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Empowering Entrepreneurship:

Exploring the Untapped Potential of Our Nation's UI System

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INTRODUCTION

At present, the United States is enjoying a stunningly low rate of unemployment. The federal government's most recent report puts that rate at 3.6% and notes that job openings continue to rise.[1] That's a dramatic rebound from the dark days of Spring 2020, when unemployment skyrocketed to 13%.[2]

To cope with the flood of laid off workers during the COVID-19 crisis, America relied heavily on our nation's Unemployment Insurance (UI) system.[3] Its mission is twofold: First, to provide an income-smoothing effect for workers and their families during times of joblessness; and second, to sustain and stabilize consumer spending during economic downturns. The UI system enables unemployed workers to keep paying bills and caring for their families, which, in turn, keeps other workers employed and regional economies vital.

In short, the UI system is a lifeline for jobless Americans in bad economic times that also has the "countercyclical" effect of shortening recessions. However, the system nearly crashed in many states during the pandemic, and experts believe it's not prepared should the economy start contracting and shedding jobs.[4] U.S. policymakers need to act now, while the system is not under stress, to make it more resilient against future emergencies.

As they do that, policymakers should not overlook UI's untapped potential to create more opportunities for entrepreneurship. Currently, a small program within America's UI system seeks to address this need — the Self-

Employment Assistance Program (SEA).[5] SEA offers qualifying individuals the opportunity for self-employment by combining income support during periods of unemployment with activities related to starting a business. Only 5 states have active programs and as a result, the SEA program serves a very small, distinctive slice of UI recipients, with less than 1% of UI claimants participating in the program.[6] In fact, in 2022, there were only 1,404 SEA participants nationwide.[7] This is a stark comparison to the number of entrepreneurs across America's workforce — with some research now showing there are 31 million entrepreneurs in the U.S. making up 16% of the adult workforce.[8]

While UI undeniably offers support during job loss, it falls short in fostering opportunities for entrepreneurship. This policy brief aims to illuminate the importance of creating more opportunities for entrepreneurship in the U.S., the transformative role UI can and should play in creating these pathways to self-employment and outlines actionable policy recommendations for federal leaders to consider. By enabling dislocated workers to pursue entrepreneurship even amidst financial distress, we can provide increased economic opportunity for individuals, communities, and the nation at large.

THE IMPACT OF ENTREPRENEURSHIP

As policymakers consider this type of reform to UI, they can't ignore the impact of entrepreneurship on the American economy. Right now, U.S. entrepreneurship is surging. In 2020, Americans filed paperwork with the Internal Revenue Service to start 4.4 million new businesses, a 24% increase from the previous year.[9] The boom continued in 2021 and figures released by the Census Bureau showed that new business applications rose by 23% in 2021 to 5.4 million, the most since the government started collecting data in 2004.[10] While maintaining a business is difficult, with only 50% succeeding after the first five years, if a small business survives it yields excellent returns for the economy and the individuals themselves.[11]

New businesses inject vitality into the marketplace, sparking competition that ultimately benefits consumers and ensures the nation's economy remains resilient and competitive. Today, startups and small businesses make up 99.9% of all U.S. businesses.[12] They create two-thirds of net new jobs and generate about 50% of our GDP. In addition, they also drive local economic development efforts — putting money back into their communities through paychecks and taxes.[13]

On a more individual level, entrepreneurial opportunities can help workers get ahead, especially workers stuck in low-paying jobs or those at risk of disruption. These opportunities don't discriminate based on educational attainment — like the rest of our country's labor market. Today, 30% of entrepreneurs finish only high school, 31% have an associate degree, 17% have a bachelor's degree, 18% obtained a master's degree, and 4% have a doctoral degree — demonstrating that entrepreneurship can break down the persisting diploma divides and create more opportunities for working Americans without degrees.[14]

There's also evidence that entrepreneurship can be an attractive reentry strategy for returning citizens — individuals who have previously faced incarceration. A recent report from PPI focused on the fact that entrepreneurship presents a promising pathway to economic security and reintegration into communities as it requires minimal formal schooling, provides additional income, control over one's livelihood, and has the potential to uplift the often-low-income communities to which these individuals return.[15] A 2020 study by Kyle Hwanga and Damon Philips further proves this point, estimating that entrepreneurship reduces the likelihood of re-offense by 5.3% among Black returning citizens.[16] If entrepreneurship can create these types of opportunities for people, it should be offered to support laid-off workers who face high barriers to finding jobs and need alternative options to be upwardly mobile.

