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Conference Paper

Providing portable unemployment insurance to overseas workers

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Providing Portable Unemployment Insurance to Overseas Workers

The Challenges

The recent global financial crisis had destructive consequences for the world's labor markets. Migrant laborers and overseas contract workers were at the forefront of massive retrenchments and, as a result, remittances fell sharply in some of the world most remittance-dependent economies.

Large waves of returnees were reported, while other unemployed migrant workers stayed on in their host countries, competing for scarce jobs, and likely fueling social tensions in the process. Unfortunately, the majority of overseas workers fall outside formal unemployment insurance systems.

In host countries around the world, there are typically no mechanisms for guest workers to pay into an unemployment insurance system. Nor are migrant workers covered by unemployment insurance systems in their countries of origin. At the same time, a large fraction of migrant workers are undocumented workers and would not be covered by any social insurance system in the first place. Some unemployed workers with adequate savings may have fared well, but for most workers, the consequences of the crisis have likely been borne fully by them and by their households.

In the post-crisis environment, host countries and countries of origin have an opportunity to consider how best to provide safety nets for their overseas workers. As the global economy recovers, unemployed migrant workers will likely find new jobs and those who returned to their home countries will likely be redeployed. How should a portable unemployment insurance system be established? Are there political economy constraints that need to be addressed? Should such a system be negotiated bilaterally or in a multilateral setting? Should it be managed by the private sector or the public sector? What are the design features of such a system? An appropriate unemployment insurance system would be an important step toward offsetting the devastating impact of the next economic downturn—whether local or global in scope—among overseas workers and their families.

Proposed Solutions

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Background Discussion

A number of European nations face a “demographic disaster” due to declining fertility. Might migration solve Europe’s population problem? Countries like Germany need both people and skills:

Germany’s labor market is already facing skill shortages, which will intensify from 2010 when the postwar baby boomers enter retirement. When that happens, virtually all measures of economic dynamism, from gross domestic product per head to labor productivity, will plummet. As the working population shrinks and the number of pensioners rises, its welfare state, which dishes out €700bn a year in benefits to the elderly, the sick and the unemployed, will come under huge strain.

Free migration has been the subject of extensive theoretical investigation, dating back to Adam Smith (1776) who pointed out that curtailing free migration has a similar (and negative) effect to curtailing free flows of capital. In his words:

"Whatever obstructs the free circulation of labor from one employment to another, obstruct that of a stock likewise; the quantity of stock which can be employed in any branch of business depending very much upon that of the labor which can be employed in it.”

Nevertheless, whereas free capital mobility is widespread, free migration is very rare in practice.

About a century later, the Noble laureate, Milton Friedman, remarked that obviously one can not have free immigration and a welfare state. That is, a welfare state with open borders might turn into a heaven for the poor and needy from all over the world, thereby draining its finances, and bringing it down. This observation underscores the motivation for this book.

As a backdrop, in 10 of the European Union’s 27 member states deaths are expected to outnumber births in 2010. As of 2015 the EU as a whole is expected to experience negative natural population growth. The European Union has attracted 26 million migrants in the past two decades, but most of the European countries attempt to protect native-born labor by shutting out foreign workers, which results in massive inflow of illegal immigrants. That is, Europe generous social benefits encouraged a massive surge of “welfare migration.” Consequently, Europe has ended up with 85% of all unskilled migrants to developed countries, but only 5% of the highly skilled migrants.

As a consequence, public opinion in the developed economies, with their fairly generous welfare system, favors putting, in some way or another, restrictions on migration.

A skilled and young migrant may help the finances of the welfare state; whereas an unskilled and old migrant may inflict a burden on the welfare state. Of a particular interest is therefore the skill and age composition of these restrictive policies. A welfare state, with a heterogeneous (by age, skill, etc.) population, typically does not have a commonly accepted attitude towards migration.

