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Chapter 2

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The experience of the Great Depression, with unemployment rates reaching 25 percent in 1933, had a devastating impact at both the individual and societal level, making it abundantly clear that the United States needed to establish an unemployment insurance (UI) program (Haber and Murray 1966). It was during this crisis that the political will was found to enact legislation enabling UI in the Social Security Act of 1935.

The Great Recession was unquestionably the worst economic downturn the United States faced since the Great Depression (Goodman and Mance 2011). The experience of the Great Recession demonstrated the UI program’s success at mitigating individual economic insecurity (Gabe and Whittaker 2012) and providing macroeconomic stabilization (Kekre 2016). However, even though some of the problems outlined below developed over many decades, they were greatly exacerbated during and after the Great Recession and threatened the program’s ability to effectively function as a meaningful social insurance program. While these programmatic challenges are serious when the economy is growing, the weakening of the social safety net for jobless workers and their families could have devastating consequences for local and state economies, as well as the national economy, during the next economic downturn.

Building on the lessons learned from the past and looking to the future, the fiscal year (FY) 2017 Obama Budget contained a set of UI reform proposals aimed at addressing many of these challenges in order for all states to have a robust, meaningful, and genuine UI program with adequate resources in reserve to provide unemployed
workers with sufficient benefits as they seek new jobs. This chapter provides an overview of the UI program, defines the problems that were the basis for the UI reform proposals in the FY 2017 Obama Budget, describes those proposals, and explains how they were intended to remedy the problems.

OVERVIEW OF UNEMPLOYMENT INSURANCE

UI is designed to provide partial, temporary income support to individuals who are unemployed through no fault of their own. This program is a federal-state partnership (USDOL 2017a) based on federal law, but it is administered by states under state law. Unless there is an explicit requirement or prohibition in federal law, states have great latitude to establish the parameters of their UI programs. For this reason, there is much variation among the states with respect to qualification and eligibility requirements, weekly benefit amounts, number of weeks of benefits, disqualification provisions, taxable wages, tax rates, and many other key policy areas (Employment and Training Administration [ETA] n.d.-a).

Eligibility

Determining benefit eligibility is a multi-step process. First, UI applicants must have sufficient recent labor market attachment, measured by work experience, to qualify for UI benefits. New entrants to the labor market, reentrants after a withdrawal from the labor market, the self-employed, and genuine independent contractors are not eligible for UI because they have not recently worked in covered employment positions. In general, prior to becoming unemployed, applicants must have earned sufficient amounts working in covered employment during at least two calendar quarters in a 12-month period to qualify for benefits. Traditionally, states would examine earnings during the first four of the most recently completed five calendar quarters when
making what is called a “monetary determination.” Recognizing that using this period of time (i.e., the “base period”) as a basis for establishing UI eligibility does not take into account up to the most recent six months of an individual’s work history, many states have begun to use an alternative base period that examines earnings during the most recent four completed calendar quarters when making a monetary determination (Mastri et al. 2016).³

Next, a determination must be made that the applicant was separated from employment (i.e., became unemployed) through no fault of their own. The classic example of this is when an employer lays someone off because work is no longer available. However, under certain circumstances, if an individual quits or the employer fires an individual they may still be eligible for benefits. Every state’s UI law defines what constitutes good cause for quitting (ETA 2016a). While all states include good cause connected with work, many states also include certain personal reasons in their definition. Similarly, although there are many reasons an employer may decide to fire an employee, individuals generally would be disqualified from receiving UI benefits only if they were fired for work-related misconduct.

After the initial eligibility determination is made, applicants must demonstrate their continued attachment to the labor market by meeting a set of ongoing eligibility requirements each week that they claim benefits. These include being able to work, being available for work, and actively seeking work. Reflecting workforce behavior from decades ago, even if individuals earned/worked enough in part-time employment to qualify for benefits, many states continue to require individuals to be available for and seek full-time work to be eligible for benefits due to the presumption that individuals who work part time do not have a genuine attachment to the labor market.

Financing

The UI program is funded primarily through federal and state taxes assessed on employers.⁴ In general, the Federal Unemployment
Tax Act (FUTA) effective tax rate is 0.6 percent (ETA 2016b)\(^5\) on the first $7,000 of workers’ earnings (Griffin 1999).\(^6\) The full FUTA tax is 6.0 percent, but employers get a credit of up to 5.4 percent if the state’s UI law conforms to federal UI law and the state has no long-term outstanding federal advances (loans) to pay benefits. FUTA revenue is primarily used to pay for states’ costs in administering the program, benefit costs for certain programs that extend (provide additional weeks of) benefits, and for advances to states that run out of funds to pay UI benefits.

State unemployment tax revenue is used to pay for “regular” benefits—typically up to 26 weeks of benefits are payable to individuals when they become unemployed. Some states provide a uniform number of weeks of benefits to all jobless workers who qualify. Other states provide a variable number of weeks of benefits whereby individuals with earnings throughout the base period will be eligible for more weeks of benefits than individuals with earnings during only a small part of the base period. The unemployment tax rates and the amount of wages that are subject to state unemployment taxation vary significantly among the states. In addition, in all states, the state unemployment tax rate assigned in a given year varies from employer to employer based on the employer’s experience with unemployment (i.e., “experience rating”). Employer accounts are “charged” for benefit payments made to their former employees, and these charges are factored in when determining employer tax rates in subsequent years. In general, employers that have more former employees who receive UI benefits pay higher state unemployment taxes than employers with lower UI benefit costs associated with their former employees.

The range of applicable state unemployment tax rates varies from year to year depending on the reserves the state has in its account in the Unemployment Trust Fund (UTF) to pay future benefits. When the economy is strong, trust fund balances increase because there are more employers paying taxes on more employees’ wages while fewer benefit payments are made. If the state’s trust fund account balance exceeds certain levels, the range of applicable rates decreases in the
following year because less revenue needs to be raised. When the economy declines, trust fund balances decrease because benefit payments go up as layoffs increase and tax revenue decreases as fewer employers pay unemployment taxes on the wages of fewer employees. If the state’s trust fund account balance goes below specified levels, the range of applicable rates increases in the next year so that more funds will be collected to pay for benefits. Thus, not only will state unemployment tax rates vary from employer to employer based on their experience with unemployment, rates also will vary from year to year based on the state’s reserves in the UTF.

