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STATEMENT OF WILL RADERMAN

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TESTIMONY FOR THE UNITED STATES HOUSE WAYS AND MEANS COMMITTEE

WORK AND WELFARE SUBCOMMITTEE HEARING ON:

"Reforming Unemployment Insurance to Support American Workers and Businesses."

JUNE 4, 2024

Chairman Smith, Chairman LaHood, Ranking Member Davis, and Members of the Committee, thank you for inviting me here today and for holding a hearing on how to better administer unemployment benefits. My name is Will Raderman, and I'm an employment policy analyst at the Niskanen Center, a non-partisan think tank founded in 2015. We have been privileged to support this committee's work, most recently with the Tax Relief for American Families and Workers Act. Our central economic philosophy is the idea that strong free markets and robust social policies together provide the foundation for a free and fair society.

Unfortunately, programs meant to complement our dynamic labor market and keep families stable following job loss are falling short in key ways. This includes recurring performance and integrity issues with the state unemployment insurance (UI) systems that provide economic security to laid off workers searching for their next role. These weaknesses are, in part, a product of flawed UI administration financing by the federal government.

My testimony will touch on three related points.

1. Federal funding directed to state agencies for UI administration has been eroded by inflation and fluctuates year-to-year, making it difficult to develop strategic long-term plans and investments.
2. Substantial amounts of tax revenue raised specifically for program administration is not ending up in state agency accounts to fund system improvements.
3. Congress should reform the financing process so that state agencies have the resources needed to maintain the highest levels of program integrity and effectiveness.

Early on in the Covid-19 pandemic, it became clear that state unemployment insurance agencies were not equipped to handle the surge of claims. Although the UI agencies received an influx of additional funding to help manage the situation, years' worth of necessary system improvements could not be implemented once the crisis arrived. Many legitimate applicants were forced to wait months before receiving their benefits, while criminals stole up to $135 billion according to Government Accountability Office estimates.[1] Improper payments, of which fraud is one cause, soared tens of billions of dollars higher.[2]

This administrative collapse was due to a culmination of factors.[3] There was inadequate communication between states and under-utilization of available data sharing systems to verify claims.[4] Agencies were under-staffed and often lacked essential in-house technical expertise to make quick adjustments as the situation worsened. Proposed modifications were also held up because of complicated program rules. Finally, relaxed self-certification requirements for one of

[1] U.S. Government Accountability Office, *Unemployment Insurance: Estimated Amount of Fraud During Pandemic Likely Between $100 Bil- lion and $135 Billion*, GAO-23-106696 (Washington, D.C.: September 12, 2023).
[2] Office of Inspector General, *OIG oversight of the Unemployment Insurance program* (Washington, D.C.: U.S. Department of Labor, December 15, 2023).
[3] Statement for the record on "*Investigating Pandemic Fraud : Preventing History from Repeating Itself*", Before the U.S. House Ways & Means Oversight Subcommittee, 118th Congress (2023) (Statement by Matt Darling et al., Niskanen Center).
[4] Angela Hanks, "Encouragement for States to Use the Integrity Data Hub (IDH) available through the Unemployment Insurance (UI) Integrity Center" (Washington D.C.: Training and Employment Notice 24-21, Department of Labor, May 5, 2022).

the major federal emergency unemployment programs left it vulnerable to criminal enterprises.[5]

The magnitude of the fraud was unprecedented. However, these administrative shortcomings were not. For instance, Hurricane Katrina exposed many of the same alarming system gaps that were exploited at a far more costly scale during COVID-19.[6] UI agencies in the affected states were unable to efficiently ramp up their capacity, loosened eligibility rules to get emergency benefits to displaced workers faster, would have benefitted from better data sharing, and had an elevated rate of improper payments.

These sorts of malfunctions will repeat themselves without changes to the general administrative financing process so state agencies can steadily invest in better staffing, systems, and technology.

Unreliable allocations provided to state agencies

Each year, Congress provides state agencies with a base allocation to fund program administration.[7] Additional dollars are only released when the workload exceeds expectations, meaning agencies must plan their years according to the initial funding allotted. But those base allocations are not reliable. Since 2007, the value of the annual base allocations sent out to states has declined by around $900 million dollars when adjusting for inflation, a 27% decline. Every state agency is worse off as a result.[8]