For instance, a skilled (rich) and young native-born who expects to bear more than an average share of the cost of providing the benefits of the welfare state is likely to oppose admitting unskilled migrants on such grounds. On the other hand, the same native born may favor unskilled migrants to the extent that a larger supply of unskilled workers boosts skilled-workers wages. The native born old may favor migration, even low-skilled, on the ground that it could help finance her old-age benefits. Chiswick and Hatton (2003) provide some figures describing the shift from uncontrolled migration in the pre-WWI to selective policies afterward. Despite the dramatic decline in the cost of relocation to the migrants, rates of migration went down. For instance, the annual immigration rate to the USA fell from 11.6 immigrants per thousand population in the first decade of the 20th century to 0.4 per thousand population in the 1940s, rising to 4.0 per thousand population in the 1990s. The post WWII immigration rates are substantial bellow the pre-WWI rate.

Indeed, Canada decided to keep its borders open and even to speed up acceptance procedures for some highly skilled arrivals. While migrants have lost some ground recently, they are still twice as likely as native Canadians to hold doctorates or master's degrees. Sweden was not satisfied with merely implementing a new, skills-based immigration policy; it actually upgraded its integration efforts, including language and vocational training for existing immigrants, right in the middle of the financial crisis.

The variety of effects of migration necessitates the use of a general equilibrium framework in order to study how migration policies affect the native-born voters. Furthermore, there are conflicting interests among the native-born voters concerning these policies. This book develops a framework to study how these many conflicts are resolved in a politico-economic setup.

The political economy set up features two aspects in policy formation: skilled (rich) vs. unskilled (poor), and young vs. old. Thus, the analysis consists of policies which resolve both the intra and inter-generation conflicts.

Fiscal aspects of migration: Evidence

The European Union, both the "old" (EU-15) and the "new" (after the enlargement to EU-27), faces a severe aging problem. For instance, the ratio of the elderly population (aged 60 years and over) to the working age population (aged 15–59 years) in the EU-15 is projected to at least double from about 20% in the year 2000 to over 40%, in the year 2050. Official retirement ages have failed to keep up with life expectancy, making pensions and health care provisions increasingly unaffordable. "Many people in the rich-world OECD countries retire relatively early, which let them enjoy, on average, some 19 years in retirement before death." (The Economist, February 2nd, 2010). Years in retirement in Italy, Austria and France are 23, 24 and 25, respectively. The aging process shakes the financial soundness of the welfare state, especially its old-age security and medical health components, because there are fewer workers asked to support increasing numbers of retirees. As put metaphorically by the Economist (March 15th, 2003, 80): "…the fiscal burden on the diminishing number of worker-bees will rise as more people turn into pensioner drones." The Economist (24th August, 2002) also looks at some of the dimensions of the financial burden: "On some estimates, by 2050, government debt could be equivalent to almost 100% of national income in America, 150% in the EU as a whole [EU-15] and over 250% in Germany and France." Nevertheless, note that migration of young workers (as distinct from old ones), even when driven by the generosity of the welfare state, slows down the trend of increasing dependency ratio. However, economic intuition suggests that even though unskilled migration improves the dependency ratio, it nevertheless burdens the welfare state. This is because low-skill migrants are typically net beneficiaries of the generosity of the welfare state. In 1997 the US National Research Council sponsored a study on the overall fiscal impact of immigration into the US (see Edmonston and Smith 1997). The study looks comprehensibly at all layers of government (federal, state, and local), all programs (benefits), and all types of taxes. For each cohort, defined by age of arrival to the US, the benefits (cash or in kind) received by migrants over their own lifetimes and the lifetimes of their first-generation descendents were projected. These benefits include Medicare, Medicaid, Supplementary Security Income (SSI), Aid for Families with Dependent Children (AFDC), food stamps, Old Age, Survivors, and Disability Insurance (OASDI), etc. Similarly, taxes paid directly by migrants and the incidence on migrants of other taxes (such as corporate taxes) were also projected for the lifetimes of the migrants and their first-generation descendents. Accordingly, the net fiscal burden was projected and discounted to the present. In this way, the net fiscal burden for each age cohort of migrants was calculated in present value terms. Within each age cohort, these calculations were disaggregated according to three educational levels: Less than high school education, high school education, and more than high school education. Indeed the findings suggest that migrants with less than high school education are typically a net fiscal burden that can reach as high as approximately US$100,000 in present value, when the migrants' age on arrival is between 20–30 years.

