

UNEMPLOYMENT COMPENSATION

HEARING

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE
ONE HUNDRED SECOND CONGRESS

FIRST SESSION

APRIL 23, 1991



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CONTENTS

OPENING STATEMENTS

	Page
Moynihan, Hon. Daniel Patrick, a U.S. Senator from New York	1
Breaux, Hon. John, a U.S. Senator from Louisiana	2
Grassley, Hon. Charles E., a U.S. Senator from Iowa	3
Chafee, Hon. John H., a U.S. Senator from Rhode Island	3

COMMITTEE PRESS RELEASE

Senator Bentsen Calls Hearing on Unemployment Compensation, Leadoff Witness to be Labor Secretary Martin	1
---	---

ADMINISTRATION WITNESS

Martin, Hon. Lynn, Secretary of Labor, accompanied by Hon. Roberts Jones, Assistant Secretary for the Employment Training Administration	13
---	----

CONGRESSIONAL WITNESSES

Sarbanes, Hon. Paul S., a U.S. Senator from Maryland	4
Levin, Hon. Sander M., a U.S. Representative from Michigan	19

PUBLIC WITNESSES

Snider, Anthony, a Pennsylvania taxpayer	25
Cunningham, William J., legislative representative, AFL-CIO, Washington, DC	27
Reuther, Alan, associate general counsel, International Union, United Auto- mobile, Aerospace, Agricultural Implement Workers of America (UAW), Washington, DC	31
Brooks, Keith, coordinator, New York Unemployed Committee	34
Thodis, John G., president and chief executive officer, the Michigan Manufac- turers Association, Lansing, MI, representing the National Association of Manufacturers	35
Motley, John J., III, vice president for Federal governmental relations, Na- tional Federation of Independent Business, Washington, DC	39
Grossenbacher, William D., administrator, Texas Employment Commission, Austin, TX, representing the Interstate Conference of Employment Security Agencies, accompanied by Cherly Templeman, unemployment insurance director	43
Burtless, Gary, Ph.D., senior fellow, the Brookings Institution, Washington, DC	44
Topel, Robert H., Ph.D., professor of business economics and industrial rela- tions, University of Chicago Graduate School of Business, Chicago, IL	47

ALPHABETICAL LISTING AND APPENDIX MATERIAL SUBMITTED

Breaux, Hon. John: Opening statement	2
Brooks, Keith: Testimony	34
Prepared statement	53
Burtless, Gary, Ph.D.: Testimony	44
Prepared statement	54

IV

	Page
Chafee, Hon. John H.:	
Opening statement.....	3
Cunningham, William J.:	
Testimony	27
Prepared statement with appendixes.....	64
Grassley, Hon. Charles E.:	
Opening statement.....	3
Grossenbacher, William D.:	
Testimony	43
Prepared statement	72
Levin, Hon. Sander M.:	
Testimony	19
Prepared statement	75
Martin, Hon. Lynn:	
Testimony	13
Prepared statement	78
Motley, John J., III:	
Testimony	39
Prepared statement	80
Moynihn, Hon. Daniel Patrick:	
Opening statement.....	1
Reuther, Alan:	
Testimony	31
Prepared statement with exhibits.....	85
Sarbanes, Hon. Paul S.:	
Testimony	4
Prepared statement	97
Snider, Anthony:	
Testimony	25
Thodis, John G.:	
Testimony	35
Prepared statement	103
Topel, Robert H., Ph.D.:	
Testimony	47
Prepared statement	106

COMMUNICATIONS

American Federation of State, County and Municipal Employees	112
State of Illinois, joint statement of various officials	114
Terry, Patricia A.....	116
United Mine Workers of America	116
U.S. Chamber of Commerce.....	118

UNEMPLOYMENT COMPENSATION

TUESDAY, APRIL 23, 1991

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:03 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Daniel Patrick Moynihan presiding.

Also present: Senators Breaux, Packwood, Chafee, and Grassley.
[The press release announcing the hearing follows:]

[Press Release No. H-14, April 16, 1991]

SENATOR BENTSEN CALLS HEARING ON UNEMPLOYMENT COMPENSATION, LEADOFF WITNESS TO BE LABOR SECRETARY MARTIN

WASHINGTON, DC—Senator Lloyd Bentsen, Chairman of the Senate Finance Committee, announced a hearing on America's unemployment compensation program.

Bentsen (D., Texas) said the leadoff witness will be Secretary of Labor Lynn Martin.

The hearing will be *Tuesday, April 23, 1991, at 10 a.m.*, in Room SD-215 of the Dirksen Senate Office Building.

"I want to take a fresh look at our unemployment compensation program in light of America's rising unemployment rate," Bentsen said.

"We saw unemployment rise from 6.2 percent in January to 6.8 percent in March, and in the coming months we can expect it to continue rising. Almost 500,000 American workers lost their jobs in February and March alone. We need to consider whether, against this backdrop of rising unemployment, the unemployment compensation program is meeting the needs of the people who must depend on it," Bentsen said.

Bentsen said he wants to learn more about whether the program is meeting its traditional objectives of providing income support for people who lose their jobs and stimulating the economy, whether the states' unemployment compensation trust funds have enough funds to pay benefits during a deep recession, whether the states have enough funds to administer the program for both fiscal years 1991 and 1992, and whether the extended benefit program needs to be changed to make it accessible to more workers.

OPENING STATEMENT OF HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM NEW YORK

Senator MOYNIHAN. A very good morning to you, our guests and our distinguished witnesses; and of course, first of all Hon. Paul Sarbanes, U.S. Senator from Maryland, who will begin this hearing of the Senate Committee on Finance on the subject of unemployment compensation.

This is an old matter for our committee, but one which we address in a new circumstance. It may not be generally remembered—and not everybody was around to do so—but the unemployment compensation program began with the Social Security Act of 1935.

That was a general provision, a comprehensive provision, the most important I suppose in our history, which provides insurance against an interruption in income.

Typcially, we think of Social Security as providing retirement income for workers who have left the work force owing to age.

But we also have disability benefits for those who are disabled and can't work during the normal working years and unemployment compensation for persons who lose their work or cannot find work, particularly when, for example, there is a recession, as there is today.

Over the years, this has been a stable system, operated jointly by the Federal Government and the State employment offices.

I can recall 30 years ago, I became Assistant Secretary of Labor for President Kennedy's administration. There were many issues that pressed us in those days, but the one system that seemed to be in place and working well and responding nicely to changes in the economic climate was unemployment compensation.

Thirty years later, this is different. We look up and we find that of all the insurance systems set in place by the Social Security Act of 1935, none has been allowed to deteriorate, so much as unemployment compensation.

In the 1970's, upwards up 75 percent of the unemployed would find themselves covered in a time of economic downturn. Two decades later, that has dropped to 35 percent or something like that, a situation never intended by this committee or Congress.

But it has happened. It is part of a general decline in institutions and arrangements that troubles us all.

I don't know how anybody else on the committee feels, but I for one really felt badly when I learned—as we all did last week—that in 1990, for the first time in the history of our Nation, a decennial census was worse than its predecessor.

And after two centuries of getting a better census every 10 years, learning more about how to do the job well; we did it worse. And now, we don't know how legitimate are the numbers on which we allocate the most important thing we have in our country—representation.

I don't want to speak any longer as we have very able members of the committee here and then the distinguished witnesses. I believe, Senator Breaux, you were here first, and perhaps you would like to make a comment?

OPENING STATEMENT OF HON. JOHN BREAU, A U.S. SENATOR FROM LOUISIANA

Senator BREAU. I think you have said it, Mr. Chairman. I am anxious to hear the witnesses. My own State has some of the highest unemployment numbers over the last decade in the country. We also have the lowest average weekly unemployment benefits in the Nation. And I am anxious to hear what the witnesses have to say. Thank you, Mr. Chairman.

Senator MOYNIHAN. You are very kind, sir. Senator Grassley?

**OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S.
SENATOR FROM IOWA**

Senator GRASSLEY. Mr. Chairman, thank you for the opportunity to consider this issue of unemployment compensation and particularly those problems that affect the unemployment insurance fund. I have been told that around twelve States' unemployment insurance funds are in trouble and that 10 of those are in very serious trouble.

Now, fortunately for my State, it is not that way. My State of Iowa has the 15th healthiest fund in the Nation. We have around \$525 million in reserve.

However, with growing unemployment, we can't take anything for granted; and hence, I think it is very important that you hold this hearing because, even in my State, just since last October, Iowa's unemployment rate has risen from 3.9 percent to 5.9 percent.

At the same time, the Unemployment Insurance Administration account formula, I think, is biased against low population, low unemployment States, such as my State. In fact, Iowa gets back less than 50 percent of the amount of taxes paid into the administrative fund. Last year, the Federal Government returned only \$25 million out of \$54 million paid by Iowa employers.

I look forward to considering how the Nation's unemployment insurance fund can be used more effectively and applied more fairly. I thank each of the witnesses that are going to participate here today.

Senator MOYNIHAN. We thank you, Senator. Senator Chafee, good morning, sir.

Senator CHAFEE. Thank you, Mr. Chairman.

**OPENING STATEMENT OF HON. JOHN H. CHAFEE, A U.S. SENATOR
FROM RHODE ISLAND**

Senator CHAFEE. Mr. Chairman, first of all, I see that we are going to have with us Secretary Lynn Martin, which is very nice; this is the first time she has appeared before us, which makes it a pleasure for all of us.

Mr. Chairman, my State has an 8.3 percent unemployment rate right now. So, we are naturally deeply concerned about the unemployment compensation system.

It is my understanding that there are many holes in the so-called safety net that unemployment compensation is meant to provide for. So, we look forward to hearing the testimony today and are grateful for those of our witnesses who are appearing. Thank you.

Senator MOYNIHAN. We thank you, sir, and I certainly want to acknowledge the presence of Secretary Martin. Yesterday, I presided at the Committee on Foreign Relations at which Secretary Martin spoke and here we are this morning. Senator Packwood?

Senator PACKWOOD. No statement, Mr. Chairman.

Senator MOYNIHAN. In the interest of brevity and directness, we go to our good friend and distinguished colleague, Senator Sarbanes. Good morning, sir.

**STATEMENT OF HON. PAUL S. SARBANES, A U.S. SENATOR FROM
MARYLAND**

Senator SARBANES. Thank you very much, Mr. Chairman. Mr. Chairman and members of the committee, I appreciate this opportunity to testify on the problems of the unemployment insurance system during this recession.

Mr. Chairman, if I could have my full statement included in the record?

Senator MOYNIHAN. It will be, and you proceed exactly like you wish.

Senator SARBANES. I know the committee has an extended agenda.

Senator MOYNIHAN. We do. Would you mind? I omitted to make the point that you are Chairman of the Joint Economic Committee and appearing in that capacity.

Senator SARBANES. Thank you, Mr. Chairman. In fact, the Joint Economic Committee, at the beginning of this Congress, in their course of reviewing the economic situation, considered the unemployment insurance system as it related to the recession and how well it was serving its countercyclical purposes.

Mr. Chairman, I think it is clear that the unemployment insurance system is not doing the job of providing stimulus to the economy in alleviating hardship in depressed areas. Therefore, I think we need to consider in the Congress going back to the precedent of previous recessions in extending unemployment insurance benefits in economically distressed States.

I would like, first of all, to address the notion that this is a short and shallow recession; and I want to take just a moment to set the context in which we are dealing with this issue.

There is reason to believe, despite these predictions, that this may develop into a more serious recession than is generally perceived; and in fact, I heard coming in this morning on the radio that the new orders for durable goods were down 6.2 percent last month, the sharpest drop since late 1987.

If we date the end of the last business cycle expansion as August of last year, we have 7 months of recession to examine. In terms of lost jobs, output, and income, this recession tracks the average of the initial 7 months of post-war recessions; and the average length of recessions in the post-war period has been just under a year. So, these predictions of a quick upturn have to be viewed in that context.

Over the last 7 months, businesses have reported a decline of 1.2 percent in payroll employment, exactly the same decline as occurred during the first 7 months of the average post-war recession. That is reflected in this chart. You can see that, while they don't exactly track, the two lines are roughly at about the same point now. In the last 7 months, 1.3 million payroll jobs have been lost compared to 1.2 million lost in the first 7 months of the very deep 1981-1982 recession. That was the worst recession we had experienced since the 1930's.

Likewise, this recession has been every bit as serious as those of the past in terms of the number of workers laid off from their jobs. The fraction of the labor force who have lost their jobs and are still

looking for work has risen from 2.8 percent in August to 3.8 percent today.

Senator MOYNIHAN. Officer, would you please close the door? There are persons who want to get in, and the room will be filled with as many as can be accommodated; but we will not have demonstrations. Excuse me, Senator Sarbanes, would you proceed, please?

Senator SARBANES. That is a 1 percent point increase compared to 0.9 in the last four recessions. In this graph you can see job losers; while they ran under previous recessions, they now have in fact crossed that line in terms of the number of job losers.

The two most widely watched indicators of the recession are given more rose-colored impressions of this downturn. One is the unemployment rate, which has gone from 5.6 percent to 6.8 percent. The change in the rate, it must be understood, is a misleading guide to the severity of the recession because it reflects growth in the labor force as well as job losses. The labor force has been growing slowly in recent years. So, the ranks of the unemployed are not being swelled by new entrants. In other words, if we had had labor force entry as we have had in past years, the unemployment rate today would be at 7.6 percent instead of 6.8 percent. Now, the demographics are such that we don't have that labor force increase. Therefore, the rate figure has not gone up; but the amount of the increase, going from 5.6 to 6.8 percent, roughly corresponds to the amount of increase in the previous recessions.

The final point I want to make is that there is no assurance of an immediate turnaround, even though the forecasters' consensus calls for the recession to end soon. This can be seen in this next chart, which talks about the consensus forecast at the time of the 1981-1982 recession.

The red line traces the actual unemployment rate, which rose from a quarterly average of 7.2 percent to 10.7 percent by the end of the recession. Yet at virtually every point during the long climb of the unemployment rate, the consensus forecast was for an imminent improvement; and that is the green line. This shows you what the 50 forecasters—the blue chip forecasters—were all predicting as we moved through the last recession. And of course, what this shows is that they invariably were underestimating the severity of the recession which was taking place.

Now, let me just turn very quickly to the unemployment insurance system itself, recognizing, as I think this very short exposition does, that the recession we are confronting may linger for some time yet and, in fact, be deeper and longer than the forecasts. In any event, we must provide for that possibility; and a strengthened unemployment insurance system, in my judgment, is the best way to do it.

As a quick targeted program of income replacement for jobless workers, the unemployment insurance system is ideally situated to counteract the effects of recession. Funds are spent immediately without lag of bureaucratic or political decisionmaking. The funds are automatically spent in the locations of greatest distress, which is a very important point. You don't draw it unless you are unemployed; and therefore, by definition, it goes to the places where it is needed the most.

The unemployment insurance system is not performing its stabilization role as well during this recession as it has done in the past. From the perspective of workers who have lost their jobs and remain unemployed, the unemployment insurance system is replacing the income lost during this recession only one-half to two-thirds as well as in previous recessions. Figure 4 shows that the income replacement ratio anticipated for this recession is much lower than the last four recessions. This is primarily because of the failure to have an extended benefits program that kicks in at the appropriate time. As you can see from this chart, this is this recession; and this compares the replacement of lost income to the worker in the recession through the unemployment insurance system. The dark part is the regular program; the shaded part is the extended program, which we have made very little use of in this recession.

So, both the regular program is less, as you can see; and the extended program has not kicked in. If the current recession lasts longer than the Administration forecasts, this replacement ratio will decline further because more workers will exhaust their unemployment insurance benefits.

Longer term benefits are now projected to make up only 4 percent of the rise, as seen by this very tiny red shaded part in the final figure. This is because the trigger for applying extended benefits programs has been made much more difficult; and of course, we no longer have a supplemental program which supported incomes in the last recession.

The number of workers who are unemployed longer than 6 months and exhaust their benefits rises sharply during a recession, and continues to rise for several months after it ends. During the first 7 months of this recession, 1.5 million have exhausted their unemployment insurance benefits, a 28-percent rise over the 7 months of the previous year. The administration projects that 3.3 million workers will exhaust their regular unemployment insurance benefits in fiscal year 1992, an increase of 1.4 million over fiscal year 1989.

Unemployment insurance, as we know, provides income support to workers for a reasonable period to find a new job. In normal times, the States set a maximum income-support period of 26 weeks. In a recession, it is very difficult, and often impossible, to find a job within 26 weeks; and over the last 25 years, the Congress and the President have recognized in each of the previous recessions extending for more than 6 months the need to enact temporary provisions to lengthen the period for receiving unemployment insurance benefits, especially for States in the most depressed condition.

In addition, the law has in it a permanent provision for extended benefits of up to an additional 13 weeks during particularly adverse conditions. I submit to you that the formula for triggering those benefits needs to be examined by this committee. It is now set in such a way that, in some States, the actual unemployment rate would have to reach 15 percent before the extended benefit trigger would be reached. In fact, since the enactment of the extended benefit program in 1970, the level of total unemployment needed to trigger it in has been effectively raised by roughly 40 percent.

This is shown, Mr. Chairman, by the fact that the number of unemployment insurance recipients, which until 1970 closely tracked the number of job losers—in other words, unemployed who had involuntarily lost their last job—no longer does so. And that is reflected in this chart. This line is the job losers; this line is unemployment insurance recipients. As you can see, they closely tracked one another. But now, a gap has grown between the job losers and the unemployment insurance recipients.

Senator MOYNIHAN. And that appears to begin with the 1981-1982 recession. Is that about right?

Senator SARBANES. That is right.

Senator MOYNIHAN. It is a big difference.

Senator SARBANES. That is when you have the very sharp difference.

Senator MOYNIHAN. Yes. There was one curve from 1967 to 1980; and then, it ceases to be.

Senator SARBANES. That is right, essentially.

Senator MOYNIHAN. Yes.

Senator SARBANES. That is correct. So, the first recommendation I have to make very strongly is that the trigger mechanism—

Senator CHAFEE. Mr. Chairman, I will tell you what I would be interested in. Why does that big difference between job losers and unemployment insurance recipients exist? What caused that situation to occur? As best I can read your chart from here, it started occurring about 1978, didn't it? And then, this great gap appeared in the 1982 recession.

Why is that? Did we change something, or what occurred?

Senator SARBANES. Two things happened. We changed the law in the Congress to some extent, making it more difficult for job losers to obtain unemployment insurance benefits; and the States, which ran large deficits in their funds in 1981-1982 recession, tightened up the requirements in order to try to move back out of that position.

That is not a bad approach, or not an utterly illogical approach. If you are operating in an environment that is not in a downturn, if you are sort of moving out of it, you get something of a gap growing, although I think it is too much in any event. But of course, when you go back into a downturn, as we now are into, that situation then is exacerbated both in terms of the human suffering, since they are not able to find other jobs—they are not operating in an economic environment in which other jobs are available—and also as a countercyclical measure, you are not offsetting the income loss. Therefore, in a sense, you are helping to contribute to the downturn because you are not sustaining purchasing power.

Senator CHAFEE. But I recall some of the changes we made in 1981 or thereabouts; and as I recall they mostly dealt with whether so-called casual employees or summer employees would be entitled to workmen's compensation.

Now, there may have been other changes; but it seemed to me—and somebody can correct me if I am wrong here—but it seemed to me that what we were dealing with in those changes was the college student who would work in the summer X weeks and then was unemployed for a variety of reasons, one of which may be he went back to college.

But in any event, we said he couldn't collect; that was a very restricted group, and I am not sure we are all wrong. Were there other changes? Am I missing something? Because I must say, it is a very dramatic gap.

Senator **SARBANES**. Yes. A number of States tightened up their eligibility requirements, well beyond what you are describing. I think actually, at the Federal level, we tightened them up beyond what you have just described, although what you have just described was part of it.

And at the State level they also tightened it up. So, it was more difficult to be eligible for unemployment insurance, and you get this gap between the job losers and the people collecting unemployment insurance.

Now, if you are in an economy that has some expansion to it, it is not as serious a problem because people may be able then to find other work. They lose their job; they are not entitled to unemployment insurance, but they may be able to find other employment.

But when you are in a downturn, as we now find ourselves, it becomes a crisis situation; and I think that is what has developed.

The extended benefit trigger that was enacted—just to give you an example—after the sharp decline in oil prices in 1986, unemployment rose above 9 percent in the major oil producing States. Oklahoma and Texas never were able to trigger the extended benefit program, even though they had what anyone would regard as high unemployment levels in their States.

Senator **BREAUX**. But Louisiana did.

Senator **SARBANES**. I think Rhode Island has just triggered it recently, finally. I think the level in Rhode Island was sufficient to trigger the extended benefits. Louisiana triggered the benefits on; but then, they triggered them off while their unemployment rate was still at 10 percent. The extended benefit trigger is not working; and I think it needs to be recalibrated.

Secondly, the failure of the unemployment insurance to act as an effective countercyclical tool can also be seen in the budget numbers for the Extended Benefits Trust Fund. There is an Extended Benefits Trust Fund. According to the Office of Management of Budget, this fund began fiscal year 1991 with \$7.2 billion. It is projected to receive another \$700 million in taxes and \$600 million in accrued interest during fiscal year 1991. During this recession year, however, the fund will pay out only \$140 million for benefits, one-fifth of the taxes taken in. In other words, you have the Extended Benefits Trust Fund that is actually building up a surplus at a time when they should be drawing down past surpluses to fund adequate income replacement for laid-off workers.

If one regards this recession as a consequence and needing to be addressed, it makes absolutely no sense that the payments into the Extended Benefits Trust Fund should be significantly exceeding the payments out of the fund.

Senator **MOYNIHAN**. Is there any historical equivalent of this? It is astounding that we are building up a surplus in the Extended Benefits Trust Fund at a time when there is a sharp rise in unemployment due to the recession.

Senator SARBANES. Mr. Chairman, I haven't run those figures, but I think it is correct to say that in past recessions, we drew down on those funds, just as we should do in a recession.

Senator MOYNIHAN. Rather than build up funds.

Senator SARBANES. That is right.

Senator MOYNIHAN. It is a rainy day fund.

Senator SARBANES. It makes no sense to be building up the fund even further in the midst of a recession.

Now, part of this issue—a minor part of it—was joined when we had the fight—actually, it wasn't really a fight—in the Congress; and the Administration in the end was also amenable to providing administrative funding dollars for the unemployment insurance fund to cover the cyclical increases in the workload.

As you will recall, the claims had gone up, but the administrative funds with which to handle the claims were not being provided. That led to a virtual breakdown in administration in some States, people getting their checks 6 to eight weeks after they filed the claim instead of 1 to 2 weeks after they filed the claim. There were long lines, people unable to file their claims, a really very difficult situation in some States. We provided additional funding as an emergency under the Budget Act, outside of the spending caps, which the Administration recognized.

It makes no sense to have a program where benefits and claims expand automatically with a deteriorating labor market, but the administrative funds needed to process those claims remain frozen. In fact, the amount of money in the fund for administrative costs was well above the ceiling. In other words, we were building up an excess there as well.

We need to address how to provide, in a more automatic way, for those administrative costs in the course of revising the unemployment insurance system. That raises some difficult questions of jurisdiction between this committee and the Appropriations Committee, but I think it is important to try to work that out.

Let me simply close, Mr. Chairman, by again observing that we have been experiencing a serious recession in terms of the number of workers who have lost their jobs and are looking for a new job. Over the last 7 months, unemployment has fallen as fast as the average rate for the first 7 months of the post-war recession.

I think we need to strengthen this unemployment insurance system, which really is our first line of defense against the recession. It is our most immediately effective countercyclical tool. It addresses very important humanitarian considerations in terms of the hardships experienced by workers and their families.

I urge the committee, one, to reexamine the trigger mechanism for applying extended benefits, to consider a supplemental insurance program, as we have done in past years, to provide in a more automatic way for the administrative funds necessary to administer the system. The employers, after all, are paying these funds into the system, and they have been willing to carry the tax burden on the assumption that, in an economic downturn, the unemployment insurance will help to meet the problems which their workers confront in terms of providing for their family, and also that it will provide something of a support in order to keep the economy from going down further. We have heard from employers

who have complained about the failure of the system to use the funds they have paid in for this purpose.

I very much commend the committee for scheduling these hearings. My own view is that we need to take action. If we take action and the recession proves to be short and shallow, then the benefits will never be drawn upon.

That is one of the advantages of this system; you only draw on the benefits if, in fact, you are unemployed. If we strengthen the system, and then the recession turns out to be short and shallow, those strengthened benefits will not be called upon because, in effect, the economy will have turned up.

If the economy doesn't turn up, then we need those extended benefits; we need that strengthened system, and then it will be called upon, and it will direct the money. Unlike most other programs, this program directs the money 100 percent to the people who need it because, by definition, it directs the money to the unemployed.

Thank you very much, Mr. Chairman.

Senator MOYNIHAN. We thank you, sir. I wonder if you could keep that chart up just one more moment? Mr. Chairman, you present to us a very powerful proposition, which is that the fiscal year 1991 began with \$7.2 billion in the fund and then, in the course of the fiscal year, will receive \$700 million additional; that is out of the economy. And then, there is \$600 million in interest.

But it will only spend \$140 million. Of course, the Federal Government getting the money will spend it for other reasons than the trust fund indicates. Are we dealing here, sir, with a situation where trust funds are being used for other purposes than they were designed?

We encounter this in the highway system; we encounter this in the Social Security System; we encounter this in unemployment. It seems to be a pattern. I don't want to suggest how you respond; we want your views, not your confirmation.

Senator SARBANES. Well, yes, we are running up balances in these trust funds far in excess of what is required as the sort of working minimum. And we are doing it at the very time when we ought to be drawing out of the trust fund, not putting into the trust fund.

Senator MOYNIHAN. That is why we created the trust fund.

Senator SARBANES. That is why we created the trust fund, and that is why we built up the balances so that, when we go into an economic downturn and we begin to get this rise in unemployment, we are able to compensate the workers.

Let me emphasize again: This recession, in terms of the number of people who have lost their jobs, tracks previous recessions. Now, the unemployment rate is not as high as in previous recessions; but that is because the number of new entrants into the labor market has decreased because of demographic changes. But the number of people losing their jobs and, therefore, needing unemployment insurance tracks the previous recessions. In that respect, this recession is not short and shallow compared with past recessions.

Senator MOYNIHAN. A very powerful remark; and I will just make a comment to emphasize what you have said. The demography, that is the number of people born 18 years ago and coming

into the labor force—18, 19, 20—is such that, in the 1990's, there will be a tight labor force. The entrance will be about half the rate of the 1980's.

And of course, those people typically have high unemployment rates. You are unemployed if you are looking for work, even if you have never had work. But in terms of this recession, the number of people who have lost their jobs because their firms have gone out of business, is very like those of the previous recessions.

Senator SARBANES. There is the chart.

Senator MOYNIHAN. There it is.

Senator SARBANES. Those are job losers as a percent of the labor force, and this is in this recession; and this is in past recessions.

Senator MOYNIHAN. And that unemployment compensation explicitly had in mind the people who got laid off—people with a solid attachment to the work force, who, through no fault of their own are out of work.

This insurance is not only for them, but for the economy itself—to maintain demand. If I have your numbers right, we are taking \$700 million away from employers and only putting \$140 million back into the economy as benefits.

Senator SARBANES. That is for the extended benefits.

Senator MOYNIHAN. Yes.

Senator SARBANES. That part of the trust fund.

Senator MOYNIHAN. Yes.

Senator SARBANES. Not for the entire trust fund, but for the extended benefits part of the trust fund. That is correct.

Senator MOYNIHAN. It makes no sense.

Senator SARBANES. Which underscores how difficult this trigger is that we have now established for kicking in extended benefits. I think the trigger is unworkable, and we need to develop a new measurement for triggering in the extended benefits because, as I pointed out, in Texas and Oklahoma, which had high unemployment levels, they never in fact triggered in the extended benefits. In Louisiana, they triggered them in; but then, they triggered them off when they had an unemployment rate still at 10 percent—a State unemployment rate still at 10 percent. Something is wrong with that mechanism, when you are looking at those levels.

Senator MOYNIHAN. I think you make your case, sir; and it may be useful just to record that the Joint Economic Committee was created by the Employment Act of 1946.

Senator SARBANES. That is correct.

Senator MOYNIHAN. And here you are testifying. Senator Chafee?

Senator CHAFEE. Thank you, Mr. Chairman. I think it is well to point out that, as the distinguished chairman has mentioned, under the Extended Benefits Program, it is hard to qualify currently.

What he is suggesting is that you make it easier to qualify. I would then point out as a supplement to that, and having worked with this as a Governor, I know how quickly this does, the withdrawals under that fund will accelerate at a dramatic pace.

Senator CHAFEE. And that fund will disappear. And so, I believe every proponent of change in connection with the current system is suggesting an increased tax, an increased tax through a broadened

base. In other words, now it is the employer pays X percent on—what is it?—the first \$3,000.00.

Senator SARBANES. I believe it is that.

Senator MOYNIHAN. \$7,900.00 I think.

Senator SARBANES. \$7,000.00.

Senator CHAFEE. \$7,000.00. And all of the people who have come in with suggestions have suggested that that amount be increased rather dramatically. I have here—and some of you will have to correct me—the Downey bill would increase the base by nearly 800 percent.

So, I think we have got to bear in mind what that is going to do for the chances of a recovery; and these taxes, as we all know, are paid by the employer. They are not paid by employees.

So, if you put that kind of a tax on an employer, what is it going to do for the chances of a recovery? Obviously, that has got to be in our minds as we debate this matter.

Senator SARBANES. Yes. Well, you have different stages of that, and you have to make your calculations as you go along. I would submit to you that there is sufficient money in the trust funds now that you can make some changes and make a somewhat more generous insurance system without having increased taxes.

Now, if you make changes even further along, then you may have to provide revenues. It all depends how far you go in terms of strengthening the underlying program. You can make it somewhat easier to kick in extended benefits and probably not have to resort to taxes. If you go further along that path, you may in fact have to find additional revenues; but that is all a matter of calculating very carefully how much money you have in, what your payout rate is going to be.

At the moment, it is very clear that in comparison with past recessions, first of all, we are only providing one-half to two-thirds of the income replacement. First of all, it is harder to get unemployment insurance now. So, many people who would have gotten it are not getting it at all. Secondly, if they do get it, the amount of income that is replaced is significantly less than in past recessions.

Senator CHAFEE. But that depends on the State. Each State sets its benefits. At the national average, that may be true, but you would have to look at the respective States.

Senator SARBANES. Yes, but I think it is true in almost every State, if you check it out.

Thirdly, the time period for which you get the benefits is shorter in most instances because it is the basic 26 weeks because the extended benefits have not kicked in; and there is no supplemental benefit program now. We previously had a 13 week extended benefit program, a 13 week supplemental benefit program, which made possible 52 weeks. Previous recessions, as I said, have averaged in the post-war period just under a year as the length of the recession period.

If this recession proves out not to be short and shallow and parallels past recessions—approximately a year's time—many people, even if they could get the benefits and even if they got the benefits replacing a reduced level of income, will exhaust them and no longer be eligible at a much earlier period of time.

Senator CHAFEE. Thank you, Mr. Chairman.

Senator MOYNIHAN. Thank you, Senator. Senator Grassley?

Senator GRASSLEY. Senator, I would like to ask you a question about something that has come up on the taxing of unemployment insurance. A witness that is going to be testifying in a later panel says that he suspects that the taxation of unemployment benefits deters some unemployed workers from applying for benefits.

My first point is whether or not you agree; and even with taxation, it seems to me that it is so obvious that a worker is going to have a lot more with unemployment benefits than without them. So, why would a worker be deterred in applying for them because of the issue of taxation of the benefits?

Senator SARBANES. I don't know the answer to that question. I don't know whether, in fact, workers are deterred because they are taxed.

Senator GRASSLEY. Well, this will be the testimony of this witness.

Senator SARBANES. I am sure they will develop the reasons for that. I do know that on the taxation of the benefits, there was not an adjustment upwards in the amount of the benefits to take into account the fact that they were being taxed at the time that they were made taxable.

The net result was to reduce for people receiving the benefits the effect of purchasing power. In other words, at the time that benefits were made taxable, you didn't get an adjustment upward of benefits to take that into account. Workers on unemployment in a sense are receiving less real purchasing power because of the taxing of the benefits.

Senator GRASSLEY. Thank you, Mr. Chairman.

Senator MOYNIHAN. Thank you. Mr. Chairman, Senator Sarbanes, we thank you very much, sir. You have given us an assignment that cannot be more explicit. We thank you for your data. We will look to you for your assessment of how we do.

Senator SARBANES. Thank you very much, Mr. Chairman.

SENATOR MOYNIHAN. And we thank your staff for so ably presenting all those charts.

Senator SARBANES. Thank you.

[The prepared statement of Senator Sarbanes appears in the appendix.]

Senator MOYNIHAN. And now, owing to our difficulty in scheduling, Madam Secretary, you have been here waiting very patiently from the beginning; and I know you are on a tight schedule. Representative Levin has been kind enough to defer. So, would you come forward directly and let us hear from you. We have Secretary Lynn Martin, our distinguished Secretary of Labor; and would you perhaps introduce your associate who is with you?

STATEMENT OF HON. LYNN MARTIN, SECRETARY OF LABOR, ACCOMPANIED BY HON. ROBERTS JONES, ASSISTANT SECRETARY FOR THE EMPLOYMENT TRAINING ADMINISTRATION

Secretary MARTIN. Yes, thank you, Mr. Chairman. It is a pleasure to be here; and joining me is Assistant Secretary Roberts Jones of the Department of Labor to answer questions that you may have.

Senator MOYNIHAN. Good morning, Mr. Jones, and the committee welcomes you.

Secretary JONES. Thank you, Mr. Chairman.

Secretary MARTIN. We have got to stop meeting like this, Mr. Chairman. People will talk. [Laughter.]

Senator MOYNIHAN. Yes.

Secretary MARTIN. It is a pleasure to be before you today; and, Mr. Chairman, I understand you are not aware that Chairman Bentsen and I had worked this out. As you know, I am appearing before a lot of committees; and I think it is worthwhile for me. It certainly was interesting to listen to Senator Sarbanes.

I will have to tell you we had agreed that I would be out of here by 11:00 o'clock; and so, if I leave, it is not because of any lack of desire on my part to spend additional time with you.

Senator MOYNIHAN. We understand. The sooner you start, the more we will learn.

Secretary MARTIN. Having represented the city with one of the highest unemployment rates in the Nation during the 1982 recession, I assure you I am exceedingly sensitive to the profound way that unemployment affects not just the individual's life, but a family's life as well.

The Labor Department is and will remain committed to seeing that the programs it oversees are operated as effectively and humanely as possible.

Some Members of Congress have suggested that the Extended Benefit Program be expanded and administrative funding increased. Such changes to the program are hardly reasonable to even discuss when the other body has just provided \$400 million less than needed to administer the current program in fiscal year 1992.

The House budget resolution figures are totally unreasonable, but were passed at the same time that the House is calling for more money in the program. I am sure that increased funds may well be the subject of Congressman Levin's testimony; and yet, I am writing Congress about the severely reduced mark from the current presidential request.

The administration believes that the unemployment insurance program is continuing to effectively perform its prescribed and targeted mission to provide temporary, partial wage replacement to experienced workers who become unemployed through no fault of his or her own and encouraging an early return to work.

As to the outlook for the current fiscal year, budget outlays for the UI benefit payments are expected to be \$25 billion in fiscal year 1991, up from \$17 billion in fiscal year 1990. The number of those receiving benefits is projected to rise from 8.3 million in 1990 to 11 million in 1991.

It is clear from the data that, over the next year, the program is expected to experience a sharp increase in activity; but I am just hopeful that the Senate will repair that damage.

Senator MOYNIHAN. This is to the administrative funds that you need to send out the checks.

Secretary MARTIN. Yes, that is right. Right now. The money for UI administration fiscal year 1992.

So, while some may be talking about "let's give more," and expanding the program, it seems to me that it just sort of staggers the imagination that the House voted to provide less money than the administration required for administering the current UI program. And sometimes, it is the same people taking both positions, which I find really remarkable; but I would hope that the Senate, in its wisdom, will repair that damage.

With respect to financing these added outlays, the unemployment insurance program is more solvent now than at any time since 1973. State accounts totaled \$40 billion at the end of 1990.

The vast majority of State accounts have sufficient funds to pay for the increase in the number of claims, although we do estimate that from four to six States may have to borrow funds during the next 2 years to cover costs.

In general, while current high outlays will reduce balances over the next several years, the trust fund will remain solvent.

Very quickly, let me focus on some other issues that you have talked about.

The EB program, the gap between the total number of unemployed workers and those collecting benefits, and administrative financing.

The Extended Benefits Program is designed to provide benefits to eligible individuals when unemployment in a State is relatively high. Indeed, the Extended Benefits Program is responding to the recent increases in insured unemployment in precisely the manner to which it was designed, with nine States now paying benefits.

While this number is smaller than in past recessions, it reflects the lower number of claimants expected during this recession, which will serve to reduce the need for extended benefits.

The Administration believes the Extended Benefits Program is operating effectively, and revisions will not be necessary; and this gets us to the gap.

During the past few years, concern has been expressed about the difference between the total number of employed individuals and those who collect benefits, referred to as "the gap." It is important to remember that some of the gap is normal because UI benefits are generally paid to workers with substantial labor force attachment, who have lost their jobs through no fault of their own.

A number of studies have determined that there isn't a single explanation for the gap. Some of the factors included changes in the very economic structure of the Nation; the fact that some individuals who are eligible do not apply, and changes in the demographic makeup of the labor force.

And lastly, administrative financing. The administrative financing of the UI program is meant to provide stable and adequate funding for the cost of UI administration to the States. We are well aware that the current recession has put an added strain on the delivery of services to unemployment claimants and that some claimants have experienced difficulties in having their claims processed.

The \$150 million that was included for UI administration in the supplemental appropriations bill will increase the total amount available for fiscal year 1991 to \$2.1 billion. We do believe this

amount is adequate. And if you want to ask some questions about specific States, I will be happy to answer.

I should add briefly that I am going to be writing a few of the Governors who have hiring freezes on, which is affecting the time it takes for claims to be processed. Now, remembering that they are totally reimbursed, we would hope that the money which is there in the account can be used so that we can cut down processing time in a few of those States where there are budgeting problems.

A few other States have internal mechanical problems—one with a new computer system, one with a system that remains manual in an age where that just really slows up claims. We are helping those States.

Senator MOYNIHAN. The name of the States?

Secretary MARTIN. Michigan in the latter one, and the Governor there has asked for help; and we are giving it. In the other case, New Hampshire, I think, is having some problems with the new computer system.

So, there are some specifics that no national bill would cover; but in the one, we hope the problem will be rectified, and in the other, the Governor and his new commissioner have asked for the help of the department and they are receiving it, to make sure the system comes into this century.

I hope that I can work with you, Mr. Chairman, to make sure that we have exactly what we need; and if I might for a second discuss an issue that Senator Chafee talked about.

And that was: many of us—and I use the “us”—voted to enact the changes that are incorporated in the current UI program. We may now want to reexamine our votes, but the fact is we did vote for the current program. The Reconciliation Act had the effect of tightening the targeting of extended benefits. It raised the trigger rate from 4 percent to 5 percent. It eliminated the national trigger.

Senator MOYNIHAN. Could I just ask you, Madam Secretary, which Reconciliation Act that was?

Secretary MARTIN. Surely. Of 1981.

Senator MOYNIHAN. Of 1981?

Secretary MARTIN. Right, yes. It eliminated the national trigger; it also added some solvency provisions for the trust fund. It put interest on State loans, but it also said to the States that, if you raise your State taxes, and if you take steps on the benefits side, we will give you a break on the loans payback.

The reason for this—and it is easy now to look back and question this when you see all this money in the loan fund—but if you recall, after the 1983 recession, there were worries. And even before that, there were worries about the stability of the funds.

By amending the program this way, it has worked; you can argue because now the funds, as you so wisely pointed out, Mr. Chairman, are in good financial shape. And so, part of this involves the health of the trust funds.

Lastly, and I don't need to talk to members of this Committee—some of whom I know have served on the Budget Committee and on a committee such as the Finance Committee—but the trust fund is not used for other purposes. It is an accounting offset.

But let me be very clear. There is no money directed from that fund to purposes other than UI. In other words, you can't write the check from that fund for anything else.

Now, it is an accounting offset, it is true; and I am not trying to argue that. But I don't want anyone who would hear this to think that money from that fund was specifically used for another purpose; it is there in the unemployment trust fund.

Senator MOYNIHAN. The fund is invested in Federal securities.

Secretary MARTIN. Yes.

Senator MOYNIHAN. And the Federal Government sells the bond and receives the money; then, the money itself is used as Federal revenue.

Secretary MARTIN. But you and I would both agree that there is—neither of us under current conditions have worries about the fact that there wouldn't be money available for those benefits as prescribed by law in the funds. And that is what you want to reassure people about, Mr. Chairman.

Senator MOYNIHAN. I agree, and I think it is important that you made that statement; but can I just ask you a question?

Secretary MARTIN. Sure.

Senator MOYNIHAN. How would you address the matter which Senator Sarbanes, as Chairman of the Joint Economic Committee raised, which is that revenues coming into the Extended Benefits Trust Fund are large and outgoes are small during a recession? How is that working?

Secretary MARTIN. Well, it is working.

Senator MOYNIHAN. That wasn't our plan.

Secretary MARTIN. It is part of what Congress said they wanted. I mean, I would have to come back to this law Congress passed; and that is the unemployment rate at which States would trigger on extended benefits.

Senator SARBANES. I know, was trying to be careful with this; and I certainly would never—he is such a bright, able guy—put words in his mouth. But if you spend down that fund, Senator Chafee is exactly right. You know, the money comes from somewhere.

And you can't talk about having a stable fund; and then, on the other hand, say now that it is stable, let's spend the money out of quickly. And then, let's increase the tax—in my view, you can't, anyway—when the economy is in some jeopardy.

I know of few economists—in fact, I don't know of any off the top of my head—who would say this would be the time for a new employment tax. The person who has the small or medium business is going to choose then not to rehire. In effect, you are just going to exacerbate the problem, not cure it.

