

Wage insurance may be the best bet for older displaced workers

Displaced workers face enormous difficulties in attempting to re-enter the workforce. Governments attempt to resolve this problem through retraining programs for these workers to equip them with the necessary skills and knowledge for a new career.

A 2007 Statistics Canada study by René Morissette, Xuelin Zhang, and Marc Frenette indicates that men aged 25 to 49, who lost their jobs sometime between 1982 and 2002 through firm closures or mass layoffs and subsequently found new jobs, were earning on average between 9 and 22 percent less five years later.^a

The average decline for women was 12 to 35 percent. Earnings losses by displaced workers with five or more years of seniority were higher than those for other workers. The earnings loss was more severe in the 1987–92 period, which included a deep recession.

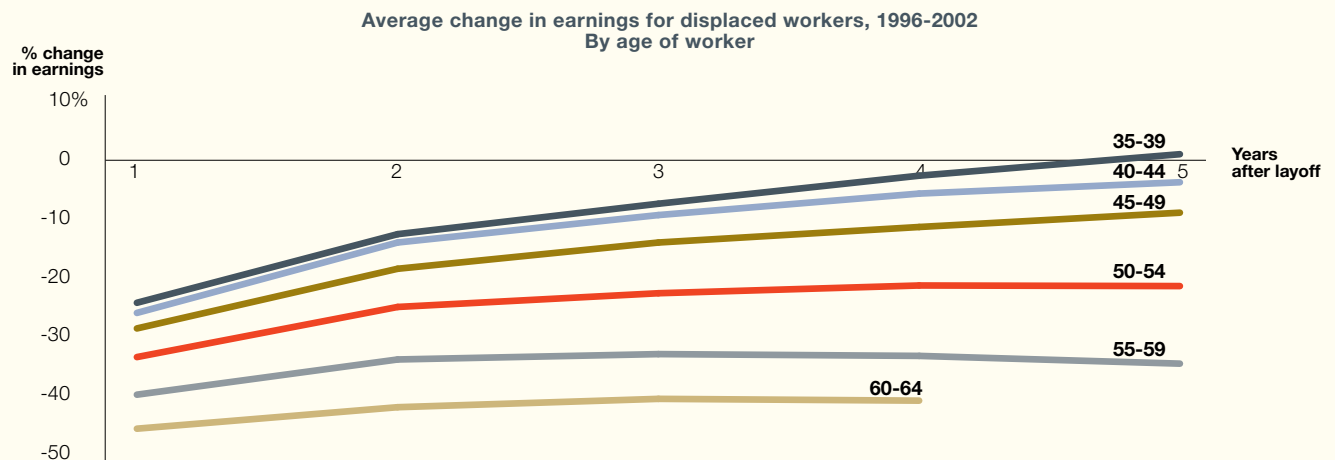
A recent study by University of Ottawa economists Ross Finnie and David Gray highlights the special challenges faced by older workers.^b The older the laid off worker, the greater is the subsequent earnings loss. Five years after a layoff, workers aged 35 to 39 who were still working were earning more in constant dollars before their layoff. At the other extreme, workers aged 60 to 64 realized earnings losses of more than 40 percent (*Exhibit B*).

Unfortunately, there is no proven plan to help these displaced workers. Retraining is the panacea most often promoted. But definitive positive results are hard to come by.

One of the most extensive studies on retraining was conducted in 2008 for the US Department of Labor.^c It indicated that retraining laid-off workers has limited success at best. The study tracked the experience of 160,000 laid-off workers in twelve states from 2003 to 2005, a period of economic expansion. It compared the results for who had participated in formal training with those who had not and found very little difference in earnings three and four years later. It concluded that the “ultimate gains from participation [in formal training programs] are small or non-existent.”

A study conducted by the Canadian Auto Workers, Chrysler Canada, and the Ontario Government assessed the experiences of laid-off auto workers moving through the adjustment process at CAW Action Centres, first point of contact for workers seeking retraining. Despite high interest and involvement among the laid-off workers, results were disappointing. Only a quarter of the participants in the study sample found jobs and most of these were part time or low paid, with fewer benefits than the old jobs and with greater employment insecurity.^d

Exhibit B Older workers are most severely affected by layoffs



Source: Ross Finnie and David Gray, “Labour-Force Participation of Older Displaced Workers in Canada,” IRPP Study, No. 15, February 2011, Table 5.

^a René Morissette, Xuelin Zhang, and Marc Frenette, “Earnings Losses of Displaced Workers: Canadian Evidence from a Large Administrative Database on Firm Closures and Mass Layoffs,” Statistics Canada, January 2007.

^b Ross Finnie and David Gray, *Labour-Force Participation of Older Displaced Workers in Canada*, IRPP Study, No. 15, February 2011.

