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BOLSTERING THE ECONOMY: HELPING AMERICAN FAMILIES BY REAUTHORIZING THE PAYROLL TAX CUT AND UI BENEFITS

HEARING

BEFORE THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

ONE HUNDRED TWELFTH CONGRESS

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BOLSTERING THE ECONOMY: HELPING AMERICAN FAMILIES BY REAUTHORIZING THE PAYROLL TAX CUT AND UI BENEFITS

TUESDAY, FEBRUARY 7, 2012

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, DC.

The committee met, pursuant to call, at 2:34 p.m. in Room 216 of the Hart Senate Office Building, the Honorable Robert P. Casey, Jr., Chairman, presiding.

Senators present: Casey, Klobuchar, and Lee

Representatives present: Brady, Duffy, Mulvaney, and Maloney.

Staff present: Gail Cohen, Will Hansen, Colleen Healy, Jesse Hervitz, Patrick Miller, Robert O'Quinn, Steve Robinson, and Jeff Schlagenhauf.

OPENING STATEMENT OF HON. ROBERT P. CASEY, JR., CHAIRMAN, A U.S. SENATOR FROM PENNSYLVANIA

Chairman Casey. The hearing will come to order. We will get started. I know some are delayed by votes, but we will get started.

I want to thank the witnesses for being here at this busy time. I will do my opening, and then we will turn to our witnesses. Vice Chairman Brady, after he's voted, will be able to do his opening when he gets here. But we know that the House is voting as we speak.

But thanks very much. Today's hearing on the Payroll Tax Cut and Unemployment Insurance is indeed timely. I believe it can be helpful for Members of Congress on both sides of the aisle who are wrestling with how to continue these two programs through the remainder of 2012; it is good that we have a hearing like this in the midst of those discussions and debates and deliberations.

Like our Vice Chairman, Congressman Brady, I am a member of the Payroll Tax Cut Conference Committee, and we are making progress. It is slow, but we are making progress.

While the Conference Committee is immersed in the details of how to pay for Unemployment Insurance and the Payroll Tax Cut through the remainder of this year, today's hearing can shed additional light on the impact both programs have on the economy.

By reaching an agreement to cut payroll taxes for the remainder of 2012 and continue Unemployment Insurance for workers who have been out of work for more than six months, we can help

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Americans regain their economic footing, create jobs, and bolster the recovery.

While the economy has made good progress, adding more than 100,000 jobs in each of the last five months, we still have a long way to go to dig out from the Great Recession and the weak job growth that preceded it in the previous decade, the so-called "2000s".

The Democratic staff here at the Joint Economic Committee recently prepared a report that highlights how continuing the Payroll Tax Cut and Unemployment Insurance Benefits will boost consumer demand and strengthen the economy.

Both policies put money into the hands of consumers, money in their pockets so to speak, that they can spend. Unemployment insurance goes to workers struggling to make ends meet while they search for new jobs. Through the Payroll Tax Cut, over half of the increase in take-home pay in 2011 went to families making less than $100,000, and 86 percent of the increase in take-home pay went to families making less than $200,000.

The boost to paychecks has been critical to helping workers who have been coping with weak wage growth, which has failed to keep pace with the cost of living since early 2010.

This same Joint Economic Committee report that I referred to provides an analysis of the impact—or I should say, the economic impact of failing to continue Unemployment Insurance and the Payroll Tax Cut for the remainder of the year.

This particular Report estimates that failing to reauthorize Unemployment Insurance Benefits and the Payroll Tax Cut for the remainder of this year would reduce GDP growth by 1.7 percentage points in calendar year 2012. That is a very big hit when you consider real GDP is expected to grow by just 2.2 percent in 2012, according to the Blue Chip Consensus. We cannot afford to jeopardize the modest economic growth that is currently forecasted.

Last week, the Joint Economic Committee released a second report detailing on a county-by-county basis the impact of extending the Payroll Tax Cut. The report specifies the additional take-home pay that a worker would receive in each county in the country, if Congress were to reauthorize the cut for the remaining 10 months of the year.

We know that this data will be helpful in states and by county. The Employment Report that was released on Friday showed that the economy added more than 250,000 private-sector jobs in January. The unemployment rate dipped for the fifth consecutive month to 8.3 percent. This is both welcome and encouraging news.

But—and this is a big "but"—with the economic growth forecasted to be slow in the first half of the year, we cannot be complacent, or take our eye off the ball. As I said at the outset, this hearing is timely. We have just three weeks before the two-month reauthorization of both Payroll and Unemployment Insurance expires, three weeks to come together on a bipartisan manner to continue these very important programs to help families and to strengthen the economy.

So I look forward to listening to each of our witnesses, and to a good discussion of these topics.

I will first provide just a brief introduction of our witnesses. Moving from my left to your right, Dr. Mark Zandi is the Chief Economist of Moody's Analytics, where he directs the company's research and consulting services to business, governments, and other institutions. Dr. Zandi's research includes macro-economic, financial, and regional economics. In addition, he conducts regular briefings on the economy. He received his Ph.D. at the University of Pennsylvania.

I'll just stop there and pause for a moment.

[Laughter.]

He received his BS Degree from the Wharton School at the same University of Pennsylvania. So, Dr. Zandi, welcome, and welcome back.

The Honorable Mark W. Everson——

Mr. Everson. "E-"verson.

Chairman Casey. Oh, I'm sorry, "Ee-verson". I'm sorry for mispronouncing that.

Let me start again. The Honorable Mark W. Everson became Commissioner of the Indiana Department of Workforce Development, or DWD, on June 1st, 2010, and is a member of the cabinet of Governor Mitch Daniels.

The DWD manages and implements training and employment programs for Hoosiers, unemployment insurance systems, facilitates regional economic growth issues for the State of Indiana. Mr. Everson has extensive Federal Government and private sector experience, including service as an IRS Commissioner and president and CEO of the American Red Cross. He has held operating and financial posts with major companies in the United States and abroad.

Thank you, sir, for being here.

Mr. James Sherk is Senior Policy Analyst in Labor Economics at the Heritage Foundation. Mr. Sherk has written on the dynamics of rising unemployment in the recession, the economic consequences of extending Unemployment Benefits, Cardcheck, and other labor policy issues. He joined the Heritage Foundation in 2006 after completing Master of Arts at the University of Rochester, where he concentrated in econometrics and labor economics.

Mr. Sherk, thank you for being here.

Mrs. Judy Conti—Ms. Judy Conti, I should say, is the Federal Advocacy Coordinator for the National Employment Law Project, so-called NELP. We all have acronyms around here; we should use them where we can. Judy joined NELP in 2007 after spending seven years as co-founder and executive director of the D.C. Employment Justice Center, a legal service provider devoted to workplace justice in the D.C. Metropolitan Area. Before joining NELP, Judy's work has been widely recognized with awards from the American Bar Association, the Washington Area Women's Foundation, the Hispanic Bar Association of the District of Columbia, and the Echoing Green Foundation. Ms. Conti has a J.D. from the College of William & Mary.

So those are the biographical sketches, and we will start with Dr. Zandi.

STATEMENT OF DR. MARK M. ZANDI, CHIEF ECONOMIST, MOODY'S ANALYTICS, PHILADELPHIA, PA

Dr. Zandi. Thank you, Senator.

I want to thank you and other members of the Committee for the opportunity to speak today. The views I express are my own and not those of the Moody's Corporation.

I am going to make five points in my remarks.

Point number one is that the economy is much improved, and fiscal policy has contributed significantly to that improvement. The improvement is most evident in the job market. As you pointed out, we saw payrolls grow almost a quarter of a million in January; 2 million payroll jobs have been created over the past year through January.

The job gains are increasingly broad-based across industries and regions of the country. Hours worked has improved. Hours worked in manufacturing were as high as they have been since the 1990s. Unemployment has declined significantly—almost a percentage point—over the past year. That is due to the stronger job growth, not due to weaker labor force growth, which is encouraging.

I do think fiscal policy has contributed significantly to this improvement. There are many things that you and other Congressmen and the Administration have done. I would just like to point out, though, that last year's Payroll Tax holiday and Emergency UI Programs were very instrumental in keeping the economy together.

I would argue that without the benefit of those programs last year the economy would likely have fallen back into Recession; that the surge in gasoline, food, apparel prices was a significant hit to the economy and the help from Emergency UI and from the Payroll Tax helped fill the void. That was very significant.

The second point that I would like to make is that the economy, while much improved, is still very fragile, as you pointed out. Growth is still less than we would hope for, and there are significant threats to the recovery.

The European sovereign debt crisis remains a very significant threat, and the European economy is in recession, and the financial system there is still in turmoil.

The housing crisis here in the United States is also a very significant program. The foreclosure crisis continues on and we are still suffering house-price declines. As long as house prices are falling, it is hard to get entirely enthusiastic about the economy's prospects. The home is still the most important asset that most people own. It is key to small businesses that use their home as collateral for getting a loan. Of course local governments rely on property tax revenue.

Judging from surveys of consumers and businesses, the collective psyche is still very fragile. So if anything else goes wrong, I think the recovery could easily be derailed. We cannot conclude that we are off and running here.

This leads me to the third point. I do think it is vital that you extend the current Payroll Tax Holiday and the Emergency UI Program through the end of the year. This is important to the recovery, keeping it together.

It is a lot of money to American households. By my calculation, it's almost $150 million in total, which is about 1 percent of GDP.

Based on my work, if the programs are not extended, GDP growth in 2012 will be seven-tenths of a percent lower this year than otherwise would be the case. We would lose roughly a half-million jobs compared to what we would have gotten otherwise if we extend them. Unemployment would be measurably higher.

So in my view, it is very important. The Payroll Tax Holiday is particularly important because it is big. It's about a little over $100 billion of the $150 billion, and evidence from other similar kinds of tax cuts indicate that roughly two-thirds of any tax cut will be spent within six months. So this is very important to spending and keeping the economy going in the near-term.

The UI is also very important. It is much smaller in cost, but the bang-for-the-buck is very large. Unemployed workers will use the benefits quickly to spend.

There are disincentive effects. I do think there is evidence to suggest that some people will stay out of the workforce, out of work longer because of the UI benefits; but those negative disincentive effects are swamped by the benefits of the UI Program in terms of its benefit to aggregate demand.

Fourth, I think reforming UI is very important, but I also think it is important not to restrict UI. My favorite reforms would be work/share, wage-subsidy programs. I think they hold out a lot of potential benefit. But restrictions on UI, such as some of the discussion regarding the need for a high school diploma, drug testing, I think is unnecessary and counterproductive in the current context.

Finally, my fifth point, I think this should be paid for. I think we are now at a point where we can't do this without paying for it in the long run. I will point out, though, that there is a lot of fiscal restraint coming in current law in 2013. So any pay-for should be accounted for over a longer period of time. I don't think you want to pile on in terms of the pay-fors in 2013. The economy will already have a lot to digest.

Thank you.

[The prepared statement of Dr. Mark M. Zandi appears in the Submissions for the Record on page 34.]

Chairman Casey. Thank you. Commissioner Everson.

STATEMENT OF THE HONORABLE MARK W. EVERSON, COMMISSIONER OF THE DEPARTMENT OF WORKFORCE DEVELOPMENT, STATE OF INDIANA, INDIANAPOLIS, INDIANA

Mr. Everson. Mr. Chairman, Senator, Congressman:

The Federal-State Unemployment Insurance partnership is an important, proven system which has successfully served the Nation for more than seven decades. Over time, the system has adapted well to changes in the American economy and the evolution of the Nation's workforce.

Nevertheless, the system has been severely strained by the recent Recession. It can weather the storm, but states require flexibility on the part of the Federal Government to do so. States can also be laboratories for policy changes that can improve the program and help the Nation's workforce meet the challenges of the 21st Century.

Last week, 138,000 individuals collected some form of Unemployment Insurance Benefits in Indiana, comprising 74,000 who drew state benefits, and 64,000 whose benefits were paid 100 percent by the Federal Government.

Similar to other states, Indiana has a significant number of people who unfortunately have been unemployed for over a year. I would note, however, that our state initial and continued claims have now returned to 2007 levels. So that is good news.

As you are no doubt aware, 27 States have borrowed over $38 billion to continue funding the state portion of Unemployment Insurance Benefits. You can see there is a map in the testimony on page 3. The States with the highest indebtedness per worker are Indiana, Nevada, North Carolina, California, and Pennsylvania, Mr. Chairman.

At the start of the last decade, Indiana's trust fund had a $1.6 billion surplus. In 2001, the State Legislature enacted a series of benefit increases implemented in steps over much of the past decade and provided limited premium relief to employers.

These legislative changes created a continuing structural imbalance. In Indiana, our trust fund coffers were empty by late 2008, just as the collapse began. At the end of 2010, the trust fund owed the Federal Government $1.96 billion.

The Unemployment Insurance Program has three overall design elements: Revenues, the premiums paid by employers into the system; eligibility—that is, who is entitled to receive benefits; and benefit levels—that is, the method of calculating how much an unemployed individual receives each week, and for how long.

In early 2011, Indiana's Legislature enacted balanced, comprehensive reform addressing all three elements. Although the trust fund got into trouble mostly due to an increase in benefits, over two-thirds of the cost of this solution is being borne by employers.

Premiums increased—and the total aggregate cost for employers between the premiums and the interest surcharge, and the FUTA reclaim went up by 60 percent from 2010 to 2011.

The most notable change in eligibility standards in Indiana's reform package addressed repeat users of the system who plan and conduct regular shutdowns of their operations.

Prior to the 2011 reform package, Unemployment Insurance Benefit amounts in Indiana—as in many states—were calculated based only on the highest quarter of a worker's earnings. This method of calculation often yielded different benefit amounts for individuals who had earned the same wages over the course of the year.

To provide an example: Under current law, last month my department received a WARN notice of the closure of a K–Mart in Portage, Indiana. Over 200 people would lose their jobs. Assume that one of the workers has earned $500 a week. That is $26,000 a year. Under current law, that individual will receive $280 a week in benefits.

Take a construction worker earning the same $26,000 but only working 9 months. That individual receives $367, much more because of the high quarter calculation. To address this inequity, the legislature determined that the future benefit amounts should be calculated based on annual earnings.

Thus far, our reform package is working as intended. The trust fund balance, as I indicated, was $1.96 billion at the end of 2010 and held steady in 2011. That is also a chart in your packet. You can see it goes flat.

Now most of that, or the big piece of that is a reduction in the benefits, because as was indicated the economy is better, but the increase in the premiums also significantly contributed.

My last section: The Federal non-reduction rule was initially established in 2009 to prevent states from offsetting through benefit reductions a $25 supplemental payment paid for with federal funds. The $25 supplement has been discontinued, but for the first time—in early 2010—the Federal Government required the non-reduction rule be tied to Federal Extended Unemployment Benefits. This is a departure from the past when Federal extensions of benefits were provided in periods of high unemployment but there was no such rule.

When Indiana enacted its reform package, the new benefit calculation was purposefully delayed until July 1, 2012, in order to take effect after the expiration of the Federal extensions. While the non-reduction rule was eliminated from the House version of the most current Federal extensions, it was retained in the recent two-month law. We urge you to eliminate it from any further extension of this program.

There are currently three other states that may be implicated by the non-reduction rule, along with Indiana: Rhode Island, Arkansas, and Pennsylvania.

Other states have addressed trust fund insolvency by avoiding the non-reduction rule but decreasing the number of weeks of Unemployment Insurance compensation available to individuals. Several have reduced the duration of benefits from 26 weeks to 20.

If the non-reduction rule remains in place, more states will likely shorten the number of weeks of Unemployment Insurance Benefits, and in fact they may be reluctant in the future to increase benefits at all for fear that if there are more Federal extensions in bad times they can't bring them down.

The recently enacted non-reduction rule has significantly altered the long-standing Federal-State balance of the program. States should retain the flexibility to determine the most appropriate Unemployment Insurance Benefits program and the method of addressing the insolvency of their trust funds.

I would note that the National Association of State Workforce Agencies called for the elimination of the non-reduction rule in its last annual conference in September.

In Indiana, we value our partnership with the Federal Government in operating the Unemployment Insurance System. We believe we have put our program on a healthy and sustainable path. I commend Congress for looking at avenues of reform, such as work search and training requirements. However, as with the non-reduction rule, I ask you to provide states the flexibility to provide appropriate overall program design best suited for their circumstances.

Thank you.

[The prepared statement of Hon. Mark W. Everson appears in the Submissions for the Record on page 47.]

Chairman Casey. Thanks, Commissioner. Mr. Sherk.

STATEMENT OF MR. JAMES SHERK, SENIOR POLICY ANALYST IN LABOR ECONOMICS, THE HERITAGE FOUNDATION, WASHINGTON, D.C.

Mr. Sherk. Chairman Casey, Vice Chairman Brady, and members of the Joint Economic Committee:

Thank you for inviting me to testify this afternoon. My name is James Sherk. I am a Senior Policy Analyst in Labor Economics at the Heritage Foundation. However, the views I express in this testimony are my own and should not be construed as an official Heritage position.

This afternoon I want to explain to you that, while the Unemployment Insurance System should be changed in a recession, spending more on UI benefits does not bolster the economy.

There are three factors for Congress to consider about extended Unemployment Insurance.

The first factor is that increasing the duration of benefits in a recession does make sense, but these increases should be proportionate to the state of the economy. Unemployment Insurance insures workers against the risk of losing their job. Since it takes longer to find new work in a recession, it takes longer benefits to provide the same degree of insurance.

The question is: How much longer? Additional benefits help workers in a difficult situation, but they also cause UI claimants to stay unemployed longer. This fact is one of the most conclusively established findings in all of labor economics.

Unemployment Insurance encourages the unemployed to search for the jobs they want to find, rather than the jobs they are most likely to find. Alan Krueger, Chairman of the President's Council of Economic Advisors, finds that unemployed workers tripled their time job-hunting when their benefits were about to run out.

Researchers at the Federal Reserve Banks of San Francisco and Chicago found that extending Unemployment Benefits to 99 weeks has increased the unemployment rate by about half a percentage point. Extended benefits are not the main reason unemployment remains high, but they are economically significant. And even in today's job market, 99 weeks of benefits is excessive.

In a normal economy, Unemployment Insurance's six months of coverage provides benefits for about 50 percent more than the average spell of unemployment. Now in the current down economy, the average length of unemployment has risen to 40 weeks. Extending benefits to 60 weeks would thus proportionately increase benefits in accordance with the state of the weak economy.

But especially in light of recent improvements in the labor market, benefits should be brought down from the level of 99 weeks.

The second factor Congress should consider is that Unemployment Insurance benefits do not stimulate the economy. Benefits should only be extended if the humanitarian arguments for doing so justify it.

Over the past four years, the federal and state governments have increased Unemployment Insurance spending by $300 billion. Congress has repeatedly heard testimony that this increased spending will bolster the economy. Instead, Americans have suffered through the slowest recovery of the post-War era.

This should have not come as a surprise. Empirical studies find that government spending does not spur private-sector growth. Empirical research into UI spending in individual states also finds it has negligible economic effects. And international evidence reinforces this conclusion.

If Unemployment Insurance spending stimulates the economy, then unemployment would not rise as fast in countries that have more generous systems. The automatic stimulus from the more generous benefits would cushion the shock of any recession. Instead, the opposite happens.

Unemployment rises faster in countries with more extensive benefits. The disincentive effects of Unemployment Insurance overwhelm any stimulus they provide. And this may be why few policymakers in other developed countries argue that UI spending stimulates demand and employment. This is a uniquely American debate.

Now this does not mean, and I am not arguing, that benefits should drop back to six months. What it means is that extending benefits are not an economic free lunch, and they come at a cost.

If extended benefits are a priority, they should be paid for by reducing spending on less important programs that are less of a priority.

The third factor is that Unemployment Insurance needs reforms that go far beyond changing the number of weeks of benefits. The UI system largely focuses on distributing benefits to covered individuals. It places little emphasis on returning the unemployed to work, the primary policy goal.

Unemployment Insurance also needs more safeguards against abuse. In most states, claimants apply either online or by calling an automated hotline. They attest to their job search by clicking a box or pressing a button. Now this reduces administrative costs, but it also enables individuals to collect checks without trying to find work.

The vast majority of UI recipients try hard to find work, but some do not. Experiments in Maryland found that stronger job search requirements reduced UI claims by 5 to 8 percent. Reducing Federal UI spending by a similar amount would save about $2 billion.

The UI system should be reformed to address these problems. The Federal Extended Benefits Program should have job-search requirements, which are not currently in place. State law requires it, but the extended benefits do not require job-search.

The states should also be given freedom to innovate, to try different reforms to get the unemployed back to work faster. Now some of the ideas would be those that Mr. Zandi has suggested that I am somewhat skeptical of—things like work sharing, or wage subsidies.

There are other ideas that different states might try like intensive job search assistance, or requiring more training as a condition of receiving benefits, or even getting an associates degree online, which state could do at relatively low marginal cost.

We don't know in advance which of these systems would work. The federal government should allow the states to innovate. Give the states waivers from the Federal requirements to let them try new approaches, but require them to demonstrate that any innovation they're doing is actually succeeding.

That was how welfare reform happened in the 1990s, because the waivers for individual states demonstrated successful policy solutions. By 1996 there was a bipartisan consensus, and overwhelming bipartisan majorities in both Houses that passed welfare reform, and President Clinton signed it. And it has been one of the greatest public policy successes of the past several decades.

This is a model we should look to for improving Unemployment Insurance. Thank you for inviting me to testify.

[The prepared statement of Mr. James Sherk appears in the Submissions for the Record on page 54.]

Chairman Casey. Thanks very much. Ms. Conti.

STATEMENT OF MS. JUDITH M. CONTI, FEDERAL ADVOCACY COORDINATOR, NATIONAL EMPLOYMENT LAW PROJECT, WASHINGTON, DC

Ms. Conti. Thank you, Senator Casey, Congressman Brady. I appreciate the opportunity to come here today.

The National Employment Law Project is a nonprofit organization that advocates on behalf of low-income and unemployed workers. We work to maintain strong federal and state programs of Unemployment Insurance that are providing an essential lifeline of support for individuals who, through no fault of their own, have lost a job.

As we have discussed, the economy is improving—and that is a good thing—but unemployment still remains unacceptably high, and long-term unemployment, more than six months, remains dangerously high. And we cannot lose sight of that.

Therefore, it is crucial for Congress to maintain the robust support that it has provided for the unemployed over the past three years, and to refrain from enacting unnecessary and harmful barriers to benefits that would impair the economic functions of the UI safety net now and in the future.

Presently, 42.9 percent of those who are unemployed, nearly 6 million, have been out of work for over 6 months. Average durations of unemployment in November reached a record high of almost 41 weeks; and they have only come down slightly, registering 40.1 weeks in our latest work—jobs statement.

UI Benefits are an essential lifeline for the unemployed Americans. The average UI Benefit is only $296 per week, and this represents about 50 percent of the income needed to cover the most basic necessities of food, housing, and transportation as measured by the Annual Consumer Expenditure Survey.

While the average family spends about $1,380 per month on housing alone, the average monthly UI Benefit is $100 less than that. Put simply, today's unemployed workers are not living the high life. Yet these benefits, modest as they are, have gone a long way to prevent economic hardship for millions of families since the Recession began.

In 2010 alone, according to recent Census figures, UI kept 3.2 million Americans out of poverty, over 1 million of whom were children. Equally important, UI plays an important and positive role in the overall economy and broader labor market.

Over the years, several exhaustive studies have documented the countercyclical impact of Unemployment Insurance, lifting up an economy that's been beaten down by a Recession. The most recent such study, authored by Wayne Vroman of the Urban Institute, reviewed the role of UI Benefits in this particular economic downturn and Recession and found that the Nation's economy grew by $2 for every $1 spent on Unemployment Insurance during the latest Recession.