So, you know, he may have a different view of that. Again, without him here, I don't want to suggest that this is his view. However, the idea of these huge new employer taxes, at a time when the economy has problems, is one that is extraordinarily questionable in my view.

The wisdom of the Senate and the House will prevail on that subject. I will obey the law as you pass it; but that is what the department is doing now.

Senator MOYNIHAN. A fair point. May I ask that you give us a response in writing—I am sensitive to your time right now—on this point that the Chairman of the Joint Economic Committee just made, that \$700 million will come into the Extended Benefits Trust Fund this year and only \$140 million will be paid out? I see Secretary Jones is nodding.

Secretary MARTIN. I will be happy to provide an answer.

[The written response of Secretary Martin follows:]

It is true that the Extended Unemployment Compensation Account in the Unemployment Trust Fund is expected to take in about \$720 million in revenues under the Federal Unemployment Tax Act in fiscal year 1991 and pay out about \$140 million in extended benefits.

The Congress specifically established this trust fund account in 1970 to ensure that funds would be available for the payment of extended benefits when the program is triggered on in a State as prescribed by law. The amount in the account is a function of both the taxes flowing into the account, and the ceiling on the account. The program is now triggered on in nine States. Congress tripled the ceiling in this account in 1987, allowing the previous amount to build up, and the account is now at its current ceiling of \$7.55 billion. Presumably, Congress acted in 1987 to preclude the necessity of borrowing in the future from increasingly scarce general revenues to finance the cost of extended benefits.

Therefore, the disparity between income and outgo in the Extended Unemployment Compensation Account is one that I believe was planned for by the Congress in its attempt to emulate the ant and not the grasshopper in storing up in the good times in preparation for the bad times.

Secretary MARTIN. Quickly, I am glad that the Joint Economic Committee agrees. In effect, what that is saying is it is going to be a mild, quick recession. We all want that, Mr. Chairman; we all do. But one of the reasons for a fund is to protect oneself if it is not.

You can't have it both ways. You can't say, well, it is working and we now have enough money there; let's spend it. Then, what if you didn't have it next year? What if you didn't have it next month?

So, we will be happy to answer the question but be very careful.

Senator MOYNIHAN. The question is why Extended Benefits are not being paid out to the degree they are being taken in during a recession.

Secretary MARTIN. Yes. I will be happy to answer the question. May I respond just briefly, too, that we deliberately increase the FTA tax—when I say “we,” I am speaking in terms of the Congress when I, too, was a member—and we put a very high ceiling on the account. That is part of the law.

The point I am making is that, if you as a committee are looking to change the law, we will be happy to comment on that; but the fund is working as the law prescribes it should work.

Senator MOYNIHAN. Thank you, Madam Secretary.

Secretary MARTIN. And the reason I am leaving, if you want—

Senator CHAFEE. Could I ask one quick question for the record before the Secretary goes, Mr. Chairman?

Senator MOYNIHAN. Sure.

Secretary MARTIN. Sure. I should add that Assistant Secretary Jones is truly an expert, and I know how much he enjoys testifying before the Congress, too. [Laughter.]

Senator CHAFEE. All right. Here is my question. The National Chamber Foundation, which is the research and education affiliate of the Chamber of Commerce, recently submitted a report on the

macroeconomic effects of the Downey proposal to the unemployment insurance fund program.

According to the summary of this report—and I am just giving you a summary—the Downey bill will do the following: one, cost the economy approximately 127,000 jobs a year; two, it will cut GNP by roughly \$8 billion per year for the next 6 years; and three, it will drive business profits down by nearly \$6 billion each year.

Could you comment on that? Now, I know you have to go; so, if you want Mr. Jones to speak for you, or if you want to do it writing, do whatever you wish.

Secretary MARTIN. All right. On this one, they used a DRI model. The methodology is an interesting one over a broad sample. We think it is probably fairly accurate—the methodology.

I should also add that it would cost businesses, who would have to get the money from somewhere—new jobs, research, productivity increases—somewhere—\$47 billion over 6 years. That is also indicated in the survey.

So, it would probably do the exact opposite of what I would hope that most members of the Congress would want it to do, which would be to provide a thriving economy and more jobs. We think it is a pretty good study; it is not ours.

But even if one argues on the margins of some of it, the downside of the costs of the Downey bill are extraordinary in nature; and I will be glad to also send a fuller answer as we have looked at it, and I have directed Secretary Jones and his department to look carefully at the study.

Senator CHAFEE. Thank you very much. Thank you, Mr. Chairman.

[The written response of Secretary Martin follows:]

The Department agrees with the National Chamber Foundation study's conclusion that the employer tax increase contained in the Downey bill would result in a significant loss of job opportunities. The particular magnitude of the estimated job loss, however, will vary depending on the model assumptions. The Department is further examining the econometric models and other information that is available to assist in evaluating the economic effects of the FUTA tax.

Senator MOYNIHAN. We thank you, Madam Secretary. Thank you, Mr. Jones.

Secretary MARTIN. Thank you. See you tomorrow.

Senator MOYNIHAN. See you tomorrow.

[The prepared statement of Secretary Martin appears in the appendix.]

Senator MOYNIHAN. Now, we welcome once again our good friend and colleague and a friend of the Secretary of Labor obviously, Sander Levin.

STATEMENT OF HON. SANDER M. LEVIN, A U.S. REPRESENTATIVE FROM MICHIGAN

Representative LEVIN. Good morning, Mr. Chairman.

Senator MOYNIHAN. Good morning, sir.

Representative LEVIN. And your distinguished colleague from Rhode Island. Let me first ask that my testimony be printed in the record, first so it will be there and second so that I can be briefer than the testimony.

Senator MOYNIHAN. By all means then, and it is so ordered; but please, take your time. We are interested in hearing you.

Representative LEVIN. I would like to comment on several issues. I was going to focus on two—the administrative funding issue and also job search and job training as relevant to unemployment compensation; but let me say a few words, if I might, on the extended benefit issue since it has been raised so articulately on both sides.

We are in this dilemma. In good times, we say there is no need to reform the unemployment compensation system. In bad times, we say we can't do it. The result is we never do so. And we come into a recession with a system that is outgunned by the realities.

So, what is the answer? Well, there are several responses; and you have heard some of them today. One of them is to assure everyone that the bad times are really good; that is one way to handle it. There is no problem.

As has been testified here, the system is working effectively.

As I invited Mr. Jones at a hearing in the House some weeks ago, I invite anybody who believes that to come with me to Madison Heights, Michigan to the employment compensation office, the MESC Office, and just talk to people on the line, often several hours long, waiting for their unemployment compensation checks, or waiting to talk to the employment service, or waiting to try to talk to somebody there about a problem with their benefit check or the lack of it.

All kinds of figures are thrown around; 72 percent of job losers are covered. I suggest, as you will, that the committee go beyond those figures and behind them because, included in most calculations, for example, are people who were laid off, exhausted their benefits, and then are disqualified because they had earlier left a job to take a better one.

A recent study indicates only 37 percent of the unemployed in this country today are covered. It is the worst record of any industrial nation.

Senator MOYNIHAN. And quite at odds with our previous experience.

Representative LEVIN. It is.

Senator MOYNIHAN. Fifteen years ago, it was about twice that.

Representative LEVIN. Exactly, Mr. Chairman. Exactly.

It takes close to 11 percent unemployment to trigger on. Why should every State have to go through the experience of Michigan in order to become eligible—or the employees therein eligible—for beyond 26 weeks?

And I just say to everybody who says the system is working: 200,000 to 250,000 workers each month this year have exhausted their benefits. Now, is that a system that is working?

These are people who work for a living. We are not talking about people on the so-called "dole." These are people who have been working and are laid off through no fault of their own.

So, I think to pretend that bad times are good is a rosy colored view from Washington, DC that looks at people as numbers. And everybody who says that should go to an unemployment compensation office in their own home town.

In terms of the cost, there will be a cost. The Downey bill, of which I am one of the chief cosponsors, postpones the initial impact

on employers until 1992, when we presumably would be out of a recession.

Maybe it should be trimmed down, but let no one say that it should be just thrown to the side, that this Nation can't look at unemployed—hard workers, women and men—and say: There is no safety net for you.

Now, let me just quickly talk about two other issues that I wanted to focus on. One is on administrative funding, and the other is on job training and unemployment compensation.

What happened is this, Mr. Chairman; I will be very brief. I was in my district office 1 day—I think it was on a Saturday; and I picked up the phone, and this unemployed worker starts telling me that he has been off work, as I remember it, 7 or eight weeks, has several children. His creditors are after him, and he can't get a check.

I just had no answer. And it turns out that there were thousands like him in Michigan and throughout the country. And at the same time, we had \$1 billion here in Washington set aside.

So, what am I going to tell him? Am I going to tell him—and you are an expert on this issue—well, we need the \$1 billion to cover the deficit? Somebody else can tell him that; I am not going to tell him that. I had no answer. And he energized me.

And I came back here, determined to look into it. John Thodis of the Michigan Manufacturers Association is going to testify later because, here, employers and employees in Michigan have of one mind, that it isn't fair to tax employers, send the money to Washington, and have them keep it for some other purpose, rather than sending it back to the States.

It is just that simple. That is a strange form of federalism.

Let me just say a word about the notion: What are we doing arguing about this when the House budget underfunds the administrative account for next year? There is a disagreement between OMB and CBO on baseline; and the Budget Committee asked the two to straighten this out.

If CBO turns out to be wrong and OMB right, we will have to rectify that; but you know, that disagreement shows the very need to change the administrative funding so that it is on a mandatory basis. I want to make just two points on that subject.

I was thinking about it. For food stamps, we don't rely on the supplemental system for administrative funding. AFDC, we don't; right, Mr. Chairman?

Senator MOYNIHAN. No, we do not.

Representative LEVIN. We don't because we don't want the responsibility of people starving while we wait for the Administration to recommend a supplemental and for us to pass it, as we did in March, 5 months out after the beginning of the fiscal year. We don't want that responsibility.

Why should unemployment compensation be different? Why should we treat people who have worked hard for a living, laid off through no fault of their own, leave them to the uncertainties of the supplemental process in Washington?

Senator MOYNIHAN. If I can just offer the thought—and others may or may share it—unemployment insurance is paid for in advance insurance and ought to be paid out automatically.

Representative LEVIN. I think so, and there has been some talk of a reserve fund; and since the idea emanates from Michigan, I think it is a pretty good idea.

But it really isn't adequate simply to set up a reserve fund for administrative funding for a number of reasons, including that the reserve fund has the problem that it bumps up against budget ceilings.

And also, it is somewhat guesswork; and if you get into a difficult situation, as we have in the last months, even that may be inadequate.

So, I hope very much that this committee will take the lead in making the administrative portion of it mandatory. One last word on it.

It is said, well, then it is just Washington shoveling out the money to the States; and we don't have a control over efficiency. This really isn't true because the Federal Government will set the standards by which money—and it does—is allocated to the States.

So, so much for administrative funding. I hope that your committee will show the leadership and not be diverted by the notion that the present budget is inadequate because it again just shows the inadequacy of hundreds of thousands of workers laid off, relying on the supplemental appropriation process here to get their checks.

On job search and training, Mr. Chairman, you and this committee have been in the past in the lead in linkage of training and retraining and the welfare system. I think we need to take a look at the unemployment compensation system—this is my own view—and in a careful way, but a deliberate way, begin to more effectively link unemployment compensation, income replacement, and job search and job retraining.

Other nations do it and very effectively. I don't suggest we do this in a way that diverts from the basic income replacement benefit. We take some modest steps in the Downey bill that would tie, after 10 weeks, unemployment benefits to job search.

Essentially, we say that when it is pretty clear there will be long-term unemployment, there ought to be a job search required. But I want to say one word about that.

If we are going to require it, we have to make sure that the employment service is responsive. I was in this same Madison Heights office 3 weeks ago or 4 weeks ago. Two workers were processing 500 cases through the employment service—impossible to do it effectively.

The employment service designated personnel were being shifted over to other parts of the office because they were inadequately staffed; and the employment service phone operates through the main number. They don't have enough money in the Madison Heights office for a separate telephone number for the employment service.

So, somebody who wants help finding a job has to go through the general number, which as I said took us 5 hours to reach one Friday morning. That really pays lip service to our belief—and legitimate belief—in the value of work and putting people back to work.

So, if we are going to step up—and I think we should—the connections between the unemployment system and job search and re-

training, we are going to have to make sure that we fund the system.

I leave with a feeling of urgency. I go back to the Madison Heights office every few weeks because that is the real world; and I want us to remember it and to reform the system.

For us to refer to 1981 as a defense for the sins of 1991, in my judgment, simply uses the omissions, to put it mildly, of the past to excuse inaction in the present.

Thank you very, very much for your time.

Senator MOYNIHAN. There, we have heard from the real world. Could I say to you, sir, that 30 years ago, I came to Washington as an Assistant Secretary of Labor under President Kennedy's Administration; and frankly, we would not have known what you were talking about.

The U.S. Employment Service was something we were very proud of. I mean, it was an active enterprise; it didn't take 5 hours to get on the telephone. It worked. It was there. It was something that had an esprit.

I mean, people said: We are the U.S. Employment Service. It used to drive them crazy when people would say "I am going to the unemployment office." This has been a decline in an institution. What would Walter Reuther say? Let's get onto this; I couldn't agree more.

I think your point about the automatic payment of insurance benefits is good. I mean, what would you think if you put your money in a bank in a savings account and went to draw it out and they said it will take 4 weeks? I mean, what is that all about?

That money is insurance payments paid in advance, held for the purpose; the receipt was to be automatic and prompt. What is going on with our Government?

We thank you very much. Senator Grassley, I am sure you would agree.

Senator GRASSLEY. Yes. My questions deal with the subject of performance by the unemployment and job service, as much as about the fund; but you know, basically, the question is what we are doing. Are we getting our money's worth?

And as you are aware, Congressman, we currently have a book of Federal rules and standards that States have to comply with regarding their unemployment insurance fund; but on the job service side, there are no such standards.

So, how would you feel about setting up minimum standards for the performance or placement for job service? I guess my question would come from a point that, if we aren't being successful in helping people find jobs, then we are failing. Making sure we get our money's worth is basically my question from State-administered services.

Representative LEVIN. Yes. I am very much in favor of doing that.

I don't want to say that the State bureaucracy--if one wants to call it that--always works perfectly any more than the Federal. You know what the trend line has been for the employment service the last years.

I don't have the figures for Iowa in terms of the dip, but I am sure the situation there is as true as in Michigan. You have had a

diminution, a depreciation—to pick up your thought, Mr. Chairman—of the value of this service; and if it isn't working well enough, change it—don't kill it.

I suggest you ask employers. I happened to spend a lot of time in your State in 1987 and early 1988, when it was going through some very difficult times. I don't think people understand the diversified nature of Iowa; you know, we just think of the agricultural part, and there is real deprivation there.

And there needed to be a service that did not have two people trying to place 500. So, I am in favor of setting standards but also understanding what we have done to strangle the employment service efforts in a number of ways.

Senator GRASSLEY. Let me run a thought by you on another subject as far as the soundness of the trust funds. If you would have any opinion in regard to providing incentives that would help States keep their trust funds solvent, and I would suggest—and you might react to this suggestion but also have some of yours—what about sanctions, such as increased employer taxes for States that are negligent or poorly managing their program and their fund?

Representative LEVIN. We have had forms of sanctions in terms of the interest system and in terms of the efficiency of these various systems.

I am not opposed to rigor in a system; I am all for it, but I will tell you the truth, Senator. What moved me was that call from a constituent that morning, but also when I visited the Department of Labor soon thereafter, or maybe it was earlier. It was around the same time.

And I talked to the Civil Service personnel there, and trying to get their explanations as to what the Federal Government had done to the States. The truth of the matter is that, while we need to make sure there is effectiveness within the States and the operation of their system.

And there is now an entry into Michigan, and I am all for taking a hard look at how well it is run. There is a new computer system going in.

We can't ask for effective implementation of Federal laws if the Federal Government that has the money for the implementation of these laws undernourishes that system. We are talking out of both sides of our mouth.

So, I think what you are saying is let's have rigorous standards; but let's also have rigorous compliance with the spirit of Federal law that says give the States the administrative funding they need.

Senator GRASSLEY. All right. Thank you, Mr. Chairman.

Senator MOYNIHAN. And thank you, sir.

Representative LEVIN. Thank you very much, Mr. Chairman and Mr. Grassley.

Senator MOYNIHAN. We will be attentive to this testimony.

Representative LEVIN. Good luck. We look to you to join in, if not lead.

[The prepared statement of Representative Levin appears in the appendix.]

Senator MOYNIHAN. We have Mr. Anthony Snider here, a Philadelphia resident, who is part of the Philadelphia Unemployment

Project, and who has a brief testimony he would like to make. Mr. Snider, we welcome you to the committee.

Mr. SNIDER. Thank you, Mr. Chairman.

Senator MOYNIHAN. Please proceed. We will put your statement in the record, and you can summarize it or read it, as you like.

STATEMENT OF ANTHONY SNIDER, A PENNSYLVANIA TAXPAYER

Mr. SNIDER. Thank you, Mr. Chairman. Mr. Chairman, my name is Anthony Snider. I am 37 years old, and I have been unemployed for 5½ months from my job as a carpenter for Worgor Interior Systems.

I come before you with only 2 weeks unemployment checks left until my benefits run out. I appreciate this opportunity to present the views of the unemployed on the serious problem in the Nation's unemployment insurance system.

I represent the Philadelphia Unemployment Project, an organization of and for the unemployed. Unemployment insurance is the first line of defense for workers and our families when a bread winner loses his or her job. It is supposed to be a key part of the Nation's safety net, which helps us maintain a minimum standard of living when we lose our jobs and our income.

There are thousands of unemployed workers who cannot find a job and no longer have any benefits to help them get through the recession. In 1975, benefits were provided for 65 weeks; in 1983, it was 49 weeks.

We support H.R. 1367, the Downey bill, for 52 weeks of benefits and a very important retroactive provision that would pick up workers who exhaust their benefits after January 31, 1991. Twenty-six weeks is totally inadequate with the economy the way it is today.

When our benefits run out, we are told to go on welfare and become a burden of other taxpayers. This is not what we want to hear, when there is \$8 billion sitting in a fund for the extended unemployment benefits.

The President deemed it an emergency that the administrative part of the unemployment offices needed \$150 million to keep them running. If that is the case, then we, the unemployed, must be the emergency.

We, as taxpayers, demand that this money be given to the unemployed now. We did not start this recession; we didn't ask to be laid off. It is time the Federal Government takes care of the people in its own country, instead of every other country in the world.

There are unemployed taxpayers here in this country who are losing or have lost their homes, their cars and, in some cases, their families, because they can't afford to pay their bills.

We are not asking for handouts. We are asking for extended benefits of another 26 weeks or jobs to provide for those depending on it. As workers and taxpayers, we demand that our tax monies be spent here to help the laid-off workers who need it.

The President didn't ask the taxpayers if he could spend \$30 billion to save the building and loans or if he could cancel the debts of other foreign countries. He can save \$100 billion to save Kuwait, but he can't spend anything to help his own countrymen.

If the President thinks the system is working, then he should ask the 6.8 percent of the people in this country who are not.

I have sent out over 150 resumes and have filled out 50 to 60 job applications since I was laid off. I have even read through the phone books and called companies to ask if they were hiring, only to be told that they have their own people laid off or the company is closing.

Recently, I went to Boise Cascade in suburban Philadelphia, which had five jobs to fill in the warehouse. Over 2,000 people showed up to apply for five jobs.

Kraft Food had a job fair for 20 temporary jobs in their Breyers Ice Cream factory. Over 1,500 people applied.

The bottom line is: There are no jobs. I want to work and have worked all my life. I was in the military for 14 years. I have managed from 40 to 100 people at one time in the military and managed \$1 billion in aviation equipment in the service.

When I apply for a job, I am told I don't have management experience. Does this mean I wasted 14 years of my life? In a decent economy, I would be working. With this recession, I will soon be out of my benefits.

We, the unemployed, need the extension now. If the extension is not granted, it will be the first time since the 1930's that the unemployed workers have not received extension benefits during a recession.

Justice to the unemployed must be served in great haste so that we may continue to serve our country as viable citizens.

I thank the committee for allowing me the opportunity to address this urgent need for the extension of unemployment compensation. Thank you.

Senator MOYNIHAN. We thank you, sir. [Applause.]

We would like to keep our proceedings in order.

Were you in the Air Force, Mr. Snider?

Mr. SNIDER. No, sir, I was in the Army and the Navy.

Senator MOYNIHAN. Yes. Please sit down. Could I ask you: Have you asked for help at the U.S. Employment Service in Philadelphia?

Mr. SNIDER. Yes, sir, I have.

Senator MOYNIHAN. Representative Levin was just talking about that. How did that go?

Mr. SNIDER. I have asked help from there. I have asked help from the VA. I filled out SF-171's for the Federal Government. Every place I turn, there are no jobs. Either they are not hiring, or they want to tell me that, because I have a military background, I have no management experience. I have more management experience than most people that are running companies do. I have handled a lot more money.

Senator MOYNIHAN. You made that point in your testimony.

Mr. SNIDER. Yes, sir.

Senator MOYNIHAN. That doesn't sound like a very sensitive U.S. Employment agency, does it—to say that anyone who has had \$1 billion worth of equipment under his responsibility has had no managerial experience. I am sure we would like to know more about that.

If you will just stay in touch, we will get in touch with that U.S. employment agency and see what they can do. Meantime, you came here to speak about legislation; you spoke very well. You spoke very forcefully; you spoke from experience, which can be illuminating here in Washington. Thank you very much. .

Mr. SNIDER. Thank you, sir.

Senator MOYNIHAN. And now, we will hear from a panel of representatives of the labor movement: Mr. William Cunningham, who is the Legislative Representative of the AFL-CIO; and Mr. Alan Reuther, who is association general counsel of the International Union, United Automobile, Aerospace, Agricultural Implementation Workers of America (UAW), both of Washington, DC.

Good morning to you both. Gentlemen, Mr. Cunningham, you are first; and Mr. Reuther, you are next.

STATEMENT OF WILLIAM J. CUNNINGHAM, LEGISLATIVE REPRESENTATIVE, AFL-CIO, WASHINGTON, DC

Mr. CUNNINGHAM. Thank you, Senator Moynihan. We appreciate the opportunity to testify before the Senate Finance Committee on the Nation's unemployment insurance system.

As you know, Senator, the unemployment insurance system is the first line of defense for workers and their families when the worker loses his job. Unfortunately, the UI safety net is full of holes. Coverage is tragically inadequate.

Appended to my testimony is a list of average recipients in each State. New York is about 50 percent; that is atypical.

Let me say that the focus on the UI system comes at the right time in the process. The AFL-CIO Research Department projects that the unemployment rate will remain high over the next 3 years. So, we will have this problem with us.

Even if the recession turns around, the unemployment figures will lag behind. We believe it will lag for 3 years.

Senator MOYNIHAN. Yes, that happens. That happens.

Mr. CUNNINGHAM. Senator Moynihan, for us, we have several issues that are of vital concern. Perhaps the most important concern to us—and you have heard it mentioned before—is that only 37 percent of unemployed workers get unemployment compensation benefits.

As an entitlement program, this is seriously deficient. In my testimony, I relate how many people are unemployed. For example, in 1990, 6.9 million persons were unemployed—but only 2.6 million were getting UI benefits, only 37 percent of the jobless.

We believe that the changes that took place in 1981, basically to reduce eligibility requirements to get the system under financial control, are outmoded, and are now counterproductive and should be changed.

We are fully aware that, when you raise eligibility standards, this is going to cost money. It is not done on the cheap; it is not done by smoke and mirrors.

We would ask this committee to look at initial eligibility as one of the important problems that should be addressed by a comprehensive rewrite of the unemployment compensation system.

I mention in my testimony—and it is there for review—what we believe the new Federal standards, which I think is the way to go, should be put in place. We would also note in passing that UI benefits are low compared to where they should be over time. Again, we understand that if you raise benefits in each State, this is going to cost money, too.

Nothing in the UI system can be done on the cheap.

The Extended Benefits Program is something that everybody wants to look at and work on. You understand and we understand that we can't play around with the existing Extended Benefits Program because, if we do, it will require action by the State legislatures, which will delay resolution of this issue into the indefinite future.

So, we have to look at a different kind of program to rectify this mistake.

The AFL-CIO sincerely believes that we should get rid of the insured unemployment rate as the measure. It doesn't mean anything to most people; basically, if you are writing news articles or letters to get people to be aware of a program, you start using insured unemployment rate and you say 2, 3, 4, percent, no one knows what you are talking about.

We believe that the total unemployment rate should be used as a new local figure for whatever program is done in the Extended Benefits Program or in a short-term new Federal program.

Senator MOYNIHAN. You know, that is a very clarifying thought. You can live with this subject for 30 years and you still find new things. Now, what is this? There is the unemployment rate, and there is the insured unemployment rate. How do things get fuzzy? Why are the numbers different?

I know there is a reason, but it doesn't help to have two numbers with respect to the same subject.

Mr. CUNNINGHAM. It also confuses the recipients of the program, who don't know what you are talking about and whether the program is on. If they know their State has a total unemployment rate of, say, 6 percent and that was the new trigger, they would know they would be eligible for a revised program under this.

When you say it is only 4.2 percent and they may be eligible, I don't think they really know exactly what is going on. Confusion in this system---

Senator MOYNIHAN. And the press does not report the insured unemployment rate.

Mr. CUNNINGHAM. That is right.

Senator MOYNIHAN. They are pretty good about monthly reporting from the BLS of the unemployment rate; and that is what you know. Well said.

Mr. CUNNINGHAM. Senator, you also know—and it was mentioned here earlier—that the unused money in the Extended Benefits Program is a source of concern for everyone. I heard the Secretary basically saying, well, it is not here and it is not there; and we are buying debt and all the rest.

I mean, this money—just like Social Security money—is being used currently to finance ongoing programs. We sincerely believe that the money in this fund should be used to be paying unemployment benefits to workers.

Let me go to the administrative financing issue that is of serious concern. Each year, or at least every other year—

Senator MOYNIHAN. You passed over some things. I have taken the liberty of reading from your full text. You mention an article by Gary Burtless of the Brookings Institution, who says: Brookings reviewed the issue. For practical purposes, the Extended Benefit Program has now virtually ceased to function.

Mr. CUNNINGHAM. That is correct. There are only nine States that have triggered on. I would venture to say that there are more States and areas within States which the high unemployment rate should, by more sensitive triggers, have triggered on much earlier.

Senator MOYNIHAN. Yes, we thought we had done something good there 30 years ago.

Mr. CUNNINGHAM. Yes. You have to remember in 1981, when you made these changes and the system was in disarray, you basically ceded to the States the authority to ratchet down these benefits and programs; and that is the problem.

The problem is that you can have a good financial system if it doesn't pay benefits. I think what this debate is to look at the other side. Should we be paying more benefits?—and what is the cost associated with that?—rather than just having a financially sound system that doesn't cover a whole bunch of people.

Administrative financing: as you well know from delegations that have come into your office almost on an annual basis looking for emergency appropriations, we believe that there should be an entitlement program set up for State administrative financing.

It makes absolutely no sense to us to have this fight each year and look at it. Since the States have already paid the money to the Federal Government for this, we think the money should be turned around rather rapidly.

And we believe that an entitlement grant that is appropriated automatically should be put in place. It should be parallel Social Security office. If you had a Social Security office that couldn't provide services, I think the lynching crews would be heading to Washington at great rate.

Why are unemployed workers any less deserving of a benefit and service than people having Social Security benefits?

Senator MOYNIHAN. If I can just interrupt for one second?

Mr. CUNNINGHAM. Yes, sir.

Senator MOYNIHAN. You make a good point. This is an entitlement. You don't get the entitlement by virtue of your having blue eyes; you get it because monies have been paid into a fund to ensure you against the risk of unemployment. When that insurance is due, it is due.

It is not a benefit provided you; it is insurance paid to you. We ought to be a little indignant about this. We say: You are entitled, but we haven't got any money for postage.

Mr. CUNNINGHAM. I think that is a benefit side of the problem, the other part of the problem. As I mentioned earlier, if you keep on allowing the States to restructure their eligibility requirements, you may think you are entitled to them; and if you do make it to the front of the desk, you will find out that, for one or another of the State requirements, basically you are not eligible for benefits.

And this is a frustrating part of the problem.

Let me just turn to State solvency for a minute. It is hard at the time of a recession to argue for State solvency. As Sandy Levin pointed out, the only real hook we have—or the system has—now is basically interest on loans paid by States.

But it seems to us that in a long-term solution to unemployment compensation, which we are basically looking at now in terms of a small package or a small package to basically handle this problem, the idea of a prospective solvency package should be looked at.

Based on the GAO study, we are informed that if the recession is very severe into 1991, 22 States will have to borrow more than \$17 billion from the Federal Government; and of course, the Federal Government doesn't have this loose change lying around. It will have to borrow in turn from the private sector—the private market—to do it.

Mr. Chairman, as you know, we support Congressman Downey's bill as a good first effort to address these issues. The Downey bill deals with eligibility standards, disqualification periods, the flawed Extended Benefits Program, and inadequate funding of the State Unemployment Compensation and Employment Service; but it does not go into financial solvency.

We believe that the Downey bill is a good start. We understand that the Senate is working on not a companion piece, but a different way of looking at this.

Before I turn it over to my colleague, Mr. Reuther, Senator Chafee mentioned the Chamber of Commerce study, which basically panned the Downey bill and said that it would cost inordinate amounts of money and throw a lot of people out of work.

I assume that the model that they used was the same model that basically said—and this is their positive spin; the Chamber's positive spin—that if they rolled back the capital gains tax, put IRA's in place and, indeed, reduced the Social Security tax, the Federal Government would get \$109 billion by 1995.

What I am trying to say is that it really depends on how you skew this model. I don't think anybody looking at it, no matter where you are on capital gains—we are against it; we tend to be neutral on IRA's—that no one objectively looking at these positive things can credit them with not losing revenue in the short term.

And yet, the Chamber's model, which pans the Downey bill, basically says that this would indeed produce new revenue by 1995.

The point I am making here is that models are things that are basically used by proponents and opponents; and we believe that, on this issue, the Congress would be well served to keep focusing on the unemployed individual.

Unemployment is probably a most traumatic time for anybody—basically, heads of families, losing their job.

As you rework the unemployment compensation system, we know you will, and we hope other members will, focus on the persons who have lost their jobs and make sure they have benefits in place for them when this occurs.

Thank you very much.

Senator MOYNIHAN. We thank you, sir. We won't be hearing from the Chamber this morning, but John Thodis of the NAM will be here; and we can arrange to do that later.

[The prepared statement of Mr. Cunningham appears in the appendix.]

Senator MOYNIHAN. Mr. Reuther, I believe this is the first occasion you have appeared before our committee.

Mr. REUTHER. I have actually been here several other times, but the first time on this subject.

Senator MOYNIHAN. We welcome you on this subject.

**STATEMENT OF ALAN REUTHER, ASSOCIATE GENERAL COUNSEL,
INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE,
AGRICULTURAL IMPLEMENT WORKERS OF AMERICA (UAW),
WASHINGTON, DC**

Mr. REUTHER. The UAW appreciates the opportunity to testify on the critical subject of unemployment insurance. My colleague from the AFL-CIO has already discussed issues relating to the Extended Benefits Program and administrative financing.

We wholeheartedly agree with the positions articulated by the AFL-CIO and by Senator Sarbanes and Representative Levin on these matters. Our written statement goes into a discussion of them in more detail.

Senator MOYNIHAN. We will put the statement in the record as if read.

Mr. REUTHER. For purposes of my remarks here today, I would like to focus on another critical issue, namely the need for Federal standards relating to trust fund solvency, benefit adequacy, monetary eligibility requirements, and disqualification provisions.

We are entering the current recession with our unemployment compensation system in its worst shape ever. Trust funds in many States have inadequate reserves; State and Federal legislative actions have cut the proportion of the unemployed eligible for unemployment benefits; and benefits are too low to adequately assist those who receive them.

If the current situation persists, only one in three unemployed workers will draw benefits in the current recession. This is a decline from 1980, when one-half of unemployed workers were paid benefits. In about a dozen States, fewer than one in five unemployed workers will receive a check.

Those workers who do receive unemployment benefits will receive an average benefit check of about \$160.00 a week, which will replace only about 35 percent of average weekly wages. Again, in some States, the situation is far worse than the average.

Sadly, the shortcomings in the unemployment insurance system are in large measure the result of legislative actions. During the 1980's, a majority of the States adopted tighter earnings requirements or tougher disqualification provisions to avoid or reverse solvency problems. Some States froze or reduced unemployment benefits.

The UAW believes the time has come to reverse the trends of the 1980's and restore our unemployment compensation system's ability to protect jobless workers and to counteract an economic downturn.

Unfortunately, unemployment insurance at the State level is not debated in terms of the twin national purposes of the program—

providing a prompt wage replacement for unemployed workers and preserving the level of economic activity during a downturn.

Senator MOYNIHAN. Yes.

Mr. REUTHER. Instead, State administrators, Governors, and legislators typically view unemployment insurance in the context of a business climate discussion. In effect, the States have been in competition with one another to reduce their unemployment costs.

As a result of this competition, the last decade has seen a steady deterioration in the unemployment insurance system's ability to satisfy its twin purposes.

The national goals of the unemployment insurance system deserve national safeguards. Therefore, the UAW urges the adoption of national standards to match the national goals in four interrelated areas.

During the 1980's, one of our Nation's longest periods of relative economic stability, State trust fund solvency did not improve dramatically. There is no State, to our knowledge, which has its trust fund in a position to pay adequate benefits to a reasonable percentage of its unemployed workers through a severe national recession.

In the long term, underfunding the unemployment insurance system helps keep benefits low and provides a rationale against efforts to improve the system. Accordingly, we believe Congress should adopt a trust fund solvency standard to require States to build up sufficient trust fund reserves during economic good times.

But simply adopting a trust fund solvency standard will not move the unemployment compensation system in the right direction. Unless a Federal standard for benefit adequacy is also adopted, many States will reach solvency by simply restricting benefits.

In fact, there is some evidence that this is already the situation. Seven States had high cost multiples over 1.5 in fiscal year 1990. As indicated in Exhibit 2 in our testimony, of these seven States, South Dakota and Oklahoma ranked in the bottom five States; and Mississippi and New Mexico ranked in the bottom 11 States in terms of the proportion of their unemployed receiving a benefit.

Senator MOYNIHAN. Yes.

Mr. REUTHER. In 1980, the National Commission on Unemployment Compensation recommended that Congress require States to have a maximum weekly benefit not less than two-thirds of the State's average weekly wage. The Commission further recommended that Congress require the States to pay weekly benefits which replace on the average at least 50 percent of the individual's wage. We urge this committee to adopt a similar approach.

In the past decade, the States have not only reduced or frozen unemployment benefits; most have taken other legislative actions which have limited access to benefits.

In its 1988 report, GAO found that 44 States adopted tighter monetary eligibility standards or stricter disqualification provisions between 1981 and 1987.

In order to further examine the effect of State law changes on the decline in the receipt of benefits, the UAW examined the States which paid the highest and lowest proportions of their unemployed workers during the decade of the 1980's.

Six States paid less than one in four of their unemployed workers a benefit, on average, for the years 1980 through 1989. Those

States were Virginia, Florida, Texas, South Dakota, Indiana, and Oklahoma. In contrast, the top six States were Rhode Island, Alaska, Massachusetts, New Jersey, Vermont, and Pennsylvania.

Senator MOYNIHAN. That is striking, that prosperous States such as Virginia and Florida pay benefits to one-third the proportion of unemployed workers that States like Rhode Island do.

Mr. REUTHER. We examined the State unemployment insurance statutes for two factors which commonly restrict the unemployment insurance program: the monetary eligibility earnings requirements and the type of disqualifications imposed upon claimants.

Exhibit 4 in our testimony summarizes our findings. Comparing the current legal situation in the States with the highest and lowest percentages for receipt of benefits, it is immediately evident that in general States with the lowest reciprocity levels have higher earnings requirements and stiffer disqualification penalties in their State UI laws.

The UAW believes that Congress should enact a Federal standard to set a floor below which States cannot go in restricting their unemployment insurance programs. In our view, a worker who works 20 hours at the minimum wage for 14 weeks should be eligible for UI benefits.

It is important to keep in mind that low wage or part-time workers will get lower benefits, often for shorter durations, than higher wage workers with greater labor market participation. But these low wage or part-time workers should not be completely excluded from our unemployment insurance system. In addition, the UAW also believes that Congress should set a national standard with respect to disqualification provisions. We would support Federal legislation prohibiting the States from using durational disqualifications, as has been recommended by the National Commission on Unemployment Compensation.

In conclusion, Mr. Chairman, the UAW appreciates the opportunity to present our views on the coverage and financing issues in the unemployment insurance system.

We believe the adoption of Federal standards with respect to trust fund solvency, benefit adequacy, monetary eligibility, and disqualification provisions would be an important step to fairer treatment of unemployed workers and the restoration of the unemployment insurance system.

We look forward to working with you and the other members of this committee as you consider these important issues. Thank you.

[The prepared statement of Mr. Reuther appears in the appendix.]

Senator MOYNIHAN. We thank you, Mr. Reuther. I can only speak for myself, but I completely agree with you—and I am sure with the AFL-CIO—on this question of national standards. And if Frances Perkins were about, she would be here testifying the same.

The decision in the 1935 legislation to have a Federal program but State standards with respect to unemployment insurance—but not retirement insurance, which is Social Security—had to do with theories at the time about public administration and different rates of industrialization. There were still States predominantly agricultural in their employment.

And as you may know, the curiosity is that there is almost no such thing as unemployment in agriculture. You can be half starved, but you are "employed."

Mr. REUTHER. Right.

Senator MOYNIHAN. And this was sufficient until the 1930's. Well, that was at the beginning of the century; we are now at the end of it, and we have a much more national, or international, economy. National standards are long past due.

We would like to thank you particularly for the research you did; those exhibits are very helpful to us and to the committee.

Thank you both, and we appreciate your coming.

I have a statement by Mr. Keith Brooks on behalf of the New York Unemployed Committee, which I would like to place in the record at this time, and I would like to thank the members of that group. I hope to be seeing them later.

[The prepared statement of Mr. Brooks appears in the appendix.]

STATEMENT OF KEITH BROOKS, COORDINATOR, NEW YORK UNEMPLOYED COMMITTEE

Mr. BROOKS. Mr. Chairman, I would like to have an opportunity. There are 100 people here from New York, unemployed people, who came down here at 5:00 o'clock this morning and would like to be heard.

Senator MOYNIHAN. Fine.

Mr. BROOKS. These people have filed into the hearing room, and I would like the opportunity to speak. It will only take a few minutes to address the committee on the issue.

Senator MOYNIHAN. Well, you are going to have to take your turn. We had a gentleman from Philadelphia, and we didn't know that you wanted to testify. You are entirely welcome in this room. There are seats that aren't taken.

Mr. BROOKS. A request was made a couple of weeks ago to testify. I think there is something inherently flawed in a hearing where the very people who are most affected by it are shut out of the hearing, whether intentionally or otherwise.

If we could take the opportunity to testify for a few minutes for you to hear from some people from New York—

Senator MOYNIHAN. Now, sir, just be a little patient. I did not expect to be chairing this hearing this morning; I was asked to do so yesterday morning while I was chairing another hearing.

We will try to get to you. We are going to try to keep to our schedule.

We just heard from the people from the AFL-CIO and the UAW.

We will now hear from the next panel of Mr. John Motley, who is vice president for Federal Governmental relations, National Federation of Independent Business, Washington, DC; Mr. John G. Thodis, who is president and chief executive officer, the Michigan Manufacturers Association, Lansing, MI, representing the National Association of Manufacturers. Mr. Thodis, did I pronounce that correctly, sir?

Mr. THODIS. Yes, sir.

Senator MOYNIHAN. All right. Now, Mr. Thodis, you have to leave; so, we are going to put you on first.

STATEMENT OF JOHN G. THODIS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, THE MICHIGAN MANUFACTURERS ASSOCIATION, LANSING, MI, REPRESENTING THE NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. THODIS. Thank you very much, Senator. Mr. Chairman and members of the committee, I am John G. Thodis. I am president and chief executive officer of the Michigan Manufacturers Association; and I am testifying today on behalf of the National Association of Manufacturers, a board I also serve on.

MMA is an organization that was founded in 1902 in Michigan. We have 3,500 members that employ 90 percent of the industrial work force of our State.

I have submitted a written text for the record; I would like to summarize, if I may.

Senator MOYNIHAN. It will be put in the record as if read.

Mr. THODIS. All right. Thank you. I thank you for the opportunity to present NAM's views on the current state of the unemployment compensation program. We commend the chairman and the members of this committee for holding today's hearing on this important issue.

The present economic climate facing the U.S. economy highlights the debate over what, if anything, needs to be done to address the relatively high number of unemployed individuals.

The current recession is expected to last through the end of the second quarter of 1991, with a decrease in unemployment to follow. Regarding the recession, businesses generally are optimistic.

Two-thirds of the 90 manufacturing companies surveyed at the February 9, NAM board of directors meeting agreed that the recession will be shallow. As for the recovery, well over half predicted steady but unspectacular growth.

Confidence in recovery is very important, leading employers to invest, rehire, and create new jobs.

Congressional considerations to expand unemployment compensation benefits to sectors of the economy that the program clearly intended to exclude—workers who quit jobs, who are involuntarily separated for cause, who have no attachment to the labor market, who do not earn wages subject to unemployment taxes—are unwarranted.

The system was never intended to provide benefits to every unemployed individual. It was designed for benefits to be paid to experienced workers for temporary periods of time.

Benefit payments must be strictly limited to compensation for periods of temporary, involuntary job-connected unemployment. Unemployment of longer duration is outside the proper scope of a program which is financed by a payroll tax system.

From time to time, the dynamic nature of our industrial economy may bring with it temporary and involuntary unemployment. Unemployment is an intrinsic characteristic of our economic system. Recessions come and go at periodic intervals. Some are prolonged; others are relatively brief.

Congress has always been sensitive to the hardship resulting from troughs in the business cycle. In 1970, Congress enacted a per-

manent program to automatically extend UI benefits when unemployment exceeded specific thresholds.

