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UNINTENDED CONSEQUENCES: IS GOVERNMENT EFFECTIVELY ADDRESSING THE UNEMPLOYMENT CRISIS?

HEARING

BEFORE THE

SUBCOMMITTEE ON ECONOMIC GROWTH, JOB CREATION AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

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CONTENTS

	Page
Hearing held on February 14, 2013	1

WITNESSES

Casey B. Mulligan, Ph.D., Professor in Economics, The University of Chicago	
Written Statement	5
Oral Statement	7
C. Eugene Steuerle, Ph.D., Institute Fellow and Richard B. Fisher Chair, The Urban Institute	
Written Statement	25
Oral Statement	27
Andrea L. Carter, Owner and President, Carter Machine Company	
Written Statement	39
Oral Statement	41
Chad Stone, Ph.D., Chief Economist, Center on Budget and Policy Priorities	
Written Statement	46
Oral Statement	48
The Honorable Stacy G. Reece, Former Member of the Georgia State House, Franchise Owner, Spherion	
Written Statement	56
Oral Statement	58

APPENDIX

The Honorable Jim Jordan, a Member of Congress from the State of Ohio, Opening Statement	90
The Honorable Gerald E. Connolly, a Member of Congress from the State of Virginia, Opening Statement	92

EFFECTIVELY ADDRESSING THE UNEMPLOYMENT CRISIS?

Thursday, February 14, 2013

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ECONOMIC GROWTH, JOB CREATION,
AND REGULATORY AFFAIRS,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, D.C.

The subcommittee met, pursuant to call, at 2 p.m., in Room 2247, Rayburn House Office Building, Hon. Jim Jordan [chairman of the subcommittee] presiding.

Present: Representatives Jordan, McHenry, DesJarlais, Collins, Meadows, Bentivolio, DeSantis, Cartwright, Duckworth, Connolly, Pocan and Horsford.

Staff Present: Brian Blase, Professional Staff Member; Linda Good, Chief Clerk; Tyler Grimm, Professional Staff Member; Christopher Hixon, Deputy Chief Counsel, Oversight; Michael R. Kiko, Staff Assistant; Kristin L. Nelson, Counsel; Jaron Bourke, Minority Director of Administration; Devon Hill, Minority Research Assistant; and Brian Quinn, Minority Counsel.

Mr. JORDAN. The Subcommittee on Economic Growth, Job Creation and Regulatory Affairs will come to order. I want to welcome our new members, and we have two of them here today, Mr. Meadows and Mr. Collins. I'm glad to have you part of the committee. And, of course, the ranking member Mr. Cartwright, I want to welcome you and your team as well. We've had a great relationship working with the minority party the last 2 years, and I would like to think before that. Mr. Kucinich and I have been on this committee for 4 years had a great relationship when we were in the minority. So we look forward to working with you and your team as we have several hearings here in this Congress.

You got to listen to me do an opening statement and then Mr. Cartwright an opening statement, and then we'll get you sworn in and get right to it. We have a great panel, some small business owners and some experts in the field. We will get to you as quickly as we can. But let me just do a quick opening statement, and then we'll turn it over to Mr. Cartwright and get right to our witnesses.

Today's hearing is about America's unemployed and understanding the failure, the failure of Federal efforts to get them back to work. Four years ago this week, an 800 billion stimulus spending package was signed into law with the intent of creating jobs and jump-starting economic growth. The administration justified the stimulus with a report stating that as a result of this legisla-

tion, the unemployment rate would never, never exceed 8 percent and would be 7 percent and falling by February of 2011.

Obviously that didn't happen. That unemployment rate is still hovering around 8 percent, representing 12.3 million Americans out of work. When we also count the broader universe of people seeking work, the unemployment rate climbs to over 14 percent. We are still in the jobs crisis, and we must understand why.

Since 2007, there have been at least a dozen new or expanded Federal safety net programs. For example, various unemployment insurance and food stamp programs have increased, and eligibility has been expanded. The most drastic of these changes came via the 2009 stimulus law. These additions to the way the Federal Government assists the unemployed have in their totality collectively changed the incentives faced by those seeking work.

One of our witnesses today, Professor Mulligan of the University of Chicago, has done groundbreaking research that shows that as a result of our layered social safety net programs, there is a large number of American households for whom the reward for working is zero or negative when compared to the benefits received while unemployed. In other words, a person might have more income to use or save as a consequence of working less. Professor Mulligan estimates that in 2009 approximately 4 million individuals, 4 million of our fellow citizens, would either not benefit at all from returning to work or, even more troubling, would actually be worse off financially from getting a job.

No one believes that President Obama or my colleagues on the other side of the aisle wish to prolong the time Americans spend without jobs. The focus of today's hearing is on the unintended consequences that too often stem from well-intentioned policies.

In addition to our expert economist this afternoon, we'll also hear from two job creators who have experienced this unsettling phenomenon firsthand as they try to hire people and they get reasons why, no, it is better off if I don't take the job that you are offering and that you need to better your business.

Some may charge that the arguments presented here today are uncompassionate to folks struggling to find work, but nothing could be further from the truth. Of course we believe in a safety net for those who have fallen on hard times, but people must not be made worse off as a result of that safety net. What is truly not compassionate is penalizing people for going back to work. We need to rethink and reorganize the way we administer our social safety net so that we empower people rather than dooming them to a life of dependency.

That is our focus today.

Mr. JORDAN. And with that I will turn it over to our ranking member Mr. Cartwright. The gentleman may proceed.

Mr. CARTWRIGHT. I thank you, Chairman Jordan. I certainly look forward to working with you and the members of this subcommittee on issues and policies relevant to strengthening our economy, creating jobs and ensuring reasonable regulation of markets.

I would like to welcome our witnesses here today. I look forward to hearing your testimony and your perspectives on government policies to address the unemployment crisis that has resulted from

America's longest and deepest economic downturn since the Great Depression. Of course, President Obama inherited an economy in free fall. It was losing over 700,000 jobs a month. GDP was contracting at an annual rate of 6 percent. The Great Recession was characterized by a 10 percent unemployment rate, the highest level of unemployment in 30 years.

Congress responded to the economic crisis by passing the Recovery Act. The law included stimulus funding to create new jobs and spur the economy, as well as several provisions that expanded and enhanced safety net programs and tax policies intended to support the unemployed and encourage their efforts to regain permanent employment.

These policies provided critical assistance to individuals facing hardships from the loss of employment. Those policies also helped stimulate economic growth by stabilizing the decline in demand. Economists have estimated that without the Recovery Act and other fiscal policies, unemployment would have topped 11 percent, costing nearly 4 million jobs, and that recession would have been far worse.

Throughout our history we've seen the government soften recessions through investments in our country which help inject needed capital into the economy and create jobs, and therefore, I am extremely concerned that the pending across-the-board spending cuts demanded by the Budget Control Act will damage our still fragile recovery. Slash-and-burn cuts at a time when the economy is growing slowly will stifle growth and intensify the hardships faced by many Americans.

Economists have estimated that the sequestration will cause our economy to shed as many as 2 million jobs. We're busy worrying about unintended consequences of unemployment insurance when we should be worried about the unintended, but clear-as-day consequences of a sequester that will put an additional 2 million people out of work. Instead we should choose to make critical investments that would significantly grow the economy and address this unemployment crisis.

During past economic crises our country has been in far greater debt when put in the proper perspective as a proportion of GDP. At the end of World War I, in 1946 the debt-to-GDP ratio stood at almost 122 percent, but we were able to gradually lower our debt because government investment in public infrastructure spurred decades of immense growth. Our greatest generation came back from war, and our government led the way by giving people an education through the GI bill, and lifting them into the middle class by putting people to work on the Interstate Highway System, and by engaging engineers and scientists to put a man on the moon.

If we want to reduce the deficit, which is a goal all of us share, then getting our economy going is the surest way to do that. Between 2008 and 2009, Federal tax receipts fell by 17 percent, $419 billion, the largest year-over-year drop in 70 years. Corporate tax receipts fell by 54 percent in 1 year. Deficits are more than just about spending; they are also about the economy and revenues by investing in getting our economy going, which will for a time in-

crease the deficit. In the long term the deficit will shrink far faster as tax receipts grow.

That's why sequestration is not the right approach. We need targeted investments so that in the future we can have a more productive economy and more jobs for our citizens. Congress needs to have a balanced approach, raising revenues and cutting unnecessary programs, to get the budget on the right path.

Infrastructure investment was a part of the Recovery Act, it was proposed in President Obama's American Jobs Act, and it was emphasized again in the President's State of the Union Address earlier this week. It's time we take action, propose initiatives, invest in improving school and transportation infrastructure that will create jobs throughout the country. This is how the Federal Government can continue to effectively address the unemployment crisis, and I thank the chairman for calling this hearing and look forward a productive dialogue on these issues.

Mr. JORDAN. I thank the ranking member for his statement.

Let's get right to our panel. Dr. Casey Mulligan is professor of economics at the University of Chicago. A great tradition that university has is of producing outstanding economists.

Dr. Eugene Steuerle is the Richard B. Fisher Chair and Institute Fellow at the Urban Institute. I want to thank you for being with us today.

Ms. Annie Carter is the co-owner and president of her family business, Carter Machine, in Galion, Ohio, so I am especially glad to welcome Annie. Galion is part of the Fourth District of Ohio.

And we also have Dr. Chad Stone, who is the chief economist at the Center on Budget and Policy Priorities.

And I will yield to the gentleman from Georgia to introduce our last witness.

Mr. COLLINS. Thank you, Chairman Jordan.

I am pleased to introduce Stacey Reece. He is a constituent, a former State representative, and longtime member of the Gainesville, Georgia, community.

Mr. Reece is a 15-year veteran of the professional recruiting and staffing industry. He is co-owner of Spherion, a national professional recruiting and staffing franchise. Mr. Reece graduated from the University of North Georgia and University of Georgia banking school. He served as the vice president of the First National Bank in Gainesville for almost 15 years prior to entering the staffing industry. Mr. Reece also served two terms in the Georgia House of Representatives where he served on committees as economic development, appropriations, and held other various leadership roles.

I am pleased to welcome Mr. Reece, and I appreciate you testifying before the subcommittee today.

Thank you, Mr. Chairman. I yield back.

Mr. JORDAN. Thank you, Mr. Collins, and thank you all for being here. We have—pursuant to committee rules, all witnesses are to be sworn in before testifying, so if you will please stand and raise your right hand.

Do you solemnly swear or affirm that the testimony you're about to give will be the truth, the whole truth, and nothing but the truth, so help you God?

Let the record show all witnesses answered in the affirmative.

I have got one more thing to do before we get to Professor Mulligan. Members have 7 days to submit opening statements for the record.

And, Doctor, you are recognized. You know how it works. You get 5 minutes, and I'm a nice guy, so keep it close, and you'll be fine. And then we go right down the list.

WITNESS STATEMENTS

STATEMENT OF CASEY B. MULLIGAN

Mr. MULLIGAN. Thank you, Chairman Jordan, and Ranking Member Cartwright and members of the committee. I appreciate the opportunity and honor to discuss with you today how public policy has changed the reward to work. A multitude of programs affect that reward and thereby affect who is employed.

The monetary reward to work can sometimes be zero or worse, because retaining or accepting a job creates tax expenses and denies subsidies with a combined value that sometimes exceeds the paycheck from working. Nobel laureate James Tobin was a leading Keynesian economist and key advisor to President Kennedy, and he pointedly described 100 percent implicit tax situations. He said that they caused needless waste and demoralization. It is almost as if our present programs of public assistance have been consciously contrived to perpetuate the conditions they are supposed to alleviate.

The monetary reward to working is the difference between the resources a person has available to use or save if she works and what she has available if she does not work. People without jobs or otherwise with low incomes sometimes receive benefits from safety net programs. The benefits are rarely called taxes by the laymen, but economists understand the benefits to have many of their characteristics of tax rates, because a program beneficiary loses some or all of her benefits as a consequence of accepting a job.

The more income that a person receives when not working, the less is the reward to working. The combined effect of taxes and subsidies on the reward to accepting a new job can be summarized as a job acceptance penalty; that is, the effective amount that is lost from paying taxes and replacing benefits associated with not working. I like to express that penalty as a rate, namely, as a percentage of employee compensation. Now, if there were no penalty, then that rate would be zero. But the job acceptance penalty rate can also be large; it can sometimes equal or exceed 100 percent, which means that a person might have more resources available to use or save as a consequence of working less.

Legislation that cuts or credits taxes, so to speak, can nonetheless reduce the reward to working and increase the job acceptance penalty rate if it cuts taxes more for those who work less.

The reward to working matters. High penalty rates are associated with small incentives to seek, create and retain jobs. The consequences of high penalty rates are felt all over the economy, even by people whose individual penalty rates might not be all that high.

At the same time that safety net programs implicitly tax job acceptance, they also implicitly subsidize layoffs, because the pro-

grams absorb some of the income and production that employer and employee lose when an employee stops working. Now, America absolutely must have taxes and safety net programs even though they reduce the reward to working in subsidized layoffs, but if this Congress wants to understand what is happening in the labor market, it would be counterproductive to approximate penalty and subsidy rates as zero or to assume them to be eternally constant regardless of what incentives are embodied in new legislation.

Unemployment benefits are, of course, now available longer into unemployment spells than they were 6 years ago. But also don't forget that new modernization provisions now provide benefits in a variety of circumstances when they were formerly unavailable. While it lasted, the Recovery Act also added a bonus to weekly unemployment checks and helped unemployed people pay for their health insurance. The Food Stamp Program expanded in a variety of dimensions.

The combined effect of these and other changes through 2012 was to reduce the reward to work for most of the nonelderly population. Among the 23 million layoffs experienced by nonelderly American household heads and spouses during the recession, at least 4 million of them had penalty rates near or above 100 percent.

I brought a chart with me today and the height of the bar in that chart is the average penalty among those 4 million layoffs. One hundred percent means that the entire compensation from the job offer, fringe benefits and all, would be devoted to paying added tax expenses and replacing withdrawn benefits. It did not have to be this way. The bar on the right shows what would have happened to the same 4 million penalties if there had been no Recovery Act. The white space at the top is the reward to working. It's what's left over after expenses are paid and withdrawn benefits are replaced. Yes, that reward is small compared to all the expenses, but it was something, and, by looking at the left bar, we can see how the Recovery Act completely erased it.

The chart also shows us how several programs combined to create these penalties. Unemployment insurance is the single largest disincentive, but without the others the reward to working would have been pretty large. It's no surprise that layoffs surge and unemployment durations lengthen during the recession, at the same time when new laws were adding to layoff subsidies and adding to job acceptance penalties. A presumably unintended consequence of the recent safety net expansions has been to reduce the award to working and thereby keep employment rates low, keep unemployment and property rates high, and keep national spending low longer than they would have been if safety net program rules had remained unchanged.

Thank you.

Mr. JORDAN. Thank you, Doctor.

[Prepared statement of Mr. Mulligan follows:]

Work Incentives, the Recovery Act, and the Economy

Testimony for the

Committee on Oversight and Government Reform, U.S. House of Representatives

Subcommittee on Economic Growth, Job Creation and Regulatory Affairs

Hearing on "Unintended Consequences:

Is Government Effectively Addressing the Unemployment Crisis?"

2157 Rayburn House Office Building

February 14, 2013

by

Casey B. Mulligan

University of Chicago

Chairman Jordan, Ranking Member Cartwright, members of the committee: thank you for the opportunity and honor to discuss with you today how public policy has changed the reward to work. A multitude of programs affect that reward, and thereby affect who is employed.

Unfortunately, the monetary reward to work can often be zero, or worse, because retaining or accepting a job creates tax expenses and denies subsidies with a combined value that sometimes exceeds the paycheck from working.

Nobel laureate James Tobin was a leading Keynesian economist and key adviser to President Kennedy, and pointedly described 100 percent implicit tax situations. He said that they "caus[e] needless waste and demoralization.... It is almost as if our present programs of public assistance had been consciously contrived to perpetuate the conditions they are supposed to alleviate." (Tobin 1965, 890)

Overview

A basic economic principle is that the monetary reward to working has important effects on how many people are employed, and how much they work. By definition, the monetary reward to working is the difference between the resources a person has available to use or save if she works and what she has available when she does not work.

People without jobs or otherwise with low incomes sometimes receive benefits from social safety net programs. The benefits are rarely called taxes by laymen, but economists understand the benefits to have many of the characteristics of tax rates because a program beneficiary loses some or all of her benefits as a consequence of accepting a new job. The more income that a person receives when *not* working, the less is the reward to working.

The combined effect of taxes and subsidies on the reward to accepting a new job can be summarized as a job acceptance penalty: that is, the effective amount that is lost from paying taxes and replacing benefits associated with not working. I like to express the penalty as a rate: namely, as a percentage of employee compensation.

If there were no penalty, then the rate would be zero. Thanks to a labyrinth of tax and subsidy programs, the job acceptance penalty rate can equal or exceed 100 percent, which means that the reward to working is zero or less. In such cases, a person might have *more* resources available to use or save as a consequence of working *less*.

Legislation that "cuts" or "credits" taxes can nonetheless reduce the reward to working, and increase the job acceptance penalty rate, if it cuts taxes more for those who work less than it cuts taxes for those who work more.

The reward to working affects behavior. High job acceptance penalty rates are associated with small incentives to seek, create, and retain jobs. The consequences of high penalty rates are

felt all over the economy, even by persons whose individual penalty rates might not be all that high.

At the same time that safety net programs implicitly tax job acceptance, they also implicitly subsidize layoffs because the programs absorb some of the income and production that employer and employee together lose when an employee stops working. Layoff subsidies give employers and employees less incentive to take steps that might avoid or delay layoffs.

America absolutely must have taxes and safety net programs, even though they reduce the reward to working and subsidize layoffs. But if this Congress wants to understand what is happening in the labor market or to the budgets of social programs, it would be counter-productive to approximate job acceptance penalty and layoff subsidy rates as zero, or to assume them to be eternally constant regardless of what incentives are embodied in new legislation.

Of course, unemployment insurance program benefits are now available longer into unemployment spells than they were six years ago. But also don't forget that new modernization provisions now provide unemployment benefits in a variety of circumstances when benefits were formerly unavailable. While it lasted, the 2009 American Recovery and Reinvestment Act (hereafter, ARRA) also added a bonus to weekly unemployment checks, and helped unemployed people pay for their health insurance. The food stamp program expanded in a variety of dimensions.

The combined effect of these and other changes through 2012 was to reduce the reward to work for most of the non-elderly population. Among the 23 million layoffs experienced by non-elderly American household heads and spouses during the recession, at least 4 million of them resulted in penalty rates near or above 100 percent.

The height of the bar in the chart I've shown is the average penalty rate among the 4 million layoffs I mentioned. 100 percent means that the entire compensation from the job offer – fringe benefits and all – would be devoted to paying added tax expenses and replacing withdrawn benefits.

It did not have to be this way. The bar on the right shows what would have happened to the same 4 million penalties if there had been no Recovery Act. The white space is the reward to working – it's what's left over after expenses are paid and withdrawn benefits are replaced. Yes, the reward is small compared to all of the expenses, but it was something and by looking at the left bar we can see how the Recovery Act completely erased it.

This chart also shows us how several programs combined to create these penalties. Unemployment insurance is the single largest disincentive, but without the others the reward to working would have been pretty large.

We shouldn't have been surprised to see layoffs surge during the recession at the same time that new laws were adding to the layoff subsidies or to see unemployment durations lengthen as new rules added to job acceptance penalties. A presumably unintended consequence of the recent safety net expansions has been to reduce the reward to working and thereby keep employment rates low, keep unemployment and poverty rates high, and keep national spending low, longer than they would have been if safety net program rules had remained unchanged.

The remainder of my testimony offers more detail as to penalty and subsidy rate changes in recent years, and how they relate to the government safety net. The testimony is my own and does not necessarily reflect the views of the University of Chicago.

A Labyrinth of Public Policies Combine to Reduce the Reward to Working

The monetary reward to working is the difference between the resources a person has available to use or save if she works and what she has available when she does not work. Federal, state, and local governments deal in massive amounts of resources, and affect the reward to working both in the process of obtaining revenue and in the process of distributing revenue to beneficiaries.

The Bureau of Economic Analysis estimates that income, payroll, sales, and excise taxes amounted to about 23 percent of national income and over 30 percent of the nation's labor income, on average between 2000 and 2010. Even if none of that revenue had been spent on safety net programs, the tax collections by themselves would have reduced the reward to working.

Safety net program spending is also significant, especially during the last several years. Federal, state, and local spending on non-elderly beneficiaries of unemployment insurance, nutrition assistance, Medicaid, and other means-tested subsidies occurred at a combined rate of more than $400 billion per year in 2009 and 2010, measured in fiscal year 2010 dollars (Mulligan 2012). Even if governments had somehow been able to fund these programs without any taxes, the process of distributing the program benefits would have reduced the reward to working.

Legislation that "cuts taxes" can nonetheless reduce the reward to working, and increase the marginal tax rate appropriate for labor market analysis, if it cuts taxes more for those who work less than it cuts taxes for those who work more because the reward to working depends on the difference between taxes (net of subsidies) paid when working and taxes (net of subsidies) paid when not working.

The effects of public policy on the reward to working and thereby the labor market and the economy can be summarized in terms of various measures of marginal tax rates. My testimony discusses two of those measures: the job acceptance penalty rate and the layoff subsidy rate.

The job acceptance penalty and layoff subsidy rates are marginal tax rate concepts related to the decision margins of when to accept a new job and when to experience a layoff. Among the variety of measures that economists use to study the reward to working, these two concepts of the marginal tax rate have the advantages that (a) they readily capture important combined incentive effects of a multitude of tax and subsidy programs and (b) they relate to decisions to exit and reenter employment (Gruber and Wise 1999).

The job acceptance penalty rate is the difference between taxes paid net of subsidies received when working and net taxes paid when not working, sometimes expressed as a fraction of the total compensation to be earned on the new job. The layoff subsidy rate is the difference

between taxes paid net of subsidies received when working on the previous job and net taxes paid after a layoff, inclusive of former employer payroll tax liabilities, sometimes expressed as a fraction of the amount of compensation earned on the previous job.

Thanks to the labyrinth of relevant programs moving large amounts of resources, both rates can equal or exceed 100 percent in some cases, which means that the reward to working is zero or negative. In such cases, a person might have *more* resources available to use or save as a consequence of working *less*.

The reward to working affects behavior. High job acceptance penalty and layoff subsidy rates mean small incentives to seek, create, and retain jobs, and to make the sacrifices of time, hassle, etc., naturally required by employers, customers, and clients in exchange for a paycheck. The consequences of a low reward to working are felt all over the economy, even by persons whose individual reward to working might not be all that low.

The economic distortions created by job acceptance penalty and layoff subsidy rates are not proportional: an increase from 90 percent to 100 percent has a greater effect on incentives than an increase from 40 to 50 percent, which itself has a greater effect on incentives than an increase from 0 to 10 percent. A rate increase from 0 to 10, for example, still leaves a worker with 90 percent of her reward from working, whereas a rate increase from 90 to 100 leaves her with no reward.

Recent Changes in Government Safety Net Rules Related to the Reward to Work

At least a dozen new and important federal and state safety net benefit rules have collectively changed the reward to working, especially for groups whose employment rates are particularly sensitive to safety net benefits.

