CALEDON INSTITUTE OF SOCIAL POLICY

Fixing the Hole in EI: Temporary Income Assistance for the Unemployed

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Introduction

In Canada today there are two main programs providing financial assistance to unemployed adults of working age: Employment Insurance and social assistance (better known as welfare). Each of these programs serves important objectives, but there is a critical gap between them.

Many workers who have paid Employment Insurance premiums find themselves ineligible for benefits upon becoming unemployed. Many other workers are not even able to participate in and pay premiums to the Employment Insurance program in the first place. When unemployed Canadians who cannot collect Employment Insurance find themselves in dire financial straits, having used up all their savings and borrowed as much as they can from family and friends, welfare is their only alternative.

But welfare rates are low in every province and territory, especially for single employable recipients. Welfare is inadequate to maintain basic living standards during periods of unemployment for many of the jobless, even when all possible 'extras' are cut out. To become eligible for welfare, applicants must exhaust their financial assets, including RRSPs, as well as non-financial assets – excepting only an older car, a home and personal possessions, such as clothing. Further, the paternalistic requirements of welfare administration are inherently stigmatizing and draining of self-confidence and independence, as discussed at length elsewhere [e.g., Herd, Mitchell and Lightman 2005; Battle, Mendelson and Torjman 2006]. All of this makes it difficult both psychologically and materially for those who have to rely on welfare to bounce back into the economic mainstream. Yet welfare remains the only alternative today for unemployed workers who do not participate in or are otherwise ineligible for Employment Insurance.

Something is needed between Employment Insurance, with its relatively higher benefits but limited reach, and welfare, to which anyone in need can apply but only for inadequate benefits if in fact they are deemed eligible.

Proposals to fill the gap have commonly focused on loosening the entry and other rules for Employment Insurance [e.g., Vosko 2011]. While improved access to Employment Insurance would go some way to providing an alternative to welfare for some of the unemployed, we show in this paper that many other jobless Canadians would still be left in the cold. So we propose a new program to fill the gap that would remain between Employment Insurance and welfare, even were Employment Insurance to be somewhat enhanced.

This paper is organized in two parts. The first part is a discussion of why simply enhancing or modifying Employment Insurance could not fill the gap, at least while maintaining the integrity of that important program. We begin with a discussion of the existing Employment Insurance program – why was it set up as a social insurance; what can we reasonably expect it to do (and not do) in our income security system; and why do we need a social insurance? We then analyze who is not eligible for Employment Insurance and whether they could be covered. The next section of Part 1 discusses welfare and its relationship to unemployment. Part 2 sets out detailed designs for our proposed new program.[1]

Part 1: The Gap between Employment Insurance and Social Assistance

Why unemployment insurance?

We may define three archetypes for income security programs: universal, selective and social insurance. A universal program pays every person in a broad demographic group the same amount, regardless of their income or needs. A selective program pays a variable amount of benefit to eligible recipients according to some test of their level of income (known as an income-tested program) or their needs, assets and other resources (characterized as a needs-tested program). A social insurance program collects premiums from contributors and pays benefits more or less scaled to their contributions. Both universal and selective programs are usually financed through general revenue, while social insurance plans are typically funded primarily through premiums.

Of course, the real world is neither so simple nor clear cut. In reality, there are a thousand and one variations on these three archetypes, including many hybrids. Nevertheless, this typology provides a useful lens through which to understand the income security system and analyse the roles that different types of programs can and should play.

Canada established its national unemployment insurance program in the shadow of the 1930s depression. The new national program was set up in 1940 as a social insurance, and this was not a mere whimsy. The federal government encountered significant legal and jurisdictional barriers as a consequence of deciding on the social insurance model for its new unemployment assistance program.

The British Judicial Committee of the Privy Council, which then functioned as Canada's final court of appeal, ruled that social insurance was indeed a form of insurance, like private insurance, and thus was within provincial and not federal jurisdiction under the *British North America Act*. Consequently, an amendment to the *British North America Act* was deemed necessary to permit the national government to operate a contributory unemployment insurance program. (An amendment to the *British North America Act* is more or less equivalent to a Constitutional amendment today.) Although Quebec had originally objected to empowering the federal government to run a national unemployment insurance plan, a new Liberal government in Quebec granted its approval and the required amendment was duly passed in 1940 with the unanimous consent of the provinces.

In persevering to overcome these barriers, the governments of the day demonstrated their determination to deliver unemployment assistance as a social insurance. Ottawa and the provinces needed the new national program to be a social insurance because that type of income security program has several unique characteristics vital to meeting the objectives of unemployment assistance for most unemployed workers, and for the nation as a whole.

On the macro-level, a social insurance program can act as a counter-cyclical stabilizer by building up a fund when times are good and then drawing down the fund when times are bad. On the micro-level, a social insurance scheme creates a relationship between an individual's contributions and that person's potential benefits. Here we are interested in the micro-level features of unemployment insurance.

In a social insurance plan, it is generally possible to maintain an individual account of the amount contributed by or on behalf of each participant. Benefits may then in turn be paid out more or less proportionally to the total amount of premium paid by each participant, according to various formulae. This feature gives social insurance programs the capacity – unique among income security programs – explicitly to pay higher benefits to those who have higher incomes. (Tax deductions and exemptions also pay higher benefits in the form of income tax savings to those with higher incomes, but do so implicitly and without the widespread understanding of much of the public.) In addition, because social insurance benefits are financed mainly from premiums, there is likely less public resistance to higher levels of benefits than would be found in most income-tested or needs-related income security programs.

In contrast, a non-social insurance program will usually be funded from general revenue, making it impossible or at best hypothetical to maintain a record of individual contributions and to relate benefits directly to past contributions. In an income security program funded from general revenue, public acceptability typically demands that differences in benefits be based on criteria such as income or need wherein those with the least get the most. As well, these programs may encounter significant public resistance to higher benefit levels.

A social insurance type of program is therefore especially suitable when the objective is to provide continuity of living standards for those with modest or middle incomes, rather than the more limited objective of providing protection against deep poverty for those with the lowest incomes.

Historically, the reasons for adopting the social insurance model of unemployment insurance in 1940 were many and complex. But through the assorted legal barriers and political compromises, the provinces and the federal government arrived at a social insurance model that offered some financial protection from unemployment for the 'average' worker, not just a safety net for the destitute. And the model has remained sufficiently robust to survive for 70 years.

It is our contention that the original decision was correct. If Canadians want an unemployment insurance plan that allows the unemployed to maintain their standard of living at least for a short to medium term period of unemployment – which tangibly means keeping up mortgage and car payments, paying taxes, buying groceries and the other ongoing unavoidable expenses of everyday life – then unemployment protection designed as a social insurance makes good sense.

Better financial protection for the unemployed individual also has implications for the whole community. From the perspective of the overall economy, it is preferable to enable the unemployed to spring back quickly to work as the economy recovers from a downturn. If unemployed households are forced to begin stripping assets, such as selling homes and vehicles, this will reduce asset prices for everyone and inhibit economic recovery. As we have seen in the recent waves of house foreclosures in the United States, a neighbour's problem can very soon become a neighbour*hood*'s problem.

What unemployment insurance cannot do

While the social insurance model has advantages in respect of important objectives, it also has limitations. If unemployment benefits require premiums to be paid, then workers with little or no premiums collect little or no unemployment assistance. Yet, in a dynamic modern economy with a flexible labour market, there are many different forms of employment, and much entry and re-entry into the labour market. Immigrants, young people newly entering the labour market and re-entrants into the labour market will likely not be included at all in a contributory social insurance scheme because they cannot meet the work eligibility requirements.

The self-employed must also be excluded from an insurance-based unemployment program because of the difficulty of defining when exactly a self-employed person is unemployed – for example, is a self-employed consultant temporarily unemployed if she does not get a contract for two or three months? Osberg, Phipps and Erksy [1995] ask the same question prior to proceeding to a 'hypothetical' simulation: "Even though, for example, a self-employed economic consultant might in fact be working for weeks or months on a particular consulting contract, their payment is typically on an infrequent basis. One does wonder how it would be possible to accurately record the weeks of self-employment work effort which would qualify such individuals for UI (Unemployment Insurance, as Employment Insurance was then called] benefits, if UI coverage were extended." Is a small business owner unemployed if she sells her business and is seeking other opportunities for investment or for employment? In addition, how can the 'unemployed' self-employed be paid unemployment insurance benefits if contributors voluntarily leaving a job – who represented 17.9 percent of unemployed contributors in 2008[2] – are denied eligibility?

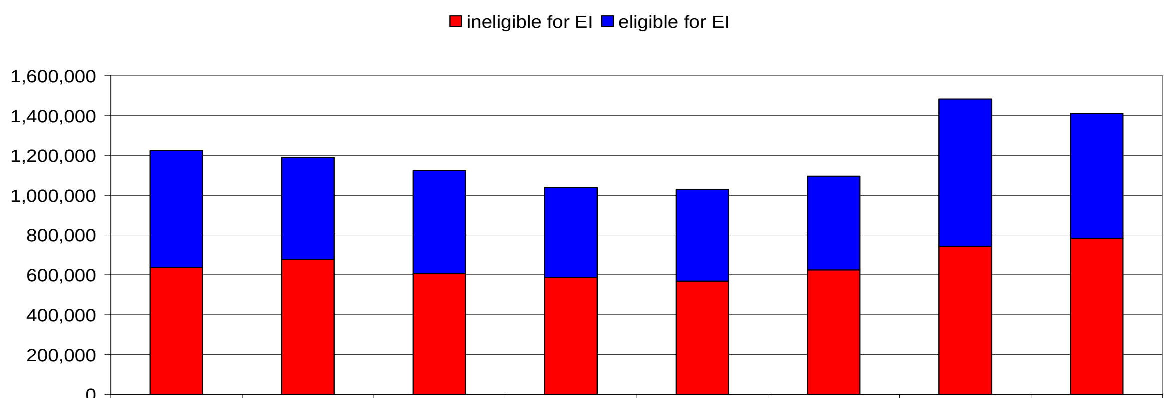
The tendency for the social insurance model to provide less protection for some groups has long been observed, as noted in Vosko [2011]. Vosko cites, for example, Schmid and Reissert [1996: 248]: "Just as older people tend to be better protected under insurance-based systems, the young are less well protected. Insurance-based systems are, therefore, biased towards protecting core workers (mostly male and elderly) over marginal workers (mostly young, female and casual)."

