

# **Reemployment Bonuses in the Unemployment Insurance System**

## **Evidence from Three Field Experiments**

Copyright©2001 W.E. Upjohn Institute for Employment Research

### **Ch. 1 - Introduction and Background of the Reemployment Bonus Experiments**

Walter A. Corson and Robert G. Spiegelman

#### **MOTIVATION FOR A BONUS PROGRAM: WORK INCENTIVES IN THE UNEMPLOYMENT INSURANCE SYSTEM**

In the 1980s, the federal government sponsored several field experiments to evaluate alternative approaches to reducing voluntary unemployment and improving the functioning of the unemployment insurance (UI) system. Four of these experiments involved the offer of bonuses to encourage more rapid return to work by UI recipients. Other experiments to enhance work search and to encourage self-employment were also implemented. Some of these experiments emphasized the offer of "carrots" to encourage desired behavior, while other proffered "sticks." These two approaches are described more fully in later sections.

Theoretical and non-experimental empirical work had consistently found that the availability of unemployment benefits led to voluntary and unproductive reduction in work effort, thereby leading to unnecessarily high costs to the UI system. The three experiments that we describe in this study were designed to test whether offering bonuses to UI claimants would reduce voluntary unemployment. As we will show, the bonus experiments were successful in reducing the length of insured unemployment spells (see Chapter 4) and thus in reducing benefit payment costs to the UI system. They accomplished this reduction without any observed adverse effect on the quality of jobs obtained from job search (see Chapter 5), indicating that the bonus offer did not reduce effective job search activities.

The majority of the 11 alternative programs tested in the experiments, and all of the hypothetical programs using the combined data from the three experiments, generated positive net benefits to society (see Chapter 7). This result reflects the low costs of administering a bonus program, accompanied by the generally positive effects on claimants' earnings. However, only a few of the designs provided net benefits to government in general, or the UI system in particular, because the costs of paying bonuses usually exceeded the UI payment reductions. As discussed in Chapter 7, however, if one sector benefits from the program but other sectors do not, then the

program can be implemented by transferring funds from the winners to the losers. For instance, if society benefits but the UI system does not, an option is to pay the bonuses out of general revenues.

These experiments were conducted over a decade ago. Why should we still be interested in them? The policy issue raised by the experiments, though temporarily in abeyance, is not a dead issue. The possibility of using bonuses or similar mechanisms (such as wage supplements) to encourage more active job search is still one under consideration. The Reemployment Act of 1994 (submitted by President Clinton, but not enacted by Congress) emphasized "UI flexibility" as an integral part of employment and training policy. The concept was that a series of interventions would include short-term compensation, reemployment services, self-employment assistance, and reemployment bonuses. The intent of the act was to turn the UI program toward reemployment assistance. When the Workforce Investment Act was passed by Congress five years later, the emphasis on UI flexibility was gone, but when the concept is again of political interest at some future time, consideration of bonuses can be expected to return.

This book also contains several features not often found in social policy research: 1) multiple experiments with very similar designs, enabling the comparison of results of experiments conducted in different locations and different social contexts; and 2) the transference from experiment to policy by considering impacts on nonparticipants and through explicit benefit-cost analysis.

The remainder of this chapter discusses the motivation for the experiments in more detail and their theoretical and historical underpinnings. An overview of the book is presented in the final section of this chapter.

## **THE UNEMPLOYMENT INSURANCE SYSTEM**

As part of the Social Security Act of 1935, a national UI system was introduced to the country for the first time. After slowly building in the late 1930s and through the war period, the UI system reached its stride near the end of the 1940s, after the conversion from a wartime to a peacetime economy had taken place. By 1948, almost three-quarters of the unemployed were covered by UI, and total benefit outlays in that year were just under \$800 million. By 1992, although benefit outlays had grown to \$23 billion, coverage had declined to about one-third of the unemployed. In the remainder of the 1990s, outlays declined to about \$20 billion per year, or even less, and coverage remained about one-third of the unemployed.<sup>1</sup>

As in any insurance program, UI has a mechanism to fund future obligations, a mechanism to determine entitlement, and a procedure for making payments. Administrative costs are mostly covered by the federal government, while benefit payments are made out of a trust fund, which is administered by the U.S. Treasury but funded through taxes on employers. Each state has an independently administered trust fund. If payments exceed the funds available in the trust, the state must borrow from the Treasury and repay with interest. Total state reserves were a comfortable \$8 billion in 1948, representing 8 percent of total payroll. Reserves rose to \$38 billion in 1990 but represented less than 2 percent of payrolls in that relatively prosperous year. After falling to \$26 billion in 1992, reserves recovered to \$48 billion in 1998, but that represented only 1.5 percent of payroll.<sup>2</sup> In 1948, the average employer paid UI taxes amounting to 1.2 percent of taxable wages. By 1992, that percentage had increased to 2.2 percent, about where it has remained to date. Interestingly, however, because of declining coverage, benefit outlays were 0.8 percent of taxable wages in 1948 and only slightly higher in 1992. By 1998, that percent had declined to only 0.6 percent. For detailed discussions of UI financing, see Vroman (1990) and Blaustein (1993).

