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BY THE COMPTROLLER GENERAL

# Report To The Congress

OF THE UNITED STATES

# Unemployment Insurance--Inequities And Work Disincentives In The Current System


Unemployment insurance protects workers who lose their jobs However, the program has not kept up with social and economic changes, such as increases in taxes, retirement income, and work-related expenses As a result, many recipients of unemployment compensation lose little income when they become unemployed These persons are more likely to

be unemployed longer although jobs similar to their last one are often available,

exhaust compensation, and

quit their most recent jobs

This report offers several possible ways for the Congress to modify the program so that recipients will be treated more equitably and have a better financial incentive to work GAO's views generally differ from those of the Department of Labor





HRD 79 79

AUGUST 28, 1979

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D C 20548

B-133182

To the President of the Senate and
the Speaker of the House of Representatives

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This report discusses the inequities and work disincentives in the current system of unemployment compensation. We made our review to see whether unemployment compensation recipients who replaced a large part of their previous income stayed out of work longer than those who replaced a smaller part of previous income.

This report urges the Congress to consider--as possible solutions to inequities and disincentives in the program--including compensation in taxable income, reducing compensation by retirement income, and establishing a uniform methodology for determining compensation.

Copies of this report are being sent to the Director, Office of Management and Budget, and the Secretary of Labor.

John D. Heller
ACTING Comptroller General
of the United States

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COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

# UNEMPLOYMENT INSURANCE-- INEQUITIES AND WORK DISINCENTIVES IN THE CURRENT SYSTEM

## D I G E S T


Unemployment insurance is a Federal-State program enacted in 1935 under the Social Security Act. The program was established to provide a temporary income to unemployed workers and to help stabilize the economy by maintaining the purchasing power of laid-off workers. In 1978 about 8 million people received $9.7 billion in compensation. The Federal Government paid about 11 percent of this amount, and the States paid the balance. During periods of high unemployment, the Federal share has been nearly half because of special federally funded programs and loans to the States. (See pp. 1 and 2.)

States normally pay 26 weeks of compensation, but during periods of high unemployment, they pay an additional 13 weeks. Weekly compensation in most States is half of a recipient's average weekly gross wage before becoming unemployed, up to a maximum limit. (See pp. 1 to 3.)

LIMITED FINANCIAL INCENTIVE TO WORK

GAO's interviews with 3,000 persons receiving unemployment compensation showed that compensation, either alone or combined with other income, replaced an average of 64 percent of a recipient's net income before unemployment. About 25 percent of these persons replaced over 75 percent of their net income, and about 7 percent replaced over 100 percent. (See p. 6.)

Persons who replaced over 75 percent of their net income before unemployment

--collected compensation over 2 weeks longer than those who replaced 75 percent or less,

--were more apt to exhaust compensation,

--were nearly twice as likely to have quit their most recent jobs, and

--generally had held jobs similar to ones listed by the Employment Service and local newspapers.

Further, nearly 30 percent of those who replaced over 75 percent of their net income told GAO they had only a limited financial need to work. These factors indicate that some persons receiving compensation are not financially motivated to work. (See pp. 8 to 10.)

## FACTORS LIMITING FINANCIAL INCENTIVE TO WORK

Social and economic changes occurring since the program began have reduced recipients' financial incentive to work.

### 1. Increased taxes on workers' income

Increases in Federal, State, and local income taxes and social security taxes since the 1930s have reduced the amount of take-home pay and resulted in a significant gap between gross and net income. The Federal income tax was primarily limited to high income families in the 1930s, but today most workers pay income taxes. State and local personal income taxes have increased by over 500 percent in the past 25 years. Social security taxes have increased by over 600 percent since the early years of the program. Because unemployment compensation is based on gross income, the increased taxes have resulted in unemployment compensation replacing a higher percentage of take-home pay. Unemployment compensation was not taxed until 1979 and is now taxed only at high income levels. (See p. 15, 16, and 23.)

2. <u>Unemployment compensation may be supplemented by retirement income</u>

Retirement income, such as social security, private, and military pensions, when combined with unemployment compensation, minimizes some recipients' financial incentive to work. Some States do not reduce compensation by the amount of retirement income. (See pp. 16 and 17.)

3. <u>Reduced expenses during unemployment</u>

The absence of work-related expenses during unemployment also increases the net value of unemployment compensation. Such expenses as transportation and child care, although quite high while a person works, are substantially lower or nonexistent during unemployment. Over 75 percent of the persons GAO interviewed had work-related expenses, excluding child care, averaging $17 per week. About 10 percent had child care expenses, which averaged $26 per week. However, less than 3 percent had child care expenses while unemployed. (See p. 17.)

4. <u>Unequal computation of unemployment benefits</u>

Among the States, no uniform methodology exists for determining the compensation a recipient is entitled to receive. For example, States use different time periods for determining claimants' average weekly wage, the basis for computing compensation. Some States pay additional compensation for dependents, while others do not. As a result, recipients in the same circumstances receive different compensation entitlements and therefore can have varying financial incentives to seek work. (See pp. 18 to 22.)

## RECOMMENDATIONS TO THE CONGRESS

GAO believes the evidence presented in this report strongly warrants congressional action to assure that all unemployment compensation recipients have adequate work incentives and benefit more equitably from the program. The Congress should consider the following as possible solutions to the inequities and disincentives in the program:

--Including unemployment compensation in taxable income.

--Reducing unemployment compensation by retirement income.

--Establishing a uniform methodology for determining compensation. (See pp. 23 to 26.)

Taxing compensation would reduce the percentage of income replaced during unemployment. This would also help to eliminate a situation whereby compensation is more valuable to some recipients than to others. Currently, recipients with working spouses benefit more from the tax-free nature of unemployment compensation. These recipients have higher family earnings, and they are in higher income tax brackets than similar recipients who are sole wage earners. (See pp. 23 and 24.)

Reducing unemployment compensation by retirement income lessens the percentage of income replaced. If the portion of retirement income contributed by an employer is deferred income, one could argue that the employer's share, at least, should be treated no differently than current earned income, such as part-time wages. All States but one reduce compensation by a portion of a claimant's part-time earnings. However, States are not consistent in their treatment of retirement income. Some offset retirement income, while others do not. (See pp. 24 to 26 .)

In an April 5, 1978, report (HRD-78-1), GAO recommended that the Congress establish a uniform methodology for determining compensation so that all recipients are treated equally. Lack of uniformity also affects a recipient's financial incentive to accept employment. (See p. 26.)

The National Commission on Unemployment Compensation is studying these issues and has expressed certain views in its November 1978 Interim Report. For example, the Commission is uncertain what impact taxing compensation may have. The Congress should consider both the Commission's and GAO's views in changing the program. (See pp. 23 to 26.)

The Department of Labor said this report contains major methodological weaknesses which lead to unwarranted policy recommendations. GAO disagrees for the reasons discussed at the end of chapters 2 and 3. (See pp. 10 and 26.)

# Contents

## ABBREVIATIONS

| | |
|---|---|
| GAO | General Accounting Office |
| UC | unemployment compensation |

# CHAPTER 1

# INTRODUCTION

Unemployment insurance was established in 1935 as part of the Federal-State employment security program authorized under the Social Security Act (42 U.S.C. 501) and the Wagner-Peyser Act (29 U.S.C. 49). The primary objective of unemployment insurance is to insure most workers against lost wages by providing temporary compensation for those who lose their jobs. The program also helps stabilize the economy by maintaining some purchasing power of laid-off workers and establishes economic incentives to encourage employers to maintain steady employment levels.

The Department of Labor's Employment and Training Administration administers the employment security program, which provides (1) employment services and (2) unemployment compensation (UC). Within the Employment and Training Administration, the Unemployment Insurance Service establishes performance standards and provides guidance and technical assistance to the 50 States, the District of Columbia, and Puerto Rico. The States 1/ operate about 1,700 local unemployment insurance offices.

## UNEMPLOYMENT INSURANCE PROGRAMS

States normally provide 26 weeks of compensation. An additional 13 weeks is provided under the Extended Benefits program during periods of high unemployment. This program was established by the Federal-State Extended Unemployment Compensation Act of 1970 (Public Law 91-373, title II; 26 U.S.C. 3304 note).

Other Federal programs that provide compensation to specific groups of unemployed workers are:

--Unemployment compensation programs for Federal civilian employees and veterans.

--Trade Adjustment Assistance for workers who are unemployed because of the adverse effects of imports.

--Disaster Unemployment Assistance for individuals whose employment is terminated because of a natural disaster.

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1/Includes District of Columbia and Puerto Rico.

## FUNDING

The unemployment insurance program is financed by Federal and State taxes paid by employers. The Federal tax rate is currently 3.4 percent of the first $6,000 of an individual's earnings from employers covered by the Federal Unemployment Tax Act (26 U.S.C. 3301). The law provides a 2.7-percent credit against the 3.4-percent Federal tax--an effective Federal tax rate of 0.7 percent--to employers who pay State unemployment taxes under programs approved by the Secretary of Labor.

State unemployment taxes are deposited in each State's trust fund, and they are used for the first 26 weeks of compensation and half of the cost of Extended Benefits. Federal taxes are deposited in various Federal unemployment accounts, which are collectively called the Unemployment Trust Fund. This fund, which is administered by the Federal Government, is used to (1) pay all administrative costs of the program, (2) pay one-half of Extended Benefits, and (3) maintain a loan fund from which States may borrow to pay compensation if their trust fund accounts become insolvent. Other Federal programs that provide compensation for specific groups of unemployed workers are financed by Treasury general funds.

UC payments increased dramatically in the mid-70s. During the program's first 32 years, $51.2 billion was paid in compensation; from 1970 through 1978, $84.2 billion was paid. In 1978 an estimated 8 million recipients received $9.7 billion in compensation. The percentage of costs borne by the Federal Government has ranged from nearly 50 percent in 1976 to about 11 percent in 1978, with the States paying the balance. The Federal share increases during periods of high unemployment, such as in 1976 due to the Extended Benefits program, two federally funded supplemental programs, and Federal loans to insolvent State funds.

