2009, Washington D.C., available at <http://workforcesecurity.doleta.gov/unemploy/content/data.asp>.

Figure 1 Reasons for unemployment (in thousands of persons)

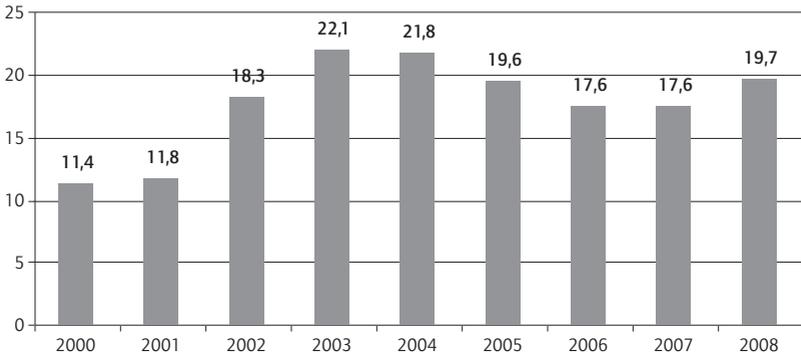


Source: data from the Bureau of Labor Statistics (US Department of Labor).

The specific problem of the long-term unemployed

Although it seems to perform well, the US labour market shows signs of structural weakness. This can be seen in the fact that since 2002 there has been a persistently high level of long-term unemployment (more than 6 months), in spite of the strategies developed in the 1990s to try and combat this phenomenon (CBO, 1997).

Figure 2 Trend in the % of long-term unemployed, 2000-2008



Source: data from the Bureau of Labor Statistics (US Department of Labor).

In 1993, one such federal law required states to carry out an early identification of those job-seekers on benefit considered to be high risk, so that they might be steered towards specialised programmes and tailored job-search assistance. The job-seekers thus identified are required to participate in these programmes, or lose their unemployment benefit. This use of statistical profiling of the unemployed has helped to reduce the cost to the budget of the public Employment Service, with cost savings estimated at \$143 per person thus identified. Nevertheless, it enables jobs to be found for only a low percentage of job-seekers, fewer than 6% in 2007 (Wandner, 2008). Two other types of experimental system have been tried out to encourage the unemployed to return to work, either by giving them a re-employment bonus, or by offering partial financial compensation where the worker's new earnings were lower than in his/her previous employment. The latter provision is similar to the unemployment (and sickness) insurance programme introduced in 2002 for workers over the age of 50 having lost their job as a result of globalisation, by amendment to the 1962 Trade Expansion Act, which set up a federal welfare programme for workers whose jobs had fallen victim to globalisation (Sauviat, 2007).

A low level of benefits, generally time-limited

As a rule, the states provide weekly benefit for a basic maximum period of 26 weeks. When unemployment rates are particularly high, a federal programme (the Federal-State Extended Benefits Program), financed equally by the federal government and the states, allows for supplemental unemployment benefit of between nine months and a year. This programme was adopted in 1970 and amended at the beginning of the 1980s to make it more restrictive. It is now, as it stands, largely ineffective: the relevant legislation is often implemented too late, after the recession is over, and, besides, few states manage to meet the criteria to bring it into play⁷. These flaws have led Congress to vote through an emergency legal text with the same fundamental content as the aforementioned permanent legislation, to be implemented during

7. To benefit from the programme, the state unemployment rate must be at least 120% of its historical average over the reference period (2 years) and at least 5% higher in absolute value over a 13 week period, or exceed 6% in absolute value. Claimants must also have worked full-time for at least 20 weeks or have earned a certain amount before their period of unemployment.

exceptional periods of economic recession. This occurred in 2002, with the voting through of Temporary Extended Unemployment Compensation (TEUC), and once again in 2008 with the Emergency Unemployment Compensation (EUC).

From the very beginnings of the unemployment insurance system, it was generally agreed that the wage replacement rate should stand at around 50%, striking a balance between the two objectives of maintaining purchasing power and avoiding any disincentive to returning to work. Unemployment benefit, which has been fully taxable since 1987, is set at a statutory rate representing between 50 and 59% of pre-tax earnings, subject to a ceiling which varies from state to state. However, the actual replacement rate, as estimated by the Department of Labor, basing itself on the relationship between the average benefit received by the unemployed and the average weekly earnings of workers covered by the scheme, has in fact fluctuated between 30 and 40%, as a national average, since the end of the Second World War. In 2008 it stood at 35%, when the actual weekly benefit received was then close to \$300, for an average effective duration of benefit of nearly 15 weeks⁸.

As well as this publicly funded regime, private unemployment insurance schemes were set up from the mid 1950s, as part of company collective agreements in the automotive sector in particular (Gordon & Amerson, 1957). They provide unemployed trade union members with benefit payments for around a year. When added to the compensation received under the general regime, beneficiaries receive a total replacement income of around 70 to 75% of their gross earnings, subject to a ceiling. This top-up compensation has always been included in the taxable wage base.

Worsening unemployment protection

Originally, the system was designed to support the income of private sector workers working full-time (generally in the manufacturing industry), who had been temporarily laid off for economic reasons (recession or just a slow-down) and would be taken on again when the economy began to recover. It was not intended, then, to combat poverty,

8. Cf. *UI Data Summary, 1st Quarter 2009*, US Department of Labor, *op. cit.*

an objective covered by various social welfare programmes which are generally means-tested. Thus the system was at that time geared solely to adult male bread-winners. This group also happened to correspond to typical US trade union members. This is why union members are still more likely to receive unemployment benefit than other workers (Budd & Mc Call, 2004).

