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**CONGRESSIONAL TESTIMONY ON THE
EFFECTIVENESS OF THE EMPLOYMENT SERVICE IN AIDING UI CLAIMANTS**

(Before the House Committee on Ways and Means, Human Resources Subcommittee)

Upjohn Institute Staff Working Paper 91-08

28 February 1991

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Summary

This testimony describes the results of a study of the Employment Service (ES) conducted by Dr. Jacobson and Prof. Arnold Katz of the University of Pittsburgh using data on over 100,000 individuals who registered with the Pennsylvania ES between 1978 and 1987, and an even larger sample of non-registrants.

One major finding is that much of the decline in the ES's performance over the past thirty years can be explained by changes in: funding, characteristics of registrants, and characteristics of job vacancies. Thus, we concluded that criticism of the ES often ignores changes in crucial factors outside of the ES's control that reduced its effectiveness.

A second major finding is that most criticism of the ES is based on the inappropriate assumption that the primary goal of the ES should be to maximize placements. The proper measure of ES benefits is how well it reduces joblessness, increases earnings, and reduces UI and welfare payments.

We found that the ES reduced the average duration of unemployment of long-term UI claimants by nine weeks. This was for UI claimants who were unemployed for at least 30 weeks. But the ES reduced joblessness of claimants unemployed for 12 weeks by less than two weeks.

This is evidence that the ES is most effective in aiding claimants who had substantial trouble finding work on their own. But we suspect that the jobs found with the help of the ES do not compare favorably with jobs held prior to becoming unemployed. Thus, we believe the ES primarily acts as a backstop preventing large earnings losses.

Finally, although savings in UI benefits and increases in earnings created by the ES may be modest, the cost of ES service is so low, \$75 on average, that modest benefits would more than offset those costs.

We believe our results, coupled with similar findings from related studies, is sufficiently strong to warrant increasing the funding of the ES. That measure is favored because it would be at least budget neutral. In contrast, other measures to assist the long-term unemployed, such as providing extended UI benefits or training, would not come close to being budget neutral. In addition, \$1 spent on job search assistance is likely to be more effective in helping claimants than \$1 spent on training.

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I am honored to have this opportunity to discuss my research on the Employment Service (ES) with you today. And am equally pleased that the committee is interested in a broad assessment of the ability of job search assistance to aid unemployment insurance claimants.

The research that Arnold Katz of the University of Pittsburgh and I conducted used administrative data routinely produced by the Pennsylvania UI and ES systems to examine the effectiveness of the ES in Pennsylvania. We assembled detailed histories of the work, unemployment, and ES usage of over 100,000 individuals who registered with the ES between 1978 and 1987, and compared their histories to those of an even larger sample of non-registrants.

We chose Pennsylvania for several reasons. First, it is one of only two states with data covering a full business cycle. Second, it has an unusual, diverse economy. The western third resembles the rust-belt of the industrial heartland, while the eastern section resembles prosperous areas along the North Atlantic seaboard. But most important, it is the only state where use of the ES is voluntary for UI claimants. This key fact provides unique information about the optimal timing of ES usage.

Importantly, our results are consistent with Terry Johnson's 1981 study which examined the ES in 29 states, and the results of demonstration projects in a number of states including Texas, South Carolina, Washington, and New Jersey, which examined the effectiveness of programs providing job search assistance to UI claimants.

Recently, we have heard a great deal about the fog of war. I have found, however, that a fog of misunderstanding surrounds many public policy issues, including how well the ES fulfills its mission. What was clear when we began our study was that the ES is unpopular "inside the beltway". For example, last year Secretary of Labor Dole expressed concern about the effectiveness of the ES in a letter to state administrators. She cited, among other criticisms, "declines in the percent of all hires placed by the ES from 20 percent in 1962 to 7 percent today". But what was lost in a thick haze was whether or not the criticism leveled at the ES was valid.

One major element of our study assessed the accuracy of the widespread negative views by placing ES performance into an appropriate context. We found much of the decline in performance can be explained by changes in: funding, characteristics of registrants, and characteristics of job vacancies.

Perhaps most important, we found that ES funding levels fell dramatically. These cuts were particularly sharp in the early 1980's. Between 1979 and 1986 Pennsylvania registrations increased by 15 percent, but total funding, in inflation adjusted dollars, decreased by 10 percent.

We also found that 25 percent of ES registrations were mandatory under the WIN program. WIN is a program for AFDC recipients with school-age children, a program that began five years after 1962. As you might guess, WIN participants are about twice as difficult to place as other registrants.

In addition, we found that the ES is most effective in placing low-skilled workers. The fraction of jobs held by workers with high-school education or less has declined substantially since 1962.

