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Assisting Dislocated Workers: Dimensions, Needs and Tax Policy Options

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ASSISTING DISLOCATED WORKERS: DIMENSIONS, NEEDS AND TAX POLICY OPTIONS

by

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INTRODUCTION

POLICY MAKERS MUST be cognizant of the difference between a personal trouble and an issue.[1] A personal trouble occurs within the character of an individual. Because a trouble is a private matter, the statement and resolution of a trouble lies within the individual and his immediate milieu. On the other hand, an issue transcends an individual's local environment. An issue is a public matter, involving a crisis of institutional arrangements. The magnitude of the plight of dislocated workers, now and in the future, constitutes an issue, not a personal trouble.

When one person is unemployed in a city of 100,000, that is his personal trouble. When the United States economy is undergoing a profound transformation, the resulting displacement of workers rises to the level of an issue. New technologies, including improved automation techniques, and the growth of foreign competition have increased worker dislocation. The solution to this issue cannot and will not be found within the range of opportunities available to any individual. A need exists for a massive retraining effort to provide the skills necessary to meet changing demands of the job market.

The involvement of the federal government in retraining of dislocated workers raises the specter of rigidity, bureaucracy, paternalism, and cost. After examining the dimensions of the dislocated worker problem and the need for governmental involvement, this article examines the use of tax policy to enable workers to bridge the gap between old and new jobs and to thrive in an economy in transition. The policy making challenge can be succinctly stated: is it possible to use the federal income tax system to the advantage of society by creating tax incentives for a retraining program based on individual choice and limited government involvement?

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[1]C.W. MILLS, THE SOCIOLOGICAL IMAGINATION 8-9 (1959).

I. DIMENSIONS OF THE STRUCTURAL UNEMPLOYMENT PROBLEM

A. *The Components of Unemployment*

Official United States unemployment figures, which have exceeded seven percent for the last decade with limited exceptions, mask different components of the unemployment problem.[2] Not all individuals who desire work are included in the official statistics. Furthermore, the unemployed who are counted lack work because of different causal factors. Many Americans have given up looking for work. These "discouraged workers" are not included in the unemployment statistics. In 1982-83, for example, when the number of unemployed exceeded 10 million, the number of people who wanted jobs but were too discouraged to look for them rose to the range of 1.6 to 1.8 million.[3] According to one observer, about 14 percent of the unemployed by the end of 1982 had either been unemployed for 49 weeks or were discouraged and had given up hope of finding a job after experiencing various periods of unemployment during the prior year.[4]

Further complicating the interpretation of unemployment statistics for policy making are the underlying causes. It is imperative to distinguish between the cyclical and structural components of unemployment.

Cyclical unemployment results from the fluctuations of the economic system. Macroeconomic factors, such as recession and high interest rates, create cyclical unemployment. By neutralizing these macroeconomic factors, the

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[2] Civilian Unemployment Rates in the United States (percentages)

Year	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1975	8.3	8.9	8.4	8.4
1976	7.7	7.6	7.7	7.7
1977	7.5	7.2	6.9	6.6
1978	6.2	6.0	6.0	5.8
1979	5.9	5.8	5.7	5.7
1980	6.3	7.3	7.6	7.5
1981	7.4	7.4	7.4	8.3
1982	8.8	9.5	9.9	10.6
1983	10.4	10.1	9.3	8.5
1984	7.9	7.5	7.4	7.2
1985	7.3	7.3		

EMPLOYMENT & EARNINGS, UNITED STATES DEPARTMENT OF LABOR, BUREAU OF LABOR STATISTICS, Table A-41 (Employment status of the noninstitutional population by sex, age, and color, seasonally adjusted) (January 1976), Table A-44 (Employment status of the noninstitutional population by sex, age, and race, seasonally adjusted) (January 1979), Table A-44 (Employment status of the noninstitutional population by sex, age, and race, seasonally adjusted) (January 1982), Table A-43 (Employment status of the civilian noninstitutional population by sex and age, seasonally adjusted) (January 1985), Table A-43 (Employment status of the civilian noninstitutional population by sex and age, seasonally adjusted) (July 1985).

[3] Flaim, *Discouraged Workers: How Strong Are Their Links To the Job Market,* 107 MONTHLY LAB. REV. 8 (1984). Some estimate that as many Americans have given up looking for work as are unemployed. *See, e.g.,* Clark & Summers, *Unemployment Reconsidered,* 58 HARV. BUS. REV. 171, 173 (1980) (Exhibit I Characteristics of Unemployment in April 1979).

[4] McLennan, Vice President and Director of Industrial Relations, Committee for Economic Development; *Unemployment and Its Underlying Causes, Hearings before Committee on Education and Labor, House of Representatives,* 98th Cong., 1st Sess. 443, 447 (1983).

cyclically unemployed will return to work in jobs and industries from which they were temporarily displaced or to similar ones. A sustained economic recovery comprises the most effective remedy for cyclical unemployment.

Many economists estimate that even in a buoyant economy, characterized by strong economic growth, unemployment will remain at the 6 or 7 percent level. In 1983, the Council of Economic Advisors indicated that a 6 to 7 percent level probably represents the "inflation-threshold unemployment rate," the rate below which macroeconomic policies designed to reduce cyclical unemployment would result in an increase in the rate of inflation.[5] In other words, the acceleration of economic growth as a means of reducing cyclical unemployment runs into the continuing specter of renewed inflation.

Structural changes, which currently characterize the American economy, include the shift away from manufacturing industries toward the service sector and the computer information industry.[6] Traditional manufacturing industries are collapsing or relocating outside the United States leaving holes in our industrialized economy. Other structural forces affecting unemployment include changing international trade patterns, shifting consumer preferences, and a failure of workers' skills to meet the needs of employers.

Structural unemployment connotes the joblessness that results from a fundamental mismatch between skills, experience, job readiness, and location of workers on the one hand; and the skill requirements, qualities, and locations of job vacancies on the other hand.[7] Structural unemployment results not only in the inability of displaced workers to find new jobs in their former industries or occupations but also their inability to find comparably paying jobs. In short, the structure of the labor market is shifting. Many skilled workers are becoming stranded while some employers, having vacant positions for employees with training in the new technologies, scramble to meet their staffing requirements.

Dispute exists over how much any one factor has contributed to structural unemployment in the United States. Two factors in particular are singled out: increased imports of foreign goods into the United States and the impact of technology, particularly that growing from utilization of robotics, computer assisted operations, and chemical discoveries. Trade related structural unemployment results from the United States economy experiencing the intensification of international trade pressures, including mounting rivalries, increased dumping, and trade imbalances between nations.[8] Observers are quick

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[5]Economic Report of the President Transmitted to the Congress February 1983 at 37.

[6]*See generally* A. TOFFLER, THE THIRD WAVE ch. 12 (1980); P. HAWKEN, THE NEXT ECONOMY (1983); R. SHELP, BEYOND INDUSTRIALIZATION: ASCENDANCY OF THE GLOBAL ECONOMY (1981).

[7]Sheingold, *Helping Dislocated Workers,* 7 J. CONTEMP. STUD. 27, 28 (1984). *See also* Samuelson, *The Old Labor Force and the New Job Market,* 15 NAT'L J. 426 (1983).

[8]*See generally* Minard, *Noah's Ark, Anyone?* FORBES 76 (August 12, 1985).

to point to the adverse unemployment impact of the mounting level of foreign imports. For example, the textile/apparel industry in the United States lost approximately 300,000 jobs between 1969 and 1982 due to foreign competition.[9]

The widely discussed impact of technology on employment remains controversial. While the introduction of new technology may have a positive effect on aggregate level employment, it may have dramatically negative effects on specific skill groups. On an industry wide level, one study shows a net growth in employment in several United States industries: namely, steel, automobile, aluminum, coal and iron ore production, over a twenty-year period as a result of technological change.[10] In the industries studied, new technology led to lower prices, increased quantity of outputs, and employment gains that counterbalanced much of the labor-reducing characteristics of the technological changes introduced in the industries examined during the survey period.

However, traditional occupations in these industries are being eliminated and replaced by computer operators and machine tenders. As the new technologies demand different skills, different individuals are often hired. Rarely do employers retrain the original workers. Attrition, encouraged by early retirement and other union negotiated benefits, is most often the strategy applied to eliminate former smelters, welders, and other occupations replaced by new technology.

It is difficult to arrive at valid conclusions regarding the long-run employment effects from the new technologies due to the lack of data specifically identifying the number of jobs eliminated, changed, created or increased (or to be eliminated, changed, created, or increased).[11] In addition, sufficient research has not been undertaken to demonstrate the possible multiple effects of automation in multi-industry or multi-occupation situations. For instance, poten-

[9]NATIONAL ACADEMY OF ENGINEERING AND NATIONAL RESEARCH COUNCIL, THE COMPETITIVE STATUS OF THE U.S. FIBERS, TEXTILES, AND APPAREL COMPLEX 37 (1983). One econometric model estimates that by 1990 imports may cut United States textile/apparel employment in half to 915,000. Bus. Wk. *Textile Imports Are Swamping Even the Best Companies*, 50 (September 16, 1985).

