# Work Incentives and Disincentives

Paul T. Decker
*Mathematica Policy Research*

# Work Incentives and Disincentives

Paul T. Decker
*Mathematica Policy Research*

The unemployment insurance (UI) system must address a funda-
mental trade-off between two important factors: (1) the need to provide
unemployed workers with benefits that are "adequate," as discussed in
Chapter 5, and (2) the need to minimize the disincentive to rapid reem-
ployment implicit in the provision of UI benefits. The intent to provide
adequate benefits tends to encourage more generous ones, which
would ensure that the economic needs of a larger proportion of claim-
ants are met. However, more generous benefits tend to strengthen the
reemployment disincentive. Given this trade-off, states have been
urged to provide benefits high enough to replace a substantial portion
of lost wages, but not so high as to significantly dilute the incentive to
return to work. As a result, a "rule-of-thumb" that has guided UI policy
since the inception of the system is that weekly UI benefits should
replace roughly 50 percent of workers' weekly wages.

This chapter reviews the theory and empirical evidence on the
effects of UI policy on the behavior of unemployed workers in order to
investigate the following issues:

- Whether and the extent to which more generous benefits act as a
  disincentive to reemployment, thus prolonging unemployment and
  increasing the unemployment rate
- Whether prolonged unemployment can have a positive impact by
  leading to higher-paying work if claimants use the period of unem-
  ployment to select the best possible job
- Whether the negative effects of UI on reemployment are offset by
  effects of UI on labor market transitions other than the unemploy-

ment-to-employment transition or by spillover effects of claim-
ants' behavior on unemployed workers who do not receive UI
benefits

The discussion then turns to policy options that have evolved in
response to the reemployment disincentive that is inherent in UI and
concludes with a consideration of the task faced by policy makers in
light of the theoretical and empirical evidence on the effect of UI on
employment.

## Direct Effects of Unemployment Insurance
## on Claimants: Disincentives to Reemployment

Theoretical studies have demonstrated that more generous benefits
create an incentive for claimants to remain unemployed, and empirical
studies have shown that UI does indeed tend to lengthen unemploy-
ment spells of claimants. Increases in either the amount of benefits or
in the potential duration of benefits induce longer spells, but the magni-
tude of these effects is still uncertain. In this section, both the theory
and empirical findings related to this effect are reviewed.

### Theory

The theory supporting the disincentive effect of UI is based on the
premise that UI tends to prolong unemployment spells because it low-
ers the cost of unemployment. Unemployed workers who receive UI
benefits tend to consume more leisure, to reduce the intensity (and
therefore the cost) of their job search, or to be more selective in accept-
ing a job offer than they would be in the absence of UI. All of these
tendencies will generate longer unemployment spells. Increasing the
two key parameters of the UI system—the amount and potential dura-
tion of benefits—would tend to exacerbate this effect.

Two general theoretical models, the labor-supply model and the job-
search model, have been used to describe the disincentive to reemploy-
ment inherent in UI. Moffitt and Nicholson (1982) utilized a labor-sup-
ply model to represent the effect of UI on the duration of
unemployment spells. In this model, a newly unemployed individual is

assumed to plan his or her activities over a fixed period, deciding how to divide his or her time between work and leisure in the form of unemployment. During the period, the individual may either consume the maximum amount of leisure by remaining unemployed for the full interval or accept a job that is to begin at a particular point, remaining unemployed until that point.

In the labor-supply model that includes UI, the budget constraint relevant to individuals who are eligible for UI and are planning employment-related activities over period $T$ is represented by line $ABC$ in figure 7.1. For an unemployment spell that exceeds the point at which UI benefits are exhausted, which is typically 26 weeks after the initial claim, the cost of an additional week of unemployment is the foregone earnings for that week. The individual worker is assumed to receive a fixed weekly wage, $w$, when employed, and this fixed wage represents the earnings foregone for a week of unemployment. For an unemployment spell that is less than 26 weeks, the net cost of an additional week of unemployment is $w$-$b$, where $b$ is the weekly UI benefit received by the claimant. The relatively lower cost of unemployment during periods of benefit receipt represents the unemployment subsidy of UI.

The labor-supply model can be used to show that making UI benefits more generous (by increasing either the amount or potential duration of benefits) will increase unemployment spells of claimants. An increase in the weekly benefit amount tends to lengthen unemployment spells because it lowers the net cost of unemployment. The effect of the weekly benefit increase is represented in figure 7.1 by the shift of the budget constraint out to line $AB'C'$. For claimants who would exhaust benefits if the weekly benefit were not increased—that is, those between $B$ and $C$ on the original line—the increase in the benefit amount causes a pure income effect that raises consumption of leisure/unemployment, as long as leisure is a normal good. For claimants who would not exhaust benefits if the weekly benefit were not raised— those located between $A$ and $B$ on the original line—the benefit expansion generates both substitution and income effects in the same direction, thus increasing unemployment.

As is true for an increase in the amount of benefits, an increase in potential duration of benefits tends to lengthen unemployment spells, by extending the period in which the cost of unemployment is lowered by the availability of benefits. If, for example, the potential duration of

benefits were increased from 26 to 39 weeks, the budget constraint in figure 7.1 would shift to line $AB''C''$. The only claimants who would be affected by the shift are those who would have exhausted benefits in the absence of the shift. For these claimants, the income and substitution effects of the shift are also in the same direction—toward greater unemployment—so the impact of a longer potential benefit period is to unambiguously increase unemployment.

**Figure 7.1  Impact of Increases in UI Benefit Parameters on the Budget Constraint for UI Claimants**
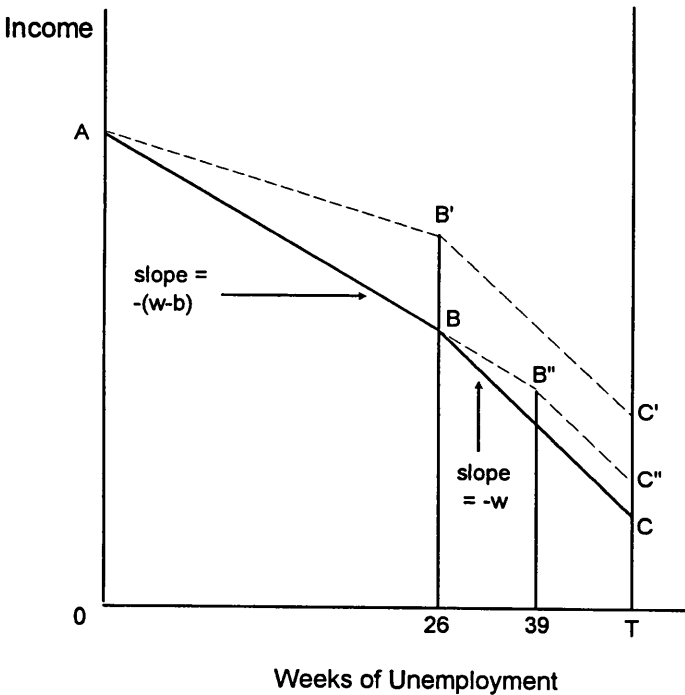


The labor-supply model further implies that many claimants will return to work near the time that they exhaust their benefits. Reemployment is likely to occur at this point because of the sudden increase in the cost to claimants of an additional week of unemployment when
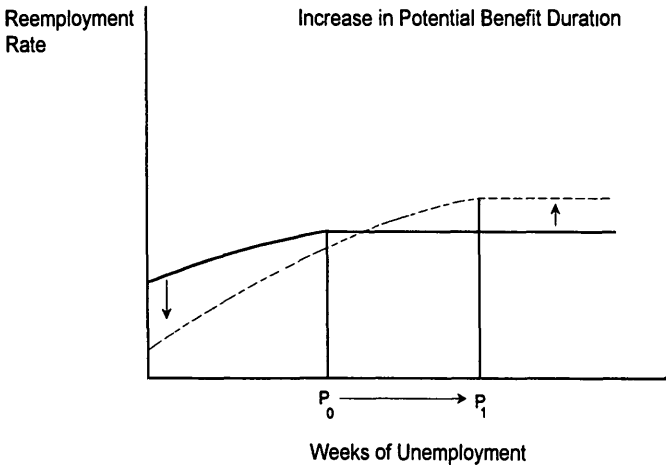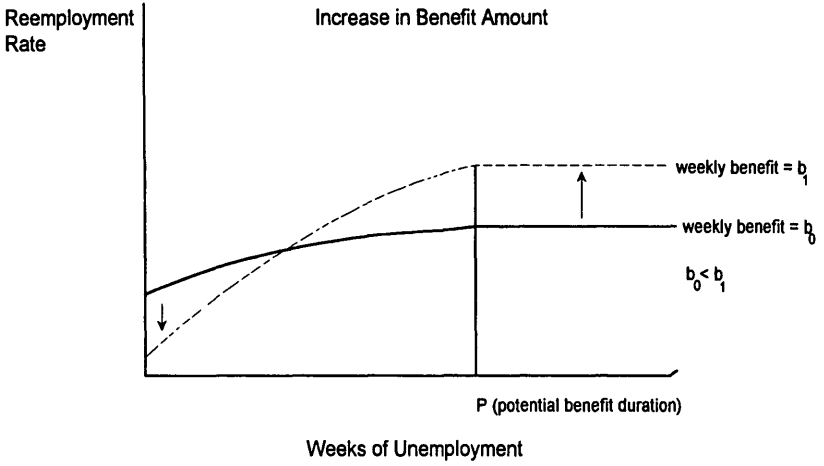
benefits are exhausted. This is represented by the kink in line *ABC* in figure 7.1. Many claimants will respond to this increase in the cost of unemployment by accepting a job or at least by searching more actively.[1]