In short, we concluded that criticism of the ES often ignored changes in crucial factors outside of the ES's control that reduced its effectiveness. Ignoring those factors is much like George Steinbrenner placing all the blame for the decline of the New York Yankees on his managers.

But of even greater importance, we found that the criteria used to judge the ES were inappropriate. Most criticism is based on the assumption that the primary goal of the ES should be to maximize the number of placements. The proper measure of ES effectiveness, however, is how well it reduces joblessness, increases earnings, and reduces UI and welfare payments.

The second major element of our study examined how well the ES gets UI claimants with over three years of work experience back to work. Unadjusted figures showed that UI claimants who used the ES took considerably longer to find work than non-users. Those results reflect the fact that the most effective means of finding work are through tips from friends and relatives, direct applications at work sites, answering want ads, and using private agencies. Such comparisons tell us little about the ES's effectiveness, however, because jobless workers typically turn to the ES only after use of other methods have failed.

Key evidence that ES use is triggered by the failure to find work by other means is that more than half of the claimants who used the ES delayed use until all, or almost all, of their UI benefits were exhausted. In contrast, two-thirds of the non-users returned to work before coming close to exhausting benefits.

To control for factors which influence the return to work, including access to various job search methods, we used an estimating technique that compared ES-users to non-users with similar demographic and work history characteristics. Most important, we determined the delay in ES use--how long the users were unemployed at the point they first looked for a job at the ES. We then compared the subsequent duration of unemployment of the users to non-users whose prior spells of unemployment were equal to that of the users. For example, UI claimants who registered with the ES in their thirtieth week of unemployment were compared to otherwise

similar UI claimants who also were unemployed for 29 weeks, but did not register with the ES in the thirtieth week.

That comparison showed that UI claimants who delayed use of the ES by roughly 30 weeks returned to work 9 weeks sooner than they would have had they not used the ES. In contrast, we found that UI claimants who delayed ES-use for roughly 12 weeks had at most a two-week reduction in unemployment.

The shift from a 2 to 9 week reduction in unemployment as the delay in ES-use lengthened suggests that the ES is particularly effective in aiding a relatively small segment of claimants who have trouble finding work on their own.

Additional evidence bearing on ES effectiveness is the percentage of claimants who use the ES. If the ES provides a valuable service, we would expect a high percentage of claimants to use it. About 55 percent of the claimants exhausting UI benefits used the ES, compared to only 13 percent of those who did not exhaust benefits. This reinforces the view that the ES is most effective in dealing with those having trouble finding work.

A potential problem with the analysis I have just discussed is that use of the ES may not have caused all the reduction in joblessness. Instead, some claimants may have begun to use the ES and other job finding methods intensively as they came close to exhausting benefits, but use of the other methods may have contributed to the speedier reemployment.

To rule out this possibility we examined how the quality of the services provided by the ES influenced the duration of joblessness. All the ES-users in our sample searched the ES's lists of job openings to find work. Half of the users could not find a job opening to which they wanted to be referred. One-third of the users were referred to jobs, but that referral did not lead to being hired. One-sixth of ES-users were placed at the jobs to which the ES referred them.

If the ES caused the reduction in joblessness, we would expect the reduction in joblessness would be large for those placed, moderate for those referred but not placed, and small for those who could not even find an opening worth pursuing.

Our analysis was much in keeping with these expectations. Among claimants who delayed use of the ES by about 30 weeks, the duration of unemployment was reduced by 18 weeks among those placed by the ES, 12 weeks among those referred but not placed, and 2 weeks among those who could not find a job listing to which they were willing to apply.

This is powerful evidence that the ES was responsible for the reductions in unemployment. But you may still be skeptical that the ES contributed to reducing the joblessness of users who were not directly placed. A plausible explanation for the positive effects is that the ES provided information which led to the adoption of more realistic expectations about job vacancies. For example, after seeing that the ES had no listings of interest, some claimants quickly took jobs

they knew were available, but had been hesitant to accept because they thought they could do better.

To summarize the key findings about ES effectiveness, we believe that the ES reduced the average duration of joblessness by about 9 weeks for more than half of UI claimants who were unemployed for 30 weeks, and therefore, clearly had substantial trouble finding work using other job search methods.

Further, our evidence that most ES users accept jobs after exhausting UI benefits suggests that jobs obtained through the ES are much preferable to remaining jobless, but do not compare favorably with jobs held prior to becoming unemployed. Thus, we believe the ES primarily acts as a backstop preventing large earnings losses.

A final issue of great importance is assessing how the benefits of ES use compare to the costs. We are still working on that part of our analysis. Thus, we can not provide figures on the savings in UI payments and gains in earnings, but we suspect those benefits are modest. On the other hand, only modest benefits are needed to offset ES costs.