We concur fully with this observation regarding social insurance programs. The policy question is what to do about it. One strategy is to attempt to adjust the parameters of social insurance programs. An alternative or perhaps complementary strategy is to introduce non-social insurance programs that fill the gaps left by social insurance programs. The following sections argue that the former strategy has only limited capacity to reach those currently left out of the Employment Insurance program, or at least to do so without also undermining Employment Insurance. We then present an alternative strategy.

Who is ineligible for Employment Insurance?

Figure 1 shows the total number of unemployed in Canada and their eligibility status for regular[3] Employment Insurance benefits from 2003 through 2010. Unemployment was falling from 2003 to 2007, but with the economic downturn beginning in mid-2008 the unemployment rate rose and then increased substantially in 2009, decreasing only a little in 2010. In every year in this period, well over half a million unemployed Canadian workers were not eligible for Employment Insurance, with more than 600,000 ineligible in most years. In 2010, with higher unemployment levels for the last two years, 784,000 unemployed Canadians were not eligible for Employment Insurance.

Figure 1
Eligibility and ineligibility for
Employment Insurance 2003-2010



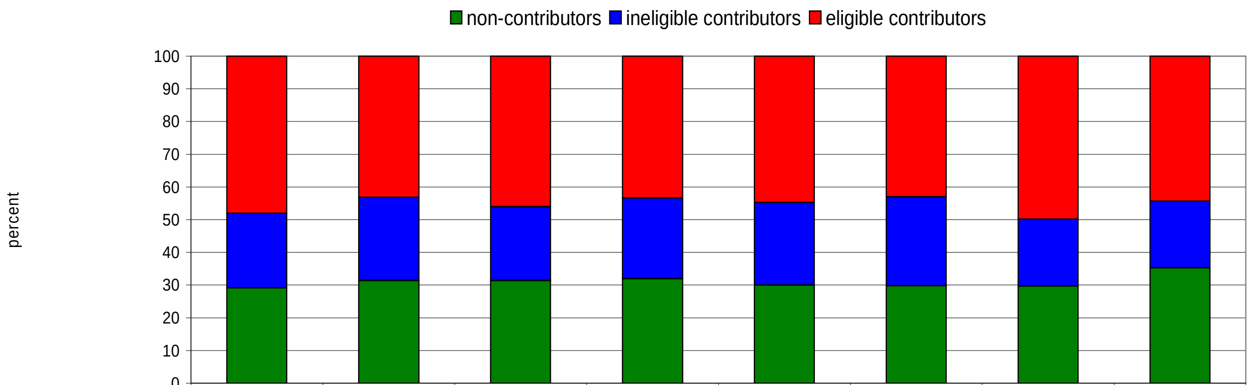
	2003	2004	2005	2006	2007	2008	2009	2010
eligible for EI	587,520	515,028	516,580	450,926	460,410	469,755	739,000	626,000
ineligible for EI	636,480	675,972	606,420	588,074	569,590	625,245	744,000	784,000
total	1,224,000	1,188,000	1,123,000	1,039,000	1,030,000	1,095,000	1,483,000	1,410,000

source: The Daily, 23 July 2009, 21 June 2010 and 27 June 2011, Statistics Canada

Figure 2 shows the *percentage* of unemployed who were eligible[4] and ineligible for regular Employment Insurance benefits in each year in the seven-year period 2003 through 2010. Figure 2 further displays ineligibility for Employment Insurance in two categories: those who were contributing participants in the Employment Insurance program (defined as having made at least one premium payment into Employment Insurance in the prior 12 months) but were in any case ineligible, and those who were non-contributors and consequently not eligible.

As can be seen on Figure 2, fewer than half of the unemployed have been eligible for regular Employment Insurance benefits since 2003. The share of the unemployed who are eligible for Employment Insurance declined from 48.0 percent of the unemployed in 2003 to 42.9 percent in 2008, but increased to 49.8 percent in 2009, falling again to 44.4 percent in 2010.

Figure 2
Percentage of the unemployed contributing and not contributing, eligible and ineligible for Employment Insurance, 2003-2010



	2003	2004	2005	2006	2007	2008	2009	2010
eligible contributors	48.0	43.1	46.0	43.4	44.7	42.9	49.8	44.4
ineligible contributors	22.9	25.5	22.6	24.6	25.3	27.2	20.4	20.3
non-contributors	29.1	31.4	31.4	32.0	30.0	29.9	29.7	35.3

source: The Daily, 23 July 2009, 21 June 2010 and 27 June 2011, Statistics Canada

There were no legislative changes affecting the eligibility of the unemployed from 2003 to 2008, so the decline in eligibility over this period was not caused by policy changes. During this whole period up to 2008, unemployment rates were falling. Consequently, entry requirements were increasing in most regions (those whose unemployment rates fell sufficiently) and this may have reduced the proportion of the unemployed in aggregate eligible for benefits. However, unemployment rates also fell in 2005 (from 7.2 percent in 2004 to 6.8 percent in 2005) so the increase in eligibility in that year would be an anomaly.

There were legislative changes in 2009 which temporarily lengthened the duration of benefits, but the rule changes in themselves did not reduce the number of hours required to be eligible for benefits or otherwise change entry requirements. Nevertheless, the automatic adjustment of entry requirements with higher rates of unemployment did result in a rapid reduction in the number of hours required for eligibility in most regions across Canada. Those changes, combined with the layoff of tens of thousands of full-time workers who had been steadily employed for many years, resulted in a large increase in the number of unemployed eligible for Employment Insurance benefits in 2009. Yet, despite this expansion of eligibility in 2009, eligible contributors remained only about half of the total unemployed.

By 2010, the increase in eligible contributors in 2009 had been entirely lost, accounted for by a substantial rise in the percentage of non-contributors among the unemployed. As we shall see below (Figure 4), this development is due to an increase in long-term unemployment as many more unemployed in 2010 were non-contributors due to being unemployed for the previous 12 months.

Ineligible unemployed may be further divided into those who are Employment Insurance contributors and those who are non-contributors. The former are ineligible because they do not meet the Employment Insurance qualifications for a regular benefit despite having contributed and being participants in the Employment Insurance scheme. The latter are not eligible because they were not participants in the first place.

Figure 2 shows that about 30 percent of the unemployed were non-contributors from 2003 through 2009, with very little fluctuation. The percentage of unemployed who are non-contributors has been remarkably stable, even through widely varying labour markets. Despite a huge increase in unemployment in 2009, the portion of non-contributors remained a constant 30 percent – the same as it was in 2006, with 400,000 fewer unemployed. Neither the rule changes in 2009 nor the automatic reductions in hours of work required for eligibility affected *non-contributors'* ability to participate in Employment Insurance and thereby become eligible for regular benefits. Since the percentage of non-contributors has remained constant through 2009 while the percentage of ineligible unemployed has been increasing, all of the change in the percentage of ineligible unemployed workers until 2010 was the result of variation in the share of eligible contributors – i.e., changes in the proportion of participants in the Employment Insurance program who are eligible upon becoming unemployed.

As noted above, in 2010 the number of non-contributors increased substantially for the first time. We will not know for a few years whether this augers a permanent change in the labour force, or whether the percentage of non-contributors will fall back to 30 percent if and when unemployment decreases.

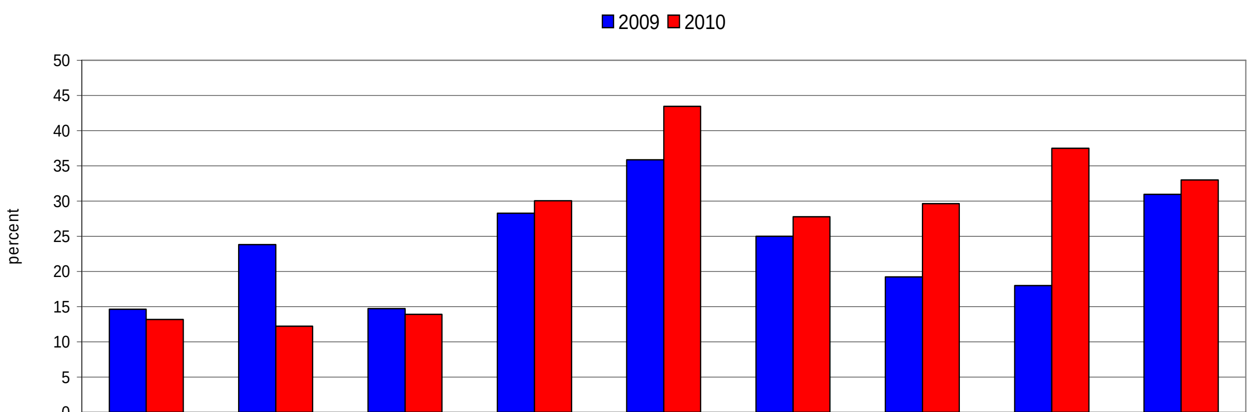
In sum: about 55 percent of the unemployed in Canada are currently ineligible for Employment Insurance. This is a lower figure than in the previous few years excepting 2009, when ineligibility had been nudging upwards close to 60 percent, possibly due to the effects of automatic adjustments in entry requirements as unemployment rates fell. Independent of any other long-term trend, until 2010 about 30 percent of all the unemployed (i.e., about 60 percent among the 50 percent of unemployed ineligible for Employment Insurance in 2009) were ineligible because they were not participants in the Employment Insurance system, having not paid any premiums in the previous 12 months. Non-contributors remained a stable 30 percent of the unemployed over the last several years until 2010, despite even the substantial changes in the labour market and consequently in Employment Insurance eligibility in 2009. We will not know for a few more years whether the percentage of ineligible among the unemployed will return to the 30 percent long-term trend or remain at the elevated level of 35 percent reached in 2010.

