

Reforming Employment Insurance: Transcending the Politics of the Status Quo

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Les changements apportés au programme d'assurance-chômage pendant les années 90 ont résulté en une réduction du programme de même qu'à des changements significatifs dans l'importance relative de ses objectifs. La réforme de l'assurance-emploi de 1994-1996, en introduisant des changements structurels via une stratégie incrémentelle, illustre la relative autonomie du gouvernement fédéral et de Développement des ressources humaines Canada face aux intérêts sociaux de même que les limites à cette autonomie imposées par les intérêts régionaux et la dynamique des relations entre le fédéral et les provinces. La compétition interne au sein de la bureaucratie fédérale, du Cabinet et du caucus a joué un rôle plus significatif dans la formation de la réforme de l'assurance-emploi que les intérêts externes.

Incremental changes to the Unemployment Insurance program during the 1990s have resulted in a substantial retrenchment of the program, along with significant changes in the balancing of its objectives. The EI reforms of 1994-96 in introducing structural change through a strategy of purposeful incrementalism illustrate both the relative autonomy of the federal government and Human Resources Development Canada from major societal interests and the limits on that autonomy imposed by regional interests and the dynamics of federal-provincial relations. Internal competition within the federal bureaucracy, Cabinet, and caucus played a more significant role in shaping the EI reform agenda than external interests.

The restructuring of major social security programs is one of the most daunting tasks facing a democratic government challenged by the need for fiscal retrenchment or a reallocation of resources in response to changing social conditions. This challenge is even more daunting when it involves a rethinking of the basic objectives of such programs or reductions in existing benefit entitlements.

The 1994-96 reforms to Canada's Unemployment Insurance (UI) — now Employment Insurance —

system are an example of structural change to one of Canada's largest entitlement programs. In this article, I review the factors that led to the political entrenchment of UI as an often disjointed mixture of social insurance, income maintenance, and social adjustment programs and the constraints faced by the federal government in rationalizing these policy goals and instruments. It examines the Employment Insurance reforms of the mid-1990s as a response to the growing challenges of structural unemployment and structural economic change,

summarizes the incremental efforts of successive federal ministers of employment (now ministers of human resources development) to modify the existing system within these constraints, and the UI reform debate which culminated in Bills C-111 and C-12, the 1995-96 package of amendments to the *Unemployment Insurance Act*.

UNEMPLOYMENT INSURANCE AND THE PROBLEM OF WELFARE STATE REFORM

The problem of structural reform to major social policies such as Unemployment Insurance can be approached at several levels. These include the entrenchment of entitlements through the logic of collective action, bureaucratic politics, institutional competition, and the federal imperative (in Canada) of regional redistribution.

While the federal government has formal constitutional responsibility for Unemployment Insurance, it faces a wide range of informal constraints on its ability to introduce major changes to the program. Some of these have been described by Courchene (1994), Pierson (1994), and others who have studied the efforts of governments around the world to restructure major elements of the welfare state in ways that amount to a retrenchment or systematic reallocation of benefits.

Many of these benefits are widely considered as entitlements of citizenship, a form of civic property rights (Bell 1974; Macpherson 1978, p. 8; Deaton 1988, p. 9). They are energetically defended by the societal interests which are their beneficiaries, and often, by government agencies that administer them. The proliferation of program objectives lends itself to a complexity in the rules and operations of these programs which effectively reduces accountability to a broader public, assisting entrenched policy communities of stakeholders to fend off political or budgetary challenges to the status quo (See Courchene 1994; Olson 1982; Pal 1988; Lowi 1985; Pierson 1994). Policy trade-offs embodied in pro-

gram design and incremental policy changes become entrenched. This, in turn, limits the capacity of governments to adapt program goals and rules to changing societal and economic conditions.

All of these factors are reflected in the immensely strong political attachment of voters and advocacy groups in Atlantic Canada and large parts of Quebec to the large-scale income transfers under the Unemployment Insurance program which had become a mainstay of their regional economies since the early 1970s. The successful efforts of regional advocates to maximize UI's income maintenance functions for seasonal workers and repeat beneficiaries in these areas to a far greater extent than for the unemployed in other parts of Canada — despite the best efforts of government officials to modify UI rules to reduce work disincentives and promote labour force mobility — helped increase the complexity of the program and the difficulty of introducing widespread changes without major effects on regional economies. As a result, any discussion about Unemployment Insurance reform rapidly becomes focused on its regional implications, especially in Atlantic Canada, and the need to develop strategies to mitigate or compensate for the regional effects of proposed changes.

Regional Redistribution

Unemployment Insurance was the single largest direct federal transfer program to individuals in the five provinces east of the Ottawa River, especially in Atlantic Canada (May and Hollett 1994, pp. 163-66), and a linchpin in the Canadian system of distributive federalism, the redistribution of income and wealth from more prosperous to less prosperous regions. Table 1 outlines the extent of UI-related interregional transfers in 1994.

Regional resistance to change has been reinforced by a political culture that continues to emphasize the distributive role of governments and specifically of political parties and elected officials in securing benefits for their supporters and constituencies. The pervasive impact of this culture can be seen in the

TABLE 1
Unemployment Insurance Benefits and Premiums, by Province, 1994

	<i>Benefits</i>	<i>Premiums</i>	<i>Benefits/Premiums</i>
	<i>in \$ millions</i>		
<i>Atlantic Provinces</i>			
Newfoundland	803	272	2.95
Prince Edward Island	192	67	2.87
Nova Scotia	796	534	1.49
New Brunswick	830	426	1.95
Total	2,621	1,299	2.02
Quebec	4,879	4,574	1.07
Ontario	4,515	7,849	0.58
<i>Western Provinces and the Territories</i>			
Manitoba	425	682	0.62
Saskatchewan	329	530	0.62
Alberta	1,159	1,916	0.60
British Columbia and the Northwest Territories	1,863	2,416	0.77
Total	3,776	5,544	0.62

Source: Human Resources Development Canada (1996a)

success with which members of Parliament from regions of relatively high unemployment have repeatedly mobilized to frustrate or contain federal attempts to reduce or reallocate UI spending, especially its regional components.

The regional dimension of UI reform is further aggravated by the Quebec dimension — both in the traditional role of government MPs from that province fighting to preserve regional privileges conferred by the program, and in the ongoing contest between the federal and nationalist or separatist Quebec governments for the hearts and minds of voters in that province. Taken together, these groups accounted for 40 to 70 percent of the government caucus from the early 1970s to the early 1990s. The role of the “UI caucus” and its capacity to constrain proposed changes to the UI system are addressed in greater detail later below.

The economic dependence of Atlantic Canada, especially its rural areas and their largely seasonal, resource-dependent economies, is even greater. UI claimants accounted for 24 to 37 percent of provincial labour forces in the four Atlantic provinces and 18 percent in Quebec in the post-recession year of 1994, compared with 10 to 13 percent in the five provinces west of the Ottawa River (Human Resources Development Canada 1996a). UI dependence in rural Atlantic Canada is even greater; 50 to 80 percent of families living outside major cities received UI benefits in the recession year of 1992 (Table 2).

This creates a strong attachment to existing forms of UI program delivery, based on the not unreasonable expectation that other forms of government economic development assistance offered in its place may prove either temporary or largely illusory.

TABLE 2

Levels of Unemployment Insurance Dependence in Atlantic Canada, by Province, 1992 and 1994

	<i>UI Families / Census Families: 1992</i>		<i>UI Claimants / Labour Force:1994</i>
	<i>Total</i>	<i>Rural</i>	
Atlantic Region	46.1%	59.2%	29%
Newfoundland	61.7%	80.1%	36%
New Brunswick	41.4%	52.7%	30%
Nova Scotia	39.0%	50.3%	24%
Prince Edward Island	N/A	N/A	37%

Sources: May and Hollett (1994), Tables 4, A1-3, B1-4; Human Resources Development Canada (1996a), A3, pp. 1-7.