Changes in the labour market since the 1980s have rendered this safety net ineffective for a large number of workers falling victim to unemployment, especially women, who suffer several disadvantages, often occupying a succession of part-time, poorly paid jobs. Loss of employment, on the one hand, has become a lasting, if not permanent, fact of life for a growing number of workers. Periods of unemployment have also grown longer since the 1950s, and there has been a parallel increase in the number of long-term unemployed. Finally, women, whose activity rate has gone up from 37.7% in 1960 to 59.9% in 2000, have reason to leave their jobs more often than men to care for dependent family members. They also work more frequently on a part-time basis and tend to swell the ranks of the lowly paid (US GAO, 2007). For these reasons, women are particularly vulnerable to unemployment but cannot generally meet the criteria entitling them to receive benefit.

The unemployment insurance system is also particularly ineffective in helping people who have just left the main US social welfare programme, set up in 1935 and renamed TANF (Temporary Assistance to Needy Families) in 1996, the beneficiaries of which are, once again, mainly women. This social welfare programme has, for a long time, acted as a safety net against unemployment for poor jobless women, providing them with income support. The 1996 reform, however, tightened up conditions for accessing the regime and thus undermined its role vis-à-vis this particularly vulnerable group. Those women, in particular, who have come to the end of the five years of assistance to which they are entitled, and who find themselves without a job, are usually unable to meet the financial eligibility criteria for unemployment benefit, because of their low past earnings and intermittent employment record (Boushey *et al.*, 2003).

Because of the difficulties in accessing this regime, those people most at risk of unemployment are increasingly addressing claims to the Social Security Disability Insurance scheme instead. It is striking, for example, that the number of claims put to this programme increases or decreases

in line with the unemployment rate, especially since the 1980s, when the disability insurance programme made its eligibility criteria more flexible (Autor & Dugan, 2006). The scheme also has the advantage of opening up access to the Medicare health insurance regime for older people, whereas the unemployed, even those receiving benefit, have generally lost this entitlement at the same time as their job.

Resistance to reform despite the crisis

The unemployment benefit system has never been the object of large-scale reforms at federal level. Neither its structure nor the principles on which it is based have ever been significantly questioned. One reason for this is probably the low cost of this programme compared to other social programmes such as Medicare or the state pension scheme. Another is the fact that the unemployed are particularly poor at lobbying members of Congress, and that the trade unions have never thrown their weight behind the fight to modernise the system, since they are able to negotiate top-up benefits for their members during company collective bargaining sessions.

The system has, however, come under fire from many economists. During the 1990s, Martin Feldstein, Chairman of the Council of Economic Advisers to President Reagan at the beginning of the 1980s, and known for his arguments in favour of privatising the social security system, proposed the abolition of the current system, based as it is on modulated employer contributions, and seen by him as ineffective and liable to affect the reservation wage of the unemployed. He suggested that it be replaced by personal savings accounts, to be used to cover the temporary risk of unemployment (Feldstein & Altman, 1998). The current crisis, which officially struck the US economy from December 2007, and which has resulted in a rapid increase in the unemployment rate, has clearly altered the terms of the debate. At the end of 2008, Congress voted twice to activate the Emergency Unemployment Compensation programme, designed to come into play in the event of recession. The adoption of this programme meant that those people whose entitlement to benefit had run out were entitled to firstly a further thirteen weeks, then another twenty. However, as the crisis worsened, and the repeated lowering of interest rates by the Federal Reserve was seen to fail, a newly installed President Obama proposed a budgetary recovery plan, the American Recovery and Reinvestment Act, on a scale (\$787 billion) unprecedented

since the Second World War. This plan was adopted by Congress in February 2009.

One notable feature was a boosting of the assistance to be given to the unemployed. This improvement took various forms: a \$25 increase in the amount of weekly benefit; a further extension to the period for receipt of benefit, starting at twenty extra weeks and reaching thirty-three extra weeks in certain cases⁹; and assistance to states to allow them to improve their coverage of workers most at risk of unemployment (part-time and poorly paid workers¹⁰). The Trade Adjustment Assistance programme, for workers particularly affected by globalisation, was extended to workers in service sectors, who find themselves increasingly unprotected, and a state subsidy was granted to workers losing their jobs, enabling them to pay 65% of their health insurance premiums for a nine month period, under the health coverage provided by their former employer.

The recovery plan, however, is struggling to achieve its expected effects on the labour market, and the unemployment rate is still getting worse, having reached 9.8% in September 2009. Ten or so states have refused to implement the reforms required in order to qualify for federal assistance to extend unemployment insurance to part-time and low-paid workers, for fear of having to raise taxes when this aid is no longer available after 2011. Other states have not yet received all the funds available, since their reform process is not completed. There has in fact been no other measure in the recovery plan more controversial than the assistance given to states to modernise their unemployment insurance regime. The controversy shows the extent to which the ideas behind and founding principles of this system, dating back to the New Deal, still resonate and how they have been able to withstand economic pressures. Unless the crisis deepens still further, it is unlikely that the unemployment benefit regime will undergo many major changes. The system has always been effective, as planned, as a countercyclical force

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9. A twenty week extension was granted to all unemployed people receiving benefit, plus thirteen further weeks to those living in states where the unemployment rate had reached 6.5%.
 10. The reference period used by the states to assess job-seeker earnings tends to omit the period of work just before the person becomes unemployed (three to six months, depending on the case). Although several states have reconsidered this policy, more than half had not done so before the plan came into force. Moreover, the states have, over the years, gradually tightened up the eligibility criteria for unemployment benefit, thus competing with each other to attract and retain businesses on their territory. This is an unfortunate effect of the decentralised structure of the unemployment insurance system, and of the absence of minimum criteria set by the federal government.

during periods of economic recession, backed up where necessary by the voting through of emergency measures. Up until now, it must be said, no more has been required of it.

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