The Extended Benefits Program was marketed as an automatic response that would activate and deactivate, as appropriate, obviating the need for congressional action. Over the years, however, Congress has desired to make several temporary extensions beyond the permanent program.

Temporary benefit extensions beyond the permanent Extended Benefits Program enacted to mitigate the hardships of temporary unemployment are costly and often untimely. They tend to prolong spells of unemployment, and they are rarely delivered to those most needy and deserving.

The Extended Benefits Program is not broken; and certainly, it does not need reconstructive surgery, as some have suggested. NAM, however, does realize that in times of economic recession, there may be a need for extending the duration of unemployment benefits in those States that have determined that the period of temporary unemployment is of such duration to necessitate triggering of the EB Program.

The National Association of Manufacturers supports the present unemployment compensation program that balances responsibility for sound employment practices between the Federal Government, States and employers, and efficiently delivers benefits to individuals the program was designed to serve.

The UC program continues to operate as intended. Thus, given—hopefully—the shallowness of the current economic recession, efforts to expand benefits beyond its intended purpose are ill advised.

For the past 2 or 3 years, the UC program has been criticized for its declining coverage rates resulting in less than one-third of the unemployed workers actually obtaining coverage.

“Coverage” is a lexicon of the UC program; it has nothing to do with whether a worker files a claim for benefits, nothing to do with whether a covered worker is eligible for benefits, nothing to do with the disqualification from receipt of benefits. There has been, in fact, no decline in the coverage of the system. Over 98 percent of all waged and salaried workers are covered.

I digress for a moment, Senator. When you made the observation about the difference between the unemployment rate and the insured rate, the unemployment rate that is covered by the media all the time obviously, in my State of Michigan, is a sample of 1,000 households. That is how we come up with the unemployment rate in the State of Michigan.

The insured rate is very, very accurate because it is an accurate count of those people who have been laid off through no fault of their own.

Senator MOYNIHAN. Oh, we don't disagree there at all, sir. I might say to you that that is a pretty good sample, you know.

Mr. THODIS. Well, when we do political samples, we try to get more than 1,000 households to see how the voters are going to vote back home.

There is, however, a gap between the total unemployment count and the number of unemployed actually drawing UC benefits. There has always been a gap; and there are legitimate reasons for this gap.

Studies have shown that over two-thirds of the unemployed did not apply for benefits—a point missed by many critics. Of those who do apply for benefits, between 52 percent and 93 percent receive benefits. This simple comparison seems to indicate that the benefits are being paid at higher rates than the proponents of expanding the system would like you and the committee to believe.

The UC program should be soundly financed, using experienced rating as the basis for any unemployment compensation tax policy. The purposes of sound, experienced rating are to distribute costs, provide incentives for employers to stabilize employment, and generate the necessary active interest.

Now, program administration is one area where NAM, organized labor, and State agencies all agree. Sufficient funds need to be appropriated for proper and efficient claims administration. UC programs should encourage maximum employer interest and participation.

Efficient administration of State UC programs requires the cooperative exchange of information between responsible administrative agencies and employers for the proper determination and adjudication of claims. Efficient administration also means the timely adjudication of claims and payments of benefits.

Unfortunately, eligible unemployed workers have had to wait in line for hours upon hours to file their claim and weeks upon weeks to receive their first benefit check. This does not serve the employer or the employee.

In my State, in Michigan, earlier this year it took 6 to seven weeks for the first check. Now, most get it in 4 weeks. Now, there aren't a lot of people that have a month's backup in their back pocket.

Senator MOYNIHAN. No.

Mr. THODIS. And that is unconscionable, what we are doing to the unemployed who have to wait 4 weeks to get 3 weeks of their prior checks. And the employer community does not support this. It is inexcusable.

We have met our obligation to the Federal Government; we pay our Federal UI taxes.

Senator MOYNIHAN. You have already paid the money.

Mr. THODIS. We have paid it. And currently, over \$2 billion is available for program administration; but because of budgetary sleight of hand, the States are inadequately funded.

The basic infrastructure, I would venture, sir, is that the employment security system is so broken down that the agencies cannot respond in economic downturns. They do fine when the economy is good; but they can't respond in economic downturns.

Employers pay, I am told, approximately \$5 billion a year to the Federal Government for UI taxes. About \$2 billion goes back. I would submit: Where is the other \$3 billion, sir?

Senator MOYNIHAN. If he isn't careful, he might not get that plane. [Laughter.]

Mr. THODIS. That is all right. It is worth it if it helps. NAM believes that if Congress appropriates adequate administrative funds, the unemployment compensation program is currently providing the benefits to the very individuals that the program is intended to serve.

The program is not in need of reform, as some have suggested; rather than expanding unemployment benefits, we, the NAM, believe that Congress should focus on efforts to increase U.S. competitiveness and the growth of its economy.

This broader strategy will, by definition, reduce unemployment rates through the creation of more jobs.

I thank you for the opportunity to appear before you today. It has been an honor to be with you.

Senator MOYNIHAN. We thank you, sir.

[The prepared statement of Mr. Thodis appears in the appendix.]

Senator MOYNIHAN. Like any committee, we particularly appreciate the convergence of views that we have heard from Senators, from representatives of labor, from the UAW, and now from you that, whatever else, these are insurance payments, which are paid in advance. And they ought to be made promptly. There is no excuse for having persons wait 4 weeks for an unemployment insurance check, to which they are entitled and for which you, the employers, have contributed to a fund.

This requires our attention. May I ask a question? I know you have to hurry.

Mr. THODIS. No, I have time.

Senator MOYNIHAN. Would you consider getting us a little more detail on this proposition you have here about a survey in which two-thirds of the unemployed did not apply for benefits?

Mr. THODIS. Yes, sir.

Senator MOYNIHAN. If you could provide that in writing to the committee at your opportunity?

Mr. THODIS. We will be very happy to provide your office or the committee with that information.

Senator MOYNIHAN. The committee. We would like to put it in the record.

[The response of Mr. Thodis follows:]

The average application rate of job losers, the group most likely to apply for unemployment benefits is only 53 percent. For job leavers and workforce reentrants the overall benefit application proportions are 11 percent and 13 percent respectively. For these three categories the combined average unemployment insurance application rate is only 34 percent. These 1989 and 1990 data indicate that only approximately one-third of unemployed individuals tried to receive benefits.

Source: "Decline in Unemployment Insurance Claims Activity in the '90's"; Produced by the U.S. Department of Labor.

Occasional Paper 91-2, written by: Wayne Vroman, January 1991.

Payment rate describes the ratio of people collecting their first benefit check after filing an initial claim. The likelihood that a beneficiary of the unemployment insurance system will exist ranges on a state-by-state basis from 57 percent to over 90 percent for calendar year 1990.

Prepared by: Laurdan Associates

Source: U.S. Department of Labor/Employment and Training Administration/Unemployment Insurance Service.

Senator MOYNIHAN. We thank you very much, Mr. Thodis. Mr. Motley, I have got to be elsewhere. This is budget day, and my good friend and yours, Senator Breaux, has agreed to chair the remainder of the hearing. I want to turn the scepter over to you, sir.

Senator BREAUX. A little symbolism here. Thank you very much, Mr. Chairman. Mr. Thodis, you are excused. We are glad to have

you here, Mr. Motley. I understand this is also your birthday. I can't imagine your wanting to spend it here. [Laughter.]

But we are delighted to have you on behalf of the National Federation of Independent Business.

STATEMENT OF JOHN J. MOTLEY III, VICE PRESIDENT FOR FEDERAL GOVERNMENTAL RELATIONS, NATIONAL FEDERATION OF INDEPENDENT BUSINESS, WASHINGTON, DC

Mr. MOTLEY. Thank you very much, Senator Breaux. If Senator Moynihan is heading to the floor to speak on behalf of his proposal to cut Social Security taxes, I wish him Godspeed.

Thank you very much, and I thank the committee very much for the opportunity for me to appear here today, on behalf of NFIB's more than half million members across the country, on our thoughts on the current unemployment compensation program.

I have a full statement that I would like to submit for the record and then summarize orally for the committee.

NFIB's view of the UI program is colored by three factors.

First, we believe that the program was meant to provide temporary assistance between jobs for those people who have lost their employment for no reason of their own.

Second, we believe that the program should be and is intended to be run primarily by the States, who have very broad authority to make adjustments in that program, either to raise taxes to provide additional benefits, or to otherwise adjust them in some way.

And last, the program is funded by what we believe to be a very regressive payroll tax that has a proportionately larger impact upon smaller firms than it does upon anyone else because we tend to be labor-intensive.

While UI taxes have not gone up recently, in the 1980's, the other part of the payroll tax burden on smaller firms has crept ever upward; and that, of course, is the FICA tax—the Social Security tax. It increased from about 5.1 percent on the first \$25,000 of income in 1980 to 7.65 percent on the first \$53,400 worth of income just a decade later.

If you combine both of these taxes (FICA and FUTA), they present a tremendous problem for smaller firms, especially in the role smaller firms play as the job creators of the American economy.

NFIB believes that the current UI system, if you define it as a program which is supposed to provide temporary help to people between jobs, is working well. Changing the nature of the program could cause serious problems.

In fact, changing the nature of the program to expand it to take care of other purposes, we believe, would endanger the overall health of the program.

Changing the program in a recession would very likely have a negative impact upon the economy, and changing the program by dramatically increasing payroll taxes is very likely to have a negative impact upon smaller firms and their ability to create jobs which, in turn, will help lead us out of recession.

There have been a number of suggestions made to change the UI program. One is to expand the trust funds as an antirecessionary

measure, to make sure that the trust funds have enough money in them to take care of all possible demands that may be placed upon them. The second is to increase the length of benefits available to the unemployed.

NFIB believes that both of these suggestions are unnecessary at this time; and I would like to briefly go into our reasons why.

First of all, the question of the adequacy of the trust funds is a question that reasonable people can disagree on. In fact, Mr. Chairman, it is more like a balancing act.

Too much money being pulled out of the economy in taxes is going to hurt the economy, especially during a recession. Too few funds for the trust funds will mean that taxes will have to be raised too much at any given time.

Most of the State funds will weather the current recession; and the few that won't have two options. One, they can raise taxes temporarily; or two, they can borrow from the Federal Government to tide them over.

In terms of expanded benefits, Mr. Chairman, we do look at the program as a temporary program to help those people who are between jobs. The program provides 26 weeks of benefits and an additional 13 weeks of extended benefits when unemployment is high.

According to the latest figures available from the Department of Labor, 88 percent of those people who went on unemployment compensation found new jobs before the 26 weeks were up.

Providing benefits for much longer periods will change the fundamental nature of the UI program. Its funding source, its structure, its delivery system are simply not suited to a longer program.

You and I believe the UI system is not meant to address a societal problems of the long-term unemployed or displaced workers in this country. These problems very well may need addressing, but not through the unemployment compensation program.

We do not believe that the program should be turned into a social welfare program for the long-term unemployed. In conclusion, Mr. Chairman, the current unemployment system provides 26 weeks of benefits for people who are out of work and between jobs.

In addition, the current system provides an extra 13 weeks of benefits to workers who are out of work and happen to be living in States where unemployment is high.

According to the Department of Labor, only 12 percent of the unemployed were out of work for more than 26 weeks. The current system was not designed to provide for, and cannot afford to provide for, individuals who are unemployed for very long periods of time.

The Federal Government already has an intricate safety net of programs designed to help those whose income has dropped below a certain level. After current unemployment benefits end, workers are not left totally out in the cold. They may be eligible for benefits from AFDC, Medicare, food stamps, WIC, school lunch programs, etcetera. The unemployment insurance system was not designed to be a worker welfare program; and it can only be converted into such a program at great cost to the national economy.

In the midst of a recession and gradually increasing unemployment, legislation boosting unemployment insurance benefits will increase the cost of hiring workers. The last thing Congress should

do in the midst of an economic downturn is to increase a tax on jobs.

Congress should be encouraging employers to hire more employees, not discouraging them from doing so. Thank you, Mr. Chairman.

Senator BREAUX Thank you very much, Mr. Motley, for appearing on behalf of NFIB and also being with us on this important day for you. Happy birthday.

[The prepared statement of Mr. Motley appears in the appendix.]

Senator BREAUX. Let me ask the general question—and it may have been brought up when I was not here: Is there an incentive for some States to, in fact, enact lower unemployment benefits as a means of creating some sort of a better business climate?

My own State, for instance, has the lowest unemployment benefits in the nation; and that may be used to say, well, bring your business to Louisiana because, if you have unemployed, you are not going to have to pay very high unemployment insurance.

Does that present a problem for unemployed workers, that States could begin to compete for who can have the lowest unemployment insurance benefits?

Mr. MOTLEY. States, indeed, act in very strange ways when it comes to competing with each other to entice businesses across their borders.

The other side of the coin, Mr. Chairman, is that I think State legislators generally tend to be very close to the situation back home. If anybody should feel for those who are unemployed, it is the legislators who represent the citizens who live there.

It is sort of a time-tested tradition in the United States that the government that is closest to home is the government that generally tends to work best; and the further we get away, the more difficult it is to make things work.

We would very much agree with that premise.

Senator BREAUX. You would not support any type of a uniformity on the national level as far as benefits tied to some per capita income measure for the State?

Mr. MOTLEY. No, we would not support that, Mr. Chairman, not at this time. I don't think we have taken a very close look at that particular proposal, and we would be more than happy to do so; but at this time, we wouldn't support that.

I don't know if we would oppose it either, although it would dramatically change the nature of the current system. And as I said, we tend to feel that the current system works fairly well, if you take a look at what it was designed to do.

Now, if we want to take a look at other things, then we can all sit down and try to design a different type of system, a supplemental type of system. But the current system, if you take a look at what it was designed for, we believe works fairly well.

Senator BREAUX. I think I heard Mr. Thodis say that there may be a need to extend the benefits from a time standpoint. He didn't come out, I know, in favor of it; but there was some implication—at least I think I heard it correctly—that there may be a need to extend the benefit period. I take it you disagree with that?

Mr. MOTLEY. We would disagree with it in the current situation. I wouldn't come right out and say that there is never going to be a need to extend the benefit period.

In particularly severe recessions, I think that is something that Congress is going to have to take a look at; but this recession doesn't look like it is going to be particularly severe.

The economic data that we collect on a monthly basis would indicate that our membership is looking at the economy in a very positive way in the very immediate future.

Senator BREAUX. You pointed out about the no increase in unemployment taxes over a substantial period of time; they have not gone up, but Social Security taxes in fact have gone up, I guess seven times in the last decade.

Mr. MOTLEY. Yes.

Senator BREAUX. Is that an indication of support for the premise that Senator Moynihan is proposing on the reduction of Social Security taxes?

Mr. MOTLEY. Yes. NFIB supports this Moynihan proposal. In addition, I think the problem that you have in trying to use the UI program to pay for extended benefits is really how much can you raise a payroll tax and not have a dramatic impact upon the creation of jobs.

If you view a payroll tax as a hurdle that the employer has to overcome every time he or she makes a decision to hire somebody, then you have to assume at some point the hurdle is going to get too high. And that is really going to have a tremendous impact upon the ultimate decision of whether or not to hire additional employees.

One of the things that has made this economy so strong over the last several decades is the fact that we do create jobs at such a rapid pace.

If you compare the unemployment system in Western Europe, which is what we are generally most compared to, and the United States, the duration that people are out of work in the Western European democracies is a tremendous difference—2 to 3 years in some cases—because they are not creating jobs.

And they are not creating jobs because so much of the taxes that they use to support their social welfare system over there are pegged to the job itself. Therefore, the decision to hire is a momentous decision over in Europe.

The decision to hire in the United States is much less so. I think we are terribly concerned if the current trend continues that we are going to reach the same situation, taking the great flexibility that we have in our current system and doing away with it.

Senator BREAUX. I appreciate your response; and of course, the committee appreciates your appearing on behalf of NFIB. We look forward to having the benefit of your input and working with you as we move along on this particular problem. Thank you very much.

Mr. MOTLEY. Thank you, Mr. Chairman.

Senator BREAUX. Let me go ahead and ask the following witnesses, who are scheduled, to please join as one panel. We will bring up Mr. William Grossenbacher, who is administrator of the

Texas Employment Commission, representing the Interstate Conference of Employment Security Agencies.

And also, at the same time, I would ask Dr. Gary Burtless, Senior Fellow from the Brookings Institution and Dr. Robert Topel, professor of business economics and industrial relations at the University of Chicago, to come on up, please. We will take the testimony from everyone.

You have all been here for a long period of time. If you could summarize your statements, it would be very much appreciated.

Mr. Grossenbacher?

STATEMENT OF WILLIAM D. GROSSENBACHER, ADMINISTRATOR, TEXAS EMPLOYMENT COMMISSION, AUSTIN, TX, REPRESENTING THE INTERSTATE CONFERENCE OF EMPLOYMENT SECURITY AGENCIES, ACCOMPANIED BY CHERYL TEMPLEMAN, UNEMPLOYMENT INSURANCE DIRECTOR

Mr. GROSSENBACHER. Mr. Chairman, I am Bill Grossenbacher. I am the administrator of the Texas Employment Commission, and I am the president-elect of the Interstate Conference of Employment Security Agencies, which represents the administrators of the all the various employment security agencies around the country.

I have asked Ms. Cheryl Templeman to come with me today, who is UI associate with the Interstate Conference here in Washington.

To be very honest, it is very difficult not to be quite redundant after all the testimony of the witnesses this morning. We have prepared in-depth testimony, and we would ask that our written testimony be included in the record.

Senator BREAU. Without objection.

Mr. GROSSENBACHER. I would just like to take a few moments to visit two or three issues that we think are very important for this committee to look at.

One is the discussions on the number of unemployed individuals actually filing and receiving benefits, the gap that has been discussed throughout this morning. What we would recommend is that a review be made of the Federal legislation and the restrictions that were enacted in the early 1980's; and we have some examples of those laid out in our written testimony.

The position of the Interstate Conference is that those issues, those policies and laws, actually be repealed or considered for repeal by Congress.

Our second issue involves and also includes a discussion on the Extended Benefits Program.

While there is really no consensus among the State administrators on the various trigger levels for the Extended Benefits Program, we would just like to place in the record and for the awareness of the committee that many of the States, in terms of working on their trust fund projections and their revenue systems in the various States, have based that on the current trigger mechanisms and that, when Congress is looking at changing those or doing different things, experimenting with different triggers, that they remember that States need a year, and in some cases up to 2 years, to react to those changes, based on the times that the State legislatures meet.

The most critical issue that we would like to call the committee's attention to has to do with the administrative financing issue. Many of the comments that have been made this morning in terms of the long lines in the employment offices—Representative Levin talked about that—from someone who actually administers a State employment security operation, the administering finance is just critical to us.

For the past 10 years, we have been reducing our staff, reducing our automation, barely holding our own in terms of carrying out these various programs for the unemployed.

We would ask that the Congress consider actually three things.

First, we would ask that it be considered that the UI trust funds actually be moved off budget; and we know there will be opposition to that. Second, in lieu of moving the trust funds off budget, we would ask you to consider moving the administrative funding for the unemployment insurance operations from the discretionary to the mandatory category. I believe that was mentioned earlier this morning.

And third, we would ask you to consider some type of a reserve fund in order to handle the fluctuations in unemployment workloads that occur around the country.

One other issue we would like to comment on has to do with the solvency of trust funds. We spend a great amount of time working with both our labor representatives as well as our business community in fine-tuning our State unemployment insurance law.

For instance, in our State, we have a benefit escalator, but we also have provisions to give tax credits to employers when the ceiling of the fund reaches a certain level. I would simply caution the committee in terms of national standards and so forth.

I would ask you to look at the kind of work that is actually done at the State level to establish the solvency of the funds; and I think the consensus of the Interstate Conference is that trust fund solvency really should remain a State issue as opposed to a Federal issue.

Thank you.

Senator BREAUX. Thank you, Mr. Grossenbacher. Dr. Burtless?

[The prepared statement of Mr. Grossenbacher appears in the appendix.]

**STATEMENT OF GARY BURTLESS, PH.D., SENIOR FELLOW, THE
BROOKINGS INSTITUTION, WASHINGTON, DC**

Dr. BURTLESS. Thanks. I am glad for the invitation to testify before this committee. I have prepared a lengthy statement answering the questions that were posed in Senator Bentsen's letter of invitation; but I would like to just comment briefly on a few of the main points.

The Nation's unemployment insurance system is in poor health. Contrary to some reports, it is not a death's door, like some savings and loans I can think of; but it is in poor health. It belongs in bed.

Changes in the system over the past decade have hurt the adequacy of benefits, reduced the coverage of unemployed, and diminished the effectiveness of the program as an automatic economic stabilizer.

The percentage of unemployed collecting regular State unemployment checks has fallen; it has fallen about one-fifth compared with the situation before the early 1980's.

Some of this decline occurred, as we just heard, because of changes in the geographical location and industrial attachment of the unemployed; some occurred because of the secular increase in the duration of unemployment in this country so that more people exhaust benefits.

But most of the decline is probably due to changes in State eligibility rules and administrative practices and to the declining after-tax value of benefits. For most people thinking of filing a claim for unemployment insurance, there is a hassle that is involved; and they weigh the hassle against the benefits they can expect to receive.

As the benefits have diminished because of benefit taxation, the hassle might look less promising to some potential applicants.

It wouldn't be strictly accurate to say that the extended unemployment benefits program belongs in a sick bed; a morgue would be more appropriate. For all intents and purposes, the program has disappeared.

It is a stealth program, a safety net that is so invisible that most long-term unemployed workers fall right through it without even knowing it is there.

Over time, the unemployment rate that triggers the program—the IUR—has fallen about one-fifth relative to the civilian unemployment rate; and the IUR, therefore, reaches the critical threshold level needed to trigger benefits very late in a recession or never at all.

If the program is triggered on, experience in your own State, Louisiana, suggests that it triggers off while unemployment remains very high. I happened to be in Louisiana during the week that the Extended Benefits Program clicked off in the mid-1980's, throwing tens of thousands of people off the unemployment rolls, even though it was virtually impossible for many of them to find work in the Louisiana business climate of the mid-1980's.

Over the past 12 years, unemployment compensation has been made completely taxable. This reduces its after-tax value to the people who claim benefits.

I entirely support the idea of including unemployment benefits in the tax base; I think it increases tax fairness. But we should recognize that, by taxing benefits without adjusting their pretax values, we have effectively reduced greatly the income protection and countercyclical stimulus offered in the program.

The impact of the dropoff in the regular program, the virtual elimination of the extended program, and the taxation of all unemployment benefits can be described fairly briefly; and I only repeat what Senator Sarbanes said earlier: Compared with the income protection and countercyclical stimulus available over most of the post-war period, unemployment insurance now provides about one-third less protection and less countercyclical stimulus.

Because the system offers less protection, it is naturally less costly. As a share of the total compensation that employers pay their wage and salary workers, the unemployment insurance tax must be near an all-time low. Howls that the UI payroll tax is ex-

cessive and further increases threaten employment in this country are based, I think, largely on ignorance.

I have an urgent short-term suggestion: Change the extended benefits trigger. I have made a couple of recommendations in my formal statement; but whatever you do, do something.

I would also recommend for your consideration for long-term reform of the system thinking about a different financing mechanism for unemployment benefits, one that gives States stronger incentives to build up healthy trust fund reserves during economic expansions.

The wrong time to address the solvency issue of unemployment insurance is during the middle of a recession. Reform at that point only compounds the effect of the downturn.

Second, raise the wage base used in the UI payroll tax. In many States, the earnings base is now as low as \$7,000 per worker; in only a handful of States is it as much as \$14,000.

As a result, States impose a relatively high tax rate on the initial earnings of new workers that they hire. If, as most economists believe, the burden of the tax is ultimately borne by wage-earners themselves, this means that it is a very regressive tax. It is an extremely regressive way to pay for this program.

Even more strangely, since employers must pay a relatively high rate on initial earnings, the current structure of the tax perversely discourages employment when the economy is struggling to recover, when employers are attempting to put new workers on their payrolls.

So, it seems to me that we should raise the tax base in unemployment insurance to at least \$25,000 and lower the rate; that would seem to me to be a sensible proposal.

Finally, consider giving States firmer guidance in establishing benefit levels, eligibility standards, and payroll tax schedules. States now have scandalously wide differences in the benefits they pay, in the eligibility criteria they impose, and in the tax schedules that they impose on employers.

Between 1979 and 1989, only one in five of the unemployed in Texas, Florida, and Virginia received benefits. The percentage receiving benefits was more than twice that level in California, Pennsylvania, and a number of other States.

Weekly differences in the benefit checks that unemployed workers can draw are almost equally wide. These differences don't arise because the States are struggling with one another to offer good insurance protection. They arise because States are competing with one another to get employers to locate in the State.

Now, this might work for an individual State so that the State might get an additional employer. But for the Nation as a whole, it cannot work. We are not going to get any additional jobs or any additional companies in this country because an employer happens to locate in Wisconsin instead of Tennessee or in California instead of Texas.

In a rational system, I think we would try to minimize this interstate competition so that the system offers an adequate level of insurance.

Consider what the Social Security system would look like if we permitted every State to offer its own retirement program and

have its own independent tax base for financing old-age retirement benefits. I don't think the elderly or the disabled would like that kind of a system, and I don't see why we impose it on the unemployed.

Thank you.

Senator BREAUX. Thank you, Dr. Burtless.

[The prepared statement of Dr. Burtless appears in the appendix.]

Senator BREAUX. Dr. Topel?

STATEMENT OF ROBERT H. TOPEL, PH.D., PROFESSOR OF BUSINESS ECONOMICS AND INDUSTRIAL RELATIONS, UNIVERSITY OF CHICAGO GRADUATE SCHOOL OF BUSINESS, CHICAGO, ILL.

Dr. TOPEL. Thank you for inviting me to testify. I was given a broad mandate by the person who invited me to testify. He asked me to come to Washington and say whatever I want about the unemployment insurance system.

It is difficult for a professor to say no to that kind of an invitation; so, here I am.

A substantial part of my research over the last 10 years has been devoted to understanding unemployment, including the important role played by the unemployment insurance system. That system was put in place to soften the blow of job loss by creating a continuing source of consumption income for recently displaced workers.

In many ways, the system is a success. Yet based on the research findings from a number of sources, I believe that the unemployment insurance system in the United States is badly in need of reform.

My testimony, which I have included separately, addresses two major shortcomings of our current unemployment insurance system.

First, the current system provides insurance for small losses where insurance is least needed, while leaving uncovered the large losses caused by long spells of unemployment. Since long unemployment spells have recently become a much more important component of overall unemployment, this aspect of the system should cause concern to policy makers.

Second, our current methods of financing unemployment insurance offers substantial subsidies to employers who engage in layoffs. This means that unemployment insurance causes unemployment in a very real sense. The subsidy to unemployment is an artifact of the way State systems have financed unemployment insurance since the 1930's. The subsidy can be reduced or eliminated without affecting the benefits that are available to displaced workers or by increasing taxes paid by employers.

In light of these shortcomings, I propose two basic reforms of the unemployment insurance system. These are long-term reforms that are not targeted specifically at the current recession or at the issue of whether benefits should be temporarily extended to the long-term unemployed. I believe that the current policy debate is excessively focused on the short term, to the detriment of the effective operation of the UI system.

These reforms are designed to make unemployment insurance operate as a more effective source of income insurance for workers who have lost their jobs. They would not increase the tax burden of unemployment insurance or the cost of running the system. In fact, they would probably reduce unemployment insurance taxes, and unemployment as well.

The first reform is to reallocate benefits over the duration of people's spells. Most of the discussion today has focused on extending benefit programs. I think that discussion focuses too closely on the current situation while ignoring the fact that long spells are always the most costly unemployment spells that people can experience.

Many unemployment spells are very short. Evidence and common sense suggest that they are not very costly to those who experience them. Other spells, however, are quite long, lasting 6 months or more; and they are very costly. These spells are common among more senior workers who have displaced from a long-term employment relationship. Paradoxically, our current system provides more insurance for the first type of spell than for the second. I believe that the UI system should provide greater coverage for the long-term unemployed, and I am confident that this coverage can be achieved without increasing taxes.

As it turns out, each \$1 increase in benefits available to the long-term unemployed will cost only 25 cents in reduced benefits for the short-term unemployed.

In light of that tradeoff, I propose an increase in waiting periods to collect unemployment insurance benefits to a month, with the savings to be used to extend UI coverage for the long-term unemployed for as long as 1 year. This change would significantly improve the role of unemployment insurance as an insurance program for people who have been displaced from long-term employment relationships.

The shift in the timing of benefits would be budget balancing; so, there would be no increase in program costs. Other incentives that are created suggest that total costs would actually fall.

My second proposed reform deals with financing. I believe that we should enhance the experience rating of unemployment insurance tax rates now paid by employers so that tax contributions to unemployment insurance funds are more closely tied to benefit withdrawals.

As I noted, current systems of financing subsidize benefit payments of persistently high unemployment firms. This subsidy increases unemployment for two reasons.

First, high unemployment firms pay less in taxes than their workers collect in benefits. So, unstable industries are encouraged to expand.

Second, the system provides incentives for every employer to engage in temporary layoffs.

I propose simple changes in methods of experience rating that would reduce or eliminate those subsidies. A substantial body of research suggests that these changes would reduce unemployment, which means that they enhance overall productivity and welfare. This also means that they would reduce the overall cost of running the unemployment insurance system.

That is the end of my remarks. Thank you very much. •

[The prepared statement of Dr. Topel appears in the appendix.]

Senator BREAUX. I thank the panel for being with us all morning and for your presentations.

Let me ask anyone to comment on the question that has been mentioned by other witnesses, as well as yourselves. My own State of Louisiana—and Texas is very similar—went through some very difficult times during the decade of the 1980's with unemployment. We had the highest in the Nation for almost 10 years.

I noted that in 1987, Louisiana had qualified for the Extended Benefits Program, and then we became unqualified, yet our unemployment was still way up; over 10 percent of the State was unemployed.

Witnesses have talked about a change in how we calculate that. Mr. Grossenbacher, do you agree with that?

Mr. GROSSENBACHER. Well, Mr. Chairman, we had the same situation as you talked about in Texas. At the height of our recession in 1986, which I think was the year we paid out over—I guess we had borrowed over—\$1 billion to make our UI payments, we never triggered on EB, even though we had a double digit total unemployment rate.

I think perhaps there may be some serious consideration of going back to the triggers that were in force prior to this last congressional change.

Senator BREAUX. Would that be just considering the total unemployment as opposed to the gap comparison?

Mr. GROSSENBACHER. Well, I think it would go back to lowering the triggers by 1 percent. That might be what we would like to see from a Texas perspective. There is a lot of discussion about using the TUR versus the IUR and so forth.

The only problem I have with using the total unemployment rate is that, in Texas—and I think it was mentioned earlier—I think that rate is determined by about 1,500 households in the State of Texas on the survey, and that TUR tends to jump around an awful lot on a monthly basis.

Perhaps if you wanted to use the TUR and set it up for a longer term look of, say, 6 months or something like that, perhaps you could do it. But I have some real reservations about the TUR as the trigger.

Senator BREAUX. Well, our total unemployment in Louisiana has come down; but I am not so sure it is because of the new jobs as much as it is that people have just left the State and gone somewhere else to look for jobs.

Dr. Burtless or Dr. Topel, do you have any thoughts on that point?

Dr. BURTLESS. Well, if we had the extended unemployment insurance triggers that were in effect before October 1982, seven States that do not now have the Extended Benefits Program turned on would have it turned on. And those States include California, New York, and New Jersey.

They are 3 of the 10 largest States, including the largest two. So, obviously, this would have a very major impact; it would probably much more than double the number of people currently collecting extended benefits.

So, moving back to the old trigger would help; but the thing we have to remember, when we look at this list of States that would be triggered on, is that there is still a great inequity.

And that inequity is that States like Louisiana and Texas, where the qualifying requirements for unemployment insurance benefits are harder than they are in the northeast and in the upper Midwest, would seldom reach the trigger levels, even under the law that was in existence before 1982.

I have to question, as a Federal taxpayer, whether it really makes sense for Federal taxes to be spent for a program that primarily benefits people in States where there are relatively generous qualifying requirements for regular unemployment benefits because, in the end, that is what moves the insured unemployment rate.

It is the degree of difficulty that the unemployed workers have in qualifying for State benefits in their local area.

Senator BREAUX. And you point out that unemployment insurance is in poor health and that the extended benefits belong in the morgue already.

Dr. BURTLESS. Well, I think there are now eight States in which the program is in effect—the Extended Benefits Program is in effect. So, it has certainly perked up a lot in the last 3 months.

But even so, I think the number of States offering benefits is way, way below where it would have been had the same fraction of unemployed been receiving regular benefits as we saw before 1981. For example, in the 1970 recession and the 1974-1975 recession, and in the 1980 recession, far more States offered extended benefits.

So, I think, yes, it is near death's door.

Senator BREAUX. Mr. Grossenbacher, what about the suggestion of Federal guidelines? I have some concern about States competing for industries by having lower unemployment benefits or rates or triggering mechanisms.

Is it appropriate for the Federal Government to have more detailed guidelines for the States in setting standards?

Mr. GROSSENBACHER. Mr. Chairman, speaking from a Texas perspective, we would prefer to leave that to the individual States. You know, in my experience, I have seen our benefits in Texas or our law go from conservative to somewhat liberal, going back and forth.

And I think a lot of discussion and a lot of thought go into that, as I mentioned before, between organized labor in our State, as well as the Texas Association of Business. I really don't think there is a plot to reduce benefits in order to attract industry to the State of Texas.

I think when we sit down and look at our unemployment insurance law, there is a fair give and take between business and labor and particularly during the recession, when we had to begin the rather tough payback to the Federal Government for our borrowing.

The compromise was about a 300-percent increase in UI taxes and a 2-year freeze on benefit escalation. That was the agreement that was reached between business and labor in our State.

As I say, as that went off and we became solvent, now we have an agreement that we reinstated our benefit escalator. Our weekly benefit amounts are among the highest in the country, I think; I think it is something like \$224.00 a week.

Also, there is the fact that, at this point, we are fortunate that our trust fund is about \$1.3 billion; and we have a provision to give back in tax credits to employers in the amount over that billion dollar ceiling.

Again, that was a conscious decision that was hammered out between business and labor and seems to work well. You know, I can't speak for all the States; but in general, I think the system of having the individual States set their own laws and their own limits has been a good one.

Senator BREAUX. Dr. Burtless, I know your recommendation on that. Dr. Topel, do you have a thought on the Federal guidelines for some of these triggering mechanisms and standards?

Dr. TOPEL. Like all economists, I will tell you there are costs and there are benefits. I have been in situations with State administrators where they have confessed to their efforts to attract business to the State by manipulating the tax rates.

So, on the one hand, there is not much of a gain, as Gary Burtless has pointed out, in terms of aggregate employment across the Nation in terms of location of firms within particular States.

At the same time, the competition among the States is something of a brake on any tendencies to increase spending rapidly on unemployment insurance systems.

And so, it operates as an incentive for State legislators to keep the total costs of the program down. So, it goes both ways.

I wanted to make one other point that echoes earlier discussion; and that is that if we are going to have extended benefit programs that are based on the total unemployment rate, the number of individuals in many small States is quite small, given the current way that we collect unemployment statistics.

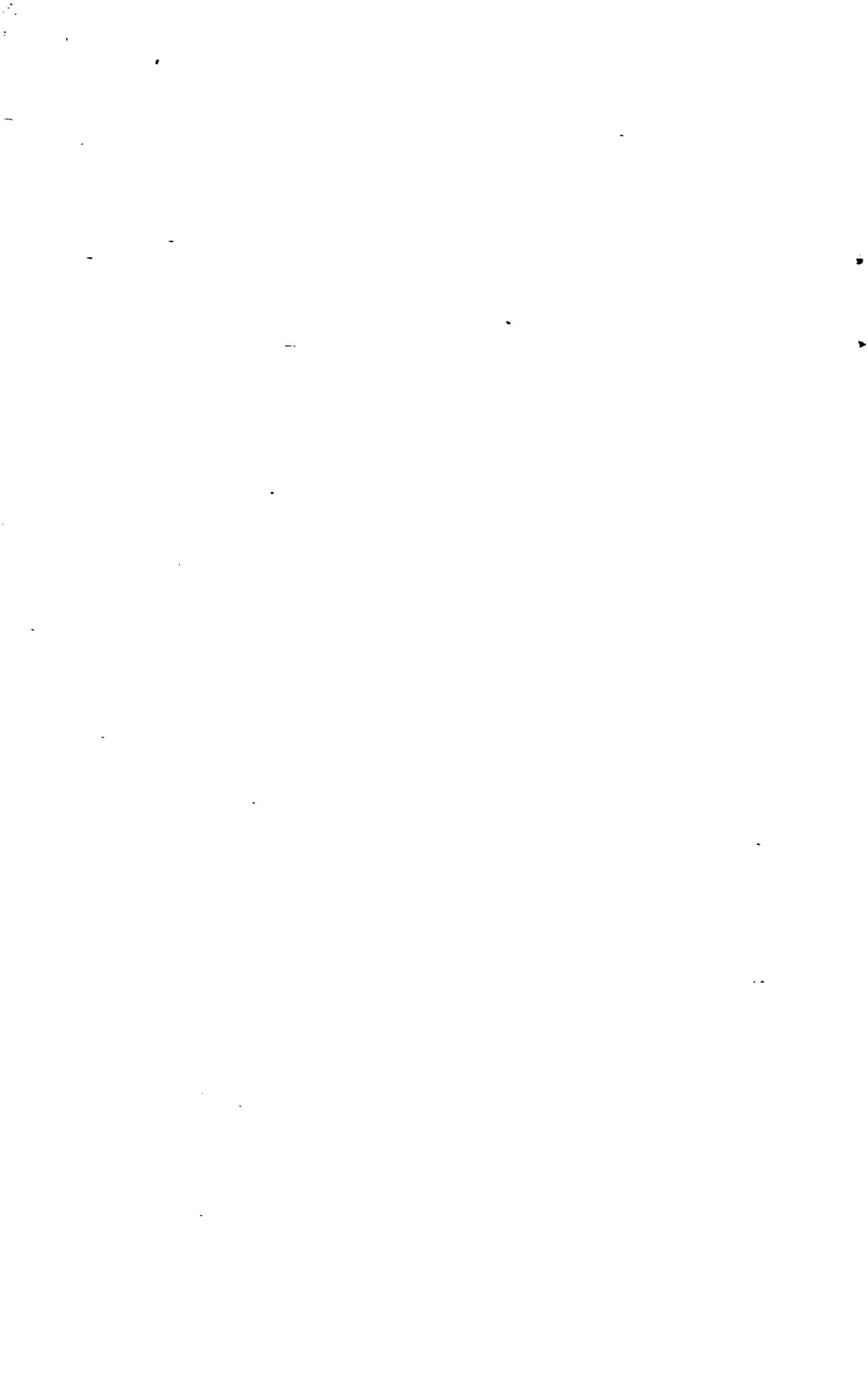
And so, for them to change the triggering mechanism in that way, it is going to involve a substantial revision of the way we collect unemployment statistics in the United States, not unemployment insurance statistics but the way we count the unemployed and the size of the samples that we would have to use to do that.

Senator BREAUX. All right. I think all of you have made some very good suggestions, particularly our two professors; and Mr. Grossenbacher, you have given us some pragmatic suggestions. We appreciate your being with us and your testimony before the Finance Committee.

With that, this will conclude our hearing this morning. We thank all of the witnesses.

The committee will stand adjourned until further call of the chair.

[Whereupon, at 12:50 p.m., the hearing was adjourned.]



APPENDIX

ADDITIONAL MATERIAL SUBMITTED

PREPARED STATEMENT OF KEITH BROOKS

The New York Unemployed Committee (NYUC) has been denied permission to address the April 23 U.S. Senate Finance Committee hearing on unemployment problems.

Two busloads of NYUC members will be leaving at 5 am on Tuesday morning in order to attend the 10 am hearing in Washington. The buses will leave from the Unemployment office at 4th avenue and Dean street in Brooklyn.

Responding to the Finance Committee denial to let the unemployed testify, NYUC member Nelson Valentin said "they are going to hear from everybody except the real experts on unemployment. They don't want to hear from the people who are behind in their rent, who have exhausted their unemployment benefits, or who have not received a check in a month. But *that is why we are going to Washington—to make sure they get the message from the unemployed themselves!*"

It is also a sad commentary on how our government views the unemployment problem that the Senate is first holding *hearings* on the problem at this late date, notes another NYUC member, Joan Shepard. While a bill has been introduced in the House of Representatives (H.R. 1367) to provide more weeks of benefits and make other changes in the unemployment insurance system, *the Senate has yet to act.*

Over 200,000 people used up all their unemployment benefits last month nationwide. While these people are left without a job or source of income, \$8 billion sits almost untouched in a special Federal account for extending unemployment benefits. The quickest way to access this account would be for the Congress and the President to declare this an emergency item. "We demand that our elected officials recognize the miserable failure of the unemployment insurance system to deal with the needs of jobless workers during this recession and *declare this is an emergency item*" said NYUC coordinator Keith Brooks.

U.S. Senator Patrick Moynihan, who sits on the Finance Committee, has agreed to meet with the NYUC after the hearings.

NYUC members include blue collar and white collar, union and non-union workers. The cost of the trip has been funded by the Newspaper Guild of New York, Communication Workers of America Locals 1180 and 1150, Local 802 American Federation of Musicians, United Autoworkers Local 259 and other donations.

NEW YORK UNEMPLOYED COMMITTEE DEMANDS CONGRESS AND PRESIDENT DECLARE THE PLIGHT OF THE UNEMPLOYED A NATIONAL EMERGENCY

We would all rather be working today, but we came to Washington DC today to attend these hearings because we want to make sure that our elected officials get our message first hand—the Unemployment Insurance system stinks. It is failing miserably to provide protection to jobless workers in this recession. With over 200,000 people exhausting all benefits every month, the 26 weeks of unemployment benefits available is simply not enough.

It is an outrage that while we fall behind in our rent, put off medical care, and scrape to survive without a job or source of income, that there is an *\$8 billion dollar fund* intended for more weeks of unemployment benefits that only six states qualify for.

And it is an outrage that while we sometimes wait 4, 6 even 8 weeks for our checks because of understaffed and overburdened unemployment office staffs that over \$1 billion sits unused in another fund intended for running the centers.