Following the recent enlargement of the European Union to 27 countries, there were concerns that the EU-15 was likely to face a rise in welfare migration. Hans-Werner Sinn (Financial Times, July 12th 2004) made a somewhat alarming prediction:

"There will be more migration in Europe, but it will be 'bad' migration as well as 'good.' 'Good' migration is driven by wage and productivity difference. 'Bad' migration is driven by generosity of the welfare state."

Indeed, only three members of the EU-15 (the UK, Sweden and Ireland) allowed free access for residents of the accession countries to their national labor markets, in the year of the first enlargement, 2004. The other members of the EU-15 took advantage of the clause that allows for restricted labor markets for a transitional period of up to seven years.

Focusing on the UK and the A8 countries

The A8 countries are the first eight accession countries (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Slovenia and Poland.), Dustmann et al . (2009) bring evidence of no welfare migration. The average age of the A8 migrants during the period 2004–2008 is 25.8 years, considerably lower than the native UK average age (38.7 years). More accurately, the said period extends from the second quarter of 2004 through the first quarter of 2009.

The A8 migrants are also better educated than the native-born. For instance, the percentage of those that left full-time education at the age of 21 years or later is 35.5 among the A8 migrants, compared to only 17.1 among the UK natives. Another indication that the migration is not predominantly driven by welfare motives is the higher employment rate of the A8 migrants (83.1%) relative to the UK natives (78.9%). Furthermore, for the same period, the contribution of the A8 migrants to government revenues far exceeded the government expenditures attributed to them. A recent study by Barbone et al (2009), based on the 2006 European Union Survey of Income and Living conditions, finds that migrants from the accession countries constitute only 1%–2% of the total population in the pre-enlargement EU countries (excluding Germany and Luxemburg); by comparison, about 6% of the population in the latter EU countries were born outside the enlarged EU. The small share of migrants from the accession countries is, of course, not surprising in view of the restrictions imposed on migration from the accession countries to the EU-15 before the enlargement and during the transition period after the enlargement. The study shows also that there is, as expected, a positive correlation between the net current taxes (that is, taxes paid less benefits received) of migrants from all source countries and their education level (see also Boeri, Hanson, and McCormick 2002).

Indeed, the general public perceives unskilled migrants as a drain on the public finances. In the UK, the Daily Mirror (24 July, 2006) puts it in bread and butter terms: "Economic migrants need schools for their children. They need housing .They need medical care. They can even lose their jobs."

Hanmeueller and Hiscox (2010), using survey data in the US, find two critical economic concerns that appear to generate anti-immigrant sentiments among voters: concerns about labor-market competition, and concerns about the fiscal burden on public services. Not unexpectedly, employing opinion surveys, Hanson et al (2007) bring evidence that in the US native residents of states which provide generous benefits to migrants also prefer to reduce the number of migrants. Furthermore, the opposition is stronger among higher income groups. Similarly, Hanson et al. (2009), again employing opinion surveys, find for the US that native-born residents of states with a high share of unskilled migrants, among the migrants population, prefer to restrict in migration; whereas native-born residents of states with a high share of skilled migrants among the migrant population are less likely to favor restricting migration (see also Mayda 2006). Indeed, developed economies do attempt to sort out immigrants by skills (see, for instance, Bhagwati and Gordon 2009). Australia and Canada employ a point system based on selected immigrants' characteristics. The US employs explicit preference for professional, technical and kindred immigrants under the so-called third-preference quota. Jasso and Rosenzweig (2009) find that both the Australian and American selection mechanisms are effective in sorting out the skilled migrants, and produce essentially similar outcomes despite of their different legal characteristics.

While Europe ended up in the last two decades with 85% of all unskilled migrants to developed countries, US retain its innovative edge by attracting 55% of the world educated migrants.

But there are also fears that low-skilled immigrants may add to that fiscal burden. The idea that immigrants are attracted to the welfare state because of its benefits, in the form of social security, education, etc., is well known. A generous welfare program serves as a magnet to foreigners (“welfare migration”).

Empirical evidence, addressing internal US migration, is inconclusive. Some support the welfare migration notion (Southwick 1981; Gramlich and Laren 1984; Blank 1988; Borjas 1999; Gelbach 2000; McKinnish 2005, 2007); others find no such evidence (Walker 1994; Levine and Zimmerman 1999).

