

UNEMPLOYMENT COMPENSATION REFORM

HEARING
BEFORE THE
SUBCOMMITTEE ON HUMAN RESOURCES
OF THE
COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES
ONE HUNDRED SIXTH CONGRESS

SECOND SESSION

—————
FEBRUARY 29, 2000
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Serial 106-97
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Printed for the use of the Committee on Ways and Means



U.S. GOVERNMENT PRINTING OFFICE

70-276 DTP

WASHINGTON : 2001

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402

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UNEMPLOYMENT COMPENSATION REFORM

TUESDAY, FEBRUARY 29, 2000

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON HUMAN RESOURCES,
Washington, DC.

The Subcommittee met, pursuant to notice, at 1:34 p.m., in room B-318, Rayburn Building, Hon. Nancy L. Johnson (Chairman of Subcommittee) presiding.

[The advisory announcing the hearing follows:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

SUBCOMMITTEE ON HUMAN RESOURCES

FOR IMMEDIATE RELEASE

CONTACT: (202) 225-1025

February 22, 2000

No. HR-16

Johnson Announces Hearing on Unemployment Compensation Reform

Congressman Nancy L. Johnson (R-CT), Chairman, Subcommittee on Human Resources of the Committee on Ways and Means, today announced that the Subcommittee will hold a hearing on unemployment compensation reform. **The hearing will take place on Tuesday, February 29, 2000, in room B-318 Rayburn House Office Building, beginning at 1:30 p.m.**

In view of the limited time available to hear witnesses, oral testimony at this hearing will be from invited witnesses only. Witnesses will include Governor Jane Dee Hull of Arizona and Governor Bob Taft of Ohio, Members of Congress, and a representative of the U.S. Department of Labor. Additional witnesses will include representatives of employers, labor, State administrators, and scholars. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

BACKGROUND:

The Unemployment Compensation system is a Federal-State program that provides benefits to unemployed workers with a history of labor force attachment. Every State designs its own benefit program, within a broad framework provided by Federal law, and levies taxes on employers to pay for regular unemployment benefits. The Federal Government also imposes a tax on employers, based on their number of employees, that pays for the Federal parts of the system. These parts include payments for State and Federal administration, funds for the U.S. Employment Services which helps unemployed workers reenter the labor market, funds for loans to States with bankrupt programs, and funds for half of extended unemployment benefits for workers in States with exceptionally high levels of unemployment. All funds, both those for regular State benefits and for the Federal parts of the system, are kept in Federal accounts that, like Social Security funds, are part of the unified Federal budget.

In the last three years, several proposals for reforming the Unemployment Compensation program have been discussed. Several of these proposals have appeared in proposed legislation. Some of the major legislative proposals would:

- eliminate the 0.2 percent surtax placed on employers in 1976 and was extended most recently through 2007 by the Balanced Budget Act of 1997;

- change the base period employment requirements to qualify for unemployment benefits and thereby allow more workers to qualify;

- shift some Federal responsibilities, including control over the taxes that support them, to the States;

- provide incentives for States to improve the solvency of their benefit accounts;

- make the extended benefits program more accessible; and
- increase access to unemployment benefits for laid-off workers seeking part-time work.

A working group of the Administration, labor, business, and various entities with an interest in Unemployment Compensation has been meeting for nearly two years in the attempt to reach a compromise proposal that could draw support from across the political spectrum.

In announcing the hearing, Chairman Johnson stated: “The nation’s unemployment program provides critical services to out-of-work Americans. As we move into the 21st Century, it is important that we improve and strengthen the system so we can meet the increasingly complex needs of the changing workforce. This hearing will give us an opportunity to review a variety of proposals developed to meet this goal.”

FOCUS OF THE HEARING:

The hearing will focus on the various reforms now under discussion.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Any person or organization wishing to submit a written statement for the printed record of the hearing should *submit six (6) single-spaced copies of their statement, along with an IBM compatible 3.5-inch diskette in WordPerfect or MS Word format, with their name, address, and hearing date noted on a label*, by the close of business, Tuesday, March 14, 2000, to A.L. Singleton, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public at the hearing, they may deliver 200 additional copies for this purpose to the Subcommittee on Human Resources office, room B-317 Rayburn House Office Building, by close of business the day before the hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be submitted on an IBM compatible 3.5-inch diskette WordPerfect or MS Word format, typed in single space and may not exceed a total of 10 pages including attachments. Witnesses are advised that the Committee will rely on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. A witness appearing at a public hearing, or submitting a statement for the record of a public hearing, or submitting written comments in response to a published request for comments by the Committee, must include on his statement or submission a list of all clients, persons, or organizations on whose behalf the witness appears.

4. A supplemental sheet must accompany each statement listing the name, company, address, telephone and fax numbers where the witness or the designated representative may be reached. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press, and the public during the course of a public hearing may be submitted in other forms.

Note: All Committee advisories and news releases are available on the World Wide Web at “<http://waysandmeans.house.gov>”.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-225-1721 or 202-226-3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman JOHNSON. We are going to delay our opening statements and move right to Congressman Levin and hopefully Congressman English so that they have full opportunity to give their testimony and answer questions before the Governor arrives at 2. We will adjust our activities according to the needs of those who are testifying. And so with that, Sandy, I would really like to welcome you.

Mr. LEVIN. Thank you.

Chairman JOHNSON. You have been a long and active Member of this Subcommittee of many years and I appreciate your testifying. And if then Ben would like to open.

Mr. CARDIN. My opening statement was devoted to the great career that Congressman Levin has had as Ranking Member of this Committee, but I will defer all those comments and just welcome our colleague to the Committee.

**STATEMENT OF HON. SANDER M. LEVIN, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF MICHIGAN**

Mr. LEVIN. Well, thank you. And to the two of you and to Jim McCrery, I very much appreciate the chance to testify today. You have my written statement and I will refer to it.

Chairman JOHNSON. And it will be entered in—

Mr. LEVIN. Good.

Chairman JOHNSON.—its entirety in the record.

Mr. LEVIN. As you know, this is a vital issue. I was thinking about it yesterday and the only way it would not be absolutely important would be if anybody thinks there will never be another recession. And none of us like to think that there ever will be. But I think the likelihood is there will be some kind of a downturn at some point in the future.

And that is why I think it is so wise to Congresswoman Johnson and to you, Mr. Cardin, and, Mr. McCrery, that you are taking the time to look at this issue. And as I look at the various proposals, I would like all of you to consider the clear need for a continuing Federal role in this matter.

History has taught us that states cannot always address unemployment singlehandedly, and that as a nation we should save resources during good times to prepare for less fortunate circumstances.

And as I was reading that over, it struck me, I think more and more there is some agreement across party lines that, as they say now in a trite way, we should fix a roof when the sun is shining. And I think that very much applies to Unemployment Compensation. And I fear that advocates of eliminating the current Federal-State partnership on unemployment have failed to accept these two lessons.

And let me give you, if I might, one example. It is from my own home state. And this is a reference to 1982, the last recession of the early 'nineties. I did not look up the figures for the even more severe recession in the 'eighties, but my guess is the figures would be even more dramatic.

In 1992, 188 million in Federal unemployment taxes were paid in my home state of Michigan. But the Federal Government spent \$719 million that same year in Michigan for administrative costs and emergency unemployment benefits. I understand the Governor of Ohio was not—is not able to be here today.

Chairman JOHNSON. Unfortunately.

Mr. LEVIN. I do remember at a hearing of the Subcommittee a few years ago when he was here, I raised this issue relative to Ohio and presented figures showing, in a particular year, how much was paid in and how much was paid out. And while the figures were not quite as striking as those from Michigan, I thought they were rather dramatic. And I think that so-called devolution proposals, including H.R. 3174, would eliminate or seriously erode this Federal backstop protection during economic downturns.

The major impetus behind proposals to eliminate the Federal collection of unemployment taxes is the concern that states have expressed regarding inadequate administrative funding being provided by the Federal Government. And let me say unequivocally that this is a legitimate concern which should be addressed. And 3174 shines a spotlight on that issue, though it goes much beyond it.

However, we do not need to eliminate the Federal role in helping unemployed workers to achieve that goal. In the legislation that I have introduced with Representative English, who is next to me, administrative funding—additional funding would be provided to those states that make an even modest improvement in the solvency of their state UI trust funds.

And I would like to point out, according to the Labor Department, 20 states currently have insufficient reserves in their unemployment trust funds to weather a severe recession. Encouraging them to save for the future is certainly consistent with common sense.

I also understand that a working group on unemployment issues, which represents employers, workers, the states, and the administration, have discussed the advantages of making UI administrative funding mandatory, rather than discretionary. This proposal warrants some attention, particularly concerning the recent trend in the Appropriations Committee.

In fact, the shortfall between funding provided by the Appropriations Committee and the level of financial need in the states to administer the UI systems has grown considerably since 1994. And I point that out to—in part because that is the fact and, in part, because I do think that everybody who wants to flirt with the idea of devolution should look at what the record is.

Because from 1995 to 1998, a shortfall between administrative funding and financial need increased from three percent to more than 13 percent. Continually cutting appropriations for UI and employment services and the claiming that reduction makes the case for devolution, seems a bit disingenuous.

There are two other issues the Subcommittee should consider, I think, when reviewing proposed reforms for the UC system. First, during the last recession, the Extended Benefits Program did not trigger on appropriately, meaning Congress was forced to pass an Emergency Unemployment Compensation program at \$28.5 billion dollars as I remember it. And I think that all of you were on the Subcommittee during at least some of those years. And I was. And the difficult task we had in terms of providing for emergency funding.

And the legislation introduced by Mr. English and myself proposes an alternative trigger for the EB program to ensure that it works as intended. This approach, which assesses the total number rather than the insured number of unemployed workers, is consistent with the recommendations of the Advisory Committee on Unemployment Compensation.

And, second, some low-income workers are being denied UI benefits because their most recent earnings are not considered by many states when eligibility decisions are made. To address this situation, H.R. 1830 would provide funds to help states voluntarily implement—and I emphasize voluntarily implement—so-called Alternative Base Periods, which calculate the last four quarters of earnings, rather than the first four out of five. This change represents one way to begin to reverse the long-term trend of fewer unemployed Americans receiving UI benefits.

And I do say to all of you, as colleagues, if we asked our constituents what percentage—just give us a rough approximation—of unemployed people are eligible for Unemployment Compensation, I doubt if anybody would come any close to as low a figure as one-third. There is something wrong.

And it seems to me—for example, people who have moved from Welfare to work who would be vulnerable in a recession, I just think for those and others, there has to be some answer. And the notion that only a third of the unemployed workers, people who are working are eligible these days for unemployment—a historic low—I think is contradictory to what we believe in the value of work.

In closing, let me say that I hope this Subcommittee is guided by one overriding concern when considering reforms to our Nation's Unemployment Comp system—the well-being of workers without employment. We need a system capable of providing them with temporary wage replacement, and I would add, with permanent re-employment—a system that is dependable on both good times and bad. Thanks very much.

[The prepared statement follows:]

Statement of Hon. Sander M. Levin, a Representative in Congress from the State of Michigan

Madame Chairwoman, I would like to thank you for allowing me to testify today on a very important issue—our Nation's response to unemployment. It is a pleasure to return to the Human Resources Subcommittee, if only for a day.

As you consider various proposals to reform the unemployment compensation system, I urge you to consider the clear need for a Federal role in addressing a National issue.

History has taught us that States cannot always address unemployment single-handedly, and that as a Nation, we should save resources during good times to prepare for less fortunate circumstances. I fear that advocates of eliminating the current Federal-State partnership on unemployment have failed to learn these two lessons.

Let me give you one example of this issue. During the last recession in 1992, \$188 million in Federal unemployment taxes were paid in my home state of Michigan. But the Federal government spent \$719 million that same year in Michigan for UI administration costs and emergency unemployment benefits. So-called devolution proposals, including HR 3174, would eliminate this Federal backstop protection during economic downturns.

The major impetus behind proposals to eliminate the Federal collection of unemployment taxes is the concern States have expressed regarding inadequate administrative funding being provided by the Federal government. Let me say unequivocally this is a legitimate concern which should be addressed.

However, we do not need to eliminate the Federal role in helping unemployed workers to achieve that goal. In the legislation I have introduced with Representative English (HR 1830), additional administrative funding would be provided to those States that make even modest improvements in the solvency of their State UI Trust Funds.

I should say that, according to the Department of Labor, 20 States currently have insufficient reserves in their unemployment trust funds to weather a severe recession. Encouraging them to save for the future is certainly consistent with common sense.

I also understand that a working group on unemployment issues, which represents employers, workers, the States and the Administration, have discussed the advantages of making UI administrative funding mandatory, rather than discretionary. This proposal warrants some attention, particularly considering the recent trend in the Appropriations Committee.

In fact, the shortfall between funding provided by the Appropriations Committee and the level of financial need in the States to administer their UI systems has grown considerably since my friends who advocate on behalf of devolution assumed majority status in Congress. From 1995 to 1998, this shortfall between administrative funding and financial need increased from 3% to more than 13%. Continually cutting appropriations for UI and employment services, and then claiming that reduction makes the case for devolution, may seem a little disingenuous to a neutral observer.

There are two other issues the Subcommittee should consider when reviewing proposed reforms for the Unemployment Compensation system. First, during the last recession, the Extended Benefits Program did not trigger on appropriately, meaning Congress was forced to pass an Emergency Unemployment Compensation program. My legislation proposes an alternative trigger for the EB program to ensure that it works as intended. This approach, which assesses the total number rather than the insured number of unemployed workers, is consistent with the recommendations of the Advisory Committee on Unemployment Compensation.

And second, some low-income workers are being denied UI benefits because their most recent earnings are not considered by many States when eligibility decisions are made. To address this situation, HR 1830 would provide funds to help States voluntarily implement so-called Alternative Base Periods, which calculate the last four quarters of earnings, rather than the first four out of five. This change represents one way to begin to reverse the long-term trend of fewer unemployed Americans receiving UI benefits.

In closing, let me say that I hope this Subcommittee is guided by one overriding concern when considering reforms to our Nation's unemployment compensation system—the well-being of workers without employment. We need a system capable of providing them with temporary wage replacement and permanent re-employment—a system that is dependable in both good times and bad.

Thank you.

Chairman JOHNSON. Thanks very much, Congressman Levin. And, Congressman English, a pleasure to welcome you before the Committee. It has been a great help to me to have you on my right hand and I am delighted to have you—

Mr. ENGLISH. Thank you, Madam Chair. That is—

Chairman JOHNSON.—testify in support of your legislation.

**STATEMENT OF HON. PHILIP S. ENGLISH, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF PENNSYLVANIA**

Mr. ENGLISH. That is high praise. And I want to, first of all, thank you for the opportunity to testify. Second of all, say that I would like to associate myself with remarks of the distinguished gentleman from Michigan and it is a privilege for me to be the prime cosponsor of his legislation, which, I believe, has the support of the administration.

I would like to kind of condense the remarks I had intended to deliver here today, but simply make the point that there is a real problem in our system of unemployment insurance. The safety net is badly tattered and there are many holes that the public is largely unaware of. I think we need to move to address that.

Second of all, the time to act is now. The fact that we are in a period of comparatively low unemployment and comparatively low utilization of the program, means that it is a perfect time to try to address this problem because of cost factors. We need to move now, not when we are next in a recession.

And, third, I want to caution the Subcommittee against the dangers of vulcanizing [ph] unemployment insurance in America. I believe we need to have a strong national system of unemployment insurance that can guarantee that people can receive like treatment in states across the country and that states will have a comparable fiscal capacity to deal with problems.

When I began to deal with this issue, I was a young staffer working for the State Senate Labor Committee in Pennsylvania and our experience was that Pennsylvania was going afresh into a recession. And, in fact, our state had been plagued with high employment for a long period of time. I fear that if we tamper with the Federal nature of the unemployment insurance system, we run the risk of putting states who had—go through longer spells of unemployment at a comparative disadvantage dealing with their problem because they are forced to raise taxes and ultimately make themselves a less attractive place for investment.

Lake last year, in addition to the legislation that I have cosponsored with Mr. Levin, I introduced legislation designed to empower states to meet the needs of the long-term unemployed. The current unemployment insurance system was created to help states combat short-term unemployment. Unfortunately, workers who are laid off from their jobs now are less likely to return to their previous jobs as in the past, even in the situation where we are running and it—through a period of extended growth.

Unemployment is hard enough on families without the worry that benefits will not be available because of the structure of the system. H.R. 3167, the legislation which I have introduced, will make several important changes to the current system.

One, it will make it easier for states to provide extended unemployment benefits to workers who have been unemployed for long periods by broadening the trigger states can use to access benefits.

Research has shown that the combination of the reduction in the Insured Unemployment Rate and the increase in the trigger level during the recession of the early 'nineties, resulted in the failure of the Extended Benefits program to trigger on as unemployment continued to rise.

As a result, Congress found it necessary to pass a series of emergency extensions of UC benefits. Put simply, no state was able to tap into Extended Benefits during the most recent recession. That is a signal that the system is broken.

Two, my legislation would encourage states to maintain sufficient unemployment trust fund balances to cover the needs of unemployed workers in the event of a recession. States that maintain adequate reserves, based on their own experience, to cover expenses in future recessions would receive slightly increased interest earnings on the part of their trust fund; states that fall short would receive slightly reduced interest earnings. This would provide an incentive for states to be good trustees of the system.

Third, it would allow interest-free cash-flow Federal loans only for states that have sufficient trust fund reserves to last through a future recession.

Fourth, it would allow states to collect the Federal share of unemployment insurance taxes from employers, allowing employers to fill out one form and write one check, not two, one of the benefits attributed to some of the devolution plans that this Subcommittee will also consider.

It would also, fifth, require states to distribute information packets explaining unemployment insurance eligibility conditions to unemployed individuals.

All of these provisions are based on recommendations from the Advisory Counsel on Unemployment Compensation. The findings from the Advisory Counsel, which was established in 1991, have been out there for a number of years and my legislation freely was modeled on them. I—the process of drafting H.R. 3167 allowed me to utilize my experience when considering the effects each recommendation would have on the unemployment insurance system.

And, finally, Madam Chair, I would also hope that the Subcommittee would consider the pernicious effects of the current Tax Code on the unemployment insurance system. Specifically for the—we now, unlike in the early eighties, tax unemployment insurance benefits as income. This has put many people who go through an extended period of unemployment and collecting benefits at a big disadvantage in the following year when they are forced to pay taxes. This is the cruelest tax of all.

The tax on Unemployment Compensation kicks workers when they are down. Unemployment benefits are intended to stabilize the income of individuals and families in the face of layoffs. Yet someone who experiences lengthy unemployment, a situation that depletes the financial reserves of most middle class families, will face a large, and usually unexpected, tax liability the next year. That is unfair and I would hope we would move to address that at some point in the future.

I thank you for the opportunity to testify and for the fact that you have been willing to take the Subcommittee and focus on this very important issue in this important system.

[The prepared statement follows:]

Statement of Hon. Philip S. English, a Representative in Congress from the State of Pennsylvania

Madame Chairwoman and fellow Members of the Subcommittee, I want to thank you for holding this important hearing and for allowing me to address my colleagues

and everyone in attendance today on unemployment reform. As most of you may know, before being elected to Congress, I was the Research Director for the Senate of Pennsylvania Labor and Industry Committee. During my tenure, I dealt with many of the issues being discussed today and I can tell you from my own hands-on experience that the current unemployment insurance (UI) system is badly in need of reform. States are not equipped to tackle unemployment as we begin the new millennium with a UI system that has changed very little since its inception and cannot deal effectively with the changing nature of unemployment. I will discuss several changes to the system I am proposing as well as the unfair taxation of benefits during my testimony today.

Late last year, I introduced legislation designed to empower states to meet the needs of the long term unemployed. The current unemployment insurance system was created to help states combat short-term unemployment. Unfortunately, workers who are laid off from their jobs now are less likely to return to their previous jobs as in the past—and long-term unemployment is increasing. The current system cannot adequately address long-term unemployment.

Unemployment is hard enough on families, without the worry that benefits will not be available because of the arcane structure of the system. H.R. 3167, the legislation which I have introduced will make several important changes to the current system:

1.) Make it easier for states to provide extended unemployment benefits to workers who have been unemployed for long periods by broadening the trigger states can use to access benefits.

Research has shown that the combination of the reduction in the Insured Unemployment Rate and the increase in the Trigger level during the recession of the 1980's resulted in the failure of the Extended Benefits program to trigger "on" as unemployment continued to rise. As a result, Congress found it necessary to pass a series of emergency extensions of UI benefits. Put simply, no state was able to tap into Extended Benefits during the most recent recession. Therefore, it is absolutely necessary to reform the program prior to the onset of the next recession. Emergency extensions of benefits are a Jerry-Built policy prescription neither well-timed nor well-targeted.

2.) Encourage states to maintain sufficient unemployment trust fund balances to cover the needs of unemployed workers in the event of a recession. States that maintain adequate reserves (based on their own experience) to cover expenses in future recessions would receive slightly increased interest earnings on part of their trust funds; states that fall short would receive slightly reduced interest earnings.

3.) Allow interest-free, cash-flow federal loans only for states that have sufficient trust fund reserves to last through a future recession.

4.) Allow states to collect the federal share of unemployment insurance taxes from employers, allowing employers to fill out one form and write one check, not two.

5.) Require states to distribute information packets explaining unemployment insurance eligibility conditions to unemployed individuals.

All of these provisions are based on the Advisory Council on Unemployment Compensation's Collected Findings and Recommendations for 1994–1996. As most of you know, the Advisory Council was established under the Emergency Unemployment Compensation Act of 1991. That law instructs the Council to evaluate the unemployment compensation program and make recommendations for improvement. The process of drafting H.R. 3167 allowed me to utilize my experience when considering the effects each recommendation would have on the UI system. I have concluded that if the recommendation were enacted into law, as I propose in H.R. 3167, states (like Pennsylvania) would have the tools to assist workers faced with the long-term unemployment.

Another important issue I would like to address is the current tax on unemployment compensation (UC) benefits. Before 1979, UC benefits were excluded from inclusion in income tax purposes. UC benefits are currently fully subject to tax. This tax treatment, in place since 1987, puts UC benefits on par with wages and other ordinary income in regard to income taxation. Last year, I introduced legislation, H.R. 3169, the "Unemployment Tax Repeal Act," to gain exclude UC benefits from inclusion in gross income for tax purposes. The pre-1979 exclusion was upheld by Internal Revenue Service rulings based on three arguments: 1.) the law did not explicitly require taxation of UC, 2.) the benefits were viewed as part of the social welfare system and not regarded as wages, and 3.) taxation would undercut UC's income support objectives. I feel the final justification is particularly true. The UC tax is not a tax on income; it is a tax on benefits—benefits received during one of the most difficult times in a person's life. The UC tax hurts the economic security of workers throughout America. Our system should be structured to provide benefits to taxpayers, not dump penalties on the unemployed.

Madame Chairwoman I have talked to literally dozens of people in Western Pennsylvania who have collected unemployment benefits—and then paid taxes on the benefits as normal income. Their experiences highlight now grossly unfair tax is.

The tax on unemployment compensation kicks workers when they are down. Unemployment benefits are intended to stabilize the income of individuals and families in the face of layoffs. Yet someone who experiences lengthy unemployment—a situation which depletes the financial reserves of most middle class families—will face a large (and usually unexpected) tax liability the next year. For many who have struggled to survive a layoff, this tax bill is the last straw.

Simply allowing tax withholding on these benefits is no solution: it merely depletes the value of compensation that is already merely adequate. I would argue that however this tax is administered, it is fundamentally inequitable and perversely burdensome to a beleaguered middle class.

Madame Chairwoman, I will conclude by emphasizing my strong support for reforming our unemployment system. It is my hope that our Committee will give its strongest consideration to developing legislation that will encompass many of the suggestions heard here today. Following through on these recommendations will result in a more manageable system and a more secure U.S. workforce.

Thank you for the opportunity to testify today.

Chairman JOHNSON. Thank you. I appreciate you both providing us with a very thoughtful introduction to this hearing. And I am going to yield to Mr. McCrery to question first since we are short of time.

Mr. MCCREY. Thank you, Madam Chairman. Gentlemen, thank you for your testimony today and for your thoughtfulness in looking at our unemployment insurance system and the system of benefits for the unemployed. And you bring up some very good questions that we ought to take a look at.

However, I am puzzled by your reluctance to promote a repeal of the .2 percent surtax. The point—the revenue from the .2 percent surtax is overflowing. It is causing our caps, our various funds, to overflow and we have continually jiggered the caps and created other funds that they could—excesses could flow into. It is a really bizarre, almost Byzantine—here is a chart showing all the funds that we now let over excess funds flow into.

And really, the only reason we have been doing that is not for the benefit of the unemployed. It is for the—it has been for the benefit of the deficit. It was to hide the deficit. It was just to bring revenues into the Federal Government that mask the true size of our deficit. And now that we don't have a deficit, how can you justify not promoting, in your bills or in any bill addressing the UI system, repealing this burdensome, unnecessary tax on employers?

Mr. LEVIN. Go ahead.

Mr. ENGLISH. I may have a different answer than some others might. My opposition to it at this stage is purely tactical rather than philosophical. I would like to see us deal with all of the problems in the UC system, or, at least, look for ways of improving the UC system overall. As part of doing that, I am perfectly willing to entertain the repeal of the .2 percent surtax. I think your criticism of the surtax has considerable merit.

My concern is that, in the process of going forward to repeal it, we not also forget some of the other things that need to be fixed in the UC system, like the Extended Benefits Program. I would point out to the gentleman that fixing the Extended Benefits Program would be a very inexpensive thing to do in the big picture.

And if we were to do that and several other reforms and also repeal the .2 percent surtax, you would see it as a win-win for workers and for small business. And I thank the chair—

Mr. MCCRERY. Thank you.

Mr. LEVIN. And, Mr. McCrery, my response is not so different. I think it is a mistake to take one piece of this. We should look at the larger picture. And I think the Advisory Committee—or there is a working group that is doing just that. And I would think we should encourage it.

I looked at the figures for various states and it is true that there is a major discrepancy between what is paid in and what is paid out in administrative costs. For example—and the Governors will be here for Arizona—and I didn't copy down the year—45 million paid—no, 112 million paid in and 45 million paid back. But the percentage of unemployed who receive insurance in Arizona is 21 percent.

And I mention your state because I think you will be unsatisfied—dissatisfied with the figure. You paid in with both figures 92 million and received back 38 in administrative. But your—the rate of coverage in Louisiana is 26 percent.

Now, there is something wrong with the system that leaves only a fifth or a quarter coverage. So, in a word, I favor looking at all of these issues, the Extended Benefit Program, the coverage problem, as well as the two percent—the .2 percent.

Mr. MCCRERY. Well, Mr. Levin, I think you make a legitimate point in urging us to look at the reasons for such a low rate of coverage across the board. However, imagine what the states would have to be doing if their workloads were any higher than they are in terms of their administrative expenses, which they are being shorted on and have been shorted on for the last number of years. So—

Mr. LEVIN. But they would be receiving more in administrative costs if they had a higher rate of coverage.

Mr. MCCRERY. Well, it—I mean, I am not sure of that. That the—

Mr. LEVIN. I see. I see.

Mr. MCCRERY.—the appropriate is up to the Congress. And we have been the ones that have been shorting that appropriation year after year, making the formulas work to fit the appropriation. So I am not sure that you are accurate in saying that states would necessarily get more. And that is why in my bill I make it a mandatory spending item and then the states could draw down what they need for their administrative expenses.

So I think that is a superior approach to this method that we have been using for a number of years that have shorted the states. So I don't mind looking at the rationale for the low rate of coverage. But I would urge you to look at the fact that we have been short-changing the states for years now on their administrative costs. And the tax was designed to cover those and we have not been fulfilling the promise of that tax.

Mr. LEVIN. Could I just add briefly? The fact there is a surplus is also a reason for us to go to the Appropriations Committee and urge that they provide adequate funding for administrative costs.

Mr. MCCRERY. Well, in my bill we wouldn't have to do that. They would be relieved of that burden. Thank you, Madam Chairman.

Chairman JOHNSON. Thank you. Mr. Cardin.

Mr. CARDIN. I thank you, Madam Chair. Let me agree with Mr. McCrery in regards that the—our budget systems shouldn't force us into a conclusion. We should have—we should do what is the right policy here. And I agree with the essence of your point that we have done it—we have kept the FUTA tax in place because of the budget considerations, not because of the need for the funds, and it should be considered on its own merits.

Having said that, let me just concur in the comments of both Mr. Levin and Mr. English. I thought both of you made very, very effective points which I concur in. And I think it was very important that we hold these hearings now to try to look at our unemployment insurance system and strengthen it. And the points that both of you raised about having a fair way to compensate the states for their administrative costs and to have incentives in the program to strengthen the solvency of the state funds are things that we need certainly to improve upon.

One concern I have is that we are also looking at other fundamental changes. Mr. McCrery has some legislation that would devolve a good part of this to the states. I guess one of my concerns is that we are enjoying a very robust economy right now, very low unemployment rates. We are all very optimistic. But I remember a special session in the State of Maryland when we had a slight recession that nearly caused panic in our states about providing unemployment extended benefits to—and emergency benefits to our workers.

So I am concerned that we might be lulled into a sense of security here, that we can make changes and allow the states to have more control over their own unemployment system, not recognizing the fact that when a recession hits, it doesn't hit evenly among all states. Certain sectors are—certain geographical areas are hit much more—have much more difficult problems than others. And that is our responsibility to make sure that we have a national unemployment system—unemployment insurance system that protects those regions, those areas, and helps them deal with the problems of a recession so they don't have to impose new taxes when it is the worst time in the world to impose those taxes.

I just appreciate your testimony. Do you want to respond to that—

Mr. LEVIN. Mr. Cardin, just briefly, I could not agree with you more. The recessions in the 'eighties, and it was also true in the 'nineties, hit regions—it was not national in its immediate impact. The largest newspaper sales in Michigan in the 'eighties was the newspaper from Texas, people looking for jobs outside of the State of Michigan.

And I think we need to be sure that we have a national Unemployment Compensation system. Otherwise, we are going to rely on states coming here and regions coming here asking for Federal funds in massive amounts. That is what happened in the 'eighties when we did not have an effective trigger on extended benefits. So we went through the difficult process of trying to convince people from one region, people all over the country, to essentially chip in.

And then when the recession moved from the midwest, Pennsylvania, Michigan, and Ohio were terribly hit. Then down to the southwest. Then that process started all over again. And unemployed people move from place to place. We need a national system. And the problem with devolution proposals is that they fly in the face of the fact that unemployment can be, and almost always is, ultimately a national problem that requires some action on a community—an American community basis.

Mr. CARDIN. Another issue that would concern me is that the Extended Benefit Program has a funding—national funding source for part of the cost. And if we repeal that funding source, it wouldn't take too long in a recession for us to exhaust our funds nationally and have a difficult time meeting any Federal responsibility for extended benefits.

Mr. LEVIN. Absolutely.

Mr. CARDIN. Thank you, Madam Chair.

Chairman JOHNSON. I want to put on the record—I was going to do this in my opening statement, but I think it is really important to do it right now. Unemployment Compensation has been seen in Congress by members of both parties and, I believe, by the administration as a very partisan issue. I think your testimony demonstrates, and Mr. McCrery's bill demonstrates, that it is not a partisan issue. We have a system that was built for an entirely different era, when people were to be sustained until they were recalled to their jobs.

And as we have changed our work force reinvestment, et al., our job training moneys and everything, I think we should be looking at how do we fix this system so it better serves the people?

Sandy and I were both on the Committee when we struggled through those periods in the eighties. No matter what we did, we never were able to trigger and target in a way that New Britain, Connecticut benefited because we made bearings and machine tools and we had very high unemployment. The state generally didn't. And no matter what we did in Washington, we couldn't fix it.

So I do think we need to look at the issues that you have pointed to. I am very pleased with the specificity of the ideas in both of your legislative initiative and I am very grateful for Mr. McCrery's hard work on this issue.

The states, as you will hear later, need money because they are focused now on re-employment. They are not focused on sustaining people until they are rehired by their former employer. And they are doing a phenomenally better job than they were in the 'eighties. And so they need some of this money for that.

And we do have a system in which some states have 122 months worth of benefits stored up; others only seven. So not only should we be concerned about the covered population, but we ought to be concerned about states that are stockpiling dollars they need to improve the quality of their program and to move people into jobs. So there are a lot of issues here and you have raised a number of them.

And I would just hope that business and organized labor could lay aside the belief that this is somehow a divisive issue. It is as important to people's lives as fuel assistance, you know. And we ought to look at it in that way. Every bill that has come out of this

Committee has been nonpartisan. And I personally have not taken a stand on any of the legislation. And I know, from working with Members of the Committee, that they are very substantively oriented.

And I would just hope that we would all work together in this realm to see what we could do about the problems that are plaguing this system and the bizarre nature of the tax revenue and how it is used because it is really bizarre.

Let me just conclude. We do have Governor Hull here. But I want to throw out for the two of you, and I want to throw out for the audience, you know, Unemployment Compensation doesn't require you to do anything but receive. If you are on Welfare, you are required to search for a job. You are required to participate in job training.

Are we in an era any more where we can allow people to be unemployed, receive benefits, and not participate in developing computer skills and thinking about their career and changing their jobs and lives? Don't answer, because I don't want you on the record on this one. But I think we have to think about those things. And I think everyone in this room has to think about those things because, in the end, unemployment systems are to create re-employment. They are not a permanent support system.

Mr. LEVIN. Could I just say quickly? As you know, the states, I think, in every case, have a looking-for-work requirement.

Chairman JOHNSON. It doesn't work, though, Sandy. It doesn't work.

Mr. LEVIN. Well, but that is—but there is that requirement. But, second, I believe fervently that we need to look at our training and retraining programs and our Unemployment Comp programs and figure out how to mesh them. We do not intervene early enough in this country, compared to—

Chairman JOHNSON. Right.

Mr. LEVIN.—Canada and many other places—

Chairman JOHNSON. That is all—that is only—

Mr. LEVIN.—where people are going to be laid off.

Mr. CARDIN. Would you yield just for one moment?

Chairman JOHNSON. That is the only issue I am raising. Yes, sir.

Mr. CARDIN. And I appreciate the way that you phrased the dilemma. I must tell you, I have met many people who collect unemployment insurance who would love to have a job. It depends on the economy. It depends on the circumstances within the community. And there are people, I am sure, who are collecting unemployment insurance who could be working.