**Advances**

Unemployment Insurance is, as its name implies, a social insurance program paid as a matter of right to all individuals who meet its requirements. If a state runs out of funds to pay benefits, the state may borrow from the federal government\(^7\) to continue to meet its obligations to all eligible unemployed workers. Federal advances accrue interest under certain circumstances. Since states may not use trust fund dollars to pay this interest, many states assess a separate tax on employers to cover this cost. Also, in general, should a state have outstanding federal advances as of January 1 on two consecutive calendar years, its employers’ FUTA tax credit will begin to be reduced, with the resulting additional revenue being used to pay back the federal debt.\(^8\) States may avoid the credit reduction or reduce it if certain requirements are met.\(^9\) In short, sustained insolvency results in marked increases in employers’ total unemployment-related costs—the schedule of applicable state tax rate increases and/or a solvency add-on tax may be triggered, additional state taxes to pay interest may be assessed, and net federal unemployment taxes may increase to pay down the outstanding federal advances to the state to pay benefits.
Solvency

Maintaining sufficient reserves of benefit funding is essential to mitigate the likelihood of large fluctuations in employers’ state UI tax liability from year to year, with especially large increases needed if the economy is recovering from a recession. Hence, states are encouraged to forward-fund their accounts in the UTF (U.S. Advisory Council on Unemployment Compensation 1996). The average high cost multiple (AHCM) measures state solvency. Using data from the most recent three recessions to determine high benefit costs in a state, the AHCM measures how long the state could pay benefits when benefit payment levels are high given the state’s current balance in the UTF. Although it is recommended that states maintain trust fund balances sufficient to pay benefits for one year at recessionary levels, there is no federal requirement concerning state solvency. Because states have great latitude when designing their UI tax structures and the revenues they are expected to yield, some states have opted to follow more of a “pay as you go” model that keeps employer taxes low but does not generate enough revenue to build significant reserves for use during the next economic downturn. As explained above, this can result in greater volatility in the state and federal unemployment tax payments that employers are required to make.

Extended Benefits

Recognizing that during recessionary periods regular state UI benefits provide insufficient income support for many unemployed workers, the federal-state Extended Benefits (EB) program is intended to provide for additional weeks of UI benefits when unemployment is high and rising. Benefit costs are shared equally by the state and federal government. EB is “triggered” when states’ unemployment rates exceed certain levels and are higher than they had been in recent years. All states must have an EB trigger based on the insured unemployment rate (IUR), which is based on data concerning individuals
who are currently receiving regular UI benefits. To trigger on, the 13-week IUR must be at least 5 percent and be at least 120 percent of the rate for the equivalent 13-week period in each of the preceding two calendar years. Under the IUR trigger, individuals may receive up to 13 additional weeks of benefits. If a state uses an optional total unemployment rate (TUR) trigger, which uses the Bureau of Labor Statistics’ (BLS) household survey data about individuals who are not working and have looked for work during the last four weeks, individuals may receive up to 13 or 20 weeks of additional benefits, depending on the state’s TUR. Up to 13 weeks of benefits would be available if the state’s three-month TUR is at least 6.5 percent and at least 110 percent of the rate for the corresponding three-month period in either of the two previous calendar years. A total of up to 20 weeks of benefits would be available if the state’s three-month TUR is at least 8.0 percent and the rate meets the 110 percent “lookback” requirement. Because these triggers are not very responsive to economic downturns and states historically have not been triggering EB during recessions (or not triggering on soon enough), especially via the IUR trigger, special federal programs have been created to provide additional weeks of benefits to unemployed workers.

Reemployment

Although providing benefits to individuals unemployed through no fault of their own is the overall mission of the UI program, there has been an explicit acknowledgment of the importance of helping individuals who receive UI benefits to become reemployed since the program’s inception. Whereas some workers maintain their attachment to their jobs (i.e., they are on a temporary layoff), most do not. It is for this reason that federal law requires UI payments to be made through public Employment Offices. Thus, in the past, when unemployed workers had to go in person to apply for UI benefits, those who were not job attached would be referred for assistance finding work to the Employment Service, which was colocated with local UI
offices. As UI claims taking moved out of local offices in the 1990s and was increasingly handled over the phone or via the Internet, the connection to public Employment Offices weakened in some states. To strengthen this connection, several strategies have been implemented, including the development of the UI Reemployment and Eligibility Assessment (REA) program. Since 2005, funds have been appropriated to the U.S. Department of Labor (USDOL) to enable states to address the individual reemployment needs of UI claimants, and to prevent and detect improper benefit payments by reviewing their eligibility for benefits (ETA 2016c). The results have been positive with respect to reducing the number of weeks claimed and compensated, the likelihood of exhausting UI benefits, and improper payments (Benus et al. 2008). Due to its early successes, REA funding was increased. The program was renamed Reemployment Services and Eligibility Assessments (RESEA), which reflects a narrower focus on individuals who are most likely to be long-term unemployed (and on those who transitioned out of the military). Recognizing the need for increased reemployment services for these individuals, RESEA funding may now be used for this purpose. In February 2018, explicit permanent statutory authority for RESEA was included in the Bipartisan Budget Act of 2018.

**Short-Time Compensation**

When tackling the problem of unemployment, increasing emphasis has been given to implementing strategies that avoid layoffs. Starting in 1982, federal UI law permitted states to experiment with short-time compensation (STC), also known as work sharing, which provides a partial UI weekly payment to certain individuals whose work hours were reduced. This is noteworthy because such individuals normally wouldn’t be eligible for any weekly UI payment because they earned too much money. Authority to run STC programs became permanent in 1992. While not all states operate STC programs, there has been increasing recognition of its value. By reducing
hours of work for a group of employees rather than laying off a portion of them, employers maintain their skilled workforce and no one loses their job. The workers meanwhile experience a smaller reduction in their earnings because they receive a reduced UI payment. For these reasons, STC is considered a win-win situation. Interest in STC heightened during the Great Recession, and the Middle Class Tax Relief and Job Creation Act of 2012 included several provisions designed to encourage more states to enact STC laws and for existing STC states to expand their programs (ETA n.d.-b). These provisions include two measures: 1) reimbursing states for up to three years of STC benefit costs, and 2) providing grants to states for implementation or improved administration of STC programs and for promotion of and enrollment of employers in STC programs. Sixteen states received grant funds totaling $46,154,004. As a result of these offerings, the STC program has grown and strengthened (Bennicci and Wandner 2015).