A worker who is in a firm covered by the UI system and becomes unemployed because of lack of work (not because of voluntarily quitting, or being fired for committing acts detrimental to the employer) is entitled to receive unemployment compensation. Entitlement to compensation, however, is conditional on the worker having sufficient earnings in the *base period*, usually the first four of the last five calendar quarters prior to filing for benefits. The dollar value of benefits payable in a week in which the UI beneficiary is fully unemployed is usually 50 percent of previous weekly wages, subject to a minimum and a maximum. Because of minimums and maximums, on the average, UI recipients receive about 40 percent of previous weekly earnings. The beneficiary is entitled to these payments for a certain number of weeks during the year after filing for benefits (called the *benefit year*). Twelve states (including Illinois) pay benefits for a fixed number of unemployed weeks, typically either 26 or 30. However, most states (including Washington and Pennsylvania) pay benefits for a variable number of weeks, depending upon the claimant's work history. A beneficiary is said to have "exhausted benefits" if the beneficiary remains unemployed after having received all the benefits to which he or she is entitled for the benefit year. In some recession years, when unemployment has remained high, the federal government has financed extended benefit programs and benefits have been provided for up to 52 weeks.

From the start, however, there has been some ambiguity as to whether the system is primarily designed to "alleviate the hardships that result from the loss of wage income during unemployment" (Blaustein 1993, p. 43) or "to insure workers against the risks of earnings loss from unemployment" (Burtless 1990, p. 75). The system today contains elements of both. For instance, the replacement rates are

higher for low-wage workers. On the other hand, the insurance concept prevails in the requirement that the claimant must be involuntarily unemployed to collect benefits. No one collects fire insurance for burning down their own house; life insurance is not usually paid in cases of known suicide. Thus, the insurance principle is violated if the insurance is paid for strictly voluntary periods of unemployment. This principle drove the requirements that unemployment beneficiaries be "able and available" for work and be actively seeking employment. Furthermore, benefits cease to be paid if the beneficiary refuses the offer of "suitable" work. That the work must be "suitable" implies that simply minimizing the period of unemployment by requiring beneficiaries to take any job is not an objective of the program. Extending the search to find suitable work is acceptable and even encouraged—through, for instance, the requirements that the Employment Service (ES) assist the beneficiary to find suitable work.

Legislation in the second half of the 1990s has dramatically changed the nature and functioning of the UI system. The emphasis overwhelmingly has become the return to work. This emphasis, however, has been coupled with a vast simplification in the handling of claims to reduce administrative costs, a process that may not be totally compatible with the back-to-work goal. Changes in the UI system are foreshadowed in the reform of the nation's welfare system. The Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) established a system of bloc grants from the federal government to the states, with the fundamental requirement that states have most recipients working within two years of first receiving assistance benefits. Today, all but four states have what is called *work-based welfare* as their *modus operandi*.

The Workforce Investment Act (WIA) signed into law in 1998 includes many of the characteristics of the PRWORA for the UI system. The emphasis is on speedy reemployment, with training provided only if necessary to obtain employment; the philosophy is that the best training is a job. The new federal system under WIA provides reemployment services under one roof—including payment of UI benefits, job placement, counseling, and job skill training—unless initial claims are taken by telephone, in which case there is no UI office as such.

### **Unemployment Insurance and the Duration of Unemployment**

Starting in the early 1970s, Martin Feldstein, and then others, argued that UI has contributed to increased unemployment by reducing the incentive to become reemployed (see especially Feldstein 1973). This problem can arise in any insurance scheme because of "moral hazard," whereby agents who are being insured against a state (e.g., unemployment) do not take all measures to avoid that state (Burtless 1990, pp. 78-79; Bailey 1977). If a job seeker extends unemployment in order to obtain a better job, society may be better off. However, if the additional unemployment is not

used for effective job search, then the additional unemployment may be considered voluntary and a net cost to the system.

It would be desirable to be able to determine the effect of UI on the amount of voluntary unemployment and clearly distinguish it from the involuntary kind. But, as Burgess and Kingston (1990, p. 138) pointed out, such a distinction is muddy. There is an involuntary element in all unemployment, in the sense that no one chooses bad luck over good; there is also a voluntary element in all unemployment, in the sense that however miserable one's current work options, one could always accept some job (p. 138). Thus, in the end, the UI question is empirical—how much does UI increase unemployment and what is the result of the increase in terms of job matches?

A large body of research has estimated the effects of UI benefits on the duration of unemployment. Decker (1997) summarized estimates of how the entitled duration of benefits and the rate of wage replacement<sup>3</sup> affect the length of joblessness. The studies showed that lengthening the entitled duration of benefits by 1 week lengthens joblessness by between 0.1 and 0.5 weeks, and a 10 percent increase in the wage replacement rate is estimated to increase joblessness by between 0.3 and 1.5 weeks.

However, these results might understate the effects on the population of particular interest for the bonus experiments (i.e., those claimants not expecting recall to their previous job). The work by Topel and Welch (1979) is informative on this issue. Separating UI claimants on temporary and permanent layoff, they found that UI effects on duration were greater for the latter group. A 10 percent rise in the benefit replacement rate extended the average unemployment spell of insured workers who change jobs by 1.2 weeks; the increase was much less for those temporarily laid off.