^c “Workforce Investment Act Non-Experimental Net Impact Evaluation,” IMPAQ International, December 2008, available online: http://wdr.doleta.gov/research/FullText_Documents/Workforce%20Investment%20Act%20Non-Experimental%20Net%20Impact%20Evaluation%20-%20Final%20Report.pdf

^d Sam Vrankulj, “CAW Worker Adjustment Tracking Project: Preliminary Findings,” First Round Report, June 2010, available online: http://www.caw.ca/assets/pdf/Tracking_Study.pdf

Some studies show positive returns for retraining displaced workers. Research conducted for the Federal Reserve Bank of Chicago indicated that under some conditions, formal retraining can pay off.⁶ The research, drawn on data from the State of Washington, concluded that the equivalent of a year of community college raises the long-term earnings of displaced workers by about 9 percent for men and 13 percent for women. Returns varied significantly and were higher if the courses were “quantitative” (e.g., technical trades, health related, and science) and near zero if the courses were “non-quantitative” (e.g., basic skills, sales and service, social sciences).

A study released recently by Statistics Canada also shows positive benefits from formal training of younger (aged 25 to 44) displaced workers. Marc Frenette, Richard Upward, and Peter Wright analyzed impact of retraining in post-secondary institutions for displaced workers in Canada, using the Longitudinal Worker File (LWF). The wage results over a period of five years preceding and nine years following job loss, indicated that workers who attended post secondary education shortly following displacement (in the next calendar year) saw their earnings increase by almost \$7,000 more than displaced workers who did not.⁷ The impact, however, for men between 35 and 44 was non-existent. The authors noted that only a small percentage of displaced workers actually participated in post secondary retraining – and acknowledged that characteristics of the workers who choose this formal retraining may be the cause of the increased earnings.

Given the high cost of retraining programs and the paucity of research findings on the benefit of this spending, we ought to review carefully the results of such efforts.

Wage insurance could be a useful approach to supplement existing programs for workers transitioning to lower paid work. It could help ease the transition that some workers face in our rapidly changing economy – particularly older workers with less transportable skills. At the same time, it motivates unemployed workers to find a new job; in fact, by reducing the sting of lower wages, it encourages them to consider jobs in other sectors where their current skills are not as valuable. In a sense, it subsidizes employers to hire and re-train these workers on the job. Wage insurance can also assist older workers to remain in the labour force rather than retire early because of poor job prospects at a wage equal to what they earned before being laid off.

Wage insurance, as presented by its proponents, could work as follows. It would be targeted at workers who have been in a job for a period of, say, ten years. In fact, while benefits could be available to all workers, wage loss is a much less significant problem for workers who have been in the same job for less time, partly because they are younger.

When these workers are re-employed at a lower wage rate, wage insurance benefits would cover half the earnings difference for a period of two years. The benefit would be capped at \$10,000 annually to ensure targeting at lower- and middle-income earners. The coverage rate, the coverage period, and the benefit cap could be adjusted up or down.

Some problems could undermine the effectiveness of the program. Higher earnings replacement rates would lower the incentive for a worker to secure a higher paying job and to invest in retraining while in the new job. The same challenge exists for the length of coverage. Program costs could also be an issue, but US calculations of a wage insurance program as outlined above indicate a \$3.5 billion annual cost, equal to an annual premium of \$25 per worker.

Although the concept of wage insurance is promising, one experiment conducted in 1995–96 by the federal government’s Social Research and Demonstration Corporation yielded disappointing results. The experiment focused on workers who had lost their job after at least five years of continuous employment. Participants who chose to leave Employment Insurance for full-time work within a specified period of time received 75 percent of the difference between earning in their previous job and their new job, up to a weekly maximum of \$250 for up to two years. Among eligible displaced workers, interest was high. However, the program produced only a modest increase in full-time employment and, after fifteen months, earnings for participants were about 5 percent lower than for those who chose not to join the program.⁹

It is possible that better results could come from a redesign of the experiment – different qualifying time periods, richer benefits, and a focus on situations with older, less skilled workers, for example. There is still much work to be done in assessing the costs and benefits of wage insurance. We would be wise to study the program further.

⁶ Louis Jacobson, Robert LaLonde, and Daniel G. Sullivan, “Estimating the Returns to Community College Schooling for Displaced Workers,” Working Paper 2002-31, Federal Reserve Bank of Chicago, December 2002.

⁷ Marc Frenette, Richard Upward, and Peter W. Wright, “The Long-term Earnings Impact of Post-secondary Education Following Job Loss,” Statistics Canada, March 2011.

⁹ Howard Bloom, Saul Schwartz, Susanna Lui-Gurr, Suk-Won Lee with Jason Pend and Wendy Bancroft “Testing a Re-employment Incentive for Displaced Workers: The Earnings Supplement Project,” Social Research and Demonstration Corporation, May 1999.