Total Compensation Paid

| | (billions) |
|---|---|
| 1938 - 1969 | $ 51.2 |
| 1970 | 4.2 |
| 1971 | 6.1 |
| 1972 | 6.0 |
| 1973 | 4.5 |
| 1974 | 6.9 |
| 1975 | 18.1 |
| 1976 | 16.2 |
| 1977 | 12.5 |
| 1978 | 9.7 |
| Total | $135.4 |

Employer taxes have not kept up with compensation payments. Many States have borrowed from the Federal Government to maintain the solvency of their funds. As of February 28, 1979, 18 States owed $5.1 billion. Also, the Federal Unemployment Trust Fund has been depleted, necessitating the borrowing of $13.7 billion (as of Dec. 31, 1978) from Treasury general funds.

## COMPENSATION AMOUNTS

The Social Security Act allowed each State to set UC eligibility standards and amounts. Federal legislation did not mandate that UC replace a specific percentage of lost wages. However, most States adopted laws that make weekly compensation equal to 50 percent of a recipient's average weekly gross wage but restricted compensation amounts to State-set maximums. The States' decisions were apparently based on the Wisconsin unemployment compensation law, the first in the Nation when enacted in January 1932. A former director of the Wisconsin State Employment Security Agency, explaining the rationale for the 50-percent rate, indicated that for public acceptance the rate had to be less than that for workmen's compensation and not high enough to encourage malingering.

Today, most State laws still provide compensation equal to 50 percent of a recipient's average weekly gross wage. Nine out of 10 States in our review provided compensation on this basis. The other State provided compensation equal to 60 percent of a recipient's average weekly gross wage.

## SCOPE OF REVIEW

Our review was made primarily at State agency headquarters and selected local offices in 10 States--California, Connecticut, Florida, Georgia, Michigan, Nevada, New Mexico, Ohio, Texas, and Vermont. These States were selected to provide a broad geographic representation of urban and rural areas, different unemployment rates, and different claimant populations. At least two local unemployment offices were visited in each State. (See app. I.)

We interviewed 3,000 compensation recipients (300 in each State) during February, March, and April 1978 to evaluate their financial incentives to work. We randomly selected the recipients as they reported to the unemployment office to either pick up their checks or report their job search efforts. Appendix II compares the characteristics of these 3,000 recipients with the national insured unemployed population. We later contacted 2,785 recipients 1/ through a followup questionnaire, about 3 months after the interview, to obtain data on their employment status. About 2,100 recipients (nearly 75 percent) responded.

While interviewing recipients at local offices, we reviewed job openings listed with the Employment Service and in local newspapers to determine the availability of jobs and labor market conditions. We also contacted 92 employers in the 10 States to determine whether they had experienced any difficulty in filling job vacancies.

We analyzed UC computation provisions in all 50 States, the District of Columbia, and Puerto Rico to determine how a State's method for computing compensation affects the amount of replaced income and a recipient's incentive to seek work. In this regard, we developed 100 hypothetical cases and asked the States to compute each claimant's compensation.

We interviewed several researchers in unemployment insurance. In addition, we spoke with Labor headquarters and regional officials and State Employment Security Agency officials in 10 States and reviewed legislation and regulations related to the unemployment insurance program.

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1/Followup questionnaires were not sent to 215 recipients because they did not give us their addresses.

RELATED REPORTS

Following is a list of other GAO reports pertaining to the employment security program.

1. "Unemployment Insurance--Need to Reduce Unequal Treatment of Claimants and Improve Benefit Payment Controls and Tax Collections," HRD-78-1, April 5, 1978.

2. "The Employment Service--Problems and Opportunities for Improvement," HRD-76-169, February 22, 1977.

3. "Evaluation of Comments on Report on Problems in Filling Job Orders and Placing Job Applicants in Massachusetts," MWD-75-49, January 23, 1975.

4. "Problems in Filling Job Orders and Placing Job Applicants in Massachusetts," B-179083, October 30, 1974.

## CHAPTER 2

## UC RECIPIENTS OFTEN HAVE LITTLE FINANCIAL INCENTIVE TO WORK

Based on a sample of 3,000 recipients, we found that compensation, either alone or combined with other income, replaced an average of 64 percent of a recipient's net income before unemployment. About 25 percent of these recipients replaced over 75 percent of their net income, and about 7 percent replaced over 100 percent.

Recipients who replaced over 75 percent of their net income before unemployment collected compensation over 2 weeks longer than those who replaced 75 percent or less. Recipients who replaced over 75 percent of their net income were also more apt to use all their compensation and were nearly twice as likely to have quit their most recent jobs. Further, these recipients generally had occupations similar to jobs listed by the Employment Service and local newspapers, and nearly 30 percent stated that they had only a limited financial need to work.

As discussed in chapter 3, social and economic changes have occurred since 1935, but the unemployment insurance program has not adjusted to them. For example, States do not consider the increased impact of taxes on an individual's take-home pay; they still base compensation on gross wages. Although pensions have become more common, many States do not consider them in computing compensation. This lack of change has enabled some recipients to replace a much higher percentage of their prior net income than they would have in the 1930s and 1940s. Chapter 3 also describes several alternatives for the Congress to consider in updating the unemployment insurance program.

### METHODOLOGY FOR DETERMINING REPLACED NET INCOME

While interviewing 3,000 UC recipients, we obtained financial data that enabled us to compare a recipient's total net income 1/ just before unemployment to total

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1/Net income consists of wages, social security income, pensions, welfare, veterans' benefits, alimony, child support, etc., after social security and Federal, State, and local income taxes.

net income, including UC, available during unemployment. Recipients also provided information on their work-related expenses, consisting primarily of transportation costs and child care. Because these expenses are not generally incurred during unemployment, they were deducted from net income before unemployment so that a more meaningful comparison of incomes could be made.

For our analyses, recipients who replaced over 75 percent of their prior net income after work-related expenses comprised the "higher income replacement group," and those who replaced 75 percent or less formed the "lower income replacement group." UC is generally intended to replace 50 percent of prior gross income, but we established 75 percent of net income as a cutoff for our analyses. An analysis based on net income is more meaningful because of the wide disparity between gross and net income, a situation that did not exist at the start of the program. Although several factors, such as learning new skills, gaining experience in a job, and maintaining one's self-respect, often affect a recipient's desire to work, we believe that, as the percentage of replaced income increases, a recipient's financial incentive to work decreases.

## MANY RECIPIENTS LOSE LITTLE INCOME

For many UC recipients, unemployment results in a small loss of net income. The 3,000 recipients we interviewed replaced an average of 64 percent of prior net income. Nearly 25 percent replaced over 75 percent of prior income, while about 7 percent replaced over 100 percent. The following table shows the number and percent of recipients by percentage of net income replaced.

| Percent of net income replaced | Number of recipients | Percent of recipients |
|---|---|---|
| 30 and below | 188 | 6.2 |
| 31-40 | 300 | 10.0 |
| 41-50 | 435 | 14.5 |
| 51-60 | 572 | 19.1 |
| 61-75 | 776 | 25.9 |
| 76-90 | 381 | 12.7 |
| 91-100 | 131 | 4.4 |
| Over 100 | 217 | 7.2 |
| Total | 3,000 | 100.0 |

## RECIPIENTS WHO LOSE LITTLE INCOME COLLECT LONGER

Recipients whose net income is not significantly reduced by unemployment collect UC longer. A total of 2,082 responded to the followup questionnaire that we sent about 3 months after the interviews. Of these, 499 were still collecting UC and 1,583 were not. For those who were not, we were able to determine that 1,479 had collected UC for an average of 19.8 weeks. Those who replaced less than 75 percent of their net income collected for an average of 19.3 weeks, whereas those who replaced more collected an average of 21.4 weeks, or 2.1 weeks longer. As shown by the following table, in general, as the percentage of replaced income increased, so did the length of time recipients collected UC.

| Percent of net income replaced | Number of recipients | Percent of recipients | Average number of weeks UC received |
|---|---|---|---|
| 30 and below | 95 | 6.4 | 16.5 |
| 31-40 | 158 | 10.7 | 19.1 |
| 41-50 | 237 | 16.0 | 19.3 |
| 51-60 | 254 | 17.2 | 19.2 |
| 61-75 | 388 | 26.2 | 20.1 |
| 76-90 | 180 | 12.2 | 20.3 |
| 91-100 | 68 | 4.6 | 22.8 |
| Over 100 | 99 | 6.7 | 22.3 |
| Total | 1,479 | 100.0 | 19.8 |

## EXHAUSTEES ARE MORE PREVALENT IN THE HIGHER INCOME REPLACEMENT GROUP

Recipients who replaced a high percentage of prior net income were more likely to use all of their compensation. Of the 1,583 recipients who stopped collecting, 656 (41.4 percent) exhausted their compensation. Exhaustees accounted for 39.3 percent of the recipients in the lower income replacement group (479 of 1,218) and 48.5 percent of the higher group (177 of 365).

Data obtained from the followup questionnaire indicate that many of the exhaustees may not have been actively pursuing employment while collecting UC. Ninety stated they were not seeking employment because they were retired or students or for other undisclosed reasons. Of the exhaustees who returned to work, most did so within 4 weeks of exhausting their UC.

## RECIPIENTS WHO QUIT JOBS ARE MORE PREVALENT IN THE HIGHER INCOME REPLACEMENT GROUP

Individuals who lost little income because of unemployment were more apt to have quit their most recent jobs than individuals whose unemployment resulted in a major income loss. Overall, 411 (13.7 percent) of the 3,000 recipients interviewed quit their jobs. In the lower income replacement group, 11.2 percent of the recipients quit their jobs; in the higher group, 21.4 percent quit.

We recognize that all States disqualify claimants who voluntarily quit their jobs without cause. Some States disqualify them for a variable number of weeks, others for a fixed number of weeks, and still others for the duration of unemployment. However, some recipients in States using each of these methods told us they quit their jobs. This could have been true for one of several reasons.

- --Some claimants and their employers may not have informed the unemployment office that they had quit; therefore, they were considered to have been laid off and thus eligible for UC.

- --Some may have satisfied the disqualification period.

- --Some may have quit for good cause and thus were not disqualified.