But, by and large, the unemployment—and the people who are insured and are collecting unemployment insurance, want work. The problem is that their company has downsized or industry has left or their skills are no longer needed in the work force. And I agree with you, one of our focuses need to be to make sure that people are trained for the opportunities that are there, which is part of our system, and we need to make sure this is properly coordinated with any change we make in the unemployment insurance system. And I appreciate you yielding.

Chairman JOHNSON. The reason I wanted to bring it up is, I think when you rethink a program that was established as long

ago as our Unemployment Compensation program was established, and you look at the extraordinary pace of change in our economy now, the likelihood that that pace is going to accelerate, not diminish, that the nature of jobs people will be moving to will change more rapidly, not less rapidly, I think if we are going to look at how we deal with—how we provide people with security during periods of job change, we need to think of it at every level.

And so I am happy to have your input and I want you to help us raise the questions at the biggest level. My goal, ultimately, is to address the personal security needs of people who lose their job through no fault of their own. That was always the purpose of the Unemployment Compensation system and it is an extraordinarily important purpose. And if we don't meet it better, it is not just the individual workers who will be the worse off, it will be the nation, because we are going to increasingly have a labor shortage as we move into the future.

So it is incumbent upon us to develop a system that far better supports individual development of individual resources to create one's own best opportunity in life. And so I welcome—

Mr. LEVIN. Thank you.

Chairman JOHNSON.—this opportunity and I thank Mr. McCrery for his hard work to make this hearing possible. I would like to now welcome Governor Jane Hull of the great State of Arizona. I regret that at the last Bob Taft, of Ohio, was unable to join us and I very much appreciate, Governor Hull, your willingness to be here with us. This is an extremely important issue that states have a great stake in. And so we thank you for being with us.

STATEMENT OF HON. JANE DEE HULL, GOVERNOR, STATE OF ARIZONA

Governor HULL. Good afternoon, Chairman Johnson, and I am glad to be here, Mr. Cardin.

Chairman JOHNSON. It is a tradition that your total statement will be inserted in the record and you could either adhere to it or not. But we welcome you.

Governor HULL. Thank you.

Chairman JOHNSON. Oh. Sorry.

Governor HULL. Mr. Cardin—

Chairman JOHNSON. Wait a minute. Excuse me. One moment, please. I didn't realize we had been joined—

Governor HULL. Yes. We have got company.

Chairman JOHNSON.—by an esteemed Member of the Ways and Means Committee from your very own state—Mr. Hayworth.

Mr. HAYWORTH. Madam Chairman, thank you. And I shall not force the Governor to interrupt her testimony other than to thank her for coming all the way from our beautiful state, where spring training is starting, to be here in Washington and the National Governors' Association and also to spend time here in front of the Subcommittee. So on behalf of the entire Ways and Means Committee, Governor, thank you for coming and we look forward to your testimony. And, thank you, Madam Chairman.

Chairman JOHNSON. I thank you.

Governor HULL. Thank you.

Chairman JOHNSON. Good to see you.

Governor HULL. And, again, it is nice to be here and I appreciate your taking time to hear my testimony. As you have noted, Governor Taft was called back to Ohio, so you will get briefer testimony than if you had had both of us. I am sure some days it is probably a good idea for you.

I am Governor Jane Dee Hull from the State of Arizona. And, again, I do truly appreciate the opportunity to appear before you. This issue, Mr. McCrery's bill, is of great significance to the economic future of the State of Arizona, as well as many other states. What I am representing is a shared bipartisan position that has been adopted by the Western Governors' Association and, today, by the Southern Governors' Association. The issue is reforming the National Employment Security System and repealing the Federal Unemployment Tax Act (FUTA) surtax begun in 1976.

My state, like many others, is enjoying unbelievable and unprecedented economic growth. The prosperity has been aided by sound state and national policy decisions. We are going to continue to enjoy those benefits. We have got record increases in education spending and in our other priorities. We have the highest, depending on the day—between Nevada and Arizona, one of us is first in growth of population. We have low unemployment. We have a greatly increased per capita income, which, as Arizona is a low income state, we are very proud of that.

We have to continue to make wise decisions based on this new economy that the Governors have all just spent so much time talking about and all Governors spend a lot of time talking about. The Western Governors and the Southern Governors, as of this morning, have joined me to support the repeal of the FUTA surtax and reform of the Employment Security System. It is administered, as you know, in partnership between the state and the Federal Government.

As Governors, we share the challenge to maintain a solid, economic foundation upon which to build future prosperity. Members of the Subcommittee, I know, from your comments, Madam Chairman, all share the same concern. In Arizona, we minimize government interference in our economy. We maximize the effectiveness of the state's limited role by fostering reasonable growth and quality job creation. We cannot address these issues without your help.

The reason I am here supporting legislation repealing the temporary FUTA surtax and to urge you to return these funds to the businesses in each of our states. Arizona business leaders, both small and large, have one clear top priority—work force development. We need to identify and supply a well-educated and a skilled work force.

Washington is collecting a surtax that is being used to offset the Federal surplus, that \$1.5 billion is something that if were turned to the states, we believe that we could provide better employment services, and also reducing the financial burden on businesses who employ our people.

The money is being doled out to the state in ever decreasing amounts. Arizona right now is getting about 45 cents on the dollar. We are in the lower third of those states. And, again, we could do better with the return of those dollars. It is making it increasingly difficult for us to administer the unemployment services that we

believe we need to be administering in order to get people into the work force.

We share the commitment to use these funds in the administration of employment services to truly help our citizens who are seeking better jobs, seeking re-employment, or who are seeking to enter the work force for the first time.

Likewise, you hear, from the same employers, who are begging for quality employees, so they can meet the opportunities and demands that our growing economy is creating for them. The funds are being collected by the Federal Government today, but they are not being used to address the need.

As you well know, the temporary FUTA tax—surtax is padding the Federal budget surplus. It is not helping us take advantage of the potentially unique opportunity to get people into quality jobs that they need for themselves and for their families.

Under the reform proposal that you are considering, Representative McCreery's bill, my state could see an increase of \$36 million a year in funds available for quality jobs, to help our employers, and to serve the unemployed.

We have worked out an innovative programs—several innovative programs in Arizona that meet the employment needs of our private sector as well as the needs of those who need to find jobs. It will be another chance for you to devolve to the states the opportunity of helping our people join the work force of tomorrow. It would allow Arizona to participate more effectively in the employment services programs with the Federal Government.

The effectiveness would also extend the benefits to include utilizing a portion of the repealed temporary surtax to better ensure the quality of jobs in my state.

I would respectfully ask that you would have included in the record the comments of Governor Taft too—as he has been called back to Ohio, the WGA, the Western Governors' Association resolution of yesterday, and the Southern Governors' Association of today. And I know that you do have my comments which I have tried to greatly shorten knowing that your time is limited and that you are all very capable of reading them yourselves. With that, I want to thank all of you for the opportunity to appear before the Subcommittee today on this issue of importance to the workers, citizens and employers in the State of Arizona. I welcome the chance to work with you to help move this proposal through Congress.

[The prepared statement follows:]

Statement of Hon. Jane Dee Hull, Governor, State of Arizona

Good afternoon Chairman Johnson and members of the Subcommittee. I am Jane Dee Hull, Governor of the State of Arizona. I appreciate the opportunity to appear before the Subcommittee today to discuss an issue of significance to the economic future of my state. I also come before you to present the shared, bi-partisan position adopted by the Western Governors Association in support of the issue under consideration here today—reforming the National Employment Security System and repealing the Federal Unemployment Tax Act (FUTA) surtax.

The State of Arizona, like many other states across the country, has been enjoying unprecedented economic growth over the past decade. In addition to the hard work and ingenuity of the American people, I believe this prosperity has been aided by the sound policy decisions of elected leaders at the state and national level. If we are going to continue to enjoy the benefits of this success, which in my state has led to record increases in education spending and other important public priorities,

then we must continue to make wise decisions on those matters impacting our economy.

That is why my fellow Western Governors joined me several weeks ago in adopting a policy position supporting the repeal of the FUTA surtax and reform of the employment security system administered in partnership between the state and federal governments. (A copy of the Western Governors Association Resolution 99-029 on Employments Security is attached.) As Governors, we share of ensuring that we maintain a solid economic foundation upon which to build further prosperity and opportunity in each of our states in the new century ahead of us. I know the members of the Subcommittee have the same concern.

In Arizona, we are building that foundation with a common commitment among state leaders to minimize the level of government interference in our economy while maximizing the effectiveness of the state's limited role by developing sound policies that foster reasonable growth and quality job creation. My fellow Western Governors share this view, and we have spent considerable time discussing how we can sustain the prosperity in our region, which has even outpaced the nation's success in many areas.

Clearly we cannot address these challenges without your help. It is for the reason that I am here to ask for your support of legislation repealing the "temporary" FUTA surtax and urge you to return these funds to the businesses in the states where they have been collected. In anticipation of a possible repeal, there has been considerable discussion of how these funds might then be best used—by the businesses and the states—to achieve the economic policy objectives I mentioned earlier.

Specifically, through regular meetings with Arizona business leaders, both small and large, I have heard one clear message about their top priority. Without exception, the number one issue facing Arizona businesses today is workforce development. Like many states, Arizona needs to meet the challenge of helping identify and supply a well-educated and skilled workforce.

Frankly, we are constrained in our ability to address this challenge when a fund in Washington is continuing to grow by collecting a surtax that is padding the federal surplus, but not helping provide employment services or reducing the financial burden on the businesses that want to employ our citizens. However, the money is being doled out to the states in ever-decreasing amounts that make the employment services of states increasingly difficult to maintain at a time when these efforts could be their most effective by getting more of our people into the workforce.

Let me restate that point, perhaps a little more directly. I know you share the commitment of Governors, like myself, who want to use these funds and the administration of employment services to truly help our citizens who are seeking better jobs, seeking reemployment, or who are seeking to enter the workforce for the first time. Likewise, you hear from the same employers who are begging for quality employees so they can meet the opportunities and demands that our growing economy is creating for them.

The funds to meet these vital public and business needs are being collected by the federal government today, but they are not being used to address the needs. As you well know, the "temporary" FUTA surtax is flowing into one of the many federal trust funds that are padding the federal budget surplus. The surtax is not helping us take advantage of the important, and potentially unique, opportunity to sustain our prosperity and ensure that our people are getting into the quality into the quality jobs they need for themselves and their families.

More specifically, under the reform proposal you are considering in Representative McCrery's bill, my state could see an increase of \$18 million in a year in funds available to help provide quality jobs, help our employers and serve the unemployed. At the same time employers in my state would see a tax reduction of \$28 million—a portion of which they would like to commit to further workforce development. Finally, even without the FUTA surtax, the trust fund would continue to collect \$4.23 billion a year for the administration of these services.

Should you succeed in returning these funds to the states and businesses paying bills surtax, we have worked out an innovative program in Arizona that meets the employment needs of both the public and private sector. As with other programs and policies that the Congress has devolved to the states, this would allow Arizona to participate in a more effective employment services program with the federal government.

Again, thank you for the opportunity to appear before the Subcommittee today on this issue of importance to the workforce, citizens and employers in the State of Arizona. I welcome the change to work with you to help move this proposal through Congress.

Chairman JOHNSON. Yield to Mr. McCrery of Louisiana to question first.

Governor HULL. Yes.

Mr. MCCRERY. Thank you, Madam Chair. And, Governor Hull, thank you for coming to Washington and sharing with us your views on the state of affairs in our unemployment insurance system. And your testimony speaks for itself, but I want to make—let you make it clear that you and your Western Governors' Association are supporting the bill that I have introduced on the House side, 3174. Is that right?

Governor HULL. Yes. Absolutely. The Western Governors—and this is a, again, bipartisan group—have all endorsed the proposal strongly as have the Southern Governors.

Mr. MCCRERY. Now, while it is commendable, in my view, that Governors are concerned about the employer community in their states and want to cut taxes—and I think certainly it is a tax that was imposed for a good reason, but that reason has gone away and so we ought to repeal that tax, as you have stated—but certainly another factor in your support of my legislation is the ever-increasing demand on states to assist in finding people jobs.

With Welfare reform, with recent Federal legislation, it is more and more incumbent on the states to provide services to people to find jobs, to get training, get education, to get into worthwhile jobs. Is that a fair statement?

Governor HULL. Absolutely. And I appreciate it.

Mr. MCCRERY. And right now, you are basically being short-changed. Are you not?

Governor HULL. Absolutely. We are.

Mr. MCCRERY. By the Federal Government.

Governor HULL. And as—I think as you have looked at the list that we have looked at, say, we are at 45 cents, we can't provide the services that we need and want to be able to provide. It would be just a boon to our economy to be able to do a better job with job services.

Mr. MCCRERY. And when you say you are getting 45 cents, what you are saying is that you are sending \$1 to Washington—

Governor HULL. That is right.

Mr. MCCRERY.—in the form of payroll taxes that were designed to provide the administrative expenses to states for administering the unemployment insurance company—unemployment insurance program and you are only getting 45 cents out of that dollar back for the purposes for which the tax was imposed.

Governor HULL. Yes. Absolutely. If they—when you get the Governors together we talk about whether we are donor states or donee states. And I am very aware, and you have compensated for it in your legislation, the fact that there are smaller states that are doing—are getting more than that and appropriately should be. I am—

Mr. MCCRERY. Right.

Governor HULL. I am aware of that.

Mr. MCCRERY. Yeah. And that is taken care of in my legislation. Now, to be fair, I want to point out that of that federally imposed

payroll tax that is collected from employers, sent to Washington, and then sent back to the states, actually 20 percent of that is intended to go into the Extended Benefits Program. So really only 80 percent of that payroll tax is, on paper, designed to go back to the states for administrative expenses.

So I want to make that clear. Where—it is accurate to say you are only getting 45 cents back of every dollar you send, but perhaps it is more accurate to say you are getting maybe 65 percent of what you were intended to get when the tax was imposed. Either way, you are getting shortchanged and you are having to come up, are you not, with funds from other sources to cover your expenses in administering this program?

Governor HULL. Yes. We have to juggle—and, you know, again, I think we could do a much better job if it was adequately funded.

Mr. MCCRERY. Well, again, thank you very much for coming here on behalf of Arizona and also bringing us the news of the Western Governors' Association endorsement of my legislation. Thank you very much.

Governor HULL. Uh-huh.

Chairman JOHNSON. Mr. Cardin.

Mr. CARDIN. Thank you, Madam Chair. And, Governor, it is a real pleasure to have you before our Committee. Let me start off by saying that I do have certain concerns about this legislation. But let me ask you a specific question. If I understand H.R. 3174, it would allow the states to collect and keep most of the Federal FUTA tax, 96 percent of it.

My question is, why should we have a Federal tax then? Wouldn't it be just more efficient for the—to allow the states to impose whatever tax they want to impose which they currently can do? Why have a Federal unemployment tax?

Governor HULL. Madam Chairman, and, Mr. Cardin, that is the way you all have designed it and that is the way we accepted it. And I think you are looking at kind of reforming the whole system. I believe there is certainly a place for you and that it should not be entirely our system. But I think what we would like to do is—as things are devolving to the states, that we would like to be able to do a better job of running our share of the program.

Let me just comment, too, because I realize that when you get into the unemployment issues, there is always the concern whether we are underbenefited or are we overcharged. And we have certainly faced that in the State of Arizona over the last few years. In the late 'eighties, Arizona was in a major recession. And I certainly—you know, we looked at those funds as something that we used a lot. We now have a work force that is largely employed.

But we have been able in the—last couple of years ago, we basically, again, cut our own employers unemployment insurance and raised benefits too. So we have had statewide experience as to what we can do.

Mr. CARDIN. Yes. Now, I guess my concern is that if the revenues are more than you need, but we are imposing the tax, if we let you impose your own tax, you wouldn't have to worry about that. But let me—if I might say, your state has the distinction—this might be—I don't know how to look at it, but you have the distinction of

having the lowest percentage of unemployed people who are receiving unemployment insurance—21 percent.

I guess my question to you is, one of the things that Arizona does that two-thirds of states are in a similar situation, is that you deny unemployment benefits to part-time workers. That is, people who have become qualified for unemployment insurance who are part-time employees, many of whom are women who can only work part time because of their family commitments. They get laid off. They are seeking part-time employment, but they are unable to collect unemployment insurance because of your state's requirement that the person be ready for full-time employment, even though they qualified for their insured benefits by part-time employment. Is that fair?

Governor HULL. Madam Chair, and, Mr. Cardin, we have—again, we have a very successful unemployment program and I would contend, having been in the State Legislature for many years and being active in it, probably one of the reasons it has been appropriately funded and, I believe, appropriately benefits is because it was always a discussion between the employers and the employees. The legislature rarely comes in and changes things.

So obviously what you are talking about is something that has been negotiated through state terms with employers and employees. And I think it is fair. I think we talk about full-time employment and not part-time employment. And, again, you have to look at Arizona as a state that has much seasonal employment.

Mr. CARDIN. Well, I would just urge you to perhaps take this back to your coalition of employers and employee groups. We all want to be more family friendly these days and we certainly don't want to discriminate against a family where they need income, but cannot work full time because of the needs of their family.

Particularly, in the times, when you were having large surpluses and the percentage of your unemployed population receiving insurance benefits is at a historic low—21 percent. And historically, nationwide, we have been at 50 percent or more.

Governor HULL. Yes.

Mr. CARDIN. So it seems to me that you need to sort of evaluate what are you trying to accomplish by your unemployment insurance system. And I would urge you to take another look at that. And, Madam Chair, thank you very much for your courtesy.

Chairman JOHNSON. Governor, I am going to have to leave for just a couple of minutes—

Governor HULL. Okay.

Chairman JOHNSON.—to testify at another Committee on behalf of the cleaning up of Long Island Sound, which is very important to my district. But just before I leave, in your discussion with the Governors who support this bill, did you discuss at all the problem of extended benefits? And do you think there would be opposition to retaining at the Federal level enough of the tax stream to fund an extended benefits program so that when it was triggered in, there would be money there to redistribute among the states? I mean, that is really what the Extended Benefits Program does.

Governor HULL. Yes.

Chairman JOHNSON. It redistributes money from the gross national product to states where there is a high unemployment for a

temporary period. Do you think that reserving some of the current system to fund that kind of program would be a problem for the Governors?

Governor HULL. Madam Chairman, the Governors actually did not discuss it. We discussed really this surtax and that was the extent of it. On my own side speaking for myself, no, I don't think it would be.

Chairman JOHNSON. Uh-huh.

Mr. MCCRERY. Madam—

Chairman JOHNSON. Thank you. Yes. Mr. McCrery.

Mr. MCCRERY. Madam Chair, if I could respond to that before you go so you could hear it?

Chairman JOHNSON. Okay.

Mr. MCCRERY. In my legislation we do preserve an Extended Benefits Program. There is now in the Extended Benefit Trust Fund—well, the cap is about \$16 billion, I think. So Congress has decided, through legislation, that that cap, which is .5 percent of covered wages, is sufficient to meet the needs of an Extended Benefit Program in a recession.

My bill would reduce that to \$14.4 billion or .25 percent of covered wages, whichever is higher. So I would maintain a very healthy balance, roughly twice what we have experienced we have needed in past recessions to take care of extended benefits. I think the legitimate point that could be made is if we do have a recession and we deplete that fund or even cut it in half, there is nothing in my bill that would replenish the fund. And I think that may be a shortcoming in my legislation and I am willing to work with other Members of the Subcommittee—

Chairman JOHNSON. Well, thank you.

Mr. MCCRERY.—the Governors to cure that. But—

Chairman JOHNSON. Well, I thank you.

Mr. MCCRERY.—my bill does not ignore the Extended Benefits Program at all.

Chairman JOHNSON. No. My concern more has been the replenishment. And I think it is a small issue—

Mr. MCCRERY. It is a legitimate point.

Chairman JOHNSON.—that can be discussed in more time. And I would like to ask you to come take the chair while I am gone, Mr. McCrery, and recognize Mr. Foley of Florida.

Mr. FOLEY. Thank you very much. Governor, we are honored to have your presence today testifying before the Committee on this important on this important issue, and to particularly have Mr. Hayworth, who is such a capable representative not only of your state, but, in particular, Native Americans. And that is an issue I would like to discuss today. And it is an issue, if you will, of fairness.

Mr. Shadegg, from your delegation, has brought to light an issue that I wanted to explore quickly with you, if I may. As you know, we recognize tribal governments as sovereign nations, yet we also do not exempt them as we do exempt state governments from paying the Federal Unemployment Tax. Given the importance of tribes in your state, do you think this Subcommittee should explore providing that exemption as a matter of fairness?

Governor HULL. Mr. Chairman, Mr. Foley, this was something that was just brought to my attention and I appreciate your bringing it to my attention and I appreciate the Congressman and my own Congressman, Mr. Shadegg, having legislation regarding it. Yes. As I said, I did not actually know there was a difference and I think it is a very good idea and I would be very supportive of it.

Mr. FOLEY. Thank you. And I also wanted to obviously share the credit with Mr. Hayworth. He has, as I said earlier, and as a prestigious Member of the Ways and Means Committee, been a strong vocal advocate not only for your state, but for Native Americans. And many of these issues we are considering obviously have to be brought forward in the light of fairness.

Governor HULL. Absolutely.

Mr. FOLEY. And I think in order to make equity particularly as it relates to their business and their tribal issues, that we would like to see this. And I commend the now Chair, whose bill we are debating to work with myself and Mr. Shadegg to look at this issue and see if we can define in such a way to provide a provision in your bill to allow for a fairness, if you will. And I yield back.

Chairman MCCRERY. Does any other Member of the Subcommittee or Member of the Full Committee have questions for the Governor? If not, Governor Hull, once again, thank you very much—

Governor HULL. Thank you, gentlemen.

Chairman MCCRERY.—for sharing your views with us and we would welcome you back anytime.

Governor HULL. Thank you. I appreciate it. I will catch a plane back to Phoenix.

Chairman MCCRERY. And now the Subcommittee would call Hon. Raymond J. Uhalde, Deputy Assistant Secretary, Employment and Training Administration, United States Department of Labor.

Mr. Uhalde, your written testimony will be entered into the record without objection and you are free to summarize those remarks as you please in the timeframe roughly equivalent to 5 minutes.

STATEMENT OF HON. RAYMOND J. UHALDE, DEPUTY ASSISTANT SECRETARY, EMPLOYMENT AND TRAINING ADMINISTRATION, U.S. DEPARTMENT OF LABOR

Mr. UHALDE. Thank you, Mr. Chairman, and Members of the Subcommittee. Thank you for the opportunity to testify on the unemployment insurance program. With me today is Grace Kilbane, who is the administrator of the Office of Work force Security.

As this is our first time for testifying on this program under the leadership of the Madam Chairwoman, I am hopeful that today's hearing is as meaningful a step as changes we have had in the employment and training system because of passage on a bipartisan basis of the Work force Investment Act. Today's hearing, I hope, proves to be an important step toward reforming and strengthening unemployment insurance and the one-stop Employment Service programs, known collectively as the employment security system. I will address the employment security reform initiative first.

Extensive research by the Advisory Council on Unemployment Compensation, a large national dialog for reform and other activi-

ties, have laid the groundwork for UI/ES reform. Based on a large part on what we have learned, the President committed in the Fiscal Year 2000 budget proposal to work with our partners and stakeholders toward developing a comprehensive bipartisan legislative proposal centered on five principles—expand eligibility for benefits, streamline filing and reduce employer taxes where possible, put people back to work sooner, combat fraud and abuse, and improve administrative funding.

To accomplish this considerable task, a work group comprised of partners and stakeholders, specifically employers and worker representatives, state agency officials, and Department of Labor officials, was convened. Discussions of this group have been very open and creative and more than 70 ideas for reform were addressed.

I especially want to thank the Interstate Conference of Employment Security Agencies, ICESA, for organizing the work group and chairing the meetings. At this time, I would like to address some of the work group's suggestions for a comprehensive reform proposal organized around the five principles. In the interest of time, I will be brief. My written statement provides more detail.

First principle, to expand eligibility, the work group suggests that we examine, first, fixing the Extended Benefit Program now in this good economy so that it can respond more effectively to any future economic downturns.

Second, to expand benefits to part-time and low wage workers who are laid off. Employers already pay taxes on the wages of these workers, but in many cases they are not eligible for benefits.

Third, allow victims of domestic violence, who are forced to flee work for safety reasons, to qualify for benefits while seeking new employment.

To streamline filing and reduce employer taxes where possible, the work group suggests accelerating the termination of the 0.2 percent FUTA surcharge, and, second, streamlining the filing of the FUTA tax by making minor, largely technical changes to Federal law.

To put people back to work sooner, we should amend the Social Security Act to require states to provide job search assistance to those identified as likely to exhaust unemployment benefits under state profiling systems. Even in this super hot economy, workers exhausting their benefits remain high at about 31 percent for 1999, and duration is 14½ weeks, higher than it should be by as much as maybe ¼ weeks, according to a recent study. Jobs search assistance would put people back to work sooner.

Now, also I am pleased to note that the Fiscal Year 2001 budget continues the President's Universal Re-employment initiative, which aims to serve all dislocated workers in need of assistance. Specifically, the budget request includes \$50 million for re-employment service grants to states for providing re-employment services to unemployment insurance claimants.

To combat fraud and abuse, the work group suggests we grant states access to the National Directory of New Hires for purposes of administering the UI program. A similar provision allowing state UI agencies access to the new hire database was included in the House passed Fathers Count bill thanks to Chairman Johnson's leadership on this provision.

To improve administrative funding the work group believes that the administrative costs of the UI and ES programs are underfunded due to Federal budgetary rules and constraints. Underfunding of UI is affecting the program as evidenced by the reduction in benefit payment and appeals timeliness, by increases in overpayments, and decline in employer tax/wage reporting timeliness.

The work group also believes the best way to arrest this program erosion caused by funding shortages is to move administrative costs to the mandatory side of the budget so funding better tracks workload.

At this point, I would like to ask for the Subcommittee's support with the Appropriations Committee to achieve an interim step toward improving administrative funding for state UI programs. The Administration's Fiscal Year 2001 budget request proposes to fund a larger proportion of each state's projected total workload in the base grant at the beginning of the year. This would give states additional funds to meet their infrastructure costs, more certainly about funding for the year, and an improved ability to plan utilization of resources.

In summary, we acknowledge the difficulty in creating a comprehensive proposal since it must include features which, if offered as free-standing items, would draw opposition from one or more partners and stakeholders, including the Department of Labor.

In fact, if a major area such as benefit expansion were eliminated from any package, we would not be able to reach agreement to include the termination of the FUTA 0.2 percent surcharge in the package. I firmly believe that an opportunity exists now to secure funding and program reform only if a proposal which addresses the major concerns and garners broad support can be developed.

Before addressing last year's legislative action, I would like to recognize Representative Cardin for his efforts on behalf of part-time workers. The bill he introduced today, requiring the payment for certain part-time workers, is an important aspect of reform. I am pleased that this inequity is being addressed, both in the discussions with the reform work group and by Mr. Cardin's bill.

I will address H.R. 1830. This legislation was based on the administration's proposal, and represents an important step toward ensuring that the UI program fulfills its mission in today's changing economy. I want to thank Representatives Levin and English and others who introduced this bill.

Key among the bill's provisions are providing incentive grants to states to voluntarily implement administrative changes, which would take account of a claimant's more recent earnings, making EB more readily available during recessions by using a trigger based on total unemployment, and strengthening administrative funding for UI by increasing the amounts distributed under the Reed Act for Fiscal Years 2000 through 2002.

The significant reforms proposed by H.R. 1830 would result in expanding eligibility, and improving administrative funding of the UI program. Accordingly, we would fully support H.R. 1830 as a first step in comprehensive reform.

As to H.R. 1975, this bill would repeal the 0.2 percent surcharge imposed under the FUTA. We strongly believe that any repeal

should only be considered as part of a comprehensive UI reform package, which couples this relief to employers with assistance to states which administer the program and the workers who depend on it. Therefore, we would oppose H.R. 1975 and any stand-alone proposals to accelerate the termination of the surcharge.

H.R. 3174, Mr. McCreery's bill. While I certainly agree that the states should be fully funded to provide appropriate services to UI claimants, other job seekers, and employers, this proposal would make some very fundamental changes in Federal laws governing the employment security system—changes, which I believe compromise the Federal-State balance and erode the system as a safety net for the nation's work force.

Significant among the bill's provisions are transferring the collection of the FUTA tax from the Federal Government to states, allowing states to retain 96 percent of the collections, and shifting an additional 2 percent to small states. In effect, the Federal Government would establish the tax, but yield the authority to appropriate 98 percent of the tax's revenue.

Under such a funding system, the FUTA revenue does not necessarily track with the workload and there is no guarantee the states would appropriate sufficient revenues either in good times or in downturns. Transferring only 2 percent of the congressional appropriation grossly underfunds the Federal activities. While we agree the administrative funding mechanism for employment security needs repair, we do not believe transferring funding from the Congress to the states ensures full funding. We, therefore, oppose H.R. 3174.

In closing, we have an excellent opportunity to use this period of time in this good economy to move this successful New Deal program to a successful new millennium program. Not only is the economy right, but the time is right. The Administration has made a commitment to change. This Subcommittee and the various House Members have demonstrated their great interest in reform. States, employers, organized labor advocates, and Department of Labor staff have been diligently working on UI reform. We are hopeful that this dedicated interest and leadership can produce a comprehensive approach that would do four things.

First, help part-time and low-wage workers receive the benefits for which they have earned when they were laid off, just as other workers do. The benefit ideas that are on the table would produce equity among workers and assist approximately an additional 850,000 workers a year.

Second, help employers by making it easier to file FUTA taxes, cutting taxes, and providing more resources to help workers get jobs faster to reduce their time on unemployment benefits.

Third, help the economy by making sure the UI program meets the needs of today's labor force and also is prepared for any future economic downturns by making the Extended Benefit program more responsive.

And, fourth, help with the Federal-State administration of these programs by providing adequate funding, needed flexibility, and new tools to prevent fraud and abuse and promote re-employment.

This may seem like a tall order, but the groundwork has been done and a chance of consensus is near, and with the leadership

of this Committee and that of this Subcommittee and Madam Chairwoman, we could achieve great success.

This concludes my formal remarks. And, again, I appreciate the opportunity to speak and look forward to your questions.

[The prepared statement follows:]

Statement of Raymond J. Uhalde, Deputy Assistant Secretary, Employment and Training Administration, U.S. Department of Labor

Madam Chairwoman and Members of the Subcommittee:

Thank you for the opportunity to testify on the unemployment insurance (UI) program. As this is our first time testifying on this program under your leadership, I want to recognize your efforts on behalf of the millions of people who depend on the UI program each year. Just as the Congress and interested parties successfully negotiated changes to the employment and training system with the Workforce Investment Act, I am hopeful that today's hearing is a meaningful step toward reforming and strengthening the UI and one-stop/Employment Service (ES) programs, known collectively as the employment security system.

My testimony will focus on the development of the UI reform initiative, what I hope will be a bi-partisan reform proposal, and on several legislative proposals introduced last year.

With me is Grace Kilbane, Administrator of the Office of Workforce Security.

BACKGROUND

I would like to begin by providing some background information and current activities relevant to the UI program. Enacted in the Social Security Act nearly 65 years ago as a Federal-State partnership, UI is the primary source of temporary, partial wage replacement for the nation's laid-off workers who are seeking jobs. It is also the nation's leading economic stabilizer during downturns, returning \$2.15 to national output for every \$1.00 spent on UI benefits and helping workers put food on the table. It was designed to be administered in connection with the ES program which has helped UI beneficiaries and others find jobs, and assisted employers in finding new workers since 1933. Since the 1930s, the economy has changed, the workforce has changed, and the way we work has changed. Workers and businesses have all been affected.

Previously, this Subcommittee has heard testimony on the Advisory Council on Unemployment Compensation's (ACUC's) final report, issued in 1996. The findings of this group influenced the legislation proposed by the Administration, which was first introduced by Representatives Levin, English, and Rangel in early 1998. This legislation was meant to be a first step to further reform.

In mid-1998, the Department of Labor, in consideration of the ACUC recommendations and other research, announced its plan to conduct a broad dialogue on the UI and ES programs and released a white paper to start that dialogue. The paper focused on the effectiveness and design of the UI and ES programs in today's economic environment. We requested comments from all interested parties in such major areas as the stabilization of the nation's economy, financing benefits, and administrative funding. We convened 65 dialogue sessions throughout the country to provide the public additional opportunities to offer suggestions for reform and over 3,800 individuals participated. The intent of this effort was to listen and learn from partners, stakeholders, and other interested parties.

Based in large part on what we learned, the President committed in the fiscal year 2000 budget proposal to work with our partners and stakeholders toward developing a comprehensive, bi-partisan legislative proposal centered on five principles:

- expand coverage and eligibility for benefits;
- streamline filing and reduce tax burden where possible;
- emphasize reemployment;
- combat fraud and abuse; and
- improve administration.

Obviously, any legislative proposal resulting from this process would need to be accomplished within the framework and concepts established in the President's budget.

To accomplish this considerable task, a workgroup comprised of partners and stakeholders—specifically, employer and worker representatives, State agency officials, and Department of Labor officials—was convened. The discussions of this group have been very open and creative in identifying areas where consensus for change is possible and discussing more than 70 ideas for reform. I especially want

to thank the Interstate Conference of Employment Security Agencies (ICESA) for organizing the workgroup and chairing the meetings.

A COMPREHENSIVE REFORM PROPOSAL

At this time I would like to address some of the workgroup's suggestions for a comprehensive reform proposal. It should be noted that in approaching their work, all parties in the workgroup accepted the fact that, since they were representatives of broader groups, any final package would need to be ratified by additional parties. For example, the participating States have been working through ICESA to brief all States, and DOL would need to secure Administration approval of any final package. For ease of discussion, the proposal is organized by the five principles mentioned above.

Expand Coverage and Eligibility for Benefits. Many agree that the UI program has not responded to changes in the workplace (i.e., increases in part-time, temporary, and short-term jobs) and is not always equitable to low wage workers. We have seen the reciprocity rate drop from an average 49 percent in the 1950s to a low of 32 percent in 1993. A number of factors have been identified as underlying the observed decline in reciprocity rates, although not all of the decline has been explained. More restrictive eligibility requirements and stricter penalties for disqualifications are part of the reason. Research shows that the changing labor force also contributed to the decline. Factors include the shift in unemployment from geographical areas with traditionally high reciprocity rates to areas with lower rates; reduced growth in industries with traditionally high claims, such as mining, construction, and manufacturing; the decline in union membership where members are usually well informed about UI rights; and increases in new entrants to the labor force (e.g. more women). Although there is not consensus on benefit expansion, we are encouraged by the fact that the following proposals have been part of the workgroup's discussions:

- Fix the extended benefit (EB) program now in this good economy, so that it can respond more effectively to any future economic downturns.
- Expand benefits to part-time workers and low wage workers who are laid off. Employers already pay taxes on the wages of these workers. Even so, part-time workers may not be eligible for benefits even if they are seeking work equivalent to the type they lost, and low-wage workers may not be eligible due to low earnings even though they may have a stronger attachment to the workforce than eligible higher-wage workers.
- Allow victims of domestic violence who are forced to flee work for safety reasons to qualify for benefits while seeking new employment.