[10]LEVY, BOWERS, & JONDROW, *Technical Change and Employment in Five Industries: Steel, Autos, Aluminum, Coal and Iron Ore*, PUB. RESEARCH INST. 21 (June 1983).

[11]For example, the United States Department of Labor Bureau of Labor Statistic (BLS) concluded that automation will cause growth in jobs from 1980 to 1990 in almost as many different occupations as it will cause job loss. The BLS concludes: "Despite widespread technological advances, . . . employment should continue to increase in most industries and occupations during the 1980's and early 1990's. U.S. DEPARTMENT OF LABOR, BUREAU OF LABOR STATISTICS, OCCUPATIONAL OUTLOOK HANDBOOK 15 (1984-85 ed. April 1984). Unemployed workers whose skills are not in demand should be able to find jobs because employment growth is projected for most occupations associated with dislocated workers. While tasks performed by lesser-skilled manufacturing workers are considered by the BLS to be susceptible to future encroachment by robots and other technologies, the BLS does not anticipate that technological change will result in any significant occupational impact outside of a few industries (e.g., autos and printing) until such time as the technology improves and its cost is reduced. Legrande, *Economic Growth and Changing Labor Markets: Those Left Behind: Dislocated Workers: An Analysis*, CONG. RESEARCH SERV., Report No. 83-220E at 16 (1983); Silvestri, Lukasiewicz, & Einstein, *Occupational Employment Projections Through 1995*, 106 MONTHLY LAB. REV. 37 (November 1983). *See generally* G. SCHWARTZ & W. NEIKIRK, *The Work Revolution* 92-99 (1984); W. LEONTIEF & F. DUCHIN, THE IMPACTS OF AUTOMATION ON EMPLOYMENT 1963-2000 (April 1984).

tial research may reveal that an application reduces employment in one industry or occupation but increases employment in other industries or occupations.

B. *The Displaced Worker: Magnitude of Structural Unemployment Dilemma*

A precise analysis of the magnitude of the structural unemployment dilemma is impossible because of the wide disparity in estimates of the number of dislocated workers. This reflects disagreement among labor market analysts about how many of those who have lost their jobs in the last several years should be labeled dislocated workers. However, a general definition and characteristics of the dislocated worker emerges from the mass of statistical data.

Many would accept a definition of the dislocated worker group as including individuals who: 1) are experienced members of the labor force with steady work histories; 2) were previously employed in a declining industry or occupation, for example, those in which employment dropped for several years; 3) have little likelihood of finding new jobs in their former industries or occupations; and 4) who live in an economically depressed or declining geographic region, for example, one that has lost population or has had an above average unemployment rate.[12]

Characteristics commonly associated with a dislocated worker include a middle-aged male who has been employed in a durable goods manufacturing industry (for example, motor vehicles or steel), by one firm, and for most of his working life. Most workers displaced by economic change come from manufacturing industries, although not solely from the durable goods sector. They were formerly employed in occupations typical of manufacturing industries, with the majority concentrated in low-skilled operative and laborer jobs. Most often, the Northeast or the Midwest is their home. A substantial proportion, but not all, are high school graduates. Men outnumber women, and whites outnumber minorities in most areas. Compared with other groups experiencing unemployment, dislocated workers are somewhat older, usually age 40 or more. As full-time, full-year employees, they have enjoyed a relatively high income, many with incomes of $15,000 or more belonging to families with additional wage earners. They fall in the upper half of the income distribution of American families.[13]

Dislocated workers tend to have shown a strong desire to work, generally have little previous experience with unemployment, and often expect to be recalled by their same employer to their previous jobs following a period of tem-

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[12]Bendick, Jr. & Devine, *Workers Dislocated by Economic Change: Do They Need Federal Employment and Training Assistance?*, NATIONAL COMMISSION ON EMPLOYMENT POLICY, SEVENTH ANNUAL REPORT: THE FEDERAL INTEREST IN EMPLOYMENT AND TRAINING 184-215 (1981) (Appendix B); Legrande, *supra* note 11, 12-13.

[13]*See generally* Flaim & Sehgal, *Displaced Workers of 1979-1983: How Well Have They Fared?* 108 MONTHLY LAB. REV. 3, 6-7 (1985); B. BLUESTONE & B. HARRISON, THE DEINDUSTRIALIZATION OF AMERICA 49-81 (1982).

porary idleness. The characteristics and expectations evidenced by dislocated workers encounter a cruel reality: the skills they possess do not match those currently, and for the foreseeable future, demanded by local employers.

While a determination of the number of dislocated workers is critical to policy making, a disparity of opinion exists regarding the magnitude of the problem. The number of unemployed who are actually displaced depends largely on the time period in question as well as the economic assumptions, expectations about future employment growth in manufacturing industries, and the definition of dislocated worker used. Based on these variables, the number of dislocated workers in the United States in the 1980's ranges from as few as 100,000 to as many as two million.

The Congressional Budget Office found a wide range of estimates depending on definitional criteria utilized.[14] At the lower extreme, if only workers who lost jobs in declining industries or occupations and remain unemployed for more than twenty-six weeks are counted, the number of dislocated workers in early 1983 was estimated at 100,000 to 150,000 (about 1 percent of all unemployed persons).[15] Blue-collar workers in the Midwest and Northeast constituted a majority of these dislocated workers. If all unemployed workers in declining areas are considered dislocated, the number would have risen to 2.2 million (about 20 percent of all unemployed) in early 1983.[16] By including workers who, whether because of youth or other factors, will probably not face serious reemployment problems similar to those of typical dislocated workers, the higher estimates of dislocated workers are likely excessive.

In order to obtain an accurate picture of the magnitude of the structural unemployment problem, a generally agreed upon, uniform and precise definition of a dislocated worker must be used. Making the definition of a dislocated worker uniform and more precise turns on narrowing the categories of workers included in the definition.

One study separated job loss due to structural change into two categories. The first category represented job loss primarily due to a declining industry, while the second represented job loss due to a declining occupation which is made obsolete by technology even within healthy industries.[17] To avoid significant impact of cyclical factors, the study removed from the data base unemployed workers believed to be on temporary layoff. Only individuals with more

[14]CONGRESSIONAL BUDGET OFFICE, DISLOCATED WORKERS: ISSUES AND FEDERAL OPTIONS 21 (July 1982).

[15]*Id. See also* Bendick, Jr. & Define, *supra* note 12, at 196. Although the Bendick and Devine study has received much attention, the estimate of 100,000 may be inaccurate for several reasons. First, the 1980 data used did not take into account the effect of the 1981-82 recession. Second, the estimate implied that most manufacturing sector employees would return to their former jobs or others in that same sector. However, many industries are unlikely to return to their pre-1980 employment levels. Third, the criterion used to reach the estimate was too restrictive to account for all unemployed who might be considered dislocated workers. Sheingold, *supra* note 7, 27, 34.

[16]CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 21.

[17]Sheingold, *supra* note 7, 27, 34.

than twenty-six weeks of unemployment were included in the dislocated worker category. Twenty-six weeks represents the time by which most workers exhaust their regular state unemployment insurance benefits. Based on this methodology, the study concluded: "[t]he number of workers whose jobs have been permanently lost due to structural change appears to be between 1.1 and 2.0 million. In contrast, the number of dislocated workers — those who will also experience substantial trouble in gaining productive reemployment — falls between 435,000 and 815,000, or roughly 5 to 10 percent of the total unemployed."[18]

C. *Conclusion*

One key point stands out from this analysis of the structural transition of the American economy and the magnitude of the dislocated worker problem. Those who obtain the jobs that trade and new technologies create are rarely the same people who lose their jobs as result of the adverse impacts of technology or trade. Many who are displaced by structural change, whether from technological advances, foreign competition, or other reasons, cannot expect to return to their jobs after an economic upturn. They must be retrained. The need for retraining exists now and in the immediate future. The nation cannot afford to ignore the issue. Some policy decisions are necessary. Although action may be taken on the state or regional level, this article next considers the rationale and policy options available for a national strategy to retrain dislocated workers.

II. RATIONALE FOR GOVERNMENT INVOLVEMENT

A. *The Rationale Explained*

Why must the government provide skills retraining for displaced workers? Four possible entities are involved in employment relations: management, labor unions, individual workers, and government. The motivation of each to participate in retraining is next discussed. In this era of public sector disengagement and greater private sector initiative, the government remains the body that is ultimately responsible for dislocated workers, particularly for their retraining.

Management's motivation first and foremost is making as much profit as possible for the corporation's shareholders.[19] One management technique to

[18] *Id.* The Congressional Budget Office also generated statistics based on defining dislocated workers according to a specific cause of unemployment, either plant shutdown or mass layoff. Data on the extent of unemployment due to plant closings and mass layoff was unavailable when the estimates were projected. However, if all workers who were on indefinite layoff or who lost their job from a plant in a declining industry were considered as being involved in a mass layoff or plant closing, the number of dislocated workers would be approximately 760,000 (about 7 percent of total unemployed) in early 1983. CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 40-41.