In the next sections we look more closely at each of the two categories of ineligible unemployed: those not participating in Employment Insurance and those who are participating but still ineligible.

Unemployed workers not participating (non-contributors) in Employment Insurance

Figure 3 shows the percentage of unemployed workers in each province (except PEI due to its inadequate sample size) who were non-contributors to Employment Insurance in 2009 and 2010. While the national average was 30 percent in 2009 and 35 percent in 2010, there are large differences among the provinces. Ontario, in particular, stands out with 36 percent and 43 percent of its unemployed being non-contributors to Employment Insurance in 2009 and 2010, respectively. In contrast, all of the Atlantic provinces had non-contributor rates in the low teens in 2010.

Figure 3
Percentage of non-contributors to Employment Insurance among the unemployed, by province, 2009 and 2010



	Nfld	NS	NB	Que	Ont	Man	Sask	AB	BC
2009	14.6	23.8	14.7	28.3	35.9	25.0	19.2	18.0	30.9
2010	13.2	12.2	13.9	30.0	43.5	27.8	29.6	37.5	33.0

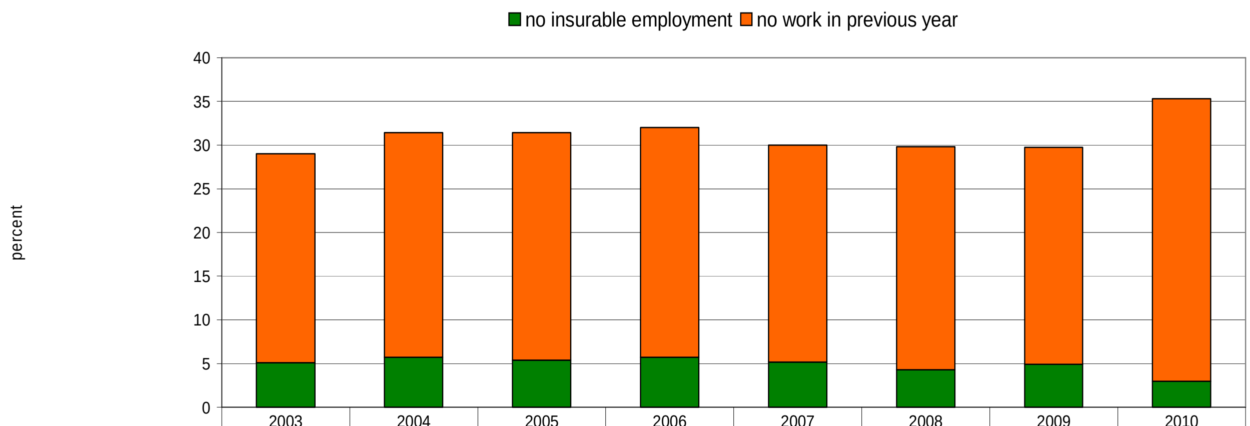
source: Statistics Canada The Daily, 21 June 2010, and 27 June 2010 Employment Insurance Coverage Survey

These are substantial differences among the provinces. Note that the regional variation in rules for Employment Insurance eligibility are not relevant to this group, as these are non-contributors and are not affected by variable entrance requirements or the number of weeks for which benefits are paid. Newfoundland’s percentage might be lower due to seasonal benefits, but this does not explain Alberta’s low rate in 2009 – nor its sizable jump in 2010. Whatever the explanation for the provincial differences, the much greater prevalence of non-contributors among Ontario’s unemployed must be one of the underlying explanations for relatively poor coverage of the unemployed by Employment Insurance in Ontario [Black and Shillington 2005].

In 2009, 84 percent of non-contributors reported having not worked for the previous 12 months (although actively engaged in the search for a job) and 16 percent reported having had no insurable earnings. Put another way, up to but not including 2010, of the approximately 30 percent of unemployed who were non-contributors, about 25 percent (370,000 in 2009) were non-contributors because they had not worked in the preceding year and 5 percent (74,000 in 2009) did not have insurable earnings, despite reporting having worked in the previous year. The

'25+5' percent split remained quite stable over the 2003-2009 period, as can be seen in Figure 4. In 2010, the share of non-contributors went up to 35 percent, and the share reporting not working in the previous year climbed to 32 percent from the more or less stable 25 percent of the previous seven years. It will be a few more years before we know whether this represents a permanent or temporary shift.

Figure 4
Percentage of unemployed not contributing to Employment Insurance, by reason for not contributing, 2003-2010



	2003	2004	2005	2006	2007	2008	2009	2010
no work in previous year	23.9	25.7	26.0	26.3	24.8	25.5	24.8	32.3
no insurable employment	5.1	5.7	5.4	5.7	5.2	4.3	4.9	3.0

source: The Daily, 23 July 2009, 21 June 2010 and 27 June 2011, Statistics Canada

As we have seen, over the period 2003 to 2009, the proportion of non-contributors among the unemployed appeared to be impervious to both fluctuations in the level of unemployment and easing the rules for eligibility among contributors – as seen in 2009, when automatic adjustments in the entry requirements had no effect on the proportion of non-contributors among the unemployed. In 2010, the percentage of non-contributors increased, rather than decreased, due to longer-term unemployment. Rule changes such as reducing entry requirements that are ordinarily contemplated to improve lack of coverage of Employment Insurance will therefore likely have no effect on improving coverage for non-contributors, who form the majority of those ineligible for Employment Insurance. To the extent that differential proportions of non-contributors explain differential Employment Insurance coverage among the provinces, loosening entry requirements and other rules will also have no impact on lessening these provincial variations.

Until 2009 (the year 2010 may be an anomaly due to the recession), roughly 5 percent of the unemployed report having been employed the previous year but with no insurable earnings. Presumably, bringing the self-employed into the Employment Insurance system would improve the coverage among this 5 percent of the unemployed, if it were possible to do so. However, as discussed previously, there are significant administrative barriers to including the self-employed in Employment Insurance. In a social insurance program such as the Canada Pension Plan, it is possible to include the self-employed because a person either meets the program's age requirement or not. There are stringent eligibility tests for Canada Pension Plan disability benefits. But there are no means to identify objectively when a self-employed person really is ‘unemployed’ in the same way as other workers. Indeed, there is no way to define ‘unemployment’ for the self-employed.

Attempting to include a group whose employment status is so nebulous is an invitation to mismanagement, rapidly escalating costs and abuse of the Employment Insurance program. It would also necessitate doing away with the requirement that unemployment be involuntary on the part of the employee in order to qualify for Employment Insurance. It is our view, therefore, that there is no mechanism to include the self-employed in Employment Insurance without undermining the whole program.

The recent voluntary inclusion of the self-employed in Employment Insurance for purposes of ‘special benefits’ is a case in point. Although the program does not make the self-employed eligible for regular benefits, it does allow them to opt into the program to become eligible for maternity, parental, sickness or compassionate care benefits. Of course, only those with a high likelihood of using the benefits will opt in (in insurance terms this is known as ‘adverse selection’), so the addition will undoubtedly be a net financial burden on Employment Insurance financing. But it will also be impossible to enforce rules. Will the Employment Insurance program police the parental leave program to ensure that the small business owner does not in fact go into work?

This extension of special benefits in the Employment Insurance program to the self-employed doubtless will have a minor impact on costs. Given the small size of special benefits for the self-employed, fraud and infractions will likely simply be ignored. But the extension of special benefits to the self-employed should not be taken as evidence that a much larger program for the self-employed of mandatory inclusion in Employment Insurance for regular benefits would be realistic.

Despite its support for the self-employed and its wish to create greater security for the self-employed, the Canadian Chamber of Commerce arrived at the same conclusion [2009: 8]:

> Self-employed workers are not insurable under the Employment Insurance Act for one key reason – “moral hazard” – the problem that arises from the fact that self-employed workers can control whether they accept work or create the conditions necessary for unemployment. Extending Employment Insurance benefits to the self-employed appears to contradict the original intent of the Employment Insurance Program – to provide insurance coverage against temporary unemployment through no fault of the individual worker. Program administrators would face the challenge of distinguishing between involuntary and voluntary unemployment among self-employed workers. The moral hazard problem is considered to be less serious in the case of special benefits (like maternity and paternal) since the conditions triggering these benefits provide Program administrators with greater control over access to them.

Unemployed workers participating in but not eligible for Employment Insurance

Figure 5 shows the percentage of unemployed workers who were participating in the Employment Insurance program (i.e., had made at least one premium payment in the previous 12 months), but were in any case ineligible. There are two categories of reasons for ineligibility: an invalid job separation (such as leaving voluntarily to return to school) and insufficient hours to qualify.

As can be seen, ineligible contributors were a gradually increasing proportion of the unemployed from 2005 to 2008 until the big increase in unemployment levels in 2009 and the consequent automatic loosening of entry requirements in Employment Insurance. In 2009, 20.5 percent of the unemployed were ineligible contributors. However, by 2010 the percentage of ineligible contributors had resumed its upward trend, following the trend line established from 2005 through 2008, to reach 31.4 percent in 2009. The 31.4 percent of the unemployed who were ineligible contributors in 2010 were the sum of 18.3 percent ineligible due to invalid job separation and 13.1 percent ineligible due to insufficient hours.

