Volume 17
Issue 2
Fall 2012

inside the vault

AN ECONOMIC EDUCATION NEWSLETTER FROM THE FEDERAL RESERVE BANK OF ST. LOUIS

Unemployment Insurance

Payments, Overpayments, and Unclaimed Benefits

BY DAVID L. FULLER, B. RAVIKUMAR, AND YUZHE ZHANG

Overpayments in the U.S. unemployment insurance system have received increasing attention of late. For example, CNN.com cited a recent study by the Department of Labor in reporting that 11 percent of all unemployment benefits were overpayments. Overpayments can be the result of errors on the part of government administrators, employers, and employees or it can be outright fraud.

First we examine the benefits the U.S. unemployment insurance system has paid out from 1989 to 2011. Next we look at the overpayments for the same time period. Finally, we discuss a fact that is less well-known: Not everyone who is eligible for unemployment benefits actually collects them. Over the longer horizon, these unclaimed benefits are much larger than the overpayments that have received recent attention.

Unemployment Insurance

Unemployment insurance programs insure workers against the risk of lost income if they lose their job through no fault of their own. In the U.S., the program is run at the state level. Each state sets its benefit level and eligibility criteria and finances these benefits through payroll taxes. There are three primary criteria for eligibility: First, the individual must have accumulated enough earnings or worked a minimum number of weeks during the previous year. Second, only those who lost their job through no fault of their own are eligible; thus, people who quit their job or are fired because of poor performance are not eligible. Third, the duration of benefits is limited.

Typically, unemployment benefits last for a maximum of 26 weeks. These regular unemployment benefits paid by the states increased sharply during the recent recession. Measured in 2005 dollars (all amounts are reported in 2005 dollars), these benefits more than doubled, from $31 billion in 2007 to almost $72 billion in 2009. Since 2009, these regular benefits have decreased to levels below what they were after the previous recession: In 2011, the unemployment insurance program spent less than $42 billion on regular benefits, while the corresponding figure in 2002 was more than $46 billion.[1]

In periods of high unemployment, benefits may be continued beyond the typical cap of 26 weeks. Most states offer an additional 13 weeks of benefits when the unemployment

continued on Page 2

What's Your Question?
Unemployment Benefits

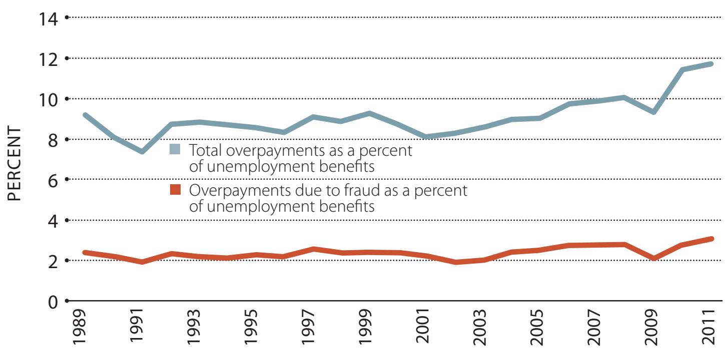
Economic Snapshot
Unemployment Benefits

Resources
Econ Lowdown lessons and online courses

www.stlouisfed.org/education_resources

rate in that state remains above a certain threshold. The federal government may also finance more benefits. For example, the federal government recently provided financing to some states to extend their benefits to a maximum of 99 weeks. During the early 1990s, extended unemployment benefits added 60 percent on top of the regular 26 weeks of benefits. During the past two years, the extended benefits have added more than 125 percent.

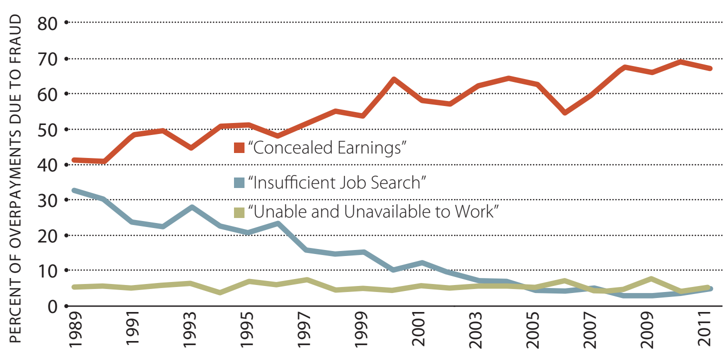
FIGURE 1



SOURCES Benefit Accuracy Measurement (BAM) program, U.S. Department of Labor; authors' calculations.