## JOBS WERE AVAILABLE FOR MANY RECIPIENTS

Three of our prior reports 1/ showed that many UC recipients who registered with the Employment Service were not referred to jobs for which they were qualified. Furthermore, our February 1977 report showed that the Employment Service was far more successful in finding jobs for people who were not collecting compensation than for those who were. The Department of Labor's statistics also showed that, during fiscal year 1977, the Employment Service was nearly twice as successful in finding jobs for people who were not collecting compensation.

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1/The first, second, and fourth reports listed on page 5.

During this review we compared the most recent prior occupations of UC recipients in the higher income replacement group to jobs listed by the Employment Service and local newspapers. About 65 percent of the recipients in the higher group had occupations that appeared similar to jobs listed by these sources. Although we did not identify similar job openings for the remaining 35 percent, jobs may have existed. For example, in our February 1977 report, employers identified newspapers and the Employment Service as sources for only 30 percent of their job referrals.

Whether the recipients for whom jobs were identified could have actually qualified for the positions is unknown. The existence of these jobs, however, indicates that recipients who lost little income because of unemployment may not have been actively seeking work. In fact, about 26 percent of all recipients said they had only some, very little, or no financial need to work. This percentage was slightly lower for recipients in the lower income replacement group, but increased to nearly 30 percent for those in the higher group.

### Employers and State officials believe UC reduces work incentives

Most of the 92 employers advertising jobs similar to those formerly held by recipients in the higher income replacement group told us that they experienced considerable difficulty in filling job vacancies. About 65 percent of these employers believed that UC reduces work incentives.

We asked 31 State Employment Security Agency officials whether they believed that compensation reduces work incentives. All but two believed that a significant number of recipients or certain groups of recipients lack a financial incentive to work. Secondary wage earners who collect UC were the group most frequently mentioned.

## LABOR COMMENTS AND OUR EVALUATION

Labor, in a June 8, 1979, letter (see app. V), questioned our methodology for computing income replacement rates and our sampling approach. The following section includes Labor's comments on our methodology and sampling approach, and our evaluation. Labor's comments on our recommendations and our evaluation of those comments are included at the end of chapter 3.

Labor was concerned that our report does not adequately describe the sampling and interviewing methods used and how the interview questions were worded. The scope of review section in chapter 1 outlines our sampling methods in some depth. Regarding the wording of our questions, copies of our interview document and followup questionnaire are now included as appendix IV.

Labor stated that our method for calculating a recipient's net income replacement rate was inappropriate because income other than wages was included in our analysis. Labor believes the replacement rate should be based strictly on a comparison of prior wages to compensation amounts. We disagree with Labor's approach. In our opinion, income is income regardless of its source, and a recipient's financial incentive to work can best be measured by comparing all income before unemployment to all available income, including UC, during unemployment. In the real world, people do not differentiate between income sources when evaluating their financial incentive to work.

Further, Labor stated that the same logic which suggests deducting taxes and work expenses from wages also suggests that fringe benefits foregone and job search costs should be deducted from UC when calculating replacement rates. We agree that such an analysis would be desirable. However, quantifying fringe benefits on an individual basis is very difficult. In addition, the loss of such benefits would probably not affect recipients' financial incentive to work to the same extent as the loss of available cash. Job search costs will reduce income replacement rates to the extent incurred; however, assistance toward these costs can be provided under a number of federally funded programs. To the extent that assistance is not provided, job search costs can be another disincentive for people to actively seek work.

According to Labor, the report ignored the benefit adequacy issue. One objective of unemployment insurance is to provide income protection to unemployed workers to minimize the disruption of their standards of living. Labor stated that, while the potentially negative effect of excessive benefits needs to be considered in determining benefit levels, it is vital that the adequacy of benefit levels also be considered.

We agree that the adequacy of benefits is an important issue. Our report shows that about 16 percent of the recipients replaced 40 percent or less of net income. However, our study was primarily directed toward the work incentive issue, and we did not pursue the adequacy issue. Although some recipients replaced less than 40 percent, over 7 percent replaced over 100 percent of their prior income. We agree, however, that this issue may warrant a separate study.

Labor stated that our report depends exclusively on an analysis of two variables--income replacement rate and duration of unemployment--and that any conclusion drawn from such an analysis is methodologically deficient and unsuitable for policy analysis. Labor contends that the data should have been adjusted for the effects of other variables using the multiple regression technique.

We did analyze the data using multiple regression. We used duration as the dependent variable and considered income replacement rate, age, secondary wage earner status, expected recall, and State unemployment rates as independent variables. Unfortunately, the results of the analyses did not further explain the differences in duration and therefore are not included in the report. However, we did not rely exclusively on duration to reach our conclusions. We also considered a number of other factors including those who quit their jobs, those who exhausted their benefits, and what they said about their financial incentive to work.

Labor stated that our analysis does not reflect that, beginning in 1979, UC is taxed for high income families. The present tax provisions, applying to individuals with incomes over $20,000 and couples filing jointly with incomes over $25,000, may reduce UC for many recipients currently replacing a high percentage of income.

We did consider the new tax provisions in our study, and they are discussed in chapter 3. They were not included in our analyses because they will affect only a small number of recipients. Most will not have taxable income high enough to be subject to the tax. Those that are affected will tend to have high incomes and thus replace less than 50 percent of prior earnings due to State ceilings on compensation levels. In addition, the new tax provisions will not have any impact until tax returns for 1979 are filed in 1980.

Labor stated that a response rate of 75 percent to our followup questionnaire is low enough to suggest bias in our data. We believe a response rate of 75 percent to a mail questionnaire is very high. Furthermore, we have no reason to believe that the data obtained from the questionnaire responses were biased in any way. In fact, the distribution of income replacement rates did not vary significantly when comparing our entire universe to the recipients who responded to our followup questionnaire and had stopped collecting UC. (See tables on pp. 7 and 8.)

Labor claims that the report fails to consider the inherent scarcity of employment opportunities when many recipients are unemployed. Further, Labor stated the report did not consider the "suitable" job provision of unemployment insurance. We disagree with both of Labor's comments. As noted in our report, we found that about 65 percent of the recipients in the high income replacement group had occupations <u>similar</u> to jobs listed by the Employment Service and local newspapers. Although we did not identify similar job openings for the remaining 35 percent, jobs may have existed because, as found in a prior GAO review, newspapers and the Employment Service are sources for only 30 percent of job referrals to employers.

Labor stated the analysis failed to consider the dynamic effect of unemployment insurance. Labor believes that the report should

> "* * * take into consideration the effects of the current and successive receipts of benefits on the parameters of job search decision and the feedback of these effects on the current decision."

We recognize that measuring the financial work incentive of UC recipients is a highly complex issue. But we continue to believe that the data in this report show that many recipients have a limited financial incentive to seek and accept work.

According to Labor, the report's analysis of recipients who quit their most recent jobs is ambiguous and would be clearer if these recipients had been classified according to the types of quits. We agree that this type of analysis might have been meaningful; however, we did not ask recipients to distinquish between the various types of quits.

Labor stated that the title used on a draft of this report presumed that recipients prolonged their unemployment without offering any evidence that they actually do so. We recognize the complexity involved in deciding whether or not a UC recipient prolongs unemployment even though a large percentage of prior net income is replaced. Therefore, we have changed the title on the final report to better describe the report's contents.

Labor said that the report's analysis on recipients who worked part time just prior to unemployment may not be relevant, because many people work a reduced workweek before layoff. (See p. 17.) The phrase "just prior to unemployment," as used throughout the report, relates to a 2- to 3-month period, which should be a long enough period to offset the impact of reduced workweeks just before unemployment.

Labor also stated the high incidence of part-time workers in the higher income replacement group may be largely explained by the benefit maximum. We agree with Labor. However, this does not detract from the fact that many of these recipients had little financial incentive to work.

# CHAPTER 3

## WHY DO MANY UC RECIPIENTS LOSE LITTLE INCOME, WHO ARE THEY, AND WHAT CAN BE DONE ABOUT IT?

Social and economic changes since 1935 have allowed many recipients to lose little income when receiving UC. Increases in Federal, State, and local income taxes and social security taxes have widened the gap between gross and net income. Because the UC amount is based on a recipient's average weekly gross wage, increased taxes have resulted in an even higher replacement of net wages. Therefore, these tax increases have lessened the financial effect of unemployment on UC recipients. Also, the receipt of social security income and pensions and the absence of high work-related expenses during unemployment are factors that bear on the likelihood of recipients to collect compensation rather than accept work. Finally, the lack of Federal standards for computing UC payments has affected some recipients' work incentive, depending on where they live.

### INCREASED TAXES MINIMIZE LOST INCOME

As in the early years of the program, most States still provide UC in an amount that replaces about 50 percent of a person's gross wages up to a maximum established by State law. However, increases in Federal, State, and local income taxes and social security taxes over the past 40 years have widened the gap between gross and net income. Therefore, most recipients now replace at least 60 percent of their prior net wages during unemployment.

In 1935, little or no difference existed between gross and net pay. The Federal income tax was small and limited to high income families. Twenty-seven States imposed income taxes, but the amounts were not significant. Also, the social security tax, first imposed in 1937, was only 1 percent of the first $3,000 of earnings. Overall, an average family paid between 6 and 10 percent of its income in direct taxes, and workers took home an average of 92 cents of each dollar earned. For UC recipients, compensation generally replaced about 50 percent of gross wages and not more than 55 percent of net wages.

Since 1935 taxes have increased dramatically. Now, most workers pay Federal income taxes. Also, 41 States have income tax laws covering earned income with tax rates ranging from 0.5 to 19.8 percent of adjusted gross income. In the past 25 years, State and local personal income taxes have increased by over 500 percent. Finally, employees' share of the social security tax has increased to 6.05 percent of the first $22,900 of earnings, or over 600 percent since the social security program began. As a result, workers are fortunate if they take home 82 cents of each dollar earned. Although UC still replaces about 50 percent of gross wages, due to higher taxes it tends to replace 60 percent or more of net wages. This is one reason why many recipients do not have a financial incentive to seek and accept a job. For example, one recipient told us that he had no incentive because most of the money he would earn over what he received in compensation would have to be paid in taxes. He had already collected for 25 weeks when we interviewed him, and since the Extended Benefit program was in effect, he was entitled to collect for 39 weeks.