Time and time again, the nonpartisan Congressional Budget Office rates UI Benefits as among the most impactful economic stimuli possible.

And contrary to claims that receipts of UI Benefits serves as a substantial significant disincentive to work—and these claims are often based on dates studies of the impact of UI during non-recessionary periods—recent research by Professor Jesse Rothstein of the University of California at Berkeley, roundly refutes that assertion.

Rothstein's work is a careful study of the effects of UI extension on the job searches in this Recession. Although he finds a .3 percentage point increase in the December 2010 unemployment rate, he also found that at least half of this increase is due to the fact that receipt of UI Benefits keeps workers in the labor force. It keeps them searching for jobs, rather than dropping out and becoming discouraged workers.

And just two weeks ago, the Federal Reserve Bank of San Francisco put out a report concluding that weak labor demand is the big driver of increases in the length of time that workers are unemployed, not UI Benefits.

Finally, a recent survey and report from the Heldrich Center for Workforce Development at Rutgers University of workers who had lost their job during the Recession showed that unemployed workers who received UI were more likely to have been proactive in seeking work than those who didn't receive UI, with beneficiary recipients reporting more hours devoted to job search, more frequency contacting friends and examining job postings.

As a final matter, I note that there are many proposals in H.R. 3630, the bill in the House of Representatives that is the subject of the Conference Committee that Mr. Brady and Mr. Casey both serve on. Many of these proposals represent unnecessary and punitive barriers to benefits that should not be rushed into law in the context of a Conference Committee negotiation over a much larger bill.

There is a full discussion of these proposals in my written testimony, including NELP's arguments as to why we need to retain the non-reduction rule, and I am happy to answer questions about that during the question and answer period.

If we do want to have a serious conversation about how to help reattach people to the workforce, there are actually many tried and true programs that we could better fund or enact, such as work sharing, or enhancing the high quality reemployment services that are already offered by all state agencies with only modest Federal funding right now.

If Congress is serious about aiding re-employment, these are the ideas to consider, not ill-advised proposals that do nothing but serve as barriers to benefits, or as ways for states to raid already stretched UI trust funds and use that money for unproven programs, rather than paying benefits that workers have earned.

It is inconsistent with American values and bad for the American economy to penalize those who have suffered most as victims of the Great Recession by denying or reducing their UI benefits, or to demonize them through unnecessary and stigmatizing barriers to participation in the program.

Instead, Congress should reauthorize the Federal UI programs immediately, and without reductions or barriers to benefits.

Thank you very much for your time.

[The prepared statement of Ms. Judith M. Conti appears in the Submissions for the Record on page 64.]

Chairman Casey. Thanks, Ms. Conti.

We are joined by Vice Chairman Brady, who had a series of votes, and then sprinted over to get here. So we are grateful he is here. Vice Chairman Brady will do his opening, and then we will get to questions. Thank you.

OPENING STATEMENT OF HON. KEVIN BRADY, VICE CHAIRMAN, A U.S. REPRESENTATIVE FROM TEXAS

Vice Chairman Brady. Great. Thank you, Mr. Chairman, for holding today's hearing. I appreciate the witnesses being here today.

I agree with you that this Committee must examine the whole picture—understanding both the benefits of extending the Payroll Tax Cut and long-term Unemployment Benefits and their unintended consequences.

There is a strong bipartisan consensus in Congress to extend both of these expiring provisions through the end of this year. However, serious differences remain over how we should pay for these expensive extensions and whether we should reform the outdated Unemployment Insurance program.

As popular as the Payroll Tax Holiday may be, economists disagree about its effectiveness as an economic stimulus. However, economists agree that Social Security faces serious and growing cash-flow deficits. I want to refer to this chart over here that shows the cash-flow deficits for Social Security over the next decade.

[Chart submitted by Vice Chairman Brady titled "Social Security's Cash Flow Deficits" appears in the Submissions for the Record on page 84.]

In the black area of that graph, you can see what has happened as a result of diverting one-sixth of Payroll Tax revenue away from the Social Security revenue stream. It creates a significant sinkhole that exacerbates Social Security's cash flow problems. Noncash accounting transfers from the General Fund cannot alleviate these cashflow problems.

Last year, the U.S. Government had to borrow $142 billion from investors—including foreign countries like China—to pay Social Security benefits to our seniors.

Congress must fill this sinkhole to ensure that we will be able to pay promised Social Security benefits. That is why House Republicans are insisting that Congress must offset any loss of payroll tax revenue with actual cash savings in other areas of the government, not simply accounting gimmicks. House Republicans will protect this vital program from debilitating cash diversions with common sense savings that have had strong bipartisan support.

As for unemployment, clearly economic policies of the Obama Administration did not produce the vigorous recovery, for which hardworking taxpayers had hoped. Tens of millions of Americans are struggling to make ends meet. Millions can't find a full-time job, and millions more can't find any job at all. Even worse, other millions have simply given up and stopped looking for work, leaving us with the lowest workforce participation rate in nearly three decades.

Our priority must be to create a far stronger economy in which American businesses will have the confidence to make investments in new buildings, equipment, and software, expand production; and create millions of new well-paying jobs to get this economy back ontrack.

As to Unemployment Insurance, we should reform this program and refocus it on the common-sense goal of getting people back to work sooner rather than just paying benefits. House Republicans have passed legislation that would:

One, renew the long-term Federal Unemployment Benefits for the rest of this year while gradually reducing the maximum duration of benefits to 59 weeks.

We require recipients to search actively for work from day one. We know the longer the people are unemployed the harder it is for them to new employment. Under existing law, beneficiaries may collect unemployment checks for a year and a half without really having to look for a job. In some states, they don't even have to search for a job at all. That's unacceptable.

This bill, passed in the House with bipartisan support, allows the States to adopt innovative programs to match beneficiaries with local jobs.

We also require those on unemployment without a high-school degree to work on earning a GED. Adults without high school diplomas have a very hard time finding and keeping a job. They are often the last hired and often the first fired.

We also end the Federal prohibition against States testing applicants for illegal drug use. Drug-screening ensures that recipients will be able to take the jobs that they are offered.

As we will hear today, and have heard today, long-term unemployment benefits have clearly helped families in need, but there is a cost as well. Two recent studies found that extending the duration of benefits actually increases the unemployment rate:

A study by the Federal Reserve Bank of San Francisco found the unemployment rate at the end of 2009 would have been nearly half a percentage point lower—9.6 percent instead of 10 percent—if jobless benefits had not been extended beyond their usual 26 weeks to as much as 99 weeks.

According to a Brookings Institute paper, the 2011 extension of long-term Unemployment Insurance raised the number of unemployed in January of last year by between 0.2 and 0.6 percentage points. That translates into between 200,000 and 900,000 additional workers without jobs.

Repeated extensions of long-term benefits are also threatening the solvency of the entire unemployment system, as Commissioner Everson has pointed out. States have borrowed over $38 billion from the Federal Government to cover their shortfalls. Under current law, repaying these Federal loans and rebuilding state trust fund balances would require an unprecedented payroll tax increase in nearly every State. These higher taxes would punish the very job creators that we hope will add new jobs to hire the unemployed.

To conclude, we must move forward with a bipartisan agreement to extend the payroll tax holiday and long-term unemployment benefits. But at the same time, we must also adopt common-sense reforms to make the Unemployment Insurance Program work better and avoid adding to our unsustainable federal debt.

I look forward to the testimony of the witnesses today and to the questions, as well, Mr. Chairman.

[The prepared statement of Representative Brady appears in the Submissions for the Record on page 85.]

Chairman Casey. Vice Chairman Brady, thank you very much.

I will start. We will do five-minute rounds, and just so our colleagues know, the lineup we have so far is after me; Vice Chairman Brady, then Senator Klobuchar if she is back, Senator Lee, Representative Duffy, and Representative Mulvaney, and we will keep to that. And we can certainly add a second round.

Dr. Zandi, I wanted to start with you. Particularly with regard to the so-called bang-for-the-buck argument and the analysis that undergirds the conclusions that you and others have reached about the benefit of spending a buck on Unemployment Insurance, say, or in another program, and the economic benefit that follows from that.

Can you walk through some of that? I know in your testimony you did not have time to get through every part of it that you prepared, but I just wanted to get a sense of that, especially on the two major topics of the bang-for-the-buck on the Payroll Tax Cut, as well as that for Unemployment Insurance.

Dr. Zandi. Sure. In my testimony there is a table where I lay out my current estimates of the multipliers, or so-called bang-for-the-buck for different programs, including the Payroll Tax Holiday and Emergency UI.

For UI I'm speaking from memory, I think it is $1.55. That is an estimate of the impact on GDP one year after the benefit is provided. So looking out a year from now.

For the Payroll Tax Holiday it's smaller. I believe it is $1.27, something like that.

I should point out that the logic is pretty straightforward; that you provide a benefit to a household, particularly in the case of UI, a very financially stressed household. They take that dollar. They have no other financial resources. They've probably blown through their savings, any help they could get from family and friends, and they spend that money to support themselves. And that money gets into the economy and creates other economic activity and jobs and so forth and so on down the road, and it is about $1.55.

These multipliers, bang-for-the-buck estimates, are varied. They depend on the various models that are being done. In the case of UI, the range of estimates—and this is from the CBO and the Urban Institute, Department of Labor, other studies that have been done over the years, range from $1.50 to over, in the case of the Urban Institute $2, and some are higher than that. It is one of the most effective forms of support to the economy, particularly in recessions.

I should say also that these multipliers are not immutable. They vary according to the economic environment. So for example in a well-functioning economy where the unemployment rate is near full employment, let's say 5.5, 6 percent, then providing this kind of benefit will not result in a very large multiplier, and in some cases for some kind of stimulus it could be negative because they do have to pay for it, and it has negative consequences through issuing debt and interest rates and so forth and so on.

So in an economy that is operating flat out, you don't want to do something like this. But in an economy that is really struggling with unemployment in the case of the Great Recession at 10 percent, then you don't have those kinds of negative effects and you get much larger multipliers.

Also in the analysis that I do, you will note that over time I've produced similar kinds of multipliers for you and Congress over the past several years, you'll note that those multipliers change over time. In the case of UI, the multipliers have actually declined over time because I do think that there is some disincentive effects from long-term unemployed, and they cease to benefit of Unemployment Insurance. But net-net, considering the disincentive effects and the positive benefits that are created by supporting consumer spending and demand in helping these households, it's a slam-dunk positive. It is still very, very important to do.

Chairman Casey. I know that in the context of both these issues, and especially in the context of the work of the Conference Committee that Vice Chairman Brady and I are serving on. One of the things we have tried to emphasize and I think it's better to be positive and emphasize the benefits, but also the consequences of not getting an agreement on the two. In particular it has been helpful for me in Pennsylvania. Our staff asked you months ago and you produced an analysis that was just payroll tax cut consequence in Pennsylvania for one year.

And the job impact—because sometimes when people hear "GDP" impact it's kind of hard for folks to measure—but I know the analysis you gave was just for Pennsylvania, just on payroll, and the consequence of not doing it was I think 19,700 jobs. In 2011 we grew north of 50,000 jobs. A lot of states would be envious of that, not enough but it was a significant job growth for one year, and you would cut off roughly 20,000 of that kind of growth if you didn't get it done.

So having that number is very helpful. The other analysis that I referred to earlier is kind of the county-by-county impact for an individual worker. In a lot of counties in our State it works out to be a little bit more than $400 per worker just for the 10 months. In other words, the 10 months we don't have an agreement on yet.

That was true whether they're in a big city like Philadelphia, or a smaller county like Potter County, for example. They were both in the $400 range. So we will talk more about it as we go.

I am actually over time a little bit, and I will turn to our Vice Chair.

Dr. Zandi. I am amazed at your memory. You're sure it's 19,700?

Chairman Casey. Repetition helps me.

[Laughter.]

Vice Chairman Brady. It's like a steel trap with the Chairman, I'm telling you.

Because I was late, I would like to defer to Senator Lee for the first question.

Senator Lee. Thank you, Vice Chairman Brady, and Chairman Casey.

I intend to make just two quick points before I launch into questions because I am of course more interested in hearing from you. But the first point I wanted to make is, our Social Security tax is a tax. It is just like any other tax imposed by the Federal Government. In the sense that, although some of the proceeds from that tax are spent on today's retirees, none of that money that is saved, none of the excess is currently saved for the benefit of retirees.

It is spent through the General Fund just like all other revenue. And so Social Security is not a savings program, as it is commonly billed, and as it was intended to be. The mere fact that Congress has strayed so far from the original intent of Social Security is yet further evidence of Congress's lack of fiscal discipline over a rather prolonged period of time. And I think that is something that we need to consider as we evaluate our tax policy generally and as we evaluate our approach to Social Security.

Second, as several of you have mentioned today, economic research on Unemployment Insurance indicates that many recipients of UI tend to wait for their benefits to expire before going back to work. Therefore, this does seem to suggest that to some extent extending benefits can tend to lengthen the amount of time that many people are unemployed, actually increasing unemployment and, to that extent, reducing economic growth and even overall prosperity.

Consequently, I do worry that extending Unemployment Benefits might be harmful to the economy and might result in expanding dependence on an already bloated and already deeply indebted Federal Government.

This is not just a hypothetical concern. It is one that I think about from time to time, and especially in light of evidence suggesting that as long as we remain in a position in which our Federal debt to gross domestic product ratio is in excess of 90 percent—we're over 100 percent now—our economic growth is going to continue to take a hit.

So for us to fund programs that we cannot afford could tend to exacerbate that trend.

Mr. Sherk, I wanted to start with you and ask you if you are familiar with something that I am told has been introduced in the House, sometimes referred to as "The Spice Act," the Social Security Preservation Through Individual Choice Act, which would indefinitely extend in some circumstances the Payroll Tax Holiday, but do so on an opt-in basis, allowing every employee to make this determination on an annual basis, pushing back the retirement age by one month for every year that this partial holiday is extended.

Are you familiar with that proposal?

Mr. Sherk. I'm not, so it's not something I can comment on. It sounds like a good idea, but it's not something I have examined.

Senator Lee. Okay. But in theory it is something that you could support insofar as it expands individual choice, assuming it can be made actuarially sound?

Mr. Sherk. Based on what you have described, it certainly sounds like something I would support, but I would want to study it in detail before I would commit to that.

Senator Lee. Okay. I heard you mention that unemployed workers tend to triple the amount of time that they spend job hunting when their Unemployment Insurance Benefits are about to expire. Wouldn't that suggest then that extending them would reduce them by two-thirds, reduce the amount of time that they might otherwise be spending looking for jobs by two-thirds?

Mr. Sherk. This is research done by Alan Krueger, which he published shortly before he joined the Administration. Krueger examined Time-Use diaries that the Bureau of Labor Statistics produces and found that workers who don't have UI benefits have a fairly constant level of job search all throughout their time unemployed. But those who have UI benefits, have a lower level of job search in the months before their benefits run out, and then their job search triples in the last few months before their benefits start to run out.

There is very clearly a disincentive effect. There are some people who are clearly abusing the system who could get a job and don't. And a lot of people know stories of people who have done exactly that.

But I think a better way to think about it is that workers have in mind the kind of job they are looking for. In many cases, in the previous industry they were in before, which is what they are skilled in, or in the same city; often they want something near their old salary range. And so quite understandably that is what they initially look for when they are unemployed.

Now unfortunately about half the jobs lost in this recession were in manufacturing and construction. Those sectors are not going to recover to anything near what they were before. There's going to be some increase, but a lot of workers are going to have to move into different industries. A lot of workers are going to have to move to different states.

Having almost two years of benefits encourages workers to search for jobs that they are simply not going to find; no matter what the government does, the jobs that were created by the housing bubble are not going to come back. And it is ultimately not helpful for them if they spend a year searching for a job they cannot find, a year-and-a-half searching for that job, and then spend the rest of the time when their benefits expire looking for positions that they are more likely to find.

It is counterproductive in the long run, even if it is well intentioned.

Senator Lee. It does not mean they are abusing their benefits; it is just a natural consequence of what happens.

Mr. Sherk. Exactly. It is an understandable response, but it is not helpful to them.

Senator Lee. Thank you. I see my time has expired. Thank you, Mr. Chairman.

Chairman Casey. Thank you, Senator Lee. Representative Duffy.

Representative Duffy. I travel my District. I am in the northwest corridor of Wisconsin. I run into a lot of people who are going through some very difficult times, and they rely upon these benefits to make sure they can bridge that gap between their time of unemployment to the time of their next employment.

I think everyone on this panel, everyone in both chambers, agrees that when people fall on hard times we want to be able to help them out. And sometimes it may be several months, sometimes it may go up to 99 weeks.

I think many of our concerns are not about those who truly need the help, who have families, who have young children, and who need the help of this Unemployment Benefit; but it is those who abuse the program, who abuse the system, and who don't actually go out there and look for work. They eat up that benefit at a time when they could really find some other kind of employment.

The way we weigh and balance; to weed out the bad actors and provide the benefit to those who truly need the benefit; is, I think, the real issue that we struggle with in the two chambers.

I guess I would throw it to the panel as a whole. If we have an unemployed individual who is looking to get back in the market, I mean I think there are some reasonable steps that we can take to make sure they are aggressively trying to find work.

One is to verify, not through lax standards where we do the call-in, as I think Mr. Sherk indicated, but to actually verify that they are looking for work. And if they are looking for work but they cannot find it, that we encourage them to go get other job skills training so if they have to transition from one job skill to another they are going to have a skill set that can actually be used in this ever-changing economy.

And finally, we have talked about drug testing. I mean, I think this just makes sense. If you're using drugs and you're saying you're looking for work, I would call bogus on that. You're not going to get a job if you're doing drugs. There's too many people out there that are engaged, and good employees, and so that we would drug test those who are getting benefits I think makes sense.

And I guess Mr. Zandi, based on your research and study, I mean would you have any objection to these simple concepts being in place for those to receive Unemployment Benefits to go through these steps of work search and job training, and drug testing?

Dr. Zandi. Well I think it is important not to restrict UI Benefits to unemployed workers who have earned those benefits. I think that the principle that underpins the Unemployment Insurance System since it was founded in the Great Depression of the '30s was that if you work, and you pay an insurance premium while you're working, that if you lose your job you should receive a benefit, an insurance payout. And, that there should be no restrictions on that. That is what I get nervous about when we start talking about these things.

Drug testing, I'm not sure really matters. In the studies I've seen they show that that's not significant in areas where we've had drug testing. It is costly. Someone is going to have to pay for it.

Moreover——

Representative Duffy. But I'm sure you would have no objection to drug testing, though?

Dr. Zandi. One other thing I would say is, I don't know—we're here in an—in my view, what matters most is making sure that we get through this very trying time with an economy that is back on track, and I don't think we should muck it up now.

I am all for reform of the UI System. I think there are lots of things we should do. But that is one thing I don't think I would throw into the mix at this point in time.

Representative Duffy. But to regain my time here, when we're talking about a benefit that's been promised because it's insurance, that initial promise wasn't for 99 weeks, was it? The agreement was something other than 99 weeks? So if we're going to extend it beyond what you originally bargained for, is it then fair to say if we're going to give you more than what you bargained for it might be fair to ask for job search, job training, and drug testing?

Dr. Zandi. Yes, but I would say that, you know, in every recession since World War II, particularly severe recessions, we have provided benefits, emergency UI. That is part of the deal, in my view.

Representative Duffy. But to 99 weeks, have we?

Dr. Zandi. 99 weeks, given the severity of what we have gone through, the recession that we've been through, I would say that's part of the deal.

Representative Duffy. No, no, I'm saying going back to the Great Depression. 99 weeks?

Dr. Zandi. I think this is the first time we have gone up to 99 weeks.

Representative Duffy. And I guess——

Dr. Zandi. But——

Representative Duffy [continuing]. And as I switch gears, we go to this theory of a multiplier effect where every dollar spent will give us a return of $1.55, I think that same argument was made for the nearly trillion dollar stimulus package. And I think, as most Americans look at that, they will go: I don't think that that multiplier came into effect. We see the pain continue to grow, even though all those dollars rolled out the door.

And to make the same argument that it is going to now work for Unemployment Benefits, I think the American people will probably reject that. But I see my time is up and I yield back.

Dr. Zandi. Darn.

[Laughter.]

Representative Duffy. Maybe we will have a round two.

Chairman Casey. Thanks very much. Senator Klobuchar.

Senator Klobuchar. Well thank you. My time is not up. So thank you. I have heard most of your opening statements. I had to go for another meeting, and I am glad to be back.

Our State actually, when I was listening to Dr. Zandi about the fragile recovery, we have been ahead of the curve. We are down to 5.7 percent unemployment in Minnesota. And we have a major metropolitan area, and the rural has been very strong, as well. And it is this combination of innovation, exports which is huge in our State, which I think should be a good message for where we can go with the rest of the country.

But that being said, there are still a lot of people that can barely afford their mortgages and are having trouble hanging on. Maybe they have lost part of a job, and only have one, or they are working more jobs to make up for the money. And so that is why this Payroll Tax Cut is so meaningful to them.

And I know, Dr. Zandi, you wrote last fall that, quote, "Expiration of the Tax Holiday, Emergency Unemployment Benefits, and other stimulus efforts could shave up to 1.7 percentage points from Gross Domestic Product in 2012. These are expensive programs, but not extending them could be even more costly to taxpayers if the economy slips back into recession."

So, despite the recent signs that our economy is picking up steam, we know you still want to see this extended. And do you think we could still risk slipping back into recession, or at least not moving as far forward as we want to if we let all of this lapse?

Dr. Zandi. Yes, that is correct. You know, my sense is that if you do not extend these programs, the economy in all likelihood will make its way through without backtracking recession. But the odds are that we are far enough along in the recovery that that will occur.

But I think the risks are high that I am wrong, and that if anything else does go wrong—and of course there's a long list of things that can go wrong—we could easily be derailed again.

Senator Klobuchar. You mentioned Europe as one of those.

Dr. Zandi. Just as an example. The housing crisis as another example. And I would also point out that we are guarding against very dark scenarios.

So if we go back into a recession, the cost to taxpayers will be enormous. That would dwarf what we are talking about here. And, it will undermine what I consider to be some very significant progress in righting the wrongs that got us into this mess.

I feel like we have done a lot good—you have done a lot of good, and that this will shine through. But that will not happen if we backtrack into a recession.

Senator Klobuchar. And I know that Senator Casey is on the Conference Committee in the group, and so is Congressman Brady, working on this. Do you have any thoughts on how this should be paid for, these three major programs, plus perhaps some tax extenders?

Dr. Zandi. Well of course that's why you get paid the big bucks. [Laughter.]

Senator Klobuchar. Right. I just thought I'd ask you.

Dr. Zandi. I'll give you my sense of it. My view would be that the cost should be included in the spending cuts that would be part of the sequestration process going forward; that that is going to be done over a 10-year period. The impact of that can be smoothed over time.

In that way we do not get bogged down in some other ways of paying for this that could be counterproductive, as in the case of paying for this last two months. In my view, that was not very productive, and is in fact counterproductive. So I think I would go down that kind of a path.

Senator Klobuchar. And to follow up on your last comment there, just the cost of brinkmanship that you've seen, the debt ceiling issue this summer, as well as what happened at the end of the year, when you look at it as an economist in terms of the consumer confidence, which is an incredibly important factor here, that is hard to measure, as well as the effect of really our reputation in other countries and across the world in terms of people wanting to make investment in our country, and business as well.