Federal-Provincial Relations

The informal integration of the federal UI system, federal and provincial training programs and provincial welfare programs makes provincial governments significant, if indirect, players in any discussion of UI reform.¹ Regional business elites and public service unions have a vested interest in the status quo — whether as an implicit employment subsidy for many firms in seasonal industries² or an interregional transfer of income and wealth capable of sustaining higher levels of private consumption, business activity, public services, and public sector employment than would otherwise be sustainable especially outside major urban areas.

The result has been an asymmetrical, *deux nations* approach to unemployment and labour force adjustment programs in which Ottawa seeks to prop up an increasingly economically and socially dysfunctional system east of the Ottawa River. As a result, the government's ability to introduce significant changes to the UI system which reallocate or reduce benefits must take into account — and to some extent compensate for — these regional variations.

The system of variable entrance requirements introduced in 1977, combined with a series of incremental changes over the following two decades,

has reversed the significant work disincentives resulting from the 1971 Mackasey reforms to the Unemployment Insurance system in Ontario and Western Canada to the levels of the mid-1950s, while diluting their effect somewhat in the rest of the country (Table 3).

As a matter of practical politics, it is far easier for the federal government to pursue incremental changes to the UI system in areas within its exclusive jurisdiction than to negotiate a sweeping reallocation of powers and responsibilities in the UI-Welfare-Training subsystem with the provinces. The economic and fiscal challenges of the late 1980s and early 1990s made it inevitable that, despite these obstacles, successive governments would continue to do just that.

Purposeful Incrementalism: Introducing Structural Change on the Installment Plan

The persistence of high structural and seasonal unemployment in Atlantic Canada and large parts of Quebec helped defenders of the EI status quo to sidetrack proposals for fundamental structural changes to the EI system such as those proposed by the Forget Commission in 1986, to defer and dilute federal efforts to introduce more stringent qualifying rules during the late 1980s and early 1990s, and to derail

TABLE 3
Distribution of Unemployment Insurance Induced Disincentives by Region, (Canada, 1970 = 100)

	1972 Reforms	June 1995	UI Recipients (as percent of unemployed)
Newfoundland	263	145	90
<i>Maritime Provinces</i>	230		
Prince Edward Island		153	110
Nova Scotia		119	85
New Brunswick		115	121
Quebec	239	117	64
Ontario	202	89	43
<i>Western Provinces</i>	202		
Manitoba		84	48
Saskatchewan		86	54
Alberta		84	51
British Columbia		87	61

Source: Sargent 1995, pp. 40-41.

proposals for a “two-tier benefit system” for occasional and repeat users of the UI system advocated by business groups — an idea floated in conjunction with Human Resources Development Minister Lloyd Axworthy’s social policy reforms in 1994-95.

These events made it clear that root-and-branch changes to the UI system, such as those suggested by a series of economists, royal commissions, and business groups, were not politically sustainable. However, concerns over the effects of structural economic change on unemployment, along with sustained fiscal pressures and growing trends toward the targeting of social spending, persuaded a series of employment ministers and their senior officials of the need to shift a significant share of program spending away from its post-1971 emphasis on passive income support toward a more activist strategy of helping employers and workers adapt to structural changes affecting the entire labour market and economy.

As a result, successive governments introduced a series of progressive, incremental changes over ten years, culminating in the EI reforms of 1994-96. These changes have been aimed at reducing long-term dependence on UI as a regular, structural source of income for entire regions of the country, while restoring it to a transitional source of income capable of assisting workers to achieve greater self-sufficiency within a market economy (Human Resources Development Canada; senior officials of HRD Canada and the Department of Finance). More recent initiatives have sought to increase the program’s emphasis on income redistribution, based on family income, to compensate for reductions both in levels of regional redistribution and overall program spending.

However, while this process of incremental policy change reflects ongoing efforts by the federal government to balance political, economic, and social

interests in the broader society, it also reflects an ongoing process of bureaucratic politics *within* the federal government. This process reflects intense interdepartmental competition for the control of policy agendas and available resources in translating ideas for policy innovation into sustainable changes to one of Canada's largest social programs.

UI REFORM AND THE LIMITS OF BUREAUCRATIC POLITICS

Leslie Pal has argued that Unemployment Insurance policies between the 1960s and the mid-1980s were largely the product of bureaucratic politics, subject to the constraints of federalism, in which government decisions were driven by the internal goals and needs (or "internal logic") of federal agencies and their officials, and by the exigencies of interdepartmental competition for fiscal resources (1988, pp. 99-101). While Pal's thesis continued to apply to some extent in the decade from 1986 and 1996, political and fiscal pressures for major structural change have changed the terms of the debate and the relative influence of policy actors in setting and enforcing policy priorities. This section assesses the case for departmental and state autonomy on UI policy making and the constraints imposed by bureaucratic politics and competing state elites on that autonomy.

The lead agency in the UI policy community is Human Resources Development (HRD) Canada, formerly the Department of Employment and Immigration (CEIC). Pal suggests that HRD and its predecessors have enjoyed a considerable degree of autonomy from societal interests — whether critics in business or labour organizations — in managing the operations of the system. CEIC/HRD's relative autonomy is exercised in the context of "intra-organizational logic" — the department's legislative mandate, the policy principles guiding its operation, and its technical expertise in balancing the program's multiple objectives and administrative complexity. He stresses that these forces are "distinct in origin, detail and sometimes direction from

pressures being exerted by outside (e.g. societal groups)" (*ibid.*, p. 101).

Pal attributes CEIC/HRD's ability to maintain its relative autonomy in managing UI policy and program operations to several factors. These include the UI system's complexity — its often bewildering mix of policy goals and operating rules — the department's specialized expertise in managing the program, and the inability of program critics since the mid-1970s to offer a politically and financially viable alternative to the existing system. A mid-ranking departmental official commented in an interview that despite extensive and ongoing consultations with business, labour, and other groups, "interest groups have minimal influence on the policy level. Ministers have their own agenda, and if interest groups' agendas coincide with theirs, so much the better." Pal suggests that the "internal logic" of HRD's policy goals must balance a number of competing interests and objectives. Three of its major elements are a strong emphasis on income maintenance, especially in regions of chronically high unemployment, assistance for labour market adjustment, and what Pal describes as the "actuarial ideology" of social insurance — a measurable relationship between benefit levels, costs, and conditions of eligibility that provides transitional (or periodic) income support for the unemployed in a fiscally responsible manner (Pal 1988, pp. 101, 134-35). The long-standing tension between the goals of income maintenance and "actuarial ideology" is at the heart of the political and policy debates surrounding UI reform.

At one level, the 1993 reorganization of the Ministries of Employment, Labour and the social assistance component of Health and Welfare into the single Ministry of Human Resources Development has contributed to a shift away from the traditional "actuarial ideology" in favour of a greater emphasis on needs-based income transfers more closely related to family income levels (HRD officials).

Pal also notes that CEIC/HRD's autonomy was (and is) limited within the context of internal

government decision-making processes by the reality of interdepartmental competition. If anything, this reality has intensified in recent years. During the late 1980s, CEIC/HRD's autonomy in the design and operation of the UI system was challenged by progressive budgetary constraints, culminating in the end of subsidies from general federal revenues in 1990 for social benefits delivered through the UI program such as those related to parental leave, supplemental regional benefits and employment training. These actions, combined with a sharp cut in premiums at the beginning of the 1990-91 recession, marked the end of the increasingly threadbare pretense that UI was run on an actuarially sound basis on behalf of the so-called premium partners, business and labour.