An alternative approach to modeling the effect of UI on unemployment spells is based on the job-search model (Burdett 1979 and Mortensen 1977). In this model, it is assumed that the search occurs in an environment in which claimants are uncertain about the wage offers they will receive from one week to the next. Given such uncertainty, unemployed workers set their search intensity and their minimum acceptable wage so as to maximize the present value of lifetime income. It follows that claimants will end their unemployment spell when they receive a wage offer that exceeds their minimum acceptable wage.

In the job-search model, UI lowers the cost of unemployment and therefore encourages claimants to reduce the intensity of their search or to raise their minimum acceptable wage. Either response tends to prolong unemployment spells. In addition, an increase in the amount or potential duration of benefits will strengthen the reemployment disincentive. The resulting impact on rates of reemployment is illustrated in figure 7.2, which presents the time pattern of reemployment for UI claimants. The top panel shows that an increase in the benefit level tends to lower reemployment rates early in unemployment spells and to increase reemployment rates near and beyond the point of benefit exhaustion, *P*. The bottom panel shows that an increase in potential duration of benefits from $P_0$ to $P_1$ also decreases reemployment rates early in the unemployment spell and increases subsequent reemployment rates. The overall impact of these changes in reemployment rates would be to raise average unemployment spells.

Although both the labor-supply theory and the job-search theory imply that UI is likely to prolong unemployment spells, the job-search theory also suggests that prolonged unemployment spells can have a positive impact. Because UI provides financial assistance to claimants, they can presumably be more selective in taking a new job than they would be in the absence of UI. That is, because of UI, claimants can spend more time searching for the best possible job opening. If, as a result, claimants obtain more stable or higher-paying jobs than they would in the absence of UI, the prolonged unemployment spell has

**Figure 7.2  Impact of Increases in UI Benefit Parameters on Reemployment Rates**



Increase in Benefit Amount

weekly benefit = $b_1$

weekly benefit = $b_0$

$b_0 < b_1$

P (potential benefit duration)

Weeks of Unemployment

Increase in Potential Benefit Duration

$P_0 \longrightarrow P_1$

Weeks of Unemployment

been productive. Hence, if the job-search model is valid, and UI constitutes a subsidy to job search rather than to leisure, a full evaluation of UI must weigh the benefits of increased search against the costs of increased unemployment.

The reemployment disincentives inherent in UI are intended to be offset somewhat by partial benefit schedules that allow claimants to accept part-time work and to still retain a portion of their UI benefits. However, partial benefit schedules, which vary by state, have been criticized because they do not create clear incentives for partial benefit claimants to work as much as possible. The effect of the typical partial benefits schedule on the relationship between a worker's earnings and income (earnings plus benefits) is shown in figure 7.3. Claimants with zero earnings have income equal to their full weekly benefit amount (WBA). A small amount of earnings, up to one-quarter of WBA in figure 7.3, is disregarded in computing the partial benefit amount, so a one-dollar increase in earnings generates a one-dollar increase in income over this range. For earnings above the disregard, the benefit payment is reduced by a dollar for each additional dollar of earnings; the earnings-income function in figure 7.3 is flat over this section, as earnings simply displace benefits. Benefits are eliminated altogether if earnings exceed WBA. The effect of this elimination of benefits, combined with the earnings disregard, is to create a point where a marginal increase in earnings causes a decline in income. This is reflected in the discontinuity in the earnings-income function at the point where earnings equal WBA in figure 7.3.

Two aspects of the partial benefit schedule can be criticized for impeding work incentives. First, workers on the flat section of the earnings-income function have no incentive to increase earnings at the margin, since the gain in earnings has no effect on income. Second, the discontinuity where earnings equal WBA creates a disincentive to raise earnings at the margin, since that increment will generate a decrease in income. Munts (1970) presents data from Wisconsin on benefit receipt that suggest that claimants are responsive to the work disincentives created by partial benefits schedules.

The simplest way to maintain work incentives is to construct a partial benefits schedule without an earnings disregard that reduces benefits by a fraction of one dollar for every one-dollar increase in earnings. A benefits schedule of this type will create a relatively smooth,

upward-sloping earnings-income function, ensuring that as earnings increase income will also increase and benefits will be phased out gradually. This type of benefits schedule is used in Kentucky, where claimants lose 80 cents in benefits for every additional dollar of earnings.

**Figure 7.3  Example of a Partial UI Benefits Schedule**
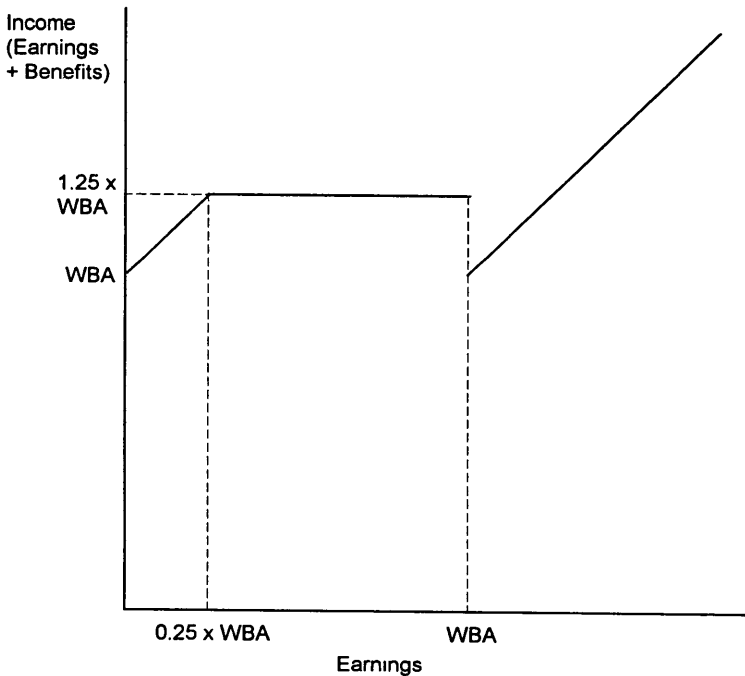


WBA = Full weekly benefit amount

*Empirical Evidence*

Over the past twenty years, many researchers have studied empirically the impact of UI benefits on unemployment spells. Danziger, Haveman, and Plotnick (1981), Gustman (1982), Burtless (1990), and Atkinson and Micklewright (1991) summarize the literature before the

**Table 7.1 Estimated Impacts of UI Benefit Parameters**

| Study | Data used | Estimation methods | Impact of weekly benefit amount | Impact of potential benefit duration |
|---|---|---|---|---|
| Newton and Rosen (1979) | UI records on Georgia claimants (1974-1976) | Tobit | -- | A one-week increase in potential duration increases unemployment spells by 0.4 - 0.5 weeks |
| Moffitt and Nicholson (1982) | Survey of FSB claimants (1974-1976) | Maximum likelihood with kinked budget constraint | A 10 percentage-point increase in the replacement rate increases unemployment spells by 0.98 weeks for men and 0.84 weeks for women | A one-week increase in potential duration increases unemployment spells by 0.1 weeks for men and women |
| Moffitt (1985a) | CWBH administrative records, men only (1978-1983) | Proportional hazards model | A 10 percent increase in the benefit amount increases unemployment spells by half a week | A one-week increase in potential duration increases unemployment spells by 0 15 weeks |
| Moffitt (1985b) | CWBH (1978-1983), JSARP survey data (1979-1981), UI records on Georgia claimants (1974-1976) | Proportional hazards model | -- | A one-week increase in potential duration increases unemployment spells by 0.17 to 0.45 weeks for men, 0.10 to 0 37 weeks for women |
| Solon (1985) | CWBH-Georgia (1978-1989) | Proportional hazards model, based on taxation of benefits imposed in 1979 | A 10 percentage-point increase in the replacement rate increases unemployment spells by between half a week and a full week | A one-week increase in potential duration increases unemployment spells by 0.3 weeks |