Dr. Zandi. Yes. That is an excellent point. Now of course it is very difficult to quantify these things, but again my sense is that the political acrimony that was exhibited last year relating close to the government shutdown in the Spring, and then the debt ceiling spectacle, that that did undermine confidence significantly. It caused already shellshocked households and businesses to pull back.

If you think back to that time in August-September, we did come very close to recession. The other thing I will say is that I have no inside information here. I'm part of Moody's Analytics, not part of Moody's Rating Agency, but just listening to what they say, and observing how they are thinking, if we go down that path again it's not going to be just one rating agency that potentially downgrades, it could be others.

So again, I have no inside information. I am just forecasting what I am hearing. But I think we should be cognizant of that, and that could have significant ramifications.

Senator Klobuchar. I remember having lunch with Bob Ulrich, who is a former CEO of Target. He retired, and it was during the McCain/Obama race, and he was saying, he just said, "I want these negative ads to end." And I figured it was because he was weighing in—I think he was supporting Senator McCain, but I said, what do you mean? And he just said: "It's so bad for consumer confidence. No one wants to buy anything."

And I think that I have always thought about that in terms of the much bigger picture, not just negative ads but what is going on when we go to this brinkmanship, what we do to our country when we do that. And it is just my hope, I will say it to all the panel members, that that just can't happen again with this work that is being done on the Payroll Taxes and other things. We just cannot afford to do it again. We have major decisions to make, but I would like to get through this and then go on to the much bigger issue of tax reform after that, which I think there's been some reference to that that could be very helpful.

So thank you very much.

Dr. Zandi. That makes a lot of sense, yes.

Chairman Casey. Thanks, Senator Klobuchar. Congressman Mulvaney.

Representative Mulvaney. I will preface these comments by saying I agree with the lady from Minnesota regarding the undesirability of brinkmanship, and the Senate is more than welcome to take up and pass our Cut, Cap, and Balance bill from last year. That would end a lot of this discussion.

But anyway, I will return to Unemployment Insurance for a second, because I hear what Dr. Zandi says about what matters most is that we get through these trying times, and I tend to agree with that, but I also hope that we get through them in such a fashion that it does not bankrupt the States.

In looking through Commissioner Everson's testimony, I see that Indiana's circumstance is only slightly worse than ours in South Carolina. We have gone from a six or eight hundred million surplus in the beginning of this decade to owing the Federal Government almost $800 million. At one point, a five or six trillion—excuse me, billion dollar swing. You've been here too long now. "Trillion" comes out of my mouth too easily.

So I want to press you, Ms. Conti, specifically on what's wrong with drug testing? What's wrong with looking at that as a reasonable way to cut costs and, more importantly perhaps, to make sure that this benefit is going to those truly in need and not to those who are taking advantage of the system?

Ms. Conti. Sir, I think what I would say by introduction is: It is a solution in search of a problem. There is no evidence, statistical or otherwise, to show that there is any sort of broad-based epidemic, or even significant drug use among the people who are receiving Unemployment Insurance today.

Twenty States in their UI law already provide that if you lose your job because of some sort of drug abuse—either you are using drugs on the job, you are intoxicated on the job, you fail a drug test—you are ineligible for Unemployment Insurance. The vast——

Representative Mulvaney. Okay, how many states?

Ms. Conti. There are 20 States that have it explicitly in law——

Representative Mulvaney. It's not 50?

Ms. Conti. Let me finish.

Representative Mulvaney. Okay.

Ms. Conti. The vast majority of other States have that exact same prohibition in case law that has developed around the law of misconduct. If you lose a job because of misconduct, you are generally disqualified from receiving Unemployment Insurance as well—misconduct or gross misconduct.

Representative Mulvaney. But you are talking about something else, which is drug use on the job and the reason for the discharge, which——

Ms. Conti. Or, or failing—or failing a drug test, even if you were not using drugs on the job.

Representative Mulvaney. I am talking about as a prerequisite to receive the entitlement. Not what got you fired——

Ms. Conti. Right.

Representative Mulvaney [continuing]. But what is related to your receiving a benefit.

Ms. Conti. But I'm saying there's—within the UI System there is already adequate protection against it. I would also point to some recent——

Representative Mulvaney. Let me stop you there. Let me stop you, because you are answering a different question. I didn't ask you if there was adequate protection for folks who get fired because they're using drugs. I'm talking about the entitlement.

Ms. Conti. Right.

Representative Mulvaney. What is wrong with asking people to take a drug test before they actually get their Unemployment Insurance check?

Ms. Conti. Well first of all there is no evidence that it is a problem, in the first instance, that there are all of these drug users getting Unemployment. It is an unfair and mean-spirited, we believe, stigmatization of people who are unemployed through no fault of their own. It is the bad economy that is prohibiting them from getting jobs; it is not drug use.

And we can look to some recent examples. I would point to Indiana in general that just started—or just recently last year conducted a pilot program. It was testing people who were getting job training, who are people by definition who are either unemployed or under-employed and want to better themselves, to the tune of $45,000. I believe they tested about 13,000 workers, and 13 tested positive.

That was $3,500 per worker. Whereas, that money could have been spent, we believe, much more productively on high-impact re-employment services for the workers——

Representative Mulvaney. But if a state wants——

Ms. Conti [continuing]. That would get more people into jobs, which is what we say we all want to use the UI System to do.

Mr. Everson. Could I comment on that, since Indiana has been drawn into this?

Representative Mulvaney. Sure.

Mr. Everson. When I got to my job two years ago, I toured the State and I was repeatedly told: Mark, you guys do a great job—We run the Unemployment Insurance System and the Worker Training System—But you keep sending us people who, when we tell them you're going to have to take a drug test, they say "thank you very much, and good bye."

And what I did was, I went back to my office and I said: What can we do about this? In the WIA, the program that is the enabling statute for the biggest training program, it said specifically, since '98, that no DOL could not prohibit any state Workforce System from having a drug test. And I checked into this, and we did it.

And our rate, our failure rate since July 1 when we put it in, is 2.2 percent. 2.2 percent. That compares to about 3 percent in the private sector, which is the failure rate for pre-employment drug screening. Most people do not show up when they are going to take a drug test if they are using drugs.

Representative Mulvaney. That is to say, isn't there a deterrent effect?

Mr. Everson. That's the point. And that's the point.

Representative Mulvaney. Once a State starts to do this, Ms. Conti, don't you think it will deter people from either doing drugs in the first place, or showing up to collect their benefits if they know they are going to be tested?

Ms. Conti. It could equally encourage people to find out how to do the proper type of fasting and cleansing processes for three to seven days before they have to take the drug test in order to beat the test.

Again, we are assuming that there's some sort of widespread problem among those receiving Unemployment, that they're not getting jobs because they are using drugs.

Representative Mulvaney. No, I'm not. I can see how you might think that. I am assuming that the State knows best how to implement its own Unemployment Insurance Program. My guess is you probably have not talked to many employers in Indiana—neither have I—and there may not be a difficulty in North Dakota. There may be a difficulty in Florida. And I am simply suggesting that the States are more effective at doing that, but I will continue this line of questioning next time around.

Chairman Casey. Thank you very much. Vice Chairman Brady.

Vice Chairman Brady. Thank you, Chairman. And again, thank you to the witnesses and the Members who are here today.

Will you put up that poster on Social Security? It is important we extend these benefits, that we do it now; that we not have another two-month extension. That was a disaster, in my view, for businesses, workers, and our local physicians.

One of the big issues that Chairman Casey and I are dealing with is how you pay for these costs. These are real costs, more than $100 billion at a time we cannot afford it. And the one point I want to make today is: The Payroll Tax Holiday alone blows a significant hole in the cash flow of Social Security. And if we do nothing else with that important program, it is critical that we fill that hole back up with real cost savings.

Again, we are not talking about the Trust Fund for Social Security. We are not adding. We are not running surpluses. We are running deficits and borrowing extensively. It is important we fill the sinkhole now, this year. And certainly it is clear that extending the Payroll Tax Holiday further would have dramatic impacts on Social Security.

I want to talk about the unemployment reforms. I am just not convinced we run unemployment very well at the Federal level. Our focus is on getting those checks out for extended periods of time and not getting people back to work.

One of the requirements that we are suggesting in the House is focused on those with the least education, those without a high school degree. We know they struggle to find a job.

One of the points Ms. Conti made, which others have made, is that, look, some people, older workers, requiring them to get a GED as a condition of receiving Unemployment does not make sense. Everyone agrees with that. But how old is too old?

A recent Census Bureau report looking at the one-half million people without a high school diploma, without a job today, 1 in 5 were under the age of 30, very young; 2 in 5 are under the age of 40. So, with my math, high-level math, 3 out of 5 are under 40 years old, have at least a quarter century of work time left in which a high school equivalent degree would put them in a better position.

So, Ms. Conti, you are one of those who thinks we ought not be encouraging States to help these people work toward a GED. Why is that? You don't think they will be in a better position?

Ms. Conti. No, I think you have actually misstated my position rather substantially. At the National Employment Law Project we are huge proponents of lifelong learning, of federally and state subsidized job training at all levels, whether it is GED or other sorts of occupational training; and we believe that workers of any age—nobody is ever too old to learn more skills and to get more knowledge.

Vice Chairman Brady. So you would support that provision?

Ms. Conti. We don't support that provision, but you stated that we don't support workers getting more education, getting their GEDs, and that is not correct.

Vice Chairman Brady. So you support people getting more education, but you oppose helping unemployed work toward a GED——

Ms. Conti. We support helping the unemployed work toward a GED through appropriate means. We do not believe that the UI Benefit should be conditioned on getting or enrolling in a GED program; rather, we support something that I believe the Senate Conferees have put out. The notion of putting some additional funds into re-employment and training services, and giving workers appropriate re-employment assessments. And if through that part of the employment services, not as, you know, sort of the stick over the head, you won't get UI if you don't get it, but through appropriate re-employment assessments——

Vice Chairman Brady. I think we just have a disagreement on how——

Ms. Conti. We do. Could I finish my statement, sir?

Vice Chairman Brady. No. You answered it beautifully and I appreciate it.

Let me go to job search. I would think most people are searching aggressively from day one when they don't have a job. Unfortunately, not all do. A recent report in The New York Times now, since 2009, show that the average unemployed in America spend about 30 minutes per day looking for work, and 1 in 6 unemployed people look for work on a typical day.

What we know is those who aggressively job search usually find a job sooner than others. Can I ask you, Commissioner Everson, do you have a job search requirement in your State Unemployment Benefits?

Mr. Everson. Yes, sir, we do.

Vice Chairman Brady. And would you recommend that at the Federal level we do the same, as well, since obviously your Unemployment Taxes don't pay for all your benefits; others chip in to do that. You would think that would be sort of a responsible reform to enact.

Mr. Everson. I believe that job search, you want to certainly emphasize it. I agree with that a hundred percent. But I think that the traditional way the system has worked, with the States determining what is best in their circumstances, is an important principle. And the States do vary what they want to do.

What I don't want to see happen is, like the nonreduction rule, is that you look at these occasional extensions, and we are in this period of extension now——

Vice Chairman Brady. Yes.

Mr. Everson [continuing]. And you force back changes into the core program which runs pretty well and has served us well for seven decades. The problem being, again, you are seeing right now that States have already cut the benefit duration from 26 weeks to 20 weeks—a number of them have done it—because of they can't go through the nonreduction rule.

So I just think it can have unintended consequences when you have the Federal mandates. But I do agree, you need enhanced work search.

If I can make just one additional point, because it keeps coming up, the duration and lack of effort that's talked about. There is a public policy tension here. There is no doubt—I am not going to comment on the stimulative effect of the benefits—but there is no doubt we have in Indiana tens of thousands of people who benefit from these extensions. That is absolutely clear.

But there is another factor that has not been touched upon. Clearly individuals make a decision every day not to take a job if it's paying $15 and they were making $20 in their old job. If they look at the economics of it, and they say, geese, my spouse is working so I've got health care. And I am avoiding child care costs. And, they say, I am going to wait until that better job comes along.

It is just, as my colleague on the panel said, that is a good short-term decision for the individual, but it is a bad long-term decision for him or her because employers are increasingly skeptical about people who have been out of work for a year, or 18 months, or 2 years. That is just a consequence we have not touched on here that is real.

Vice Chairman Brady. Thanks, Commissioner. And I apologize, I went way over my time, but thank you.

Chairman Casey. Thanks, Commissioner. Thanks, Vice Chairman Brady. Congresswoman Maloney.

Representative Maloney. I want to thank the Chairman for calling this hearing. And since we have one of the most respected economists here, I would like to ask Dr. Zandi your reaction to the recent jobs numbers: 253,000 new private-sector jobs created. I believe that is the 23rd month of job growth, and a very positive unemployment. After five consecutive months, the rate has been coming down, reaching 8.3 percent in January.

We had an interesting hearing on Friday from the Bureau of Labor Statistics. They said that the recent decline in the unemployment rate was driven by unemployed workers finding jobs, which is a very positive sign.

I wish you would just give us an overview of where the economy is. Is this a positive sign? Do you see this as a trend that will continue? What do we need to keep this positive jobs' situation moving forward?

Dr. Zandi. Well thank you for the very kind words. They are much appreciated. Too bad we're not on TV so my wife could hear that.

[Laughter.]

Or better yet, my kids. That would even be better.

I think we've made a lot of progress. The economy is improving, and that is evident in lots of different ways, but most encouraging in the job market. As you pointed out, almost 250,000 payroll jobs in January; 2 million jobs over the past year through January.

As you point out, the decline in unemployment is real. It is not a declining labor force; it is an increase in jobs. The job increase is broad-based across industries and regions. So I don't want to go so far as saying that we're off and running, you know, because we have had some head fakes before. This time last year, we were feeling good about things and we got nailed by higher energy prices, and surging food and apparel prices, and a lot of other things.

But it feels like we are getting very close to that light switch going on; that businesses I am in economic consulting with business, and I talk to a lot of business people in lots of different walks of life. Just talking to them in traveling the country recently, you get the sense that they are at a point where they are about ready to engage and look for growth and revenue opportunity, and that means more investment and more hiring.

So I think we have made a lot of progress, but we are really close to evolving into the economy evolving into a self-sustaining strong economic expansion.

That is why I think it is so important to extend the Payroll Tax Holiday/Emergency UI to make absolutely, positively sure that that is in fact what is happening here.

Representative Maloney. So you think that is important, to continue the Payroll Tax Cut for 260 million working Americans?

Dr. Zandi. I think it is absolutely vital. I think we do not want to take the chance that we let that lapse, and that we get derailed. Because if we do, the cost to taxpayers will be measurably more significant than the money that we are talking about here.

So I view this as an insurance policy to make sure that the economy is indeed off and running.

Representative Maloney. Well also a part that President Obama is working hard on in a bipartisan way is to extend the Unemployment Benefits. As a gentleman pointed out, Commissioner Everson and others there, the jobs are not out there. For every job, how many people do you think line up for it? Six? Seven? How many people are there for every job? So through no fault of their own, they are out of work.

So is that also an important component to keep this economy moving, the Unemployment Benefits? Because that will go back into the economy.

Dr. Zandi. Yes. So I would advocate extending both the Payroll Tax Holiday and the Emergency UI Program at least through the end of the year. And the statistic that I think is—we have not brought up at the hearing yet, but I think is very important is the fact that for every job opening, there are now four unemployed workers.

Just to give you context, in a normal, well-functioning labor market, that should be closer to two to one. So for every unemployed worker—for every job opening there should be two unemployed workers.

At the worst of the Recession it was six to one. But four to one is still very high. And we have been talking about disincentive effects and other issues, but we just need to remind ourselves that the predominant reason why people are looking so long for a job is because there aren't jobs. It is hard to find a job.

Representative Maloney. Coming in, Ms. Conti was mentioning the GED and getting those degrees. I would like to ask you, what jobs do you think are out there in the future? And do you think having a GED degree is important to get those jobs?

Dr. Zandi. Yes. I think the jobs we are going to create in the United States of America will embody a highly skilled and educated workforce; that that is our Nation's comparative advantage: producing goods and services that embody the skills and educational attainment of our population.

So we need to work really hard at raising everyone's educational attainment level, particularly people who don't have good skills or lack at least a high school degree, because they are going to get creamed by the global world that we live in and the competition that we are in.

So it is very important to spend resources to educate these folks, give them the training they need, and help them gain the skill set that they need to compete.

Representative Maloney. Are you still the economist for Moody's?

Dr. Zandi. I am, for Moody's Analytics, which is the independent subsidiary of the Moody's Corporation. So I am not part of the rating agency, but I am the Chief Economist of Moody's Analytics.

Representative Maloney. I must say, I always listen to you because you work for the private sector. And if you're wrong, you're going to get fired.

[Laughter.]

So I know you are going to be very careful in what you say. Anyway, we appreciate——

Dr. Zandi. You are very kind.

Representative Maloney [continuing]. All your hard work, and we appreciate everybody's testimony. And we have been called to a vote, so I've got to go. Bye-bye.

Dr. Zandi. Thank you.

Chairman Casey. Congresswoman, thank you very much.

I will move to a very brief—I won't call it a second round, we will call it a lightening round. There is a lot we could do. We could even start a great debate right at that table there, but we probably do not have time for it today. You can stay if you would like, but we are grateful to all of our witnesses.

Just one point I wanted to make, Mr. Conti, regarding your testimony. I do not have a lot of time, but maybe even not by way of a comment, but if there is something you want to add to this:

On page 3 onto page 4 of your testimony, you talk about the impact on children, Unemployment Insurance's impact on children. And I was struck by the sentence at the top of page 4, and I'm quoting, " . . . , the federal investment in unemployment benefits has an immediate payoff for those kept out of poverty, but it also produces long-term dividends for children and families given the social costs associated with child poverty and severe economic hardship. Children who experience economic hardship are more likely to drop out of school, suffer poor health, and experience difficulty maintaining stable employment as adults." Unquote.

Ms. Conti. Um-hmm.

Chairman Casey. I want to ask you, and it may be by way of repetition, but you had a number that you attached to that in terms of the number of children prevented from poverty. What was that number?

Ms. Conti. The recent Census showed us that in the year 2010 over 1 million children were kept out of poverty because their parents were receiving UI Benefits.

Chairman Casey. Just for that one year?

Ms. Conti. Right. And the number was about the same the previous year.

Chairman Casey. That is the latest year we have data for?

Ms. Conti. Yes.

Chairman Casey. Thanks very much. Congressman, do you have something before we go?

Representative Mulvaney. Very briefly, because I spent more time than I intended to with Ms. Conti. I enjoyed the conversation, but I did want to come to Dr. Zandi, and it follows up on what the Congresswoman was just talking about on job growth and how—"disappointed," Dr. Zandi, is not the right word, but I guess I am skeptical about your commentary.

Your testimony reads that the recent rapid drop in unemployment rate is real, resulting primarily from more jobs and not a declining labor force. And actually you go to the extent of footnoting that by pointing out that since August the unemployment rate has fallen to 8.3. During this period, the BLS has recorded an employment increase of 1.9 million jobs and a gain of more than 700,000 people in the labor force. And you use this as evidence, I guess, to support the previous assertion that these are real job growths.

Yet, sir, during the same period of time the labor force participation rate has fallen. Last month it went from 64 percent to 63.7. The number of discouraged workers is up last month. The number of other marginally attached, U–5 unemployment, is up last month. The number of U–6, part-time for economic reasons, is up. The unemployment by the widest measure is up. The total number of long-term is up. And I guess at a certain point I have to wonder, how do you back up that statement, that these are real jobs because the labor force is growing?

It seems to me that the labor force did go up, sir, but not as fast as it should have, given the population growth. That even if your number of jobs goes up, if your participation rate in the job pool—in the workforce goes down, that clearly we are not keeping up with population growth, and the numbers are effectively cooked.

The 8.3 percent number that we saw last number is not a real number. How do you respond to that?

Dr. Zandi. Well a couple of things.

When I cautioned your use of the data, the decline in the labor force participation rate in January is a statistical result. It is new population controls by Census. They go back and revise the data and they put all the revisions in January.

Representative Mulvaney. But I think they said that was only one-tenth of one percent at the hearing we had on Friday last week.

Dr. Zandi. I think by my calculation the labor force participation rate, from August of last year through January of this year, has been essentially constant, no change.

Representative Mulvaney. Okay. Well it leads to the same question, though. If your labor force participation rate is unchanged——

Dr. Zandi. Right.

Representative Mulvaney [continuing]. But you are having more people in the workforce, how do you make the assertion that this is real job growth? If you're not growing fast enough to give people who come out of college and out of high school and out of the vocational schools jobs?

Dr. Zandi. Right. Well I'll say two other things.

First is the increase in the labor force since August is 700,000. That is the Household Survey.

Representative Mulvaney. Right.

Dr. Zandi. That is what you would expect to see in a reasonably normal, well-functioning economy, about 700K in that five-month period, because that on an annualized basis results in 1.5 million labor force growth, which would be normal labor force growth in a good economy.

Representative Mulvaney. But not in an economy that is coming out of a recession. We should be growing faster than that on an average basis, right?

Dr. Zandi. Well you make a good point. I think there will be some point down the road when the labor market gets to a point where it's really healthy, unemployment has fallen some more and we start to——

Representative Mulvaney. 700,000 jobs over five months is one hundred and twenty-odd thousand jobs a month, and I think the break-even number we have been told by BLS is we need 125- to 150,000 jobs a month just to keep up with the population growth.

Dr. Zandi. Well let's not confuse things. We actually created 1.9 million jobs, household jobs, in that period; 700K labor force. So 1.9 million. That is a lot of jobs. That is boom times. We are not going to sustain it. I am not arguing that. But if we could, that would be fantastic. But I am not arguing that.

But to your point, I do think there are a lot of people who have stepped out of the workforce. They are not counted as unemployed. They feel disenfranchised. They don't feel like there is job opportunity, and wage growth has been so weak, to the Commissioner's point, they don't feel like it is worth coming back into the labor market. I've got child care, I've got gasoline prices, I've got commuting costs. But at some point when the job market does improve, unemployment becomes low enough and we get a little bit of wage growth, those folks are going to start coming in and the labor force growth will pick up a lot more. And it is going to be harder to make progress in reducing unemployment.

Representative Mulvaney. And this is my last question, because I just want to make sure I am reading this correctly. Your testimony says that you think unemployment might be below 8 percent by the end of 2012.

We just heard from the CBO last week, they are actually revising up their unemployment rates over that same period of time. They originally thought it would be about 8.2 percent; now they are up to 8.9.

And I am led to believe that when you participate in the Blue Chip Analysis last month you yourself had suggested it might be 8.8 percent at the end of this year.

Dr. Zandi. Yes.

Representative Mulvaney. Up from 8.3 percent in a previous estimate that you made, and that is a fairly dramatic change in a month, if I got my data right. Last month you thought it would be 8.8 at the end of this year, and now you think it might be below 8. That is a significant change. What caused that?

Dr. Zandi. You are absolutely right. And I think CBO, like all the economists, including CBO, when they do their forecasting will be marking down their forecasts for the unemployment rate. So my guess is, the consensus view now——

Representative Mulvaney. They're making it up, sir.

Dr. Zandi. No, but they will mark it down. They're lagging. They're going to mark it down. Given what's happened to the economy and to the unemployment rate. We are now at 8.3 percent unemployment. Everybody is going to be marking down their expectations for the unemployment rate. When you get next month's consensus, it is going to be at year-end probably 8.2, 8.3.

Representative Mulvaney. What has happened in the last 30 days to change that, then?

Dr. Zandi. The very dramatic improvement in the job market, and revisions to past data. So we have now a better sense of what has actually happened.

I think there is a growing understanding of what is going on with the labor force. I think the views with respect to the growth of the labor force are changing so that people now think the labor force is now going to actually be slower than originally thought over the next year or two.