There has been very little variation over the 2003-2009 period in the percentage of unemployed contributing workers who were ineligible for Employment Insurance due to insufficient hours. In 2005, the highest proportion was ineligible for Employment Insurance due to insufficient hours – 10.5 percent of the unemployed. In 2009, the lowest proportion was ineligible, but this was only a little changed at 8.0 percent. The only big jump in those ineligible due to insufficient hours was in 2010 to 13.1 percent. It will be a few years before we know whether this higher percentage of contributors who find themselves ineligible due to insufficient hours is a new trend, or a reflection of the second year of relatively high unemployment.

Figure 5
Percentage of unemployed contributing to Employment Insurance but ineligible for benefits, by reason for ineligibility, 2003-2010

	2003	2004	2005	2006	2007	2008	2009	2010
invalid job separation	13.9	15.1	13.4	15.4	15.7	17.9	12.5	18.3
insufficient hours	9.1	10.5	9.2	9.1	9.6	9.3	8.0	13.1

source: The Daily, 23 July 2009, 21 June 2010 and 27 June 2011, Statistics Canada

Despite the surge in unemployment in 2009 and 2010 and the consequent less stringent entry requirements, the total range of change in eligibility due to insufficient hours amounted to only about 5 percentage points. This is evidence that reducing the hours of work required to qualify would not have a huge impact on eligibility, unless taken to extremes. Were the prior work requirements so diminished as to, say, reduce the number ruled ineligible by half, this would still increase eligibility only by about 6 to 7 percent of the unemployed at most in 2010, and by only 4 or 5 percent in most years. At the same time, such extreme lessening of work requirements would substantially alter the social insurance nature of the Employment Insurance program, effectively all but severing the connection between contributions and benefits.

The evidence overall suggests that there is little scope for improving Employment Insurance coverage through reducing hours of work required for eligibility. This conclusion accords with the views of Human Resources and Skills Development Canada as reported in Black and Shillington [2005] and as reported orally to these authors as well. According to officials at Human Resources and Social Development Canada, their internal models showed at that time that there would be little significant increase in the coverage of unemployed in Toronto were the entrance requirements lowered even to the lowest levels of all regions in Canada.

Social assistance

Although Employment Insurance and social assistance (better known as welfare) are the two main income security programs for working age adults in Canada, there has been little empirical research (i.e., research on what actually happens to people in the interaction of the two programs) on the relationship between the two programs. With only a few exception, the empirical studies have looked exclusively at the extent to which workers who have been collecting Employment Insurance benefits but have now run out of benefits (so-called exhaustees) enrol on welfare [e.g., Finnie et al. 2011]. However, this is only one piece and, as Finnie shows, a rather small piece of the inter-relationship between the two programs. As we have seen, many unemployed workers are not eligible for Employment Insurance to begin with, so the more fundamental question is where do these workers go if they are excluded from EI and in financial need?

The most detailed research not limited to the study of exhaustees was presented in two studies undertaken in the mid-1990s under the sponsorship of Human Resources Development Canada, following various reductions in what was then called Unemployment Insurance in 1993 – principally the exclusion of so-called 'voluntary quits.'

The first study – *Studies of the Interaction of UI and Welfare Using the COEP Dataset* – focused on the effects of reductions in Employment Insurance on takeup rates for welfare. The results were straightforward: a cut in Unemployment Insurance eligibility results in an increase in the number of welfare cases. The authors found:

> …a substantial February to May decline in UI take-up among VQs [Voluntary Quits] with little re-employment success and a coincidental rise in welfare take-up among the same

> group that was at least of equal magnitude and probably larger. This result was robust to conditioning on cross cohort differences in the interval between separation and the first interview and in other personal and economic variables. This suggests that for this group the Canadian UI and welfare programs may act as close substitutes, that the incentive and income distribution effects of Bill C-113 may have been mitigated by the availability of a substitute program, and that the examination of UI in isolation from other social programs is highly problematic [Browning, Jones and Kuhn 1995: 7].

The second empirical study looked at the flow of clients between Employment Insurance and welfare. *The Interaction of Unemployment Insurance and Social Assistance* used administrative data from what was then called Unemployment Insurance and welfare in British Columbia, New Brunswick, Newfoundland, Prince Edward Island and Alberta over the period 1986-1992. In essence, the study found that many people used both Unemployment Insurance and welfare, with some drawing welfare benefits before going on Unemployment Insurance and others drawing welfare after being on Unemployment Insurance. Both the Unemployment Insurance population and the welfare population were found to have had workforce experience. Indeed, the study was not able to identify a statistically valid set of observable labour force characteristics differing between those using both Unemployment Insurance and welfare versus those using only one or the other program" [Barrett et al. 1996: 7]:

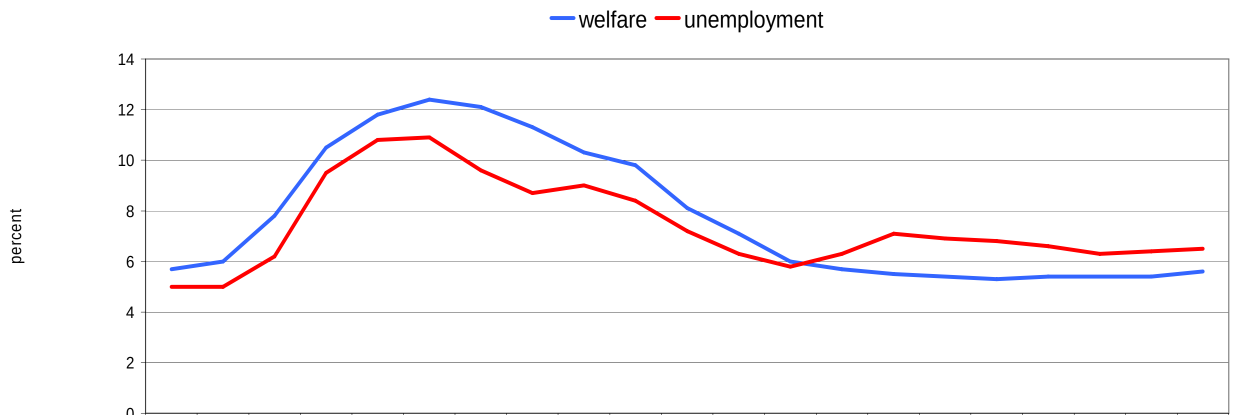
> We find that a large proportion of welfare recipients have some attachment to the workforce and that there is a large overlap in the clientele of UI and SA. There is also evidence of an upward trend over the 1986-92 period in the extent to which the programs serve a common group of participants. Welfare spell durations had a distinct bimodal distribution, with UI-SA interaction concentrated among short welfare spells. SA use was found to be associated with substantially longer UI spells in New Brunswick but not British Columbia.

One further broad empirical study of the interaction of Unemployment Insurance and welfare, outside of the Human Resources Development-sponsored series, was undertaken with a sample of Quebec lone-parent households that had received welfare payments at least once over the period 1979-1993. The study found that reductions in Unemployment Insurance benefits resulted in increased use of welfare by lone-parents in Quebec [Fortin, Lacroix and Thibault 1999].

All of these studies were of programs and conditions quite different than today's. The study period of 1986-1992 coincided with the end of an economic boom accompanied by rising inflation (1986-1989) and the onset of a significant recession characterized by price stability and rapidly rising unemployment (1989-1992). In the latter period, both Unemployment Insurance and welfare rolls were rapidly increasing. Between 1988 and 1992, the percentage of the Ontario population relying on welfare doubled from 6 percent to an astonishing 12 percent. Many workers who might never have dreamed of needing public assistance found themselves relying on one (or both) of these programs. The major reductions in Unemployment Insurance, along with its Orwellian renaming as 'Employment Insurance,' were yet to occur. On the other side of the equation, welfare was relatively easier to get and somewhat more generous than it is at present, but the system of refundable tax credits – notably the Canada Child Tax Benefit, which provides substantial benefits to lower-income families – was not yet in place. Thus it may be that the findings from these studies are not fully representative of what would be found were similar research done with today's array of programs.

More up-to-date evidence that welfare is being used as a bulwark against unemployment can be found by analysing the relationship between unemployment rates (i.e., percentage of unemployed among the labour force) and welfare caseloads. Figure 6 shows the proportion of the Ontario population on welfare and the provincial unemployment rate.[5]

Figure 6
Percentage of population on welfare and unemployment rate, Ontario, 1988-2008



	88	89	90	91	92	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08
welfare	5.7	6.0	7.8	10.5	11.8	12.4	12.1	11.3	10.3	9.8	8.1	7.1	6.0	5.7	5.5	5.4	5.3	5.4	5.4	5.4	5.6
unemployment	5.0	5.0	6.2	9.5	10.8	10.9	9.6	8.7	9.0	8.4	7.2	6.3	5.8	6.3	7.1	6.9	6.8	6.6	6.3	6.4	6.5

source: Human Resources and Skills Development Canada - Indicators of Well-being in Canada, and Stapleton 2009

As is immediately evident from a look at Figure 6, unemployment rates and welfare caseloads have been highly correlated in Ontario over the last 20 years. A regression analysis of the data produces an R-squared of over 80 percent, meaning that more than 80 percent of the variation in the caseload data in Ontario is explained by changes in the unemployment rate. This correlation is particularly striking since this period encompasses a number of substantial policy shifts both towards making welfare more generous and less intrusive and later in exactly the opposite direction. This strong correlation can most readily be explained by the proposition that a substantial number of the unemployed have turned to welfare – at least in Ontario. (And the fact that unemployment remains an excellent explanatory variable for caseload changes suggests that welfare rules and benefit changes are a lot less important in determining welfare caseloads, including the notable post-1995 decline, than is ordinarily supposed.)

