PAID NOT TO WORK

HOW SUPPLEMENTAL UNEMPLOYMENT INSURANCE BENEFITS DECREASED EMPLOYMENT FROM 2020 TO 2021

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Paid Not to Work:

How Supplemental Unemployment Insurance Benefits Decreased Employment From 2020 to 2021

E. J. Antoni, Ph.D.

Executive Summary

This paper provides an overview of the basic workings of the unemployment insurance program and focuses on supplemental unemployment benefits employed during the COVID-19 pandemic, the latest iteration of which ended nationwide in September 2021. These supplemental benefits were paid in addition to normal benefits to those receiving unemployment assistance. The effect was to incentivize people not to work, resulting in increased unemployment, greatly hampering the labor market by contributing to an artificial shortage of labor.

The consequences were observed in two ways. First, when the program was implemented and ended nationwide, there were nationwide effects, showing that people sought jobs substantially faster when not receiving the supplemental benefits. Second, when individual states ended the latest iteration of the program before it expired nationwide, it provided a contrast with those states that continued the program until its termination in federal law on September 6, 2021. Those states that ended the program early experienced substantially faster job growth in terms of how quickly they approached pre-pandemic employment levels.

Regardless of the positive effects the supplemental unemployment benefits may or may not have provided, the program had a detrimental effect on the labor market. Those states that concluded their participation in the program early experienced less of this effect. Given these results, supplemental unemployment insurance benefits should likely never be implemented again, and states should reject such assistance if offered.

Key Points

- The supplemental unemployment insurance benefits disincentivized working and exacerbated unemployment.
- Many people received more on unemployment than they did while working.
- The supplemental benefits' effects were seen at both the national and state levels. Those states that terminated the program early converged to pre-pandemic employment levels substantially faster.

Introduction

The initial response to the COVID-19 pandemic included a series of government-imposed lockdowns that forced many businesses to close, resulting in many people losing their jobs. A variety of government measures were employed to counteract those impacts. This paper focuses specifically on the labor market effects of supplemental unemployment insurance benefits. The overall efficacy of the lockdowns in response to COVID-19 is beyond the scope of this paper. Likewise, the numerous other measures used to combat the harmful economic effects of those lockdowns are left to future research.

Traditional unemployment insurance is a dual federal-state program that typically provides benefits equal to approximately half of what an individual made while

working. Every state has a minimum and maximum weekly benefit and various qualification standards. Most people would be eligible to receive a benefit in the event of a faultless job separation, meaning that the employee was not fired for cause nor quit.[1]

Traditional unemployment insurance benefits receive preferential tax treatment in two ways. First, although subject to federal income tax, benefits are not subject to federal payroll taxes. Second, six states with income taxes do not levy that tax on unemployment benefits. The equivalent earned income of these benefits is, therefore, higher than the amount of the benefits themselves.[2]

Like any program that provides income only when someone is unemployed, unemployment insurance diminishes the financial pain of being out of work. Both theoretical and practical observed studies have demonstrated this effect.[3] The effect is related positively to the amount of unemployment benefits. As benefits become larger, all else being equal, individuals receiving unemployment benefits will take longer to find a new job. Conversely, those receiving less in unemployment benefits will find a new job faster, all else being equal.

During the 18-month period beginning in March 2020, the U.S. Congress issued a series of supplemental unemployment insurance benefits. These increased benefits exacerbated the negative effects of unemployment insurance on the labor market and contributed to fewer people being employed in the American economy.

Coronavirus Aid, Relief, and Economic Security Act

The Coronavirus Aid, Relief, and Economic Security (CARES) Act, passed in March 2020, was the first in a series of efforts to provide additional weekly unemployment benefits. The law both gave an additional $600 per week in federal supplemental benefits and expanded eligibility for unemployment insurance for about four months.[4] Not only did the act greatly increase the maximum weekly benefit for many of those who were unemployed, but it also further divorced the relationship between what a person earned in wages while employed and what that individual received in benefits while unemployed. Many of those who were unemployed received more in unemployment benefits for not working than they did in wages while working. In fact, those earning near the median household income (approximately $30 per hour for a 40-hour workweek) received roughly the same amount in unemployment benefits while not working. Roughly 5 out of 6 people who received unemployment benefits during this time effectively had a higher take-home pay than they did while working (Congressional Budget Office, 2020). **Figure 1** shows unemployment benefits relative to the income a person received while working. The incentive not to work was most pronounced at lower income levels where total unemployment benefits were a multiple of an unemployed person's previous income.