We demand that this money, already collected through a tax on employers, immediately be made available to the unemployed. The quickest way to gain access to this fund would be for the Congress and the President to declare this an emergency item. This is an emergency item—**WE ARE IN A STATE OF EMERGENCY WITHOUT A JOB OR SOURCE OF INCOME!**

It is time for Congress to wake up and take action. It is an outrage that the Senate is first holding hearings on the unemployment problem at this late date—as if they do not know there is a problem.

It is also an outrage that the unemployed have been shut out and denied the opportunity to testify at these hearings today. But they cannot ignore the problem—and they cannot ignore the unemployed. We are here to make sure our demands for more **WEEKS OF UNEMPLOYMENT BENEFITS, TO GET OUR CHECKS ON TIME, AND FOR REFORMING THE UNEMPLOYMENT INSURANCE SYSTEM** are clearly heard.

We do not want to hear any nonsense about how this recession is already over. And shame on those whose attitude is to wait for the recession to end—instead of really putting maximum pressure on our government to protect the unemployed.

We call upon the U.S. Senate, the House of Representatives and President Bush to immediately declare the need for extending benefits and reforming the unemployment insurance system an emergency budget item. **RELEASE THE \$8 BILLION FUND NOW!**

PREPARED STATEMENT OF GARY BURTLESS ¹

OVERVIEW

The nation entered recession in the last quarter of 1990. But the country's unemployment insurance system entered this downturn in worse shape than ever at the start of a recession. The system was designed to serve two critical functions. It should provide workers with essential income protection during temporary spells of unemployment. And by helping to sustain the consumption of jobless workers, it should give the economy a needed counter-cyclical boost during periods of high national unemployment.

Changes in the system over the past decade have reduced the adequacy of unemployment benefits and diminished the effectiveness of the program as an automatic stabilizer. The percentage of unemployed now collecting insurance benefits is about one-fifth below levels that were typical before the early 1980s. Moreover, the value of unemployment insurance shrank in the past decade as a result of the decision to make benefits completely taxable. In the short run, Congress and the President should shore up the system by reforming the way we provide extended benefits to the unemployed in slack labor markets. Over the longer term, the program should be strengthened by reform of its financial structure and increased harmonization of eligibility and benefit formulas across states.

In the remainder of my testimony, I discuss why the protection offered by unemployment insurance has fallen so much in the past decade, how Congress can revamp the system in the next few months to make it work better during the current recession, and what steps could be taken in the long run to improve the effectiveness of the system. I begin with a brief discussion of the labor market effects of unemployment insurance.

EFFECTS OF UNEMPLOYMENT INSURANCE

Unemployment insurance (UI) offers vital income protection to experienced workers who become jobless because of involuntary layoff. In spite of the crucial economic role played by the program, it suffers from a somewhat unsavory reputation among a few economists, journalists, and policymakers. This is because unemployment benefits can prolong spells of joblessness among workers who are eligible to receive benefits. Workers collecting a weekly unemployment check might not devote as much time or effort to finding a new job as workers who do not collect benefits. Even more important, insured workers might reject a job offer that an uninsured worker would accept, because the income cushion provided by UI permits them to be choosier in accepting a job. Economists say that these behavioral effects of unemployment insurance represent "adverse incentives" of the program.

¹ Senior Fellow, The Brookings Institution, Washington, D.C. I am grateful to Suzanne Smith of Brookings for help in preparing this testimony. The views expressed are solely my own and should not be ascribed to the staff or trustees of the Brookings Institution.

Policymakers were aware of adverse incentives when they designed the current system. To reduce the influence of these incentives, Federal and state legislatures imposed two important conditions on insurance. First, benefits can only be paid to unemployed workers who can demonstrate they are available for and actively seeking work. And second, benefits can be denied to workers who reject an offer of "suitable" employment (meaning a job roughly equivalent to the job that was lost). These two conditions are notoriously difficult to enforce in practice, so the American system of unemployment insurance possesses one other notable feature: Benefits are generally limited to only 26 weeks. Unemployment lasting longer than 26 weeks is not ordinarily compensated in this country. By international standards, this level of protection is very brief. Virtually all other industrialized countries offer at least a year of unemployment insurance benefits, and in several countries the duration of benefits is much longer.

In spite of these limitations on American benefits, many economists and policymakers suspect that unemployment insurance contributes to the high level of unemployment we now suffer. A variety of analysts have examined the size of the adverse impacts of unemployment insurance and concluded that more generous benefits do indeed prolong average durations of unemployment among insured workers. A good guess is that a 10-percent increase in weekly benefits prolongs the average duration of unemployment by around one week. A one-week increase in the potential *duration* of benefits (from, say, 26 weeks to 27 weeks) would increase the average length of an insured unemployment spell by about one-tenth of a week, or perhaps a bit more. An honest assessment of jobless benefits must therefore conclude that some of the adverse consequences that economists worry about do in fact occur.

These adverse consequences do not take us very far, however, in explaining the current level and trend in national unemployment. Only about four in ten unemployed workers collect unemployment benefits, and nearly all of the insured became jobless because of a layoff that was in no way caused by the existence of the program. Thus, if insurance were eliminated altogether, the level of joblessness would fall only slightly. Furthermore, if some of the *insured unemployed* experience longer spells of unemployment because of the existence of the program, it must also be the case that some *uninsured unemployed* workers experience *shorter* spells, because they are more likely to land a job that has been turned down by an insured unemployed worker. In a labor market with a long queue of workers seeking jobs, a job vacancy that is rejected by a worker collecting benefits will be quickly snapped up by an uninsured worker desperate to find employment.

More fundamentally, it is the goal of unemployment insurance to permit insured workers to reject unsuitable job offers. We provide jobless benefits in this country (and in other advanced industrialized economies) precisely because our workers must acquire costly skills that can often be applied only in relatively specialized occupations or jobs. When workers lose these jobs because of a downturn in demand, it is advantageous for them and for the wider economy if they carefully seek out the best opportunity to apply their specialized skills. If there are two unemployed workers and two job vacancies, it is economically efficient to subsidize the workers to sort themselves into the two job openings so that their skills are put to best use and their earnings are maximized. The two workers benefit and the wider economy gains if the best possible match between workers and vacancies occurs. Furthermore, the insurance protection provided under UI encourages workers to undertake investments in specialized skills that otherwise might be regarded as excessively risky. On balance, I think that some economists (and most editorial writers at the *Wall Street Journal*) tend to exaggerate the adverse effects of unemployment insurance and ignore the vital function it plays in protecting skilled and semi-skilled workers against the hazards of job loss. Sadly, they also ignore the program's efficiency *promoting* impact on the labor market.

DECLINING UI COVERAGE

Whatever the effects of unemployment insurance, positive or negative, they have shrunk in recent years. In the 1980s joblessness rose to new post-war highs, but the share of unemployed workers drawing unemployment benefits fell to new lows. The percentage of jobless workers collecting benefits has risen modestly in the past couple of years, but still remains well below the level prevailing before the mid-1980s (see Figure 1).

The proportion of unemployed collecting benefits declined for several reasons. First and most important, fewer unemployed workers now apply for benefits when they lose their jobs. In part the drop in applications is due to a change in unemployment insurance eligibility requirements, which are established both at the state and national levels. In addition, some unemployed workers may have decided against ap-

plying for benefits as the after-tax value of those benefits fell. Finally, the nature of unemployment has changed over time.

The unemployed are now drawn from different industries, geographical areas, and demographic groups than was the case through much of the post-war period. For example, as the nation's population has moved toward the south and west and out of the northeast and midwest, a shrinking fraction of the unemployed have held jobs in states with liberal eligibility requirements. Workers losing their jobs in many southern and western states are less likely to collect benefits than jobless workers in the northeast and upper midwest. (The recent jump in the fraction of jobless collecting benefits is partly due to the sharp increase of unemployment in New England and the mid-Atlantic states, where liberal eligibility requirements are common.) However, careful analysis of the regional distribution of unemployment has shown that this factor can explain only a small part of the decline in insurance coverage over the past decade. The percentage of jobless workers collecting unemployment insurance payments has dropped in every region and nearly every state in the union.

A much more important reason for the drop in the percentage of unemployed collecting benefits is the change in UI law and regulation that has occurred since 1976. Some important legal changes occurred at the Federal level, but many changes were instituted at the state level as state governments responded to shortfalls in their unemployment insurance trust funds by scaling back on benefits. Many of these changes affected the eligibility of unemployed workers to receive insurance benefits. For example, several states have increased their base period earnings requirements, reducing the chances that part-time or intermittently employed workers will become insured. Workers receiving pensions or severance pay are also more likely to be denied insurance benefits or to receive smaller benefits when they qualify.

STATE UI RESERVES

Why did so many states take the unprecedented step of tightening eligibility requirements in the midst of a severe recession? One reason is that most states entered the 1980-82 recession with relatively small trust fund reserves. As the trust funds were depleted by soaring joblessness, state legislatures were forced to boost payroll taxes or slash benefits in order to restore their programs to solvency. In the previous recession of 1974-76, many states had freely borrowed from the Federal Treasury to keep benefit payments flowing. But under legislation passed in 1981, the Treasury began imposing interest charges of up to 10 percent a year on new borrowing. The interest charge placed greater pressure on states to take immediate steps during a recession to ensure that their trust funds did not fall far out of balance.

States were not obligated to restrict eligibility or slash benefits, of course. They might have raised the payroll taxes imposed on employers. In fact, many states did so. But in the anti-tax climate of the last decade, it became difficult for legislators to raise taxes enough to keep their systems financially healthy. Moreover, as labor unions have weakened, the voice of the unemployed has become much fainter in most state capitols. The views of business lobbying groups remain very influential. The net result is a bias against raising taxes and in favor of restricting benefits.

One hopeful aspect of the current situation is the relatively strong condition of most state UI trust funds. This is primarily the result of the very long economic recovery over the second half of the 1980s rather than a carefully considered policy on the part of state governments. An analysis by the Department of Labor's Unemployment Insurance Service shows that most states entered 1991 with healthier reserves than was the case in 1980. Thus, state legislators will not find themselves pressed to trim benefits quite so early in the current recession. Nonetheless, reserves are lower than they were at the start of the 1970 and 1974-76 recessions, and the anti-tax climate is even stronger at the state level today than it was in the early 1980s. If state trust funds face insolvency during the next couple of years, I expect that many state governments will turn to the same remedy they used in the 1980s: curbs on UI eligibility.

Whether states decide to raise taxes or reduce benefits, however, the macroeconomic consequences will be the same. If legislatures act to shore up UI reserves in the middle of the recession, the counter-cyclical stimulus provided by the program will be reduced. The appropriate time to boost reserves is during an economic expansion, not a contraction, but the anti-tax climate of the 1980s worked against the accumulation of adequate reserves.

I should emphasize, however, that much of the current concern about the adequacy of UI reserves is misplaced. Some observers needlessly worry that reserves will prove inadequate to pay for benefits in the current recession. They believe that

shortfalls in state funds will mean that benefit checks will not be written or that a costly Federal bailout of the state funds will be necessary. Based on the past history of the program, neither concern appears well-founded. Even if a state trust fund is exhausted, benefits in the state will continue to be paid, possibly with a loan from the Federal Treasury. States will eventually repay the Treasury with funds raised under the unemployment insurance payroll tax imposed on employers within the state. Contrary to popular belief, the situation is in no way analogous to the savings and loan fiasco. Unlike an insolvent savings and loan, a state can impose taxes on employers to restore its unemployment insurance trust fund to solvency.

The more relevant concern is that states will act with undue haste to raise taxes or reduce unemployment benefits, even as state economies tumble further into recession. A payroll tax hike or benefit cut can actually delay economic recovery by discouraging new hiring and reducing consumer spending in a state. For that reason it is much better to build up healthy reserves during an economic recovery than to try to rescue a depleted trust fund in the middle of a recession.

TRENDS IN COVERAGE UNDER STATE UI PROGRAMS

The percentage of jobless workers collecting regular UI benefits has dropped by roughly 20 percent compared with the level that prevailed before 1980. This estimate is based on analysis of trends in the percentage of unemployed workers who are most likely to be eligible for benefits under the rules in effect before the 1980s. In the U.S. system of unemployment insurance, benefits are not provided to all jobless workers. New labor market entrants and most reentrants into the job market are not eligible to receive benefits, because the program insures only those workers with recent employment in a covered job. In addition, workers who voluntarily leave their jobs may not be eligible for benefits or may be eligible only after a specified waiting period, such as 6 or 10 weeks. This means that the overwhelming majority of workers eligible for benefits will be those who are unemployed because they are on temporary layoff or because they involuntarily lost their last jobs. As noted earlier, the regular state UI programs limit jobless benefits to the first 26 weeks of a spell of unemployment. Thus, the group of unemployed most likely to be insured are involuntary job losers who have been unemployed for fewer than 27 weeks.

Figure 2 shows the number of regular unemployment insurance claimants measured as a fraction of the number of involuntary job losers unemployed fewer than 27 weeks. In previous research, I found that this coverage ratio remained quite stable over the thirteen years from 1967 through 1979. Over that span of years, there were about 108 recipients of regular state UI for every 100 job losers unemployed less than 27 weeks. This ratio fluctuated somewhat over the business cycle, as can be seen in the figure, but it was otherwise reasonably stable.

Beginning in 1980 the ratio of regular UI recipients to short-term job losers fell very sharply. This coverage ratio reached an all-time low in the third quarter of 1984, when it fell to just 71 insurance recipients for every 100 job losers. Since 1984 the coverage ratio has recovered somewhat, until now there are about 85 regular UI claimants for every 100 short-term job losers. In spite of its recent recovery, however, the ratio remains well below its level during the 1960s and 1970s and even below its level during the 1980 recession. The current recession is one in which the unemployment insurance system could provide benefits to a historically low percentage of job losers.

TAXATION OF BENEFITS

In addition to legal changes that directly affected workers' eligibility for regular benefits, several other changes reduced the value of benefits and hence the attractiveness of applying for compensation during very short spells of joblessness. An analysis by the House Ways and Means Committee, for example, shows that Federal taxation of UI benefits reduced their value to unemployed workers by 16 percent.² Because most states with an income tax system use the same tax base defined in the Federal system, many UI claimants now pay state as well as Federal taxes on their benefits. Thus, the combined income tax rate on unemployment insurance benefits probably ranges between 18 and 20 percent on average.

Although it is certainly equitable to include UI benefits in the tax base, taxing benefits without raising benefit levels is equivalent to a sizable benefit cut. Until 1979 unemployment compensation was exempt from all income taxes, and between 1979 and 1986 benefits were taxable only for taxpayers with incomes above certain

² Committee on Ways and Means, U.S. House of Representatives, *1990 Green Book* (Washington, DC: U.S. Government Printing Office, 1990), pp. 467-68.

thresholds.³ The benefit cut not only reduces income protection offered to jobless workers, it also diminishes the effectiveness of unemployment insurance as a counter-cyclical stabilizer. I suspect that it also deters some unemployed workers from applying for benefits.

EXTENDED UI BENEFITS

The extended benefit UI program offers additional insurance protection beyond 26 weeks of unemployment for workers who have exhausted regular benefits and who live in states with high unemployment. The drop in the percentage of unemployed job losers collecting regular benefits has directly affected the insured unemployment rate (IUR), which serves as the basis for triggering extended UI benefits. If I am correct in estimating that the number of regular UI claimants has fallen by one-fifth, then the IUR is also about one-fifth too low relative to the civilian or total unemployment rate (TUR), which provides a more accurate gauge of current labor market conditions.

The relationship between the insured and total unemployment rates is shown in the two panels of Figure 3. Although the IUR and TUR tend to move in parallel fashion over the business cycle, they have drifted apart since 1955. Before 1980, this drift could be easily explained by the changing composition of the civilian unemployed—who were younger, less likely to be job losers, and increasingly drawn from industries with low levels of insurance coverage—and by changing regulations about the insurance coverage of employed workers. After 1980, however, the sharp decline in the IUR relative to the TUR has been almost entirely due to the sharp drop in the fraction of new job losers collecting benefits.

As a result of the drop in the IUR, the extended benefit program has virtually ceased to function. At the moment, only a half dozen states offer extended benefits even though many more states have total unemployment rates exceeding 7 percent. When the employment situation in a state deteriorates, its total unemployment rate rises, but its insured unemployment rate often does not rise by enough to trigger extended benefits. The result is that the extended benefit program either fails to trigger on or triggers on late in an economic downturn. Moreover, even where extended benefits become available, the IUR can be expected to fall below the critical threshold relatively early in an economic recovery. Many beneficiaries are thus dropped from the insurance rolls even though the job market remains very weak.

The extended benefit program also contracted over the past decade because of significant changes in Federal law passed in 1981. Before 1982 the extended benefit trigger rate was computed by including recipients of both regular and extended benefits in the count of insured unemployed. (Thus, the trigger rate used before 1982 was not identical to the IUR, which excludes recipients of extended benefits from the numerator.) Since extended benefit recipients are now excluded, the level of insured unemployment needed to trigger the extended benefit program has effectively been raised. Also, before 1981 the extended benefit program could be triggered in all states if the national insured unemployment trigger rate exceeded 4.5 percent. The national trigger rate was eliminated by the 1981 legislation. Beginning in October 1982, extended benefits have been available only in states in which the IUR exceeds 5 percent and is at least 120 percent of the rate over the previous two years. Some states also provide benefits when the IUR reaches 6 percent, regardless of the rate in previous years. These trigger rates are one percentage point higher than the comparable rates in effect before 1982.

The legislative reforms of 1981, along with the sharp drop in the number of regular UI claimants, had a calamitous effect on the extended benefit program. At the end of 1982, when the civilian unemployment rate reached 10.8 percent—a post-war record—only fourteen states with particularly high insured unemployment rates offered extended benefits. By October 1983, with unemployment still hovering above 9 percent, only two states and Puerto Rico offered extended benefits. In contrast, during the 1974-76 recession, when unemployment reached a high of only 9.0 percent, all 50 states offered extended benefits for prolonged periods. As a practical matter, the extended benefit program no longer operates as an effective counter-cyclical stabilizer. Except in extraordinarily severe recessions, the program is unlikely to offer benefits to a sizable number of workers.

³ The Revenue Act of 1978 taxed UI benefits received by some middle-income and all high-income taxpayers, while the Tax Act of 1982 (TEFRA) reduced the income thresholds for taxation of benefits to \$12,000 for single filers and \$18,000 for married couples filing jointly. The 1986 Tax Reform Act made all unemployment compensation subject to taxation under the personal income tax.

POLICY IMPLICATIONS

An important implication of these developments is that the unemployment insurance system has become a much weaker source of counter-cyclical stimulus during economic downturns: (1) The effectiveness of the extended benefit program has been cut at least in half as a combined result of the legislative changes passed in 1981 and the continued weakness of the IUR as a measure of the labor market situation; (2) The stimulus provided by the regular 26-week program has dropped by one-fifth because of the decline in the number of claimants relative to the number of unemployed job losers; And (3) The stimulus provided under both the regular and EB programs has dropped by an additional 15-20 percent as a result of the taxation of benefits. *In comparison with the level of counter-cyclical stimulus available during the 1960s and 1970s, the stimulus provided by the current system has dropped by at least a third.* The income protection available to jobless workers has dropped by a similar amount.

Reform of extended benefit trigger. Because the IUR is a poor indicator of the condition of the job market, it is a faulty instrument for triggering state-level extended benefit programs. The current trigger is like an oral thermometer that registers a temperature that is 4 or 5 degrees below the patient's actual temperature. The patient might be burning with fever, but the defective thermometer could show a healthy temperature of 98.6 degrees. Under these circumstances, a sensible doctor would throw out the thermometer and try to obtain a more accurate assessment of the patient's condition. We should do the same with the extended benefit unemployment rate trigger.

Given present limitations in state-level unemployment data, the best trigger mechanism must depend on a combination of information about overall unemployment, as reflected on the Current Population Survey, and state-level insured unemployment, as indicated by the IUR or some other statistical series maintained by state UI systems. One possibility is the Bureau of Labor Statistics' estimate of state-level unemployment rates. This estimate is available on a timely basis, although it suffers from somewhat questionable reliability. As a practical matter, I would suggest that we rely on the BLS estimate of the state unemployment rate, which is based on data from the Current Population Survey as well from the state unemployment insurance system. When the state unemployment rate rises above, say 7 percent, states could be required to offer, at least seven weeks of extended benefits. States with BLS-estimated unemployment rates above, say, 9 percent should be obligated to offer seven more weeks extended benefits in addition to the seven just mentioned.

A simpler reform would be to reduce the current insured unemployment trigger rates enough to make the extended benefit program approximately as generous as it was before 1981. Reducing the critical threshold rates about 1.5-1.8 percentage points would accomplish this goal. One weakness of this procedure is that the extended benefit program would remain vastly unequal across the 50 states. States in the south and west typically have lower insured unemployment rates than states in the north and midwest because they make it more difficult for job losers to collect regular unemployment benefits. Thus, in a recession that is equally severe all across the nation, Massachusetts and Michigan might offer extended benefits when Florida and Texas did not. To eliminate this inequity, it is necessary to move away from insured unemployment statistics in triggering extended benefits.

But the first necessary step is to get the extended benefit program working again. We should try to avoid a repetition of the experience of the early 1980s, when the extended benefit program shrank even as unemployment—especially long-term unemployment—rose to new post-war highs.

Long range reform. In the long run it would be worthwhile to consider alternatives to the current method of financing unemployment insurance and of setting eligibility requirements and benefit levels. Experience over the past 15 years suggests that state legislatures are reluctant to build up their UI reserves during economic expansions by enough to weather deep recessions. When a severe recession occurs, state governments often resort to immediate payroll tax hikes or benefit cuts to keep their programs solvent. Either action reduces the effectiveness of unemployment insurance as an automatic stabilizer. A benefit cut also adds unnecessary hardship to the plight of the unemployed. A long-term remedy to this problem is to give states substantial incentives to build up their trust fund reserves during good times, for example, by penalizing states with low reserve ratios if their unemployment rates have remained low over several years. On the other hand, states with low reserve ratios or negative balances in their trust funds should be assured that in recessions the U.S. Treasury stands ready to loan money to replenish reserves at

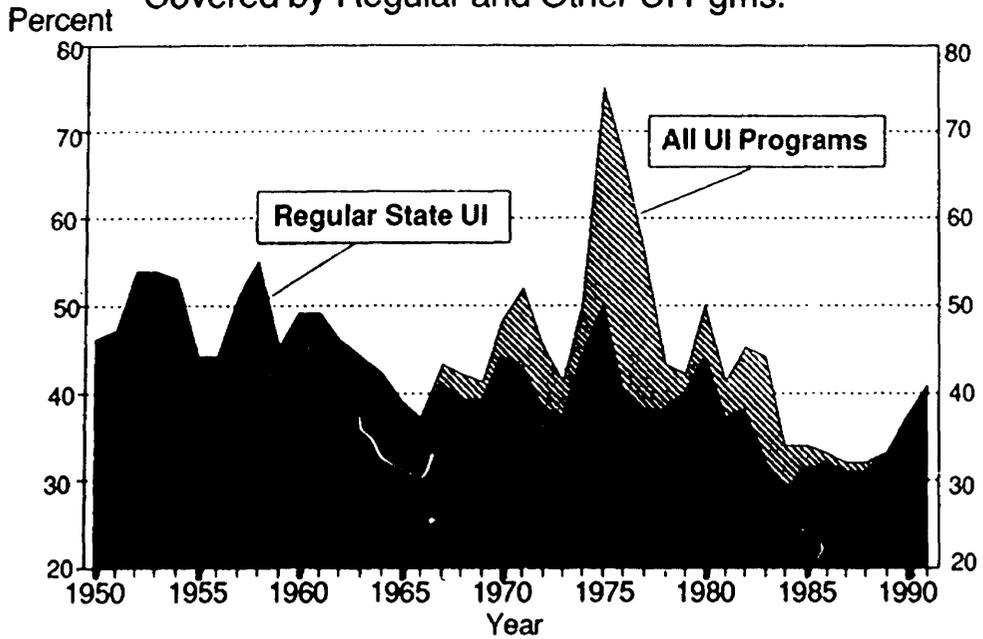
comparatively low interest rates *if the state has experienced high unemployment over a substantial period.*

In addition, it would be useful to raise substantially the wage base currently used to assess unemployment insurance payroll taxes. In many states, the tax base includes only the first \$7,000 of a worker's earnings. In only a handful of states does the wage base exceed \$14,000. Thus, states impose relatively high tax rates on initial earnings rather than lower rates on a much larger base. If the burden of the payroll tax is borne by workers in the form of lower compensation, as most economists suspect, this means that a disproportionate share of the tax is borne by low-wage or intermittently employed workers. The tax is regressive, and it perversely discourages employers from hiring extra workers when the economy improves. In my view, the tax base should be raised to at least \$25,000 in all states.

It would be desirable within the next year or so to consider a thorough overhaul of unemployment insurance. Congress and the President, perhaps with the help of a broadly representative study commission, should ponder whether there are ways to reduce the wide disparities in benefit levels, eligibility standards, and payroll tax formulas that now exist in the 50 states. Many of these disparities unfortunately arise because states feel they must compete in attracting business, usually through a low payroll tax rate. The differences between programs seldom arise because states are competing with one another to offer workers good protection against the hazard of job loss. Yet an effective unemployment system must strike a reasonable balance between the goals of keeping costs low and offering enough income protection to minimize the suffering of jobless workers and their families.

A vital task for policymaking in the coming year is to restore the ability of the nation's unemployment insurance programs to deal with severe recession. A worthwhile start on this task would be a modest reform of the triggering mechanism for extended unemployment benefits.

Figure 1. Share of Unemployed Workers Covered by Regular and Other UI Pgms.



All Programs include state UI, UCFE, UCX, RR, EB, FSB, SUA, and FSC.
Data for all programs begin in 1967. SOURCE: DoL/ETA/UIS.

Figure 2. Number of Regular Benefit Claimants for Every 100 Short-Term Job Losers, 1968-90

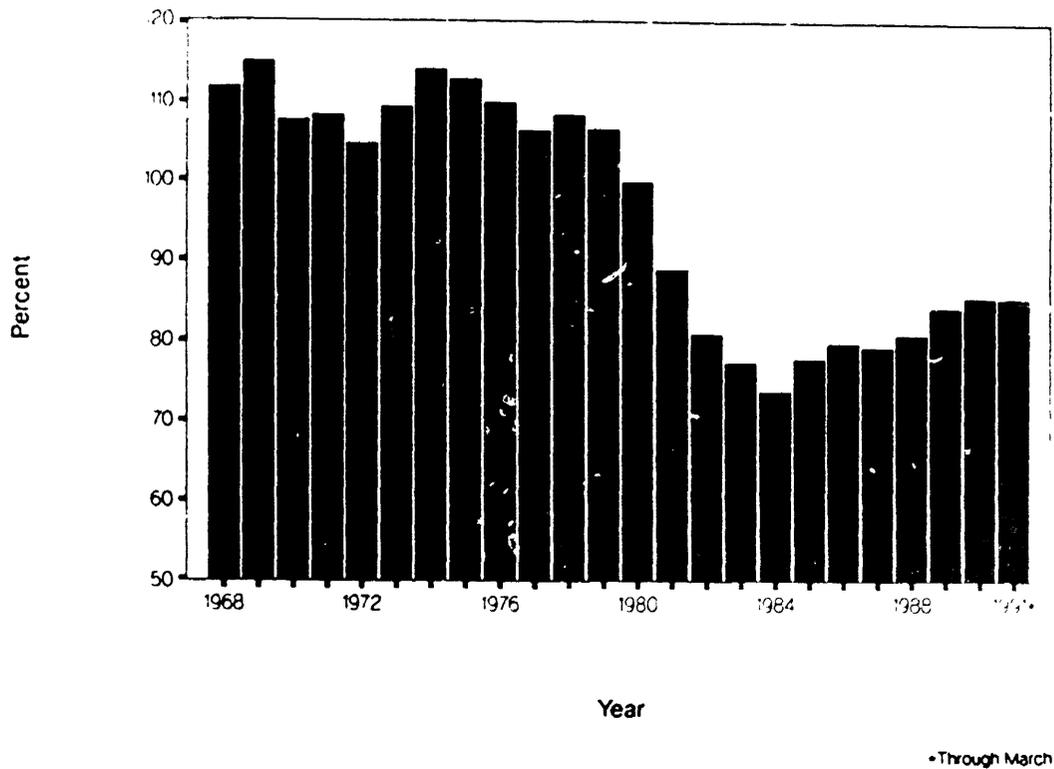
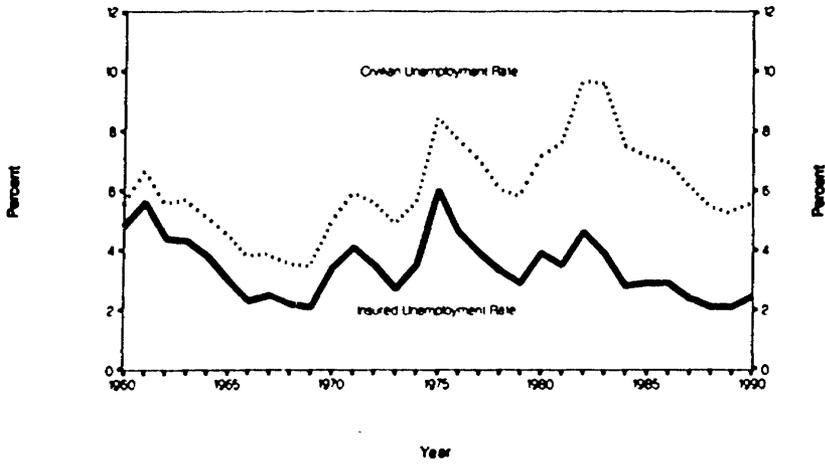
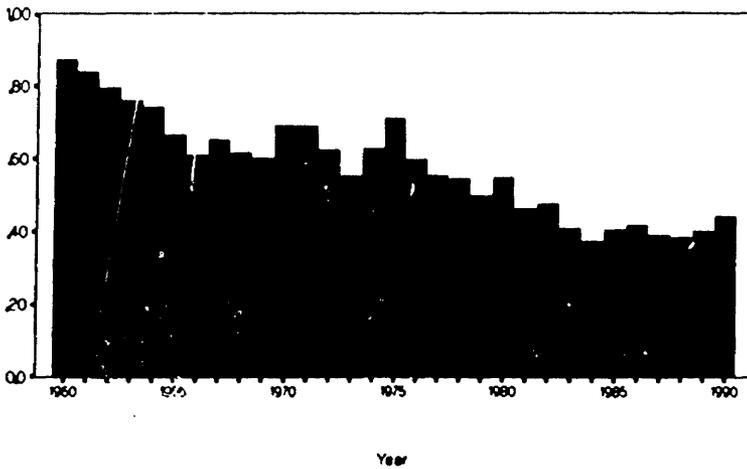


Figure 3. Insured Unemployment Rate Versus Civilian Unemployment Rate



Insured Unemployment Rate as a Fraction of Civilian Unemployment Rate



PREPARED STATEMENT OF WILLIAM J. CUNNINGHAM

Mr. Chairman, I appreciate this opportunity to present the views of the AFL-CIO on problems of the nation's unemployment insurance system.

Unemployment insurance (UI) is the first line of defense for workers and their families when the worker loses his or her job. It is a key part of the nation's "safety net" which helps workers and their families maintain a minimum standard of living when workers lose their jobs and their income. By helping to maintain consumer buying power, UI benefits serve as a counter-cyclical stimulus when the economy is in recession.

Unfortunately, the UI "safety net" is full of holes. Coverage of workers is tragically inadequate. Since 1984, just one-third of the unemployed have been getting UI benefits. The long-term jobless have been largely uncompensated. And UI income replacement rates continue to be far below adequate levels.

Reform of the UI system is urgently needed to deal with current high levels of unemployment and with persistent long-term joblessness even after the end of the recession. I have attached to my testimony a graph (Appendix A) which indicates worse unemployment lies ahead in this current recession and a table (Appendix B) which indicates that unemployment remains high for a long time after the official end of a recession.

According to the AFL-CIO Research Department, using data from the Bureau of Labor Statistics, the graph in Appendix A shows that unemployment rose more than three full percentage points from beginning to end of our last major recessions. We can expect unemployment to go over 8 percent with more than 10 million people who will need income support while looking for work. And we can expect more than 3 million unemployed workers to exhaust their UI benefits in 1991.

The table in Appendix B warns us that unemployment does not drop rapidly after recessions end and after the economy turns up. In fact, it took *at least three years* after the economic upturn into post-recession recovery for unemployment to fall below 6 percent in our last major recessions.

Even if the recession were to end today, the need for unemployment insurance reform will be with us for a long time to come.

The AFL-CIO Executive Council recently called on Congress to ease the suffering of unemployed Americans and declared that, "The unemployment compensation system needs immediate reform to provide extended benefits, expanded eligibility, and adequate funds for efficient administration of the program." Let me turn first to the eligibility issue.

ELIGIBILITY

In 1989, about 6.5 million persons were unemployed every month, but the number getting UI benefits averaged only 2.2 million. So only 33 percent of all unemployed workers were getting UI benefits in 1989.

In 1990, an average of 6.9 million persons were unemployed every month, but only 2.6 million were getting UI benefits—only 37 percent of all jobless in 1990. About 4.3 million unemployed Americans, 63 percent of all jobless workers, went without UI income support in a typical month in 1990.

I have attached to my testimony in Appendix C a state-by-state list with the percentage of unemployed who got UI benefits in the 12 months ending September 1990. This percentage ranges from a high of 58 percent in Rhode Island to a low of 11 percent in South Dakota, with a national average of 33 percent for fiscal 1990.

Disqualification and denial of eligibility of UI claimants by state UI administrators are key reasons for the low rate of unemployed workers receiving UI benefits. State UI administrators too often are responsive to employers' demands to keep benefits low and eligibility restrictions high so that state UI taxes can be kept low. This "business climate" approach to UI encourages states to compete with one another, not in a positive sense but in a fashion harmful to the interests of jobless workers.

The National Commission on Unemployment Insurance pointed out in 1980 that these issues go to the heart of the nature of unemployment compensation as a system of social insurance distinct from welfare.

The Commission declared that in the area of cancellation of benefit rights, the trend by states to impose strict disqualifications "has been so strong that Congress should intervene to correct what is widely regarded as a loophole in the Federal law." (page 48)

Both of these statements by the Commission indicate a long-standing need for Federal standards to restrict disqualifications of UI claimants by the states.

And the Commission recommended to Congress "that the FUTA be amended to provide that State laws may not require any reduction of benefit rights except for fraud or receipt of disqualifying income." (page 48)

The purpose of the UI system is to help unemployed people in time of need, not to punish them for the circumstances under which they lost or left a job.

For this reason, the AFL-CIO strongly supports Federal standards which would generally limit state disqualification of UI claimants. We believe that jobless workers who have earned enough quarters of coverage should be eligible for UI payments after 10 weeks at a maximum, and that there should be no disqualification except for fraud or felony offenses.

Federal standards to set minimum UI eligibility requirements are necessary to assure "safety net" assistance for the 60 percent of the unemployed who are not now getting UI benefits. This is a legitimate and proper role for the Federal Government, and it is much needed to assure a greater degree of fairness and equity in the state UI programs.

The experience of the last ten years indicates clearly that in the absence of strong protective Federal standards, most state unemployment insurance programs do not adequately protect workers, and, in fact, deny UI benefits to most jobless workers.

We believe unemployment compensation is an earned right, based on work experience. Workers have a stake in this system by virtue of the contributions made on their behalf. Should they become unemployed, and if fraud and disqualifying income are not factors, they should have automatic rights to jobless assistance.

This view justifies a Federal prohibition against states cancelling a UI claimant's wage credits or cancelling a claimant's rights to weeks of benefits for any cause other than fraud in a UI claim, or receipt of disqualifying income.

We have serious reservations about exceptions for discharges for misconduct connected to work because employers so often claim such misconduct in order to evade responsibility for a layoff and thus avoid raising their experience-rated state UI taxes. We also oppose exceptions for labor disputes as a failure by the state to pay earned benefits. Failure to pay benefits in such situations places the state on the side of the employer in the dispute.

Eligibility for UI benefits should be made more inclusive than it now is in almost all states. Therefore, we strongly support Federal standards which limit state disqualification of UI claimants. Hundreds of thousands of jobless workers and their families will benefit from the widening of eligibility and coverage made possible by enactment of these provisions.

UI BENEFIT LEVELS

Even those jobless workers lucky enough to get UI benefits do not do very well. They end up getting an average of only one-third of the previous earnings—far less than the 50 percent average recommended by the National Commission on Unemployment Insurance.

The average weekly UI benefit was just \$161 a week in fiscal 1990. But the state-by-state range, as you can see on Appendix C attached to my statement, goes from a high of \$212 in Massachusetts to a low of \$101 in Louisiana. As a percentage of average weekly wages, the state-by-state average weekly UI benefit ranged from a high of 46 percent in Hawaii and Rhode Island to a low of 27 percent in Louisiana.

The low level of UI benefits reflects the power of employers in state legislatures. Too many state legislators and too many state UI administrators adopt the employers' view that it is more important to keep UI taxes low and UI benefits low rather than to help jobless workers and their families with adequate UI payments. This approach defeats the purpose of the UI system.

BENEFITS FOR THE LONG-TERM JOBLESS

The UI system does not now cope effectively with long-term unemployment. Almost one-third of those who do get UI benefits exhaust their benefits before they find a job.

In 1990, there were 2,300,000 jobless workers who used up all their UI benefits. In 1991, this total will certainly exceed 3 million. A state-by-state listing of the percentage of UI claimants who exhausted their UI benefits in fiscal 1990 appears in Appendix C of my testimony.

Unrealistic and unworkable state unemployment triggers for extended benefits have the effect of denying benefits to most long-term unemployed workers.

The existing Insured Unemployment Rate (IUR) trigger for activating extended UI benefits is unrealistic and unworkable. The IUR is far below the Total Unemployment Rate (TUR) and, therefore, a poor indicator of the true level of unemploy-

ment. Furthermore, the IUR is excessively and wrongly stable when the TUR goes up. The TUR is the obvious and logical trigger to use in determining when a state can activate its extended benefits program.

At the beginning of this year, with total unemployment at 6.1 percent, not a single state had an extended benefits program triggered on. Even now, with unemployment at 6.8 percent, only seven states have an EB program in effect. As a result, the present EB program is only minimally effective in helping long-term jobless workers. Gary Burtless of the Brookings Institution says, "For practical purposes, the extended benefit program has now virtually ceased to function." (*Brookings Review*, Spring, 1991, page 40)

To amend the present EB program would not have immediate benefit because the benefits would not take effect in a state until the state amended its state extended benefits law, a process which could take over a year.

There is an urgent need, therefore, to reform or replace the present federal-state extended benefits program to help workers and their families through the personal and family crisis of long-term unemployment.

ADMINISTRATIVE FINANCING

In recent years, as unemployment has been going up, there have been chronic problems of under-funding of Federal grants to the states for administering the unemployment insurance system. This creates serious problems and inefficiencies in administration of UI—and it leads to heart-rending delays and hardships for jobless workers seeking the UI benefits to which they are entitled.

The tragic effect of this under-funding for administration at the state level is a reduction of services to jobless workers at a time when they are most in need.

Administrative funding shortfalls and instability in local offices serving unemployed workers have grown in recent years. Offices are closed, hours of service are shortened, and experienced UI staff are laid off. This makes it increasingly difficult for jobless workers to collect the UI benefits to which they are entitled and to receive the counseling and assistance to help them become reemployed.

For example, in Michigan, workers claiming UI benefits are waiting up to five weeks for their first check. In Maine, workers are waiting three to four weeks for a check. As the recession gets worse and unemployment rises, we will see longer lines at overcrowded UI offices, more offices closing, and more service breakdowns like the January failure of New York State's computer system because of an unmanageable overload of UI claims.

Therefore, we urge that funds for a UI administration should be an entitlement grant appropriated automatically. This would provide funds necessary for local unemployment compensation offices and for local employment service offices to assure adequate services for the growing number of unemployed.

STATE SOLVENCY

Unfortunately, state trust fund accounts from which UI benefits are paid are in terrible shape to deal with recession and high unemployment. The General Accounting Office has detailed the failure of many states to accumulate sufficient reserves during the years of economic growth to pay UI benefits during recession years. The GAO noted that a severe recession in 1991 will force 22 states to borrow more than \$17 billion to keep up their UI benefit payments.

The May 1990 GAO report warned that the probable result of state UI trust fund insolvency in 1991 would be (1) intensified action by the states to make it more difficult for workers to qualify for UI benefits; (2) continued state action to restrict the size and duration of UI benefits; and (3) perhaps even higher state UI taxes on employers.

All these actions in time of recession would be contrary to the two key purposes of the unemployment system: first, to provide cash benefits and income support to unemployed workers; and second, to help stabilize the economy during recession by helping to maintain consumer buying power.

DOWNEY BILL

In conclusion, Mr. Chairman, let me state again that the existing unemployment compensation system falls far short of its two key goals—income replacement for jobless workers and counter-cyclical economic assistance for local communities and the nation.

The problems with eligibility standards, benefit levels, disqualification periods, a flawed extended benefits program, inadequate funding of the state unemployment

compensation and employment services, and the financial solvency of the state trust funds all require urgent action by Congress.

On the House side, the AFL-CIO is supporting H.R. 1367, the UI reform bill sponsored by Congressman Downey, Chairman of the House Ways and Means Subcommittee on Human Resources, which is working on this bill. We hope the House Ways and Means Committee will approve legislation along the same general lines.