On average the ES spends only \$75 per registrant, and the average weekly UI benefit payment for claimants using the ES was \$170. Thus, a reduction in 2 days of UI compensation per ES-user would nearly offset the cost of the ES services.

Alternatively, if we conservatively assume 15 percent of earnings are paid in federal taxes, the ES would have to increase annual earnings by only \$500 on average to pay for the ES services. If the pay of post-unemployment jobs held by the users was half the pay of their pre-unemployment jobs, average weekly earnings would be \$200. Thus, a modest increase in employment of two and a half weeks would be sufficient to pay for the cost of ES services.

The bottom line question facing the committee is whether these results are sufficiently strong to act upon, and if so what actions should be taken.

My view is that these results are strong--the sample is unusually large, the data are accurate, the analysis uses the best available estimation techniques, and Pennsylvania is a sufficiently diverse state to suggest the results would hold elsewhere. Moreover, the results are consistent with those from the only other similar analysis of the ES. And studies examining the value of providing job search assistance to UI claimants also generally show positive results.

A major factor favoring increasing ES funding is that there is a strong chance that such expenditures would return more than their costs to the Federal treasury in terms of reduced UI payments and increased taxes. Alternatives to aid the long-term unemployed, such as extending UI benefits, or increasing training, would certainly not be budget neutral.

Further, the triad of job search assistance, training, and transfer payments appears to be out of balance. The US-DOL has steadily favored training at the expense of job search

assistance, despite consistent evidence that training is no more productive for the long-term unemployed than job search assistance, but much more expensive.

Although both JTPA and EDWAA have job search assistance components, and the ES receives contracts to provide those services in many states, the ES has been starved for funds. A testimony to the perceived value of the ES "outside the beltway" is that states have used their own funds to partially offset Federal cuts. Despite state actions, Federal cuts led to the virtual elimination of promising counseling and job development efforts, as well as delays in purchasing cost-saving automation systems.

The DOL's negative attitude towards the ES is difficult to understand, given that through the ES the DOL runs the only public institution providing job search assistance for all workers. It would make much more sense for the DOL to down grade training since public schools, community and four-year colleges, and many other public institutions provide vocational training.

In short, given the strong, consistent evidence that the ES is effective in aiding the unemployed, the DOL's attempts to cut the ES budget makes about as much sense as the U.S. Navy recommending giving a large fraction of the money spent on nuclear submarines to the Air Force to maintain the other two components of the nuclear triad--manned bombers and land-based missiles.

I hope this testimony has dispelled some of the fog surrounding the ability of the ES to fulfill its mission. I very deeply appreciate having this opportunity to discuss with you the research that Arnold Katz and I have done.

Appendix A. The Organization, Funding, and Mission of the ES.

The Employment Service and Unemployment Insurance System were created in 1933 by the Wagner-Peyser Act. Both are federally mandated programs that leave to the states wide discretion in organizing both agencies. Technically the UI and ES are separate entities. However, states usually have a single State Employment Security Agency, cross-train personnel, and locate offices in the same buildings.

The UI and ES also share the same funding source--the FUTA payroll tax. UI and ES administrative costs are formula funded out of a small fraction of the total tax. About \$800 million of that tax is spent on the ES.

The primary mission of the ES is to provide a public labor exchange where all employers can list openings and all job seekers can come to find suitable matches. In practice the ES tends to occupy the niche of providing services to workers with problems finding work, and best serves employers hiring those workers.

The original focus was helping workers unemployed during the Great Depression. During World War II the ES funneled workers to defense industries, and at the end of the war assisted veterans to find civilian jobs. The ES's special mission with vets has persisted. Today about 15 percent of the ES staff is dedicated to aiding veterans and paid from a separate federal fund.

The ES also has been given special responsibility to assist welfare recipients, other economically disadvantaged persons, and the long-term unemployed. The ES sometimes receives contracts to place JTPA, EDWAA, and JOBS participants, but the ES receives no special funding for assisting most economically disadvantaged persons.

Usually UI claimants must register with the ES. But the ES offers both a carrot and a stick for such registrants. If the ES finds a suitable job opening for a UI claimant, that person is obliged to interview for that job. Failure to do so is reported to the UI system and can lead to a particularly severe penalty--loss of benefit entitlement until the claimant returns to work for four to six weeks.

The ES also provides labor market information. The collection of basic information about employment and earnings has been organized and separately funded as cooperative program between the Bureau of Labor Statistics in the US-DOL and the state ES's.

Finally, the ES provides counseling and testing. It sometimes does job development--seeking vacancies that fit the skills of registrants. ES funding cuts during the 1980's, however, reduced these activities almost to the vanishing point.