Streamline Filing and Reduce Tax Burden Where Possible. Employers are concerned with complex tax forms, multiple tax filings, and complex record keeping requirements. They are also concerned about a tax burden which serves to build up Federal UI account balances in the Federal budget beyond apparent need. A comprehensive proposal could include:

- Accelerate the termination of the "temporary" 0.2 percent Federal Unemployment Tax Act (FUTA) surcharge.
- Streamline the filing of the FUTA tax. The workgroup has identified several largely technical changes to Federal law which would simplify reporting for employers.

Emphasize Reemployment. The UI and ES programs could be improved to greater facilitate the return to work of laid-off workers. An early return to work means a reduction in the duration of benefits and exhaustion levels—in other words, overall economic improvement.

- Require States to provide job search assistance to those identified as likely to exhaust UI benefits under State profiling systems.
- I am pleased to note that the fiscal year 2001 budget continues the President's Universal Reemployment initiative which aims to serve all dislocated workers in need of assistance. Specifically, the budget request includes \$50 million for Reemployment Service grants to States for providing reemployment services to unemployment insurance claimants who have been profiled as likely to exhaust their UI benefits.

Combat Fraud and Abuse. Although there are a number of ongoing administrative fraud and abuse prevention activities connected with the UI program, there remains a legislative barrier which prevents more from being done.

- Grant States access to the National Directory of New Hires (NDNH) for purposes of administering the UI program; the NDNH's primary use currently is for child support enforcement. A similar provision allowing State UI agencies access to the NDNH for purposes of the UI program was included in the "Fathers Count" bill that was passed by the House last year.

Improve Administration. The workgroup believes that the administrative costs of the UI and ES programs are underfunded due to Federal budgetary rules and constraints. Underfunding of UI is affecting the program as evidenced by the reduction in benefit payment and appeals timeliness, increase in overpayments, and decline in employer tax/wage reporting timeliness. For example, since 1995 the percent of intrastate first payments made within 14 days (or 21 days for States with a waiting week) declined from about 93 percent to about 90 percent in 1998, the last year for which data are available, despite the fact that workload dropped from 7.8 million to 7.1 million intrastate first payments. With respect to overpayments, while falling workloads would suggest that staff would be able to devote more time to resolving issues and ensuring accurate payments, the nonfraud overpayment rate increased from 1.26 percent of benefits paid in 1995 to 1.43 percent in 1997 and 1.37 percent in 1998. Finally, in 1996, 89 percent of employers filed tax and wage reports in a timely manner and 98 percent of delinquent reports were resolved by the end of the quarter in which they were due, while by 1998 there was a decline in these percentages to 86.9 and 97 percent, respectively. A continued erosion of program performance will damage public confidence in the UI program and result in losses to the unemployment trust fund. The workgroup believes the best way to arrest this erosion caused by funding shortages is to move administrative costs to the mandatory side of the budget.

At this point, I would like to ask for the Subcommittee's support with the Appropriations Committee to take an immediate step toward improving administrative funding for State UI programs. The fiscal year 2001 budget request proposes to fund a larger portion of each State's projected total workload in the base grant at the beginning of the year. This would give States additional funds to meet their infrastructure costs, more certainty about their funding for the year, and an improved ability to plan the efficient utilization of resources.

In summary, we acknowledge the difficulty in creating a comprehensive proposal since it must include features which, if offered as free-standing items, would draw opposition from one or more of the partners and stakeholders, including the Department of Labor. In developing the proposal, the members of the workgroup are striving to achieve a comprehensive package which contains elements that address all major concerns. In fact, if a major area such as benefit expansion were eliminated, we would not be able to reach agreement to include the termination of the FUTA 0.2 percent surcharge in the package. I firmly believe that an opportunity exists to secure funding and program reform only if a proposal which addresses the major concerns and garners broad support can be developed.

LEGISLATIVE PROPOSALS

Now I would like to turn to several bills which were introduced during the first session of this Congress and affect the Federal-State employment security system. They include:

- H.R. 1830—Unemployment Compensation Amendments of 1999
- H.R. 1975—Temporary Tax Termination Act of 1999
- H.R. 3174—Employment Security Financing Act of 1999

H.R. 1830—Unemployment Compensation Amendments of 1999. This legislation was based on the Administration's proposal and represents an important step toward ensuring that the UI program fulfills its mission in today's changing economy and that it remains on a sound financial footing for the 21st Century. I want to acknowledge Representatives Levin and English for the introduction of this legislation.

First, the proposal would provide incentives to States to implement administrative systems—commonly called alternative base periods—that will make the program more accessible to new entrants into the labor force who tend to be lower wage workers. Specifically, it would provide \$20 million in grants to States in each of fiscal years 2000, 2001, and 2002 to voluntarily implement a base period (for determining eligibility for benefits) that takes into account the claimant's more recent earnings.

Second, the proposal would make EB more readily available during a recession. EB triggers would be based on total unemployment rates that are more responsive to rising State unemployment and more accurately reflect when it is most difficult to find work.

Third, the proposal would encourage States to voluntarily build adequate reserves in their unemployment trust fund accounts and as a result avoid having to increase employer taxes, reduce benefits, or borrow during a recession. More precisely, it conditions receipt of a portion of funds distributed under the Reed Act in fiscal year 2003 on State trust fund accounts meeting or making acceptable progress toward a solvency target.

Fourth, the proposal would strengthen funding of the States for administration of the UI program by increasing the amounts distributed under the Reed Act (which is on the mandatory side of the budget) for fiscal years 2000 through 2002.

Finally, the proposal would clarify technical requirements relating to short-time compensation programs, under which employers that choose to participate reduce the workweek of their employees in lieu of temporary layoffs, and the affected employees receive partial UI.

In summary, the significant reforms proposed by H.R. 1830 would result in expanding eligibility and improving administrative funding of the UI program. Accordingly, we fully support H.R. 1830 as the first step in comprehensive UI reform.

H.R. 1975—Temporary Tax Termination Act of 1999. This proposal would repeal the 0.2 percent surcharge imposed under the FUTA.

Right now the Administration projects that Reed Act distributions to the States of excess FUTA balances will occur in 2003. Nonetheless, we believe the repeal of the 0.2 percent surcharge prior to its expiration at the end of 2007 must be accomplished within the framework of the President's budget. Also, we strongly believe that any repeal should only be considered as part of a comprehensive UI reform package, which couples this relief to employers with assistance to the States which administer the program and the workers who depend on it. Therefore, we oppose H.R. 1975 and any stand-alone proposals to accelerate termination of the surcharge.

H.R. 3174—Employment Security Financing Act of 1999. As you know, this bill was developed by a coalition of State officials and employer groups for the most compelling reason of addressing administrative funding problems, as well as to reduce the tax and streamline reporting under FUTA. While I certainly agree that States should be fully funded to provide appropriate services to UI claimants, other job seekers, and employers, this proposal would make some very fundamental changes in Federal laws governing the employment security system—changes which I believe compromise the Federal-State balance and erode the system as a safety net for the nation's workforce. Of the many changes contained in H.R. 3174, I would like to highlight several of particular concern.

This proposal would change the administrative funding system by transferring the collection of the FUTA tax from the Federal government to States, with the States retaining 96 percent of the collections. Another 2 percent would fund a "supplemental" account which would provide additional funds to small States. The remaining 2 percent would be available to the Congress to appropriate for Federal activities. The basic question here is: What incentive does the Federal government have to establish a Federal tax while yielding its authority to appropriate 98 percent of the tax's revenue? That authority would be transferred directly to States.

We believe that administrative funding for the employment security system should be related to the number of claims filed for UI benefits, the number of employers from whom taxes are collected, and the number of unemployed workers and others seeking job-finding assistance. These workload factors do not necessarily track with FUTA revenues. Under a devolved system, it is anticipated that small States would expend all their FUTA revenue, while other States would have more than is needed for administration.

There is no guarantee that States would appropriate sufficient revenues. State legislatures could transfer their FUTA proceeds to the benefit accounts, allowing for tax reduction, rather than expending for administration. Also, most State legislatures meet for only a portion of a year and six meet on a biennial schedule. This might make it difficult for States to respond quickly to changes in workload caused by an unforeseen economic downturn.

The proposal would grossly underfund the Federal administration of UI, ES, labor market information, Veterans Employment and Training, and foreign labor certification programs, which are currently funded out of FUTA proceeds. Assuming that the proposal would have been applicable for fiscal year 1999, the 2 percent of revenue that States would have transferred for congressional appropriation would have been less than half the amount the Congress appropriated for Department of Labor activities for that year. I emphasize that the Federal staff provide national leadership, policy direction, and coordination for these programs. Key among the many functions provided by Federal staff are:

- Administering (through the Bureau of Labor Statistics) statistical programs essential for development of national statistical series, including core economic statistics related to employment and unemployment.
- Reviewing and certifying that State laws conform with Federal law and State activities substantially comply with the requirements of State and Federal law, and negotiating resolution of issues.
- With State partners, establishing standards, policy, and programs to promote and appraise the effectiveness and efficiency of the administration and operation of

UI and ES programs for performance management and facilitating the sharing of best practices.

- Assisting States in the establishment and maintenance of actuarially sound systems of UI by providing consultative and supportive services in the fields of actuarial analyses and special studies.

Concerning State collection of FUTA, simplifying employer tax reporting and filing is an important issue; however, the mere collection of the tax by States does not alleviate the current complex tax offset system, and could actually be burdensome because the States would be working under two sets of UI rules—State law and the Internal Revenue Code. Likewise, employers would still have to comply with different definitions. Additionally, there are questions concerning enforcement, underpayments, and back-up systems. Further, multi-State employers, who now report only to the Internal Revenue Service (IRS), would have to report to many States. As far as saving costs, a joint Treasury/Labor report indicated that there would be no real cost saving without harmonizing definitions of wages, employment, employee, etc.; the coalition proposal does not propose to harmonize these definitions.

As an aside, I would like to mention the Simplified Tax and Wage Reporting System (STAWRS) project which is an inter-departmental initiative comprised of staff from the Department of the Treasury, the IRS, the Social Security Administration, and the Department of Labor. STAWRS is currently working on a “Targeted Harmonized Wage Code” that State UI agencies and the IRS (and other taxing authorities) could adopt to reduce employer burden caused by different definitions. Thirteen wage components in 96 different laws have been identified for harmonization. The STAWRS project office and the UI office have entered into an agreement to conduct a joint study on the impact of the Targeted Harmonized Wage Code on UI benefit amounts. The study is scheduled to be completed in September, 2001.

Finally, and most significantly, this proposal would effectively repeal important provisions of Federal UI law. Currently, to receive administrative grants, States must meet the requirements of Title III of the Social Security Act. Although Title III is not repealed, there would be no effective mechanism to enforce State compliance with its requirements since the Federal government would no longer provide administrative grants. Some of the significant requirements which would be nullified are “methods of administration” assuring prompt and accurate payment of benefits “when due,” a fair hearing for all claimants whose claims are denied, and a limitation restricting UI grant funds to expenditure for proper and efficient administration of the UI program. For the same reason, the proposal would effectively nullify the requirements that State UI programs participate in the Income and Eligibility Verification System and the Systematic Alien Verification for Entitlement system, and cooperate with child support enforcement agencies.

In summary, while we agree that the administrative funding mechanism for the employment security system needs repair, we do not believe that transferring funding from the Congress to States ensures full funding. We oppose H.R. 3174. We believe a reform bill must address the most fundamental principle of the UI program—assurance of adequate benefits for a sufficiently large number of unemployed job seekers so that the program is an effective economic stabilizer. This has been and remains, after all, the primary purpose of the UI program.

CONCLUSION

In closing, we have an excellent opportunity to use this period of time, in this good economy, to move this successful New Deal program to a successful new millennium program. Not only is the economy right, but the time is right. The Administration has made a commitment to change; this Subcommittee and various House members have demonstrated an interest in reform; and States, employers, organized labor advocates, and Department of Labor staff have been diligently working on UI reform in various forums. We are hopeful that this dedicated interest and leadership can produce a comprehensive approach that would:

- Help part-time and low-wage workers receive the benefits they have earned when they are laid off, just as other workers do. The benefit ideas that are “on the table” would produce equity among workers and assist approximately an additional 850,000 mostly low-wage workers per year.
- Help employers by making it easier to file FUTA taxes; cutting taxes; and providing more resources to help workers get jobs faster to reduce their time on unemployment benefits.
- Help the economy by making sure the UI program is responsive today and also prepared for any future economic downturns by changing the extended benefit program.

- Help with the Federal-State administration of these programs by providing adequate funding, needed flexibility, and new tools to prevent fraud and abuse and promote reemployment.

This may seem like a tall order, Madam Chairwoman, but the groundwork has been done, a chance of consensus is near, and with your leadership and that of this Subcommittee, we could achieve success.

This concludes my formal remarks. Again, I appreciate the opportunity afforded me to speak to the Subcommittee and look forward to working with you, the States, and all other stakeholders.

Chairman MCCRERY. Thank you, Mr. Uhalde. Before I begin questioning Mr. Uhalde, I want to point out that in our effort to get Governor Hull on, on time, we dispensed with opening statements. At this time, I would tell any Member of the Subcommittee if you have an opening statement, you may present that and it will be included in the record. And I have one that I have presented to the Subcommittee staff for inclusion in the record and any other Member may do so without objection.

Mr. CARDIN. Thank you, Mr. Chairman. It is my understanding that the Chairman and I do have opening statements that we would be ask made part of the record.

[The opening statements of Chairman Johnson, Mr. Cardin, and Mr. McCrery follow:]

**Opening Statement of Hon. Nancy L. Johnson, a Representative in
Congress from the State of Connecticut**

Most of the issues that our Subcommittee has undertaken in the last two years have been fundamentally bipartisan. Don't get me wrong. We still found issues to argue about in child support, child protection, Title XX, and welfare reform, but in the end all of our legislation has enjoyed solid bipartisan support. In fact, many of our bills have emerged from Subcommittee on voice votes.

But now we come to the Unemployment Compensation system. Although we all agree that the nation must have a strong, well-funded program for unemployed workers with a history of labor force attachment, there are lots of diverse views about how the system should be strengthened. At the risk of over-simplification, let me claim that there are three big issues that we are trying to resolve.

First, the 0.2 percent FUTA surtax was imposed in 1976 when the Unemployment Compensation system was in serious financial trouble. Many businessmen and members of Congress thought that there was an understanding that when the federal parts of the system were back on firm financial footing, the surtax would be dropped. That was almost a quarter of a century ago, and still the surtax continues to impose additional taxes of over \$1.7 billion each year on American businesses. Most Republicans want to repeal the surtax; the Administration and most Democrats would rather retain the money in federal accounts.

Second, under Mr. McCrery's leadership, a substantial group of Republicans, joined by a few Democrats, are proposing to simplify the collection of the state and federal taxes that support the unemployment system and to provide states with greater control over funding for state administration of the program. Democrats seem to generally oppose this proposal because, in their view, it weakens the federal commitment to the program.

Third, Mr. Levin and Mr. English have introduced legislation that would make unemployment benefits more accessible to unemployed workers and strengthen the solvency of state accounts. Most Republicans seem to oppose this bill, however, because it could lead to increased unemployment taxes.

There is a fourth issue that is now brewing; namely, whether unemployment benefits should be used to pay cash benefits to parents who take family leave after having a baby or adopting a child. Many Democrats and the Administration support this proposal while Republicans generally oppose the proposal because it seems to violate a long-standing tenet of the unemployment system that benefits go to those who are involuntarily unemployed. We have called a hearing next week to deal with this issue in great detail.

Despite the seemingly partisan nature of these various proposals, a remarkable bipartisan group of about 25 representatives from the Clinton Administration, workers, business leaders, and state administrators has met seven times over the past year to explore whether a compromise among these various proposals might be possible. Although this group has not reached a final compromise, it is my understanding that they have reached agreement on many issues. We will hear more about this important effort today.

For my part, I am not at all certain what if any action our Subcommittee should take. I plan to listen carefully to our distinguished witnesses today, to discuss these matters further with my colleagues on both sides of the aisle, and then decide whether there is enough agreement to move forward.

**Opening Statement of Hon. Benjamin L. Cardin, a Representative in
Congress from the State of Maryland**

Madame Chairwoman, reviewing proposals to reform our Nation's unemployment system is an important and timely duty. With unemployment at a 30-year low, we have a rare opportunity to fix the roof while the sun is shining.

Before we evaluate various plans to modify the current unemployment compensation system, we should first agree upon what we want and expect from such a system. In this context, let me quickly mention what should be three consensus objectives: (1) providing a timely and reliable source of partial wage replacement for unemployed Americans; (2) stabilizing both the national and regional economies during recessionary periods; and (3) linking individuals to re-employment programs.

Measured against these goals, the so-called devolution approach taken by HR 3174 falls short. The bill focuses too much on dismantling the Federal role in combating unemployment, and not enough on implementing reforms to improve the long-term solvency and accessibility of our Nation's unemployment compensation system.

Let me mention a few specific concerns about HR 3174. First, the legislation would sever the link between administrative funding and need. For States hitting a recession, this would mean they could no longer expect a boost in their administrative funds without raising taxes in the middle of an economic downturn.

Second, by eliminating the ability of the Federal government to disburse administrative funds, HR 3174 guts the primary enforcement mechanism for Federal protections in the unemployment system, such as assuring prompt and accurate payment "when due" and providing a fair hearing for individuals whose claim was denied.

Third, the bill undercuts the future solvency of the Extended Benefits (EB) program by eliminating its funding source (proceeds from the FUTA tax).

And fourth, the legislation ignores one of the primary problems with the current Unemployment System—a declining percentage of unemployed Americans receiving UI benefits. In fact, because the bill breaks the connection between administrative funding and UI workloads, HR 3174 would disproportionately benefit those States with the lowest UI reciprocity rates among the unemployed.

This is not to say that we should remain unresponsive to one of the major complaints that HR 3174 seeks to address, namely inadequate Federal funds for the administration of the unemployment compensation system.

Congressman Levin has introduced legislation to increase administrative funding for States that make progress in improving the solvency of their State UI Trust Funds. Furthermore, the so-called working group on unemployment compensation, which represents employers, unions, the Administration, and the States, have discussed making UI administrative funds mandatory, rather than discretionary.

And finally, the Administration has requested an increase in funding for both UI administration and re-employment services. All of these proposals deserve our attention.

As we consider these and other proposed reforms, I want to highlight one issue that should be addressed in any comprehensive package. Currently, unemployed, part-time workers who meet monetary eligibility requirements are prohibited from receiving Unemployment Insurance in two-thirds of the States solely because they are seeking part-time rather than full-time employment. This means that a laid-off parent can be denied unemployment compensation simply because they are seeking to continue to work part-time in order to care for a child.

Such a policy is neither family-friendly, nor fair to part-time workers. Both the research-oriented Advisory Council on Unemployment Compensation and the busi-

ness-driven Committee for Economic Development have recommended prohibiting this type of discrimination against part-time workers.

To address this inequity, I introduced legislation today to prohibit States from denying UI benefits for individuals who otherwise qualify for unemployment compensation based on part-time work. I believe the bill is particularly relevant for unemployed women since they comprise roughly 70% of our nation's part-time workforce.

Madame Chairwoman, I look forward to the testimony of our distinguished guests today, particularly my friend Sandy Levin, who is the former Ranking Member of this Subcommittee.

Thank you.

**Opening Statement of Hon. Jim McCrery, a Representative in Congress
from the State of Louisiana**

Chairman Johnson, I want to thank you for scheduling this hearing today on Unemployment Insurance administrative financing reform. As you know, I have introduced legislation to restore common sense to the administrative financing of the UI system and look forward to working with you and the other members of the Subcommittee to address this issue.

As you and the other members of the Subcommittee know, the employment security system, established as a federal-state partnership more than 60 years ago, is the system employers use to provide unemployment insurance and a public labor exchange for workers. Since its inception, major structural changes to our country's economy have taken place as a result of rapid technological advances and the growth of globalized trade and investment. Adjusting to meet the demands of our changing economy, our nation's labor market has fundamentally changed as well. Therefore, the employment security system should be reformed to meet the demands of the changing labor market and to ensure that states are able to provide the services necessary for employment and re-employment services aimed at matching employers and qualified job-seekers.

Madam Chairman, a major focus of reform should be to improve the efficiency of the current administrative financing mechanism and to reduce the tax burden imposed on employers.

Unfortunately, states aren't receiving a proportionate return on the FUTA tax dollars contributed by their employers. Since 1990, less than 59 cents of every FUTA dollar has been sent back to the states for the purpose of administering their unemployment system, and the percentage is shrinking. Now less than 52 cents is returned. As a result, states are being forced to either make up for the shortfall from their own general funds, impose new payroll taxes, or cut back on services provided to workers.

Madam Chairman, to address this issue, I have introduced H.R. 3174, the Employment Security Administrative Financing Act of 1999. H.R. 3174 is designed to address the problems that the current system continues to impose on the states and the FUTA taxpayers, while preserving and strengthening protections for workers.

Specifically, the bill would: reduce the tax burden on large and small businesses by repealing the unnecessary, "temporary" 0.2% FUTA surtax imposed in the 1970's; eliminate inefficiencies experienced by employers by transferring responsibility for collection of the FUTA tax to the states; strengthen administration of the system by ensuring that states get a greater return on their employers' FUTA tax dollars and by ensuring greater accountability for the use of these funds; improve employment services with an emphasis on re-employing dislocated workers; combat fraud and abuse in the present system; and, increase state flexibility to administer their unemployment insurance and employment services programs to serve local needs.

Without these reforms, the current system will continue to overtax and overburden employers, shortchange states, and, most importantly, underserve those who need it most—the involuntarily unemployed and those striving to move up the career ladder.

Madam Chairman, I applaud you for scheduling this hearing and look forward to working with you to bring about a much-needed reform of the current system which will bring our employment security system into the 21st Century.

Chairman MCCRERY. Without objection. Mr. Uhalde, to you, and, Mr. Cardin, who have both questioned the efficacy or the rationale behind a federally imposed tax basically being shifted to the states for their use, we would point out to you that is exactly what we do with the highway trust fund. We federally impose a gasoline tax, we collect the money, and then we ship it to the states and they may use it basically however they like within the parameters that we set, which is exactly what we propose to do in my legislation. And I don't hear anybody from the administration here saying we need to change the operation of the highway trust fund.

In your conclusion, you point out four goals, one of those being to help employers by cutting taxes. And I am certainly pleased that the administration supports repeal of the .2 percent surtax. However, isn't it so that if we federally impose an expansion of benefits, that that will require the states to increase taxes to cover the costs of those expanded benefits?

Mr. UHALDE. Mr. Chairman, you are right, the administration does support a repeal of the 0.2 percent FUTA surcharge earlier than its scheduled time if, and only if, we have a more comprehensive agreement and that agreement includes expansion of benefits.

Chairman MCCRERY. Well, if I may interrupt?

Mr. UHALDE. Yes, sir.

Chairman MCCRERY. In fact, you said if legislation did not contain expansion of benefits you would not support the repeal of the 0.2 percent surtax.

Mr. UHALDE. That is correct.

Chairman MCCRERY. So it is—while I appreciate your call for compressive reform, what you are really saying is you have got to have expanded benefits or it is no deal. And that—hence, my question, if we have expanded benefits, don't we have to pay for them?

Mr. UHALDE. But the whole point of this exercise, as you well know, is that the unemployment insurance fund, at this point, does have a good balance. And if there is any time that we are going to use the revenue that currently resides in the trust fund, it is now to be able to expand benefits to workers.

The purpose of the trust fund is not just to collect revenues and to keep them there. Having reciprocity rates of 21 percent in states, I don't believe is necessarily a badge of honor that we are not being able to pay benefits out to individuals, individuals for whom UI taxes are being paid. The part-time workers—taxes are being paid on the part-time workers. They are laid off. They then are looking for part-time work and they are denied benefits. It seems to me it is a matter of equity and justice that these workers be able to receive benefits.

Chairman MCCRERY. Well, so are you proposing that the Federal Government finance the increased cost of providing services from trust fund balances?

Mr. UHALDE. No. I believe in the discussions that we have had and we have had some questions about how one would cover any extensions of eligibility benefits, and I think there have been some interesting discussions. There is not agreement on that. But, you

know, one obvious way is to cover it through the states as it is—has been in the past.

Chairman MCCRERY. Which would necessitate an increase in their taxes.

Mr. UHALDE. Well, if the states didn't have adequate balances in their trust funds.

Chairman MCCRERY. And I would assume that they would increase their payroll tax for employers. So what you give with one hand, you would take back with the other.

Mr. UHALDE. Well, it is not clear to me that states are in a position, certainly the vast majority of states, that would necessitate tax increases.

Chairman MCCRERY. Well, Mr. Uhalde, you have mentioned that you would favor an increased appropriation as a transition to making the administrative expenses a mandatory Federal expense rather than a discretionary public Federal expense. Is that right?

Mr. UHALDE. Yes. That is correct.

Chairman MCCRERY. And do you—can you expound a little bit on the structure of the mandatory regime once that is in place?

Mr. UHALDE. I am sorry. Could you repeat it?

Chairman MCCRERY. Could you expound a little bit on the mandatory regime that you had put in place to ensure adequate funding of administrative expenses?

Mr. UHALDE. Well, I think we have been at least discussing as—amongst the work group, a couple of different mechanisms. First of all, the advantage on the mandatory side is we are trying to get the amount for administration to better match the workload. And we think, since the benefits are on the mandatory side, that the administrative dollars ought to be on the mandatory side.

Regarding the mechanism for actually distributing funds to the states, we have considered several options, one of which would be by a formula driven by workload that would have some floor for small states and be able to distribute resources to states on an automatic basis.

The second option would be some sort of a matching grant approach. Actually, this Committee is very familiar with this approach, where states would appropriate some portion of the money and then that would drive the distribution from the Federal trust fund—say ²⁵/₇₅ or something else.

Right now, we are looking at the advantages and disadvantages of each of these approaches and other approaches. And so there are different ways to actually distribute the funds if it is on the mandatory side of the budget.

Chairman MCCRERY. Well, Mr. Uhalde, it is the Federal Government that is imposing a tax rate on employers in the various states. And we say to them that the purpose of exacting that tax is to pay for the administrative expenses of administering the unemployment insurance system. So how can we justify having any mandatory program that falls short of returning every penny of that back to the states minus whatever expenses that we legitimately need for Federal administration?

Mr. UHALDE. Well, first of all, yes, there is Federal administration. There is also, as was pointed out in discussion before, Extended Benefits. But—

Chairman MCCRERY. But short of that—

Mr. UHALDE. Yes. Your question is, why has the Congress and the administration collectively over the last several years, not returned a higher proportion back to the states.

Chairman MCCRERY. Well, I know why we haven't done it over in the past, because we have had a deficit. Now, we have a surplus. And I am saying to you, I can't think of a rationale now for—in fact, the rationale we did use wasn't a public rationale; it was a hidden rationale. We all knew it and we all kind of winked and went ahead with it. But now, we don't even have the cover of the deficit. So how can we possibly justify not putting in place a mandatory regime to ship back to the states every penny based on this?

Mr. UHALDE. Well, first of all, as you well know, while we may now have a surplus, we also have an overall Federal budget strategy collectively with the Congress and the administration that you have to develop this UI program policy in concert with that entire overall policy. Currently revenues coming in from the FUTA tax are, what, six-and-a-half—\$6 billion? The administration of the programs is currently funded at something like \$3.5 billion. And the question that is going to arise is, what is going to happen in the overall Federal budget strategy with that difference of \$2.5 billion?

Now, the administration believes that there ought to be more of that money devoted to administration of the unemployment insurance program. I think it is an overall strategy, budget and administration strategy, as to whether that is every dime or not.

Chairman MCCRERY. Well, thank you. I appreciate the administration moving in what I think is the right direction. Mr. Cardin.

Mr. CARDIN. Thank you, Mr. Chairman, and thank you very much for your testimony. We may have projected surpluses, but we still have the same budget rules. And that makes it difficult for us. And you give a very diplomatic response to the Chairman's question. Maybe we can find a bipartisan way to deal with the budget caps and deal with the size of a tax bill and deal with this FUTA surcharge also. So maybe we can find a bipartisan way to do it.

But until we do, we are stuck with the budget rules. We are stuck with the appropriation process and their caps and your stuck with whatever—you—I think you have been very clear that you want to spend more of this money.

Mr. UHALDE. Absolutely.

Mr. CARDIN. And the states need it.

Mr. UHALDE. Absolutely.

Mr. CARDIN. So let's try to figure out a way that we can get this done in a fair way to the states. And, Mr. Chairman, let me point out—I thought I did in my question to Governor Hull that my reasons for raising the issue of whether the states should impose the tax that they collect, was not to suggest that as a solution, but to just raise a question about the bill that you filed. I certainly support the national system with a national tax for unemployment.

And it gives us—and I stated this in my opening statement—gives us the ability to have a framework for unemployment insurance in this country, a way we can enforce the states establishing certain standards and having the Federal Government act as a backstop to deal with national economic turns.

So I guess let me just ask a couple of questions, if I might, about H.R. 3174 and try to get your response to some of these issues. As I understand it, it would sever the link between the administrative fundings of the states and their needs so that some states would be getting a lot—do a lot better, other states would do a lot worse as to their needs. And it does not really have a relationship to the ability of the state to deal with these additional burdens.

Mr. UHALDE. Well, while the principle reason for the proposal is to address the adequacy of administrative funding, there is no guarantee with state appropriations that necessarily states are going to appropriate the adequate amounts for administration. There is no guarantee that that will happen when one enters a downturn and states are trying to shepherd their resources as much as has been done in the Federal Government through deficits. So there is no automatic guarantee that that is going to happen at the local level.

Mr. CARDIN. A second concern I have that is more fundamental is that there would be no—I don't know of any way that we could enforce standards if the states have all the money and remit to us just that extra four percent of the total amount. For example, let us say a state didn't have any effective appeal mechanism for someone denied unemployment insurance. What could you do to get the state to impose an effective appeal process for that individual?

Mr. UHALDE. Well, there are currently two ways right now. There is the sort of the big club, which is the offset credit.

Mr. CARDIN. You would lose that though under H.R. 3174.

Mr. UHALDE. No. We would retain that. That assures state laws are in conformity with Federal law. The second—

Mr. CARDIN. Oh. OK. Correct.

Mr. UHALDE. And that is the big club. And it is when we certify that states' laws are in conformity with Federal law and our regulations. Then we certify the offset credit. But that is a big deal. The second—

Mr. CARDIN. But if you did do that you would be imposing another five percent tax and save which is—

Mr. UHALDE. Absolutely. At 5.4 percent—

Mr. CARDIN. Right.

Mr. UHALDE.—offset credit. The second and the one that is an important lever in ensuring the types of issues that you talked about, prompt appeals hearings, proper and efficient administrative methods, is that we are making grants to states conditioned on states applying proper methods of administration that are laid out in the Title III of the Social Security Act.

If we are not making grants, as under a devolution proposal, then, in fact, the Federal Government doesn't have that mechanism for enforcement.

Mr. CARDIN. Thank you. And just let me also thank you for your comments about the part-time employee issue. And you raised a very good point on that. This unemployment insurance is an insurance program. Part-time employees insurance premium or insurance is paid on their employment. They have to remit the money under their state program, so the state is taking the revenue without providing any uninsurance protection.

Mr. UHALDE. Well, exactly. I mean, the system as a whole is essentially making a profit off of part-time workers who—in many states, part-time workers who seek to return to work in a part-time status. And increasingly, that is an important work force component that employers who are scrambling to get workers are putting together all sorts of benefit packages to attract nontraditional pools of work. And part-time workers are an important source for employers.

And having the ability to tell workers that they will be treated like every other worker, as long as they earn the qualifying amount of wages, I think, is important as both an efficiency argument for employers as well as an equity argument.

Mr. CARDIN. Thank you. Thank you, Mr. Chairman.

Chairman MCCRERY. Mr. English.

Mr. ENGLISH. Thank you, Mr. Chairman. Mr. Uhalde, my formative experience with Unemployment Compensation came in the Pennsylvania and state government in the early eighties, when after a long period of maintaining relatively low unemployment in the late 'sixties and early 'seventies, and relatively low tax rates, Pennsylvania abruptly went into a recession and then went into a series of recessions. And by the early eighties, we had, as I recall, a trust fund negative balance approaching \$3 billion, which, in the state government, is real money.

I wonder, looking at the proposals that have been laid out here, including the Levin bill, which I have cosponsored and which the administration supports, my bill and Mr. McCrery's bill, how would you assess their relative incentives for state solvency? And do they provide—how do each provide for states to maintain adequate balances even when we recognize state officials frequently find it very difficult to focus on these issues in the long-term and there is a tendency in state government maybe to short some of these commitments and not provide adequate funding?

Mr. UHALDE. Well, Mr. English, of course, I think your bill—yours and Congressman Levin's bill—directly addresses the solvency question. And I think it is a serious question that we have to look at. This bill does it through a system of incentives. I think there is criticism that the approach of setting some de facto standard of 1 year of benefits is arbitrary; but it is voluntary. And it uses an incentive approach using distribution of funds from the Reed Act.

Why that is important? There is some significant number of states, large states, that effectively have in their trust funds—they are not quite on a pay-as-you-go basis, but they have one quarter worth of resources there for any type of recession.

Now, the question we have to ask in that kind of system is, are we going to pay now or are we going to pay more later? And the experience with Pennsylvania, the experience with Michigan, and many other states through the eighties, was that through the need to borrow, that they would end up paying more.

But the other thing is the timing. To repay substantial amounts of borrowings and to sort of make the trust funds whole after the recessions have happened is to either have to lower benefits or raise taxes during a downturn—

Mr. ENGLISH. Sure.

Mr. UHALDE.—or during a recovery.

Mr. ENGLISH. Mr. Uhalde, I think we understand, you know, broad-stroke—

Mr. UHALDE. Uh-huh.