**Integrity**

An operational area that has received increasing attention and emphasis in recent years concerns integrity. This is a broad undertaking that includes efforts to ensure that employers are paying the proper amount of unemployment taxes as well as efforts to prevent, detect, and recover improper benefit payments. These efforts have been central to the UI program for quite some time, but new challenges have arisen as the claim-taking process moved out of local offices due to advances in technology. These technological advances, however, have also provided more tools to help states in their efforts to combat these challenges. For example, states cross-match claim information with information in their state directories of new hires for the purpose of finding individuals who continue to claim UI benefits after they return to work. In addition, under certain limited circumstances, states may recover improper UI benefit payments by offsetting federal income tax refunds due to the individual.
The UI reform proposals in the FY 2017 Obama Budget addressed several key policy areas: solvency, benefit adequacy, extended benefits, reemployment, short-time compensation, and integrity. Before discussing the specifics of these proposals, it is essential to provide both the high-level context and a broad description of the state of the UI program, which help define the problems that the proposals were designed to address.

Unemployment

Unemployment is a lagging indicator, so the national TUR peaked in June 2009 as the Great Recession ended (Figure 2.1). As economic recovery continued, job growth exceeded and TUR dropped below prerecessionary levels. These data are quite compelling, but they do not tell the entire story (BLS 2009).

Figure 2.1 Job Growth and Unemployment, 2007 to 2016

SOURCE: USDOL/BLS data.
Although the economy continued growing and there were increasing opportunities for workers, significant challenges remained. For example, consistent with changes at the national level, TUR declined in most states (Figure 2.2), but it remained markedly higher than the national average in some states. In addition, long-term unemployment remained a persistent challenge (Ghayad 2013) even as economic recovery continued (Figure 2.3). For example, in September 2016, 24.9 percent of the unemployed (2.0 million people) had been unemployed for more than 27 weeks.

**UI Benefits**

Consistent with the long-term unemployment data, the average number of weeks an individual receives UI benefits (i.e., “duration”)

**Figure 2.2 Unemployment Rates by State**

*Seasonally adjusted, October 2016*

*U.S. = 4.9*

NOTE: Inset maps not to scale.
increased. Historically, the average duration of UI benefit receipt has varied consistently with changes in TUR, but the average duration of UI benefit receipt did not decline as much as would have been expected when TUR declined (Figure 2.4). There are many possible reasons for this, including insufficient job growth, proportionately more permanent layoffs, and a mismatch between worker skills and emerging employer needs.

When an individual initially establishes eligibility for UI benefits, the state UI agency issues a “first payment.” As expected, the number of first payments has varied, consistent with changes in TUR (Figure 2.5). However, increasingly, the percentage of individuals who were eligible for and claimed UI benefits (i.e., claimants) and who received everything to which they were entitled (i.e., they “exhausted” benefits) did not track with changes in TUR and exceeded the exhaustion rates of prior recessions (Figure 2.6). This was probably due to both

Figure 2.3  Incidence of Long-Term Unemployment (more than 27 weeks)

SOURCE: USDOL/BLS data.
Figure 2.4 Average Duration on UI in the Regular Program

![Graph showing average duration on UI in the regular program from 1973 to 2013. The graph includes a line for the total unemployment rate (TUR) and a line for the average duration (R). Gray shaded areas represent recessions.](image)

NOTE: The gray shaded areas represent recessions.
SOURCE: USDOL/OUI and USDOL/BLS data.

Figure 2.5 People Receiving First Payments in the Regular UI Program

![Graph showing people receiving first payments in the regular UI program from 1973 to 2013. The graph includes a line for the total unemployment rate (TUR) and a line for the first payments (moving average). Gray shaded areas represent recessions.](image)

NOTE: The gray shaded areas represent recessions.
SOURCE: USDOL/OUI and USDOL/BLS data.
the increase in long-term unemployment and the fact that, with the maximum number of weeks of UI benefits having been cut in several states (see Table 2.1), individuals exhausted benefits earlier in their unemployment spell than they previously would have.

Evidence of the declining role of the program can be found when comparing UI claims data with the size of the civilian labor force and the TUR. The number of weeks of UI benefits claimed is expected to vary cyclically as TUR rises and falls. However, it would also be expected that, as the civilian labor force increases and with everything else being equal, the number of weeks of regular UI benefits claimed would increase because the pool of workers who may lose their jobs is increasing. However, as Figure 2.7 shows, this has not been the case. The trend in weeks of regular UI benefits claimed, other than the spikes during recessionary periods, is flat. Overall, the number of weeks claimed remained constant while the civilian labor force increased.
When data about the percentage of unemployed workers who received UI benefits (i.e., the “recipiency rate”) are examined, it becomes increasingly evident that, over time, fewer unemployed workers have been accessing UI benefits when they lose their jobs (Figure 2.8). As noted earlier, not everyone who loses their job is eligible for benefits. It would be expected that when the economy is in a downturn, layoffs become the dominant form of unemployment, and proportionately fewer individuals will become unemployed because they were fired for misconduct connected with work or because they

<table>
<thead>
<tr>
<th>State</th>
<th>Effective</th>
<th>Previous maximum (weeks)</th>
<th>New maximum (weeks)</th>
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<tr>
<td>AR</td>
<td>7/27/11</td>
<td>26</td>
<td>25</td>
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<tr>
<td></td>
<td>7/15/15</td>
<td>25</td>
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<tr>
<td>FL</td>
<td>1/1/12</td>
<td>26</td>
<td>12–23&lt;sup&gt;a&lt;/sup&gt;</td>
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<tr>
<td>GA</td>
<td>7/1/12</td>
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<td>14–20&lt;sup&gt;b&lt;/sup&gt;</td>
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<tr>
<td>ID</td>
<td>7/1/16</td>
<td>26</td>
<td>20–26&lt;sup&gt;c&lt;/sup&gt;</td>
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<tr>
<td>IL</td>
<td>1/1/12</td>
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<td>MI</td>
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<td>MO</td>
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<td>SC</td>
<td>6/19/11</td>
<td>26</td>
<td>20</td>
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<sup>a</sup> The number of weeks is tied to the unemployment rate.