A third group of studies measured the effects of UI compensation on the wage rate of jobs accepted after receiving benefits. Several studies found substantive effects of changes in the UI replacement rate, especially on male wages, with smaller effects on female wages.<sup>4</sup> Other researchers, however, have failed to find any earning effects (see Classen 1979; Welch 1977). Welch doubts there is one, because if all unemployed are searching more, the wage can not be expected to rise (Burtless 1990, pp. 96-97). Overall, the evidence as to whether or not there is an effect of UI on the reemployment wage rate is weak.

As noted above, theory suggests, and the empirical work demonstrates, that UI increases the duration of unemployment. Both theory and empirical evidence, however, are imprecise in estimating the quantitative effects and are ambiguous as to the extent to which the additional unemployment leads to improved job matches.

Thus, the stage is set to design and test programs with the goal of reducing voluntary unemployment without adversely affecting the quality of job matches.

### **Why a Bonus Offer Might Reduce Unemployment**

The expectation that an offer of a bonus would lead to reduced unemployment has theoretic roots in contemporary job-search theory, which developed the concept of an optimal search strategy for unemployed workers.<sup>5</sup> McCall (1965) described an optimal search rule for job seekers as involving a sequential process in which the worker decides whether or not to continue searching after obtaining each wage offer. In this context, a bonus offer to find a job within a specified time raises the cost of rejecting a given job offer, thereby reducing the reservation wage and increasing the likelihood of accepting any particular job offer (see Davidson 1990, pp. 15-17). This theory, in conjunction with job-matching theory, would hold that reducing the reservation wage would not necessarily reduce the offered wage because the higher reservation wage was unrealistic in terms of job offers available. Thus, the critical questions to be answered for a potential bonus offer program are 1) will it reduce unemployment and 2) will the reduction affect job matches?

Before discussing the three bonus offer experiments that are the main focus of this book, it is of value to briefly describe other experimental approaches to unemployment reduction. Experimental research could take two alternative directions: 1) programs that increase the requirements for job search and job acceptance and/or impose penalties for failure to conduct active search (i.e., a "stick"), or 2) positive incentives to increase the intensity of job search or more rapid acceptance of job offers (i.e., a "carrot"). The bonus offer is obviously of the latter category.

## **THE "STICK": UI WORK TEST REQUIREMENTS**

### **Work Test Requirements and Their Implementation**

State UI programs contain various work-test requirements to ensure that UI benefits are paid only to claimants who show a continuing attachment to the labor market. In most states, the cornerstone of these requirements is a set of provisions that require claimants to search actively for work. These requirements are integrated with work-test rules pertaining to claimants' ability to work, availability for work, and refusal of suitable work. By requiring active work search, these rules are also intended to increase the level and intensity of search and hence to promote rapid reemployment.

Individual states have latitude in defining and applying work-search rules according to their specific policy concerns, political climates, and economic conditions. Consequently, work-search rules and their application vary considerably among the states (Corson, Hershey, and Kerachsky 1986). Although a few states do not impose search requirements, most do impose some work-search requirements on claimants, exempting those with definite recall dates and those who use union hiring halls to find jobs. These search requirements typically specify either the number of contacts to be made by claimants or a specific number of contacts according to the claimant's occupation and local labor-market conditions. Most states with search requirements ask claimants to list their job contacts on a biweekly claim form. These forms are usually checked to determine whether job contacts are filled in, but few states actually verify the contacts. States that perform verification tend to do so only for a sample of claimants.

All states also expose claimants to job openings by requiring that claimants register with the state Employment Service (ES). However, the degree to which states monitor compliance with ES registration varies. Some states require proof of registration before UI claims can be completed, while others do no more than schedule a time for registration. More recently, in states with initial claims processing by telephone, ES registration is completed electronically. Even when ES registration was carefully monitored, fewer than half of the claimants who registered received job referrals or reemployment services from the ES (Corson, Kerachsky, and Eliason-Kisker 1988).

Research by Burgess and Kingston (1987) indicated that many claimants did not fully comply with their state's work test rules, particularly those pertaining to active search. In a five-state study, Burgess and Kingston found that half of the dollars overpaid in each of the states were due to work-search violations. Fourteen percent of claimants required to actively search for work failed to do so, and verification procedures were unable to confirm 25 to 50 percent of the employer contacts.

Burgess and Kingston's recommendation that computerized screening profiles be used to target administrative resources on high-risk claimants has been widely implemented. Their recommendations for increased penalties for noncompliance—presently, the main, if not only, penalty is return of overpayments without added penalty—and increased noncompliance detection have received much less support.

In fact, the main result of these recommendations in the 1990s has been a reduction in work-search requirements in order to reduce error rates. One major change in processing UI claims in the 1990s, which many believe actually reduces the motivation of UI claimants to seek work, is the adoption by most states of telephone

processing of subsequent weekly claims. Only the new initial claim is filed in person. Other recent innovations center on the use of modern technology to improve job search. Automated job matching is starting up in Washington and other states. However, it is not clear whether modern technology reduces or increases work-search accountability.