International migration studies also exhibit mixed results. Pedersen at el. (2004) find that the tax-revenue-to-GDP ratio is negatively correlated with immigration flows from 129 countries of origin into 27 OECD countries. Peridy (2006), Leblang et al. (2007) and Warin and Svaton (2008) find positive effect of welfare-state benefits on immigration, from various countries into OECD countries. De Giorgi and Pellizzari (2006) examined the immigration into the EU from outside the EU, finding that immigrants are attracted to welfare, with no significant difference across skill levels. Docquier et al. (2006) explored immigration into OECD countries from 184 countries of origin. They find that low-skilled immigrants are motivated by welfare benefits much more than high-skilled immigrants. This indicates that even though the volume of immigrants increases with the generosity of the welfare state, their skill composition decreases.

None of these studies, however, distinguishes between the notion of “free migration” and “policy-controlled migration.” Making such distinction, arguably, could explain the mixed results in the literature.

Free migration means that all individuals can freely move into the host country, reside, work and retire there. The EU is an example of such regime. EU members, in general, are obligated (by international treaties) to enable free entrance to any individual originated in other EU country.

Policy-controlled migration is exercised between any pair of countries that are not obligated to free migration. Immigration quotas are such a policy. Another sort, which becomes increasingly popular, is quality-selection migration policy. The host country screens out less desirable immigrants. Immigrants with high skills and education are preferred over immigrants with low skills and education. Quality-selection immigration policy is well established in Australia, New Zealand and Canada. The US also adopted such rules in 1990, as have a growing number of EU countries, including France, Ireland and the UK (Docquier and Marfouk 2006).

Why is such a distinction of crucial importance? In the case of free migration, equilibrium reflects the preferences and constraints of migrants in source countries (the “supply-side”). In the case of policy-controlled migration the equilibrium reflects the attitudes of policymakers in the host country (the “demand-side”). In order to examine the effect of welfare on the skill composition of immigrants, one therefore must separate between the “demand-side” (or more accurately, the “policy-side”) and the “supply-side” effects, which are, in fact, operating in opposite directions. Failing to distinguish between these migration regimes may bias estimates of the effect of welfare state generosity on immigrants’ skill composition. The effect of the generosity of the welfare state on the skill composition of migrants depends crucially on the policy regime, namely whether migration is free or restricted. Chapter 2 first builds a parsimonious (static) model to analytically study how different is the effect of the generosity of the welfare state on the skill composition of the immigrants across these policy regimes. In a free-migration regime, a typical welfare state with relatively abundant capital and high total factor productivity (implying relatively high wages for all skill levels) attracts unskilled and skilled migrants. Furthermore, the generosity of the welfare state attracts unskilled (poor) migrants, as they expect to gain more from the benefits of the welfare state than what they expect to pay in taxes for these benefits; that is, they are net beneficiaries of the generous welfare state. In contrast, potential skilled (rich) migrants are deterred by the generosity of the welfare state.

Thus, the latter tilts the skill composition of the migrants towards the unskilled. In the restricted migration regime, these same considerations lead voters to open the door wide to skilled migration and slam the door shut on unskilled migration. Voters are motivated by two considerations: how migration affects their wages, and how it bears on the finances of the welfare state. Typically, unskilled migration depresses the unskilled wage and boosts up the skilled wage. The opposite occurs with skilled migration. The effect of migration on the finances of the welfare state is common to all voters of all skills, because skilled migrants are net contributors to the welfare state, whereas unskilled migrants are net beneficiaries. From a public finance point of view, native-born voters of all skills would therefore opt for the formers to come in and for the latter to stay out.

The EU-15 can serve as a laboratory for studying empirically the policy-regime differential effect of the generosity of the welfare sate on the skill composition of migration. Freedom of movement and the ability to reside and work anywhere within the EU are one of the fundamental rights to which member states of the EU are obligated towards each other. In contrast, labor mobility into the EU-15 member states, from non-EU-15 states, is still restricted to various degrees by national policies. Cohen and Razin (2008) utilizes this difference in policy regimes across EU-15 and non-EU-15 states in order to test the predictions of the model about key differences between free and policy-restricted migration concerning the effect of the welfare state on the skill composition of immigrants.