NOTES The fractions reported by the blue line are the total dollar amount of overpayments in a calendar year divided by the total dollar amount of benefits paid in the same year. Both amounts were obtained directly from the BAM sample and include only the payments by states for the standard 26 weeks. A similar calculation was used to compute the fraction reported by the red line.

FIGURE 2



SOURCES Benefit Accuracy Measurement (BAM) program, U.S. Department of Labor; authors' calculations.

NOTES The calculations use dollar amounts, not number of cases. To calculate the numbers in the figure, we first sum up the dollar amounts of overpayments due to all 28 types of fraud. Then, for each of the three forms of fraud discussed in the article, we calculate the total dollar amount of overpayments from the category. The numbers reported in the figure are the latter amounts each divided by the former.

Overpayments and Fraud

Some unemployment benefit payments have indeed been overpayments, as recent newspaper reports suggest. Figure 1 illustrates the amounts overpaid. The average overpayment as a fraction of benefits during 2007-2011 was 11 percent. For example, during the middle of the recent recession in 2008, total unemployment benefits were $40 billion and total overpayments were $4 billion.

The overpayments could stem from simple typographical errors on one extreme to outright fraud on the other extreme. For example, an individual's benefit may be inadvertently set too high because the wrong formula was applied. This represents a simple error. Fraud, on the other hand, is a deliberate act. During 2007–11, overpayments due to fraud accounted for 25 percent of all overpayments and 3 percent of all payments on average (see Figure 1). Put differently, overpayments due to fraud were roughly a fourth of the total overpayments.

Types of Fraud

The Benefit Accuracy Measurement (BAM) program run by the U.S. Department of Labor classifies fraud in 28 categories. The dominant form of unemployment insurance fraud in recent years is what's classified as "Concealed Earnings" fraud: collection of unemployment benefits by individuals who are gainfully employed. As Figure 2 illustrates, overpayments from Concealed Earnings fraud have been steadily rising over the past 22 years and were almost 70 percent of the overpayments due to fraud in recent years.

Recent headlines on prisoners collecting unemployment benefits fall under "Unable and Unavailable to Work" fraud. This category includes cases where an unemployed person is not healthy enough to work or is in school, for example. Overpayments due to the entire Unable and Unavailable to Work category amounted to barely 5 percent of fraud in 2011.

Meanwhile, overpayments due to "Insufficient Job Search" (cases where the unemployed individual did not, but claimed to meet the mandatory work search requirement, such as the minimum number of job applications to be filed each week) have been declining and are down to less than 5 percent of fraud.

Unclaimed Benefits

Some unemployed persons never seek benefits. Although overpayments have grabbed recent headlines, only 35 percent of the unemployed have been collecting benefits over the past 22 years on average. Not all of these people are eligible to collect benefits,

however. For instance, the typical duration of unemployment benefits is 26 weeks, and a person who continues to be unemployed past 26 weeks is not eligible.

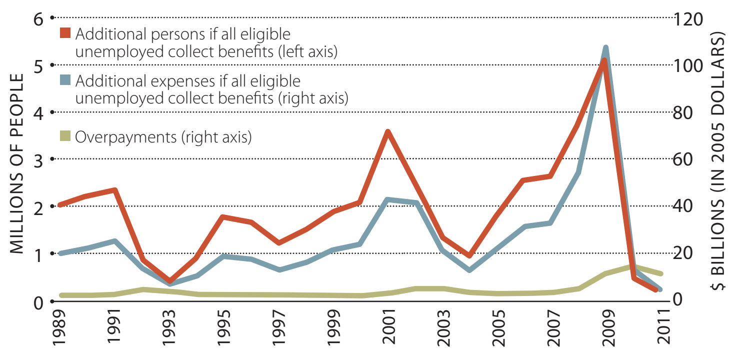
During the recent recession (2007-09), roughly 50 percent of those eligible were collecting benefits. The fraction increased to 95 percent in 2011. In Figure 3, we illustrate the number of people who could have collected unemployment benefits but chose not to do so.