Mr. ENGLISH.—the need to move in the direction of encouraging states to maintain their solvency. And I guess the question I wanted to pose to you directly on the last point, on Mr. McCrery's bill, do you have any concerns about the incentives built into that bill that allows states to run balances and then potentially, down the road, make some use of them? Is—do you feel that there are adequate incentives in Mr. McCrery's bill to provide long-term solvency at the state level?

Mr. UHALDE. Well, I don't believe there is a direct response to the solvency question in Mr. McCrery's bill. And the question on the Extended Benefits was already addressed. And I think there was a fair conversation on that where once that pot was exhausted or whittled down, there is no mechanism currently to replenish it.

Mr. ENGLISH. Okay.

Mr. UHALDE. But, no, there isn't a direct response on that.

Mr. ENGLISH. Okay.

Mr. UHALDE. And I am concerned that problems with addressing unemployment insurance and adequately funding it at the Federal level, would be repeated 50 times over at state legislatures—

Mr. ENGLISH. Sure.

Mr. UHALDE.—in trying to appropriate the—

Mr. ENGLISH. Before my time runs out, I do have one last question. And that is, you have talked about being willing to be flexible as part of an overall package on the .2 percent surtax. One of the tax issues that doesn't typically get brought up in the context of tax reform is the fact that since 1986 or '87, we have been taxing UC benefits in a way that substantially reduces their value to the workers.

Is the administration willing to consider taking the tax off of Unemployment Compensation benefits as part of an overall fix to this system? And is it the view of the Department of Labor that taking the tax off of UC benefits would substantially improve their value to the people that we are trying to serve?

Mr. UHALDE. Well, clearly, the answer to the latter is, yes, that taking the tax off would improve the value to workers. I have not been involved in any Administration discussion of taking the tax off. Again, we are caught in the whole issue of the overall budget package. And there has been discussion in the work group, frankly, to whether or not some of those revenues from the tax ought to be targeted toward some of the aspects of expansion, for example, in this.

Mr. ENGLISH. Sure. Thank you. And, Mr. Chairman, I thank your indulgence. Let me say, I hope that the administration will take a look at the tax on UC benefits. I think this is an extremely important issue. It is one that has been long neglected and has needed a champion. The rollback of this tax has never been proposed by the administration. I think the time has come to take a look at this. I think this is one tax cut that even the administration will concede is not tax cuts for the rich. Thank you, Mr. Uhalde.

Chairman MCCREY. Thank you, Mr. English. I thank you, Mr. English. As to your point about incentives, I can—my experience comes from the State of Louisiana with the Unemployment Compensation system. And I can assure you that that experience in the eighties has made us very much aware of the need to prepare for downturns. We were hit very hard, as was Michigan and a few other states. We had to borrow sizeable amounts of money from the Federal Government and pay it back with interest.

And, as a consequence, we had to increase, on a temporary basis, a true temporary basis, I might add, the payroll taxes on our state's employers, which was a heavy burden. But once we paid off those sizeable loans that we got from the Federal Government, we took the temporary surtax off, which should be a lesson to Federal policy makers. Once the need for the temporary tax is gone, you should do away with the temporary tax. And, Ms. Johnson, do you have questions for Mr. Uhalde.

Chairman JOHNSON. I am sorry I had to miss your testimony, but I do look forward to working with the Administration on this issue. I don't see that anyone who has testified today can say this is a program that is working. And when you listen and you look at the chart that I was reading from, some states have four or 6 months of benefits in reserve and others have 168 months. This is not a system that is healthy.

It is also true that there has been a dramatic change in the kinds of services that unemployed people need. Really, a radical change from 10 years ago. And the kinds of services that states need to be able to provide are more expensive. They are more technologically based. There are not just transportation—they are doing a lot of different things. And they need the resources and the flexibility. I don't see any reason why we can't think this through in a way that gives states better resources, since we all acknowledge that part of this was deficit-driven, and, at the same time, guarantee that the Extended Benefits program will not only be in place, but will be funded.

I think the regular benefits program has always had the backup only of Federal loans. And my state, as well as Louisiana, was one that borrowed heavily, spent years paying back the costs of recession, and then, when those costs were gone, they did gradually lower the rate. Now, that can be done at the local level. It is very hard to do that at the Federal level. Once we get it in there—I mean, the FUTA surtax is 25 years old. That is my understanding—my recollection. Is that correct? Twenty-five years? So, you know, it is not a temporary tax.

So the degree to which we are able to really honestly manage a program like this, it is not great. So if we focus our interests and our expertise and our commitment to funding what we need to fund, which is the Extended Benefits program, because that really does require a redistribution, in a sense, of wealth between states that are doing well and states that aren't in a period of recession, then I think we have a chance to reform and strengthen that program and, at the same time, give states better resources to meet what is a very different and very exciting and very positive demand. And the better the states meet it, the better people getting unemployment benefits will do getting back into the work force.

I don't see any reason why we can't do this in a way that is a win-win for everybody. And I just hope the administration will get back to us on sort of the key things that you are concerned about. And I don't know whether we can open it up to part-time people right now. We will look at every idea that is brought up here today.

But I think we also need to look at what is the incentive we provide for unemployed people to participate in job training, because many are afraid of it. I mean, they don't participate because, frankly, they have never seen a computer and they are hoping like heck they will get a job that will require the old skills. And I think we need to think also about what help and what incentives do people need to change careers and change their lives, because it isn't easy, but it does work. So I thank you for your testimony and I look forward to working with you.

Mr. UHALDE. Thank you, Madam Chairman.

Mr. MCCRERY. Thank you, Mr. Uhalde, very much for your testimony and your patience in answering our questions. And now, as Ms. Johnson and I have changed chairs, I would ask the final panel to approach the witness table as Mr. Robert C. Gross. Chuck Yarborough, David Smith, Mark Wilson, Hon. Gary Forster, and Van Doorn Ooms.

Chairman JOHNSON. I would like to welcome this panel. You may be aware that the Subcommittee has been doing some field hearings, and those have generally brought us to visit some of the one-stop centers that have developed at this end of the country. And I would have to say I am very pleased to have with us Mr. Robert Gross, who has developed a level of integrated services at these one-stop centers that, frankly, I have not had the privilege of visiting. So we look forward to the panel's testimony. Feel free to stray from your written testimony. We do include all of your statements in the record of our Committee proceedings. So if you would like to summarize your hearing and maybe address issues that have been raised, that is always very helpful to us.

Mr. MCCRERY. Madam Chair.

Chairman JOHNSON. Oh, and I should mention, you know, the light. It is red, yellow, and green. When you get to yellow, you should recognize your 5 minutes is coming to a conclusion, and then we will have more time for questions.

Mr. MCCRERY. Madam Chair.

Chairman JOHNSON. Yes, Mr. McCrery.

Mr. MCCRERY. If I might just take a minute to introduce a colleague from the State of Louisiana, Mr. Garey Forster, who is the Secretary of Labor in Louisiana, and comes to that position with considerable experience from the legislative end. He was a State Representative for many years, representing the New Orleans area. So he comes to us with a great deal of experience from both the policymaking side and the policy enforcement side. So welcome, Mr. Forster, and thank you for making the trip.

Mr. FORSTER. Thank you, Jim.

Chairman JOHNSON. Thank you, Mr. McCrery, and also for pointing out his background because it is very useful to us to have someone who has had your breadth of experience before us. Let us start with Mr. Gross, Robert Gross, who is President of the Interstate

Conference of Employment Security Agencies and Executive Director of Utah Department of Work force Services.

STATEMENT OF ROBERT C. GROSS, PRESIDENT, INTERSTATE CONFERENCE OF EMPLOYMENT SECURITY AGENCIES, AND EXECUTIVE DIRECTOR, UTAH DEPARTMENT OF WORK-FORCE SERVICES

Mr. GROSS. Thank you, Madam Chair and Members of the Subcommittee. I am pleased to be here and certainly grateful for the extension of your invitation to testify here. As you indicated, Madam Chair, I wear a couple of different hats. In fact, I am wearing several hats, although, I am here to testify today on behalf of the Interstate Conference of Employment Security Agencies. I am also a state administrator, and also have had the privilege of chairing the work group to which Mr. Uhalde and others have referred to during the course of the past year, in which we have attempted to forge a comprehensive and bipartisan approach to Unemployment Insurance and Employment Service reform.

You have my written testimony, as was acknowledged. So I will attempt to extrapolate five or six key points that we think are important. And again, I would reiterate that while my positions here—I will be articulating positions on behalf of the Association and my 53 colleagues from the states and territories, and not exclusively and obviously my feelings or concerns about my own State of Utah.

Let me first address the point that has already been addressed, and that is plain and simply, the Federal grants to administer Unemployment Insurance and the Employment Service systems need to be sufficient. They have been inappropriately low for the past several years. In fact, Department of Labor statistics indicate that the Unemployment Insurance administration system has been under-funded by about 10 percent per year for several years, and the employment service purchasing power has been eroded by nearly 60 percent since the early eighties.

Again, as you have heard in previous testimony, there is almost uniform and unanimous consensus among work group members that we need ways to better fund the system and, yet, adequate funds seem to be inherent within the amounts collected from the employees of this country. One of the things that we need, we would encourage this Subcommittee to look at, of course, is moving the funding of this from the discretionary side to the mandatory side of the budget. We commend Mr. McCrery for his approach. We think that offers one thoughtful approach for that important budget consideration.

As you have also heard, there has been other testimony today that there are other proposals that our work group has looked at, including a formula approach and a matching grant approach. We think there is good in each of those approaches, and we would like to work—continue to work together as a work group, but also work with this Subcommittee in finding a solution.

Second, I would like to reiterate that we need to invest more in the Employment Service and Reemployment Services for claimants. Madam Chair, as you indicated, and as we had an opportunity to talk earlier, states are in the vanguard of an increasingly complex

work force service—public work force service delivery system. The system of Unemployment Insurance and Employment Services that was provided for sixty years ago is no longer a match for today's complex economic circumstances.

My own state, for example, of Utah, is one of a handful of states that is in this vanguard of looking at the comprehensive array of services, and we deal with such diverse issues as Public Assistance, food stamps, in addition to being the administrators of the Employment Security System, Employment Training, and so on.

The hallmark of our system and, increasingly, the system that we see throughout the country, is a system that is built on the need for adequate programs to deal with employment and employability. And certainly, a hallmark of that is adequate funding for the employment service. A recent Department of Labor study found that job search has reduced the average duration in the Unemployment Insurance by one-half to 4 weeks, depending on states. And the government has saved \$2 for every dollar spent in Employment Service activities. It is, frankly, a good investment, and one that we do not believe has been sufficiently attended to in the past several years.

The third point I would like to make is that we obviously believe that there needs to be a reduction in the tax burden, and we need to minimize the tax filing burdens that are currently imposed. ICESA, our organization, does support a repeal of the two-tenths percent Federal unemployment tax for many of the reasons which have been articulated here in previous testimony. We question the accumulation of an \$18 billion reserve in the Federal Unemployment account at a time now when we have moved into a budget surplus. We also would strongly urge the retention of quarterly tax depositing, rather than a monthly system as proposed by the administration.

The fourth point I would make for my testimony is that we also support efforts to reduce fraud and abuse by granting State Unemployment Insurance programs to the National Directory for New Hires. We commend the Congress for the approach that was taken last year although it did not pass. Frankly, over 20 states are currently cross-matching their intrastate new hire data with Unemployment Insurance Claim data, and the number is growing.

In my own State of Utah, we believe that we have cut Unemployment Insurance overpayment by nearly 50 percent as a result of our ability and the consolidation of the services in our agency, and the fact that our Employment Security programs are also housed with the efforts in terms of the Directory itself.

We need the access to this Directory, because new hires in other states, claimants find jobs in other states, and the intrastate new hires sometimes are reported under current statute by multi-state employers to other states. We know a concern that was expressed last year was over the confidentiality and privacy in terms of the sharing of this data. We, too, in the states, are just as concerned about the confidentiality and privacy as are those of you in the Federal Government. Since we are the ones to collect the data in the first place, our rules need to be strict in order to protect privacy and confidentiality.

A fifth point I would make is that we are in favor of repealing the special eligibility requirements on the Extended Benefit program. Again, the EB program has been previously discussed. And finally, I would suggest that our association is unanimous in indicating that we believe that we need to stop the application of the Federal budget principle of budget neutrality to self-financing Unemployment and Employment Service programs. The Unemployment Insurance and Employment Service systems have been under-funded and overtaxed as a result of this principle, and this has been previously testified. During these economic times, now is the time to prepare for the next downturn or the next recession, and correct these principles. As we have previously articulated today, one of the ways that we believe insures this is moving the funding of these programs to the mandatory side of the budget.

[The prepared statement follows:]

Statement of Robert C. Gross, President, Interstate Conference of Employment Security Agencies, and Executive Director, Utah Department of Workforce Services

Madame Chair and Members of the Subcommittee on Human Resources, I am Robert C. Gross, President of the Interstate Conference of Employment Security Agencies (ICESA) and Executive Director of the Utah Department of Workforce Services. Thank you for inviting me to testify today on behalf of ICESA and its 53 state and territorial members. ICESA represents state workforce agencies in general and the Unemployment Insurance (UI) and Employment Service (ES) programs in particular. Many of our state members also administer welfare-to-work programs and some administer other public assistance programs, such as TANF, under the jurisdiction of the Subcommittee on Human Resources.

I want to thank and commend the Chair for scheduling a hearing on UI and ES reform. It is not easy to gain attention for this subject during a time of sustained economic growth and low unemployment, but the system is in need of reform before we experience another economic downturn.

In addition, I want to thank the U.S. Department of Labor for its commitment to working on comprehensive UI and ES reform with business, workers, and states.

During the past year, ICESA has sponsored seven meetings of a UI and ES reform workgroup representing the state and federal partners and business and worker stakeholders. We discussed principles and options, and identified where we agree, where we disagree, and where we hold out the possibility of compromise. Although we have not agreed on a package, my testimony today reflects the substantial progress we have made toward that end. I want to emphasize that I wear multiple hats as I discuss these issues with you. As executive director of the Utah Department of Workforce Services, I have been one of the state administrators who has supported the state-business coalition approach to UI and ES reform as embodied in Mr. McCrery's bill. As a state member of the UI-ES reform workgroup that has labored over the past year, I recognize that our federal partner in this critical safety net system feels very strongly about expanding coverage and eligibility for benefits in any comprehensive reform package. The state members of that workgroup have been clear that worker advocates and business—the principal stakeholders in the system—should agree on components of a comprehensive reform package. Finally, as President of ICESA, I represent 53 state and territorial administrators with whom I must coordinate any official organization position. In this statement I have attempted to be clear on which reform principles we have an official position and on which states have shown interest, or recognize others' interests, but need to discuss further. Most importantly, the state administrators want to work directly with you in addressing UI and ES reform this year.

Administrative Financing Reform

ICESA believes grants to states for the administration of state UI and ES programs have been inadequate. The U.S. Department of Labor has estimated grants for administration of the UI program have been under-funded each year by roughly 10 percent and the purchasing power of grants for administration of the ES program has diminished by around 60 percent since the early 1980s. In response, states have been forced to spend their own funds just to maintain essential services. Preliminary results from a recent ICESA survey show that states spent nearly \$320 million

of their own funds on the administration of the UI and ES programs. About one-third of this sum was spent on UI administration and the remaining two-thirds was allocated to the ES program.

ICESA believes the UI and ES programs must be funded adequately. Members of the UI/ES reform workgroup have concluded this cannot happen as long as the federal government treats grants to states for administration of the UI and ES programs as discretionary federal spending. These grants should be on the mandatory side of the federal budget so that states can receive sufficient funds to administer the UI program in a proper and efficient manner and provide effective reemployment services to unemployed workers. Mr. McCrery's bill takes this approach and is one way to reform administrative funding.

Mr. McCrery's bill would authorize states to collect the Federal Unemployment Tax and retain most of the funds for state spending on administration of the UI and ES programs. Such funds would remain in the federal unemployment trust fund in new separate state administrative accounts, but would be appropriated by states and treated as mandatory federal spending. We don't know whether the Appropriations Committees, Budget Committees, the U.S. Treasury, or the Office of Management and Budget (OMB) would agree to these unprecedented changes, but many states and businesses are supporting this approach.

The states participating in the reform workgroup find another approach, a matching grant, worth exploring also because it is used already for mandatory spending on administration of such programs as child support enforcement and child welfare, both of which are under the jurisdiction of the Subcommittee on Human Resources. In this approach, the Federal government would continue to collect the Federal Unemployment Tax, but about one-fourth of the revenue would be deposited into new state administrative accounts in the unemployment trust fund to finance state matches to federal funds for administration of the UI and ES programs. Although this approach has not been developed fully by the UI/ES reform workgroup, it holds promise because there are precedents in other Human Resources programs for classifying such spending on administration as mandatory.

ICESA does not know which approach best assures adequate funding for UI and ES administration, but it believes states are willing to accept additional responsibility in this system and are willing to be held accountable by the public for results. We would like to work with you and the Administration to achieve this end.

Reemployment

ICESA believes the federal government should invest more funds in the Employment Service and reemployment services because unemployed workers can return to work sooner, save taxpayer dollars, and help employers find qualified workers to produce their goods and services. We commend Mr. McCrery for provisions in his bill establishing new mandatory spending for providing job search and other employment services for UI claimants. The potential return on this investment was summarized in a recent USDOL report entitled, "Evaluation of Worker Profiling and Reemployment Services Policy Workgroup: Final Report and Recommendations."

(1) Individuals receiving job search assistance found new employment one-half to 4 weeks sooner (depending upon the state) than similar individuals who did not receive assistance.

(2) Savings to the government (savings in UI benefit payments plus the increase in tax receipts due to faster reemployment) averaged around \$2 for every \$1 invested in targeted job search assistance.

(3) Individuals receiving job search assistance found jobs with wage rates comparable to those found by individuals who did not receive assistance.

Tax Burden and Tax Filing Burden

ICESA believes the federal government should reduce federal unemployment taxes by repealing the temporary 0.2 percent federal unemployment surtax. The federal government has not only been under funding the administration of UI and ES, but also it has been overtaxing the taxpayers, apparently to fund non-UI and non-ES federal activities. When the federal government extended this tax in 1997, there was little or no need for these additional funds in the UI program. The funds were added to "paper balances" in the Federal Unemployment Account and backed by a promise to make loans to insolvent state programs in future recessions. Even though this account shows these funds as "reserves," the funds were used to finance non-UI/ES spending when the federal budget was running a deficit. Now that the federal budget is running a surplus, these funds are being used for non-UI/ES debt retirement, non-UI/ES tax cuts, or non-UI/ES spending. This practice should stop.

These funds should be used for UI and ES purposes as needed and excess amounts should be returned to the taxpayers.

Many ICESA members are interested in a new idea discussed by the reform workgroup—the possibility of repealing the Federal Unemployment Account and distributing the “reserves” to the state accounts. In an ideal world for states, distributing these “reserves” to state UI accounts could—at individual state’s option—increase the solvency of state UI programs, fund coverage or eligibility expansions, or fund state unemployment tax cuts. Employers, for example, might want these funds to be used for tax cuts. Worker representatives and the Clinton Administration might press for linking the distribution of these funds to potential coverage and eligibility expansions. Such expansions might include lowering state minimum qualifying earnings for claimants, providing benefits to workers who restrict their job search to part-time work, taking into account recent earnings through the use of “alternate base periods,” and providing benefits to claimants who left their jobs to avoid domestic violence. ICESA understands that the Department of Labor might link FUA distributions to such eligibility expansions, but it strongly believes decisions about eligibility for state benefits should be made by states, not the federal government.

ICESA is interested in reducing employer tax filing burden through simplifying tax forms and consolidating wage and tax reporting with states and would not preclude considering such a proposal in a comprehensive reform package.

ICESA strongly supports quarterly (not monthly) tax depositing and commends Mr. McCreery for including this provision in his bill. The Clinton Administration proposal to collect unemployment taxes on a monthly rather than quarterly basis is another bad example of a budget gimmick proposed to finance non-UI/ES expenditures at the expense of the integrity of the system.

ICESA member states are likely to support Internal Revenue Service (IRS) disclosure of information to states for the purpose of combining state and federal employment tax reporting and would not preclude considering such a proposal in a comprehensive reform package. A recent federal law authorized disclosure to the State of Montana for this purpose. Other states are interested in working with IRS on combining employment tax reporting, but they need legislation to proceed.

Fraud and Abuse

ICESA supports reducing fraud and abuse in the UI program by granting state UI programs access to the National Directory of New Hires (NDNH) and commends the House Committee on Ways and Means for including it in the “Fathers Count” bill it reported last year. Individual states already contribute most of the quarterly wage and new hire data in the NDNH, but this national database is not shared with the states. As a result, although states are able to cross match intrastate new hire data with UI claims data, they are not able to run similar cross matches with new hire data from other states. The intrastate cross match enables states to cut overpayments to UI claimants who obtain jobs within their states, but they cannot catch UI claimants who have been reported as new hires in other states. There are nearly one million UI claimants per year nationwide who might be hired in one state while claiming benefits in another state. In addition, there are countless other UI claimants whose intra-state new hires are reported by multi-state employers to other states, a practice explicitly allowed under federal law to lessen employer reporting burden. If the state paying benefits is not promptly informed that such a UI claimant has been newly hired, substantial overpayments occur. These overpayments can be substantially reduced. Utah, for example, was able to cut its average UI overpayment nearly in half by cross matching intra-state new hire data with UI claimant data.

ICESA is aware that the provision granting access to the NDNH was deleted from the “Fathers Count” bill last year because of concerns about privacy and confidentiality. I assure you that states are equally concerned about privacy and confidentiality. In fact, states have strict rules about the wage data and new hire data they submit to the NDNH and are currently working on strict rules for sharing wage data among themselves in the new interstate Wage Record Interchange System (WRIS). We believe states are in a unique position as the source of the NDNH data to protect these data and to use them in an effective manner. Please work with us to grant state UI agencies access to the NDNH. The integrity of the UI program will be enhanced as a result.

Eligibility

In general, ICESA believes states should determine eligibility for state UI programs, not the federal government. However, a comprehensive reform that solves

the problem of inadequate funding, provides additional resources for reemployment services, reduces unemployment tax burden and employer tax filing burden, and combats fraud and abuse, and requires or provides incentives for expanded eligibility, could be attractive to some states.

ICESA believes applicants for Federal Unemployment Compensation, such as benefits for ex-military service personnel or ex-federal employees, should not be required under the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996 to prove their citizenship or qualified alien status in person. ICESA has filed its objections to this policy with the Immigration and Naturalization Service (INS) and is awaiting the final version of its proposed regulations implementing this provision of PRWORA. Because inadequate federal funding for UI and ES administration has forced states to close many local offices and adopt remote claims taking via telephone and the Internet, states no longer can verify citizenship or qualified alien status in-person, which the draft INS regulations seem to require. In addition, since monetarily eligible UI claimants' citizenship or qualified alien status is already supposed to be verified by the employer, we see no reason to duplicate this effort when the worker applies for unemployment benefits.

ICESA supports repeal of special eligibility requirements under the Extended Benefits (EB) program. ICESA believes states should have the authority to set eligibility requirements. In addition, when these requirements differ from state requirements, they impose an added administrative burden on already overburdened states. These requirements include:

- EB claimants must conduct "systematic and sustained" work searches and provide tangible evidence of the work searches.
- EB claimants must accept any offer of suitable work that they can perform.
- EB claimants must have either worked 20 weeks or earned an amount equivalent to either 40 times the weekly benefit amount or 1.5 times the highest quarterly wages in the base period.
- EB claimants who are disqualified for voluntarily leaving, misconduct or for refusing suitable work can receive EB only if they perform work following the disqualification.
- For interstate claims, individuals can only be paid for two weeks of benefits if the state in which they worked is activated on EB and the state where the individual filed his claim is not activated on EB.

ICESA is interested in a proposal to increase the federal share of Extended Benefits from 50 percent to 75 percent and would not preclude considering such a proposal in a comprehensive reform package. Coupled with some reform in the trigger mechanism, such a change might help the federal government avoid the need to enact an emergency federal program during another recession. The last such emergency program in the early 1990s cost the federal government about \$28 billion.

Budget Neutrality

Finally, ICESA strongly objects to the continuing application of the federal budget principle of "budget neutrality" to the self-financing UI and ES system. This has led to the under-funding of administration of UI and ES and over taxing of taxpayers in order to finance other federal spending during deficit years and now the retirement of other federal debt, spending on other federal programs, and cutting of other federal taxes during surplus years. It is time Congress corrected this problem. Our system, and the programs under the jurisdiction of the Subcommittee on Human Resources, should not have to cut services even more and impose even more taxes for a problem that was largely created by the wrongful application of this principle.

Madame Chair, ICESA, its federal partner, and business and worker representatives have done much work in the last year on UI and ES program reform. We are ready to work with you and the Subcommittee to solve these problems this year. Time is short. Let us begin.

Thank you.

Chairman JOHNSON. Thank you very much, Mr. Gross. And I do appreciate your offer to continue working with us and with the administration. It is very helpful that there has been a working group. It is time that the working group realize that we need to bring this to a substantive project.

Mr. Chuck Yarbrough, Chairman, Board of Directors, UWC-Strategic Services on Unemployment and Workers' Compensation. Mr. Yarbrough.

STATEMENT OF CHUCK YARBROUGH, CHAIRMAN, BOARD OF DIRECTORS, UWC-STRATEGIC SERVICES ON UNEMPLOYMENT & WORKERS' COMPENSATION, AND DIVISION PERSONNEL MANAGER, TYSON FOODS, INC., SPRINGDALE, ARIZONA

Mr. YARBROUGH. Thank you, Madam Chairman and Members of the Committee. It seems only natural that we have an opportunity to discuss FUTA on the 29th of February, a day that only comes about in the year ending in double zeroes every 400 years.

I am a Division HR, Human Resource Manager in a 16-state employer with 66,000 employees. I do serve as Chairman of UWC, a group that is dedicated to look at the Workers' Compensation as well as Unemployment Insurance issues. I am a volunteer and a user in the system of Unemployment Insurance, Employment Service, as well as Employment and Training for the past 25 years in doing my job.

With just 5 minutes to impress you about the need for true and effective FUTA reform, I will try to do both, but that is a lot of pressure. Should I spend my time discussing problems of the past or the future? And so I am going to try to do a little bit of both, so here goes. A couple of things on why I believe 3174 is important to us.

My company recently paid \$18,000 to pay the building rent on a Texas Employment Commission office just so that local office could maintain and stay open. This provided East Texas with service where the rural people in Texas were going to have to drive 60 miles to get service. This helped us staff a local plant as well as provide service to that geographical region. We see many veterans lose their representatives out of their local office.

And in Arkansas, we seen the layoff of permanent state employees in a reduction of full-time offices to part-time offices. Since 1980, in Arkansas, my home state, we have experienced across-the-board economic industrial growth with 11-percent growth in population and 1998 Census estimate, a 22-percent growth in the number of men and women in the work force, and a 37-percent growth in the number of employers. But yet, our permanent staffing in the Employment Security Department has been reduced by 50 percent because of the lack of funding.

These reductions, instituted by an employer fund service provider are not based upon any business decision, nor are they based on a technological enhancement, nor are they based upon the decline for the desire of the services. These reductions in personnel and service availability are based upon the fact that the taxes being paid by Arkansas employers are not being returned to the state but, yet, staying in Washington to pad the surplus. These services which taxes are being collected for which the citizens have a great need.

Many states have stopped providing I-nine certification, which puts employers right in the middle of the Immigration Naturalization Service and the Equal Employment Opportunity Commission.

Many employers have had to open up main street recruitment and employment offices even though we are still paying FUTA, and this is another way of us being taxed.

Many work force investment boards are concerned about the money for their one-stops, and unless reform happens, there will be no money. Job seekers are confused on where to go for service. This is a system that is different from any other system. A state agency whose funding comes from a Federal Government, paid by the employers in that state, the budget issues dealing with the dedicated trust fund that is counter-cyclical by nature with discretionary funding by Congress but, yet, is a mandated state system. Therefore, it should be treated differently.

So what will 3174 do? For job seekers in their first because of a labor shortage, it will truly provide a one-stop no wrong door; more employment counselors to provide job matching and better retention and better increased services for the veterans; an effective UI system that will get them their benefits in a timely manner. With proper funding and control, the states could consider providing increased benefits and expanded eligibility for UI for claimants that fits their local state needs.

For the state agency, and they are in the middle because they provide the labor exchange, proper funding would allow a forward thinking approach as to what service are we going to reduce next, deal with local elected officials to help them improve their system, and provide long-range funding for one-stops instead of worrying about what grant they are going to receive. Provide employment services for all Federal work force investment programs into one-stop, which is the future, and still giving the veterans first choice.

For employers, because we are the long-term solution to provide better retention and longer term careers, it improved employment service and a better applicant flow in the time in which the Unemployment rate is at its lowest. Access to state elected officials for proper funding for the one-stop, a reduction of FUTA by 25 percent, a reduction of \$100 million that the IRS collects for tax dollars, collect in the distribution of FUTA. Single payment system collected quarterly, state certified I-9's that would help us in our employment group, and moneys to support the work force investment boards, and refer those veterans who help us fulfill our affirmative action plan requirements. Unemployment Insurance system that seeks to prevent fraud in greater integrity. This is a win-win-win for veteran job seekers, state agencies and employers.

Thanks for your time, and please enact H.R. 3174 for all the right reasons. I would like to say that I have served in Region VI National Employer Council since 1992, an elected representative of employers for the states of Arkansas, Louisiana, New Mexico, Oklahoma and Texas. I have also served on the local PIC. I have also served in a job service advisory council. I am a member of the IAPES, which is the association which the people that work in the system belong to, and I have spent 25 years working inside this system.

Although I am not going to receive a pension, I have received a lot of excellent service from this group of people and they have been tremendously beneficial in allowing me to perform my job. Thank you.

[The prepared statement follows:]

Statement of Chuck Yarbrough, Chairman, Board of Directors, UWC—Strategic Services on Unemployment & Workers' Compensation, and Division Personnel Manager, Tyson Foods, Inc., Springdale, Arizona

Good afternoon, Madam Chairman and members of the committee. My name is Chuck Yarbrough, and I am Division Personnel Manager for Tyson Foods, Inc., the nation's leading producer, processor and marketer of poultry and poultry based food products, as well as other convenience food products.

I am testifying on behalf of UWC—Strategic Services on Unemployment & Workers' Compensation. I am proud to serve as the Chairman of the UWC Board of Directors. UWC, which was founded in 1933, is the only business organization specializing exclusively in public policy advocacy on national unemployment insurance (UI) and workers' compensation issues. UWC is intimately acquainted with UI laws; our research arm, the National Foundation for Unemployment Compensation & Workers' Compensation, publishes numerous materials on UI, including the annual Highlights of State Unemployment Compensation Laws. I have also been a member of the National Employers Council (NEC) since 1992. I served as NEC's elected representative for employers in the Department of Labor's Region VI (Arkansas, Louisiana, New Mexico, Oklahoma, and Texas). In this capacity, I represented employers before the Department of Labor (DOL) and state employment security administrators.

UWC is business leader of the Coalition for Employment Security Financing Reform, an informal coalition of business organizations and states who support H.R. 3174, the Employment Security Financing Reform Act.

H.R. 3174 was introduced by Rep. Jim McCrery with the bipartisan support of 35 co-sponsors. Support for the proposal is growing daily. UWC and the Coalition believe that the swift enactment of H.R. 3174 is essential to strengthen the state unemployment insurance and employment services (UI/ES) system and the workers and employers whom it is designed to serve. Unlike the Administration's proposals, the bipartisan Employment Security Financing Reform Act will improve the method by which FUTA taxes are collected and funds are provided to administer the state UI and ES programs. The Employment Security Financing Reform Act will fix serious problems with the state UI and ES system resulting from the federal government's failure to provide adequate funding and will also provide funds needed to implement the Workforce Investment Act. The Administration's proposals will not achieve these goals.

UWC supports a strong UI/ES program through which employers provide fair and affordable insurance benefits for a temporary period of time to workers with a strong attachment to work who are temporarily and involuntarily jobless when suitable work is no longer available. UWC believes that a sound UI program is best embodied through the state UI/ES system, with a limited federal role where uniformity of state law is considered essential.

Unfortunately, the present system is not working effectively. Workers are underserved, employers are over-taxed, and state UI/ES agencies are under-funded. Under the current system the federal government collects 100% of Federal Unemployment Tax Act (FUTA) receipts but returns only 50% to the states.

Because of the chronic under-funding of UI/ES agencies, workers in the midst of a labor shortage are collecting more weeks of unemployment benefits—at employer expense—and states are reaching into their own general revenues—and employer pockets—by levying add-on taxes to make up for the shortfall in FUTA funds coming back to the states.

The good news is that we have a historic opportunity to enact H.R. 3174 and thereby improve efficiency and streamline the system by fully covering UI/ES administrative costs. This funding is necessary to improve services for jobless workers, reduce taxes on employers, and alleviate the financial pinch on state administrators. Now that's what I'd call a "win-win-win" situation.

In evaluating legislative proposals to improve and simplify UI/ES administrative financing reform, UWC believes there are 3 core ingredients:

1. Eliminate the unnecessary "temporary" 0.2% Federal Unemployment Tax Act (FUTA) surtax on employers which should have expired in 1987 as promised
2. Impose employer taxes to finance the system consistent with sound UI operations rather than inflexible federal budget rules
3. Maintain the FUTA tax at a level that is neither excessive nor inadequate for UI/ES program needs.

These concepts are embodied in H.R. 3174, the Employment Security Financing Act of 1999. Under H.R. 3174, the basic framework of the federal-state UI partner-

ship will remain intact, and all benefits and legal protections for jobless workers will be unchanged. Let me repeat: All worker protections and benefits will remain in place or even be strengthened.

In addition, under H.R. 3174 there will be no change in the rules governing the state unemployment trust accounts used to finance UI benefits. The 0.2% FUTA surtax will expire at the end of this year rather than the year 2007. However, instead of pooling all FUTA payments in a single federal UI/ES administration account (ESAA), FUTA taxes paid by employers in each state will be credited to a new administration account set up for each state. Each state legislature, rather than Congress, will determine how much it needs to administer its UI program. A small amount will be transferred into a special account to be used for additional grants to small states which need additional funds to administer their program, and a small amount will be set aside for U.S. Labor Department operations related to UI. FUTA funds that are not needed for administration—and excess FUTA funds that have already been accumulated—will automatically flow into the state's UI benefits account.

Under H.R. 3174, FUTA and state unemployment taxes will be payable no more often than quarterly, and employers will no longer have to fill out duplicative FUTA and state unemployment tax forms. Instead, states will collect FUTA on the same form used for state unemployment taxes. This approach will simplify tax payment for employers and states, as well as the federal government. It will also increase tax compliance, because states are closer to the situation and in a better position to detect under-payments of FUTA.