In the 1998 Employment Insurance Coverage Survey, unemployed respondents ineligible for Employment Insurance were asked about their source of income. The results of the survey are shown in Table 1. Some 23 percent of unemployed persons ineligible for Employment Insurance stated that welfare was their source of income. A further 12 percent said that they were using savings or were relying upon loans from friends or family. These latter sources are obviously limited in time, so that if alternatives are not found, we can anticipate up to 35 percent of ineligible unemployed Canadians eventually turning to welfare.

Table 1
Main sources of income of unemployed people who are not eligible for Employment Insurance

Main source of income in reference month	Unemployed persons not eligible for Employment Insurance	
	000s	%
Living at home and relying on parents	246	34
Social assistance	171	23
Spouse's or partner's earnings	139	19
Savings	51	7
Loans and assistance from friends or family	35	5
Other government transfers	22	3
Pension of self or spouse	19	3
Own wage or salary	15	2
Other sources or no sources	36	5
Total	734	100

Source: Roller 1999

Although the empirical evidence is outdated or indirect, all the data that exists confirms that welfare is indeed being used as an alternative source of income for some portion of those who are unemployed and ineligible for Employment Insurance. The possible numbers are difficult to quantify but, coincidentally, the number of ineligible unemployed in 1998 was almost identical to that in 2009 – so, at a rough guess, if the proportions remained roughly similar, this would suggest that between 170,000 and 260,000 of the ineligible unemployed drew on welfare in 2009 and 2010.

While welfare is a necessary program of last resort for many Canadians, it imposes significant social and personal costs. Yet, as we saw in the earlier discussion of Employment Insurance coverage, it is difficult to see how Employment Insurance can be redesigned to expand coverage substantially while remaining a viable social insurance plan. So why not instead reform welfare to make it less invasive, eliminate asset stripping and raise benefit levels?

Countless attempts to liberalize welfare have been undertaken over the last 40 years or so, and all have been rolled back or at best allowed to erode through the gradual effect of inflation, to the extent that welfare is today as ungenerous and onerous as it has ever been in the last few decades in almost every jurisdiction. The lesson of history is that reforming welfare is a dead end as long as welfare remains a program used by a significant portion of the population. Instead, advocates of reform have suggested strategies to establish broad-based alternative programs such as the Ontario Child Benefit [The Ontario Social Assistance Review Advisory Council 2010]. This is not to say that welfare can never be improved and we should just give up on it entirely: rather that the strategy for changing welfare is to transform it from a program serving 5 or 6 percent of the population to a program serving 1 or 2 percent of the population, by providing other forms of financial assistance for many of those in need.

In line with this strategy, we propose instead a new program 'between' Employment Insurance and welfare, which will provide financial assistance to those among the unemployed who need it, while avoiding the potential long-term negative consequences of welfare and permitting welfare to get on with the task of better serving its core clientele. In Part 2 we describe the conditions under which adding a new program of this nature to Canada's income security system would be ethically and economically justified; set out a possible design for such a program; and discuss some of its implications.

Part 2: Filling the Gap between Employment Insurance and Social Assistance

Should the gap be filled?

Being on welfare is an unpleasant, psychologically depressing and perhaps even devastating experience for the recipient [Herd, Mitchell and Lightman 2005]. The amounts paid by welfare are extremely low, especially for single employable recipients. Individuals who would otherwise have to be on welfare would indisputably be better off were they able instead to obtain assistance from a much less invasive and demeaning program paying higher benefits. But the same could be said about any program paying higher benefits with fewer conditions. A program 'between Employment Insurance and welfare' might be good for recipients. However, would Canada be better off? Are there broader social or economic arguments as to why society as a whole should be willing to pay for such a program?

We can ask these questions more generally: Why provide any income security programs at all? Why not just let market forces distribute income and let the chips fall where they may, as some would doubtless advocate?

There are two different types of responses to these questions. First, we might argue that an income program is needed for ethical or moral reasons. For example: ‘in a wealthy country it is wrong to allow families to live in abject poverty’ or ‘it is unfair for unemployed workers to bear the full financial risk of unemployment’ are two ethical claims for income security programs. Second, it might be argued that there is a net benefit to a particular social program so that we are as a whole better off as a result of paying for the program – whether economically better off in the sense of having a higher GDP or by using some other measuring stick. Employment Insurance acts as an economic and social stabilizer such that GDP is higher in the long run with the program than without it. The ethical aspect may be said to be about fairness; the analysis of net benefit may be said to be about utility.

With respect to the ethical dimension, in *A Theory of Justice* the philosopher John Rawls sets out a framework for understanding whether a social program (or any other social arrangement) should be part of a fair and just society [Rawls 1971]. Rawls asks us to consider social policy from behind what he calls a ‘veil of ignorance.’ Behind the veil of ignorance the observer does not know “his place in society, his class position or social status, nor does he know his fortune in the distribution of natural assets and abilities, his intelligence and strength, and the like” [Rawls 1971: 137]. Would a well-informed and intelligent observer from behind the veil of ignorance choose a society with or without the particular social program, on the assumption that he could find himself, figuratively speaking, cast into any position within that society with any possible natural endowment?

The Rawlsian theory of justice is not by any means universally accepted, but it is an especially useful framework for exploring the ethical dimensions of income security programs because it focuses us on the distributive fairness of a program, and not just on its utility. From behind the veil of ignorance, most of us would likely choose a society in which there were at least some less harsh alternative to welfare given the possibility that we might end up as one of the unlucky unemployed without eligibility for Employment Insurance. Whether through a Rawlsian lens or other framework, the ethical argument is that a more just society is one in which both opportunities and outcomes are more equally distributed, so that if less dehumanizing and more generous temporary assistance than welfare can be offered without huge cost to society, it should be done.

Turning from the ethical to the utilitarian perspective, one of the key purposes of a new temporary assistance program for the unemployed not eligible for Employment Insurance but who are in financial need would be to divert them from welfare. The assumption is that diverting unemployed people from welfare reduces the likelihood of their going on to welfare in the future. Diversion also insulates them from the negative experience of welfare which many believe makes employment much more difficult in the future, so that diversion increases the likelihood of their getting and keeping a good job. This is far from a new idea. Many provinces have considered various ways to divert clients from welfare for this reason. It is difficult to find information on diversion programs in Canada, but in the United States there are diversion programs of various kinds in all but three states. Thirty-five states offer a single lump-sum payment as an alternative to welfare for applicants who would otherwise be eligible [Rosenberg et al. 2008].

Unfortunately, as in many areas of social policy, there are no acceptable quantitative analyses of whether diversion programs actually decrease long-term costs to the state or increase the overall income of the recipients. Nevertheless, we know that some administrators in the field have been acting on this premise and that a utilitarian argument is possible.

A utilitarian argument for a temporary unemployment assistance program may also be made in respect of less tangible benefits for the whole community. As is evident in the current economic downturn, the liveability and vitality of a neighbourhood are affected for everyone by each household in the neighbourhood. Excluding the very wealthy who can live behind gated fences, most Canadians' well-being is affected in concrete ways by the well-being of their neighbours. If unemployed people in the neighbourhood cannot afford to keep up mortgage or rental payments, the value of everyone's property declines. If the appearance and orderliness of a neighbourhood declines, this deterioration affects everyone in the neighbourhood.

As Canadians increasingly live closely packed together in cities, it is more apparent that we are not isolated atoms unaffected by those around us. Rather, the quality of our life is at least partly dependent upon the quality of life of those around us. Again, it is difficult to quantify this phenomenon, but by helping to sustain material and psychological well-being for at least a little longer, giving the jobless time to search for a job, the potential benefits of a temporary unemployment assistance program extend not only to the recipient household but to all the other households in the community. This too is a utilitarian argument.

A third benefit of a new alternative to welfare is the effect on welfare itself. Welfare was intended by the founders of the Canadian income security system to provide a last-resort safety net for the relatively few people who have nowhere else to turn. It never was meant to become a major income source for so many people in need. The objective of temporary unemployment assistance would be to divert the most 'job ready' needy from welfare and so leave the welfare rolls smaller. The expectation is that more of those who do have to resort to welfare will be hard to employ and require more intensive assistance to become employable. Clearing the caseload of those who are only temporarily in financial need would permit the welfare administration to be less of a warehousing operation and more of an opportunity planning organization.

Finally, we need to be concerned about the potential effects of a temporary unemployment assistance program on the labour market. As is discussed further below, such a program is likely to be taken up by relatively few workers, so that any effect likely would be minor. To the extent that there is an effect, any program which lessens the cost of unemployment and encourages people to report that they are actively seeking work, will necessarily increase the unemployment rate and participation rate. On the other hand, by reducing the cost of unemployment, a temporary assistance plan would also increase the length of job search, possibly resulting in a better match up of workers and jobs, which in the long run decreases unemployment and improves productivity.

Assessing the net effects on the labour market would require weighing the negative effects on unemployment and the positive effects on participation and job search, which can only be done with some experience of a program in real life. The extent of any such effects would also depend upon the specific parameters of the program: A smaller program with less generous payments will necessarily have less impact on the labour market. So, while this is likely a negative on the 'utility' argument, it is probably a small negative.

Regretfully, the utilitarian arguments are not resolvable without better data. In the following sections, we set out the parameters for a specific temporary unemployment assistance plan, with a design new to Canada's income security system. This undertaking will allow us to estimate very roughly the scope and cost of this program and to discuss several critical administrative issues.

Essential characteristics of temporary financial assistance for the unemployed

An income-tested program providing temporary assistance for the unemployed in financial need – without the asset stripping, myriad rules and stigma of welfare – could provide an option 'between' social insurance and needs-tested social assistance. We would see a new program of this kind as a complement to a stronger Employment Insurance (strengthened in its social insurance characteristics) roughly analogous to the way that the income-tested Guaranteed Income Supplement complements retirement benefits in the Canada and Quebec Pension Plan.