The unemployment insurance (hereafter, UI) program offers weekly cash benefits to people who have lost their jobs and have as yet been unable to find and start a new one. On average they receive about $300 a week until they start working again, until they stop looking for work, or until their benefits are exhausted. Before the recession, an unemployed person in a typical state without high unemployment would often have his benefits limited to a maximum of twenty-six weeks (United States Department of Labor 2007). The federal law in place before the recession included some local labor market "Extended Benefit" triggers that, based on the statewide unemployment rate, would automatically lengthen the maximum benefit period. These automatic triggers began to extend the duration of benefits around the nation in the middle of 2008 (United States Department of Labor 2011a). At about the same time, the Supplemental Appropriations Act of 2008 included new "Emergency Unemployment Compensation" (EUC) legislation that extended maximum benefit periods for the entire nation. The Worker, Homeownership, and Business Assistance Act of 2009 further extended the EUC periods, so that unemployment insurance benefits could be paid up to 99 weeks (United States Department of Labor 2011b), which continued until 2012.

It is widely recognized that the UI benefit duration rules changed over the past couple of years (see Elsby, Hobijn and Sahin (2010), Shimer (2010), Daly, et al. (2012) and the studies cited in Council of Economic Advisers (December 2010)). Nor is it a surprise that a person

unemployed more than 26 weeks saw her job acceptance penalty rates increase as a result of the rule changes, because they provided benefits that would terminate if and when she went back to work before the benefits were exhausted. More surprising is that other safety net expansions collectively served to increase job acceptance penalty rates significantly more than the new UI benefit duration rules did, not to mention reinforce the labor market impacts of the latter (Mulligan 2012).

The February 2009 American Recovery and Reinvestment Act expanded eligibility by encouraging states to "modernize" (and relax) their UI eligibility requirements by processing earnings histories through an "alternative base period," including persons who quit their job for compelling family reasons, adding 26 weeks of eligibility for persons enrolled in training programs, and/or paying benefits to persons who search only for part-time work (United States Department of Labor 2009). The modernization provisions raised job acceptance penalty and layoff subsidy rates for people who would have found it difficult or impossible to qualify for UI under the previous rules.

The ARRA also raised job acceptance penalty and layoff subsidy rates by exempting the first $2,400 of unemployment benefits received by an unemployed person from 2009 federal income tax (United States Department of Labor 2011b). This provision is an example of a "tax cut" that nevertheless reduced the reward to working because it reduced taxes for people who experienced unemployment sometime during 2009 and did not reduce taxes for people who worked throughout the year.

The ARRA's Federal Additional Compensation (FAC) provision also raised job acceptance penalty and layoff subsidy rates by adding $25 per week to unemployment compensation checks. This $25 per week was not available to people who were working, because unemployment compensation checks are reserved for people who are unemployed.

For laid off workers who wanted to remain on their former employer's health plan, the ARRA's COBRA subsidy offered to pay 65 percent of the cost. For a $13,027 annual family health insurance premium (Crimmel 2010), that subsidy was worth more than $700 per month. Many of the unemployed did not receive the COBRA subsidy, but the subsidy increased job acceptance penalty and layoff subsidy rates for people who did receive it, or would have received it had they not been working.

The Department of Agriculture's food stamp program, now known as Supplemental Nutrition Assistance (SNAP), provides funds to low income households for the purpose of buying food (Social Security Administration 2008), often in conjunction with cash assistance programs. The rules for SNAP eligibility were relaxed in and around the 2008-9 recession as states were eliminating the "asset test," as the 2002 Farm Bill permitted them to do. The asset test elimination increased job acceptance penalty rates because households could receive SNAP benefits based solely on their net income, and not based on the value of their assets. For persons in the few states that retained asset tests, federal asset eligibility rules were relaxed by the 2008 Farm Bill (Eslami, Filion and Strayer 2011, 6).

Both the 2008 Farm Bill and the 2009 ARRA increased the amount of the SNAP benefits paid to eligible households, and thereby increased job acceptance penalty and layoff subsidy rates.

Prior to the recession, able-bodied adults without dependents who were not working or participating in a work program had their receipt of SNAP benefits limited to three months in a three year period (United States Department of Agriculture, Food and Nutrition Service 2012).[1] Entire states could obtain waivers from the work requirement whenever the Department of Labor indicated that the state was eligible for extended unemployment benefits (United States Department of Agriculture, Food and Nutrition Service 2009). The ARRA waived all states through October 2010. Since then, almost all states have obtained waivers pursuant to the Department of Labor triggers (United States Department of Agriculture, Food and Nutrition Service 2011). Altogether, the state-wide waivers and ARRA changed eligibility requirements in the direction of making SNAP eligibility more inclusive than it would have been if able-bodied adults without dependents were required to work (or have their benefits limited), as they typically were before the recession began.

The Housing and Economic Recovery Act of 2008 created a first-time home buyers' tax credit of up to $8000, but it phased out as annual family income varied beyond the income limitation. This provision is another example of a "tax cut" that nevertheless reduced the reward to working because it reduced taxes for people below the annual income limit more than it reduced taxes for people earning above it (people who work fewer weeks during the year are more likely to earn below the annual income limit required to obtain the full credit).

The 2009 ARRA created a refundable personal income tax credit for calendar years 2009 and 2010 called the "Making Work Pay Tax Credit" (hereafter, MWPTC). For most people, the MWPTC had no effect on the reward to working because they or their household would have received the same amount of the credit regardless of an individual's work decision. A few persons saw their reward to working increase from the MWPTC (by itself), a few others saw it reduced.

In contrast to the many provisions cited above, the employee portion of the federal payroll tax was cut – effective between January 2011 and December 2012 – and thereby reduced job acceptance and layoff subsidy rates during that time frame. The combined effect of all of these changes through early 2013 is job acceptance penalty rates for the median household head or spouse about five percentage points greater than they were in 2007, accounting for the fact that many people do not participate in safety net programs even when they are not working (Mulligan 2012). Job acceptance penalty rates have increased even more for less-skilled people and for unmarried people (Mulligan 2013a). Job acceptance penalty rates were at their peaks in 2009 and 2010: during the ARRA.

The Patient Protection and Affordable Care Act was passed in March 2010. As a result of this legislation, Medicaid enrollment and spending are expected to increase significantly in 2014, when the program is made "available to able-bodied adults with incomes up to 133 percent of the federal poverty level" in many states (Sack 2010). By increasing the resources that part of the population can have when their incomes are low, this provision of the Act will increase their job acceptance penalty and layoff subsidy rates. Other provisions of the Act, such as means-tested health insurance premium support, means-tested medical cost sharing, employer penalties,

[1] States could exempt up to 15 percent of such persons from the work requirement, or request a waiver for people in areas with an unemployment rate over 10 percent.

and hardship waivers from the individual mandate, will also further increase job acceptance penalty and layoff subsidy rates.

In Millions of Cases, Public Policy Erased the Reward to Working

Job acceptance penalty and layoff subsidy rates can equal or exceed 100 percent in some cases, which means that the reward to working is zero or negative. My work has begun to estimate the frequency with which non-elderly American workers and their families have been presented with these very high and, as James Tobin put it, wasteful and demoralizing rates. I have also calculated how the frequency might have been different under alternative tax and subsidy rules (Mulligan 2013b).

My estimates consider the combined incentives of several subsidies: unemployment insurance (UI), Federal Additional Compensation (FAC), the ARRA's COBRA subsidy, SNAP, and Medicaid. The dollar value of Medicaid participation is taken as one-half the amount the program spends on medical care per non-elderly non-disabled participant, times the number of family members who are calculated to be Medicaid eligible on the basis of weekly income. Taxes include payroll taxes, state personal income taxes, the regular federal income tax (i.e., the amount on line 44 of Form 1040), and several federal income tax credits: the earned income tax credit (EITC), Child Tax Credit (CTC), Additional Child Tax Credit (ACTC), and Making Work Pay Tax Credit (MWPTC).[2] I also estimate work expenses, such as the expenses associated with commuting to a job.

A worker's job acceptance penalty and layoff subsidy rates depend on the type of job to be accepted (or terminated), the size and composition of his household, and the amount and composition of his household's income. Hundreds of different rates are therefore present in the population, and some are more common than others. I used the Census Bureau's Current Population Surveys to estimate the frequency of the various household and tax situations when the ARRA was in force.

One of the common situations was a middle class dual-earner couple with no children earning about $600 per week and the other earning about $800 plus health insurance. If the latter earner were laid off from his job and participated in the UI program under the ARRA, just a couple of items would by themselves push his penalty rate (for accepting a similar job) over 70 percent: his basic UI benefit, his UI bonus (FAC), payroll taxes, employment expenses, and the ARRA COBRA subsidy. State and federal income taxes would push it even higher.

Accounting for the rich variety of tax and family situations present in the population, I found that, among the 23 million layoffs experienced by non-elderly American household heads

[2] In order to calculate personal taxes and credits, I use the actual personal income tax schedules for a household taking its standard deduction and assume that: the work decision interval is 16 weeks, the person was unemployed six weeks and employed 30 weeks during the remainder of the calendar year, employees with health insurance pay 35 percent of the premiums and those payments are excluded from the payroll and personal income tax bases, and the spouse (if any) earns $600 weekly (plus fringe benefits) throughout the calendar year.

and spouses during 2009 and the second half of 2008, at least 4 million of them resulted in job acceptance penalty rates near or above 100 percent.

The attached chart shows more about those 4 million extraordinary job acceptance penalties. The height of the left bar is the average penalty rate among the 4 million. 100 percent means that the entire compensation from the job offer – fringe benefits and all – would be devoted to paying added tax expenses, paying employment expenses and replacing withdrawn benefits.

It did not have to be this way. The bar on the right shows what would have happened to the same 4 million penalties if there had been no ARRA. The white space between 100 percent and the top of the bar is the reward to working – it's what's left over after tax and other employment expenses are paid and withdrawn benefits are replaced. Yes the reward is small compared with all of the expenses, but it was something and by looking at the left bar we can see how the Recovery Act completely erased it.

The chart also shows us how several programs combined to create these penalties. Unemployment insurance is the single largest disincentive, but without the others the reward to working would be pretty large.

More than two million non-elderly household heads and spouses had layoff subsidy rates near 100 percent, meaning that they could be (and perhaps were) laid off with little or no short-term reduction in their disposable income even if they had to compensate their employer for the UI payroll tax liabilities associated with the layoff as a consequence of "experience-rated" UI financing. The large majority of these workers were in that situation because of the safety net rule changes implemented by the ARRA.

Job acceptance penalty and layoff subsidy rates would have been even higher if the ARRA had been bigger in terms of the help it offered the poor and unemployed. Under a "bigger stimulus," more than half of the 23 million layoffs of non-elderly household heads and spouses could have job acceptance penalty rates near 100 percent. Roughly 20 million non-elderly household heads and spouses could have been laid off from their job with a subsidy rate near 100 percent, even accounting for their employers' payroll tax liabilities.

My findings of large, even confiscatory, job acceptance penalty and layoff subsidy rates are not the result of "cliffs" in transfer program formulas in which many dollars of benefits are lost for earning a single marginal dollar (Yelowitz 1995) because I look at the consequence of more "discrete" decisions of accepting a job, or initiating a layoff, that change calendar year income by thousands of dollars. Instead, my findings reflect the combination of tax and subsidy rules, especially unemployment insurance.

Wage Garnishment and Related Private Sector Activities Raising Marginal Tax Rates

The Internal Revenue Service, Department of Agriculture, and state unemployment agencies are not the only institutions looking at a person's employment status and federal individual income tax return to determine how much she should pay or receive. My own employer, the University of Chicago, and thousands of other universities, colleges, and schools

look at federal income tax returns through their financial aid programs to determine how much a parent should pay for her child's education. While we welcome the opportunity to help students from disadvantaged families, economists have long recognized that financial aid practices affect incentives for students' parents to work and save (Dick and Edlin 1997).

Workers sometimes have their wages garnished by creditors. Garnishments may be a necessary part of a well-functioning credit market, but they also serve to reduce the reward to working by the person whose wages would be garnished.

Even if these private sector actions affecting the reward to work had been constant over time, they still interact with the safety net expansions cited above because the economic distortions resulting from marginal tax rates depend on the sum total of all taxes, subsidies and garnishments that derive from a person's wages. In other words, the presence of private sector marginal tax rates made the government safety net expansions more distortionary than they would have been without the private rates.

Moreover, it does not appear that the private sector's influence on marginal tax rates has been constant over time. A new federal bankruptcy law went into effect in late 2005. Perhaps the most dramatic single increase in job acceptance penalty rates has been associated with the federal guidelines for the settlement of "under-water" home mortgages. Mortgage modification initiatives have been one of the main ways the federal government has sought to reduce home mortgage foreclosures, especially when those foreclosures are motivated by negative home equity (Congressional Oversight Panel 2009, 4). In 2008, the Federal Deposit Insurance Corporation (FDIC), Federal National Mortgage Association (Fannie), and the Federal Home Loan Mortgage Corporation (Freddie) all announced debt forgiveness or "loan modification" formulas. The Treasury Department continued this work under President Obama's administration with its "Home Affordable Modification Program" (HAMP) as part of its "Making Home Affordable Initiative," which replaced the Fannie and Freddie programs.

These programs often recommend a new mortgage payment amount that is lower than the payment specified in the original mortgage contract. More important in terms of marginal tax rates, the new payment is set in proportion to the borrower's income at the time of the modification. The more the borrower is earning, the more she will be required to pay her lender over the next five to seven years, or more. The marginal tax rate on income earned at the time of modification can easily exceed one hundred percent and sometimes exceed two hundred percent as a result of the federal modification guidelines, not to mention the many other taxes and subsidies that also reduce the reward to working (Mulligan 2012; Herkenhoff and Ohanian 2011).

The Income Maximization Fallacy

It is sometimes claimed, by non-economists at least, that the safety net does not prevent anyone from working because everyone strives to have more income rather than less, and would gladly take any available job that paid them more than the safety net did. This "income maximization" hypothesis is contradicted by the most basic labor market observations, not to mention decades of labor market research.

Before the recession began, over 80 million American adults were not working. To be sure, some of them could find no reward in the labor market and would be stuck without gainful employment no matter how lean the safety net got. But many others were not working by choice. You probably know skilled stay-at-home mothers or fathers who could readily find a job but believe that the net pay from that job would not justify the personal sacrifices required. They are examples of people who deliberately do not maximize their income. Other examples are people who turn down an out-of-town promotion in order to avoid relocating their families, and workers who eschew higher paying but less safe occupations. Earning income requires sacrifices, and people evaluate whether the net income earned is enough to justify the sacrifices.

When the food stamp or unemployment programs pay more, the sacrifices that jobs require do not disappear. The commuting hassle is still there, the possibility for injury on the job is still there, and jobs still take time away from family, schooling, hobbies, and sleep. But the reward to working declines, because some of the money earned on the job is now available even when not working.

A related fallacy is that employees would do absolutely anything to avoid a layoff, regardless of the layoff subsidy rate. It's true that employers sometimes experience reductions in demand from their customers, as auto manufacturers and home builders did early in the recession. But layoffs are not always the inevitable result. Employers and employees could adapt to less demand by work-sharing (D. Baker 2011), reducing prices charged to customers, reducing wages, or have pursued a less cyclical line of business in the first place. Heavy layoff subsidies give them less reason to pursue the alternatives to layoffs (Topel and Welch 1980).

Decades of empirical economic research show that the reward to working, as determined by the safety net and other factors, affects how many people work and how many hours they work. To name a small fraction of the many studies: Hoynes and Schanzenbach (2012) show how potential participants stopped working or reduced their work hours when the food stamp program was introduced. Studies of unemployment insurance find that program rules have a statistically significant effect on how many people are employed, and how long unemployment lasts. Yelowitz' (2000) research shows how a number of single mothers found employment exactly when, and where, state-level Medicaid reforms increased their reward from working. Gruber and Wise (1999) and collaborators show how the safety net for the elderly results in less employment among elderly people. Autor and Duggan (2006) and the Congressional Budget Office (2010) explain how the number of disabled people who switch from work to employment-tested disability subsidies depends on the amount of the subsidy relative to the earnings from work. Murphy and Topel (1997) show how poor wage growth among less-skilled men helps explain their declining employment rates during the 1970s and 1980s.

Because economists have identified many other cases in which means-tested and employment-tested subsidies caused people to work less (Krueger and Meyer 2002), it should be no surprise that the same kinds of behavioral responses occurred since 2007: a larger safety net reduced aggregate employment and hours worked.

Programs assisting the poor and unemployed interact with private-sector demand shocks in determining the number unemployed. An adverse demand shock increased unemployment more under the ARRA than it would if the same demand shock had been experienced under 2007 tax and subsidy rules because each dollar that wages are reduced is a bigger proportion of the

reward to work for someone whose reward has been largely whittled away by tax and subsidy programs than it is for someone who keeps a large fraction of what she earns.

Other Misconceptions about the Reward to Working

I previously cited at least a dozen changes in subsidy rules that served to raise job acceptance penalty and layoff subsidy rates. Any one of them may appear insignificant by itself, especially for the purpose of aggregate labor market analysis. But that doesn't mean that the combination of a dozen or more potentially small job acceptance penalty and layoff subsidy rate increases is itself small.

Focusing on just one of any of the safety net expansions is also misleading as to the magnitude of the overall increase in job acceptance penalty rates and therefore potentially misleading as to the sources of the major changes in the labor market since 2007. It is even possible that attention to one program in isolation of the wider safety net could motivate backwards public policy responses.

To see this, imagine that UI rules became more generous, and that added to the number of households who were unemployed and with less income than they have when working. A number of the added unemployed people apply for food stamps, which from the food stamp program's point of view makes it look like "the economy is getting worse," so food stamp officials recommend enhancing food stamp benefits, which further increases the job acceptance penalty rate. But, in this example, the added food stamp applications come from higher job acceptance penalty rates created by UI, and the right food stamp policy response may be to reduce benefits in order to stabilize the overall job acceptance penalty rate. The point of this example is not that the actual safety net expansions were excessive but rather that the economics of the safety net can be different when the safety net is viewed as a whole rather than on a program-by-program basis. The distinction is more than academic: recent events involved expansions of the safety net in many dimensions, and all of that occurred on top of a multitude of other safety net programs.

Another misconception is that most of the growth of federal income security program spending came from the recession, and not from more generous program rules (Krugman 2011). My estimates suggest the 2007 to 2010 rate of increase of inflation-adjusted per capita government spending on Unemployment Insurance and SNAP was at least triple of what it would have been if the real benefit and eligibility rules had remained what they were in 2007 (Mulligan 2012).

Among the hundreds of labor market studies, two of them – Rothstein (2011) and Ben-Shalom, Moffitt and Scholz (2011) – have been misrepresented as showing that recent safety net expansions had no visible effect on employment. Ben-Shalom et al. (2011) looks at the pre-recession safety net, and thereby does not consider the safety net expansions that have occurred since then. Rothstein (2011) looks at the allowable duration of unemployment benefits, finding that benefit durations have a statistically significant effect on unemployment exits, but does not examine a single one of the safety net program parameters that are examined in the chart

attached to my testimony. Neither study considers layoff subsidies or what happens when job acceptance penalty rates approach one hundred percent.

The number of job openings per unemployed person fell sharply during the recession (U.S. Bureau of Labor Statistics 2013). This fact has been misinterpreted by journalists as proving that unemployment subsidies are not a significant factor depressing the labor market. To the contrary, expanding unemployment subsidies can by themselves, or in conjunction with other factors, reduce job openings per unemployed person (Pissarides 2000). If you want to understand what caused and prolonged the recession, you have to look beyond the ratio of job openings to people unemployed.

It is sometimes thought that safety net transactions only impact the people who participate in the programs. To the contrary, the safety net is funded by taxpayers, lenders, owners of government debt, beneficiaries of government programs other than the safety net, or some combination thereof. As a portion of the beneficiaries opt to earn less, they also opt to spend and save less, as their household budget constraint frequently requires. They lawfully pay less tax. Businesses anticipate having fewer employees and invest less. These behavioral changes are bad news for employers in general, for people who produce the consumer and investment goods that beneficiaries would be buying if they were back at work (and goods the program funders would be buying if they were not funding the expansions), and for people who live in places like Michigan whose economies are especially intensive in the production of such goods (Galí, Gertler and Lopez-Salido 2007).

Research has shown that the poor and unemployed tend to quickly spend what they have on basic needs, which is why helping them is intrinsically valuable (Gruber 1997), but "stimulus" advocates sometimes further assert that spending patterns of the poor are why redistribution serves as a great boost in total spending and thereby total employment. Even if redistribution did not depress the reward to working, the stimulus assertions would be wrong because they ignore the spending of the people who fund the programs. Redistributing resources to the poor from everyone else changes the composition of spending and employment in the direction of industries like discount groceries that disproportionately serve poor customers and away from industries like high-end restaurants serving relatively few poor customers, but redistribution by itself has little effect on *aggregate* spending.[3]

When redistribution is combined with increases in job acceptance penalties and layoff subsidies – as a number of recent policies have done – it significantly reduces aggregate spending because people typically spend less when they are not working.[4]

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[3] Redistribution to the poor may reduce aggregate labor demand if the poor tend to purchase goods and services that are less labor intensive in their production than are the rest of the goods and services in the economy. Also note that (a) government transfers are very different from government purchases of goods and services such as military spending or highway construction, which have been shown to significantly increase GDP in many instances (if nothing else, government purchases are automatically considered part of GDP, whereas transfers are not), and (b) aggregate spending is the sum of investment spending, consumer spending, government purchases, and net exports.
[4] Aguiar and Hurst (2005). To the extent that it redistributed resources to low-income families, the 2011-12 payroll tax cut is an exception because it achieved its redistribution while increasing the reward to work.

Conclusions

The bottom line is that helping the poor and economically vulnerable has a price in terms of labor market inefficiency. Since 2007, we have been paying more of that price: American public policies moved significantly in the direction of less labor market efficiency, and perhaps more than was necessary for providing assistance to those who need it.

First of all, 100 percent job acceptance penalty rates are difficult to justify as a reasonable balance between equity and efficiency and the recent safety net expansions documented here added millions to the number of people facing such rates.

Second, rather than making people feel safer, a number of the safety net expansions may themselves be a source of uncertainty via the political process because, among other things, they must be repeatedly renewed by Congress, and taxpayers are still unsure of exactly who will pay for them (Baker, Bloom and Davis 2011).

Third, my testimony explains how multiple parties – governments, lenders, and courts – have claims on the income that appears on a person's tax return. Multiple tax collectors can lead to excessive marginal tax rates, as each individual collector might not value the effect of his extraction on the revenues received by the other collectors (Olson 2000).

For these reasons, it is likely possible to reduce job acceptance penalty rates, reduce layoff subsidy rates, and enhance labor market efficiency without giving up much or any of the genuine benefits America enjoys from safety net programs.