Figure 3 also illustrates a back-of-the-envelope calculation. If all of those who are eligible to collect unemployment benefits were to indeed collect the benefits, what would be the additional expenditures for the unemployment insurance program? The additional expenditures in 2009, toward the end of the recent recession, would have been a whopping $108 billion. As Figure 3 illustrates, the overpayments in 2009 were $11 billion. On average, more unclaimed benefits are left on the table than improper benefits taken off the table.

Looking at the unemployment insurance program over the longer horizon, overpayments are less than one-tenth of the benefits paid, overpayments due to fraud are less than 3 percent of the benefits paid, and unclaimed benefits are nearly seven times the overpayments. Although reducing the overpayments would clearly help reduce the expenditures for the unemployment insurance program, a higher fraction of eligible people choosing to collect unemployment benefits would significantly increase the expenditures for the program.

1. We obtain the nominal actual outlays from the Department of Labor, www.doleta.gov/unemploy/chartbook.cfm, and convert them to 2005 dollars using the GDP deflator in the FRED database, http://research.stlouisfed.org/fred2/.

FIGURE 3



SOURCES Overpayments: Benefit Accuracy Measurement (BAM) program, U.S. Department of Labor; authors' calculations.

NOTES We calculate the numbers for the green line by multiplying the overpayment rate in Figure 1 by the amount of total unemployment benefits paid (that is, including extended benefits) reported by the Department of Labor.

To obtain how many additional people could collect benefits, we use the calculations in this paper: Auray, Stephane; Fuller, David L.; and Lkhagvasuren, Damba. "Unemployment Insurance Take-up Rates in an Equilibrium Search Model." Working Paper, Concordia University, 2012. They compute the fraction of eligible unemployed who are collecting benefits by using Current Population Survey data and details on eligibility requirements for all U.S. states. We increase their fraction to 100 percent (as if all eligible unemployed collect benefits) and calculate the additional number of unemployed who could legitimately collect benefits. Additional expenses are calculated as follows: We divide the total unemployment benefit expenditures each year by the number of unemployed people collecting benefits in that year to obtain a benefit amount per person. Both of these numbers are tabulated by the U.S. Department of Labor; see www.doleta.gov/unemploy/chartbook.cfm. We then multiply the additional number of people by the benefit/person to obtain "Additional expenses if all eligible unemployed collect benefits."

Glossary

Back-of-the-envelope calculation — Informal computation using estimates and/or rounded numbers to reach a general answer.

Benefit Accuracy Measurement (BAM) program — BAM is a quality control statistical survey that investigates and reviews the records of a sample group of claimants selected each week at random to test the accuracy of decisions to issue or deny benefits for that week. The program, administered by each of the 50 states for the U.S. Department of Labor, identifies errors and abuse in unemployment programs from approximately 24,000 cases annually. Causes of erroneous payments or denials may include administrative oversight and misrepresentation or errors by claimants and/or employers.

Concealed earnings fraud — Deliberately not revealing earnings in order to receive unemployment benefits; deception by gainfully employed individuals to collect unemployment benefits for which they are not eligible.

Employed — People 16 years and older who have jobs.

Employer — A person or business that provides work to others and a monetary payment in exchange for that work.

Employee — A person who works for an employer in exchange for a monetary payment.

Extended unemployment benefits — Additional weeks of benefits available to workers who have exhausted regular unemployment insurance benefits during periods of high unemployment.

Fraud — Deliberate misrepresentation of facts for profit or gain in violation of laws and regulations.

Job Search Fraud — Deliberate misrepresentation by unemployed persons to collect unemployment benefits by claiming to meet mandatory work search requirements, such as the minimum number of job applications to be filed each week.