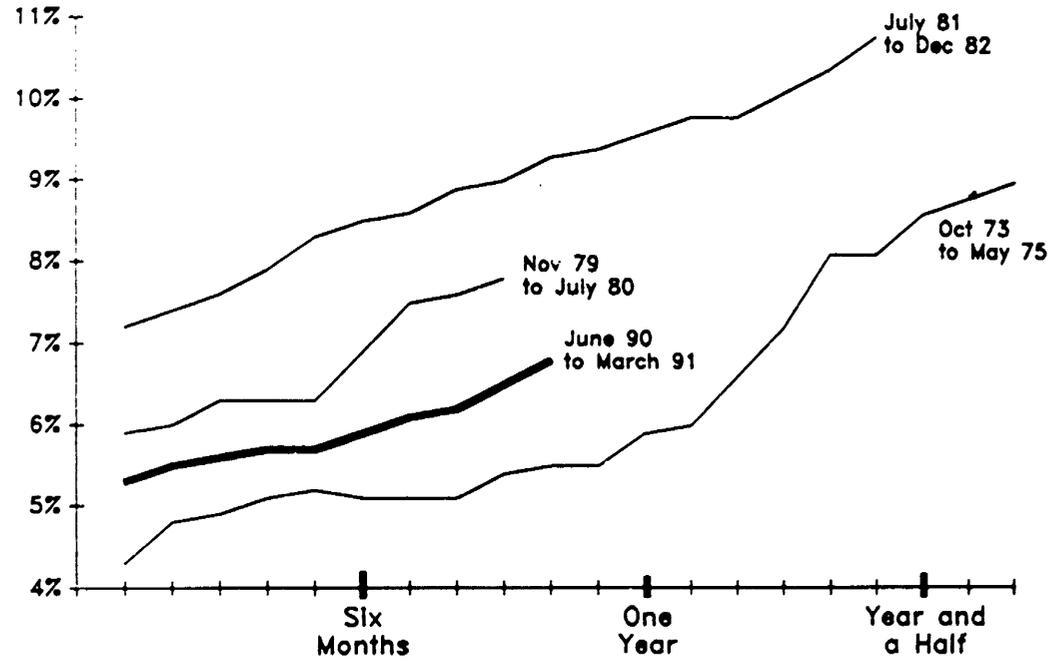
The Downey bill is a significant step forward toward effective Federal standards to widen eligibility for benefits, a new and improved Federal supplemental compensation program to help workers who exhaust their regular UI benefits, and an appropriated entitlement grant for state administration of UI. We regret, however, that the Downey bill does nothing to improve the miserably low level of state UI benefits.

Mr. Chairman, we appreciate your leadership and the interest of this Committee in maintaining and improving the nation's unemployment insurance system. The AFL-CIO is eager to work with you and the members of this Committee to advance sound legislation in this area.

Thank you.

Attachments.

Past Recessions Indicate Worse Unemployment to Come



In past recessions unemployment rose more than 3 percentage points.

Source: Bureau of Labor Statistics

It Takes Years For Unemployment To Go Down

After Oct 73–May 75 Recession

It took 3 years for unemployment to fall below 6 percent. Unemployment never reached its pre-recession unemployment rate of 4.3 percent.

After Nov 79–July 80 Recession

Unemployment declined for only 9 months to 7.2 percent before turning up again in the 1981 recession.

After July 81–Nov 82 Recession

It took 4 1/2 years for unemployment to fall below 6 percent.

Even after the official end of a recession, unemployment remains high for a long time.

Source: Bureau of Labor Statistics

Unemployment Insurance Under State Laws, Jan. 1, 1991

	Jurisdiction (States grouped by Region; District of Columbia within Region)	Maximum Weekly Benefit ^a	Average Weekly Benefit Paid for Total Unemployment FY 90	Average Weekly Wages in Covered Employment ^b	Average Weekly Benefit as a Percentage of Aver- age Weekly Wages ^c FY 90	Percent of Unemployed Receiving Benefits ^d	Regular Duration of Benefits by Week ^e	Percent- age of Unemployed Receiving Benefits FY 90	Average Employer Tax Rate 1990 (Estimated)	Percent- age of Total Payroll 1990	Percent- age of Total Payroll 1990	Leading Wage Base
	United States	\$ —	\$181	\$433	37%	33%	—	28%	2.0%	0.7%	\$ 7,000	
Region I	Michigan	278	206	477	44	27	18-26	29	3.0	1.3	8,500	
	Wisconsin	225	167	390	43	41	13-26	22	2.5	1.1	10,500	
	Illinois	206-278	166	468	36	27	26	34	2.8	0.9	8,000	
	Indiana	96-181	111	400	28	16	8-26	21	1.4	0.5	7,000	
Region II	Kansas	222	160	374	43	31	18-26	26	2.4	1.0	8,000	
	Arkansas	229	132	334	40	30	18-26	24	2.2	1.0	8,000	
	Oklahoma	187 ^f	150	372	40	21	20-26	30	1.8	0.7	8,700	
	Missouri	170	134	481	34	32	15-26	28	1.4	0.5	7,000	
Region III	District of Columbia	293	216	568	37	44	26	52	1.7	0.8	8,000	
	Pennsylvania	291-299 ^g	183	430	43	47	18-26	24	3.5	1.2	8,000	
	West Virginia	251	145	379	38	21	20	21	2.2	0.9	8,000	
	Delaware	225	173	451	38	24	24-26	11	2.3	1.0	8,500	
	Maryland	215	160	444	36	30	26	24	1.1	0.3	7,000	
	Virginia	180	146	414	35	29	12-26	14	0.8	0.3	8,000	
Region IV	Texas	224	162	418	39	18	8-26	48	2.3	0.9	8,000	
	Louisiana	181	181	380	27	22	8-26	27	2.3	1.0	8,500	
	Mississippi	145	111	328	34	24	13-26	24	1.2	0.5	7,000	
Region V	North Carolina	245	154	373	41	39	13-26	13	0.8	0.4	11,500	
	Florida	226	144	387	37	21	18-26	30	0.7	0.3	7,000	
	Georgia	185 ^h	142	412	35	24	8-26	26	1.4	0.5	8,500	
	South Carolina	175	131	359	36	30	18-26	18	1.0	0.7	7,000	
	Alabama	150	118	373	31	24	15-26	17	1.4	0.6	8,000	
Region VI	Marshall	275	162	414	40	38	26	17	1.3	0.9	21,400	
	Colorado	210	134	484	29	43	14-26	30	2.0	0.8	7,000	
	Nevada	282	162	413	39	41	12-26	25	1.4	0.8	13,000	
Region VII	New Jersey	291	206	321	39	51	15-26	39	1.7	0.8	14,400	
	New York	260	181	533	34	47	20	35	1.0	0.5	7,000	
	Puerto Rico	120	78	238	33	29	23	54	5.4	2.0	7,000	
Region VIII	Massachusetts	282-425	212	481	43	52	18-30	37	2.7	0.8	7,000	
	Rhode Island	269-334	189	413	46	50	15-26	36	2.5	1.3	14,400	
	Connecticut	278-320	195	534	36	48	20	29	1.9	0.9	7,100	
	Maine	188-282	158	367	43	49	21-26	29	2.2	0.9	7,000	
	Vermont	182	140	377	39	43	26	17	3.0	1.2	8,000	
	New Hampshire	168	128	418	31	30	26	5	0.8	0.3	7,000	
Region IX	Oregon	247	162	381	41	39	8-26	23	2.8	2.0	10,000	
	Washington	248	189	417	40	44	18-30	26	2.3	1.4	10,000	
	Alaska	212-284	158	879	28	48	18-26	46	4.1	2.0	22,400	
	Idaho	206	138	345	40	37	18-26	29	1.7	1.2	10,000	
	Montana	183	129	327	40	29	8-26	32	1.3	0.8	13,400	
Region X	Kentucky	199	134	365	37	29	15-26	18	2.1	0.8	8,500	
	Ohio	196-291	166	423	39	38	20-26	22	2.0	0.8	8,000	
	Tennessee	165	113	378	30	41	12-26	27	1.5	0.6	7,000	
Region XI	Colorado	229	187	421	40	24	13-26	35	1.5	0.7	10,000	
	Utah	221	158	367	43	18	18-26	27	1.5	0.8	14,500	
	Wyoming	208	187	387	43	18	11-26	25	3.1	1.5	10,500	
	New Mexico	177	129	353	37	22	18-26	33	1.7	1.0	11,700	
	Arizona	185	132	488	33	29	12-26	28	1.2	0.4	7,000	
Region XII	Minnesota	260	183	430	43	27	18-26	31	2.0	1.0	13,300	
	North Dakota	190	128	324	40	22	12-26	30	2.3	1.2	11,000	
	Iowa	186-228	157	355	44	25	11-26	22	1.6	0.8	12,200	
	South Dakota	148	118	299	37	11	18-26	11	0.6	0.3	7,000	
	Nebraska	144	118	340	35	32	20-26	26	1.1	0.4	7,000	

^a For the ending September 1990 - actual data available.
^b Where two figures are shown the larger includes maximum dependent allowances.
^c Where two figures are shown the lower represents the duration payable duration to most states that is the equivalent of a standard with minimum weekly benefits and minimum qualifying wages.
^d Maximum weekly benefit is a specified percentage of average weekly covered wages and is computed annually or on a five-year rolling basis.
^e For the ending September 1990 the percentage figures may vary from statutory percentages.
^f For the ending March 1990.
^g For the ending September 1990.
^h For the ending March 1990.

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 President

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 Secretary-Treasurer

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Adopted by the AFL-CIO
Eighteenth Constitutional Convention
November 1969, Washington, D.C.

Unemployment Insurance

The nation's unemployment insurance system is failing its mission to provide a cushion for those in our society who have lost their job. For the past five years just one-third of the jobless have received benefits under this program. Last year nearly 70 percent of the unemployed got nothing. Without substantial reform, the unemployment insurance system will be unresponsive to demands in future recessions and will be unable to provide the countercyclical stimulus to the economy that is a hallmark of the program.

The AFL-CIO has urged Congress to reform the unemployment insurance system. Intentional underfunding of state benefit trust fund accounts has resulted in severe restrictions on eligibility and has encouraged states to keep benefit payments low. Federal minimum standards for benefits and financing are desperately needed to protect the unemployed. The AFL-CIO strongly supports indexing the federal taxable wage base to provide a fixed statutory relationship between earnings and the way funds are accumulated to support benefits when those earnings are disrupted. Indexing the federal taxable wage base at 65 percent of the average annual wage is a moderate, reasonable step to provide the underpinnings for a sensible jobless insurance scheme.

The AFL-CIO believes that the Extended Benefit program, which for all practical purposes is inoperative today, must be reformed by making the system more responsive to the problems of long-term joblessness. We believe that if the extended benefits program must rely on triggers, reform must move away from, or even abolish, reliance upon the insured unemployment rate (TUR) in favor of the total unemployment rate (TUR). Despite some problems and inequities that are certain to occur, we endorse the notion that a TUR for local labor market areas (or sub-state triggers)—even if dependent upon a discretionary act by the governor of the state—ought to be another avenue available to activate extended benefits.

The failure to adequately fund the administration of the UI and Employment Service system has resulted in serious problems for policy makers, for state agencies and their employees, and for the people they are pledged to serve. Reform in financing the administration of the unemployment insurance system must involve an increase in the federal taxable wage base. This would enable Congress to appropriate more adequate amounts for the operation of the program while allowing the necessary and continued build-up of funds in the federal accounts. The Department of Labor should establish basic levels of administrative support that would be consistent regardless of the condition of the economy. The distribution formula can be adjusted to give states better planning capabilities and assistance in computerization efforts.

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PREPARED STATEMENT OF BILL GROSSENBACHER

Mr. Chairman and members of the Committee, my name is Bill Grossenbacher. I am Administrator of the Texas Employment Commission and President-Elect of the Interstate Conference of Employment Security Agencies (ICESA). ICESA's members are the state officials who administer unemployment compensation laws, the public employment service, labor market information programs, and in many states, job training programs. Thank you for the invitation to appear today to discuss the state-Federal unemployment compensation program in the context of the current recession.

Unemployment compensation has long been, and continues to be, the Nation's first line of defense in a recession. Cash benefits, provided as a matter of right to workers who are idled by the economic downturn, serve the dual purposes of alleviating personal hardship and stabilizing the economy. State financed benefits tide workers over for up to 6 months; when unemployment reaches levels high enough to trigger payment of Extended Benefits, another 3 months of payments, financed jointly by the state and Federal Government are available. During past recessions, the Federal government has provided additional weeks of supplemental benefits financed entirely by the Federal Government. During the current recession, questions have been raised about whether the unemployment insurance system is fulfilling its traditional roles adequately.

DECLINE IN PERCENT OF UNEMPLOYED RECEIVING BENEFITS

During this recession, the press has frequently reported that in 1975, a recession year, about three quarters of the unemployed received benefits while now only 35% are compensated. Often, the major reason cited for this decline has been action by states resulting in more restrictive qualifying and eligibility requirements. While some states have tightened requirements, especially those related to voluntary separation from a job and the minimum amount of work/earnings to qualify for benefits, the restrictions on benefits at the Federal level have had a much greater impact.

The portion of the unemployed who receive benefits tends to fluctuate with economic conditions. A higher portion of the unemployed are paid benefits during recessions because those who have recently lost their jobs usually qualify. Unemployment insurance was not structured to provide assistance to new entrants or reentrants to the labor force or to the long term unemployed. Now, as we have entered a recession, the gap in insured and total unemployment is narrowing.

In March, 47.1% of the unemployed were receiving *state* unemployment benefits, compared to 49% who received state unemployment benefits in 1975. In 1975, 26% of the unemployed received Federal unemployment benefits; including extended benefits; Federal supplemental benefits, special unemployment assistance, and benefits for former military service personnel. In March, only 0.4% were receiving state-Federal extended benefits and other Federal benefits such as those available to former Federal workers. Most of the Federal benefits, which were available primarily to those who had already received state benefits in 1975, have been either eliminated or restricted since that time.

The restrictions made to the state-Federal extended benefits program are listed below:

- In 1980, P.L. 96-499 required states to deny extended benefits to individuals who failed to meet certain Federal eligibility requirements. These include presenting "tangible proof" of the individual's search for work each week, and denial of benefits if the individual failed to meet the requirement, not just for that week, but for the duration of the individual's unemployment. Another requirement is application for "suitable" work, suitable being defined as any work for which the individual is capable and which pays at least the minimum wage or as much as the individual's weekly benefit amount.

- In 1981, the national trigger for extended benefits was eliminated, making extended benefits available only when the state insured unemployment rates meet the required levels.

- Also in 1981, the calculation of the state extended benefit trigger rates was revised to exclude extended benefits claims, in effect, increasing the level of unemployment required to trigger an extended benefit period.

- In 1982, the state trigger rates were changed from 4% (plus an increase of at least 20% compared to the same period in the prior two years) and the optional 5% without regard to the comparison with a prior period, to their present levels, which are 5% plus a 20% increase and the optional 6%.

- Also in 1982, states were required to deny extended benefits to unemployed workers who had not worked at least 20 weeks in full time employment, or the equivalent, during the 12 month period on which his/her state unemployment benefit claim was based.

There were cuts in other Federal unemployment benefits as well:

- In 1980, Federal funding of benefits for former public service workers (under the Comprehensive Employment and Training Act) was eliminated.
- In 1982, P.L. 97-362 limited payments to former military service personnel to half the number of weeks available to unemployed civilian workers and imposed a 4 week waiting period for benefits.

In addition to the cut-backs in Federal benefits, the Federal Government has both required and encouraged states to restrict benefits over the last ten years:

- In 1980, P.L. 96-364 required states to deduct pension payments, including social security, from unemployment benefits. In many cases, this disqualifies otherwise eligible unemployed workers from benefits entirely.
- Also in 1980, Federal reimbursement for the first week of extended benefits was eliminated for any state that did not require at least a one week waiting period for regular state benefits, in effect, a financial penalty for states that chose to have no waiting week.
- In 1983, states with insolvent trust funds were offered a chance to stretch out repayment of loans to the Federal Government if they took steps to cut benefits as well as increase revenues. States in poor financial condition had little choice but to make benefit cuts part of their package of "solvency legislation."
- Also in 1983, states were required by Federal law to deny benefits to nonprofessional employees of educational institutions between academic terms.
- In 1986, unemployment benefits were made subject to Federal income taxation without regard to the individual's total income. Some believe that this reduction in the value of benefits has made some unemployed workers less likely to claim benefits.

ICESA urges you: to repeal the Federal qualifying and eligibility requirements associated with the extended benefit program and other Federal requirements related to eligibility for state unemployment benefits; to provide unemployment benefits to former military personnel on the same basis as benefits are provided to civilian workers; and to monitor the number of workers who have exhausted state benefits to determine whether a Federal supplemental benefits program is needed.

As you consider changes to the extended benefits program trigger levels, please keep in mind that states have made decisions about their trust fund reserve levels based on projections of outlays under the current extended benefit trigger levels. Any changes which would increase state financial obligations during this recession could lead to insolvency of some states' trust funds. States need sufficient lead time to factor any increased benefit obligations into their trust fund reserve calculations. Lead time of at least one year, and two years in states where the legislature does not meet every year, is also needed to enact necessary state legislation to implement changes to the program.

ADMINISTRATIVE FUNDING

As we entered this recession, most state employment security agencies were not as well prepared as they needed to be to serve a growing number of jobless workers. Cutbacks in Federal appropriations for administration of unemployment insurance and employment services during the 1980's have left most states with fewer staff and local offices than they need to meet recession-level workloads.

One of the great strengths of the unemployment insurance system over the years has been its ability to expand and contract in direct response to economic conditions. This flexibility has been due in great measure to reliable Federal funding based on workload—the number of unemployed workers filing claims for benefits. In recent years Federal funds have been greatly restricted. Since 1983, state unemployment insurance staff levels have dropped from about 57,000 to about 43,000. Over the last ten years, the number of employment service staff nationwide has dropped from about 32,000 to the present level of about 17,000. Although the drop in unemployment insurance staff has been due, in part, to lower unemployment during the late 1980's, the combined reduction in resources for UI and ES which share many facilities reduced the system below the level necessary to maintain an adequate infrastructure of offices and computer systems. Thus the unemployment insurance

system entered this recession without the capacity it needed to respond to recession level unemployment.

The system was able to expand expeditiously in the past because Federal administrative funds increased concurrently with increases in unemployment. Before Fiscal Year 1990, when claims for unemployment benefits exceeded the level on which the appropriation was based, the Department of Labor requested supplemental funds to pay for services to the additional unemployed workers. However, our experience in FY 1990 and the changes to the budget process enacted last year suggest that we can no longer rely on additional Federal resources when unemployment increases, creating uncertainty in state planning and service delivery.

For the past two years, there have been shortages in funds for administration of unemployment insurance due to underestimation of the unemployment rate and consequently, the number of people filing claims. Last year, the Department of Labor notified states that although unemployment projections were higher, the Administration would make no supplemental funding request. Instead, the Department of Labor reduced the amount of basic grant funds previously allocated to states by an average of 6.7% and implemented plans to reimburse states at a reduced rate each quarter for additional workload. As a result, many local unemployment offices were closed. For example, 17 full-time offices and 45 part-time offices were closed in Indiana. There were long lines in many offices; unemployed workers waited four to five hours to file claims in Michigan, for example. Due to these obvious hardships, Congress took the initiative and provided \$100 million in supplemental funds in May, 1990. These additional resources shored up the system for the remainder of FY 1990; however, the delay of almost six months meant that from January to May many unemployed workers were subjected to overcrowded offices and delays in claim filing and payments. Our own employees in these offices were pushed further than good management dictates. They put in long hours and were blamed for the overcrowded conditions by understandably frustrated unemployed workers.

Again this year, we were faced with a shortfall, estimated at \$201 million. The Department of Labor notified states that reimbursements to states for additional workload each quarter would be reduced by 25%. The Administration requested only \$100 million in supplemental funds, just half the amount needed to fully fund state costs. Earlier this month, the President signed the supplemental funding bill providing \$150 million for unemployment insurance administration, \$50 million more than the Administration had requested and enough to fund 97% of state costs for the remainder of the year. However, the shortfall from the first quarter will not be made up. Although the supplemental this year came earlier than last year, states were operating on the basis of reduced funding during the winter peak claims months. The resulting long lines of unemployed workers became a familiar sight on televisions and in newspapers throughout the country.

Fundamental changes are needed in administrative funding arrangements for unemployment insurance in order to avoid even worse problems in the future. Changes made by the Budget Enforcement Act will create serious funding problems for the unemployment insurance system when unemployment declines. The baseline estimate for unemployment insurance and other social insurance programs is to be adjusted for changes in the number of beneficiaries. While this was intended, presumably, to adjust funding for workload changes, it does not take into account that about 40% of the basic administrative costs of unemployment insurance are associated with collection of state unemployment taxes, costs that are not related to the number of beneficiaries. (These costs are related to the number of employers subject to the state law and the number of their employees). The baseline methodology will reduce the entire amount of funding for unemployment insurance, including the significant portion associated with tax collections, by the percent decline in the number of beneficiaries. Therefore, when unemployment goes down, the potential reduction in resources would be so great as to virtually destroy the system. This is illustrated by the recently adopted House Budget Resolution for FY 1992 which assumes a level of funding for unemployment insurance which is \$412 million below the President's request.

ICESA has several recommendations for improving administrative funding for unemployment insurance:

First, ICESA has long advocated excluding the Federal Unemployment Trust Fund from Federal budget totals. This would permit appropriations to be made on the basis of programmatic considerations rather than Federal budget deficit reduction goals. The scarcity of funds for unemployment insurance is particularly difficult for employers, workers, and state officials to understand because a Federal payroll tax, the Federal Unemployment Tax, produces revenue which is dedicated to providing administrative funds for unemployment insurance, em-

ployment services and certain veterans employment programs. These funds are held in the Employment Security Administration Account in the Federal Unemployment Trust Fund, from which appropriations for these programs are made. The Employment Security Administration Account was projected to have a balance at the end of FY 1990 of \$2.24 billion, \$1.08 billion above its statutory ceiling. More than sufficient Federal unemployment tax revenues are collected for unemployment insurance and employment services; however, they are held hostage like many other trust funds to the Federal budget deficit.

Second, serious consideration should be given to switching the administrative costs of unemployment insurance from the discretionary to the mandatory category. Administrative costs of many other entitlement programs are structured in such a way that those costs are also an entitlement. If unemployment insurance remains in the discretionary category, increases in the cost of unemployment insurance administration will either be ignored to the detriment of unemployed workers or funded at the expense of other domestic discretionary programs. By switching unemployment insurance administration to the mandatory category, these changes in cost could be accommodated.

Third, language should be included in appropriations for unemployment insurance operations which would provide necessary funds to process claims for unemployment which are not anticipated at the time the appropriation is made. This would ensure that funds would be available if unemployment should rise even higher, without the necessity for supplemental appropriations. Similar "contingency" appropriations language already exists for administrative costs of other benefit entitlement programs.

STATE TRUST FUND SOLVENCY

During the past seven years states have repaid about \$14 billion in Federal loans and built up total state trust fund reserves of about \$40 billion. Studies by the General Accounting Office project that in a severe recession beginning in 1991, 22 states would borrow \$17.4 billion over a five year period from the Federal Unemployment Account (loan fund) in the Federal Unemployment Trust Fund.

ICESA has no independent projections of state borrowing; however, we believe that the Federal policy decisions in the 1980's related to unemployment trust fund loans will tend to limit borrowing and encourage quicker repayment. The interest charging provisions which went into effect in 1982 have eliminated any incentives for states to build large debts.

While adequate reserves are always a goal, there are tradeoffs between higher reserves, which require higher taxes, and lower reserves which may require occasional borrowing. Each state has determined the risk it is willing to take. There have been suggestions for Federal incentives for higher trust fund reserves. For example, the Federal Government could pay a higher rate of interest on state trust fund reserves that exceed a certain level of solvency, or discount the rate of interest charged on loans if the state met a certain level of solvency in the year prior to borrowing. We think that these are interesting ideas which should be explored further.

However, we urge you to reject any proposals for Federal solvency standards for state trust funds. We believe that such standards are neither feasible nor desirable. They could result in benefit cuts or inappropriately timed tax increases. Decisions about state trust fund solvency should be made in the legislative process of each state where the many variables which must be considered can be taken into account.

Mr. Chairman, ICESA appreciates your continuing interest in unemployment insurance. If you have any questions, I would be pleased to address them.

PREPARED STATEMENT OF REPRESENTATIVE SANDER M. LEVIN

I appreciate very much the opportunity to testify at this hearing on our Unemployment Insurance (UI) program.

Mr. Chairman, we all share the same goal: a UI program that delivers on its promise to provide unemployment benefits to those who find themselves stranded by economic forces beyond their control.

Put more bluntly, we need a UI program that allows American workers to land on their feet, not their face. We also need a program that provides the services for which employers have paid taxes.

We do not have such a program today. As many of your witnesses will testify later this morning, our UI program is frightfully unable to cope with the increased demands placed upon it by the current recession. Many of these witnesses have de-

livered the same message to the Ways and Means Committee, on which I sit, and we've crafted a UI reform bill that I believe will go a long way toward repairing the program.

Many important aspects of the program need to be examined—why UI covers only 37 percent of the unemployed?, why only six states have triggered on to the EB program?, whether eligibility standards and benefit payments should vary so widely among States.

Because of time constraints, I want to focus today on two elements of the UI program—administrative financing and job search/job training—to which I've devoted considerable energy and attention. In both cases, the Federal Government has a unique and important responsibility, and experts and interest group agree there is an urgent need for reform.

ADMINISTRATIVE FINANCING

The Federal government's primary obligation is to provide the funding necessary to administer the UI program. The Social Security Act of 1935, which established the UI program, requires the Federal Government to provide all the funding needed to operate "efficiently and effectively" our unemployment compensation system.

Yet for the past several years, the spirit of this law has been repeatedly and recklessly violated. Though the UI Trust Fund contains over \$1 billion in the administrative expenses account, and though UI is an entitlement program, the need to reduce the deficit has dictated overly rosy economic forecasts and skimpy UI administrative budgets. Budget politics have overridden the welfare of the American worker and our responsibilities to American business, and put the integrity of the unemployment compensation system at risk.

Recently, I visited an unemployment office in Madison Heights, Michigan, just outside Detroit in my district. What I saw shocked me. Lines stretched to the doors as overburdened staff workers sorted through the piles of unfiled claims. Two Employment Service staffers were trying to place over 500 UI claimants in jobs, and many times they were called off their jobs to help out processing initial UI claims. They simply couldn't perform their important task of placing UI beneficiaries in new jobs.

Several of the workers I talked to had been waiting over five weeks to hear word on their claims, and they'd been forced to idle on the line just to get an update on their status. I knew their predicament, since my staff had just spent four hours trying to reach the same unemployment office by phone. I later learned there is no separate phone line for the Employment Service—one phone line must handle all the traffic. All my staff got, and all those workers got, was a busy signal.

Over the past several months, a similar scene was repeated in unemployment offices across the United States. Unemployed workers in many cases waited four to five weeks for their claims to be processed. Benefit checks went out late. Mortgage payments and other bills went unpaid. Job searches were delayed.

Just as importantly, the Federal Government has a strong interest in providing the necessary administrative funding beyond simply eliminating the delays in claims processing, for two reasons. First, administrative funds are used to help collect the FUTA tax from employers. The Labor Department estimates that the cumulative past taxes total over \$1.7 billion as of 1989. Second, administrative funds are also used to track down and correct overpayments made to claimants. As of 1989, it was estimated that over \$1.1 billion in overpayments had not been caught and rectified.

The result: our policy of skimping on administrative funding has cost the UI Trust Fund up to \$2.8 billion, and sowed the ground for future program fraud and abuse.

Viewed against this backdrop, the recent snafu over providing supplemental monies seems shortsighted and needlessly aggravating.

As early as last December, a number of us realized that the weakening economy and rising unemployment rate would create a large shortfall in administrative funds for the UI program. Sixty of my colleagues joined me in sending a letter to President Bush urging him to provide for fiscal year 1991 the needed supplemental funding, and to declare it an emergency so as not to jeopardize other important programs through a sequester.

The Bush Administration's response was faltering at best, insensitive at worst. Though its own budget estimated the shortfall at \$200 million, only \$100 million in supplemental funding was requested and no emergency declaration was attached. After much wrangling back and forth, OMB Director Darman admitted in a letter to Senator Byrd that he hadn't understood the true extent of the shortfall, agreed to

provide \$150 million in supplemental appropriations for UI, and declared that funding an emergency. At last, the system is beginning to respond.

I'm sure that Mr. Darman had strategic political reasons for initially denying greater funding and then later reversing himself. I'm equally sure that other officials, including my good friend Lynn Mertin, had no choice but to tow the Administration line.

What concerns me is the devastating toll this debilitating and unnecessary debate took on those unemployed Americans who look to UI to sustain them in times of need. While we argued inside the Beltway, too many Americans outside encountered a UI program in disarray, unable to deliver the promised benefits.

I come before you to plead, on their behalf, for a permanent solution to the ongoing administrative funding crisis. The supplemental appropriation process is too cumbersome and inflexible to do the job properly.

There are a number of possible approaches, and I understand that several of you are working on an anti-recession package that may address this issue of UI administrative funding. I hope that during your deliberations, you'll consider a proposal I developed with Rep. Don Pease and that is now included in Chairman Tom Downey's overall UI reform bill.

Our proposal is quite simple. It would change UI administrative funding from a discretionary to a mandatory spending program. Such an approach would put UI on the same footing as other state-administered entitlement programs like Food Stamps and AFDC, would provide for quick and efficient responses to unanticipated increases in the UI workload, and would guard against sequesters in other programs to make up those unanticipated increases.

Some have suggested that establishing a Contingency Reserve Fund on the annual Labor-HHS appropriations bill would take care of the problem. It is true that a Contingency Reserve Fund would provide funding for unanticipated increases in UI caseload, and in fact, I pushed for its inclusion on the recent domestic supplemental bill.

But we should be clear that this is only an interim measure. Two large problems would remain. First, the Contingency Reserve Fund does nothing to restore the erosion in base funding for UI administration over the past several years and to ensure that this base funding keeps up with the increased costs of service delivery in the future. The UI administrative base has been nicked several times by sequesters, has not been adjusted for the increases in size of the labor force and increases in salaries States must pay their workers, and faces a sharp decline in future funding under OMB baseline projections if nothing is done.

Second, any increased funding from the Contingency Reserve Fund for unanticipated increases in UI caseload would count against the domestic discretionary cap on spending, and therefore might risk sequestering other important programs. During last fall's budget negotiations, it was agreed that any unanticipated increases in caseload for other state-administered entitlements programs, such as AFDC, should not jeopardize other programs and therefore would not count against the spending caps. The same should be true for the UI program.

One more point. Like you, I'm concerned that we not automatically provide new monies to UI administration, without regard for how that money is spent or what efficiency savings might be squeezed out of the program.

That's why it's important to understand that States cannot simply ask reimbursement for any costs they incur. Instead, they're paid a fixed amount for each additional claim filed, and that amount has built into it efficiency standards and assumptions. Furthermore, this compensation rate for additional claims, which is negotiated with individual States, has not been adjusted since 1984, meaning no correction has been made for the increasing costs of service delivery. Finally, the States have in reality been paid only 84 percent of their claim compensation rate, leaving them far short of what they need to handle new claims.

JOB SEARCH JOB TRAINING

Fixing the administrative financing mechanism, while an important first step, is not enough. What we desperately need in this country is an unemployment compensation system, similar to those in other industrialized countries, that prepares unemployed workers to reach their production potential.

What is required is a transformation of UI from an income replacement program to a comprehensive unemployment recovery system that provides income benefits as it also provides the skills and knowledge to successfully meet the challenges of an increasingly competitive, rapidly changing workplace.

Unemployed German workers rejoin the workforce to build cars or engineer computers, not flip hamburgers. We sell American workers short when we shy away

from adopting the comprehensive, cooperative models of job training and unemployment assistance that have worked so well in Europe and Japan. Examples abound of successful partnerships, such as the UAW-GM joint training center in my backyard, and we should look at these models in constructing our own system.

Given our present fiscal environment, however, any transformation must be undertaken gradually and carefully. But there are proven steps that would put us further down the road.

For example, the UI reform bill we've put together would significantly enhance job search and job training activities. If a UI claimant had been employed for the past three years and had received ten weeks of UI benefits, he or she would be required to participate in an intensive job search program. Job training could be elected as long as the particular state could not prove there was no net social benefit to such training.

We didn't put this provision in on a whim or a hunch. We adopted this reform because a demonstration project conducted by the U.S. Department of Labor in New Jersey showed conclusively that enhanced job search and training was cost-effective and allowed unemployed workers to find jobs paying wages more comparable to those in their previous jobs. Unemployed workers would be afforded the chance to find meaningful work in a tough job market, and consequently, would leave the UI rolls earlier—an outcome favorable to employees and employers.

Makes sense, doesn't it? Yet the Bush Administration, which partially funded the New Jersey demonstration project, opposes this provision of our bill. Why is it that we fund a study to determine what cost-effective reforms in UI we might undertake, and then when we find one, we decide against adopting it. Perhaps we should just let GAO run the government, and all go home.

President Bush has just unveiled his education reform package to prepare our students for their economic future. We need to do the same for our unemployed workers who face a similar challenge, and I hope you'll seriously consider supporting some of the reforms I've mentioned here today.

CONCLUSION

Mr. Chairman, employers and employees alike deserve more than a busy signal from their government.

There are many nettlesome issues to consider, including financing, in tackling reform of our UI system.

But I hope these problems will not distract your attention from our common purpose, to offer a helping hand to those who want to work but cannot because the system has failed them.

PREPARED STATEMENT OF LYNN MARTIN

Mr. Chairman and Members of the Committee: I am pleased to appear before you today and appreciate the opportunity to discuss with you the unemployment insurance program. Having represented the city with one of the highest unemployment rates in the nation during the 1982 recession, I can assure you that I am exceedingly sensitive to the profound way unemployment affects people's lives. As you know, the Labor Department oversees the basic unemployment insurance program, extended unemployment benefits when they are triggered, and training programs for dislocated workers and the long-term unemployed under the Economic Dislocation and Worker Adjustment Assistance Act. The Department is, and will remain, committed to seeing that these programs are operated as effectively and humanely as possible.

The Administration believes that the unemployment insurance program is continuing to effectively perform its prescribed and targeted mission of providing temporary, partial wage replacement to experienced workers who become unemployed through no fault of their own, and encouraging an early return to work. The program is paying out over half a billion dollars per week to almost four million persons. In March 1991, 73 percent of job losers—the target population for the UI program—received benefits. Before commenting on the specific issues which you have asked me to address, I would like to review the current outlook. Budget outlays for benefit payments in all unemployment insurance (UI) programs are expected to be \$25 billion in FY 1991, up from \$17 billion in FY 1990. The number of those receiving benefits is projected to rise from 8.3 million in FY 1990 to 11 million in FY 1991. We expect to continue the current level of activity into FY 1992 as we project spending \$25 billion for benefit outlays again to about 10.4 million individuals.

TRUST FUND SOLVENCY

With respect to financing these added outlays, the UI program is more solvent now than at any time since 1973. State accounts in the unemployment trust fund totaled \$40 billion at the end of 1990. This represents nearly two percent of total wages and salaries, and is the highest percentage in 18 years.

The vast majority of State accounts have sufficient funds to pay for the increase in the number of claims, although we estimate that four to six States may have to borrow funds during this year and next to cover benefit costs. The Federal Unemployment Account has more than adequate reserves at \$3.35 billion to cover these projected loans. Also, the Employment Security Administration Account has sufficient funds to cover all expected workload-related administrative costs. Finally, with a balance of about \$7 billion, the Extended Unemployment Compensation Account has ample resources to cover expected outlays under the current extended benefit program. In general, although current high benefit outlays will reduce balances over the next several years, the trust fund will remain solvent.

I will now focus on the other issues concerning the UI program: the extended benefit program, the gap between the total number of unemployed workers and those collecting benefits, and administrative financing.

EXTENDED BENEFIT PROGRAM

The extended benefit (EB) program is designed to provide benefits to eligible individuals when unemployment in a State is relatively high. The program pays up to an additional 13 weeks of unemployment benefits when States reach a "trigger" rate of insured unemployment. The EB program was implemented on a permanent basis in 1970 and since then has undergone a number of modifications. The latest changes occurred in 1981 and were aimed at achieving effective targeting of benefits. Indeed, the extended benefit program is responding to the recent increases in insured unemployment in precisely the manner in which it was designed. Extended benefits are now payable in nine States (Alaska, Maine, Massachusetts, Michigan, Oregon, Puerto Rico, Rhode Island, Vermont and West Virginia). This number is smaller than in past recessions, reflecting the lower number of claimants expected during this recession which will serve to reduce the need for extended benefits. Further, the benefit exhaustion rate is expected to reach about 32 percent at the bottom of this recession. This is sharply below the 41 percent exhaustion level reached at the bottom of the last recessionary period. The Administration believes the EB program is operating effectively and that no revisions are necessary.

THE "GAP"

During the past few years, concern has been expressed about the difference between the total number of unemployed individuals and the number of unemployed who collect benefits, referred to as the insured unemployment "gap." It is important to remember that this gap is normal. It is due to the design and purpose of the UI program. UI benefits are generally paid to workers with substantial labor force attachment who have lost their jobs through no fault of their own—not to workers who quit their jobs voluntarily, who were fired for cause, or who have had no recent employment, such as those entering or reentering the labor force. As I indicated earlier, 73 percent of job losers in March 1991 received UI benefits.

Currently, the proportion of all unemployed individuals receiving regular benefits—47 percent in March—is significantly higher than the proportion that received benefits during the last half of the 1980s, and remains above the proportion who drew benefits during the 1982-83 recessionary period. It also is consistent with the proportion receiving UI benefits in the 1970s.

Generally, the number and proportion of the unemployed who receive benefits increase during periods of high unemployment. This happens because: job losers make up a larger proportion of the unemployed compared to those newly seeking work and those who quit their last job; the average length of time individuals receive benefits increases; and some recipients can receive benefits for longer durations in States which trigger on to the EB program.

The Department has been studying the causes of the larger gap that occurred in the 1980s. A number of studies have determined that there is no single explanation for the 1980s increase in the gap. Some of the factors responsible included:

- Changes in the economic structure of the nation, with employment declines in sectors of the economy, such as mining and manufacturing, which historically have had higher UI benefit receipt levels;
- Some individuals who may be eligible for UI benefits do not apply; and

—Changes in the demographic makeup of the labor force, with many of the unemployed having weak job attachment and an insubstantial work history.

Concerning the demographic make-up of the labor force, a recent study by the Congressional Research Service showed that those unemployed workers who do not receive unemployment benefits are a diverse group, but typically they are young, do not head families, and were not their family's primary source of income when they were employed. The largest group of the unemployed who do not receive unemployment benefits, about two-fifths of the total, are teenagers and young adults still living with their parents.

ADMINISTRATIVE FINANCING

As to administrative financing of the UI program, the Department is committed to providing stable and adequate funding for UI administrative costs including:

- timely and adequate funding to the States for unanticipated workload increases; and
- equitable and fair allocation of resources among the States in a way that promotes innovation and cost-effective practices.

We are well aware that the current recession has put an added strain on the delivery of services to unemployment insurance claimants and that some claimants have experienced difficulties in having their claims processed. The Dire Emergency Supplemental Appropriations bill recently signed into law by the President (Public Law 102-27) included a provision, supported by the Administration, providing a \$150 million supplemental appropriation for UI administrative costs for the current fiscal year. This addition increases the total amount available for FY 1991 for administration to \$2.1 billion, which we believe will be adequate to address the increased activity. This includes recently announced grants to 17 states to upgrade their automation systems, which will enhance their ability to administer increased workloads.

In summary, the unemployment insurance program is successfully providing an important line of defense for individuals and families against the effects of the recession. The Administration does not believe revisions to the program are necessary at this time.

Mr. Chairman, this concludes my prepared statement. I hope to work with you and other Committee members to ensure that our programs are responding to the needs of the unemployed in an effective manner. I would now be pleased to answer any questions you or other members of the Committee may have.

PREPARED STATEMENT OF JOHN J. MOTLEY, III

Mr. Chairman on behalf of the National Federation of Independent Business (NFIB) and the more than 500,000 small businessmen and women who are its members I want to thank you for this opportunity to present NFIB's comments on the need for changing the current unemployment insurance program.

NFIB is the nation's largest small business advocacy organization, and our members employ approximately 7 million people. NFIB's membership consists of approximately the same percentage of manufacturers, farmers, accountants, etc. that exist in the national economy. The typical NFIB member employs 8 workers. These firms are Main Street small businesses—they are the backbone of their local economies, and consequently the national economy.

In the 1980's small firms were responsible for over 70% of the more than 14 million net new jobs created. The reason for this phenomenon is that small firms hire people—not machines—to work. People are a small firm's most important as well as most expensive resource. That is why payroll tax issues, like Social Security (FICA) and in this case, unemployment insurance (FUTA), have such a tremendous bearing on the health and viability of small businesses.

HISTORY OF THE FEDERAL UNEMPLOYMENT TAX ACT

In considering whether or not to change the current unemployment insurance program, it is important to recall the reasons for establishing the program over 50 years ago and its success in meeting the needs for which it was designed.

The unemployment insurance system was designed to:

- provide *temporary* cash benefits to those out of work through no fault of their own;

- provide for additional circulation of money during economically disastrous downturns;
- assist the unemployed in finding gainful employment; and
- pay for these benefits through a tax on employers based on the number of employees they hire, the salary they pay those employees, and their unemployment experience rating.

After focusing on the needs the unemployment insurance system was designed to address and how the system is financed, it becomes clear why legislation to expand the current system of benefits is potentially dangerous to our national economy and the economic health of the unemployment system.

In 1935, Congress adopted the Federal unemployment insurance program as part of the Social Security Act. This was the first comprehensive Federal approach. Prior to this time, some individual states had taken the lead in establishing programs of this type for their citizens. For the first time, the Federal Government took the initiative by adding incentives and penalties to encourage participation. As a result, every state that did not have a state unemployment insurance (UI) program prior to 1935 adopted legislation so that they would be able to take advantage of the Federal unemployment tax (FUTA) credit available to employers in states with a state program in place.

Under current law, FUTA tax funds (collected by the Federal Government) are used to finance state and Federal administrative costs of the UI program, the 50% Federal share of the Extended Benefits program, and a loan fund for states that need money to temporarily bolster state trust funds. The Federal Government sets certain basic requirements that states must meet in order to be in conformity with Federal law and eligible for the FUTA tax credit. Since the employers in a state will have to pay an extra 5.4% tax if the state is not in conformity with Federal law, all states are in conformity.