While starting a business is not for the faint of heart, it's clear these opportunities are more attractive than ever and can help those with barriers to success in our nation's labor market, like those that are facing unemployment. While building their own business could be a quality option for displaced workers our UI system is geared toward job placement and what does exist serves an extremely small proportion of people — reducing so many workers' shot at parlaying their latent entrepreneurial skills into opportunities for self-employment.

WHAT EXISTS TODAY: THE SELF-EMPLOYMENT ASSISTANCE PROGRAM (SEA)

As mentioned, the one program that does exist today — aimed at supporting UI-eligible individuals in building their own businesses — is the Self-Employment Assistance Program (SEA). SEA is a voluntary state program. States operating an SEA program, like UI, pay a weekly allowance to eligible participants. Participants are exempted from UI rules requiring them to actively job search, so instead they can devote their energies to self-employment activities.

Like the rest of our UI System, the SEA program is financed by federal taxes under the Federal Unemployment Tax Act (FUTA) and by state payroll taxes under the State Unemployment Tax Acts (SUTA). SEA was created in 1993 and permanently authorized in 1998. More recently, provisions in the Middle-Class Tax Relief and Job Creation Act of 2012 gave states the authority to expand SEA participation to certain claimants in the Extended Benefit (EB) and temporary Emergency Unemployment Compensation programs. This bill also provided $35 million in SEA grant funding for FY2012 and FY2013, for states to update and modernize their SEA system.[17] Five states (Mississippi, New York, Oregon, Rhode Island, and Vermont) were awarded the SEA grants in 2013. With the grant dollars and cost for regular enrollment, the total spending for SEA in 2013, which is the last available summary of annual costs was roughly $2.9 million.[18]

Coming back to present day, as of July 2022, five states have active programs with the Department of Labor (DOL), and they are not the same states that received the grant funding in 2013. Today, Delaware, Mississippi, New Hampshire, New York, and Oregon have active programs. SEA programs serve a very small, distinctive slice of Americans unemployed, with 1,404 SEA participants in 2022, which is less than 1% of UI claimants nationwide.[19] This low participation is due to barriers around cost and eligibility which make it very difficult for states to run active programs and for individuals to participate.

The challenge of cost

While the investment (over a decade ago) helped to cover some administrative costs of the program, today, most states find covering the cost of administering the SEA a challenge — resulting in a lack of uptake. Program administrators note that administering SEA is more expensive than administering UI. This is due to the required services attached to SEA. States who offer it are required to provide entrepreneurial training, business counseling, and technical assistance to SEA participants, which are more costly services. What's more is that even with the high cost of services, federal policy requires that SEA programs be budget neutral, meaning states cannot spend more on an SEA participant than what they spend on those receiving UI.

As a result, states must seek out separate resources to finance program administration and training — using non-UI funds to pay for SEA-specific costs. Most states that offer SEA partner with other relevant agencies in order to provide the required services. They also look to leverage other government funds or grant opportunities to cover costs.

The challenge of eligibility

In addition to cost, the issue of eligibility is another challenge. Federal policy requires that no more than 5% of individuals receiving regular UI benefits in a state may participate in SEA.[20] The legislation also requires for an individual to be eligible for SEA, they must be permanently laid off from their previous job; identified as likely to exhaust UI benefits; and enrolled in self-employment activities including entrepreneurial training, business counseling, and technical assistance. States identify individuals as likely to exhaust benefits through the Working Profiling and Reemployment Services (WPRS). WPRS exists across the entire UI system and requires those that are likely to exhaust benefits to be referred to various types of reemployment services (e.g., orientation, assessment, counseling, placement services, a job search workshop, and referral to training). The use of the WPRS score often acts as a screening mechanism. For instance, depending on how the score was calculated, the WPRS requirement could disqualify potential participants, some of whom would likely benefit from program participation. Additionally, to help manage the course load, some states add eligibility criteria that supplement federal guidance — making it more selective and harder for individuals to access.