[19] M. FREIDMAN, CAPITALISM & FREEDOM 133-34 (1962). The classic judicial formulation is found in Dodge v. Ford Motor Co., 204 Mich. 459, 170 N.W. 668 (1919).

achieve competitive parity (or superiority) turns on continually upgrading production and office technology. Such new technologies are often designed with the specific purpose of reducing labor costs by not only eliminating large numbers of workers, but reducing dependence on more skilled, and, therefore, higher paid employees.[20] Executives justify substantial capital investments in new plants and equipment with the savings in human compensation. With this in mind, little or no incentive exists for management to undertake employee retraining.

Traditionally, corporations have not invested in transferrable skills training below middle management levels. Most training at the production worker level has been equipment or firm specific. With increased expenditures for modernized facilities, comes the accompanying incentive to reduce past employment levels. Beyond retraining a limited number of workers to maintain the new equipment and perhaps for other available jobs in the company, management has no incentive to invest in retraining their soon to be former employees. If firms are responsible for supporting "excess" workers, they will pass their costs on to consumers in the form of higher prices thereby rendering them unable to compete in the modern transnational economy.

Labor unions are heavily involved in the employment impact of plant closings and new production equipment.[21] Unions generally have two major objectives: representing their current members and building future membership to ensure the continued existence of organized labor as an effective economic organization. Although new skills training may offer the best approach for the structurally unemployed, such training usually creates job opportunities outside the specific union's domain. It is difficult to imagine a union seeking to train its current members for jobs which that union does not represent.[22] Continuing members would surely question the use of their dues being spent to assist other members in obtaining jobs represented by competing unions or jobs without union representation.

Some unions, it must be noted, especially in the construction trades, have long established apprenticeship programs which are not designed as retraining programs for displaced workers. Apprenticeship programs are generally limited to applicants younger than the average displaced worker. Often such programs stipulate a maximum age of 25. Openings in apprenticeship programs are also limited by a negotiated journeyman-apprentice ratio. This ratio controls the labor supply by making the number of apprentices dependent on the number of journeymen for each employer.[23] Practically, apprenticeship training programs

[20] B. BLUESTONE & B. HARRISON, THE DEINDUSTRIALIZATION OF AMERICA 55-61, 115-18 (1982).

[21] *Id.* at 235-39.

[22] J.S. Solomon, Union Responses to Technological Change: Protecting the Past Versus Looking to the Future, paper presented at Southern Regional Industrial Relations Research Association. Academic Seminar (October 1985).

[23] S. LEVITAN, J. MANGUM, & R. MARSHALL, HUMAN RESOURCES AND LABOR MARKETS 211 (2nd ed. 1976). *See* Davis-Bacon Act, Ch. 411, 46 Stat. 1494 (1931).

are not a viable alternative for any significant number of displaced workers.

In short, the absence of incentives for unions to assume the responsibility for retraining their members for new careers through either special situation programs or existing apprenticeship programs, combined with the limited resources of unions, eliminates organized labor as a major factor in the solution of the structural unemployment problem.

If management and labor unions are unwilling to take responsibility for necessary retraining, why don't the individuals do it themselves? Often the answer is that they simply cannot, either emotionally or financially. The combination of risk aversion and limited access to capital makes workers reluctant to invest in gaining new skills during their careers. The dislocated worker is often a married male with children and a stable member of the community. His educational accomplishments frequently extend only to a high school degree. The typical dislocated worker has had few or no employment changes and often anticipates staying with the same employer for the remainder of his life.[24]

A tremendous emotional shock often occurs when employment is terminated. Psychological issues of separation from the company as well as self-esteem problems during unemployment are overwhelming. Statistics of increased alcoholism, drug abuse, wife and child abuse, and divorce and suicide rates attest to the problem.[25]

Assuming for the moment that the emotional trauma can be overcome, pressing financial needs are encountered. As head of a household, the dislocated worker (and his spouse) experience difficulty in providing for the basics of everyday existence: food, housing, and clothing.[26] Where medical and dental care are often shunned as too costly, it is difficult to imagine the displaced worker expending money to complete a high school equivalency program, which is often an entry requirement for jobs training programs plus six months or a year of technical training. Furthermore, many workers left school before graduation to work in high paying factory jobs precisely because they did not like the school environment. The fears of returning to a school atmosphere further complicate an individual's ability to seek new training. Most often the unemployed individual's emotional and financial needs compel him to seek the most immediate job available, often at a lower salary and with fewer benefits than previously enjoyed.[27]

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[24] *See supra* text at note 13; *see generally* CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 13.

[25] B. BLUESTONE & B. HARRISON, *supra* note 20, 63-66.

[26] *Id.* at 55-63.

[27] *Id.* at 55-61. The theory that middle-income jobs are being destroyed thereby threatening the very essence of middle-class society in the United States remains controversial. *See* Samuelson, *Demolishing a Myth,* Washington Post, June 26, 1985, at D1 col. 1. (distribution of earnings along occupations has remained stable) and Lawrence, *Stubborn Demographics: The Middle Class is Alive and Well,* New York Times, June 23, 1985, at F3 (problem is demographic). *See generally* Kuttner, *A Shrinking Middle Class Is a Call For Action,* BUS. WK, 16 (September 16, 1985).

The argument is advanced that rather than providing retraining; the displaced workers should relocate, usually to the Sunbelt.[28] However, the personal attributes of many displaced workers are linked to an unwillingness to relocate. This reluctance to relocate stems from a variety of reasons. First, because displaced workers are often older, they are involved in community and church activities and are unwilling to give them up. Additionally, they may have relatives living in the vicinity. Their spouses and children often have strong attachments to friends and the community. Their established community ties also stem from having family members who are employed locally and owning their own homes, which are particularly difficult to sell.[29]

Second, dislocated workers, who have little previous experience with unemployment, are extremely loyal. In layoff situations, they frequently exhibit long-term loyalty to their employers and wait to be recalled to their former jobs. Dubbed by some as "recall fantasy,"[30] the emotional inability to accept the reality of a layoff as permanent keeps former employees in stagnant communities.

Third, social welfare policies have rendered dislocated workers geographically immobile. The fragmented administration of welfare and unemployment insurance programs, imposing different benefits in every state,[31] discourages mobility. As one observer noted, "[m]any unemployed

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[28]PRESIDENT'S COMMISSION FOR A NATIONAL AGENDA FOR THE EIGHTIES, URBAN AMERICA IN THE EIGHTIES: PERSPECTIVES AND PROSPECTS (1980); Fallows, *America's Changing Economic Landscape*, 255 ATL. MONTHLY 47 (March, 1985).

[29]Flaim & Sehgal, *supra* note 13, 3, 8.

[30]Interview with Audrey Theis, Director Eastside Occupational Training Center; interviewed Essex, Maryland (March 14, 1984). The first stage of the Center's program confronts the promotions of stress, anger, and denial that the layoff is permanent.

The shut down in September 1977 of a major steel facility in Youngstown, Ohio and the layoff of approximately five thousand workers provided the context for researchers to assess the role of training and education in dealing with massive structural unemployment. Culture, tradition, and unique local characteristics were found to exert as profound an influence on a worker's decision to become involved in education and training as did economic need. Steel making was perceived as a way of life experienced by generations within the same families and was not discarded lightly. In Youngstown, the mill was virtually the "heart" of the town, making mass unemployment there qualitatively different from the sum of people without jobs. Local conditions — the active belief that the mill would reopen — provided a potent source of apathy on the part of the steelworkers with respect to relocation and retraining. Boggs & Buss, *Retraining and Educating Displaced Persons: The Youngstown Case*, 6 J. HEALTH AND HUM. RESOURCES Ad. 240 (1983).

[31]R. SCHULER, PERSONNEL AND HUMAN RESOURCE MANAGEMENT 313 (1981). The Unemployment Insurance System, administered by the federal government and the states, provides cash benefits to workers for limited periods of unemployment. The Unemployment Insurance System is run by the states according to federal guidelines and is financed by federal and state payroll taxes imposed on employers. The amount of benefits, as a percent of regular earnings, as well as the time period benefits may be received vary, often depending on the stability and size of each state's Unemployment Insurance Fund. CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 25-26.

Dislocated workers often do not have the personal financial resources to acquire the retraining skills that could lead not only to reemployment but also to a maintenance of their standard of living. Many states prohibit workers from enrolling in retraining programs while they are collecting unemployment insurance. This "catch-22" forces laid-off workers onto the horns of a dilemma: whether to make the difficult choice between minimal income support for their families today or to take the training necessary to insure that their families will have adequate income tomorrow. For many unemployed workers, this choice may be meaningless because the temporary income provided by unemployment insurance is crucial to meet family living ex-

Americans are reluctant to look for work in another part of the country for fear that they will lose the minimal assistance they have."[32]

In short, only a small percentage of all displaced workers will consider relocating as part of a reemployment strategy. A guidebook for employers on managing plant closings notes that only about 20 percent or less of the workers in most plants would consider relocating as part of a reemployment strategy.[33]

If management, unions, and the individuals lack the incentives and/or the resources to provide retraining, then the burden falls to the government, the one remaining entity. The structural component of unemployment has introduced a powerful variation of an old issue, the political agenda. Several questions exists. What is an acceptable level of unemployment, and to what extent is government responsible for assuring an acceptable level of employment for all Americans, particularly during a period of industrial restructuring? More precisely, is special assistance needed for displaced workers? If so, what form should such assistance take?