<sup>b</sup> In Illinois, the number of weeks for 2012 was reduced to 25. For 2013, both the taxable wage base and the duration would have remained in place unless the state generated sufficient revenue to overcome a 2011 loss to the unemployment fund. Since Illinois generated sufficient revenue to overcome the loss, the benefit cut to 25 weeks only applied to 2012. The number of weeks increased to 26 weeks in January 2013 and has not changed.

<sup>c</sup> The number of weeks of benefits is equal to the number of credit weeks, up to a maximum of 26. Claimants with fewer than 18 credit weeks are not entitled to any benefits.

SOURCE: USDOL, Division of Legislation.
Figure 2.7  Weeks Claimed, Civilian Labor Force, and Total Unemployment Rate (TUR)

NOTE: The gray shaded areas represent recessions.
SOURCE: USDOL/OUI and USDOL/BLS data.

Figure 2.8  UI Recipiency Rates, All Programs (Insured Unemployed/Total Unemployed)

NOTE: The gray shaded areas represent recessions.
quit their jobs without good cause. Thus, recipiency rates would increase during recessions because proportionately more individuals become unemployed because they were laid off (i.e., because of a lack of work). However, as shown in Figure 2.8, the UI recipiency rate nationwide plummeted to less than 30 percent and was lower than it had been at similar points during economic recoveries in recent decades.

State-level data are even more striking. Because states have much discretion with respect to determining who is potentially eligible for UI benefits, it is not surprising that there is huge variation among the states with respect to recipiency rates. As shown in Figure 2.9, in the second quarter of calendar year 2016, the range of recipiency rates among the states went from less than 10 percent to more than 65 percent, with a national average of 28.6 percent.

Figure 2.9 Recipiency Rates by State (Insured Unemployed/Total Unemployed), Second Quarter 2016

SOURCE: USDOL/OUI and USDOL/BLS data.
UI Taxes and Solvency

The UI program is intended to operate counter-cyclically, with benefit payments increasing during economic downturns and funding reserves being built up when unemployment is low. Figure 2.10 shows how state tax rates, contributions (taxes) collected, and benefits paid varied since 2000 and the impact these factors had on trust fund balances. During the Great Recession, when trust fund balances were negative, most states borrowed from the federal government. In total, 36 states borrowed and the peak amount of the advances was $47.2 billion (Figure 2.11).

The primary reason for this impact on the trust fund was the severity of the Great Recession—some states would have become insolvent no matter how well they prepared in advance. However,

Figure 2.10 Contributions Collected, Regular Benefits Paid, Tax Rate on Taxable Wages, and Year End Net Reserve Balance (UTF), 2000 to 2015

the data demonstrate that had more states achieved an adequate level of solvency beforehand, fewer states would have run out of benefit funds and borrowing levels would have been much lower for the states whose economies were hard hit by the recession. The AHCM is the federal measure of state solvency, where an AHCM of 1.0 means that a state has a trust fund balance sufficient to pay benefits for one year during a recessionary period. Only about one-third of the states had an AHCM of at least 1.0 when the recession began (Figure 2.12). There were a few states that met this solvency standard that still borrowed from the federal government to pay UI benefits, but most of the states that borrowed did not meet the standard (Figure 2.13).

Between the economic recovery and the actions states took to increase revenue and decrease expenditures, there have been marked improvements in solvency in recent years. However, as of 2015 a couple of states still had outstanding UI debt, and most states (includ-
NOTE: An AHCM of 1.0 (the gray line) means that a state has a trust fund balance sufficient to pay benefits for one year during a recessionary period.

SOURCE: USDOL/OUI data.

UI Benefit Adequacy

Although there are no federal standards regarding the adequacy of UI benefits, there has been a long-standing recommendation that the weekly benefit amount (WBA) replace at least 50 percent of lost earnings over a six-month period, with a maximum WBA equal to two-thirds of the state’s average weekly wage (AWW) (U.S. Advisory Council on Unemployment Compensation 1996). At the national level, not only has that recommendation not been met during the last 40 years, there is a long-term declining trend in the replacement rate (Figure 2.15).

Another way to examine benefit adequacy is to examine recipiency rates (Figures 2.8 and 2.9). Of the many factors that influence
this rate, UI eligibility requirements, disqualification provisions, and the number of weeks of benefits available are among the most important. In recent years, several states enacted laws (ETA n.d.-c) that restrict access to the program in a multitude of ways, including raising qualifying earnings requirements, broadening the scope of what constitutes misconduct connected with work, and increasing the requirements needed to overcome a disqualification and reestablish eligibility for UI benefits. In addition, several states cut the maximum number of weeks of UI benefits (Table 2.1). In the past, states generally offered up to 26 weeks of benefits. About one-quarter of the states now offer fewer than 26 weeks. In several states, the maximum available depends on the unemployment rate. For example, in North Carolina, as few as 12 weeks of benefits will be available under certain circumstances.
As should be evident from the above discussion, the UI program has deviated from historical standards and its original goals, resulting in an erosion of the social safety net for jobless workers. The proposals detailed in the following section were designed to address several of the most important causes of these problems.

BUDGET PROPOSALS AND ANALYSIS

Solvency

From the brief examination of the data in the previous section, it should be clear that states are not prepared for the next recession because they don’t have sufficient funds to pay benefits when demands are high. Most states’ UTF accounts do not meet the federal
The FY 2017 Obama Budget recognized the importance of states having sufficient reserves to pay benefits, to avoid borrowing, and to avoid large increases in employer taxes when economic conditions are weak or recovering, so it included a set of legislative proposals to address solvency. First, in 2017, it would have restored the 0.2 percent FUTA surtax, which would help the federal accounts in the UTF pay their outstanding debts. For example, as of November 10, 2016, the Extended Unemployment Compensation Account owed $7.2 billion to the General Fund of the U.S. Treasury and $7.5 billion to the Federal Unemployment Account. Since the amount of wages subject to unemployment taxation at the state level is closely related to the corresponding amount at the federal level, there was also a proposal to increase the federal taxable wage base to $40,000 in 2018 (at present, it is $7,000) and to index it to inflation in subsequent years. By itself, this would have a limited effect on state

**Figure 2.15 Average Weekly Benefit, Average Weekly Wage, and UI Replacement Rate, 1970 to 2015**

SOURCE: USDOL/OUI data.
solvency, but it was expected that the change would encourage states to take action to improve their solvency. However, it would have more equitably allocated the tax burden among employers. When a taxable wage base is low, employers with more low-wage or part-time workers pay unemployment taxes on a larger portion of employee earnings than employers with more high-wage or full-time workers.