Because the supplemental benefits were a flat amount irrespective of previous income while working, their effect was most pronounced at lower incomes where they were a larger percentage of that previous income from working. Coupled with the preferential tax treatment and expanded eligibility, the $600 weekly supplemental benefit created a considerable disincentive for many people to return to work or even to continue working an existing job. In some cases, total unemployment insurance benefits were a multiple of previous take-home pay. Even at higher incomes, the supplemental benefits, in conjunction with other government programs and payments, provided the equivalent of a $100,000 annual income for a family of four in 19 states and the District of Columbia.[5]

Unfilled job openings climbed considerably beginning in May 2020 until August of that year, as seen in **Figure 2**. August was the first full month without the $600 weekly supplemental benefits, and the results were borne out in the macro-level data as benefit-induced separations decreased substantially. Employers did not have to compete with the higher unemployment benefits and were able to fill significantly more jobs.[6]

1 See Mulligan et al. (2021a) for a more comprehensive overview of the Unemployment Insurance program.

2 In California, for example, $100 of unemployment benefits is approximately equal to the after-tax take-home pay of $118 in income from working.

3 This paper does not perform an analysis of the total costs and benefits of the unemployment insurance program. As such, that critique is left to other research. Instead, this paper builds upon the well-established principle that one effect of unemployment insurance on the unemployed is a disincentive, at least temporarily, to return to work.

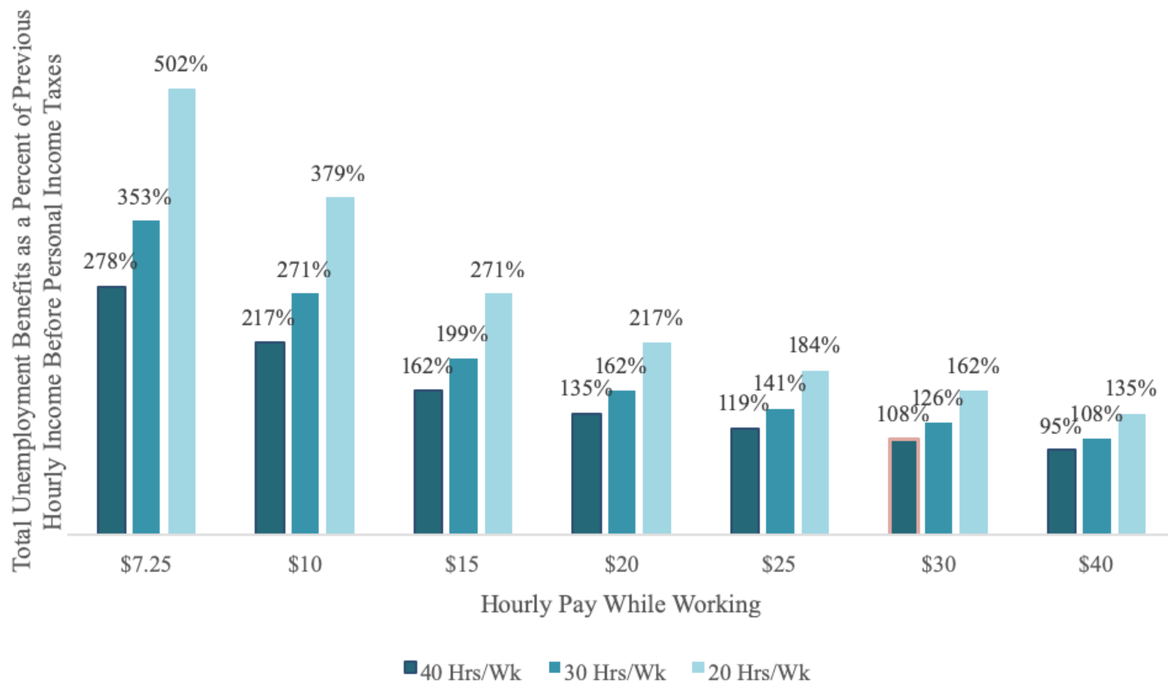
4 The reasoning for the supplemental benefits was never promulgated before passing the bill. People have conjectured after the fact that the motivation regarded aggregate consumer spending levels.