Recession — A period of declining real income and rising unemployment; significant decline in general economic activity extending over a period of time.

Unemployed — People 16 years of age and older who are without jobs and actively seeking work.

Unemployment — A condition where people at least 16 years old are without jobs and actively seeking work.

Unemployment benefits — Unemployment insurance payments given to provide temporary financial assistance to eligible unemployed workers who are unemployed through no fault of their own and who meet their state's eligibility requirements.

Unemployment insurance — Federal-state insurance that provides unemployment benefits to eligible workers who are unemployed through no fault of their own and meet the eligibility requirements of their state's law.

Unable and unavailable for work fraud — Deliberate misrepresentation of not being healthy enough to work or being available for work by an unemployed person filing for unemployment benefits.

Unemployment Benefits

1. **Why does the cost of unemployment benefits vary among the states?**

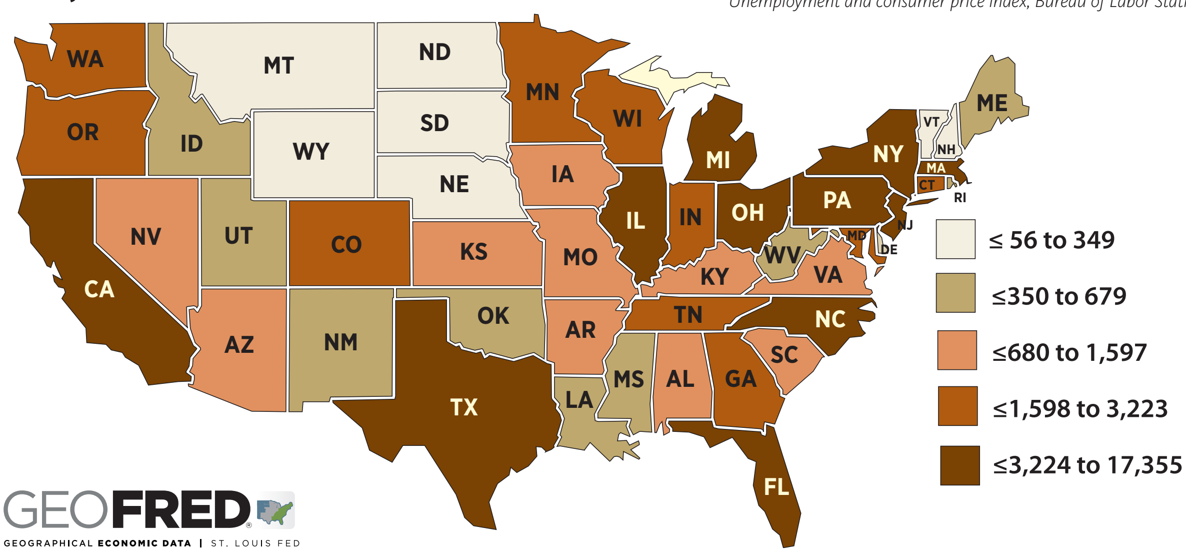
   The cost of unemployment insurance claims in individual states varies due to several factors: the total population, the number of persons who are unemployed, the unemployment rate of the state, and the specific guidelines of the state.

Current Economic Data

	Q4-'11	Q1-'12	Q2-'12	Q3-'12
Growth Rate Real GDP	4.1%	2.0%	1.3%	2.7%*
Inflation Rate Consumer Price Index	1.3%	2.5%	0.8%	2.3%
Civilian Unemployment Rate	8.7%	8.3%	8.2%	8.1%

