VI. REVIEWS OF BOOKS AND STUDIES

Income Security

RESEARCH REVIEW

JOHN J. HORN, Commissioner

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THE PLACE OF DEPENDENTS' ALLOWANCES, AND THE DEFINITION OF "DEPENDENT"

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The National Commission on Unemployment Compensation has commissioned a series of research studies on key issues in unemployment insurance. The following summary of the National Commission's Study of Dependency Benefits was prepared by James Phillips of the Division of Planning and Research.

THE DEPENDENCY BENEFITS ISSUE

Historically, the unemployment insurance program was designed to provide individuals who lost their jobs through no fault of their own and who were attached to the labor force a replacement of their previous wages large enough to enable them to meet the costs of life's necessities while avoiding payment of benefits that would discourage their incentive to seek work. From its inception in the United States in 1935 UI has been wage-related insurance provided as a matter of right; no questions were asked concerning a claimant's other income, expenditures, or assets. These features served to distinguish UI from welfare, which seeks to establish need based on the financial and familiar responsibilities of potential recipients.

Dependents' allowances were generally rejected by the framers of the UI system because they introduce a needs test into a wage-related program, but nevertheless, are currently paid by twelve states. These provisions differ with respect to both the definition of compensable dependent and the method of determining the amount of the allowance. Dependents have always been restricted to specified relations of the claimant in order to simplify administration. In all twelve states there is a requirement that the extent of support be more than half or "wholly or mostly." Seven states provide for a spouse to be a dependent. Eight states add a fiscal amount for each dependent up to some dollar maximum while two limit benefits to the basic maximum.

ARGUMENTS IN FAVOR OF DEPENDENCY BENEFITS

The principal argument in favor of the dependency benefits provision is that individuals with dependents spend a greater proportion of their wages on living costs than when only one worker is supported and, therefore, should be entitled to higher benefits. Proponents argue that "need" in the relief sense is not really used, since the claimant is presumed to require more benefits, while no inquiry into the claimant's personal affairs is made.

ARGUMENTS AGAINST DEPENDENCY BENEFITS

Opponents of the concept of dependency benefits point to the fact that they introduce a needs test into a wage-related program. The beneficiary's previous standard of living was based on his wages, which did not reflect the number of his dependents. Further, because some degree of support is always stipulated, inquiring into the claimant's finances must be made in order to avoid payments to ineligible individuals. Also, those states that pay dependency benefits are clustered at the low end of the scale in terms of the maximum wage-replacement percentage. It is also clear that this provision discriminates against women claimants, whose generally lower wages make it difficult for them to meet the statutory requirement of providing more than 50 percent of the support of dependent children. Further, administrative procedures in most states provide for considerably more inquiry of women in cases of questionable eligibility. In fact, during 1977, only 17 percent of women but 48 percent of male claimants received dependency benefits in the states providing them.

CONCLUSION

The authors urge the National Commission on Unemployment Insurance to reject the concept of dependency benefits as inappropriate in a wage-related social insurance program. Those states that continue to pay them should follow certain principles: (1) basic benefits should be adequate in the absence of the allowances; (2) tests to determine the dependency of a spouse should be liberalized; (3) other relatives such as parents and sibilings should be included in the definition of dependent; and (4) maximum benefits should still be somewhat less than the claimant's previous wages.

Income Security

RESEARCH REVIEW

JOHN J. HORN, Commissioner

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FINANCING AMERICA'S UNEMPLOYMENT COMPENSATION PROGRAM

BY: Donald L. Diefenbach

The American unemployment insurance (UI) system has been the subject of controversy and debate since its enactment in the 1930's. The focus of popular debate has most often centered upon the controversial benefit issues of fraud, malingering, escalating weekly benefits and the duration of benefits. In recent years, however, the problem of how to finance the program has emerged as a most pressing concern. Nearly half of the states have completely exhausted all trust fund reserves and have been forced to borrow large sums of money in order to continue paying benefits to the unemployed.

This report will review the benefit financing problem, identify major taxation issues, enumerate policy options and offer specific recommendations appropriate to the times and to American traditions in financing this social insurance program.

The attached summary of Financing America's Unemployment Compensation Program outlines major findings and recommendations of the study. The full study will be distributed by the U. S. Department of Labor later this year. This study will be listed in the Income Security Bibliography for circulation to Department of Labor and Industry staff as soon as possible.

Financing America's Unemployment Compensation Program

A Condensed Report

THE PROBLEM

The tax structure which is used for financing America's Unemployment Compensation program is inadequate. During the recessions of the 1970's, half of the states exhausted their unemployment trust funds. As we face a third major recession in this decade, 17 states are still in debt. Major structural improvements are needed in the system for financing this important social insurance program.

The following questions and answers summarize major findings and recommendations of the study.

FUTURE BENEFIT COSTS

Q. *What is the outlook regarding future unemployment benefit costs?*

A. Benefit costs during the next decade may run 20% to 30% above historic costs.

UNEMPLOYMENT COMPENSATION DEBT

Q. *What is the extent of the Unemployment Compensation Debt?*

A. There are two separate debts. A state debt of $5 billion owed by 17 different states and a federal debt of $8 billion owed collectively by covered employers in all of the states.