While HRD continued to exercise effective control over the UI policy agenda in the mid-1990s, its ability to manage the political and policy trade-offs among stakeholder groups was increasingly constrained by demands by the Department of Finance for additional reductions in direct UI spending as part of its deficit-reduction strategy. Finance also imposed a multi-year fiscal strategy that would make the UI/EI fund self-sustaining through a major recession, despite strenuous objections from both business and labour. In macro-policy terms, this meant a return to the insurance concept of setting aside premium revenues to meet *future* claims on statutory benefits, rather than financing cyclical premium shortfalls from general revenues.

However, the argument for state autonomy or the dominance of the bureaucratic politics model cannot be taken too far. Federal ministers of manpower, employment, and human resources development have been frustrated repeatedly in their efforts to introduce major changes to the UI system. The introduction of UI experience-rating for employers, as recommended by the Forget Commission in 1986, and the comprehensive realignment of federal-provincial social policy responsibilities within a regionalized two-tier system, as proposed in Lloyd Axworthy's Green Paper of December 1994, proved

to be totally beyond the political capacity of the federal government (Greenspon and Wilson-Smith 1996, pp. 147-48; 245-46; officials from Department of Finance, the Privy Council Office, and HRD).³

The department has been generally unsuccessful in introducing substantial changes to the system of variable entrance requirements, being forced to find new revenues instead through the reduction of UI earnings replacement rates⁴ and a series of incremental reductions in UI benefit entitlements within the existing framework of regional redistribution. One senior official, a veteran of most of HRD's legislative initiatives of the past decade, commented in an interview that "the idea of a bureaucratically driven process is subject to politics. Bureaucrats have a lot of good ideas, but ultimately, their role is to find a political strategy that will work."

However, CEIC/HRD's capacity for more-or-less autonomous action can be seen in the gradual extension since 1977 of UI program goals to reflect the increasing preoccupation of federal officials with labour market adjustment and training, the gradual loss of autonomy of the bipartite Canada Employment and Insurance Commission, which ostensibly represents employer and employee stakeholders in the management of the UI system, the marginalization of business and labour organizations in UI-related decisions, and CEIC/HRD's success in shifting the funding of many of its operations from general tax revenues to those supplied by employer and employee UI premiums in spite of consistent stakeholder objections.

Even so, HRD's priorities increasingly appear to have been set in response to fiscal priorities — described by one senior official interviewed as "the only framework in which hard political decisions can be made" — and not just in matters that touch upon the use of UI premium revenues or the department's capacity to access other government revenues for its employment and training programs. For example, the 1992 and 1994 UI changes, which removed eligibility for persons quitting their jobs and

increased the qualifying period for benefits, respectively, were announced by ministers of finance in their budget speeches.

Pal argues that the department has sought to preserve a general balance among different societal forces consistent with overall government policies while remaining impervious to the specific demands of major business and labour groups. This has been reflected since the mid-1980s in a process of incremental (though often contested) changes which has seen almost an annual process of amendment. These changes reflect five broad trends in the funding and operations of the Unemployment Insurance system (see Table 4):

- a gradual shift in the costs of non-insurance benefits to the employer-employee account (UI premiums) from general government revenues;
- the growing use of UI funding to support “active labour measures” including training and employment subsidies;
- the gradual expansion of other non-insurance related benefits — e.g., maternity, paternity, and adoptive parental leave, often under pressure from the federal courts;
- the gradual reduction of UI income replacement rates from 60 percent (1979-93) to 57 percent (1993-94) to 55 percent since 1994 for recipients without dependents *and* earnings of less than 50 percent of maximum insurable earnings along with a gradual reduction in benefit duration;
- greater restrictions on benefits for the “voluntarily unemployed” (quits and terminations for cause), with benefits deferred from 6 (1976-90) to 12 weeks (1990-93, combined with benefit reduction from 60 to 50 percent of earnings), and finally eliminated in 1993.

Labour critics of these trends tend to argue that progressive restrictions on UI benefits, the government’s toleration of mass unemployment, and its advocacy of more flexibility in labour markets amount to a pro-business bias both in program operations and the general drift of government economic policy (McBride 1992; Cameron and Browne 1994; Jackson 1995; Rau 1997). However, these claims ignore consistent business objections to steady increases in total program costs (until 1994), the withdrawal of government funding for “non-insurance related objectives” built into the UI

TABLE 4
Distribution of Total Unemployment Insurance Benefits, by Category of Benefit, 1973-1995

<i>Category of Benefit</i>	<i>1973</i>	<i>1975</i>	<i>1980</i>	<i>1985</i>	<i>1990</i>	<i>1992</i>	<i>1995</i>
	<i>percent</i>						
Regular	92.3	92.4	85.3	87.8	85.6	79.8	71.9
Training	0.0	0.3	3.6	2.3	2.5	8.3	10.9
Other active labour	0.0	0.0	0.0	1.5	1.3	1.3	3.3
Fishing	1.0	0.8	1.9	1.8	2.0	1.5	1.7
Parental, adoption	3.3	3.2	5.3	4.3	5.5	6.9	9.2
Sickness	4.0	3.5	3.5	2.2	3.0	2.3	3.2
Total Benefits (\$ millions)	\$ 2,005	3,146	4,393	10,227	13,189	19,308	13,528

Source: Lazar (1994), p. 55; Canada, *Public Accounts of Canada, 1996*, p. 4:21.

system, and an increasing trend toward income-based redistribution through the UI system.

Thus, the general preferences of the business community for a full-scale restructuring of the UI system to conform with “insurance principles” (Unemployment Insurance Reform Business Coalition) has carried far less weight than the policy preferences of ministers and officials at HRD and Finance, along with the political constraints imposed by the “UI caucus” of MPs from areas of high structural unemployment.

The relative political impotence of both business and labour in shaping EI policy in the 1990s is evident in the finance department’s ability to run up an EI fund surplus far greater than required to maintain premium stability despite business demands for major premium cuts and calls by union and social activists for benefit improvements and more direct job creation (Table 5).

The 1995-96 reforms, which relabelled the program “Employment Insurance,” continued and expanded the incrementalist pattern of policy change initiated in the late 1980s while, at the same time, pursuing a significantly broader range of policy goals. These measures, which will be examined later in greater detail, reflect the institutional trade-offs and political brokerage that have dominated debates over federal UI reforms since the mid-1970s — CEIC/HRD’s relationships with the federal Department of Finance, the “UI caucus” of the federal Parliament, and to a lesser degree, provincial governments responsible for social assistance and some employment training programs.

INSTITUTIONAL POLITICS: FINANCE, THE PROVINCES AND THE “UI CAUCUS”

The most important constraint on HRD’s autonomy both at the Cabinet table and within the federal bureaucracy during the 1990s has been the Department of Finance. Savoie (1990) characterized this relationship as one between the “guardians” of the fed-

eral purse at the Finance Department (and occasionally other central agencies), and the “spenders” in other federal departments. The Department of Finance wields its institutional influence over UI policy through the exercise of four main roles: as guardian of the fiscal framework, in its jealously guarded control over tax policy and tax rates, as the main custodian of federal interests in federal-provincial fiscal relations, and as the senior (and increasingly dominant) economic policy ministry of the federal government.