Representative Mulvaney. Thank you, Mr. Chairman. Thank you for your leniency. I apologize for going over in the lightening round.

Chairman Casey. Congressman, thanks so much.

Dr. Zandi, thank you. Mr. Everson, thank you for being with us today. Mr. Sherk. Ms. Conti.

Before we go, let me just say, I think from this hearing and the testimony that has been offered, one bipartisan note, we need to extend the Payroll Tax Cut and Unemployment Insurance Benefits through the end of 2012.

I believe this is essential for an economic recovery that is still fragile. I am confident, and I think others are as well, but I will speak for myself, that the Conference Committee will be able to fashion a bipartisan agreement to get this done that will help both the economy and our families.

Just so the witnesses and the Members know, the record will remain open for five business days for any Member who wishes to submit a statement or additional questions.

And with that, our hearing is adjourned.

[Whereupon, at 4:06 p.m., Tuesday, January 7, 2012, the hearing was adjourned.]

SUBMISSIONS FOR THE RECORD

Written Testimony of Mark Zandi
Chief Economist and Co-Founder, Moody's Analytics

Before the Joint Economic Committee

"Bolstering the Economy: Helping American Families by Reauthorizing the Payroll Tax Cut and UI Benefits"

February 7, 2012

The U.S. economy is improving. Manufacturing is strengthening, construction has turned the corner, vehicle sales are posting healthy gains, and, most importantly, the job market is gaining traction. Two million payroll jobs were added on net during the past year, and the unemployment rate is falling quickly. A self-sustaining economic expansion appears to be finally taking hold.

Yet it is premature to conclude that the economy is off and running. The economy was performing similarly at this time last year, only to be derailed by a surge in oil and other commodity prices, the Japanese earthquake, the European sovereign debt crisis, and political brinksmanship around the Treasury's debt ceiling.[1] The collective psyche remains fragile; it would not take much to unnerve households and businesses once again, thwarting the economy's full revival.

The immediate threats are familiar. Europe's economic problems, while less pressing given recent aggressive action by the European Central Bank, remain significant. The U.S. foreclosure crisis is pulling house prices lower, adding pressure on stretched homeowners, on small businesses looking for credit, and on local governments struggling to fund schools and other important services. A further risk is another misstep by U.S. policymakers, who will soon face a significant test over extending the current payroll tax holiday and the emergency unemployment insurance program.

Missing link

The missing link in the current economic recovery has been businesses' reluctance to step up hiring. Firms have done an excellent job of reducing costs, increasing profitability, and restructuring their balance sheets. While larger companies are in better shape than smaller ones, in aggregate, the financial condition of American businesses is arguably as good as it has ever been. Across nearly every industry, profits are at record highs and cash has never been more abundant.

Their healthy finances have enabled businesses to increase investment and curtail layoffs. Equipment and software purchases have been sturdy, and layoff rates have never been lower. Unfortunately, the rate of hiring has also been moribund (see Chart 1). The pace of new business formation has been exceptionally weak, and existing businesses have lacked the confidence necessary to expand and add workers. The nightmare of the

Great Recession still conditions their thinking, and uncertainty about changes in the regulatory and legal environment has not helped.

Chart 1: Hiring May Be Coming Back to Life

Number of monthly hires ex census, ths, SA

Sources: BLS, Moody's Analytics

The recent jobs data may be signaling that businesses are finally getting their groove back. Discounting the effects of mild winter weather and other technical factors, payrolls appear to be adding close to 200,000 jobs per month. Moreover, the job gains are increasingly broad-based across industries, occupations, and regions of the country. Employment as measured by the household survey—the basis for the calculation of the unemployment rate—has grown even more strongly in recent months. The household survey is better at picking up employment at new and smaller establishments, particularly at turning points in the business cycle. All of this is consistent with faster hiring.

The real thing

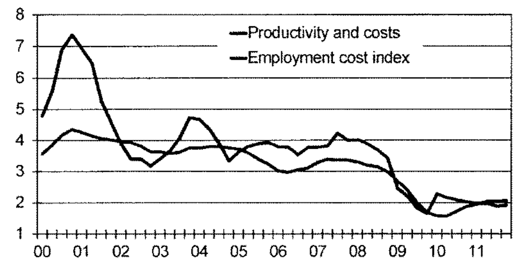
The recent rapid drop in the unemployment rate is thus real, resulting primarily from more jobs and not from a declining labor force.[ii] It would not be particularly encouraging if unemployment had declined because discouraged workers were leaving the workforce or if those who had left the job market earlier felt it was still too tough to come back. But this is not the case, because the unemployment rate has declined even as the labor force showed a meaningful increase.

Nonetheless, labor force growth is likely to remain soft in coming months, suggesting that even with only modest job growth, the unemployment rate will fall further and more quickly. An unemployment rate below 8% by the end of 2012 and closer to 7% by the end of 2013 now appears possible.

Not until unemployment falls meaningfully below 7% will wage growth pick up enough to draw more potential workers back into the labor force. Supply and demand conditions in the labor market have kept annual compensation growth stuck close to 2% since the Great Recession (see Chart 2).[iii] This is at best keeping pace with inflation. For many households, a job may not make financial sense, given commuting and child care costs. This may be why female labor force participation rates are declining while male participation rates have held up recently.

Chart 2: Compensation Barely Keeps Pace With Inflation

% change yr ago, 4-qtr MA



Sources: BLS, Moody's Analytics

Low after-inflation wages may also help explain unusually weak growth in foreign immigration, historically a vital source of U.S. labor force growth. Stiffer border controls and enforcement of immigration laws are likely also contributing, but many potential immigrants probably believe that their chance of finding an adequately paying job in the U.S. is too low to make the costly trek.

European turmoil

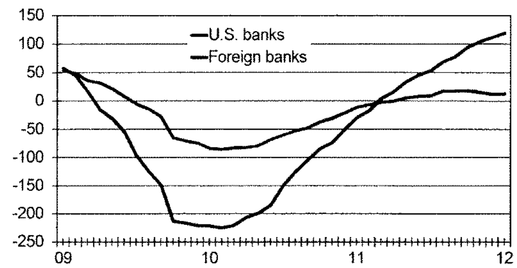
While the economy began 2012 on a more solid footing, it remains vulnerable, facing many serious threats. The ongoing European sovereign debt crisis is especially worrisome. Europe is in recession; and while the U.S. economy can tolerate a mild and short European downturn, anything more severe would be difficult to shrug off. The severity of Europe's recession depends on policymakers there.

Events in Europe affect the U.S. economy most immediately through the stock market. Movements in U.S. share prices have been closely tied to Europe's crisis since it erupted in early 2010. This is not surprising; U.S. multinationals are deeply involved in Europe, as they are across the globe. Although stock values are little changed over the past two years, prices have swung up and down in the interim. Wealthier U.S. households have had difficulty determining their net worth, which weighs on their willingness to spend. Such spending counts for a lot; households in the top 20% of the income distribution are responsible for almost 60% of consumer purchasing.

Europe's crisis may also impair the availability of credit, putting pressure on financial systems on both sides of the Atlantic. European banks make approximately a fifth of all U.S. commercial and industrial loans and are tied to big U.S. banks through a number of business channels. According to the Federal Reserve, foreign banks have tightened their commercial and industrial lending standards, and their volumes of outstanding loans have begun to decline (see Chart 3). U.S. banks have been able to fill the void so far, but this deserves close attention.

Chart 3: European Banks Pull-Back

Yr-over-yr change in C&I loans at foreign banks, $ bil



Source: Federal Reserve Board

A European recession will further weaken global trade, hurting U.S. export growth. One-fourth of U.S. exports go to Europe, but exports to the rest of the world are hurting as well, as all economies struggle with the effects of Europe's downturn. Asia seems particularly vulnerable. Exacerbating this threat is a rising U.S. dollar. The greenback has strengthened significantly against the euro since the summer and is also up strongly against the currencies of most emerging economies. Even the Chinese yuan appears to have slowed its appreciation against the dollar.

Europe's downturn is expected to be mild, lasting through the middle of 2012, with real GDP in the euro zone falling no more than 1%. However, this depends on how quickly policymakers can stabilize financial markets. It is encouraging that the European Central Bank has teamed up with the Federal Reserve and other key central banks to provide cheap funds to the stressed banking system. The ECB is also providing longer-term financing and easing collateral requirements for banks seeking loans. To the relief of financial markets, this signals clearly that monetary policymakers will not allow a major bank to fail because of a lack of liquidity.

Financial markets should also be cheered by the increasing commitment of European policymakers to fiscal discipline. The most profligate nations have replaced their governments and appear to be implementing serious austerity programs. Collectively, European Union governments have agreed to stiffer fiscal rules, more stringent oversight, and harsher penalties for violations. Officials also say they will enlarge the European bailout fund and the International Monetary Fund to help fiscally troubled governments. This should allow the ECB to continue buying enough debt to keep these governments' borrowing costs from spiraling out of control.

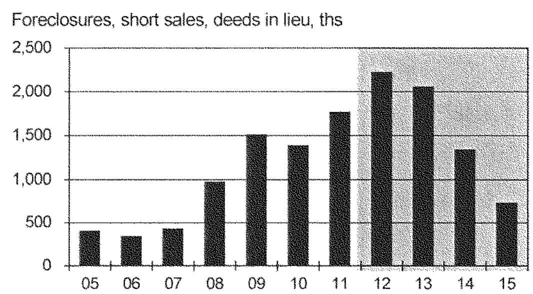
Nonetheless, it is not hard to construct darker scenarios in which Europe loses the political will to keep the euro zone together in its current form, and its economy enters a deep downturn, with serious repercussions for the U.S.

Falling house prices

The six-year housing crash is easing, but it is not over, and it remains a problem for the economy. Home sales and construction have hit bottom, and multifamily construction is picking up, but prices continue to slump. Average nationwide prices are down by about a third from their peak, falling almost 4% in 2011, and have further to go before they turn upward.

Behind this pessimism is the expectation that the share of distress sales, including foreclosures and short sales, will increase this year (see Chart 4). Distress sales occur at a large price discount; as they grow in proportion to the overall housing market, prices decline. The volume of distress sales was constrained last year because of the robo-signing scandal and other foreclosure process issues, which prompted regulatory and legal action against large mortgage servicers. The largest of these still outstanding is a suit filed by state attorneys general against the servicers. Once it is settled—most likely early this year—the foreclosure process will ramp up again, the number of distress sales will rise, and house prices will fall further.

Chart 4: More Distress Sales, More House Price Declines



Sources: FDIC, Equifax, RealtyTrac, Moody's Analytics

Prices are expected to fall only modestly from here, another 5% at most. Limiting the downside is sturdy investor demand for distressed properties; prices have fallen enough and rents are strong enough for investors to cover their costs while they wait for markets to firm. Unlike the house flippers who infected the market during the housing bubble, today's investors have longer horizons. Prices for nondistressed properties are also holding up well, suggesting the market for these has its own separate dynamic.

Nonetheless, the economy's prospects remain questionable as long as house prices are falling. A house remains the most important asset for most middle-income Americans; small business owners tap home equity for seed money and collateral, and property taxes fund most local governments. Most worrisome is the chance of another vicious cycle in house prices, similar to that during the depths of the Great Recession: As prices fell, more homeowners were pushed under water, producing more mortgage defaults, foreclosures and distress sales, and thus more price declines. With nearly 15 million home loans estimated to be under water, this is a serious threat.[iv] Worse, policymakers are unlikely to respond to a new downturn, given the lack of funds and political will.

Payroll tax holiday and UI

The U.S. economy's performance also depends on what Congress and the administration do about the temporary 2% payroll tax cut and emergency unemployment insurance program. Policymakers bought time late in December when they agreed to extend these programs through February, and an extension through the rest of 2012 is widely expected and necessary. Extending the payroll tax holiday through the remainder of 2012 will put approximately $100 billion in workers' pockets, while extending the emergency UI program will provide $45 billion to the unemployed. Together, the benefit of these programs to American households is equal to almost 1% of GDP.

The near-term bang for the buck—the additional economic activity generated within one year of the temporary tax cut and spending increase—is also meaningful. There was arguably no more effective form of government support during the recession than the emergency UI benefits provided to workers (see Table).[v] Emergency UI provides an especially large economic boost, as financially stressed unemployed workers spend any benefits they receive quickly. With few other resources, UI benefits are spent and not saved. The multiplier from a payroll tax cut, while sizable, is smaller since some of the benefit is saved or not spent quickly, particularly the portion going to higher-income households. More detailed analysis of spending by consumers indicates that approximately two-thirds of the tax cut is spent within six months.[vi]

The importance of extending the payroll tax holiday and emergency UI program is evident in the support these measures provided to the economy in 2011. Given the decline in the personal saving rate last year—from closer to 5% in January to 4% by year's end—it is clear that the bulk of the tax cut and increase in UI was spent. Indeed, the money not collected in payroll taxes last year largely covered the surge in gasoline, food and apparel costs. The higher costs for these necessary goods is one of the key reasons why the economy struggled in 2011; without the payroll tax cut and emergency UI, it is possible the economy would have experienced another recession.

Fiscal Stimulus Multipliers
As of 2011Q3

	Bang for the Buck
Tax Cuts	
Refundable Lump-Sum Tax Rebate	1.22
Nonrefundable Lump-Sum Tax Rebate	1.01
Temporary Tax Cuts	
Child Tax Credit, ARRA parameters	1.38
Payroll Tax Holiday for Employees	1.27
Earned Income Tax Credit, ARRA parameters	1.24
Job Tax Credit	1.20
Making Work Pay	1.19
Payroll Tax Holiday for Employers	1.05
Across-the-Board Tax Cut	0.98
Housing Tax Credit	0.82
Accelerated Depreciation	0.29
Loss Carryback	0.25
Permanent Tax Cuts	
Extend Alternative Minimum Tax Patch	0.53
Make Dividend and Capital Gains Tax Cuts Permanent	0.39
Make Bush Income Tax Cuts Permanent	0.35
Cut in Corporate Tax Rate	0.32
Spending Increases	
Temporary Increase in Food Stamps	1.71
Temporary Federal Financing of Work-Share Programs	1.64
Extending Unemployment Insurance Benefits	1.55
Increase Defense Spending	1.53
Increase Infrastructure Spending	1.44
General Aid to State Governments	1.34
Low Income Home Energy Assistance Program (LIHEAP)	1.13

Note: The bang for the buck is estimated by the one-year $ change in GDP for a given $ reduction in federal tax revenue or increase in spending.
Source: Moody's Analytics

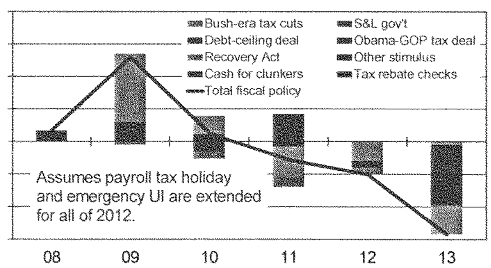
Not extending these programs would deliver a significant blow to the still-tentative economy. Based on the Moody's Analytics model of the U.S. economy, failure to extend the payroll tax holiday will reduce real GDP in 2012 by 0.4 percentage point, while not extending emergency UI will reduce real GDP by 0.3 percentage point. Real GDP is expected to grow 2.6% this year under the assumption that these programs will be extended, but not doing so would result in real GDP growth of less than 2%. The impact on the job market will also be meaningful, costing the economy more than half a million jobs and raising the unemployment rate by at least 0.3 percentage point by the end of 2012.

Extending the payroll tax holiday and emergency UI programs thus makes the difference between an economy that is expanding at close to its long-run potential rate and an economy growing below potential.[vii] While odds are the recovery will continue even if these programs are not extended, the economy will be vulnerable to anything else that may go wrong. The risks will be greatest this spring and summer when the economy is struggling most with the fallout from the European debt crisis and further house price declines.

It is also important to consider that even if these programs are extended, federal fiscal policy will be a significant drag on the economy this year. As the remaining fiscal stimulus from the 2009 Recovery Act fades, and as spending cuts agreed to in the August debt-ceiling deal kick in, the changes will shave 0.8 percentage point from 2012 real GDP growth. Spending cuts by local governments will trim another 0.3 percentage point from growth (see Chart 5).

Chart 5: Federal Fiscal Drag Intensifies

Contribution to real GDP growth, %



Source: Moody's Analytics

Fiscal considerations

The cost of extending the payroll tax holiday and emergency UI program should be offset by future government spending cuts and tax increases. The nation's fiscal situation has become more tenuous, as the federal government's debt-to-GDP ratio has risen by 30 percentage points during the past four years. At close to 70%, it is the highest debt load since just after World War II (see Chart 6).

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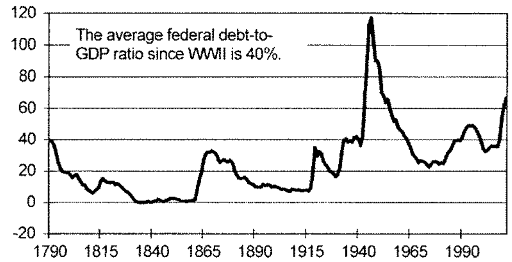
Chart 6: Any Additional Fiscal Support Must Be Paid For

Federal publicly traded debt-to-GDP ratio



Sources: Treasury, Moody's Analytics

The deterioration in the government's fiscal condition largely reflects the impact of the Great Recession on tax revenues and government spending and the policy response to the recession. Policymakers aggressively used government resources to fill the hole created by the collapse in private sector demand, putting more than $1.3 trillion into fiscal stimulus programs during the past four years. While not responding to the recession would have cost taxpayers even more, given what would have arguably otherwise been a depression, the government's actions have been extraordinarily costly.[viii] And the costs continue to mount, as this fiscal year's federal budget deficit will again equal 8% of GDP.

When determining how to pay for these programs, policymakers should consider that under current law, the fiscal drag will intensify substantially in 2013. If policymakers make no other legislative changes, not only will the payroll tax holiday and emergency UI program expire, but spending cuts that were part of the debt-ceiling deal will take effect as well. Marginal tax rates for individuals will also rise as the Bush-era tax cuts end. Fiscal policy will thus slash nearly 3 percentage points from 2013 real GDP growth. This would be very difficult for even a fast-growing economy to withstand.

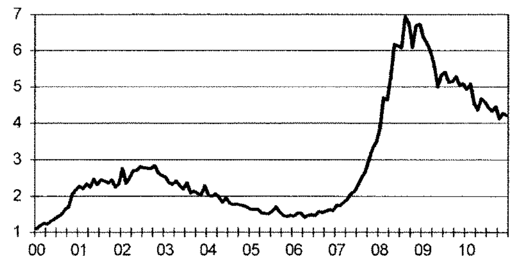
Other considerations

There are reasonable concerns that some recipients of emergency UI are taking advantage of the program, particularly given that as many as 99 weeks of benefits are available in economically hard-hit states. For instance, some of the unemployed may be slow to take jobs, preferring to collect UI. Some older workers may also be delaying retirement, but rather than take a job they remain unemployed and claim UI, retiring after their benefits are exhausted. There is increasing anecdotal and statistical evidence of these and other kinds of abuses in the UI system. Indeed, research on the topic suggests that the current unemployment rate is approximately half a percentage point higher than it would otherwise be, due to the disincentive effects of emergency UI benefits.[ix]

But while there are disincentive effects from emergency UI, the vast majority of UI beneficiaries are not taking advantage of the system. They clearly need the help. The most telling statistic supporting this perspective is the large ratio of unemployed workers per job opening, which according to the BLS is near 4-to-1. (see Chart 7). This is down from about 6-to-1 during the worst of the recession, but it remains more than double the level consistent with a well-functioning job market. Moreover, it would be undesirable for the unemployed to take jobs that were not suitable. It may very well be better for them, their employer, and the broader economy for them to search longer for work to find a more appropriate job.

Chart 7: Unemployed Struggle to Find Jobs

Unemployed per job opening



Sources: BLS, Moody's Analytics

After considering all the effects of the emergency UI program, including the disincentive effects and the benefits to aggregate demand, ending or scaling back the program would be a significant macroeconomic mistake.[x]

There has also been some debate among policymakers over whether UI benefits should be denied to any worker who lacks a high school diploma or GED and is not enrolled in classes to get one or the other. This would unnecessarily complicate and perhaps significantly delay the provision of UI benefits to hard-pressed unemployed workers at a critical time for the economy. Any such restriction would also undermine a key principle of the UI system since its inception during the Great Depression, namely that workers who paid insurance premiums to the UI system when they were on the job should be able to collect on that insurance when they lose their job.

Policymakers should also consider extending the period over which states are able to borrow interest-free from the federal government to meet their UI obligations. According to National Conference of State Legislators, 27 states have outstanding loans totaling $38 billion from the federal government to pay state unemployment compensation. The largest debts are owed by California, New York, Pennsylvania, North Carolina, Illinois, Ohio, Indiana, Florida and New Jersey. It would also be helpful if penalties on states that are borrowing to pay unemployment compensation are also waived for a longer period.

Without such relief, states are beginning to raise payroll taxes at a still-difficult time for the economy.

Work share

This is not to say the unemployment insurance program does not need significant reform; it does. While there are a number of ways to improve the UI system, one of the most promising would be the wider adoption of work-share programs, also called short-term compensation. Work-share programs in a number of states have successfully limited layoffs.

Work share was effectively used by Germany during the recession. German real GDP declined almost 6% peak to trough, but unemployment rose only modestly, to around 8%. U.S. real GDP declined closer to 5%, yet unemployment rose by more than 5 percentage points to 10%. There are a number of reasons for the difference, but the wider use of work share in Germany is an important one.

Work share allows employers to reduce employees' hours for a time and for the workers to receive proportionate unemployment benefits for those reduced hours to lessen the financial impact. Employers are generally required to submit a plan describing the program. Work share is especially helpful for firms that expect workforce reductions to be temporary, allowing them to avoid the cost of severance, rehiring and training. It also promotes employee morale, allowing workers to maintain their health insurance and retirement benefits.

A number of features can make work-share programs more effective. Most important is to have employers administer work-share payments as part of their regular payroll process rather than have employees file claims with unemployment agencies. The rules should also allow employers to determine the appropriate reduction in hours for individual employees rather than impose a uniform reduction for all affected workers. Employers should also be allowed to adjust their plans as circumstances change, which they will in an economic downturn. It is also important that experience under work share count in determining workers' eligibility for full unemployment benefits. Work share would also be more effective if combined with training requirements to ensure that workers use the additional downtime effectively.

Conclusions

The U.S. economy has performed much better in recent months. Most encouraging are the recent revival in job growth and the substantial decline in the unemployment rate. There are nascent signs that businesses are hiring more, which is necessary for a much stronger economy.

But while prospects are looking up, the economy still faces formidable hurdles, the most obvious of these being the troubles in Europe and falling house prices at home. It would not take much to undermine confidence, which remains on edge after the nightmare of the Great Recession and amid Washington's partisan acrimony. Given that 2012 is an election year, policy uncertainty will only intensify. The economy is not yet home free.

It is thus important for fiscal policymakers to be judicious about how they withdraw support from the economy. Fiscal policy has already become a drag as various tax cuts and spending initiatives implemented during the recession fade. This is on top of the economic drag created by cuts in state and local government budgets.

Given this, Congress and the Obama administration should agree to extend the current payroll tax holiday and emergency UI program through the end of 2012. This will ensure that fiscal policy does not become even more of a weight this spring and summer, when the economy will still be vulnerable.

Policymakers have worked very hard and used tremendous financial resources to end the Great Recession and support the subsequent recovery. It has been an extraordinarily trying time, but it would have been measurably more difficult if not for policymakers' unprecedented efforts. A self-sustaining economic expansion is close at hand, but only if policymakers do not pull their support from the economy too quickly.