Whereas FUTA is a flat-rated tax, state UI taxes (used to pay for basic unemployment benefits) are experience-rated, i.e. graduated tax schedules based upon layoff experience. The state taxable wage base varies among the states, but must be at least the Federal wage base (\$7,000). These state taxes are used to pay the basic UI benefits and 50% of the extended benefits.

A very important aspect of both the Federal and the state UI taxes is that they are paid solely by the employer. The amount of state unemployment tax an employer will pay is based on: (1) the number of employees working for that employer; (2) whether or not those employees are earning less than the state wage base (which ranges from \$7,000 to \$20,900); (3) and the layoff experience of the employer (the more people they have fired or laid off the higher their state UI tax rate). The Federal UI tax (FUTA) is almost exclusively based on the number of employees an employer has. (The tax could be lower if the employee earns less than \$7,000 a year, but few employees earn less than \$7,000.)

Taxing employers on the number of employees they hire is a strange way to pay for unemployment benefits. Increasing UI taxes increases the cost of hiring, and as a result employers hire fewer workers. Small businesses are particularly hard hit by this type of tax because they tend to be more labor intensive and less likely to be able to absorb any increase cost in labor.

SMALL BUSINESS COMMENTS ON CURRENT LAW

As you may know, six times a year NFIB polls its members on policy issues. Based on these polls, NFIB knows the issue of unemployment insurance is a continuing concern to our small business members. Listed below are a series of positions our members have taken on issues relating to unemployment insurance.

On the overall structure of the UI system, NFIB members strongly support efforts to provide a more fully experience-rated system than is currently in place in most states (78% favor to 16% oppose—Mandate #463, December 1985). In most states small firms with stable work forces typically subsidize employers in declining industries with large layoffs. This shift in the UI tax burden unfairly penalizes good, stable, employers, benefiting employers with high levels of employee turnover.

NFIB members also support (83% favoring while 14% oppose—Mandate #434, June 1981) the change enacted in 1981 in which the national trigger for extended benefits was eliminated and state triggers were substituted. This change more accurately reflected the differing employment situations in the states. States with relatively low unemployment no longer have to pay higher taxes because of the higher unemployment rates in other states.

NFIB members voted in 1985 against the creation of sub-state triggers to determine whether or not a worker should be eligible for extended benefits (10% favor while 65% oppose—Mandate # 459, April 1985).

Not surprisingly, NFIB members also oppose extending the duration of unemployment benefits (9% favor while 86% oppose—Mandate # 430, December 1980). This is not surprising because business owners bear all the costs of the unemployment insurance system but are rarely eligible for benefits themselves even when they go out of business and are unemployed.

NFIB members do, however, support changing current law to increase the amount of administrative funds paid to the states. The Federal Government collects these funds and is supposed to then return them to the states. *Unfortunately, these funds are being kept by the Federal Government to offset the budget deficit.*

Several states have been forced to levy additional taxes on employers because they do not have enough money to operate their unemployment insurance programs. As a result, the employers of these states *end up paying the costs of administering their state's program twice.* This double taxation of employers should be remedied immediately by returning administrative funds to the state.

Another complaint we hear from small business owners regarding the unemployment compensation system is the unfair treatment of some owner-employees. After having paid their FUTA taxes, some small business owners are denied unemployment benefits if their firm goes out of business. NFIB members strongly support (72% supported while 25% opposed—Mandate # 447, February 1983) exempting employers from payment of UI taxes if they are ineligible to receive UI benefits. There is no reason for small business owners to be required to pay unemployment tax on their own salary if, as a matter of law, they are going to be ineligible to collect any benefits.

Although NFIB members have a variety of concerns with the current unemployment compensation system, these concerns are not with the fundamental nature of the system and do not require a major overhaul of the current operations of the system.

IMPACT OF PAYROLL TAXES ON SMALL BUSINESS

The concern of small business over any increase in FUTA taxes is exacerbated by the increasing burden of payroll taxes in general. Over the last decade, income taxes have come down, but payroll taxes have increased. In 1980, employers paid a 5.1% FICA tax on the first \$25,000 their employees earned. Today, employers pay a 7.65% FICA tax on the first \$53,400 their employees earn. A typical small business now pays more in payroll taxes than all other taxes combined.

Increasing reliance on payroll taxes to pay for government benefits is particularly onerous for small businesses. Small businesses are labor intensive and, as a result, pay a disproportionate amount of payroll taxes. In addition, payroll taxes must be paid regardless of whether or not the business is making any money. As a result, small businesses making little or no profit have to pay thousands of dollars in payroll taxes.

Increasing the amount of FUTA taxes small businesses pay should be considered in light of the total payroll tax burden on small business.

THE NEED FOR EXPANSION OF THE TRUST FUNDS

Some have expressed concern over the adequacy of the current state trust funds. They argue that the trust funds need to be higher to weather a recession. NFIB believes the current system is operating well, even though it appears that a couple states may have to borrow money before the end of the year.

The question of state unemployment compensation trust fund adequacy is one about which reasonable men and women can disagree. We view this issue of trust fund adequacy as a balancing act. On the one hand, you do not want the states to have bloated unemployment compensation trust funds because extracting excess tax revenues from employers hurts the economy, and excessive trust fund reserves are an invitation for benefit increases based solely on the dollars available at any given time. On the other hand, states should not sit back and watch their trust funds dwindle down to nothing and then either have to raise taxes in a recessionary period or borrow heavily from the Federal Unemployment Account (FUA). What you want to do is maintain sufficient but not excessive reserves.

In addressing the need to change the current system to develop larger state trust funds, it is important to keep two factors in mind. First, the current system provides a Federal pool of funds from which the states can borrow to allow states to keep their trust funds low. At the end of 1991 the Federal Government currently will

have \$3.35 billion in a fund created solely for the purpose of providing states with additional funding when needed. Second, the states, themselves, currently have all the authority they need to increase taxes in their state to boost the amount of revenues flowing into their trust funds.

NFIB SEES NO NEED FOR THE FEDERAL GOVERNMENT TO ACT ON BEHALF OF THE STATES

It appears that all but a few of the state trust funds will have no problem weathering the current recession, and those few states will be able to borrow from the Federal trust fund.

NFIB also supports repeal of the 0.2% temporary FUTA surtax. The surtax has repaid the debt it was specifically designed to repay—in fact, it has overpaid the debt by almost \$5 billion. It has served its purpose. It is not needed to bolster either the Extended Unemployment Compensation Account (EUCA) or the Federal Unemployment Account (FUA). Those funds are flush.

NFIB is concerned, however, that the ceilings for the EUCA and FUA funds have been raised in recent years as the influx of revenues has come close to reaching the ceiling levels. In 1987 the ceiling for the Extended Unemployment Compensation Account was tripled and the Federal Unemployment Account ceiling was increased by a multiple of five. We fear that as the Federal accounts continue to grow, the ceilings will be raised again.

Raising these ceilings is akin to moving back the ballpark fence in order to deter home runs. What is the point of having these ceilings if we raise them every time we approach them? The Employment Security Administration Account is full, and by the end of 1991, the Extended Unemployment Compensation Account will have over \$8.4 billion.

THE NEED FOR ADDITIONAL BENEFITS

The current UI system has worked well over the past fifty years with its specific goal of providing temporary replacement income to unemployed individuals. In our view and that of many other experts in the field of unemployment insurance, the funding, structure, and delivery system of the unemployment compensation program is not designed to be expanded beyond its current limits.

Taxes are currently sufficient to cover benefits and all states are currently paying statutorily authorized benefits to all eligible Unemployment Compensation claimants. No eligible claimants are being denied benefits. If a state does not have sufficient funds to pay the benefits authorized by state law, it has three choices to make: (1) increase taxes; (2) cut benefit payments; or (3) borrow money from the Federal Unemployment Account (FUA). This is preeminently a matter for the states, who determine benefit levels, to decide.

Another point of contention is benefit adequacy. The question of benefit adequacy is a very subjective issue. It is essentially a question of how much is enough.

As debate on this issue has highlighted, the current UI program does not protect workers who have been out of work for more than 26 weeks (39 weeks if they are eligible for extended benefits). How long unemployment benefits should last is also a question on which reasonable men and women can differ. On the one hand, the program should cover the amount of time it takes most people who have lost their jobs to find another. On the other hand, the system should not be converted into a long-term program for dislocated workers.

The current system already covers the vast majority of workers who lose their jobs. According to the most recent statistics from the Department of Labor, 88 percent of workers who lost their jobs in 1988 found another job in less than 26 weeks. Although the number of workers who will find a job will likely fall a slight amount because of the current recession, Congress should still weigh the cost of expanding unemployment compensation against the relatively minor number of workers who would benefit.

NFIB understands the argument of those who maintain that the Unemployment Insurance system does not adequately address the problems of the long-term unemployed and the dislocated worker. Although we recognize this as a significant societal problem, the Unemployment Insurance program was not designed to address this problem. It was designed to provide short-term wage replacement to unemployed workers as a bridge between jobs. A complex safety net of other Federal programs is already in existence to protect those who find themselves out of a job for an extended period of time. The UI system was not designed to be a social welfare program, and it should not be turned into one.

Do not forget that the UI program is funded by a tax that employers pay on all of their employees. In effect this tax is a direct tax on jobs. Increasing this tax to pay

for extended benefits will make it that much more likely that employers will not hire any additional workers, resulting in an increase in the unemployment rate.

COMMENTS ON H.R. 1367, THE UNEMPLOYMENT INSURANCE REFORM ACT OF 1991

Allow me to comment briefly on the only legislation that has been introduced to date on expanding unemployment benefits, H.R. 1367. This bill was introduced by Rep. Downey (D-NY) on March 11, 1991.

NFIB members strongly oppose increasing the wage base to pay for the new Federal extended benefit program. NFIB members have historically opposed increasing taxable wage bases because they have traditionally been tied to increases in taxes. Last year, Senator Moynihan broke with tradition by introducing legislation that would increase the FICA taxable wage base but coupling the increase with a decrease in the tax rate. The net effect of the Moynihan legislation is that it would result in a tax cut for all working taxpayers. NFIB supports Senator Moynihan's efforts.

H.R. 1367, however, is not a tax cut. In fact, employers will experience a tax increase because the wage base is raised immediately, but the cut in the tax rate is delayed. In 1992, employers will have to pay more FUTA tax on every worker earning more than \$7,467. In that year, an employer hiring a worker for \$18,000 will have to pay 241% more FUTA tax under H.R. 1367 than that employer has to pay under current law. This legislation does not really address the regressive nature of the FUTA tax until 1994-5.

Although H.R. 1367 does eventually address the question of the regressive nature of FUTA taxes, the regressivity of the tax is really a secondary issue. The primary issue is whether or not this country really needs to raise taxes in order to spend \$24 billion more on unemployment insurance benefits. As mentioned above, Department of Labor statistics show that very few workers are unemployed for more than 26 weeks. The system adequately serves those it was designed to serve—workers in between jobs.

It makes little sense to increase a tax that is a direct tax on jobs to pay for increased unemployment benefits. If instead of paying \$27 billion in taxes for expanded benefits employers could use that money to hire extra workers, they could afford to hire 270,000 workers for five years at \$20,000 per year. NFIB strongly believes that employment taxes should be kept as low as possible to avoid discouraging employers from hiring new workers.

The effects of H.R. 1367 are not limited to the Federal portion of the unemployment insurance system. H.R. 1367 also seriously undermines the states' ability to determine who is eligible to receive benefits and who is not. Historically, the states have been almost exclusively in charge of determining eligibility and paying unemployment benefits. Limiting the ability of states to determine who is ineligible for benefits will greatly increase the cost of state programs, resulting in increased state borrowing from the Federal trust funds or higher state unemployment taxes. Under this system, the incentive is too great for the Federal government to expand benefits if the state governments then pick up the tab.

Federal tinkering with state eligibility requirements will force states to increase their unemployment insurance taxes to pay for the increasing number of unemployed workers who are eligible for benefits.

CONCLUSION

The current unemployment system provides 26 weeks of benefits for people who are out of work and between jobs. In addition, the current system provides an extra 13 weeks of benefits to workers who are out of work and happen to be living in states in which unemployment is high. According to the Department of Labor, only 12 percent of the unemployed were out of work for more than 26 weeks.

The current system was not designed to provide for, and cannot afford to provide for, individuals who are unemployed for very long periods. The Federal Government already has an intricate safety net of programs designed to help those whose income has dropped below a certain level. After current unemployment benefits end, workers are not left out in the cold. They may be eligible for benefits from AFDC, Medicaid, Food Stamps, WIC, the school lunch program, etc. The unemployment insurance system was not designed to be a worker welfare program, and it can only be converted into such a program at great cost to our national economy.

In the midst of a recession and gradually increasing unemployment, legislation boosting unemployment insurance benefits will increase the cost of hiring workers. The last thing Congress should do in the midst of an economic downturn is increase

a tax on jobs. Congress should be encouraging employers to hire more employees, not discouraging them.

PREPARED STATEMENT OF ALAN REUTHER

Mr. Chairman, my name is Alan Reuther. I am an Associate General Counsel with the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW). On behalf of its 1.4 million active and retired members, the UAW thanks the Committee for the opportunity to testify on the critical subject of unemployment insurance reform and financing issues.

In our view, the current recession is unlikely to be the short, painless affair which some have predicted because the recovery preceding this recession had some unique aspects. Unlike previous recoveries, the 1980s saw an increase in inequality and a decline in real median weekly earnings. Despite the recovery, the U.S. has lost 2 million manufacturing jobs since 1979, jobs that traditionally pay above average wages and boost the whole economy. Moreover, the recovery was built largely on a foundation of debt. *Business Week* reported at the beginning of the recession that the ratio of private debt to GNP was 1.4 to 1 in 1989 and 1990. In 1981 and 1982, that ratio was only 1 to 1.

It is worth remembering how slow economists were to realize the depth of the 1981-82 recession. As late as December of 1981, the consensus forecast said that first quarter 1982 would see GNP decline by only .8 percent. This was overly optimistic by a full 5.1 percentage points. In May of 1982, the consensus was that unemployment had already peaked at 9.2 percent. Six months later, the unemployment rate was 1.5 percentage points higher. Although the consensus forecasts tend to be optimistic, the current consensus predicts slow growth, .1 percent, for the coming year. The March consensus also says unemployment rates will stay above six percent through 1992. Under these conditions, talking about "recovery" will have little meaning for the unemployed. Indeed, as John Bregger of the Bureau of Labor Statistics told a House Subcommittee, long-term unemployment didn't peak until six months *after* the 1982 recession ended.

Already 1.5 million workers have already lost their jobs since last June, placing an increased strain on state unemployment agencies and trust funds. More than half of that number represents lost manufacturing jobs. Administrative funding for the current fiscal year is well short of the levels required by the states to operate their programs in light of these new claims. Unless Congress acts swiftly, the existing shortcomings of our nation's unemployment compensation system will result in needless delays, hardships, and suffering on the part of unemployed workers, their families, and their communities.

SHORTCOMINGS IN THE UNEMPLOYMENT INSURANCE SYSTEM

We are entering this recession with our unemployment compensation system in its worst shape ever. Trust funds in many states have inadequate reserves, state and Federal legislative actions have cut the proportion of the unemployed eligible for unemployment benefits, and benefits are too low to adequately assist those who receive them. The state unemployment security agencies do not have sufficient administrative funds to operate their unemployment insurance programs effectively.

The Federal-State unemployment insurance system was enacted in the mid-1930s in recognition of the enormous costs borne by unemployed workers facing economic, political and social forces over which they have no control. Two major goals were set: first, to cushion workers against economic hardship when they become unemployed; second, to bolster purchasing power when total spending is declining, thereby helping to automatically stabilize the economy when it is weak. These twin goals are closely related—an adequate level and duration of benefits is required to ease private hardships and strengthen a community's purchasing power during a period of economic decline and increasing unemployment.

Not only have unemployed workers and their families suffered from the shredding of the safety net provided by the unemployment insurance program, but employers and their businesses, the communities in which the unemployed live and ultimately the entire economy is hurt by the shrinkage of the unemployment insurance system. The costs arising from unemployment and the exhaustion of benefits are being borne privately in the homes of the unemployed—private costs that range from financial insolvency and the inability to pay for urgently needed medical care to the rise in intra-family tensions and health care problems. The costs also are being borne socially as the long-term impacts of the additional welfare costs, higher

crime, community instability, and mental health problems associated with increasing unemployment begin to spread.

Currently, trust funds of several states do not have sufficient reserves to pay benefits throughout the recession. If past recessions are any indicator, this means the unemployed workers in those states will be faced with unemployment cutbacks during the downturn to reduce benefit payments and reduce or prevent Federal borrowing by states. This not only hurts the unemployed workers and their families, but further reduces the countercyclical effects of the unemployment compensation system.

If the current situation persists, only 1 in 3 unemployed workers will draw unemployment benefits in the current recession. This is a decline from 1980, when one half of unemployed workers were paid benefits. In about a dozen states, fewer than 1 in 5 unemployed workers will receive a check. At the same time, over half the unemployed workers in Rhode Island, Alaska, and Massachusetts will be compensated during their period of unemployment.

Those workers who do receive unemployment benefits will receive an average benefit check of about \$160 a week, which will replace only about 35 percent of average weekly wages. Again, in some states the situation is far worse than the average. In a dozen states, average benefits replace a third or less of that state's average wages. California's average weekly benefit for 1990 was \$123, which replaced only 26 percent of California's average weekly wages. In Indiana, the average weekly benefit of \$105 replaced only 27 percent of the state's average wage.

In comparison, workers in Canada, the United Kingdom, France, and Germany receive much better protection from their nation's unemployment compensation systems. These industrialized countries pay higher benefits to a larger percentage of the unemployed for a longer period of time than in the United States. See Exhibit 1.

In the UAW's view, U.S. workers deserve a level of assistance similar to that of Canada and Europe. Instead, over the last decade our unemployment compensation system has moved in the wrong direction. Sadly, the shortcomings in the unemployment insurance system are in large measure the result of legislative actions. At the Federal level, restrictions on extended benefits, interest on Federal loans, solvency requirements, and taxation of benefits have contributed to the decline in the unemployment compensation system. At the state level, the majority of states adopted tighter earnings requirements or tougher disqualification provisions to avoid or reverse solvency problems. Some states froze or reduced unemployment benefits. The time has come to reverse the trends of the 1980s and restore our unemployment compensation system's ability to protect jobless workers and to counteract an economic downturn. In order to do so, the UAW would suggest a number of reforms.

EXTENDED BENEFITS REFORM

In recent years, the long-term unemployed have been without an effective extended benefits (EB) program. Under the EB program, a jobless worker who has exhausted all regular state benefits may receive up to 13 additional weeks of benefits. EB is intended to ease the additional hardships which fall on unemployed workers during a serious downturn in the economy. When hard times are widespread, the length of unemployment spells increase as jobs become more scarce. EB helps fill the gaps which occur when state benefits are exhausted.

In order to offer extended benefits, a state's unemployment level must exceed a threshold. The 1981 Omnibus Budget Reconciliation Act raised the EB threshold, making it nearly impossible for states to qualify for extended benefits. As a result, EB has not been available during periods of serious economic slowdowns in many states over the last decade.

Before the changes in 1981, a state could trigger on extended benefits if its insured unemployment rate (IUR) was above 4 percent and if its IUR was 120 percent higher than the State rate for the previous two years, or if State insured unemployment rate was above 5 percent. The 1981 changes raised both of these threshold rates by a full percentage point and eliminated a national trigger by which all states would qualify for extended benefits when the national IUR was above 4.5 percent.

The effective elimination of EB has undoubtedly contributed to the decline in the proportion of the unemployed receiving unemployment insurance. One step which would reverse the trend in the proportion of the unemployed receiving unemployment insurance would be the restoration of the EB program, or the adoption of an effective replacement for EB.

Any effective reform of the EB program should set more realistic trigger levels, exempt EB outlays from sequestration, and raise the ceiling on EB trust fund accounts in order to assure adequate funding for EB.

The enactment of any EB reform program must include the adoption of realistic EB triggers. Many observers believe that the use of a total unemployment rate (TUR) trigger would improve the accuracy of our EB triggers. The UAW will support any measure of unemployment as an EB trigger, so long as it is set at a level which will provide EB during periods of economic slowdowns.

The UAW believes the Committee should consider making the EB program completely federally funded. This would relieve the added pressure on state trust funds caused by paying its EB share when the state is experiencing high unemployment.

In addition to the enactment of realistic EB triggers, a more longstanding restriction on EB should be reexamined. This restriction is the trigger provision which requires a state's unemployment rate to be 120 percent of the rate for the comparable period two years earlier. This restriction cuts off EB in a state which has relatively constant, but high, levels of unemployment.

For example, in June 1983, Michigan triggered off the EB program despite a total unemployment rate of 14.6 percent. Ohio triggered off EB in May 1983 when unemployment was 12.9 percent. New York never triggered on EB during the 1982-83 recession despite an unemployment rate that reached nearly 10 percent in early 1983. Later in the decade, during the downturn in the oil industry, Louisiana triggered off EB in March 1987 despite an unemployment rate of 12.7 percent. While unemployment in Louisiana remained over 10 percent for two more years, extended benefits were never available to assist the long term unemployed. Rather than using the blunt instrument of the 120 percent provision, a more precise EB cutoff would require a tangible improvement of a state's current unemployment picture.¹

THE NEED FOR FEDERAL STANDARDS

The last decade provides clear evidence that, in the absence of Federal standards, our nation's unemployment insurance system will not adequately protect unemployed workers. In too many cases, the Federal partner has required or encouraged states to restrict unemployment insurance eligibility. In other cases, the states have acted to limit the costs to employers of their unemployment insurance systems without sufficient regard for the income maintenance and countercyclical purposes of the program.

Unfortunately, unemployment insurance at the state level is not debated in terms of the twin national purposes of the program—providing a prompt wage replacement for unemployed workers and preserving the level of economic activity during a downturn. Instead, state administrators, governors and legislators typically view unemployment insurance in the context of a "business climate" discussion, often in terms of how to bring one state's unemployment costs into line with those of its neighbors.

More often than not, the result of such discussions has been the enactment of higher earnings requirements for program eligibility and stricter disqualification provisions. As a consequence, the economic interests of the entire employer community in preserving the purchasing power of unemployed workers has been lost. Moreover, the states have, in effect, been in competition with one another to reduce their unemployment costs. As a result of this competition, the last decade has seen a steady deterioration in the unemployment insurance system's ability to satisfy its twin purposes.

The national goals of unemployment insurance system deserve national safeguards. Therefore, the UAW urges the adoption of national standards to match national goals in the following four interrelated areas.

TRUST FUND SOLVENCY

During the 1980s, one of our nation's longest periods of relative economic stability, state trust fund solvency did not improve dramatically. While experts may disagree on the extent to which trust fund solvency is a problem in particular states, the fact remains that several states will be forced to borrow Federal funds to pay

¹ 1980 and 1981 amendments to the EB program act as an incentive for the states to adopt restrictive legislation for their regular state unemployment insurance programs. These restrictions work by requiring states to pay for the Federal share of EB or requiring certain features in the regular UI program before workers can receive EB. For example, current EB provisions encourage states to require at least 20 credit weeks for basic eligibility and impose a waiting week for state unemployment benefits. Ironically, since EB has been so tightly restricted in the last decade, some states have resisted the pressure to adopt these and other EB restrictions in their state programs. The existence of these restrictions furnish a significant rationale for states to adopt restrictions in their regular unemployment programs in our experience. These restrictions should be repealed.

unemployment benefits in the current recession. In other states, solvency concerns will arise, even if borrowing is not necessary. There is no state, to our knowledge, which has its trust fund in a position to pay adequate benefits to a reasonable proportion of its unemployed workers through a severe national recession.

There are two ways for states to achieve solvency. One way is to levy increased payroll taxes on its employers. Employers naturally oppose increased taxes. Employers view unemployment taxes as a cost of doing business which should be minimized to the greatest extent possible. In fact, the Congressional Research Service found in its January 1990 study that effective unemployment tax rates have *fallen* since 1984. In short, employers, governors, and state legislators, for the most part, have not sufficiently concerned themselves with the social insurance goals of unemployment insurance.

The second way for states to move toward solvency is to cut the size of their unemployment insurance programs. To do so, many states have adopted unemployment benefit freezes or reductions, restrictions on program eligibility, and stricter disqualifications. In its September 1988 report, the General Accounting Office found that 44 states adopted tighter monetary eligibility standards or stricter disqualification provisions between 1981 and 1987. Other states imposed benefit freezes or reductions and lowered the maximum number of weeks for which they paid benefits.

Typically, the issue of tax increases or program restrictions is faced during a period of economic downturn. As a result of the increased benefit payments and solvency pressures on the trust funds, unemployment insurance cost reduction is on the states' political agenda. In this setting, an "equality of sacrifice" theme develops. Workers are expected to give a roughly equivalent amount in program reductions to reflect the increases in employer payroll taxes. Yet, a close examination of state level actions shows that benefit reductions and tax increases enacted in the 1980s have not sufficiently increased trust fund solvency.

In Michigan, two legislative packages of increased taxes and program reductions were passed in 1981 and 1982. The packages were negotiated and agreed upon by representatives or organized labor, business, the governor and legislature at a time when Michigan was the largest debtor state. These changes raised the monetary eligibility from 14 credit weeks to 20 weeks, increased the earnings required for a credit week from \$67.00 to \$100.50, froze the maximum benefit at \$197 for four years, and reduced benefits from 70 percent to 65 percent of take-home pay through calendar year 1986. The percentage of workers receiving a benefit in Michigan fell from 36.2% in 1981 to 28.2% in 1986. Employers saw the maximum payroll tax rise from 9 to 10 percent, the taxable wage base rise in annual steps from \$6,000 to \$9,500 in 1986, and a solvency tax on negative balance employers.

Michigan's program temporarily helped the state's trust fund move toward solvency. Significant repayments of Federal interest-bearing debt were made and some FUTA penalty taxes on employers were avoided. By 1986, actual benefit payments were lowered by \$3.2 billion below the projected level before the 1982 amendments and employers had paid \$1.6 billion in increased taxes.² Despite this, due to the structure of the state's experience rating system, Michigan's system did not reach solvency. Instead, as the high unemployment years of the early 1980s dropped out of the five year base period used for experience rating purposes, employer taxes began falling.

As a result, revenues were sufficient to pay current benefits and a portion of Michigan's old, non-interest-bearing debt, but not adequate to build trust fund reserves. By late 1988, neutral observers had concluded that further benefit restrictions would have little, if any, impact, on long-term solvency, since any "savings" achieved through benefit reductions would flow through the experience rating system and further reduce employer payroll taxes.³ At this point, discussions of further legislative changes in Michigan's unemployment insurance system deadlocked. Michigan's system entered the current recession as among the most insolvent in the nation.

Illinois provides a different scenario. In 1983, faced with a large Federal debt, Illinois passed a negotiated package of tax increases and benefit reductions. The package was designed to split the sacrifices 60 percent on business and 40 percent on workers over a three year period. An increase in the taxable wage base from \$7000 to \$8500 in the third year, a shift in the maximum tax rate from 5.7 percent to 7.1 percent, and a small percent surtax were expected to produce \$1.15 billion in added

² Economic Alliance for Michigan, *Unemployment Insurance Report* (July 1986), 3-4.

³ Economic Alliance for Michigan, "Memorandum Re: Solvency Issue," September 30, 1988.

revenue. On the workers' side, the maximum benefits were decreased with an expected "savings" of \$780 million dollars.

In 1987, a second negotiated package was passed by the legislature. Under this five-year-package, benefits were increased by 4 percent each of the first three years and employer payroll taxes were reduced an average of 7 percent. This was accomplished by switching the trust fund to a "pay as you go" system, which is designed to automatically raise taxes if the trust fund balance fell below \$750 million. If the trust fund balance falls below \$250 million, and other conditions are met, benefits are reduced by 10 percent. By taking this approach, Illinois turned away from the idea that trust fund solvency is reached by accumulating reserves prior to a recession. Instead, Illinois has opted to rely on the ability of its employers to pay for increased benefits near the time they are paid to workers.

As a consequence, the Illinois trust fund collects additional revenues during an economic downturn, rather than during a recovery. In the view of many observers, this violates social insurance principles and could adversely impact Illinois' employers by raising taxes when they are already affected by a recession. To date, Illinois' trust fund has climbed from a reserve multiple of .13 at the end of 1987 to .55 at the end of the third quarter of 1990. In our view, the jury is still out on the "pay as you go" approach to trust fund financing.

In both Michigan and Illinois, the state trust funds were subjected to severe financial strains due to a national economic downturn. Forced to negotiate under these terms, the workers and employers of both states made sacrifices, but these sacrifices did not produce an enduring resolution of the solvency issue in either state. More importantly for today's hearing, the unemployment insurance systems in Illinois and Michigan were forced to cope with the problems caused by a national economic crisis by turning away from the national unemployment system's goals.

In the long term, underfunding the unemployment insurance system helps keep benefits low and provides a rationale against efforts to improve the system. In periods of high unemployment, states will respond by restricting benefits and raising taxes at the time when both workers and employers can least afford it. Congress should adopt a trust fund solvency standard to require states to build up sufficient trust fund reserves during economic good times.

Most experts are agreed that a reserve multiple is currently the best indicator of trust fund solvency.⁴ For a number of years, the Department of Labor has employed the 1.5 high cost multiple as its measure of solvency. We believe a 1.5 reserve multiple is a reasonable balance between prudence in building adequate reserves and the costs of collecting and holding excessive taxes in trust funds. A Federal standard should require states to reach or exceed a reserve multiple of 1.5 in periods of economic recovery. Such a standard should be put in place gradually over a period of years.

BENEFIT ADEQUACY

Simply adopting a trust fund solvency standard will not move the unemployment compensation system in the right direction. Unless a Federal standard for benefit adequacy is also adopted, many states will reach solvency by simply restricting benefits. In fact, there is some evidence that this is already the situation. Seven states had high cost multiples over 1.5 in fiscal year 1990. Of these seven states, South Dakota and Oklahoma ranked in the bottom five states and Mississippi and New Mexico ranked in the bottom eleven states in terms of the proportion of their unemployed receiving a benefit. See Exhibit 2. In other words, these states have achieved solvency, at least in part, by reducing the scope of their unemployment programs.

In 1980, the National Commission on Unemployment Compensation recommended that Congress require states to have a maximum weekly benefit not less than two thirds of the state's average weekly wage. The Commission further recommended that Congress require that states pay weekly benefits which replaced, on average, at least 50 percent of the individual's wage. We urge the Committee to adopt a similar approach.

In the eleven years since the National Commission made this recommendation, the need for its adoption has grown considerably. The national benefit replacement rate has declined from .361 percent to .349 percent in 1988. The enactment of a Federal benefit adequacy standard, in conjunction with a trust fund solvency standard,

⁴ The reserve multiple is calculated by dividing the ratio of net trust fund reserves to total covered payrolls by the ratio of benefit payments to total covered payrolls. See Wayne Vroman, *Unemployment Insurance Trust Fund Adequacy* (Kalamazoo, Michigan: The Upjohn Institute, 1990) at 44.

would be an important step in addressing the shortcomings of today's unemployment insurance system.

MONETARY ELIGIBILITY

The states have not only reduced or frozen unemployment benefits over the past decade, but most have taken other legislative actions which have limited access to benefits. The Department of Labor contracted for two studies that found that state administrative actions contributed to the decline in the proportion of the unemployed receiving unemployment insurance. A study by Mathematica Policy Research in 1988 estimated that state actions caused from 22 to 39 percent of the decline. More recently, Wayne Vroman of the Urban Institute completed an analysis of a special supplement to the Current Population Survey. Vroman likewise found that state statutory and administrative changes have probably contributed importantly to the decline in receipt of unemployment benefits over the last decade.

In order to further examine the effect of state law changes on the decline in the receipt of benefits, the UAW Research and Legal Departments examined the states which paid the highest and lowest proportions of their unemployed workers during the decade of the 1980s. Six states paid less than 1 in 4 of their unemployed workers a benefit, on average for the years 1980 through 1989. These states are Virginia (18%), Florida (19%), Texas (21%), South Dakota (21%), Indiana (25%), and Oklahoma (25%). In contrast, the top six states were Rhode Island (63%), Alaska (53%), Massachusetts (49%), New Jersey (45%), Vermont (44%) and Pennsylvania (44%). See Exhibit 3.

State unemployment insurance statutes were examined for two factors which commonly restrict a state's unemployment insurance programs: the monetary earnings requirement for benefit eligibility and the type of disqualifications imposed upon claimants. Exhibit 4 summarizes our findings.

The monetary earnings provision is the number of weeks of work or the amount of wages that a state requires for threshold unemployment insurance eligibility. These provisions commonly use a "base period" of 52 weeks or the first four of the last five calendar quarters to measure an individual's labor market attachment. Eligible workers with low base period earnings receive a correspondingly lower weekly benefit amount and a shorter duration of benefits, but workers who do not meet the earnings eligibility requirement get no benefits.⁵

Comparing the current legal situation in the states with the highest and lowest percentages for receipt of benefits, it is immediately evident that, in general, states with the lowest reciprocity levels have higher earnings requirements and stiffer disqualification penalties in their UI laws. See Exhibit 4.

Among the states which pay the highest portion of their unemployed workers, their earnings requirements are lower, in monetary terms, than those in the lowest states. For example, in Alaska a claimant must earn \$1000 in total base period wages and must have wages in two of the four calendar quarters in the base period. Rhode Island adopted a somewhat stiffer earnings requirement in 1989 than was previously in effect. A claimant is required to earn two hundred times the \$4 an hour minimum wage in a quarter, have base period wages equal to 1½ times his or her high quarter wages, and have base period wages of 400 times the minimum wage to qualify for benefits. An alternate qualifier makes a claimant eligible if he or she earns \$4800. Massachusetts has an earnings eligibility provision which calls for a claimant to earn 30 times his or her weekly benefit amount, but not less than \$1200, in the base period. New Jersey expects claimants to earn 20 "base weeks" or \$6200 in the base period. A "base week" is earned when weekly wages equal 20% of the statewide weekly wage. In 1991, this figure is \$103. Vermont has an earnings requirement of wages of \$1000 in a single quarter and wages equal to 40 percent of total base period earned outside the high earnings quarter. Pennsylvania has a similar provision which requires base period wages of \$1320 with at least 20 percent of total base period wages earned outside the high earnings quarter.

⁵ The National Commission was divided on the question of how much previous work should be required for receipt of the maximum 26 weeks of benefits. The Commission recommended to the states that "substantially" less than 39 weeks of work be required for 26 weeks of benefits and that no less than 14 weeks of work should entitle a claimant to 26 weeks of benefits. In an indicator of how far the discussion has shifted in the last eleven years, the Commission did not make any recommendations on minimum earnings requirements. The Commission did note a Department of Labor "recommendation" that a range of 14 to 20 weeks of work or the equivalent in earnings be sufficient to qualify for benefits, depending on each state's determination of what was appropriate for that state.

In contrast, states with the lowest rates for receipt of benefits have stiffer basic earnings requirements. For 1991, Virginia requires a claimant to earn \$3000 in the two highest quarters of earnings in his or her base period. The requirement was \$2800 in two quarters for 1990. Florida demands that a claimant earn his or her average weekly wage for 20 weeks, with the average wage no less than \$20 a week. A claimant in Indiana must earn wage credits of not less than \$1500 in the last two quarters of his or her base period *and* at least \$2500 in the base period and have base period wages at least 1.5 times his or her high quarter wages. South Dakota expects a claimant to earn at least \$728 in his or her high quarter and 30 times his or her weekly benefit amount outside the high quarter. Texas requires a claimant to earn 37 times his or her weekly benefit amount and have wages in two quarters. In Oklahoma, a claimant must have earnings greater than 40 percent of the taxable wage base and earn 1-1/2 times his or her high quarter wages in the base period. The taxable wage base for 1991 is \$9700.

It is something of a simplification to translate these earnings eligibility requirements into monetary terms, since this omits the requirement, which is found in some of the states, to earn wages over certain quarters. However, translation into monetary terms offers a quick summary of the variation between states. In all cases, Exhibit 4 uses each specific state's 1989 average weekly benefit amount or average weekly wage for mathematical purposes. For example, in Texas, the earnings eligibility requirement of 37 times the weekly benefit amount is translated into monetary terms by multiplying the state's 1989 average weekly benefit (\$159) by 37.

The UAW believes that the Congress should enact a Federal standard which sets a floor below which states cannot go in restricting their unemployment insurance programs. Such a standard would be in keeping with the twin goals which initially motivated the system. In our view, a worker who works 20 hours at the minimum wage for 14 weeks should not fall below this floor. Keep in mind that low wage or part-time workers will get also lower benefits, often for shorter durations, than higher wage workers with greater labor market participation. However, these workers should not be completely excluded from our unemployment insurance system.

DISQUALIFICATION PROVISIONS

Individuals laid off from their jobs form the basic group of unemployed workers for whom the UI system is intended to provide benefits. However, in all states there are statutory disqualification provisions which govern the circumstances for payment of UI benefits to workers leaving their jobs voluntarily or as a result of discharges by their employers. Workers who refuse an offer of suitable work are also subjected to disqualifications in all states. These three disqualification provisions vary from state to state in terms of their scope and the severity of their penalty provisions.

The basic distinction in penalty provisions lies between states which disqualify claimants for a period of weeks of unemployment ("suspension or denial period") and those which require a claimant to find work and earn specified wages, sometimes for a specific number of weeks, in order to terminate the disqualification ("durational or full spell disqualification"). This latter type of disqualification provision is termed a "durational disqualification" because it operates to deprive claimants of benefits for the entire duration of a spell of unemployment. In other words, the unemployed must work before they again qualify for unemployment benefits.

Beyond these two basic types of disqualification provisions, some states employ additional penalties. Some states reduce the number of weeks of potential benefits or cancel wage credits. In the event the worker does have enough earnings to satisfy the disqualification penalty, he or she will have a reduced entitlement to benefits if laid off again in the same benefit year.

A number of states have also adopted voluntary quit disqualifications which result in a laid off worker being disqualified due to a previous voluntary leaving from a job held prior to his or her most recent employment. In effect, the quit disqualification "follows" the worker to the next job and disqualifies him or her at the time of layoff from that job. These punitive measure are partially ameliorated by permitting a worker to leave for a better job or ending the disqualification if the second job which the quitter takes lasts a specified number of weeks.

The National Commission recommended to Congress that states not be allowed to use reduced benefit rights as a disqualification for any action other than fraud and receipt of disqualifying income. The Commission also recommended that the states not employ "durational disqualifications." The Department of labor agreed with both of these positions in 1979.

There is no question that "durational disqualifications" and their severity have spread over the last decade. In January 1976, 19 states imposed "durational dis-

qualifications" for misconduct discharges. Currently, 39 states have such provisions. Thirty one states imposed durational disqualifications for voluntarily leaving work in 1976. Under present law, 47 of the 51 jurisdictions impose a durational disqualification for voluntary quits. In addition, some states now require fairly long periods of work to satisfy their disqualification provisions. Several states use 10 or more weeks or 10 or more times the worker's weekly benefit amount to end a disqualification.

The statutory disqualification penalties for refusals of work, discharges for misconduct, and voluntary leavings were examined in the ten states under study. Again, the unemployment laws of the five states which compensate the highest proportion of their unemployed workers had more lenient disqualification provisions than the five lowest states. See Exhibit 4. A more detailed discussion of the disqualification penalties, beginning with the lowest states, gives a fuller picture of the contrast between the highest and lowest states.

South Dakota imposes a durational disqualification under which a claimant must work 6 weeks and earn wages equal to or greater than his or her weekly benefit amount in each of those weeks. This is termed a "6 x 6" disqualification in the UI trade. Texas does likewise. Virginia penalizes claimants found disqualified by requiring the individuals to perform services for 30 days. These days need not be consecutive and need not be in UI covered employment. Indiana exacts a stiffer penalty, which provides that a claimant must work eight weeks and earn eight times his or her weekly benefit amount (8 x 8) to terminate a disqualification. In addition, the agency may reduce a claimant's benefit entitlement by up to 25%. Florida has the sternest disqualification penalties. It imposes a disqualification penalty for voluntary leavings, misconduct discharges, and refusals of work which requires a worker to earn 17 times his or her weekly benefit amounts. The refusal of work disqualification is linked with a discretionary 5 week penalty period or a 3 week reduction in benefit duration. The severity of these impediments defeats the national need for a fair and consistent response to the hazards of unemployment.

In contrast, the states with the highest average jobless beneficiary rates used denial periods rather than durational disqualifications or had shorter earnings penalties for ending a durational disqualification. New Jersey uses staggered denial periods. A claimant must serve a 4 week denial period for refusals of work, a 5 week denial period for voluntary quits (which can be terminated at any time with a 6 x 6), and a six week denial period for misconduct discharges. Massachusetts uses a 4 x 4 durational disqualification for voluntary leavings and discharges for "deliberate misconduct." In the case of a work refusal, Massachusetts imposes a 7 week denial period and a reduction in benefit entitlement to no more than 8 weeks of benefits following the denial period. Alaska's penalty provisions are a hybrid of denial periods and durational disqualifications. For all three types of disqualifying acts, Alaska requires a claimant to serve a 6 week denial period. In addition, the claimant's benefit entitlement is reduced by the *lesser* of 3 times the weekly benefit amount or the amount of any remaining benefits. All penalties can be satisfied if the claimant serves an 8 x 8. Rhode Island has a penalty provision which requires a claimant to have 4 weeks of work at least 20 times the minimum wage (\$4 an hour in 1991).

Current law forbids a state from cancelling wage credits or totally reducing benefit rights for any action other than discharge for misconduct, fraud, or receipt of disqualifying income. Obviously, many of the states have misused the flexibility granted to them under current law to adopt overly punitive disqualification provisions. The UAW supports a Federal limitation preventing the states from disqualifying workers for more than a 6 week denial period for any disqualifying act, other than program fraud, or serious incidents such as theft or assault which are connected to the claimant's work.

Thus, Mr. Chairman, based upon our examination of the role of state law restrictions on the decline in the proportion of the unemployed receiving benefits, we are convinced that these laws have contributed to the decline which has occurred during the 1980s. We urge the adoption of Federal standards to limit the freedom of states to impose overly strict disqualification penalties. The adoption of these standards would be an important step to fairer treatment of unemployed workers and restoration of the unemployment insurance system.