While the Department of Finance’s capacity to enforce budgetary discipline has increased greatly since the mid-1980s, its power until quite recently was primarily that of constraining the spending decisions of other ministries rather than dictating its own micro-policy framework. For example, faced with a significant cyclical surplus in the “UI account”⁵ in the late 1980s, Employment Minister Valcourt accommodated the Finance Department’s budgetary constraints by financing active labour market measures and other “non-insurance” elements of the UI system from employer-employee premiums rather than general government revenues, as had previously been the case. This change increased the cost of benefits financed by UI premiums by \$2.9 billion — about 30 percent — in 1990.

The Finance Department’s growing power to enforce its deficit reduction strategy since the 1993 election has imposed significant fiscal and political constraints on HRD’s capacity to pursue an innovative social policy strategy. During the Chrétien government’s first mandate (1993-97), this not only precluded the use of fiscal dividends from economic recovery to “purchase” support for policy changes through increased program spending or transfers to the provinces. It resulted in the application of virtually all new federal revenues and cyclical reductions in UI spending to deficit reduction.

First, the Finance Department enforced a net spending reduction in the UI/training segment of the social policy envelope in 1994 — reducing HRD’s

“Consolidated Revenue Fund budget” by \$1.1 billion. One HRD official interviewed commented that “when the social security review emerged from Cabinet, the driving force was the fiscal imperative. Senior officials [of HRD, Finance, and the Privy Council Office] met frequently. There was blood on the floor. It was our blood.”⁶

This was repeated in the 1995 budget cycle. According to one of Axworthy’s senior advisors, “Finance’s needs changed dramatically between the beginning of the process and the 1995 budget. [Finance Minister Paul] Martin wanted over \$1 billion [in budget reductions] on social policy and about \$800 million on UI.” (interview) As a result, HRD could only shift about half the savings from its hoped-for UI restructuring to the expansion of other income support programs. The other half went to short-term deficit reduction. Additional funds for training and other active measures became contingent on greater UI cuts. This, according to an HRD official interviewed, severely undermined Axworthy’s ability to “sell” UI reform to the social policy community and the Canadian public as a “positive sum game.”⁷

Second, the Finance Department used its control over tax rates to strengthen UI’s function as an automatic stabilizer as part of its medium-term fiscal strategy. This was one of the department’s major objectives in pressing for net program savings from UI reform (Department of Finance official). On the one hand, Finance Minister Paul Martin sought to avoid a recurrence of the major UI premium increases of the 1991-93 recession, which led to a loss of at least 130,000 jobs (Parker 1995, pp. 32-33; Little 1995). On the other, the swelling UI/EI surplus became a major component in Martin’s successful deficit-elimination strategy. When a growing economy generated annual surpluses of UI premiums over benefits averaging \$6 billion in 1994-97 (see Table 5), Martin had to fend off growing pressures from business, the provinces, and the parliamentary opposition to reduce premiums by more than token amounts.⁸

Third, the 40 percent reduction in federal-provincial transfers for shared-cost programs between 1995 and 1998 announced in the 1995 budget, most notably, the replacement of the Canada Assistance Program (CAP) and Established Programs Financing (EPF) transfers with the new Canada Health and Social Transfer (CHST) effectively shifted much of the burden of federal deficit reduction to the provinces.

Finance also made its policy views known on a number of micro-policy issues, most notably the desirability of reducing work disincentives and its scepticism over the effectiveness of active labour market measures — a large element of the “reinvestment” package proposed by HRD in the name of reducing regional disparities (Sargent 1995; officials from Privy Council Office, Department of Finance, and HRD).⁹ However, in these matters, HRD Minister Lloyd Axworthy’s political and policy judgement as the responsible minister were ultimately decisive. The trade-offs between reduced income maintenance and increased “reinvestments” in training and labour market development were closely linked to the need to prepare a package that would withstand the predictable backlash from the Atlantic caucus and their constituents.

Parliament and the Government Caucus

It’s very hard to do structural reform unless you have an Atlantic strategy — senior HRD official.

The second major institutional constraint on the autonomy of the HRD/CEIC bureaucracy to introduce major changes to the UI system is the government’s parliamentary caucus. Thomas (1985) has noted the strength of regional party caucuses over the years in lobbying Cabinet on behalf of regional interests. MPs from regions of chronically high unemployment — Quebec, Atlantic Canada, Northern Ontario, and Northern Manitoba — accounted for well over half the membership of the Liberal caucuses of 1974-79 and 1980-84, and just under half the Progressive Conservative caucuses between 1984 and 1993 (see Table 6). Both under the Trudeau

TABLE 5
 The "UI Account," 1990-1997 (\$ billions)

	1990	1991	1992	1993	1994	1995	1996	1997 ^a
<i>Revenues</i>								
Premiums	12.9	14.8	17.9	18.5	19.3	19.2	19.1	19.1
CRF ^b	2.4	—	—	—	—	—	—	—
Other	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.4
Total	15.1	14.9	18.0	18.6	19.4	19.3	19.2	19.5
<i>Expenses</i>								
Benefits	13.4	17.7	18.1	18.0	15.5	13.6	12.9	12.0
Other costs	1.2	1.3	1.2	1.4	1.3	1.3	1.2	1.3
Interest on CRF advances	—	0.1	0.3	0.4	0.3	0.1	—	—
Total	14.3	19.0	20.5	19.8	17.0	14.9	14.1	13.3
Surplus or (Deficit) in \$ Millions								
> Premiums-Benefits	(503)	(2,930)	(1,225)	496	3,864	5,675	6,200 ^a	7,108
> UI Account	925	(4,205)	(2,631)	(1,208)	2,283	4,267	4,999	6,211
Cumulative Balance	2,160	(2,045)	(4,676)	(5,884)	(3,601)	666	5,665	13,512

 Notes: ^aEstimated

^bConsolidated Revenue Fund

 Sources: Canada, *Public Accounts of Canada, 1992-96; Estimates, 1996-97, 1998-99*; HRD Chief Actuary (1997).

 TABLE 6
 The "UI Caucus," 1974-1997

Government	Total Government MPs	Government MPs from			"UI Caucus"	"UI Caucus"/ Government MPs
		Atlantic	Quebec	N. Ont./N.Man.		
1974-79 (L)	141	13	60	8	81	57.4%
1979-80 (PC)	136	18	2	0	20	14.7%
1980-84 (L)	147	19	74	11	147	70.7%
1984-88 (PC)	211	25	58	4	87	41.2%
1988-93 (PC)	169	12	63	1	76	47.8%
1993-97 (L)	177	32	19*	12	63	35.6%

Note: "UI caucus" figures for this Parliament may be overstated as all but 3 of 19 Quebec Liberal MPs come from the Montreal or Ottawa areas.

Liberals and the Mulroney Conservatives, the Quebec and Atlantic caucuses usually formed a cohesive bloc within the governing party which, together with their “regional ministers” in Cabinet, proved capable of forcing successive employment ministers to water down proposed changes to Unemployment Insurance (Thomas 1985, pp. 96-97; Savoie 1990, pp. 142-46).¹⁰ Since the restructuring of the House of Commons’ committee system in the mid-1980s, their efforts have been reinforced by those of the Standing Committee on Employment and Immigration — since 1993, the Standing Committee on Human Resources Development. Whether under the Tories or the present Liberal government, the CEIC/HRD Committee has usually been the preserve of MPs favouring the protection and expansion of redistributive and remedial social programs. As such, it has frequently provided a platform for members of the social policy community — social policy advocates, groups representing beneficiaries, trade unions, and government-funded social agencies — to lobby against reductions in UI entitlements or more stringent conditions for the receipt of benefits.