The identification strategy is to use the decomposition the source-host country pairs into two groups: One group, a “free-migration” group, consists of source-host country pairs within the EU; and another group, “policy-controlled migration” group, consists the pairs from non-EU countries into the EU. We find evidence in support of the predictions of the parsimonious model that the generosity of the welfare state adversely affects the skill-composition of migrants under free-migration; but it exerts a more positive effect under a policy-controlled migration regime relative to a free-migration regime.

Carlos C. Salinas

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The topic presented for discussion opens up an interesting exchange on whether or not there is a need to establish safety nets as part of the career roadmaps of migrant workers.

And if there is indeed a need for this, what comes to the forefront is:

1. Who should provide for the safety net; and
2. How much should be provided for.

Background

A unique element of migrant work is the allure of financially rewarding jobs in a remote location (host country) relative to the conditions present in their current location (home country). For professionals to take the significant step of moving offshore, the economic benefits should be substantial in order to warrant the risks, hardships and sacrifices that this career move will likely cause the individual and his or her family. Financial rewards that would bring about a better quality of life for the individual's immediate and extended family back home—housing, education, livelihood, higher professional attainment and greater disposable income.

For land-based Filipino overseas workers, these overseas opportunities require at least a 2-year commitment per contract, where the earnings from the first six months or so are channeled to cover the costs incurred to get the job in the first instance. Thereafter, future earnings are then projected as savings toward their individual needs, as listed above.

In the sector of Filipino seafarers, the industry I have been involved in for some 50 years now, almost from day 1 of their deployment, just about all their earnings can be earmarked towards their desired goals and objectives. This is so because by law, seafarers do not shoulder any cost for their deployment (other than their individual licenses). And while on contract, they incur neither living nor travel expenses to and from home, and are in fact, amply covered by both health insurance and disability or death insurance. Such insurance benefits immediately go to the individual's beneficiaries.

It is noteworthy that from the Philippine perspective, both overseas land-based and seafaring Filipino workers are not taxed on their income and as such, enjoy added financial gains.

Who should provide?

1. The migrant worker

Given this background, it would seem appropriate to me, that a first solution to the matter of providing unemployment insurance rests initially on the migrant worker. The notion here is that through proper education and exposure, the migrant worker should consider adopting a "forced" savings program that will cover for his needs if their continued employment overseas is curtailed.

2. The home country

As a complementary support to the individual's effort to provide for himself, as was suggested by Ms. Sto. Tomas, the government of the home country, in this case, the Philippines, can also set aside a portion of the fees it earns from the Philippine Overseas Employment Administration and from the Overseas Workers Welfare Administration towards a "fund" that can serve to cover "emergency dislocation" expenses and possibly some related expenses towards re-immersion into the home country for a limited period of time following repatriation. The basis for this scenario is that the Philippine government enjoys certain benefits from Filipino overseas work:

(a) By promoting overseas work, unemployment pressure on the home front as well as the associated domestic social tension that this brings about, are somewhat alleviated.

(b) Overseas workers remit a considerable amount of foreign exchange to the Philippines. Our 9 million or so overseas professionals account for anywhere between 25%–30% of total dollar inflows into our country. This is a significant boost to our gross international reserves resulting in a very stable currency.

Therefore, a case can be made for the government to consider such a safety net for a sector of its citizenry that has actively contributed to overall national development through their foreign exchange remittances.

3. The host country

A third source of potential assistance towards some form of unemployment insurance can be targeted towards the host country. The host country stands to benefit from gaining service workers who assume jobs that other host nationals may no longer care to take on. In the event that these workers are laid off, rather than availing of a host country's "safety nets," it may be less costly for the host country to repatriate such temporary workers and offer them a "displacement" allowance to return to their own country, until such time that the host country is back on a path of economic growth which in turn will usher the next wave of temporary workers.

4. The host country employer

A fourth source of potential assistance might be the sponsoring employer in the host country. However, in the event of a downturn in the host employer's financial position that would result in the loss of employment of migrant or temporary workers, he ability to incur additional costs for unemployment insurance would seem highly unlikely. Nevertheless it is mentioned here as a possible fourth source.