Some might argue that policy makers should rely solely on market forces to handle the economic change the United States political economy is undergoing, specifically the transition of dislocated workers to new jobs. A number of reasons exist to doubt the market itself. As developed in Part I of this article, many of the dislocated workers will not be reabsorbed into their old jobs or jobs in new industries. Many of the old jobs are gone forever. In addition, these workers are not interchangeable. Dislocated workers lack the skills, as well as the attitudes and values, needed for new jobs, particularly jobs created by the new technologies. It seems naive to believe that the retooling process will occur magically by the market mechanism. Fortunately, modern societies, despite their free market bent, have been unwilling to see large numbers of displaced workers thrown out of work and dependent on their own limited resources. Mass unemployment without public benefits or public sector employment creates a widespread impact on many communities and a dangerous level of political instability that policy makers regard as unacceptable.[34] The costs of unemployment have traditionally been absorbed by the government in welfare states. In other words, the public pays the cost of public benefits, subsidies, or employment in the form of taxes. To help the unemployed find jobs, the federal government has devised programs to promote knowledge of job opportunities and retraining.

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penses. An analysis of the Unemployment Insurance System and its possible reform is, however, beyond the scope of this article.

[32]R. REICH, THE NEXT AMERICAN FRONTIER 216 (1983).

[33]Flaim & Sehgal, *supra* note 13, 3, 8. (*citing* P. SWIGART, MANAGING PLANT CLOSINGS AND OCCUPATIONAL READJUSTMENTS: AN EMPLOYER'S GUIDEBOOK 49 (1984)).

[34]*See generally* K. POLYANI, THE GREAT TRANSFORMATION (1944).

B. *The Policy Rationale Implemented: Federal Government Programs*

The mere availability of jobs in other areas of the United States does not directly translate into reemployment. The dislocated workers, among others, must be made aware of the new job opportunities elsewhere. The limited availability of information on new jobs prevents labor markets from operating effectively.

To meet this gap in the market, the United States Employment Service, a nationwide network of federally funded but state operated labor exchanges, has existed since 1933.[35] The Service serves as a clearinghouse to match the skills of job seekers with the needs of prospective employers. However, the system has not operated as envisioned. Lack of funding and unofficial neglect, coupled with existing barriers to relocation, have resulted in a little over 21,000 job placements annually by various state offices during the past few years.[36] The nature of the applicants and the jobs listed by corporations with the Service have combined to limit this potentially effective tool to the unskilled, low wage labor market. Most of the country's employers never use the Employment Service. Furthermore, only a small fraction, less than one quarter, of the applicants are successful in obtaining a job through the Service.[37] Because a job search in a continentwide economy does not respect state and local boundaries, a need exists for continued public sector involvement in promoting an interstate job bank and interstate and interregional cooperation. This, of course, requires more public sector funds thereby heightening the federal budgetary deficit. In addition, creative mechanisms to gain the cooperation of private employment agencies must be sought.

Since the Depression, the federal government has attempted to develop employment opportunities by influencing not only the supply of jobs but also available workers' skills. Retraining has been perceived as more cost effective than permanent subsidizing the retirement of displaced workers. The first postwar federal employment and training effort, the Area Redevelopment Act (ARA) of 1961,[38] sought to attract new businesses to economically depressed areas and to provide a limited amount of training to provide the necessary skilled workforce from a disadvantaged pool.

In 1962, the Manpower Development and Training Act (MDTA)[39] replaced the training provisions of ARA, providing a broader range of training

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[35]Wagner-Peyser Act, Ch. 49, 48 Stat. 113 (1933); Guzda, *The U.S. Employment Service: It Too Had To Wait Its Turn,* 106 MONTHLY LAB. REV. 12 (1983). *See generally* S. LEVITAN, G. MANGUM & R. MARSHALL, *supra* note 23, 301-02.

[36]CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 23. *See also* S. LEVITAN, G. MANGUM, & R. MARSHALL, *supra* note 23, 303-04.

[37]CONGRESSIONAL BUDGET OFFICE, *supra* note 14, 23. *See also* D. BEACH, PERSONNEL: THE MANAGEMENT OF PEOPLE AT WORK 211 (4th ed. 1980).

[38]Pub. L. 87-27, May 1, 1961, 75 Stat. 47.

[39]Pub. L. 87-415, May 15, 1962, 76 Stat. 23.

services and allowances. Initially, MDTA training and other assistance programs were intended for experienced coal miners, steelworkers, and factory workers being replaced by automation. However, once underway, the need for those who had no skills or work experience became evident. Since then, separate training programs have existed for those with previously stable employment patterns (the "dislocated" workers) and those with no experience (the "disadvantaged" workers).

After 1964, the year in which President Johnson declared the "War on Poverty," the government undertook huge job training programs for the disadvantaged workers while skilled workers enjoyed low unemployment rates. In 1973, the Comprehensive Employment and Training Act (CETA)[40] was enacted to coordinate the proliferation of programs of the previous ten years. By the late 1970's, however, CETA's inability to serve the growing need of the displaced workers was evident.[41] The Trade Act of 1974,[42] specifically the Trade Adjustment Assistance (TAA) program, also provided assistance to workers displaced by foreign competition, such as those in the steel and auto industries.[43]

In 1982, CETA was replaced by the Job Training Partnership Act (JTPA),[44] currently the only federal program aimed specifically at dislocated workers. The JTPA is based on the concept of private sector involvement in planning and administering job training programs, which had been established in Title VII of CETA.[45] Private sector participation in job training programs through Private Industry Councils (PIC's) is a vital element of JTPA and is crucial to any effective program.[46] The experience of the Kennedy years, and more recently the 1980's, has shown that private industry will not train the displaced workers on their own. In addition, the late 1960's and 1970's demonstrated that the government cannot solve the problem alone. The JTPA attempts to join private and public sector efforts to achieve a more effective solution.

The participants under Title III of JTPA, the dislocated workers program, must belong to one of three categories of eligibility: (1) people who have been terminated or laid-off from their job or who have been notified of pending layoff, who are eligible to receive or have exhausted their unemployment benefits and are unlikely to return to their previous industry or occupation; (2) people

[40]Pub. L. 93-203, Dec. 28, 1973, 87 Stat. 839.

[41]Spar, *Job Training Partnership Act: Background and Description, Report No. 83-76 EPW*, CONG. RESEARCH SERV. 1-2, 9 (April 19, 1983).

[42]Pub. L. 93-618, Jan. 3, 1975, 88 Stat. 1978.

[43]Spar, *supra* note 41, at 5. *See also* EMPLOYMENT AND TRAINING ADMINISTRATION, A GUIDE FOR COMMUNITIES FACING MAJOR LAYOFFS OR PLANT SHUTDOWNS — A CHECKLIST FOR COMMUNITY LEADERS, at 26 (1980).

[44]Pub. L. 97-300, Oct. 13, 1982, 96 Stat. 1322. *See* Guttman, *Job Training Partnership Act: New Help For the Unemployed*, 106 MONTHLY LAB. REV. 3 (1983). The development of the Job Training Partnership Act is discussed in detail in K. Spar, *supra* note 41, at 1-2, 7-10.

[45]Spar, *supra* note 41, at 2, 4, 8.

[46]*Id.* at 8. *See also* F. PIERSON, THE MINIMUM LEVEL OF UNEMPLOYMENT AND PUBLIC POLICY 191 (1980).

who have lost or are about to lose their job because of a permanent plant or facility closing; or (3) the long-term unemployed who have limited opportunities in their industry or occupation in the region where they live, including older workers whose age creates a barrier to employment.[47]

Many states have amended these eligibility requirements to specify the exhaustion of unemployment benefits in the hope of limiting abuse of the program. However, more skills retraining could be accomplished if participation in the dislocated workers program could begin before an individual exhausts his unemployment benefits. The dislocated worker has typically not sought public solutions to his problems nor is he a likely abuser of the system, but rather is highly motivated to return to self-sufficiency. Allowing training of workers who will never return to their previous occupations to begin while still receiving unemployment compensation could provide increased occupational training instead of job search training, as is often the case.

While the JTPA emphasizes training for employment skills in short supply,[48] training in job search techniques has become more often the primary emphasis of the dislocated worker programs.[49] With unemployment benefits exhausted, the individual's financial needs overcome his desire for skills retraining. Thus, the dislocated worker programs offer resume writing, interview techniques, and job search strategies hoping for quick placement back into the work force with whatever skills and aptitudes the participants already possess. The job search training simply does not meet the needs of dislocated workers who, by definition, will not find easy reentry into their local work force. Placement into positions which provide on the job training satisfy both the public sector's obligation and the individual's financial and psychological needs for self-sufficiency. Therefore, these become the most sought after positions.[50]

The total funds allocated for JTPA programs have been constricted. Limited funding to meet the problem of dislocated workers means only a small part of the workers who require retraining receive this assistance. Specifically, $223 million was set aside in 1984 to aid dislocated workers as part of a $3.6 billion JTPA budget.[51]

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[47]Spar, *supra* note 41, at 22.