The “UI caucus” thus links regional and ideological pressures to maintain the political status quo, while arguably transcending both. It reflects one of the most enduring characteristics of Canadian politics, a commitment to “distributive federalism”: the use of federal power to transfer tax revenues and economic opportunity from more prosperous to less prosperous regions of the country. Preserving the system of variable entrance requirements and enriched benefits for regions of chronically high unemployment and their major seasonal employers has been the central objective of the UI caucus since the late 1970s — and the central political reality to be accommodated or circumvented by Minister of Employment Lloyd Axworthy in attempting to introduce large-scale changes to the UI system in the mid-1990s.

The blocking power of the UI caucus after the 1993 election was reduced somewhat by the victo-

rious Liberals’ relatively weak performance in Quebec and, ironically, by their near-monopoly in Atlantic Canada. Axworthy met regularly with Cabinet and caucus colleagues from Atlantic Canada to refine a package that they could present to voters as protecting the region’s vital interests. Prime Minister Chrétien ultimately dealt with the divisions within his Cabinet and caucus by assigning the issue to a special Cabinet committee which would vet Axworthy’s proposals for their political, regional, and fiscal impact (Greenspon 1996*b*; Department of Finance official).

Federal-Provincial Relations

UI reform and the federal government’s pursuit of broader social policy reforms have also been constrained by the broader trend of federal-provincial relations in the late 1980s and 1990s toward a more decentralized approach to the federal-provincial division of powers. This can be seen in the ongoing efforts of the Province of Quebec and other provinces to secure exclusive jurisdiction over employment-related training — along with the fiscal resources to pay for it.

Federal fiscal retrenchment during the early and mid-1990s contributed to a decline in the influence and the perceived legitimacy of the federal spending power as a policy instrument to shape provincial spending priorities and facilitate the harmonization of federal and provincial policies. Instead of the national shared-cost programs of the 1960s and 1970s, there has been a growing trend since the mid-1980s toward bilateral agreements between the federal government and individual provinces both under the Mulroney and Chrétien governments.¹¹ These can be more closely tailored to local political conditions and avoid the necessity of winning consensus among the provinces. It remains to be seen whether the package of education and training subsidies announced in the 1998 federal budget signals a significant shift in federal-provincial relations as the allocation of fiscal surpluses replaces deficit reduction as the defining reality of budgetary politics.

HRD's autonomy in restructuring its labour market adjustment and training programs in conjunction with its proposals for UI reform has faced three other significant constraints related to federal-provincial relations. With UI's high visibility as the major federal income support program in large areas of Quebec, the imminence first of a Quebec election, then of a sovereignty referendum in 1994-95 forced the Chrétien government to defer or soft-pedal its plans for UI and social policy reform for the first two years of its mandate (senior HRD officials). The federal government also conceded the demands of Quebec and other provinces for paramount jurisdiction over training — forcing HRD to coordinate changes in its training and adjustment programs with the provinces. These changes, in turn, reflected an increasingly “decentralist” outlook within the Privy Council Office, the federal central agency most directly responsible for the government's constitutional strategy (*ibid.*).

While federal action on EI reform proceeded independently of provincial views and occasional protests, both of Lloyd Axworthy's successors at HRD Canada, Doug Young and Pierre Pettigrew, have negotiated bilateral agreements with nine provinces on training and adjustment programs in the year following the passage of Bill C-12.¹²

THE EMPLOYMENT INSURANCE (EI) REFORMS OF 1994-1996

Unemployment Insurance reform was probably the most difficult public policy undertaking undertaken by this government (Department of Finance official).

Unemployment Insurance reform initially began as part of a larger consultation process on social policy reform in October 1994, following more than a year of internal departmental activity (Greenspon and Wilson-Smith 1996, pp. 137-52). Human Resources Development Minister Lloyd Axworthy suggested several reasons for considering “fundamental reform” of the UI system:

- the growing need to shift UI's emphasis away from passive income support to active labour market measures — training and adjustment support for individuals facing long-term unemployment due to structural economic change;
- the growing number of frequent UI recipients, especially in seasonal industries, and of employers structuring work requirements to coincide with UI eligibility requirements; internal HRD studies showed that about 40 percent of recipients had made at least three claims in the past five years (Human Resources Development Canada 1995b);¹³
- the persistence of work disincentives and “abuses,” related to the so-called 10/40 system of short-term work requirements for extended periods of benefits in areas of chronically high unemployment;
- growing program costs, and related payroll tax increases, creating a drag on economic activity and job creation;¹⁴
- the growing number of part-time workers and other “non-standard” forms of employment not covered by the existing UI system. None of these circumstances were new. Most had been occurring for 10 to 20 years. However, a combination of changing economic circumstances — which drew attention to the growing problem of structural unemployment and the UI system's inability to cope with it — and changing political circumstances increased pressures for major changes to UI policies, programs, and budgets.

The following section will examine the economic and political circumstances surrounding the EI reform debate of 1994-96 and the three phases through which it passed before Parliament approved Bill C-12 in May 1996.

Unemployment, Structural Economic Change and UI Reform

The changing nature of Canadian unemployment, and the role of the state in shaping economic and

social policies capable of responding to it, were central to the rethinking of Unemployment Insurance policy during the late 1980s and 1990s. Even before the negotiation of free trade with the United States, Canada's economy went through a period of massive structural economic change which resulted in significant disruptions in employment and labour markets. While overall employment levels grew steadily during the late 1980s, permanent layoffs averaged almost 1.2 million annually between 1981 and 1993, with only minor cyclical variations (Picot and Lin 1997, p. 5). Hiring levels show much greater cyclical variations. Unemployment levels for young workers, workers lacking a postsecondary education, and older workers increased sharply during the early 1990s, well beyond normal cyclical levels. While the severity of the 1991-92 recession contributed to the growth of long-term unemployment, several factors contributed to the growth of structural unemployment above and beyond its cyclical effects.

Wage costs increased faster than labour productivity in the late 1980s. Increasing international competition and the effects of technological change led to high levels of capital investment and the substitution of technology for labour in many industries — along with regional and sectoral shifts in available employment. The impact of steadily falling commodity prices after 1989 was particularly great in the resource-dependent economies of Atlantic Canada and Eastern Quebec. Steady increases in payroll taxes — especially those needed to finance UI — also cut significantly into job creation (Canada. Department of Finance 1994*b*, pp. 3-6, 17-24; Parker 1995; Osberg, Wien and Grude 1995).¹⁵

While the existing UI system was set up to deal with cyclical economic fluctuations, as well as to accommodate the needs of workers and employers in seasonal industries, numerous political and economic observers expressed concern that its traditional emphasis on passive income maintenance was not enough to reverse the trend toward higher levels of structural unemployment — the mismatch be-

tween available skills and jobs — and thus to address the changing skills required for Canadians to find (or hold on to) work and compete effectively in a changing economy. Political support for increased government spending on job creation and income maintenance entitlements for the unemployed was seen to be limited by the stagnation and decline of disposable household incomes and the increasingly skewed regional distribution of UI benefits (Axworthy 1994, p. 5; Courchene 1994; Osberg 1995, pp. 5-9; Greenspon 1996*a*).

Regional variations in the role of the UI system have always reflected the problems of chronic structural unemployment and seasonal employment in large parts of rural Atlantic Canada. While most observers recognized that UI has become part of a vicious cycle of underdevelopment and dependence, there was far less consensus over the extent to which UI-related distortions to economic and work incentives were and are a cause of structural unemployment rather than a reflection of the region's chronic economic weakness. Nor was there much consensus on alternative measures to increase the supply and quality of employment in the region, or the relative degree to which the state, employers, workers and those seeking work should accept responsibility for finding solutions to the problem of unemployment (Corak 1994; McBride 1992; Osberg, Wien and Grude 1995). These competing and overlapping analyses are enmeshed with moral, philosophical, and ideological commitments that transcend the technocratic dimensions of the policy process.