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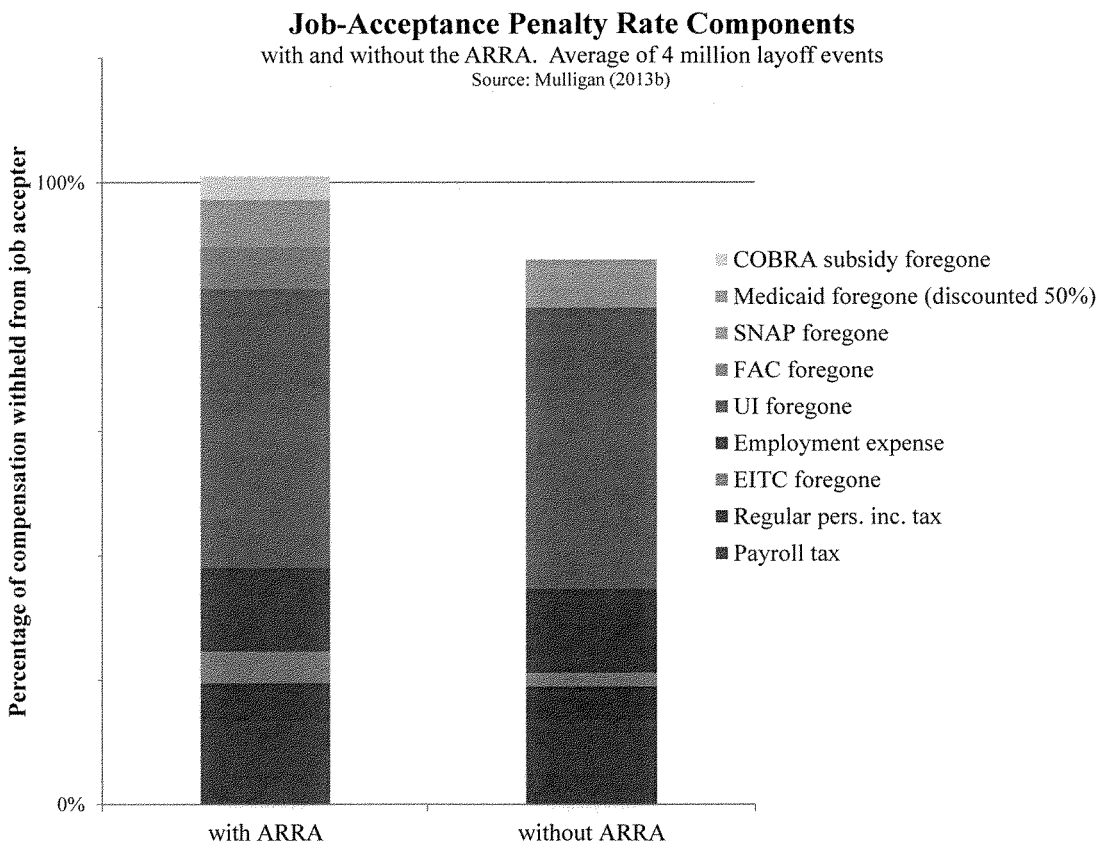
Job-Acceptance Penalty Rate Components
with and without the ARRA. Average of 4 million layoff events
Source: Mulligan (2013b)
Percentage of compensation withheld from job accepter
100%
0%
with ARRA
without ARRA
COBRA subsidy foregone
Medicaid foregone (discounted 50%)
SNAP foregone
FAC foregone
UI foregone
Employment expense
EITC foregone
Regular pers. inc. tax
Payroll tax

Mr. JORDAN. We will go next to Dr. Steuerle.

STATEMENT OF C. EUGENE STEUERLE

Mr. STEUERLE. Thank you, Mr. Chairman, Mr. Cartwright and members of the subcommittee. I appreciate the opportunity to testify before you today on labor force participation and our Nation's tax and social welfare systems.

I begin by putting all of this into a much broader context that goes beyond just what's happened in the Great Recession. Modern society must begin to adjust to a very different labor force dynamic than prevailed in the last half of the 20th century. At that time baby boomers, women, and a more educated young population entered the workforce. Today all of those forces of growth for labor force as well as their positive impact on being able to come out of recessions and promote demand have gone by the wayside. And today we also face extended joblessness among the young, the unemployed and the disabled. Labor force participation among the young, particularly men, has trended downward for the past three decades, only exacerbated by the Great Recession.

Evidence shows that prolonged periods of labor force separation create longer-term problems. They depress future earnings for such workers, work habits can dissipate, and feelings of depression can set in.

Now, consider whether our social welfare system is starting to adjust to these new circumstances. These systems have largely been devoted over time to providing higher levels of consumption to people, but consequently have added to the disincentives for work and saving.

Now, one can disagree, and there is disagreement in the literature, on the extent of past successes, yet still agree that at the margin we ought to be shifting more of our dollars towards government programs aimed at opportunity, those that favor education, work and saving, and put less emphasis on consumption.

Now, our social welfare system affects work in two ways. First, the additional consumption provided to people or income is often sufficient for some of them simply to reduce their labor supply; and, second, a major focus of this hearing, families can face prohibitively high penalties for additional work.

Consider particularly households with children. Right now our combined tax and spending systems encourage labor force participation until family income reaches the poverty level. This has actually been a positive aspect of welfare reforms and earned income credit reforms in previous decades. That is, we have favored movement into the workforce except for the unemployment case that Dr. Mulligan points to. But after reaching about poverty level, low- to moderate-income households often face marginal tax rates of about 50 to 60 percent merely if they participate in universally available programs like food stamps, now SNAP, the earned income credit, and soon, by the way, the new health exchange subsidies, which also have their own implicit tax rate on additional earnings.

How benefits change with income levels is shown in figure 1 in my testimony. Meanwhile, households who participate in other programs such as limited entitlement programs such as the Temporary Assistance for Needy Families or housing subsidies often

face tax rates of 80 to 100 percent. And again, these figures are independent of the unemployment compensation examined by Dr. Mulligan.

The problem of high effective marginal tax rates facing low-income workers especially affects households looking to move out of poverty toward middle-class status. I deem this the "twice poverty trap." Now, one thing have we learned from public finance is the taxes have significant effects on portfolio behavior even if there is less certain effect on work and saving. Not getting married has now become the major tax shelter for low- and moderate-income households with children facing these high marginal tax rates. By avoiding marriage they avoid the high tax rates that would be implicitly borne by the household when they marry and they combine their incomes and thereby lose benefits.

These high tax rates and marriage penalties arising in these systems occur in part because of the piecemeal fashion in which they are considered. Congress has designed so many direct and indirect taxes and phaseouts that it can have little idea of how it affecting the true returns to work for large portions of the population.

So just to give you some idea of these implicit taxes and where they sit, they are everywhere. They are in TANF; in SNAP, or food stamps; they are in Medicaid and the new health exchange subsidies; they are in PEP and PEAS, which we just reenacted as part of the recent tax reforms; they are in Pell grants and student loans; American Opportunity credits and Lifetime Learning tax credits; housing vouchers or low-income housing tax credits; child tax credits or income credits; Medicare Part B and Part D; Social Security exemption from taxation of supplemental security income; school lunches and Child Care and Development Fund; Head Start and Early Start; Special Supplemental Nutrition Programs for Women, Infants and Children, or WIC; child independent care tax credits; retirement saving credits; premium assistance credits; and unemployment compensation, workers compensation. All of these have implicit tax rates in them.

My point simply is this, that our modern economy requires modern approaches to social welfare and taxation. Many compromises I believe can cut across traditional liberal and conservative boundaries by maintaining a progressive agenda, yet emphasizing better the work, education and saving requirements required for the modern economy and required for the modern worker to succeed. At a minimum we need to begin approaching our wide assortment of programs, benefit phaseouts and tax rates in a much more integrated fashion. It's hard to design programs well if we lack even basic understandings of all the ways they interact.

Mr. JORDAN. Thank you, Doctor.

[Prepared statement of Mr. Steuerle follows:]

Statement of

C. Eugene Steuerle

on

Labor Force Participation, Taxes, and the Nation's Social Welfare System

Committee on Oversight and Government Reform
United States House of Representatives

February 14, 2013

C. Eugene Steuerle is the Richard B. Fisher chair and an Institute Fellow at the Urban Institute. He is indebted particularly to Adam Carasso, Linda Giannarelli, Elaine Maag, Caleb Quakenbush, Gillian Reynolds, and Katherine Toran for past and current work with him on both mobility and marginal tax rates. All opinions expressed herein are solely the author's and should not be attributed to any of these individuals or any organizations with which Steuerle is associated.

Mr. Chairman and members of the Subcommittee:

Thank you for the opportunity to testify before you on the relationship between labor force participation and our nation's tax and social welfare systems. Although there is some disagreement over how these systems affect work efforts, there is almost no disagreement that they are designed in piecemeal fashion, leading to various unfair, inefficient, and somewhat strange effects. Nor do most disagree that whatever the failures or successes of these structures in the past, they must be reformed to meet 21st century demands and economic conditions.

The Economic and Demographic Context

Even before the Great Recession, it was becoming clear that modern society must begin adjusting to a very different labor force dynamic than what prevailed in the last half of the 20th century. Historical sources of labor force growth have now ended as we face new challenges of high unemployment and declining labor force participation among younger workers, the long-term unemployed, and the disabled.

For many decades, our labor force expanded and grew more competitive with the entrance of baby boomers and women into the economy. These new entrants on average had attained higher levels of educational success than those who were leaving the workforce. But boomers are now retiring, and catch-up in the labor force participation of women has leveled off. The trend of retiring elderly workers being replaced by a more educated younger population has largely ended as well; for the first time in modern American history, young workers entering the workforce are not more highly educated than the older age groups they are replacing.

At the same time, the United States is no longer as economically dominant as it once was. Increasing competition from abroad has particularly cut into the incomes possible for those with limited education.

Meanwhile, there has been rising concern about extended joblessness among the young, the unemployed, and the disabled.

Evidence shows that shows that prolonged periods of labor force separation depress future earnings for such workers. Labor force participation among the young, particularly men, and especially young black men has trended downward over the past three decades. Only some of this can be attributed to increased full-time schooling. Even into their late twenties and thirties, many men remain separated from the labor force. Since the 1980s, labor force participation rates among men in this age range have fallen between 5 and 6 percentage points. Among black men, the decline is more than 8 percentage points.

The consequences of prolonged separation from the formal economy often extend beyond the period of unemployment. Work habits can dissipate and feelings of depression can set in. Long-term asset development has also been held in check for both the young and people of color.[1]

Now add to this labor force environment during the Great Recession. Employment rates plummeted and are recovering at an extraordinarily low rate. The effect extends from unemployment to underemployment, including workers moving to part-time work and dropping out of the labor force entirely.

These labor force pressures reinforce each other by reducing demand, including the demand that formerly came from population growth and the formation of more new households who then bought goods and services, including housing.

Social Welfare and Tax Systems Oriented toward Consumption

Many of the forces I just discussed operate independently of government programs. But they raise the broad question of how to reform a social welfare system largely constructed for a period very different from today.

These social welfare systems largely were oriented around providing minimum levels of consumption to people. On many fronts, particularly among the elderly, they successfully reduced poverty, although progress has slowed considerably in recent decades relative to the additional sums that have been spent. Efforts to expand consumption additionally tend to reduce work and saving.

Also, when in the midst of a recession or early in recovering from one, offering tax breaks to the broad middle class may provide both less (Keynesian) demand-side stimulus and less supply-side incentive than efforts focused on job subsidies aimed toward those with low to modest incomes.

One can disagree on the extent of past success, yet still agree that at the margin we ought to be shifting more dollars toward government programs aimed at opportunity—those that tend to favor education, work, and saving.

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[1] For instance, my Urban Institute colleagues and I have been examining the limited asset building among people of color and younger people. From 1983 to 2010, black and Hispanic average net worth stagnated at about 1/5 the average net worth of whites, working against traditional patterns of upward mobility among more disadvantaged groups. Meanwhile, despite an economy twice a rich as it was a quarter-century or so ago, young people today have no more net worth than their parents when they were young. By contrast, those of us in older age groups are on average about twice as wealthy as our parents.

Effective "Tax" Rates for Low- and Moderate-Income Households

Our social welfare systems affect work in two ways. First, the additional consumption or income provided is sufficient for some simply to reduce their labor supply.

In addition to the effect of this additional income or consumption support on work efforts, families can face prohibitively high penalties for additional work. Accepting a higher paying job could mean a steep cut in child care assistance for a single worker with children, for instance. For some, the rapid phaseout of benefits can offset or even more than offset additional take-home pay. Asset tests in means-tested programs create similar barriers to saving.

One way to look at the disincentives facing lower-income households is to consider the effective tax rates they face, both from the direct tax system and from phasing out benefits from social welfare programs.

Consider particularly households with children, as Congress has provided many benefit programs that phase out to such households. Right now our combined tax and spending systems encourage labor force participation until family income reaches the poverty level. After that, low- to moderate-income households often face marginal tax rates of about 50 or 60 percent if they participate in universally available programs like SNAP (formerly food stamps), the EITC, and (soon) the new exchange subsidies, while some households face rates of 80 percent or higher if they participate in programs with limited enrollment, like TANF or housing subsidies.

Figures 1 and 2 display the benefits available to a single mother with two children in 2011 under these two cases. The first case, what I call the "universal" case, shows the benefits available to anyone whose income was low enough to qualify for them, namely nutrition assistance and tax benefits. The second case adds to those benefits narrower assistance—TANF and housing subsidies and supplements to nutrition assistance—that is available to some households but not to others based on availability, time limits, and other criteria. Because health reform will soon alter the delivery of health benefits in an important way, in both cases I assume that the provisions of the Affordable Care Act are in effect.

Families are eligible for a large amount of assistance at very low annual incomes but then lose that assistance very quickly as they move into moderate income ranges. Figure 3 shows the effective marginal tax rate that derives from income, Social Security, and state taxes, combined with the phaseout of these benefits. As can be seen, tax rates begin to spike somewhere above $10,000 or $15,000.

These taxes derive largely from a liberal-conservative compromise that emphasizes means testing as a way of both increasing progressivity and saving on direct taxes needed to support various programs. Although low- and moderate-income households are especially affected, middle-income households face these expenditure taxes, too, through the phaseout of Pell grants and child credits, the gradual removal of "preferences" in the alternative minimum

tax and of the exemption of Social Security benefits from taxation, and the forthcoming exchange subsidies under ACA.

Recent work at the Urban Institute has examined this issue in greater detail.[2] Using the Institute's net income change calculator (NICC),[3] we looked at the effective marginal tax rates facing hypothetical families as they moved between levels of poverty. The tables included at the end of this testimony summarize our findings for each state for a joint return with two children participating in SNAP and TANF.

Despite changes to welfare since the end of the AFDC program in the 1990s, the problem of high effective marginal tax rates facing low-income workers looking to move out of poverty toward middle-class status—what I deemed "the twice poverty trap"—appears to have persisted in many states. While households receiving assistance often face negative marginal rates for moving into the labor force, income and payroll taxes and the phaseout of benefits imposes troublingly high rates on them if they move from poverty-level income to 150 or 200 percent of the poverty level.

Note that the effects shown here deal with permanent moves off programs. They exclude some of the effects from temporary support derived from unemployment compensation or delays in some welfare programs before benefits are clawed back.

A recent CBO study largely corroborates our findings.[4] It found that median marginal tax rates were steady in the 30 percent range on incomes between 50 and 350 percent of the poverty level, but many families, particularly at lower income levels, could face rates much higher. Households with earnings less than 150 percent of the poverty level experienced the most variability in the rate they faced, as did single-headed households with children.

Marriage penalties

One thing we have learned in public finance is that taxes have significant effects on portfolio behavior, even if there is less certain effect on work and saving. Not getting married is the major tax shelter for low- and moderate-income households with children. In many low-income communities around the nation, marriage is now the exception rather than the rule.

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[2] Elaine Maag, C. Eugene Steuerle, Ritadhi Chakravarti, and Caleb Quakenbush, "How Marginal Tax Rates Affect Families at Various Levels of Poverty," http://www.taxpolicycenter.org/UploadedPDF/412722-How-marginal-Tax-Rates-Affect-Families.pdf.

[3] Available at http://nicc.urban.org/. Initial development of NICC was funded by the Annie E. Casey Foundation as part of the Low Income Working Families project. Funding for the update of the 2008 rules was provided, in part, by HHS/ASPE. Additional funding came from the John D. and Catherine T. MacArthur Foundation. NICC's development built on an earlier tool, the Marriage Calculator, developed at the Urban Institute under contract with HHS/ACF. NICC's calculations are performed by an adapted version of the TRIM3 microsimulation model. The standard version of TRIM3 is funded and copyrighted by HHS/ASPE and developed and maintained by the Urban Institute.

[4] "Effective Marginal Tax Rates for Low- and Moderate-Income Workers," http://www.cbo.gov/publication/43709.

Marriage penalties or subsidies are assessed primarily for taking wedding vows, not for living together with another adult.[5] Those who do not feel morally compelled to swear fidelity in religious or public ceremonies for the most part do not suffer the penalties. Our tax and welfare system thus favors those who consider marriage an option—to be avoided when there are penalties and engaged when there are bonuses. The losers tend to be those who consider marriage vows sacred.

At another extreme in this story is another group: young, uneducated, childless men or noncustodial fathers, who have seen their wages in unskilled labor decline in real terms over time.[6] Because many benefits are targeted toward households with children, these men also find themselves shut out from most forms of assistance. The system also makes young men's economic contributions a liability to their parents, relatives, potential spouses, and children in terms of the government benefits that would be lost, essentially reinforcing their noncustodial status. For example, a working young man who marries a working single mother could cause here to lose child care assistance and part of her EITC.

These effects of marginal tax rates extend well beyond the marriage patterns of low-income families. Divorced couples allocate child support to maximize future college aid. Some couples avoid remarriage to avoid losing Social Security or pension benefits. As noted, the disabled sometimes avoid work to keep Medicaid, while some unemployed delay going back to work.

Our Discombobulated System and Options for Reform

The high rates and marriage penalties arising in these systems occur in part because of the piecemeal fashion in which they are considered. Congress has designed so many direct and indirect taxes and phaseouts that it can have little idea of how it is affecting the true returns to work for large portions of the population.

Implicit taxes are everywhere, whether in TANF or SNAP (formerly food stamps), Medicaid or the new exchange subsidy, PEPS (the personal exemption phaseout) or PEASE (the limitation on itemized deductions), Pell grants or student loans, American Opportunity Credits or Lifetime Learning Tax Credits, housing vouchers or low-income housing tax credits, child tax credits or earned income tax credits, Medicare Part B or Medicare Part D, Social Security exemption from taxation or Supplemental Security Income, school lunches or Child Care and Development Fund, Head Start or Early Start, Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) or child and dependent care tax credits (CDCTC), retirement savings contributions credits (saver's credits) or premium assistance credits

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[5] See Adam Carasso and C. Eugene Steuerle, "The Hefty Penalty on Marriage Facing Many Households with Children," http://www.urban.org/UploadedPDF/1000844_marriage_penalty.pdf.

[6] Adam Carasso, Harry J. Holzer, Elaine Maag, and C. Eugene Steuerle, "The Next Stage for Social Policy: Encouraging Work and Family Formation among Men," http://www.urban.org/UploadedPDF/411774_encouragingwork.pdf.

(beginning in 2014), unemployment compensation or workers compensation. These implicit taxes combine with explicit taxes to create inefficient and often inequitable, certainly strange and anomalous, incentives for many households.

Efforts to design benefit packages more comprehensively could greatly improve both the incentives faced by families and the quality and choice of benefits they receive.

One option is to integrate the many separate programs for which families are eligible into a single bundle within which recipients would have the flexibility to allocate resources to meet their specific needs.[7] For instance, a worker could opt to spend less of his or her voucher on food in favor of better housing or child care. Such a system could be designed so the selection of services and goods within the bundled set must be agreed to by those directly advising and guiding recipients.

Even without formal restructuring of many of these programs, innovative approaches can be tried. Catholic Charities, for instance, supports a National Opportunity and Community Renewal Act for a pilot project that is people focused and case managed, based on local community opportunities. In the suggested programs under this experiment, a person might qualify for help, but the exact nature would depend on agreement between the case manager and client, allowing them to tie together and reallocate resources for which the client is eligible. That reallocation would likely increase labor force participation, as it would be largely aimed at improving opportunity and addressing issues that cause the poverty in the first place.

Another partially integrated approach by policymakers would involve setting a maximum marginal tax rate across tax and transfer programs for families receiving assistance. Phasing out benefits at one rate instead of several can temper the disincentives to increasing earnings and allow workers to reallocate their remaining assistance in a way suited toward their needs.

Separating childrearing incentives from work incentives could help. The EITC provides wage subsidies to low-income workers raising children, but then leaves out other low-wage workers and usually creates high tax rates when two earners marry. Reform could separate out the subsidy for children from that for low-income workers. As I noted earlier, I think this would be especially appropriate during a recovery from a recession.

There will inevitably be trade-offs involved in any such reform. A reform that creates only "winners" is unlikely. The process of slower benefit phaseouts will require either more expensive programs explicitly financed by taxpayers or less generous assistance for someone else.

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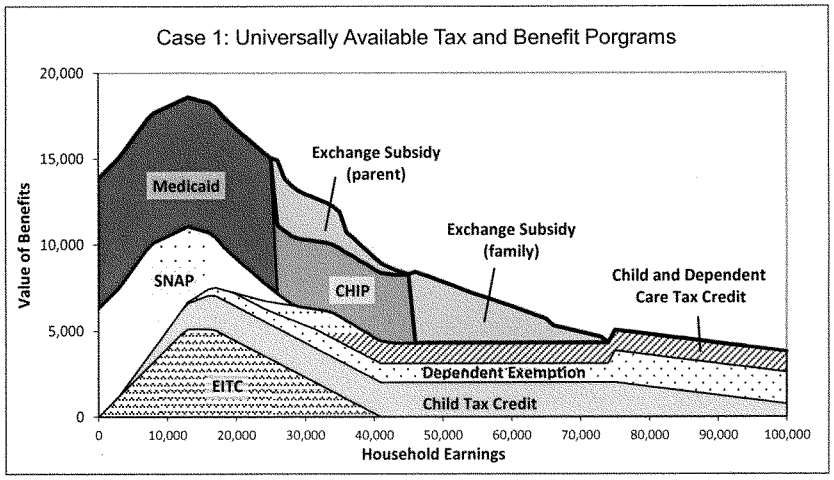
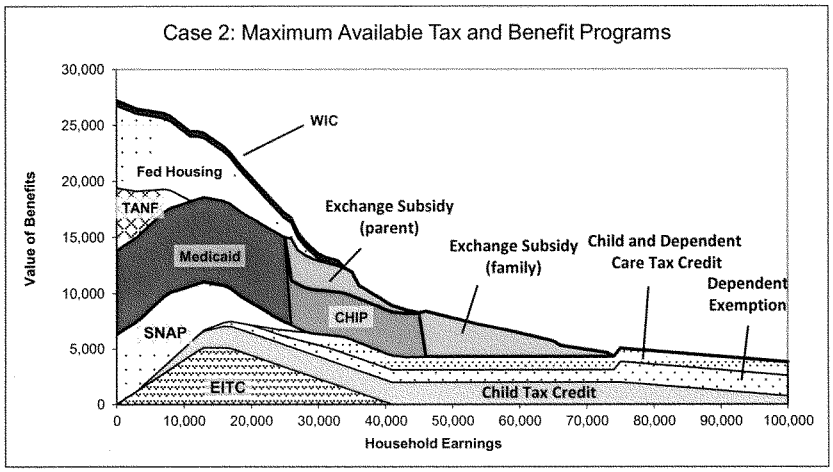
[7] See Robert Lerman and C. Eugene Steuerle, "Structured Choice versus Fragmented Choice: Bundling of Vouchers," from *Vouchers and the Provision of Public Services* (Washington, DC: Urban Institute Press, 2000).