## RETIREMENT INCOME MINIMIZES LOST INCOME

Some UC recipients also receive retirement income, such as social security, public, and private pensions, which were not generally available in 1935. This income, combined with UC, further minimizes recipients' financial need to seek employment, because many States do not offset UC by retirement income when computing the amount a claimant will receive.

Over 8 percent of all recipients we interviewed were receiving some type of retirement income. Although most were age 62 and over, some were not. Not surprisingly, these recipients were nearly six times more likely to be in the higher income replacement group. Furthermore, recipients with retirement income who stopped collecting UC and responded to our followup questionnaire collected UC for an average of 23 weeks, about 3 weeks longer than the average of all recipients who stopped collecting and responded to our followup.

Under the social security system, an eligible person at age 62 receives from $98 to $428 a month. At age 65, the minimum and maximum benefits increase to $134 and $533, respectively. After combining this income with UC, individuals who are contemplating retirement may not need to work. Further, they might not inform State UC officials of their retirement status, because persons who state they are not available for work are not eligible for UC.

During our interviews, several UC recipients who were also receiving retirement income commented on their financial incentive to work. One recipient who had collected UC for 23 weeks at the time of our interview was receiving social security and a private pension. He explained that he did not want to earn too much money, because if he did, he would lose his social security. While unemployed, this person was replacing 126 percent of prior net income. In contrast, other recipients told us they were looking for a job, but could not get one because of their age. As a result, they said they needed UC as a supplement to their pensions to maintain their standard of living.

## THE ABSENCE OF WORK-RELATED EXPENSES INCREASES THE VALUE OF UNEMPLOYMENT COMPENSATION

Although the median family income has increased over the years, so have work-related expenses. Years ago, most workers lived near their place of employment. Today, many live farther away, resulting in increased commuting time and costs. Also, child care costs have become more common, due to the increased number of multiple wage earner and single heads of household families.

During unemployment, most people no longer pay child care and other work-related expenses. As a result, the value of unemployment compensation dollars is greater than the same dollars in wages. Of the 3,000 people we interviewed, 2,267 had work-related expenses, excluding child care. These expenses, which averaged $17 per week, were not incurred during unemployment. In addition, 301 recipients had child care expenses averaging $26 per week while they were working. Only 82 recipients had child care expenses during unemployment. Clearly, the lack of work-related expenses during unemployment is another factor which might influence a recipient to collect UC rather than seek work.

## OTHER CHARACTERISTICS OF RECIPIENTS IN THE HIGHER INCOME REPLACEMENT GROUP

Of the 3,000 recipients we interviewed, 1,556 were married, of whom 888 (57 percent) had spouses who also worked. Almost two-thirds of the UC recipients with working spouses were secondary wage earners. Further, we found more secondary wage earners proportionally in the higher income replacement group than in the lower group.

Also, part-time and unskilled workers were more likely to be in the higher income replacement group. About 6 percent of all recipients we spoke with worked part time just before unemployment. While about 4 percent in the lower income replacement group worked part time before becoming unemployed, the percentage increased almost three times for recipients in the higher group. Many of the part-time workers were secondary wage earners who depended on a spouse for financial support.

Recipients previously holding unskilled jobs accounted for about 35 percent of the 3,000 we interviewed. Unskilled workers made up about 32 percent of all workers in the lower income replacement group and about 43 percent of those in the higher group. This appears logical because many unskilled workers tend to work at lower paying jobs and are usually not affected by States' ceilings on weekly compensation. This is not true for skilled or professional workers with higher earnings, whose UC might be limited by the States' maximum compensation, which is often less than 50 percent of their prior gross earnings.

## DIFFERENCES IN STATE UC COMPUTATION METHODS RESULT IN VARYING FINANCIAL INCENTIVES TO WORK

Although unemployment insurance is a joint Federal-State program, no uniform methodology exists for determining compensation amounts. In a prior report, 1/ we showed that, because of various State computation formulas to determine weekly UC amounts and various State laws regarding such matters as dependents, part-time employment, and pensions, often recipients in similar circumstances are treated differently. Differences in methodology also affect the percentage of prior wages replaced by UC.

To demonstrate the disparity in UC among States, we developed 100 hypothetical cases which represented workers with different wage histories who lost their jobs. The cases were designed to generally coincide with the proportion of married recipients, pensioners, and partial wage earners in the national insured unemployed population. The cases specified gross wages at various income levels. After Labor agreed that the cases were realistic, we sent them to all States and asked State Employment Security Agency officials to compute the compensation the individuals would be entitled to receive.

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1/The first report listed on page 5.

Our objective in developing these cases was to calculate the percentages of prior take-home pay workers would replace with UC while unemployed. In this report we have compared prior net income with UC. Because we used gross wages in the cases, we assumed a 20-percent tax rate to arrive at the net income.

In some States, individuals were not entitled to any compensation because they had not worked long enough or earned enough wages to be eligible. In other States, the same individuals replaced over 100 percent of their most recent net wages. For example, one did not qualify for UC in 43 States due to inadequate wages, but in 9 States replaced from 83 to 140 percent of his or her prior average weekly net wage.

Of the 100 individuals, the number who would qualify for UC ranged from 82 in one State to 99 in three others. Appendix III shows, for each individual, the lowest and highest percentage of prior net income replaced. The appendix also lists the number of States that denied compensation to each of the 100 individuals.

We recognize that differences exist in wage levels among States. These differences are not as significant, however, as the disparity in unemployment compensation. For example, the average weekly wage in two States was $184. Of the 100 individuals in our hypothetical cases, 85 would replace at least 10 percent more of their prior net earnings in one of these States than in the other. Using this method, we repeatedly compared different States with approximately the same average weekly wages and continued to note substantial differences in compensation for individuals with the same income.

## Different base periods result in varying amounts of compensation

To qualify for UC, an individual must have earned a specified amount of wages or worked for a certain length of time in the base period. States set different time frames for their base periods, such as the first 4 of the last 5 calendar quarters or the most recent 52 weeks. From earnings in the specified base period, most States compute an average wage for the claimants and use this figure to determine the amount of compensation they are entitled to receive. Accordingly, the disparity in UC, even for claimants with identical wages, is often the result of differences in base periods used among States. The following example shows the effect of different base periods on the percentage of income a recipient replaces:

> A worker, before unemployment, had average net earnings of $88 per week. During unemployment, this person would qualify for UC in all States. However, weekly compensation would range from $49 in one to $68 in another. This worker's earnings were higher just before unemployment. The States which provided the lower compensation amounts did not consider these more current earnings in their base period. Due to these differences in base periods, the recipient would replace from 56 to 77 percent of prior net wages, depending solely on the State in which the claim was filed.

## Dependency allowances result in varying amounts of UC

Differences in UC also result from variations in State laws providing added compensation for dependents. While 12 States add an allowance for dependent children, UC in the other 40 States is unaffected by the number of children in a family. Also, seven States pay an allowance for a non-working spouse. States which pay dependency allowances believe that a person with dependents needs a larger replacement of lost wages. States which do not pay dependency allowances argue that such benefits are not appropriate because they introduce an element of need into the program. Notwithstanding these arguments, the States are inconsistent in their treatment of recipients with dependents. The following example illustrates how the percentage of replaced income varies among the States based on whether or not they pay extra for dependents:

> Before unemployment, a person with a nonworking spouse and three children had average net earnings of $135 per week While unemployed, this worker would qualify for UC in all States, ranging from $64 to $111. With this compensation, the recipient would replace anywhere between 47 and 82 percent of prior net wages. This person would generally collect higher compensation in those States with dependency allowances, and therefore, would replace a higher percentage of prior net wages.

## Wage determination method affects weekly compensation

States use one of two systems to determine a claimant's prior wages. The method used affects the amount of weekly UC. Forty States use the wage record system, which requires employers to provide quarterly lists of all employees and wages earned. Earnings in the current quarter and the most recently completed quarter are generally not considered in computing UC. The other 12 States use the wage request system, in which wage data are obtained only when a worker applies for UC. Under this system, an employer reports the individual's earnings through the most current week of employment. This permits the States to use more current wage data to compute weekly compensation. Under a wage record system, recipients with higher wages in recent weeks would receive less UC than in most States using a wage request system.

The following example shows the effects of using the two systems to determine a recipient's UC:

> Before unemployment, a worker had average weekly net earnings of $166 during the last 2 calendar quarters; however, the worker had no earnings in the 4 quarters before this time. During unemployment, this claimant would not have sufficient wages to qualify for compensation in 36 wage record States. But UC would range from $27 to $122 in the other four wage record States and in the 12 wage request States. In 12 States, compensation would be over $100 and would replace about two-thirds of the prior net wage.

Clearly, most wage record States did not have enough current wage data for this individual to qualify for compensation.

## Treatment of partial income affects amount of UC

All States except one reduce UC for workers who are partially employed. Most States disregard some partial earnings as an incentive for recipients to work part time while seeking full-time employment. Methods used to compute UC and the amount of earnings disregarded vary among States and affect the amount of a claimant's weekly compensation, as illustrated by the following example:

A worker with two children, before unemployment, had average weekly net earnings from a full-time job of $121. During unemployment, the worker would be entitled to collect UC in all but seven States, even though net earnings from a part-time job were $60 per week. Weekly UC in the 45 States would range from $9 to $91. UC, when added to partial net earnings, would replace between 57 and 125 percent of prior net wages.

## Treatment of retirement income affects UC amounts

States treat retirement income differently when computing unemployment compensation. Some States reduce UC if retirement income is being received; others do not. Some reductions are partial; others are dollar for dollar. Procedures also vary depending on whether the retirement income is from a private, military, or Federal civil service pension, or from social security. The following example illustrates how a recipient may have a reduced financial incentive to seek work in States that do not reduce compensation by the amount of social security income:

> Before unemployment, a worker had average weekly net earnings of $248. During unemployment, this person received a social security income of $91 per week and applied for UC. While social security income would eliminate UC in three States, UC in the other 49 States would range from $9 to $160. By combining compensation with social security income, this recipient would replace anywhere from 40 to 101 percent of prior net wages.