(continued)

# Table 7.1 (continued)

| Study | Data used | Estimation methods | Impact of weekly benefit amount | Impact of potential benefit duration |
|---|---|---|---|---|
| Meyer (1989) | CWBH (1979-1984) | OLS, based on increases in state WBA minimums and maximums | A 9 percent increase in benefits increases weeks of UI benefits by one-and-a-half weeks | -- |
| Meyer (1990) | CWBH, men only (1978-1983) | Proportional hazards model | A 10 percentage-point increase in the replacement rate increases unemployment spells by one-and-a-half weeks | -- |
| Katz and Meyer (1990) | CWBH, men only (1978-1983) | Proportional hazards model | -- | A one-week increase in potential duration increases unemployment spells by between 0 16 and 0.20 weeks |
| Davidson and Woodbury (1995) | Estimates from UI bonus experiments | Simulations based on estimated impacts of bonus experiments | A 10 percentage-point increase in the replacement rate increases unemployment spells by 0.3 to 1.1 weeks | A one-week increase in potential duration increases unemployment spells by 0.05 to 0.20 weeks |

NOTE: FSB = Federal Supplemental Benefits CWBH = Continuous Wage and Benefit History These data were extracted from UI administrative records in thirteen states. JSARP = Job Search Assistance Research Project (also known as the Employment Opportunity Pilot Project). The project was conducted in twenty sites. FSC = Federal Supplemental Compensation

1980s. Therefore, the following discussion focuses primarily on estimates that have appeared in the literature over the past ten to fifteen years, as summarized in table 7.1. The estimated impacts of the two main UI parameters on unemployment spells will be considered, as well as recent findings related to the timing of reemployment as associated with the point of benefit exhaustion, and the research on the potential impact of UI on reemployment wages.

### Impact of Changes in the Benefit Amount

Studies of the effect of changes in the weekly benefit amount have consistently demonstrated that there is a disincentive to reemployment associated with UI. Almost uniformly, the research has generated estimates showing that higher weekly benefit amounts lengthen the duration of unemployment spells. The magnitude of this effect, however, is uncertain. Based on the studies completed as of 1977, Hamermesh (1977) concludes that the best estimate is that a 10 percentage-point increase in the wage replacement rate (the ratio of the weekly benefit amount to the pre-UI after-tax weekly wage) raises the average unemployment spell by half a week. However, this conclusion is founded on studies that present estimates ranging from zero to about 1.5 weeks. Danziger, Haveman, and Plotnick (1981) report a similarly wide range of estimates.

Recent research on the effect of increasing the two main parameters of the UI system has attempted to refine estimates of these effects by using new data or new methodologies. The Continuous Wage and Benefit History (CWBH), which combines administrative data from several states, has been used in many studies over the past 10 years. The CWBH includes accurate administrative data on levels of UI benefits, potential duration of benefits, and weeks of UI receipt, thereby precluding the measurement errors associated with survey data on unemployment spells.[2] Recent studies also tend to use hazard models to control for the use of incomplete, or censored, measures of unemployment spells. A measure of unemployment is said to be "censored" if the unemployment spell is not completed at the point of observation. This happens either because observed spells are measured by UI receipt, which cannot account for unemployment beyond benefit exhaustion, or because survey data measure unemployment as of the time of the survey and cannot measure spells that continue beyond the time of the sur-

vey. Since weeks of UI receipt are often used in recent studies, censoring can be a major issue because the measure itself can introduce bias into the estimates—especially since substantial rates of benefit exhaustion imply that a large proportion of observed unemployment spells are, in fact, incomplete. Hazard models allow researchers to control for the biases introduced by censored measures of unemployment by explicitly treating censored spells differently than completed spells in the estimation procedure.

The recent studies that use new data and more appropriate methods find that the estimated impact of increased benefit amounts on unemployment spells tends to be higher than the half-week response to a 10 percentage-point increase in the replacement rate cited by Hamermesh (1977). Moffitt and Nicholson (1982) estimate that a 10 percentage-point increase in the replacement rate extends unemployment spells by slightly less than one week (table 7.1). Moffitt (1985a) reports that estimates based on the CWBH data imply that a 10 percent increase in the weekly benefit amount (which represents an increase in the average replacement rate of about 6 percentage points) raises unemployment spells by half a week. In terms of replacement rate impacts, this suggests that a 10 percentage-point increase in the replacement rate would raise unemployment spells by about 0.8 weeks. Meyer (1990), using the same data as Moffitt but somewhat different estimation methods, finds an even greater impact. His findings suggest that a 10 percentage-point increase in the replacement rate lengthens unemployment spells by one-and-a-half weeks.

Because the evidence shows that the benefit amount significantly affects unemployment spells, it seems clear that disincentives to reemployment are inherent in the UI system and should not be ignored in setting the benefit amount. If benefits are increased because of concerns about adequacy, the result will be longer unemployment spells for claimants. Although the exact magnitude of the response is uncertain, the lengthening in average unemployment spells is likely to be in the range of 0.5 weeks to 1.5 weeks for every 10 percentage-point increase in replacement rates.

### Impact of Changes in the Potential Duration of Benefits

Studies have generally shown that, as predicted, increases in the potential duration of benefits lengthen unemployment spells, although

the magnitude of the impact is not clear. The recent estimates shown in table 7.1 suggest that a one-week rise in potential duration extends unemployment by between 0.1 and 0.5 weeks. This is a fairly wide range of estimates, which suggests, for example, that increasing potential duration from 26 weeks to 36 weeks would lengthen average unemployment spells by between 1 week and 5 weeks. Even estimates near the lower end of the range imply that the impact of an increase in potential duration is important. Katz and Meyer (1990) show, for example, that a given cut in UI expenditures achieved by reducing the potential duration of benefits shortens unemployment spells by twice as much as a similar cut achieved by reducing benefit levels. Regardless, policy prescriptions based on estimates of such uncertain magnitudes need to be evaluated with great care.

Research has also addressed the issue of the timing of reemployment relative to the timing of benefit exhaustion. Both the labor-supply and job-search theories imply that the probability of reemployment increases near the point of benefit exhaustion. These predictions are confirmed by empirical research (Katz and Meyer 1990), which shows that the rate at which claimants secure work increases substantially just before they exhaust their benefits. Katz and Meyer conclude from these findings that the potential duration of benefits has a strong effect on either recall policies of firms or on job-search strategies of workers.

In a different study based on a nationally representative sample of UI claimants, Corson and Dynarski (1990) also detect a jump in the probability of reemployment near the point of benefit exhaustion, but, contrary to Katz and Meyer, they argue that the magnitude of the effect is modest.[3] They emphasize that 75 percent of workers who exhausted their benefits were still unemployed more than a month after receiving their final UI payment, and that 60 percent were still unemployed 10 weeks after their final payment.

While the estimates from these studies apply to the UI claimant population as a whole, researchers have recently emphasized the importance of distinguishing between claimants who eventually return to their previous job and claimants who accept a new job. Data drawn from the Panel Study of Income Dynamics (PSID, 1980-1981) for a sample of unemployed workers (both UI claimants and nonclaimants) show that 52 percent of unemployment spells in that sample ended in a return to the previous employer (Katz and Meyer 1990). Research has

shown that at the time of their layoff, workers are generally able to accurately predict whether or not they will be recalled. Among a nationally representative sample of UI claimants from 1987 and 1988, 92 percent of those who were given definite recall dates returned to work for their pre-UI employers. About 70 percent of claimants who expected to be recalled but who were not given definite recall dates returned to work for their pre-UI employers. In contrast, only 9 percent of claimants who did not expect to be recalled returned to work for their previous employers.

One would predict that claimants who expect to be recalled are likely to differ in their job-search behavior from claimants who do not expect to be recalled. The possibility of being recalled may prompt claimants to invest less time and money in the search for a new job. Claimants who anticipate recall may also respond differently to changes in UI than do other claimants. The models presented in the preceding section on theory may not apply to claimants who expect to be recalled and who have little control over the timing of their recall. Hence, the predicted effects of UI based on these models may apply best to claimants who do not anticipate being recalled.