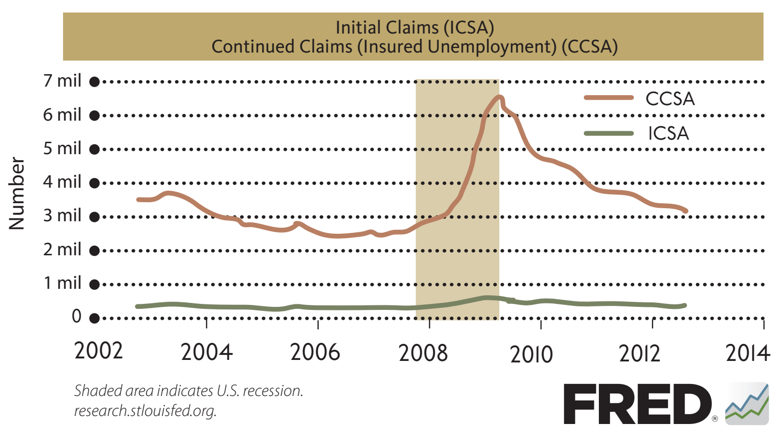
**Second estimate*
SOURCE: GDP, Bureau of Economic Analysis; www.bea.gov.
Unemployment and consumer price index, Bureau of Labor Statistics; www.bls.gov.

2011 State Unemployment Benefits by State (millions of dollars)



2. **How does the number of initial claims for unemployment insurance compare with the number of continued claims? What conclusion can be drawn from this analysis?**

   The number of initial claims has remained relatively stable over the past ten years and the greatest fluctuation is seen in the tan bar, which shows the recent recession. The number of continued claims has consistently been much higher than initial claims and has shown more volatility, especially during the past recession (as shown in the graph at right). This indicates a recent trend for unemployed persons to receive continued benefits.



Shaded area indicates U.S. recession.
research.stlouisfed.org.

Unemployment Benefits

1. What government agency collects data on unemployment insurance benefits?

United States Department of Labor

2.When was the unemployment insurance program created, and how is the program managed?

The current federal-state system of unemployment insurance (UI) traces its origins to the Social Security Act and related laws of 1935. Each state administers a separate unemployment insurance program within guidelines established by federal law.

3. How are unemployment insurance benefits funded?

In most states, benefit funding is based solely on a tax imposed on employers. Unemployment taxes are paid by employers to the federal government and to states to fund unemployment compensation benefits for out-of-work employees. (Three states—currently, Alaska, New Jersey, and Pennsylvania—also impose unemployment insurance taxes on employees.)

The Federal Unemployment Tax Act (FUTA) authorizes the Internal Revenue Service (IRS) to collect a federal employer tax used to fund state workforce agencies. Currently, the federal tax is 6.2 percent on the first $7,000 in annual wages to each employee. FUTA covers the costs of administering the program in all states, pays one-half of the cost of extended unemployment benefits during periods of high unemployment, and provides a fund from which states may borrow to pay benefits.

State law determines individual state unemployment insurance tax rates. The state unemployment tax, paid to state workforce agencies, is used solely for the payment of benefits to eligible unemployed workers. State tax rates vary from state to state, as does the amount of each worker's income that's subject to the tax—which ranges from $7,000 to $34,000.

4. Is the national unemployment rate released each month by the Bureau of Labor and Statistics the same as the number of persons receiving unemployment insurance benefits?

No. The unemployment rate released each month by the BLS estimates unemployment based on a monthly sample survey of more than 60,000 households. A person's unemployment status is established by responses to a series of questions about whether they have a job, whether they want a job and are available to work, and what they have done to look for work in the preceding 4 weeks. The unemployment rate is the number of unemployed persons as a percent of the labor force (employed and unemployed persons). There is no requirement or question relating to unemployment insurance benefits in the monthly survey. The unemployment data derived from the household survey in no way depend upon the eligibility for or receipt of unemployment insurance benefits. Some people are still unemployed even when their benefits run out, and many more are not eligible at all or delay or never apply for benefits.

Statistics on persons receiving unemployment insurance benefits (sometimes called insured unemployment) are collected as a byproduct of unemployment insurance programs.

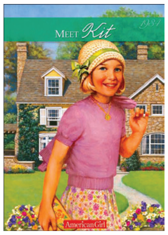
5. How long can a person receive unemployment benefits?