Although UC is now reduced by retirement income in some States, the Unemployment Compensation Amendments of 1976 (Public Law 94-566; 26 U.S.C. 3304 note) mandate that it be reduced dollar for dollar in all States, effective October 1, 1979. Section 3304 (a) of the Internal Revenue Code of 1954 was amended to extend this date to March 31, 1980. Implementation is uncertain however, because the National Commission on Unemployment Compensation is required to study the issue and make recommendations. The Commission, established in February 1978, is scheduled to issue its final report in 1980.

## CONCLUSIONS

Changes are needed in the unemployment insurance program to assure that recipients have a financial incentive to actively seek and accept work. Presently, many recipients do not seek employment, and they are more likely to collect compensation longer and quit their jobs. Measuring the financial incentives of prospective job seekers is highly subjective, but we believe the evidence presented in this report strongly warrants congressional action to assure that all UC recipients have adequate work incentives and benefit equitably from the program.

## RECOMMENDATIONS TO THE CONGRESS

We recommend that the Congress consider the following possible solutions to existing inequities and disincentives in the program.

### Include UC in taxable income

The original decision to make UC nontaxable income was not part of any legislation, but the result of a 1938 Internal Revenue Service ruling. Because relatively few people were subject to Federal income taxes in 1938, the exclusion was a matter of administrative convenience with little economic impact. The situation today, however, is much different because most workers pay taxes.

To give recipients an incentive to seek employment and treat UC consistent with unemployment benefits paid in private plans, the Congress passed the Revenue Act of 1978 (Public Law 95-600). This act revised the tax exempt status of UC for a small percentage of the recipients. Compensation will be taxed if adjusted gross income exceeds $25,000 for those married, filing jointly; $20,000 for single taxpayers; and, regardless of income, for those married, filing separately. The act becomes effective in 1979, and it will be reflected in tax returns filed by April 15, 1980.

The National Commission on Unemployment Compensation, in its November 1978 Interim Report, expressed concern about the long-range implications of this legislation. For example, the Commission believed that, while taxation might increase equity among some groups of workers, it would decrease equity among others, particularly seasonal workers. Also, the Commission felt that taxing UC shifted the image and mission of the program away from a wage insurance system. The Commission did not state its rationale for these concerns or include any supporting data in its report. Instead, it recommended that the Congress delay the effective date of the act until the Commission studied the issues further.

We believe including UC in taxable income has merit both in increasing equity and in providing recipients with a financial incentive to work. When compensation is nontaxable, recipients in a high tax bracket benefit more from the tax-free nature of UC than recipients in a lower tax bracket. Further, recipients with working spouses benefit most from this inequity. As one of two workers in the family, these recipients would normally be in a higher tax bracket than if they were sole wage earners.

Recipients in our sample who were not married had an average weekly net wage of $155 before unemployment. Married recipients in single wage earner families averaged $206 net before unemployment, while recipients and their working spouses averaged $332 net before unemployment. Using the standard deduction and one exemption for unmarried recipients and two exemptions for married recipients filing jointly, the Federal annual income tax rates for these three groups of recipients would be 11 percent, 9 percent, and 15 percent, respectively. Accordingly, the married recipient and working spouse who pay 15 percent of their income in Federal income taxes benefit more from the nontaxable status of UC than does the married, sole wage earner recipient who pays 9 percent. This inequity is significant because almost one-third of all recipients and about one-half of the married recipients in our sample had working spouses.

In addition to the equity issue, taxing UC reduces the percentage of income replaced and increases recipients' incentive to seek employment. The decision of whether or not to tax UC is complicated and has different ramifications for different classes of tax filers. The National Commission on Unemployment Compensation is studying the potential effects of taxing. In light of the equity and incentive advantages of taxing UC, we believe the Congress should also consider the effect of expanding the act's coverage to include recipients at all income levels.

<u>Reduce UC by retirement income</u>

In many States, UC is not reduced by the amount of pensions, social security, or other retirement income a person receives, while in other States, it is. As a result, recipients who receive retirement income and reside in States which do not reduce UC, replace a higher percentage of prior wages.

Persons who continue working after receiving their retirement income and then become unemployed are in a different situation from persons who stop working at the time they become eligible for retirement income. Many of the latter group are going to retire regardless of job availability and will likely go on collecting UC until they exhaust their benefit entitlement. Members of the former group will likely have more labor force attachment.

The Unemployment Compensation Amendments of 1976 (Public Law 94-566) contain a provision that would require all States to reduce UC by the amount of a recipient's retirement income. The effective date of this legislation was originally January 1, 1978, but was extended to March 31, 1980, so that the National Commission on Unemployment Compensation could study the issue and provide recommendations.

The Commission, in its First Interim Report (November 1978), recommended repealing the retirement income offset because it would introduce a form of "needs" test to a program based on the insurance concept. The Commission believed that pension payments are not simply a substitute for current lost wages, but a fringe benefit accrued over a person's entire career. Further, it was concerned that recipients who receive income, such as interest and dividends, would not have their benefits reduced. The Commission also believed that the issue of offsetting retirement income is currently not within the scope of policy determination at the Federal level.

We believe that, if retirement income is considered to be deferred wages, one could argue that the portion contributed by the employer (50 percent in the case of social security) should be treated no differently than current earned income, such as part-time wages. All States but one reduce compensation by a portion of a claimant's part-time earnings. However, the States are not consistent in their treatment of retirement income. Some offset retirement income, while others do not.

The Commission argues that retirement income should be treated similarly to a recipient's less obvious income, such as interest and dividends. We believe a similar analogy can be made by comparing retirement income to part-time earnings, and thus offsetting it.

We recognize that States have traditionally determined UC policy. However, changes in economic conditions over the years have resulted in a substantial increase in the number of recipients with retirement income. This income reduces recipients' incentive to work. Accordingly, the Congress should determine the Federal role in setting UC policy. In this regard, the precise rule on retirement income that should be mandated is a complex matter. Although we recommend that all retirement income be deducted in computing UC, the Congress may want to consider the different ways that retirement income is treated by the States in setting this policy.

### Uniform methodology for determining compensation amounts

In a prior report 1/ we recommended that the Congress establish a uniform methodology for determining compensation amounts, so that all recipients are treated equally. An example of unequal treatment is the variation in the handling of retirement income. Because the lack of a uniform methodology also affects a recipient's incentive to seek employment, this is another reason the Congress should consider this recommendation.

## LABOR COMMENTS AND OUR EVALUATION

Labor agrees, in principle, that taxing UC would be more equitable. However, because taxing would reduce compensation, Labor believes that any new taxation proposal should ensure that adequate benefits be provided. As noted in our report, we believe the decision of whether or not to tax UC is complicated and its ramifications vary for different taxpayers. For recipients with high income replacement rates, taxing UC would obviously increase their incentive to work. Those with low income replacement rates tended to have higher previous incomes, and should be subject to taxation on an equity basis, i.e., in accordance with the progressive nature of U.S. tax laws. As discussed in our evaluation of Labor's comments in chapter 2, the subject of benefit adequacy may warrant a separate study.

Labor does not agree that UC should be reduced by retirement income, but does not state the basis for its objection. Further, Labor believes no action should be taken until the National Commission on Unemployment Compensation studies this issue and makes legislative recommendations. We agree that the Congress should consider the Commission's views, along with our own, in arriving at any decisions on this subject.

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1/The first report listed on page 5.

Labor does not agree that the Congress should establish a uniform methodology for determining compensation amounts. According to Labor, the variations in compensation formulas and other State UC provisions do not always lead to the inequitable treatment of recipients. Labor cites the fact that States differ in their industry, demographic mix, and other economic conditions which are closely associated with what a given amount or duration of compensation means to a recipient. Labor states that factors determining the compensation formula, such as the high quarter earnings fraction and minimum and maximum weekly compensation amounts, should logically vary according to the States' cost of living or other unique economic factors. Also, economic activities in some States may be characterized by industry mixes and occupational compositions that are inherently more vulnerable to cyclical and/or trend changes than those in other States. In these States, therefore, longer potential compensation duration may be needed to equalize the chance of finding suitable jobs.

We agree with Labor that minimum and maximum compensation levels should vary by State based on economic considerations. However, the actual factors used as the basis for computing compensation, such as determination of base period wages, dependency allowances, method of wage determination (wage record versus wage request), and treatment of partial and retirement income, should be standardized. Labor's comments do not address these issues, which are the real basis for determining compensation amounts.

APPENDIX I

## LOCATIONS OF LOCAL OFFICES REVIEWED

California
- Sacramento
- San Francisco

Connecticut
- Hartford
- New Haven

Florida
- Hollywood
- Tallahassee

Georgia
- Atlanta
- Decatur
- East Point
- Marietta

Michigan
- Detroit
- Sterling Heights

Nevada
- Las Vegas
- North Las Vegas
- Reno

New Mexico
- Albuquerque
- Santa Fe

Ohio
- Columbus
- Dayton

Texas
- Dallas
- Fort Worth

Vermont
- Burlington
- St. Albans

## COMPARISON BETWEEN GAO SAMPLE RECIPIENTS AND THE NATIONAL INSURED UNEMPLOYED POPULATION

| | GAO sample--3,000 recipients | | National insured unemployed population (note a) | |
|---|---|---|---|---|
| | | (percent) | | (percent) |
| Sex | Male | 61 | Male | 63 |
| | Female | 39 | Female | 37 |
| Race | White | 71 | White | 80 |
| | Other | 29 | Other | 14 |
| | | | Information not available | 6 |
| Age | Under 22 | 10 | Under 22 | 11 |
| | 22-61 | 83 | 22-59 | 78 |
| | 62 and over | 7 | 60 and over | 10 |
| | | | Information not available | 1 |
| Skill level of most recent job | Professional | 18 | | |
| | Skilled | 47 | (b) | |
| | Unskilled | 35 | | |
| Recipient's average take-home pay before unemployment | $169 per week | | (b) | |
| Average weekly compensation | $79.66 | | $76.81 | |
| Other income during unemployment | Pension | 8 | | |
| | Veterans' benefits | 2 | (b) | |
| | Welfare | 1 | | |
| Marital status during unemployment | Single | 31 | | |
| | Married | 52 | | |
| | Divorced or separated | 14 | (b) | |
| | Widowed | 3 | | |
| Married recipients who had working spouses during unemployment | Yes | 57 | | |
| | No | 43 | (b) | |

| | GAO sample--3,000 recipients | | National insured unemployed population (note a) |
|---|---|---|---|
| | (percent) | | (percent) |
| Spouse's take-home pay during recipient's unemployment | $168 per week | | (b) |
| Wage earner status before unemployment | Primary wage earner | 81 | (b) |
| | Secondary wage earner | 19 | |
| Average weeks collected compensation (note c) | 20 weeks | | 18 weeks (est.) |
| Number of weeks collecting compensation (note c) | Less than 15 weeks | 34 | (b) |
| | 15-25 weeks | 43 | |
| | Over 25 weeks | 23 | |

a/Represents most recent data available (1977).

b/Information not compiled by the U.S. Department of Labor.

c/For those who were no longer collecting compensation at the time of our followup.