Finally, accountability for use of the money will be enhanced by requiring each state agency to report annually to its legislature and the public on services provided to UI claimants.

Some specific advantages of H.R. 3174 are as follows:

- **Better service for UI claimants, jobseekers, veterans and employers.** States will have the necessary resources and flexibility to provide needed services.

- **Funding to serve workers and employers in rural areas.** Cutbacks in FUTA grants have forced states to close offices—this has been an acute problem for workers in rural areas and others who are costly to serve. H.R. 3174 will provide the funds needed to keep these lifelines open.

- **Greater oversight by state and local worker, veterans, and employer groups.** These groups will now have a critically important role in assuring the state UI/ES system delivers needed services effectively and efficiently.

- **More resources for administration of the UI program.** All states will be “winners.” With FUTA funds for states currently getting lost in the federal budget process, all states are being shortchanged.

- **Greater responsiveness to local needs and circumstances.** State legislatures, rather than federal appropriations committees and DOL and Office of Management and Budget (OMB) staff in Washington, D.C., will determine how much is needed to run state UI programs. This will maximize effectiveness by providing greater flexibility—and accountability for state UI/ES agencies. States are responsible for establishing benefit levels and eligibility, salaries of state employees, and other factors that affect the cost of administering the state programs.

- **Provide more resources to prevent and detect UI fraud and abuse.** Improper UI payments are a serious and costly problem, and states will have the resources they need to address them.

- **The elimination of unnecessary paperwork for employers.** Employers will complete and submit a single unemployment tax form rather than two separate state and federal unemployment tax forms.

- **Greater accuracy in the collection of the administrative tax.** Currently enforcement efforts relating to the FUTA are a low priority, but states will be motivated and have the ability to detect errors and delinquencies.

- **Savings to the Federal government.** The cost of having the U.S. Treasury Department collect FUTA taxes will be substantially reduced.

- **Lower net taxes on employers/greater solvency of state UI trust funds.** Currently the federal government keeps half of FUTA taxes paid by employers. If the additional revenue flows into state benefit trust accounts, it will improve the solvency of state UI benefits accounts (a DOL concern). Where funds are not needed for benefits, employers will pay lower state UI taxes, in some cases automatically, and in other cases through reductions in state UI tax rates.

- **Greater employment opportunities.** Because UI taxes are based on payroll, a reduction in employment taxes will make it easier for employers to hire additional workers—such as individuals coming off of welfare rolls.

- **Elimination of the unnecessary 0.2% FUTA surtax.** This payroll tax cut will contribute to employment opportunities by saving employers \$1.5 billion or more a year.

- **Additional savings.** These savings are possible through the release of surpluses in FUTA receipts into state benefit accounts and through the repeal of state tax diversions and add-on taxes on employers, which will no longer be necessary.

- **No reduction in legal rights or unemployment benefits** for workers. However, better service to UI claimants will reduce the duration of UI claims, which has been growing as a result of the squeeze on state UI agencies. An average reduction of as little as one week will save another \$1.5 billion a year for employers by reducing their state unemployment tax. To many of our members, this is the element—along with elimination of the 0.2% FUTA surtax—that offers the greatest promise of future savings and associated job creation opportunities.

- **Funds will be available for states to implement the Workforce Investment Act and operate One-Stop Centers** which deliver UI benefits and coordinate employment services. Without H.R. 3174, there will be no funding for states to deliver the services mandated by DOL.

We recognize that today the UI program is not perceived to be in a “crisis” mode and therefore may not be high on the agenda for immediate action by Congress. However, this is the most propitious time to institute meaningful reforms that can improve service for jobless workers, save money for the federal government, free resources for the states, and reduce the tax burden on employers.

Administration Proposals

The Administration has asked Congress to consider several UI proposals.

As it has done in previous years, the Treasury Department has submitted a budget proposal for FY 2001 which again will require employers to file FUTA and state unemployment taxes *monthly* rather than quarterly. UWC and the Coalition are staunchly opposed to such a requirement. Monthly filing is a budget “gimmick” that will permanently triple the paperwork for employers and state UI agencies, while raising virtually no additional revenue (it would allow some revenue to be “scored” for budget purposes because a relatively small amount of taxes would be received in an earlier fiscal year). Conversely, H.R. 3174 will codify quarterly filing of unemployment taxes.

DOL has asked Congress to enact its “UI Safety Net” proposal, H.R. 1830. The major provisions of H.R. 1830 will (1) provide monetary rewards to states that meet or make progress on new federal standards for state trust fund solvency; (2) provide additional funds for UI/ES administration to states which implement an alternative base period in place of (or in addition to) the “first 4 of the last 5 quarters” test used in most states; and (3) expand eligibility for extended benefits.

We believe H.R. 1830 will take the UI program in the wrong direction and will hurt the workers it is designed to help. H.R. 3174 is a much more flexible, effective and efficient way to improve the UI system.

The problems with H.R. 1830 are as follows:

1. A federal solvency standard for state UI programs is inappropriate

Although UWC encourages states to exercise fiscal responsibility by establishing taxes at the level reasonably needed to fund benefit costs, and we believe that DOL has performed a public service by calling attention to trust fund balances, UWC does not advocate adoption of a federal solvency standard for state unemployment trust accounts, either directly, or indirectly by rewarding states that meet the standard with the release of more FUTA funds. There are simply too many differences among the states for a single federal standard to make sense. UWC is a strong proponent of the present requirement to pay interest on federal loans, which must be levied separate from state unemployment taxes. The existence of the interest requirement provides significant incentive for states to act responsibly. Furthermore, many states may reasonably choose more flexible funding approaches, if their costs are lower through borrowing on the open market rather than relying on interest-bearing federal advances.

The accumulation of large surpluses in periods of economic prosperity can stimulate calls to liberalize benefit eligibility and/or increase benefit levels, which would increase the risk of insolvency. A one-size-fits-all standard fails to take into account triggers under existing state laws, which rapidly and automatically raise additional funds when the balance drops below a given figure; if the trigger is only slightly lower than the minimum funding level DOL recommends, the state is still acting responsibly, but the standard would treat the state as out of compliance. Finally, the DOL proposal would rely on historical experience that may not be indicative of future experience. During the past 20 years, there has been a dramatic change in

the American economy and work place demographics. In many (if not most) states, using old figures that are now obsolete will produce misleading results.

We reiterate our strong conviction that reducing the FUTA rate rather than returning some excess FUTA funds with new strings attached is a more sensible tax policy than the solvency mechanism in H.R. 1830. H.R. 3174, by lowering the FUTA rate and providing making more funds available to state benefits trust accounts, is a more effective approach to improve state solvency.

2. States should be free to determine the base period for establishing UI benefit eligibility

The base period used to determine whether a worker has sufficient wages to qualify for benefits is both a test of attachment to work and a measure of efficiency of administration. Using the first 4 of the last 5 quarters is the more efficient approach, considering resources of state agencies and employers, because this information has already been reported. At one time, many states used the “wage request” method, under which the employer is asked for wage information only when a worker files a claim. However, the federal government mandated submission of quarterly wage reports for all employees—for reasons of efficiency. Now that this costly change has been implemented, employers are opposed to a federal mandate to use both wage request and wage report systems, which is the most inefficient approach. Of course, the limited amount of additional FUTA grants for states with alternative base periods—which we do not believe would be sufficient to offset the cost to states—does nothing to reduce the added burden on employers.

Litigation attempting to interpret the FUTA as somehow requiring states to adopt alternative base periods was initiated in Illinois and California. In 1997, however, Congress enacted legislation expressly amending FUTA to preempt federal courts from misinterpreting the FUTA in this fashion. H.R. 1830 appears to reverse this congressional determination, and we believe it is ill-advised in this respect.

Although UWC opposes a federal mandate for state adoption of alternative base periods, or an inducement in the form of “greenmail” (higher grants for states with alternative base periods), we do not oppose the voluntary adoption of alternative base periods by states. States should continue to be free to consider alternative base periods, as a number have already done. Unlike a unilateral federal mandate, states can consider these proposals as part of a balanced examination of its unemployment insurance statute, taking into account various UI-related concerns of workers, employers, and the state agency.

By making more funds available for state administration of UI and employment services, H.R. 3174 is a more flexible and permanent way to provide administrative resources for those states which choose to use alternative base periods.

3. “Trigger” levels for extended benefits should not be changed

The DOL proposal reflects its concern that the present extended benefits (EB) triggers may be too difficult to satisfy during economic downturns, leading to congressional intervention that is more expensive than a more liberal EB law would have been. We believe further study of EB triggers is warranted, but also observe that Congress has a propensity to mandate supplemental benefits as part of its response to an economic downturn, regardless of EB trigger levels.

DOL and other supporters of benefits expansion cite state UI “reciprocity” rates, i.e., the percentage of all unemployed workers who collect UI benefits to justify extending UI eligibility to individuals with weak attachment to work or who are not involuntarily unemployed because the employer does not have suitable work available. Using the DOL formula, the percentage of all unemployed individuals who now collect UI benefits is lower than at previous times. However, while this information is of interest, it does not justify the conclusion that the UI program is not working as intended.

First, let me say that UI benefit reciprocity should be low during our present prosperous economic conditions. Jobs are plentiful, and in most areas of the country workers who want to work can easily find employment. In today’s economy, workers realize that a new position may be available almost immediately and may not believe it is worth filing for UI benefits for the brief time between jobs.

Furthermore, using the reciprocity rate as a test of whether UI is serving its intended purpose is misleading for several reasons.

1. The reciprocity rate counts as unemployed many people who are not and should not be receiving UI:

- Workers who are disqualified because they voluntarily quit their jobs
- Workers who are disqualified for misconduct or fraud
- UI claimants who have exhausted their benefits
- New entrants or recent reentrants to the labor force

- Workers who do not qualify for UI because they have a weak attachment to work

2. Many eligible UI claimants choose not to file for UI benefits. In many cases, they have been discouraged from filing for benefits because of the closure of state UI/ES offices due to inadequate FUTA funding. Another important factor is the fact that jobs currently are plentiful—many people do not file a claim knowing they can quickly and easily return to work at any time.

3. Statistics on the number of UI claimants and the individuals who are considered in the total unemployment rate use different geographic tests, leading to distortions in computing the reciprocity rate in areas of the country with extensive numbers of workers who live in one state but work in another.

4. Reciprocity rates vary widely from state to state. Some states which use expansive eligibility criteria have low reciprocity.

The federal government must fix the UI/ES problems it has created

Employers, who finance the UI program through federal and state payroll taxes, regard UI as an integral part of the array of the employee benefits they provide. Because employers pay for UI, UI costs are a part of business overhead. UWC believes it is important to keep UI costs as low as possible consistent with its basic goals: prompt return to suitable work by workers with a strong work attachment who lose their jobs through no fault of their own, as the result of action taken by their employer in managing its workforce. By design, UI allows such workers to collect benefits partially replacing wages during short-term unemployment, while they are able to work and are actively seeking suitable full-time employment. How much work constitutes “attachment,” what percentage of lost income is sufficient “partial wage replacement,” how long is “short-term,” what makes unemployment “involuntary,” and which work is “suitable,” are all key issues that bear on the cost of the program to employers. We believe these questions are best resolved by each state under its own UI statute, in light of its own needs and economic circumstances.

During the past 20 years, many American businesses have undergone a basic restructuring to achieve efficiencies necessary for them to be competitive in the global economy. This restructuring, while painful at times, has produced a healthy economy in the United States, including a booming stock market, a budget surplus, and the lowest unemployment rate in more than 25 years. American workers have shared in this prosperity.

UWC supports responsible funding for the UI system and opposes over-taxation. Payroll taxes for UI should be at the minimum level necessary to provide the protections promised, because unnecessary taxes harm corporate competitiveness in the United States. It is especially important for the counter-cyclical UI program to be mindful of this principle, because benefit improvements instituted during periods of low unemployment could create damaging cost increases when the economic cycle turns, as it eventually will.

The greatest problem most employers are experiencing with the UI program—and according to Alan Greenspan, the greatest threat to continued economic growth—is a labor shortage. The tight labor market makes it important to avoid policies that will increase utilization of transfer payments such as UI at a time when employers are having difficulty finding applicants for job openings.

We want to provide some additional specifics about employer concerns with the present federal role in the UI system.

1. FUTA tax rate is too high

Under current law, the Federal Unemployment Tax Act (FUTA) rate is 0.8%. This rate is 25% too high as the result of a 0.2% “temporary” surtax which is no longer needed and which is now being collected only because inclusion of the FUTA surpluses in the unified federal budget allows the federal government to meet budget targets for other spending programs. Federal law expressly limits the use of FUTA funds to UI/ES functions spelled out by statute. The practice of counting FUTA funds for spending on other programs, leaving only an IOU and an accounting entry behind, is contrary to the very reason why Congress placed these funds in the Unemployment Trust Fund in the first place. In effect, the budget rules allow the misuse of FUTA funds for purposes unrelated to the UI/ES system.

Congress originally imposed the surtax in 1976 to pay for a temporary federal program of supplemental benefits for workers who had exhausted the 6 months of regular state UI and the 3 month extension under the permanent Extended Benefits (EB) program. The deficit created by the supplemental program was retired in 1987 but the surtax has been extended until 2007.

Despite the fact that the ceilings on the FUTA accounts in the Unemployment Trust Fund were doubled when the surtax was last extended, balances in these accounts now far exceed their statutory ceilings. When the FUTA accounts are all at

their maximum, as they are today and into the foreseeable future, a law known as the “Reed Act” requires any surplus to be distributed into the state UI benefits accounts. However, instead of making this disbursement, the Reed Act distribution has been limited to \$100 million a year. Consequently FUTA funds are building up despite the statutory ceilings.

Let me make repeat: The revenue from the FUTA surtax is not needed for the UI program. Only 50 cents out of every FUTA dollar is being spent as intended on administration of the UI program and state employment services. Furthermore, no additional accumulation of funds in the account used to pay the 50% federal share of extended benefits (EB) is necessary to meet foreseeable needs, even if EB triggers were lowered as proposed by DOL in H.R. 1830.

Some proponents of an increased federal presence in the state UI system and expansion of state UI benefits and eligibility propose to hold the elimination of the unnecessary FUTA surtax “hostage” to justify new federal mandates or “incentives” for states to expand their UI programs. Similarly, in H.R. 1830 DOL has proposed that new “strings” be tied to the distribution of Reed Act funds by allowing the funds to flow only to states that meet new DOL solvency. DOL has also proposed that additional Reed Act distributions be tied to state expansion of eligibility for benefits. However, it is better unemployment insurance policy and tax policy to lower the FUTA rate and let states continue to determine their own reserve needs and benefits and eligibility standards.

2. State administrative grants are too low for efficient administration

To effectively serve its customers, UI/ES agencies must be efficiently administered. In recent years, this goal has been frustrated because appropriations for state UI agencies have been inadequate, leading to a reduction in claims services for jobless workers that in turn results in indirect state tax increases. This indirect tax comes about because the average claim duration is longer (and thus cost is higher) than necessary. Average claim duration is extraordinarily high for the present period of low unemployment.

Although (as mentioned above) FUTA revenue is legally dedicated to funding the operations of state UI administrative agencies, in practice U.S. budget laws and the appropriations process force state UI administration to compete for funding against other social welfare programs that are funded from general revenues. UWC believes that this process is fatally flawed and that the funding decision for state UI agencies should be handled at the state level. We recommend that each state, rather than Congress, be given authority to control the appropriation of FUTA funds paid by its own employers.

3. Employers are quadruple taxed

Employers pay more than enough in FUTA taxes to provide proper funding for state UI and ES agencies, but because of inadequate flat-line federal administrative grants for state UI/ES agencies we’ve been asked to pay a second, third, and fourth time—quadruple taxation. The inadequate federal grants have directly increased the state tax burden on employers in several ways.

- Many states have been forced to dip into their own general revenues or impose new add-on payroll taxes on employers—above and beyond the state tax used to finance UI benefits—to make up some of the shortfall in FUTA funding from Washington. Most of the additional tax burden directly or indirectly falls on employers.

- In addition to the add-on taxes, basic state UI taxes are inflated because inadequate funding for fraud and abuse and re-employment services results in workers collecting additional weeks of UI benefits. DOL estimates that UI claims on average now last 2 weeks longer than expected in this tight labor market.

- On top of paying higher state taxes, many employers are forced to expend additional resources for employment services we’ve already paid for through FUTA but don’t receive because states have been forced to close offices and eliminate employment counselors and other services. For example, my own company has actually paid the rent to keep the local employment service office open in Carthage, Texas.

Freeing FUTA funds already contributed by employers for the very purpose of providing efficient and effective UI and ES services—as proposed in H.R. 3174—will eliminate the need for supplemental taxes and unnecessary direct expenses.

4. Ineffective work search enforcement and excessive amount of improper payments

The UI system is designed so that claimants generally can collect unemployment benefits only while they are actively seeking work. However, lax enforcement of the work search test continues to be a major weakness of the UI program, resulting in

more costly claims and higher taxes than necessary. We recommend that state agencies be required to be publicly accountable for their use of FUTA funds.

5. Unemployment taxes are too complicated

The present unemployment tax system is needlessly complicated. Although the federal government holds all the money, employers must file two separate federal and state unemployment tax returns. This situation only doubles the paperwork. Moreover, the Internal Revenue Service often pays relatively little attention to small FUTA payments, which causes inaccurate and inconsistent enforcement and is unfair to honest, conscientious taxpayers. We advocate that states collect FUTA on the same form used for filing state unemployment taxes—cutting the paperwork in half, and increasing accuracy.

6. Income tax on UI benefits should be repealed

Although we believe benefits adequacy determinations should be made at the state level, there is one step UWC would support at the federal level that will increase the purchasing power of UI benefits. Under the present federal income tax, amounts received as unemployment benefits are considered taxable income. UI benefits are also taxable as income under state income tax codes that “piggyback” onto federal income tax. However, similar types of benefits that replace involuntary loss of wages—workers’ compensation, for example—are not taxable. UWC believes this hidden tax on UI claimants should be repealed, and we support H.R. 3169, the Unemployment Tax Repeal Act, proposed legislation introduced by Rep. Phil English that eliminates this unwarranted tax.

Conclusion

UWC supports a strong UI system and the concept of a federal-state partnership, under which the UI system has been a general success. However, the present UI/ES system is not working effectively. The federal budget process as now applied to FUTA taxes and UI/ES administrative funding is detrimental to a sound, efficiently administered program. UWC has always advocated that state law be responsible for basic determinations of benefit levels, eligibility, and financing. The federal “partner” now proposes to increase federal involvement in areas traditionally left to the states, leading to higher spending and higher payroll taxes on employers. Considering that federal stewardship of program administration has resulted in over-taxation of employers and under-financing of administrative agencies, we believe that workers, employers, and the public will be better served if instead of an expanded federal presence, states are allowed greater control over FUTA resources contributed by their own employers, as provided in H.R. 3174.

Federal expansion of the UI program, as proposed in H.R. 1830 or other proposals, will take the program in the wrong direction. Expanding the program through relaxed eligibility rules and higher weekly benefits will ultimately weaken the system and hurt those individuals it is designed to protect. The UI system is designed for workers with strong attachment to work who become involuntarily unemployed because their employers no longer have suitable work available for them. Federally mandate or financial incentives for state benefit expansions will dilute the purposes of the UI program. They will also increase federal spending and restore policies that greatly contributed to the bankruptcy of the UI program in the 1970’s and 1980’s in many states. These policies will produce the same result when the economic cycle turns by making the UI program much more costly. Instead of sending more money to Washington, UWC believes that it would far more sensible instead to improve the system and direct funds where they are needed, as provided in H.R. 3174.

I therefore urge that you actively work to enact H.R. 3174 on a bipartisan basis, while opposing the Administration’s proposals. H.R. 3174 is sound public and fiscal policy, and we respectfully urge you to support its speedy enactment.

Chairman JOHNSON. Thank you very much, Mr. Yarbrough. Mr. Smith, David Smith, Director of Public Policy Department, AFL-CIO.

**STATEMENT OF DAVID A. SMITH, DIRECTOR, DEPARTMENT OF
PUBLIC POLICY, AMERICAN FEDERATION OF LABOR AND
CONGRESS OF INDUSTRIAL ORGANIZATIONS**

Mr. SMITH. Madam Chair, thank you. Members of the Committee, I am delighted to be here on behalf of our almost 14 million members. You have my testimony so let me try to briefly focus on a couple of issues.

Chairman JOHNSON. Excuse me. Mr. Smith, do we have your testimony?

Mr. SMITH. You should.

Chairman JOHNSON. Oh, thank you. Okay. Thanks.

Mr. SMITH. It looks like you do, Madam Chair. As the previous panelists have said and as you heard earlier today, we have an enormous opportunity now to take advantage of the expansion, to take advantage of the relatively burgeoning coffers in the system to make some long needed reforms and address the sort of absurdities, Mrs. Johnson, that you talked about, the widely uneven levels of funding, the growing disparity of benefits, and frankly, I think the increasing fragmentation of the system.

Let me emphasize two things and then briefly touch on three or four others that Mr. Yarbrough and others mentioned. This system is out of date in important ways. It is out of sync with the work force. It hasn't changed either to keep up with changing patterns of employment or changes in the employment relationship itself.

First, as more and more women have entered the workforce and their attachment is not so regular. It is interrupted by child-care and other reasons; and as more of us have contingent or part-time relationships to the work force, the sort of assumptions that underlie the structure of benefit provision that assume all of us work full-time for an employer for most of our lives and are only disrupted by cyclical movements in the economy simply don't work. We need to change eligibility rules to reflect those changes in the work force, and the workplace.

You know, in over a dozen states today, less than 25 percent of workers who experience unemployment are eligible for Unemployment benefits. There are a number of suggested eligibility reforms that are talked about in my testimony. Let me mention six of them briefly.

Most importantly, we need to move to an alternative base period that captures the most recent period of employment. That is the single largest cause of the enormous falloff in coverage that I described. We need to lower the earnings threshold to something on the order of 400 times the state's minimum wage. And we ought to increase the taxable base. The FUTA base at the moment, as you know, is only \$7,000. It has been there for almost two decades.

Several people have, and others will, commented on the inequity out current funding. As all of you know well, the best way to address inequity in funding is to broaden the base and lower the rate. But with the base so low, it is very difficult to think about that. As I think Mr. English mentioned, we certainly need to address the extended benefits trigger, and we ought to speak to the issue of taxation of benefits. Mr. Cardin has been very interested in coverage of part-time workers and eliminating the exclusion for those

who wish to continue to seek part-time work. He is absolutely right, we ought to do that.

As both of the previous speakers have said, this is a system that is badly underfunded. But I think we too quickly come to the conclusion that devolution is the answer. First, there are important administrative coherence reasons that Mr. Uhalde talked about, which would suggest that too much devolution will magnify the problems of our currently fragmented system rather than fix them. But I would add another.

Our labor market is no longer only a local labor market or a metropolitan area labor market, it's a national labor market. And the Employment Service system needs to have the same kind of scope and reach that labor markets do in order to adequately address both the Employment Service needs and the Unemployment Compensation administrative needs.

I think I agree with what several of you have said, both my colleagues have said, that the first place to start fixing the administrative funding issue is that we ought to move it from the discretionary to the mandatory side of the budget. There is no reason to continue the current practice. And as we move it, that will obviously require the development of a formula. There are some principles that ought to guide the development of the formula. We ought to hold states harmless against current levels of funding. There should be adequate funding to support both a technological and a personal infrastructure that is appropriate. And we ought to consider building in some flexibility between ES and UI functions.

Three concluding points, Madam Chair. You know, the question of fraud is an interesting one. Now, clearly, none of us are going to come out in favor of fraud, but as I think you know, and as the Department of Labor has testified, the most serious problem facing the system that might be described as fraud is underpayment by employers, not overpayment to employees. We think the resources devoted to going after overpayment as opposed to those that go after underpayment by employers ought to be looked at. We think they are upside down at the moment.

Repeal of FUTA is not the answer. Surely, it should be considered as part of a comprehensive reform as Mr. English mentioned, but it ought not to be considered on its own. We can't, on the one hand, sensibly talk about a system that is badly underfunded and talk about repealing part of its revenue base in a single isolated stroke. In a comprehensive reform package that addresses the issues that we have raised and that others have raised, we certainly ought to think about that. But we ought not to begin with the assumption that the answer to our problems is repeal of FUTA.

Lastly, a comment on the stakeholder process which Mr. Gross has chaired and that many in this room have been involved in. It hasn't reached a conclusion, Madam Chair, that can come to you and your colleagues at the moment, but the effort is moving in that direction. It is one we intend to continue to participate in and we look forward to working with you to bring us all to a conclusion that can address—take the opportunity we now have to address some of these overwhelming problems. Thank you.

[The prepared statement follows:]

**Statement of David A. Smith, Director, Department of Public Policy,
American Federation of Labor and Congress of Industrial Organizations**

Madam Chair, and members of the Human Resources Subcommittee, I would like to take this opportunity to thank you for holding this hearing on the unemployment insurance and employment services system, and for inviting the American Federation of Labor and Congress of Industrial Organizations to testify on behalf of the workers whom these programs were intended to serve. Contrary to the views of others, we believe that now—as the unprecedented economic expansion continues and state trust funds fill with money—is the time to carefully consider and craft reforms to this important system that economically sustains workers during a particularly hard time in their lives and links them to re-employment services, including job training and a job search, and that operates to enhance the economy's capacity to respond to downturns and change. Certainly, the middle of a recession will be too late to make the reforms we will mention in our testimony.

The union movement believes that the unemployment insurance (UI) and employment services (ES) systems are in desperate need of repair and reform. Currently, the UI and ES system is failing to serve its three principle objectives: (1) providing income replacement during periods of unemployment; (2) improving the economy's counter-cyclical capacity; and (3) serving as a gateway to re-employment. We believe that the goals and interest of *all* who have an important stake in the UI system—workers and their representatives, the Department of Labor, states and employers—can be best accomplished with a comprehensive proposal that addresses the concerns of *all* interested parties.

In its 1994 Report and Recommendations, the Advisory Council on Unemployment Compensation stated that the core mission of the UI/ES system is to “serve as the foundation of economic security for millions of workers who are temporarily laid off or permanently lose their jobs.” What is best for the working families the UI program serves and what is best for the economy as a whole are dependent upon each other and lead to an inevitable conclusion about the appropriate course of action: Federal and state unemployment insurance reforms that strengthen program capacity, expand eligibility, and improve benefits for workers. These same considerations counsel against major program changes, such as the devolution of administrative financing, that will further fracture and fragment an already highly decentralized system that already vests extensive authority in the states.

The Unemployment Insurance Program Fails to Meet Needs of Today's Working Families.

The national UI system has fallen into a state of disrepair. It pays too few of the unemployed too little in benefits for too short a time with too little help in finding re-employment. Falling wages, more women in the workforce, declining manufacturing employment, the growth of “contingent” work, and reduced unionization have combined with higher eligibility requirements and tougher penalties to reduce access to benefits for the unemployed. States continue to maintain eligibility standards for UI benefits that are largely based on the concept of a workforce that is comprised mostly of men who are their families' principal breadwinners and who work on a full-time permanent basis in blue collar manufacturing jobs. This conceptualization of the workforce no longer fits:

- Women comprise almost half of the workforce. Sixty-five percent of the mothers of young children are working for pay.
- Over the last decade, “non-standard” or “contingent” work, such as part-time, temporary or contract positions, has accounted for almost one-third of all jobs. These positions are often not the “choice” of workers: many employers only hire on a part-time basis, while other workers are forced to take part-time work to care for a dependent child, or elderly parent.
- The share of workers earning the poverty level or less rose from 24% in 1973 to 29% in 1997.

The failure of the states to change their eligibility rules to reflect the realities of the workplace and work force have resulted in ever increasing numbers of workers being excluded from UI and ES benefits and services. More than a dozen states (Kansas, Florida, Virginia, Utah, Texas, New Mexico, South Dakota, New Hampshire, Colorado, Georgia, Arizona, Louisiana and Oklahoma) pay benefits to 25% or less of their unemployed workers. Of course, unemployed workers who do not receive benefits have already had unemployment insurance taxes withheld from their wages (like any other payroll tax, workers pay by reduced wages; employers simply write the check) and as such, are paying for a social insurance system that does not provide them benefits.

Several UI reforms would address these eligibility problems and, in the process, also make the UI/ES system run in a more fair manner for all parties involved.

Alternative (Movable) Base Periods—States should be required to count the most recent wages of a worker when calculating minimum earning for UI eligibility. Failing to count these wages disqualifies more workers from UI benefits than any other eligibility rule. Six to eight percent of the unemployed would gain access to benefits if states simply counted their most recent earnings.

Lower the Earnings Threshold—The monetary eligibility tests of UI were intended to measure attachment to the labor force. As wages have fallen and work patterns are increasingly irregular, state monetary requirements no longer accurately account for a worker's commitment to work. The Advisory Council on Unemployment Compensation recommended that earnings requirements not exceed 800 times the state's minimum wage. However, even this amount is too high given the growth of low-wage and contingent work. Reducing the earnings threshold further, to an amount equal to 400 times a state's minimum wage, will allow more hardworking, low earning workers to qualify for benefits.

Increase the Taxable Wage Base—The federal taxable wage base has been fixed at \$7,000 since 1983. This low base violates a fundamental principle of equity in generating UI revenue: it regressively taxes a larger portion of payroll for lower wage employers than high wage employers. Raising the taxable wage base will restore progressivity to the system, generate needed resources, and reduce burdens on small employers. Today, 41 states have taxable wage bases that exceed the federal level.

UI Benefits Should not be Subject to Taxation—Currently all UI benefits are taxed as income. This is a cruel tax on individuals suffering economic hardship. As state benefits have declined, unemployment insurance benefits now replace an average of 46% of previous wages. The additional reduction of benefits through taxation reduces the value of benefits for individuals and limits the counter-cyclical impact of the UI system.

The Extended Benefits Trigger Should be Fixed Before the Next Recession—Due to reforms in the 1980s, the current trigger does not accurately reflect labor market difficulties. A lower trigger, tied to the state's total unemployment rate, would be more responsive to recessionary conditions. Special Extended Benefit eligibility requirements, which often mandate an even-greater job search during a recession, should be eliminated.

Coverage of part-time workers—As we previously stated, part-time work is often not a "choice" for the worker. In recognizing both the changing job market and workforce family obligations, searching for part-time work should not disqualify claimants.

Expanding Coverage for Personal Cause Reasons for Separating From Employment—State laws vary in their treatment of personal issues such as quitting work to move with a spouse, domestic violence, child and elder care and part-time work requirements. The union movement supports efforts to expand personal cause exemptions as a valid response to new labor market realities.

Tying Workers to Temporary Help Agencies—In some states, a worker who loses a job which she obtained through a temporary help firm must reapply to that temporary firm or be ruled ineligible. These laws essentially lock unemployed workers into temporary jobs by preventing them from seeking alternative employment. The AFL-CIO opposes this effort to degrade the employment opportunities of the unemployed.

Eliminating Non-Monetary Disqualifications—The use of durational disqualifications—penalties which eliminate eligibility during the entire period of unemployment instead of reducing weeks of eligibility—has expanded to include a wide range of both separation issues and continued eligibility decisions. Re-qualification requirements have also increased, forcing unemployed workers to find jobs and work extensively before regaining eligibility for benefits. Regardless of the cause of separation, at some point in the duration of an unemployment spell, the initial cause of separation is no longer the determining factor in individuals condition of unemployment and that person should be eligible for benefits.

Improvements in Administrative Financing

By all accounts, the UI and ES systems have been badly underfunded in recent years. Insufficient federal funding is leading to harmful state responses. Recent efforts to devolve administrative financing decisions entirely to states, however, in response to this shortfall is a step in the wrong direction, adding greater state authority to a system which already relies too heavily on state discretion. Devolution will result in a less responsive national system as the federal government loses the ability to shift funds among states to match ability to pay and need. A state-based fi-

nancing system will also effectively destroy federal oversight by eliminating the incentive which the rebate of federal taxes provides. Devolution of administrative financing will likely exacerbate competition and the corresponding race to the bottom among states, as it increases states' capacity to use their UI programs as lures to attract business. Finally, the additional fracturing and fragmenting of the federal-state UI program resulting from devolution makes no sense in an economy that increasingly operates nationally and competes internationally.

As states' reaction to the recent economic expansion has shown, devolution will do nothing to address the UI systems' problems for workers, though it very one-sidedly implies that states will use their additional funding to shore up the system for workers. As the economic expansion has resulted in ever-increasing amounts in state trust funds, the end result has not been an expansion of eligibility or an increase in benefit levels. Instead states have fallen all over themselves to provide tax break after tax break to employers. Devolution of administrative financing will add even more fuel to this race to lower employer taxes, resulting in continued downward pressure on benefits.

We believe that the answer to the administrative financing crisis is mandatory reclassification of administrative funding for the Employment Security trust fund using a formula that reflects need. To this end, the AFL-CIO has established principles for guiding formulation of both the budget formulation and an interstate distribution.

- No state should receive less than it currently receives.
- There should be stable funding to support stable infrastructure for both ES and UI, which is not affected by economic fluctuations and which reflects state variations in costs and policies.
- While reflecting actual state needs, the base budget also can and should reflect other policy goals and be supplemented by additional resources to promote certain policy objectives.
- Consider flexibility of funding between ES and UI functions.
- Contingency funding should be continued.

While we continue to search for an effective solution to the administrative financing problem, the AFL-CIO firmly opposes proposals based on the concept of a state match. We have yet to see administrative finance proposal based on a state match that is workable. Under a state match financing system, states determine how much money will be spent on their UI/ES programs, no matter how inadequate. In a climate where the UI system is highly politicized, Governors may attempt to curry favor with business by proposing tax cuts rather than benefit and coverage improvements. Given that the federal government would have no control over the accounts states will use to fund their share of the state match, there is nothing to stop states from taking significant amounts from their general revenue funds to pay for their match, even if these programs are equally important to vulnerable populations. This becomes especially problematic during a recession when additional funds are needed for both UI and other programs.

Handing this type of control to states is tantamount to devolution. Because the state match system leaves little control over state behavior, there is no way to ensure that states will contribute additional funding to their UI/ES systems during a recession. Perhaps worst of all a state match will lead to a "race to the bottom" as states forgo good practices such as keeping UI/ES open, depending less on telephone claims, providing multilingual staff and materials and extending benefits for training. A state match provides a perverse incentive for states to cur investments in administrative reforms that serve workers, while providing tax cuts to employers, leading to further benefit cuts.