[i] There was a significant amount of optimism regarding the economy's prospects in early 2011. According to Consensus Economics, the consensus of economists as of January 2011 was for real U.S. GDP to grow 3.4% in 2011. It actually grew only 1.7%.

[ii] From 9.1% in August, the unemployment rate has fallen to 8.3% in January. During this period, the BLS household survey has recorded an employment increase of 1.9 million jobs and a gain of more than 700,000 in the U.S. labor force.

[iii] The chart shows two broad measures of labor compensation growth. Compensation as measured by the employment cost index is the most comprehensive and consistent measure; it controls for the shifting mix of jobs across industries and occupations. Compensation as measured in the productivity and cost report is significantly influenced by the value of stock options granted as compensation.

[iv] The Moody's Analytics estimate of the number of underwater homeowners is based on actual mortgage debt outstanding from Equifax credit files. It differs from estimates by CoreLogic, which put the number of underwater homeowners at closer to 11 million households. The Moody's estimate is nearly the same as CoreLogic's in California, much lower in Florida, and higher almost everywhere else. The difference in estimates may be due in part to CoreLogic's estimate of current debt outstanding, which is based on the amount of debt outstanding at origination. CoreLogic may have some difficulty measuring debt outstanding in rural or exurban areas, where homeowners generally have little equity even in good times (since house prices never rise much) and go into small negative-equity positions in difficult times. The Moody's estimate is much higher in Texas, for example. CoreLogic data are also unavailable for a half-dozen states.

[v] The bang-for-the-buck estimates are based on simulations of the Moody's Analytics econometric model of the U.S. economy.

[vi] See "Consumer Spending and the Economic Stimulus Payments of 2008," Parker et al, January 2011. http://finance.wharton.upenn.edu/~souleles/research/papers/PSJM2011.pdf. Also see "Household Expenditure and the Income Tax Rebates of 2011," Johnson et. al, *American Economic Review*, December, 2006. http://www.aeaweb.org/articles.php?doi=10.1257/aer.96.5.1589.

[vii] The economy's potential rate of growth is defined as a rate at which jobs are being added fast enough to maintain a stable rate of unemployment. The U.S. economy's long-run potential growth rate is estimated to be 2.6%.

[viii] See Blinder and Zandi, "How the Great Recession Was Brought to an End," Moody's Analytics Special Study, July 2010. http://www.economy.com/mark-zandi/documents/End-of-Great-Recession.pdf.

[ix] See Mazumder, "How Did Unemployment Insurance Extensions Affect the Unemployment Rate in 2008-10," Federal Reserve Bank of Chicago, Essays on Issues No. 285, April 2011; Rothstein, "Unemployment Insurance and Job Search in the Great Recession," NBER Working Paper No. 17534, October 2011; and Valletta and Kuang, "Extended Unemployment and UI Benefits," Federal Reserve Bank of San Francisco Economic Letter 2010-12, April 19, 2010.

[x] See Valletta and Kuang, "Why is Unemployment Duration So Long," Federal Reserve Bank of San Francisco Economic Letter 2012-03, January 12, 2012.

INDIANA
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February 7, 2012

PREPARED TESTIMONY FOR THE RECORD of the:

JOINT ECONOMIC COMMITTEE

Offered by Mark W. Everson, Commissioner

Indiana Department of Workforce Development

I. Introduction

Mr. Chairman, Vice Chairman Brady, and members of the committee, thank you for the opportunity to testify on the important subject of unemployment insurance.

My name is Mark W. Everson, and I serve as commissioner of the Indiana Department of Workforce Development. The Department of Workforce Development operates the state's unemployment insurance system, workforce training programs funded by the United States Department of Labor, and works with the Bureau of Labor Statistics to report labor statistics for Indiana. Additionally, we administer Adult Education programs working with the United States Department of Education.

The federal-state unemployment insurance partnership is an important, proven system which has successfully served the nation for more than seven decades. In my testimony today, I will review the condition of the unemployment insurance system in Indiana, as well as actions Indiana has taken to reform our program and eliminate the indebtedness of our trust fund. In addition, I will explain the need for flexibility on the part of states if we are to collectively secure the long-term health of the unemployment insurance system.

Unemployment insurance has provided support for those temporarily out of work in both strong and weak economies. Over time, the system has adapted well to changes in the American economy, and the evolution of the nation's workforce. Nevertheless, the system has been severely strained by the recent recession. It can weather the storm, but states require flexibility on the part of our federal partners to do so. States can also be laboratories for policy changes designed to improve the program and help the nation's workforce meet the challenges of the twenty-first century. While you consider the appropriateness of extending emergency unemployment compensation and perhaps imposing new rules upon states, I urge Congress to respect the long established separation of the roles played by states and the federal government in the operation of the program. Please also consider that the future of the program depends not only on how well the unemployed are served, but also on continued support of employers who fund the system, as well as the public at large. The vast majority of

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Americans support a system providing relief to the worker who finds himself or herself involuntarily unemployed, and who actively seeks to return to work. However, if those outside the system begin to believe that amounts paid are too generous, are paid for too long, or that those who do not qualify can obtain benefits, support for the system is undermined. This damages both the system itself and tarnishes the image of those who are unemployed. It remains important to let states design their unemployment insurance programs. We are closest to the businesses and claimants who use the system, and best positioned to balance competing public policy interests.

II. Overview of Indiana's Unemployment Insurance System

Last week 138,000 individuals collected some form of unemployment insurance benefits in Indiana, comprising 74,000 who drew state paid benefits and 64,000 whose benefits were paid 100% by the federal government. Those individuals drawing federal benefits had exhausted eligibility for state benefits and were either on emergency unemployment compensation or state extended benefits. Similar to other states, Indiana has a significant number of people who unfortunately have been unemployed for over half a year. I would note, however, that our state initial and continued claims have returned to 2007 levels.

In Indiana, the total number of claimants drawing either state or federally funded benefits at any one time peaked at over 271,000 in early 2010. For calendar year 2011 Indiana paid out approximately $2.0 billion in benefits, down from $3.5 billion in 2009. This included $840 million in state benefits, down from $1.9 billion in 2009, as well as $1.2 billion in federal benefits, down from $1.6 billion in 2009. Over the course of last year, 373,000 discrete individuals collected benefits for one week or more, and received an average weekly benefit of just under $300.

Indiana Unemployment Insurance
System Benefits Paid
($ millions)

	2009	2010	2011
State	$1,865	$1,025	$840
Federal	$1,600	$2,004	$1,171
Total	$3,465	$3,029	$2,011

III. Indebtedness of the Trust Fund

As you are no doubt aware, 27 states have borrowed over $38 billion to continue funding the state portion of unemployment insurance benefit programs. Three states also incurred

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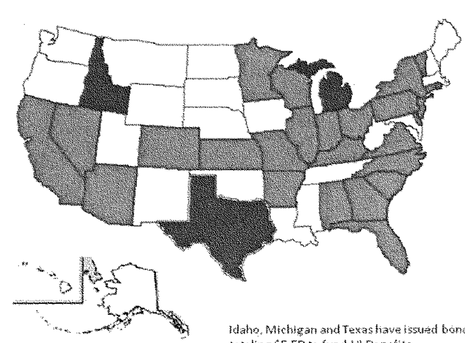
significant indebtedness, but have borrowed over $5.5 billion from other sources to pay off their federal debt. The states with the highest indebtedness per worker are Indiana, Nevada, North Carolina, California and Pennsylvania.

At the start of the last decade, Indiana's trust fund held a $1.6 billion surplus. In 2001, the state legislature enacted a series of benefit increases implemented in steps over much of the past decade, and provided limited premium relief to employers. These legislative actions created a continuing structural imbalance. To work, the trust fund should realize a surplus in good years for use when times get tough. Revenues have failed to exceed benefit expenditures in every year since the passage of the 2001 legislation. Many states may blame their trust fund insolvency on the severity of the recent recession. In Indiana trust fund coffers were empty by late 2008, just as the collapse arrived. Over the next two years, the trust fund plummeted as benefit payments skyrocketed. At the end of 2010, the trust fund owed the federal government $1.96 billion.

State Unemployment Insurance Trust Fund Loan Balances

(in $millions)



Idaho, Michigan and Texas have issued bonds totaling $5.5B to fund UI Benefits

State Trust Fund Advances as of January 30, 2012

State	Loan Balance	Interest Payable
California	$10,214.9	$120.3
New York	3,641.3	41.4
Pennsylvania	3,517.2	40.2
North Carolina	2,743.3	33.1
Illinois	2,322.1	25.9
Ohio	2,166.7	28.4
Indiana	2,037.6	24.6
Florida	1,832.5	22.0
New Jersey	1,632.7	18.0
Wisconsin	1,326.5	15.3
Kentucky	948.7	12.1
Nevada	806.7	9.5
South Carolina	782.5	10.2
Missouri	770.3	9.3
Georgia	721.1	9.2
Connecticut	709.9	10.0
Arizona	398.3	4.4
Colorado	382.2	4.0
Arkansas	330.9	4.2
Virginia	318.3	3.2
Rhode Island	254.0	2.8
Minnesota	241.1	2.3
Michigan	118.3	31.8
Kansas	92.8	0.7
Vermont	77.7	1.0
Delaware	68.0	0.8
Alabama	55.1	0.4
Virgin Islands	31.9	0.4
Totals	$38,542.5	$485.3

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IV. Indiana's Actions to Repair its Unemployment Insurance Program

The unemployment insurance program has three overall design elements; revenues – the premiums paid by employers into the system; eligibility - that is, who is entitled to receive benefits; and benefit levels - that is, the method of calculating how much an unemployed individual receives each week and for how long. A change in any element impacts the trust fund. In early 2011, Indiana's legislature enacted balanced, comprehensive reform, addressing all three elements. Although the trust fund got into trouble mostly due to increases in benefit payments, over two-thirds of the cost of the fix is being paid by employers.

A. Revenues:

Before the 2011 reform of the unemployment insurance program, Indiana employers paid premiums on the first $7,000 of taxable wages and were charged a rate ranging from 1.1% to 5.6%. The 2011 reform increased the taxable wage base from $7,000 to $9,500 per employee and established new rates ranging from 0.5% to 7.4%. The wider range of rates increased total revenues, while at the same time providing relief to employers not utilizing the fund. The reform also established a surcharge to fund interest payments on our federal loan (Indiana paid $60.4 million to the federal government September 30, 2011). These changes took effect January 1, 2011. When taking into consideration the premium changes, interest surcharge and a FUTA credit reduction of $21 per employee, Indiana employers saw an aggregate cost increase of 60% in 2011 over 2010.

B. Eligibility:

Just as with premiums, states have had wide latitude in determining eligibility standards for coverage by the unemployment insurance system. The most notable change in eligibility standards in Indiana's reform package addressed repeat users of the system who plan and conduct regular shutdowns of their operations.

In recent years, more than 10% of individuals receiving unemployment insurance benefits in Indiana also received benefits in at least the prior two years. Many employers schedule routine factory shutdowns, usually during holiday periods, and have historically relied on the state's unemployment insurance fund to compensate workers during these events. Often these employers already paid the maximum premium rate under state law and had long since lost the disincentive that experience rating presumes. As a simple matter of arithmetic, any benefit payments that exceed an employer's contribution need to be covered by higher contributions from others, or be funded by the trust fund itself. The reform package included provisions that workers who are part of a shutdown based upon regular practice and policy of the employer, and who return to work after the routine shutdown, were not unemployed for the purpose of

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receiving unemployment compensation. This provision and other less significant eligibility provisions took effect on July 1, 2011.

C. Benefit Levels:

Prior to the 2011 reform package, unemployment insurance benefit amounts in Indiana, as in many states, were calculated based only on the highest quarter of a worker's earnings. This method of calculation often yielded different benefit amounts for individuals who had earned the same wages over the course of the year. To provide an example under the current law, last month my department received a WARN notice indicating over 200 individuals will soon lose their jobs due to the closure of a K-Mart in Portage, Indiana. Assume that one of these workers has earned $500 per week over the past year for a total annual salary of $26,000. If this individual files, he or she qualifies for $280 weekly. Contrast this with a worker earning the same $26,000, but working only 3 quarters, common in Indiana's construction industry. Even though their annual earnings are equal, this construction worker would qualify for $366, or $86 more dollars weekly because only the high quarter is considered.

To address this inequity, the legislature determined that in the future benefit amounts should be calculated based on annual earnings. The reform statute will base benefit amounts on the individual's average weekly wage as opposed to just high quarter earnings. The new benefit formula also provides for replacing 47% of the individual's average weekly wage while holding unchanged the states maximum benefit amount of $390. Under the reform package, the total projected reduction in expenditures with these adjustments to benefit levels is approximately 22%. These changes will apply to claims for benefits filed after July 1, 2012.

Thus far, the reform package is working as intended. As noted above, the trust fund balance was $1.96 billion at the end of 2010 and held steady in 2011 to end the year at $1.97 billion. This reflected lower benefit payments largely associated with an improving economy, but also the premium increases mentioned above. For calendar year 2012, premiums should exceed benefits for the first time in more than a decade. Given current projections, we expect to pay off the federal debt by 2018 (chart shown below).

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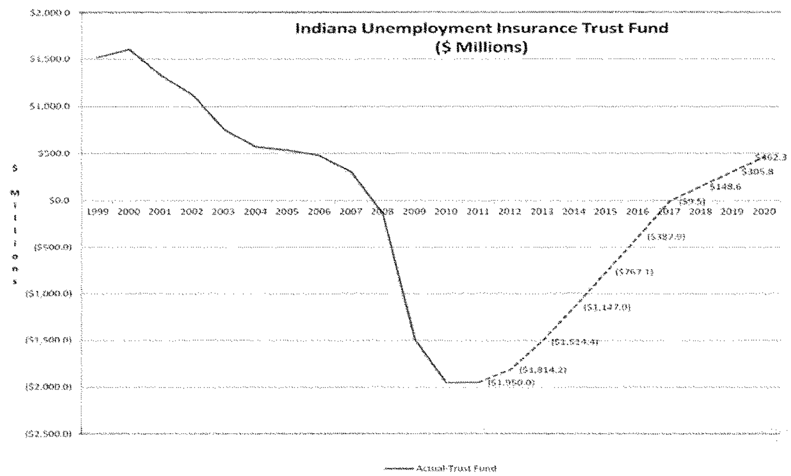

V. <u>The Non-Reduction Rule</u>

The federal non-reduction rule was initially established in 2009 to prevent states from offsetting through benefit reductions a $25 supplemental payment paid for with federal funds. The $25 supplement has been discontinued, but for the first time, in early 2010, the federal government required the non-reduction rule to be tied to federal extended unemployment benefits. This is a departure from past federal extensions of benefits during periods of high unemployment, when no such rule was in place.

When Indiana enacted its reform package, the new benefit calculation was purposefully delayed until July 1, 2012, in order to take effect after the expiration of the federal extensions. While the non-reduction rule was eliminated from the House version of the most current federal extensions, it was retained in the recent two-month extension. We urge you to eliminate it from any further extension of this program.

There are currently three other states that may also be implicated by the non-reduction rule along with Indiana. These three states, Rhode Island, Pennsylvania and Arkansas, have in some form also reduced or are scheduled to reduce their weekly benefit amount. I would also note that other states have addressed trust fund solvency by avoiding the non-reduction rule but decreased the number of weeks of unemployment compensation eligible individuals can receive. A couple, Michigan and Florida, have gone from 26 weeks to 20 weeks of regular state

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unemployment benefits. If the non-reduction rule remains in place, more states will likely shorten the number of weeks of unemployment in an effort to reduce their costs. In the future states may also be reluctant to increase benefit payments.

In summary, the recently enacted non-reduction rule has significantly altered the long-standing federal-state balance of the program. States should retain the flexibility to determine the most appropriate unemployment insurance benefits program and method of addressing unemployment insurance trust fund solvency. In recognition of this need for state sovereignty in determining the best unemployment insurance program, the National Association of State Workforce Agencies called for elimination of the non-reduction rule at its September 2011 annual meeting.

VI. Conclusion

In Indiana we value our partnership with the federal government in operating the unemployment insurance system. We believe we have put our program on a healthy and sustainable path. I commend Congress for looking at avenues of reform, such as work search and training requirements. However, as with the non-reduction rule, I ask you to provide states the flexibility to provide appropriate overall program design best suited for their circumstances. Thank you.

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CONGRESSIONAL TESTIMONY

Attempting to Bolster the Economy: The Effectiveness of Extending UI Benefits

Testimony before
The Joint Economic Committee
United States Congress

February 7th, 2012

James Sherk
Senior Policy Analyst in Labor Economics
The Heritage Foundation

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Chairman Casey, Vice-Chairman Brady, and members of the Joint Economic Committee, thank you for inviting me to testify before you today. My name is James Sherk. I am a Senior Policy Analyst in Labor Economics at the Heritage Foundation. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

Extending the length of time workers can collect unemployment insurance (UI) benefits in a recession makes sense, but only for humanitarian reasons. Extended benefits moderately increase the unemployment rate; they do not bolster the economy. 60 weeks of benefits represent a proportionate increase in UI duration that matches the increased difficulty of finding work. Two years of benefits are excessive and counterproductive.

Congress should also reform the UI system to place a greater focus on returning the unemployed to work. Currently the system focuses almost entirely on distributing UI checks. Congress should both increase job search requirements—which most unemployed workers already fulfill—and enable the states to experiment with innovative strategies to help the unemployed find jobs.

The Unemployment Insurance System

Congress created the unemployment insurance system in the 1930s as an insurance system to enable workers who lose their jobs to smooth consumption until they find new work. It is an unemployment insurance system: the program insures workers against the risk of a harmful event outside their control. Consequently only involuntarily unemployed workers may collect benefits. Workers who voluntarily leave their jobs may not collect benefits, nor may workers who are not searching for new work. UI normally provides workers with six months (26 weeks) of benefits through a system largely financed by state-level taxes. Workers in states with higher unemployment levels may collect an additional three months (13 weeks) of benefits through the jointly funded state-federal Extended Benefits (EB) program.

Since the recession started Congress has increased length of time workers on UI can collect benefits. Congress created the Emergency Unemployment Compensation (EUC) system with a maximum of 53 weeks of benefits, while taking over all the financing of the EB system and extending it to 20 weeks. As a result workers in many states can collect up to 99 weeks of benefits—almost two years.

Effect on Job Search

Like most insurance programs, unemployment insurance suffers from moral hazard. UI payments make remaining unemployed less costly, causing UI recipients to take longer to find new work.

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The fact that UI benefits cause workers to stay unemployed longer is one of the most conclusively established findings in labor economics.[1] Researchers of every political persuasion have come to this conclusion. Even Alan Krueger, the Chairman of President Obama's Council of Economic Advisors, agrees.[2]

Contrary to some stereotypes, however, this does not primarily occur because most workers on UI enjoy receiving government handouts. While some individuals do abuse the system, UI benefits are not especially generous. They typically replace between 35 and 40 percent of an employee's previous income. Relatively few unemployed stay jobless to UI checks from the government.[3]

Instead most of the effect comes from changing how the unemployed search for jobs. UI benefits reduce the importance of finding a new job immediately. This enables the unemployed to focus their search on jobs they prefer to find. Often this means looking for jobs near the city, the occupation, and/or salary they had before. As benefits draw down, workers widen their search to jobs they would not previously consider. Alan Krueger finds that the amount of time that workers on UI spend job hunting triples when their benefits start to run out.[4]

Moderately Higher Unemployment Rate

Extending unemployment benefits to two years has kept many workers unemployed longer than they otherwise would have. Researchers from many institutions, including Federal Reserve Banks, have examined how this affects the unemployment rate. They concluded that extending benefits to 99 weeks has increased the unemployment rate by approximately 0.5 percentage points.[5] Extended unemployment benefits have had a nontrivial effect on the unemployment rate, but they are not the main reason it remains so high.

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[1] See David Card and Phillip B. Levine, "Extended Benefits and the Duration of UI Spells: Evidence from the New Jersey Extended Benefit Program," *Journal of Public Economics*, Vol. 78 (1–2) (October 2000), pp. 107–38; Lawrence Katz and Bruce Meyer, "The Impact of the Potential Duration of Unemployment Benefits on the Duration of Unemployment," *Journal of Public Economics*, Vol. 41, No. 1 (1990), pp. 45–72; Stepan Jurajda, "Estimating the Effect of Unemployment Insurance Compensation on the Labor Market Histories of Displaced Workers," *Journal of Econometrics*, Vol. 108, No. 2 (2002), pp. 227–52; John T. Addison and Pedro Portugal, "How Does the Unemployment Insurance System Shape the Time Profile of Jobless Duration?," *Economics Letters*, Vol. 85, No. 2 (November 2004), pp. 229–34; Rafael Lalive, Jan Van Ours, and Josef Zweimüller, "How Changes in Financial Incentives Affect the Duration of Unemployment," *Review of Economic Studies*, Vol. 73, No. 4 (October 2006), pp. 1009–38.

[2] Alan B. Krueger and Bruce D. Meyer, "Labor Supply Effects of Social Insurance," in A. J. Auerbach and M. Feldstein (ed.), *Handbook of Public Economics*, First Edition, Vol. 4 (2002), pp. 2327–92

[3] Raj Chetty, "Moral Hazard versus Liquidity and Optimal Unemployment Insurance," *Journal of Political Economy*, Vol. 116, No. 2 (2008), pp. 173–234.

[4] Alan Krueger and Andreas Mueller. "Job Search and Unemployment Insurance: New Evidence from Time Use Data," *Journal of Public Economics*, Vol. 94, Nos. 3–4 (2010), pp. 298–307.

[5] Bhashkar Mazumder, "How Did Unemployment Insurance Extensions Affect the Unemployment Rate in 2008–10," Federal Reserve Bank of Chicago, *Essays on Issues* No. 285, April 2011; Jesse Rothstein, "Unemployment Insurance and Job Search in the Great Recession," *NBER Working Paper* No. 17534, October 2011; Rob Valletta and Katherine Kuang, "Extended Unemployment and UI Benefits," Federal Reserve Bank of San Francisco *Economic Letter* 2010–12, April 19, 2010.

Appropriate Duration

Providing longer UI benefits during a recession makes sense because job loss becomes more costly when it takes longer to find new work. Consequently providing the same insurance against the risk of unemployment requires longer benefits. The important question is "How long should the government provide benefits for?"

To answer this question Congress needs to balance several factors. Additional benefits provide workers with more resources and flexibility. However, they also increase unemployment and can hurt those they are meant to help. Many of the jobs that unemployed workers would prefer to find do not exist and will not return.[6] To find work, many workers will have to take positions that are much less than ideal. Extending benefits for too long encourages the unemployed to search for jobs that they will not find. This can hurt them in the long run.

Congress also has to consider fairness to taxpayers. The federal government is running record deficits. Current and future taxpayers should not be asked to pay for unreasonably long benefits.

Even with the difficult job market 99 weeks–almost two years–of benefits is excessive. In normal economic times the average unemployed worker is jobless for four months.[7] During these times the government provides six months of unemployment insurance coverage – 50 percent greater than the average duration of unemployment. In the current recession the average duration of unemployment has risen to 40 weeks (nine months).[8] Providing 60 weeks of UI payments would increase benefits proportionately to the deterioration of the labor market.

Congress should keep UI benefits extended beyond six months while reducing benefit duration to an appropriate level. Especially in light of recent improvements in the labor market, taxpayers should not be required to pay for two years of UI benefits.

Keynesian Models

The arguments for extended benefits must rest on humanitarian grounds. Congress should not expect extended UI benefits to provide stimulus. While it would be nice if extended UI benefits also boosted the economy, they do not.