Critics of the UI system have long argued that regional variations in qualifying periods and benefits have hindered economic restructuring and the mobility of labour. Moreover, pointing to steadily rising levels of unemployment and UI costs at each stage of successive business cycles between the program's massive expansion in 1971 and the early 1990s, they contended that UI's traditional emphasis on passive income support rather than making benefits conditional on increased work effort or the

acquisition of marketable labour skills amounted to a self-defeating policy of reinforcing economic dependence (Canada. Royal Commission 1985; Canada. Commission of Inquiry 1986; Newfoundland. Royal Commission 1986; May and Hollett 1994). Finance Minister Paul Martin clearly signalled the government's acceptance of this analysis in his "purple book" of October 1994, noting that while governments should assist Canadians to acquire needed skills and "adapt to new opportunities," "the primary responsibility to develop the nation's base of skills lies with Canadians themselves" (Canada. Department of Finance 1994*b*, p. 41).

Defenders of the existing EI system, particularly from organized labour and social policy groups, tended to reject the "artificial" distinction between cyclical and structural unemployment, arguing that both were the outcome of deeply flawed fiscal and monetary policies, especially the high interest rate policies of the Bank of Canada during the early 1990s (Osberg and Fortin 1996; Jackson 1995, pp. 25-26). They bitterly opposed cuts to existing entitlements, arguing that they have mitigated the worst effects of structural unemployment by maintaining consumer purchasing power and with it, the economic viability of many smaller communities dependent on seasonal and resource industries. They have consistently rejected any approach to UI reform that would force the unemployed to bear the primary burden of economic adjustment, and in favour of macroeconomic policies more conducive to full employment (McBride 1992; Jackson 1995; Riche 1995; Osberg 1996; Cameron and Browne 1994). Alternative approaches suggested including government-mandated measures to redistribute available work such as shorter work weeks, incentives for job sharing, and mandatory restrictions on overtime (Canada. House of Commons 1995, pp. 47-49; Finn 1996, pp. 51-52).

EI Reform — Changing the Terms of the Political Debate

The political environment in which Lloyd Axworthy sought to introduce major structural changes to the

UI system had also changed significantly from that which had frustrated the efforts of previous governments.

Four factors appear to have been critical in shaping the direction of policy changes:

- the continuing trend to the dilution of universal social programs in favour of increased selectivity and targeting;
- the disruption of traditional patterns of party competition arising from the 1993 election;
- growing public acceptance of the spending reductions necessary to curb huge structural public deficits as an alternative to the continuing growth of taxes;
- a strong ambivalence in public opinion about applying significant spending reductions to social program spending.

Axworthy's inability to overcome this ambivalence ultimately appears to have dictated both the contents and limits of the EI reforms of 1994-96.

In its efforts to curtail a persistent structural deficit, the previous Conservative government had taken several initiatives to limit universal access to social benefits, whether delivered directly or through the tax system, in favour of greater targeting of policies and programs "to those in greatest need." Typically, this involved placing a greater emphasis on income redistribution based on family incomes which limited the eligibility of middle and upper income families to such programs as family benefits (replaced with the Child Tax Credit in 1991) and increased the upper-income clawback for UI benefits. Other policies sought to discourage "inappropriate" or repeated use of UI benefits by reducing benefit levels for repeat users. Public opinion surveys commissioned by HRD Canada in 1994 identified fairly broad support for both approaches (Angus Reid Associates 1994*a*; 1994*b*; 1994*c*).

The 1993 federal election also resulted in a major disruption of traditional patterns of party representation in Parliament which affected the terms of the social policy reform debate. The Liberals' virtual sweep of Ontario and their continued weakness in Quebec meant that the five UI-dependent provinces had the weakest representation in the caucus of a majority government since the program's inception in the 1940s. When the Chrétien Liberals, once in office, repudiated their once reflexive opposition to any significant retrenchment or restructuring of social spending, the decimation of the New Democrats and the political isolation of the Bloc Québécois opposition meant that the most significant pressures for further change would come from a Reform Party deeply committed to deficit reduction and a comprehensive rethinking of traditional Canadian approaches to social insurance.

The emergence of deficit reduction as a major public priority appears to have followed the conversion of political elites, reinforced by the pressures of international financial markets, rather than from any significant groundswell of public opinion. The Liberals' electoral commitments of 1993 had been built around relatively soft options in addressing the deficit. Only when it became clear in mid-1994 that the federal government could not "grow itself out of the deficit" did a serious effort at deficit reduction involving significant spending reductions begin to take shape (Greenspon and Wilson-Smith 1996, pp. 153-70). Even in this effort, Martin recognized the ambivalence of public opinion about the government's apparent reversal of priorities and was careful to focus the bulk of initial spending cuts on federal-provincial transfers and Ottawa's own administrative expenses rather than on direct federal transfers to individuals (Canada. Department of Finance 1995).

This ambivalence in public opinion clearly identified both the terms upon which the majority was likely to be receptive to social policy reforms — including UI reform — and its reluctance to contemplate a full-scale restructuring of social programs

as part of a larger commitment to deficit reduction. Studies conducted during 1994 identified a core group of between 30 and 40 percent of voters willing to support such a program, with 35 percent sceptical of or opposed to both UI restructuring and spending cuts. The remainder, labelled "trusting compassionates" by Angus Reid, indicated a willingness to support reform if those in greatest need were protected and spending was targeted to help the unemployed more effectively improve their skills or find work (Angus Reid Associates 1994a; 1994b; 1994c).

While a small majority had indicated support for components of a two-tier system, this proved insufficient to sustain proposals for such fundamental structural change against the determined opposition of most social policy groups and the UI caucus. A more modest, but more clearly targeted set of initiatives which balanced more stringent entrance requirements (and reduced benefits) for repeat users with expanded benefits for part-time workers and low-income families — while not enough for enthusiasts of all-out restructuring (Angus Reid Associates 1996) — was enough to win the support of Liberal voters anxious to maintain and improve the social safety net while questioning the value or effectiveness of universal entitlements.

EI reform went through three major stages in its passage through Parliament. The first stage, a consultation process based on the social policy reform Green Paper of October 1994, proved too ambitious for the limited fiscal and political resources available to promote it. Bill C-111, which contained a scaled-down but still significant series of EI reforms, was introduced in December 1995. Doug Young, who succeeded Axworthy as HRD minister, fine-tuned the legislation, reintroduced as Bill C-12, in response to a strong backlash from rural Atlantic Canada, before its passage through Parliament in May 1996.

Stage One: The Green Paper, October 1994

Axworthy tabled his discussion paper on social policy reform in October 1994. A wide-ranging

document, the Green Paper outlined options for the restructuring of a number of social programs including Unemployment Insurance, federal contributions to training and postsecondary education, and possible changes to the Canada Assistance Program.

One of the possible alternatives to UI canvassed in the discussion paper was a two-tier approach to EI, maintaining existing benefit structures for individuals with a consistent attachment to the labour force, but suggesting either reduced or conditional benefits for frequent UI claimants. Senior officials interviewed for this article suggest this was the department's preferred approach.

