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WORSENING THE RECESSION: PROPOSALS FOR A FURTHER EXTENSION OF UNEMPLOYMENT BENEFITS

Last Fall, Congress pushed through legislation, reluctantly signed by President Bush, extending unemployment compensation benefits for an additional 13 or 20 weeks, depending on a state's unemployment level (see "Making A Bad Situation Worse: The Ill-Considered Plan To Extend Unemployment Benefits," IRET *Congressional Advisory* No. 1A, September 26, 1991.) Now the President and many members of Congress are prepared to legislate another 13 week benefit extension, for a total extension of 26 or 33 weeks. This extension would be temporary, expiring shortly before the November election. But with timing like that, does anyone doubt that it would then be renewed, with little heed as to cost?

If unemployment benefits were costless, everyone would be in favor of sweetening them. Indeed, if the benefit checks had no costs, the government could (and should) make us all rich by increasing benefits 10 or 20 fold and giving them to everyone, including the employed. In reality, government checks do have costs. As a result, higher benefits — unless financed by cuts in other government spending — tend to have the perverse effect of destroying jobs, throwing more people out of work and increasing the burden on those who manage to retain their jobs. Policy makers should consider these costs, along with their unpleasant consequences, in assessing whether to expand again unemployment compensation benefits.

Because the government does not create wealth, it has to get the resources to pay for a larger unemployment program from somewhere else. In last year's legislation, Congress secured the funds by accelerating individual income tax payments, causing current-year tax collections to be higher and next-year tax collections to be lower. Unfortunately, this change replaced a simple rule regarding estimated tax payments with a complicated, punitive rule that often requires taxpayers to compute their liabilities based on information they will not have until it is too late. The new rule will generate business for accountants and tax lawyers but will raise the cost for many taxpayers participating in the types of activities whose yearly income is most difficult to estimate: productivity-enhancing investments with great potential but uncertain returns. In short, the change was a model of bad taxation that contravenes the goals of making the tax system simpler, fairer, and less of a drag on employment and production.

This year's proposal, in its current form, would eschew a tax hike in favor of declaring an emergency and just spending the money. Since the government doesn't have the money, that means deficit financing: borrowing more from the public and going deeper into debt. Although deficit financing is less damaging than a complicated, hidden, or anti-investment tax increase, a further rise in a federal deficit, already estimated to top $350 billion, carries dangers of its own. Not the least of these hazards is that financing the additional benefits by borrowing makes them appear to be costless.

The only sound way to pay for more unemployment compensation benefits is to cut other government spending. That way the amount that the government takes from the productive private sector would not continue to climb as sharply as in recent years. Surely, in a federal budget approaching $1.5

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trillion and one-quarter of national output, a few wasteful or ineffective government programs can be identified and cut — if Congress is serious about controlling the amount it spends out of taxpayers' wallets.

If policy makers really believe that additional assistance to the long-term unemployed is appropriate, the best targeted spending reform would occur right within the unemployment compensation program. Robert Topel of the University of Chicago has pointed out that people currently qualify for benefits almost as soon as they lose their jobs. If the waiting period were lengthened by a week or two, there would be large savings in terms of benefits and administrative costs for the very-short-term unemployed. This makes sense because unemployment usually does not bite hard financially until people have been out of work for a few weeks. A slight delay in benefit eligibility would also have the salutary effect of encouraging people to take more responsibility for their own welfare by saving more.

A different concern with respect to prolonged unemployment benefits is that it tends to prolong the duration of unemployment. Studies have found that the long-term unemployed are much more successful at finding work shortly after their benefits have expired than they were before, presumably because they intensify their job search efforts following the removal of a government check that pays them for <u>not</u> finding work.

An important question that has been entirely overlooked in this debate is whether government provision of what is essentially a type of insurance should be curtailed, not increased. When nations around the world and states and localities in this country have discovered that private firms can often provide less costly, higher quality services than can governments, should the federal government be expanding its role as an insurance supplier? A better approach might be to think about privatizing unemployment insurance. The rates set by private insurers would furnish employers and employees with objective information regarding the risks of unemployment in different businesses and industries. Private insurance would also give those in the job market the freedom to accept or reject unemployment compensation insurance as a part of their pay package, depending on whether they thought the insurance was sufficiently valuable to justify foregoing other kinds of compensation.

An additional extension of unemployment benefits, such as is being proposed in Congress, threatens to boost unemployment, slow growth, and increase people's dependence on government handouts instead of gainful employment. To minimize these costs, any extension of benefits should be financed through government spending cuts. An excellent reform, which could pay for lengthened benefits but should be adopted in any case, is to increase the initial waiting period. The best route for policy makers to follow in relieving the suffering of joblessness, though, is to remove government-imposed tax and regulatory barriers to productivity improvements and job creation. The American people would much prefer jobs to government assistance checks.

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Note: Nothing written here is to be construed as necessarily reflecting the views of IRET or as an attempt to aid or hinder the passage of any bill before Congress.