Some economic models, particularly those of Mark Zandi and some of models at the Congressional Budget Office, do forecast that spending more on UI benefits boosts the economy. These models typically show that spending $1 on additional UI benefits

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[6] For example, over half of net employment losses occurred in the manufacturing and construction sectors. Many workers in these sectors will need to switch industries.

[7] Department of Labor, Bureau of Labor Statistics, "The Employment Situation," Table A-12 / Haver Analytics. The average duration of unemployment in non-recessionary periods is between 16 and 18 weeks – four months.

[8] Ibid.

increases economic output by between $1.50 and $1.90.[9] It is important to understand that such results are pre-programmed into these models.

A computer model is only as good as the assumptions built into it. The macroeconomic models that find that UI payments stimulate the economy are Keynesian models. They assume that government spending adds to total economic output, or that government spending adds value to the economy. It does so through a "multiplier" effect in the economy. That is, when the government spends a dollar the recipients of that dollar spend it elsewhere. The recipients of those dollars then spend it elsewhere again, and so on, boosting demand and spurring production throughout the economy above what the private sector would produce. In this theory government spending is the ultimate free lunch: each dollar the government spends creates more than a dollar of economic output.

Keynesian models naturally show that extending UI benefits stimulates the economy. UI spending gives money to households, who the models assume spend it immediately, creating the multiplier effect and stimulating GDP. Given these assumptions it is virtually impossible for these models to come to any other conclusion.

No Economic Stimulus

Unfortunately, there is no such thing as a free lunch. Keynesian theories and models do not accurately describe how the economy operates. Many of these models assume that individuals consume almost every dollar of UI benefits they receive.[10] However, empirical research shows that receiving a dollar of UI benefits increases household consumption by just $0.55.[11]

Consumption does not rise by more because unemployment benefits change household behavior. For married men, each dollar of UI benefits reduces their wives' earnings by between 36 and 73 cents.[12] The fall in spousal income partly offsets the increase in UI benefits. Workers also spend more of their savings if they do not have UI.[13] Extended UI benefits provide alternative financing for some consumption that

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[9] See for example: Mark M. Zandi, "Assessing President Bush's Fiscal Policies," Economy.com, July 2004, Table 4, at http://www.pbs.org/wsw/opinion/zandionbush.pdf; Congressional Budget Office, "Options for Responding to Short-Term Economic Weakness," January 2008, pp. 17, 22,

[10] For example, see Wayne Vroman, "The Role of Unemployment Insurance as an Automatic Stabilizer During a Recession," IMPAQ International, July 2010, page 33, at http://wdr.doleta.gov/research/FullText_Documents/ETAOP2010-10.pdf "These transfer payments are then almost entirely spent on consumption items in the same year."

[11] Jonathan Gruber, "The Consumption Smoothing Benefits of Unemployment Insurance," *American Economic Review*, Vol. 87 (March 1997), p. 195. Note that a 10 percent increase in the replacement rate (representing a 10 percent increase in individual income) reduces the fall in individual consumption by 2.65 percent. Footnote 9 of this paper notes that the average recipient obtains 48 cents out of every additional dollar of which he or she is eligible because not all workers eligible for benefits receive them. So when UI raises incomes by 4.8 percent, consumption rises by 2.65 percent. Each dollar spent on UI raises consumption by approximately 55 cents.

[12] J. B. Cullen and J. Gruber, "Spousal Labor Supply as Insurance: Does Unemployment Insurance Crowd Out the Added Worker Effect?," *Journal of Labor Economics*, Vol. 18, No. 3 (2000), pp. 546–72.

[13] Eric M. Engen and Jonathan Gruber, "Unemployment Insurance and Precautionary Saving," *Journal of Monetary Economics*, Vol. 47 (June 2001), pp. 545-579.

would nonetheless take place. Assuming households consume every dollar of benefits artificially inflates their modeled "multiplier effect" on the economy.

More fundamentally, the "multiplier effect" only looks at half the story. The resources the government spends do not materialize out of nowhere. They are borrowed or taxed from elsewhere in the economy. This reduces spending and demand. Further, government borrowing redirects resources away from productive investments that produce economic value.

Empirical studies shows that increasing government spending reduces private sector output. Recent empirical work published by National Bureau of Economic Research concludes that the multiplier is approximately 0.5. For each dollar the government spends the private sector produces $0.50 less.[14] Other studies come to similar conclusions.[15] The economy does not operate the way Keynesian models assume it does. The multiplier is actually a divisor.

The models are wrong about how government spending generally affects the economy. Their forecasts about UI spending are similarly inaccurate. From 2008 through 2011 the government increased UI spending by $300 billion.[16] Congress has repeatedly heard testimony that extending UI benefits will bolster the economy. The White House predicted that if Congress passed the stimulus—which included UI extensions—then unemployment would not rise above 8 percent. Congress passed the stimulus.[17] Unemployment rose to 10 percent and Americans have suffered through the slowest recovery of the post-war era.

This should not have come as a surprise. Macroeconomic empirical studies have demonstrated that UI spending has at most a small effect in stabilizing the economy.[18] Empirical research into UI spending in individual states also finds it has negligible economic effects.[19]

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[14] Valerie Ramey, "Government Spending and Private Activity," National Bureau of Economics Working Paper No. 17787, January 2012

[15] Robert Barro and Charles Redlick, "Macroeconomic Effects from Government Purchases and Taxes," Quarterly Journal of Economics, 2011, Vol. 126, No. 1, pages 51-102; Robert Hall, "By How Much Does GDP Rise if the Government Buys More Output," Brookings Papers on Economic Activity, Fall 2009, pages 183-236

[16] Heritage calculations using data from the Bureau of Economic Analysis, "Personal Income and Outlays," Table 1, unemployment insurance income from 2008-2011 / Haver Analytics. From 2005 through 2007 the government spent an average of $31.6 billion a year on UI spending. From 2008 through 2011 the government spent $427 billion on UI benefits—$300 billion more than in UI spending had remained at normal levels. These figures include both regular state UI programs and the extensions funded by the federal government.

[17] Christina Romer and Jared Bernstein, "The Job Impact of the American Recovery and Reinvestment Plan," January 10, 2009, p. 2, at *http://otrans.3cdn.net/45593e8ecbd339d074_l3m6bt1te.pdf*

[18] George M. Von Furstenberg, "Stabilization Characteristics of Unemployment Insurance," Industrial and Labor Relations Review, Vol. 29, No. 3 (April 1976), pp. 363-376. Alan J. Auerbach and Daniel Feenberg, "The Significance of Federal Taxes as Automatic Stabilizers," Journal of Economic Perspectives, Vol. 14, No. 3 (2000), pp. 37-56.

[19] Kyung Won Lee, James R. Schmidt, and George E. Rejda, "Unemployment Insurance and State Economic Activity," International Economic Journal, Vol. 13, No. 3 (Autumn 1999), pp. 77-95.

The International Experience

International evidence reinforces this conclusion. If UI spending stimulates the economy then unemployment would rise less rapidly in countries with more generous benefits. Instead the opposite happens. Unemployment rises faster in countries that provide more extensive benefits.[20] The disincentive effects of UI overwhelm any stimulative effects.

This may be why the argument that the government should spend heavily on UI to stimulate the economy is rarely heard internationally. In few other OECD countries do policymakers argue that UI boosts demand and employment.[21] Generous UI systems have not stimulated European nations out of persistently high unemployment. Just the opposite. Countries that reduced the generosity of UI benefits saw their unemployment rates fall.[22]

Policy Tradeoffs

This does not mean Congress should return to six months of benefits. It means that Congress faces economic tradeoffs. The humanitarian benefits of extending UI come at a fiscal and economic cost. Congress can certainly conclude that the benefits outweigh the costs. But any extension of benefits should recognize these tradeoffs. If extending benefits is an important priority then they should be paid for by reducing spending on less important programs.

Additional Problems in the UI System

Changes to the UI system should extend beyond changing the weeks of benefits provided. The UI system currently places little emphasis on returning the unemployed to work. Instead UI administration largely focuses on distributing benefits to covered workers. Job search assistance is often a secondary concern.

The UI system also has few safeguards to prevent abuse. The federal government does not require workers receiving EUC or Extended Benefits to search for work. State laws do require claimants in the regular UI system to search for a job. However, states do little to verify that workers actually do so. In most states claimants reapply for their benefits either online or by calling an automated hotline. They indicate they have contacted employers by clicking a box or pressing a button. Most states do little to follow-up to ensure that workers were truthful.[23] This saves money on overhead and

[20] Andrea Bassanini and Romain Duval, "Unemployment, institutions, and reform complementarities: re-assessing the aggregate evidence for OECD countries," Oxford Review of Economic Policy, Oxford University Press, vol. 25(1), pages 40-59, Spring 2009.

[21] David Grubb, "Assessing the impact of recent unemployment insurance extensions in the United States," Organization for Economic Cooperation and Development, Working paper, OECD June 2011, page 49.

[22] Ibid, pages 46, 55-59.

[23] Testimony of Douglas J. Holmes, President, UWC- Strategic Services on Unemployment & Workers' Compensation, Before the Subcommittee on Human Resources, Committee on Ways and Means, United States House of Representatives. Hearing on "Improving Efforts to Help Unemployed Americans Find Jobs," February 10, 2011.

administration, but claimants who collect benefits without looking for work face few consequences.

Substantial evidence suggests that tightening requirements can reduce the time workers spend on UI. In the mid-1990s Maryland conducted a series of experiments. The state told some workers that the government would verify their employer contacts.[24] They required other workers to attend a four-day workshop on how to search for a new job. Other workers stayed on the regular program. The workers with the more stringent requirements spent 5 to 8 percent less time on UI than the workers in the regular system.[25] Interestingly, most of the increased job finding by those assigned to the workshop occurred before the workshop began. It appears that the cost of spending four days in a workshop prompted UI recipients who had the ability to return to work to do so. Most other studies also find that penalizing inadequate job search reduces the time workers spend on UI.[26]

The vast majority of workers on UI try to find work. However, screening out the minority who do not would save a lot. Spending 5 percent less on UI extensions would save $2 billion a year.[27]

Reforming UI

The government should reform the UI system to address both these problems. The unemployment insurance system should focus on returning the unemployed to work. Those who can work should not be allowed to abuse the UI system.

The federal government should require workers claiming extended benefits to actively search for a job. However, the unemployment insurance system operates as a joint state-federal program. The federal government should not trample on the states as it reforms UI. Rather the federal government should work with the states to improve the system. The provisions in the House passed payroll tax cut and UI extension (H.R. 3630) provide a good starting point for such reforms. The House bill required workers receiving UI benefits to:

(1) Actively search for work, in such manner as states direct;
(2) Register with state reemployment services within 30 days;
(3) Post a resume or job application on a state database; and
(4) Participate in any reemployment services the state refers them to.

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[24] Most states did not switch over to online or phone systems to reauthorize claims until the late 1990s or early 2000s. Before then workers in many states filed paper forms listing the employers they had contacted.

[25] Jacob Benus and Terry Johnson, "Evaluation of the Maryland Unemployment Insurance Work Search Demonstration," Maryland Department of Labor, November 1997, at http://wdr.doleta.gov/owsdrr/98-2

[26] Peter Fredriksson and Bertil Holmlund, "Improving Incentives in Unemployment Insurance: A Review of Recent Research," The Journal of Economic Surveys, Volume 20, No. 3 (2006), pages 357-386.

[27] The Congressional Budget Office estimates that maintaining the benefit extensions will cost $50 billion in 2012. Five percent of $50 billion is $2.5 billion. See Congressional Budget Office, cost estimates, "Budgetary Effects of the Temporary Payroll Tax Cut Continuation Act of 2011," December 22nd, 2011. Note the CBO estimates the two month cost of the extensions is $8.4 billion. The 12 month cost is six times greater, $50 billion.

The federal government should also allow the states to experiment with larger reforms to the UI system. Federal law tightly restricts how states can use UI funds. They may only use them to pay for UI benefits or administrative costs. This prevents states from enacting more innovative reforms focused on returning the unemployed to work.

Some analysts have proposed wage subsidies for employers that hire workers on UI. Others have suggested intensive job search assistance services or employer sponsored job training programs. Others have pointed out that 99 weeks is enough time to earn an Associate's degree. States could require UI claimants to study for a degree. Online technology would allow states to do this at low cost while allowing workers to study from home—and not disrupting their job search.

Congress does not know which of these programs will succeed and which will not. Congress should give states the flexibility to experiment with UI reforms, such as through a waiver system. States could innovate and policymakers would learn what works and what does not. Congress should allow the states to innovate.

Congress should also give states more flexibility under the existing system. The stimulus funded a $25 increase in weekly UI payments. To prevent states from simply reducing their UI benefits by an equal amount Congress passed a "non-reduction" rule. The rule prevents states from reducing their UI benefit amounts. Congress did not renew the supplemental federal payment, but the non-reduction rule remains on the books. This has handcuffed states as they try to close shortfalls in their UI trust funds. Several states have turned to cutting their weeks of benefits to reduce costs. Congress should once again let states determine the appropriate mix of benefit levels and duration.

Conclusion

Although two years of benefits is excessive, extending the duration of UI benefits in a recession is reasonable. However, the arguments for this policy should rest on humanitarian grounds. U.S. and international evidence shows that spending more on UI moderately increases unemployment. It has not and will not stimulate the economy.

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Testimony of Judith M. Conti, Federal Advocacy Coordinator
National Employment Law Project
Before the U.S. Congress Joint Economic Committee

February 7, 2012

The National Employment Law Project (NELP) is a 501(c)(3)national non-profit organization that engages in research, education, litigation support and policy advocacy on issues affecting low wage and unemployed workers. In partnership with national, state and local organizational allies, NELP works to maintain strong federal and state programs of unemployment insurance (UI) benefits that are providing a lifeline of support for individuals who, through no fault of their own, remain jobless after exhausting their state UI benefits. These federal benefits have kept millions out of poverty and are pumping vital stimulus into local economies. On an ongoing basis, NELP also engages directly with unemployed workers to help them assess and address the problems they are facing in trying to find work in an economy that, though growing modestly, is not creating enough jobs to meet the employment demand.

As we address below, though we are in a period of recovery and have seen promising trends of job growth in recent months, unemployment still remains unacceptably high and long-term unemployment remains dangerously high. Thus, while we are pleased with the general economic trends we are seeing, it is important to stress that the long-term unemployed, in particular, are still suffering badly and not sharing in the recovery nearly enough. Therefore, it is crucial for Congress to maintain the robust support it has provided for the unemployed over the past three years, and refrain from either eviscerating that essential life-line, or enacting unnecessary and harmful barriers to benefits that would impair the important economic functions of the UI safety net in the future.

A Crisis of Long-Term Unemployment Persists Because of Inadequate Job Creation

America is in the midst of a near-unprecedented crisis of long-term unemployment. Of the 12.8 million officially unemployed workers in January, 42.9 percent—nearly six million—had been unemployed for six months or longer. Average durations of unemployment in November reached a record high of almost 41 weeks and have only come down slightly, registering 40.1 weeks in January. As NELP recently reported, the rate of long-term unemployment has equaled or exceeded 40 percent for roughly the last two years, the longest stretch of such high long-term unemployment since this data was first reported in 1948.[1] Finally, there are roughly 8.2 million people who are under-employed – they want to be working full-time but can only find part-time hours.

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[1] National Employment Law Project, "Unemployment Insurance: Jobless Workers and Our Economy Hanging on by a Thread," October 2011, p. 4 (url: http://www.nelp.org/page/-/UI/2011/NELP_UI_Extension_Report_2011.pdf?nocdn=1)

Combining the unemployed, the under-employed and marginally attached workers, those who have not looked for work recently but still want to work and are available to do so, the "real" unemployment rate is 15.1%. Again, this number is trending downward, but it's still unacceptably high.

The principle reason for sustained high rates of long-term unemployment is that employers are simply not creating enough jobs to put Americans back to work. The nation's jobs hole is deep and competition for job openings is stiff.

Although job creation has been anemic since job growth resumed in the summer of 2010, the good news is that over the past six months, average job growth has slightly exceeded population growth. Nevertheless the jobs deficit—the hole we need to fill to restore employment levels to pre-recession status—remains deep.

As shown in NELP's recent analysis, the economy must add another 6.1 million jobs to make up for those lost during and in the aftermath of the 2007 recession, along with an additional 4.7 million jobs to account for growth in the working age population since there. Altogether, this amounts to a deficit of 10.8 million jobs. Closing this gap in three years would require the addition of 400,000 jobs per months on average—a level more than twice as great as average job growth of the past six months.[2] Plainly, job creation is simply not keeping up with the demand for work, either from the unemployed or from new work force entrants.

Comparing new job openings to official unemployment levels underscores the gap between the supply of individuals who want to work and the opportunities available to them. In November (latest comparative data available), there were more than four officially unemployed workers (13.3 million) for every new job opening (3.2 million). This gap has persisted for nearly three years. Under the best of circumstances, job competition would be stiff when the ratio of applicants to openings is greater than four to one. But even this figure understates the real level and intensity of job competition as it relates to the unemployed. Official unemployment counts do not include the under-employed—those who want full-time hours but are able only to get part-time work—or individuals "marginally attached" to the labor force, that is those who want to work and have looked for jobs in the past year but not in the preceding month. Including these individuals in official unemployment counts would nearly double the number of potential unemployed or under-employed applicants for each vacancy. Of course, anecdotal evidence suggests there are numerous applicants for every job opening, with thousands showing up at job fairs.

[2] National Employment Law Project, "Jobs deficit ticks down to 10.8 million," January 6, 2012 (url: http://www.nelp.org/page/-/Press%20Releases/2011/nelp.jobs.deficit.december.pdf?nocdn=1

Unemployment Benefits Are Modest and Hold the Line Against Poverty

Consistent with President Franklin D. Roosevelt's ambitious vision for the unemployment insurance program when it was created more than 75 years ago, the federal UI benefits have made all the difference in the lives of millions of families suffering from the fallout of the jobs crisis. New evidence from the states also puts to rest the exaggerated claims of some detractors that the modest unemployment benefits have motivated unemployed workers to avoid seeking work. The reality, especially in today's severe labor market, could not be further from the truth.

Today's average unemployed worker on the federal extension receives just $296 in weekly unemployment benefits. That represents only 50 percent of the income needed to cover the most basic necessities of food, housing, and transportation, as measured by the annual Consumer Expenditure Survey.[3] While the average American family spends $1,380 per month on housing alone, the average monthly unemployment benefit is only $1,283. Put simply, today's unemployed workers are not living the high life on jobless benefits.

Yet these benefits, modest as they are, have gone a long way to prevent economic hardship for millions of families since the recession began in 2007. In 2010 alone, according to recently released Census figures, unemployment benefits kept 3.2 million Americans out of poverty. The Census Bureau reports that in 2010, poverty increased by 2.6 million people over 2009 levels; however, the unemployment insurance program kept an even greater number of Americans from slipping into poverty. Indeed, were it not for unemployment benefits, the increase in the number of Americans in poverty would have more than doubled, from 2.6 million to 5.8 million people. To put these figures in perspective, the number of people protected against destitution has increased nearly sevenfold since 2007 thanks to the unemployment program.

Significantly, unemployment insurance has played a more prominent role in alleviating child poverty during the course of the recession. According to the Bureau of Labor Statistics, the share of families with at least one member unemployed during the year climbed to 12.4 percent in 2010, the highest rate since the data series began in 1994. This 12.4 percent figure, which represents a total of 9.7 million families, was nearly double the 6.3 percent of families reporting at least one jobless member in 2007, when the recession officially began. In 2010, children accounted for over a quarter (27 percent) of all those who were kept out of poverty due solely to the support their families received in the form of unemployment benefits (900,000 in total).

[3] These monthly figures for selected expenditures are derived from the 2010 annualized data reported by the Bureau of Labor Statistics. See Bureau of Labor Statistics, Consumer Expenditures Survey News Release (September 27, 2011).

Thus, the federal investment in unemployment benefits has an immediate payoff for those kept out of poverty, but it also produces long-term dividends for children and families given the social costs associated with child poverty and severe economic hardship. Children who experience economic hardship are more likely to drop out of school, suffer from poor health, and experience difficulty maintaining stable employment as adults. The National Center for Children in Poverty has documented the invaluable role that economic stability plays in laying the groundwork for later school achievement, economic productivity, and responsible citizenship.

Federal Jobless Benefits Provide a Boost to the Economy

It is easy to appreciate how much unemployment insurance benefits mean to families struggling to get by when they are unemployed. A few hundred dollars a week may be enough to keep a family out of poverty or avoid losing a home while an unemployed family member scrambles to find work. Narrowly focusing on individual circumstances, however, ignores the equally important and positive role unemployment insurance plays in the overall economy and the broader labor market.

Over the years, several exhaustive studies have documented the "countercyclical" impact of unemployment insurance in lifting up an economy that has been beaten down by a recession. The most recent such study, authored by Wayne Vroman of the Urban Institute, reviewed the role unemployment benefits have played during the most recent economic downturn from 2007 to 2010.[4] Consistent with the prior research, Vroman found that the nation's economy grew by $2 for every dollar spent on unemployment insurance during the latest recession, as unemployed workers spent their benefits in their communities at grocery stores, gas stations, and other retail and service outlets. And time and time again, the non-partisan Congressional Budget Office rates UI benefits as among the most impactful economic stimuli possible.[5]

Moreover, billions of dollars that otherwise would not have been spent flowed directly from unemployed consumers to local businesses, which translated into hundreds of thousands of jobs created or saved by the federal unemployment insurance benefits. In fact, according to the Center for American Progress analysis of Vroman's findings, unemployment benefits saved or created 2.3 million jobs in the fourth quarter of 2009 (on an annualized basis).[6] Federal unemployment benefits were responsible for nearly

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[4] Vroman, Wayne, "The Role of Unemployment Insurance as an Automatic Stabilizer During a Recession" (Urban Institute, 2010), Table 4.3 Real GDP and Real Extended Benefits, 2008Q1 to 2010Q2.
[5] "Policies for Increasing Economic Growth and Employment in 2012 and 2013," CBO testimony before the U.S. Senate Committee on the Budget, November 14, 2011, http://www.cbo.gov/ftpdocs/124xx/doc12437/11-15-Outlook_Stimulus_Testimony.pdf; " Estimated Impact of the American Recovery and Reinvestment Act on Employment and Economic Output from July 2011 Through September 2011, November 2011, http://www.cbo.gov/ftpdocs/125xx/doc12564/11-22-ARRA.pdf.
[6] Boushey, Heather and Matt Separa, "Unemployment Insurance Dollars Create Millions of Jobs" (Center for American Progress, 2011).

half of those jobs (1.1 million), while regular state unemployment benefits accounted for the remaining half. The latest research provides compelling new proof that pulling the plug on the federal extension will produce a major drag on the nation's economy. The Economic Policy Institute estimates that if Congress maintains the 2011 level of federal UI benefits through 2012, it will be responsible for saving and/or creating over half-a-million jobs.[7]

Unemployment Benefits Enhances Job Search Activities by the Unemployed and Keeps Unemployed Workers Attached to the Workforce

Some detractors of unemployment insurance maintain that unemployment insurance recipients prefer to collect an unemployment check rather than seek or accept work, despite the desperate economic circumstances of families surviving on their modest unemployment benefits. Recent research by Professor Jesse Rothstein of the University of California at Berkeley roundly refutes that assertion. Evaluating the impact on the unemployment rate of workers collecting benefits under the recent federal extension, Professor Rothstein concluded that the effects are "quite small, too small to outweigh the benefits on transfers to people who have been out of work for over a year in conditions where job finding prospects are bleak."[8]

Rothstein's work is a careful study on the effects of UI extensions on job searches in the Great Recession. Although he finds a 0.3 percentage point increase in the December 2010 unemployment rate could be attributed to extended unemployment benefits, he also finds that at least half of this increase is due to the fact that receipt of UI benefits keep workers who it in the labor force, searching for jobs.[9] According to an analysis by the Economic Policy Institute (EPI), even this small increase may be overstating the impact of extended unemployment benefits.[10] EPI economists note that the Rothstein study does not account for the fact that unemployed workers greatly outnumber job openings, nor does it account for macroeconomic effects of UI benefits on unemployment rate.