5 In Massachusetts, the amount was nearly $150,000 in equivalent annual income (Mulligan et al., 2021b).

6 Mulligan (2020) tested an alternative hypothesis that the stark decline in job openings was due to the economic recovery faltering. He concludes this is incorrect given the data on employment, consumer spending, and gross domestic product.

Figure 1

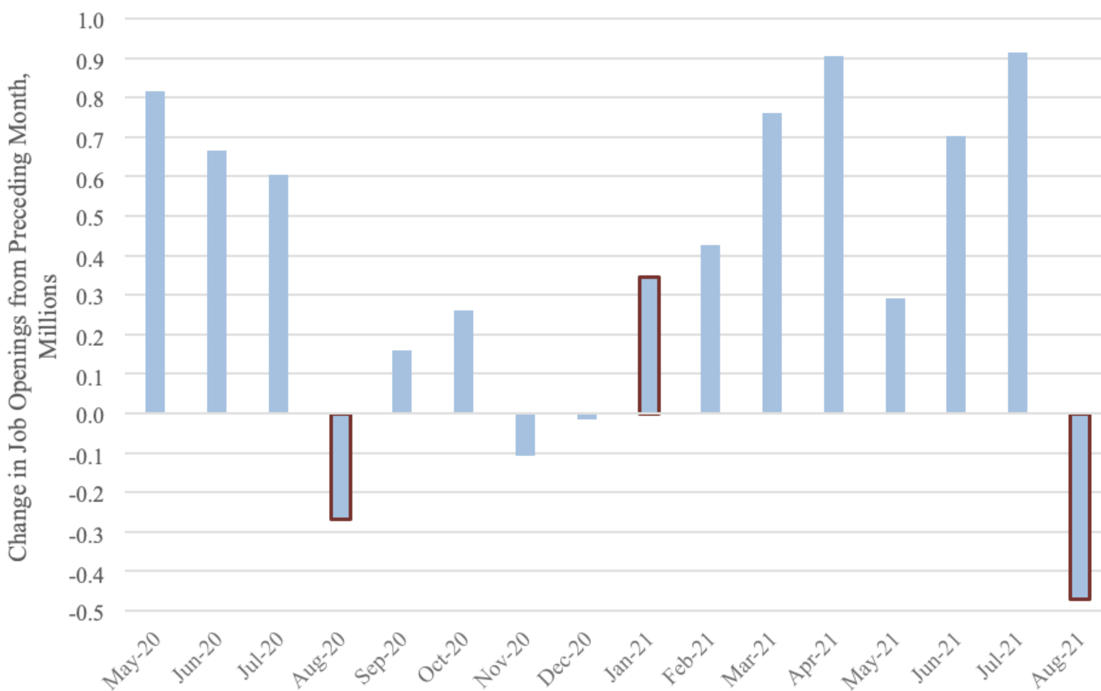
Unemployment Insurance Benefits Frequently Exceeded Previous Income in the U.S.



Note. Data from *Biden's Stimulus Plan Will Reduce Employment by Six Million Workers*, by C. Mulligan, S. Moore, and E. Antoni, Committee to Unleash Prosperity, 2021 (https://committeetounleashprosperity.com/wp-content/uploads/2021/05/CTUP_BidensStimulusPlan-1.pdf) and author's calculations.

Figure 2

Monthly Job Openings in the U.S.



Note. Data from *Job Openings and Labor Turnover Survey*, Bureau of Labor Statistics, n.d. (https://www.bls.gov/jlt/).

Executive Order, Continued Assistance for Unemployed Workers Act, American Rescue Plan Act

Following the expiration of the $600 weekly supplemental benefit in August, President Trump used executive action to temporarily enact a $400 weekly supplemental benefit that expired before the end of 2020 when the program's funds were exhausted (U.S. Department of Labor, n.d.). Whereas the federal government funded the $600 weekly supplemental benefit, the states were required to contribute one quarter of the $400 weekly supplemental benefits under this executive order.

In January 2021, a $300 weekly supplemental benefit was introduced as part of the Continued Assistance for Unemployed Workers Act, which had been signed into law the previous year (U.S. Department of Labor, 2021). Unfilled job openings in January then increased more than any month since July 2020, when the $600 supplemental benefit was still in effect. While the $300 supplemental benefit was set to expire in March 2021, President Biden signed the American Rescue Plan Act that month, which extended the supplemental benefit into September (H.R.1319, 2021).[7] March 2021 saw a then-record high for unfilled job openings, followed by four more new highs in as many months. The first decline in job openings did not come until August, when about half of the states were no longer participating in the supplemental benefit program.