Conclusion

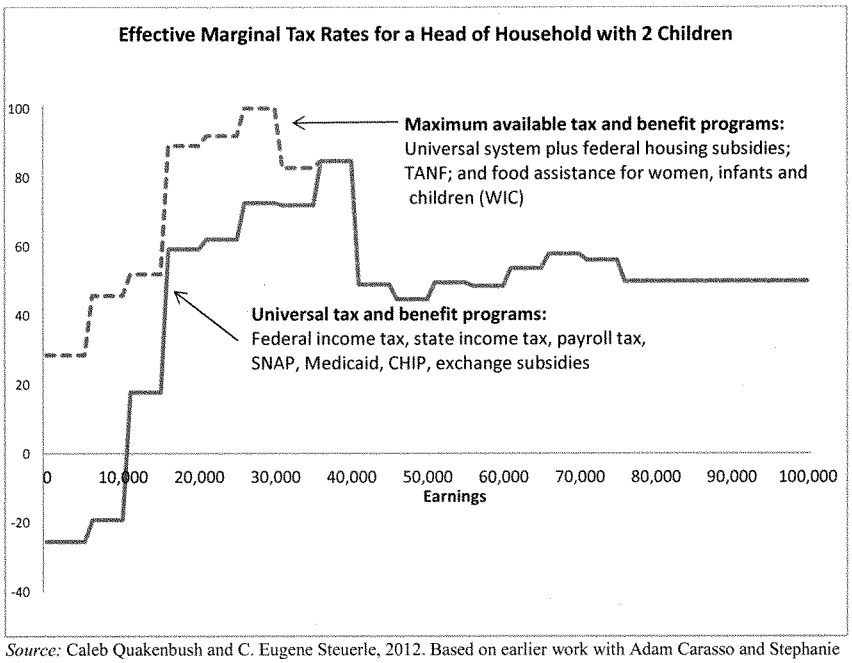
Our modern economy requires modern approaches to social welfare and taxation. Many compromises can cut across traditional liberal and conservative boundaries by maintaining a progressive agenda, yet emphasizing better the work, education, and saving requirements for today's economy.

At a minimum, we need to begin approaching our wide assortment of programs, benefit phaseouts, and tax rates in a more integrated fashion. It's hard to design programs well if we lack even basic understanding of all the ways they operate and combine.





Source: Caleb Quakenbush and C. Eugene Steuerle, 2012. Based on earlier work with Adam Carasso and Stephanie Rennane.
Notes: Heath benefits are calculated as if the Affordable Care Act had been fully implemented in 2011.



Source: Caleb Quakenbush and C. Eugene Steuerle, 2012. Based on earlier work with Adam Carasso and Stephanie Rennane.

Notes: Includes TANF, food stamps, federal and state income taxes, and the employee portion of payroll taxes. The effective marginal rate is the marginal tax rate faced in the formal tax system (federal, state, and payroll) in addition to the rates arising from the reduction in disposable income from the loss of transfer benefits. The tax rules used for federal and state income taxes are for calendar year 2011. The payroll tax rate does not include the temporary reduction of the employee portion of the tax. Health benefits calculated as if the Affordable Care Act had been fully implemented in 2011.

Table 1. Married with Two Children - Effect of Moving from Various Earnings Levels for People Receiving TANF and Food Stamps; Equal Earnings in 12 Months

	$0 Earnings to Half Poverty	Half-Poverty to Poverty	Poverty to 150 Percent of Poverty	150 Percent of Poverty to Twice Poverty	$0 to Poverty	$0 to Twice Poverty
Alabama	-78.8%	22.8%	51.2%	61.4%	-28.0%	6.5%
Alaska	-44.8%	49.9%	75.0%	55.8%	2.5%	29.3%
Arizona	-40.9%	18.5%	57.1%	63.7%	-11.2%	16.0%
Arkansas	-59.7%	19.2%	64.1%	59.9%	-20.3%	13.8%
California	-32.0%	53.6%	59.7%	66.4%	10.8%	27.5%
Colorado	-55.3%	34.5%	57.1%	61.8%	-10.4%	16.9%
Connecticut	-65.1%	69.2%	55.0%	62.9%	2.0%	22.7%
Delaware	-71.4%	42.0%	61.8%	56.6%	-14.7%	17.1%
District of Columbia	-66.1%	44.2%	68.4%	52.0%	-10.9%	21.7%
Florida	-46.9%	18.5%	54.1%	66.4%	-14.2%	13.1%
Georgia	-49.9%	20.6%	59.8%	60.4%	-14.7%	15.7%
Hawaii	-71.0%	55.9%	102.9%	59.5%	-7.6%	29.3%
Idaho	-52.9%	18.5%	56.0%	60.4%	-17.2%	13.5%
Illinois	-48.9%	34.6%	58.0%	62.3%	-7.2%	18.7%
Indiana	-58.9%	30.9%	58.7%	61.8%	-14.0%	15.4%
Iowa	-49.7%	38.1%	61.9%	58.2%	-5.8%	21.3%
Kansas	-52.7%	34.7%	62.7%	59.0%	-9.0%	19.6%
Kentucky	-53.8%	21.9%	68.3%	60.6%	-15.9%	16.9%
Louisiana	-78.8%	42.0%	58.2%	61.7%	-18.4%	13.0%
Maine	-48.8%	47.7%	55.3%	60.4%	-0.6%	22.0%
Maryland	-32.4%	31.7%	62.8%	55.7%	-0.3%	25.0%
Massachusetts	-38.9%	44.4%	62.1%	57.8%	2.7%	25.9%
Michigan	-27.6%	23.4%	60.3%	59.9%	-2.1%	22.5%
Minnesota	-47.2%	31.7%	64.3%	50.9%	-7.7%	22.7%
Mississippi	-65.5%	19.1%	57.9%	61.3%	-23.2%	10.5%
Missouri	-59.2%	29.3%	59.3%	60.4%	-14.9%	15.4%
Montana	-24.4%	20.4%	58.6%	60.6%	-2.0%	22.0%
Nebraska	-47.7%	23.5%	58.4%	60.7%	-12.1%	16.6%
Nevada	-72.1%	18.6%	36.8%	66.4%	-26.7%	2.6%
New Hampshire	-29.2%	36.4%	54.1%	66.4%	3.6%	22.5%
New Jersey	-79.7%	21.2%	41.6%	60.0%	-29.3%	4.0%
New Mexico	-45.7%	34.7%	57.7%	61.3%	-5.5%	19.8%
New York	-40.5%	46.7%	64.8%	55.4%	3.1%	27.4%
North Carolina	-55.5%	19.8%	60.7%	59.2%	-17.8%	14.5%
North Dakota	-86.9%	18.5%	55.5%	64.3%	-34.2%	3.5%
Ohio	-44.8%	33.6%	57.5%	62.7%	-5.6%	19.3%
Oklahoma	-47.7%	19.7%	60.2%	59.8%	-14.0%	16.2%

Table 1. Married with Two Children - Effect of Moving from Various Earnings Levels for People Receiving TANF and Food Stamps; Equal Earnings in 12 Months

	$0 Earnings to Half Poverty	Half-Poverty to Poverty	Poverty to 150 Percent of Poverty	150 Percent of Poverty to Twice Poverty	$0 to Poverty	$0 to Twice Poverty
Oregon	-25.6%	23.5%	64.3%	56.1%	-1.1%	24.9%
Pennsylvania	-32.2%	18.5%	54.1%	54.2%	-6.9%	20.0%
Rhode Island	-38.9%	38.9%	55.3%	59.5%	0.0%	22.6%
South Carolina	-76.4%	42.9%	54.1%	64.9%	-16.7%	12.2%
South Dakota	-21.5%	18.5%	54.1%	66.4%	-1.5%	19.8%
Tennessee	-79.4%	35.9%	54.1%	66.4%	-21.7%	9.2%
Texas	-70.9%	35.6%	54.1%	66.4%	-17.7%	11.3%
Utah	-42.0%	34.7%	57.9%	60.0%	-3.7%	21.1%
Vermont	-33.8%	35.8%	63.3%	56.2%	1.0%	25.7%
Virginia	-72.0%	53.3%	59.7%	56.3%	-9.4%	19.4%
Washington	-30.0%	34.4%	54.1%	66.4%	2.2%	21.7%
West Virginia	-44.7%	19.7%	61.5%	62.0%	-12.5%	16.8%
Wisconsin	-23.3%	20.4%	62.7%	56.0%	-1.5%	24.3%
Wyoming	-49.5%	18.5%	54.1%	66.4%	-15.5%	12.4%
Simple Average	-51.2%	31.8%	59.2%	60.6%	-9.7%	18.1%
High	-21.5%	69.2%	102.9%	66.4%	10.8%	29.3%
Low	-86.9%	18.5%	36.8%	50.9%	-34.2%	2.6%

Source: Elaine Maag, C. Eugene Steuerle, Ritadhi Chakravarti, and Caleb Quakenbush, 2012, "How Marginal Tax Rates Affect Families at Various Levels of Poverty," *National Tax Journal* 65(4): 759–82.

Notes: Includes TANF, food stamps, federal and state income taxes, and the employee portion of payroll taxes. Calculations performed using the Urban Institute's net income calculator.

Mr. JORDAN. Ms. Carter, you're up.

STATEMENT OF ANDREA L. CARTER

Ms. CARTER. Thank you for inviting me to testify today.

Mr. JORDAN. Make sure your microphone is on there.

Ms. CARTER. Thank you for inviting me to testify today. My name is Annie Carter. I am the president and co-owner of Carter Machine Company. We are located in Galion, Ohio. Our company designs, repairs and manufactures hydraulic and pneumatic cylinders mainly for the steel industry, and baling industry, recycling industry, large presses, material movement. We currently have 57 employees, but we would greatly benefit by having an effective employee rate of about 70 to 75 people.

Manufacturing was the foundation and the backbone of this country, and it is now considered something that people will do if they don't have any other choices. Our company is comprised of 50 percent administrative staff, such as engineers, production, purchasing, computer programmers, human resources, and 50 percent skilled labor. Our business is a custom design business. We—our company is built on a quality platform, and we require machinists and staff that have above-level skills in order to make the products that we market. This can include older-style manual equipment and also sophisticated CNC equipment.

It's very difficult for us to find people that want to do any of those jobs, let alone run the older, manual, more sophisticated, let's say, skill-related machining than the regular CNC-type equipment.

We have a real need for manufacturing or skilled trades in our area. We have a true deficit through many of our companies. Our individuals are proud to be machinists, they are proud of our product, and they take their jobs very seriously and consider themselves something more than what they are considered today in the outside world by people that are looking for jobs.

We've reached a point in society where it's not honorable to learn a trade or to perfect a skill. It's considered as something, again, people do when they don't have anything else to do. I've spoken to high school students many times who are consistently fed the career path through college. They don't know what a trade job is, and they don't consider that an option for them in the long term. I don't think they believe they can make a living at the trades because of what they're being taught. And they really don't have any exposure anymore through wood shop, metal shop, any of those things in the past that were part of the curriculum in school.

We continue to receive comments from students that, you know, that's going to be a hot and dirty job, and I'm just not interested in doing that type of work. In our area it has become very obvious that work is an option, not a necessity. Programs intended to be a bridge from one employment situation to another have turned into lifestyle choices, again, not a necessity to get a job.

Our experience in our hiring practice would say that 8 out of 10 of the people that we hire, offer jobs, consider for employment would prefer to stay on benefits than to learn a trade or to have a longtime career with pay and benefits. Often we hear, I have X number of weeks left on unemployment; I'm going to ride it out, then look for a job. I think there will be an extension on unemploy-

ment, and I won't need to look for a job. I've been on unemployment for 2 years, and when it runs out in a couple weeks, will you have any openings then? The starting training wage for this job is less than I make on unemployment; I will stick with unemployment until it runs out. And one of the significant ones for our area, because we have had some companies close that were higher wage levels, I made more on my last job than your starting wage, and I'm making more on unemployment now, and, you know, I don't need to get a job right now because I can use these benefits.

Our county is comprised of about 43,000 citizens. About 20 percent of them are receiving some form of assistance or another, and that continues to grow. Our condition in our county is not uncommon; we hear this from other counties as well. But we do continue to have a vibrant manufacturing culture in our county. Our company, again, has been around for 72 years, and we, again, have been looking for people for years to do the work that we need to do.

Again, in our area it's far too easy to stay on benefits than to attempt to qualify for a job, attempt to transfer a job, and continue to hold that job. We have a significant issue in our area for people that will start jobs and not finish them because they will go back to benefits.

We very much need help with this issue. We don't need more training programs, we don't need more assistance, we need willing workers that will take a job seriously, do not come to the job with drug and alcohol problems, and are willing to, you know, join the workforce, contribute to their communities, and offer tax base and, again, value to the community. They have to feel that work is more than just a job. So thank you.

Mr. JORDAN. Thank you, Ms. Carter.

[Prepared statement of Ms. Carter follows:]

"Unintended Consequences: Is Government Effectively Addressing the Unemployment Crisis?"

Testimony of

Andrea (Annie) L. Carter
President
Hydranamics, Inc. div. Of
Carter Machine Company, Inc.
Galion, Ohio

February 14, 2013

Before the

Committee on Oversight and Government Reform
United States House of Representatives

Subcommittee on Economic Growth, Job Creation and Regulatory Affairs

The Honorable Jim Jordan, Chairman

The Honorable Matt Cartwright, Ranking Member

Thank you for inviting me to testify today. My name is Annie Carter. I am the president and co-owner of Carter Machine Company located in Galion, Ohio. My grandparents started the privately held company in 1941. This year will be our 72nd anniversary. I am the third generation to operate the company. My mother and I joined the company after my father's untimely death in 1995. I have been in a leadership role within the company since 1997. We are the designers and manufacturers of Hydranamics' brand hydraulic and pneumatic cylinders. Our products are used mainly in the steel industry to operate steel making equipment, material movement equipment, etc. We also provide custom designed cylinders for industries producing baling/recycling, material movement, packaging, press, and various other types of equipment. We currently employ 57 individuals, but could benefit in many ways with an effective employee level of 70-75.

Manufacturing was the foundation and backbone of this country. It is now considered something people will do if they have no other options.

Our company is comprised of 50% administrative staff such as engineers, accounting, production control, sales, purchasing, cost estimators, programmers, human resources, and support and 50% skilled labor. Our business is a custom build situation. We generally produce one cylinder at a time, designed and manufactured to each customers' specific design criterion. In order to produce cylinders in this manner, we require a mix of operators trained to run older "manual" style equipment as well as sophisticated, CNC (computer numerically controlled) equipment. The level of skill we require is significant due to the nature of our product. Cylinders designed or manufactured incorrectly can be dangerous. We require top level craftsman to perform our machining and produce our parts. The individuals in our facility are proud of the product that we make because they take their professions very seriously and consider themselves something more than just a machinist or a blue-collar worker.

We have reached a point in society where it is no longer honorable or desirable to learn and perfect a trade skill. I have spoken to high school students many times who have no idea what a trade job is or more importantly that a person can make a comfortable living working a trade job and not attending college. They no longer have exposure to the trades in school through wood or metal shop and they really don't know what it means to work in manufacturing. Continually we receive comments that it will be hot and dirty and "I'm not doing that".

Working has become an option instead of a necessity for some people. Programs intended to be a bridge from one employment situation to another have morphed into a lifestyle choice. Our experience would say that 8 out of 10 people on unemployment or other benefit programs will utilize those benefits as much as possible to avoid working. We have interviewed and offered people jobs on various benefits and we often hear:

"I have x number of weeks left on unemployment, I'm going to ride it out then look for a job."

"I think there will be an extension to unemployment and I won't need to look for a job."

"I've been on unemployment for 2 years and it runs out in a couple of weeks. Do you have any openings?"

"The starting/training wage for this job is less than what I make on unemployment. I'll stick with unemployment until it runs out."

"I made more in my last job than your starting/training wage. I'll need to make that same amount. I'll just stay on unemployment and do nothing and get paid. (often skilled labor from closed facility such as GM or facility that moved processes overseas or out of the area for cheaper labor)."

Crawford County's most recent statistics from Job and Family Services:

Here are some average **monthly** statistics for Crawford County:

Food Assistance recipients: 8147
Amount of Food Assistance distributed: $994,770.10
Cash assistance recipients: 529
Cash assistance distributed: $91,478.30
Medicaid recipients: 10,468
Medicaid expenditures: $5,064,050.70
Unemployment rate for December 2012: 7.8%

The condition of Crawford County is not uncommon. We are in the rust belt and continue to lose companies and jobs to various economic factors,

but we continue to have a vibrant manufacturing culture in this county. I have often said that our major competitor for jobs in this county is the Government. It is far too easy to receive benefits and to stay on benefits versus qualifying for job and maintaining employment. We have hundreds of job openings in this county at all experience levels and we do not have enough people willing to fill the jobs. The options for not working are too attractive and easier than working.

Many citizens of this county have taken our condition very seriously. We have formed a public private partnership to attempt to combat and correct our many issues including employment issues. Our effort is called the Crawford County Economic and Educational Partnership. It is comprised of county-wide Government entities and businesses working to improve the condition of our cities and county. You can learn more about our efforts at: www.growcrawford.org and www.growcrawford.org/Vision-Book-2011-REDUCED.pdf

Through this group and our local Chambers, we consistently hear the growing frustrations of our business leaders regarding their inability to staff properly. Most of the manufacturing plants in this area desperately need people to work right now. Most of these plants will provide access to training programs or train on site. No experience required.

In this area we have a trade school, and many training programs currently exist but go unfilled. We do not need more programs for training. We need interested people to take the training and fill a job opening.

Another significant issue we have in this county is drug and alcohol abuse. An unintended consequence of benefits is substance abuse. Most employers require prescreening for drugs and alcohol. We have a higher than average percentage of failed tests as well as people who simply refuse to test. Crawford County has requested inclusion in a pilot program within the state of Ohio to test benefit recipients for drugs in order to receive benefits. Although controversial, this type of program could curtail drug abuse with government dollars.

As I have already mentioned, our local employers are exceeding frustrated. We struggle to successfully run our companies continually short-handed. Our growth is smothered by our lack of employees. Inability to grow

directly impacts our sales revenue and tax revenue, jeopardizes our ability to serve our customer base. If we cannot provide necessary services, our long-term survival is threatened.

Tax revenues are used to support our deteriorating communities. This is circular problem that desperately requires solutions. We do not have a lack of jobs in Crawford County and most likely many other counties and states, but a lack of willing workers. The deteriorating moral fiber of this country does not support philosophy of the trades. Machinists, in particular, are a self-motivated, mechanically gifted group that continue to learn and grow and continue to enhance the businesses that they work for. The youth leaving high schools and entering the work force aren't motivated to learn and grow. A growing number of eligible workers today are more interested in what they are entitled to, not what they can earn or will earn if they work hard. What can I get today and if I don't get it, I'll move on. Employee, employer relationships are 50/50. Fair days work for a fair day's pay and benefits. This relationship builds companies and their employees who then contribute to their communities with tax base, and involvement in the schools, churches, volunteer programs, etc. These are dying ideas that are being supported by continual government handouts without accountability by the recipients or consideration to the long-term negative impact to communities.

Mr. JORDAN. Dr. Stone.

STATEMENT OF CHAD STONE

Mr. STONE. Chairman Jordan, Ranking Member Cartwright and other members of the subcommittee, thank you for the opportunity to testify on this important topic. I'll summarize my written testimony, which falls into two parts, one focusing on the extraordinary macroeconomic situation in which we found ourselves since 2007, and the other focusing specifically on unemployment insurance.

There is no doubt that the United States continues to suffer a serious unemployment problem in the wake of the Great Recession. Five years after the onset of the recession and 3–1/2 years after the economy turned around and began growing, there was still 3.2 million fewer jobs on nonfarm payrolls than there were in December 2007, private payrolls are smaller by 2.7 million, and the unemployment rate hovers near 8 percent.

You've heard testimony implying that much of this job loss can be traced to work disincentives in the 2009 economic Recovery Act that discouraged people from seeking or taking jobs. I, along with the Congressional Budget Office and, I believe, a large number of economists, have a different view; namely, that today's unemployment problem stems from the sharp contraction in demand for goods and services in the Great Recession, and that the legacy of that recession continues to be an economic slump in which the demand for goods and services, gross domestic product or GDP, remains far short of what the economy is capable of producing with the existing business capacity and a labor force that includes people who are willing to work, but currently can't find a job because the affect of weak demand on businesses for the most part is that they don't have the sales to justify expansion.

I don't have PowerPoint for my charts, but the chart on page 4 of my testimony reproduces a chart from the latest CBO budget and economic outlook illustrating the large gap, currently about a trillion dollars, that exists between actual demand for goods and services and what we could be producing on a sustainable basis with high employment and capacity utilization. That's potential GDP.

Congressional Budget Office projects that we won't get back to high employment until 2017. That could be optimistic. The Recovery Act did not make the unemployment problem worse. CBO's reports on its economic effects show that the 2009 Recovery Act had an important effect in keeping GDP from falling even further and unemployment from rising even higher than it did. Economists Alan Blinder and Mark Zandi have shown that aggressive actions by the Federal Reserve, and the financial stabilization and fiscal stimulus policies enacted in late 2008 and early 2009 averted what they say could have been the Great Recession 2.0.

The problem is the policymakers took their foot off the accelerator too quickly and started to apply the brakes too fast to an economic recovery under the misguided view that budget austerity, especially austerity that focused on spending cuts, would be expansionary and good for the economy. We now know from the experience of Great Britain and the European community, and from revised assessments from the International Monetary Fund, and

other research that austerity is contractionary. And contrary to the view that government spending is, quote, "out of control," fiscal policy has been contractionary for the past couple of years.

I have another chart in my testimony on page 5 from a recent speech by Federal Reserve Vice Chair Janet Yellen that shows that Federal, State and local government purchases of goods and services—that's the spending that gets into GDP—have exercised an unprecedented drag on economic growth in this recovery not just compared with the average of past recoveries, but also in contrast to the expansionary contribution that that spending made in the Reagan recovery and in the Bush recovery, and it's very notable, the difference.

That's why it's so important not to let sequestration take place as scheduled and to replace it with a more sensible approach that balances spending and revenue measures that do not exert such a sharp, immediate drag on the recovery, a drag that CBO estimates is about a half percent of GDP this year.

Let me make just a couple of brief remarks about unemployment compensation in the Great Recession and the ensuing job slump. First I acknowledge that Federal emergency UI provided substantially more weeks of benefits than past programs did in previous recessions. That's because the depth of the recession was much larger. As Roy Scheider said in Jaws when he first saw the shark, you're going to need a bigger boat, and we needed a bigger boat in this case.

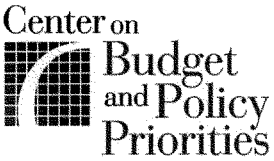
Second, when jobs are scarce, the likelihood of finding a suitable job even with diligent search is much lower than it is when jobs were plentiful. Moreover, there are plenty of people looking for work who are not receiving UI. So if a UI recipient doesn't take a job in this kind of environment, that opens up an opportunity for someone else.

Third, in a weak economy, UI creates demand that wouldn't otherwise be there, and that supports job creation, as the CBO reports on unemployment insurance and on economic Recovery Act have shown.

Thank you, and I expect we'll have a lively debate about incentives and how the economy works.

Mr. JORDAN. Thank you, Doctor.

