Insight

Unemployment Insurance in the President's FY 2016 Budget

BEN GITIS | FEBRUARY 2, 2015

This week the president unveiled his proposed budget for fiscal year 2016. Many of the president's labor market policy recommendations are ones we have heard before: raise the minimum wage, encourage paid sick leave, expand paid maternity leave, and enhance worker protections. One new proposal, however, is a significant reform of the Unemployment Insurance system. The President proposes to replace the current Extended Benefits (EB) program with a new one that is entirely federally funded and more than doubles the program's maximum duration of benefits from 20 weeks to 52 weeks.

Currently, regular Unemployment Compensation (UC) typically provides unemployed workers with benefits for up to 26 weeks. However, if a state's unemployment rate increases to a certain level, the state must provide an additional 13 or 20 weeks of benefits through the EB program. Half of the funding for EB comes from state governments and the other half comes from the federal government. Regular UC and EB are both permanent programs, so under current law in times of severe economic hardship, unemployed workers may be able to receive up to 46 weeks of unemployment benefits. Moreover, up until the end of 2013, additional weeks of benefits were available through the Emergency Unemployment Compensation Act of 2008 (EUC08). Between all three programs benefits were available for up to 99 weeks.

While Congress allowed EUC08 to expire at the end of 2013, the president hopes to replace temporary emergency unemployment benefits programs altogether. The president proposes to replace the current EB program with a new 100 percent federally funded permanent EB program that provides additional benefits for up 52 weeks. The new EB program would provide an additional 13 weeks of benefits each time a state unemployment rate reaches 6.5 percent, 7.5 percent, 8.5 percent, and 9.5 percent. As a result, between regular UC benefits and the new EB program, benefits would be available for up to 78 weeks during a severe recession. The President's Office of Management and Budget estimates that this reform would increase the federal deficit by $49.2 billion over ten years.

Unfortunately, it appears that the White House did not learn any lessons when EUC08 expired at the end of 2013. Evidence consistently suggests that extending the duration of unemployment benefits has a negative side effect of increasing unemployment even further. Increasing the duration of unemployment insurance increases the relative value of not working and as a result puts upward pressure on market wages. This in turn decreases employers' willingness to hire. AAF found that the extensions in unemployment benefit duration elevated national unemployment throughout recession, increasing the quarterly unemployment rate by as much as 1.3 percentage points and keeping almost 2 million people from finding jobs.

Additionally, EUC08's expiration in 2013 provided a natural experiment for how the labor market would react to reducing the duration of unemployment benefits. So far, the evidence is clear. Reducing the duration of benefits fueled the strong labor market growth we witnessed in 2014. Once benefit durations went back to normal, job creation increased, the unemployment rate fell, and job openings and hiring increased. Researchers also found that in 2014 1.8 million jobs were created due to EUC08's expiration, accounting for 61 percent of all jobs added last year.

Today, one of the government's top labor market priorities should be to do no harm. However, the President's proposal to reform EB could significantly harm job creation and increase unemployment. As evidenced by the labor market's growth in 2014, permanently extending the maximum duration of unemployment benefits to 78 weeks is the last thing this nation needs.