### **The "Stick": Recent Experimental Evidence**

Alternative job search strategies were examined as part of experiments in South Carolina, New Jersey, and Washington.<sup>6</sup> Some of this work was instrumental in the enactment by the federal government of the Worker Profiling and Reemployment Services (WPRS) System in 1993.<sup>7</sup>

The two federally sponsored studies in Charleston, South Carolina, and Tacoma, Washington, provided particularly strong evidence that tightening work-search requirements can be effective in reducing claimants' duration on UI and promoting reemployment.<sup>8</sup> Charleston's Claimant Placement and Work Test Demonstration, conducted in 1983 (Corson, Long, and Nicholson 1985), made registration with the ES mandatory for all treatment-assigned claimants who received a first UI payment (except for those filing through mass layoff procedures). Compliance with the registration requirement was carefully monitored through a computer matching process, and claimants who failed to register could no longer receive UI benefits until they could verify that they were indeed available for work. Claimants were assigned to one of three treatment groups that represented three different levels of service: 1) a basic placement interview, 2) a more intensive placement interview with a second call-in for services, or 3) a more intensive interview with a call-in for a short job-search workshop, as well as the second placement interview. A fourth group, the control group, was not required to register with the ES.

As expected, each of the treatments increased the use of the ES among UI claimants. The experimental treatments also reduced weeks of UI benefits by 0.5 week for the group that received the basic call-in and placement interview and 0.75 week for the group that received the additional call-ins for the job-search workshop and second placement interview. Overall, the treatments were cost-effective, with net savings in UI benefit payments (after deducting added administrative costs) ranging from \$46 to \$56 per claimant. No evidence was found, however, that the treatments increased employment or earnings.

The Washington Alternative Work Search Experiment was conducted in Tacoma, Washington, in 1986 and 1987 (Johnson and Klepinger 1991). This demonstration, unlike the others, focused directly on work-search requirements (as opposed to strengthening the link between UI and the ES). A control group was

subjected to Washington's standard work-search requirement that claimants make three employer contacts per week. Control group members were also required to participate in both group and individual interviews to review work-search and UI eligibility issues. These sessions were held about 13 to 15 weeks after the claimant filed the initial claim. One treatment enhanced this approach with a customized approach to work-search requirements,<sup>9</sup> and another treatment used a more intensive approach that included a two-day job-search workshop. A final treatment—exception reporting—abandoned all work-search reporting requirements. This final treatment required only that claimants report when they became reemployed or changed their earnings; if no report was made, a benefit payment was mailed to the claimant.

The exception reporting approach was clearly a disaster; it led to an *increase* in UI benefit payments of 3.3 weeks, on average. No significant differences in UI receipt were found for the customized approach relative to the standard work-search policy of three contacts per week, but a reduction of about 0.5 week in UI benefits was found for the more intensive service approach (Johnson and Klepinger 1994). Interestingly, a hazard rate analysis indicated that the impact of this treatment appeared to occur at the point when claimants received the letter telling them to come to the workshop, not at the end of the workshop. This finding suggests that the effect was the result of the claimants perceiving the workshop as a "cost" of receiving UI payments and not as a benefit.

Not all experiments that tested increased work-search requirements provided support for this approach. In 1991, Ashenfelter, Ashmore, and Deschênes (1999) evaluated an experiment conducted in four states with two treatments. In one treatment, the subject was exposed to the so-called Benefits Rights Interview (BRI), wherein the claimant's responsibility to actively search for work is explained on the first visit to the UI office. The controls would receive the BRI on the second visit, as would normally be the case. In addition, the treatment group received an expanded initial eligibility questionnaire. For a second treatment group, an additional aspect of the treatment involved an actual verification that the claimant undertook job search. There were about 1,900 experimental subjects and the same number of controls in four states: Connecticut, Tennessee, Massachusetts, and Virginia. No results in the individual states achieved a 95 percent confidence level. In the pooled data, claimants in the overall treatment group did show a 5 percent decrease in the likelihood of qualifying for benefits in the first week; however, there were no statistically significant effects on benefit amounts or duration, once qualified. The authors concluded that the results of this experiment failed to confirm the benefits of stricter work-search enforcement. This finding may only apply to the specific treatments tested, and does not necessarily contradict other findings that stronger work-search requirements would be effective.

## **THE “CARROT”**

Self-employment experiments fall into this category. Two were conducted in the UI systems of Massachusetts and Washington. Benus, Wood, and Grover (1994) summarized findings of these experiments. The findings led to a temporary five-year authorization of self-employment assistance (SEA) being included in the North American Free Trade Agreement (NFTA) Implementation Act.<sup>10</sup> The Massachusetts design was implemented, as it promised a neutral impact on the Unemployment Trust Fund. SEA programs currently operate in 10 states, with New York having the most participants. Vroman (1999) summarized state SEA practices.

The reemployment bonus experiments have not yet been authorized by any federal legislation. However, as discussed in the first section of this chapter, the Reemployment Act proposed by President Clinton to Congress in 1994 recommended permitting states to establish reemployment bonus programs. Three of the experiments—those in Illinois, Pennsylvania, and Washington—are described in detail in this book. A fourth experiment conducted in New Jersey had a bonus component, but it had design characteristics that made it unfeasible to compare its results with those of the other three experiments. We provide a summary description of the New Jersey experiment in the following section.