[48]Identification of state and local employment skills needs is coordinated by the State Job Training Coordinating Council in conjunction with the Private Industry Council. *Id.* at 13, 15-16.

[49]J.S. Solomon, Re-Employment for Dislocated Workers: The Jobs Training Partnership Act Experience in Maryland, unpublished paper, (1985).

[50]Interview with Beverly Miller, Director, Project Renew, Bradley Worker Assistance Center, Baltimore, Maryland (June 28, 1984).

[51]Hook, *A Prominent "New Idea,"* 42 CONG. Q. 781, 782 (1984).

Federal funds budgeted for JTPA programs for dislocated workers are guided by a formula which allocates 75 percent to the states based equally on: (1) the relative number of unemployed individuals; (2) the relative number of unemployed individuals in excess of 4.5 percent of the civilian labor force; and (3) the relative number of people unemployed 15 weeks or longer. K. Spar, *supra* note 41, at 22. The amount each

While skills training may be a luxury for the program participants, such training may also be a luxury for state agencies, which, because of financial restrictions, must spread limited funds over many people. Agencies are anxious to limit the amount spent on any one individual. Returning a dislocated worker to paid employment through counseling and job search training is quick and reduces the cost per worker placed, a primary performance measurement. Thus, the agencies emphasize reemployment over skills training, ignoring the long-term needs of displaced workers.

Since the dislocated worker program under JTPA currently serves less than 100,000 individuals,[52] there exists a need for more far reaching programs for dislocated workers. Devising public sector programs to assist dislocated workers which will neither block the economic transformation the United States is undergoing nor make individuals dependent on government for their livelihood[53] constitutes one of the most challenging policy issues for the balance of this century, particularly during an era of budgetary constraints.

III. TAX POLICY OPTIONS

Recently, policymakers have begun to investigate methods by which workers might be able to help facilitate their retraining, rather than relying on direct governmental expenditures, in the event that they become displaced workers. This section considers two tax policy options involving the Individual Retirement Arrangement model. Both options would attempt to provide retraining funds for dislocated workers based on the concepts of individual choice and limited government involvement. In particular, one mechanism would provide for the establishment of new accounts similar to individual retirement arrangements but with the goal of creating an individually controlled fund to meet possible retraining needs. The other proposal, a revision of current Internal Revenue Code provisions pertaining to individual retirement arrangements, would provide for penalty-free withdrawals from existing and future individual retirement arrangements to fund retraining or relocation. In order to better understand these proposed financing techniques, it is necessary to review the current individual retirement arrangement provisions in the Internal Revenue Code and the Treasury Regulations.

A. *Individual Retirement Arrangements*

Individual retirement arrangements offer two major tax benefits. First, an individual can deduct his contributions. The deduction enables an individual to

state receives is, in turn, spent at the discretion of the governor of the state, within federal guidelines. *Id.* at 15. The remaining 25 percent of federal funds belong to a discretionary pool for the Secretary of Labor to award on a competitive basis for special situations such as mass layoffs, natural disasters, and federal government facility relocations having major impact on regional unemployment. *Id.* at 21-22.

[52]Hook, *supra* note 51, at 781-82.

[53]*See generally* C. MURRAY, LOSING GROUND: AMERICAN SOCIAL POLICY 1950-1980 (1984); G. GILDER, WEALTH AND POVERTY ch. 6, 10, 11 (1981).

build his retirement investment with pre-tax dollars. Second, earnings on the contributions to an individual retirement arrangement accumulate tax-free until distributed.

Anyone who has compensation income may participate in an individual retirement arrangement. In brief, compensation income is defined as wages, salaries or professional fees, and other amounts received for personal services rendered, including commissions paid sales personnel, commissions on insurance premiums, tips, and bonuses.[54]

There are two types of individual retirement arrangements: individual retirement accounts and individual retirement annuities. An individual retirement account (IRA) takes the form of a trust[55] or custodial account.[56] To constitute an IRA, the trust or custodial account: (1) must be created or organized in the United States and maintained at all times as a domestic trust or custodial arrangement;[57] (2) must be for the exclusive benefit of an individual taxpayer or his beneficiaries;[58] (3) must have a trustee or custodian of which must be a bank or similarly qualified person or institution;[59] and (4) must use a written trust or custodial agreement.[60]

The annual contribution to an individual retirement arrangement is deductible to the extent of the lesser of $2,000 or 100 percent of the compensation includible in the taxpayer's gross income for the year.[61] The contribution amount is deducted from the taxpayer's gross income in computing his or her adjusted gross income.[62] Thus, even a taxpayer who does not itemize his or her nonbusiness deductions may deduct amounts he or she contributes to an individual retirement arrangement. However, no deduction is allowed once the owner attains age 70-1/2.[63]

Income earned on contributions to an individual retirement arrangement

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[54]Treas. Reg. § 1.219-1(c)(1).

[55]I.R.C. § 408(a). Employers, unions, and other employee benefit associations may establish individual retirement accounts for the exclusive benefit of their employees or members and their beneficiaries. I.R.C. § 408(c).

[56]I.R.C. § 408(h).

[57]I.R.C. §§ 408(a) and 7701(a)(9); Treas. Reg. § 1.408-2(b).

[58]I.R.C. § 408(a).

[59]I.R.C. § 408(a)(2), (h), and (n). A nonbank entity wishing to be an IRA trustee must apply to the Service and demonstrate its eligibility to be an IRA trustee or custodian. An individual trustee or custodian will not qualify. Treas. Reg. § 1.408-2(b)(2).

[60]I.R.C. § 408(a).

[61]I.R.C. § 219(b)(1). The term "compensation income" is defined in Treas. Reg. § 1.219-1(c)(1). An employed spouse may set up an individual retirement arrangement for his or her nonworking spouse who receives no compensation income for the taxable year. A maximum of $2,250 per year may be contributed by a married couple to an individual retirement arrangement for the working and nonworking spouse. I.R.C. § 219(c)(2). A joint return must be filed to obtain the deduction for a contribution to a spousal individual retirement arrangement. I.R.C. § 219(c)(1)(A).

[62]I.R.C. § 219(a).

[63]I.R.C. § 219(d)(1).

accumulates tax-free until distributed.[64] Substantially greater amounts accumulate than if the earnings were currently taxable. The larger amounts accumulated significantly increase the effective rate of return on an investment in the individual retirement arrangement. Distributions from an individual retirement arrangement to an owner are taxable as ordinary income when received.

An owner of an IRA cannot borrow money from his account. If he or she does so, it ceases to be an IRA as of the first day of the taxable year in which the loan was made.[65] Disqualification triggers a constructive distribution to the owner in an amount equal to the fair market value of all assets in the account as of the first day of the tax year.[66] This amount is taxed to the owner as ordinary income. In addition, a ten percent premature withdrawal penalty tax is imposed on a constructive distribution if the owner is not disabled or has not attained age 59-1/2 on the first day of the tax year.[67]

Likewise, if an owner pledges all or a portion of his or her IRA as security for a loan, the portion so used results in a constructive distribution to the owner.[68] The amount of the distribution is taxed to the owner as ordinary income, and he or she is subject to the ten percent tax on premature withdrawals.[69]

B. *Proposed National Individual Training Account Act*

One mechanism for financing worker retraining is the Individual Training Account (ITA). Modeled after individual retirement arrangements, the ITA would offer incentives to save for retraining by making contributions to an ITA fund tax deductible. The ITA's and individual retirement arrangements are similar in several respects. Both are designed to mitigate financial problems. The individual retirement arrangement is intended to provide a greater degree of financial security on retirement. The ITA is designed to provide a means by which an individual finances his training when laid-off. Both serve as income substitutes. Furthermore, as designed, both are portable, moving with an employee from one employer to another employer.

An ITA would constitute a savings based system analogous to the individual retirement arrangement but with provisions that apply specifically to displaced worker retraining and relocation. Generally, the ITA would work as follows:[70]

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[64] I.R.C. § 408(e)(1).

[65] I.R.C. § 408(e)(2)(A).

[66] I.R.C. § 408(e)(2)(B).

[67] I.R.C. § 408(f).

[68] I.R.C. § 408(e)(4).

[69] I.R.C. § 408(f).