[Prepared statement of Mr. Stone follows:]



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February 14, 2013

TESTIMONY OF CHAD STONE
Chief Economist, Center on Budget and Policy Priorities

Before the
Economic Growth, Job Creation, and Regulatory Affairs Subcommittee
of the Committee on Oversight and Government Reform
United States House of Representatives

Hearing on Unintended Consequences: Is Government Effectively Addressing the Unemployment Crisis?

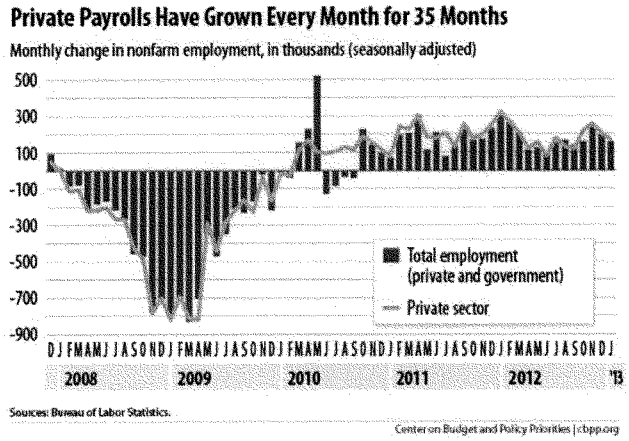
Mr. Chairman and members of the subcommittee, thank you for the opportunity to testify on this important topic. The first half of my testimony focuses on the macroeconomic roots of our current jobs crisis and the second part focuses specifically on unemployment insurance.

There is no doubt that the United States continues to suffer a serious unemployment problem in the wake of the Great Recession. Five years after the onset of the Great Recession and three and a half years after the economy turned around and began growing, there are still 3.2 million fewer jobs on nonfarm payrolls than there were in December 2007. Private payrolls are smaller by 2.7 million, and the unemployment rate hovers near 8 percent.

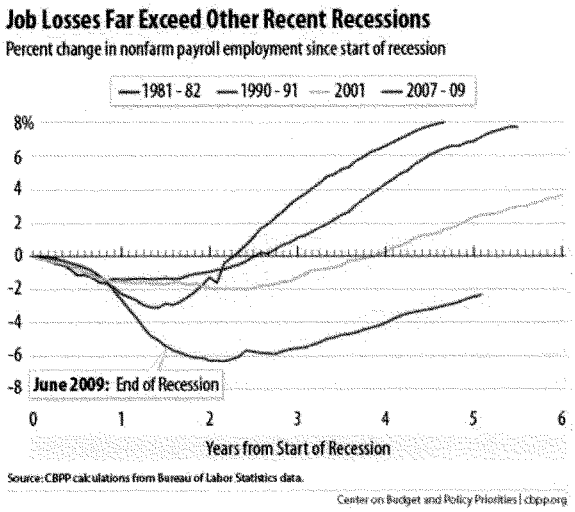
The Legacy of the Great Recession

To be sure, there was a dramatic turnaround in the jobs picture starting in 2009 when aggressive actions by the Federal Reserve and the financial stabilization and fiscal stimulus policies enacted in late 2008 and early 2009 averted what economists Mark Zandi and Alan Blinder say could have been the "Great Recession 2.0."[1] As the first chart shows, the economy was hemorrhaging jobs at the time but the magnitude of the job losses quickly shrank in 2009 and we've seen 35 straight months of private sector job creation; total nonfarm employment has grown by an average of 157,000 jobs a month.

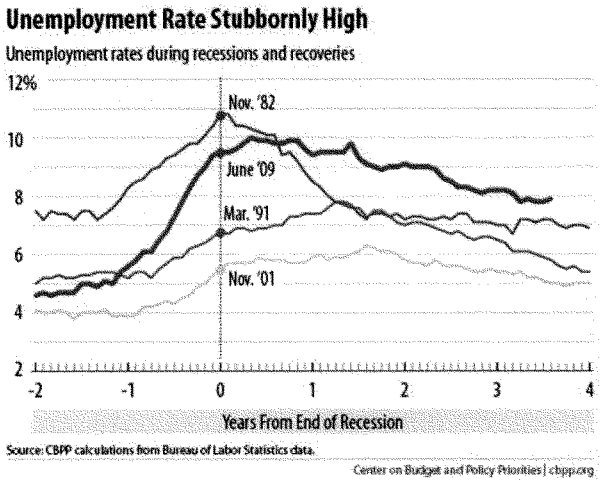
[1] Alan S. Blinder and Mark Zandi, "How the Great Recession Was Brought to an End," July 27, 2010, available online at http://www.economy.com/mark-zandi/documents/end-of-great-recession.pdf



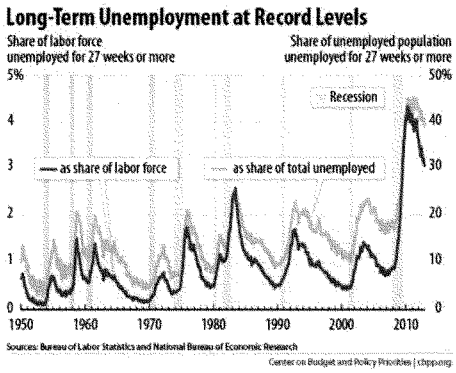
The problem is that the Great Recession created a jobs deficit much larger than any we have seen since the 1930s and we still have a long way to go to erase it, catch up with population growth over the intervening years, and get back to full employment. The next chart illustrates how deep the job losses were compared with recent recessions. It also shows that the rate of job growth since early 2010 has not been that different from the last recovery, but we started from a much deeper hole.



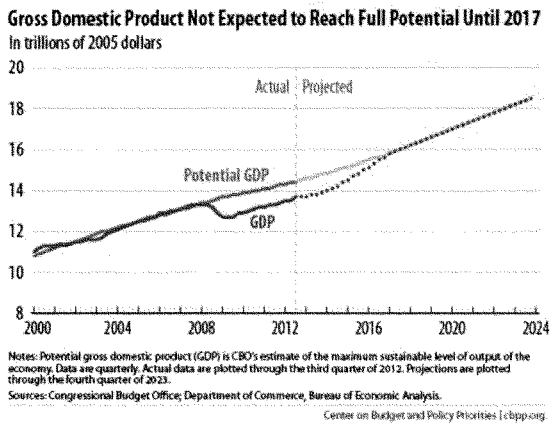
The next chart illustrates how the pattern of unemployment has combined the worst features of the past three business cycles. The unemployment rate shot up even faster than it did in the deep 1981-82 recession (though not quite as high) but it kept rising and has come down only slowly after the formal end of the recession in June 2009, matching the pattern of slow jobs recoveries in the previous two recessions.



A final disturbing feature is the extent of long-term unemployment. The percentage of the labor force and the share of the unemployed who are unemployed for 27 weeks or more rose to unprecedented levels in the Great Recession and, while they have come down, they remain higher than their previous peaks in any prior recession in the post-World War II era.



CBO estimates that the economy will grow just 1.4 percent this year and the unemployment rate will remain near 8 percent through the year.[2] That means another year of enormous economic waste and high unemployment. CBO estimates that gross domestic product in 2013 will fall short of the economy's full potential by $1 trillion (see chart). It projects that the gap won't close and we won't see a high level of employment until 2017. That will require sustained economic growth at a faster pace than we have seen thus far in the recovery — and much faster than we will likely see this year under current law.



There is tremendous economic waste and human hardship in an economy that is operating well below full capacity. The goods and services that are not produced, the wages and business income that is not earned, and the revenues not received are lost forever. Potential GDP is effectively a ceiling on sustainable production, so periods of severe economic slack such as we are currently experiencing are not offset in the future by periods when actual GDP exceeds potential by a comparable amount.

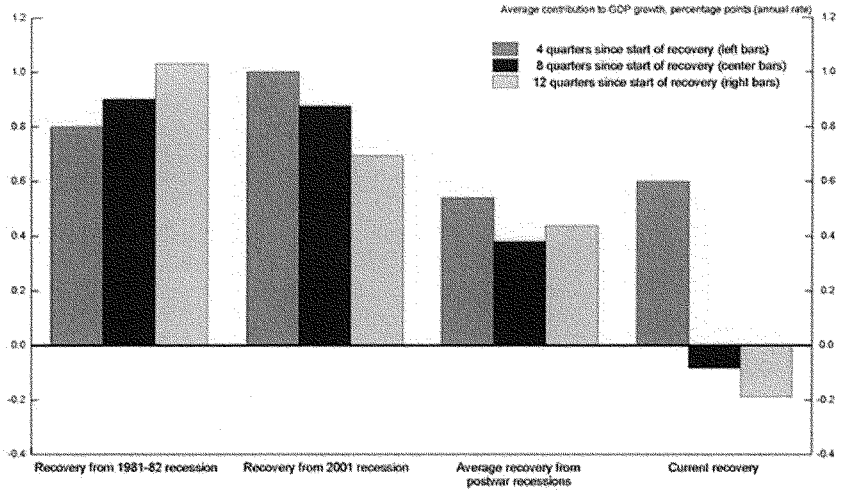
CBO —and I would venture to say a majority of economists—believe that this large output gap stems mainly from inadequate demand for goods and services, not a lack of incentives for businesses to supply goods and services or an unwillingness of workers to offer their labor services. The cure for most of our current unemployment problem is faster economic growth to close the output gap more quickly. The Federal Reserve has gone to extraordinary lengths within its powers to encourage greater growth, but since 2009 fiscal policy has been a drag on growth.

I know it sounds strange to people used to talking about "out-of-control" government spending, but changes in combined federal and state and local spending on goods and services have made a negative contribution to economic growth since 2009 — not because government spending has

[2] Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2013 to 2023*, February 2013, p. 43

been growing, but because it has not, as shown in the following chart from a recent speech by Federal Reserve Vice Chair Janet Yellen.[3]

Exhibit 3: Estimated Effect of Discretionary Fiscal Policy on the Economy during Recoveries



Note: Average recovery from postwar recessions excludes recovery after 2007-09 recession; because of data limitations, average also excludes recovery after 1948-49 recession.
Source: Federal Reserve Board staff calculations

This chart shows the contribution of federal, state, and local government purchases of goods and services to economic growth one year, two years, and three years after the end of the recession for the current recovery, the average of past recoveries, and the recoveries from the 1981-82 and 2001 recessions. In the first year, the contribution of government spending to growth was about the same as the average of past recoveries but nowhere near what it was in the Reagan and Bush recoveries. And in the two subsequent years, government spending was a drag on growth.

We do have to take steps to stabilize our long-run budget situation, and our macroeconomic policies have not been as disastrous as those of Great Britain or the EUC, but our pursuit of too much budget austerity, too soon has not done the economic recovery any favors.

CBO estimates that the fiscal restraint still in effect after the fiscal cliff deal will subtract 1½ percentage points from economic growth this year. Three things account for the bulk of that restraint: the automatic cuts in federal spending ("sequestration") due to kick in March 1, the

[3] Vice Chair Janet L. Yellen, "A Painfully Slow Recovery for America's Workers: Causes, Implications, and the Federal Reserve's Response," February 11, 2013, available online at http://www.federalreserve.gov/newsevents/speech/yellen20130211a.htm

expiration of the 2009 payroll tax cut, and expiration of some of President Bush's tax cuts for wealthy taxpayers.

Although sequestration does the least of these three policies to cut the budget deficit this year, dollar-for-dollar it restrains growth and job creation the most. In fact, CBO estimates that it accounts for roughly the same overall drag on growth as the combined tax changes. Moreover, most of the drag from the tax changes arises from the 2 percentage point increase in the payroll tax; dollar-for-dollar, higher tax rates on the very affluent do little to hamper the economic recovery.

Policymakers missed an opportunity in the "fiscal cliff" negotiations to resolve the sequestration issue by replacing the across-the-board cuts with policies that achieved equivalent budget savings but that were more balanced between taxes and spending and that did not take effect until the economy was stronger. They missed an opportunity to boost the recovery and brighten jobless workers' job prospects when they failed to extend the payroll tax cut. And they missed an opportunity to achieve more deficit reduction that didn't threaten the recovery when they did not end Bush-era tax cuts for more very well-to-do Americans.

My colleagues at the Center on Budget and Policy Priorities' recent analysis shows that $1.5 trillion in additional deficit reduction would stabilize the debt over the next ten years.[4] Moreover, it shows that deficit reduction should be designed carefully to avoid further slowing the recovery, and it should be phased in over coming years. Preferably, policymakers would couple those permanent deficit-reduction measures with some targeted temporary fiscal measures to accelerate growth and job creation now.

A good place to start would be to replace sequestration with a balanced package of tax and spending measures that do not exert such a sharp, immediate drag on the recovery.

Unemployment Insurance

Policymakers acted with uncharacteristic speed to enact emergency unemployment compensation (EUC) in mid-2008 and to expand it in late 2008 when the severity of the job losses became evident. The 2009 Recovery Act added full federal funding for the joint federal-state Extended Benefits (EB) program, and added a federal benefit of $25 per week. While the maximum number of weeks of unemployment insurance (UI) available in the typical state in normal times is 26, the combined number of weeks of regular UI, EUC, and EB eventually available in states with particularly high unemployment was 99 from late 2009 to early 2012.

The maximum number of weeks was reduced by changes in the law in February 2012, and as the number of unemployed workers drops and state economies improve, federal emergency UI spending will diminish. Congress has enacted emergency federal UI in every major recession since the 1950s, and it has always allowed the program to expire once the labor market is strong enough that workers can be expected to find a job in a reasonable period of time. However, the highest unemployment rate at which previous programs were allowed to expire was 7.2 percent — a rate

[4] Richard Kogan, Robert Greenstein, and Joel Friedman, " $1.5 Trillion in Deficit Savings Would Stabilize the Debt Over the Coming Decade," Center on Budget and Policy Priorities, February 11, 2013, available online at http://www.cbpp.org/files/2-11-13bud.pdf

CBO does not expect the economy to reach this year or next under its baseline assumption that current laws continue to govern taxes and spending.

Clearly, federal emergency UI was a larger program in the Great Recession and its aftermath than it was in previous recessions, but as I hope I have shown, the unemployment problem was much larger this time as well.

Finally, I want to address the question of whether emergency unemployment insurance discourages unemployed workers from looking for work and could be a significant contributor to the high levels of unemployment in the Great Recession and its aftermath. CBO provides a useful discussion[5] of the variety of ways providing additional weeks of unemployment insurance might affect the incentives of workers receiving UI to search for a job and accept a job if offered. Importantly, CBO also distinguishes between such effects in a strong labor market versus one with substantial unemployment.

Opponents of continuing emergency unemployment benefits often assert that UI discourages people from looking for work and that ending these benefits would speed a return to full employment. Though research from earlier periods showed that additional weeks of unemployment insurance have an impact in lengthening unemployment spells, the most careful recent research indicates that these effects are much smaller in a weak economy.

Additional weeks of UI benefits have three distinct effects on the duration of unemployment spells. First, unemployment insurance has the beneficial effect of allowing an otherwise financially strapped unemployed worker to search more efficiently for an appropriate job (rather than having to accept the first job offered, whether or not it is a good match for his or her skills). Second, since unemployed workers are required to seek work in order to qualify for UI benefits, additional weeks of UI benefits keep unemployed workers attached to the labor force and looking for jobs for longer than they might have without those benefits. Finally, UI may create disincentives to look hard for a job.

One study released in early 2010 offers the "back of the envelope calculation," based on the relevant research, that weeks of benefits added through EUC could account for "between 0.7 and 1.8 percentage points of the 5.5-percentage-point rise in the unemployment rate."[6] But it also suggested that "the true effect of extended UI benefits on unemployment duration is likely to be at the lower end of these estimates."

Indeed, a careful study of recent evidence by economist Jesse Rothstein found that federal extensions of UI in the past few years likely had an *even smaller* effect than this. Rothstein found that the unemployment rate in December 2010 would have been only about 0.2 percentage points lower without the extension of unemployment compensation.[7] Moreover, Rothstein also found that at least half of this 0.2 percentage-

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[5] Congressional Budget Office, "Unemployment Insurance in the Wake of the Recent Recession," November 2012.

[6] Michael Elsby, Bart Hobijn, and Aysegul Sahin, "The Labor Market in the Great Recession," Brookings Institution Papers on Economic Activity, Spring 2010, http://www.brookings.edu/~/media/Files/Programs/ES/BPEA/2010_spring_bpea_papers/2010a_bpea_eslby.pdf

[7] Jesse Rothstein, "Unemployment Insurance and Job Search in the Great Recession," University of California, Berkley, October 16, 2011, http://gsppi.berkeley.edu/faculty/jrothstein/workingpapers/Rothstein-UI-Oct2011.pdf. For a concise summary of this paper, please see Heidi Shierholz, "What's UI got to do with it?" Economic Policy Institute, September 22, 2011, http://www.epi.org/blog/unemployment-insurance-benefits/.

point increase could be from increasing labor force attachment — i.e. keeping UI recipients actively searching for work rather than dropping out of the labor force. Most other studies of the disincentive effect of UI in the current downturn have also found relatively small effects.

Harvard economist Lawrence Katz has also observed that traditional estimates of the relationship between UI and the length of unemployment spells ignore other effects, such as "the macroeconomic stimulus impacts of increased consumption expenditures by the unemployed … as well as the gains from keeping more of the long-term unemployed attached to the labor market rather than moving onto disability programs."[8]

Arguments that emergency UI benefits are an important contributor to high unemployment in today's economy have cause and effect backwards. We have a temporary federal program *because* unemployment is so high and jobs are so hard to find.

In assessing the economic effects of extending UI, CBO concluded that "the various effects of extending additional unemployment benefits, apart from the effect on the overall demand for goods and services would, on balance, make little difference to overall output or the number of people employed" under weak economic conditions. CBO has, however, found UI to be one of the most cost-effective ways of stimulating output and employment in a weak economy.

The impact on unemployment is more complicated. People who have dropped out of the labor force are not counted as unemployed, and some of the stimulative effect on *em*ployment could come from bringing people back into the labor force. At the same time, if UI has a strong enough effect keeping recipients in the labor force looking for work rather than dropping out, a longer duration of emergency UI could also increase *un*employment. But once again, keeping people looking for work is a desirable outcome not a problem with the program.

Concluding Observations

The United States continues to have an unemployment problem. That problem is a legacy of the Great Recession and the subsequent slow recovery. Part of the reason for the slow recovery and persistently high unemployment is that policymakers have pursued budget austerity during a period of economic weakness. Ideally, policymakers would have chosen a better mix of policies between those with high job-creating bang-for-the-buck in the early years combined with those that would achieve significant deficit reduction but only in the later years when the economy is stronger. Policymakers should apply that approach in their upcoming decisions about sequestration.

With the economy still weak, programs like emergency unemployment insurance, which put money in the hands of people likely to spend it, not only meet their primary goal of providing help to people in need but also provide valuable support to the economic recovery by boosting demand for goods and services. These programs do not add significantly to long-term deficits and debt because they shrink automatically as the economy improves, and emergency measures expire.

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[8] Lawrence F. Katz, "Long-Term Unemployment in the Great Recession," testimony before the Joint Economic Committee, U.S. Congress, April 29, 2010, pp. 4-5, http://jec.senate.gov/public/index.cfm?a=Files.Serve&File_id=e1cc2c23-dc6f-4871-a26a-fda9bd32fb7e. For a concise summary of this testimony and other recent research, see Joint Economic Committee, "Does Unemployment Insurance Inhibit Job Search?" July 2010, http://jec.senate.gov/public/?a=Files.Serve&File_id=935ec1e7-45a0-461f-a265-bbba6d6d11de.

Mr. JORDAN. Mr. Reece.

STATEMENT OF STACEY G. REECE

Mr. REECE. Chairman Jordan, Ranking Member Representative Cartwright, committee members, thank you for inviting me to testify before you today. I'm Stacey Reece, coowner of Spherion Staffing and Professional Recruiting. Spherion is a national recruiting franchisor, my market is located main office in Gainesville, Georgia, and the western part of North Carolina.

The employees we provide to our clients don't always meet their internal hiring criteria; therefore, we believe that the employees that we place, we give them an opportunity to work for an employer of choice to demonstrate that they are capable of meeting the employer's hiring criteria and eventually becoming full-time employees of that client. We also belive we're an economic barometer. We're one of the first business sectors to fill an economic downturn and one of the first to see the economy recover.

Prerecession we observed clients that were hiring temporaries permanently begin to keep them temporary. Next the clients suspended the hiring of any new temporary workers. It then escalated to waves of layoffs for temporary employees. That was followed by clients no longer needing temporaries. And then finally clients began the process of laying off their permanent workers. Our industry was devastated, much like the banking industry, the automobile industry, the housing industry, and the staffing industry did not receive any form of Federal assistance during that time.

I would like to offer you insight into the almost daily obstacles that our recruiters deal with regarding our unemployment insurance program and the impact we see the system having on qualified and employable job applicants. And let me state for the record my testimony is not against providing any form of safety net for any unemployed American citizen.

In late 2009, we began to see hiring returning to the economy. We were hit head on with a hurdle we didn't anticipate. We had applicants applying for jobs, but only to protect status their for unemployment insurance. Just to turn down the job, applicants would use the regulation related to earning a reasonable percent of their previous pay.

The reasonable distance to travel to work was also a factor utilized to turn down a job. If it was more than 25 miles, they didn't have to take it. If it was 26.5, they didn't have to take it. If it was 19.5, then they had to consider it.

Our staff believed that these applicants were possibly unemployable to begin with, but as they looked more closely, they found that most of the applicants were very skilled, capable, and had been on prior jobs for several years before being laid off.

Prior to the recession clients were willing and able to pay wages that were above the prevailing market rates. We have found that the unemployed who are holding out and choosing to stay on unemployment now face the reality that those jobs will no longer pay what they once earned. They will look our recruiters in the eyes and state, well, I will just stay on unemployment. One of our clients that has multiple manufacturing, assembly and distribution facilities across the United States, and they employ thousands of

employees across the country, had this to say, quote: "We've actually had applicants say that they had done the math, and they were not willing to work for $10 an hour because their unemployment check, coupled with gas savings, lunch and uniforms made it more attractive to stay home." The way they saw it, they would be working for $2.50 an hour above what they could get on unemployment, so they'd rather stay home.

This client also interviewed a purchasing professional recently, and when the HR director asked him what had he been doing since he was laid off from his previous job, he just laughed and said, nothing, I'm a 99-weeker. They didn't hire him.

Our other clients state that applicants have told them similar stories. One says, I have no interest in getting a job because I can live off my spouse's income until the full unemployment benefits run out.

We believe the impact, the continuous extension of unemployment, has enabled people that are extremely talented and capable of working to continue to remain unemployed. These applicants are often bitter and irritated that they cannot simply go back to pre-2008 times. In our markets these individuals are typically in the pay range of 9 to $12 an hour.

Once an employee is offered permanent work with one of our clients, typically their pay goes up 8 percent, plus benefits, paid time off, a progression plan and training, all paid by the new employer. It is not only a win for the employee and the employer, it is a win for our economy.

I believe we should stop the extension, implement a strict graduated system that would pay full benefits up to 12 weeks, and then gradually drop down maybe every 4 weeks after that until the benefits are exhausted. At that point if the individual is still unemployed, there has to be other viable Federal programs that support them, but remove the burden from the employer themselves.