Amidst these challenges — and there are many — some states have been able to operationalize successful programs. New York and Oregon are the two best examples in the U.S., and both have operated SEA programs since the 1990s.

OREGON & NEW YORK

As part of the 2012 Middle-Class Tax Relief and Job Creation Act, Congress required DOL to complete an evaluation of the program's economic outcomes for SEA participants and compare them to outcomes of regular UI claimants in the two states with the largest SEA programs — New York & Oregon. DOL produced a final report in January of 2017 and though a bit dated, it remains the most recent analysis of SEA's effectiveness.[21] While no causal inferences could be made from this study, it did find interesting findings that are worth noting for future policy action.

Oregon

In Oregon, to access SEA, individuals must adhere to federal requirements, they must be eligible for UI and must be likely to exhaust benefits. What is different in Oregon is that to apply to the program, individuals must submit a market feasibility worksheet — this helps potential SEA participants understand whether there is enough consumer demand for their business to succeed.[22] After getting accepted into the program, individuals must create a written business plan within 45 days and perform self-employment activities each week to claim their benefit. However, these activities are much more flexible than what is expected in federal guidance. This is a result of Oregon waiving the requirement for entrepreneurial training and business counseling activities. This makes it more affordable for the state to administer and allows individuals to choose the activities that best fit the unique needs of their new business venture.

Oregon's SEA program has helped more than 1,500 Oregonians on UI start their own business.[23] Additionally, the 2017 evaluation study found that once SEA participants got their businesses up and running, they earned similar or higher wages and healthier revenue streams over time than to regular UI claimants in the state.[24]

New York

In New York, the state follows the basic guidelines for an SEA program. Eligible individuals receive benefits while starting their new business.[25] New York requires applicants to submit a defined business plan before being accepted into the program and to maintain their benefits individuals must participate in 20 hours of entrepreneurial training.[26] New York also requires that each SEA participant has a business counselor, but the counselor can be of the individual's choosing. This allows SEA program participants to find leaders in their community or experts in their space to help guide their business development.

Among SEA participants in New York who were approved for the program in 2013 and 2014, DOL surveyed 847 individuals after the fourth quarter from beginning SEA. 17.5% were still operating businesses out of the sample in the state.[27] Additionally, among SEA survey respondents in New York who reported operating businesses, there is a clear trend of increasing revenues, staff size, and wages paid over time. The evaluation study also estimated that from these businesses, the SEA program in New York generated $536,937 in federal income taxes and $140,136 in state income taxes in 2014.[28]

The examples of Oregon and New York demonstrate the potential economic impact of SEA participants when they successfully develop and sustain a business. However, even with the state's relatively good outcomes, the data is old, has gaps, and just represents two out of 50 states — reaching an extremely small subset of the unemployed. It is clear something must change so we can better understand the true impact of SEA and determine the future scale of the program.

POLICY CONSIDERATIONS

While unemployment is low, we still have 5.7 million Americans out of work and looking for ways to provide for themselves and their families.[29] The SEA Program offers an innovative approach to help people transition after job loss — providing services to help them be self-employed. Yet the program served less than 2,000 people last year — making it clear SEA is not making the impact that is needed to help those that are interested and eligible.

This is especially disheartening knowing the impact entrepreneurial opportunities can have — on individuals, on communities, and on the U.S. economy at large. Innovation and entrepreneurship undeniably contribute to economic growth yet traditionally, it has mostly been accessed by those with means and access to capital. To avoid leaving certain Americans out of these opportunities and encouraging more inclusive entrepreneurship, federal and state policymakers should look to our Unemployment Insurance system, specifically the SEA program, to address these challenges and enact the necessary reform.

Because of the limited number of people this program supports and the limited access to strong data on business development and success, PPI is not advocating for the growth of SEA or an increase or decrease in federal investment. What we are asking for is an initial reorganizing that cuts some of the red tape as well as creating a pilot that can help encourage more entrepreneurial activities within the UI system. This can help SEA make a larger impact and policymakers can learn if it is a program worth scaling in the future.

