Beware the “Insurance Model”: Cautionary Tales from Canada’s Employment Insurance Plan

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Introduction & Context

• Continuing global discussions about “reform” of income security

• Various motives:
  - Fiscal constraint
  - Issues of “incentives” & “moral hazard”
  - Growing poverty, inequality in most countries
  - Challenges of precarious work
  - “Wedge politics”

• GFC has increased the urgency

• Reference to the “Canadian model”
Overview

1. Stylized facts of Canada’s labour market
2. Introduction to Canadian system.
   • “Employment Insurance” (EI)
3. Discussion of problems and challenges.
4. What are “insurance principles,” anyway?
Participation Rate

Percent of Working Age Population

Provincial Unemployment Rates

Percent of Labour Force

West

BC
Alta
Sask
Man
Ont
Que
NB
NS
PEI
Nfld
AVG
CDA

East

Nfld
AVG
CDA
Canada/US Unemployment Rates

Percent of Labour Force

Canada

U.S.
First Principles: The Goals of Unemployment Benefits

• Replace income lost due to loss of employment
• Prevent individual / social costs resulting from unprotected unemployment
  - Loss of accumulated assets
  - Family disruption / damage
  - Broader social costs (crime, depression)
• Alter balance of power within workplace
  - Compensation
  - Workplace intensity
Canadian EI: Basics

• Income replacement scheme for involuntary unemployed
• Designed to protect ("insure") income up to a threshold (average industrial wage = $43,200 per year; indexed)
• Replaces 55% of pre-layoff pay
• Collects premiums from employees and employers
• Special benefits available for special circumstances of joblessness
Canadian EI: Premiums

- Set annually by Canadian Employment Insurance Financing Board (CEIFB) to cover expected benefit payouts
- Universal & compulsory, from 1st hour of work
- Current employee premium: $1.73/$100
- Current employer premium: $2.42/$100
- Employer/Employee Ratio 1.4:1
  - Reflects employer “responsibility” for joblessness
- Premium capped at threshold ($43,200)
  - Maximum $750 employee / $1050 employer
- Premiums effectively paid into government general revenue
Canadian EI: Regular Benefits

- Equal to 55% pre-layoff weekly income
- Capped at 55% of threshold
  - 55% of $43,200 = $457 / week (indexed)
- Average benefit is lower: $350 / week
- 2-week waiting period before benefits begin
- No benefits for quits/dismissals
  - “deserving” unemployed only!
- Benefits last 19-50 weeks, depending on region
Qualifying for Regular Benefits

• “Hours system”
• Access to regular benefit requires having worked a minimum threshold of hours in previous 52 weeks (or since last EI benefit claim)
• Hours threshold varies from 420-910 hours, depending on:
  - Region (unemployment rate)
  - Labour force history (new entrants)
  - Previous claims (“repeat users”)
Canadian EI: Special Benefits

- Provided to individuals without work for other “legitimate” reasons
- Also paid at 55% of previous weekly income, to same maximum, same qualifying hours
- Maternal: 15 weeks max.
- Parental: 35 weeks max. (shared)
- Sickness: 15 weeks max.
- Compassionate (caring for dying): 6 weeks max.
- Fishery benefits: 26 weeks max., special qualifying terms
- Self-employed can opt in
History of Unemployment Insurance in Canada

• 1930s: Debate, but no action
  - Constitutional issue (federal-provincial)
• 1940: Unemployment Insurance Act
  - National system (constitutional change)
  - Fund run by independent Commission
  - Excluded many sectors (seasonal, resource, teachers); covered 42% of labour force
  - Tripartite contributions
  - 52 weeks benefit
History of Unemployment Insurance in Canada (cont’d)

• 1955: Overhaul
  - Include seasonal work; cover 75% L force
  - Reduce benefit duration to 36 weeks

• 1971: Modern UI is born
  - Virtually universal (96% of L force)
  - Qualify with 8 weeks work in last 52
  - Maximum benefit restored to 52 weeks
  - 75% pre-layoff wage replacement
History of Unemployment Insurance in Canada (cont’d)

- 1970s to 1990s: Whittling away at UI
  - Wage replacement cut 4 times (55% by 1994)
  - Tighter qualifications
  - New clawback for high-income UI recipients
  - 1990: Government contributions abolished (though still funder of last resort)
  - 1993: Quits and dismissals disqualified

  - New “hours system” for qualifying
  - Penalties imposed for repeat users

- 2008: New governance structure (CEIFB)
Governance System

• **EI Commission (tripartite)**
  - Four members
  - Includes one worker rep, one employer rep
  - Mostly governs appeals

• **CEIFB**
  - Sets premiums annually on cost-recovery basis
  - Manages a nominally independent “account” (still integrated with general revenues)
  - Response to criticism of fiscal abuse 1997 through 2007 (cumulative $55 billion surpluses)
  - Starts with $2 billion cushion
  - Premiums can change only 15 cents per year
Other Applications