In summary, our economic system is not based on a workforce that believes it should be rewarded for not working, nor entitled to be maintained by the government. Our current state of economic affairs does not dictate that we ask our government to sustain our standard of living. It demands that we as American citizens reexamine our own values, our wants and our desires, and realize that we must face the reality of what today is, and adjust our lifestyles accordingly.

I look forward to the committee members' questions.

Mr. JORDAN. Thank you.

[Prepared statement of Mr. Reece follows:]

"Unintended Consequences: Is Government Effectively Addressing the Unemployment Crisis?"

Testimony of
Stacey G Reece
Co-Owner
Gainey-Reece Associates, Inc.
D/B/A
Spherion Staffing and Professional Recruiting

Before the
Committee on Oversight and Government Reform – Subcommittee on Economic Growth, Job Creation, and Regulatory Affairs

United States House of Representatives

The Honorable Jim Jordan, Chairman

The Honorable Matt Cartwright, Ranking Member

Chairman Jim Jordan and Ranking Member Rep Matt Cartwright, thank you for inviting me to testify today. My name is Stacey Reece; I am Co-owner of Gainey-Reece Associates, Inc. d/b/a Spherion Staffing and Professional Recruiting. Spherion Corporation is a national staffing and professional recruiting franchisor. Our exclusive geographical market is Northeastern Georgia and Western North Carolina. Our main office is in Gainesville, Georgia located one hour north of Atlanta and just a few miles south of the Appalachian Mountains. You might say we have the best of both worlds being located so close to one of the nation's largest cities and at the foothills of nature's most beautiful mountains full of fishing streams, hunting, hiking, and folks that are making this country one of the best in the world.

What We Provide for Our Employees –

Spherion is a company that specializes in recruiting professionals and providing temporary staffing. We cover a large arena of recruiting. Today we currently have three branches and two onsite locations. At Spherion, the employees we provide to our clients may not meet their internal hiring criteria; therefore, we provide the employee an opportunity to work for an "employer of choice" to demonstrate that they are capable of meeting the

employer's hiring criteria. Our clients provide us basic criteria and standards to hire from that are typically less stringent than their own standards. They will then utilize the Spherion employee for the next 90 – 180 days to measure their abilities.

Clients like this arrangement because it gives them the ability to see an employee's work ethic, ability to learn, and gage their overall performance. Our clients hire us to manage a labor intensive process that allows them to focus on their core goals of delivering their product/services. Some clients that are very high volume employers invite us to establish an onsite office at their business to manage their staffing needs exclusively.

We are an Economic Barometer –

The staffing industry is one of the first business sectors to "feel" an economic downturn brewing on the horizon and one of the first to see the economy recover. We started to see the downturn in our economy as early as mid-2007 with the slowing of job orders across most all segments.

Prior to the recession we had six branches and seven onsite locations. Pre-recession, in 2006 we billed out 2.3 million staffing

hours and averaged an FTE of 1150 employees working in the field on a daily basis. During 2012 we averaged an FTE of 450 temporaries.

Clients that were hiring temporaries permanently were now keeping them temporary. Next, the clients suspended the hiring of temporary workers to replace those temporaries being hired permanently. It then escalated to waves of layoffs for temporary employees. That was followed by clients no longer needing temporaries and finally clients began the layoff of permanent workers.

Our industry was devastated much like the banking industry, the automobile industry, and the housing industry. The staffing industry did not receive any form of federal assistance during this time.

We have fourteen full-time staff members. That number is down from a high of thirty-two pre-recession. We experienced multiple rounds of layoffs with our internal staff. Most all of those laid off were able to secure some other form of employment and avoided unemployment in most all situations.

Then after reducing remaining salaries by 20%, the final round came and we were able to do a temporary layoff where one group of staff would work one week and then have the other half work the

next week. As the economy improved all of those individuals were restored to fulltime employment and eventually all salaries were restored to their original amount.

The Unintended Consequences –

Today, I would like to focus on the temporary staffing portion of our business and offer you some insight into the almost daily obstacle that our staff deals with regarding the state of crisis we find our unemployment insurance program. Let me state for the record that my testimony is not against providing a safety net for any unemployed American Citizen. What I want to share with you is the impact we see our current unemployment system having on qualified and employable job applicants.

In late 2009 when we began to see some glimmer of hiring returning to the economy; however, we were hit head on with a hurdle we did not anticipate. We had applicants applying for jobs, but only to protect their status for unemployment insurance. Applicants would use the unemployment regulations related to the reasonable percent (%) of prior pay rate vs. the lower pay rate the job opportunity offered to turn it down. The reasonable distance to travel to work was also a factor utilized to turn down a job offer. Our staff first believed that these applicants were maybe unskilled or

maybe even unemployable to begin with. As we examined more closely, we found that most of the applicants were very skilled, capable, and had been on prior jobs for several years before being laid off.

Reality –

Prior to the recession when the inventory for entry level workers was scarce, clients were willing and able to pay wages that were above the prevailing market. We have found that the unemployed who are holding out and choosing to stay on unemployment now face the reality that jobs no longer pay today what they had earned pre-2008. The unemployed will look our recruiters in the eyes and state, *[Quote] "...well I'll just stay on unemployment..." [Un-quote]*

One of our client's that has multiple manufacturing, assembly, and distribution facilities across the United States and employees 1000's of employees provided the following examples:

[Quote] "We've actually had applicants say that they had done the math and that they were not willing to work for $10 per hour because their unemployment check coupled with gas savings, lunch and uniforms made it more attractive to stay home. The way they saw it,

they would be working for $2.50 per hour above what they could get on unemployment so they'd rather stay home. We also interviewed a purchasing professional recently and I asked him what he had been doing since he was laid off from his previous job and just laughed and said "nothing, I'm a 99 weeker!" We didn't hire him." [Un-quote]

And, we have heard from applicants, as well as, our clients' state that applicants have told them, *[Quote] "...I have no interest in getting a job because I can live off my spouse's income until the full unemployment benefits run out..." [Un-quote]*

I believe these individuals honestly have faith in that the economy will rebound and they will once again earn the higher wage that they once enjoyed.

The Impact –

The continuous extensions of unemployment have enabled people that are extremely talented and capable to work to continue to remain unemployed. These applicants are often bitter and irritated that they cannot simply go back to the pre 2008 times. Again, they are largely individuals that had advanced well in their trades during better times. In our markets, these individuals are typically in a pay range of $9.00 – 12.00 per hour.

Once an employee is offered permanent work with our client their pay rate usually increase on the average of 8% - 10% plus benefits, paid time off, and a progression/training program all paid by the new employer. It is not only a win for the employee and employer – but a major win for our economy!

Solution –

Stop the extensions! Implement a strict graduated system that would pay full benefits up to 12 weeks and then gradually drop down every four weeks until the benefits are exhausted. At that point, if the individual is still unemployed there are other viable federal programs that could support them at that point. This would remove the cost from the employer over to other appropriate federal agencies.

Summary –

My Grandfather was a business owner when the Great Depression hit and his small general merchandise store survived although most of his cash on hand was in a bank that didn't make it. My dad labored as a manager of a full service gas station for 35 years and the final 10 years of his career as a small business owner. I have

invested almost 16 years as a small business owner. The true question today is what do I inspire my 20 year old son and my 17 year old daughter that they pursue? Do I recommend business ownership in the environment that we are currently experiencing? It may still be a few years before I can honestly answer the question from my children.

Our free enterprise market system was not based on a workforce that believed that it should be rewarded for not working or entitled to be maintained by the government. Our current state of economic affairs does not dictate that we ask our government to sustain our standard of living. It dictates that we as American Citizens reexamine our values, our wants, and our desires to realize that we must face the reality of today and adjust our life styles accordingly. I look forward to the committee members questions.

Respectfully,
Stacey G Reece
Business Owner

Mr. JORDAN. Ms. Carter, how many employees do you have at Carter Machine today?

Ms. CARTER. Fifty-seven.

Mr. JORDAN. And how many would you have—I mean, if you could find people to work and do the kind of expansion you want to do and think you need to do to meet your customer and clients' demands, how many more people would you have working today if you could find those individuals?

Ms. CARTER. Immediately we could use 70 to 75 people.

Mr. JORDAN. Additional or 56 up to 75?

Ms. CARTER. Up to 75.

Mr. JORDAN. So another 20 people you are ready to hire today?

Ms. CARTER. Yes.

Mr. JORDAN. How much do you pay your folks?

Ms. CARTER. Generally starting wage is 12 to $14 an hour. And they can earn——

Mr. JORDAN. So significantly above minimum wage.

Ms. CARTER. Yes.

Mr. JORDAN. Do you offer a benefit package?

Ms. CARTER. Yes.

Mr. JORDAN. Health care?

Ms. CARTER. Health care, pensions, 401(k), lots of other little benefits in there.

Mr. JORDAN. And you can't find people.

In fact, Ms. Carter and I were at a meeting in our district where we had nine employers sitting around a table. My guess is all of you, both sides of the aisle, had the same experience. We had nine employers sitting around the table. We went around the room, and I asked each employer how many folks they would hire that day if they could find people to work, who would pass a drug test, who would show up on time, who weren't getting so much benefits, and giving the same kind of stories you and Mr. Reece related. Three hundred twenty-five jobs. And Ms. Carter from Galion, Ohio, Crawford County, a relatively small county in our district, 50,000 population in the entire county, 325 well-paying jobs between 12 and $18 an hour. So we are hearing this all the time.

And I think you said in your testimony, Ms. Carter, 8 out of 10, 80 percent, of the folks you interview say, you know what? I'd rather just stay on the benefits. It's not worth me leaving the benefits and coming to work even for a job that starts at $12 an hour and has full benefits.

Ms. CARTER. Right.

Mr. JORDAN. So if that's not a disincentive to work, I don't know what is. It points to if we got 80 percent of the folks—now, think about it, we have 12 million unemployed people around the country. Maybe not 80 percent around the country, I get that. But Dr. Steuerle in his testimony talked about the depression that sets in, the loss of skill that sets in, the personal damage that happens to individual Americans when they fail to work for a sustained period of time.

Dr. Steuerle, would you elaborate a little bit on that statement? And let me just start here first, too. Dr. Steuerle, you work for the Urban Institute?

Mr. STEUERLE. That's correct.

Mr. JORDAN. You don't work for Cato, right?

Mr. STEUERLE. No.

Mr. JORDAN. You don't work for the Heritage Foundation.

Mr. STEUERLE. Urban Institute considers itself a nonpartisan. I testify often for both sides of the aisle.

Mr. JORDAN. I understand. We're glad to have you here. So if you can elaborate on the phenomena that Ms. Carter described in her testimony and Mr. Reece described in his testimony and how it impacts that individual.

Mr. STEUERLE. Well, there's no doubt that when people are unemployed, they acquire different habits. You and I would acquire different habits if we left Congress, if I left my job.

Mr. JORDAN. Maybe get some good habits. I'm kidding.

Mr. STEUERLE. There is a fair amount of evidence, for instance, by employers who pay workers comp that if they can interact quickly with the person who becomes injured, they are much more successful——

Mr. JORDAN. I hear that all the time.

Mr. STEUERLE. —than the person who is laid off 6 or 8 weeks and other habits form. Now, I'm not saying they—I'm not saying in many case these people aren't worthy of help and support. In most cases I think they are. But there is the issue about how quickly you intervene, and how you intervene, and how you interact with them. So there are costs there.

We've also found just by the way that savings—we're not talking about savings very much here, but you start dealing with an unemployed population, a population depending upon benefits, and it also impacts upon their saving behavior as well.

Mr. JORDAN. Let me just take it one step further, because we're focused on that individual and that family and the negative impact there, but it's got to be broader than that. And it is something Ms. Carter related to me in her experience and what she sees in Galion, Ohio, but there's a cultural, and community, and, frankly, nationwide impact to what's going on here because it reflects on your entire community. People aren't saving as much, which means they can't spend as much, which means they are not getting the skills, they are not bettering themselves. It is a broad impact, I would argue, in a negative way for our entire culture. Have you looked at that—in your research have you looked at that as well?

Mr. STEUERLE. I can't say that I've looked at it adequately to say that I'm an expert on its aggregate impact upon our culture. I think in general my concern—there's actually two concerns being expressed at the table here. Some are short-term, and some are long-term. In fact, a lot of what Dr. Stone said and Dr. Mulligan said is actually reconcilable.

Dr. Mulligan and to some extent I have emphasized supply-side effects, tax rate effects, incentive effects. Dr. Stone has emphasized—I'm not saying there's some disagreement there, but he's emphasized the fact that this great financial depression caused a lot of unemployment that was probably unavoidable. So we might debate to some extent how much each one impacts, but they are both there, they're both present.

Mr. JORDAN. No one argued—I mean, Mr. Cartwright in his opening statement talked about the economy that this administra-

tion inherited, no one argues that it was bad and headed in the wrong direction. The point here today is what was undertaken has not worked. I mean, I said many times if big government spending was going to get us out of this mess, well, for goodness sake, we'd have been out of it a long time ago because that's all the government's done for 4 years, at a record rate the largest stimulus bill in history, then piled on—more and more piled on top of that. So it just, frankly, hasn't worked. That's what we're trying to point to. We understand it was a difficult situation for any administration.

Mr. STEUERLE. My concern is not just with how to debate the past, but how to debate going forward.

Mr. JORDAN. Well said.

Mr. STEUERLE. Ms. Carter talks about the 20 percent of people that are on some form of assistance she has trouble dealing with. I—on the other side of my work, I deal with things like Social Security and retirement. We are soon scheduled to have close to a third of the population on Social Security alone. So add these numbers up, and we're doing a great deal of finance consumption of peoples for very worthy purposes that I just think—I am not just saying we need to spend less money, I'm just saying I think we need to start emphasizing more work, saving and education to get the positive——

Mr. JORDAN. And you would argue—and I will go to our ranking member—a comprehensive approach. We know there are—our research says there are 70 different means-tested social welfare programs at the Federal Government your tax dollars are involved with. We might be better off and actually help families, help our culture, help our country if we didn't have 70 different programs administered in the various agencies across the Federal Government working with the States if we focused that on a few that actually had a positive impact. That's one of the things we're trying to look at, and we'd appreciate your help even though you're from the Urban Institute and not Cato or Heritage. I'm kidding, I'm kidding.

Mr. Cartwright, you're recognized for 5 minutes. No, you get 6 minutes if you want.

Mr. CARTWRIGHT. Thank you, Mr. Chairman.

Dr. Stone, I want to thank you for coming here today, and I want to follow up on some of your comments. You mentioned the sequestration. Obviously sequestration is going to and it's designed to impose across-the-board spending cuts to an economy that is still slowly recovering. This is likely to halt any further economic growth in the short term, and also impede any improvements to our unemployment rate, which is what we're here talking about today.

Now, economists, Dr. Stephen Fuller, examined the impact of the sequester and concluded that in 2013, it would cost the U.S. economy over 2 million jobs, decrease personal earnings by $109 billion, and reduce our Nation's GDP by $215 billion.

Now, Dr. Stone, I understand that Dr. Fuller's Ph.D. Is from Cornell, and yours is from Yale, but is that something you can get past, and can you agree with Dr. Fuller on his statement?

Mr. STONE. Well, I can certainly agree on the contractionary impact. I'm not sure his analysis didn't include not only sequestra-

tion, but also the budget caps that are already in, which might make it larger than what's due to sequestration alone. CBO estimates that the sequestration would cut a half point or more off GDP. So there's definitely contractionary effect. The exact numbers, that's tough to know.

Mr. CARTWRIGHT. And just so we're all clear, you said austerity is contractionary. What does that mean about unemployment?

Mr. STONE. It means that when you enact policies that raise taxes and cut spending in an economy where the Federal Reserve has limited ability to offset it with interest rate cuts, and in an economy where there's already a lot of unemployment, unemployment goes up, and GDP goes down.

Mr. CARTWRIGHT. Now, the White House has released a fact sheet on how the sequester would impact jobs and economic security. This fact sheet identified emergency unemployment compensation as one program that would see significant reductions itself. These cuts wouldn't only hurt the long-term unemployed as they search for permanent employment, but they also slow economic growth as the result of a corresponding reduction, as you said, in demand for goods and services.

Dr. Stone, in your testimony you state, and I'm going to quote from your submitted testimony, "A good place to start would be to replace sequestration with a balanced package of tax and spending measures that do not exert such a sharp, immediate drag on the recovery." And that's the end of the quote.

Dr. Stone, why is it important that deficit reduction measures are carefully designed——

Mr. STONE. Well, for the reasons that your first question raised, that if they're not carefully designed, they impede the economic recovery. We can achieve significant deficit reduction. My organization has estimated we need about $1–1/2 trillion more over 10 years to stabilize the debt relative to the size of the economy. And if we try to do it all now, we'll have that austerity as contractionary problem. But if we phase it in, we can still get to where we want to go with respect to deficit reduction without hurting the economy in the short run.

And can I just say about unemployment, unemployment insurance has, in fact, been coming down. There are probably about 5 million people out of the 12 million on unemployment insurance now, so that means that there are a lot of people who might be showing up for work who are not on unemployment insurance, and certainly the high school students who don't have a good work ethic, unemployment insurance isn't the problem there. So it's a bigger deal than just the unemployment insurance.

Mr. CARTWRIGHT. Well, thank you for those comments. This is not the time for broad cuts to programs intended to support the unemployed. Cuts like that are projected to worsen the economic outlook and the hardships faced by the unemployed that I think all of you agree on.

Our economy is recovering, we've seen 35 months of job creation, but the sequester cuts and the uncertainty associated with them is going to put a significant drag on our American recovery and negatively affect the number of jobs available. If we in Congress are serious about making sure our Federal Government is effectively ad-

dressing unemployment, we have to avoid these broad cuts and instead focus our efforts on investments that stimulate the economy and create jobs.

Thank you, Mr. Chairman. I yield.

Mr. JORDAN. Thank you, Mr. Cartwright.

Mr. Reece, do you think the Federal Government has taken its foot off the accelerator? Do you think it's been practicing austerity? Just your gut reaction. As a successful business owner, do you think the Federal Government's been spending less money?

Mr. REECE. No.

Mr. JORDAN. No.

Ms. Carter, do you think the Federal Government's been spending less money?

Ms. CARTER. No, just in the wrong place.

Mr. JORDAN. Well, you would be right, because we are spending a trillion dollars more as a Federal Government than we were spending in 2007, so this idea that we've been practicing austerity is just not the case.

With that I would yield to Mr. Collins from Georgia—or I'm sorry, Mr. DesJarlais is next, and then Mr. Collins.

Mr. DESJARLAIS. Thank you, Mr. Chairman.

Thank you all for being here today. This is really kind of an amazing subject. It certainly should be a bipartisan subject because we all are struggling with these high unemployment rates, but yet to hear this testimony, there are jobs out there, we just got to figure out a dollar value right now that can compete against the Federal Government in terms of unemployment.

Just like Chairman Jordan, in my district I visited with several employers that right now could hire people. We have a rural area that $10, $12 an hour is not enough to entice people off their unemployment to go to work, and that is with benefits. So certainly we see the same frustration.

It is something that—I look at why is this happening? We all get frustrated at people and say, you know, why are they gaming the system so to speak? But yet it's human nature to take things for free, right? I mean, if we all go out to a restaurant, a fancy restaurant, and we eat and we're full, and the waitress comes by with the dessert tray and says, hey, would you like dessert? If it costs 8 or $10, you're going to say no. But if she says, hey, it's free tonight, you're probably going to take some even though you really don't need it and you're not hungry.

So that's kind of what's happening to the American society is the government is just offering up all this free stuff. So we need to work from within, and we need to work on both sides of the aisle to solve this problem.

Dr. Mulligan, you have much more eloquent ways of putting this, but really the safety nets that are supposed to be there for people who need it have really turned into hammocks under the Stimulus Act; would you agree?

Mr. MULLIGAN. We all wish we were in the spot that we could just ignore all these programs. Remember, unemployment is not a median experience. Unemployment you can measure, you call it 12 percent, 14 percent. Most people are not unemployed. And something bad's happened in your life, and you're in that spot, and it's

not a hammock time of life, but sometimes your best choice in that bad spot is to let the government help you rather than let Ms. Carter or Mr. Reece help you.

Mr. DESJARLAIS. Psychologically laziness breeds laziness. It's much better to be busy. No one likes to sit and watch the clock tick by, it's very boring. But as you said, if there's a struggle, if you're not in your chosen vocation, it's hard to, you know, go to a job that maybe is distasteful, so you get caught in this trap. And I think, Doctor, you were also referring to that; is that correct? It creates a pattern of disincentiveness.

Mr. STEUERLE. That's right. Again, I want to be very careful. I think what we're trying to achieve here is a balance act, and I think there are ways in which we can meet some of, say, the demand concerns that Dr. Stone so eloquently raises, but by doing them in ways that tend to subsidize jobs more than, for instance, just subsidize either unemployment or in some cases just general tax cuts, like the across-the-board Social Security tax cut that everybody in this room benefited from, but probably had very—you might argue that it slightly increased our demand. It might have been better to have some of that money go to help people get jobs.

Mr. DESJARLAIS. Ms. Carter, you shared several stories about why people couldn't work. I think my favorite was a while back last year when we were deciding whether to extend unemployment, and I saw on a Facebook where somebody was telling their friend that it looks like they wouldn't be able to go fishing with them on Monday because his wife had scheduled him a haircut because it looked like they were serious about not extending unemployment this time, and he was going to have to go look for a job.

You know, I wish that was a joke. But I saw several references, and that's what you were saying is that people just are just not incentivized right now to go get this. So it's our job to protect those who are really in need of these safety programs. We don't want anybody to suffer, we don't want anybody to do without, we don't children not to be fed.

But the bottom line is we know that these programs are being abused; we just can't agree on what extent they're being abused. And it seems like any time we try to make a correction here in Congress, we get into an argument over maybe the Republicans are trying to do too much, and the Democrats are trying to protect too many. But somewhere there's got to be some common ground here because we know that these entitlements are driving our debt. We know health care is a major driver. We know entitlements are a major driver.

So I really appreciate this hearing today because this problem is obvious, it should be a bipartisan solution, and we need to find a means to rein back these basically entitlements and disincentives for people to get back to work. So I know I'm stating the obvious, that that is the problem that's before us. Does anybody have any quick solutions, anything that you would recommend? I will just open that to the panel.

Yes, Ms. Carter.

Ms. CARTER. We're not saying that there shouldn't be benefits or that they should be eliminated, but there has got to be some accountability by employees, potential employees, that when we have

such a great number of jobs available in our county, why is it an option to not take a job? There has to be some accountability there. They have to apply for jobs. If there's jobs available, people should be taking jobs.

People that currently work become more and more resentful of people who do not work who are supported off of a system when you have many Americans who work as hard as they can, and everybody knows somebody that's taking advantage.

Mr. DESJARLAIS. Okay. And my time has expired, but I think what you're saying is that we need to promote a society that promotes accountability and responsibility, and we are getting away from that. Thank you.

Mr. JORDAN. Thank the gentleman.

I now turn to the gentleman from Virginia Mr. Connolly.

Mr. CONNOLLY. Thank you, Mr. Chairman.

And I must say from the conversation I've just heard, I have a sense of deja vu all over again. One wants to know why President Obama won the reelection and why Mr. Romney lost. The idea that people who are unemployed, it's their own fault and they are takers, and unemployment insurance to provide a safety net for them is a disincentive to work. Well, good luck with that theory, but I can tell you it didn't play in this country.