The other major alternative was consistent with the trend of recent years — increasing the number of weeks required to qualify for UI and reducing the scale and duration of benefits. In either event, Axworthy and HRD officials were determined to shift more UI resources away from passive income support toward employment adjustment and training programs — the “active labour market” approach (Human Resources Development Canada 1994*a*, HRD officials). An official in the Privy Council Office said, “Axworthy was deeply committed to structural reform ... by changing the very logic of the program rather than just shrinking it, so that it would be more conducive to work.” This approach soon ran into conflict with the Liberals' Atlantic caucus, including several of Axworthy's Cabinet colleagues, the Commons' Human Resources Development Committee, and much of the social policy community, especially in Quebec and Atlantic Canada.

Most social welfare advocates rejected both the analysis of the UI “problem” advanced by Axworthy and his officials, and the policies intended to deal with them. Testimony before the Commons HRD Committee suggests that most of these groups tended to view UI as an income support program rather than an insurance program. As noted earlier, they tended to view structural unemployment either as the effect of job shortages or misguided economic poli-

cies rather than the inadequate skills of seasonal workers or the work disincentives built into the UI system (Cameron and Browne 1994; Canadian Labour Congress 1994; Canada. House of Commons 1995). After years of seeing government-funded training programs result in little change in regional employment patterns, the proposed emphasis on active labour measures was rejected by most unions, social policy groups, and even many businesses as a largely ineffective palliative for structural unemployment, particularly in rural Atlantic Canada and Quebec (Lazar 1994, pp. 60-73; Jackson 1995; Osberg 1996). Most elements of the social policy community argued instead for maintenance of UI as an unconditional income maintenance system.

While public opinion as a whole seems to have been rather more supportive of Axworthy's initial proposals for UI reform than was the social policy community, he was caught in the political crossfire in his attempt to overhaul social assistance policies and postsecondary-education financing at the same time. The widespread perception that EI reform was primarily driven by the federal government's deficit reduction program (Angus Reid Associates 1994*c*, p. 6) also undermined Axworthy's ability to sell the proposed changes on their merits. Before long, he was widely seen to have lost the political initiative.

The HRD Committee's report of January 1995 rejected the two-tier approach outright, and was highly critical of efforts to reduce direct UI spending in favour of increased funding for training and adjustment (Canada. House of Commons 1995). Even stronger internal opposition to conditional benefits came from Atlantic Liberal MPs and from several of Axworthy's own Cabinet colleagues, especially Fisheries Minister Brian Tobin (Greenspon and Wilson-Smith 1996, pp. 295-304; senior HRD official). Based on HRD projections, Axworthy's proposed changes would have reduced EI transfers to Atlantic Canada by almost 20 percent prior to “reinvestments” — in addition to previous reductions in 1990, 1992, and 1994 (Human Resources Development Canada 1996*a*; HRD official

interviewed by author). The introduction of UI reform legislation was further deferred until December 1995 to give Axworthy time to respond to his critics inside and outside government.

Stage Two: Bill C-111, December 1995

Axworthy's long-awaited legislation, which renamed the program "Employment Insurance," was a complex series of political and policy trade-offs intended to shift the emphasis of the program away from passive entitlements while selectively enriching or broadening access to benefits for low-income families and part-time workers and continuing to shift resources toward training programs and other "active labour market" uses. The new bill included a number of technical proposals presented by Axworthy as a "balanced" package designed to address specific problems and mitigate the effects of proposed changes on existing beneficiaries. These measures can be summarized under three headings: reducing work disincentives and creating incentives for greater "work intensity"; pursuing greater distributive equity among EI beneficiaries, including the extension of benefits to part-time workers; and the "reinvestment" of a share of EI savings to finance a number of new or redesigned job creation and training programs. Axworthy earmarked about \$800 million of the \$1.9 billion in projected savings in "employment initiatives" — funds for training, employment subsidies, and direct job creation. These measures, targeted mainly at high unemployment areas of Atlantic Canada and Quebec, were intended to ensure that "no province [would] see an overall financial reduction of more than seven percent" (*ibid.*) over the five years in which the new system would be phased in.

Work disincentives were to be countered by several measures:

- a shift from weeks to hours worked, based on a standard 35-hour work week, to recognize greater "work intensity" during limited periods of employment; this also facilitated access to benefits for part-time workers;

- a gradual increase in the minimum number of weeks to qualify for EI benefits from the equivalent of 12 to 16 weeks;
- a longer qualifying period for new entrants to the labour market (those without a minimum of 14 weeks' insured employment during the previous year);
- a longer "averaging" period on income earned for regional qualifying periods of fewer than 20 weeks, to encourage seasonal workers (and their employers) to prolong employment beyond the minimum qualifying period;
- reducing EI benefit rates from 55 to as little as 50 percent, depending on the extent of UI claims during the past five years;
- reducing the maximum period of benefits from 50 to 45 weeks of benefits in areas of high unemployment (Human Resources Development Canada 1995*b*).

Axworthy's proposals also sought to achieve a greater distributive equity among EI recipients by:

- reducing the income threshold for the 30 percent tax clawback on EI benefits from \$63,570 to \$48,750 for infrequent claimants;
- reducing the clawback threshold to \$39,000 for more frequent or extended claimants (more than 20 weeks' benefits in past 5 years) and escalating the clawback rate from 50 to 100 percent, depending on the frequency and duration of claims during the previous five years; and
- increasing benefits payable to lower income EI beneficiaries with dependent children to as much as 80 percent of insured earnings.

This, in turn, was balanced by reducing maximum insurable earnings from \$42,000 (or 140 percent of the average industrial wage [AIW]) to

\$39,000 (130 percent of AIW), and by introducing a series of administrative changes intended to speed tax collection. This approach was consistent with the internal logic of departmental policy making, particularly as HRD's own consultants were suggesting that the complexities of the existing system, which reflected its multiple objectives, effectively precluded sweeping policy solutions (Corak 1994, pp. 90-111).

While these measures enjoyed broad, if somewhat superficial, public support (Angus Reid Associates 1996), Bill C-111 was bitterly attacked, especially by resource industry unions in Atlantic Canada, as an assault on regional entitlements in the name of deficit reduction.¹⁶ The unions organized active resistance, especially among forest and fish-plant workers, which resulted in a series of well-publicized demonstrations, sit-ins in government offices, and the occasional riot.

At the end of January 1996, Prime Minister Chrétien replaced Axworthy as minister of human resources development with New Brunswick's Doug Young. Young set to work to make changes to Axworthy's EI reforms that would address the most pressing regional grievances while preserving his predecessor's main political and policy thrusts.

Stage Three: Bill C-12, April-May 1996

Young's main political challenge was to address the grievances of seasonal workers with the new EI system's efforts to encourage greater "work intensity" or workplace attachment — in effect, the principle that "the more you use (UI), the less you get." While Young had initially hinted at broader changes to the legislation, including a reduced emphasis on training programs and fewer penalties for repeat users (Greenspon 1996a), amendments finally announced in April 1996 were relatively minor. Young's influence may have been more decisive in accelerating the transfer of jurisdiction over training programs to the provinces, a step that had been resisted by Axworthy. However, this policy shift had become inevitable when Prime Minister Chrétien announced

his conversion to it on the eve of Quebec's sovereignty referendum the previous October (Greenspon 1996b).

Young's revised legislation, necessitated by a new session of Parliament, was introduced as Bill C-12 in April 1996. He made a series of technical changes aimed primarily at the concerns of seasonal workers in Atlantic Canada that were expected to reduce projected benefit cuts by \$365 million, or 17 percent of the original fiscal impact. Another series of measures intended to discourage benefit fraud by employers and workers was supposed to recover \$245 million, while "reinvestment" programs were to be adjusted in proportion to benefit increases in each province to meet existing fiscal targets.