Addressing Fraud and Abuse

The AFL-CIO agrees that the UI/ES system should address problems of fraud and abuse, whether perpetrated by recipients or by employers. It is troubling, however, that many in government, especially at the state level, focus largely on overpayments to workers due to error (whether on the part of the worker or the state) as fraud, while showing considerably less concern about underpayments by employers. It is our experience that most recipients who receive overpayments after they have begun work at a new job often do not understand that they are not entitled to the money, and do not understand that states may seek recoupment in the near or distant future.

DOL reports that since the early 1990s, the number of employer audits performed by the state Employment Services agencies declined by 30 percent, indicating that it is increasingly easy for employers to get away with cheating on their UI taxes. As of last year, DOL states underpayment by employers have cost the system far more money than overpayments to workers. Administrative financing reform will

allow states and the federal government to target employers and industries that routinely underpay taxes, and aggressively pursue taxes that are owed the system. The AFL-CIO believes that implementation of employer profiling would target those employers who consistently underpay UI taxes. Employers in certain industries, and those with a high use independent contractors should be the focus of monitoring and collection efforts. Employer profiling will create more equity among employers and can have a positive effect overall on employer tax rates.

Responding to Employer Concerns

For years, many of the most vocal of employer representatives have declared devolution and repeal of .2 percent FUTA surtax as the panacea to their UI problems. In truth, neither proposal really addresses employer's tax and paperwork concerns. Consolidation and piggy-backing of reporting requirements at the federal level (for example, FICA and FUTA) would have the same effect of reducing employer burdens without creating the problems devolution will spawn. Technology advances will greatly alleviate employer paperwork burdens, if only they were fully utilized. The Social Security Administration requires that employers with 100 or more workers file the W-2 forms electronically, and will accept voluntary electronic filings from smaller employers. These types of advances, rather than devolution, will save employers time and money.

The AFL-CIO strongly opposes repeal of the .2% surtax unless it is tied to a package of comprehensive UI/ES reform that includes a solution to the administrative financing issue *and* significantly expands eligibility for workers. Repeal of the surtax without comprehensive reform amounts to taking a significant amount of money out of the system, money that would have been available in the case of an economic downturn, while the problems left unsolved for workers compound. To separate repeal of the surtax from comprehensive UI/ES reform is irresponsible and unnecessary, and will serve only to further fragment the parties involved in the system.

With the understanding that all parties, worker advocates, DOL, state administrators and business have legitimate concerns for a program that is not working, the AFL-CIO participated in good faith for almost a year long effort to craft comprehensive UI/ES reform. Clearly, because we do not have a comprehensive reform package to present to you, the work of the stakeholder group is not finished. However, we do view the efforts as more than a mere exercise, perhaps the only means of fixing a system that all parties admit is badly in need of repair. It is our hope that the work of this group will continue and ultimately culminate in reforms for a system that will truly serve as the financial lifeline to workers who lose their jobs, the bridge to successful re-employment, and a stabilizer for the economy.

In conclusion, we all must face the reality that the good economic times will ultimately end, and in the past, efforts to "fix" the UI/ES system were hurried, leading to decisions that we now know hurt, rather than help the situation of unemployed workers. But worst of all, efforts to "fix" the UI/ES system came far too late for working families seeking assistance during economic hard times. Therefore, it is essential that we reform the UI/ES system while there is time and money, and work to strengthen the program to become the national economic safety net for unemployed workers, and their path to re-employment as it was created to be.

Chairman JOHNSON. Thank you. I do hope that one of the things that will come out of this meeting is that there is some urgency about that. And there are some things that we can do at this time and there are some things we can't do. So maybe we will get better parameters out of this.

Next I would like to recognize Mark Wilson from the Heritage Foundation.

STATEMENT OF MARK WILSON, RESEARCH FELLOW, HERITAGE FOUNDATION

Mr. WILSON. Thank you, Madam Chairwoman, Members of the Committee, for giving me this opportunity to testify before you today. As the 106th Congress begins its debate over the Unemployment Compensation system, I would like to encourage the members

to consider three important principles to ensure that both workers and employers receive the greatest benefit from any reform.

First, we need to reduce the record high tax burden on American jobs. Second, we should consolidate to the greatest extent possible the responsibility for the Unemployment Compensation system to one level of government. And finally, Unemployment Compensation benefits should be paid only to individuals who are involuntarily out of work.

Members of the Committee, the third largest tax increase in the Taxpayer Relief Act of 1997 was an extension of the temporary FUTA surtax that was scheduled to expire at the end of 1998. Ending the FUTA surtax would reduce the overtaxation of American jobs and allow workers and employers to keep nearly \$8 billion more of their hard earned money over the next 5 years to spend and invest as they see fit.

Consolidating responsibility for the UC system at one level of government is important. The taxing and spending authority for the UC system should not be split between the Federal and government states. In 1996, Congress passed Welfare reform that provided states with greater flexibility while holding them accountable for reducing Welfare caseloads.

In 1998, Congress passed the Work force Investment Act that created one-stop career centers and gave states greater responsibility for job training and employment service programs while demanding more effective results. Instead of federalizing Unemployment Insurance benefits, Congress should now do the same for Unemployment Compensation. And a positive step in that direction is H.R. 3174.

It would provide states with sufficient funding to deliver UC services and maintain program integrity. It would reduce the length of unemployment for many unemployed claimants. It would provide a better capacity to provide job search assistance, and the Employment Security system would help more claimants return to work sooner, which is the primary function of the Unemployment Compensation system. It would reduce employer tax and paperwork burdens and would eliminate burdensome Federal mandates that cause inefficiencies and impose increased costs.

When both the UC system and the Social Security program were created in 1935, policymakers knew there would be political pressure to use tax revenue that builds up in the trust funds for other government programs. That is why they placed limits on those funds. Now the Department of Labor is rushing to remove those limits by regulatory fiat. Congress should not allow the President to unilaterally convert the UC program into a huge new government entitlement program unrelated to unemployment.

I would like to talk a little bit about recipient rates. There has been a number of percentages that have been thrown around here, both at the state level and the national level. And I think it is important to remember that when looking at recipient rates, be it a third, be it 40 percent, be it 25 percent, depending on whether it is a national average or a state average, that one use the appropriate denominator when calculating this percentage. It is not total unemployed, it is the number of job losers that is the appropriate denominator. It is important to remember that over half of the peo-

ple who are currently unemployed either quit voluntarily, they recently reentered the labor market, or they are new entrants. They are not job losers. And when one uses the appropriate denominator when calculating this percentage, the recipients rates look far less onerous than they currently—some people would like to have you believe.

Finally, I would like to strongly discourage you from moving UI and the Unemployment Compensation program to the mandatory side of the budget. The last thing we need is to put another program on autopilot here and take it out of the reach of Oversight or more careful, and direct, and thoughtful, and deliberate, of Oversight by Congress. Thank you very much.

[The prepared statement follows:]

Statement of Mark Wilson, Research Fellow, Heritage Foundation

Madam Chairman, Members of the Committee, thank you for the opportunity to testify before you today. The views I express in this testimony are my own and should not be construed as representing any official position of The Heritage Foundation.

As the 106th Congress begins its debate over the Unemployment Compensation (UC) system, members should consider three important principles to ensure that both workers and employers receive the greatest benefit from any reform.

1. Lower the tax burden on American jobs.

The third-largest tax increase in the Taxpayer Relief Act of 1997 was an extension of the temporary Federal Unemployment Tax Act (FUTA) surtax that was scheduled to expire at the end of 1998. The FUTA surtax was extended to December 2007 because many Members thought they needed to increase tax revenues to balance the budget. As a result, the tax burden on American workers has hit a record post-World War II high. Moreover, surplus unemployment taxes continue to be used for purposes totally unrelated to the UC system. Surplus FUTA surtax revenue that builds up in federal trust funds, like the Social Security payroll tax, is converted to federal government bonds and spent as general revenue or used to pay down publicly held debt.

Ending the FUTA surtax would reduce the overtaxation of American jobs and allow workers and employers to keep \$8.3 billion more of their hard-earned money over the next five years to spend or invest as they see fit.

2. Consolidate responsibility for the UC system at one level of government.

The taxing and spending authority for the UC system should be at one level of government and not split between the federal government and the states. Effective program accountability requires the states to be responsible for both raising and spending the revenue to run the UC system. Maintaining bifurcated taxing and spending authorities diminishes direct accountability.

In 1996, Congress passed welfare reform that provided states with greater flexibility while holding them accountable for reducing welfare caseloads. In 1998, Congress passed the Workforce Investment Act that created one-stop career centers and gave the states greater responsibility for job training and employment service programs while demanding more effective results. Congress should now do the same for the unemployment compensation system and a positive step in that direction is contained H.R. 3174 the Employment Security Financing Act of 1999.

H.R. 3174 would:

- Provide states with sufficient funding to deliver UC services and maintain program integrity.
- Reduce the length of unemployment for many unemployment claimants. With better capacity to provide job search assistance, the Employment Security system will help more claimants return to work sooner.
- Reduce employer tax and paperwork burdens. Employers will no longer pay the temporary FUTA surtax and they will only have to deal with one tax collection agency—the state, not the IRS.
- And eliminate burdensome federal mandates that cause inefficiencies and impose increased costs.

3. UC benefits should be paid only to individuals who are involuntarily out of work.

When both UC and Social Security were created in 1935, policymakers knew there would be political pressure to use the tax revenue for other government programs. That is why they placed limits on the use of those funds. Now the Department of Labor is rushing to remove those limits by regulatory fiat. Congress should not allow the President to unilaterally convert the UC program into a huge new government entitlement program unrelated to unemployment. Surplus UC tax revenue should be returned to employers and workers and not used to expand the program to cover family leave. Any new expansion of the program to cover new parents would pit employees who voluntarily choose (and in many instances can afford) to be out of work against workers who involuntarily lose their jobs.

If Congress follows these three principles and recommendations, Members would strengthen and improve the UC system while reducing the record high tax burden on American jobs. Thank you for your time and I will be happy to answer any questions you may have.

Chairman JOHNSON. Mr. Forster, The Honorable Mr. Forster.

STATEMENT OF HON. GAREY FORSTER, SECRETARY, LOUISIANA DEPARTMENT OF LABOR, BATON ROUGE, LOUISIANA

Mr. FORSTER. I am glad to be here today, not only on behalf of the Louisiana Department of Labor, but on behalf of my boss, Governor Mike Foster, who was going to be here, is the Second Vice Chairman of the Southern Governors' Association, introduced the resolution supporting Congressman McCrery's bill. But unfortunately, we are having a few budget problems back in Louisiana and he chose not to come to Washington at this time.

As Congressman McCrery stated, I served for 15 years in the Louisiana House, and that entire time served on the Labor Committee and, in fact, was Chairman when the Governor asked me to take over the Labor Department. So I am very familiar with the issues. And when I arrived at the Department, I saw a different side of what the Department of Labor was about, and that was as a result of its budget being reduced over the last ten to twelve years, \$5 million going from around \$26 million down to \$21 million, and the consumer price index over that time going up about 40 percent. What the state had done is closed ten local offices and consolidated five others. So where we used to be in about 40 plus parishes, out of 64 parishes in Louisiana, we are now down to about half of the parishes. So we have gone from a presence of two-thirds of the state to around half the state.

And why do I raise that issue? Chuck Yarbrough mentioned it, and I don't know if it is as clear to everyone as it is to me. And that is, when you close offices, Members of the Committee, you don't close the big cities. You don't close the office in Shreveport. You don't close New Orleans. You close the little rural offices. And if you are worried about services, and if you are worried about trying to achieve full employment, and if you are worried about somebody who is laid off and has to drive 60-70-80-100 miles to go and file a claim, then you don't do that stupid thing. You don't close those rural offices. And that is what all the states have been forced to do. They are forced to economize. We serve the big cities and we leave the rurals to, basically, to die.

What has happened in Louisiana is we have had to go find funds and work with the employers to try to come up with a temporary solution until, hopefully, the urgency of this Chairman moves this bill to some kind of fruition where we begin to stabilize funding. Let me tell you a little story, quite briefly. My first day on the job, 30 months ago, we had a major garment manufacturer, which as a result of NAFTA, laid off over 4,000 employees. Now, they didn't do this in Lafayette. They did it in St. Martinville, they did it in Abbeville, they did it in Jeanerette, they did it in Port Barre.

Do you know what? We didn't have a labor office in any of those small communities, in any of those small parishes. They had to, at a tough time in their life, drive into Lafayette. Now, the employer worked with us and we sent staff to the plant site to try to help them. But I want you to understand the reality of when something hits, and I would also like you to know that that is not the only layoff in Louisiana. I carry around with me, and have it updated bi-monthly, all the WARN notice layoffs in the state. And they are not all in one city and they are not all in one industry. They are all over the state and those people need help.

And just to give you some idea of it, 230 people in LaPlace getting laid off is a big deal; 130 in Braithwaite, a real big deal; 94 in Jonesville; 138 in St. Martinville; 210 in Narco; 106 in Rayville, 160 in Gramercy; 308 in Tallulah; 177 in Jennings. Those are real live people who congressmen represent who don't have offices around to solve their problems because the staff has been cut and we have been forced to close those offices.

And what I want you to understand is as we try to move in the direction of full employment and the new Work force Investment Act, and all the great things that my buddy, Ray Uhalde, talked about, we didn't get ten extra cents to implement this new legislation. We have to survive with what we have been getting over the last few years with all of the cuts, and try to reach out, reengineer an old system that was built when unemployment was high and not looked at while the economy has changed.

In summary, since I see I am running out of time, let me just tell you that what is important is that Congressman McCrery's bill, I believe, does have a comprehensive look at why FUTA was implemented at a time of high unemployment and hasn't been reengineered. Somebody is doing something, finally, about that in a major way. And it looks at, I think, the changes in the economy and the workplace. Employers, as well as unemployed and underemployed individuals, demand different services from the system than was thought at the inception of FUTA legislation.

Therefore, my Governor, Mike Foster, and the Southern Governors' Association support the bipartisan bill that Congressman McCrery has introduced, which among other things, repeals the temporary FUTA surtax, transfers the collection of FUTA tax to the states, ensures that states get a greater return on their employers' FUTA tax dollars, improves Employment Services, combats fraud and abuse in the system, and increases state flexibility to administer the Unemployment Insurance and Employment Services program at a time we desperately need it.

I implore the Committee to act as soon as possible to begin to change a system that I think is broke. And it needs fixing, and it needs fixing immediately. Thank you very much.

[The prepared statement follows:]

Statement of Hon. Garey Forster, Secretary, Louisiana Department of Labor, Baton Rouge, Louisiana

Good afternoon, Chairman Johnson and members of the Subcommittee on Human Resources of the Committee on Ways and Means. I am Garey Forster, Secretary of Labor for the Louisiana Department of Labor, appearing on behalf of the Honorable M. J. "Mike" Foster, Governor of the state of Louisiana and Second Vice Chairman of the Southern Governors' Association. For the 15 years prior to my appointment as Secretary, I served as a member of the Louisiana House of Representatives and worked in the private sector. During my entire tenure as a legislator, I served on the House Committee on Labor and Industrial Relations, serving as chairman for the two years immediately preceding my appointment. I was the floor leader for the business community and the Republican Administrations on legislation regarding unemployment insurance, workers' compensation, and job training reform. As a result, I bring to you years of experience on unemployment insurance and employment services from the viewpoint of a private sector businessman, a legislative policy-maker, and now as an administrator of the program. I am very familiar with the administrative funding problems of the programs, and I look forward to upcoming discussions on reforming the present system.

When I arrived at the Louisiana Department of Labor approximately 30 months ago, in August of 1997, the department was near the breaking point resulting from many years of under-funding. From Fiscal Year 1988 to FY 2000, administrative funding for the Louisiana Department of Labor actually decreased by \$5 million, from \$26 million to \$21 million. At the same time that administrative funding was decreasing, the cost to the Department to provide the mandated services was increasing. As a result of the decreased funding, the department was forced to close ten local offices, and five other offices were consolidated into two offices. The greatest impact of these closures and consolidations was felt in the rural areas. Unfortunately, it is the rural areas of a state which usually have the highest rates of unemployment and house residents who need the most intensive services to move into employment. These closures were based on the fact that it is more expensive, or less cost effective, to maintain an office in a rural area since such offices serve fewer customers on a daily basis.

On my first day on the job as Secretary, I was confronted with the initial phase of a major layoff by a garment manufacturer in our state. The layoff affected approximately 4,000 individuals at four facilities in four rural parishes, only one of which had a local office. This experience exposed me to the particular challenges presented to a local economy by a major layoff in a rural area. Since transportation is a significant issue in the rural areas, it is especially important to deliver services in the immediate vicinity. It is critical for the Department to be in a position to respond timely and effectively to provide services to both employees and businesses in order to mitigate and address the devastating effect a major layoff can have on a rural economy.

The legislation proposed to reform the administrative funding portion of the Federal Unemployment Tax Act will alleviate many of the budget shortfalls experienced by state labor departments in the past. Reform proposals introduced by Congressman Jim McCrery and Senator DeWine along with numerous co-sponsors represent a collaborative effort of many persons with a stake in the system. These proposals could provide resolutions to many problems currently faced by states. It has long been recognized that the level of funding provided to the states to administer the unemployment insurance and employment services programs is inadequate. Since 1976, employers have paid a surtax that was originally designated as a temporary tax to fund a deficit in the employment security system. This deficit has been extinguished, but the surtax remains as a burden on employers. In addition, employers have paid substantial amounts of employment taxes to the federal government. Over time, less and less of these federal taxes have been returned to the states for administering state unemployment taxes and claims and employment services.

Declining funding has resulted in inefficiencies in the system and the inability of customers to receive adequate services. With the national unemployment rate at the lowest level that it has been in 30 years, labor departments are more likely to see customers with multiple barriers to employment. Typically, these individuals are harder and more expensive to serve and require a more personal and "hands-on" approach. More personal interaction means that agency workers spend more time

with each customer and will ultimately require additional resources to provide an adequate level of service. We all recognize that the days when offices were fully staffed are gone and will never return. As new and innovative programs are implemented with specific mandates on the provision of employment services, such as the Workforce Investment Act, additional resources become more critical. The work processes of state labor department programs must be reengineered to meet these new demands. Yet, the state's already under-funded system did not receive any additional resources to accomplish this.

In conclusion, FUTA was implemented at a time of high unemployment and has not been reengineered in many years to adapt to changes in the economy and the workplace. Employers, as well as unemployed and underemployed individuals, demand different services from the system than was thought of at the inception of the FUTA legislation. Therefore, my governor, Governor Foster, and the Southern Governors Association support FUTA reform which, among other things: (1) repeals the temporary FUTA surtax; (2) transfers collection of the FUTA tax to the states; (3) ensures that states get a greater return on their employers' FUTA tax dollars; (4) improves employment services; (5) combats fraud and abuse in the system; and (6) increases state flexibility to administer the unemployment insurance and employment services programs.

This concludes my comments, Chairman Johnson and members of the Subcommittee; however, I would be pleased to answer any questions that you may have. I would like my oral and written comments to be made a part of the official record for today's hearing.

Chairman JOHNSON. Thank you very much. Now, to conclude then, Van Doorn Ooms, Senior Vice President and Director of Research, Committee of Economic Development. Thank you, Mr. Ooms.

**STATEMENT OF VAN DOORN OOMS, SENIOR VICE PRESIDENT
AND DIRECTOR OF RESEARCH, COMMITTEE FOR ECONOMIC
DEVELOPMENT**

Mr. OOMS. Thank you, Madam Chairman. I am honored to accept your invitation to testify on behalf of CED on Unemployment Insurance.

CED is a nonprofit, nonpartisan, nonpolitical research and policy organization of over 200 business and education leaders. Its purpose is to recommend policies to promote economic growth, higher living standards and equal opportunity for all Americans. CED's policy positions are adopted by a vote of the 62 members of its Research and Policy Committee, who speak in their individual capacities.

My testimony is going to be fairly narrowly focused, because CED has not addressed directly a number of the Unemployment Compensation reform proposals before you today and, therefore, does not have an official policy position on them. However, CED has considered and made recommendations on certain aspects of the UI system, and in particular, the extent to which it covers the American work force, and that is the issue I wish to address in this testimony.

In summary, CED's view is that a number of longer term trends and recent developments in the American economy have significantly changed the nature of the American work force and the nature of employment, as you noted earlier, Madam Chairman. As is well known, one of the major results of this change is that the proportion of unemployed workers that receives Unemployment Com-

pensation has fallen sharply, from roughly one-half of the fifties to about one-third recently.

CED believes that the fundamental purposes of Unemployment Compensation and the national economy would be served better by somewhat broader UI eligibility and coverage. Consequently, CED has supported several proposals to broaden eligibility among certain low-wage, part-time and seasonal workers that were made by the Advisory Council on Unemployment Compensation 4 years ago.

The Committee, I am sure, is familiar with the Council's report, so I will not describe its recommendations in detail, but there are four, essentially. Two of them would remove categorical prohibitions against eligibility—one with respect to part-time workers, which Mr. Cardin mentioned earlier, and one with respect to seasonal workers. To deal with the issue of lower wage workers, CED believes that the earnings requirement should be set at levels that better reflect the attachment to the workforce of many low-wage workers that work many hours but, nevertheless, have relatively small earnings.

Finally, we also believe that there should be an adjustment of the base period where that is appropriate and necessary to create the eligibility of workers who would be eligible if their more recent earnings records were taken into account in the calculation.

The reason for our position on these, Madam Chairman, has to do with the profound changes in the economy over the last few years that have made our UI system, which was created in a very different world somewhat obsolete. Let me just note those changes very briefly.

First of all, rapid technological change. In the process of creative destruction, as new sectors, firms, and workers advance, others decline. Downsizing and growth now often go hand-in-hand. The transfer of resources required for this process is not instantaneous and it is not smooth. And the larger the resource transfers required, the larger the likely temporary unemployment and the demands on the UI system.

There is evidence, although it is still preliminary, that productivity growth is now accelerating and has been over the last several years. At the moment, of course, the extraordinarily strong demand for labor and the very tight labor market masks the amount of resource transfer that is going on. We don't observe what will happen when the labor market slackens, which will be higher temporary unemployment.

The organization of work has also changed, and a major result of those changes has been an increase in the importance of temporary part-time and other irregular employment arrangements, many of which are not covered under the current UI system. In part, technological change has meant that skill requirements have increased; as a result, the skill bias in the system has widened the gap between the earnings of highly skilled workers and less skilled workers. That means that earnings have become a less reliable index of labor force attachment, and we believe that needs to be taken into account in addressing adequacy of the system.

Globalization is another important aspect of change. Like technological change, globalization results both in great benefits for the society as a whole and substantial adjustment costs. We believe

that to address the concerns about globalization that were revealed most dramatically in Seattle, we need to have safety net mechanisms that are seen as equitably sharing those adjustment costs.

Finally, as you noted yourself, Madam Chairman, there are two other major things that are going on at the present time. One, the composition of the labor force has changed dramatically over many years and is about to change even more dramatically as the baby-boomers reach retirement age. When that happens, either for reasons of preference or reasons of requirement, many older workers will remain employed past the ordinary retirement age. There is no doubt that part-time, short-term and seasonal work arrangements will become more important in that world.

Finally, on the subject of welfare reform, with which the Subcommittee is also concerned, we are now engaged in a major experiment in this country with respect to the integration of several million low-income and typically low-skill single parents into the mainstream of American life. The success of that experiment is going to depend to a very large extent on whether, when the economy slackens, those workers are forced back into some kind of dependency or remain as part of the American workforce. Some of the reforms that have been mentioned today that would address part-time and low-wage work would make it more likely that that very important experiment succeed. Thank you, Madam Chairman.

[The prepared statement follows:]

Statement of Van Doorn Ooms, Senior Vice President and Director of Research, Committee for Economic Development

Madam Chairman and Members of the Committee:

My name is Van Doorn Ooms and I am the Senior Vice President and Director of Research of the Committee for Economic Development (CED).¹ I am honored to accept your invitation to testify on behalf of CED on the Unemployment Insurance system (UI). Before joining CED in 1991, I served as the Chief Economist for the Senate Budget Committee, the Office of Management and Budget, and the House Budget Committee. My curriculum vita is attached, as requested in your letter of invitation.

CED is a nonprofit, nonpartisan, and nonpolitical research and policy organization of over 200 business and education leaders. Its purpose, pursued throughout its 58-year history, is to recommend policies to promote economic growth, higher living standards, and equal opportunity for all Americans. CED's policy positions are adopted by a vote of the 62 members of its Research and Policy Committee, who speak in their individual capacities.

In line with these concerns about national economic growth and equal opportunity, CED produced a number of policy statements during the 1980s and 1990s recommending measures to improve the functioning of our labor markets and to extend the opportunities for all workers to participate in the nation's growth and prosperity: *Work and Change: Labor Market Adjustment Policies in a Competitive World* (1987); *An America That Works: The Life-Cycle Approach to a Competitive Work Force* (1990); *American Workers and Economic Change* (1996); *New Opportunities for Older Workers* (1999); and the recently released *Welfare Reform and Beyond: Making Work Work* (2000).

CED has not addressed directly some of the unemployment compensation reform proposals before you today and therefore does not have an official policy position on them. However, CED has considered and made recommendations on certain aspects of the UI system, and in particular the extent to which it covers the American workforce. I will address that issue in this testimony.

In summary, CED's view is that a number of longer-term trends and recent developments in the American economy have significantly changed the nature of the American workforce and employment. As is well known, one important result of

¹ CED has a long-standing policy of neither seeking nor accepting Federal government grants or contracts, and neither CED nor I personally have received any such grants or contracts during the current or preceding two fiscal years.

these changes is that the proportion of unemployed workers that receives unemployment compensation has fallen sharply, from roughly one-half in the 1950s to about one-third recently. CED believes that the fundamental purposes of unemployment compensation, and the national economy, would be better served by somewhat broader UI eligibility. Consequently, CED has supported the proposals to broaden eligibility among certain low-wage, part-time, and seasonal workers made by the Advisory Council on Unemployment Compensation in 1996.

Functions of Unemployment Compensation

CED believes there are at least three major functions to be served by a well-functioning UI system. It should:

1. provide temporary, partial wage replacement for involuntarily unemployed workers who are significantly attached to the labor force and actively seeking work;
2. facilitate the dynamic economic change on which our higher living standards depend by shifting some of the costs of adjusting to that change to the larger society; and
3. help to stabilize the national economy by supporting consumer purchasing power when unemployment rises.

Economic Changes Affecting the UI System

A number of major changes in the American economy have affected, or soon will affect, the effectiveness with which the UI system performs these functions. Some of these changes have been ongoing for decades, while others await us in the future, but all have important implications for unemployment compensation.

Technological change New knowledge and its applications are the major source of growth in our productivity, incomes, and living standards. Productivity growth has accelerated in the last 4–5 years, driven both by rapid technical change in information technology and the investment boom associated with it. But while the benefits of technological change are large, they carry with them the costs of adjusting to that change. In the process of “creative destruction,” as new sectors, firms, and workers advance, others decline. “Downsizing” and growth now often go hand-in-hand. The transfer of resources, including labor, required for this process is neither instantaneous nor smooth; the larger the resource transfers required, the larger the likely temporary unemployment and demands on the UI system. These effects, of course, remain in abeyance during periods of very strong labor demand such as the present, but are likely to appear when demand again slackens.

The organization of work Both rapid technical change and the increasingly competitive structure of the U.S. economy have brought major changes to the operations of American business and the workplace. New structures of production, decentralized operations, new relationships with suppliers, and increased flexibility have characterized the last two decades in particular. A major result of these changes has been an increase in the importance of temporary, part-time, and other “irregular” employment arrangements. Our UI system, of course, was designed with a more traditional model of employment arrangements in mind, and does not always cover such workers when unemployed.

Skill requirements and earnings During the last several decades, the changes described above have increased the demand for highly skilled workers relative to those with fewer skills. This “skill bias” has produced a sharp increase in the wage premium paid for skills and in the earnings differentials between high- and low-wage workers. Indeed, the real earnings of low-wage male workers declined absolutely and substantially until very recently. As a result, earnings *per se* have become less reliable indicators of employment and labor force attachment. The UI system, of course, bases benefits eligibility primarily on an earnings history. Given the large population of low-wage workers potentially affected, a reexamination of the minimum earnings required for UI eligibility may be warranted.

Globalization Like technical change, the expansion of international trade, investment, and immigration has produced both large overall economic benefits and significant adjustment costs that impact particular industries, workers, and communities. While some of the reactions against globalization recently displayed in Seattle reflect misunderstanding and misplaced apprehension, those concerns must be addressed if further progress is to be made in trade and investment liberalization. This will require safety-net mechanisms that equitably share adjustment costs. Trade-specific mechanisms appear less promising in this respect than a UI system with broad coverage that addresses economic adjustment generally.

Composition of the labor force In the last half-century, female participation in the labor force has nearly doubled (from 34 percent in 1950 to 60 percent today) and the need for more flexible and “family friendly” work arrangements has become apparent to many, if not most, employers. A new set of changes lies just ahead, as

the baby-boomers age and their preferences or circumstances lead many of them to continue to work past the traditional retirement age.² While new models of employment suited to both older workers and employers will certainly evolve, there can be little doubt that part-time, short-term, and seasonal work arrangements will become more important than at present, and that our social insurance systems will have to adapt to such change.

Welfare reform The U.S. is now engaged in a major economic, social, and cultural experiment that attempts to integrate several million low-income and typically low-skill single parents into mainstream American economic life. Although welfare reform, aided by an extraordinarily tight labor market, has been more successful to date than many observers expected, the experiment is far from over.³ Its ultimate success will hinge on whether welfare-leavers can be incorporated into the labor force on a permanent basis, rather than falling back into dependency of one kind or another. An important test of this will come when the labor market softens. A large proportion of these workers are in part-time, temporary, or short-term jobs that are categorically excluded from UI coverage in some states or in jobs with earnings too low to meet UI eligibility requirements. It is estimated that no more than 20 percent of persons leaving welfare for work are likely to become eligible for UI through their post-welfare employment.⁴

Recommendations

As a result of these considerations, CED supports four key recommendations of the Advisory Council on Unemployment Compensation that would extend UI eligibility to more low-wage, part-time, and seasonal workers with significant labor force attachment. A number of states already have policies that accord with some or all of these recommendations, but CED urges those that do not to adopt such policies.

The first two of these recommendations would remove the *categorical* exclusion of part-time and seasonal workers who would otherwise be eligible. Some states categorically exclude workers applying for part-time work even though they have met the state's monetary eligibility requirements. Fifteen states permit workers in seasonal industries to collect benefits only during the season in which that industry is active, and thirteen states do not allow seasonal earnings to count towards the earnings requirement even if the worker later works in a non-seasonal job.

- **States should eliminate seasonal exclusions; claimants who have worked in seasonal jobs should be subject to the same eligibility requirements as all other unemployed workers.**

- **Workers who meet a state's monetary eligibility requirements should not be precluded from receiving UI benefits merely because they are seeking part-time, rather than full-time, employment.**

The third recommendation would reduce the number of workers made ineligible by low wages. The base period and "high quarter" minimum earnings requirements in 9 states would exclude workers who worked two days per week for a full year (about 800 hours) at the minimum wage, whereas workers earning \$8.00 per hour for the same employment would be eligible in all states but one.

- **States should set their earnings requirements so that a worker with 800 hours of work, evenly distributed over the year, at the state's minimum hourly wage would be monetarily eligible for benefits**

Finally, a fourth recommendation would reduce the number of workers made ineligible merely because their last completed quarter of earnings was not used in the calculation of monetary eligibility. Many states compute workers' monetary eligibility on the basis of their earnings during the first four of the last five completed quarters of work, a practice once required by pre-computer technology. Some states now use a "moveable base period" to allow the most recent four quarters to be used as an alternative.

- **States should use a moveable base period in cases in which its use would qualify a UI claimant to meet the state's monetary eligibility requirements.**

CED recognizes, in making these recommendations, that the payroll taxes that finance UI are a tax on labor services that may have a negative impact on employment, especially at low-wage levels. It would be counterproductive to discourage the employment of low-wage workers at the same time that we attempt to facilitate both their labor force participation and their employment by extending UI benefits to

²See CED, *New Opportunities for Older Workers* (1999), Chapter 1.

³CED, *Welfare Reform and Beyond: Making Work Work* (2000), Chapter 2.

⁴See Wayne Vroman, *Effects of Welfare Reform on Unemployment Insurance*, (The Urban Institute, 1998) p. 2

them. In addition, there is evidence that, in the longer term, a substantial portion of such taxes is borne by workers themselves in the form of lower wages.

CED therefore also recommends that the federal and state governments consider ways to support broader eligibility for benefits with general revenues rather than higher UI payroll taxes. Some degree of general revenue financing would also seem to be indicated by the fact that the benefit extensions would serve several broad social goals, such as the facilitation of change and the success of welfare reform, in addition to meeting the needs of individual firms and workers. One possible approach would be to credit the UI trust fund with income taxes paid on UI benefits, as is done with the Social Security and Railroad Retirement trust funds. This arrangement would generate at least \$3.6 billion annually for the UI trust fund, which would more than cover the estimated \$2.0 billion dollar cost of the four recommendations.

CED believes that the implementation of these recommendations in all the states would substantially improve the effectiveness of the Nation's unemployment compensation system in performing its essential economic and social functions.

Chairman JOHNSON. Thank you all very much for your testimony. I am going to start with Mr. English. Unfortunately, the Ways and Means Committee does have a meeting a little later today, and we have been asked to conclude by 4. Whether we will be able to do exactly that, I don't know, but it does shorten our question period. Mr. English.

Mr. ENGLISH. And Madam Chairman, I appreciate the opportunity to question perhaps the best and most stimulating panel I have heard on this subject in a long time. I note that Mr. Smith and Mr. Yarbrough come at this issue from rather different philosophical perspectives, but both of you have concluded on one of my favorite topics, that there should be no Federal taxation of Unemployment Compensation benefits. Would the two of you like to very quickly elaborate on that?

Mr. YARBROUGH. Go ahead, sir.

Mr. SMITH. Let me do it very briefly, Mr. English. Folks aren't getting Unemployment benefits because they are living high off the hog. They have lost a job, it is an enormously difficult time. Not only has eligibility for Unemployment Compensation decreased, but the replacement value of the check has decreased. This is one way to stretch those resources further at a time of difficult adjustment for a lot of the reasons that my friend from CED talked about.

So I think you were right when you said earlier this is a tax cut that even some of us unexpected taxcutters could support, although, we might set some limits on it.