Let me ask, Dr. Mulligan and Dr. Steuerle, if I understood your answer correctly to Mr. DesJarlais, do you subscribe to the theory that ipso facto unemployment insurance actually serves as a disincentive to employment in this country?

Mr. MULLIGAN. Yeah, I'm not here to testify to what's politically correct. I'm here—I'm an economist. I'm an expert on the economy.

Mr. CONNOLLY. I know. I'm asking you about your answer, Dr. Mulligan, to Mr. DesJarlais.

Mr. MULLIGAN. It is a disincentive. It is a disincentive. It reduces aggregate employment, it reduces aggregate spending. It may by worth it for helping people, but helping people is not free. You have a price. You want to help people, you're going to shrink the economy.

Mr. CONNOLLY. So the reason we have 7.9 percent unemployment in part is because we have the safety net of unemployment insurance?

Mr. MULLIGAN. It's the totality of the programs of which the biggest piece would be UI, yes.

Mr. CONNOLLY. So would it be your belief that we should therefore abolish it because it serves as a disincentive, based on your testimony, to job creation?

Mr. MULLIGAN. I'm sorry, I thought I was clear about that. I said we absolutely must have taxes and safety net programs even though they discourage work and subsidize layoffs.

Mr. CONNOLLY. Why would you want something that discourages work?

Mr. MULLIGAN. Maximizing work is not everything. There's trade-offs in life. You want to help people but you want to have the economy strong, and there is a trade-off. What I have said is what has happened in the last couple of years is we have moved in a direction of really too much help and not enough efficiency.

Mr. CONNOLLY. Well, Dr. Mulligan, I'm just trying to follow your train of thought. If, as you say, it is a disincentive to job creation, or to working, what kind of help is that? I mean, why would you—I don't understand why we would want to support something like that.

Mr. MULLIGAN. Something called moderation. Let's bring, maybe bring up my chart. My chart showed a bar and indicated the amount of disincentives, okay. One hundred percent is too much. Mr. Tobin explained this. One hundred percent is overboard. It shouldn't be zero either. It should be somewhere in between 100 and 0, and we have gone in millions of cases over 100. And that is overboard. It is not a balance anymore between two goods. It's gone overboard.

Mr. CONNOLLY. Dr. Stone, do you agree with that analysis?

Mr. STONE. I do accept that one of the many effects of programs like unemployment insurance and programs that phase in and phase out like SNAP, one of the effects is a disincentive to work effect. That is one of many effects, and it is not necessarily the overwhelming effect. If there are some cases where there is 100 percent marginal tax rate on work, then that is potentially a problem. But you know, I would have to look at those data.

Now, what Professor Tobin was talking about, who actually was a professor of mine in graduate school, was back in the time we were talking about a negative income tax of the sort that Milton Friedman from the University of Chicago was recommending, and that was kind of along the lines of what Dr. Steuerle is talking about, which is instead of a whole collection of programs, there is a straight set of income support, one program.

Now, we probably need more than one program, but, so, yes, there is some disincentive effects. They are nowhere near as large, for the most part, or as prominent in people's decisions as we might think.

Mr. CONNOLLY. Are you aware of empirical, in your own studies, empirical data that it in fact serves as a disincentive to job creation in the aggregate?

Mr. STONE. Studies have found some minor job, minor disincentive effects, but not at 100 percent for the typical situation. And as Dr. Mulligan said, there is a trade-off. You don't want to get rid of the safety net. You don't want to have huge disincentives, and we don't have huge disincentives for the most part.

Mr. CONNOLLY. Well, I leave unsatisfied because I hear from the right and the left a sense of dissatisfaction. I would like to know a lot more empirically about whether we have got data that in fact can support such a contention. And if so, then why in the world would we maintain an unemployment insurance program.

Mr. STEUERLE. Mr. Connolly, can I just jump in one——

Mr. CONNOLLY. If the chairman will allow it because I have now——

Mr. JORDAN. Yes.

Mr. CONNOLLY. Thank you, Mr. Chairman.

Mr. STEUERLE. We had a similar debate about welfare recipients for some time, about 10, 20 years ago. And one result of that debate was we actually boosted something called an earned income

tax credit. Our earned income tax credit also has some negative disincentives.

Mr. CONNOLLY. I believe that came out of the University of Chicago, Dr. Mulligan.

Mr. STEUERLE. Yes, but if I could finish, and just to defend myself, I don't consider myself on the right or left on this at all, I don't consider my employer as being on the right or the left, is I was one of the people in the Tax Reform Act. I was coordinating in Treasury. We put forward the first major increase in the earned income tax credit. It's from the Tax Reform Act of '86. Gradually, that increased earned income credit allowed us to displace a welfare system that had more negative work disincentives. And I think that combination of trade-offs helped solve problems from both left and right because we got more work—less work disincentives, not more work incentives, but less work disincentives than we had in the welfare system, but yet we managed to be able to maintain a base of support for people in need. So I think there are ways this committee could work on compromises that cut across this issue.

Mr. CONNOLLY. Thank you. Mr. Chairman, thank you for your indulgence.

Mr. JORDAN. You bet. It seems to me we have got three economists talking about what Mr. Mulligan initially said, which is there are trade-offs, and why we want some kind of safety net. I think both sides agree with that. There comes a point where the safety net incentives are not what we need to maximize employment and maximize economic growth.

Dr. Stone, real quickly, now—I want to try to get two more in before we vote.

Mr. STONE. Fifteen seconds. Most of the empirical evidence I have seen about unemployment compensation in this recent Great Recession is that only a very small part of unemployment is due to the safety net program, or due to the unemployment insurance.

Mr. JORDAN. I think Mr. Mulligan's research shows that 4 million have a complete disincentive to going back to work based on unemployment and a host of other things, and that would be, if my quick calculation is right, one-third of the total unemployment number out there. So that is pretty significant.

Mr. DesJarlais, a quick statement and then we have got to votes, but I wanted to give 5 minutes to Mr. Collins.

Dr. DESJARLAIS. This is in response to Mr. Connolly. I was not trying to sound uncompassionate. Penalizing people for working is not compassionate. We need to rethink and restructure the way we administer our social safety nets so that we are actually empowering people rather than dooming them to dependency, and that was my point.

Mr. JORDAN. No, well said. I think we have enough time. Mr. Collins a quick 5 and then I want to get—Mr. Horsford was actually supposed to go first. I wanted to give you a chance before we go vote if we can. The gentleman from Georgia.

Mr. COLLINS. Thank you, Mr. Chairman. I think one of the things that is important especially from my background is uplifting people and empowering them to do work that they feel good about, work that they can be encouraged, and also, you know, have a job that they can look forward to going to——

Mr. JORDAN. Would the gentleman yield for just one second?

Mr. COLLINS. I will always yield, Chairman.

Mr. JORDAN. Just for those members leaving, we will reconvene at 3:40, for just—if you want to come back for question, I want to give you plenty of time. We will do that. The gentleman can proceed.

Mr. COLLINS. Thank you, Mr. Chairman. And just following through that, is we have got to provide those—Dr. Steuerle, you mentioned something in your testimony that talked about that the government policies have led to significant long-term unemployment over time. But it also, the thing that interests me the most, and I think something that we are missing here, instead of getting, you know, focused away from where it actually—how we do help people and then how we empower them to be all that they can be, so to speak. And you mentioned the long-term consequences of prolonged unemployment in your testimony. I would like for you to elaborate on that a little bit more, and especially from the incentive, not only the incentive side, but what people lose by not being employed.

Mr. STEUERLE. Well, that's why I have much to add to what I already said in terms of habit formation and the consequences for depression and things like that. But in point of fact, the main way that most of us learn is on the job. We also think of education taking place in the school, but in fact, when you go work for Mrs. Carter—Ms. Carter, you actually end up getting educated as you stay on the job and that is one reason over time she is able to promote you to higher levels of work. So you are not only losing some human capital by being unemployed, but you are losing that educational opportunity that you would have on work.

Again, I don't want to say, and let me be clear, most people do not want to be unemployed. I don't want to—I don't indicate by any means this is something people want. I just think we need to figure out ways to be able to help them more.

Mr. COLLINS. Exactly, and I think, that's my point is, is people want to work. I believe that that's the genius of the American system, that we want to work. We want to provide those incentives, and I think that you are providing something that, that sometimes we miss in what we do lose for those who are actually working. And Ms. Carter's place is a place to do that. You learn more than just a job skill. You learn life, and I think that is so important.

One quick question, and I may come back in just a second. Mr. Reece, one of the things that you had mentioned in employment, is you talked about the cost that they would actually in some ways do the cost-benefit analysis, I mean, which is a complex thought process to go through. So what you really saying is they are not qualified—they are not unqualified for the jobs that you could be providing.

Mr. REECE. No, they are very qualified individuals. My belief, and the doctors here are talking about statistics and that is great, but I actually know the statistics. They come in my office and meet with my recruiters. And they are hung up on what they had accomplished in their lives at a certain point prior to the recession. And their irritation comes that they can't get that same thing. They can't get the $15 an hour job today, but they could get the 13

hour—dollar-an-hour job. And until they are forced, and I hate to use that harsh word, but until they are forced to do something, much like a parent sometimes has to force their child to do, then they are going to continue to use those benefits until the day they run out.

It is human nature to want—to not go backwards in life. But at some point in time, I think we as people have to make a decision. Am I better off stepping back just a little bit, taking a lower pay rate to go to work for Ms. Carter and letting her train me to be something better? She is investing in me, but I'm going to have to invest in her as an employee.

Mr. COLLINS. It goes back into the maturity cycle as we move forward, and I think people do want to work. And I think that's what I want to emphasize here. This is not a negative hearing. This is a positive hearing in terms of what we can do. And really, and Dr. Steuerle, following up on that I love the academic and real world. It is almost like a reality TV show here, you know, we have this—and one of the things, Dr. Stone, I would like for you to blame, or maybe blame is probably not the right word, but discuss the fact of the constriction of the economy, the constriction of the economic forces going along as a higher reason for why there is up and down employment. And there is other things we can talk about, disability; there's other things that can go along with this, which have grown, amazingly, when jobs were low. It seems like there is a bad correlation there. When disability claims have all of a sudden now skyrocketed when jobs are available. I ask you, how do you reconcile the research that you have done with the real world sitting right besides you on each side in the sense of just taking it from a constriction standpoint, and not just the sense that we are—there may be other things involved here?

Mr. STONE. I have no doubt that people have shown up saying I would like to stay on unemployment and keep—rather than take a job. I have no doubt that some small businessmen cheat on their taxes. I mean, these kind of things go on, and there is a balance of can you—we don't have the resources to enforce the—we have chosen not to invest in the resources to support the requirement that you search for a job, things like that. Our unemployment——

Mr. COLLINS. Well, okay, as far as enforcing a requirement to go get a job, I mean, that's the intuitive part here. I mean, that is a problematic, you know, issue here, and I know my time is running out, but I'm—to say to them to put money to enforce that, really, sort of defeats or adds to the problem we are talking about.

Mr. STONE. Well, and might not be worth spending just as we decide how much we want to spend with IRS audits versus accepting a certain degree of——

Mr. COLLINS. I understand. All right, I think it is a positive discussion. I think it is a first step. Thank you, Mr. Chairman.

Mr. JORDAN. Thank you. Mr. Horsford, we have 5 minutes and 21 seconds in this vote, but they always go long because there is only 88 people who have voted. So you can take your full 5. You can take part of it and come back, but that is up to you because I took you out of order. So are you up.

Mr. HORSFORD. Thank you, Mr. Chairman. I appreciate very much the panel, and I know people come from a broad perspective

on this. Prior to coming to Congress, I ran the Culinary Training Academy in Las Vegas that trained thousands of people for careers in partnership with 26 of our largest employers in Las Vegas. And I know, without a doubt, after 11 years of doing that work, that people want jobs. They do not want to be on food stamps. They don't want to be on long-term unemployment. They don't want to rely on assistance. They want a job. But for those individuals who cannot find a job, they also need to depend on unemployment, and other work supports in order to survive.

And so I would like to just reframe a bit of the discussion, because I think we have focused so much on a disincentive to work. I would like to focus on an incentive to survive. And the fact that people who are unemployed, Nevada has higher than the national average unemployment. My unemployed constituents are not lazy. They are not immature. They have a desire to work, but our economy is not producing the types of jobs that they are trained or skilled to do right now.

And so my question is, how can we balance those interests, Dr. Stone, to provide us assistance that allows people to buy food, pay their rent, and you know, provide for the basic necessities for their family as a bridge until they are able to find employment?

Mr. STONE. Well, the point of most of our, and the way most of our safety net programs work these days is that there are strong work requirements attached to them, and large numbers of SNAP recipients have good work histories, are tied into the labor force. They fall on hard times; they go on SNAP. It is not like it is perpetual not in the workforce. Now, there is two issues. There is the short-run issue that this economy is really in—still in tough shape, and the income support is important, and more important when it is harder to find a job than when it is easier to find a job. These incentives, as Dr. Steuerle said, you worry about incentives when the economy is in strong shape and there is plenty of jobs available and people are discouraged from working for one reason or another.

We have done a lot in our social safety net to minimize that outcome. So I think that the trade-off is that we want to make sure that people who truly fall on hard times have the support they need to get through, and that includes unemployment insurance for people who lose their jobs through no fault of their own.

Mr. HORSFORD. What about the concept of—for those who have worked? We have a program that trained people to be guest room attendants, food servers. I recall this one woman, she worked for 20 years in the same job and became displaced and did not know how to really go about applying for jobs, or to market her skills, or to transfer those skills. So what about that within the framework of this discussion today?

Mr. STONE. Well, that's an important thing. And that's why job counseling for unemployed workers can help them have a realistic view of what their job opportunities are, have a realistic view that, you know, jobs matter, strengthen that, but that costs money. And so there's that tension between the budgetary cost of us having more job counseling and the fact that it actually could be helpful in the kind of situations we are all talking about.

Mr. HORSFORD. Yeah, I think, Mr. Reece, you hit on it. Like sometimes we had to counsel people that the job that they wanted

to do wasn't going to be readily available; construction, for example, which was our number two industry, there just wasn't those jobs.

Mr. REECE. Right.

Mr. HORSFORD. And so to help people understand that, yeah, you might have to go back and retool your skills, and that might mean you are going to get paid a different wage when you get placed, but at least getting you training, and then placement into a new career field is something that has to be part of the equation. So you know, I understand that, but that's—sometimes it takes a professional person who can provide that unemployed individual that perspective.

Mr. REECE. Right. And if I could comment just quickly to that. You are exactly right from the standpoint that the person has to be counseled. But when a client expects you to provide them with the best possible applicant, oftentimes the reluctance that our recruiters see in that person as they are trying to encourage them to take the lower paying job, and to take the employer's training, when you see that lack of interest, and then you have someone else sitting over here that is looking more attractive to place, you tend to give the client the more attractive looking applicant, the one that has the higher skill level. So sometimes without that eagerness to want the job, our recruiters are sometimes reluctant to recommend them for the job.

Mr. HORSFORD. Thank you, Mr. Chairman. I will finish there. I would say I would love to—hope that we can talk about the chronically unemployed and the fact that there are actually laws on the books in some States that are disincentives to employers hiring the chronically unemployed, and we need to have that discussion as part of this as well.

Mr. JORDAN. Yeah, we will reconvene at 3:40 and we can bring that issue up and a host of others. Thank you all for being here. So we are standing in recess.

[Recess.]

Mr. JORDAN. The committee will come to order. We appreciate our panel's patience, and we will start with the gentlelady from Illinois, Ms. Duckworth.

Ms. DUCKWORTH. Thank you, Mr. Chairman. I have been somewhat aghast at the tone of this hearing, and being a freshman Member, perhaps I will learn over time. But you know, my father who worked from the age of 14 and lied about his age to enlist in the Marine Corps and build a life, lost his job at 55 and was on unemployment insurance for a very, very long time. In fact, he maxed out his benefits. And he didn't not find work because he was lazy. He did not find work because he did not have a trade or a skill. He was a business executive. He couldn't find work because he was 55 years old, and no one would hire him because he was overqualified.

I watched that man collect grocery carts to return them for $0.25 a pop. This is an honorable man. I was on food stamps, and oftentimes those food stamps provided the only meals that I ate throughout my teenage years. I hope you don't think that I look like someone who is lazy and on government handouts.

I have a question, Ms. Carter. You, in your testimony, you said that: "We have reached a point in society where it is no longer honorable or desirable to learn and perfect a trade skill." You also say in your testimony that: "An unintended consequence of benefits is substance abuse."

And I'm going to ask you two questions. The first one is with regards to receiving government benefits being linked to substance abuse. Do you have children in college, or did you go to college and receive Pell grants, or subsidized student loans or anything like that yourself?

Ms. CARTER. No.

Ms. DUCKWORTH. You did not?

Ms. CARTER. No.

Ms. DUCKWORTH. Do you think then for other people's children who are on Pell grants that we should have them give a urine sample prior to receiving those government funds for education?

Ms. CARTER. I didn't say anything like that. That is not anywhere near what my testimony was about. We have a problem in our county. We do not have enough employees to fill jobs. We consistently hear unemployment is so high. There's no jobs. There's no jobs for the middle class. We have jobs. We don't have workers.

Ms. DUCKWORTH. Your testimony actually says, and I'm reading it verbatim. "An unintended consequence of benefits is substance abuse." I think that——

Ms. CARTER. That's true.

Ms. DUCKWORTH. I think there are many people who receive benefits who are not drug addicts and are suffering—are abusing drugs.

Ms. CARTER. My statement doesn't say 100 percent of people are on—have drug problems. In our county we have a significant drug problem. When employers release people because they test positive for drugs, they have accidents in the workplace, they are accepted into the unemployment program with no questions. That doesn't correct their problem, and it doesn't support unemployment.

Ms. DUCKWORTH. And I—you know, I have worked with veterans for a very long time, and veterans are a community with a very high unemployment rate. I think for the 20 to 25-year-old age group, it is twice as high as the same age group in the general population. And I would think that they have perfected a trade and a skill, and that they are very honorable. So I don't understand how we say, how we connect people who are on unemployment who are on unemployment because they are there through no fault of their own, are people who are not willing to find a trade or accept employment, when I know many, many, many thousands of veterans try very hard to find employment, and no one will hire them. Yet, they have a trade and a skill.

Have you tried to hire veterans specifically and tried to recruit among the veteran community?

Ms. CARTER. I believe that we have. We haven't personally. We place ads if we are looking for people. We work with our local job and family services unit to have—make a match with someone who is looking. Again, we don't have those people applying for jobs. We can place an ad and have zero people apply for an ad—for a job.

Ms. DUCKWORTH. And then you think that is probably because they are out using drugs and not wanting to develop a skill and not because you have not done a good job of reaching out to a community like veterans who have extremely well trained, who are extremely well trained in trades and certainly have been able to perform in some pretty severe conditions?

Ms. CARTER. You are misrepresenting what I'm saying. It is not about 100 percent of people. It is about a large percentage in our county that have these issues, and again are being supported by government programs. And if—there are definitely people that require the assistance. Nobody has said that's not the case. But there is also, again, a grand case—cases of abuse, and again, we are trying to grow the economy. We are trying to provide jobs.

Ms. DUCKWORTH. I'm sorry, I have to interrupt because I'm running out of time. So do you think then that we should only drug test those people that have a problem, or are you saying that we should drug test 100 percent of people who are on unemployment? Because if it is not 100 percent of the people that have the problem, why would you trust 100 percent of them?

Ms. CARTER. I'm saying that the government should not be providing benefits to people who are spending the money on drugs and that are not providing—are not working.

Ms. DUCKWORTH. I'm out of time, Chairman.

Mr. JORDAN. You can take some more if you like.

Ms. DUCKWORTH. Thank you, Mr. Chairman. My next question is for you, Dr. Stone.

One of the things that I have been able to work on that I'm very proud of in the State of Illinois is actually incentives for employers. I think that employers who hire someone who has been unemployed for, for example, more than 6 months, or employers who hire someone such as a veteran, should be rewarded, should be rewarded for taking that chance because when you have someone who is an infantryman, it is hard to figure out how an infantryman is going to fit into your business, or how someone who fixed tanks will fit into your business.

Could you talk a little bit about a different type of program, perhaps not the unemployment insurance, but how you would think—how you feel the effects of incentives for employers—in Illinois, we provided, when I was a Director of Veterans Affairs, $600 per every employee who was a veteran that a company hired. It is up to $5,000 now. Could you talk a little bit about the employer benefit side to reward employers for hiring the unemployed?

Mr. STONE. Yeah, and that's a good question—that's a very good point that you raise, because we talk about some of the problems of the long-term unemployed or the people who don't look that attractive when they present themselves to the employer. And if the employer can be given some incentive to take a chance on that person, which is the way I interpret how your program works, then there is going to be a good percentage of those people that they take a chance on that are going to turn out to be better workers than they look like they are, but they need the chance.

Ms. DUCKWORTH. Thank you. Dr. Mulligan, could you speak a little bit from an economist's perspective on incentives for employers

and how you feel that might work in terms of helping with the unemployment problem?

I mean, if the insurance is not, you know, the unemployment insurance is not the answer.

Mr. MULLIGAN. Incentives for employers, you know, fit into the calculus. I talk about the reward to working and it includes fringe benefits. Things that come on the employer's side. So if there were a subsidy for hiring, that would increase hiring. And if there were a subsidy for having people on the payroll, that would reduce layoffs. That would—it would have those kind of effects. And as economists we kind of know how to quantify that. Until you tell me how big the program is, I can't tell you how big the effects will be, but I know the direction.

Ms. DUCKWORTH. Thank you. Thank you, Mr. Chairman.

Mr. JORDAN. I want to thank the gentlelady for her questions and for her service and your family's service to our country. We certainly appreciate that.

It seems to me we have got this quandary. I would agree with what both sides of the aisle said. Most people do want to work. They want a job. But yet, the incentives are such that if the real world experience that Miss Carter related in her testimony, I believe was 8 out of 10 people she interviews for potential employment at her company decide that it is just not worth it, even though it is $12 an hour starting pay plus benefits.

So that's what we are trying to get at. And I love the graph that I think Dr. Mulligan put up where it shows that, you know, most people want to work, but they are also rational, smart people. And if in fact going to work means they are going to lose financially, then that is the quandary we are in and we have got to try to address that.

Let me just do a couple of questions for Mr. Stone, excuse me, Dr. Stone. You talked about a balanced approach to dealing with our problem. So do you—you support raising taxes on who, and if so, how much? What kind of tax increases would you employ?

Mr. STONE. I support looking at the tax expenditures, the tax loopholes. That gets talked about in the context of——

Mr. JORDAN. Which ones specifically are you referring to? We are all against loopholes. That sounds like something bad, but tell me which specific ones you think make sense.

Mr. STONE. That's a tough decision because——

Mr. JORDAN. But you have got to have——

Mr. STONE. —as witnessed by the fact that we still have all of those loopholes.

Mr. JORDAN. Yeah, you're—but I mean, you don't have the political implications that we, you know, we might have as Members of Congress. As an economist, which ones specifically would you get rid of? Which expenditures, loopholes, whatever, credits, deductions, which one would you go for?

Mr. STONE. Look, on economic grounds, the big ones are the hardest to do politically, employer healthcare, the home mortgage deduction, all those things are ones that you want to look seriously at. That's where money is, but those are politically tough, and economists have problems with them. Economists have recommended alternative ways of approaching that issue, but——

Mr. JORDAN. Do you support raising marginal tax rates?