[70] This discussion describes the ITA as envisioned by Pat Choate, senior economic analyst for TRW, Inc. in P. CHOATE, RETOOLING THE AMERICAN WORKFORCE: TOWARD A NATIONAL TRAINING STRATEGY 42-45 (1982). *See* National Individual Training Account Act of 1985, sponsored by Rep. Richard J. Durbin (D. Ill),

(1) A personal training fund would be established for each worker, financed through 50-50 matching contributions made by the worker and his or her employer. Both the employee and the employer would have to participate in order to take advantage of the ITA mechanism. Employer participation would be encouraged by requiring nonparticipating employers, except for those with less than 25 employees, to continue to pay the .02 percent surtax on federal unemployment taxes, due to expire in 1986.[71]

(2) Employee contributions would be 100 percent deductible by the employee. Employer contributions would be 125 percent deductible by the employer.[72]

(3) The total collected from each worker and each employer for that specific employee's account would be $2,000 each, producing a $4,000 ITA fund for each individual. The employee and the employer would each contribute the lesser of .8 percent of the employee's salary or $250 annually.[73] Once the $4,000 fund was collected, employee and employer contributions would cease, but interest would continue to accrue on the amounts contributed.[74] Part of each contribution would go for insurance coverage enabling participating workers to draw on their ITA's before paying the full $2,000.[75]

(4) The funds would be administered by the United States Treasury, and such administration would be financed by a small fee on contributions, perhaps 1/4 percent of any contribution to an ITA, not by federal appropriations.[76] The Treasury would invest the funds in United States government securities and the interest earned would be credited to each account.

(5) The funds in the account would be available to an employee-participant who has been laid-off or whose employer certifies that he will be laid-off within six months.[77] If a worker was displaced from his job, both worker and employer contributions could be drawn upon for approved job training. The funds would be available in the form of a voucher to pay for training expenses at a federally certified training

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introduced on January 3, 1985 and S. 934, National Individual Training Account Act of 1985, sponsored by Sen. Gary Hart (D. Colo.), introduced on April 17, 1985. *See also* G. HART, A NEW DEMOCRACY 102-103 (1983); Mathews, *Tax Aid for Obsolete Workers, One of Hart's "New Ideas," is Catching on,* Wash. Post, May 20, 1984 at A3, col. 1; NORTHEAST/MIDWEST COALITION, INDIVIDUAL TRAINING ACCOUNT (1984).

[71] I.R.C. § 3301; H.R. 26, S. 934, 99th Cong., 1st Sess. § 204 (1985).

[72] H.R. 26, S. 934, 99th Cong., 1st Sess. § 203 (1985).

[73] *Id.* at § 202.

[74] *Id.* at § 203.

[75] *Id.* at § 106(a). The insurance would be purchased through an annual assessment of $25 per account, $12.50 each from the employer and the employee. The $25 would come out of the funds contributed each year by both the employee and the employer and would not constitute a special, additional assessment.

[76] *Id.* The ITA would be set up as a separate trust fund in the Unemployment Insurance System.

[77] *Id.* at § 103(a)(1) and (3).

program.[78] The choice of training and provider would be left to the worker, but the federal government would certify training establishments.

In addition, funds in an account could be used for relocation expenses, including moving and other reasonable costs, up to a maximum of $1,000.[79] Again, the funds would be available in the form of a voucher to pay relocation expenses. Eligible individuals could use funds immediately for approved relocation assistance for moves within their home state. Individuals wishing to relocate outside their home state must have looked for work for at least 13 weeks and be certified by the state Employment Service that no jobs were available within the state in their occupational field.[80]

(6) Distributions used to pay approved training or relocation expenses would have no federal income tax consequences for the employee.[81]

(7) On reemployment, the employee and his new employer would begin the process of contributing until the $4,000 limit is reached.

(8) If the worker voluntarily left his employment (or involuntarily ceased to be employed through his or her fault), the employer's contributions would be refunded.[82]

(9) At retirement, the worker would be entitled to withdraw the funds he contributed plus the accumulated interest on his contributions.[83] If the worker died before retirement or before withdrawing the contributions and accumulated interest, the funds the worker contributed plus the accumulated interest on his contributions would go to his estate.[84] When the worker retired or died, the firm would receive a refund of its contributions plus its share of the accumulated interest on its contributions.[85]

(10) Distributions at retirement or on the death of the employee would be taxable in the tax year received to the extent such amounts represent a return of the employee's deductible contributions, including interest accrued and attributable to such contribution.[86]

The ITA, a simplified, self-financing, displaced worker voucher system, offers many advantages as well as being subject to significant disadvantages.

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[78] *Id.* at §§ 103(a)(2) and 104. Training expenses means: (1) tuition and fees required for enrollment in an eligible training program (as certified by the Secretary of Labor) and (2) books, supplies, and equipment required for enrollment in such program and supplied through such program. *Id.* at § 203.

[79] *Id.* at §§ 103(a)(2)(B) and (5), 105(b), and 203.

[80] *Id.* at § 105.

[81] *Id.* at § 203.

[82] *Id.* at § 103(b)(1).

[83] *Id.* at § 103(b)(2) and (5).

[84] *Id.*

[85] *Id.*

[86] *Id.* at § 203.

The ITA proposal is analyzed from the viewpoint of workers, employers, and the government.

The ITA accords employees a number of benefits. The ITA provides flexibility to a dislocated worker in the choice of training (and location) and encourages the wise use of funds for retraining and relocation assistance. Because the worker has contributed funds directly to the ITA, distributions from the ITA probably would be used more prudently than would funds allocated generally out of the tax revenues. In the later situation, the dislocated worker has little direct interest in such expenditures. With the ITA, the worker would control the expenditure of funds.[87] The certification process, similar to that in effect under the GI bill,[88] would provide greater assurance of quality training because the federal government would strive to maintain overall standards.[89]

In order to assist laid-off workers in identifying emerging jobs that will be available to them, the ITA program would require that workers receive job counseling at state employment offices before choosing a retraining program or relocating.[90] This requirement would assist the workers in choosing the proper type of retraining. Though counseling would not guarantee jobs for

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[87]However, one study indicates that unemployed workers given training vouchers in Denver and Seattle chose courses that failed to increase their earnings over a six year period. G. BURTLESS & R. HAVEMAN, POLICY LESSONS FROM THREE LABOR MARKET EXPERIMENTS 106-13 (1985) (at 113; "When given the resources and freedom to choose their own training strategy, low-income breadwinners appear to be no better at selecting a winning strategy than are the administrators and training specialists who now run training and employment programs"). *See generally* L. SHARPE, G. BURTLESS, A. RICHARDSON, & L. RINDLER, VOUCHERING MANPOWER SERVICES: PAST EXPERIENCES AND THEIR IMPLICATIONS FOR FUTURE PROGRAMS (1982).

[88]38 U.S.C. § 1775 (1982). Training and education benefits have been available to veterans of military service since the end of World War II. Benefits under the GI Bill cover classroom training (college and vocational education), on-the-job training, correspondence instruction, and certain types of farm and flight training. The training must have vocational objectives. Benefits are paid directly to the veteran to be allocated to his training and living costs. The vendors of training must be approved by the Veterans Administration. Nondegree granting institutions must have operated for two years before being eligible to apply for approval. L. SHARPE, G. BURTLESS, A. RICHARDSON, & L. RINDLER, *supra* note 87, at 51-54.

One study of the utilization of the GI Bill by Vietnam veterans indicates, through earnings comparisons, consistent advantages for veterans who obtained training. For example, the post-program annual earnings of veterans who attended vocational training schools, on a full-time, continuous basis, were about 10 percent higher than those of nonusers. However, the training participants may have been favored by differences in physical and mental health as well as motivation, family, and parental status. *Id.* at 57-60, 98-99 (*citing* study by D. O'NEILL & S. ROSS, VOUCHER FUNDING AND TRAINING: A STUDY OF THE GI BILL (1976). *See also* O'Neill, *Voucher Funding of Training Programs: Evidence from the GI Bill*, 12 J. HUM. RESOURCES 425 (1977).

[89]Certification of a training program would require a determination by the Labor Department that:

(1) the quality of the program is "adequate and reasonable" for the trade or occupation for which training is provided;
(2) a program "in low-wage industries where prior skill is typically not a prerequisite and labor turnover is high" is ineligible for approval;
(3) the trade or occupation for which training is provided is likely to lead to employment opportunities for the program participant;
(4) the facilities and equipment are suitable for the program, and the instructors are qualified to provide training in such trade or occupation; and
(5) the program meets other requirements as established by the Secretary of Labor.

Supra note 72, at § 104(b) and (d). Additional factors considered before making a certification are set forth in the proposal to be contained in regulations promulgated by the Secretary of Labor. *Id.* at § 104(c).

[90]*Id.* at § 202(a).

displaced workers, it would permit them to make more informed choices.

Similar to the current individual retirement arrangement mechanism, workers would take a tax deduction for their annual contributions. Taxes on funds within the ITA would be deferred, and these funds would earn interest. However, one major tax advantage of the ITA proposal is that funds withdrawn, including interest earned on an employee's account, which are used to pay for retraining or relocation expenses would not be taxable.

