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Filling the Holes in Family and Business Budgets: Unemployment Benefits and Work Sharing in the Time of Pandemics

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We are in the midst of a multi-faceted health and economic crisis. At a basic level, to successfully deal with the COVID-19 pandemic requires social distancing, lockdowns, or quarantines which all create a temporary but steep decline in economic activity. This reduction in economic activity can create great pains for many workers and families, and also lead to business failures when employers cannot afford to weather the storm. We want to prevent businesses failures, and want to help preserve the matches between workers and employers—as these are costly to recreate. In addition, the reduction in earnings and demand can prolong the downturn through induced reduction in aggregate demand which may stretch considerably longer than the duration of social distancing. Therefore, a key goal of fiscal policy right now needs to help plug the hole in family and business balance sheets and help them stay afloat.

The good news is that there are policy levers at our disposal to help with this. Already, we have seen governments of Denmark, Belgium, France, Germany, New Zealand and United Kingdom and others announce variants of plans to do this. Our ability to implement successful policies depend on the institutional features and existing programs that are in place. In this policy brief, I propose using the existing Unemployment Insurance (UI) system in the United States to provide relief to families and businesses. Here is the short of it—we need to (temporarily) convert the UI from a system that provides partial assistance to some jobseekers while they look for a job to a funding system that helps (1) preserve jobs through job sharing, (2) provide nearly full compensation for lost hours for those who see reduction in hours, and (3) provide nearly full compensation for lost earnings for those on layoffs, with the goal of making most of these layoffs temporary ("furloughs") which allows workers to stay formally employed. And all of this needs to be paid for by the federal government. To put it simply, instead of UI being a payroll tax financed vehicle to help workers modestly while encouraging them to look for work, we want it to (temporarily) become a fully federally financed vehicle allowing workers to stay at home and companies to not go bankrupt.

UI is not the only vehicle to do something along these lines. A recent proposal by Saez. and Zucman would create a different mechanism to compensate businesses for demand loss.[1] This is a smart proposal we should seriously look at. Similarly, Hubbard and Strain propose a loan to small and medium size businesses that would convert to a grant if employers do not lay off workers.[2] At the same time, in my assessment, the UI system is up-and-running already here in the US, and we have all of the ingredients (including work sharing) in place for use. What we need to do is to change the parameters substantially, and (like we did during the Great

Recession) fund it using federal dollars.

Here I lay out the key changes we need to put in place to obtain this temporary transformation, beginning with making UI generous enough to actually support workers to weather this storm at a time they cannot be expected to find a job. Next, I talk about expanding on the work-sharing component to keep workers on the payroll.

This is not meant to be a comprehensive economic plan to deal with the pandemic. There are many other steps. This includes shoring up paid sick and family leave, strengthening safety net programs like SNAP ("food stamps"), transfer funds state and local governments, and also additional stimulus measure to boost aggregate demand when the social-distancing period ends. However, helping workers and businesses directly harmed by the pandemic and the necessary public health response is the most important place to start.

Making UI cover full (or nearly full) paychecks

First, we need to substantially reduce *eligibility* requirements to help people access UI. Most importantly, we need to drop the requirements of a one week waiting period, and the requirement to be actively searching for a job. In addition, we need to reduce the past earnings requirement that keeps many workers with lower hours or tenure from qualifying for UI benefits. Many low-wage workers with limited hours just do not have sufficient past hours in the "base period" to qualify for UI. Allowing all workers who lost their jobs (not just those who are technically "laid off" as opposed to fired) can also help. And unlike the current system, the crisis response should also allow self-employed workers, including those in the gig economy, to apply. These changes can go a long way in making sure people affected by this downturn can actually access the UI system. While typically only around a quarter of unemployed workers in the US actually receive UI, the goal should be to move this much closer to one hundred percent.

Second, need to make UI much more generous to fill paychecks of people who are temporarily out of a job or face cuts in hours and earnings. We can do that via increasing the *replacement rates* for those who are laid off (temporarily or permanently). Replacement rates refer to the share of your normal income that you receive as UI benefits. These typically range between 33 and 55 percent across states. But there are also maximum benefit caps that vary considerably across states. So, if the replacement rate is 50% and the maximum weekly benefit is $500, and your usual earnings is 1500, you will actually receive $500/$1500 = 1/3 of your usual earnings replaced. My proposal would start with moving to a replacement rate of at least 75% and raising the cap on weekly benefits to $1,500. The goal is to cover much of the paychecks of most workers who are laid off.