LOW AND HIGH NET WAGE REPLACEMENT

PERCENTAGES FOR 100 HYPOTHETICAL CASES

| GAO case number | Wage replacement percentage--range (note a) | Number of States individual ruled ineligible |
|---|---|---|
| 001 | 63 - 219 | 23 |
| 002 | 63 - 145 | 11 |
| 003 | 46 - 103 | 42 |
| 004 | 56 - 179 | 1 |
| 005 | 59 - 84 | 0 |
| 006 | 50 - 85 | 0 |
| 007 | 55 - 85 | 0 |
| 008 | 63 - 120 | 41 |
| 009 | 33 - 103 | 0 |
| 010 | 56 - 83 | 0 |
| 011 | 20 - 86 | 0 |
| 012 | 63 - 83 | 0 |
| 013 | 59 - 100 | 0 |
| 014 | 30 - 88 | 0 |
| 015 | 5 - 129 | 3 |
| 016 | 21 - 83 | 36 |
| 017 | 63 - 90 | 0 |
| 018 | 33 - 58 | 0 |
| 019 | 55 - 93 | 0 |
| 020 | 75 - 145 | 43 |
| 021 | 3 - 89 | 0 |
| 022 | 55 - 83 | 0 |
| 023 | 21 - 128 | 21 |
| 024 | 63 - 106 | 0 |
| 025 | 60 - 98 | 0 |
| 026 | 71 - 115 | 42 |
| 027 | 55 - 76 | 0 |
| 028 | 58 - 83 | 0 |
| 029 | 61 - 83 | 0 |
| 030 | 40 - 91 | 0 |
| 031 | 63 - 84 | 0 |
| 032 | 60 - 83 | 0 |
| 033 | 26 - 80 | 14 |
| 034 | 59 - 83 | 0 |
| 035 | 43 - 90 | 0 |
| 036 | 24 - 83 | 28 |
| 037 | 49 - 79 | 0 |
| 038 | 58 - 83 | 0 |
| 039 | 40 - 84 | 0 |
| 040 | 5 - 75 | 7 |

| GAO case number | Wage replacement percentage--range (note a) | Number of States individual ruled ineligible |
|---|---|---|
| 041 | 51 - 76 | 0 |
| 042 | 46 - 84 | 0 |
| 043 | 6 - 126 | 1 |
| 044 | 48 - 81 | 0 |
| 045 | 50 - 94 | 0 |
| 046 | 58 - 103 | 0 |
| 047 | 83 - 140 | 43 |
| 048 | 30 - 89 | 3 |
| 049 | 54 - 91 | 0 |
| 050 | 45 - 76 | 0 |
| 051 | 9 - 84 | 4 |
| 052 | 46 - 81 | 0 |
| 053 | 41 - 76 | 0 |
| 054 | 5 - 113 | 7 |
| 055 | 41 - 88 | 0 |
| 056 | 53 - 83 | 0 |
| 057 | 29 - 108 | 0 |
| 058 | 41 - 86 | 0 |
| 059 | 45 - 81 | 0 |
| 060 | 56 - 84 | 0 |
| 061 | 45 - 84 | 0 |
| 062 | 20 - 81 | 25 |
| 063 | 6 - 56 | 2 |
| 064 | 43 - 85 | 0 |
| 065 | 3 - 85 | 14 |
| 066 | 48 - 81 | 0 |
| 067 | 24 - 75 | 2 |
| 068 | 43 - 75 | 0 |
| 069 | 44 - 100 | 0 |
| 070 | 41 - 74 | 0 |
| 071 | 38 - 80 | 0 |
| 072 | 26 - 101 | 0 |
| 073 | 36 - 71 | 1 |
| 074 | 38 - 78 | 0 |
| 075 | 8 - 70 | 0 |
| 076 | 34 - 71 | 0 |
| 077 | 16 - 73 | 26 |
| 078 | 35 - 70 | 0 |
| 079 | 31 - 75 | 0 |
| 080 | 34 - 74 | 0 |
| 081 | 44 - 100 | 0 |
| 082 | 31 - 70 | 0 |
| 083 | 31 - 70 | 0 |

| GAO case number | Wage replacement percentage--range (note a) | Number of States individual ruled ineligible |
|---|---|---|
| 084 | 26 - 68 | 0 |
| 085 | 16 - 68 | 24 |
| 086 | 33 - 78 | 0 |
| 087 | 30 - 76 | 0 |
| 088 | 3 - 64 | 3 |
| 089 | 24 - 63 | 0 |
| 090 | 25 - 65 | 0 |
| 091 | 24 - 59 | 0 |
| 092 | 23 - 59 | 0 |
| 093 | 6 - 54 | 0 |
| 094 | 24 - 59 | 0 |
| 095 | 5 - 59 | 2 |
| 096 | 21 - 53 | 0 |
| 097 | 21 - 56 | 0 |
| 098 | 14 - 51 | 34 |
| 099 | 19 - 51 | 0 |
| 100 | 15 - 40 | 0 |

a/Ranges for States in which individuals were ruled eligible.

# INTERVIEW DOCUMENT

| Question | Coding |
|---|---|
| | * [ ][ ][ ][ ][ ][ ] 1–6 [1] 7 |
| 1 Sex (To be determined by auditor)<br>1 - Male<br>2 - Female | [ ] 8<br>* Begin Card #1 |
| 2 What is your race?<br>1 - White<br>2 - Black<br>3 - Other<br>9 - No response | [ ] 9 |
| 3 How old are you?<br>(Enter number in years or 99 for no response) | [ ][ ] 10 |
| 4 What is the highest grade in school that you completed? (For college insert 13 for completion of one year, 14 for completion of 2 years etc - Do not include vocational training) (99 - no response) | [ ][ ] 12 |
| 5 Have you taken part in a vocational or technical training program related to your prior job, and if so who sponsored it?<br>1 - No (GO TO QUESTION 8)<br>2 - Yes -Private vocational/technical training<br>3 - Yes -State or Federal vocational/technical training<br>4 - Yes -Don't know who did<br>9 - No response (GO TO QUESTION 8) | [ ] 14 |
| 6 What was the month and year that you started and ended this training?<br>START<br>END<br>AUDITOR - COMPUTE TOTAL TIME IN MONTHS<br>TOTAL | MO [ ][ ] 15 YR [ ][ ] 17<br>[ ][ ] 19 [ ][ ] 21<br>mos [ ][ ] 23 |
| 7 Indicate the occupation or skill in which you were trained during this training? For example, computer programmer, secretary, bricklayer<br>Auditor - Write In ________ | |
| 8 For how many years have you been in the work force working for pay on a full time basis and how many years on a part time basis? Don't include summer jobs<br>Full time (in years)<br>Part time (in years)<br>00 - no years<br>99 - no response | [ ][ ] 25<br>[ ][ ] 27 |
| 9 Since January 1973 how many different times have you been unemployed and received benefits? 99-No Response | [ ][ ] 29 |

—NOW I'D LIKE TO ASK YOU SOME QUESTIONS ABOUT THE PERIOD OF TIME BEFORE YOU BECAME UNEMPLOYED

10 Were you working full-time or part-time before you became unemployed?

1 - Full time
2 - Part time
9 - No response

31

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11 How many hours a week were you working?

999 - no response

32

---

12 What was your occupation or title of your job before you became unemployed?

Auditor - Write in ____________

Auditor - Classify occupation

1 - Skilled
2 - Unskilled
3 - Professional
9 - No Response

35

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13 What was your average take home pay each week before you became unemployed? (Use whole $)

9999 No response

36

---

14 What was your marital status before you became unemployed? Were you married, single or what?

1 - Single (GO TO QUESTION 17)
2 - Married
3 - Divorced or separated (GO TO QUESTION 17)
4 - Widowed (GO TO QUESTION 17)
9 - No response (GO TO QUESTION 17)

40

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15 Did your husband or wife work before you became unemployed?

1 - Yes
2 - No (GO TO QUESTION 17)
9 - No response (GO TO QUESTION 17)

41

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16 About how much take home pay did your husband or wife earn each week? (Use whole $)

9999 No response

42

---

17 Did any other members of your household work before you became unemployed?

1 - Yes
2 - No (GO TO QUESTION 19)
9 - No response (GO TO QUESTION 19)

46

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18 About how much did these other household members contribute to the household each week? Or if you lived with a parent or relative, how much did they contribute to your financial support each week? (Use whole $)

9999 No response

47

APPENDIX IV

19 Were you contributing the most toward the income of the household? (Were you the main wage earner for the household?)

1 - Yes
2 - No
9 - No response

[ ] 51

20 Before you became unemployed, did you or other members of your household receive any financial assistance from the following sources?