Unemployment insurance payments (benefits) are intended to provide temporary financial assistance to unemployed workers who meet the requirements of state law and typically run for 26 weeks. However, since 1970, federal law requires provisions for extended unemployment benefits in times of high and rising unemployment and some unemployed persons may qualify for these benefits. When a state's unemployment rate reaches a certain level, the time for receiving benefits must be extended. The basic Extended Benefits program provides up to 13 additional weeks of benefits and some states have also enacted a voluntary program to pay up to 7 additional weeks (20 weeks maximum) of Extended Benefits during periods of extremely high unemployment.

6. Is unemployment insurance taxable, and how often are the payments received?

Unemployment insurance payments are deemed taxable income by the Internal Revenue Service. Most states measure unemployment in calendar weeks and make payments weekly.

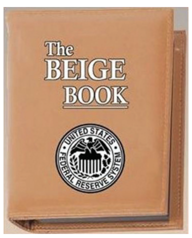
GRADES 3-5



Meet Kit: An American Girl

This lesson with SMART™ Board application complements the book, *Meet Kit: An American Girl*. Students listen to the story about a young girl's life in America during the Great Depression. They learn through discussion and role-playing about the impact that unemployment and reduced consumer and business spending can have on people's lives. *(Book written by Valerie Tripp / ISBN: 1-58485-016-7)*

GRADES 6-12



Are you looking for a lesson that features an active demonstration, primary sources, data, and current events. Look no further. *What Is Unemployment, How Is It Measured, and Why Does the Fed Care?* features all of these. Students participate in an activity to determine who makes up the labor force and who the unemployed are. They then use the data generated to learn how the unemployment rate is calculated. Next, they read and interpret maps that contain actual unemployment data. They compare verbal descriptions for the labor market from the Federal Reserve's *Beige Book* with the mapped data. They look at mapped data from other years and write descriptions to represent the data like those they read in the *Beige Book*.

GRADES 9-12

The *Story of Unemployment* online course teaches students the answer to these questions: How is unemployment calculated? Why might people become unemployed? What can be done to get people back to work? Students also explore how education will help them avoid unemployment in the future. Enroll your students in the two-hour course today at www.stlouisfed.org/education_resources/The_Story_of_Unemployment.cfm.

Two St. Louis Fed Economic Lowdown podcasts complement this edition of *Inside the Vault*. Go to www.stlouisfed.org/education_resources/podcasts.cfm to access Episode 5: *Unemployment* and Episode 10: *The Labor Market*. Use this extra review to reinforce concepts already learned.

That's a Winner!

For the second year in a row, the St. Louis Fed's Education Resources website has won an Award of Excellence from *Tech & Learning Magazine.*

Bank Contacts

Little Rock
Kris Bertelsen
501-324-8368
Kris.A.Bertelsen@stls.frb.org

Louisville
Erin Yetter
502-568-9257
Erin.A.Yetter@stls.frb.org

Memphis
Jeannette Bennett
901-579-4104
Jeannette.N.Bennett@stls.frb.org

St. Louis
Mary Suiter
314-444-4662
Mary.C.Suiter@stls.frb.org

Barb Flowers
314-444-8421
Barbara.Flowers@stls.frb.org

Scott Wolla
314-444-8624
Scott.A.Wolla@stls.frb.or

Jennifer Bradford
314-444-4608
Jennifer.L.Bradford@stls.frb.org

FEDERAL RESERVE BANK *of* ST. LOUIS
CENTRAL to AMERICA'S ECONOMY®
P.O. Box 442
St. Louis, MO 63166
STLOUISFED.ORG

PRSRT STD
U.S. POSTAGE
PAID
ST. LOUIS, MO
PERMIT NO. 444

Inside the Vault is written by economic education staff at the Federal Reserve Bank of St. Louis, P.O. Box 442, St. Louis, Mo., 63166. The views expressed are those of the authors and are not necessarily those of the Federal Reserve Bank of St. Louis or the Federal Reserve System.