The funds in an ITA constitute a nest egg which, if unused, can supplement the worker's retirement savings or his or her estate. For participants who do not draw from the ITA account during their working lives, the refund could be substantial.[91]

The analytic picture becomes far more mixed when employers and the public are considered. ITAs impose a limited financial burden on an employer, namely, a total contribution of $2,000 per worker. A serious drawback of the ITA, particularly if it is structured as a mandatory system for all employers, is that it would increase the cost of hiring labor for several years after its introduction and may, therefore, cut the profits of corporations which can least afford any additional financial burdens and inhibit the growth of employment.[92] ITA's may not constitute an impediment for "large" corporations but may discourage smaller firms from hiring additional workers. This consequence of the ITA may point to the advisability of allowing withdrawals, without penalty, from individual retirement accounts, which is discussed later in this article. However, a voluntary ITA approach, in which the employer may concur in the initial decision to set up an ITA, may minimize any adverse employment effect on one hand but limit the availability of ITA's on the other hand.

Because of the matching contribution mechanism, the employer has an incentive to participate in the ITA program. The employer's incentive is in the form of avoiding loss of its contributions by continuing to employ a worker or finding him another job in the firm. In short, participating corporations would have an incentive to retrain workers rather than laying them off.

From the government's perspective, the ITA offers four major advantages; namely, administrative ease, low cost, a source of funds, and promotion of a more rational tax system. The ITA suffers from two disadvantages: the biggest incentive to save goes to the wrong people and the low rate of return given the age of displaced workers.

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[91]One estimate places the size of the retirement nest egg for an employee who never uses his or her ITA at over $35,000. Fact Sheet on H.R. 26, The Individual Training Account Act, Attached to Letter To Colleagues, Richard J. Durbin (D.-Ill.) and Sherwood L. Boehlert (R-N.Y.), February 10, 1985.

[92]K. McLENNAN, OUTLINE OF REMARKS, POLICY OPTIONS TO FACILITATE THE REEMPLOYMENT OF DISPLACED WORKERS 6 (Washington, D.C., October 18-19, 1983). Kenneth McLennan, Vice President and Director of Industrial Studies, Committee for Economic Development, in a telephone conversation on June 4, 1985, noted; "European countries have run into that [extra cost of hiring labor imposed by governmental policies]. It makes people cautious about hiring people."

Looking at the advantages accruing to the government, first, the ITA is easy to administer. The ITA system, for example, would have clear eligibility criteria. Only participating workers who lost their jobs involuntarily and who were eligible for unemployment insurance could use their ITA funds for retraining and relocation expenses.[93] Furthermore, no new government bureaucracy would be required. The government would not direct public funds to vocational schools or other institutions. The program, particularly the certification of training programs, would be administered by the Secretary of Labor, who would be responsible for establishing regulations and for oversight of ITA's. Local employment service officers, acting as agents of the Secretary of Labor, would run the program on a day-to-day basis.

Second, as noted, the program would be financed by contributions from employers and employees up to a specified annual amount. The only cost to the government is the loss of tax revenues for the tax deductions allowed employers and employees on annual contributions.[94]

Third, the ITA proposal would provide a source of funds for the federal government. Because the ITA funds would be held by the United States Treasury Department, the unused funds could be borrowed by the federal government, as are all funds held by the Treasury. It is impossible to estimate precisely the number of dollars available for government borrowing because the program would be voluntary and there is no way to determine how many participants would need to draw on their accounts in the future. The best estimates indicate that for every million participating workers, 240 million dollars would be available for governmental borrowing.[95]

Finally, the tax incentives provided by the ITA system would comprise a rational part of the tax system. The Code's current incentives reward investment in future productivity through capital spending. ITA's would reward employers and workers by making annual contributions deductible from their respective taxable incomes for investing in the future through improved worker productivity. When unemployed, participating workers could gain new skills which would enable them to add to national productivity.

However, the biggest tax incentive goes to the wrong people. Although the ITA proposal is targeted to displaced workers in anticipation of being laid off, there is a high likelihood that it will be used as a tax avoidance scheme because it raises the amount of income people can shelter from federal income taxes. The tax benefits for those in the lower income tax brackets, within

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[93] *Supra* note 72, at §§ 103(a)(1) and 202.

[94] Estimates place the revenue loss to the United States Treasury at $72.5 million in the first year. *Mathews, supra* note 70 (*quoting* LINDA SPENCER, NORTHEAST/MIDWEST COALITION).

[95] Telephone conversation with Linda Spencer, Northeast/Midwest Institute, August 26, 1985. The $240 million estimate is based on one million participants times $120 from each participating employee and employer.

which group the displaced worker is often found, are not significant because they would save little, if any, federal income taxes. Therefore, the ITA utilization rate would be inversely proportional to the people it is most meant to help. Only those who have something to set aside would take advantage of the ITA mechanism. Those workers most in need more than likely could not afford to invest or save for retraining.[96] Furthermore, the savings incentives do not focus on the needs of many displaced workers who lack the basic education skills requisite to taking advantage of retraining courses.

In addition, a low rate of return may be generated from this type of investment in human capital because of the age of the displaced workers. Despite the need for retraining, the role educational institutions can play in assisting displaced workers is limited by the likely characteristics of the displaced workers, particularly the blue-collar, less-skilled workers who are less apt to take advantage of adult education opportunities.[97] Because the displaced workers are likely to be overrepresented in middle age groups, the rate of return from this type of investment in human capital will be quite low and perhaps negative for many displaced workers.[98]

C. *Proposed National Training Incentives Act*

One variation on the individual retirement arrangement theme, the proposed National Training Incentives Act,[99] would allow individuals seeking retraining to withdraw from their existing individual retirement arrangement without penalty. The proposed National Training Incentives Act provides that an individual may take funds out of his or her individual retirement arrangement without the imposition of the usual 10 percent penalty for premature withdrawals.[100] He or she must be a displaced worker, as defined,[101] and the funds must be used for training expenses, as defined.[102] Withdrawals would be

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[96]Hook, *supra* note 51, at 781-82. Telephone conversation with Gary Burtless, Brookings Institute, June 4, 1985.

[97]Hook, *supra* note 51, at 781-82.

[98]K. MCLENNAN, *supra* note 92, at 4-5.

[99]H.R. 1219, 99th Cong., 1st Sess. (1985); The National Training Incentives Act, introduced by Rep. Nancy Johnson (R. Conn.) on February 21, 1985.

[100]*Id.* at § 102 amending I.R.C. § 408(f).

[101]To constitute a displaced worker, an individual must: 1) have at least 20 quarters of Social Security coverage; 2) have received counselling relating to seeking employment from a state public employment office; 3) (a) be receiving (or eligible to receive) unemployment compensation or have exhausted his right to receive "regular" unemployment compensation, or (b) be unemployed (or have received a notice of termination of employment within 6 months) as a result of his employer closing the plant or facility where the individual is or was employed, or (c) be unemployed for at least six months and have limited opportunity for employment in the same or similar trade or occupation within a reasonable commuting distance from his principal residence. *Supra* note 99, at § 103(b)(1).

[102]Training expenses constitute: (1) tuition or fees for enrollment or attendance at an eligible training program, as certified by the Secretary of Labor and (2) books, supplies, or equipment directly related to such training program. H.R. 1219, at § 103(b)(2).

limited to a maximum of $4,000 over any five-year period.[103] However, the amounts withdrawn would be taxed as ordinary income.

In addition, the bill also provides a 25 percent employer tax credit for employer-provided qualified training expenses, as defined, over each employer's average level of training expenses during the previous five years.[104] Accordingly, the credit would permit a business to deduct from its tax liability, 25 percent of its training costs above its average training costs for the previous five years.[105]

The withdrawal without penalty and tax credit provisions would constitute two parts of an overall employment and retraining strategy with other programs, such as the Job Partnership Training Act, serving the most disadvantaged unemployed workers.

Finally, the bill calls for the Secretary of Labor to conduct a study to examine the feasibility of a nationwide computerized job bank and the effectiveness of the United States Employment Service.[106]

The proposed National Training Incentive Act offers advantages and disadvantages for workers, employers, and government. From the viewpoint of employees, the individual retirement arrangement aspect of the proposal would reach millions of households, thereby shortening the period of dislocation and encouraging people to withdraw funds for retraining. For example, Internal Revenue Service statistics indicate that 13.7 million workers contributed to individual retirement arrangements in 1983.[107] Despite the magnitude of these figures indicating the breadth of ownership of individual retirement arrangements, the proposal would not help the millions of workers who do not have such arrangements nor those who have individual retirement arrangements but are unable to make substantial contributions. The ownership of IRA's is skewed by the distribution of family income. While 66 percent and 50 percent, respectively, of the families with annual incomes of $50,000 or more and between $40,000 to $49,990 have opened IRA's, only 25 percent and 8 percent, respectively, of the families with annual incomes of $15,000 to $29,999 and less than $15,000 have done so.[108]

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[103] *Supra* note 99, at § 103(b)(3).

[104] *Supra* note 99, at §§ 101(a) and (c). The term "qualified training expenses" refers to expenses paid or incurred by the taxpayer in connection with training its employees under "approved training programs," as defined in H.R. 1219, § 101(b)(1). The term "approved training programs" is defined in H.R. 1219, § 101(b)(2).