States Reject Supplemental Benefits

By the late spring of 2021, a considerable amount of economic research—both theoretical and empirical—indicated that the $300 weekly supplement was causing millions of people to remain unemployed instead of returning to work (Mulligan et al., 2021b). Given this information, many states ended their participation in the program before its expiration in September, causing supplemental benefits to cease in those states. Twenty-two of these states ended their participation in the program in June, while three ended it in July and one in August.

This produced a pronounced effect in those states' labor markets. Holzer et al. (2021) found workers moved from unemployment into employment about two thirds more quickly following termination of the supplemental benefits. Furthermore, those states that terminated the program early converged on their pre-pandemic employment levels significantly faster than those states that continued with the weekly supplemental benefits.

While a variety of methods exist to examine a labor market, the one chosen for this analysis is the rate at which a state is approaching its pre-pandemic level of non-farm payroll. This is expressed as a ratio of monthly job increases to the jobs below the February 2020 level. (See the appendix for a more comprehensive explanation of this metric.)

In May 2021, the last month in which all states participated in the $300 weekly supplemental benefit program, the states that would end those benefits in the next month gained 3.96% of their "missing" jobs — that is, the difference between a state's current employment level and that state's employment level in February 2020. Meanwhile, the states that continued participating in the program through June gained 4.05%, meaning the labor market in those states was recovering faster. That changed the following month, however.

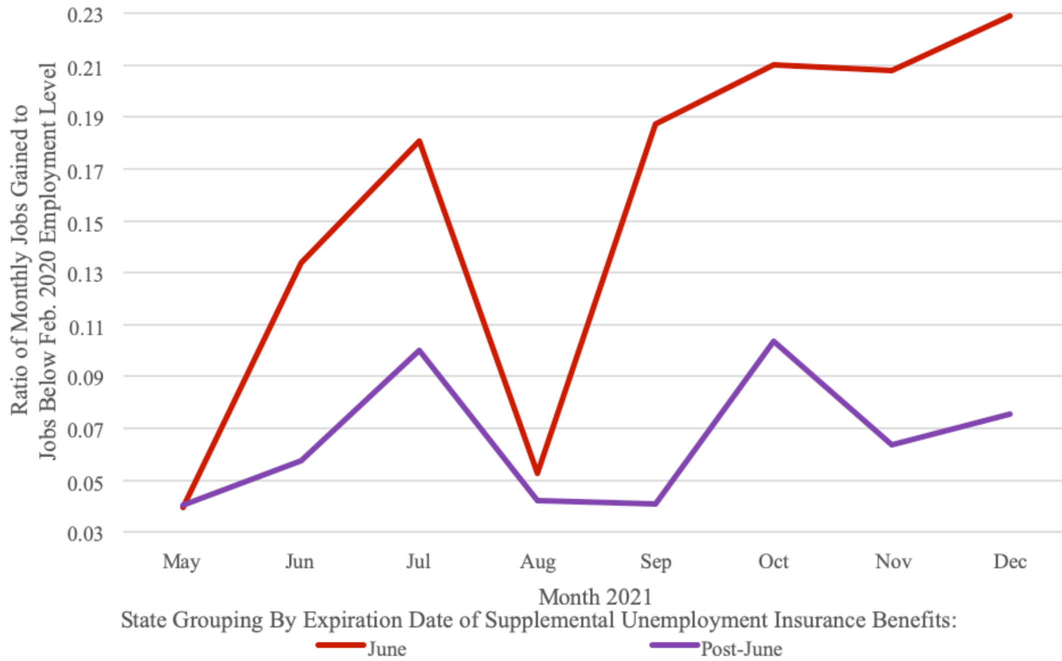
In June, states that ended the supplemental benefits recovered 13.38% of their missing jobs, while those that allowed the program to continue added only 5.75% of their missing jobs, less than half the rate of their counterparts (**Figure 3**). Each month through December 2021, the states that stopped the supplemental benefits in June continued recovering their missing jobs faster than those states that ended the program after June.

Similarly, those states that ended the supplemental benefits by July (**Figure 4**) and August (**Figure 5**), as compared to those states that did not end the program by those months, also approached pre-pandemic levels of employment significantly faster, though not as fast as those states that terminated the program in June.