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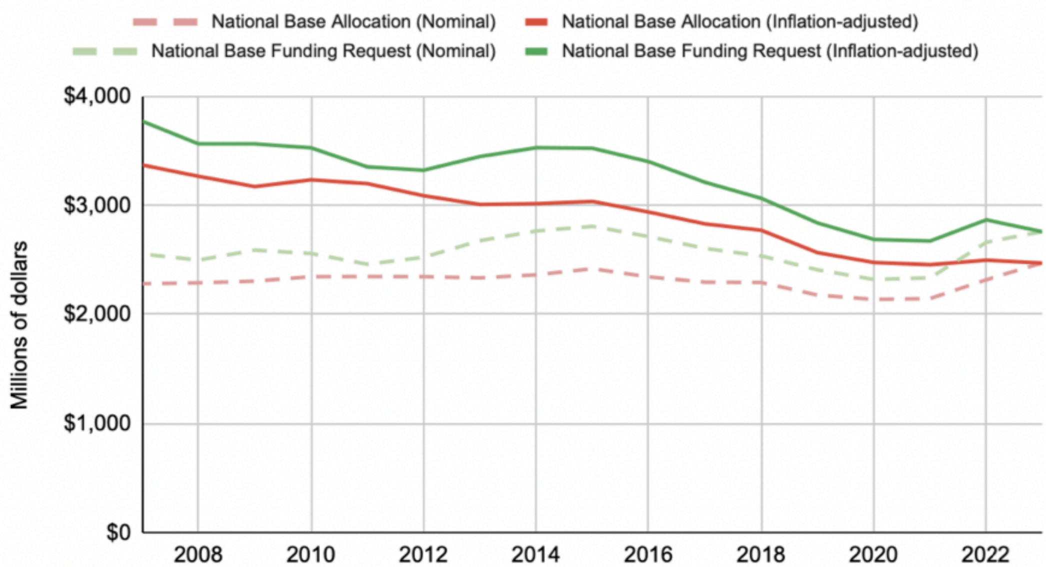
[5] Matt Weidinger and Amy Simon, *Pandemic Unemployment Fraud in Context: Causes, Costs, and Solutions* (Washington, D.C.: American Enterprise Institute, January, 2024).

[6] U.S. Government Accountability Office, *Hurricanes Katrina and Rita: Federal Actions Could Enhance Preparedness of Certain State- Administered Federal Support Programs*, GAO-07-219 (Washington, D.C.: February 7, 2007); Elliot P. Lewis, "Individuals Received Disaster Unemployment Assistance in Both Louisiana and Mississippi" (Washington, D.C.: Management Letter No. 06-06-010-03-315, U.S. Department of Labor Office of Inspector General, September 29, 2006).

[7] Congressional Research Service, *Funding the State Administration of Unemployment Compensation (UC) Benefit* (Washington, D.C.: June 2, 2023).

[8] Will Raderman, *Getting the job done on unemployment insurance: How Congress can reinforce program administration and integrity with finance reform* (Washington, D.C.: Niskanen Center, May, 2024).

Base funding sent out to states for UI administration

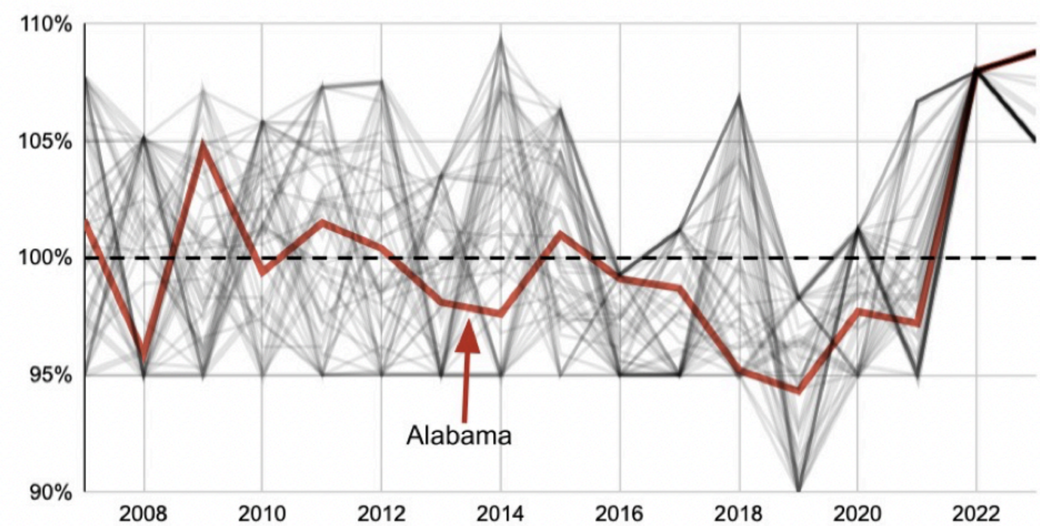


Sources: Department of Labor Unemployment Insurance Program Letters and state allocation data

States' base funding is also quite volatile. Less overall base funding is released during stronger economic cycles when fewer claims are projected. The result is that UI agencies receive fewer total resources when they have the most opportunity to focus on system updates, whether that be adding new verification tools or streamlining internal procedures.