Another recent analysis by researchers at the Federal Reserve Bank of San Francisco provides additional evidence that extended benefits are not a big driver of increases in the length of time that workers are unemployed.[11] In searching for an explanation of the dramatic rise during this recession of the average duration of a worker's unemployment, the researchers determined that weak labor demand is the primary

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[7] Michel, Lawrence and Shierholz, Heidi, "Labor Market Will Lose Over Half A Million Jobs if UI Extensions Expire in 2012," Nov. 4, 2011, http://www.epi.org/publication/labor-market-lose-million-jobs-ui-extensions/.
[8] Rothstein, Jesse, "Unemployment Insurance and Job Search in the Great Recession" (NBER, July 2011)
[9] Id.
[10] Lawrence Mishel and Heidi Shierholz, "Labor market will lose over half a million jobs if UI extensions expire in 2012', Economic Policy Institute (November 4, 2011)
[11] Rob Valletta and Katherine Kuang, "Why Is Unemployment Duration So Long?", FRBSF Economic Letter (January 30, 2012)

cause, not extended unemployment benefits. Using Bureau of Labor Statistics data on job openings to pinpoint labor market demand, they conclude that the "ratio of the total number of unemployed workers to job vacancies accounts for about 11.5 weeks of the 15.7 extra weeks of duration in 2010–11, explaining virtually all the increase in duration"[12]

Moreover, new evidence from two states further debunks these exaggerated claims, which are divorced from the reality of unemployed families living in today's economy. State agencies in Connecticut and Washington surveyed the conditions of workers who have reached the end of their state and federal jobless benefits. If, as the argument goes, unemployment benefits were motivating these workers to stay unemployed, it stands to reason that these workers would be looking harder and finding work just before their benefits run out, or shortly thereafter. But that is simply not the case.

In Connecticut, where 9.0 percent of working-age residents are unemployed, just one-quarter (24.7 percent) of the 43,172 workers who had exhausted their unemployment benefits over the second quarter of 2010 to the first quarter of 2011 were reemployed by the end of the next quarter. In Washington, where unemployment is 9.3 percent, the findings are consistent with the Connecticut survey.[13] Of those workers who exhausted all of their unemployment benefits, just one-quarter (24.4 percent) had found work. Of those exhaustees who had not found work, more than 86 percent said they were *still* looking for jobs—reaffirming that it is the desperate condition of the job market, and not unemployment benefits, that account for the continued high levels of long-term unemployment.

A recent survey and corresponding report by the John J. Heldrich Center for Workforce Development of workers who had lost jobs during the Great Recession is also directly on point. Analysis of survey results showed that "[u]nemployed workers who received [unemployment insurance] benefits were **more likely** to have been proactive in seeking work than those who did not receive UI" (emphasis in original), with benefits recipients reporting "more hours devoted to the job search and more frequently contact[ing] friends and examin[ing] job postings."[14] Continuing joblessness among the long-term unemployed was not because they were not looking for work. According to the Heldrich Center report, the unemployed participated in substantial job search activities, with three-quarters having applied for a job within the preceding month and two-thirds having searched newspapers and online job postings.

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[12] Id.
[13] For the Washington survey results, see Washington State Employment Security Department, "Unemployment Benefits Exhaustee Survey Report" (July 2011). The findings from Connecticut are drawn from "Following Connecticut's Unemployment Insurance Claimants Through the Recession," by Manisha Srivastava, Connecticut Department of Labor, Office of Research, October 2011.
[14] John J. Heldrich Center for Workforce Development, "The Long-Term Unemployed and Unemployment Insurance: Evidence from a Panel Study of Workers Who Lost a Job During the Great Recession," November 2011, p. 2 (url: http://www.heldrich.rutgers.edu/sites/default/files/content/UI_Unemployed_Brief.pdf)

Erecting Barriers to Unemployment Insurance Does Not Put the Unemployed Back to Work

During the 2011 debates about renewing federal unemployment extensions for 2012, House Republicans heaped criticisms on state unemployment insurance (UI) programs, primarily by claiming that the program is broken and requires major changes. As part of their critique, House Republicans offered a series of proposals in H.R. 3630, all of which would create new barriers to state UI benefits while drastically slashing the duration of federal UI benefits. Though these proposals are touted as "reforms," nothing could be further from the truth. Rather, these new barriers would abandon fundamental underpinnings of the federal-state nature of the basic UI program while leaving jobless workers without an appropriate safety net in a labor market that, while improving, still has been the worst since the Great Depression.

The fact is the UI program is *not* broken. If anything, the last few years have proven that even in the worst of economic times, the basic program functions just as intended by replacing part of the wages workers lose when they are laid off so that they have a safety net while looking for a new job, while at the same time stabilizing local economies.

Instead of doing anything to improve the UI system, the provisions in H.R. 3630 would make it harder for ordinary Americans who lose their jobs to access their unemployment insurance. It would subject workers to mandatory drug tests, disqualify workers who were not fortunate enough to finish high school, and allow states to experiment with new workfare-type requirements that have no place in a social insurance program in which unemployed Americans' work has paid for the insurance to provide wage replacement when out of work. Far from being real and meaningful "reforms," these barriers to benefits are politically motivated solutions in search of problems.

If lawmakers really want to improve the UI program, they would not be erecting new barriers to benefits, but would instead adequately fund job search assistance and reemployment programs. They would provide state agencies with the resources needed to help jobless workers re-enter the workforce. But these kinds of *real* reforms are not part of the House package. At a time when the UI program remains crucially important to millions of workers, their families, and national and local economies, H.R. 3630 proposes only mean-spirited and punitive barriers to benefits that begin to dismantle the UI system, and do nothing to create jobs, improve the economy, or help unemployed workers get back to work.

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Congress Should Reject Waivers of Federal Law Protecting Against Abuses of Dedicated UI Trust Funds

As stated by the bi-partisan federal Advisory Council on Unemployment Compensation in 1995, "[t]he most important objective [of UI] is the provision of temporary, partial wage replacement as a matter of right to involuntarily unemployed individuals who have demonstrated a prior attachment to the labor force."[15] Under federal law, UI was exclusively established to insure employees from the hazards of wage loss due to involuntary unemployment and is funded and paid solely in relation to unemployment. In other words, eligibility for UI benefits is not conditioned upon other factors unrelated to unemployment, like income or education levels. UI is a social insurance program, like Social Security and Medicare, plain and simple. As such, in order to ensure that UI meets its major objective, federal law has always provided that payroll taxes can be withdrawn from dedicated UI trust funds "solely for payment of unemployment compensation."

Rather than openly trying to repeal longstanding federal protections for UI recipients, H.R. 3630 would instead allow states to be granted waivers to use UI funds for purposes other than paying UI benefits. This may sound harmless at first blush, but in fact, this would mean a dramatic shift in the UI program's most basic principles and begin the unraveling of the program. In particular, H.R. 3630 would permit up to 10 states each year to get waivers from key federal UI law requirements for purposes of operating "demonstration projects" for up to five years, each allegedly designed to promote more rapid reemployment of jobless workers. Notably, there is no overall limit to the number of demonstration project waivers that could operate under the H.R. 3630 proposal.

These waivers would have immediate, negative impacts on UI programs. First, waivers would permit states to use scarce UI trust funds for purposes other than the payment of UI benefits to jobless workers. Second, federal waivers could permit demonstration projects that condition payment of UI benefits upon reasons unrelated to involuntary unemployment; namely, income limits, education requirements, or other reasons not related to each UI claimant's unemployment. Third, allowing waivers of the administrative standards established in the Social Security Act would eliminate long-standing UI program safeguards that require states to make eligibility decisions and pay benefits to unemployed workers promptly. Ultimately, allowing states not to comply with these three basic obligations is giving states license to take the element of insurance out of unemployment insurance.

Equally important, proponents of these waivers are offering a solution to a problem that doesn't, in fact, exist. States already have broad authority under existing federal UI guidelines to define labor market attachment eligibility rules, benefit levels, and

[15] Advisory Council on Unemployment Compensation (1995), statement of purpose cited in *Defining Federal and State Roles in Unemployment Insurance: A Report to the President and the Congress*, p. 28 (January, 1996).

disqualification penalties for separations other than layoffs. And states are currently free to use non-UI funding for reemployment and job search assistance. In fact, many states have demonstrated that they already have the capability of accelerating the return of UI claimants to work within the parameters of existing state and federal UI law through effective reemployment services. In Washington State, for example, staff-assisted placement services reduced UI claimants' duration of unemployment by 7.7 weeks.[16] Wisconsin provides expanded reemployment services for UI claimants and increased collaboration between the UI program and Employment Services, which have reduced the average duration that claimants receive benefits by between 0.6 and 0.9 weeks.[17]

Drug Testing the Unemployed Penalizes and Stigmatizes Honest Workers and Pointlessly Burdens State UI Agencies

When Congress created the UI program in 1935, the Senate report accompanying the legislation spelled out that UI *"differs from relief in that payments are made as a matter of right not on a needs basis, but only while the worker is involuntarily unemployed."* Federal UI law has been consistently interpreted to prohibit states from restricting benefit receipt based upon conditions unrelated to the "fact or cause of worker's unemployment." State statutes governing eligibility and disqualification already ensure that workers who collect benefits were sufficiently attached to the labor force and have the capacity to rejoin it. Requiring a claimant to pass a drug test is an additional qualification that goes beyond the "fact or cause" of the worker's unemployment. That is why the U.S. Department of Labor, under both Democratic and Republican administrations, has stopped states from implementing such programs.

There is no reasonable basis to subject the unemployed to a drug testing requirement, and proponents of this proposal cite no data or verifiable evidence showing any need for such testing. While it may make for a good sound bite in certain circles, it is, in reality, a not-so-subtle attack on the character of unemployed Americans. This proposed draconian over-reach seems rooted in a blanket assumption that unemployed workers are to blame for their own unemployment and that the ranks of the unemployed are crowded with lazy drug abusers.

Moreover, the UI system already appropriately penalizes job-related drug use. Twenty states already explicitly deny benefits for any job loss connected to drug use or a failed drug test. And based on the laws on the books in the remaining states, they would also likely treat a drug-related discharge as disqualifying misconduct even though it is not explicitly referenced in their discharge statutes. Thus, states already restrict eligibility for workers whose job loss is related to drug use.

[16] Testimony of Karen Lee, President of the National association of State Workforce Agencies, before the Senate Finance Committee, April 15, 2010.
[17] Id.

And employers already have testing as a tool to screen out drug users. Pre-employment drug testing has become a standard part of the hiring process for millions of employers. Recruiters estimate that more than half of newly hired employees are subject to a pre-employment drug screen.[18] Employers have the capacity to screen out applicants who use illegal drugs without a program of government testing.

Finally, large-scale government drug-testing would be very expensive, and the cost would greatly outweigh any slight benefits. At a time when there are not enough resources to adequately fund and staff state UI programs, layering on a bureaucratic new qualifying requirement would be very expensive and senseless. As a conservative figure, the Substance Abuse and Mental Health Services Administration estimates the cost for drug testing to be between $25 and $75 per test.[19] As federal law prohibits assigning this cost to claimants, states would have to absorb the cost of drug testing thousands of unemployed workers. In March 2011, the Texas Legislative Budget Board estimated the full year cost of implementing such a program in Texas to be nearly $30 million.[20]

Two recent examples of drug testing recipients of federal assistance show the folly in such programs. Florida recently started drug testing in the TANF cash assistance program. The testing, which has been halted by a federal judge on grounds that it likely violates the Fourth Amendment's protection against unreasonable search and seizure, revealed positive results in only two percent of applicants, a rate substantially below the CDC's estimate of 8.5 percent drug-use rate in the general population.[21] An Indiana requirement to drug test unemployed applicants for a government training program yielded an even more paltry one percent positive result. Indiana spent $45,000 to drug test approximately 1,240 people, and only 13 individuals tested positive.[22]Spending an average of $3,500 per applicant to root out only one drug user for every 95 tested is hardly a good use of scarce resources.

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[18] Drug Testing Efficacy Poll, Society for Human Resource Management, http://www.shrm.org/Research/SurveyFindings/Articles/Pages/lDrugTestingEfficacy.aspx.
[19] U.S. Department of Health and Human Services Substance Abuse and Mental Health Services Administration (SAMHSA) Drug Testing Facts and Statistics Fact Sheet, http://workplace.samhsa.gov/WPWorkit/pdf/drug_testing_facts_and_stat_fs.pdf.
[20] 9Texas Legislative Budget Board Fiscal Note, 82nd Legislative Regular Session, March 24, 2011, http://www.legis.state.tx.us/tlodocs/82R/fiscalnotes/html/HB00126I.htm.
[21] "Welfare Drug Testing Yields 2 Percent Positive Result," Tampa Bay Tribune, August 24, 2011, http://www2.tbo.com/news/politics/2011/aug/24/3/welfare-drug-testing-yields-2-percent-positive-res-ar-252458/.
[22] http://abclocal.go.com/wls/story?section=news/local/indiana&id=8483514.

Requiring UI Claimants to Have or Pursue a High School Diploma or GED is a Misguided and Impractical Barrier to Benefits

For the first time in federal law, H.R. 3630 would establish as an eligibility requirement that all UI recipients have a high school or general educational development (GED) degree, or be making sufficient progress toward getting such a degree. While states could waive this requirement for individuals for whom it would be unduly burdensome, the legislation provides no standards guiding this waiver, and it is a requirement that should not exist in the first place.

Let me be clear: NELP is very much in favor of adult workers getting the additional training and education they need in order to be successful in the workforce. We are enthusiastically support the Workforce Investment Act, Trade Adjustment Assistance, and publicly funded job training programs. But there is an appropriate way to incentivize workers to receive training and education, and an entirely improper way to force GEDs though the UI system. Indeed, even the National Coalition for Literacy, a group whose mission is "[t]o advance adult education, family literacy, and English language acquisition in the U.S. by increasing public awareness for the need to increase funding and programs; promoting effective public policy; and serving as an authoritative resource for the field on national adult education issues," has said that the GED requirement would be "going against common sense," and is actively working to oppose this misguided proposal.[23]

First, as noted earlier but it bears repeating: UI is a social insurance program in which eligibility is driven *solely* by loss of employment, attachment to the workforce, and employer payments into the applicable UI trust funds on behalf of the employee, *not* income level, educational attainment, or other characteristics of unemployed workers. Employer contributions are made for the entire workforce, including those without high school diplomas or GEDs, not simply those with certain characteristics.

Second, this proposal would have a significant negative impact on unemployed workers with low education levels who have been dramatically affected by the recent recession. A survey of a random sample of claimants who had weeks compensated in the regular program during 2010 found that between 13 and 14 percent have not completed high school or the equivalent.[24] Given that there were 2.2 million successful new claims of unemployment payments in the third quarter of 2011, this educational requirement would have affected about 284,000 people in one quarter alone – leading either to a denial of benefits or forced enrollment in adult education courses.

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[23] "Going Against Common Sense: Denying Undereducated Workers UI Benefits," January 17, 2012, http://blog.ncladvocacy.org/2012/01/going-against-common-sense-denying-undereducated-workers-ui-benefits/; http://www.national-coalition-literacy.org/uibenefits.html.

[24] Center for Law and Social Policy (CLASP) calculations based on data provided by the Employment and Training Administration, U.S. Department of Labor. See also, "Beyond Basic Skills," Center for Law and Social Policy, March 2011, http://www.clasp.org/admin/site/publications/files/Beyond-Basic-Skills-March-2011.pdf.

Third, this provision would have a huge impact on older workers. The Center on Budget and Policy Priorities recently reported that almost half of all UI claimants without a high school degree are over age 45, and 35 percent are over age 50. In addition, there were half a million UI claimants in 2010 who were age 50 and over without a high school diploma.[25] Does it make sense to require these older workers to return to high school just so that they can qualify for the unemployment insurance they have earned through their long work histories?

Fourth, this is a substantial unfunded mandate on the states, at a time when they can least afford to cover the costs. State funding, a traditionally robust source of funding for adult education, is becoming less reliable as a result of crumbling state revenues. Moreover, it is unlikely that state programs could accommodate a new surge in enrollment. A survey conducted during the 2009-2010 program year found that nearly every state had a waiting list for adult education/ESL services, and that nearly three-quarters of local programs reported waiting lists. About 160,000 learners across the country were on these lists, and the number of months on the waiting list has increased since the previous survey, with 81 percent reporting waiting lists of two months or longer.[26]

Congress Must Maintain the Rule Limiting State Cuts in Weekly Unemployment Benefits When the Federal Extensions are in Place

H.R. 3630 would eliminate the "non-reduction rule" that has been in place since February 2009. This rule bars states from cutting the weekly amount of state benefits they provide claimants as long as the state is accepting money to pay EUC. The purpose was to insure that states did not undermine the stimulative impact of federal dollars by changing their formulas in a way to reduce the corresponding UI dollars paid out under the state program.

Despite the clear intent of Congress, some states found a way around this rule in 2011 and cut the UI dollars paid out under the state program by reducing the total number of weeks of benefits. Six states reduced the maximum available benefits below the historic standard of 26 weeks, with three states cutting the limit to 20 weeks, and one state (Florida) creating a sliding scale that could reduce its maximum to as low as 12 weeks.[27]

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[25] Robert Greenstein, Hannah Shaw and Chad Stone, "Hundreds of Thousands of Lower-Wage Workers, Many of Whom Worked for Decades, Would be Denied Unemployment Insurance Under Provision Now Under Consideration," Center on Budget and Policy Priorities, January 6, 2012, http://www.cbpp.org/cms/index.cfm?fa=view&id=3652.
[26] Id.
[27] Claire McKenna and George Wentworth, "Unraveling the Unemployment Insurance Lifeline: Responding to Insolvency, States Enact Cutes in 2011, August 2, 2011, http://www.nelp.org/page/-/UI/2011/Unraveling_UI_Lifeline_Report.pdf?nocdn=1.

States claim to be doing this in an attempt to deal with the extreme solvency problems many have experienced as their trust funds have run out of money, and they've been forced to borrow from the federal government in order to make payments on state UI claims. But the assertion is misguided at best, and more often, disingenuous. State UI trust funds are NOT in such bad shape because of the claims levels or the claims amounts. The problem lies in at least a decade of neglect and poor fiscal management of the trust funds – of a failure to "forward fund" and build up the trust funds while economic times were good. Instead, states abandoned this hallmark principle of UI funding and, bowing to the pressure of corporate lobbyists, granted a series of unwise tax cuts to employers during a stronger economic periodic when the taxes were affordable and sound cushions could be built. [28] It is regrettable that the price of that profligacy is such great trust fund indebtedness, but unemployed workers did not create this crisis and they should not be doubly victimized now—unable to find work and unable to collect the unemployment insurance benefits they worked for and earned. The appropriate response to the indebtedness crisis is to raise employer taxes in order to pay down debts and restore solvency to state trust funds. But, it is true that this is not an opportune time for employers to have to pay larger UI taxes. That is why NELP supports the Unemployment Insurance Solvency Act of 2011 (S. 386) introduced by Senator Richard Durbin of Illinois. This bill would waive employer taxes for two years, as well as state interest payments on the UI trust fund loans, in exchange for states entering into voluntary agreements with the U.S. Department of Labor to enact sensible policies to get their trust funds solvent and ready for the next recession.[29] This approach is far superior to one that leaves the states without any incentives for making smart choices in how to repair their UI trust funds.

Eliminating the non-reduction rule would give states even more leeway to do harm to the underlying state UI programs that are still so desperately needed. Congress should, in fact, be strengthening the non-reduction rule to prohibit states from cutting their existing maximum weeks of benefits as long as they receive federal EUC dollars. Were Congress to eliminate the one provision that requires states to keep their part of the deal to help the unemployed in these economic hard times, it would be akin to an open invitation for states to slowly and surely abandon them and the communities in which they live and hope to work.

H.R. 3630 Usurps Established Authority of States to Determine Their Own Standards for UI Eligibility and Repayment, While Penalizing Millions of Deserving Workers

It is ironic that H.R. 3630, which purports to give states flexibility in administering their UI programs (through waivers, for example) actually imposes severe eligibility mandates that create new burdens for states and tie their hands in program administration.

[28] "Rebuilding the Unemployment Insurance System: A Deficit-Neutral Plan that Limits Tax Increases and Maintains Benefits," National Employment Law Project and Center on Budget and Policy Priorities, February 9, 2011, http://www.nelp.org/page/-/UI/UI%20Solvency%20Report%20FINAL.pdf?nocdn=1.
[29] http://www.nelp.org/page/-/UI/2011/solvency.leg.summary.04.05.2011.pdf?nocdn=1.

Redundant Work-Search Requirements: H.R. 3630 requires every state to establish new work-search documentation requirements for every week of benefits claimed for regular state UI benefits, not just the federal programs. States already mandate that UI claimants must be available for suitable work and that they must make their best efforts to find a new job. But H.R. 3630 further mandates that states develop and implement expensive new programs to track where and when unemployed workers have applied for jobs. The "documentary evidence" requirement for each and every week of benefits claimed creates huge new administrative burdens for states already straining from the unprecedented demands imposed on them – demands the agencies simply do not have the resources to meet. The proposed job search mandate is an anachronistic form of enforcement that is so expensive and unwieldy, state administrators across the political spectrum have uniformly supported a proposal to eliminate it altogether from the Extended Benefits program. And of course, there is no funding provided for states to meet this extreme administrative burden.

Expecting workers collecting UI benefits to look for work is entirely reasonable, and that is why states already do so. State UI agencies already have the flexibility to review the job search efforts of UI claimants through whatever systems work best in their states. State UI agencies know that some workers on temporary layoff will return to their jobs in a week or two and that it makes no sense to require these workers to look for new jobs and comply with bureaucratic documentation requirements. States do not need the new unfunded across-the- board mandates that H.R. 3630 would impose. The problem is not workers' lack of effort in searching for jobs; it is lack of jobs.

Draconian Rules on Overpayments: Currently, federal law authorizes states to recover federal and state UI benefits that are overpaid, whether due to innocent error on the part of the agency, workers, or employers, or because of claimant fraud. In fact, of the relatively small share of all UI payments that are determined to be improper "overpayments," only about one-quarter are attributable to claimant fraud (only 2 to 3 percent of all UI payments).[30] States have a full range of collection tools and legal remedies for recovering both categories of overpayments, and most states employ appropriately tough collection rules in fraud cases. Indeed, just a few months ago, Congress authorized states to intercept federal income tax refunds to collect benefits overpaid due to fraud.

However, most states have also carefully crafted rules to insure that workers are treated fairly when an overpayment issue arises, especially in cases involving honest errors by the agency or the worker. These errors can produce overpayments of thousands or even tens of thousands of dollars because they are often detected weeks or months after the claimant began filing. As a result, these determinations can impose extreme financial

[30] U.S. Department of Labor, Unemployment Insurance (UI) Improper Payments By State, http://www.dol.gov/dol/maps/Data.htm.

hardship on unemployed workers to repay the benefits. As a result, about half the states authorize a "waiver" of part or all of these overpaid benefits in cases of "equity and good conscience," i.e., when the worker did nothing to defraud the state agency and where repayment would be unfair and unduly burdensome.