- **Training programs**
  - In general, students cannot collect EI
  - Under special programs, displaced workers can be funded for retraining
  - Stricter hurdles (including family means test)

- **Work-sharing**
  - EI will subsidize temporary job-sharing as alternative to lay-offs

- **Other forms of “active labour market policy” or job-retention prohibited**
EI: Regional Issues

• Canada demonstrates very uneven development across regions
  - Peripheral areas: more dependence on resources, seasonal work, lower incomes

• Regional issues were important to the politics of UI reform in 1990s
  - Though regional inequality continues

• Regional qualifying standards and benefit duration still imposed

• Core regions cross-subsidize peripheral regions
  - Benefit accessibility lowest in core regions
Fiscal Balances

• Tightening of benefit accessibility in 1990s, combined with falling unemployment, produced large surpluses
• These subsidized other fiscal priorities
  - Deficit reduction exercise of 1990s
• Now program is supposed to be self-financing only
  - Government still the backstop
  - $55 billion surplus “disappeared”
• Recession means deficits ($6 b / year)
• Financing mechanism may be pro-cyclical
  - Increasing premium rates during prolonged recessions
Problems of Canadian EI: Benefit Accessibility

• Tighter qualifying rules (reinforced by the hours system) resulted in sharp decline in benefit recipience among unemployed
• Cut in half from 85% initially, to 40-45% by late 2000s
• This excludes “unreported” unemployed
• Even in latest recession, most unemployed received no benefits
Problems of Canadian EI: Precarious Work

• Growth of precarious work in various forms:
  - Part-time
  - Self-employment
  - Temporary / contract / agency

• More difficult to qualify for EI
  - Self-employed cannot (regular)

• Gendered impact

• Disproportionate impact on visible minorities
Benefit Recipiency by Gender

- Men: 50%
- Women: 40%

Percent of Unemployed: 35% to 55%
Precarious Incomes

Average Weekly Earnings

Permanent

Temporary
Problems of Canadian EI: Benefit Adequacy

- Principle of scaled benefits
- Provides protection to middle-class workers
- Level of benefits is low for low-income & precarious workers
- Example: Part-time workers
  - Average weekly income = $275
  - EI benefit would be $150 / week *(IF they qualified!)*
  - They would be better off under a flat-rate system
Average Benefit Replacement

Percent of Average Earnings


Percent of Average Earnings

30% 35% 40% 45% 50%
Problems of Canadian EI: Funding Mechanism

- **Capped payroll tax is regressive**
  - Trade-off: produces “entitlement” to a progressive benefit
  - BUT: access to the benefit was uncertain

- **Cost-recovery funding model is pro-cyclical**
  - Destabilizing macroeconomic effects
Problems of Canadian EI: Active Labour Market Policy

- EI program has not been used actively to facilitate job retention and active adjustment
EI in the GFC

• Modest rebound in coverage
  - Newly laid-off longer-term workers
• Most unemployed still excluded from benefits
• Modest temporary expansion of benefits
  - Extra 5 weeks in certain regions for certain workers
• EI fund tips back into deficit
  - $2 billion CEIFB cushion gone in 4 months
  - Coming increase in premiums
Proposals for Reform

• Labour movement / social advocates:
  - Harmonize, reduce qualifying hours (to 360)
  - Increase benefit replacement to 60% of best 12 weeks
  - More pro-active uses for training and job retention
  - Higher premiums

• Business advocates:
  - Eliminate regional preferences; harmonize at the stricter criteria
Evaluation

• **Canadian system contains many positive features**
  - Scaled benefits offer some protection, security for middle-class workers
  - Special benefits are innovative, beneficial

• **Canadian system reflects several failures**
  - Principle of “entitlement” is desirable, but has not been achieved
  - Benefits inadequate for many (esp. low-income)
  - Fiscal abuse by governments
  - Pro-cyclicality of cost-recovery financing
What are “Insurance Principles” Anyway?
... and should N.Z. follow them?

• Scaled benefit?
  - If adequate for low-income ✓
  - If access to benefits is reliable

• Premium-style funding?
  - Regressive distributional effect
  - May alter political “buy-in” ?

• Self-financing?
  - Introduced pro-cyclicality ×
  - Government is always funder of last resort
What are “Insurance Principles” Anyway? ... and should N.Z. follow them?

• “Entitlement” to benefit?
  - Less stigma

• Experience rating?
  - Higher premiums / restricted benefits
  - Loses social pooling of risk

• Incentive to assist return to work?
  - ALMP aspects of EI have been minimal

• Exclude benefits to cut cost?
  - Prelude to privatization?
Conclusion

• Whatever you call it, unemployment benefits are a social program

• Canada’s “insurance” model does not really incorporate “insurance principles”
  - Though some aspects of the program are positive & progressive

• Whatever you call it, there will be an ongoing conflict of interest over the provision of unemployment benefits
  - Workers want more
  - Employers want less
Beware the “Insurance Model”:

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