In normal times, the concern with having a very high replacement rate is that it discourages job search as people take advantage of the generous benefits instead of looking harder. This is a reasonable concern in normal times. But this is not the concern now – we don't really expect many of those laid off to be able to find jobs in this environment. Indeed, ideally most of those laid off will be so only temporarily, and will be called back once the pandemic subsides and the recovery begins. Therefore, in this case, providing a generous replacement rate of at least 75 percent (better perhaps at 80 or 85 percent) is a reasonable strategy that will get money in the hands of the people who are most strongly hurt by the crisis. This recognizes that the problem is not to help the unemployed along while they look for a job (which they cannot do very effectively right now) but rather to fill the holes in their budgets during this temporary pandemic.

Third, we need to help the currently unemployed who will have a hard time finding jobs by extending the *maximum benefit duration*. In normal times, workers are typically eligible for 26 weeks of UI. At the peak of the Great Recession, this was extended to as much as 99 weeks. We don't expect the pandemic related downturn to last anywhere near as long as the Great Recession. However, those who were unemployed even prior to the shock cannot be expected to find a job very easily. If someone has been unemployed for 25 weeks, we don't want their benefits to run out next week because it's going to be very hard to find a job right now. For this reason, I suggest that we expand the maximum benefit duration to 52 weeks immediately to avoid loss in benefits.

Helping keep workers on payroll

When it comes to layoffs, the goal should be to incentivize temporary layoffs (or "furloughs") which keeps workers on payroll and allows workers to return easily. This also allows employees to potentially access some of their benefits. What this means is that the employer retains the worker while the federal government is replacing (much of) their earnings during a time where the government has essentially forced many workers to not be at work in order to fight a pandemic. Not all employers may use furlough, but making this option easily available and attractive (via a much higher replacement rate) will help both workers and businesses.

Another avenue for employers to keep their workers on payroll is through work-sharing. For many employers considering cutting back on employment due to social distancing measures, work sharing measures can help keep workers working but for less hours, with the government paying for much of the lost hours. Essentially, it's the government paying workers to stay home because doing so is a public health benefit.

The best way to do this in our current environment is using the work-sharing provisions within the UI system. Here's the basic idea. Imagine you're a business owner and your employees can work remotely. However, because of lost demand, you can't afford to keep all your workers on payroll full time and are considering reducing total work hours by 30. You could lay off 30% of your workers, or you could cut hours. An alternative is if the government steps in and says, lower your hours by 30% for your workers, don't lay anyone off, and we will pick up (much of) the tab. That's exactly what work sharing does. This option may also be attractive to businesses where workers can work remotely, but the slowdown in the economy has reduced revenues substantially. Work-sharing has worked well in other countries, especially Germany during the last recession.[3] It's no wonder that Germany has announced plans to use work sharing to deal with the COVID-19 crisis.

Currently, 27 states in the US have work-sharing provisions. Under my plan, the federal government would require all states to offer it. Moreover, and equally importantly, it would provide and pay for much higher wage replacement for lost hours (perhaps around 90-95%). Why is this important? First, because it makes sure workers' paychecks are being sufficiently secured. It's also costly for incumbent workers (who would not have lost a job) to see a pay cut. Employers want to minimize that pay cut as much as possible, as pay reductions to incumbent workers can reduce morale and lead best workers to leave. Indeed, too much of a wage reduction for incumbent workers would likely lead employers to not participate in rent sharing. In addition, the somewhat higher replacement rate provides an incentive to employers to use work sharing over temporary layoffs. The rationale for that is we want to incentivize employers to keep workers not only on their payroll but economically engaged if it meets economic and health objectives (e.g., remote work). This can help facilitate the recovery after social distancing ends by preventing depreciation of firm-specific skills.

Some employers may not participate in work sharing and may cut workers' hours. To protect workers against this, and to help workers stick around at their jobs, we can boost the partial UI benefits. This program allows workers with an involuntary reduction in. hours to receive partial benefits. However, as it is structured, a worker who saw her hours cut by 50% would receive little or no benefits in most cases. But we can easily modify this to ensure that those workers seeing reduction in hours can keep much of their earnings intact.

Federal funding

The final part of this is funding. In normal times, UI is funded using employer payroll taxes, and using "experience rating" which means those employers whose workers end up using UI more see hike in what they pay. However, in times of economic crises, the federal government usually steps in.

Under my proposal, the federal government would re-start the Emergency Unemployment Compensation (EUC) system, the key vehicle it used during the Great Recession to fund the dramatic increase in UI maximum benefit duration to as much as 99 weeks during that period.