### **The New Jersey Unemployment Insurance Reemployment Demonstration Project<sup>11</sup>**

In 1986 and 1987, an experiment was conducted in New Jersey in which almost 9,000 claimants were assigned to one of three treatment groups, defined as follows:

- Treatment 1 (referred to as Job Search Assistance [JSA]): a set of requirements and services that began with a notification letter sent to each enrolled claimant after they received their first UI payment, which occurred in about the third week after filing. The letter required the claimant to come to the ES office for services. The services included orientation and testing in the fifth week, followed a week later by a job-search workshop consisting of five half-day sessions, and then a one-on-one counseling/assessment session, which usually occurred in the seventh week. Of course, employment or termination of benefit receipt could terminate the sequence at any time. There were periodic follow-up contacts 2, 4, 8, 12, and 16 weeks following assessment.
- Treatment 2: JSA plus training or relocation available after assessment. Those assigned to treatment 2 were told about the availability of classroom and on-the-job training and encouraged to pursue training.

- Treatment 3: JSA plus a reemployment bonus, which was offered to claimants who were still unemployed after assessment. The bonus offer provided for one-half of the claimant's remaining UI entitlement at the time of assessment, declining after two weeks at a rate of 10 percent of the original amount per week unit it was no longer available. To qualify, the claimant had to obtain a permanent, full-time job, not with a relative or the immediately preceding employer. Sixty percent of the bonus was paid after 4 weeks of employment and the remainder if they remained employed for 12 weeks. The full bonus offer averaged \$1,644, and the overall average of the two bonus payments was close to \$1,300 for those who received payment.

The eligible claimant population was restricted to workers who were over 25 years of age and identified as being dislocated, which was defined as having been employed by the same employer for three years prior to filing and not being on standby or a member of a union that places its workers through a hiring hall. The demonstration sample of 11,060 UI beneficiaries was randomly selected from the population of eligible UI beneficiaries filing in 10 of New Jersey's 38 local UI offices.

All 8,675 participants assigned to one of the three treatments were offered job-search assistance. Of these, 77 percent attended the initial orientation, 50 percent completed a job-search workshop, and 56 percent attended an assessment/counseling interview. About 15 percent of the claimants who were offered training participated in training, most of which was classroom training. Nineteen percent of those offered the bonus received at least the first payment, and 84 percent of this group also received the second installment.

The JSA and training provided by the experimental treatments were not unique in that these services were also available to nonparticipants in various forms, such as through the Job Training Partnership Act (JTPA). There were, however, significant differences in the amount of such services received by participants and nonparticipants. The most easily identifiable part of JSA is the job-search workshop. Whereas almost half of claimants assigned treatment received the workshop, only 7 percent of controls did (see U.S. Department of Labor 1989, Table IV.II, p. 248). The authors estimate that the 15 percent attendance rate of training classes for participants in treatment 2 was about three to four times that of similar nonparticipants.

There were strong effects of the treatments on UI outcomes, namely benefits paid and weeks paid in the benefit year.<sup>12</sup> Job-search assistance was associated with an average decline in UI payments in the benefit year of \$87 and a decline in number of weeks of benefit payments of almost 0.5 week. The bonus offer was associated with an additional decline of \$83 in benefit payments in the benefit year and an additional reduction of 0.5 week of benefit payments. The training offer had no effect

on benefit payments in the benefit year, which may not be surprising, since the initial impact must be to increase UI payments during the training period. Any positive effects of training may show up in the second year.

Although the bonus offer treatment in the New Jersey experiment had strong results, we do not believe that this experiment provided much guidance for policy, because the particular bonus-offer treatment was not replicable. In the New Jersey experiment, bonus offers were made only after seven weeks of insured unemployment, and the pending offer was unknown to the selected participants prior to that time. Such a situation could not be replicated in a real program, as knowledge of the pending offer would be available to all claimants from the start of their benefit year (and probably prior to that, an issue that will be explored further in Chapter 6). This knowledge can be expected to critically affect job-search behavior during the first seven weeks of the benefit year, as well as during the period in which the bonus was available.

A more replicable bonus offer experiment, in which the experimental subjects are informed of the bonus offer at the time they file for UI benefits, thereby not contaminating the search process, was needed to provide guidance to policy in this area. In fact, a bonus offer experiment with this characteristic was undertaken by the Department of Employment Security in Illinois. The experiment in Illinois was to be followed by similar experiments in Pennsylvania and Washington. In this book, we report on the Illinois, Pennsylvania, and Washington experiments, because the designs of the three experiments were sufficiently similar to make comparison of results among them, and combining of data for simulations, feasible. The New Jersey experiment could not be used in this manner.

## **BONUS OFFER EXPERIMENTS IN ILLINOIS PENNSYLVANIA, AND WASHINGTON**

Three bonus offer experiments conducted in Illinois in 1984-1985, in Pennsylvania in 1988-1990, and in Washington in 1988-1989 provide evidence of the efficacy of a bonus offer program in UI. These three experiments are the subject of the remainder of this book.

In May 1984, the Illinois Department of Employment Security contracted with the W.E. Upjohn Institute to conduct an experiment with bonus offers in Illinois. This experiment was funded by use of the governor's discretionary money under Title 7(b) of the Wagner-Peyser Act, which allows states to use funds "for exemplary models for the delivery of services." The initial interest of the state was in an experiment involving an offer of a bonus to employers for hiring UI claimants within a specified period of time. A second experimental treatment, called the Claimant Experiment, in

which bonuses were offered directly to unemployed claimants with the same proviso, was added in order to compare the effects on unemployment of a labor "supply" and a labor "demand" incentive. Because of very low participation, the Employer Experiment had little effect on behavior, but the Claimant Experiment was very successful in reducing UI benefit payments (see Chapter 4). Its success, plus the encouraging results of the New Jersey experiment, led the U. S. Department of Labor (more specifically, the Employment and Training Administration, Unemployment Insurance Service) to undertake two more bonus experiments, with offers made to claimants.