An additional proposal would have required states to impose a minimum tax per employee equal to 0.175 percent of taxable wages, thereby spreading the cost of UI more widely among all employers. At present, many states allow a significant portion of employers with the best unemployment “experience” to pay a zero tax rate. Not only does this hamper efforts to improve solvency, but it undermines the fundamental principle of insurance—paying a premium to insure against the risk of an event occurring, in this case, the risk of unemployment. As it is for other types of insurance, premiums reflect the likelihood of an event happening. However, contributions are made on behalf of everyone covered by the insurance because everyone has the benefit of potential access to funds if the insured event occurs.

Another proposal to help states attain solvency in the FY 2017 budget was to reduce the FUTA credit available to employers when a state had an AHCM of less than 0.5 on January 1 in two consecutive years, with the additional amounts paid being used to bolster the state’s account in the UTF. This process would be similar to that used to reduce FUTA credit to help states pay back their outstanding advances to pay UI benefits.

To avoid a massive federal tax increase when the federal taxable wage base increases, the proposal would have decreased the effective FUTA tax rate to 0.167 percent. However, FUTA revenue would have gradually increased over time as the federal taxable wage base increased after indexing. This would have mitigated the likelihood of future borrowing from the General Fund of the U.S. Treasury, because the administrative and benefits costs paid from the federal accounts in the UTF would increase over time as well.
Benefit Adequacy

As described above, UI claims have plummeted. They have reached the lowest level since the 1970s. For example, in October 2016, initial claims were below 300,000 for more than 85 consecutive weeks—the longest streak since 1970 (USDOL 2016). Although much of the reduction in claims is due to improving economic conditions, actions by several states to cut benefits and restrict eligibility also were factors. For this reason, the FY 2017 Obama Budget included a set of proposals designed to expand access to UI benefits and services. First, it would have established the following federal requirements:

- States must provide at least 26 weeks of benefits for the regular program.23

- States must adopt the following three provisions for which UI Modernization incentive payments were made available under the American Recovery and Reinvestment Act (ARRA):
  1) Use an alternative base period.
  2) Allow benefits to individuals who seek part-time employment.
  3) Allow unemployed workers to be eligible for benefits if they leave their jobs for family reasons.

Increasing the number of weeks of benefits back to the historic norm is important because it takes time for an individual to find a job, even in a good economy. Moreover, it is beneficial to both the individual worker and the economy as a whole if workers are able to take the time to find jobs that align well with their skills, education, and experience. These workers would be able to increase their contributions to society, as well as better provide for themselves and their families. Additional weeks of UI benefits would also result in increased macroeconomic stabilization.
To understand the importance of the alternative base period proposal, it is important to note the history and evolution of monetary determinations. Before employers began reporting their employees’ quarterly earnings to the states (ETA 1984), the UI base period used to determine whether an individual earned enough to qualify for benefits was generally the most recent 52 weeks before the individual filed a claim. Although this procedure was more administratively challenging because states had to contact employers to get this information about each individual applying for UI benefits, it more accurately captured the individual’s recent attachment to the workforce. When states transitioned to establishing eligibility based on quarterly wage reports, administrative necessity forced states to use more remote work experience when making this determination. Before electronic reporting was possible, employers had to mail paper copies of wage information. Given the lag between when a calendar quarter ended and when the state could reasonably expect to have wage information from most employers, states opted to consider wages earned during the first four of the most recent five completed calendar quarters. As technology has advanced and employers report increasingly sooner after the end of the calendar quarter, this administrative constraint has largely disappeared. Therefore, administrative issues such as this should no longer be the deciding factor for a UI benefit eligibility requirement. Using the most recent available reported earnings data more accurately measures a worker’s present attachment to the workforce and should be the basis for determining who qualifies for UI benefits (Carr 2016). As of 2016, 37 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands already used alternative base periods when making monetary determinations (ETA 2016b).

The remaining proposed requirements were designed to help the UI program better reflect the twenty-first century economy. In the 1930s, the single breadwinner model was typical for most families—very different from today’s conditions. With that construct in mind, and with the intent to design a program that provided benefits only to individuals who became and remained unemployed involuntarily,
individuals who left their jobs for personal reasons or who were only working part time were not considered to be genuinely attached to the labor force. While the risk that is insured by the UI program today remains the same— involuntary unemployment—the way in which that concept is defined should be reexamined. In particular, with an increasing number of two-earner families, the meaning of labor-force attachment has changed. For example, it is hard to argue that quitting a job to move across the country when a spouse’s job necessitates the move is voluntary. Maintaining a family unit is paramount and does not equate with a decision to leave the workforce. In this type of circumstance, since the individual’s employer did not cause the unemployment, the UI benefits paid may be “non-charged” (i.e., won’t be taken into account when determining the employer’s state unemployment tax rate). However, denying benefits to such individuals would be inconsistent with the goals of the UI programs and the values of our society.

Similarly, regardless of economic necessity or overall preference, the demands of family life or older workers’ transition to retirement often require some individuals to work part time. This does not automatically equate with a weak or casual connection to the workforce. For this reason, if individuals earn enough to qualify for UI benefits and meet all other requirements, making them ineligible because they are only available for part-time work also would be out of line with the principles upon which the UI program is based (Michaelides and Mueser 2009).

The FY 2017 Obama Budget also provided for a new $5 billion Modernization Fund. To become eligible for its share of funds, a state would have had to:

- allow for broader federal access to wage records;
- adopt employer electronic filing and/or increased penalties for employer nonreporting; and
- have a definition of “misconduct” that conforms to a USDOL model.
In recent years, UI wage records are increasingly being used to evaluate and measure the performance of a vast array of public programs. Evidence-based decision making regarding investment of public funds requires access to high-quality, comprehensive data, which is why the first two prerequisites were chosen.

