

Employment Insurance (EI) Reform

The desired long-term goals of EI reform are to improve fairness of the system, reduce work disincentives, promote labour force mobility, and ensure program costs do not create a drag on economic activity and job creation.

Under existing rules, the Canadian Employment Insurance Financing Board is mandated to increase EI premiums to eliminate deficits (any excess of EI benefits over premiums) accumulated in the EI account since 2009, excluding \$2.9 billion of benefit enhancements announced in Budget 2009 that the federal government has committed not to count among the funds to be replenished in future years.

The projections in the 2010 federal budget suggest EI premiums will rise significantly (the maximum of 15 cents) over the 2011-2014. Thereafter, premiums will be set at the break-even level. Rising payroll taxes will discourage employers from hiring just as the economic recovery matures. Over the long-term, these costs are ultimately passed on to employees in the form of lower wages, taking a bite out of personal income. The large "wedge" created between the cost of hiring employees and workers' take-home pay stifles productivity and damages the economy's long-term performance.

The Canadian Chamber believes EI premium rate increases can be kept at manageable levels by balancing the EI Account over the business cycle of up to ten years.

To promote fairness and efficiency in the tax system, a number of longer-term structural issues must also be addressed:

- Both the Technical Committee on Business Taxation (1997) and the OECD (2004) recommended that Canada design and introduce an employer-based experience rating system. Businesses that lay off fewer workers would pay lower premiums, and would have a greater incentive to create jobs. Without employer-based experience rating, the EI system levies taxes on firms that minimize layoffs (for example, through smoothing of production and the use of work-sharing arrangements) and subsidizes businesses that readily resort to layoffs. The Canadian Chamber recommends that the federal government gradually phase in an employer-based experience rating system.
- Employers pay 1.4 times the employee premium rate, or 58.2 percent of EI premiums. This is a significant cost for businesses, particularly small- and medium-sized businesses. The rationale behind this is that employers have greater control over layoff decisions and, therefore, should bear a higher overall share of program costs. In recent years, however, EI benefits totally unrelated to layoffs (for example, parental leave benefits) have contributed to higher program costs, and represent about 37 percent of income support provided through EI. There is no reason for employers to pay more for these benefits than employees do.
- If employee EI premium payments exceed the maximum contribution limit, employees are refunded the difference between what they have paid in any given year and the maximum annual contribution limit when they file their yearly income taxes. Employers are not afforded the same treatment. Even though an employee has contributed the maximum amount in his/her previous job during a given year, the employee's new employer must also contribute on the basis of current employee earnings. While it is difficult to quantify the exact level of over-contributions by employers, it is certainly in the several hundred million dollar range. Given the fact that EI premiums represent a barrier to job creation, the federal government should devise and implement a system that allows for over-contributions by employers to be refunded.

To improve accountability and transparency, the EI program should be operated as a true insurance program – one that provides temporary income support to qualified individuals who involuntarily lose their job. The social-program aspects of EI (like training-related benefits) should be placed within general program spending. Employers and employees would fund the insurance elements, and taxpayer would

cover the social benefits. This would facilitate further reductions in EI premium rates, making it more attractive for employers to hire more workers.

Finally, fiscal conditions permitting, the government should adopt a national eligibility standard (560 hours) and standardize duration of benefits (22 to 45 weeks) to ensure regional fairness. For EI purposes, Canada is currently divided into 58 'economic regions'. The criteria to qualify for EI benefits ranges from 420 to 700 hours of insured work in the previous 52 weeks, and benefits last from 14 to 45 weeks depending on regional unemployment rates. Where benefits are less accessible, Canadians who lose their jobs are unfairly treated. When they are more accessible, they discourage labour market adjustment (i.e. upgrading of one's skills and relocating to where the jobs may be). The misallocation of labour reduces overall economic output and hampers productivity.

Recommendations

That the federal government:

1. Immediately amend the present rate-setting formula with a view of balancing the EI Account over the business cycle of up to ten years.
2. Operate the EI program as a true insurance program to facilitate further reductions in EI premium rates. Remove the social-program aspects of EI from the regular premium structure, and fund these programs out of general revenue (i.e. from taxes collected).
3. Gradually (i.e. over a five year period) reduce the employer EI premium rate to equal that paid by employees.
4. Implement a system that allows for over-contributions by employers to be refunded.
5. Ensure equal access to benefits across Canada by standardizing eligibility requirements at 560 hours and benefit duration at 22 to 45 weeks.