There are several essential characteristics for an effective temporary unemployment assistance program. It should be minimally invasive and non-stigmatizing. It needs to be temporary, so that no one can remain on it for longer than some specified period (e.g., six months every five years). It should allow recipients to carry on job search and continue most essential aspects of their normal life. And it needs to give recipients the opportunity to get back on their feet without losing everything and having to restart financial life from zero.

The fundamental purpose of this paper is to open discussion of a new temporary unemployment assistance program between Employment Insurance and welfare. Once the need for a temporary assistance program is accepted, all the rest is 'detail' – but without this detail, it is difficult to imagine what such a program would actually look like. In this second part of the paper, then, we explore options and alternatives for these all-important 'details' including the specific elements of program design. We do so mainly to stimulate discussion of a temporary income plan and not because we are wedded irrevocably to any of the design features discussed below. Our intent is to draw a clear picture of what such a program could be by offering a concrete example.

Federal or provincial? or both?

Among the multitude of design issues for social policy reform in Canada is the question of which order of government should be responsible for the new program. The 1930s legal ruling preventing the federal government from delivering social insurance programs would not apply because the temporary assistance program would neither be contributory nor a social insurance program. Since the temporary assistance program would in essence constitute a payment of money to an individual, it would be constitutionally within the spending power of either order of government. Constitutionally, the temporary assistance program could therefore be financed and delivered by either the federal or provincial orders of government, or some combination of the two.

We argue in *Towards A New Architecture for Canada's Adult Benefits* [Battle, Mendelson and Torjman 2006] that the temporary income assistance program would be best if financed and delivered by the federal government. There are several reasons for this preference (discussed in more detail in that paper). First, the federal government is the order of government primarily responsible for macro-economic policy, particularly the level of unemployment, so it makes sense that Ottawa would also be responsible for programs meant to ameliorate the effects of unemployment and which may also act as counter-cyclical measures. Second, since temporary assistance would be a closely complementary measure to Employment Insurance, the two programs need to be coordinated and the governing rules should be continuously harmonized as they evolve over time. Third, as a minimally invasive program requiring little detailed interaction with recipients, temporary assistance is the kind of program which the federal government is well-suited to deliver, leaving the provinces and territories with more capacity to provide the intensive case work and education and skills acquisition opportunities required by longer-term recipients of social assistance. Finally, a federal program could offer an opt-out provision for those provinces that wish to operate the new temporary program at the provincial level, whereas it is hard to see how a provincial program could have a federal opt-in provision, so a federal program is more flexible in this respect.

In the discussion below, we assume that the new program would be federal rather than provincial. But notwithstanding our preference for a federal program, the *social policy* goal of providing non-welfare assistance to the unemployed in financial need who are not eligible for Employment Insurance could also be met by a provincially financed and delivered program.

Temporary income assistance based on retrospective monthly income reporting

The simplest way to deliver a temporary unemployment assistance program would be via a monthly income test. Using this delivery mechanism, recipients would be required to submit a completed form every month stating their previous month's income and any other pertinent information required. The amount of the temporary income benefit would then be determined according to the previous month's income. This mechanism for administration is known as a 'retrospective' test of the previous month's income.

This standard type of delivery mechanism based on retrospective monthly reporting of income is similar to welfare. But the temporary income program would differ from welfare in several important respects. It could have a single flat-rate benefit; it could be calculated on the basis of individual income rather than household income (more on this below); it could contain no adjustment for factors such as presence of spouse and number of children, housing tenure or costs and the other many calculations of individual needs required in welfare. In short, the new temporary income program could be much simplified with much less personal information and much less policing than is the case for welfare. In this crucial respect, the new temporary income program would be very different and far less complicated and intrusive than needs-tested social assistance.

Retrospective monthly income reporting is a viable administrative alternative for a temporary income program. Nevertheless, this delivery mechanism does have some downsides. It requires setting up a whole new administrative system with all its associated costs and inevitable growing pains.

Monthly reporting and payment based on the previous month's income was used for the Manitoba Mincome experiment, a large guaranteed annual income experiment in the 1970s. Despite the common assumption that a guaranteed income would be simple to administer, Mincome encountered many complicated administrative issues, as found in an unpublished study of Mincome administration done by Mendelson. For example, if there is an error or misreporting in one month, does this result in a deduction the next month? And would this end up with a benefit cheque which consists of dozens of adjustments carried forward in incomprehensible ways? The amount of processing and complexity of actual calculations turned out to be a challenge for the Mincome experiment. All of this added to administrative costs. Of course, information technology is immeasurably more powerful today than it was in the 1970s, but despite this, some of the Mincome administrative complexity would doubtless be encountered if the temporary assistance program used a monthly retrospective income text.

Without emergency funding available immediately, as in the welfare system, the question of timing of payments may also present some challenges for a temporary assistance program based on retrospective income testing.

Using a retrospective test of the previous month's income, benefits could be paid about one month after submission of the monthly forms. This practice implies that the benefits paid would not be perfectly 'timely' in that the amount would not reflect income exactly at the time of benefit payment, as the benefit calculation would be a maximum of about two months out of date at most. (For a discussion of 'timeliness' and why it is important, see Mendelson, Millar and Whiteford 2003.)

To understand this problem, imagine the following scenario. A recipient's own income consists of a single lump sum payment on September 1 with no other income for the remainder of the month; the temporary income program requires the recipient to submit a report on monthly income by September 30; and the temporary income benefit is then paid on October 31. This scenario is an example of the longest possible delay between the payment and the income which is used to calculate the payment – about two months. This approach assumes that it is administratively possible to process information and make payments within a month.

Two months may be too long to wait for someone with no other income, so in this instance welfare might be required as a stopgap measure, which more or less defeats the whole purpose of the reform. Of course, this is an example of the longest lag time possible. But some time lag is unavoidable in any program based on retrospective income, and any time lag is difficult for those with little or no income.

Although the retrospective temporary assistance program would be designed to provide only a short-term financial respite and to be non-invasive, it might be similar enough to welfare to be perceived socially as just another welfare program – with all its negative characteristics. It might be seen as a program only for ‘poor’ people, which would stigmatize those who are unemployed, actively searching for work and in financial need. One of the objectives of the temporary income plan is to avoid stigmatizing recipients so as to give them the best possible platform from which to get back into employment. To the extent that there is stigma associated with the program, unfortunately, this objective would not be fully met.

In the next section of this paper we set out a different and, we believe, novel design for a temporary unemployment assistance plan which might avoid many of the problems with a program based on retrospective reporting of monthly income. We set out a number of detailed parameters for the alternative program. All of these parameters could also be applied to delivery based on a retrospective monthly income reporting system. The difference is in the delivery mechanism.

The Jobseeker’s Loan model

In this design, temporary unemployment assistance would be provided in the form of a forgivable loan whose repayment is contingent upon income reported through the income tax system. The program would be unlike any existing income security program. We have called this the ‘Jobseeker’s Loan’ (borrowing the name ‘Jobseeker’s’ from the UK, though our program design is nothing like theirs).

Rather than paying benefits adjusted for the previous month’s income, the Jobseeker’s Loan would make a loan available to all unemployed adults actively seeking employment. The loan would be entirely forgiven if income in that year as reported through income tax was very low, but the loan would be partially or fully repaid if income were higher.

The loan would be advanced to the recipient in biweekly instalments, like a paycheque. A maximum amount of loan would be available only within a defined period of time, say five years, so that once the loan was taken up it would require another five years before the recipient once again became eligible for the full Jobseeker’s Loan. There would be rules to prevent ‘doubling up’ so that a loan would not be available to anyone collecting full Employment Insurance benefits, welfare benefits or other social program benefits (in particular, those that are not taxable). However, a loan could top up partial Employment Insurance or other benefits where the amount of those other program benefits is less than the maximum amount of the loan.

It is possible to describe a Jobseeker's Loan program with just eight parameters, as set out on the first half of Table 2 under 'input parameters.' We have also set specific values for each of these parameters. These values could, of course, be different in amount. They represent what we consider reasonable configurations for the Jobseeker's Loan, but are here used only to illustrate how an income-contingent forgivable Jobseeker's Loan would work. Should the Jobseeker's Loan be implemented, more detailed work will need to be devoted to the actual values to be used.

Given the values of the eight parameters used to define the loan program, the result is the program parameters (dependent variables) in the bottom five rows of Table 2: a Jobseeker's Loan which pays $692 bi-weekly for up to 13 pay periods (26 weeks). This amounts to a maxi-

Table 2
Variables required to define the Jobseeker's Loan Program

Jobseeker's Loan input parameters	*Values*
Percentage of provincial minimum wage	90%
Hours per week minimum wage	37.5
Eligibility period in weeks	260
Weeks of loan entitlement acquired for each week in the eligibility period	10%
Jobseeker's Loan repayment tax rate for income below first federal rate	0%
Jobseeker's Loan repayment percentage of tax rate for income above first federal rate	50%
Jobseeker's Loan repayment percentage of tax rate for income above the second federal rate	100%
Percentage restoration of weeks	50%
Jobseeker's Loan program benefits (output variables)	
Weekly gross loan	$346
Maximum eligible weeks	26
Maximum loan per eligible period	$8,994
Taxable income at which Jobseeker's Loan begins to be paid back	$10,382
Taxable income at which Jobseeker's Loan is fully paid back	$71,426

mum loan of $8,994 in each five-year period. Below the first federal income tax bracket, the loan would be forgiven; between the first and the second tax brackets, an amount equal to 50 percent of the federal tax rate on income (i.e., 7.5 percent, half of the bottom 15 percent tax rate) would be repaid, and the rest of the loan forgiven; above the second income tax bracket, an amount equal to the existing federal tax rate (i.e., 22 percent) up to the full amount of the loan would be repaid, with the rest of the loan, if there is any, forgiven.