When determining whether individuals became unemployed through no fault of their own, the state must decide whether the reason an employee was fired was “misconduct connected with work,” which would disqualify them from receiving benefits—typically for their entire spell of unemployment. Although there are many reasons why an employer may legitimately and legally fire a worker, only a small subset of those reasons would constitute misconduct connected with work. Historically, states generally defined misconduct connected with work narrowly in line with the definition in *Boynton Cab Co. V. Neubeck*, 237 Wis. 249 (Wis. 1941):

> [T]he intended meaning of the term “misconduct” . . . is limited to conduct evincing such willful or wanton disregard of an employer’s interests as is found in deliberate violations or disregard of standards of behavior which the employer has the right to expect of his employee, or in carelessness or negligence of such degree or recurrence as to manifest equal culpability, wrongful intent or evil design, or to show an intentional and substantial disregard of the employer’s interests or the employee’s duties and obligations to his employer. On the other hand, mere inefficiency, unsatisfactory conduct, failure in good performance as the result of inability or incapacity, inadvertencies or ordinary negligence in isolated instances, or good-faith errors in judgment or discretion are not to be deemed “misconduct” within the meaning of the statute.

Some states have significantly broadened the definition of misconduct connected with work, which has had the effect of disqualifying more workers from receiving UI benefits. To be eligible for its share of the Modernization Fund, a state’s definition would have to conform to the federal definition.
In addition to the prerequisite requirements, to receive a Modernization Fund payment, states would have had to adopt one benefit expansion and two pro-work reforms. The benefit expansions were:

1) allow more individuals to receive UI benefits while participating in training;

2) provide a maximum WBA equal to at least two-thirds of the state’s AWW during the most recent 12 months; or

3) improve eligibility for temporary workers.

Recognizing that training may increase the likelihood of reemployment and the quality of the job obtained, federal UI law prohibits states from making individuals ineligible because they are not available for work or actively seeking work while they are in training approved by a state agency.26 States would have sole authority to determine which types of training to approve for this purpose, but this proposal would have given states an incentive to expand the scope of training they approve.

The formula established in many states’ UI laws to determine the WBA is generally designed to replace one-half of a worker’s weekly wage (ETA 2016c). This amount helps jobless workers meet the necessities of life without providing a disincentive to work (Chetty 2008). However, regardless of the WBA the formula would generate based on an individual’s wage history, the maximum amount is capped. In some states, the maximum WBA is a fixed amount that can only be changed by enacting a state law. In other states, the maximum WBA changes each year because it is set as a specified percentage of the AWW. Ensuring that the maximum WBA increases are consistent with increases to the state AWW avoids an erosion of benefits, particularly for middle income workers.

Some states establish additional requirements in order for temporary workers to be eligible for UI benefits. The FY2017 Obama Budget was designed to ensure that such requirements didn’t become a barrier to temporary workers getting benefits.
States would have had to adopt two of the following five pro-work reforms to qualify for an incentive payment:

1) progressively more intense reemployment service delivery as duration of benefit receipt lengthens;
2) improved reemployment services for UI claimants;
3) subsidized temporary work programs;
4) relocation assistance coupled with individual case management, in-person career counseling, provision of customized information about job opportunities, and referrals to suitable work; or
5) improved data systems for workforce and education program performance, research, and evaluation purposes.

From its inception, the UI program has been closely tied to the U.S. Employment Service because, unless workers are on a temporary layoff, it is imperative to help them find jobs, which is the rationale for the first two options. The next two options represent alternative ways to help individuals find work—via temporary work programs and relocation. The last pro-work choice was premised on workforce and education programs becoming more effective at giving people the knowledge and skills they needed to become reemployed if data were used more effectively when evaluating, researching, and assessing the performance of these programs.

Extended Benefits

EB does not function effectively because it doesn’t trigger on soon enough (or at all) in states with high unemployment. Since its inception in 1970, special federal programs providing additional weeks of benefits were created during each major downturn and were effective during the periods 1972 to 1973, 1975 to 1978, 1982 to 1985, 1991 to 1994, 2002 to 2004, and, most recently, 2008 to 2013 (ETA n.d.-d). Implementing these temporary federal programs poses several chal-
challenges. Foremost of these, it takes too long. It takes several months for sufficient economic information to become available to demonstrate need and design an extension program; legislation to be drafted, passed by Congress, and enacted into law; the USDOL to develop operating instructions and guidance; and the states to implement the new program. In addition, in these temporary federal programs, some portion of the benefits is generally available in all states, rather than targeting all benefits only to the states experiencing higher unemployment. Moreover, without knowing the program parameters of a new extension, states do not have sufficient time to prepare to implement and administer these special federal programs, which leads to further delays, public confusion, and occasionally errors. In short, while providing vital benefits to jobless workers and their families, these ad hoc programs do not provide for efficient and timely macroeconomic stabilization.

To obviate the need for hurried enactment of temporary federal UI extension programs, the FY 2017 Obama Budget included a proposal to reform the EB program. Specifically, it would have:

- Provided for four 13-week tiers of benefits, with availability depending on the state’s TUR.
- Provided permanent 100 percent federal funding of EB with nonrepayable advances from the General Fund if there were insufficient amounts in the federal account in the UTF.
- Established new TUR trigger thresholds of 6.5, 7.5, 8.5, and 9.5 percent. These thresholds would have been met if the state’s TUR met or exceeded one of those levels or if the total of the state’s TUR and the change in the TUR from a comparable period in one of the previous two years equaled or exceeded one of those levels.
- Required reemployment services and eligibility assessments for all EB claimants.
These proposals drew largely on experience from the Great Recession—not just with EB, but also with the Emergency Unemployment Compensation (EUC) program (ETA n.d.-e). At its peak, EUC was a four-tiered program providing up to 53 weeks of benefits, depending on the state’s TUR. After the federal account ran out of funds to pay for EUC, it was paid with funds from General Revenue that did not have to be repaid.28 The triggers changed over time. Most recently, Tier 1 had no trigger, and Tier 2 triggered on in states with a three-month TUR of at least 6.0 percent. For Tier 3, the rate was at least 7.0 percent, and for Tier 4, it was 9.0 percent.