Recent estimates tend to support this prediction. Corson and Dynarski (1990) find that, as postulated, increases in the replacement rate and in the potential duration of benefits lead to longer unemployment spells for claimants who do not expect to be recalled. However, increases in the replacement rate are associated with significant decreases in UI receipt for claimants who expect to be recalled, and variations in potential duration of benefits have a small and insignificant impact on these claimants. Corson and Dynarski attribute the reduction in UI spells of claimants who expect to be recalled to the layoff and recall policies of firms.

### Impact of Unemployment Insurance on Reemployment Wages

The preceding empirical studies suggest that the availability of UI tends to prolong unemployment spells. Despite these findings, we cannot determine whether the additional periods of unemployment due to UI represent leisure time or extra job-search time. Presumably, if UI gives claimants extra time to search for a job, and the search is productive, then reemployment outcomes should, on average, be more favorable with UI than in the absence of UI.

One important outcome that can be used to test this hypothesis is the wage at reemployment. UI may have a positive impact on reemployment wages by inducing claimants to be more selective in their acceptance of wage offers. Several studies that have attempted to estimate the impact of UI on reemployment wages provide only mixed evidence that such an effect exists. In an early study of the relationship between UI and reemployment wages, Ehrenberg and Oaxaca (1976) estimated that a 10 percentage-point rise in the wage replacement rate increased the reemployment wage by 7.0 percent for men and 1.5 percent for women. These results suggest that the growth in unemployment associated with increases in UI represents, to some extent, productive job search. However, subsequent studies have failed to support this finding (Classen 1977, 1979; Moffitt 1985b; and Meyer 1989). Most recently, Meyer (1989) found no evidence that increases in state minimum and maximum benefit levels have caused claimants to have higher reemployment earnings. His point estimates imply a decline in wages in response to benefit increases, but the large standard errors of these estimates make it impossible to say anything conclusive about the actual sign of the effect.

Several factors may complicate the potentially positive link between UI and higher reemployment wages. First, claimants may use their UI to search longer for jobs that have better benefits or other desirable characteristics, but not necessarily higher pay. Second, claimants may use their UI to search longer for jobs with better training opportunities but with relatively low pay in the short run. Both of these factors imply that even if claimants use UI to look for a better job, the effect on reemployment wages may still be ambiguous.

*Institutional Factors Affecting the Job-Search Behavior of Claimants*

To counteract the reemployment disincentives inherent in UI, state UI systems refer claimants to the Employment Service (ES) and impose various work-search requirements on them.[4] Most states require all new claimants who are not employer-attached to register with the state ES. These claimants can use job placement assistance and other ES services, such as employment counseling. The ES may also refer claimants to particular jobs if their skills match the requirements of positions listed with the ES. In this case, state laws generally

require individuals to accept the referral to "suitable work," or they may be denied benefits. However, the ES does not have the resources or the appropriate job listings to provide job referrals to the majority of claimants.

Claimants are also expected to document their work search as part of the UI claims process. In many states, they must provide UI with a minimum number of names of potential employers contacted for each claims week. Nevertheless, state agencies usually do not aggressively validate the information provided, which leads one to question the effectiveness of the current work-search requirements in offsetting the reemployment disincentive of UI. On the other hand, evidence from a recent demonstration of alternative work-search policies shows that standard work-search requirements do reduce benefit receipt as compared with a system in which claimants do not have to document their work-search efforts (Johnson and Klepinger 1994). New legislation requires claimants identified as likely to exhaust UI benefits to participate in mandatory job-search assistance services, which have the potential to further offset the reemployment disincentive effects of UI. These requirements are discussed later in this chapter.

### Other Effects of Unemployment Insurance

Although it seems clear that UI tends to prolong the unemployment spells of claimants, its impact on the unemployment rate or on the proportion of the population that is employed is unclear. UI prolongs unemployment spells because it negatively affects the transition of UI claimants into jobs. While this particular consequence would tend to decrease employment at any given time, it could be offset by UI impacts on other labor market transitions. Furthermore, UI may have spillover effects on individuals who do not respond directly to UI but are nonetheless affected by the behavior of UI claimants.
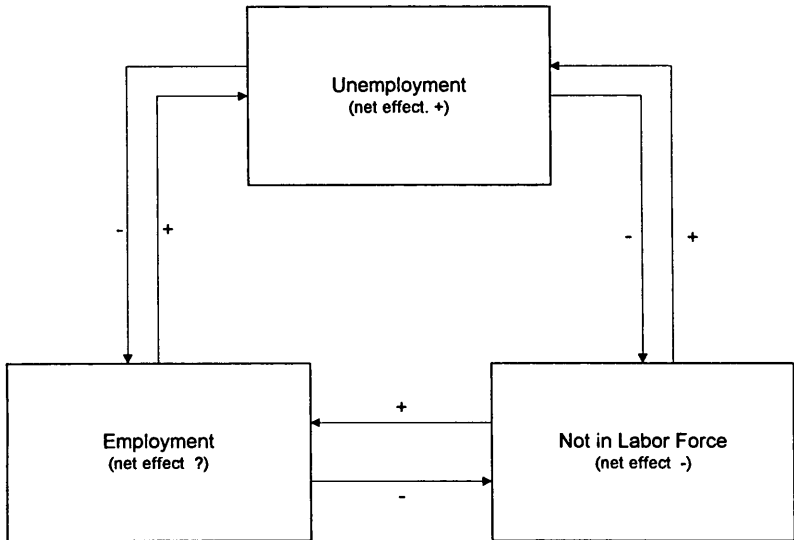
*Effects on Labor Market Transitions*

The effects of UI may extend to labor market transitions beyond that from unemployment to employment, which has been the focus of most

research on UI. Figure 7.4 shows the predicted impact of UI on transitions between three different situations: employment, unemployment, and not being in the labor force. The effect discussed so far, the reemployment disincentive faced by benefit claimants, is represented by the negative sign next to the arrow from unemployment to employment. This shows that, given the reemployment disincentive inherent in UI, one would predict that UI has a negative impact on the rate at which workers move from unemployment to employment. However, the existence of UI may also affect the flow of individuals in the opposite direction. For example, UI may increase the transitions from employment to unemployment because the protection it offers makes jobs with a high risk of layoff more attractive than they would be in the absence of UI. If workers are more likely to take high-risk jobs, the layoff rate for the labor force in general should rise, expanding the flow from employment to unemployment. Furthermore, UI may cause firms to increase the use of temporary layoffs to manage their workforce, which would also increase the rate at which individuals move from employment to unemployment.[5]

In addition to the effect on the transitions between employment and unemployment, UI may influence the transitions in and out of the labor force. First, the existence of UI should decrease the flow of people out of the labor force. Employed workers are less likely to leave the labor force directly because they can receive UI benefits by moving to unemployment instead. Similarly, unemployed workers are reluctant to leave the labor force because such a move would entail the loss of their benefits. Hence, both employed and unemployed individuals are less likely to leave the labor force than they would be in the absence of UI.

The existence of UI should increase the flow of individuals from outside the labor force into both employment and unemployment. The insurance value of UI increases the movement of individuals into the labor force because it makes work more attractive.[6] This effect tends to increase the flow into both employment and unemployment because some workers move directly into jobs while others begin searching for work and are therefore classified as unemployed. Hamermesh (1979) studied the effect of UI on flows into employment and found that, for married women, the estimated rise in employment because of UI was nearly large enough to fully compensate for the increase in unemployment due to the UI-related reemployment disincentive.

**Figure 7.4  Theoretical Effect of UI on Labor Market Transitions**



Accounting for the effects of UI on all labor market transitions gen-
erates some clear hypotheses on the net effects of UI on unemployment
and labor force participation. First, as shown in figure 7.4, UI is pre-
dicted to generate a net increase in labor force participation because it
positively influences both of the flows into the labor force and nega-
tively influences both of the flows out of the labor force. Similarly,
unemployment should rise because the existence of UI increases both
of the flows into unemployment and decreases both of the flows out of
unemployment. Only the net effect on employment is ambiguous given
the impacts shown in figure 7.4.

Clark and Summers (1982), who have conducted the only compre-
hensive empirical study of the effects of UI on labor market transitions,
present findings that are largely consistent with figure 7.4. They esti-
mate that UI has a positive and significant impact on the transition
from employment to unemployment, a strong negative effect on the
transition from employment out of the labor force, and a positive and

significant effect on the transition to unemployment from outside the labor force. However, they find that UI has a negative effect on the transition to employment from outside the labor force, contrary to what is shown in figure 7.4. In addition, the estimated effects on the transitions out of unemployment are small and insignificant.