According to the December 2021 Employment Situation from the U.S. Department of Labor, the latest data available at the time of this writing, only four states have reached (and surpassed) their pre-pandemic levels of employment: Arizona, Idaho, Texas, and Utah. All four terminated the supplemental benefits before September 2021.

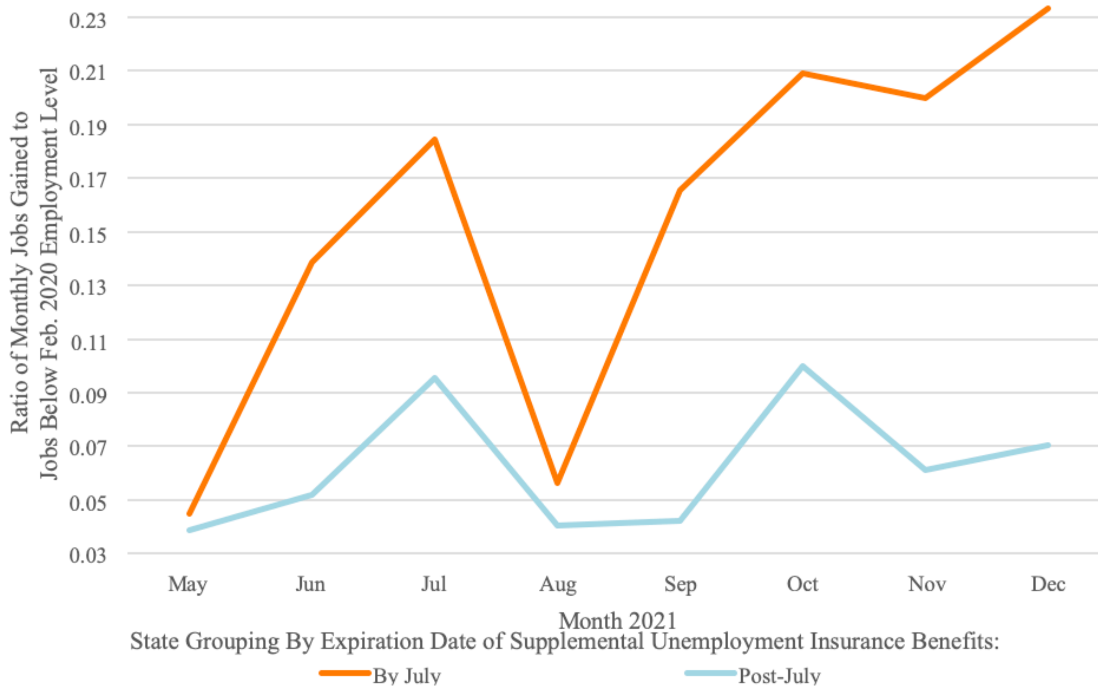
7 This act also retroactively made the first $10,200 of unemployment compensation non-taxable for federal income tax purposes (Internal Revenue Service, 2021). While this effectively rewarded people for not working, it would not have had an impact on someone's decision to work in 2020 because it was enacted in 2021. However, it could have changed people's expectations as to the tax treatment of future unemployment compensation, which would then impact unemployment levels beyond February 2021. It is also possible that an individual's unexpectedly reduced tax liability could result in a savings windfall, with money previously set aside for payment of taxes now available to be spent. This influx of liquidity would also impact unemployment levels beyond February 2020.

Figure 3
States Terminating Supplemental Benefits Recovered Faster



Note. Data from *State Employment and Unemployment,* Bureau of Labor Statistics, 2022, (https://www.bls.gov/news.release/laus.nr0.htm) and author's calculations.