In 1987, the Department of Labor selected Washington and later that year selected Pennsylvania to be experimental states. The Department of Labor asked the W.E. Upjohn Institute to undertake the design and evaluation of the Washington experiment, which became known as the Washington Reemployment Bonus Demonstration<sup>13</sup> (henceforth referred to simply as the "Washington experiment"). The Upjohn Institute obtained a matching grant from the Alfred P. Sloan Foundation to fund the design and evaluation of the experiment. Institute staff worked with the Washington State Employment Security Department to design the Washington experiment.

In 1988, the Department of Labor selected Mathematica Policy Research, Inc., to design and evaluate the Pennsylvania Reemployment Bonus Demonstration (referred to in this volume as the "Pennsylvania experiment"). Washington was to be a pure test of the bonus offer, with several treatments providing a sufficient range of alternative bonus offers to permit mapping of the feasible alternative policy options. Pennsylvania was similarly to provide a range of bonus offers, some of which would also provide enhanced job-search assistance.

As this book unfolds, it will become clear that the bonus offer clearly reduced the weeks of benefit receipt and generally sped reemployment of UI recipients into fully satisfactory jobs. However, the net benefit analysis is not as strong. In general, the bonus offer appears to be of positive net benefit to society as a whole, but the benefits are usually not positive for the UI system, meaning that only if money is transferred into the system to pay the bonuses is it a benefit to the UI system. Such transfer, however, is well within a feasible policy set and may be undertaken for programs that are overall beneficial, even if not to the implementing agency. We believe, in addition, the results do provide important information as to the existence of voluntary unemployment by those receiving UI benefits. Secondly, we believe that this book provides important guidance to researchers and policymakers alike who want to understand how to use field experiments to design or improve social policy.

## OVERVIEW OF THE BOOK

Chapter 2 starts by formally presenting the four elements that comprise an experimental design: 1) who will participate, 2) what are the experimental treatments, 3) how many subjects will be in the experiment and how will they be allocated, and 4) where will the experiment take place and under what conditions. The chapter next grapples with the essential feature of any experiment, i.e., random assignment, discussing the process and its success in this case and looking at the characteristics of the control populations across experiments. The chapter concludes with the description of experimental operations. The bonus experiments were unusually "clean" experiments in that they did not suffer from selection bias, contamination of treatments, difficult operational environments, or inconsistent treatments.<sup>14</sup>

Chapter 3 describes the participants and rules of participation, and it presents results on the rate of participation and the characteristics of participants and nonparticipants. In this chapter, the authors provide an estimate of the extent to which UI claimants assigned to the experiment failed to collect bonuses for which they appeared to be eligible. A large proportion of bonus money was "left on the table" so to speak, and this has important implications for estimates of the cost and benefits of a program that would be modeled after the experiments (discussed more fully in Chapters 6 and 7).

Chapter 4 presents the most critical results of the experiments, namely, the effects directly on the UI system. The impact of the experiment on two variables—namely, the dollar value of UI benefits paid out to claimants and the number of weeks (duration) of insured unemployment—are estimated. The chapter concentrates on the difference between experimental and control parameters over the benefit year. The results are presented utilizing different statistical methods, starting with a simple comparison of means that, because of random assignment, can provide unbiased estimates of the treatment impacts. The chapter then presents results that have been adjusted to account for accidental differences in the characteristics of treatment and control groups. Results are also presented to show how the bonus offers affect the timing of leaving unemployment and to show how the outcomes respond to sequential increases in the amount of the bonus offer and the length of the qualification period. Overall, the bonus offer tended to reduce the length of insured unemployment, and there were differences in impacts by size of the bonus offer and length of the qualification period.

Chapter 5 proceeds to discuss some other important results, primarily the impact of the treatments on the earnings of claimants, the nature and quality of jobs, and employer attachment (i.e., did it affect the tendency for UI claimants to return to their previous employer?). Earning impacts are investigated by comparing the earnings in the year starting with the quarter in which benefits are filed—thereby

combining the direct impact of the offer on the timing of reemployment and any differences in wage rates in the post-filing job that might be due to the experimental treatment. The latter is directly addressed by comparing experimental and control differences in earnings after termination of UI benefits. The impact on the degree to which UI claimants returned to the pre-filing employer was deemed important because of employer concern that the bonus offer—not payable if the claimant is recalled to the previous job—might loosen employer attachment. No support for this concern was found.

