

Executive Summary

This report examines the hypothesis that unemployment insurance (UI) claimants have been shifted from the UI program to federally-financed welfare programs in order to reduce the costs of state-financed UI benefits. The investigation is divided into four main sections. Section I introduces the cost shifting hypothesis. Some alternative ways that a negative association between the receipt of UI and the receipt of welfare can arise are identified and discussed. Section I also conducts a literature review, and it notes specific welfare programs where unemployed workers may seek benefits.

Section II examines national time series data on the receipt of UI benefits and the receipt of welfare benefits. A state-level analysis of UI reciprocity is undertaken in Section III. The analysis identifies states where the receipt of UI has declined the most. Section IV then examines state-level data on the receipt of welfare for three major programs: AFDC, Food Stamps and Medicaid. The objective is to determine if receipt of welfare has increased most in states where receipt of UI benefits has decreased the most. This analysis draws upon simulation results from the Urban Institute's TRIM2 model. A summary of findings is then given in Section V.

The cost shifting hypothesis that motivated this study asserts that a part of UI costs has been shifted to welfare programs through reduced availability of UI benefits. The driving force behind cost shifting could be either deliberate (or inadvertent) state actions or evolutionary economic and demographic developments affecting UI and welfare caseloads in opposite directions. This cost shifting purports to explain much of the decline in UI reciprocity observed over the past twenty-five years.

Following an analysis that covers both a literature review and new research, the principal finding can be simply stated: The cost shifting hypothesis is not supported.

The cost shifting hypothesis can be criticized from three distinct perspectives. 1) From the standpoint of state government fiscal calculus, the hypothesis is incomplete. Shifting potential UI claimants to Food Stamps would clearly save a state money since Food Stamps are fully federally financed. However, welfare recipients typically receive benefits from three programs: AFDC and Medicaid as well as Food Stamps. AFDC and Medicaid are partly state financed. The growth in state-level Medicaid costs dominates all of the others (UI and welfare) program costs under consideration in the report. Because Medicaid costs are so large and grow so rapidly, it would not reduce state-level costs to move UI claimants onto welfare.

2) The main empirical evidence supporting the cost shifting hypothesis is work by the staff of the recent Advisory Council on Unemployment Compensation. This analysis concluded that 64 percent of the decline in UI claims activity between 1971 and 1993 can be explained by growth in welfare. The principal empirical variable used

in a pooled regression analysis was annual per capita Food Stamp expenditures. Section I reviews this study and raises several criticisms regarding its logic and the specification of the analysis. At a minimum, the evidence adduced to support the cost shifting hypothesis is unpersuasive.

3) New analysis of state-level data on reductions in UI claims and increased utilization of welfare did not support the cost shifting hypothesis. The states where UI claims decreased the most did not exhibit above-average increases in utilization of welfare. This analysis was based partly on the Urban Institute's TRIM2 microsimulation model and covered the years 1979 to 1993. Welfare reciprocity and benefit payments were examined for the three programs: AFDC, Food Stamps and Medicaid. The most rapid growth in welfare caseloads was observed in states and regions where welfare participation rates had been lowest during 1979-1981 and where population growth was the most rapid. In many specific instances, rapid growth in welfare caseloads occurred in states in the South and West, states where the IUTU ratio (a principal indicator of UI claims) declined less than or about the same as the national average decline.

These three criticisms of the cost shifting hypothesis are quite persuasive. It seems more likely that the states have not attempted to shift potential UI claimants onto welfare. Other readers may draw a more agnostic conclusion. This could provide a reason for undertaking more research. The place to start any additional work, however, is with an explicit formulation of the cost shifting hypothesis that has testable implications.

The report had other findings that should be noted. 1) A recent Canadian empirical study of the unemployment-UI-welfare interrelation (summarized in Section I) tracked UI claimants longitudinally. It documented the size of the interface between UI and welfare for job leavers during a period when access to UI was restricted. After UI eligibility was restricted, the fraction of job leavers who received welfare did increase, but the increase was rather modest. While the Canadian study provides important evidence, the federal-provincial fiscal relationship and associated financial incentives differ from those in the U.S., e.g., UI is federally financed in Canada. This study's relevance lies mainly in its methodology, i.e., the longitudinal tracking of the unemployed, rather than demonstrating the effects of intergovernmental fiscal incentives.

2) Section II documented the time periods when decreases in UI claims activity and increases in welfare caseloads occurred during the past forty years. UI claims (as reflected in IUTU ratios) declined most during two periods: the decade of the 1960s and the early 1980s with larger declines taking place during the 1960s. Growth in caseloads and total benefit payments were also traced for AFDC, Food Stamps and Medicaid. Relative to the size of the poverty population, AFDC caseload growth was most rapid between the mid 1960s

and the early 1970s while Food Stamp caseload growth was most rapid between the mid 1960s and the mid 1970s. Growth in Medicaid caseloads could not be traced as far back in time as for AFDC and Food Stamps. Caseloads for all three welfare programs grew noticeably after 1989, but this was a period when UI caseloads were, if anything, higher (not lower) than anticipated based on IUTU ratios from the 1980s.

3) A regression analysis conducted in Section II examined decreases in UI claims. The estimated size of the reduction was found to be sensitive to the estimation period, inclusion of state-level weights as controls and the choice of the dependent variable. Comparing 1981-1994 with the earlier 1967-1980 period, the receipt of UI benefits was estimated to be 8.3-8.7 percent lower during 1981-1994.

4) Section III used descriptive data and regressions to characterize the size of the decrease in UI claims for each state. A wide range of state-level decreases was documented. For the fifteen states with the largest decreases, the IUTU ratio declined by an average of 0.111, i.e., by slightly more than one-tenth of average unemployment. For the fifteen with the smallest decreases, the change in IUTU averaged almost exactly zero. Section III also examined whether UI monetary eligibility requirements had increased more in states with the largest decreases in UI claims and/or in states which experienced the largest UI financing problems during the early 1980s.

5) A state-level analysis of AFDC, Food Stamps and Medicaid reciprocity was undertaken for the period 1979 to 1993. Detailed results of this analysis are presented in Section IV and in Appendix A. For all three welfare programs, similar findings were observed on the relation between changes in the receipt of UI benefits and the receipt of welfare. The group of 15 states where UI reciprocity declined the most (as reflected in IUTU ratios) had the smallest increases in welfare caseloads and associated costs. In contrast, the fifteen states where IUTU ratios decreased the least had the largest increases in welfare caseloads. Details for individual states were displayed in Tables 10, 11 and 12 with supporting detail in Tables A1-A5 of Appendix A. An unpublished version of this report also includes in Appendix A a state by state graphical display of welfare caseloads for the 1979-1993 period.