Taken together, the estimated impacts of UI on all labor market transitions imply that UI increases unemployment, but that it also raises labor force participation and employment. Clark and Summers estimate that UI, as it existed in 1978, caused a net increase in the unemployment rate of 0.65 percentage points, a net increase in the employment ratio of 0.62 percentage points, and a net decrease in the labor force nonparticipation ratio of 1.11 percentage points.[7] These estimates are consistent with the predicted net effects shown in figure 7.4.

These findings suggest that studies that focus solely on UI claimants in evaluating the incentive effects of UI may overstate the impacts of the program on net unemployment. However, so far, the issues addressed by Clark and Summers have not been examined by other empirical studies. More evidence is needed before we can declare that UI increases employment.

*Effects of UI on Nonrecipients*

A majority of unemployed workers do not receive UI benefits either because they are not eligible or because they do not choose to receive them. In addition, the rate of benefit receipt among the unemployed has declined in recent years.[8] The ratio of claims to unemployment averaged 0.35 in the 1980s, compared with 0.41 in the 1970s (Corson and Nicholson 1988).

Recent discussions of the disincentive impacts of UI have addressed the possibility that the behavior of recipients has spillover effects on unemployed workers not receiving UI. If UI recipients and other unemployed workers are competing for a limited number of job vacancies, the ability of the other unemployed workers, or nonrecipients, to find a job may be affected by the actions of the UI recipients. If UI reduces the job-search intensity or the rate of job acceptance among recipients, it may enhance the reemployment opportunities available to nonrecipients, allowing the nonrecipients to return to work faster than they

would have in the absence of UI. This would shorten the average unemployment spells of nonrecipients. The size of this effect would depend partly on the degree to which nonrecipients are substitutable for recipients with regard to filling the existing job vacancies. Given the potential for substitutability, a full analysis of the net effect of UI on unemployment spells must address potential impacts on average spells of nonrecipients as well as of recipients.

Initial empirical evidence suggests that these spillover effects are important. Levine (1993) estimates that the effects are substantial: a 10 percentage-point increase in the replacement rate shortens unemployment spells of nonrecipients by one week or more. Since the majority of unemployed workers are nonrecipients, a spillover effect this large would completely offset the increase in unemployment caused by the rise in UI benefits, according to the estimates discussed earlier in this chapter. In fact, the magnitude of the effect suggests that an increase in UI benefits would probably generate a *decrease* in aggregate unemployment. Levine supports this conclusion by estimating that a 10 percentage-point increase in the replacement rate would lead to a 0.4 percentage-point reduction in the unemployment rate, although the estimate is not statistically significant. This finding appears to contradict Clark and Summers (1982), who showed that a rise in UI benefit amounts would increase the unemployment rate; however, they did not explicitly control for unemployed nonrecipients. Given that the Levine study represents the first direct analysis of spillover effects, further research will be required before we can draw firm conclusions on this potentially important outcome.[9]

### Potential Policy Responses to Reemployment Disincentives

The UI system has traditionally promoted rapid reemployment through work-search requirements and referrals to the ES. However, for many years, policy makers have discussed the possibility of changing the program in such a way as to create new financial incentives for reemployment or to provide additional job-search assistance or other employment services that would expedite claimants' return to work. The policy option related to financial incentives that has received the

most attention is a reemployment bonus, a lump-sum paid to those who become reemployed quickly. Several social field experiments were conducted over the past decade to rigorously test this concept in an operational UI environment.[10] Two other sets of field experiments evaluated a more service-oriented approach to encouraging reemployment. The first set tested different strategies for providing employment services, especially enhanced job-search assistance, to make claimants more employable or to make their job search more effective. The second set offered services and benefits to claimants interested in starting their own business. While these experiments focused primarily on providing claimants more services, they also affected reemployment incentives. Both the bonus experiments and the enhanced services experiments were based on a random assignment design in which claimants were part of a control group that received existing services or were part of a treatment group that received the service package or the bonus offer being tested.

This section presents a discussion of the bonus and enhanced-services experiments and of how they affect the reemployment incentives faced by claimants.[11] Also included is a description of how legislation, based on the findings from these experiments, has changed the UI system.

*The Reemployment Bonus Experiments*

Three bonus experiments were conducted between 1984 and 1989. They were designed to counteract the reemployment disincentives inherent in UI by offering a direct financial incentive for reemployment. The first experiment, the Illinois UI Claimant Bonus Experiment, was conducted in 1984 by the Illinois Department of Employment and Security. In this experiment, eligible UI claimants were assigned randomly to the treatment group, which received a bonus offer, or to the control group, which received no offer. A bonus of $500 was paid to claimants in the treatment group who started work at a full-time job within 11 weeks of filing their initial UI claim and who remained employed for at least four months. The difference in average UI receipt between the treatment and control groups implies that the bonus offer reduced the average spell of UI benefit receipt by more than one week. Furthermore, the bonus was cost effective from

the perspective of the UI system: for every dollar spent on bonuses in Illinois, UI benefit payments were reduced by more than two dollars (Spiegelman and Woodbury 1987).

The Illinois findings led the U.S. Department of Labor to sponsor additional field experiments to further test the hypothesis that a reemployment bonus offer could significantly shorten spells of insured unemployment and save the UI system money. In 1988 and 1989, two other experiments were conducted in Pennsylvania and Washington to test a variety of reemployment bonus offers. The findings from these experiments are similar.[12] Bonus offers in the two experiments tended to reduce benefit payments, but the effect was more modest than that found in Illinois.[13] Moreover, for nearly all of the bonus offers that were tested, the amount of bonus payments plus the administrative costs associated with making the offers exceeded the estimated savings in UI payments generated by the offers (Decker and O'Leary 1995). These results from Pennsylvania and Washington therefore contradict those from Illinois and suggest that reemployment bonuses are unlikely to be a cost-effective method for speeding reemployment, at least from the standpoint of the UI system.[14]

Overall, the outcomes from the bonus experiments clearly demonstrate that claimants respond to financial incentives for reemployment, and that a reemployment bonus can at least partly counteract the reemployment disincentives in the UI system. However, the findings also preclude us from being optimistic about the possibility of using reemployment bonuses to generate net savings for the UI system. The estimated impacts are generally not large enough to generate such net savings.

Two other factors not reflected in the estimates of the bonus impacts may cast further doubt on the potential for net savings from reemployment bonuses. First, the behavior of claimants who are offered a bonus may have displacement effects on other UI claimants and unemployed workers who are not offered a bonus. Second, the availability of reemployment bonuses may increase entry into UI.

If all unemployed workers generally compete for a limited number of job vacancies, claimants who find positions more quickly because they receive a bonus offer may displace other unemployed workers from these jobs. The increase in employment among the bonus claimants may therefore be partly or fully offset by decreased employment

among other unemployed individuals. Consequently, the impact estimates cannot be used to determine the full effect of a bonus on the total unemployment rate because they do not account for displacement.[15]

In terms of how the availability of reemployment bonuses affects entry into UI, unemployed workers who previously did not apply for UI might be induced to do so once they know they can receive a special payment upon reemployment. For example, individuals who expect to be unemployed for a few weeks might not apply for UI under normal circumstances. However, a reemployment bonus would make applying for UI considerably more valuable to them, since they are likely to receive that payment when they return to work. The potential for entry effects would add to the net costs of offering a permanent reemployment bonus, and entry effects are not accounted for in the estimated impacts from the bonus experiments.[16] One way to address increased entry would be to tie the bonus offer to an increase in the waiting period for filing an initial benefit claim. The longer waiting period would discourage the short-term unemployed from filing a claim that establishes potential eligibility for the reemployment bonus.

An alternative to a bonus as an incentive for reemployment would be a wage supplement for claimants who take a job. Wage supplements may encourage some claimants to accept job offers that they otherwise would not take, thus shortening average unemployment spells. The impact of such a supplement would probably vary according to its size and duration and how eligibility for it is defined. The displacement effect of changing the incentives for reemployment is an issue for a wage supplement as it is for reemployment bonuses. Claimants who take jobs more readily in response to a wage supplement may displace unemployed workers who are not offered a wage supplement. To date, there have been no experiments to test the effect of wage supplements on UI claimants,[17] but the findings from the bonus experiments suggest that the effect would probably be modest.

### Enhanced Services Experiments

Two types of services for unemployed workers, job-search assistance and self-employment assistance, have been tested in recent experiments. This section presents the results from these experiments and describes the UI legislation based on these findings. The discus-

sion focuses particularly on the relationship between the tested services and the reemployment incentives faced by UI claimants.

