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OpEd

Getting off the EI roller-coaster

September 21, 2010, Calgary Herald – Colin Busby, Alexandre Laurin

News that the federal government is considering raising employment insurance (EI) premiums rightly concerns the workers and employers who may face higher tax burdens. But for those who read budget documents carefully, this announcement is no surprise.

The prospect of raising EI premiums was largely settled in the last federal budget. Indeed, EI premium rates were budgeted to rise substantially over the next few years from their current historical low.

In fact, were it not for a temporary rate freeze as part of the fiscal stimulus package, EI premium rates would have started their ascent right in the midst of the recession. Why? Because under existing legislation, neither an EI account surplus nor a deficit is allowed to 'permanently' mount up.

Consequences of this legislation are that EI rates must rise when the economy slows and unemployment sharply ratchets up, and must keep on rising for years until any EI-related accumulated deficits are repaid. On the contrary, when the economy is expanding rapidly and unemployment is on a gradual decline, premium rates must fall to avoid the build up of a surplus within the EI account.

Paradoxically, this EI rate-setting process was passed into legislation just a few months before serious economic troubles began at the end of 2008. At the time, some observers, such as the Canadian Institute of Actuaries, recognized the dangers of EI premium rate variations closely mimicking economic ebbs and flows and thus fiercely opposed this new mechanism during Parliamentary Committee review.

The real question is whether more fiscal stimulus is required next year, especially since further growth of the EI account deficit -- which is already expected to reach about \$11 billion by the end of 2010 -- would need to be immediately repaid by a greater and longer climb of EI premium rates, according to the legislation. And since the 2008 reform now prevents the diversion of EI funds for other government purposes, accumulated EI deficits can only be funded with government debt in the short run.

If one rejects that model, it thus follows that a temporary band-aid solution -- such as an extension of the EI rate freeze -- is not what is needed. Instead, Canada needs a new EI rate-setting mechanism altogether. In the summer of 2009, we proposed a permanent solution to these predictable woes.

We start from the public policy perspective that the EI program should -- both for revenues or expenses -- counteract, or not contribute to, the negative effects of economic cycles. For fiscal planning purposes, this is an important and desirable feature because the timing of rate hikes can have adverse effects on hiring decisions, tax burdens and employment, and because EI payouts directly affects the government's bottom line.

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Policy-makers should move toward a more stable EI rate that tries to break even over time. And to prevent the development of a large surplus or deficit, such a mechanism would ensure that the cumulative balance remains within plus or minus a reasonable figure, say \$15 billion. If the cumulative balance were to move out of these limits -- due to unforeseen strength or weakness in unemployment, for example -- premium rates would then automatically adjust.

The integrity of this proposal, however, requires removing as much as possible EI funding decisions from political influences. This would be best accomplished through isolating the EI account bottom line from the federal general fiscal planning framework. It would remove the political temptation of using EI funds for other purposes, which undermined the last government's attempt at stabilizing EI rates in the mid-90s.

One way to completely isolate EI program finances from federal budgetary policies would be to separate the EI account from the official books and to manage the separate EI Account transparently at arm's length from the government. In its current form, however, segregating the EI account would likely violate the public accounting principle that a government's financial statements should comprise all activities controlled by that government.

Another feasible but less effective option would be to target a budgetary balance figure excluding EI. The EI account would still be part of federal financial statements, but its annual movements would have little influence on budget planning.

Canada's EI program, which is intended to function as an economic stabilizer, should not face pressure to raise rates in troubled times. A funding plan that stabilized rates over time would inject some long overdue credibility into EI's finances. History should not be repeated.

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