In particular, all additional UI expenditures should be In particular, all additional UI expenditures should be borne by the federal government, which is uniquely advantaged in doing so. Moreover, it's important that businesses accessing these emergency UI provisions are not penalized through increased experience rating;

so there would be a experience rating holiday until the crisis passes. (Experience rating means that in normal times, businesses with a lot of workers using UI have to pay more in taxes; right now we do not want to do that.)

At the end of the day, we need a way for the federal government to pay workers to stay at home and get a paycheck. First and foremost, this helps our public health objectives of keeping non-essential workers home and reduce the risk of transmission. Second, it helps workers most at need. Third, it not only helps workers, but also helps reduce the burden on employers. By removing a large part of the costs facing an employer to the public sector, it can make the difference when it comes to an employer deciding to shut down or not. The federal government can help by temporarily picking up the tab when it comes to the paycheck.

The size of this program will depend critically on the size of the downturn and the exact parameters we choose—replacement rates, benefit caps, and so on. Assuming an average replacement rate of 85 percent, and a maximum weekly benefit cap of $1500, I estimate that the average UI-eligible earnings of workers would be around $910, and that their weekly benefit amount would be around $773. To put this in perspective, the current average weekly UI benefit is around $350, so this would likely more than double the take home pay for those on UI.[4] What would this UI expansion cost? Consider a hypothetical scenario where the unemployment rate is sharply elevated to around 20 percent for around six months and assume that with more comprehensive coverage, 75 percent of the unemployed receive benefits. The combination of comprehensiveness and generosity will mean that expenses grow by roughly $365 billion. The higher replacement rate and higher eligibility both make important contributions to this increase.

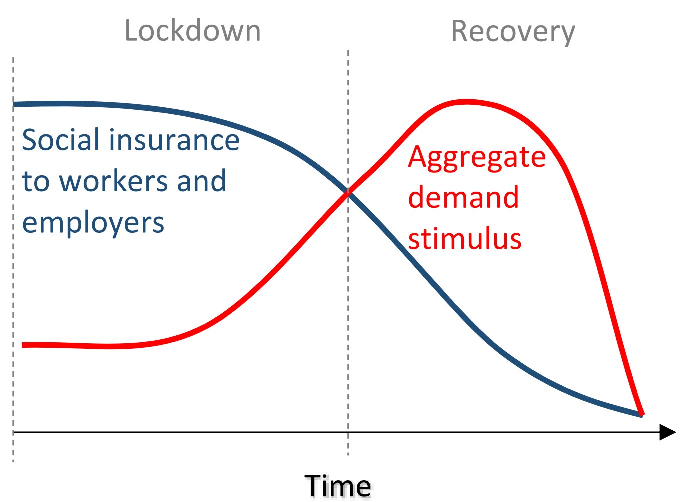
Of course, there are many unknowns about the depth and duration of this downturn. But the key point is that if the size of the hole is bigger than we thought, we should want to spend more to plug it. And UI spending is extremely well targeted for both social insurance and aggregate demand purposes.

What's not here?

To be clear, this is not the only piece of fiscal policy we need to enact. We will need additional provisions to help employers (like no-interest loans proposed by Ozimek and Lettieri[5] or subsidies for rent and other non-labor costs), especially in hard hit sectors. We will need to strengthen the safety net for low income families, especially through SNAP. The federal government will also need to help support state and local governments' finances to avoid reduction in spending and employment that can prolong the downturn.

And finally, we need to plan for a big consumption increase once the social distancing is removed to help supercharge a recovery. As the figure below suggests, we want to move from social insurance to stimulus over time.

Figure 1 What the ideal balance of fiscal policy should look like.



This means there is definitely a scope for general stimulus policies (like a check for several thousand dollars to each family as pushed for by proponents from both sides of the isle). This will set us up for a faster recovery once we are in that phase (and it may take some time for those checks to arrive). But it is critical that we deal with the balance sheets of households and businesses who are most severely hit by the current crisis.

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Endnotes

1 Saez, Emmanuel and Gabriel Zucman. 2020. "Keeping Business Alive: The Government as Buyer of Last Resort" EfIP Policy brief # 20.

2 Hubbard, Glen and Micahel Strain. 2020. "A Business Fiscal Response to the Covid-19 Recession" AEI Report.

3 Hassett, Kevin and Michael Stang. 2014. "Worksharing and long-term unemployment" AEI Report.

4 https://www.usatoday.com/story/money/2019/06/02/best-and-worst-states-to-be-unemployed/39526585/

5 https://eig.org/news/main-street-rescue-and-resiliency-program