OTHER PROPOSALS FOR GREATER FAIRNESS

Mr. Chairman, the UAW urges the Committee to consider a number of other comments and proposals as part of any comprehensive reform of the unemployment insurance system.

- In order for the unemployment insurance system to work effectively for unemployed workers, their employers, and the affected communities, state employ-

ment security agencies must have adequate administrative funds. The UAW supports an adequate level of administrative funds tied to current workload indicators and automatically supplemented in the case of increases in workload. The current system has underfunded state agencies for a number of years and should be revised.

- Nonprofessional educational employees who are unemployed during summer recesses through no fault of their own should not be deprived of unemployment insurance without a written, legally-enforceable assurance of reemployment from their employers. Current Federal law requires bus drivers, janitors, clerical, and other nonprofessional school employees to file claims, seek work, and otherwise comply with UI eligibility requirements, with a retroactive payment of benefits made in the event that reemployment does not materialize in the fall. The retroactive payment of unemployment benefits, if reemployment does not occur, is no substitute for the timely payment of benefits. The revision of this law would provide greater justice to nonprofessional school employees.

- In some states, the courts have utilized unemployment insurance decisions to prevent workers from pursuing employment-related lawsuits. These courts applied the doctrine of collateral estoppel. Denying collateral estoppel effect to the decisions of state UI agencies preserves the informality and speed essential to the UI appeals process. The UAW urges the Committee to prohibit this practice.

- Financing should be strengthened by raising the current taxable Federal unemployment insurance wage base in steps up to the Social Security taxable wage base and by assuring that the unemployment insurance base thereafter keeps pace with the base for Social Security.

- Unemployment insurance financing should be based on a uniform Federal tax. In the absence of such a tax, the experience rating system should insure that all employers share at least part of the costs of unemployment. A program of cost-equalization and reinsurance, across the states, should be established to reduce the burden on those states experiencing abnormally high costs during a national recession.

- Taxation of unemployment insurance should be repealed. Federal taxation of unemployment insurance benefits is, in effect, a federally mandated reduction in benefit amounts which only exacerbates the need for increased weekly benefit amounts.

- The unemployed insurance trust funds should be removed from the Federal unified budget. These monies are reserved for the payment of unemployment insurance benefits and administrative costs. Their inclusion in the budget for bookkeeping reasons should be stopped.

- Unemployment insurance should not be reduced by pension income. Social Security, separation, severance or termination pay. We have worked with others to repeal the Federal law requiring states to provide for reduction of unemployment insurance by pension income after March 1980.

CONCLUSION

Mr. Chairman, the decade of the 1980s was a decade of decline for our nation's unemployment insurance system. In our view, the lack of solvency in the state trust funds created pressures which resulted in the adoption of restrictive state legislation. This state legislation contributed importantly to the decline in the unemployment insurance system. The time has come for the enactment of a comprehensive program of unemployment insurance reform which will reverse the decline and restore the effectiveness of our unemployment insurance system as an income maintenance and countercyclical program.

The UAW appreciates the opportunity to present our views on coverage and financing issues in the unemployment insurance system. We look forward to working with the members of this Committee as you consider these important issues. Thank you.

Exhibit 1

	Percent of the Unemployed Receiving Benefits (1985) (1)	Duration of Benefits (1989) (Months) (2)	Jobless Payments as a % of GDP (4)	Replacement Rate (2)	
U.K.	90	13	1.62	40%	(3)
France	72	3	2.87	42%	
Germany	72	4-13	2.32	68%	
Sweden	68	10	2.38	30%	
U.S.	34	6.5	0.62	35%	(5)
Canada	NA	6.25	2.09	60%	

(1) Gary Burless, "Jobless Pay and High European Unemployment," in Robert Lawrence and Charles Schultz, eds., *Barriers to European Growth*, (The Brookings Institute, 1987).
(2) Social Security Problems Throughout the World 1989, Social Security Administration
(3) Burless. The replacement rate is the ratio of UI benefits to the average wage of a production worker in manufacturing who is married to a dependent spouse and
(4) The OECD Observer, June/July 1990, p. 30.
(5) U.S. Dept. of Labor, Employment and Training Administration.

Exhibit 2

	High Cost Multiple (2)	Replacement Ratio (3)	Replacement Ratio Rank (1)	IUR/TUR (4)	IUR/TUR Rank (1)
Hawaii	1.57	44%	8	42%	9
Kansas	1.52	45%	1	39%	16
Mississippi	1.66	34%	39	28%	40
New Mexico	1.65	36%	32	26%	45
Oklahoma	1.61	39%	20	25%	47
Oregon	1.57	40%	16	40%	12
South Dakota	1.52	40%	15	21%	48

(1) Ranking includes District of Columbia
(2) Fiscal Year 1990
(3) Calendar Year 1989
(4) Ten Year Average, 1980-89
Source: U.S. Dept. of Labor,
Employment and Training Administration.

Prepared by UAW Research Department

Exhibit 3

1980 - 1989 STATE AVERAGES
(TUR / TUR)

1	Rhode Island	63%	27	Arkansas	32%
2	Alaska	53%	28	North Carolina	32%
3	Massachusetts	49%	29	Nebraska	32%
4	New Jersey	45%	30	Michigan	32%
5	Vermont	44%	31	Utah	31%
6	Pennsylvania	44%	32	South Carolina	31%
7	Maine	42%	33	Ohio	31%
8	California	42%	34	Iowa	31%
9	Hawaii	42%	35	West Virginia	31%
10	Wisconsin	41%	36	Louisiana	29%
11	Idaho	41%	37	Tennessee	29%
12	Oregon	40%	38	Colorado	28%
13	Washington	39%	39	Kentucky	28%
14	North Dakota	39%	40	Mississippi	28%
15	New York	39%	41	New Hampshire	27%
16	Kansas	39%	42	Arizona	26%
17	Connecticut	38%	43	Georgia	26%
18	D. of Columbia	38%	44	Alabama	26%
19	Minnesota	35%	45	New Mexico	26%
20	Montana	34%	46	Indiana	25%
21	Nevada	34%	47	Oklahoma	25%
22	Missouri	34%	48	South Dakota	21%
23	Illinois	33%	49	Texas	21%
24	Delaware	33%	50	Florida	19%
25	Maryland	33%	51	Virginia	18%
26	Wyoming	33%			

Note: Percentages are calculated for the entire ten year period.

Source: U.S. Department of Labor, Employment and Training Administration.

Prepared by UAW Research Dept.

ki/ana/rickl

Exhibit 4

Top States	IUR/TUR (80's Avg.)	Replacement Ratio (89)	Monetary Eligibility (In Dollars)	Monetary Eligibility As a percentage of State Avg. Ann. Wage	Durational Disqualification:		
					Refusals	Quits	Discharges
Rhode Island	63%	45%	1,600	8%	Yes	Yes	Yes
Alaska	53%	28%	1,000	3%	No	No	No
Massachusetts	49%	44%	6,210 (1)	25%	No	Yes	Yes
New Jersey	45%	38%	2,060	8%	No	No	No
Vermont (4)	44%	38%	1,400	7%	Yes	Yes	No
Pennsylvania (5)	44%	43%	1,584	7%	No	Yes	Yes
Bottom States							
Indiana	25%	26%	2,500	12%	Yes	Yes	Yes
Oklahoma	25%	39%	3,600	19%	Yes	Yes	Yes
South Dakota	21%	40%	3,480 (1) 2	23%	Yes	Yes	Yes
Texas	21%	39%	5,883 (1) 2	27%	Yes	Yes	Yes
Florida	19%	38%	7,640 (2)	38%	Yes	Yes	Yes
Virginia	18%	34%	5,600 (3)	28%	Yes	Yes	Yes

(1) \$1200 base period earnings or 30 times claimant's weekly benefit amount.
(2) State average weekly wage for calendar year 1989 multiplied by twenty.
(3) Two thousand eight hundred dollar requirement for two quarters of the base period doubled to reflect an annual amount.
(4) Must earn \$1,000 in a quarter and 40% of total must be outside highest quarter.
(5) Base period wages must exceed \$1,320 and 20% of base wages must be paid outside highest quarter.
Source: U.S. Dept. of Labor, Employment and Training Administration
Prepared by IAW Research Department

PREPARED STATEMENT OF SENATOR PAUL S. SARBANES

Chairman Bentsen, Members of the committee, thank you for this opportunity to testify on the problems of the unemployment insurance system during this recession.

We are now experiencing a much more serious recession than most people have recognized. The unemployment insurance system should play vital countercyclical and humanitarian roles in such a recession. The current UI system is doing an unsatisfactory job of providing stimulus to the economy and alleviating hardship in depressed areas. For that reason, I urge this Committee to follow the precedent of the last five recessions of this length going back to President Eisenhower and extend UI benefits in economically distressed states.

NOT A "SHALLOW" RECESSION

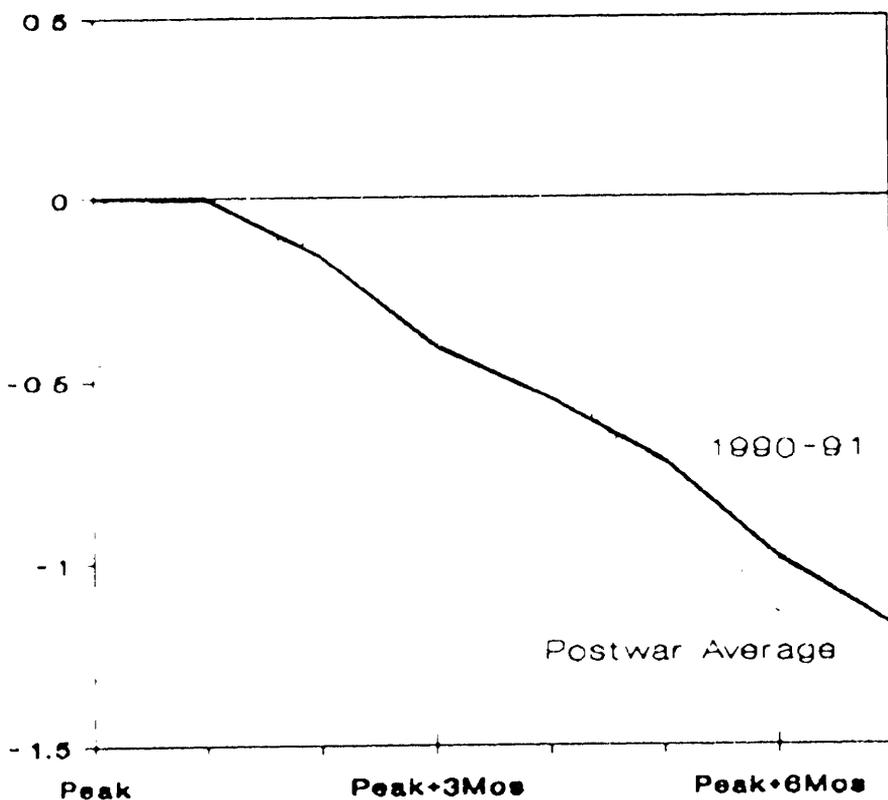
It is widely believed that the current recession represents a minor dip in economic activity—"short and shallow" is the phrase heard most often. A review of the available data indicates, however, that in many important respects this is developing into a more serious recession than is generally perceived. Dating the end of the last business cycle expansion as August of last year, we have seven months of recession data to examine. In terms of lost jobs, output, and income, this recession has been right on track with the average of the initial seven months of post-war recessions:

- Over the last seven months, businesses have reported a decline of 1.2 percent in payroll employment, exactly the same decline as occurred during the first seven months of the average postwar recession. (See Figure 1). In the last seven months, 1.3 million payroll jobs have been lost, compared to 1.2 million lost in the first seven months of the deep 1981-1982 recession.

Figure 1

Private Nonfarm Employment

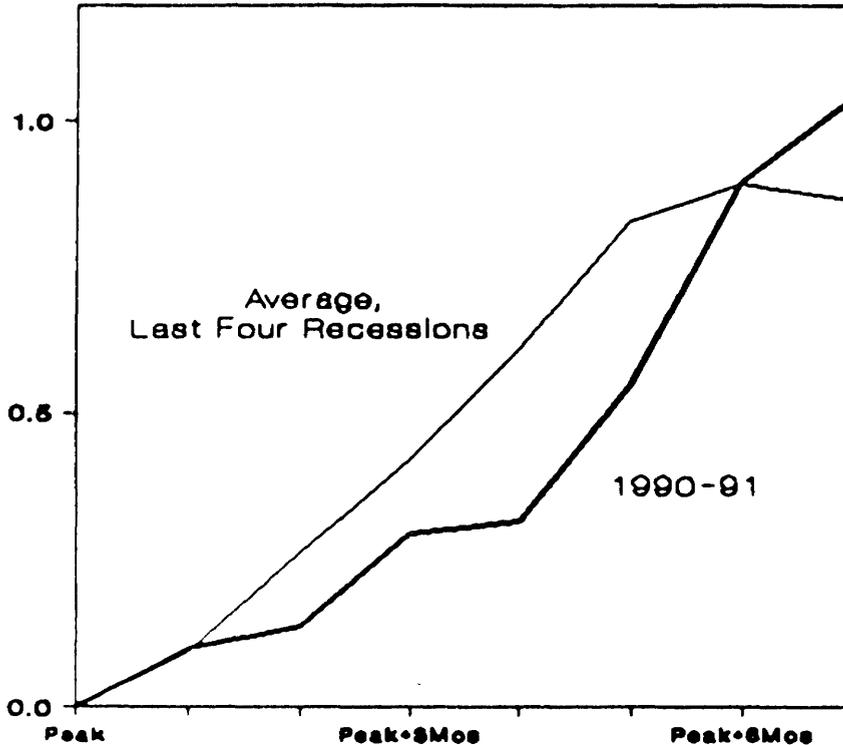
Percent Change from Peak



• Likewise, this recession has also been every bit as serious as those of the past in terms of the number of workers laid off from their jobs. The fraction of the labor force who have lost their jobs and are still looking for work has risen from 2.8 percent in August to 3.8 percent today, a one percentage point increase, to an increase of 0.9 percentage points in the average of the last four recessions. (See Figure 2).

Figure 2

**Job Losers as a Percent of Labor Force
Change from Peak, Percentage Points**



The two most widely watched indicators of the recession are giving more rose-colored impressions of this downturn. The unemployment rate has risen by 1.2 percentage points (from 5.6 percent to 6.8 percent) since August, while the average rise in unemployment in the first 7 months of a recession has been 1.5 percentage points. Similarly, the official GNP on a 1982 basis has so far registered only a 1.6 percent rate of decline for one quarter. Those two indicators are misleading for different reasons:

- The change in the unemployment rate is a misleading guide to the severity of the recession because it reflects growth in the labor force as well as job losses. The labor force has grown slowly in recent years. As a result, the ranks of the unemployed are not being swelled so much by new entrants as in previous recessions. If the labor force had grown as fast over the last year as it did in previous recessions, today's unemployment rate would stand at 7.6 percent instead of today's 6.8 percent.
- GNP figures also understate the severity of the current recession. Unfortunately for understanding this recession, the official measure of real output continues to be based on outdated 1982 prices and spending which understate the severity of the current recession. The Department of Commerce is in the process of converting all its detailed measures of real GNP to the more appropriate price and spending patterns of 1987. However, they are already publishing overall GNP data using the more current 1987 basis. These show real GNP falling at a 3.5 percent annual rate

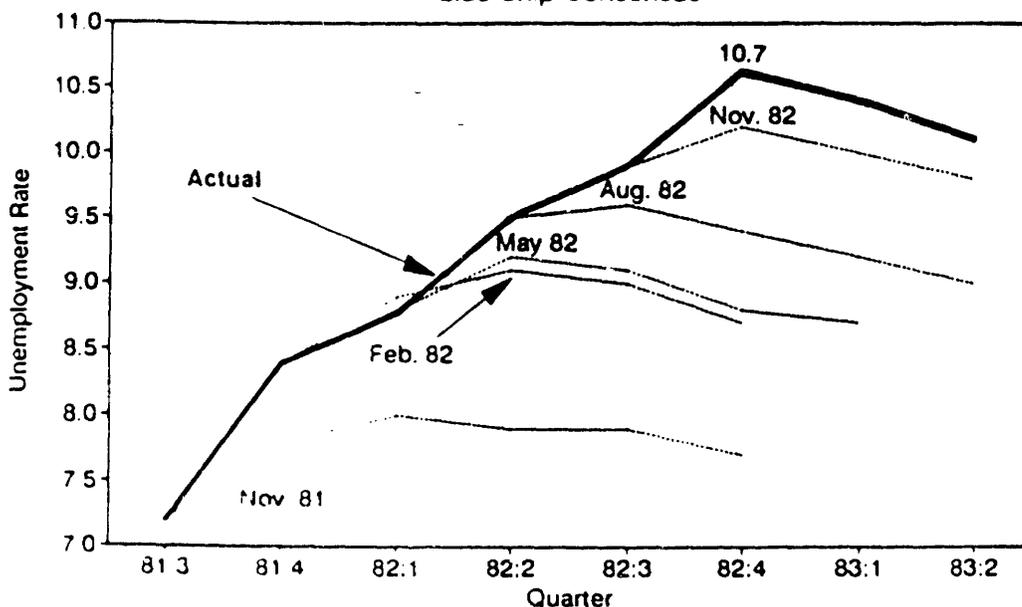
in the fourth quarter of 1990 instead of the 1.6 percent decline indicated by the outdated 1982 basis.

NO ASSURANCE OF AN IMMEDIATE TURNAROUND

Although the consensus among forecasters calls for the recession to end soon, history provides some grounds for questioning the prescience of this consensus. Economic models, by their very nature, tend to miss sharp turns in the economy, and to impose a "short and shallow" bias on recession predictions. This tendency to forecast a smoother path for the economy than actually occurs is especially pronounced for the *consensus* of forecasting models.

This bias can be seen clearly from the "consensus" forecasts surrounding the deep 1981-82 recession. The solid line in Figure 3 traces the actual unemployment rate from a quarterly average of 7.2 percent when the recession began in July 1981, to an average of 10.7 percent by the recession's end in the fourth quarter of 1982. Yet, at virtually every point during the long climb of the unemployment rate, the "consensus" forecast was for imminent improvement.

Figure 3
Projected vs. Actual Unemployment Rates
Blue Chip Consensus



Source: *Blue Chip Economic Indicators*.

The dotted lines in Figure 3 show the path for the unemployment rate that was predicted at various points during the recession by the "consensus" of 50 economic forecasters surveyed by the Blue Chip Economic Indicators organization. As with the current recession, the initial consensus for the 1981-82 recession (represented by the bottom line marked "November 1981") called for the unemployment rate to rise modestly for another quarter and to decline thereafter. By May 1982, the consensus was concluding that the unemployment rate had already peaked at 9.2 percent. In fact, the quarterly average unemployment rate rose by another 1.5 percent over the next six months. (On a monthly basis, the unemployment rate peaked at 10.8 percent during that quarter.)

Available data on employment, production, and housing through March suggest a further sizable decline will be registered when the preliminary report on first quarter GNP is issued on Friday. Employment declined at an annual rate of 2.3 percent in the first quarter of 1991 compared to a 1.6 percent rate in the previous quarter. Industrial production fell at a 9.3 percent annual rate in the first quarter, after falling at a 7.0 percent rate in the fourth. First-quarter housing starts dropped 12.3 per-

cent below their fourth-quarter level, which was down 7.8 percent from the third quarter.

This review suggests that it is clearly possible for the recession to linger for some time yet. Congress needs to move expeditiously to deal with the human consequences of this recession. One particularly timely response to the recession concerns the reforms to the unemployment compensation system which your committee is considering in today's hearing.

EXTENDED UI AS ANTI-RECESSION STABILIZATION TOOL

As a quick targeted program of income replacement for jobless workers, the UI system is ideally suited to counteract the effects of recession. Funds are spent immediately without the lags of bureaucratic or political decision-making typical of other countercyclical spending. Moreover, the funds are automatically spent in the locations of greatest distress. According to Administration projections, during this fiscal year 10.7 million jobless workers will receive \$24.3 billion in benefits compared to 7.0 million receiving \$13.5 billion in FY89.

The UI system is not performing its stabilization role as well during this recession as it has done in the past. From the perspective of workers who have lost their jobs and remain unemployed, the UI system is replacing the income lost during this recession only a half to two thirds as well as in past recessions. As shown in Figure 4, the income replacement ratio anticipated for this recession is much lower than in the last four recessions. The regular 26 weeks of benefits are projected, on the basis of the Administration's Budget numbers, to replace 10 percent less of unemployed job losers' missing paychecks than in 1981-82 (the difference from some earlier recessions is even larger). The bulk of the difference shown in Figure 4 comes from the absence of extended benefits for rising number of long-term unemployed.

If the current recession lasts longer than the Administration forecasts, this replacement ratio will *decline* further, because more workers will exhaust their UI benefits. Longer-term benefits are now projected to make up only 4 percent of the cyclical rise in UI payments in 1990-91—far smaller than in past recessions as shown by the shaded portions of the figure. This decline is the result of changed trigger levels in the existing "extended benefits" program, along with the absence of the "supplemental benefits" program that had helped support incomes in the last recession.

EXTENDED UI AS SOCIAL INSURANCE IN A RECESSION

The number of workers who are unemployed longer than six months and exhaust their UI benefits rises sharply during a recession and continues to rise for several months after it ends. During the first seven months of this recession, 1.5 million have exhausted their unemployment benefits, an 28 percent rise over the same seven months of the prior year. According to Administration projections, 3.3 million workers will exhaust regular UI benefits in FY92, an increase of 1.4 million exhaustees over FY89.

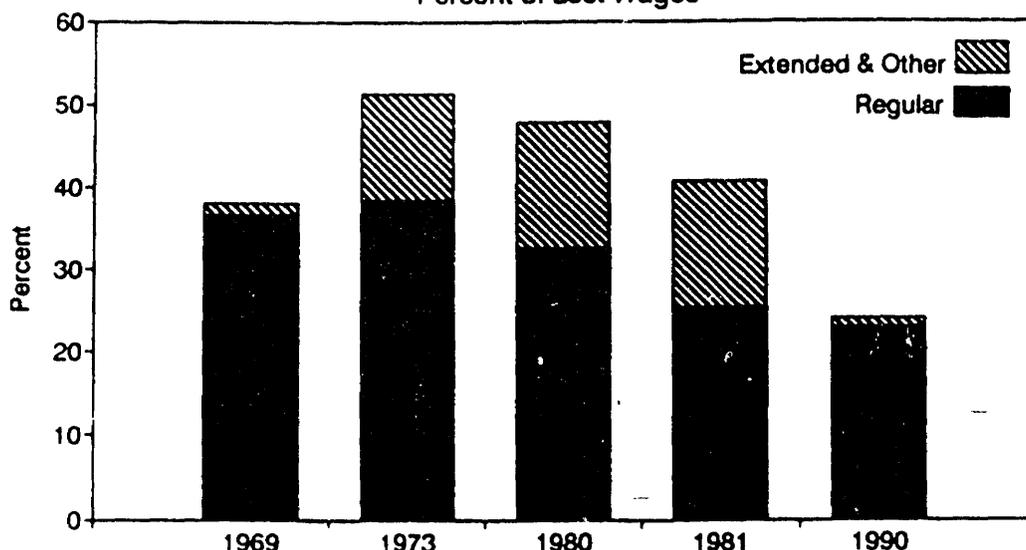
For workers threatened with job loss, the UI system provides "insurance" in the form of income support for a reasonable period to find a new job. In normal times, virtually all states set a maximum income-support period of 26 weeks. However, during a recession (regional or national), the chances of finding a job within 26 weeks are greatly reduced. To provide equivalent "insurance," the reasonable period of time to find a job should be extended. Over the last 25 years, the Congress and President have recognized this during each of the five recessions that lasted longer than six months. We have enacted temporary provisions to lengthen the period for receiving UI benefits, especially for states in the most depressed conditions.

In addition, permanent U.S. law has provided for "Extended Benefits" (EB) up to an additional 13 weeks during particularly adverse conditions. The formulas used to initiate EB payments have become increasingly outdated. A witness before the JEC recently estimated that unemployment would have to reach 15 percent for the EB trigger to be reached in some states.

Since enactment of the EB program in 1970, the level of total unemployment required to trigger Extended Benefits has effectively been raised by roughly forty percent. Half of that increase came as a result of the 1981 legislative changes. State responses to the budget pressures of the deep 1982 recession account for much of the rest.

Until the late 1970s, the number of UI recipients closely tracked the number of "job losers," i.e. unemployed who had involuntarily lost their last job. The deep recession of the early 1980's left many states with UI trust funds in substantial debt to the Federal government. To repay these debts, many states not only raised UI

Figure 4
Replacement of Lost Income in Recession
 Rise in Unemployment Insurance Benefits as a
 Percent of Lost Wages



Sources: Department of Labor and Joint Economic Committee.

Note: Lost wages are the peak to trough change in wages that would have been earned by job losers

taxes but also tightened eligibility requirements. In recent years, the number of UI recipients has fallen to four fifths of the number of "job losers." (Figure 5).

Since EB is triggered by a state's insured unemployment rate ("IUR": the number of UI recipients relative to the number of employed and covered by UI), the declining coverage noted in the previous paragraphs has the effect of raising the EB trigger by one fourth. However, the effects are very uneven. While some states would require total unemployment rates as high as fifteen percent to trigger EB, a few states with much lower unemployment rates have triggered EB in recent months. After the sharp decline in oil prices in 1986, unemployment rose above 9 percent in major oil producing states. The current formula caused Extended Benefits to trigger off for Louisiana while the state's unemployment rate remained above ten percent and never to trigger on for Oklahoma or Texas.

Thus, to maintain an appropriate level of "insurance" for unemployed workers, we should extend unemployment insurance in depressed states. To do this fairly and effectively, the trigger for longer term UI benefits in a recession should be recalibrated. Given the wide divergence among states in eligibility requirements, and therefore their IUR rates, the recalibrated trigger should not hinge on the IUR. Another measure, such as the total unemployment rate, would better reflect the chances of finding a job within 26 weeks and not the stringency of a state's eligibility criteria.

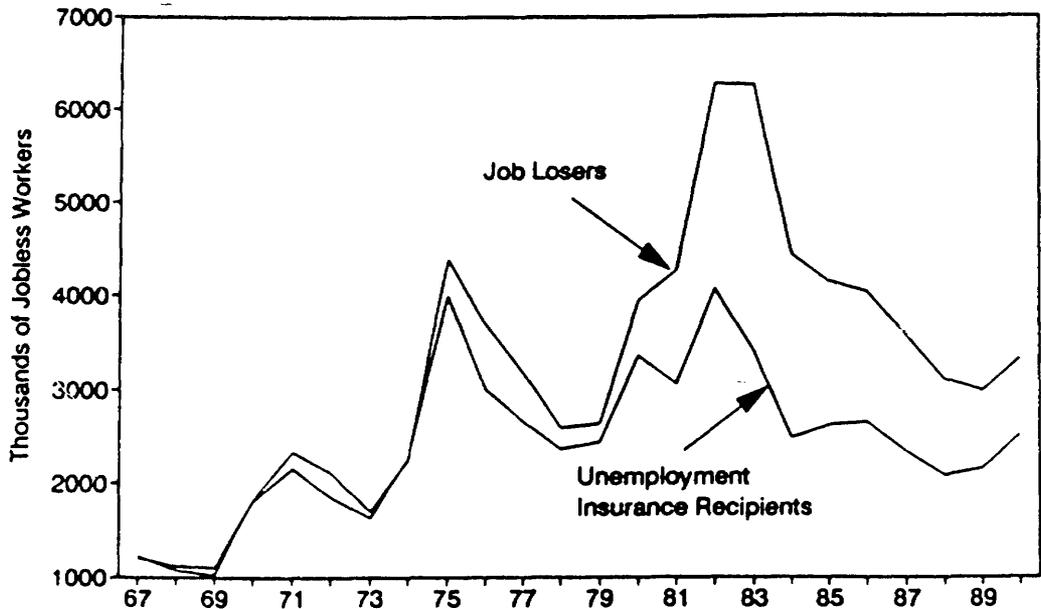
CONTRACTIONARY FISCAL EFFECT OF EXTENDED BENEFIT TRUST FUND

The failure of the UI system to act as an effective countercyclical tool can also be seen in the budget numbers for the Extended Benefits trust fund. According to the Office of Management and Budget, this fund began FY91 with \$7.2 billion and will receive another \$700 million dollars in taxes and \$600 million in accrued interest during FY91. During this recession year, the fund will pay out only \$140 million for benefits—one fifth of the taxes taken in.

Thus the EB trust funds will actually build up surpluses at a time when they should be drawing down past surpluses to fund adequate income replacement for laid off workers.

Figure 5

Job Losers and Unemployment Insurance Recipients 1967 to 1989



Source: Congressional Budget Office.

An analogy to the Social Security trust fund is revealing. While we may debate how much of a surplus to run during the prime earning years of the Baby Boom generation, no one argues that we should continue to build up the trust fund during the retirement years of the Baby Boom. Yet the EB trust fund was intended to spend down during recessions but is in fact expanding by one seventh in this recession year.

ADMINISTRATIVE FUNDING

The shift from a deficit cap to spending caps in the budget process was intended to permit cyclically sensitive programs to respond to the business cycle. Debate over deficit-cutting was to focus on structural aspects of the budget. Yet, no provision was made to provide UI administration funding for cyclical increases in the workload.

We should make the system for providing UI administrative funds more flexible to respond to recessions. It makes no sense to have a program where benefits and claims expand automatically with a deteriorating labor market, but the administrative funds needed to process those claims remain frozen, subject to sporadic supplemental appropriations. This is a complex issue that not only raises jurisdictional issues between this Committee and the Appropriations Committee but also questions of budget scorekeeping. Yet I am confident that a satisfactory compromise on the jurisdictional and scorekeeping issues can be reached so that we do not repeat this year's crisis in the future.

CONCLUSION

We have been experiencing a serious recession in terms of the number of workers who have lost their job and are still looking to find a new job. Over the last seven months, employment has fallen as fast as the average rate for the first seven months of post war recessions.

Just as it has done for all five recessions of this length over the last quarter century, Congress and the President should act to extend UI benefits in states hit by the recession. Such legislation would both stimulate the economy and relieve some of the hardship for the soaring number of workers who have lost their jobs.

PREPARED STATEMENT OF JOHN G. THODIS

Mr. Chairman and members of the committee, I am John G. Thodis, President and chief Executive Officer, Michigan Manufacturers Association. I am testifying today on behalf of the National Association of Manufacturers.

Thank you for the opportunity to present NAM's views on the current state of the Unemployment compensation (UC) program. We commend the chairman and members of the committee for holding today's hearing on this important issue.

NATURE OF CURRENT RECESSION

The importance of the unemployment compensation program is directly related to the current economic conditions, therefore, I would like to start first by giving our views as to the extent and nature of the current recession. According to our estimates, the recession that began last summer will last through the second quarter of 1991. Declining inflation rates will set the stage for the recovery. The inventory liquidation cycle characteristic of most postwar recessions will not be in evidence since inventories are now being kept tight relative to sales. consumption spending will account for a larger share of the downturn, due to losses in purchasing power implied by higher inflation, increasing personal indebtedness, and the decline in housing prices.

With respect to the magnitude of the downturn in the economy, the peak unemployment rate, likely to occur in June, should be in the area of 7.0 percent, or slightly less. This is somewhat less than the postwar average, where the peak rate of unemployment was 7.4 percent. comparisons of unemployment rates are difficult, of course, inasmuch as this figure is influenced by the starting value. Another way of evaluating the impact on labor markets is the change in civilian employment. Here the postwar average has been -1.2 percent. For the current recession, we anticipate a -1.1 percent decline.

While the recession promises to be relatively mild, the recovery will be unusually slow by comparison with prior business cycles. This time, the rise in consumption that has typically driven postwar recoveries will be considerably weaker than usual, as consumers continue to adjust to weak growth in real incomes, excessive debt, and declining home values. Instead, the role of exports will be proportionally larger. This is a reversal of the normal pattern in which domestic demand drives the economy in the initial stages of an expansion, and exports only take over in the final years; this time industry is more likely to undergo a phase of export-led growth early on.

On this basis we anticipate that the unemployment rate will fall gradually, to 6.5 percent by the end of the year (essentially, its current level) and 6.0 percent or less by the end of 1992, assuming a GNP growth rate of 2.6 percent that year. The total rise in civilian employment during the 18-month period (July 1991-December 1992) is likely to be 1.7 percent.

Regarding the recession, businesses generally are optimistic. Two-thirds of the 90 manufacturing companies surveyed February 9 at NAM's semiannual board of directors meeting agreed that the recession will be shallow. As for the recovery, well over half predicted "steady, but unspectacular growth." confidence in recovery is important, leading employers to invest, rehire and create new jobs.

STATUS OF THE U.S. UNEMPLOYMENT COMPENSATION PROGRAM

From time to time the dynamic nature of our industrial economy may bring with it temporary and involuntary unemployment. Unemployment is an intrinsic characteristic of our economic system. Recessions come and go at periodic intervals. Some are prolonged, others are relatively brief. Congress has always been sensitive to the hardship resulting from troughs in the business cycle. In 1958 and again in 1961, Congress enacted temporary programs to extend the duration of unemployment benefits as a partial response. Then in 1970 Congress enacted a permanent program to automatically extend UC benefits when unemployment exceeded specified thresholds. The Extended Benefits (EB) program was marketed as an automatic response that would activate and deactivate as appropriate, obviating the need for congressional action. It was a prudent thing to do; but, prudence and politics do not always

enjoy a contented conjugal relationship. Over the years Congress has desired to make several temporary extensions beyond the permanent program. Over this same period the unemployment threshold levels (the levels at which UC benefits are extended) were frequently lowered, or waived, to increase the availability of benefits.

Temporary benefit extensions beyond the permanent EB program enacted twenty years ago to mitigate the hardships of temporary unemployment, are costly, and often untimely and unnecessary. They tend to prolong spells of unemployment and they are rarely delivered to those most needy and deserving. The greatest danger, however, is that availability of benefits will be expanded by modifying the permanent EB program. The extended benefits program is not broken and certainly does not need reconstructive surgery, as some have suggested.

Since 1935, this nation has utilized the federal-state system of unemployment compensation to provide benefits to the unemployed and to encourage steady employment, which is vital to our free enterprise economy.

The National Association of Manufacturers believes that adherence to the following principles is essential if a state-administered unemployment compensation system is to work successfully in our free economy.

(1) The intent of the unemployment compensation program should be to serve the public interest and not special interest groups. Any extension of the program resulting in a maldistribution of costs or administrative problems should be discouraged.

(2) To meet the varying economic and social conditions throughout the country, the responsibility for administration of sound unemployment compensation systems should remain with the state governments, since they are better equipped to evaluate their individual state's needs.

(3) Federal legislative and administrative action should not infringe upon the rights and abilities of states to autonomously administer their systems. Further, Federal responsibilities should be limited to assuring that states establish and operate a state unemployment compensation program, and to the financing of costs directly related to the administration of such a program. These responsibilities should not include the establishment of any binding standards which preempt the states' formulation and administration of their respective unemployment compensation programs.

(4) State-administered unemployment compensation benefit payments should be directly related to earnings and service resulting from previous employment and should constitute a partial indemnity for loss of wages as determined by each state. Payments should not be so high as to weaken the incentive to return to the work force.

For the past two or three years, the UC program has been criticized for its declining coverage rates resulting in less than one third of the unemployed workers actually obtaining coverage. The obvious conclusion to this claim is that the program is inadequate and unresponsive to the vast majority of unemployed workers. The use of the word "coverage" inaccurately portrays the nature of the gap. In the traditional vocabulary of the unemployment compensation system, the word "coverage" has an established meaning. "Covered employers" are those who pay unemployment taxes on the wages of their employees. "Covered wages" are the payrolls upon which those taxes are paid. "Covered workers" are those employees who earn wages subject to the unemployment tax. "Coverage" in the lexicon of the program has nothing to do with whether a worker files a claim for benefits—nothing to do with whether a covered worker is eligible for benefits—nothing to do with the disqualification from receipt of benefits. There has, in fact, been *no decline* in the *coverage* of the system. Over 98 percent of all wage and salaried workers are covered.

There has always been a gap between the total unemployment count and the number of unemployed actually drawing UC benefits. There are legitimate reasons for the gap. Some of the unemployed are new entrants to the workforce and have no covered wages; others have scant work history with insufficient covered wages; others are reentrants to the labor market having no recent wages; others were disqualified from benefits because they voluntarily left their job without good cause, or were guilty of misconduct connected with their work, or they refused an offer of a suitable job; others have exhausted all of their benefit entitlement.

Studies have shown that over two-thirds of the unemployed did not apply for benefits, a point missed by many program critics. Of those who do apply for benefits, between 52 percent and 93 percent receive benefits. These figures simply compare the number who applied for benefits and the number of individuals who received benefits on a state-by-state basis. This simple comparison based on Department of Labor information seems to indicate that benefits are being paid at higher rates than the proponents of expanding the system would like you to believe.

Some studies have attributed the gap to the tightening of eligibility and/or disqualification provision by the states and more restrictive provisions imposed by Congress upon the extended benefits program. Other significant factors that seem to contribute to the gap include:

- Almost two-thirds of the unemployed surveyed did not apply for benefits.
- 83 percent of the unemployed surveyed either quit their last job (32%) or did not work long enough to qualify (52%).
- Application for benefits increased with unemployment duration. The rate of application among those unemployed 27 or more weeks was three times as high as those unemployed only 1 or 2 weeks.
- About one-fourth of the unemployed had no recent work experience, and more than half of the unemployed were part-time workers before losing their jobs.

NAM believes that benefit payments made under the program should be paid only to individuals who become temporarily unemployed through no fault of their own, who are genuinely part of the work force, who are sincerely and actively seeking employment, who do not refuse suitable employment when offered, and who are not unemployed as a result of a labor dispute. Benefit eligibility should be reestablished only by proof of reentering the work force and working at a job for a reasonable time.

Benefit payments must be limited strictly to compensation for periods of temporary involuntary job-connected unemployment. Unemployment of longer duration is outside the proper scope of a program to be financed by a payroll tax system. Determination of what may be considered "temporary unemployment" periods should be within the discretion of the individual states.

NAM opposes the addition of any Federal supplemental benefit programs to the unemployment compensation system. Unemployment of durations longer than those "temporary unemployment" periods, as determined by the individual states, is symptomatic of far greater, more deeply ingrained economic problems than those which employers can reasonably be held responsible. However, NAM does recognize that in times of economic recessions, there may be a need for extending the duration of unemployment benefits in those states that have determined that the period of "temporary unemployment" is of such duration to necessitate "triggering" of the federal-state (EB) program.

The program should be soundly financed using experience-rating as the basis for any unemployment compensation tax policy. The purposes of sound experience rating are to distribute costs, provide incentives for employers to stabilize employment and generate the necessary active interest of employers in the program.

The tax rate structure in any state program should feature provisions insuring sufficient contributions to maintain adequate balances in the trust funds to meet current and reasonably foreseeable future benefit payment liabilities. The program should also provide for adequate contributions to the trust funds during times of high employment so as to minimize the increase in tax rates during periods of recession. However, restrictions should be imposed to insure against excessive accumulation of revenues.

While it is the responsibility of each state to finance its own system on a sound basis, temporary emergencies do arise. When it becomes necessary for a state to borrow from the Federal Unemployment Account (State Loan Fund), specific provisions should be made for repayment, review and approval of such loans under definite terms which would encourage the state to place its own system on a sound financial basis as soon as it is possible, within the limits of the economic climate.

Unemployment compensation programs should encourage maximum employer interest and participation. Efficient administration requires the responsible administrative agency to provide adequate current information to employers. Efficient administration can be accomplished only by effective employer cooperation in providing information necessary for the proper determination and adjudication of claims.

Efficient administration also means the timely administration of claims and payment of benefits. Unfortunately the evidence suggests that eligible unemployed workers have had to wait in line hours to file their claim and weeks to receive their first benefit check. This is inexcusable when employers have met their obligation in paying their Federal UI taxes. Currently over \$2 billion dollars are available for program administration. But because of budgetary slight of hand, the states are inadequately funded. This causes problems, not only for claimants, but in some states has led to additional state taxes on employers to fund program administration. This is double taxation.

Program administration is one area where NAM, organized labor, and state agencies agree. Sufficient funds need to be appropriated for proper and efficient claims administration.

Regarding the use of Federal Unemployment Tax Act (FUTA) receipts, NAM believes receipts should be used for the following purposes:

- To finance Federal and state administrative costs directly related to benefit payments and determination of employers' tax liability;
 - To finance those functions of the employment service system which are essential to a state's UC program; and
 - To provide a loan fund for states that temporarily exhaust their trust funds.
- However, realistic and enforceable repayment provisions should be provided.

There should be no allocation of FUTA receipts for the purpose of providing special benefits to a specific industry which is adversely affected by economic conditions relative only to that industry. There should be no excessive accumulation of FUTA revenues. If additional FUTA funds are needed, they should be obtained by adjusting the tax rate.

CONCLUSION

In conclusion, the National Association of Manufacturers supports the following: experience rating as a means of assessing the UI tax employers pay; receipt of benefits being determined by an individual's attachment to the labor force and earnings; the temporary nature of the unemployment compensation program; and the current Federal/State balance, enabling states to be responsive to local economic and work-force conditions. NAM believes that, if Congress appropriates adequate administrative funds, the Unemployment Compensation program is currently providing the benefits to the very individuals that the program is intended to serve. The program is not in need of reform, as some have suggested.

PREPARED STATEMENT OF ROBERT H. TOPEL

Thank you for inviting me to testify.

The stated purpose of the Unemployment Insurance system in the United States is to reduce the costs of unemployment by providing a steady source of income and consumption for the unemployed. In this sense, the UI system is meant to be a form of "insurance" in the truest sense: premiums are collected through payroll taxes, and these premiums finance the payment of benefits to persons who experience a "loss" because of unemployment. In practice, however, the existing UI system performs poorly as a system of insurance for workers. Moreover, that performance has deteriorated through time because of important recent changes in the labor market.