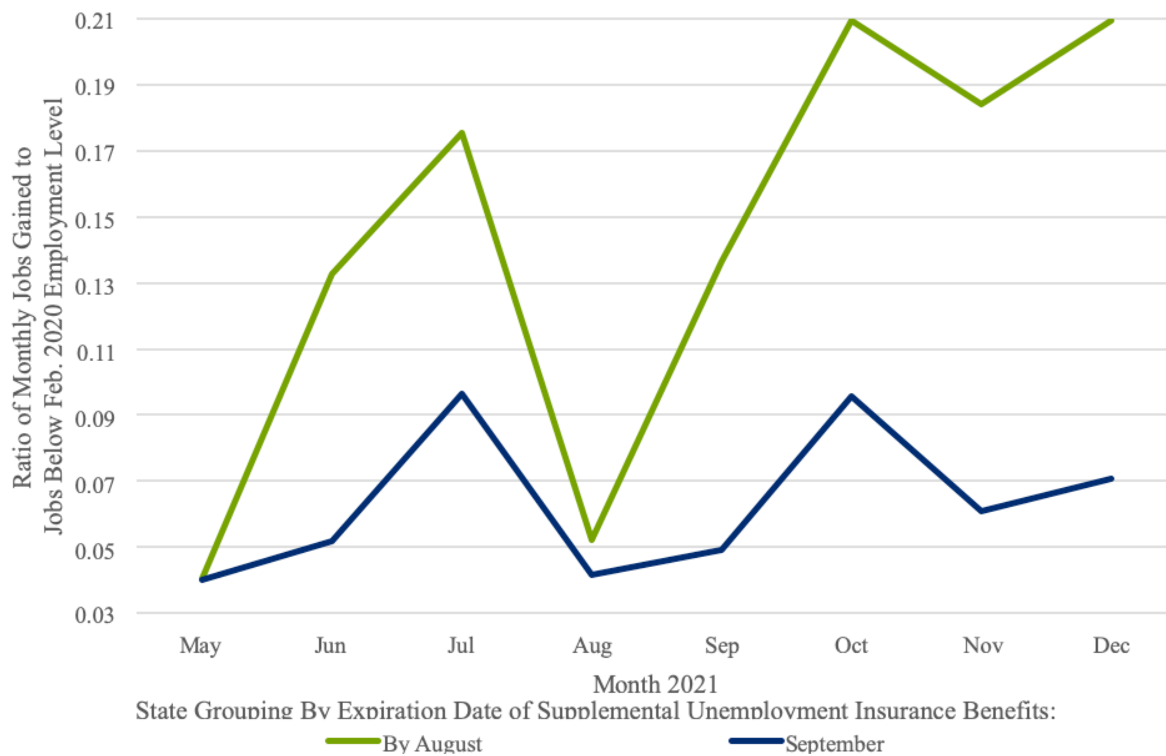
Figure 4
Supplemental Benefits Terminated by July



Note. Data from *State Employment and Unemployment*, Bureau of Labor Statistics, 2022, (https://www.bls.gov/news.release/laus.nr0.htm) and author's calculations.

Figure 5

Supplemental Benefits Terminated by August



Note. Data from *State Employment and Unemployment*, Bureau of Labor Statistics, 2022, (https://www.bls.gov/news.release/laus.nr0.htm) and author's calculations.

In aggregate, the states that withdrew from the program early have recovered 98.9% of their pre-pandemic jobs, while those states that kept the supplemental benefits in place through September have recovered only 95.9%. That 3.0-percentage-point difference represents about 3 million employees that still have not returned to the labor market. Of the 20 states with the highest ratios of current employment to pre-pandemic levels, 17 ended the supplemental benefits early. The two states with the lowest ratios (Hawaii and New York) maintained the benefits through September. Of the 19 states with the lowest ratios, 15 maintained the supplemental benefits through September.

Conclusion

The implementation of supplemental unemployment insurance benefits disrupted the labor market recovery in 2020 and 2021 by providing a strong disincentive to work. This was true in each incarnation of the policy, whether at $600, $400, or $300 per week, although the effect was certainly diminished as the benefit amount decreased. The astute observer will likely note that those 26 states that ended the supplemental benefits early are almost all typically classified as Republican states, with only one of the governors being a Democrat. However, data are nonpartisan. The supplemental unemployment insurance benefits were begun under a Republican president and continued under a Democrat. This analysis demonstrates that the issue here is about policy, not politics. Acknowledging this reality may serve to prevent the implementation of a similar statute in the future. Even if this or a similar policy is again enacted, the states should likely withdraw their participation to mitigate the economic fallout within their respective borders.

One alternative to supplemental unemployment insurance benefits would have been eliminating payroll taxes. While the supplemental benefits disincentivized millions of people returning to work in 2020 and 2021, cutting payroll taxes would instead have removed an existing disincentive by allowing employees to keep more of what they earned, a benefit that is only accrued by working. Mulligan and Moore (2020) found that eliminating payroll taxes would have added 2.7 million jobs in six months and increased gross domestic product by 1.2%. This is just one example of a policy that, instead of disrupting the labor market recovery, would have facilitated job growth. ✩

Appendix

Measuring the health of the labor market poses many challenges. The unemployment rate illustrates this phenomenon. If people actively searching for jobs become employed, that will lower the unemployment rate, all else being equal. However, if those same people instead stop looking for work and leave the labor force, that will also reduce the unemployment rate because of how the rate is calculated, all else being equal. Furthermore, the commonly cited unemployment statistic (known as U-3) does not include marginally attached or underemployed workers. Other metrics like total compensation add further complications such as questions of distribution.