These changes were intended to deal with four specific issues:

- permitting individuals with "gaps" in employment to qualify by allowing them to count only actual weeks worked (minimum 16 within 26 consecutive weeks), rather than averaging earnings for the entire qualifying period; this was intended to reduce penalties for persons with intermittent work, consistent with overall policies of encouraging greater work intensity;
- revising the controversial new "divisor" rule, whereby workers would have received significantly reduced benefits unless they had worked three or four weeks *more* than the minimum qualifying period;
- exempting low income families from the intensity rule — a gesture toward income redistribution for those most in need; and
- reducing the time needed to requalify for benefits for workers earning some income while receiving EI benefits (Human Resources Development Canada 1996b).

The targeted changes made in Bill C-12, while economically significant, did not alter the broad

thrust of the legislation, which was passed by the House of Commons in May 1996. While Young addressed a number of concerns raised by seasonal workers, including those in his own riding, his refusal to revisit the basic goals of EI reform and his brusque dismissal of protesters contributed to his subsequent electoral defeat in what had been one of the safest Liberal seats in Atlantic Canada.

Young's tenure as minister of human resources development was relatively brief, as he was appointed minister of national defence in October 1996 in the aftermath of the Somalia scandal. His successor, Pierre Pettigrew, carried forward Young's commitment to negotiate the transfer of responsibilities for labour market training to the provinces. Pettigrew also introduced a new hiring incentive program for small businesses to encourage job creation and offset the increased payroll tax burden created by Bill C-12 for employers of part-time workers. In March 1997, Pettigrew also announced further changes to the work intensity rule for part-time workers in areas of high unemployment to reduce their effect on seasonal workers, particularly those in the fishery (*The Globe and Mail*, 6 March 1997, p. A8; McCarthy 1996).

CONCLUSION

The Employment Insurance reforms of 1994-96 were the culmination of a process of incremental reforms stretching over almost a decade. During this period, the federal government effectively restructured the program — significantly reducing work disincentives, promoting greater workplace attachment and strengthening the program as a tool of economic stabilization by “pre-funding” benefits and running up huge surpluses during the economic expansion after 1994. Regional benefits were maintained, on a reduced scale, and compensation of a sort paid to the provinces in the form of increased training and job creation subsidies from EI funds.

EI reform demonstrates both the extent and limits of departmental and state autonomy in the de-

velopment of EI policy. HRD Minister Lloyd Axworthy and his officials were modestly successful in persuading the Canadian public to accept their critique of the old UI system and the need for reform — despite significant opposition in Atlantic Canada and continuing public concerns that EI reform was merely a cover for deficit reduction. Regional interests inside and outside the federal government blocked fundamental changes to the program — notably Axworthy's proposal to introduce a two-tier system — and extracted significant compensation to regional stakeholders for changes introduced in Bills C-111 and C-12. However, HRD Canada was able to pursue its broader objectives — including a series of measures which, taken together, significantly increased incentives for work intensity and labour force attachment and which shifted additional resources toward increased training and active labour market policies — despite considerable stakeholder opposition in many cases.

While these policies reflect some aspects of the business critique of the old UI system, especially in their attack on “work disincentives,” business groups' direct influence can be discounted heavily in narrower UI/EI policy terms. The new program's increased emphasis on active labour measures, its commitment to intensified income redistribution based on family income and the Finance Department's success in building up EI fund surpluses far above levels required to maintain stable premium levels through a business cycle — rather than cutting premium rates sharply as advocated by all major business groups — all reinforce arguments for relative state autonomy both in sectoral policy issues and related details of fiscal policy.

The existence of sizeable EI fund surpluses, currently approaching \$20 billion and growing by \$7 to \$8 billion annually, is certainly a destabilizing factor in the future of EI policy. However, if recent history is relevant, future program changes are likely to be guided by the Finance Department's assessment of the fiscal framework and the policy priorities of HRD Canada rather than the wish lists of mutually antagonistic stakeholders.

NOTES

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¹A 1992 CEIC study calculated that the “recycling” of provincial welfare recipients on to Unemployment Insurance through provincial make-work programs added as much as \$2.6 billion to federal UI costs in 1991 (Canada. Office of the Auditor General 1994, Vol. 3, p. 47).

²Cross-subsidization of industries ranges from benefit to contribution ratios of 5.04 in logging and forestry and 3.94 in construction to 0.40 in education and 0.48 in finance/insurance, assuming that overall UI premiums equal benefits (Human Resources Development Canada 1996a, p. 1:3).

³One HRD official comments that Forget’s proposals “shut down the reform process for five years.”

⁴Earnings replacement rates are UI benefits as a percentage of weekly employment earnings under the maximum insurable earnings.

⁵The UI account refers to a notional account reflecting UI premium revenues and expenditures charged against the “fund” related to UI expenditures (including interest costs of financing UI deficits); consolidated with federal budgetary accounts since 1986 (Treff and Perry 1996, p. 9:4).

⁶This comment is challenged by other HRD officials interviewed who, while acknowledging the fiscal element in UI reforms, insisted that it was equally driven by internal policy considerations.

⁷Despite Axworthy’s efforts to promote UI reform on its own merits, the Ottawa press gallery tended to report the proposed reforms as little more than a cover for the Finance Department’s deficit reduction exercise. Freeman and Greenspon 1994; Greenspon 1995a. These views appear to have been shared by about two-thirds of Canadians (Angus Reid Associates 1994c, p. 6).

⁸Premium reductions from \$2.90 to \$2.80 and subsequently \$2.70 per \$100 of insured payroll were announced

after the 1997 budget, effective in 1998, as part of a trade-off with the provinces for approving accelerated Canada Pension Plan premium increases.

⁹While some HRD officials also expressed scepticism of the value of training programs in depressed labour markets (Lazar 1994, pp. 60-73), this had relatively little impact on short-term policy decisions. In the longer term, Finance preempted the debate by directing education and training funds to individuals rather than institutions — most of which are within provincial jurisdiction (Canada. Department of Finance 1998).

¹⁰Newfoundland’s Brian Tobin and Cape Breton’s David Dingwall appear to have been the strongest regional advocates — at least on social programs — in the first Chrétien Cabinet.

¹¹Both the Meech Lake and Charlottetown rounds of constitutional negotiations sought to place tight restrictions on the use of the federal spending power in areas of provincial jurisdiction. This “decentralist” outlook toward fiscal federalism appears to have become entrenched in the Privy Council Office, even under the Chrétien Liberals (senior HRD official).

¹²As of November 1998, bilateral agreements for the devolution of administrative responsibility for training had been concluded with all provinces and territories except Ontario (Human Resources Development Canada 1998). Funds for EI-eligible clients were to be financed from “reinvestment funds” set up under Bill C-12.

¹³A senior HRD official interviewed commented that addressing the issue of repeat users was one of the department’s top priorities in UI reform.

¹⁴UI premium rates increased by 54 percent between 1989 and 1993, while the UI account went from a cumulative surplus of \$1.1 billion to a cumulative deficit of \$5.9 billion at the end of 1993 (Canada. Office of the Auditor General 1994, pp. 6-50).

¹⁵UI premium increases accounted for three-quarters of the rise in the national effective rate of payroll taxes between 1990 and 1993 (Picot, Lin and Beach 1995).

¹⁶The Angus Reid Study indicated that while about half of Canadians surveyed thought the government was “moving in the right direction,” support for reform increased to 75 percent (64 percent in Atlantic Canada) following a discussion of the specific proposals.

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The author wishes to acknowledge the cooperation of a number of senior officials of Human Resources Development Canada, the federal Department of Finance and the Privy Council Office who generously shared their time and expertise on the condition of confidentiality.

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