With a simple one-word change in the federal law,[31] substituting "may" for "shall," H.R. 3630 would require states to collect *all* overpaid benefits, robbing them of any discretion to consider the cause of the overpayment or the financial circumstances of the worker. This preemption of long-standing reasonable state protections would come at a time when the state UI systems are dealing with a high volume of non-fraud overpayments that are attributable to errors that result from the complexity of dealing with on-line and telephone claim-filing systems. In addition, many overpayments result from employers and their third-party representatives routinely failing to respond timely to state agency requests for information or delaying their objection to a claim until benefits have already been approved.[32]

Congress Should Make Proven Reemployment Tools for Jobless Workers a Priority

Rather than presuming that lagging efforts by UI claimants are a major reason for long-term unemployment, or that drug use is a major barrier to reemployment, justifying across-the-board drug testing of jobless workers, Congress should prioritize UI reforms directed toward implemented reemployment tools with a proven record.[33] Instead of limited and somewhat symbolic reemployment demonstration projects under a waiver approach, the following reemployment tools should be adopted and funded immediately.

Support Effective "High Quality" Job Search Assistance. To preserve workers' skills and channel those skills into jobs for which they are best suited, workers should not to be forced to apply for and accept jobs that are not suitable to their education and skill level as part of regular UI benefit requirements. Instead, workers should receive effective reemployment assistance, including personal attention, referrals and placement in job openings, and counseling on work search plans, all strategies that have proven effective in getting workers back to work as quickly as possible.[34]

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[31] 26 U.S.C. 3304.

[32] Jason DeParle, "Contesting Jobless Claims Becomes a Boom Industry," New York Times, April 3, 2010, http://www.nytimes.com/2010/04/04/us/04talx.html?pagewanted=all.

[33] Christopher T. King and Carolyn J. Heinrich, University of Texas, "How Effective Are Workforce Development Programs? Implications for U.S. Workforce Policies," Paper Presented at APPAM Fall Research Conference (November 2011), http://www.utexas.edu/research/cshr/pubs/pdf/King-Heinrich-APPAM-10222011.pdf.

[34] Paul Decker, Robert Olsen, Lance Freeman and Daniel Klepinger, "Assisting UI Claimants: The Long-Term Impacts of Job Search Assistance Demonstration," USDOL Occasional Paper 2000-02, (2000), http://wdr.doleta.gov/owsdrr/00-2/00-02.pdf; Stephen Woodbury, " Long Term Effects of the Work Test and Job Search Assistance: Reexamining the Washington Alternative Work Search Experiment" (2001), http://econ.as.nyu.edu/docs/IO/14690/Woodbury_20100412.pdf.

The Employment Service (ES) was established by the Wagner-Peyser Act in 1933 as the nation's public labor exchange mechanism. It is a system that benefits both workers and employers, enabling employers to find qualified workers more quickly and employees to gain reemployment or better employment. UI plays a role in unemployed workers' return to work by requiring that claimants register for work, and disqualifying those who refuse offers of suitable work. In addition to its public labor exchange functions, the Employment Service was charged with enforcing the UI work search test. And starting in 1995, all UI claimants are "profiled" by state UI agencies so that those who are deemed likely to exhaust benefits and need reemployment services are referred to such services with a suspension of UI benefits if they do not cooperate.

Despite its role in these important labor market functions, Employment Service funding under the Wagner-Peyser Act has remained at roughly $700 million for many years under administrations of both political parties. And despite expressed concern about enforcing the UI work search test on the part of employers and UI critics, the public Employment Service has languished as an "orphan program" that receives little attention or support. Employment services are important because they are universal and available to both employed and unemployed job seekers as well as UI claimants and jobless workers who have exhausted UI. To a significant extent, few job referrals are made to UI claimants in many states due to the decline in ES services.[35] In Michigan, job seekers must rely upon computer job listings as the sole public labor exchange tool available statewide, and few employers post job openings to the public computer listings.

In contrast to its neglect by Congress and several administrations, there is general agreement among program evaluators that ES job referrals and job search assistance "is highly cost effective,"[36] returning as much as $4.50 to taxpayers for every dollar spent.[37] Studies by Lou Jacobson, President of New Horizons Economic Research and a nationally recognized expert on the costs and benefits of workforce development programs, demonstrate that personal contact by trained personnel with jobless workers can particularly help shorten time spent on UI benefits. He has found that states could improve job search assistance and shorten unemployment spells by increasing the number of unemployed individuals who visit one-stops for group workshops and one-on-one counseling; expanding job development (i.e., employer outreach) to ensure that more jobs are listed on public labor exchanges; and providing assessment and counseling for potential trainees to determine what type of training, if any, would be

[35] *See* Christopher J. O'Leary and Randall W. Eberts, "The Wagner-Peyser Act and U.S. Employment Service: Seventy-Five Years of Matching Job Seekers and Employers," Upjohn Institute (2008), http://research.upjohn.org/cgi/viewcontent.cgi?article=1032&context=reports, for a general account of these trends.

[36] O'Leary and Eberts, *supra*, p. viii; Louis S. Jacobson, "Strengthening One-Stop Career Centers: Helping More Unemployed Workers Find Jobs and Build Skills," Brookings Institution (2009), p. 8, http://www.brookings.edu/papers/2009/0402_jobs_skills_jacobson.aspx.

[37] Jacobson (2009), p. 29.

most beneficial.[38] His work calls particular attention to automation used in Oregon and Washington that immediately lists job openings and notifies job seekers of openings in their occupational fields.[39] Jacobson's findings about the success of Employment Services are all consistent with Assistant Labor Secretary Jane Oates' October 6, 2011 testimony before the House Ways and Means Subcommittee on Human Resources.[40]

Use Wage Subsidy Programs to Promote Reemployment.

Studies show that with each passing month workers are unemployed, they face more obstacles to reemployment. Subsidized employment programs, in which a worker's wages are subsidized for a given period of time, have a proven record of promoting reemployment for disadvantaged workers. They give jobless workers a chance to reestablish connections to paid employment and revive employer confidence in their viability as productive employees.[41]

A recent example of wage subsidies was the TANF Emergency Fund created under the Recovery Act. The District of Columbia and 39 states operated subsidized jobs programs, putting nearly 260,000 people to work, until the majority of programs ended in late 2010 with the expiration of Recovery Act funding.[42] These programs were highly effective in reaching the long-term unemployed. In Illinois, for example, 39 percent of the 27,000 participants in its Put Illinois to Work program had been out of work for two years prior to the program, and all participants, on average, had been out of work for an average of 15.4 months.[43] A similar wage subsidy model was adopted by Mississippi,

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[38] Based on previous demonstration projects, Jacobson estimates that UI weeks claimed could be reduced by 1.1 weeks for claimant call-ins, 2.8 weeks for job search assistance, 3.8 weeks for job development, and 0.8 weeks for counseling for potential trainees. Id. at p. 24, Table 2A.

[39] "Powerful evidence has accumulated that high-quality job search assistance helps claimants return to work more quickly with no negative effects on future earnings." Jacobson (2009), p. 18-20, 29; Louis S. Jacobson, Ian Petta, Amy Shimshak, and Regina Yudd, "Evaluation of Labor Exchange Services in a One-Stop Delivery System Environment: Final Report," USDOL Employment and Training Occasional Paper 2004-09 (2004), http://wdr.doleta.gov/research/FullText_Documents/Evaluation%20of%20Labor%20Exchange%20in%20One-Stop%20Delivery%20System%20-%20Final%20Report.pdf; Louis S. Jacobson and Ian Petta, "Measuring the Effect of Public Labor Exchange," USDOL Office of Workforce Security Occasional Paper 2000-06 (2000), http://wdr.doleta.gov/owsdrr/00-6/00-6.pdf.

[40] Testimony of Jane Oates, Assistant Secretary, Employment and Training Administration, DOL, at an October 6, 2011 hearing, "Moving from Unemployment Checks to Paychecks: Assessing the President's Proposals to Help the Long-Term Unemployed."

[41] Timothy J. Bartik, "Adding Labor Demand Incentives to Encourage Employment for the Disadvantaged." *Employment Research*, Upjohn Institute for Employment Research (2009), http://research.upjohn.org/cgi/viewcontent.cgi?article=1079&context=empl_research.

[42] LaDonna Pavetti, Liz Schott and Elizabeth Lower-Basch. "Creating Subsidized Employment Opportunities for Low-Income Parents: The Legacy of the TANF Emergency Fund," Center for Budget and Policy Priorities and Center on Law and Social Policy (February 16, 2011), http://www.cbpp.org/cms/index.cfm?fa=view&id=3400.

[43] "Put Illinois to Work evaluation: An early look," Social IMPACT Research Center of the Heartland Alliance (October 2010), http://www.heartlandalliance.org/whatwedo/advocacy/reports/put-illinois-to-work.html.

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where Governor Barbour used the state's STEPS program to create 1,800 permanent jobs in less than nine months in 2010. In the 1980's, Minnesota pioneered a similarly successful wage subsidy program, the highly acclaimed MEED program, that specifically targeted the long-term unemployed.[44] Tim Bartik of the Upjohn Institute recently estimated that a similar program could assist many workers with reemployment in today's labor market.[45]

States' experiences with the TANF Emergency Fund program produced a number of strong models for successful subsidized employment programs that can lead to high levels of permanent job retention. Another promising pilot project in Connecticut has leveraged public and private resources and begun to pair training and wage subsidies for a pool of long-term unemployed workers who have run out of their unemployment insurance benefits.[46]

Adopt Work Sharing Programs. "Work sharing," "shared work," or "short-time compensation" are terms that refer to a UI program that serves as an alternative to layoffs during temporary declines in business. Under a work sharing program, an employer may reduce hours of its employees in lieu of worker layoffs. As a result, employees qualify for unemployment benefits to partially compensate them for the reduction in hours and pay they have experienced. If work sharing was not utilized, some of the employees would be laid off and draw full UI benefits, while the rest would remain fully employed. These programs are currently permitted, but not required, within our federal-state unemployment insurance laws. There are 23 states with functioning work-sharing programs.[47]

Participating employers are able to retain a skilled, trained workforce and do not incur new training costs when a business upswing occurs and laid-off workers are no longer available for recall.[48] In addition, by committing to workforce continuity and job security, employers enjoy the benefits of increased employee morale.[49] Significantly,

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[44] William Schweke, "Minnesota Emergency Employment Development Program (MEED)," CFED Newsletter, v. 3, no. 9 (September 2001).

[45] Timothy J. Bartik, "How a Renewed MEED Program Can Help Solve the Unemployment Problem," Upjohn Institute Presentation (November 12, 2009), http://www.upjohninstitute.org/bartik_meed_11-12-09.pdf.

[46] For more information on Connecticut's pilot program, see The Workplace Inc., www.theworkplace.org, and "Social Enterprise Initiative in CT Seeks Jobs for UI Exhaustees," UnemployedWorkers.org, June 19, 2011, http://unemployedworkers.org/sites/unemployedworkers/index.php/site/blog_entry/social_enterprise_initiative_in_ct_seeks_jobs_for_ui_exhaustees.

[47] These states are Arizona, Arkansas, California, Colorado, Connecticut, Florida, Iowa, Kansas, Maine, Maryland, Massachusetts, Minnesota, Missouri, New Hampshire, New York, Oklahoma, Oregon, Pennsylvania, Rhode Island, Texas, Vermont and Washington. In January 2012, Governor Chris Christie signed a New Jersey work sharing program into law.

[48] Neil Ridley, "Work Sharing – an Alternative to Layoffs for Tough Times," Center for Law and Social Policy (March 2009), p. 2, http://www.clasp.org/page?id=0009.

[49] Steven Greenhouse, "Work-Sharing May Help Companies Avoid Layoffs" The New York Times, June 15, 2009, http://www.nytimes.com/2009/06/16/business/economy/16workshare.html?pagewanted=all.

this program should not create additional UI costs for employers since the charges for one full week of UI benefits are equivalent to the charges for five employees each receiving 20 percent of a full week's benefits.

On the other side of the coin, workers retain their jobs and the financial security that comes with continuing employment. They are compensated for the unemployment they experience and are able to continue to meet their financial obligations and to contribute to their local economies. Workers retain their health insurance and keep accruing any retirement benefits in a properly structured program. In addition, employees avoid the economic and emotional hardship associated with layoffs, and the stress of looking for a new job in a tough labor market is averted.

Currently, work sharing is more prevalent in certain European countries than in the United States. In Germany, for example, widespread use of work sharing in the most recent recession is credited with keeping that country's unemployment rate substantially lower than other countries that experienced similar declines in GDP.[50] Even in limited use in this country, the work-sharing programs currently running in the United States saved an estimated 265,000 jobs in 2009 and 2010.[51]

President Obama's American Jobs Act, as well as legislation introduced by Senator Jack Reed (D-RI) and Rep. Rosa DeLauro (D-CT), would facilitate widespread adoption of work sharing programs within states and set national standards for short-time compensation to ensure that workers retain their health care and retirement benefits while participating in work sharing.[52] The proposed legislation would also provide $700 million in temporary funding to states that enact new work-sharing programs, covering implementation expenses and administrative costs associated with outreach and enrollment of employers. These relatively meager financial incentives are critical for taking work sharing to scale in states where it already exists as well as implementing programs in the remaining states and promoting the benefits of work sharing among employers and workers.[53] This small investment could reap significant returns in terms of successful layoff aversion in the future.

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[50] Dean Baker, "Work Sharing: The Quick Route Back to Full Employment," Center for Economic Policy and Research (June 2011) http://www.cepr.net/index.php/publications/reports/work-sharing-the-quick-route-back-to-full-employment.

[51] "Reed Calls for New National Plan to Help Save American Jobs," Press Release, July 6, 2011, http://reed.senate.gov/press/release/reed-calls-for-new-national-plan-to-help-save-american-jobs.

[52] U.S. Congress, House, Layoff Prevention Act of 2011, H.R. 2421, 112th Cong., 1st sess. (July 6, 2011). U.S. Congress, Senate, Layoff Prevention Act of 2011, S. 1333, 112th Cong., 1s t sess. (July 6, 2011). United States. Cong. House. H.R. 1950, Newborns' and Mothers' Health Protection Act of 1995. 104th cong. 1st sess. 8 June 1995. 14 Feb. 2004 . U.S. Congress, Senate, American Jobs Act of 2011, S. 1549, 112th Cong., 1st sess. (September 13, 2011).

[53] Kevin Hassett, "Testimony before the Joint Economic Committee, The Road to Economic Recovery: Prospects for Jobs and Growth," (February 26, 2010), http://jec.senate.gov/public/?a=Files.Serve&File_id=fdd8c30e-59a5-47c6-b482-9810229edb4c.

Conclusion

We all know that the root cause of the persistent long-term unemployment in the aftermath of the Great Recession is that there simply aren't enough jobs being created. There are still more than four times as many unemployed workers as there are available jobs. It is inconsistent with American values and bad for the American economy to penalize those who have suffered most as victims of the Great Recession by denying or reducing their unemployment insurance benefits, or to demonize them through unnecessary and stigmatizing barriers to participation in the program. Instead, Congress should reauthorize the federal unemployment insurance programs, immediately and without reductions or barriers to benefits, in order to provide for workers and families that continue to need this limited wage replacement, keep these workers actively engaged in the job search, and maintain the economic recovery.

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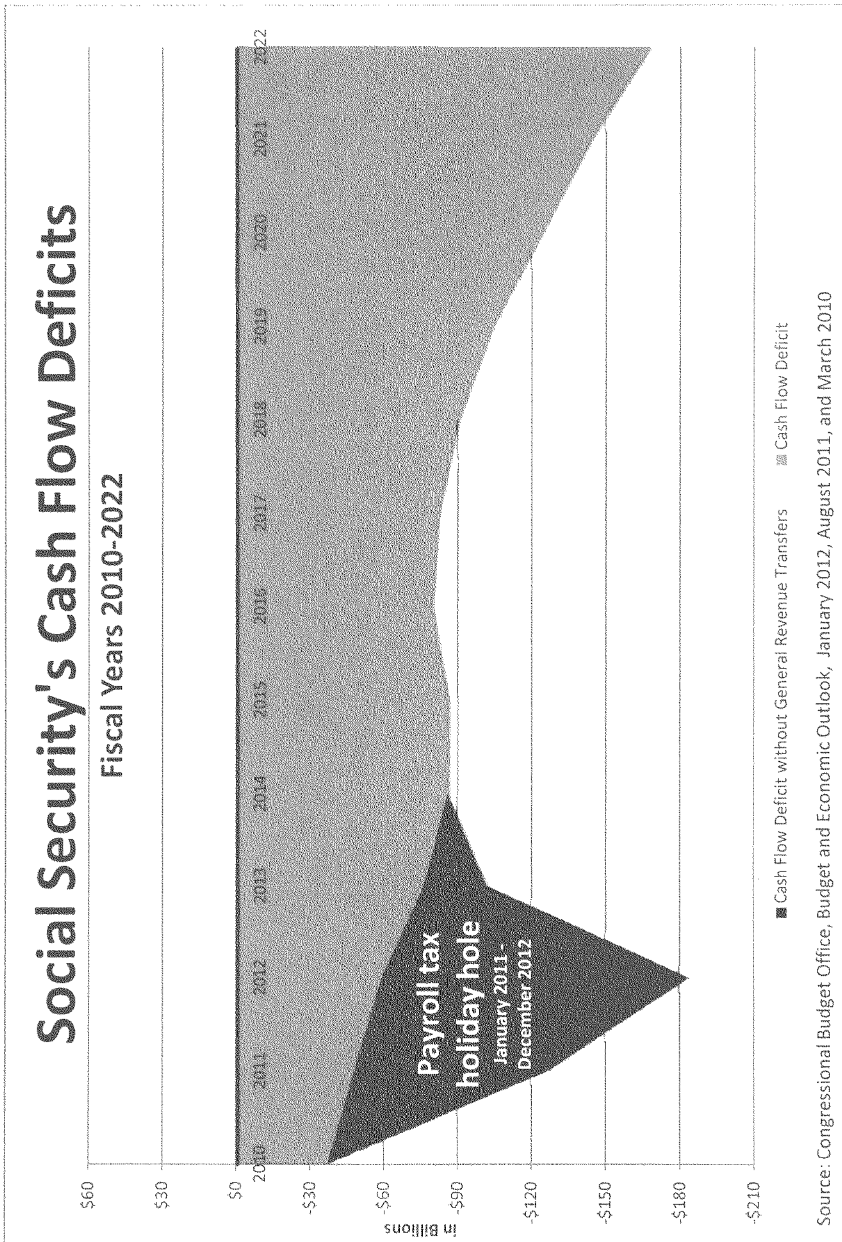
Social Security's Cash Flow Deficits
Fiscal Years 2010-2022
in Billions
$60
$30
$0
-$30
-$60
-$90
-$120
-$150
-$180
-$210
2010
2011
2012
2013
2014
2015
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2017
2018
2019
2020
2021
2022
Payroll tax holiday hole
January 2011 - December 2012
Cash Flow Deficit without General Revenue Transfers
Cash Flow Deficit
Source: Congressional Budget Office, Budget and Economic Outlook, January 2012, August 2011, and March 2010

PREPARED STATEMENT OF REPRESENTATIVE KEVIN BRADY, VICE CHAIRMAN, JOINT ECONOMIC COMMITTEE

Mr. Chairman, thank you for holding today's hearing. I agree with you that this committee must examine the whole picture—understanding both the benefits of extending the payroll tax cut and long-term unemployment benefits and their unintended consequences.

There is a strong bipartisan consensus in Congress to extend both of these expiring provisions through the end of this year. However, serious differences remain over how we should pay for these expensive extensions and whether we should reform the Unemployment Insurance program.

As popular as the payroll tax holiday may be, economists disagree about its effectiveness as an economic stimulus. However, economists agree that Social Security faces serious and growing cash-flow deficits. Diverting one-sixth of payroll tax revenue away from the Social Security revenue stream creates a significant sinkhole that exacerbates Social Security's cash-flow problems. Non-cash accounting transfers from the General Fund cannot alleviate these cash-flow problems. Last year, the U.S. government had to borrow $142 billion from investors—including foreign countries like China—to pay Social Security benefits to our seniors.

Congress must fill this sinkhole to ensure that we will be able to pay promised Social Security benefits. That's why House Republicans are insisting that Congress must offset any loss of payroll tax revenue with actual cash savings in other areas of the government, not accounting gimmicks. House Republicans will protect this vital program from debilitating cash diversions with common sense savings that have had strong bipartisan support.

As for unemployment, clearly the economic policies of the Obama Administration did not produce the vigorous recovery, for which hardworking taxpayers hoped. Tens of millions of Americans are struggling to make ends meet. Millions can't find a full-time job, and millions more can't find any job at all. Even worse, other millions have simply given up and stopped looking for work, leaving us with the lowest workforce participation rate in nearly three decades.

Our economy grew at a rate of 2.8 percent in the fourth quarter of 2011. Given this sluggish pace, many Americans don't believe that the Great Recession is really over, or else they fear it may return. Last week, the non-partisan Congressional Budget Office forecast that economic growth would slow to 2.0 percent this year and 1.1 percent in 2013, while the unemployment rate would once again begin to rise all the way to 9.1 percent in the fourth quarter of 2013. And that's obviously the wrong direction.

Our priority must be to create a far stronger economy in which American businesses will have the confidence to make investments in new buildings, equipment, and software; expand production; and create millions of new well-paying jobs.

As to Unemployment Insurance, we should reform this program and refocus it on the common-sense goal of getting people back to work sooner rather than just paying benefits. House Republicans have passed legislation that would:

1. Renew long-term federal unemployment benefits for the rest of this year while gradually reducing the maximum duration of benefits to 59 weeks.
2. Require recipients to search actively for work from day one. The longer that people are unemployed, the harder it is for them to find new employment. Under existing law, beneficiaries may collect unemployment checks for a year and a half without really having to look for a job. In some states, they don't even have to search for a job at all. That's unacceptable.
3. Allow the States to adopt innovative programs to match beneficiaries with jobs.
4. Require those on unemployment without a high-school degree to work on earning a GED. Adults without high school diplomas have a hard time finding and keeping a job. They are often the last hired and the first fired.
5. End the federal prohibition against States testing applicants for illegal drug use. Drug-screening ensures that recipients will be able to take the jobs that they are offered.

As we will hear today, long-term unemployment benefits have clearly helped families in need, but there is a cost as well. Two recent studies found that extending the duration of benefits actually increases the unemployment rate:

- A study by the Federal Reserve Bank of San Francisco found the unemployment rate at the end of 2009 would have been nearly half a percentage point lower—9.6%, instead of 10%—if jobless benefits hadn't been extended beyond their usual 26 weeks to as much as 99 weeks.
- According to a Brookings Institute paper, the 2011 extension of long-term unemployment insurance raised the number of unemployed in January 2011, by

between 0.2 and 0.6 percentage points. That translates into between 300,000 and 900,000 additional workers unemployed.

Repeated extensions of long-term benefits are also threatening the solvency of the entire unemployment system. The States have borrowed over $38 billion from the federal government to cover their program shortfalls. Under current law, repaying federal loans and rebuilding state trust fund balances would require an unprecedented payroll tax increase in nearly every State. These higher taxes would punish the very job creators that we hope will add new jobs to hire the unemployed.

To conclude, we must move forward with a bipartisan agreement to extend the payroll tax holiday and long-term unemployment benefits. At the same time, we must also adopt common-sense reforms to make the Unemployment Insurance program work better and avoid adding to our unsustainable federal debt.

I look forward to the testimony of our witnesses as we consider how best to achieve these goals.

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