STATE UI DEBT

Q. *How should the State UI debt be repaid?*

A. Under current law, outstanding state loans of $5 billion will be repaid throug' annually escalating federal unemployment tax rates of 0.3%, 0.6%, 0.9%, 1.2% and beyond. These pending federal tax rate increases have discouraged unemployment compensation tax reform at the state level. Indeed, state legislatures would be well advised to refrain from imposing additional state unemployment taxes when excess federal unemployment taxes of 0.3%, 0.6%, 0.9%, 1.2% and beyond are scheduled to take effect in future years. This report proposes that loans should be repaid at an annual rate of 0.2%. Under this plan, structural reform at the state level would be encouraged, rather than discouraged. For instance, the loan repayment rate would remain constant at 0.2% in states which maintained solvency financing; the rate would escalate only in states which continued borrowing in future years.

FEDERAL UI DEBT

Q. *How should the federal UI debt be repaid?*

A. Under current law, outstanding federal loans of $8 billion will be repaid through an excess FUTA tax of 0.2% on covered employers in all states. This charge will continue through much of the 1980's. This debt, which relates to extended benefit durations during national recession, should be financed retroactively through general revenues. This financing proposal has been endorsed by the National Commission on Unemployment Compensation.

EXTENDED BENEFITS

Q. *Who should bear the costs of extended benefits beyond 26 weeks?*

A. Extended benefits costs related to economic recession are beyond the control of individual employers and states. Benefit costs beyond 26 weeks should be funded out of general revenues. At the very least, extended benefit payments forced upon the states during periods of a national "on" trigger should be financed out of general revenues.

TAXABLE WAGE BASE

Q. *Is a federal taxable wage base of $6000 adequate for the future?*

A. No. Benefit and Administrative costs are escalating with inflation rates of 10% and more. By 1980, under a fixed taxable wage base of $6000, less than 50% of total payrolls will be subject to unemployment insurance taxes. In contrast, 61% of payrolls were taxed in 1960; 93% of payrolls were taxed in 1940. The federal taxable wage base should be redefined from a fixed value of $6000 to a variable value of 70% of the national average annual wage in covered employment; under this rule, the federal taxable wage base would have been $8000 in 1979.

LONG RANGE PLANNING

Q. *What policy approach should be used to remedy the financing shortfalls of the current system?*

A. Legislative action is required at both the federal and state levels. In addition to the federal legislative proposals outlined above, all state unemployment insurance agencies should define and adopt a long range financing plan. This report will help state policymakers in this task. The report devotes a chapter to the issue of "Long Range Financial Planning". In addition, another chapter of the report defines "Key Elements of Tax Structure Adequacy" to guide state policymakers in designing custom systems to meet individual state financing needs.

UNEMPLOYMENT COMPENSATION REFORM

Q. *What are the prospects for comprehensive unemployment compensation reform in the near future?*

A. Unemployment Compensation Reform is a perennial issue in The Congress and in The State Legislatures. Substantive changes in the program, however, are few and far between. The recent establishment of The National Commission on Unemployment Compensation, Chaired by former HEW Secretary Wilbur Cohen, has given the issue of unemployment compensation reform a high degree of visibility and a new sense of urgency. The time is ripe for unemployment compensation reform; the need is pressing. The prospects for comprehensive unemployment compensation reform within the next three years are excellent.

In conclusion, it is emphasized that the financial imbalances which persist today can be remedied through increased taxes, reduced benefits or a combination of the two. In addition to the taxation reforms suggested above, there is an equally if not more compelling need to restructure the benefit side of the program, to reduce fraud and abuse of the system and to improve the quality of job placement and unemployment benefit services which are provided to American Workers.

In addition to the major issues summarized on the preceding pages, Financing America's Unemployment Compensation Program addresses many other issues, including:

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... COUNTERCYCLICAL FINANCING: A highly effective countercyclical financing system has yet to be implemented by any of the states. This report illustrates two models of countercyclical financing and simulates historic experience for selected states to illustrate how a countercyclical financing system would operate.

... MAXIMUM TAX RATES: A greater proportion of the aggregate tax burden should be shifted to employers who consistently generate very high levels of unemployment. This report introduces two new experience rating concepts--Limited Liability and Continuous Rating--which could be utilized to attain a more equitable experience rating system.

... MINIMUM TAX RATES: States should not permit "zero" employer tax rate assignments under their laws; the practice of "zero" rate assignments is inconsistent with social insurance principles.

... FUND ADEQUACY: The federal fund adequacy guideline recommends that states should have between "one-and-a-half and three" years of recessionary level benefits stored in the fund. This guideline should be revised downward. States can operate solvent systems with substantially lower reserves than those recommended in the federal guideline of fund adequacy.

... TAX STRUCTURE ADEQUACY: This report develops a much needed concept of "Tax Structure Adequacy" which complements and extends the concept of "Fund Adequacy". "Fund Adequacy focuses upon the problem of providing enough funds to get through the next recession; the concept of "Tax Structure Adequacy" considers the long term, focusing upon the problem of getting through successive recessions and fund rebuilding periods.

... COST EQUALIZATION: There is a need for some limited system of cost equalization to help promote financial stability of the federal-state unemployment insurance system. The cost equalization issue should be given very high priority by The Congress.