In the following discussion we explain each of these variables and describe some examples of how the Jobseeker's Loan program might work.

percentage of provincial minimum wage

There are many different ways that the maximum amount of Jobseeker's Loan could be set. One mechanism would be to set the loan as some percentage of the Employment Insurance benefit. However, Employment Insurance benefits paid to each recipient reflect that recipient's prior earnings, since benefits are calculated as a percentage of insurable earnings up to a maximum. Consequently, it is difficult for an Employment Insurance recipient to obtain benefits greater than previous earned income.

The amount of the Jobseeker's Loan would not reflect the amount of prior earnings – or any earnings at all. Thus it lacks the built-in assurance of Employment Insurance that the loan will not exceed prior earnings. If this problem is to be prevented, the maximum loan has to be determined with a view to ensuring it is not greater than earnings for most full-time workers.

Here we illustrate the maximum loan as a percentage of the prevailing provincial minimum wage for a week's work, defined in respect of a number of hours. Using the minimum wage in each province maintains a relationship with income obtainable from work, and also reflects the existing standards in that province. It also provides something of an incentive for provinces not to fall too far below the national norm in their minimum wage levels.

hours per week at minimum wage

Using the minimum wage to set the maximum Jobseeker's Loan benefit makes it necessary to assume a number of hours as the standard work week. Here we assume 37.5 hours per week as reflecting the prevailing standard in Canada. Where the maximum loan is set at 90 percent of minimum wage, Table 2 shows the maximum loan in Ontario, where the minimum wage is currently $10.25 per hour. The result is a Jobseeker's Loan per week of 37.5 X 90 percent X $10.25 = $346. While this is a modest amount relative to the average wage ($880 per week in Ontario as of 2010), it is much more than is paid to single adults in the welfare system ($132 weekly in 2009).

eligibility period in weeks

The claimant can claim up to a maximum number of weeks, less any weeks of Jobseeker's Loan she or he has claimed within the most recent of a defined number of weeks, called the 'eligibility period.' In this example, we have set the eligibility period as five years – i.e., 260 weeks. Upon reaching minimum age, say 19, an applicant obtains eligibility for up to the maximum number of weeks of Jobseeker's Loan. Upon reaching the maximum age of eligibility, say 65, each person would be eligible for a lump-sum loan equal to any outstanding Jobseeker's Loan payable. This practice would be of most value to those with the lowest incomes as much of the Loan would be taxed back for those with higher incomes (who presumably would not then take it). The retirement benefit under the Jobseeker' Loan could be viewed as a boost to the Guaranteed Income Supplement for the lowest-income seniors.

eligibility per weeks in period

The claimant accumulates additional weeks of Jobseeker's Loan eligibility as a percentage of the number of weeks within the eligibility period, such that the eligibility period times the percentage equals the maximum number of weeks of Jobseeker's Loan. Eligibility is accumulated whether or not a person is working or available for work.

In the values set out in Table 2 as an illustrative example, the percentage of Jobseeker's Loan weeks eligibility accumulated is 10 percent, as it takes 260 weeks to acquire 26 weeks of eligibility, which then becomes the maximum number of weeks of Jobseeker's Loan in any five-year period. Jobseeker's Loan can be claimed at any time at the discretion of the applicant, with the requirement that the claimant be actively engaged in the search for employment. There is nothing to prevent a recipient working part time while in receipt of the loan, so long as the recipient is able to demonstrate that she or he is still engaged in actively seeking full-time employment, except that the amount that must be paid back at the end of the year will thereby be increased if that person earns more than the basic exemption (see below).

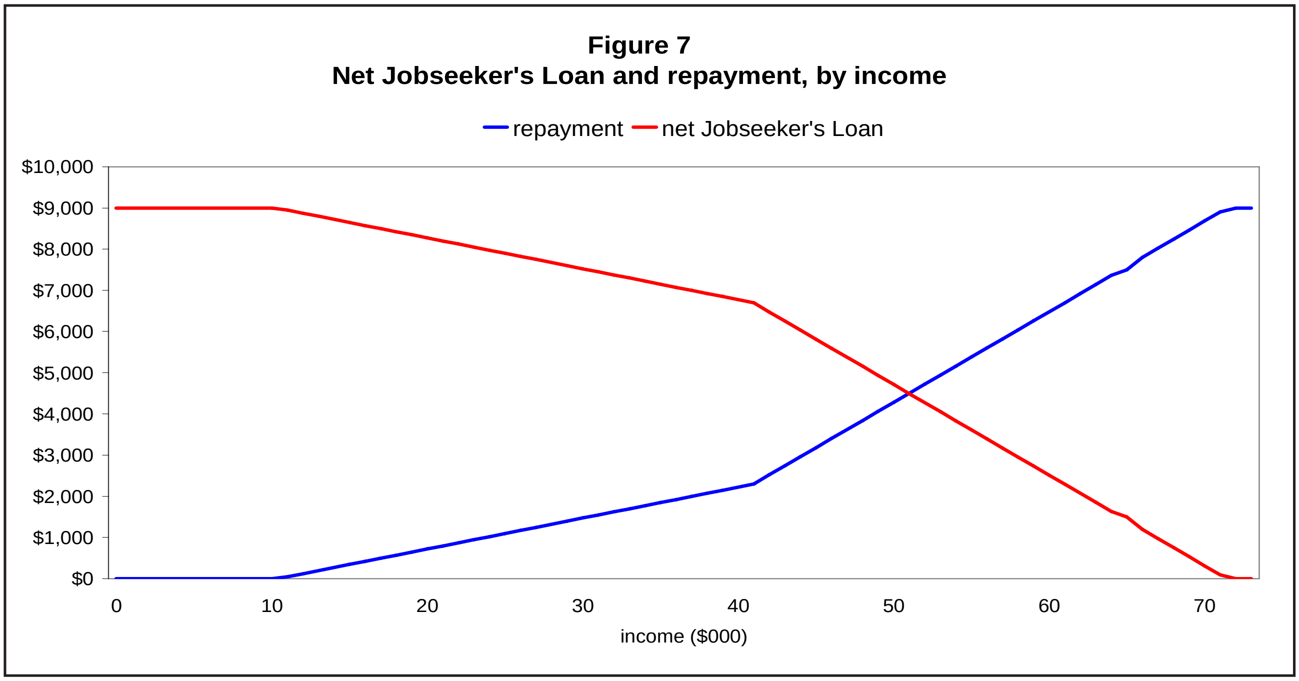
repayment through income tax system

Upon paying income tax at the end of the year, the Jobseeker's Loan must be partially or fully repaid as a percentage of income, except for those whose income is very low. This repayment mechanism would function as a kind of income tax surtax designed so that the amount of Jobseeker's Loan repaid would climb as income climbed. At middle incomes, all of the Jobseeker's Loan would be repaid.

In this case, we have model ed the Jobseeker's Loan repayment schedule as a progressive percent of the prevailing 2010 federal tax rate in the recipient's income bracket, with the Basic Personal Amount here used as a the income threshold for maximum benefits. Up to the basic exemption level of $10,382, there is no repayment required. From $10,382 up to $40,970 (the second income bracket), the repayment rate is half of the income tax rate of 15 percent, or 7.5 percent of income. Between $40,970 and $81,941, the repayment rate is equal to the income tax rate in that bracket (22 percent). The repayment rate would also be 100 percent of the prevailing tax rate for higher brackets, but this is not relevant since the Jobseeker's Loan in our model is fully taxed back within the second tax bracket – at $71,426.

Note that the tax rate is *not* a tax on the loan as income; rather, it is a repayment schedule as a percentage of income. For example, if a recipient has a Jobseeker's Loan of $2,000 and income of $15,382, she or he must repay 7.5 percent of $5,000 or $375. The remaining $1,625 would be forgiven. The person would have to have had an income of $37,049 or more to be required to fully repay a $2,000 Jobseeker's Loan.

The added 'marginal tax rate' on income is therefore nil up to $10,382, 7.5 percent from $10,382 to $40,970 and 22 percent from $40,970 to $71,426. However, as this constitutes a loan repayment rather than a tax, it is not clear that it should be seen as an addition to the marginal effective tax rate (e.g., is repayment of an income contingent student loan an addition to the marginal *tax* rate?). In any case, the increment to the average 'tax rate' of each individual (i.e., total tax plus loan repayment as a percentage of total income) is, of course, much less than the marginal rate due to the Basic Personal Amount and the stepped nature of the marginal tax rate.



As illustrated in the example, the amount of loan which was not repaid in any year due to income being insufficient would be forgiven.

We have here modelled the Jobseeker's Loan repayment based on the assumption that it would reflect total income as reported in the tax system. This is the simplest course and may also be the most equitable. However, if this were not desirable, it would be possible to include other income not counted under the 'regular' tax system, such as TFSA income and welfare income (while a person cannot collect a Jobseeker's Loan while on welfare, it is possible to have collected a loan and been on welfare during a single year).