The EB triggers failed for several reasons. First, even with the TUR-based triggers, it took too long for EB to become available in many states. The EUC program was first enacted in June 2008, six months after the Great Recession began.29 In January 2009, most states still hadn’t triggered onto EB—more than one year after the recession began (ETA n.d.-f). Related to this concern is that too few states had a TUR trigger in their laws before the recession began. One of the most important EB-related provisions in ARRA was temporary 100 percent federal funding of EB.30 As a result of the 100 percent federal funding, 29 states amended their EB laws to provide for temporary TUR triggers conditioned on 100 percent federal funding. The final negative consequence of the design of the EB triggers is the fact that states with sustained high unemployment eventually triggered off EB. To remain on EB, a state’s TUR must not only meet or exceed certain levels, but the rate had to be higher than it had been during comparable periods in the prior year or two. With the impact of the Great Recession lasting for such a long time, the unemployment rates in some states, while high, were not higher than they had been during the previous two years. Even though federal law was amended to allow states to use a three-year “lookback,” and 33 states amended their laws to provide for it, the longer lookback eventually became insufficient, and this component resulted in EB no longer being available to long-term unemployed workers in states with sustained high unemployment (ETA 2012).
Recognizing the importance of helping individuals find jobs, in particular the long-term unemployed, and ensuring that they continue to meet all eligibility requirements, the EUC program was modified in 2012 to require all new EUC claimants to receive reemployment services, and reemployment and eligibility assessments (ETA n.d.-g). This is the reason the EB proposals in the FY 2017 Obama Budget would have required reemployment services and eligibility assessments for all EB claimants.

Reemployment

The increases in long-term unemployment, average duration, and exhaustion rates demonstrate the need for strategies designed to assist with reemployment efforts for individuals who become unemployed. Building on the initiative that began in 2005 in a few states and national implementation in 2012 for individuals receiving EUC, the FY 2017 Obama Budget proposed making the RESEA program a permanently authorized program that would have required all states to participate and would have provided enhanced funding to enable more individuals to be served. For the regular UI program, the one-third of new claimants who would have been identified as the most likely to be long-term unemployed and in need of reemployment services would have been required to participate in RESEAs as a condition of eligibility for UI benefits.

Recognizing the importance of helping transitioning veterans find employment in the civilian labor force, the FY 2017 Obama Budget also proposed requiring all new claimants for the Unemployment Compensation for Ex-Servicemembers program to participate in RESEAs as a condition of eligibility for UI benefits.

The FY 2017 budget included another proposal designed to encourage reemployment—wage insurance. Particularly for workers transitioning to new occupations, new jobs might pay significantly less than the jobs individuals had prior to becoming unemployed. To provide a safety net to such workers and to encourage their swift
reemployment, this wage insurance proposal would have been available to individuals who had been working for at least three years with their prior employer. If their new job paid less than $50,000 per year, workers would have received a payment equal to half the difference between their prior and new annual wage, up to $10,000 over a period of two years.

**Short-Time Compensation**

The experience during the Great Recession highlighted the importance of helping workers to keep their jobs. While many states did avail themselves of the STC-related funding opportunities in the Middle Class Tax Relief and Job Creation Act of 2012, and a few states created new STC programs, not all did. Although there are a variety of explanations, one of the most meaningful is timing. To implement a new program requires an extensive time commitment. In 2012 and 2013, states had limited capacity to take on new initiatives, given the high workload and the complex modifications to the EUC program that they had to administer, among other reasons. Since economic conditions improved significantly after recovery from the Great Recession, states were in a much better position to consider commencing STC programs or improving existing ones. For this reason, the FY 2017 Obama Budget included proposals to give states an additional two years of federal reimbursement of STC benefit costs and two more years to apply for and receive STC grants. In addition, there was a proposal to make state STC benefit costs subject to 50 percent federal reimbursement whenever the state triggered on the EB program.

**Integrity**

Despite states’ best efforts, many challenges remain to prevent improper payments. The FY 2017 Obama Budget included a set of highly technical proposals related to benefit integrity that built on
recent enactments. They were designed to provide states with additional resources to dedicate to this purpose and to ensure that states used all of the tools at their disposal to combat this issue. Specifically, they would have:

- allowed states that contracted out all information technology functions to use the Treasury Offset Program for benefit overpayment recovery;
- required states to use an electronic system to transmit information with employers to obtain information needed to determine benefit eligibility;
- required states to use the National Directory of New Hires to find individuals who continued to claim benefits after returning to work and to require penalties on employers that did not report their new hires;
- allowed the USDOL to require that states whose poor program performance required creation of corrective action plans to dedicate specified amounts of their administrative grants to implementing those plans, and to provide awards or incentives to states with excellent performance;
- required states to use UI penalty and interest funds for UI administration with a portion dedicated to program integrity activities;
- required states to cross-match UI claim information with the Prisoner Update Processing System to find individuals who were claiming benefits while incarcerated; and
- allowed states to use up to 5 percent of recovered overpayments or delinquent employer contributions collected for integrity purposes rather than for future benefit payments.
CONCLUSION

As is evident from this brief description and analysis, the FY 2017 Obama Budget included an ambitious set of UI legislative proposals that focused on many of the most profoundly meaningful aspects of the program. Opinions will certainly vary about those proposals from both a substantive policy perspective as well as from an ideological perspective. However, when considering UI’s philosophical underpinnings, it should be clear that many of these proposals could bring the current UI program into better alignment with its foundational principles, given the economic, societal, and technological changes that have occurred during the more than 80 years since the inception of the UI program in 1935. Moreover, by raising the profile of some crucial issues and setting forth a comprehensive plan for addressing them, public dialogue and debate might yet be encouraged and result in permanent positive reforms to the UI program.

Notes

The opinions expressed in this chapter are the author’s alone. They do not purport to reflect the official position or views of the U.S. Department of Labor. Many thanks are given to Daniel Hays in the Division of Legislation of the U.S. Department of Labor’s Office of Unemployment Insurance for his assistance with research. Thanks also to Ed Dullaghan in the Division of Fiscal and Actuarial Services of the U.S. Department of Labor’s Office of Unemployment Insurance for creating and updating all of the figures.