To make matters worse, the approved funding is divided up differently between the agencies each year through a distributional Resource Justification Model (RJM). This formula causes states' allocations to fluctuate over time – making it hard to advance long-term plans with the present resource levels – and tends to shortchange agencies struggling the most to effectively process benefit claims. In particular, the RJM contributes to significant regional disparities that hurt Central and Southern states. Their agencies must administer UI benefits with under $10 per working-age resident while states in other regions of the country typically rely on double-digit rates, with the best-resourced UI agencies receiving over twice as many dollars per working-age resident.

States' base UI administrative funding as a % of prior year base allocation



Author's calculations using Department of Labor data

Recent one-time funds approved by Congress have helped agencies take steps to update their systems, but are not a substitute for steadier annual administrative allocations that support long-term planning. As my colleague, Jen Pahlka, has documented, "big-ticket" purchases have a limited impact when the agencies are not capable of adapting their systems and ensuring the right tools are being added over time.[9] Furthermore, what may reduce fraud and poor performance today could be less effective tomorrow. New Jersey Labor Commissioner Robert Asaro-Angelo made a similar point in testimony before the House Ways and Means Oversight Subcommittee last Fall, saying, "There's no 'silver bullet' to completely eradicate fraud from our benefits systems, but, we can combat it in every way possible" by "continually learning and training so we stay one step ahead."[10] Predictable, consistent investments are required to build up that valuable internal capacity.

[9] Jennifer Pahlka, "Better government tech starts with people. New Jersey shows how.," The Washington Post, June 13, 2023.

[10] *Testimony from New Jersey Labor Commission on Fraud Prevention*, Before the U.S. House Ways & Means Oversight Subcommittee, 118th Congress (2023) (Testimony by Robert Asaro-Angelo, New Jersey Department of Labor Commissioner).

Only a fraction of dollars raised for UI administration are utilized

There is a gap between what is raised for program administration and what is distributed to state agencies. Thanks to inadequate appropriations and complex Trust Fund rules, we are leaving significant amounts of revenue *already* raised for the purpose of UI administration on the sideline.

The Federal Unemployment Tax, known as FUTA, is paid by employers and applied to the first $7,000 of a worker's wages, usually at a 0.6% net rate.[11] This generally translates to $42 in taxes generated per worker, which gets deposited into federal accounts. 80% of the funding raised through FUTA is kept in the Employment Security Administration Account (ESAA) to fund program administration, while 20% is automatically directed to the account that funds the federal portion of Extended Benefits, additional weeks of benefit eligibility activated in times of high unemployment.

Agencies are not given full access to the 80% of FUTA funds intended for program administration due to the congressional appropriations rules. In an average year, there is around a $400 million difference between what is deposited into ESAA for administrative tasks and what is actually sent to agencies.[12] The vast majority of states are only getting back a fraction of dollars raised in their borders specifically for program administration, with Southeast and Central states seeing the worst returns.

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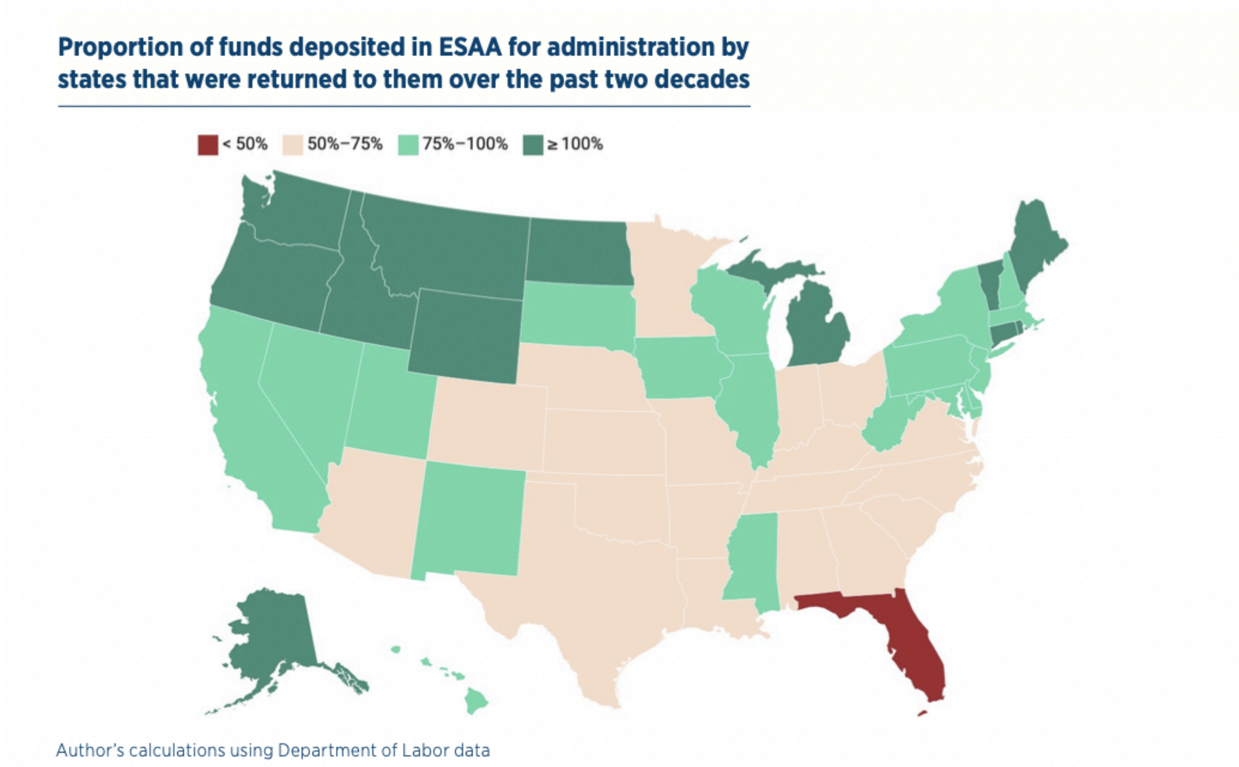
[11] Internal Revenue Service, *FUTA Credit Reduction* (Washington, D.C.: April 3, 2024).