Chapter 6 provides the bridge from experiment to program by discussing the various issues needed to translate experimental results into programs. It is both the most unique and in many ways most important chapter in the book; it reflects the need to consider how a policymaker is to make use of experimental results. Experimental results are confined to a subset of the total population who are exposed to the experimental treatment, but they provide no estimate of the experimental impact on subsets of persons in the total population who are not exposed to the treatment. In the case of the bonus experiment, all UI claimants are in the exposed group, leaving all unemployed workers who are not UI claimants outside of the experimental realm. In a full program, UI-eligible nonclaimants can enter the program realm by claiming benefits, while those ineligible for benefits might be affected by the program even if they do not participate in it. Chapter 6 attempts to measure these effects. This chapter discusses, and attempts to quantify, the effects of a bonus offer in a full program on the "entry effect" (i.e., the tendency to increase filing for UI benefits) and on "displacement" or crowding out (i.e., the tendency for participants to increase job acquisition at the expense of nonparticipants). The format and approach of Chapter 6, by necessity, differs from that of the preceding three chapters. To measure entry and displacement effects in the economy at large, it is necessary to reach out to models of employment equilibrium. Thus, these results must be considered more speculative than those that are derived directly from experimental results.

Chapter 7 presents the results of a benefit-cost analysis that shows the net benefits that can be potentially derived from a bonus offer program from the perspective of society, government, the UI system, and claimants. Although recognizing that many benefits and costs cannot be captured in this analysis, it is suggestive of the net benefits to be derived from such a program from the perspective of different constituents. In the last section of this chapter, we attempt to show the impact on net benefits from the programmatic effects discussed in Chapter 6. Basically, the low administrative costs make a bonus offer an appealing program from society's perspective. Although only the high bonus program generated net benefits from the government's perspective, the treatment simulations, using combined data from the three experiments, demonstrated positive benefits from all three perspectives—society, government, and the UI system—from a relatively small (\$500) bonus.

Chapter 8 presents an overview of what we have learned and the policy implications. The expected effects of a bonus offer program on work effort and the UI system are described, as is why an experimental approach to answering the questions seems warranted. The features of the experiments and the essential findings are reviewed. The average effects of the treatments in each of the three experiments are summarized in Table 8.1. The summary demonstrates that the treatments significantly reduced the number of claimants receiving benefits but that the bonus offer program appears to have been cost-effective only in Illinois. In assessing the experiments, Professor Robins, the author of this chapter, concludes that, from the standpoint of standards for social policy research, the experiments were quite successful. However, the experiments were not successful in pinpointing statistically significant differences across treatments, and Robins attempts to answer why this is the case. Most of the remainder of the chapter discusses alternative policies that could be employed to accomplish the goals of a bonus offer program to cost-effectively reduce insured unemployment. Four alternatives are discussed: earnings supplement, stricter sanctioning of work-search requirements, worker profiling, and Unemployment Insurance Savings Accounts.

### Notes

1. U.S. Department of Labor, *Unemployment Insurance Financial Data*, ET Handbook 394, 1948-1998, and U.S. Department of Labor, Bureau of Labor Statistics, Labor Force Statistics from the Current Population Survey, 1948-1998.
2. U.S. Department of Labor, ET Handbook 394.
3. The replacement rate is the proportion of previous weekly earnings that is replaced by UI benefits; specifically, it is the ratio of the weekly benefit amount to the net pre-UI weekly wage.
4. Ehrenberg and Oaxaca (1976) estimated that a 10 percentage point rise in the UI replacement rate (40 percent to 50 percent) would increase a male's reemployment wage by 7.0 percent and a female's wage by 1.5 percent. Burgess and Kingston (1976) and Holen (1977) found similar results.
5. The origins of job-search theory are found in the work of George Stigler (1961, 1962).
6. For evaluations of South Carolina, see Corson, Long, and Nicholson (1985); for New Jersey, see Corson et al. (1989) and further discussion in the section below; for Washington, see Johnson and Klepinger (1991, 1994).
7. The unemployment compensation amendments of 1993 (Public Law 103-153) revised extended benefit rules and also required states to implement a system to identify UI claimants most likely to need job-search assistance to avoid long-term unemployment. The system for identification became known as the Worker Profiling and Reemployment Services system.
8. Later work-search demonstrations in Nevada and Minnesota (see Meyer [1995]) confirmed the positive effects of work-search requirements on duration of UI benefits.
9. Different work-search requirements were developed for different groups of workers, depending on their job prospects. In addition, search requirements were strengthened as the unemployment spell increased.
10. The NAFTA Implementation Act (Public Law 103-182) gave states the option of continuing UI benefits for claimants who elect to start their own business. Permanent authorization was granted by federal legislation in 1998 for states to provide self-employment assistance

- with UI trust fund money.
11. The design, operation, and evaluation of this experiment is described in detail by Corson et al. (1989).
  12. A goal of the experiment and its most likely outcome is a reduction in UI utilization. These also happen to be outcomes that are readily measured, since receipt of unemployment benefits and weeks of benefits paid are data available directly from the UI record system. Thus, for the New Jersey experiment, as well as for the three experiments that occupy most of this book, a principal measure of experimental impact is the average difference in the dollars of benefits received and in the number of weeks benefits were paid between those assigned to bonus offer treatments and those in the control group.
  13. While Department of Labor refers to the Washington and Pennsylvania experiments as "demonstrations," we use the term "experiment" to make it clear that random assignment to treatment and control groups was used to permit unbiased estimates of program effects. Demonstrations do not involve random assignment and are most useful in testing workability of alternative administrative procedures.
  14. See Nathan (1988) for discussion of what makes good demonstration research.