Figure 7 illustrates the amount of loan repayable and the net amount of Jobseeker's Loan to a person claiming the maximum loan, at various income levels.

percentage restoration of weeks

Recipients repaying the Jobseeker's Loan would be deemed to have recovered a portion of their eligibility for a new Jobseeker's Loan, as a percentage of the amount repaid. For example, if the weekly Jobseeker's Loan maximum is $346, and there is repayment of 2 X $346 = $692 of the Jobseeker's Loan, this would result in restoration of eligibility for one week of Jobseeker's Loan, assuming eligibility is restored at 50 percent. Aside from making the overall program fairer, it also reduces the effective marginal tax rate on income as a result of the Jobseeker's Loan repayment by up to one-half (depending upon how one values the restoration of eligibility). Note that a full loan entitlement would still have to be regained over time, but the length of time needed to restore full eligibility would be reduced through loan repayment. Restoring half of eligibility is fair given that the loan is repaid. But restoring only partial eligibility will restrain frivolous claims for the Jobseeker's Loan.

weekly gross loan

The weekly gross maximum loan is simply a function of the minimum wage and the percentage of the minimum wage reflected in the Jobseeker's Loan benefit level. We are here proposing a Jobseeker's Loan not adjusted for any personal budgetary factors. Costs such as home ownership or food expenses would also not be reflected, any more than they are for wages, and therefore would not have to be reported or accounted for in any way. Child benefits would continue to be provided through the federal Canada Child Tax Benefit and other federal and, in most cases, provincial and territorial child benefits (e.g., in Ontario the maximum combined payment from the Ontario Child Benefit and federal child benefits now is more than $5,000 per year).

We do not here include any deductions for payroll taxes such as C/QPP contributions or EI premiums, mainly for simplicity. These would be possible to include if thought desirable.

maximum eligible weeks

As noted, the maximum eligible weeks – 26 in this illustration – are a function of the eligibility period and the rate at which eligibility is accumulated.

maximum payable per eligible period

The maximum loan in any eligibility period is simply the maximum number of weeks times the gross weekly benefit: 26 X $346 = $8,994.

taxable income at which a Jobseeker's Loan begins to be repaid

This is a function of the decision to use the federal Basic Personal Amount as the income threshold for maximum benefits for the purposes of this model – $10,382.

taxable income at which a Jobseeker's Loan is fully repaid

This amount – $71,426 – is a function of the application of the federal tax system and the tax rate for calculating repayment required.

Reporting unit

In any income tax or transfer payment system, one of the critical variables is the reporting unit. In Canada, the personal income tax system is based primarily on individual income, not household income (unlike the United States). Canada's transfer payment system is mixed: Some programs – including refundable credits paid through the tax system – are based on household income, while other programs are based on individual income.

In this paper, we propose that the Jobseeker's Loan be based on the individual reporting unit rather than the household. A couple, each of whom was on Jobseeker's Loan, could get a maximum $692 a week (per couple), but of course only for a half of a year every five years.

It would be possible to adjust this amount so that the total received was some fraction of the sum of two individual benefits (in the Guaranteed Income Supplement, it is 81 percent) when both members of a couple collected at one time, or otherwise define the reporting unit as a household or a couple. However, this approach would require the tax department to become even more intimately involved in personal lives to determine who is and who is not actually a 'partner.' This is no simple matter, as there are many forms of economic unit today. In contrast, with a forgivable loan based on individual income, the form of relationship is irrelevant. A married couple would be equally able to benefit from the forgivable loan as two sisters living together and sharing resources.

Another positive consequence of counting individual income rather than household income is to provide what is in essence a benefit to any at-home partner with no taxable income who returns to the labour market. This is especially important for the next few decades as the population ages and higher levels of participation in the work force are required to support pension and other benefits.

In the interests of least intrusiveness and in recognition of the increasing difficulty of defining what constitutes a couple expected to share economic resources, as well as to encourage workforce participation, we would view maintaining individual treatment as preferable, although this does add to costs. Note, however, that this is not a necessary feature of the Jobseeker's Loan: The program could as easily be organized to require repayment on a household basis.

Costs of the Jobseeker's Loan

Obviously, it is difficult to estimate the cost of the Jobseeker's Loan. How many people would actually take it up is hard to predict, as voluntary programs of this kind have typically been significantly undersubscribed. We will not in this paper attempt to provide a detailed estimate – only a rough ballpark estimate to show the scale of program.

The size of the Jobseeker's Loan program in any year will be dependent on the unemployment rate. By using 2010 as an example of a high unemployment year, we can estimate an approximate upper limit on the potential size of the program. According to the most recent results from the Employment Insurance Coverage Survey, there were about 700,000 unemployed Canadians in 2010 ineligible for Employment Insurance [Statistics Canada 2011]. This figure does not include about 84,000 students who left their employment to return to school, and so would not be eligible for the Jobseeker's Loan as they were not actively engaged in looking for work and available for employment – at least as given the rules suggested in this paper.

The 700,000 unemployed are eligible for Jobseeker's Loan only once every five years, so we can assume about one-fifth or 140,000 might take up the loan in an average single year (there are some additional phase-in costs which we do not consider here). Assuming all of these took up the full loan the gross federal cost would be about $1.26 billion. However, it is likely that at least some of the loans would have to be repaid, so assuming a modest average repayment of $2,000 each, the net cost to the federal government would be about $980 million.

Add to this the cost of the Jobseeker's Loan retirement benefit. There were about 15,000 new partial or full Guaranteed Income Supplement beneficiaries in each year over the last five years [Service Canada 2010]. Here we assume 20,000 full or partial new Guaranteed Income Supplement recipients a year. These people represent the lowest-income seniors. Assuming all of them are entitled to the Jobseeker's Loan retirement benefit, it would cost about $180 million annually.

Adding the cost of the unemployed and the retirement benefit brings the net federal cost back up to about $1.16 billion. But the new federal program would also result in some savings to provincial governments.

In Part 1, we estimated that 170,000 to 260,000 unemployed were ineligible for Employment Insurance and were relying upon welfare in 2009. Assume the figure is roughly the same for 2010 – say, for purposes of a rough ballpark calculation, 200,000 people. If one-fifth of these 200,000 unemployed were eligible for and received the maximum Jobseeker's Loan, – assuming that costs to provinces for social assistance would have been about $3,000 per person for half a year, the length of the loan – the total welfare saving would be about $120 million.

So, factoring in the savings to provinces, the overall net cost of the proposed Jobseeker's Loan comes to a little more than a billion dollars a year. This amount does not take account of macroeconomic effects which might be especially important when unemployment is high, resulting in slightly higher Gross Domestic Product as a result of the program and consequently higher tax revenues at both the provincial and federal levels, which would further reduce net cost.

This is anything but a precise estimate, but it does give us some sense of the expense of the proposed Jobseeker's Loan program, which is likely in the vicinity of one billion and not five or six billion dollars. One billion is certainly a very large figure, but it is well within the range of new government initiatives recently taken or promised. For example, the Conservative party estimated the cost of its promised income tax splitting for couples with children at $2.3 billion annually. The cost of the pension income splitting tax break, which goes almost entirely to benefit wealthy seniors with non-working partners, is $920 million today and will grow rapidly in the future along with the number of pensioners. The list could go on. The point here is that the new Jobseeker's Loan program would not be prohibitively costly.

Conclusion

This paper has shown that inadequate coverage of the unemployed through the Employment Insurance program is due to non-participation in the Employment Insurance program as well as ineligibility of many who do participate. Consequently, liberalizing the eligibility criteria for Employment Insurance is not going to correct this deficiency. Indeed, given that Employment Insurance is and should remain a social insurance program, it is unlikely ever to be able to cover self-employment or many contractual and other unorthodox employment arrangements that have been growing in our labour force.

At present, welfare is the only resort for the unemployed in financial need who are not eligible for Employment Insurance. But welfare is a highly stigmatizing and invasive program. We have therefore proposed the development of a new income-tested program 'between' welfare and Employment Insurance which would provide limited and temporary financial assistance to those in need who are actively engaged in job search.

The second part of this paper addresses the design of the program to provide temporary income to the unemployed. This program could be designed in the 'usual' way with monthly reporting and the amount of benefit calculated on the basis of the report. However, we explore in detail the possibility of a novel type of design which instead pays a forgivable income-contingent loan to persons searching for work, with the repayment administered through the income tax system. We have called this the 'Jobseeker's Loan' to distinguish it as a non-welfare program that is intended to provide temporary assistance for those looking for work, but is repayable for those with the means to do so.

The proposed new income security program for the unemployed fits within a larger agenda for reform of Canada's income security system set out in *Towards a New Architecture for Canada's Adult Benefits* [Battle, Mendelson and Torjman 2006]. We have not here spelled out in detail the complementary reforms which could be undertaken along with the introduction of the Jobseeker's Loan. However, among these measures could be a substantial improvement in provincial welfare to transform it into a program that really does provide recipients with the opportunity to gain skills and knowledge needed for employment. We also believe that the Jobseeker's Loan could make reform of Employment Insurance itself more palatable, such as raising benefits to provide better continuity of living standards, increasing work sharing programs such as were implemented in Germany during the recession, and reducing or eliminating the favoured treatment of some unemployment regions across Canada. Overall, we would see the Employment Insurance program run more rigorously as a social insurance, including real stewardship by business and labour, rather than by government.

The Jobseeker's Loan proposed in this paper would fill a large hole in Canada's income security system, at a reasonable cost.

Endnotes

1. The proposal in this paper fits within a larger critique and re-conceptualization of income security in Canada which we discuss in *Towards a New Architecture for Canada's Adult Benefits* [Battle, Mendelson and Torjman 2006]. Readers interested in this larger context should refer to *A New Architecture* which is available on the Caledon Institute of Social Policy website.

2. This and all subsequent data, except where otherwise stated, is from the *Employment Insurance Coverage Survey* as reported in Statistics Canada (2009; 2010).

3. In this and the following discussion, 'Employment Insurance benefits' means regular benefits and does not include parental leave, fishers' benefits and other benefits, unless otherwise stated.

4. 'Eligible for Employment Insurance' includes both those who collected benefits and the small number who were eligible for benefits but did not make a claim (about 3 to 4 percent of the unemployed population).

5. Data from Human Resources Development Canada *Indicators of Well-being in Canada* *www4.hrsdc.gc.ca/h.4m.2@-eng.jsp* and Stapleton 2009.

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