(Use whole $)

Received by

| financial assistance from | | Yourself | Your spouse | Other members |
|---|---|---|---|---|
| (1) Welfare - If yes, how much per month if no, enter 0' in each box | | 52 | 56 | 60 63 |
| (2) Social Security | per month | ** 8 | 12 | 16 |
| (3) Pension | per month | 20 | 24 | 28 |
| (4) Food stamps | per month | 32 | 36 | 40 |
| (5) Veteran's benefits | per month | 44 | 48 | 52 |
| (6) Alimony or child support | per month | 56 | 60 | 64 |
| (7) Other (specify) _______ ________________ | per month | 68 | 72 | 76 79 |
| (8) Total | per month | *** 8 | 12 | 16 |

9999 - no response

(Do not add 9999 codes into the total)

**Begin Card #2

1 Case 6 — 2 Card

--NOW, I'D LIKE TO ASK YOU SOME QUESTIONS CONCERNING YOUR CURRENT UNEMPLOYMENT

*** Begin Card #3

1 Case 6 — 3 Card

21 How did you become unemployed?

1 - Fired (GO TO QUESTION 25)
2 - Quit (GO TO QUESTION 25)
3 - Laid off
4 - Labor dispute (GO TO QUESTION 25)
5 - Other (specify (GO TO QUESTION 25)

________________________________

________________________________

9 - No response (Go To Question 25)

[ ] 20

22 Do you expect to be recalled by your former employer?

1 - Yes
2 - No (GO TO QUESTION 25)
9 - No response (GO TO QUESTION 25)

[ ] 21

23 How many weeks will you have been on unemployment when you are recalled?

00 - Don t know
99 - No response

[ ][ ] 22

 APPENDIX IV

| | | |
|---|---|---|
| 24 | In the last 5 years, how many times have you been laid-off and recalled by your former employer? The one that laid you off the last time (Should be at least one time)<br><br>99 - No response | 24 |
| 25 | About what date did you start collecting unemployment benefits? Can you give me the month, day and year?<br>99 - No response<br>AUDITOR Calculate number of weeks to date | MO 26, DAY 28, YR 30, WKS 32 |
| 26 | How much money do you receive each week in unemployment benefits? (Use whole $)<br><br>999 - No response | 34 |
| 27 | In addition to unemployment benefits do you have any earnings through part time employment?<br><br>Yes, enter amount (Use whole $)<br>No, enter 000<br>999 - No response | 37 |
| 28 | What is your current marital status? Are you married single or what?<br><br>1 - Single (GO TO QUESTION 31)<br>2 - Married<br>3 - Divorced or separated (GO TO QUESTION 31)<br>4 - Widowed (GO TO QUESTION 31)<br>9 - No response (GO TO QUESTION 31) | 40 |
| 29 | Is your husband or wife working now?<br><br>1 - Yes<br>2 - No (GO TO QUESTION 31)<br>9 - No response (GO TO QUESTION 31) | 41 |
| 30 | About how much take home pay does your husband or wife earn each week? (Use whole $)<br><br>9999 no response | 42 |
| 31 | Are any other members of your household working now?<br><br>1 - Yes<br>2 - No (GO TO QUESTION 33)<br>9 - No response (GO TO QUESTION 33) | 46 |
| 32 | About how much do these other household members contribute to the household each week? Or if you live with a parent or relative how much do they contribute to your financial support each week?<br><br>9999 no response | 47 |

33 Are you or any other members of your household now receiving any financial assistance from the following sources?

(Use whole $)

Received by

| Financial assistance from | | Yourself | Your spouse | Other members |
|---|---|---|---|---|
| (1) Welfare - If yes, how much per month If no, enter 0 in each box | | | | |
| (2) Social Security | per month | | | |
| (3) Pension | per month | | | |
| (4) Food Stamps | per month | | | |
| (5) Veteran's Benefits | per month | | | |
| (6) Alimony or child support | per month | | | |
| (7) Other (specify) ______ ________________ | per month | | | |
| (8) TOTAL | per month | | | |

9999 No response
(Do not add 9999 codes into the total)

**** Begin Card #4

Case

4 Card

34 How many people are in your household?

Interviewee 1
Wife or husband ___
Children (enter number) ___
Other dependents - e g parent(s), other relatives, friend(s) ___

TOTAL ___
99-No Response

*****Begin Card #5

Case

5 Card

35 Did you have child care expenses prior to becoming unemployed? Nursery school, babysitting etc

Yes - How much did you pay per week? (Enter whole $)

No - Enter 000
999 - No response

36 Did you have any other work related expenses prior to becoming unemployed? (transportation uniforms, etc )

Yes - How much did they amount to in total each week? (Enter whole $)
No - Enter 000
999 - No response

37 Do you have child care expenses now?

Yes - How much do you pay per week? (Enter whole $)
No - Enter 000
999 - No response

38 What is the lowest amount of take home pay per week you need in order to take a job? (Enter whole $)

999 - No response

39 Consider your total household income before you were unemployed and compare it to your current total income including unemployment insurance Based on that how much financial incentive do you have to look for a job

(Read options)

1 - None
2 - Very little
3 - Some
4 - Considerable
5 - Great

9 - No response

22

40 If the individual has been unemployed for at least 8 weeks, ask the following questions

(a) Why do you believe people like yourself have difficulty finding a job?

(b) What do you feel could be done to improve the situation?

Record other comments

# FOLLOWUP QUESTIONNAIRE

U S GENERAL ACCOUNTING OFFICE
REVIEW OF INDIVIDUALS WHO COLLECTED
UNEMPLOYMENT COMPENSATION

1 Are you still receiving unemployment benefits? (Check one.)

1 ☐ Yes (IF YES, DO NOT ANSWER ANY FURTHER QUESTIONS PLEASE MAIL BACK THIS QUESTIONNAIRE )

2 ☐ No (If no, answer remaining questions )

2 When did you stop collecting unemployment benefits?

____/____/____
Month /Day /Year

3 Why did you stop getting unemployment benefits? (Check one )

1 ☐ My benefits ran out

2 ☐ I was called back by my former employer

3 ☐ I got another job

4 ☐ Other (Please specify) ______________________

______________________

4 If your benefits ran out, how long were you without benefits until you got a job? (Check one )

1 ☐ Without benefits for ______ weeks

2 ☐ Benefits did not run out

5 Are you working now? (Check one )

1 ☐ Yes, full-time

2 ☐ Yes, part-time

3 ☐ No (If no go to question No 8 )

6 What is your occupation or title of your job?

I am a ______________________

7 How much money do you take home each week after taxes?

$ ______ each week

8 If you are not working now, which best explains what you are doing? (Check one )

1 ☐ Retired

2 ☐ Student

3 ☐ Unemployed looking for work

4 ☐ Unemployed, not looking for work

because ______________________

______________________ (fill in)

**U S Department of Labor**

Inspector General
Washington D C 20210

JUN 8 1979

Mr Gregory J Ahart
Director
Human Resources Division
U S General Accounting Office
Washington, D C 20548

Dear Mr Ahart

Thank you for the opportunity to review the draft General Accounting Office report, "Unemployment Insurance--Why Do Many Recipients Prolong Their Unemployment?"

We also appreciate the time taken by GAO staff members on May 30, 1979, to meet with Department of Labor staff to discuss this report

Enclosed are the Department's comments on this draft report These comments indicate that the Department continues to have concerns regarding the analysis of data and the policy recommendations contained in the report

Sincerely,

Marjorie Fine Knowles

MARJORIE FINE KNOWLES
Inspector General

Enclosure

GAO note: Page references have been changed to correspond to page numbers in the final report.

U S. DEPARTMENT OF LABOR COMMENTS ON THE DRAFT GAO REPORT
UNEMPLOYMENT INSURANCE--WHY DO MANY RECIPIENTS
PROLONG THEIR UNEMPLOYMENT?

## Introduction

GAO has compiled some potentially valuable data on Unemployment Insurance (UI) recipients for this report Unfortunately, the present report contains major methodological weaknesses. These shortcomings lead directly to unwarranted policy recommendations

One major weakness of the report is that it ignores information on benefit inadequacy for a substantial portion of UI recipients Even though these benefit inadequacies are implicit in the data presented in the study, the report focuses entirely on work disincentives resulting from UI benefit levels In considering possible policies for taxing UI benefits, it is essential that UI benefit inadequacies be analyzed along with possible work disincentives resulting from UI benefits

The second major weakness of the report is that the data analysis is deficient The methodological errors contained in the present study make it impossible to draw meaningful conclusions from the analysis

The following sections discuss (1) the specific GAO recommendations (2) major analytical problems, and (3) additional analytical problems.

## I. The GAO Recommendations

### 1. Taxation of UI Benefits

Based on equity and work incentive considerations, GAO recommends that Congress consider taxing UI benefits of recipients at all income levels. To the extent that taxation would more equitably distribute net benefits among the beneficiaries, we concur in principle However, since taxation of benefits results in a reduction of net benefits to UI recipients, any new taxation proposal should ensure that adequate benefits be provided to all claimants so that the UI program fulfills its objectives. There are many claimants who receive benefits that are less than 50 percent of their previous wage. Taxing UI benefits without raising their benefit amounts will make this situation worse. This is inimical to the basic goal of UI programs. Congressional consideration of taxing all UI benefits should include consideration of measures to raise benefit levels where they are inadequate

### 2. Pension Reduction

We do not concur with the GAO recommendation for reducing UI benefits by retirement income. We believe that no action should be taken on this issue. Congress has mandated that the National Commission on Unemployment Compensation (NCUC) study this issue and make legislative recommendations. Any action should be deferred until the NCUC makes its recommendations.

### 3. Uniform Compensation Formula

We do not concur with the GAO recommendation that "the Congres establish a uniform methodology for determining compensation amounts." The reason given for the GAO recommendation is the unequal treatment of similarly-situated beneficiaries that may arise due to interstate variation.

However, it is not always true that the variation in benefit formulas and other State UI provisions lead to inequity in treatment of claimants. In fact, these variations can have an equalizing, rather than unequalizing, effect on treatment of claimants because the States differ in their industry, demographic mix, and other economic conditions which are closely associated with what a given amount of UI benefits or a given benefit duration means to a claimant. For example, the factors determining the benefit formula--such as the high quarter earnings fraction, minimum and maximum weekly benefit amounts--should logically vary according to the States' cost of living or other unique economic factors. Also, economic activities in some States may be characterized by industry mixes and occupational compositions that are inherently more vulnerable to cyclical and/or trend changes than those in other States. In these States, therefore, longer potential benefit duration may be needed to equalize the chance of finding suitable jobs.