### References

- Ashenfelter, Orley, David Ashmore, and Olivier Deschenes. 1999. "Do Unemployment Insurance Recipients Actively Seek Work? Randomized Trials in Four U.S. States." Working paper no. 6982, National Bureau of Economic Research, Cambridge, Massachusetts, February.
- Bailey, Martin N. 1977. "Unemployment Insurance as Insurance for Workers." *Industrial and Labor Relations Review* 30(July): 495-504.
- Benus, Jacob, Michelle 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, Washington, D.C.
- Blaustein, Saul. 1993. *Unemployment Insurance in the United States: The First Half-Century*. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research.
- 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, pp. 69-107.
- Burgess, Paul L., and Jerry L. Kingston. 1976. "The Impact of Unemployment Insurance Benefits on Reemployment Success." *Industrial and Labor Relations Review* 30(October): 25-31.
- \_\_\_\_\_. 1987. *An Incentives Approach to Improving the Unemployment Compensation System*. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research.
- \_\_\_\_\_. 1990. "Monitoring Claimant Compliance with Unemployment Compensation Eligibility Criteria." In *Unemployment Insurance: The Second Half-Century*, W. Lee Hansen and James F. Byers, eds. Madison: University of Wisconsin Press, p. 138.
- Classen, Kathleen P. 1979. "Unemployment Insurance and Job Search." In *Studies*

- in the Economics of Search*, S.A. Lippman and John J. McCall, eds. Amsterdam: North Holland.
- Corson, Walter, David Long, and Walter Nicholson. 1985. *Evaluation of the Charleston Claimant Placement and Work Test Demonstration*. Unemployment Insurance Occasional Paper 85-2, U.S. Department of Labor, Employment and Training Administration, Washington, D.C.
- Corson, Walter, Alan Hershey, and Stuart Kerachsky. 1986. *Nonmonetary Eligibility in State Unemployment Insurance Programs: Law and Practice*. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research.
- Corson, Walter, Stuart Kerachsky, and Ellen Eliason-Kisker. 1988. *Work Search among Unemployment Insurance Claimants: An Investigation of Some Effects of State Rules and Enforcement*. Unemployment Insurance Occasional Paper 88-1, U.S. Department of Labor, Employment and Training Administration, Washington, D.C.
- Corson, Walter, Paul T. Decker, Shari Miller Dunstan, and Anne R. Gordon, with Patricia Anderson and John Homrighausen. 1989. *The 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, Washington, D.C.
- Decker, Paul T. 1997. "Work Incentives and Disincentives." In *Unemployment Insurance in the United States: Analysis of Policy Issues*, Christopher J. O'Leary and Stephen A. Wandner, eds. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research, pp. 285-320.
- Davidson, Carl. 1990. *Recent Development in the Theory of Involuntary Unemployment*. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research.
- Ehrenberg, Ronald G., and Ronald L. Oaxaca. 1976. "Unemployment Insurance, Duration of Unemployment, and Subsequent Wage Gain." *American Economic Review* 66(December): 754-766.
- Feldstein, Martin. 1973. "Unemployment Insurance: Adverse Incentives and Distributional Anomalies." *National Tax Journal* 27(June): 231-244.
- Holen, Arlene. 1977. "Effects of Unemployment Insurance Entitlement on Duration and Job Search Outcome." *Industrial and Labor Relations Review* 30(July): 445-450.
- Johnson, Terry R., and Daniel H. Klepinger. 1991. *Evaluation of the Impacts of the Washington Alternative Work Experiment*. Unemployment Insurance Occasional Paper 91-4, U.S. Department of Labor, Employment and Training Administration, Washington, D.C.
- \_\_\_\_\_. 1994. "Experimental Evidence on Unemployment Insurance Work-Search Policies." *Journal of Human Resources* 29(3): 695.
- McCall, J.J. 1965. "The Economics of Information and Optimal Stopping Rules." *Journal of Business* 38: 300-317.

- Meyer, Bruce D. 1995. "Lessons from the U.S. Unemployment Insurance Experiments." *Journal of Economic Literature* 33(1): 91-131.
- Nathan, Richard. 1988. *Social Science in Government: Uses and Misuses*. New York: Basic Books, Inc.
- Stigler, George. 1961. "The Economics of Information." *Journal of Political Economy* 69: 213-225.
- \_\_\_\_\_. 1962. "Information in the Labor Market." *Journal of Political Economy* 70: 94-104.
- Topel, Robert, and Finis Welch. 1979. "Unemployment Insurance: What the Theory Predicts and What the Numbers (May) Show, Survey and Extensions." Photocopy, University of California at Los Angeles.
- U.S. Department of Labor, Employment and Training Administration. 1989. *New Jersey Unemployment Insurance Reemployment Demonstration Project*. Unemployment Insurance Occasional Paper 89-3, U.S. Department of Labor, Employment and Training Administration, Washington, D.C.
- Vroman, Wayne. 1990. *Unemployment Insurance Trust Fund Adequacy*. Kalamazoo, Michigan: W.E. Upjohn Institute for Employment Research.
- Vroman, Wayne. 1999. *Self-Employment Assistance (SEA) Program: Report to Congress*. Unemployment Insurance Occasional Paper 99-5, U.S. Department of Labor, Unemployment Insurance Service, Employment and Training Administration, Washington, D.C.
- Welch, Finis. 1977. "What Have We Learned from Empirical Studies of Unemployment Insurance?" *Industrial and Labor Relations Review* 30(July): 451-461.