[12] Author's calculations based on three Department of Labor documents covering historical program data from 2006 to 2022. See: U.S. Department of Labor, *Unemployment Insurance Program Outlook, President's Budget*(s).



The spare revenue could be used by state UI agencies to improve their systems, but it is rarely made available for that purpose. Instead, a strict statutory provision frequently causes unused funds in ESAA to be diverted to the Extended Benefits account, even though that account has already received its automatic share of FUTA revenue. When the end-of-year balance for ESAA exceeds 40% of the Congressional appropriations made over the past year, the "excess" funds must be transferred to the account for Extended Benefits.[13]

This requirement cements the existing funding problems established by the appropriations process. In the five fiscal years leading up to the Covid-19 pandemic, over $4.5 billion was transferred out of ESAA due to this balance provision.[14] A better use of those funds would have been to allow state UI agencies to upgrade their institutional capacity over that period, which would have reduced the enormous scale of criminal fraud suffered during the pandemic and allowed more legitimate claimants to quickly access benefits.

[13] Julie M. Whittaker, *Unemployment Compensation (UC) and the Unemployment Trust Fund (UTF): Funding UC Benefits*, (Washington, D.C.: Congressional Research Service, October 28, 2016).
[14] U.S. Treasury, *ESAA Account Statement Reports* (Washington, D.C.: January, 2024).

Ways to reform the financing process

The financing of UI administration warrants a significant overhaul in order to better serve laid-off workers and protect taxpayer dollars. We advise Congress pursue the following reforms:

1. The full 80% of FUTA revenue set aside for program administration should be dedicated to this purpose each year. Importantly, this entails eliminating the ESAA balance limit provision or making it obsolete. Too much funding meant for administrative tasks is currently being diverted away due, in part, to this rule and should be directed back towards UI agencies.
2. Besides making full use of available funding already being raised, those resources should be distributed in a more reliable manner. The Resource Justification Model contributes to the variable state-level allocation amounts and creates unreasonable disparities between states, with harms to agencies most in need of additional resources for cleaning up their systems. Congress should distribute administrative allocations to states with a clearer link to each state's overall working-age population.
3. The above steps would provide critical support to state agencies and make complete, efficient use of existing revenue generated for UI administration. But to prevent further erosion in the inflation-adjusted value of UI administration investments, additional revenue must be generated through indexation of the FUTA taxable wage base. The wage base has not been updated in over forty years, weakening the true value of the annual FUTA funds raised over time as price levels increase.[15] This decline can be halted by indexing FUTA's taxable wage base right now for inflation or adjusting it in accordance with an average wage index as done with Social Security's taxable wage base.[16] Congress can also permanently reverse past erosion by doubling the FUTA wage base now and indexing it.

To conclude, there are serious, chronic issues with how we finance unemployment insurance administration. Under a broken status quo, far too many legitimate UI claimants are

[15] Andrew Stettner, *Increasing the Taxable Wage Base Unlocks the Door to Lasting Unemployment Insurance Reform* (Washington, D.C.: The Century Foundation, July 14, 2021).

[16] Social Security Administration, *Contribution And Benefit Base* (Washington, D.C.: 2024).

under-served, while fraudulent claims go undetected. Financing reforms are necessary to maximize agency performance.

Chairman Smith, Chairman LaHood, Ranking Member Davis, and Members of the Committee, thank you again for the opportunity to testify today. I look forward to hearing your questions.