1. Although this overview addresses many key aspects of the UI program, it mainly focuses on the aspects of the program pertinent to the reform proposals discussed in this paper. It is not comprehensive and is intended to provide the information necessary to understand the issues that presently exist and how the proposals were intended to address them.
2. Washington State does not determine UI eligibility based on earning wages equal to or exceeding a specified amount. Instead, state law requires an individual to have at least 680 hours of base period employment.
3. Following the enactment of the American Recovery and Reinvestment Act, 23 states enacted new or modified existing alternative base periods.

4. Alaska, New Jersey, and Pennsylvania levy nominal UI taxes on workers under certain limited circumstances. In Alaska, the tax rate is equal to 27 percent of the average benefit cost rate, but not less than 0.5 percent or more than 1.0 percent of taxable wages. In New Jersey, the tax rate is 0.3825 percent. Depending on the adequacy of the fund balance in a given year, Pennsylvania employees pay contributions ranging from 0.0 percent to 0.08 percent of total gross covered wages earned in employment.

5. Until June 2011, the FUTA tax was 6.2 percent and the effective FUTA tax rate was 0.8 percent. A 0.2 percent “surtax” was originally added in 1985 to help the federal accounts in the Unemployment Trust Fund (UTF) pay back their advances from the General Fund of the U.S. Treasury. Between advances to states and federal benefit spending during the Great Recession, the federal accounts in the UTF ran out of funds and had to borrow to meet all obligations.

6. At the onset of the program, the FUTA tax was 1.0 percent on total wages with an effective rate of 0.1 percent. In 1939, the FUTA taxable wage base was set at $3,000, which exceeded the annual wages of 98 percent of workers. According to USDOL estimates, FUTA taxable wages in 2015 represented less than 17 percent of total wages in the United States.

7. States may use other state funds or may borrow from other sources to pay UI benefits. During the Great Recession, Colorado, Illinois, Michigan, Nevada, Pennsylvania, and Texas borrowed via bonding. On December 31, 2013, the outstanding bond amount for these states was $9.725 billion.

8. If on November 10 of the year in which on a second consecutive January 1 a state has a remaining outstanding Title XII advance balance, the state’s FUTA credits will begin to be reduced in the subsequent year to repay the outstanding debt.

9. The state must apply for and be found eligible for relief from tax credit reduction in the form of avoidance or a cap on reduction (26 U.S.C. 3302 and Social Security Act, Section 901(d)(1)).

10. There is an incentive in 20 C.F.R. 606.32 for states to maintain a solvent account in the UTF. Without meeting the funding goals prescribed by this regulation, any Title XII advance that a state receives is interest accruing.

11. The program was created in the Federal-State Extended Unemployment Compensation Act of 1970.

12. FUTA revenue in the Extended Unemployment Compensation Account is used for this purpose.


16. It is important to note that the workers who would not have been laid off (typically those with most seniority) experience a reduction in their income that they otherwise wouldn’t have. However, the fact that most states require labor union approval of STC plans if the workplace is subject to a collective bargaining agreement demonstrates the overall support for STC because it helps workers (typically the most junior) avoid becoming unemployed. Anecdotal evidence indicates that workplace morale often improves when an agreement is reached to avoid layoffs by reducing hours and offering STC.

17. STC payments are treated like unemployment compensation (UC) payments. Thus, they are deducted from an individual’s maximum benefit amount during a given benefit year, which would reduce the number of weeks of UC available should the individual later become unemployed. Similarly, under permanent law, STC payments are “charged” to employers’ accounts for purposes of determining their experience-rated state UC tax rate in the same way UC payments are charged.


19. The figures contained in this section were prepared by staff in the Division of Fiscal and Actuarial Services utilizing ETA and BLS data.

20. The AHCM is calculated by dividing the Calendar Year Reserve Ratio (or “Trust Fund Balance as a percent of Taxable Wages”) by the Average High Cost Rate.

21. The material in this section draws on USDOL (2017b).

22. To a certain extent, this is an inherent design feature of insurance. It generally is not expected that premiums would cover the full cost of the benefits. However, it is widely acknowledged that excessive levels of socialized costs due to ineffective charging and insufficient maximum tax rates to reflect employer experience with unemployment result in some employers paying for a smaller portion of benefits than others. Also, it is important to note that for UI purposes, certain entities are permitted to self-insure. State or local governmental entities, 501(c)(3) nonprofit organizations, and Indian tribes may opt to reimburse benefit costs rather than be assessed a contribution rate.

23. Regular benefits are paid at the beginning of a spell of unemployment. This is in contrast to programs like EB, which are available to individu-
als who exhaust entitlement to regular benefits in states whose unemploy-
ment rate exceeds certain levels.
24. Consistent with the insurance principle of the UI program, states have
been allowed to have “non-charged” UI benefit payments when the
employer is not at fault for the spell of unemployment. A typical reason
has been when benefit payments are made to individuals who quit for
good personal cause.
25. Older workers increasingly are taking part-time “bridge jobs” after they
leave their career jobs and before they fully retire.
27. Since enactment of the Workforce Investment Act of 1998, the Employ-
ment Service has been incorporated into the one-stop career center
system. For additional information, see http://research.upjohn.org/cgi/
viewcontent.cgi?article=1032&context=reports (accessed March 24,
2018).
28. Although it was expected that the proposal to improve federal solvency
would generally obviate the need for General Revenue, during severe
recessions that might not have been the case, and such funds would have
become available under this EB proposal.
(accessed March 24, 2018).
30. Although EUC eventually was funded with General Revenue, federal
EB costs continued to be funded by FUTA revenue in the EUC Account.
When those funds were depleted, the federal accounts in the UTF bor-
rowed from the U.S. Treasury to meet its obligations.
31. Federal law presently requires states to operate the worker profiling
and reemployment services program, which identifies claimants likely
to exhaust benefits and need reemployment services to find work, and
requires such individuals to participate in those services as a condition
of UI eligibility.
32. Since state UI programs do not cover individuals who work for the fed-
eral government, there are separate federal UI programs to provide ben-
efits to such workers when they become unemployed. States administer
these programs under an agreement with the USDOL. One such pro-
gram is Unemployment Compensation for Ex-Servicemembers.
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