Mr. ENGLISH. Thank you. Mr. Yarbrough.

Mr. YARBROUGH. Thank you, Mr. English. Yes, I think that the employer community feels like that the taxation of the UI benefits diminishes the benefits in which we are paying for. You know, it is—and when people get reemployed and they get the services and they come back, and then it rolls around again in taxation time, they are having to spend more of their additional income that they are trying to get back on their feet and recover, you know, back to pay more taxes.

Mr. ENGLISH. Mr. Yarbrough, on a couple of other points, I am curious. You come out very strongly against establishing a Federal solvency standard on the theory that there is substantial differences among the states. Do you feel those differences are so dif-

difficult to quantify that we can't establish at least some Federal standard that establishes a clear bench mark so we don't see the states reverting to the situation that we had back in the 'seventies and' eighties?

Mr. YARBROUGH. Well, I think when it comes to, you know, solvency issues, you know, and how each state, and whether or not there should be a standard—let me also, I guess, look at something that has just recently been passed, which is our Work force Investment Act. And we have given that down to the local level and given the local people the opportunity to decide how they are going to do what they are going to do, when they are going to do this. And it involved the employer community as well as the state agencies to do this. So you know, anything along those lines, I think, that forces it down and gives the states the opportunity.

I am not necessarily—feel like different states probably need different solvency levels just as they have different requirements. You have some states that are benefit receivers because they pay less than what they return. So you know, does that change their solvency ratio any different than someone who in the region that I serve in the National Employer Council who receive an average of about 46 cents? So you know, I think there is still a lot of variety that is—

Mr. ENGLISH. I think you make a very good point, that there is a lot of variety. It just seems to me that solvency is something that is a little more easy to quantify than some other things in public policy. And there ought to be some sort of a Federal standard if there are going to be Federal tax dollars.

Mr. YARBROUGH. Let me say that if you return these dollars back to the states and give them the opportunity to have, you know, like control that money and provide local service and things like that, that adds a lot of solvency back to their general treasuries.

Mr. ENGLISH. The point is well taken. Mr. Wilson, should states raise taxes during a recession?

Mr. WILSON. No, of course not. They should try to maintain as low a tax rate as possible. And when it comes to—I would like to mention a few things about solvency.

Mr. ENGLISH. Could I go—

Mr. WILSON. Sure, go ahead.

Mr. ENGLISH. I appreciate it. But isn't the implication—you have testified that, essentially, we should consolidate Unemployment Compensation within one level of government, the state government, and that the McCrery proposal is a—what you view as a useful transition to that. May I ask, isn't the implication of that, that states, individual states that might have a protracted recession, would be more or less on their own under the system you envision? And wouldn't they be required to dramatically increase taxes if they don't have an adequate solvency in their system, and they don't have Federal standards, and they face a severe protracted recession?

Mr. WILSON. The H.R. 3174 allows and enables the states to borrow from the Federal Government.

Mr. ENGLISH. That is true.

Mr. WILSON. And currently—or for that matter, they have the ability now to go to the private sector and borrow funds in the private sector—

Mr. ENGLISH. That is true.

Mr. WILSON.—and they should if their solvency levels—the point I would like to make about solvency is there is no money in the trust funds. These are bonds. These are government bonds like Social Security in the trust funds. The Federal Government is going to have to borrow that money. So what difference is it whether the state borrows it from the private sector, or that the state borrows it from the Federal Government, or when the Federal Government turns around and has to borrow it from the public sector again?

Somebody is going to have to borrow the money somewhere in order to prevent taxes from rising during a recession because neither the states nor the Federal Government are going to do that, nor should they. So somebody is going to have to get the money from somewhere. It is going to be borrowed somewhere, whether it is borrowed at the state level, either in private markets or from the Federal Government, as H.R. 3174 allows or whether the Federal Government turns around and does it. It is just six of one or half-dozen of the other.

Mr. ENGLISH. It is very possible though. My time has expired, but it is very possible for a state or a region to experience a recession at a time when the Federal Government and the nation as a whole is maybe doing rather better. You look at the recent experience of Hawaii. I yield back my time. Thank you.

Chairman JOHNSON. Thank you. Mr. Cardin.

Mr. CARDIN.—the major difference here, when the Federal Government borrows the money, it need not raise taxes to pay it back. That is one of the aspects of the Federal budget system, it has the capacity to respond to economic conditions and put more money into the economy or less money into the economy. The states aren't quite as—have the same flexibility. If they don't have enough money in their Unemployment Insurance fund, yes, they can borrow it from the Federal Government, but they will be required to raise taxes in order to repay that money to the Federal Government, and that is how the current system operates.

So Mr. Yarbrough, I am somewhat puzzled by your position that we shouldn't have national solvency standards. We have two of the large states right now, California and Texas, that have, I think, about 25 percent of what the recommended levels are. And if we were to let that—and then when we go through a recession, then we are going to be encouraging states raising taxes during a recessionary period in order to deal with our Unemployment Insurance needs, and that seems to me to be counter-intuitive. So I don't quite understand your position of allowing a system to evolve that could very well encourage raising taxes during recessionary times.

Mr. YARBROUGH. I believe the two-tenths was added during recessionary times. Is that not a true statement?

Mr. CARDIN. It was—I don't know the exact year—

Mr. YARBROUGH. I mean, you know, you are answering your own question from the standpoint that the two-tenths was added during recessionary time.

Mr. CARDIN. But the Federal Government has the opportunity to make that judgement as to whether it needs the revenue. But it can—the Federal Government is fully capable of responding to a recession by pouring more money into an economy. It can do that if it wishes to, and it has done that in the past, and it has incurred more debt in doing that. The states can't do that.

Mr. WILSON. But it has to pay off that with interest at some point in time.

Mr. YARBROUGH. Absolutely. I mean, the Federal Government, yes, maybe—there is no legal requirement. I mean, right now it is politically fashionable to speak about retiring the entire Federal debt. And based upon the strength of our current economy, there are economists who say that may well be the right thing to do. But if you talk to economists, they will quickly point out that debt is useful to our economy at different times. The states, on the other hand, have to run a much more balanced operation.

I guess the point I am bringing up is if you believe in Unemployment Insurance and you believe that the Federal Government should develop a system that makes sure that during recessionary times there is adequate income to people who through no fault of their own have lost their jobs, then I am somewhat puzzled by why you do not believe there should be an adequate standard, national standard, to make sure that there is adequate resources at the state level to deal with this.

And employers continue to be somewhat puzzled about why there is not proper funding for the Employment Service and the UI whenever the trust funds are at an all time high and an all point level but, yet, we can't seem to come up here for 25 years and knock on the door, trying to help those local people in the local community. You know, the work force investment boards and what is out there, basically, what the statements are made in here, we divested all this information and all of this down to the local level but, yet, we are not willing to fund them.

Mr. CARDIN. I agree with you. And I think that one of the matters that we may have to look at in this Committee is the relationship to the appropriation process, because I am somewhat amazed that there is not a more adequate funding during this period of our economy to the Unemployment Insurance accounts of the states. So it is something we need to take a look at and it is a fair comment, something that is not within the jurisdiction of this Committee, but something that, clearly, we are very, very concerned about.

One last point if I might make. Mr. Smith, one thing that concerns me, it seems to me under the current system where interstate competition among the states drives states to use the stingiest standards for accepting Unemployment Insurance eligibility because of the competition among the states. And if we pass a bill that devolves the revenues to the states, that might just be exaggerated and worked to the disadvantage of working people. I am just curious as to your assessment on that.

Mr. SMITH. Well, I think you are absolutely right. And the two points that you have raised are related. If we don't set Federal solvency standards, states can compete and will compete with each in ways that reduce their solvency. The lesson of the 'eighties is unmistakably clear, and we forget it at our peril. It is also true that

we ought not to encourage states to compete by lowering benefits for many of the reasons that you talked about and that both Van Ooms and I talked about. This work force has changed a lot. We need a different benefit structure than we have had over the past five decades.

This is an opportunity to address both the solvency issue and the benefit adequacy issue that is almost impossible to address during recessionary times. But if we take the step now of foregoing our opportunity to insist on solvency, to help states assure solvency in some of the ways that Mr. English has proposed, we will relive the 'eighties a couple of months after the next recession hits.

Mr. CARDIN. Let me make just one last point. And I appreciate the references that have been made to Welfare reform. And it just seems to me, again, counter-intuitive that if we are concerned about people leaving Welfare for permanent employment, and we know that many of them will have low-paying jobs and part-time jobs, and they are not going to be qualified for Unemployment Insurance. That doesn't seem to me to be consistent with our strategy to get people off of Welfare permanently into the employment structure. I thank you for your comments.

Chairman JOHNSON. Mr. McCrery.

Mr. MCCREERY. Well, thank you all for your testimony, for bringing us your particular perspectives to this discussion about our Unemployment Insurance system. Just at couple of things I want to comment on: (1) The solvency issue. I am looking at the list of states here and their trust fund balances, and my State of Louisiana has about 8 years worth of excess benefits in the trust fund. I hope we don't have an 8-year recession. If we do, we are all in trouble.

There are very few states on this list that have what I would consider to be low trust fund balances; there are a few, and shame on them, I guess, if they get into a tight—because we did that in Louisiana, as I pointed out before, and paid through the nose for it. But we have recovered, and we have reduced taxes, and we have a sufficient—more than sufficient—trust fund balance for a rainy day. So I think all this talk about solvency is perhaps a little overblown and maybe even a red herring.

The fact is we have huge surpluses in our Unemployment trusts funds at the Federal level. The only reason for that—it has nothing to do with the workers, it has nothing to do with taking care of people. The only reason is we were hiding our deficit. We were masking the size of the Federal deficit. So I am a little bit upset that we are talking about all these other things, solvency, and increasing benefits, and all this stuff, as a roadblock to doing what we should have done a long time ago in being honest with the taxpayers and say we are not using this money for the purpose for which we told you we were collecting it and we are going to give it back to you. That is point one. So to say—for the administration to say we will not accept any bill that reduces the employment tax unless you attach all these other reforms on it is really disingenuous, I think.

In my bill we do exactly with the Unemployment system what we have done with Welfare and had so much success with. And Mr. Smith, I have not read your testimony, and I will, but you made

reference to, or you started to tell us why devolution was a bad idea. But you only mentioned one thing, and that was some vague reference to there being a national labor market now. I don't understand that comment. What do you mean by that? What is a national labor market? Why is that argument against devolution? What do you mean by national labor market?

Mr. SMITH. Well, Congressman, we have a much more integrated national labor market than we did a few decades ago and, certainly, than we did when the Social Security Act was passed. We are more mobile. Not only do we move among jobs, but we move among places. And the structure of the economy is now evolving in much more rapid ways, partly due to technology, partly due to telecommunications. The old assumptions about a place and a worker no longer describe either the employment relationship or the employment experience of most of us. And we need to help people prepare for a labor market which isn't defined in as simple geographic terms as it used to be.

Mr. MCCRERY. So in other words, the folks in South Louisiana that lost their jobs recently, you would just tell them to move?

Mr. SMITH. Congressman, I didn't say that. You did. No, I wouldn't just tell them to move, but I would want to make sure that the system of employment assistance, the one-stop centers, the way in which benefits are structured, encourage them to have the same kind of flexibility and ability to move, and information about opportunity, and access to national information that employers have.

Mr. MCCRERY. Well, but surely, you are not suggesting that conditions in Louisiana are the same as conditions in California, or New York, or Michigan. Surely, you are not suggesting that the people in my state who have lost their jobs don't deserve at least the chance to find a job in their home state and get serviced by an employment benefits office in their home state?

Mr. SMITH. They do, Congressman. And I think you and I would agree that that is an argument the AFL-CIO has made with great regularity. My point here is that it may not be true any longer that the best and most promising opportunity for an employee who loses their job in one parish is in that same parish. You talk about 108 months of coverage, but your colleague talked about closed offices. There is something wrong with a system that creates both of those outcomes at the same time. It is not at all clear—

Mr. MCCRERY. My bill would solve that.

Mr. SMITH.—that your bill will solve that or that devolution is the magic bullet here.

Mr. MCCRERY. Well, the reason that devolution works so well, one reason that devolution works so well with Welfare reform, is because different areas of the country have different needs, have different resources, different assets. The same thing holds true with employment. And therefore, I think devolution makes a lot of sense in the area of Employment Insurance as well. Louisiana knows its needs. They know where they need to put offices. They know the kinds of jobs that might be available to somebody who loses their job in a garment factory. They are not necessarily going to be able to get a job in Houston even at the shipyards where there might be jobs. But they might be able to get a job in the tim-

ber industry right next door because that is the kind of jobs that we have. We know that. Ms. Johnson doesn't know that, Mr. Cardin doesn't know that, people up here in Washington don't know that. Mr. Forster does. It is his job. So I question your conclusion that devolution is not possible because of the changing labor market.

And I want to look at this alternative base period, because I have to admit I am not as up to speed on this as I hope to be. But it seems to me that you are talking about simply making an effort to include more recent wages in the calculation of benefits. Is that correct?

Mr. SMITH. That is correct.

Mr. MCCRERY. So it is not any alternative. It is not some alternative—

Mr. SMITH. Right. It is an alternative to the current—

Mr. MCCRERY. It is really just capturing that data or most recent wages and including that, which seems to be an eminently reasonable thing. However, I want to ask the folks from the private sector, and maybe Mr. Forster, does that involve a cost to gather that data? Is it reasonable to get that data or is there a problem with that?

Mr. FORSTER. Yes. I don't think that is a problem. I don't think that data would be the problem, you know, assuming that they are working for a contributing employer, then we have that information.

Mr. YARBROUGH. Even though I represent a large employer, my dad is a small employer. And they pay taxes on a quarterly basis, and they still use their accountant and their bookkeeper to calculate, and estimate, and pay their taxes. And therefore, if they did have a small shutdown or a layoff, some of that information will not be as capturable in the small employer, small segment, of the economy. Remember that small employers have created more jobs and have created more opportunities for folks than all of the Fortune 500 companies have in the last 5 years. So the small employer is the one who would be at risk in trying to provide information on an alternate base period.

Mr. SMITH. If I could just briefly, Congressman—

Mr. MCCRERY. Sure.

Mr. SMITH. It might be more difficult for small employers but, you know, this is an opportunity to take advantage of the technology that is available to us that doesn't discriminate based on size. This information is available. Just remember, the alternative is a large number of hardworking men and women who don't qualify for Unemployment Insurance when they most need it.

Mr. YARBROUGH. One follow-up. We continue to try to permanently expand coverages with a temporary tax.

Mr. MCCRERY. Are we talking about a month's worth of wages or a quarter's worth of wages?

Mr. SMITH. A quarter.

Mr. MCCRERY. A whole quarter's worth that are not reflected—

Mr. SMITH.—that are not counted in the current calculation as to eligibility and benefit level.

Mr. MCCREERY. Well, Madam Chairman, thank you for allowing me that time to question the witnesses, and thank you all for appearing with us today.

Chairman JOHNSON. I am getting a sort of hook from behind me here, because the Full Committee begins its proceedings in a few minutes, but I did want to point out this. I think that the comments that have been made here are very, very helpful, and it helps me to see places that we could all agree, places that we will clearly not be able to resolve in the context of a session this year. But I think there is an urgency here that merits our consideration of action, even though this isn't the ideal session to make such significant changes.

But it is very disturbing to see how the system as it is currently structured does disadvantage the most rural, the most isolated workers. And that is an enormous concern and a very clear insight that you brought to us. It is also true that as we move into a global era, we absolutely have to have a better way of responding to the substantial adjustments that have to be made. And we have not been very successful at this in the past. It is also true that our Trade Adjustment Assistance Act, whose goal it was to deal with this, does have the merit of allowing people to be trained while receiving some income.

So there are a number of issues that I think we need to think further about here. There have been some very good suggestions, I think, some very doable suggestions. But one thing you haven't talked about much, and we don't have time to talk about, so I am just going to talk about it and then you can think about it and get back to me.

The strength of our workforce, the opportunity for welfare recipients who are moving into the workforce to advance, and the opportunity for people who are moving from one sector to another to do well all depends on training. And I have been very impressed with the extent to which some of my employers who have had significant layoffs have been quite generous about training. And I have had a number of people say to me, oh, yes, I got a job offer, but I am going to finish this training first. I haven't had this opportunity in my life. And that is very important.

So I think we need to give some significant thought to the difference between the Unemployment benefit for someone who is getting training for reemployment and Unemployment benefits for someone who isn't attending, in a sense, to the business of future employment. I know this is hard. I am not intending that we mandate it, but I am proposing that we at least think about differential issues or freeing states to do that, because education is so key.

Look at the difference between the rich/poor statistics of every organization, and the one thing in which they are all in agreement is that if you have less education, you earn less. And the people who are sort of condemned to do poorly in life are the people who didn't graduate from high school or now who graduated from high school but who had no other additional training. Mr. Forster.

Mr. FORSTER. Madam Chairman, you—and it was one of the things that I left out and you just hit on it—and that is, as this country and as our states move down to record low unemployment, 3 percent, 4 percent, whatever it might be, those people that are

left, that you are talking about, they are the ones that have the most barriers, need the most help, need the most people help. You can't give them the Internet and say go find a job.

So you do need training, you do need people, they do need the help more than if—during a recession when unemployment is up at 6, 7, 8 percent. Those people have work experience, they have got work ethic, they can move back into the work force much quicker than what the country is experiencing now, not only with Welfare recipients but with people coming out of jail, another critical group that we have to do something with that the Department of Labor has really ignored, that those people are coming out regardless, and they don't have any training, and we give them \$20 and we say good luck.

Chairman JOHNSON. And one of the reasons that welfare reform has worked is because it has accepted part-time employment and complemented that with a lower but still real benefit. Now, you know, I think we have just got to look at part-time employment and part-time training. What should be our position as a support program to someone who wants to work part-time so they can take this three, or four, or five, or 6-month training program? We have got to really begin to think about these things. It is really breaking away from the past well beyond where these legislative proposals are, but opportunity is so clearly a function of skill growth that I think we cannot just be blind to that real fact. Mr. Smith.

Mr. SMITH. You are surely right about that, Madam Chair, and this country sinfully underinvests in training our workers, not simply those who have lost their job. I would caution, as you would expect me to, this is an insurance program. Workers pay for it all of their life. Many of them are cyclically and truly temporarily unemployed. The notion that we might treat them differently than someone who was unemployed in a place like some of the garment factories that Mr. Forster talked about who really do need training, we need to be very careful here.

This is an insurance program. Most economists, I think we would all agree, one way or another, this it is paid for out of the wage packet. We ought to spend more money on training for each and every worker, with or without a job, but I am not sure we want to think about turning this insurance program that people rely on during temporary spells of unemployment as well as more permanent, into a training program that is mandatory.

Mr. YARBROUGH. Madam Chairman, I would like to mention that in the Work force Investment Act, the 134 Federal programs that were put down to four block grants, and that is an essential part of the one-stop but, yet, we have not expanded the job service side in order to help place these people who are now being referred to those programs. And states by states, there are states who exempt the job search requirement for people that are going to training. Our company alone, we have GED classes and additional training from outside voc-technical schools that are conducted inside our plants and inside our locations every day to help increase the skills of our current work force. We have to continue to do that.

But the Employment Service side, what we are talking about here is such a flat funded level that they are not going to be able to refer people that are going to be coming out of these Work force

Investment Act training programs in the next couple of years. Remember July 1, 2000, when that becomes mandatory this year, you know, if we don't send some money their way, they are not going to have the ability to deliver those folks to the employers that are needing them in high skilled jobs and medium skilled jobs that employers are looking for.

Chairman JOHNSON. I do appreciate the tremendous pressure on our Unemployment services and how creative they have been, and how remarkably different they are from 5 years ago. And I think it is almost criminal to be holding a state with 161 months of benefits, which they will probably never use, and not give them the resources for a much more vital employment support system.

I was very interested in the low wage issue. I am, however, concerned that, apparently, under the current system, if you earn \$7 an hour, which is above a number of states' minimum wages—not that I support that, but I mean this is just a fact—that you would have to work 4.5 out of every 13 weeks for two quarters in order to qualify. In other words, you would only have to work five-and-a-half weeks out of a quarter in two successive quarters to qualify. So I mean I am interested in following up on this because I do think—I am concerned about the lack of eligibility of the low earners, but that is not a very high threshold, five-and-a-half weeks out of thirteen weeks, two quarters in a row.

So lets give that some thought. I welcome your follow-up input and, you know, if we all recognize that nobody is going to get everything they want, there is an opportunity to make a very significant stride forward this year. And you know, if we don't do it this year, we are going to have a new president. I don't care what party, a new president will take a long time to ever get down to an interest at this level of legislative activity. Truthfully, there will always be big item issues that will take precedence.

So this is nobody's favorite issue. That is why the system is so grossly outdated. And we do have an opportunity here if we can do something together that would be better for people who are unemployed, better for state systems that have shown extraordinary creativity in helping the least likely workers to get into the work force and begin to advance. But my whole view, as many of you have heard me say before, is that the challenge to Welfare reform is now how do you help people move up the career ladder and how do you help them earn more. Well, that takes a different kind of unemployment system than we have in place now.

And if we can use this opportunity to move forward an employment service that not only helps you look for a job but helps you keep in touch. Some of the one-step centers have gone to actually keeping track of people and moving them into the next higher level job and bringing some unemployed person into the bottom level job. There is a lot of opportunity out there for career advancement, for wage development. And I don't know how much of that we can do from the Federal level or, particularly, through this lever, but I do think we have an opportunity. It would be unfortunate if we couldn't find some agreement on a number of the very specific recommendations that all of you have made. And I thank you for being here.

[Whereupon, at 4:25 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

Statement of American Federation of State, County and Municipal Employees

The American Federation of State, County and Municipal Employees (AFSCME) submits the following statement for the hearing record on legislative proposals to reform the employment security system. AFSCME represents 1.3 million, federal, state and local government employees and workers in health care facilities and other private sector institutions, including the employees of employment security agencies in 19 states.

Since its inception in the 1930s, the unemployment insurance system has played a crucial role in stabilizing the American economy during recessions and providing unemployed workers with temporary wage replacement income when they lose their jobs. However, dramatic structural changes in the nation's economy and employment arrangements are making the system increasingly less effective. In addition, persistent underfunding of the state infrastructure is leaving the system so weak that it is doubtful it could respond effectively and efficiently to a surge in unemployment.

• Today's employment security system needs to be strengthened and modernized to make it work effectively in the new economy. These reforms must address:

• *The changing nature of the workplace.* Low-wage and part-time employment continues to increase, as does contingent work, which does not follow traditional employer-employee relationships on which the unemployment insurance program is based. This trend is due to a variety of developments, including the growth of two-earner families and their desire for more employment options; industry's interest in a more flexible workforce; and rapid technological change. With few exceptions, the states have failed to adjust their systems to cover workers in these employment situations and continue to use outdated measures of workforce attachment, which exclude many workers in the new economy. They also have maintained restrictive policies implemented in the 1980s when federal law changed to require states to pay back federal loans with interest. As a result, reciprocity rates are at an all-time low, with some states experiencing rates as low as 19-20 percent.

• *The decline in stable long-term employment with one employer.* The old model of lifetime employment with one manufacturer and cyclical periods of unemployment has become less common. As the information technology and service sectors have grown and displaced the old industrial economy, increasingly workers change employers and even occupations one or more times in their lives. In order to minimize personal hardship and promote national productivity, we need to make these transitions as smooth as possible. The employment security system is the natural gateway for income replacement and reemployment services to workers who experience dislocations and need retraining.

• *Deterioration of the system's infrastructure.* Chronic federal underfunding of the states' unemployment insurance and employment services operations has reached a critical stage. The employment service has lost half its staff since the 1980s while most states have had to close offices. New technology, such as America's Job Bank and America's Talent Bank, can enhance the system's productivity, but states have reacted to the funding shortfalls by relying heavily, if not exclusively, on automated systems. For example, many now use centralized telephone systems for taking unemployment insurance claims. Telephone claims can provide added convenience and increased efficiency, but it is not well suited to handling mass layoffs or appeals of denied claims. In addition, highly automated systems are likely to undermine the unemployment insurance "work test." Replacing local offices and personnel with automated systems has created new access problems for unemployed workers and can undermine their statutory rights to a fair appeals process and to timely payments when due.

These problems result from both federal and state neglect of this important safety net program. The solution, however, is not for the federal government to withdraw from its small, but critically important, role in the system as H.R. 3174 proposes, or just to cut the federal unemployment tax as H.R. 1975 proposes. Instead, the solution lies in a comprehensive package that addresses the issues of reciprocity rates, solvency of state trust funds, the adequacy of administrative funding, and the correct level and structure of the federal unemployment tax.

AFSCME opposes H.R. 3174 because it will result in a maldistribution of administrative resources and undermine the central national risk-pooling feature of the unemployment insurance system. In doing so, it will create a new set of incentives which may actually favor continued underfunding of administrative costs and new employer tax cuts at the expense of unemployed workers.

H.R. 3174 addresses the problem of federal underfunding of state operations by giving states authority to set administrative funding levels. It does this by creating 50 state administrative accounts, returning to the states the percentage of Federal Unemployment Insurance Tax Act (FUTA) revenues which their employers pay into the Federal Trust fund, and empowering the state legislatures to set annual administrative spending levels. This is in distinct contrast to the current practice of pooling the FUTA revenues among the states and then distributing the funds based on their actual workload needs. It means that states with relatively large FUTA payments but low reciprocity rates will get a windfall, while states which pay benefits to more workers will not.

Furthermore, H.R. 3174 is likely to encourage continued underfunding of state operations. It requires that unused FUTA administrative funds be transferred from each state's administrative account into its benefit account thereby eliminating the current separation between federally-funded administrative accounts and state-funded benefit accounts. Since states directly control the level of employer taxes and revenues for the state benefit accounts, H.R. 3174 is likely to create new pressures at the state level to transfer as much federal FUTA revenue as possible to state benefit accounts in order to hold down or reduce state employer taxes.

The pressures at the state level to create a "business friendly" environment have been strongly evident in recent years. Between 1992 and 1999, total yearly increases in state trust fund balances overall averaged an unprecedented 85.62 percent as economic activity surged. Yet even as reciprocity rates and wage replacement rates were dropping nationally, at least 25 states have cut their unemployment taxes over the last few years, according to a recent analysis by the National Employment Law Project. At least nine states, which adopted tax cuts, had reciprocity rates below the national average of 33S percent, and three of these states were among the four states with the lowest reciprocity rates in the country. Three of the states that awarded tax cuts did so despite the fact that their trust funds are below the national average in terms of solvency and could not withstand a serious recession.

There is no reason to expect this dynamic will be different with respect to the administrative funding accounts. In the end, pressures to cut state employer taxes will thwart the goal of adequate administrative funding.

H.R. 3174 also will cripple the federal government's ability to enforce federal accountability requirements. These requirements include: 1) proper and efficient administration of the program using state merit-staffed employees; 2) "methods of administration" assuring prompt and accurate payment of benefits; and 3) due process and fair hearing protections for claimants who are denied benefits. These standards are critical to ensuring strong accountability in the system and protecting the rights of unemployed workers to fair treatment and prompt action by state agencies.

AFSCME has participated in the stakeholder dialogue meetings that began last spring. The stakeholder dialogue process focused on three basic aspects of the system: administrative funding, reciprocity rates, and the federal unemployment tax. We believe these meetings have been extremely valuable in educating the participants about each others' viewpoints and in identifying areas of potential consensus.

All of the stakeholders agree on the need to make the financing of unemployment insurance and employment service administrative costs mandatory in light of the failure of the appropriations process to provide adequate infrastructure funding. AFSCME supported and continues to support a workload driven formula, which retains the current federal role in pooling risk and resources and encourages states to respond to demands of the national economy. We opposed and continue to oppose the idea of a state match to draw down federal resources which emerged as an alternative to full devolution.

As conceived to date, the state match proposal would return to the states a certain percentage of their proportionate share of FUTA taxes paid by employers in their states which they would use to draw federal trust fund revenue. We oppose this approach because it contains key elements of the full devolution proposal. By basing the state share on FUTA tax receipts, the proposal runs into the same distribution problems inherent in full devolution. In addition, the state match contains the same requirement to transfer unused administrative funds to state benefit accounts, thereby undermining the national insurance features of the present arrangement and potentially encouraging states to use federal unemployment tax revenue to help lower state unemployment taxes. And, finally the proposal would create 50 state administrative accounts, setting the stage for full devolution.

AFSCME strongly believes that federal FUTA resources should be allocated based on state workload needs and that a formula approach does this best. In addition, a formula has the advantage of allowing the federal government to guide state behavior from a national perspective in a way that the states by themselves may not. For example, the Department of Labor (DOL) has been instrumental in moving

states to participate fully in America's Job Bank, a highly successful endeavor. It also has awarded technology grants to states to increase the system's productivity, and federal law has made worker profiling a national requirement.

True unemployment insurance reform, however, would be seriously lacking if it were defined only as administrative financing improvements. The administration's proposal, introduced as H.R. 1830 by Reps. Sander Levin and Phil English, represents a good first step by recognizing that the scope of UI reform must be more comprehensive. It provides incentives for states to implement alternative base periods that will help more lower wage workers qualify for benefits; improves the extended benefits trigger to make it more effective during recessions; encourages states to improve the solvency of their trust funds; and increases Trust Fund distributions to provide some very modest interim administrative funding relief to the states. However, we do not believe the legislation goes far enough in either the area of benefit expansions or tax reform.

It should be a matter of major concern to anyone who believes in the value of employment security as an economic stabilizer that reciprocity rates are as low as they are. The system's ability to soften the economic effects of recession will be seriously compromised if the percentage of unemployed workers it reaches continues to decline. Furthermore, workers on whose behalf employers pay unemployment taxes should not be denied the income replacement they have earned because of inequitable and outdated rules. A reform package that does not improve reciprocity rates in a meaningful way would not be true reform at all. Accordingly, AFSCME strongly supports the following measures to improve reciprocity rates:

- **Alternate Base Period:** There is no good reason for states not to use an alternate based period now that technology allows for speedier reporting and posting of wages. Furthermore, mandating an alternate base period would allow 450,000 more workers to receive unemployment benefits. Requiring states to use available technology in a way that benefits unemployed workers is consistent with the federal duty to ensure the "proper and efficient" administration of the program and federal requirements for payments to be paid in a timely fashion.

- **Part-time Workers:** Workers seeking at least 20 hours of work per week should not be disqualified from receiving unemployment benefits if they have met the earnings requirements. Part-time employment has become a major component of the economy and increasingly is recognized as an acceptable option in a society in which workers face intense pressures in balancing the demands of work and family. Furthermore, employers often prefer to hire part-time workers in their search for a more flexible workforce.

- **Lower or Replace Earnings Requirements:** The increase of low-wage and intermittent employment arrangements has acted as a barrier to many workers, and many states have been slow to adjust their earnings requirements in recognition of these trends. Requiring or encouraging states to have an earnings requirement of 400 times a state's minimum wage and eliminating the high quarter earnings requirement would address this problem. Alternatively, the federal government could award technology grants to states to encourage them to establish information systems that can replace earnings with hours worked as the measure of labor force attachment. The technology is available now, and such an approach would eliminate the current discriminatory treatment of low wage earners.

- **Extended Benefits:** AFSCME supports eliminating the federal work search requirements so that the federal and state rules are consistent. We also urge a lowering of the federal trigger and the use of a trigger based on total, instead of insured, unemployment.

- **Separations for Personal Cause:** Workers may have to leave work for personal reasons, such as domestic violence or the transfer of a spouse by the employer to a different state. While, in the very strictest sense, the decision to leave work for these reasons may be viewed as "voluntary," in reality it rarely is. Some states have begun to recognize this fact as evidenced by the recent adoption of new laws that provide unemployment benefits to victims of domestic violence. AFSCME supports encouraging state adoption of such policies.

Of the current proposals relating to taxes, AFSCME strongly supports Rep. English's proposal in H.R. 3169 to repeal the income tax on unemployment benefits. This tax was adopted to increase revenue at a time of federal deficits and creates undue hardship on many workers when they most need assistance. With surpluses projected well into the future, the need for this unfair tax no longer exists.

AFSCME opposes repealing the FUTA surtax before comprehensive reform is considered. While amounting to only \$14 per worker per year, the surtax raises 25 percent of current FUTA revenues. Repealing the surtax before comprehensive reform can be debated would distort congressional consideration of broader reform and potentially jeopardize it.

AFSCME believes that reforming the federal FUTA tax is a much more complicated matter than simple repeal of the surtax. The current federal wage base of \$7,000 has not been updated since 1983. At the time, the \$7,000 wage base was roughly equivalent to the federal minimum wage. (In 1939, the federal FUTA tax was .30 percent on a taxable wage base of \$3,000 which was much closer to the average weekly wage than the minimum wage of \$.30 per hour or \$624.) Since 1983, 41 states have established state taxable wage bases that are higher than the federal taxable wage base. They range from \$8,000 all the way up to \$25,500.

A substantial increase in the federal wage base could allow the FUTA tax rate to be adjusted downward in a way that could relieve the tax burden on small employers with low wage earners. For example, with a \$19,000 wage base, it would be possible to lower the FUTA tax rate from the current .8 percent to .34 percent while still raising the same amount of revenue currently raised. The tax on employers with workers earning a wage equal to the new minimum wage just approved by the House of Representatives would drop by \$7.00 or half the \$14 cut they would enjoy under the surtax repeal.

While these figures could be adjusted to accommodate the revenue needs of a comprehensive reform package, the example serves to demonstrate a key point. Repealing the surtax is not the most efficient way to provide small employers tax relief, and it does not address the fact that they are carrying a disproportionate burden of the FUTA tax. A better approach would be to restructure the FUTA tax to achieve more progressivity and equity among employers. This could be done in concert with a possible decrease in total revenue should that be justified on the basis of a final package.

In closing, AFSCME believes that the current strength of the economy and the broad concern about underfunding of state administrative costs present a unique opportunity to enact the most significant changes to the unemployment insurance system since the early 1980s. H.R. 3174 looks to the past of the early 1930s, when the federal government had no meaningful role in the nation's economy. Instead, we urge the committee to transform the unemployment insurance system into a modern employment security system by building on and strengthening the federal-state partnership.

Statement of Hon. Bob Taft, Governor, State of Ohio

Good afternoon, Madam Chairman, Congressman Cardin and members of the Subcommittee. My name is Bob Taft, Governor of Ohio. It is an honor and a pleasure to appear before the Subcommittee today, to testify in favor of Congressman Jim McCreery's legislation, H.R. 3174, the "Employment Security Financing Act." I would like to start by asking that my full written statement be included in the hearing record.