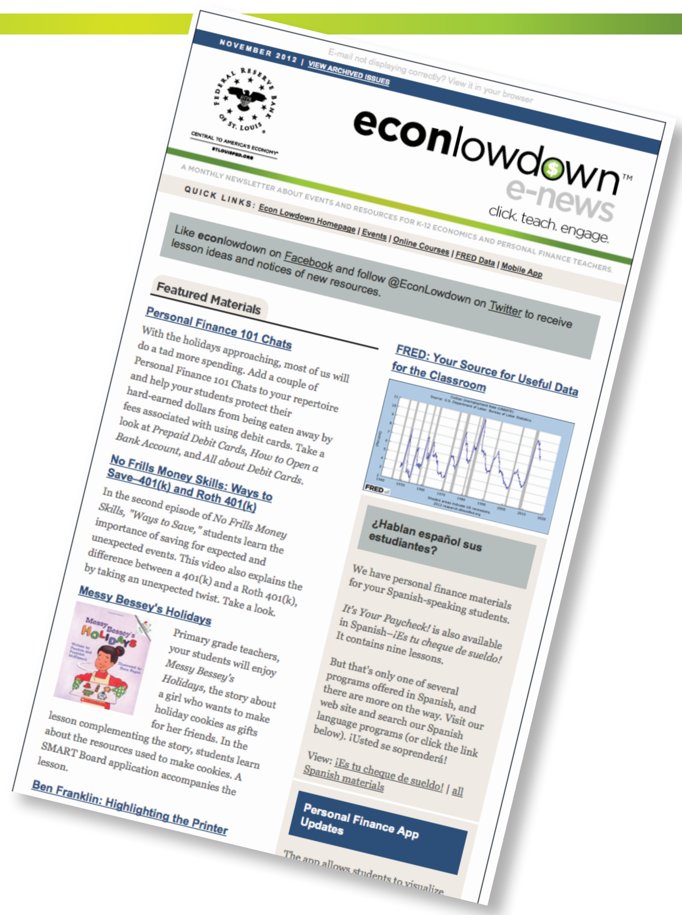
---

econlowdown™
click. teach. engage.

Would you like to receive our monthly newsletter about new resources and programs?

Subscribe here:

www.stlouisfed.org/education_resources/econ-lowdown-newsletter/


NOVEMBER 2012 | VIEW ARCHIVED ISSUES
E-mail not displaying correctly? View it in your browser
econlowdown™ e-news
click. teach. engage.
A MONTHLY NEWSLETTER ABOUT EVENTS AND RESOURCES FOR K-12 ECONOMICS AND PERSONAL FINANCE TEACHERS
QUICK LINKS: Econ Lowdown Homepage | Events | Online Courses | FRED Data | Mobile App
Like econlowdown on Facebook and follow @EconLowdown on Twitter to receive lesson ideas and notices of new resources.

Featured Materials

Personal Finance 101 Chats
With the holidays approaching, most of us will do a tad more spending. Add a couple of Personal Finance 101 Chats to your repertoire and help your students protect their hard-earned dollars from being eaten away by fees associated with using debit cards. Take a look at *Prepaid Debit Cards, How to Open a Bank Account,* and *All about Debit Cards.*

No Frills Money Skills: Ways to Save–401(k) and Roth 401(k)
In the second episode of *No Frills Money Skills,* "Ways to Save," students learn the importance of saving for expected and unexpected events. This video also explains the difference between a 401(k) and a Roth 401(k), by taking an unexpected twist. Take a look.

Messy Bessey's Holidays
Primary grade teachers, your students will enjoy *Messy Bessey's Holidays,* the story about a girl who wants to make holiday cookies as gifts for her friends. In the lesson complementing the story, students learn about the resources used to make cookies. A SMART Board application accompanies the lesson.

Ben Franklin: Highlighting the Printer

FRED: Your Source for Useful Data for the Classroom

¿Hablan español sus estudiantes?
We have personal finance materials for your Spanish-speaking students.
It's Your Paycheck! is also available in Spanish—*¡Es tu cheque de sueldo!* It contains nine lessons.
But that's only one of several programs offered in Spanish, and there are more on the way. Visit our web site and search our Spanish language programs (or click the link below). ¡Usted se sorprenderá!
View: ¡Es tu cheque de sueldo! | all Spanish materials

Personal Finance App Updates
The app allows students to visualize