### The Job-Search Experiments

The UI system has traditionally encouraged reemployment of claimants through work-search requirements and referrals to the ES. Over the past 15 years, there has been a trend toward relaxing work-search requirements, and some states have eliminated them altogether. However, federal policy makers have recently moved toward requiring claimants to participate in employment services as a condition of UI receipt. In the final extension of the federal Emergency Unemployment Compensation program,[18] states are required to implement a system for evaluating claimants as they enter the UI system and to provide permanently displaced claimants with mandatory job-search assistance or other employment services. The states must use a set of characteristics to create a "profile" of each claimant and to identify claimants who are unlikely to become reemployed quickly.[19] These individuals are then provided a set of mandatory services intended to help them prepare for and find a new job. The mandatory nature of these services suggests that, in addition to preparing claimants for a new job, they may increase the perceived costs of collecting UI benefits and therefore affect the reemployment incentives faced by claimants.

The impetus for the creation of a worker profiling and reemployment services system is a set of findings from the New Jersey Unemployment Insurance Reemployment Demonstration. As with the bonus experiments, the New Jersey demonstration was based on a classical design in which claimants were assigned to the control group, which received existing services, or to a treatment group, which was required to participate in a set of job-search assistance activities.[20] The package of job-search assistance offered to treatment group members was intended to speed reemployment by encouraging claimants to search more aggressively and more effectively for a new job. The findings from this demonstration show that claimants who received mandatory job-search assistance returned to work more quickly than claimants who did not receive such help. Because claimants resumed work more quickly, they also claimed one-half of one week less of UI benefits over the year after their initial claim, and the decrease in UI payments generated by mandatory job-search assistance was large enough to pay

for the provision of the services (Corson et al. 1989). Job-search assistance therefore appears to be a cost-effective method for encouraging reemployment. Two other random-assignment studies that tested the effects of alternative job-search assistance policies, the Charleston Claimant Placement and Work Test Demonstration (Corson, Long, and Nicholson 1984) and the Washington Alternative Work Search Experiment (Johnson and Klepinger 1994), also show that mandatory job-search assistance can help expedite reemployment.

Most discussions about the impacts of mandatory job-search assistance focus on the magnitude of the impacts rather than on the process through which they occur. We can consider at least three different ways in which assistance can have an effect on reemployment. First, job-search assistance can make claimants more effective job searchers, resulting in quicker reemployment. I refer to this influence as the *skills effect* of mandatory job-search assistance because it occurs as claimants take the skills that they learn from the job-search workshop and related services and apply them in looking for a new job.

Second, job-search assistance can lead to more rapid reemployment by encouraging claimants to begin searching for work sooner than they otherwise would. The help may give claimants a psychological boost that inspires them to begin looking for work immediately. I refer to this impact as the *encouragement effect* of mandatory job-search assistance. Like the skills effect, the encouragement effect is related to the substance of services designed to help claimants cope with the psychological aspects of unemployment and to stimulate claimants to search aggressively for a new job.

Finally, mandatory job-search assistance may also affect the incentives for reemployment. As is true for the financial parameters of UI, its nonfinancial aspects, such as administrative requirements or mandatory services, have important influences on reemployment incentives. Regarding mandatory job-search assistance, claimants may return to work more quickly in order to avoid participating in job-search assistance services. Because this behavior is caused by the incentives created by the services rather than by the services themselves, I refer to this impact as the *incentive effect* of mandatory job-search assistance.

Indirect evidence of the potential importance of these different effects of mandatory job-search assistance can be obtained by examining the impact of assistance on the rates at which claimants exit the UI

system, focusing especially on the timing of these impacts. If the skills effect is dominant, and claimants exit UI because the services make their job search more effective, we would expect the impact on the exit rate to occur either after the services are received, or possibly near the end of services if claimants apply their new search skills immediately. If the encouragement effect is important, we would expect the impact on the exit rate to occur somewhat earlier than with the skills effect. This is because the encouragement effect could occur as services are beginning, such that claimants are inspired to immediately begin searching for a new job. Of course, even if claimants begin looking right away, it may take them some time to find a new job. Hence, the encouragement effect may increase the exit rate both during and after the services. The incentive effect would generate earlier impacts than would either the skills effect or the encouragement effect. Claimants who return to work and exit UI to avoid participating in services would do so after being informed of the services, possibly before such assistance even begins. The incentive effect may continue as services are being delivered if claimants want to avoid participating in additional services. Thus, it is impossible to disentangle the incentive effect from the encouragement effect because both impacts would increase the UI exit rate throughout the period of service delivery.

Evidence from the UI demonstrations on the timing of exit from UI suggests that the encouragement and incentive effects play important roles in the impact of assistance on employment and on UI receipt. Corson and Decker (1989) show that, in the New Jersey demonstration, a significant part of the impact of mandatory job-search was due to an increased UI exit rate in the first seven weeks after the initial claim. The timing of this result corresponds to the periods in which claimants were notified about services (generally in week four after the initial claim) or were required to participate in services (generally weeks five to seven after the initial claim).[21] Johnson and Klepinger (1994) detected a similar effect of mandatory services in the Washington Alternative Work Search Experiment. This early impact implies that mandatory job-search assistance encouraged some claimants to return to work quickly, before the services were completed or, in some cases, even before services began.

Although the early impacts suggest that the incentive and encouragement effects are important, we do not know whether they account

for most of the impact of job-search assistance or whether the skills effect is also key. In addition, regardless of the source of the impact of job-search assistance, the service had important long-run benefits. In an evaluation of the long-run impacts of the New Jersey demonstration, Corson and Haimson (1996) find that job-search assistance reduced UI benefit receipt not only in the initial benefit year but in subsequent years as well. They conclude that claimants who were assigned to mandatory job-search assistance found employment that was more stable than that found by control group members.

### The Self-Employment Experiments

Self-employment assistance is another policy option that expands the services available to UI claimants and expedites reemployment. Under the traditional UI system, claimants must be available for work and conduct an active job search. Therefore, an individual who "works" full-time on starting a business is generally ineligible for UI. This policy creates a disincentive to self-employment, but recent legislation gives states the option to change this policy. Title V of the North American Free Trade Agreement (NAFTA) Implementation Act (P.L. 103-182) allows states to offer self-employment assistance to help speed the transition of dislocated workers into new employment. Under this service option, eligible claimants who want to establish their own business are paid a self-employment allowance that is equivalent to their UI benefit. They are expected to work full-time on starting their business, and they are exempted from UI work-search requirements. In addition, they are allowed to retain any earnings from self-employment. In effect, the new law removes the barrier to full-time self-employment by allowing payments to self-employed claimants. States are also required to provide self-employment assistance services to claimants receiving self-employment allowances.[22] Participation in these services, which is mandatory for recipients of the allowance, is limited to no more than 5 percent of regular UI claimants. So far, four states are operating self-employment programs for their UI claimants.[23]

This legislation is a response to the relatively positive findings from random-assignment self-employment demonstrations conducted in Washington and Massachusetts. The results indicate that self-employment is a viable reemployment option for a small proportion of UI claimants. Both demonstrations provided self-employment allowances

and additional assistance to claimants who completed a set of initial intake activities. In Washington, the self-employment allowance was offered as a lump-sum payment equal to the amount of the claimant's remaining UI entitlement, while, in Massachusetts claimants were offered weekly allowances equal to their UI benefit amount. Of targeted claimants, 4 percent in Washington and 2 percent in Massachusetts completed the initial intake activities and were determined to be eligible for participation in the program (Benus, Wood, and Grover 1994). In terms of the impact on economic outcomes, the availability of self-employment assistance shortened unemployment spells among claimants in both demonstrations and increased earnings in one of the demonstrations (Washington).[24] Only in Massachusetts did the self-employment program reduce total benefits (regular UI payments plus self-employment allowances) paid during the benefit year, by about $700 per eligible claimant. The program in Washington, which paid lump-sum self-employment allowances, increased total benefits paid by about $1,100 per eligible claimant. Self-employment assistance may also decrease the probability that individuals file claims in the future, which would generate savings in UI benefits in the long run. At this time, the data to investigate this potential long-run impact on new claims are not available.

## Conclusion

Changes in the parameters of the UI system affect unemployment as predicted by theory: increases in the amount and potential duration of benefits tend to prolong unemployment spells. These effects should therefore be considered in evaluating any proposals to alter UI parameters. In fact, work disincentives were an important consideration in the move to apply the federal income tax to UI benefits beginning in 1979, which reduced the after-tax benefit paid to claimants.[25]

Despite evidence of the presence of disincentive effects, researchers disagree on the importance of these effects. This dispute arises partly because estimates of the impacts of changing UI parameters cover a wide range, and partly because researchers describes similar estimates in different ways. Where one researcher characterizes an effect as

"substantial," another views it as "modest." Regardless, work disincentives of some magnitude are implicit in UI insofar as it pays claimants for staying unemployed. The task of policy makers, therefore, is to balance the need for adequate benefits with the need to limit the disincentive to work.