You may recall I appeared before the full Ways and Means Committee in June, 1999 to speak in favor of the concepts that ultimately were included in the bill Congressman McCreery introduced in October. Last June, I asked Congress and the White House to embrace needed reforms to the Federal Unemployment Tax system. I said FUTA reform is necessary to eliminate a needless, 24-year old "temporary" surtax on the nation's employers, and to allow state re-employment services access to the dedicated revenue flow that helps them put the unemployed into jobs, and helps place the under-employed into better jobs.

Since my testimony last Summer, the FUTA system has not improved. It still fails to serve the workers who need it and employers who pay for it.

FUTA—A SYSTEM IN NEED OF REFORM

Employers continue to be overtaxed. In 1976, Congress enacted the FUTA surcharge to provide funds to reimburse depleted trust fund accounts that have long since been restored. The Tax Relief Act of 1997 extended this surcharge much longer than necessary, through the year 2007. There is no justification for the 30-year extension of this "temporary" surcharge.

Not only are employers being overtaxed, but appropriations from this dedicated source of administrative funding also have been reduced. In 1997, 48 of the 53 states and jurisdictions receiving administrative funding for unemployment insurance and employment service functions received less than the FUTA taxes collected from employers in those states. Since 1990, less than 58 cents of every employer FUTA tax dollar has been returned in administrative funding for states.

A comparison of the taxes paid by employers to administrative funds provided to the states paints a dramatic picture. From 1993 to 1998, annual FUTA tax collections increased from \$4.23 billion to \$6.37 billion while administrative funding was cut from \$3.81 billion to \$3.47 billion. I have provided several graphs demonstrating this trend, which are appended to my statement. Although the latest data are only available through 1998, the trend line has continued in 1999 and 2000, rendering the return of employer taxes to the states an increasingly smaller percentage each year.

In Ohio, we receive 39 cents on the dollar. Inadequate funding in recent years has forced us to close 22 local offices, significantly reduce staff, and use State general revenue to make up for cuts in federal funds that are being maintained in trust, ostensibly to provide the very services that have been cut through the federal appropriations process.

The differential between federal administrative funds provided and actual costs continues to increase. In 1993, the state deficit in federal funding compared to cost was \$13.3 million. By 1998, the deficit had grown to \$17.5 million.

We must do a better job of supporting state efforts to ensure the ability of American families to adjust to the demands of the workforce in this new century by providing adequate funding for employment services for those who become unemployed.

It is time for a change. We need a system that properly provides sufficient funds to states for administration, and minimizes the tax burden on the employers who pay for it.

Congressman McCrery's bill, and a similar measure introduced by Senator Mike DeWine of Ohio, S.462, are carefully crafted to reform a federal-state partnership that does not adequately serve its state partners. We need Federal Unemployment Tax reform that will do each of the following:

- Repeal the 0.2 percent FUTA surcharge;
- Provide adequate dedicated funds for administration of the unemployment insurance program and public employment services;
- Increase flexibility on the use of funds as states develop their integrated workforce development systems, as Congress has mandated; and
- Transfer responsibility for collection of the FUTA tax to the states.

FUTA Reform: a Catalyst for Effective Workforce Development

FUTA reform no doubt has considerable fiscal significance for states. But I believe the larger, more compelling story is how important it is for meaningful, effective workforce development. I view the McCrery and DeWine legislation as a key tool with which to complement earlier reforms that were the product of bipartisan cooperation between this Congress and the White House. The "Employment Security Financing Act" really completes the work on landmark successes such as Welfare Reform and the Workforce Investment Act. I regard the "Employment Security Financing Act" as a necessary next step toward ensuring that more of our citizens and their families can enjoy our booming economy, and thrive as members of an ever-changing workforce.

Since 1997, when Congress enacted Welfare Reform, states have risen to the challenge and have used their new flexibility in ways that have guided more of our citizens toward self-sufficiency. From a federal point of view, Welfare Reform provided much-needed budgetary certainty, replacing an open-ended federal entitlement with a capped entitlement in the form of a block grant. Near-term efforts to balance the federal budget clearly were aided by states' acceptance of the Welfare Reform package crafted by Congress and the Administration.

States continue to invest heavily, and creatively, in those areas which will empower more of our fellow citizens to break the cycle of dependency through state- and local-based strategies. We are investing great resources in our schools, in health care and other areas to let more Americans participate in the best social program ever devised—steady employment.

The nation's employers have been a key component to this success story. As you know, many employers provide an array of benefits to employees and their families that go beyond a paycheck.

Now states and employers are wrestling with the next challenge: Workforce Investment Act implementation. States face tremendous challenges in the 21st Century to develop workforce investment systems with the resources and the flexibility to develop skilled workers and match them to employers' needs. The enactment of H.R. 3174 will give states greater flexibility and adequate resources to meet this challenge.

With the Workforce Investment Act of 1998 (WIA), Congress and the President took an important step in requiring coordination of workforce development activities at the state and local level. The legislation, now being implemented across the coun-

try, requires the participation of a number of agencies involved in workforce development activities as part of a coordinated state plan. Although WIA contemplates the coordination of various workforce activities covering a number of categorical programs as part of a one-stop system, funding of core employment services to be available to a universal population is not sufficient. The McCrery bill addresses the need for adequate funding for critical public employment services, which include: job search and placement services; counseling; testing; occupational and labor market information; assessment; and referral services.

Throughout the WIA implementation process, funding flexibility has been identified as an absolute necessity for effective workforce system development. Categorical funding streams, each with specific limitations, create barriers to the effective use of resources at the state and local level to serve our worker and employer customers. H.R. 3174 eliminates barriers by providing maximum flexibility for the use of funding for unemployment insurance and public employment services, with primary emphasis on returning unemployed individuals to work.

We need this additional flexibility and funding to make the link for individuals from welfare to work, from training to work, and from unemployment to work. In this time of economic boom and worker shortages, employers desperately need assistance in finding skilled workers. Without the funding necessary to develop an integrated, universal workforce development system, our effectiveness in serving employers and the full range of workers is limited.

Experience has taught Ohio that many of the same populations most reliant on employment services are often the people most in need of other support services. My state has demonstrated its commitment to successful service integration by merging our Department of Human Services with our Bureau of Employment Services. The new agency will be the Ohio Department of Job and Family Services. Besides making administrative sense, I believe the title of the revamped agency underscores the commonality of the missions it will serve.

Many employers, large and small, currently are having difficulty locating workers as the nation's unemployment rate hovers near a record low and the economy enters its ninth year of expansion. All employers are burdened with the costs of locating, training and retaining employees, when they should be receiving these services through state and local workforce development systems. Employers have a right to expect federal and state governments to honor their commitment to construct the integrated workforce development systems that are mandated under the Workforce Investment Act and provide the employment services for which employers pay nearly \$7 billion in taxes annually.

Businesses and workers deserve reliable re-employment services, both in a booming economy, and when the economy cools. States are the principle providers of those services, and proper FUTA financing will give them the resources and predictability that are missing from the current federal-state partnership.

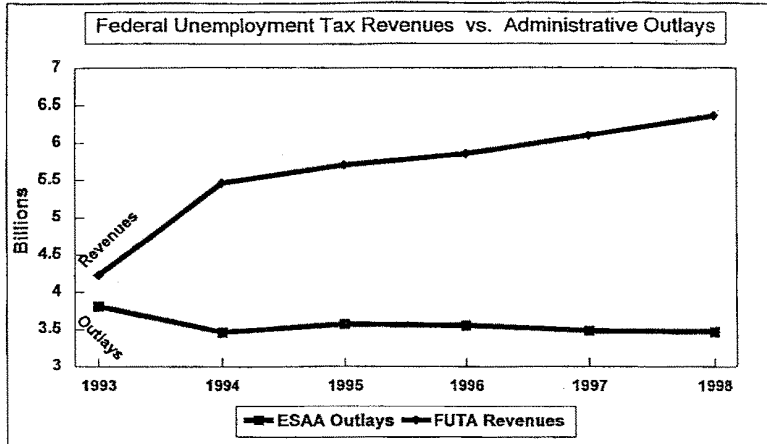
It is true that states now confront the task of finding jobs for some of our hardest to place individuals. As governors, we must be prepared to serve all of our citizens, particularly those requiring extra assistance in joining the workforce. To be successful, to the degree envisioned by Congress and the President, we must have employment services that are properly funded and have sufficient flexibility. That will be true no matter what shape our economy is in.

As the federal government now has achieved an on-budget surplus, the time is right to embrace reforms which will help states meet their responsibilities to all workers and to the employer community.

Since my testimony to the Full Committee last June, the number of states that have embraced the FUTA reforms contained in H.R. 3174 has grown to 32. Congressman McCrery now counts some 40 cosponsors for his legislation.

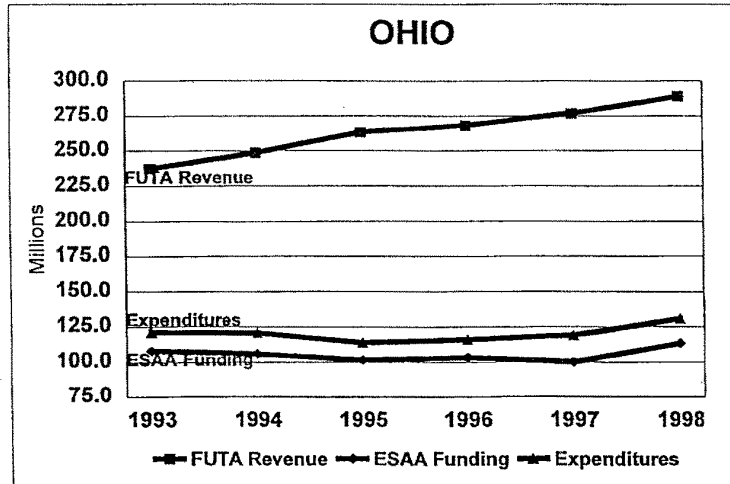
Please join me in support of these necessary reforms, which represent a logical next step to guaranteeing the other historic reforms which Congress and the White House have enacted during these past several years.

I urge your favorable consideration of H.R. 3174.
Thank you.



YEAR	ESAA Outlays (billions)	FUTA Revenues (billions)
1993	\$3.81	\$4.23
1994	\$3.46	\$5.46
1995	\$3.57	\$5.70
1996	\$3.55	\$5.85
1997	\$3.48	\$6.10
1998	\$3.47	\$6.37

Source: USDOL, UI Outlook June 1999



OHIO (in millions)	1993	1994	1995	1996	1997	1998
FUTA Revenue	237.1	248.4	263.1	268.3	276.9	288.9
ESAA Funding	107.8	105.7	101.6	103.3	100.1	113.4
Percentage	45.5%	42.6%	38.8%	38.5%	36.2%	39.3%
Expenditures	121.1	120.7	113.8	115.9	119.0	130.9

1998 includes Year 2000 conversion costs and supplemental funding.

**Statement of Society for Human Resource Management, Alexandria,
Virginia**

Madam Chair and Members of the Subcommittee:

The Society for Human Resource Management (SHRM) is the leading voice of the human resource profession. SHRM provides education and information services, conferences and seminars, government and media representation, online services and publications to 130,000 professional and student members throughout the world. The Society, the world's largest human resource management association, is a founding member of the North American Human Resource Management Association (NAHRMA) and a founding member of the world federation of Personnel Management Associations (WFPMA). On behalf of NAHRMA, SHRM also serves as president of WFPMA.

SHRM urges the Subcommittee to support the swift enactment of H.R. 3174, the bipartisan Employment Security Financing Reform Act. H.R. 3174 is essential to strengthening the state unemployment insurance and employment services (UI/ES) system and the workers and employers whom it is designed to serve. SHRM is a member of the Coalition for Employment Security Financing Reform, an informal coalition of business organizations and 32 states that support H.R. 3174. This legislation would amend the Internal Revenue Code, the Social Security Act, the Wagner-Peyser Act, and the Federal State Extended Unemployment Compensation Act of 1970 to improve the method by which Federal unemployment taxes are collected and to improve the method by which funds are provided from Federal unemployment tax revenue for employment security administration. Specifically, the bill would:

- repeal in the year 2004 the "temporary" unemployment surtax that employers have been paying since 1976;
- increase the flow of dollars from the Federal Unemployment Tax back to the states; and
- streamline how the tax is collected.

H.R. 3174 was introduced by Rep. McCrery (R-LA) with the bipartisan support of 35 co-sponsors. Unlike the Administration's proposals and Rep. English's (R-PA) H.R. 1830, the bipartisan Employment Security Financing Reform Act, H.R. 3174, will improve the method by which FUTA taxes are collected and funds are provided to administer the state UI and ES programs. The Employment Security Financing Reform Act will fix serious problems with the state UI and ES system resulting from the federal government's failure to provide adequate funding and will also provide funds needed to implement the Workforce Investment Act. The Administration's proposals will not achieve these goals.

For more than 60 years, employers have paid payroll taxes to fund programs collectively known as the Employment Security System. The program is a Federal-State partnership that provides four major programs:

- Employment Services,
- Unemployment Insurance,
- Veterans' Employment Services, and
- Labor Market Information

The programs are operated by State Employment Security Agencies (SESAs) using federal grants financed from a federal payroll tax on employers. In addition, states collect a separate state payroll tax to finance unemployment insurance benefit payments. The Federal government establishes the overall legal framework, provides technical assistance, collects and allocates funds for administration and provides oversight. States provide services to customers and establish laws for the collection of state unemployment taxes and payment of benefits.

The Employment Security System is founded on a "compact" by employers, workers and the State and Federal government, through which employers provide financing through payroll taxes, and workers receive unemployment benefits along with re-employment services to shorten their spells of unemployment. Employers also receive services to assist them in meeting their needs for skilled workers.

Although the federal budget is now described as balanced, some of that balance has been achieved over the years by offsetting balances in trust funds, including those within the employment security system. Consequently, employer payroll taxes are underwriting federal general revenue and providing funds for domestic spending unrelated to employment security. In 1976, Congress established the 0.2 percent "temporary" surtax to pay a debt arising from repeated supplemental extensions of unemployment benefits. This "temporary" tax has been extended numerous times and is now scheduled to continue until December 31, 2007. SHRM has historically

supported the repeal of the FUTA 0.2 percent surtax and supports the provision in H.R. 3174 and other pending legislation that would quickly accomplish this important goal.

SHRM has historically supported the repeal of the FUTA 0.2 percent surtax and supports the provision in H.R. 3174 and other pending legislation that would quickly accomplish this important goal. On February 11, 2000, the SHRM Board of Directors approved the following position statement on Unemployment Expansion and Reform:

Changes are needed to improve efficiencies in the Unemployment Insurance (UI) program. Unemployment Insurance reform can be accomplished without taking away any legal protections or benefits for workers under current law and without creating unnecessary burdens on employers. Legislation is crucial to reduce burdensome paperwork for employers, promote efficiencies in returning UI claimants to work, weed out fraud, and promote greater government accountability and efficiency in the use of FUTA funds. Many of the tax dollars that employers pay to finance the nation's Employment Security System are being used to artificially offset the federal deficit. For example, in 1997 alone, employers paid over \$6 billion in FUTA taxes and only \$3.5 billion came back to pay for programs. The remaining \$2.5 billion is being used to artificially offset the federal deficit.

States should determine the circumstances under which *unemployed* workers collect benefits under state Employment Security programs and how much they receive. However, the fundamental nature and purpose of the UI system should not be changed to allow individuals who are not unemployed to collect funds from the Unemployment Insurance Trust Fund. The UI Trust Fund should be reserved for involuntarily unemployed individuals who are able and available to work, and should not be diverted for other purposes, regardless of the merits of that purpose. Allowing states to divert funds away from unemployed individuals is short sighted and would inappropriately change the fundamental nature and purpose of the UI system. Allowing the misdirection of unemployment benefits for family and medical leave or other non-employment benefit purposes will shred the safety net that the unemployment insurance system is designed to provide to workers.

SHRM supports proposals to allow for faster and more efficient employment security services and to shift decision making closer to home where unemployment services/training can be customized to local conditions. SHRM supports the efficient collection of employment taxes and opposes proposals to accelerate FUTA and state unemployment tax collections due to the unnecessary paperwork burdens that would be imposed. Moreover, SHRM believes tax dollars that employers pay to finance America's employment security system should not be used to artificially offset the federal deficit.

SHRM opposes the extension of the 0.2 percent FUTA surcharge because it represents a breach in the 1976 congressional commitments that the tax would be temporary. This unnecessary increase will ultimately result in a tax increase at the cost of job creation.

Consistent with the SHRM board approved position, SHRM strongly supports the Employment Security Financing Reform Act, H.R. 3174 and urges its speedy enactment.

The Administration has repeatedly proposed a provision in its annual U.S. Treasury Department budget requests that would accelerate FUTA and state unemployment tax collections from a quarterly to a monthly basis. SHRM does not support the Administration's proposals as presented in Unemployment Compensation Amendments of 1999, H.R. 1830. H.R. 1830 would continue the 0.2 percent FUTA surtax through calendar year 2007 and would permit the Secretary of the Treasury to collect FUTA on a monthly or other basis.

H.R. 3174 will provide that FUTA and state unemployment taxes will be payable no more often than quarterly, and employers will no longer have to fill out duplicative FUTA and state unemployment tax forms. Instead, states will collect FUTA on the same form used for state unemployment taxes. This approach will simplify tax payment for employers and states, as well as the federal government. It will also increase tax compliance, because states are closer to the situation and in a better position to detect under-payments of FUTA.

Accountability for use of the money will be improved by requiring each state agency to report annually to its legislature and the public on services provided to UI claimants. More resources will be provided to prevent and detect UI fraud and abuse. Improper UI payments are a serious and costly problem, and states will have the resources they need to address them.

The greatest problem most employers are experiencing with the UI program is a labor shortage. The tight labor market makes it important to avoid policies that will increase utilization of transfer payments such as UI at a time when employers are

having difficulty finding applicants for job openings. With H.R. 3174, funds will be available for states to implement the Workforce Investment Act and operate One-Stop Centers, which deliver UI benefits and coordinate employment services. Without H.R. 3174, there will be no funding for states to deliver the services mandated by DOL.

Federal expansion of the UI program, as proposed by the Administration and in H.R. 1830, will take the program in the wrong direction and will hurt the workers it is designed to help. Expanding the program through relaxed eligibility rules and higher weekly benefits will ultimately weaken the system and hurt those individuals it is designed to protect.

On a related issue, SHRM also urges the Subcommittee to quickly hold hearings on and to pass legislation to stop the Administration's proposed Birth and Adoption Unemployment Compensation (BAA-UC) Rule (Federal Register, Vol. 64, No. 232/ Friday, December 3, 1999). The rule would allow states to use their unemployment insurance trust funds to provide paid family leave. The proposal would allow states to amend their state "able and available" requirements to include individuals on temporary leave for birth or adoption. This proposal could be finalized at any time.

SHRM strongly opposes the BAA-UC proposal on both policy and process grounds. Allowing the misdirection of unemployment benefits for family and medical leave or other non-employment benefit purposes will shred the safety net that the unemployment insurance system is designed to provide to workers. While SHRM strongly agrees that paid leave is a desirable benefit and encourages its members to provide a whole host of work-life benefits to employees, including leave for the birth or adoption of a child, we take strong exception to the approach taken in the BAA-UC rule. We strongly disagree with the President's May 23, 1999 statement that, through the BAA-UC: "We can do this in a way that preserves the soundness of the unemployment insurance system and continues to promote economic growth." May 23, 1999 Statement of President William J. Clinton at Grambling State University.

The BAA-UC proposed rule violates the clear and unambiguous intent of the letter and the spirit of both the Unemployment Insurance and the Family and Medical Leave Act laws.

SHRM supports a strong Unemployment Insurance system and believes that the present system needs reforms in order to effectively improve services for jobless workers. H.R. 3174 will allow for greater responsiveness to local needs and circumstances. State legislatures, rather than federal appropriations committees and U.S. Department of Labor and Office of Management and Budget (OMB) staff in Washington, D.C., will determine how much is needed to run state UI programs. This will maximize effectiveness by providing greater flexibility—and accountability for state UI/ES agencies. H.R. 3174 provides more resources for administration of the UI program. All states will be "winners. With FUTA funds for states currently lost in the federal budget process, all states are being shortchanged.

SHRM commends the Subcommittee for holding this important hearing on Unemployment Insurance reform. As we move into the 21st century, it is important that we strengthen the unemployment insurance system so that it meets the increasingly complex needs of the changing workforce. Therefore, SHRM urges the members of the Subcommittee to actively work to enact H.R. 3174 on a bipartisan basis, while opposing the Administration's proposals.

Statement of Hon. Gary Locke, Governor, State of Washington

Nearly 65 years ago, the Social Security Act forged a partnership between the States and the Federal Government to provide for the needs of unemployed workers. It blended a mix of basic Federal requirements with State flexibility in designing programs to meet local needs. The States financed the actual benefits, while the Federal Government financed the administrative costs. For the most part, the system has worked well.

But, much has changed since the 1930s. The work world is a dynamic one. What we produce, where we work and how we work now would seem like science fiction to most workers in 1935. Technology, too, has improved our services so we can do more with less and serve our UI customers by telephone and computer. All these changes have created new needs and new opportunities.

We need services for the unemployed and underemployed that are relevant to the 21st century—not the early 20th century. We need a comprehensive approach.

Reciprocity rates need to improve. In some states, as few as 17% of all unemployed workers actually receive benefits. The national average is too low—just over one-third of all workers are eligible for benefits. Washington State, with a reciprocity rate of about 53%, has long been among the leaders in making the UI Program accessible to a broad range of workers:

- In 1977, our Legislature recognized the weaknesses of conventional employment and earnings thresholds and established Washington's unique 680 *hours-worked* test.
- We've long had the *alternate base year* in place. New workers who can't meet the standard hours-worked test become eligible based on their most recent completed calendar quarter of work.
- Our state's *injured workers* are able to freeze wage credits until they are again able to work and are seeking work. Our Temporary Total Disability (TTD) program is an unqualified success.
- We were quick to recognize the benefits of short-time compensation and enacted our Shared Work Program in the early 1980's.
- In some cases, Washington law allows good cause for voluntarily quitting work to follow one's spouse to new employment.
- Due to continued underfunding even though federal account balances were full, Washington State is one of several that found it necessary to seek state money and enact state law to finance reemployment services for UI claimants provided through our Claimant Placement Program, and to use state penalty and interest funds to detect and collect overpayments, contributing to our efforts to combat fraud and abuse.
- We are currently trying to address the needs of our contingent workforce, and are especially hampered by federal law that requires different standards for educational employees in a labor market that has changed dramatically since those federal laws were passed in the 1970's. We believe the federal law is out of step with the current working conditions of teachers and needs to be changed to allow benefits to teachers between school years when they don't really have a guaranteed job for the next term.
- In Washington State, job search assistance, monitoring and verification are important enough that our Legislature specifies these activities in state statute. We know from the Work Search Study in Tacoma, Washington, and a more recent analysis in Maryland, that monitoring and verification make a difference by reducing the length of time unemployed, but the current federal funding formula doesn't reward states to fully operate these components.

Wage replacement rates must increase. When the Social Security Act was written, UI benefits were envisioned as replacing half a worker's weekly wage. Today, only 13 states replace at least half, the lowest state is at 32% and the national average is about 46%. In Washington State the replacement rate is 50%, just meeting the target and eighth highest in the system. Clearly, there's room for improvement.

Worker retraining needs to be supported. For most dislocated workers, retraining for new jobs is just hit or miss, with support dependent on a hodgepodge of Federal grants or targeted programs. Often, adequate financial support for living expenses is missing.

We actively supported retraining and I just signed legislation that provides up to 22 weeks of additional, state-funded benefits to workers in approved retraining programs. In some targeted industries up to 44 weeks of benefits are available. This action recognizes that, although unemployment is at its lowest point in generations, there are still structural changes taking place and dislocated workers need new or updated skills in order to find suitable work in our dynamic labor market.

There are issues, however, with the effective use of state and federal dollars for dislocated workers in training. When silo-funded federal benefits programs like Trade Readjustment Assistance (TRA) must be replaced by state-funded benefit programs when available, other dislocated workers lose out. If Washington had the flexibility to pay TRA benefits to certified TRA workers, we have estimated that an additional \$5–10 million in state-funded retraining benefits would be available to other dislocated workers who do not qualify for TRA.

There are financing issues, too.

States must maintain actuarially sound trust funds. Aside from the obvious logic for a sound foundation for the UI system, underfunding UI by some states puts other responsible states at an economic disadvantage.

The 30-year temporary tax must be repealed.

To achieve and maintain the economic growth that Washington and other states have had over the last decade, we urge you to repeal the "temporary" FUTA surtax, returning those tax dollars to the employers who paid them. In Washington State,

we've estimated that repeal would put an additional \$34 million dollars in the pockets of our employers. Nationally, possibly \$1.6 billion. This would go a long way to helping businesses to continue to invest in their workforce and improve the economy.

A comprehensive proposal is needed.

In the past, we've supported H.R. 1830 as a good first step toward a multi-faceted piece of legislation, expanding eligibility and improving administrative funding. But there is more that needs to be done.

With H.R. 1975, employers get relief of the temporary .2% FUTA surcharge, but that legislation does not address reforms needed in eligibility standards and administrative financing. Repeal of the .2% FUTA surcharge should only occur as part of a comprehensive proposal.

On the other hand, H.R. 3174 focuses all its energy toward a revamp of the UI program's financing structure, without addressing the other side of the equation—benefits, and in fact may reward states that have low reciprocity rates. We do not believe this is the answer either.

H.R. 3167 would change extended benefits requirements, offer incentives to states with healthy trust funds, allow states to collect the federal portion of the FUTA tax, and require states to fully inform UI claimants of their rights. It is a mix of fixes, but incomplete.

The Administration's request for FY 2001 starts to address one of our issues—under-funding of UI and ES activities—by requesting an additional \$50 million for the One Stop Employment Service to provide targeted, staff-assisted reemployment services to UI claimants identified as being at risk of exhausting benefits. What is not evident is an expanded investment in the technology solutions we need to serve the unemployed.

These bills and budgets all have pieces of the solution, but none provide the comprehensive reforms that we believe are necessary. We are encouraged by the efforts of the ICESA State-Federal UI/ES Reform Workgroup as it works toward consensus on a proposal that combines broader access to benefits with simplified tax collection, and administrative funding changes while focusing on putting people back to work and combating fraud and abuse. Our stakeholders, worker advocates and businesses must agree on any comprehensive reform.

The Western Governors' Association passed a resolution in December calling for reform of the National Employment Security System. We felt the need to respond to continuing the "temporary" FUTA surtax, the use of FUTA funds to offset the deficit rather than pay for employment services, and the long term under-financing of the system that has caused us to close offices. Taken together, these federal policies and laws have reduced access to and lowered local levels of service.

Western states gave a substantial commitment to job training and workforce development. Resolution 99-029 supports a comprehensive reform through federal legislation of the financing and administration of the National Employment Security System. This resolution was delivered to your committee on February 29, 2000 by my colleague, Governor Jane Dee Hull of Arizona.

The strength of a comprehensive and fully supported proposal is that it will generate the support needed for the more difficult components of reform like mandatory funding and increased access to benefits. Such a proposal must solve inadequate funding, provide additional dollars for reemployment, reduce UI tax burdens and employer filing burdens, combat fraud and abuse, and expand eligibility. We believe this is possible.

We support

1. Moving UI and ES funding to the mandatory side of the budget.
2. Fully funding the costs of administering UI and ES Services, including:
 - the baseline technological infrastructure needed to offer unemployment and re-employment services;
 - integrity activities such as collection/detection of UI overpayments and finding fraudulent employers;
 - strengthening the administration of the system by ensuring that states get a greater return on their employers' FUTA tax dollars, with greater accountability for the use of these funds;
 - a funding strategy that ensures that states with small tax bases will have administrative funds to deliver the employment security system.
 - Repealing the 0.2 percent FUTA surcharge, but only as part of a comprehensive proposal.
 - Eliminating inefficiencies experienced by employers by transferring responsibility for collecting the FUTA taxes to the states. Simplifying the UI tax process and employer reporting process.

- Increasing the states' flexibility to administer their UI and ES programs to serve the needs of their employers and workers while providing incentives.
- Improve employment services with an emphasis on re-employing dislocated workers;
- Making it clear that job search and placement services are to be provided UI claimants. States must have the resources to ensure a strong link for UI recipients to the employment services that will get them back to work. Current federal funding formulas do not reward states to fully operate these components;
- Granting access to the National Directory of New Hires to state UI overpayment detection programs—it would provide access on hiring information from multi-state employers in order to detect individuals who work while claiming UI benefits;
- Making the Directory of New Hires a more valuable tool for Child Support Enforcement and UI Programs by including the actual start-work date in reports required by employers;
- Eliminating all extended benefit special eligibility requirements including the complicated computations for eligibility and the often-penalizing work search requirements placed on these individuals during recessions;
- Providing a higher federal share of extended benefits during periods of high unemployment;
- Correcting the triggers for extended benefits so that they work;
- Eliminating in-person citizenship verification on federal UI claims;
- Enabling states to implement alternative base periods;
- Repealing the federal income tax on UI benefits, which would increase the purchasing power of UI benefits and would treat UI benefits like other wage replacement benefits such as workers' compensation;
- Expanding coverage for part-time and contingent workers. Part-time work is often not an individual's choice—but ever more typical in the changing job market with increased family obligations. Coverage for workers who are monetarily eligible but who are seeking part-time work is a valid response to current labor market realities;
- Allowing more state flexibility for payments to educational employees with a different labor market than in the past. Federal law needs to be changed to allow benefits to teachers between school years when they don't really have a guaranteed job for the next term;
- Providing effective use of federal dollars for dislocated workers in training. Federal benefits programs like Trade Readjustment Assistance (TRA) must be able to be used even when state-funded benefit programs are available.

We can not support:

- Requiring states to adopt 400 times the minimum wage as the workforce attachment threshold. A minimum threshold based on wages penalizes low-wage workers. Since 1977, Washington State has used the best measure of workforce attachment—hours worked. It is independent of wage level and determines the amount of work—the true attachment to the labor force. Oregon is also now using an hours threshold as an alternative test for UI eligibility, following discussions with Washington State on the effectiveness of using hours as a true consideration of an individual's attachment to the labor force. If there is a need to set a national threshold, set it at 400 hours of employment which would allow more hardworking, low earning workers to qualify for benefits.
- Shifting to monthly tax reporting. This would triple the burden on employers and the administrative costs of processing taxes.
- Standalone repeal of FUTA surtax. This repeal is important, but only as a part of a comprehensive reform.

We are still considering:

- Offering incentives to states to maintain recession-proof balances in their trust fund. In the event of economic downturns, when states use their funds the most, incentive-based funds would be non-existent since Average High Cost Multiples would drop below targeted levels.

Our state has a strong interest in a strong UI program. Our legislature has authorized several studies of the Unemployment Insurance system in Washington State in the coming year. We are ready for federal help with reforms that make will our system more effective.

The time is right. The partners are at the table. Comprehensive reform is possible. We agree with Chairman Johnson that we must improve and strengthen the system to meet the increasingly complex needs of our workforce. We look forward to working with you and the Department of Labor, our federal partners, as well as our stakeholders, to make informed public policy that will guide the UI system into the 21st century. Thank you for the opportunity to provide comment on this important subject.

Statement of Western Governors' Association, Denver, Colorado

A. BACKGROUND

1. The National Employment Security System has been systematically underfunded for over a decade as a result of reduced Congressional appropriations and the impact of the Budget Enforcement Act and prior budget reduction legislation.

2. In 1976, Congress enacted a 0.2 percent Federal Unemployment Tax Act (FUTA) surtax as a temporary measure to fund deficits in the employment security system. These deficits were addressed long ago by this temporary measure.

3. A substantial portion of the employer-paid FUTA taxes dedicated for the purpose of employment security administration are now being collected and withheld by Congress to off-set the Federal deficit rather than expending them for the purpose they were intended.

4. Access to services and the level of services provided have declined as a result of this under-financing of the employment security system. For example, a number of states have had to close employment services offices resulting in both employers and workers not receiving the services they paid for and need.

5. Inadequate administrative funding has hindered states' abilities to provide job search assistance to help more claimants return to work. This has resulted in additional benefit payments to these claimants.

6. As a result, states have been forced to assume these administrative costs in ways that essentially tax employers twice for services that should be paid for from the FUTA revenues already paid by employers.

7. Inadequate administrative funding has undermined the ability of state administrators to fully maintain the integrity of the system, leading to unnecessary program inefficiencies.

8. Employers are burdened by having to make separate federal and state unemployment tax filings.

9. Western governors have made a substantial commitment to job training and work force development within their states.

B. GOVERNORS' POLICY STATEMENT

1. Western governors support reforming through federal legislation the financing and administration of the National Employment Security System. These reforms should:

- Reduce the tax burden placed on large and small businesses by repealing the unnecessary and "temporary" 0.2 percent FUTA surtax, thereby cutting FUTA taxes to 0.6 percent.
- Develop a funding strategy that utilizes the FUTA tax dollars for their intended purpose and adequately funds the employment security system.
- Preserve the protections for workers and more adequately address the needs of the workers.
- Eliminate the inefficiencies experienced by employers by transferring responsibility for collecting the FUTA tax to the states.
- Strengthen the administration of the system by ensuring that states get a greater return on their employers' FUTA tax dollars and ensure greater accountability for the use of these funds.
- Improve employment services with an emphasis on re-employing dislocated workers.
- Combat fraud and abuse in the present system.
- Increase the states' flexibility to administer their unemployment insurance and employment services programs to serve the needs of their employers and workers.
- Develop a funding strategy that ensures that states with small tax bases will have administrative funds to deliver the employment security system.

C. GOVERNORS' MANAGEMENT DIRECTIVE

1. The Western Governors' Association shall transmit a copy of this resolution to the President, the Office of Management and Budget, the Secretary of Labor and the chairman and ranking minority member of the Senate Finance, Budget and Health, Education, Labor and Pensions committees, and to the chairman and ranking minority member of the House Ways and Means, Budget and Education and Workforce committees.

Approval of a WGA resolution requires an affirmative vote of two-thirds of the Board of the Directors present at the meeting. Dissenting votes, if any, are indicated

in the resolution. The Board of Directors is comprised of the governors of Alaska, American Samoa, Arizona, California, Colorado, Guam, Hawaii, Idaho, Kansas, Montana, Nebraska, Nevada, New Mexico, North Dakota, Northern Mariana Islands, Oregon, South Dakota, Texas, Utah, Washington and Wyoming.