My purpose in this testimony is to suggest two important reforms that will improve UI as a system of insurance. These reforms would not increase the costs of UI programs or the tax burden on employers and workers. In fact, they may reduce aggregate UI costs. The reforms I suggest will also reduce some of the adverse incentives of UI that have actually contributed to the unemployment problem in the U.S.

The study of unemployment and of the Unemployment Insurance (UI) system has been a major component of my research agenda for the past 10 years. During that time I have studied the evolution of unemployment in the United States, the incentives created by our current UI system, and methods of financing UI benefits in state and Federal programs. Based on my research and that of others, I believe that the changing nature of unemployment in the United States places new demands on the UI system as a program of insurance for workers. I begin by summarizing some recent trends in unemployment in the U.S., after which I will discuss the implications of these changes for the UI system.

I. BACKGROUND: THE CHANGING NATURE OF UNEMPLOYMENT IN THE U.S.¹

During the recession of 1971, the unemployment rate of prime-aged men peaked at about 4 percent. In contrast, after the longest decline in unemployment in the

¹ Comments in this section are based on K. M. Murphy and R. H. Topel, "The Evolution of Unemployment in the United States: 1968-1985" *The NBER Macroeconomics Annual*, vol. 2, 1987, pp. 7-58; and C. Juhn, K. M. Murphy, and R. H. Topel, "Unemployment, Non-Employment, and Wages: Why Has the Natural Rate Increased through Time?" *Brookings Papers on Economic Activity* (forthcoming, 1991).

post-war period, the unemployment rate in the late 1980s settled at about 5 percent. This trend toward rising overall unemployment is just one aspect of the changing nature of joblessness in the U.S. There are (at least) four major developments that underlie this trend.

1. *Increasing Non-Employment:* From the late 1960s to the late 1980s, the average amount of non-working time of prime-aged men increased by about 2.7 weeks, or 84 percent. About two-thirds of this increase is due to rising unemployment, and the rest is due to a decline in labor force participation. Thus rising unemployment has been accompanied by an increased propensity of potential workers to withdraw from the labor force.

2. *The Importance of Long Unemployment Spells:* Most of the secular increase in unemployment is accounted for by an increase in the number of very long jobless spells. For example, during the late 1960s persons with more than 6 months of unemployment during a year accounted for about a quarter of all unemployment. That percentage has increased steadily through time, so that today these long term unemployed account for about half of all unemployment. The number of very short unemployment spells has remained fairly constant through time. Following the recession of 1982-83, flows into unemployment declined to levels reminiscent of earlier, non-recessionary, periods. But rates of job-finding among the unemployed remained unusually low, so unemployment durations remained high. It is worth noting here that weeks of unemployment beyond 6 months are not typically covered by the UI system.

3. *Concentration of Unemployment among the Less-skilled:* Less skilled people are more likely to suffer unemployment. This has always been true. Accompanying the well-known trend toward greater inequality in wages and earnings over the last 20 years, the trend toward rising unemployment has also fallen disproportionately on less skilled workers. Unemployment rates among workers in the bottom quarter of the wage distribution roughly tripled between the late 1960s and the late 1980s. These workers have more frequent spells, and they are more likely to withdraw from the labor force.

4. *The Costs of Unemployment:* For many persons the long-term costs of an unemployment spell are quite small. These are typically young workers, those who did not hold their previous jobs for a long period, or workers from certain industries such as construction and retail trade, where high turnover and unemployment are common. These persons find new jobs fairly quickly, and they do not suffer important wage reductions upon reemployment. But for older individuals who held the same job for many years, the costs of displacement can be large. Their unemployment spells are very long, they suffer large wage reductions upon re-employment, and many older persons simply leave the labor force after displacement. They do not fully "bounce back" from their earnings losses, even after several years. On average, recent research implies that workers displaced from long-term employment relationships experience a 30 percent reduction in earning capacity.²

Against these facts about overall unemployment and its cost, the percentage of total unemployment that is compensated by the UI system declined during the 1980s.³ There are several possible reasons for this, including shifts in the geographic and industrial mix of employment, changes in administrative procedures by state systems, and changes in the propensity of unemployed persons to apply for UI. On the surface, this decline in "coverage" suggests that UI is playing a smaller role in providing insurance to workers, while at the same time the costs of unemployment to job losers have risen. This would be a particular concern if a large portion of the decline is accounted for by the increased importance of long spells, outlined in point (2). There is no empirical evidence on this issue.

II. TWO REFORMS

The changes in unemployment outlined above have presented new challenges to the UI system, and new strains on its resources. Even if qualifying criteria had remained the same as they were in the 1970s, the increased importance of long unemployment spells would reduce UI coverage, since durations greater than 26 weeks

² See R.H. Topel, "Specific Capital and Unemployment: Measuring the Costs and Consequences of Worker Displacement," *Carnegie-Rochester Series on Public Policy*, 1990; W. Carrington, "Specific Human Capital and Worker Displacement," Ph.D. Dissertation, University of Chicago, 1990.

³ For studies of the decline in UI coverage, see G. Burtless, "Why Is Insured Unemployment So Low?" *Brookings Papers on Economic Activity*, 1983, pp. 225-249; and W. Vroman, "The Decline in Unemployment Insurance Claims Activity in the 1980s," Unpublished, December 1990.

are not typically covered by UI programs except in special periods of extended benefits. These long spells are most likely for prime-aged workers who had been stably employed in the past, and who suffer large reductions in earning capacity following a job loss. For them, unemployment insurance replaces only a small portion of their lost wealth, and the most costly weeks of unemployment (those beyond 26 weeks) are not insured at all.

Political and budgetary realities being what they are, proposals that would increase total spending on unemployment insurance will face strong opposition. That is not necessarily bad. In light of these constraints, I propose two important (and feasible) reforms of the UI system that would improve its performance as a program of insurance, and that would not significantly increase program costs. In fact, taken alone, these reforms would probably *reduce* program costs, which means a lower UI tax burden on employers and workers.

A. Waiting Periods and the Extension of UI Coverage

My first proposal deals with the *timing* of UI benefits during a spell. In language familiar to buyers of insurance, I would increase the deductible (waiting periods) in order to achieve increased coverage (longer benefit durations).⁴ The outcome is better insurance.

A typical state UI system requires a one-week waiting period before benefits payments begin, after which coverage continues for up to 26 weeks. In starkest terms, this means that a construction worker who is laid off for one month each winter will always receive UI, even though his spells are always short and largely anticipated. In contrast, factory workers who are displaced from long-term employment by a plant closing will typically suffer larger losses, composed of more unemployment and a greater wage reduction. For these people, UI coverage will stop after six months. This arrangement can hardly be called "insurance."

If UI is to act as a system of insurance, the resources of the system should be spent where they will do the most good. As it stands, workers who experience only short unemployment spells receive UI benefits. Yet even without UI coverage, the effect of a short unemployment spell on a worker's wealth and consumption will usually be small. Most workers who experience brief periods of unemployment have assets, family connections, and sources of credit that allow them to maintain their consumption patterns during periods of transitorily low income. Recent research confirms this view: for the typical person, temporary reductions in income are "self-insured," so that consumption patterns are maintained. Long-term reductions in earning capacity, say due to illness or substantial period of unemployment, have larger effects on consumption spending because families draw down their assets as a spell progresses.⁵ These long spells substantially reduce an individual's wealth.

The implications for UI are clear. When workers can self-insure against temporary losses of earnings, a dollar in UI benefits will be more valuable to a person experiencing a long unemployment spell than to a person experiencing a short one. Putting UI funds where they provide the most value, this means that UI programs should include a substantial waiting period that plays the role of a "deductible" in a standard insurance policy. Weeks of unemployment that fall within the range of the deductible should be "self-insured," while more serious events should be covered by the UI system. All state systems (at Federal urging) contain a one week waiting period. I think that one week is too short. Specifically, I believe that waiting periods should be substantially lengthened, and that the savings should be used to provide greater insurance coverage to the long term unemployed, who need it the most.

Some simple calculations show what can be accomplished by this type of reform. Suppose that UI coverage were extended to a full year for *all* qualified workers, which adds 6 months of new coverage, at current benefit levels, to the typical program. Using data on job finding rates for the long term unemployed, I calculate that in a typical year this would add about 14 weeks of actual benefit payments for workers who now exhaust benefits at 26 weeks.⁶ Since less than a quarter of all new spells of insured unemployment actually last 6 months, these benefits could be fully financed by increasing the waiting period for UI to one month. *Thus we can "buy" 6 months of additional coverage, in months where benefits are most valuable, by sacri-*

⁴ A formal treatment of these issues appears in S. Shavell and L. Weiss, "The Optimal Payment of Unemployment Insurance over Time," *Journal of Political Economy*, December 1979.

⁵ P. Burgess, J. Kingston, and C. Walters, "The Adequacy of UI Benefits," U.S. Department of Labor, 1979; J. Cochrane, "A Simple Test of Consumption Insurance," University of Chicago, August 1990.

⁶ Data on insured spell durations are published in B. Meyer, "Unemployment Insurance and Unemployment Spells," *Quarterly Journal of Economics*, July 1990.

ficings one month of coverage in months where benefits are least valuable. This is a trade worth making. Most workers subject to unemployment would be better off, and there would be no new UI tax liabilities.

My conclusion that this reform would be wholly self-financing rests on the assumption that the number of spells of various durations would remain roughly what it is under the current system. That may not be true. The extension of benefits will cause some persons with long spells of unemployment to remain unemployed even longer. That will increase costs somewhat, but the effect is likely to be small. A more important impact will be a reduction in the number of short unemployment spells. Since benefits will not be available for spells lasting less than a month, the current incentive for employers and workers to abuse the UI system with temporary layoffs will be greatly reduced. In fact, more than 40 percent of all insured unemployment spells are temporary layoffs that end in recall by the previous employer.⁷ Among the short spells for which my proposal would reduce coverage, the proportion is substantially more than half. Since many of these spells are at the discretion of employers, and since my proposal would reduce benefits paid to workers on temporary layoff, I expect that these changes in incentives would actually reduce the total number of unemployment spells. That means lower total benefit payments and lower UI taxes.

There are many refinements that might go with this proposal. I will mention just one. Since the purpose is to target increased UI coverage to those who have the largest losses, extended coverage might be made contingent on the duration of the previous job and other long-term indicators of a person's labor force participation. Rather than an earnings test that is contingent on just one year's experience, as in current laws, extended duration (and perhaps benefit levels as well) should be contingent on previous employment and earnings, since these are indicators of the magnitude of losses.

Finally, a larger percentage of total weeks of unemployment will be covered by UI under this proposal. This means a slight reversal of the trend toward less UI coverage.

I'm a professor, but I'm not completely naive. While I think it is obvious that this proposal would make UI a more effective program of insurance against serious earnings losses, I also recognize that not everyone will gain from this reform. There are winners and losers. The winners are the long term unemployed, especially those displaced from long term jobs whose skills are not easily transferable to other activities. They get more insurance. The losers come from industries and occupations that experience lots of temporary layoffs, so they benefit greatly from a UI subsidy under the current system. They will get less of a subsidy under my proposal, and so they will tell you that it is a terrible idea. Don't listen to them.

B. Improved Experience Rating and UI Financing

In contrast to other countries' systems, UI benefits in the U.S. are financed by payroll taxes that are to some degree "experience rated." This means that the tax rate levied on an individual employer depends in whole or in part on that employer's history of generating insured unemployment. A reading of the original UI debates from the 1930s reveals that the system was put in place to provide incentives: firms that generate more unemployment will have to pay more taxes, and this might dissuade some layoffs. It doesn't work that way.

Methods of financing UI in state systems are a far cry from true experience rating of UI benefits. In practice, even the best systems simply advance interest free loans (benefits) to employers of laid-off workers, and these loans are repaid by higher future tax rates.⁸ Many employers, especially those in high unemployment industries such as construction, are not experience rated at all. For them, layoffs generate UI benefits for employees, but the cost of these benefits is never repaid. The UI system provides "free money," which is often a substantial subsidy to unemployment. A simple example will illustrate the point.

In a state like New York, most construction firms pay a fixed maximum tax rate, so they are not experience rated at all. For an employee who qualifies for \$200 per week in UI, a one month temporary layoff yields \$600 in income (allowing for a one

⁷ L. Katz and B. Meyer, "Unemployment Insurance, Recall Expectations, and Unemployment Outcomes," *Quarterly Journal of Economics*, November 1990.

⁸ R. Topel and F. Welch, "Unemployment Insurance: Survey and Extensions," *Economica* 47 (August 1980): 351-79; R. Topel, "Unemployment and Unemployment Insurance," *Research in Labor Economics* 7 (1985): 91-135; R. Topel, "Financing Unemployment Insurance: History, Incentives, and Reform," in *Unemployment Insurance: The Second Half Century*, ed. W. Lee Hansen and J. Byers. University of Wisconsin Press, 1990.

week waiting period) for the worker, but no cost for the firm. In effect, the UI system tells the firm: "We will give you \$600 with which to pay your workers, but only if you lay them off for a month." The incentive to increase the number of temporary layoffs is obvious.

This example is not an isolated case. Current methods of UI financing subsidize layoffs in virtually every industry and in every state system. Some state systems are worse than others, but the overall subsidy to unemployment is large and important. Empirical research in this area suggests that about one third of all temporary layoffs would not occur if the subsidy were eliminated.⁹ There are smaller effects on permanent layoffs as well. Thus the overall evidence is that current methods of financing UI increase unemployment.

What can be done to reduce the unemployment subsidy? Within the framework of current financing systems, three reforms are obvious and inexpensive. First, interest should be credited and charged to individual employer's accounts with the UI system. Under current accounting rules, which do not include interest, even experience rated employers repay only about \$0.60 for each dollar of benefits that workers receive. Interest bearing accounts would eliminate this aspect of the subsidy. This reform is politically feasible. Second, state maximum tax rates should be increased, which will extend experience rating to high unemployment firms, who account for most layoffs. Third, states should be required to index taxable wages to benefit levels, which would also extend serve to enhance experience rating for the typical employer.

What would be the overall effects of these changes? The most obvious effect would be reduced unemployment, especially temporary layoff unemployment. In turn, since aggregate benefit payments must be balanced by aggregate tax receipts, average UI tax rates could be reduced or UI coverage could be increased. Further, the move toward enhanced experience rating would also change the industrial composition of employment. The current system of subsidies means that unstable, high unemployment industries are too large, and stable employment industries are too small. In the long run, elimination of subsidies will shift employment from the one to the other, so aggregate employment will be less volatile.

Finally, these reforms would enhance the solvency of UI systems in the U.S. As I have shown elsewhere,¹⁰ lawmakers have been reluctant to raise UI taxes and taxable wages in proportion to legislated increases in benefits. The result is declining fund balances, which in many cases led state systems to borrow from Federal UI reserves. Long term balancing of employer accounts carries over to the aggregate, so the danger of fund "insolvency" would be reduced.

The financing reforms I have mentioned can be accomplished within the framework of current UI accounting systems. Those systems were designed in the 1930s and 1940s, when the costs of tracking individual employer accounts was substantial. As a result the similarity between "experience rating" of UI taxes and true experience rating of insurance premiums is remote. It need not be.

A bolder reform would put UI financing on a firm actuarial basis. The UI system could be run like any other form of insurance. Just as with the insurance that we all buy, premiums (taxes) can be based on an employer's (or an employee's!) expected loss (insured unemployment). Current technology is perfectly capable of predicting these losses using a wide array of information, including past losses, current market circumstances, industry, and so on. The system of UI taxes generated by such a system would be little different than the premium structure that successfully finances private insurance, so cost is not a major barrier. Relative to current financing methods, it would provide greater diversification of unemployment risks (better insurance), more experience rating (smaller unemployment subsidies), and greater solvency. I believe that it is worth thinking about.

III. CONCLUSION

I have proposed two reforms of the UI system. Neither reform would increase the cost of UI; probably the overall costs of running the system would fall, and total unemployment would be reduced. Their unifying theme is that UI is currently a poor system of insurance, but it can and should be substantially improved.

By extending waiting periods, the role of UI as insurance is enhanced because benefits can be increased during the portion of unemployment spells where they are most valuable. Short spells of unemployment can and should be self-insured by

⁹ R. Topel, "On Layoffs and Unemployment Insurance." *American Economic Review*, September 1983.

¹⁰ R. Topel, "Financing Unemployment Insurance," *op. cit.*

workers and their families. Public insurance should be concentrated on more serious losses, especially for workers who have lost a long-term job. Increased waiting periods offer the opportunity to enhance coverage in other dimensions as well.

By enhancing the degree of experience rating in UI tax liabilities, an important source of subsidy to unemployment would be eliminated. This alone would reduce unemployment, and it would have the added benefit of improving the solvency of state systems.

COMMUNICATIONS

STATEMENT OF THE AMERICAN FEDERATION OF STATE, COUNTY AND MUNICIPAL EMPLOYEES

The American Federation of State, County and Municipal Employees (AFSCME) submits the following statement for the record of the Senate Finance Committee April 23, 1991 hearing on Unemployment Insurance (UI). AFSCME represents 1.4 million state and local government employees, approximately 25,000 of whom work in local unemployment offices.

The Unemployment Insurance (UI) program was established in 1935 to serve two important purposes: to provide temporary income to unemployed workers until they return to work and to produce a countercyclical effect on the economy by sustaining consumer buying power.

A decade of neglect by the Federal and state governments has seriously impaired the ability of the UI program to fulfill these twin objectives. The nation entered the current recession with benefit coverage at an all-time low and with state administrative capacity to process benefit claims so weakened that the entitlement to benefits has been jeopardized.

BENEFIT COVERAGE

Unemployment insurance protection declined significantly during the 1980's. When the program was created in 1935, almost all of the unemployed were eligible. In the late 1970's, 50-70 percent of the unemployed received benefits. By last year, only one-third of the unemployed received benefits.

Federal and state policies contributed to this significant reduction in coverage. The states came out of the 1982 recession with their benefit trust funds almost \$6 billion in the red and with a new Federal requirement to pay interest on money borrowed from the Federal Government. Many built up their reserves to avoid future borrowing by increasing disqualification penalties, shortening maximum benefit durations, and raising base period earnings rules. In other words, they restricted eligibility and benefits in order to improve solvency and avoid employer tax increases.

The Federal Government took similar steps during this period. Among other actions, it arbitrarily excluded non-instructional education employees from the unemployment insurance system during their recurring bouts of involuntary joblessness. AFSCME has sought to restore the state option to provide unemployment compensation to this group of education workers since its removal in 1983. The House approved a provision to do so as part of the Budget Reconciliation Act of 1989, but the provision failed in conference. Restoring eligibility to this group of low-wage workers would have a major impact on the lives of thousands of families living at or near the poverty level. These workers should not be differentiated in such a punitive way from other seasonal workers who are entitled to unemployment benefits under state law. We strongly urge this Committee to support the restoration of the state option to correct this inequity.

The Federal Government also limited benefits for the entire workforce in the early 1980's by raising the Insured Unemployment Rate (IUR) trigger for activating the extended benefits program and by excluding from the IUR calculation unemployed workers receiving extended benefits. The combined effect of state and Federal policies restricting eligibility means that the IUR covers a much smaller share of the unemployed today than it did ten years ago. It has become a poor indicator of unemployment, and, consequently, the extended benefits program has become much less effective in reaching the long-term unemployed.

AFSCME strongly supports the provisions in H.R. 1367, sponsored by Representative Tom Downey (D-NY), which would reverse Federal and state policies that have

restricted benefits over the last ten years. The legislation prevents states from establishing unreasonable disqualification rules to limit benefit coverage. It also replaces the extended benefits program with the Federal Supplemental Compensation program triggered by state total unemployment rates and financed through a Federal unemployment tax levied on a greatly expanded and more progressive wage base.

ADMINISTRATIVE FINANCING REFORM

Improvements in extended benefits and coverage will be undermined, however, without administrative financing reform. It is essential that the administration of the local unemployment offices be placed on a more reliable and flexible basis. Otherwise, eligible workers may not receive the protection to which they are entitled.

Ironically, even as participation in the unemployment program shrank during the 1980's, the states found it increasingly difficult to maintain an adequate level of offices and experienced employees to process unemployment claims. Since 1983, state unemployment insurance staff levels dropped by 25 percent, from 57,000 to 43,000. The system entered the current recession with the least administrative capacity in decades.

A major reason for the dramatic decrease in staff and offices was declining Federal financial support. Indeed, the full extent of the Federal retreat has been obscured by the \$140 million that approximately 38 states have contributed to the system. With 28 states now facing serious deficits, we expect state support to diminish and conditions in local unemployment offices to worsen.

Federal funding also has become less reliable. Two years in a row, the unemployment insurance system faced serious administrative funding shortfalls. They developed because far more workers became unemployed than was anticipated when the UI appropriation for each year was enacted into law. A shortfall of substantially greater magnitude could materialize in Fiscal Year (FY) 1992 because of new pressures created by the Budget Enforcement Act.

The funding reductions and recent shortfalls have created serious hardship on unemployed workers and on local unemployment office employees. This year, unemployed workers in the upper peninsula of Michigan had to drive 80 miles one way to reach an unemployment office. It was taking five weeks or more to get the first unemployment check in Michigan. Payment delays increased in Connecticut, Maine, New Mexico, Indiana, and West Virginia. In Indiana, where the average number of claims per week jumped from 29,670 in October to 57,330 in December, the state was trying to operate without 17 offices that it had to close last year. In one week in March, one Indianapolis office had three claims takers trying to manage 750 new claims.

Some unemployed workers were waiting ten weeks for their first checks. A wait of 5, 6 or even 7 hours just to file a claim was not uncommon in many states. Telephones went unanswered; people got turned away from overcrowded offices; nerves got frayed; and backlogs built despite hours of overtime by tired and discouraged local office employees. Needless to say, the bill collectors still wanted their money, and the children still needed to be fed. Clearly, the safety net is failing.

Administrative funding shortfalls are not new to the UI system. Indeed, shortfalls occurred in 10 out of the last 18 years, and supplemental appropriations were routinely provided. What is new now, however, is a budget process that has made it increasingly more difficult to assure adequate and timely funding.

Under the current budget rules, unemployment benefits are mandatory expenditures, but the administrative funds to pay benefits are classified as discretionary. UI administrative funds must compete with all other domestic discretionary programs under strict spending caps.

It has become much harder to secure adequate UI funding in the regular Labor-HHS appropriation in this environment. This past fall, for example, conferees on the FY 1991 bill increased funds for UI and several domestic programs only to turn around and impose an across-the-board cut on all programs to bring the bill within the required spending ceiling. This action caused UI to lose \$49 million of the \$90 million increase and to enter the year with a certain shortfall.

Even if the Appropriations Committee fully funds the workload projected at the beginning of the fiscal year, unemployment may increase as the fiscal year progresses. Needless to say, the economy simply does not conform to the Congressional budget cycle. For example, as Congress worked on a supplemental appropriation for FY 1990, unemployment started to escalate. The FY 1990 supplemental came too late to prevent many office closings, and was too little by the time it passed. The estimated unemployment rate for FY 1991 has been revised upward three times since January of 1990. It rose from 5.3 percent in January, 1990 to 5.8 percent last July, to 6.1 percent last October, to 6.5 percent this January.

As disruptive as they were, the FY 1990 and 1991 shortfalls will seem minor compared to the potential crisis that could develop in FY 1992. The House Budget Resolution assumes a funding level of approximately \$400 million less than the President's request, and \$645 million below the January OMB baseline. The reasons appear to be both technical—relating to serious problems with the Congressional Budget Office (CBO) baseline for Unemployment Insurance used by the House Budget Committee—and procedural—concerning the lack of room under the domestic discretionary spending caps to finance recession-level UI workloads and other important domestic human resources programs.

Even if supplemental funding were approved as the House Budget Committee Report indicates, the UI system would go through an unprecedented upheaval before supplemental funds actually reached the states. As much as 45 percent of the presently-anticipated claims workload could be unfunded for a time.

The current method for appropriating administrative funds is too inflexible and unresponsive to changing economic conditions. Surely the authors of the 1935 law never expected the entitlement to unemployment benefits to be jeopardized by a Congressional budget process that prevents administrative funds from rising and falling with workload fluctuations.

We do not believe that the Appropriations Committees, faced with intense pressures to finance many important domestic programs, can solve the administration financing problem in a manner that will result in stable financing and responsible management. Supplemental appropriations help, but they are not a solution.

Unemployment insurance is the only state-administered benefit entitlement program which is subject to the domestic discretionary spending caps. This classification has caused a breakdown in the reciprocal relationship between the Federal and state governments originally established by the unemployment insurance law 56 years ago. Under that arrangement, the states were charged with the "proper and efficient administration" of the program. The Federal Government was charged with financing state administrative expenses from an employer tax levied by the Federal government under the Federal Unemployment Tax Act (FUTA).

There is no shortage of money from the Federal unemployment tax. The Federal account presently holding FUTA revenue dedicated exclusively to state administration had an excess balance of over \$1 billion at the end of FY 1990. The money, however is being held hostage by a rigid budget process that fails to accommodate the effect of economic changes on this entitlement program.

The only effective solution for the UI administrative problem is a reform that will make such costs mandatory. H.R. 1367 does this by creating an appropriated entitlement that releases funds according to workload demands and that removes UI administrative funds from the arbitrary constraints of the domestic discretionary caps. Doing so would put UI administrative financing on the same basis as all other state-administered benefit entitlement programs. We strongly urge the Finance Committee to include such a mechanism in any legislation it considers.

In summary, the Employment Security system is ill-equipped to provide adequate financial support to the unemployed. Coverage and benefits are grossly inadequate, and the system is staggering under the demands of those who are applying for benefits. While the nation relished the benefits of a boom economy in the 1980's, the safety net for the unemployed disintegrated. AFSCME is committed to rebuilding and modernizing the unemployment insurance program and looks forward to working with the Committee in that endeavor.

STATEMENT OF JIM EDGAR, GOVERNOR OF ILLINOIS; RICHARD J. WALSH, PRESIDENT, ILLINOIS AFL-CIO; LESTER W. BRANN, PRESIDENT, ILLINOIS STATE CHAMBER OF COMMERCE, ON BEHALF OF THE ILLINOIS EMPLOYERS' JOINT POLICY COMMITTEE ON UNEMPLOYMENT INSURANCE; AND LOLETA A. DIDRICKSON, DIRECTOR, ILLINOIS DEPARTMENT OF EMPLOYMENT SECURITY

Thank you, Mr. Chairman and members of the Committee, for the opportunity to present the view from the State of Illinois.

Honest differences will likely exist among us over many of the issues you are considering, but we all agree on at least two points. (1) Persistent shortfalls in Federal administrative funding are seriously threatening the ability of state unemployment insurance and job service programs to effectively serve the nation's job seekers and employers. (2) In view of the Unemployment Trust Fund's growing balances of dedicated administrative dollars, those shortfalls are totally unnecessary.

A sound employment security system for Illinois' job seekers and employers is crucial to the state's ability to compete in the world economy. In Illinois, business,

organized labor and state government are committed to working together to maintain that system.

Working together, we literally rebuilt Illinois' once debt-ridden unemployment insurance program since the beginning of the last decade. Through a series of overhauls of the state's unemployment insurance law, we have set competitive tax and benefit rates and balanced the need for prudent benefit account reserves against the cost of those reserves to the state's economy. Despite a currently rising claim load and statutory benefit increases in each of the last three years, Illinois' benefit account is expected to finish calendar year 1991 with a positive balance of more than \$1 billion.

Working together, we can help Illinois' employment security system successfully confront the challenge posed by the present economic downturn. To do so, however, the system must have administrative resources sufficient to get the job done.

To our dismay, Federal administrative funding for Illinois' unemployment insurance and job service programs has dropped steadily since Federal fiscal year 1984, by 21 percent after adjusting for inflation.

Since state fiscal year 1984, the Illinois Department of Employment Security has cut its staff levels by more than 25 percent—from 4,000 to fewer than 3,000. The Department has consolidated a network of 128 local unemployment insurance and job service offices into 63 facilities. In all regards, Illinois has operated its employment security system with a keen interest in efficiency and has consistently worked to do more with less.

However, Illinois still finds itself expending significant amounts of state-generated resources to maintain the Federal unemployment insurance and job service programs at effective levels of operation. State funding for Illinois' employment security system has risen by more than 320 percent since state fiscal year 1984.

As you know, Illinois is not alone. It is estimated that, in Federal fiscal year 1990, 33 states committed more than \$200 million in state funds to maintaining their unemployment insurance and job service programs. Still, nationally since 1980, 662 local unemployment insurance and job service offices have been shut down and more than 14,000 employees of state employment security agencies have been let go, according to the Employers' National Job Service Committee.

Compounding the problem, the current fiscal picture for Illinois and many other states will not allow the present level of state funding for the two programs to continue.

Today, unemployment insurance claimants in many states wait too long to receive their benefit checks. Others endure excessive delays in understaffed unemployment insurance offices, frequently after travelling long distances to get there. Higher unemployment workloads may ultimately threaten accuracy in state benefit payments and tax collections, with disturbing implications for state benefit accounts. The ability of state job service programs to adequately serve their customers is also suffering. Without adequate administrative funding from the Federal government, the situation will only get worse.

The Unemployment Trust Fund's Employment Security Administration Account ended Federal fiscal year 1990 with a balance of more than \$2.2 billion—over \$1 billion in excess of the statutory maximum. That account, which is financed by employers' Federal unemployment (FUTA) taxes, is dedicated exclusively to the administration of state unemployment insurance and job service programs and Federal oversight of the programs. The account's year-end balance for Federal fiscal year 1991 is projected at nearly \$2.4 billion—more than \$1 billion in excess of the statutory maximum.

By Federal fiscal year 1995, the administration account's year-end balance is expected to climb above \$3.6 billion, exceeding the maximum by almost \$2.4 billion.

Yet, the funds necessary to do the job are not reaching the states because of Federal budgeting decisions unrelated to the needs of the employment security system. Since the Unemployment Trust Fund remains part of the unified Federal budget, deposits into the Fund that are not spent offset expenditures from other Federal funds, including the Federal general fund. Accordingly, constraining administrative outlays from the Fund produces "on paper" a lower Federal deficit number.

The Federal deficit exists, however, because obligations against the Federal general fund consistently and substantially exceed Federal general revenues. Holding dollars in the Trust Fund does not correct that fundamental imbalance. It simply masks the extent of the imbalance, at the direct expense of the people the Unemployment Trust Fund was established to serve.

The present constraints on the highly workload-sensitive unemployment insurance system are particularly troubling. Of the nine major Federal entitlement programs run by the states, the unemployment insurance program is the only one for

which administrative expenses are subject to the discretionary spending caps set by last fall's budget agreement.

The Unemployment Trust Fund should be used for the purposes for which it was established—not to camouflage the Federal debt. To that end, the Trust Fund should be removed from the unified Federal budget. At a minimum, the cost of running state unemployment insurance programs should be treated the same as the administrative costs of other state-run Federal entitlement programs—as a mandatory rather than discretionary budget item.

The administrative funding problems now facing state employment security programs across the nation are very serious. We hope that, through your deliberations, you will be able to resolve those problems to the satisfaction of all interested parties. We are eager to work with you.

Thank you again for your time and attention, as well as for your interest in the employment security system and the people it serves.

PATRICIA A. TERRY,
April 25, 1991, Mesa, AZ.

WAYNE HOSIER,
U.S. Senate,
Committee on Finance,
Washington, DC.

ED MIHALSKI, *Minority Chief of Staff*,
U.S. Senate,
Committee on Finance,
Washington, DC.

Re: Bentsen calls hearing on unemployment compensation, leadoff witness to be Labor Secretary Martin (Hearing date: Tuesday, April 23, 1991)

Dear Sirs: I would like to submit my written statement on the above issue and hearing.

The Unemployment Compensation Program is in need of serious reconsiderations and adjustments. People are not being paid enough to survive, are not getting benefits fast enough, and is a long process in general.

Arizona is a prime example of the total problems. We have a high unemployment rate and rising. I believe it is in the 6% range. The most any person may receive for benefits is \$165.00 a week which averages out to \$4.12 an hour which is lower than minimum wage (4.25). That in itself is rather pathetic!

My husband is unemployed and I am not working. The future holds very dim right now. My husband is looking for a job by resume, answering ads in the paper, and listing with the job service at the unemployment office. It is tough and the pay scale from his layed off position does not come close to the pay he will receive from unemployment. I question how are we to survive under these circumstances?

I am hopeful you will take my statement in consideration when deciding how you will revamp the Unemployment Compensation Program. There are many others such as myself who have experienced similar problems with this program.

Please do some thing immediately to relieve the distress of the unemployed worker collecting benefits!

Respectfully,

PATRICIA A. TERRY.

UNITED MINE WORKERS OF AMERICA,
Washington, DC, May 3, 1991.

HON. LLOYD BENTSEN, *Chairman*,
Senate Committee on Finance,
U.S. Senate,
Washington, DC.

Dear Mr. Chairman: Though I was unable to appear before your Committee to testify on unemployment insurance issues, I would ask that you include in the record of the hearing this letter supporting changes in the nation's unemployment insurance system.

The U.S. coal industry experienced a 50 percent decline in employment during the last decade. Over 100,000 miners lost their jobs during the 1980s; most exhausted

their unemployment insurance benefits before they found new jobs, and most are working for significantly lower wages.

For example, in 1980 there were 53,000 miners working in West Virginia; today there are fewer than 25,000. Yet only 21 percent of the unemployed in West Virginia are receiving regular benefits. The short duration of benefits makes it nearly impossible for unemployed miners to be retrained for jobs in other industries.

We therefore recommend that Congress establish a new Federal Supplemental Benefits Program that would increase the length of benefits as unemployment rises. Providing extended benefits in areas with high unemployment will give more unemployed workers the opportunity to train for new jobs.

In addition, Congress should arrest the trend whereby states are achieving solvency by reducing the level of benefits. The National Commission on Unemployment Compensation has recommended that weekly benefits should be at least two thirds of the state's average weekly wage, and that benefit levels replace at least 50 percent of the individual's wage. We strongly urge Congress to adopt this policy.

Another problem that needs to be addressed is the chronic underfunding of state administrative services for the unemployed. Long lines and shorter hours at unemployment offices and long delays in claims processing confront jobless Americans just when they are most in need of government assistance. It is not unusual for workers claiming UI benefits to wait four or five weeks for their first check. Congress should either appropriate sufficient funds for this program or create an entitlement for UI administration.

Finally, the expansion of the Federal unemployment program should be funded by an increase in the taxable wage base to the Social Security wage base. At the same time, the tax rate can be reduced from .8 percent to .4 percent.

Today's unemployment insurance system supports less than a third of the jobless, and for those lucky enough to receive benefits, they often run out before the worker is able to find new employment. The United Mine Workers of America appreciates your efforts to draw attention to the problems of the unemployed and hopes that you will quickly achieve these crucial reforms.

Sincerely,

RICHARD L. TRUMKA, *International
President, United Mine Workers of
America.*

STATEMENT BY REBECCA BARNA, DIRECTOR, UNITED MINE WORKERS OF AMERICA
UNEMPLOYMENT ASSISTANCE FUND

April 25, 1991.

RE: Unemployment Insurance Problems

This letter is sent to address the concerns of our UMWA unemployed mine workers. Unemployment is difficult and very frightening for someone who has worked for years in providing an adequate income for their family.

The UMWA Unemployment Assistance Fund was established in 1989. The areas largest employer, Rochester and Pittsburgh Coal Co., Indiana, PA furloughed over 1,800 mine workers. The surrounding counties in Western PA were dealt other severe blows with the following announcements:

1989 Benjamin Coal Co., LaJose, PA (Clearfield County)—233 furloughed

PENNSYLVANIA MINES

1991, June Rushton Mine, Ocoola Mills, PA—250 jobs lost

The mines below will be phased out by 1992:

1992 Greenwich Mine—585 jobs lost

1992 Tunnelton Mines, Tunnelton, PA—250 jobs lost

Pennsylvania Mines Total—1,085 jobs lost

ROCHESTER & PITTSBURGH

1992 Florence Mine #2—350 jobs lost

BETH ENERGY MINE

1991 Cambria Slope #33—387 jobs lost

Add to this that each job lost from a mine closing has a statistical impact of 2.5 other support jobs lost. The statistics are overwhelming. This is devastating to the

whole economy in Western Pennsylvania. These are not minimum wage jobs. This will compromise the families' quality of life.

On April 4, 1991, the Labor Department stated the number of people filing new unemployment claims rose to 543,000 in the week ending March 23. This is the highest one-week level since January 1983.

Analysts have stated that the persistent high levels in March of 6.8 percent suggest that the recession was continuing despite other more favorable reports of an improved consumer confidence. Indiana County's unemployment in March 1991 was 11.8 percent. Pennsylvania's unemployment rate was reported at 7.4 percent; the highest in almost five years. PLEASE NOTE, these unemployment figures represent those that are receiving unemployment benefits and not those who have exhausted their unemployment or are on welfare.

The JTPA (Job Training Partnership Act) assists dislocated workers, individuals who have virtually no chance in obtaining work in the same field in which they worked due to shutdown, closings, etc. in obtaining schooling to re-enter the job market.

The UMWA Unemployment Assistance Fund works with the area S.D.A.'s (Service Delivery Areas) in assisting dislocated mine workers to attend approved schools that match the person's skills and interests. The major stumbling block encountered is that once the unemployed workers 26 week unemployment expires, there is only a small needs base payment allowance provided that in no way can cover expenses while attending schools. For a family of four the amount of needs base is 21 dollars a day while attending school.

HOWEVER, according to Federal regulations, the dislocated worker has to be physically enrolled in school within the 13th week of unemployment. This is virtually impossible except in anticipated shut down of a mine.

With an extension in unemployment benefits a dislocated worker could attend school for 18 months with only six months of the needs base payments being used. It would be much easier financially to complete the two-year course and re-enter the job market as a working member of society.

Presently, the workers attending school are living at below poverty level and have to apply for welfare assistance.

H.R. 1367 is a major step towards assisting the unemployed in keeping a positive attitude while obtaining schooling for future job goals.

We encourage you to improve the nations unemployment insurance system and we commend your leadership and committee members in your interest in this important issue for not only the coal mining regions, but the whole United States.

Sincerely,

REBECCA BARNA, *Director, UMWA/UAF.*

U.S. CHAMBER OF COMMERCE,
Washington, DC, May 6, 1991.

Hon. LLOYD BENTSEN, *Chairman,*
Committee on Finance,
U.S. Senate,
Washington, DC.

Dear Mr. Chairman: The U.S. Chamber of Commerce has a strong and active interest in the nation's unemployment insurance (UI) system, and is committed to assuring its long-term viability. The Chamber would like to offer its views on the current state of the system and on proposals to reform it.

It is interesting to note that all the UI constituencies, from business to organized labor to state legislators, agree on one point: administrative funding shortfalls have reached crisis proportions. Employment security agencies simply cannot respond to the volume of claims the recession continues to generate. Similarly, all interest groups hold that an insufficiency of tax revenues is not the problem. The Employment Security Administration Account in the Federal trust fund is projected to post a surplus in excess of its statutory ceiling at least through 1996. Rather, the problem is that Congress has been unwilling to appropriate the requisite dollars from a fund which, while formally dedicated to UI administration, still serves to pad the plus side of Federal deficit calculations.

Numerous sources can speak to lengthening unemployment lines, delayed payments, and overburdened state agency employees trying to stay afloat in an ever-rising tide of claimants. Neither the unemployed nor employers are receiving the service they deserve and—in the latter case—have paid for. As the Chamber has

pointed out, often these employers have paid twice for this poor service: once to the Federal government and once to a state which is scrambling to make up for funding not forthcoming from Washington. The Chamber urges Congress to take action to redress a situation that daily becomes more painful for all concerned.

Another topic receiving widespread attention—though not unanimous agreement—is the gap between the total number of unemployed persons and those receiving benefits. Figures as low as 33 to 40 percent have been cited for the percentage of the jobless being served by the system. Eldred Hill, President of UBA, Inc. and a member of the Chamber's Council on Unemployment Compensation, recently made the excellent observation that this gap is not really a matter of "coverage." Many workers who are in fact covered by the system—that is, their employers pay unemployment taxes on their wages—do not collect benefits because they fail to meet basic eligibility requirements. This group includes workers who voluntarily quit their jobs, were discharged for misconduct, had not worked long enough to meet minimum qualifying requirements, or have exhausted the benefits available to them by law.

Workers in the categories just enumerated are included in the Total Unemployment Rate (TUR), which some members of Congress advocate as a more appropriate rate to use for triggering extended unemployment benefits than the current Insured Unemployment Rate (IUR). The Chamber believes that the IUR remains the proper trigger, and notes that the TUR includes persons who do not even apply for UI benefits.

The benefits "gap" shrinks markedly when one compares not the whole jobless universe but those who apply for benefits to the number who receive them. Ronald L. Adler, President of Laurdan Associates and also a member of the Chamber's Council on Unemployment Compensation, used Department of Labor data to calculate the percentage of applicants who receive benefits: the national average is 73 percent.

The UI system was designed as a program of income maintenance for temporarily and involuntarily unemployed persons who have demonstrated a strong attachment to the work force. If Congress wishes to extend benefits to persons who do not meet this definition, it must be prepared to abandon a targeted UI program in favor of a welfare program under which entitlement, rather than eligibility, is the central criterion. On principle, as well as in light of Federal budget constraints, the Chamber assumes Congress would not seriously consider such a drastic change in program character.

Some members of Congress have raised questions about variations among state tax rates and benefit levels and have indeed suggested the imposition of Federal standards on what always has been a federal-state partnership. The Chamber believes that states should retain the prerogative to determine the amount and duration of cash benefits, conditions of benefit qualification, method of employer experience rating, and related matters. Each state can best judge its own unique economic and social conditions and create programs tailored to its short- and long-term needs, including cyclical economic variations. The Chamber strongly opposes attempts to recast the partnership in the direction of further federalization. The Federal partner can best serve the system by making good on its funding obligations.

Finally, the Chamber urges the Committee to resist suggestions that the system's perceived problems can be solved by increasing employer taxes. As noted, there is abundant money in the FUTA trust fund already. Further, it should be remembered that what will help the unemployed most is jobs. A tax increase that raises the cost of labor can only inhibit both job creation and economic recovery.

The Chamber thanks you for your consideration of its views, and requests that this statement be made part of the April 23 hearing record.

Sincerely,

DONALD J. KROES.