To do this effectively, PPI urges national policymakers to adopt the following reforms:

1. Strike down arbitrary eligibility requirements: The SEA program's eligibility requirements make it hard for individuals to access this program. Between federal mandates and the additional requirements put on by most states, too much time, money, and energy is spent screening claimants. Specifically, the likelihood of exhausting resources measure is arbitrary and people who might be good candidates for the SEA program can be categorically disqualified from the program. This provision should no longer be used to determine eligibility so the program can serve more individuals that are willing and interested in participating.

2. Remove requirements that make SEA too costly for states to administer: On the spending front, states must adhere to the budget-neutrality provision, yet the services that are required by SEA are more costly (i.e., training, business counseling, technical assistance). This makes it difficult for state administrators to offer these services without additional funding and disincentivizes states from participating in the program. However, even though these services are costly they are important — ensuring individuals have the skills and supports needed to succeed as an entrepreneur. PPI recommends federal policy should no longer require states to offer these services and instead, allow them to be provided if states want to and are able. Additionally, to solve cost concerns, SEA can better incentivize and promote cross-agency partnerships so resources can be better leveraged, and programs can be more aligned to make a bigger impact.

3. Create a pilot program to empower UI to support more entrepreneurship: In addition to removing barriers related to participation, PPI recommends a pilot program to empower more entrepreneurial opportunities within our UI system. The pilot would be a $200 million competitive grant program awarded to four states without active programs. This modest investment would provide $50 million per grantee and have a 25% federal match requirement, requiring states to identify how they will pay for 25% of the project with a share of non-federal funds to achieve the purpose of the award – which would allow the total project costs to reach $62.5 million. The pilot would remove some of the requirements (as mentioned above) that exist in SEA to see if increased flexibility can help serve more claimants, increase interest in entrepreneurship from dislocated workers and encourage stronger outcomes, primarily focusing on business development and sustainability. To pay for it the federal government could carve out some of the unattached UI modernization money from the American Rescue Plan (ARP) which was reduced through the Fiscal Responsibility Act of 2023 to $1 billion.[30] This pilot while administered through state UI systems would have to partner with state economic development, workforce, and small-business leaders to encourage alignment, leveraging of resources and greater impact in states.

Eventually, there should be larger changes to the SEA program that allow more Americans experiencing unemployment to access pathways to entrepreneurship. But to implement the right changes, policymakers need a better understanding of the program's efficacy. These small fixes and creation of a pilot program can allow for this understanding while further encouraging states to offer these opportunities and potential claimants to participate.

Lastly, while this brief focuses on the entrepreneurial element of UI, it is worth noting that in addition to SEA, PPI would like to see robust reform to the UI system generally. This program is critical to support workers during times of economic transition, yet unemployment insurance has fallen short in recent years. To unlock the potential of UI to counter future recessions, PPI developed this policy brief, which offers a new tax plan, UI infrastructure modernization, and better wage replacement for workers. These considerations are critical to ensure the UI system is prepared for expected economic disruption, through creating a more modern, sustainable, and responsive system that is truly helping Americans succeed in times of increased financial distress.

CONCLUSION

While UI serves as a crucial policy tool to assist workers during job transitions, it falls short in fostering entrepreneurship. Entrepreneurship plays a vital role in

America's economy, driving business growth, revitalizing regional economies, and maintaining national competitiveness. Yet despite the economic impact, entrepreneurial opportunities are unavailable to most, especially those who are unemployed or face barriers to employment. While the SEA program seeks to change this, its impact has been insufficient.

To promote alternative pathways to employment, immediate and feasible reforms to SEA are imperative to incentivize greater state participation and expand its reach to benefit more individuals. However, broader, long-term reforms are also necessary to establish a more modern UI system that effectively supports all workers in times of economic downturns and transitions. This is critical for policymakers to address to ensure that American workers have every opportunity to improve their circumstances, bring jobs back to communities, and foster a strong and competitive economy. By addressing the lack of entrepreneurial opportunities and providing more avenues for business creation, the U.S. can empower individuals to forge their own paths to success while contributing to the overall prosperity of our nation.

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Taylor Maag is the Director of Workforce Development Policy at PPI. In this role, Taylor leads the New Skills for a New Economy Project, developing policy solutions that strengthen our nation's workforce, ensuring employers have the talent they need to remain competitive and people have the skills and critical supports necessary to succeed in today and tomorrow's economy.

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