Thus, while it may be true that the existing variation in State UI laws causes some form of "inequity", this is not sufficient reason to propose eliminating all variation in State UI provisions. Instead, it may be desirable to reduce, rather than eliminate, the variation in State provisions The exact amount of reduction that should be undertaken, if any, should be based on a more thorough analyses of the inequities stemming from the program and on the options available for removing these inequities.

## II. Major Analytical Problems

### 1. Ignoring the Benefit Adequacy Issue

One of the objectives of unemployment insurance in the United States is to provide income protection to unemployed workers to minimize the disruption of their standards of living. Thus, while the potentially negative effect of excessive benefits needs to be considered in determination of UI benefit levels, it is vital that any such consideration be balanced by the evaluation of the income necessary to tide unemployed workers over a temporary period of joblessness until they find suitable jobs. Without such a balanced approach, any policy evaluation will over emphasize work disincentives and the need to cut benefits, thus defeating the primary purpose of the program We believe that the GAO report is likely to lead to this by being heavily weighted by the concern for the disincentive effect of unemployment benefits, while giving no attention to the appropriate benefit amounts for income protection purposes.

By providing wage loss replacement during unemployment, unemployment insurance provides a unique type of income protection for experienced workers. Federal guidelines specify a 50 percent replacement rate However, some recent studies have found even this replacement level is not adequate Moreover, many claimants fail to reach the 50 percent rate because of the maximum weekly benefit amount. Therefore, there is little basis to presume that UI claimants generally receive benefits, adequate to fulfill the programs mandated goal, in fact, the opposite may be true Even the GAO study has found, based on a highly unconventional definition of the replacement rate which we will comment on in the next section, that as many as 31 percent of the claimaints received less than 50 percent of their net lost income, and as many as 6 percent received less than 30 percent of their net income loss Since the GAO definition of the replacement rate tends to overstate the extent that UI benefits replace earnings, it is quite likely that these proportions may understate the extent of "inadequate" benefits

APPENDIX V

The most desirable benefit formula is one which balances adequacy and incentive effects Because there is no agreement as to the adequate wage loss replacement and because the GAO report offers little statistical evidence as to the presence of work disincentive, we are not convinced that "UC recipients often have little financial incentive to work", as the Chapter 2 heading states.

2. Inappropriate Calculation of the Replacement Ratios This study uses a definition of the wage loss replacement ratio, which is inappropriate for the analysis presented. The definition used in the report is the percentage of a recipient's net income before unemployment that is replaced by unemployment compensation plus other income A more appropriate measure is the percentage of the net wage loss due to unemployment that is replaced by unemployment compensation. For example, assume an individual is earning $150 per week in net wages prior to becoming unemployed The individual also receives $40 per week in child support net of income taxes. Upon unemployment the individual receives $75 per week in UC. Then net "income replacement" as defined in the report is.

$$\frac{75 + 40}{190} = .61,$$

while the traditional calculation of wage loss replacement would yield.

$$75/150 = 50.$$

The latter is the correct ratio to use for analyzing work disincentive effects because it measures the net benefit from returning to work. For example, for this individual a return to work at the previous wage generates $150 in net earnings but results in the loss of $75 in benefits--a net gain of 50 percent of earnings Moreover, the same logic which suggests deducting taxes and work expenses from wages also suggests that fringe benefits foregone, and job search costs should be deducted from the UC benefit when calculating replacement rates This would further lower the rates presented in the report

Finally, the use of the GAO "replacement ratio", because of the inclusion of other income, means that the effect of receiving UI benefits on unemployment duration cannot be separated from the effects of receiving other income. As such, the GAO report does not determine the impact of UI benefits alone on UI claimants' behavior. Thus, the report does not analyze the work disincentive effect of UI benefits during periods of unemployment. Rather, it is a commentary on the incentive to work for unemployed individuals given all sources of income available to them.

3. <u>Failure to Account for the Multi-dimensional Nature of the problem</u>

The report depends exclusively on two variable analyses. The multi-dimensional nature of labor market behavior makes it difficult to make a definitive empirical analysis of the effect of UI benefits. Any conclusion drawn from an analysis of only two variables is methodologically deficient and unsuitable for policy analysis.

There are many variables which affect weeks of unemployment, some of which may be correlated with wage loss replacement rates The two variable analyses of the type used in this report runs a risk of unduly attributing the effects of these other variables to the replacement rate. The data should have been adjusted for the effects of other variables, e.g., using the multiple regression technique

III Additional Analytical Problems

1. Lack of Analysis of Present Tax Provisions

The analysis in the GAO report does not reflect the fact that, beginning in 1979, UI benefits are taxed for high income families The present tax provisions, applying to singles with incomes over $20,000 and couples with incomes over $25,000, may reduce UI benefits for many persons currently receiving a high UI replacement rate. The GAO report should analyze what the effects of the current tax provisions would have been if they had applied to the UI claimants in the GAO samples.

2. Lack of Analysis of Non-response.

The response rate of 75 percent to the follow-up questionnaire is low enough to raise questions concerning bias in the data of the table on page 8. For example, what if the nonrespondents were, on average, high replacement rate individuals who had short durations of unemployment? The same possibility arises with the 499 individuals who are still unemployed at reinterview time. While it is not possible to give weeks of unemployment for non-respondents, unless UC records could be obtained, the report could compare their average replacement rate to those of the respondents. Other characteristics, such as age, sex, and race, of the non-respondents could be compared to those of the respondents. Such comparisons could allow judgment of possible biases Similar comparisons could be made for the 499 "still unemployed" recipients.

3. Failure to Take Note of Inherent Scarcity of Employment Opportunities When Many UI Claimants are Unemployed.

One objective of unemployment insurance is to provide benefits for a temporary period of joblessness when there is slack in demand The cause of unemployment of many experienced workers who are protected by unemployment insurance is often of a cyclical or other temporary nature, thus, there is a good probability that these workers will return to the same employers or to the same occupations. In addition, while they are unemployed, alternative employment opportunities are likely to be scarce Together with the "suitable" job principle of unemployment insurance which will be discussed in the next section, these factors would explain in part the relatively low rate of placement of UI beneficiaries by the State Employment Services (Job Service) compared to that of non-beneficiaries. Thus, the following assessment provided by the U.S. Employment Service is quite in accord with the program goals of unemployment insurance

- Many workers on temporary or short term layoff with a job attachment do not actually compete in the job market.

- UI claimants tend to be older, more experienced, higher skilled workers, and, therefore, more selective in job acceptance.

It must also be remembered that unemployment of UI beneficiaries is but a portion of the total unemployment to which the function of the Employment Service is directed As the Employment Service has indicated, a large number of openings filled by the Job Service tend to fall in the entry level category. It is expected, therefore, that the success rate in placing non-UI claimants should be higher than that applicable to UI beneficiaries Even in the face of these difficulties the placement rate by the Employment Service of UI claimants increased between FY 1975 and FY 1978 from 11.6 percent to 20.7 percent.

4 <u>Failure to Take into Account the "Suitable" Job Provision of Unemployment Insurance</u>

The intent of the UI program is not for the claimants to accept just any job. While the program does require the beneficiaries to be "able and available" for work, at the same time, the program emphasizes that the beneficiaries be given the chance to maintain the accustomed living standard through reemployment at "suitable" jobs -- i e., commensurate with their skills and qualifications This emphasis is also in accord with the social goal of minimizing the loss of job skills and ensuring the greatest possible output for the U S. economy by having workers placed in productive and suitable jobs Viewed in this sense, the prolongation of the jobless period among the beneficiaries is not necessarily undesirable.

5. Failure to Consider the Dynamic Effect of UI.

We are dissatisfied by the GAO report's implicit dependence on the static consumption theory as its analytical framework. We believe that the effect of unemployment benefits on the beneficiaries' labor market behavior must be viewed in a dynamic context -- i.e., to take into consideration the effects of the current and successive receipts of benefits on the parameters of job search decision and the feedback of these effects on the current decision. Thinking in the static mode cannot, for example, incorporate the job search efficiency effect of UI benefits on the expected income stream, and ultimately, on the beneficiaries current labor market decision. In a dynamic analysis, we believe that even a shortened unemployment duration (hence, benefit duration) can be logically deduced as a result of an increased UI benefit amount.

6. Ambiguity of "Quits" in the GAO Report.

The implication of the data given on page 9 would be clearer if the sample claimants who have quit their most recent jobs had been classified according to the types of quits. Interpretation of the positive correlation between quits and wage loss replacement would differ depending on the nature of quits. For example, if claimants who quit for good cause are predominant in the high replacement group, the interpretation would be different from that where the predominance of voluntary quits without good cause were in the high replacement group.

7. Absence of the Description of Sampling and Survey Methods

This report contains very little description of the sampling and interview methods used. In an empirical study such as this, the outcome of the analysis may depend on the sampling method, nature of sample observations, extent and nature of non-responses and interview techniques. We are especially interested to know how the interview questions were worded and posed to the claimants. Many of the expressions usually used to describe the claimant status or behavior are qualitative with a wide range of possible meanings.

8 Title and Sub-titles

The title of this report presumes that recipients prolong their unemployment without offering any evidence that they do in fact do so Also, one objective of UC is to allow recipients to seek jobs in keeping with their skills and experience, which may mean some prolongation of their unemployment A more descriptive title such as "The Effect of Unemployment Compensation on Duration of Unemployment", would be more appropriate

Another example of such language is the subtitle used on the first page of the digest of the report We recommend the following language "Net Income Replacement Rates Among UC Recipients"?

9 Regarding the paragraph on the bottom of page 17:

First, part-time work "just prior to unemployment" may not be particularly relevant When a slow down occurs, many who are to be laid off begin to work a reduced work week just prior to the lay-off Moreover, the higher percentage of part-time workers in the higher income replacement group may be largely explained by the benefit maximum

(20267)

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