Mr. STONE. We supported letting all of the upper-income Bush tax cuts expire, so yes.

Mr. JORDAN. So you supported raising taxes on middle class, and in effect, business owners like Miss Carter who is an LLC or not a C Corp?

Mr. STONE. Our—a lot of people's definition of middle class would not go to $400,000 a year.

Mr. JORDAN. Do you support additional revenue from that, so let's say you would have got all of those tax increases that you were—the 2001, 2003 tax increases would have expired, those tax cuts would have expired so, in essence, raising taxes on all of those brackets, what additional taxes aside from loophole, or do you support additional marginal tax increases?

Mr. STONE. We don't have a program of tax increases, or a program of spending cuts.

Mr. JORDAN. What I'm trying to get at is, you talked a lot about, you know, contractions and things that would contract the economy. It seems to me, and you talked about how government spending is—we have been austere. I mean, I would argue the last thing we have been is any type of austerity in this government. We have never seen so much spending. But you talked about contraction, how that impacts demand, how that impacts the economy. Raising taxes on job creators, how is that going to help grow jobs and improve the employment situation that we all want to improve?

Mr. STONE. The specific—the spending cuts that I talked about were spending cuts——

Mr. JORDAN. No, but you talked about spending cuts in the same breath you talked about with Mr. Cartwright, you talked about a balanced approach, and you just told me in a balanced approach, you preferred tax increases, and you preferred raising taxes on everybody when this so-called fiscal cliff debate we just had instead of just top margin you supported all of the marginal brackets going up.

Mr. STONE. No, no, no. I didn't—I said that the top, the marginal rates on incomes above $250- and $125- not——

Mr. JORDAN. Okay, my question is, do you support further marginal tax increases? You won't answer that one. And I'm wondering how if you think contracting, you know, by not spending somehow we are going to hurt the economy and yet when you take money out of the economy by raising taxes on small business owners, how that is going to help promote jobs and increase employment. I can't get the contradiction here.

Mr. STONE. First of all, we have—almost all of the deficit reduction that we have done so far has been on the spending side. There has been about $1.5 trillion.

Mr. JORDAN. Doctor, how can you say we have done any deficit reduction? That is all in the outyears. We haven't done anything. We are spending more in discretionary spending this year and certainly more overall spending this year than we spent last year, and last year we spent more than we spent the year before, and 2 years ago we spent more than we spent 3 years ago, and 3 years ago we spent more than we spent 4 years ago. So how have we cut spending? Do you not agree the government is bigger today than it was

4 years ago? We are spending like $3.6 trillion. In 2007, we were spending $2.8 trillion. Last time I checked—even as a Republican I can do that math—last time I checked that is a lot more.

Mr. STONE. The measure we would look at would be spending as a share of GDP, relative to the size of the economy. It's—you need a metric. You can't just talk about dollars, and it's true——

Mr. JORDAN. That is huge spending. The economy has been contracting for the last 4 or 5 years, just finally started to grow at that wonderful rate of 1.5 percent after all this spending we have done, that further confirms. So spending as a percentage of GDP is way up because GDP has been down. That is what is killing our economy overall.

Mr. STONE. A large amount of the spending that has gone up in the past few years has been spending that has to do with emergency, with temporary spending, temporary programs. The budget caps that are in place——

Mr. JORDAN. The very temporary programs that we are talking about today that have been a disincentive to work, exactly.

Mr. STONE. Well, I don't agree that they have been a major disincentive to work. But I agree that they have been an important—my view is that they have been an important contributor to keeping the recession from being worse than it was.

Mr. JORDAN. Well, it is tough to prove a negative. What we can prove is we are spending a lot more today than we were 4 years ago. That's obvious. That's a simple subtraction, mathematics addition problem.

Mr. STONE. And over the past couple of years, spending as a share of GDP is going down. And the spending that I was talking about was, in my testimony, was spending on goods and services by Federal, State, and local governments, which has been very contractionary. We had some support for State and local governments in the Recovery Act, but we stopped doing that. And the budget constraints that State and local governments have faced has forced them to be very austere. Huge numbers of jobs have been shed, and the output, and now purchase of goods and services from State and local governments is way down.

Mr. JORDAN. Let me do one other thing before turning to the ranking member for a second round.

Dr. Mulligan, let me ask you, the big thing that's coming starting to impact right now and employers are starting to look at, is the Affordable Care Act—some Obamacare, Affordable Care Act. CBO estimates that this piece of legislation will lead to 800,000 fewer Americans working in the economy by the end of this decade. Do you agree that this is going to be an impediment to job creation, going to cause a loss of jobs, and if so, would you agree with CBO? Do you think they are right, they are wrong, that they got it, or missed it, or what?

Mr. MULLIGAN. Well, CBO, I have seen that 800,000 number. I have seen something else they put out, too, very earlier. I was impressed by this. They did some work on marginal tax rates from the sliding-scale aspect of the exchange subsidies, and they talked about marginal tax rates in the neighborhood of 25 percent. That would be one of the biggest squares in my chart. It is not there yet. But when they did their 800,000—it is not the way I would have

done it—when they did their 800,000 they ignored that 25 percent disincentive. They have not calculated. I have been working with them and they have not calculated how many millions of people will have tax rates over 100 percent under Obamacare. Maybe that is something they will do, but they haven't factored that in yet. So I'm pretty sure when you factor that in you are going to have to say there is going to be more than 800,000 jobs lost. I wish I could bring you numbers today. It should be a lot more. How many more, how many millions, I can't tell you right now.

Mr. JORDAN. Can you hazard a guess?

Mr. MULLIGAN. I think it would be on the order of what the Recovery Act did. I mean, the exchange subsidies are kind of like that COBRA subsidy in my graph, but on steroids. So I kind of think of it on the order of the Recovery Act, which means multiple points on the unemployment rate, or nonemployment rate. I'm not sure whether these people will go into unemployment or out of the labor force, but something like that.

Mr. JORDAN. Really quick, before turning to Mr. Cartwright.

Doctor, your thoughts on the CBO assessment that 800,000 fewer people are going to work as a result of the Affordable Care Act.

Mr. STEUERLE. Well, I think it raises an issue of two groups of the population we haven't really focused much on in this hearing. The first one is the elderly. I think one of the reasons that CBO came up with this number, I may be wrong, but I think one reason they came up with this number, is now those people who want to retire early, they do have access to health insurance. And so this may be a major group upon whom this has an impact. And I don't know that it is necessarily a combined marginal tax rate, it just may mean at that point with some matched amount of 401(k), with health insurance, they can make it to 62 or something and retire for a few more years. I remind you, the average couple now gets benefits that retire at 62 for about 27 years, for younger people going towards 30. But there's another group that we haven't talked about which is on the other end of the spectrum that doesn't really have access to almost any of these welfare programs and that is the young. And I gave statistics in my testimony also about what's going on with the labor force among the young and younger workers, and that is not an issue of the social welfare programs, in many cases particularly young men, especially some young women, especially those who don't have children, don't really have access to almost anything in the social welfare system. I think our systems do a pretty bad job in terms of dealing with their needs for the right type of training and the right type of job opportunity if they are not going to college. I think the whole program of apprenticeships needs to be examined. And so I hope this committee, beyond just this issue of combined tax rates and everything else will start to look at also what is happening in employment patterns among the young. I don't have an answer there, but I think that's an issue worthy of consideration, and I say it goes beyond just what social welfare programs we have, because in many cases, they don't have access to them that help in any way.

Mr. JORDAN. Great, thank you. The gentleman from Pennsylvania.

Mr. CARTWRIGHT. Thank you, Mr. Chairman. And Ms. Carter, we certainly don't mean to ignore you, and I wanted to ask you a question. What is the name of your company?

Ms. CARTER. Carter Machine Company.

Mr. CARTWRIGHT. And okay. What is the town that it is in?

Ms. CARTER. Galion, Ohio.

Mr. CARTWRIGHT. Galion, okay. And is it your testimony that you have up to 20 jobs available there right now?

Ms. CARTER. We could, yes.

Mr. CARTWRIGHT. So if I called up your company, they would say they are hiring right now?

Ms. CARTER. Yes.

Mr. CARTWRIGHT. Okay. All right. And now, Dr. Stone, I want to follow up with you, and I promise not to interrupt you. Why is it important to talk about spending as a percentage of GDP?

Mr. STONE. Well, because it is a measure of how much we are spending relative to our capacity to engage in all kinds of things; that it makes no sense to talk about 1950, how many dollars we were spending on something in 1952, compared with how many dollars we are spending on it in 2013. Because there has been so much price change in between.

Mr. CARTWRIGHT. Okay.

Mr. STONE. It is not just a matter of real. And the economy has been growing, so we can support a certain level of spending in a bigger economy than we can in a smaller economy.

Mr. CARTWRIGHT. Okay, so that's why it makes no sense to talk about us spending more dollars today than we did last year, okay.

Now, I also wanted to touch on something called automatic stabilizers. A key tool, I think you have been touching on, used to ease the consequences of negative economic shocks in response to a downturn in the economy, automatic stabilizers such as unemployment compensation or even food stamp benefits automatically increase as jobs are eliminated and more people become eligible for the benefits.

These benefits provide critical income support, obviously, to unemployed individuals and they also ease financial burdens while the recipients seek permanent employment.

Dr. Stone, do you agree that unemployment compensation and food stamp benefits are effective forms of support to the individuals and families struggling during economic crises?

Mr. STONE. They are very effective and they are very supportive of the economy. That is the automatic stabilizing role, is that they keep spending at a higher level than it would be if these people were left on their own.

Mr. CARTWRIGHT. So do you agree then that businesses and employees of businesses at which food stamps and unemployment recipients spend their money are positively impacted by those programs as well?

Mr. STONE. That's right. In a weak economy, that's extra demand. If we were back in the 1999 economy, when the unemployment rate was closing in on 4 percent, there would be questions about spending here or crowding out spending there, but that makes no sense in today's environment when there's so many idle resources.

Mr. CARTWRIGHT. Well, the fact of the matter is, if you don't have a job, you don't have income, you don't really have the option to put money in the bank, generally speaking, beneficiaries of these programs spend their unemployment or food stamp benefits just as quickly as they receive them, causing a boost in demand, nationally, for goods and services in the economy.

Dr. Stone, is that correct?

Mr. STONE. That's right. The Congressional Budget Office finds that to be the highest bang for the buck programs in—of the ones they look at in a weak economy like we have been experiencing.

Mr. CARTWRIGHT. And you mention the Congressional Budget Office. Is that a partisan outfit?

Mr. STONE. No.

Mr. CARTWRIGHT. Okay.

Mr. STONE. They have had Republican and Democratic directors. They work for the Congress, the whole Congress.

Mr. CARTWRIGHT. Now, Dr. Stone, a recent study by Wayne Vroman examined the stabilizing role of unemployment compensation during the '07, '09 recession. He found that the unemployment compensation, it closed 18.3 percent of the GDP shortfall that was caused by the recession. He also found that extension of benefits played an important role in that stabilization effect. We can't ignore the positive effect of those benefits, nor can we ignore the harm it would cause to the unemployed during an economic downturn if these benefits were not there to respond.

Now, Dr. Stone, isn't it also important to note that the increased budgetary cost associated with the expansion of these programs is temporary and projected to decline as a share of the GDP?

Mr. STONE. Yeah, and decline in dollar terms, too. The number of unemployed will fall as the economy improves, and Congress has always let emergency unemployment programs expire once the economy is strong enough. They have just never done it any time in the past when the unemployment rate was higher than 7.2 percent and we are not expected to get below that in CBO's projections until sometime in 2014.

Mr. CARTWRIGHT. Well, thank you, Dr. Stone. I appreciate your comments.

Mr. JORDAN. Real quick. Dr. Stone, if food stamps and unemployment insurance increase demand and are stimulative in the economy, why then should we—why shouldn't we just increase them even more? Why not—I mean, I don't—I just fail to grasp this logic that says, oh, these are the best stimulus programs we can do in a difficult economy. Well, if that is the case, we should be pumping a lot more money into these programs.

Mr. STONE. They have high bang for the buck. There are obviously political constraints on how high you would want to push those things.

Mr. JORDAN. Do you think there should be an asset test required before an individual can receive food stamps? Do you agree with the fact—well, let me ask you this way. Do you agree that waiving the asset test for food stamps is a good thing?

Mr. STONE. I don't have a—I'm not an expert on food stamps.

Mr. JORDAN. Well, I mean, right now there is an income—there is an income requirement, that's it. You don't have income, you get

food stamps. There used to be an asset test. In other words, today, in some places you can have, you know, three brand-new cars sitting in the garage but you don't have an income, you are eligible for food stamps. Do you think that is appropriate?

Mr. STONE. In many of our programs where we have asset tests, they have not been——

Mr. JORDAN. This is why the lady in Michigan who won the lottery could still get food stamps. She doesn't have an income, but she just, you know, she landed a little bit of cash there all of a sudden, yet she can still get food stamps. Do you think that is right?

Mr. STONE. There are particular examples.

Mr. JORDAN. There used to be an asset test. There is no longer an asset test. In some situations do you think that is appropriate? Simple question.

Mr. STONE. There are problems with asset tests, and there are problems when you get rid of asset tests. It is a trade-off, a balance.

Mr. JORDAN. Do you think there should be a work requirement—no, let me ask it the other way. Do you think it is appropriate for this administration to waive the work requirement for able-bodied adults receiving some type of social services, some type of welfare recipient?

Mr. STONE. In a situation where it's—in an economy like——

Mr. JORDAN. The law has been around for 16 years, signed by President Clinton, bipartisan support.

Mr. STONE. Yes, President Clinton, whose——

Mr. JORDAN. Do you think there should be a work requirement?

Mr. STONE. Waiving it at a time when jobs are hard to find makes perfect sense to me.

Mr. JORDAN. Let me ask you, Dr. Steuerle. Do you think a work requirement would help with this phenomena you describe in your testimony where people who are unemployed for a significant period of time, it is not good for that individual, not good for that family. Miss Carter is talking about how it is not good for the community, good for her county. Do you think it would be helpful if there was a work requirement that may help them retain some of those skills as they are trying to find that employment that we all know everyone wants to find? Do you think that would be helpful?

Mr. STEUERLE. I think it would be helpful to try to move in that direction. I think work requirements are very hard to implement. That is one reasons, for instance, through devices like earned income credit, it effectively has a work requirement because you don't start getting the benefit until you at least do some work, even though I recognize—I'm sorry, even though I recognize that at some income level——

Mr. JORDAN. I understand they are hard to do. I mean, lots of—you know, lots of things that are worth doing are hard to do. That is just the way life is. Any goal that is worth achieving is never easy. That's life. But my question to you is, do you think it helps if we have that, helps those very individuals you talked about in your testimony?

Mr. STEUERLE. I would move in that direction, but one way I would do that is probably trying to provide more money in work supports and less money in consumption-related programs.

Mr. JORDAN. Fine, but there is a work requirement. That is now being waived in all places across the country.

Dr. Mulligan, do you think unemployment compensation and food stamps are actually stimulative to our economy?

Mr. MULLIGAN. No, they are not stimulative. I think—there's a couple of mistakes I think made here. It was said that the CBO showed, and the CBO found, and Mr. Vroman showed that UI and food stamps are stimulative. They didn't. They assumed. The CBO assumes——

Mr. JORDAN. Oh, so there's—there's no empirical, there's no real research that confirms what Dr. Stone described?

Mr. MULLIGAN. Right, but there is research on—first let me say, there is research in a couple of areas related to this. Number one, research shows pretty clearly that the poor and unemployed tend to quickly spend what they have on basic needs. Mr. Cartwright mentioned that. That's true. They quickly spend——

Mr. JORDAN. Yeah, that's common sense. We all understand that.

Mr. MULLIGAN. That's why the programs have intrinsic value, but that is different than stimulative value. You have to recognize that some of them, not all—Mrs. Duckworth, I think, didn't characterize it right. It is not true about all, but some are going to work less. And working less is a ticket to spending less. They kind of go together. Unless you are in the 100 percent tax situation, they go together. So it actually leads to less aggregate spending. I think what gets forgotten is these programs have to be funded. Somebody's got to buy the government bonds, or pay the taxes, or maybe it's some other program that gets shrunk, and those people are going to spend less, and you have to count that, too.

Mr. JORDAN. Yeah, opportunity costing——

Mr. MULLIGAN. So the aggregate spending declines, and the thing that CBO, that—the way they make their assumption is, they look at studies of purchases. Dr. Stone mentioned government purchases, but you weren't asking me about purchases. You were asking me about transfers. Transfers are very different. Purchases means you pay a guy to work. You pay a guy to build a highway. You pay a guy to help build a military airplane. Transfers mean you pay a guy for not working, and really they are kind of the opposite. But CBO and some other economists have picked up on the purchases study and said, hey, purchases expanded the economy; therefore, transfers must expand the economy, and that last piece of the logic is backwards.

Mr. JORDAN. Yeah, well said.

I want to thank you all for being here today. We have had a great hearing. Your testimony was very much appreciated. Sorry we had to have a break in there, but that is the way this place works. There's votes called at certain times, and when it is time to vote, we have to do that. So this committee is going to continue to look at this issue, and again we appreciate your time and we stand adjourned.

Thank you.

[Whereupon, at 4:10 p.m., the subcommittee was adjourned.]

Opening Statement – Chairman Jordan

Unintended Consequences: Is Government Effectively Addressing the Unemployment Crisis?"

February 14, 2013 – 2:00 p.m.

Today's hearing is about America's unemployed and understanding the failure of federal efforts to get them back to work.

Four years ago this week, an $800 billion stimulus spending package was signed into law with the intent of creating jobs and jump-starting economic growth. The Obama Administration justified the stimulus with a report stating that as a result of this legislation, the unemployment rate would *never* exceed 8 percent and would be 7 percent and falling by February of 2011. Yet, the unemployment rate is still hovering around 8 percent, representing 12.3 million Americans out of work. When we also count the broader universe of people seeking work, the unemployment rate climbs to 14.4 percent.

We are still in a jobs crisis and we must understand why.

Since 2007, there have been at least a dozen new or expanded federal safety net programs. For example, various unemployment insurance and food stamp programs have increased and eligibility has been expanded. The most drastic of these changes came via the 2009 stimulus law. These additions to the way the federal government assists the unemployed have, in their totality, collectively changed the incentives faced by those seeking work.

One of our witnesses today, Professor Casey Mulligan of the University of Chicago, has done groundbreaking research that shows that as a result of our layered social safety net programs, there is a large number of American households for whom the reward for working is zero or negative when compared to the benefits received when unemployed. In other words, a person might have more income to use or save as a consequence of working less. Prof. Mulligan estimates that in 2009, approximately 4 million individuals would either not benefit at all from returning to work or, even more troubling, would actually be worse off financially from getting a job.

No one believes that President Obama or my colleagues on the other side of the dais wish to prolong the time Americans spend without jobs. The focus of today's hearing is on unintended consequences that too-often stem from well-intentioned policies.

In addition to our expert economists, this afternoon we will also hear from two job-creators who have experienced this unsettling phenomenon first hand.

Some may charge that the arguments presented here today are uncompassionate to folks struggling to find work, but nothing could be farther from the truth. Of course we believe in a safety net for those who have fallen on hard times. But people must not be made worse off as a result of that safety net. What is truly not compassionate is penalizing people for going back to work. We need to *re-think* and *re-organize* the way we administer our social safety net so that we *empower* people rather than dooming them to dependency.

I now yield to the Ranking Member, Mr. Cartwright from Pennsylvania. I'd like to welcome Mr. Cartwright to the Congress and to the Subcommittee and I look forward to working closely with him as we move forward.

Statement of Congressman Gerald E. Connolly (VA-11)
Subcommittee on Economic Growth, Job Creation, and Regulatory Affairs
Committee on Oversight and Government Reform
Unintended Consequences: Is Government Effectively Addressing the Unemployment Crisis?
February 14, 2013

Mr. Chairman, four years ago, when President Obama first took office, our economy was reeling from the worst recession in 80 years. We were losing more than 750,000 jobs a month. In total, 8 million Americans lost their jobs during the Great Recession. Under Democratic leadership, Congress passed the Recovery Act to provide tax cuts and additional assistance for those families struggling to make ends meet. We also made critical infrastructure investments to create jobs and help get our economy back on track. Since that time, the private sector has created more than 6 million jobs, but as the President acknowledged this week in his State of the Union address, there is still much to do. Too many people are still searching for work.

I know my Republican colleagues think the Recovery Act was an overreach, hence today's hearing, but what about the "unintended consequences" of not doing enough? For example, could we be putting more people back to work with new investments aimed at modernizing our crumbling transportation infrastructure? You bet. Every $1 billion invested in transportation creates or sustains 35,000 jobs. My Republican colleagues know that, or at least they do when a ribbon is placed before them and scissors are put in their hands, yet they refuse to set aside their cut-spending-no-matter-the-cost approach to governing. Want another unintended consequence of that approach? Consider what our unemployment situation might look like if we had not lost 700,000 public sector jobs in the last four years. The most recent 4th Quarter GDP data from the Department of Labor suggests the steady decline in government spending at all levels has been a drag on the economy for the past two years, and it is that contraction that resulted in the GDP's first decline since the spring of 2009.

What my colleagues conveniently fail to mention is that the Federal programs they are most likely to criticize today actually have a measurable benefit to the economy. The director of the nonpartisan Congressional Budget Office has said that increasing the value and duration of unemployment benefits is one of the more effective methods for stimulating the economy. As my colleagues know, unemployment benefits restore only part of a person's lost income and any benefit they receive is quickly put back into the economy to buy things like groceries and gas. Mark Zandi, the former economic adviser to John McCain's presidential campaign, estimates the multiplier effect for every $1 in unemployment benefits to be $1.64 in additional economic activity. In fact, a recent Congressional Research Service report found that unemployment benefits provided during the heart of the recession between 2007 and 2009 actually helped stabilize the GDP, closing 18.3 percent of what otherwise would have been the shortfall.

The same is true for the Supplemental Nutrition Assistance Program, formerly known as food stamps, which generates $1.72 in related economic activity for every $1 in benefits. As the Oversight Committee heard in testimony last year, the SNAP program is efficiently managed. USDA has reduced improper

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payments to a record low of 3.8 percent or $13.2 million. By comparison, the failure to manage oil and gas leases on Federal lands costs $1.8 *billion* a year, according to GAO testimony before the Committee.

So rather than use this hearing as a partisan attack on Federal benefits, I suggest we spend this time looking at actual unintended consequences of things like reducing Postal Service delivery, which is of great concern to the Committee. Eliminating Saturday mail service would result in layoffs for more than 50,000 letter carriers. If we look at the combined public and private mailing industries, they employ 8.4 million workers or 6 percent of all American jobs. For every job in the Postal Service, there are 10 corresponding jobs in the private sector mail industry, and 3 out of 4 of those jobs depend on the Postal Service's current delivery model, including 6-day mail. Last year, the combined industries supported $1.3 trillion in sales revenue or 8.6% of the GDP. So any reduction in USPS delivery surely will have ripple effects across the economy. Upon closer reflection, it seems the Postmaster General's recent proposal to eliminate 6-day delivery would actually lead to more unemployed middle-class workers needing federal assistance to make ends meet. Gee, that sounds like an unintended consequence.

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