The employment level avoids some of these concerns, but admittedly not all, and introduces others. The establishment survey data from the U.S. Department of Labor does not include agricultural workers or the self-employed but can double count workers who hold more than one job, for instance. Despite these shortcomings, it is the best available data for this analysis.

The choice of using a relative metric instead of a one-to-one comparison was three-fold. First, since the states vary in size, comparing total job growth from one state to another would be irrelevant. Second, some states had sustained much larger job losses due to stricter and more prolonged lockdowns than other states. In the late spring and early summer of 2021, many of those states began reopening their economies, creating job growth that many other states had already undergone in the previous months. This offers an explanation as to why states that would maintain the supplemental benefits were gaining jobs faster in May than their counterparts that would end the supplemental benefits. Therefore, a metric comparing the states must account for the relative positions of each state in February 2020 and May 2021. Third, as an economy approaches full employment, nominal job gains increase at a decreasing rate, adding fewer and fewer jobs until maximum employment is reached, all else being equal. Consequently, one would not expect the labor market in a state to continue adding the same number of jobs every period until full employment is reached, at which point the number of jobs added would suddenly decline to zero. The more asymptotic path from recessionary trough to full employment creates a challenge for comparing states that are at different points along that path, requiring a relative measurement of how fast a state is converging upon full employment or some other threshold.

In this analysis, that threshold is February 2020, the last month of data before the pandemic. To measure the monthly convergence of a state toward its pre-pandemic labor market norm, I compute the following ratio for each month beginning in May 2021:

$$\frac{m_{i1} - m_{i0}}{Feb2020_i - m_{i0}}$$

where m_{i1} is the current month's employment level, m_{i0} is the previous month's employment level for state i, and $Feb2020_i$ is the employment level in February 2020 for state i. Thus, the ratio expresses the proportion of jobs gained in a period to the number of jobs still below the February 2020 employment level for each state.

While perhaps not representative of full employment in every state, using pre-pandemic levels of employment accounts for many extraneous factors, such as state tax rates (a heterogeneity that is constant over the time period in question). This approach is similar to the statistical technique of a Fixed Effects estimator, which measures within-unit differences and not between-unit differences, after the Fixed Effects transformation demeans the data. In that kind of regression analysis, each unit can have a unique intercept. In this paper's analysis, each state has its own baseline, which serves as a benchmark for recovery in the labor market to its respective pre-pandemic norm of February 2020.

Lastly, there is still the question of what appears to be lingering effects through the remainder of 2021, with those states that continued supplemental benefits still lagging their counterparts. Some possible explanations follow here.

In October 2021, the first month in which the $300 weekly supplemental benefit had ended nationwide, the states that had participated in the program through September saw a marked improvement in employment, approaching pre-pandemic employment levels 94% faster than in September. Conversely, states that ended the supplemental benefits before September improved 54% from September to October. While the labor market grew substantially nationwide in October, there was a noticeable improvement in states that had been paying supplemental benefits in the prior month.

Additionally, maintaining the supplemental benefits resulted in fewer people working, which meant less productivity and output. That may have driven jobs out of state as the economy shrank, or at least grew slower, and people left for states where they could hire workers, taking their businesses with them; recent census data indicate that, in 2021, people moved out of states maintaining the

benefit and into states that terminated the benefit early (U.S. Census Bureau, 2021).

Furthermore, personal savings increased nearly fourfold during the pandemic because of the myriad of government stimulus efforts that were employed (U.S. Department of Commerce, 2021). With the expansion of various federal and state welfare programs (such as the Supplemental Nutrition Assistance Program), people have been able to spend longer periods of time on government assistance. With the withdrawal of supplemental unemployment benefits, and as savings levels return to their pre-pandemic norm, this is expected to wane.

Finally, when faced with an inability to hire employees, businesses may also have automated where financially feasible and when previously near the margin of that decision, thereby eliminating some jobs that predated the pandemic. Empirical testing of these theories is left to future research when more adequate data are available.

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