[105] The credit is modeled after the 25 percent research and development tax credit for research expenditures made after June 30, 1981 and before 1986. A taxpayer is entitled to a tax credit for certain research and experimentation expenditures paid or incurred in connection with "carrying on" a trade or business. To be eligible for the research expense credit, the research must be performed in a field of laboratory science, engineering, or technology. The credit equals 25 percent of the qualified research or experimentation expenses paid or incurred, to the extent such expenditures exceed the average yearly amount of such expenses over a base period of the preceding three tax years. I.R.C. § 44 F.

[106] *Supra* note 99, at § 302.

[107] R. VICKER, THE DOW JONES-IRWIN GUIDE TO RETIREMENT PLANNING 99 (1985).

[108] Wall St. J., July 30, 1985, at 33, col. 2.

A question exists as to the type of retraining provided and whether outside (nonemployer provided) training is the answer of the quandry of displaced workers. The aspect of the proposal dealing with the withdrawal without penalty of funds in individual retirement arrangements leaves the decisions regarding the type and quality of the training to those who have the most direct stake in the processes, the individual workers. Because these provisions involve the expenditure of employee funds, the employee who seeks retraining has a personal stake in the selection and quality of the retraining. In short, the training should be "useful," or at the least, the thousands of individual decisions should result in training as useful as could be devised by government bureaucrats.

To critics who assert that those who are faced with structural unemployment neither adapt to retraining nor have the flexibility or resources to undertake retraining on their own,[109] the on-the-job training provided for by the tax credit mechanism has many advantages. Workplace training is a powerful lever for resolving some of the economic and human problems dislocated workers face. Available data suggests that adult Americans would prefer that their training be provided through the workplace.[110] While workplace training only addresses the problems of the employed, such training may prevent future dislocation. Moreover, the workplace may be the most appropriate situs for retraining. It is in the workplace where subtle shifts in products, prices and new technologies are translated into new skill requirements. Workplace training also overcomes the fear and dislike evidenced by many adults of the more formal educational endeavors.

What must be kept in mind is that training does not create jobs. For those workers who do not have individual retirement arrangements upon which to draw, the proposed act would provide employers with a tax credit for sponsoring training at levels greater than the average amount of money expended over the prior five years. Employer financed retraining would, however, only reach workers who have jobs and who are functioning effectively and, therefore, those with respect to whom an employer would expend funds to train (or retrain).

Another advantage of the proposed National Training Incentive Act, in contrast to the proposed National Individual Training Act previously con-

[109]The kinds of workers being laid-off, in general, are not the "perfect candidates" for retraining. "The blue-collar, less-skilled workers who have the biggest reemployment problems are those who take the least advantage of adult educational opportunities." Hook, *supra* note 51, at 781-82 (*quoting* M. BENDICK, JR., THE URBAN INSTITUTE). Furthermore, critics of governmental efforts in this field have argued that training may be useless. One statistical analysis of occupational structure, for example, suggests that the majority of existing jobs are undemanding and routine. Extrapolation from existing trends suggested that these jobs will not soon disappear. The demand for better training, at least in its present formulation, is pointless because the better educated displaced worker may enjoy no advantage over other workers with lesser scholastic and training backgrounds in securing employment. B. TIPTON, THE QUALITY OF TRAINING AND THE DESIGN OF WORK (1983).

[110]A. CARNEVALE, WORKPLACE TRAINING 1 (1985).

sidered, is that a worker's participation in an individual retirement arrangement is not tied to his or her employer's participation. An employee can establish an individual retirement arrangement on his or her own initiative. He or she is not dependent on the willingness of his or her employer to participate in the program.

From the vantage point of employers, the individual retirement arrangement aspects of the proposal minimize their payroll burden. Furthermore, allowing displaced workers to use funds in their individual retirement arrangements, without the imposition of any federal income tax penalty, for retraining is only a part of an overall approach. Although the proposal will not reach all dislocated workers, the tax credit is a mechanism for leveraging a substantial amount of retraining funds. This approach would generate four dollars in private sector outlays for every dollar in lost federal revenues.

Finally, the proposal must be examined from the standpoint of the federal government. The proposal provides two approaches for financing training, neither of which would require direct federal outlays. The first approach, the individual retirement arrangement provisions, allowing workers to withdraw money from such arrangements for their own retraining, would build upon an existing private retirement system. The second approach, the 25 percent training tax credit, would leverage four dollars in private sector training expenditures for every dollar in lost taxes.

Either of these two approaches constitutes an indirect subsidy[111] and would result in a loss of tax revenues. The impact of the proposal on governmental revenues must be assessed. The Joint Committee on Taxation estimates that the revenue loss would average about $600 million a year through 1990.[112] That amount would leverage in excess of 2 billion dollars in private sector spending per year because of the tax credit mechanism. The lost revenues would be recaptured, in part, through increased worker productivity and earning power, which would generate more federal revenue. The Committee admits its estimate does not take into account taxes from increased

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[111] For a detailed discussion of the concept of the use of Code provisions as tax expenditures and indirect subsidies, *see* S. SURREY, PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES (1973). *See also* Davenport, *Tax Expenditure Analysis as a Tool for Policymakers,* 11 TAX NOTES 1051 (1980). A critique of the tax expenditure concept is found in Bittker, *Accounting for Federal "Tax Subsidies" in the National Budget,* 22 NAT'L TAX J. 244 (1969).

[112] Telephone interview with Steve Hoffman, House Wednesday Group (August 26, 1985). According to a letter from David H. Brockway of the Joint Committee on Taxation to Rep. Nancy L. Johnson (R. Conn), dated February 19, 1985, in response to her request for a revenue estimate for her proposal to (1) suspend interest penalties on withdrawals from IRA's by qualifying unemployed individuals and (2) establish a 25 percent tax credit for investments in any skills training expenses in excess of the average skills training expenses incurred by the employer over the preceding three-year (not five-year) period, and assuming an effective date of January 1, 1985, the Joint Committee on Taxation estimated the following effect on the federal budget receipts:

FISCAL YEAR:

1985	1986	1987	1988	1989	1990
(BILLIONS OF DOLLARS)					
-0.1	-0.7	-0.9	-0.8	-0.5	-0.4

employment.[113]

The Code reflects a strong commitment to capital investment. Federal income tax incentives overwhelmingly favor capital and technology investments over worker training as a route to productivity growth. Present tax incentives for business investment (nearly $50 billion) are more than 70 times greater than the value of tax incentives for worker training (about $600 million).[114] The tax credit for worker training expenses would encourage investment in employees in the same way that tax credits are used to promote investment in research and plant and equipment. Furthermore, with respect to the individual retirement arrangements, funds placed in such an arrangement are intended as an investment, albeit for the owner's retirement. It seems only logical to permit workers to use individual retirement arrangement funds for retraining which also constitutes a long-term investment in human capital.

A question remains as to the necessity of providing an additional incentive for employers to retrain employees. Put simply, since an employer can already take a deduction for retraining, why is this legislation necessary? If an employer wants to train employees, it is permitted to write off the full cost of training.[115]

The tax credit provided in the proposal differs substantially from the business expense deduction, which fails to differentiate one type of business expense from another. Moreover, the tax credit will not merely reward employers for current levels of retraining, but will only reward for retraining over and above a five-year average. Also, it is better to reward employers through a credit than a deduction because a credit reduces an employer's tax liability dollar for dollar, rather than just by a percent of the employer's tax bracket. A deduction is more valuable only to employers in a high tax bracket.

CONCLUSION

The flexibility of firms to change rapidly in an environment of industrial and technological change and increased foreign competition depends on the ability of workers to adapt quickly to new technical and skill requirements. The two tax incentive proposals considered in this article provide a mechanism to facilitate worker adaption coupled with limited governmental involvement and reliance on private initiative.

These tax oriented proposals suffer from a common, and perhaps fatal, defect. Middle and low income workers would have little or no use for the tax deduction. In the face of pressing immediate financial obligations, such in-

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[113]Telephone interview with Steve Hoffman, House Wednesday Group, August 26, 1985.

[114]Statement by Rep. Nancy L. Johnson (R. Conn.) National Training Incentives Act of 1984 (March 15, 1984) (1982 figures), BNA DAILY LAB. REP. E-2 (March 16, 1984).

[115]I.R.C. § 162.

dividuals may be unwilling or unable to put aside a small amount of money for future retraining. In addition to the financial barriers, adults, particularly the typical dislocated worker, fear and dislike schools.

Furthermore, are workers sufficiently future oriented? Do workers think they will be unemployed, and will they need up to date skills and training in the future? Will the average worker feel secure with a high school diploma and a job at a local plant? Use of tax incentives to fund a retraining program based on individual choice and limited government involvement turns on a level of foresightedness many employees lack. Hopefully, this article will stimulate academics and policy makers to strive to devise creative governmental mechanisms to assist dislocated workers. In developing and implementing successful employment strategies, policy makers must keep in mind that the success of any retraining program depends on the availability of jobs and the general health of the American and the transnational economy.