Other potential effects of UI beyond work disincentives should also be considered in setting benefit parameters. Although higher benefits prolong unemployment, they may generate better reemployment outcomes if the period of additional unemployment is spent finding the best possible job. The most obvious implication of this argument is that higher UI benefits should cause higher reemployment wages, but empirical studies of this issue have thus far provided only mixed evidence that such an effect exists.

Even though UI benefits prolong unemployment spells of claimants, they may not necessarily lead to lower aggregate employment or to higher aggregate unemployment for the population. Individuals are probably more likely to enter the labor force and less likely to leave it because of the availability of UI. As the labor force expands, aggregate employment would tend to increase. UI benefits may also have an indirect effect on those unemployed workers not receiving benefits. If all unemployed individuals tend to compete for a limited number of job vacancies, greater unemployment among claimants might be matched by a drop in unemployment among other jobless persons who would otherwise be crowded out of work opportunities by claimants. To date, not enough empirical research has been conducted to fully assess the impact of UI on all possible labor market transitions.

## NOTES

I thank Ronald Oaxaca, Christopher O'Leary, Stephen Wandner, Walter Corson, Sheena McConnell, and Daryl Hall for their comments on earlier drafts of this chapter

1 Another reason for an increase in the probability of reemployment near the point at which benefits are exhausted is that firms who have temporarily laid off workers have an incentive to recall them while they are still receiving benefits Otherwise, some portion of those laid off will accept other jobs after benefits are exhausted This is expensive for the firm if the workers have skills or training that are specific to that firm. See chapter 8 for a discussion of the effect of UI on layoff and hiring incentives for firms

2. For example, Sider (1985) discusses errors in measuring unemployment spells using Current Population Survey data.

3 Corson and Dynarski also note that the precision of the estimates does not allow them to reject the hypothesis that the increase in reemployment probabilities in weeks near benefit exhaustion was due to chance.

4. Chapters 4 and 11 discuss the effect of UI work-search requirements.

5. See chapter 8 for a full discussion of employer behavior under UI.

6. The insurance value of UI that makes work more attractive may be somewhat offset by UI taxes, depending on whether the incidence, or the true burden, of the tax falls on employees or employers. If the incidence falls on employees, their net wage will be reduced, which will make work somewhat less attractive

7. The employment ratio is the proportion of total employment to the total working-age population The nonparticipation ratio is the proportion of working-age individuals who are neither employed nor unemployed to the total working-age population.

8. Corson and Nicholson (1988), Blank and Card (1991), and Vroman (1991) discuss this trend and its causes.

9. Davidson and Woodbury (1995) present preliminary findings, based on a simulation model calibrated using estimates from the UI bonus experiments (see the following section), which suggest a much smaller spillover effect than that found by Levine (1993) They estimate that a 10 percentage-point increase in the benefit amount would shorten unemployment spells of nonrecipients by one-half to one day, and that a one-week increase in the potential duration would shorten spells by one-quarter of a day.

10 Laboratory experiments can also be used to investigate the factors that affect job search in a setting with UI benefits. Cox and Oaxaca (1989) discuss how laboratory experiments can test some of the principles that underlie the existing research on UI.

11. Meyer (1995) provides a detailed summary of many of the UI experiments discussed in this chapter

12. O'Leary, Spiegelman, and Kline (1995) discuss the findings from the Washington experiment, and Corson et al (1992) discuss the findings from the Pennsylvania experiment.

13. A reemployment bonus was also tested as part of the New Jersey UI Reemployment Demonstration. Since the design of this bonus was different from that of the bonuses offered in Illinois, Washington, and Pennsylvania, I exclude it from my discussion However, as is true for the results from Pennsylvania and Washington, the findings from the New Jersey bonus experiment suggest that a bonus has a smaller impact than that found in Illinois. See Decker (1994) for a detailed comparison of the Illinois and New Jersey findings.

14. Davidson and Woodbury (1991) argue that the relatively larger impact in the Illinois experiment was due to the inclusion of a subset of claimants who were eligible for an additional 12 weeks of UI benefits through Federal Supplemental Compensation. Analysis based on claimants eligible only for regular UI benefits generates impact estimates similar to those found in Pennsylvania and Washington. These findings suggest that the potential savings from a reemployment bonus increase when potential benefit durations are longer.

15. Corson et al. (1992) make an effort to account for displacement in their estimates of the impacts of the Pennsylvania Reemployment Bonus Demonstration, but the imprecision of the estimated displacement effect renders the estimate essentially meaningless. Dynarski (1993) describes the general problem in trying to detect displacement effects in a demonstration setting Davidson and Woodbury (1993) present an alternative approach to investigating displacement effects based on a simulation model.

16 A reemployment bonus could also tend to increase entry into the labor force by making UI and therefore employment more valuable. This is in addition to the general effect of UI benefits on labor force entry discussed in the previous section of this chapter

17. Corson and Haimson (1994) review issues related to the design of a wage supplement The use of wage supplements to encourage employment among low-income individuals is currently being tested in two demonstrations: the Canada Self-Sufficiency Project (Mijanovich, Gurr, and Vernon, forthcoming) and the New Hope Project in Milwaukee (Kerksick 1993)

18. The relevant legislation is the Unemployment Compensation Amendments of 1993 (Public Law 103-152), section 4 on worker profiling. U S  Department of Labor (1994) provides a description of the system requirements.

19. Chapter 11 discusses claimant profiling

20. Mandatory activities included orientation, vocational testing, a one-week job-search workshop, an assessment interview, and follow-up contacts

21. The primary service, the job-search workshop, generally occurred in week six or seven after the initial claim, depending on the individual.

22. The self-employment activities that must be offered include entrepreneurial training, business counseling, and technical assistance.

23. The four states operating UI self-employment programs are New York, Maine, Oregon, and Delaware.

24. These measures include combined employment and earnings from either wage and salary employment or self-employment.

25. In 1979, UI benefits were made taxable for single individuals whose income exceeded $20,000 and for married taxpayers filing jointly whose incomes exceeded $25,000  Further legislation in 1982 lowered these income limits to $12,000 and $18,000, respectively. The Tax Reform Act of 1986 made all UI benefits taxable

# References

Atkinson, Anthony B., and John Micklewright. 1991. "Unemployment Compensation and Labor Market Transitions: A Critical Review," *Journal of Economic Literature* 29, 4: 1679-1727.

Benus, Jacob, Michelle L. Wood, and Neelima Grover. 1994. "Self-Employment as a Reemployment Option: Demonstration Results and National Legislation." Unemployment Insurance Occasional Paper 94-3, U.S. Department of Labor, Employment and Training Administration.

Blank, Rebecca, and David Card. 1991. "Recent Trends in Insured and Uninsured Unemployment: Is There an Explanation?" *Quarterly Journal of Economics* 106, 4: 1157-1189.

Burdett, Kenneth. 1979 "Unemployment Insurance Payments as a Search Subsidy: A Theoretical Analysis," *Economic Inquiry* 17, 3: 333-343.

Burtless, Gary. 1990 "Unemployment Insurance and Labor Supply: A Survey." In *Unemployment Insurance: The Second Half Century*, W. Lee Hansen and James F. Byers, eds. Madison: University of Wisconsin Press.

Clark, Kim B., and Lawrence H. Summers. 1982. "Unemployment Insurance and Labor Market Transitions." In *Workers, Jobs, and Inflation*, Martin Neil Baily, ed. Washington, DC: Brookings Institution.

Classen, Kathleen P. 1977. "The Effect of Unemployment Insurance on the Duration of Unemployment and Subsequent Earnings," *Industrial and Labor Relations Review* 30, 4: 438-444.

_____. 1979. "Unemployment Insurance and Job Search." In *Studies in the Economics of Search*, S. A. Lippman and John J. McCall, eds. Amsterdam: North-Holland Press.

Corson, Walter S., and Paul T. Decker. 1989. "The Impact of Reemployment Services on Unemployment Insurance Benefits: Findings from the New Jersey Unemployment Insurance Reemployment Demonstration." Unpublished manuscript, Mathematica Policy Research.

Corson, Walter, Paul Decker, Shari Dunstan, and Stuart Kerachsky. 1992. "Pennsylvania Reemployment Bonus Demonstration: Final Report." Unemployment Insurance Occasional Paper 92-1, U.S. Department of Labor, Employment and Training Administration.