The shipping/seafaring sector

Allow me to comment on these suggestions from the perspective of the shipping industry. For one, this industry is steeped in international agreements and conventions and thus, is well-regulated in matters of safety and the environment, and policies on social protection and benefits to employees.

It is an industry that falls under the purview of several multilateral agencies of the United Nations: the International Maritime Organization for safety concerns, and the International Labor Organization for matters of employment.

An industry that is also highly structured in terms of tripartite working arrangements among government, labor and the private sector.

An industry with a finite number of employers and very similar working conditions which are stringently defined.

An industry where there is no "host government" that gains the benefit of the services of such temporary workers. Seafarers are highly mobile—their work place being on board a moving vessel.

Comparatively speaking, and because of its structure, this industry is perhaps furthest along in terms of policies of recruitment, and more importantly retention. In fact, it is because of the active need to retain its crew (they largely being short-term contractual workers with tours of duty lasting from a couple of months to 9 months in total) that the concept of social benefits has taken on higher dimensions within the shipping sector.

While ship owners may incorporate into their retention strategies the concept of unemployment insurance for seafarers on top of the other social benefits they already provide, the Filipino seafarer is already presently equipped to protect himself, given the financial and other benefits of a seafaring career, against unforeseen unemployment.

How much to cover?

From what we gather, the USA has established a program of providing unemployment benefits for forced work loss which runs to a maximum of 6 months covering almost 40% on the average of basic monthly wage. So perhaps this can serve as a base or starting point for an individual to consider starting a "savings program" for themselves.

If in addition to this and as I have suggested earlier—where both home and host governments can be asked to "participate," short of this being mandated—that would then be the ideal scenario.

Patricia Sto. Tomas

Chairperson of the Board of Directors, Development Bank of the Philippines

Does a reverse tax on government equivalent to 1/10 of 1% of annual workers' remittance put this in the national social security system and use it as a start up fund for unemployment insurance for overseas workers? Overseas Filipino workers (OFWS) work overseas but send their money home and spend it there for education, housing and others. These are jobs that have been created without government help. When the workers' contract expires, unemployment insurance should help them transition into a local job or business venture. Government owes them that.

Erwin R. Tiongson

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1. One option is to offer unemployment benefits in multiple tranches: The first tranche is received in the host country while the second and subsequent tranches are received in the country of origin, subject to the usual eligibility requirements. The implementation and monitoring of the system require the collaborative efforts of both home and host country governments. This structure potentially helps reduce labor market pressures in the host country during a downturn and encourages the movement of workers back to their countries of origin. Spain offered something similar in the middle of the global financial crisis. Eligible migrant workers could elect to receive 40% of benefits in Spain and 60% of benefits in their country of origin, if they agreed to move out of Spain for at least three years. (In contrast, in systems such as Korea's, unemployment benefits are not conditional on return to home country.) It seems that few applied for the "return bonus" for fear of being subsequently denied entry into Spain—i.e., applicants were asked to give up their work and residence cards—even three years after. The challenge then is to reduce uncertainties in the treatment of migrant workers, at the end of the jobless spell.
2. Another option is to introduce Unemployment Insurance Savings Accounts (UISAs). This system—a self-insurance system that facilitates the portability of benefits across sectors and occupations, within countries, and across countries—requires each worker to save a portion of earnings in a savings account. As currently implemented across countries, UISAs vary in its design features: Withdrawals can be severely restricted (and subject to maintaining a positive balance) or some borrowing can be allowed. The system is thought to dampen moral hazard while promoting work incentives. It can also be privately managed.
3. One modification to UISA would be to structure the system in a way that mixes social insurance and self-insurance, such as in the case of Chile (which is a domestic UISA but can be a model for a globally portable system). In Chile's system, there is an individual account and a common or pooled account, which is in part financed by government. Withdrawal from the common fund is conditional on funds in the individual account being insufficient and subject to usual eligibility requirements of an unemployment insurance system.
4. One alternative is not an insurance system but a temporary loan facility made available to jobless migrant workers, conditional on previous contributions to a social security fund. They could also be funded out of mandatory contributions from workers just prior to deployment, as in the case of a Philippine migrant welfare fund (which, as currently implemented, is used for various contingencies, and not necessarily unemployment spells).