Corson, Walter, and Joshua Haimson. 1996. "The New Jersey Unemployment Insurance Reemployment Demonstration Project: Six-Year Folllowup and Summary Report" (revised edition). Unemployment Insurance Occasional Paper 96-2, U.S. Department of Labor, Employment and Training Administration.

Corson, Walter, Shari Dunstan, Paul Decker, and Anne Gordon. 1989. "New Jersey Unemployment Insurance Reemployment Demonstration Project: Final Evaluation Report." Unemployment Insurance Occasional Paper 89-3, U.S. Department of Labor, Employment and Training Administration.

Corson, Walter, and Mark Dynarski. 1990. "A Study of Unemployment Insurance Recipients and Exhaustees: Findings from a National Survey." Unemployment Insurance Occasional Paper 90-3, U.S. Department of Labor, Employment and Training Administration.

Corson, Walter, and Joshua Haimson. 1994. "Wage Supplements for Dislocated Workers: The TAA Wage Supplement Demonstration." Mathematica Policy Research.

Corson, Walter, David Long, and Walter Nicholson. 1984. "Evaluation of the Charleston Claimant Placement Work Test Demonstration." Mathematica Policy Research.

Corson, Walter, and Walter Nicholson. 1988. "An Examination of Declining UI Claims During the 1980s." Unemployment Insurance Occasional Paper 88-3, U.S. Department of Labor, Employment and Training Administration.

Cox, James C., and Ronald L. Oaxaca. 1989. "Unemployment Insurance: The Worker's Perspective." In *Investing in People: A Strategy to Address America's Workforce Crisis*. Washington, DC: U.S. Department of Labor, Commission on Workforce Quality and Labor Market Efficiency.

Danziger, Sheldon, Robert H. Haveman, and Robert Plotnick. 1981. "How Income Transfer Programs Affect Work, Savings, and the Income Distribution: A Critical Review," *Journal of Economic Literature* 19, 3: 975-1028.

Davidson, Carl, and Stephen A. Woodbury. 1991. "Effects of a Reemployment Bonus under Differing Benefit Entitlements, or, Why the Illinois Experiment Worked." Unpublished manuscript, Michigan State University and W.E. Upjohn Institute.

_____. 1993. "The Displacement Effects of Reemployment Bonus Programs," *Journal of Labor Economics* 11, 4: 575-605.

_____. 1995. "Unemployment Insurance and Unemployment: Implications of the Reemployment Bonus Experiments." Draft paper prepared for the Advisory Council on Unemployment Compensation.

Decker, Paul T. 1994. "The Impact of Reemployment Bonuses on Insured Unemployment in the New Jersey and Illinois Reemployment Bonus Experiments," *Journal of Human Resources* 29, 3: 718-741.

Decker, Paul T., and Christopher J. O'Leary. 1995. "Evaluating Pooled Evidence from the Reemployment Bonus Experiments." *Journal of Human Resources* 30, 3: 534-550.

Dynarski, Mark. 1993. "The Effects of Displacement on Measures of Reemployment Bonus Impacts." *Evaluation Review* 17, 1: 47-59.

Ehrenberg, Ronald G., and Ronald Oaxaca. 1976. "Unemployment Insurance, Duration of Unemployment, and Subsequent Wage Gain," *American Economic Review* 66, 5: 754-766.

Feldstein, Martin. 1974. "Unemployment Compensation, Adverse Incentives, and Distributional Anomalies," *National Tax Journal* 37: 231-244.

Gustman, Alan. 1982. "Analyzing the Relation of Unemployment Insurance to Unemployment." In *Research in Labor Economics*, Vol. 5, Ronald G. Ehrenberg, ed. Greenwich, CT: JAI Press.

Hamermesh, Daniel. 1977. *Jobless Pay and the Economy*. Baltimore: Johns Hopkins University Press.

_____. 1979. "Entitlement Effects, Unemployment Insurance and Employment Decisions," *Economic Inquiry* 17, 3: 317-332.

Johnson, Terry R., and Daniel H. Klepinger. 1991. "Evaluation of the Impacts of the Washington Alternative Work Search Experiment." Unemployment Insurance Occasional Paper 91-4, U.S. Department of Labor, Employment and Training Administration.

_____. 1994. "Experimental Evidence on Unemployment Insurance Work-Search Policies," *Journal of Human Resources* 29, 3: 695-717.

Katz, Lawrence F., and Bruce D. Meyer. 1990. "The Impact of the Potential Duration of Unemployment Benefits on the Duration of Unemployment," *Journal of Public Economics* 41, 1: 45-72.

Kerksick, J. 1993. "Implementing the New Hope Project." Paper presented at the Association for Public Policy Analysis and Management Annual Conference.

Levine, Phillip B. 1993. "Spillover Effects between the Insured and Uninsured Unemployed," *Industrial and Labor Relations Review* 47, 1: 73-86.

Meyer, Bruce D. 1989. "An Event Study Approach to the Effects of Unemployment Insurance." Unpublished manuscript, Northwestern University.

_____. 1990. "Unemployment Insurance and Unemployment Spells," *Econometrica* 58, 4: 757-782.

_____. 1995. "Lessons from the U.S. Unemployment Insurance Experiments," *Journal of Economic Literature* 33, 1: 91-131.

Mijanovich, T., S. Gurr, and S. Vernon. Forthcoming. "The Self-Sufficiency Report: A Report on the First Year of a Program to Make Work Pay for Income Assistance Recipients." Social Policy Research Demonstration Corporation, Vancouver, Canada.

Moffitt, Robert. 1985a. "Unemployment Insurance and the Distribution of Unemployment Spells," *Journal of Econometrics* 28, 1: 85-101.

_____. 1985b. "The Effect of the Duration of Unemployment Benefits on Work Incentives: An Analysis of Four Data Sets." Unemployment Insurance Occasional Paper 85-4, U.S. Department of Labor, Employment and Training Administration.

Moffitt, Robert, and Walter Nicholson. 1982. "The Effect of Unemployment Insurance on Unemployment: The Case of Federal Supplemental Benefits," *Review of Economics and Statistics* 64, 1: 1-11.

Mortensen, Dale T. 1977. "Unemployment Insurance and Job Search Decisions," *Industrial and Labor Relations Review* 30, 4: 505-17.

Munts, Raymond. 1970. "Partial Benefits Schedules in Unemployment Insurance: Their Effect on Work Incentives," *Journal of Human Resources* 5, 2: 160-176.

Newton, Floyd C., and Harvey S. Rosen. 1979. "Unemployment Insurance Income Taxation and Duration of Unemployment: Evidence from Georgia," *Southern Economic Journal* 45, 3: 773-784.

O'Leary, Christopher J., Robert G. Spiegelman, and Kenneth Kline. 1995. "Do Bonus Offers Shorten Unemployment Insurance Spells? Results from the Washington Experiment," *Journal of Policy Analysis and Management* 14, 2: 245-269.

Sider, Hal. 1985. "Unemployment Duration and Incidence: 1968-82." *American Economic Review* 75,3: 465-472.

Solon, Gary. 1985. "Work Incentive Effects of Taxing Unemployment Benefits," *Econometrica* 53, 2: 295-306.

Spiegelman, Robert G., Christopher O'Leary, and Kenneth J. Kline. 1992. "The Washington Reemployment Bonus Experiment Final Report." Unemployment Insurance Occasional Paper 92-6, U.S. Department of Labor, Employment and Training Administration.

Spiegelman, Robert, and Stephen A. Woodbury. 1987. "Bonuses to Workers and Employers to Reduce Unemployment: Randomized Trials in Illinois," *American Economic Review* 77, 4: 513-530.

U.S. Department of Labor. 1994. "Worker Profiling and Reemployment Services System: Legislation, Implementation Process and Research Findings." Unemployment Insurance Occasional Paper 94-4, U.S. Department of Labor, Employment and Training Administration

Vroman, Wayne. 1991. "The Decline in Unemployment Insurance Claims Activity in the 1980s." Unemployment Insurance Occasional Paper 91-2, U.S. Department of Labor, Employment and Training Administration.

# UNEMPLOYMENT INSURANCE

## IN THE

# UNITED STATES

*Analysis*

*of*

*Policy Issues*

Christopher J. O'Leary

*and*

Stephen A. Wandner

Editors

1997

W.E. Upjohn Institute for Employment Research
Kalamazoo, Michigan

The facts presented in this study and the observations and viewpoints expressed are
the sole responsibility of the authors. They do not necessarily represent positions of
the W.E. Upjohn Institute for Employment Research.